

# Spotlight

## Residential Development

### Who will build the homes we need? 2015



## SUMMARY

Housebuilders need more planning consents in areas of high demand to address shortage

We are facing an annual shortfall of 136,000 new homes across Great Britain, 100,000 of which is in England. Our analysis suggests we can reduce this gap substantially if we deliver:

■ **More planning consents in high demand areas.** Our analysis shows the rate of new planning consents is not keeping up with the rate of housebuilding in the strongest markets in and around London and in the strongest employment markets around the country. In many parts of the South East and the east of England, the number of planning consents are falling well below objectively assessed need. p.2/3

■ **Continued support for housebuilders to increase market capacity.** We estimate the private

sector has the potential to deliver 150,000 new homes starts a year in England in 2020. Our projection is based on larger housebuilders pursuing controlled growth averaging 6% per annum during the next five years, similar growth among refinanced medium-sized builders and steady output from smaller housebuilders bolstered by the custom build and self-build sectors. This level of growth also requires continuation of demand side support such as Help to Buy beyond 2020 to prevent starts tailing off at around 2018 and a higher number of planning consents in strong markets where sales rates can increase. p.4/5

■ **Additional building from housing associations, local authorities and large scale build to rent operators.**

We are also projecting the potential for 55,000 more starts in England from housing associations, local authorities and large scale build to rent operators. The scale of this additional building is conditional on increased construction capacity (more skilled labour and materials) and more land with planning consent in the right places. p.6/7

■ **Increased supply of land to prevent steep rise in land values.** The additional potential demand for land that we are projecting will inevitably lead to higher land values, a squeeze on margins and a choking off of volume growth, unless there is a significant increase in the volume of land that is made available for development in the right places. p.7

# Planning

## MORE LAND IN THE RIGHT PLACES

To ensure continued housing delivery, we need more planning consents where need is highest and where it is possible to sell homes most quickly

Words: Emily Williams

### The link between housebuilding starts and residential market transactions

Our analysis of private housebuilding and wider market transactions in England shows that the private sector has built to market capacity in a relationship of one new home for every 10 sales across the whole market over much of the last 25 years.

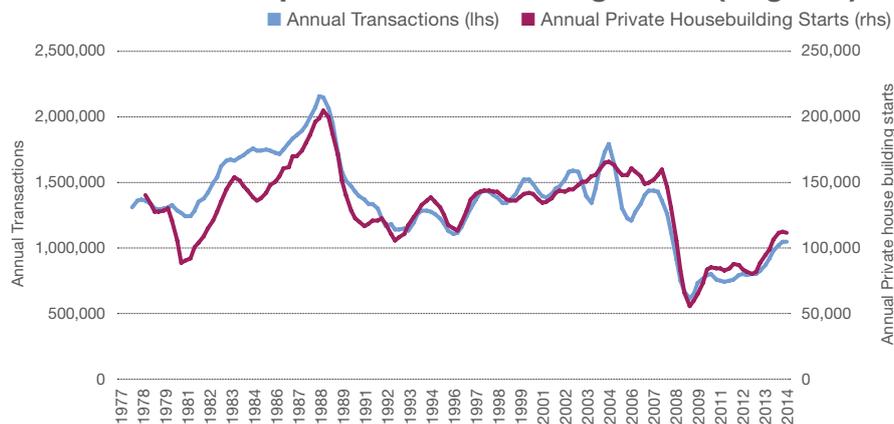
While the ratio is currently 1:9, demand side interventions such as Help to Buy have failed to alter this ratio substantially. If this ratio persists, private housebuilders are unlikely to deliver more than 121,000 homes in 2020.

However, if this were to shift to a relationship of one new home for every seven sales, then private sector starts could reach 150,000

in 2020. This ratio was last reached in the first quarter of 2006, but was not sustained. To permanently alter the ratio, we need a higher number of planning consents to be granted consistently in areas of high housing demand, where it is possible to sell homes most quickly.

