savills

Spotlight

What's Next for Residential Development?

May 2014

SUMMARY

As demand grows, the over 60s will play a key part in the prime regional new build market

■ **New build buyers:** Our survey of Savills applicants for prime property shows that over half of those aged over 60 said they would buy new compared with 31% of 30 to 39 year-olds. Equity rich downsizers are a key market for new properties. p.6/7

■ **Housing market recovery spreads:** Although London continues to lead the charge, with values up 13.8% over the year to February 2014, price growth is spreading as buyers take advantage of the wide price gap between the capital and the rest of the country. p.2/3

■ **Demand for new homes:** Homebuilders have been reporting increases in new home prices for the past 14 months. This largely reflects price growth in the wider market. Savills analysis shows that new build premiums, where they exist, are not uniform. The scarcity of similar property available in the second hand market is a significant contributor to the price differential. p.2/3

■ **Help to Buy:** Equity Loan scheme is supporting 30% of new build sales. The deal, which has helped 25,000 households buy or reserve a new build, is having the biggest impact in lower value markets. By comparison, London has seen very few deals. Assuming continuing take up of 2,000 deals a month, the funds could last beyond the end date of 2020. p 2/3

■ **Developers respond:** The rate of housebuilding is rising. We forecast it will increase to 167,000 new homes by 2018. This is still short of the 240,000 new homes we need and competition for land is already starting to grow. p.4/5

■ **Land sales:** Savills data shows national greenfield development land values, excluding London, increased by 7.5% in the year to March 2014. Urban land values grew by 6.4% over the same period. p.4/5

"We forecast housebuilding will increase to 167,000 new homes by 2018" Savills Research

Market recovery

HOUSING MARKET RECOVERY SPREADS

While demand for new homes is rising across the UK, downsizers are emerging as an important market for developers

Confidence has returned to property markets beyond London, supported by the economic recovery and government measures to stimulate demand and instigate further housebuilding.

Property prices in England and Wales grew by 5.3% in the year to February 2014 according to the Land Registry. Although London continues to lead the charge, with values up 13.8% over the same period, price growth is spreading as buyers take advantage of the wide price gap between the capital and the rest of the country.

The flow of wealth has contributed to strong price rises in Windsor and Maidenhead (6.4%), Reading (6%) and Surrey (6.2%). Beyond London's commuter belt, the southern cities such as Brighton and Hove (5.9%), Bath and NE Somerset (4.4%) and City of Bristol (6.5%) have outperformed their rural counterparts since the credit crunch, as buyers seek higher end homes in more urban locations.

Even stronger growth was recorded in Oldham, greater Manchester, where prices grew by 8.8%. However, this comes from a low base as values still remain -24.9% below their 2007 peak despite recent growth.

Overall average values across England & Wales remain 7.1% lower (Feb 14) than they were at 2007-08 peak values. London, where average prices now stand 17.1% higher than the previous peak, is still the only region that has recovered all of its earlier falls, although the South East is now catching up.

New Home Premiums

The ongoing undersupply of homes for sale in stronger markets, particularly in the south, is contributing to price increases and boosting demand for new build properties. Sales of new homes now account for one in ten transactions but values can differ significantly from second hand stock.

Homebuilders have been reporting increases in new home prices for the past 14 months, according to a survey by Home Builders Federation (HBF). This growth reflects price rises in the wider market as well as the effect of the Help to Buy equity loan scheme. It also explains why the industry is cutting back on the use of sales incentives.

Our analysis of Savills own sales records shows new build price premiums, where they exist, are by no means uniform. There are many factors driving these numbers, not least the building specification of the new homes being sold compared with the existing stock in the area.

In general, our figures suggest that niche developments in strong markets can achieve premiums over both the average second hand sales values at local Savills offices and the top values in the general local second hand market.

This effect is observed most clearly in the Winchester and Canford Cliffs offices, where median sales values for new build have outperformed comparable second hand stock. Research into buyer demographics reveals that a high number of older buyers links these two locations.

Downsizer demand

Developers targeting this demographic in higher value areas are set to benefit. Our survey of Savills applicants for prime regional property (see p.7) shows that the over 60s are the age group most likely to consider purchasing a new property. We've also calculated that the over 65s own nearly £1 trillion of equity in residential property. This suggests that significant demand for new build homes, particularly at the higher value end of the market, is likely to come from those looking to downsize and release equity.

