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Can Nama add value to its property loans?

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Nama faces a great challenge and a great opportunity to deliver on its role as a 'value added asset manager'

In the pre-crash days asset management used to mean adding value to assets by judicious decisions. Currently most of the need for property asset management relates to distressed property assets held as security for loans which have moved from the control of developers and investors to the control of Nama or the banks.

Nama has been branded as the biggest property asset managers in the world. But do they, or we the citizens, really know the task it has been charged with? Does it have the wherewithal to do the job? What are the risks/rewards? Can it do a job which requires Nama to focus on the bottom line as if it is Ryanair but politically be everyone's friend?

Michael Geoghegan, former chief executive of HSBC, in a hard-hitting report advised Nama and the Minister for Finance Michael Noonan before Christmas that "it is of fundamental importance that Nama evolves further beyond the start-up phase and becomes a proactive, externally focused, entrepreneurial, confident business; it needs to be – even when its actions may not be popular politically or in the media".

Mr Geoghegan could have been describing a private sector asset management business accustomed to making hard-headed decisions. Decisions by asset managers must be made for financial – and not political – or social reasons. Here is the conflict: can Nama manoeuvre between these often conflicting goals? Managing a property portfolio can be broken into sections. Firstly, a passive strategy of simply collecting the rents, etc, or secondly, making change happen and adding value. The former is a low risk, low skill and a "market taking" approach. The second is a higher risk, high skill "market making" strategy.

Much Irish property now under the control of the banks and Nama does not fall into this "passive management" category. Nama took over mainly development loans and, by definition, these loans relate to property or property portfolios which have problems.

The banks and Nama now find themselves in an environment that is unstable both at borrower level and local market level. Witness the fall in values since Nama was set up – not of their making – mainly due to the arrival of the IMF, the problems of the euro, sovereign debt and the local and world economies.

The asset management challenge is to increase the value of the asset(s) by applying technical skills, market knowledge, additional investment and leadership, plus acceptance of risk, and all for an expected higher price down the line. It involves hard decisions – some of which will be unpopular or wrong or questionable in hindsight or through the media lens.

So why not simply wait until the market returns as some day it will? Because doing nothing is not a cost-free option for property. Property assets tend to lose value or incur costs of up to 10 per cent each year depending on market conditions. Buildings need to be insured, secured, inspected regularly, heated and repaired, etc. The banks or Nama (or a receiver) will also have their costs of “minding” the situation. But simply “minding” is not adding value.

So the banks and Nama are stuck with many assets which will not sell at a price that is acceptable and, indeed, will fall in net value if not nurtured. The only choice is to hold and to try to add value during the hold period. This takes time and skilled resources and also incurs risk. However, by taking the active workout route the banks/Nama should be rewarded by an eventual higher price – or in the worst case simply preserve values.

But how long can you wait? Will the value keep slipping?

The skills and knowledge required to add value to problem properties typically include: building technology; town planning; legal; marketing; risk assessment; and financial, plus management, leadership and decision-taking. The latter two are often overlooked. All must be fully co-ordinated in a tied-up bundle so as to represent value for money and not yield to value-damaging side pressures – the Ryanair approach rather than the populist one.

Assessment and acceptance of these risks and associated decisions, and balancing them with potential rewards are of key importance in agreeing a brief for any asset manager – including Nama’s brief from the Government.

Mr Geoghegan pointed this out to the Nama board and the Minister in his report. He also suggested that some of Nama’s assets should be managed externally to benchmark its own performance.

One of big challenges facing Nama is the amount of time and number of decisions that go into a complicated asset workout. Do Nama and the banks have the resources and skills, or indeed are the resources present in the country, to do the volume of work that is involved in the very many stalled and complex projects? Are many of the smaller borrowers, even with approved business plans, up to the job? Can receivers do a better job?

While some of the borrowers may have the skills, their progress and performance will require careful input and monitoring. A workout is not the same as a development.

Take, for example, a single shopping centre that was stopped in midstream and abandoned by its developer three or four years ago. By now it will probably have physically deteriorated, its planning permission is likely to have expired, its design team dispersed and most of the subcontractors are possibly bust – and with them the warranties for completed work. To put this shopping centre back together again will take an experienced manager with a support team the best part of two years as well as a lot of cash and many downstream decisions – many minor but all important. It is hugely skill and time intensive.

Nama and the banks have spent the past two years taking over the loans and fighting live fires and selling the low hanging fruit but now the heavy lifting starts. The big issue now for Nama is how a public body with ultra accountability and under ultra scrutiny can do the necessary job and get action.

Only time will tell and, as Mr Geoghegan points out, if Nama does not get this right, it will cost the taxpayer quite a few billion euro. Nama will also be in competition with the non-Nama banks not subject to the same type of intense public scrutiny. Nama faces a great challenge and a great opportunity to deliver on its role as a “value added asset manager”.

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