The Suburban BTR Housing Report

2021

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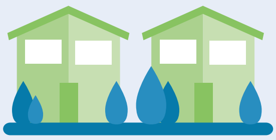
KEY FINDINGS

£7.8bn

of institutional capital ready to be committed to the suburban BTR housing market over the next five years by leading investors

11%

of completed operational BTR stock is suburban housing



60%

of UK private rented accommodation is houses, rather than flats

27%

of privately rented households are aged between 35 and 44, up from 17% a decade ago

2.6m

number of privately rented households who currently live in houses

Low rise, high expectations

NICK PLEYDELL-BOUVERIE
HEAD OF RESIDENTIAL INVESTMENT AGENCY

It's clear that the UK Build to Rent sector has undergone a step change since the beginning of 2020, with operational residential real estate proving to be extremely resilient despite wider macro-economic challenges. Occupancy levels have remained high and rent collections rates have been consistent and impressive. Consequently, we have seen a search for diversification, as well as secure long term income underpinning a rise in investment volumes in Build to Rent, as well as a significant increase in the volume of capital seeking exposure to the sector.

Urban flatted schemes remain in high demand following their strong performance over the past 24 months, but there has also been a rapid acceleration of interest and activity within the suburban build to rent housing sector. As we outline in this report, for investors already active in the multifamily market, suburban rental housing gives them exposure to different geographies and a diversified demographic, made up more of families than young professionals.

Around 60% of privately rented properties in the UK are houses. An estimated 1.8 million families with children already live in rented accommodation. The scale of the opportunity for institutional investors to deliver and manage suitable housing options for these households is huge.

Already, institutions including Goldman Sachs, L&G, Apache Capital, PGIM, Ares, Aviva and Blackstone have invested, or set up ambitious targets in the sector. Where they lead, more will follow.

To date, the capital committed to single family rental remains low as a proportion of overall institutional investment into BTR, however the sector is set to see significant growth over the coming years.

Moving to the suburbs

Investor interest and activity are rising, but what's driving a move into suburbia?

Some £275 million of institutional capital has been invested in the suburban Build to Rent housing market since the start of 2020 as investors look to diversify and grow their exposure to the private rental market. Strong demand fundamentals and proven resilience, as well as the potential for lower voids and operating costs compared with multifamily schemes, make family rental housing an increasingly attractive market.

We have surveyed 15 of the leading investors currently active or with capital committed to the sector. By our calculations, they have a combined £7.8 billion capital committed to target suburban build to rent housing over the next three to five years either through funds already secured or active fundraises.

The success of city centre multifamily schemes has helped lay the groundwork for a move to the suburbs. It also means that, unlike the early years of multifamily BTR, where investment was more gradual until the concept was proven, the suburban housing rental market is seeing a rapid increase from a range of institutional capital sources over a far shorter period.

TAKEAWAY

£7.8bn

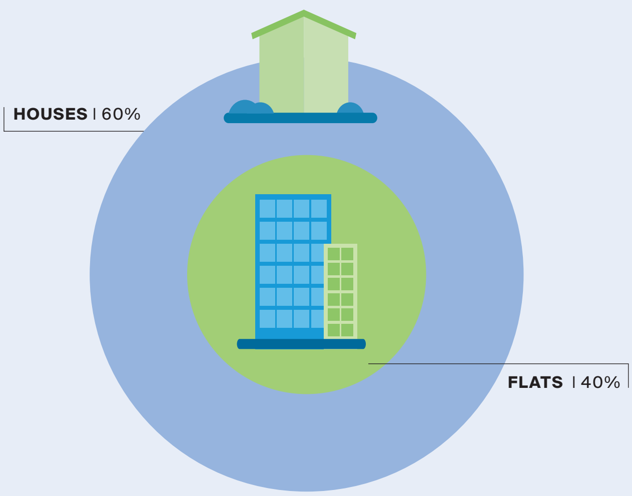
of institutional capital committed to target suburban rental housing in the next 3-5 years

Some 34% of the investors we spoke with are from higher risk value add funds, with the remaining 66% being core and core plus money. Around 38% of that capital originates from outside of the UK.

