Celebrating 30 Years of Industry Service

IREI

THE EVOLUTION OF THE INSTITUTIONAL REAL ESTATE INDUSTRY

INSTITUTIONAL REAL ESTATE, INC.

INSTITUTIONAL REAL ESTATE, INC.

A publication of Institutional Real Estate, Inc.

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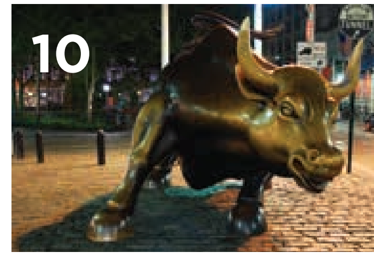

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Thanks for the **Memories**

Geoffrey Dohrmann

Thirty years ago, I was 36 years old, and working alone in the recently remodeled basement office at my home in Montclair, a suburb of Oakland, Calif. I was laboring on my new business venture, Institutional Real Estate, Inc.

At the time, I was armed with a new Macintosh Plus, which was about the size of a mix master, an Apple Laser printer, a fax machine (remember those?), a landline (ditto) and some file cabinets.

At any rate, my "business" at the time was two pronged — serving a small clientele of consulting clients in the Bay Area and Buffalo, N.Y., and working on financing the business plan for a new magazine I was planning to launch soon — *Institutional Real Estate* magazine.

It had occurred to me that the same thing was happening to the world of real estate investment that had happened to the equities and fixed income markets 20 years earlier. The ownership and management of those assets was gradually shifting from the hands of private individuals into the hands of professionals managing money for the benefit of third parties like pensions, foundations and endowment funds. In short, the business was becoming institutionalized, and, I surmised, there would be a need for a new kind of information that was less transaction-oriented, less bottom up, and more strategic, more top down.

I had assembled a small "team" to help me launch the publication — all were gainfully employed doing something else, and looking to me to give them the go signal that I had succeeded in securing funding, and it was "safe" for them to quit their jobs and come to work for me. (It always puzzled me that they argued that they couldn't afford to do what I was doing as an entrepreneur. They had mortgages to pay and families to support. Of course, I had a mortgage and a family to support at the time, too.)

At any rate, my first objective was to find us some start-up capital.

To focus my search, I had purchased a directory of venture capitalists (things like databases and the Internet were not readily available in those days). I had highlighted all of those entities that had made an investment or indicated they were willing to make an investment in publishing enterprises, and I started dialing for dollars.

As I kept dialing, I discovered that there were two kinds of VCs with publishing investment experience. The first kind — and these were the majority of the firms I called

— admitted they had invested in publishing in the past and advised me that they had concluded they would never be investing in a publishing enterprise again. The others — a handful, really — had experienced some modest success and were willing to take a look at my business plan.

When I called to follow up with the handful, most responded by asking me the same two basic questions. The first was, "Are you sure you have the right team?" And the second was, "Are you sure the market is deep enough?" (I finally figured out this was just venture capital-eeze for, "You have the wrong team, dummy," and "your market's too small.")

Of course, I did have the wrong team, and the market was too small at the time. I had estimated the entire market cap of the institutional real estate investment business at that time to be somewhere in the neighborhood of $90 billion. (To provide some perspective, today there are several firms with more assets under management than $90 billion).

I was undaunted, however, and continued calling until I finally found a VC in Chicago that was willing to take a closer look. They agreed with my basic premise and recognized a potential opportunity. So they provided me with a list of documents they needed to review, and invited me and one of my "partners" to fly out to Chicago to begin the preliminary due diligence process.

All of our resources at that point had been pretty much depleted, but we each bought the cheapest ticket we could find and hopped on the earliest flight out of SFO to Chicago the very next Monday morning.

You can imagine our concern when, as the flight started to climb out over the Sierras, the captain came on the intercom to inform the cabin that the right engine was leaking oil, and we'd have to return to the terminal for a change of equipment.

