

RESIDENTIAL RESEARCH



HOUSEBUILDING REPORT 2018

EXCLUSIVE
HOUSEBUILDER SURVEY
2018

HOUSING SUPPLY

POLICY DEVELOPMENTS

SECTOR OUTLOOK

KEY SURVEY FINDINGS

It is achievable to build 200,000 - 250,000 net additional homes each year, according to 61% of respondents. Just 1% say it's possible to surpass 300,000 by 2022.

The large majority of volume housebuilders plan to increase construction starts this year. Most small developers intend to decrease activity or leave output unchanged.

Half of respondents say the Help to Buy Equity Loan Scheme should end via a tapered withdrawal starting in 2021.

Planning remains the main barrier to speeding up housing delivery, respondents say, although the proportion identifying the planning system as a hurdle has fallen since last year.

Respondents said outer London, the South East and the West Midlands present the greatest opportunities for housebuilders during the next three years.

MARKET UPDATE

The Housebuilder Survey examines the opportunities and challenges ahead for the development sector. It comes at a febrile time for housing policy, and also as the trends for price growth across the country are changing.

The housebuilding industry has responded strongly to the demand for new housing, increasing output by 55% over the last five years. Our annual survey aims to give a snapshot of where the sector is now, and where future opportunities and hurdles lie.

It reflects the views of respondents from more than 100 housebuilders and developers, ranging from FTSE100 companies to firms building fewer than 10 homes a year. Together, the respondents account for almost three quarters of all homes built across the country each year.

The survey comes at a key time for housing policy, with another new housing minister (FIG1) and a raft of consultations and new rules set to be introduced in the coming year (see timeline on page 6). Many of these changes, especially those that focus on providing infrastructure, amenities and Affordable Homes, will be welcomed, however the policy overhaul comes at a time of wider political and economic uncertainty.

In terms of house prices, the picture across the UK is changing, with a more evenly-spread rate of growth across the country, in contrast to growth being concentrated in

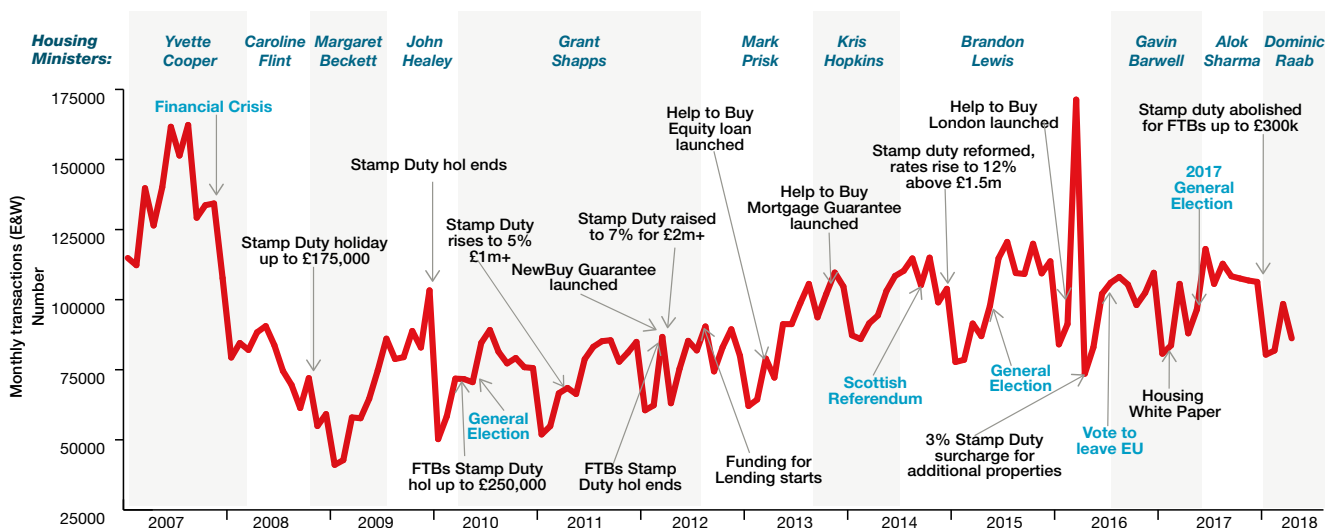
London and the South East, as has been the case in recent years. This more fully reflects the economic recovery seen outside London, especially in major cities. In fact, official government data shows that housing starts over the last 18 months in Manchester and Birmingham reached highs not seen since before the global financial crisis.

Housebuilders are generally upbeat about the opportunities to build more in the coming years, according to our survey, although the majority feel that meeting the 300,000 target every year will be a stretch.

