



# **The Real Estate Debt Series: Event 1** **'Introduction to Real Estate Debt'**

**Thursday 16<sup>th</sup> November 2023**





**Welcome from our Host**  
**Irfan Butt, Partner at RSM**





## **Moderator Introduction**

**Darren Stolzenberg, Partner at CMS  
& Chair of AREF's Education & Training Committee**



# Presenters



**Kristina Foster**  
**Fund Manager**  
**Schroders**



**Christian Janssen**  
**Head of Real Estate Debt**  
**for Europe**  
**Nuveen**



**Paul Richards**  
**Managing Director**  
**AREF**



# Agenda

- **Moderator Welcome & Intro**
- **Setting the Scene: Paul Richards**
- **Current Debt Market – Opportunity: Christian Janssen**
- **Debt funds & their place in the market: Kristina Foster**
- **Moderated Q&A**
- **Finish by 10:15am**





# Setting the Scene

Paul Richards, AREF





**Current Debt Market – Opportunity**  
**Christian Janssen, Nuveen**

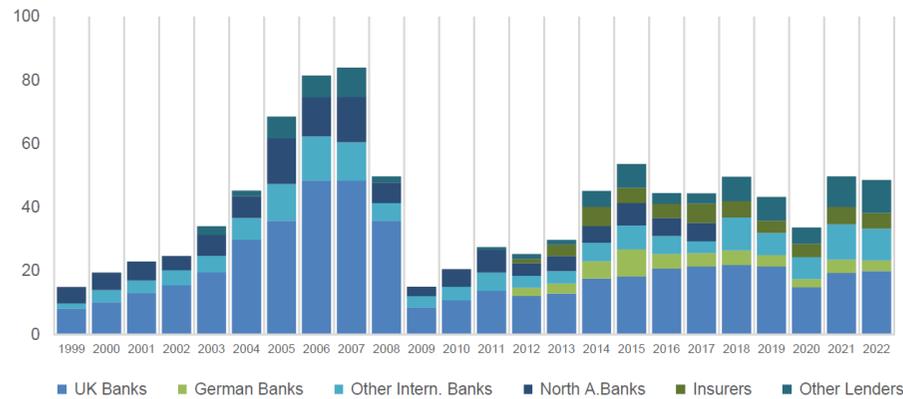


# Current Debt Market – Opportunity

## Evolution of non-bank lending in Europe

- Timing / History – pre-GFC and post-GFC

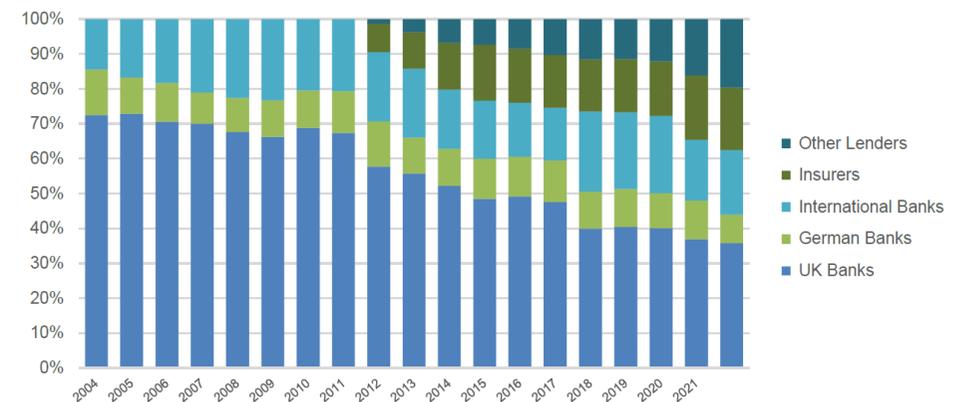
Figure 2. Loan originations by lender type, £bn and % of total 1999 – 2022



Source: Bayes Business School Commercial Real Estate (CRE) Lending Report.

Note: Insurers were not identified as a separate lender type before 2012. North A. Banks were merged with Other International Banks from 2018.

