National Asset Management Agency

<u>Address by</u>

<u>Mr. Frank Daly, Chairman of NAMA</u>

<u>to the Governing Council of the Royal Institution of Chartered Surveyors (RICS)</u>

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Introduction

President of the RICS (See Lian Ong), Incoming President (Alan Collett), CEO (Sean Tompkins), Members of the Governing Council, it is a pleasure to welcome you to Ireland. Let me start by congratulating Alan on his impending inauguration as President of the RICS later this evening. I understand Alan that your inauguration will be the first in the RICS' 150 year history to take place outside of the UK. I am delighted that you have chosen Dublin for the honour and I am sure you will have a successful Presidency.

I believe that the SCSI has provided you with a briefing paper on the NAMA's genesis and overall *raison* d'être and that therefore I can concentrate this afternoon on our future plans and some key messages about the Agency's intentions..

The past and a little of the present

That said, it is important to remind ourselves that the need for NAMA is rooted in the financial and property crisis that hit this country very hard in the later years of this decade. Specifically it developed because of the crisis in our banks – a crisis brought on in the main by injudicious lending to property developers – and which crystallised when the much prophesied "soft landing" for property prices did not materialise. The Banks were left holding extensive land and development loans on their books – most not being serviced, most with little prospect of repayment – in effect deadweight on the Banks' balance sheets and compounding other problems that were emerging for those Banks in different areas. NAMA removed those deadweight loans from the Banks – at a price – we paid them €32 billion for loans nominally valued at €74 billion – a discount of 57% across all the Banks involved.

So in essence we took on the problem loans – 11,000 of them and close to 800 debtors associated with them – and in exchange gave the Banks €32 billion in liquidity. Our Banks are still fragile as they struggle to get back to normal business and ensure adequate capitalisation – one can only speculate as to how much more fragile they would be if that deadweight €74 billion was still on their books.

That is a very potted summary of why we are here.

An even more potted summary of what we are today would be as follows:

An Asset Management Company with a balance sheet of €32 billion – or if you like controlling a property portfolio of €32 billion.

- €18b of that portfolio in Ireland
- €11b of that portfolio in Britain
- €1.3b of that portfolio in Northern Ireland
- €1.8b of that portfolio elsewhere – principally US and Europe

29% of that portfolio is land and development; 55% is office, retail and other investment property (including hotels) and 16% is residential.

We have approximately 800 clients (or debtors) and we have a staff of just over 200 employed in the Agency. Those staff directly manage the top 189 debtor connections who are responsible for 82% of the debt and they oversee management by the Banks of our remaining 583 debtor connections.

We are two and a half years in operation this month; have sold about €5billion assets since inception; approved about €1.3billion in working and investment capital; generated €8 billion in cash in the last 15 months and will show an operating profit after impairment in excess of €200m for 2011.

We are a statutorily independent fully accountable commercial State Organisation (and I emphasise the word "commercial") – you will see why later.

And finally, just before I move on to speak about the future, it is important, in terms of confidence in the Agency – the confidence that is important to Government, to Public Representatives, to taxpayers and currently in Ireland's case the Troika – to be able to say that the first phase of our activities has been completed successfully and effectively.

On that score just in the past month, the Comptroller and Auditor General (C&AG), the State's auditor, has given his verdict on how the Agency handled its first phase, the acquisition of the 11,000 individual loans from the five financial institutions (Participating Institutions) with a face value of €74 billion.

Acquiring these loans was an enormous undertaking.

In less than two years, NAMA built up a loan portfolio of €74 billion; most lending institutions take several decades to build up loan books of that size. Our biggest concern was that we would pay more for loans than they were really worth, by failing to review the underlying loan documentation for potentially costly flaws, or by sacrificing best practice for the sake of speed or convenience. This did not happen. Based on the C&AG's report, I am satisfied that the Agency adopted the right approach in the way it bought and transferred the loans it now owns.

The future

That is the past – and the present.

This afternoon I want to focus largely on where NAMA is going in the future. In particular, I want to focus on asset management, which will be at the core of our activity from now on.

In this respect, today's event is very timely. It follows on two very recent announcements by NAMA:

- that we intend to provide finance of up to €2 billion in development capital in order to preserve, enhance and complete commercial and residential projects in Ireland over the period to 2016, and:
- that we intend to make a further €2billion in vendor finance available for interested investors in the coming few years.

