
Reference:

CASE STUDY III

From:

Advanced Development

Date, Place:

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To:

WHOM IT MAY CONCERN

CASE STUDY III

The issue

A developer declared default on his 15 million euro residential development scheme as a result of the 60 % fall in prices and a significant drop in demand. The project is in the design phase, no construction works have been started.

The issue is that banks could face a loss of up to 80 % because of the market circumstances that lead to a dramatic decrease in value of the land plot and due to the time and money consuming legal procedures.

Normal situation and normal market conditions:

- The bank would move to fire sale via an enforcement officer. This officer will organize a tender to sell the land plot. From the financial point of view the loan is valued usually at 65-75% of the asset value and following the tender the bank would have obtained up to 85-90% of the asset value. Thus the entire cost of the debt, interest and cost of enforcement would have been covered.

Current situation:

- The value of the asset will cover in the best case scenario 20-25 % from the value of the loan (considering a 60 % fall in real estate value), since there is no secondary market and often the "same developer" buys its property in the tender thus causing a serious loss for the bank. Also this is a lengthy procedure requiring extra costs from the bank.

The solution – project rescues to maximize return and avoid a fire sale or a bankruptcy procedure.

The process was structured in two sections, analysis and implementing.

Analysis

A thorough analysis of the development and all aspects of the real estate market that might have a direct impact on the success of the project (e.g. legal status, local authority infrastructure development, competition, market forecast (demand) etc.) has been conducted.

The present case study relies on a full cooperative investor/developer to the agreed solution with the bank.

Implementation and adding value

The master plan will be revised to add value and renegotiate the conditions with the local authorities to fit the new concept. Also the financial structure will be redesigned and EU funding structures for the local authorities will be primarily taken into consideration.

Analysing the market situation and the plot conditions, in order to make this project successful involvement of all parties (i.e. lender, investor, public authorities, etc) is required.

An envisaged solution may be a sport and entertainment park.

For this type of development there are EU funds which can be used for extension of utilities for such park and for other developments in the nearby area, as well. Also the investor (i.e. developer) should inject additional funds in development of the sport and entertainment park.

The decision to go ahead with the development is based on prior agreement with a well known specialized operator and a detailed study about present and future competition (i.e. another investor develops a similar project in the same region).

Second phase would be a food retail store with a well known operator, with the aim of securing fast and steady cash inflow for the project.

With the EU funding and in close connection with local authorities new amenities will be brought to the site and at the same time local community's living standards will be improved. Also, the cash flow will grow significantly and new construction solutions could be designed.

The advantage for the lender is that it will get the benefit to receive money from the exploitation of the sport and entertainment park and the increase of the land value which is not used for the construction of such park.