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Real Estate Finance & Investment

RUFRANO SETS OUT LONG-TERM GOALS FOR GROWTH AT VEREIT

BY SAMANTHA ROWAN

Glenn Rufrano, the chief executive of VEREIT, is setting the foundations for long-term growth at the once-troubled real estate investment trust. The Phoenix-based company had a strong second quarter, with earnings of $0.22 per share, and is set to shed non-core assets as well as properties where there isn't much long-term potential. "Long-term goals start out with short-term decisions. Our business plan is a foundation for growth and the primary discussion along that route is what we will do from now to the end of 2016," he told *REFI*. "The long-term growth starts after that."

Rufrano took the helm of the company, formerly known as American Realty Capital Properties, on April 1 with the mandate of moving VEREIT past widely publicized accounting issues. "We decided that we needed to start out with the basics—we're a real estate company so we should look at the portfolio and make sure that long term, this is what we want it to be," he said.

The company had about $2bn of assets in June 2013, but by the same time a year later, its assets had ballooned to $20bn. "When you go from $2bn to $20bn in assets, you should cull from the portfolio. It's a very natural process and the first part of what we're doing is getting the portfolio right," Rufrano said.

Glenn Rufrano, CEO, VEREIT

In its analysis, VEREIT is looking for diversity and a strong risk-return *Continued on page 14*

CUSHMAN POISED TO RE-INVENT BRAND

BY ELIZABETH BLOSFIELD

Cushman & Wakefield, which recently completed its merger with DTZ, is preparing to re-invent its entire brand from the ground up. "I think what really has people fired up about this recent development is the idea that we can build essentially a new company using two iconic brands," according to Joe Stettinius, CEO in the Americas at DTZ, who will continue in that role at Cushman. "We're taking the best of all of these companies that we've assembled and creating a single force that better addresses the needs that our clients are articulating."

The firm's clients are increasingly looking for the security of a well-established, global firm combined with the deep market knowledge and individualized approach of a smaller, local firm. Specifically, they want more personalized services, such as advisory, management, leasing and brokerage, in an increasing range of sectors and markets throughout the globe, he said. "Clients are asking for a variety of services in a broader range of places and an integrated

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THE RISE OF THE NON-BANK LENDER

Stuart Boesky, founder of Pembrook Capital Management, explains how the banking crisis opened the door to non-regulated lenders to fill the gap left by banks in the real estate sector

Real Estate Finance & Investment (REFI): What is your background in the lending industry and what drove you to found Pembrook Capital Management?

Stuart Boesky (SB): I was educated as a real estate and tax attorney and took a job with one of my clients early in my career, which turned into a partnership two years later. This company grew into a major, international real estate firm. While I was there I managed the real estate and financial services business, which involved investing both retail and institutional money in various parts of the capital stack of commercial real estate with an emphasis on multifamily rental housing. We took the company public and when I left in 2005, we had $19bn AuM.

Pembrook was founded in 2007 as a joint venture focusing on real estate commercial debt with Mariner Investment Group, a large alternative asset manager. At that time, Mariner did not have any exposure to commercial real estate. They were primarily a large credit-oriented hedge fund operation, and it seemed like a perfect fit. We launched our first fund in 2007, and followed it up with our second fund in 2010. In 2013 we launched our third fund.

From the beginning, our strategy was very conservative, notwithstanding our unease with the level of real estate values as well as the narrowness of credit spreads at the time. We believed the best way to create value in the lending space was to be a direct originator portfolio of real estate loans, which is what we continue to do now.

Due to the fact we were extraordinarily conservative in our first fund, we got through the banking crisis in excellent condition. At

"OUR LIMITED USE OF LEVERAGE IS ONE OF THE FEATURES THAT DIFFERENTIATE US IN THE MARKET, AND IT ALLOWED US TO SURVIVE THE 2008 CRASH"
STUART BOESKY

Pembrook we are very focused on selecting assets very carefully as well as managing our liabilities very closely. Our limited use of leverage is one of the features that differentiate us in the market, and it allowed us to survive the 2008 crash.

