

Q2 2022

BUILD TO RENT REPORT

CONTENTS

Single Family Housing

Rental Performance

Build to Rent Investment Volumes

Build to Rent Stock

Build to Rent UK Yields

European Cities Yields

SINGLE FAMILY HOUSING

INTRODUCTION

Institutional investment into the UK rental market has gathered pace over the last decade, with an estimated 230,000 units completed, under construction or in planning. The majority of this has been focused in city centres. According to the BPF, 92% of development has been in urban areas. However, over the last few years we have seen a shift, with a growing number of investors entering the Single Family Housing (SFH) market.

Not all renters live in city centres. The suburban renter population is huge, with nearly two-thirds of UK renters living in rural or suburban locations. This means the market for single family homes is substantial, at an estimated 2.9 million households. This is only going to grow.

DEMAND TRENDS

Growing number of households

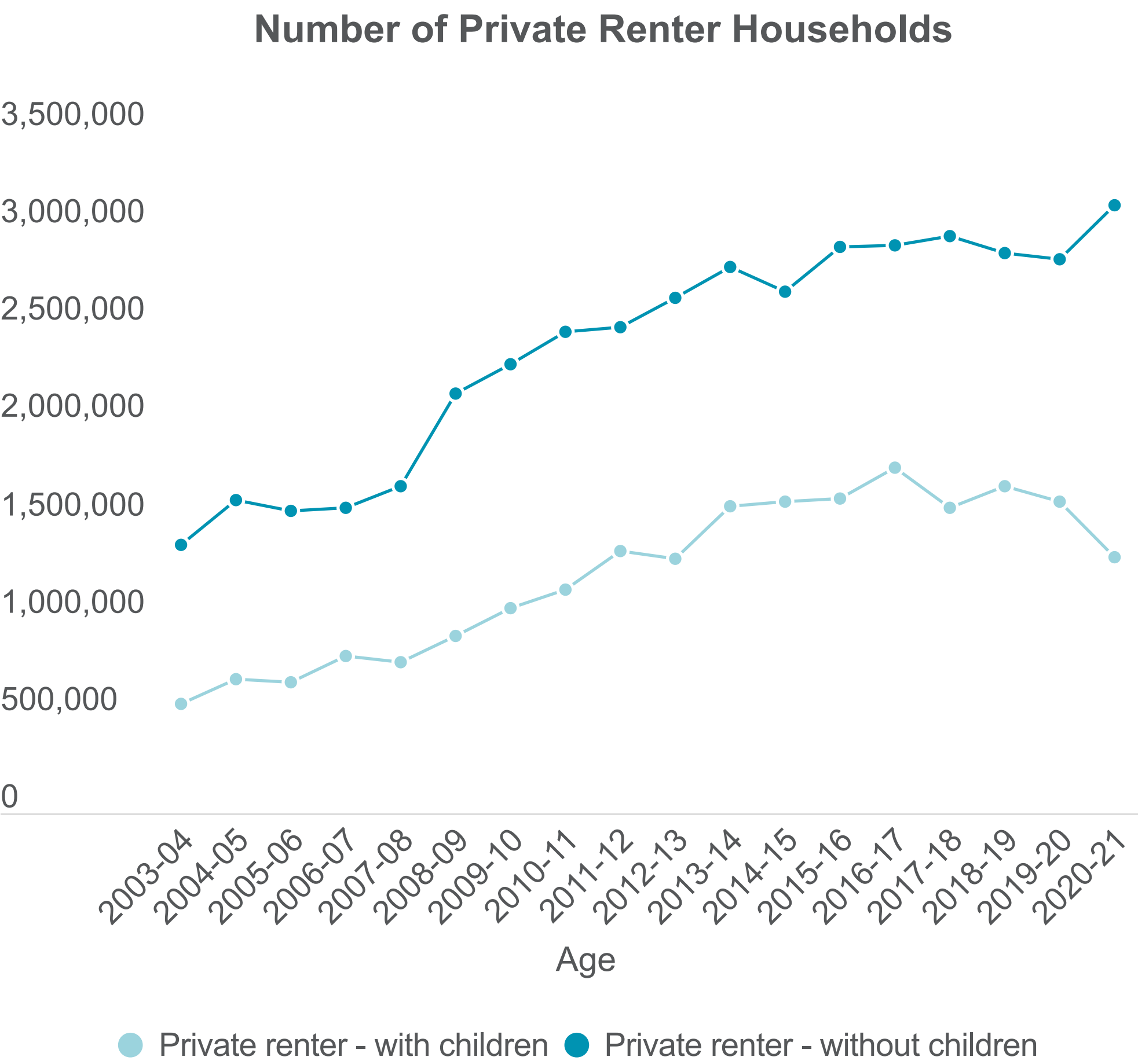
Households have increased from 21.9 million to 24 million over the last 10 years and are forecast to reach 25.3 million by 2031 (ONS). That would be an extra 1.3 million households. If tenure distribution stays the same, with 19% of households living in the private rented sector - which is unlikely given the stretched buyers' affordability - then there will be an additional 248,000 private rented households by 2031. If two thirds live in rural or suburban locations, this takes the total size of the SFH market to an estimated 3.1 million households.

More families are renting

One might make the assumption that the rental market is made up of the younger generation, however this is not the case. The number of families in the private rented sector has been rapidly increasing.

Two parent households (dependent children) in the private rented sector have increased by 15% over the last decade (an additional 105,600 households). This figure is much higher when you look at the ten years prior to the pandemic, when two parent households had grown by 78%. Couples are no longer waiting until they have bought their first home to have children.

Note: English Housing Survey unless otherwise stated



Cushman & Wakefield, English Housing Survey

DEMAND TRENDS CONT.

A far greater proportion of single parent households live in the private rented sector than own their own home. They now represent 11% of the private rented sector, compared with just 3% in the owner occupied market. The number of single parent households (dependent children) increased by 19% over the last decade (an additional 82,100 households), higher than in the ten years prior to the pandemic, where it was 16%. SFH is important to divorcees as it provides flexible and affordable rental options.

It might be assumed that families are more likely to want to live in houses rather than flats (gardens, space and community). However, families are not the only households competing for rental houses. Sigma Capital Simple Life developments are made up of only 43% families (BPF), the rest are sharers, couples, and singles.

