research

from Hurford Salvi Carr

MIDTOWN, CITY AND DOCKLANDS

RESIDENTIAL REVIEW 2014

“

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HURFORD SALVI CARR

Market Overview

MARKET SLOWS AHEAD OF UK ELECTION

Given the amount of public debate and newspaper headlines dedicated to the housing markets in 2014, the reader might expect to find some sensational trends in our year-end report. It is not the case. 2014 was a remarkably stable and uneventful year in the Central London residential markets. There has been no bubble and no crash, London continues to represent a safe haven for capital and a magnet for young highly skilled labour from across the world. There were willing buyers and willing sellers, albeit fewer of them and they were no longer panicked into bidding up prices.

The rental market, by contrast, improved over the course of 2014 and by the year-end further growth seemed to be in prospect.

An unexpected development emerged in the final month of the year as the Chancellor announced sweeping changes to the Stamp Duty Land Tax system.

However, the most surprising aspect of the market in 2014 was its dependability. The number of overseas buyers fell, enough to reduce the pressure on prices, the supply of money loosened just enough to encourage more UK buyers into the market, and fewer sales meant rather more renters while the flow of new development completions expanded the rental stock.

Concerns expressed by the Governor of the Bank of England several times in 2014 probably helped to avert any serious risk of over-inflation and instability and, without any significant interventions beyond warning speeches and tax proposals, the market slowed down and effectively self-corrected long before the Chancellor's announcement on Stamp Duty.

NEW HURFORD SALVI CARR ISLINGTON & SHOREDITCH OFFICE OPENS DECEMBER 2014

No doubt, overseas investors have been carefully watching the progress of the UK Election and latest thoughts on taxation policy. The continuing threat of taxation on foreign investors and high value homes disheartened some overseas buyers and reduced demand from that quarter.

CLERKENWELL EC1 - CONTEMPORARY FREEHOLD HOUSE, SOLD OCT 2014

The effect of the slowdown was most evident at the top end of the sales market, specifically on properties valued at more than £2 million. There has been a gradual build up of un-sold stock in this price bracket over the year, in all of City, Midtown and Docklands and yet price corrections have not provided a quick solution. Responsibility for downward pressure on demand for most of the year lay with the combined effect of the 7% stamp duty threshold and Labour's mansion tax proposals. The additional stamp duty tax burden imposed overnight on December 3rd, made it even more difficult to secure buyers at the top end of the market.

But price reductions were still rare in 2014, except when the property had been seriously over-priced at the outset and we do not sense that owners are under any particular pressure to sell. We expect 2015 to bring fewer sales and more letting transactions. Demand will be robust enough to support current pricing across Midtown, City and Docklands for properties up to £1million but, above that, we now expect prices to finish the year 5% below the highs recorded in 2014. In other words, we expect to see a two-pace market in 2015.

> "Buyers from the UK dominated our markets in 2014, accounting for almost 70% of sales."

Economic Overview

LONDON'S HOUSING MARKET TARGETED BY POLITICIANS

The UK economy has been recovering since early 2013. In early December, the OBR (Office of Budget Responsibility) announced that it expects real GDP growth to average around 3% in 2014 and 2.4% in 2015. Both of these figures were revised upwards from its March forecasts (2.7% and 2.3%). This would make the UK the fastest growing economy in the G7. In June, the IMF Managing Director, Christine Lagarde, acknowledged that the growth of the UK economy had exceeded the IMF's expectations.

The services sector remains the key driver of growth while manufacturing has suffered from the renewed economic uncertainty in the Eurozone – the UK's main export markets. The government had hoped to rebalance the economy by boosting manufacturing, but a strong services sector still underpins growth in London and the South East. The service sector has also been the main driver of employment growth.

At the same time the FTSE 100 index slid to its lowest level all year in October as the markets responded to the falling oil price, slowing growth in developing economies and persistent weaknesses in the Eurozone economy, with even the robust and usually reliable German economy giving cause for concern. On 16th December the Russian Rouble lost 20% of its value and the Russian Central Bank lifted interest rates from 10.5% to 17%. Here too, the falling oil price was held responsible, along with western sanctions over Ukraine and investor concern about Russia's growing political isolation.

The Bank of England continues to postpone any prospect of a rise in interest rates, indicating that the, admittedly encouraging, headline statistics on the UK economy have not yet entirely convinced the Monetary Policy Committee.

Low wage growth and a vacillating housing market are the two contra-indicators within the UK and inflation remains doggedly low at 1.2% with some commentators predicting that it could fall below 1%. But the Bank's main concern is whether the UK can withstand shocks from outside its national boundaries.

BLOOMSBURY WC1 - FOUR BEDROOM APARTMENT, SOLD AUG 2014 £1,875,000

The consensus view now is that rates will remain on hold until mid-2015 at the very earliest, and possibly not rise until much later in the year. As and when rates do rise, they are likely to affect housing markets in Outer London but Central London is largely insulated by the predominance of cash and low loan-to-value buyers.

In this report, we regularly reflect on the impact of the economy on housing markets but, over the past year, there has been an enormous swell of concern amongst politicians about the impact that housing markets have on the economy – and on political fortunes.

The 'Housing Crisis', has risen to the top of the political agenda in the run up to the 2015 election, with policies designed to expand supply, improve access to mortgage finance and to grab more from national and local taxation emerging from all the parties. The issue of affordability, (the ratio between average wages and average house prices), or more accurately unaffordability, is particularly acute in London. However, it hardly impacts on central London's property market, where the majority of purchasers buy with cash.

RIDGMOUNT GARDNS WC1 - FOUR BEDROOM APARTMENT, LET SEPT 2014 £950 PER WEEK

Employment trends on the other hand do have an impact on our markets and, while there were some job losses in the City, the employment market in Central London remains robust. CityUK reported that, while investment banking and insurance both experienced small reductions in employment of less than half a percentage point, the number of jobs in fund management grew by 4.5% in the first half of 2014 and accountancy and management consultancy by 5%. That meant that financial and related professional services employment in London grew by 1.6% overall to June 2014.

