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.**

HIGHER SUPPLY LEADS TO RENTAL VALUE DECLINES IN PRIME CENTRAL LONDON

Increased stock levels and jitters in global financial markets have combined to produce a decline in rental values, says Tom Bill

May 2016

Annual rental value growth declined to -2.3%, the lowest rate since February 2014

The number of new properties coming onto the market between January and April rose 18.1% compared to 2015

The number of new prospective tenants fell -2.3% between January and April versus 2015

Prime gross yields rose to 3.11% after inclusion of east London offices

Macro View: The new Mayor and London housing

Annual rental value growth in prime central London declined to -2.3% in May, which was the lowest rate since February 2014.

This compares to a figure of 4.2% a year ago in the month of the UK general election, which was the strongest month for annual rental value growth since December 2011.

The positive figure then reflected the fact many buyers were uncertain over the trajectory of the sales market and instead decided to rent as a short-term measure.

However, uncertainty has also since affected vendors, who have opted to let out their properties until greater clarity emerges around the short-term prospects for price growth in the sales market.

As supply levels have risen, the balance of power has shifted towards tenants and rental values have fallen.

The number of new lettings properties coming onto the market in prime central London between January and April 2016 increased 18.1% compared to 2015.

In the same period, the number of tenancies started declined -5.4% and the number of new prospective tenants registering fell -2.3%, underlining the growth in the amount of rental properties compared to tenants.

The number of viewings rose 5.9% over the same period, highlighting how tenants have become increasingly selective and take longer before agreeing letting deals.

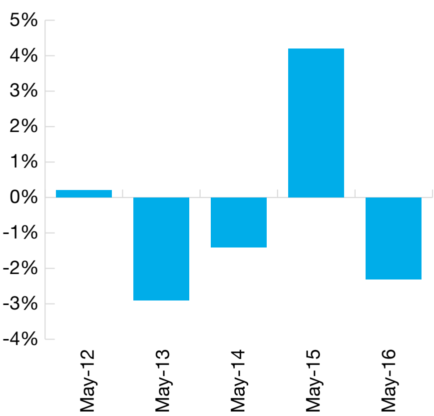
This shift in the balance of supply and demand has taken place against a jittery global financial backdrop, which means many corporate tenants, particularly at senior executive level, have reduced budgets or curbed relocation plans.

Demand remains stronger below £1,500 per week and at the super-prime £5,000-plus per week levels, where higher transaction costs have caused some buyers to explore to rental option.

Levels of optimism in the financial sector fell in the first quarter this year, exacerbated by uncertainty ahead of June's EU referendum vote, as figure 2 shows.

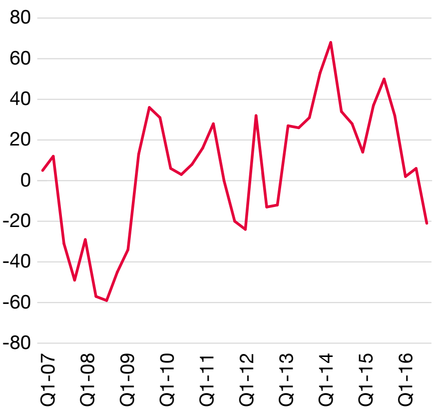
Prime gross yields increased to 3.11% in May, largely due to the stronger performance of east London markets and the inclusion of data from Aldgate and King's Cross.

FIGURE 1
Annual rental value growth in prime central London



Source: Knight Frank Research

FIGURE 2
Pessimism grows in the financial sector
Optimism levels versus three months ago, PWC/CBI survey (zero equals no change)



Source: Knight Frank Research

TOM BILL
Head of London Residential Research

"As supply levels have risen, the balance of power has shifted towards tenants and rental values have fallen"

