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Large Scale UK Residential Investment: Achieving Market Maturity

SHORT PAPER

COMMISSIONED BY THE IPF RESEARCH PROGRAMME

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This Programme supports the IPF's wider goals of enhancing the understanding and efficiency of property as an investment. The initiative provides the UK property investment market with the ability to deliver substantial, objective and high-quality analysis on a structured basis. It encourages the whole industry to engage with other financial markets, the wider business community and government on a range of complementary issues.

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Large Scale UK Residential Investment: Achieving Market Maturity

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Large Scale UK Residential Investment: Achieving Market Maturity

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1. EXECUTIVE SUMMARY

This short paper reviews the evolution of UK residential sector as an institutional investment and considers the prospects for further growth. It primarily draws on the institutional investment surveys the IPF conducted over the nine years from 2012 to 2020.

The IPF's Size and Structure of the UK property market report estimated £10.0 billion (bn) of UK private rented sector investments were held by mainstream investors at the end of 2012, with a further £6.0bn invested in student accommodation. By end 2018, these figures were estimated to have increased substantially to £35.0bn and £21.0bn respectively, representing growth of over 23.0% p.a. of private rented sector (PRS) investments held by mainstream investors. This rapid growth has been reflected in the survey of institutional investors, with coverage expanding from £7.6bn in 2012 to £30.0bn in 2020[1]. For context, Savills has estimated £3.1bn was invested in the Build-to-Rent (BTR) sector in the first three-quarters of 2020, with BTR activity averaging £2.5bn to £4.0bn p.a. over the last five years. Similarly, CBRE estimate that 2020 was a record year[2] for multifamily residential investment with £3.5bn invested.

However, the residential sector remains a relatively small, albeit growing, proportion of most institutional investor portfolios, compared to the potential scale of the market. Even from the respondents to the UK residential property institutional investors survey, UK residential still only accounts for 12.9% of their UK real estate assets and only around 3.0% of the UK PRS market is estimated to be owned by institutional investors.

The main investor concerns back in 2012 were the management intensity of the sector and the difficulty of achieving scale and acquiring assets. The first of these concerns has faded as investors have become more familiar with the sector, as third-party management services have improved and as the operational intensity of other sectors has increased. The second of these concerns remains and this has led to many investors undertaking or funding developments themselves to secure investment stock. The market is clearly maturing but the widespread liquidity of standing investments, such that new investors can rapidly gain exposure, still appears some way off.

The main focus of investment over the past decade has been directed at good or high-quality market rental property for young professionals, notably in city centres. However, more recently, there appears to be a shift towards a much broader offer, partly accelerated by the impact of Covid-19. Looking forward, it seems likely that there will be significant growth in investment in single family housing and growth in investment outside the city centres of the UK's major conurbations, alongside the traditional city centre locations.

In addition, expansion into affordable and discounted market rental housing has accelerated. The 2020 IPF Residential Survey reported net intentions of over £2.0bn, significantly higher than levels reported in previous survey years. The sub-sector looks likely to see further substantial growth going forward, given the focus of investors on stability and resilience of income.

There is a strong commitment amongst mainstream investors to environmental standards and ESG issues and these are expected to play an important role in shaping UK residential investment in the future. However, the financial viability of net zero carbon buildings looks challenging without government support, for example, through planning, reduced taxation, land release/partnering or financial support.

[1] The survey includes development capital expenditure whilst the focus of the size and structure report is standing investments.
[2] CBRE data started in 2015.

1. EXECUTIVE SUMMARY

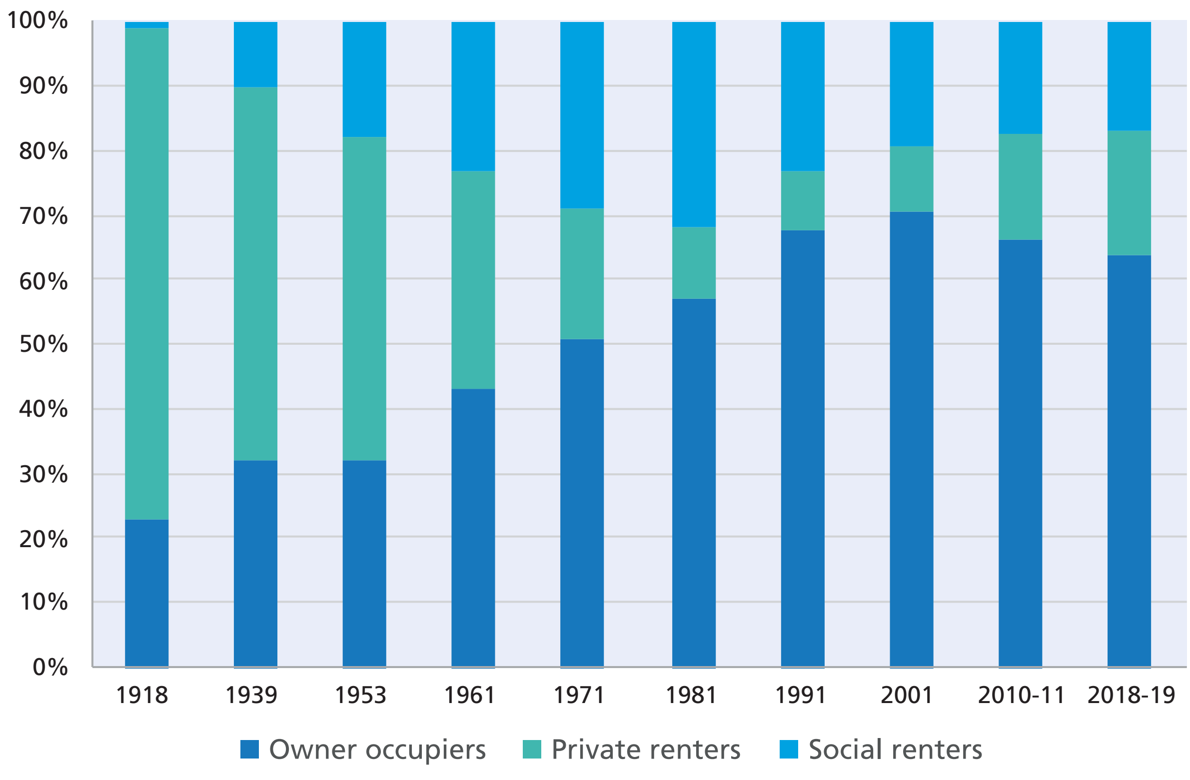
Further substantial growth of institutional investment in residential property is nonetheless still likely. This will aid improvement in the quality of housing on offer to renters across the UK and help address the overall housing needs in the UK, with government currently targeting an annual increase of 300,000 new homes a year by the mid-2020s.