TABLE 1

New homes median sale price by Savills office – £psf

London	£1,143	Northwood	£390	Southampton	£323	Cardiff	£262
Canary Wharf	£525	Bishops Stortford	£350	Dorset	£311	Edinburgh	£250
Sunningdale	£508	Locksbottom	£346	Oxford	£300	Norfolk	£218
Winchester	£459	Sevenoaks	£343	Chelmsford	£292	Ipswich	£200
Cambridge	£424	Tunbridge Wells	£331	Glasgow	£283		
Guildford	£398	Bristol	£326	Manchester	£279		

Source: Savills Research. For sales since January 2013. Figures will differ from general market new build pricing due to nature of stock.

Off-plan sales are up

A snapshot of the London market in March 2014 shows that less than 5% of available new build units were complete, but across the country a similar analysis gives a wide range of results. In strong markets such as Oxford and Bristol the levels of built stock are also very low, with less than a quarter of the available properties complete. There is a higher number of built stock outside these hotspots.

HELP TO BUY

Greatest impact in lower value markets and funds could last beyond 2020

Since its launch in 2013, Help to Buy Equity Loan, aimed at buyers of new build, has played a significant part in supporting sales of new homes. The extension of the scheme to 2020 enables housebuilders to plan ahead for growing demand.

The initial investment of £3.5 billion, which is expected to support 74,000 sales, has so far helped more than 25,000 households buy or reserve a new build home. The Government says the further £6 billion investment will help 120,000 more households purchase a new home. Funds will also be available for Wales and Scotland, although the Scottish and Welsh Governments are not obliged to use the funds for a Help to Buy Equity Loan scheme.

According to the Treasury, Help to Buy Equity Loan is supporting 30% of new build sales. The lower value property markets across England have felt the biggest impact. By comparison, London has seen very few deals.

Savills analysis shows that in Cannock Chase in Staffordshire, the scheme supported 48% of new build sales. It is followed by Derby and Gravesham (which partly includes Ebbsfleet in Kent) where 45% and 40% of new build deals respectively were down to Help to Buy 1.

Of the 14,823 completed sales to date only 977 have been in London. Nine boroughs in the capital (including Kensington & Chelsea, Westminster and Richmond) have seen no deals at all. A few London boroughs have seen high levels of new build sales as a result of the scheme, including Barking & Dagenham (37%) where prices are still 8% below their 2008 peak levels.

