

EBS DKM Affordability Index



First Time Buyers now a stronger force in the Irish Mortgage Market, writes Dara Deering, Director, EBS Membership Business

So far in 2009 we continue to see a contraction in the overall economy and at the same time the personal wealth of the Irish consumer has reduced due to lower incomes and the cumulative impact of the October 2008 and April 2009 budgets.

Despite this, affordability, which measures, in this case, a First Time Buyers ability to purchase a new home and make their monthly mortgage repayment, has improved once again this quarter. This improvement is due in the main to the continued decreases in house prices and a continued low interest rate environment.

The ESRI/PTSB house price index to the end of August has shown that house prices fell by a further 10.1% this year. National House Prices are now down 24.4% since their peak in January 2007 and at €235,260 are now back to levels last seen in January 2004.

Mortgage interest rates, which directly impact affordability for new buyers, have reduced significantly in the past 12 months. Last September the average standard variable rate in Ireland was 5.82%. The average standard variable rate is now 3.15%. This equates to an average savings to mortgage holders of €400 per month on a typical mortgage of €250k.

At the same time consumer sentiment (as measured by the IIB Bank/ESRI Consumer Sentiment Index) has remained at low levels over the last year and with the exception of December, has been consistently below 50 points, the latest index for September showing sentiment now at 49.6

Understandably continued uncertainty has dampened demand in the first six months of 2009 as can be seen by the figures released by the Irish Banking Federation. 5,540 loans were issued to First Time Buyers in the first six months of 2009 and while this figure is down from 10,435 for the same period in 2008 the first time buyer share of the market increased significantly this year. First Time Buyers accounted for 45% of the house purchase market in H1 2009, up from 35% of the market in H1 2008.

Looking towards the end of 2009, on a national basis we expect house prices to have dropped c. 14% for the full year and new house completions to be in the order of 21k units down from 52k units last year. All of this will lead to a total new lending market of c. €8.8bn in 2009 down from €23bn in 2008 and a fraction of the highs of €40bn seen in 2006. While a pick up in application levels is being experienced by some lenders, it will take some time before lending volumes return to the average levels seen over the last number of years.



The **EBS DKM Housing Affordability Index** is a measure of the proportion of after tax income required to meet first year mortgage repayments for an 'average' first time buyer (FTB) working couple, each on average earnings. It takes into account changes in mortgage rates, changes in the level of mortgage interest relief, and is based on average earnings and new house prices in Dublin and across the national average.

Key Highlights October 2009

- Forecast December 09: First Time Buyer working couples will pay 13% of their net income in mortgage repayments (16.1% in Dublin). These figures compare with 26.4% (32.5% in Dublin) at the end of 2006.
- First Time Buyer mortgage repayments expected to fall by 43% in the period July 2008 to December 2009.
- National house prices are now down 24.4% since their peak in January 2007 and at €235,260 in August 2009 are back to levels last seen in January 2004.
- In September 2008, the average standard variable rate in Ireland was 5.82%. The average standard variable rate is now 3.15%. This equates to an average savings to mortgage holders of €400 per month on a typical mortgage of €250k.

Housing market remains subdued due to lack of confidence, writes Annette Hughes, Director DKM Economic Consultants



Consumers continue to hold back on house purchases, despite considerable improvements in affordability from reductions in house prices and falling mortgage rates. By and large, this reflects very weak consumer sentiment. The onset of recession and a bleak outlook for employment and earnings growth are keeping consumers cautious. As a result, overall conditions in the housing market continue to be depressed.

Average first-time buyer house prices, according to the permanent-tsb/ESRI index, fell below €200,000 in July 2009 for the first time since October 2003. Average prices in July were 29.1% down from the peak in early 2007. Using different datasets and methodologies, other sources have estimated reductions of closer to 40% in real terms.

Housing transactions (mortgage based only) have dropped sharply with house purchases predominantly being made for owner occupation rather than for investment purposes.

Among those that remain in the housing market, three main factors have been influencing purchase decisions for the past year: (i) an expectation that house prices will fall further; (ii) concerns over job security; and (iii) concerns over difficulties securing adequate mortgage funding, due to ongoing issues in the banking sector.

