

Balham Battersea Battersea Park Chelsea Clapham East Putney Fulham Gloucester Road
Hammersmith & Shepherd's Bush Kensington **Notting Hill** Pimlico & Westminster South Kensington Southfields West Putney

The Investor View

Notting Hill
Q3 2015

PORTOBELLO
ROAD,



Douglas
& Gordon

Good to know.

Introduction

Anyone who owns a property in London is a property investor. Our lives and plans often depend on the performance of what is likely to be the largest asset we own. So perhaps it will be helpful to take more of an investor's view of the market.

To produce this report we worked closely with D&G Asset Management, a company we co-founded in 2005. They deploy money into London residential property all the time, so they are constantly analysing different areas and the assets within those areas, seeking to maximise returns.

As well as publicly available sources, we have used the proprietary data that we have been capturing since 1996 to help us make decisions and provide advice and guidance to our clients.

D&GAM has helped us focus on the data that counts and we think the results make fascinating reading.

If you would like to learn more about the Notting Hill area, please do get in touch with our office on Westbourne Grove. Contact details can be found on the back page.

Property Values

In Q2 2015 capital values were unchanged after a strong Q1.

Q2 2015 performance

Capital values in Notting Hill, with the exception of one bedroom flats, were unchanged in Q2. There was a similar picture across many of our other Prime offices where prices rose on average at 0.7%, driven by smaller flats. Our Emerging Prime offices saw stronger prices, at an average growth of 1.81%, fuelled by flats and smaller houses.

In the context of the last 12 months

In Q2, the strongest section of the Notting Hill market was flats. In our Q1 data we had in fact started to detect pre-election strength, particularly in sub £1m stock. Notting Hill flats are one of the few parts of the market across D&G Land that have seen a positive performance over the last 12 months.

The price movements in the Notting Hill house market during Q2 are interesting. The election result, which lifted any threat of a mansion tax on properties over £2m, has had little impact to date.

New Stamp Duty rates (announced in December), however, have made some vendors deliberate for longer before moving. Buying a £3.5m property now incurs SDLT fees of £333,750 (against £245,000 last year and £35,000 25 years ago) but is less volatile than many other asset classes.

The election result produced the ingredients necessary to create a strong and stable market.

The Election Effect

Immediately after the surprise election result on 7th May we forecast that the outcome would produce all of the ingredients necessary to create a strong and stable London property market.

Whilst post-election prices in some parts of the market are rising, data from the last six weeks indicates that in other segments, particularly for higher valued stock, it is too soon to detect any market movement.

Notting Hill Nominal Property Values

	Q2 2015	Q1 2015	Since Q2 2014
1 Bed Flats	0.92%	1.63%	7.56%
2 Bed Flats	0.00%	3.25%	3.77%
3 Bed Houses	0.00%	2.99%	2.99%
4 Bed Houses	0.00%	0.00%	4.35%

Source: D&G proprietary data

Looking to the future, investors should consider the following:

- One of the new government priorities is to return its stake in Lloyds and RBS to the private sector. This will create a political landscape that will see an increase in lending, with potentially helpful consequences for the housing market.
- The early signs of change are evident in the mortgage market. Data from the Bank of England has shown that 5 year fixed rate mortgages (for 75% LTV) fell below 3% in Q2 2015. The recent upward trend in mortgage approvals, although way below historic levels, is also a positive sign.
- We have consistently argued that any fiscal tightening from the new government will keep base rates low.
- We are hearing that following the election, vendors have hardened their stance towards price reduction. In some instances this is understandable. In general, however, as the market strengthens, vendors looking to move up the property ladder should consider the risk of holding out for an aspirational sale price, whilst the purchase price of their new property increases at an incrementally higher rate.

How an investor looks at the market

Residential property investors use two key measures: the capital value of the property and its net rental yield.

You can make money from an increase in capital value and earn additional income by renting out a property you own. The net yield is the annual rent, less expenses, divided by the property's capital value.

Both are important and are influenced by many factors including: supply of new properties,

infrastructure projects, demographics of the area, the economy (in particular, interest and tax rates) and the wider geopolitical picture.

The interplay of these factors is what determines investment returns and what makes property investment decisions so interesting. We hope this report provides some help as you assess your options.

Rents were strong in Q2 2015 after two weak quarters.

Rental Growth & Yield

Q2 2015 performance

In Q2 2015 average rents across D&G Land rose by 1.6%. In Emerging Prime rental growth averaged +1.7%. This was higher than in Prime, which saw an average growth of 1.5%.

Against this rather buoyant background, our data shows that in Q2 Notting Hill (+3.2%) was our strongest performing Prime office.

- Houses produced the strongest rental growth in Q2.
- The weakest performance came from one bedroom flats, which were unchanged in Q2. Interestingly they are the only category that has seen positive rental growth over a 12 month period.
- There is also evidence that the very top end of the rental market has been firm of late.

