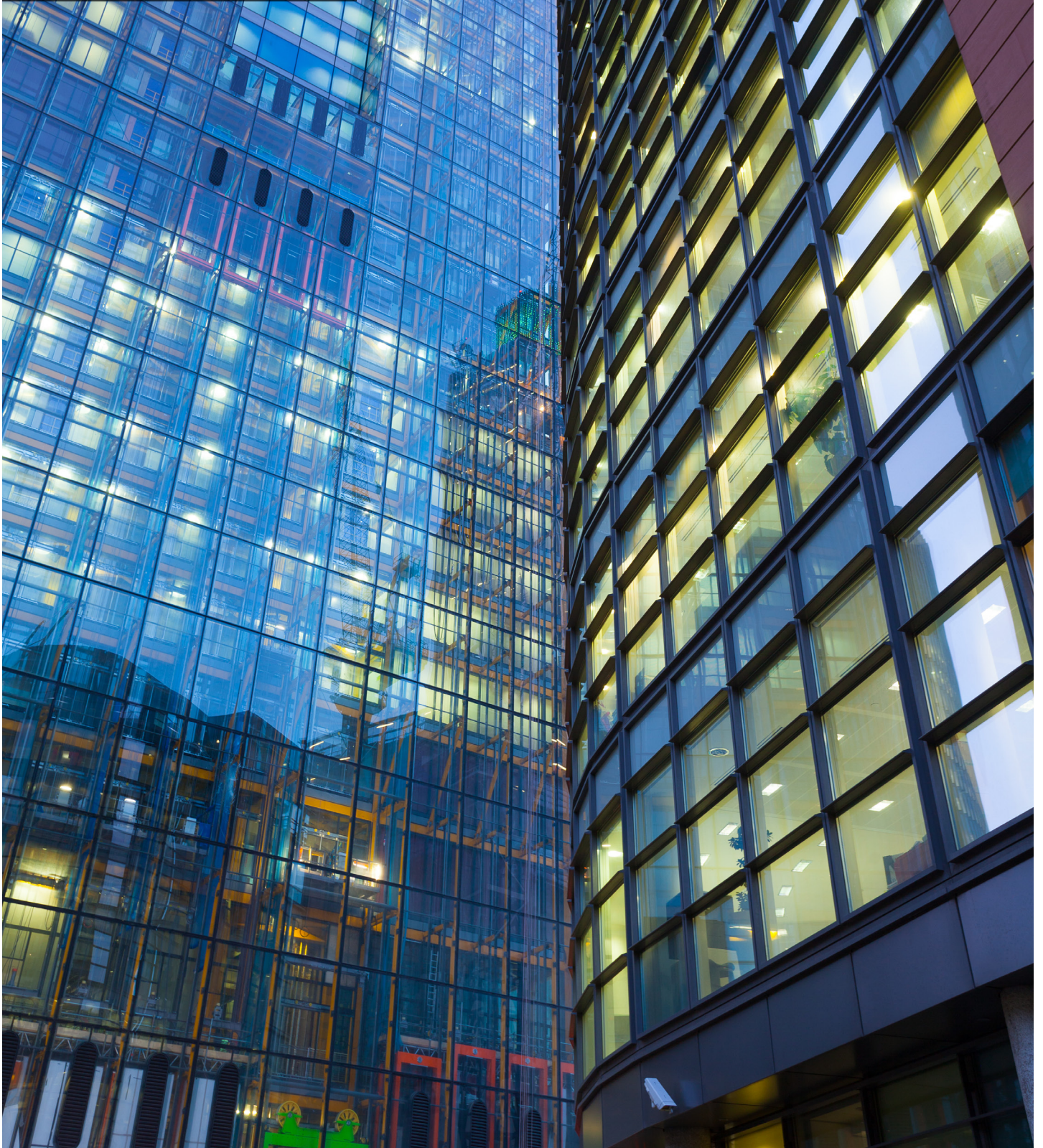


Riverside
CAPITAL

THE
PROPERTY
INVESTMENT
PEOPLE

01/17

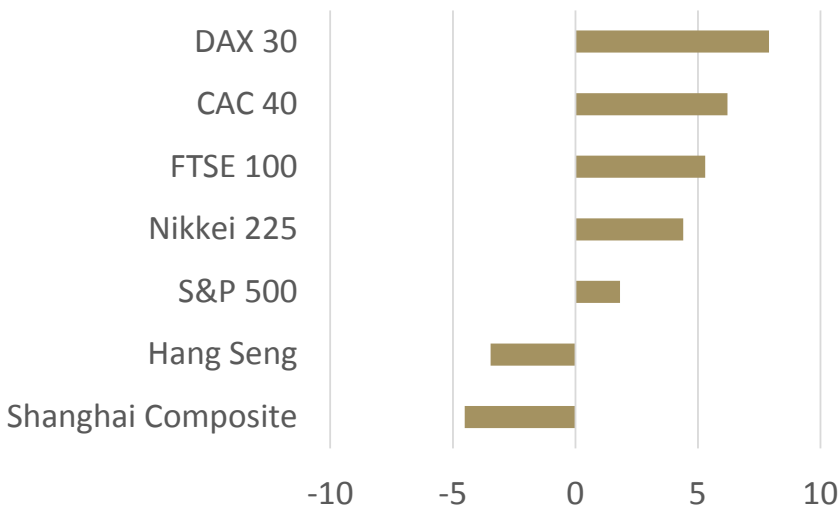
London Property
Market Snapshot:
January 2017



Global Macro overview

With the exception of the Shanghai Composite and Hang Seng indices, key global stock markets recorded gains in December. The strongest gains were in Germany and France, where the benchmark DAX 40 and CAC 30 indices rose by 8% and 6% respectively.

Chart 1: Selected Equity Market Indices (% change December 2016)



Source: Thomson Datastream

The strength of the two largest European equity markets was consistent with some encouraging news about the euro-zone economy. For example, in November unemployment fell by 15,000 leaving the unemployment rate unchanged at 9.8%. December's PMI suggested that GDP growth is likely to accelerate slightly in the fourth quarter, to perhaps 0.3%q/q. And although, headline inflation rose from 0.6% in November to 1.1% in December, this reflected rising energy costs rather than growing domestic inflation pressures.

Meanwhile, economic data coming out of the US was also positive.

