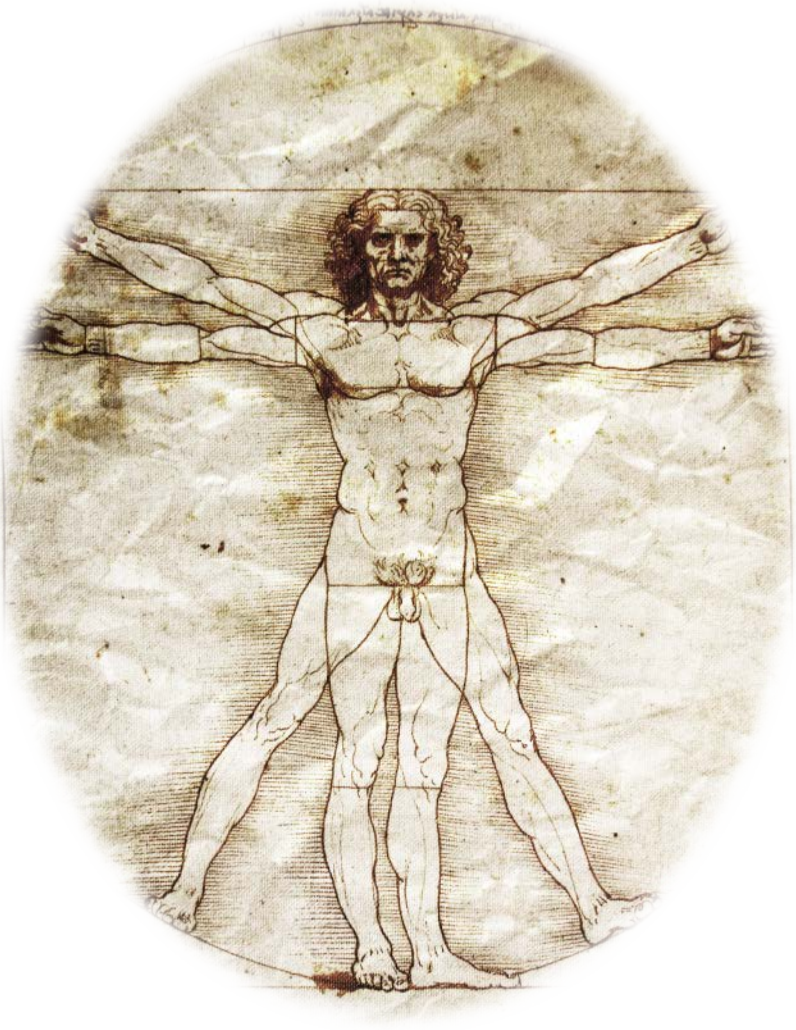
UK Housebuilding Sector in 2017; e il futuro

Winter 2018



Source: iStock

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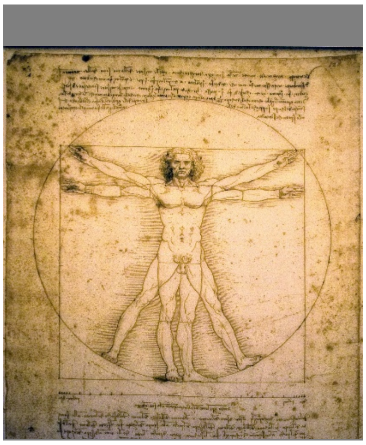
The Vitruvian Man



Source: Shutterstock

Leonardo da Vinci's 'Vitruvian Man' (circa 1490) is often used as a representation of symmetry i.e. the workings of the human body are an analogy for the workings of the Universe.

The drawing, which is in pen and ink on paper, depicts a man in two superimposed positions and it is accompanied by notes based on the work of the architect Vitruvius - who believed that the human figure was the principal source of proportion among the classical orders of architecture.

Like most works on paper, it is displayed to the public only occasionally.

Symmetry, when it is exhibited, is a harmony of parts with each other and the whole – and it can be beautiful. Humans, for example, find bilateral symmetry in faces physically attractive. It indicates health and genetic fitness.

The neo-classical UK Housebuilding Sector (circa 2017) is a picture of bilateral symmetry too.

Last year it increased in value 43% to £43 billion.

It is also healthy and exhibits genetically modified fitness (based on empiricism).

What could go wrong?

Share prices in 2017; and Q4

In the calendar year, the stock market value of the UK Housebuilding Sector rose 43% to close at £43 billion (which compares with a decline of 14% in 2016).

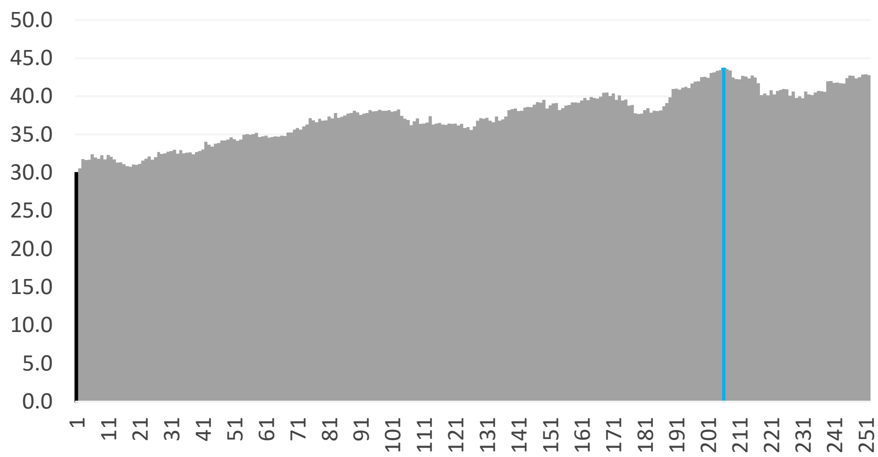
This was also just 2% off its all-time high, which was recorded on 24 October 2017 (£43.6 billion) and 22% above its pre-Brexit level.

The Sector painted new ground a record 34 times in 2017, with 14 of these in Q4.

In total, too, there were 252 trading days and the Sector rose on 60% of them and fell on 40% – and there were no flat canvases.

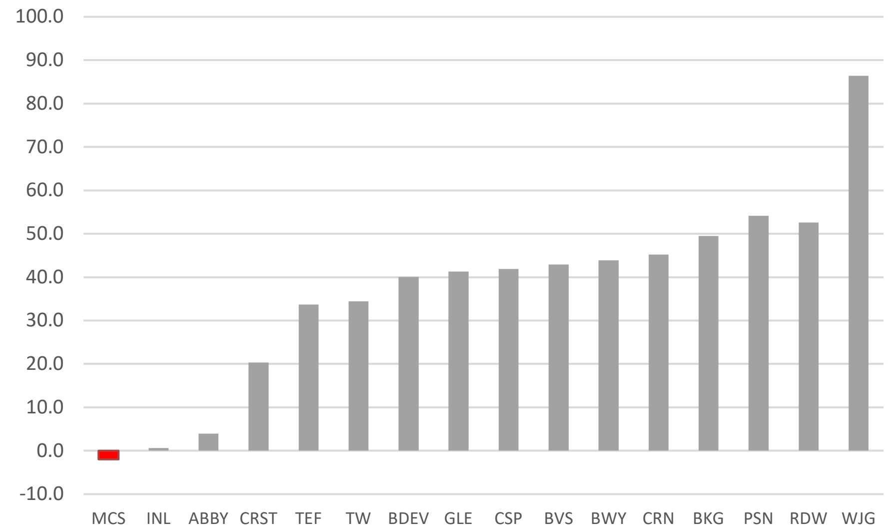
Similarly, in 52 weeks the rise and fall ratio was 67:33 and there were only three colour red months: June (-6%), September (-2%) and November (-5%).

Housebuilding Sector stock market value - daily - in 2017 (£bn*)



Source: Hardman & Co Research
**blue denotes peak on 24 October; black denotes low on 03 January*

Share prices in 2017 (% change)



Source: Hardman & Co Research

All four quarters were brushed positive, especially 1Q (+16%) and 3Q (+11%).

