

Savills Research – Q2 2021

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MARKET
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MINUTES
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Irish Development Land Market

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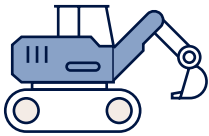


Macro view • Land sales market • Outlook



47%

of land sales in Q2 were for residential use



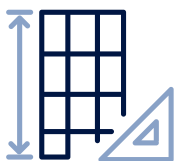
Cost of a new 3-bed house could increase by

€12-15k



Appetite remains for newly built

OFFICE STOCK



SHD related planning uncertainty has been

RESTRICTING OUTPUT

Macro view

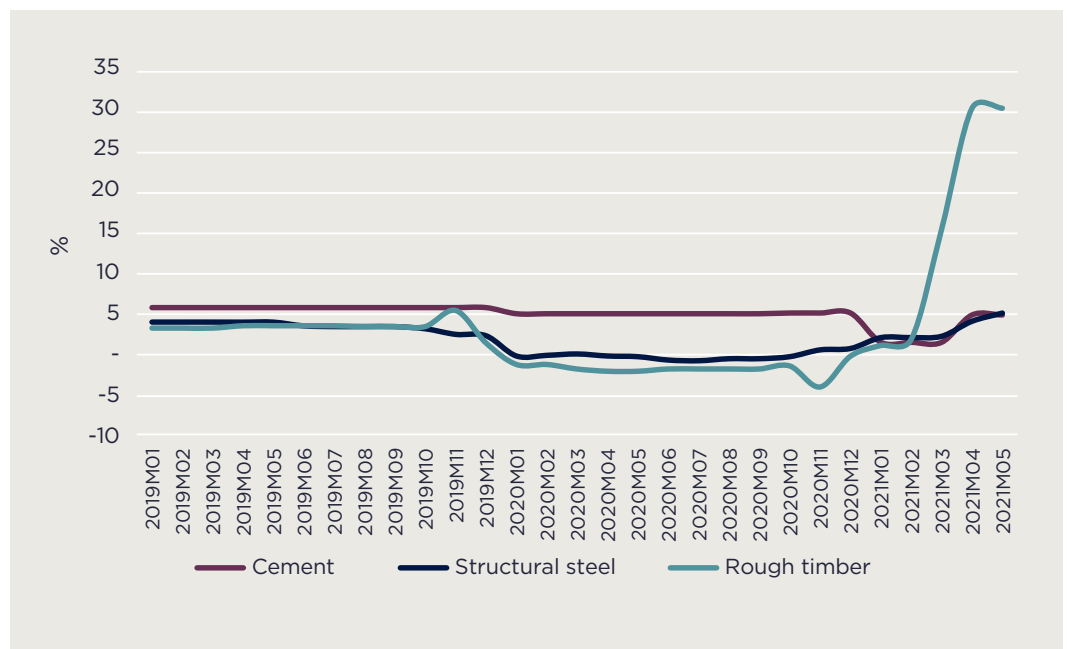
Focus to pivot back to sectoral market dynamics as pandemic-related uncertainty begins to wane.

Over the last number of years, strong population growth combined with a chronic shortage of supply has led to steady growth in house prices and rents. While this has generated steady interest in land with potential for residential development, viability constraints and a shortage of sites with planning permission have restricted output.

Further to this, the Covid-19 pandemic is causing

a global shortage in many building materials which is leading to strong inflationary pressure on construction costs. The strongest price growth has been for rough timber, with prices increasing by almost 30% since the start of 2021. A survey of members of the Irish Home Builders Association found that the average price of a new 3-bed house could increase by €12,000 to €15,000 by the end of 2021 to adjust for these increased costs.

Figure 1: Construction materials price inflation



Source: CSO

Despite these rising costs, the new homes market continues to perform strongly with anecdotal evidence from our agents pointing to an over-subscription for new schemes brought to the market. Indeed, data from the CSO shows house prices grew by 3.1% in the first five months of 2021. Notably, demand for residential units is such that these rising costs are being absorbed by buyers as prices continue to rise.