An increasingly diverse array of tenures now play a vital role in satisfying housing demand, particularly the build-to-rent sector across cities and town centres. There are also increasing opportunities across the sector for joint ventures, working with Registered Providers and Local Councils to provide new homes. As is clear from the survey, alternative methods of construction are also set to have an impact on the sector.

As for future opportunities, housebuilders have their eyes on most parts of the country – as shown in the map on 8.

FIGURE 1
UK housing transactions and policy changes
2007-2018



Source: Knight Frank Research/HMRC

FTB = First-time buyer office at the end of this report

Supply

In 2013, Mark Prisk, the then housing minister, lamented the UK's undersupply of housing and pledged to accelerate building to the fastest rate in more than 20 years.

At the time, housebuilding was in the depths of the post-crisis trough, with just 120,000 new homes being built every year. Hitting 180,000 completions seemed a stretch. However, in the five years since Mr Prisk's remarks, new-build completions have climbed steadily, rising by 55%.

Taking into account conversions and change of use, such as permitted development rights (PDR) – transforming commercial space into homes – the number of dwellings added during 2016-17 stood at 217,350.

Much of the increase can be attributed to an improving economic picture, though continued support for Help to Buy has enabled some buyers to circumvent the 'deposit gap' when buying a home, thereby underpinning confidence among developers to commit to large schemes.

But there is more to do. Ministers are targeting 300,000 additional homes a year by the middle of the next decade – a 38% increase from current levels. Delivery looks set to climb in the short term, and the Office for Budget Responsibility (OBR) has forecast net additions will reach 257,600 this year. Maintaining these levels of housebuilding will be a challenge however. The OBR is forecasting net additional dwellings will plateau at about 240,000 between 2020 and 2023 (FIG 2).

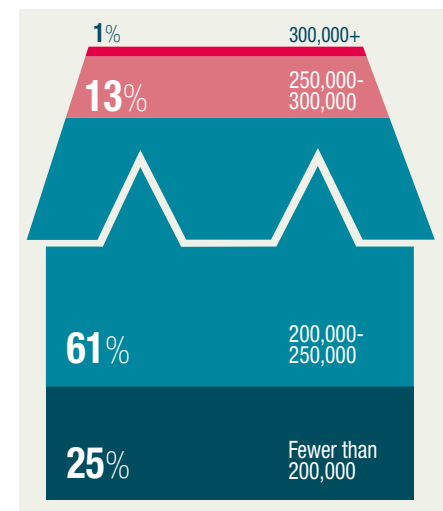
Responses from the housebuilder survey echo this outlook. Some 61% of respondents said between 200,000 and 250,000 net additional homes are achievable and sustainable by 2022, should current market conditions persist.

A quarter believe net supply will be fewer than 200,000, and 13% said levels would reach 250,000-300,000. Only 1% of respondents thought more than 300,000 was achievable by 2022 (FIG 3).

Developers, housing associations and local authorities in England started 163,000 homes in 2016/17 (FIG 4). In terms of their

FIGURE 3

What levels of net supply of housing do you believe will be achievable and sustainable in England on an annual basis by 2022, under current market conditions?

