

Market review

Economic overview

UK Buy-to-Let gross advances

£35.8bn



Source: UK Finance

UK house price inflation

5.2%



Source: ONS, Survey of mortgage lenders

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The housing market

The housing market in 2017 continued to reflect the uncertainties that emerged in 2016 after the UK's vote to leave the EU. Transaction volumes remained at much the same levels as they have since 2014¹, reflecting ongoing challenges posed by affordability driven by low wage growth and higher house price inflation ('HPI')². 2017 has seen HPI fall back, particularly in London, and it is possible that we may see a return to a moderate level of growth in transactions.

In February 2017, the government issued a long-awaited housing white paper. This reflected a shift in sentiment towards a more holistic approach to property tenure and away from an explicit focus on demand side initiatives that promoted home ownership. The political instability that followed the General Election has, however, left most of the proposed measures untouched. With the housing market remaining in the national spotlight, it is likely that the agenda set out in that white paper will re-emerge.

The mortgage market

According to UK Finance, gross mortgage lending reached £257bn in 2017³, ahead of the expected figure of £248bn and 4.4% up on 2016, driven largely by an increase in remortgage activity. The larger house purchase market rose by 9% to £139bn.⁴

First time buyers continued to take advantage of Help to Buy, with overall first time buyer lending up by 11% to £59.2bn (2016: £53.5bn).⁵ The effect of the Stamp Duty Land Tax ('SDLT') change for first time buyers that was announced in the Budget came too late to have any influence on the market in 2017; however, our view is that any impact will be minimal.

OneSavings Bank's lending markets:

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UK Buy-to-Let/specialist SME market

The Private Rented Sector ('PRS') accounts for approximately 5.5 million households.⁶ In the year to December 2017, it grew by 2.2%, a figure less than a third of that for the same period in 2014 and less than half of what it was in 2016.

This was, of course, a reaction to a series of regulatory and political interventions aimed at cooling the rate of market growth and improving levels of home ownership. In the year, new Buy-to-Let lending of £35.8bn was down 12% on 2016 (£40.6bn).⁷ This is, however, within the context of a continuing shortage of housing supply and mortgage regulation that keeps house prices relatively high and mortgage finance beyond the reach of many, thus underpinning strong and sustained demand for rental property.

The PRA changes to affordability assessment and to underwriting standards for portfolio landlords have driven two significant shifts within the Buy-to-Let market. First, we have seen growth in the professional landlord community, at the expense of the amateur. Second, we have seen these professional landlords increasingly prioritise yield, resulting in an increase in Houses in Multiple Occupation ('HMO') and student let lending, coupled with geographic diversification away from the South East, where yields tend to be lower.

Furthermore, professional landlords continue to mitigate the impact of tax changes by borrowing through limited companies. OSB is a respected lender within the specialist Buy-to-Let sector with a strong reputation for limited company lending and that has been beneficial to date and is expected to continue to be so.

Commercial

The UK commercial property market saw investment demand continue to increase during 2017, driven by overseas investors, who accounted for 60% of the whole market, up from around 50% in 2016.⁸ Uncertainty caused by Brexit continues to present risks, but there are strong underlying factors which mean the UK, and particularly London, remains attractive to investors. Demand has grown in all sectors except retail, with strong growth in offices, and particularly the industrial sector, which has benefited from the same types of shift – towards e-commerce – that has damaged the retail sector.

Research from JLL shows commercial property investment recorded double digit growth in 2017 to £60bn, although the share of that accounted for by properties over £200m is more than twice as high as 2016, and the proportion of smaller lot sizes has dropped.⁹ However, yields in cities across Europe came under more pressure in 2017 compared to London and other regional UK cities, creating the possibility for more activity in the UK during 2018, albeit with growth returning to more ‘normal’, single digit levels.

The lending market is dominated by the high street banks. Opportunity exists for specialist lenders whose manual underwriting approach, and willingness to engage in a dialogue to ensure robust understanding of customer requirements, can provide a service differential.

Residential development

The UK has experienced a long-term upward trend in real house prices, creating affordability problems as demand for housing continues to outstrip both supply and real wage growth. Furthermore, turnover in the second-hand housing market is subdued.

The housing white paper published in February 2017 refers to a “broken housing market” and identified that “not enough homes are being built” and thus prioritised initiatives that will seek to address this. Notable among the initiatives announced in the white paper were a raft of measures to encourage smaller builders to build more homes, through an improved planning framework. The government also expressed a desire that lenders should “back developers... in building more homes”. The white paper represents a holistic assessment of the UK’s housing needs, and it is encouraging to note the emphasis placed on supporting the small and medium sized developers who form our core audience for development finance.



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Specialist residential lending

OneSavings Bank’s manual underwriting and individual case assessment model provides a strong platform for specialist residential lending. Customers with unusual asset and income structures, or complex credit histories as well as those seeking shared ownership mortgages, are ill-served by the commoditised and inflexible decision making processes of mainstream lenders. We have identified strategic opportunities in this market that we will pursue in 2018.

Second charge lending

The second charge market saw approximately £1bn¹⁰ of gross new lending in 2017 (2016: £874m). This market continues to adjust to the changes in regulation that came into effect in March 2016 and the short-term outlook is at best neutral; any significant increase in market size is considered unlikely. In this context, we continue to resist the market trend to aggressively chase business through widespread price reductions or relaxation of credit standards, believing the returns available to be insufficient reward for the risks involved.

Funding lines

There are a number of successful non-bank or alternative providers of finance to retail and SME customers in the UK. These businesses are funded through a variety of means including wholesale finance provided by banks, high net worth investors and market based/peer-to-peer finance. OSB is an active provider of secured funding lines to the non-bank finance market, to date focusing on short-term real estate finance, leasing and development finance. Through these activities the Bank has achieved senior secured exposure at attractive returns to asset classes that it knows well. This financing activity covers a broad range of business sectors and its overall size is thus difficult to quantify. OSB sees a regular flow of opportunities, adopts a very selective approach and has a strong pipeline of new business.

1. UK Finance, Property sale transactions, UK countries, PT2, 21 Feb 2018.
 2. UK Finance, House price changes, UK countries and regions, HP14, 13 Feb 2018.
 3. 4. UK Finance, New mortgages by purpose of loan, ML1, 1 Feb 2018.
 5. UK Finance, First-time buyers, new mortgages and affordability, UK countries and regions, ML2, 1 Feb 2018.

6. Kent Reliance Buy-To-Let Britain Report, edition 7, Dec 2017.
 7. UK Finance, New and outstanding buy-to-let new mortgages, 2 Feb 2018.
 8. 9. JLL, The UK Commercial Property Market, Jon Neale, Jan 2018.
 10. FLA, Second charge mortgage new business volumes grow in 2017, 9 Feb 2018.