

Proposed Apartment Scheme at Queen Victoria Street, Reading

Report on Market Demand and Unit Mix

Prepared for Pepa Holdings

March 2017

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About Haslams

Haslams Estate Agents is one of the oldest and most respected companies in the Reading area having been at the forefront of the property market for over 175 years since 1838. Importantly, it also continues to be one of the most innovative and forward-thinking companies being instrumental in attracting international buyers to Reading and the Thames Valley new homes market.

Haslams is a multi-discipline property business and the market leader for new homes sales having sold in excess of 2,000 new units since 2005. Clients range from small local developers through to some of the UK's largest residential builders and global asset managers. All trust Haslams' experience, knowledge, and service and appreciate the level of investment we commit to our staff, technology and marketing facilities.

Background & Sources of Data

Background

This report has been written for Pepa Holdings by Haslams Estate Agents.

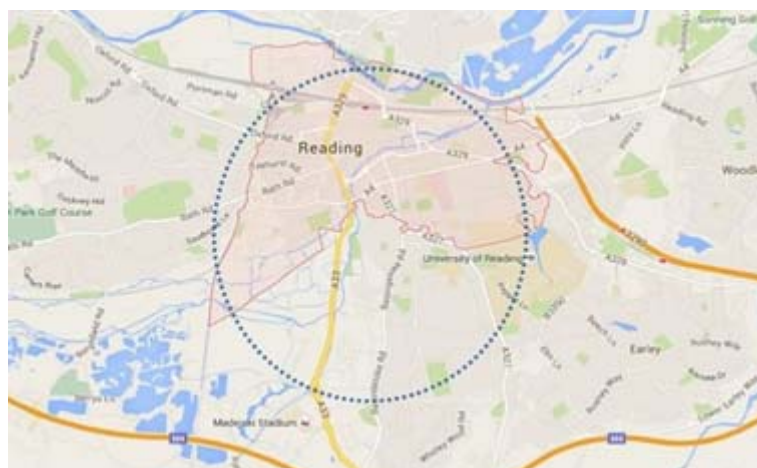
The report is based on data contained within Haslams' new homes database and supplemented with information from other objective sources including The Land Registry, property portals (e.g. Rightmove), and Haslams' proprietary residential sales system for second-hand homes.

Haslams new homes database is the most comprehensive and long-established database in the region, containing data collected on 8,000 units worth over £3bn of residential sales since 1998. No other organisation has access to such data nor has the level of market intelligence for Reading and the Greater Reading Area.

Data is collected and interpreted by 2 full time market research analysts.

Scope

This report provides information on the current market in Reading (as at February 2017) with focus on the apartment market and the demand for 3 or more bedroom apartments in particular. The focus of this report and the supporting market data for new homes and second hand homes is represented by the area on the map below (c.4 miles diameter). All reference to "Reading" refers to the area depicted by the blue outline:



Market Summary

Buyer demand in Reading at the time of writing is remains strong, with interest from both the main owner occupier and private investor markets in one and two bedroom apartments. To a lesser extent demand does exist for studio or micro apartments, though as is evidenced elsewhere in this document demand for larger (three bedroom units) is extremely limited.

A notable change in private investor/owner occupier balance has occurred following the EU-referendum with previous investor dominance (c.90% of new-build apartments were investment purchases in 2015). Despite negative press sentiment in the lead up to and immediately after the referendum, market reports and forecasts by institutional bodies, professional firms and lenders alike (recently The National Association of Estate Agents, PwC, Nationwide) are demonstrating an overall improvement in outlook whilst better-than-expected sales figures reinforce the property market's strength in the short-term.

The potential redevelopment of the Queen Victoria Street site responds well to the rebalance in demand from both owner occupiers and investors, being close to local amenities, within easy access of the IDR and the M4, as well as The Oracle shopping centre and mainline station.

Owner occupier and tenant demand for residential properties in Reading is currently steady despite some traditionally adverse conditions such as slowing capital growth and above-average supply of rental properties. This stability should continue as a consequence of Reading's strong fundamentals; a fast-growing local economy, high employment, and significant inward investment into infrastructure and redevelopment projects.

Recent activity in the Reading apartment market has largely been driven by investors and permitted development schemes which have resulted in spikes in sales values (£ sq ft) and the increased prevalence of micro-units. Permitted development rights have now been extended indefinitely and thus we have seen further, although not as extensive, inclusion of micro-units in new schemes.