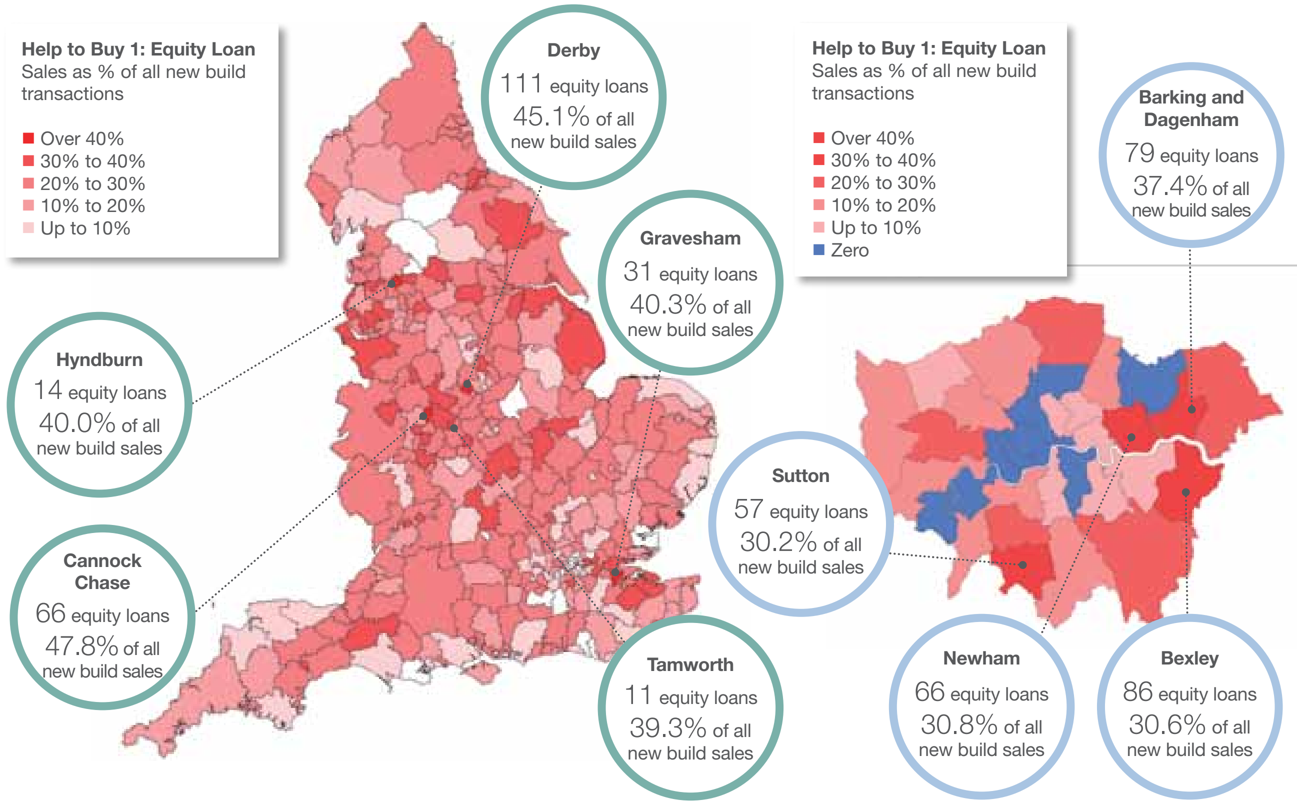
Following a surge in Help to Buy sales at the end of 2013, the rate of take up has slowed from 2,500 deals a month to 1,642 deals in February. This could be the result of a lack of available properties and demand may rise again if the rate of building increases.

Assuming continuing take up of 2,000 deals a month at the current average equity loan of £40,000, the allocated funds could last beyond the proposed end date of 2020. At 3,000 sales per month, the current size of loan the funding would last until early 2020, but at 4,000 it would be exhausted in mid-2018.

Planning an orderly end to the scheme remains crucial particularly if smaller companies become increasingly reliant on the Government support. According to the HBF, 94% of the builders taking advantage of the deal are small and medium-size businesses. Tapering is likely to be the best option.

MAP 1

Help to Buy



Source: DCLG, Land Registry (for completions up to 28th Feb 2014)

Housebuilding

DEVELOPERS RESPOND TO RISING DEMAND

Housebuilding set to increase to 167,000 new homes a year by 2018. But this is still well short of the 240,000 needed

Private sector developers are responding to rising house prices and growing demand for more homes by increasing production and buying more land. With all three main political parties focused on policies to increase the rate of house building, this trend is set to gain momentum over the medium term.

Current household projections suggest that we require 240,000 new homes a year. The Labour party has responded by voicing its intention to build at least 200,000 new homes a year and the Liberal Democrats state that 300,000 new homes a year is necessary if we are to consider the backlog of demand that has built up over the years.

While the Conservatives have shied away from the numbers game, it has been the Coalition's Government policy to encourage more housebuilding not only to provide more homes but also to stimulate the economy and create jobs.

In this pro-development climate, the players with the best access to finance and land are set to reap the greatest benefits. These tend to be the major housebuilders who can move quickly.

Their response is already reflected in data. At 174,471, the number of planning permissions granted for 2013 is the highest yearly figure since 2007 according to Glenigan. Last year's number represents a 24% climb on 2012 and a 51% increase on 2011.

Housebuilding forecast

We forecast that the private sector will increase production by 8% a year in the five years to March 2018 at best – a total increase of 35% over the period. This results in an average output from private housebuilders of 107,000 new homes a year over the next five years.

This is a best case scenario which assumes support from Help to Buy and finance easing for small and medium builders. Historically, we have seen periods of similar growth in the 1980s and noughties but there is no precedent for faster growth over a sustained period.

Together with output from housing associations and local authorities, we expect housebuilding to increase to 167,000 new homes by 2018. Whilst this is an improvement, it is still short of the 240,000 new homes we need to meet household projections according to the Town and Country Planning Association (TCPA).

