Residential Property Focus

The Noughties and beyond

As we enter a new decade, what lessons have we learnt?

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This publication

This document was published on February 15. It contains a review of all the key housing market indicators and news to the end of December 2009. The data used in the charts and tables is the latest available at the time of going to press. Sources are included for all the charts. We have used a standard set of notes and abbreviations throughout the document.

Glossary of terms

- **Mainstream** – mainstream property refers to the bulk of the UK housing market with, for example, price movements monitored by reference to national and regional average values.
- **Prime** – the prime market consists of the most desirable and aspirational property by reference to location, standards of accommodation, aesthetics and value. Typically it comprises properties in the top five per cent of the market by house price.

The most commonly used abbreviations are:

- Q110 – refers to the first quarter of 2010
- Q409 – refers to the fourth quarter of 2009
- H209 – refers to the second half of 2009
- PCL – prime central London
- Peak – refers to the first half of 2007

Foreword

A lesson in property market history

At the beginning of a new decade and with a general election on the horizon, **Yolande Barnes** takes stock by looking back to the patterns of the past

A week, it is said, is a long time in politics, and as the campaigning begins to take off in earnest, seven days will inevitably seem an awful lot longer in the run-up to the general election.

Elections can signal a change in property markets. Agents often observe a lack of willingness on the part of buyers and sellers to commit to deals in the face of uncertainty, and so a period of low turnover precedes the new government.

Viewed in the longer term context though, a week is but a blink of an eye for the housing market. The real trend unfolds over years or even decades. So, as we enter the second decade of the third millennium, it is natural that our attention focuses on the last cycle.

According to the Nationwide Building Society, average UK house prices rose by 117% between December 1999 and December 2009. This averages 8% per annum or 6% per annum real growth (adjusted for CPI inflation). However, the true story of the housing market unfolds over the last 20 years, and now is a particularly good time to take stock of this.

Looking back to look forward

Standing today near the bottom of the market having seen, in 2008, some of the biggest and certainly the fastest price falls since the Second World War, we can look back to 1989 when similar falls were about to happen (and over a longer time period).

The housing market slump of the early 1990s resulted in overall real price falls during that decade so that average annual growth was negative in inflation adjusted terms, at -1.2% per annum.

Taken together, the decades of the 1990s and the Noughties, produced average growth per annum of 5% or 2.5%, when adjusted for inflation. This real growth broadly reflects the longer term trend for house prices to rise in line with household disposable incomes.

The growth in house prices, in excess of general inflation, is down to the inelastic supply that has dominated the UK market for at least half a century. New homes in the UK are built at a much lower rate per household than is common for other parts of the developed world – particularly where low house-price inflation is common. Soaring home-owner aspirations, fuelled in the most part by the home improvement TV shows, magazines and show homes of the Noughties, are set against this underlying shortage.

Households sought to maximise their purchasing power and were in competition for scarce stock, especially in high-demand areas. One way they did this was to increase borrowing. Mortgages outstanding in 2009 amounted to £1.226 trillion, up 375% on the £256 billion outstanding in 1989. Meanwhile, interest rates fell from 15% in 1989 to 0.5% in 2009.

This enabled asset prices, borrowing, and consequently the house price to income ratio, to increase without damaging household cashflow. Indeed, our measure of household spending power grew considerably over this period.

Rising assets

As asset prices rose, so too did the equity used in the housing market. In 1989, total private sector housing stock (owner occupied and privately tenanted) could be valued at £1.02 trillion, 0.76 trillion of which was held as equity. By 2009, the value of the housing stock was £3.4 trillion, the un-mortgaged portion of which was up more than threefold – at £2.2 trillion.

The coincidence of low interest rates, poor stock market returns and opportunity for low cost gearing encouraged many equity-rich homeowners to become residential landlords over this period. This, combined with the increased inaccessibility of the housing market for those without the equity for a deposit, ensured that rental demand exceeded or matched supply.

It was the growth in the private rented sector by about 1.3 million homes, from 9% of the stock in 1989 to 13% in 2009 that was the biggest story of the last housing cycle.

Given the continued credit constraints likely to pertain in the coming decade, increased competition from the equity-rich for properties and relatively low returns on cash, it seems likely that stock shortages and the growth of the private rented sector is assured – regardless of which party is in power after the general election. ■

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Mainstream

The legacy of the Noughties

Over the past decade the average price of a UK house increased by 67% in real terms; a rate higher than any of the preceding four. **Yolande Barnes** looks to the next ten years

Over the course of the Noughties the average value of the UK house increased by 117%; on the face of it much less than in the 1980s (180%), or indeed the extraordinary growth of the 1970s (409%). However, because this growth occurred in a low inflation environment, a real (or inflation adjusted) growth rate of 67% stands head and shoulders above that seen in previous decades (see Graph 1.1).

2000 to 2004
Sustained sustainable growth

While for the most of us the Noughties will be remembered for the 2007/2008 downturn in values, the sustained growth in the first half of the decade was actually the real story, when the average value of a house in the UK rose by 112%. This rise in house prices was underpinned by surplus household incomes derived from a period of consistent economic growth.

At an individual household level, these surplus incomes were assisted by the ready availability of discounted mortgage deals. Rates on these mortgages, which reflected the ultra-competitive lending environment that existed for the majority of the decade, tracked the bank base rate – just 4.64% over the five years to the end of 2004, and on average 1.6% below standard variable rates.