Like multifamily, investor interest is supported by robust demand-side fundamentals. More than half of the 4.5 million privately renting households in England live in suburban areas, a figure equivalent to nearly 2.3 million households, while around 60% of existing private renters already live in houses as opposed to flats. Clearly, the existing pool of demand is vast - and likely to be supplemented further by rising interest in less dense environments and more space post-pandemic. Meanwhile, affordability pressures in the sales market mean home ownership remains out of reach for many households. However, there is currently limited supply of high quality professionally managed institutional rental stock to meet this need.

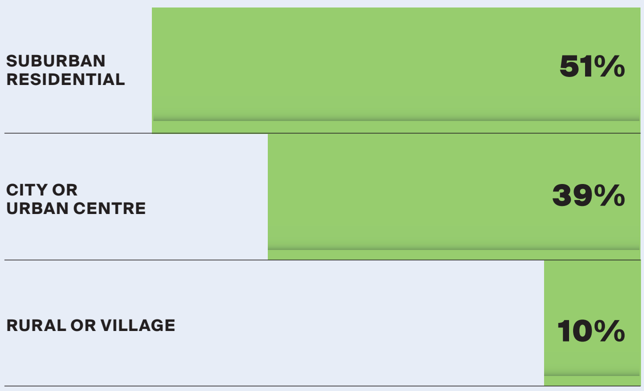
Depth of market

Proportion of privately rented households (England)



Most renters live in suburban locations

Proportion of privately rented households (England)



Sources: Knight Frank Research, English Housing Survey 2019-20

NEW WAVE OF CAPITAL

Despite strong investor and demand-side fundamentals, actual institutional ownership of suburban rental housing still remains low. BTR development to date has been focused on new build apartments in city centres, accounting for nearly 90% of all operational purpose-built rental stock – Sigma Capital/PRS REIT being the notable exception.

This is changing, however. Over the last year, a growing number of new dedicated investment and development vehicles have been created targeting the suburban housing market.

Investors include Legal & General who, in 2020, announced the expansion of their BTR offer to the traditional suburban home market with a target to deliver 1,000 rental homes per year from 2024; Elsewhere, Packaged Living launched a suburban BTR platform aiming to deliver 5,000 homes over the next five years; and Apache Capital is rolling out a rental housing platform with a £1.6 billion pipeline, both of which are discussed later in this report. Meanwhile, Ares Management is to back Moda Living's expansion into the suburban housing rental market.

From an investment perspective, the c.£150 million acquisition of the Thistle Portfolio comprising more than 900 suburban homes in the North West by Goldman Sachs-backed Pitmore in early 2021 provides evidence of investor appetite for standing assets, as did PGIM Real Estate's purchase of a portfolio of five stabilised assets and three development sites, comprising predominately two and three bed homes, across the Midlands and the North of England.

Due to the nascent nature of the market, we believe there is a significant opportunity to increase the ownership and delivery of purpose-built SFH, in turn bringing the benefits of institutionally-managed product to the largest pool of renters who are already living in single family accommodation.

> ***"Combined, it is estimated L&G, Packaged Living, Apache Capital and Goldmans Sachs could deliver nearly 20,000 new family rental homes between them over the next five years."***

Why do investors like it?

Positive demographic and demand-side drivers help underpin the investment case for SFH.

Data suggests that more people than ever are now likely to rent throughout their lifetime, through both choice and necessity. This has led to shifts in the composition of the rental sector, with 27% of all privately renting households now aged between 35 and 44 years, up from 17% a decade ago and fewer than 10% in 2000.

