UK RESIDENTIAL MARKET UPDATE

Knight Frank

NEW RATE REALITY

The Bank of England's base rate cut was accompanied by measures to encourage the effects of the cut to be passed straight to borrowers. Meanwhile UK house price growth remained steady, while average values in prime central London dipped again in July.

Key facts August 2016

Average UK house prices rose 0.5% in July, taking the annual rate of growth to 5.2%, up from 5.1% in June

Prime central London prices were 1.5% lower at the end of July compared to July 2015

Mortgage lending to first-time buyers rises to the highest level since 2007 in July

Bank of England base rates are cut **to a new record low of 0.25%**

GRÁINNE GILMORE
Head of UK Residential Research

"Buyers with access to a deposit can lock into ultra-low rates for years, helping boost the number of first-time buyers to a 9-year high in July."

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Economic and housing market overview

The Bank of England's rate-setting committee made its first move in more than seven years this month. Contrary to strong indications in the past, the move was not a base rate rise, but a cut to a new ultra-low rate of 0.25%.

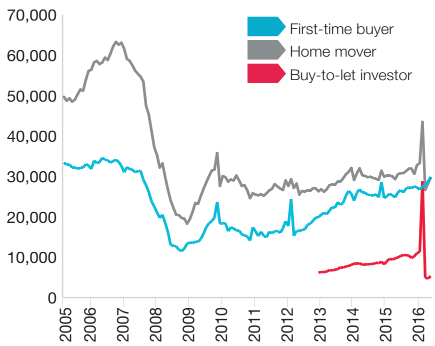
The central bank's move was accompanied by three other measures – an extension of quantitative easing, a scheme to purchase corporate bonds, and a Term Funding Scheme (TFS), which will allow banks and building societies who lend into the 'real economy' – to homeowners and businesses – access to even cheaper money.

The rate change came in the wake of closely-watched business surveys which suggested that the Brexit vote had delivered a knock to confidence, investment intentions and trading activity. However, the Bank's own verdict on the economy stopped short of forecasting a recession, although it did heavily revise down its GDP growth forecast for next year from 2.3% to 0.8%. It also expects unemployment to rise.

While the moves by the Bank of England seem to echo those taken after the financial crisis, there is one big difference. Banks are now much better capitalised than in 2008 and 2009, so there is still an appetite to lend. After the financial crisis there was an abrupt withdrawal of credit.

Mortgage lending by type

Number of mortgage deals



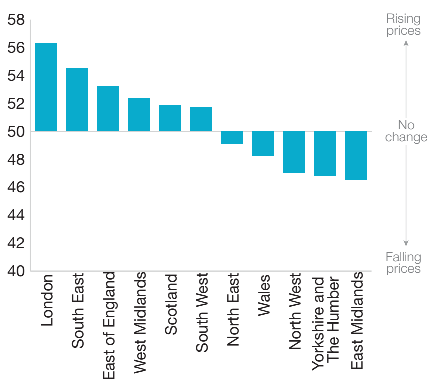
Source: CML

In fact, the rate cut means that mortgage rates, some of which are already at record lows, could edge slightly lower. This could further encourage buyers, especially first-time buyers with access to a deposit, as they can now lock into rates which will guarantee low monthly rates for years. This is underlined by new data from the CML showing the number of mortgages taken out by first-time buyers in July rose to the highest level since 2007.

In terms of price growth, the data from the housing market reflects the regionalised nature of the market. Prices are slipping in prime central London, while annual growth remains steady in the rest of the UK.

Expectations for house prices

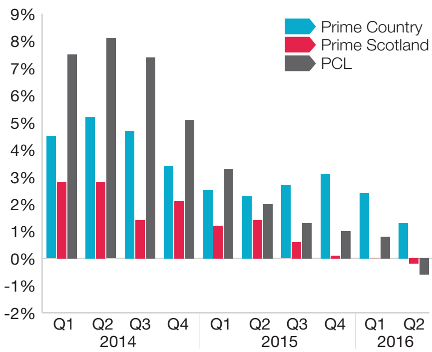
By region, HPSI



Source: Knight Frank Research/ IHS Markit

Prime price growth

Annual % change in PCL, Scotland and the prime country market



Source: Knight Frank Research

However, it will probably take another few months for the data to price in the scale of any Brexit impact. There is more detail on all aspects of the residential and rural markets in Knight Frank's new Post-Brexit market update and Risk Monitor.

