RESIDENTIAL RESEARCH

PRIME CENTRAL LONDON RENTAL INDEX

This report analyses the performance of single-unit rental properties in the second-hand prime central London market between £500 and £5,000-plus per week. For an analysis of the build-to-rent market and the institutional private rented sector in London and the rest of the UK, please see our Private Rented Sector Update report here.

December 2016

Annual rental value growth **eased to -5.1% in December**

The number of new instructions fell -17% in November, the first decline in 2016

The number of tenancies agreed in November was 34% higher than the same month in 2015

Average prime **gross yield was 3.21%**

Macro View: The difficulty of assumptions in 2017

TOM BILL

Head of London Residential Research

"If the rate of new stock continues to slow, there could be a stabilising effect on rental values at the start of 2017"

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NEW SUPPLY SHOWS SIGNS OF RECEDING IN PRIME CENTRAL LONDON

High stock levels continue to put downwards pressure on rental values but the trend is showing early signs of a reversal, says Tom Bill

The prime central London lettings market in 2016 was marked by high stock levels and falling rental values.

The trend was caused primarily by an uncertain outlook for price growth in the sales market following a series of tax changes, which meant more vendors decided to let their property until greater clarity emerged.

Despite the seasonal slowdown, November 2016 was the first month that marked a reversal of this trend, suggesting rental value declines may be starting to bottom out.

Annual rental value growth last peaked at 4.2% in May 2015, the month of the UK general election, and has been on a downwards trajectory since then.

However, November saw a minor improvement, with rental value growth of -5.1% compared to a figure of -5.2% in October.

Falling rental values coupled with impending tax changes that will affect landlords in 2017 have had a dampening effect on new supply.

The number of new properties placed on the market in November fell -17% compared to the same month in 2015, which was the first year-on-year decline in 2016. If the rate of new stock continues to slow, there could be a stabilising effect on rental values at the start of 2017.

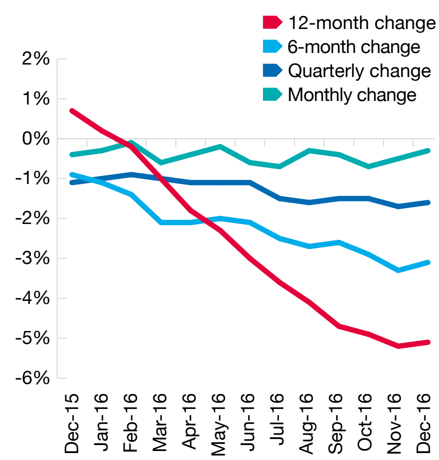
For now, however, prime central London remains a tenants' market due to the high levels of stock that came onto the market in 2016, primarily in higher price brackets.

Activity levels remained high as the Christmas holiday period approached. The number of tenancies agreed in November was 34% higher than the same month in 2015, which compared to a rise of 23.6% over the first eleven months of the year (figure 2). The number of viewings rose 17.8% between January and November, while new prospective tenants increased 6.9%.

Furthermore, despite ongoing weaker demand among company executives due to the uncertain global economic backdrop, many markets experienced an uptick in viewings and new prospective tenants ahead of the holiday period among executives who delayed acting until after the US general election.