It is suggested that government could do more to support the growth and impact of institutional investment in the UK residential market. Contributors to the survey highlighted a more supportive and simplified planning regime and the removal of the 3% SDLT surcharge for large-scale residential rental investment, introduced in 2018, as two key areas for government review. There is a sense that policy has become overly focussed on supporting home ownership rather than an integrated strategy to support the delivery of good quality sustainable housing of any tenure.

2. INTRODUCTION

In 2012, the UK government, keen to encourage greater investment into privately rented residential, tasked Sir Adrian Montague with an exploration of how greater flows of investment could be encouraged into the sector. His review was published later that year. In response to this publication, the IPF issued their first 'Institutional Attitudes to Investment in UK Residential Property' report at the end of 2012. This report surveyed institutional attitudes towards residential and aimed to encourage greater understanding of the sector by large-scale institutional investors, who had limited exposure at that time. Historically, private renting has been much more common and institutional investors were active in the sector but, by the 1980s, the private rented sector had become only a small part of the housing market (see Figure 2.1).

Figure 2.1: Trends in Residential Tenure



Source: 1918 – Estimates by Alan Holmans of Cambridge University Department of Land Economy; 1939-1971 – "Housing Policy in Britain", Alan Holmans; 1981-1991 – ONS Labour Force Survey; 2010-2019 – English Housing Survey

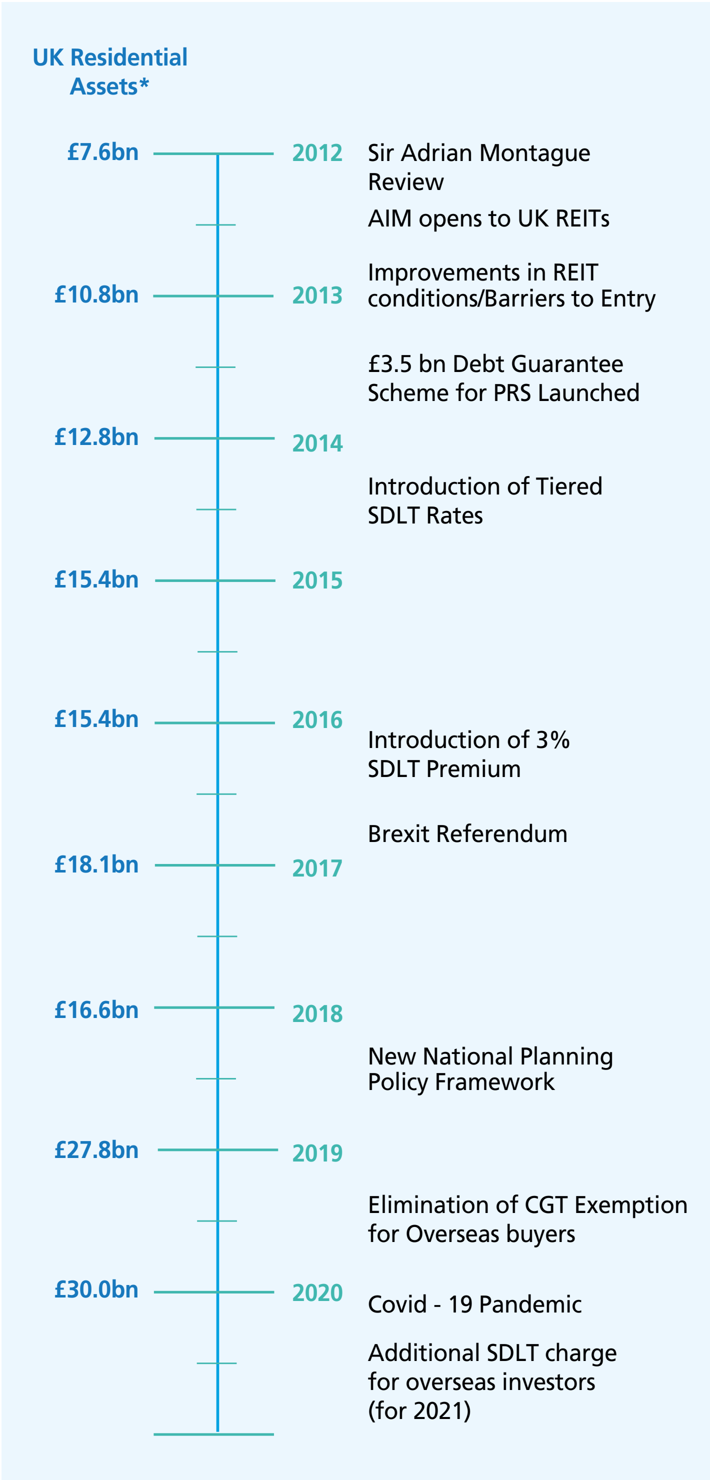
The key attractions for investors at the time of the first survey were the return profile offered by the sector, followed by stability of income and its low correlation with other assets. The main barrier of entry noted, for non-investors, was the management of the properties and operational intensity, reflecting the different nature of residential tenancies relative to commercial assets.

