RESIDENTIAL RESEARCH

LONDON RESIDENTIAL REVIEW

SPRING 2019

PENT-UP DEMAND BUILDS | ASKING PRICES ADJUST | OUTPERFORMANCE VERSUS OTHER ASSET CLASSES

KEY FINDINGS

4.9
The ratio of new demand versus new supply in PCL in Q4 2018, the highest figure in four years

5%
The rise in the number of new prospective buyers during 2018 in PCL and POL

15%
The year-on-year decline in transaction volumes in 2018 in PCL

4.4%
The annual price decline in PCL in December 2018

PRIME LONDON SALES MARKET INSIGHT

The prime London property market is in a stronger position than it appears to be on the surface

The influence of political uncertainty on the prime London property market grew markedly over the course of 2018.

In the first half of the year there were signs the market was beginning to rally as asking prices adjusted more fully to reflect higher transaction costs.

Sales volumes in PCL were 7% higher in the year to March than the previous 12-month period, LonRes data showed. However by December, with Brexit uncertainty persisting ahead of the UK's planned departure from the EU in March 2019, volumes were down by 15% year-on-year.

Pricing behaved in a similar way. While the annual decline recorded in PCL in January was 0.7%, by December the decrease had widened to 4.4%.

Identifying individual factors affecting the performance of the prime London property market can be a complex task but the impact of political uncertainty was decisive during 2018.

Indeed, economic sentiment indicators displayed a similar trend. The Lloyds business barometer began the year with a reading of 35% in January but had fallen to 17% by December. Similarly, the Deloitte CFO survey fell from a net reading of +1 in Q2 to -30 in Q3 2018.

However, there are underlying signs that pent-up demand and the conditions for a recovery in the prime London residential market are building.

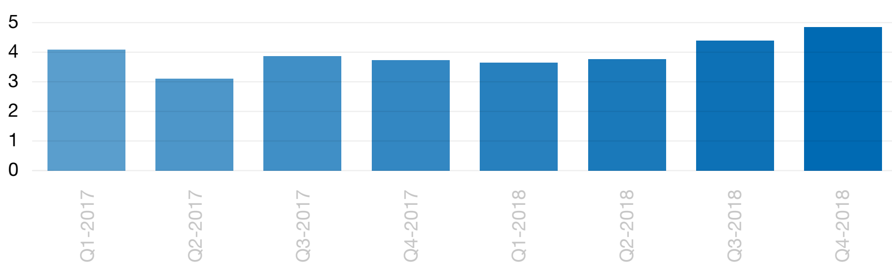
While the number of exchanges declined over 2018, the number of new prospective buyers registering rose by 5%.

Indeed, the ratio of new demand to new supply rose to 4.9 in the final quarter of 2018, the highest level in four years.

Meanwhile, the average number of days between listing and a property going under offer fell 2% in 2018 compared to the previous year as more appropriately-priced properties went under offer more quickly.

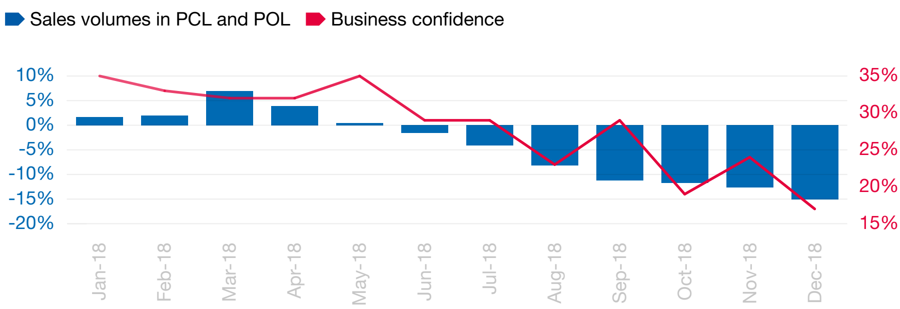
While it is unknown when the current level of political uncertainty will recede, the conditions for a recovery in the prime London property market appear to be taking shape.

