RESIDENTIAL RESEARCH

PRIME CENTRAL LONDON SALES INDEX

GLOBAL ECONOMIC VOLATILITY COOLS DEMAND IN PRIME CENTRAL LONDON

Uncertainty in financial markets and domestic political concerns have moderated demand in prime central London, says Tom Bill

February 2016

Annual growth eased to 1% in February as prices fell -0.1% from the previous month

The half-year decline of -0.6% was the **weakest since June 2009**

Prices in the boroughs of Westminster and Kensington & Chelsea have **fallen by an average of -0.8% in the last year**

Asking prices are being lowered so that buyers feel they are getting value for money

Macro View: Brexit and the London property market

A combination of higher levels of stamp duty and volatility in global financial markets means demand for prime central London property has been subdued in the first two months of 2016.

In particular, the start of the year has been overshadowed by fears surrounding the impotence of central banks. Indeed, the prospect of negative interest rates triggered a fall in the share price of European banks and spread uncertainty in markets already digesting low oil prices and a Chinese economic slowdown.

Buyers have adopted a wait-and-see approach as the negative headlines in the business pages combine with domestic political uncertainty in the shape of a London Mayoral election in May and an EU referendum in June.

As we discuss in more detail in the Macroview section on page 2, uncertainty ahead of the EU vote is likely to produce a "Brexit" effect irrespective of the outcome.

As a result of these numerous imponderables, annual growth in prime central London eased to 1% in February after prices fell -0.1% from the previous month.

The half-year decline of -0.6% is the lowest rate since June 2009, as the market found its feet following the collapse of Lehman Brothers.

The 1% annual increase is skewed by the relatively stronger performance of eastern markets including Islington, City and Fringe and South Bank. Prime central London markets in the boroughs of Westminster and Kensington & Chelsea have fallen by an average of -0.8% over the last year.

In this highly price-sensitive market, asking prices are being reduced by 5% to 10% or more for buyers to feel they are getting value for money. This is less true for best-in-class properties located in the best prime locations, for which demand remains strong.

Stamp duty remains a live issue, though there has been added impetus ahead of a proposed change on 1 April that is likely to add three percentage points to the upfront cost of purchasing buy-to-let properties and second homes.

TOM BILL
Head of London Residential Research

"Buyers have adopted a wait-and-see approach as the negative headlines in the business pages combine with domestic political uncertainty"

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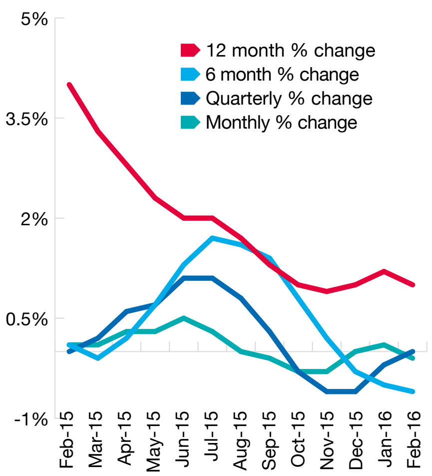
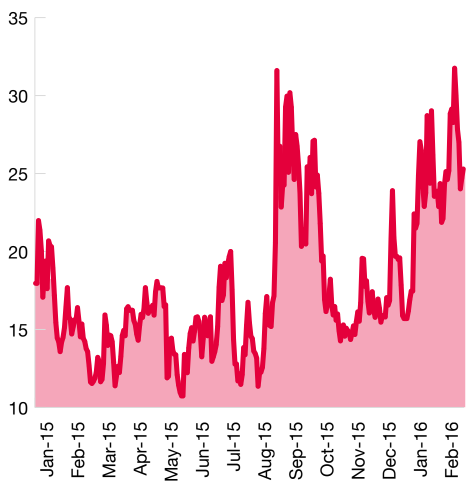
FIGURE 1
Price growth in prime central London



