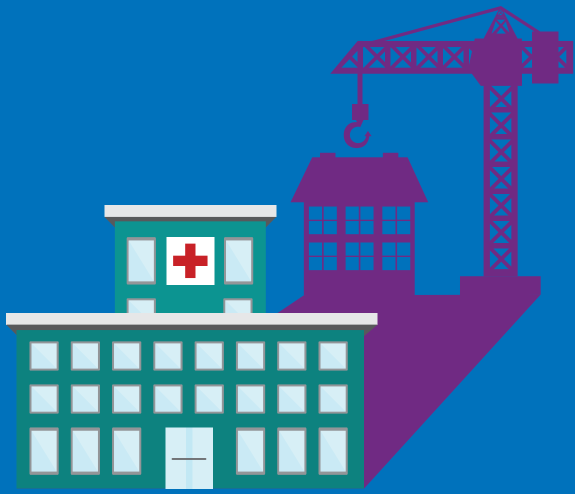
KPMG

Build more houses - reduce rents

Using our best disruptive thinking to achieve public policy goals



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kpmg.com/uk/reimaginepublicpolicy

There are not enough houses being built. Developers say they can build them but they can't sell them.
Can employers help?

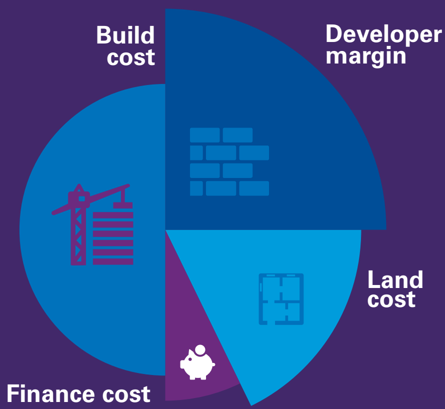
Build more houses. Reduce rents

Mark Essex and Jan Crosby

01 The way it's done now: build for sale

Typically, build costs and land costs are givens. Developers preserve their margin by achieving a sales price high enough to provide their return.

Market absorbtion pricing in the second hand market means that if the developer over-supplies the market, the price falls. That's the main reason supply is constrained.



02 Why not build to rent instead?

Building for rent means developers must swap a cash receipt on sale for a stream of less certain future cash flows. They offset that risk by charging a gross yield higher than their cost of financing, typically six percent. But what if a tenant's employer assumed some of the risk? Could the developer achieve the same risk – adjusted return but charge less rent?

Cost of finance is the risk free return

Tenant credit risk covers for losses when tenants default on rent

Void risk covers loss of rent when property is not occupied

03

If employers took on some of the risks, could that help reduce the yield and lead to lower rent? Let's look at a hypothetical example.

Gross rent is

6%

of property value

Taking off administration, collection costs and maintenance gets to:

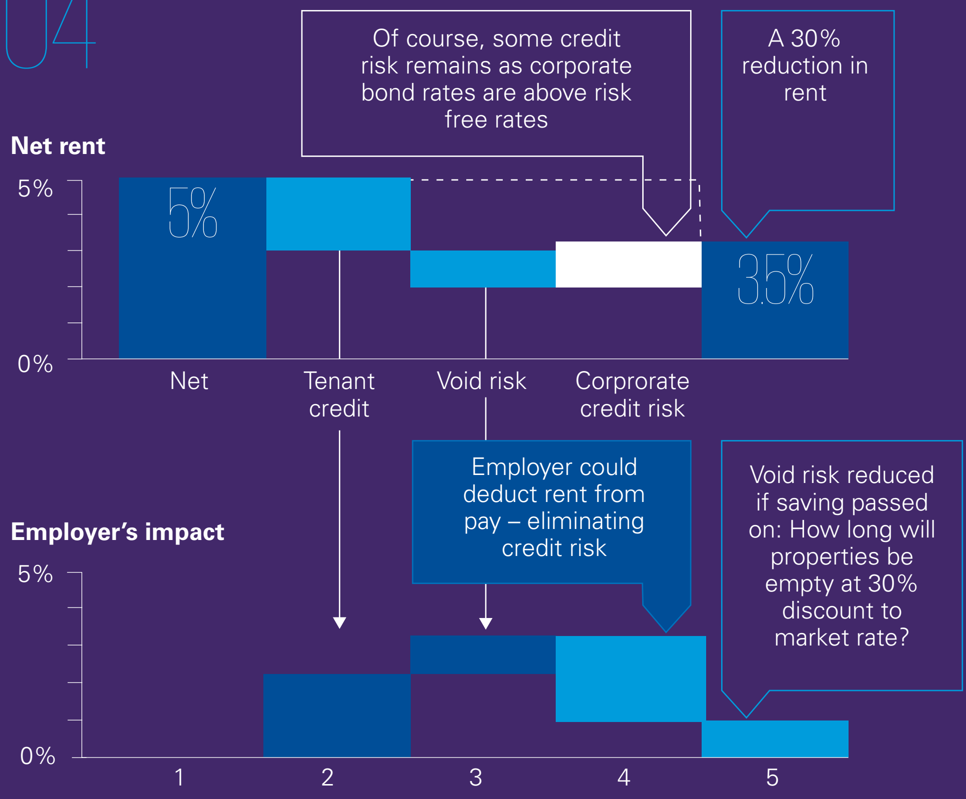
Net rate (the yield) is

5%

of property value

A solution: Employers take a bigger role in meeting staff housing needs

04



05

A game changing impact

20% – 35%

Reduction in market rent payments for participating employees, depending on employer's credit worthiness

06 ...and finally

Goverment is an employer too, with a credit risk equivalent to gilt rates.

Could housing be part of a new deal for public sector workers?

AND, could government-backed build to rent be a new way to stimulate social housing developments

Contacts

We publish these ideas to stimulate debate so please contact us and share your own at ukfmpsmarket@kpmg.co.uk
Alternatively, please feel free to contact the authors directly.

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