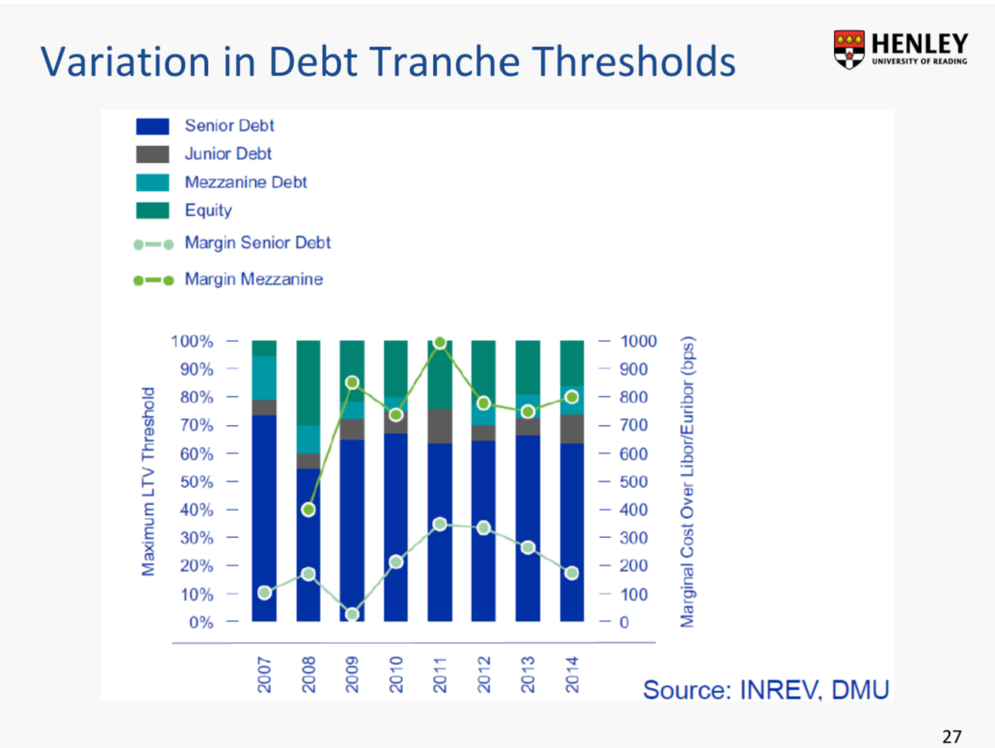
The global financial crisis as one of the most important moments in economic history of the world which fundamentally changed the financial markets. One of the biggest drivers of the crisis was the real estate bubble. The deregulation in terms of mortgages, lending and rating of financial instruments such as MBS pushed the prices of real estate to unsustainable levels often without strong fundaments for such inflation. The crisis started by many foreclosures and defaults which pushed prices of real estate down, further incentivising more mortgage payers to default due to lack of incentive to pay the instalments. Simply said the total mortgage payments were significantly higher than the value of the property thus the owners of the property preferred to default than payback the bank. The connection between the real estate market and financial market was visible mostly by the derivatives. For commercial banks the long maturity loan is risky taking into account the fixed rate of the loan versus the floatation of interest rates and very limiting considering the cash reserve requirement. The solution for the banks was to sell the mortgages to financial institutions. After securitising the mortgages the pools of mortgages are sold to the investors usually big financial institutions such as insurance companies, investment banks, hedge funds. Those institutions usually have connections to the general public, thus the circle ends. The high complexity and interconnection of those institutions made the crisis so profound and affected both the big institutions and the general public.

As indicated on Graph 1, before the crisis developers were able to borrow about 75% of LTV for the investment in real estate simply by the senior loan usually sourced from big banks. After that the ratio went down to about 50-60%. Having that in mind the role of equity has been crucial after the crisis and more conservative investors had an advantage over the aggressive highly leverage competitors.



Graph 1: Variation in Debt Tranche Thresholds, Henley Business School lecture materials, 2024

The BTR sector is fundamentally different than the general real estate market. Usually the developers in order to maximize the rate of return use as much senior debt as possible, sell the project as fast as possible, usually just after stabilisation or even practical completion. Of course the BTR sector also focuses on the return and efficiency but it usually focuses on more than only the financial return but stability and long term perspective of the project. Another aspect which is different for the BTR sector is that because of the future ownership of the development the quality of the project is crucial part of the development. For the rest of the market, the quality is important but it's usually not the cornerstone of the project. The focus is on the costs optimization which usually leads to lower quality. Another aspect is the user experience and sustainability. The BTR sector has always been focusing much more on the user experience and sustainability because it improves long term potential of the development. Those striking differences and the turbulence of financial markets made the BTR sector a very interesting alternative.