These announcements signal clearly that NAMA has entered a new phase. Whereas the first phase was about protecting Irish taxpayers by being rigorous in the acquisition and valuation of the loans, the second phase is about being innovative and dynamic in maximising the return from those loans and the assets securing them.

Innovative, dynamic and responsive to market demand and market opportunity.

Maximising the return from our loan portfolio at a minimum means recovering the cost of acquiring the loans plus carrying costs and any working and development capital expenditure advanced to debtors. Whilst a large number of factors will go into ensuring that the Agency achieves this objective, I will focus today on essential aspects of our work which I hope will resonate with you as land, property and construction surveyors.

These are the Agency's debtor engagements, our asset disposal strategy, our capital investment programme and our wider policies designed to invigorate the Irish property market.

Debtor Engagement

An optimal asset management strategy requires the Agency to work closely with debtors but in return they must demonstrate that they possess the experience and expertise and are willing to contribute in a tangible way to the workout of their loans and underlying property portfolios. They must also be willing to work with us.

We are sometimes criticised for being too aggressive with debtors and too hasty in appointing receivers; others criticise us for being too soft and not pursuing them aggressively enough. There is a balance to be struck; our approach to an individual debtor is dictated only by what course of action will bring the best result for the taxpayer. Right now we are satisfied that we can work with around two-thirds of our debtors – those who have shown that they can be commercially viable and where we feel there is sufficient trust and goodwill to enable us to work together.

It is useful to say what working with NAMA means for debtors.

It means the sale of properties to support debt reduction, assignment of rental incomes to NAMA, the granting of charges over unencumbered assets where these exist and the reversal of asset transfers to relatives and others in cases where these have occurred. It also means a significant readjustment in terms of lifestyle for debtors. Anything less would be unacceptable to us and to the taxpayers that we serve.

Where debtors are incapable or unwilling to work to NAMA's expectations, we reluctantly consider all available options, including enforcement. To date, NAMA has taken enforcement action in relation to about 200 debtors. But enforcement,, for the reasons outlined, is always the option of last resort.

Rather than emphasising the negative of enforcement however I would reiterate the positive of the prospect of two thirds of our debtors being commercially viable in the future – a more optimistic view of "being in NAMA" than perhaps would have been current this time last year.

Asset Sales

NAMA's asset management strategy is predicated on the phased and orderly disposal of assets. Central to this approach is the disposal of property over the short-term in liquid markets. This enables us to meet our debt reduction targets – *(€7.5 billion by the end of next year – we have €3.25bn of that already paid off and we have full confidence that we will meet the €7.5bn target*). It also enables us to invest in enhancing assets in markets such as Ireland to enable their disposal over medium and longer-term horizons and to provide vendor finance – and of course to pay our way as we go without calls on the Exchequer.

56% of NAMA assets are located in Ireland and a further 34% in Britain, with a large proportion located in the main cities of Dublin, Cork, Belfast and London. Our strategy could be summarised as follows: sell where there is demand and where the price is right; otherwise, develop and enhance to optimise value over the medium-term. In practice, the latter entails resolving outstanding legal and planning issues or completing development works and ensuring the letting of buildings to strong tenants to increase their future attractiveness to prospective investors.

Reflecting the Agency's disposal strategy, of the €9.2 billion worth of asset sales approved to end-May 2012, 81% relate to assets located in Britain.

The key message is that NAMA has the time and the ability to take a longer-term view of its property portfolio and does not need to engage in fire sales. At the same time, the Agency does not intend to hoard land or property. There is, for instance, an estimated €1 billion worth of enforced properties currently for sale, predominantly in Ireland, by NAMA receivers, which is in addition to the sale of assets being conducted directly by NAMA debtors. To further illustrate this point, it is worth considering that while NAMA's residential property portfolio represents less than 1% of the total housing stock in the country; residential properties for sale by NAMA debtors and receivers account for about 10% of all properties currently for sale in Ireland.

To help you get a sense of the process, all NAMA sales are conducted on a competitive basis and in line with prevailing market practices for the asset class and jurisdiction in which the sale takes place. This means in effect that the full range of sales methods are employed – private treaty, sale negotiated directly with a purchaser, sale by public auction, sale by public tender, sale by sealed bids, and other mechanisms tailored to the specific characteristics of the underlying real estate.

There are also specific marketing and reporting requirements, including a statement disclosing any commercial relationship between the agent, debtor and purchaser so as to avoid conflicts of interest during the sales process and to avoid connected party sales, which are prohibited under the NAMA legislation.