Not only does that make households aged over 35 the fastest growing group of private renters in recent years, it also means more families are living in privately rented accommodation. Private renters with children now account for 36% of households in the private rented sector, up from 31% a decade ago.

As people grow older and as their lifestyles change so do their accommodation requirements. Larger properties in less urban locations become more desirable – preferably a house with a garden, located close to local amenities and within reach of employment hubs.

Consequently, investors are drawn to suburban rental markets by the nature of the tenants themselves. They tend to be less frequent movers – given their ties to local schools, employment and support networks. That means a lower turnover of tenants, longer tenancy terms and fewer and shorter void periods, all of which help maintain more secure income streams. Longer tenancies and fewer voids materially reduce operating costs compared with multifamily schemes.

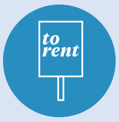
In addition, suburban rental schemes tend to require less extensive communal services, or maintenance costs associated with lift cores and onsite amenity. Typically, this results in the gross-to-net income leakage being lower than on urban BTR sites.

TAKEAWAY

The potential for lower voids and longer tenancies helps materially lower operating costs.

"Private renters with children now account for 36% of households in the private rented sector."

Investor benefits

1 

Lower tenant turnover

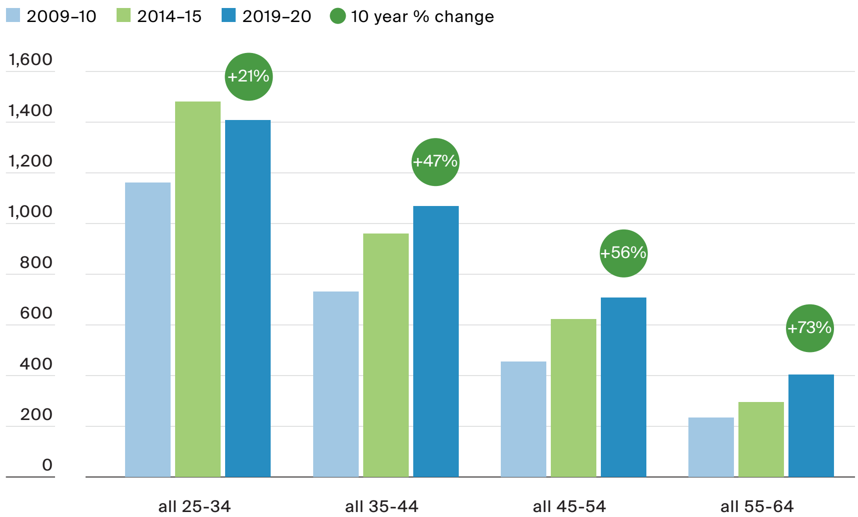
2 
Longer tenancies

3 
Lower operational costs

4 
Lower gross to net income leakage

Long-term change in private renters by age

England



Source: Knight Frank Research, English Housing Survey 2019-20

"The upshot of months of being homebound as a result of the pandemic has been to increase people's desire for space, inside as well as out. This has driven further demand for suburban markets, particularly for houses."

