RESEARCH & FORECASTING UK

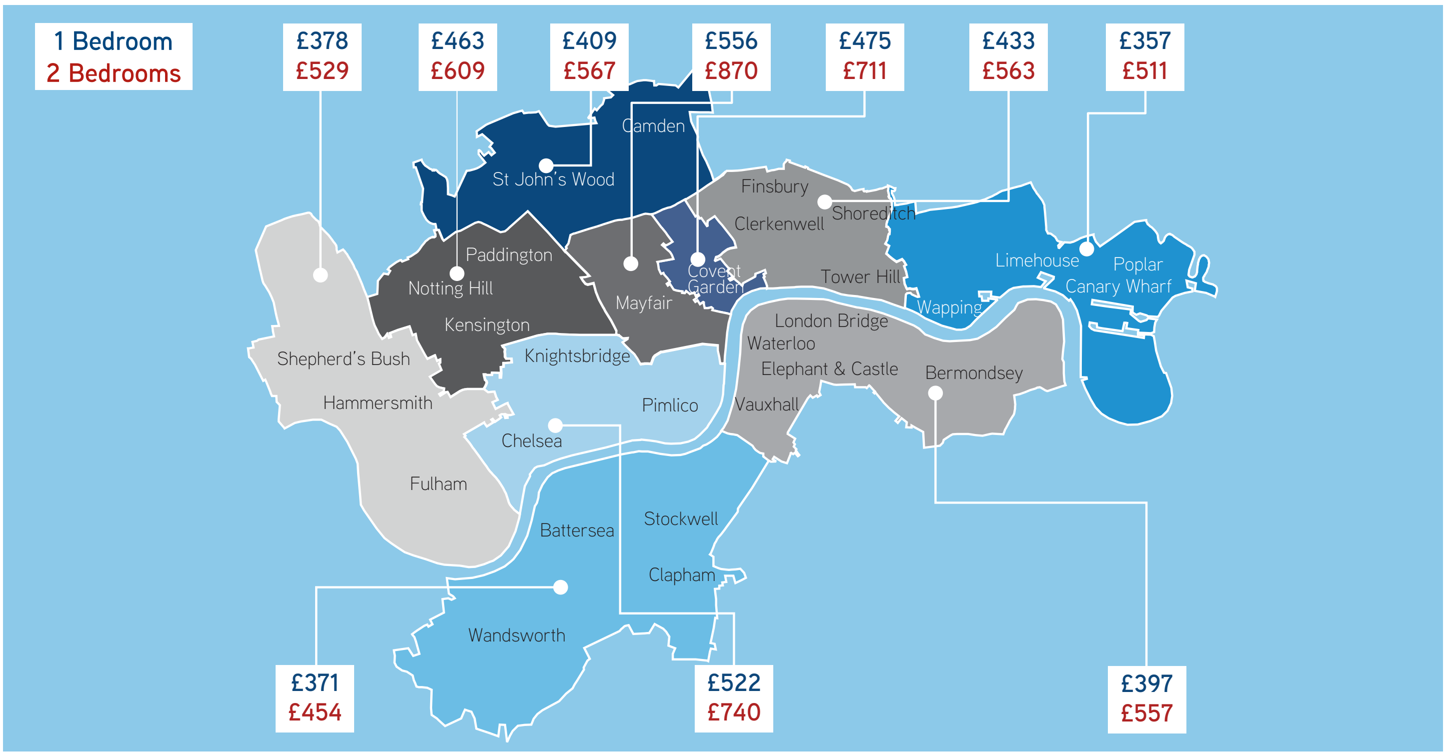
CENTRAL LONDON RESIDENTIAL

Central London Residential Market

The Central London residential market remains attractive to foreign buyers, investors, commercial property companies, developers and private domestic buyers because of its stability and liquidity. The devaluation of the pound in 2008 helped to make London more affordable; however, much of this affordability for domestic buyers has since been eroded due to domestic and global economic difficulties. Foreign buyers, both private and corporate, have not found the same affordability difficulties as UK buyers. It was reported recently by Wetherells, a Mayfair residential property specialist, that 70% of sales in the Mayfair area in 2012 were to overseas buyers. According to LonRes, foreign investors spent £5.2bn in 2011 from a wide range of nationalities.

