



nerej

Tom Goodwin - An opportune moment to acquire commercial real estate

July 07, 2011 - Financial Digest

If you're looking to buy commercial real estate (CRE), the path to a successful transaction today is mostly likely through a financial institution.

The Great Recession has at least for now, redefined the traditional rules of acquiring CRE assets. With so many transactions involving properties that are under water (the outstanding loan balance is greater than the property's value), buyers often must be willing to work with the property's lender to get a deal done.

The good news is that there are presently outstanding opportunities to acquire CRE by acquiring the debt. The correction in property values, combined with a growing sense of urgency among financial institutions to dispose of non-performing loans, is giving investors a rare opportunity to purchase notes on properties at a substantial reduction to peak values.

Opportunities Everywhere:

Judging by the inventory selling at DebtX's loan marketplace, value and yield investors are being presented with a plethora of attractive choices. For value investors, there has been a significant volume of non-performing or under-performing loans collateralized by stalled condo projects; dated or challenged hospitality assets (hotels/motels/extended stay); land, acquisition & development and builder loans. Also being sold in growing numbers are loans secured by franchise assets, such as restaurants or convenience and gas stores; retail locations hit hardest by the economic downturn; smaller securitized loans that have defaulted; and loans secured by operationally intensive businesses, such as nursing homes and marinas. These loans are being offered by high-quality issuers, including banks, special servicers, insurance companies, and government agencies, such as the FDIC and the U.S. Department of Housing And Urban Development (HUD). Acquiring properties collateralized by non-performing debt can be a cleaner and simpler way of buying into a property than trying to free the assets of encumbrances before it is purchased. Those issues can be resolved after taking possession of the property and as part of the turnaround plan for the asset, or after a re-capitalization of the ownership structure.

Performing Loans In Demand:

For investors not interested in purchasing the underlying asset or getting into the capital structure, there is also a growing pool of seasoned performing loans that offer attractive yield adjusted returns. These loans are being sold by banks, insurance companies and pension funds for a number of reasons: They are now outside of the lender's core market geography; the institution has discontinued lending to that market segment; or the loans no longer fit the lender's strategy because of the loan size or property type. An institution may also have recently completed an acquisition and wants to sell the loans that don't fit with its strategy or portfolio moving forward, possibly to raise capital or for other reasons. This type of active portfolio management strengthens an institution by

re-liquefying its balance sheet and creating opportunities to deploy the capital into more profitable segments of the market.

More Inventory On The Way: Financial institutions are racing to strengthen their balance sheets and improve revenue for at least two compelling reasons. First, financial institutions continue to be under pressure to grow topline revenue in the wake of tepid economic growth and new regulation, such as Dodd-Frank. The soon-to-be implemented Dodd-Frank regulations will result in a loss of billions of dollars of fee revenue across the industry that is unlikely to be replaced any time soon. Second, institutions need a strong balance sheet to dictate the terms of their own future, now that another round of banking consolidation is under way. Only those with a robust balance sheet will be in a position to acquire competitors or fend off unwanted suitors. Small and regional banks in particular are most vulnerable. They have a higher concentration of the most toxic loans and a narrower revenue base than the nation's largest banks.

The bottom line for investors is that there will continue to be many opportunities to either acquire the underlying real estate (or an interest in it) by acquiring the loan, or invest in notes with good risk-adjusted returns. For sellers, there's never been more liquidity in the marketplace and more opportunity to maximize price through a loan sale.

Tom Goodwin is executive vice president, sales at DebtX, Boston, Mass.

New England Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540