RESIDENTIAL RESEARCH

Knight Frank

PRIME COUNTRY REVIEW

UK PRIME COUNTRY HOUSE MARKET

SPRING 2016

MULTI-SPEED MARKETS | THE COST OF UPSIZING AND DOWNSIZING | FARMLAND MARKET UPDATE

KEY FINDINGS

Prime country house prices rose by **2.4% over the year to March 2016**

Prices remain on average 13.6% below their 2007 levels, but there are notable variations dependant on property type, location and price

A growing number of **Londoners are trading the capital for prime regional markets**

The cost of **upsizing or downsizing by one bedroom is around £52,000** on average across England and Wales

OLIVER KNIGHT
Senior Analyst

"The moderation in price growth since 2014 reflects a greater sensitivity to pricing from buyers who continue to adjust to a different tax landscape."

MULTI-SPEED MARKETS

Prime markets in the UK have enjoyed a busy start to 2016. One of the key questions for the market is whether this momentum will be maintained for the remainder of this year.

Prices have been rising in the prime country house market for 13 consecutive quarters, the longest period of sustained quarterly price growth since before 2007.

But despite this relatively prolonged period of unbroken growth, prime property prices outside of the capital still remain 13.6% below their 2007 levels, on average. By way of comparison, London values are some 33% above their pre-crisis peak.

More recently, over the year to the end of March 2016 price growth in the prime markets outside of London has slowed to 2.4%, down from 5.2% in 2014.

The moderation in price growth reflects a greater sensitivity to pricing from buyers who are continuing to adjust to a different tax landscape. In some cases asking prices have had to be reduced to align with buyer expectations.

However, these headline figures do mask significant variations across the market.

The most active markets continue to be prime town and city locations with excellent transport links back to the capital which have been among the first to benefit from the ripple effect of demand out of London.

As regional economies continue to recover and the London housing market remains subdued more London buyers are likely to make the move out of the capital. Analysis of Knight Frank data shows this trend has already begun to gather pace. There was a 46% increase in sales to Londoners over the first quarter of 2016 compared to the previous year.

Following recent tax changes, demand has generally been concentrated on lower price brackets, something which is underlined by figure 2 below. Transaction volumes have slowed more markedly above £2 million across England and Wales since the change.

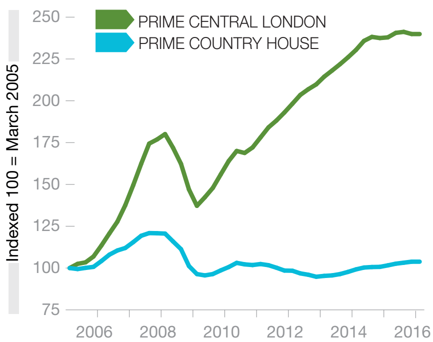
However, there are initial indications that the stamp duty increase in December 2014 is slowly being absorbed, with the higher transactional costs being factored into pricing at the outset. But taxation remains a live issue. The 3% surcharge for additional homes which came into effect from April means that prime second-home markets are likely to remain price sensitive.

Agents note that there was a spike in second-home sales ahead of the introduction of the additional levy.

Knight Frank forecasts prime price growth of 3.0% on average in 2016.

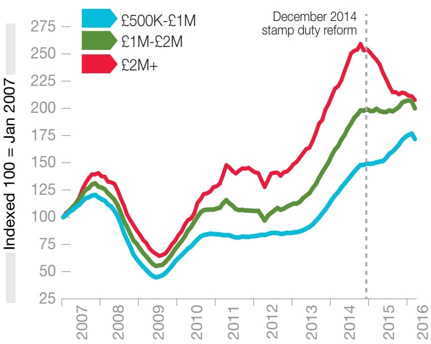
In the short term, uncertainty surrounding the outcome of the EU referendum could have an impact on the market, causing some buyers to adopt a wait-and-see approach until after the vote.