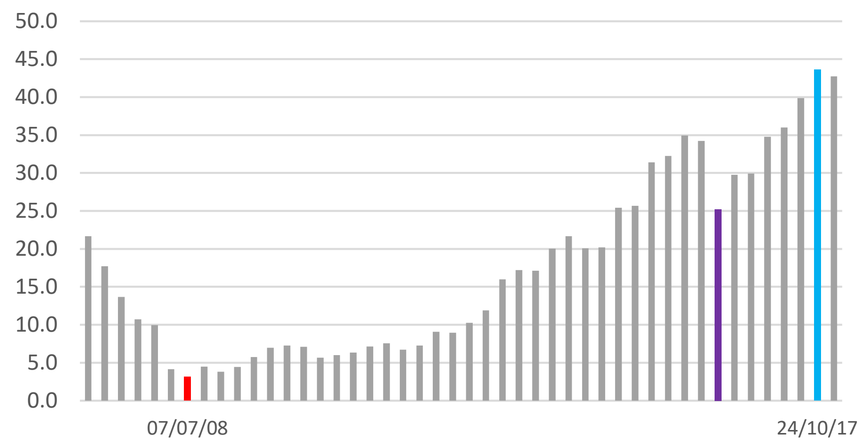
The best week was Week 1 (+5.8%) while the worst was Week 45 (-4.7%).

Best day was 5 January (+4.0%) with the worst on 9 November (-3.7%).

Looking back to the Sector's trough (7 July 2008), the rise has been 1,263% or £39.6 billion; and the Brexit bombard – when Housebuilders lost 40% of their value in two days – is an historical charcoal.

Yet, the Sector still trades on a barely double-digit prospective PER.

UK Housebuilding Sector: market value (£bn): 1Q 2007 to 4Q 2017 *



**Low was on 7 July 2008 and (red) and high was on 24 October 2017 (blue); post-Brexit is in purple*
Source: Hardman & Co Research

Share prices in 2017; and Q4 cont.

Housebuilders' share prices rose by an average of 37% last year actual or 43% weighted by market capitalisation; in 2016, there was a deficit of 13% and 17% respectively.

Watkin Jones, the artistic student flat developer, was the winner up 86%

Next best with a palette were Persimmon (+54%), Redrow (+53%) and Berkeley (+50%) with six other stocks at 40% or better.

McCarthy & Stone was the sole negative engraver (-2%) in a difficult year for the re-drawn corporate; and it closed 2017 at 157.8 pence which compares with a November 2015 IPO price of 180 pence.

It is also the case that the Housebuilders significantly outperformed the UK equity market's principal drawers by three or five times. The same goes for the two prime real Estate Indices, while Construction, overall, was red.

Turning, specifically, to the 4Q easel, housebuilders' share prices added an average 5.9% in 4Q 2017 on an actual basis and 7.1% weighted by capitalisation (in 3Q, these paint-by-numbers were +7.6% and +11.0%, respectively).

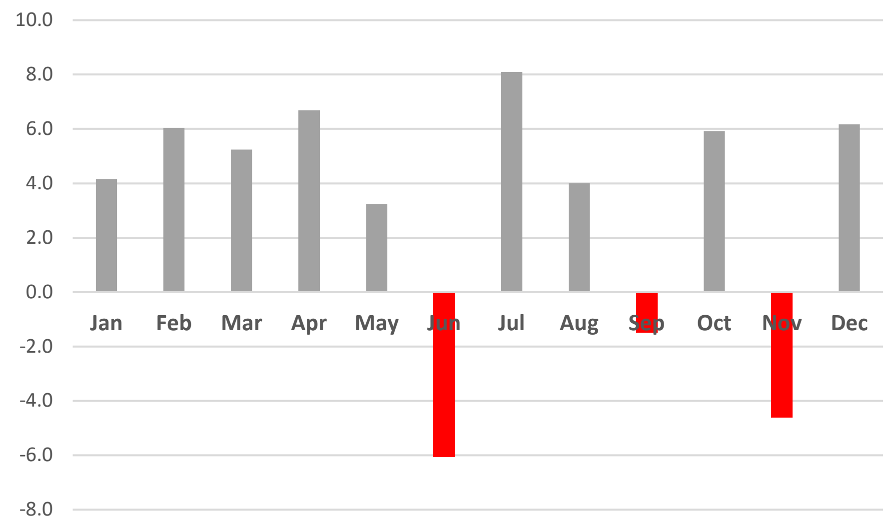
Gleeson led from the front, up 14.9%, with able support from Cairn (+14.1%) plus double-digit percentage gains at Berkeley and Redrow. At the other end, Crest Nicholson (-1.4%) and Abbey (-2.0%) were the only negative images.

We have also added Springfield Properties, the Scottish impressionist, in 4Q, after its 16 October IPO.

In total, 4Q had 63 trading days and 13 weeks with rises on 34 and nine of these, respectively.

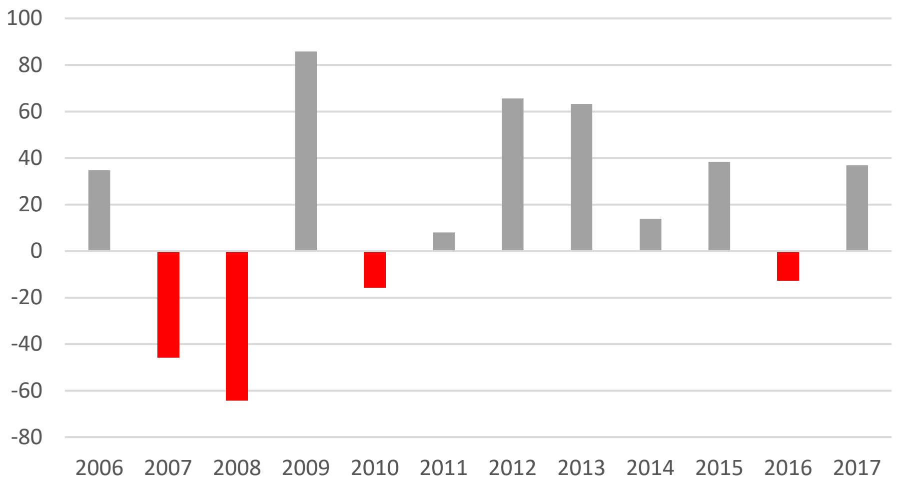
4Q 2017 also marks the 26th quarter from the last 32 in which Housebuilders' average share prices have risen.

UK Housebuilding Sector: monthly 2017 YTD (% change in share prices)



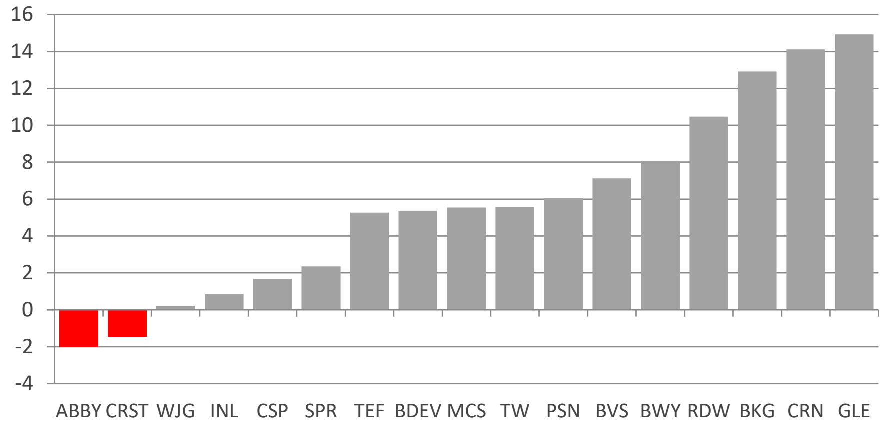
Source: Hardman & Co Research

UK Housebuilding Sector: annually 2006-17 (% change in share prices)



