

Residential Quarterly | Winter 2016/2017

Research - Market View

Economic outlook

The global political and economic outlook was uncertain throughout 2016 and with the realisation of Brexit and the inauguration of US President Donald Trump, uncertainty is likely to persist during 2017. Throughout Western Europe there are signs of discontent amongst the working and middle classes. The result has been a rejection of constitutional reform in Italy, rising popularity for right wing parties in Austria and Germany and increasing support for Marine Le Pen in France. The realisation of Prime Minister May's promise to trigger Article 50 by the end of March 2017 and the upcoming elections in France and Germany are all likely to increase uncertainty in UK markets.

The ONS's preliminary estimate of GDP growth forecasts for Q4 have narrowed, with most commentators estimating that around 2% growth was achieved, a view echoed by the OECD. Her Majesty's Treasury publish forecasts from several independent forecasters and on average the forecasts expect GDP to grow by 1.3% during 2017.

The British Chamber of Commerce's Quarterly Economic Survey for Q4 2016 identifies that on every measure they collect there is an expectation that there will be an expansion of activity. Manufacturing appears to have seen a significant boost in the balances felt around employment growth, investment and confidence all increasing by 8, 11 and 7 percentage points compared to the third quarter of 2016. However, both the manufacturing and service sectors expect their prices to rise due to the increased price of raw materials.

Rising costs for business may still impact the domestic market, both by increasing costs for domestic firms and making imports more expensive. The YoY growth of CPI has been strong when compared to 2015 but it remains low; in December (the latest release) growth was 1.6% over half of the Bank of England's target rate (2%). The Bank of England, after cutting the UK base rate to 0.25%, has stated it will tolerate some inflation over the short-medium term.

Despite a brief slump in the wake of Brexit, the FTSE 100 was on an upward trend during 2016, finishing the year with growth of almost 20%.

GDP is now 8.7% higher than its pre-crisis peak in 2008. However, on a per capita basis the gain is a more modest 1.9%.



The key Purchasing Managers' Indices for the UK ended 2016 in strong positive territory.



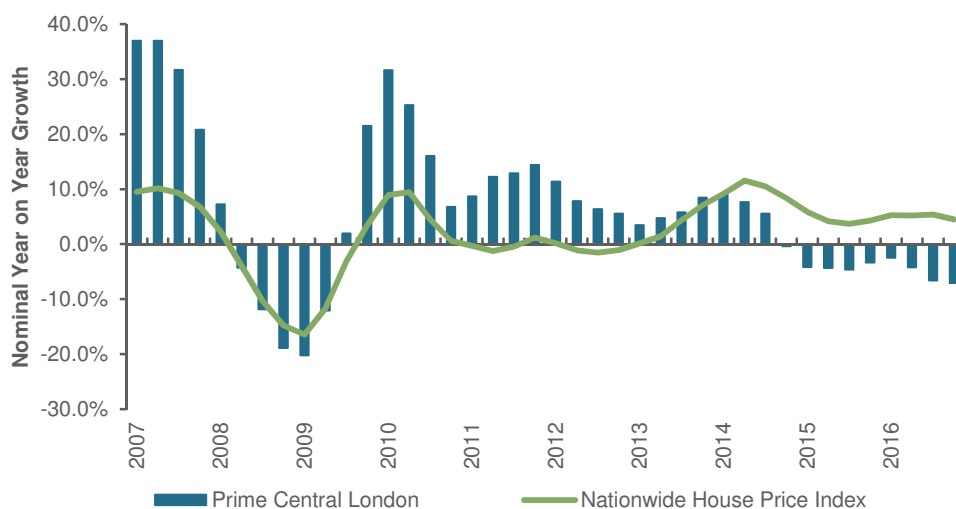
The latest employment statistics for the three months to November 2016 show a decrease in employment of 9,000 when compared against the three months to August 2016. Unemployment fell by 52,000 to 1.6 million, with the unemployment rate falling marginally to 4.8%.



