

Absorption Rate Report - DRAFT

OPDC Internal Report

28 September 2016

Executive Summary

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Introduction

This report sets out case study market research, our interpretation of the research and recommendations to OPDC in determining indicative absorption rates for both residential and office accommodation at OOC.

Purpose

The recommended absorption rates within this report are to be reviewed and interpreted by OPDC to update their housing trajectory model with market based evidence. This report will also provide OPDC with an understanding of the current absorption rates in key regeneration projects across London. This will assist OPDC in negotiations with private sector land owners about their housing delivery to ensure there is no adverse competition.

Absorption Rate Definition

For Private units, the term 'absorption rate' can be interpreted in numerous ways: sales exchange, sales completion or construction competition. Within this report we refer to absorption rate as sales exchange as this is the point when developers assume the sales on their balance sheet and is the earliest point market demand can be proven.

For the historic data within our case studies we have captured information on sales exchange, however, for forecasted data we have assumed a per annum level of construction completions. This difference is referenced throughout the report.

Affordable Housing absorption rate assumptions

The absorption rate of affordable housing units differ depending on how the units are delivered. Should a Registered Provider (RP) purchase the units from a private developer it is assumed, for the purpose of this report, that all the units are absorbed. However, in reality absorption of affordable housing is dependent on the sub-tenure.

The high demand for Social and Affordable Rented Housing and the associated waiting lists suggests product is instantly absorbed. Intermediate tenures (e.g. Shared Ownership), or emerging products such as Starter Homes, where there is a discount to market value, is more dependent on market demand and traditional sales methods and are likely to have a slower absorption rate than Social and Affordable Rented although recent evidence in inner London suggests that these could also be absorbed almost instantly. Some other types of products/tools such as 'help to buy' have proven to be very successful with waiting lists for products in many London schemes (therefore instant absorption).

Executive Summary – Analysis of Case Studies

Case Studies

Seven case studies have been identified as key comparable regeneration projects to OOC both individually and in combination. The case studies are at different stages of maturity as shown on the summary matrix table below. Detailed matrix table and full breakdown into each case study can be found in Appendix B.

Redevelopment Scheme	Size (ha)	Construction programme	Total units	Actual affordable housing provision*	Total office space (m sq ft)
Nine Elms	227	2007-30	20,000	19.58%	2.6
Kings Cross	64.5	2004-20	1,452	31.49%	3.0
Stratford	c.700	2011-31	21,552	29.92%	1.3
Earls Court	77	2015-30	9,235	15.22%	0.6
Greenwich Peninsula	190	1025-35	12,678	34.57%	1.4
Wembley	171	2004-29	11,500	31.66%	1.1
Docklands	97	1994 – Ongoing	-	-	12.6

**** The affordable housing percentage is the combined average of schemes within the case studies that are either in planning, under construction or have reach practical completion.***

Interpretation of Case Studies

From analysing the case studies over the past 10 years we have been able to ascertain how absorption rates differ depending on the market conditions and delivery of off plan sales to the market.

This analysis excludes developer specific factors and conditions which may affect delivery i.e. its own funding requirements and financial position. The table below provides an overview of the historic and projected (based on future completions) average absorption rates per annum per case study.

Having considered the data from the case studies we have analysed key moments in time reflecting their peak, stable and low market conditions.

Redevelopment Scheme	Total units	Historic absorption rates (average units pa)*	Projected construction completion rate (average units pa)*
Nine Elms	20,000	687	796
Kings Cross	1,452	79	177
Stratford	21,552	615	886
Earls Court	9,235	96	651
Greenwich Peninsula	12,678	222	190
Wembley	11,500	190	180

Executive Summary – Analysis of Case Studies cont. and Methodology

Interpretation of Case Studies cont.

We have then framed our analysis based on the following assumptions:

1) OPDC comprises of several submarkets with different characteristics, which would lead us to believe that simultaneous development can occur.

2) The scale of the opportunity at OOC is similar to that of a borough. The boroughs analysed on page 17 are likely to have more constrained land supply than OOC (with the exception of Greenwich and Newham where there is a considerable quantum of land available for development).

