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.

RENTAL VALUE DECLINES BOTTOM OUT IN PRIME CENTRAL LONDON AS SUPPLY SLOWS

The final quarter of 2016 saw strong growth in lettings volumes, with activity particularly strong at the highest and lowest price points, says Tom Bill

January 2017

The decline in annual rental value growth **slowed marginally to -5% in January**

There was a 5% year-on-year increase in the number of super-prime deals in 2016

There was a 12% year-on-year increase in the supply of new lettings properties in the final quarter of 2016

Average gross prime yields **were 3.22%**

Macroview: Banks and a hard Brexit

Rental value declines in prime central London continued to moderate in January, as the rate of supply of new available rental properties slowed.

While there was a 12% year-on-year rise in new rental properties in the final quarter of 2016, that figure was lower than the increase of 30% recorded over the first nine months of the year.

Accordingly, an annual rental value decline of 5% in January was marginally stronger than that seen in the previous two months, as figure 1 shows. Rental values have been declining since May 2015 in part due to higher levels of rental stock.

The fact landlords face a less favourable tax environment from April, has contributed to the slowdown in supply to some degree.

However, demand continues to strengthen, particularly at the higher and lower end of the prime central London market.

Above £5,000 per week, in the so-called super-prime section of the lettings market, demand remains strong among tenants who are uncertain over the short-term trajectory of pricing in the sales market. The number of super-prime deals rose 5% in 2016 versus 2015, LonRes data shows.

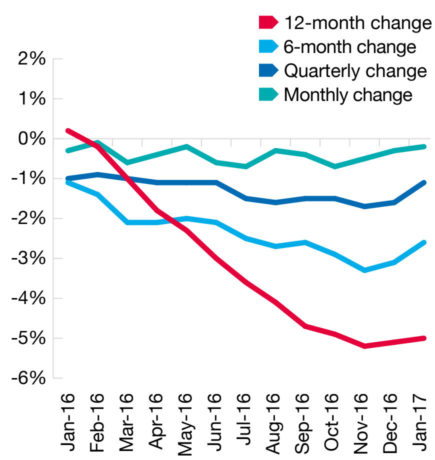
Activity is also relatively stronger below £1,500 per week, as the rental value data in figure 3 shows on page 2.

As figure 2 shows, the number of tenancies agreed across prime central London was 20% higher in the final quarter of 2016 compared to 2015, which puts upwards pressure on rental values. For rental properties between £1,500 and £5,000 per week, activity is improving but remains comparatively slower. The primary cause is that budgets for senior executives at financial institutions have been reduced due to the wider mood of economic uncertainty.

While the UK's decision to leave the European Union has raised some questions over the status of London as a leading global financial centre (see Macroview section on page 2), this trend for greater efficiency pre-dates Brexit and relates to the increased regulatory pressures on banks as well as a low interest rate environment that curbs profitability.

FIGURE 1

Rental value growth in prime central London

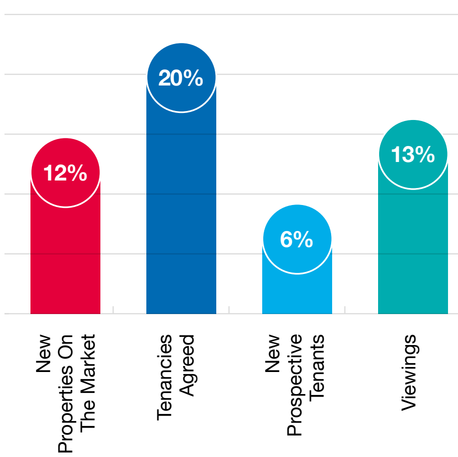


Source: Knight Frank Research

FIGURE 2

Lettings demand strengthens in PCL

Q4 2016 versus Q4 2015



Source: Knight Frank Research

TOM BILL
Head of London Residential Research

"Demand continues to strengthen, particularly at the higher and lower end of the prime central London market "

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MACROVIEW | BANKS AND A 'HARD' BREXIT

London-based banks have shifted their position in relation to Brexit in recent weeks.

