

The appetite for development finance in uncertain times

Opinions

03.01.23

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Development finance has recently become a popular product offering for many lenders. It is used to support the delivery of a project, such as building or refurbishing a property.

It is significantly different to bridging loans in that bridging finance is a way to either purchase, refinance or raise capital utilising all the funds advanced from the facility.

Funds are secured against an existing tangible asset, land or airspace, whereas development finance is designed to assist with the purchase or refinance, and then subsequent costs of developing a property that's not yet built.

Funds are drip-fed throughout the process of the build and provided to the borrower through multiple 'drawdowns'.

Previously, lenders may not have wanted to move into development finance due to the lack of experience or expertise needed to fully understand and manage the lifecycle of a development loan, or the risks involved.

Developers can and often go over time and budget, which is why it is important to have a deep understanding of the construction process.

To allow for this, lenders will require a quantity surveyor as well as a traditional valuer so that they can appraise the build costs for the project and ensure they are viable for the fulfilment of the scheme.

Moving into development finance also allows lenders to add to their value chain and assist their existing borrowers.

If they offer a [bridging loan](#), they can now offer an exit strategy via development finance. Lenders will have already completed their due diligence on an asset which will provide comfort to the borrower, should the borrower want development finance.

Similarly, the borrower will feel comfortable staying with the same lender when looking for development finance.

While there are more hoops to jump through, and the process of arranging the loan can take a little bit longer than a traditional bridge, this is outweighed by the benefits.

Although borrowers can get a development loan from a bank, they would not benefit from the turnaround time and expertise that a commercially minded lender, such as TAB, would provide. The TAB team has first hand experience overseeing and delivering properly managed schemes.

Development finance can be seen as lower risk lending than bridging finance because lenders' exposure is managed throughout the build process.

Funds provided to the developer are allocated for specific purposes. This is determined by the monitoring surveyor, who signs off before each tranche is drawn down.

The monitoring surveyor will have factored a contingency in the budget which allows for unforeseen costs to be covered.

This monitoring of the project means the lender has a set of eyes and ears on the scheme at all times.

Should there be any disputes then the monitoring surveyor is well positioned to act as a go between to find solutions.

Other concerns might prevent a lender from moving into development finance, namely the rising cost of construction.

This is countered with making advanced due diligence at the outset more of a priority. With larger contingencies and a lower loan to GDV (for example, 60.00%) it is not too risky.

Additionally, with more focus on experienced borrowers with a proven track record and by working with experienced contractors, the risk element is less of an issue.

Something else to remember is that construction and development are important linchpins of the economy, and there is a lack of much needed housing within the UK, making development finance important to the economy.

Developers and builders have different needs – whilst large housing developers will go to banks for their development finance, small to medium builders and developers will go to smaller banks or specialist lenders.

Ultimately, despite concerns about risk and increasing build costs, development finance is a beneficial addition to a lender's service offering.

With the proper due diligence on both the borrower and the asset, and by utilising the services of experienced developers and builders who understand the supply chain, many risks are mitigated before the loan is agreed upon.

While there remains to be a lot of question marks surrounding whether development opportunities are still as lucrative to developers in the current market, we are still seeing plenty of profitable and exciting schemes that we remain keen to support.

The continual development of property across the UK remains necessary, which is why we view development finance as an essential product within our offering and could be one of the key factors as to why so many more lenders are adding it to their product ranges too.

As seen in the press: Bridging Loan Directory

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