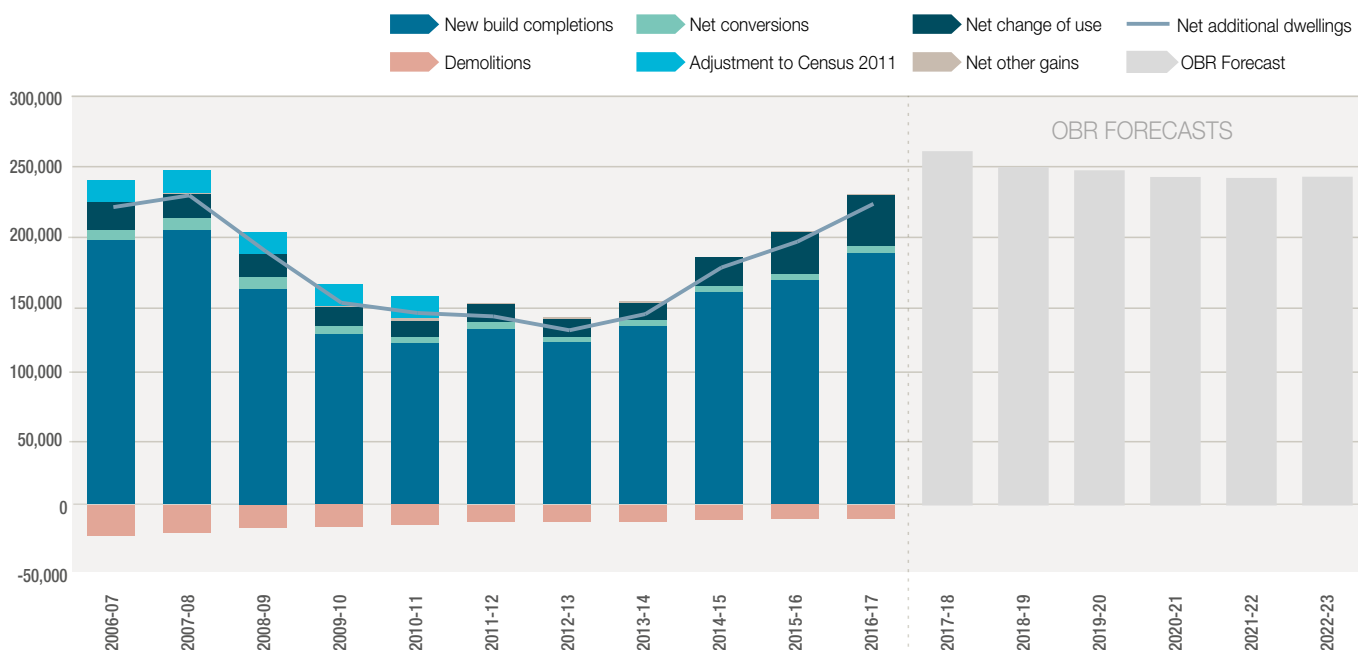


Source: Knight Frank Housebuilder Survey

FIGURE 2

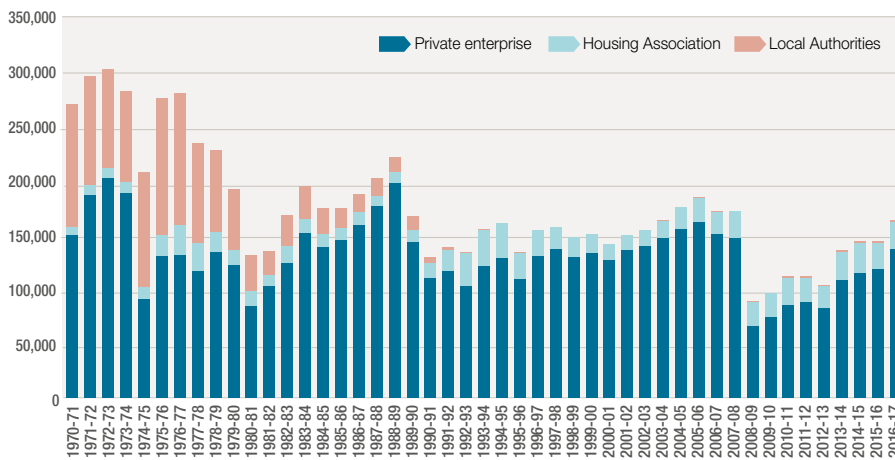
Housing supply

Net additional dwellings, England



Source: Knight Frank Research/MHCLG

FIGURE 4
New-build housing starts, England



Source: Knight Frank Research/DCLG

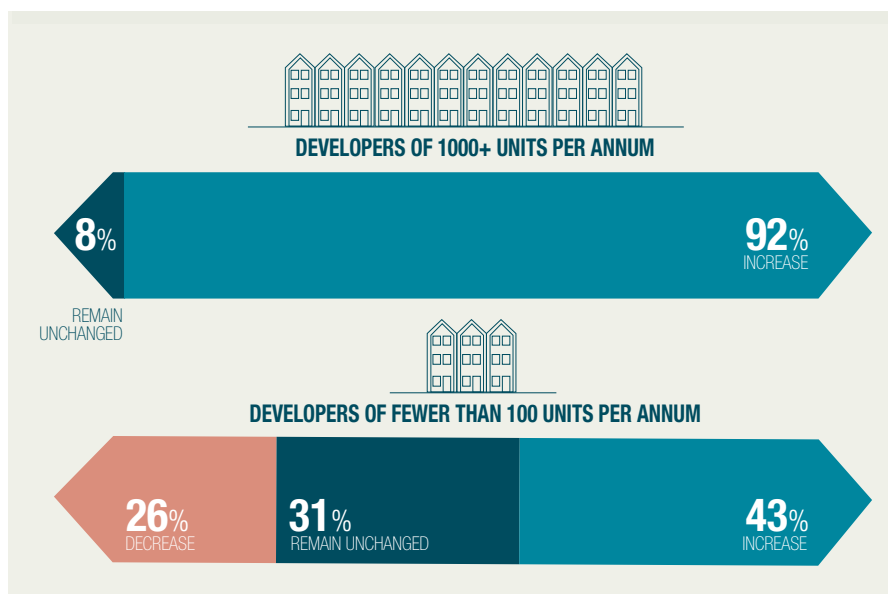
own businesses, 61% of survey respondents said they expected to increase the number of units started during the next 12 months, compared to the previous 12, but that headline figure hides a split between the outlook of larger housebuilders and SMEs.