Figure 12. Outstanding loans by lender size, % of total



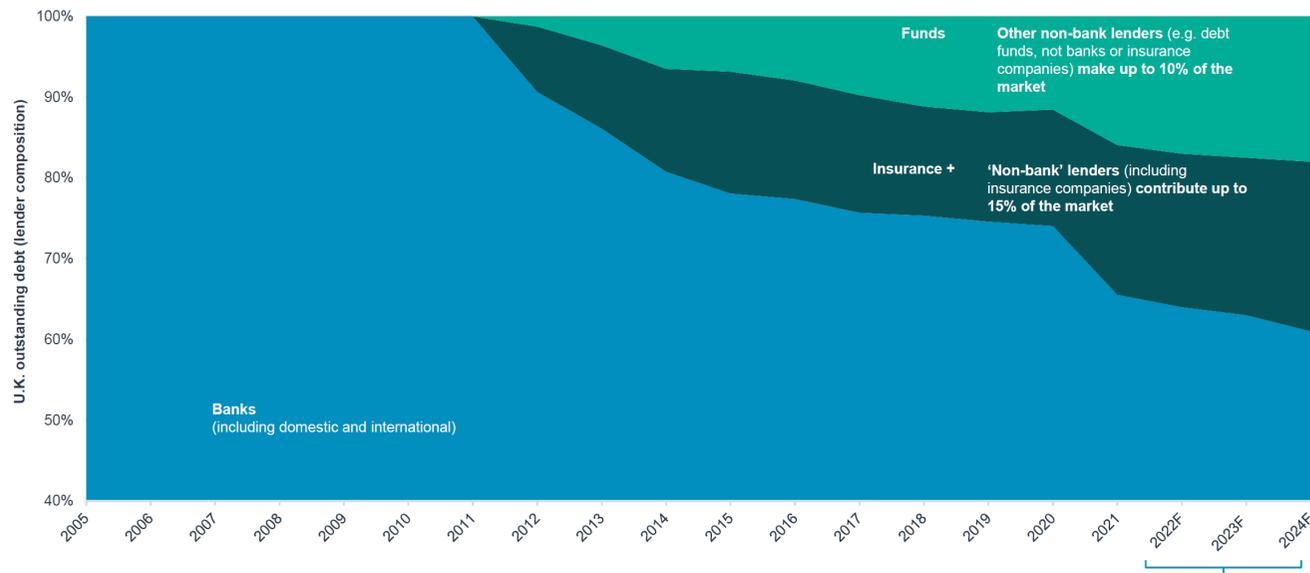
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# Current Debt Market – Opportunity

## Evolution of non-bank lending in Europe

- Drivers / Catalyst for change and evolution
- Market Participants / Types of Lenders



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# Current Debt Market – Opportunity

## Lending Market Update

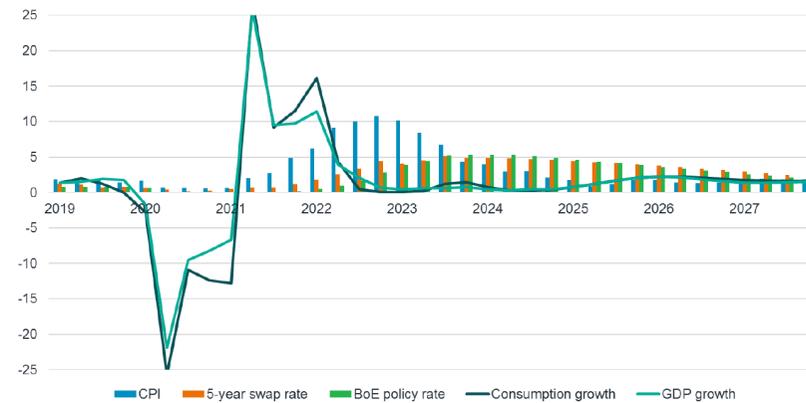
- Current Dynamics
- Property Valuation adjustments and uncertainty
- Interest Rates (base rates and spreads)
- Supply / Demand and funding gap
- Bifurcation of the Credit Market

