UNITED KINGDOM: GROWTH, STRUCTURE AND PRIORITIES OF THE UK REAL ESTATE DEVELOPMENT INDUSTRY: THE LONGSTANDING DIVISION BETWEEN COMMERCIAL AND RESIDENTIAL DEVELOPERS[1]

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Abstract

This chapter explores the growth, structure and priorities of the UK real estate development industry. It highlights the longstanding division between commercial and residential developers, while differentiating between those developers who have a long-term interest in the value of the product they create and those who do not. The chapter shows how the commercial and residential sectors are both dominated by large well-established companies with the capacity to operate across the UK, even if they choose to concentrate their activities in particular regions. It emphasises the volatility and spatial unevenness of real estate development in the UK, revealing the significant financial losses experienced by major companies as a result of the post-2008 financial downturn and the tendency among many players in the industry to concentrate their activities on what are perceived to be low-risk locations, such as London and the south-east. Although real estate development in the UK is primarily a private-sector activity, it takes place within the context of significant State intervention, especially through a comprehensive planning system. This turns planners into a significant constitutive element of real estate markets in the UK – indeed the continuous and dynamic of this interaction means that planners themselves operate as market actors, even if they may not formally acknowledge this characterisation. Nevertheless, the chapter argues that although planning has a significant impact on the overall location and quantity of development produced in the UK, its influence on development quality is less apparent as a result of which many developers still continue to create places that function badly, impede social and economic interaction or have little visual appeal.

1. INTRODUCTION

Real estate development in the UK is a mature and diverse sector of the economy, closely connected to financial services and well embedded within its political and institutional context. The sector is dominated by large and well-established companies with the capacity to operate across the country, even if they choose to concentrate their activities within particular regions and localities. Very few such companies are active in both commercial and residential development, for most see themselves as specialists in one or other of these sectors (Harvard 2008). Residential developers are primarily traders building for the important owner-occupied market (Calcutt 2007). This short-term mentality is reflected by the commercial traders, who move on from one development to the next, without retaining any long-term interest. Developer-investors, however, are also important players in the commercial sector, and focus on producing modern office and

retail stock. Their longer-term mentality tends to be highly selective and risk averse, with evident concentration on developing the very best commercial property in the very best locations (Guy and Henneberry, 2000).

More peripheral locations in the UK tend to experience interest from real estate developers only during times of intense boom. This means that the window of opportunity in which development takes place there is much shorter than in favoured locations. While central, devolved and local governments rarely participate directly in private real estate projects, the contextual influence of the State is highly significant since the supply of land on which new development is to be permitted is closely regulated by the planning system. This makes it difficult to evaluate UK real estate development in isolation from planning policy. Indeed, understanding what might be termed 'state-market' relations in the process of development is crucial to explaining what is actually built in the UK (Adams and Tiesdell, 2013).

These are the themes explored in more detail in this chapter. The chapter first examines the importance of state-market relations in UK real estate development, before looking more closely at the different types of real estate developers operating in the UK. After exploring their spatial and geographical strategies, the chapter explains how the implementation process requires developers to co-ordinate their operations across several different types of market. Throughout the account, we witness a tension between the immediate profitability of real estate development and its often negative impact on place quality. The chapter concludes by asking why real estate development in UK results in so much 'default urbanism' and whether this can be remedied.

2. BROAD PHILOSOPHY AND APPROACH TO REAL ESTATE DEVELOPMENT

In some countries, the State allocates land for development in a plan, acquires the land from the owner and undertakes the development itself. This has never been the case in the UK, except in very special circumstances, such as the development of new towns or the reconstruction of obsolete or war damaged city centres. Although the allocation of land is a public decision taken by planning authorities, the release of land to implement that allocation is normally a private decision left to landowners and developers (Cullingworth and Nadin 2006).

Real estate markets are thus central to the way development occurs in the UK. In reflecting on the power of real estate markets, it is important not to regard them as some abstract force beyond human control, but rather as a channel for human interaction, which reflect society's rules and conventions (De Magalhães 2001). Such markets both express society's financial view of different locations and channel resources to enable the creation and subsequent management of places considered of value. Conversely, they drain resources away from places that are considered unattractive or hard to manage. Their constant, but often elusive, search to create and capture value produces a real sense of market energy, dynamism and turmoil. This makes location, product and timing equally important in real estate development, which contrasts to the common British misconception that value is determined solely by 'location, location and location'.[2] For particular locations may fall out of favour if the products they contain become obsolete, physically, functionally or more often economically. The highly cyclical nature of development production can also mean that developers who miss the top of a boom may have to offer substantial price discounts to avoid lengthy vacancy periods until the market recovers (Maclaren, 2003).

A comprehensive town and country planning system has operated in the UK since 1947 and provides an important context for real estate development. Crucially, each development project (apart from limited exceptions) is required to obtain its own approval from the local planning

authority, which is normally the locally-elected council for this area. This process, which is known as development control or development management, accords considerable administrative flexibility to the planning authority, even though individual proposals are meant to be tested primarily against the authority's published development plan for the area. The discretionary nature of the UK planning system creates considerable uncertainty for real estate developers, especially as it encourages community engagement in the process, and often responds to community concerns on individual planning applications. Although developers can always appeal against planning refusals (normally to central or devolved government) the appeal process can itself be protracted and again uncertain.

We can think of a planning system, such as that operating in the UK, as a form of intervention in the real estate development process through the deployment of four main types of policy instrument (Adams and Tiesdell 2013). 'Shaping' instruments are the first of these, since they seek to shape the decision environment of individual development actors by setting a broad context for market actions and transactions. In the UK, development plans, strategies, visions and other similar documents setting out what local planning authorities would wish to see happen in particular areas provide good examples of shaping instruments.

