

House price growth remains stubbornly in double-digits

- Annual house price growth remains resilient in May, but monthly rate slows
- Latest rate rise will cool activity and price growth further
- Threats of higher rates should signal a warning to those stretching their finances
- Waiting time for HIPs grows longer

| Headlines | May 2007 | April 2007 |
|------------------------------|----------|------------|
| Monthly index * Q1 '93 = 100 | 359.2 | 357.5 |
| Monthly change* | 0.5% | 0.9% |
| Annual change | 10.3% | 10.2% |
| Average price | £181,584 | £180,314 |

* seasonally adjusted

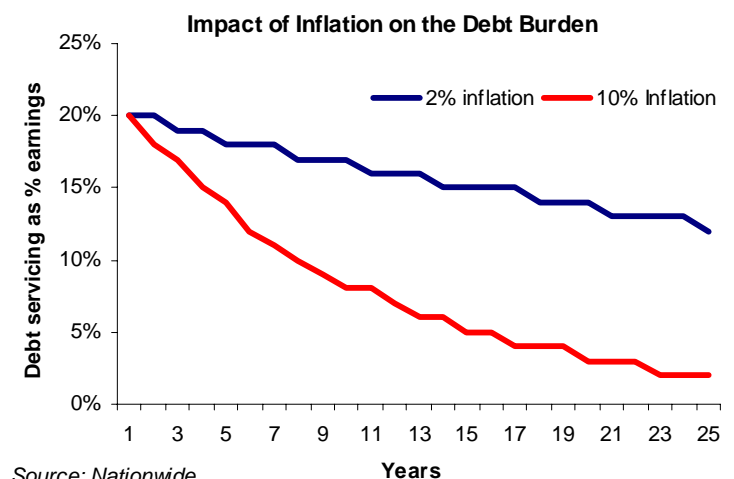
Commenting on the figures Fionnuala Earley, Nationwide's Chief Economist, said:

"House prices increased by 0.5% in May, down from 0.9% in April. However, the headline annual rate remained stubbornly in double-digits, largely due to slower house price inflation at this time last year. House prices increased by 10.3% during the year, bringing the price of a typical house to £181,584, almost £17,000 higher than at the same time last year. The underlying trend is still showing signs of slowing however. The three-month on three-month growth rate fell to 1.8% in May; its lowest level since August 2006.

"There was no surprise in the MPC's decision to raise rates by 0.25% at their May meeting, but there is still a question over whether we will see a further increase in rates or whether the effect of falling gas and electricity prices on the CPI will continue to dominate. The inflation forecast in May's *Inflation Report* was very similar to February's analysis, in spite of factoring in an additional rate rise, but it is clear that the MPC remains in hawkish mode, reinforced by the revelation that it actively discussed increasing rates by 0.5% at the May meeting. The MPC will not be willing to take the risk that growing inflationary pressures may be disguised by falling energy prices and the tone of the minutes suggest that they will move swiftly should more buoyant data come through. For this reason, along with the momentum in the financial markets for a further rise, we now expect that there is a strong chance that rates will be increased once more this year, to 5.75%. Higher interest rates clearly present risks to the housing market, but providing the economy, and particularly the labour market, remain in good shape, we should still be able to expect a measured cooling.

Higher rates should cause further caution among buyers

"The housing market is still showing signs of cooling and should therefore add little to the upside inflationary risks considered by the MPC. The three-month on three-month rate of growth still shows a clear downward trend as the effect of earlier increases in interest rates takes hold. However, higher interest rates, with the threat of more on the horizon, should signal caution to those thinking about stretching themselves to get a foot on the ladder. This is not only because of the level of debt in the short term, but also because, in a low inflation world, the real value of the



debt is not eroded as quickly. As a result the burden of servicing that debt remains heavier for much longer¹.

Why didn't 2003-4 history repeat itself?

"The last rate rising cycle in 2003-4 saw a rise of 1.25% in the bank rate from 3.5% to 4.75% in a period of 10 months.