2. INTRODUCTION

The IPF has continued to investigate institutional involvement in the UK residential sector over the last nine years and the final survey in the series was recently published. During this time, there has been a substantial shift in sentiment towards residential, reflected in its growing weight within investment portfolios and that many large institutional investors are now committed to the sector. It is increasingly viewed as a mainstream sector alongside industrial/logistics, offices and retail. This paper looks forward over the next five to 10 years and explores the issues and influences that are liable to shape institutional investment in UK residential in the future.

The paper draws on responses to the 2020 IPF Residential Survey (and earlier IPF surveys). The survey was carried out on-line and was directed at major institutional and large-scale investors, including pension funds, life assurance companies, property companies, including real estate investment trusts (REITs), sovereign wealth funds, fund and investment managers and developers. In addition, further comments and views were garnered from 18 interviews with survey contributors, both investors and non-investors. All information was provided in confidence and is reported in aggregate. Data collection took place over 13 weeks from late July 2020, with interviews taking place during October.

3. RESIDENTIAL IN RECENT TIMES



* Covered in IPF Residential Surveys

Before exploring the future issues and influences on UK residential, it is worthwhile reflecting on the development of the sector over the past decade. During this time, there has been a sharp increase in institutional involvement in the UK with PRS investments estimated to have increased from £10.0bn in 2012 (with a further £6.0bn in student accommodation) to £35.0bn in PRS and £21.0bn in student accommodation in 2018 (source: IPF Size and Structure of the UK Property Market).

This growth is supported by the results from the IPF surveys of investor attitudes to residential. Contributors to the 2012 survey were responsible for £7.6bn of residential stock. By 2020, this exposure had grown to £30.0bn. This rapid growth reflected a significant rise in the proportion of UK portfolios allocated to the sector. In the 2012 survey, residential constituted just 4.6% of UK real estate portfolios but, by 2020, this figure had risen to nearly 13.0%.

In the first half of the last decade, government policy was generally supportive of UK and overseas institutional investment in the residential rental market. Since then, policies have been less encouraging, with the primary focus on supporting home ownership. It is not possible to quantify the negative impact of these policies, such as the 3% SDLT surcharge, on investors' intentions towards the residential but they will have made UK residential less attractive, when compared to other investment sectors and markets.

3. RESIDENTIAL IN RECENT TIMES

Interviewees were questioned over what major events or initiatives have impacted on their organisation's residential strategy over the last 10 years. Most made their first significant investments into the sector during this time. The replies indicate the main drivers have been market dynamics and investment characteristics. A number of investors discussed the attractive supply/demand dynamics that the sector offered, and still offers, with a limited supply pipeline and a substantial consumer requirement for good quality residential stock. Government's current housebuilding target for new homes is 300,000 per annum by the mid-2020s.

The fallout from the global financial crisis, towards the end of the last decade, sparked interest in residential from a number of investors, attracted by the relative resilience of house prices, and an increased appetite for lower return/lower risk product with inflation-matching qualities. The under-developed nature of the market compared to other countries, such as the US, Germany and the Netherlands, encouraged a number of investors to bring their experience, acquired in other markets, to the UK.

Government policy appears not to have been a major driver in encouraging investment although the more supportive environment initially, reflected in the Montague Review, was a factor for some. One investor mentioned the 2013 change in permitted development rights, allowing the conversion of offices to residential, as the spark that ignited their interest in the sector. Another highlighted that the early priming of debt finance markets, through government-backed products, was a significant enabler and confidence builder for early developers and investors in the sector.

One investor explained that institutional investors have become more comfortable with taking on operational risk over the past decade. In addition, in the commercial property market the long secure leases of the past are generally no longer available, hence the shorter leases offered by BTR residential are less problematic.

In the 2012 IPF Residential Survey, the most prevalent reason cited for not investing was the difficulty in managing assets, given the specialist skills required. Interviewees commented that better quality residential property managers are now more widely available; this is supported by the results from subsequent IPF Residential Surveys.

Half of the interviewees stated that diversification was a fundamental reason for entering the sector. Several interviewees mentioned that they already had considerable exposure to student accommodation and were looking to broaden portfolio focus. Those that have considered residential investment recently, cited the decline in the UK retail market as the impetus for considering other options and, in the near-term, Covid-19 and the acceleration of the working from home trend for a weakening of interest in offices.