FIGURE 1
Price gap narrows



Source: Knight Frank Research

FIGURE 2
England & Wales sales volumes



Source: Knight Frank Research / Land Registry

URBAN MARKETS BOOSTED BY UPSIZERS AND DOWNSIZERS

Since the financial crisis there has been a growing trend towards living within thriving towns and cities other than London. This has resulted in prime urban properties outperforming their rural counterparts across the UK.

Across all the prime regional markets, urban properties are now on average 4.1% above their 2007 peak. This has been particularly evident in prime towns and cities including Bath, Oxford, Winchester and Cheltenham.

Demand is strong in these locations, in part due to the high concentration of prime housing stock and good schools which make them attractive to families looking to upsize, but also thanks to a growing number of equity-rich downsizers looking to move to areas where they can have access to a range of good restaurants, shops and amenities.

An important consideration for such buyers, however, is just how much extra it costs to move to a property with more bedrooms, or how much equity can be released by downsizing, especially given the fact that in some regional cities the price per sq foot can be similar to some London boroughs.

Looking at the latest average house price trends across the country, we have calculated that the cost of adding or removing a bedroom is around £52,000 on average across England and Wales.

This figure does not take into account the added costs associated with buying a property, including stamp duty.

The regional nature of the market means that in terms of costs and savings there are large variations depending on where households are based and where they are moving to, as well as the type of properties involved, as shown in figure 4.

We also acknowledge that the size and amenities of homes with more bedrooms will generally differ from those with fewer bedrooms, and this too will be reflected in the price.

For example, downsizing from a 5-bed detached house to a 3-bed terrace in the South East could release around £263,000 in equity, based on average property prices, while downsizing from a 4-bed to a 3-bed property in the West Midlands could release £45,000 in equity.

There are also notable differences in terms of property type. Moving from a 3-bed terraced house to a 4-bed terraced property in Yorkshire costs, on average, £38,000. Making that same move from a detached property to another detached property costs closer to £50,000.

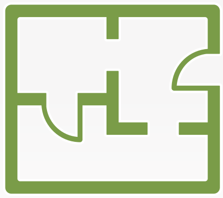
Costs are greatest in markets on the outskirts of the capital such as Elmbridge, St Albans and Guildford – perhaps unsurprisingly given average property prices tend to be higher in such locations. A full regional breakdown is shown opposite.

These markets have also been among the first to reap the benefits of the ripple effect of demand coming out of London. As regional economies continue to recover, more London buyers are expected to make this move.

46%

Increase in prime sales to Londoners over the first quarter of 2016 compared with the previous year

Source: Knight Frank Research



£51,939

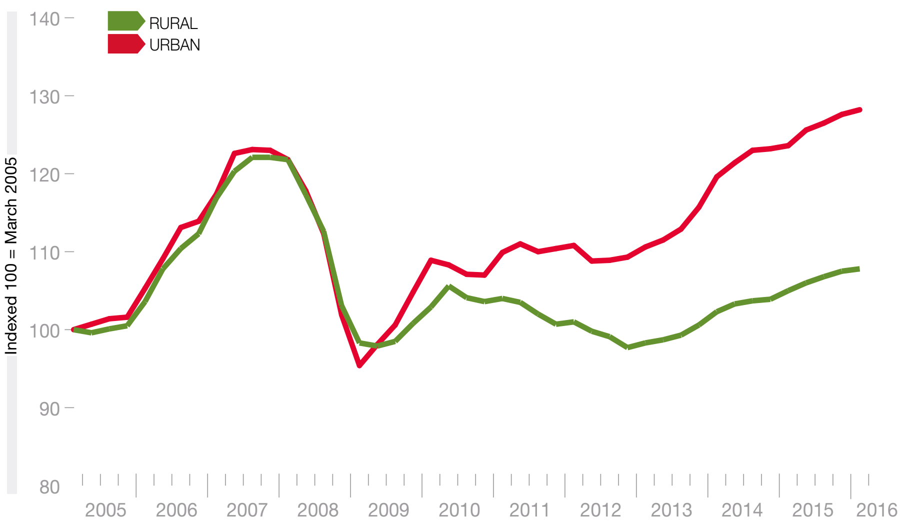
Average cost of upsizing or downsizing by one bedroom in England and Wales