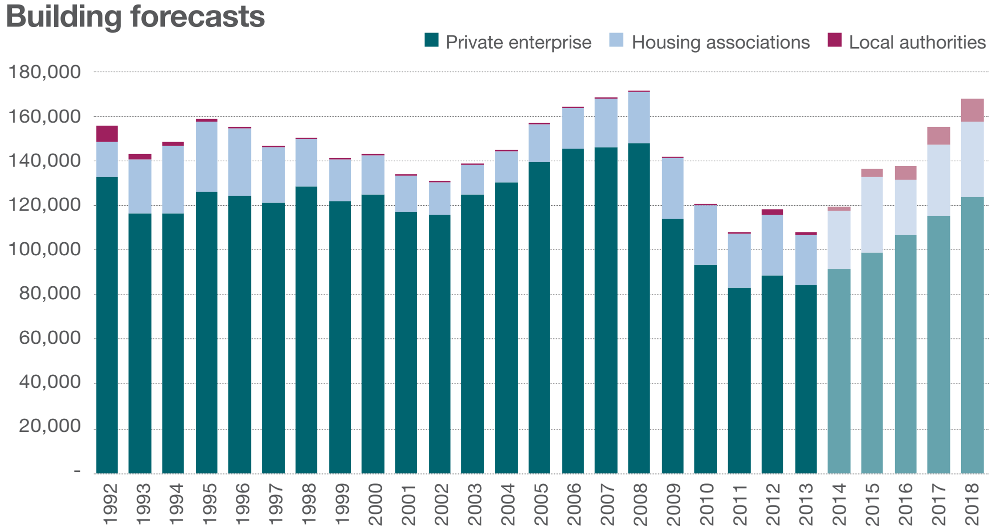
Land sales

Developers, which have succeeded in converting their strategic land holdings into planning permissions, are now seeking new sites.

Strong demand for a limited pool of sites continues to drive land price growth outside London. Savills data shows national greenfield

GRAPH 1

Building forecasts



Source: DCLG and Savills 'Best Case' Forecast

> "In this pro-development climate, the players with access to finance and land are set to reap the greatest benefits"
> Savills Research

development land values, excluding London, increased by 7.5% in the year to March 2014. Urban land values grew by 6.4% over the same period.

In the more buoyant markets of southern England, land prices have returned to peak 2007 values.

Builders Finance Fund

As part of a package of Government measures in the recent Budget to stimulate housebuilding, George Osborne announced a £525 million Builders Finance Fund introduced to help small and medium sized developers access finance to unlock 15,000 stalled homes. The fund is intended to support the delivery of housing schemes of between 15 and 250 units.

Small and medium builders were particularly hard hit by the economic downturn as many struggled to access finance. NHBC figures show that in 2006 companies producing under 100 units year accounted for 26% of all private building. Last year that figure was down to 14%.

Constraints remain

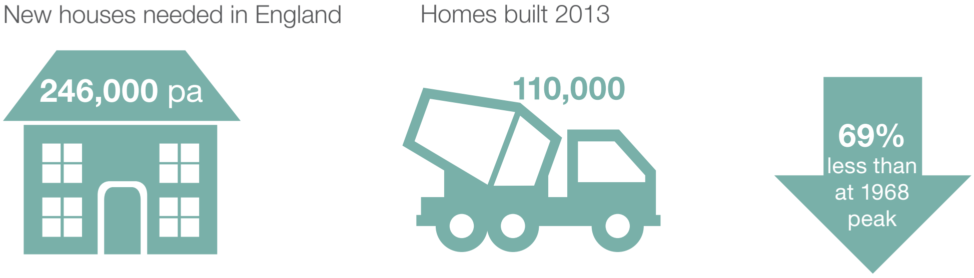
One major barrier is that the deposits they require are much greater than they used to be. Historically, builders could borrow up to 80/85% of the development cost, but since the downturn the amount banks will advance has generally dropped to 60/65%.

More and more developers are seeking alternative sources of finance. Smaller players in particular are increasingly relying on mezzanine funding, despite the higher costs of borrowing. However, bigger players still dominate the market. Last year companies delivering more than 500 units a year accounted for 73% of private building.

