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Off-market deals gain favour with investors in overbought markets

The flexibility and exclusivity of off-market deals is becoming increasingly more popular for sellers as it offers clear advantages compared to structured bidding processes, says John Amram, founder of Berlin-based investment services boutique HPBA.

John Amram (photo: HPBA)

"In many cases, sellers will achieve a better result in off-market deals than in structured bidding processes," Amram told PIE in an exclusive interview. "The latter are simply too rigid and cannot offer the flexibility and depth necessary to create a sustainable win-win situation." He noted that the highest sales price may not always be the ideal outcome of a given transaction. Strategic deliberations are playing an increasingly important role as access to assets is proving difficult in the hot German property market, according to him.

For HPBA – an investment services boutique focused on brokerage across the major asset classes in Germany – an off-market deal is not necessarily an exclusive negotiation between two parties only. "We usually identify between five and 15 potential buyers for a specific deal," said Amram. One advantage is the possibility to create "friendly contracts" in order to build or expand a good relationship, which could lead to making further deals or becoming joint venture or equity partners, Amram added. Other deliberations that are uncoupled from the highest achievable sales price include the execution probability of the deal, finding a buyer who is not a direct competitor, one who is willing to take on the asset management platform of a portfolio or the possibility to arrange an asset or portfolio swap.

"The problem these days is getting access to assets," said Amram. "In off-market negotiations we have the flexibility to agree on more creative solutions such as asset or portfolio swaps.

We can therefore access products, which would otherwise not have been sold at all." For example, a company selling a non-core portfolio outside its focus location could be partly or fully paid with a portfolio in its target region. A recent mandate won by HPBA included the sale of a niche asset fund portfolio. "We were charged to find an 'unusual suspect' for the portfolio, not a direct domestic competitor. The portfolio was sold to a new market entrant in the end, an international insurer." Some hybrid asset classes, for example senior-friendly housing developments, have not made it onto the general investors' radar yet and are thus often sold in off-market deals. "The asset simply does not really fit in with large investors' strict investment guidelines. It is more expensive compared to nursing homes and fits more into the residential asset class," said Amram.

He also told PIE that fewer investors are willing to actually enter bidding processes. "As a participant in these bids, you are typically one of between 50 to 100, so the likelihood to actually close the deal is very low," he said. Across potentially several rounds in a bid, the high costs of due diligence will be taken on by all investors, whereas it is normally only incurred in the exclusivity phase in an off-market deal. The pressure to find product of course still fuels the bids. Amram said that investors are willing to act more quickly, take on more risk, to actually secure deals in Germany. "Another point in case is the rise of share deals, which were avoided in the recent past, but have become more acceptable due to the lack of alternatives."

Amram, who has 15 years' experience in the property industry, believes that pricing is starting to become speculative in some cities. "For some residential investors, for example, high prices are forcing them to stretch their business case," he said. "And so some investors in the residential sector are planning to privatise parts of portfolios to raise returns. But in some cases even that measure is not sufficient anymore and they start to speculate on a continually rising market, which we find questionable."

HPBA operates with a team of five, serving mandates from private investors, family offices and equity groups, for which it seeks acquisition or sales opportunities on the German market, usually ranging in size between €100m and €300m for portfolios and in the single to three digit millions for single assets. Its clients include US investor Thor Equities, German housing firm Wertgrund and Berlin-based value-add investor Caleus. It has also accompanied the market entries of foreign investors into Germany, advised on transactions, coordinated due diligence processes or valued portfolios. "In 2014, we accompanied transactions worth €280m, in 2015 €400m and this year up to €600m," said Amram. "In the mid-term, we are aiming to accompany deals worth €1bn every year." pie