3) The absorption rate of all housing units is impacted by the percentage of affordable housing where higher percentages of affordable housing may impact on the absorption rate of the private homes as shared ownership and similar products compete with private for sale units at entry level to the housing market.

4) Absorption rates will vary at different price points as higher value locations have a more limited demand pool. Similarly we have made an assumption on the number of developers who will operate in each price point at any given time. i.e. the broader the demand pool the higher the number of developers that could be delivering units at any one time.

Methodology

- **We have identified indicative value areas across OOC and have chosen three case studies to correlate to the different value submarkets as follows: Nine Elms – High Value, Greenwich – Medium Value and Wembley – Low Value.**
- **From reviewing the case studies we have been able to ascertain how many developers were active within a submarket and how many units each developer was able to dispose of per annum in different market conditions.**
- **We have considered the land mass within each submarket at OOC and applied our analysis of the case studies in determining our view of the housing trajectory at OOC. We have made adjustments to account for scale, sub-market proximities and market trends at a borough level in order to provide our view.**

Executive Summary – Recommended Absorption Rate per annum

Recommended Residential Absorption Rate for OPDC

From the analysis of data and using experience based judgements, we have provided a view on absorption rates for Peak, Stable and Low market activity. This will help to provide some context for future development environments at OOC given the long term nature of the project and provide some indication of how absorption rates might increase or decrease over time.

There are a number of variables impacting the absorption rate including price, unit mix, tenure mix, market conditions, land availability, momentum of regeneration and wider investment. While it is impossible to forecast every eventuality we have taken a pragmatic approach through understanding the case studies when drawing our conclusions.

We have not attempted to predict market cycles as each cycle varies in magnitude (from peak to trough) and length and therefore recommend that OPDC looks at using the 'stable market condition' as a proxy for average market conditions over the lifetime of the development.

The following table outlines our recommended absorption rate for a stable market condition at OOC to total 700 private units per annum and 466 affordable units (at 40% affordable housing).

STABLE MARKET CONDITIONS	Capital Value Submarket			
	High Value	Medium High – Medium Value	Low Value	Total
Max number of developers	2	3	2	7
Max private units per developer	75	100	125	
Max private units sold annum	150	300	250	700
Max units inc. 40% Affordable	250	500	416	1,166

The type of affordable tenure, particularly if there is a high percentage in the 'ownership spectrum' (including starter homes, shared ownership and shared equity), will have a negative impact on absorption, particularly if they begin to compete with entry level market housing and more analysis will be required when there is more clarity on the tenure types adopted by OPDC.

PRS will have a positive impact on absorption rates. This is principally because it will not directly compete with the private for sale market. We would envisage between 1 and 3 schemes coming forward within each of the value areas across OOC's masterplan.

Executive Summary – Office Absorption Rate

Office Absorption Rate

In determining an appropriate absorption rate for office accommodation we have taken a different approach compared to the residential analysis. This is because of the nature of the product and the fact that the office market take up rate varies considerably from an immature market to established market conditions where place making and anchor pre-lets have been agreed.

Subsequently we have reviewed periphery and core office sector locations across London, alongside a greater detailed review of Docklands, Stratford and Kings Cross and have determined the below take up rates. We have only analysed a stable market condition due to the complexity of reviewing economic cycles alongside office market maturity, and the irregular nature of office developments.

	Maximum office sq ft delivered per annum (million sq ft)
Capital value category	Stable Market Conditions
Current market conditions	0.05
Interim market conditions	0.1
Established market conditions	0.5

Key points for consideration by OPDC

1) The housing trajectory and broader phasing plan should be updated taking into account the findings of this report.

2) Points raised in this report should be considered as part of the Housing Strategy. The mix of affordable housing should also be considered as the balance of tenures will impact viability, absorption rates and housing delivery.

3) PRS should be considered alongside the total provision of housing and the assumption that PRS is instantly absorbed onto the market.

4) Layer office absorption rates alongside the housing trajectory and stagger residential delivery within the commercial plots (or visa versa). This is predominately applicable to the HS2 and Crossrail Depot sites.