4. ACHIEVING MARKET MATURITY: INFLUENCES AND ISSUES

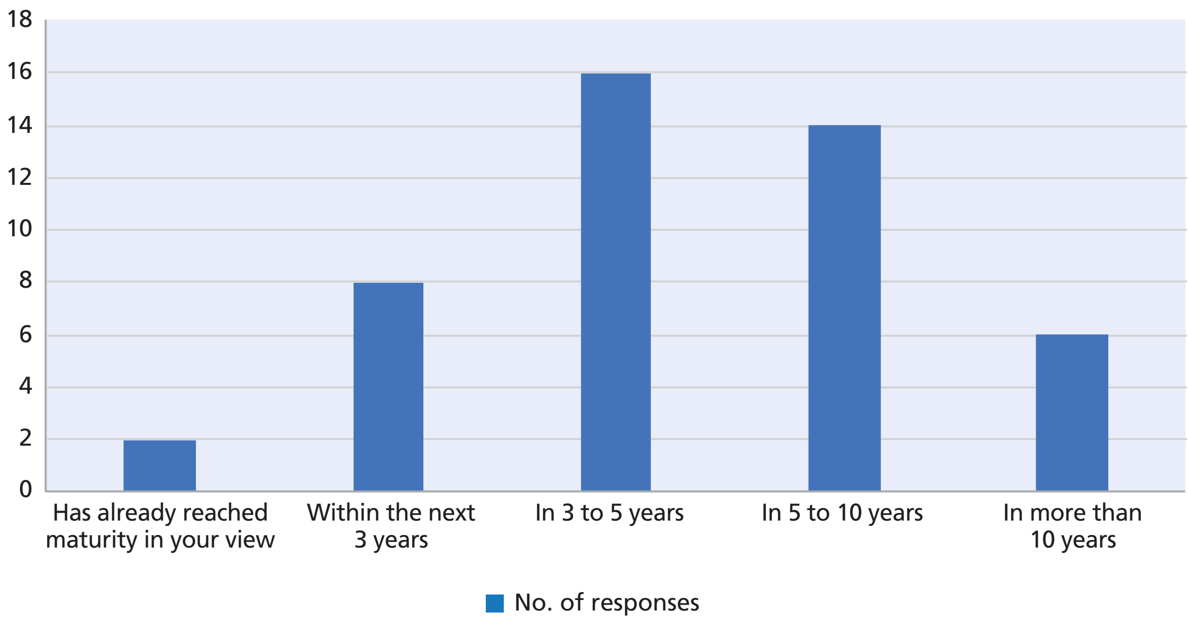
Interest in the UK residential market by institutional investors has grown significantly in recent years. This has been well documented by the IPF Residential Survey and the 2020 survey indicates that this demand will continue for at least the next 12 months, with nearly £8.0bn intended to be allocated to the sector. However, residential is still a long way behind the other commercial real estate sectors, in terms of size and maturity of large-scale institutional investor portfolios. The IPF Size and Structure report figure of £35.0bn for PRS in 2018 compares with £374.0bn for commercial real estate held by institutional investors (excluding that held by private companies, individuals and other).

This section of the paper explores when investors believe market maturity will be reached and examines some of the key influences and issues on the growth of the sector, drawing upon survey and interview responses. Strong liquidity, an indication of a mature market, encourages investment, as well as reducing the cost of capital, as the risk premium is reduced.

4.1 Defining Market Maturity

For many investors, investing in developments has been a necessary route to access the modern, institutional residential stock desired, as there is inadequate depth in the standing investment market. Respondents to the survey were questioned about when they anticipate the residential market will reach maturity (when investors would have the choice to simply buy existing investment stock). The responses from 46 survey contributors in 2020 are shown in Figure 4.1.

Figure 4.1: Large-Scale UK Residential – Reaching Market Maturity



Source: IPF Residential Survey, 2020

4. ACHIEVING MARKET MATURITY: INFLUENCES AND ISSUES

Just over one third of respondents anticipate that the UK residential market will reach maturity within the next three to five years. A further third expects the sector to mature between five and 10 years.

Discussing the issue in further depth in the interviews, many commented that they were starting to see a small number of suitable standing investment transactions coming across their desks but agreed that maturity is some way off. One explained that an increase in the number of standing investments available will naturally take time as, the large-scale residential assets which are in demand by institutional investors, take approximately four years to develop, from start to completion.

In addition, many investors currently involved in the funding of residential developments are also intending to hold these properties as investments, so these assets may not come to market anytime soon. This will provide a barrier to investment for those not prepared to undertake their own development programme.

Several interviewees commented that if the UK population viewed renting in a more positive light (it is often looked down upon as a housing option) this would help expand the sector. One interviewee stated that there also needs to a more positive narrative towards large institutional landlords and the product they offer, in the press and from local and central government.

Interviewees were questioned about what indicators they would look for to convince them that market depth in standing investments has been reached. Almost all of the interviewees mentioned that the level of turnover was a good gauge of market maturity and would use other sector turnover levels for comparison.

4.2 Strategic Influences on Future Portfolios

Interviewees were questioned over how their organisation's residential investment strategy will change over the next five years and how this will influence the profile of their tenant base, for example, in terms of age or family size. The feedback received indicates a desire to broaden the offering of residential portfolios, as the portfolios mature and experience in the sector expands.

