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Residential Research – February 2025

UK Build to Rent Market Update

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Is the bottom of the market behind us?

If 2024 was the year real estate capital markets stabilised, then 2025 could be the springboard for recovery. A number of key milestones were reached in the second half of last year which has noticeably improved investor sentiment and built momentum.

CPI inflation returned to the Bank of England's target range in April. The bank, feeling much more at ease with the prospects for inflation looking ahead, made its first cut to the base rate in August. A second cut came in November, and another in February, signalling that the anticipated pivot in monetary policy is upon us.

More base rate cuts are expected in 2025, which will improve the pricing of debt available to investors. But market experts are divided on the likely pace of rate cuts. Oxford Economics expect three more cuts in 2025 while financial markets are pricing in two.

Market sentiment and activity suggest that the bottom of the market is either already behind us, or very close to being behind us. That said, the high level of volatility in recent weeks, notably in the bond and swap markets, has added an air of uncertainty. While this shows that we are not out of the woods yet, the outlook should improve this year and encourage further investment.

Cheaper debt available amid tighter lender margins

An interest-rate driven recovery will encourage greater activity in the residential investment market, with both the commercial lenders and debt funds keen to deploy - and many have significant lending targets for 2025.

A lack of opportunities relative to demand has created competition between lenders and applied downward pressure on pricing. Given this appetite, banks have been willing to push leverage. More lenders are prepared to offer 60% loan-to-cost (LTC) and in recent months some mainstream banks have offered 65% LTC to strong covenants and those backed by strong balance sheets. At the same time, non-bank lenders have been eager to retain market share and while many are unable to compete with banks in terms of outright pricing, they have been willing to lend at above 70% LTC with margins well below SONIA +400bps to remain competitive.

Lender margins have tightened across the board amid increased competition. This has been consistent for both development and investment opportunities. For example, between December 2023 and December 2024 the margin on investment debt reduced from 4.00% to 3.00% at 70% LTV.

Development remains the primary route to market for BTR investors and they will be encouraged by the reduction in development debt costs. In 2025, we should see more development margins below SONIA +300bps from banks and SONIA +400bps from other lenders.

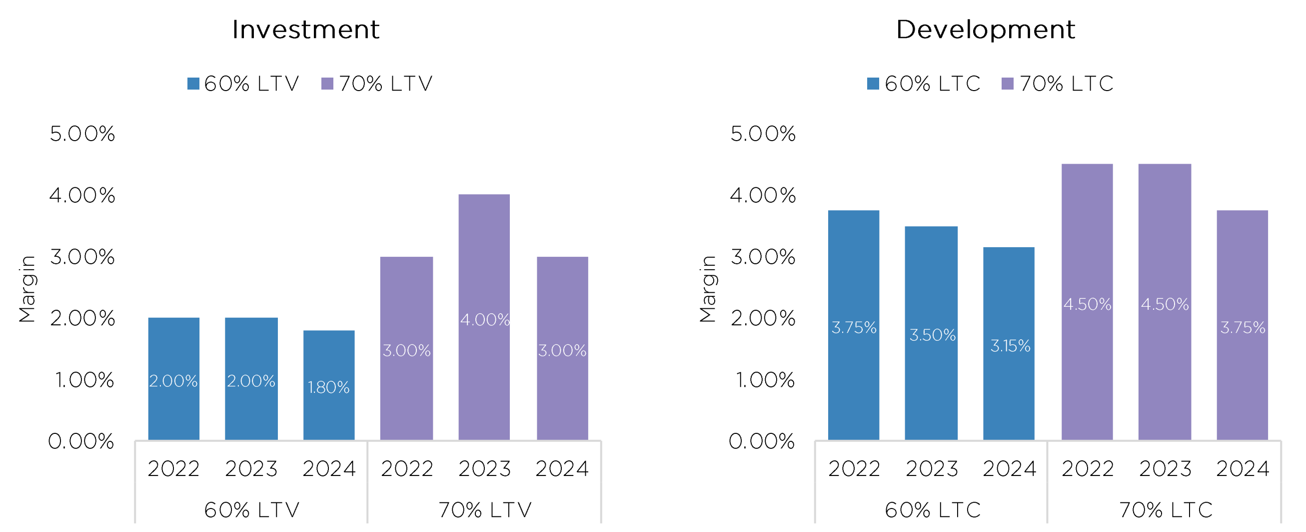
Beyond improving leverage and margins, competition between lenders has led to more borrower-friendly structures. Side by side loans are becoming more common, while interest rate margin step-downs are being set so that schemes achieve stabilisation more quickly upon practical completion.