Given the array of property-related proposals put forward by the various political parties, from mansion tax, to revisions of the council tax bands, amendments to stamp duty thresholds, rent controls, longers period ASTs, planning deregulation and wrangles over the sacrosanctity of the green belt, it is not surprising that the Central London residential market has been less active than in the recent past. Uncertainty of any kind undermines confidence and puts a dampener on sales as both buyers and sellers postpone decisions to act. The Chancellor's surprise announcement on Stamp Duty is a good illustration of the impact of unforeseen policy interventions.

STAMP DUTY REFORM

On December 3rd, in his Autumn Statement, the Chancellor announced changes to the way that Stamp Duty Land Tax is calculated. The changes fundamentally alter the amount of tax payable on the purchase of a residential property in the UK. The Chancellor's proud claim was that 98% of home-buyers in the UK would be better off as a result and it is indeed the case that anyone buying a home for under £937,000 will pay less tax under the new system, but in Central London, that applies to a relatively small proportion of buyers.

Under the old system Stamp Duty was a 'slab tax' meaning it was levied at a single rate on the whole of the purchase price, at a rate determined by the price. The tax was set at 1% for properties sold for over £125,000, 3% over £250,000; 4% over £500,000; 5% over £1 million and 7% over £ 2 million. The tax distorted prices around the thresholds of each tax band.

Under the reformed system, which came into effect at midnight on December 3rd, the tax rate still varies according to the price but the big difference is that, although the rate steps up at a series of price thresholds, the tax is payable in tranches, at the rate appropriate to each price band. Thus, the buyer of a property sold for £2 million will pay no tax on the first £125,000, 2% for the portion between this and £250,000; 5% on the portion from £500,000 to £925,000; 10% from there to £1.5 million and 12% thereafter.

It means that for lower priced properties, the no or low-tax portion of the sale price makes up a larger proportion of the total and the effective tax rate is therefore lower. That is why the Chancellor could rightly claim that 98% of buyers would be better off under the new system. This table, adapted from The Times on December 5th illustrates the impact at a range of prices, around each of the tax thresholds.

TABLE 1
STAMP DUTY LIABILITY BEFORE AND AFTER DECEMBER 3RD 2014

Sale Price	Stamp Duty before 03.12.14	Stamp Duty after 03.12.14
£125,000	£0	£0
£185,000	£1,850	£1,200
£275,000	£8,250	£3,750
£510,000	£20,400	£15,500
£937,500	£37,500	£37,500
£1,500,000	£75,000	£93,750
£2,100,000	£147,000	£165,750

Source: Hurford Salvi Carr

Below a sale price of £937,500 the transaction attracts lower taxation under the new system and above that price, it is, in almost every case, higher. The exception is a small band of properties sold for between £1 million and £1.125 million, within which buyers will be some £6,250 better off under the new system.

In Kensington and Chelsea, London's most expensive borough, 61% of sales in 2014, up to the end of October, were over £937,500 – in other words only 39% of buyers would be better off under the new system. In our markets too, large numbers of transactions are over the £937,500 threshold, as illustrated in table 2. In stark contrast to the Chancellor's estimate that 2% of sales will attract higher stamp duty, in Camden it is 30%, Islington it is 16% and even in Tower Hamlets it is twice as high as the government estimate.

Figure 1 shows how the gap between stamp duty payable under the old system and the new system opens up, as prices rise. It begins to be substantial at around £1.5 million, when the additional tax

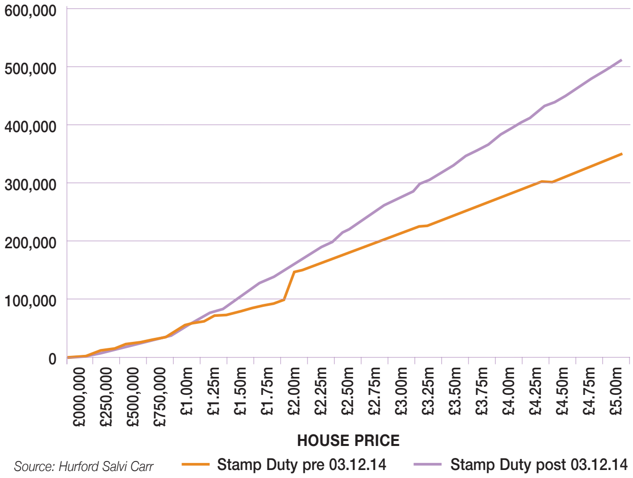
TABLE 2
PROPORTION OF SALES IN 2014 (UP TO END OCTOBER) AT PRICES OF OVER £937,500

Borough	% of all sales over £937,500
Camden	30%
City of London	24%
Hackney	8%
Islington	16%
Tower Hamlets	4%
Westminster	45%

Source: Hurford Salvi Carr

under the new system is almost £20,000 – an increase of 25% on the previous tax liability. Across our markets, the average price of a one bed flat is £520,000. At this price, there will be a 23% saving on the tax payable – the difference between £20,400 under the old system and £16,000 under the new. In fact, for sales up to £1.2 million the buyer is in a better position, or a not much worse position than before.

FIGURE 1
STAMP DUTY PAYABLE BEFORE AND AFTER DECEMBER 3RD 2014



Source: Hurford Salvi Carr

But over £2 million, where the market had already weakened in 2014, the new stamp duty system adds another £53,750 to a tax bill that was £100,000 under the old system. That said, the additional tax for a property sold at £2.1 million is less than £20,000. This is because the new system eradicates the big step changes that occurred with each tax threshold under the old system – see the smooth trajectory of the line representing the new system in Figure 1.

We have no doubt that changes to SDLT will affect prices in our markets. Properties priced below £1 million will be given an added impetus to rise because buyers will be able to bid prices up. For properties priced at above £1 million, where there was already pressure on prices, we expect to see prices stagnate with some developers offering stamp duty contributions to incentivise potential buyers and in order to maintain headline prices.

Buyers who had already exchanged on a presale before December 3rd, will be able to choose which system of SDLT suits them best at completion. For off-plan buyers, with a long gap between exchange and completion, the saving might feel quite significant by the time they complete on the purchase in one or two year's time.

Sales Market

PRICES RISE BY 4% IN 2014

After a busy start to the year, the market slowed down in Q2 as demand levelled off and properties stayed for longer on the market. There was a growing sense that homes had become 'too expensive' and the feeling was reinforced by press headlines. But two segments of the market bucked these trends. Demand for entry-level one-bed apartments continued to outstrip supply so that it will be no easier to buy a pied-a-terre in Central London in 2015 than it was in 2014. The other segment to buck the trend was Docklands, where demand strengthened, as buyers looked to East London to deliver value for money, although plentiful supply kept a lid on price increases.