Six investors stated they would be diversifying their portfolios by providing more single-family housing. An additional investor, already extensively invested in this sub-sector, confirmed that they would continue with this strategy. Four investors also cited the importance of broadening product range to encompass other types of residential assets, such as co-living and senior housing, although one interviewee provided a note of caution in relation to senior housing, as they felt that this type of tenant still typically preferred to buy rather than rent. One interviewee revealed that they were broadening their offer by offering a variety of price points within schemes.

Investment intentions in the next 12 months, recorded by the 2020 IPF Residential Survey, also support the trend for diversification, with over £2.0bn allocated to affordable or discounted market rental housing. This is a record for the survey and represents over a quarter of the entire allocation to all residential.

The majority of investors stated the importance of having a nationwide strategy to spread risk and enhance returns. Those that have already adopted such a strategy will continue to do so, while others will ensure countrywide exposure through strategic decisions. One investor, pursuing a strategy of larger schemes, will focus on the major UK cities. In terms of micro locations, a third of interviewees indicated that they are considering expanding into more suburban locations, partially influenced by Covid-19 but also by a desire to broaden geographical and tenant exposure.

Five investors stated that they were considering scaling up the size of their residential investments to benefit from economies of scale in terms of management time and provision of shared amenities.

4. ACHIEVING MARKET MATURITY: INFLUENCES AND ISSUES

Interestingly, one investor considered that as graduates are housed in increasingly higher quality accommodation during their student days, they will expect a higher quality of accommodation post-graduation.

Currently, the majority of investors state that the average age of their tenant base is in the early thirties. However, investors expect to see a wider spectrum of ages investigating rental options, including retirees who have a mixture of motives for choosing to rent, including equity release, flexibility, service and less hassle. With an uptick in intentions to provide rental accommodation across the generational groups, as well as a greater proportion of investment in more suburban locations, most investors expect the age of their tenancy base to rise over the next five years.

4.3 Government Policy Influences

Survey contributors were asked which policies or changes to policy would be most helpful in achieving further growth in institutional residential investment. Thirty-one provided a response, many detailing several issues, and the most prevalent are ranked in Table 4.1. The most commonly quoted policy changes were the provision of a more supportive and simplified planning regime and the removal of the additional 3% SDLT surcharge for large-scale institutional investors.

Table 4.1: Desired Policy Changes

Policy/Policy Change	No of respondents	Additional Comments
More supportive and simplified planning	20	Particularly in relation to the inclusion of BTR in large scale development Review of viability assessments, particularly late stage BTR to have its own specific planning class
SDLT surcharge for second homeowners	11	Removal of the 3% surcharge, introduced in 2018, for large-scale institutional investors
Clarity around affordable housing	8	Desire for standardisation across local authorities
Reduction in VAT charges	5	Including: VAT changes on developments designated for rental purposes to allow VAT recovery in-line with developments designated for sale; a reduction or removal of VAT on costs associated with the refurbishment of existing buildings; and on management and maintenance costs.
Reduction in Capital Gains Tax	4	
Simplified landlord licencing regime	3	To provide a more supportive environment for institutional landlords

Source: IPF Residential Survey, 2020

The narrative from government today is most pronounced around home ownership. While acknowledging the importance of delivery of all housing tenures, it may be that policy becomes increasingly focussed on the ownership agenda in the near term. Given the positive early catalyst of Montague and the ultimate alignment of interest between all groups willing and able to invest into UK housing supply, it is important that the institutional investor continues to engage and build a narrative for the rental sector within government.

4. ACHIEVING MARKET MATURITY: INFLUENCES AND ISSUES

There continue to be many areas that resonate with the government agenda around high quality homes, consumer choice, flexibility and mobility. There is also a place for presenting housing rental as a steppingstone and gateway to home ownership, even if it may be a long-term transition for many, and perhaps investors may begin to innovate and create tenure models that specifically respond to that opportunity, including 'rent to buy' or 'try before buy'. Being proactive, creative and 'part of the answer,' will be important in further establishing an institutionally backed housing market, in a virtuous circle with housing and planning policy.

