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Market in Minutes
UK Residential Development Land

April 2012

SUMMARY

Recapitalised housebuilders fuel transactional activity in high value, high turnover markets

■ Recapitalised housebuilders are fuelling transactional activity, leading to some value growth, particularly in the South East and other high value, high turnover locations.

■ In central London, land values stand on average just -7% below their 2007 peak, having increased by 3.9% over the last six months.

■ Average residential land values in the capital are now double that of land for hotel or office use.

■ National Planning Policy Framework guidance may go some way to improve the supply of land in local authorities that have historically under-delivered on new housing.

■ In the short-to-medium term, smaller land opportunities, fundable from housebuilders' own balance sheets will dominate activity.

■ We forecast serviced land values will return to their former peak levels by 2016.

■ A separate market has emerged for larger sites or 'bulk land' – we expect value for this type of site to remain flat for at least the next five years.

"In central London, land values stand on average just -7% below their 2007 peak"

Yolande Barnes, Savills Research

Re-capitalised housebuilders are fuelling transactional activity and driving up values in buoyant markets. Nationally, greenfield values recorded growth of 1.1% in the first quarter of 2012.

Focus on the South East has seen greenfield values here grow by 1.6% over the same period, the biggest quarterly rise in the region since September 2010. This comes as housebuilders focus on delivering houses, rather than flats, in the region, which accounted for 63% of completions in 2010/11, up from 46% in 2007/08.

Interest in urban land remains restricted to manageable opportunities in the best towns, while larger urban sites, particularly those in secondary locations, are not trading. At the national level, urban land values increased by just 0.3% in the first quarter of this year.

The funding environment

The level of lending to companies active in real estate development and investment remains suppressed. The forthcoming Basel III banking regulations could further constrict this source of debt funding. There are banks willing to lend, and new players are emerging, but they are selective in their activity and terms are tight.

In the short to medium term, smaller land opportunities, fundable from housebuilders' own balance sheets will therefore continue to dominate. Our outlook for serviced land is positive. We anticipate serviced land values to return to their former highs by 2016 (See Graph 1).

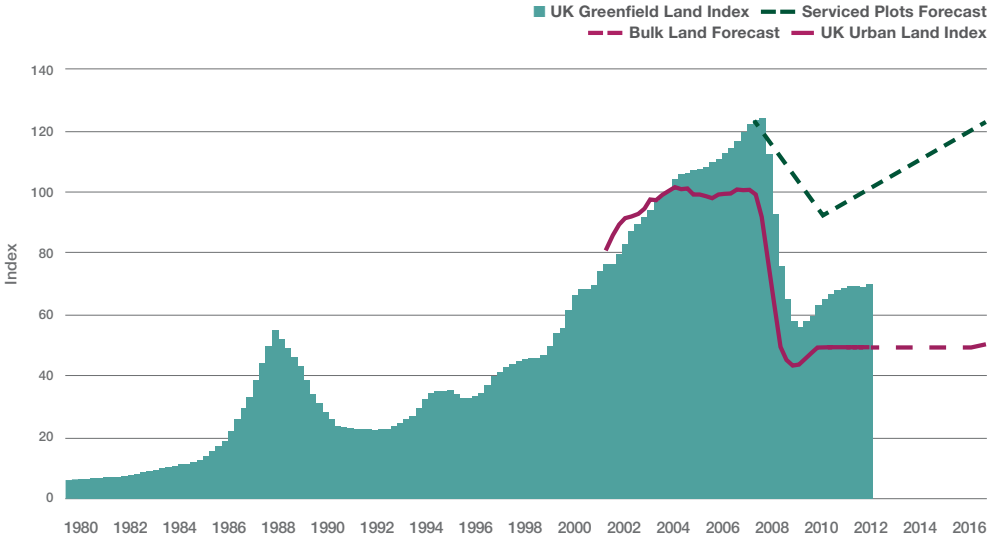
Many large scale sites in weaker markets remain unviable, requiring significant upfront investment to stimulate development. Some of these markets may be aided by the Get Britain Building fund, which is making £570million available to unlock 15,500 homes for delivery by December 2014. The fund is focused on short term land with planning permission, deliverable by 2014.

While this will help in bringing some mothballed sites back into active use, it does not address the issue of viability on many pre-consented, medium to long term sites. The reality is that for the short to medium term, the majority of 'bulk land' around the country will not stack up as a development opportunity. As a consequence, we forecast that bulk land values will remain flat over the next five years.

Nonetheless, some larger urban sites – in strong markets – are starting to move 'above water' in rare cases where equity investment is being made available. We are seeing early examples of this via investor joint ventures with landowners. In many cases the built stock, or a portion of it, will be held for investment return, rather than sold to owner occupiers. In this way the value and viability of land can be realised over a longer time period.

