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UK Residential
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Spotlight | January 2018

# Prime residential rents

**Summary** Although rents fell in 2017, the lower and super-prime ends of the market are fuelling demand. Property condition, location and closeness to schools remain key factors in a rental decision

Over the course of 2017 prime London rents fell by 3.1%. Yet this was a slower fall than seen previously, suggesting the imbalance between supply and demand in the current market has eased a little.

Despite falling rents, the market has remained active. This activity has been from needs-based tenants at the lower end of the market, fuelling demand for smaller properties, as well as from super-prime tenants at the top end and affluent students.

Rents in the prime rental markets outside London have also fallen by 1.5% over the last year, but their longer-term growth has remained stronger than the capital. Properties that remain popular are those of the highest condition in the most convenient locations.

Schools remain an important source of appeal for larger family properties – international tenants choosing markets located close to the best international schools. As our exit from the EU unfolds, we expect to see more demand from relocators within the diplomatic community moving with their families.

Completing stock from the new build pipeline is likely to suppress rental growth in the capital in the mid-term. We expect confidence to return to the market once we have a better understanding of our future relationship with the EU.

# Prime London rental market is active

Prime London rents continued to soften over the last three months of 2017, leaving them 3.1% down over the year. A high level of supply has continued to hold back rents, with tenants remaining cost conscious in the current economic climate.

But, while rents are sliding, they are doing so at a slower pace. This suggests that the imbalance between supply and demand has eased a little.

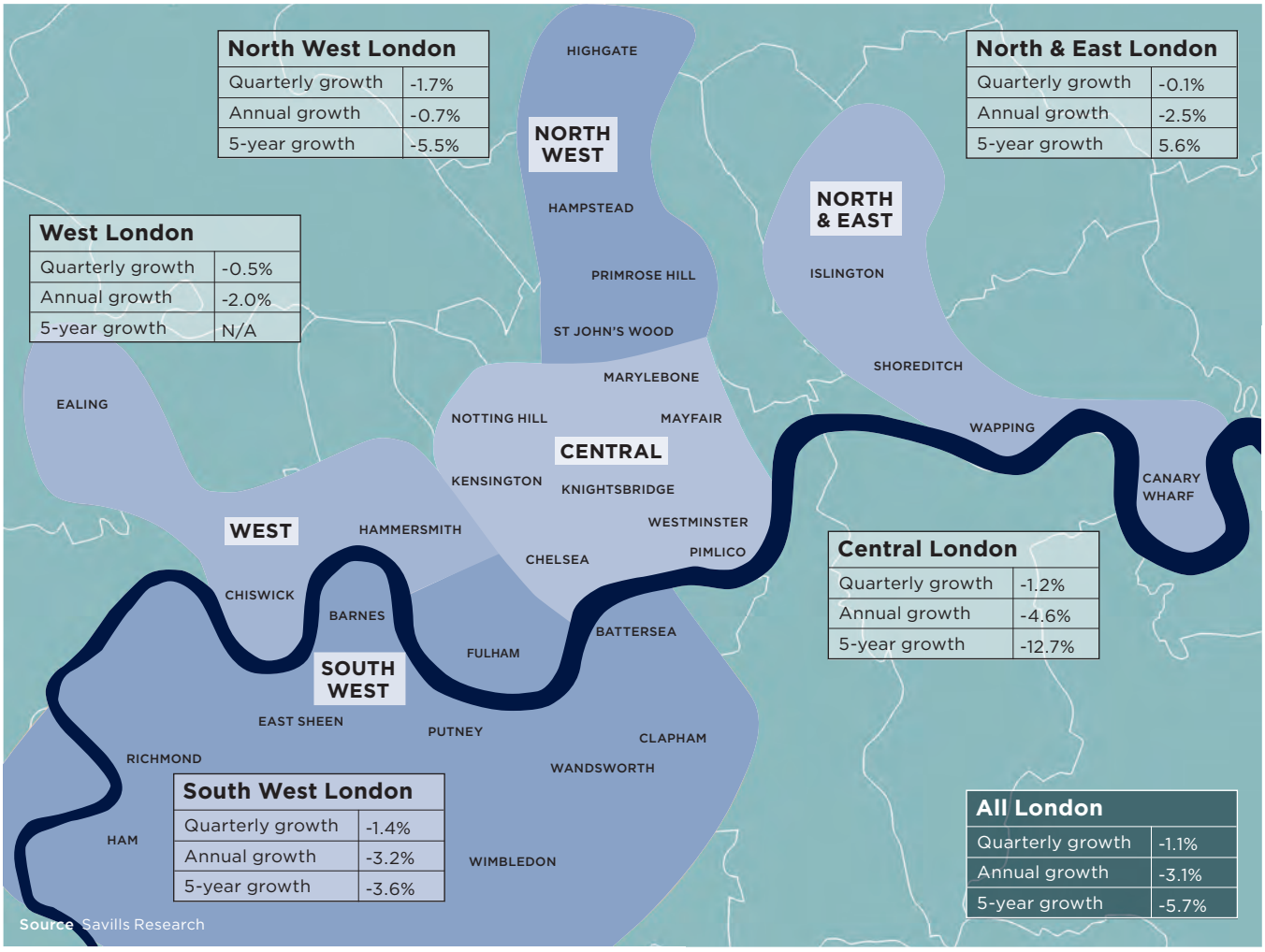
The high levels of stock brought to the market in the immediate aftermath of the stamp duty surcharge of April 2016 appear to have worked through the market. However, increased new build volumes and, to a lesser extent property brought to the rental market by those struggling to sell, provide tenants with significant choice.