This still leaves a shortage of 90,000 homes against the 240,000 number we need per year. It is therefore clear we need to encourage a broader range of developers with different business models including local authorities and housing associations, to deliver a wider variety of tenures including building homes for market rent (see p.6/7).

GRAPH 1 **Transactions and private housebuilding starts (England)**



Source: HMRC, DCLG, Savills Research

Over the year to March 2015, 156,000 new homes were started in Great Britain, of which 140,500 were in England. This is the highest number of new starts since the downturn in 2008 but it is still just over half of what we should be building. To meet housing need, we must deliver between 240,000 and 245,000 new homes in England per annum, 35,000 in Scotland and 14,000 in Wales.

The current levels of housebuilding therefore leave us with an annual shortfall of 136,000 homes across Great Britain, including a shortage of 100,000 homes in England. Unless further steps are taken to boost capacity, accumulated shortfall will rise to around one million over the course of the next decade.

However, our analysis shows that there is potential to deliver 205,000 new homes a year in England alone provided key barriers are eliminated. One of the major constraints is the restricted availability of development land, particularly in areas of high housing need.

While the number of planning consents is up, with permissions for 200,000 homes granted in England last year, this number not only still falls short of need but also is not necessarily located in the right places.

### Building starts

We have seen an increase in new homes starts over the last two years, from 97,000 in England in 2012 to 140,500 in the year to March 2015. However, this progress could come to a halt if housebuilders are not able to replenish their pipeline of consented land, particularly in the high demand markets of Surrey, Hampshire and Berkshire, and in the East of England, including Cambridgeshire and Suffolk.

By measuring the 3-year average of consented residential units against the 3-year average of housing starts for each local authority, we can assess whether there is enough land coming forward for residential development, and highlight pressure points where there are insufficient sites to maintain the current state of building.

These pressure points include: Babergh, South Bucks and Worthing, where the 3-year average of new homes starts is almost five times higher than the 3-year average of units consented. In Merton, the rate of new build starts outstrips consents by 4:1, and in Elmbridge and Watford by 3:1.

The problem is not confined to high value and high demand areas or places constricted by the Green Belt; both Kingston upon Hull and Newcastle have a 3-year average of new build starts that is over four times higher than the 3-year average of new consents.

### Planning consents

There is also concern that the consents that are being granted are not in the areas where there is the greatest housing need and where it is possible to build and sell the fastest.