TABLE 3
PRICES AND ANNUAL GROWTH IN THE RESALE MARKET AT YEAR END

Submarket	2013 £	2014 £	Annual	2014 £psf
Midtown One Bed	580,000	620,000	7%	1,240
Midtown Two Bed	950,000	960,000	1%	1,280
City One Bed	550,000	595,000	8%	1,190
City Two Bed	800,000	810,000	1%	1,080
Docklands One Bed	400,000	420,000	5%	840
Docklands Two Bed	580,000	600,000	3%	800

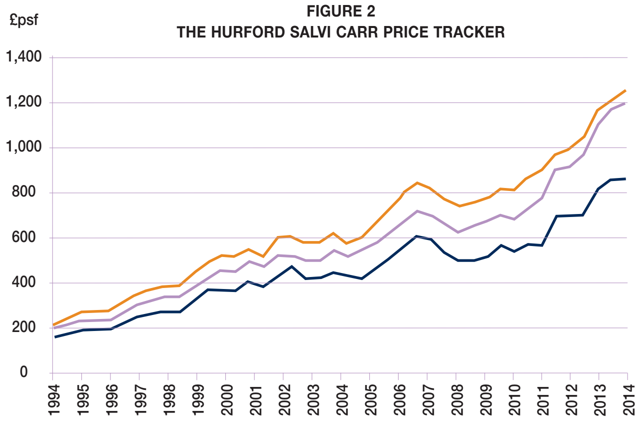
Source: Hurford Salvi Carr

One Bed is 500 sq ft
Two Bed is 750 sq ft and two baths

Over the whole year, property prices rose by an average of around 4% in 2014 across City, Midtown and Docklands. There was significantly better performance from one bedroom than two bed flats and stronger growth in the Central London areas than in Docklands. The price differential between City and Midtown is now very narrow but Docklands still operates at a significant discount to central and west London. (See table 3).

Growth was restrained compared with previous years and, by the end of Q3 2014, it had all but petered out. A slowdown should not come as a surprise after a sustained period of growth that began in 2009. Indeed it is as we predicted in our year-end report, 2013. It is always the case that markets need time to absorb new price levels and this time, with a General Election looming, we expect sales activity to remain subdued until the summer of 2015 when certainty will return to the markets.

FIGURE 2
THE HURFORD SALVI CARR PRICE TRACKER



Source: Hurford Salvi Carr

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

The blended average price for a one bed flat reached £520,000 for the first time in 2014, adding £34,000 or 7% to its value in a year. (See table 4). Although there was never a significant resistance to stamp duty in this part of the market, the erasure of the distinct tax threshold at £500,000 will now enable prices to edge up further in the sub-£1 million price bracket.

TABLE 4
PRICES AND ANNUAL GROWTH 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
2013	20%	486,000	81,000
2014	7%	520,000	34,000

Source: Hurford Salvi Carr

Residential property markets generally stall in the lead up to a General Election. It is a response to uncertainty. Buyers and sellers both delay decisions until they know more about the tone of the government and direction of future policy.

LIMEHOUSE E14 - TWO BEDROOM APARTMENT, SOLD SEPT 2014 £665,000

For most of 2014, there were fewer overseas buyers in London, fewer rental investors and fewer high-end buyers. While none of these groups has disappeared from the market altogether, a reduction in all three affects sales rates at the margins and weakens any upward pressure on prices.

TABLE 5
LONG RUN PRICE CHANGES
FOR A ONE BEDROOM APARTMENT IN THE RESALE MARKET

	1994 - 2014	2000 - 2014	2007 - 2014	2008 - 2014
Midtown	553%	148%	49%	64%
City	580%	174%	69%	86%
Docklands	546%	147%	42%	65%

Source: Hurford Salvi Carr

Given the pace of price growth in Central London since 2008 it is not surprising that investment buyers, whether of UK or overseas origin, have receded from the market. Since 2008, the average price of a 1 bed flat in City has risen by 86% and both Midtown and Docklands have experienced increases of around 65%. (Table 5). During this period rents hardly changed. Quite simply, prices have risen to a level at which returns on investment are less attractive than other parts of the UK property market.

Demand for Central London residential property may have softened in 2014 but it did not become a 'buyer's market'. While there are fewer investors buying, there is no evidence of owners becoming forced sellers. Very few owners are exposed to loan rates and, as long as the UK and London economy remain strong, most are sitting comfortably and see residential property in the capital, as a secure long-term investment.

In fact, the slowdown in activity is frustrating to prospective purchasers for whom it remains difficult to secure suitable properties. There is no doubt that the intense competition between prospective buyers waned during 2014. Price reductions began to appear in Q4 2014 and they attracted headlines. It is worth noting that, in our experience, a price reduction rarely resulted in a fast sale, suggesting that most of these properties were over-priced at the outset and that the reduction is merely resetting them to their correct (or more realistic) market level. The sense that vendors had become over-optimistic, which we flagged up in our last report, was reinforced by data from Hometrack in the autumn, which found that sellers in London were achieving the lowest percentage of their asking price since June 2013.

The visible outcome of the old SDLT system was that the price of a one bed flat continued to edge upwards in 2014 towards £750,000 in Midtown, while demand for two bed apartments, priced at over £1 million, weakened. We expect this pattern to be reinforced by the new system and concerns over the introduction of a new mansion tax at above £2 million.

Council tax is a different matter. There seems to be wide acceptance that council tax rates levied in Central London are disproportionately low compared to other parts of the UK. A recent study by Westminster City Council on the prime residential market recommended the introduction of three new council tax bands at £2 million to £5 million, £5 million to £15 million and over £15 million. And we can see merit in revisions to the council tax bands being addressed following the General Election even by the parties that have not committed to a mansion tax.

SHOREDITCH EC2 - 1,741 SQ FT TWO BEDOOM LOFT APARTMENT, SOLD NOV 2014 £1,820,000

MANSION TAX PROPOSALS

The Labour party's proposal for a mansion tax, in December 2014, is to impose a levy of £3,000 per annum on properties valued at between £2 million and £3 million. They have not yet announced the amount that will be levied on higher value properties but various commentators have calculated that, if the tax take is to raise the funds suggested for the NHS, it implies that there will be a considerably heavier tax burden on properties valued at over £3 million.

