Build to Rent in Scotland
Market Briefing
Summer 2017

RETTIE

Rettie & Co. advised Moda Living on their purchase of Springside, Edinburgh. The mixed use scheme will deliver 500 Rental Units with a GDV over £200m.

Build to Rent in Scotland - Is the wait finally over?

Build to Rent (BTR) has been a sector that has caused much excitement and anticipation in recent years, but, until now, the actual delivery of units in Scotland has been mainly a theoretical, rather than a practical concern. In 2017, this looks set to change.

Both Edinburgh and Glasgow have seen major announcements of large-scale BTR projects now in planning for development. These schemes will supply over 2,500 BTR units in Scotland's two largest cities. While this is a step forward, Scotland still lags London and other major regional centres in leveraging institutional investment to deliver any volume of new housing at pace.

Having recently advised on the largest BTR deal in Scotland, and other prominent BTR schemes as well as delivering over 600 properties into rental tenure, in this Market Briefing, we consider some of the factors shaping the Scottish BTR sector. We also outline some of the drivers, challenges and opportunities facing the sector if it is to break through into the mainstream in Scotland.

Andrew Meehan
Senior Researcher

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What is Build to Rent?

There has been much hyperbole about the shifting tenure of the UK housing market and its future in the private rental sector (PRS). This has led to numerous terminologies being adopted; Institutional PRS, Private Rental Communities and, in the US, Multi-family Housing. Currently in the UK, Built to Rent (BTR) seems to be the prevailing acronym of choice when discussing blocks of apartments, under single ownership and management, for rental in the private sector. While this concept is fairly straightforward, what is delivered and the mechanisms of funding can vary widely in this embryonic UK sector.

The Multi-family Housing market in the US is well-established and typically accounts for around 25% of residential construction annually[1]. Like the UK, the number of people moving into the rental tenure in the US has been on the increase and is now up to 35% overall, with 25 million in BTR [2]. The US BTR market predominantly targets younger professionals, with a premium product through the provision of contemporary units with an aspirational specification, additional services and lifestyle amenities, allowing an average premium of c.20% on average market rents [3]. This premium clearly makes BTR an attractive investment proposition. The BTR model is also well-established in Europe, e.g. in Germany, where 60% of adults are in the PRS; this equates to 24 million households in the sector, with 9.5 million of these units being built and managed by institutions.

So why is Build to Rent only now being promoted as the tenure of the future for the UK when it's been active in the States for so long, and is so well-established with our European neighbours?

The UK is under provided in terms of investor housing

Fig1. Ownership Distribution of Occupied Dwellings by Country

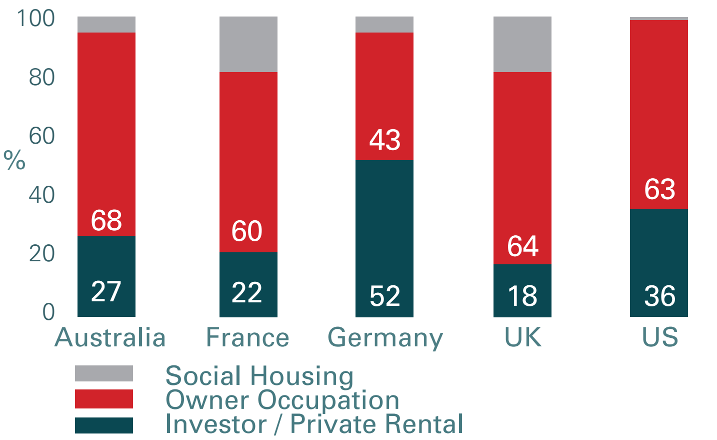
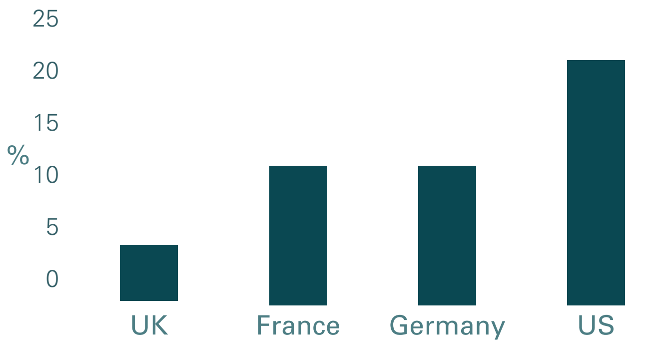


Fig2. Share of Residential Holdings in Institutional Portfolio Holdings



Source: IPF Short Paper 21: IPD Multinational Index Spreadsheet
Notes: IPD estimates volumes of institutional property holdings by property sector on the basis of IPD's actual databank sector values. Estimates are IPD approximations of the unleveraged total value. 2012

Sources: IPF Short Paper 21: UK: ONS, 2011 Census, Tenure, local authorities in the United Kingdom; Netherlands: CBS, Woningvoorraad naar eigendom, regio, 2006-2012; Germany: Zensus 2011, Buildings with residential space depending on type of ownership of the building; France: INSEE, Statut d'occupation des résidences principals; United States: Census 2011, Estimates of the Total Housing Inventory for the United States: 1965 to Present, and HUD, Number of Public Houses; Australia, ID, Housing tenure.

Why Build to Rent Now?

The Global Financial Crisis lies at the heart of many of the drivers that have driven BTR in the UK by creating a series of circumstances that have either changed, or amplified, shifts in the housing market and economy.

In the post-war period, owner occupation rose consistently, taking advantage of an unprecedented level of housebuilding, combined with a prevailing political philosophy of owner occupation. The Conservative Government under Margaret Thatcher engrained this belief with the introduction of the Right to Buy. Moving towards the 2007 market peak, soaring house prices and enthusiastic mortgage lending drove more and more people into home ownership. These mortgages financially underwrote the housebuilding sector.

Then came the financial crisis, with a collapse in private housebuilding and tightening lending restrictions with the mortgage market review (MMR). Recession and wage stagnation solidified the retreat of mortgage lending. This has meant that younger would-be home owners can no longer meet deposit requirements at 90%- 95% Loan to Value (LTV), so remain in the PRS longer, despite monthly rental costs often outstripping mortgage repayments.

At the turn of the millennium, 53% of 16 to 34 year-olds were owner occupiers, and 13% were in private rental. Over the past 15 years, this tenure balance has reversed, with 30% now owner occupiers, and 41% in the PRS. Conversely, owner occupation in the 60+ age bracket has continued to rise to almost 70%, with over 55% of households owned outright. The combination of rising house prices supported by limited new build delivery, limited credit and stagnant wages has kept many younger buyers effectively locked out of owner occupation. The average first time buyer now takes 7 years to save for their deposit and this has pushed the average FTB age into the 30s [4]. Simplistically, these circumstances have created a strong demand for housing in the PRS from under 35s urban dwellers, who can afford monthly costs, but not the capital requirements to own a home.

So while housing demand is strong, the number of mortgages that once bankrolled new housebuilding are still 40% below 2007 levels. A new model for funding housing is required.... *Enter Build to Rent.*

1 https://www.forbes.com/sites/billconerly/2014/05/19/multi-family-real-estate-forecast-2014-2020/#576f976665aa
2 https://www.estateagenttoday.co.uk/industry-views/2015/11/build-to-rent--what-we-learn-from-germany-and-the-us
3 http://www.chapmantaylor.com/en/insights/article/residential-from-prs-to-build-to-rent-to-multifamily-housing-uk/en/
4 https://static.halifax.co.uk/assets/pdf/mortgages/pdf/halifax-first-time%20buyer%20review-13-january-2017-housing-release.pdf

Advantages of Build to Rent

Construction Risk
Development can be completed for a single client reducing multiple buyer risk.

Absorption
Removing mortgage affordability constraints, especially for the sub 35-year old target market, allows far quicker occupation in the rental sector.

Speed of Delivery
Units can be sold en masse to a single entity rather than sold to individual buyers at a constrained sales rate.

Management
Centralised management and maintenance can deliver greater efficiencies and savings across the development.

Mortage Reliance
The delivery of housing is not tied to the constraints of mortgage affordability to underwrite new housing development.

Placemaking
Fast delivery and occupation can assist with regeneration and large-scale developments by creating a sustainable community quickly.

Efficiencies
Faster construction programmes can allow for the capital being deployed to be recycled more quickly into other future schemes.

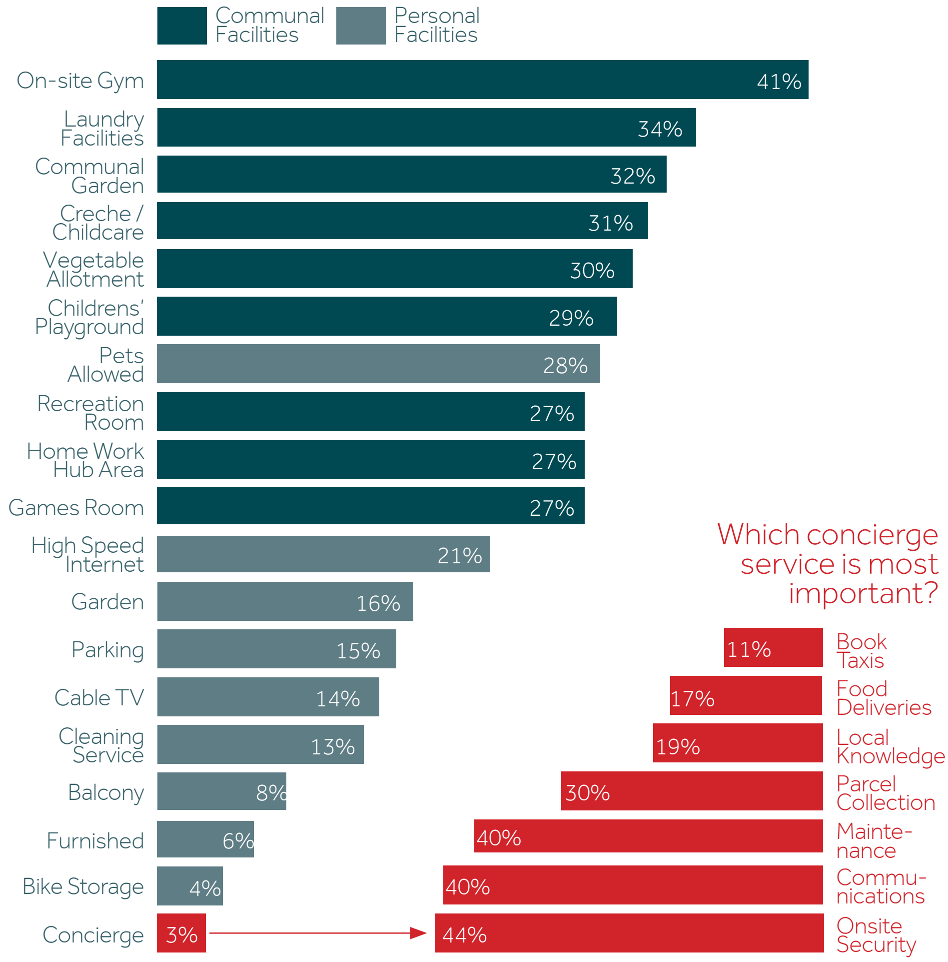
Tenure Flexibility
While units may be delivered quickly into PRS, units can revert to alternative tenures at a managed rate in the future.

