Our place in the housing market

To understand how our market impacts our operations we start by considering our place in the wider housing market. We completed 15.7k homes this year and are one of the UK's largest homebuilders.

To put that in context, UK new build transactions for the year to March 2019 were around 203k, putting our share of the new homes market at around 8%. However, we are also part of a much larger market which sees around 1.2m in annual housing transactions of which around 83% relate to second hand or existing housing. Being a small but important part of a much larger market has clear implications for our strategy, particularly in terms of market positioning and pricing power.

In recent years the relative performance of second hand and new build transactions has diverged. The second hand market has undergone a difficult period owing to political uncertainty, particularly in higher priced areas such as London and the South East where sales have been sluggish. Over the same time period demand for new homes has been robust and we have grown our UK new home completions by 8% since 2017.

This divergence is partly explained by the different customer drivers impacting each market. Second hand house sales tend to be more discretionary, as sellers, and some buyers already own property and are often more willing to defer sales and purchases than first time buyers, who may be adults living with parents or those starting new families.

In addition, the Help to Buy Equity Loan scheme introduced in 2013, which has assisted many buyers to access housing, is only available for new build homes. Under the current scheme the Government will lend up to 20% of the value of a new build home via an equity loan (interest free for five years) to homebuyers outside Greater London (40% within Greater London) who are able to meet certain criteria, including raising a 5% deposit.

Total housing completions 2018-2019

c.1.2m

New build completions 2018-2019

c.203k

Sources: HMRC, ONS.

Key customer drivers

The key drivers of our market; house prices, inflation and interest rates, mortgage affordability and availability, and employment and consumer confidence, are interlinked. The minimum deposit requirements of mortgage providers plays a key role in our customers' ability to access home ownership, particularly in the case of first time buyers. For this reason, the Help to Buy scheme has been important for the sector.

For those able to achieve the necessary deposit to buy a home, affordability is good. Current low interest rates and widespread availability of mortgages at competitive rates mean that, on average, today's new owners can expect to pay a lower proportion of average household income towards their mortgage than they would have back in 1984 (see chart on page 19).

Interest rates

Impacts
- Affordability (mortgage rates)

Contributing factors
- Inflation
- Economic growth
- Consumer confidence

Medium term expectation
- Remain low
- Potential for modest basis points moves in either direction

Long term expectation
- Dependent on UK economy
- Likely to rise steadily from low base

Mortgage availability

Impacts
- Credit availability for house purchases
- Mandated deposit requirements of lenders

Contributing factors
- Interest rates
- Liquidity of banks
- Economy

Medium term expectation
- Remain low

Long term factors
- Dependent on UK economy

Employment

Impacts
- Consumer confidence
- Wage growth

Contributing factors
- UK economic performance
- Business confidence

Medium term expectation
- Record employment levels
- Dependent on public and private investment outlook
- Dependent on inflation

Long term expectation
- Dependent on UK economy
- Dependent on impacts of trade deal with EU
- Dependent on global economy

Help to Buy

Impacts
- Affordability for homebuyers

Contributing factors
- Adaptability of lenders to provide alternative products

Medium term expectation
- Price caps in place from 2021 and restricted to first time buyers with scheme to phase out by 2023
- Potential market adjustments as scheme ends
- Dependent on alternative financing options available

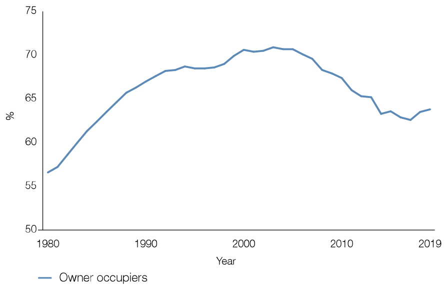
Long term factors
- Dependent on UK economy
- Structural undersupply should underpin market demand

PR Read more on pages 48 to 53

Unsatisfied demand for homes

For the medium to long term, demographic factors such as changes to population and household formations and the rate of home ownership will impact demand from our customers. The rate of home ownership has fallen from its peak in the early 2000s of c.70% to c.64% in 2018. This reflects stretched affordability, and according to HSBC, the average age of first time buyers in July 2019 was 33 and could rise to 40 in the next decade. This suggests that accessibility to home ownership remains an issue, something we are keen to address, and that underlying demand for housing overall is likely to continue to outpace supply for some years.

The home ownership rate in England



Source: Ministry of Housing, Communities and Local Government.