December's weighted average of ISM indices also pointed to a pick-up in growth in the fourth quarter, to around 3% on an annualised basis. Meanwhile, the recent recovery in oil prices has meant that US mining output has shown signs of improvement.

Recent developments have done little to alter the prospects for monetary policy in the world's largest economies. Indeed, the monetary stance of central banks in Japan, China and the euro-zone will probably stay very loose, despite the temporary increase in euro-zone inflation. By contrast, inflationary pressures are likely to force the Fed to tighten monetary conditions. The markets are currently anticipating that the Fed funds rate target will increase from 0.5%-0.75% to 1%-1.5% by the end of 2017. But a larger rise, to perhaps 1.5%-1.75%, is certainly a possibility.

Recent developments have done little to alter the prospects for monetary policy in the world's largest economies.

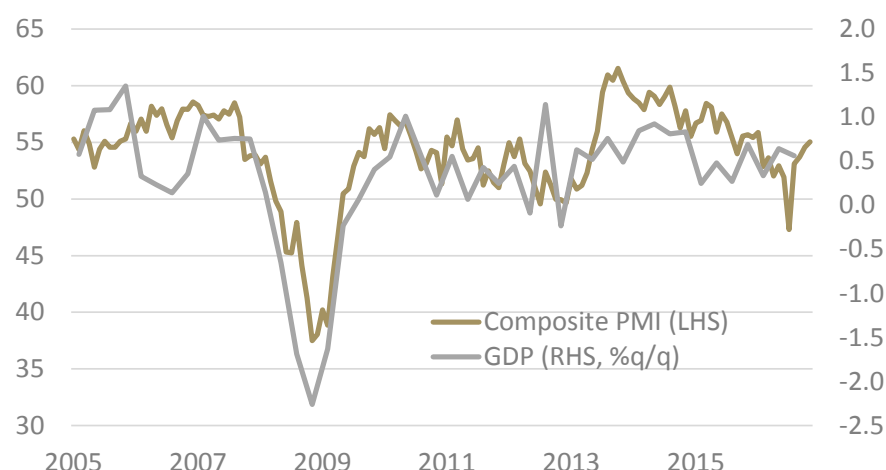
UK Economy

Rising by just over 5%, the FTSE 100 posted solid gains in December

Yet, unlike in recent months, this has not been down to movements in the exchange rate. Sterling hovered around \$ 1.25 over the month. Similarly, at around 1.4%, 10-year gilt yields were broadly unchanged in December.