We returned and changed equipment, and finally started out again for Chicago, talking excitedly about our prospects the whole way, and arrived at O'Hare around 3 p.m. This gave us just enough time to flag a cab and hightail it to the VC's downtown offices. Where we sat. And we waited. Until it was about 6 p.m., when the gentleman we were scheduled to meet with finally appeared, with his briefcase and overcoat in hand. He obviously was all set to leave for home.

"Who are you, and who are you here to see?" he asked.

"We're here to see you," we responded.

"And who are you?" he asked again.

"We're Institutional Real Estate, Inc.," we responded.

"Oh," he said. "The startup." Then a long pause. "We're not doing startups any longer."

"Why not?" we asked, not a little bit shocked and surprised.

"Don't you know what happened today?" he asked us.

"No," we responded. "We've been on a plane all day. What happened?"

"The markets have crashed," he said. "So now we can buy companies cheaper in the secondary market than we can by starting them up."

While we had been in the air, apparently, an unprecedented drop in the market had occurred. We had been flying — unbeknownst to us — on Black Monday.

There was nothing else for us to do but — with our tails between our legs — pack up the piles of documents we had brought with us, catch a cab back to O'Hare, to catch the return flight home. Not much was said on the return flight. Several days later, my "partner" quit.

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THE INSTITUTIONAL REAL ESTATE LETTER

People

The Trouble With Real Estate

In This Issue

Despairing but refusing to give up, and after being turned down by several family members, I finally convinced our neighbor and a friend to invest a grand total of $15,000 to help start up — not the magazine I had originally planned to launch, but a slimmed down version in the form of a newsletter, which I named *The Institutional Real Estate Letter.*

I used most of the proceeds from that initial stock sale to put together a direct mail campaign (email for the masses hadn't been invented yet). I designed the flyers, walked the artwork down to the printer, waited for the print run to complete, and then, took the materials back home and hand-addressed and hand-stuffed several thousand envelopes on our kitchen table, bundled them up into zip code packets, and dropped them all off at the post office.

Then, every morning for the next two weeks, I'd go down to the mailbox and wait. And every morning for the next two weeks I'd see the same thing — bills, but no responses.

Finally, after two weeks, I got my first three orders. "It's starting," I thought to myself with some excitement.

But then the next day, nothing. Then the following day, a few more.

This continued for weeks, until I finally had no choice but to produce the first edition, mail it out to the handful of new subscribers my mailings had attracted, while mailing several thousand promo copies to a larger potential audience in hopes of snaring a few more subscriptions.

This process of produce and mail, go to the mailbox, and pick up the handful of new orders that would trickle in each week, went on for months. Finally, in desperation, I called up my mentor Larry Hull to report that, like the secretary in the movie *Ghostbusters,* "I had quit better jobs than this."

Larry assured me we were starting to make an impact, and to hang in there, which I did somehow.

Gradually we did begin to get noticed and recognized, and although the publication was about as amateurish as you could possibly imagine, the underlying thesis definitely was resonating with the markets we were serving.

Eventually, after a long process of trial and error, we hit on the idea of providing the publication on a controlled circulation (free-to-qualified basis) to our pension, foundation and endowment fund audience, underwritten by grants from members of the investment management community, whom we called "sponsors."

After many, many years as a newsletter, the publication did eventually morph into the magazine format I had originally envisioned. And, we eventually ended up publishing separate editions for investors in Europe, the Americas and the Asia Pacific region. We also started producing events, developing a database, and branched our publishing, conference and database offerings out to include coverage of the infrastructure investment space. We also developed a publication for the private wealth advisory business and launched a membership organization for investors, investment managers and their operating partners (the Institute for Real Estate Operating Companies).

Meanwhile, over the course of the past 30 years, we have witnessed and chronicled the birth of an infant business as it has grown up to become the mature investment industry that it is today.


