



STATE OF PLAY:

CHALLENGES AND OPPORTUNITIES FACING SME HOME BUILDERS

2021 EDITION



Travis Perkins



Close Brothers
Property Finance





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CLUBMAN

FOREWORD



STEWART BASELEY

EXECUTIVE CHAIRMAN, HOME BUILDERS FEDERATION

Despite the events of the past 18 months, the housing market, with important government support, has overall proved resilient in the face of such economic uncertainty. Although sites had to close completely or had to operate at reduced capacity due to social distancing and isolation measures, housing delivery has been sustained close to the record highs we've seen in recent years.

Despite these positive output indicators, the barriers facing builders, particularly smaller firms who make up the majority of HBF's membership, have not gone away. The pandemic has brought with it new challenges, such as supply chain issues and materials shortages, and exacerbated the existing ones, with local authority budgets stretched even more than before causing further delays to planning applications.

The redefining of the significance of the home throughout the various lockdowns amid all the changes to our working and social patterns means that the sector's role has rarely been more important. While the housing supply increases of the past few years have been impressive, it has been driven primarily by a relatively small group of larger builders. Meanwhile, small builders continue to be blighted by a growing list of barriers.

This report shows the fast-moving environment in which builders operate, with new challenges emerging quickly that have the ability to threaten housing supply but also, for some, their very existence. At the heart of this are the constant difficulties caused by the planning process. A successful, vibrant and sustainable new build housing market requires greater diversity. The growth ambitions of smaller and medium-sized firms will be a key component in achieving this.





FRANK PENNAL

CEO OF CLOSE BROTHERS
PROPERTY FINANCE

Supporting the housing market has been a key pillar in the Government's coronavirus relief strategy and as a result we have avoided a property recession - instead, enjoying a buoyant resurgence in the sales market across the UK. All good things, however, must come to an end and with the return of stamp duty and reforms to the Help to Buy programme, we must now look at how the housebuilding sector can continue to grow and prosper - standing on its own two feet - as we rebuild our economy.

The concept of our 'home' has changed dramatically over the last 18 months, with many of us seeing our homes as a safe haven. But this period has also shone an uncomfortable spotlight on the need to improve much of our existing housing stock; moving away from high density and towards sustainable, spacious homes with outdoor space. SMEs have a vital role to play here as they bring innovation, creativity in design and the agility to pivot; adapting to these new challenges more quickly than their Plc counterparts.

We are delighted that so many of our SME housebuilder borrowers participated in this survey and gave us their time in the focus groups, as they have provided a great deal of insight into how we can help this important part of the housing market thrive once again. It was also pleasing to see that Development Finance remained a low barrier to growth.

As our report shows, SMEs have their own bespoke needs which must be addressed, however, the thorny issue of planning remains top of this list. The recent local and cabinet political changes have demonstrated that reforming the system is not straight forward and politicians are under increasing pressure from their constituents to maintain the status quo.

Our report clearly outlines the procedural changes, which could be implemented without the need for extensive legislation and it is these small but significant changes, which would really seek to even the playing field for SME's and also allow the next generation of housebuilders to come through and flourish.

It is our hope that these insights will help to influence the necessary changes to the housebuilding industry and will help to increase the number of SMEs across the UK, which can only be a good thing for our local communities and national economy.





KIERAN GRIFFIN

MANAGING DIRECTOR, TRAVIS PERKINS

I am delighted to partner with the HBF and Close Brothers on this survey in 2021. We believe SME housebuilders will play a vital role in the future growth of the house building industry.

Travis Perkins' strives to deliver best-in-class products and added value services that are tailored to the needs and requirements of our customers - that is our purpose. We are dedicated to truly understanding our customers, so we can offer the best choice of products and expertise from our knowledgeable teams and key suppliers.

Travis Perkins has worked closely with SME house builders over a number of years (especially throughout the Covid 19 pandemic) to understand what you need from a materials supply partner in order for your business to flourish in the short to longer term. This survey has supported and expanded our knowledge and understanding of how we can work together to resolve some of the challenges you meet every day. We would like to thank you for your participation and look forward to working together.



INTRODUCTION

Last year, the Home Builder's Federation and Close Brothers Property Finance conducted a survey of almost 200 small and medium sized home builders across England and Wales to better understand the impact of the pandemic on the operation of their businesses. Now, a year on, we have conducted another survey, to look deeper at how the events of the two years have changed the landscape for SMEs.