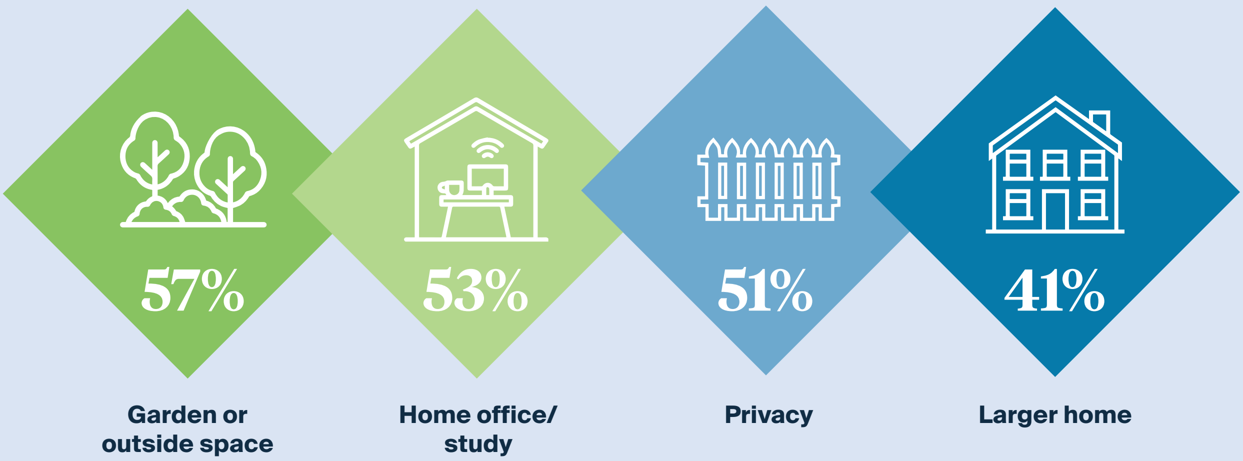
Changing requirements post-pandemic will boost demand

Some 57% of respondents to Knight Frank's latest client survey said that having a garden or access to nearby green space is more important to them now than it was pre-pandemic, while 41% said their experience from lockdown meant they were now looking for a larger property. Some 57% pointed to a desire for dedicated space to work.

The upshot of this 'search for space' has been to drive demand in suburban markets, particularly for houses. Data from property portal OnTheMarket shows that across the country it took an average of 26% less time to let out a house in the second quarter of 2021 compared with pre-pandemic. Well-connected suburban locations, ideal for those who can split their working week between home and office, will remain in demand moving forward.

Changing requirements post-pandemic

% of respondents saying a factor was 'more important' than pre-pandemic (June 2021)



Source: Knight Frank Research

Building the pipeline

Rising investment volumes specifically targeting suburban build to rent housing will drive a significant uptick in delivery from current levels.

Analysis of the Knight Frank development database shows there are 6,000 completed purpose-built rental properties in suburban single family rental schemes across the UK, currently representing less than 11% of total BTR operational stock by unit numbers.

Most of these operational units are located in the North West, accounting for 74% of the total, and most are owned by Sigma Capital / PRS REIT, which was one of the first movers in the sector. As more investors enter the market, this geographic distribution will shift and more regional markets will be unlocked. Already, our analysis of the future pipeline suggests that 80% of private build to rent houses in planning or under construction are located outside of the North West.

The average size of schemes is also getting larger, from an average of 85 homes for current operational schemes to 145 homes for schemes in the planning pipeline. This is partly a reflection of investors' desire for scale, but also of a greater understanding of the ideal unit mix, scheme density and economies of scale.

"There are 6,000 completed purpose-built rental properties in suburban single family rental schemes across the UK, less than 11% of total completed BTR stock by unit numbers."

But while supply of suburban build to rent housing is growing, there are hurdles. Land availability and competition for sites from for-sale housebuilders is a barrier to further growth, particularly in southern England and, while we expect to see more partnerships between investors and housebuilders to deliver rental housing on sites, the strong sales market currently makes for a tougher climate to deliver rental housing. That said, the benefits are clear. As well as helping to de-risk projects by forward selling part of a development, building non-competing uses can also help shorten development timeframes and support more diverse local housing markets.

The planning perspective

CHRIS BENHAM
KNIGHT FRANK PLANNING

The issue of delivering the right sort of homes in the right location, for rent, is highly relevant to policy makers. It is inevitable that local planning authorities will, in the future, include policies specific to the build to rent sector. Innovation in housing products is evolving much faster than planning policy is able to respond, and whilst the National Planning Policy Framework and National Planning Practice Guidance provide support for build to rent, those looking to develop purpose built suburban rental housing for rent are currently operating in a policy vacuum. This presents an opportunity for the sector to establish itself without many of the usual shackles of planning policy and, in turn, to influence how future policies are worded.

