research

from Hurford Salvi Carr

MIDTOWN, CITY AND DOCKLANDS

RESIDENTIAL REVIEW 1ST HALF 2013

Hurford Salvi Carr is an innovative firm of property advisors and development consultants who have become synonymous with urban living in central London. Our experience and expertise in both the residential and commercial markets, in the City, West End, Docklands and East London puts us at the forefront of property agency.

Since 1996 Hurford Salvi Carr has been a driving force of the 'city living' phenomenon having sold more than 4,000 new homes in over 300 developments, the majority created from former commercial premises, and we have played a pivotal role in the repopulation of Bloomsbury, Clerkenwell, Shoreditch and the City.

As real estate agents we are widely respected throughout London and are well known in property circles around the world. Our reputation is based on the accuracy of our advice, the quality of our marketing, and most importantly for achieving results.

The Company is divided into six divisions, specialising in Residential Sales, New Homes, Residential Lettings, Residential Investment, Commercial Agency, and Property Management. In many instances the skills of each division combine to provide our clients with best advice. Our fresh approach and award winning on-line marketing expertise complement our service.

We are committed to providing a personal service to each of our clients and we maintain the highest standards in every aspect of our business.

HURFORD SALVI CARR

Overview

PRICES RISE, RENTS FALL

Capital values and rental values moved in opposite directions in the first half of 2013. Strong price rises in the City, Midtown and Docklands contrasted with falling rents across much of the same area. Only in Midtown was there any uplift in rental values. The result is that investments yields have declined and we expect further decline over the next 18 months, as the supply of rental property being delivered by the current building boom, expands.

January 2013 turned out to be one of the most active sales markets since our records began in 1996 and, from memory, long before that, in all sectors. Buyers were out in force and show-flats drew flocks of keen purchasers. The sensational launch of Battersea Power Station, when mustard-keen buyers queued up to hand over their deposits, set the tone for the first six months of the year. In our own markets, the competition to buy was intense and best bids became commonplace in Q1. Although supply began to dry up and the rate of sales slowed down in early summer, the pace of the first six months left the price of a one bedroom flat in the City up by 6%, in Midtown by 5% and by 2% in Docklands.

These price rises were boosted by the influx of overseas capital but 54% of our buyers in 1st half 2013, were well-resourced and UK-based, investing in buy to let or as a second home.

The flat or falling values of rental property reflect the increase in supply coming to the market via buy to let investors. One bedroom flats have held their value better than two bedrooms which have dropped by as much as 11% in the City since the beginning of the year. It seems that renters prefer to rent a smaller property rather than compromise on location. Midtown bucked the trend in rental values and here, there were increases of 5% for two bedroom and 6% for one bedroom flats because the supply of rental accommodation remains restricted to older stock. Demand for rental property in London peaks in the summer months and we expect values to stabilise over the second half year.

The buoyant sales market unrolled against the backdrop of a lacklustre UK economy, although by the middle of the year there were more encouraging signs. The early months of 2013 did not bring economic recovery to the UK despite high hopes in the last quarter of 2012. GDP grew by 0.3% in the first quarter – narrowly avoiding a slide back into recession but it was hardly a comfortable margin - and the UK's GDP remains smaller in 2013 than it was five years ago, before the financial crisis. In February, the UK lost its triple A rating from Moody's. The mood lifted in the early summer with the announcement of some more positive news.

In May, The Chartered Institute of Purchasing and Supply (CIPS) reported growth in the services sector. Services account for three quarters of the UK economy and range from IT and accountancy to hotels and restaurants. The evidence of growth led the survey compilers to forecast GDP growth of 0.5% in Q2 – a slight improvement on Q1. If they are right, it would mean two successive quarters of growth for the first time since 2011. Also in May, the Bank of England revised its output forecast for 2013 upwards to 1.5% (from 1.2% at the beginning of the year) although Mervyn King, outgoing governor of the Bank of England continued to advise caution, pointing out that rebalancing the UK economy would be a long slow process.

The stock market, which is an accurate indicator of confidence, flourished throughout the first six months of 2013 – the FTSE index climbed to 6300 in January, was 6444 in March and by May it had reached 6557. Share offerings for Countrywide and Crest Nicholson both produced strong returns for investors who hope to benefit from a house-building boom in London, as the UK tries to meet the ever-increasing demand for homes, with encouragement of government policy interventions such as Help to Buy.

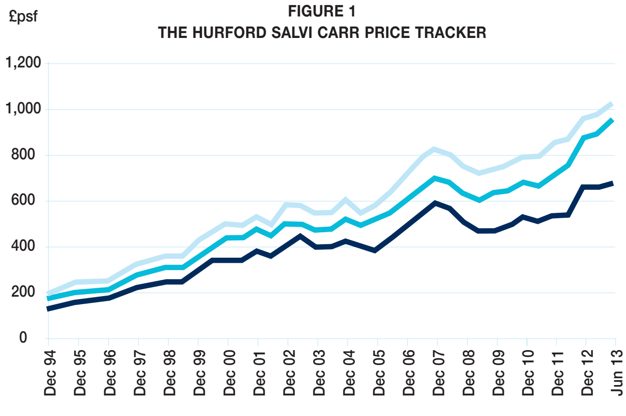
Signals from the Eurozone were less positive and, as long as these economies flounder, the demand to invest capital in the UK remains strong. Q1 2013 was the sixth successive quarter of falling economic output in the Eurozone. The economies of France, Spain, Italy and Netherlands all contracted and even Germany only managed a paltry 0.1% growth. Both Greece and Spain have unemployment rates of around 25% and far higher for their youth and even in France, unemployment reached a record high in April. In March, the financial crisis in Cyprus shocked investors and acted as a reminder that finding a safe haven for capital is highly prized.

