Philadelphia Investment Manager Switches Fund's Focus to Debt

Commercial Real Estate Direct Staff Report

Iron Stone Real Estate Co. has switched its investment focus to distressed debt from equity transactions and is leveraging its local market expertise to find opportunities.

"Lenders are not about to air their dirty laundry, so a lot of what you can learn about debt available for sale is through word of mouth and knowing your market," said Jason Friedland, partner and director of investments at the Philadelphia firm. "Sometimes you have to know whether a specific property or its borrower is in trouble and then go to the lender to ask about that loan."

Iron Stone is seeking troubled first mortgages on Philadelphia-area multifamily properties on behalf of Iron Stone Real Estate Fund II, which has raised about $50 million of equity and could raise another $25 million by its final closing in August.

The fund last month acquired a $12 million loan on Ogontz Manor, a 205-unit property at 5600 Ogontz Ave. near the campus of LaSalle University in Philadelphia. It has since taken over the property in a deed-in-lieu of foreclosure and launched a renovation effort to improve its 70 percent occupancy. The surrounding area has a 94 percent average occupancy.

The fund previously acquired a package of loans against 13 properties with a combined 364 units in Philadelphia and its suburbs from Astoria Savings Bank of New York.

Iron Stone's predecessor fund, which raised about $10 million, has been fully invested in equity stakes in several Philadelphia properties. Its deals included taking part in a joint venture that in 2006 paid $12 million for Falls Center, a stalled 700,000-square-foot mixed-use project on Henry Avenue near Interstate 76 in Philadelphia's East Falls neighborhood.

The seller was a nonprofit agency that the state of Pennsylvania organized to manage the property after its former owner-occupant, the Medical College of Pennsylvania Hospital, ceased operations there.

Iron Stone's venture, which already had its financing assembled, won the property after the original winning bidder was unable to complete its proposed purchase.

Iron Stone has raised equity for its funds from high net-worth individuals. Principals of the firm have committed 10 percent of the equity for each of the funds.

The firm had planned to launch the second fund as another vehicle that would acquire equity stakes in properties. But it changed its thinking last September when credit-markets dislocation was exacerbated by a banking-industry downturn, led by the bankruptcy filing of Lehman Brothers Inc.

"In September, the whole world fell apart for lenders and we saw an opportunity emerging in acquiring non-performing debt," Friedland said.

Iron Stone, which owns and manages about 500 multifamily units in the Philadelphia area, is targeting its debt fund at multifamily deals because it knows that sector the best. In addition, the multifamily sector benefits from the fact that the housing-finance agencies, Fannie Mae and Freddie Mac, are still providing debt.

The fund's strategy includes assisting borrowers of the loans it acquires to improve the collateral properties to qualify them for new financing, which could be used to fund discounted pay-offs. It will also look for agency financing for properties that it takes from borrowers.

The Iron Stone fund is in the market for agency financing for the improvements it makes to Ogontz Manor, and will later return to the agency market for permanent financing on the property.

Friedland further said that the fund is looking only for first mortgage positions because holding those positions, as opposed to junior layers or mezzanine debt, offer a more direct route to acquiring loans' underlying assets through foreclosure.

The fund is mainly interested in loans with face values of $5 million to $25 million, and would look to partner with other investors to make larger acquisitions.

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