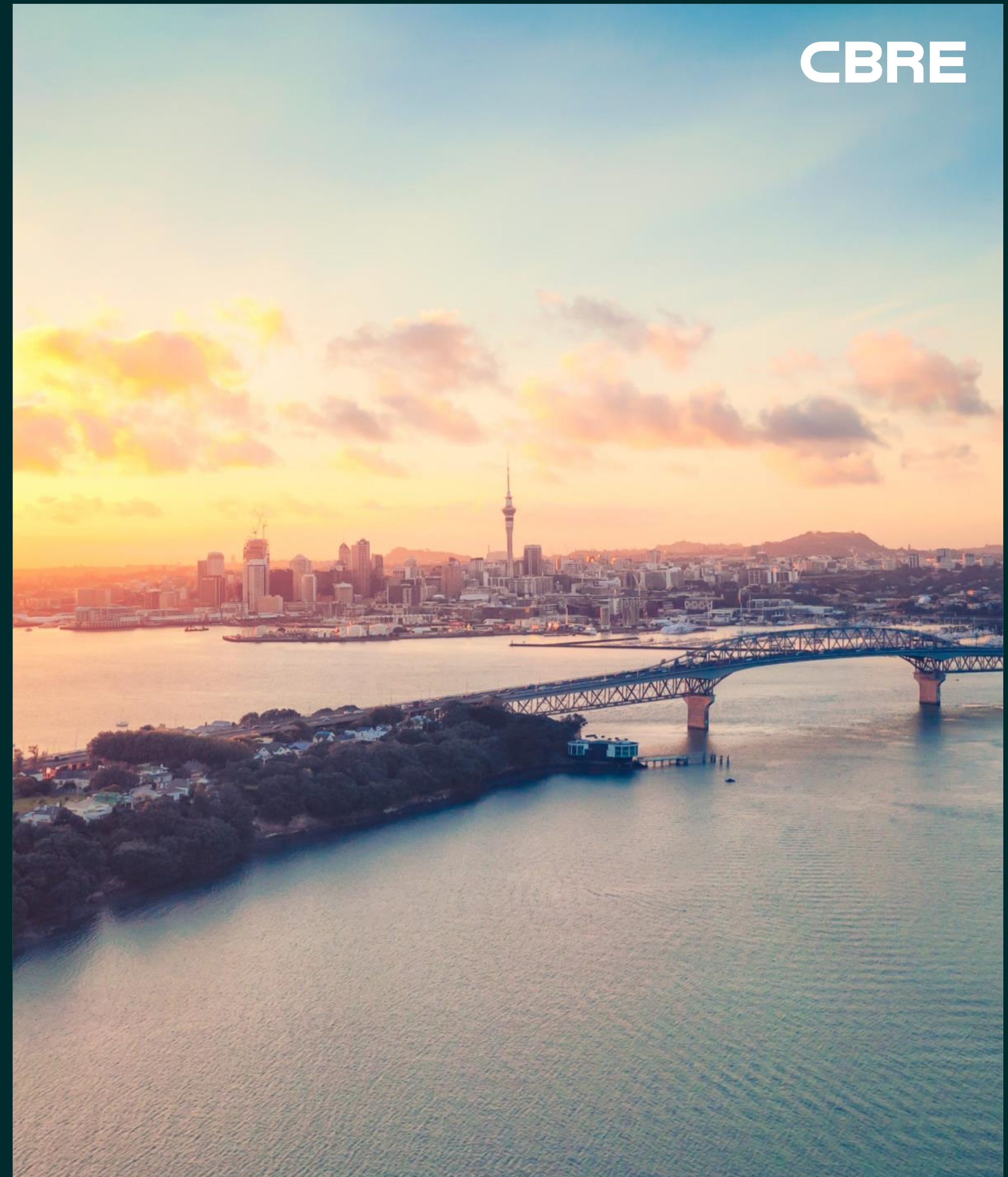
Intelligent Investment

New Zealand Lender Sentiment Survey Q3 2022

LOCAL RESPONSE
NEW ZEALAND

CBRE RESEARCH
SEPTEMBER 2022



Lenders are open to business... but at a higher cost

CBRE Research conducted a survey of 16 lenders to the New Zealand commercial real estate sector. The lenders comprised a mix of banks and non-banks, both local and international. We anticipate repeating this survey on a regular basis.