There continues to be virtually no demand for 3 or more bedroom apartments. Larger units appeal to a very niche market and consequently care should be taken when considering incorporating such units as the value per square foot is lower than the smaller unit formats and the rate of sale is significantly slower meaning that this unit type will have a negative impact on a schemes viability, is likely to be a less attractive lending proposition and as a consequence this can adversely impact on the schemes affordable content.

It is strongly recommended that any decision regarding the mix of apartments should be demand led. Our research data indicates that in virtually any scheme at least 90% of units should be 1 and 2 bed units.

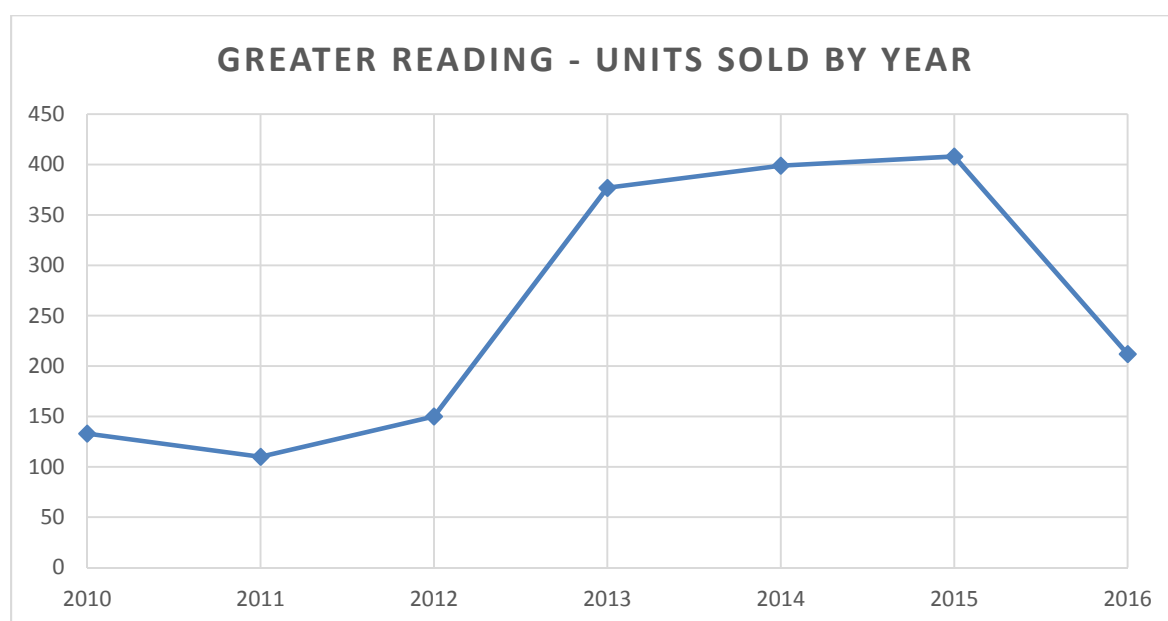
Two developments recently completed in Reading town centre offer a good example of the shift in demand; Tamar House (completed and launched in January 2016) and Summit House (completed and launched in May) are schemes built by the same developer and are comparable in terms of location and specification. All 20 apartments in Tamar House were reserved within 1 month of launch with 95% sold to investment buyers. Of the 21 apartments in Summit House around 50% were investment purchases. Our case studies contained within this report provide further detail.

New Apartments

Unit Sales

Since 2013, new apartment stock levels have increased significantly largely due to the introduction of permitted development schemes. Supply peaked in 2015 and we are currently experiencing a relative shortfall of new stock due to a lack of the kind of larger schemes prevalent in 2014/15. We expect levels of stock to increase in the years leading to 2020 with several large new-build schemes in the pipeline.

The table below shows the number of apartment reservations since 2010. Peaks have been achieved when larger scale developments such as Chatham Square and Hanover House have come to market:



Source: Haslams New Homes Database – data for Reading as depicted by map

Year	Units Sold
2010	133
2011	110
2012	150
2013	377
2014	399
2015	408
2016	212

Source: Haslams New Homes Database – data for Reading as depicted by map

Apartment Averages & Composition

There is very little demand for 3 or more bed units amongst investors or owner occupiers. The preference across both markets would be to reconfigure units into large 2 beds rather than small 3 beds. This is driven not only by investors who typically find letting 3+ bed units problematic and expensive (e.g. lack of demand leads to long void periods) but owner occupiers are typically singles or couples with little demand for extra space and/or amenity.

