

unexploded LAND MINE

With house sales stagnant and predictions that the market will stay flat for the next few years, or longer, the effects of housebuilders' land-buying when prices were at their peak will start to hit profits in the next two years. Pressure is mounting for the government to act. Alastair Stewart reports.

HOUSEBUILDERS ARE ANGRY. Their impressive financial results announcements over the past few months contrast starkly with the gloomy statements from contractors. So why the anger? Because two time-bombs – high land values and stagnant house prices – are threatening housebuilders. They are now pressing the government to act. Fast. House Builders Federation director Roger Humber says action will have to be taken before November: "The next budget will be too late. Anything that is changed then will not come into force until next April."

Humber, who is at the forefront of regular talks with government on housing, says he does not know whether ministers will perform a midsummer volte-face and introduce incentives. But, he says, there is pressure for such a move at the highest levels in the Tory party. "If they ignore it and soldier on they will suffer the consequences."

Housing operating profit at Britain's top 10 housebuilders leaped 47% in the latest financial year (see table). This compares with only a 2.9% improvement in contracting profit at the top 10 contractors (26 May, pages 30-32).

Yet builders and economists are warning that stagnating house prices – the subject of an apocalyptic *Panorama* documentary two weeks ago – could scupper any further growth in housebuilders' profit and lead to falls for many companies next year. The BBC broadcast predicted house prices will fall in real terms for the next 20 years.

However long it takes for the market to recover, housebuilders are certain to

suffer – particularly those that bought expensive land in the past two years anticipating a recovery this year. Housebuilders' anger over this financial squeeze has been turned on ministers. Although Tony Pidgley, managing director of Berkeley Homes, does not believe the market will stagnate for 20 years as *Panorama* suggested, he says: "The only thing it showed was how appallingly the government is running the economy."

According to Countryside chairman Alan Cherry: "The government appears to be anti-homeownership."

In the past two years, rising interest rates, the reduction of tax relief on mortgage interest and the threatened

withdrawal of income support for mortgage payments from unemployed homeowners have helped undermine confidence in the housing market. The HBF is pressing for a reversal of the Tories' apparent U-turn on their traditionally fierce commitment to homeownership. Many Conservative MPs predict the next budget will contain measures to boost the housing market.

The damaging effect of government policy on the housing market was demonstrated last month when broker UBS halved its forecast for house price inflation in 1995 to 3%. This is still higher than some other brokers' predictions. UBS housing analyst Rob Thomas says life for housebuilders will be tough for