Oversupply is another factor. DKM has calculated that there is currently a supply overhang (i.e. over and above what is considered as the 'normal' level of vacant units) in the residential market of 136,000 units on average. This is equivalent to around four years of current housing demand nationally, although the mismatch between supply and demand is likely to be less in some areas of the country. (For further information, see the Review of the Construction Industry 2008 and Outlook 2009-11, available on www.dkm.ie/index.php?page=reports). The number of unsold new homes is estimated at around 35,000.

...while housing affordability continues to improve

The EBS DKM Housing Affordability Index is a measure of the proportion of after tax income required to meet first year mortgage repayments for an 'average' First Time Buyer (FTB) working couple, each on average earnings, borrowing 90% of the average FTB house price. It takes into account mortgage rates and mortgage interest relief; and is based on average FTB new house prices in Dublin and across the State. The current estimates assume that the average income for a working couple has remained unchanged since July 2008 at €82,370.

Figure 1 illustrates the significant improvement in housing affordability for FTB couples since early 2007, both in Dublin and on a national basis. We forecast that, by December, the national average FTB working couple will be paying 13% of their joint net income in mortgage repayments and 16.1% in Dublin. These figures compare with 26.4% and 32.5% respectively at the peak (December 2006).

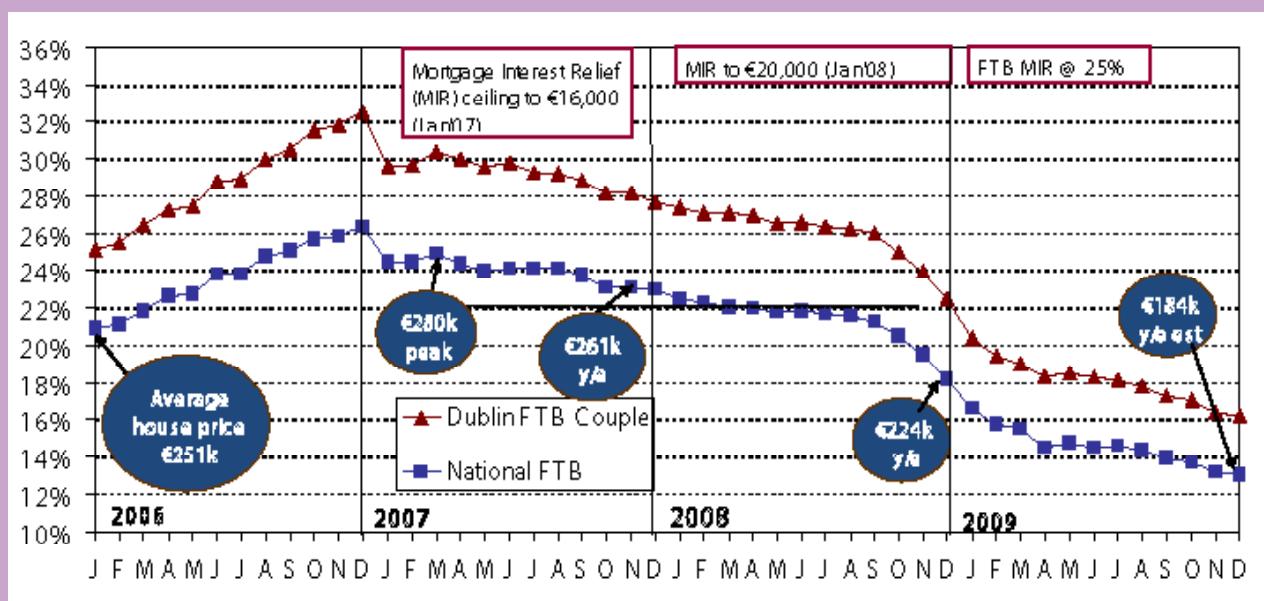


Figure 1: Net repayments as a % of disposable income (Dublin and National FTB couples)

Lower net monthly mortgage repayments have accelerated improvements in affordability

By December 2009, the projected net repayment for a First Time Buyer will have fallen by €513 per month since July 2008 (on a national basis) – roughly 43%, (based on €165,000 mortgage in December 2009). The equivalent drop in Dublin will be €643 per month, or 41% (based on a €218,000 mortgage in December 2009). This has helped affordability in a situation in which incomes have remained the same or have declined over the period.