Ageing Renter Population

The notion that renters move out of the market in their early 30's and buy a home is a diminishing idea thanks to stretched affordability among buyers'. Renters are getting older. The number of 35-44 year olds who are renters has increased by 21% over the last ten years. The 45-54 year old age group has risen by 50% and the 55-64 year old age group by 111%. An ageing renter population could mean more demand for suburban homes.

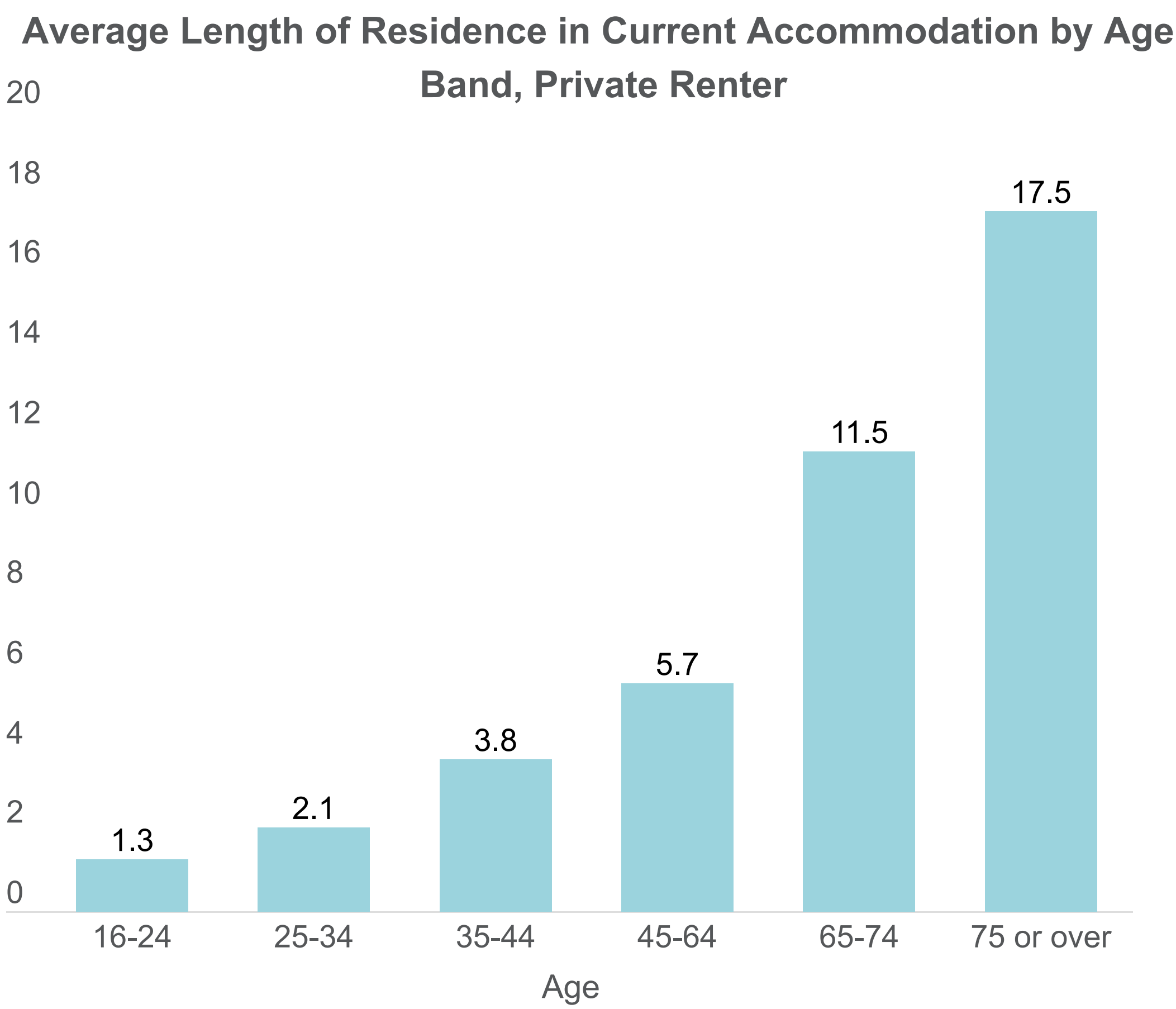
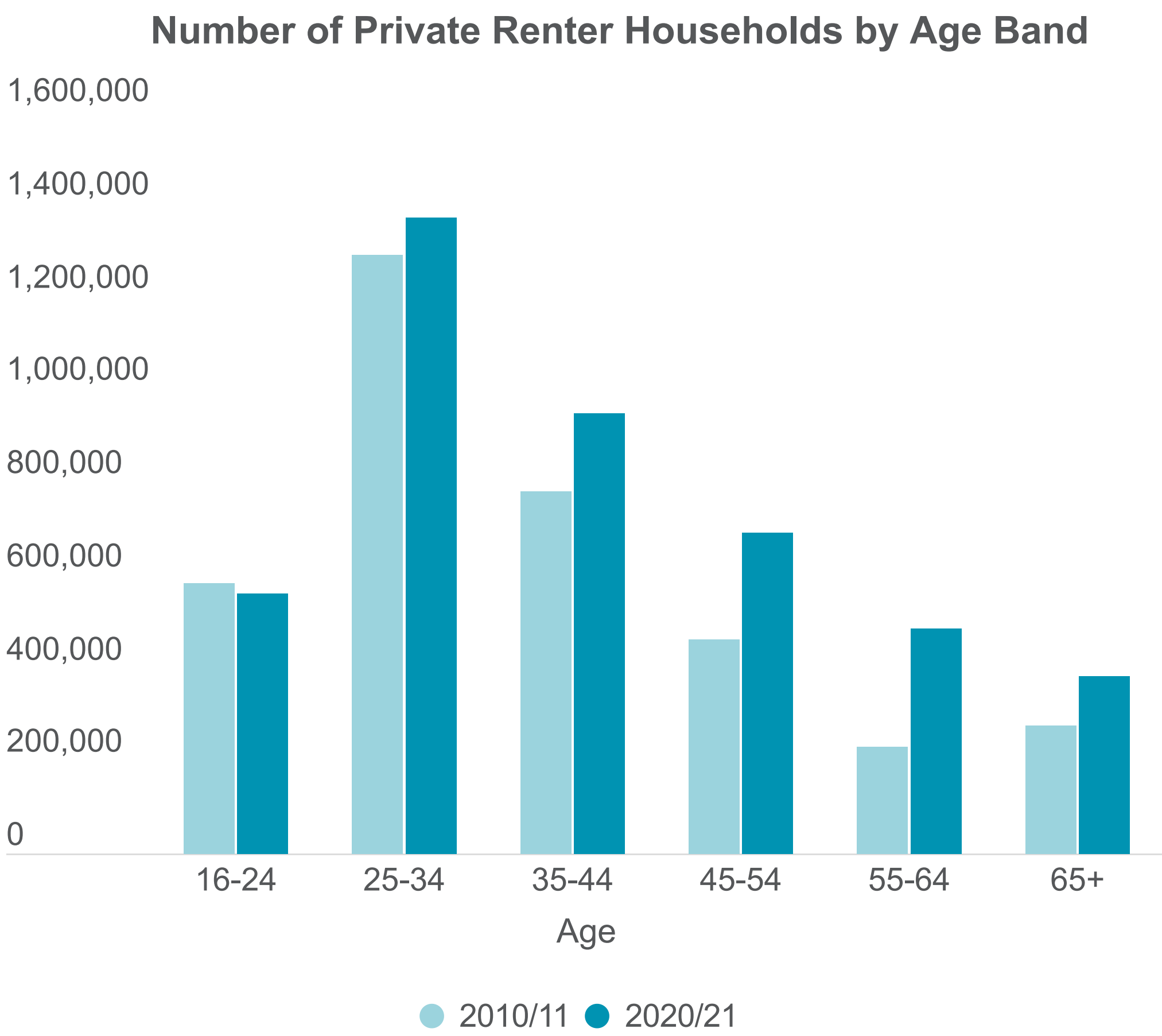
In addition, older renters typically stay in their rental homes longer, meaning lower voids and lower turnover. The average length of stay for a 25-34 year old in their current accommodation is 2.1 years, compared with 3.8 years for 35-44 year olds and 5.7 years for 45-64 year olds.