Property market pricing

According to the Nationwide House Price Index, UK property prices grew 4.5% during 2016. Historically London has been the driving force of UK prices, but this changed during 2016. Whilst London achieved growth of 3.6% over the year, the region was outperformed by 8 of the 12 other regions, most notably East Anglia (10.1%), Outer South East and Outer Metropolitan (6.9% and 6.8% respectively). The two Midlands regions, Yorkshire and the South West all experienced growth of over 4%.

Figure 1. UK house price growth vs Prime Central London (PCL)



Source: Nationwide House Price Index, Volterra

UK residential sales transactions

Table 1. Number of Properties Sold by property type for 2016

Region	Detached	Semi-Detached	Terraced	Flats
East Midlands	23,411	21,274	18,953	4,816
East of England	25,197	22,594	25,714	16,255
Greater London	4,142	11,938	24,193	44,998
North East	5,741	10,419	11,241	3,529
North West	17,798	31,481	33,535	11,481
Scotland	23,456	17,104	22,808	36,461
South East	32,652	30,206	36,104	31,066
South West	24,899	19,279	26,275	16,768
Wales	11,103	10,873	12,832	3,102
West Midlands	17,920	23,164	21,655	8,038
Yorkshire and Humber	15,796	24,152	23,529	7,143

Source: Dataloft, Land Registry as at 20th January 2017; Registers of Scotland as at 1st February 2017

Price growth in London dipped below the UK average for the first time in 8 years, according to Nationwide.



Annual Price Change by Nation (seasonally adjusted):

England: 5.1%
Wales: 2.4%
Scotland: 2.2%
N Ireland: 0.7%

Source: Nationwide



“Whilst Brexit headwinds still exist the country is getting back to business as usual. The lack of housing supply and strong demand will continue to drive pricing up, though perhaps in single digits.”

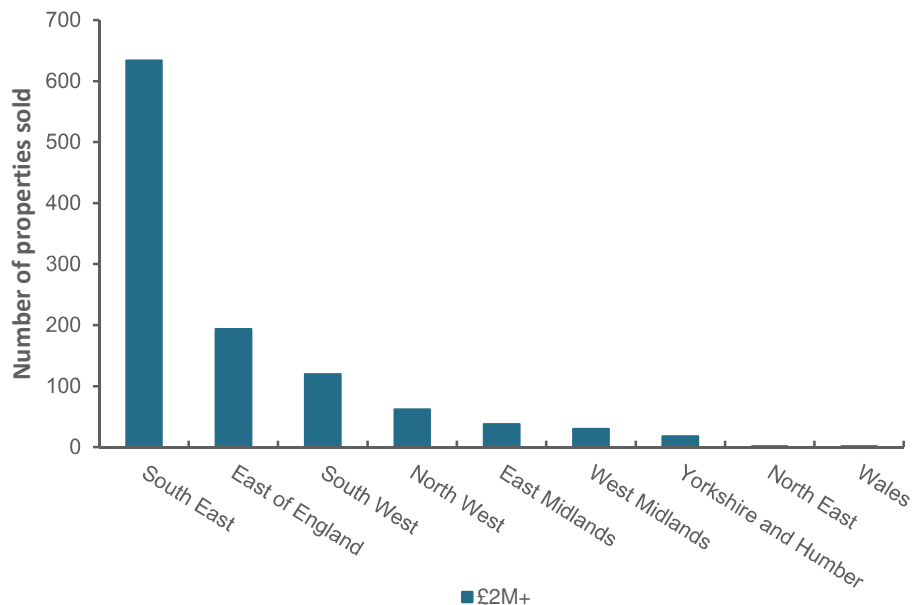
- Guy Robinson
Head of Regional Residential Agency



Country house highlights

During 2016 the Stamp Duty Land Tax on additional homes went into effect and the EU Referendum was held causing two pauses in the overall housing market. However, transaction volumes in the £2M+ market remained relatively steady in 2016 compared to 2015 with the South East showing the highest level of activity with over 600 houses sold in 2016.