The second type are 'regulatory' instruments, which constrain the decision environment of individual development actors by regulating or controlling market actions and transactions. The development control system is a prime example of such regulation (although there are others too). It has increasingly been complemented by measures to capture some of the financial returns from development in the form of community benefits. In England and Wales at least, reliance on individual planning agreements or obligations to capture perceived planning gain on a case-by-case basis has begun to give way to a more regularised system of charges (not unlike impact fees imposed in parts of the USA), which is known as the Community Infrastructure Levy.

'Stimulus' instruments, which the third type of intervention in the development process, seek to expand the decision environment of individual development actors by facilitating market actions and transactions. Development grants and subsidies are the most obvious example of market stimulus, although their use has been much curtailed in recent years, as a result of EU rules restricting State aid to the private sector. However, there remain many alternative ways in which local government in the UK can seek to stimulate private sector development, including land assembly and disposal and ensuring improved strategic management of town and city centres.

'Capacity building' instruments are those which seek to support the previous three by enabling development actors to operate more effectively within their own decision environments. These may include seeking to change cultures, mindsets and ideas, building networks, enriching the information and knowledge base, and enhancing skills and capabilities.

State-market relations in real estate development are constituted by the varied way in which these four types of policy instruments are deployed in particular places and at particular times. Some proposed development types encounter significant opposition from the combined power of different policy instruments. This is well illustrated by relatively few regional out-of-town shopping centres above 50,000m² that have been permitted in the UK since the mid 1990s. In contrast, development opportunities bringing new manufacturing jobs to regeneration areas almost consistently receive a strong welcome from their local planning authorities.

What turns politicians and planners in the UK into potentially powerful actors within the real estate development process is their control over the allocation and supply of land, rather than any direct involvement in development, which remains rare. Most textbook accounts of how markets work

mistakenly see planning as quite distinct from the market, and portray planners as external agents, who make specific interventions from off the field of play. This is not what happens in practice, at least in the UK, where the relationship between planning and real estate markets is one of continuous and dynamic interaction. Planners essentially operate as 'market actors' in the sense that they are intricately involved in framing and re-framing real estate markets and so become a significant constitutive element of such markets (Adams and Tiesdell 2010).

3. CHARACTERISTICS AND MECHANISMS INVOLVED IN REAL ESTATE DEVELOPMENT

In the UK, there has been a longstanding distinction between developers who build new homes and those who concentrate on commercial, leisure and business property. Although Havard (2008) argues that the recent trend towards city centre living has helped break down some of the barriers between commercial and residential developers, he still maintains the importance of the distinction. Genuine and experienced mixed-use developers remain relatively rare in the UK making genuine mixed-use development hard to achieve. It is therefore important to understand how the commercial and residential sectors have evolved and now operate.

3.1 The commercial development sector

A specialist commercial development sector, concentrating on the production of new shops and offices to rent, is reflective of the transformation of an economy from a manufacturing to service base. In the UK, the sector grew rapidly from the mid 1950s onwards, often partnering local authorities keen to transform run-down and war-damaged city centres through the development of pristine new shopping centres and office blocks. In a classic text, Marriot (1967) captures the spirit of the wheeler-dealer property tycoon of the 1950s, listing over 100 ordinary individuals, each of whom became property millionaires in a few years. As companies founded in this period matured, they increasingly sought to retain completed developments as landlord, and so create an investment portfolio comprised largely of properties they had themselves built. This highlights an important distinction which still persists within the commercial development sector between companies who are essentially dealers or traders (and who are usually of more recent origin) and those who combine development with investment (and who usually are longer established) (Adams 1994, McNamara 1983).

A trader developer spots the development potential of a site, acquires the rights in land, commissions the design, seeks planning consent, lets the building contract, provides project management and, on completion, sells or lets the development. If the completed development is let to tenants, the trader developer sells out as landlord to an investor. Profits are normally reinvested by trader developers to produce rapid expansion. As a trader developer, Roxhill Developments provides a good example how quickly those with the necessary experience and contacts in UK real estate development can establish new companies and attract substantial business. Roxhill, which concentrates on industrial and warehouse development, was started in 2010 by David Keir, who during 25 years of prior experience in the industry had founded or co-founded three previous development companies which had then been sold on to larger organisations.

In establishing Roxhill, Keir foresaw a shortage of high quality distribution warehouses, especially for large retailers, and knew that only three or four other developers were active in the field. Roxhill's prospective development sites are almost all located close to motorways or major trunk roads, with some having rail freight facilities (see, for example, Figure 1). Roxhill's sites are capable of accommodating individual 'sheds' of between 5,000m² and 100,000m². Almost all of these are at greenfield locations, highlighting the importance of planning and infrastructure expertise, which

the company claims amongst its strengths. It also specialises in fast-track construction and in sustainable design with high energy efficiency ratings. Completed developments will either be sold or let to occupiers, with the latter associated with an investment sale.

Figure 1: Roxhill's proposed London Distribution Park with 93,000m² of strategic warehousing space to be built on 28 hectare site at the Port of Tilbury, London, close to the M25. (Source: Roxhill Developments at http://www.roxhill.co.uk/portfolio/port-of-tilbury/)

In contrast, developer/investors typically hold and manage completed developments, retaining the full equity as a long-term investment. Such companies have grown and diversified over many years, often by taking over smaller firms in the process. They comprise the most influential and well established commercial development companies, many of whom now operate as Real Estate Investment Trusts (REITs). The strength and reliability of investment income, protected even in a recession by long-term leases, shields developer/investors from the full force of a development downturn, to which trader developers are exposed. To benefit from rental and capital growth, developer/investors concentrate on prime property built to the highest quality design and specification, with subsequent occupancy restricted to tenants considered unlikely to default on rent payments.