The survey highlights the following key messages:

- More than twice as many lenders want to grow their loan book as those wanting to shrink but appetite is lower for construction compared to investment lending.
- Lenders are most overweight in build to sell residential and most underweight in industrial.
- Industrial is the most preferred sector for both construction and investment lending. This is true for even non bank lenders that typically focus on the residential sector.
- However, non bank lenders continue to seek exposure to residential construction loans with terrace houses and land subdivision being the preferred form over apartments.
- Influenced by higher risk margins and lower liquidity for some lenders, the cost of debt is expected to increase with three quarters of lenders indicating moving to higher margins.

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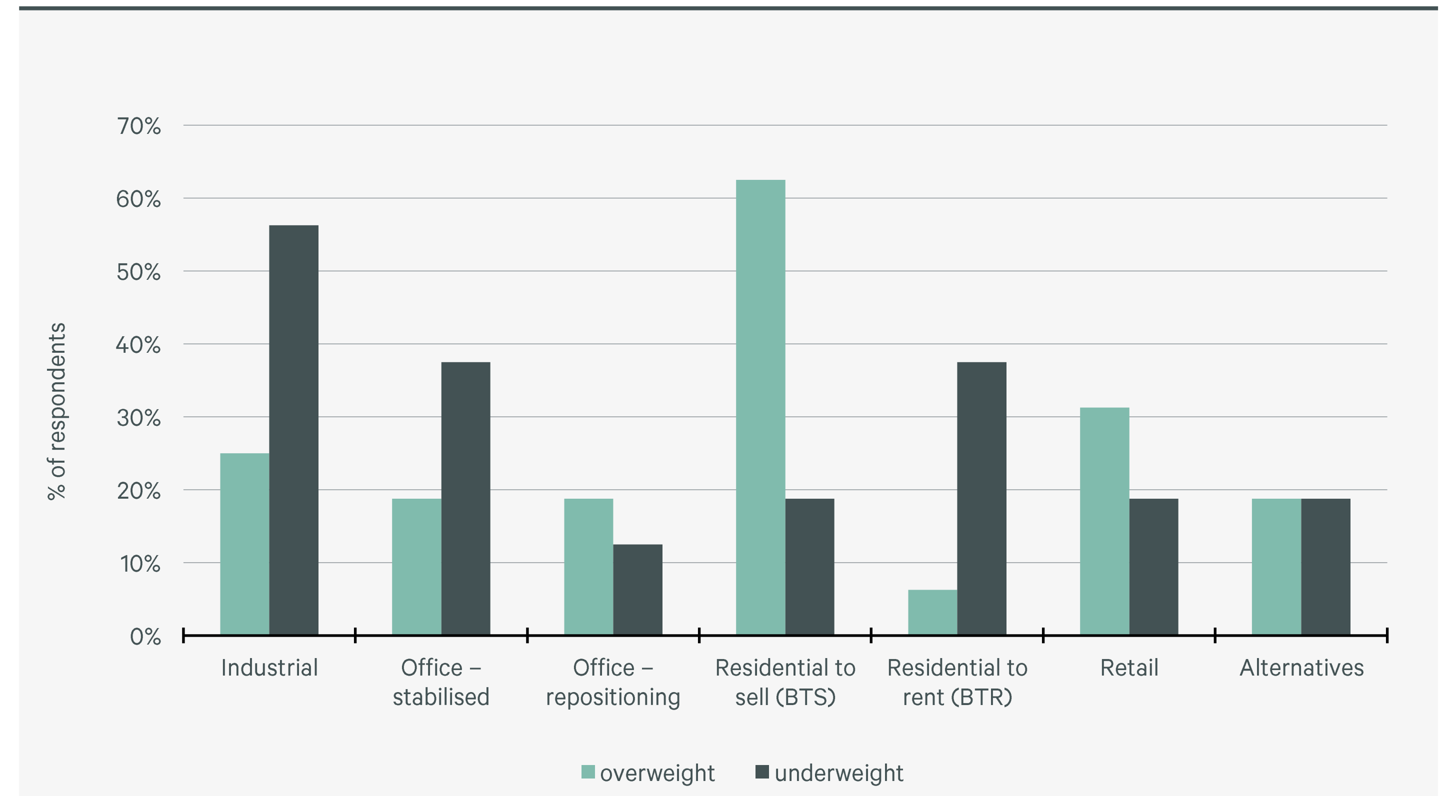
Lenders view their books as being most overweight Residential to sell and Retail and most underweight Residential to rent (BTR) and Industrial.

