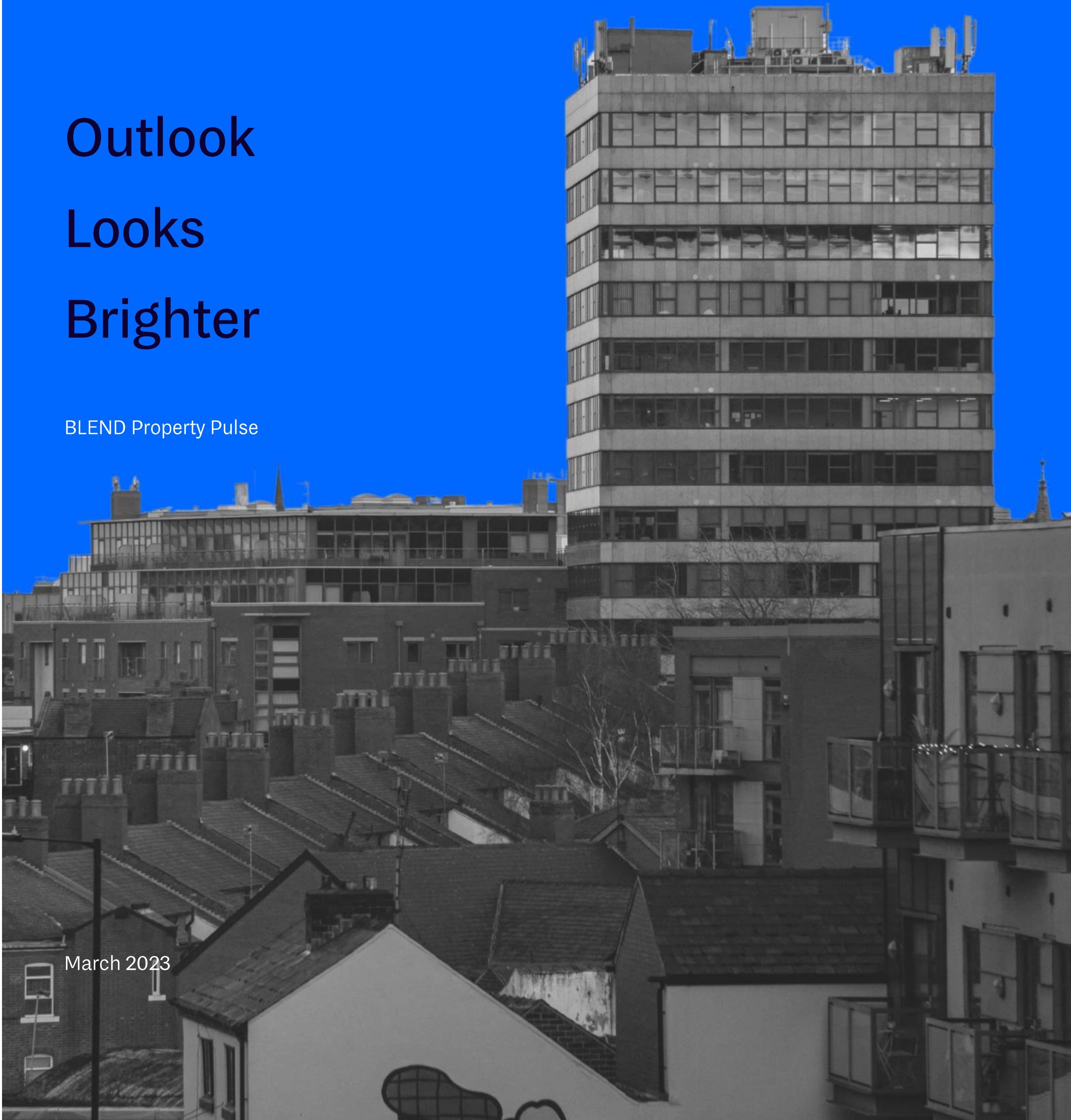
BLEND

Outlook Looks Brighter

BLEND Property Pulse



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Author
ROXANA MOHAMMADIAN-MOLINA

01 MIXED SIGNALS

Sentiment is becoming more balanced

The market remains subdued and transaction volumes of any quality are still relatively low. That being said, the outlook looks brighter than it was at the back end of last year and prices in most markets to date seem to have held up contrary to most economic forecasts. Limited stock supply appears to be the main driver of this meaning that competition for good quality available stock is buoyant and sellers are still achieving reasonable exit values.