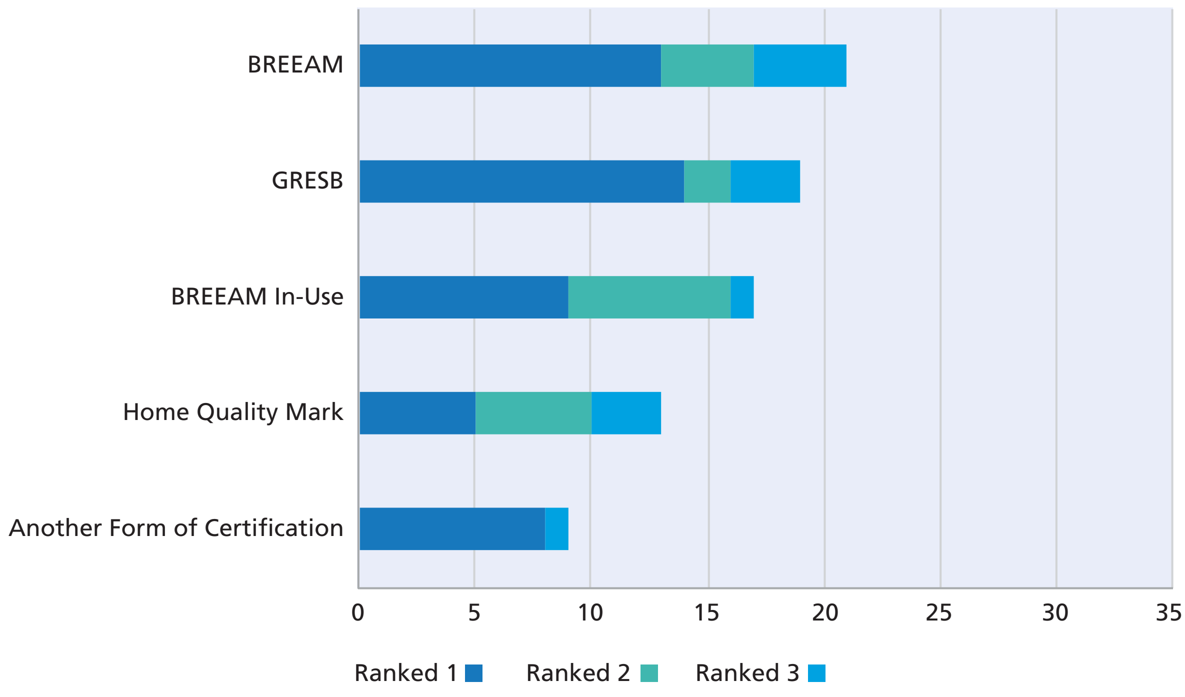
4.4 ESG

ESG issues are receiving ever greater attention across all asset classes but what influence does it have on the residential market? Both survey respondents and interviewees were questioned about the impact of ESG on the monitoring of residential portfolios; the development of assets; and the type of investment decisions actioned.

4.4.1 Measurable ESG Goals

To measure the extent of ESG influence, it is important to have measurable goals and to identify the extent to which they are going beyond the standards set out in building regulations. Survey respondents were questioned over which form of ESG certification they would like to see more extensively adopted by the investment industry. They were asked to rank all applicable options. These choices are listed in Figure 4.2, which also displays the relative importance of each accreditation to contributors. No requirement for accreditation was also an option.

4.2: Preferred Type of Accreditation Scheme



Source: IPF Residential Survey, 2020

4. ACHIEVING MARKET MATURITY: INFLUENCES AND ISSUES

The response from survey respondents was overwhelming positive towards a requirement for more extensive use of environmental certificates, with all contributors stating the need for some form of accreditation. The most popular choices were BREEAM and GRESB. Seven respondents did not give an opinion.

By contrast, during interviews, there was little mention of the above ESG accreditations when discussing measurable ESG goals for residential portfolios. Only two interviewees stated that they were currently utilising BREEAM, as a measurement tool for their assets, while two interviewees had completed the GRESB survey for their residential assets. A further investor had recently reviewed the GRESB survey but considered it unsuitable, in its current form, for the particular subsector they invest in.

Interviewees were probed over what measurable ESG goals their companies have set. Currently, almost half of interviewees have set some form of measurable goals, the majority based on either EPC Ratings or net zero carbon targets.

Three investors have a minimum EPC Rating target of ‘B’ for their assets with a further two have a minimum target of ‘C’. One investor explained that they have investigated the cost implication of adopting an EPC rating of A for their entire portfolio but found the increased target removes all the development profit and there were difficulties progressing some elements through planning, for example, smaller windows designed to minimise heat loss.

Achieving net zero carbon by 2030 is the goal of four investors, with a further investor targeted to achieve this by 2040 but ideally between 2030 and 2035. Additional measurable goals mentioned include Net Promotor Score (NPS) and Disability Discrimination Act (DDA) compliancy.

Despite the lack of measurable goals for some investors, all stated that ESG was an integral component of their future strategy and many have more qualitative measures in place at present, for example, ESG checklists for each asset. At least half of the interviewees were in the process of quantifying their ESG strategy and any measurable goals, at the time of interview. One interviewee was keen for government to take a lead in the process as their regulations were becoming more and more stringent. It would also result in a more level playing field in terms of costs incurred.

4.4.2 Building Specification

Interviewees were questioned over the influence of ESG in the design of their BTR properties and, in particular, what level of specification they currently build to.

Most interviewees are keen to push ESG boundaries. Over 80% of those involved in the specification stage adopt local building regulations but with additional requirements based on the organisation’s own criteria. Examples of these requirements include electric charging points in all vehicle parking bays, using the highest grade of thermal insulation, solar panels where possible and ensuring all assets have a high level of walkability and are surrounded by extensive public transport infrastructure.

There is recognition that design specifications need to go beyond standard building regulations as top ratings can become outdated quickly and targets change. Furthermore, many of the additional features result in a more resilient asset and institutional clients are keen to pursue an increasingly “green” agenda. However, cost is often a constraint on ambition and there was a question over whether residents will be prepared to pay a premium for a more environmentally friendly home. It is more likely to appeal to the younger elements of the rental market.