Potential for yield compression?

The UK rental market has been characterised over the past few years by a supply and demand imbalance and high levels of rental growth. This supported investment values and meant yields proved resilient, particularly compared to other real estate asset classes such as offices and logistics. While there are signs that availability of stock is returning to pre-pandemic levels in some markets, rents continue to rise faster than the long-term average.

There is a growing opportunity for yield compression, with downward pressure coming from falling borrowing costs (a combination of a reduction in underlying forward rates, as well as lender competition leading to tighter margins) and competition for a small amount of opportunities from a growing pool of buyers. The path of future base rate cuts will be key to unlocking this potential.

Figure 1 Lender margins have reduced for Residential investment and development debt (Dec 2022–Dec 2024)



Source: Savills

UK Build to Rent attracted record levels of investment in 2024

Investment volumes for BTR broke new ground in 2024, reaching the £5 billion mark for the first time and surpassing the previous record of £4.8 billion achieved in 2022. This amount is based on actual capital deployed into BTR rather than Gross Development Values and excludes Co-Living.

The total was once again boosted by a bumper Q4, as investors worked to close deals before the year end. In three of the last four years, Q4 has seen the greatest share of annual investment.

Activity was supported by a resurgence in investment from outside the UK. Having fallen to 42% of investment in 2023, the lowest proportion since 2018, cross-border investment rose to 51% in 2024, and 56% across Q3 and Q4. This signals renewed optimism in UK BTR, particularly from North American capital, which deployed over £1 billion in Q4 alone. Starlight Investments agreed to forward purchase four Multifamily schemes, set to deliver over 1,800 homes in Manchester, Leeds and Basildon.

Single Family Housing (SFH) enjoyed a busy year again, with £2.5 billion deployed - another record.

Established players like Lloyds Living, Sigma Capital and Leaf Living meaningfully expanded their portfolios in 2024, alongside the emergence of new capital such as Greykite and Kennedy Wilson. We expect to see more investors pursue investment across both houses and apartments moving forward as part of a diversified UK residential investment strategy.

Funding new development remains the primary route to market for investors but there has been an uptick in the number of deals to purchase stabilised schemes. 25 operational deals occurred in 2024 and, as we reported in our paper over the Summer, we expect this number to rise as the market continues to mature.

Figure 2 Funding is the primary route to market

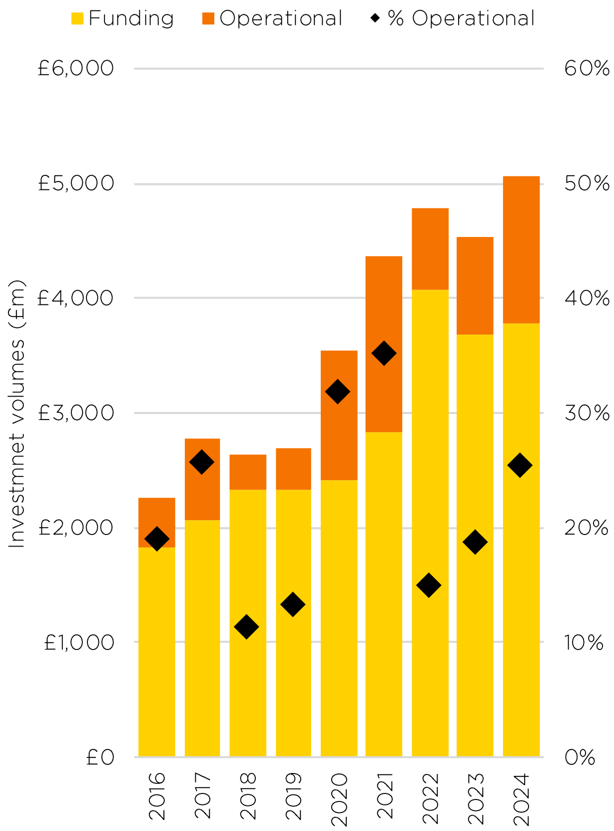


Figure 3 SFH has grown its share of BTR investment

Source: Savills

Developers and housebuilders are delivering more BTR homes

In recent years, developers have become more experienced at delivering homes for institutional investors, and a number have restructured their businesses to include BTR, particularly those with a strong presence in London.