Whatever the sales or marketing strategy employed, the objective in every case is to maximise the realised proceeds of asset sales.

Capital Investment

To return to our commitment to provide €2billion in capital investment in Ireland in the period up to 2016.

Government and industry studies suggest that €2 billion of such finance injected into the completion of construction work in progress and new projects to meet future supply shortages could generate up to 25,000 jobs in the construction sector here and a further 10,000 jobs downstream in the wider economy. These benefits are very welcome given current conditions in the Irish economy but NAMA's primary motivation is to generate a greater return for the Irish taxpayer when these projects are completed and ultimately sold.

The Agency is already investing to enhance the assets securing its loan portfolio in all geographies. To end-May 2012, we had approved new capital advances of €1.3 billion to debtors and receivers to develop assets located mainly in Ireland and Britain. Projects supported range from completion and fit-out works across the spectrum of commercial and retail assets through to new residential development.

Needless to say all proposals for new development funding have been subject to full cost benefit analysis to compare the cost of each option against the total expected benefits, to see where the benefits outweigh the costs, and by how much. The key consideration for NAMA is whether the expected return in developing out projects is potentially greater than that from selling the site in its current state or waiting for market improvements – in effect, whether NAMA's debt position is strengthened.

To avoid compounding previous bad practice, NAMA will not advance funds to develop property for which there is no foreseeable demand. So we look for pre-letting of proposed buildings, phased drawdown of funding linked to achievement of pre-agreed sales or rental targets and phased delivery of commercial and residential projects in line with realistic assessments of likely future demand. Our approach also means independent rigorous assessment of construction cost budgets and other financial projections. Joint Venture partnerships will be important to us in terms of our options. They can provide capital and construction expertise and coordinate and manage available resources to best effect. They will be part of our make up in the future.

Asset management requires specialised skills and these will be found in a new Asset Management Division which we have set up to focus on development of a number of larger-scale projects and to work on asset management solutions more generally in conjunction with our Asset Recovery Division.

Right now the new Division is identifying markets where NAMA has material exposure and where demand for completed or new buildings can justify, or can be expected to justify, a project-focused effort, ranging from securing planning permission for development or redevelopment through to actual financing and delivery of significant development projects.

Initial key markets are likely to include the Dublin Central Business District office market, where a shortage of larger office spaces is emerging and the London and Dublin residential markets. The new Division will also focus on managing specific programmes including the delivery of social housing in conjunction with the Department of Environment, Community and Local Government, the Housing and Sustainable Communities Agency and individual housing authorities.

The strategy adopted by the Agency is a joined up one, focusing on near-term development opportunities where they exist whilst, in parallel, working through planning and development challenges in other markets to enable future investment and ultimately, disposal.

Property Market Initiatives

We that our success in meeting our commercial objective is closely linked to the performance of the economy in general: a vibrant domestic economy means increased demand for the property assets which secure NAMA's loans. We also recognise our role in making whatever contribution we can towards instigating a renewal of sustainable activity in the property market in Ireland. Towards this objective, we are implementing a number of initiatives aimed at increasing transactional activity, including the provision of vendor finance, the launch of at least one Qualifying Investor Fund before the end of 2012, and the introduction of a deferred payment mortgage initiative in Ireland.

Vendor Finance

Alongside our recent announcement to invest up to €2 billion in development funding in Ireland, we also announced that we expect to make €2 billion in vendor finance available to prospective buyers in the markets in which we hold commercial properties.

€2 billion is a substantial injection of capital.

To put it in context, Ireland's commercial property market saw just €200 million worth of investment last year. At the peak of the market in 2006, investment levels reached €3 billion. The €2 billion is not, of course, restricted to Ireland but these figures give you a sense of the potential contribution that NAMA vendor finance can make in the Irish market.

Why would NAMA get involved in this?

There is significant investor interest in NAMA's commercial property portfolio but lack of finance is a major constraint, both in Ireland and internationally. Traditional lenders to the commercial property sector are either substantially reducing their exposure to the sector or are withdrawing entirely from it. Where finance is available, funding costs tend to be prohibitively high.

For this reason we are willing to fund transactions for amounts up to 75% loan to value, in the right circumstances. This vendor finance provides a number of benefits. It generates transactions that might not otherwise take place and ensures that we thereby receive 25% or more of the asset price upfront. It also involves a favourable shift in credit risk from debtors to more creditworthy investors. Applied judiciously, vendor finance will enhance competition and price tension and will enable NAMA to convert international investor interest in its portfolio into sales.