Despite falling rents, the market remains active. This is especially true at the lower end of the prime market, where demand has been propped up by more needs-based renters.

At the upper end of the market, demand has been supported by those choosing to rent rather than buy, given the high costs of stamp duty and the underlying political and economic uncertainty.

**-3.1%**
**Rental falls across prime London in 2017**

**Rental values** Prime London rents are down over the year, but the market remains active



Source Savills Research

## Prime country rentals have long-term strength

The story for prime markets within an hour of London is similar to that of the capital. However, rental falls have been to a lesser extent, decreasing by 1% in the fourth quarter of 2017, and by 1.5% over the year. Yet, this was a smaller fall than earlier in the year.

Over the longer term, prime country rental markets have remained stronger than London, with five-year growth of 3.7% compared with falls of 5.7% in prime London.

Across the market, activity levels vary by location. For example, while there has been an increase in corporate demand for top-end family houses in Esher from the recovering oil and gas industry, most other locations are seeing more activity at the lower end of the market from cost-conscious tenants.

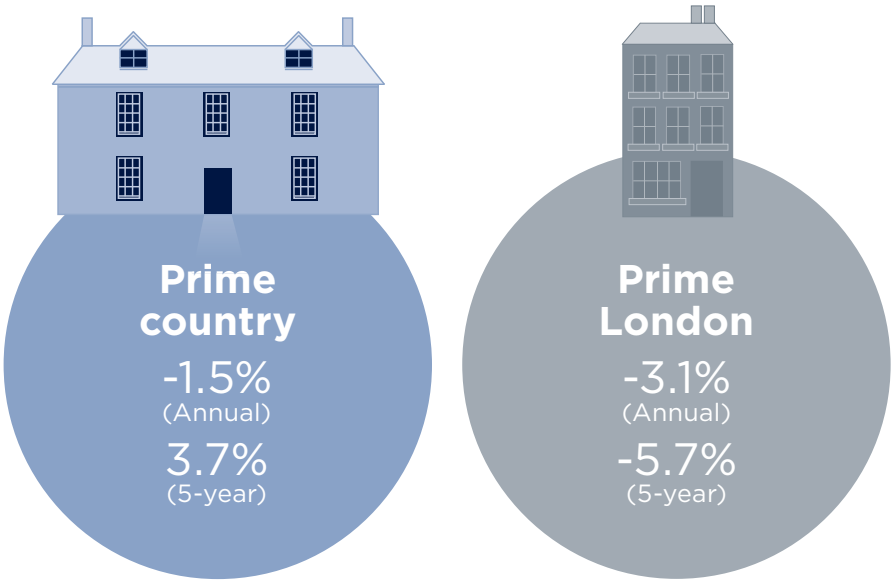
Supply at the top end of country rentals has remained high in most markets, especially with an increase in accidental landlords renting out their property in an uncertain sales market.

As such, we are seeing an increase in void periods. In Beaconsfield, for example, the average time between tenancies has increased from just under one month in 2016 to just over two in 2017.

Properties that remain popular are those in the best possible condition, situated in the most convenient locations.

## Comparing the markets

Prime London rents are sliding, but they are doing so at a slower pace. Even so, longer-term rental growth in prime country markets continues to outperform the capital