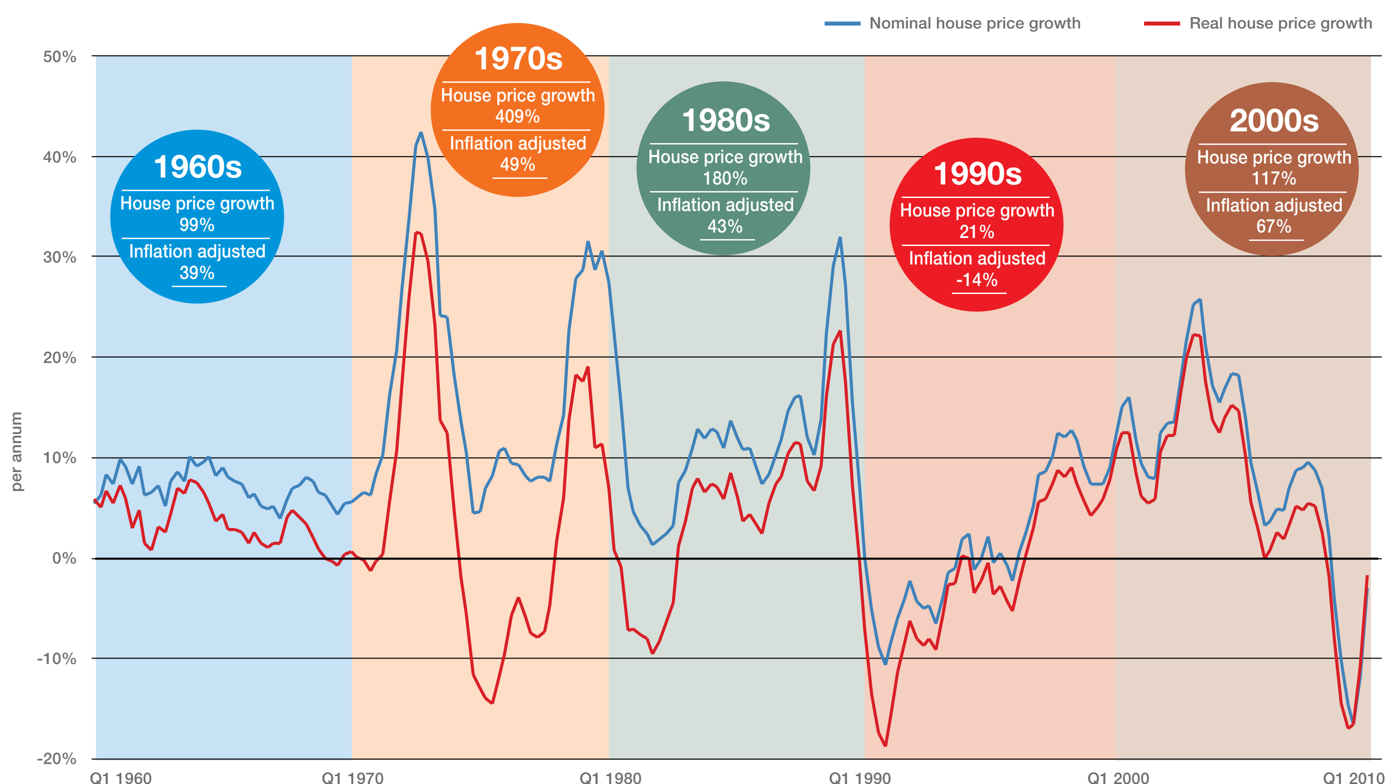
2005 to 2007
A sentiment-led second wind

The growth from 2000 to 2004 was compounded by further growth in 2006 and 2007 when, after stalling in 2005 as economic growth slowed, house prices benefited from a second wind. During these last two years of the 1997/2007 mainstream house price boom, positive sentiment remained, and was fuelled by easy access to mortgage finance. Meanwhile, the prime markets of London, which had been relatively subdued for five years, began to show record levels of growth.

2008
The price of excess

By defying rising interest rates, growth in 2005/2007 eroded the surplus household incomes of buyers. This left affordability in the mainstream market stretched and the housing market exposed to the external shock, that came in the form of the paralysis of credit availability of late 2007 and 2008.

Graph 1.1
House price growth over the past five decades



Source: Nationwide, ONS

What does this mean for the next 10 years?

1 A less accessible housing market

An important consequence of the strong growth in house prices seen prior to the downturn in the financial sector was that, even before the credit crunch, deposit levels rose significantly in relation to household incomes. During the 1980s and all but the last few years of the 1990s they had been in decline or, at worst, static.

In a credit-constrained environment the ability to raise a deposit is likely to be the most limiting factor for those trying to access the housing market, especially given the prospect of much tighter mortgage regulation.

As a result of these factors, we fully expect to see a continuing decline in owner occupation and a shift back to renting, as was the case for the first time in the post-war era during the latter part of the Noughties.

2 House price sobriety in a different credit climate

This lack of accessibility is also likely to mean more sober house price growth. This will be the case particularly in the lower price brackets of the market and in equity starved areas, where owner occupation goes hand in hand with a sizeable mortgage requirement relative to house prices.

Even if a new age of austerity falls short of a 1970s mortgage rationing, those seeking mortgage finance will have to pass more rigorous assessments of their ability to meet interest payments in the short and medium term. Also with much more attention paid with regard to repaying capital, the ability of homeowners to move up the housing ladder, in the way they would have done in the Noughties, is likely to be restricted.

In this respect, whatever the outcome of the FSA proposals for mortgage reform, it seems inevitable that we have seen the end of self-certificated mortgages. Similarly, levels of equity withdrawal amongst existing homeowners will have to be curtailed, wherever they need to protect their equity in order to work their way up the housing ladder.

3 Money makes money; market divergence

For those able to access the mortgage market, affordability is high. This means that for those markets rich in equity, which are less dependent on borrowing, price growth will be much less constrained, especially during the first part of this decade. Equally, even if last year's price growth is a temporary phenomenon that was driven by the short-term dynamics of pent-up cash rich demand chasing constrained stock, any short-term softening in values is likely to be far less pronounced in these markets.

In markets rich in equity, which are less mortgage dependent, price growth will be much less constrained

4 Back to the long-term average?

Taking all of these factors into account, once we pass the volatility expected during the next few years we should see a return to a more stable long-term average price growth. Therefore, inflation adjusted growth for this decade is likely to be in the region of 40% to 45%, a figure which is some way short of that sum in the Noughties.

Like all averages, this growth will mask quite significant variances across the different sectors of the market, which may be the biggest legacy of the Noughties. ■

The geographical dimension

Regional growth pattern reflects the ripple effect

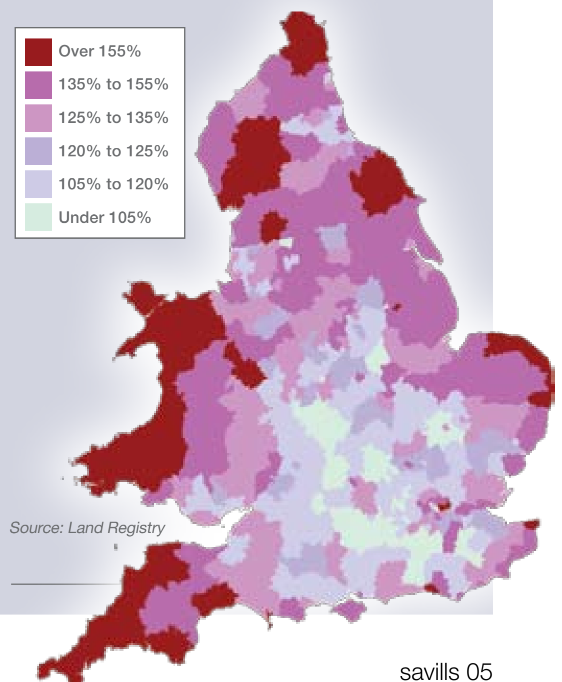
Analysis of Land Registry data for England and Wales shows that during the Noughties the highest house price growth was seen in northern England, the deep south west, west Wales and the more isolated parts of south east England.