In persuading planning authorities of the need to plan for rental housing, the following points are worth highlighting:

Contribution to national housing delivery – at the national level there is a target of at least 300k new homes being delivered each year. Historic building rates show that achieving this rate of delivery consistently is a significant challenge. The development of build to rent can help to meet the ambitious national housing delivery target. As increasing numbers of people decide to rent a home, developers in the sector will be encouraged to maintain higher rates of delivery to keep pace with demand.

Housing choice – historically housing has been delivered for those who can afford to buy it, and as various forms of affordable homes. The new model of family build to rent offers a different choice for those who rent. Creating professionally managed rented accommodation is an attractive proposition for many people – planning authorities should welcome this new form of housing to meet the needs of this community.

Affordable housing – whilst most planning authorities do not have policies on affordable housing that apply to build to rent, the NPPF creates a policy position to promote locally. The provision of Discount Market Rent, which is a recognised form of affordable housing, offers a new form of affordable housing that can contribute towards meeting housing need.

Stimulating regeneration – where an area is subject to a wider regeneration initiative, the delivery of build to rent can be a useful means of creating a core community in earlier phases and helping to create an identity for the area. The presence of a community is vital to providing economic stimulus to support the establishment of new businesses, amenities and infrastructure, and drive further inward investment.

Economic prosperity – the opportunity to reduce out-migration exists with the increase in single family build to rent. Rather than the economically active being forced to relocate to other areas to find suitable family accommodation, the delivery of single family build to rent provides greater opportunity for the retention of those people locally.

Suburban build to rent housing schemes

COMPLETED SCHEMES

	AVERAGE SIZE OF SCHEME (number of units)	PROPORTION OF TOTAL (number of units)
NORTH EAST	39	1%
NORTH WEST	87	74%
SOUTH EAST	129	5%
WEST MIDLANDS	90	15%
YORKSHIRE AND THE HUMBER	64	6%

