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Why Build to Rent has remained resilient despite Covid-19

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Build to Rent has weathered the pandemic resiliently. With rent collection and occupancy remaining high, and economic trends looking supportive, we believe that the sector has many compelling features for the LGPS.

2020 was a dramatic year for all investors and we believe many clients, particularly those with longer time horizons, will be reconsidering their portfolios not only with an eye on returns, but also on volatility. In this article, we look at how the Build to Rent (BTR) sector has fared so far during the pandemic, and what risks and opportunities may lie ahead. We also include a short case study on how one of our recent investments, Box Makers Yard in Bristol, is designed and built for the new demands and future of the the rental market.*

Slate Yard, Salford

Rentals and resilience

National and local lockdowns have had a far-reaching impact on businesses and individuals, with knock-on effects reverberating through the real estate sector. While rental receipts have fallen for much of the market during the pandemic, collection levels and occupancy have remained high for BTR; Knight Frank estimate that 95% of rent in the BTR sector was collected in the second quarter of 2020, compared with average collection levels below 80% in the commercial sector, while LGIM's portfolio registered 97.6% rent collection. This is not to say, however, that BTR has been completely insulated from the effects of the pandemic. Through the first lockdown period, the number of occupied units within our portfolio fell by 8% as residents benefited from the flexibility offered by break clauses. But, testament to its resilience and fundamental housing demand, new lettings activity recovered quickly as lockdown restrictions eased and economic activity increased, and occupancy levels had rebounded to their pre-lockdown levels by the end of August 2020.

Records from recessions

Whilst the full economic fall-out from the pandemic may not yet have filtered through, there are reasons to be reassured of BTR's resilience. Residential rental investment has typically remained robust in periods of uncertainty: during the 2008/09 financial crisis, occupancy levels in the UK residential sector only fell to 96%, 2% lower than long-term average.

As history shows, recessionary periods are typically followed by periods of increased demand for rental homes, as uncertainty and economic conditions deter households from making 'big ticket' purchases like new homes.

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We would expect to see the same occur through this crisis. The US multifamily** sector, which is much more mature than UK BTR, also provides a rough guide to the relative resilience of the sector. Through both the 2001 and 2008/09 recessions, the US multifamily sector saw marginal falls in occupancy rates, shorter periods of rent decline and a quicker return to pre-recession rent levels, than traditional commercial real estate sectors.

Furthermore, banks are increasingly tightening credit conditions for households. Available mortgage products at high LTV (90% and above) have already reduced substantially and mortgage rates have increased, despite the Bank of England's benchmark rate at 0.1%. This is likely to create additional barriers for those looking to move into homeownership and continue to support rental demand.

The relative stability seen so far, however, is not completely cut and dried. The Government's furlough scheme and a demographic tilt in the BTR sector towards young professionals, typically in jobs which have been able to transition to working from home, have helped to protect household incomes and have played a role in limiting the impact. But as the furlough scheme transitions into its latest form, the job retention scheme, and the risks of unemployment potentially increase, there could be future negative impacts.

Case study

Box Makers Yard, Bristol: The future of rental*

In February 2016, the BTR Fund completed the acquisition of a development site in Bristol city centre. **Box Makers Yard** is situated within 300m of Temple Meads Station and benefits from the wider investment into the Temple Quarter Enterprise Zone, one of the largest urban regeneration projects in the UK.
The scheme is creating bespoke, purpose-built, quality rental stock (376 apartments) that will provide a positive lifestyle choice for elective renters. First residents are now being welcomed from January 2021.

Affordability: There are a number of apartments available at 50% of the open market rent and we collaborate with the local council to ensure that the affordable housing is occupied by those most in need.

Sustainability: The average EPC rating of the apartments is B, with each apartment fitted with a smart meter so residents can track their electricity consumption, as well as aerated taps to help save water resource. The kitchens are fitted with A-rated white goods and appliances, which not only reduces electricity consumption but also reduces spending on bills. Residents are provided with a 'Residents Handbook' and offered a tour which includes general advice on how to conserve energy as well as details on recycling, heating, and sustainable travel; there are electric vehicle charging points and there is car club parking space onsite as well.

Community: We have taken care to commission a local artist for a unique piece of public artwork for the scheme, with plans for the management team to organise a programme of community events utilising the Residents Lounge - a space that has been decorated to ensure biodiversity and has been designed for a number of purposes, including working from home stations.

Box Makers Yard, Bristol

* For illustrative purposes only. Reference to a particular security is on a historic basis and does not mean that the security is currently held or will be held within an LGIM portfolio. The above information does not constitute a recommendation to buy or sell any security.

** 'multifamily' is the US equivalent of the BTR sector.

Looking ahead

We believe that the BTR sector is continuing to prove its resilience; whilst we are not yet out of the woods, the existing imbalance between demand and supply should continue to support growth.

We have identified a number of other factors at play which, in our opinion, should support the BTR sector, with assets benefitting from some household behavioural trends and preferences, emerging through the pandemic; examples include the increased likelihood of needing a functional space to work, as we move to working more frequently from home, and the desire to reduce the use of public transport. These trends and preferences are well catered for in BTR schemes, with dedicated co-working amenity spaces and assets located close to local cultural and leisure amenities.

Through the medium to long term, the mismatch between housing demand and supply in the UK should continue to support demand in BTR, and the pandemic is driving secular changes and a fundamental rethink of many areas across the real estate sector. A constant throughout the crisis, however, has been a reinforcement of the need and importance of quality homes. This need continues to be underserved in the UK and will not have been helped by the negative economic impact of the pandemic. With all these push and pull factors at play, we believe BTR will continue to play an important role in meeting that need, and for investors such as the LGPS, with long time horizons and a requirement for diversified returns, we believe that the sector could be a compelling investment opportunity.

Contact us

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