PRS Amenity

One feature that sets BTR apart from the wider PRS is the package of services and amenities that are offered. In the mature US market, the focus on the 'client', rather than the tenant typifies the sector as a lifestyle product. The targeting of rents at a premium to broader market rents is tied-up in the aspirational lifestyle being promoted through on-site gyms, concierge and a range of additional amenities and services from delivery rooms to cinemas and shared entertaining space.

The first BTR schemes saw little in the way of additional inclusive on-site amenity beyond a concierge, but as the sector matured, competition drove facilities. The most highly valued service that comes top of residents' surveys are lifestyle and convenience-based – on-site gyms, pools, communal outdoor space, parking, storage and a concierge. Increasingly, the key for communal space has been flexibility. In many US schemes, for example, expensive cinema rooms are now being replaced with yoga studios as tastes change.

What would tenants pay more for?



Source: LSL 2017 Tenant Survey

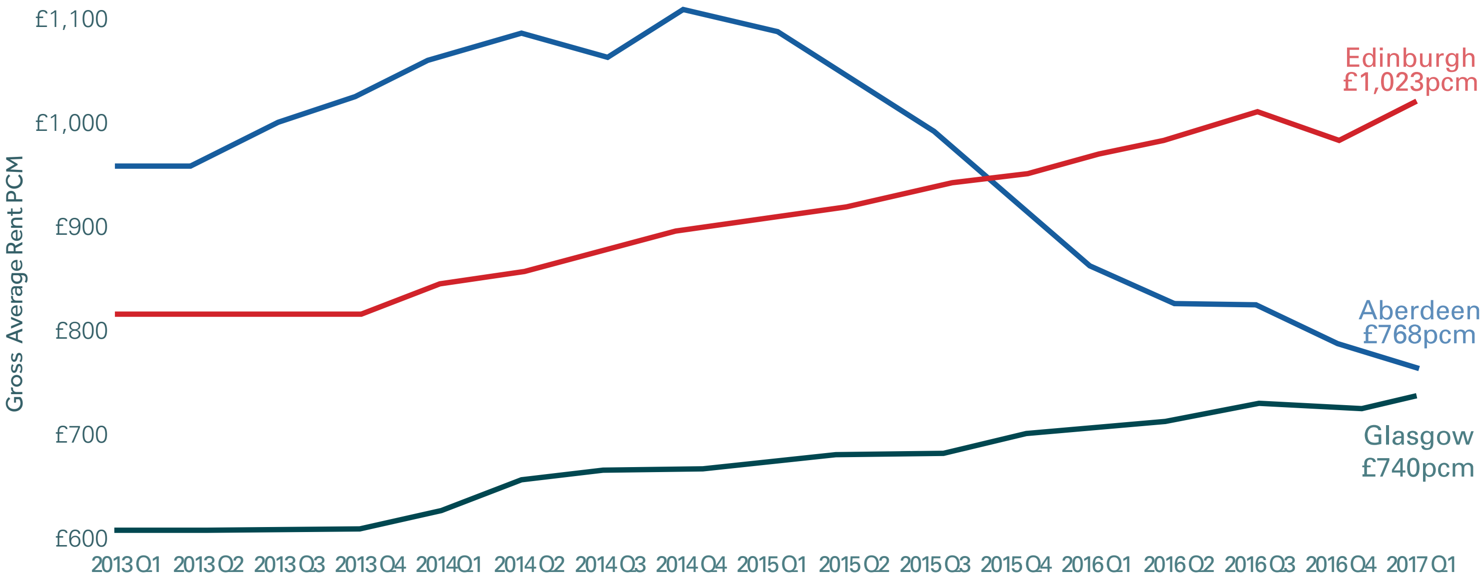
The Rise of the Rental Market

Underpinning the rise of BTR has been the rise of the PRS. As a percentage of all households, the PRS has doubled from 7% nationally, to 15% in the past 20 years. In Edinburgh, the PRS now accounts for 27% of households, 21% in Dundee, and Glasgow and Aberdeen are both at 18%.

Combined with historically low levels of new housebuilding and mortgage unaffordability, this has made it the dominant tenure in younger age brackets and driven the demand in the rental market, supporting rising rental values in most urban markets (Fig3).

There is an obvious exception in Aberdeen where rental values have slumped following the drop in oil prices. With rental growth outstripping house price growth across Scotland, yields have strengthened for investors over recent years.

Fig3. Rental Growth has been strong, with the exception of Aberdeen
Comparison of Gross Yields & Change in Avg. Price since the Market Peak in Real Terms



Source: Citylets / Rettie & Co. Research

The PRS Premium

A key driver of investment in BTR development in more established markets has been the ability to target the prime rents and achieve a premium over the wider market. While there are limited BTR schemes in Scotland to establish the presence of such a premium, where quality contemporary rental product has been delivered into the market, a clear premium over the local market can be seen.

In Edinburgh, two city centre developments illustrate this premium. Fountainbridge, which has 48 BTR units, has been achieving c.30-50% above the city-wide average and 15-20% above EH3, which includes the Edinburgh New Town. Quartermile, which while not BTR, has seen high levels of BTL investment and has been achieving between 50-100% premium over Edinburgh-wide rental values. Quartermile also achieves a premium of 30-50% over the EH3 postcode area.

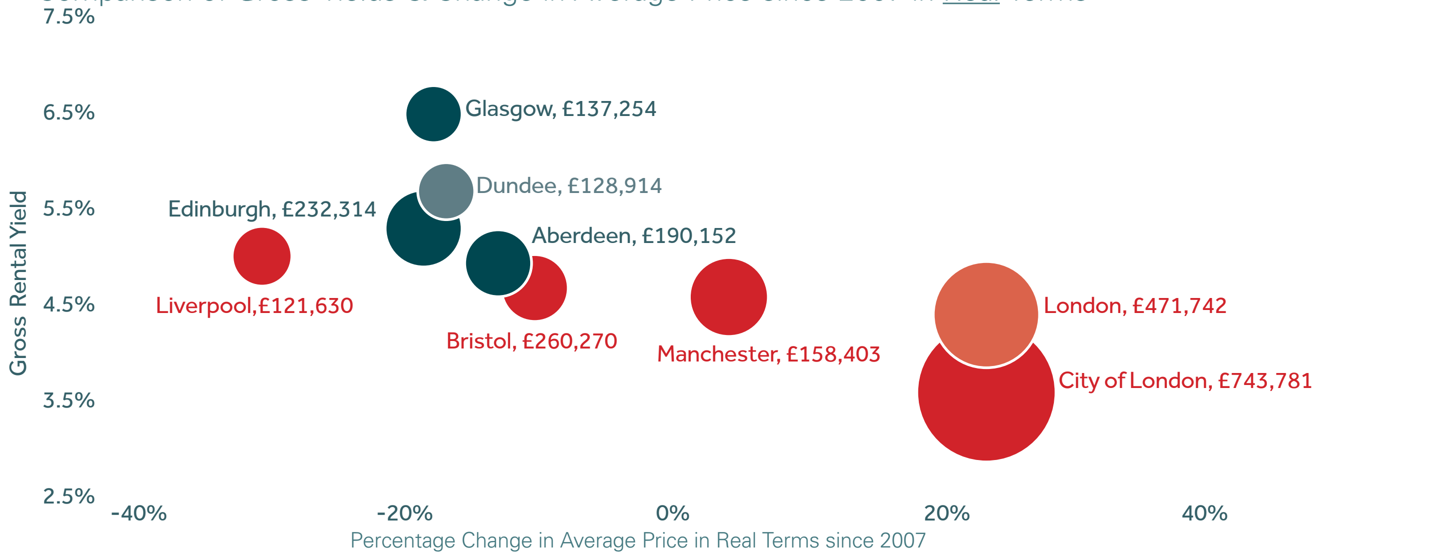
Fig4. New build development can achieve strong rental premiums
Comparison of Average Rents by Bed against Edinburgh Average

Source: Citylets / Rettie & Co. Research

The Scottish Context

Investment in Scotland has undoubtedly been hesitant since the first announcement of the Scottish Independence Referendum. Since then, there has been the EU Referendum and potentially a second Scottish Independence Referendum. For some domestic and international funds, this has removed Scotland from their target list. However, for other investors, the current perceived specific "Scottish risk", is counteracted by strong underlying investment fundamentals. The major Scottish cities, compared with their southern counterparts, have strong yields, low entry prices, growth potential, demographic drivers and market demand underpinning an investment case. This has led to the greenlighting of a number of high profile deals in Scotland's cities. Scotland may now become more attractive, after the recent UK general election, an outcome of which is to make Indy Ref 2 much less imminent.

Fig5. Scottish Cities have higher yields, lower capital requirements and potential for market growth
Comparison of Gross Yields & Change in Average Price since 2007 in Real Terms



Source: Land Registry / Registers of Scotland / VOA / Citylets / Bank of England

Drivers of BTR Demand

Demographic
A concentration of sub-35 year olds are the key target market. Rising population projections are also positive.

Economic
Strong levels of professional tier employment with suitable earnings. High education levels are also a positive.

Tenure
A pre-existing vibrant PRS, typically over 30% of all households, is a strong indicator of activity and demand.

Location
Accessibility to urban amenities and employment centres. Transport, services and recreation are key.

Product
The housing product being delivered has to match affordability and aspiration of target market.