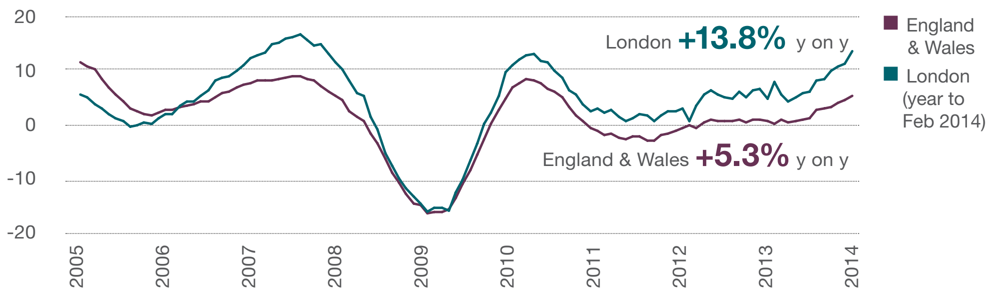
Access to sites is another issue for smaller companies. Analysis of land ownership using Glenigans data shows that the number of units controlled by smaller players stays more or less constant throughout the planning process. However, bigger housebuilders acquire more units further up the planning process. The top five housebuilders (Barratt, Persimmon, Bellway, Taylor Wimpey and Berkeley) control 10% of units at the 'outline plans submitted' stage. However, they control 23% of units at 'full permission'.

MARKET MATRIX

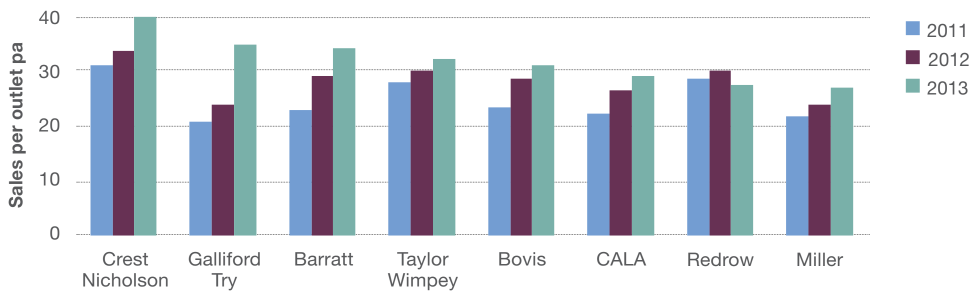
Housing need exceeds supply



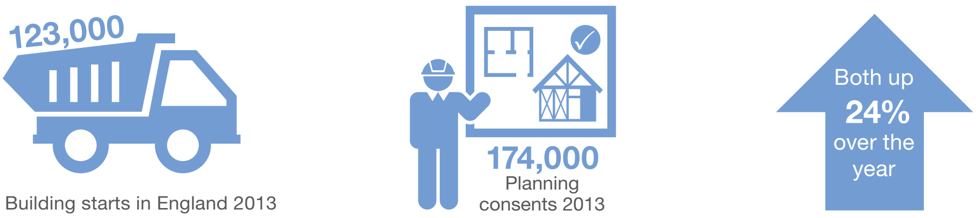
This mismatch is pushing up property prices…



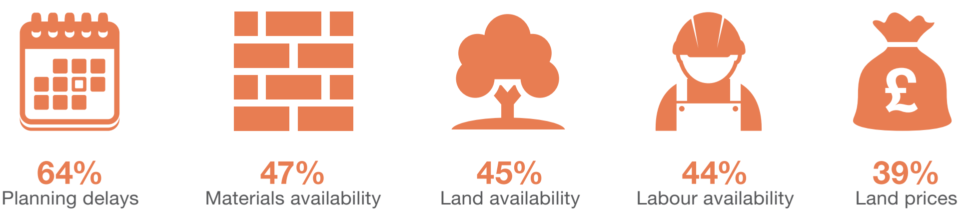
…and increasing rates of sale among major housebuilders



Rising demand is stimulating more housebuilding…



…but barriers still exist (HBF survey of factors considered a major constraint)



Sources: Savills Research, DCLG, Land Registry, Housebuilder annual reports, HBF Housing Market Report

Transactions

BUYERS RETURN TO THE MARKET

Cash purchasers continue to dominate the market. But home movers are due a comeback as house prices pick up

Buyers, who sat on their hands during the economic downturn, made a return to the property market over the past year. Growing consumer confidence in the property market is reflected in figures from HMRC which show that the number of transactions rose by 24% in the year to February 2014.