Non bank lenders, both domestic and international, principally see their current loan books as being overweight in the residential to sell and alternatives sectors and underweight in industrial.

International bank lenders are generally overweight in industrial and residential to sell, domestic banks in office and retail. However an equal number of domestic banks also report being underweight in office indicating a lack of clearly differentiated industry wide exposure to the sector. In contrast, international banks are nearly unanimous in their view of being underweight in BTR.

In our view these trends reflect lenders' strategies. Non bank lenders (seeking higher investor returns) generally have a stronger focus towards development/construction lending and within these residential BTS being the dominant area of activity. In contrast, bank lenders spread their weightings further, across development and investment lending, in all traditional commercial property sectors.

FIGURE 1: Current overweight/underweight investment lending exposures (choose top two)



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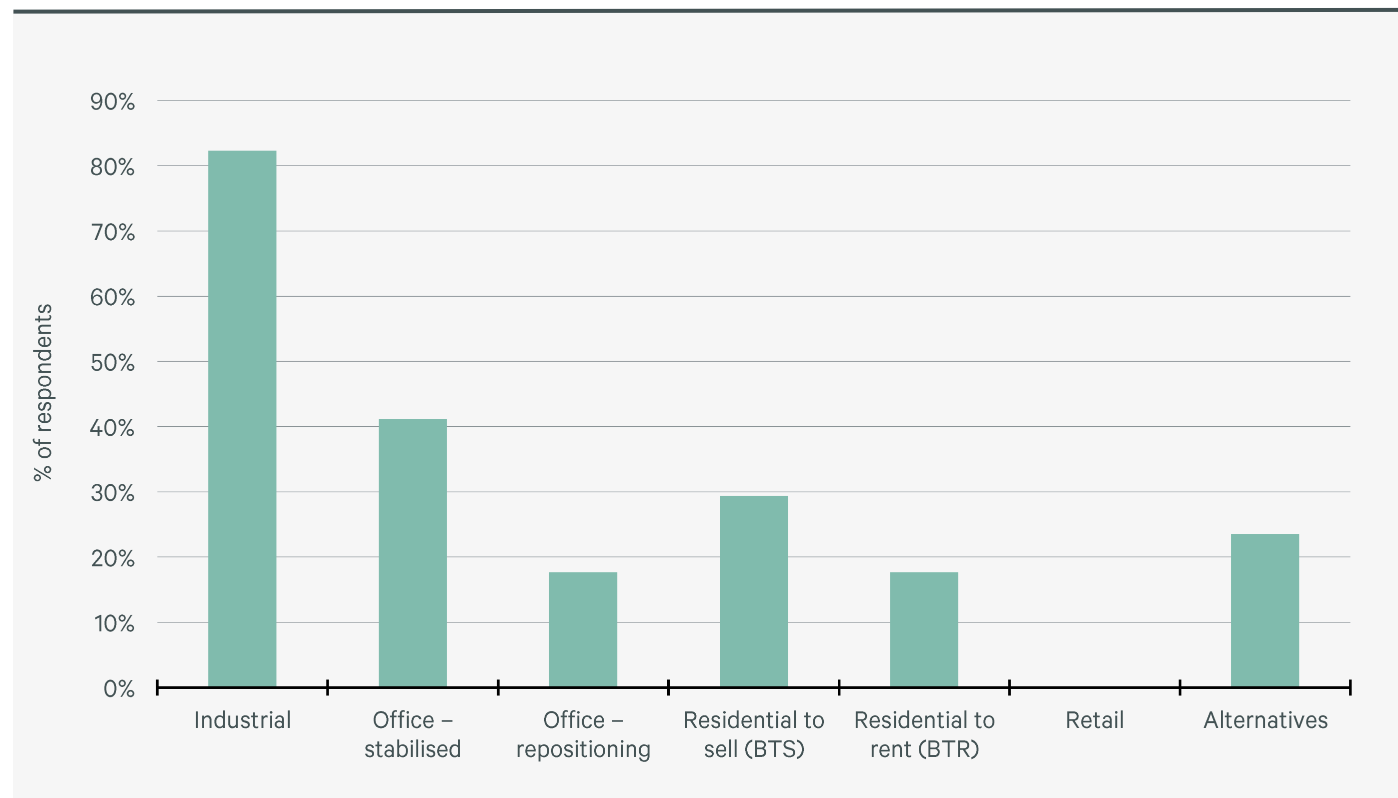
Lenders are eager to grow their exposure to Industrial, Stabilized Office, and BTS