IT TAKES A
STRONG HISTORY
TO UNDERSTAND THE
FUTURE OF REAL ESTATE
Since 1981, AEW has been a constant for its clients during the ups and downs of the global economy. We've navigated through many market cycles and have successfully provided disciplined, real estate investment solutions to the world's foremost institutional investors.
As CEO and Founder of IREI, Geoff Dohrmann also had a vision about the future of real estate. His career accomplishments and success as a thought-leader, and the ability of the IREI team to bring like-minded people together has been invaluable.
Congratulations on this tremendous 30-year milestone.
BOSTON LOS ANGELES LONDON PARIS DÜSSELDORF HONG KONG SINGAPORE SYDNEY | AEW.COM
AEW

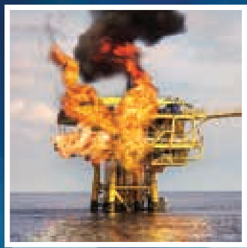
Along the way, we were assisted by far too many people to mention here. It truly took a village to get us to where we are today, and we are eternally grateful to the many individuals and companies who have helped and supported our cause along the way – mentors, staff members, editorial contributors, editorial board members, advertisers, publication sponsors, consulting clients, database subscribers, conference attendees and conference sponsors.

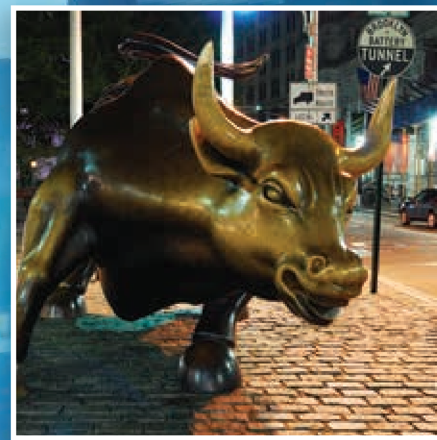
A business like ours exists solely because people like our readers and our sponsors and other customers have needs that we can fill. We exist, in other words, at your disposal and with your permission – in order to serve you.

We will be eternally grateful for all of you who have made our business possible, and for the guidance you have provided and the incredible support you have shown us for the past 30 years.

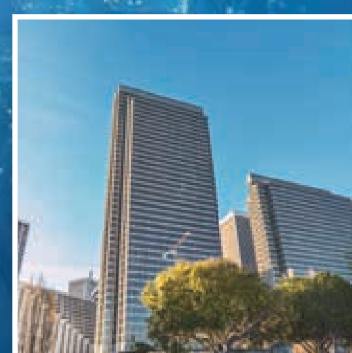
In the meantime, one thing hasn't changed. As always, it's important to be careful. Be very, very careful. It's a whacky world out there. Now, more so than ever.

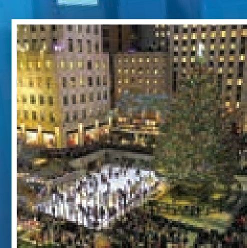
Geoffrey Dohrmann
President & CEO
Institutional Real Estate, Inc.





EVOLUTION





Rising from the Ashes ... **In the Beginning**

Flashback to the first decade of real estate's institutionalization

By Loretta Clodfelter

Would a contemporary investor even recognize the institutional real estate market of 30 years ago? The size of the market would be much smaller, and the technology would seem positively archaic. No smartphones. No World Wide Web. Instead, investors could purchase listings of the latest RTC inventory "in 5-1/4" floppy disk form in ASCII format using an IBM-compatible PC with high-density drives."

But the themes and concerns of institutional investors and investment managers might sound more familiar than not. The lead story in the January 1990 issue of *The Institutional Real Estate Letter* notes, "Today, as we enter the 1990s, co-investment appears to be emerging as the next hot investment vehicle."

