Market Briefing: March 2025

Key developments in the economy, housing and mortgage markets

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Executive summary

- GDP growth remains sluggish. The economy expanded by 0.1% in the fourth quarter of 2024, after showing no growth in Q3. January saw a 0.1% drop in output.

- The Bank of England cut Bank Rate by 0.25% in February, taking it to 4.5%. The Bank is having to balance the effect of slower growth and greater uncertainty stemming from possible US tariffs with higher than expected inflation and wage growth.

- CPI inflation rose to 3.0% in January before easing back to 2.8% in February. Core inflation has also been higher, rising to 3.7% in January before slipping to 3.5% in February.

- There are tentative signs that the labour market is stabilising despite increased tax costs for employers. The number of job vacancies in the December-February period was slightly up on three months earlier and employment increased by 144,000 over the same period. Unemployment was broadly flat and the unemployment rate remained at 4.4%.

- The government bond and interest rate swaps markets suffered considerable volatility in January, as investors' concerns about the sustainability of the UK's public finances came to the fore. But investor fears were eased by the government response, and fixed-rate mortgage pricing was only fractionally up over the month.

- The housing market remained resilient going into 2025, although there are signs that house price inflation is easing off from around 4% at the year's end as the rush to beat the stamp duty increase in April subsides.

- Mortgage approvals experienced the usual seasonal dip in December and January but, given the likely level of transactions being brought forward to beat the stamp duty hike, approvals may remain subdued in the coming months.

- The recovery in buy-to-let lending continued going into 2025. Lending in January was 15% above the average monthly figures for 2024, with a particularly strong performance in remortgages, which were up 20%.

- Mortgage arrears over 2.5% of the loan balance fell modestly in both Q3 and Q4. Owner-occupied mortgage arrears were 4% lower than in the first half and buy-to-let arrears down 6%.

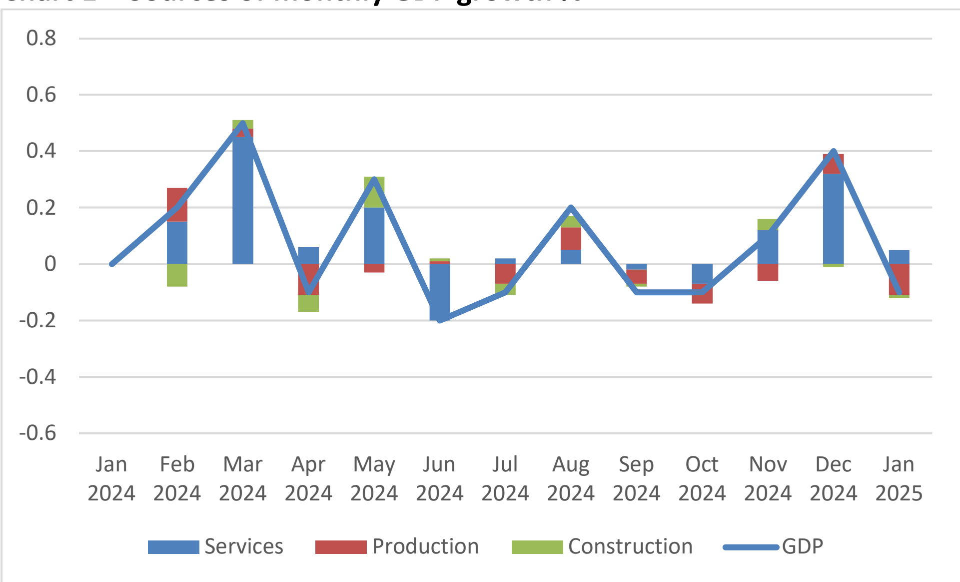
The economy

Output

GDP growth has disappointed since the middle of 2024. After showing no growth in Q3, the economy expanded by a modest 0.1% in Q4. Data for January showed a 0.1% contraction (see Chart 1).

Production led the decline in Q4, falling 0.4%, the third consecutive quarterly decline. It fell by a further 0.9% in January, driven by weakness in the manufacturing sector. Services and construction have performed better. Services output was up 0.1% in Q4 and also by 0.1% in January while construction was up by 0.3% in Q4 but fell 0.2% in January.

