Savills Research – Market Review and Outlook 2022

MARKET IN MINUTES

Savills Research

Irish Development Land Market

savills

Macro view • Land sales • Planning

Outlook for 2022

1

Demand high for well-located sites with planning in place

While issues such as planning uncertainty and cost inflation continue to present challenges for the market in general, demand is nevertheless very strong for the right parcels of land. In particular, land in prime areas with planning permission in place has attracted strong bidding across sectors. Even sites without planning permission have performed well if they are sufficiently well located, as evidenced by the sale of 1-6 City Quay for €40.5m in Q3. The price achieved was well ahead of the guide of €35.0m and attracted a deep pool of bidders.

2

Doubts whether the LRD process will succeed where the SHD failed

With the new Large-scale Residential Development (LRD) process now signed into law, the industry is hoping that it will prove successful where the Strategic Housing Development process failed. The increase in speed and clarity emphasised in the LRD process has been welcomed, however, its success continues to be dependent on the efficiency and resourcing of local authorities to be the first point of contact in reviewing and responding to plans. If mismanaged, it could result in the continued use of judicial courts for planning decisions, slowing the planning process and resulting in another missed opportunity to help improve the delivery of residential units.

3

Draft County and City Development plans adding further unnecessary uncertainty

The draft county development plan process is underway across a number of counties in Ireland, with differing approaches to planning policy causing considerable uncertainty for developers. Perhaps the most pressing proposals are presenting in the build-to rent-sector, either by mandating a minimum 'for sale' share of any apartment development or by requiring minimum amenity and storage provisions that would render schemes unviable. The lengthy period of the process also adds to the uncertainty, adding another layer of planning doubts to an already difficult environment to navigate.

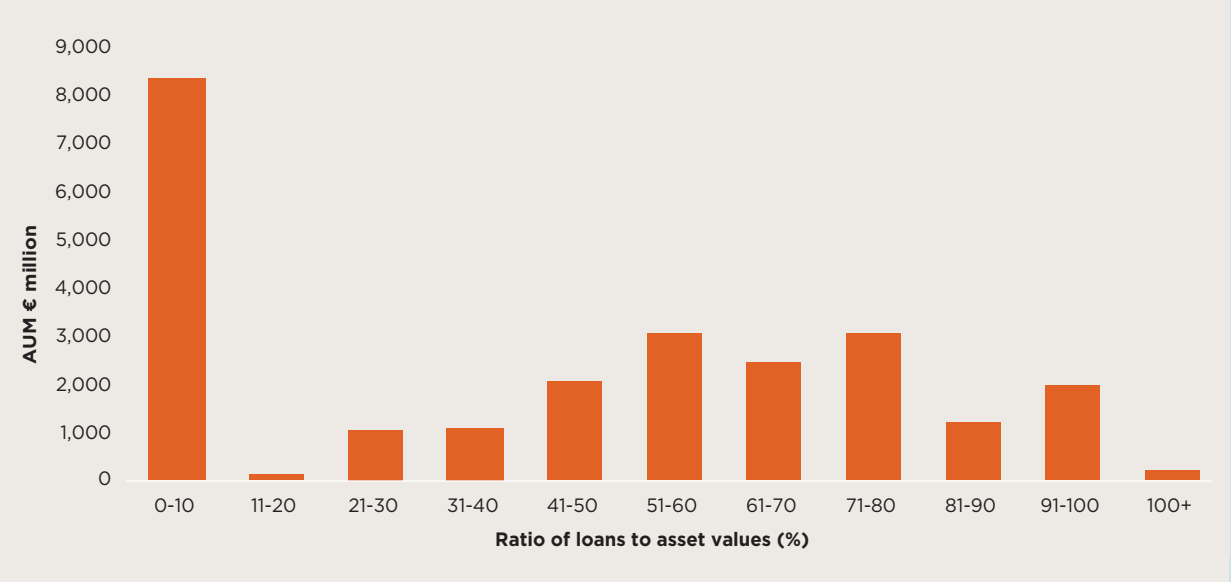
4

Proposed leverage caps may provide headwinds

The Central Bank of Ireland has added to developer uncertainty with proposals to limit leverage on Irish domiciled real estate funds to 50% of the fund's value. Long-term holders of assets would generally not be impacted by such measures as their gearing falls below this threshold. However, the proposed limits present a challenge for residential developers, who typically carry more leverage in their capital structure than this.

