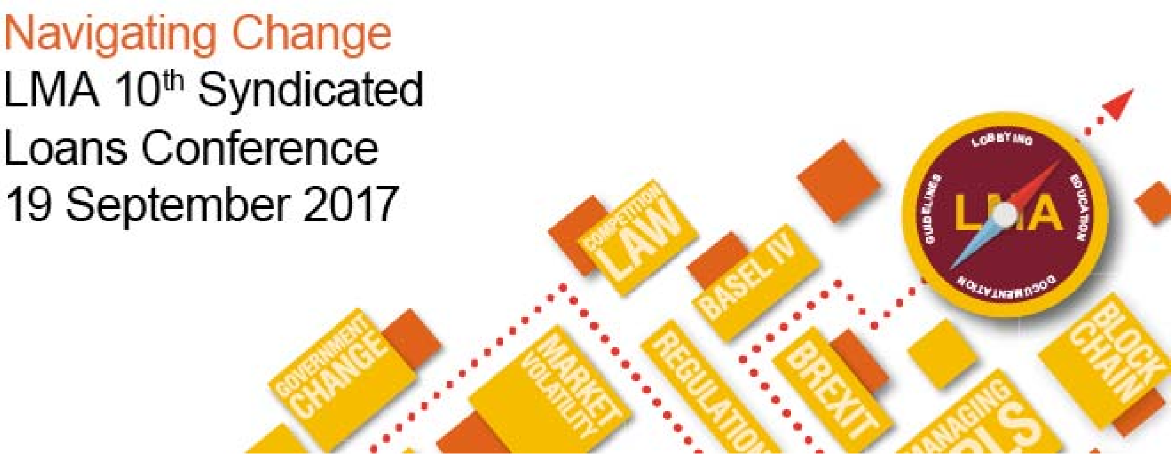

Real Estate Finance in a post Brexit world: the winds of change? (19 September 2017)

QE2 Conference Centre, Broad Sanctuary, London SW1P 3EE, UK

Panel Speakers:	(Chair) Sébastien Marcelin-Rice, Partner – Baker & McKenzie Russell Gould, Managing Director, Commercial Real Estate Finance - Citi Cyrus Korat, Partner – DRC Captial David Phythian, Regional Head of Real Estate, London – HSBC Bank Craig Prosser, Director – LBBW Real Estate Finance Arron Taggart, Director – Cheyne Capital

Panel Discussion

Triggering Article 50

Following the referendum vote on 23 June 2016 to leave the European Union, the UK real estate finance market saw a "liquidity hiccup". Prior to the vote, 30% of the London market was comprised of UK buyers. Following the vote, however, there was a surge in activity by international buyers, owing largely to the fall in sterling, consequential with UK institutions adopting a more cautious approach to lending and investment. After this initial hiccup, volumes for investment properties in the UK have picked up again. The change in risk appetite, however, particularly with regards to UK investors, has resulted in a fall in funding for developments, due to this being a more complex market with lower levels of liquidity.

Can banks still syndicate following Brexit?

In short – yes. Brexit has not halted banks' ability to syndicate a real estate finance loan. However, there has been an increase in the number of club deals, primarily due to European borrowers having a preference for dealing with those lenders with whom they have an existing relationship.

Directly after the referendum period, it was not uncommon for liquidity to dry up during the syndication phase for certain transactions. That said, the market has picked up from this point, and there is currently significant competition amongst international banks looking to participate in real estate loans, particularly for prime assets.

Have leveraged loan terms made it into real estate finance documents?

Leveraged loan terms have not seeped into real estate finance loan documentation. Lenders remember the problems of the global financial crisis and the importance of retaining strong covenants. With global macroeconomic risks, of which Brexit is only one of, creating uncertainty in the market, it is important for lenders and investors to ensure their interests are adequately protected under the terms of the loan, leading to a general resistance to agree to covenant-lite deals.

Debt funds, in particular, have been able to hold steady on this approach, perhaps due to the environment in which they operate. Overall, however, when it comes to documentation terms, the market has experienced a more balanced negotiation between borrower and lender when it comes to loan agreements, with the borrower having more weight to push its terms than it did immediately post financial crisis.

What are the current sectors that are attracting investors?

There are a number of sectors attracting investment, albeit the attractiveness is usually determined by the sponsor and the nature of capital required. Post Brexit, investors are increasingly looking at assets with stable and robust cash flows, with prime assets, such as towers and offices in central London attracting a large amount of liquidity. This long-income asset class is being fed with overseas capital due to its highly liquid nature. In addition to this, overseas buyers have also taken an interest recently in PRS, as well as logistics, both of which are also long-income assets.

Finally, the market has seen a lot of capital being directed into residential in prime central London, as this asset class is predominantly capitalised by way of equity. Lastly, student housing has attracted a large amount of capital over the past year, particularly from equity investors. Overall, capital is being played defensively in the UK, a symptom of the uncertainty surrounding Brexit. An outcome of this has been less capital flowing into retail, an asset class that has become difficult to manage due to the increase in the volume of online shopping.

Aside from the UK, where are investors looking to invest? Are banks already shifting to the EU?

Brexit has meant that some investors have chosen to look to other European countries for potential future investment. Germany and France, in particular, remain attractive countries to invest in.

That said, foreign investors are still highly attracted to the scale and yield that London can provide compared to other European cities. Internationally, London is only the fourth most expensive city, with Hong Kong being the most expensive, Singapore second and Manhattan third. To a Hong Kong investor, London is a large, "affordable" market with long leases. One can argue therefore that with the fall in sterling, Brexit had made London an even more attractive city for investment, especially since asset price adjustment did not take place after the referendum vote. This meant that assets became cheaper for investors paying in foreign currencies.

12 month projection for the real estate finance market

Due to the influx of foreign capital into the UK real estate finance market, the central London market will likely be resilient to any economic waves created by Brexit. There are concerns regarding the durability for mid-market residential developers, who are projected to have issues achieving velocity of sales. Apart from this, the market is optimistic, as the fundamentals that made London attractive to investors before Brexit are still prevalent. Furthermore, due to the flexibility of capital, investors can keep an eye on which assets and sectors are the most liquid in the market in the event of future volatility.