Berkeley Group has established its own BTR platform in 2024 which plans to deliver around 4,000 homes over the next 10 years. While the plc housebuilder has had recent success selling homes to investors, it believes that there is also a strong opportunity in delivering and operating a stabilised portfolio. Opportunities to purchase large-scale, diversified portfolios are few and far between and such a portfolio would be an attractive proposition for investors once stabilised.

Most recently, Hill Group appointed a dedicated Build to Rent manager and entered the BTR sector in a deal with Lloyds Living for 246 BTR apartments in Stevenage. We expect to see more housebuilders pursue multi-tenure delivery strategies, particularly to accelerate delivery amid a recognition that sales rates, when they recover, will not return to the levels seen when Help to Buy was available.

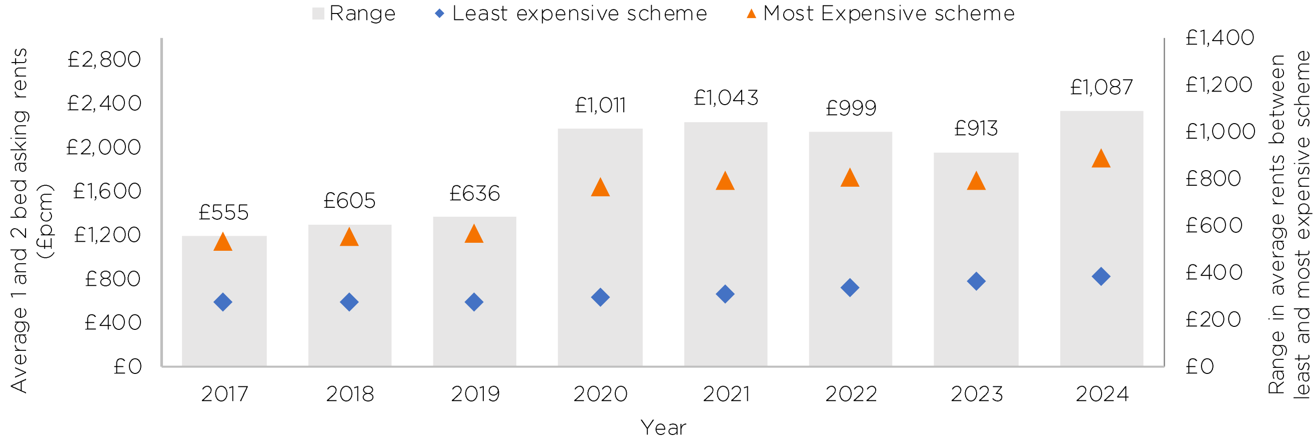
Build to Rent is adding supply across many price points

Build to Rent schemes, by virtue of being new, are often priced at the upper end of their local rental markets. Over time, schemes are superseded by newer and higher quality schemes that are able to target a higher price point. Older schemes still retain the high quality, responsive professional management that is synonymous with BTR, but the natural ageing of stock causes them to trend towards mid-market price points over time.

Nowhere has this been more evident than in Manchester, the most mature regional BTR market. As delivery in Manchester has grown, and a wider number of investors have entered the city, BTR has become more accessible to a much larger pool of tenants.

Over 19,000 Build to Rent homes have been delivered across Greater Manchester in nearly a decade, the majority of which are in the boroughs of Manchester (9,000 homes) and Salford (8,000 homes). Analysis of listings data in Manchester shows that over time, BTR is being offered across a greater spread of price points. In 2024, the average advertised rent (1 & 2 beds) at the least expensive BTR scheme was £825pcm compared to £1,912 at the most expensive. The range between the least and most expensive scheme was £1,087pcm. BTR therefore spans a much greater proportion of Manchester's rental market than in any of the past eight years (2017-2024).