The economic and political uncertainty in the eurozone has only served to bolster London's status as a global "safe haven" for high net worth individuals and families seeking capital protection. The UK's strong reputation in higher education is another draw for international students and their families. Italians, Russians and the French were the most active investors in the private residential market in 2012. In the latter part of 2012, due to the higher tax rates in France, there was an increase in interest from both French and returning British ex-pats. Chinese and other Asian buyers have tended to focus on the prime residential areas of London, such as Kensington and Chelsea and along the River Thames, in upper price bands and in new build high-rise flats, more than on the resale markets.

FIGURE 1: CENTRAL LONDON 1 & 2 BEDROOM RESIDENTIAL FLATS AVERAGE RENTS ACHIEVED PER WEEK



Source: LonRes, Colliers International

LENDING

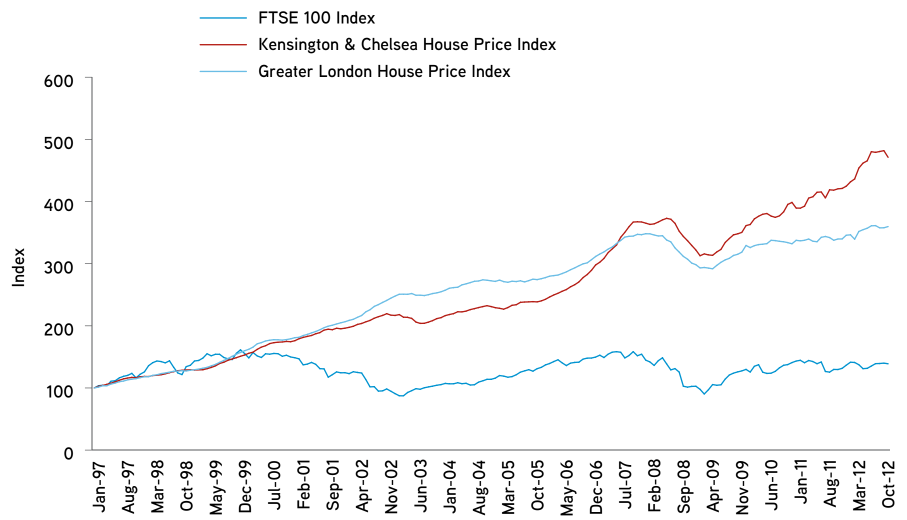
The lending environment in the UK residential market is still very difficult – so much so that the government has launched several initiatives since March 2011 designed to increase lending to first-time buyers in particular. First-time buyers have been squeezed out of the market as banks have tightened their lending criteria. These initiatives have been moderately successful, but have failed to ignite the market through significant increased mortgage borrowing.

Amongst the new initiatives for first-time buyers was the FirstBuy Scheme launched in the March Budget 2011. This is a shared equity scheme allowing first-time buyers to pay a lower deposit, with the government and developer providing 20% as a low interest rate loan. A year later, the Chancellor announced the Newbuy Scheme in the March 2012 Budget. This scheme is the first to offer 95% mortgages on properties up to £500,000. And finally, the Bank of England launched the Funding for Lending Scheme. The £80bn emergency lending facility saw the Bank of England make low-cost funds available to banks and building societies with the aim of passing the savings onto borrowers. The objective is to tackle rising borrowing costs and a drop in lending, which has fallen by 16% since its peak in 2008.

According to the Bank of England, Credit Conditions Survey (Q4 2012), the three months to December saw a substantial increase in the availability of secured credit to households. Amongst the lenders who took part in the survey, the Funding for Lending Scheme was reported as one of the main reasons for this increase alongside improving funding conditions.

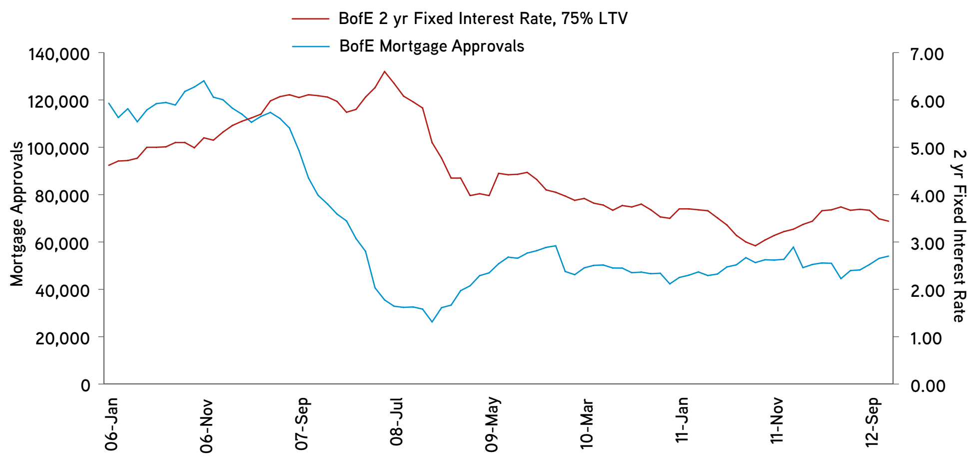
The number of mortgage approvals reached 54,036 in November 2012 (see **Figure 3**).