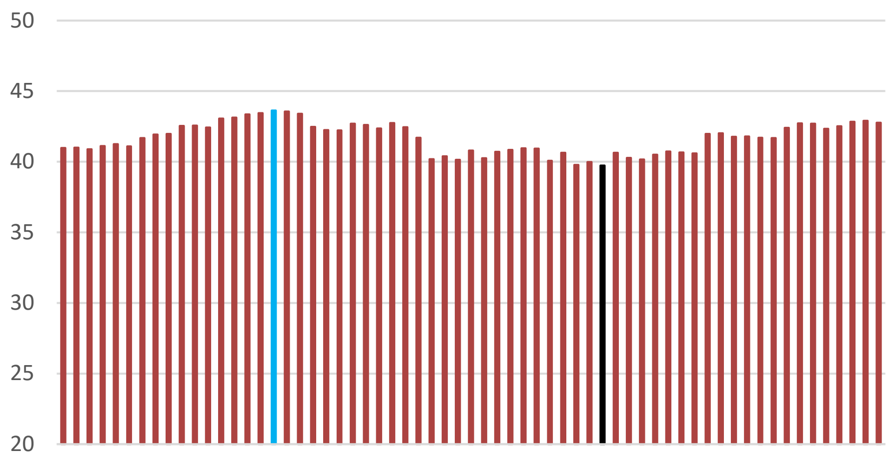
Source: Hardman & Co Research

Share prices in 4Q 2017 versus 3Q 2017 (% change)



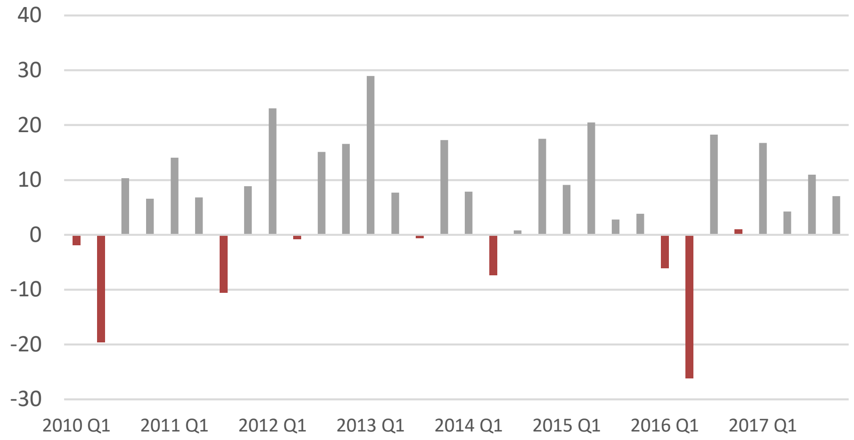
Source: Hardman & Co Research

Housebuilding Sector daily stock market value in 4Q 2017 (£bn*)



Source: Hardman & Co Research
**Blue denotes peak (24/10/17) and black denotes low (28/11/17)*

UK Housebuilding Sector share prices: 1Q 2010 to 4Q 2017* (% change)



**weighted % change in share prices quarter by quarter*
Source: Hardman & Co Research

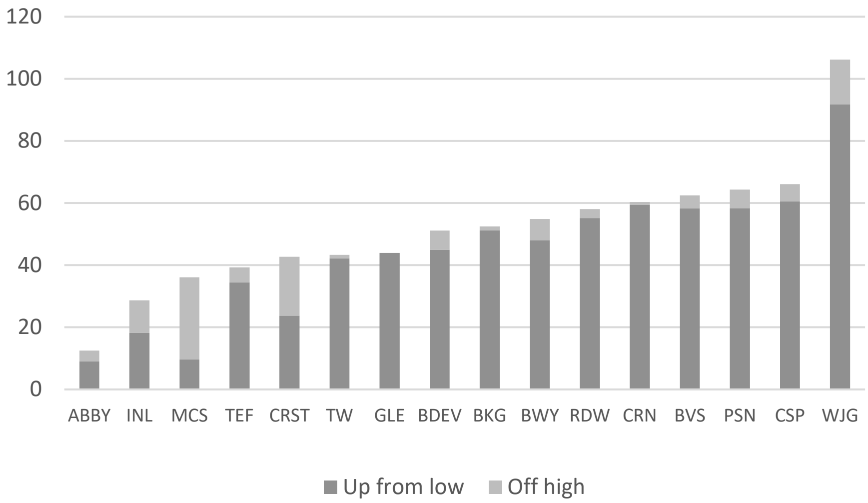
Peaks and values

Housebuilders' share prices are, on average, 20 times above the lows of 2008 and 44% up on more recent 52-week lows (weighted, these numbers are 29 times and 49%, respectively).

However, they are also some 8% below their 2007 peaks (13% weighted) and 6% off 52-week highs (5% weighted).

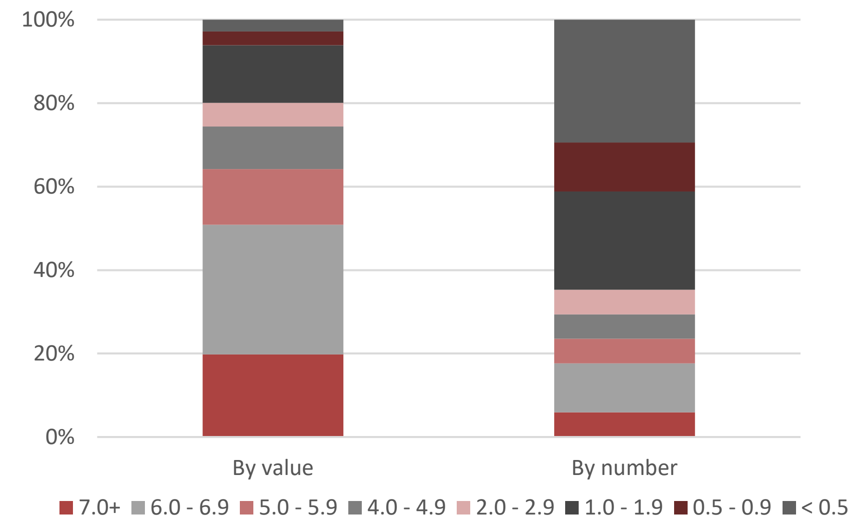
Nonetheless, four housebuilders continue to mix in the FTSE 100: Berkeley (number 85); Barratt (72); Taylor Wimpey (67); and Persimmon (53). And, together, these four account for 64% of the UK Housebuilding Sector value.

Movement against 52-week lows and highs (% change)



Source: Hardman & Co Research

Sector structure by stock market value: 17 firms worth £42.8bn at 29/12/17*



**Legend is in £bn*
Source: Hardman & Co Research

Current share price as % of all-time peak level at 29/12/17* (red shading)

**except Abbey in Euro cents; and ex Cairn, Crest, McCarthy & Stone, Countryside & Watkin Jones*
Source: Hardman & Co Research

Price-to-Book and Total Return

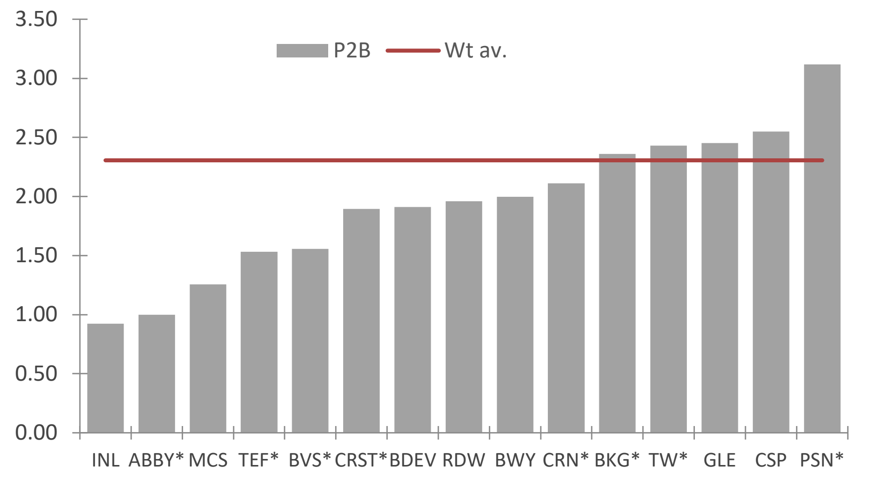
The Housebuilders' latest average Price-to-Book valuation was 1.94 at 29 December 2017 and 2.21 weighted (at the end of the previous year, the figures were 1.60 and 1.82 respectively).