Fig6. Scottish Cities have strong indicators of demand
Comparison of Key Performance Indicators by UK City

		London	Manchester	Liverpool	Edinburgh	Glasgow	Aberdeen
House Prices	Average Price	£471,742	£158,403	£121,630	£232,314	£137,254	£190,914
	Nominal % change from 2007 peak prices	58%	14%	-7%	4%	5%	11%
Population	Forecast growth to 2037	27%	19%	11%	27%	18%	18%
	% 16 - 35 years old	31.5%	40.4%	33.9%	33.3%	33.6%	34.5%
Rents	Average Rents	£1,714	£615	£502	£1,023	£740	£768
	PRS Tenure (% 2011)	24%	28%	20%	24%	17%	17%
	Avg Gross Rental Yields	4.4%	4.7%	5.0%	5.3%	6.5%	4.8%
Employment	Employment Rate	78.3%	69.0%	69.2%	74.4%	71.6%	76.1%
	Avg. Earnings	£653	£468	£497	£560	£524	£554
	NVQ4+ Education Level	58%	39%	35%	59%	44%	53%

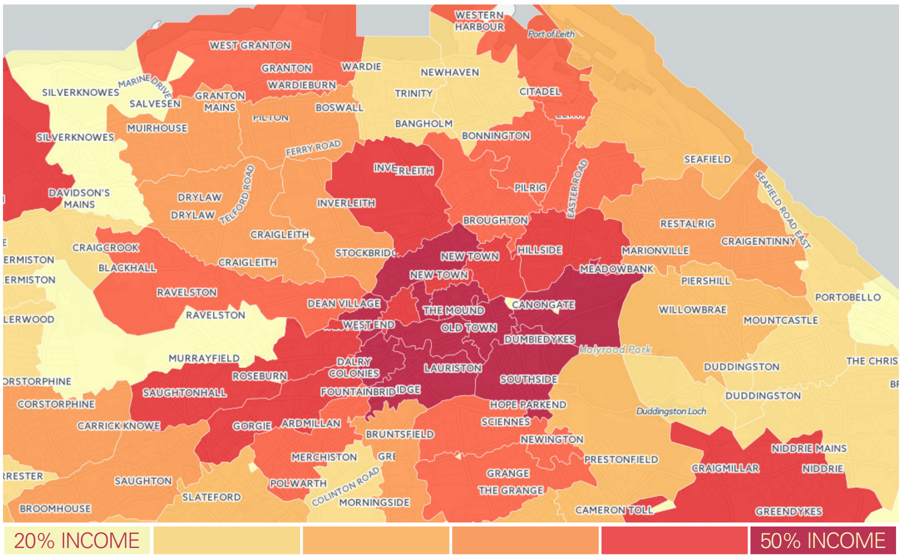
Source: Land Registry / Registers of Scotland / VOA / Citylets / Bank of England / Census / NOMIS

Rental Affordability by City

EDINBURGH

While the New Town is the prime rental location in Edinburgh, the rise of quality rental stock has materially impacted the market. Not only is Quartermile one of the most expensive rental locations but, along with Fountainbridge, the new build rental stock has been achieving rents at a marked premium to the surrounding area and level of earnings. This means that to rent an average 2-bed apartment in either location, it would cost over 40% of the average gross household income for the local area.

Fig7. Ratio of Household Income against Average 2-Bed Rents



Top 5 Highest Apartment Rents
Average 2-Bed Rent by Address

St Vincent Place	£1,985pcm
Grosvenor Crescent	£1,858pcm
Quartermile, City Centre	£1,837pcm
Moray Place, New Town	£1,835pcn
Rothesay Terrace	£1,750pcm

Based on 2-Bed apartments advertised in the past 12 months

Highest Cost Against Local Income
Avg 2-Bed Rent vs Local Avg Income

EH3 9	- Quartermile	47%
EH3 8	- Fountainbridge	39%
EH8	- OldTown/Abbeyhill	38%
EH3 7	- West End	37%
EH1	- City Centre	37%

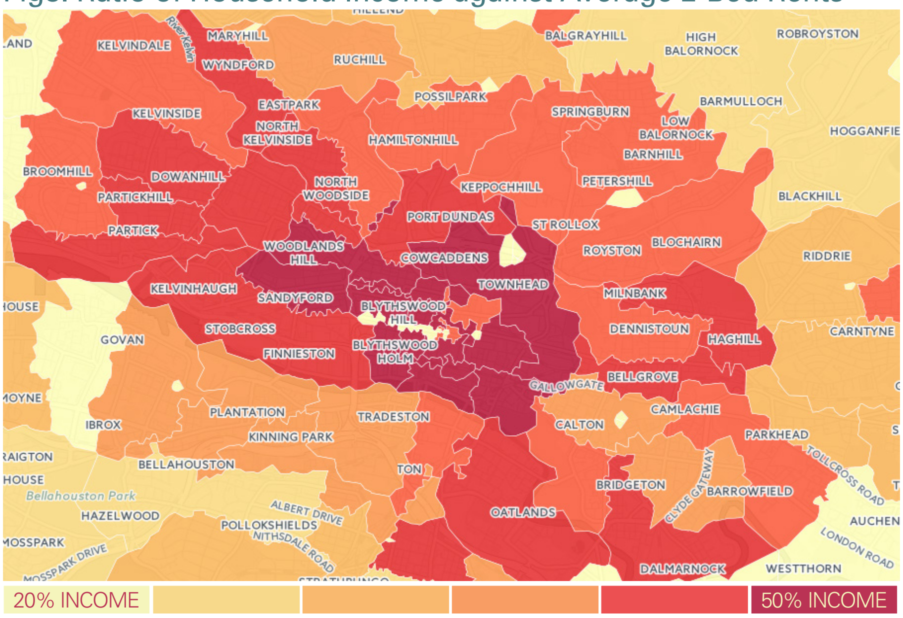
Based on 2-Bed apartments advertised in the past 12 months

GLASGOW

The Prime West End remains the most expensive place in Glasgow to rent a 2-bed apartment. This is also the case when comparing the ratio of household income against average 2-bed rents.

In the West End, renting an average flat in G3 7 would require almost 50% of the average gross household income for the area. This reflects the high rents achieved in the area despite strong earnings. The City Centre and Yorkhill have lower earnings, but still have strong rental markets which also drive up this ratio.

Fig8. Ratio of Household Income against Average 2-Bed Rents



Top 5 Highest Apartment Rents
Average 2-Bed Rent by Address

The Park	£1,810pcm
Devonshire Terrace	£1,745pcm
The Terraces on GW Rd	£1,525pcm
Woodside, West End	£1,450pcm
Merchant City	£1,350pcm

Based on 2-Bed apartments advertised in the past 12 months

Highest Cost Against Local Income
Avg 2-Bed Rent vs Local Avg Income

G1	- Merchant City	46%
G4	- City Centre North	40%
G3	- West End	37%
G2	- City Centre	37%
G11	- Yorkhill	33%

Based on 2-Bed apartments advertised in the past 12 months

Rental Affordability by City

ABERDEEN

The Inner West of Aberdeen remains the most sought after area of the city. With traditional stock in these areas competing alongside new build developments such as May Baird Gardens and Dempsey Court.

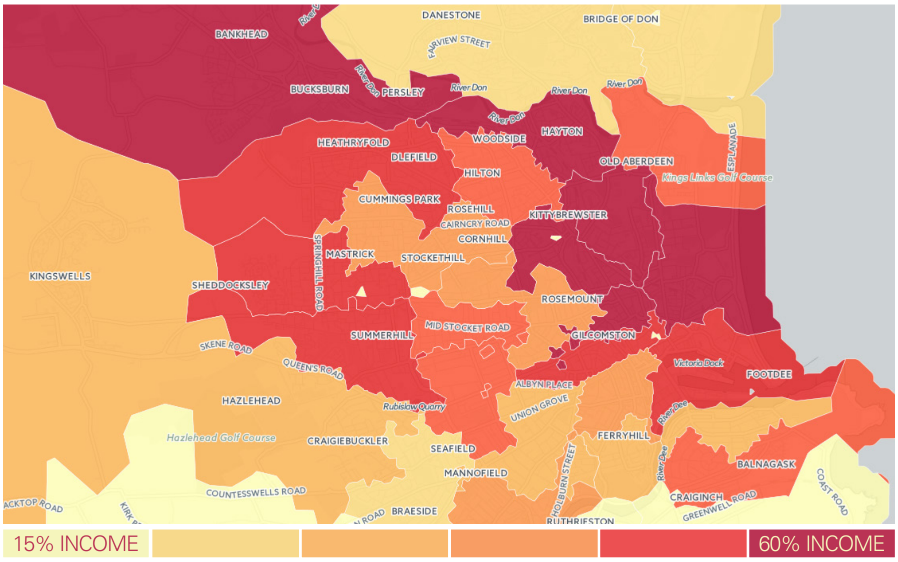
Falling rents in the city since 2015 have driven down the ratio of 2-bed rental values against local income. The highest ratios are now in areas with moderate earnings but where new build stock has come to the rental market, especially to the north of the City Centre.

Top 5 Highest Apartment Rents
Average 2-Bed Rent by Address

King's Gate	£1,429pcm
Queen's Gardens	£1,400pcm
May Baird Gardens	£1,340pcm
Fountainhall Road	£1,300pcm
Dempsey Court	£1,219pcm

Based on 2-Bed apartments advertised in the past 12 months

Fig9. Ratio of Household Income against Average 2-Bed Rents



Highest Cost Against Local Income
Avg 2-Bed Rent vs Local Avg Income

AB25	Union & Esplanade	29%
AB24	Old Aberdeen	27%
AB21	Bucksburn	25%
AB16	Mastrick	25%
AB15	Summerhill	25%

Based on 2-Bed apartments advertised in the past 12 months

DUNDEE

The Dundee rental market shows the current transformation of the city through investment and development. The top rental values achieved for 2-bed flats are all within new build developments, either on the shore or city centre. These developments are offering aspirational contemporary living with strong lifestyle amenities.