In recent decades housing supply has become more dependent on a small number of very large developers and, despite an increasingly favourable policy environment for SMEs, responses to the survey suggest most plan to build the same amount of homes or fewer over the coming 12 months.

Developers that build more than 1,000 homes every year overwhelmingly suggested they would be ramping up production during the coming year, with 92% stating that intended to increase starts (FIG 5).

Among developers that produce 100 homes a year or fewer, 43% said they would increase starts during the coming year, while 31% said they would leave production unchanged and 26% said they would start fewer homes.

FIGURE 5
In terms of the activity of your business over the next 12 months, compared to 2017/18, you expect start volumes to...



Source: Knight Frank Housebuilder Survey

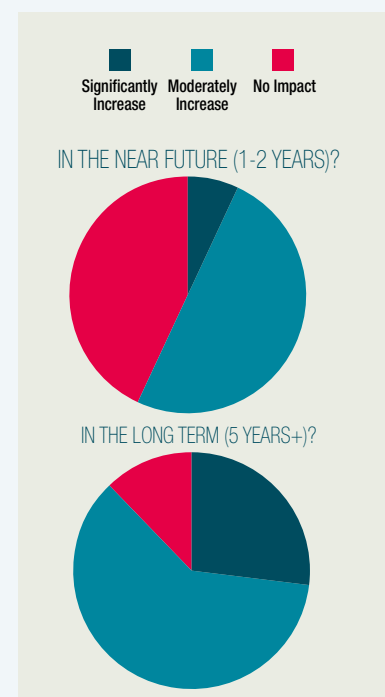
MODULAR

Modular construction has long been hailed as a potential game changer that may help the industry get closer to reaching the government's ambitious construction targets. Impetus on the sector has been further renewed in the past two years prompted by fears of a shortage of skilled construction workers due to Brexit and an aging workforce, and the rising costs of traditional building materials, particularly bricks.

Respondents to the survey were sceptical about the impact modular construction could have on supply in the short-term. Half expected the industry to "moderately" contribute to overall supply, while 43% said it would have no impact on supply at all.

However, the picture changes dramatically when respondents considered the opportunities over the longer term. Nearly nine in ten respondents said it would boost supply in five years' time, with more than a quarter saying it would have a significant impact (FIG 6).

FIGURE 6
What impact do you think modular or pre-manufactured housing will have on supply?



Affordable Housing

Delivery of Affordable Housing has grown in importance both politically and economically as affordability constraints have tightened, particularly in large cities. The number of Affordable Homes built in England in 2015-16 fell to its lowest level in 24 years amid rising private new build completions, before partially recovering to 41,530 the following year (FIG 7).

Unsurprisingly, responses to our survey tallied closely with developer's outlook for private housing starts with 92% of large developers (1000+ units) stating they expected delivery of Affordable Homes to rise during the coming year.

Of developers building 100 homes or fewer, 26% said they expected Affordable Housing delivery to increase, with 54% expecting it to remain unchanged.

The government and the Greater London Authority have sought to increase delivery by making policy changes aimed at reducing the use of viability assessments. In London, Mayor Sadiq Khan introduced a threshold of 35% Affordable Homes that would enable developers to fast-track through the planning system. The intention is to give clarity to developers over what they could pay for land, while simplifying and speeding up the development process.

The draft revised NPPF has followed suit, and is seeking to move away from viability

