LEXI®

REACT news

EXPERT REACTION RESIDENTIALUK & IRELAND

We must empower smaller developers to tackle the shortage of rental homes

21 Oct 2021 | by Nick Holding-Parsons

If we truly want to boost rental supply, we need to widen access to finance options

Nick Holding-Parsons GUEST WRITER Nick Holding-Parsons is co-founder of Lexi Finance

Over the past 18 months, the UK build-to-rent industry has grown exponentially, with a wall of institutional capital flooding into the market. Big names you'd expect to see such as Legal & General, Grainger, Macquarie and now Lloyds have been joined by less likely entrants such as John Lewis, who are reportedly looking at their entire retail portfolio as a build-to-rent opportunity.

With the promise of long-term income and rising demand for rental homes, it is not hard to see why many more are keen to enter the market. Savills data shows a record year of investment into build-to-rent in 2020 of £3.5bn and over £2.2bn so far in 2021.

But to tackle the endemic imbalance between the supply and demand of homes, plots of land of all sizes – not just those that entice the institutional players – must be unlocked. This is where small to mid-size developers come in.

Making financing more efficient

Until fairly recently, anyone other than household names would have struggled to obtain competitive finance for build-to-rent schemes. However, an increased number of lenders have entered the market this year as build-to-rent becomes an established asset in the UK property market.

Though this is a step in the right direction, there is still a huge disparity between the finance options available to the larger and smaller players in the build-to-rent space.

Large build-to-rent developers borrowing £50m or more per transaction can access facilities where the one loan covers the three phases of development, stabilisation and investment, with the interest rate ratcheting down according to the phase of the cycle (and the associated decreasing risk).

“There is still a huge disparity between the finance options available to larger and smaller players”

Smaller build-to-rent developers with a similar risk profile don’t easily have access to this type of product, despite there being a clear demand for it.

These operators tend to need to use one lender for development finance, another for the investment phase, and occasionally a third to bridge the stabilisation period in between. These refinances mean a higher cost of borrowing; add time delays; increase uncertainty; and can ultimately break the viability of a project.

To boost SME housebuilders producing build-to-rent assets, especially in secondary and tertiary towns, efficient financing through one loan covering all stages needs to be more readily available. If we are to start truly boosting rental supply in this country, SME developers must also be catered for in a similar fashion to the institutional players.

"Smaller developers can deliver schemes quickly, gradually boosting local capacity and supply"

Developers focused on sites with 150 or fewer units deliver schemes in towns and locations the institutions won't touch. They can also develop these smaller schemes quickly, gradually boosting local capacity and supply. They don't tend to suffer the same issues as larger schemes, which either need to be phased or risk over saturation in one area.

Many lenders are keen to support these smaller developments but will require a developer to switch between products or internal funding lines, rather than offering a bespoke funding package to cover the asset's cycle from the start. This creates uncertainty, higher pricing and increases risk.

Levelling up in action

An added benefit to funding partners is that these smaller build-to-rent schemes, often 150 units or less, tend to stabilise quickly and don't tend to suffer from the same issues as larger schemes that can flood markets and take longer to reach full occupancy. They also tend to be built with the potential sales of individual dwellings in mind, meaning there is a ready alternative business plan.

At a time of rising inflation and material shortages, it is vital that those in the SME build-to-rent space have sufficient access to cheaper capital to tackle the ongoing shortage of quality rental spaces.

Often when the phrase 'levelling up' is used it is not clear what it means. However, in the build-to-rent space, it is clear. To level up, the market needs to provide a wider range of more competitive funding options and empower smaller developers to help tackle the shortage of rental homes.

Read the article here.

LEXI Finance
151 Wardour St,
London, W1F 8WE

T. +44 (0)2081 383 284
E. hello@lexifinance.com