And real estate investors were working to define which investments should be classified as real estate, and which should not. Were REITs real estate? Were commercial mortgages real

1987

Oct. 19, 1987
Black Monday — stock markets around the world crash, with Dow Jones Industrial Average falling 508 points — 22.6%

1989

Resolution Trust Corp. is established to unwind assets from insolvent savings and loan institutions

"Trophy properties may look nice on the cover of your beautiful brochure, but they've become the booby prize in today's real estate investment market."
*— **Stephen Steppe**, RREEF (1989)*

Mitsubishi Estates buys an 80% equity interest in the Rockefeller Center REIT for $1.4 billion

Oct. 13, 1989
Dow Jones Industrial Average drops 190 points in what becomes known as the Black Friday mini-crash

Nov. 9, 1989
The fall of the Berlin Wall

"There's also the problem of letting success go to your head. Too often you see a firm that's been successful in raising capital, and all of a sudden, they think they have all of the answers. They evolve into organizations of arrogance."
*— **John Koza**, Frank Russell Co. (1990)*

1990

July 1990–March 1991
U.S. experiences recession

"Germany could be the meeting place between East and West. A meeting place, not of conflict, but of collaboration."
*— **Richard Plummer**, MIM (1990)*

"Charging Bull" sculpture in Lower Manhattan, signaling the new era of real estate securitization and sophistication, as real estate goes to Wall Street

estate? (Has this debate been truly settled, even now?)

TROUBLED IN THE START

The early 1990s were an era of increasing institutionalization and securitization, of sophistication and globalization for the real estate industry. The wall had just fallen in Berlin, and new opportunities for investment in Central and Eastern Europe were arising.

But commercial real estate was also struggling with an oversupply problem. Excess development in the late 1980s had led to skyrocketing vacancies in the early 1990s, creating challenges for investors. By 1991, rents were falling and new construction had "ground to a screeching halt." With wide spreads between bids and asks, property transaction activity slowed to a trickle.

In addition, the Resolution Trust Corp. had been created in the wake of the Savings & Loan crisis, and it began selling assets at the beginning of the decade. The U.S. economy had slipped into recession, and it seemed as if only distressed assets were priced to sell.

As commercial real estate performance suffered in the early part of the decade, investors started lining up to exit from commingled funds. In the case of open-end real estate funds, exit queues in 1992 of $2 billion to $4 billion represented nearly 20 percent of their equity investment capital. Meanwhile, closed-end property funds were facing a bloodbath

"The broad category of real estate won't show a favorable appreciation component for a number of years, unless you happen to be talking about a takeover or workout situation. In the normal course of events, the overabundance of supply will not allow rents to inflate with the rest of the economy."
*— **Paul McEvoy**, Dreyfus Realty Advisors (1990)*

"The investment community thinks in straight lines. When the market is going up, it thinks it will go up forever. When the market is going down, it thinks it will go down forever."
*— **Michael Falker**, Cambridge Realty Partners (1991)*

"Real estate was promoted as an investment that always goes up in value. That gave rise to the notion that it had low volatility. Given the industry collapse in the past couple of years, one of the main reasons to invest in real estate — its low volatility — has gone away."
*— **Paul Saint-Pierre**, Kenneth Leventhal & Co. (1992)*

1991

"The fee structure needs to be tied to what the manager is doing and to what type of risk the deal is associated with."
*— **Sylvia Ferrell-Jones**, State of Connecticut Trust Funds (1991)*

Dec. 31, 1991
NCREIF Property Index records an annual total return of –5.59%, its worst of the decade

"Retrospectively, the advisers and plan sponsors set a bad date when they started the closed-end funds. They didn't know it at the time, but they are now being forced into sales at the end of the most expansive real estate boom in centuries."
*— **Blake Eagle**, Frank Russell Co. (1992)*

1992

June 3, 1992
IBM reports $4.97 billion loss for 1992, largest annual loss in America corporate history

1993

Feb. 26, 1993
A truck bomb detonates below the World Trade Center, killing six people and injuring thousands

"The various property types all have pluses and minuses, but I don't see any pluses in the CBD class A office building today — to my mind, the trophy office building today is all minuses. Some cities are going to win, and some won't. Cities where people still live downtown — midtown New York, for example, or Denver — they have a chance. But cities like Atlanta, Houston and Los Angeles are in trouble."
*— **Mike Miles**, Prudential Realty Group (1993)*

November 1993
Mark Jorgenson, a portfolio manager with Prudential, files a lawsuit alleging his employer had inflated the values of some of the properties in the PRISA open-end fund, systematically defrauding institutional investors

Dec. 13, 1993
Simon Property Group raises $840 billion in an initial public offering

as they reached the end of their scheduled life, with funds forced to liquidate assets at what seemed to be the worst possible time.