The growth was mostly driven by a sharp increase in the number of cash purchasers and first-time buyers. Although cash buyers continue to dominate the market, improved credit conditions has supported the return of first-time buyers. The latest figures from the Council of Mortgage Lenders also show that mortgage approvals to home movers have started to pick up again, having remained largely static over the last couple of years.

Purchases by existing homeowners remain well below where they were at the height of the market and account for one in three sales. This compares with almost half of all transactions between 2002 and 2007, when many took advantage of rapidly rising prices to trade up the property ladder.

With fewer people trading up, the supply of homes coming onto the market has been subdued. This restriction on the number of homes for sale is one of the main factors contributing to house price rises. It also underpins the appetite for new build.

Past falls in house prices mean that many second and third steppers have not built up enough equity to pay for a deposit on their next home. This is likely to change as price growth picks up, prompting more homeowners to sell and trade up the property ladder. Greater movement in the market should support demand for new homes at all levels, not just from first time buyers and downsizers. Some locations, such as Bristol, have seen greater interest from investors.

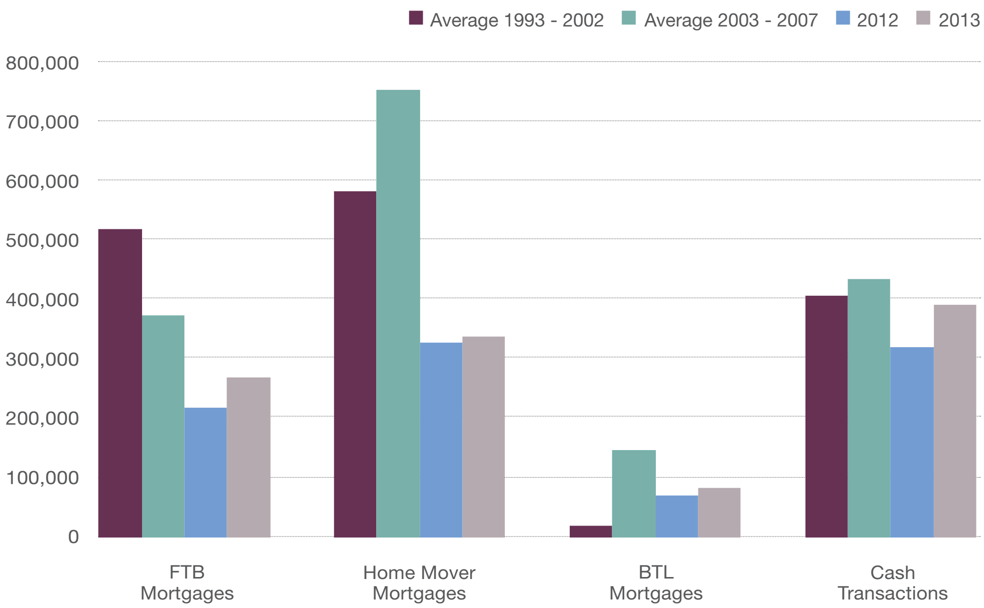
However, transactions levels are unlikely to continue the steep trajectory we have seen over the past 12 months, as mortgage reforms limit accessibility to debt.

Following the Mortgage Market Review, which came into play in April 2014, borrowers are likely to face bigger hurdles as lenders tighten credit scoring criteria and cut the share of applications approved. Future interest rate rises are also likely to dampen demand especially from those whose affordability is already stretched.

We forecast that transactions are set to rise to 1.35m by the end of 2018. While this figure represents a 85% increase since 2009, when the number of transactions hit their lowest point since the downturn, it remains 14% below the long-term average of 1.6m.

GRAPH 2

The rise of the cash buyer



Source: HMRC, CML, Savills Research

Undersupply continues

Despite growing demand, Local Authorities in southern England are not planning to deliver enough homes according to Savills Research. The findings published in *Planning: Countdown to the Election*, reveal that there will be a shortfall of more than 160,000 homes across London, East of England, South East and South West regions over the next five years.

