Early signs that rental market imbalance is ending

Sales market shows resilience in final months of 2022

Mini-Budget impact lingers

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London Residential Review

Q1 2023

PRIME LONDON SALES MARKET

Market resilient as mini-Budget shockwaves dissipate

The prime London sales market finished 2022 digesting the mini-Budget, and the sense of indigestion was more pronounced in some areas than others.

The cause was straightforward enough. Kwasi Kwarteng's mini-Budget took place more than three months ago, but mortgage rates have not yet resumed the path they were on in the middle of last year.

Financial markets took fright at the previous government's low-tax economic plan and borrowing costs spiked in anticipation of higher inflation.

This created a disorderly picture at the end of last year.

Some buyers had mortgage offers that pre-dated the mini-Budget and were motivated to move quickly.

Elsewhere, budgets were cut as monthly repayments rose. More discretionary buyers stepped back and waited for mortgage rates to come down, while others still need to move.

It means that until mortgage rates settle, the recalculation of budgets that will have to happen among buyers and sellers hasn't taken place yet. That will come this year.

Despite this, the property market in prime London postcodes proved resilient in the final quarter of 2022.

The fact cash buyers are more prevalent in higher-value markets will protect prices as borrowing costs rise.

The number of exchanges in November in prime London markets was 16.2% higher than the same month in 2021 and 15% higher than the five-year average.

However, buyers are understandably wary, particularly in lower-value markets where debt is used to a greater extent. (fig. 1). The number of offers made in Q4 was 12% below the five-year average, reflecting the uncertainty that has arisen from the spike in borrowing costs.

However, as the falling five-year swap rate shows, mortgage rates should continue to decline, which means the fall in offers made may have bottomed out.

Meanwhile, the number of offers accepted was 24% above the five-year average in Q4, which suggests the nervousness among prospective buyers does not mean sales volumes are about to fall meaningfully.

The resilience of prices in prime London property markets will be put to the test this spring when activity levels traditionally pick up across the UK.

Prices should remain in somewhat of a holding pattern until then, although the steeper monthly declines that followed the mini-Budget have now ended.

NOTED

24%
The increase in the number of offers accepted in Q4 versus the five-year average.

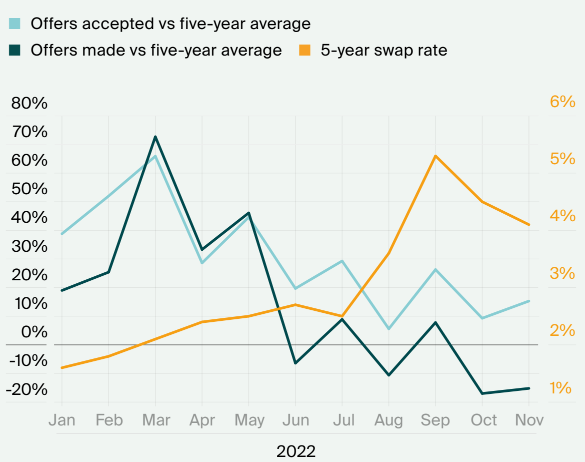
12%
The decrease in the number of offers made in Q4 versus the five-year average.

15%
The increase in exchanges in November versus the five-year average, suggests buyer nervousness doesn't necessarily mean a fall in transaction volume.

"The resilience of prices in prime London property markets will be put to the test this spring when activity levels traditionally pick up across the UK."