FIGURE 2: LONDON RESIDENTIAL OUTPERFORMANCE



Source: Haver Analytics, Land Registry

FIGURE 3: MORTGAGE APPROVALS



Source: Bank of England, Haver Analytics

FIGURE 4: MAYOR OF LONDON'S CIL AGREEMENTS

Local Authority	Site Name	Units	Habitable Rooms		CIL	
			Total	Private	Total (£s)	Per Priv. Hab. Room (£s)
Hammersmith & Fulham	Stewarts Garages	107	352	299	380,813	1,274
Hammersmith & Fulham	84-88 Fulham High Street	58	192	179	272,000	1,520
Lambeth	Land at Blairderry Road	66	186	140	146,685	1,048
Newham	Strand East	1,200	3,662	3,282	3,642,640	1,110
Southwark	St Mary's Tower (Former Swimming Pool)	284	747	747	997,465	1,335
Southwark	Stead Street Car Park	140	445	170	537,985	3,165
Tower Hamlets	58-64 Three Colts Lane	149	424	305	375,025	1,230
Tower Hamlets	Riverside Industrial Estate	109	316	211	222,670	1,055

Source: Molior

LAND VALUES

The continuing high level of demand from overseas buyers for new build residential property in prime Central London and along the Thames has resulted in intense competition from developers for sites where local plans allow housing or where planning permission for residential is likely. Well-known national house builders like Barratt and Redrow, who in previous years hadn't focused on the capital, have increased their specifications to compete in a profitable market – profits which still elude them in most of the UK. They are now competing with the more niche high-end developers for the limited number of possible sites and pushing up prices. This has resulted in developers pushing the boundaries of what could be considered to appeal to high-end and foreign buyers into areas of South and North London that have good transport links to the centre. Consequently, there has been strong competition between these private developers and well-capitalised housing associations and social landlords who have traditionally been more active in these areas. Equity funding for land acquisition is abundant, but bank debt is still expensive and difficult to obtain.

DEVELOPMENT PIPELINE

The Community Infrastructure Levy (CIL) is a charge on new developments that can be used to raise money to provide facilities and infrastructure. With all new construction starts this will be a factor in gaining planning permission for any prospective developments. Local authorities have been given the power, but are not required to raise a charge. This means that, if they choose to do so, local authorities can secure planning gain exclusively from either Section 106 payments, CIL or a combination of both.

In London both the London Boroughs and the Mayor of London can charge the new levy. The Mayor has introduced a Mayoral CIL on all new developments from 1 April 2012 to raise £300m towards the delivery of Crossrail. The levy will be charged according to three zoned area bands. The most expensive zone is Zone 1 (£50 per sq m), Zone 2 is £35 per sq m and Zone 3 is the cheapest at £20 per sq m. The idea of the levy is to provide a faster and more transparent alternative to the current system.

Since its inception, 32 relevant permissions have been granted. Analysis (by Molior) shows that the average CIL contribution is £1,132 per private habitable room. **Figure 4** gives an overall view of the Mayor's CIL agreements.

The lack of suitable development sites in central areas may be about to ease due to the government's proposed changes to the planning system. Planning minister Nick Boles' push for more favourable 'change of use' from commercial to residential and 'Permitted Development Rights' could have a profound effect on the availability of residential development sites within prime Central London. Changes first intimated two years ago are likely to become policy, freeing up many well-located but commercially redundant office buildings for residential development. Previously, rules regarding employment and restrictions on change of use prevented many schemes, but the new rules combined with as much as 50% higher capital values achievable on residential schemes as opposed to commercial could considerably increase the supply of well-located residential developments.

There are 105 development schemes in Central London under construction, equating to 8,645 homes, of which 53% have been sold off-plan (see **Figure 5**).

43 schemes completed in 2012, equating to an extra 2,878 units in Central London. Of those 43 schemes, 15 have unsold units (see **Figure 6**).