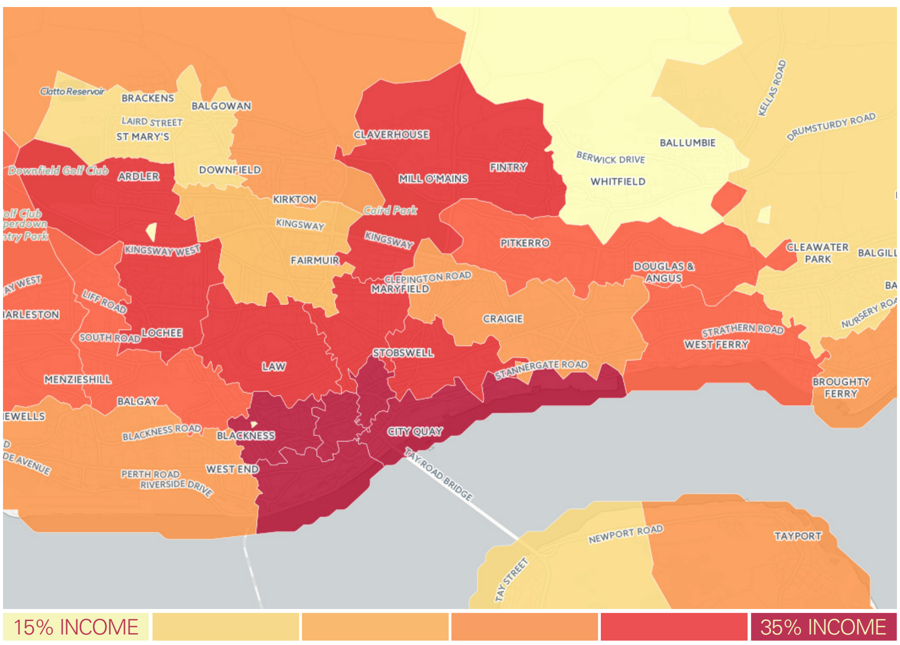
The willingness to pay extra is illustrated by City Quay achieving the highest ratio of average 2-bed rent against local income levels.

Top 5 Highest Apartment Rents
Average 2-Bed Rent by Address

Riverside Drive	£1,095pcm
Mortimer Drive	£950pcm
Bader Square	£875pcm
Mcvicars Lane	£853pcm
Marine Parade Walk	£825pcm

Based on 2-Bed apartments advertised in the past 12 months

Fig10. Ratio of Household Income against Average 2-Bed Rents



Highest Cost Against Local Income
Avg 2-Bed Rent vs Local Avg Income

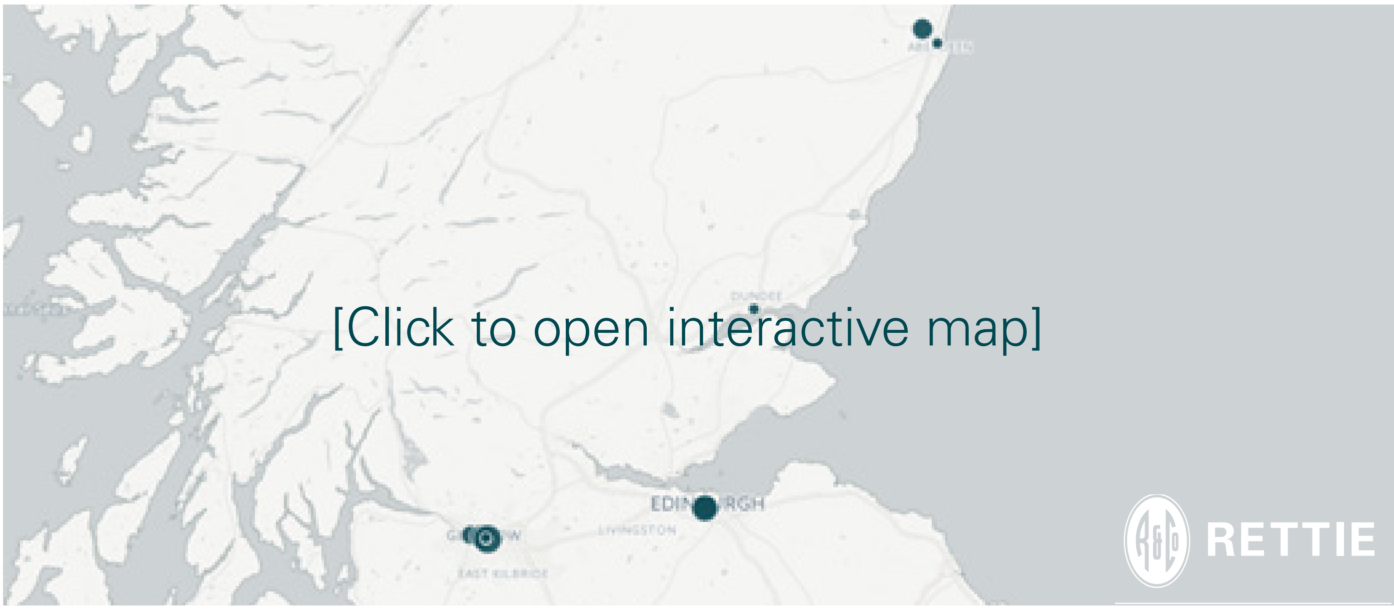
DD1 3	City Quay	34%
DD1	City Centre	29%
DD4 6	Stobswell	24%
DD3 6	Coldside	24%
DD3 7	Maryfield	23%

Based on 2-Bed apartments advertised in the past 12 months

Current Supply & Forthcoming Pipeline

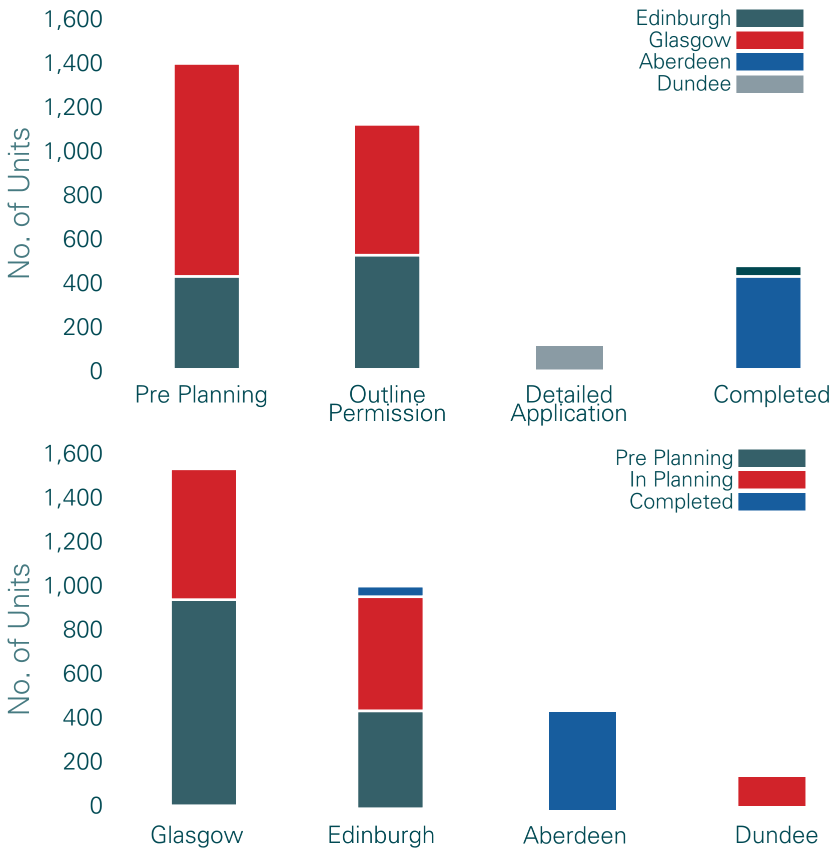
There is already a BTR Scheme operating in Scotland at Forbes Place, Aberdeen (345 units). The high profile announcements of schemes by Moda Living / Apache at Fountainbridge in Edinburgh, and Holland Park in Glasgow, account for almost 1,000 BTR units. In Glasgow, the Candleriggs and Merchant City schemes also recently announced a further 1,000+ units. Meanwhile, in Edinburgh, India Quay has the potential to deliver an additional 400 units. There are a number of other sites that could contribute up to 3,000 more units. This pipeline is likely to see Scotland's overall BTR stock rise from around 500 units to over 3,000 in the next few years. However, this would still only represent around 5% of all BTR current and planned in the UK.

Fig11. Scotland's Two Largest Cities are set to see over 2,000 units delivered in the next few years.
Map of Current & Planned BTR Schemes in Scotland [click to open online map]



Source: Land Registry / Registers of Scotland / VOA / Citylets / Bank of England

Fig 12 & 13. BTR delivery is focused in Edinburgh & Glasgow
Scottish BTR Units by Planning Stage (above) / City (below)



UNITS PIPELINE BY CITY

1500 GLASGOW

1000 EDINBURGH

350 ABERDEEN

City Profile: EDINBURGH

Edinburgh has proven to be somewhat challenging for the delivery of BTR, despite strong demand drivers. A population with a high concentration of young well educated professionals located in a compact city centre and a vibrant existing PRS makes BTR highly viable.

A major barrier to BTR delivery has been strong sales values and land prices, which have made BTR less competitive than traditional sales or other land uses, such as student housing, in the city centre. However, BTL investors have achieved strong premiums in new build developments in the city centre, showing the city is suitable for prime BTR product. The likes of Quartermile and Fountainbridge have proven popular with BTL investors and tenants, achieving PRS premiums of between 30-100% over local market rents. This level of performance underpins Moda Living's project to deliver 500 BTR units at the 3.5 acre Springside site, adding to the pre-existing 48 units already operating there.

However, BTR is also emerging in the guise of Mid Market Rent (MMR), in what might have previously been deemed more secondary locations such as Leith and other parts of North Edinburgh. Sailmaker Apartments by Teague Homes is delivering 145 units; Shrubhill on Leith Walk has 150 MMR units in the pipeline; and the 96 MMR units at Harbour Point have shown the demand and potential of the Western Harbour, enabling the delivery of a further 138 units to create a 234 unit BTR portfolio for Forth Ports.

The logic of these locations can be understood when viewing the tenure pattern of Edinburgh in Fig14. There is a high concentration of PRS in the city centre, as is typical, but there are also PRS arteries to the west in Haymarket, Dalry and Gorgie, to the south at Tollcross and Bruntsfield, and to the north along Leith Walk into Leith and Western Harbour.

These routes have strong transport links, providing accessibility to the city centre and employment, and provide a convenient urban lifestyle appealing to a young urban renter.

