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## NEWS & ANALYSIS

# Inside Brookfield's San Francisco multifamily expansion

The Toronto-based manager is looking at the city on a long-term basis

**B**rookfield, which earlier this month gained control of a portfolio of 2,149 rent-controlled multifamily properties in San Francisco via a foreclosure auction, sees the situation as an increasingly common example of the impact that higher interest rates are having on commercial real estate capital stacks.

It was a months-long process for the Toronto-based manager to acquire the portfolio, which has been on the firm's radar for some time, Mike Greene, a senior vice-president at Brookfield told Real Estate Capital USA.

"This is a portfolio that has traded hands over the years and our team's history with it dates back to 2010," Greene said. "The prior ownership group was looking to sell in late 2019/early 2020. We didn't end up getting to the pricing where it was awarded, but then covid hit and the deal ended up falling apart. We continued to track it over the subsequent few years and then this opportunity came back around as a non-performing note sale in April of last year."

The foreclosure came after Brookfield in December acquired two portfolios of non-performing first mortgages secured by the 75 properties. The mortgages, totaling about \$915 million, were split into two portfolios and, ultimately, Brookfield won the assets at a foreclosure auction in January.

"This was a unique opportunity to get access to non-performing debt with a path

to ownership," Greene said. "We bought the debt, owned it for a period, filed a notice of trustee sale. No one came to bid against us, and we took ownership of the real estate."

The path to the foreclosure auction was not a simple one, added Swarup Katuri, a managing partner in the firm's real estate group.

"Ultimately, it was a lender-directed sale of the loans," Katuri said. "We are one of the largest real estate investors in the world and we are also a large borrower. Lenders had a lot of comfort with our ability to transact and our understanding of the portfolio."

Katuri, who runs the firm's housing business, noted the process was handled by many different parts of the broader Brookfield team.

"We did all the valuation work up front, but through the process we worked with our capital markets and special situations team, all of whom helped us through the process. Our capital markets team had relationships with the lenders who were selling, which was instrumental in helping us win and close the deal. It was a full team effort here and multiple groups worked on it."

### San Francisco conviction

The firm – now the largest multifamily investor in the city – has partnered with San Francisco-based Ballast Investments, which will manage the assets. The firm's

existing scattered-site, rent-controlled portfolio in San Francisco and its expertise with this more niche product type helped Brookfield to get comfortable with the partnership – and make a plan.

"What we saw was that this portfolio, operationally, was dislocated," Katuri said. "We know what we could do operationally and married that up with the financial metrics and got to a valuation that we thought was very compelling."

That valuation is about 50 percent of replacement cost, a discount of about 35 percent to comparable trades, with what Katuri characterized as a real path to operational upside.

"These assets were in default and had not been invested in for some time. Occupancy had significantly dipped. It was core real estate with a bad capital structure that needed an investor to come in, invest some money and then stabilize the portfolio," Katuri added.

Brookfield is a long-term believer in the San Francisco market, Greene said.

"San Francisco, like many urban centers in the US, has had its fair share of challenges recently. We are not naïve enough to think those challenges do not exist. But the city gets painted with a broad stroke and if you go there, spend time there and are familiar with the neighborhoods, you will see they are alive and well," Greene added.

# Real Estate Capital USA

About 86 percent of the value of the portfolio is in neighborhoods Greene characterized as some of the best in the city, which he added continues to be a hub for venture capital dollars.

“If you look at what we bought, we bought core real estate with a durable income stream. Ultimately, with some investment, these are rent-controlled properties with very sticky tenant bases. We did that knowing and seeing the recovery in our own apartment portfolios,” Katuri said. “We are not expecting

everything to recover fully for this investment to work especially because it is core real estate with durable income streams.”

## **Outlook**

Looking ahead, Brookfield is expecting to see more situations like this in the multifamily sector.

The firm was one of the largest sellers of multifamily properties in 2021 and 2022, even though it continues to like the sector. Pricing at that time was creating

what Brookfield believes was a substantial number of harvesting opportunities, Katuri said.

“On the flip side today, we are one of the more active buyers, and we are seeing interesting places to deploy capital. I think it will be interesting for the next few years because it is not just a function of capital structures being dislocated; we are absorbing record-high supply in the sector,” Katuri said. “If people have enough liquidity, like we do, you will see very interesting opportunities.” ■

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