Affordability and mortgage availability

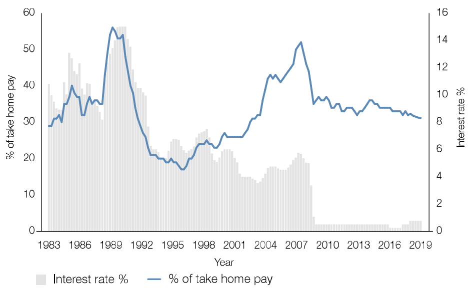
Homebuyers who are able to raise a deposit often find monthly mortgage costs lower than the alternative cost of rental for comparable properties (on average £666 per month versus £722 per month[1]). The relative cost of buying to renting depends on interest rates and, while there are no imminent signs of major rises, in the longer term we would expect interest rates to rise, albeit gradually and well signalled, from historic lows.

By other traditional metrics, affordability of housing, be it buying or renting is more stretched. The housing to average earnings ratio, important in determining how much lending a mortgage company will provide, was 6.7 times in August 2019[2] having eased back, yet remained close to the 2007 peak.

The UK Government led the Mortgage Market Review (MMR) in 2009 following the financial crisis. The MMR found prior instances of high-risk lending to people unable to afford their mortgages. New measures to regulate lending came into force in 2014 and stricter criteria impacted upon the ability for some people to gain access to housing. Overall availability of mortgage products remains healthy and UK mortgage approvals for December 2019 were at their highest rate since 2015.

1. Sources: Halifax, BM Solutions, ONS.
2. Sources: Zoopla, ONS.

UK first time buyers mortgage payments as a percentage of pay/interest rates



Sources: Nationwide, Bank of England.

Our performance in 2019

Despite wider macro-economic and political uncertainty, the UK new build housing market remained stable during 2019, albeit with more challenging conditions in London and the South East and at higher price points. Customer demand for new build homes continued to be robust, underpinned by low interest rates, a wide choice of mortgage products and the Government's Help to Buy scheme. During the year, we saw good levels of demand throughout the country, which converted into strong sales rates across the business.

In 2019, total home completions increased by 5% to 15,719, including joint ventures (2018: 14,933). During 2019, we delivered 3,548 affordable homes (2018: 3,416), including joint ventures, equating to 23% of total completions (2018: 23%). Average selling prices on private completions increased by 1% to £305k (2018: £302k), with the overall average selling price increasing to £269k (2018: £264k).

We estimate that market-led house price growth for our regional mix was c.1% in the 12 months to 31 December 2019 (2018: c.3%).

Our net private sales rate for 2019 remained strong at 0.96 homes per outlet per week (2018: 0.80). Consistent with our strategy to optimise our large sites, and our long term approach to reducing cyclical risk by maintaining a strong order book, we achieved a strong sales rate of 0.92 in the second half of the year (H2 2018: 0.76). Cancellation rates remained low at 15% (2018: 14%). First time buyers accounted for 34% of total sales in 2019 (2018: 34%). Investor sales continued to be at a low level of c.5% (2018: c.5%).

Strong forward orders

We ended 2019 with a record total order book valued at £2,176 million as at 31 December 2019 (31 December 2018: £1,782 million), excluding joint ventures, which represents 9,725 homes (31 December 2018: 8,304 homes). We traded from an average of 250 outlets in 2019 (2018: 273) and enter 2020 with 240 outlets (31 December 2018: 256). As previously guided, we expect 2020 outlet numbers to be broadly similar to 2019.

Help to Buy

During 2019, approximately 34% of total sales used the Help to Buy scheme, and we worked with 5,693 households to take the first step to home ownership or to move up the housing ladder (2018: 36% and 5,828). Approximately 76% of sales through Help to Buy in 2019 were to first time buyers (2018: 77%) at an average price of £277k (2018: £270k). During the year 30% of sales in the London market used Help to Buy London (2018: 29%).

We welcome the Government's announcement within the Autumn Budget 2018 to introduce tapering measures to the Help to Buy scheme as the Equity Loan Scheme transitions to a close in 2023. Help to Buy has been popular with our customers and has supported them in getting onto and moving up the housing ladder, however, we believe that the changes announced are appropriate and are in the best long term interests of the housing market and homebuyers.

Industry structural factors

There are a number of structural factors that impact our industry. Structural factors are conditions that have built up over decades and may take many more to resolve, such as the availability of skilled labour (e.g. a UK workforce aligned to other areas such as finance, the service sector, social sciences and public and private sector administration) and a shortage of housing supply (due to growing population, changing UK demographics, years of underinvestment in housing). The land and planning environment has structurally changed this cycle.