Pembrokeshire experienced the highest growth in England and Wales at 213% followed closely by Penwith in Cornwall at 208%. At the other end of the scale, in Surrey Heath and Wokingham average house price growth grew by just 83% and 86% respectively.

This geographical pattern of house price growth reflects the ripple effect through the growth stages of the housing cycle that started in the mid to late 1990s. More locally this has been exacerbated by two factors. Firstly the radical changes in commuting patterns that were enabled by the ability to work from home for all or part of the working week. Secondly, by the dramatic price growth in second-home hotspots, which became magnets for wealth.

In contrast, we fully expect that house price growth will be much stronger in the equity-rich markets of south east and central England, as we move out of the current period of anticipated house price volatility, and into the next cycle of growth. ■

10-year house price growth by local authority



Source: Land Registry

Prime markets

A decade of highs and lows

Despite periods of exceptional growth, the Noughties saw the prime London housing market outperformed by its mainstream counterpart. **Lucian Cook** explains why

Prime central London residential values featured in many a headline during 2006 and 2007, when the average growth in house prices alone was 44%. Strong demand from billionaires drove the upper echelons of this market, while city bonuses were responsible for much of the growth elsewhere. Indeed, according to estimates from the Centre for Economic and Business Research total bonus payments exceeded £10 billion in both years.

The surge in interest during these boom years was very strong for townhouses in the south west areas of central London, particularly Chelsea, Knightsbridge and South Kensington. This resulted in a 127.7% increase in values for these properties for the decade as a whole. Yet across the whole of PCL residential market 10-year price growth was just two thirds of its mainstream counterpart.

Prime markets are more susceptible to the negative sentiment that accompanies financial and political shocks

Before the Noughties

The real headline success story for prime London property was, in fact, the 1990s. While values in the mainstream markets languished following the downturn early on in the decade, values in the prime markets of central London continued to increase substantially.

Even when the mainstream markets started their 10-year period of sustained growth, the prime markets of London continued to outperform them. As a result, while the average value of a house in the UK grew by just over 20% in the 1990s, values in the prime central London markets increased by as much as 91%.

This scenario goes some way towards explaining why prime London underperformed during the Noughties. It also reinforces the fact that it is the equity-driven prime markets that are the first to benefit from improved buyer sentiment and lead the recovery.

Time of upheaval

However, a lesson to be learnt from the first half of the Noughties is that the prime markets are much more susceptible to the negative sentiment that accompanies financial and political shocks.

A succession of seismic events, which started with the bursting of the dotcom bubble, followed by the trauma of 9/11 and then the invasion of Iraq, significantly influenced prime market performance between the period of September 2001 and December 2005.

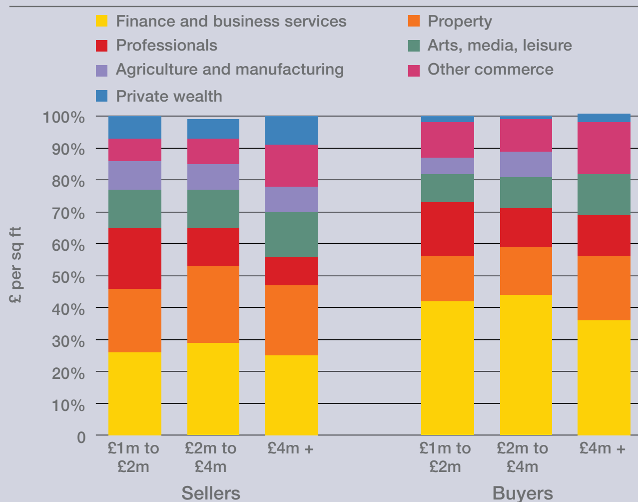
During this time of upheaval, prime central London witnessed value growth of just 8.7%, while mainstream values increased by an average of 73% according to the Nationwide index.

Perhaps given this relationship it should not have come as a surprise when the credit

Prime regional market

New decade signals capacity for growth

Graph 2.1
Sources of wealth – prime regional markets



Source: Savills

During the last decade, growth of 59% in the value of prime property outside of London was more subdued than that seen in either the UK mainstream markets or the prime London markets. While the prime regional markets were affected in a similar way as prime central London by the credit crunch and the political and financial events of the decade, it did not enjoy the same extent of growth during 2006/07. This can partly be explained by the fact that demand from international and bonus-fuelled buyers was far less intense outside of London.

However, there are signs that internationalisation is creeping into the country house market. This is particularly prevalent in the south east of England, where the giant's share of prime regional properties bought by overseas buyers are located. In the £2 million-£4 million market overseas buyers account for 15% of the market, a figure that rises to 31% for properties over £4 million.

In the country house market there is evidence that the upsizing buyers are increasingly coming from sectors more readily associated with the London prime markets. For example, in the over-£2 million bracket, 43% of buyers are from the finance and business services sector.

Against this backdrop, the relative under-performance in the last decade of the prime regional markets points to a stronger capacity for growth during this new decade. ■

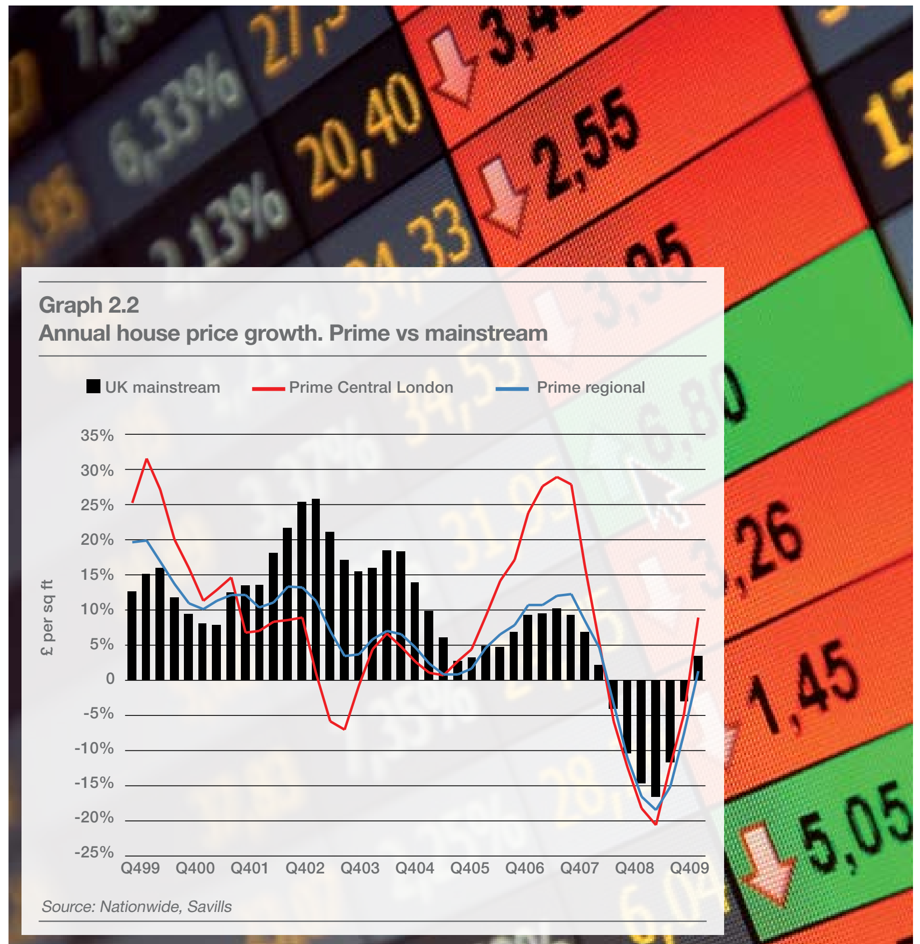
crisis affected both the mainstream and prime markets in equal measure. Albeit that the erosion of global wealth and reduced earnings in the financial and business services sector played a greater role in the prime markets than the mortgage famine that largely afflicted the mainstream markets.