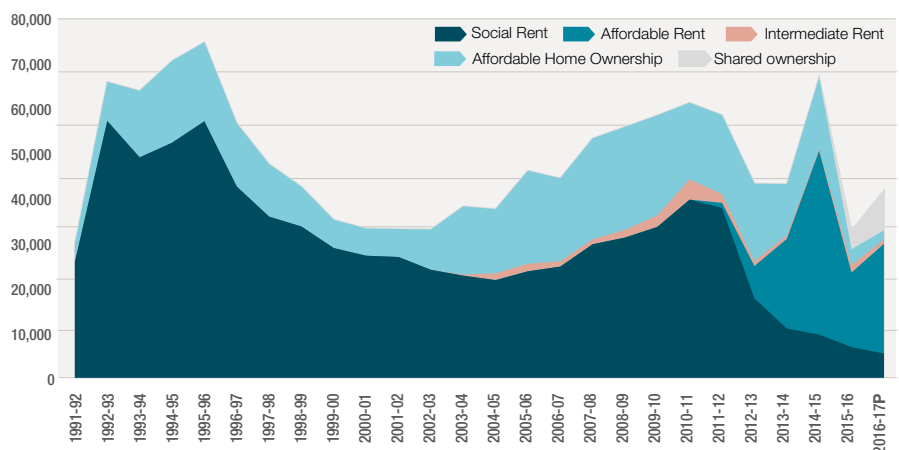
assessments in the decision-making stage of development.

The majority of respondents to the survey, at (55%), said the Mayor's approach could, if applied on a national basis, hinder the delivery of Affordable Homes. Respondents suggested any threshold would need to be set locally, allowing some flexibility where needed, otherwise there was a risk that the overall delivery of Affordable Homes could decrease. Many respondents said it was important that the system maintained some option to negotiate.

Several build-to-rent developers said regional governments would need to be flexible if they hoped to attract a diverse range of tenures. (FIG 8).

We also asked whether developers favoured this threshold approach to Affordable Housing provided the target was set clearly and adhered to. Interestingly, this time most respondents, at 62%, agreed, with many favouring that approach due to its transparency, and the likelihood it would make bidding for land more competitive.

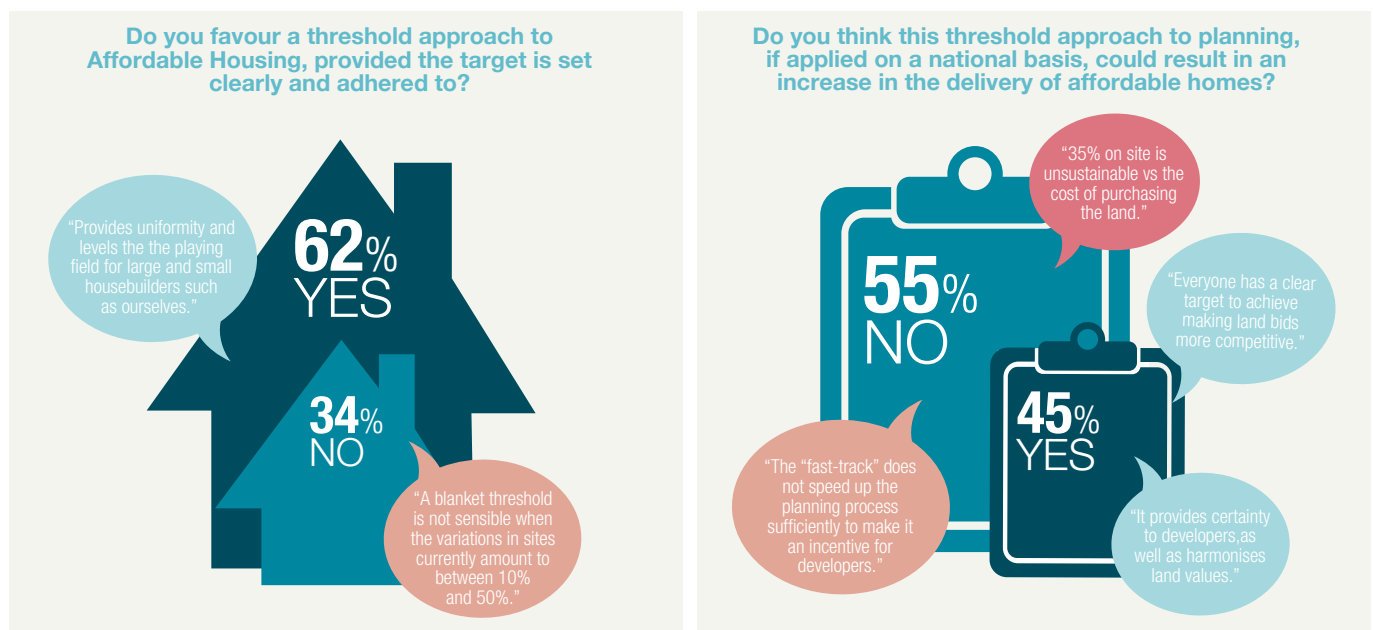
FIGURE 7
Changing mix of Affordable Housing completions



Source: Knight Frank Research/MHCLG. P = provisional

LONDON MAYOR SADIQ KHAN HAS LAUNCHED A "FAST-TRACK" THROUGH PLANNING FOR SCHEMES THAT MEET A 35% THRESHOLD OF AFFORDABLE HOMES.