Source: Land Registry

FIGURE 3

Prime urban outperformance

Prime urban v prime rural property price growth



Source: Knight Frank Research

FIGURE 4 **Average cost of upsizing or downsizing by one bedroom**

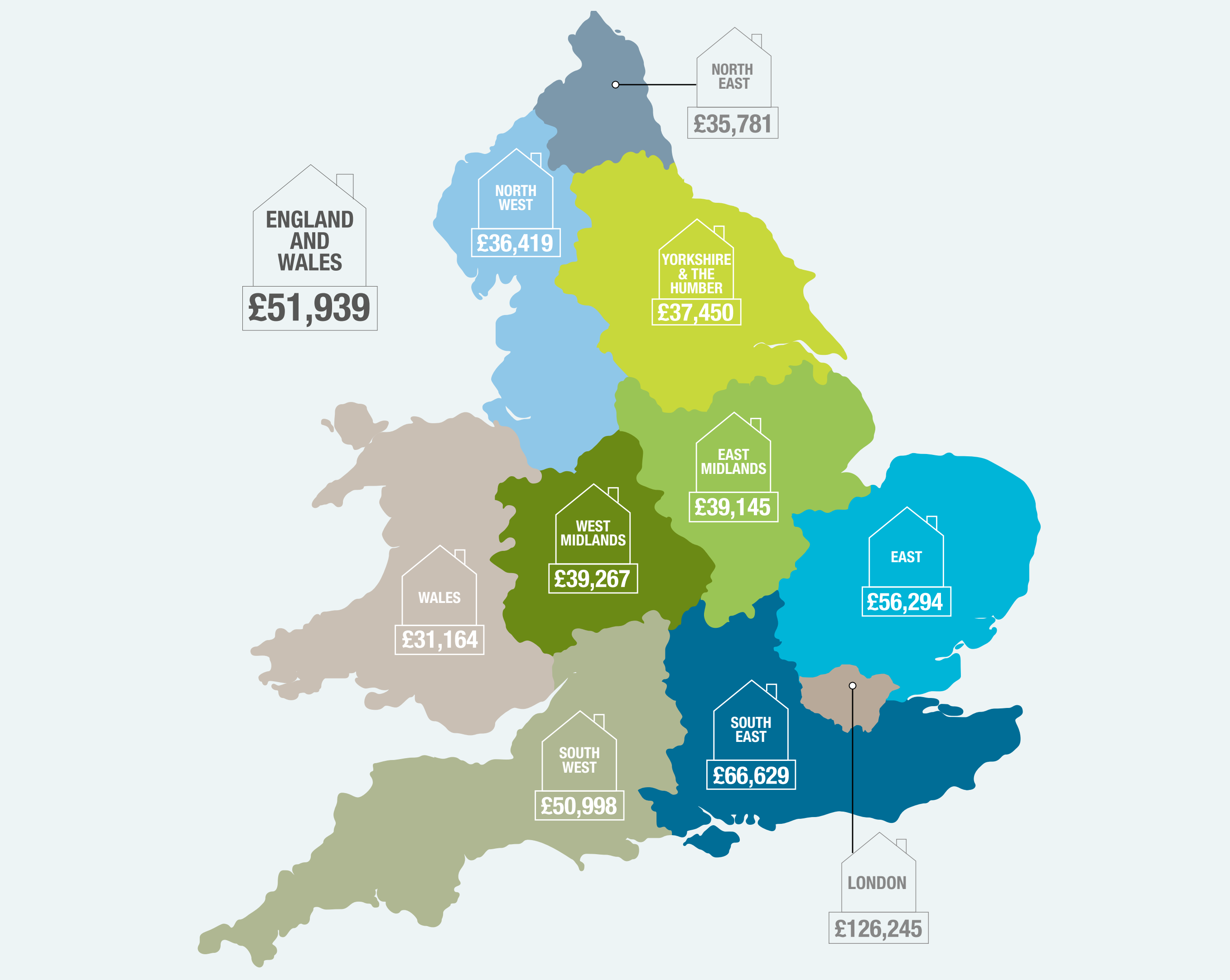


FIGURE 5 **Average cost of upsizing or downsizing by one bedroom: top five biggest uplift by region**