Non bank lenders show strong interest in the industrial sector in which their current exposure is weak but also seeking greater exposure to office repositioning (value add and repurposing) and residential; mainly for built to sell.

Industrial is also preferred by all bank lenders with international banks also showing a strong preference for stabilised office.

Retail currently appears to be shunned by all lender categories and the appetite for BTR also appears limited. This however needs to be interpreted in the context of the questionnaire which asked lenders their top two asset class preferences. As such, even though retail assets are generally not highly preferred, this does not mean that they won't be lent against for the right asset and/or investor.

FIGURE 2: Preferred asset class for new investment (choose top two)



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The cost of debt is expected to increase with three quarters of lenders indicating moving to higher margins. This is likely to be influenced by higher risk margins and may also reflect lower liquidity for some lenders. While the view on margins is largely unanimous between domestic and international, and bank and non bank lenders, LVR and hedging requirements vary by lender type.

International banks are the only ones with hedging requirements in the 55% to 75% category, with domestic banks more often in the 25% to 45% range. Reflecting their lending strategy and loan books, non bank lenders operate in the 0-25% range typically.

The LVR capacity of non bank lenders tends to be 60% and above for both domestic and international. The current LVR requirements of international banks are typically slightly higher than for domestic banks.

FIGURE 3: **In the next three months, credit margins on new loans are likely to move:**

