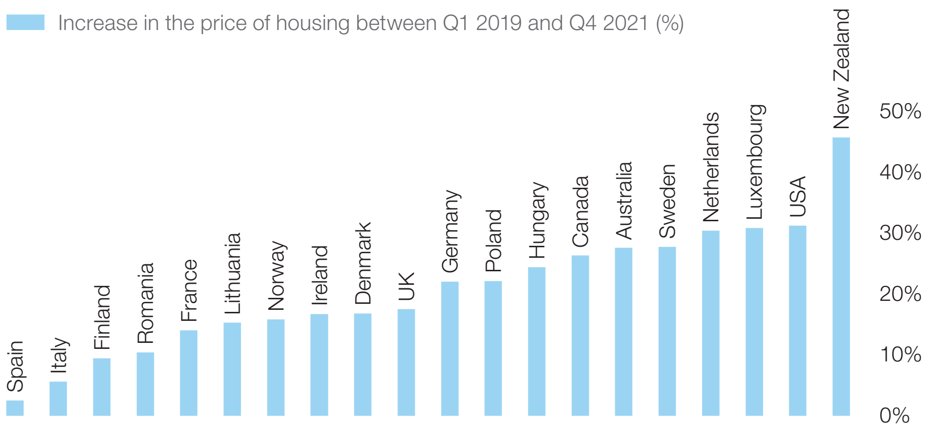
Accuracy

REAL ESTATE DYNAMICS

June 2022

The world economy is experiencing shock after shock arising from various sources: the COVID-19 pandemic, supply chain shortages, the war in Ukraine, severe inflationary conditions and stalling growth. However, in this edition of the Economic Brief, we will delve into the real estate sector to consider just how the economy is faring; after all, as the French saying goes, ‘when real estate is doing well, everything is’. [1]

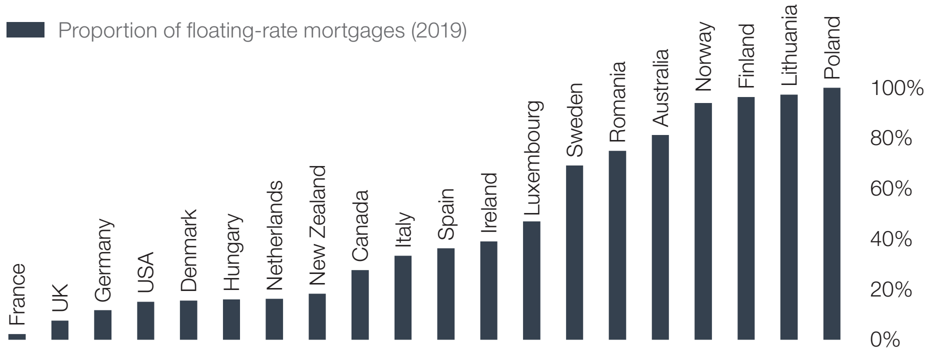
The rise of property prices is widespread



Sources: Accuracy & The Economist

The graph opposite shows the average percentage increase in the price of housing between Q1 2019 and Q4 2021. New Zealand posts the highest increase of 46% on average, but almost all countries in the sample show an impressive rise. This trend is linked to the record low interest rates of recent years, facilitating access to credit for buyers, combined with property scarcity and a boom in demand during the pandemic.