On the commercial side, appetite remains for newly built office stock, with predictions of a large-scale

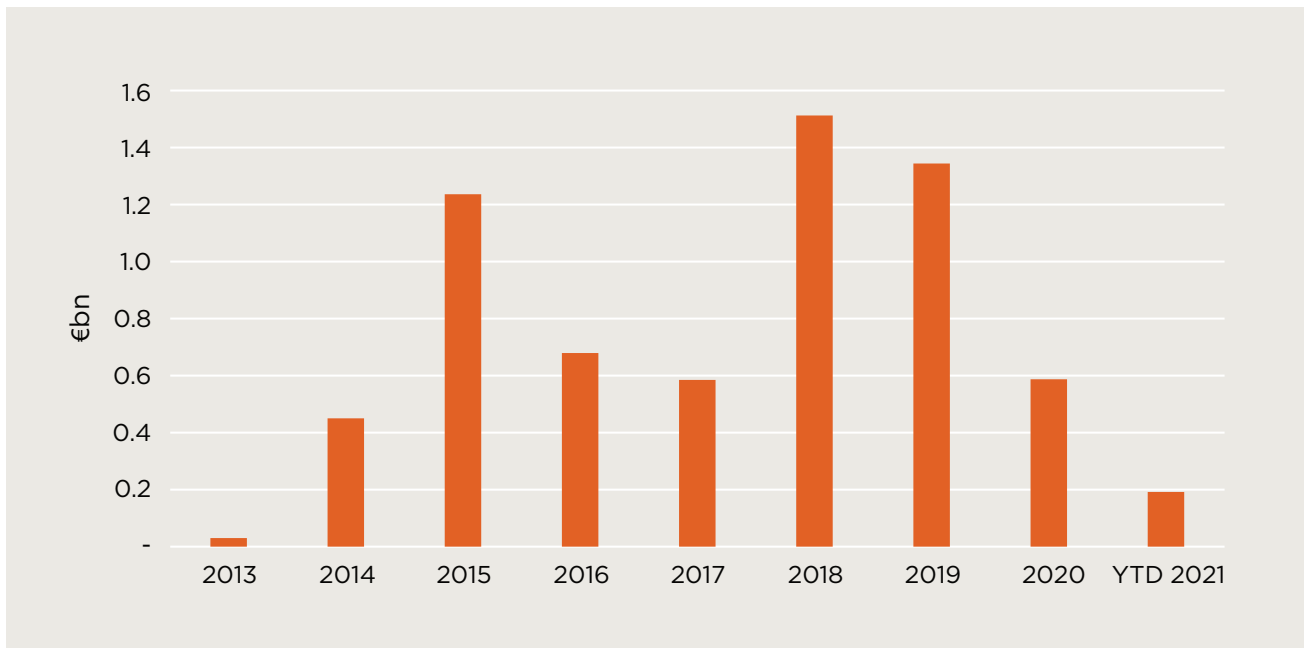
shift to remote working looking increasingly unlikely as hybrid models emerge. Meanwhile, the industrial and logistics market is characterised by a shortage of modern stock and an occupational market that has remained relatively robust throughout the pandemic. Indeed, the pandemic has hastened the shift towards e-commerce which generates demand at a greater rate than traditional bricks and mortar retail. This will drive stronger demand for industrial and logistics space in the medium to long-term if this trend persists.

Land sales market

Irish land sales totalled €99 million in Q2, which brought total year-to-date turnover to €194 million. This represents an increase of 16% compared to the same period in 2020 when turnover reached €167 million. Notably however, it marked a decline of 59% compared to the first six months of 2019 when turnover reached €473 million.

Crucially the first halves of both 2020 and 2021 should be considered in the context of national lockdowns. In Q1 2021, most formal sale processes were postponed while on-site visits were prohibited during the level 5 restrictions. As a result, many sales processes were deferred which impacted half-year land sales volumes.

