



Real Estate Series -

The opportunities and challenges for RE funds in a post-Covid19 environment

Pierre Beissel

Partner,
Private Equity & Real Estate

Rodrigo Delcourt

Partner,
Private Equity & Real Estate

The speakers



Pierre Beissel
Partner,
Private Equity & Real Estate



Rodrigo Delcourt
Partner,
Private Equity & Real Estate

Agenda

- Introduction
- State of the nation
- Fund structuring perspective
- Regulatory perspective
- Takeaways

State of the nation – the real estate market

■ Market correction

- Certain strategies (hotels, retail in certain locations)
- Bid-offer spread emerged in certain sectors and countries with discounts (5-10%)
- European deals down 75%
- Lower volume expected in Q2 and onwards
- No distress effect so far

■ Impact of real economy on financial market

- Deflation
- Unemployment
- GDP

■ Impact on the debt market

- Borrowing costs increase due to costs of liquidity and risk premium
- Number of lenders to shrink

State of the nation – the real estate market

■ Sectors

- Offices: prime locations secured by low vacancy – subject to impact of “real economy”
- Industrial and logistics: growth of e-commerce and distribution to positively impact logistics. Industries to partially resume activity end of Q2
- Retail: resuming activity to gradually influence the sector – subject to impact of “real economy” and “cost of the debt”
- Hotel: substantial short term impact caused by lockdown. Resuming “real economy” is critical to preserve the domestic market
- Residential: relatively stable during the crisis and potential to grow subject to “impact of real economy”

■ Geographies

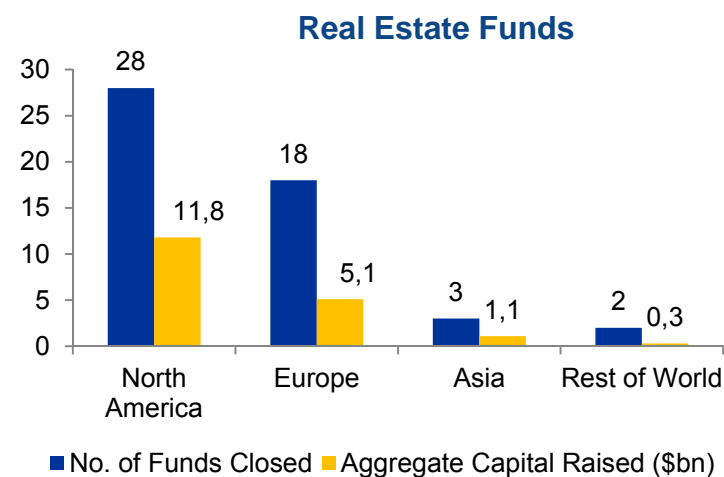
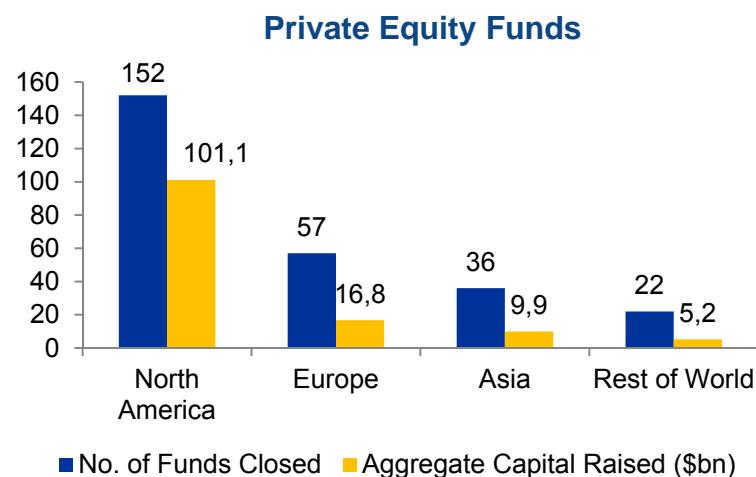
- Some markets seem to be more resilient than others (Germany vs. UK for instance)

■ Expectation:

- Lower activity 2020 and resuming 2021

State of the nation – the private funds market

- In Q1 2020, a total of **USD133 billion** was raised globally across **267** private equity funds, and a total of **51** private real estate funds were closed, raising **USD 18 billion**.