FIGURE 1

Rental value growth in prime central London

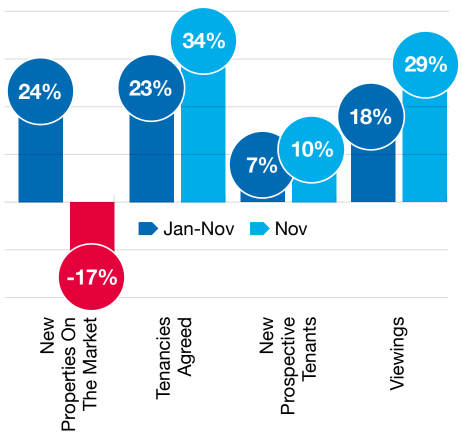


Source: Knight Frank Research

FIGURE 2

New supply falls while demand remains resilient

2016 versus 2015



Source: Knight Frank Research

FIGURE 3

Rental value growth in prime central London by area in the year to December 2016

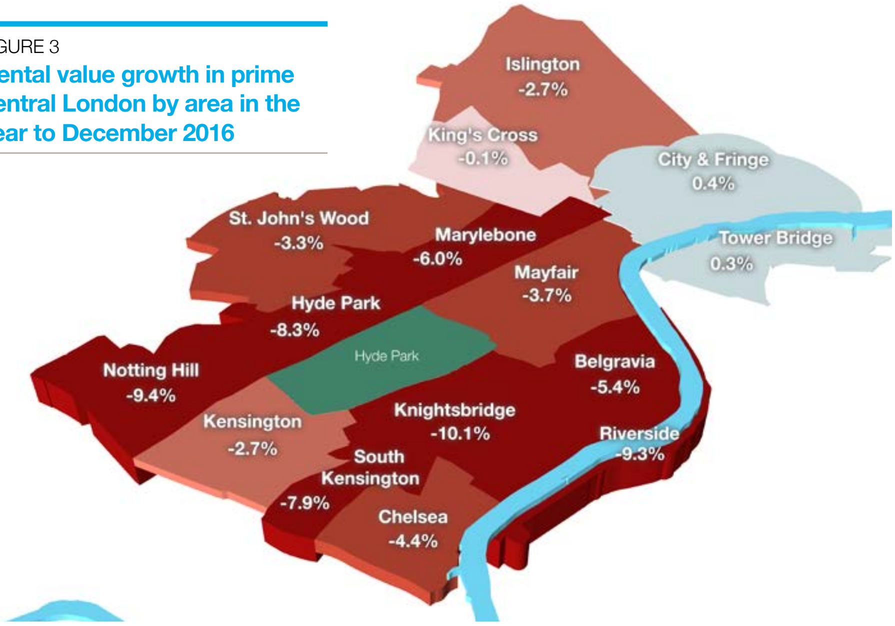


FIGURE 4

Rental value growth in prime central London by price bracket and property type, December 2016

Prime Central London Index **166.8**

	£250 - £500 pw	£500 - £750 pw	£750 - £1,000 pw	£1,000 - £1,500 pw	£1,500 - £2,000 pw	£2,000+ pw	Flat	House
1 month	-0.1%	0.7%	-1.0%	-0.7%	-0.6%	-0.6%	-0.3%	-0.5%
3 months	-0.5%	-0.5%	-1.5%	-2.6%	-2.6%	-2.0%	-1.4%	-2.0%
6 months	-0.8%	-1.8%	-2.2%	-4.5%	-4.5%	-4.1%	-2.6%	-4.3%
1 year	-1.2%	-2.3%	-5.3%	-8.1%	-6.5%	-6.6%	-4.5%	-6.8%
YTD	-1.2%	-2.3%	-5.3%	-8.1%	-6.5%	-6.6%	-4.5%	-6.8%

THE DIFFICULTY OF ASSUMPTIONS IN 2017

Sales volumes in prime central London stabilised at the end of 2016 following a two-year period during which buyers and sellers absorbed a succession of tax changes.

The extent to which market activity normalises next year is difficult to assess due to the shifting political and economic backdrop.

Following the Federal Reserve's decision to raise the base rate in December and its signal there would be three rises in 2017, the dollar has strengthened against the pound, boosting the buying power of those denominated in US dollars and dollar-pegged currencies.

Fuelled by the expectation of a Trump stimulus package, there is a belief the dollar will remain broadly strong versus the pound in 2017 while the Bank of England keeps rates low. However, assumptions about the strength of the dollar are linked to the wider potential for political uncertainty. For example, there are concerns a strong dollar could affect US competitiveness, which could increase the likelihood of trade tariffs and protectionism in the US and beyond.

Together with the prospect of continued Brexit-related volatility around sterling, anticipating the correct moment in 2017 to buy London property from a currency perspective is likely to remain high-risk.

Meanwhile, any assumption that the UK will start Brexit negotiations from a position of weakness will recede as economic self-interest takes precedence over shorter-term political motives, said Savvas Savouri, chief economist at asset manager Toscafund.

"There is a comprehensive lattice-work of cross ownerships connecting corporate fortunes between the economies of the EU27 and that of the UK," he said. "Consequently were tariff walls to be erected between Britain and the Single Market, a great many EU27 firms would be forced to reveal share price harming financial impairments; from horrible profit warnings to balance sheet damaging asset write-downs."

DATA DIGEST

The Knight Frank Prime Central London Index, established in 1995 is the most comprehensive index covering the prime central London residential marketplace. The index is based on a repeat valuation methodology that tracks rental values of prime central London residential property. 'Prime central London' is defined in the index as covering: Belgravia, Chelsea, The City& Fringe, Hyde Park, Islington, Kensington, King's Cross, Knightsbridge, Marylebone, Mayfair, Notting Hill, South Kensington, St John's Wood and Tower Bridge. 'Prime London' comprises all areas in prime central London, and in addition Canary Wharf, Fulham, Hampstead, Richmond, Riverside*, 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.

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