This improvement in sentiment comes after a speech by Bank of England governor, Andrew Bailey, earlier this week was interpreted as signalling that interest rates may have peaked after 10 successive increases since December 2021 and that the BoE is intending to call time on its hiking cycle as soon as it feasibly can[i].

Lenders still cautious

On the lending side, liquidity is still there, and the majority of the banks and non-bank lenders remain keen to transact albeit at varying risk appetites. Focus appears to be on servicing existing portfolios and guarding existing relationships over farming new business and growing lending books.

Now, more than ever, is the time for 'Know Your Customer'/'Know Your Lender'. Deliverability and certainty of funding are key in an uncertain time.

Not out of the woods yet...

While prices have so far held up much better than initially feared by many forecasters at the start of Q4 last year, concerns remain and we are unlikely to be out of the woods yet. According to the latest edition of Nationwide House Price Index published last week[II], house prices were down by 1.1% year-on-year in February - the first annual decline since June 2020 and the weakest since November 2012 (Exhibit 1).

Compared to their peak last August, the price of the average UK home is now down by £16k, pretty much equivalent to the price rise we saw during the pandemic. The latest Bank of England figures last week showed UK mortgage approvals fell in January to their lowest since 2009 excluding the Covid-19 pandemic period, with net mortgage lending to individuals decreasing to £2.5 billion from £3.1 billion in December.

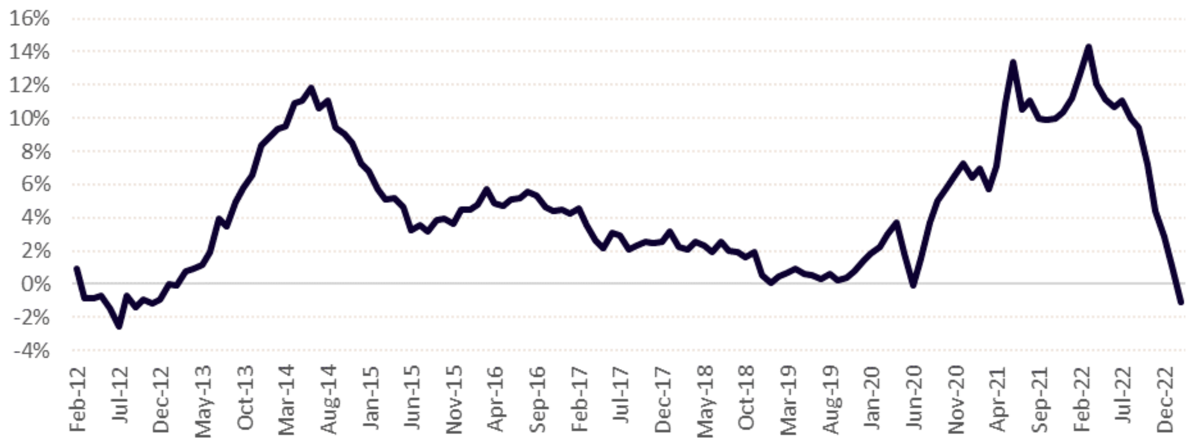
Net mortgage approvals fell for a fifth consecutive month to 39,600, the lowest since January 2009 excluding the pandemic era in which the housing market came to a standstill.

We remain positive and believe that lack of supply will keep prices well supported. According to a recent study published by the Home Builders Federation last month, after a decade of positive growth in housing supply figures, the forthcoming months and years look less positive for the homebuilding industry, due to a culmination of political and legislative decisions and interventions by Natural England.

HBF estimate that housing supply could drop by up to 122,000 homes per year due to proposed changes to the NPPF (77,000 homes a year), nutrient neutrality requirements (37,000 to 41,000 homes a year), water neutrality (1,500 to 1,900 homes a year) and recreational Impact Zones (1,200 to 2,100 homes a year).

Exhibit 1

Year-on-Year change in UK house prices (2012-2023)



Source: Nationwide House Price Index, Blend

02 LAND PRICES IN FOCUS

Land prices have started to adjust...