2016 Reservations				
Accommodation	Studio	1 bed	2 bed	3 bed
Proportion	1.5%	67%	30%	1.5%
Average size	248 sq ft	419 sq ft	617 sq ft	818 sq ft

Source: Haslams New Homes Database – data for Reading as depicted by map

Unit Values

Year to date average price per sq ft for new apartments in the area depicted above is £510 per sq ft. This is a blended value dependent on supply, demand and resulting inflationary pressures, and average apartment size; there are now some new benchmarks of value being set by developments comprising of 'micro-units' that deliver very high values per square foot.

Whilst the vast majority of smaller units have been sold off-plan to investors (Hanover House was sold to 95% investors in 2015/16), a shift towards owner occupiers has been illustrated by recent schemes (Summit House reservations are currently 50% to owner occupiers). This change in buyer profile has a notable impact on the optimal specification and size of new apartments, which should now ideally be slightly larger than has been typically built over the last 2 years with an enhanced specification and quality that is required due to post completion marketing needing to appeal more to owner-occupiers.

The data shows that new apartments in Reading have increased in value by an average of 9.7% per annum since 2010.

Case study – Chatham Square

Following the block purchase of the North Tower at Chatham Square in 2013 (arranged by Haslams to an investment company), individual apartment resales of the North Tower were delivered to the open market on a contract-reassignment basis by Haslams from November 2015. The table below illustrates these sales split to reflect the effect of the political events in April and June 2016.

The South Tower offered for sale the highest percentage of 3 bedroom units in a single block in recent years. The units were extensively marketed with particular emphasis placed on the rarity of 3-bed apartments in Reading.

Despite their rarity, the new 3-bed apartments were by far the worst performing unit type in terms of value and rate of sale. Demand was not forthcoming and as a result the average time to reserve a 3-bed apartment was twice as long as any other unit type.

It should be noted that the top floor 3 bedroom apartment reserved within 3 days of release and those of the higher floors reserved quicker than those on the lower floors which one would expect within a relatively central location with enhanced views and privacy.

Excluding the top floor 3-bed, the average rate of sale for 3-beds increased from 14 weeks to 17 weeks: almost 3 times longer than a one bed unit. Most 3 bedroom units were sold with the additional benefit of a parking space (buyers were therefore incentivised to purchase these units), however, the third bedrooms have typically been utilised as a study/storage.

Recent Development Case Studies

Tamar House, Station Road			
Total number apartments:	20	% Investors:	95%
Total sold:	20	Expected yield:	5%
Launch date:	January 2016	Average discount:	0%
Date of first reservation:	13 th Jan 2016	Parking arrangement:	None
Date of latest reservation:	12 th Feb 2016	Rate of sale:	5 per week
Marketing duration:	4 weeks		

Summit House, Greyfriars Road			
Total number apartments:	21	% Investors:	53%
Total sold:	21	Expected yield:	4.77%
Launch date:	29th May 16	Average discount:	(1.16%)
Date of first reservation:	29th May 16	Parking arrangement:	License
Date of latest reservation:	24th Sept 16	Rate of sale:	1.24 per week
Marketing duration:	17 weeks		

57 Castle Street			
Total number apartments:	12	% Investors:	67%
Total sold:	12	Expected yield:	4.80%
Launch date:	20th July 16	Average discount:	(1.73%)
Date of first reservation:	20th July 16	Parking arrangement:	£10,000 per space
Date of latest reservation:	21 st Nov 16	Rate of sale:	0.7 per week
Marketing duration:	17 weeks		

The Effect of Permitted Development (PD) Schemes

The year to date has seen the average apartment price per sq ft rise to £510 per sq ft. This has been partially skewed by certain types of development: especially those delivered under PD

Many PD schemes are characterised by 'micro-units': 1, 2, and a few 3 bed room units significantly under the standard unit size for traditional new-build. They have typically delivered very high returns (up to £705 per sq ft) but we believe these values to be artificially high and so do not recommend they are benchmarked unless being used as comparable evidence for other micro-units on other PD schemes.

Permitted development rights have now been extended indefinitely and thus we have seen further, although not as extensive, inclusion of micro-units in new schemes.