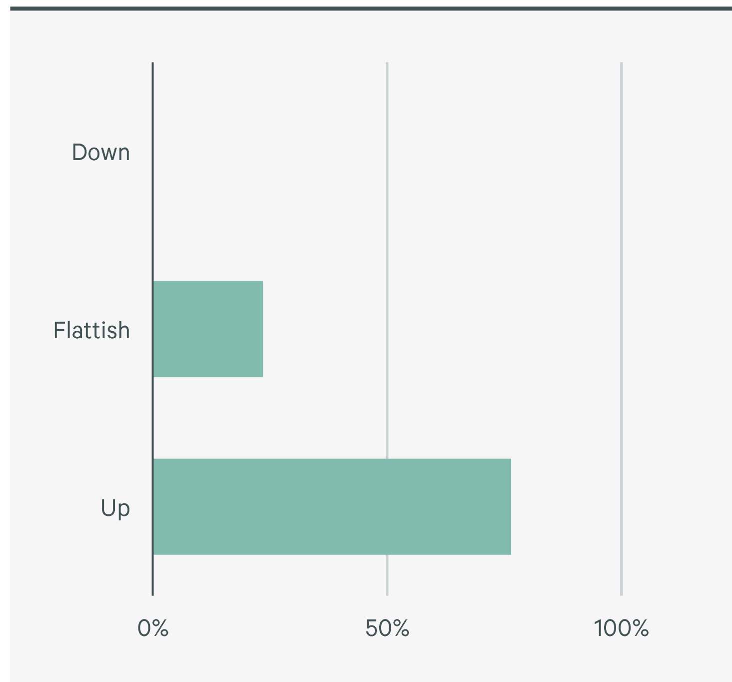


FIGURE 4: **Current LVR requirement**

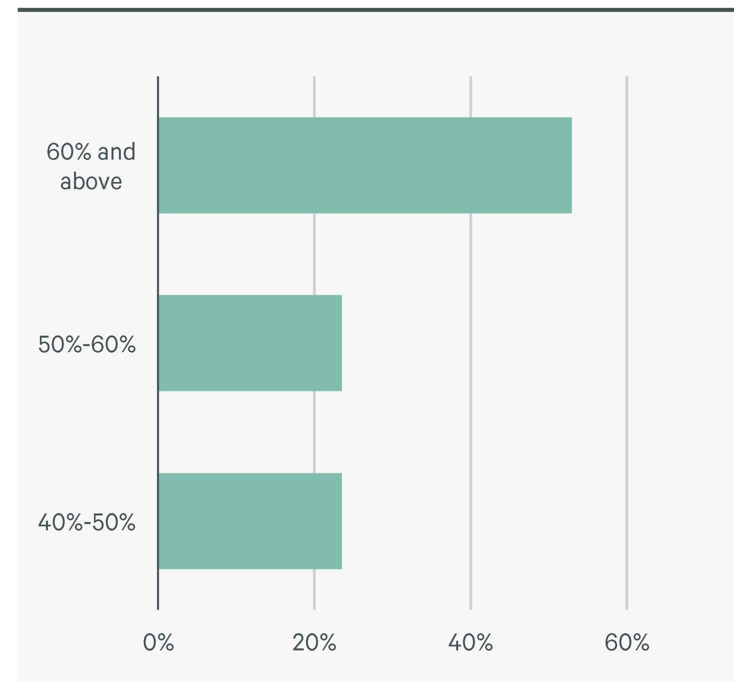
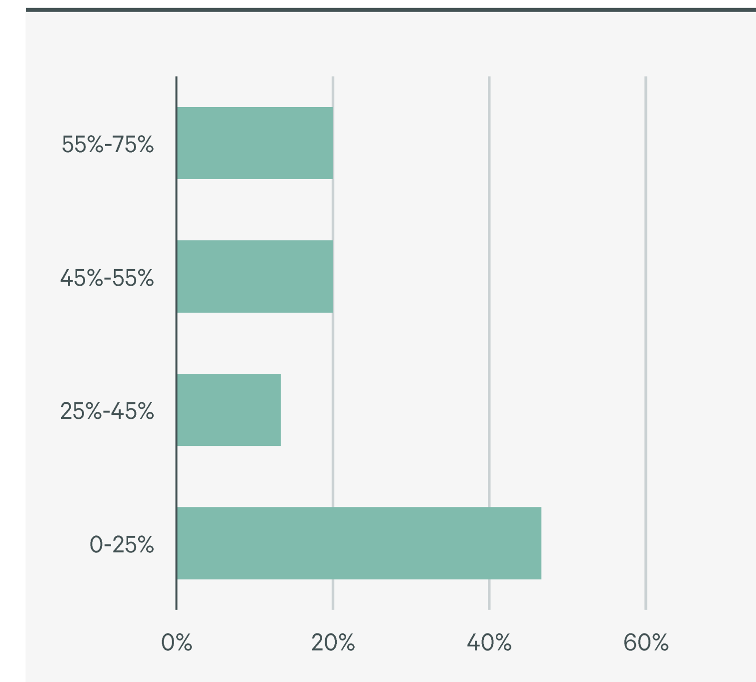