**Source** Savills Research

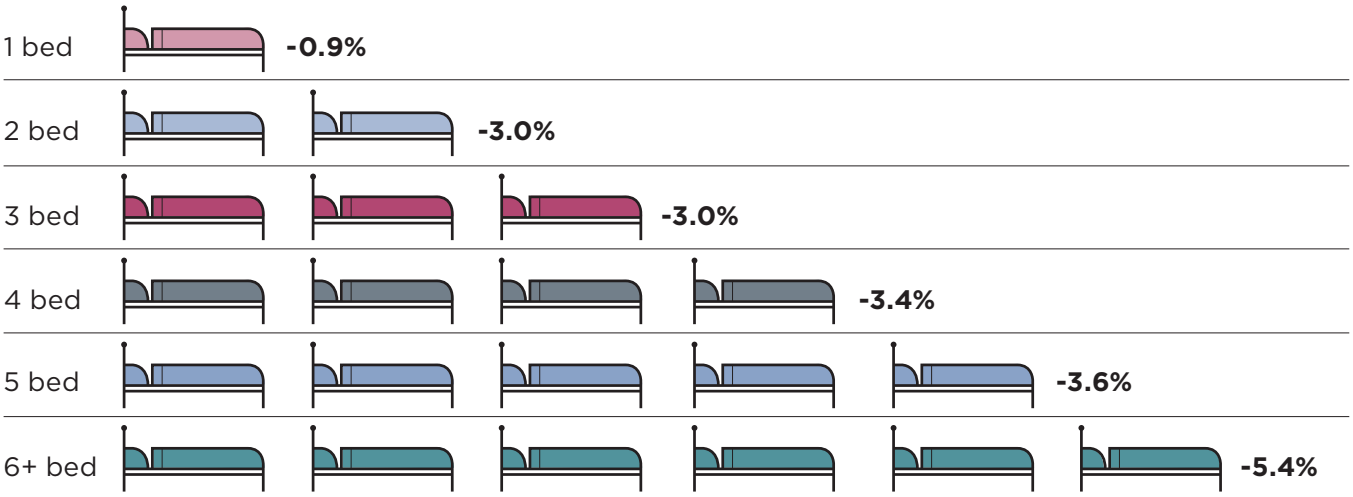
## Schools: international appeal

Larger properties in both London and the country markets continue to remain popular with families looking to live close to good schools, especially international schools.

While Americans favour St John's Wood for the American School in London (above), eastern Europeans prefer central markets for the International School of London. Western Europeans look to Chiswick, Fulham and Richmond, as well as prime markets in Surrey, for international schools located there.

As the Brexit process unfolds, we expect an increase in the number of international tenants working in the diplomatic sector being relocated to London with their families.

**Annual falls in prime London rents by bedroom number** Demand grows for smaller properties




**Source** Savills Research

## Size issues in London

In prime central London, markets which provide better value for money, such as Earl's Court, Pimlico and Marylebone, have fared better than the more expensive areas.

Some of the markets are those with a large new build supply pipeline – a situation that has brought them to the attention of a wider range of tenants. This is especially true for Marylebone, with half of Savills renters relocating here for the lifestyle. But as delivery of new build units increases, existing landlords are likely to find these markets becoming ever-more competitive.

The focus on value also means we are continuing to see more demand for smaller properties than larger ones. This is particularly true for markets in the capital which are popular with affluent students.

A good example of this is Westminster, where such tenants have accounted for 29% of demand over the last two years. As such, rent for one-bedroom properties across prime London fell by just 0.9% over the last year, compared with a fall of 3% for three-bedroom properties and 5.4% for properties with six or more bedrooms.

## Wider choice for tenants

With rents falling in and outside London, we are seeing a shift in the traditional relocation routes of tenants. In 2015, 23% of Savills tenants renting in country markets had moved from the capital. In 2017, it was 19%.

High supply in the London market is allowing tenants to get more for their money, and they have become increasingly footloose in their choice of location. However, the country market still holds significant value compared with London markets – a move from Wandsworth to Weybridge, for example, would save 40% in renting the same-sized prime property.

> "High supply in the London market is allowing tenants to get more for their money"

## Outlook

Following the stamp duty surcharge, we have seen a decrease in the proportion of people buying a property for investment across the prime markets. This higher tax bill is likely to make potential investors think twice before expanding their portfolio, and the recent interest rate rise and cut in interest tax relief will limit how far mortgaged investors can stretch themselves. This is likely to mean there is less secondhand stock coming to the market.

However, new build completions across the prime London market, some of which were delayed following the Brexit vote, are expected to peak in 2019 and 2020. This means the current imbalance of supply could continue, limiting rental growth.

In terms of demand, we expect there will be continued uncertainty surrounding the UK's exit from the EU, which could also impact the corporate relocation market. It could also lead to longer-term accidental tenants who choose to wait out the sales market.

Given current market stock levels, we expect rental falls to continue in the short term, with a fall, over 2018, of 3% in London and 1% in the commuter belt. But, by 2019, we should have a better understanding of where we stand with the EU, bringing a degree of confidence to the market, though stock levels from the new build pipeline will result in a slow recovery of prime rental values.

Markets outside the capital have far less new build stock in the pipeline and have experienced smaller falls, with a view that they will recover slightly more strongly over the next five years.

Landlords will need to bear the current climate and supply in mind, remaining flexible on price and focused on the condition of their properties to remain competitive with the new build stock.

The rising popularity of short-term lets means tenants' expectations have changed – to appeal to a younger demographic landlords should also consider what they include in a rental package and remain flexible on terms.

We believe capital values are likely to increase at a stronger pace than rental values over the next five years, with a forecast of 20.3% growth in prime central London, 10.2% in outer prime London, and 14.2% in the commuter zone by 2022. Landlords will need to take a mid-term view to see the forthcoming years as an opportunity for asset wealth generation.

**Prime rental forecast** We expect rental falls to continue in the short term

| | 2018 | 2019 | 2020 | 2021 | 2022 | 5-year compound growth |
|---|---|---|---|---|---|---|
| Prime London | -3.0% | 1.0% | 2.0% | 4.0% | 3.0% | 7.0% |
| Prime commuter zone | -1.0% | 1.0% | 2.0% | 3.0% | 3.0% | 8.2% |

**Source** Savills Research **Note** These forecasts apply to average rents in the secondhand market. New build values may not move at the same rate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