Figure 2. Number of properties over £2m+ sold in England & Wales excl. London

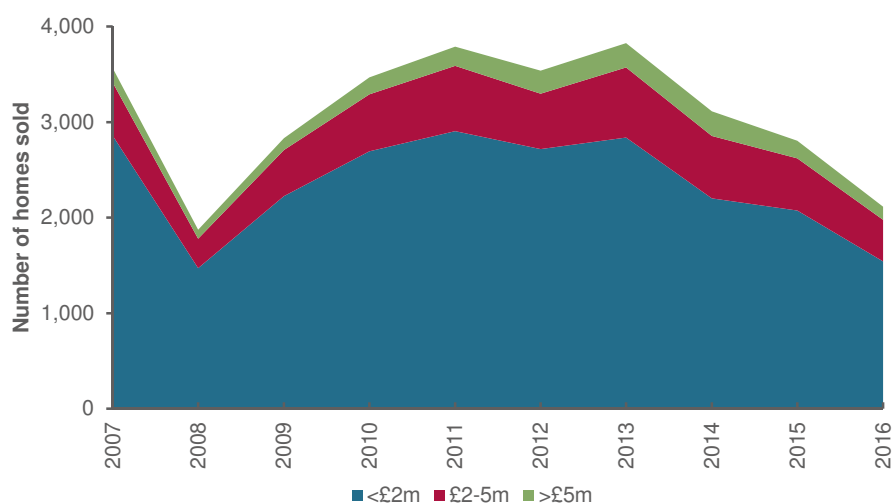


Source: Dataloft, Land Registry as at 20th January 2017

Prime Central London residential sales market

Transaction levels in 2016 were nearly 25% down compared to 2015. However, it should be noted that there was a slight pick-up in transactions during the final two quarters of 2016, but levels remain considerably below the five year average.

Figure 3. Historic number of sales in PCL



Source: Dataloft, Lonres.com, Strutt & Parker as at 20th January 2017

“Through all the political uncertainty of the past year, the country house market continues to show that bricks are stronger than anything. For 2017, resiliency will continue as demand remains high for the limited supply of good quality houses that are priced appropriately.”

- James Mackenzie
Head of Country
Department



“The politically driven changes of SDLT, ATED, non-dom status and SDLT on additional homes through 2015 and 2016 have laboured the downward trend stalling transactions and new investment in Prime Central London.”

- Charlie Willis
Head of London
Residential Agency

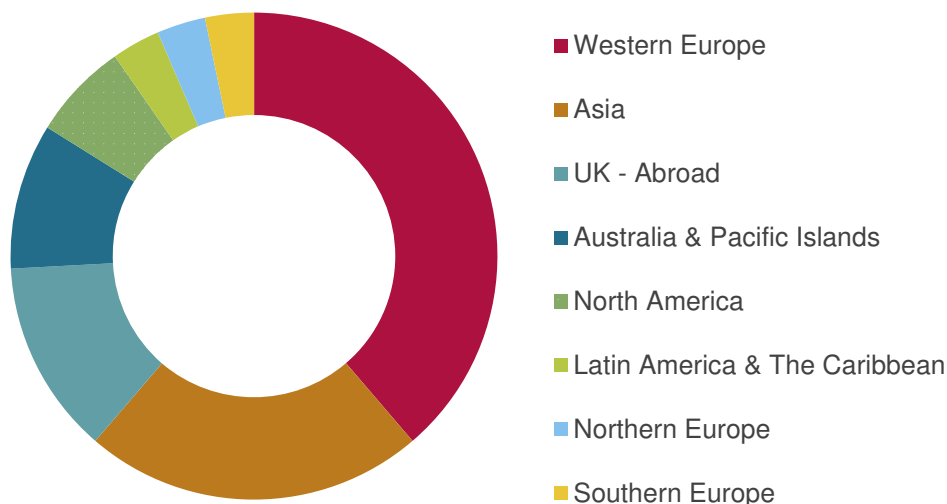


With more incidences of sellers prepared to review pricing and entertain reasonable offers, it appears the market has found a level which may provide a spur to transaction levels.

