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How bad will it get for homeowners?

From The Jewish Chronicle

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Last year, three experts correctly predicted the house-price slump. We ask them what will happen next.

Eighteen months ago, amid the first whispers that property was heading for a downturn, the JC conducted a major survey on the state of the market. We asked finance experts, economist and property professionals where the market was going. The majority gave bland assurances that property values would remain stable or continue to rise. A couple said that there could be minor "corrections", but only three warned of the kind of crash we have experienced in the past 12 months.

So what made author Fred Harrison, chartered financial planner Jonathan Davis and economist George Magnus predict a crash, and, more importantly, what do they think will happen next?

It could have been avoided

Fred Harrison is author of several of books on the housing market and the economy, including Boom Bust: House Prices, Banking and the Depression of 2010 and The Renegade Economist. In 2007, he said: "Next year the market will go into the doldrums but prices will remain stable. Eventually prices will weaken and collapse. I originally forecast a drop of 20 per cent but now I think it will be more like 30 per cent."

In 2008 Harrison is not at all surprised that his predictions came to fruition, but he is frustrated that no one in government took much notice of his warnings. "I forecast in 1997 that the housing market would reach its peak in the winter of 2007-2008. The first regional price falls actually occurred in October 2007. Everything is exactly as I forecasted in 1997. I doubt anyone can match that record."

More recently, he amended his warnings. "In 2005, when everyone said there would be a soft landing I said that there would be two years of boom before the bust - and that there would not just be a recession but a depression. I don't expect the housing market to bottom out for five years. And the economy won't return to anything resembling normal for another 10 years." Contrary to popular belief, says Harrison, the economy is predictable. "It operates on an 18-year cycle. Within that 18-year cycle is a 14-year property cycle. After the 1992 recession I was able to calculate that, barring a major event like a world war, the end of the next cycle would be in 2010. On that basis I predicted that house prices would peak at the end of 2007."

Harrison blames successive governments for the current crisis: "It all could have been avoided. I wrote a book outlining the problem and I corresponded with the Treasury. If you change the tax system so that people are encouraged to invest in enterprises which add value rather than to speculate on land, you won't have property booms and busts. Rather, property prices would rise in line with the productivity of the economy. The banks were just responding to a market opportunity. There were windfall gains to be made on land and they wanted a slice of the action.

"We in Britain have a high public debt and high household debt. And our manufacturing base was destroyed in the 1980s, which means that we put all our eggs in one basket - financial services - the very industry which has been hit hardest. So unless you really need to buy, I wouldn't bother to invest in property for at least five years."

Worse than the 1990s

Jonathan Davis is a chartered financial planner at City investment advisers Armstrong Davis. He was so convinced that there would be a property meltdown that he speaks for a website called housepricecrash.co.uk dedicated to charting the progress of the bursting property bubble.

In 2007 he said: "Society has allowed the housing bubble to grow. It has been a spending spree beyond all reasonable economic sense. The global system needs to shock itself out of its complacency and it won't be pretty. The '90s are nothing compared to what we are about to experience."

In 2008, Davis feels that his predictions were actually too optimistic. "At that time I was forecasting a 25 per cent fall from the peak. Now, given the bankruptcy of some of the largest financial institutions in the world I've revised my forecast to 45 per cent.

"I predict that London and the South East will be one of the most severely affected areas because the UK economy has been predicated on two things in the past few years - the housing market and financial services - in other words everything that happens within a 100-mile radius of Trafalgar Square."

While many potential first-time buyers are still complaining that they cannot secure a mortgage, Davis, who has rented since 2002, has a different view.

"How would it benefit first-time buyers to get a mortgage now? I do plan to buy a property but certainly not for the next two or three years. It is far too early to bag a bargain. At some point in the future, the cost of a mortgage will be below the cost of renting - that is when to look for a property.

"There is also a more esoteric gauge. Historically, when the average price of a London property has been equivalent to the price of 300 ounces of gold, that has been an interesting time to buy. At present, the price of 300 ounces is £150,000. Gold will almost certainly rise. When it gets to £225,000, property prices may well be equivalent.

"The bust has been waiting to happen for several years. There are those who said the price would plateau and then continue to go up. This is based on zero historical precedent. There has never been an asset bubble in history which has deflated gently. I admit the bubble went on longer than I expected but that just means the bust will be bigger.

"Prices nationally are definitely going back to 2003, probably 2002. There is a one in two chance of them going back to 1999 levels."

Although Davis is happy that he was able to warn people that a crash was on the horizon, he says that it cost him a lot of business. "In the short term it hindered us because no one wanted to listen to what I was saying. However, in the last year everyone has been listening. We have grown 35 per cent in the past year and saved our clients from enormous losses."

Not all gloom

George Magnus is senior economic adviser at UBS investment bank. He has been warning for some time of how, reckless lending in the United States housing market could have an effect on the world economy.

In 2007, he said: "American mortgages are worth around $10 trillion, of which 35 to 40 per cent is in the sub-prime area. The rate at which people are being forced out of their homes is beginning to be rather eye-popping. The probability is that the US housing market could keep dropping, which could have financial repercussions which spill over to other countries including our own." He predicted there could be "lean years after the feast".

In 2008, he says that the downturn has gone pretty much the way he expected it too. However, he adds that, like pretty much everyone else, "I have been quite shocked by seeing how it looks up front. In particular, the speed of the capitulation of the economy has been frightening. It has turned out to be much scarier in reality."

Despite the fact that world financial markets are in a tailspin, Magnus does not, compared to some other commentators at least, take a gloomy view.

"Some people are saying there's no hope and that we might as well go and live in a cave. I don't think that's right. I think that house prices will fall by a total of 30 per cent or so but there is a chance that prices may be bottoming out by the end of next year.

"Until debt has been reduced and the banks feel able to lend again, we won't see much progress, but the thing that makes me feel that it might not be so bad is that the government seems to have a good idea about the severity of the problem and has taken measures to contain the recession. Unusual times like these require unusual measures.

"I always say it's like in the Bible. Seven years of feast followed by seven years of famine - property certainly seems to be on a 14- or 15-year cycle.

"Will it ever change? Well demographics might well slow things down. The proportion of 20- to 44-year-olds in most rich countries is going to drop by 10 to 15 per cent, so there will be fewer people of prime first-time buyer age fuelling the demand for property. Having said that, demographics are only one side of the equation."