U.K. historic GBP swap rates (%)\*



\*Graph above shows SONIA swaps from 5 May 2021  
Source: Refinitiv, Q3 2023

U.K. base case economic scenario (% , per quarter)



Source: OEF, October 2023

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# Current Debt Market – Opportunity

## Lending Market Update

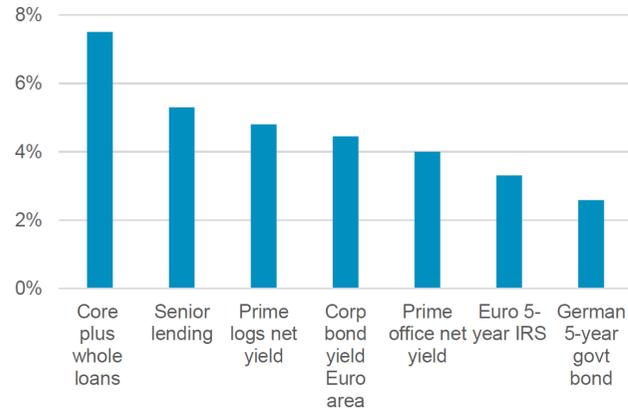
- Credit vs Equity
- Relative value
- Nominal and Risk-Adjusted Returns

U.K. relative pricing (% p.a.)

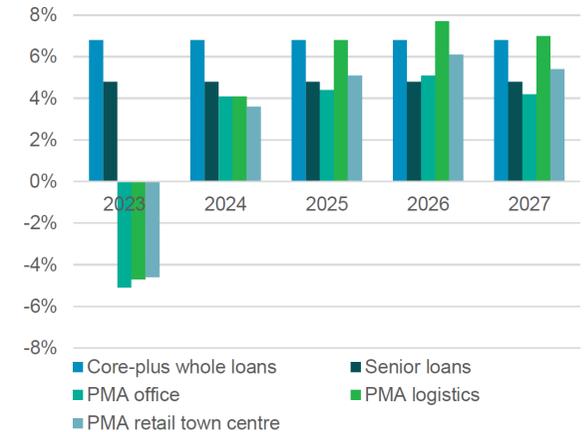


Source: Macrobond October 2023, MSCI October 2023

Interest rate and yield comparison<sup>1</sup>



CRE forecast total returns<sup>2</sup>



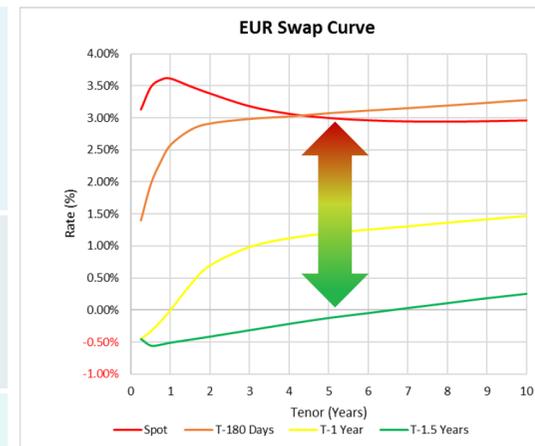
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Past performance and target forecasts are no guarantee of future returns.  
<sup>1</sup> Macrobond, Nuveen May 2023, PMA Q2 2023 Europe ex-UK  
<sup>2</sup> PMA April 2023 Europe ex-UK

# Current Debt Market – Opportunity

## Lending Market Update

<b>Increased cost of debt in last 18 months</b>	<ul style="list-style-type: none"> <li>• Base rates → dramatic change</li> <li>• 2 year swap → 400+bps increase</li> <li>• 5 year swap → 350+bps increase</li> </ul>
<b>Spreads</b>	<ul style="list-style-type: none"> <li>• Best assets / locations in resilient asset classes → little change</li> <li>• Everything else → moderate widening ... but also at lower leverage</li> </ul>
<b>Banking sector distress</b>	<ul style="list-style-type: none"> <li>• Liquidity / credit loss pressures → retrenchment of traditional lenders</li> <li>• Increased regulation and capital requirements (Basel 3 and 4) → more expensive cost of capital</li> </ul>
<b>Impact – funding gap and higher returns</b>	<ul style="list-style-type: none"> <li>• Reduced supply of, but continued demand, for debt → funding gap</li> <li>• Increased lender pricing power → higher absolute returns</li> <li>• More conservative lending basis → higher risk adjusted returns</li> </ul>