Having been particularly successful with investors of late, the recent shift in demand toward owner-occupiers has impacted on the relative success of more recent PD schemes with smaller units.

We predict that micro-units and PD schemes in general will be less relevant in coming years as the majority of office-space which would naturally lend itself to PD has already been converted or is under construction.

Second-Hand Apartments

Reading - Unit Sales

The second hand market in Reading has also experienced growth in sales volumes in recent years, the demand for property has out-stripped the supply, and this has led to prices rising beyond expectations as both owner occupiers and investors compete for what property has been listed.

Whilst the new apartment market has been driven by investors predominately with funds available to purchase off plan; the residential resale sector reflects a more balanced mix of purchasers as shown by the following Haslams sales data:

2012 to date				
Total town centre apartments sold	Studios	1 bed	2 bed	3+ bed
532	10	241	274	7

The second hand market for apartments is a very good barometer in terms of demand by unit type. If there was a demand for 3 bed apartments then it would be expected for owners to reconfigure accordingly and this would be reflected in the sales mix. Consequently, as the above tables indicate, there continues to be very little demand for 3 or more bed apartments in Reading.

Demand

The real purchaser demand by property type (i.e. “pull” demand from consumers vs “push” by new product coming to market) is best illustrated by assessing the profile of searches on Rightmove; the largest property portal in the UK.

Rightmove will not release the actual number of searches undertaken on property in Reading over the past 12 months but it has advised it to be in 5 figures (i.e. between 10,000 and 99,000 searches). This represents a good and reliable sample size.

The following table (source: Rightmove) shows the percentage of searches made by property type in Reading over the past 12 months. The data is based on unique email addresses of enquirers and does not take into account telephone calls.

Bedrooms	Flats	Houses	All
Not Specified	30.83%	26.49%	27.94%
0	12.63%	0.50%	4.53%
1	27.20%	4.74%	12.21%
2	25.29%	33.08%	30.49%
3	3.37%	27.17%	19.25%
4	0.44%	5.97%	4.13%
5+	0.24%	2.04%	1.44%

The data is split by the property type and by the number of bedrooms required by the enquirer. One and two bedroom apartments represent the most popular format (over 50% of the searches), followed by studios. Interest in larger apartment units of 3 or more beds is very low with people preferring the house format, reflecting the needs and requirements of home owners and young families.

“Pull” demand for apartments in Reading therefore appears to have been well matched to the historic mix of new apartments coming onto the market. There is no demand led evidence to suggest that constructing more 3+ bed units will increase demand.

Market Drivers

Reading is the capital of the Thames Valley – the most prosperous and fast developing financial district in the UK outside London. Key drivers of the growth in demand and price are:

Monetary and Fiscal Policy

In recent years, prices have been underpinned by long-term undersupply coupled with low interest rates. This has been reinforced by the recent Bank of England base rate cut, making borrowing more attractive, especially for first-time buyers who are already benefiting from some of the cheapest mortgages in recent times*. National sales figures for July showed an increase in sold prices of 0.5% - this, coupled with static rents is compressing yields to a near-unsustainable level for individual investors. First time buyers will subsequently continue to take advantage of falling investor demand and attractive borrowing options.

*HSBC is currently offering the lowest-ever rate of 1% for homebuyers; other lenders are likely to follow suit. Barclays is offering a 100% mortgage for first-time-buyers as of March this year.

Crossrail (Elizabeth Line)

The announcement in March 2014 that the Crossrail scheme will be extended into Reading has fuelled demand and has been cited as a driver for the substantial house price inflation reported since 2014. Network Rail's own research team suggest that property values within 1km of stations at Taplow, Slough and Maidenhead will increase by at least 74% in the period from 2014-2021 (compared to a predicted average of 50% in the same period). Reading is likely to experience similar uplifts.

Reading to Heathrow Rail Link

Network Rail announced in February last year that it would seek planning permission for a £500m rail link from Heathrow to the Great Western mainline. This would connect Reading through to Heathrow with a 28 minute journey time. Business groups suggest that this link could create up to £2 billion in economic benefits in the Thames Valley.

General Transport Links

Reading is designated as a key transport hub for the South East Plan and Reading Borough Council has an 'excellent' rating as a transport authority. In recent years a £65m investment was used to improve Junction 11 of the M4 and also several local road relief schemes are currently in construction. Reading is seen as a tremendously well connected town to live in.