Interestingly, demand in the market, as measured by the number of house purchase approvals, responded instantly to the increases in rates. Activity levels dived from a high of 132,000 house purchase approvals in November 2003, to a low of 76,000 three months after the last rise, a fall of 42% from peak to trough.

"In contrast, the first rate increase in this cycle in August 2006 had no impact on transactions levels at all. Demand continued to climb from 120,000 in the month of the first rate rise, to 128,000 by November. It required the rate increases in November and January to have any sobering effect on the numbers of approvals. But transactions were only reduced by 6% by March.

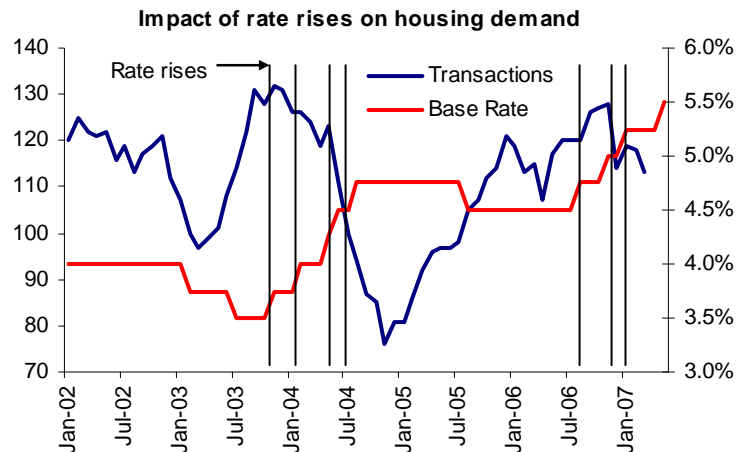
"The underlying momentum of demand may have had something to do with this but so too will the actual pricing of mortgages. In 2003-4 two-year swap rates – a good proxy for the cost of fixed rate mortgages - moved sharply upwards quickly raising the costs of fixed rate mortgages as well as variable rate loans. The rapid increase in loan costs choked off demand more quickly. In contrast the movement in swaps rates in this rate cycle has been much more modest and so keeping the cost of fixed rate loans down and allowing demand to continue stronger for longer.

"However, the last rise in rates and the financial market expectation of at least one more will dampen demand and buyers' expectations of further house price growth during the rest of 2007 and contribute to the slowing rate of house price growth.

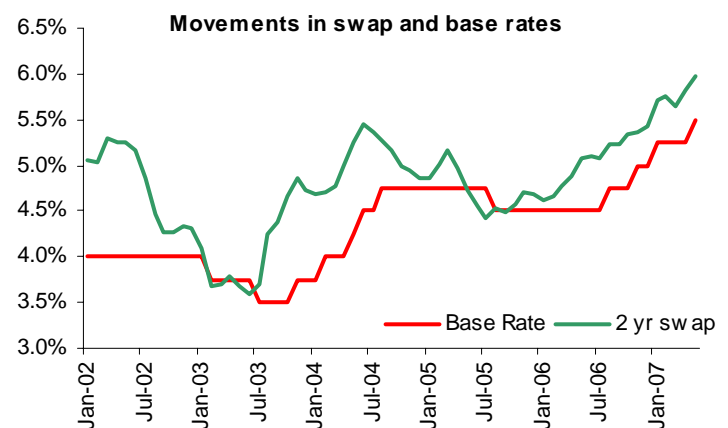
Longer waiting list for HIPs?

"There is some debate about whether the increase in the number of new instructions has been due to sellers anticipating the implementation of HIPs and thus trying to avoid the costs by marketing their property before the deadline. While there may have been some element of this, the picture will be further clouded by the Government's decision to dilute the regulation and delay its implementation to 1 August.