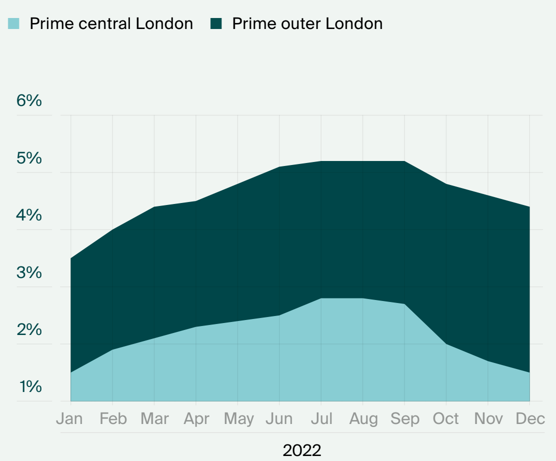
TOM BILL
HEAD OF UK RESIDENTIAL RESEARCH

1 Offers accepted steady as offers made faded



Source: Knight Frank Research

2 Prime London annual % price growth



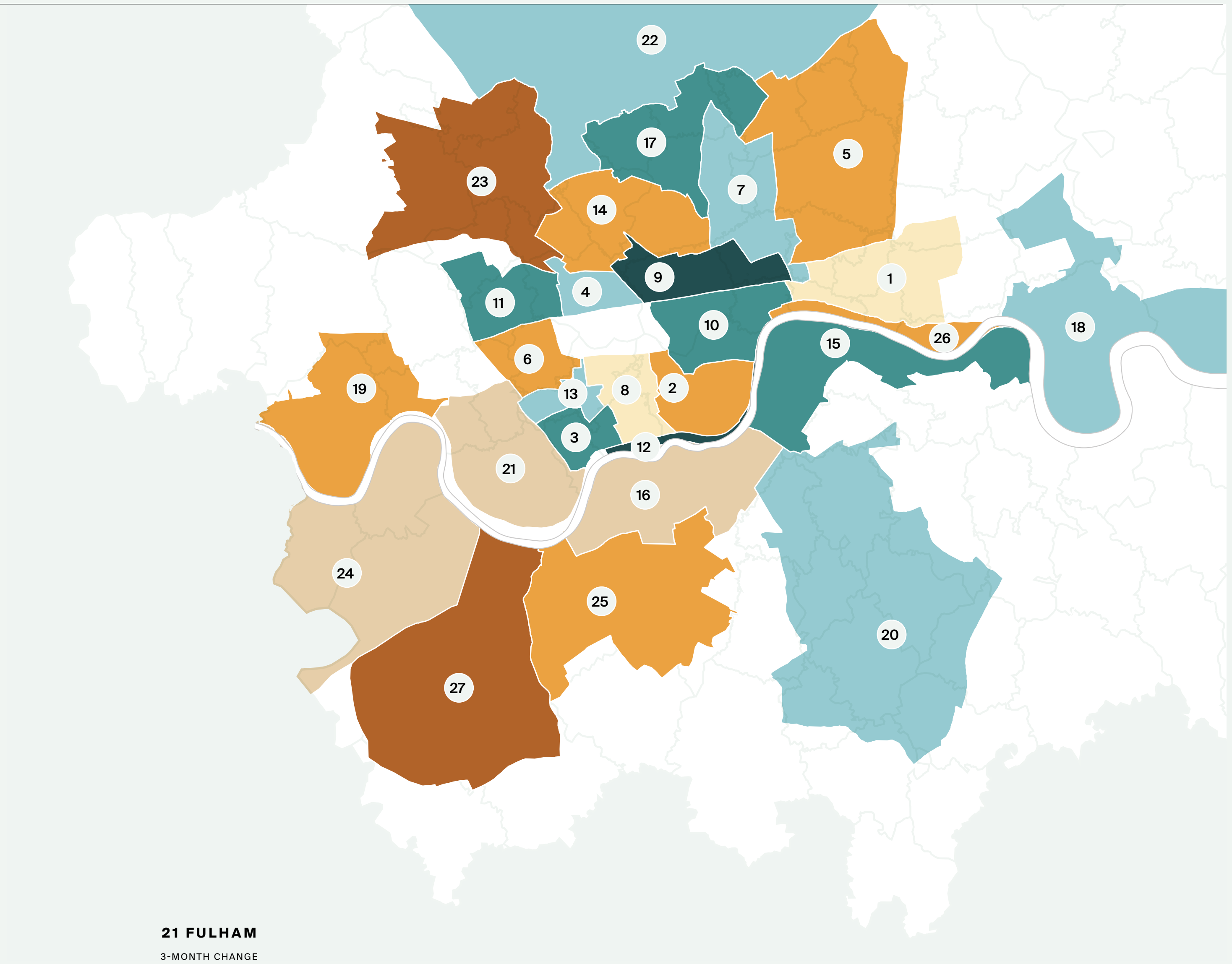
Source: Knight Frank Research

PRIME LONDON PRICE AND RENTAL GROWTH, DECEMBER 2022

PRIME CENTRAL LONDON

SALES -0.6% RENTS 3.0% 3-MONTH CHANGE

3-month change	Sales	Rents
1 ALDGATE	-1.5%	4.8%
2 BELGRAVIA	0.7%	2.9%
3 CHELSEA	-1.0%	2.5%
4 BAYSWATER	-0.3%	4.8%
5 ISLINGTON	-2.8%	4.7%
6 KENSINGTON	-0.2%	5.4%
7 KING'S CROSS	-1.9%	-3.7%
8 KNIGHTSBRIDGE	0.4%	4.6%
9 MARYLEBONE	-0.2%	2.8%
10 MAYFAIR	-0.8%	2.7%
11 NOTTING HILL	-0.3%	0.9%
12 RIVERSIDE	-0.8%	7.0%
13 SOUTH KENSINGTON	-0.8%	0.2%
14 ST JOHN'S WOOD	-0.7%	0.4%
15 TOWER BRIDGE	0.4%	4.5%



PRIME OUTER LONDON

SALES -0.2% RENTS 3.2% 3-MONTH CHANGE

3-month change	Sales	Rents
16 BATTERSEA	1.2%	7.2%
17 BELSIZE PARK	0.3%	1.2%
18 CANARY WHARF	-0.4%	0.3%
19 CHISWICK	-3.6%	
20 DULWICH	0.0%	
21 FULHAM	-0.4%	6.6%
22 HAMPSTEAD	0.0%	1.3%
23 QUEENS PARK	-0.4%	6.5%
24 RICHMOND	-0.6%	1.2%
25 WANDSWORTH	0.7%	0.4%
26 WAPPING	0.0%	6.0%
27 WIMBLEDON	-0.6%	0.1%

PRIME LONDON LETTINGS MARKET

Growing evidence that rental market may rebalance in 2023

There has been a marked imbalance between supply and demand for 18 months in the London lettings market, and the narrative of frustrated tenants and fast-rising rents has become familiar.

Supply remained tight at the end of 2022, and the number of market valuation appraisals to let in the 12 months to December was 10% lower than the previous year.

On the demand side of the equation, the number of new prospective tenants in Q4 was 30% above the five-year average.

Consequently, average rental values in prime central London (PCL) ended the year 17.8% higher, or 23.2% above their pre-pandemic average (see fig 3).

In prime outer London, the annual rise was 15.8%, meaning rents were 21.1% above their level in March 2020.

It means prospective tenants have been operating in a highly competitive market.

However, there are some signs that supply is improving in higher-value markets as owners tend to be more discretionary with their options (see fig 4.). Market valuation appraisals for lettings properties valued between £1,000 and £4,999 per week were 15% higher In November 2022 than January 2022. Below £1,000 per week, there was a decline of 27% in the same period. Appraisals are a leading indicator of supply.

It could even be a sign of things to come for the rest of the market in 2023.

By the time the spring selling season gets underway, mortgage rates will be at least two percentage points higher than they were in spring 2022 as rates the Bank of England responds to double-digit inflation.

It will force a recalculation on the part of buyers and sellers around what they can afford. We expect this process will drive prices 10% lower over the next two years.

Some owners will accept lower prices while others will decide to let out their property instead. The recent history of strong double-digit rental value growth will be an added attraction for 'accidental landlords'.