Chart 1 – Sources of monthly GDP growth %

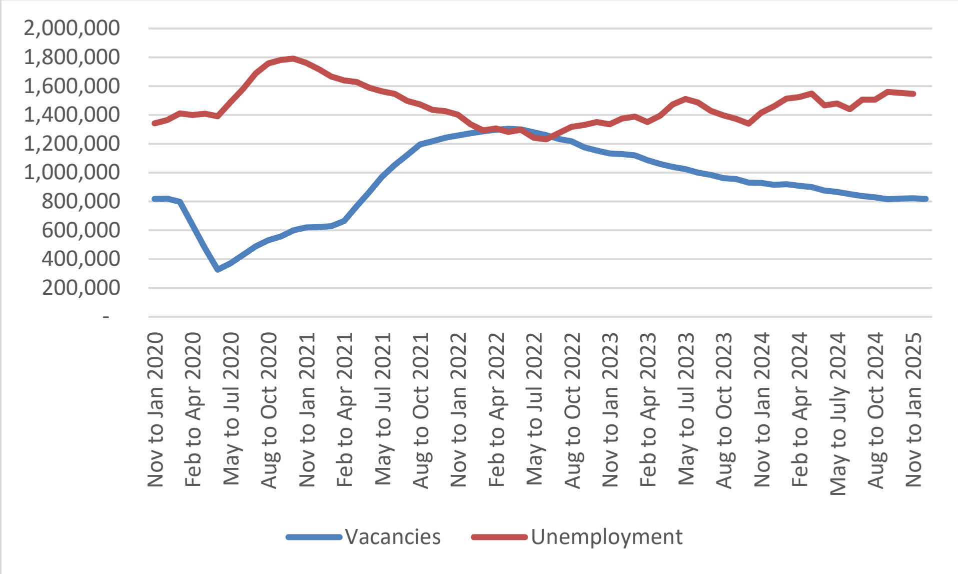


Source: Office for National Statistics

Labour market

Despite concerns about the impact of the rise in employers' national insurance announced in the autumn budget and the weakness of the economy, there are tentative signs the labour market is stabilising after a long period of falling vacancies and gradually rising unemployment. The Recruitment and Employment Confederation (REC) job ad tracker improved in January and February while overall job vacancies were up fractionally in the three months to December-February (see Chart 2). The unemployment rate was also steady at 4.4% between October and December with the number of unemployed dropping slightly in both November and December.

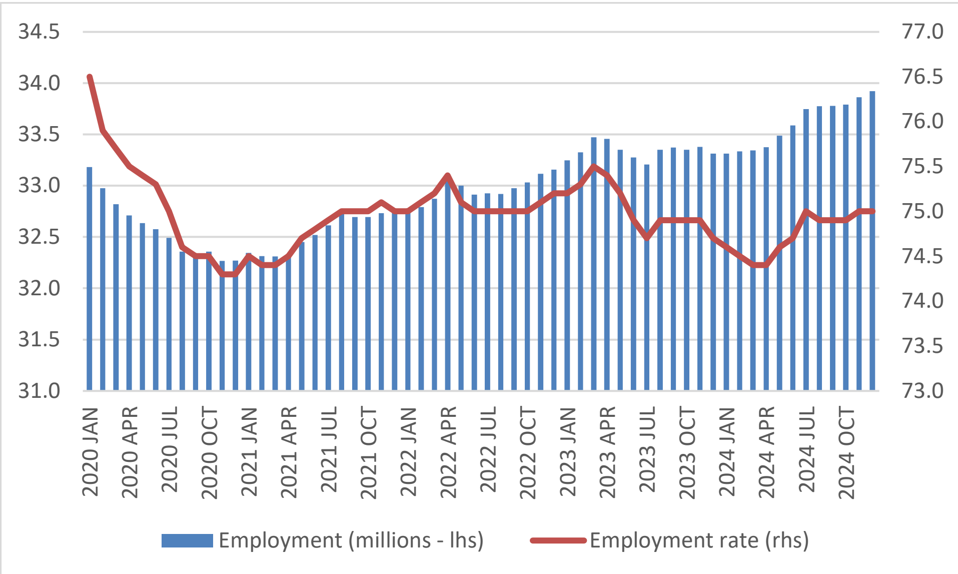
Chart 2 – Job vacancies and unemployment



Source: Office for National Statistics

Similarly, the overall level of employment and the employment rate do not point to any weakness, with total employment rising 144,00 between September and December. Although the rise in employers' national insurance and the minimum wage do not take effect until April, many employers, particularly larger ones, would have been expected to anticipate the future labour cost changes and adjust their workforce requirements accordingly, so the impact may not be as serious as some feared.

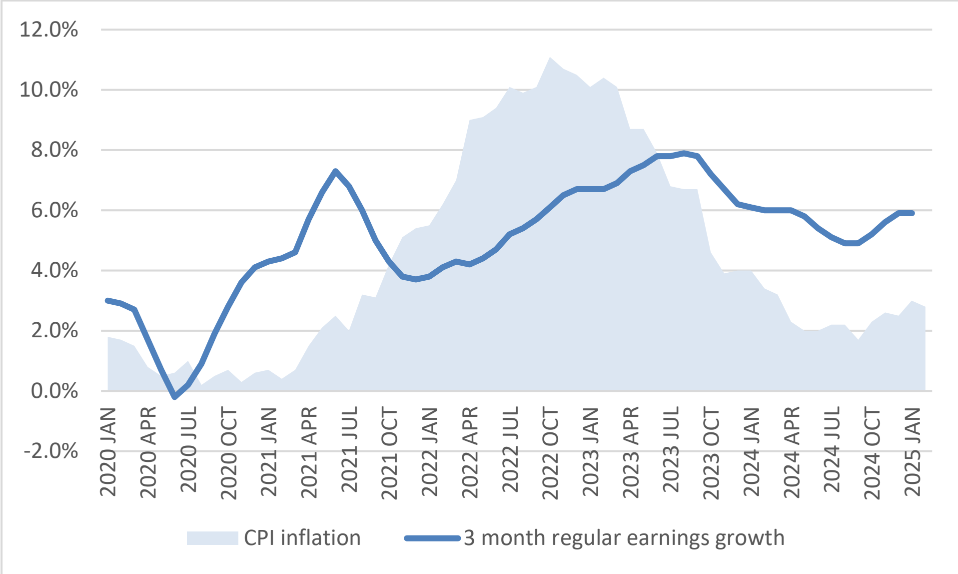
Chart 3 – Employment and the % employment rate



Source: Office for National Statistics

Earnings growth has also been on an upward trend in recent months (see Chart 4). In September, regular earnings growth (excluding bonuses) dipped to 4.9% but was back to 5.9% by January. The rise in headline inflation was probably the largest cause, but the stabilisation of the labour market will have helped support wages. One surprising trend is the recent sharp rise in public sector regular wage growth, up from 4.2% in October to 5.3% in December.