The key drivers which drove the BTR market after the GFC can be categorised in three sections

Investment opportunity with risk mitigations:

The BTR sector provides an opportunity for investors to diversify and allocate the funds in a more stable and predictable investment. The steady income from tenants without including many intermediaries, creating the derivatives such as MBS, makes the investment less risky and more close to the investor. Big investors have a real impact on the way the development will take place and can adjust it to their preference and risk exposure.

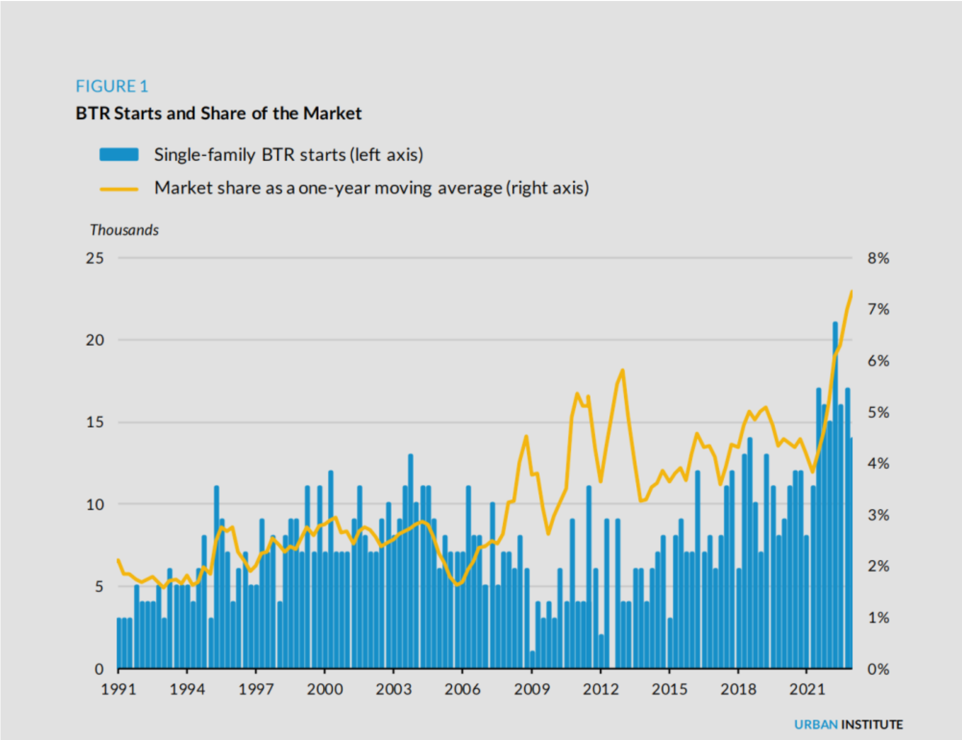
Market recovery stimulus with urban regeneration:

After the GFC many investors were very sceptical about the real estate market. Thus investment in property naturally went down. The BTR sector was able to partially fill the gap and provide the public a new type of product. Because of personal involvement and long term perspectives in the sector the final product is more stable and easy to manage. The other aspect of BTR is its focus on local community and urban structure. Those long term goals also cover this aspect further making the product more friendly to the public.

Higher demand on rental market after the GFC:

Apart from big institutions falling such as Lehman brothers in September 2008 the biggest victims of the crisis were ordinary people. Apart from government bailouts for other big institutions which were to big to fall, funded by the taxpayers the unemployment rate spiked from about 5% to about 10% in U.S. only.

This loss of job naturally decreases the disposable income and reduces the ability of mortgage. Combined with higher requirements after the GFC for the control over the credit score the access to mortgage funding for real estate was way more limited. The inability of consumers to afford buying a house pushed the general public more to the rental sector. With that in mind and all the benefits of BTR for the consumers such as organized management, community and other benefits the choice even though usually forced, improved the potential of BTR sector.



Graph 2: BTR starts and share of the market, Laurie Goodman and Amalie Zinn, Housing Finance Policy centre, June 2023

As seen on the graph 2, the BTR sector accelerated after the GFC and maintains as a strong sector for the residential market. The more holistic and long term approach of BTR created a safe haven for the investors which recently experienced a traumatic event. The crisis caused in big part by speculation, greed and deregulation made the BTR sector seem like a reality check and escape from the extreme. Recent covid and affordability crisis pushed the sector even further and may make it the main offer to consider as a consumer, thus increasing the demand on such a product. The benefits of BTR for the residents such as stability in management, flexibility to exit, security of tenure and certainty of costs in todays market of high inflation and uncertainty makes the BTR a great option for the tenants to consider thus giving the sector a bigger market share in the long term.

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Graphs and pictures:

1. Variation in Debt Tranche Thresholds, Henley Business School lecture materials, 2024
2. Graph 2: BTR starts and share of the market, Laurie Goodman and Amalie Zinn, Housing Finance Policy centre, June 2023