Commercial real estate buyers, though, were starting to get into a stronger position, and institutional investors began acquiring distressed real estate packages. In 1992, the Illinois Teachers' Retirement System (total assets at the time: $11 billion) acquired a $500 million distressed real estate loan package through adviser LPC Realty, an affiliate of Dallas-based Lincoln Property Co. And other pension plans were looking to do similar deals.

The 1990s also were an era of continued suburbanization, and many investors worried about their CBD office holdings as U.S. businesses relocated to suburban office parks. But if CBD office was a dog's breakfast, regional malls were unstoppable.

RISE OF THE REITS

In the middle of the decade, REITs began to come into their own as an institutional investment opportunity. Prior to the Omnibus Budget Reconciliation Act of 1993, REITs were prohibited from having five or fewer individuals own more than 50 percent of their stock, which meant a pension fund could not hold more than 10 percent of a REIT's outstanding shares. But the August 1993 passage of OBRA relaxed those rules, so a pension fund did not represent a single entity but all the individuals benefiting from that pension fund.

Sam Zell, "The Grave Dancer," launched three REITs in the 1990s: Equity Residential, Equity Office Properties Trust and Equity Lifestyle Properties.

By making it easier for pension funds to own REIT shares, OBRA also created an opportunity for sponsors of commingled real estate funds to convert into REITs, creating an exit strategy for many of the pooled funds raised in the first half of the decade. In 1993, 46 REITs went public with initial public offerings raising $8.5 billion, with nearly half of the offerings in the final quarter of the year. Another 43 REITs went public in 1994, raising $6.7 billion with their IPOs. Many of those companies have gone on to become some of the biggest REITs in the market today: Equity Residential, General Growth Properties, Simon Property Group and Vornado Realty Trust in 1993; Prologis and AvalonBay Communities in 1994.

The rise of REITs came at a moment when private open-end funds had received a black eye. Mark Jorgensen, a former portfolio manager at Prudential, filed a lawsuit in 1993 alleging the

1994

Jan 1, 1994
OBRA goes into effect, making it easier for pension plans to own REITs

"We're getting calls every day from pension plans trying to make up their minds about REITs."
*— **Michael Oliver**, PRA Securities Advisors (1994)*

April 1994
Prudential settles with whistle-blower Mark Jorgensen, and apologizes to its clients regarding PRISA valuations

October 1994
Heitman acquires JMB Institutional Realty Corp. for more than $200 million

December 1994
Equitable Real Estate is the largest U.S. real estate manager, with tax-exempt real estate assets under management of more than $10 billion

"Last year, the REIT industry raised $17 billion. The real estate industry is $3 trillion big. There's plenty of room to grow. REITs will be the growth industry of the Nineties."
*— **Burland East**, Kemper Securities (1994)*

values of some of the properties in the PRISA open-end fund — which first launched in 1970 — had been inflated. The Jorgensen case raised significant issues and prompted an industrywide self-examination regarding appraisal valuations. Prudential settled with Jorgensen in 1994, writing a formal statement of policy for its employees and a formal letter of apology to its clients. Despite the challenges, Prudential raised an additional $400 million in 1994 and ended the year as the second-largest U.S. real estate manager, with tax-exempt real estate assets under management of $6 billion, behind only Equitable Real Estate, which had tax-exempt real estate assets under management of more than $10 billion.

On the economic front, 1994 also saw an economic recovery, with robust job formation and a stunning 7 percent GDP growth in the first quarter. The real estate industry also saw a strong recovery, though rising interest rates held some of the frothiest exuberance in check.