Figure 4 The range of BTR rents in Manchester has widened



Source: Savills analysis of listings data, British Property Federation

New supply at any price point improves rental affordability

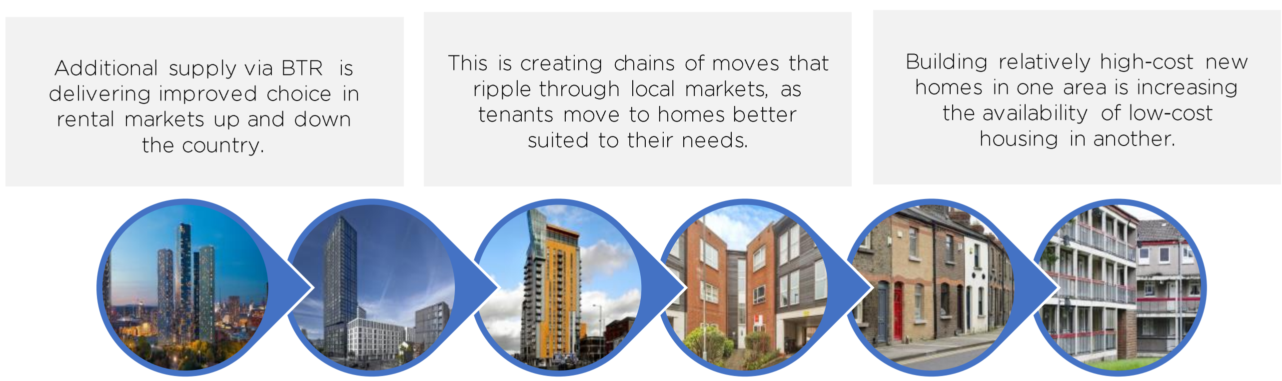
Increasing new supply in a market will exert downward pressure on housing costs over the long-term. Research by the Greater London Authority (GLA) found that building new market-rate homes makes other housing more affordable by creating a chain of vacancies that permeates across an entire housing market.

New homes deliver improved choice and affordability beyond the immediate beneficiaries. The chain of moves initiated by new supply means that one new home, even an expensive one, can improve the housing circumstances of several households.

For example, a household may have the finances and desire to move to a higher-quality home, but limited choice prevents this move. With the addition of a new build home for rent, this household will move and free up their previous home for another household to move up the ladder, and so on.

Whilst the addition of new market-rate housing will indirectly benefit lower income households, it will not provide the same benefit as directly building social housing and other kinds of Affordable housing.