SUPPLY TRENDS

A longstanding issue in the private rented sector is the imbalance between supply and demand. This has been made worse by stretched buyer affordability. In addition, more Buy to Let landlords are leaving the sector as government policies have made/are making the sector a less attractive proposition.

However, we have seen a huge increase in the number of Build to Rent (BTR) homes being delivered, with 230,000 units now complete, under construction or in planning. This has helped the overall delivery of new homes across the country, and in 2021 accounted for 8% of completions (GOV.UK & BPF). However, as mentioned earlier, the majority of development has focused on urban areas.

Note: English Housing Survey unless otherwise stated. Age based on household reference person



Cushman & Wakefield, English Housing Survey

RATIONALE FOR SINGLE FAMILY HOUSING

Undersupplied market

A shortage of rental stock, growing population and stretched buyer affordability is causing the private rented sector to grow. The private rented sector accounted for 10% of households in 2001, it now accounts for 19%. This is only going to increase.

Low risk asset class

The longstanding imbalance between supply and demand in the rental market creates a low risk asset class. Time and time again the rental market has proven its resilience, the strong pandemic recovery only goes to prove this point. This is particularly the case with suburban houses, especially those at an affordable price point and a popular product; for example three-bed houses.

SFH appeals to older renters and families. As previously mentioned, families and older tenants stay longer, which therefore means lower turnover, fewer voids and less gross-to-net leakage for the investor.

Easier, quicker and cheaper to build

Most investors enter the SFH market at the development stage. Often purchasing homes from housebuilders. Houses are easier, cheaper and faster to build than large blocks of flats. It is also easier to manage build cost risk, especially with the rising cost of construction, particularly with the use of modular construction.

SFH is not as sensitive to location as urban development. Sites with good schools, access to green space and strong local amenities are preferable. Pairing with regeneration schemes can work well.

Phased delivery

Houses can also be delivered in phases, meaning investors can have access to income more quickly, rather than having to wait for a full block of flats to complete.

Delivering units faster appeals to local authorities as it helps them reach their housing targets quicker. It also creates a community in the early stages of regeneration, often helping housebuilder sales further down the line.

Housebuilders on board

Historically investors have been focused on a discount to break up values, however there has been a shift in recent years, with income becoming the most important factor. This has led to prices close to break-up value being achieved. This is very appealing to housebuilders and in turn helps reduce risk; a very attractive proposition given the looming economic headwinds.

Lower operational costs

The cost of managing SFH is lower than urban BTR schemes, especially when houses are grouped together. With the rising cost of goods, as well as labour shortages, this is very favourable. SFH often ends up with lower gross to net and better overall returns.

The nature of SFH means community creation is more organic, households stay for longer and are more embedded in the neighbourhood through schools and local activities.

Yield advantage

SFH yields have compressed over the last few years. The lower SFH yields reflect strong investor appetite and new capital entering the market. With SFH still in its infancy there is a great opportunity to enter the market and benefit from strong yields which are likely to compress further as the sector grows.

SUMMARY

Supply and demand dynamics, along with strong investor rationale, make a very positive case for SFH investment. Investors have been quick to realise the market potential, with key UK and international players entering the field. SFH investor demand is expected to continue to increase, especially as the cost of living hits first-time buyers and the Help to Buy scheme ends in 2023.

A lack of sites is a challenge for investors, but there has been a shift in sentiment from housebuilders who are keen to diversify their exit strategies, and protect their delivery rates long term.

RENTAL PERFORMANCE

RENTAL MARKET OVERVIEW

The UK has seen record inflation, with the UK CPI reaching 9.4% in June 2022. Wage growth continued to lag behind the rising inflation rate in the three months to May 2022, with regular pay showing a 2.8% fall (ONS).

The rising cost of living will put financial pressure on some renters. However, the long-standing imbalance between supply and demand is likely to support rents. The June RICS Residential Market Survey continues to report tenant demand rising and landlord instructions still in decline.