Strutt & Parker data for the fourth quarter of 2016 showed a small uplift of 4.6% in UK domestic market buyers when compared to the same period last year.

However, despite the Brexit vote and the continuing uncertainty, PCL still retains its attractiveness to overseas buyers with an increase of buyers coming from both Western Europe and Asia relative to the fourth quarter of 2015.

Figure 4. Known PCL buyer nationalities for Q4 2016 (excl. UK domestic market)

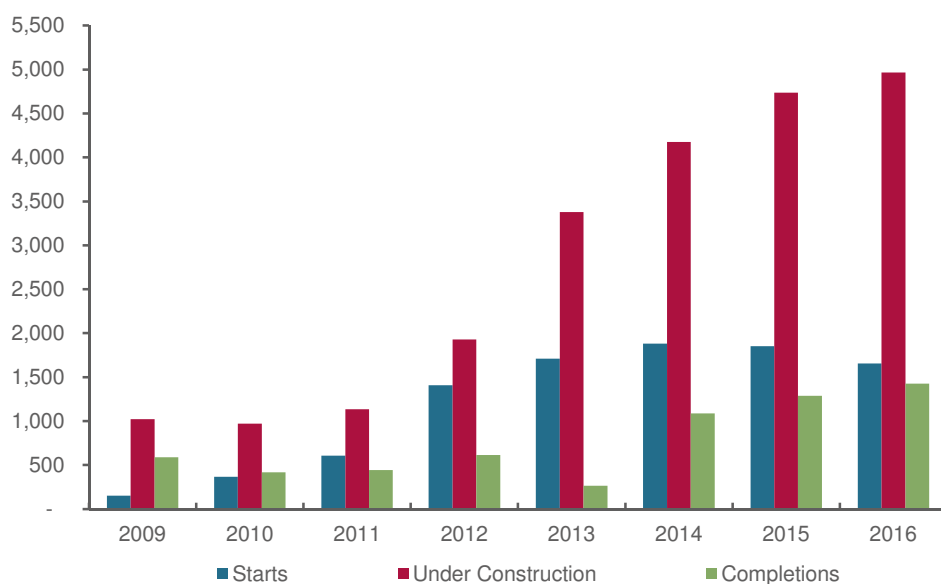


Source: Strutt & Parker

Prime Central London residential new homes

There was an almost 11% decrease in new home construction starts for 2016 compared to 2015 in PCL, however a proportional increase (11%) of new homes completed for the same time period.

Figure 5. Construction status of new homes in PCL



Source: Molior, Strutt & Parker as at 31st January 2017; PCL defined as Local Authorities of Hammersmith & Fulham, Kensington & Chelsea and Westminster

Looking at financing options and Strutt & Parker buyer profiles, there has been an increase in cash purchases with nearly 55% in 2016 compared to 46% in 2015.



There also has been a shift in the desire to purchase a house (52%) over a flat (48%) in 2016 compared to 40% and 60% respectively in 2015.



“Despite 2016 being a year of twists and turns both domestically and overseas, London remains a world city and global financial hub. Currency advantages and a reduced supply chain in Prime Central London point towards a positive outlook for 2017.”