FIGURE 1
New demand rises in relation to new supply Ratio of new prospective buyers/new listings in PCL



Source: Knight Frank Research

FIGURE 2
Sentiment dips in H2 2018 Annualised % change in sales volumes compared to business sentiment



Source: Knight Frank Research / Lloyds Bank Business Barometer

TOM BILL
Head of London Residential Research

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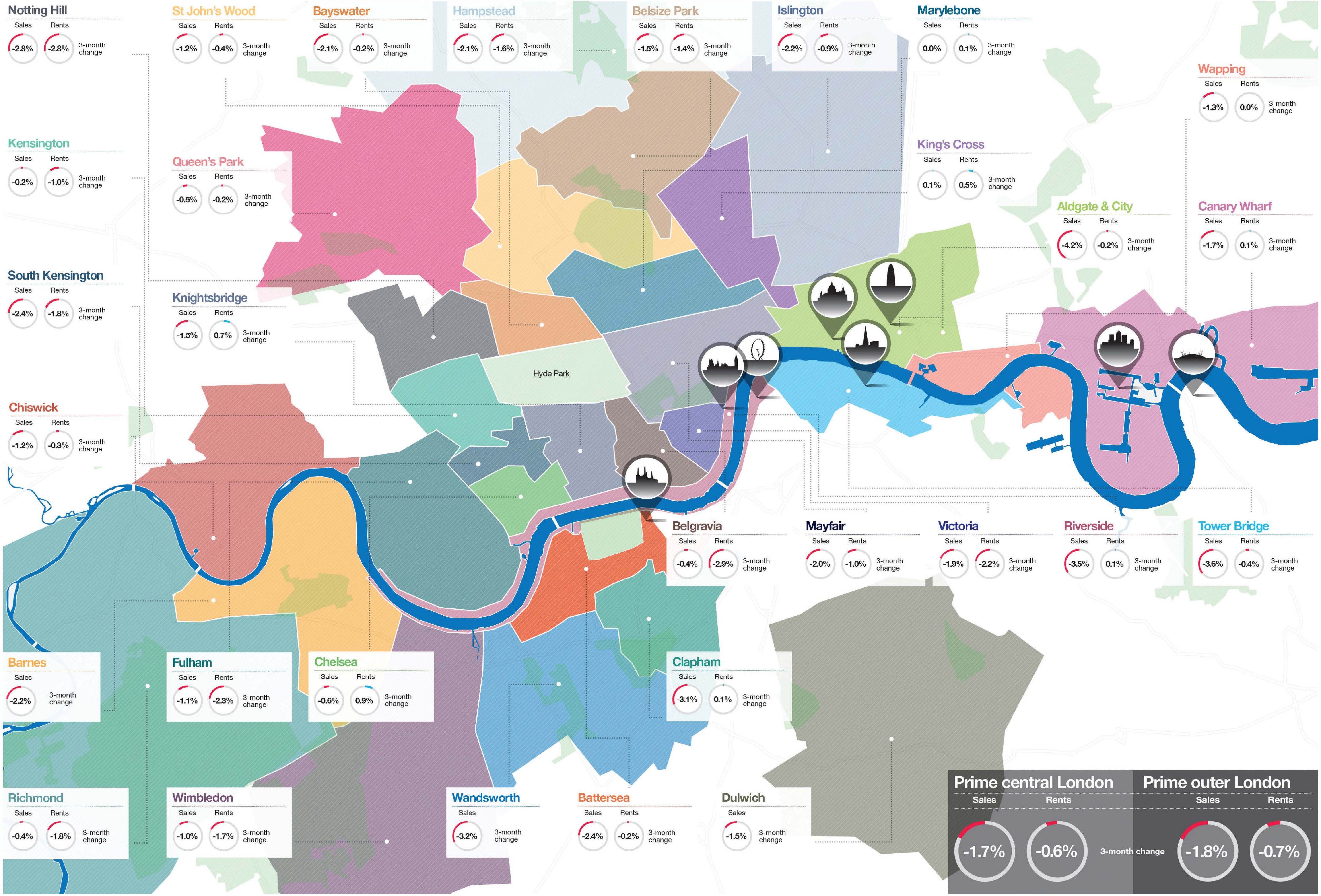
PRIME LONDON PRICE AND RENTAL GROWTH, DECEMBER 2018