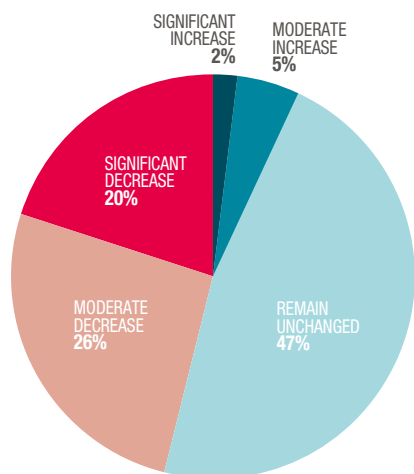
FIGURE 8



QUOTES SHOWN ARE EXAMPLE RESPONSES FROM SURVEY

FIGURE 9

The Help to Buy Equity Loan ends in 2021 and, if current market conditions persist, how will this affect the number of homes your business delivers?



Policy

There have been myriad policy announcements and consultations over the last few years around housebuilding, starting with the publication of the Housing White Paper in February 2017, and including an announcement of a Social Housing Green Paper, a draft revised National Planning Policy Framework, a new draft London plan and a review into UK housebuilding by Sir Oliver Letwin MP.

The results of these different approaches will emerge over the rest of 2018, but perhaps a key policy decision for housebuilders is Help to Buy, and what will happen to the Equity Loan scheme designed to help buyers bridge the 'deposit gap' after it is slated to end in 2021. Since the scheme was introduced in 2013, around 160,000 home buyers have taken out an Equity Loan, with around 80% of these being first-time buyers.

Help to Buy

Nearly half of respondents (46%) said ending the scheme in 2021 would have a negative impact on the supply of homes they were able to deliver, while 47% said that it would have no impact (FIG 9).

More large developers say that the end of the scheme will affect output, with some 85% of developers who deliver 500+ homes a year saying that supply will fall modestly or significantly. In contrast, some 20% of developers delivering up to 100 units a year say that their production levels will fall, with two-thirds (65%) saying their output will remain the same.

FIGURE 11

What do you think should happen to the Help to Buy Equity Loan scheme after 2021?

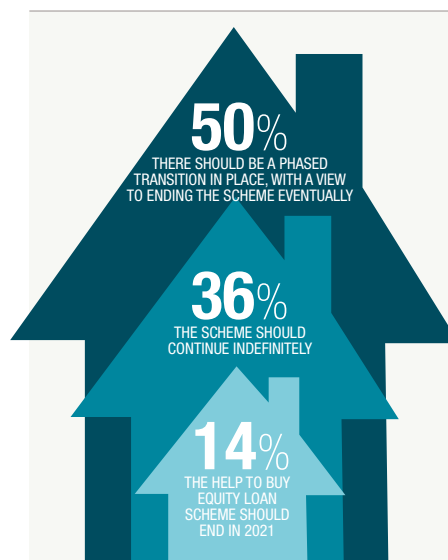
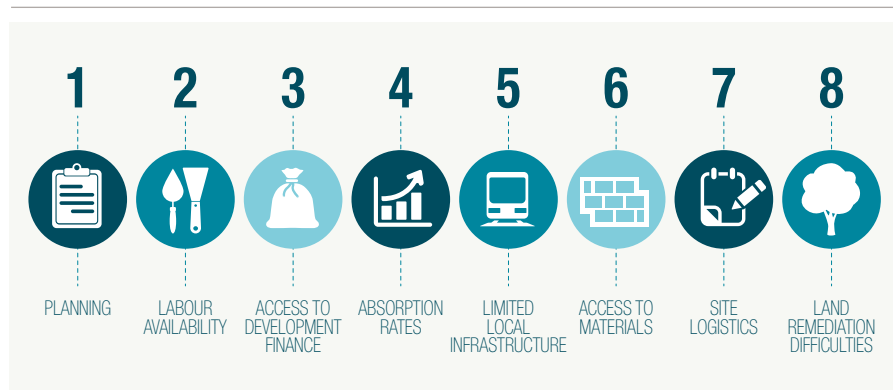