However, there were some small victories in the battle to stabilise the Eurozone economies. Greece agreed to austerity measures and the real fear of a break up seems to have abated. In May, the ECB cut interest rates to a new record low and Mario Draghi said that the Eurozone economy is on track for a gradual recovery later in 2013. For the time being however, London residential property remains a highly sought-after commodity for equity rich-investors in the Eurozone economies, attracted by its relatively robust economy and stable political system.

In April, the Evening Standard ran a headline about a house for sale in Carlton Terrace for £250 million. This style of reporting, alongside stories about queues to buy flats in new developments, sent out warning signals of the potential for an overheated market and persuaded some buyers to stand back from the fray so that, by mid April, the market had calmed down.

Nevertheless there are plenty of buyers ready to commit when the right property comes to the market. A third of our buyers in the first six months of the year were buying to let the property and we see no evidence of that changing despite increasing prices and declining investment yields. Buyers are prepared to accept yields that now range between 4.5% and 5% for one bedroom apartments and nearer 4% for larger apartments.

FIGURE 1
THE HURFORD SALVI CARR PRICE TRACKER



Source: Hurford Salvi Carr, CCR

Data based on the value of a 500 sq ft one bed apartment in the re-sale market

Sales Market

BUYER CONFIDENCE FUELS MARKET

2013 dawned with a remarkably strong sales market, fuelled by keen buyers from the UK and overseas and the tone established in the first two months left a lasting impression on the whole of the first half year. So far in 2013, the sale price of a one bedroom flat in the resale market has risen by an average of £3,000 per month.

Our offices agreed and completed on a high volume of sales across all locations at record prices during the first half of 2013.

From March onwards, we detected a reduction in sales enquiries. Buyers in our markets are sophisticated and familiar with the vagaries of investment returns. When the headlines used in the press to announce residential trends become excitable to the point of hyperbole, our typical buyers retreat. It feels overheated. They can bide their time. We see no reason for this change of tempo to translate into a price correction however, since the supply of properties is limited and vendors of second hand properties will withdraw from the market rather than contemplate adjusting asking prices. Equally, when we bring new stock to the market, buyers respond quickly as soon as supply comes through on the website. To that extent, activity levels are stock driven. Our website and online marketing provide the platform to keep buyers informed.

TABLE 1
PRICES AND PRICE CHANGES FOR ONE BED APARTMENTS IN THE RESALE MARKET AT YEAR END : AVERAGE FOR MIDTOWN, CITY AND DOCKLANDS

Year	Annual Price Change	Market Value (£)	Annual Change in Value (£)
1998	N/A	150,000	N/A
1999	26%	189,000	39,000
2000	11%	210,000	21,000
2001	10%	230,000	20,000
2002	13%	260,000	30,000
2003	-8%	245,000	-15,000
2004	0%	246,000	1,000
2005	10%	270,000	24,000
2006	26%	340,000	70,000
2007	9%	371,000	31,000
2008	-15%	318,000	-53,000
2009	8%	338,000	20,000
2010	4%	351,000	13,000
2011	10%	386,000	35,000
2012	5%	405,000	19,000
Mid 2013	5%	425,000	20,000*

Source: Hurford Salvi Carr, CCR   ** half year*

The upshot of such a strong start to the year is that prices rose by between 5% and 6% in City and Midtown and by 2% in Docklands in the first half of 2013.

Several commentators have dared to use the B-word – Bubble - but in our view, this is not a fragile market at risk of bursting. The spiralling prices in the prime market have been driven by a real and long-term desire to invest money in the UK because of its reputation as a 'safe-haven'. Such investors are unlikely to pull out en masse unless there is a dramatic and unforeseen collapse in the UK economy and political system.

A more plausible scenario is that the interest of overseas investors will wane if the exchange rate becomes less favourable or yields become unattractive. UK buyers will continue to invest in residential property within Central London until the point that confidence is dented, possibly when interest rates begin to rise. This would slow capital growth but there is no reason to think it would prompt a race to exit the London Residential Market. Bubbles tend to be fuelled by debt rather than equity and the majority of buyers in the Central London markets today are affluent equity purchasers with deep pockets, who are more likely to sit out any lowering of prices rather than realise a capital loss on these income producing assets. For them, these are discretionary purchases – in other words, they are luxuries (investments) not necessities.

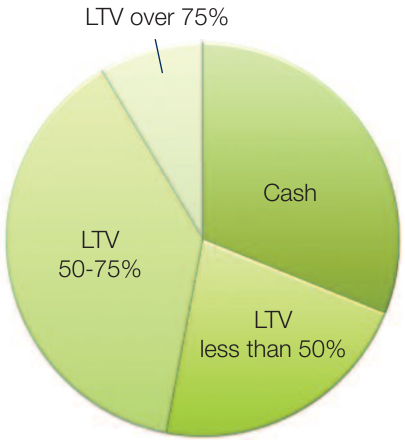
LIMEHOUSE E14 - TWO BED, TWO BATH APARTMENT SOLD APRIL 2013 £560,000

In fact, it is their status as luxuries that has caused so much controversy in the media, with stories of blocks in which almost all the flats are unoccupied despite (or because of) being sold for many millions of pounds. This is not the case in our markets. In Midtown, City and Docklands, many purchasers, overseas buyers included, have a genuine use for a home in one of the world's leading global centres.

Most of our buyers are secure equity investors buying property as pied-a-terres, buy to let investments, or as a home with backing from affluent parents. (See buyer profiles). Homes purchased by parents frequently find their way into the rental market eventually, once they are no longer in use by the owner's family. Rarely do they come back to the sales market.