Chart 4 – Regular pay growth compared to CPI inflation



Source: Office for National Statistics

Inflation and interest rates

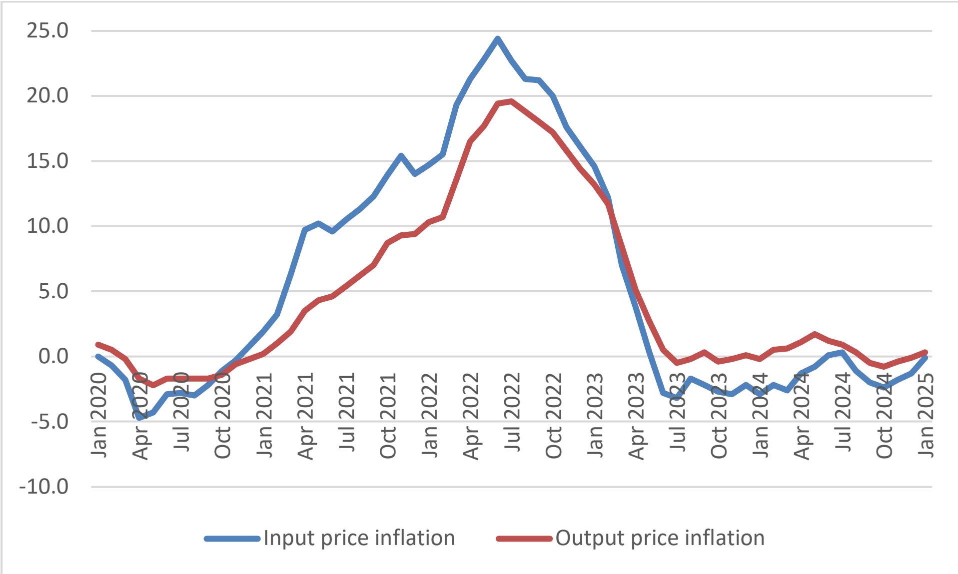
As Chart 5 shows, after falling back in the second half of 2022, unwinding some of the previous spike caused by the Russian invasion of Ukraine, commodity prices have stayed in a fairly narrow band, falling 8% since the end of 2022. Fears of a trade war have not had much impact on average commodity prices, but probably have affected oil prices, which fell from $79 a barrel in mid-January to below $70 by late March.

Chart 5 – S&P GSCI Global Commodities Price Index in Sterling

Source: S&P

UK producer input and output prices reflect the more settled pattern of global commodity prices (see Chart 6). In January, input prices were down 0.1% while factory output prices were up 0.3% on the year. Within the components of producer prices, fuel prices have experienced the largest falls over the past year.

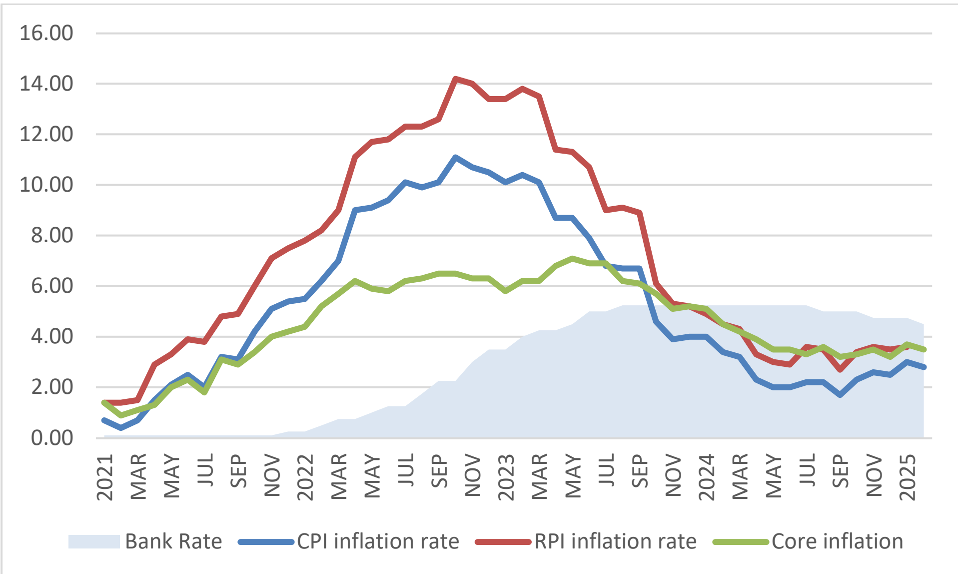
Chart 6 – Producer prices (% annual increase)



Source: Office for National Statistics

The trend in consumer price inflation over the past few months has been up, as Chart 7 shows. Headline CPI reached 3.0% in January, the highest rate since March 2024 before falling to 2.8% in February. Of particular concern was the rise in core CPI, which excludes volatile food, energy and tobacco prices. It rose sharply from 3.2% in December to 3.7% in January before falling back slightly to 3.5% in February.