This suggests that the healthy rise in the FTSE 100 reflected stronger-than-expected economic data. The latest survey data has given weight to the idea that the UK economy has maintained its momentum during the last months of the year. For example, rising from 54.7 to 55.2, the weighted average PMI reached to its highest level since January. Based on past form, this is consistent with GDP growth in the fourth quarter at least matching the third quarter's 0.5%q/q rate.

Chart 2: Composite PMI and GDP growth



Source: Thomson Datastream

Much of the UK's recent resilience reflects the strength of consumer demand. Consumer spending continued to increase solidly in the run up to Christmas, rounding off the fastest growing quarter for two years. Average year-on-year growth for each month in Q4 2016 was 2.8%, twice as high as the average rates for Q2 and Q3.

Admittedly, the outlook for consumers next year is a little less positive.

For example, at minus 6,000 in the three months to October, job creation fell for the first time since 2015. And while average earnings growth rose from 2.4% to 2.5%, inflation jumped from 0.9% to 1.2%, implying that the anticipated moderation in the rate of real earnings growth is underway.

Nevertheless, the pass-through of inflationary pressures should be limited by a competitive environment amongst retailers. What's more, even though further cuts to Bank Rate now seem improbable, the MPC is still likely to keep monetary policy loose to support activity in the short-term.

The pass-through of inflationary pressures should be limited by a competitive environment amongst retailers.

London Residential

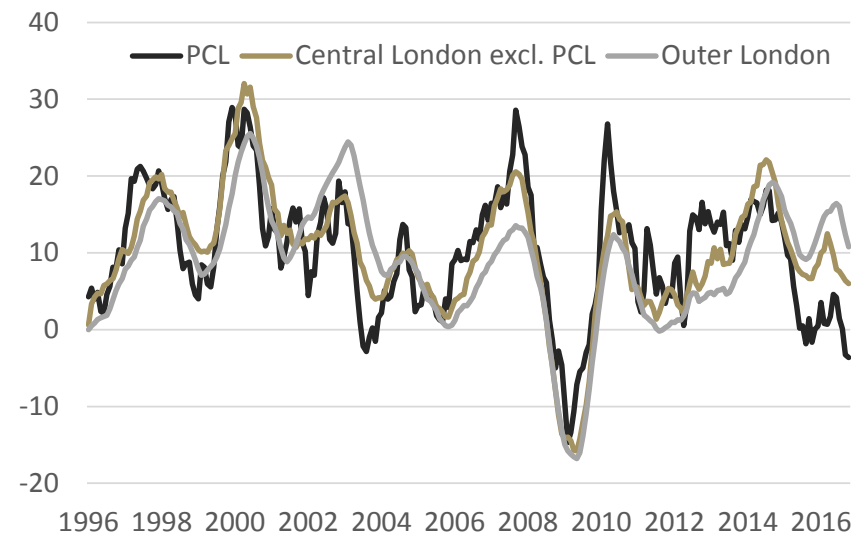
November’s RICS survey for London pointed to a rise in buyer demand.

Indeed, London’s new buyers enquiries balance was in positive territory for a second consecutive month, the first time this has happened since January. But, at just 3%, the balance of surveyors reporting a rise was below the national average, implying that demand in London is comparatively weak.

November’s RICS survey also highlighted the continuing fall in the number of homes for sale. Despite improving from June’s reading of -61%, the new sales instructions balance sat at -7% at the latest reading. Meanwhile, the past prices net balance has notably risen from its reading of -43% in June to at -8%. However, it still indicates that more surveyors are reporting falling rather than rising prices in the capital.