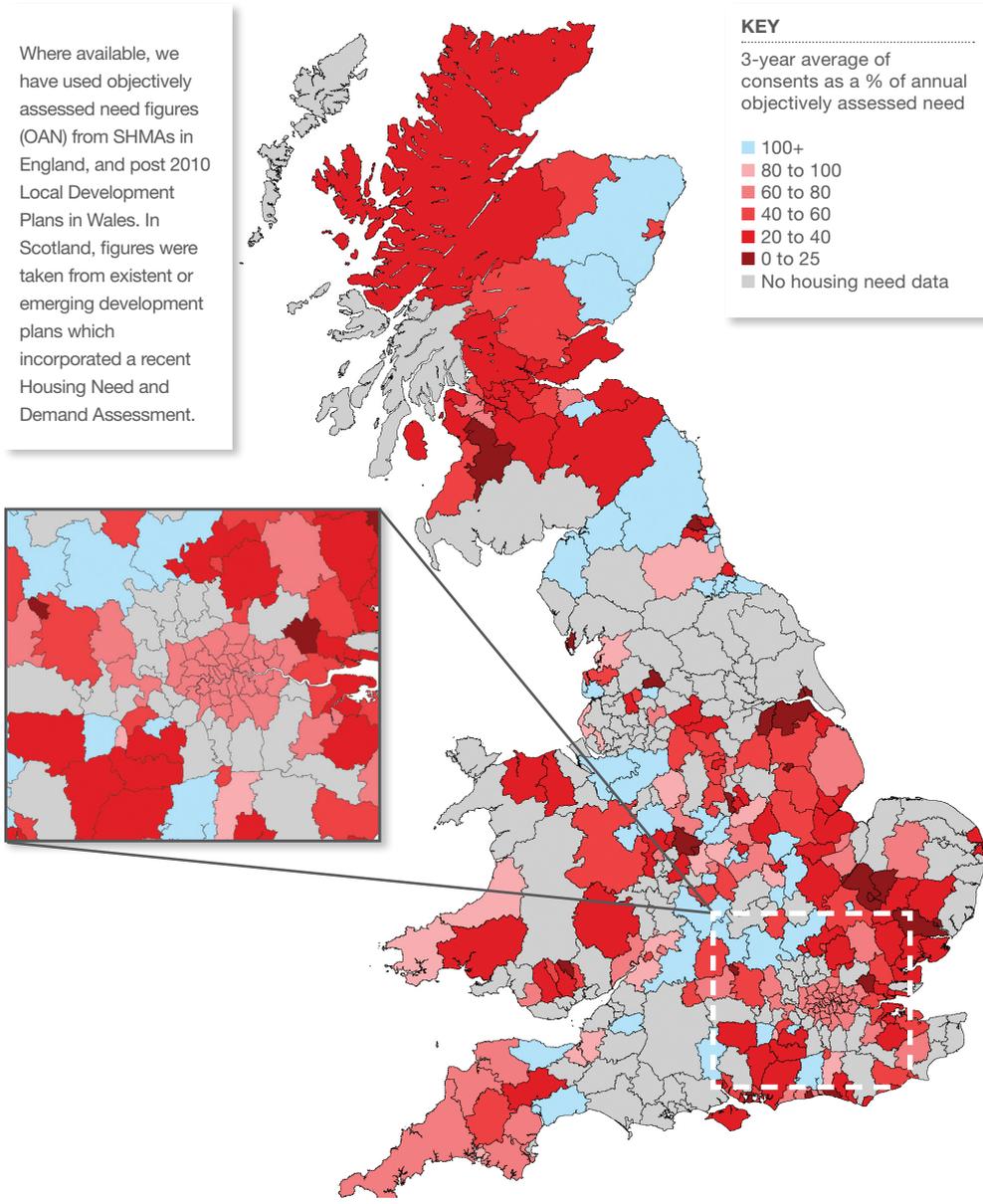
Map 1 shows the three year average of detailed consents granted in each local authority against the housing need specified in the local development plan. Areas in red are those where the number of consents granted falls below the assessed need in an adopted local plan.

The problem is particularly acute in parts of the East of England and the South East where there is high demand. In Oxford, the 3-year average of detailed consents granted between 2012 and 2014 would meet 12% of housing need, in Brighton & Hove this amounted to 16% of need, and in East Cambridgeshire, only 7%.

On the flipside, the map also highlights in blue that some areas appear to have sufficient consents. In Allerdale, Flyde and Stafford, for example, the three year average of consents outstrips the objectively assessed need by over 2:1.

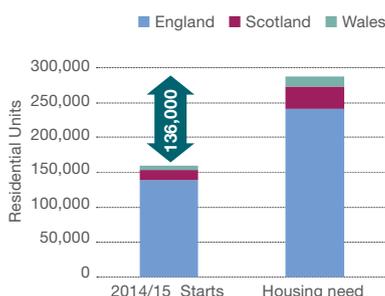
Local authorities with no recent figure for housing need are shown in grey. Analysis of those areas using household projections reveals a similar pattern of a shortage of consents in areas of high housing need, particularly in the local authorities neighbouring London.