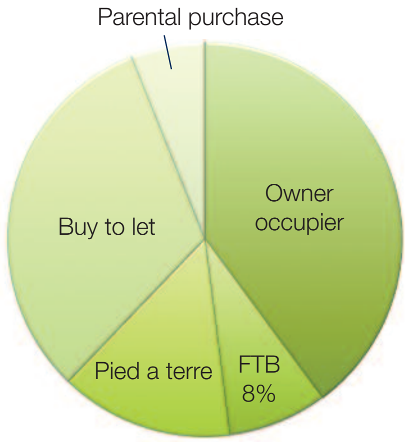
FITZROVIA W1 - FREEHOLD HOUSE SOLD MAY 2013 £2.2 MILLION

BUYER PROFILES FIRST HALF 2013



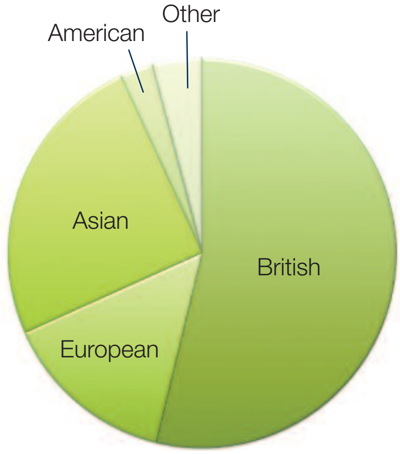
FUNDING

100% Cash	Loan to Value <50%	50-75%	>75%
31%	22%	38%	9%



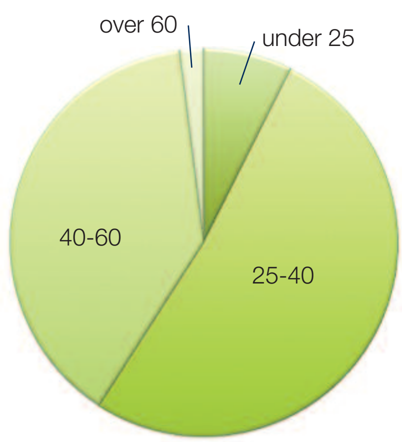
USE

Owner Occupier	First Time Buyer	Pied a terre	Buy to Let	Parental Purchase
40%	8%	14%	32%	6%



NATIONALITY

British	Asian	European	American	Other
54%	25%	14%	3%	4%

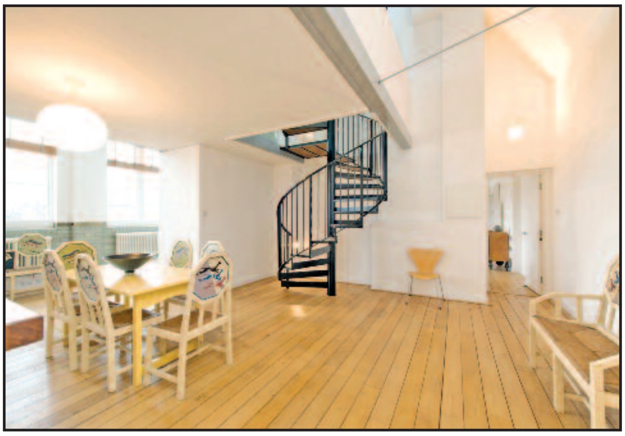


AGE

Under 25	25-40	40-60	Over 60
7%	52%	39%	2%

Hurford Salvi Carr Buyer profiles are based on the analysis of transactions in Midtown, City and Docklands in the first half 2013

It is recognised that overseas buyers are attracted by London's political stability, well-ordered legal system and economic security. It is ironic that weaknesses in the domestic economies of the Eurozone and strength in the domestic economies of the Far East are both driving capital to London.



KINGSWAY PLACE EC1 - THREE RECEP, TWO BED APARTMENT SOLD JULY 2013 £1.7 MILLION

The debacle in Cyprus in March, over tax on cash deposits, showed investors that anything is possible in Europe and has served to reinforce London's brand as a safe haven. The EU's treatment of Cyprus directly affected many Russian investors and opened their eyes to the fact that deposits of over £80,000 held in bank accounts, may not be secure. It was yet another big wake-up call for investors and a reminder that it may not be wise to leave capital assets in a bank. New York is also a beneficiary of these global forces, while France is excluded by the unsettling shifts in its political and tax regime.

There is no doubt that the Central London residential market has decoupled from rest of the UK and even from London's own suburban markets. The relationship between average salaries and property prices, often quoted in the press, has little direct impact on markets where almost half of buyers are based overseas. The average deposit required to purchase even the most modest Central London residence is beyond the pockets of most young Londoners – in fact, most Londoners of any age.

UK buyers in City, Midtown and Docklands are generally drawing on capital reserves and the greatest incentive to invest is the low rate of interest available from cash deposits - such buyers tend to have a long term perspective because of the high costs associated with the initial purchase, including stamp duty.

We know from experience, that a downturn in value growth does not result in distressed sellers in City, Midtown and Docklands. Like West End owners, they think long term and hold on to their assets. The reality is that very few existing home owners are forced sellers and when they read that prices are rising above inflation, equities or salaries, the obvious choice is to retain their old property as a rental investment when moving to a larger home. The long run price trends for Central London residential values support that view.

Values have increased by as much in the first six months of 2013 as they did in the whole of 2012.

We are now in the fourth consecutive year of above average growth in the value of Central London residential property. Large segments of the London population are priced out of the market and the affordability gap is getting wider. Nevertheless, as long as there is strong demand from wealthy UK and overseas equity-led buyers, confidence remains high and the integrity of the market is not threatened. Despite rents softening, capital values are also underpinned by reliable demand for property to rent – as we explain elsewhere in the report.

Docklands benefits from greater affordability than Midtown and City and some parts of Hackney, (London Fields, Victoria Park and Hackney Wick) as well as most waterfront locations, have begun to look like very good value in comparison with areas at a similar distance from Central London and with comparable amenity. This is the result of vast improvements to the transport connections, and environmental improvements as well as the opening of Westfield Stratford and the proliferation of restaurants and cafes supported by a changing demographic profile. East London has become 'more doable' for many Londoners over the past decade and summer 2012 Olympics has cemented its new profile.