The approach of developer/investors is well illustrated by Land Securities, which is the UK's largest commercial development and investment company, with a market capitalisation of over £5 billion. Founded by Harold (later Lord) Samuel in 1944, the company grew rapidly in the postwar property boom, focusing on the development of central London offices and provincial shopping centres. This created the base of a strong investment portfolio, which has enabled Land Securities to ride out subsequent booms and slumps with varying degrees of comfort. In 2007, it converted to become a Real Estate Investment Trust, but still remains listed in the FTSE 100 top UK companies.

Figure 2: At 37 storeys high and topped by a public sky garden, Land Securities' 'Walkie-Talkie' development will provide 64,000 m² of prime office development at the heart of the City of London. (Source: Gareth Williams – available under a Creative Commons Licence at: http://www.flickr.com/photos/gareth1953/9614036489/sizes/o/in/photostream/)

Within London, Land Securities owns about 9.5 million square feet of office and retail accommodation valued at around £5.5 billion. Some 13 major development projects have recently been finished in London or are in course of preparation, reflecting the company's financial strength even at economically challenging times along with its capacity to take advantage of lower construction costs and so have new space ready for the next market upturn. These include a £542 million shopping and office complex in the City of London, known as One New Change, and a nearby 37-storey commercial office tower, again costing around £500 million and known colloquially as the 'walkie-talkie' (see Figure 2). Outside London, the company owns 25 shopping centres and 20 retail parks providing around 20.6 million square feet of accommodation and worth around £4.8 billion. Major shopping centres completed in recent years include St David's in Cardiff and Cabot Circus in Bristol.

Developer/investors are matched in their strategies and actions by investor/developers who comprise those institutional investors (mainly insurance companies and pension funds) who from time to time undertake development themselves, rather than simply purchase completed projects from trader developers. Significantly, investor/developers have no sentimental commitment to property. If property performs badly, funds will be gradually switched into alternative investments. To capture their attention, property must offer returns which, taking account of good investment practice, compare favourably with gilts and equities. Insurance companies and pension funds are more likely to fund development in the UK when opportunities to purchase existing properties (known as 'standing investments') become rarer. Although mortgage finance, sale and leaseback and direct development have all featured within past investor approaches to funding development projects, more recent emphasis has been placed on arrangements such as forward sale and forward funding that enable investors to acquire projects from developers on completion. Significantly, investors use their financial power to ensure that any developments intended to be acquired in this way are developed in what are perceived to be prime locations and built to the highest quality design and specification.

3.2 The residential development sector

The growth of speculative residential development can be traced to the early-19th century, when industrial methods of building replaced traditional craft production (Clarke 1992). Speculative house-building for rent, dominant throughout the 19th century, declined sharply in the decade before the First World War. After 1920, social and economic benefits encouraged the rapid expansion of speculative housebuilding for sale. With owner occupation increasing from 26 per cent of households in 1946 to 71 per cent in 2007, the postwar period saw significant further growth in the industry (Wellings 2006). Between 1990/91 and 2007/08, almost 2.95 million new homes across the UK were built by private developers, accounting for 85 per cent of all housing production (DCLG 2013). As a result of the recession, this proportion fell away to 75% by 2011/12, but is likely to increase again once confidence returns. Figure 3 shows the relative importance of local authorities, housing associations and the private sector in UK housebuilding over the last two decades.