Figure 2: Development land turnover



Source: Savills Research

There is currently a lack of development opportunities available, as evidenced by the subdued quantum of land being marketed for sale. Many prospective sellers were previously adopting a wait-and-see approach to the pandemic, particularly in the first half of this year. With that being said, we are seeing more confidence returning to the market as a whole and we expect to see an increase in the supply of development land in Q3 as pandemic related uncertainty is reduced, with a number of large transactions - both with and without planning - expected to come to market in September. Seasonality will also play a role, with Q3 typically seeing elevated levels of activity in any given year.

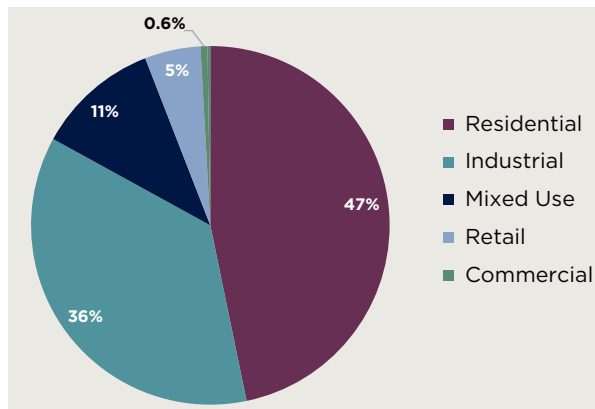
With the current uncertainty surrounding the planning process, it is unsurprising that land with residential zoning made-up the highest share of turnover in Q2. In total, we estimate that residential zoned land sales accounted for almost 50% of sales volumes, with many of the mixed-use sites that traded in the quarter also having the potential to accommodate a significant residential component. A high proportion of land with industrial zoning also traded in Q2, accounting for 36% of turnover. The industrial market is currently suffering from a similar lack of supply with new development required to ease the shortage.

🍷 We expect to see an increase in the supply of development land in Q3 as pandemic-related uncertainty is reduced. 🍷

Top deals



Figure 3: Q2 land sales by potential use



Source: Savills Research

The largest deal of the quarter was the sale of the Airlinks landbank, located just off the M2 motorway. The site, which has 55 acres zoned for industrial use and an additional 10-acres with development potential, traded for €26.0 million. The second-largest transaction was the sale of an 11-acre site on Glenamuck Road, Dublin 18 which traded for €10.5 million. The site has full planning permission granted by An Bord Pleanála in 2020 for a Strategic Housing Development of 197 residential units. This follows on from a deal for a 33-acre site on Glenamuck Road in Q4 2020, which sold for in the region of €20 million, while a third site of approximately 7.5 acres in the area has just gone sale agreed. Another notable sale in the quarter was M3 Gateway Lands site in County Meath, which reportedly traded at a price in excess of €10.0 million. This is an industrial site with the potential for a logistics/distribution hub or data centre.

Table 1: Q2 top 5 deals

PROPERTY	LOCATION	POTENTIAL USE	SIZE (ACRES)	PRICE	PRICE PER ACRE
Airlinks, Cherryhound Junction	Co. Dublin	Industrial	64.5	€26.0m	€403,101
Glenamuck Road, Kiltarnan	Dublin 18	Residential	11.1	€10.5m	€944,245
Off Market	Co. Meath	Residential	32.3	€10.1m	€312,597
Jamestown, Ratoath	Co. Meath	Residential	14.9	€10.0m	€671,141
M3 Gateway Lands, Clonee	Co. Meath	Industrial	22.2	€10.0m*	€450,857

*Traded in excess of this

Looking ahead, we expect to see several large deals transact in the latter half of the year which will boost turnover volumes significantly. The market for commercially zoned land remains strong with our agents reporting strong levels of interest in the former City Arts site at 1-6 City Quay, Dublin 2. The site, which extends to approximately 0.55 acres, has the potential to