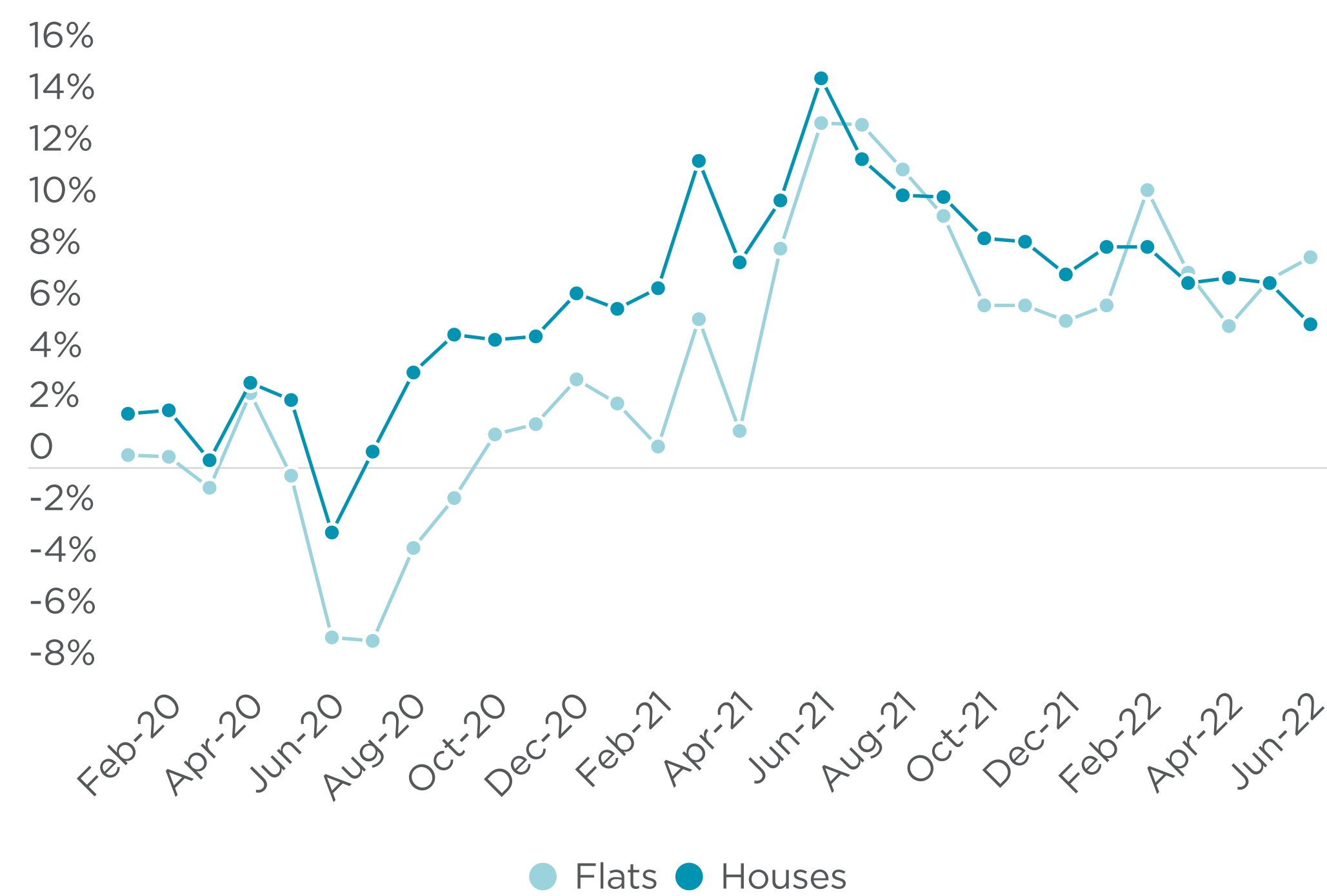
The pandemic demonstrated the resilience of the BTR market as well as other living sectors. Operators reported strong occupancy levels and high levels of rent collection, despite the challenging environment some tenants were facing.

The rental market has recovered well following the pandemic. The average asking rent in the UK is now at £1,153 a month, up 6.7% on June 2021 and 18.6% above pre-pandemic levels (February 2020).

