UK Affordable Housing – Summer 2024

SPOTLIGHT
Savills Research

Shared Ownership:
A key piece in the housing puzzle

savills

Scale of the market ■ Occupier demand ■ SWOT analysis

Shared Ownership (SO) has come a long way since its introduction in the 1980 Housing Act as an affordable home ownership product. It allows buyers to purchase a share of a property and then pay a subsidised rent on the remaining share. SO has grown significantly to a quarter of a million homes and has become a well-established affordable housing tenure providing households that would otherwise not be able to access the home ownership market with a route to home ownership with much lower deposit requirements.

SO is likely to continue to provide an affordable route to home ownership in the future and our paper highlights how there are likely to be market-led opportunities for SO to grow further.

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An enduring element of the market

Shared Ownership has become an established fixture on the affordable housing landscape, but what is the total scale of the sector?

We remain in a housing crisis with an urgent need to provide households with access to more affordable and quality housing. Need for affordable housing continues to significantly outstrip high quality supply with close to 113,000 households in temporary accommodation as of Q4 2023, and estimates that we should be building between 120,000 and 140,000 affordable homes each year to meet affordable housing need. A new incoming government will be looking at how best to tackle need. SO could have an important role to play as an established affordable housing tenure continuing to provide an affordable route to home ownership. Another key element here is the significant number of investors looking to deploy private capital and enter the sector.

If the Government commits to maintaining current delivery levels for SO, the tenure could support 100,000 homes over the next five years. This helps towards the Government target of 300,000 homes a year and would draw down £2.2 billion of private capital into the sector each year.

In 2023, Low Cost Home Ownership (LCHO) homes (mostly SO) owned across the sector exceeded 250,000 homes. Whilst the overwhelming majority of SO homes are owned by Private Registered Providers (Housing Associations), For Profit Registered Providers (FPRPs) have significantly increased their share of SO homes as more new entrants bringing new private capital have entered the sector. SO remains a key priority for FPRPs providing investors with a secure rental income and exposure to house price inflation through staircasing.

SHARED OWNERSHIP IN NUMBERS

252,220
Total SO homes (England)

3,345
SO homes acquired by For Profit Registered Providers in 2022-23

9%
New AHO completions as % of net additional dwellings, five year average

91%
% of SO homes owned by Private Registered Providers (Housing Associations)

37%
New AHO completions as a % of total additional affordable housing supply, five year average

2.6%
100% staircasing sales as a % of total SO homes each year, long term average

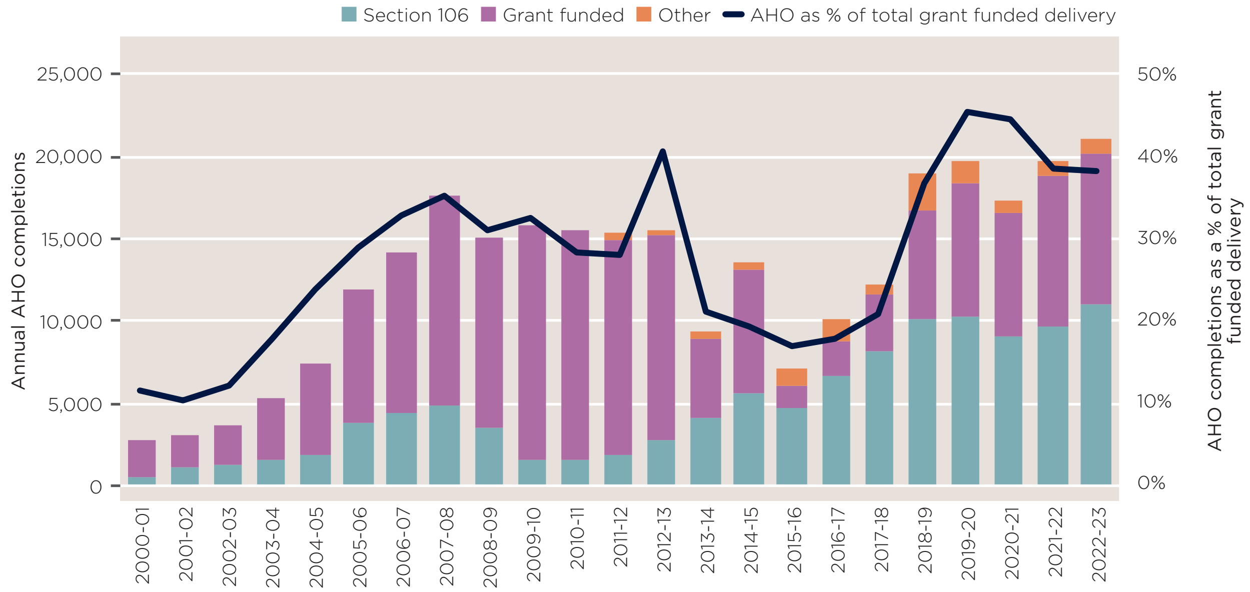
Source: Statistical Data Return (SDR), DLUHC

"Shared Ownership could draw down £2.2 billion of private capital into the sector each year"

Increasing reliance on Section 106 delivery

In line with the wider expansion of Section 106 affordable housing delivery, Affordable Home Ownership (AHO) homes (mostly SO) are primarily delivered through Section 106 and are therefore exposed to market conditions and impacted by the wider slowdown in private housing delivery. This slowdown has been driven by weaker sales rates for new homes and a drop off in planning consents. A higher proportion of new AHO completions are delivered through Section 106 than across all affordable tenures, reaching a peak of 67% in 2017-18. In recent years, AHO Section 106 delivery has fallen back slightly whilst completions through grant funding have increased. This has been supported by an increase in grant funding available in the current Affordable Homes Programme including grant to buy and to flip completed homes originally intended for outright private sale to SO.