Developers require high gearing to hit their target returns and will thus see expected returns fall with the cap. This could impact the development land market, as we may see pushback from developers on land pricing as a way to clawback returns. The proposals may also limit the number of international funders in the residential development land market as their business model would no longer work here.

Figure 1: Distribution of property funds by leverage



Source: Central Bank of Ireland

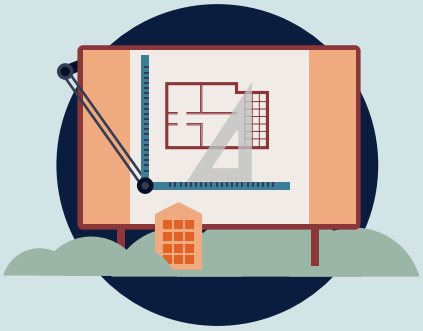
5

Industrial and logistics land pricing to come under upward pressure

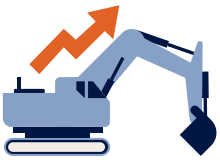
The strength of the industrial and logistics investment market is likely to filter through to the development land market in 2022. The industrial and logistics sector registered strong growth in 2021, resulting in robust demand from occupiers for new product. We would expect demand for industrial and logistics development land to follow and stimulate pricing growth over 2022, as investors and their development partners look to rapidly provide product for this buoyant market. Because of development restrictions in the south, we may see greater demand for industrial and logistics land in north Dublin.

6

Focus on new development land markets



With the industrial and logistics development market likely to go through a significant growth phase in 2022 and greater planning risks to residential developers in prime Dublin areas, developers may increasingly look to new markets to develop parcels of land. This has been aided in the industrial and logistics sector by the less location-specific nature of this market. But also on the residential side, by a greater desire among some city workers to trade larger residential properties for longer commute times. Developers are naturally looking to predict market conditions over the length of a build project. They will closely watch how the post-pandemic return to the workplace unfolds and its ramifications for residential development in locations that would have been previously viewed as peripheral.



9.5%
growth in construction costs

€648m
transacted, up 11% on 2020

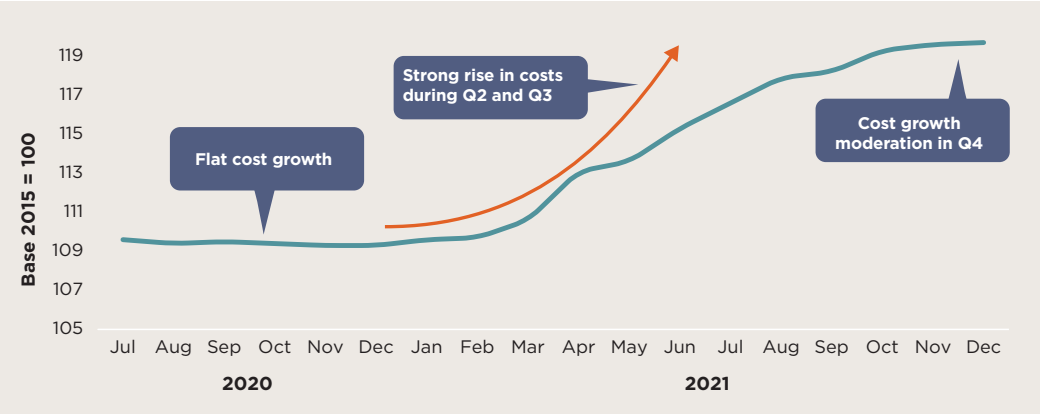
59%
of transactions were for potential residential use

Draft development
plans are providing uncertainty for developers

Macro view

Construction cost inflation impacted the viability of sites in 2021; however, slowing cost growth provides some optimism for developers in 2022.