Fig14. PRS Tenure Corridors in Edinburgh run west, north east and south in the city
Percentage of Population in PRS

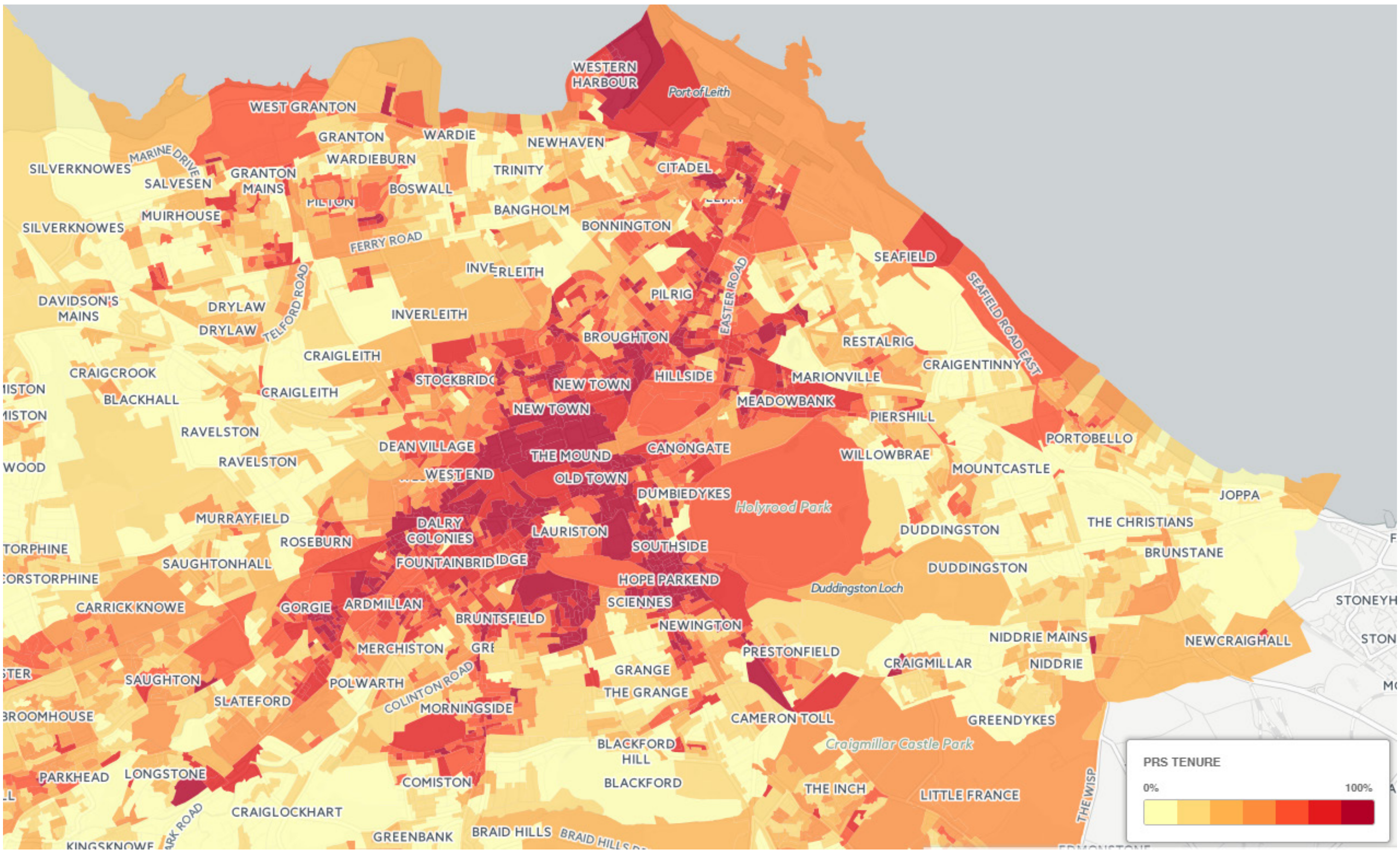


Fig15. Average 2-Bed Rent in Edinburgh by Postcode District

City Profile: GLASGOW

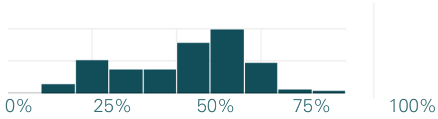
Glasgow is set to lead the BTR sector forward in Scotland, with at least three major schemes set to deliver around 1,400 units, much of which will be targeted at addressing prime market demand within the city.

These schemes will deliver high quality mixed use schemes in Glasgow's City Centre and the Merchant City.

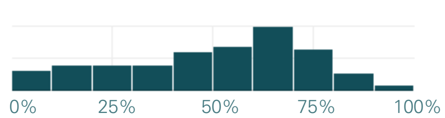
In Glasgow, prime residential demand is typically in the West End as well as suburbs such as Bearsden, Milngavie, Newton Mearns and Uddingston. The City Centre itself has been seen as comparatively undesirable as a residential destination, but this is changing as prices and availability have pressurised traditionally desirable areas. Both Council policy and the crop of new BTR developments are set to pull residents back to the City Centre with aspirational, lifestyle and service driven offerings.

The drivers of BTR are strong within the City Centre of Glasgow. Fig16. below shows the concentration of under 30 year-olds in the City Centre. Combine this with a high level of degree level education, which is double the city average, and PRS tenure averaging 50% of all households, and Glasgow City Centre offers a clear opportunity to deliver a BTR product to the key target market.

Degree Level Education
City Centre Average: 47%
City Average: 18%

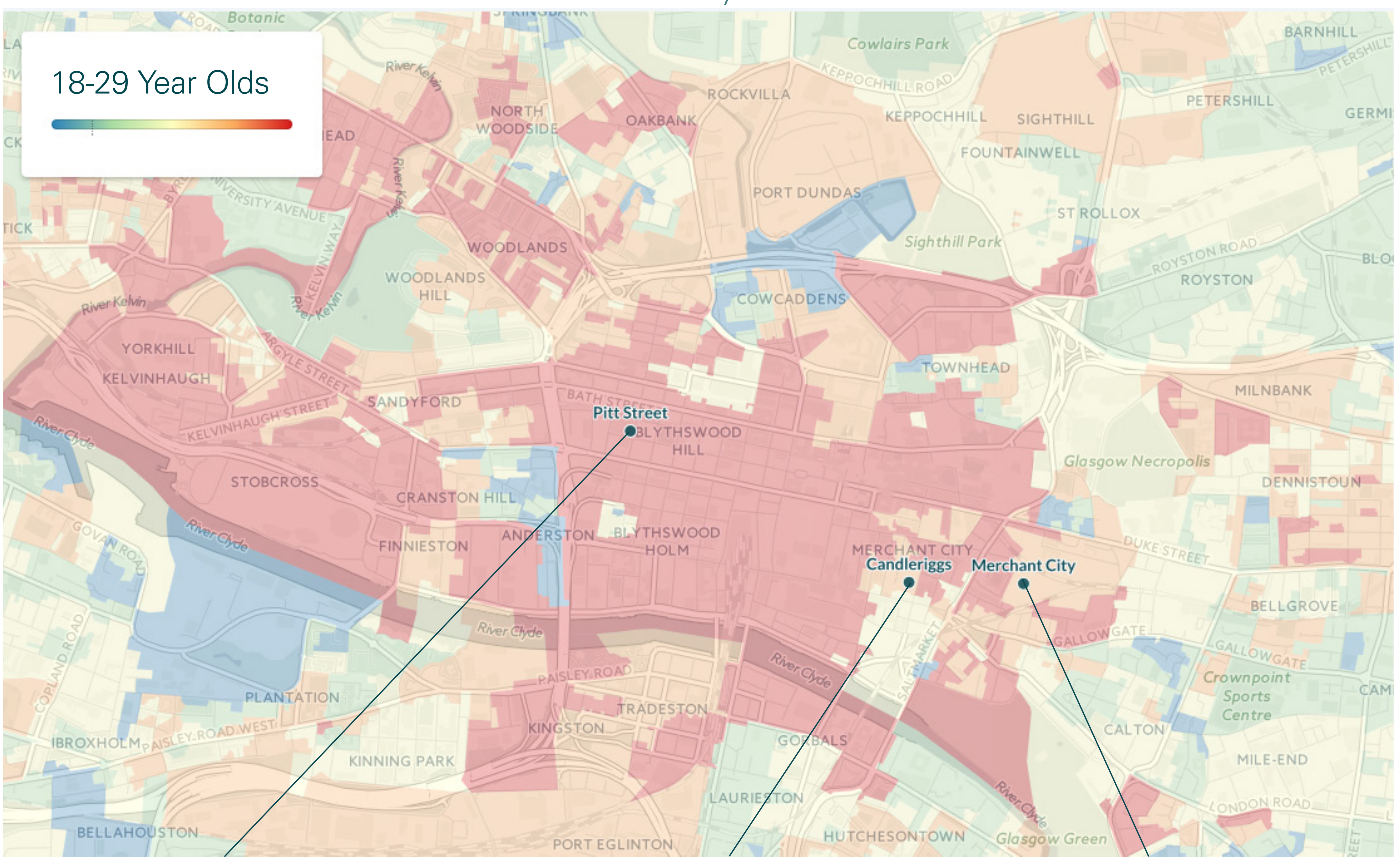


PRS Tenure
City Centre Average: 50%
City Average: 18%



1,395
Planned BTR Units

Fig16. Younger Age Profile is a strong driver of PRS demand
Location of BTR Schemes over concentration of 18-29 year-olds



Holland Park
Moda Living/Apache
450 Units
Pre Planning
Mixed Use

Candleriggs
Candleriggs Limited
345 Units
Pre Planning
Mixed Use

Merchant
Get Living
600 Units
Outline Permission
Mixed Use

Scheme Profile: BROADFORD WORKS, ABERDEEN

Aberdeen saw the delivery of the first BTR scheme in Scotland at Forbes Place, with planned delivery of further BTR units at the historic Broadford Works site just to the north of the City Centre.

