COLLAS CRILL

Debt funds and the real estate finance market

JANUARY 2022

With the onset of the global pandemic approximately two years ago, there was a sense that new lending in the real estate finance market ('**REFM**') would cease or be severely curtailed while the lenders reassessed their positions in the market. That was certainly true in part and particularly with the clearers and other established lenders within this market. While such lenders negotiated and amended existing loan facilities, there proved to be an absence of bandwidth – and perhaps appetite – among those more established lenders (with large loan books) to write new loans.

Debt funds had risen to prominence during the last international financial crisis as established lenders reduced their lending because of a lack of liquidity and a downturn in certain part of the real estate sector. While debt funds increased their market share in this sector during that crisis, the established lenders maintained their dominant position.

The recent (and continuing) global pandemic has again seen a shift in REFM and an increase in the debt funds' position within this market. Suppressed interest rates, good levels of liquidity, a boom across the UK in the value of both residential and commercial real estate but a lack of appetite from more established lenders in REFM has led to investors pooling assets and exploiting an absence of supply.

Critically, debt funds are not traditionally limited by hard and fast restrictions; they analyse and approve loans based on individual criteria. While there has been no return to the environment where the borrower/lender relationship trumped all other considerations, debt funds are a lot more flexible with their loan portfolio and are able to offer loans with higher loan-to-value ratios. Regulation has also played a part in the rise of the debt funds. Banks are subject to capital adequacy requirements meaning that higher leveraged loans are more expensive to provide.

So what for the future of this sector and debt funds? That somewhat depends upon the direction of travel of the clearers and their appetite to re-engage in those areas of the market together with the outlook for the UK property market.

In the short term, interest in the real estate market does not show any signs of decline and together with repurposing of commercial assets, debt funds will continue to lend and increase their market share in this sector. It is clear that debt funds are here to stay and we will see an evolution in loan arrangements perhaps with future loan-for-equity exchange positions being negotiated. In the meantime, we can clearly conclude that debt funds provide an important (and in some cases, vital) resource for borrowers in the current climate.

Collas Crill acts for a number of debt funds who participate in both the REFM and other markets and are uniquely positioned to advise on the whole lifecycle of offshore debt funds from our offices in the BVI, Cayman,

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Guernsey and Jersey.

To find out please get in touch with Matt Gilley.

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