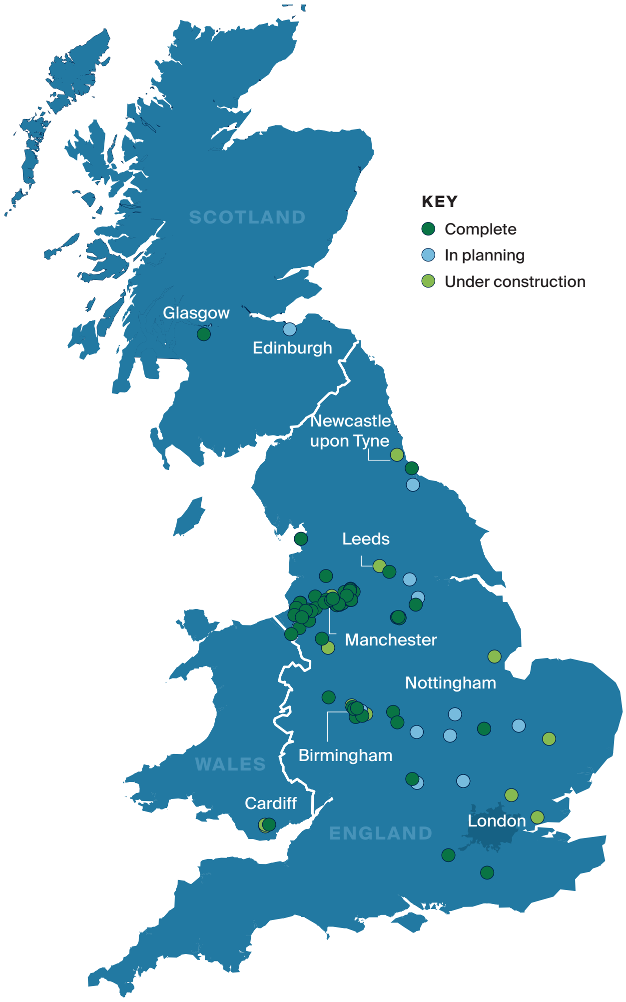
PIPELINE SCHEMES

	AVERAGE SIZE OF SCHEME (number of units)	PROPORTION OF TOTAL (number of units)
EAST MIDLANDS	103	6%
EAST OF ENGLAND	209	21%
NORTH EAST	100	4%
NORTH WEST	173	21%
SCOTLAND	232	9%
SOUTH EAST	162	9%
WALES	394	8%
WEST MIDLANDS	87	9%
YORKSHIRE AND THE HUMBER	105	14%

*statistics exclude MOD rental housing

SUBURBAN BUILD TO RENT HOUSING DELIVERY

COMPLETED AND PIPELINE SCHEMES



Source: Knight Frank Research

"We expect to see more partnerships between investors and housebuilders to deliver family rental housing at scale."

The expert view

Having advised a number of institutions and delivery partners on suburban build to rent housing investments and developments, Knight Frank's Jack Hutchinson gives his view on what works, supported by the results of our survey of 15 leading investors.

JACK HUTCHINSON
RESIDENTIAL CAPITAL MARKETS

Rental levels in the UK follow the concept that price is more aligned to bedroom numbers than size of unit. As a result, investors into the suburban build to rent housing sector are looking to fund schemes which enable them to maximise rental income whilst reducing both operating and delivery costs. Consequently, we are typically witnessing the majority of suburban build to rent housing product being approximately 15% to 20% smaller in size than traditional for sale product.

Investors are also becoming increasingly discerning with regards their required unit mix. Whilst this will be led by planning and location specifics, investors require a heavy weighting towards two and three bedroom houses. These units, by virtue of their size, assist in driving the strongest investment value on a rate per sq ft and also reflect the most prevalent rental unit types in the housing market.

We know from our list of active requirements, past deals and survey results, that the 'sweet spot' in terms of scheme size is just over 100 units – though both larger and smaller requirements exist and will be dependent on the supporting nature of the local market demographics and an investors' specific strategy.

On average, the investors we spoke with are targeting gross-to-net income leakage of 21%, reflective of the operational efficiencies present at suburban housing schemes (compared to multifamily schemes) with lower levels of communal services and amenity required and longer tenancy terms with fewer voids.

Due to the nascent nature of the SFH sector, with little access to stabilised assets, investors are predominately looking to forward fund new developments to aggregate portfolios. Forward fund structures can also benefit investors by enabling a level of input on their required specification, unit mix and design.

As the weight of capital chasing suburban rental housing stock continues to grow, we are supporting clients on deals that are being conducted through varying avenues, from strategic landowners through to housebuilder framework agreements.

TAKEAWAY

Partnerships between housebuilders, developers and investors will underpin an uptick in the delivery of new rental homes across suburban markets

4 developer delivery benefits

1. De-Risking: the forward fund or forward commit nature of the majority of suburban build to rent housing deals helps to de-risk projects for delivery partners, which otherwise would be subject to a fluctuating sales market.

2. Non-compete: the delivery of rental product, being a non-competing use with the sales product, can shorten development timeframes and release areas for development ahead of a sales delivery strategy.

3. Massing: there is an ability to improve massing on suburban sites, with the adoption of efficiently designed units with a greater weighting towards the predominant rental unit type of two and three bedroom houses.

4. Bring life to developments: the delivery of rental product, on a development can assist in the early marketing of the sales product, by creating a bustling and lively community in which people wish to live.

