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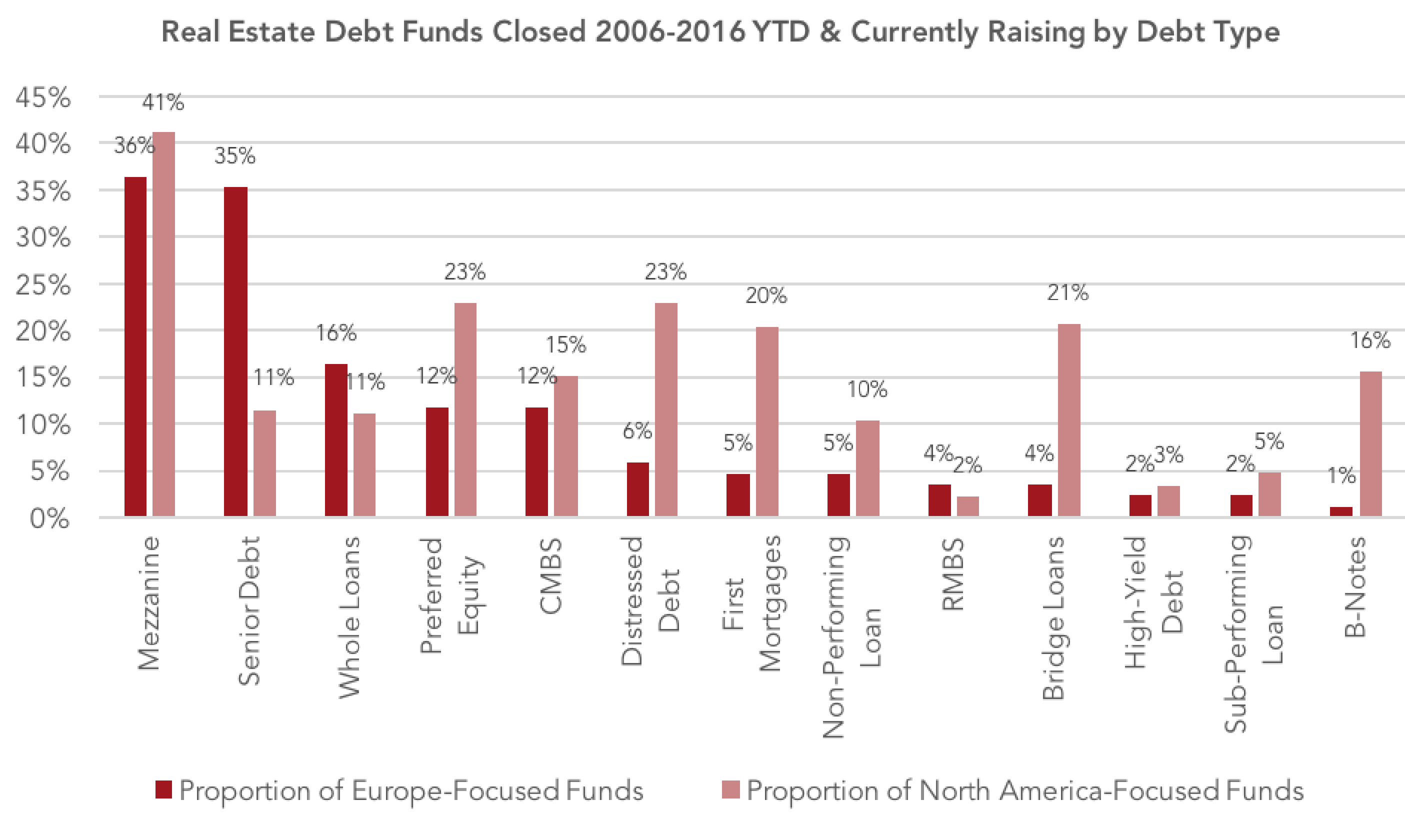
Europe- and North America-Focused Real Estate Debt Funds

Real estate debt has seen considerable growth within European markets over the past few years and fundraising grew significantly from €0.5bn in 2012 to €4.3bn in 2015, while a further €3.7bn has already been secured in 2016 YTD. Nonetheless, North America-focused fundraising still dwarfs that of Europe, with funds already raising a record €12.3bn in 2016.

Aside from the sheer difference in size between the two markets, the marked disparity in fundraising seems to be primarily a result of the varying investment outlooks between the two regions. On the whole, Europe-focused vehicles have tended much more towards lower-risk investments across the private debt spectrum – both in real estate and in alternative lending. North America, meanwhile, supports a greater range of opportunistic and distressed vehicles which look to make investments higher on the risk/reward curve.



The opposing attitudes can be seen in the different debt types that real estate debt funds focused on Europe and North America have pursued over the past 10 years. The highest proportions of Europe-focused funds use a mezzanine or senior debt strategy, both of which are towards the lower end of the risk/return spectrum. Although, North America-focused funds also commonly use a mezzanine debt approach (likely in part because of the strategy's longevity), the next highest proportions use preferred equity, distressed debt and bridge loans. Just 11% of North America-focused funds use a senior debt strategy, compared to 35% of Europe-focused funds; by contrast, 23% of funds in North America take a distressed debt approach, compared to just 6% of Europe-focused funds.

This trend is further exemplified in the largest funds to have closed targeting the two regions over the last 10 years: six of the top 10 largest Europe-focused real estate debt funds closed since 2006 are pure senior debt funds, while a further three predominantly take a mezzanine approach. Just one of the largest funds looks to target distressed debt opportunities. By contrast, five of the 10 largest North America-focused funds closed in the same period pursue mezzanine investments, while three target distressed or high-yield debt, and a further three look to invest opportunistically.

As non-traditional financing in the real estate sector grows in prominence in Europe, it will be interesting to see whether real estate fund managers investing in Europe shift towards higher risk strategies in the pursuit of greater returns.

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