4. ACHIEVING MARKET MATURITY: INFLUENCES AND ISSUES

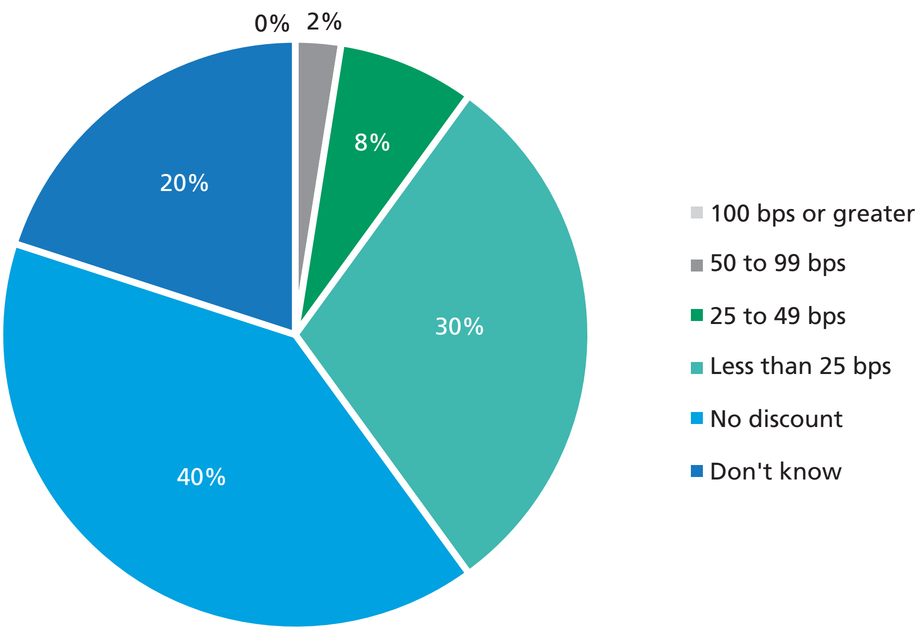
Several interviewees expressed an interest in adopting more stringent design measures, such as Passive House, a voluntary standard for energy efficiency in buildings. However, there was an acknowledgment that there are significant cost and viability issues when developing properties for the rental market and no respondents were currently adopting this level of specification as it was described by one as "financially challenging".

Three interviewees solely adopt the building regulations of the local area when specifying the design of their properties at design stage.

4.4.3 ESG Investing

Are investors prepared to accept a discount on return for investing in the most sustainable or socially responsible way? Survey participants were questioned over whether they would accept a discount on return for investing in net zero carbon housing. The results are shown in Figure 4.3. From the 40 responses, 40% stated that they would not accept a discount for this type of investment. Just under a third said that they would be prepared to accept a small discount, less than 25 bps. Only a tenth of respondents said they would accept a discount of more than 25 bps.

Figure 4.3: Discount on Return for Investment in Net Zero Carbon Housing



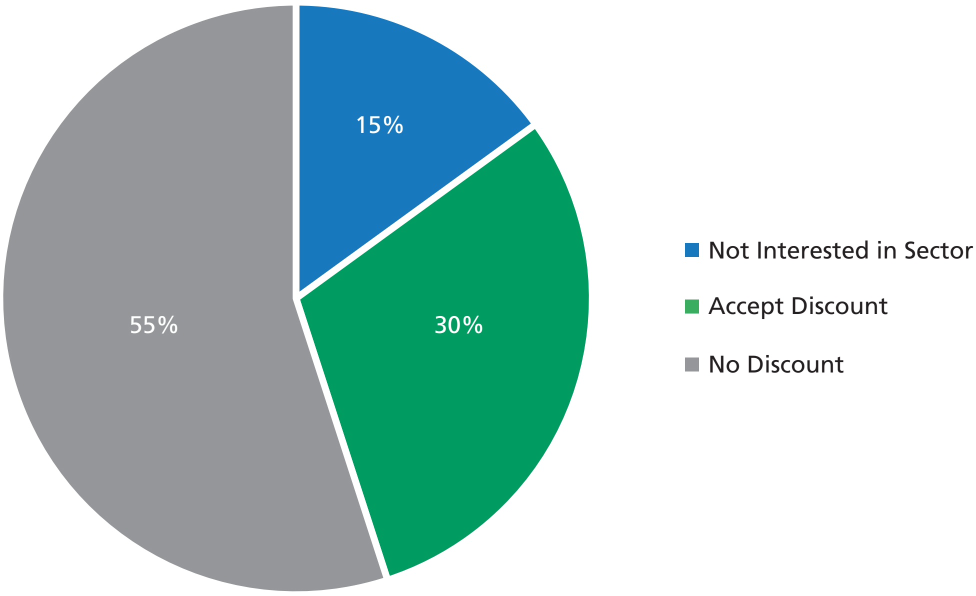
Source: IPF Residential Survey, 2020

Respondents to the survey were also asked if they would accept a discount on their return for investing in affordable housing and the results are shown in Figure 4.4. Currently, over half said they would not accept a discount for affordable investment while just under a third said they would accept some form of a discount. Six (15%) said they were not interested in affordable housing at the present time.

4. ACHIEVING MARKET MATURITY: INFLUENCES AND ISSUES

Of those who stated they would accept a discount, when asked to quantify this, reported a range from 25 bps to 100 bps. One investor, backing up the survey findings, stated that "given the more resilient returns profile of affordable housing, we would expect investors to pay a keener yield for this type of product. I just don't think the market is at the stage of realising just how resilient cashflows are in this area of the market yet."

Figure 4.4: Discount on Return for Affordable Housing



Source: IPF Residential Survey, 2020

4.5 Performance Measurement

The 2017 IPF Residential Survey highlighted the dual issues of an absence of appropriate investment benchmarking and transparent market data in the residential market. Both are widely available for mainstream commercial sectors of the UK real estate market. Interviewees were probed to ascertain whether this situation had improved over the intervening years.