## MAP 1 Residential consents and housing need



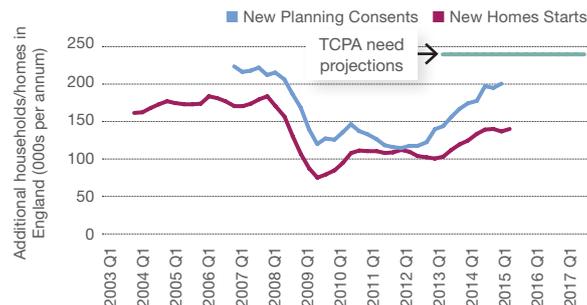
Source: Savills Research, Glenigan

### GRAPH 2 Annual housing shortfall across Great Britain



Source: DCLG, TCPA, CCHPR, Scottish Government, Welsh Assembly

### GRAPH 3 The gap between new homes starts, planning consents and housing need



Source: HBF, DCLG, TCPA

# Housebuilding

## CAN THE PRIVATE SECTOR DELIVER?

Private housebuilders can potentially start 150,000 new homes in England by 2020 if barriers to expansion are removed

Words: Lucy Greenwood

**P** private housebuilders currently build the majority of new homes in Great Britain. We estimate that the number of homes they could potentially build in England is 150,000 per year by 2020 if the barriers to volume expansion are removed.

The largest housebuilders have the capacity to increase output through measured and planned expansion. Better finance availability will support the medium-sized, often regional, housebuilders to expand. The smaller housebuilders are not expected to



54% of private starts are delivered by the 11 largest builders

recover back to their former levels but will be able to expand output via niche opportunities and through custom and self build.

### Levels of housebuilding

Private housebuilding levels (starts) have been increasing over the last six years since the downturn. Graph 4 shows the growth of the sector and the breakdown by housebuilder size estimated using the number of NHBC builder registrations. Not only are housebuilders increasing their output to meet demand, they built approximately 45% of all new affordable homes last year.

The majority of new homes (54%) are being built by the 11 largest housebuilders (those building over 2,000 homes a year) and levels of starts have recovered to 20% below their 2007 peak. One third of new homes are being built by medium-sized housebuilders (100 to 2,000 homes a year) who are back to the levels of building in 2007.

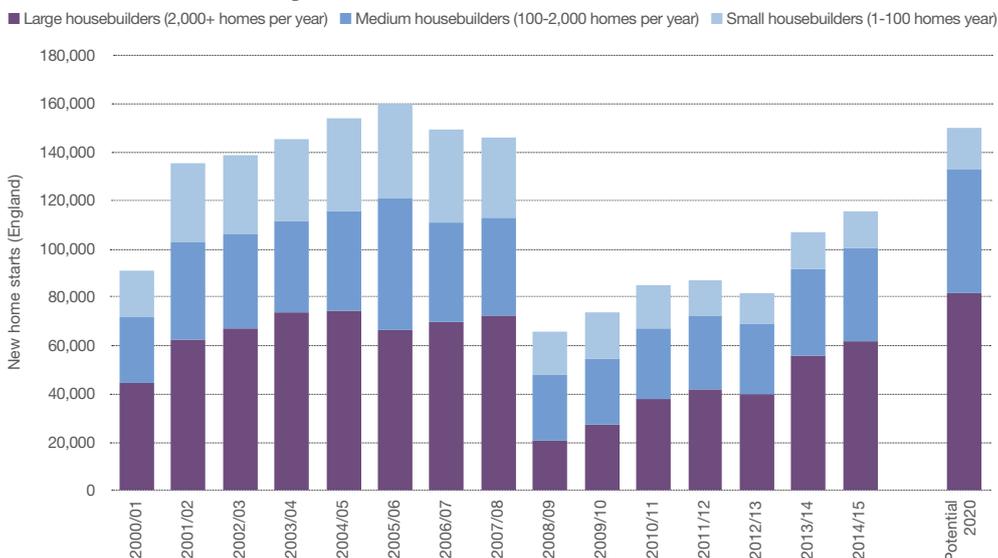
The group that has struggled the most since the downturn are smaller housebuilders. Although some have expanded to produce more than 100 homes per year to become medium-sized, others have stopped registering new homes altogether contributing to the 10% decline in registered housebuilders in 2014 vs 2013.

### Help to Buy

Help to Buy Equity Loan and NewBuy schemes supported 30,146 sales of new homes in England in the year to March 2015. Among many of the largest housebuilders an average of 32% of sales are supported by Help to Buy.

