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The expected impact of COVID-19 on the housing market

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Abstract
The outbreak of COVID-19 has been an unprecedented disruptor in the world´s social and economic fabric. However, the crisis has only barely affected the real estate market, which continues its upward trend in many countries as of the fourth quarter of 2020. Drivers of housing prices and possible effects of the pandemic on the housing market are examined in this article. Special emphasis lies on developments in the EU.

I Introduction

Having spread to over 180 countries within the first 3 months since its outbreak, COVID-19 has impacted the world unprecedentedly. From a viral epidemic to a global pandemic, the loss of lives has been devastating. Consequences for certain sectors of the economy, like public health or travel and tourism, will be felt for years to come.

On the economic front, COVID-19 caused Gross Domestic Product (GDP) growth rates to plunge below -6%[1] for some regions in the European Union (EU) in the year 2020. To mitigate the effects of the crisis, governments and central banks across the globe have, through stimulus packages and quantitative easing measures, sustained income and employment levels temporarily.

Now, a year later, the road leading to recovery appears to be relatively close at hand. With vaccination programs underway in most countries, there is a sense of optimism. Going forward, government policies will soon move from aid to self-reliance, taking lessons from the pandemic into consideration. In the European Union, overall GDP is expected to shrink in the first half of 2021, but then rise and grow by 3.7%. Globally, real GDP is predicted to grow by 5.2% in 2021[2]. On the downside, strains of contagious mutants of the virus are causing a sense of uncertainty. Post-pandemic optimism is therefore cautious, as some countries of the EU return to pre-pandemic growth levels faster than others.

Housing markets worldwide have been trending upwards during the pandemic even as unemployment rates increased and GDPs fell. This article takes a snapshot of the housing market in the EU and sheds light on questions like: How is the pandemic affecting the real estate market? How are government policies designed to help home buyers? What possible outcomes lie ahead?

II The pandemic and beyond

Trends in housing prices

After the financial crisis of 2009, housing prices in the EU as well as in countries like the UK and the US continued to fall for a few years (see Figure 1)[3] [4]. Since 2015, however, they have been rising steadily. Housing prices in the UK, which had levelled off in the years preceding the pandemic, increased in 2020, even as the pandemic began. In Australia, while the heated housing market plunged in 2017 and 2018, prices rallied in 2019 and the impact of the pandemic in 2020 was only marginally perceptible. Housing prices in the US, Germany, and the EU as a whole appear to have been keeping pace since 2015. Despite the pandemic, the house price index trended further upwards during the first three quarters of 2020.

The OECD´s housing prices is a measure of the real house price index, which is given by the ratio of the nominal house price index to the consumers' expenditure deflator in each country[5]. OECD data is used to depict house prices in the UK, USA, Australia, and Germany in Figure 1. Eurostat defines the

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[1] European Commission (2020). JRC analyses COVID-19 impact on economy and labour markets to help guide EU response. Retrieved February 10, 2021, from https://ec.europa.eu/jrc/en/news/jrc-analyses-covid-19-impact-economy-and-labour-markets-help-guide-eu-response

[2] European Commission (2021). European Economic Forecast. Winter 2021. Retrieved February 22, 2021, from https://ec.europa.eu/info/sites/info/files/economy-finance/ip144_en_1.pdf

[3] European Commission (2021). Eurostat, House price index, quarterly data. Retrieved February 12, 2021, from https://ec.europa.eu/eurostat/databrowser/view/tipsho40/default/table?lang=en,

[4] OECD (2021). Housing prices. Retrieved February 10, 2021, from https://data.oecd.org/price/housing-prices.htm

[5] Ibid

house price index (EU) as an index that captures price changes of residential properties, both newly built and existing, purchased by households. It also includes the land component.6