There is no single standard set of terms for vendor finance which NAMA may offer to parties acquiring property from our debtors or receivers. Terms quoted will vary to reflect the attributes of various commercial property categories and individual properties, the strength of tenants and leases, and the strength of counterparties/property purchasers. Only strong and reputable counterparties will be considered.

For prime properties, which would qualify for the most generous loan terms, the Agency may offer up to 75% of the purchase price for a period of 5 years at a typical interest margin of 3% over NAMA cost of funds.

The first NAMA vendor finance transaction, involving the sale of an office building at No. 1 Warrington Place in Dublin, was completed in April 2012 to a US investment fund making only its second ever purchase of property in Europe.

QIF, REIT and a Deferred Payment Mortgage Initiative

Before the end of the year, the agency also aims to launch at least one qualifying investor fund (QIF) as a way of attracting institutional investors such as pension funds and sovereign wealth funds to buy properties on a phased basis.

The NAMA Board is supportive of the introduction of REIT legislation in Ireland on the basis that international investors understand the product and that it represents a further potential aid to international investment here. The Agency therefore welcomes the Minister's commitment to keep under review the possibility of introducing REIT legislation in Ireland.

In recent weeks the Agency also launched, on a pilot basis, a Deferred Payment Initiative for certain residential assets under the control of our debtors in Ireland. The initiative aims to improve liquidity in the housing market by reducing the risk of negative equity to purchasers of residential property and thereby encouraging latent demand among those who are keen to purchase but who are concerned that prices have not yet reached bottom. To date, the total value of properties sale agreed under the pilot

Initiative is €7.4 million, with a further €1.8 worth of properties reserved. We envisage that the Initiative,, on the basis of a successful pilot, will be rolled out across the range of regions in which NAMA debtors control properties that may be suitable.

The view ahead

President, having concentrated on NAMA up to now I would like to conclude on a wider note regarding the property market.

There are tentative but encouraging signs of stabilisation emerging in the Irish property markets – and the market-based mechanisms I have spoken about will help reinforce these emerging signs.

These mechanisms are not of course a panacea.

Recovery will ultimately be anchored in economic and financial developments here and internationally and in all parties in the property sectors being innovative, responsive and collaborative.

Its seems to me for example that, in the reality of the Irish property sector June 2012, areas such as density ratios and development levies need to be examined to ensure that they are contributors to recovery rather than barriers.

In that same vein I would place the need for greater transparency on prices within both the residential and commercial property markets. Such transparency would surely improve buyer confidence. NAMA welcomes the proposed publication by the Property Services Regulatory Authority (PSRA) of residential property sales prices. We favour extending this proposal to commercial property sales transactions because we believe that transparency would enhance the efficiency of that market also.

Your members, President, are also very important parties in the property sector and in that context I certainly welcome and congratulate you on the Valuers Registration Scheme being launched here this afternoon. In the past I have criticised the way valuations were conducted in Ireland by some in the years immediately preceding the economic crisis. We are still feeling the aftershocks. So it is only fair that I should commend today's launch as a welcome and positive development.

Your initiative assures the quality of valuations which are key components underpinning most economic activity. I note that you developed this Scheme in response to the global financial crisis – surely the reason I am speaking to you today in the first place! In recognising that there was a need to reduce the risk associated with valuations of real estate and land assets you are surely hitting the nail on the head! By reinforcing professional standards and raising consumer confidence in the delivery of valuation advice your Institution is certainly contributing in a practical manner to the sustainable recovery that we all wish to see and that we must all work together towards achieving.

The Scheme is, I believe, a restatement of the highest standards and integrity that are essential hallmarks of the profession. When referring to the decisions of banks and borrowers that led to NAMA's establishment, I have repeatedly said that we cannot repeat the sins of the past. It is a credit to both the SCSI and RICS that this mantra is being actively applied in the surveying profession.

Conclusion

Whilst there continue to be many challenges facing us, you are visiting Ireland at a time when there are also many opportunities. As a country we have confronted very difficult circumstances but, as in the past, we are managing to move forward. We in NAMA see the Agency as being part of the process of moving forward. Through the approaches I have outlined to you today, we believe we are firmly on course not just to achieve NAMA's core objectives but to be a key contributor to the achievement of economic and employment recovery in this country.

Ireland remains a country that it is open for business, good to do business in and good to do business with.

NAMA too is open for business – open for sales; open for investment; open for joint ventures; open for opportunity.

Thank you.