**More attractive debt investments**

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**Debt funds & their place in the market**  
**Kristina Foster, Schroders**

Schroders  
capital

November 2023

*REAL ESTATE DEBT*

# Real Estate Debt Fund Structure

Pan-European, commercial real estate debt funds

## Investing in real estate debt in Europe

Debt strategies to meet risk/return profiles

	Structure	Regulated Investment Fund i.e. Luxco Structures
	Fund Life	Typically 5-7 years
	Interest Rate	Fixed or floating
	Target markets	Country specific, European.....Global
	Target Sectors	Commercial real estate debt across all RE sectors
	Investment strategy	Bi-lateral loans, real estate secured
	Performance objectives	Target returns based on strategy
	Investment Period	24 months

Real estate debt platforms are usually spread across three risk/return profiles:

	<b>Investment Grade</b> Secured investment grade senior loans Average LTV <b>&lt;55%</b>	Target returns + Sonia / Euribor <b>+150-250 bps</b>
	<b>Senior / Whole Loan</b> Senior secured and senior whole loans Average LTV <b>60-75%</b>	Target gross returns <b>8-10% p.a.</b>
	<b>High Yield / Opportunistic</b> Senior Secured, mezzanine and development loans Average LTV/LTC <b>60-80%</b>	Target gross returns <b>10%-12%+ p.a.</b>

# Non-Traditional Lenders vs Traditional Lenders

Different approach to lending

1

## Approach

- Ability to support specific equity strategies with tailored credit solutions
- Unlocking value for borrowers and providing enhanced returns to investors

2

## Risk/Return

- Bespoke risk/return solutions developed to meet particular investor requirements
- SMA strategies allow targeted approach to investment

3

## Regulation

- Basel IV adjustments to RWA calculations requires greater capital allocation
- Forbearance rules around covenant breaches
- Both have reduced Bank lending capacity creating a 'funding gap' which alternative credit sources will need to fill

4

## Capital

- European investment banks are acutely impacted by Basel IV reducing liquidity available for CRE from traditional finance
- Forbearance rules, around covenant performance, will reduce liquidity further
- A demand / supply imbalance for credit opens the door for private capital