There is a difference however. Prices fell more steeply in Docklands than the other two markets between the summer of 2007 and the end of 2008, (by 19% compared with 13 or 14% in Midtown and City respectively). For that reason the growth achieved, if 2007 is taken as the base date, is significantly lower in the Docklands market. But over a 20-year period price growth has been remarkably similar in all three markets, as it is if 2008 is taken as the base date (see table 2).

TABLE 2
LONG RUN PRICE GROWTH
BASED ON ONE BEDROOM APARTMENT IN THE RESALE MARKET

	1994-2013	2000-2013	2007-2013	2008-2013
Midtown	442%	106%	24%	36%
City	445%	119%	35%	49%
Docklands	426%	101%	16%	34%

Source: Hurford Salvi Carr

In the 19 years since our records began in 1994, the capital value of a one bedroom flat in Midtown has risen by 442%, in the City by 445% and in Docklands by 426%. As ever timing is critical in property and during that period the differential in price between Midtown and Docklands has varied between 27% and 38%. Today it is relatively high, at 34% and the gap has widened over the course of 2013. This data demonstrates the rewards of patience in these markets.

In 1st half 2013, in our markets, the majority of properties priced at £500,000 or lower were sold to buy to let investors and second home owners, while the majority of sales over £1 million, were made to owner-occupiers.

New Homes Market

DEVELOPMENTS SELL OUT

The proliferation of cranes piercing the London skyline is visible proof that the city is in the midst of a building boom. Each new development strives to be more attractive than the last by enhancing its specification, which helps to drive demand and support price growth. Meanwhile the condition of second hand stock deteriorates, slowly but surely over time.

Volume house-builders are delivering large-scale, high-rise developments in a corridor running from King's Cross, via City Road and Shoreditch, to Aldgate. These larger style developments tend to sell off-plan and are popular with overseas, particularly Far Eastern, investors for whom they are reminiscent of domestic property in their home markets.

Smaller but more numerous conversions or new buildings knitted into existing streetscapes by high-end niche developers, have more appeal for British buyers who seem willing to pay a premium to get into well-located boutique schemes in one of London's villages: Covent Garden, Bloomsbury, King's Cross, Holborn, Clerkenwell, Shoredtich, The City or Docklands.

BLOOMSBURY WC1 - TOWN HOUSE SOLD JUNE 2013 £2.35 MILLION

Most developers rely on some form of debt finance. Even if they are funded by private equity, as many are, they will generally seek to maximise their leverage with bank funding and the banks will normally insist on a substantial element of pre-sales before releasing development finance. Typically the bank will require between 20% and 40% of the units to be sold before construction. This means that a buyer has to commit to the purchase of a property that may not be ready to occupy for another 2 years, or longer. Any buyer requiring mortgage finance is effectively excluded from this market because mortgage offers are only valid for 6 months and ironically, banks are unwilling to change this criteria for off-plan, UK purchasers. Few owner-occupiers would have the confidence to pay a non-refundable deposit to secure a home off-plan, in the expectation that mortgage finance will be available at an attractive rate in 18-24 months' time. And therefore off-plan sales are inevitably to investors.

The inherent scarcity of supply of residential property in Central London will ensure that demand for new homes is maintained, at least in the prime markets. To all intents and purposes, Zone 1 is saturated. One option is to build higher and most of the sites suitable for intensification have been developed or optioned in the past few years. There is a swathe of towers being developed at present but it is a tightly defined geography. The number of opportunities to create new stock is diminishing and the balance between commercial and residential development viability has shifted, for some sites, in favour of commercial.

On paper, capital values remain higher for residential than commercial development, typically, by a factor of between 200 and 250%. In practice however, the cost of delivering high value residential and associated planning hurdles are so much greater for residential, that commercial property becomes the more economically viable use on many Central London sites. The type of stock that is most suitable for residential conversion – listed, architecturally attractive, characterful – had, until recently, little appeal for the commercial markets but that has changed with the rising influence of creative and tech sector businesses. There is now a strong unmet demand for simple, unadorned, warehouse style workspace in many parts of Central London and the fact that institutional investors generally prefer commercial property reinforces the trend.

The Help-to-Buy scheme announced in the March budget has been seen by some commentators as an ill-judged boost to the availability of debt that will artificially inflate values but we have not seen it offered by housebuilders or private developers in City, Midtown or Docklands and we do not expect it to have any impact on prices in our markets.

In the first half of 2013 a range of new developments were launched across Midtown, City and Docklands and a high volume of sales were achieved, including the final units from developments launched in late 2012. Prices that may have looked optimistic at the end of 2012, were achieved in the first half of 2013.

In January, we sold the final 7 apartments at **Ixia on East Road N1** for Crest Nicholson and by the end of March we had sold the final 17 apartments at the **Panoramic, Willis Road E14** for Telford Homes as well as the final phase of 49 units at **Avant Garde, Bethnal Green Road E1** for Telford Homes.

PANORAMIC BUILDING, WILLIS ST E14 - TWO BED FLATS SOLD MARCH 2013 £330,000 - £385,000

The experience in Midtown, City and Docklands was mirrored in other central London locations. Show homes reported recorded visitor numbers and reservations, the majority from UK buyers. Overseas buyers remained enthusiastic with pre launches attracting purchasers from Singapore and Hong Kong.