SME builders continue to face obstacles at all stages of the house building process. This is preventing many from reaching their ambitions for growth and threatening the existence of some. The 12 months since has been bookmarked by the yoyo-ing between varying levels of lockdown restrictions and Brexit, which have both exacerbated the existing problems and presented new issues for the construction industry.



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The ongoing challenges associated with the planning process, as well as new materials and labour challenges, have made the market increasingly difficult for SMEs. A summary of the key findings of the survey can be found in this report, along with suggestions to how SME house builders could be best supported.

The construction industry is, and will continue to be, a key driver of our economic recovery as we move back towards normality, and it is critical that SME builders are able to play their part in this recovery as we seek a more diverse sector with a thriving local and regional network of home building firms.



METHODOLOGY

To inform the report, we compiled an online survey for senior representatives of SME companies which was then circulated around the members of HBF and the clients of Travis Perkins and Close Brothers. The survey combined a mix of quantitative and qualitative data and included a section for respondents to leave any additional comments. We received more than 100 responses to the survey with a 100% completion rate. Respondents were geographically spread across England and Scotland. The responses also had a good split in terms of business size and how long they had been trading.

Once the survey was complete, focus groups were set up with smaller groups of respondents to gather more qualitative information about some of the most prominent barriers highlighted in the survey. The focus groups looked at planning and land, labour and apprentices, cost pressures and the impact of the pandemic. A total of 13 senior representatives from SME housebuilders took part in three focus groups and one in-depth interview. The SMEs housebuilders represented were located across England, delivered between 30 and 200 units a year. Some had specialisms, such as net zero and sustainable developments or off-site construction.



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CURRENT CHALLENGES

1. PLANNING

The survey results showed that the planning process was, again, the most significant challenge that SMEs face and that the problems with the process have worsened over the last 12 months. When asked what the major barriers to housing delivery facing SME builders are:

- 94% of respondents see delays in securing planning permission or discharging conditions as a major barrier to housing delivery. This is up from 83% in 2020.
- 90% of respondents believe a lack of resource in local authority planning departments is a major barrier. This is up from 73% in 2020.

In particular, the length of time it takes for some planning applications to reach fruition was repeatedly raised – most respondents could give instances of a development that had taken years for a planning resolution. With local authority budgets stretched even further by the pandemic, calls for change are increasingly passionate.

Many who took part in our survey and subsequent focus groups also said they felt that the planning process disadvantaged smaller firms as compared with larger home builders. This is partly because larger builders have the financial clout to soak up the costs of the long and complex planning processes, but also because councils are indirectly incentivised to make the planning process more straightforward for large housebuilders. The bigger developments typically taken forward by larger developers enable councils to more easily meet local housing supply requirements and involve fewer community discussions around new development.



[For one planning application] We are on the fourth conservation officer...the fifth planning officer and the second head of planning. There is no consistency whatsoever between people.

FOCUS GROUP PARTICIPANT



It is a totally different relationship between the nationals and the SMEs.

FOCUS GROUP PARTICIPANT



2. LAND AVAILABILITY

Land availability has become increasingly problematic for smaller firms. There are a range of local and regional factors causing this, but the issue of availability was consistent across respondents and had increased considerably since our last survey:

- 47% now see this as a major barrier, compared to just 32% in 2020

Factors affecting availability include:

- Areas that are deemed more desirable places to live suffer from land price inflation
- Bigger organisations acquire sites that would usually be taken by SME housebuilders, changing the local market
- Ecological issues, such as nitrate issues, mean sites in some areas cannot be developed because of moratoriums imposed by authorities or, for instance, Natural England.

Participants argued that these issues would be less problematic if the planning system did not restrict the supply of land in a way they felt was unnecessary, such as by placing too many conditions on a site to be given planning approval. This forces SME housebuilders to turn their attention to sites where houses would be much harder to sell or that had many more planning hoops to jump through.



There are sites out there, a lot of them heavily constrained... it is all tied in with planning. The right sites are overlooked and not given permission, the wrong sites are.

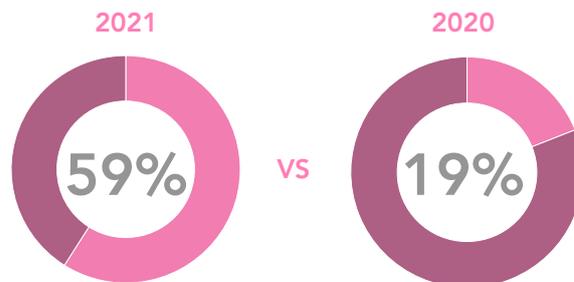
FOCUS GROUP PARTICIPANT



3. LABOUR SUPPLY

The home building industry is a major employer in the UK with an estimated 800,000 directly or indirectly supported by the planning, design and delivery of new homes. With construction activity one of the major drivers behind post-pandemic economic growth, and alongside an increasing demand for housing, it is vital that home builders can continue to attract the necessary talent.

