RESIDENTIAL RESEARCH

Knight Frank

LONDON RESIDENTIAL REVIEW

AUTUMN 2017

THE DEMAND RECOVERY | THE THREE-TIER LETTINGS MARKET | BREXIT AND FINANCIAL SERVICES

KEY FINDINGS

6%
Year-on-year rise in transaction numbers between January and August

24%
Year-on-year increase in the volume of transactions in Chelsea between January and June

28%
Year-on-year increase in the number of transactions in prime outer London between Janaury and August

39%
Increase in the number of properties under offer in prime outer London at the end of H1 2017 versus H1 2016

TOM BILL
Head of London Residential Research

"Higher-value properties outperformed lower-value properties for the sixth consecutive month in August, demonstrating how the market is adapting to the changed fiscal landscape."

PRIME LONDON SALES MARKET INSIGHT

Despite the backdrop of political uncertainty following June's general election, some markets are adjusting to the new stamp duty landscape more quickly than others, says Tom Bill

Demand and transaction volumes in prime central London have continued to improve steadily in 2017 as asking prices come down, although the scale of these rises is not uniform across all markets.

A number of economic, political and policy factors have affected the market over recent years, not least the snap General Election, which weakened transaction volumes marginally over the summer.

However, deal volumes were up by 6% year-on-year between January and August as buyers and sellers increasingly assimilate higher rates of stamp duty, LonRes data shows. The number of new prospective buyers rose by 8% over the same period, according to Knight Frank data.

A separate analysis of Knight Frank and LonRes data shows Chelsea registered the largest decline in sales volumes in prime central London between the first half of 2014 and 2016 - a fall of 54% compared to an average of 38%. Underlining how some markets are recovering more quickly than others, transactions in this area climbed 24% year-on-year in the six months to June 2017, which was one of the biggest rises.

While there are clearly discernible signs of an improvement in activity, it is worth noting for historical context that sales volumes in PCL remain 10% below 2015 levels and 28% below the levels of 2014.

In terms of pricing, average values in prime central London fell 0.2% in August while on an annual basis the decline was 5.4%, the first time this measure has been above -6% since last November.

As with transaction levels, the pricing recovery is not taking place in a uniform manner and sensitivity to price remains high.

Price declines are moderating in all price bands, although some appear to have begun a process of bottoming out before others, as figure 1 shows.

Higher-value properties outperformed lower-value properties for the sixth consecutive month in August, demonstrating how the market is adapting to the changed fiscal landscape.

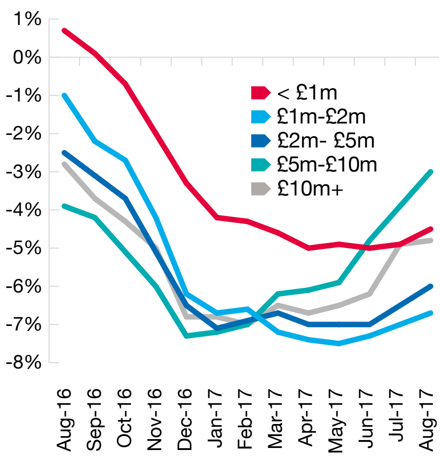
Prices between £5 million and £10 million were down 3.7% in the year to August 2017 compared to a decline of 5.4% across the whole PCL market, and a drop of 6.7% between £1 million and £2 million.

The last time there was a similar outperformance was in the second half of 2009, during the initial stages of the global financial crisis, when the safe haven appeal of the prime London residential market rose strongly.

Demand is also stabilising in prime outer London and an analysis of Knight Frank exchange data shows a 28% year-on-year rise in transactions between January and August.

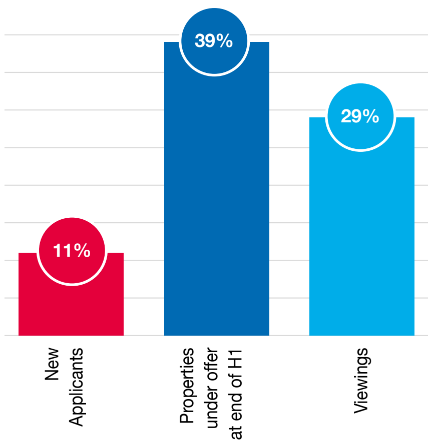
Average prices fell 2.2% in the year to August in prime outer London, although there were regional differences. The east London index rose 1.1% while the southwest London index declined 2.4%. Meanwhile prices across Knight Frank's north London offices fell 1.5%.