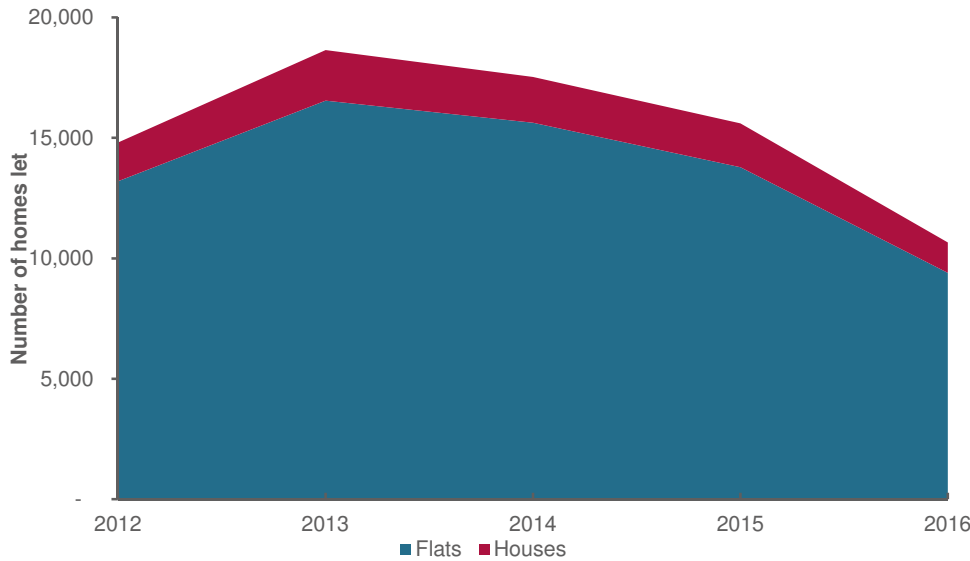
- Mark Dorman
Partner, London
Residential Development
& Investment



Prime Central London lettings market

There were nearly 11,000 property lets agreed in PCL in 2016, which was 31% down compared to 2015 when nearly 16,000 property lets were agreed.

Figure 6. Historic agreed lets in PCL



“The lack of new tenancies in PCL year on year reflects the uncertainty in the market following Brexit, our tenant profiles show that over 40% of our tenants are European and those tenants are simply renewing and staying put to see how Article 50 unfolds.”

*- Kate Eales
Partner, Head of Lettings*

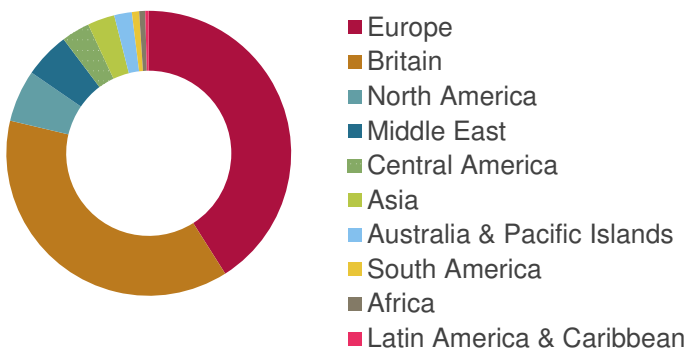


Source: Dataloft, Lonres.com, Strutt & Parker

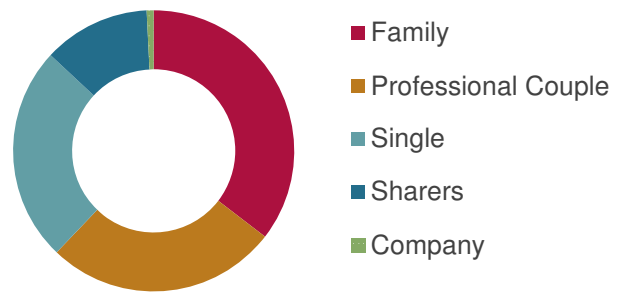
The current economic conditions and the SDLT for additional homes which went into effect in April 2016 are having an impact on the lettings market in PCL.

