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Property Week

LEXI's Sam Le Pard on why 'crazy' proposals for property finance aren't so crazy anymore

By Sam Le Pard Wed 4 January 2023

There will always be genuinely crazy proposals for property finance, and there will also be those proposals that initially seem crazy simply because they are unusual.

While a solar-powered crypto mining farm could realistically tick either box, specialist lenders are increasingly becoming open to giving a wider range of real estate projects the green light, or at least careful consideration. Last year's crazy is next year's maybe. A hard 'no' because the client lacks credibility or experience makes sense. A 'no' because the asset is unusual, the exit or income is complex or there is misunderstanding of risk mitigants could be a missed opportunity for everyone; borrower, broker and bank.

Last year, unusual projects broadened further. As well as that crypto mining operation, we had proposals for a commercial mausoleum, a retirement living concept in Spain, a network of multi-storey EV charging car parks and a microfilm studio.

So, why the shift towards these more eye-catching projects?

First, the real estate finance space is fiercely competitive. To deploy cash, lenders with a higher cost of capital are used to taking the time to consider alternative asset classes and less mainstream business plans.

The fragmentation of the funding market and the movement of private equity money into direct lending has also prompted an incremental change in mindset.

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Private equity houses are often hunting for higher returns and the next hot alternative asset class. So it's no surprise that this mindset and a willingness to listen to alternative proposals have influenced the debt teams that they sit alongside.

Second, while there is no shortage of aspiring property developers, there is a dearth of cheap land and a lack of viable planning consents. Combine this with increasing costs of materials and debt, and developers are branching away from the mainstream and into alternatives.

Some are considering alternative methods of construction to find their delta, while others look to alternative real estate classes. Here, they often find less competition, higher profit margins and more amenable planning departments far more likely to support projects that bring new jobs, have an environmental twist, or protect the vulnerable.

Potential returns on leftfield projects can also be much higher, especially if the asset class yield compresses over time or as greater scale is achieved.

It has always been the case that barriers to entry limit competition. The way the industry is evolving also means deals are more streamlined. The market is better advised than it used to be, with a wider class of specialist debt advisers emerging to support more complicated transactions by bringing participants together from the furthest corners of the market and ensuring good, but unusual, business plans are not overlooked.

An alternative project must be thoroughly thought through and researched from the off. There is no space for unmitigated risks, and for an application to be entertained, there needs to be a reversionary base case in mind to pitch to the lender. But ultimately, the value of commercial property is driven by its income, so if the numbers stack up, taking the time to understand a novel proposal could be rewarding for all.

Read the article here.