FIGURE 5: CENTRAL LONDON RESIDENTIAL UNDER CONSTRUCTION PIPELINE

	Construction		Sold	
Local Authority	Schemes	Homes	Homes	Percent
Camden	7	379	204	54%
City of London	4	479	364	76%
Hackney	16	1,151	560	49%
Hammersmith & Fulham	8	757	325	43%
Islington	12	769	312	41%
Kensington & Chelsea	6	593	338	57%
Lambeth	8	794	308	39%
Southwark	20	1,475	878	60%
Wandsworth	17	1,622	908	56%
Westminster	7	626	360	58%
Central London	**105**	**8,645**	**4,557**	**53%**

Source: Molior

FIGURE 6: CENTRAL LONDON RESIDENTIAL SCHEMES COMPLETED IN 2012

Local Authority Completions			Unsold		
Details	Schemes	Units	Schemes	Units	Percent
Camden	3	84	2	12	14%
City of London	0	0	0	0	n/a
Hackney	8	819	1	28	3%
Hammersmith & Fulham	1	71	0	0	0%
Islington	10	631	4	28	4%
Kensington & Chelsea	1	56	0	0	0%
Lambeth	1	114	0	0	0%
Southwark	5	346	2	14	4%
Wandsworth	5	276	1	12	4%
Westminster	9	481	5	17	4%
Central London	**43**	**2,878**	**15**	**111**	**4%**

Source: Molior

FIGURE 7: ANNUAL RESIDENTIAL PROPERTY TAX CHARGE STRUCTURE

Amount of Charge	House Price Brackets
£15,000	£2m-£5m
£35,000	£5m-£10m
£70,000	£10m-£20m
£140,000	>£20m

Source: Colliers International

INVESTMENT

Stamp Duty Land Tax (SDLT) of 7% and 15% for residential properties worth more than £2m was introduced in March 2012 to deter SDLT avoidance. In the Autumn 2012 Budget, the most welcome news was that the Chancellor ruled out a "blanket" annual tax on all UK homes worth £2m plus. However, the Finance Bill, passed on 11 December 2012, saw the introduction of the annual charge on UK residential properties over £2m held in corporate structures – at 1% of their total value. The measures take effect on April 1 2013 (see **Figure 7**). In addition, capital gains tax will become payable on capital gains accruing on or after 6 April 2013 only. It will take time to realise how much the additional taxes will affect the prime London residential market; however, a period of static house prices in 2013 will be expected as a result. It was unclear at the time how this would affect the Central London luxury residential market with the majority of the buying activity coming from abroad, but it appears that the introduction of the new SDLT regulations has caused some international buyers to reconsider the Central London residential market as the best option for their investment.

In a recent article from the FT, demand is reported to have fallen in the Central London super luxury residential markets. In our own survey on SDLT, we found that some of the purchasers in this market were very keen to keep their privacy, whereas, this tax forced them to make public their purchase. In a related article in the FT, the very same wealthy families who would have bought flats for their children studying in London are now renting flats for their children at the high end of the market, thus inflating rents. Anecdotally, estate agents in Central London are reporting an increase in the number of foreign student lettings in the capital.

We have found that the £2m-£5m sales bracket in the UK market has been the hardest hit. Anecdotal evidence suggests that the most affected areas are those outside of prime Central London where foreign buyers are less active and domestic purchasers largely prevail.

SALES ACTIVITY

Our analysis of average sales prices per sq ft for July – October 2012 shows that although average sales prices in the Kensington and Chelsea area are above £1,000 per sq ft for both one and two bedroom apartments, the highest achieved sales price per sq ft was for two bedroom apartments in the combined Marylebone, Mayfair and St James' areas, at £1,491 per sq ft.

The highest average sales price achieved in Kensington and Chelsea during this period for a one bedroom flat was £3.2m. For two bedroom flats, a price of £4.7m was achieved. In Marylebone, Mayfair and St James' the highest average sales price achieved was £3.8m.

RENTAL ACTIVITY

The rental market in London remains strong as many would-be buyers, priced out of the market, are forced to rent. It is no surprise that London saw the highest rental growth figures as demand exceeds supply. Average rents in London peaked at more than £1,000 pcm in 2012 and look set to continue their upwards climb.

Our rental analysis shows that the highest rents were in Marylebone, Mayfair and St James'. Average rents for a one bedroom apartment in these areas is around £556 per week and £870 per week for two bedroom flats.

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