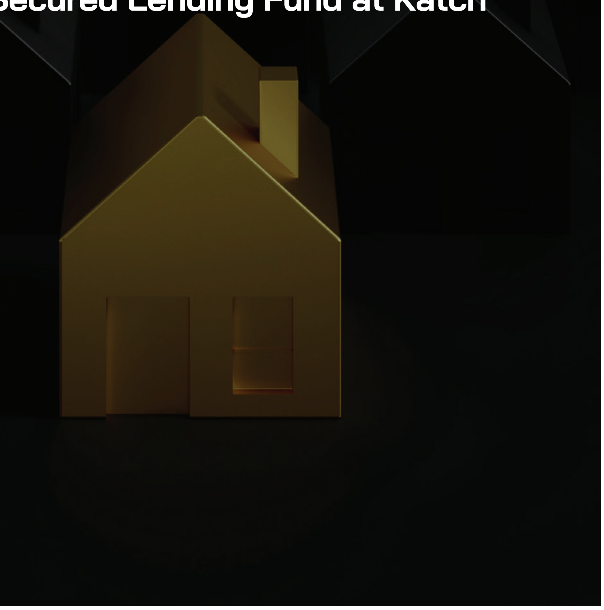
Specialist Property Debt Funding House KATCH Reports Rising Returns and Eminently Manageable Risks

Hubbis in partnership with Janus Henderson Investors and Katch Investment Group recently hosted a virtual discussion focusing on the world of real estate investment opportunities. The mission was to scan the world of international property and identify the right access points through financial sector instruments, both public and private. As a specialist in debt financing for the property sector, she offered delegates some valuable insights into the markets, the opportunities and what investment avenues private clients might consider. Maria Ryan, Portfolio Manager for the Katch European Secured Lending Fund at Katch Investment Group, was one of the experts.



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Katch Investment Group

Commercial real estate investing can take many different forms, and there are many different levels at which investors can participate. The experts on the panel reviewed the potential avenues available, including via direct private market equity, or publicly traded REITs representing equity, they looked at how actively managed mutual and other funds are faring and where the best opportunities might be today, or in the years ahead. They also highlighted the appeals of selected, well-structured private property sector credit that allows investors access to yield higher up the capital ladder and at relatively short maturities.

Catching major gaps in the market

Katch Investment Group (Katch) was founded in 2017 by three partners to offer liquid, collateral private debt products to professional investors by focussing on opportunistic short-term lending products such as first mortgage bridge lending, litigation funding and factoring. The firm has today built up roughly USD750 million of AUM with a focus on UK and European first mortgage bridge lending, UK litigation funding and a niche factoring fund in Brazil. Staff is based at the London Headquarters, where all UK and European underwriting is undertaken, as well as locations across continental Europe, Central and South America and Asia. Maria is the Head of the UK Office and manages its European real estate lending strategy.

Katch is dedicated to liquid, senior-secured private debt, focusing on investment strategies where capital is scarce with relatively high and stable returns. According to its website, in the aftermath of the global financial crisis, major central banks' liquidity injections inflated traditional asset classes, while new regulations reduced the banks' appetite and capability to lend on smaller ticket projects.

Katch identified these trends and decided to launch funds that invest in short-term lending and financing opportunities for professional investors and smaller institutions that offer strong fixed charge and mortgaged guarantees. The platform focuses on areas such as real estate bridge loans, litigation finance, and factoring.

Seven vehicles

In an interview with Laurent Jeanmart, Chairman of Katch, earlier this year, he had explained that Katch today manages seven different investment vehicles with a cumulative AUM in excess of USD750 million. All these investment vehicles deploy capital in short-term funding opportunities, the safest and most liquid area within private debt with strong guarantees, such as real estate bridge lending, factoring and litigation funding.

He added that the firm concentrates on short-term opportunities, deploying capital mostly for up to 24 months, but the vast majority of what they do is shorter than 12 months. The capital therefore very often returns to Katch on a regular basis, and with rising rates, the platform is nowadays recycling investor funds into higher-yielding opportunities. On the real estate side, loans are backed by a full security suite of 1st mortgage collateral, share pledges and first debentures at conservative entry Loan to Value of 50-70% .

> **"With banks retrenching from real estate lending, a large volume of value-added projects needs to be financed. In the current environment of uncertainty, it is important to be selective both with regards to the asset class and jurisdiction, as well as carefully scrutinising the sponsor and the associated professional team."**

Rapid growth

Katch's European secured lending fund was launched August 2021, and today manages roughly USD150 million. The Fund provides direct loans with an average duration of 18 months to professional investors, developers, private equity sponsors and corporates in select European jurisdictions, the UK and Ireland. Real asset collateral (primarily real estate) is the primary source of pledged secured loan collateral. The loans capture demand from borrowers looking to finance opportunistic projects and/or execute high asset value creation strategies, who are let down by traditional lenders and require certainty of funding. Katch European Secured Lending Fund is a great alternative to traditional assets due to its non-correlation and high return profile.

She told delegates that they concentrate on the first-mortgage, value-added, opportunistic, small ticket space, with deal sizes of between USD5 million and USD15 million. "In this niche, we really see a dislocation in the market in terms of little or no bank lending, very limited fund lending, and with the market populated by smaller professional sponsors and developers with good balance sheets and a long-standing track record in their local markets that we can back," she said.