Although the skills shortage has been a source of frustration for builders for many years, the impact of Brexit and Covid-19 has made this more acute during the past 12 months. This has also resulted in considerable wage inflation, something that SMEs are, again, less able to absorb than their larger counterparts.



59% of respondents reported the supply and cost of labour being a major barrier to housing delivery, up from just 19% in 2020.



We are probably 10% short in every trade.

FOCUS GROUP PARTICIPANT



The labour shortage has resulted in a significant growth in the number of apprentices employed by respondents, with just under 60% employing apprentices in their business, as compared to just 33% of respondents last year. A significantly higher number of respondents in the North reported that they hire apprentices (88% as compared to 59% and 52% in the Midlands and South respectively), and this coincided with only 50% of respondents in Northern regions citing the supply of labour as a major barrier, 10% lower than the other regions.

SME builders employ a disproportionately high number of apprentices, which is extremely important for maintaining a pipeline of talent in the construction industry and addressing the long-term skills shortage. However, they also report common problems in recruiting and maintaining apprentices. These include:

- Participants had previously employed apprentices, but found that after years of investing in their training, the apprentices often left to work with competitors soon after the training was completed.
- The industry could be a difficult sell to young people, with factors like location and working conditions acting as a deterrent to a career in housebuilding. It was noted that other sectors – such as the armed forces – presented a much more compelling offer to young people.
- There is not one single source of information, such as one consolidated website, that young people can find out about the roles within the industry and the qualifications required.



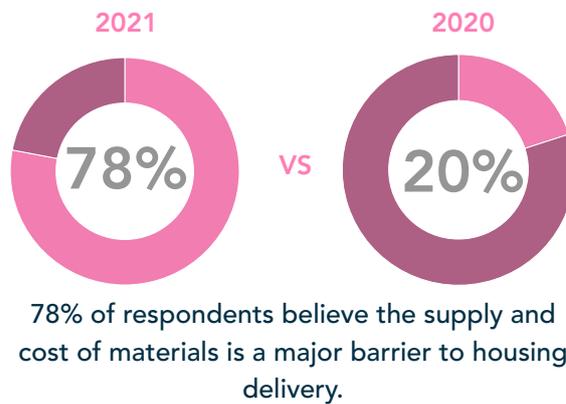
[our apprentices] used us for two years and then gone off to work with family members or something. I am extremely disappointed by it.

FOCUS GROUP PARTICIPANT



4. MATERIAL SHORTAGES AND OTHER COST PRESSURES

As previously mentioned, developers are often hit by hidden and unplanned costs at all stages of the house building process which can easily cripple SME balance sheets and force them to abandon projects. In recent months, global materials shortages and subsequent price inflation have proven to be another significant barrier for SMEs delivering on their growth plans and now features as one of the top three major barriers identified by respondents.



“ In March we were paying £9 a sheet for 9mm Oriented Strand Board, and up until two weeks or three weeks ago we were paying £32 a sheet. Every single product has gone up.

FOCUS GROUP PARTICIPANT





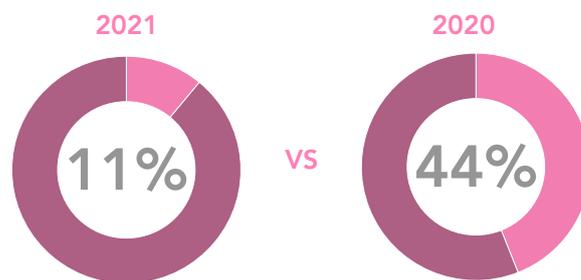
Respondents also believe that this is another area where larger developers benefit, not only because they have the cashflow necessary to cushion the effects of higher prices, but also because they are able to buy materials in bulk and therefore get better deals from suppliers.

Whilst the increase in material prices was the single biggest cost pressure facing SMEs, this came alongside a long list of other factors affecting cashflow management. The cost of labour, the cost of finance, the cost of regulatory compliance and the costs associated with the time it takes for housing transactions to complete were all raised by respondents.

