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Residential update

Central London Development

UK Residential Research | September 2017

The Central London development market has proved remarkably robust during the course of 2017 and has even staged a mini recovery. Oddly though, it doesn't really feel like it. Prices have held firm during 2017, the number of sales has increased slightly and the number of starts has also risen. Even the number of new planning applications was quite strong in Q2, albeit that was Outer Core biased. So it is encouraging, especially for government, that development activity has been maintained despite slightly less favourable market conditions.

Neil Chegwidden
Residential Research

Sales market

Sales prices

0.0%
Q2 2017 **v** Q1 2017

-1.7%
Q2 2017 **v** Q2 2016

Development market

Units started

-10%
Q2 2017 **v** Q1 2017

+4%
Year to Q2 2017 **v** Year to Q2 2016

Sales market

Sales transactions

-3%
Q2 2017 **v** Q1 2017

-8%
Year to Q2 2017 **v** Year to Q2 2016

Development market

Units applied for

+166%
Q2 2017 **v** Q1 2017

-5%
Year to Q2 2017 **v** Year to Q2 2016

Source: JLL, Molior

Central London Development

Sales market

- *Prices stable in 2017*
- *Sales activity rises in Q1 & Q2*
- *Launches continue to ease*

Sales rise

Developers are undoubtedly finding the market difficult at the moment. But this is probably because they are comparing conditions with 2-3 years ago when the market was considerably stronger.

They should take heart from the fact that quarterly sales have been on a general incline since the low ebb in Q2 2016 and have been quite robust during 2017 (see chart).

Sales in the year to Q2 2017 are only 8% down on a year earlier and although this is 19% lower than the average from 2013-2016 it is 38% higher than the average in 2011 and 2012.

So the annual trend in sales volumes has ticked up during the first half of 2017, boding well for the remainder of the year and into 2018. Developers will always want higher sales rates but the fact that sales have remained robust during the recent phase of political and economic uncertainty should be viewed as encouraging.

Core submarkets proving resilient

It is also encouraging that the level of sales in Core markets has remained firm during the past year, accounting for around half of all Central London sales.

And it has not just been the higher volume Central South (including Nine Elms) and Canary Wharf submarkets which have yielded sales.

The more expensive and traditional markets of Central West (Mayfair, Soho, Westminster etc) as well as Central South West (Knightsbridge, Kensington, Chelsea etc) have also seen robust levels of sales.

Launches continue to slow

The robust nature of sales should also be judged within the context of a fast slowing trend in unit launches.

9,310 unit launches were made in the year to Q2 2017, which was 18% fewer than a year earlier and 36% below the peak in Q1 2015.

Prices rebound marginally

Pricing in the Central London development market has stabilised during 2017 with no further price falls following the discounting which took place during 2016.

Pricing remains under pressure however, with most developers accepting the same level of discounts they were a year earlier. But importantly no further discounting has been implemented as sales rates have ticked over during the course of 2017.

Prices across Central London increased by 0.1% on average during Q1 and remained unchanged during Q2. However, due to the declines through most of 2016 the annual change is still negative at -1.7% in the year to Q2 2017.

Demand solid

Positively, the level of demand for new Central London apartments has been solid during the course of 2017.

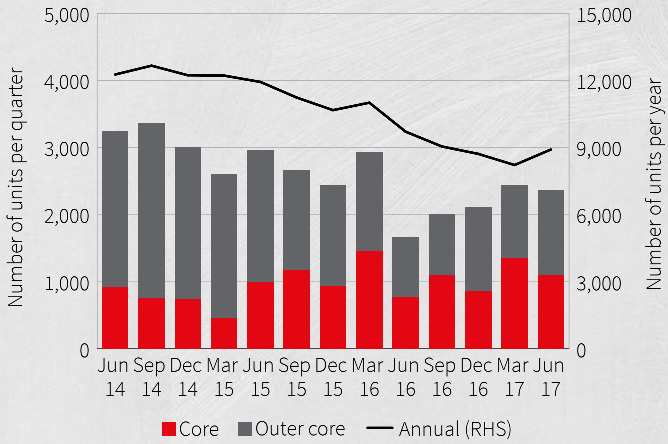
The lower-end of the market, especially when supported by Help to Buy, has remained active while the upper-end of the market has also been quite firm. It is the mid-market, typically the £1.5m to £2.0m market which has been most challenging.

There are still plenty of overseas buyers, and Chinese investors in particular. UK investors are more conspicuous by their absence at the present, deterred by higher stamp duty costs as well as a less favourable income tax regime.