We estimate Help to Buy will support 30,000 new home sales per year and our estimate of potential delivery of homes by the private sector up to 2020 relies on its continuation. If Help to Buy comes to an end after its current funding expires in 2020, we are likely to see start volumes tapering off up to two years before the end of the scheme in anticipation.

GRAPH 4  
New home starts by size of housebuilder



Source: NHBC, DCLG and Savills



An average of 32% of sales supported by Help to Buy among the majors

### Access to funding

Access to funding is easing for SME housebuilders. Competition among lenders means that the range of choice continues to grow. According to SPF Private Clients, a financial services broker, there are currently 45 different borrowing options available to SME builders. This is in sharp contrast to the very restricted market following the downturn.

Big banks which previously preferred to focus on major housebuilders are now prepared to advance in the region of 60% of the cost of a project to smaller players. Finance for up to 75% of a project is now available from about 20 specialist development lenders while debt funds, which are prepared to advance the full cost of a project, are increasingly looking beyond the M25 and further afield.

### Current constraints

Providing returns to their shareholders is a priority for the nine listed housebuilders. Their operating margins are returning to their target of 15-20% over the cycle, having been increasing from negative levels since 2008. Typically, their strategy is to deliver controlled growth in housing numbers while maintaining or expanding their margins.

Planning delays are commonly cited as a constraint to the sector with reduced capacity of local authority planning departments owing to public spending cuts.

The cost and availability of materials have been major constraints but the problem is easing with the industry responding to the increased demand. Brick manufacturing plants have been reopened and two billion bricks are expected to be made in the UK this year.

The availability and cost of labour, particularly of bricklayers and joiners, has become a considerable constraint with workers able to command greater pay or benefits. This shortage of labour has meant that current sites have taken longer to complete.

In order to overcome the problem, apprentices and former military personnel (e.g. Persimmon's Combat to Construction initiative) are being recruited and the Home Builders Federation is attempting to encourage experienced people who left the industry during the economic downturn to return. Now that the exchange rate is increasing in their

favour, we may also see an increased flow of skilled labour from Eastern Europe returning to support the industry in the UK.

### Future delivery

Our projection that the private sector has the potential to deliver 150,000 new home starts a year in England in 2020, is based on larger house builders pursuing controlled growth averaging 6% per annum during the next five years or 33% by 2020. However, several do have plans for more significant expansion. The boldest, Bovis, is planning to double their output to build 5,000 to 6,000 homes per year.

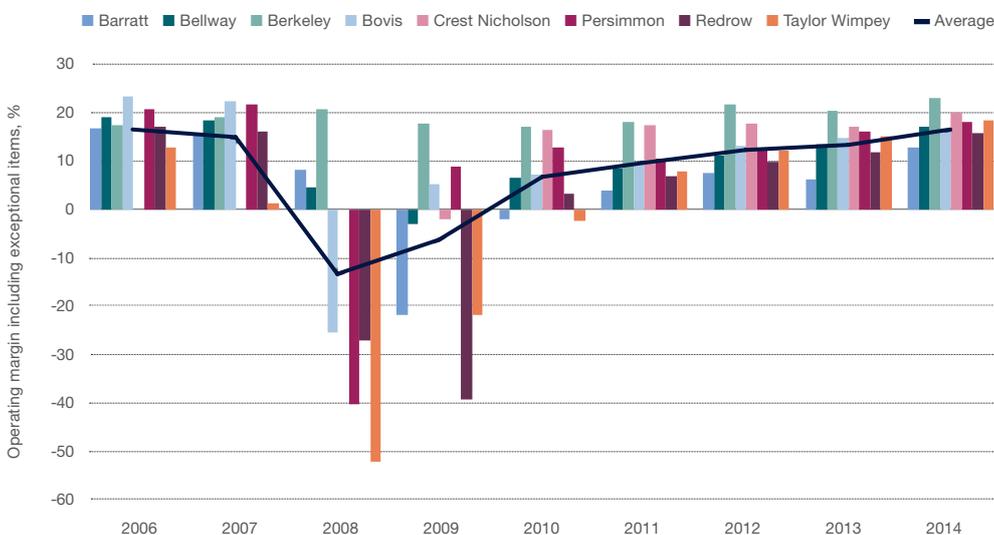
We've also taken into account the increase in the number of medium-sized builders registered. We estimate that this group, which is benefitting from better finance conditions and opportunities that are not in direct competition with the majors, has the

potential to increase the number of annual starts by 30% by 2020.