The research, which focuses on southern England and compared the latest locally planned targets with the needs projections from the TCPA, shows that the greatest shortfall will be in London.

Southern regions excluding London will be short of 91,323 homes over the period. The home counties, particularly London's commuter belt will experience added pressure as home movers spill out of London in search of housing.

WHAT NEW BUILD BUYERS WANT

Savills survey shows older downsizers are key

GRAPH 3

Reasons for buying a new build home

Source: Savills Research

Among Savills new build buyer client base, there is a fairly even split between those in their 30s, 40s and 50s which make up the bulk of buyers. The over 60s account for 17% of our buyers and under 30s, 12%. Most (71%) are looking to buy their main residence. However, 21% are buying for investment and 8% as a second home. Across the country the split of sales between flats and houses is 70-30, but certain locations are hotspots for new build houses – Northwood, Summertown, Winchester, Norwich and Sevenoaks.

The over 60s are playing an important part in the regional new build market according to our survey of 426 Savills applicants for prime property outside London. Although 44% of those questioned said they were willing to buy new build, new homes were more popular with older rather than younger generations. Over half of those aged over 60 said they would buy new compared with 31% of 30 to 39 year-olds.

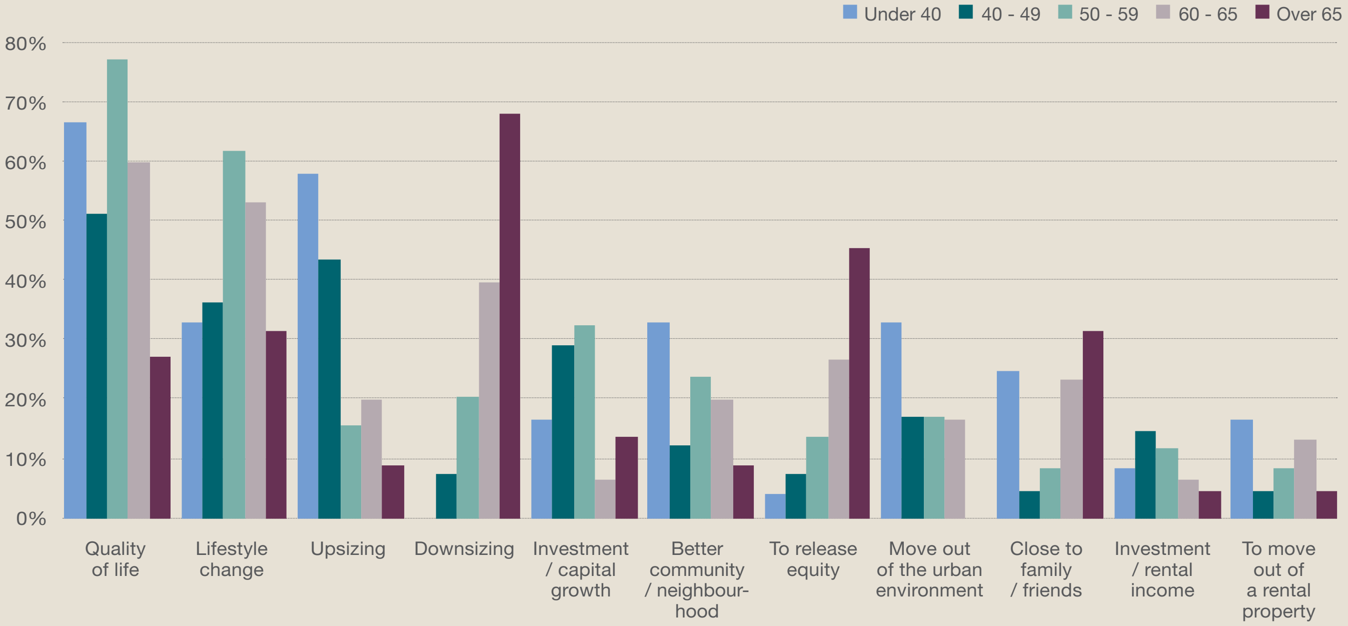
Suburbs topped the list of locations favoured by buyers of new build. Beyond that, there was a considerable difference among the age groups in terms of features sought.