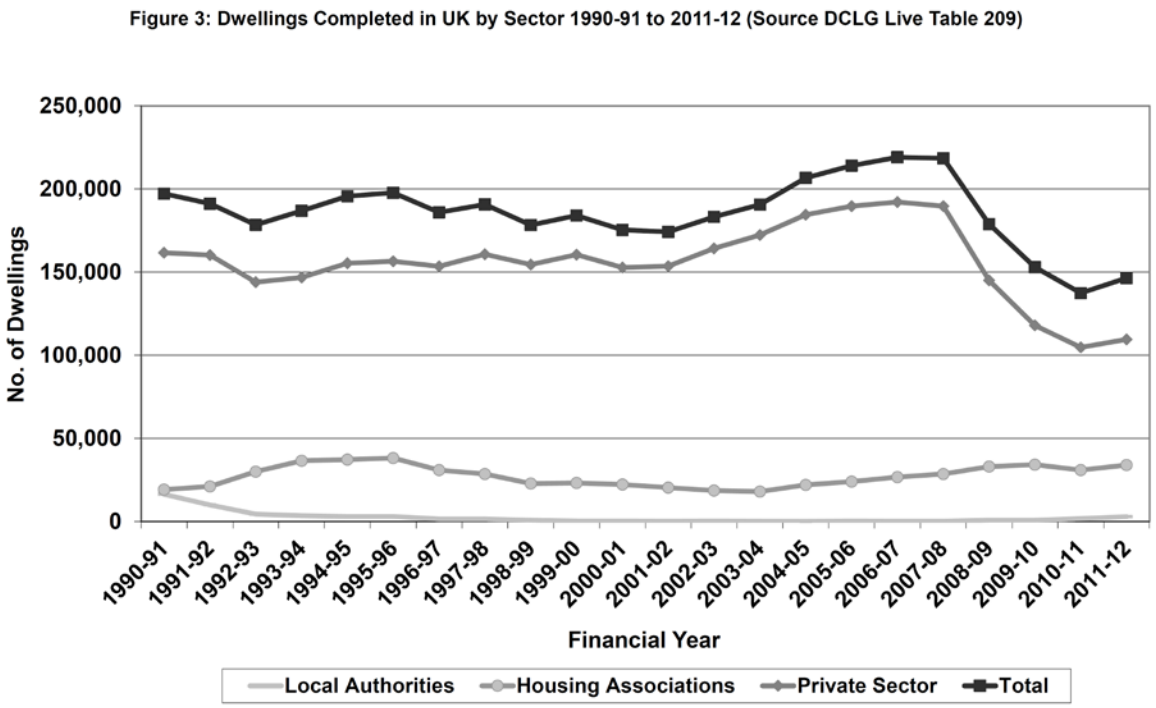

Figure 3: Dwellings Completed in UK by Sector 1990-91 to 2011-12

Significantly, this new residential Britain was disproportionately produced by a small number of very large companies. Although there are about 18,000 housebuilders registered with the National House Building Council (NHBC), speculative production of new homes is dominated by only a few major companies, each with an annual output of 500 units or more. In 2000, for example, 71 per cent of all newly-completed private homes across the UK were built by only 43 'major builders', each with an annual output of 500 or more units (Wellings 2001). The collective market share of the largest 15 of these companies, each producing 2,000 or more units annually and classed as 'volume builders', had by then reached almost 50 per cent. By 2006, the ten largest companies were responsible for 58 per cent of output (Calcutt 2007). Significantly, none of these companies succumbed to the economic downturn from 2008, although several required intensive support from their bankers to survive.

One of the UK's top three housebuilders is Persimmon, which was founded by Duncan Davidson in 1973 in York, where its headquarters are still based. It grew gradually until the mid 1990s, when its unit sales reached about 3,500. Successive acquisition of rival companies, including Ideal Homes in 1996, Beazer in 2001 and Westbury in 2006, took Persimmon's output to a record 16,700 units in 2006, making it then the UK's largest housebuilder. However, as the economic recession deepened and the housing market slumped, Persimmon's completions fell by 46% between 2006 and 2009, reducing its annual revenue from £3.1 billion to £1.4 billion. A pre-tax profit of about £585 million in 2007 turned into a pre-tax loss of £780 million the following year, taking account of exceptional items including a £650 million write-down in the value of land and work in progress.

An agreement with its bankers at the start of 2009 provided new credit facilities of just over £1 billion and enabled Persimmon to restructure and survive the recession. Employment more than halved to 2,400 while the company's debt was gradually reduced to near zero. By 2011, Persimmon was back in action, having spent around £290 million on land purchases the previous year and opening 70 new building sites in the first half of 2011 (see Figure 4). Its growth strategy is now focused on smaller cheaper homes with an average price of just over £160,000. Although around

60% of Persimmon homes are built on brownfield land, it has turned away from flats, which now account for only about 20% of sales. With a current land bank of over 62,000 building plots (25,000 of which have been bought since the downturn) Persimmon is well placed to benefit from any upturn in the housing market.

Persimmon's experience was not unusual in the UK housebuilding industry for according to a report prepared by the industry's representative body: "If 2009 was about survival and setting in train restructuring and 2010 was about restoring stability, then 2011 was certainly the year of consolidating and rebuilding profitability" (HBF 2012). Indeed, many of the leading UK housebuilders experienced some form of financial restructuring in 2009-10 as a prelude to subsequent restored profitability, including Crest Nicholson and Gladedale, which underwent debt-for-equity swaps of £630 million and £500 million respectively in 2009 (Fickling 2009a and 2009b).

Figure 4: Speculative housing development by Persimmon underway at Dumbarton, Scotland in 2011 demonstrating the industry's widespread use of standard house types. (Source: David Adams)

The increasing importance of large housebuilding capital was originally noticed by Ball (1983) who explained the relative growth of larger producers by their ready access to finance capital, often supplied by parent companies. In contrast, small and medium-sized producers were dependent for finance on the banks, which restricted the availability of capital especially during cyclical downturns. According to Ball (1983) such financial constraints prevented small and medium-sized builders from taking advantage of booms and slumps in the same way as larger companies who had the ability to acquire greenfield land cheaply during periods of slump and, as a result, were well-placed to sell houses early in a boom. Golland and Boelhouwer (2002), who compared housing market systems in the Netherlands and UK from 1975 to 1997, also emphasised the importance of land supply in explaining why the industry's structure and organisation differ

significantly between the two countries. Whereas the public sector played the major role in land supply in the Netherlands, the UK speculative housebuilding industry has long depended on securing its own access to land.

Success in the land market is indeed crucial to the commercial prospects of any housebuilder. Yet, of all the raw materials required for housebuilding, land is the most problematic to source. It is used extensively, its quality is heterogeneous and its supply is fraught with uncertainty. It cannot simply be ordered 'off the peg' like bricks or other raw materials. Indeed, its sale may never be publicly advertised, let alone take place through open auction. Its successful acquisition requires both specialist expertise and significant resources. Most housebuilders try to secure their land supplies at least two to three years in advance, often by entering into options or conditionals contracts with vendors, so delaying outright purchase until nearer the commencement of construction. To source land, companies maintain teams of land buyers and rely extensively on networks with landowners, planners and agents and other developers.

There is little point in acquiring land unless planning permission for its development can eventually be secured. Since the early 1980s, housebuilders have adopted increasingly sophisticated strategies to minimise the risk of planning refusals (Adams *et al.* 1992). These focus on seeking to influence the relevant policy framework instead of relying on an uncertain development control system. Substantial investment in planning expertise, either retained in-house or commissioned from planning consultancies (and often with some previous experience of local authority employment) enables a wide range of potential development sites to be identified which might reasonably be expected to be considered by planning authorities for possible release over a period of up to 20 years. Land buyers then set to work to secure options or conditional contracts on as many of these sites as possible.