The trend of seeing a greater proportion of sales closer to or after completion has continued with owner-occupiers active at this stage in the development cycle. And this is certainly helping to maintain sales rates.

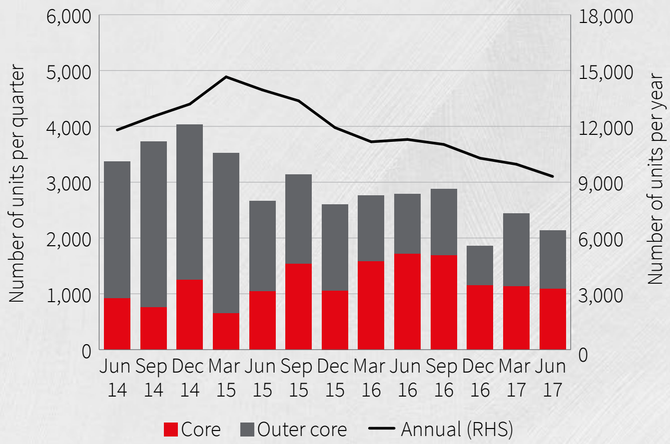
Overall, therefore, the sales market is proving pretty robust despite the political and economic uncertainties and the subdued UK investor sector.

Units sold on steady incline



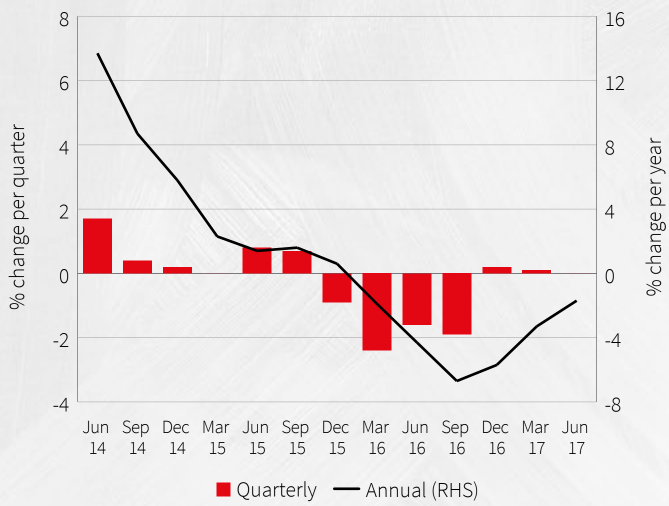
Source: JLL, Molior

Number of units launching continues to slow



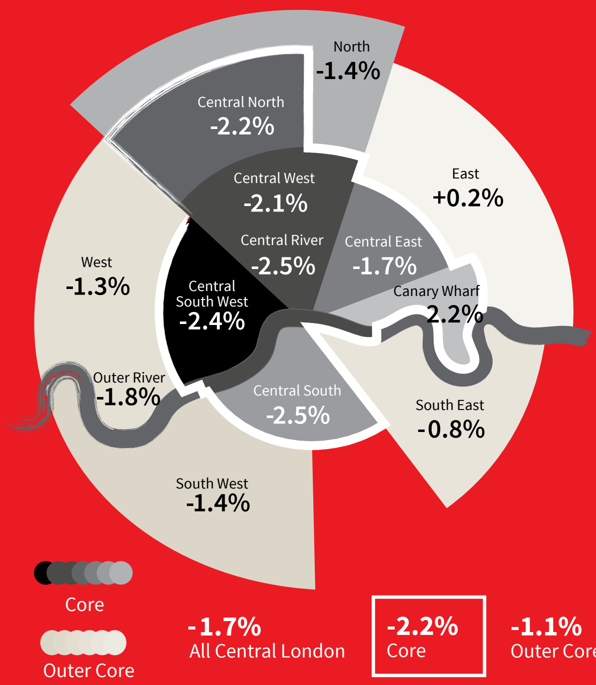
Source: JLL, Molior

Prices steady in 2017



Source: JLL

Prices down in year to Q2 2017



Source: JLL

Development market

- *Unit starts rebound*
- *Planning applications steady in 2017*
- *Development activity in Core markets to slow*

Mixed signals

The Central London development market is providing mixed signals. On the one hand, development starts, units under construction and completions are all at record levels and have shown remarkable resilience to turn around the downward trends that had been emerging.

On the other hand, the planning pipeline (outstanding applications and permissions) is shrinking as the number of units being sent for planning has slowed, especially in Core markets.

