RESIDENTIAL RESEARCH

RESIDENTIAL DEVELOPMENT FINANCE SURVEY

RISK APPETITE GROWS AMONG RESIDENTIAL DEVELOPMENT LENDERS

The relative health of the UK economy and rising competition mean residential development lenders are, within reason, embracing more risk.

Results for Q3 2014

Some 43% of respondents provide mezzanine lending, **up from 20% last year**

Some 36% of respondents have reduced pricing as a result of increased competition from other types of lender

Some 83% will consider schemes in zone 1 of central London while 89% will consider zone 2 and beyond, which represents a drop from last year

Respondents that would consider a scheme with planning risks increased **to 60% from 50% in 2013**

More lenders consider UK regions with **34% saying they would lend to a scheme in the north versus 21% last year**

TOM BILL
Head of London Residential Research

"The findings of Knight Frank's latest survey marks another step on the return to a more liquid lending environment following the financial crisis"

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Lenders to residential developers in the UK are taking on more risk as property markets stabilise after the financial crash, a survey of more than 50 major institutions has found.

The respondents, which include a mix of banks, institutional investors and private equity funds, are increasingly funding schemes outside London, plan to grow their loan books over the next year and are more open to planning risks and higher loan-to-value lending.

The findings of Knight Frank's latest survey mark another another step on the return to a more liquid lending environment following the financial crisis, when banks retreated from the sector.

The UK economy is tentatively returning to health and the prospect of a normalised interest rate environment. In September, the Office for National Statistics said the country's economy was 2.7% larger in the second quarter of the year compared to its pre-crisis peak.

This was reflected in the number of lenders who intend to grow their loan books over the next year, with the figure rising to 78% in Q3 2014 against 75% in Q3 2013. Furthermore, the amount of respondents that would consider a scheme with planning risk increased to 60% from 50% last year.

However, there is no sign banks are returning to the years of higher risk lending that preceded the financial crash and they are joined by other lenders including hedge funds and other institutions that are attracted by relatively high returns in a world of low-yielding assets.

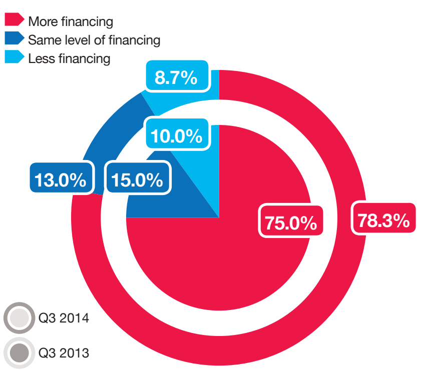
This increased competition has forced down the cost of debt, as figure 4 shows. Some 36% of respondents said they had reduced their pricing as a result of this increased competition while more than a quarter said they were prepared to take on more planning risk or boost the loan to gross development value ratio.

The sustainability of house price inflation is a concern for lenders, particularly in London, despite recent signs of moderation.

Some 83% said they would consider schemes in zone 1 of London while 89% said they would consider zone 2 and beyond. That compares to 97% who would consider schemes in any part of London last year.

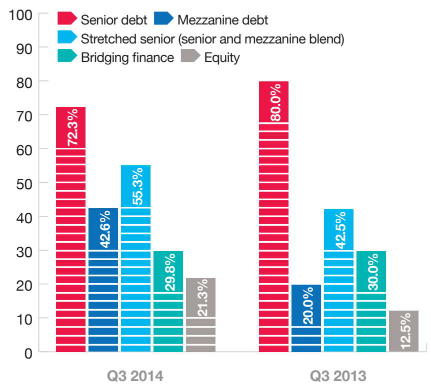
Meanwhile, appetite has grown for lending in the UK regions, where the recovery has been patchier. Some 38% said they would consider lending to a scheme in the Midlands in the next 12 months, while the figure was 34% for the north of England. That compares to 28% and 21% respectively last year.

FIGURE 1
Lenders plan to grow their loan books
How do you expect your business to develop over next 12 months?



Source: Knight Frank Residential Research

FIGURE 2
...and embrace higher-risk lending
What type of finance do you provide?



Source: Knight Frank Residential Research

RESIDENTIAL DEVELOPMENT FINANCE SURVEY Q3 2014

FIGURE 3

Venturing beyond London

Which locations in the UK will you consider for residential development financing in the next 12 months?