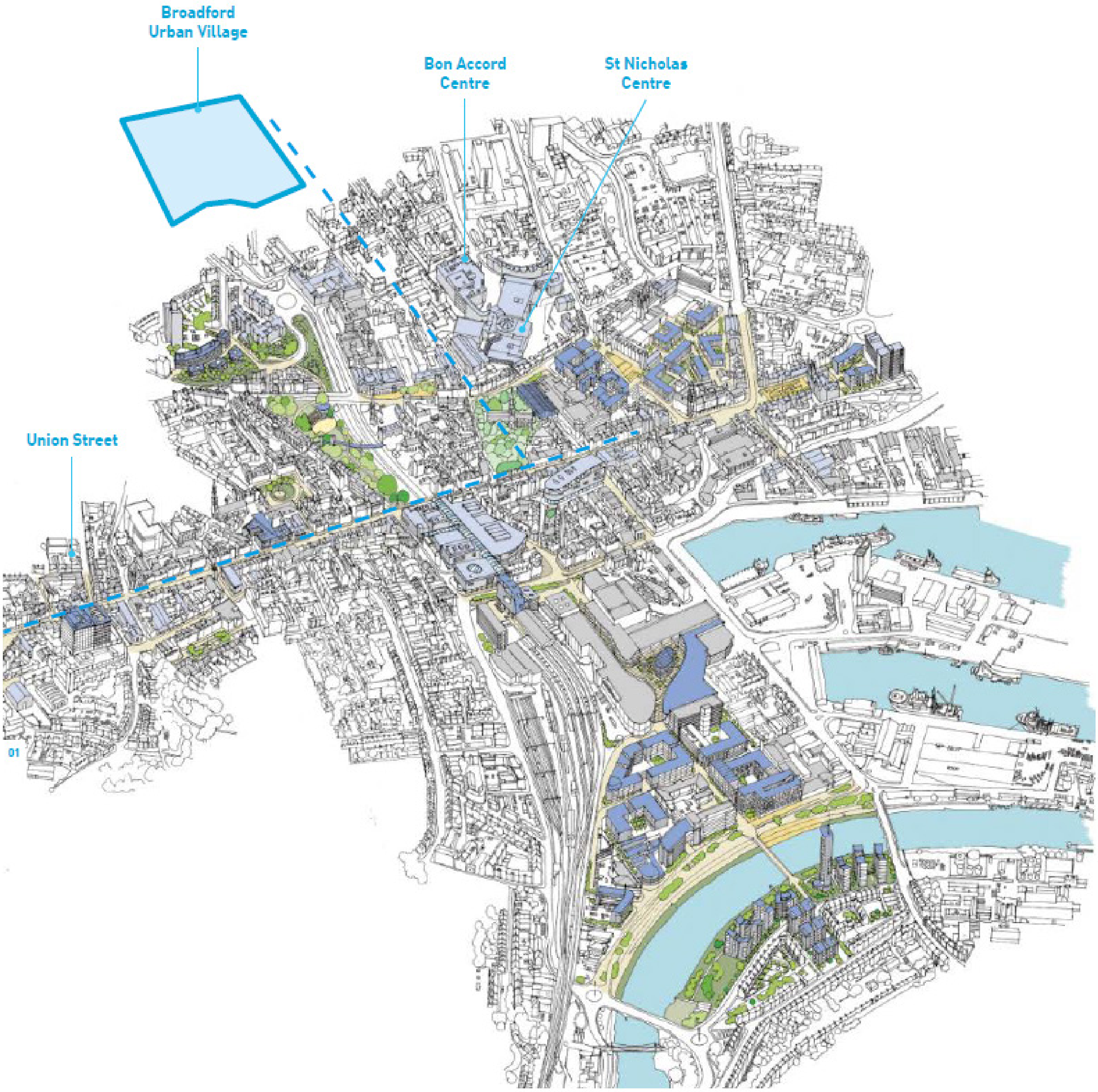
Having been submitted and approved in planning in 2016, Broadford Works is a significant residentially led mixed use scheme that aims to regenerate the largest at-risk collection of listed buildings in Scotland into a new urban village.

The conversion of the site's most historically relevant industrial buildings will be complemented by respectful new-build elements. In addition to apartments, the development will contain student accommodation and amenities such as small-scale shops & cafes, gym facilities and possible workshop / office space that will help support both the new population of Broadford Works and the surrounding community.

460 Residential Apartments

430 Student Beds

Creative Space, Cafes, Bar, Retail, Public Realm



Scheme: VOX, DUNDEE by WHITEBURN PROJECTS LTD

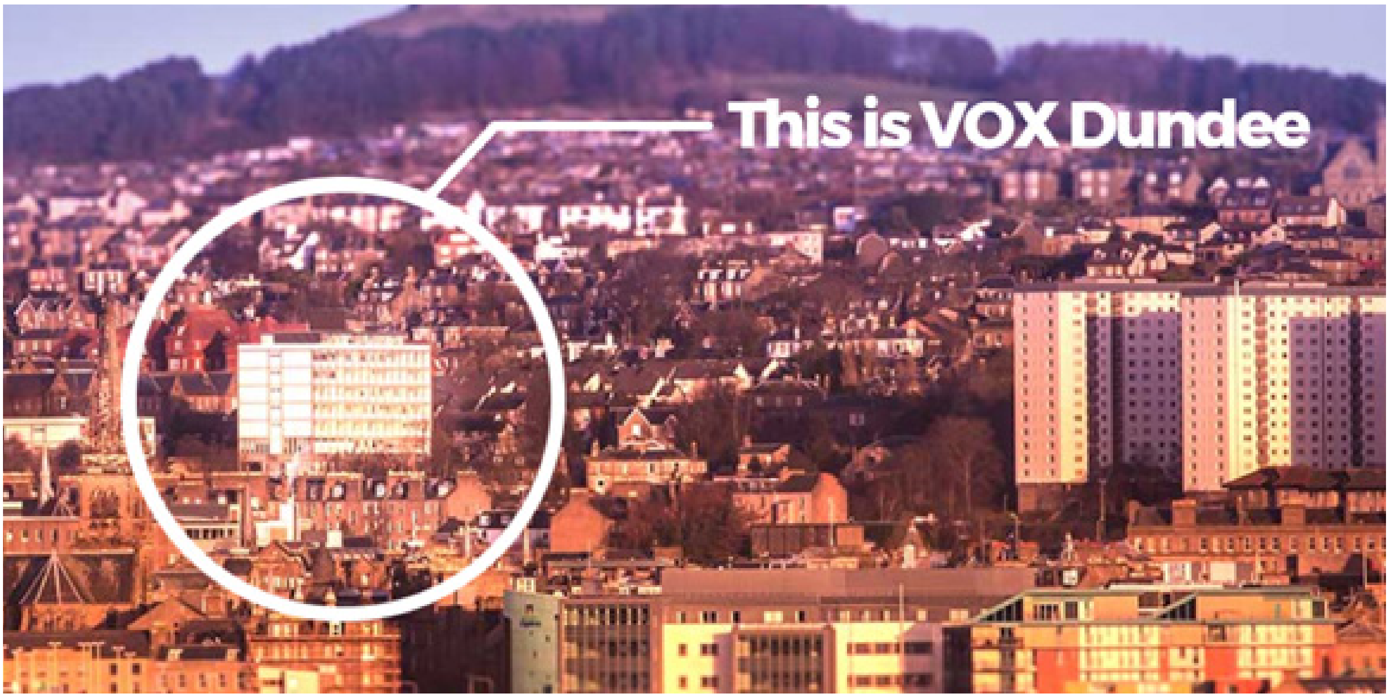
The repurposing of office floorplates into compact and efficient residential units is not a new concept, but with office uptake moving to Grade A provision, some buildings, often centrally located, offer greater potential as residential units. Schemes such as the conversion of the 1970's concrete office block Croythron House into 23 Ravelston Terrace in Edinburgh, as a residential for sale product in 2009, was an example of premium values being achieved in a former office block.

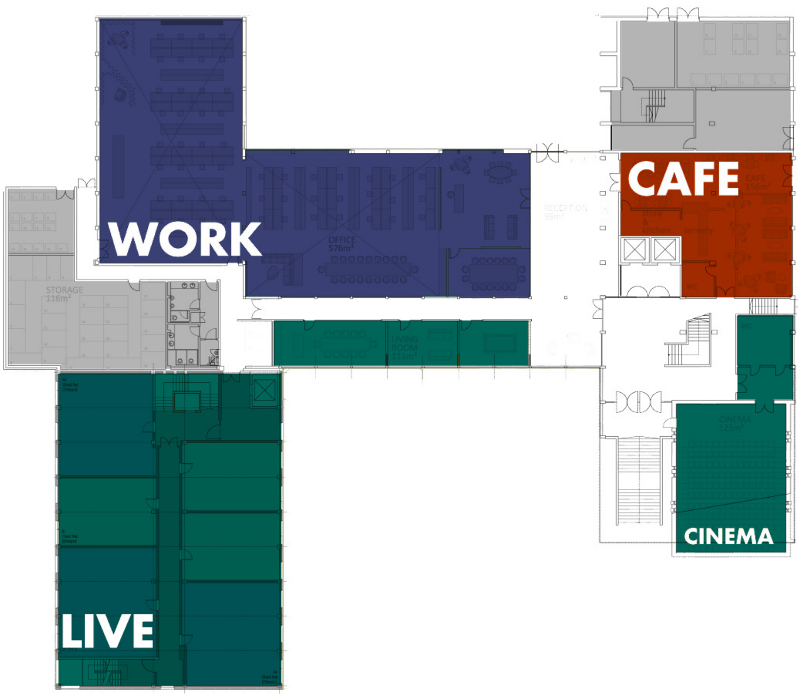
With BTR, however, the ability to purchase and convert a building under single ownership, to then retain and rent the asset, has a clear investment attraction and has been done extensively across English cities. VOX Dundee, being developed by Whiteburn, is an example of this principle being applied in Scotland. VOX Dundee is a scheme converting the 1970's former Commercial College into a mixed use scheme that will create 110 new one and two bedroom apartments alongside an office hub, café, cinema/lecture space and gym.

110 BTR
APARTMENTS

MIXED
USE DEVELOPMENT

cafe, office, gym,
cinema / lecture space





Case Study: BTR Specific Product at Forbes Place

Forbes Place is one of Scotland's first BTR schemes comprising 428 rental units

Despite the buzz in the sector, there has been very limited delivery of BTR units in Scotland. The first has been Dandara and La Salle at Forbes Place in Aberdeen. The 292 studio, one and two bed apartments located in Dyce has led the way in providing purpose-built rental product. Facilities include hi-speed broadband, secure video entry, secure bike storage, on-site management, parcel receipt and grocery storage.