New starts rebound

The number of new unit starts per quarter has been volatile over the past 18 months but the strong showing during both Q1 and Q2 this year has meant a recovery in the annual total (see chart).

The slowdown in starts was really only evident during 2016, and mainly during the first half of the year after the additional stamp duty tax announcement and prior to the EU referendum.

2017 quarterly starts are now back on a par with levels witnessed during 2013, 2014 and 2015, a sign that Central London developers are happy to maintain this new and higher volume of delivery. Indeed, the recent level of starts is significantly greater than at any time since 2009.

Units under construction up again

The higher level of starts during the first two quarters of this year has also led to a rebound in the under construction trend.

The number of units under construction looked as though it had peaked in Q3 2016 having declined in Q4 2016 and Q1 2017, but the boost in starts coupled with fewer completions in Q2 has led to this rebound.

There are now more than 36,000 units under construction, almost four times the number back in 2011.

Completions record

As previously predicted, the number of completions pushed through both the 3,000 units per quarter and the 10,000 units per year milestones during the first half of 2017. These are by far the highest levels of completions in the past six years.

New level for planning applications

The number of units sent for planning has certainly slowed during the course of the past two years but a rebound in planning applications during Q2 has led to an uptick in the annual total.

This marginal recovery could signal an important turnaround for the prospects of the Central London development market. Now, rather than being concerned about future delivery given the downward trend in planning applications, recent figures suggest a new level of applications is being established.

Indeed, the number of units being sent for planning during Q2 2017, at 5,100 units, is only marginally below the 5,380 average of the last five years.

Outlook for Core development

The latest planning data, however, paints a startling picture of the growing gap between Core and Outer Core markets.

The data in the table below shows that 49% of units currently under construction are in Core markets but that only 30% of units in the planning pipeline are in these markets.

Looking at planning applications over the last year reveals an even more stark difference. Just 18% of units being sent for planning in the year to Q2 2017 were in Core markets.

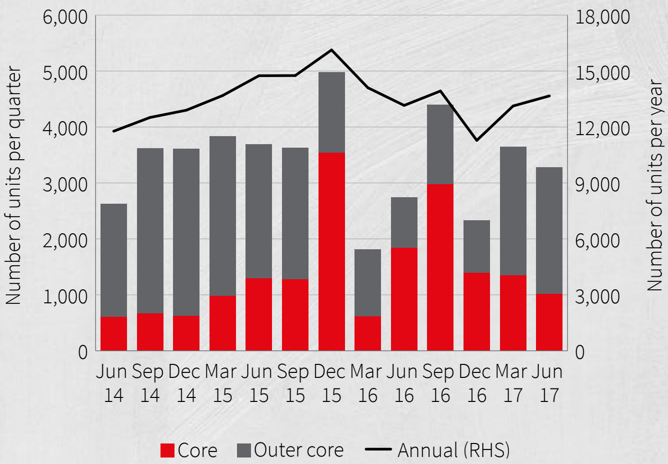
	Core	Outer Core	% Core
Under construction	17,780	18,280	49%
In planning pipeline	28,290	67,610	30%
Applied for in last year	2,980	13,980	18%

This raises serious questions about the level of development activity in Core markets in the years ahead.

We believe that this trend is reflective of the present tribulations in the sales market, namely the high price points, the higher stamp duty regime and the difficulty in selling larger and higher value apartments.

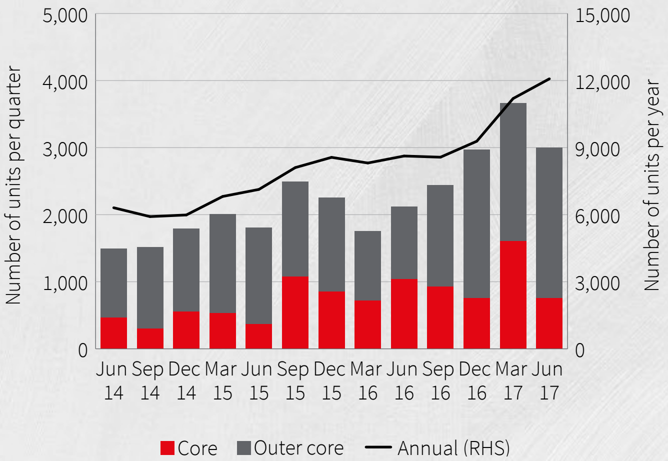
A closer look at planning applications over the past year also reveals a massive eastern bias, with 63% of all units located in just the three regions East, South East and Canary Wharf (see map).