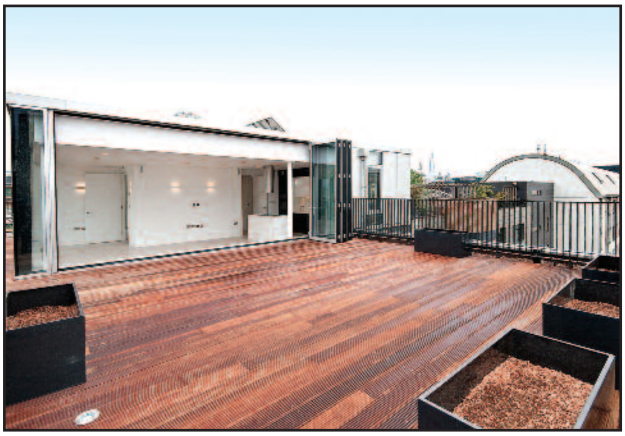
Confidence in London's property market reached a new high in January with the exceptional results at Battersea Power Station, which have become iconic. It was the single most outstanding sales weekend experienced in London. The front page headlines read: "Battersea Bonanza as £600m flats go in 4 days" together with references to a 'stampede' and tales of people queuing from 6.30am to secure a purchase. Press reports described it as 'the fastest selling property development on record in London' with 600 properties sold over the weekend in London and the remaining 200 of the first release sold over the next couple of weeks in the Far East.

The reality was a little less sensational – it emerged later in the property press that 120 were sold to UK buyers and 480 were reserved by buyers in the Far East over the course of that 4 day weekend. Nevertheless there is no doubt that the volume of sales was unprecedented, even in the London market. This development seems to represent the zeitgeist in London's super-prime market in early 2013. It was an extraordinary event in the story of London's residential markets and reinforced confidence in London as a safe haven for capital.

CORSHAM STREET, SHOREDITCH N1 - ONE BED FLAT SOLD MARCH 2013 £795,000

In February we sold 4 new apartments in a converted warehouse in **Corsham Street N1** close to Old Street Roundabout within 2 weeks, with unit prices for one bedroom apartments ranging from £500,000 to £795,000 while a three bedroom apartment achieved £950,000. Also in February we sold a stylish new block of two bedroom apartments at **103 Copenhagen Street, Islington N1** where buyers were out in force on the launch day and sales were secured at between £500,000 and £725,000.

In May we launched 17 spacious two bedroom apartments for Development Securities and Real Star at **Wick Lane Wharf at Fish Island, Bow E3** opposite the Olympic Stadium with prices ranging £299,950 to £365,000. By the end of June we had only two apartment's remaining.



PENTHOUSE KIRBY ST, CLERKENWELL EC1 - SOLD JUNE 2013 £1,250,000

In June, **30 Kirby Street, Clerkenwell EC1** completed. This high quality mixed use development designed by Buckley Grey Yeoman behalf of Mercer Real Estate Partners and Seven Capital became the first development in Clerkenwell to average £1,000/sq ft across all 5 apartments which are situated on the 5th and 6th floors above office space.

In Q2, we sold 5 waterside homes at **Islington Canalside N1** on Regents Canal, off-plan, for prices between £650,000 and £935,000.

In June Mount Anvil secured 50% pre sales at **The Orchard, One Pear Tree Street EC1** following on from their success at Central Square. It was also reported that Mount Anvil sold 71 units to a single investor during the first half of 2013, at **Eagle House, on City Road EC1**, where 206 private apartments are being built.

On 26th June some 180 buyers attended the launch of **Bloomsbury Gardens WC1** by Crest Nicholson and Passion Properties for the first phase release. It sold out on the night at prices approaching £1,200/sq ft. This launched once again demonstrated the strength of the local London market with the house builder deciding to sell in the UK rather than overseas. A second release is expected in September.

It was hard not to notice the deluge of advertising to promote 'Penthouse Collections' in Q2 of 2013. Penthouse buyers at above £2m now have the luxury of choice.

WICK LANE WHARF, BOW E3 - TWO BED FLATS SOLD JUNE 2013 £299,000 - £365,000

Development

Opportunities to develop residential property in Inner London are in short supply. The costs of planning and associated fees have escalated and most inner London boroughs are minded to protect commercial space from the further encroachment of residential conversions, as we predicted in our 2012 Year End report. All of the inner boroughs secured an exemption for at least part of their territory, from the Permitted Development Rights that would have given automatic rights for change of use from commercial to residential.

We have noted a decline in the number of small planning applications with fewer than 10 units. We believe this is, in part, due to the rising costs of submitting planning applications, in addition to CIL contributions and affordable housing and the fees for supporting reports from experts on matters such as sustainability. This has, in our view, squeezed the margins and undermined confidence in the planning system, on all but the largest schemes.

The increased demand for secondary, unadorned commercial property has played a part in this change. Many more landlords are choosing to stick with office use because it is more cost effective to renovate and provides a good income stream.

Larger schemes remain viable because the volume of units improves the margin for the developer and because the more peripheral large brownfield sites are often not attractive to office occupiers, or only at discounted rents and so there is less direct competition for the same locations between commercial and residential uses.

We remain of the view that after 2015, once the current wave of development has been completed, there is a very real chance that the development pipeline will be severely depleted across City and Midtown but the pipeline in Docklands and East London will remain high.

London development panel

The GLA is one of the largest owners of public land in London and the Mayor, Boris Johnson, is keen to make some of that land available for residential development, to help address London's housing shortage. To this end, he set up the London Development Panel, with the support of London Councils, to speed up the procurement process. It established a framework agreement with a panel of approved developers so that public landowners will be able to award contracts to developers without having to go through a full procurement process each time.

It also offers the potential for developers to 'build now, pay later' for land on some schemes to make them more viable. The panel has a four year term and the Mayor announced a list of 25 developers in May.

The Mayor said: "London Development Panel will act as a one-stop shop for public land owners in the capital, making it quicker, easier and cheaper for them to bring their land forward for development, increasing the number of homes being built, creating jobs and boosting the capital's economy."