In the middle of the decade, one big question was whether and how the SEC should be regulating private funds, including private real estate funds. By the end of 1995, real estate investment advisers managing more than $200 billion in client assets had voluntarily registered with the SEC under the Investment Advisers Act. In October 1996, The Investment Advisers Supervision Coordination Act was passed and went into effect in July 1997, splitting registration and oversight responsibilities for investment advisers between state and federal regulators. This put real estate consultants and smaller real estate investors at risk, as federal registration under the Investment Advisers Act was used to meet the ERISA definition of an investment manager (though ERISA was amended as part of the 1996 act to allow the definition of an investment manager to include registration under state law). This also meant smaller investors had to register in every state in which they did business.

PLAYING SECOND FIDDLE

Although the real estate industry was maturing in the latter half of the decade, some questioned whether a stock market boom had relegated real estate to second-class status. U.S. equities outperformed in 1995 to 1999, driven by a bubble in the first wave of Internet stocks. The Nasdaq Composite Index closed

The Nasdaq Composite Index closes above 1,000 points for the first time

July 17, 1995

1995

"Investment capital does not have a conscience. In today's global economy it will chase an eighth of a basis point around the globe on a 24-hour basis."
*— **Charlie Wurtzebach**, Heitman/JMB Advisory Corp. (1995)*

CalPERS grows to more than $100 billion in total assets under management.

1996

March 26, 1996
Simon Property Group agrees to acquire DeBartolo Realty Corp. in a $3 billion deal

"When you play in the opportunistic world, liquidity isn't always what you want. When there is lack of liquidity, there is also opportunity to buy in at a lower price, if people are willing to let go of the properties. You can always get liquidity by selling to someone at a significantly reduced price."
*— **Richard Brace**, AMRESCO Advisors, Inc. (1996)*

1997

Boston Properties raises $903 million in an initial public offering

June 17, 1997

May 1997
Lend Lease agrees to acquire Equitable Real Estate for $400 million

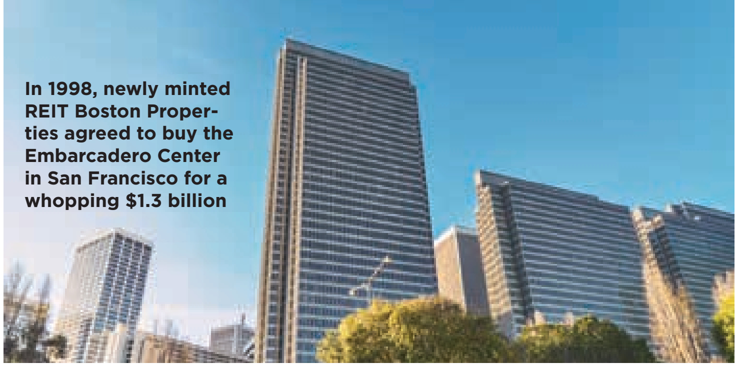
"You can't obtain incremental returns without taking on incremental risks."
*— **Nori Gerardo**, Pension Consulting Alliance (1996)*

July 1997
Asian Financial Crisis starts in Thailand and spreads throughout the region, raising concerns of global contagion

"We should not make the classic error of assuming every tomorrow will be exactly like today."
*— **Anthony Downs**, Brookings Institute (1997)*

RoProperty, a subsidiary of Netherlands-based Rodamco, acquires RREEF from its management

1998



In 1998, newly minted REIT Boston Properties agreed to buy the Embarcadero Center in San Francisco for a whopping $1.3 billion

"Everyone knows that the aging of the baby boomers and the slower growth in the labor supply will create new and different investment opportunities; however, few agree on what those opportunities will be."

*— **Steve Coyle**, Property & Portfolio Research (1999)*

"Everyone's more than happy to tell you they're Y2K compliant, but you can't get anyone to take that next step and give you a warranty or an indemnity. Some things will work; some won't. I've lived through hurricanes. I've lived through earthquakes. I think we'll live through this, too."

