HALF-YEAR STATEMENT **2021**

ANNINGTON

Half-Year Statement 2021:

Following the publication of the Annual Report for the year ended 31 March 2020, I am pleased to provide a half-yearly update on the performance of the Annington Limited Group.

Market Environment

The first half of the financial year began with the country and the world reeling from the emergence of COVID-19 and economic activity effectively grinding to a halt. The consequential impacts upon normal life were significant, with the Government announcing a UK-wide lockdown commencing on 23 March. Due to this announcement, work on 43% of construction sites – including all Annington sites – ceased. The residential sales market came to a stop as estate agents were no longer able to conduct viewings and mortgage lenders were unable or unwilling to offer mortgages to buyers ready to make offers.

There was swift action to try to get the construction sector back to work starting in early April with the publication by the Construction Leadership Council (CLC) of the Site Operating Procedure (SOP), which was designed to ensure safe conditions on site. The property market officially reopened on 13 May and market commentators considered that eight weeks of construction and sales activity was lost.

House moves and viewings were able to recommence in May and following the easing of the first lockdown at the start of July, the residential housing market, in stark contrast with the rest of the economy, has enjoyed a mini boom, creating a momentum that has surprised many commentators. An initial increase in home purchases and house moves might have been fuelled by the release of pent up demand but the market undoubtedly has been supported by economic stimuli. In addition to the existing stimulus from the help-to-buy scheme, as part of wider coronavirus support package measures, the Chancellor of the Exchequer announced an SDLT holiday until 31 March 2021 and Coronavirus wage support programmes.

While low deposit mortgages have disappeared from the market, overall mortgage approvals are now close to pre-pandemic levels. With so many working from home for an extended period, there has been time to consider requirements such as proximity to work and lifestyle. With the potential for further lockdowns, there is a determination in purchasers to act. A key driver has been the search for more room, a garden and green space; a two-tier market is developing with strong demand for smaller three and four bedroom houses in particular, something that looks increasingly like it will become an established trend. First-time buyers, historically a driving force for sales, are struggling amid growing economic uncertainty and reduced availability of higher LTV mortgages. This has led to a slight shift in the mix of moving households towards second-steppers.

Pricing has been resilient and volumes have recovered in the latter part of the year. According to the Land Registry, the average price of a property in the UK was £244,513 in September 2020, reflecting a 4.7% increase from the year before and a 5.5% increase from the £231,855 average price reported for March 2020. Property market transaction volumes decreased during the period but by September had returned to pre-COVID levels, with residential transactions valued at £40,000 or more being at a higher level in October 2020 than any time since March 2016, when changes to Stamp Duty legislation caused unusually large transaction volumes.

This has led to some commentators urging caution about the market's prospects. Rightmove has estimated that there are nearly 40% more sales going through the buying and selling process compared to last year, leading to congestion of sales in progress – something that may affect the buying power of those looking to take advantage of the stamp duty holiday over the next few months.

There has been strong demand in the rental market since May, when many renters took the first opportunity to move and where possible obtain more space. This has been tempered by concerns in the market relating to an increase in rental arrears brought on by the moratorium on rental evictions which ended on 20 September, with courts now facing a substantial backlog of cases. The Office of National Statistics reported that private rental prices paid by tenants in the UK increased by 1.5% in the 12 months to September 2020. Regional variation is still evident, with private rental prices in the South East only showing a 1.0% increase in the year to September 2020 but the East Midlands region recorded increases of 2.6% in the same period.

Operational Update

In spite of the COVID-19 pandemic, Annington, for the most part, has continued conducting business as usual. With more than 94% of rental income being Government backed and derived from the MQE and bulk leasing arrangements, the Group has been less affected by the pandemic than many other businesses. Consequently, the Group's only real financial exposure during the COVID-19 pandemic has been to bad debts and arrears arising from the Group's AST rental properties.