Six out of 15 companies are at 2.0 or better with Persimmon above 3.0 (with Watkin Jones, at 4.96, excluded).

Total Shareholder Return (TSR) for the Sector in 2017 was 42% and 51% weighted (data are drawn from Bloomberg); and this compares with -10.2% and -8.0%, respectively, in 2016.

In 2017, Watkin Jones was the resounding winner of the domestic art competition with a 93% TSR, while, at the other end, McCarthy & Stone was at 0.9%.

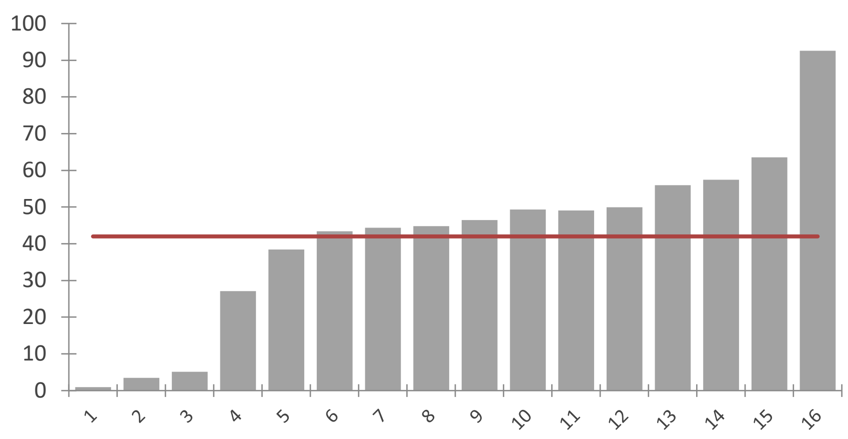
Price-to-Book Value at year-end/latest interim* priced at 29/12/17



**denotes interims; weighted avg. is 2.31 and is shown as a line; actual avg. is 1.94 and ex-Watkin Jones (4.96)*

Source: Hardman & Co Research

Housebuilders' TSR in 12 months to 29/12/17 (annual %)



Source: Bloomberg

Valuation

The Sector's prospective PERs are 11.1x in 2017 (with only six still to report), followed by 9.5x in 2018 and 9.4x in 2019. These are based on consensus forecasts and results for 15 companies in 2017, 15 forecasts in 2018 and 10 forecasts in 2019 (loss-making Cairn is excluded pro tem).

Earnings growth is forecast at 14% in both 2017 and 2018. However, 2019 growth is expected to slow to 2% on the storyboard.

Berkeley is forecast to see earnings drop sharply in 2019 which affects the average; perhaps it is a more honest painter?

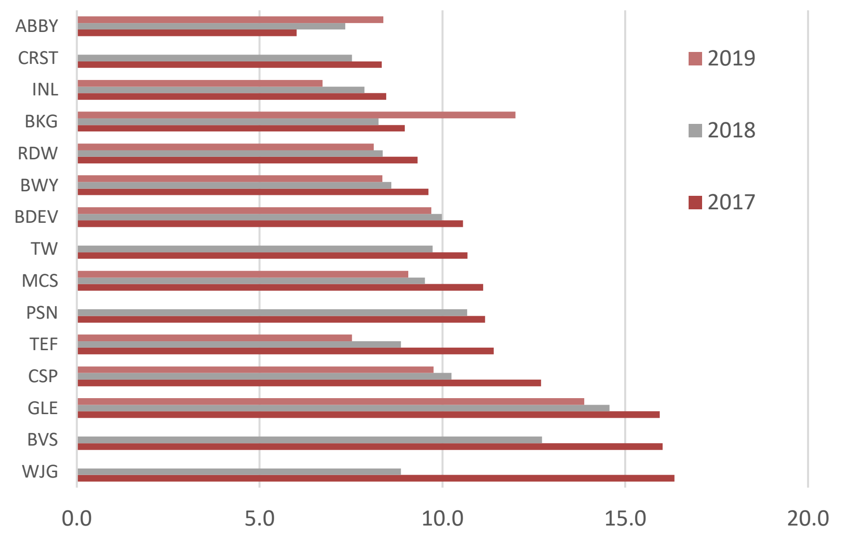
For the record, trailing 12-month PERs for the UK equity market's principal indices range from 18.4x to 22.5x.

Turning to income, in 2017E and 2018E, the Housebuilding Sector yields 3.9% (including six companies still to report) and 4.3% respectively – covered 3.3x and 3.1x – respectively. In 2019E, the yield is 4.1% covered 3.3x.

Note, too, that a number of companies has committed to layout enhanced dividends which means that Barratt, Crest and Taylor Wimpey are yielding 6.5- 7.5% in 2018E.

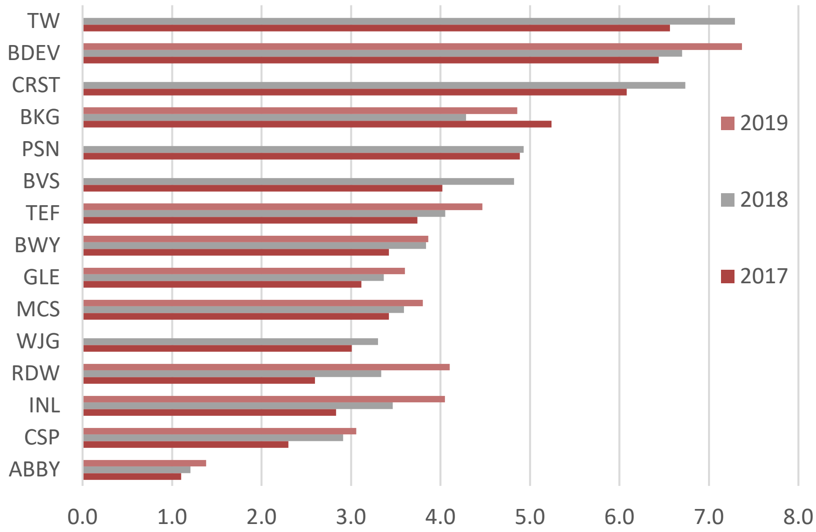
For the record, the UK equity market yields between 2.4% and 3.8% historic with average cover of just 1.5x; all calculations are made at the LSE close on 29 December 2017.

PER: 2017E (11.1x); 2018E (9.5x); and 2019E (9.4x) at 29/12/17



Source: consensus forecasts from Digital Look; Hardman & Co Research

Yield: 2017E (avg. 3.9%); 2018E (4.3%); and 2019E (4.1%) at 29/12/17



Source: consensus forecasts from Digital Look; Hardman & Co Research

Results and trading in Q4

In 4Q, there were three sets of final results, three interims and 22 other trading-related Sector announcements.

Average individual pre-tax profits for the 4Q reportees rose 18% year-on-year, while EBIT margins inched up from 19.2% to 19.8% on revenue larger by 15% annualised at a touch over £6 billion

EPS rose 11% on average (including two negatives) albeit this excluded Countryside's +71%. On the same basis, dividends were raised 11% (ex CSP's +147%); in turn, average individual cover dipped from 2.5x to 2.2x period on period (ex-Abbey's 11.6x and 11.1x respectively.

The average increase in orders was 6% (from a sample of four).