GRAPH 1

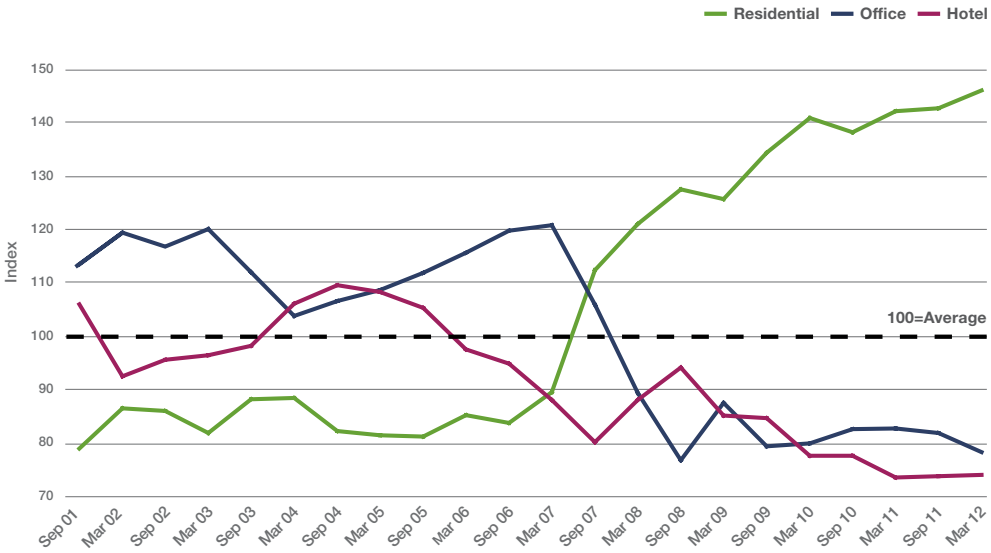
National development land forecasts



Graph source: Savills Research

GRAPH 2

Relative London land value by use



Graph source: Savills Research

Land in London

The London residential land market continues to outperform that of the rest of the UK. London residential land values grew by 3.9% over the last six months, bringing annual growth to 7.8%. This compares to land value growth outside London of 0.5% in the six months to March 2012, and annual growth of 1.6%.

Residential land values in the capital now stand, on average, just -7%

off their 2007 peak. Confidence in the London residential market remains high, as property prices in the capital continues to outperform the national average.

By contrast, a slowdown in occupier demand for office space, particularly in more peripheral London locations, is cooling speculative development of new office stock. As a consequence, office development land values saw small falls of -2.9% over the last six months, the first falls recorded since 2009.

Values remain -49% off former highs. This is making the office to residential conversion proposition even more compelling in many locations.

Hotel development land values are also muted, recording increases of 1.8% in the last six months, they stand -34% off peak. Investment in the hotel sector slowed in the final quarter of 2011, and while anticipation of the Olympics has been keeping the market moving, activity is now beginning to wane.

This has resulted in a divergence in the relative value of residential, office and hotel land since 2007 (see Graph 2 for detail).

The value of land for residential use in London is now, on average, almost double that of either hotel or office use. This chimes with NPPF guidance supporting conversion of commercial sites into residential, where housing need can be identified.

It remains to be seen which local authorities will try to retain 'employment generating land use' and which will be more amenable to conversion.

Definitions
Bulk Land: Raw tracts of agricultural land, or large strategic brownfield regeneration sites
Serviceable Land: Land serviced to the periphery, readily developable without major remediation work, but at some scale
Serviced Plots: Fully serviced land parcels, masterplanned, design coded, requiring only the dwelling to be built

OUTLOOK

The market in 2012 and beyond

■ The strength of the market today has much to do with developers' balance sheets. Those who are well capitalised are taking the opportunity to buy land at a time when the debt-laden are less able to do so.

■ We do not anticipate any significant price growth in bulk land over the short to medium term. We do foresee an unprecedented opportunity for new investors or 'land developers' to promote land to a fully serviced plots and enjoy significant value uplift. Given our positive outlook for serviced land, the opportunity lies in the transformation of bulk land into the kind of serviced product for which the market does have an appetite and ability to pay.

■ This will only work in markets that have the strength to absorb new supply. Already, there has been a shift in towards the stronger and more active markets. These markets accounted for 42% of delivery in 2010/11, compared with 36% in the three years to 2007/08.

■ Under the NPPF, local authorities with a good track record at allocating land for housing must earmark a five-year supply plus 5%. In local authorities where there has been a persistent under-delivery of housing, a five-year supply plus 20% must be earmarked. This, coupled with the general presumption in favour of sustainable development, may go some way to improving the supply of land in historically under-delivering markets.

■ Confidence in London's housing market continues to see housebuilders focus development activity in the capital. Just 17,640 dwellings were completed in 2011. This is 56% of the Mayor's target to deliver 32,250 homes per year until 2021. It is this underlying scarcity, coupled with the strength of the London market, that will underpin demand for land across London in the short and long term.

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