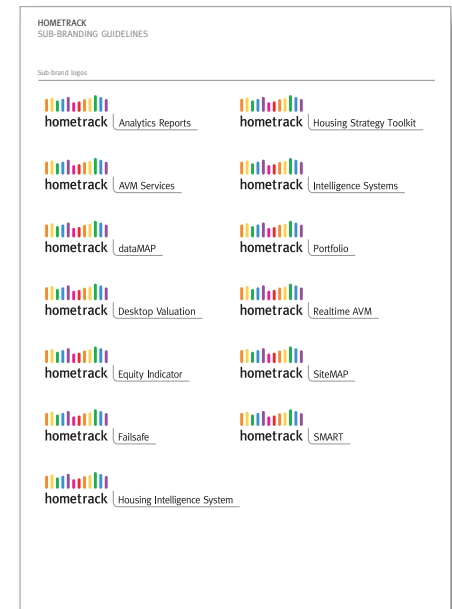
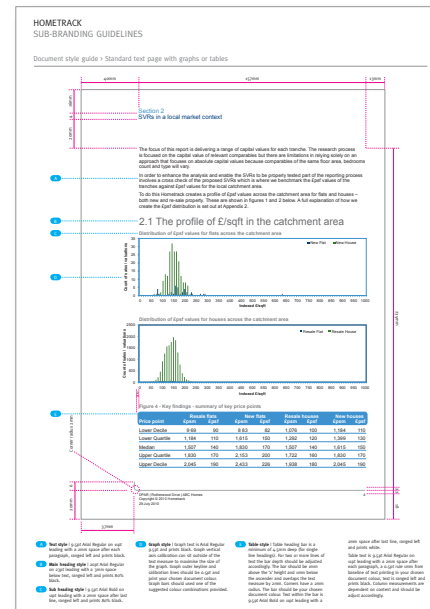
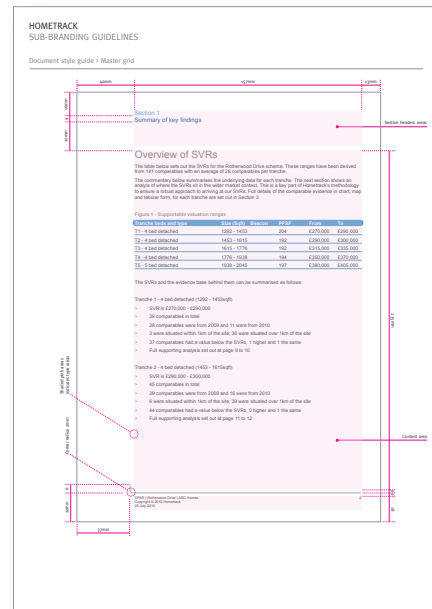
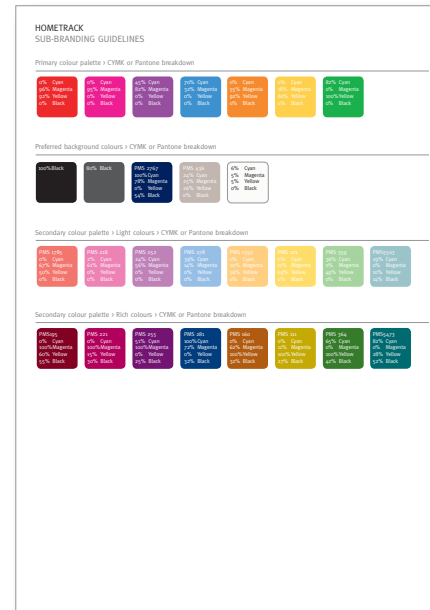
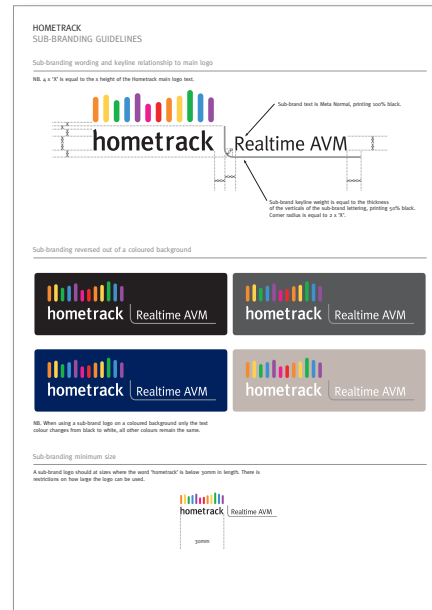
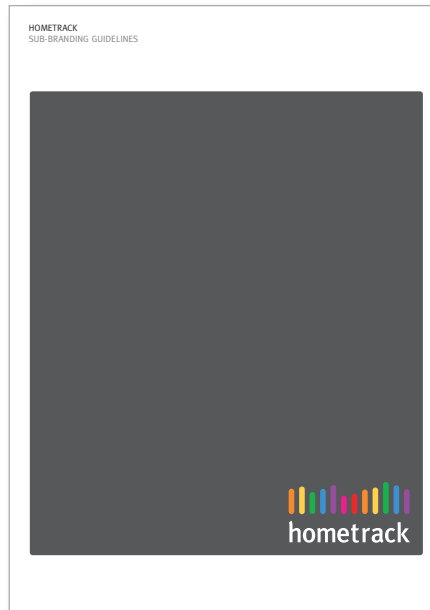
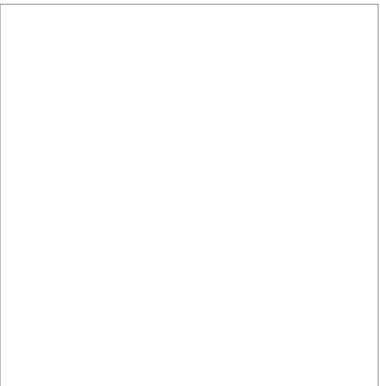
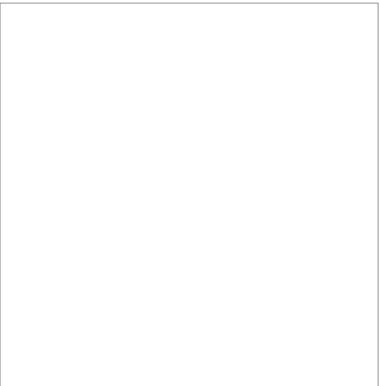
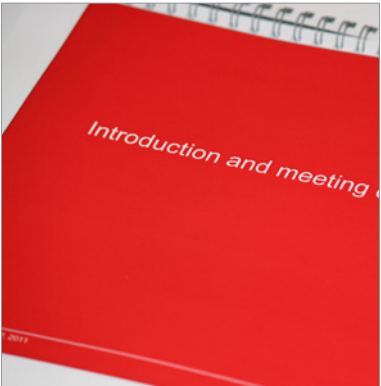
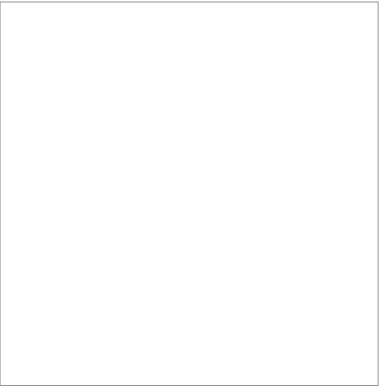
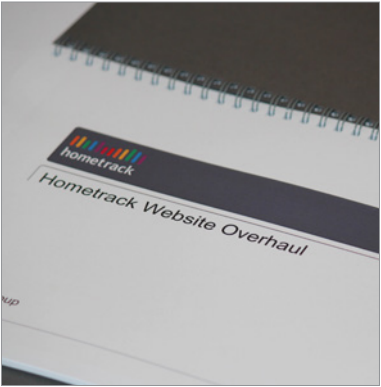