Average individual ROCE dipped 30 basis points to 20.3% with Capital Turn pretty much static at 0.87 versus 0.85 reporting period on reporting period.

Profit & Loss

Date	Company	Half or Full Year	Period ending	Pre-tax profit (£m) Old	Pre-tax profit (£m) New	PBT (% chge)	EBIT margins Old (%)	EBIT margins New (%)	Orders % chge	DPS % chge	DPS cover (x) Old	DPS cover (x) New
08-Dec	ABBY(€)	Half	31-Oct	22	23	9	24.4	25.9	-	14	11.6	11.1
08-Dec	ABBY(£)	Half	31-Oct	18	21	-	-	-	-	-	-	-
17-Oct	Bellway	Full	31-Jul	481	561	17	22.0	22.3	17	13	2.9	3.0
08-Dec	Berkeley	Half	31-Oct	366	505	38	26.3	30.5	-11	0	2.1	3.0
22-Nov	CSP	Full	30-Sep	98	155	59	15.8	16.0	8	147	4.8	3.3
14-Nov	MCS	Full	31-Aug	105	94	-10	16.9	14.6	11	20	3.6	2.6
29-Nov	Telford	Half	30-Sep	9	9	-4	9.9	9.7	-	11	1.4	1.2
TOTAL (£m)				**1076**	**1344**							
Individual average change (%)/Cover (x)						**18**			**6**	**12**	**2.5**	**2.2**
Sector average change (%)						**25**				**12**	**2.8**	**3.2**
Individual average margin (%)							**19.2**	**19.8**				
Sector average margin (%)							**21.4**	**22.4**				

Source: Company announcements and Hardman & Co Research
(i) Pretax profit (PBT) numbers are adjusted where necessary and are net of exceptional items
(ii) EBIT is earnings before interest and tax; and DPS is dividend per share
(iii) Abbey is Irish-domiciled (hence the Euros) and listed in Dublin and London; GBP only included in totals
(iv) DPS is dividend per share and average change excludes Countryside while average cover is ex-Abbey
(v) Berkeley data exclude Ground Rents
(vi) Telford data include JVs; and it had forward sales of £580 million end-November 2017 which is almost two times annual revenue

Balance Sheets

Date	Company	Half or Full year	Period ending	Net assets (£m)		Net (debt)/cash (£m)		*Gearing*	*Gearing*	*ROCE Old %*	*ROCE New %*	*Capital turn (x)*
				Old	New	Old	New	*Old %*	*New %*			
08-Dec	ABBY(€)	Half	31-Oct	266	315	85	90	*-32*	*-28*	*16.2*	*14.8*	*0.6*
08-Dec	ABBY(£)	Half	31-Oct	239	277	76	79	-	-	-	-	-
17-Oct	Bellway	Full	31-Jul	1,867	2,191	26	16	*-1*	*-1*	*25.9*	*25.7*	*1.2*
08-Dec	Berkeley	Half	31-Oct	1,969	2,409	208	627	*-11*	*-26*	*35.3*	*34.4*	*1.1*
22-Nov	CSP	Full	30-Sep	531	623	12	77	*-2*	*-12*	*21.9*	*26.2*	*1.6*
14-Nov	MCS	Full	31-Aug	627	674	55	34	*-9*	*-5*	*15.5*	*14.1*	*1.0*
29-Nov	Telford	Half	30-Sep	189	209	-34	-61	*18*	*29*	*8.5*	*6.7*	*0.3*
TOTAL (£m)				**5,422**	**6,380**	**344**	**772**					
Individual average change (%)					***14***							
Sector average change (%)					***18***							
Individual average ROCE (%)+Turn										**20.6**	***20.3***	***1.0***
Sector average ROCE (%)+ Turn										***25.1***	***25.7***	***0.9***
Individual average gearing (%)								***-6***	***-7***			
Sector average gearing (%)								***-6***	**-12**			

Source: Hardman & Co Research

Notes: (i) ROCE is return on capital employed; and adjusted where required for half years where appropriate
(ii) Abbey held restricted cash of Euro 0.7 million at 31/10/17 (Gilts and restricted cash of Euro 15.0 million at 31/10/16)

Performance and outlook

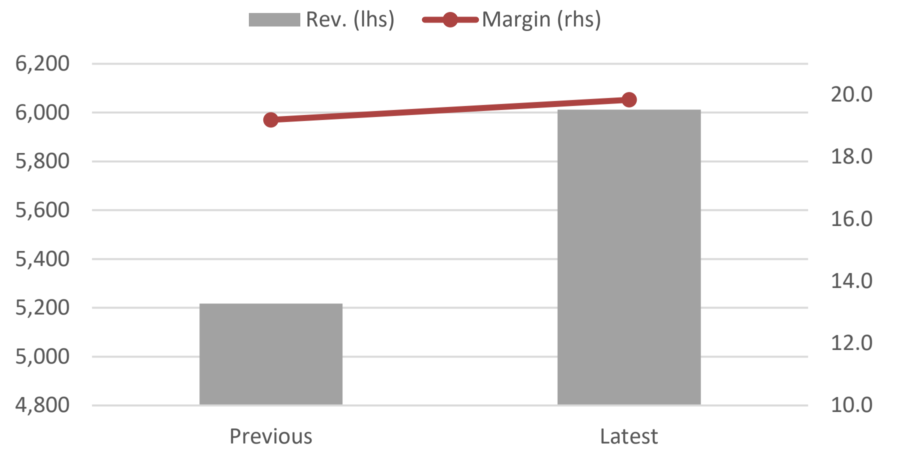
Bellway (Finals – 17 October)

This year, to 31 July 2017, lacquered up another first-class performance from the thinking man's housebuilder with units up 11% to an unprecedented 9,644 and revenue even better, up 14% to £2.6 billion.

EBIT margins were little changed (22.3% vs 22.0%) and pre-tax profit (£561 million) and EPS were up 13% each (adjusted for 2016's exceptional gain) - as was the dividend.

Perhaps best of all, though, was the order book which was up 17.4% as at 1 October to £1.36 billion representing 5,034 homes, which was ahead 7.1%; and this comprises a 5.6% increase in reservations in the first nine weeks of the new fiscal year (Bellway is a July year-end). The Group also expects volume growth this year and a 5%, on average, increase in selling prices to approximately £280,000.

Sector revenue (£ million) and EBIT margin (%): reported in 4Q 2017



Source: Hardman & Co Research

McCarthy & Stone (Finals – 14 November)

In a bumpy year to 31 August 2017, completions did manage to edge up to 2,302 units (2016: 2,296), while revenue increased by 4% to a new record of £661 million with an average selling price up 3% to £273,000.

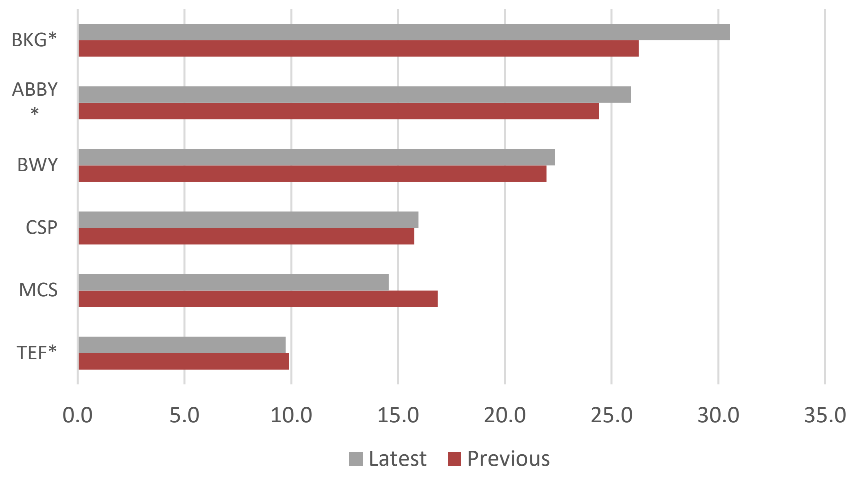
EBIT margins dropped from 16.9% to 14.6% for the year (albeit 17.0% in H2), with profit before tax off 10% at an underlying £94.1 million due to a range of legacy issues.

