

# indebted

to property

## The property funding landscape in Australia has changed dramatically.

We speak to Tim Johansen about the repricing of risk, and what property developers and investors can now expect from the funding markets.

Global and local events have had a profound effect on the property funding markets in Australia. There is less money available for property investment and development funding, and what money is available is now more expensive.

This contrasts with the experience of the past five years, when the real property and funding markets were intensely competitive as financiers, developers and investors fought for market share, bid up asset prices and bid down the cost of funds. Liquidity was abundant and funding was easy to come by.

Investec's Head of Property Investment Banking, Tim Johansen, says that it was common for financiers to misprice risk for the sake of growth in their businesses and to maintain market share.



Tim Johansen is head of Investec's Property Investment Banking.



The fallout in credit markets has put an end to easy money. The mispricing of risk has now disappeared from funding markets – as has excessive liquidity. The collapse of the sub-prime market in the United States and subsequent contraction of the debt and capital markets internationally have starved banks, non-bank lenders, funds and trusts of liquidity to fuel their lending activities.

Tim says Australia is caught up in this global funding shortage, making it difficult for the funding markets to maintain the levels of lending activity to which they have become accustomed. Banks are passing the increased cost of debt to borrowers, and the non-bank sector's ability to lend is significantly constrained by a lack of access to wholesale and retail deposit bases.

"Those that are able to raise funds are doing so at costs much greater than 12 months ago," says Tim.

Institutional funds, trusts and listed developers are also finding it harder to raise equity. The equity markets have deteriorated and the impact of liquidity on real property asset prices are yet to play out.

While it is clear that credible players in the real property market have accepted that risk will be repriced, what remains unclear is by how much, or how quickly, given the limited number of completed transactions in the past couple of quarters.

In Australia, the collapse of a number of high-profile property and financial services companies has brought clearly into focus the mismatch between long-dated property assets and short-dated funding lines.

## The new landscape

Participants in the property market are changing their criteria for doing business. Financiers are more intent on dealing with experienced counterparties who have a solid track record in their sector; and the counterparties are finding their sources of funding are becoming more limited.

Some changes taking place in the funding markets include:

- banks have slowed their lending and have tightened their lending criteria. Gearing limits are lower, and banks are only lending to existing or well-known quality clients,
- institutional first-mortgage funds have, in most cases, stopped lending and have wound back their books to enhance liquidity and to accommodate the increased rate of investor redemptions and lower subscription levels,
- property/financial services companies and second-mortgage funds are finding that poor lending and investment practices have led to asset sales (property and loan receivables), asset value write-downs, freezing of redemptions, share price collapses and trading suspensions, and
- investment banks, including Investec, have adopted a realistic approach to business; they continue to manage existing exposures and support current clients and quality target clients.

## Emerging opportunities

The structural re-rating of property risk in Australia presents greater opportunities for those with liquidity than has been the case over the previous five years.

Tim says that Investec is well-positioned to have its clients benefit from current market conditions by maintaining its core senior and mezzanine lending businesses, and by taking selective opportunistic positions in property and loan transactions.

"Managing risk through the current cycle remains a priority for us," says Tim, "and ultimately, the next milestone in property markets will be marked by the willingness of property developers and investors to accept the repricing of risk."

“ “ The thinning-out of participants in the market will see risk being assessed with  
**much more rigour**  
and this will assist a self-regulation process across the market. ” ”