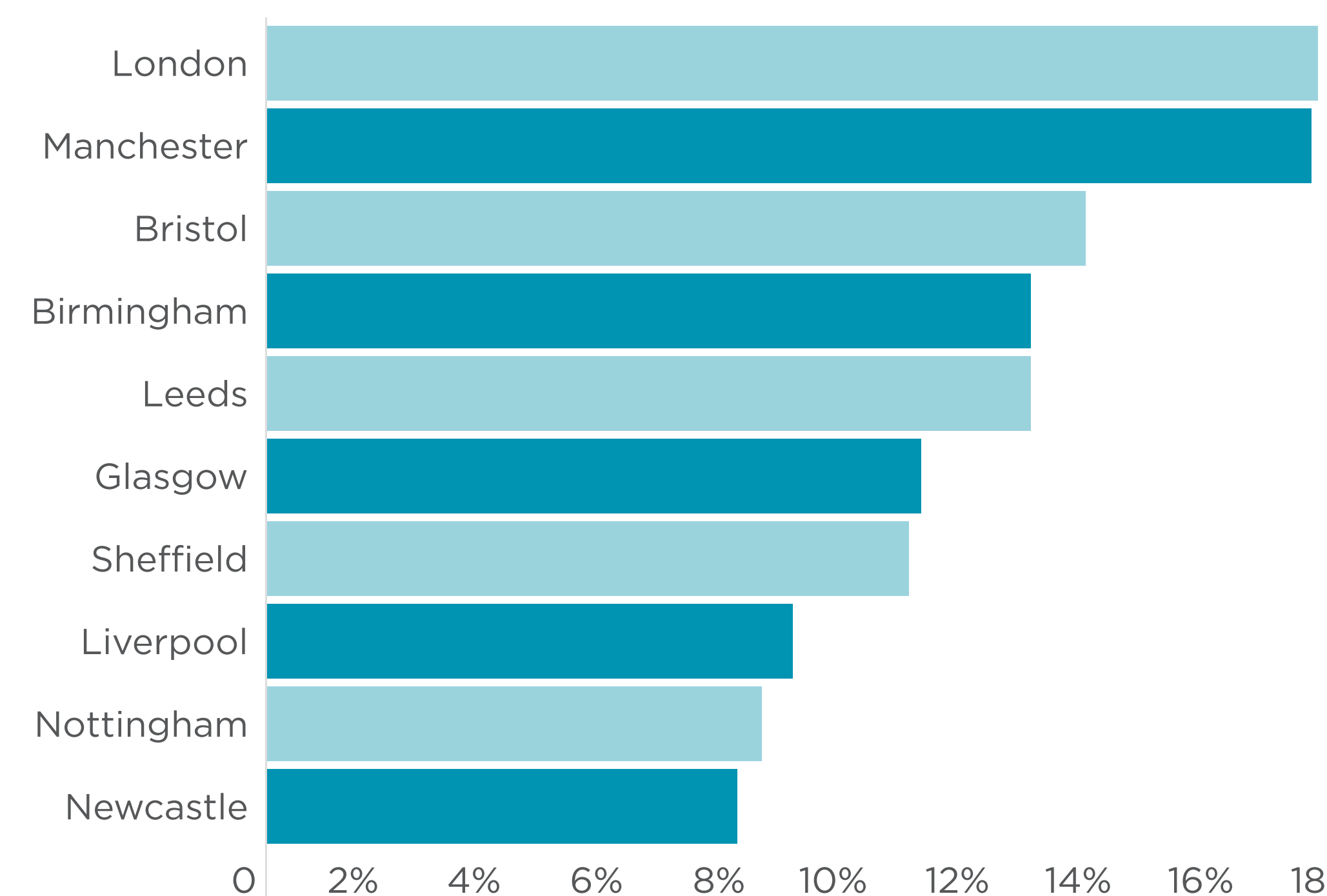
Houses experienced the greatest increase in asking rents since the start of the pandemic, increasing 19.2% between February 2020 and June 2022. Flats weren't far behind with a 16.7% increase.

Rental growth in London had been delayed, but there has been a strong bounce back. Out of the UK's top ten largest cities (by population), London had the greatest annual increase in asking rent, at 17.2%.

UK - Annual Change in Rents



Annual Change in Rents - June 2022



Cushman & Wakefield, Rightmove - asking rents

OUTLOOK

The rising cost of living will cause a financial squeeze for some renters. However, the shortage of rental homes and high levels of tenant demand is likely to keep upward pressure on rents.

With First-Time Buyer affordability being stretched even further with rising mortgage rates and the Help to Buy scheme ending in 2023, we may see the proportion of private renters increase in the medium term.

INVESTMENT VOLUMES

INVESTMENT

Strong investor momentum continued into the second quarter of 2022 with £0.89bn invested.