"Whether the implementation of HIPs in August will lead to a severe reduction in instructions is also unclear. Given that the cost of a HIP is estimated to be around £500, the cost itself is not likely to be



Source: Nationwide, Bank of England



Source: EcoWin

¹ Based on £100,000 loan at 5% equal to annual mortgage payment of £7,000. Income of £35K increased in line with 2% or 10% inflation

a big disincentive to sellers who wish to market their property seriously. Furthermore, as most of the information would have been required at a later stage in the transaction process anyway, the majority of the cost will simply be transferred from the buying to the selling stage in a property transaction. For those moving house, the additional cost will come only from the Energy Performance Certificate (EPC).

"The most recent increase in the number of new instructions could reflect a desire on the part of sellers to beat the regulations, but it might also reflect a desire by some to crystallise any property gains if they expect the housing market to be more vulnerable as a result of higher interest rates. In any event a larger number of properties for sale should help to dampen the level of house price growth further as some of the supply constraint is eased."

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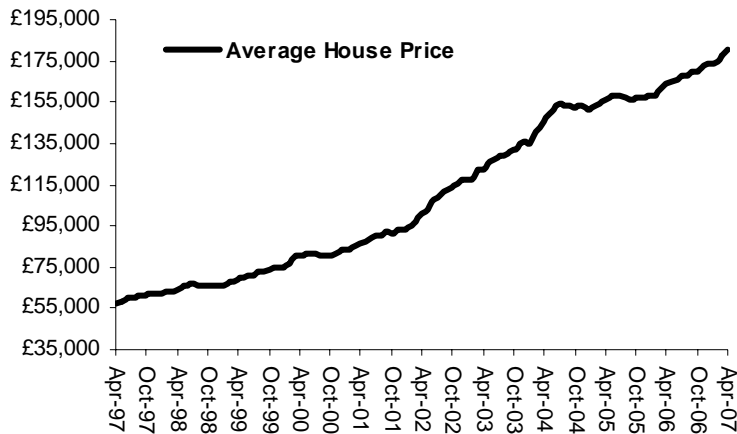
Notes:

Indices and average prices are produced using Nationwide's updated mix adjusted House Price Methodology which was introduced with effect from the first quarter of 1995. Price indices are seasonally adjusted using the US Bureau of the Census X12 method. Currently the calculations are based on a monthly data starting from January 1991. Figures are recalculated each month which may result in revisions to historical data.

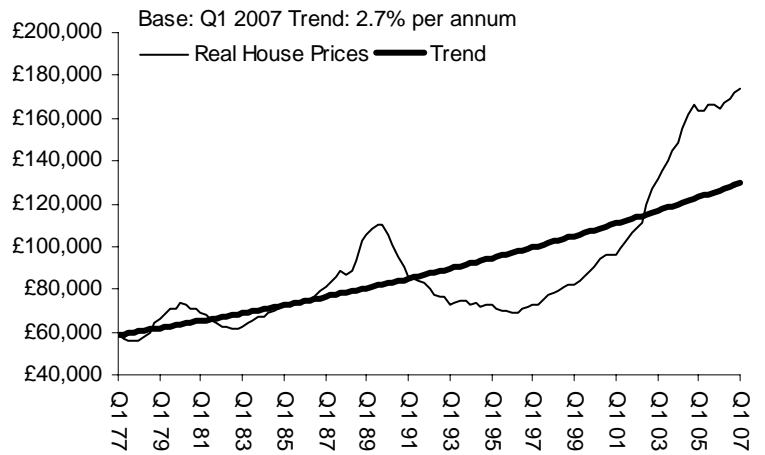
The Nationwide Monthly House Price Index is prepared from information which we believe is collated with care, but no representation is made as to its accuracy or completeness. We reserve the right to vary our methodology and to edit or discontinue the whole or any part of the Index at any time, for regulatory or other reasons. Persons seeking to place reliance on the Index for their own or third party commercial purposes do so entirely at their own risk. All changes are nominal and do not allow for inflation.