Figure 1 Section 106 comprises half of new AHO supply



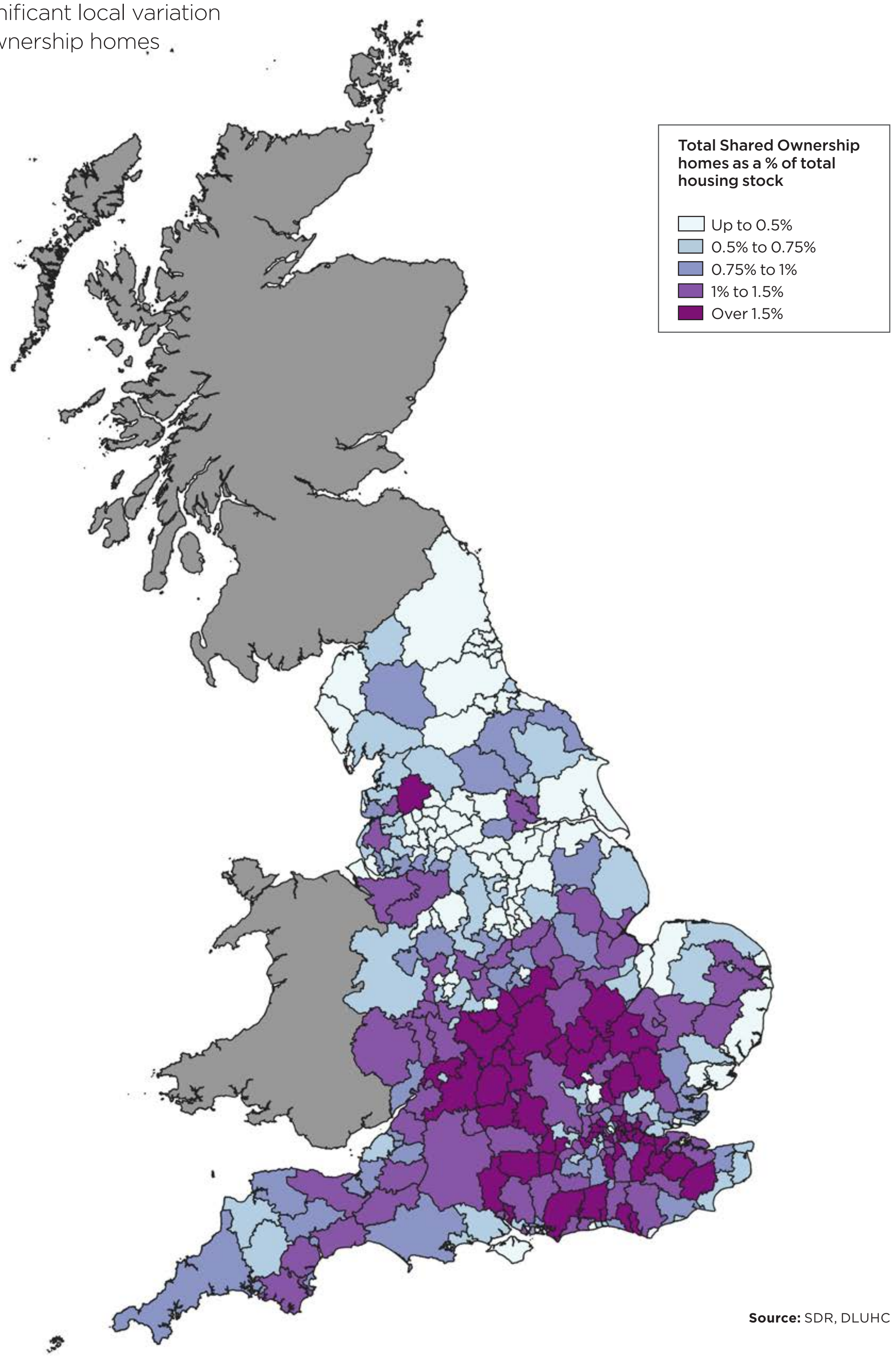
Source: DLUHC

Shared Ownership homes are concentrated in the most unaffordable markets

Unsurprisingly, SO homes are concentrated where buyer affordability pressures are greatest due to the significantly reduced deposit requirements the tenure offers. Just under a quarter of SO homes are located in London according to analysis of the SDR. Beyond London, a further 23% of homes are concentrated in the South East.

However, there is significant local variation. SO homes make up the highest proportion of total housing stock in Milton Keynes at 5.1%, followed by Dartford and Tower Hamlets at 2.8% and 2.7% respectively.

