Model of the Property Cycle

Stakeholders Demand Side	*Motivator*
First Time Buyers (FTB)	Price minimisation
Professional investors	Rental yield (inverse of price)
Speculators	Capital gain (increase in price)

(One of these stakeholders is needed at the bottom of the buying chain to complete it)

Stakeholders Supply Side	*Motivator*
Home-owners	Price maximisation
Builders	Profit, in extremis survival
Lenders	Commission, in extremis risk limitation

Variables

House Price HP, transaction volume, rental yield, risk (real & perceived), interest rates ir (nominal, i.e. published mortgage rates; & real, i.e. house price inflation HPI minus published mortgage rates), time, expectations/confidence

	Results	Explanation, starting from the bottom of the cycle
1	↑ HP	An upward trend emerges: Professional investors start buying in response to rising rental yield (yield rises as price falls)
2	↑ HP ↑ volume -ve real ir (HPI>ir)	The upward trend is reinforced: Lenders loosen lending criteria as risk falls with rising prices (negative equity less likely) FTB see market turning and start buying Builders start cranking up production, but output delayed by long lead times
3	↑↑ HP (HP now incl. speculative element) ↑ real risk ↑↑ volume ↓↓ rental yield	The upward trend gains momentum and the seller's market becomes overheated: Speculators chasing capital gain see rising prices and start buying: self-reinforcing Lenders competing for business and media reinforce demand; HPI reinforced by estate agents – 'safe as houses' – as despite more new-build being made available, demand exceeds supply and builders have no incentive to lower prices. HPI maybe limited by rising nominal interest rates Desperate FTB bring forward purchases before prices get totally out of reach and they are condemned to long periods wasting 'dead money' on rent; often ending up with unsuitable homes
4	Expectation of HP crash ≈ HP +ve real ir (HPI<ir) ↓↓ volume	Demand falls rapidly: Professional investors left market as gross yield fell with rising prices FTB priced out of market by speculators with bigger deposits & more interest-only mortgages Speculators run out of sources of funds or attracted by better performing alternative investments Latter two maybe reinforced by rising nominal interest rates & media reports of 'unsustainable' housing market, and limited by regional variations, reports of 'sound fundamentals' & increasingly desperate lenders devising ever-more unusual & risky products targeted at marginal buyers Lack of buyers at bottom of chain makes chain formation increasingly difficult
5	HP volatile Downward price pressures	Suppliers struggle to respond: Home-owners try holding out for high prices, reinforced by estate agent optimism Limited by: builders with lots of stock still in the pipeline owing to long production lead times & who need to shift it to maintain cashflow Valuation issues emerge as price surveys differ in direction; estate agents try it on with inflated prices, knowing they can 'reduce' them later if they fail to sell, whilst builders of non-FTB property need FTB-type house prices to fall; sharp speculators inflate prices reported to lenders, who are unknowingly left with 100% equity Media reports inconsistent, reflecting price volatility and differing motivations & expectations
6	HP ↓ slowly ↑ perceived risk	A downward trend emerges: Contrary to reports of excess *latent* demand *on average*, *effective* demand is *now* low as most potential buyers expect prices to fall or are still priced out of the market, & the market enters over-supply. (Buyers require both confidence & money) Limited by: ignorant speculators who still believe property is a one-way bet, some impatient FTB snapping up 'bargains' after small price falls, possible cuts in nominal interest rates Only attractive houses sell: quality – or more accurately value-for-money – replaces quantity, buttressing reported average house prices Lenders, fearing negative equity, stop competing for business and start tightening lending criteria
7	↓↓ HP negative equity ↑ rental yield	The downward trend gains momentum: More forced sales from builders, speculators, auctions, movers, repossessions, families outgrown homes, people desperate to escape unsuitable homes, deaths & divorces set the going rate at new lows for other sellers Potential sellers either cut their often paper losses & pile into the market before prices fall any lower, or prepare for a long wait until prices regain their previous highs Reinforced by: media Little demand despite falling nominal interest rates as lenders afraid to lend, fearing negative equity, and FTB and professional investors expect prices to fall further. Unattractive houses fare even worse. Buyer's market for those who are prepared to buy and get the timing roughly right