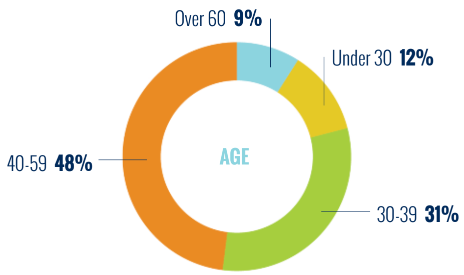
Although these proposals are considerably more moderate than earlier ideas mooted by the Liberal Democrats, the threat of a tax that would penalise owners of high value properties and the announcement of a price threshold, has had a negative impact on the market for homes priced at around £2 to £3 million.

There has been a gradual build up of unsold stock priced at over £2 million in our markets. Properties at these price levels are not part of the mainstream pied-a-terre market in City, Midtown and Docklands. The slowdown in demand for ultra high value properties experienced in some of the most prestigious West End locations, or for family housing, has particularly affected the penthouse markets in City, Midtown and Docklands.

2014 BUYER PROFILES

Buyers from the UK dominated our markets in 2014, accounting for almost 70% of sales. To put that figure in context, they made up only 54% in the first half of 2013 and 61% in 2013 as a whole. Other European buyers also increased their share by a small margin but the really big shift was in the proportion of Asian nationals, which dropped from 17% of sales in 2013 to just 7% in 2014.

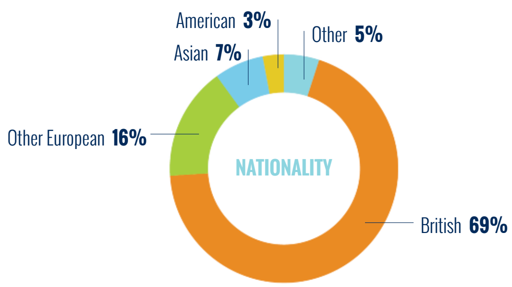
In our experience, Asian buyers tend to have a shorter-term outlook on their investment than a typical UK buyer. It means that they are more prone to profit-taking after a period of rapid price growth and as income returns decline.



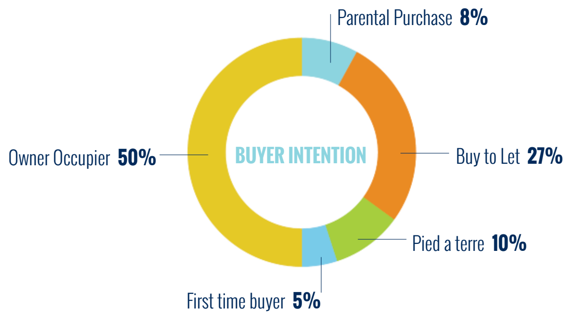
We expect a small spike in properties put up for sale in Q1 2015, in advance of the April deadline for the new Capital Gains Tax liability on overseas owners. The tax rate has not yet been confirmed, but 28% seems most likely, to bring them in line with UK taxpayers. For investors who had in any event intended to crystallise profits, April will become an artificial decision point, although we still expect most owners to retain their investments in which case they incur no tax until such time as they choose to sell.

There is no shortage of UK investors interested in one and two bed apartments, which have typically been acquired by Asian investors in previous years and UK buyers are also comfortable with second hand stock. As long as a property is not over-priced, there is every reason to expect it to find a willing buyer.

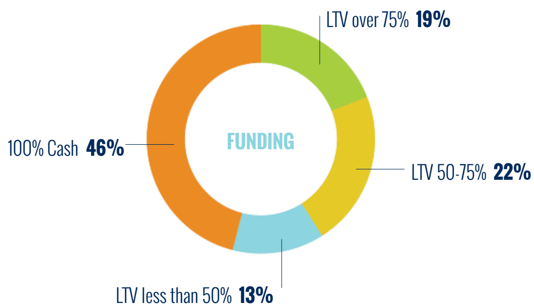
The UK still represents a safe haven for capital to citizens of other European countries, especially as the Eurozone economy continues to struggle and London is an attractive city in which to make or develop a career. Buyers from Europe accounted for 16% of all sales in 2014, up from 14% in 2013.



There were more owner occupiers in 2014 – 50% compared with 47% in 2013, and a corresponding decline in buy to let purchasers, which made up only 28% of the market in 2014 down from 33% in 2013. The number of owner occupiers has been rising since mid 2013 and in the first half of that year they accounted for only 40% of sales.



It seems that prices in Central London have begun to outstrip the means of many investors. Even when the percentage of price required for a deposit remains constant, the capital sum needed upfront becomes unaffordable for a large number of investors who have turned their attention to lower priced suburban locations. In our experience, we lose the majority of buy to let investors at prices of over £700,000 and the number of opportunities to secure properties in the range of £500,000 to £700,000 has declined in Midtown and City. In Docklands there remains a reasonable supply of properties priced at under £700,000, and that encouraged a strong sales market in East London in 2014.



In a related trend, we have noticed that more buyers are taking out loans with higher loan to value ratios – and that probably reflects the growing influence of owner-occupiers rather than investors. In 19% of sales, the buyer had taken a loan for 75% of the purchase price in 2014, compared with only 13% in 2013 and 9% in H1 2013.

That said, the number of 100% cash buyers has also risen, from 37% in 2013 to 46% in 2014 and overall, this remains a market dominated by buyers who do not depend on borrowing large sums. Almost 60% of buyers borrow less than half the purchase price.

Above Data compiled by Hurford Salvi Carr for the period January to December 2014

Lettings Market

DEMAND IMPROVES IN SECOND HALF OF 2014

2014 began slowly for the letting market but picked up the pace in Q3. There was no significant change in rental values in City Midtown and Docklands in the first half of the year, but the autumn peak in demand for rental properties was sharper than usual and we noted some upward pressure on rents, albeit sporadic and gentle, towards the end of the year.

We attribute the increase in demand to two factors – first renewed strength in the UK economy with an associated increase in graduate recruitment and second, the spill-over effect from a slowdown in the sales market, as those who might have considered buying a property, shelved plans and turned back to the rental market to find a home.