Understanding the key drivers

Ultimately, the Noughties has been responsible for reinforcing our understanding of the key drivers of the prime markets; indelibly highlighting the over-riding conditions that influence the economic environment for wealth generation.

Despite of the volatility displayed during the past decade the UK firmly remains a place to generate and hold that wealth, and London has retained its credibility as a world financial centre. ■

The Noughties has been responsible for reinforcing our understanding of the key drivers of the prime markets



Graph 2.2
Annual house price growth. Prime vs mainstream

Source: Nationwide, Savills

The scale premium

Demand drives increase in £ per sq ft

Graph 2.3
£ per sq ft by property type

Source: Savills

One of the key features of the decade in the prime London markets was the demand for large-scale dwellings. The sheer scarcity of these much larger properties led to premiums being paid as and when such a property became available.

The average value of a 1,000 to 1,500 sq ft prime central London property stood at just under £1,100 per sq ft in 2009. Units between 5,000 and 10,000 sq ft averaged £1,850 per sq ft, with second-hand properties larger than 10,000 sq ft exceeding the £2,000 per sq ft barrier (Graph 2.3).

This premium for scale is linked to the increased demands from ultra-wealthy multinational buyers for larger townhouses in the most prestigious addresses. Between 1999 and 2007 the number of global billionaires grew by 277%. Many more nationalities were now part of this exclusive club, perhaps the most influential new entrant being the Russian oligarch. The corresponding rise in demand for luxury accommodation paved the way for high-profile luxury flat developments such as The Bromptons, The Knightsbridge and One Hyde Park.

The scale premium, however, has not been confined to these rarefied markets, with identifiable £ per sq ft premiums paid in the prime central London second-hand flat market, where units are rarely of this scale. Likewise, in the more domestic prime markets of south west London units over 3,500 sq ft attracted noticeable premiums in 2009 as the value placed on space defied the law of diminishing returns. ■

Forecasts

A current snapshot of the market

Mainstream markets: Regional property value forecasts

Forecasts (as at January 2010)	2009 (Actual)	2010	2011	2012	2013	2014	2015
UK	3.4%	-6.6%	2.7%	5.5%	8.0%	5.7%	5.5%
London	7.0%	-4.1%	2.1%	5.6%	7.3%	7.0%	5.8%
South East	5.9%	-3.1%	3.8%	6.7%	6.9%	6.0%	6.0%
South West	3.8%	-2.8%	3.0%	5.7%	6.6%	5.5%	5.5%
East	4.5%	-4.2%	3.3%	6.6%	9.2%	5.5%	5.5%
East Midlands	2.5%	-4.5%	2.9%	5.8%	7.7%	5.4%	5.3%
West Midlands	2.1%	-5.2%	2.5%	4.5%	7.3%	4.8%	4.8%
North East	-2..0%	-7.0%	0.0%	3.8%	6.5%	4.5%	4.5%
North West	2.7%	-6.7%	1.7%	3.6%	6.3%	4.8%	4.8%
Yorks & Humber	2.7%	-6.7%	2.0%	3.8%	7.4%	7.1%	5.0%
Wales	-0.3%	-6.8%	1.4%	3.3%	7.3%	7.2%	4.5%
Scotland	1.0%	-2.0%	1.0%	1.0%	2.7%	4.3%	4.3%

■ Over the course of 2009 average UK residential values improved by 3.4%, according to the Nationwide quarterly indices. Meanwhile their monthly index registered slightly higher growth of 5.9%. As we embark on a new decade, average values are 12% below their September 2007 peak.

■ Royal Institution of Chartered Surveyors (RICS) data suggests that, during the second half of 2009, the imbalance between the number of new applicants and new stock coming to the market, which strengthened in the first six months of 2009, started to weaken. Seasonally adjusted figures for December indicate that the balance of surveyors seeing an increase in new applicants had fallen to +20 from a peak of +65 in June. Those seeing an increase in stock levels was 17% higher than those seeing a decrease, up from -21% in May. In the snow-affected month of January both monitors fell into negative territory (albeit that buyer enquiries were hit harder than instruction levels).

■ Data from the Inland Revenue suggested that transactions in the three months to the end of November increased to 87,000 up from a low point of 47,000 in the first quarter of 2009, but still well below the quarterly average of 132,000 recorded between 2005 and 2007. December figures show a substantial increase in transaction numbers as buyers sought to take advantage of the temporary stamp duty holiday.

■ Figures from the Council of Mortgage Lenders (CML) indicate that following a significant increase in the number of mortgage completions from January (23,000) to July (53,000) completions fluctuated between 50,000 to 55,000 per month between July and November.

■ Buy-to-let mortgages for new purchases stood at 14,500 in the third quarter of 2009, compared to 48,700 for the same period two years earlier.

Key: Annual house price growth

Prime markets: Forecast values

Forecasts (as at January 2010)	2009 (Actual)	2010	2011	2012	2013	2014	2015
Prime Central London	8.9%	-1.0%	7.0%	11.1%	7.5%	6.3%	6.3%
Prime Regional	1.3%	-1.0%	5.4%	8.9%	7.2%	6.1%	6.1%

Prime Central London

■ Savills Prime Indices show that average values in the prime central London market increased by 4.6% in the final quarter of 2009 putting annual growth at 8.9%. In prime south west London, values rose by 17.8% during the course of the year supported by equity-rich buyers acquiring their main residence who returned to the market in significant numbers. In the fourth quarter, stock levels were 30% below the 2003/2007 average in prime central London. Demand indicators based on applicant numbers, viewing numbers and transactions relative to supply suggested that the demand to supply ratio during Q409 were in line with the five-year average for the same quarter, whereas a year earlier they were 50% of this figure.