The list of developers is: Affinity Sutton Homes Ltd; Ardmore First Base Partnership Limited; BDW Trading Ltd; Bellway Homes Limited; Bouygues Leadbitter Consortium; Carillion-Igloo and Genesis; Catalyst Housing Limited; Countryside Properties (UK) Limited; Family Mosaic & Mulalley; Galliford Try PLC; Hadley Mace Holdings Ltd; Higgins Group PLC; Kier Limited Lend Lease Europe Holdings Limited; London & Quadrant Housing Trust; Lovell Partnerships; Notting Hill Housing; Places for People Homes Limited; Redrow Homes Ltd; Regenter Limited; Rydon Construction Limited; Taylor Wimpey UK Ltd; The Berkeley Group Plc; Telford Homes Plc; Wates Construction Ltd.

Rental Market

BUILDING BOOM INCREASES SUPPLY

Rental values fell in the City and Docklands in the first half of 2013, as the number of flats available to rent increased. An expansion of London's rental stock looks set to be a long-term trend and that means that stable or falling rental values are inevitable as the choice increases.

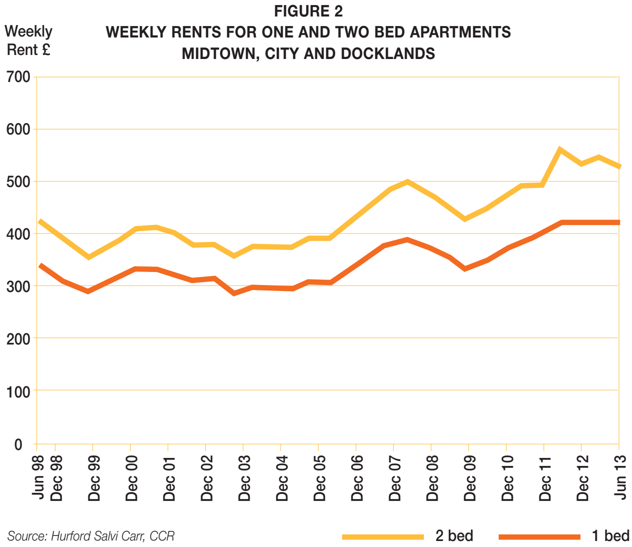
Much of this additional rental stock is entering the market via the new homes pipeline and supported by the continuing popularity of buy to let investment. We expect to see further additions to stock in the second half of 2013, as development projects, which had been pre-purchased in 2011 and 2012, are completed.

We do not expect any significant institutional investment in the Private Rented Sector in our markets in the foreseeable future, as yields are less attractive than suburban locations across London.

The falls in rental value in 1st Half 2013 were steepest for two bedroom flats in the City. Here, the rental value of a typical two bedroom flat dropped by 11%, from £630 to £560 per week. The premium a renter will pay for a second bedroom has declined, narrowing the differential between one and two beds in the City to 32%, compared with 44% in 2011. In Docklands the premium was already smaller but it too has declined, from 29% in 2011 to 21% today.

In our experience, renters are prepared to compromise on the size of their apartment in favour of a more central location and, since two bedroom properties are less affordable than those with one bedroom, we have found that renters prefer to settle for a one bedroom property rather than settle for a less central area.

FIGURE 2
WEEKLY RENTS FOR ONE AND TWO BED APARTMENTS MIDTOWN, CITY AND DOCKLANDS



Source: Hurford Salvi Carr, CCR

The Midtown market has behaved differently. The extra bedroom still commands a rent 44% higher than a one bedroom flat and rents continued to rise in 2013. By the summer, the rent for a two bedroom flat in Midtown was £650 a week, 5% up on the beginning of the year and the rent for a one bedroom rose by 6% to £450 per week. Perhaps surprisingly, this is the first time that Midtown rents have overtaken the City and at the half year, the weekly cost of a two bedroom flat in Midtown is £90 more than the City.

Long term increases in rental values are actually far more modest than newspaper headlines might suggest. In the 15 years since our data series began in 1998, the average rent for two bedroom flat in London has risen by around 32% and for a one bedroom flat, the increase has been around 23%. This compares with capital value rises of closer to 200% over the same period.

TABLE 3
WEEKLY RENTS AND ANNUAL CHANGE FOR ONE AND TWO BED FLATS IN MIDTOWN, CITY AND DOCKLANDS AT YEAR END

Market	Unit Size	End 2012 £	Mid 2013 £	Annual Change
Midtown	1 bedroom	425	450	6%
	2 bedroom	620	650	5%
City	1 bedroom	450	425	-6%
	2 bedroom	650	560	-11%
Docklands	1 bedroom	340	340	0%
	2 bedroom	425	410	-4%

Source: Hurford Salvi Carr

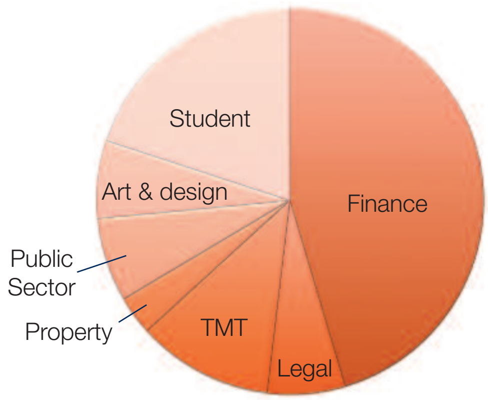
In 2012, we reported a reduction in the average length of time that a tenant stays in the same property and that has continued in the first half of 2013. It has fallen dramatically from an average of 2.5 years, to 1.5 years over the past 12 months. In our experience, it is more usual for tenants to agree lease renewals when the rental market is strong, rather than expose themselves to rising rents and websites provide tenants with the rental information to make informed decisions. As rents fall, tenants take the opportunity to move to new accommodation to reduce monthly outgoings or swap to a better flat. However, we have noted in the first half of 2013, that tenants in Docklands and east London are staying for longer terms than in City and Midtown.

The reasons why tenancies can end early are complex. Some tenants decide to buy in order to protect themselves from increases in capital values as part of their long term ambition to be home owners but perhaps this trend can be equally explained by redundancies, contract terminations and the return home of overseas workers. The rental market will always be less predictable simply because of the flexibility it gives the occupiers. Tenants are intrinsically mobile.