Figure 2: Wholesale Price Index (Building and construction materials component)



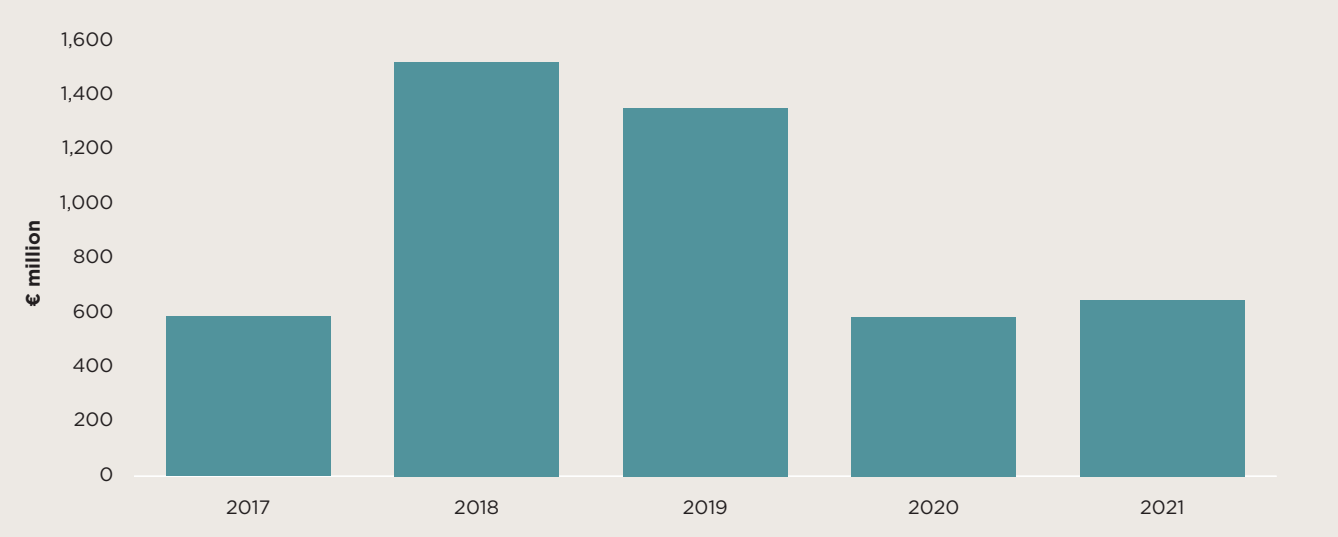
Source: CSO

The rise in construction costs in Q2 and Q3 of 2021 provided a significant risk to the viability of some development land projects, before moderating in Q4. This metric will be keenly viewed over 2022 as construction materials can account for up to half of delivery costs. The cost of building and construction materials increased by 9.5% last year, while rough timber prices rose by 70%.Rough timber is an increasingly important material used in residential development because of its speed of assembly in all weather conditions, unlike concrete, so its strong price growth has concerned developers. While the outlook for construction costs remains mixed, and there is greater overall inflation in the economy, construction cost growth appears to be softening. This may take until the second half of the year to feed through to tender prices. But any consistent moderation in construction cost growth over the year will help provide greater certainty to developers and the development land market. Furthermore, consistent residential price growth is assisting developers in passing on increased costs and, in turn, maintaining viability.


