SPOTLIGHT
Savills Research

Mainstream Residential Rental Property Forecasts

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Forecasting house prices is a delicate art, relying on an understanding of the complexities of the mortgage debt markets. While rental values are equally difficult to predict, the key driver is at least a little simpler: the balance between demand and supply.

Intense demand pressure

At its peak in July, UK rental growth was running at 12.3%. Rents in London rose by 17.8%.

This is more than just a post-pandemic recovery: rents both in London and nationally had already returned to pre-lockdown levels in 2021. Average UK rents were 14.0% above their pre-pandemic level (March 2020) by August 2022. London rates were 9.8% above.

Having recovered from the rent falls we saw during lockdown, surging demandand dwindling supply are driving rental value growth.

There were -26% fewer homes available to rent in Q3 2022 than the pre-pandemic average, according to data from Rightmove. In London the shortfall was even greater at -30%. At the same time, the monthly RICS survey shows that demand from prospective tenants nationally has increased in every month since May 2020.

These measures suggest that today's high levels of rental value growth will persist across the country through the coming months.

There are simply more people wanting to rent homes than there are homes available

What's to stop this situation persisting forever? On the one hand, we may see rental demand decline: given the rising cost of mortgage debt and limited supply of affordable housing, this seems exceedingly unlikely.

On the other hand, we could see an increase in rental supply.

Landlords return

While we expect transaction activity to slow in the coming years, many of the factors driving home moves will still continue as normal. Couples will continue to move in together. Workers will continue to take up new jobs halfway across the country. And, sadly but inevitably, the estate agent's friends death, debt, and divorce will continue to force moves.

The owners of these properties will face a choice. They can choose to sell into an uncertain, illiquid market. Or they can hang back, rent the property out for a few years, and wait for things to look a bit clearer. These accidental landlords will increase the supply of homes to rent, helping to ease the imbalance between demand and supply and stabilising rental growth at more sustainable levels.

Investor demand for homes for rent remains strong

The decision these homeowners make will depend on how long ago they bought and the strength of local demand. Someone who bought a flat in London last year, for instance, may feel uncomfortable selling 10% below their purchase price, so will be more likely to let the property out. For someone else who bought their house in the North West ten years ago (over which period prices have risen 58%), selling at a 10% discount to their home's notional value a year ago will smart somewhat less.

We can expect to see an increase in deliberate landlords too. Investors, particularly those with cash to hand or that have registered as limited companies, will take advantage of price adjustments to secure stock with less competition from mortgaged owner occupiers. Institutional investor demand for purpose-built homes for rent remains strong, with returns still looking resilient compared to other asset classes.

All this suggests that rental supply will rise again. Meanwhile, rental demand will remain strong as long as interest rates remain high enough to frustrate aspiring first-time buyers, keeping them renting for longer. That suggests we see rental growth stabilise in line with its long-term correlation with earnings growth, rather than affordability easing beyond that point.

We're predicting UK rents will have risen 10.0% by the end of this year, as the bumper growth months of Q4 2021 fall out of the annual figures. Growth will then slow to 6.5% next year, before slowing further beyond 2024 as renters return to spending a similar proportion of their earnings on housing costs as they did in 2014/15.