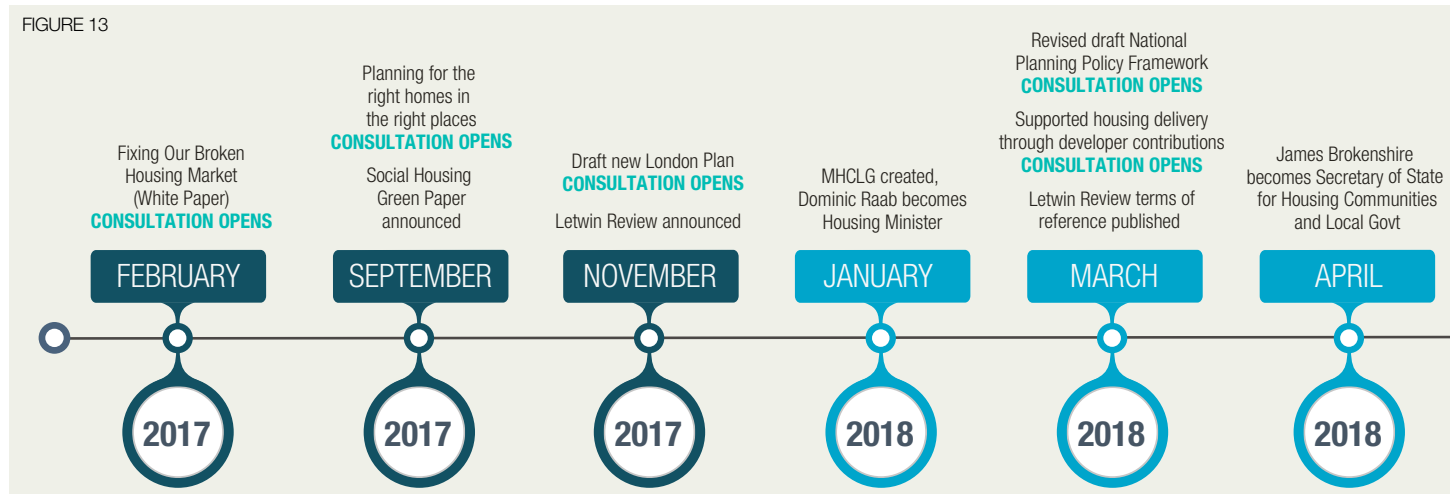
FIGURE 10

What are the key barriers to speeding up delivery?



CONSULTATIONS AND POLICY DEVELOPMENTS

FIGURE 13



The expectation that ending the Help to Buy Equity Loan could affect delivery does not simply translate into a plea for Help to Buy to continue, however. Just over a third of all respondents (36%) to our survey said that the scheme should continue indefinitely (FIG 11). Two-thirds of respondents said the scheme should end, although these were split between those who called for a tapered withdrawal of the scheme (50%) and those who said it should end completely at some point in 2021 (14%).



Whatever ministers decide, they must speak up soon if they are to avoid weighing on the supply of homes. The industry has shown itself capable of adapting to change, but businesses in every sector strain to operate amid policy uncertainty."

JUSTIN GAZE

HEAD OF RESIDENTIAL DEVELOPMENT LAND,
KNIGHT FRANK, ON THE FUTURE
OF HELP TO BUY



Another announcement expected towards the end of the year is the plan drawn up by Sir Oliver Letwin aimed at increasing the speed of housebuilding. His independent review of build out rates was announced at the Autumn Budget in 2017. Since then he has made an initial report and published his draft analysis, in which he explains that there will be a focus on encouraging a range of housing design as well as tenures on sites. While the Letwin Review focuses on challenges after the planning process is complete, when asked about the barriers to speeding up development, our respondents still identified planning issues as the biggest hurdle, with 39% identifying it as the top issue (FIG 10).

However, it is worth noting that in previous years, a much larger proportion of respondents identified planning as a barrier to activity, suggesting that the planning landscape, while still challenging, may be easing.

The future

The performance of the UK property market has shifted during the past 12 months. The north/south divide in terms of house price performance has narrowed, with mainstream markets across the Midlands, South West and Scotland outperforming.

Some of these shifts have been exacerbated by tax changes. Successive changes to stamp duty, for example, have resulted in a significant decline in new projects starting in inner London, since a 2015 peak.

We asked our respondents to list the regions in which they saw the greatest opportunity to

FIGURE 12

What do you perceive are the biggest risks to your business from Brexit?



their business during the next three years. The South East, London zones 3-6 and the West Midlands were picked as the top three hotspots (FIG 14).

Among the volume builders (1000+ units) the South East and West Midlands were picked as the most significant opportunity areas in the coming years.

Respondents to the survey were asked for their opinions on Brexit. The majority said that an uncertain economy was the greatest risk of the process of the UK leaving the EU.