On the whole, the market was able to absorb the additional demand. Uplifts in rental value were mainly confined to very high value rentals, where a fall in sales has pushed demand into the rental market and created upward pressure on high-end rents. We noted a rise in the number of properties rented for more than £1,000 per week.

But in the mainstream market, which we define as 'one and two bed flats at rents between £400 and £750 per week', there are signs that areas of central London are at risk of becoming over-supplied. Places that have been the focus of new residential developments and have attracted buy to let investors, such as Aldgate, King's Cross, South Bank and Stratford, now face the prospect of a highly competitive rental market as construction programmes reach completion and new stock is offered for rent.

TABLE 6
WEEKLY RENTS FOR ONE AND TWO BED APARTMENTS IN MIDTOWN, CITY, DOCKLANDS AT YEAR END

Submarket	2012 £	2013 £	2014 £	% Change since Dec 2013	% Change since Dec 2012
Midtown One Bed	425	425	425	0%	0%
Midtown Two Bed	620	650	625	-4%	1%
City One Bed	450	425	425	0%	-6%
City Two Bed	630	575	575	-4%	-13%
Docklands One Bed	340	350	350	3%	6%
Docklands Two Bed	425	425	425	1%	1%

Source: Hurford Salvi Carr

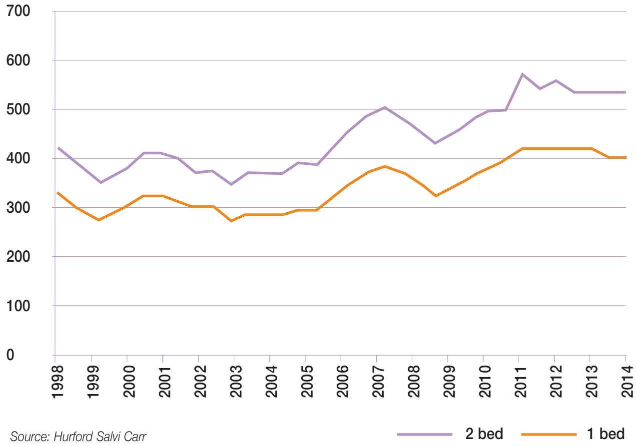
Average rents for a one bed flat remained broadly stable in 2014 but for two bed flats, there was a decline of some 4% in both the City and Midtown. Docklands was the exception with small increases in the rent of one and two bed flats although they remain more affordable than the other two markets.

Over the past two years, the fall in rental values of flats in the City has been marked. Tight planning controls restrict supply within the City Corporation's administrative boundaries but in the boroughs just beyond the City, new construction has been plentiful, as have office to home conversions and this supply has acted as a brake on rental growth.

Rental values have been tempered across the market by the growing availability of serviced, or short-term rental accommodation, which has helped to keep rents at an affordable level across our markets.

A slow sales market generally leads to a rise in properties offered for rent and in the number of potential tenants. When sale prices are flat,

FIGURE 3
WEEKLY RENTS FOR ONE AND TWO BED APARTMENTS MIDTOWN, CITY AND DOCKLANDS



Source: Hurford Salvi Carr

owners choose to look for rental income rather than capital gains, while prospective buyers stay longer in the rental market.

Growing demand will support a stronger rental market in 2015. In the early part of 2014, demand fell, as tenants took advantage of the government's Help to Buy scheme to move out of rented property and into their own homes outside of the central zone. But by the end of the year, the number making that move had already declined. Given what remains for the majority of renters the prohibitive costs of owning a home, we expect greater competition for rental accommodation and that the average length of tenancies will rise to more than two years.

We also expect rental value uplifts for next year, particularly in Docklands where demand has already begun to outstrip supply. It will however, be a relatively short-lived trend, since there is a considerable volume of pre-sold stock under construction that is likely to deliver additional rental stock to the Docklands market in 2016.

2015 will be a year of price correction – with rental values rising while capital values remain flat which provides better buying opportunities for Buy to Let investors as gross yields are likely to improve.

FINSBURY EC1 - FOUR BEDROOM HOUSE IN CONVERTED PUB, LET NOV 2014 £1,550 PER WEEK

MAYOR'S LONDON RENTAL STANDARD

In May 2014, the Mayor launched London's first ever accreditation scheme for landlords known as the 'London Rental Standard' (LRS). Under the scheme, the Mayor will award a certificate of accreditation to any landlord or letting agent that can show it meets a set of commitments to a minimum level of service that any tenant should expect.

The core commitments include: transparent fees; better property conditions; better communication between landlord and tenant; improved response times for repairs and maintenance and protected deposits.

The London Rental Standard brings together seven landlord accreditation schemes under a single framework and it is the first time that professional standards have been set for the whole of London. It aims to ensure that landlords and agents understand their responsibilities and recognise best practice.

A quarter of London's population live in rented homes and there are at least 300,000 private landlords in the city. Although the scheme is voluntary, the Mayor hopes that at least 100,000 landlords and agents will sign up by 2016. Many of London's letting agents, including Hurford Salvi Carr, have already signed up to it. There are four providers for letting agents: Association of Residential Letting Agents (ARLA); National Approved Lettings Scheme (NALS); Royal Institution of Chartered Surveyors (RICS); UK Association of Letting Agents (UKALA) and three for landlords: London Landlord Accreditation Scheme (LLAS); National Landlords Association (NLA); Residential Landlords Association (RLA)

SHORT TERM RENTALS

In June 2014, Communities Secretary Eric Pickles announced his intention to change the law that prohibits homeowners in London from renting their homes for periods of less than 90 days. The move, enshrined in the Deregulation Bill, is a part of the government's wider initiative to reduce bureaucracy in the planning system and it will mean that landlords are free to offer properties on short term or holiday lets.

Until now, holiday lets have effectively been a separate use class in Greater London and required planning permission, although enforcement has been inconsistent and it imposed a restriction on London homeowners that did not exist anywhere else in the country. The issue was highlighted during the London Olympics when many homeowners sought to earn money from letting their homes to visitors. Since then, it has become increasingly difficult to enforce with the rise of peer to peer letting websites such as Airbnb.

The government has said that it will put measures in place to prevent the system from being abused and to ensure that there is no permanent loss of residential homes.