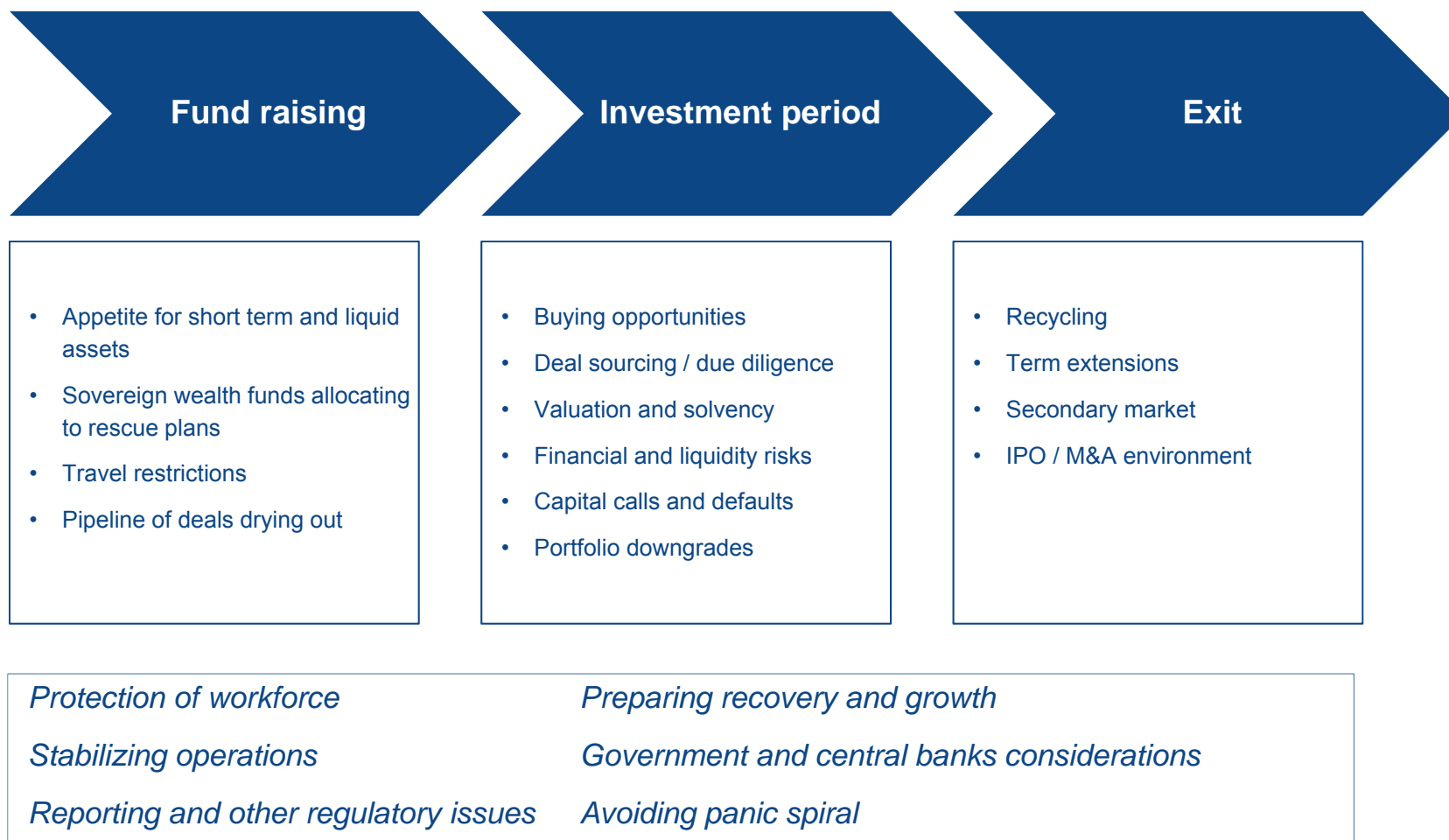
- As of April 2020, the estimated total **dry powder** of all types of private funds globally is **USD2,295 billion**, with **USD1,256.4 billion** in North America, **USD465.8 billion** in Europe, **USD439.6 billion** in Asia and **USD97.7 billion** for the rest of the world.

State of the nation – further outlook for RE funds



- Decrease in deals in 2020 and potentially 2021
- Initial decrease in funds closed and capital raised to be expected
- Substantially lower GDP growth and increased debt levels may lead to increased focus on tax and potential tax increases
- Interest rates most likely stable but borrowing costs should increase to higher risk profile of borrowers

Covid-19 and RE funds lifecycle



Fund raising

■ Challenges

- Investor withdrawal and default
- Real estate quota of investors exceeded due to drop in equity markets
- Practical difficulties in marketing due to travel restrictions

■ Outlook/opportunities

- Creation of opportunistic funds
- Creation of top-up funds
- Real estate funds, in particular with core and core+ strategies, are viewed as a safe harbour
- More opportunities for real estate debt funds
- Secondary market for defaulting investor interests
- Additional allocations to private funds and real estate funds in particular?