Operating within the single market using so-called passporting rights has slipped down the agenda following a speech by Prime Minister Theresa May that signalled the UK would not seek to remain in the single market.

It comes as the financial services industry, which plays an important role driving demand in the prime central London sales and lettings markets, is already dealing with the twin issues of ultra-low interest rates and tighter regulation.

"The major banks were already streamlining their operations," said Andrew Breach, head of financial services at executive search company New Street, who is in regular contact with senior bankers in London and Europe.

While he expects Brexit to accelerate this process, he believes the impact should not be overstated.

"London has shown over the centuries that it is resilient and flexible enough to remain the number one or number two financial centre in the world. The plan will be to retain as many staff in London as possible but I would anticipate somewhere between 10% and 20% of staff could be affected, although it depends a lot on the negotiations."

There are also practical barriers to moving large numbers of staff away from London, he said.

"A bank can announce that it plans to move 1,500 people but it may only end up moving 500 because not everyone will want to uproot their life. Also, these are people with 10 or 15 years' experience who cannot easily be replaced, which could lead to staffing shortfalls in Europe."

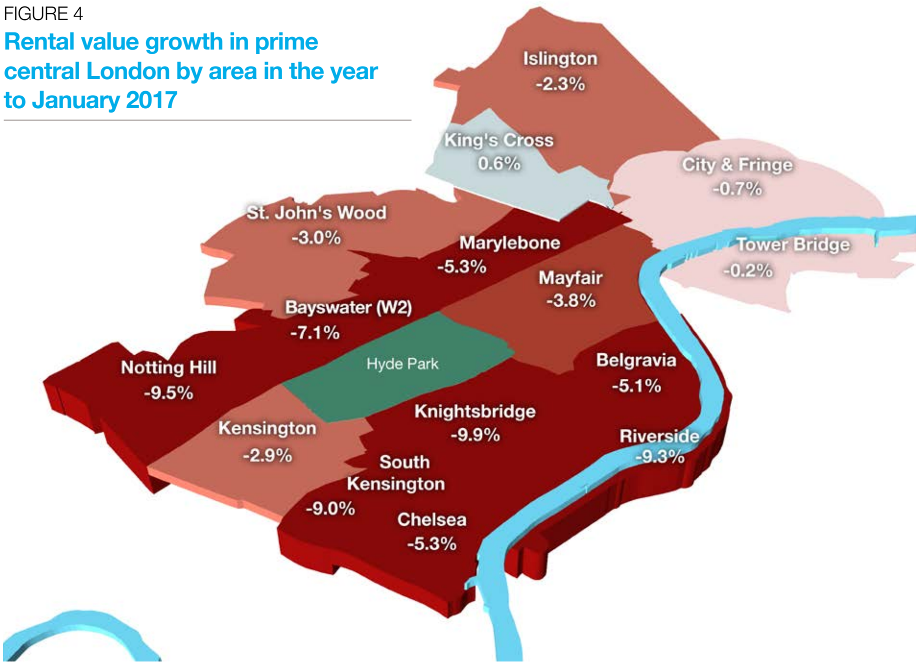
"Compliance and risk is one of the hottest markets in London for staff at the moment but you can't suddenly create that sort of knowledge elsewhere, and these are people that banks must have".

FIGURE 3
Rental value growth in prime central London by price bracket and property type, January 2017

Prime Central London Index **165.8**

	£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	0.2%	-0.1%	0.4%	-0.7%	-0.2%	-0.6%	-0.1%	-0.4%
3 months	0.1%	-0.1%	-0.7%	-2.0%	-1.7%	-1.9%	-1.0%	-1.4%
6 months	-0.3%	-1.6%	-1.7%	-4.0%	-3.3%	-3.6%	-2.2%	-3.5%
1 year	-1.1%	-2.4%	-4.6%	-8.1%	-6.0%	-6.7%	-4.4%	-6.7%

FIGURE 4
Rental value growth in prime central London by area in the year to January 2017



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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