Networks matter in UK speculative housebuilding since not all residential development land (or even perhaps a substantial proportion of it) is ever openly marketed. In any event, networks provide an opportunity to subvert market competition, since extensive personal contacts increase chances of acquisition. This is why according to one volume housebuilder interviewed for recent research: "the best way to buy current land is through contacts" (Adams *et al.* 2012). Another claimed explicitly that "the success of builders and their activities in the land market are determined by how strong their network is and how well they play that network." Reliance on networks may not produce land any cheaper than perceived market values, but it reduces risk by protecting housebuilders from what they consider outrageously high bidding behaviour from competitors whose particular circumstances necessitate or favour bullish strategies.

3.3 Development finance[3]

To a remarkable extent, places reflect the way in which their development was originally financed. Since construction is essentially a capital good, its cost is spread over many years, usually well into the future. Only exceptionally are developments financed from the accumulated reserves of their promoter. Instead, some measure of external funding will need to be secured and then mixed to a greater or lesser extent with any funds that the developer is willing and able to provide.

Whatever the exact nature of the particular relations between those who promote and those who fund any development, a transfer of power occurs in the direction of the funder. This is well illustrated by Calcutt's (2007) account of how the top management of British housebuilders report regularly to City analysts representing their main shareholders (primarily institutional investors). Calcutt recounts how presentations at these meetings by senior managers of housebuilding companies focus strongly on trading figures, past performance and future prospects, profits and

margins, earnings, dividends and especially cashflow. Analysts who fail to be convinced by these meetings may recommend that clients to reduce their shareholdings or push for management changes. The former will lessen the value of the directors' personal shareholdings and may well lead to takeover pressures. Thus, "Paying attention to shareholder value has become something of a treadmill for directors and senior management" (Calcutt 2007: 118).

A fascinating example of this pressure can be gleaned from a transcript of a conference call held in August 2011 between the Chairman, Chief Executive and Finance Director of Persimmon, and nine financial analysts based in London (Persimmon 2011). After the Persimmon management team had presented an upbeat assessment of the company's half year results, it was interrogated intensively by the analysts. Among the issues raised were:

- Why average sales prices had fallen, and whether they would continue to do so
- How much value had been already written down from the company's land bank and whether further write-downs were likely
- How quickly working capital would be turned over
- How much land had recently been acquired and where it was located.

Significantly, not a single question was asked about design or place quality or even about customer satisfaction. Indeed, the Persimmon transcript confirms Calcutt's (2007: 120) gloomy conclusion that "In practice investors place little weight on any corporate achievement that does not ultimately lead to increased shareholder value. Conversely, unless they impact on future value, they are not concerned by failures in design quality or social responsibility." As this suggests, the shareholder treadmill generates intense pressure on housebuilders and indeed commercial developer-dealers to maximise short-term development returns. This should not of course be confused with long-term investment value.

4. GEOGRAPHIES AND SPATIAL PATTERNS IN REAL ESTATE DEVELOPMENT

There is a clear distinction in the geography of UK real estate development between the residential and commercial sectors. Most volume housebuilders operate across the UK, opening up and closing down regional offices in response to local market conditions. Persimmon, for example, operates out of 25 regional offices across England, Wales and Scotland, which were responsible for a total of 380 separate development sites, from which it sold 9,500 new homes in 2010. Traditionally, British housebuilders have reaped substantial profits from greenfield sites with relatively easy physical conditions, mainly because the State long permitted and indeed encouraged extensive development of owner-occupied housing on greenfield land. In the past two decades, successive UK Governments' desire to switch the balance of residential development increasingly to brownfield sites has represented a significant challenge to behaviour and attitudes that have become well established in much of speculative housebuilding sector. Although matched, for instance, by stricter design and energy efficiency requirements, the 60% national brownfield housing target in England, introduced by the last Labour Government (but subsequently abandoned by the Coalition Government, which succeeded it in 2010), illustrates the ever tighter regulatory environment that speculative housebuilders have faced as a result of the sustainable development agenda.

In 1998, almost 83,000 new homes in England, representing 58% of the total built, were delivered on brownfield land or through the conversion of existing dwellings. By 2008, after a decade of concerted government action, including a strong policy emphasis on building at higher densities, this had risen to almost 135,000 or new homes or 77% of the total (Adams *et al*, 2010). Yet, the over-development of high-density blocks of small one or two-bedroom apartments in many

English city centres in the first decade of the 21st century led to accusations that such 'town cramming' would prove counter-productive in the context of ever-increasing consumer preferences for more space (Evans and Unsworth 2012). Apartment development has been much criticised as a result of its poor design and architecture, restricted social mix, limited energy efficiency and inadequate management and amenities (Punter 2009). Its growth was fuelled by the rapid expansion of development finance, which enabled residential developers to outbid commercial developers for any site that became available.

Leyshon and French (2009) show how this boom was initially driven by the liberal lending approaches of medium-sized and specialist financial services firms who had struggled to compete with global banks operating in the mainstream financial markets. In due course, however, these larger banks entered the buy-to-let market themselves, fuelling an even greater wave of speculative apartment building. When the buy-to-let bubble eventually burst in 2007, it led to significant collapse in the price of newly-built flats and consequent high vacancy rates. With the onset of the recession, total housing completions in England fell away from 177,000 in 2010 to 107,000 in 2011. By 2012, they had recovered to only 115,600. As housebuilders gradually recovered from the recession, they appeared to have no immediate interest in returning to large-scale apartment building, but instead showed a greater preference for more traditional forms of speculative housebuilding. The liberalisation of planning policies under the Coalition Government, elected in 2010, including the abandonment of density requirements and the national brownfield target, is likely to encourage housebuilders to return to greater emphasis on greenfield development

As a general rule in commercial development, the more established the developer, the greater its aversion to risk, whether in relation to product or location. For example, Guy *et al.* (2002: 1187) found that investors' own familiarity and proximity to 'all things London' appeared just as important as formal analysis in accounting for their disproportionate real estate investment in London and the south-east. Even when London-based capital was prepared to venture further north to the regional capital of Manchester, its interest was largely confined to the well-established central office core, in contrast to independent local developers, whose collective culture encouraged innovative schemes in fringe locations. Guy and Henneberry (2000) argue that investor strategies in the UK privilege London over other regional markets since they perceive that investment in the capital is less risky and more liquid than elsewhere. Moreover, Adair *et al.* (2009) suggest that investors unfamiliar with the UK are even more likely to confine their activities to perceived prime assets and locations.

