Highcross in discount bond offer on Alburn loan

Bridget O'Connell 05/11/2010 07:55

Highcross is funding a deeply discounted buy-back of nearly £200m of bonds linked to Noel Smyth's Alburn Real Estate Capital.

The property fund manager, through its £1.5bn Highcross Fund III, has teamed up with Smyth to offer holders of bonds between 16% and 75% of their face value.

The tender comes as a £200m loan secured on a portfolio of 44 secondary, office, retail and industrial assets owned by Smyth's Alburn heads toward default in April next year.

The loan was packaged up as bonds and securitised in 2007 when the portfolio was valued at £250m. But in October this year CB Richard Ellis valued the properties at £134m.

This is a 47% decline since Rothschild carried out the origination, putting the current loan-to-value at 138.2%. The portfolio generates a net income of around £15.5m.

In 2008, Smyth injected £3.6m of cash and provided additional property as collateral to correct a breach.

This was followed in 2009 with a restructuring of the loan which included a waiver of the LTV covenants until April 2011 and a reduction in the interest cover ratio.

The restructuring, which was approved by bondholders, also required Smyth to sell £50m of property in order to deleverage the notes.

According to tender documents, the performance of the underlying portfolio is unlikely to improve in the foreseeable future, and the loan is very likely to default again in April next year.

If the tender offer is successful, Smyth and Highcross intend to enter into a five-year business plan and "endeavour to turn around the portfolio without the restrictions and limitations imposed by the current debt structure".

However, it is uncertain whether bondholders will agree to the tender. One analyst said: "Senior bondholders could – theoretically at least – extract better value by holding out and, ultimately, enforcing. However, we would expect the balance of any such decision to consider the outlook for secondary property values as well as the management and refinancing challenges of this portfolio."

It added that some bondholders could reject the offer because they believe that the borrower is using debt discounts to recapitalise at near-bottom of the market prices.

The tender closes on Friday (12 November).

Brookland Partners and Lazard & Co are the joint dealer managers on the buy-back.