

# Residential Quarterly | Autumn 2017

## Research - Market View

### Economic Outlook

Information on the ongoing Brexit negotiations is extremely opaque but signs suggest there is significant disagreement within the Cabinet. The absence of a majority for Prime Minister Theresa May further weakens her authority and negotiating position. This lack of clarity on Brexit, party infighting and question marks over how long the current Prime Minister will be in charge are all going to increase uncertainty within the UK.

In Europe, Spain is in a period of significant political unrest as the Catalan independence movement has gained momentum and in Germany, Angela Merkel has secured another term as Chancellor of Germany, even with a reduced number of seats. This is likely to bring an element of stability as she represents the status quo and the result has huge implications for Brexit negotiations given Germany's prominent position within Europe. It will become especially important for when the UK is discussing a trade deal with Europe.

Outside of Europe, relations between Russia and the US are worsening, partly because of tensions in the Middle East but also the accusations, which are gathering in terms of momentum and evidence, of alleged Russian interference in the US presidential election. Furthermore, there remains considerable concern over the escalating situation between the US and North Korea and relations between Qatar and the surrounding Middle Eastern States. American politics continue to be dominated by arguing within Trump's inner circle and high staff turnover. Although these international issues may not directly affect the domestic market they will indicate the direction that world politics and the world economy may take, which will have knock on impacts in the UK and on Brexit negotiations.

The World Bank forecast that UK economic growth will be 1.7% over the course of 2017 and business confidence has been fluctuating over the course of the year, showing signs of recovering from the initial shock of Brexit. The rising costs for businesses (apprenticeship levy, business rates, living wage), coupled with the weak exchange rate, may still impact the market, both by increasing costs for domestic firms and making imports more expensive.

In 2017 inflation has been above the Bank of England's target rate (2%) for most of the year to date. The British Chamber of Commerce expects inflation to reach a peak of 3% before the end of 2017 and it is expected to outpace earnings until 2019. This will erode real wages and is likely to result in lower consumer spending. This is particularly worrying considering consumer spending is a key driver of economic growth.

The Bank of England finally increased the official bank rate – from 0.25% to 0.5% – the first interest rate rise in over ten years. The rate remains very low by historic standards, but it will increase mortgage rates for some households, as well as increasing savings rates for others. Financial markets are indicating two more interest rate increases over the next 3 years, taking the official rate to 1%.

The FTSE 100 is still looking positive and has registered another set of strong growth figures for Q3 2017, although this has been variable since the EU referendum. And as for productivity and unemployment, unemployment remains very low whilst productivity has fallen.

# 3.0%

September 2017 inflation  
was at 3.0% up from 2.9% in  
August 2017



PMI Services up from 53.2 &  
PMI Industrial down from 56.7



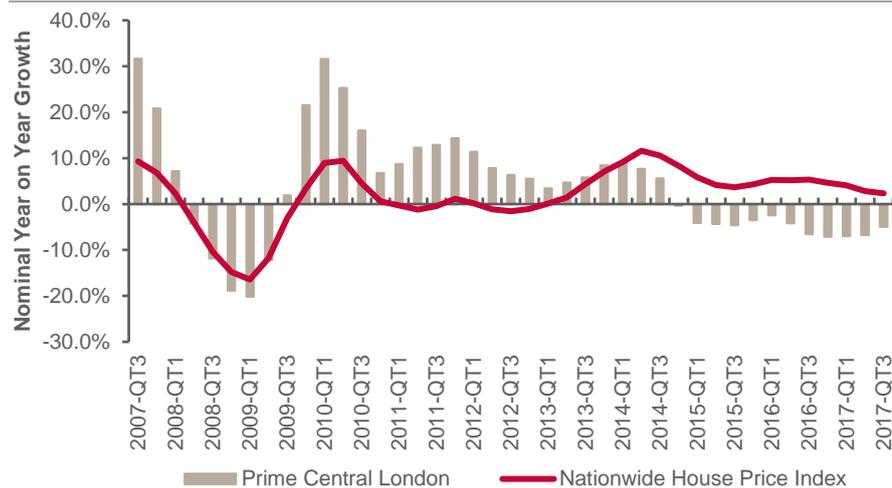
Real average weekly earnings  
(total pay) fell by 0.3% in the  
three months to August 2017,  
compared to the equivalent  
period in 2016.