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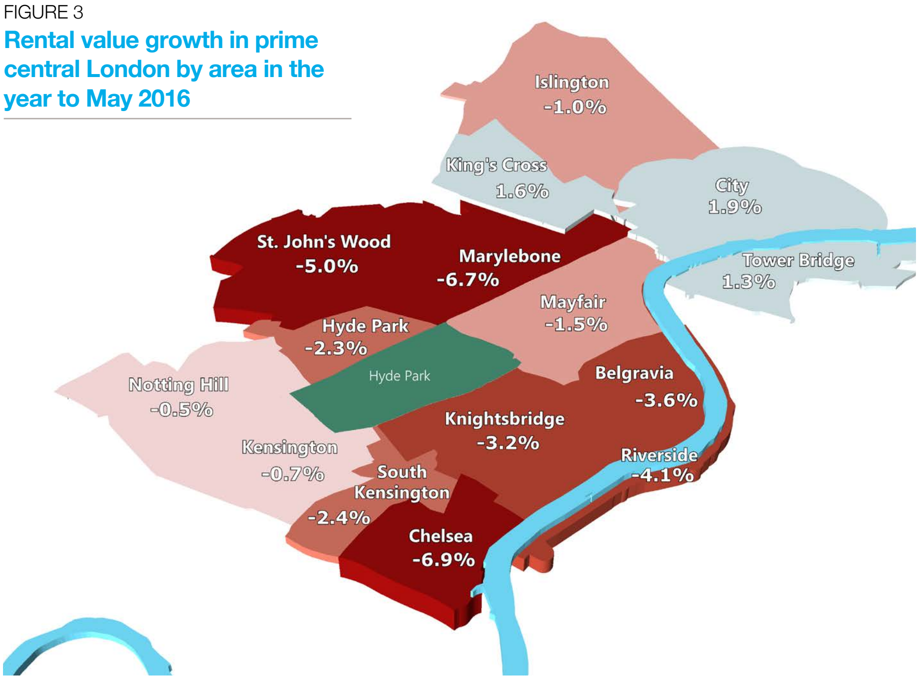
FIGURE 3
Rental value growth in prime central London by area in the year to May 2016



DATA DIGEST

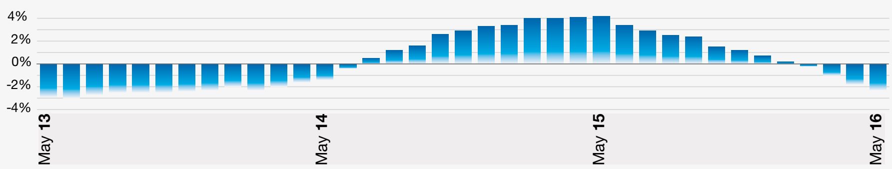
The Knight Frank Prime Central London Index, established in 1995 is the most comprehensive index covering the prime central London residential marketplace. The index is based on a repeat valuation methodology that tracks rental values of prime central London residential property. 'Prime central London' 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.

THE MACRO VIEW MAY 2016

Prime Central London Index | **172.4**

Annual rental value growth in prime central London over the last three years



THE NEW MAYOR AND LONDON HOUSING

Housing was the key political battleground ahead of May's London Mayoral election, with both candidates pledging to build more homes to address affordability concerns.

Sadiq Khan, the winning candidate, said he wants to double the amount of houses built to 50,000 a year by 2020.

He also plans to increase the number of affordable homes and has talked about tighter restrictions on overseas buyers and controlling rents.

Full details have not emerged but the high level of political scrutiny on housing means the new Mayor is likely to adopt an approach that is economically viable for developers in order to ensure his target is met, said Professor Tony Travers, a local government expert at the London School of Economics.

"All the evidence so far is that pragmatism is triumphing over ideology," he told Knight Frank. "The last thing he will want to do is emit signals that undermine the capacity to deliver at least as many homes as last year. What is essential is that the number of new homes built doesn't fall."

"What was unusual about the 2016 Mayoral election was that enough numbers were traded by the candidates to create a measurable benchmark, which his opponents in 2020 will point to if he falls short," he said. "With that in mind he needs to keep developers broadly onside."

The relatively slow pace of announcements regarding policies and appointments since Khan won the election, was also a sign of a pragmatic approach, said Travers. "If this is an indication of what is to come, the lack of rash promises suggests the cautious approach of a professional politician," he said.

However, the backdrop of the EU referendum has dominated Khan's early days in office. "If the UK voted to leave and London voted to stay in, the Mayor would be well within his rights to argue for greater autonomy from the rest of the UK to ensure the city's economy is protected."

RESIDENTIAL RESEARCH

Tom Bill
Head of London Residential Research
+44 20 7861 1492
tom.bill@knightfrank.com

PRESS OFFICE

Jamie Obertelli
+44 20 7861 1104
jamie.obertelli@knightfrank.com

Harry Turner
+44 20 3861 6974
harry.turner@knightfrank.com