Chart 7 – CPI, RPI and core % annual inflation and Bank Rate



Source: Office for National Statistics

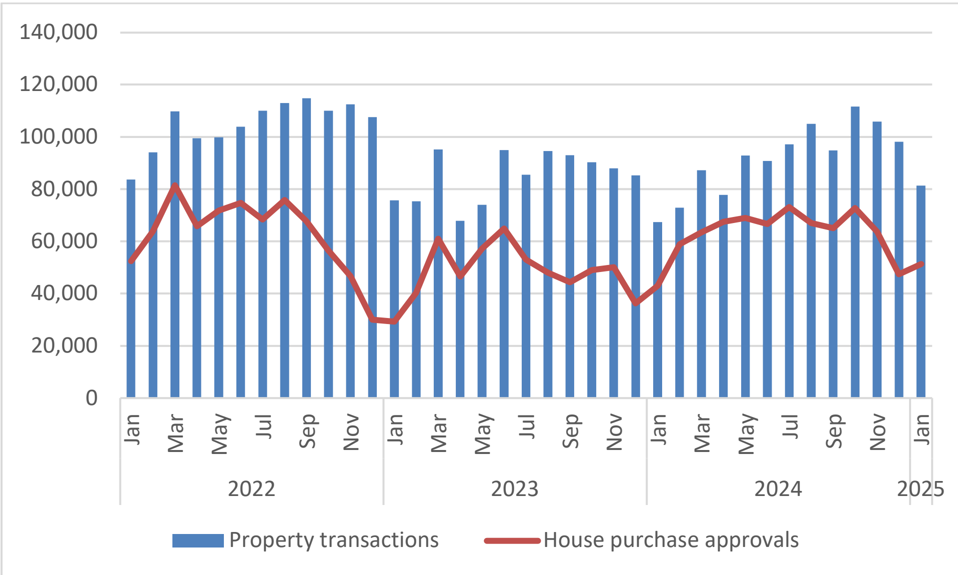
The Bank of England cut Bank Rate by 0.25% to 4.5% in February but held it at 4.5% at its March meeting. The Bank is having to balance disappointing growth and fears of a global trade war on the one hand and stubbornly high consumer price inflation and earnings growth on the other.

Housing and mortgage markets

Activity

Housing transactions fell back in December and January, in the usual seasonal lull (see Chart 8). However, on a seasonally adjusted basis they remained above the monthly average reported in 2024 and are likely to have risen in February and March, as buyers rushed to complete ahead of the upcoming rise in stamp duty.

Chart 8 – Housing transactions and mortgage approvals (monthly)

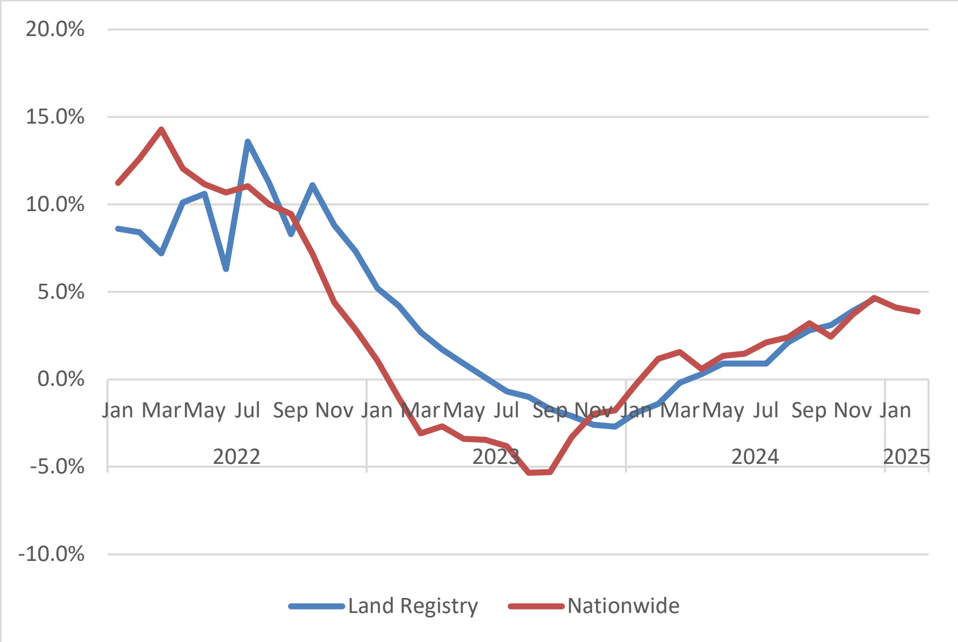


Source: HMRC, Bank of England

House prices and rents

House prices firmed over the course of 2024, with the Land Registry reporting a 4.6% increase in the year to December, the best performance since January 2023 (see Chart 9). The Nationwide and Halifax indices were showing similar increases in late 2024 but both have reported an easing of house price inflation since then, more so with the Halifax index, which showed a 2.9% increase in the year to February against 4.7% three months earlier. The RICS residential market survey shows a similar softening in agents' price expectations, which have turned negative on a three-month horizon, although respondents still expect house prices to rise over the coming year.

