RESIDENTIAL RESEARCH

PRIME CENTRAL LONDON RENTAL INDEX

TENANT DEMAND REMAINS WEAK AS STOCK MARKET VOLATILITY CONTINUES

Uncertainty in global financial markets in September dampened tenant demand though not in the highest price brackets, says Tom Bill

September 2015

Annual rental growth declined to 2.4%, the lowest rate since September 2014

Number of tenancies agreed in the three months to August fell -5.9% versus 2014

Number of super-prime tenancies agreed in the three months to September **on track to be 50% higher than previous three-months**

Stock levels are -15.6% down since April, which will put upwards pressure on rents

Prime gross rental yields remained at 2.96%

Macro View: Politics and prime central London

TOM BILL
Head of London Residential Research

"This current overriding mood of uncertainty means companies are more hesitant about recruiting and are more conservative with relocation budgets for senior executives"

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Annual rental value growth in prime central London declined to 2.4% in September, which was the lowest level it has been since September last year.

The slowdown came against the backdrop of jittery financial markets, with nerves over the state of the Chinese economy spreading to commodity and mining stocks, compounded by declines among carmakers. As a result, the FTSE 100 fell back below 6,000 in the second half of September.

This current overriding mood of uncertainty means companies are more hesitant about recruiting and are more conservative with relocation budgets for senior executives, which has dampened demand in the prime central London lettings market.

As a result, the number of tenancies agreed in the three months to August fell -5.9% compared to the previous year and the number of viewings declined -10.2%. Such declines suggest the trend for falling rental value growth will persist in the short-term.

However, the trend is less marked in both lower and higher price brackets. Demand among younger professionals remains strong while demand at the super-prime level of £5,000 per week and above has been buoyed by the fact tenants have moved across from the sales market due to last December's stamp duty increase.

The number of super-prime tenancies agreed in the three months to September was on track to be 50% higher than the preceding three-month period.

Across the whole of the market, the result has been a rise in stock levels, with weaker demand compounded by the fact more vendors have become landlords due to uncertainty over the strength of price growth in the sales market after the stamp duty rise.

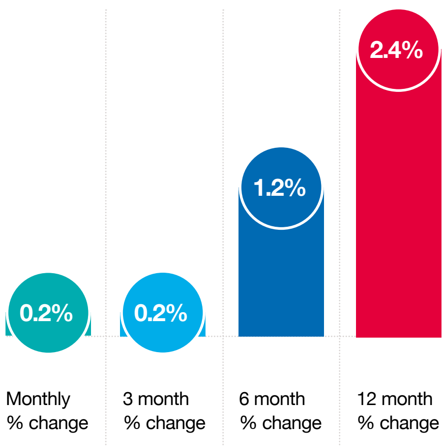
However, there are signs this trend for higher stock levels has peaked which could signal that recent changes to the sales market including stamp duty has begun to be processed, which will put upwards pressure on rents.

Stock levels in 2015 reached their peak a fortnight before the general election but have since been on a downwards trajectory that became more marked after July, meaning the level in early August was 15.6% down from its pre-election high point.

FIGURE 1

Rental value growth in prime central London

September 2015



Source: Knight Frank Residential Research

FIGURE 2

Prime central London lettings market in numbers

Number of tenancies agreed in the three months to August versus the same period in 2014	-5.9%
Number of viewings in the three months to August versus the same period in 2014	-10.2%
Expected increase in the number of super-prime tenancies agreed in the three months to September versus the previous three-months	50%
Decline in stock levels between April and August	-15.6%