3-month change

	Sales	Rents
Notting Hill	-2.8%	-2.8%
St John's Wood	-1.2%	-0.4%
Bayswater	-2.1%	-0.2%
Hampstead	-2.1%	-1.6%
Belsize Park	-1.5%	-1.4%
Islington	-2.2%	-0.9%
Marylebone	0.0%	0.1%
Wapping	-1.3%	0.0%
Kensington	-0.2%	-1.0%
Queen's Park	-0.5%	-0.2%
King's Cross	0.1%	0.5%
Aldgate & City	-4.2%	-0.2%
Canary Wharf	-1.7%	0.1%
South Kensington	-2.4%	-1.8%
Knightsbridge	-1.5%	0.7%
Chiswick	-1.2%	-0.3%
Belgravia	-0.4%	-2.9%
Mayfair	-2.0%	-1.0%
Victoria	-1.9%	-2.2%
Riverside	-3.5%	0.1%
Tower Bridge	-3.6%	-0.4%
Barnes	-2.2%	
Fulham	-1.1%	-2.3%
Chelsea	-0.6%	0.9%
Clapham	-3.1%	0.1%
Richmond	-0.4%	-1.8%
Wimbledon	-1.0%	-1.7%
Wandsworth	-3.2%	
Battersea	-2.4%	-0.2%
Dulwich	-1.5%	

	Sales	Rents
Prime central London	-1.7%	-0.6%
Prime outer London	-1.8%	-0.7%

KEY FINDINGS

1.1%
Annual rental value growth in December in PCL

3.35%
Average gross PCL yield in December, the highest in more than six years

3.5%
Average gross yield in POL in December, the highest in almost four years

PRIME LONDON LETTINGS MARKET INSIGHT

Rising rental values and declining sales values means yields have risen across prime London

Annual rental value growth turned positive in PCL last year due to declining levels of stock.

The supply of rental properties has been curbed by a series of tax changes as landlords attempt to leave the sector.

The number of new lettings listings in prime central and prime outer London was 13% lower in 2018 compared to 2017, Rightmove data shows. Meanwhile, the overall number of listings declined by 21%.

As a result of falling supply, annual rental value growth of 1.1% was recorded in prime central London in December, while the decline in prime outer London moderated to -0.2% from a figure of -4% at the start of the year.

Future legislative changes are likely to exacerbate this trend.

The tenant fee ban, which comes into effect in June this year, may further dissuade landlords from entering the sector or for current landlords it may mean that letting their property becomes a less cost-effective exercise. Additionally, there is also the possibility that any extra costs absorbed by landlords as a result of the ban will lead to higher rents.

There has also been speculation the government may introduce minimum three-year tenancy periods, which could have a similarly dissuasive effect on landlords who may not want an effective lock-up period on their investment.

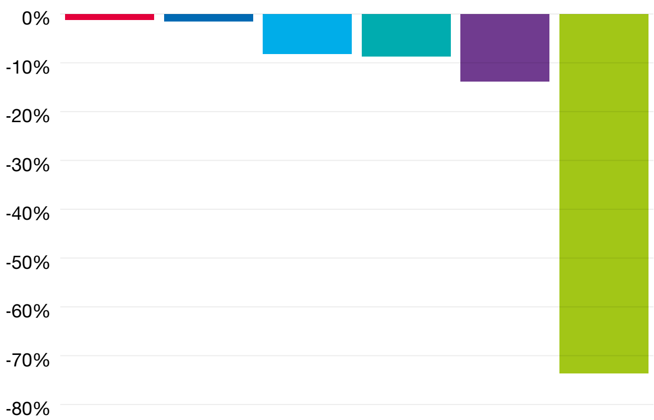
Despite this succession of legislative changes, the combination of strengthening rental values and declining sales values means that investment yields have risen in recent months.

An average gross yield of 3.35% in prime central London in December was the highest figure in almost seven years. Meanwhile, a gross yield of 3.5% in prime outer London was the highest in almost four years.

Indeed, total returns in PCL outperformed a range of other asset classes in 2018. A decline of 1.2% was relatively modest compared to a 8.7% decline in the FTSE 100 total return index, or a 14% decline in the S&P GSCI world commodity index and a 70%+ fall in the value of Bitcoin.