Lands at 1-6 City Quay, Dublin 2, 0.6 acres

Land sales market

Figure 3: Development land turnover



Source: Savills Research

€648m worth of land deals transacted in 2021, representing growth of 11% compared to the previous year's total of €585m. This indicates the market's resilience in 2021, as 2020 was highly influenced by the sale of Project Poolbeg for a reported €250 million. The 2021 development land market has a broader base of activity than in previous years. For example, there were 22 deals over €10 million last year compared to 10 in 2020. However, the market has a long way to go in order to reach pre-pandemic levels of 2019, when there were 29 deals over this threshold and a total of €1.4bn transacted.

Like a number of sectors of the property market, 2021 was a year of two distinct halves. The first half of the year was impacted by the difficulty of inspecting sites, with some vendors choosing to delay the sales process until later in the year as restrictions lifted. The second half of the year saw more robust sales volumes, comprising 64% of annual activity. There are approximately €450m in deals either currently sale agreed or being marketed. This significant level of deal flow highlights the depth of demand for sites and suggests that 2022 will be another robust year.

The largest transaction of the year was Eagle Street Partners purchase of the six-acre site at Castleforbes Business Park for €78.5m from Glenveagh in Q3. The site has planning permission for 702 residential apartments and 219 hotel rooms. The residential component is for build-to-rent units and will form part of its growing private rented sector portfolio. 1-6 City Quay made up the second-largest deal of the year and was purchased by KC Capital for €40.5m, also in Q3. This site represents one of the last remaining undeveloped waterfront sites in the city centre and received interest from several motivated bidders pushing the final price substantially over the €35.0m guide price.

€78.5m

Eagle Street Partners' purchase of the six-acre site at Castleforbes Business Park was the largest deal of the year.

Table 1: Top five deals by price achieved

Property	Planning Permission	Potential Use	Size (acres)	Price Achieved	Price per acre
Castleforbes Business Park, Dublin 1	Yes	Mixed-Use	6.0	€78,500,000	€13,083,333
1-6 City Quay, Dublin 2	No	Office	0.6	€40,500,400	€67,500,667
Cork Street, Dublin 8	Yes	Co-living	1.1	€27,500,000	€25,000,000
Airlinks, Cherryhound Junction, Co. Dublin	Yes	Industrial and logistics	64.5	€26,000,000	€403,101
The Papermill, Clonskeagh, Dublin 6	Yes	PRS	3.4	€18,000,000	€5,294,118

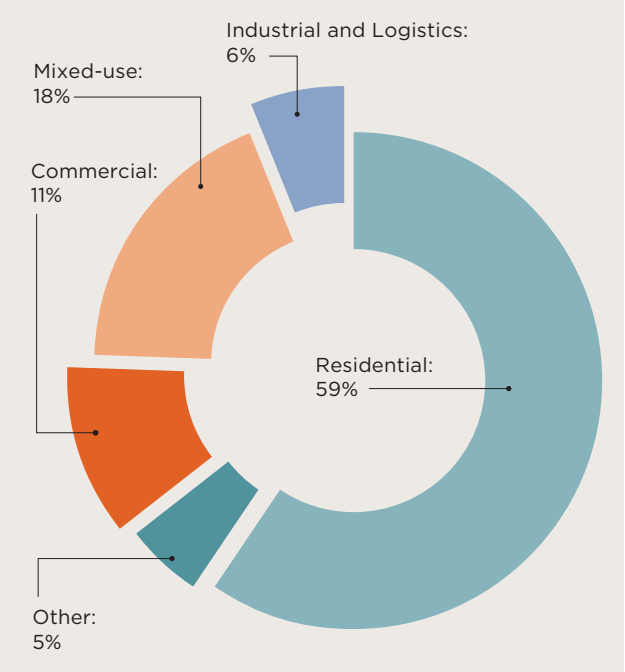
Source: Savills Research

The largest development land deal of Q4, and the third largest of the year, was a joint venture purchase between Irish entity Grayling Properties and private equity investor Crossroads Real Estate. The purchase of the 1.1-acre site at Cork Street in Dublin 8 for €27.5m represented a 10% premium on the guide price. The land comes with planning permission for 378 co-living beds, with the price paid representing a valuation of €72,750 per bed. The Housing Minister banned these developments in December 2020, although sites with planning in place before the formal induction of the ban are allowed to proceed. By limiting future competing supply, the ban on further co-living development will likely raise land values for those with planning in place.