Figure 2 Significant local variation in Shared Ownership homes



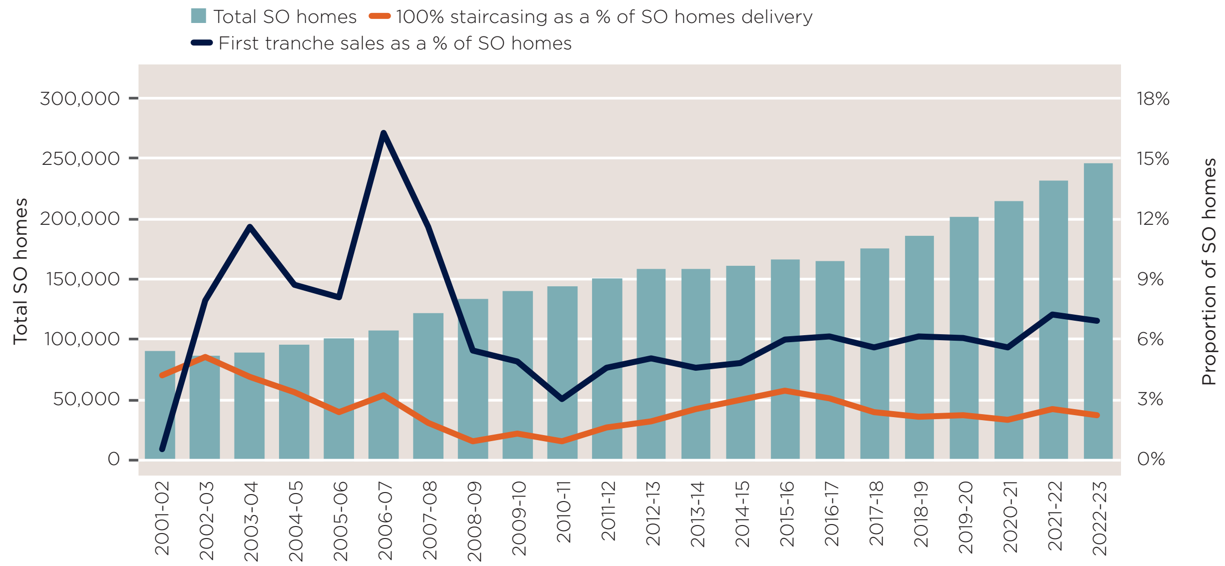
Source: SDR, DLUHC

Scale of the market

Limited turnover of Shared Ownership homes

There is a steady flow of new supply into the sector each year, but how does this compare to total homes sold to the open market through staircasing? Shared owners are given the opportunity to buy further shares in their property also known as staircasing, up to 100% ownership. This also includes buyers selling their homes on the open market and as a result staircasing to 100%. Data on full staircasing from the SDR reveals that a relatively small proportion of shared owners reach 100% ownership. On average since 2001-02, 100% staircasing sales represent 2.6% of total SO homes each year staircasing to 100% when they sell. This is outweighed by the number of additions to stock through newly built supply and units purchased by providers, with first tranche sales (i.e new shared owners coming into existence) averaging 6.7% of total SO homes each year. With low rates of 100% staircasing and an ongoing replenishment of new supply, SO stock has continued to steadily increase in size each year.

Figure 3 Ongoing replenishment of Shared Ownership supply



Source: Savills Research using HCA SDR and TSA RSR with data before 2008-09 from "Understanding the second-hand market for shared ownership properties" by Anna Clarke and Andrew Heywood, 2012, Cambridge Centre of Housing & Planning Research, University of Cambridge

Policy and regulatory risks

SO is exposed to the wider policy, regulatory and financial risks currently facing the housing sector. Sector financial capacity is significantly under strain from high build cost inflation, a focus on asset management of rented stock, higher costs of finance, caps on rental income and a lack of certainty around the future rent settlement beyond 2026. Housing Associations (HAs) are challenged with the growing requirement to invest in existing stock to meet building safety and decarbonisation requirements constraining development capacity.

The sector also faces risks around unexpected policy intervention. In recent years, the Government have made policy changes introducing changes to SO leases in May 2021, announcing that landlords are responsible for 100% of the repairs and maintenance costs up to £500 each year (for the first 10 years after completion) and lowering the minimum first tranche ownership stake to 10% (from 25%) and staircasing tranche to 1% (from 10%). Then in October 2023, the Government accelerated further reforms to new SO leases without consultation with rents for shared owners to be increased once a year at a maximum of CPI + 1%, moving away from RPI + 0.5%. Greater future stability in the SO model would support growth in investor appetite to support the tenure.

Future growth prospects

Looking ahead, there is a robust pipeline of affordable housing starts which will support total affordable housing delivery levels for 2024. However, there is greater pressure on SO delivery in the immediate term. The Q3 2023-24 quarterly regulator risk survey, an indicator of future supply, reports that total SO completions expected in the next 18 months reached their lowest levels since March 2020.

In the short to medium term, as a result of reduced sector capacity and an increasing focus on existing stock, Savills forecasts a substantial slowdown in affordable housing delivery with decreasing volumes of grant funded and Section 106 delivery. With supply through Section 106 at significant risk due to the wider slowdown in housing delivery as the two are inextricably linked, this will have a greater impact on SO due to the higher reliance on delivery through Section 106. SO supply is also at risk of displacement through the gradual implementation of First Homes, as Local Planning Authorities (LPAs) will prioritise the delivery of core rented tenures over SO. In 2022-23, over 1,000 First Homes were delivered in 63 local authorities but future appetite amongst LPAs to deliver First Homes remains highly varied.