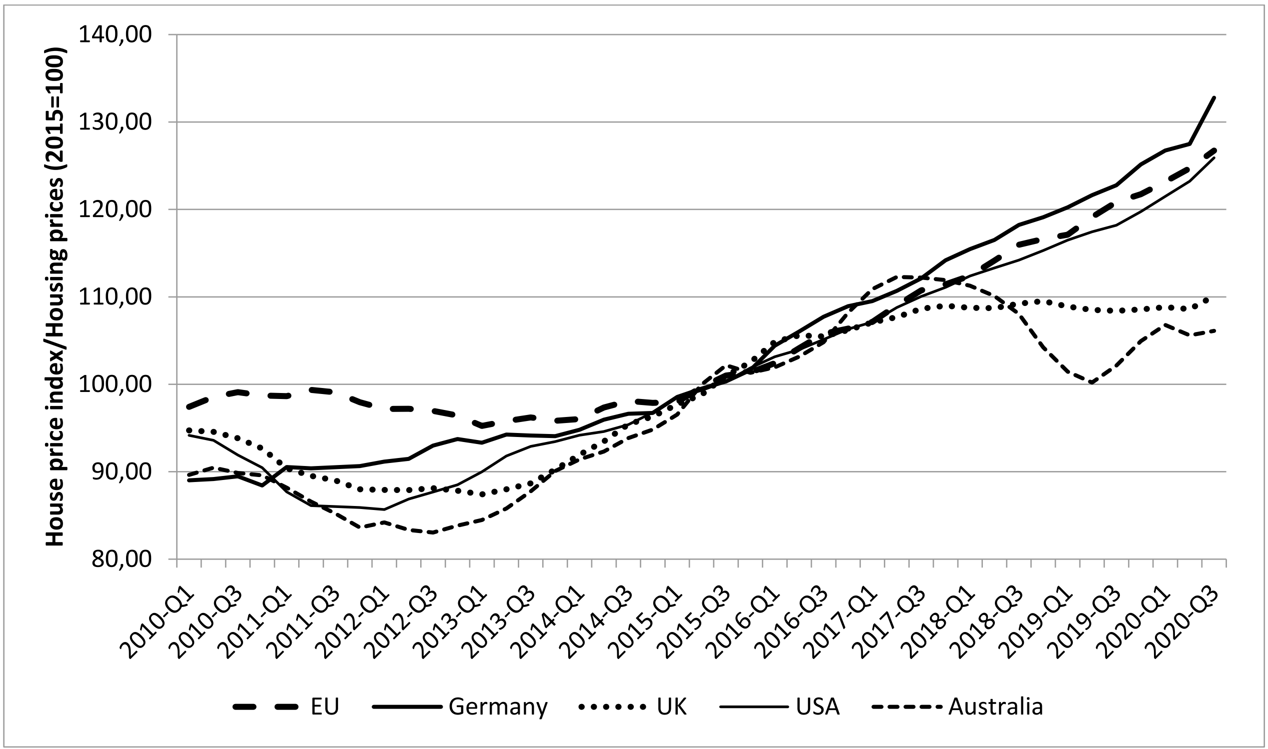

Figure 1: Own illustration based on OECD data (housing prices) for the UK, US, Australia, and Germany and Eurostat data (house price index) for the EU from 2010-Q1 to 2020-Q3

A major factor that triggered the financial crisis of 2009 was the overheated housing market in the US. Lending banks were responsible for sanctioning sub-prime mortgages which were not met when they became due, resulting in home foreclosures and the financial crash. Current rising trends in housing markets of the US and the EU are not exactly like those of the early 2000s. Sub-prime mortgage lending policies are not at play.

As Figure 1 shows, housing prices had been on the rise even before the pandemic started and continued in the same direction in 2020. Low-interest rate policies pursued by central banks like the European Central Bank (ECB) and the Federal Reserve make loans attractive to home buyers. These policies stayed in place during the pandemic.

On another note, lockdowns during the pandemic increased unemployment. The following section discusses how these two components - interest rates and unemployment - have impacted the housing market during the pandemic and how they could affect the future trajectory of house prices.

[6] European Commission (2021). Eurostat, House price index and house sales. Retrieved February 12, 2021, from https://ec.europa.eu/eurostat/web/housing-price-statistics/overview,

Monetary policy and government directives on housing

during the pandemic…

In the past several years, central banks of the world, including the European Central Bank and the US Federal Reserve, flooded markets with money, bringing down interest rates[7]. These policies continued during the pandemic. The result of easy money can be felt in developments in housing markets. In the US, current 30-year mortgage rates have fallen to below 3%[8] and interest rates on home loans (for periods of more than 10 years) are below 2% in Germany and the EU[9]. Old loans can be locked in at new, more favorable rates, bringing monthly savings to borrowers. New mortgage loans are possibly higher due to higher prices, but lower mortgage rates appear to make the deal more attractive.