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Insight paper | April 2012

## The rental market – behind the headlines

Richard Donnell, Director of Research, Hometrack

Private rents are rising on the back of growing tenant demand and static supply but the profile of growth varies across markets. With little sign of any material improvement in mortgage availability, rental demand is set to remain strong. The appetite for investing also remains strong with a 32% increase in gross lending in buy-to-let over 2011.

This paper looks behind the headline numbers. It examines the trends in rental growth and analyses the profile of the private rental market. The paper reveals a polarised market segmented by location and price and highlights the drivers of demand and regulatory challenges faced by the buy-to-let mortgage market.

- There are two very distinct rental markets – one in London and another for the rest of the UK. In 2011 rental growth was lower than in 2010 across all regions other than in London (see Figure 1).
- London has a much deeper pool of demand on the back of its world city status and large financial sector, in contrast to other cities where demand is largely domestic and driven by those unable to buy outright (see Figure 2).
- Rents today are broadly on a par with where they were three to four years ago except in London where they are higher.
- The rental market is highly segmented by price. Rents today are broadly on a par with where they were three to four years ago except in London where they are higher.
- This means there are often different trends in different segments of the market. The private market is where rents are relatively stable while the corporate end of the market – largely driven by corporate demand – is subject to greater rental volatility.
- 2011 saw a 32% increase in buy-to-let lending as investor demand grew. The risk for lenders is the origination profile of these loans against the distribution of the rental market fundamentals and by price. Local market fundamentals dictate the maximum sustainable LTV which for high capital value markets is lower than 75% (see Figure 4).
- European Union plans to introduce new regulations for the buy-to-let sector could well limit the scale of further expansion in this sector.
- Looking ahead, affordability factors will continue to limit rental growth and we expect rents to rise by 2-3% in 2012. Yields have improved modestly in the last four years and now average 5.3% gross. While better than low savings rates, investment in residential property is still motivated by an expectation of capital growth.