Growing demand

There is significant and growing demand for Shared Ownership from consumers, particularly in a high interest rate world

Shared Ownership supports a key, and sizeable part of the housing market

While there are currently a little over 250,000 SO households across England, we believe there is far greater capacity for SO homes. SO, as an Affordable Home Ownership product, helps support the "squeezed middle" part of the housing market – households aspiring to home ownership but unable to make the leap without support. This is a vast, and underserved part of the housing market.

The average household income of a SO buyer is £32,200, far lower than the typical First Time Buyer (FTB) income of £64,000 – largely a consequence of a much higher proportion of SO users buying with a single income. The majority of SO buyers have household incomes between £25,000 and £43,000, according to our analysis of data from our sponsors, With approximately 1.4 million households in the private rental sector within this income range across the UK. There is significant potential to scale up SO to meet the pool of demand that SO may appeal to.

A useful benchmark for estimating the demand for SO is data from Help to Buy. This scheme also provided a low-deposit step onto the housing ladder, and SO has often been branded its successor (despite pre-dating Help to Buy by decades). Help to Buy supported an average of 37,000 buyers per year across England over the decade it ran for. In its absence, SO is well placed to pick up this level of activity.

Shared Ownership allows buyers to step onto the housing ladder earlier in life

Over half of SO buyers are single adults, with a further 30% being couples without children, according to data from DLUHC. This aligns with data from our sponsors, which show similar proportions. This contrasts with the distribution of all FTBs however, which have a greater diversity in household types.

SO buyers also tend to be younger than FTBs as a whole, with 70% of SO buyers under 40, compared to 50% of FTBs. This skew of SO buyers to younger and smaller households is partially a consequence of its affordability. It's easier to buy a SO home solo, and at a younger phase of life compared to purchasing outright.

We've compared SO buyers to FTBs as, while SO is not restricted to FTBs, only 10% of SO buyers over the past five years were already owner occupiers, a trend that has been fairly stable for the past decade. The majority of SO buyers (82%) move directly from either living with family or from the private rental sector.

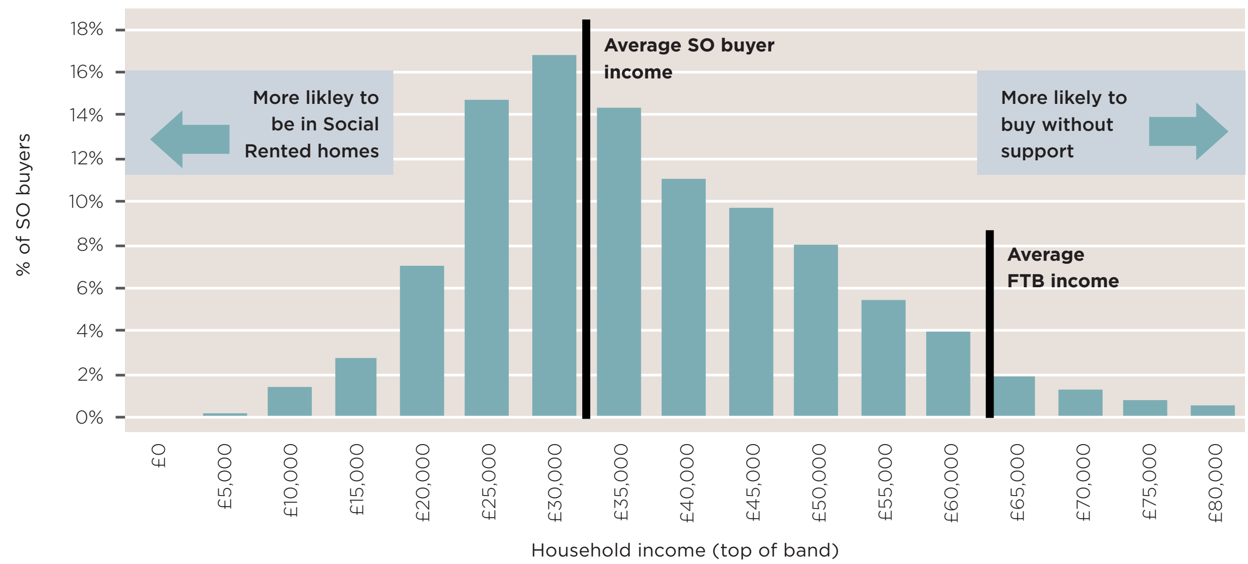
Only 4% of SO buyers have moved directly from the social rental sector, although some may have moved via the private rental sector first. Social rental tenants also have the option to buy their home via Right to Buy as an alternative route into home ownership.

What are the financial advantages to buyers?

SO is particularly appealing to buyers currently in the private rental sector but wanting a more secure form of tenure. The Government has been keen to reinforce this long term security, by encouraging 990 year leases. It gives them the ability to start building some housing equity. SO makes this possible for many households with its much lower deposit requirements.

The average FTB uses a deposit of 24%, equivalent to £71,000 for a £300,000 home. Those using SO have an average deposit of just 7%, or £22,200. The average first tranche sale proportion is 43%, meaning that SO buyers are able to acquire £129,000 worth of housing equity, and occupy a £300,000 home with a far lower deposit than they would be able to do otherwise.