FIGURE 1
Growth bottoms out in higher price brackets
Annual growth by price band, last 12 months



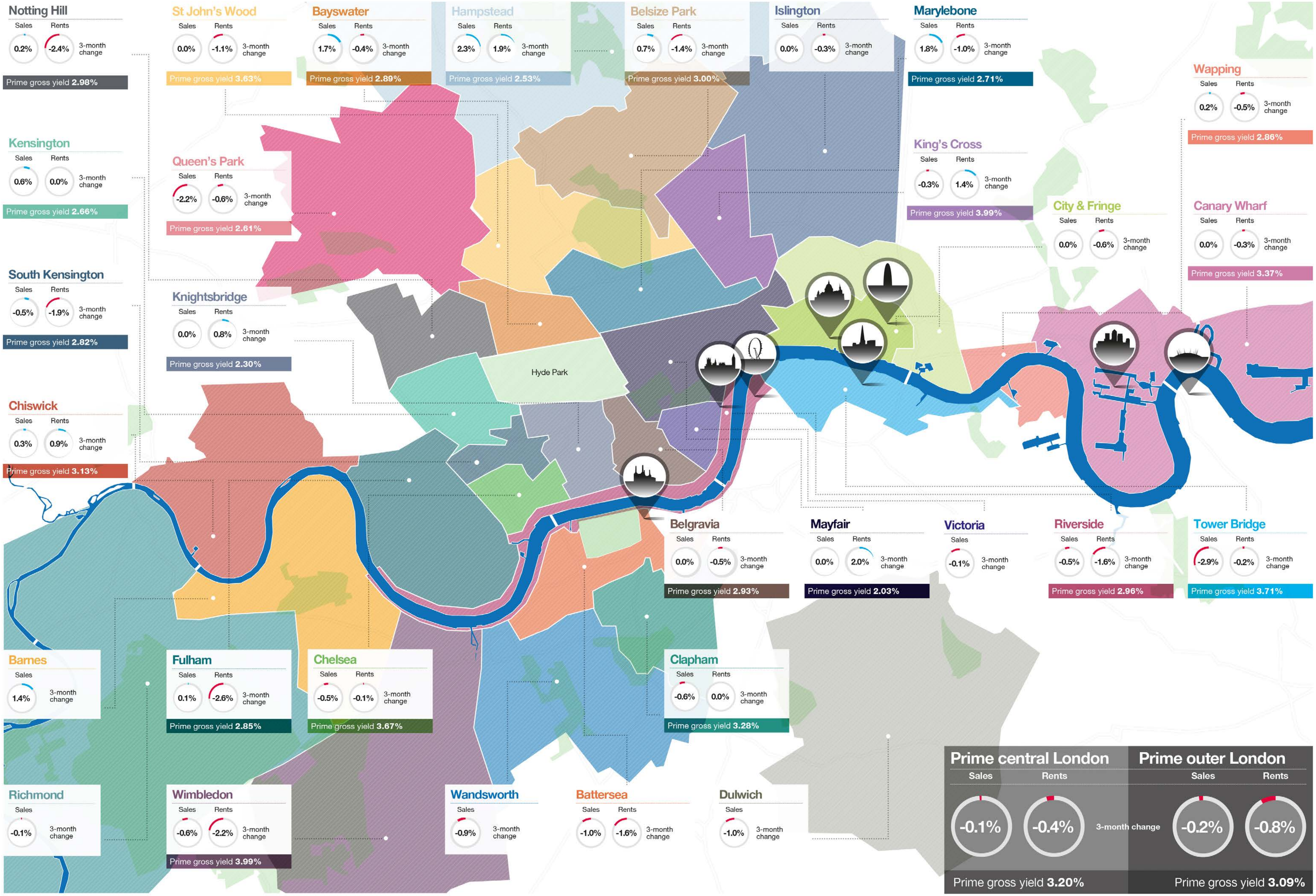
Source: Knight Frank Research

FIGURE 2
Demand indicators in prime outer London
H1 2017 vs H1 2016



Source: Knight Frank Research

PRIME LONDON PRICE AND RENTAL GROWTH, JULY **2017**



Area	Sales (3-month change)	Rents (3-month change)	Prime gross yield
Notting Hill	0.2%	-2.4%	2.98%
St John's Wood	0.0%	-1.1%	3.63%
Bayswater	1.7%	-0.4%	2.89%
Hampstead	2.3%	1.9%	2.53%
Belsize Park	0.7%	-1.4%	3.00%
Islington	0.0%	-0.3%	
Marylebone	1.8%	-1.0%	2.71%
Wapping	0.2%	-0.5%	2.86%
Kensington	0.6%	0.0%	2.66%
Queen's Park	-2.2%	-0.6%	2.61%
King's Cross	-0.3%	1.4%	3.99%
City & Fringe	0.0%	-0.6%	
Canary Wharf	0.0%	-0.3%	3.37%
South Kensington	-0.5%	-1.9%	2.82%
Knightsbridge	0.0%	0.8%	2.30%
Chiswick	0.3%	0.9%	3.13%
Belgravia	0.0%	-0.5%	2.93%
Mayfair	0.0%	2.0%	2.03%
Victoria	-0.1%		
Riverside	-0.5%	-1.6%	2.96%
Tower Bridge	-2.9%	-0.2%	3.71%
Barnes	1.4%		
Fulham	0.1%	-2.6%	2.85%
Chelsea	-0.5%	-0.1%	3.67%
Clapham	-0.6%	0.0%	3.28%
Richmond	-0.1%		
Wimbledon	-0.6%	-2.2%	3.99%
Wandsworth	-0.9%		
Battersea	-1.0%	-1.6%	
Dulwich	-1.0%		

	Sales (3-month change)	Rents (3-month change)	Prime gross yield
Prime central London	-0.1%	-0.4%	3.20%
Prime outer London	-0.2%	-0.8%	3.09%

KEY FINDINGS

7.2%
Increase in the number of lettings in H1 2017 versus H1 2016 across prime central and prime outer London

9.8%
The increase in lettings volumes below £1,000 per week over the same period

-39%
The saving in rent for a US tenant in 2017 compared to the equivalent property in 2008, following currency and rental value changes

34%
The increase in the number of new prospective tenants registering in H1 2017 versus H1 2016 in prime outer London

PRIME LONDON LETTINGS MARKET INSIGHT

Lettings volumes rose in the first half of 2017 but it was not a uniform pattern across all price brackets, says Tom Bill

The number of tenancies agreed across the prime London market in the first six months of 2017 was 7.2% higher than 2016 LonRes data shows, however there was no uniform increase across price bands.