REFI: How has the market changed since the start of your career and what is the appetite like for Pembrook's services?

SB: During the first 20 years of my career the banks were continually being de-regulated and they were clearly the biggest pre-crisis portfolio lenders. After 2008, that turned around 100%. Now the banks are extremely conservative because of the structural changes in regulation and we expect that will continue to be the case. This opened the door for non-regulated lenders who are able to act quickly, underwrite accurately and manage and assume commercial real estate risk, which is what we do.

The current credit spread, given the level of risk you are taking, is still very large compared to historical examples and other areas of the credit markets today. This is generally due to the fact that commercial real estate is not a uniform, fungible kind of asset—it is lumpy and cumbersome and takes a lot of work to get right. We believe the outlook is very good and although a lot of people have been entering the space in the past 24 months there is still an extraordinary amount of business out there in the market. The U.S. real estate debt market is valued at well over $3trn so there is plenty of room for everyone.

REFI: What aspects of bridge lending and mezzanine lending specifically attracted you initially?

SB: Historically there has been a very attractive risk-reward ratio in this business. Mezzanine loans today are included in the capital stack at a point that was included as a first mortgage by the banks previously and priced off bank cost of funds. Today the mezzanine position offers significantly less risk than was historically the case and is priced very attractively.

Again it is becoming more attractive as the banks have drawn back their own activity in this space. Banks have a very low cost of funding so if you take out this very cheap cost of capital we're able to fill that gap with a larger cost of capital as it also drives interest to the borrowers, so that it makes sense for us to be there.

REFI: **What is your experience of being a lender through the different stages of the lending cycle? Which stage are we currently at and what challenges does each phase pose?**

SB: Using a baseball analogy, we are clearly through the stage of 'opportunistic distress lending', which I call the first and second innings. Currently we are in a protracted third, fourth or fifth inning, which is different from prior cycles during my career because previously we were operating in an ever-decreasing regulatory environment. The current increase in regulation has extended the cycle phases and allowed us more time to benefit from the opportunities.

If there is a perceived chance of market slowdown or recession, we at Pembrook actually have more opportunity as the market reacts much quicker to potential turbulence. When things really start to get rocky in the seventh, eighth or ninth inning we expect to still be able to access attractive opportunities.

One of the phenomena of the seventh, eighth and ninth innings of prior cycles has always been the propensity of people in the lending business to lever up their portfolios in order to compensate for tighter spreads. As they are unable to get enough yield on their loans they use leverage to maintain the net-yield after leverage. We have been very careful not to do that. We construct our liabilities differently, so we do not have to use a lot of external leverage, by issuing low-cost preferred interests to investors in addition to common interests. We get the benefit of leverage without the risk of borrowing. We expect, by virtue of our low-debt leverage, to weather the storm next time we hit a crash or market slowdown.

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REFI: **How are you expecting the real estate lending space to evolve in the next 12 months and what does Pembrook's pipeline look like for the coming year?**

SB: Our strategy will remain unchanged overall, although we have noticed we are doing less mezzanine lending and more first-mortgage bridge lending. This is simply a result of where we think the best risk-reward return is. In the past we divided our business about 50/50 between the two products, but now it is more like three-quarters bridge lending to one-quarter mezzanine lending.

In addition, we expect to spend more time on secondary markets. Until now, we stressed primary markets because they were far more liquid and allowed us to assess the value of our collateral more accurately. However, now secondary markets are becoming more liquid, and we are able to focus more time on them.

With regard to wider lending trends, there is far more demand recently for construction lending. More and more non-traditional, unregulated lenders will start to enter the construction lending space and some will do well.

Stuart J. Boesky *has 36 years of commercial real estate experience and is CEO of Pembrook Capital Management, LLC, which he founded in 2006. Prior to that, he served as senior managing director and principal of Related Capital Company, executive VP of The Related Companies, Inc. and CEO of CharterMac, one of the nation's leading commercial real estate financial services firms.*