Underlying EPS fell 12% but the DPS was raised 20% and the Group closed the year with net cash of £31 million

Forward sales as at 10 November 2017 (week 10) were up 11% at £277 million.

"The demand for high quality retirement housing remains strong" and the Group has retained its medium term growth objective of more than 3,000 units per annum.

EBIT profit margins (%) reported in Q4 2017*



**denotes interim results*
Source: Hardman & Co Research

Countryside (Finals – 22 November)

In the 12 months to 30 September 2017, revenue rose 28% to in excess of £1 billion on which the Company earned an adjusted 16.0% operating margin (2016: 15.8%) and a profit of £164.1 million (+34%).

At the same time, profit before tax almost doubled to £142 million and the dividend was hiked 71%.

Looking forward, the Group's year-end private housing forward order book was up 8% to £242.4 million. Countryside also has a thriving partnership unit which accounted for the majority (2,192) of last year's unit output (3,389), leaving 1,197 in the private sector.

"Current trading remains robust with strong demand from owner occupiers"; and since its IPO in February 2016, the shares have risen 57% to 353 pence.

Telford Homes (Interims – 29 November)

In common with a number of its peers, the Group's six-month profit movement, to 30 September 2017, was impacted by the timing of developments and was down £300,000 at £8.7 million.

However, for the current 12-month accounting period it is "well positioned to meet market expectations for the full year to 31 March 2018 with over 95% of gross profit secured".

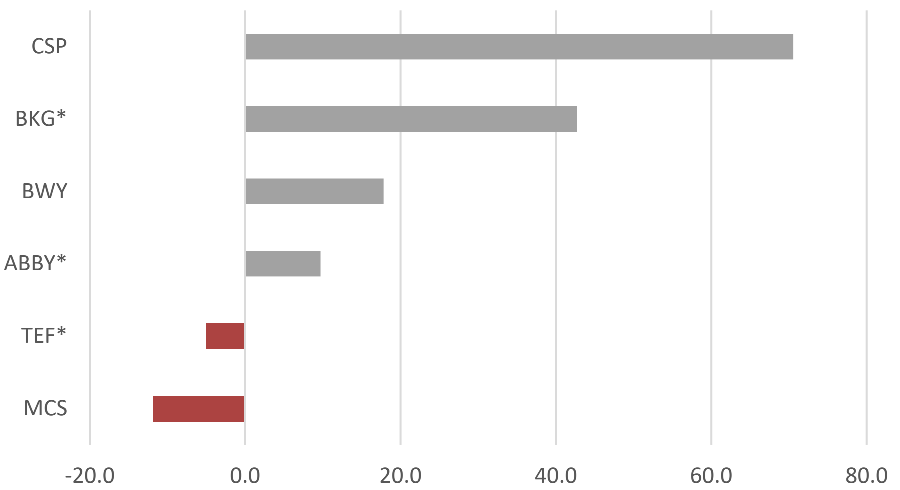
This means it is "on track to deliver over £40 million profit before tax for fiscal 2018 and it has secured over 65% of the gross profit required to exceed £50 million in fiscal 2019".

Telford also boasts a development pipeline of over £1.4 billion of future revenue comprising some 4,200 homes with an expected average selling price £540,000, including build-to-rent and affordable housing.

"Notwithstanding the need for more homes, ongoing uncertainty surrounding Brexit and a lack of political stability has deterred some potential buyers from making a purchase particularly at higher price levels. Changes to the tax system, especially the phased removal of tax relief on mortgage interest, have also dampened demand from UK based investors despite an active rental market in our typical locations”.

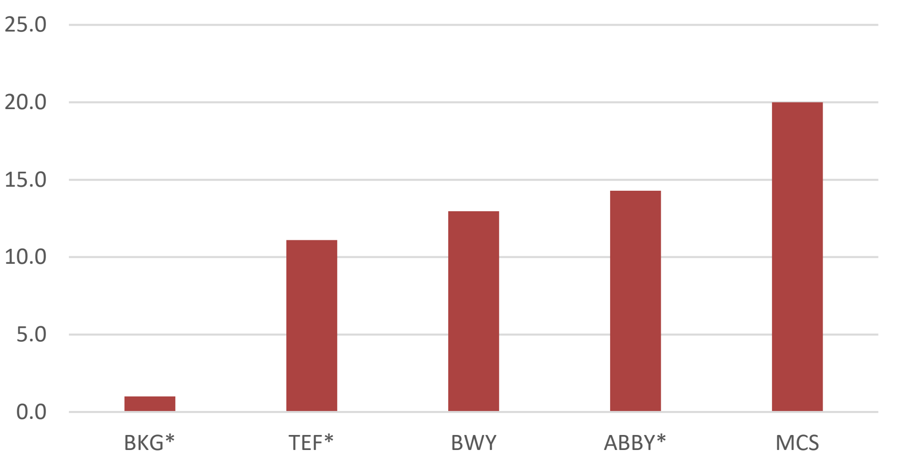
Nonetheless, London – despite facing “a prolonged period of uncertainty” – continues to attract individual investors including those based overseas who typically invest from a larger asset base. There is a growing realisation, too, from Londoners that renting rather than buying is not as undesirable as some make it out to be and the proportion of tenants versus owner-occupiers will continue to increase in the coming years mirroring the situation in many other cities globally”.

EPS growth* (% change) reported in 4Q 2017



**denotes interim results*
Source: Hardman & Co Research

DPS growth reported in 4Q 2017* (% change)



**denotes interims*
Source: Hardman & Co Research

Berkeley Group (Interims – 8 December)

This was a masterclass in communication. Firstly, it described the 'super-duper' financials of the first half (to 31 October 2017), Group strategy and good citizenship. Secondly, it spoke coherently about the risks in the market place as well as the potential undulations of its own performance.

There was a slap or two of politicking and, yes, a whiff of arrogance but that is okay given how well the Group has performed and continues to do. The shares rose 6.9% on the day of the results to £41.13 which was a new all-time high.

Unit sales were only marginally ahead (+2%) at 2,117 in 1H. Prices, however, were 10% better (at an average £719,000) which raised revenue 14% to £1.6 billion – with the net operating margin at a remarkable 30.5% (2016: 26.3%). Inevitably, net pre-tax profit surged 31% to £482 million.

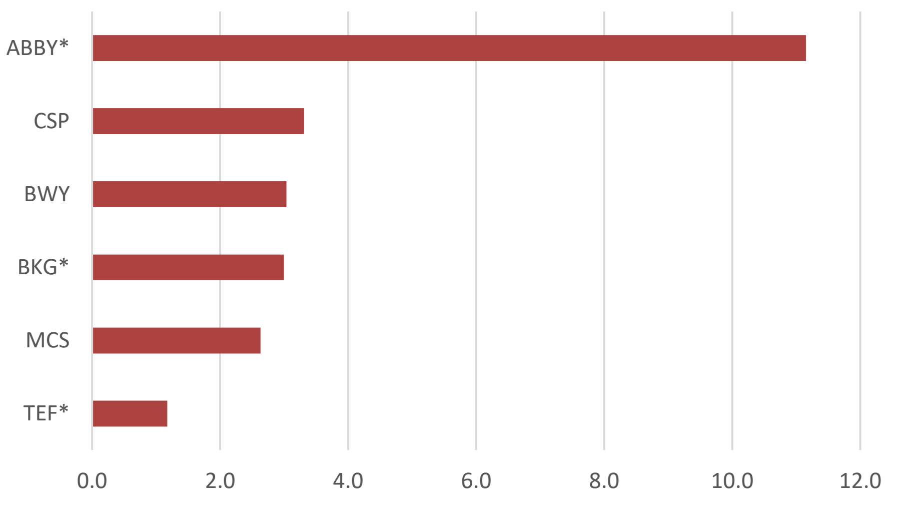
However, "the 2017-18 full year results will represent a peak for Berkeley, before returning to more normal returns in 2018-19. Our guidance of £1.5 billion of pre-tax profit for these two years will be approximately 60% weighted towards the current year".