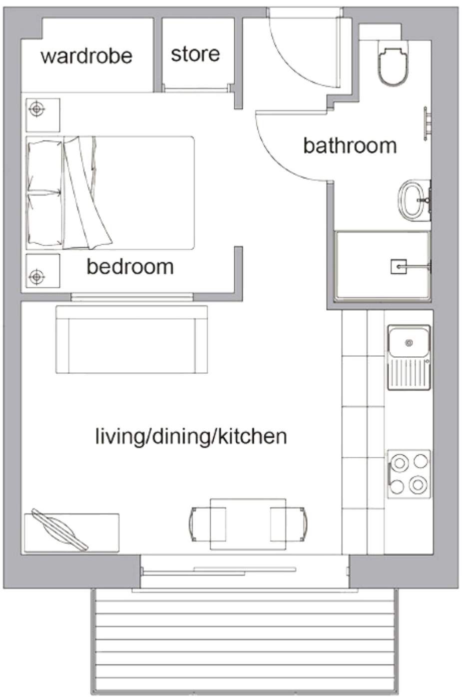
BTR is bringing a new product profile to the market that is not typical of the sales market, and Forbes Place has brought a smaller product to the market in Aberdeen, which has found traction with clients.

Product Profile

The studio product at Forbes Place is a 300sqft single aspect unit, which achieves rents of c.£775pcm. This unit type returns £31/sqft.

Design features such as minimising hall space, open plan layouts and subtle room division create a compact and liveable space, which has proven popular.

To date, demand for the studio and 1-bed units have been strongest at the development.

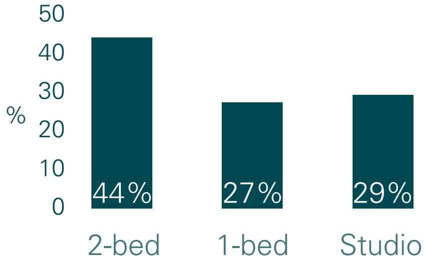


STUDIOS
300SQFT
£775PCM
£31/SQFT

ONE BED
500SQFT
£850-875PCM
UP TO £21/SQFT

TWO BED
670SQFT
£995-£1,200PCM
UP TO £21/SQFT

Phase 1 Mix



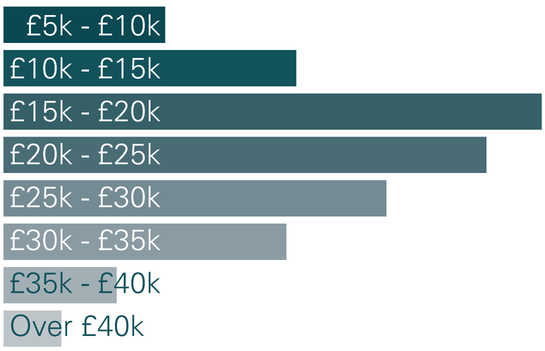
CASE STUDY: MMR as affordable BTR

Left to Right: Nick Watson (Rettie & Co.) handing over 96 completed units to Stuart Paterson (Forth Ports)

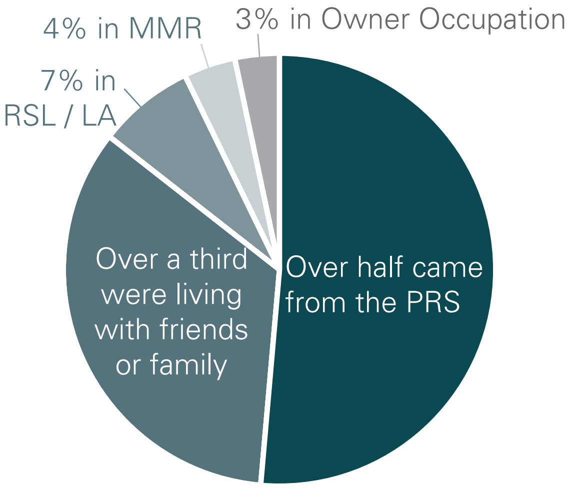
While the BTR sector is currently focused on city centre sites and the opportunity to target premium rents, Rettie & Co. have also been working to deliver Mid Market Rental units, or essentially affordable BTR, with landowners such as Forth Ports. With a household income threshold of £39,000, Harbour Point received over 3,400 tenant applications for the 96 available units. This level of demand came overwhelmingly from single applicants or couples under 35 years-old without children who were currently renting in the PRS. 90% had an aspiration to buy in the future but local ties and affordability were key drivers of their decision-making process. The success of this project led to a further 138 units being approved and commenced in February 2017 on behalf of Forth Ports.

Applicant Profile

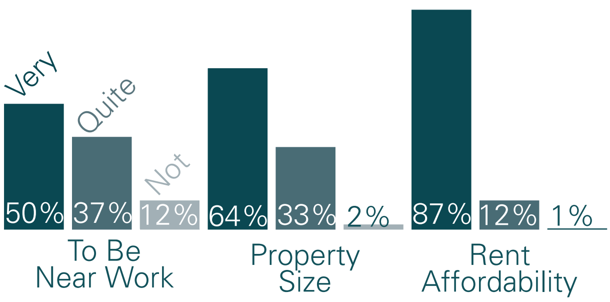
Household Income



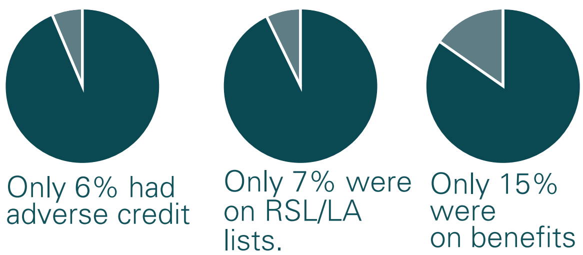
Tenure of Applicant



Drivers of Application



Applicant Characteristics



Distinctive Features of Build to Rent in Scotland

There are a number of distinctive Scottish Market features that parties need to consider prior to investing or developing in Scotland including Government support for the emerging sector.

MMR Support

The Scottish Government is proactively supporting MMR through progressive funding structures including grant funding, long-term preferential rate loans, guarantees, and equity investments have all been offered.

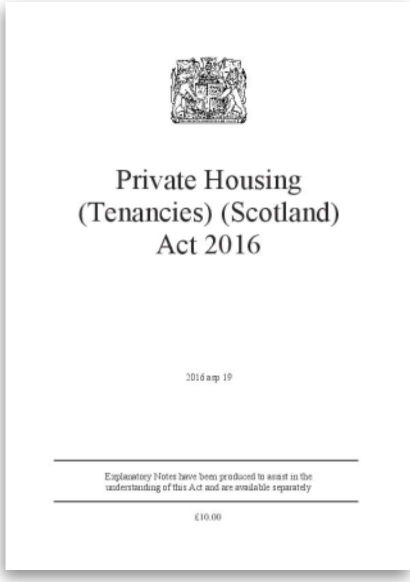
Schemes like the National Housing Trust (NHT) have, to date, delivered around 2,500 units and currently there is lobbying underway for the use of other innovative models to help deliver affordable BTR at scale.

Scottish Tenancy Reform

The Private Housing (Tenancies) (Scotland) Act 2016 introduces a number of changes that will potentially impact the PRS.

Chief among these changes will be the end to fixed term tenancies and the use of fixed grounds for repossession; annual rent reviews; and the ability of local authorities to implement rent controls in Rent Pressure Zones (RPZs).

In the case of RPZs, this would be in the form of CPI+1% + n%, which would be decided upon and set by the Scottish Government after an application by a local authority.


Private Housing (Tenancies) (Scotland) Act 2016

2016 asp 19

Explanatory Notes have been produced to assist in the understanding of this Act and are available separately

£10.00

Taxation

Land and Buildings Transaction Tax (LBTT), Scotland's Stamp Duty Land Tax equivalent, operates in a slightly different way with BTR and multiple dwelling purchases.

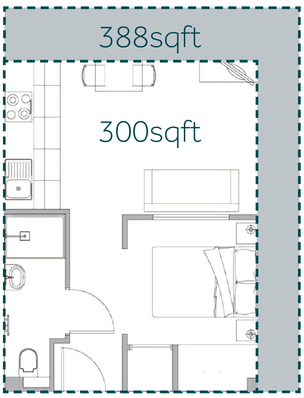
Multiple Dwellings Relief (MDR) is available under LBTT. This is where a taxpayer buying multiple dwellings in a single transaction is not taxed at a higher tax band when the transaction involves dwellings which, if bought separately, would fall into a lower tax band.

In addition under LBTT, Additional Dwelling Supplement (ADS) is not applicable on purchases of 6 or more properties, saving the 3% rate. This differs from England & Wales where ADS applies.

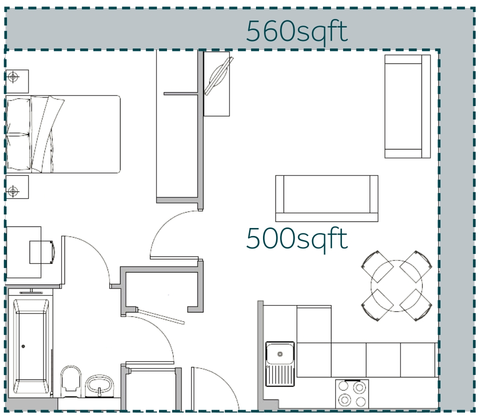
Design & Space Standards

BTR developers typically target highly efficient layouts and these can often come up against design guidelines and space requirements. For example, Edinburgh has minimum internal areas in their design guidelines of 36m2 (388sqft) for studios, which is larger than the BTR studios being delivered at Forbes Place in Aberdeen at 300sqft.

Comparison of BTR Units being delivered at Forbes Place & Edinburgh Space Standards



Studio Layout



One Bed Layout

Rental Income Guarantee Scheme

The Rental Income Guarantee Scheme (RIGS) is part of the Scottish Government's strategy to support Build to Rent. The scheme, which is currently in development by the Government, seeks to provide some security to the risks and uncertainties faced by developers and investors considering BTR in Scotland. In terms of how the scheme has been outlined as potentially working, the guarantee is to compensate for a financial shortfall in qualifying projects resulting from lower than expected rental incomes.

How it might work is as follows. The projected revenue for the scheme is set and independently validated, including an adjustment for voids and bad debt (as a standard 5%). If the revenue during the guarantee period is below a percentage of the projected revenue - the proposed level is 95% (ceiling) with a floor of 75%. Between these set boundaries, the Scottish Government would compensate the owner for 50% of this shortfall.