The consequences of materials cost pressures are varied. Some respondents stated that the increases could be absorbed by higher house prices, but most felt that this is not always possible as materials were running out before houses could be completed and they therefore could not be sold. It was also noted that house price inflation was regionally patchy but all regions are experiencing these cost increases. Not only is this reducing the ability of SMEs to compensate for the higher prices through house sales, but the interest on finance to manage cashflow until they are sold poses yet another cost pressure.

IMPACT OF THE PANDEMIC

At the time of the last survey, the economic fallout of coronavirus was far less clear, and developers were very concerned about the impact of the pandemic on housing delivery. Last year, 44% of respondents felt that effects of Covid-19, such as site closures and social distancing, would be a major barrier to delivery. However, with an unprecedented increase in demand for housing and the industry working hard to stay open safely throughout the last two lockdowns, the impact of the pandemic is now considered to have been far less severe than originally feared:



11% cited the effects of Covid-19 as a major barrier to delivery.

Some respondents also highlighted that although the pandemic had caused logistical and financial problems, it had also presented the opportunity for them to identify issues within their business and allowed them to remedy these. These include increased efficiency on sites and a better understanding of the weaknesses of the business. The impact of the pandemic on the behaviour of the country has also provided some benefit to builders, who have seen an increased demand for housing, particularly bigger houses as a result of the move to homeworking and a shift in consumer priorities.

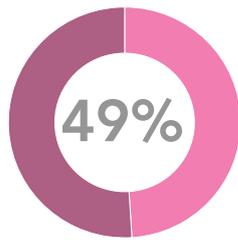


It made us stop and look at our business, and dare I say it, we are better and more efficient now as a result of covid than we were before. Because, like a lot of things, we did what we have always done and never really looked at what is important, what's essential and what could change.

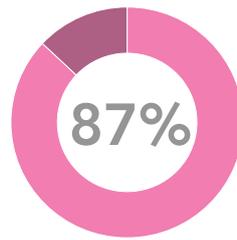
FOCUS GROUP PARTICIPANT



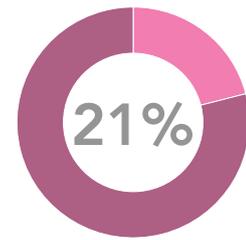
Although the pandemic has not had the negative impact previously thought, this is not to say that SME builders have emerged unscathed. In response to the question **'How was your company's profit affected in 2020?'**:



49% of respondents reported that their yearly profits were down, compared to just 14% reporting that profits were up.



Of the respondents that reported that profits were down, 87% of these reported that they were down by more than 10%.



Just 21% responded that their profits had not been affected.





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DEVELOPMENT FINANCE

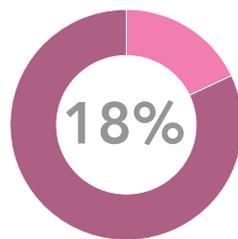
To ensure that SMEs can continue to grow and deliver the housing that the country needs, it is important that they can access the necessary development finance and that lenders and investors are incentivised to operate in this space.

Regional differences were much more prominent over development finance. 18% of respondents in the North and 24% of respondents in the Midlands saw development finance as a major barrier, as compared to just 3% of respondents in the South. Overall, 58% of respondents did not see development finance as a barrier to housing delivery.

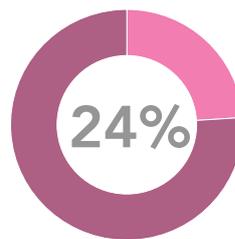
However, in response to the question on how the Government can support SME housebuilders, it was one of the most cited topics in the responses we received. In particular, respondents raised that development finance can be difficult for SMEs to access and that the Loan-to-Cost ratios often leave smaller firms maintaining high levels of equity input for considerable periods of the development process. However, returning to a previous topic, the complexity, risk and cost involved in the planning process mitigates against the availability of good finance on more competitive terms being freely available.

Although it is not identified as a major barrier and may not pose the same difficulties as some of the other issues mentioned in this report, a cumulative 42% of respondents do see it as either a minor or major barrier demonstrating that there is still considerable work to be done.

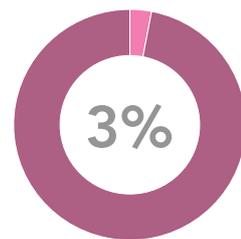
PERCENTAGE OF RESPONDENTS BY REGION CITING DEVELOPMENT FINANCE AS A MAJOR BARRIER



North



Midlands



South



CONSUMER CONFIDENCE

Key to the continuing success of home builders, particularly SMEs, is a robust housing market underpinned by confidence among consumers. Last year, amidst all the financial uncertainty brought on by the pandemic, respondents to the survey were very worried about how consumer confidence may be impacted.