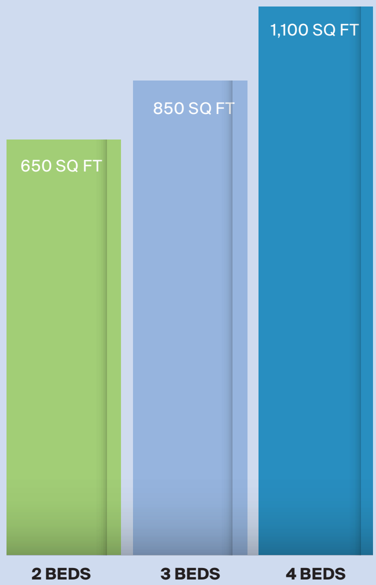
INVESTOR SURVEY RESULTS

21%

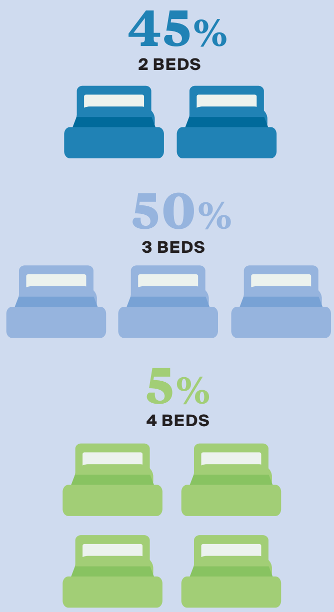
GROSS-TO-NET INCOME LEAKAGE TARGET (INCLUDING VOID)
AVERAGE OF SURVEY RESPONDENTS

Optimum SFH unit size and mix

Unit sizes



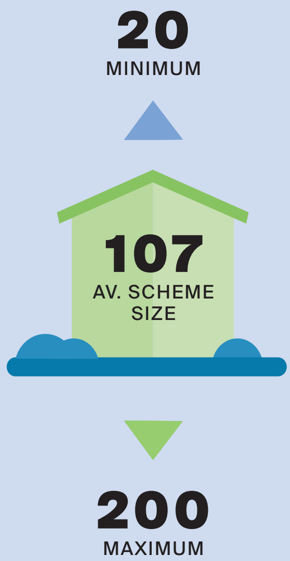
Unit mix



*averages/estimates. Exact sizes and mix will depend on location specifics

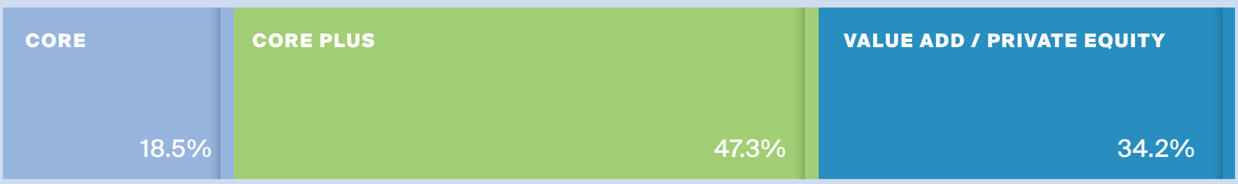
"Sweet spot" for scheme size

Number of homes, average of survey respondents



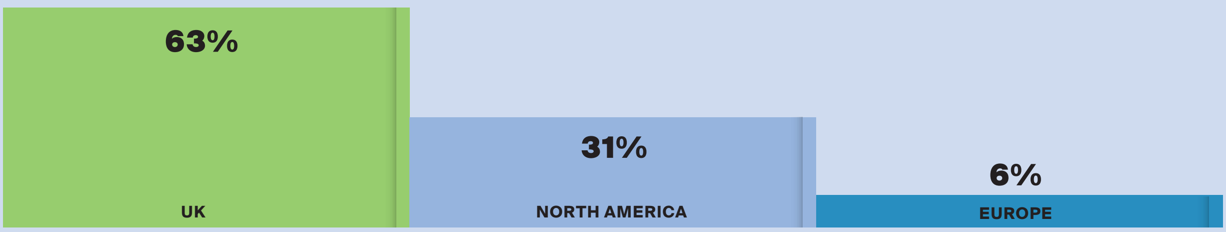
Type of capital targeting SFH

Proportion of survey respondents



Origin of capital targeting SFH

Proportion of survey respondents



The industry view

VITTORIO DAVICO

PARTNER,
PITMORE
(GOLDMAN SACHS)

The purchase of the 918 unit Thistle Portfolio from Gatehouse Bank and a 149 unit parcel at Houlton Rugby from Urban&Civic in joint venture with Goldman Sachs Asset Management were the seed investments in building a national portfolio of single family rental homes, which are currently significantly undersupplied.