Yes, Berkeley did increase its earnings guidance by 10% for the five years ending 30 April 2021 to at least £3.3 billion of pre-tax profit from £3.0 billion. However, it also expects operating margins to moderate to more normal levels and a range of 17.5 to 19.5% over the piece.

Similarly, and what appeared to go unnoticed, was the fact that cash due on forward sales had dipped 11% to £2.45 billion against end-April.

But as Chairman Tony Pidgley said: "we should remember, above all, that housing is not a numbers game. Fundamentally, it is about people and community".

Dividend cover (x) reported in 4Q 2017*



**denotes interims*
Source: Hardman & Co

Abbey (Interims – 8 December)

Revenue in Ireland more than doubled in the six months to 31 October 2017, with EBIT up from a Euro 1 million loss to a profit of Euro 2.4 million and a 22.7% margin.

The UK, however, accounted for three-quarters of Group revenue (Euro 68.2 million) and, although EBIT dipped 1.3% in British Pounds, margins remained excellent at 27.9% (2016: 29.2%).

Group EPS rose 10% and the DPS by 14%. Nonetheless, cover remained at more than 11 times. Cover may be luxuriant but the Group's prose remains lean and lithe (i.e. a 453-word Interim Report).

"The recent rise in interest rates in the UK together with moderate economic growth naturally tempers the outlook in the medium term. The uncertainty and dislocation associated with Brexit may impact both Britain and Ireland. Overall however the Group supported by a strong balance sheet continues to plan for growth".

Best-of-the-rest (8, 13 and 15 November):

Persimmon Trading Update (TU) 8 November: 2H 2017 sales were in line with the previous year, while forward sales beyond 2017 were 10% ahead at £909 million;

Taylor Wimpey TU 13 November: the current total order book, excluding joint ventures, was at 8,751 units which was 2.6% down year on year;

Barratt AGM on 15 November: total forward sales (including JVs) were up by 8.4% to £2,876 million; and

Crest Nicholson TU 15 November: "there may be some impact from current economic and political uncertainty", and there was a softer market in Central London, albeit sales rates' below £1 million remain generally strong. At the same time, total forward sales were ahead 13% at 1,997 units.

Inland Homes (Trading Update – 2 January)

This specialist brownfield land developer and housebuilder picked the first business day of 2018 to issue a positive message.

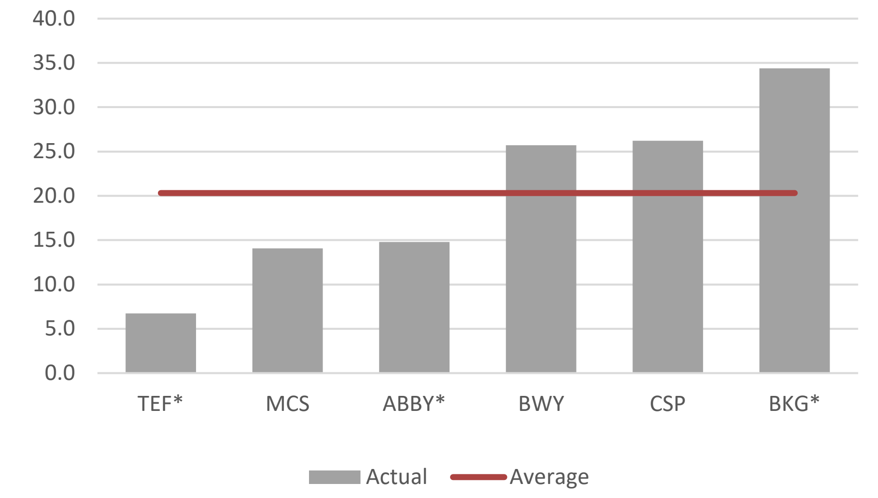
At end-November, the land bank ran to almost 7,000 plots and there has been churn since then including two sites sold for £12.5 million (including one in Birmingham to Crest and another pending.

Inland also has more than 500 housing units under construction plus £41.5 million of partnership housing contracts.

Similarly, more land is in the process of being purchased in Maidenhead and Elstree; and the Company has entered into a joint venture with the Anderson Group, an East Anglia-based construction firm.

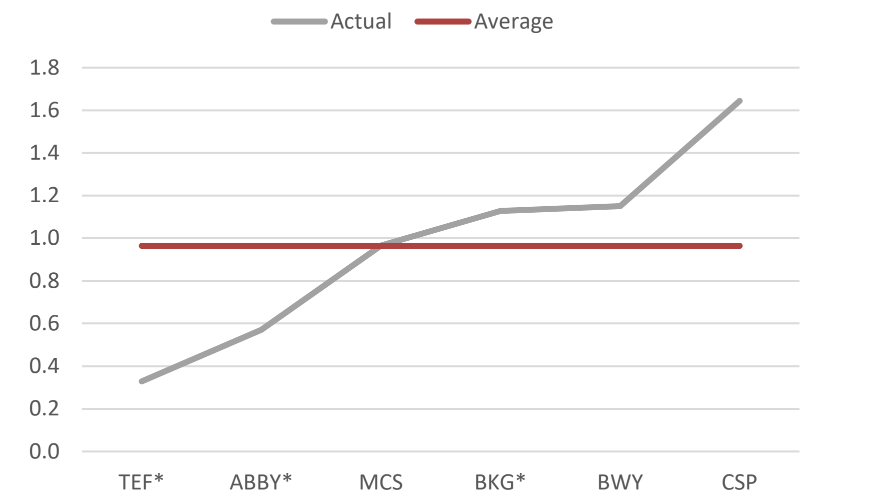
CEO Stephen Wicks said: "as we head into the New Year, Inland Homes is well placed to achieve further significant growth in 2018".

Latest reported and average ROCE (%) reported in 4Q 2017*



**denotes interims; ROCE is return on capital employed]*
Source: Hardman & Co Research

Capital turn (x) reported in 4Q 2017*



**denotes interims; capital turn is revenue divided by capital employed*
Source: Hardman & Co Research

M J Gleeson (Trading Update – 4 January)

"The urban regeneration and strategic land specialist" will report its interim results (to 31 December) on 19 February and promulgated a further Trading Update on the third business day of the year (and this also follows closely on the AGM, which was held on 7 December). It must be good news.

For the record, Gleeson Homes sold 593 units in 1H, which was an increase of 31% annualised.

Gleeson Strategic Land, meantime, was not so busy and sold the same name of sites (three) in each half year (which had been flagged). However, it is progressing the sales of a further eight sites from what is a chunky pipeline of 63 sites (12 with planning permission) comprising 21,455 plots.

"The Group results for the first half-year are expected to comfortably exceed those of the prior year comparable period".

Macroeconomics

GDP growth in the UK was confirmed at 0.4% in 3Q 2017 (vs 2Q 2017) including strong Services and a strengthening of household spend. Year on year, the volume gain is 1.5%.

The Consumer Price Index (CPI) continues to rise and was at 2.8% annualised in November 2017 which was the same as in October but up from 1.2% in November 2016.

Unemployment was at 4.3% in the October quarter which compares with 4.8% a year ago; and both tend to indicate 'full employment' by any rational definition.

Finally, Retail Sales in November, by volume, increased 1.1% month on month and 1.6% annualised; note, too, that food stores saw their largest price increase in November (i.e. 3.6%) since September 2013.

Mortgages

UK Finance (incorporating the BBA and CML data) said house purchase mortgages by High Street banks fell to 39,507 in November which was 2.3% adrift of October and minus 5% annualised (note that BBA is the British Bankers Association and CML is the Council of Mortgage Lenders).