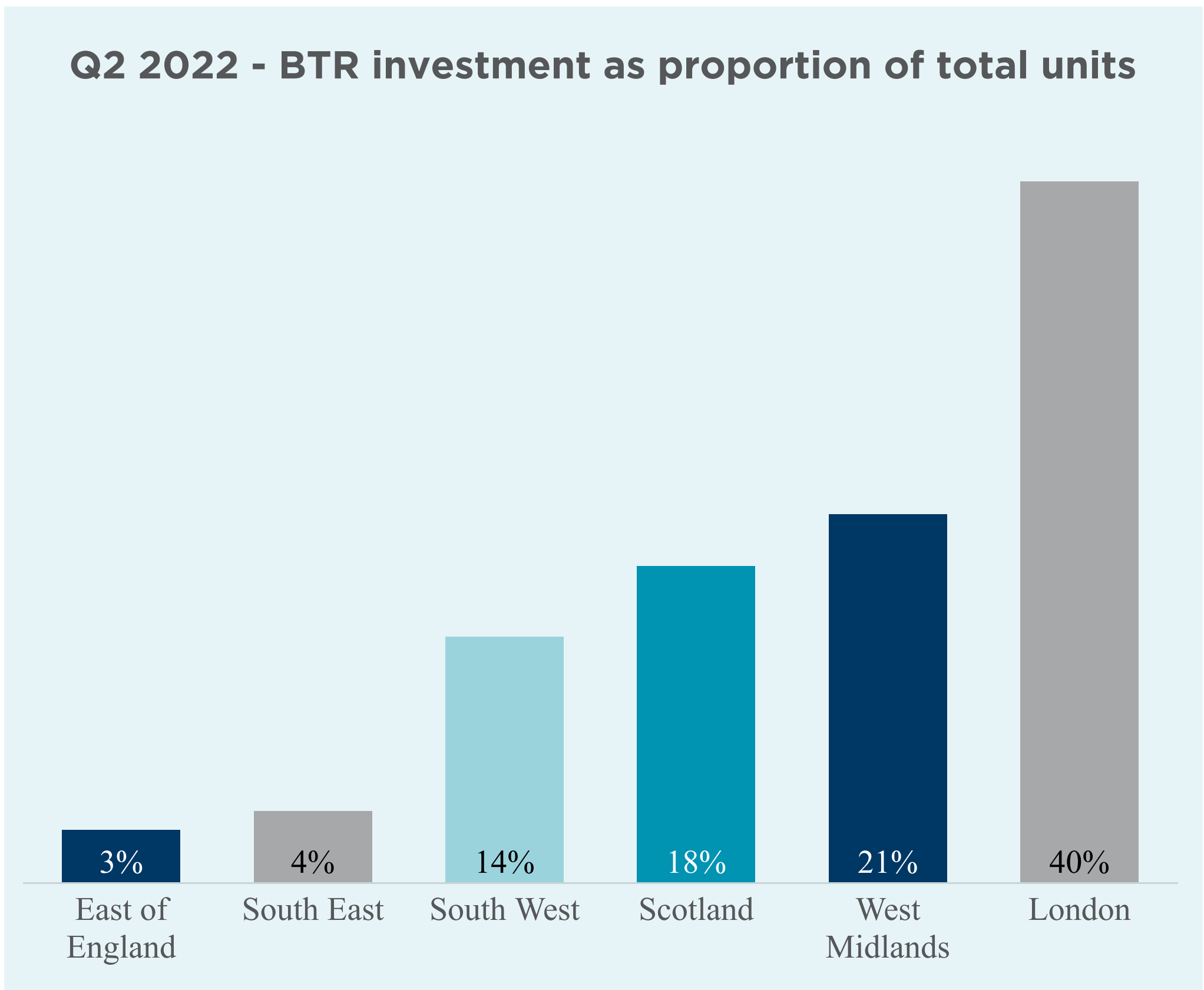
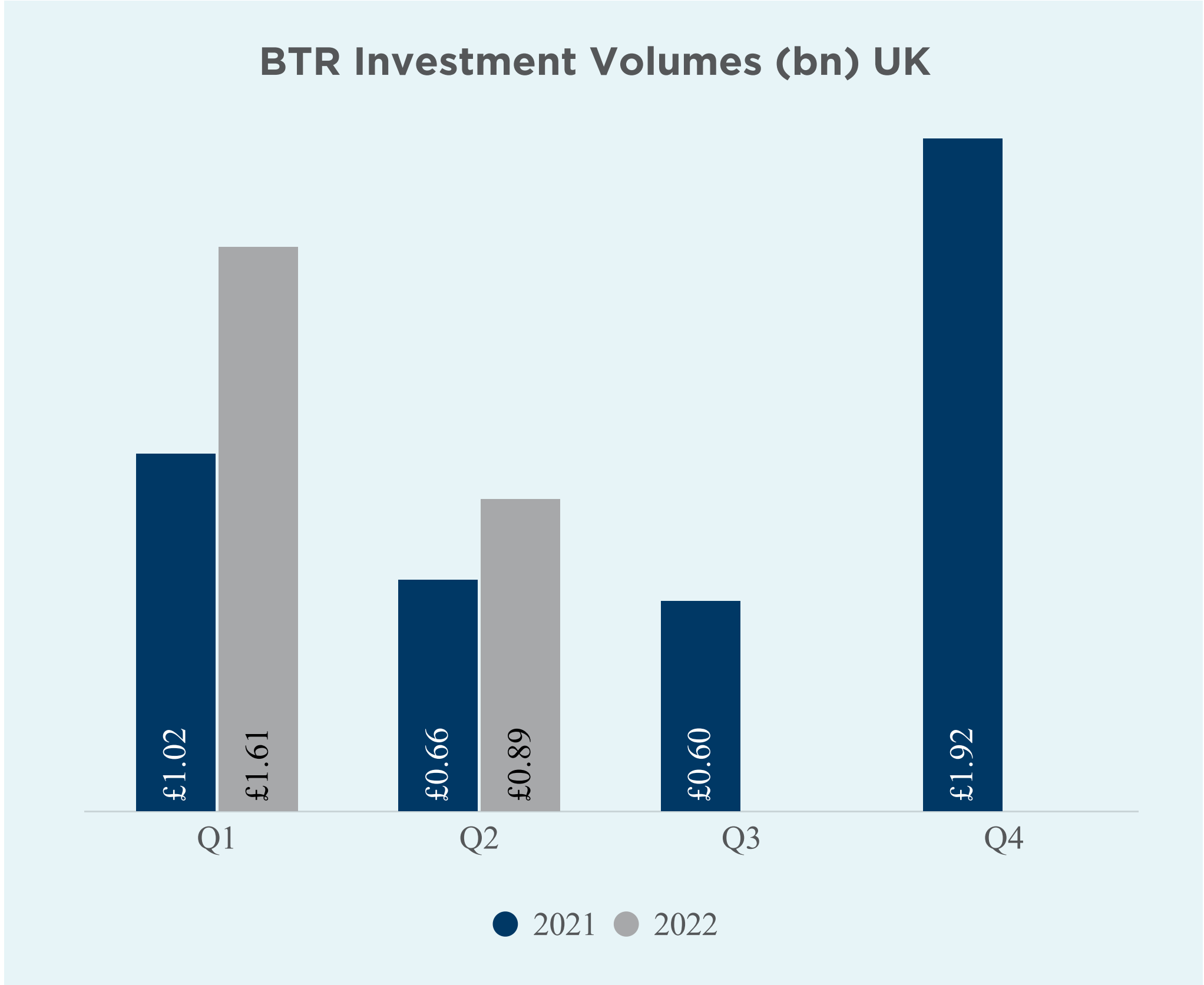
Investment in regional cities continued to thrive, with two of the biggest deals in Birmingham and Bristol.

The largest deal of the quarter was Get Living’s first acquisition in Birmingham. A £136m forward funding deal, Maker’s Yard. The scheme will provide 551 homes and will be built by the developer Watkin Jones.

The second biggest deal was a £128m investment into the Redcliff Quarter development in Bristol by Grainger. The 374 unit scheme forms part of the second phase of the wider masterplan.

The investments made in the second quarter of 2022 translate to an estimated 2,800 units. Despite the two largest deals being in the regions, London still had the highest proportion of units (40%).

Pictet and Pinnacle, together, successfully purchased A2Dominion’s Vida in Battersea for £60m, brokered by Cushman & Wakefield Residential Capital Markets team. An operational, 102 unit scheme. As the BTR sector continues to mature, particularly in London, more operational BTR deals are expected.



Cushman & Wakefield, Real Capital Analytics

BUILD TO RENT STOCK

BTR DELIVERY

Single Family Housing Stock

There are now 230,000 BTR homes under construction, in planning or completed in the UK. 18,000 of those units (8%) are in suburban locations. That figure is likely to be higher, as SFH deals with housebuilders tend to switch tenure further down the line.

SFH is often a mixed typology. Schemes are predominantly houses, but some sites include low rise flats. A mix of flats and houses allows for a higher density scheme to be delivered; this appeals to local authorities, helping them reach housing targets. It also meets the needs of the mixed household types living in SFH.