Affordability for single FTBs has similarly improved

In this issue we also look at affordability for the average single person on average earnings, unchanged from €41,185 since July 2008. Affordability for single FTBs has similarly improved with falling house prices and mortgage rates - projected to fall from 54.5% in December 2006 to an estimated 25.2% by December 2009. The improvement has been more substantial for a single person, where average mortgage repayments after MIR will have fallen by 50% by December 2009 from the peak (December 2006), as opposed to 48% for the average working couple. However, the average house price to disposable income ratio remains high for single persons. By September this year, single persons were paying an average of €192,000 for a house, which was equivalent to around 6 times their average disposable income (just under 5 times gross income).

Single first-time buyers are likely to be more sensitive to price shifts than for couples because mortgage repayments make up a greater proportion of the disposable income of just one person. There are also the higher risks associated with becoming unemployed in the case of a single person as opposed to a working couple.

Trends in housing affordability for FTB working couple with forecasts to December 2009

	Dec 05	Dec 06	Dec 07	Dec 08	Sept 09 Estimate	Dec 09 Forecast
Average mortgage rate	3.63%	4.81%	5.35%	4.79%	3.30%	3.00%
National first time buyer working couple						
Monthly repayments (€)	1,018	1,323	1,228	1,007	738	689
As % of net income	21.6%	26.4%	23.0%	18.2%	13.9%	13.0%
Ave house price (000s)	249.5	279.0	260.8	224.2	192.5	184.0
Dublin first time buyer working couple						
Monthly repayments (€)	1,295	1,741	1,573	1,325	973	908
As % of net income	25.8%	32.5%	27.7%	22.5%	17.3%	16.1%
Ave house price (000s)	309.6	359.0	333.9	294.9	253.8	242.6

ASSUMPTIONS:

Monthly House Prices: permanent-tsb/ESRI data; 90% loan to value ratio.

Latest data show average FTB prices down by 19.2% year to July; assume prices fall 1.5% per month August to December.

ECB Rates: down from peak of 4.25% on 14th Oct'08 to 1% on 13th May 2009 following 7 reductions since Oct'08.

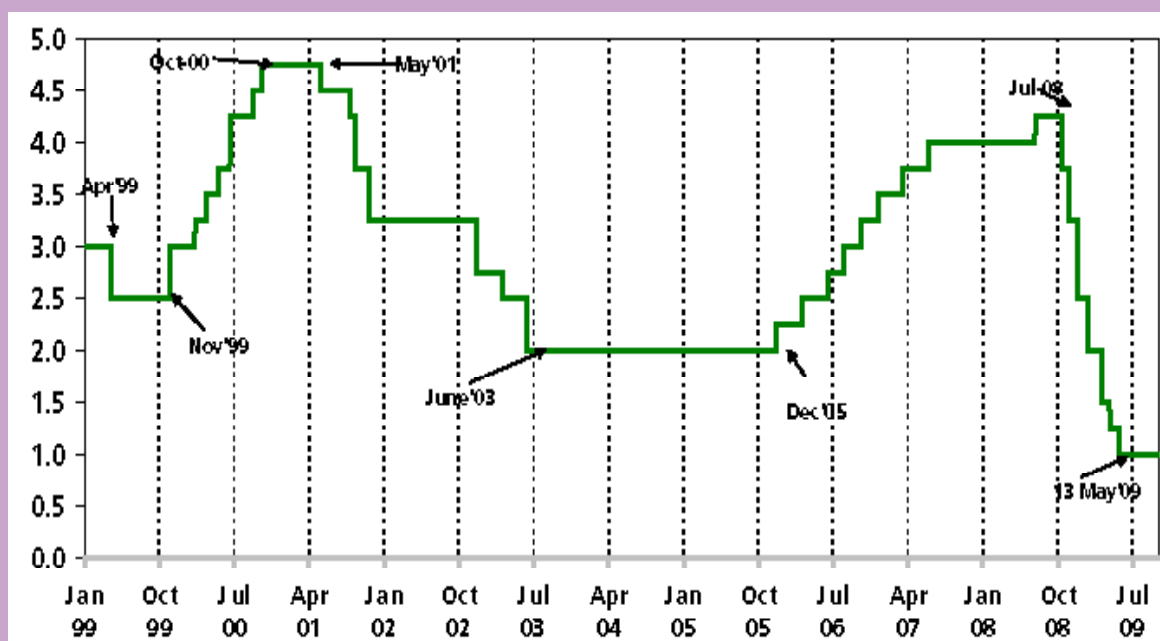
Average Mortgage Rates: Latest 3.46% in August 2009. Average of 3% forecast by year end.

