



Spatial Economics Research Centre

Thursday, 22 May 2014

Is there a London Housing Bubble?

The [latest figures showing London house prices up 17%](#) in a year can only fuel speculation about whether London is experiencing a housing bubble.

[Tim Harford](#) and [Simon Wren-Lewis](#) have both provided thoughtful commentary on this in the last few weeks (as, I am sure, many others). I don't have anything much to add to the debate on whether there is a bubble. As Tim Harford makes clear, I'm not sure how we'd know. But, to some extent, it seems to me that all this debate about whether or not there is a bubble deflects attention from the more fundamental point: highly inelastic housing supply leads to both high prices and greater fluctuation in prices.

Indeed, the last time my colleague Paul Cheshire looked at the figures, the volatility of the UK housing market as a whole exceeded the volatility of the *most* volatile metropolitan market in the US (at the time, LA). The recent housing market problems in the US may have changed the relative volatility of a few metro areas short term - but with London growing at 17% it won't be long before we reclaim our 'crown'.

Highly inelastic housing supply adds to volatility because any increase in demand gets translated into rapidly rising prices. Whether that demand comes from income growth, lower mortgage rates, easier borrowing, foreign buyers or some other structural shift, the result is large increases in house prices. This, in turn, tends to feed back into demand as people come to expect capital gains. When structural factors shift in the opposite direction, or expectations change falling demand now translates into falling house prices. Result - high volatility.

Even in Simon Wren-Lewis' view of the world, where the underlying shift in demand reflects low expected yield on other assets (rather than a bubble), it's still the highly inelastic markets that will see the large capital inflows. At the very least, if supply was more elastic, this inflow of capital would lead to increased housing supply, lower longer run rents and more affordable housing.

Is there a bubble? Who knows? But let's try not to have arguments around that question detract from the far more fundamental question of what we can do to try to increase housing supply in the parts of the country where demand is high.

Posted by [Prof Henry G. Overman](#) on [Thursday, May 22, 2014](#)

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1 comment:



Ben Jamin' said...

High volatility correlates very highly with low property taxes.

This can easily be seen in the US, in States such as California vs Texas for example.

It's no coincidence that London, with similarly low taxes also has high volatility and high HP's.

4 June 2014 at 02:18

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