Many millions of home owners across the globe are faced with making mortgage payments that become due every month. The onset of the pandemic brought on loss of income and increased unemployment which was felt more strongly in countries like the US than in the EU. If mortgage payments are not met, delinquent clients face home foreclosures. Governments across the globe have intervened in 2020 with the aim of providing homebuyers, real-estate businesses, and lending institutions with legal structures to deal with gaps in mortgage payments. These measures are meant to prevent or forestall the economic crisis from reaching the housing market.

…and beyond

To augment monetary easing strategies, two decisions were taken by the ECB in December 2020[10]: (i) extending the time periods for its purchases of net assets under the Pandemic Emergency Purchase Programme (PEPP) and (ii) planning three targeted long-term refinancing operations (TLTRO III) in 2021. These strategies will continue to boost liquidity and enable households and firms to access credit easily in 2021 and the coming years. With continued low interest rate policies in position at the ECB and the Federal Reserve of the US, it can be expected that general spending levels will be maintained and boosted in the near future. Easy credit will continue to make real estate financing easy.

Without government intervention during the pandemic, homes would be sold in an emergency frenzy, causing the market to crash suddenly. The US Federal Housing Finance Agency instructed home loan bankers: (i) To extend foreclosure protection from March 2020 to March 2021. If clients default on their mortgage payments, lending banks are not allowed to recover the value of the loan by selling the property. (ii) In order to prevent foreclosures, legal measures like forbearances have been instituted in the pandemic period. A forbearance is an agreement between the lending bank and the client to reduce or suspend mortgage payments for a fixed period of time. On expiry of this period of moratorium, the borrower and lender follow a payment plan to catch up on all missed payments. These interventions have protected about 70% of single-family homeowners with mortgages in the US.

[7] European Central Bank (2021). Key ECB interest rates, Main refinancing operations. Retrieved February 12, 2021, from https://www.ecb.europa.eu/stats/policy_and_exchange_rates/key_ecb_interest_rates/html/index.en.html,

[8] Freddie Mac (2021). Primary Mortgage Market Survey . Retrieved February 12, 2021, from http://www.freddiemac.com/pmms/

[9] Euro-area statistics (2021). Bank interest rates-Loans. Retrieved February 12, 2021, from https://www.euro-area-statistics.org/bank-interest-rates-loans?cr=eur&lg=en

[10] European Commission (2021). European Economic Forecast. Winter 2021. Retrieved February 22, 2021, from https://ec.europa.eu/info/sites/info/files/economy-finance/ip144_en_1.pdf

Similar programs have been instituted by governments of EU countries[11]. In Germany, evicting tenants, similar to foreclosures, have been suspended to 2022[12]. Moratoriums on monthly mortgage payments have also been in effect since the onset of the pandemic.

<u>Unemployment and housing markets</u>

during the pandemic…

The labor market plays an important role in developments in the housing market. Unemployment in the EU has been falling steadily in the period 2015-2019 (see Table 1)[13]. The increase in unemployment from 6.6% in the fourth quarter of 2019 to 7.5% in the third quarter of 2020 did not appear to make a dent in housing prices, which increased by over 4% in the span of 9 months (see Figure 2)[14]. Additionally, home sales in the third quarter of 2020 exceeded those of the fourth quarter of 2019 for four of the nine countries of the EU for which data was available[15].

Table 1: Unemployment rates and the housing price index, EU

Quarter	Unemployment rates	Housing price index (2015=100)
2015Q4	9.7%	101.36
2016Q4	8.8%	106.36
2017Q4	7.8%	111.44
2018Q4	7.1%	116.61
2019Q4	6.6%	121.75
2020Q3	7.5%	126.73

[11] Joint Center for Housing Studies of Harvard University (2020) The state of the nation´s housing Retrieved February 12, 2021 from https://www.jchs.harvard.edu/sites/default/files/reports/files/Harvard_JCHS_The_State_of_the_Nations_Housing_2020_Report_Revised_120720.pdf

[12] Bundesministerium des Innern, für Bau und Heimat (2021). Informationen zu Corona-Hilfen. Retrieved February 10, 2021, from https://www.die-wohnraumoffensive.de/aktivitaeten/corona-hilfen/

[13] Eurostat (2021). Unemployment rates by sex, age and citizenship (%) [lfsq_urgan]. Retrieved February 12, 2021, from https://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=lfsa_urgan&lang=en,