The reduced availability of labour will continue to affect the smallest housebuilders the most as they have less capacity to train new people. As a result we only expect them to increase output by 17% by 2020. However, their output will be bolstered by the custom build and self-build sector which aims to double their contribution to the number of new homes built annually, according to the National Custom and Self-Build Association (NaCSBA). ■

“Major housebuilders’ operating margins are only just returning to their target of 15-20% over the cycle”

GRAPH 5  
Operating margin



Source: Thomson Reuters

FIGURE 1  
% of builders considering factor a major constraint



Source: HBF Survey Q1 2015

# Boosting delivery

# ALTERNATIVE DEVELOPERS

While volume housebuilders will continue to deliver the bulk of new housing, other developers are set to play a larger part

Words: Susan Emmett  
Twitter: @saemmett  
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## BUILDING ON A DIFFERENT MODEL

Some larger housing associations such as L&Q and Places for People use different commercial models to develop without any government subsidy.



Brooklands, Milton Keynes by Places for People

**T**he capacity to build more homes would grow significantly if we support a wider mix of developers and organisations commissioning housing. Our analysis shows that housing associations (HAs) and local authorities have the potential to start building 45,000 new homes a year in England by 2020, with housing associations delivering 35,000 of these.

Housing delivery could be boosted further if more support is given to companies building for the rental market. We estimate that institutionally-funded PRS could add 10,000 new homes to the mix under the right conditions.

This would bring the potential number that could be started by alternative developers to 55,000 a year by 2020, an increase of 120% on the 25,000 new homes started by housing associations and local authorities in the year to March 2015.

### Housing associations

Reduced Government grants prompted many in the sector to build homes for market sale in order to cross-subsidise other forms of tenure. The model relies on a strong property market and as a result, appetite for development risk among the sector is generally more robust in and around London.

The g15 group of London's largest housing associations, are planning to build at least 93,000 new homes in the capital and the South by 2025. They expect to deliver at least 27% (25,110) over the next two years, 41% (38,130) in two to five years and the remainder thereafter.

At a national level, the National Housing Federation, which represents independent non-profit housing associations, told the Lyons Review that more than 100 HAs have the scope, scale and expertise to become major players with the potential to

match the private housebuilders in the delivery of new homes.

### Local authorities

Local authorities started building 1,830 new homes in England in the year to March 2015. Given the increased activity among Savills local authority client base, we estimate that there is the potential for local authorities to be starting 10,000 new homes a year by 2020.

However, the role of local authorities in boosting housing delivery goes well beyond their ability to build themselves. Councils play a crucial part in the planning system and have a responsibility to set targets that meet local need and to allocate sufficient land for residential development.

Councils can also contribute to greater housing delivery by taking a leadership role in land assembly and by contributing their own assets. These steps would help enable schemes that otherwise may not be viable.

### Government as developer

One of the key proposals within the National Infrastructure Plan 2014 is for the government to master-plan, directly commission, build and sell homes.

In a pilot programme, which aims to double the usual rate of delivery, the Homes and Communities Agency will commission local contractors to build 10,000 homes on a former RAF base at Northstowe, near Cambridge.

While this particular site carries its own development challenges, the new approach, if successful, could provide homes in addition to those delivered by conventional means. However, to ensure additionality, government commissioned homes must not simply replace existing plans for housing in any given market. Delivering a variety of tenures and targeting market sectors that are not being catered to by private housebuilders is key.