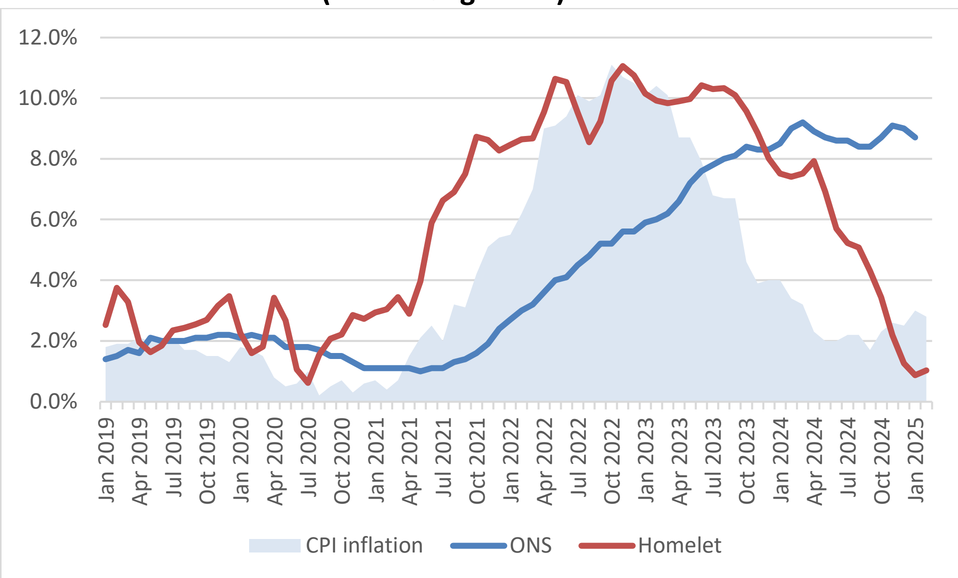
Chart 9 – House prices (annual growth rate)



Source: HM Land Registry, Nationwide Building Society

According to the Homelet rental index, rents on new tenancy contracts in the private rented sector rose by only 1% in the year to February, having notched up increases of 10.8% in 2023 and 8.0% in 2024 (see Chart 10). Rents peaked in September 2024, falling 4% since, suggesting a further deceleration in the annual rate of increase is likely this year. However, the ONS rental series still showed growth of 8.7% in the year to January, suggesting that landlords are adjusting up rents for existing tenants to reflect the sharp rise in market values in recent years.

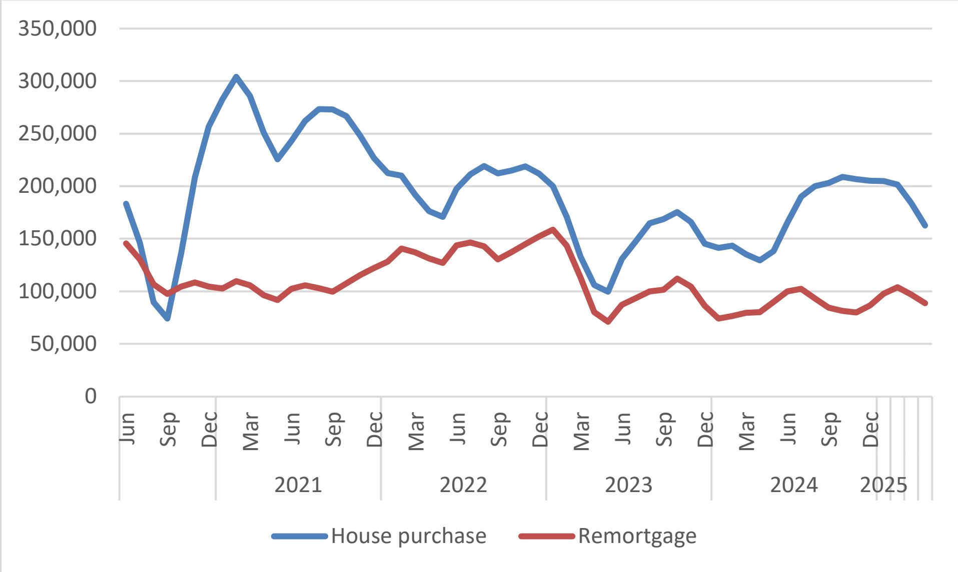
Chart 10 – Private rents (annual % growth)



Source: Office for National Statistics, Homelet

Mortgage lending

Chart 11 – Number of mortgage approvals (3 month rolling average)

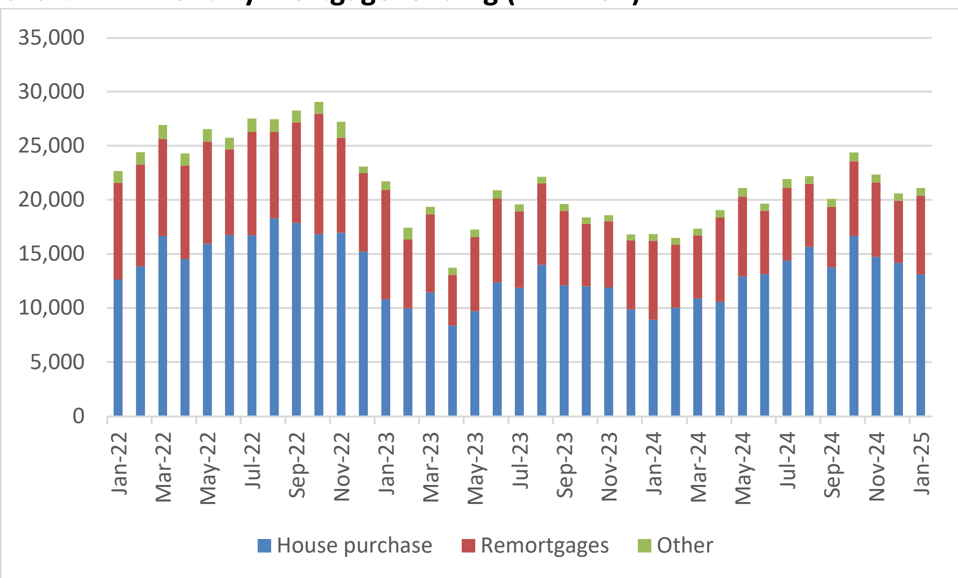


Source: Bank of England

House purchase approvals experienced the usual seasonal dip in December and January (see Chart 11), and it is likely that many buyers brought forward mortgage applications to earlier months to ensure they could complete purchases before higher stamp duty rates apply from April. This suggests that approvals might not experience much of a bounce in the short term.