■ In the ultra-prime market where values average £15m plus, values decreased by -1.3% during 2009 despite growth of 3.2% in the last quarter.

■ Meanwhile, prime central London rental values increased by a further 1.3% in the last quarter of the year, although overall they remained -2.1% below their starting point in January.

Prime Regional

■ Value growth in the prime markets outside of London was much more subdued and rose by 1.3% over the year, according to Savills Prime Regional Indices, with growth of 2.4% recorded during the final quarter of 2009. The highest growth took place in the south east region, where values ended the year 4.6% higher than at the start.

■ Much more significant improvements were seen in transactional activity, which progressively fed northwards in the prime markets of Great Britain. Scotland was the last region to benefit, with greater demand and transactional activity in the last quarter driving values up by 2.8% for that period.

Investment / Rentals

The investment yield

The Noughties was the decade of buy-to-let. **Lucian Cook** explores the investment opportunities of the future and who will be best placed in the market to exploit them

One of the key features of the Noughties was the change in attitude towards residential property as an investment asset, which was largely fuelled by the rapid expansion of the buy-to-let market. Council of Mortgage Lending (CML) statistics show the number of outstanding buy-to-let mortgages rose to over 1.2 million at the end of 2009 from just under 75,000 at the beginning of the decade.

As we start a new decade the residential investment market has reached a crossroads. The annual number of new buy-to-let mortgages is currently down by 60% from peak lending in 2007. Restricted mortgage availability and low-income yields have left this market accessible only to those with high levels of equity.

Income yield pressures

The strong growth in values from 2000 to 2007 meant that gross income yields fell from 8.1% at the beginning of the decade to just 4.6% prior to the recent downturn. This signified that for most investors total returns were governed almost exclusively by capital growth.

Even accounting for the downturn in values, average gross yields have only been pushed out to around 5.5%, meaning that the ability to borrow against new buy-to-let investments remains limited. Therefore, it is unlikely that the buy-to-let market will make a comeback in the same form during this new decade.

Despite competitive total returns and lower volatility compared to other investment asset classes, the residential investment proposition has recently largely been shunned by major institutional investors due to low income yields, the intensive management requirement and small lot sizes.

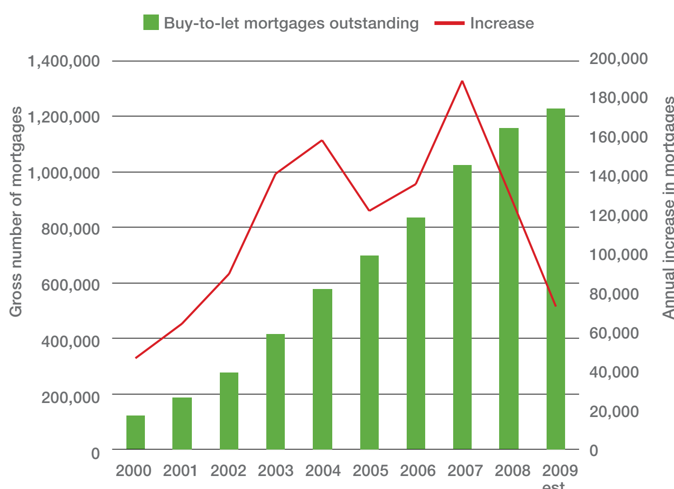
Yet, given restricted access to home ownership, large-scale investors are increasingly recognising the growing demand for private rented sector residential accommodation. This is likely to be a key driver of rental growth over the next decade, particularly in the lower tiers of the housing market to which the private rented sector is already skewed. Listings data from Globrix indicates that one- and two-bedroom flats account for 51% of the rental supply, but just 21% of sales stock. Three- and four-bedroom houses account for just 25% of the rental market, but as much as 55% of the sales market.

Divergent income returns

The differences in the profile of these markets is reflected in yields. The lower-tier markets, where renting dominates, generally deliver much higher yields than larger family houses. This is because the equity-rich owner occupier buyers dictate capital values, consequentially suppressing income returns in the higher value markets.

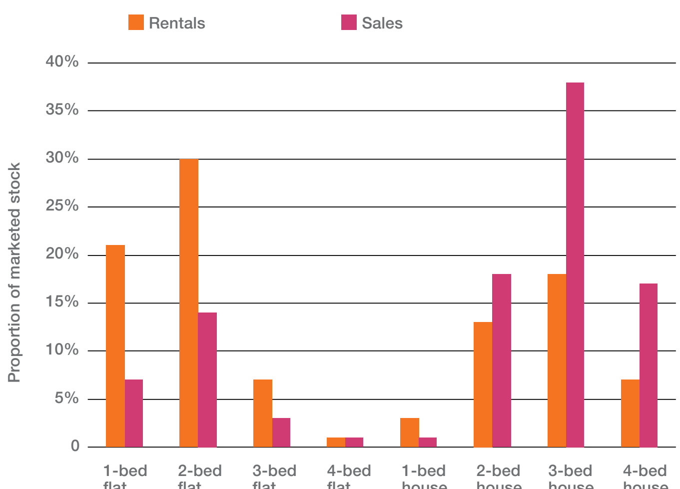
Our analysis of asking rents and house prices within 15 conurbations throughout the UK suggest that gross yields for

Graph 3.1
Buy-to-let mortgage levels



Source: CML

Graph 3.2
Stock profiles



Source: Globrix

The expert perspective
Research Director Lucian Cook provides the answers

What will now attract investors to the residential sector?
Historically, residential investment has produced total returns that are comparable to other asset classes but with much lower volatility. This factor together with the prospect of increased rental demand as the private rented sector grows, principally will drive the investment market in the future.

Who do you believe these investors will be?
A repeat of the level of investment from private investors reliant on borrowing seems unlikely. This will create opportunities for institutions and investment funds who are likely to counter low income yields by looking at any opportunities such as build-to-let.

one-bedroom flats are as high as 6.04%, whereas for a four-bedroom house the yield is as low as 3.87%.

Unsurprisingly, and for similar reasons, income yields have a geographical trend. The highest yields being in Nottingham, Tyne and Wear, Merseyside and Greater Manchester and the lowest in Bristol, Edinburgh, Bournemouth and Brighton & Hove. Likewise, across London, there are significant borough-by-borough variations. The average gross yield in Barking and Dagenham is at 6.38%, compared with 3.87% in the City of Westminster.