Figure 4 Shared Ownership supports the "squeezed middle"



Source: Savills Research

Occupier demand

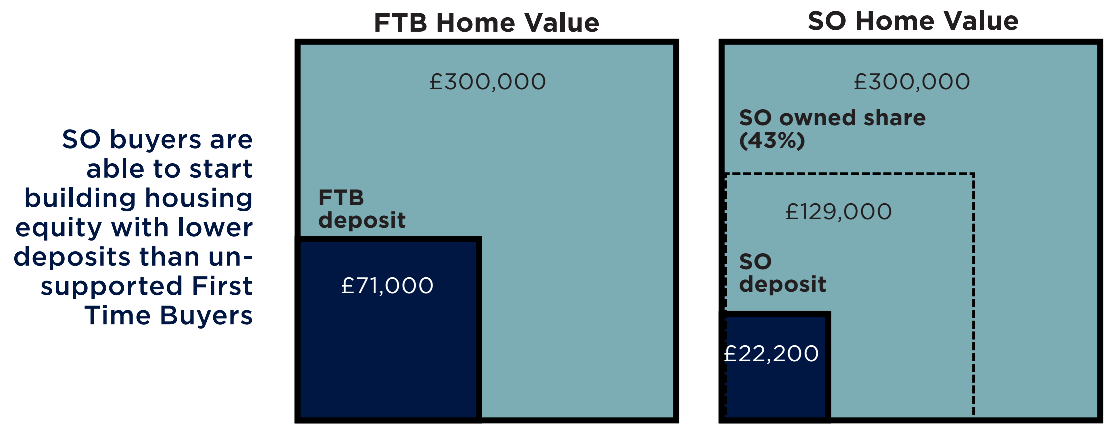
> This ability to accrue extra equity also helps buyers springboard onto their next home, potentially moving from a Shared Ownership home to a full ownership home even if they hadn't staircased to 100%

SO is also accessible to downsizers wishing to release equity for retirement, for single person households with lower deposit/income, and to equity-rich income-poor households such as divorced persons, offering scope to stay in the home ownership market. It is more flexible than First Homes, which is only available for FTBs.

Both typical FTBs and SO buyers tend to buy with essentially the same Loan-to-Income (LTI) ratios, as while SO buyers have a smaller mortgage, they also have a lower income, putting them largely on par with LTIs in the open market.

House prices typically trend upwards over time, so being able to capture some of this growth is very appealing to households who would otherwise struggle to overcome that deposit hurdle. This ability to accrue extra equity also helps buyers springboard onto their next home, potentially moving from a Shared Ownership home to a full ownership home even if they hadn't staircased to 100%.

Figure 5 Shared Ownership buyers are purchasing more expensive homes with smaller deposits



Source: Savills Research using UK Finance, CORE

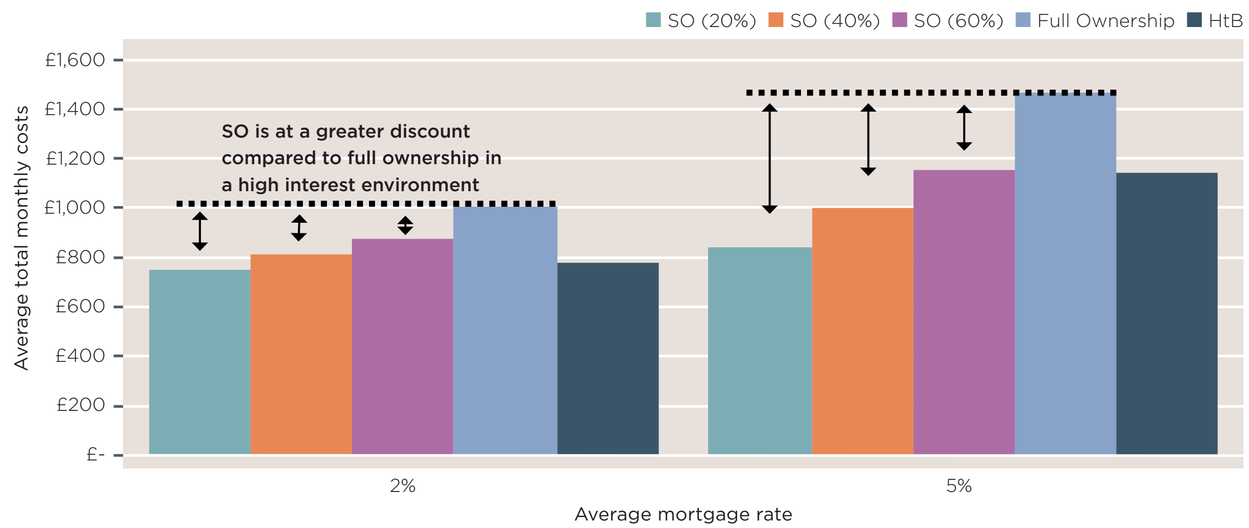
Shared Ownership is more appealing in a high interest rate environment

It's not just the lower barrier to entry, but the ongoing costs for SO are typically lower when compared on a like-by-like basis with full ownership. This effect is magnified in a higher interest rate world in which the smaller mortgage required for SO reduces exposure to the higher interest rates. This is alongside starting rent on the retained equity being locked at 2.75% – someway below current mortgage rates and rental yields.