## Property market pricing

According to the Nationwide House Price Index, year-on-year growth up to Q3 2017 showed that the best performing region has been the East Midlands (5.1%) closely followed by the South West (4.7%) and the West Midlands (4.6%). In contrast to this however is London, which has been the worst performing region with a negative growth of 0.6%.

National house prices are now 13.9% above the 2007 peak compared with six regions which have yet to achieve their previous figures. In PCL, prices have declined for the third consecutive quarter of 2017. This means prices have fallen circa 3% so far in 2017 and are down by 5% compared to the same time a year ago.

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 registered properties sold by property type for Q3 2017

| Region               | Detached | Semi-Detached | Terraced | Flats  |
|----------------------|----------|---------------|----------|--------|
| East Midlands        | 2,998    | 2,833         | 2,194    | 443    |
| East of England      | 3,444    | 3,169         | 3,129    | 1,534  |
| Greater London       | 598      | 1,698         | 3,205    | 4,324  |
| North East           | 693      | 1,472         | 1,439    | 389    |
| North West           | 2,336    | 4,410         | 4,067    | 1,126  |
| Scotland             | 7,008    | 4,973         | 6,412    | 10,149 |
| South East           | 4,785    | 4,506         | 4,635    | 2,991  |
| South West           | 3,605    | 2,771         | 3,450    | 1,734  |
| Wales                | 1,503    | 1,496         | 1,670    | 324    |
| West Midlands        | 2,296    | 3,241         | 2,718    | 852    |
| Yorkshire and Humber | 2,095    | 3,382         | 3,004    | 680    |

Source: Dataloft, Land Registry as at 13<sup>th</sup> October 2017; Registers of Scotland as at 1<sup>st</sup> November 2017



UK property prices grew 2.3%  
Y-o-Y in Q3 2017



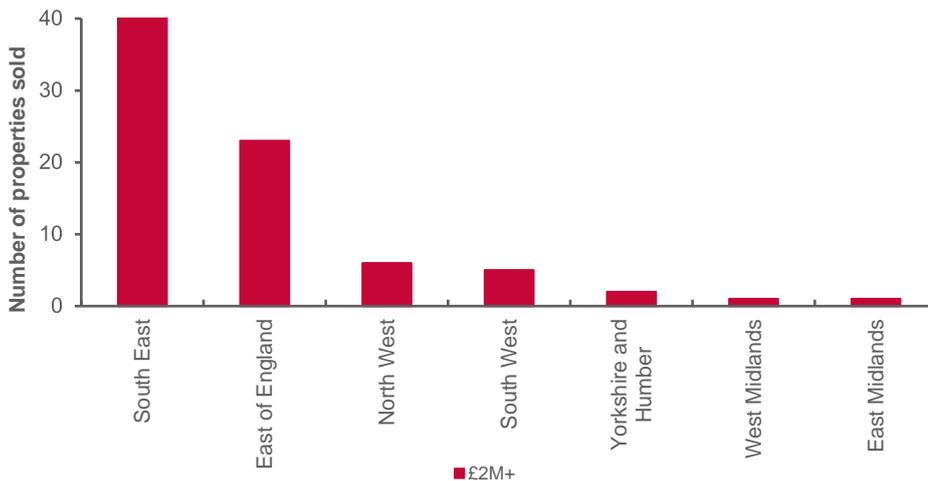
National house prices are now  
19% above September 2007,  
according to Land Registry

## Country house highlights

The majority of homes sold over £2 million so far in 2017 has been seen in the South East and South West, as the London ripple effect with increases seen in both Yorkshire & Humber and the North West.

Our buyers employment industry for this market have changed compared to the same period last year with an increase in both, finance (31.5%) and technology (9.0%) compared to 18.6% and 4.7% respectively.