The housing market cycle

Despite structural undersupply, which underpins our long term prospects, we continue to view the market as cyclical. Therefore, in our view, it is a question of when, not if, there is a period of market weakness.

It is worth considering what has happened in previous cycles and what has changed since then.

UK house prices rose by 34% and 74% in the four years leading up to the 1990 house price crash and the 2008 financial crisis. Over the last four years prices have increased by around 15%, and this year, house price growth has been outstripped by wage inflation, a small positive for affordability.

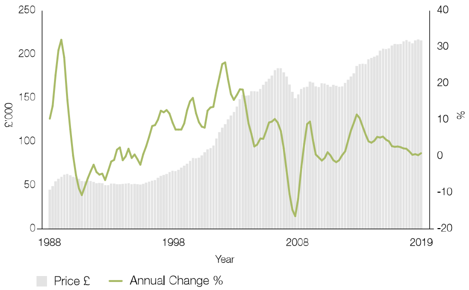
It isn't possible to predict what will happen to price and the extent of any future correction, but it is reasonable to suggest that the last few years have not replicated the 'bubble' characteristics that marked the end of previous cycles.

Changing land environment

UK housebuilders are more than just builders, we invest in land and develop it through a number of planning and regulatory stages. The time from land purchase to sale of completed homes can vary from 1.5 years in the case of short term land, with some form of planning for residential development, to over 10 years in some cases for strategic land, without planning for residential development.

The land backdrop has seen marked changes in this cycle following the introduction of the 2012 National Planning Policy Framework (NPPF). Subsequent updates to NPPF continue to confirm the importance of housing delivery and supply through both the Local Plan process and the five-year land supply balance.

House price inflation



Source: Nationwide.

The land and planning environment is structurally different in this cycle due to a generally good level of housing land availability, and is more balanced and effective today than at any point over the last 30 years. We are confident that, barring a fundamental change in Government policy, this will continue to be the case for the foreseeable future.

Given the strength of the landbank, and in light of the wider political and economic uncertainty, during 2019 we took a precautionary view of land investment and acquired new land on broadly a replacement basis, maintaining our strong locational discipline and focus on strategic land conversion.

More limited availability of land with planning under the old (pre NPPF) framework was a factor in the significant land price inflation, which amplified the impact of previous downturns. This was particularly evident during the housing market crash of the late 1980s and the housing crash during the financial crisis of 2007-2009.

Housing availability

Impacts
- Supply and demand factors
- Rate of housebuilding in industry

Contributing factors
- Availability of labour and materials
- Government intervention / planning backdrop
- Land availability

Medium term expectation
- Shortfall against 300k Government target

Long term factors
- Gradual easing of shortage but long term demand for our product

Land and planning regime

Impacts
- Availability of land
- Planning

Contributing factors
- Time taken for planning decisions
- Cost of planning obligations
- Viability of land

Medium term expectation
- Pressure on: minimum prices, options premium, cost caps
- Increasing focus on one-to-one opportunities through structured site searches
- Councils reporting climate emergency related delays

Long term factors
- Policy dependent
- Continued benign outlook

BM Read more on pages 30 to 31

Regulatory backdrop

Impacts
- Ease of building
- Cost of building

Contributing factors
- Planning environment / reforms
- Health, safety and environment (HSE) and quality requirements

Medium to long term factors
- Changes after consultations on fire safety / access
- Energy, ventilation, electric vehicle charging
- Environmental Bill, including Biodiversity Net Gain
- Further devolution of planning
- Social housing proposals
- National Model Design Code

Labour and materials

Impacts
- Pace of build
- Availability of skilled labour

Contributing factors
- Training our apprentices to offset skills shortage
- UK construction levels
- UK employment levels

Medium term expectation
- Build cost inflation expected to be c.3% this year
- Future years depend on: industry output; EU trade deal; UK immigration policy

Long term factors
- Depends on UK economy
- Dependent on education and industry training

S Read more on pages 36 to 37

PR Read more on pages 48 to 53

Our performance in 2019

Land market

Our short term landbank stands at c.76k plots (2018: c.76k plots), which has been sourced using strict criteria, including location quality. 54% of this short term landbank has been strategically sourced (2018: 51%), since 2009.

We currently have c.4.8 years of land supply at current completion levels in towns, villages and cities where customers aspire to live. During 2019 we acquired 7,268 plots (2018: 8,841 plots).

The average cost of land as a proportion of average selling price within the short term owned landbank remains low at 14.9% (2018: 15.2%). The average selling price in the short term owned landbank in 2019 increased by 1.4% to £285k (2018: £281k).

