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Latham Real Estate Leader Eyes Wave Of Opportunistic Buys

By **Andrew McIntyre**

Law360 (March 12, 2021, 9:18 PM EST) -- The COVID-19 pandemic has put considerable stress on the hotel and retail sectors, and opportunistic buyers seeking low price points are waiting to jump in, one of Latham's global real estate leaders told Law360.

Michelle Kelban

Michelle Kelban, global co-chair of the real estate practice at Latham & Watkins LLP, told Law360 that while retail bankruptcies has been one early stage of the COVID-19 cycle, there is ample capital still waiting on the sidelines for the right purchase opportunities.

Kelban recently spoke with Law360 for the third article in a five-part series of Q&A's with female real estate leaders during Women's History Month and a year into the COVID-19 pandemic.

This interview has been edited for length and clarity.

Where do you think we are right now in the real estate cycle, if you look across all that's happened in the last year?

I think we're in a really interesting place. One thing about this cycle is it almost completely interrupted the cycle that we were already in, which, as you're probably aware, was a very frothy cycle. There was a lot of capital out there. A lot of capital raising, a lot of new funds, on the equity side and on the debt side. A lot of pricing issues in the sense of people having trouble actually finding deals because the pricing was too high. People couldn't execute. Didn't want to pay those prices, etc. A lot of people looking for deals. A lot of people not being able to find deals. And then COVID happened and it completely disrupted the entire world, obviously, and the cycle that was going on.

Initially it was sort of, "OK, everyone was just completely shellshocked, like the world is shutting down. We don't know what to do. We need to asset manage. We need to deal with shutting down properties. We need to deal with liability issues, policy issues. We need to try to get money in the door, fund working capital." I mean it was just a complete disaster. And people focused on that. And then what I would say is relatively soon after that, maybe a few months, we started seeing deal activity. A lot of rescue capital. Preferred equity. Not so many acquisitions, dispositions, but people started to peek and look and say, "OK, well, maybe there's going to be an opportunity. We don't know what it's going to be, but we're kind of looking around." There was some debt starting to come out of the woodwork around May. [Parties were] trying to provide financing, some bridging, for folks that needed it. And then pretty quickly after that, it became just hyper, hyper busy, with lots of transactions going on in many sectors. I would say the least active sectors right now are retail and office, from my perspective, anyway. The most active being actually hospitality. Industrial [and] multifamily [have also been active]. And industrial's very broad, obviously. But those types of asset classes. Also SFR, single-family residential, we're seeing a lot of activity in that space.

We're starting to see people look to do build-to-rent deals. We're starting to see a lot of development, recapitalizations and transactions as well. Again, for these types of asset classes, industrial, multifamily, etc. And in the hospitality sector, we're seeing a lot of financings. People are looking to finance really solid assets. They say, "Look, these assets, they're going to survive one way or another. At some point, people will be back in hotels." They're not looking a lot at convention hotels, but we're seeing activity with sort of the more destination resort types and also some of the "regular way" travel hotels that I guess I'll call them. Some limited service stuff. Things like that. So what I would say, and that's a very long way to answer your question: I think the cycle was completely disrupted by COVID and I think that we're now in a new cycle, which is the COVID-created cycle.

And I think we haven't even seen the tip of the iceberg in terms of the opportunities that people are seeing to help distressed assets, companies. I think there's so much out there, if you think about it, that hasn't even emerged yet. For example, there have been some restaurant bankruptcies and things like that. People … buying brands, using the brands to sort of relaunch new lines of products and things like that, because the restaurant couldn't survive. I mean, it's endless, what I think we're going to end up seeing. And I don't think we're going to even know what the cycle looks like, honestly, until people are really vaccinated and things start to open up again and you start to see some recovery in certain areas. Then you're going to start to see how the cycle changes over time.

So if you think about what your typical day looked like a year ago and what it looks like now, the one obvious difference is you're doing a lot of Zooming now when you may not have been doing that a year ago. But I guess my question is really on the types of matters you're handling for clients now, the types of calls you're getting from clients and the types of deals you're doing now versus a year ago. How would you characterize the difference from a year ago?

I also wear a lot of leggings. That's a difference from what I used to do before. It's interesting. What I would say is a big difference is there's a lot of demand for high-level advising type of expertise on many more transactions than we had before. So, meaning, before you were doing transactions where you would do a deal. You would do a JV to acquire properties. You were doing financings. And a lot of them are plain vanilla. Some of them are much more complicated. But now, everything is complicated. Not only are we seeing a lot of asset management type stuff, meaning problems, issues. "What do I do with my hotel manager? I have minimum return guarantees that are not going to get paid. My hotel manager is asking for this or that." Or, "I have covenants under my loan documents and I don't know if I can comply with them." Or, "The government's put restrictions on me and that's causing me to default under different things and I don't know what to do." We've seen a lot of … distressed joint ventures. "I have a JV partner that's not putting in their capital." Or, "My JV partner and I completely disagree on what we should be doing in this circumstance. What do I do?" It's endless.

Honestly, I've been on the phone since 8 this morning doing exactly that. Advising on a very, very, very complicated deed in lieu of foreclosure transaction for a hotel. Moving on to multiple calls for different clients on a variety of asset management type issues like I just mentioned. And I haven't even started reading documents or any of my regular way deals yet. So that's what the day is now. It's like constant Whac-A-Mole just trying to address these constantly changing issues based on what's happened. We went through that dire period in March, April, May, then things got a little better over the summer and things were kind of opening up a little, and then it got bad again. ... And now things are getting a little better again. And people are looking to the vaccine. And so things just keep changing.