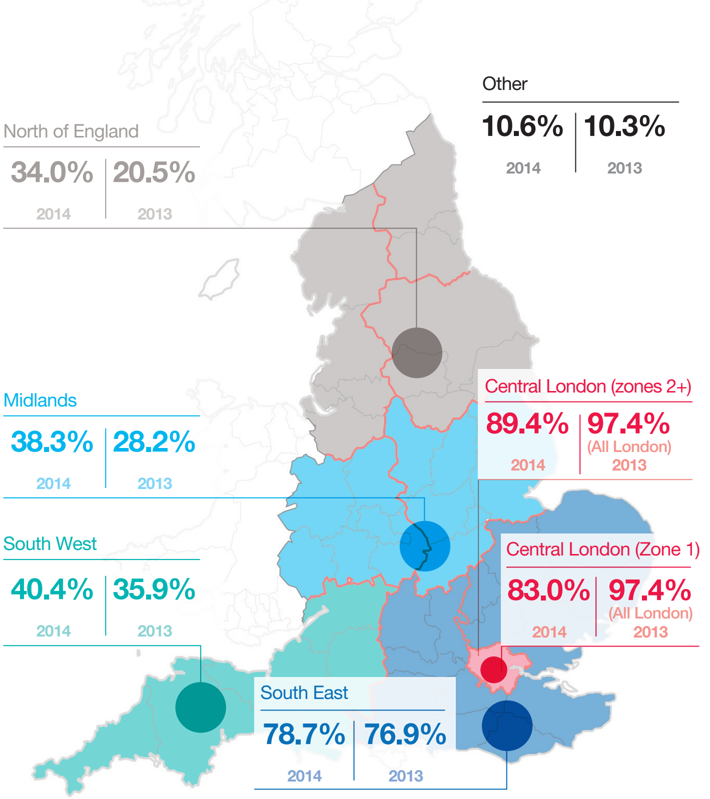


FIGURE 4

The falling cost of finance

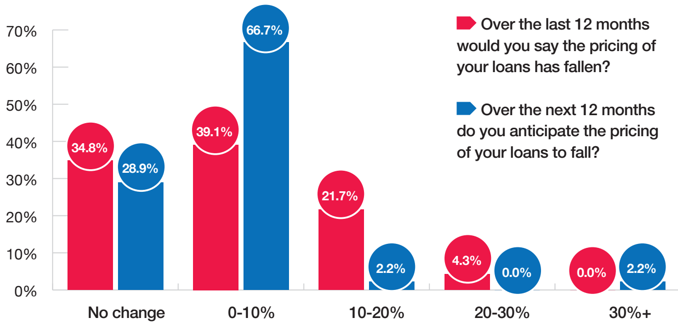


FIGURE 5

Lenders adapt as competition grows

With the increase in competition from lenders to fund sites, how have you changed your strategy to compete? (Multiple answers)

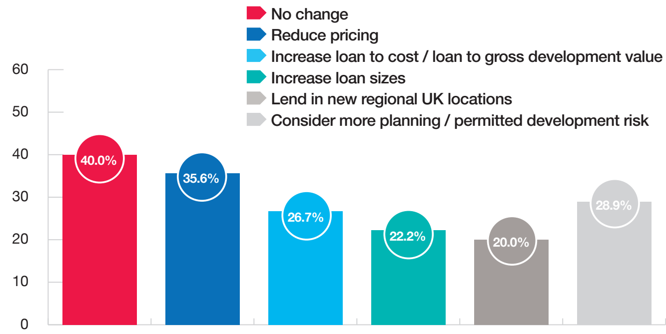


FIGURE 6

A growing appetite to lend versus other sectors

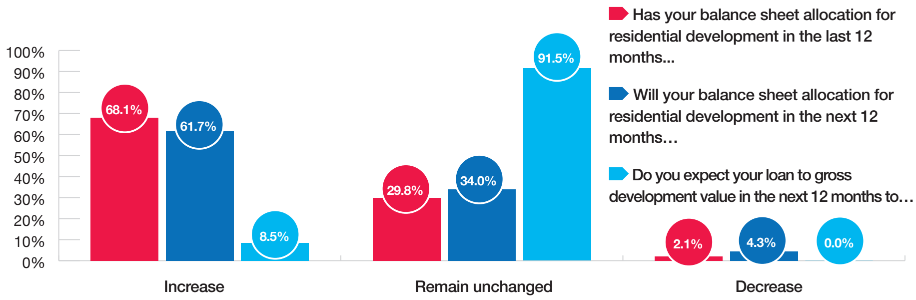


FIGURE 7

Location is still key

What is the biggest risk when underwriting a development loan?

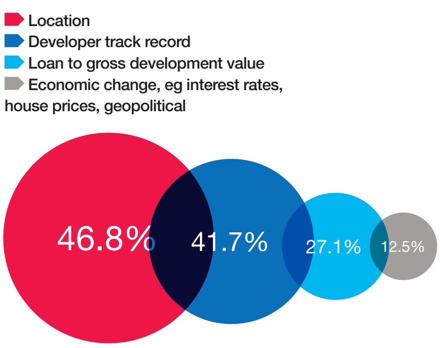
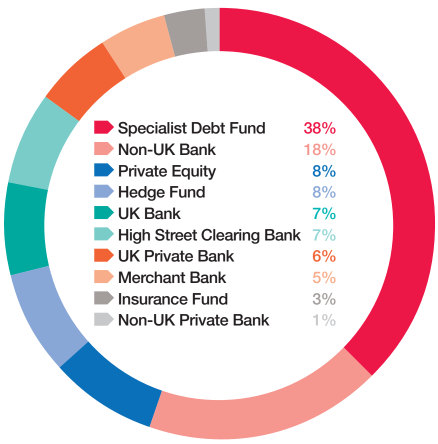


FIGURE 8

The survey respondents



SURVEY RESPONSES WERE COLLECTED BETWEEN JUNE AND AUGUST 2014

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