Remortgages have been less buoyant, averaging around 90,000 a quarter since the start of 2024, with no clear trend. However, the 30,000 remortgages carried out in January did represent a 9% increase on January 2024.

Chart 12 – Monthly mortgage lending (£ million)

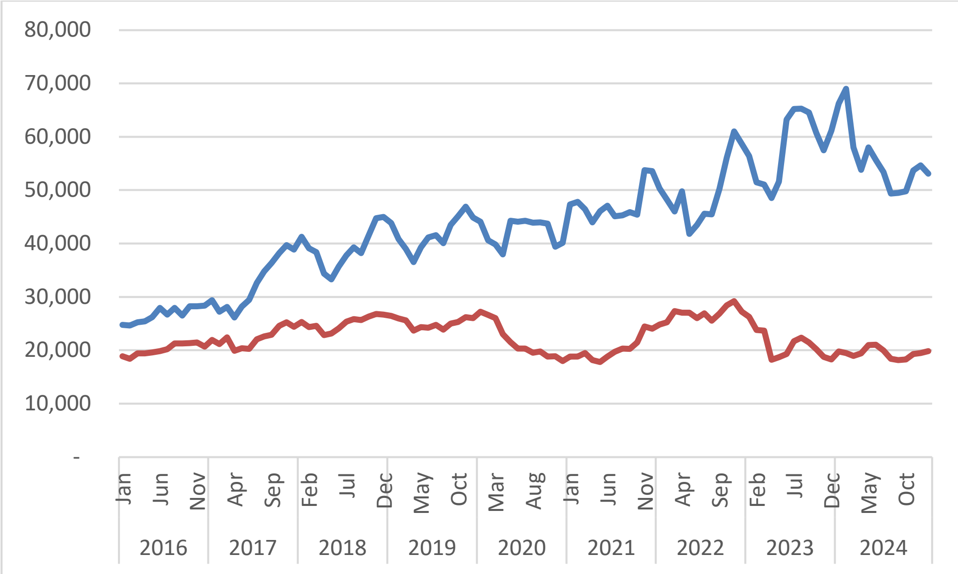


Source: Bank of England

Mortgage lending data has also been strong in recent months, led by house purchase advances which were 47% higher than a year earlier in January (see Chart 12), in part reflecting the acceleration of activity as buyers rushed to complete ahead of the stamp duty increase. Remortgage activity has generally been subdued but was up 8% in the three months to January compared to the previous three.

Product transfers

Chart 13 – Value of product transfers and remortgages (£m 3 month rolling average)



Source: UK Finance, Bank of England

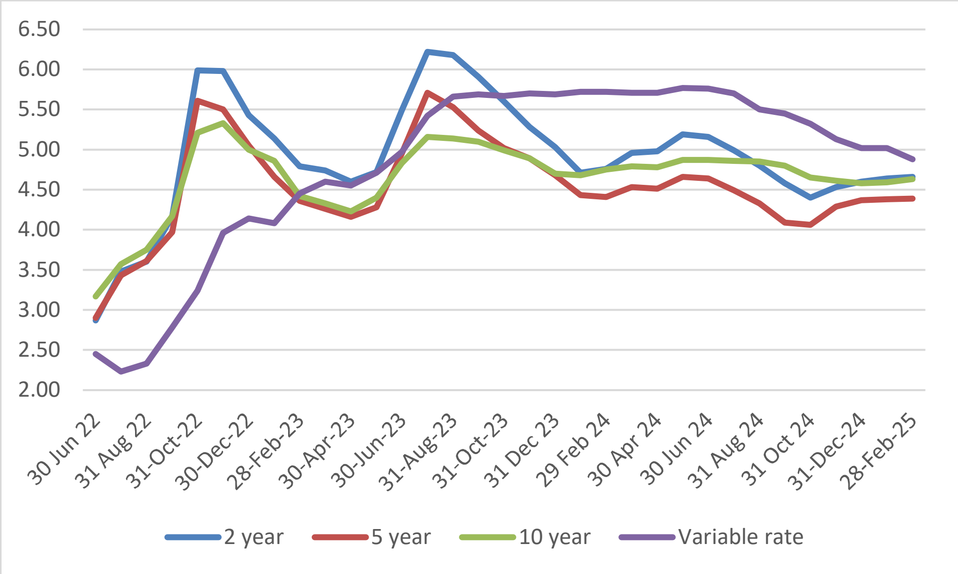
The strong upward trend in product transfers of recent years came to an end in 2024 (see Chart 13). There were 1.35 million product transfers in total in 2024, 9% below 2023's figure and the first annual decline since records began in 2015. There was also a slight switch back to remortgages, with the value of remortgages equal to 36% of the value of product transfers against 34% in 2023.