According to Knight Frank[III], a slowdown in the private sales market and higher financing costs in the wake of September's mini budget started to put downwards pressure on residential development land values in the final three months of last year. UK greenfield and urban brownfield values declined on average by 3.5% and 8.5% in Q4 2022, taking the annual cumulative change to -1.3% and -9.2% respectively (Exhibit 2). In prime central London, an ongoing scarcity of sites for sale meant values bucked the national trend and were flat on a quarterly basis and up by 2.5% annually. We believe a lot more correction is needed in light of the current economic slowdown.

...but are still excessively high

Our conversations with developers reveal that from their perspective, the ever-present issue remains the fact that land prices are still too high and have failed to adjust to the changing economic climate. Profit margins on open market consented sites remain depressed and developers and funders alike are simply failing to make deals work at these elevated levels.

As build costs have risen so steeply over the past 18 months or so and the interest rate environment has followed suit, the deals that priced off appraisals from some months ago simply no longer work.

With little to no sales price growth forecasts for the next 18 months, now is the time for intelligent, well-executed acquisitions whereby value can be locked in at an early stage either via planning gain or via enhancement to the existing scheme.

As development finance lenders and funding partner to many mid-sized developers, we have seen plenty of anecdotal evidences in the market of late which backs up the general sentiment echoed above. It looks increasingly evident that cash and/or a reliable funding partners are key to making the most of opportunities that will arise over the next few months.

Shortage of land

Despite the recent correction in land values and more that is expected to materialise, shortage of residential development land has underpinned prices across the UK in recent years (also evidenced in Exhibit 2).

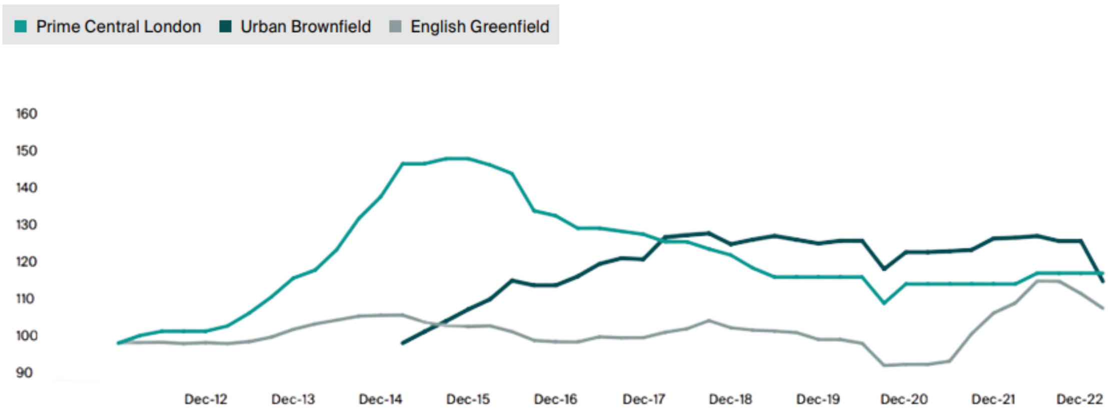
Such lack of supply has long frustrated housebuilders, especially SME developers. Ultra-low interest rates in recent years has meant that land was cheap to hold, enabling many landowners to sit tight.

That's likely to change in the months ahead. According to Knight Frank[IV], the natural pressure created on landowners through an increase in hold costs via increasing interest rates should shake the tree in terms of land supply and allow for a more fluid and liquid land market in the months ahead.

Exhibit 2

Residential development land prices

Index rebased 100 = Sep 2011 (Urban Brownfield = Dec 2014)



Source: Knight Frank Research, Blend

03 THE SHORCUT SMART STATISTICS

-9.2%

Land Value Correction

According to Knight Frank[V], urban brownfield development land values declined by 9.2% year-on-year last year. Greenfield development land values also declined by 1.3% YoY in the same period.

122,000

Declining Supply

The Home Builders Federation estimates housing supply could drop by up to 122k homes per year due to a culmination of political and legislative decisions and interventions by Natural England[VI].

-1.1%

House Price Decline

UK house prices fell by 1.1% annually in February, their first annual decline since June 2020 and the sharpest contraction since November 2012, according to data by the Nationwide House Price Index[VII].

AUTHOR

BLEND is a specialist development finance lender providing experienced property developers with development finance and bridging loans of up to £10m. For more information, please visit www.blendnetwork.com or email your enquiry to our team at: enquiries@blendnetwork.com.

ROXANA MOHAMMADIAN-MOLINA
Chief Strategy Officer at Blend

(+44) 020 3409 3300

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