Size of BTR Schemes

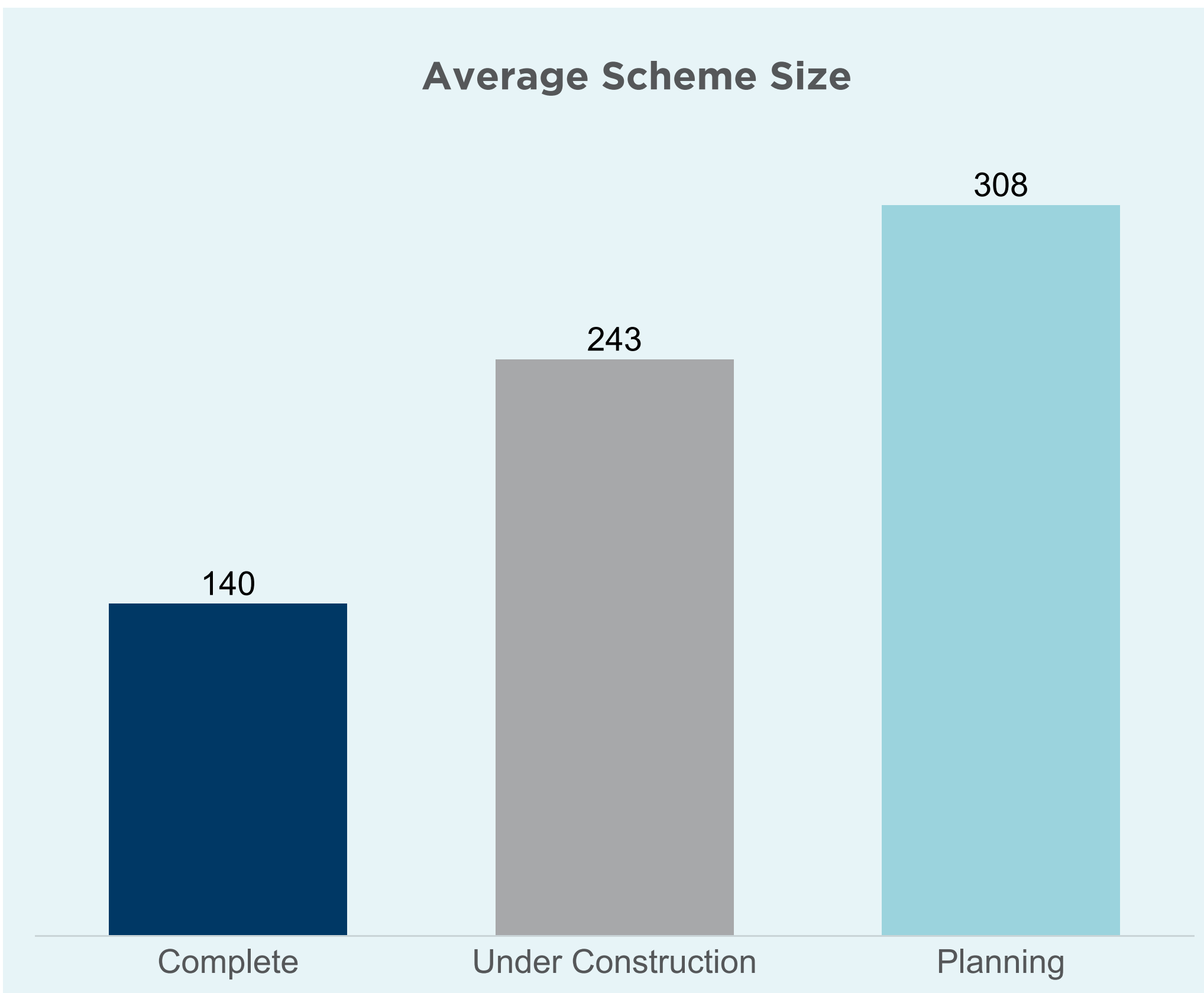
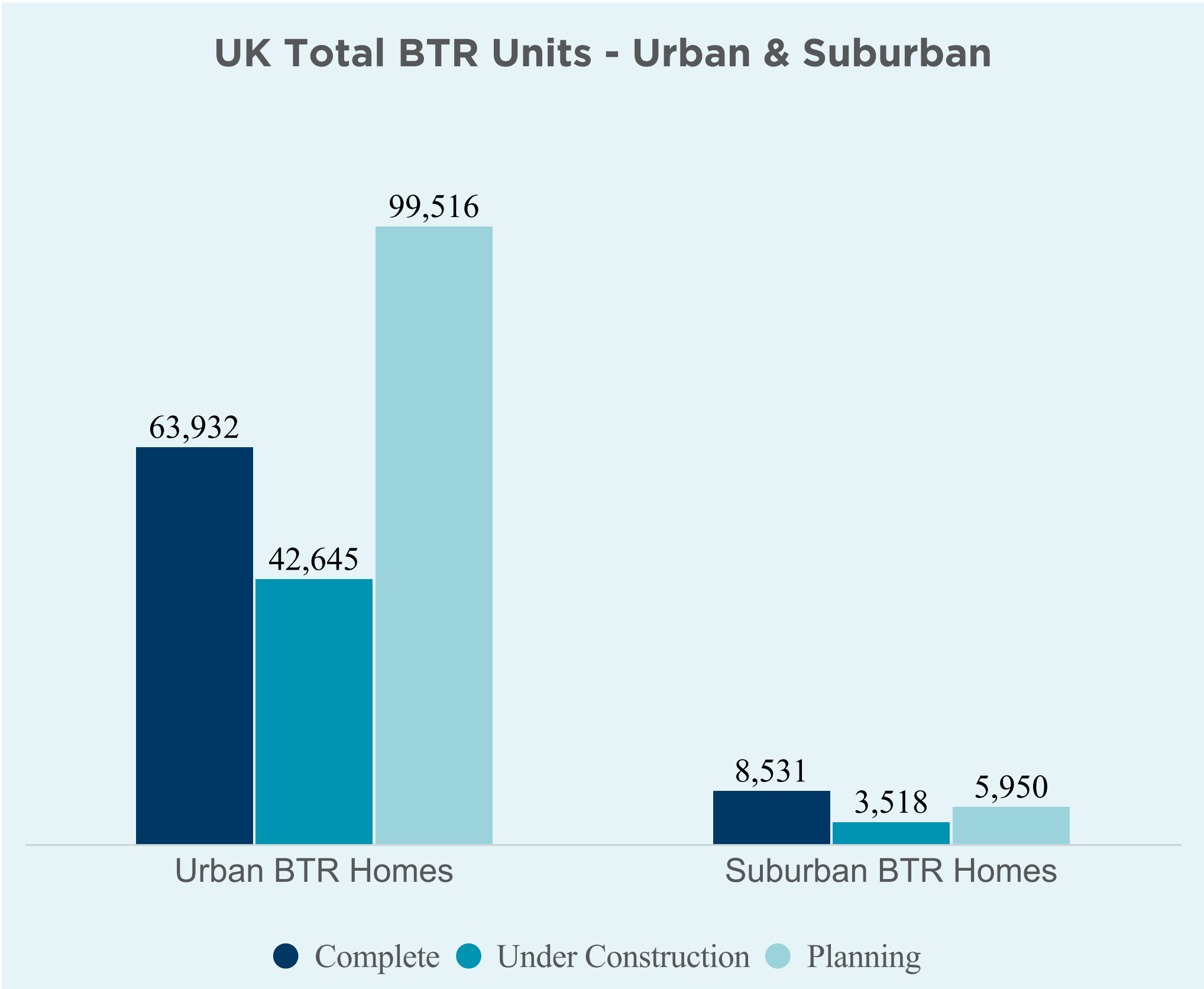
There has been a big shift in the size of BTR schemes being delivered. Investors and developers are more confident, having witnessed the success of BTR over the last few years. BTR schemes in planning now on average have 308 units. This is much larger than the first generation of BTR schemes - which have already been completed - with an average of 140 units.