Town centre investment

Reading is undergoing significant investment. Current examples include Forbury Place and R+ along with other refurbishment of large offices such as Reading Bridge House.

Reading – home to business

Reading is a major hub for tech businesses alongside other sectors. Global businesses are based in Reading: Thames Valley Park (BG Group, Microsoft, ING Direct and Oracle), Green Park (Huawei, Symantec and Quintiles), Reading International Business Park (Verizon). Surrounding areas also contribute to a vibrant zone of employment. The Thames Valley Local Enterprise Partnership aims to encourage other large businesses to Reading along with providing a platform for new start-ups (demonstrated by the Green Park Innovation Centre recently launched).

Purchaser Profiles

The Reading apartment market has been fuelled over the last 3 years by a surge in residential buy-to-let investment. Historically in the last peak of 2006/07 the investor to owner-occupier ratio in the town was as high as 70% in favour of investors, more recently we have seen the market completely dominated by investors; last year they accounted for 91% of all apartment purchases.

In the last few years investors in Reading have predominantly been private individuals holding a single property or multiple units (typically no more than say 10). The sale of Chatham Place North Tower (brokered by Haslams) changed the picture. These 139 units were sold to a UK based investor who then re-sold all units to Middle East based individuals.

There have now been more sales to overseas investors (particularly stock at Kennet Island by the Berkeley Group). Other than these two developments most of the other apartment sales are still being sold in smaller quantities to individuals.

The first time buyer market in recent years has been fuelled by the government backed Help to Buy scheme. A typical single first time buyer has a budget of around £200,000 but this can be significantly more with the provision of Help to Buy which negates the need for a large deposit and lowers the usual salary-multiplier requirements.

Potential Purchasers

Following the introduction of a second-home stamp duty levy in April the market has changed markedly in favour of owner occupiers. With further changes announced in 2015's Autumn budget in the way landlords are taxed (starting with a reduction of mortgage interest tax relief from 2017), the attractiveness of residential property as a sustainable profit-producing asset class will diminish.

For the proposed development at Queen Victoria Street we would anticipate the demand for a proportion of the units to come from owner-occupiers, comprising first time buyers, young professionals, newly single people and some down-sizers who wish to remain or retire to the area, possibly looking for a lock up and leave option. It is important to note that this category of buyer may be unable to make a commitment to an off-plan purchase due to the increased risk involved and length of time to complete on the purchase.

First time buyers – with or without parental assistance are now much older with larger savings and more stable incomes. Typically buyers are now aged in their 30's and may be well educated professional people who have paid off university loans, they may consider sharing to get on the property ladder. This buyer profile will be attracted to the relative affordability of the area in comparison to other parts of Berkshire and notably London.

Young professionals – young couples or singles attracted to a Reading lifestyle and proximity to local amenities and entertainment. This group would include young people who have already made their first purchase and now want to upgrade and have the ease of maintenance and a better class of specification as these buyers are often 'time-poor'.

Potential Tenants

Around half of the ultimate residents are likely to be those who are entering into Assured Shorthold Tenancies (AST's). For central apartments tenants are typically in the 20-40 age range and we see a large sector of demand from corporates who are often looking for accommodation for relatively short periods – one or two years.

A tenant seeking to rent an apartment in Reading would typically need to earn at least £30,000 per annum in order to qualify through the referencing process. The student market for UK nationals is mainly catered for by specific providers (Fresh Student Living is an example). Recently we have seen an increase in overseas students who have larger budgets and are seeking higher quality accommodation.

In August 2016 the Haslams lettings team achieved its highest ever number of lets agreed in a single month (97), whilst available stock levels remain at an above average level a healthy level of demand compliments this increased supply. We see no signs of demand from tenants weakening and levels of rent are being sustained.

Typical monthly rents in Reading for new or nearly new apartments are currently:

Studios:	£700 - £750 per calendar month
1 bed apartments:	£950 - £1,100
2 bed apartments:	£1,100 - £1,350
3 bed apartments:	£1,450 plus

Due to the age profile and affordability the most popular apartment choices for a typical tenant are 1 and 2 bedroom apartments. In our experience there is less likelihood of void periods with this type of accommodation. Potential tenants for 3 bedroom apartments are usually executives looking for a property close to the station or three sharers. Families tend to opt for a house with a rent of a similar value.