FIGURE 5: **Current interest rate hedging requirement**



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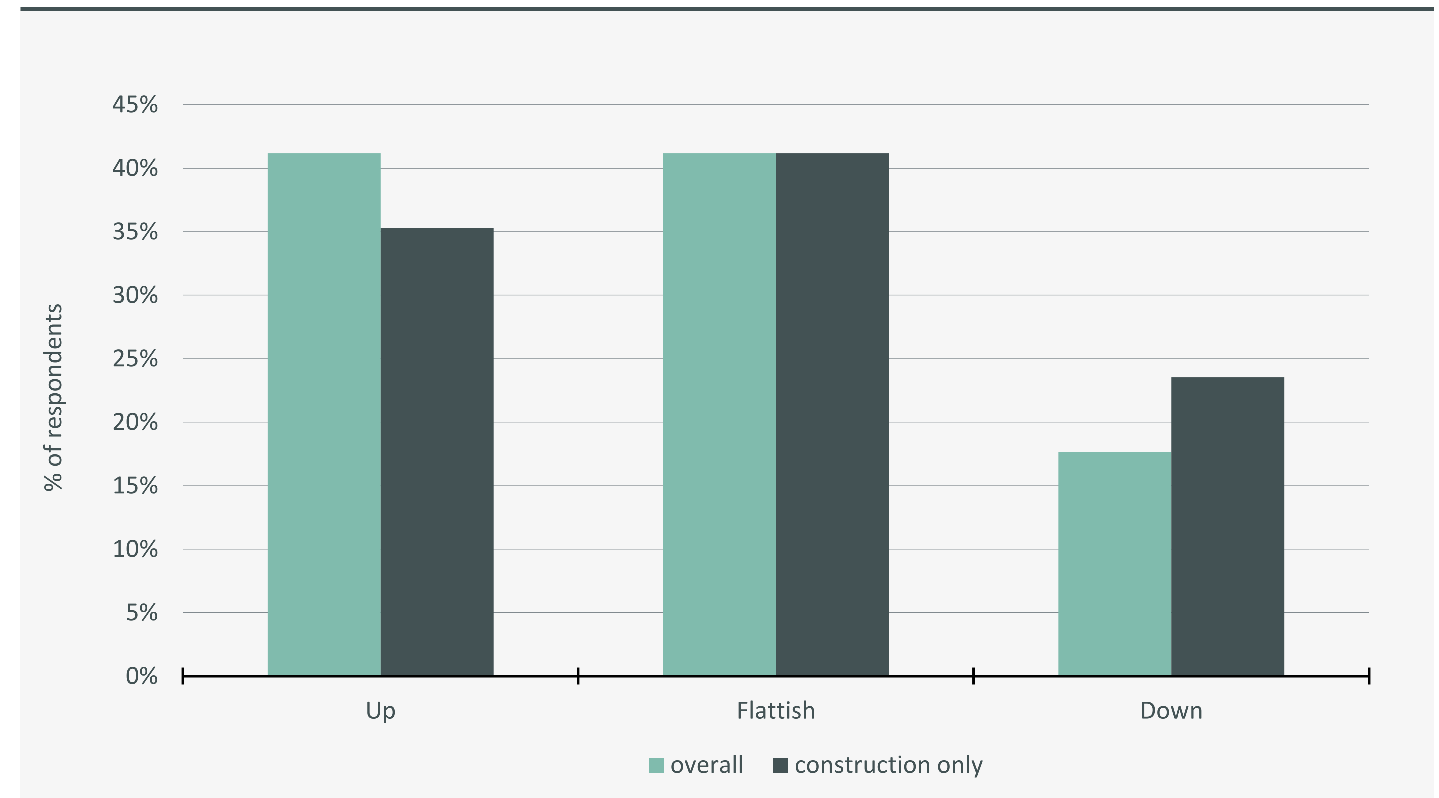
Lending appetite is stable to rising although less positive for construction loans than for investment

Lending appetite is evenly split between stable to growing with the most positive intentions from the domestic non banking sector.

There is somewhat lower appetite for construction lending with a strong distinction between domestic banks who see their appetite remain stable, international banks who see their appetite reduce, and domestic non bank lenders who see increasing appetites.

FIGURE 6: Appetite for new loans



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Construction lending preference highest for industrial