While short term letting has been a growing feature of the London letting market over the last few years, once it becomes legitimate, its impact will be more widely felt. It creates competition for the hotel and hospitality sector, by offering alternatives to the traditional options but it also impinges on the long-term rental market by offering an alternative for corporate rentals for people who might otherwise have signed a lease for a period of three or six months.

We identify three core segments to this market:

Serviced apartments: At the upper end of the supply spectrum, serviced apartments offer highly managed, luxury homes, often serviced by neighbouring hotels, and always with top end concierge services. This sector, serving London's wealthy elite, was flourishing, even without a change in the law.

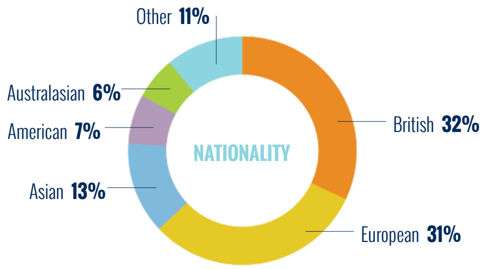
Corporate rental sector: Offering a standard equivalent to a good quality hotel room, but not overtly luxurious, are aimed at the corporate market, for businesses to accommodate staff working temporarily in the city. The usual length of tenancy is a number of weeks and less than three months. A number of specialist serviced providers tailor services for this sector where corporate bookings are made regularly and well in advance throughout the year.

Apartments as alternatives to hotels: This type of short term let is aimed at tourists, often groups or families who prefer the independence of an apartment to the formality of a hotel. This is a growing market and can encompass an array of add-on services such as: cleaning; linen changes; collection from airport; itinerary planning; meeting and greeting and so on. Airbnb is a peer-to-peer variation on this service.

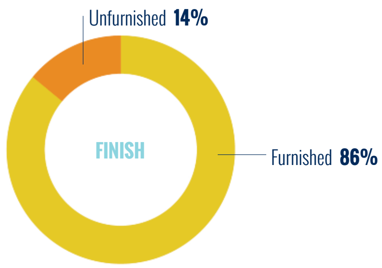
Landlords often use estate agents to secure lettings for under 90 days. It is increasingly common in recently developed blocks with high volumes of supply flowing to the rental market. It can be a source of conflict with full-time residents who believe that the continual change in residents adversely affects the sense of community.

2014 TENANT PROFILES

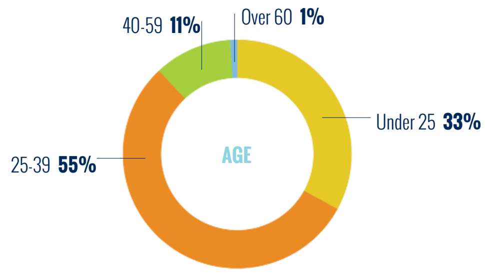
Almost 70% of tenants who acquired homes through our offices in 2014 were overseas nationals. Overall the split was roughly a third British, a third other European and a third from elsewhere in the world with Asians being the most dominant group within that.



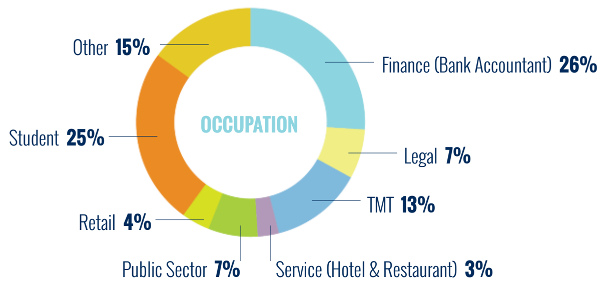
There were noteworthy differences between our submarkets with Docklands attracting a higher proportion of British tenants (43%) but the lowest numbers of American and Australians, whereas our Midtown office dealt with more Asian tenants and the City with more Americans.



It is interesting that, although Canary Wharf is the most popular location for the offices of American investment banks, Americans renting homes in London gravitate to more central locations. The relatively high proportion of Asian tenants in Midtown reflects the demand from overseas students at UCL, King's College and LSE.



Across all our markets, the most common occupation for a tenant is in the financial sector, closely followed by students. Again, these overall ratios disguise distinct differences between the markets. Unsurprisingly, the financial sector was more prevalent in the City and Docklands, where it made up over 30%, while students were by far the most common group at our Midtown office, where they accounted for 62% of all lettings.



Above Data compiled by Hurford Salvi Carr for the period January to December 2014

WAPPING E1 - ONE BEDROOM APARTMENT, LET NOV 2014 £375 PER WEEK

SHOREDITCH E2 - ONE BEDROOM APARTMENT, LET DEC 2014 £450 PER WEEK

New Homes Market

DEVELOPERS TARGET UK BUYERS

London's housing stock like London's infrastructure and transport links has benefitted from considerable improvement and investment over the past 20 years and London buyers are now able to choose from a wide range of superbly fitted and finished luxury apartments in well crafted developments featuring landscaping, comfort cooling and resident services.

In 2014 there was a shift by developers and house builders to offer the domestic buyer off plan opportunities to secure a new apartment ahead of and in many instances instead of overseas buyers. The take up by London buyers was significant but with completion dates often running into 2016 and 2017, majority of off plan sales were to investors and not owner-occupiers.

The significant increases in the marketing of off plan developments resulted in very full property supplements in the National and London press in what became an increasingly overcrowded market. This of course was great news for buyers and centrally located developments attracted buyers with higher budgets across Midtown, City and Docklands in 2014 as buyers sought out and demanded higher quality homes.

A consequence of the increase in supply coupled with pricing that often overshot the resale market by some 10-15% was a slowdown in the sale rate of new homes that resulted in prolonged marketing campaigns often spread out over the majority of the year. Developers adapted to the change in market conditions and built in longer marketing programmes which had a cost impact in most instances but was the preferred route rather than reducing prices to increase sales rates.

As already reported sales of entry level homes up to £1 million were in demand during 2014 but larger new apartments, penthouses and town houses took much longer to find buyers. As prices broke through the £1,000/sqft barrier and sales rates slowed, developers land-buying requirements refocused on sites in City fringe and outer London locations that would support sales at between £750 and 950/sq ft. There was a realisation that London buyers would have to compromise on location as central London prices became less affordable to the UK buyer.