Mortgage pricing and products

January witnessed a significant sell-off in the government bond market as a result of heightened investor concerns about the sustainability of UK public finances. This had a direct impact on the interest rate swaps market that lenders use to price fixed-rate mortgages. 10-year gilt (government bond) yields peaked in mid-January at 4.9% while 5-year swaps reached 4.5%.

The market quickly recovered, pushing yields down 50 basis points by early February, but since then an upward trend has resumed, taking the 10-year gilt yield to 4.75% in late March and 5-year interest rate swaps to 4.3%. The volatility in swap rates in January made pricing fixed-rate mortgages difficult but by the end of January average fixed rates were barely higher than a month earlier (see Chart 14). At the same time, variable rate products saw a continued decline in price, reflecting recent falls in Bank of England Bank Rate, which was cut again in February to 4.5%.

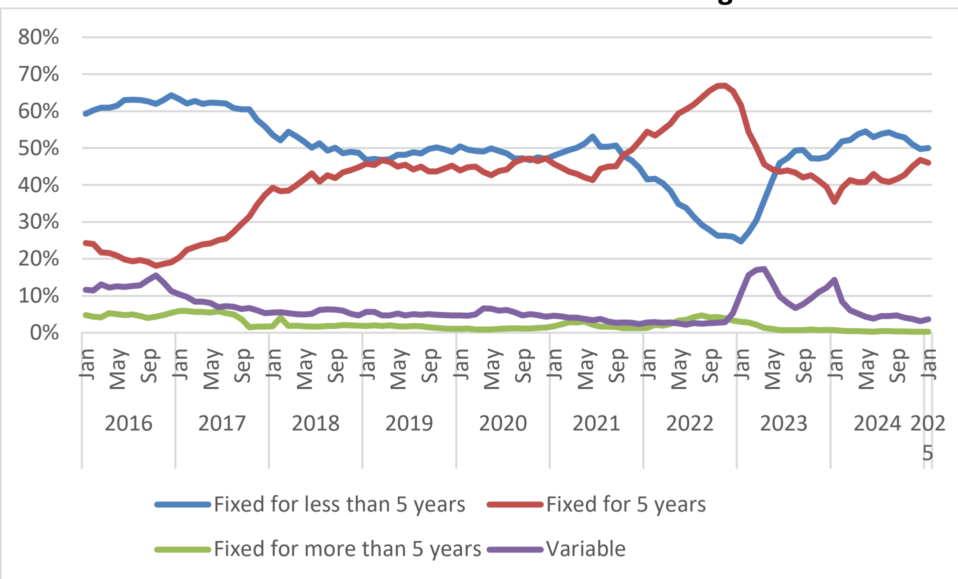
Chart 14 – Mortgage pricing for 75% LTV loans



Source: Bank of England

Despite the shrinking differential in pricing between variable and fixed-rate mortgages, the share of new loans that are on variable rate remained at only 4% going into 2025. 5-year fixes have been regaining popularity in recent months but products fixed for less than 5 years (mainly comprised of 2-year fixes) still represented 50% of all mortgages advanced in January 2025 (see Chart 15).

Chart 15 – Fixed and variable rate share of new lending

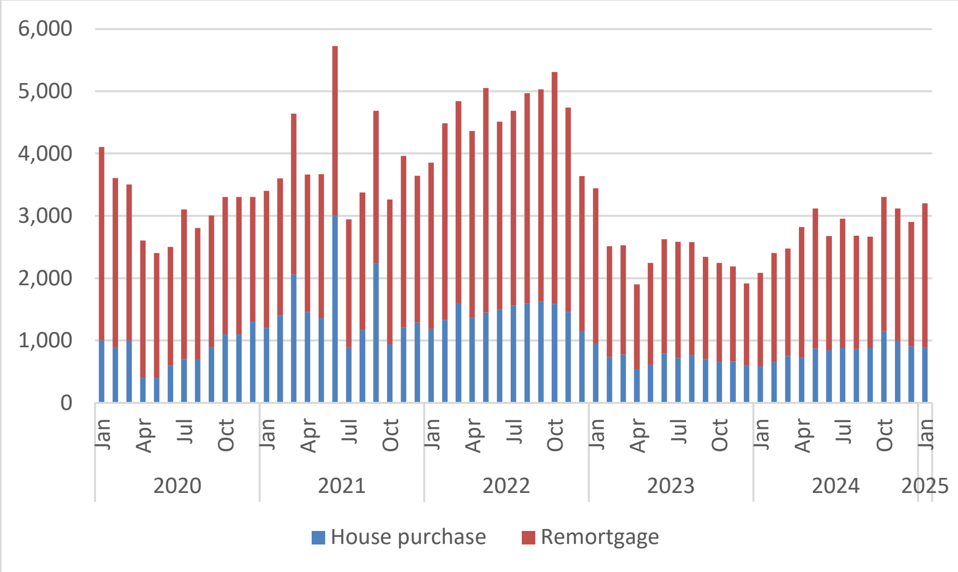


Source: UK Finance

Buy-to-let market

The recovery in the buy-to-let market continued in January. Total lending was £3.3 billion, 15% above the monthly average of 2024 (see Chart 16). While house purchase lending had been the best performing segment in 2024, rising 19% by value, January 2025 witnessed a stronger remortgage market, with £2.3 billion of lending, the highest total for two years and 20% above the average figure in 2024. Improving rental yields, resulting from the rise in rents over the past few years, are helping more landlords to meet affordability criteria, which had become challenging for some when mortgage rates rose in 2022 and 2023. Paragon Bank report that rental yields reached 6.93% in December 2024, the highest level since 2011.