So it's a lot of questions and advising, and we're seeing clients really come to us also with a lot of deals that they might have not always used a [law firm like] Latham for. They might use a different provider, but they're kind of worried … [about] making sure that they've got the best advice and they've got it in multiple areas, because the deals are tending to be more complicated. And so I think we're seeing more … flocking to certain service providers. I think a lot of our PR firms are reporting similar experiences where their clients are coming to them and saying, "Look, I just want you guys to do this because you know what's going on with everything else that we're doing at a high level."

So that has changed some. And the deals are just more complicated. There's just complexity to all of them. Maybe not all of them, but there's complexity to most of them. We're seeing a lot more preferred equity than we saw before. People just trying to sandwich in capital where they can put it, and they need it. And sometimes you can't just do that, right? There are multiple layers. … And so people are trying to create structures that ... get them what they need. It's still a very competitive market, because there's a lot of capital out there.

Let's talk about capital for a minute. How would you characterize the financing market right now, whether it be the bank lenders or the nonbank lenders? What sort of capital is out there, and are companies able to get it, from your point of view?

I think that there's a wide range of capital out there. I think that the debt markets are, generally speaking, open. The nonbank lenders I think are psyched because they're getting better returns than they were getting before, at least for some asset classes. That's why a lot of them were looking at hospitality, because [they thought], "Oh, I could actually get some returns again." Before COVID happened, nonbank lenders were struggling [based on] the pricing. It was very difficult for them to compete. … "Hey, I'm here, I'm just going to do LIBOR plus nothing, basically." That was a struggle, and so the nonbank lenders I think are flourishing. Certainly, obviously, the ones that are well capitalized, that are well positioned, sophisticated, able to really address some of the issues that are going on now in a productive way. I think that some of them did have issues in terms of how they funded themselves. That occurred more in the beginning of COVID, where there were a lot of rescue financings going on for some of the debt funds, given that they had margin calls and things like that under their [repurchase] facilities. That's how they financed their operations.

But that's kind of settled down now, and so now I think you do have players in the market. I think that end users, borrowers can definitely get financing. I think the hardest places to get financing are definitely in retail. I think hospitality is hard in certain places. I think it's hard generally, but I think for certain types of hospitality it's much harder. I mean, I don't know of anybody lending on convention [centers] right now, for example. … Industrial was hot before COVID. It's even hotter now. So in those areas, I think that everybody wants those deals. Literally. On the debt side, the equity side. It's very competitive just like it was before, and even worse, because COVID just exacerbated the need for more of these industrial spaces, distribution centers, the last mile [distribution centers], and all that stuff included. So I think the answer is the debt markets are open and it's still competitive, depending on the sector that you're looking at.

When it comes to hospitality … are those deals location specific and also asset specific, meaning maybe the trophy properties are doing a little better in terms of deal flow and the properties that are

non-trophy properties, for lack of a better word, maybe aren't as attractive? Is that an accurate way to characterize what you're seeing?

Yeah, I think that's right. I think you're seeing, generally speaking, a couple of things. You're seeing lenders and equity players focusing, like you said, on trophy assets or assets that are very strong or [have a] very strong sponsorship, because they just feel like those assets ultimately will survive. They're not convention [center] assets. They're kind of destination [assets], and particularly within the U.S. If anyone wants to travel, they're generally speaking not going internationally. So I think that's also playing into that some, particularly hotels that are close to city centers where people can drive, those hotels are seeing more traffic than they might otherwise have seen, just given all the restrictions.

And then you're seeing, also, people looking at opportunities. For example, one of the deals our firm is working on is the Colony-Highgate transaction, where you've got a big, big player in the hotel space basically saying, "OK, I'm going to buy your whole platform. And I'm going to use this as an opportunity to eat up assets on the cheap." And both of those firms are very good clients of ours, but at the end of the day, that's what it is. It's an opportunity that somebody sees to say, "Look, you want out? This is the time for me to buy it, because the values are depressed and it's a good opportunity." So you're seeing some of that opportunistic buying as well that doesn't necessarily fall into the trophy category of things.

What do you think the next stage of the real estate cycle will be as the pandemic continues to play out?

We are seeing so much deal activity right now, but I think it's going to increase multifold ... once the dust really starts to settle on: What does the economy really look like once people are vaccinated? Are we going to see behavioral changes in certain sectors like office, for example? What is retail going to look like?

I think you're going to start seeing more activity in those sectors. Because right now ... people are sort of in a holding pattern. … Everyone's pontificating about what's going to happen to those sectors since retail's dead, as you hear all the time. I personally don't think so. But what's it going to look like, and what are people going to do, and are people going to finance to do lease-ups? How are we going to deal with the vacant spaces? What are we going to do in the office sector? Are people going to be reducing space? Some people I think are going to be increasing space because they have these open floor plans with everyone sitting on top of each other. What is that all going to look like?

And ultimately there's going to be opportunities associated with that. Whenever there's distress, there's disruption and there are opportunities for people that are looking for them. So I think you're going to continue to see a very busy market across all sectors for quite some time, barring any further COVID-related curveballs. … That's kind of the way I see it. I think we're going to be seeing a lot of activity, just given the amount of distress. I'm an eternal optimist in this way. Hopefully, [there will be] some opportunity that's good for people, but also that will help really revive some of these sectors that need help. Retail and restaurants. We don't want to live in a country where there's only Walgreens. That's not fun. Nobody wants that. And so ultimately, I do think, and I being an optimist and maybe somewhat naïve in this way, I do think that people will act in ways to try to inject life into some of these places, once they can figure out where things are really going from a behavioral standpoint.

--Additional reporting by McCord Pagan. Editing by Jill Coffey and Emily Kokoll.