The yield dilemma

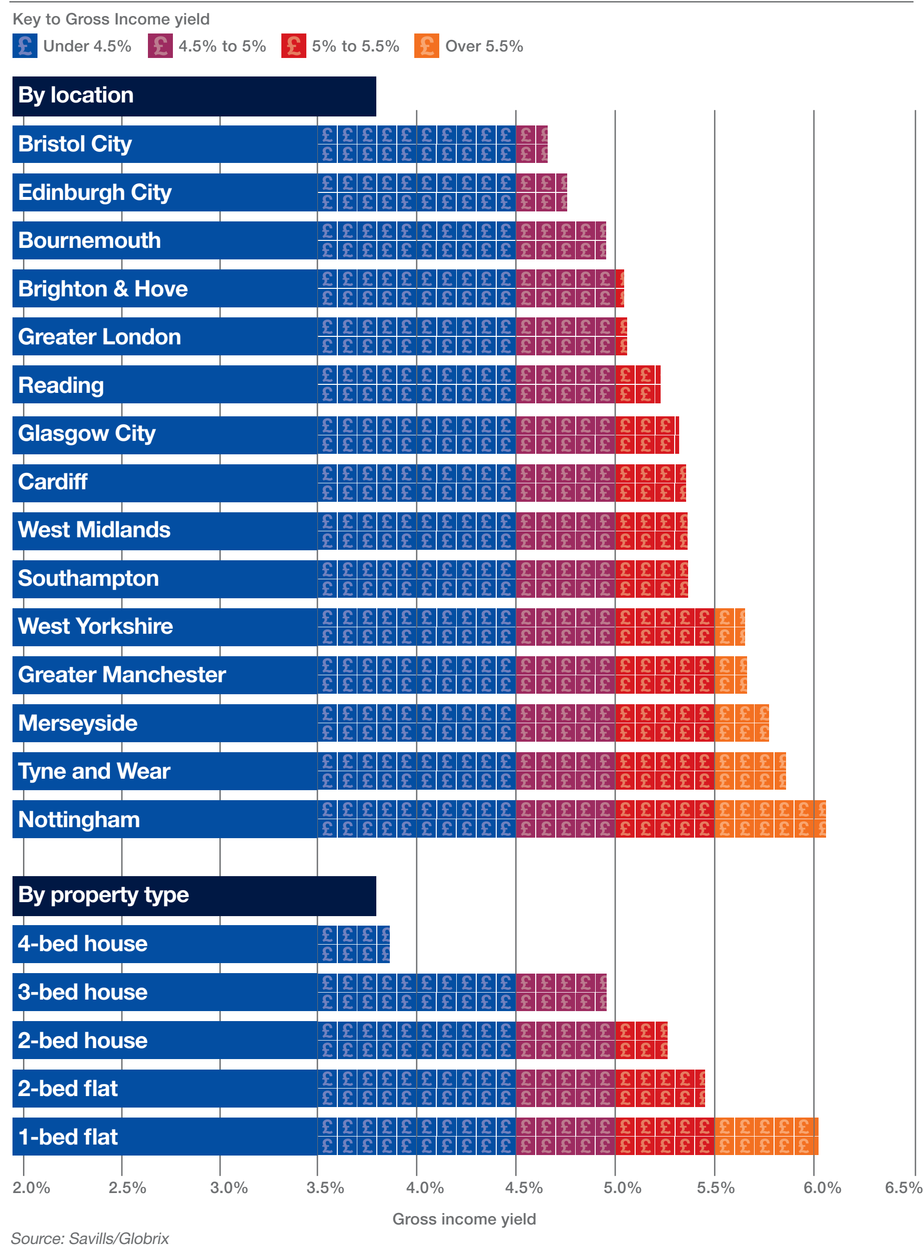
For many investors, this market and corresponding yield profile will dictate their investment choice pushing them to higher yielding, lower value markets where tenant demand is strongest.

These higher yielding options provide a greater opportunity to borrow against assets while retaining cash surpluses. The downside is that with less demand from owner occupiers, future capital growth is much lower than for the lower yielding alternatives as shown by some worked examples in Table 3.1 below.

For private investors, institutions and funds alike, diversification within residential portfolios will be fundamental in striking a balance between income yield and total return. Irrespective of this, underlying income yield constraints are likely to mean that, while the last decade will be remembered for the explosion of buy-to-let, the next will remembered for innovation in the residential investment market.

This is likely to be borne out of necessity, not just to meet the demand for private rented accommodation and intermediate tenure products, but also the need to supplement income with realisable capital growth. ■

Graph 3.3
Gross residential income yields



Source: Savills/Globrix

Table 3.1: The yield dilemma

	1-bed flat Nottingham	2-bed flat Borough of Greenwich	2-bed house Manchester	3-bed house Borough of Wandsworth	4-bed house Bournemouth
Average capital value	71,200	230,000	108,500	496,100	388,000
Average rental value	5,200	13,000	6,400	21,600	12,300
Gross yield	7.3%	5.7%	5.9%	4.4%	3.2%
Net yield @ 65%	4.7%	3.7%	3.8%	2.8%	2.1%
Expected capital 5-year growth	8%	19%	10%	29%	20%
Sustainable LTV	74%	57%	59%	44%	37%

Development

The ups and downs of high-rise living

The detached house made way for the new-build flat, and city centre living made a comeback, but what asks **Marcus Dixon** is the future of development?

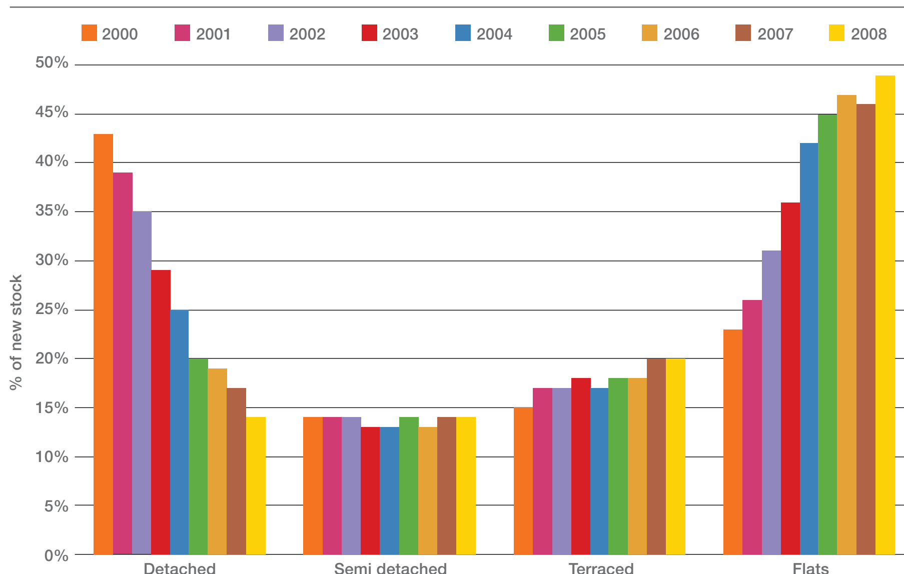
From a new-build perspective the Noughties was undoubtedly the decade of high-rise living. Development shifted from greenfield housing developments to denser brownfield schemes, particularly in more urban locations. In 1999, new-build flats accounted for just 17% of the new housing, by 2008 they represented nearly half at 48%. The casualty during this strive for higher density was the detached house, accounting for 43% of total completions in 1999, but only 14% by 2008.