The largest growth in demand remained below £1,000 per week, where the number of tenancies rose 9.8%. Over the same period, the number of super prime (£5,000-plus/week) tenancies increased to 56 from 47, a record for the first half of the year.

Below £1,000 per week, a figure that equates to a capital value of approximately £1.5 million, there has been a continuing acceptance of renting as a tenure model, in particular among younger tenants. The Knight Frank Tenant Survey shows they are likely to remain the largest group in the private rented sector until 2021.

The Survey shows that affordability constraints also curtail some tenants' plans for a house purchase, resulting in a longer stay in rented properties as they save for a deposit.

Demand in the super-prime lettings market is being driven largely by uncertainty over the short-term outlook for price growth, which remains linked to tax changes that include higher rates of stamp duty. This explains the growing number of high-value rental deals, according to Knight Frank's Head of Super Prime Lettings Tom Smith.

In a sign of this strengthening demand, there were 30 tenancies agreed above £10,000 per week in year to March 2017, which compares to 20 in the previous year.

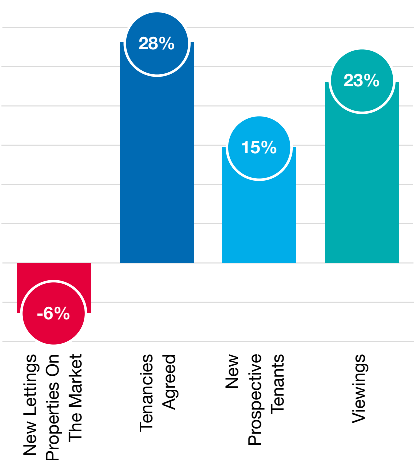
While there was an increase in the highest and lowest price brackets, there was a 6.5% decline between £1,000 and £5,000, highlighting how activity is relatively weaker in the mid-section of the market, where demand has traditionally been driven by senior executives.

As a result of political and economic uncertainty caused by issues that include Brexit, financial services companies and banks, which also face a range of regulatory pressures, have made large-scale cost savings.

However, despite any uncertainty caused by Brexit, the effect on the pound means renting has become relatively cheaper in London compared to other global financial centres. An American paying $1,000 per week for rental accommodation in 2008 is now paying the equivalent of $613 in London, after rental value declines and currency movements. The equivalent figure in Hong Kong is $792, while it is £848 in Singapore and $1,143 in Shanghai.