Investment period – general

■ Issues

- Covenant breaches – LTV, NAV triggers, margin calls
- Liquidity issues, notably due to lessee defaults and termination of leases
- Renegotiation of management fees
- Deal pipeline temporarily drying up
- Need for extension of contractual investment period due to lack of a market
- Gap between seller and purchaser pricing expectations
- Increase of cost of financing (liquidity, risk premium), even if interest rates do not rise

■ Opportunities

- Deployment of dry powder (cash is king)
- Buying opportunities (fire sales), but initial focus on liquid markets

Investment period – open-end funds

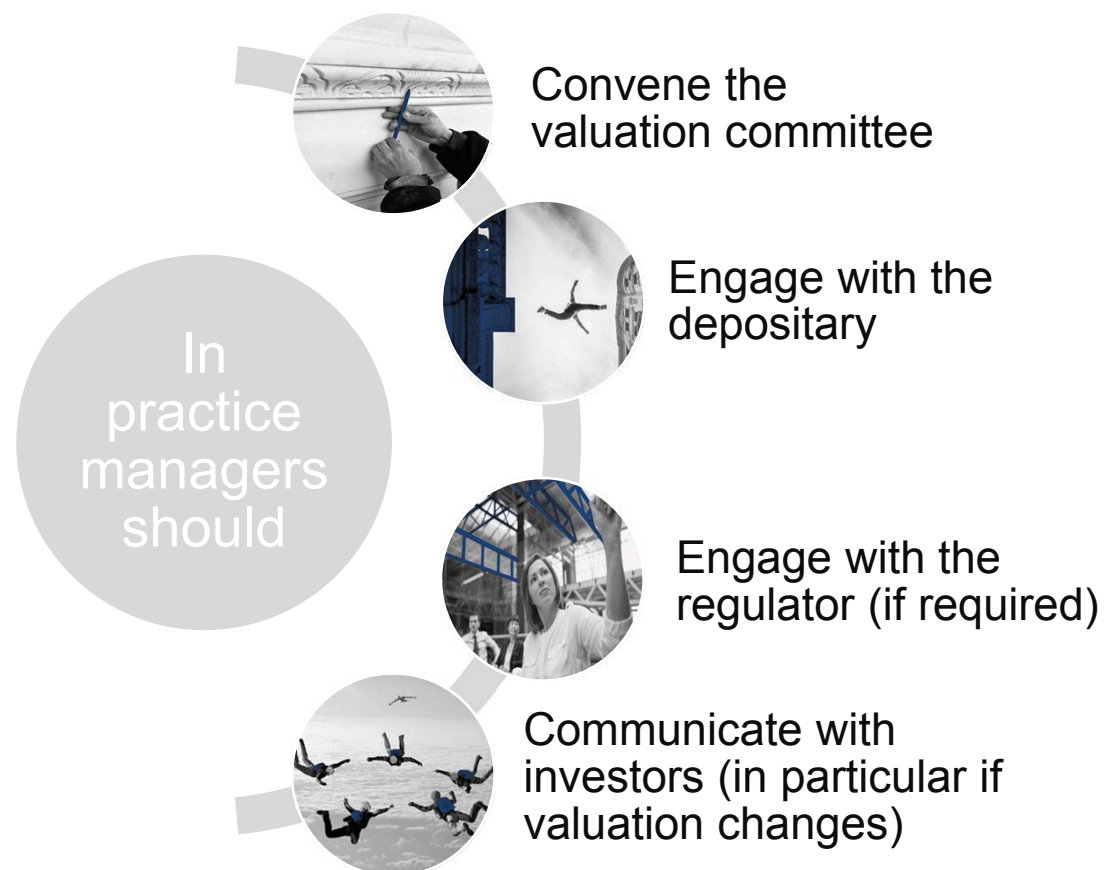
■ Liquidity management

- Restriction and suspension of redemptions (gating, redemption deferral, payment deferral)
- Distributions in kind
- Side pockets
- Restructuring into closed-end fund

■ Valuation to be addressed in order to avoid material transfer of value:

- NAV suspension and temporary or indicative NAV
- Asset value to be assessed on a case-by-case basis and discussed with valuer
- If not possible to value, need to report to management body
- Manager / AIFM ultimately responsible for valuation
- Funds' terms and regulators guidance to prevail regarding valuation
- Need to ensure full transparency and disclosure to investors and regulator
- In case of discounted NAV, relevant disclosures (and potentially priority right of subscription) to be applied to existing investors

Investment period – open-end funds



End of lifecycle

■ Issues

- Maturity of fund – possible need for extension in order to avoid losses due to low valuations – subject to fund documentation and investor consent

■ Opportunities

- Recycling of assets
- Secondary market

Regulatory outlook

- Cross-border distribution
- AIFMD 2
- AML
- ESG
- Others to come?

Conclusion and takeaways

- COVID 19 can be considered the first test for the AIFMD post 2008
- Generally, debt levels are lower than in 2008, thus reducing the risks
- Liquid real estate will remain a safe harbour
- Main liquidity and valuation issues yet to come once the economy has been kickstarted
- Valuations could generally return to more acceptable levels
- Opportunities will appear at deal and at fund levels
- Will cost cutting by tenants impact RE investments?





Contact us



Pierre Beissel
Partner,
Private Equity & Real Estate



Rodrigo Delcourt
Partner,
Private Equity & Real Estate

What's next?

Second webinar of the Real Estate series:

“Valuation and liquidity considerations in open-ended alternative funds.”

More information soon.

Visit our dedicated page ***Arendt Covid-19 Solutions*** and install the ***Arendt Insights App*** to find the most frequently asked questions and our answers



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