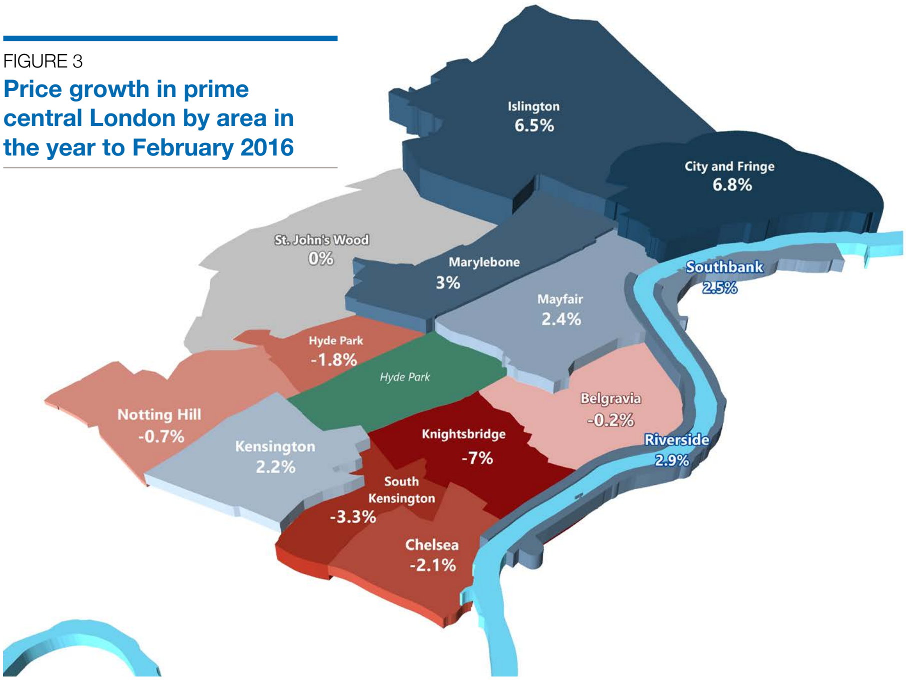
Source: Knight Frank Residential Research

FIGURE 2
Volatility on the rise
The FTSE 100 Volatility Index



Source: Knight Frank Residential Research

FIGURE 3
Price growth in prime central London by area in the year to February 2016



DATA DIGEST

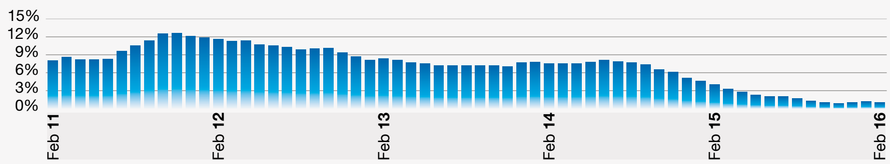
The Knight Frank Prime Central London Index, established in 1976, is the longest running and most comprehensive index covering the prime central London residential marketplace. The index is based on a repeat valuation methodology that tracks capital values of prime central London residential property. 'Prime central London' is defined in the index as covering: Belgravia, Chelsea, Hyde Park, Islington, Kensington, Knightsbridge, Marylebone, Mayfair, Notting Hill, South Kensington, St John's Wood, Riverside* the City and the City Fringe. 'Prime London' comprises all areas in prime central London, as well as Barnes, Canary Wharf, Chiswick, Clapham, Fulham, Hampstead, Richmond, Wandsworth, Wapping and Wimbledon.

* Riverside in prime central London covers the Thames riverfront from Battersea Bridge in the west to Tower Bridge in the east, including London's South Bank. The City Fringe encompasses the half-mile fringe surrounding most of the City including Clerkenwell and Farringdon in the west and Shoreditch and Whitechapel in the east.

THE MACRO VIEW FEBRUARY 2016

Prime Central London Index | **6,390.9**

Annual growth in prime central London over the last five years



BREXIT AND THE LONDON PROPERTY MARKET

Uncertainty surrounding the outcome of the EU referendum is the latest in a series of factors to affect the prime central London property market.

The UK faces four months of campaigning, headlines and polls that financial markets will use in an attempt to anticipate the outcome and move asset prices including Sterling.

However, the extent of the uncertainty in the run-up to the vote means the country is likely to experience a 'Brexit effect', irrespective of whether the country votes to leave the EU.

The uncertainty means investment decisions, including property, are more likely to be delayed until after the vote. Some predict a negative impact on the economy and Sterling weakened in the days after the date was set.

So, what if the country votes to leave? Hedge fund Toscafund analysed the issues surrounding what a 'Brexit' would mean but is dismissive of those who claim to fully understand the implications.

"I have as much confidence in claiming I know how many grains of sand there are in the Gobi desert as I do in asserting what the net cost to the UK might be were it to decamp the EU," said Toscafund chief economist Savvas Savouri, a view based on the unknown degree of isolation that a 'Brexit' would involve.

However, several short-term outcomes would be more likely than others until clarity emerged. In addition to a weaker Sterling, economic uncertainty may keep interest rates lower for longer, both factors that in more ordinary circumstances would be positive for the prime London property market.

London's dominance as a financial centre and its strengthening relationship with China would prove critical, Savouri argues, who believes the UK would be better off outside the EU.

"For China there is no plausible alternative and neither Frankfurt or New York will beat London for this hugely important and lucrative role."

He believes, however, that the likely result will be to remain in the EU. "My hunch is based on old fashioned human nature to opt for continuity over uncertainty."

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