THE SPITFIRE BUILDING, KINGS CROSS N1 - 8 TWO BEDROOM PENTHOUSES SOLD SEPT 2014

The future of Permitted Development Rights beyond the current deadline in 2016 is now likely to be dependent on the outcome of the General Election.

New development launches were fewer in number in the second half of 2014 but all benefited from the combination of strong locations, high specification and long completion dates.

A standout success in the second half of 2014 was the launch of **Barts Square EC1** at Little Britain next to St Bartholomew Hospital by Helical Bar in September. It has been reported that 50 sales out of the first phase release of 88 units had exchanged contracts at prices averaging £1,600/sq ft, the majority to UK purchasers. In total there will be 235 apartments spread across 19 buildings making this a very London scale development. Buyers are able to visit a marketing office at West Smithfield that demonstrates not only the finishes within the apartments but also reinforces the history of the site and the connectivity of the location with Crossrail due to open at Farringdon in 2018.

In September Brookfield Europe and Concord Pacific launched **Principal Tower, Bishops Place EC2** a 50 story luxury block of 243 apartments with construction due to start in Q1 2015 with first phase asking prices reported to average £1,580/sqft

Also in September we launched a development of 8 penthouse apartments all with terraces at **The Spitfire Building, Collier Street, Kings Cross N1** above a refurbished office building. Over one weekend we sold all 8 two bedroom apartments for prices ranging from £725,000 to £925,000 many at above the asking prices, which demonstrates the strength of the market at under £1 million.

At **Rathbone Square, Rathbone Place W1** Great Portland Street Estates announced that it had sold 125 of the 142 apartments off plan by October with prices averaging £1,856/sqft. Sales were conducted both in the UK and overseas and completion is expected in 2017.

In Wapping St George central London launched **Admiralty Wharf, London Dock, Pennington Street E1** the former HQ of News International with prices from £829,950 for one bedroom apartments and £999,999 for two bedroom apartments.

In Bloomsbury we launched a development of 8 spacious one and two bedroom apartments with spectacular views towards The West End, Primrose Hill and The City in August at **21 John Street WC1** for Jaspar Homes. By the end of year 4 flats had been sold at prices ranging from £850,000 for a one bedroom apartment to £1,900,000 for a two bedroom apartment.

Nearby a block of 14 apartments at **Chancery Quarter, Grays Inn Road WC1** close to Chancery Lane underground station was sold in November, together with the ground floor retail spaces to an overseas investor. Hurford Salvi Carr and CBRE represented the developer Midtown Capital.

Investment

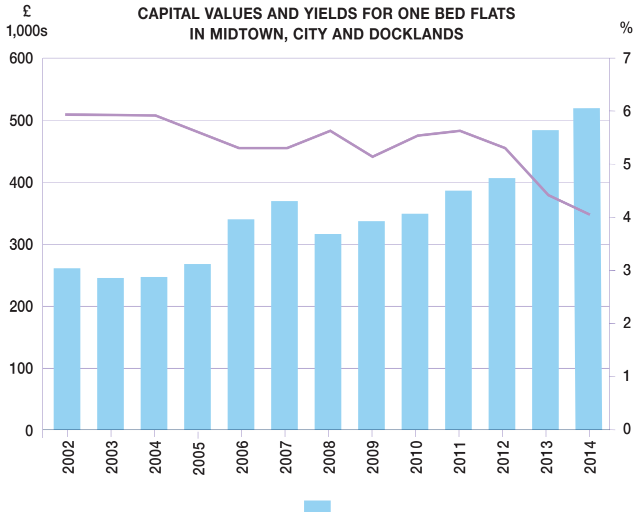
INVESTORS TURN TO SUBURBS FOR BETTER RETURNS

Yields have fallen to 4.1% on a one bedroom flat in our markets. Two years ago, at the end of 2012, the same investment would have yielded 5.4%. Rents remained static over that period which meant that the continuing rise in capital values eroded the returns available to investors. (See figure 4).

For a UK investor, as long as interest rates remain low, a 4.1% return still represents a significant premium over a cash investment but overseas investors are beginning to look elsewhere as the rental returns from central London residential apartments appear unattractive.

Sales of buildings come in different forms. In November, Hurford Salvi Carr acting collectively for the individual owners of 8 flats comprising a block at Minerva House, 21/23 Bowling Green Lane, Clerkenwell EC1, sold the entire property together with the freehold interest to a single investor looking for a long term rental investment. The opportunity to acquire a complete block of apartments close to the future Crossrail Station at Farringdon was a unique situation and the price reflected the strength of demand for freehold residential investments.

FIGURE 4
CAPITAL VALUES AND YIELDS FOR ONE BED FLATS IN MIDTOWN, CITY AND DOCKLANDS



Source: Hurford Salvi Carr — Capital value — Gross Initial Yield %

TAGWRIGHT HOUSE, WESTLAND PLACE N1 - MIXED-USE INVESTMENT SOLD DEC 2014

In December we sold a 18,351 sq ft freehold, mixed-use investment, Tagwright House, 35-41 Westland Place, London N1 located just a short distance from London's Silicon Roundabout. The property consists of 14 apartments, let on ASTs (unbroken) and offers highly reversionary commercial income and underground car parking. Hurford Salvi Carr acted for private clients, and it was sold to an overseas investor for an offer in excess of the asking price of £12 million. This sale comes within weeks of the opening of Hurford Salvi Carr's office in City Road at the end of last year.

Over the past twelve months our Investment Division has reported demand outstripping supply for ground rent investments. The traditional method of valuing this form of investment is to apply a multiple to the total annual ground rent income. Currently this form of investment is changing hands at multiples of 25 times and more.

Our Investment Division sold a number of freehold ground rents in 2014 including the sale of the former 1892 Kingsway College, Sans Walk EC1 in Clerkenwell, which was sold to the residents. Hurford Salvi Carr acted for the original developers Persimmon Homes. Another was the sale of a freehold reversion in Acton W3 comprising some 40 flats of which half were held on leases with only 23 years to run.

A growing number of funds and development companies are unearthing opportunities to buy into London's emerging institutional private rental sector (PRS). TIAA Henderson Real Estate for instance, has recently bought 1-3 Waterson Street, E2, from a private landlord, paying £8.5m for the block of 17 flats.