*Figure 2*  
Number of recorded properties sold over £2M in England & Wales excluding London in Q3 2017



Source: Dataloft, Land Registry as at 13<sup>th</sup> October 2017

*“Despite the slowdown in UK house price growth, the residential market remains active, and Strutt & Parker has recorded an 8.3% annual increase in the number of transactions concluded across the country. Over the past quarter we have seen the impact of political and economic uncertainty on house prices spread from prime central London out to the residential market around the M25, although sensible pricing and other adjustments by all parties can help the market in the commuter belt from becoming stagnant.”*

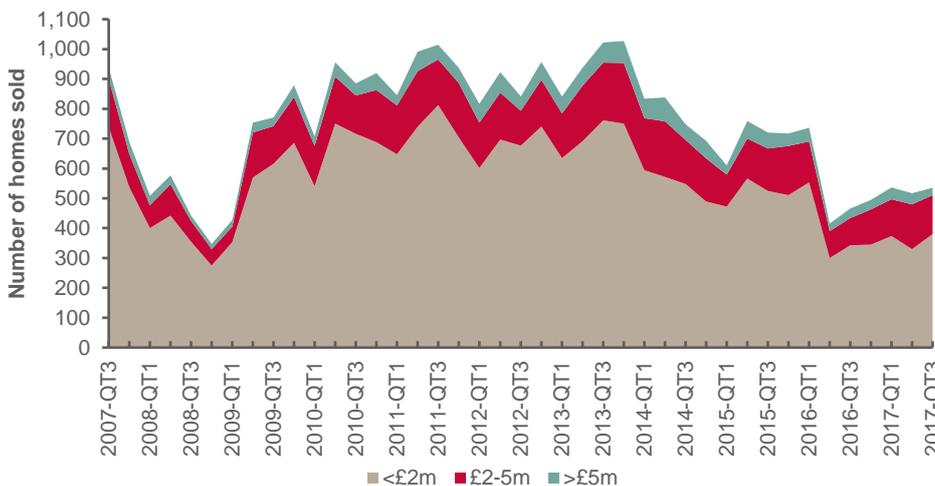
**Guy Robinson**

Head of Residential Agency

## Prime Central London residential sales market

Whilst transaction levels have been gradually increasing during 2017, according to Lonres, transactions in PCL remain considerably below the five year average. Overall PCL transaction levels remain dominated by the sub £2m bracket in the third quarter of 2017 with lower levels of transactions in the £2m-£5m and £5m+ brackets which are more sensitive to political upheaval or negative news.

*Figure 3*  
Historic number of sales in PCL

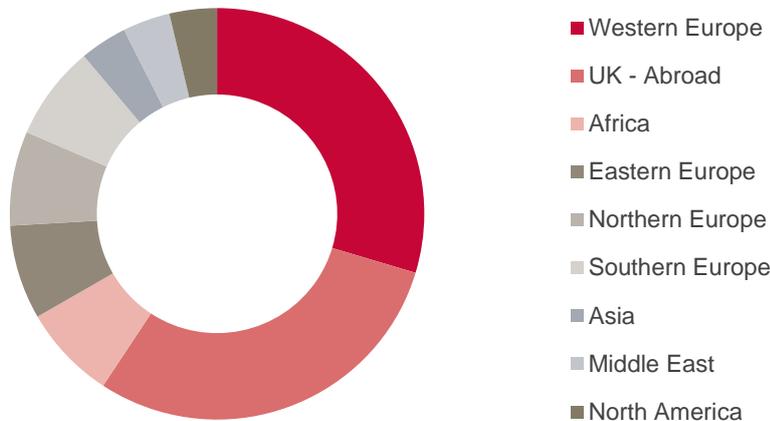


Source: Dataloft, Lonres.com, Strutt & Parker as at 1<sup>th</sup> October 2017

While our agents had reported that new buyer registrations were up during the second quarter of 2017, the Stamp Duty Land Tax (SDLT) for second homebuyers along with a progressively harsher tax system for the wealthy is continuing to be reported as having a severe impact on PCL house prices.

However, even with the SDLT challenges, the continued weakness in Sterling following Brexit has attracted overseas purchasers and assisted the higher value market sector activity to a degree.