Security was also deemed more important by older buyers, with over half of 60 to 65 year olds judging it a key attribute. One surprising result was that new technology was more of a selling point to older buyers, with 29% of over 60s noting it as a key feature against 15% of under 60s.

The top two specific reasons buyers gave for wanting to downsize were "easier to manage" and "lower maintenance costs". Upsizers were most keen to get more outside space (71%) and ground floor space (57%), with only 31% looking to move to a larger property due to a growing family.

GRAPH 4

Reasons for buying



Source: Savills Prime Regional Survey 2014 (only buyers who would consider a new build property)

OUTLOOK

Demand for new build will continue to grow as more buyers come to the market

■ As the housing market strengthens, we expect to see price growth ripple out of London as buyers move out of the capital in search of better value for money. This flow of wealth will result in stronger growth in Southern England, where regional price rises will outperform London over the next five years.

■ The number of transactions rose by 24% in the year to February 2014. We expect to see greater levels of transactions over the next five years reaching 1.35 million by the end of 2018. While we do not expect the number of transactions to reach the long-term average of 1.6 million in the short-term, greater movement in the housing market will support demand for new homes.

■ Cash purchasers, often older downsizers, will continue to play a lead role in the property market. But the number of home movers, which has remained subdued over the last couple of years, is set to pick up. First-time buyers, who made a return to the market over the last 12 months, will continue to grow in numbers.

■ The extension of Help to Buy Equity Loan scheme to 2020 will continue to support the sale of new build, particularly in lower value markets where the initiative has had the greatest impact so far. The appeal of buying new build through the scheme could increase should credit conditions tighten as a result of the Mortgage Market Review.

■ Following strong demand for the Government backed equity loan towards the end of last year, the rate of take up has slowed slightly. Assuming continuing rate of 2,000 HTB1 sales per month, and the current average equity loan of £40,000, the funds allocated following the recent extension of the scheme are sufficient for it to last beyond the end date of 2020.

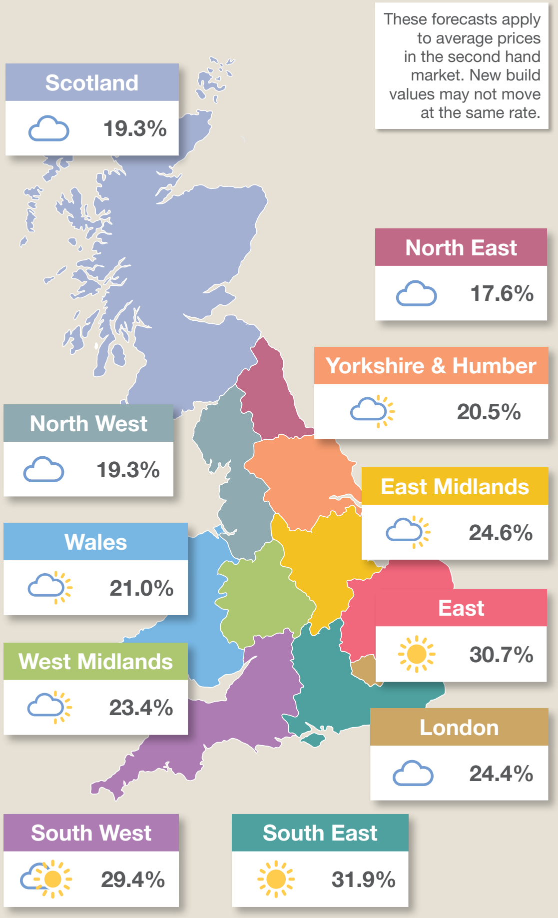
■ While the extension of Help to Buy has given the opportunity to plan ahead, the Government still needs to address how the scheme will end. Tapering remains the best option.

■ The undersupply of new homes is set to remain in the foreseeable future despite an increase in building. Our best case scenario forecast for building rates falls short of the 240,000 homes needed.

■ The burden of meeting the country's growing housing requirements needs to spread among a greater variety of players, including small and medium size builders. Improving access to both funding and land for smaller companies is a vital step forward.

MAP 2

Mainstream residential five year forecasts, 2014-18



Source: Savills Research

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