Consumer confidence today is strong, as demonstrated by a buoyant level of the demand for new housing. Subsequently:

- 43% of respondents see consumer confidence as a minor barrier and 50% reported it was not a barrier at all, as compared to 45% of respondents reporting this as a major barrier last year.

Going hand in hand with consumer confidence is the availability of mortgages, a particularly important issue given the closure of Help to Buy which will effectively cease during the middle of 2022. To date the scheme has supported more than a third of a million households to purchase a new build home without requiring a huge deposit or major support from the Bank of Mum and Dad.

Over the past 18 months, there has been some cause for concern about the availability of mortgages, particularly high loan to value (LTV) mortgages often required by first-time buyers. In December 2020, the number of mortgage products available at 95% LTV fell to just eight. It was a reduction in product availability of 98% compared with the pre-pandemic start of 2020 when there were over 400 such mortgages available. In recent months, with the long-term financial outlook more clear, this issue has started to resolve, with 49 95% LTV mortgages available in September 2021. This number is expected to continue to rise, as reflected by the response of the survey participants:

- Only 14% of respondents expect mortgage availability to be a major barrier to housing delivery over the next 12 months.
- 34% of respondents do not expect mortgage availability to be a barrier at all.







CONCLUSION

The results of the survey demonstrated just how quickly things can change and serious challenges can arise for SMEs, as seen by the emergence of material shortages and related cost pressures.

Despite all the differences seen between the results of the two surveys, the issues associated with the planning process have been consistent throughout both. With more respondents highlighting the planning process as a major barrier in this most recent survey, it is of ever increasing importance that these are addressed by the reforms that have long been promised by the Government.

The top three suggestions as to how the Government can help SMEs were:



**REFORM THE PLANNING
PROCESS, SPECIFICALLY
REMOVE RED TAPE AND
BETTER EQUIP PLANNING
DEPARTMENTS**



**ENSURE MORE LAND IS
AVAILABLE FOR SMALLER
BUSINESSES**



**MAKE DEVELOPMENT
FINANCE EASIER TO
ACCESS ON TERMS THAT
ALLOW BUILDERS TO
RECYCLE THEIR EQUITY
MORE QUICKLY**



CONTACT DETAILS

FOR FURTHER INFORMATION PLEASE CONTACT:

- David O’Leary, Policy Director at HBF: david.oleary@hbf.co.uk, 07891 167 072
- Anna Geffert, Hera Communication Strategies, anna.geffert@heracomms.com, 07773 046 337
- Daniel Joyce, Director at Close Brothers Property Finance: Daniel.Joyce@closebrothers.com, 020 385 76284



ABOUT HBF

HBF is the representative body of the home building industry in England and Wales. Our members are responsible for providing around 80% of all new private homes built in England and Wales and most of our members are small or medium-sized enterprises.

Contact

Home Builders Federation Ltd
HBF House, 27 Broadwall, London SE1 9PL
Tel: 020 7960 1600 Email: info@hbf.co.uk Website: www.hbf.co.uk

Follow us on twitter: twitter.com/HomeBuildersFed



ABOUT CLOSE BROTHERS PROPERTY FINANCE

At Close Brothers Property Finance, we are property specialists who provide personalised, flexible finance to property developers and investors across the property industry. Over the last four decades we have consistently supported small and medium sized businesses and we are currently funding over 7,250 homes with a loan book of £1.5 billion. Our bespoke financial products include development finance, bridging loans and commercial investment and our specialist teams are based in three offices across the UK.

We are part of Close Brothers Group plc, which employs over 3,700 people, is listed on the London Stock Exchange and is a member of the FTSE 250. Close Brothers is a leading UK merchant banking group, providing lending, deposit taking, wealth management services and securities trading.

For further information on Close Brothers Property Finance, visit: www.closepropertyfinance.com or for further information Close Brothers Group plc, visit: www.closebrothers.com





Travis Perkins

ABOUT TRAVIS PERKINS

Travis Perkins is part of Travis Perkins plc and the UK's largest supplier of building materials to the building and construction industry. The company has a network of 560 branches and 300 tool-hire outlets and supplies thousands of product lines to trade professionals and self-builders across the nation. Customers will find a wide and varied range of quality timber, building materials, and tools along with plumbing and heating, landscaping, painting and decorating essentials in our branches. For more information, see <https://www.travisperkins.co.uk>