A breakdown of the house price inflation data suggests that, given the higher prices and larger incidence of recent stamp duty changes, prime central London is bearing the brunt of that weakness. The annual rate of house price growth in prime central London has turned negative, falling from 3.5% in January to minus 3.5% in October. Meanwhile, the equivalent figures for parts of central London that are not considered prime were 9% and 5%; and in London’s outer boroughs, 14% and 11%.

Chart 3: Official House Price Index growth by Submarket (% y/y)



Source: ONS/Land Registry

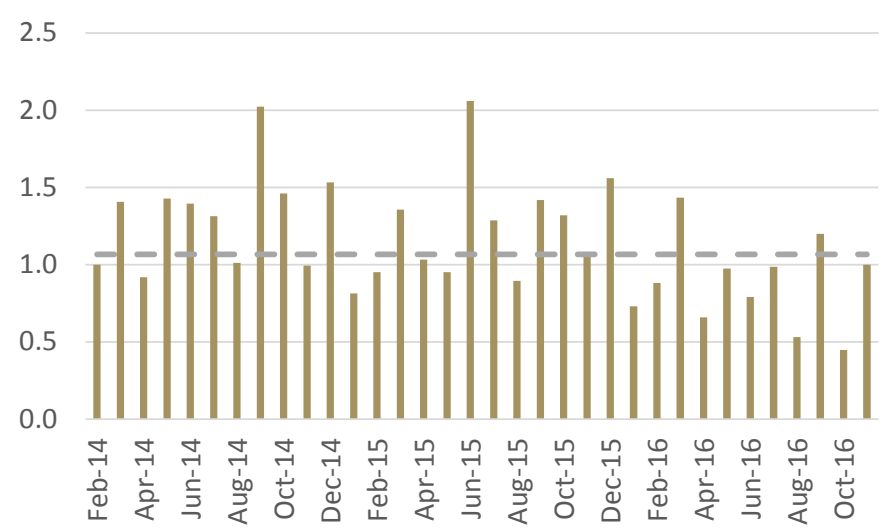
Admittedly, the resilience of the economy and low rate environment should help. Yet, with house prices still elevated, and real incomes likely to come under pressure in 2017, house prices in London are likely to fall in real terms over the next year or so.

The resilience of the economy and low rate environment should help...yet house prices in London are likely to fall in real terms over the next year.

London Commercial

The latest available data suggests that office demand approached more normal levels in November. CBRE highlighted that monthly take-up stood at just over 1m sq.ft. Not only did this represent a doubling of October's figure, but it also sat just a whisker away from its 10-year average.

Chart 4: Central London Monthly Office Take-Up



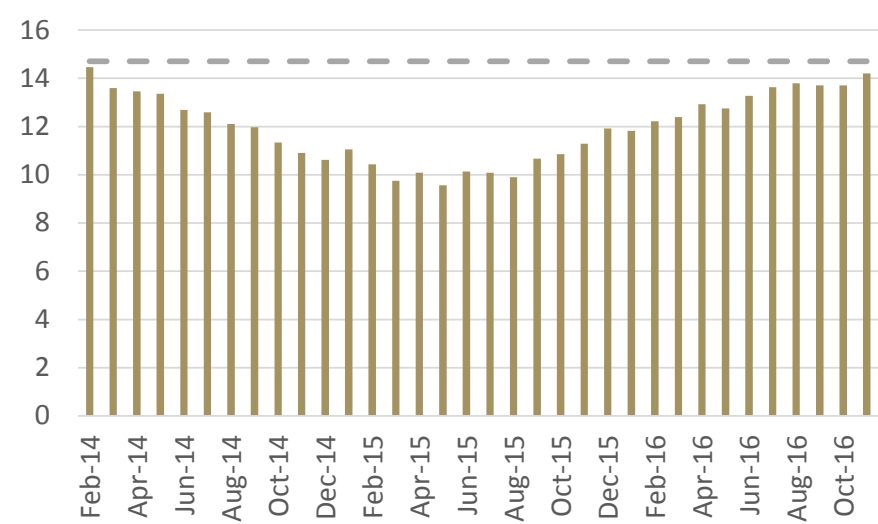
Source: CBRE

Monthly data sits just a whisker away from its 10-year average.