*** STRICTLY EMBARGOED UNTIL 7.00AM THURSDAY 31st MAY 2007 ***

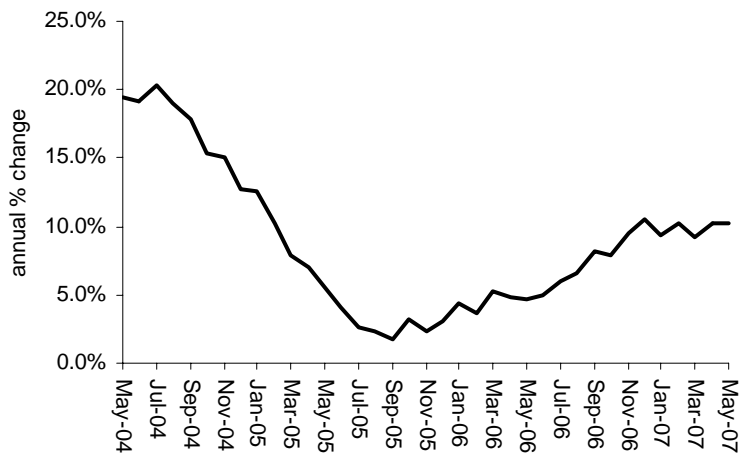
Average UK House Price



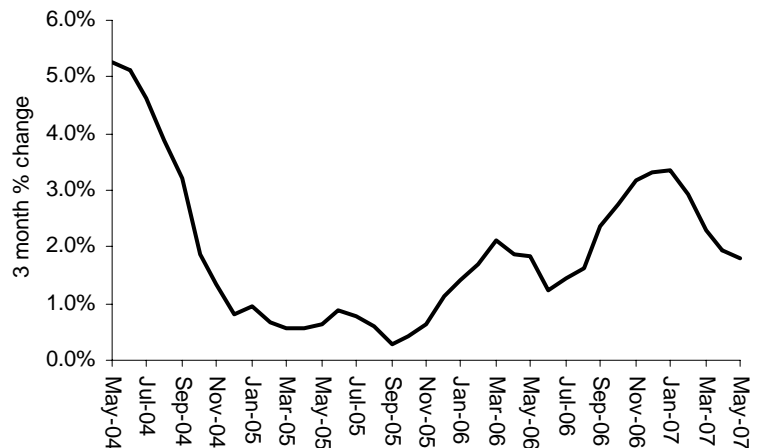
Long Term Real House Price Trend



Annual % Change in House Prices



3 months on previous 3 months % change



Historical Data

| Month | Monthly Index Q1 93 = 100 seasonally adjusted | Monthly Change % | Latest 3 months on previous 3 months % change | Monthly Index Q1 93 = 100 not seasonally adjusted | Annual Change % | Average Price £ |
|----------|---|---------------------|---|---|--------------------|--------------------|
| 2006 May | 325.7 | 0.4 | 1.8 | 328.4 | 4.7 | 164,632 |
| Jun | 327.2 | 0.5 | 1.2 | 330.6 | 5.0 | 165,730 |
| Jul | 330.3 | 0.9 | 1.4 | 334.6 | 5.9 | 167,733 |
| Aug | 332.9 | 0.8 | 1.6 | 334.6 | 6.6 | 167,721 |
| Sep | 337.3 | 1.3 | 2.4 | 338.0 | 8.2 | 169,413 |
| Oct | 340.0 | 0.8 | 2.7 | 338.4 | 8.0 | 169,623 |
| Nov | 344.7 | 1.4 | 3.2 | 343.5 | 9.6 | 172,185 |
| Dec | 349.0 | 1.2 | 3.3 | 346.6 | 10.5 | 173,746 |
| Jan | 350.4 | 0.4 | 3.4 | 345.6 | 9.3 | 173,225 |
| Feb | 352.7 | 0.6 | 2.9 | 348.5 | 10.2 | 174,706 |
| Mar | 354.4 | 0.5 | 2.3 | 353.3 | 9.3 | 177,083 |
| Apr | 357.5 | 0.9 | 2.0 | 359.7 | 10.2 | 180,314 |
| 2007 May | 359.2 | 0.5 | 1.8 | 362.2 | 10.3 | 181,584 |