This was followed by labour availability and then access to materials (FIG 12). London-focussed developers are likely to

Local Council Elections
(inc. Mayoral elections
in Hackney, Lewisham,
Watford, Newham &
Tower Hamlets)

Letwin Review draft
analysis published

Revised NPPF due to
come into force

Autumn Budget
Letwin final
Review published

Social Housing
Green Paper

Final London
Plan published

MAY

JUNE

JULY

NOVEMBER

due late 2018

Winter 2019/20

2018

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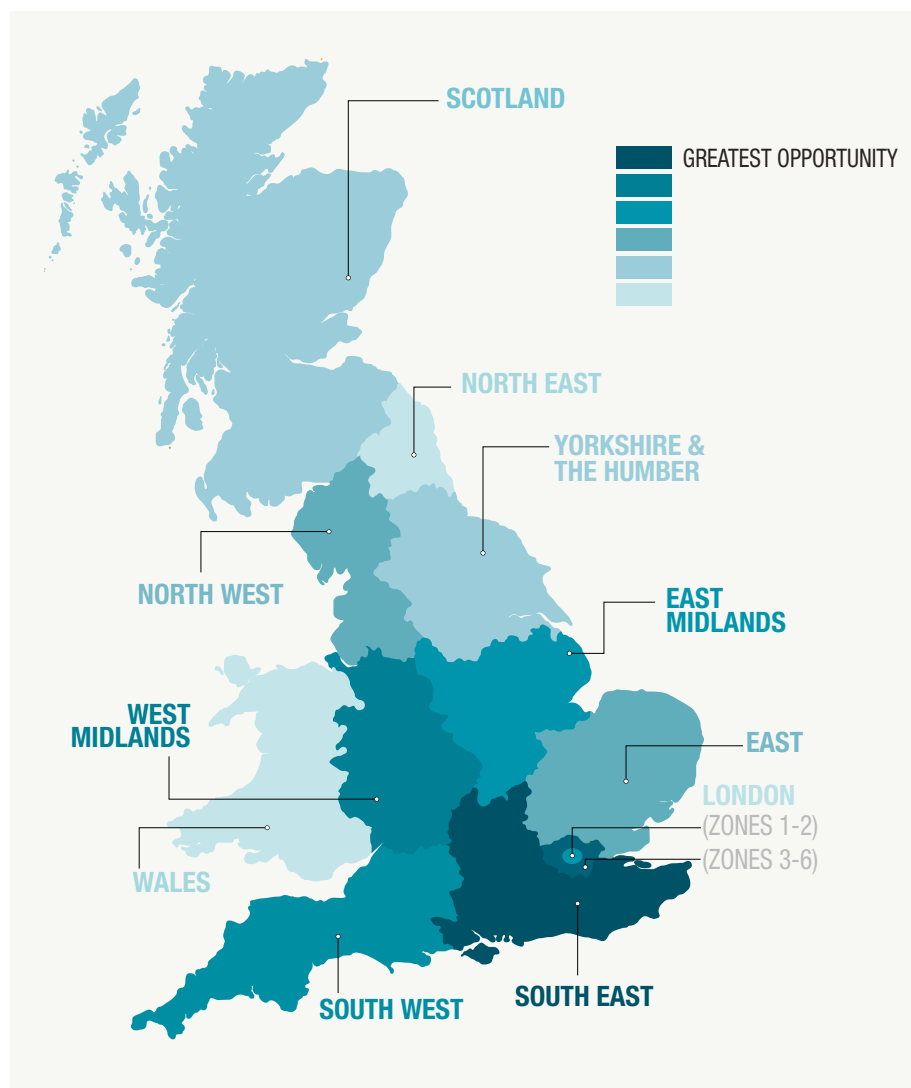
be disproportionately affected by labour availability because more than half of the capital's construction site workforce is from overseas.

In addition, many respondents suggested uncertainty over government. Developers in central London identified uncertainty in Westminster and currency fluctuations affecting investor appetite.

Nationwide, housebuilding looks set increase, particularly on the outskirts of London and across the Midlands, underpinned by more evenly distributed house price growth and high levels of employment in regional cities. However, as identified in the survey, the market is not without its challenges, and continued policy uncertainty has the potential to weigh on output in the coming years.

FIGURE 14

Regions identified by respondents as offering the greatest opportunities for their businesses during the next three years.



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With thanks to Hayfield Homes for the front page image, showing Hayfield Chase, Stratford-Upon-Avon.

Thanks to the survey respondents for their time.

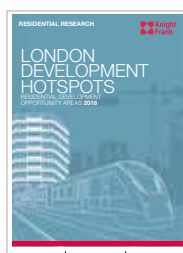
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