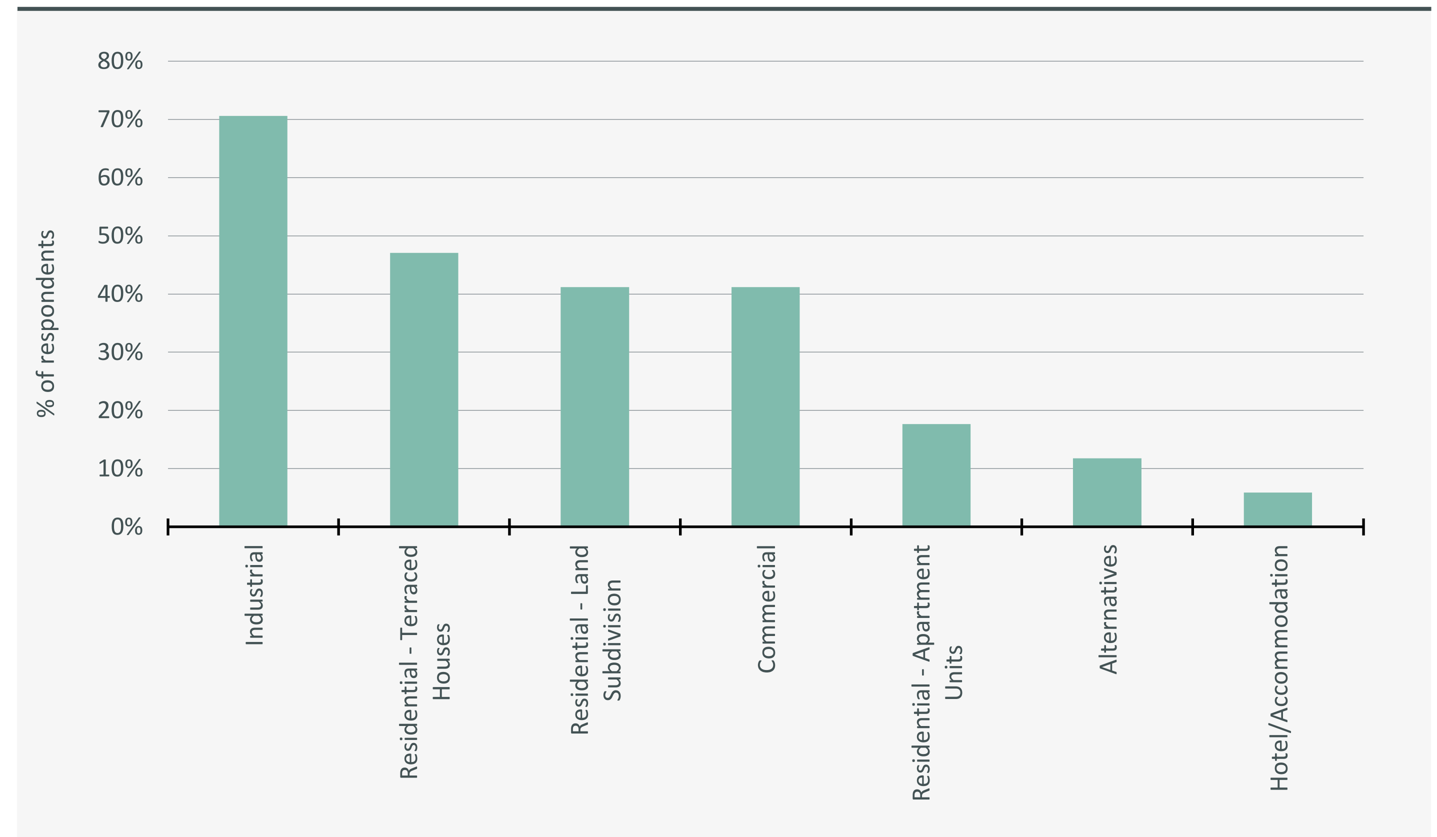
Construction lending preferences closely align with supply demand dynamics across the property sectors, and their perceived market risks.

As such industrial, the market sector which currently provides the heathiest market fundamentals, is a preferred asset class by more than 70% of lenders. It is notable that several non bank lenders, whose focus is generally on residential development or subdivision lending, are seeking exposure to industrial development lending.

For residential lending there are clear distinctions between dwelling typologies especially when it comes to lending appetites between terraces (47% of lenders choosing this as one of their top two preferred asset classes for construction lending) and apartments (cited by 18% of lenders as one of their top two).

Local banks have a fairly low appetite for residential construction lending but the other lenders continue to seek exposure with terrace houses and land subdivision being the preferred form over apartments.

FIGURE 7: Preferred asset class for new construction lending (choose top two)



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Credit metrics continue to increase for residential construction lending

As the challenge of attracting residential presales grows, lenders are seeking higher entry metrics before committing their capital. This was the case from all our respondents with local banks requiring the highest level, all requiring 100% of debt covered. Non bank lenders have increased their requirements, only a small number of respondents remain comfortable with sub-50% cover.

Generally, non bank lenders were now seeking 50% cover as a minimum, seeking comfort that the product being sold was attractive to buyers. A road map, marked by key milestones, was then required to ensure 100% of debt cover by project delivery.

Loan to Cost (LTC) and Loan to Valuation (LTV) ratios have also been impacted however not to the same extent as presale requirements. Banks continue to be comfortable at a maximum of 70% LTC. Non banks are comfortable to consider up to 90%. A few lenders have been happy to consider 100% of cost cover but only for deals that typically had stronger equity margins in the end valuation or net realisation.