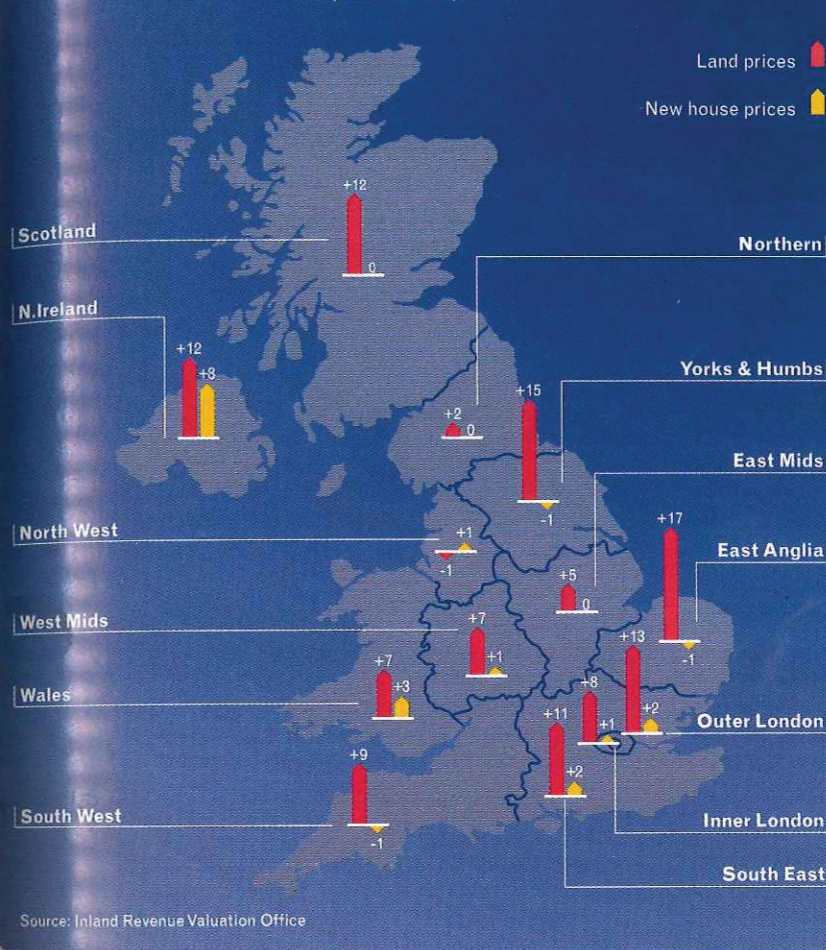
TOP 10 HOUSEBUILDERS, 1994

		Number of units sold		Housing operating profit, £m		
		1993-94	% change on 1992-93	1992-93	1993-94	% change on 1992-93
1	Wimpey	8 078	+16.5	25.4	43.1	+69.7
2	Tarmac ²	6 267	+8.3	55.2	61.1 ¹	+10.7
3	Barratt	5 782	+15.9	27.4	41.5	+51.5
4	Beazer	5 353	+11.4	37.4 ²	32.9	-12.0
5	Wilson (Connolly)	4 200	+9.4	22.5	34.4 ¹	+52.9
6	Raine	3 314	+13.4	12.1	17.3	+43.0
7	Persimmon	3 165	+14.2	19.0	26.7	+40.5
8	Bryant	3 255	+15.6	18.4	33.9	+84.2
9	Bellway	3 010	+30.9	14.6	27.1	+85.6
10	Westbury	2 685	+10.6	7.3	10.4	+42.5
	Total	45 109	+11	239.3	328.4	+46.9

Source: Credit Lyonnais Laing

¹ Pre-tax profit figures ² Nine months only ³ Includes small number of US sales

Percentage change in residential building land and new house prices
1 April 1994–1 April 1995



two years at least, although longer term, he believes prospects are good. Thomas blamed cutting his price forecast on public fears about the effect of changes to income support.

For many builders, there could not be worse news. Sniffing recovery two years ago, many firms had land-buying binges – funded by bank borrowings and more than £2bn from rights issues. The

increased demand made land prices soar – in some parts of the South by up to one-third since their low point in mid-recession.

Some of these firms based their investment decisions on ambitious projections of rising numbers of sales and house prices. This has not happened.

The latest data from the Inland Revenue Valuation Office shows the price of

The map shows that, in many regions of the country, housebuilders' profits will be squeezed over the next two years by rising land prices and stagnant house prices.

homes rose only 0.95% in the 12 months to April 1995. Over the same period, land prices rose considerably in most regions. In East Anglia, the price of land rose 17% and house prices fell 1% (see map, left).

At least now the land price inflation appears to be over. Keith Cushen, managing director of Wimpey Homes UK, Britain's biggest housebuilder, says that in the past two months, land prices have "stopped going up and in some cases are going down".

But this will be too late for some. According to Pidgley, the companies most at risk will be those that let their landbanks run down during the recession, and then bought aggressively in 1993 and 1994 hoping to raise their annual house sales – in many cases by up to 100%. These companies have few reserves of low-priced land as an alternative source. Says Pidgley: "They are not going to double volumes. The companies that sold 1000 homes a year and said they wanted to sell 2000 will have problems."

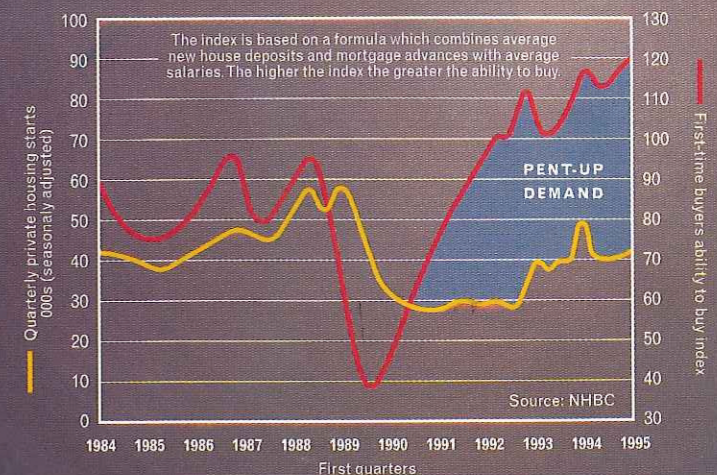
Building analyst Scott Fulton, of broker Smith New Court, believes that for many housebuilders, the time-bomb of expensive land and stagnant sales will hit their financial results for 1996.

"Housebuilders have had a good run. After profits rising 11% more than the rest of the stock market, they have come to the end of their run. In 1995, there will probably be some growth in profit margins. But it is 1996 that is the real concern," says Fulton.

But he says there is one joker in the pack for the housebuilding industry: "The escape route to 'go' without stopping at goal is for the government to introduce help for the housing market."

MIND THE GAP

Ability to buy versus housing starts



HOUSEBUILDING PROSPECTS LOOK

gloomy for the next two years. But the longer recovery is delayed, the more the backlog of potential housebuyers will grow. From 1984 to 1991, housing starts closely followed first-time buyers' ability to afford new homes. Since then, the trend has been broken and housing starts have languished despite homes being at their most affordable since the NHBC started records in 1971. This is shown by the gap between the lines on the graph. Housing experts believe there is a backlog of more than 1 million people who are prepared to buy. As a result, says Rob Thomas of UBS, *Panorama's* projections that house prices will fall in real terms are "flawed and ridiculously pessimistic". After housing emerges from its troubles, prices will rise 5-10% "in fits and starts" until the end of the decade.