Other notable deals that transacted include the sale of the Airlink lands at Cherryhound Junction in County Dublin. The €26m deal was the largest industrial and logistics transaction and the fourth largest development land transaction of the year. The 65 acre site, located just off the M2 motorway, will form a significant part of the industrial hub in the North-west suburbs, which benefits from close ties to Dublin Airport, the M1, M50 and the port tunnel.

Outside of the Greater Dublin Area, one of the largest land sales was a residential site in Drogheda, Louth. The land at Ballymakenny Road sold for €10m and has FPP for 1,056 units and will form a significant part of the North Drogheda Environs Local Area Plan that eventually hopes to cater for 20,000 people in the area.

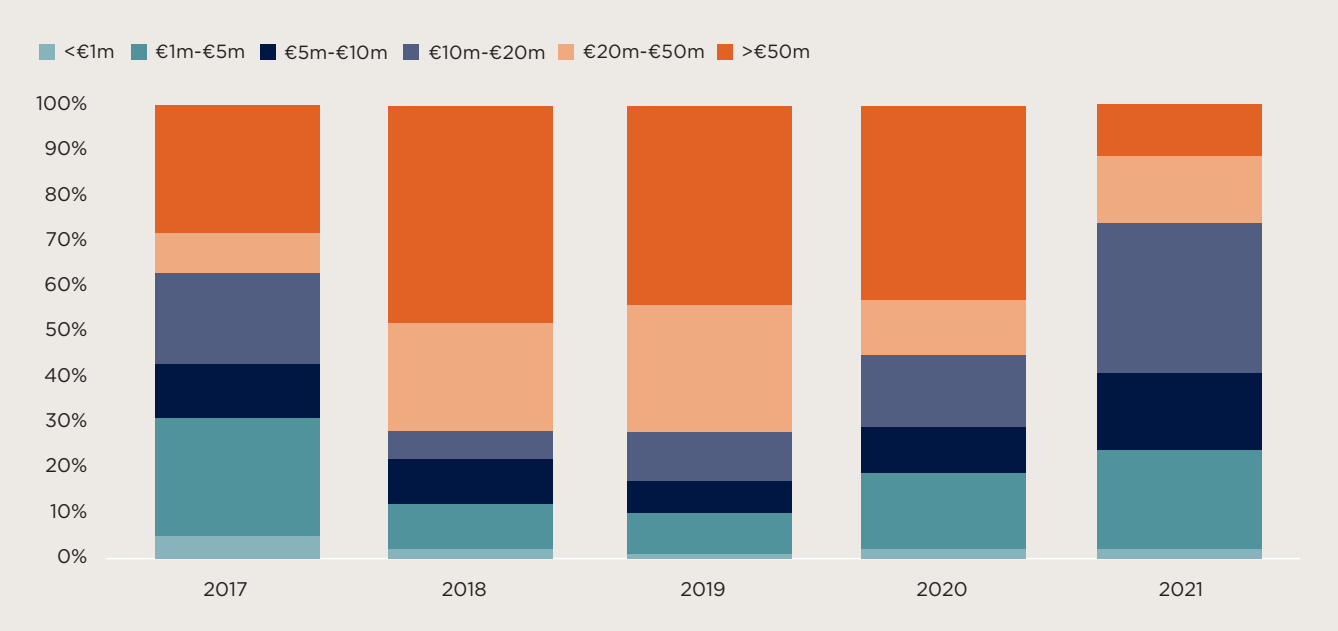
Figure 4: Turnover by potential use



Source: Savills Research

> **The largest development land deal of Q4, and the third largest of the year, was a joint venture purchase between Irish entity Grayling Properties and private equity investor Crossroads Real Estate.**

Figure 5: Transactions by size



Source: Savills Research

Whilst there is always a premium for sites with planning in place, increased planning uncertainty and cost inflation combined to further elevate this spread in 2021. There is greater uncertainty for developers taking sites through the planning process as a number of legislative risks started to present themselves in 2021. National and local policy changes in the year (more information in our planning review section) have provided significant uncertainty, costs and delays for developers taking sites through the planning process.