On the land side the development pipeline looks likely to be dominated by the outer areas in the next two years, such as Camden Town, Caledonian Road, Highbury, Dalston, Victoria Park, Stratford, Bow, Bethnal Green and Shadwell. These areas became the favoured locations for a new wave of land deals to coincide with Permitted Development Rights to convert commercial premises into residential. At the same time a surging office market across Midtown and City including hubs at Holborn, Farringdon, Kings Cross, Old Street, Aldgate and the City Fringe resulted in an upturn in new commercial lettings at record rents that now enable commercial values to compete with residential values in some instances, further reducing the opportunities for residential developments in these core areas.

TABLE 7
INCOME, VALUES AND INITIAL YIELDS FOR ONE BED APARTMENTS AVERAGE OF MIDTOWN, CITY AND DOCKLANDS 2002 TO 2014

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
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	21,060
Capital Value £	260,000	245,000	246,000	270,000	340,000	371,000	318,000	338,000	352,000	386,000	405,000	486,000	520,000
Gross Initial Yield %	6.0	6.0	6.0	5.7	5.4	5.4	5.7	5.2	5.7	5.6	5.4	4.5	4.1

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

Source: Hurford Salvi Carr

Market Prospects

RENTALS TIPPED TO OUTPERFORM SALES

SALES

We expect a two tier sales market in 2015 with demand for properties up to £1 million continuing to attract multiple buyers helped by the new SDLT rules. But at prices over £1 million, the market will be slower in the first half of 2015, as uncertainty grows in the build up to the General Election in May, as well as concerns over the potential introduction of a Mansion Tax.

The typically low gearing of owners across Midtown, City and Docklands mean that property will be slow to come to the market in 2015, since most only consider sales where market conditions allow top prices to be achieved.

There is a chance that we will experience a small spike in properties for sale in Q1 2015 as overseas owners put investments on the market ahead of the April 2015 deadline. After April, overseas owners will become liable for Capital Gains Tax on any uplift in value since the property was purchased. While we do not expect this to influence investors with a medium or long-term outlook, it could prompt investors into action if they had already intended to crystallise a gain in the short term.

We expect prospective buyers to become increasingly frustrated by lack of opportunity as prices stubbornly hold firm until confidence returns to the market following the General Election. In our experience, after the General Election, provided that there is a clear winner and a new Government is formed, the market will quickly regain confidence and we expect a feel-good, honeymoon period where buyers return with renewed confidence in the second half of 2015.

On the whole, we expect a calm market in 2015, with lower sales volumes than in recent years as prospective buyers wait for greater political certainty and relax during a period of slower price growth, while investors hold on to their reliable income-producing assets in a climate of low interest rates. The Bank of England is widely expected to edge interest rates upwards from H2 2015, which, while the level of increase is likely to be minor, will dampen upward pressure on prices.

For properties priced below £1 million, especially one-bedroom apartments, we expect no change in prices over the whole of 2015. Any falls in the early months of the year, will be recovered in the inevitable post-election bounce in June and July.

Above £1 million we expect demand to remain subdued throughout the year and above £2 million the additional purchase costs arising from revisions to SDLT will lead to price corrections. By the end of 2015, we anticipate that properties priced above £1million may lose up to 5% of their value.

Looking to 2016 and 2017, the prospect of an in-out referendum on Europe will have an impact on all aspects of the UK economy including London's housing markets. The most important component in London's housing market is demand and demand is driven by confidence in the London, UK and Global economies. We would expect confidence to evaporate in the build up to a vote on the UK's future and that would stall the market - just at the time when interest rate rises will have started to bite.

RENTAL MARKET

The strength of London's employment market should drive demand in the rental markets across Midtown, City and Docklands in 2015. At the same time higher entry levels in the buying market will encourage more tenants to remain renters in the longer term.

A combination of growth in the number of prospective tenants and the number of properties made available for rent will keep rents in check for 2015, especially as development completions due in 2015 will continue to feed new stock to the market. Rents are, in our view, sustainable for the next 12 months and we expect little change. With stable rents, landlords and agents can expect fewer voids.

However, a robust rental market in the first half of 2015, may lead to increases in some locations of up to 5% through the busier summer months when demand is at its strongest.

We expect strong demand from UK buy to let investors in 2015 as lower SDLT and a strong rental market attracts investment funds. Their attention will be concentrated at the sub £750,000 levels where returns are most attractive.

Landlords will be watching the outcome of the General Election as the Labour Party has announced plans to reform the private rental sector. The proposals include new 3 year tenancies that would limit the amount by which rents could increase each year. In reality, this will not unsettle the majority of landlords since it is usually tenants who insist on shorter 12-month tenancies to give them greater flexibility.

Finally on a positive note, Labour has supported the pensions reforms announced by the Conservative and Liberal Democrat Coalition, which allow individuals to take their pensions in a single lump sum from April 2015. This is likely to fuel greater demand for rental investments from individuals across the UK and we expect to see an influx of additional funds looking for Buy to Let product in the next year.

“Looking to 2016 and 2017, the prospect of an in-out referendum on Europe will have an impact on all aspects of the UK economy including London's housing markets.”

WEST END
39 Store Street
London WC1E 7DS
Sales & Lettings
020 7299 3322
westend@h-s-c.co.uk

CITY
37-41 St John Street
London EC1M 4AN
Sales & New Homes
020 7250 1012
sales@h-s-c.co.uk

CLERKENWELL
1 Britton Street
London EC1M 5NW
Lettings
020 7490 1122
lettings@h-s-c.co.uk
Commercial
020 7566 9440
commercial@h-s-c.co.uk
Development & Investment
020 7566 9444
investments@h-s-c.co.uk

ISLINGTON & SHOREDITCH
227 City Road
London N1 7NA
Sales & Lettings
020 7549 6969
cityroad@h-s-c.co.uk

DOCKLANDS
9 Branch Road
London E14 9HS
Sales
020 7791 7000
sales.docklands@h-s-c.co.uk
Lettings
020 7791 7011
lettings.docklands@h-s-c.co.uk
Property Management
020 7791 7033
management@h-s-c.co.uk
Renewals
020 7791 7022
management@h-s-c.co.uk

HURFORD SALVI CARR

hurford-salvi-carr.co.uk