[14] Ibid

[15] Eurostat (2021) Home sales index of number of transactions. Retrieved February 12, 2021, from https://ec.europa.eu/eurostat/databrowser/view/PRC_HPI_HSNQ__custom_547159/default/table?lang=en,

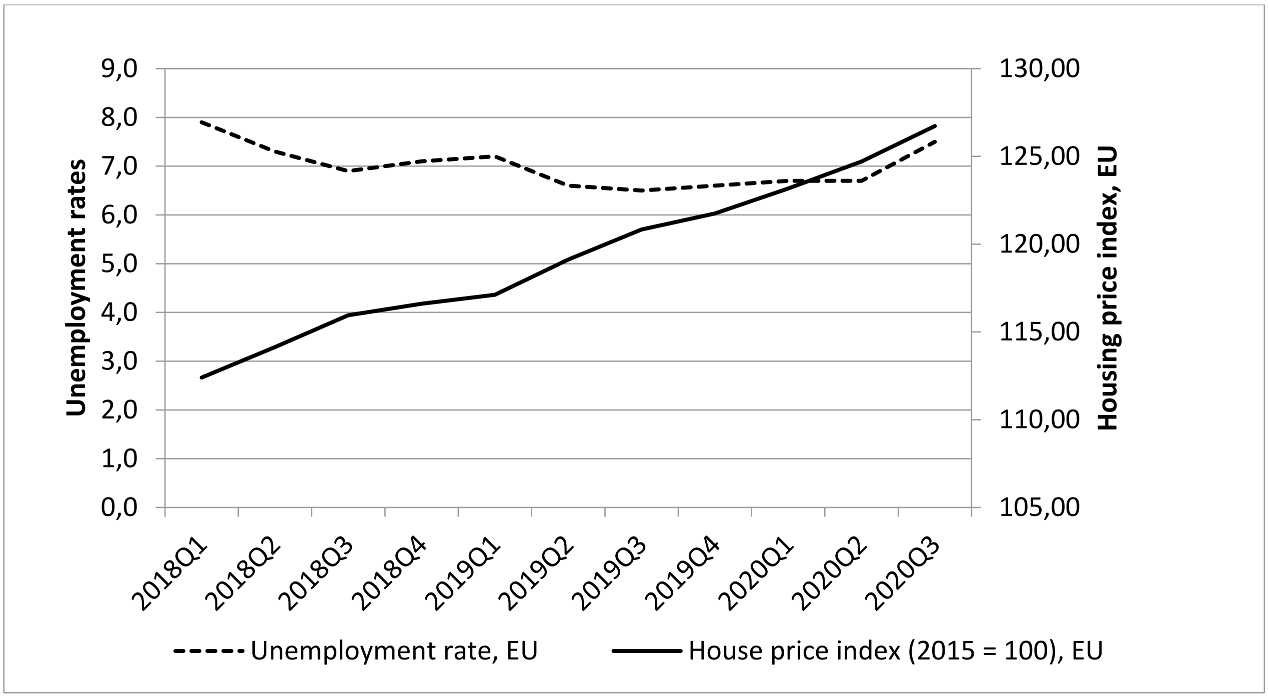

Figure 2: Own representation of Eurostat data on unemployment rates and the housing price index, 2018-2020, EU

It appears that job losses during the pandemic have not affected the housing market in the EU, at least not until the third quarter of 2020. The increase in unemployment in 2020 in the EU was relatively slow. However, unemployment figures are possibly hiding the actual situation of unemployed people in the EU.

At the onset of the pandemic, many firms closed due to lockdowns. Others faced a sharp contraction in sales, which forced employers to reduce the working hours of their employees. About 15% of employees in Germany and 34% in France were on short-time work16. Instead of laying off workers, national governments of the EU took the route of job retention schemes to support labor markets. This kept employment relatively stable, as is reflected in Figure 2. Through these stimulus measures supported by national governments, firms managed to stay liquid even as employees were retained. As regions and economies opened up after lockdowns in 2020, it was easier for firms to resume their business activities.

...and beyond the pandemic

As immunizations increase and restrictions are lifted, economies will be poised to open up in 2021. Savings accumulated during the pandemic will mean spending on consumption and spending on housing. As long as inflation is maintained at or around a safe level of 2% and unemployment rates are low, aggregate demand will boost growth. It is expected that governments will continue their stimulus measures and supportive labor market policies as required.