Turning to Bank of England data, mortgage approvals in October 2017 (67,709) edged up 2.2% but were a touch below (i.e. minus 0.7%) October 2016.

Volumes and prices

Experian (where I am advisor) estimates that Private Housing Output will have risen 6% last year, with then 5%, 4% and 1% growth forecast for 2018, 2019 and 2020 respectively (all in real terms). Meantime, the Public Sector, from a low base, is forecast at +8%, +3% and +6% on the same basis (after an estimated +6% in 2017).

Turning to house prices, the Nationwide posted the annual gain at 2.6% in 2017 (4.5% in 2016) across the UK, with London off 0.5%; and its forecast is for +1.0% this year which would be the lowest rise since 2012.

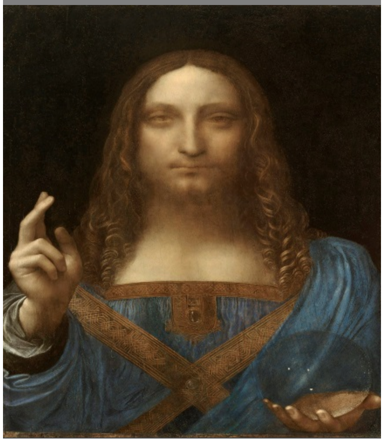
Elsewhere, Rightmove said that 2017 closed with an annual gain of 1.2% and the forecast for 'new seller asking prices' this year is 1.0% which includes higher gains for first-timers and second steppers – and top-of-the-ladder falls in London and its commuter belt. Nice imagery.

Then, at the Halifax it is keeping its options open with a 2018 forecast of a zero to 3% rise including weakness in London and the south east of England.

Finally, the Reuters Housing Market Poll (to which I contribute) expects a median +1.3% for UK house price inflation in 2017 (including -0.3% in London), and then +2.3% in 2019, followed by a 3.0% increase in 2020.

The Da Vinci Code

Salvator Mundi



Source: Creative Commoms

In arts, science and sport being known by a single name is an apogee and the Italian Renaissance polymath was latterly known simply as Leonardo. He has also been called the father of palaeontology, ichnology and architecture, as well as being dubbed one of the greatest painters of all time. In November last year, too, one of his works, 'Salvator Mundi', sold for a World record US$ 450.3 million. He was also famous for his wisdom and a favourite dictum was: "just as courage imperils life, fear protects it".

Despite the beauteous equivalence of last year's 43% increase in value to £43 billion, a number of the UK's listed housebuilders are, more prosaically, heedful of the latter of Leonardo's emotion as 2018 commences.

Berkeley has probably been most utilitarian with guidance of a significant annualised fall in pre-tax profits in fiscal 2018-19 (as at the exhibition of its Interim results on 8 December). Similarly, it said that looking out to fiscal 2020-21, the end of its guidance period, operating margins will moderate to more normal levels of 17.5 to 19.5%; and, in H1 of fiscal 2017-18, the net operating margin was 30.5%. At the end of its the half year, too, cash due on forward sales had dipped 11% to £2.45 billion against end-April.

The minimalist **Abbey** (also painting on 8 December) added that "the recent rise in interest rates in the UK together with moderate economic growth naturally tempers the outlook in the medium term. The uncertainty and dislocation associated with Brexit may impact both Britain and Ireland".

Telford, a strictly London artist, is largely sold out of works for two years (as at 28 November). However, it also noted "ongoing uncertainty surrounding Brexit and a lack of political stability" and that the phased removal of tax relief on mortgage interest has dampened demand from UK-based investors. It added, too, that London is facing "a prolonged period of uncertainty".

Earlier, on 13 November, **Taylor Wimpey** sketched a current total order book, ex-JVs, which was 2.6% lower at 8,751 units.

It was followed by **Crest Nicholson**, on 15 November, and its comment: "there may be some impact from current economic and political uncertainty". It also spoke of a softer art market in Central London, albeit that sales rates' below £1 million remained generally strong.

To be fair, other housebuilders – see earlier pages – are more positive with their brush work.

What is certain, though, is that the UK listed Housebuilding Sector has reinvented itself since the Global Financial Crisis (GFC) – okay, with the help of £5.3 billion of provisions during 2008-10 (i.e. 41% of the pre-GFC combined net asset value) and £1.7 billion of new cash from their shareholders.

It is wiser now, too, better managed, largely ungeared and spectacularly generous with dividends.

The UK economy is none of these and, although it is forecast to grow at 1-to-2% per annum through 2020, this is below trend. Inflation is rising, too, household incomes and consumption are under pressure; and Brexit etches large.

For the housebuilders, this also means that volume growth is tight, prices are under pressure (and with them margins) which means commensurate pressure on earnings growth i.e. 2% in 2019 based on consensus forecasts.

43% and £43 billion are likely not to be re-drawn in 2018; albeit in Week 1 of the New Year (four trading days) the Sector rose 1.6% in value, pretty much where it had left off in December.

Both Gleeson and Inland also issued very positive Trading Updates on 2 and 4 January and both share prices rose sharply.

We believe there could well be a profit warning early in 2018 too but, as with Berkeley, it appears honesty can be rewarded.

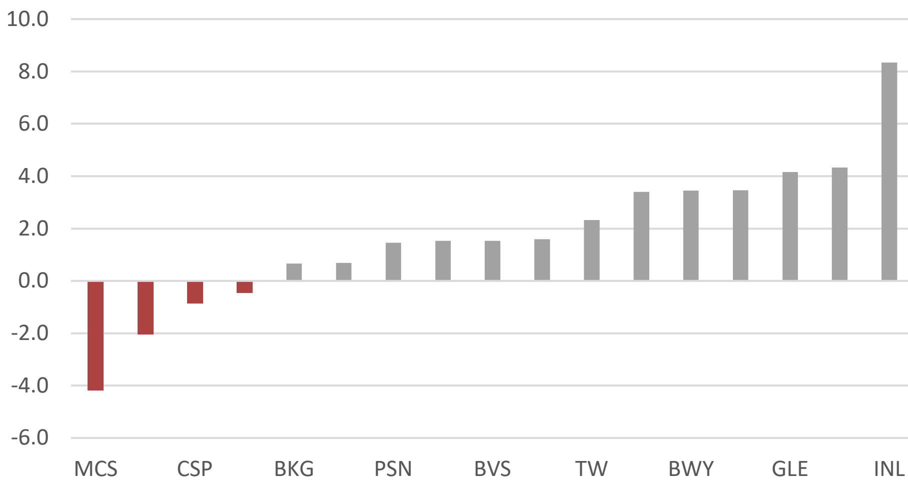
Near term, the Sector may well continue to rise but it remains on a single-digit PER a year out for a reason i.e. it is still not trusted by art lovers.

Quote:

"Just as courage imperils life, fear protects it".

Source: Leonardo da Vinci

Housebuilders share prices in Week 1 of 2018 (% change YTD)



Source: Hardman & Co Research

Glossary

Abbey (ABBY)

Barratt Developments (BDEV)

Bellway (BWY)

Berkeley Group Holdings (BKG)

Bovis Homes Group (BVS)

Cairn Homes (CRN)

Countryside Properties (CSP)

Crest Nicholson Holdings (CRST)

M J Gleeson (GLE)

Inland Homes (INL)

McCarthy & Stone (MCS)

Persimmon (PSN)

Redrow (RDW)

Springfield Properties (SPR)

Taylor Wimpey (TW)

Telford Homes (TEF)

Watkin Jones Group (WJG)

Note: Share prices at 29 December 2017
Adjustments have been made to share prices where required
Selected stocks are excluded from charts and sector averages due to extreme movements or for structural reasons

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(Disclaimer Version 2 – Effective from May 2017)

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The fact that we are commissioned to write the research is disclosed in the disclaimer, and the research is widely available.

The full detail is on page 26 of the full directive, which can be accessed here: http://ec.europa.eu/finance/docs/level-2-measures/mifid-delegated-regulation-2016-2031.pdf

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