In the short term, rental values can be volatile; this quarter should be viewed in the context of a weak Q1 2015 (-2.9%) and an even weaker Q4 2014 (-7.9%).

On a 12 month basis, Notting Hill rental values have underperformed our other D&G offices.

Expect volatility in the rental market going forward.

Outlook

In recent Investor Views we have reported that rents in Notting Hill, and other Prime markets, have failed to show any meaningful increases on a long term basis. On page 4 we discuss some of the reasons behind this.

Structural volatility is the new norm in the Notting Hill rental market - we expect this to continue going forward.

Notting Hill Nominal Rental Growth

	Q2 2015	Q1 2015	Since Q2 2014
1 Bed Flats	0.00% →	0.00% →	2.15% ↗
2 Bed Flats	4.35% ↗	-3.36% ↘	-4.00% ↘
3 Bed Houses	5.26% ↗	-5.00% ↘	-9.09% ↘
4 Bed Houses	3.45% ↗	-3.33% ↘	-11.76% ↘

Source: D&G proprietary data

Current Rental Gross yields December 2014

1 Bed Flats	2.50% - 3.70%
2 Bed Flats	2.10% - 3.50%
3 Bed Houses	2.20% - 3.20%
4 Bed Houses	2.20% - 3.20%
10 Yr UK Gilt Yield	2.12%
FTSE All Sh Yield	3.36%
UK Base Rate	0.50%

Source: D&G proprietary data

At the start of 2015 Douglas & Gordon initiated a quarterly index, tracking capital values across Emerging Prime areas of London, particularly in relation to Prime London prices.

In the rental sector, the performance of Emerging Prime in relation to Prime tells an interesting story.

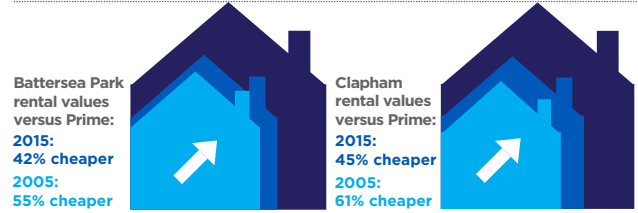
Over the last 10 years, rents in Prime have remained relatively static. By contrast, there has been considerable rental growth in Emerging Prime - consequently, the gap between the two markets is narrowing.

This movement is demonstrated in the charts using data from Battersea Park and Clapham.

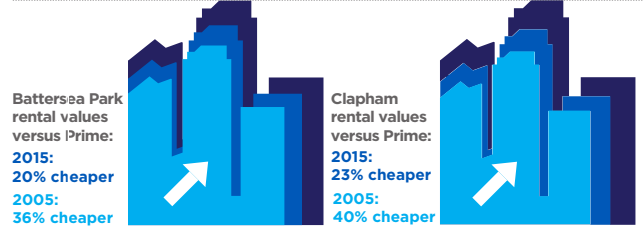
There are several factors behind this convergence:

- I Demographics: There are almost 1m more people working in London than a decade ago. This has generated increased demand in the rental market.
- I A changing corporate environment: Budgets have tightened since the financial crisis. This has led to corporate tenants seeking places to rent outside Prime London areas.
- I Social Trends: Emerging Prime is becoming more fashionable, particularly with overseas renters.

Prime (Chelsea) rental values for 3 bed houses



Prime (Chelsea) rental values for 1 bed flats



Source: D&G proprietary data

Many investors are waking up to the fact that, with changing demographics, the quality of income streams in Emerging Prime are on par with Prime. Additionally, current yields in Emerging Prime are significantly higher than Prime.

It will be intriguing to see how this unfolds.

Notting Hill key facts & figures

Here are the key facts and figures anyone investing in the property market needs at their fingertips.

Nominal Rental Income Growth to Dec 2014			
	2014	5 years	10 years
1 Bed Flats	6%	12%	n/a
2 Bed Flats	3%	19%	n/a
3 Bed Houses	-13%	0%	n/a
4 Bed Houses	-6%	-14%	n/a

Nominal Capital Returns to Dec 2014			
	2014	5 years	10 years
1 Bed Flats	7%	68%	184%
2 Bed Flats	5%	39%	125%
3 Bed Houses	2%	47%	161%
4 Bed Houses	12%	61%	189%

Other Assets Capital Returns to Dec 2014			
	2014	5 years	10 years
Nationwide HPI*	7.20%	16%	24%
Halifax HPI*	7.80%	12%	16%
FTSE100	-2.70%	21%	36%
RPI	1.6%	18%	36%

*House Price Index

Notting Hill 2015 Our view

- Capital values: Strong year ahead for sub £1m, above £1m slow start but picking up in H2 2015
- Rental values to plateau in real terms.

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