### Institutional PRS

We forecast that the number of households renting privately is set to rise by 1.2 million to just over 6 million by 2019, with almost one in four households renting privately. Institutionally-funded rental homes can help meet that demand.

Our recent survey of leading investment houses identified a collective ambition to invest over £30 billion in the UK private rented sector, with over 50 per cent from UK investment houses. However, despite

the demand from tenants and investor interest, a shortage of appropriate stock has prevented the sector from growing substantially.

Building to rent has the potential to expand. The Savills investment transactions database shows that a total of £3.2bn of residential portfolios traded last year. This includes 20 build to rent deals worth £500 million, the bulk of which were in London.

We estimate that institutionally-funded PRS has the potential to deliver 10,000 new homes a year by 2020 if the sector were given greater support via the planning system and

did not have to compete directly for land with developers building for the sales market.

### Role of contractors

The construction industry is set to play an expanding role in increasing the supply of housing by working in partnerships with different sectors, in a model that may offer greater insulation to market cycles. Construction firms building under contract bear less development risk and therefore can work to substantially lower margins than housebuilders expect.

There is potential for joint ventures between big names such as the Kier Group, Bouygues and Willmott Dixon and local authorities, housing associations and investors in the private rented sector. Willmott Dixon is already playing a greater role in the residential sphere through its specialist rental company be:here and PrimePlace, its sales company. ■

“Councils can contribute by taking a leadership role in land assembly”

## COMPETITION FOR LAND WILL PUSH UP LAND VALUES

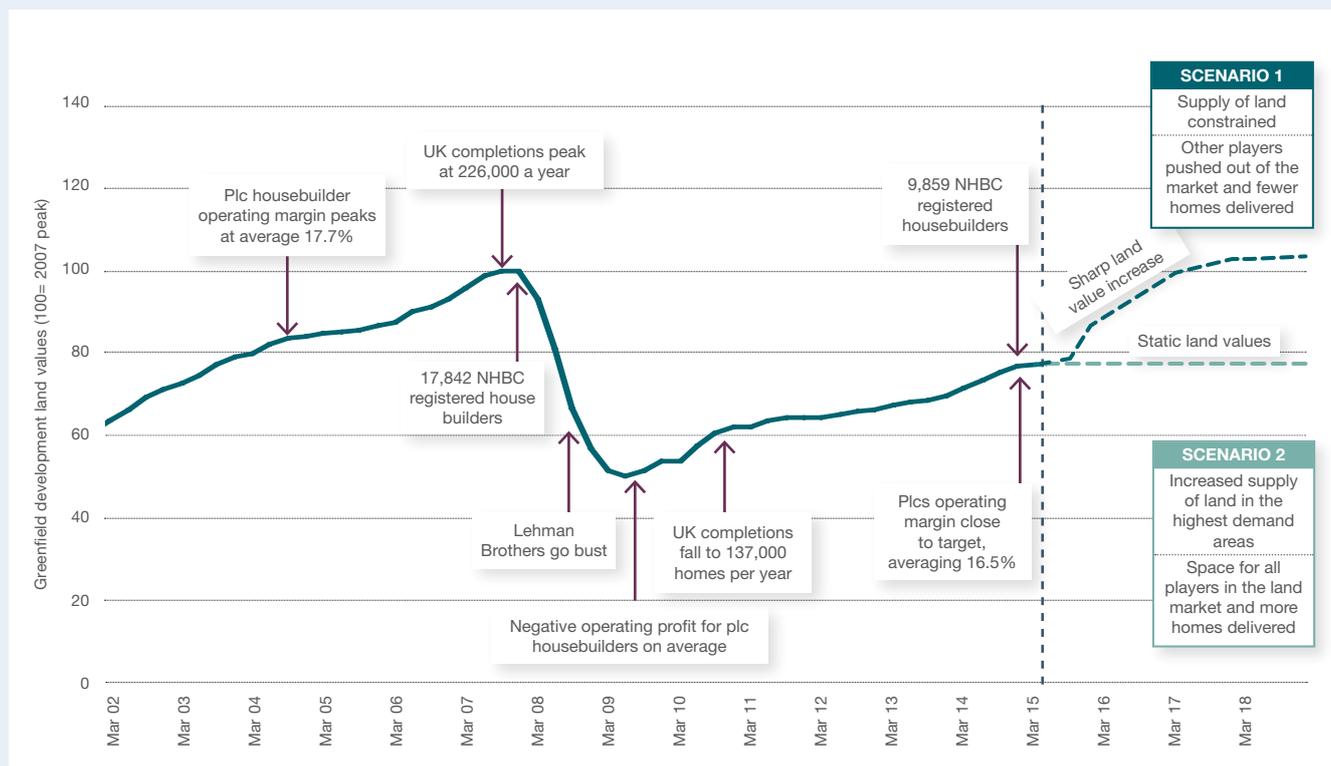
More sites for residential development are needed in markets with high demand