Nevertheless, the IPD Regeneration Index (IPD 2010), which grew of out of research originally undertaken by Adair *et al.* (2004), demonstrates the potential lucrative returns that can be achieved from urban regeneration, provided investors stick with projects over the long-term (even though comparative performance on an annual basis can edge above or below that across the UK as a whole, reflecting short-term property cycles). This is because, as Adair *et al.* (2006) argue, the regeneration process consists of three distinct phases: remediation/infrastructure provision, development and investment. As regeneration projects move through these stages, risk decreases but so do potential returns as revenue streams become more secure and capital values more predictable. New forms of investment vehicle may be needed to take full advantage of these varying risk/return profiles.

One excellent example of how urban regeneration can be promoted through sustainable property investment is provided by the UK-based Igloo Regeneration Fund, managed by Aviva Investors. This partnership between some ten pension and life funds (mainly in the public and charitable sectors) was established to invest in environmentally sustainable and well-designed developments close to the core of the UK's top 20 cities. Working with local authorities, development agencies

and other community-based partners, Igloo has marshalled the necessary funding to drive forward the development of several major urban regeneration projects such as Bermondsey Square, Southwark and Islington Wharf, Manchester.

Igloo's projects span a range of commercial, business and residential uses, often including a significant element of mixed-use development. Its development of an award-winning business and residential scheme, focused on creative and digital media in the inner city of Leeds was explained by the Chief Executive in the following terms: "If we developed 'contractor design' (as we call it), we would just be creating a poor building in an off-centre location, and we could only let it to an average tenant. Instead we commission and deliver great design to attract dynamic, design-led independent creative business occupiers" (quoted in English Partnerships 2007: 108).

As this suggests, we can postulate a continuum from those developers who are more sensitive to the intrinsic value of place, and who seek development that respects and indeed enhances its location, and those who are less sensitive (Carmona *et al.* 2010). We can think of the first group as 'place entrepreneurs' and the second as 'non-place entrepreneurs', while acknowledging that many developers will occupy some midway point and will look to shift their strategies in either direction in response to shifting structural circumstances. In essence, place-based entrepreneurs are those who actively work with the grain of a city, responding to local factors, seeing added value in design, and taking a broader view of where development potential exists. They are typified by locally, relatively small-scale, independent entrepreneurs. Non-place entrepreneurs tend to ignore, undervalue, or actively work against the grain of a city. They take a more limited view of where development potential exists and are generally risk-averse. They are typified by externally based institutional investors.

Guy *et al.* (2002) make the argument that institutional investors base their strategies on the assumption that past trends will continue, while independent developers are at the forefront of creating a 'post-industrial script' around sustainable urban living. In the designer age, it is therefore tempting to ask whether housebuilders' mass production of new homes will follow other forms of mass industrial production into oblivion and whether more bespoke and sensitive developers, smaller in size and focusing on particular niche markets, will determine how cities develop in coming decades.

5. IMPLEMENTATION AND PARTNERSHIPS IN REAL ESTATE DEVELOPMENT

Real estate development is an intensely social process in which relations between people, often nurtured over many years, matter intensely in determining outcomes. Although the relative importance, and indeed the very presence, of categories of participant may vary significantly from development to development, Figure 5 presents a broad framework of development roles in relation to their specific market involvement.

Successful development depends on co-ordination between the roles that participants play in the development process, such as those of landowner, regulator, occupier, investor or developer. Crucially, this involves cultivating networks of trust (see Adams *et al.* 2012 for evidence of networks operating in the UK housebuilding industry). Figure 5 identifies seven essential markets for real estate development. Five of these are what we might regard as input markets in the sense they create opportunities for development interests to access the necessary inputs of materials, labour, land, finance and political support. The other two markets trade the outputs of the development process, namely completed buildings ready for occupation or investment. In practice, these two

output markets overlap, so with owner-occupied housing, for example, the occupier is also the investment purchaser.