Type of BTR Products

As well as a shift in size, there has also been a change in the type of product being delivered. The UK BTR market has focused on highly amenitised schemes, which have and continue to meet the needs of city professionals. The mid-market is now blossoming, which will provide renters with a serviced, secure, and affordable rental option.

Co-living

Previously co-living has struggled in the UK market. However, there has been a shift in attitudes. Local Authorities are becoming more relaxed about co-living, understanding that the product does deliver high quality and well sized units. Hopefully in the future, a planning use class will be assigned to co-living, this will make the planning and delivery process much smoother.



Cushman & Wakefield, BPF Quarterly Build-to-Rent statistics

STABILISED BTR YIELDS



High levels of investor demand has caused yields to compress over the last year. Regional cities and SFH have led the way, as investors look to diversify their BTR portfolios and chase stronger returns than in London, whilst also gaining greater confidence in these markets through proven rental growth and tenant demand for operating assets.

As shown in our European yield tracker, UK BTR continues to provide higher returns than many other markets, whilst limited opportunities have driven competition for assets, especially from institutions with low costs of capital.

Yields remained stable in Q2 2022, unlike other asset classes dominated by geared overseas investors. The market is therefore more insulated to the volatility around the cost of debt for the moment. Economic headwinds, geopolitical uncertainty and the cost of debt will be closely watched for any impact on pricing in H2, but in the longer term, the underlying strength of the occupational markets will continue to drive investment, along with the continued requirement to diversify commercially weighted portfolios.

LEWIS SMITH - PARTNER
BTR FUNDING & DEVELOPMENT

4.25%
LONDON CO-LIVING

4.75%
REGIONAL CO-LIVING

4.0%
TIER 1 REGIONAL CITIES BTR

4.5%
TIER 2 REGIONAL CITIES BTR

EUROPEAN CITIES

CUSHMAN & WAKEFIELD RENTAL INDEX

		March 2022		June 2022		Yield Trend
		Net Initial Yield	Cap Value psf	Net Initial Yield	Cap Value psf	
Austria	Vienna	3.00%	€ 461	3.00%	€ 461	-
Belgium	Brussels	3.25%	€ 314	3.25%	€ 314	-
Czech Republic	Prague	4.10%	€ 302	4.10%	€ 302	-
Denmark	Copenhagen	3.00%	€ 801	3.00%	€ 801	-
Finland	Helsinki	2.95%	€ 879	2.95%	€ 879	-
France	Paris	2.00%	€ 1,561	3.00%	€ 1,041	↑
Germany	Berlin	2.40%	€ 905	2.70%	€ 804	↑
Germany	Frankfurt	2.80%	€ 880	2.80%	€ 880	-
Germany	Hamburg	2.48%	€ 850	2.35%	€ 1,008	↓
Germany	Munich	2.00%	€ 1,481	2.00%	€ 1,481	-
Ireland	Dublin	3.70%	€ 874	3.70%	€ 874	-
Italy	Milan	3.00%	€ 421	3.00%	€ 737	-
Italy	Rome	3.50%	€ 282	3.25%	€ 535	↓
Netherlands	Amsterdam	2.95%	€ 704	2.95%	€ 704	-
Norway	Oslo	2.50%	€ 1,133	2.75%	€ 1,043	↑
Poland	Warsaw	4.70%	€ 326	4.70%	€ 391	-
Portugal	Lisbon	4.00%	€ 305	4.00%	€ 305	-
Spain	Barcelona	2.90%	€ 641	2.90%	€ 641	-
Spain	Madrid	2.60%	€ 715	2.60%	€ 715	-
Sweden	Göteborg	2.95%	€ 607	2.95%	€ 607	-
Sweden	Malmö	3.05%	€ 558	3.05%	€ 558	-
Sweden	Stockholm	2.75%	€ 700	2.75%	€ 700	-
Switzerland	Geneva	2.40%	€ 1,466	2.40%	€ 1,466	-
Switzerland	Zurich	2.00%	€ 2,209	2.00%	€ 2,209	-
UK	Edinburgh	4.25%	€ 564	4.25%	€ 564	-
UK	London	3.25%	€ 1,230	3.25%	€ 1,230	-
UK	Manchester	3.90%	€ 502	3.90%	€ 502	-

Cushman & Wakefield prime PRS properties

Paris, Berlin and Oslo reported a rise in yields in Q2 2022. All these markets had yields of 2.5% or below in Q1 2022. With rising interest rates it was inevitable they were going to be pushed out.

The UK continues to offer attractive residential yields in comparison to other European cities and investor momentum remained strong in the first half of 2022.

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