Three years after the pandemic first struck, the lettings market may finally undergo a process of self-correction as we head into spring, potentially providing some relief to tenants.

NOTED

23.2%

The increase in average rental values in PCL since the start of the pandemic.

10%

The fall in the number of market valuation appraisals to let in the 12 months to December versus the previous year.

30%

The increase in the number of new prospective tenants in Q4 versus the five-year average.

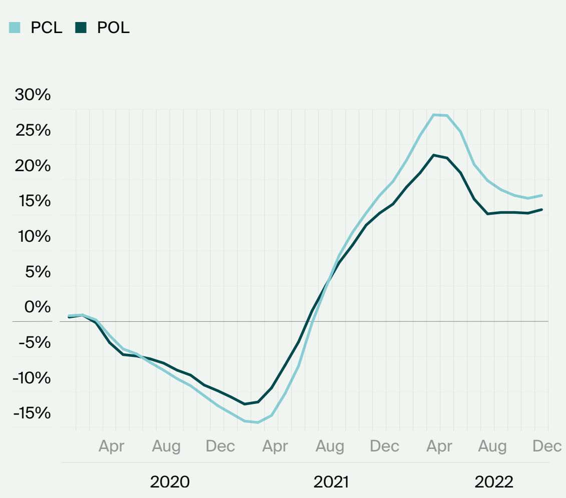
"Three years after the pandemic first struck, the lettings market may finally undergo a process of self-correction, potentially providing some relief to tenants."

TOM BILL

TOM BILL, HEAD OF UK RESIDENTIAL RESEARCH

3 London rental value growth

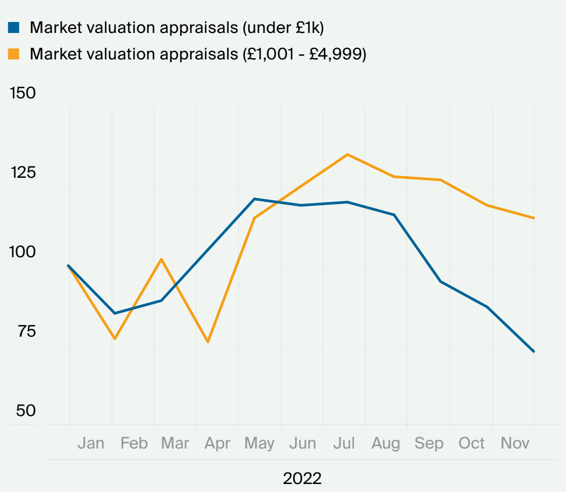
% annual change



Source: Knight Frank Research

4 Lettings supply increases for higher-value properties

Rebased to 100, January 2022



Source: Knight Frank Research

PRIME LONDON IN NUMBERS

51%

Some parts of the country may be more insulated from rising mortgage costs than others. Kensington & Chelsea (51%), the City of London (47%) and Westminster (46%) have led the way for cash buyers over the last decade. The UK average was 31%, according to an analysis of Land Registry data since 2011, placing PCL in a relatively insulated position as borrowing costs rise.

152

There were 152 super-prime sales in the year to October 2022, whole-market data shows. The figure was down slightly on the previous 12 months (159), though it may rise as Land Registry records update. Either way, the figure was higher than any of the previous five years. A total of £2.8 billion was spent in the latest 12-month period, which was the most in seven years.

10%

The US dollar has started to see some of the strength it gathered in 2022 wane. At its peak, in early November, the dollar's yearly gains were more than 10% against a basket of currencies. This came off the back of the Federal Reserve's earlier rate hiking as well as the currency's safe haven status. This could diminish to some extent in 2023.

Please get in touch with us

If you are looking to buy, sell or would just like some property advice, we would love to hear from you.

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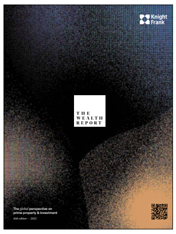

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