*Figure 4*  
Known PCL buyer nationalities for Q3 2017 (excluding UK domestic market)

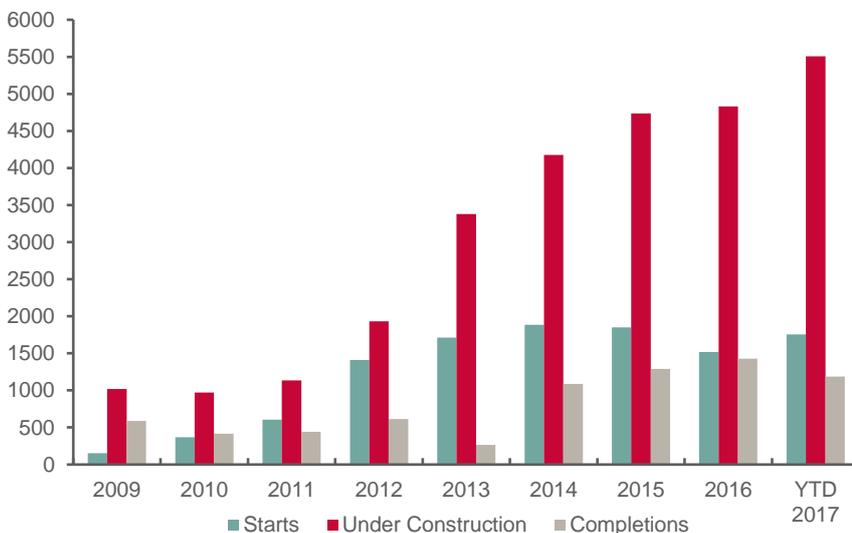


Source: Strutt & Parker

### Prime Central London residential new homes

According to Molior, there were just over 21,000 units that began construction over the first three quarters of 2017 across Greater London. This is a 17.5% increase compared to the equivalent period in 2016. In addition, there have been nearly 18,000 units completed across Greater London in 2017, which is a 14.5% increase on last year also for the same time period. These positive figures however, mask the decline in completions we have seen so far in PCL which is due to a combination of factors, such as: rising material costs, labour shortages and some revised planning permissions for re-scaling of unit sizes.

*Figure 5*  
Construction status of new homes in PCL



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

*“Prime Central London tends to be ahead of the curve in reacting to the political and economic mood, and it experienced a marked slowdown a year and a half ago. Seller expectations are realigning in most situations, with appropriate asking price adjustments. As we head into 2018, we envisage seeing a more active market with an increase in the number of buyers and sellers alike.”*

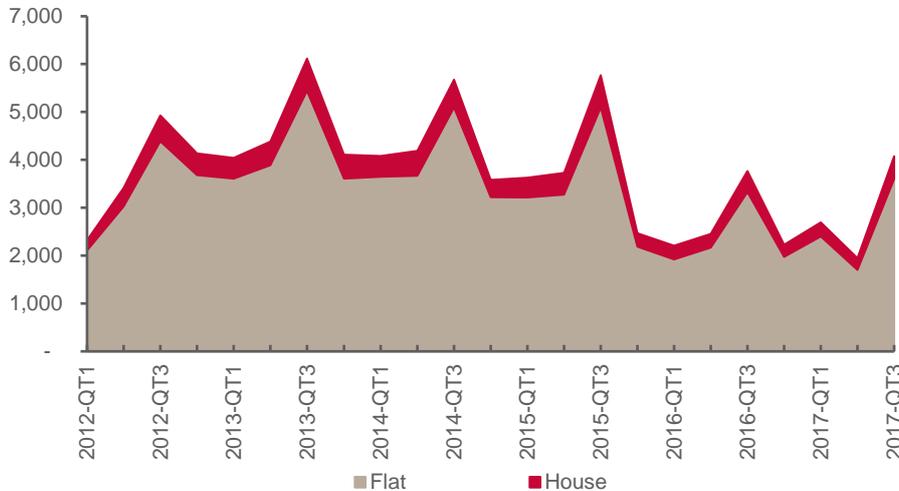
### Charlie Willis

Head of London Residential Agency

## Prime Central London lettings market

The take-up of new rental tenancies across PCL increased by 8.3% in the third quarter of 2017 compared to the same time last year. However, this positive quarter is down 19.8% on the five-year average for the quarter.