*— **Wayne Pryor**, RREEF (1998)*

Dec. 31, 1998

NCREIF Property Index records an annual total return of 16.24%, its best of the decade

"When you are striving for higher returns, you have got to guard against the associated risks, and the best way to guard against risk is to have the daily decision-makers' own money in the transaction, from the leading person to the analyst."

*— **Neil Bluhm**, Walton Street Capital (1999)*

1999

CalPERS reaches $150 billion in assets under management

above 1,000 points for the first time in 1995, doubled by 1998, and doubled again by the end of 1999, closing the year at 4,069 points.

The Internet was the hottest thing going in the late 1990s, as the advent of the World Wide Web dramatically changed information technology and telecommunications. Suddenly, everyone wanted to buy the latest dot-com stocks and own a piece of the action. (And, just as suddenly, everyone wanted to know if their investment adviser was Y2K compliant.) Investment advisers and pension funds began to need to have their own website.

A second round of REIT IPO activity also took off in 1997, with 26 companies going public and raising $6.3 billion, including Boston Properties, Equity Office Properties Trust (later acquired by Blackstone) and AMB Property Corp. (later merged with Prologis). By the end of the year, the equity REIT market capitalization was $128 billion (up from only $10 billion in 1992).

REITs became the dominant real estate buyer type, acquiring more properties than pension fund advisers in 1996 and 1997. Which is not to say pension funds weren't working hard to get the money out! The booming equities market meant institutional investors needed to keep upping their real estate investment dollars just to keep pace with a 5 percent or 10 percent allocation to the asset class. That emphasis on getting the money out meant, by 1998, it was becoming apparent discipline was beginning to slip.

MERGERS AND ACQUISITIONS

Industry consolidation was also the news of the day. In 1996, TA Associates acquired Aetna Realty Advisors, which had $3.7 billion in tax-exempt real estate assets under management, and New England Investment Companies acquired Aldrich Eastman Waltch, consolidating the firm with its existing real estate advisory firm, Copley Real Estate Advisors, into AEW Capital Management, with a combined $7.6 billion in real estate assets under management. At the end of the year, Trammell Crow sold its real estate advisory business, Trammell Crow Realty Advisors Unit, with a net asset value of commingled funds and separate accounts of $1.2 billion, to Sarofim Realty Advisors.

In 1997, Australia-based Lend Lease Corp. acquired Equitable Real Estate Investment Management and merged it with its U.S.-based real estate investment management firm, The Yarmouth Group; initially, the firm was known as ERE/Yarmouth. In 1998, a subsidiary of Netherlands-based Rodamco NV acquired RREEF, creating a firm with combined assets under management of nearly $20 billion, while LaSalle Partners merged with Jones Lang Wootton; the combined firm, Jones Lang LaSalle, had more than $20 billion in assets under management. And in 1999, UBS Brinson acquired Allegis Realty Investors, which had $5.9 billion in real estate assets under management.

And the late 1990s also saw the resurgence of CBD office, as pension fund investors began to shift their emphasis from suburban to downtown office properties. Suburban office vacancies were rising by 1998, fueled by new construction.

There were some who raised the alarm about the health of real estate opportunity funds at the end of the decade. By 1999, opportunity funds had surpassed REITs as active buyers, and they appeared to be taking on greater risks (development, foreign investment, high leverage) to deliver lower returns.

Loretta Clodfelter is the editor of *Institutional Real Estate Americas.*

By Larry Gray

Boom and Bust ... Fear and Greed ... **Repeat**

Decade produces short recession, tall midget, big trouble

Seasoned investors know there are business cycles and there are real estate cycles. Ebbs and flows, ups and downs, twists and turns. In the years 2000–2009, institutional investors saw it all ... and more.

NEW CENTURY, SHAKY START

The world celebrated the dawning of a new century as clocks struck midnight and the calendar rolled over to Jan. 1, 2000. Many also breathed a sigh of relief, as the media-hyped Y2K bug *did not* send the global population into digital dysfunction and chaos. Computers and computer networks did not crash, power grids *did not* go dark, and planes *did not* fall out of the sky. In the end, New Year's revelers *did not* have anything to fear ... except a possible hangover from the night before.