Alongside Goldman Sachs, we have successfully formed partnerships with housebuilders and master developers to generate a pipeline for developing high quality, new rental homes across a number of sites, including with Urban&Civic.

We are predominantly targeting schemes of over 100 rental units with good transport connectivity, close to major employment hubs and amenities, spread across the UK.

The institutionalised single family sector is still in its relative infancy, but as an increasing amount of investors enter the sector, we expect it to expand and become more sophisticated. We hope to be one of the drivers of that process.

ALAN PENFOLD

EXECUTIVE DIRECTOR,
PRESENT MADE
(APACHE CAPITAL)

Over four years in the making, Present Made is a vertically integrated single-family rental housing platform, meaning it develops, owns and operates purpose-design and purpose-built single-family homes for rent.

As part of our initial £1.6bn development pipeline, we will deliver over 3,000 precision engineered ‘smart’ homes for rent in suburban locations across the South of England, with a particular focus on opportunities in the Oxbridge Arc – a highly productive, innovative region with strong growth but also high housing costs.

By offering high quality single-family homes designed and built for rent, we can provide a flexible yet secure housing option that has multi-generational appeal and will help raise the bar for suburban renting.

We want to make sustainable living second nature for residents, and that means taking a different approach to how we design and build our neighbourhoods. At the core of the concept is the idea of ‘people, not cars’. That is why all our homes will be set in landscape-led, master-planned communities threaded together by streets that promote walking and cycling. At the heart of our communities will be a compelling, multi-functional amenity offering that has a broad range of uses and appeal.

The homes themselves will be engineered in factory environments in a process that results in less waste and disruption to local communities and are more sustainable to run over the long term thanks to higher energy efficiency. Offsite construction also means we can deliver the homes at speed and scale, in half the time of traditional construction, meaning can income can be secured quicker – a key benefit for investors.

JONATHAN IVORY

MANAGING DIRECTOR,
PACKAGED LIVING

Since inception, the Packaged Living build to rent business plan has been underpinned by population growth, structural undersupply of housing, falling home ownership rates and a societal shift to new ways of living including a consumer preference for customer service and the benefits of renting.

At its core, all real estate businesses are about matching capital to investment opportunities, which is why we are now significantly expanding our 2,500 unit multifamily housing development portfolio so that our yield focussed investors may access inflation matched, countercyclical, granular, and perpetual income streams that provide a significant spread over the risk free rate.

Having spent the last decade proving concept in the multifamily sector, we now recognise the benefits of single family rental housing, namely the same compelling, stable, risk adjusted income returns enjoyed in multifamily, but with more efficient operating expenses resulting from lower churn, less common area maintenance and the absence of expensive amenity space.

With lower running costs, rents can be more affordable and so capture a greater share of the local market.

UK residents have been renting affordable, well located suburban houses since home builders have been developing them, but Packaged Livings variations on an old theme include energy efficient, IoT (internet of things) homes designed for a post pandemic world that is embracing more flexible ways of working and living.

Residential Capital Markets
We are market leaders in BTR and our experienced team provides a comprehensive service offering to investors and developers in the sector. The team is dedicated to comprehensive consultancy, and securing the best results for our clients. Our breadth of expertise covers services, including forward funding transactions, joint venture structuring, funding and finance, BTR design consultancy, strategic analysis and residential investment research.

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