Hometrack © April 2012 The rental market – behind the headlines

## The Olympic London housing

Richard Donnell, Director of Research, Hometrack

Much has been made of the legacy that the 2012 Olympics will leave for East London in general and Stratford in particular, but with the Games just a matter of months away there has been surprisingly little impact on house prices across the area. Indeed an analysis of the relative performance of London's housing markets shows that the area around the Olympic site has under-performed despite high expectations and new investment. But it is early days for East London. Over the next 10-20 years a whole new residential quarter is set to emerge around the Olympic site and greater Stratford (E15) areas and with this, a new benchmark for house prices.

This paper reports on the current trends in pricing in Stratford relative to London and provides a range of pricing benchmarks for the potential uplift in values as new supply is delivered.

The analysis uses EPC data to enable a like-for-like comparison as average price data can be distorted by a change in the mix of transactions and in some cases large new developments.

- An analysis of residential capital values across London shows that on a EPC basis the area around Stratford and the Olympic site has under-performed over the last four years.
- In 2001, average EPC values in Stratford (E15) stood at a 30-35% discount to Greater London. In 2006, the year London secured the Olympic Games – the discount had narrowed to between 10-20%. Today the discount has widened to 35%.
- As a regeneration project, the area around the Olympic site and Stratford is still in its infancy. The next 10-20 years will see the growth of a new residential quarter, together with a new benchmark for residential values.
- The housing stock in E15 is set to grow considerably over the coming years. Up to 11,000 new homes have been planned for the Olympic Park and Village sites alone. A further 2,500 homes are planned on land around the Olympic Village. In total, this new supply will increase E15's housing stock by 50%.
- The Olympic site sits on an east-west pricing divide with prices to the west registering average EPC values in excess of £600psf, compared to the east (Stratford and West Ham), where values are at £250-£300psf. Around the Olympic site, values are up to £350-£400psf.
- For investors and potential owner-occupiers, the question is how does the area compare to other emerging markets across London and what are the current pricing benchmarks?

Hometrack © March 2012 The Olympics and East London housing market

the housing market to be pushed into a likely shortfall in the capacity of the private rental market to absorb the new supply.

This paper presents an analysis of the potential level of new delivery from a likely shortfall in the capacity of the private rental market to absorb the new supply.

- The average discount required to make RTB affordable to existing tenants is 40% or £50,000 – significantly higher than the current average of 25% but also more than the governments proposed cap of £50,000 on discounts.
- In London the discount required to make RTB affordable is as high as 58% or £128,000. In the South East the figure is £75,000. The proposed cap will limit take-up in higher value locations.
- The proposals are to re-invest capital receipts in new housing to ensure no erosion of stock – a so-called one-for-one replacement. The analysis suggests that the average capital receipt per sale would be £34,725 – lower than the cost of delivering a new property.
- To deliver one new home would require extra average 1.1 RTB sales. This ratio rises from a 1:1.1 ratio in the North West to 1.6:1 in London.
- A one-for-one replacement would require extra subsidy in the form of low or no cost public land or a release on RTB sales of above average value property which would deliver a higher capital receipt per sale.
- Access to mortgage finance and the fast employment mean that only a small proportion are likely to be able to take-up the RTB. Proper affordability assessments and financial advice are vital to any expansion in RTB.

Hometrack © January 2012 | Right to buy – can it work?

## Developer Pricing Analytics Report

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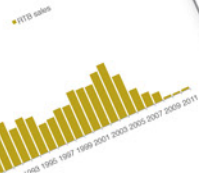
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Tom Nicholson, Group Special Projects Director, Galliford Try

### Right to buy – can it work?

Over 1.75 million households have taken up the RTB in the last 20 years and there are over 2 million tenants who still have this option. RTB has been away for a long time and it is not clear how many have taken-up the option.

### 1. The decline of RTB sales and average discounts



### Right to buy – can it work?

One-for-one replacement of new homes is central to the government's policy but the analysis reveals that the average capital receipt per sale would be £34,725 – much lower than the cost of delivering a new property and lower than the current average receipt of £77,470 in 2010/11. The gap between the capital receipt per sale and the replacement cost of a home will need to be plugged by borrowing against the rental income of the new property and/or other subsidies. Our model assumes that housing providers would be able to borrow 70% of the capital value generated from the rental income.

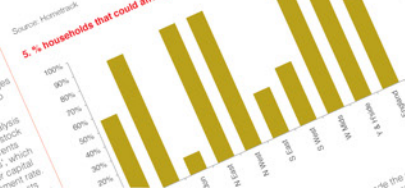
Another way to demonstrate this gap is to look at how many RTB sales would be needed to fund the delivery of one new home. Using data for replacement costs and average capital receipts by region, the analysis shows that 1.4 RTB sales are required on average to deliver one new home. The ratio rises to 1.6:1 in London (see Figure 4).

It is important to note that the analysis assumes that replacement costs are at £61 in London. The ratio rises to 1.6:1 at general needs rents, which are at a higher capital value than the average.

### 4 RTB sales needed to replace one unit



### 5. % households that could afford RTB with a 150k discount









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The 3<sup>rd</sup> Annual Hometrack Mortgage Summit  
Exploring the 'New Normal'



Tuesday, 17 May 2011  
Clothworkers' Hall, London



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