SOUTH WEST

Local Authority	Average cost
Christchurch	£103,730
East Dorset	£97,422
Cheltenham	£93,400
Cotswold	£87,481
Bath & North East Somerset	£85,112

SOUTH EAST

Local Authority	Average cost
Elmbridge	£173,774
Runnymede	£163,480
Waverley	£142,419
Guildford	£141,630
Mole Valley	£138,772

EAST

Local Authority	Average cost
St Albans	£153,001
Dacorum	£132,366
Brentwood	£128,260
Three Rivers	£117,241
East Hertfordshire	£114,361

EAST MIDLANDS

Local Authority	Average cost
South Northamptonshire	£92,589
South Kesteven	£87,817
West Lindsey	£82,862
Rushcliffe	£79,695
Blaby	£70,329

WALES

Local Authority	Average cost
Caerphilly	£55,195
Cardiff	£54,544
Monmouthshire	£51,331
Vale of Glamorgan	£50,151
Ceredigion	£45,090

NORTH WEST

Local Authority	Average cost
Rossendale	£91,883
Ribble Valley	£70,919
Trafford	£67,675
Stockport	£61,371
Warrington	£59,593

NORTH EAST

Local Authority	Average cost
County Durham	£59,435
Stockton-on-Tees	£55,033
Newcastle upon Tyne	£45,294
Sunderland	£41,930
Gateshead	£39,320

YORKSHIRE & THE HUMBER

Local Authority	Average cost
Harrogate	£88,069
Richmondshire	£59,822
Craven	£59,713
York	£58,499
Sheffield	£56,890

WEST MIDLANDS

Local Authority	Average cost
Stratford-on-Avon	£94,293
Warwick	£82,771
Solihull	£70,798
Birmingham	£61,213
Herefordshire, County of	£60,566

Source: Knight Frank Research

FARMLAND VALUES DIP AMID UNCERTAINTY

English farmland values fell by 3% in the first quarter of 2016 with average prices dropping back below £8,000/acre, according to the Knight Frank Farmland Index.

The drop was the largest quarterly decline since the 5% slide that occurred during the final three months of 2008, following the collapse of Lehman Brothers bank.

Given the significant issues weighing on the market at the moment, a period of readjustment is perhaps unsurprising. Agricultural commodity prices remain low with little prospect for a strong rebound in the short term, while the potential implications of a UK exit from the EU are adding further uncertainty.

When the vote was announced the feeling was that the "in" campaign was going to win the EU referendum relatively comfortably, but now the polls are predicting a much tighter result, with neither side of the argument yet to establish a convincing lead.

To put the drop in prices into context it should also be noted that the average value of farmland is still only £18/acre lower than it was at the end of 2014, and remains almost 180% higher than it was 10 years ago. And despite falling in the two quarters after the Lehmans' collapse, farmland values had recovered all of their lost value and more by the end of 2009.

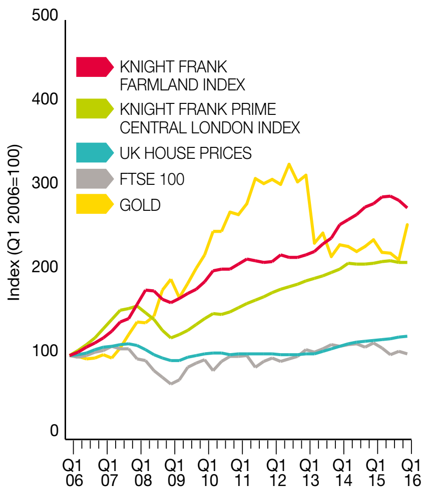
Predicting where values will head in 2016 and beyond is almost impossible until we know the results of the EU referendum in June. In the case of a Brexit much will depend on how Defra decides to replace the financial support provided the Common Agricultural Policy, and for how long it commits to providing the payments.

