

Little Hope for Investors in Distress

Niche investors are not Samaritans - they insist on quality

BY **RICHARD HAIMANN**

Michael Siefert is the last hope for investors of closed-end real estate funds beset by troubled conditions. As the Managing Director of Madison Real Estate in Germany, Siefert runs the Private Equity Real Estate Fund (PERE Fund) into which U.S. university and family offices [funds] have invested many millions. The German Madison subsidiary invests primarily in closed-end real estate funds organized by private and institutional investors.

“We could invest several hundred million dollars in coming months,” indicated Siefert. Madison, a specialist in niche strategies, is already committed to some 50 closed-end funds. The PERE Fund became known when it bought the unsold shares of "Fonds 77" of the bankrupt initiator Falk Capital. Madison thereby kept the fund with its three rented properties from going under. Since then the phones have been ringing off the hook at the Madison branch in Frankfurt. “We are being contacted by numerous investors in distressed closed-end funds,” said the Managing Director. In most cases however Siefert has to deny their requests.

After all, Madison is not a good Samaritan with a mission to save failed real estate participation funds. “We invest exclusively in funds with high quality properties that provide long-term lease opportunities,” said Siefert in identifying the core criteria. Madison has no interest in shares held in closed-end funds with vacant properties in need of repair. According to an estimate by Stephan Loipfinger, a fund expert, about 90 percent of the German funds launched in the nineties are ailing. "Three-fourths of all closed-end-end real estate funds are simply not marketable", said Bjoern Meschkat, chairman of Deutsche Zweitmarkt, a German secondary market company.

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Moreover, Madison does not depend on closed-end funds of private investors. At the present time the PERE Fund is being offered lots of shares in strongly performing closed-end funds by pension funds and insurance companies, funds that were formed especially for professional investors. “Some institutional investors want to exit these funds because the deterioration of stock values has pushed the share of their real estate investments beyond and above specified targets,” said Siefert.

However Madison itself is very reticent in dealing with these offers. The financial crisis has had a drastic impact on the real estate business. “That makes it more difficult to set prices,” explained Siefert. For lack of comparison opportunities it is often difficult to determine where the fair value of a property might be pegged. According to a study by Jones Lang LaSalle, a consulting company, some 74 billion euros in commercial properties changed hands in the first half of 2008. In the third quarter the trade volume shrank to only 15.4 billion euros.

Because banks hardly grant loans, those financial investors who during the past boom years purchased real estate on the strength of substantial loans are now excluded from the marketplace. Prior to the financial crisis investors in distressed closed-end funds had also directed their hopes to these investors. Yet even investors with strong equity positions from the United States are now acting shy. According to a study by Ernst & Young, business consultants, 85 percent of the 2300 polled professional investors indicated that they expect real estate prices to continue to fall in 2009. Only then would 60 percent start investing again. Investors in closed-end funds that have gone awry will have to continue to wait for parties interested in their real estate.