This greater discount may help to drive additional demand for SO while rates remain high.

But what happens to these costs over time? Our prior paper shows that SO costs, with upward only rent movements in excess of inflation, do trend above other tenures in the long run, but it takes many years for this to happen – often decades, depending on the initial equity stake. In reality, owners will aim to staircase, increasing their equity and reducing their exposure to these escalating costs.

Figure 6 Shared Ownership homes are partially insulated from higher rates



Note: This assumes a purchase price of £300,000 and a 30-year mortgage term.

Source: Savills Research

Why Shared Ownership?

Why do investors like Shared Ownership? What are the prospects for the sector going forward?

Increasing allocation to affordable housing

SO is an attractive long term investment proposition for the growing weight of capital targeting the affordable housing sector. It offers investors exposure to house price inflation primarily through the asset value, alongside a secure index-linked income stream on the unsold equity of homes.

To date, private investment in SO has been concentrated amongst a small number of active players, focused on buying new SO homes. Primarily, these new entrants have expanded their pipelines through acquiring Section 106 homes but more recently some FPRPs as strategic partners under the current Affordable Homes Programme, have been focused on grant funded delivery. To date, sales of existing stabilised SO portfolios have been concentrated to a handful of buyers, with other investors acquiring stabilised SO as part of mixed tenure portfolios.

However, in addition to existing players who are keen to continue to raise capital, there is an increasing pool of new entrants including pension funds looking at the sector credentials to deliver lower and more stable returns with less sales risk and access to portfolios of scale.

According to the 2024 Savills European Living Investor Survey, 39% of investors are targeting private investment in affordable housing over the next three years. Of these, over 53% are looking to invest over €100 million into the sector, indicating the scale of new capital targeting the sector.

Enhanced financial returns

SO provides capital receipts from first tranche sales and staircasing in addition to the steady rental income delivered through the unsold equity of homes. SO sales have added a total of £6.5 billion to HA turnover over the last decade through both first tranche sales and staircasing.

SWOTing up

Strengths

■ SO **increases delivery** of much needed homes and provides households with a secure route to home ownership.
■ SO delivers **social value and impact** as it allows investors to engage in responsible investment and play a significant role in helping to meet housing need.
■ SO also provides households with **security of tenure** as an alternative to the private rented sector.
■ **Well established** affordable housing tenure steadily increasing in size, with over 250,000 homes owned across the sector.
■ **Residents are part owners** of their homes and are therefore more long term partners rather than tenants. As a result, SO defaults are rare.
■ **Lower management requirements** of SO homes when compared to core rented tenures.
■ **Growing asset class** with relatively low levels of shared owners reaching 100% staircasing each year, outweighed by new first tranche sales of SO.
■ **Stable pricing** of SO as an asset class has made it increasingly attractive to investors during challenging market conditions.
■ Provides investors with a **highly secure long term, index-linked income stream** – staircasing rates are predictable and there is an ongoing source of new stock to replenish units in the fund.
■ **Exposure to house price inflation** through the increasing asset value, allowing investors to tap into what has been a consistent source of value growth.
■ **Enhanced financial returns** from staircasing and first tranche sales for new SO homes.

“Shared Ownership is an attractive long term investment proposition for the growing capital targeting the affordable housing sector”

Weaknesses

■ **High barrier to entry** due to lack of familiarity and expertise with the sector from most investors and generally requiring a purchaser to either own a FPRP, or have a FPRP manager willing to manage the stock on a long term agreement.
■ **Limited visibility and lack of publicly available data on partial staircasing**, which is a further barrier to entry for some sources of capital.
■ **Limited activity to date**, considering investing in stabilised SO is a fairly new asset class – investor confidence will grow as more FPRP funds enter the market.