The residential sector continues to make up the majority of development land sales at 59% of market turnover; this is slightly higher than the five-year average of 53%. Ireland's significant need for quality residential units is fuelling strong demand for residential development land despite planning risks. There has also been resilient demand for the commercial sector despite uncertainties surrounding the pandemic and the future of the office market. Land sales for the industrial and logistics sector continued its market share growth, encouraged by a supply-demand imbalance in the occupier market, driving rental growth and tightening yields. The industrial and logistics sector contributed 6% of land turnover in 2021, up from 2% in 2020, and we expect this trend to continue throughout 2022.

Dublin's proportion of land sales fell to 64% of total transactions in 2021, significantly below the 81% average witnessed over the past five years. This sales activity appears to have shifted to the Greater Dublin Area, with Kildare (5%), Wicklow (7%) and Meath (9%) making up 21% of transactions in 2021; this is substantially higher than their historic combined average of 11%. This may indicate that developers have started to look outside of Dublin for development opportunities as higher land prices and planning regulation changes influence developers' decision making.

"Whilst there is always a premium for sites with planning in place, increased planning uncertainty and cost inflation combined to further elevate this spread in 2021."


Lands at Roundwood, Co. Wicklow, 7.9 acres

Planning Review and Outlook

2021 was another busy year for the planning system, with national and local policy changes affecting new developments. These national and local changes have proposed several new restrictions on the residential sector that have impacted development viability. Meanwhile, increased judicial reviews of major residential developments has provided additional causes for concern for the industry and government.

National planning changes

At the national level, the government published the 'Housing for All' plan in September 2021. The plan set out how the government intends to meet its target of 300,000 new homes over the next 10 years. Policy changes include:

- **Part V:** Increased contribution, from 10% to 20%, to include affordable housing and cost rental housing.
- **Large-scale Residential Development:** Introduction of a new planning process for large-scale residential developments to replace the 'Strategic Housing Development' process.
- **Urban Development Zones:** UDZs will be a plan-led approach that, once adopted, will allow for fast-track decisions similar to the 'Strategic Development Zones' application process.
- **Land Value Sharing:** This seeks to capture more of the value uplift from the rezoning of land to residential or mixed-use. These 'Kenny Report' style powers are intended to secure land or financial contributions for the provision of infrastructure and social and affordable housing.
- **Replacement of the Vacant Site Levy:** A new tax of 3% on land hoarding has been introduced to activate vacant lands for residential development.
- **Reforming the judicial review process:** Review to address the large increase in challenges to new housing developments.

2021 also saw the continued increase in judicial review challenges of major residential developments. Whilst the current system is under review in the 'Housing for All' plan, 2021 witnessed a glut of judicial review challenges to new housing developments. The increasingly litigious nature of residential planning has had a significantly negative impact on residential delivery rates. The cost associated with taking a sizeable residential development through the planning system has always been high. Now applicants must factor in the potential of prolonged court cases, legal costs and revised planning application costs. These judicial reviews have essentially added a second stage to the SHD process. Any unnecessary costs and delays caused by these judicial reviews affect the viability of schemes and deprives the State of much needed residential units.