The delivery of new homes peaked in 2006 and 2007 with 178,000 new homes completed during each of these two years. In 2008, starts and completions were significantly less, a trend which we expect to continue for at least another six years while the market stabilises and volumes of new development return to more 'normal' levels. Even during the 2006/2007 years, where development levels peaked, household projections were still not matched. This pent-up demand coupled with the prospect of lower levels of development activity during the short and medium term will lead to future issues over housing provision. The real test being whether the right type of stock in the right place can be delivered.

Following decades of neglect, the Noughties saw city centre living once again become fashionable. There were significant levels of new development in the centres of some of the UK's largest cities including Manchester, Birmingham, Bristol and Leeds, where young professionals and the relatively new buy-to-let investor making city centres rich pickings for developers.

With memories of high-rise social housing experiments receding, the city tower block became an aspiration rather than an eyesore, and developers sought to achieve higher housing densities by building upwards. By the middle of the decade an increasing number of planning applications were being submitted for buildings above 20 storeys, with 87 in the pipeline in 2005 (almost 19,000 residential units). However, rising costs and difficulties with off-plan sales proved too much of a burden, and many of these schemes were the first to be 'mothballed' as the downturn took hold. High-rise schemes (outside of high-value markets) were no longer the jewel in the developers' crown, but the millstone around their necks.

Graph 4.1
New dwellings by type



Source: NHBF

The rise of buy-to-let

Undoubtedly, one of the major catalysts of the shift towards urban new-build development was the explosion in the buy-to-let phenomenon. The seeds for this change were sown by the changes to Landlord and Tenant legislation of the late 1980s, but it was not until the late 1990s that it became easier to obtain funding to buy property for rental purposes as lenders moved away from the previous commercial-based mortgages, which did not take into account rental income in their calculations.

The success of buy-to-let and the appetite for lending meant the buy-to-let opportunity was not restricted to larger investors and those with significant levels of equity. This resulted in high levels of take-up and ironically, led in part to the issues over buy-to-let returns and oversupply we see today in some areas.

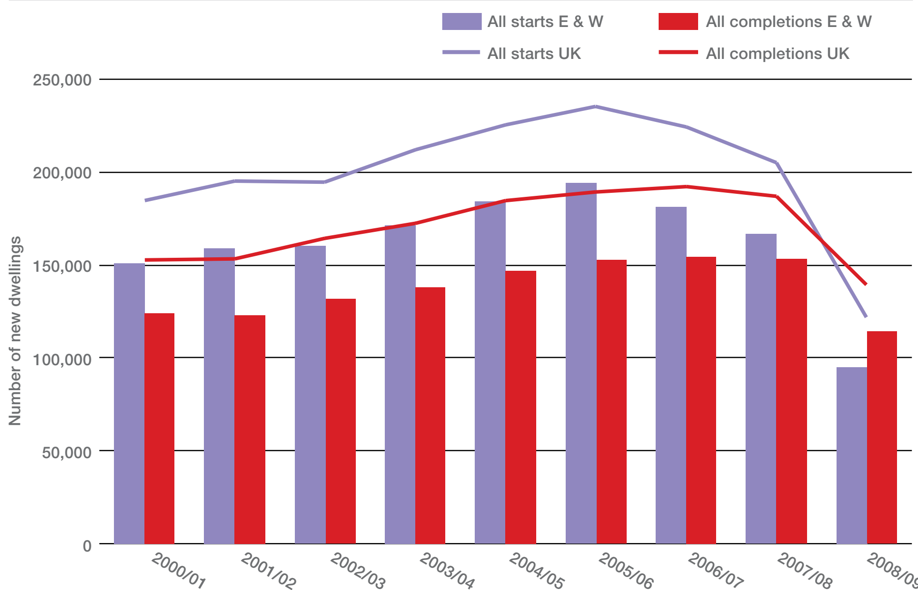
These issues were particularly acute in markets where a significant proportion of similarly priced units were being completed within a short time frame. These increased void rates and the prospect of having to lower rental levels to compete took many less experienced investors by surprise and created real issues once prices started to fall in 2007.

The expert perspective
Associate Director Marcus Dixon provides the answers

What is the future of new build? Houses or flats?
Although we do not fully expect that flatted development will disappear entirely, there is a very strong argument for high-density house development as an alternative going forward. Our research shows a distinct lack of new-build houses, with price growth outperforming that of new flats over the past decade, a trend we expect to continue in the future.

How can we meet Government housing targets?
Funding difficulties have meant that small development sites with lower upfront costs are a more viable option for many developers. However, these small sites will struggle cumulatively to meet Government targets. We now need to find a way to enable large schemes to progress and bring the new homes to market.

