Boston Business Journal - October 4, 2010
/boston/stories/2010/10/04/story4.html

Boston Business Journal

Friday, October 1, 2010

Blackstone pitching new fund targeting RE debt

Boston Business Journal - by Craig M. Douglas

The Blackstone Group is recruiting local investors to pony up for a new billion-dollar-plus investment fund targeting the massive pools of debt backing commercial properties in the United States.

The firm was in town last week and continues to make its pitch in hope of raising additional cash to invest alongside two other vehicles — the **Blackstone Real Estate Special Situations Fund** and another separate account managed by Blackstone — that already have some $1.3 billion in capital committed, according to a source familiar with the matter and a Power Point presentation circulated to prospective investors. Specifically, the recent roadshow targeted local clients within **J.P. Morgan**'s private banking group.

Blackstone said it plans to invest in both senior and junior tranches of debt backing commercial properties, mostly office, retail and multi-family locations that were highly leveraged in recent years. Many of those properties have seen their values decline in lockstep with the economy. In turn, those drops have put thousands of landlords in jeopardy of defaulting on debts set to mature in the months ahead.

In its slide presentation, Blackstone said the new fund will "focus on debt investments with the last dollar of risk well below peak real estate returns." In layman's terms, that equates to targeting slices of debt that are most likely to retain value — even if the property backing that debt falls into foreclosure or suffers further pricing declines.

Blackstone's presentation also detailed plans to fill the void left by traditional lenders — mostly banks — since the financial crisis hit in 2008. The firm said it also plans to use its new investment vehicle to originate loans and refinance properties struggling to find relief from their maturing debt loads.

Blackstone estimates some $3.4 trillion in commercial real estate debt is scheduled to mature before 2018, according to its presentation. The New York-based firm declined to comment for this story.

Real estate experts say Blackstone's strategy makes a lot of sense, given the market's problems of late. Yet they also agree that Blackstone is but one prominent investor among a growing crowd trolling for value in the commercial real estate market. "There's a lot of money on the sidelines," said Paul Donahue, a senior vice president with CB **Richard Ellis** in Boston.

In an interview concerning commercial real estate debt, Donahue said rumors abound that some $100 billion-to-$200 billion in dry powder is now earmarked for opportunistic real estate investments in the United States. He said competition is rabid when a good value proposition — a solid property with strong rent roles — pops on the market. Those factors, along with signs that the real estate market is stabilizing, have made Donahue a bit of skeptic when it comes to the potential returns available to investors.

"This is the crisis that didn't occur and isn't occurring," he said.

Blackstone is already one of the largest CRE owners in the country, having scooped up huge portfolios of U.S. trophy properties using its own funds and through acquisitions such as its $39 billion deal for **Equity Office Properties Trust** in 2007.

While it appears Blackstone has already dedicated considerable firepower to its new investment venture, the capital committed to date — slightly more than $1 billion — indicates that the firm plans to make a tactical strike, not an all-out blitz, at the market, said Bob Towsner, a director in **Goulston & Storrs**' tax and real estate groups. He said a firm as powerful as Blackstone could easily raise more.

"To me, given its size, it tells me Blackstone sees opportunities, but that they're limited," said Towsner, who is not involved with the new fund. "I think the window's there, but the number of opportunities is not what people thought it would be."

Blackstone's new investment vehicle is run by a dozen professionals with resumes steeped in commercial real estate investing. Many of those professionals hail from the very firms blamed for the market's implosion two years ago.

For example, Michael Nash, one of the new fund's two senior managing directors, joined Blackstone two years ago after running Merrill Lynch & Co.'s **Real Estate Principal Investment Group** for 10 years. He's joined by Josh Mason, a former managing director in **UBS AG**'s proprietary CMBS investing team, and Randall Rothschild, another former senior executive within Merrill Lynch's real estate investment group. Both Rothschild and Mason are managing directors for the new fund.

Four others hail from **Morgan Stanley and Bank of America Corp.**

Jonathan Gray, an 18-year Blackstone veteran, and John Schreiber, the co-founder of Blackstone's real estate division and the former president of **Centaur Capital Partners**, round out the new fund's senior executive team.