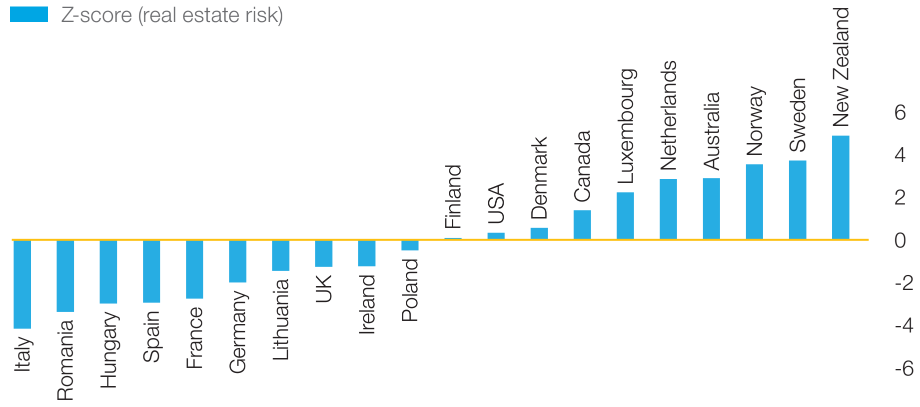
Dominance of floating-rate loans in Eastern Europe and Nordics makes them vulnerable



Sources: Accuracy & The Economist

However, it is important to bear in mind how this boom in demand is being financed. The graph opposite demonstrates the proportion of mortgage holders with floating rate mortgages. While Western Europe and the USA appear relatively safe from upward pressures on interest rates, thanks to a high proportion of fixed-rate loans, populations in Eastern Europe and the Nordics may find themselves in difficulty as interest rates begin to climb.

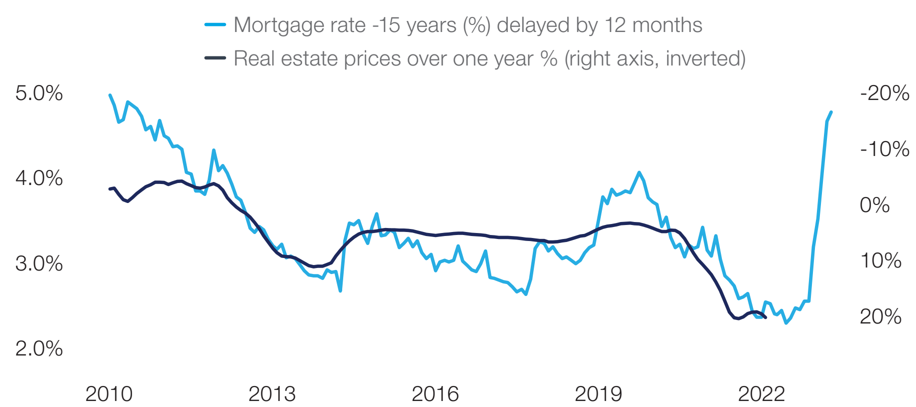
Summary of (relative) real estate risk



Sources: Accuracy & The Economist

The graph opposite attempts to summarise the relative real estate risk of each country in the sample using a standard-score analysis, which shows deviations from the mean. This analysis takes into account the increase in the price of housing and the proportion of floating-rate loans as mentioned above, but also the proportion of households with a mortgage and the measure of the outstanding mortgage amount in relation to disposable household income. Whilst it is worth noting that New Zealand and the Nordics continue to post high scores, of greater import is the USA: its position close to the mean is reassuring, in light of the systemic impact any developments in its real estate market might have.

USA: real estate market showing certain signs of deterioration



Sources: Accuracy & Bloomberg

However, unfortunately, it is not necessarily all sunshine and roses in the USA. The graph opposite shows the relationship between the average 15-year mortgage rate delayed by 12 months and the percentage change in real estate prices over one year. If real estate prices continue to follow the trend in mortgage rates, then we will see the growth of property prices begin to slow – or they may even fall – potentially leading to less investment and a slowdown in the market.

In conclusion, the real estate sector remains strong for the time being. Prices are continuing to rise, while interest rates remain low enough to boost demand. However, borrowers should be wary: in their fight to control inflation, central banks are likely to continue raising interest rates. This could have a significant impact on household disposable income across a number of countries.

Indeed, many risks lie around the corner, not least of which the potential for a slowdown in the USA, something that could have global consequences. The adage says ‘when real estate is doing well, everything is’; let us hope that the sector is robust enough to overcome these risks rather than to succumb to them.

[1] *Quand l’immobilier va, tout va.*