Acknowledging the impact of COVID-19, our AST portfolio has performed steadily. Whilst there was an increase in void and arrears levels during the initial lockdown, Annington's exposure remained insignificant within the context of the total portfolio. Voids and arrears within the portfolio have reduced more recently to levels comparable with pre-COVID-19 periods. These areas continue to be closely monitored.

Importantly, progress continued on the expedited Site Review with the MoD, albeit with hearings on the first batch of four sites being delayed to July as a result of COVID-19, with final awards for that batch being made in early October. Work continues on the second batch of eight sites, for which hearings are scheduled during February 2021.

Operating sites were back to full working capacity by the end of June, although the impact of COVID-19 on the supply chain did lead to some materials shortages and minor delays on a few of our sites. This did not prevent Annington from completing the refurbishment of 136 ex-MQE properties across seven sites and 34 new build units on sites at Brize Norton and Little Thetford.

During the first half of the year, 83 units were sold (81 investment properties and 2 units from inventory). This compares to 33 units in the comparative period last year. The increase is largely reflective of the higher volume of MQE releases since the signing of the Arbitration Agreement in March 2019, incentivising the MoD to release 500 units annually. A further 24 units were sold on our new build site at Brize Norton, where the strategic decision for those units was to sell, rather than to rent them.

In the six months to 30 September, the MoD handed over 99 units, with termination notices received for a further 223 units, taking the forecast number of releases to 322 for the 2020-21 financial year.

Outlook

With the stronger than expected rebound in the housing market after the initial nationwide lockdown, market commentators have revised short-term forecasts upwards. At the end of September, Savills was predicting 4% price increases in the 2020 calendar year. As recently as June, Savills were predicting price falls of 7.5% for the same period.

At the same time, caution prevails over medium-term forecasts. The RICS noted in their November 2020: UK Residential Market Survey that "near-term expectations for both prices and transactions point to a more moderate picture emerging over the coming months". Similarly Savills currently forecasts flat house prices for the 2021 calendar year, where in June they had been forecasting a 5% increase. Beyond the impacts of COVID-19, these sentiments are also attributed to the impact of the Brexit negotiations.

Rental demand has remained buoyant throughout the tail end of 2020, with the RICS reporting steady demand. Rental inflation forecasts are mixed, with Savills forecasting 5.5% growth through the 2021 calendar year but JLL predicting a fall of 1.5%. Savills notes that household income will be the main constraint on rental growth.

The medium- to long-term impacts of the COVID-19 pandemic remain uncertain. There are shifts in demand being experienced due to the impacts of homeworking brought about by the COVID-19 lockdowns, with shifts towards larger properties and moving away from city centres. In addition, the pandemic has delayed housebuilding within the UK, a market that was already not building sufficient houses to keep up with forecast demand. As such, the supply and demand imbalance may be further impacted, with consequential impacts on pricing and affordability.

Operationally, we are working on the remainder of last year's 266 releases and the 99 units released from the MQE during the first half. We are preparing for the remainder of the 322 units to be released before the end of March. The new build sites at Brize Norton and Allington are forecast to be completed during the 2021 calendar year.

We continue to focus on ensuring that we are prepared for the next batches of the Site Review negotiations and concurrent Beacon Unit Rent Reviews. With the receipt of the first batch of Site Review awards early in October, our focus has shifted to preparation for the second batch hearings due to take place in February 2021.

The eventual awards of the Panel will be key to the path Annington takes in the future. We understand that the General Partner to the Terra Firma funds that form a majority of the Group's equity investor base is considering exit options, with the end of these funds lives drawing nearer. Annington management continues to consider what it needs to do to make itself ready for all exit eventualities and this will become an increasing focus.

As always, we will continue to focus on actively managing the Group's current operations and developments. We will continue to manage tenancies and rental levels, and assess potential options to enhance value, including refurbishment, redevelopment and disposal.

James Hopkins
Chief Executive