



Expert Tips Corner



Sale & Leaseback

The importance of the **sale & leaseback** in times of crisis

A number of advisors propose sale & lease back operations as a financing option in times of crisis, however most likely such actors above all wish to self-publicise, above their activity as an agent in the sale of the property.

The sale of property assets and their simultaneous leaseback by the owner may make sense in certain cases and none in others.

The present health crisis is forcing the world's economies into a global economic crisis; therefore we will explain when such a transaction is viable and the circumstances under which it is not recommended.

“*Spain, along with Italy and United Kingdom will be the perfect target for this profile of transaction, considering the strong impact of the crisis on the Spanish economy, however not everything is permitted within a S&L transaction*”

KEY MARKETS TO GENERATE VALUE



Logistics



Industrial, relevant productive sectors



Retail: food distribution



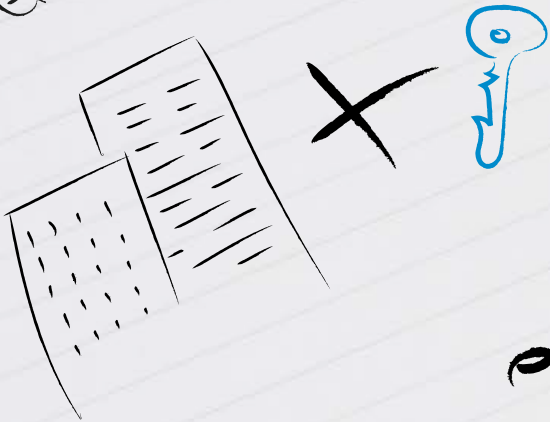
Healthcare: hospitals



Retirement homes



Maintenance = ↑ Risk



Optimize

Traditionally most companies have developed their activity by including the real estate assets on their balance sheets. Maintaining ownership of these assets, considered as strategic in many cases, has added risks and opportunities beyond the core business of these companies.

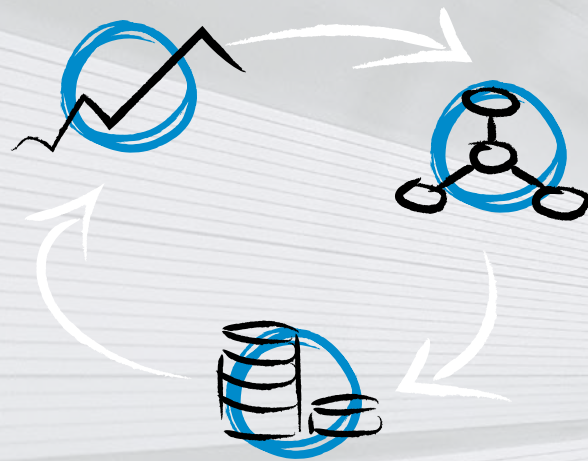
Entrepreneurs are experts in their businesses, in the markets they operate in, as well as in competing in quality, service and prices in a globalized world open to competitors. They are therefore aware of the risks and opportunities of their activity. Yet the real estate market is a different activity, with its own risks and different agents and investors.

When you own a large real estate portfolio on which your business activity is based, you increase your real estate risk in terms of price and asset liquidity, which may in turn be dangerous for your company's viability.

Under similar current circumstances, many entrepreneurs seek additional resources to strengthen their solvency and consider divesting non-critical assets such as their properties. Nevertheless, so as to optimise the sale value of these buildings, they may make mistakes that, rather than strengthening their solvency may jeopardize it.

“ The real estate market is a different activity, with its own risks and different agents and investors ”

The value of a property asset depends on many factors, including its **constant capacity to generate market rents, its versatility and its liquidity**. When attempting to sell property in times of crisis, these three factors become even more significant.



How to be successful in S&L operations

The necessity to sell at the highest possible price is usually linked to simultaneous lease agreements and long-term rent guarantee for the owner as well as the future tenant who on occasions does not have a high level of solvency. Such circumstances often go hand in hand with the need to stretch the lease agreements beyond what is reasonable so as to make attractive those properties that suffer from liquidity or multipurpose problems.

As an example of this, there were some relevant sale & lease back operations, prior to 2009, which established highly extensive minimum lease periods, rent reviews in excess of market levels, the assumption of maintenance and capex costs by the tenant, etc.

Regardless of its potential accounting treatment as debt, the major problem of forcing a lease agreement in order to add value to the asset is the “tunnel” of inflexibility for the seller. What is commonly known in Spanish as “bread for today and hunger tomorrow”.

Therefore the most important aspect in restructuring the sale & leaseback operation is not to maximise the price of the asset to be sold but to reach the perfect balance between the price, lease terms, and if any, the control over the future transfer of the asset. In short, to deal with an advisor with enough experience to be able to anticipate the troubles that a mere broker can get you in.

These types of transactions represent the financing opportunity mostly for companies in which the value of their assets is not recognised within their business valuation; this occurs in many listed companies. It is also for those who pretend to obtain liquidity while maintaining the possibility to sell the assets in the medium term, either partially or totally.

We have advised on significant transactions such as the portfolio of Telefónica, Correos (Spanish Postal System) or the Ministry of Defence and off-market operations such as BBV's headquarters in Barcelona and 3 logistics platforms in prime and secondary locations in Spain. We recently advised Family Cash on a large S&L operation in the supermarket sector.

One of the transactions we were particularly proud of was the advice we provided to a Spanish financial institution in which we were engaged in order to provide a second opinion to an investment bank and an international consulting firm as well as the advisors to that entity. The transaction in question was **the sale of its entire portfolio of branches and corporate headquarters**. Our recommendation was not to carry out such a transaction given the tremendous restrictions of the lease in the long term. And the transaction was not carried out.

This type of real estate transaction offers many different perspectives and should not be structured or executed in the same manner as a single asset sale.

The future success or a problem depends very much on the common sense of a good advisor.




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