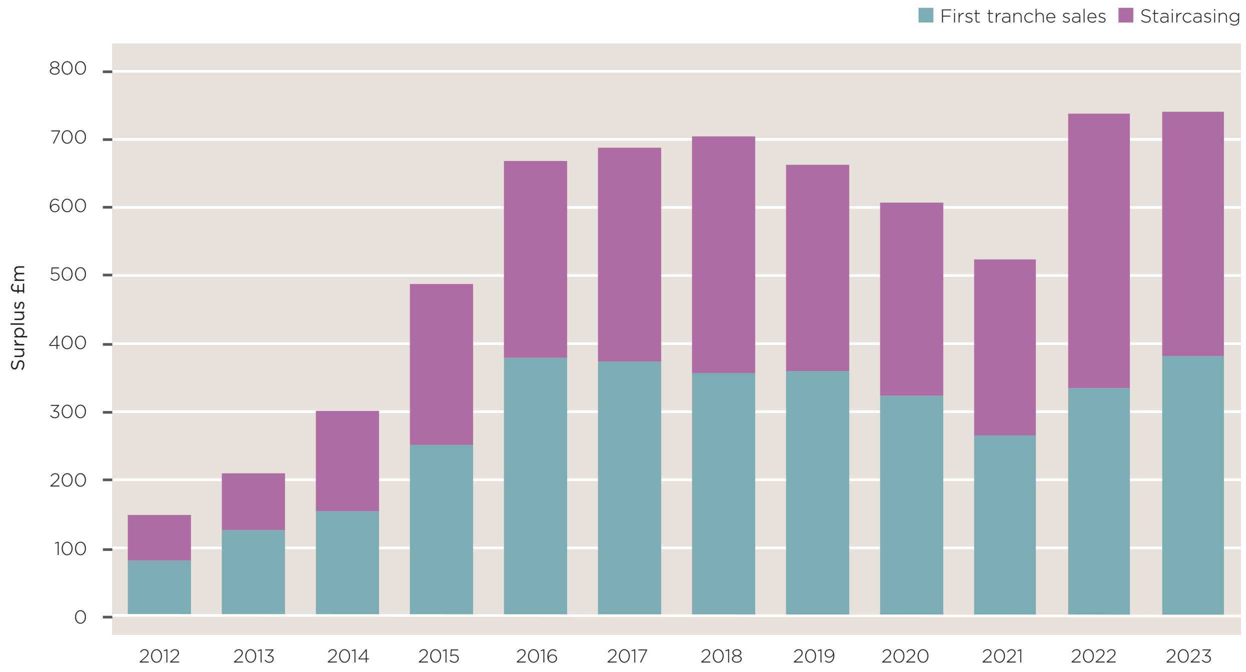
Opportunities

■ Stronger occupier demand for SO in a **higher interest rate environment**.
■ **Diverse profile of SO homes** from suburban houses to flats and with significant local variation.
■ SO provides opportunity for **investment in different forms** from forward funding deals to buying standing stock.
■ **Traditional HAs looking to dispose** of stock given sector financial capacity challenges and looking to invest in existing stock and new homes delivery.
■ Role of SO in helping to fill the gap left by **the end of the Help to Buy** scheme but limited by available grant funding.
■ **Acquisition of stock from housebuilders** has supported those looking to de-risk schemes, given the slowdown in sales rates for new homes and a lack of appetite from traditional HAs.
■ **Legacy SO homes** are less desirable to investors than new build portfolios. This stock represents a significant opportunity for investors to drive additional returns but also achieve positive environmental impact by working with leaseholders to upgrade sub EPC C stock.
■ **Liquidity can be improved** with the sale of the assets and the FPRP Op Co, enabling new entrants immediate access to the sector without the time delay of FPRP registration.

Threats

■ **General lack of understanding** of the tenure by both consumers and investors.
■ **Traditional Housing Associations’ financial capacity** is under significant strain.
■ **Unexpected policy intervention** without consultation means there is a level of uncertainty for investors, particularly in an election year.
■ **Pressure on future SO supply** due to general slowdown in market conditions including a slowdown in affordable housing delivery through Section 106 and grant funding.
■ **Strong competition from BTR / SFH investors** for alternative tenures.

Figure 7 £740 million in capital receipts from Shared Ownership sales in 2023



Source: RSH Global Accounts

What's currently trading?

Until recently, most stock delivered by investor-led FPRPs was new build development or forward funded acquisitions of new build stock and this continues to be a key supply route. For their pipelines, investors are not seen to be affected by the prospect of a rent cap (as new homes are not affected). While L&GAH and Sage have built mixed tenure portfolios, Heylo, M&G and Gresham House/ReSi have focused on SO.

Those FPRPs with leverage against their current portfolios were particularly affected by the rise in interest rates. As the market has eased, we have seen Sage enjoy success with its Home Stepper (SO) product, using grant to convert private units for market sale to SO. M&G Shared Ownership is actively acquiring stabilised SO, including older/dispersed stock. Gresham House/ReSI have focused more on new development than acquiring stabilised portfolios. The market for stabilised SO is still in its infancy, however there are a number of transactions at scale. Before 2023, trading was in the region of c.3.0-3.4% NIY depending on scale and geography. Current pricing has moved out 25-50 bps with NIY in the region of 3.5%-4.0%.