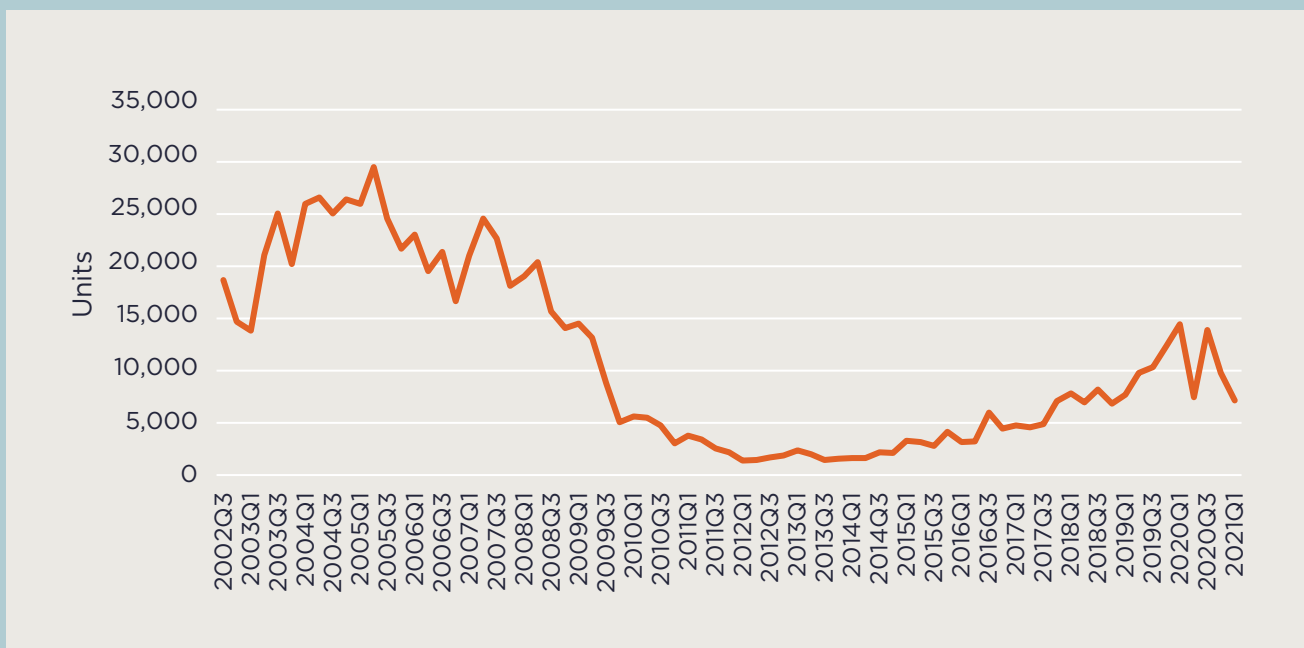
accommodate an office development of approximately 142,000 sq ft, subject to planning permission. The site was offered for sale with a guide price of €35.0 million, with several bids received well in excess of the asking price. The sale has piqued the interest of a number of new funding sources looking to enter the market, most notably from the UK and the Middle East.

Planning uncertainty: a developing concern

Sites with planning permission have risen in priority in recent times, primarily because almost one in three planning permissions under the Strategic Housing Development (SHD) process now go to judicial review, of which more than 90% are successful. It is promising that the government has recognised the inadequacy of the SHD planning application system, however, in the interim, many financiers are unwilling to take on planning risk until we have more clarity on the matter. Land with full planning permission has always traded at a premium, but in recent times we have seen this gap widen.

By analysing the number of planning permissions being granted each quarter, the impact of this development bottleneck becomes evident. In Q1 2020 planning permissions granted reached their highest point since the GFC with permission for 14,000 units granted. Although this was less than half the 29,000 units granted permission in Q2 2005, it showed a trend moving in the right direction. However, the pandemic has severely hit permissions granted with just 3,100 units granted permission in Q1 2021, in a sign that the crisis will have a detrimental impact on new supply over the medium-term.