The majority of tenants signing leases through Hurford Salvi Carr offices in 1st Half 2013 were aged between 25 and 40 and 61% were from overseas. (See buyer profiles)

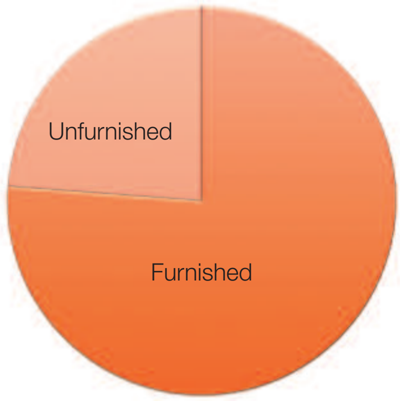
FLORENCE HOUSE, TUDOR STREET EC4 - 7 FLATS LET JUNE 2013

TENANT PROFILES FIRST HALF 2013



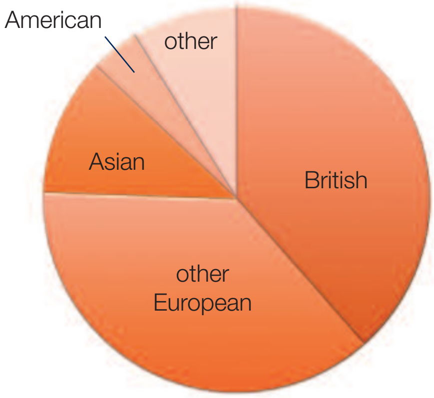
OCCUPATION

Finance	Legal	TMT	Property	Public Sector	Student	Other	Art & Design
31%	4%	8%	2%	5%	14%	32%	4%



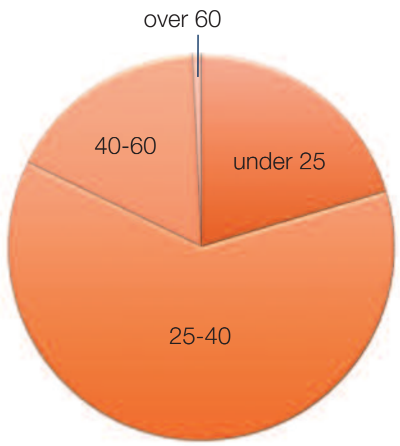
TYPE

Furnished	Unfurnished
76%	24%



NATIONALITY

British	Asian	European	American	Other
39%	11%	37%	4%	9%



AGE

Under 25	25-40	40-60	Over 60
20%	62%	17%	1%

Hurford Salvi Carr Tenant profiles are based on a sample of lettings completed by Hurford Salvi Carr offices in the first half 2013

By far the most common occupation amongst the renters that passed through Hurford Salvi Carr offices was financial sector, including banks and accountants. This is perhaps inevitable given our focus on markets to the east of Central London but it is interesting that Technology, Media and Telecoms (TMT) accounted for more (8%) than legal (4%) and that is without taking account of art and design which are often included within the definition of TMT as media businesses. Together TMT and art and design accounted for 12% of all renters.

In Midtown City and Docklands, an expanding stock of well-designed new apartments to rent in convenient locations is containing rental growth but greatly increasing the choices for renters. We expect that to continue. This is not the same situation in West or North London, which have more stable stock levels, although the recently granted Permitted Development Rights will create new opportunities for office to residential conversion in the less central parts of north and west London.

Notwithstanding long term trends in supply, there will always be a seasonal pattern. The demand for properties to rent generally increases in Q3 and it is quite normal for higher rents to be achieved in summer months. The summer is by far the most common time to enter a tenancy agreement as graduates arrive in London to start new jobs, relocation companies search on behalf of more senior executives and students secure homes in advance of the forthcoming academic year.

BEDFORD PLACE WC1 - 9 FLATS LET MARCH 2013 £550 - £1,250 PER WEEK

Regulation of the rental market

The volume of regulation and legislation designed to protect tenants from unscrupulous landlords and their advisors has begun to increase and it seems inevitable that it will proliferate in the future.

New consumer protection regulation removes caveat emptor. Today, an agent has a duty of care to their clients and a moral responsibility to the consumer – which are two different things but tend to be conflated in the minds of the client and the tenant. There is a growing will to formalise measures to protect tenants. The Advertising Standards Authority (ASA) has recently fined two letting agents following complaints from tenants who were charged agreement fees for documentation when they took a new lease, without the agents' marketing material informing tenants that fees in addition to rent, apply.

As a result, the ASA has declared that agents must adapt their marketing material to inform the public that when they sign a lease they will be liable for the transaction costs, including inventories, reference checks and that other fees may apply.

This is a strong indication that tighter regulation is on its way. As we suggested in the last edition of this report, we expect legislation covering business practices in the private rental sector to move towards recent changes in the Scottish system - whereby agents cannot charge fees to tenants for preparing tenancy agreements, taking up references, preparing an inventory and the cost of documents such as gas safety certificates; EPCs; and other, as yet unknown, consumer protection measures.

Policymakers generally assume that the costs of supplying these certificates and services for no fee, will be absorbed by the supply industry – the landlords - but in practice, it rarely works that way. In a letting market as robust as Central London, the costs are almost certain to be passed on to the tenants through rental uplifts. While landlords will not benefit, headline rents for tenants could be higher.

There is no doubt that the lettings market has, in the past, been too lightly regulated, in stark contrast to the sales market which has been over-regulated but the balance is being redressed.

Investment Market

YIELDS HIT NEW LOW

Typical income yields on one bedroom apartments fell in the first six months of 2013 from an average of 5.4% to 5.1%. The decline in the income yield is the simple and direct consequence of a rise in capital values (of around 5%) combined with static rental values. This divergence between growth rates for capital and rental values could continue over the next 3 years, as more investment properties reach the rental market, causing yields to drift below 4%. The average yield on two bedroom apartments is already approaching 4% across the market areas that we cover.