Graph 4.2
Historic starts and completions



Source: DCLG

New high-rise developments

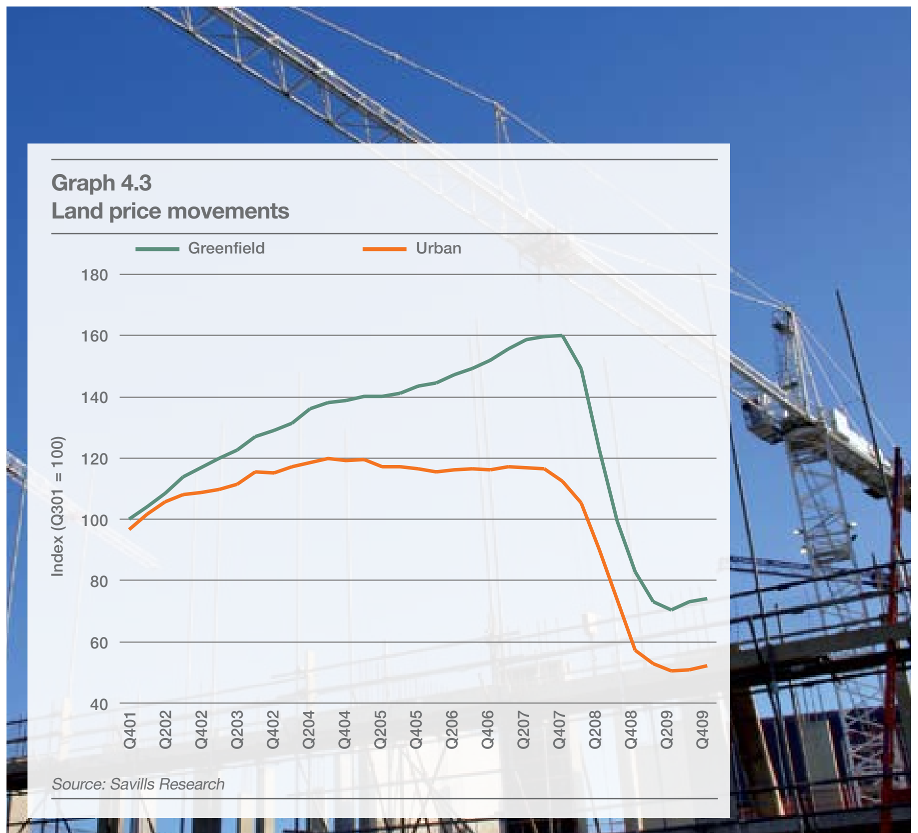
A high concentration of new high-rise developments and a change in the type and size of flats built has led to new flats underperforming the second hand market in terms of value growth. Over the Noughties new-build flat prices increased by an average of 60% compared with 117% for all property.

In terms of value, on a type-by-type basis the performance of new detached, terraced and semi-detached houses has been comparable to second-hand stock. However, the change in the profile of stock built, away from larger detached units and towards higher numbers of smaller units has affected values. The average price of a new-build house has increased by 92%, some way short of the average growth for second-hand stock.

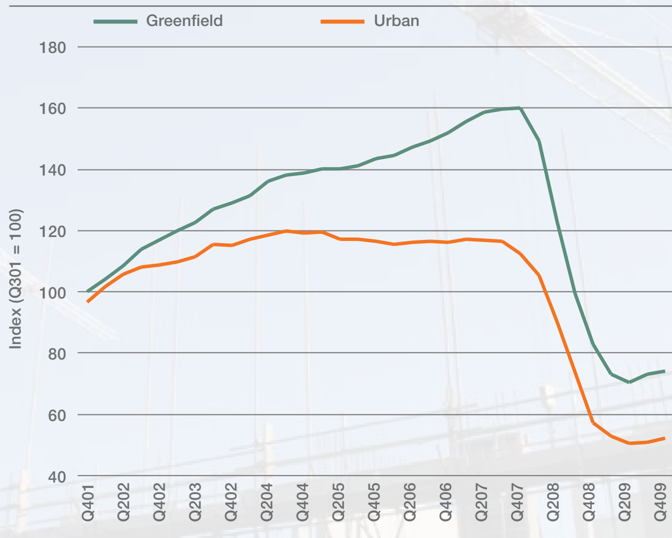
Premiums for new-build stock, which existed pre-downturn, have been significantly eroded for all but the most niche stock, with valuers and more value-savvy buyers looking for prices on a par with or (in high-supply markets) at a discount to second hand stock.

The land market

After sustained growth in the first half of the Noughties, urban land values stagnated, before recording significant falls at the onset of the housing market downturn in late 2007. By comparison, greenfield value growth continued until peak, but has subsequently been affected by developer confidence and the availability of debt finance. Although land values have stabilised in recent months this should not be read as a return to normality or even the beginning of a more prolonged upturn in the land market. However, it does reflect some broader shifts in the market.



Graph 4.3
Land price movements



Source: Savills Research

What does the future hold?

With the prospect of more constrained access to development finance, and an emphasis on owner occupiers rather than investors, we expect the next ten years in the world of residential development to be a different prospect. With large schemes making up a high proportion of the development pipeline, a new way of looking at large-scale residential development will be vital. Developers will need to look at the long-term benefits of site ownership and management in order to maximise returns and offset substantial upfront costs and infrastructure.

For developers looking for smaller sites, we expect that serviced plots will be more attractive, with smaller housing sites in high-demand areas being most likely to recover first and attract competitive bids.

Although the current situation does not signal the death of the city centre flat, both developers and investors will need to think carefully as to whether the demand is there to fill new flats in urban areas. ■

Summary

After the volatility of the last few years, the new decade heralds significant growth differences across various property sectors

■ The coincidence of low interest rates, poor stock market returns and opportunity for low cost gearing encouraged many equity-rich homeowners to become residential landlords over this period. This, combined with the increased inaccessibility of the housing market for those without the equity for a deposit, ensured that rental demand exceeded or matched supply. See page 3.

■ Following a few years of anticipated volatility in the residential property market, inflation adjusted growth during this decade is likely to be around the 40% to 45% mark. This will, however, mask quite significant differences in growth across the various sectors with stronger house price growth in the equity-rich markets of south east and central England. See pages 4-5.

■ During the last decade, growth in the value of prime property outside of London was more subdued than that seen in either the UK mainstream markets or the prime London markets. While the prime regional market was equally affected as prime central London by the credit crunch and the financial events of the decade, it did not enjoy the same extent of growth during 2006/07. Against this backdrop, the relative under-performance in the Noughties of the prime regional markets points to a stronger capacity for growth during this new decade. See page 6.

■ There are signs that internationalisation is creeping into the country house market. This is particularly prevalent in the south east of England, where the giant's share of prime regional properties bought by overseas buyers are located. See page 6.

■ There will continue to be a need for some urban high-rise development but developers and investors will need to appraise locations on a site-by-site basis to establish whether the demand is there. The prospect of more constrained access to development finance, and a shift in emphasis to owner occupiers from investors, will lead to a very different decade for the world of residential development. See pages 12-13.

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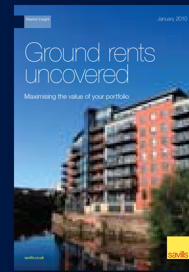

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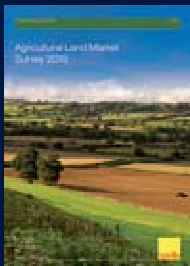

Agricultural Land Market Survey 2010

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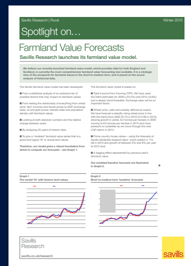

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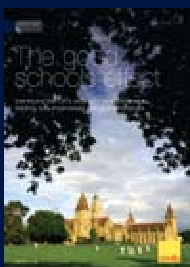

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How good state and independent school options can make houses worth two or three times their county average.

UK Office Market Report Winter 2009

Investment confidence has grown in prime stock, while the occupational markets are still below trend.

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