AlphaQ

European property debt programme

By: Beverly Chandler | 14 December 2015 – 17:58 GMT

European Real Estate Capital, the newly formed European commercial real estate debt programme set-up by Brookland Partners and backed by Omni Partners, has made its debut in the European CRE lending market. Beverly Chandler talks with the principals.

Brookland Partners, backed by Omni Partners, has launched a European real estate debt programme, European Real Estate Capital (E-REC) focusing on mezzanine and whole loans structured against good quality real estate with asset management potential.

Steve Clark, Founder and Head of Risk, Omni Partners, explains that Omni is an alternative asset management firm which was originally set up as a hedge fund manager. Clark formerly managed an event driven equity fund and has now stopped trading to focus on private credit, as a result of changes in the financing world. “We have built Amicus, a direct lending platform in real estate,” he explains. The deal with Brookland Partners was done 18 months ago.

Nassar Hussain, Managing Partner, Brookland Partners explains that the firm was set up in 2009 and has been active in the restructuring and work out space. It has been involved in approximately two thirds of all the large real estate debt restructuring transactions in Europe totalling in excess of EUR25 billion in debt, and also buys and sells loan portfolios and raises debt and equity for specific real estate projects.

The E-REC model is based on whole loan and mezzanine funding, targeting value add real estate across Europe, but principally focusing on the UK and Germany and other jurisdictions such as Ireland, the Netherlands and Spain.

Hussain says: “We focus on sponsors with whom we have existing relationships, selling down senior debt and keeping the mezzanine if possible because from a risk-return perspective and from a business perspective it makes the most sense.”

The senior debt market is well-capitalised right now, he says, with more competition and returns which are getting lower, Hussain says. “In the mezzanine space, you have a competitive edge if you can do the whole loan on day one and then sell down subsequently, especially in acquisition scenarios.”

“Within our structures there is a decent amount of first loss of 25-30 per cent,” Hussain says. “We are funding the balance of the real estate and the borrower retains the 25-30 per cent first loss piece as equity. Our sponsors have a good track record in asset management and a recognised ability to enhance the value of the underlying real estate.”

The business plan of the borrower is usually focussed on some enhancement to the underlying real estate. “Typically that means that there are vacancies or other voids in the buildings and the assets need better asset management skills or a better capitalised sponsor,” Hussain says.

“Real estate is quite cyclical and what we are seeing is lots of sub-portfolio sales by the larger private equity players in the EUR25-100 million range and, equally, smaller transactions by financial institutions with the remnants of former property portfolios. As markets have improved and values have risen, they can now exit these legacy positions.”

In terms of E-REC, Clark explains that his firm brings ten years plus asset management and investment management experience in the fund management space.

“We have an institutionally investable platform with money from some of the biggest pension funds in the world,” he says. “We look after investors, keep them informed, we have a culture of transparency. Nassar brings the real estate debt expertise and we bring the fund management expertise.”

The firm is looking to fund four to five loans to establish a track record and has EUR150 million in transactions in the pipeline in three different jurisdictions. The plan is that E-REC will be a fund by early next year and will target high single digit returns on a net basis at around the 9 per cent level.

With its hedge fund roots, the Omni culture is still to ‘eat its own cooking’. “All the business here we are personally invested in and we have run with our own capital before taking outside capital so we can prove our effectiveness,” Clark says.

The full size of the first E-REC loan was GBP23 million. Omni has funded GBP5 million of the loan with its own capital. “We will now sell down our holding and recycle capital to our next loan so we are seeking partners; investors who are attracted to the returns of the product we are producing and looking to invest in the space going forward,” Clark says.

Hussain explains that E-REC’s first loan is for the acquisition of a Liverpool office building which is 77 per cent let to the UK government. This tenant has made a significant investment by converting grade A offices into use as the regional court.

“We look for situations where there is a decent level of cash flow, or the ability to increase the cashflow and value of the underlying real estate through active asset management and capital injections rather than just movements in yields. Each scenario could be different – it could be single assets or mixed use portfolios with vacancies,” he says.