Chart 16 – Buy-to-let lending (monthly £million)



Source: UK Finance

Chancellor's Spring statement and OBR forecast

On 26 March, Rachel Reeves unveiled a Spring statement she felt compelled to make to demonstrate the government's commitment to maintaining fiscal discipline after investor concerns about the sustainability of public debt pushed up the cost of government borrowing.

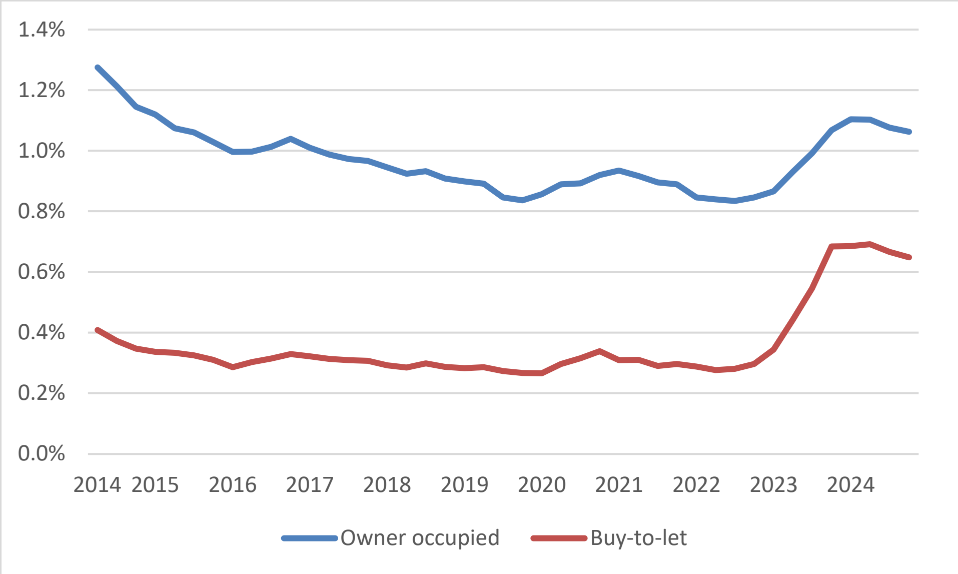
The Spring statement addressed spending rather than taxation with cutbacks focused on welfare, which saw cuts designed to save £4.8 billion, with a particular focus on health-related benefits, which have grown sharply in recent years. There were also cuts to general government spending of £3.6 billion by 2029-30 relative to previous projections, the two main exceptions being the NHS and defence, where the government wants to gradually increase spending to 2.5% of GDP.

The statement coincided with the publication of the Office for Budget Responsibility (OBR) March forecast, which cut forecast growth this year from 2% to 1%, leaving less headroom for government spending. On a more positive note, the OBR has projected that the changes to planning regulations introduced last year could boost housebuilding by 170,000 over five years, adding 0.2% to GDP by 2030 but Reeves still cut her forecast for housebuilding this Parliament from 1.5 million to 1.3 million homes.

The government also announced an extra £2 billion for social housing ahead of the Spring statement to deliver up to 18,000 new affordable homes.

Arrears and possessions

Chart 17 – % of mortgages in arrears of 2.5%+ of loan balance



Source: UK Finance

There was a modest fall in mortgage arrears in Q4 2024 for both the owner-occupied and buy-to-let sectors for the second consecutive quarter. Since the recent peak in arrears in the first half of 2024, owner-occupier arrears of 2.5% of the loan balance or more fell 4% to 1.06% of all loans. The buy-to-let sector experienced a similar decline, with this level of arrears falling 6% to 0.65% of all mortgages. As Chart 17 illustrates, arrears rose after the upward shift in interest rates in 2022 and 2023 but remain at historically low levels.

Prospects

The housing and mortgage markets continue to perform well against the background of a tepid macroeconomic picture. The underlying shortage of accommodation, robust average earnings growth and falling Bank Rate have all helped to support the market going into 2025. Indeed, housing has proved to be one of the most resilient sectors of the economy.

But the disappointing performance of the wider economy is bound to have an impact on the housing and mortgage markets. With limited productivity growth and higher employer national insurance costs, wage increases cannot outpace inflation indefinitely. Slower than expected growth has also affected tax receipts, forcing the Chancellor to commit to tighter spending controls in the Spring statement, which will in turn constrain the public sector contribution to aggregate demand.

The government is only too aware that there is also a larger threat on the immediate horizon in the form of President Trump's upcoming tariff announcement, expected in early April, which is likely to directly impact most countries including the UK. It is still far from clear how likely new US tariffs are to be permanent as opposed to being used as a bargaining chip to win concessions. But there is likely to be a retaliatory response from the EU and others, so the risk of a full-scale trade war is significant. Even if the US imposes fewer tariffs on UK goods than those of other economies, we are still likely to be hit by the negative impact a trade war would have on global growth.

As one of the most interest rate sensitive sectors of the economy, the housing/mortgage market could be somewhat insulated from the worst effects of a trade war should it come, as slower growth is likely to be accompanied by lower interest rates. Nonetheless, as we enter a period of heightened uncertainty no part of the economy can consider itself completely immune.