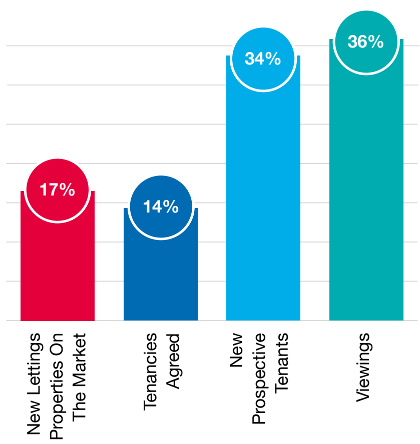
Demand across the London lettings market remains strong and Knight Frank data shows the number of new prospective tenants increased 24% in the first half of 2017. Meanwhile, the number of new rental properties, which grew 28% between the first half of 2015 and 2016, rose by 8% in the first half of 2017 across prime central and prime outer London. Slower growth in supply potentially indicates that some owners have become more attuned to lower pricing in the sales market and are removing stock from the rental market to attempt a sale.

FIGURE 3
Supply and Demand in the Prime Central London Lettings Market
Jan-June 2017 versus Jan-June 2016



Source: Knight Frank Research

FIGURE 4
Supply and Demand in the Prime Outer London Lettings Market
Jan-June 2017 versus Jan-June 2016



Source: Knight Frank Research

MACROVIEW THE IMPACT OF BREXIT ON DEMAND

The last several months have brought a general election result that few predicted and the formal start of Brexit negotiations.

It is no surprise that political uncertainty dominated a RICS report in July analysing the performance of the UK residential market.

While the prime London property market is no exception to this rule, when reflecting on the likely impact on pricing, it should be remembered that it has already faced political headwinds for almost three years.

As we highlight on page 2, the assimilation of higher rates of stamp duty has aided a general increase in transaction volumes.

While the impact of Brexit on the financial services sector has the potential to influence the future performance of the sales and lettings market, there is little evidence to suggest London's role as a leading global financial hub will be materially affected in the way some had feared.

Despite headlines suggesting an exodus of bankers from London, the numbers involved are small compared to the total. Most announcements appear to be contingency planning or part of cost-cutting programmes that pre-date Brexit.

This sentiment was echoed by recruitment company Robert Walters in July, which said banks were continuing to hire "significant numbers" of people in London and that some banks had reversed publicly-stated relocation plans due to a lack of skilled labour and tighter labour laws in the EU and the fact that a weaker pound made hiring British workers relatively cheaper.

Elsewhere, bank Credit Agricole extended the lease on 150,000 square feet of office space in the City and Deutsche Bank signed a 25-year pre-let deal for 469,000 square feet in a sign of its commitment to London.

The deals come after the UK and EU have both struck pragmatic opening positions in relation to the future of euro clearing in London. Clearing represents an important part of the financial services industry in London and at this stage, the debate is focusing on regulatory oversight rather than the exclusion of London from euro clearing operations, which the financial industry does not want due to a potential adverse impact on costs.

An industry with the potential to drive demand in the prime London property market in the longer-term is technology.

Snapchat, Deliveroo and Facebook have all signed recent office leasing deals and tech workers in London now outnumber those in finance. Furthermore, the UK tech sector has received record levels of investment. In the first half of 2017, it received more than £1.3 billion of investment, which is more than any other six-month period in the last decade.

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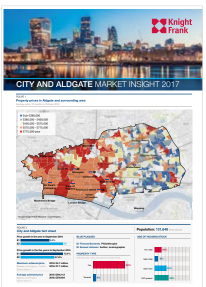
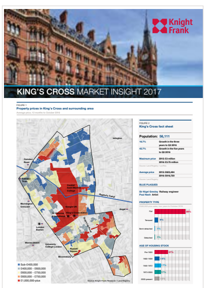
London Review Spring 2017



City and Aldgate market insight 2017

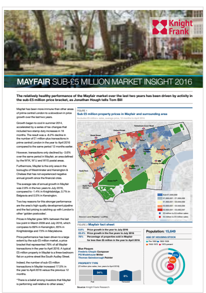


King's Cross market insight 2017

Riverside market insight 2017

Victoria and Westminster Market insight 2017

Martlebone market insight 2016



Mayfair market insight 2016

Prime Central London Rental Index June 2017

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