Figure 7. Tenant profiles in PCL Q4 2016

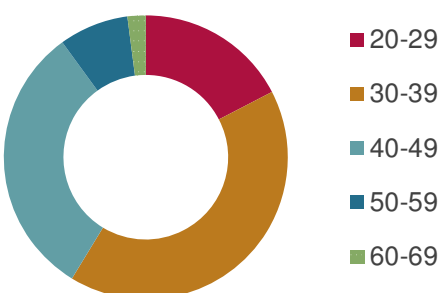
Nationality



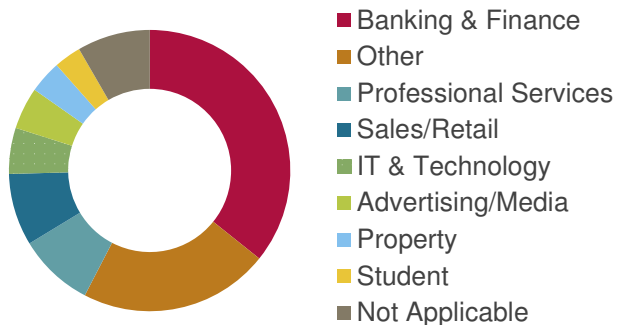
Lifestyle status



Age



Employment industry



Source: Strutt & Parker

Outlook & forecast

The downward pressure on PCL house prices because of Brexit and SDLT has likely already been experienced. Although the UK and the world are entering a period of substantial uncertainty, commentators believe the outlook for the UK remains reasonable. The immediate focus should be placed on the reaction to the triggering of Article 50 and the inauguration of Trump. The weak pound is an incentive to international investors to buy UK property but if the dollar slides it may lose some comparative advantage.

Transaction levels reportedly picked up slightly at the end of 2016, although they remain low by historic standards. This pick-up will only continue if sellers price realistically. The current attractiveness of Sterling will also be a factor in terms of market activity in the higher price sectors.

Table 2. Residential price forecast Q4 2016

Sales	2017	2018	2019	2020	2021	5 Year to 2021
Prime Central London – best case	0%	0%	8%	8%	8%	26%
Prime Central London – downside risk	-5%	-5%	4%	4%	4%	2%
UK	5%	4%	4%	4%	4%	23%
Lettings	2017	2018	2019	2020	2021	5 Year to 2021
Prime Central London - Lettings	0%	2.5%	4%	4%	4%	15%

“Uncertainty will continue with the upcoming global events in 2017 generating volatility and making it a challenge to forecast. However, with creeping inflation and questions of how long the Bank of England can hold interest rates, the extraordinary shortage of housing stock in the UK alongside housing demand will continue to keep house prices stable in London with a slight uptick across the UK.”

- Vanessa Hale
Partner, Research



Methodology

As the housing market is seasonal, for the purposes of this report; data is compared year on year, i.e. looking at 2016 in light of changes since 2015. Data may also be compared on a rolling month on month basis. When referring to the PCL market it includes those markets which Strutt & Parker operate in (Knightsbridge, Belgravia, Kensington, Chelsea, Notting Hill & Fulham) and as such is reflective of London's most prime markets. Economic views are attributed to Strutt & Parker's retained economic advisors, Volterra. Additionally, Lonres.com data is used to assess the London sales and lettings market. The behavioural data is collected from our activity in PCL markets: our proprietary "behavioural data" is not representative of the UK as a whole. The global economy remains volatile and therefore there is risk that any market commentary provided will become out-dated within a very short timescale.

Contact us

Charlie Willis

Head of London
Residential Agency
charlie.willis@struttandparker.com

Kate Eales

Partner, Head of Lettings
kate.eales@struttandparker.com

Mark Dorman

Partner, London Residential
Development & Investment
mark.dorman@struttandparker.com

Guy Robinson

Head of Regional
Residential Agency
guy.robinson@struttandparker.com

James Mackenzie

Head of Country Department
james.mackenzie@struttandparker.com

Vanessa Hale

Partner, Research
vanessa.hale@struttandparker.com

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