Demand for land is more polarised in the current cycle than in previous times, with a stronger appetite for smaller sites of 100 units compared with larger sites of several parcels on a multi-outlet site.

The more selective approach by major housebuilders, means that land value growth has slowed following a period of stronger rises. UK greenfield and urban land values increased by 0.5% and 1.6% respectively in Q1 2015.

However, the additional potential demand for land that we are projecting will inevitably lead to higher land values, a squeeze on margins and a choking off of volume growth, unless there is a significant increase in the volume of land that is made available for development in the right places. Hence more land needs to be brought forward for residential development if we are to prevent values from rising too fast and compromising the viability of new schemes. This is particularly important if we are to encourage development for a mix of tenures.

GRAPH 6 **UK greenfield development land values**



Source: NHBC, Savills, Thomson Reuters

## OUTLOOK

■ There is potential to increase the rate of building starts from the current level of 140,500 a year to 205,000 new homes a year in England. However, to achieve this, we need more planning consents to be granted in the right places and a wider range of developers participating in housing delivery.

■ We expect to see the private sector continue to deliver the lion's share of new homes with the biggest contribution coming from the 11 largest players. In total, the number of homes started by the private sector has the potential to rise to 150,000 a year in England by 2020, if planning consents can keep up with housebuilding starts in the areas of greatest demand.

■ Improved access to funding will provide medium housebuilders with greater capacity to expand their output. We estimate that this sector, which includes many regional players, has the potential to deliver

50,500 new homes a year in England by 2020.

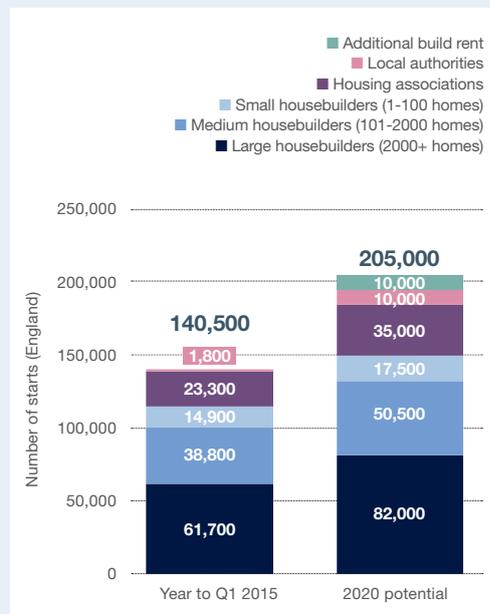
■ The smallest housebuilders, which were hit the hardest in the economic downturn, are unlikely to return to pre-recession levels of output. However, there is potential to see a greater number delivered by the custom build and self-build sector.

■ Housing associations and local authorities have the potential to start building 45,000 homes a year in England by 2020, with housing associations delivering 35,000 a year. Much of the development from housing associations is likely to be concentrated in London and the South.

■ Across Great Britain, we estimate that the private sector could start building as many as 194,000 new homes a year by 2020, based on the current levels of registrations which stand at 144,000.

GRAPH 7

### Housing starts: current and potential



Source: NHBC, DCLG and Savills

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