

'Hold versus Sell'

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As mentioned elsewhere in this edition, and the previous edition, of UK real estate insights, the nature of the real estate crisis is changing, as is the attitude of the banks. As tenants struggle and pressure increases on cash flow, we can expect to see more property companies become insolvent.



PricewaterhouseCoopers is already involved in a number of high-profile administrations of property development companies such as Castlemore, Oakdene and Rock, as well as other administrations where real estate is a significant component, such as Lehman. A key question that we are often asked is: “Why aren’t you selling more of the properties that you are holding?”

Our role, as an administrator or receiver, is to achieve the optimum return from the assets for the benefit of all creditors and, in our view, that is more likely to be achieved by holding and working the properties rather than selling somewhere near the bottom of the sharpest and deepest property-based recession in recent memory. When we are instructed, our first task is to make the assets

secure from vandalism or other threat, and then to embark on thorough due diligence from a legal, property, valuation and accounting perspective. Why accounting? Well, there may be applicable and valuable tax losses for example. We need to completely understand each property.

We also, concurrently, seek publicity for the assets to see just who, in the market, might be interested in buying the properties individually or as a portfolio. On average, within the first few weeks of an appointment, we receive and register interest from more than 100 potential buyers, and another 50 or so from agents who say that they represent clients. On Lehman, that interest topped out at more than 350 interested parties. We also make it clear that we are not interested in a so-called ‘fire-sale’ or bargain basement of selling prices, if we decide to bring the properties to the market.

In the main, our default strategy is hold. Why? There is a very simple answer – if the owning company was still trading solvently, would it want to sell its assets right now? There are some assets of poorer quality, low income or declining value, often in Law of Property Act (or LPA) or fixed charge receiverships, which should be sold quickly and these are

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often to be found in auctions, where the market can bid against each other to achieve today's best price.

So, while we are holding the assets, initially, and having completed the due diligence, we sit down as a team, often involving our lawyers and other advisers, perhaps planners or construction cost consultants, to brainstorm the best strategy to enhance value over time, or to decide to sell now. Invariably, if the property was owned by a property

company with a sound management team and viable strategy, we can continue the work they were doing (before their corporate insolvency) to realise the optimum value. The optimum is not necessarily the highest value, but takes into account the time value of money, and the allocation of profits and tax. Sometimes, of course, we amend the strategy if we think that today's market conditions call for a change of planning use, for example.

We are definitely interested in working with asset managers who have a good track record of enhancing value. We recognise that while we have a wide range of skills in-house at PricewaterhouseCoopers, and we work with some very talented property professionals and other consultants, there may be a need for a further working capital injection that the appointing funder does not wish to inject, or there are particular skills, experience or expertise that would benefit the assets for the creditors as a whole.

Sometimes, despite our default 'hold' position, there are sites that we wish to sell now as it seems strategically advantageous to do so. For example, as Administrators to Castlemore, the large Midlands-based commercial and residential property developer, we have decided to market a site called "The British" at Talywain in South Wales. This is a massive site, of some 1300 acres, which has much work to do to bring it to a profitable fruition.

The British site has the opportunity to extract some 360,000 tonnes of open-cast coal, and the entire planning regime needs to be worked up, almost from scratch, although around 150 acres of the site are included in the Local Plan as a general development area and it is estimated that it could accommodate

around 800 dwellings and mixed use developments. In this instance, we think that selling the site to an experienced open-cast coal extraction company, who has significant master-planning expertise, could produce the best result, as the profit from the coal extraction could fund the planning process, which could last between five and ten years. We will be looking for a cash disposal today, with a material overage upside, or a joint venture, where both parties share in the profits over time.

The British has great potential for profit over time from a range of property development and mining activities, so it seems to be just the right kind of property to be marketing at this stage of the recessionary cycle. Given the strong interest already registered in *The British*, we expect there will be significant competition from a range of well-funded and experienced bidders.

At *The British*, we believe that sell today outweighs hold for the next five to ten years in optimising realisations for the creditors.

There is something that funders can do, especially if they favour an early sale. This is what we call 'stapled debt', also known as 'assumable debt'. This simply means that the buyer has the

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opportunity to take over the existing debt of the failed company in respect of the particular asset, or to be able to take advantage of new debt, made available by the secured lender, in order to achieve a better price through debt leverage rather than simply selling to an equity, or cash-rich, player, who the market knows will expect a bargain. At PricewaterhouseCoopers, we expect to see more of stapled debt deals as the recession continues as lenders may well prefer to lend on properties that they already know well, focusing on the borrower – whom they may also know well from other deals, transactions or lending scenarios. Ultimately, whether a player can take advantage of these debt opportunities depends as much on their relationship with the secured lender and their recognised track record in the market, than their particular appetite for the property in question, or the percentage of equity available.

The oldest property adage is, of course, when asked the best three attributes of a particular property, the answer would be ‘location, location, location’. For those of us working in the realm of distressed property assets, when considering the conundrum du jour, of whether to hold or sell, the answer is, more enigmatically, ‘timing, timing, timing’.

[Barry Gilbertson](#) is a real estate partner in PricewaterhouseCoopers, formerly President of the Royal Institution of Chartered Surveyors, is a member of the Bank of England Property Forum and is Visiting Professor at the University of Northumbria in Newcastle.

If *The British* site might be of interest to you or your clients, contact [Palwinderjit Sidhu](#) who maintains our register of interested parties on the Castlemore administration and receivership case.



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