Maximum Mortgage Interest Relief: €20,000 max available at 25% since Jan 2009 = €417 per month max.

Average gross income for FTB working couple unchanged at €82,370 since July 2008,

Income levy from January 2009. Incomes of Dublin buyers 10% higher than for buyers across the State as a whole.

ECB interest rate cycle over ten years to October 2009



NOTE: The January Issue of the EBS DKM Affordability Index will address the impact of the December Budget on the housing market's prospects.

Generating housing transactions is the first step to recovery...

It is clear that transactions will remain sluggish while consumers are waiting to see if a better deal becomes available. This situation has persisted for the past two years, despite improvements in affordability. While consumer sentiment remains low, the outlook is also poor for house sellers, given low demand and the overhang of supply from the boom years. As such, potential purchasers may believe that house prices have further to fall in aggregate, but in the short term, it will be a buyers' market. In the medium term, however, the return to more affordable and realistic house price levels can only be good for the housing market, thus allowing transactions to recover, increasing mobility and generating improved levels of economic activity.

.....but negative equity fears remain a concern

The house price crash has caused large numbers of homeowners to end up with negative equity – i.e. the value of the house has fallen below the amount outstanding on the loan – the majority of whom are FTBs with high loan-to-value ratios. A recent ESRI paper, 'Negative Equity in the Irish Housing Market', estimated that the number of homeowners in negative equity will reach 116,000 by end 2009, equivalent to 18% of households holding a mortgage. This is double the number at end 2008 (57,000). The expectation is that the numbers in negative equity will increase further in 2010.

The key risk with negative equity is that potential sellers who are in negative equity may be discouraged from selling their house at a price lower than their outstanding debt, thus hindering mobility and slowing recovery of the housing market and the economy. However, it seems that further price falls are inevitable and they are a necessary adjustment to pull the housing market back up to 'normal' levels.

An EBS Viewpoint - early signs of pick up in the market...,concludes Dara Deering.

We know the overall economy and the Irish housing market in particular have gone through significant change in the past 18 months. Housing market activity has been in constant decline, hitting a record low in the first Quarter of 2009.

However, over the past few months there are growing signs of a pick-up in consumer interest in the market. The numbers of mortgage applications at EBS Building Society in the past three months have seen levels grow by over 66% when compared to the first three months of this year. September was a particularly busy month with more than double the level of applications seen in February.

This increased interest in the housing market is expected to continue and to encourage those who are considering buying their first home (or trading up), EBS has been running a constant theme throughout 2009 that EBS is "Open for Mortgages". The purpose of this campaign is to assist those interested in getting a first step on the ladder. This has been supported through a number of other key focused initiatives.

First Time Buyer Seminars

In the last nine months EBS has held 12 dedicated First Time Buyer Seminars with a further 4 planned before the end of the year. These seminars are organised on a national basis aimed at educating First Time Buyers on the full home purchase process. It is estimated that up to 1,000 potential buyers will have gone to an EBS First Time Buyer Seminar this year.

Affordable Housing

A fund of €150m set aside for Affordable Housing was developed to ensure that finance is accessible and available for buyers seeking to purchase their first home. Year to date EBS has seen strong demand for this offering and has already advanced in excess €120m with an estimated €160m to be drawn-down on this fund before the end of this year.

EBS has a strong track record of supporting the Affordable Housing Scheme having provided the majority of home loans that have been advanced to borrowers since that Scheme was first established. It's estimated that c. 40% of all Affordable Housing in Ireland this year has been through the society.

So while mortgage market levels continue to be at historically low levels it is encouraging to see early signs of buyers willing to find out more about their ability to buy a home be that now or in the near future.

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