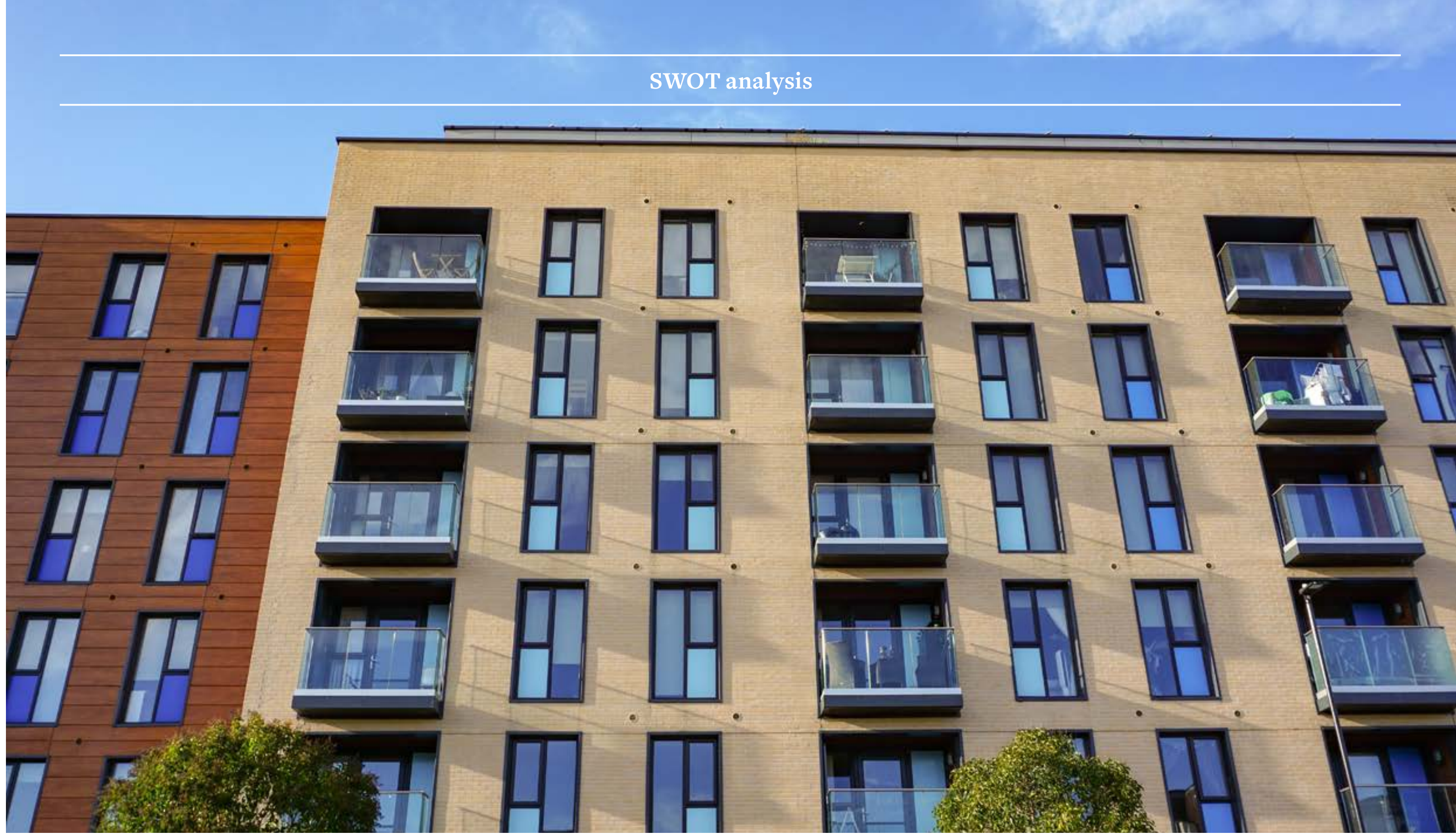
Most investors have limited appetite for sub EPC C stock and instead are more focused on delivering new build homes to EPC A or net zero standards. Investors also have less appetite for pepper potted SO flats with 3rd party freeholders. Houses and unbroken blocks are preferred.

What next for Shared Ownership?

At present, the current pool of experienced, scaled, institutionally backed FPRPs with appetite to acquire stabilised SO assets at scale is relatively small, but is expected to grow. Whilst sufficient to absorb current levels of stock presenting to market, structurally, the market requires further development to increase the pool of available capital to HAs seeking to release capital from asset sales. The market may develop in a number of ways including more funds establishing FPRP entities and HAs establishing FPRP entities as a route to access third party capital off balance sheet.

In a post-Help to Buy world, SO has significant scope to expand and help fill the gap in new build sales. Housing affordability remains a key national issue and this is unlikely to change in the near future, meaning accessible routes to home ownership will be key.

Private developers have taken note, and there is an expanding array of Shared Ownership-like products available as developers seek to innovate in the absence of Help to Buy and offer a range of options to buyers.



Mythbusting

MYTH: Shared Ownership homes are mostly flats in London

REALITY: 77% of all new SO homes are delivered outside of London. While many of those SO homes in London will indeed be flats (as with most new build homes in the city), many of them outside of the capital are houses instead. Data from Homes England indicates that over 72% of SO homes outside of London are houses or bungalows.

MYTH: Shared Ownership has high service charges

REALITY: While SO has received some negative press around high service charges, this issue is largely concentrated in flats provided in higher value areas in London, which is only a minority of overall stock. The vast majority of SO stock is houses where there are typically minimal service charges. Rising service charges are an issue for all leasehold high rise buildings, particularly in light of increasing safety regulations for such buildings. Service charges tend not to vary between SO and full ownership in a given building, all other aspects being equal. What is true is that the owner of a SO home will be responsible for 100% of the service charge, despite not owning 100% of the property.

MYTH: The occupier can never fully own their property

REALITY: Mainstream SO - the vast majority of supply - allows staircasing up to 100% ownership, with 2.6% of SO households doing so each year. There are some special situations and 'designated protection areas' (rural areas) in which there may be a cap of up to 80% total ownership to preserve access to sub market home ownership in perpetuity. In addition, even if owners don't staircase to 100%, they will have greater security of tenure and be building equity in the share they do own.

MYTH: The occupier can't sell their property

REALITY: Selling a SO home is perfectly possible and normal. The only difference is sometimes it is done via the housing association originally bought from. They have a period of time, typically between four and twelve weeks, to find a buyer for the property, and many HAs maintain waiting lists. If no buyer is found in that period, then the home can be sold on the open market via an estate agent. Because the housing association helps to find a buyer, in some ways it can be easier.

Savills Research
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