Figure 5 New rental supply creates chains of vacancies in a rental market



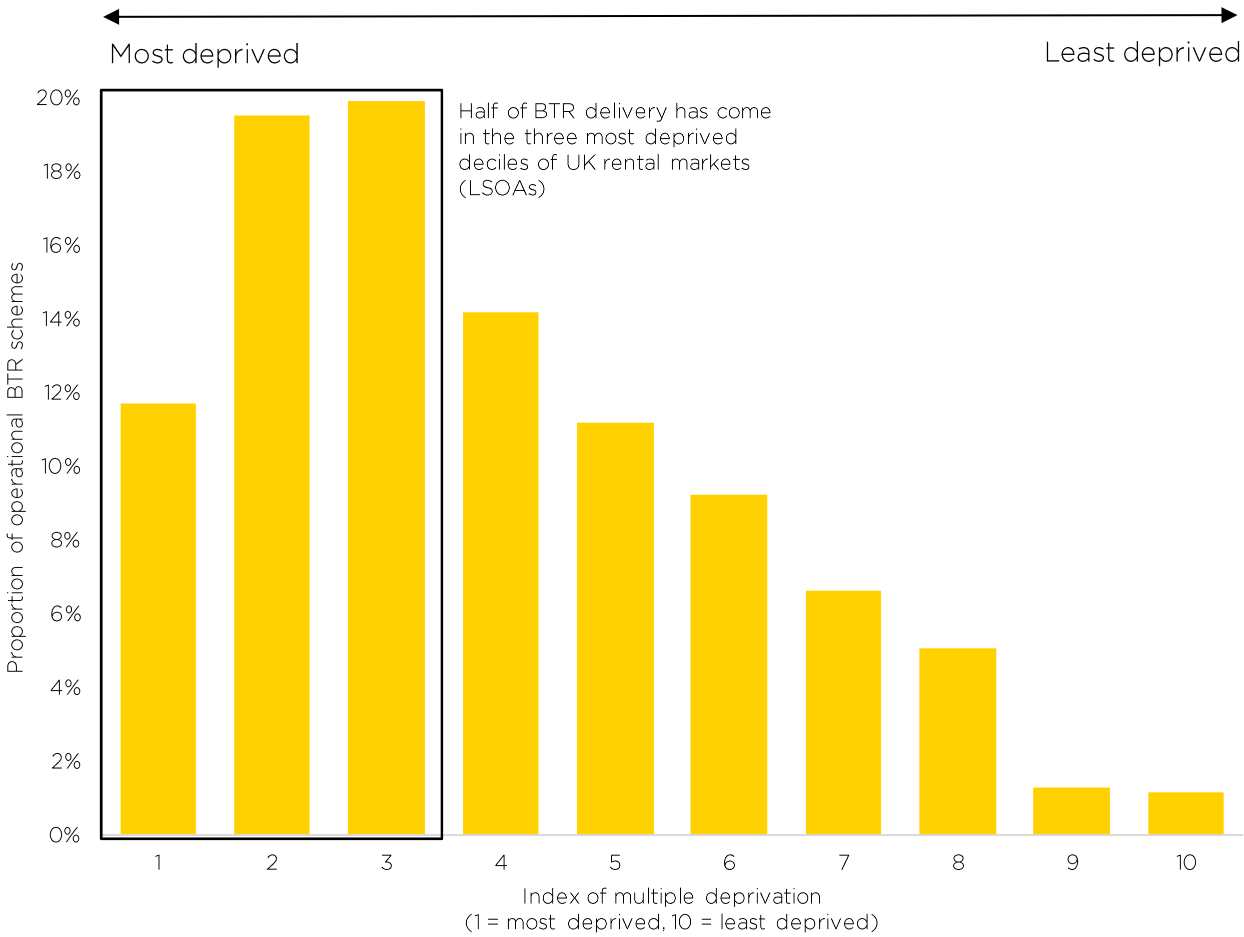
Source: Savills Research

From deprive to thrive: BTR is improving supply in deprived rental markets

Additional rental supply has helped to improve more deprived areas of the country. By delivering new homes and community facilities, BTR has made an important contribution to local economic growth as well as supporting placemaking. Delivery has been skewed towards lower value markets, where land values support development. Within London, where residential values are considerably higher, development has often focused on markets that have seen an improvement in transport or from regeneration where delivery is more viable.

Over half of Build to Rent delivery to date has come in the three most deprived deciles of rental markets, according to the ONS Index of Multiple Deprivation. These areas often contain former industrial brownfield sites which have struggled to attract investment into new housing stock over the last few decades. Brownfield development has been cited by the Government as a key source of housing delivery in the coming years and BTR will be instrumental in supporting this.

Figure 6 Most BTR delivery has come forwards in rental markets with high levels of deprivation



Source: Savills Research using British Property Federation, Molior, ONS

Supporting regeneration and unlocking development

New supply of BTR has a crucial role to play in UK housing delivery. The Private Rented Sector makes up a fifth of households in England according to the English Housing Survey. Under the UK Government's 300,000 home building target, delivering a fifth of new supply for private rent from 2030 means an annual requirement to deliver 60,000 new build rented homes.

As well as contributing to headline delivery, BTR has been an important source of regeneration in recent years. It has had particular success in cities that have pursued housing-led growth strategies such as Manchester and Leeds. Over 19,000 homes have been delivered across Greater Manchester to date, concentrated in the Combined Authority's six growth clusters - areas which aim to maximise the use of brownfield land through regeneration. These brownfield sites are often the subject of long-term, multi-phase plans and the deployment of capital through BTR investment can create new residential developments, reinvigorate communities and unlock stalled sites.

Salford's Local Plan explicitly recognises the potential of forward-funded investment and the continuing demand for BTR housing while Manchester City Council launched its 10-year economic plan in 2023 and within this, it highlighted the aim of delivering 36,000 additional homes by 2032.