Figure 1 Forecast residential rental values

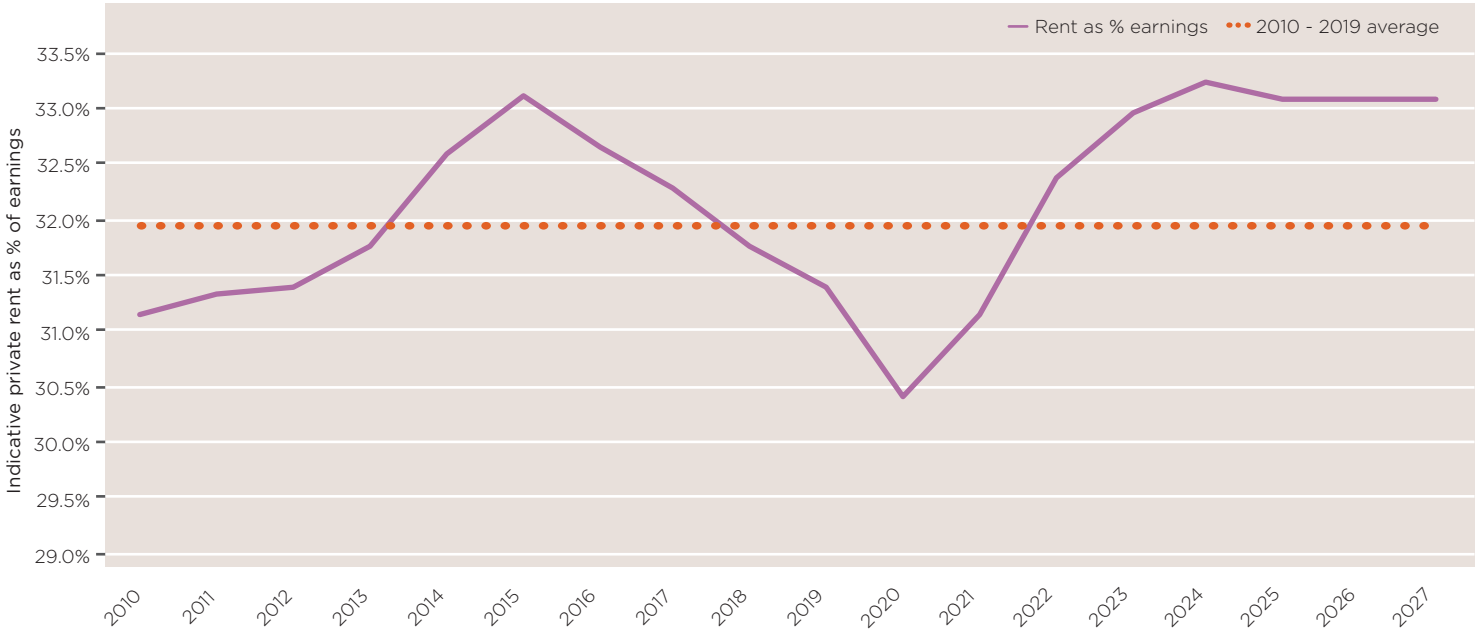
	2022	2023	2024	2025	2026	2027	2022-26 compounded	2023-27 compounded
UK	10.0%	6.5%	4.0%	2.0%	2.4%	2.3%	27.3%	18.3%
London	14.0%	5.5%	5.0%	2.0%	2.4%	2.3%	31.9%	18.4%
UK ex London	9.0%	6.5%	4.0%	2.0%	2.4%	2.3%	26.1%	18.3%
Earnings growth	5.8%	4.6%	3.1%	2.5%	2.4%	2.3%	19.8%	15.8%

Note These forecasts apply to average rental values in the second hand market. New build rental values may not move at the same rate

Source: Savills Research using Oxford Economics 26th October 2022

> **The private rented sector is not without its challenges. The Renters Reform Bill pledges to shift the balance of power further towards tenants, while landlords also face challenges from higher mortgage rates and tougher energy efficiency rules**
> Lawrence Bowles, Director, Residential Research

Figure 2 Impact on rental affordability



Source: Savills Research using Zoopla, Oxford Economics, Rightmove

Professionalising the sector

The private rented sector is not without its challenges. The Renters Reform Bill pledges to shift the balance of power further towards tenants, while landlords also face challenges from higher mortgage rates and tougher energy efficiency rules.

All this points to the professionalisation of the sector. By building management efficiencies into schemes from the design stage, Build to Rent operators can keep operational costs down while providing a high level of service to residents.

It also suggests we should see a growing premium emerge for newer, energy efficient properties. As energy bills continue to rise beyond the end of the Energy Price Guarantee, we can expect households to pay more for the most efficient properties since they offer more stable and lower occupational costs overall.

Lucian Cook
Head of Residential Research
lcook@savills.com
07967 555 418

Lawrence Bowles
Director
Residential Research
lbowles@savills.com
07855 999 466

Jacqui Daly
Director
Residential Investment Research
jdaly@savills.com
07968 550 399

Richard Valentine-Selsey
Director
Residential Research
richard.valentineselsey@savills.com
0203 320 8217

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