That said, this was not enough to prevent availability from rising. The amount of office space available for letting rose by 4%*m/m*, to 14*m* sq.ft. That left availability close to its 10-year average, of around 15*m* sq.ft. The fact that rising availability was primarily driven by firms releasing space rather than by new supply, suggests that rental growth is very likely to cool over the next few months.

Chart 5: Central London Monthly Office Availability



Source: CBRE

While timely data in the retail sector is scant, there have been some reasons to be optimistic. Data from the New West End Company suggested that, in Oxford St., Regent St. and Bond St., footfall in the run-up to Christmas improved significantly compared to last year. In turn, sales growth in the West End stood at 13.9% in November, and was expected to post another healthy figure in December. The recent strength of London’s high street shops can be attributed to the resilience of consumer confidence, as well as the boost to tourist spending brought on by the weakness of the pound.

Admittedly, given the lumpiness in the data, month-to-month office take-up figures should be taken with a pinch of salt. Nevertheless, it is encouraging that supply and demand dynamics in both the office and retail property segments have been supportive for rental values. This has also been borne out by yield stability in both sectors.

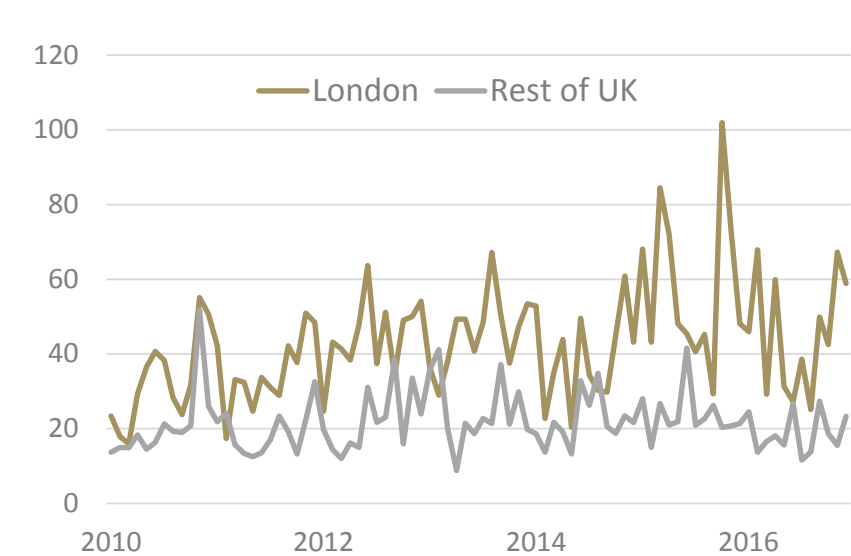
It is encouraging that supply and demand dynamics in both the office and retail property segments have been supportive for rental value.

London Investment

At £2.4bn in December, investment activity in the capital was unchanged compared to a month earlier. However, that was still 87% higher than October's figure and about a third higher than the average seen over the preceding twelve-month period. And although the share of transactions accounted for by the capital fell back, to just under half from two-thirds in November, investors have been very active in London.

Behind the jump in activity over the last two months of the year was a resurgence of large transactions. For example, the Grosvenor Hotel was under offer for a reported £930m in November. What's more, eight of the ten largest deals recorded nationally in November and December, involved assets in London, representing roughly £2.5bn. Moreover, the average lot size implied in the figures also rose significantly, from £43m in October to £59m in December.

Chart 6: Average Lot Size of Commercial Property Deals (£m)



Source: Property Archive

While a comprehensive breakdown of sectoral transaction activity by location is not available, hotel and office buildings and international investors are likely to have made up the bulk of activity. Madison International, CPPIB, Brookfield, Beijing Capital Development KanAm and Asian Growth Properties have all purchased office buildings for more than £150m.

Of course, there is no guarantee that the recent surge in investment will be sustained over the next few months. However, the continued interest in London's office sector is indicative of the fact that overseas investors have not lost faith in the long-term outlook for the market.

For further information
please contact:

Sarah White
Head of Marketing
+44 (0)20 7297 4480
sw@rivercap.co.uk

Jaspal Phull
Head of Research
+44 (0)20 7297 4480
jp@rivercap.co.uk

www.rivercap.co.uk