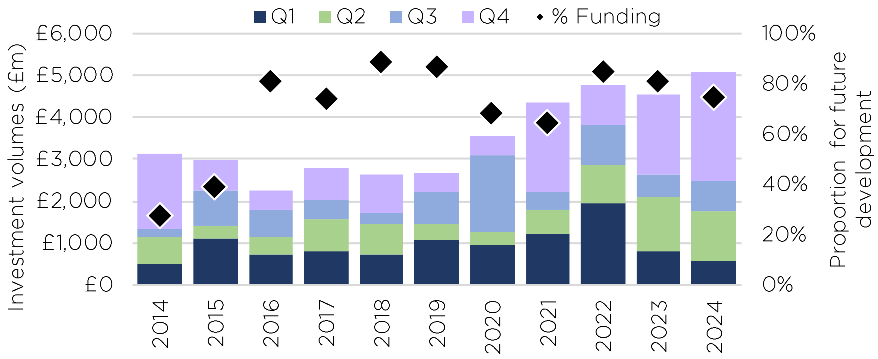
UK Build to Rent Investment

£5.1 billion was invested in 2024, with over half coming in the final quarter. This marked a record calendar year for the sector, totalling 6% higher than the previous record achieved in 2022. BTR made up 13% of all UK real estate investment in 2024, up from 5% in 2021, as investors continue to allocate more of their capital to the Living sectors.

Activity continued to concentrate in regional markets, with 88% of investment in markets outside of London in 2024, the highest proportion on record.

A key transaction in Q4 2024 was Ridgeback/AIMCo's purchase of 257 apartments in Walthamstow at Equipment Works, signalling there is still appetite to deploy capital into London for the right scheme. Other major deals in Q4 included Lloyds Living's deal with The Hill Group to forward-fund 264 BTR homes in Stevenage and the sale of a 608 apartment portfolio (operated by PLATFORM_) by Invesco Real Estate to LRC Group.

Figure 7 £5.1 billion invested in 2024, the highest year on record



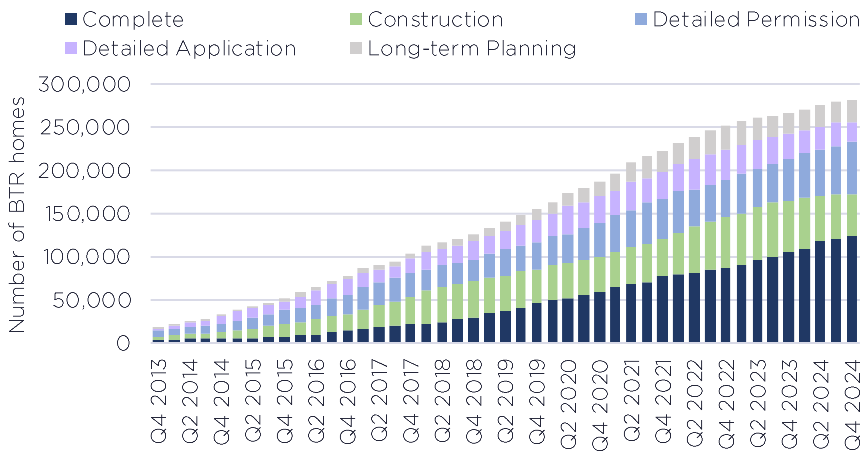
Source: Savills

UK Build to Rent Development

There are now over 123,500 completed Build to Rent homes in the UK, with a further 49,000 under construction. The additional pipeline, including those in pre-application, stands at 109,800 homes. In total, the sector therefore now totals 282,500 homes either completed or in the pipeline.

Data from Q4 shows units continuing to build out at a healthy pace, with operational stock increasing by 17% over the last 12 months. There has, however, been a drop in new starts, with the number of units under construction -18% lower than in Q4 2023. This comes amid continued cost pressures for developers. The number of homes with planning permission has increased by 28% year-on-year and so, with debt costs easing, there is optimism that these will translate into new starts on site in 2025, ensuring future delivery. The markets that saw the most BTR homes consented in 2024 were London and Birmingham. In London, Ealing and Croydon saw 2,000 and 1,200 new consents, respectively.

Figure 8 Continued growth in 2024 with increased planning consents



Source: Savills, British Property Federation, Molior

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