In scenario one below, the shortfall between 85% and 95% is covered, while, in scenario two, the shortfall between the two limits is compensated to 50%, but below the floor the shortfall falls back to the investor.

Preliminary Criteria

- New Build Scheme not under construction or stalled and switching to BTR.
- Refurbishment involving a change of use from Non-Residential.
- Meets or exceeds building standards and operation quality levels.
- At least 30 residential units.
- Located in Scotland.
- Land is under applicant's control.
- Site has outline planning consent.
- Capable of occupation within 3 years of guarantee being provided by Scottish Government.
- Development plan has clear structure and intent to hold units for duration of guarantee.
- The project has credible financial planning.
- The scheme is demonstrably viable.
- Applicant and prospective owners deemed fit, proper and qualified.
- Beneficiary of guarantee must be in the Private Sector.

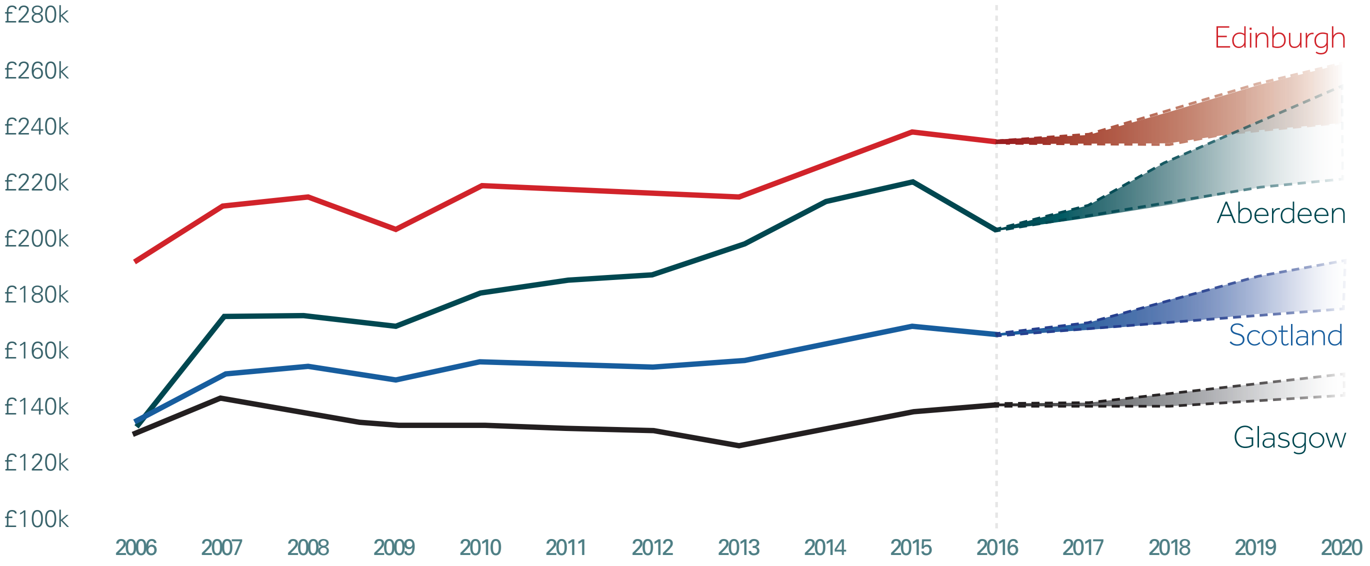
Outline Operation of Scheme

*The actual details, eligability and working of the delivered scheme may vary as it is currently being developed.

Sales Market Forecasts

The Scottish sales market has seen consistent positive growth since 2013 onwards. Aberdeen enjoyed strong counter-cyclical growth fuelled by oil prices before dropping back in 2015. Despite this correction, prices in the city have still seen the greatest growth in Scotland since 2007. Edinburgh has marginally outperformed Glasgow since 2013. Looking forward, we would expect Edinburgh to perform most strongly but all major centres to grow in terms of average prices.

Fig17. Uncertainity in Aberdeen has made its market most volatile
Average Rents and Forecast Rents for Scotland and main cities 2006 - 2020



Source: Citylets / Rettie & Co. Research

Rental Market Forecasts

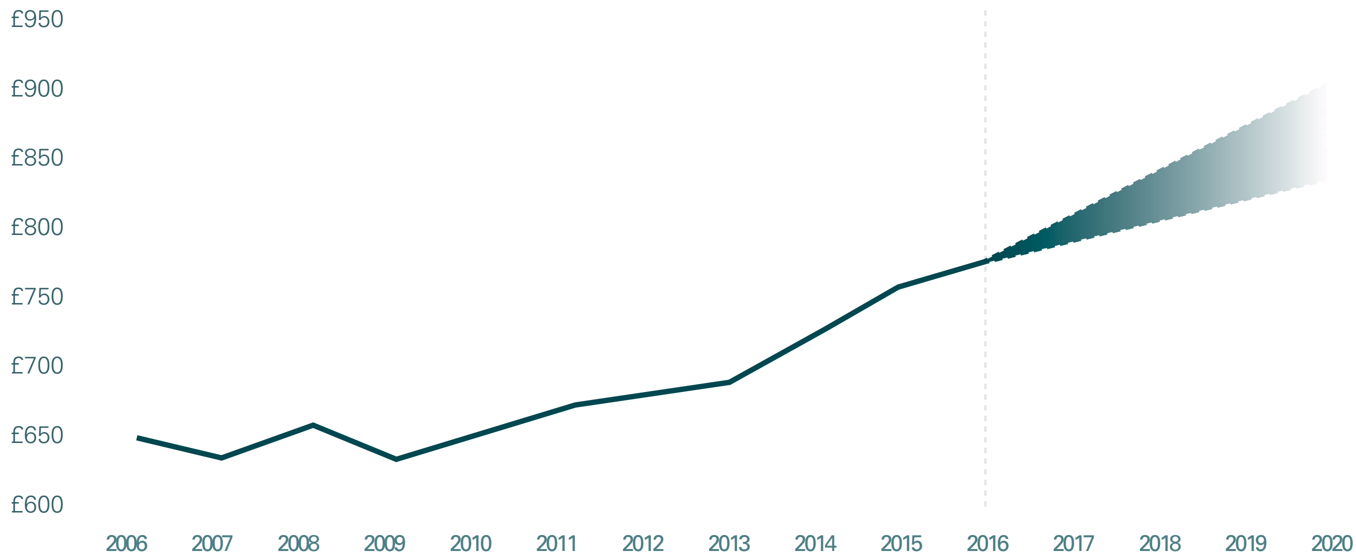
The Scottish rental market has seen strong annual growth since 2013, responding to the combination of low levels of new housebuilding, tighter mortgage lending criteria introduced in 2014 as a result of the Mortgage Market Review, and a moving tenure balance towards the PRS.

Having averaged 1% annual growth between 2007 and 2013, the market jumped to 5.7% growth in 2014 and 4.4% growth in 2015.

In 2016, a cooling in rental values towards the end of the year, returned 2.6% growth.

Looking forward, with the fundamentals of strong demand, constrained supply and limited pipeline of new homes, we expect rental values to grow between 2% and 4% per annum across the country.

Fig18. The Rental market is expected to experience between 2-4% annually
Scottish Average Rents by Year 2006 to 2016 and forecast from 2017 to 2020



Source: Citylets / Rettie & Co. Research

Conclusions

2,500
BTR UNITS in PIPELINE

BTR is now emerging in Scotland as a key new residential use class, with over 2,500 units now in the pipeline in Edinburgh and Glasgow and a successful scheme operating in Aberdeen.

5.5%
RENTAL GROWTH in EDINBURGH

Rising rental market and strong demographic and economic drivers, in the overall context of weak housing supply, creating opportunities for developers and investors. As a proportion of total households, the PRS in Edinburgh is as large as it is in London (around one-quarter of all households).

6.5%
GROSS YIELDS in GLASGOW

Scottish cities compare favourably to other parts of the UK in terms of yields, entry prices and potential for growth. At around 6.5%, average gross rental yields in Glasgow are as high as they are anywhere else in the UK.

40-50%
INCOME TO EARNINGS RATIO

The New Town, City Centre and West End are Edinburgh's rental hotspots, where rent to income ratios are around 40-45%. However, this is challenged by prime Glasgow, where affordability ratios are similar in the likes of the Merchant City, City Centre and West End. Aberdeen and Dundee have more affordable rental markets.

3,400
APPLICANTS FOR 96 UNITS

Affordable BTR schemes, such as MMR, are now established in Scotland, with high levels of demand in appropriate locations, including Western Harbour in Edinburgh, where there were over 3,400 applicants for a 96 unit development.

Development Services

Structured Finance
- 654 Build-to-Rent units delivered over the last 4 years through new rental backed funding initiatives
- Over £98m value of rental assets built on the back of funding streams
- £78.5m value of construction contracts underpinned through agreed re-financing packages

Land & Development
- Advise on land, development sites, residential investment and PRS.
- Advise on every stage of the project, from early appraisal through to site disposals.
- Best results for clients through a proactive approach, creativity and best market intelligence.

New Homes Sales
- Dominant market share in core areas of operation.
- 24 active development projects with £182m of forthcoming product.
- £104m worth of property sold in the last 12 months.
- Initial advice on mix and specification through to bespoke campaigns designed to meet clients individual needs.

Research & Consultancy
- The largest team in the Scottish private sector.
- Analysis backed by Scottish based and Scottish sourced information.
- Research rooted in real time market information.
- Full range of services provided to developers, builders, investors, landowners and the public sector.

Asset Management
- A growing portfolio of 1,500+ managed units.
- In excess of £650m in residential assets under management.
- Regulated by both RICS and ARLA.
- Management experience of both PRS & Mid-Rent assets.
- Skilled in analysis of the tenant demographics that drive asset demand.


Matthew Benson
Development Services
0131 624 9031
matthew.benson@rettie.co.uk


Will Scarlett
Land & Development
0131 624 9041
will.scarlett@rettie.co.uk


Dr John Boyle
Research & Consultancy
0131 624 4073
john.boyle@rettie.co.uk


Nick Watson
New Homes
0131 624 9042
nick.watson@rettie.co.uk


Jamie Macfarlane
Structured Finance
0131 202 0055
jamie.macfarlane@rettie.co.uk


Stuart Montgomery
Lettings & Asset Management
0131 202 9065
stuart.montgomery@rettie.co.uk