Local planning changes

A number of local authorities have either published or are due to publish their local development plans; these include Cork City and County, Galway County, Fingal County and Dublin City to name just a few. Whilst there is a lengthy consultation period with all of these plans, the lack of certainty is creating significant hesitancy for developers. While development plans from Dublin City and Dún Laoghaire Rathdown County Council's have gained attention, plans from across the country have looked to implement a number of policies seen by the sector as being restrictive to residential development.

1 Dún Laoghaire Rathdown (DLR) County Council

Dún Laoghaire Rathdown (DLR) County Council has proposed policies that require a rental scheme's unit mix to have at least 40% three beds. We believe this is restrictive as apartment schemes best meet the requirements of individuals, couples and non-family households. These groups are far more likely to reside in apartments than couples with children. According to the 2016 census, 31% of individuals, 25% of couples and 43% of non-family households lived in apartments in DLR compared with just 12% of couples with children. This increase in three-bed provision charged at market rents would create affordability challenges for price-conscious consumers. This would result in an oversupply of units that are unsuitable for the target rental demographics, while exacerbating the undersupply of much needed one and two beds units. The DLR development plan also looks to increase the storage space required to 8m^3 for a four-person two-bed, with this storage to be provided in the basement or ground floor. These two policies reduce unit density and ultimately impact the affordability of schemes, making some sites economically unviable and negatively impacting the future supply of rental units in DLR.

2 Dublin City Council

One of Dublin City Council's more controversial plans is the general presumption against developments under 100 units and schemes comprising of 100% BTR units. The plans have suggested that in a BTR development a minimum of 40% of the proposed units should be offered to individual purchasers. This restrictive policy has been met with opposition by the investment community and the Office of the Planning Regulator, and significantly impacts international investors trying to achieve scale in Dublin's residential market. This may influence decisions for similar capital to further invest. Furthermore, these investors typically want to control the vast majority of units in a block to implement asset management changes and minimise operational costs. This mixing of rental units with units for purchase is an additional risk. But most crucially, the policy doesn't address the viability issues in building city centre apartments for sale, as prevailing market prices don't necessarily meet the costs of building.

3 Local development plans

Local development plans across the country have pushed developers to build untested residential formats, which ultimately may restrict developers from the market. Outside of Dublin, proposed plans have looked to force a minimum density level of 35 residential units per hectare. This requires developers to build apartments and duplex units in markets where local demand is weighted towards family houses. Duplex units have a higher construction cost than family homes, whist the 10% rate of stamp duty for bulk purchases still applies. Duplex units also have a lower market value than family homes, and demand for the product remains untested in more rural locations, thus, a significant risk for developers. In sum, they are more costly to build, have less end value and suffer from a lack of demand outside of Dublin and major cities.

Conclusion

These three examples show how a one size fits all approach to local planning can be detrimental to providing much-needed residential units for rental and purchase markets. Planning considerations undertaken should be on an individual basis and thoroughly consider how the individual scheme works in the community and meets local demand. The government is committed to reviewing Irish planning legislation, and the long-awaited e-Planning system will help developers. It will be interesting to see if the government chooses to intervene and address some of the more controversial policies in current draft development plans.

Savills team

Please contact us for further information

John Swarbrigg
Director, Development Agency & Consultancy
+353 (0) 1 618 1333
john.swarbrigg@savills.ie

Ebba Mowat
Divisional Director, Development Agency & Consultancy
+353 (0) 1 618 1413
ebba.mowat@savills.ie

Andrew Sherry
Divisional Director, Development Agency & Consultancy
+353 (0) 1 618 1452
andrew.sherry@savills.ie

Raymond Tutty
Associate Director, Planning
+353 (01) 1 618 1316
raymond.tutty@savills.ie

John Ring
Director, Research
+353 (0) 1 618 1431
john.ring@savills.ie

Alex Norwood
Senior Research Analyst
+353 (0) 1 618 1466
alex.norwood@savills.ie

Andrew Blennerhassett
Research Analyst
+353 (0) 1 618 1705
andrew.blennerhassett@savills.ie