Unit starts bounce back in 2017



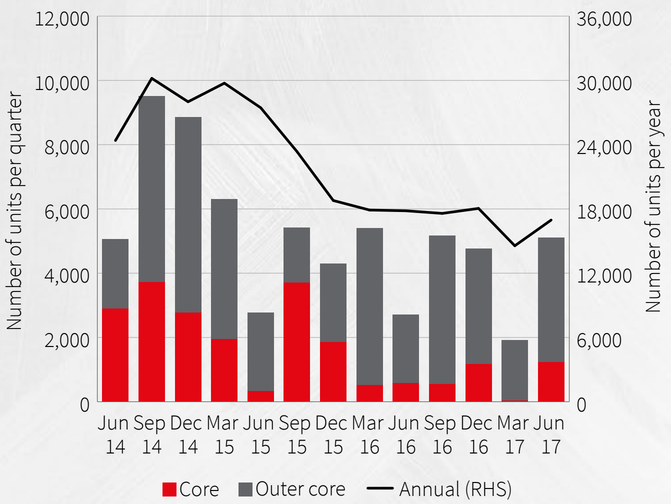
Source: JLL, Molior

Completions continue upward march



Source: JLL, Molior

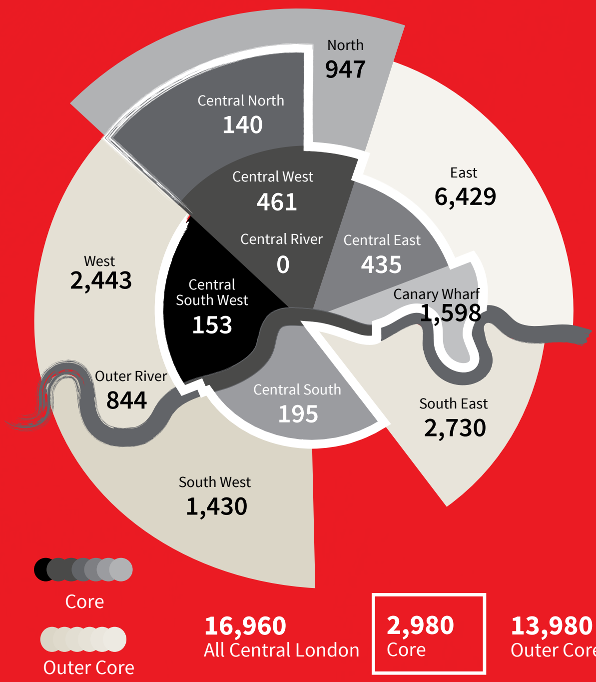
Units applied for finds new level



Source: JLL, Molior

Planning applications have Outer Core bias

Units applied for in year to Q2 2017



16,960 All Central London

2,980 Core

13,980 Outer Core

Source: JLL, Molior

Outlook

The outlook for the Central London development market is far more positive than we might have expected given the headwinds at play.

This bodes well for the next 2-3 years during which time it looks as though political and economic uncertainties for the UK will continue.

More importantly, development activity is being maintained at its current high levels. Developers could easily have taken the axe to operations given the more subdued and uncertain sales conditions. That they have only steadily slowed activity is an encouraging signal.

Despite this, pressures in the land market are deterring developers in central locations. Slow sales rates on higher priced schemes plus the more onerous affordable housing requirements since Sadiq Khan took office are not conducive to a vibrant land market, raising supply questions further out.

However, the next 2-3 years are likely to be unremarkable in terms of sales activity. Given the wider political and economic turbulence market participants will be happy to accept a relatively subdued but remarkably robust marketplace.

For the time being we are sticking by the price and rent forecasts we made almost a year ago. Strong and stable indeed.

House price growth forecasts (% pa)	2017	2018	2019	2020	2021	2017-21*
Central London Developments	0	1	2½	6½	5	15.8
Greater London	1	2	3	5	7	19.2
UK	½	1	2	4	5	13.1

Rental growth forecasts (% pa)	2017	2018	2019	2020	2021	2017- 21*
Central London Developments	1	1	3	3½	4	13.1
Greater London	2½	3½	4	4	4½	19.9
UK	2½	3	3½	3½	4	17.6

*Source: JLL *cumulative growth*

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JONES LANG LASALLE PROPERTY CONSULTANTS PTE LTD

9 Raffles Place, #39-00 Republic Plaza Singapore 048619
Tel: (65) 6220 3888 Fax: (65) 6225 3165
E: InternationalResi@ap.jll.com W: jllresidential.com/sg/ips
CEA Licence No. L3007326E

jllresidential.com/sg/ips