FARRINGDON ROAD EC1 - 16 APARTMENTS CORPORATE LET JUNE 2013

It is a fact that, while capital values are supported by inherent supply constraints, rental values are suppressed by a rising supply of rental property via buy to let investors and which might be significantly expanded in future with the emergence of a more formal Private Rented Sector.

While there remain significant obstacles to the emergence of a Private Rented Sector, we saw more signs this year of investor interest. Essential Living is set to buy a site in Poplar with consent for 345 private and 60 intermediate homes in 2 towers with 34 units for sale and 28 reserved for private rental. In April the housing minister announced a shortlist of 45 projects that could benefit from the £1billion Build to Rent Fund, set up to facilitate private rented sector construction. A quarter of these were in London.

THE COLONNADES WC1 - MEWS HOUSES LET TO SERVICED OPERATOR APRIL 2013

At the time of writing there were no examples of Help to Build being offered by housebuilders in Midtown, City or Docklands. Telford Homes, in their 2013 Annual Report confirmed:

"While the board anticipates that Telford Homes will join the 'Help to Buy' scheme in London it has not done so to date and has not needed to participate in any of the previous government initiatives." Telford Homes Annual Report 2013.

It is an indication of the strength of the market in London that developers have not felt the need to offer such incentives to buyers and, in fact, many of their buyers are cash purchasers. (see page 3 – buyer profile: funding).

Serviced apartment operators and student accommodation providers continue to be active in the investment market. Landlords and developers benefit from longer leases and savings in management costs by entering into tenancies of multiple units with a single provider.

TABLE 4
INCOME, VALUES AND INITIAL YIELDS FOR ONE BED APARTMENTS, AVERAGE OF MIDTOWN, CITY AND DOCKLANDS 2002 TO MID 2013

	Dec 2002	Dec 2003	Dec 2004	Dec 2005	Dec 2006	Dec 2007	Dec 2008	Dec 2009	Dec 2010	Dec 2011	Dec 2012	Mid 2013
Gross Annual Income £	15,600	14,820	14,820	15,340	18,200	20,020	18,200	17,680	19,760	21,840	21,840	21,840
Capital Value £	260,000	245,000	246,000	270,000	340,000	371,000	318,000	338,000	352,000	386,000	405,000	425,000
Gross Initial Yield %	6.0	6.0	6.0	5.7	5.4	5.4	5.7	5.2	5.6	5.7	5.4	5.1

Note : gross yields are typically reduced by 2.5% points by costs and voids

Source: Hurford Salvi Carr, CCR

Market Prospects

FORECASTS

Low risk, low return profile to continue

We expect the sales market to remain strong in the second half of 2013, with prices continuing to increase at a lower rate of up to 2% to end the year up 7% overall.

In the rental market we expect values to stabilise during the stronger summer months, when new entrants arrive in London fuelling demand for rental property but we do not anticipate any significant growth in rental values because there is stock flowing in to the market as developments are completed.

Landlords will be prepared to negotiate on asking rents in order to retain tenants at lease renewal.

Yields on residential property that is held for investment, will gradually fall as sales prices move upwards and rental values find a longer-term stability.

The economy seems to have finally entered a period of recovery but it is founded on consumer spending and its longevity is by no means certain. A shock could come from almost anywhere: a country leaving the Eurozone, a crisis in China, or even a widening of the conflict in Syria to the oil-producing countries of the Middle East.

Another banking crisis is quite possible, and that does not even take into account that the economy is still being propped up by the Bank of England's policy of quantitative easing (QE). For the time being however, confidence is rising.

There has been a minor building boom in London and we expect it to continue over the next couple of years. It is unlikely to temper price rises to any great degree because supply remains inherently constrained and the desire to invest money in residential property looks set to persist for a few more years. A significant proportion of the new build stock will be bought for investment and fed into the rental market.

Given the population projections for London (one million extra by 2020 and a further million by 2030 according to the ONS) and the fact that property is unaffordable for so many, demand for homes to rent seems to be ensured, albeit without any substantial rental growth.

Risk arises from the investor buyers who might be deterred by falling yields or by exchange rate fluctuations that prompt overseas buyers to look elsewhere for investment opportunities. Interest rates are also a potential trigger for a future loss of confidence in London's property market, although any rises are likely to be modest and rates are likely to remain low for the foreseeable future.

We do not foresee the bursting of any house price bubble in the near future, as demand will continue to outstrip supply.

Any slowdown in our market is unlikely to cause any distressed sales because the majority of buyers are contributing substantial tranches of equity and so small rises in interest rates are unlikely to create stress. Our typical buyer is putting down between 50 and 100% cash and so banks are able to confine their lending to customers considered to be 'low risk'.

Opportunities to develop in Central London are very limited. High-rise development is one solution to supply constraint. We expect to see development at increased densities, which, in most cases, means taller. In May 2013, Berkeley Homes submitted a planning application to build two towers of 42 and 36 storeys and four blocks of 7 to 9 storeys each containing 995 homes in a Norman Foster designed scheme at City Forum, 250 City Road, EC1, which becomes vacant in December 2015.

British Land, Barratts & Helical Bar have applied for 463 homes, an 86,000 sq ft hotel and 30,000 sq ft office, across towers rising to 26 storeys at Aldgate Place, E1, which is next to Barratts' sucessful Altitude Development and Berkeley Homes' Goodman Fields Development.

Following 20 years of residential development, the City and Docklands are now established as prime Central London addresses. Demand for sales and tenancies are stronger than ever. New residential quarters being developed at King's Cross and Aldgate will increase the range of choice available to buyers and tenants. This injection of stock will help to meet unsatisfied demand and to create new demand as the areas become established.

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