Figure 4: Quarterly planning permissions granted



Source: CSO

An undersupply of planning permissions is not the only issue the planning system is creating, with issues also arising in the way density requirements are being applied nationwide. Currently, a density requirement of between 35 - 50 units per hectare is being sought across the country, typically closer to the upper end of the scale in urban areas. These requirements are being sought irrespective of what is contained within County Development and Local Area Plans. This density works well in Dublin, and in a small number of urban centres outside Dublin, where most unit types are viable. However, in many areas outside of Dublin - which are of less interest to investors - the need for a significant volume of apartments is in some cases an onerous requirement. This is significantly increasing risk and reducing viability of new development, given the limitations on what an apartment unit might trade for in these locations compared to the cost of delivery. In a lot of cases, apartments cost significantly more to build than what they could potentially sell for, thereby restricting supply in certain locations.

Higher planning restrictions inevitably lead to increases in prices by reducing supply. Evidence from the US suggests that there are two major barriers to entry into the housing market: regulatory and geographic. The study found that when these two factors were present, a 10% increase in demand led to a corresponding 6.5% increase in prices, with both factors having a roughly equal impact. Conversely, if the increase in demand was in a city with sufficient geography (i.e. land to build on) and no regulatory barriers to building then an increase of demand would see prices increase by 0.6% in response.¹

In the context of the Irish system, it is clear that this is a contributing factor to the current supply-demand imbalance we are seeing in the residential market. The abolition of the SHD system in its current form is certainly a positive development, but a more simplified and accelerated planning process must also be quickly developed to replace it. In the long-run, an overhaul of the planning system could see more land with planning permission coming to the market, which will ultimately help ease the current housing crisis.

¹The Geographic Determinants of Housing Supply (Saiz, 2010)

Outlook

The last 18 months in the property market have been characterised by uncertainty created by the Covid-19 pandemic. The speculative nature of development land means it is the most sensitive of property sectors to uncertainty, with market participants adopting a wait and see attitude which has impacted on land sale volumes. This has resulted in a subdued level of transactions in the first half of 2021, although values have remained strong for those sites that have traded. Full-year deal volumes are likely to be relatively robust with a number of significant sites already sale agreed and a substantial sales pipeline expected in Q3. With strong take-up of the vaccination programme continuing, the degree of uncertainty caused by the pandemic is waning which is once again turning attention back to underlying market dynamics.

For the residential market, predictions made at the start of the pandemic regarding decreases in prices of excess 10% have failed to materialise, with prices in fact appreciating over the period. If anything, we have seen demand-supply imbalances exacerbate during the pandemic as a lack of construction impacted new supply. Innovations introduced in the new homes market such as virtual viewings allowed this sector to continue to service demand, with the market only limited by the supply of stock for sale. The PRS market has also performed well through this period, with rents and occupancy levels holding strong, while absorption rates for new schemes were impressive. The main concerns for developers in

this sector are rising build costs, reported difficulties in sourcing suitably qualified labour as well as planning uncertainty. Given these factors, residential land that benefits from a full grant of planning will continue to achieve the strongest prices.

On the commercial market, while there will be some degree of scarring to occupational markets caused by the pandemic, the underlying tenant base for most sectors remains robust. Crucially, there has not been an overhang of space caused by rising vacancy in the office or industrial markets of the kind that would dampen developer sentiment. Considering that offices have been functionally empty for the last 18 months, the vacancy rate has remained relatively stable and we expect to see the occupational market begin to recover in the latter half of the year. Furthermore, the ESG agenda has risen even further to the fore which is translating into demand for new energy rated office stock from both occupiers and investors alike as evidenced by the strong interest in the 1-6 City Quay sale. The industrial and logistics sector has minimal levels of existing vacancy and we have seen the dual forces of Brexit and the acceleration of online shopping reshape and boost demand for development land in this sector over the last 18 months. Even retail - which remains challenged - may have pockets of development opportunity in the coming months. Overall, Ireland's economy is set to continue to recover this year and into 2022 which will drive demand for development land to accommodate this growth.



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