

The Next Next Big Thing In Real Estate Finance... Really

Real estate funds invest in all kinds of things. Some of those investments do well. Some don't. Lately, the returns from funds haven't looked so great. As funds have grown in size and number and the real estate market has grown ever more competitive, funds have had trouble finding their holy grail of "off market deals." As a result, it has become increasingly difficult for funds to meet their investors' expectations for high returns. Also, as we all know and recall with pain, if anyone wants to invest directly in or finance commercial real estate, the potential dead-deal costs are substantial and the process of finding, vetting and negotiating a transaction is often arduous.

In the meantime, in other parts of the economy, transactions of all kinds have become easier to find, structure, understand and close. AirBnB, Uber, Amazon and eBay are just a few disruptive examples at the low end. At the high end, if anyone wants to buy shares of Apple or GE, they can do it from anywhere through any device and at minimal cost.

Real estate investment too has certainly started to move online in the form of crowdfunding websites, primarily for long-dated equity.

The landscape now offers a range of

crowdfunding options, with varying levels of real estate expertise, disclosure and compliance culture. Some say they are the alternative lenders of the future. For the most part, long-time industry professionals have barely raised an eyebrow. They argue that these crowdfunding sites have so far just financed a combination of non-institutional "fix and flips" or adversely selected assets that could not obtain traditional financing and turned to crowdfunding in desperation. These old hands view the talk of "disrupting" and revolutionizing the industry with a high degree of skepticism. And traditionally, the real estate world has resisted any form of change whatsoever, let alone disruption or revolution.

Others in the industry, a minority, have a different view. We are working with two clients who believe the key to success in real estate will depend on collaborations and partnerships between fin-tech companies and existing institutions, rather than brashly trying to speed past and ignore a huge industry that has been in place, and done business in certain ways, for decades. Whether

for borrowers or lenders, these two clients are creating more efficient capital structures based on disintermediation and transparency. The initial results: broader access to real estate investment opportunities and more favorable financing for real estate investors.

Our clients in this project, Aristone Capital and Propellr LLC (both of whom approved this article), have teamed up with Centennial Property Finance to offer real estate borrowers a complete debt stack through a combination of bank debt and securities sold to investors through an online syndication platform.

Under this partnership, Aristone and Centennial underwrite, negotiate and close a single bank loan to a real estate borrower that they would not have been able to lend to individually. The borrower sees only a single loan on familiar terms, without having to deal with multiple layers of debt. The bank keeps a senior participation that falls within the leverage it will accept. An Aristone affiliate provides the remaining proceeds and syndicates most of that participation through Propellr to small institutional investors and

high net worth investors. Those investors are more than happy to sit in the junior seat in a senior secured commercial real estate loan, while earning a double-digit yield. The entire syndication and selling process takes place online and is documented through a streamlined, comprehensible and user-friendly participation agreement, which we wrote.

Propellr isn't focused only on commercial real estate. It's designed to support similar offerings of debt or equity securities in a range of alternative asset classes (e.g., credit card debt, real estate equities, business loans, car rental financing, or any other type of loan or securities previously available only to select institutions). In any of these areas, sophisticated sponsors can use Propellr to achieve more efficient financing. Financial institutions can use it to recapture some of the business they've lost through regulatory changes.

With our help, the system that Aristone, Centennial and Propellr have developed demonstrates how technology can and will change commercial real estate finance. Pay attention!

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