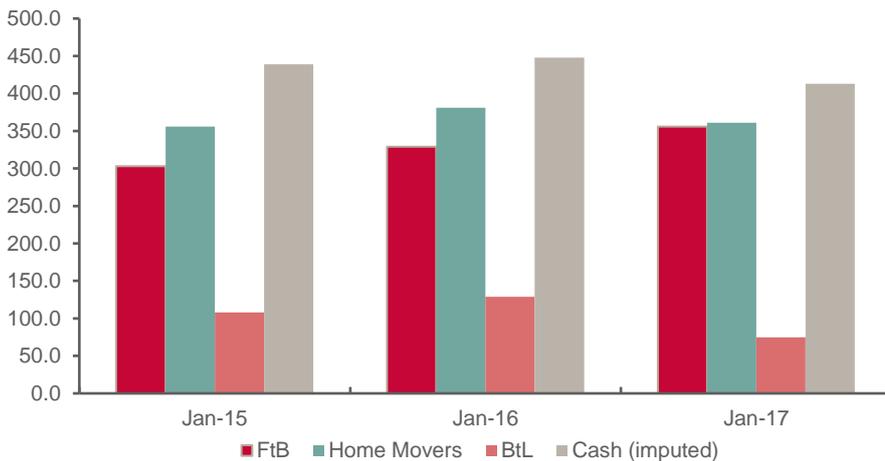
**Figure 6**  
New rental tenancies in PCL by house type



Source: Dataloft, Lonres.com as at 11<sup>th</sup> October 2017

The buy-to-let (BtL) mortgage market as well as cash purchases have seen a recent decline, according to UK Finance, as the housing market activity has seen a moderate shift towards first-time buyers (FtB).

**Figure 7**  
Rolling 12-months Sum of Activity (thousands)



Source: UK Finance – September 2017 commentary, as at 31<sup>st</sup> October 2017

However, even with the slight decline in new BtL purchases across the UK, HomeLet is reporting via their tenant referencing service the combined boroughs of Kensington & Chelsea and Hammersmith & Fulham are attaining an average rent of £1,876pcm, a 2.9% annual increase.



UK Average Rent: £927pcm  
(HomeLet)

## Outlook & forecast

Previously it was believed much of the downward pressure on PCL house prices due to Brexit and SDLT had already been experienced. However, prices in the high value brackets have continued to fall and transaction levels, which at one point appeared to be picking up, have now fallen again and although the UK and the world remain in a period of substantial economic and political uncertainty, the outlook for the UK is reasonable.

The immediate focus should still be on how Britain will fare in the Brexit negotiations. Ongoing discussions will hopefully shed some light on which issues have been discussed and to what extent they have been discussed. The weaker pound has been an incentive to international investors to buy UK property but if the US Dollar slides it may lose some comparative advantage.

Transactions, despite showing signs of picking up have now decreased again and remain very low by historic standards. It looks increasingly likely that 2017 will experience growth closer to our downside risk scenario of -5%. Realistic pricing and the continued attractiveness of Sterling will continue to be key factors affecting market activity levels in the higher price sectors. We expect this stagnation in activity levels and prices to persist in PCL during 2018 as globally and domestically the economy and political environments remain volatile. From 2019 onwards it is extremely difficult to forecast this market with any certainty but we would expect some bounce back once more stability has returned.

Table 2. Residential price forecast Q3 2017

| Sales  | 2018  | 2019 | 2020 | 2021 | 2022 | 5 Year to 2022 |
|--|-------|------|------|------|------|----------------|
| Prime Central London<br><i>Best case</i>     | 0.0%  | 4.0% | 5.0% | 6.0% | 6.0% | 23.0%          |
| Prime Central London<br><i>Downside risk</i> | -5.0% | 0.0% | 1.0% | 2.0% | 2.0% | 0.0%           |
| UK   | 2.5%  | 2.5% | 4.0% | 4.0% | 4.0% | 18.0%          |

| Lettings             | 2018 | 2019 | 2020 | 2021 | 2022 | 5 Year to 2022 |
|----------------------|------|------|------|------|------|----------------|
| Prime Central London | 1.0% | 1.5% | 2.0% | 2.5% | 2.5% | 10.0%          |

*“In the face of far from optimum conditions, it is forecast that the UK economy will grow by 1.6% over the whole of 2017, while forecasts for 2018 and 2019 have been downgraded to 1.2% and 1.4% respectively. While political and economic conditions remain uncertain, we have seen slower than expected house price growth. With the current Brexit negotiations underway, we continue to maintain that from 2019 onwards it is extremely difficult to forecast the housing market with any certainty, but we would expect some bounce back and a return to growth once more political stability has returned.”*

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## Contact us

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#### Methodology

As the housing market is seasonal, for the purposes of this report, data is compared year on year, i.e. looking at Q3 2017 in light of changes since Q3 2016. 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.

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