FIGURE 8: For Residential Construction Lending, The Minimum Presales To Debt Cover Prior/Upon Finance Close:

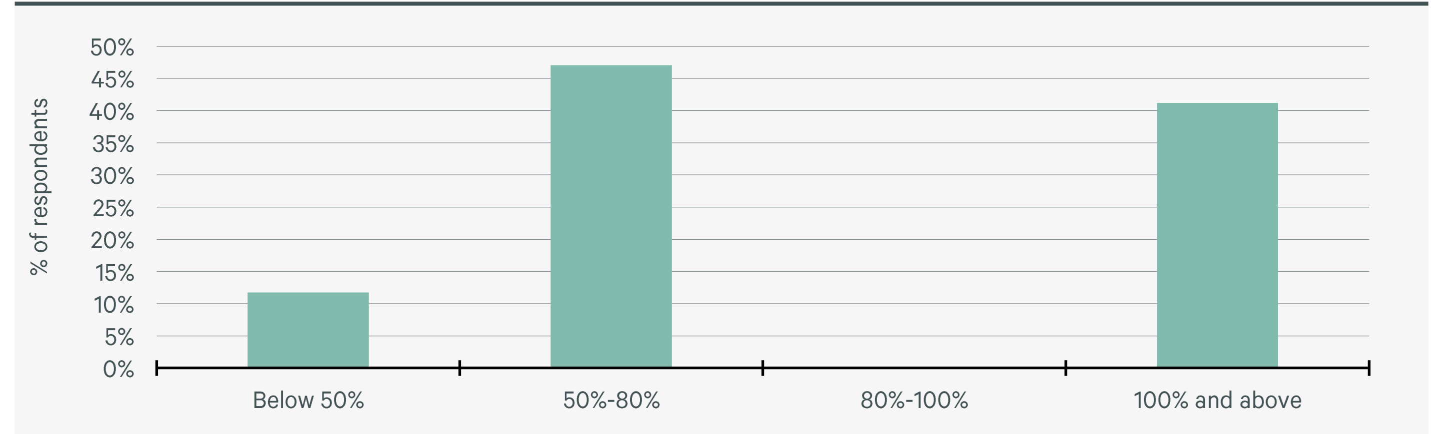
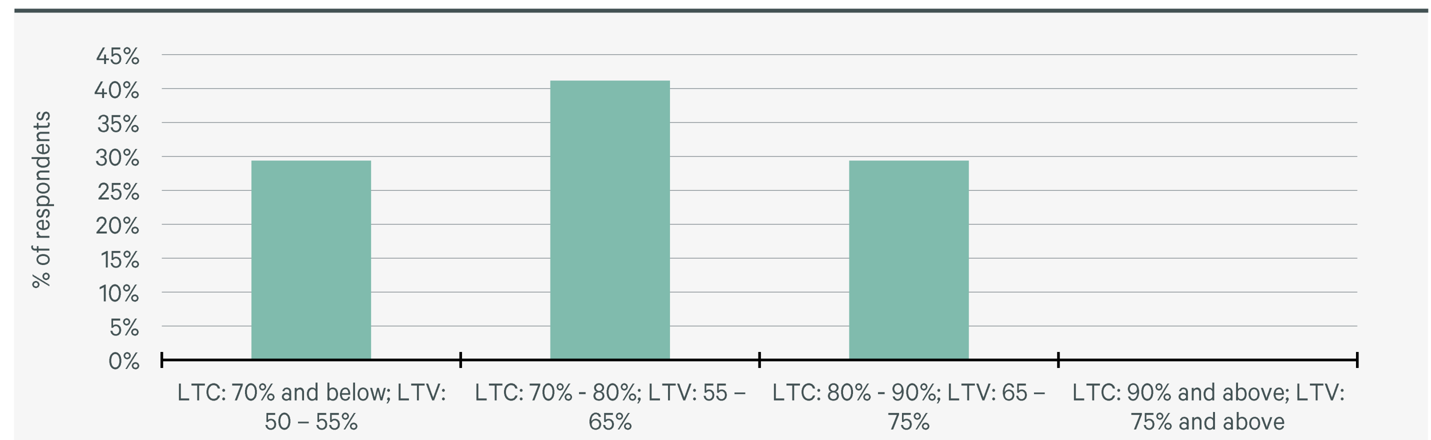


FIGURE 9: Current Maximum LTC and LTV Requirements for Construction Lending



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