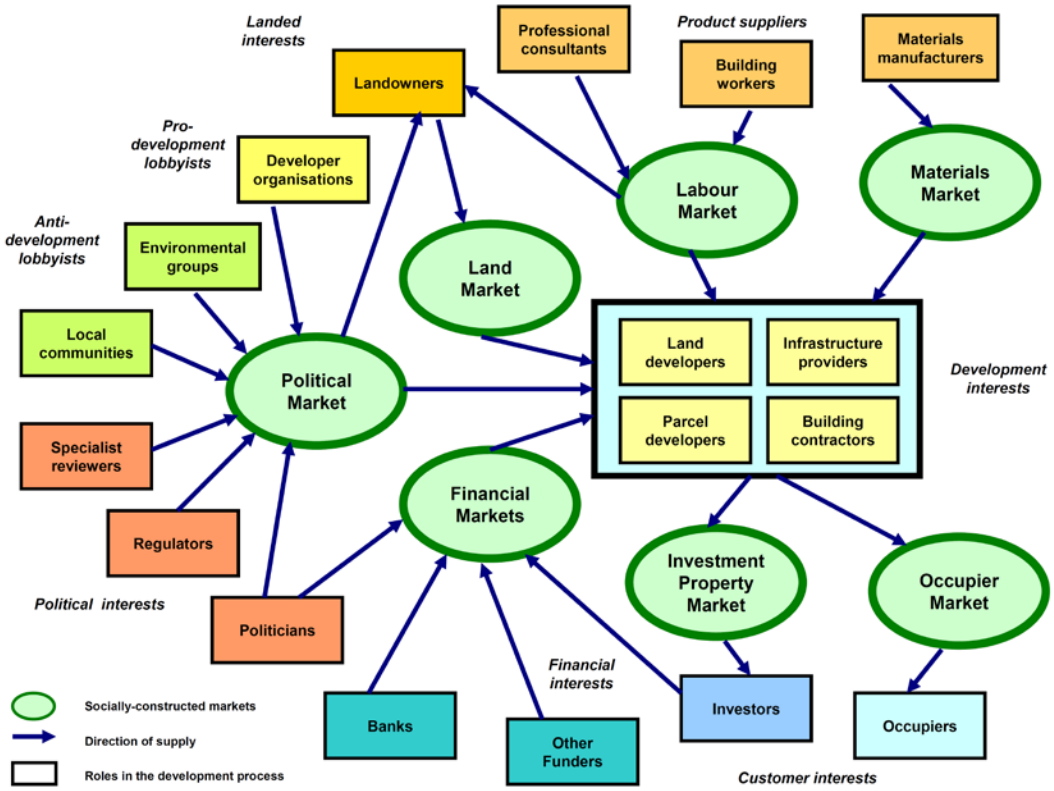

Figure 5: A role-based model of the real estate development process. (Source: Adams and Tiesdell, 2013)

Four types of development interest are identified in Figure 5. The land developer (often called the master developer) operates at a strategic level to masterplan and then to subdivide a development area into smaller parcels, each of which may be assigned to different parcel developers. The infrastructure provider is responsible for provision of roads, sewers and other major investment requirements across the development area as a whole, while the building contractor constructs the actual houses, shops, offices etc. It must be stressed that these four development roles are not necessarily undertaken by four different actors, which is why they are contained within a single box in Figure 5. In the UK, speculative housebuilders, for example, usually integrate all four roles within a single organisation.

To some, it may seem strange to identify a political market in which development interests compete to acquire regulatory consents. However, regulatory consent is a crucial development input, which developers see as highly complex and unpredictable. As the diagram indicates, the complexity of the political market arises from the scale and variety of roles who seek to influence its decisions. Political interests include elected politicians who may delegate the role of regulator to appointed officials. Specialist (and usually independent) reviewers may also have significant influence on decisions supplied by the political market. These may include design review panels, normally established on a permanent basis to offer some external expertise on design quality (Punter 2011) and major national policy reviews, such as the Barker Review of Housing Supply (2004) which resulted in fundamental change in the political market for new housing in the UK.

Importantly, the political market also provides the arena within which those for or against development proposals can engage in debate about regulatory decisions. Here, significant contributions may be made by local communities, environmental groups and representative developer organisations. While development interests are essentially concerned to gain regulatory consent from the political markets, they are normally well aware that individual consents relate to the broader policy framework generated by the political market. In this context, development interests will make full use of the resources gained from the labour, land and financial markets in attempting to influence decisions in the political market.

Developers depend extensively on the financial markets to provide both debt and equity capital for development. A variety of banks, investors and other funders channel finance for development through these markets. Since the State often acts as lender of last resort to financial institutions, politicians are portrayed in the model as an important potential contributor to the financial markets. Ironically, significant State support granted to major UK banks in 2008 was necessary mainly because those banks had overstretched themselves in lending on real estate. The customers of the development industry who occupy and/or invest in newly completed building comprise the final set of interests shown in the model.

Although seemingly static, this role-based model of the development process is energised as resources and political decisions flow, often unevenly and unpredictably, to development interests. As is well known, the real estate development process is boom-prone and crisis-prone, experiencing much more dramatic fluctuations than the economy as a whole (Edwards 1990). Power relations within the development process vary significantly between boom and bust. At boom times, power generally flows in the direction of supply shown in Figure 5. This is because development interests have to pay more for inputs (materials, labour, land, regulatory consents) when they are in short supply, but can expect to receive more from investors and occupiers for outputs in the form of completed developments. With the bust, power generally flows against the direction of supply, since the limited number of occupiers and investors still interested in new development can secure beneficial terms from developers. At the same time, developers, if able to secure a pre-let and commence a new project, can take advantage of the slackness in most input markets to drive hard bargains with suppliers. As an exception to the general rule, financial power tends to flow counter-cyclically, exacerbating development cycles with a flood of finance capital in the boom but a severe shortage in a slump.

As all this implies, development activity is concentrated in 'windows of opportunity' which open with the upturn but effectively close once it becomes evident that too much development is underway. A comparison of development activity and land vacancy in Aberdeen and Dundee (Adams *et al.* 1999) demonstrated how such windows open later but close sooner in regeneration locations than in prosperous ones. Developers are more likely to succeed if they are ready to start on site as soon as the window opens than if they still have extensive preparations to complete. The crucial importance of timing to development success thus makes it essential to use development downturns for preparatory work, especially in regenerations locations.

6. OUTCOMES AND CRITIQUES OF REAL ESTATE DEVELOPMENT

Too often, real estate development in the UK creates places that function badly, impede social and economic interaction or have little visual appeal. Examples include repetitive greenfield housing estates with few facilities, short-life retail warehouses scattered around suburbia, and city centre developments that pay no heed to their surroundings (see Figure 6). The result is what we might call 'default urbanism' – the kind of second-rate places that emerge sporadically and spontaneously,

when no-one has consciously tried to do better. This results from five failures of integration in the real estate development process, namely:

- Between one development site and the next
- Between the public and private realms
- Between use, investment and development value
- Between the additional infrastructure requirements (roads, sewerage systems, schools, hospitals etc) generated by development and their provision
- Between the present and the future.