FIGURE 3
PCL rented property compared to other asset classes
Percentage change in 2018

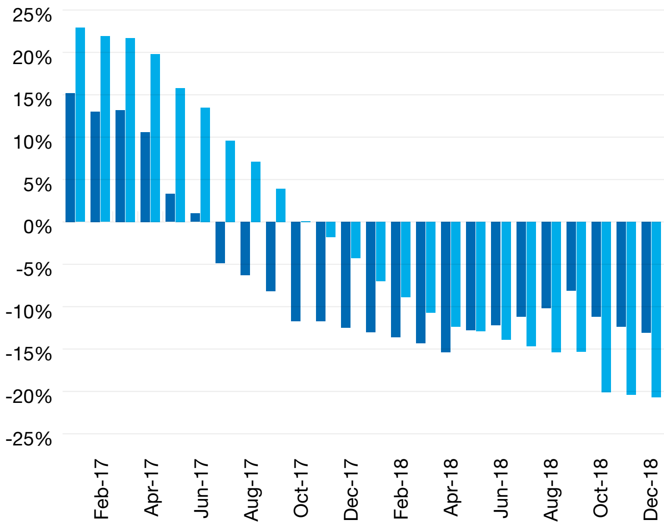
PCL
Gold
Global equity indices (MSCI mid and large cap total return)
FTSE 100 (total return)
Commodities (S&P GSCI, total return)
Bitcoin



Source: Knight Frank Research

FIGURE 4
The number of lettings listings declines
Annualised % change

New listings (PCL and POL)
All listings (PCL and POL)



Source: Knight Frank Research / Rightmove

MACROVIEW THE RISK OF A DISORDERLY BREXIT

While political divisions have deepened in recent months, the central risk for the property market and the UK economy has remained the same – a disorderly exit from the European Union.

As we discuss on page 2, the uncertain political backdrop has had a discernible impact on activity and pricing in prime London property markets since the summer.

Following the large-scale rejection of Theresa May's Brexit deal by UK lawmakers, there have been a series of cross-party initiatives on the next steps. Combined with the fact that no majority has so far materialised on how to or whether to achieve Brexit, it means UK politics has become highly unpredictable.

Rarely has it been more difficult to second-guess the short-term trajectory of the market. At the same time, rarely has it been easier to identify such a dominant reason for market's current behaviour.

As the rhetoric rises, it appears the UK government believes amending its current proposal is the best way to achieve a consensus.

The presence of the Irish backstop in the withdrawal agreement remains the most politically sensitive topic for many Parliamentarians, who believe it is likely to give the EU excessive leverage in future trade talks. As such, it will be the key focus of scrutiny as the government attempts to find a deal that can be backed by a majority of Conservative MPs.

It should also be noted, however, that Parliamentarians have also increased their efforts to prevent a so-called "no-deal Brexit", which saw sterling strengthen in early January. Should a "no deal" exit become a remote scenario, this is likely to underpin trading activity.

Indeed, the overall impact on prime London property markets in the first half of the year will depend on how long it takes the government to achieve consensus, thereby avoiding the need for a more prolonged process that could introduce the uncertainty of a second referendum.

While the political backdrop remains volatile, record high levels of employment underline the resilience of the UK economy.

Interest rates are also likely to remain low due to the political uncertainty and falling inflation, which should help liquidity.

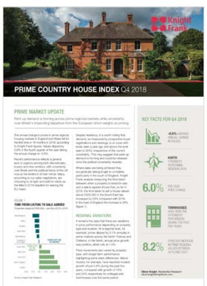
Furthermore, predictions for how many finance jobs would leave London as a result of Brexit have been systematically revised downwards to levels that will be more than compensated for by the arrival of new employees in the tech sector, underpinning future demand for prime London property.

The Wealth Report

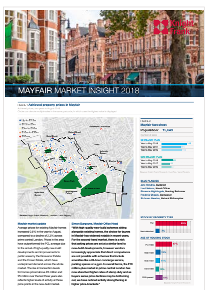
Prime London Sales Index December 2018

Prime London Rentals Index December 2018

UK Residential Market Forecast 2018



Prime Country Index



Mayfair and St James's Market Insight 2018

Richmond lettings Market Insight 2018

Bayswater lettings Market Insight 2018

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PLEASE GET IN TOUCH

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