Shot in the arm for lending market

Lending outlook
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Throughout the Covid period, Mutual Finance has been active in arranging finance across all real estate sectors, completing £962m of new business during 2020.

In my opinion, financing assets will become more difficult, more expensive and more selective.

Margins will be increased, loan-to-value ratios will reduce and certain sectors such as retail, leisure and hospitality will become exceptionally difficult to find suitors for. That being said, there is no shortage of liquidity in the lending market, and we are finding more and more new-to-market lenders, while the existing spread of banks, insurance companies, platforms and family offices are all willing to lend, albeit on slightly reduced and more cautious terms.

Today, we are not witnessing many casualties among borrowers, with lenders taking an exceptionally sympathetic view of the predicament of non-paying tenants and agreeing strategies to work with borrowers through this period.

We do however question whether this 'good-natured' approach is fuelled by genuine bank policy or the government directive not to enforce action against borrowers during the pandemic. We note that particularly the retail and hospitality sectors have received significant protection.

However, we do not expect this situation and sympathy to last beyond the period allowed to protect borrowers and tenants.

Once the shackles are off, we fully anticipate a surge in tenant failure and then a domino effect with lenders beginning to take action against borrowers.

Traditionally, we have found that experienced borrowers with deep pockets fare best in these situations. Lenders see that they know what they are doing and with monetary means can navigate through most problems with reletting, repositioning assets and working with tenants to find solutions. In contrast, borrowers that lack the knowledge of previous dips in the market learn the hard way.

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We anticipate that as we approach Q2 in spring 2022, we will begin to see significantly more opportunities in the marketplace, as lenders begin to enforce covenants and start calling for revaluations to be completed.

The lack of sales and lettings will give valuers very little evidence to seek comparable transactions and therefore valuations will inevitably be driven down and provide an exceptionally cautious approach to valuation. The surveying community have my utmost sympathy in this regard as they are being asked to value in the dark. The outcome will be that valuation covenants are breached and that borrowers will be placed in a position where they either 'cure' the situation with cash, or work with lenders in a default scenario.

Residential resilience

The resilience of the residential sector has been noteworthy throughout the pandemic. Anecdotal evidence from my residential development clients has been positive with feedback that sales are strong, demand is there and purchasers are keen to take new product.

Sales up to the £500/sq ft range have been particularly robust, with the 'affordable' pinch point in the market being most buoyant.

Moving up the scale to the sub-£1,000/sq ft range, even at this level we have seen some effect, yet this executive sector is also coping well. At £2,000/sq ft and above in the prime locations, there has been a drop-off.

Defying the general lending scepticism, residential development finance is actually increasing in the lending market. We are witnessing more and more lenders adding this product to their bow alongside new lenders entering the marketplace. Insurance companies, lending platforms and family offices are all now making strides to deploy money into this sector.

The lending parameters are loosening here and greater loan-to-cost ratios of 80% to 90% are available. It would appear that bigger development schemes of £100m-plus will have a significantly larger lender market to pick from going forward, with new entrants seeking to fill this space.

So, we need to sit back and wait – things are OK at the moment and while we do not expect a 'bloodbath' going forward, I do think that opportunities in the market will start to arise over the next 12 months.

Purchasers should keep their powder dry in anticipation of this prospect. Things could have been significantly worse, and I believe that the property market should be applauded for its composed, calm and united attitude towards the pandemic.

Like the successful national vaccination programme, the lending market has had a shot in the arm that will leave it healthy for a long time to come.

Raed Hanna is managing director of Mutual Finance