# Traditional Lenders vs Non-traditional Lenders

Key differences in practise

## Traditional Bank Lenders

Cheaper financing costs.....if you can get it

Large legacy portfolio with credit issues

Restricted, focus on core relationships

Limited for some sectors / granular or complicated transactions

Strongly risk driven and very binary

Internal reporting, extended process

Slow, drawn-out process

Forbearance rules can impact refinance

**Cost**

**Legacy portfolio**

**New business**

**Sector coverage**

**Risk appetite**

**Process**

**Execution**

**Refinancing**

## Alternative Lenders

More expensive – min target returns

Fewer legacy issues, except mezz funds

Positive, although borrower covenant important

More entrepreneurial approach to risk generally

Greater risk appetite for higher returns

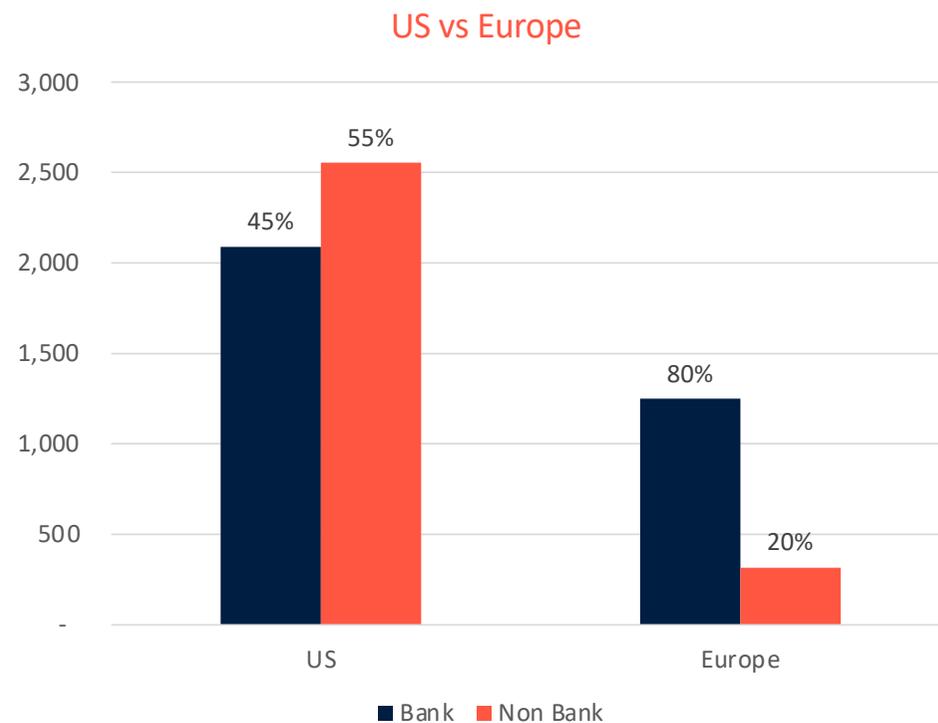
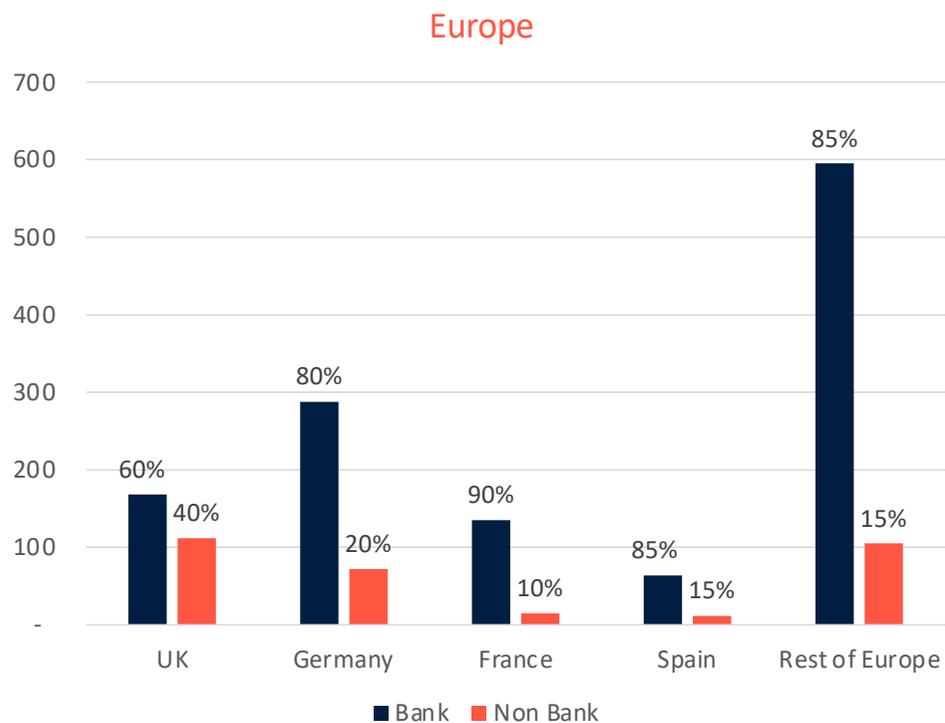
Shorter reporting lines, smaller teams

Quicker overall, entrepreneurial

Fund life reduces refinance options

# The opportunity today

## Bank vs Non-bank CRE debt market (€bn)



Source: US data from Moody's April 2023, European data from H1 2023 European Bayes Lending Report

Schroders  
capital



# Moderated Q&A



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**Final words**  
Darren Stolzenberg



**Thank you for joining us.**