Low correlation

In the same Hubbis interview earlier this year, Jeanmart also told Hubbis how this fund offers an appealing alternative to traditional assets due to its non-correlation and high return profile.

He had offered the example of a Luxembourg borrower in the form of a private equity fund that needed a small line of capital as they were selling down assets towards the end of the PE fund's life. He said the PE fund had USD350 million of assets, they borrowed 10 million from Katch against USD250 million of net asset value collateral and paid 14% per annum. "The speed of decision-making and delivery allows us to charge those types of rates," he had reported.

Watching developments carefully

Maria told delegates how they always pay great attention to the macro environment, noting that a recent visit to the Provada Conference, in Amsterdam, European institutional investors and valuers had highlighted how yields have risen in the private space by around 150 to 200 basis points across asset classes. This yield rate expansion reflects an unprecedented rapid monetary tightening and investor risk aversion. She said the Fund's focus is largely on lender friendly jurisdictions, such as the UK, Netherlands and Germany or where lender friendly lending structures can be applied, such as in France.

> **"A funding gap is driving up the 1st mortgage whole loan pricing market, in addition to the increase in base rates. At Katch, we can be very selective and conservative on the projects we support, thereby achieving double-digit returns with safe LTVs in the 50%-70% range."**

Maria explained that while residential investment volumes have dropped in many markets, as investors are more drawn to low risk fixed rate opportunities, Katch is able to still reap strong returns from value-add refurbishment projects in selective major cities, where there is a high demand for space and limited supply, where rents are trending upwards and prime yields are stable or rising.

Good timing for building exposures

"Overall, it is a favourable environment to invest in if, like us, you have capital to deploy and your portfolio is robust," she said. "I could say this is really the best vintage for private debt in over a decade as there are higher yields, asset values are lower, rents are rising and there is unsatisfied demand for financing. Our deals start with LTVs of 50% to 65% on day one at a good point in the cycle."

Maria reported that Hotels have really bounced back since the lockdowns with many cities facing a constraint on new development or licenses and excess demand for hotel rooms. The funding need here is driven by upgrades which need to happen this point in the cycle and which should see a quick payback.

Healthy returns

They also like the healthcare sector, where the market has been relatively stable and where there remains a significant structural under-supply of care homes in Europe, and long waiting lists. "We particularly like more sophisticated, high care, smaller homes, because hospital beds cost about EUR1000 per day in major European cities and the governments do not want to have their beds blocked up, so there is strong demand for space in those care homes," she explained.

Offices, however, are another story. "We are not brave enough to venture back to offices," she said. "Actually, in the UK and the US, it is rather like office Armageddon, although in Europe, working from home is not as established, partly because the commutes from nice leafy suburbs are quite short and pleasant, and there are nice bike lanes and so forth. In London, where I live, the commute is horrendous! But all-in-all we remain wary, and part of that is the pressure on ESG metrics, with regulations driving more sustainability and that means additional cost. Rents achievable in secondary and tertiary office locations would not support such essential capex spend.”

Deep analysis and long experience

The types of projects Katch buys into can be buildings in need of refurbishment, or perhaps existing income-generating properties. “We know our markets extremely well and our underwriting team in London is expert at assessing these deals,” she told guests. “You can say we are more in the higher-return, opportunistic sector, delivering bridge loans that target net returns to investors of 12% per year, and we actually surpassed that last year, achieving 12.38%.”

As to the vehicles, she explained that the funds are open-ended Luxembourg SICAV-RAIF structures, supported by well known counterparties such as Fuchs Asset Management as external AIFM, Bolder Group as administrator and Creand as depositories. The professional investor base is well diversified globally. In Asia, our investors are looked after by Richard Lamb as head of Sales in that region. The Katch Funds are accessible to investors through platforms like AllFunds, Fundsettle, Clearstream and through major custodian banks.

Maria drew her comments towards a close by highlighting how strong their market sector is currently. “The first-mortgage private debt sector we are in is probably the strongest now since about 2012 in terms of having double-digit returns in the opportunistic smaller ticket space and robust LTVs,” she stated. “We focus on favourable jurisdictions, where there are strong legal structures and recourse if required.”

In France, for example, she reported that enforcing a mortgage is difficult, but they can take the shares and property into trust structures, the fiducie-sûreté, which although somewhat more costly, enable immediate enforcement if there was to be a default. “This gives Katch a significant competitive edge and more of a clear run at deals,” she stated. “So, as a private debt fund, we are able to get very good returns on very strong value-creating projects in good and central areas, all with very conservative LTVs and with good sponsors that have equity to bring to the table and a strong track record.”

> **“If lenders effectively manage their macro risk, back solid sponsors with professional business plans and ensure there is sufficient equity cushion (30% to 40%, at least) to weather a downside, this vintage of first mortgage loans will be the best since 2012 due to the combination of lower leverage and higher returns.”**

Diversification and spreading risk

She added that France is accordingly a major focus, with activity also in key tourism towns and cities, such as Deauville, which is very much driven by local demand, or the upmarket ski resort of Megève.

Finally, she added that they spread their assets across a broad geography in Europe and also make sure they have a good mix between income generating and ‘dry’ assets, and between commercial, mixed use and residential. ■