Figure 6: Default urbanism at Kintore, Aberdeenshire, Scotland – yet another 'anywhere' housing estate developed by speculative housebuilders. (Source: Steve Tiesdell)

Default urbanism can be highly profitable for real estate developers and investors. Indeed, those who produce default urbanism do so because it seems entirely logical to them since managing complexity in development requires a clear focus on what is immediate and achievable. This means paying little or no attention to potential knock-on effects, unless obliged to do so. For real estate development is a highly risky business delivering a bulky capital good to markets that are far from perfect. Developers work hard to manage these risks. They undertake extensive preparations and often do not start on site until they have at least some commitment from end-users to buy or rent the completed space. Most stick to products and markets they know best, hoping to learn from the mistakes of others who innovate first. Above all, they try to remain on time during construction by keeping development as straightforward as possible, consistent with intended end product. The

rationale of the real estate developer is thus understandable, at least in its own terms. It reflects significant economic and financial deterrents to ensuring that individual developments contribute to the quality of the places where they are located and on whose vitality they ultimately depend.

It is the responsibility primarily of governments to create an institutional framework that encourages and rewards integration within real estate development, and deters disintegrated behaviour. For even if individual developers recognise that mounting urban congestion eventually reduces opportunities for profitable development, they may have little interest in whether their own developments contribute further to that congestion, unless required to do so. Similarly, two developers of neighbouring sites may know they could reduce their costs, and perhaps even increase their revenues, by working co-operatively rather than in competition, but without a reliable institutional framework to promote integration, they may well default to the speedy option of developing their sites in isolation.

When governments shape markets successfully, it encourages and enables developers to do more than simply produce profitable developments - they become keen to help create better places. This is not because they have turned unusually altruistic but rather from a hard-headed realisation that institutional frameworks which encourage integrated and co-operative behaviour have the potential significantly to reduce risk for any individual developer. Indeed, in principle, most market actors support rather than oppose government action to shape markets because as one interviewee in Sheffield put it "Developers and investors like to know what the picture is and what is happening in the long term and [whether] a place [has] got its act together" (quoted in Bell 2005: 91). Developers welcome the stability that government intervention can bring to real estate markets, even if they may express concern about particular types of intervention that impact on their individual plans.

Yet, shaping markets is a challenging task for governments and one with potential for failure as well as success. For example, governments are prone to information shortages, political horse-trading and pressure from powerful lobby groups (Webster and Lai 2003). To maximise the prospects of successful market shaping, two essential requirements must be met. The first is a clear articulation of how development outcomes which would otherwise have produced by markets will be improved by the proposed government intervention, taking account of its likely transaction costs. The second is a clear specification of the necessary processes by which such preferred outcomes can best be delivered.

When successful, market shaping can play a crucial role in breeding confidence, reducing risk and transforming developer attitudes and behaviour towards place-making. It has the potential to ensure that individual developments come to be planned as part of a broader picture, rather than in isolation from each other. This means that the overall value of what is created, to both the local community and developers, exceeds what would otherwise have been the sum of its individual components. By helping to manage the complexity of real estate development while reducing its uncertainties, shaping markets has considerable capacity to produce all-round gains.

7. CONCLUSION

In the UK, real estate developers have long played a crucial role in the production of the built environment. Their expertise is seen to lie in spotting development opportunities (location), knowing the target market (product), and resolving constraints to make things happen when required (timing). They are often portrayed as impresarios, orchestrating the development performance by bringing capital, labour and rights in land together to create the right product in the right place at the right time (Marriot 1967, Ross Goobey 1992). Yet, the effectiveness of this

performance is highly dependent on the relations between developers and other important contributors to in the development process, most notably landowners, funders and regulators.

While specific development projects in the UK are initiated primarily by the private sector, developer strategies are influenced by the precise nature of state-market relations at the time, and especially by the requirement of planning policy. Real estate development is not controlled by the State, but its products are clearly influenced by policy intent. In the end, however, the State's strongest card lies in its ability to prevent development it considers undesirable rather than to create development it considers desirable. Moreover, there is a limit on the extent to which that card can be played without unduly impeding the development industry. The constant tussle between the State and the market shifts the perception of that limit backwards and forwards, as political and economic circumstances change.

At most times, however, real estate developers are well aware that the power of the State to influence development products is largely indirect and that default urbanism can continue to be reproduced with only limited hindrance. To achieve otherwise would require a fundamentally different approach to the control and management of development in which quality of place was accorded far greater priority by both real estate developers and the State. In the meantime, despite variable State influence, what is actually built in the UK strongly reflects the strategies of real estate developers, which is why they deserve to be a focus for both academic study and public debate.

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[1] Much of the material in this chapter is drawn from, and indeed expanded within, *Shaping Places: Urban Planning, Design and Development* (Adams and Tiesdell, 2013).

[2] Although the phrase 'location, location, location' is often attributed to Harold (later Lord) Samuel, founder of Land Securities, and is still mistakenly ascribed to him on the Land Securities website, its origin goes back at least to the Chicago Tribune in 1926 which carried a classified real estate advertisement with the words 'Attention salesmen, sales managers: location, location, location, close to Rogers Park' (Saffire 2009).

[3] For a detailed account of development finance, readers should consult texts such as Havard (2008), Isaac *et al.* (2010) and Radcliffe and Stubbs (2009) which explore the various instruments used to finance development in depth.