On the one side, it appears that labor market policies, to mitigate the effects of unemployment combined with the ECB´s monetary policies of low interest rates, will continue to boost economies. Favorable mortgage rates and job retention strategies will push demand for homes, and house prices

16 European Central Bank (2021). The impact of the COVID-19 pandemic on the euro area labour market. Retrieved February 24, 2021, from https://www.ecb.europa.eu/pub/economic-bulletin/articles/2021/html/ecb.ebart202008_02~bc749d90e7.en.html

will continue to climb. On the other hand, as moratoriums end, high levels of accumulated debt and unemployment will have a dampening effect on the housing market.

The net effect of boosting policies versus the inherent consequences of longer lockdowns and unemployment are not clear. If boosting policies are maintained, the housing market will continue an upward, albeit slow rise in the short run. If health challenges and lockdowns continue, layoffs and social disruptions occur, and economic growth is not as strong as expected, a downturn could hit the housing market not too far down the road.

III Uncertain times

The World Pandemic Uncertainty Index measures uncertainty on a global level by counting the word "uncertain" and its variants near pandemic-related terms that appear in reports made by the Economic Intelligence Unit (see Figure 3)17. This index is calculated as a percentage and multiplied by 1,000. According to this measure, uncertainty due to the pandemic situation in the last year was about five times higher at the peak than during the SARS outbreak in 2002-03.

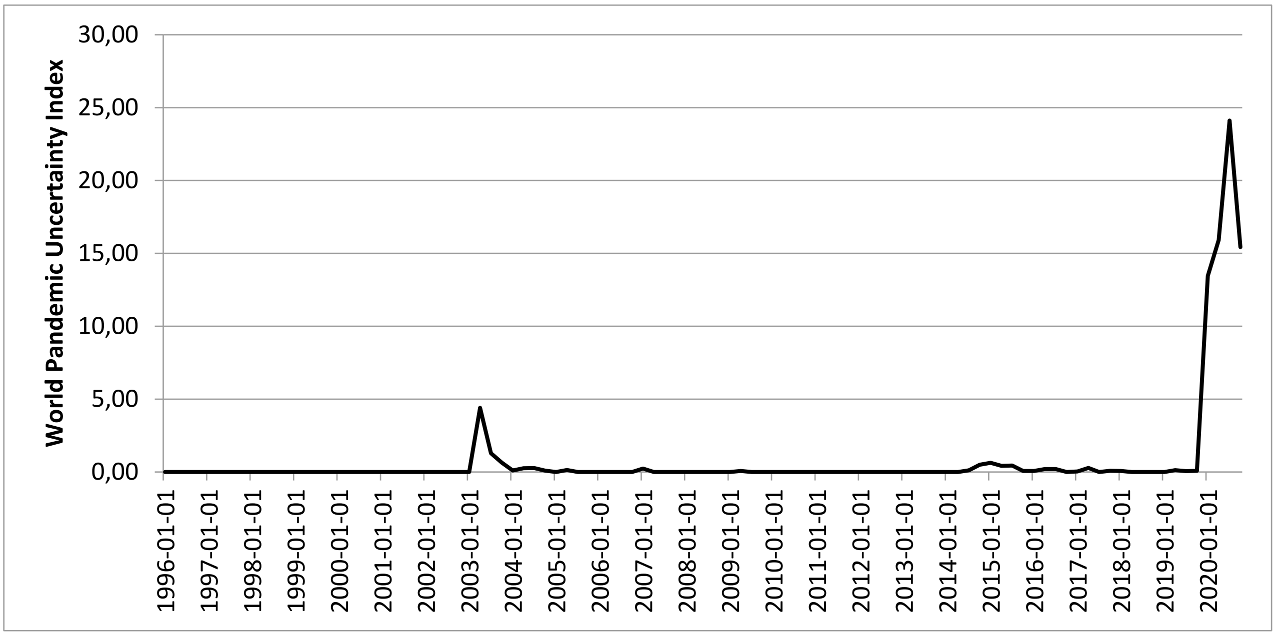

Figure 3: Own illustration based on the World Pandemic Uncertainty Index, January 1, 1996-October 1, 2021.