But if sterling weakens for a prolonged period as some analysts predict, this would make UK grain and meat more competitive on global markets. UK land, which is already cheaper than in some EU countries, may also become more attractive to international investors.

Whatever the outcome, we are still seeing strong demand from farmers who are either not reliant on EU subsidy payments or have taken the long-term view that expansion is the way forward for their businesses.

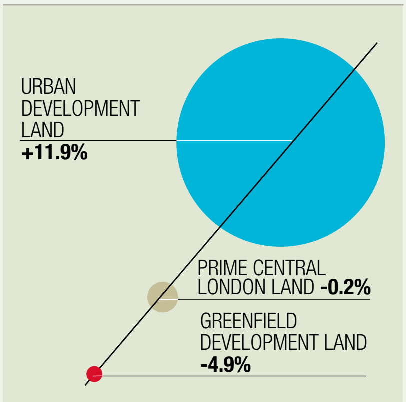
ANDREW SHIRLEY
Head of Rural Research, Knight Frank

FIGURE 6
Farmland 10-year performance vs other assets



Source: Knight Frank Research

FIGURE 7
Annual change in development land values, England 2015



Source: Knight Frank Research

Development Land

Outperformance in prime urban sales markets has also been mirrored in the performance of development site values.

The Knight Frank Development Land Index, which is based on the valuations of actual development sites around the country, shows that the cost of brownfield land in key cities rose by 2.5% in the final three months of 2015 taking annual growth for urban development land sites to 11.9%.

Like the sales market, this is well above the wider average. Greenfield development land prices have fallen by 4.9% year-on-year.

The price growth differential reflects the strengthening appetite for land among developers and housebuilders in regional urban hubs. This demand has picked up significant momentum in the last 12 months – lagging the pick-up in demand seen in the wider greenfield market two years ago.

Better local economic growth in key regional cities, coupled with more buyer confidence has resulted in a resurgence of development, and this is reflected in competition for good brownfield sites.

THE EU REFERENDUM AND THE UK'S PRIME HOUSING MARKET

A referendum on the UK's membership of the European Union has been a possibility since January 2013 when David Cameron pledged to hold a vote on the issue. This possibility became a certainty with the election of a majority Conservative government in May last year and the subsequent announcement that the vote will be held on June 23rd 2016.

Neither the "in" or the "out" campaigns have been able to establish a convincing lead, with recent polls predicting a tight result.

A key question for the UK's prime property market is just how much of an impact the vote will have, and whether a Brexit will have a significant impact on values and activity.

Pre-referendum

Without doubt, the referendum is creating uncertainty, and property markets of all types generally don't like this – potential buyers and vendors tend to sit on their hands waiting for clarity to return – similar to the slowdown we witnessed in the prime market in the run-up to the general election in 2015.

This could potentially lead to fewer residential transactions taking place as we get closer to the vote.

Post-referendum

There is no doubt that a clear "remain" vote would remove immediate economic uncertainty and market activity might be expected to recover any lost ground relatively rapidly. This was certainly the experience in Scotland following their referendum on independence.

On the other hand, a vote to leave will usher in a much longer period of uncertainty as the terms of our exit are finalised, trade treaties negotiated and, in the farms market, a new home-grown support scheme is developed by Defra to replace the Common Agricultural Policy.

Looking beyond the immediate settlement, an analysis of whether leaving the EU will result in a slow decline in the UK economy or herald a new expansionary future is beyond the ambitions of this article.

However, there is a fundamental reason to assume the impact on the UK housing market should be relatively benign whatever the outcome. The prime markets outside of London are primarily driven by domestic dynamics. An exit from the EU would not affect the demand/supply imbalance which is a key feature underpinning current housing market trends at all levels of the market.

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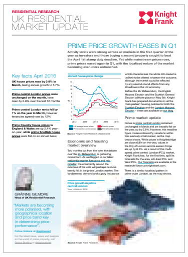

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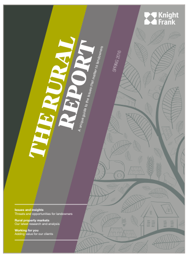

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