Source: Knight Frank Residential Research

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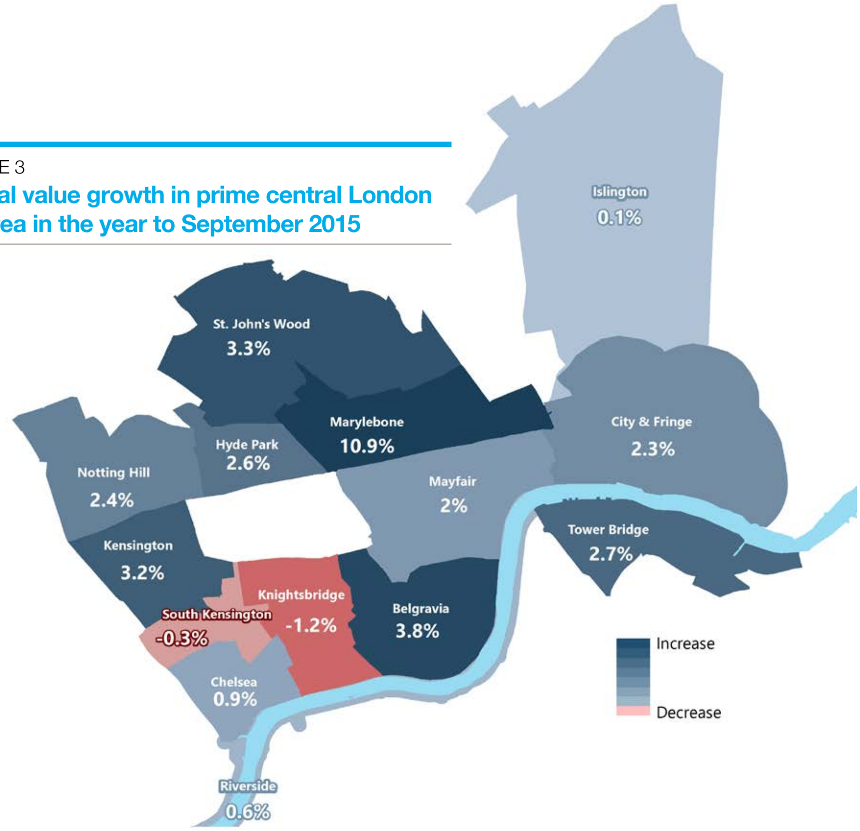
FIGURE 3

Rental value growth in prime central London by area in the year to September 2015



DATA DIGEST

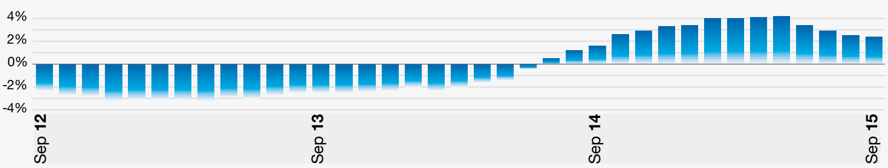
The Knight Frank Prime Central London Index, established in 1976, is the longest running and most comprehensive index covering the prime central London residential marketplace. The index is based on a repeat valuation methodology that tracks capital values of prime central London residential property. 'Prime central London' is defined in the index as covering: Belgravia, Chelsea, Hyde Park, Islington, Kensington, Knightsbridge, Marylebone, Mayfair, Notting Hill, South Kensington, St John's Wood, Riverside* the City and the City Fringe. 'Prime London' comprises all areas in prime central London, as well as Barnes, Canary Wharf, Chiswick, Clapham, Fulham, Hampstead, Richmond, 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 SEPTEMBER 2015

Prime Central London Index | **177.2**

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



While a lot has changed in UK politics over the last 12 months, housing has remained one of the most live issues.

As attention turns to party conference season and then to next May's London Mayoral election, the prime London sales and rental markets may again become the subject of proposals aimed both winning votes and addressing supply shortages.

However, the Mayor's powers are limited in their scope compared to central government, said Professor Tony Travers, a local government expert at the London School of Economics.

Speaking to Knight Frank, he said: "There is always a risk of more heat than light during the Mayoral campaign. Often, Mayoral candidates are tempted to opine about things over which they have no powers such as rent controls and overseas buyers, but I'm not sure there is much the Mayor could do without central government help."

Rather, the Mayor's key role is to tackle affordability concerns at their root by facilitating more housebuilding, Travers said. "The big challenge for any Mayor is the level of house building that needs to be achieved compared to the current reality. While it's easy to focus on foreign buyers, the knock-on effect is that it would effectively cut the amount of social and affordable housing."

On rent controls, Travers said the rental market could move up the political agenda as more Londoners become tenants, despite not tackling the supply problem at its root. "There may come a point when the balance tips in politicians' minds that there are votes to be had," he said.

For now, Travers believes George Osborne's latest increase in the rate of stamp duty for properties worth more than £1.1 million in December will reduce the level of political focus due to the dampening effect it has had on price growth and transaction volumes.

"There are fewer possible policy changes around the top-end of the London housing market for any Mayor to get their hands on anyway," he told Knight Frank.

Meanwhile, at a national level, strong indications from within Whitehall suggest the government is providing more resources and thinking more profoundly about how to increase housing supply for both the sales and private rented sector.

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