The major uncertainty of the moment is not the pandemic itself but rather how an endemic situation will play out globally. Lockdowns and restrictions of the past year have had economic and social ramifications causing a sense of insecurity. What is clear, is that closing economies is not a sustainable choice. The post-pandemic world will have to adapt by making behavioral changes. As economies open up, the world will adapt to a new way of living and working with the virus. These may include, to name a few, the surveillance of the virus and its mutants, therapies of both immunizations and booster doses, immunization verification, health education, protection measures in all areas of life, and working remotely. The next section takes a closer look at remote working and how it is affecting choices of home buyers.

Working remotely and lifestyle changes

[17] St Loius Fed (2021). World Pandemic Uncertainty Index. Retrieved February 19, 2021, from https://fred.stlouisfed.org/series/WUPI

The pandemic has brought on a digital transformation of society. Self-isolation was initiated and policed as a measure to protect citizens during the lockdowns in 2020. Employees were required to start working from home. Confined to the home space initiated a reconsideration and change in personal choices of how and where people want to live.

Remote working during the pandemic is here to stay in one way or another. It is realistic to assume that some of those who currently work remotely will continue to do so part-time or full-time even after the pandemic. In all but five states of the EU, 33-44% of all jobs can be conducted remotely. The new mode of remote working, though skewed toward white collar jobs, has spread to mid-level and clerical jobs.18 Well-known companies in the US like Google, Microsoft, and Facebook, among several others, have policies in place that support the work-from-home ethic for their employees.

With fewer commutes and more space requirements, employees working remotely have started moving away from expensive urban areas to smaller cities. When people move to smaller cities, it indicates a lifestyle change - one where 'home' extends to walkways, waterfronts, greenery, educational institutions, and amenities that enhance the quality of life.

As people move away from urban centres, inventories of homes and offices increase, bringing down rents and prices there. This trend has been observed in specific cities. In a year-to-year comparison, rents in the cities of San Francisco and New York plunged 10% in 2021. Similarly, the demand for office space is predicted to fall between 10-15% in the US.19 These changes are more evident in the US than in the EU.

In 2020, home prices in Germany increased by 5% over the previous year. Prices in the ten largest urban areas in Germany increased by 8% over the previous year. In comparison, house prices in cities located relatively far from urban centres increased by only 4.3%20. House price trends in Germany reflect the high demand for homes in urban areas and the relative shortfall in urban construction, which meets only 70% of housing demand21. The effects of remote working on regional housing markets in Germany are not foreseeable. However, if remote working continues and expands, local and regional trends can be expected to become apparent for different regions and countries of the EU.

IV Conclusion

Since 2015, housing markets in the EU and other parts of the world have been trending upwards. Low interest rate policies of the ECB, like those of many other central banks, make borrowing easy, increase the demand for housing, and push up prices. This trend has solidified during the pandemic period. Further, government labor market policies of job retention and stimulus measures have supported employees and kept unemployment low. Governments have instituted moratoriums on mortgages, which have until now kept evictions and foreclosures at bay.

As immunizations increase, countries are poised to open up in this year. On the one hand, as economies strengthen, and assuming that political and social stability is maintained, demand will fuel growth, even if there are small increases in inflation. The ECB is expected to continue its low interest rate policies and national governments will support labor market policies in the interest of their citizens. All these factors will contribute to rising housing prices in the EU. On the other hand, as post-pandemic

[18] European Commission (2020). Teleworkability and the Covid 19 crisis: a new digital divide? Retrieved February 12, 2021, from https://ec.europa.eu/jrc/sites/jrcsh/files/jrc121193.pdf,

[19] Bloomberg (2021). `How work from home´ became `work from anywhere´. Retrieved February 12, 2021, from https://www.bloomberg.com/news/storythreads/2021-02-04/how-work-from-home-became-work-from-anywhere

[20] FitchRatings (2021). German home price data consistent with regional demand trends. Retrieved February 24, 2021, from https://www.fitchratings.com/research/uncategorized/german-home-price-data-consistent-with-regional-demand-trends-12-02-2021

[21] Ibid

recoveries are organized and legal moratoriums in the EU are lifted over the next years, foreclosures may play a crucial part in the downturn of housing markets.

The outcome on housing markets, though regionally different, will reflect which of the two effects turns out to be the stronger one.

Dieser Beitrag stellt die Meinung der Autorin dar und spiegelt nicht grundsätzlich die Meinung der Hochschule.

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