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THE WALL STREET JOURNAL.
 WSJ.com

REAL ESTATE | AUGUST 11, 2010

Creditors Ramp Up Sales of Distressed U.K. Properties

By ANITA LIKUS

LONDON—U.K. banks and other creditors are speeding up commercial-property sales of distressed assets partly because they are concerned the recent increase in prices may be leveling off.



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Derwent London

Derwent London bought the Central Cross office and retail complex on London's Tottenham Court Road, in a sale forced on developer Glebe Holdings by lender Lloyds Banking Group.

But buyers shouldn't expect cheap property to flood the market and reduce prices. While banks will accelerate property sales, they will continue to sell assets in an orderly manner to protect prices in a recovering market, observers said.

This year, there have been 64 deals, which included a bank or receiver, totaling £1.71 billion (\$2.72 billion) compared with £1.91 billion for the whole of 2009, according to data provider Property Data.

A recent deal marks the first time that an issue of commercial mortgage-backed securities backed by British properties was placed in liquidation since the downturn. It involves a group of U.K. office properties, called the White Tower portfolio.

Entrepreneur Simon Halabi borrowed some £1.15 billion, mostly backed by the portfolio. His company defaulted on the loan after falling property values left it in violation of a covenant governing the ratio of the loan's size to the portfolio's value. Control of the properties went to receiver Ernst & Young LLP, which sold six of the nine assets to Carlyle Group LLC for £671 million in July.

Other deals include the £215 million sale of the Cumberland Hotel in London to Starwood Capital Group by the [Royal Bank of Scotland Group PLC](#), and the sale of the office block Central Cross for £146 million to property specialist [Derwent London PLC](#) by property investment and development company Glebe Holdings Ltd., which was forced to sell by lender [Lloyds Banking Group PLC](#).

The assets coming on the market include distressed real estate taken over as well as troubled loans whose borrowers have defaulted. Most are being sold below book value. Glebe bought the Central Cross office property in 2007 for £223.8 million.

"The scale of the deleveraging task facing the banks is huge. With their teams now in place, plus growing awareness over potential future occupier weakness, banks do have to move forward and start to make progress," said Bill Hughes, managing director at Legal & General Property Ltd. Legal & General has bought £350 million of bank-related transactions since June 2009 from five different lenders.

U.K. banks lent generously to commercial-property owners and developers before the credit crunch. When property values started falling, many borrowers defaulted on payments and loans breached covenants.

But to protect the market from further falls, banks have tried to avoid seizing collateral if the owner has been able to service debt. Banks have sold only a limited number of distressed assets.



Some observers predict sales will accelerate partly because banks have completed the process of going through their troubled loans and decided which to keep and which to sell.

Also, some banks are eager to lock in the recent rise in prices. Property values reached their trough in the summer of last year, after falling some 45% since the credit crunch in 2007. They have increased since then, but some are concerned the rise in values is slowing down.

While banks have been reducing their exposure to commercial real estate, they have a long way to go to clean up their balance sheets.

"There is still a lot of debt that needs to be taken out of U.K. commercial property," said Bart Gysens, a Morgan Stanley analyst.

Lloyds has been reducing its exposure to commercial-property loans, which fell to £35 billion in the first half of this year compared with £47 billion in 2008. The bank has identified new lending to commercial real estate as noncore, which means they won't be expanding this part of the business.

Banks also can afford to take more write-downs because their balance sheets are looking better, analysts said. The banks also are concerned some of their collateral might look less attractive to investors in the future because tenant leases are getting closer to expiration and the rental market shows little sign of improving.

Bank sales have accounted for a higher share of market activity in 2010, making up 13% of all transactions. They accounted for about 7.5% of all deals last year. Much of the increase this year is due to the sale of the White Tower portfolio.

Despite the willingness of banks to sell, some observers predict lenders will be careful to make sure the surge in selling doesn't hurt prices.

"The overall level of distressed sales resulting for bank action remains limited," said Peter Damesick, executive director at real-estate-services company CB Richard Ellis. "We expect sales by banks to increase somewhat going forward, but it is likely to be a flow not a flood."

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