Prime market update

Average prices in prime central London fell by 1.5% over the year to the end of July, down from a recent peak of 8.1% in June 2014, although the headline figure hides areas of outperformance as shown on the map below. The decision to leave the European Union has provided a backdrop of short-term uncertainty that is affecting behaviour. However, the primary factor curbing demand, and prices, remains stamp duty.

In the prime country house market annual growth eased to 1.3% in the year to the end of June, down from a high of 5.2% in 2014. Prices slipped by 0.2% in the second quarter, just ahead of the EU referendum. However, since then transactions have largely continued while the number of viewings conducted is only slightly behind the same period last year.

Elsewhere, prime property prices in Scotland fell by 0.6% annually as the market continues to adjust to higher rates of taxation. Activity levels were up year-on-year, suggesting that underlying demand remains strong.

Rental market

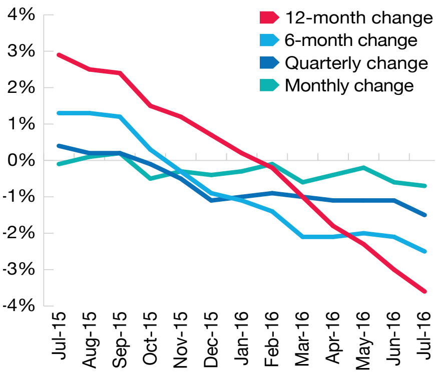
Average UK rents rose by 2.4% in the year to June, slightly down on the 2.5% growth seen in the year to May and the 2.6% reported in April. Rental prices increased in all English regions over the year to June 2016, with the biggest rise coming in the South East (3.4%).

Prime central London rents were down 3.6% on the year at the end of July, as higher stock levels and uncertainty surrounding the outcome of the EU referendum weighed on growth. This trend was mirrored in the Home Counties, where rents fell by 0.8% annually over the year to June.

But despite a decline in rental growth, the expectation is that activity levels will rise over the summer and into the autumn led by a pick-up in corporate demand from executives being relocated for work.

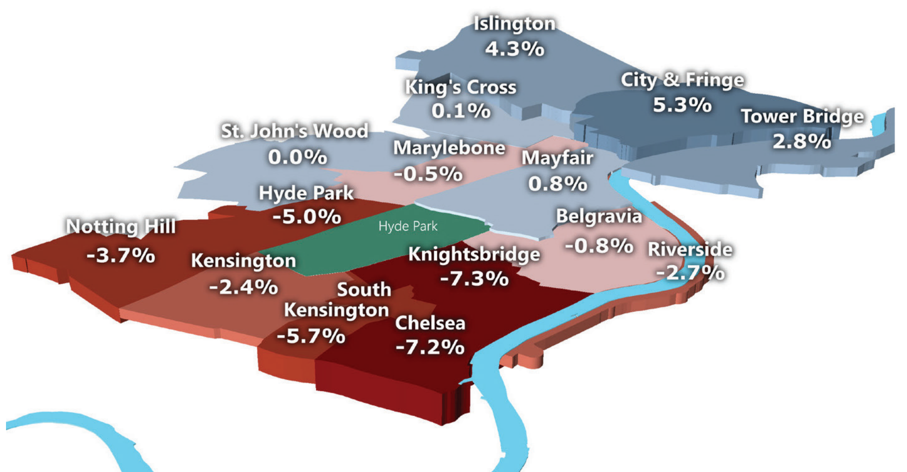
The number of tenancies started across London via Knight Frank's corporate relocation service increased 72% in the three months to the end of June compared to the same period in 2015, while in the Home Counties the number of enquiries from relocation agents in July was at the highest level all year.

Rental value growth in prime central London



Source: Knight Frank Research

Price growth in prime central London Year to July 2016



Source: Knight Frank Research

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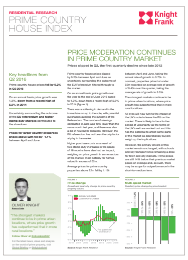
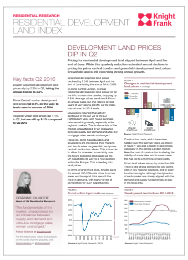


Prime Country House Index Q2 2016



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