Three-quarters of the interviewees stated that there had been no improvement in benchmarks and data availability. Two interviewees believe the quality of benchmark provision had got worse, being less reflective of the modern large-scale properties that institutions invest in, while a further two participants stated that there was more market data available now.

Interviewees were also asked if a lack of a robust and representative benchmark would hold back the residential market from reaching maturity. There was a dichotomy of views on whether a benchmark is obligatory.

4. ACHIEVING MARKET MATURITY: INFLUENCES AND ISSUES

Most investors stated that, as there is currently significant demand for residential assets, attaining market maturity will not be dependent on a lack of suitable benchmark or market data. A reliable benchmark would have been more critical a few years ago when investment intentions were less bullish. A number of investors explained that their funds have absolute benchmarks, hence peer comparison is not required. However, one investor provided a note of caution stating that it was important to have an investment benchmark as, in their view, absolute returns lose relevance over the longer term.

In addition, several interviewees indicated that it would be beneficial to have greater transparency, within the residential market, to encourage cross border investors, who are familiar with this information in other, overseas residential markets. Covid-19 has also highlighted the benefits of having a representative benchmark to help promote the robust performance of the asset class in difficult times.

One investor also explained that, for managers running balanced funds, there was a requirement to be able to compare performance across real estate sectors. Operational benchmarks and data are also useful for understanding operational performance. If an organisation is sufficiently large, efficient operating cost levels may be determined to some extent internally, but this is not possible for smaller portfolios without peer comparison.

As the residential market matures and deepens, provision of a more insightful benchmark and market data is more achievable. However, several investors commented that investors' willingness to contribute their own data will be dependent on the cost they will have to incur for the service.

5. SUMMARY, THOUGHTS ON THE FUTURE AND CONCLUSIONS

There has been a dramatic increase in mainstream institutional investment in the residential sector over the past decade. However, it remains a small proportion of the overall PRS market with substantial room for further growth. Market maturity is not expected to be achieved in the short-term, particularly if measured by turnover. Many of those currently funding developments are likely to hold on to them as they aim to grow their residential portfolios. Consequently, the ability of investors to deploy large amounts of capital into residential standing investments is likely to continue to be a constraint on investment over the next few years.

Back in 2012, investors were concerned about management issues and the operational intensity of residential. These concerns appear to have faded as the sector has become more established and as the operational intensity of commercial sectors has increased.

The focus of much investment over the past decade has been on good or high-quality market rental property for the young, notably in city centres. There appears to be a shift towards a broader offer, partly accelerated by the impact of Covid-19. Looking forward, it seems likely that there will be significant growth in investment in single family housing and outside the city centres of the UK's major conurbations, alongside more traditional city centre locations. Investors are also exploring the provision of rental options for a wider spectrum of ages to broaden lifestyle choices, including retirees.

In addition, growth in investment in affordable and discounted market rental housing has accelerated and this looks likely to continue going forward. As well as existing affordable housing tenures, large-scale investors may also start to deliver new product innovation, such as rent-to-buy and shared equity, which will provide further portfolio diversity, as well as helping to position rental housing as a key tenure within government policy.

Despite the increase in institutional investment, there remains a substantial shortage of good quality housing stock. Good quality rental properties would help fill the void and help support labour market flexibility – making it easier for people to move for work. However, a major stumbling block remains the inability to acquire suitable residential stock – something made more challenging by the focus on homeownership and build to sell, from both government and the media.

It is important that institutional investors find a voice to highlight the benefits of well-designed, professionally managed rental properties. For example, renting can provide a critical pathway to homeownership by helping tenants build up credit rating scores as well as providing flexibility and choice. The main focus of institutional investment in residential is on the mass market, mid-price and affordable markets, where the need is most acute.

The issue of under supply in the UK housing market, is further compounded by the limited land banking in the rental sector and the substantial time it takes to deliver large scale complex projects through a complicated planning and construction process. Providing a more simplified and supportive planning process and more rental-friendly policy changes, for example removing the 3% SDLT surcharge for large-scale institutional investors and other long-term investors, would help alleviate this situation.

5. SUMMARY, THOUGHTS ON THE FUTURE AND CONCLUSIONS

There is a strong commitment amongst institutional investors to environmental standards and ESG best practice and these are expected to play an important role in UK residential investment in the future, with many investors having extensive ambitions in this area. However, significant work is still required to fully integrate ESG issues into investment strategy and the financial viability of net zero carbon buildings looks challenging without government support. The commitment to high building standards and good practices by institutional investors in the sector is something that has been highlighted in the past (indeed, it formed part of the rationale for the introduction of REITs). Currently, the survey suggests that some institutional investors are willing to pay a small premium (accept lower returns) for properties with the highest ESG standards. This may become more common in the future as regulations are tightened and as capital sources focus on this issue and the risks associated with properties of lower environmental standards.

Whilst a number of residential investors are bringing experience from more established rental markets, such as in Germany, the Netherlands and the US, it is not clear that the UK will reach similar scale in terms of institutional ownership of the rental market soon. This in part reflects the relatively low base and the long time it will take to build substantial portfolios.

There is a willingness amongst investors to be part of the solution to deliver the homes that the UK needs, both in terms of meeting housing requirements in terms of stock levels, as well as, crucially, building high quality, energy efficient housing. Government could do more to encourage higher environmental standards through planning, regulation and financial incentives and to enable rental property to play an important role in facilitating flexibility for young and old, those moving for work and those who do not expect to stay in one place for a long time.

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