A key strength of Taylor Wimpey is our strategic land pipeline. This is an important input to the short term landbank and provides an enhanced supply of land with greater control over the planning permissions we receive. We have one of the largest strategic pipelines in the sector which stood at a record of c.140k potential plots as at 31 December 2019 (31 December 2018: c.127k potential plots). During 2019, we converted a further c.8k plots from the strategic pipeline to the short term landbank (2018: c.8k plots). We continue to seek new opportunities and added a net 21.2k new potential plots to the strategic pipeline in 2019 (2018: 17.8k). In the year, 56% of our completions were sourced from the strategic pipeline (2018: 58%).

Build cost

Build cost inflation in 2019 was c.4.5% (2018: 3.5%). As stated in November 2019, since the final quarter of 2019 we have seen a softening in the cost pressures experienced earlier in 2019. At this stage, we anticipate lower overall build cost inflation in 2020, though this is dependent on industry-wide production levels as well as house price inflation and expect build cost inflation of around 3%.

Current trading to February 2020

We have made a positive start to 2020 coming into the spring selling season and, with a clearer political outlook, customer confidence has improved. The net private sales rate for the year to date (w/e 23 February 2020) was 0.97 (2019: 0.99). The underlying net private sales rate for the year to date, and the equivalent period, excluding bulk deals, was 0.92 (2019: 0.90). To date we have achieved selling price growth of c.1.5% against budget. As at 23 February 2020, we were c.49% forward sold for private completions for 2020 (2019: 47%), with a total order book value of £2,606 million (2019: £2,170 million), excluding joint ventures. This order book represents 10,901 homes (2019: 9,622). In Central London c.84% of private completions for 2020 are forward sold, as at 23 February 2020 (2019: c.50%).

Outlook

Short term

The easing in build cost pressures seen in late 2019 has been maintained, and we expect build cost inflation in 2020 to be around 3%. We are focused on reducing underlying costs to mitigate future build cost inflation. This very clear focus on cost, simplification and value has been well received by the business, with employees engaged at every level. Volumes for 2020 are expected to be slightly lower and we will be targeting a slightly lower sales rate as we focus on capturing value. We aim to maintain 2020 operating profit margin broadly in line with 2019. Operating profit margin in the first half of the year will show pressure from 2019 build cost inflation and selling prices and long term investment in quality and business improvement, with margin improvement expected in the second half as cost initiatives improve performance. Margin remains a key priority for the Group and we have reconfirmed our medium term target to deliver operating profit margins of c.21-22%, assuming market conditions remain stable.

During a period of wider macro-economic uncertainty, the new build market has proved to be resilient and house prices have remained stable. We remain supportive of Government plans to introduce an independent ombudsman service to the new build sector to provide impartial rulings on unresolved customer issues and to help raise standards in the wider industry.

Whilst we recognise that the ongoing trade discussions with the European Union may create some volatility in sentiment in the housing market in the near term, we see the clearer political outlook as providing a longer period of stability for our customers. We are mindful of the changing regulatory environment for the sector in the short to medium term and will continue to monitor this closely to ensure we are able to respond.

In line with our strategy, as we continue to build a sustainable advantage, we remain committed to investment in areas that will drive long term benefits and future value for customers and investors, such as our investment in apprentices, our direct labour recruitment and our strategy for large sites. We are also committed to further strengthening our environmental, social and governance (ESG) strategy and will set out further ambitious targets in key areas such as biodiversity and continuing to reduce our carbon footprint, including developing a science-based carbon reduction target by the end of 2020.

We will continue our focus on cash generation, cost discipline and the financial returns of our business. We returned a record £599.7 million in cash to shareholders in 2019 and have previously announced our intention to return a further c.£610 million this year, subject to shareholder approval.

Medium to longer term

As we look ahead, we see the removal of Help to Buy as a continued risk, but having had visibility of, and time to plan for the changes, we consider it as one that can be managed.

Whilst it is difficult to predict the longer term outlook, there will continue to be strong demand for the homes we provide, given it is widely recognised there remains a supply and demand imbalance.

Whilst market conditions have improved markedly since the great recession, we still believe we operate in a cyclical market and we must operate prudently to be ready to absorb changes in market conditions that may lead to a price or demand correction or present opportunities to buy land at attractive prices. For this reason, we have built flexibility into our sustainable operating model, underpinned by healthy cash generation and a strong balance sheet.

Read more on pages 12 to 13