Unfortunately, the glad tidings were short lived.

In March 2000, the air started to leak out of the dot-com bubble that had been forming over the past several years. The

2000

March 2000
Start of the dot-com stock market crash; eventually results in the Nasdaq Composite losing 78% of its value

2001

U.S. experiences brief recession (8 months)

"I've often described going as a plan sponsor to a PREA meeting as like going to a dog convention with a pork chop around your neck. People think if they can get in front of you, you'll give them money."
*— **Guy Jaquier**, AMB Property Corp. (formerly with CalPERS) (2001)*

July 2, 2001
Equity Office Properties acquires Spieker Properties for $7.2 billion

Sept. 11, 2001
Terrorist attacks on the United States includes World Trade Center complex in New York City; attacks killed 2,977 people and injured more than 6,000 others

"At the beginning of the year, we were anticipating accelerating demand for real estate and for REITs, but the surprise has been the extent to which that prediction has come true."
*— **James Corl**, Cohen & Steers (2004)*

2003

Alan Greenspan

June 26, 2003
Federal Reserve lowers key interest rate to 1%, the lowest level since 1958, marking the 13th rate cut since the beginning of 2001

The year 2000 kicked off the new millennium and a decade of highs and lows for institutional real estate investors.

NASDAQ Composite stock market index, which includes many of the largest tech firms, grew from around 1,000 in 1995 to more than 5,000 in 2000. It was a time when new tech start-ups were being announced every week, investor speculation ran rampant, tech companies that had never turned a profit were going to market with IPOs and attracting lots of attention and huge prices, with stock prices sometimes doubling on the first day of trading. But then in March, values began to collapse as it became clear "the emperor had no clothes." By the fall of 2002, the NASDAQ had lost 78 percent of its value.

As the tech market plummeted, along with investor and consumer confidence, the United States sank into a mild recession. And the stock market entered one of the most ferocious bear markets in history; the S&P 500 Index posted total returns of -9.10 percent, -11.89 percent and -22.10 percent in 2000, 2001 and 2002, respectively.

It was a rough start to the new century and new decade for the economy and financial markets. One bright spot, however, was real estate, the one asset class that is usually "a rock" for investors during times of uncertainty and turmoil. Indeed, during the three-year period from 2000–2003, the NCREIF Property Index (NPI) recorded total returns of 12.24 percent, 7.28 percent and 6.74 percent, respectively. However, the problem for many institutional investors during this period was that at a time when real estate was providing the strongest returns, the denominator effect caused by the falling stock market forced investors to *cut back* their real estate investments.

But the collapse of the tech market in 2000 did have a silver lining, at least for commercial — and residential — real estate investors. To resuscitate the sluggish economy and restore investor confidence, the Federal Reserve began lowering interest rates in early 2001. After slashing rates 13 times, the key interest rate had been reduced to 1 percent by June 2003, the lowest level since 1958. Real estate investors love the arbitrage opportunity presented by low interest rates. In addition, the light bulb went on for many institutional investors, who were realizing they needed to increase their allocations to the real estate asset class so that it could have more of an impact on the portfolio as a diversifier and income producer.

"The permanent shift is that real estate is now part of the larger capital markets. It will always be priced and valued with respect to alternatives. I expect allocations to real estate to evolve to the 10 percent level over the coming 10 years — a big leap from the 4 percent average in pension funds today."
*— **Susan Hudson-Wilson**, Property & Portfolio Research (2004)*

"Who would have thought that things would have changed so much since the early 1990s, when most investors said, 'I don't want to talk to a real estate guy ever again'?"
*— **Michael Torres**, Adelante Capital Management (2005)*

2004

U.S. homeownership rate peaks at all-time high of 69.2%

2005

NCREIF Property Index (NPI) records second-highest annual total return in its history, 20.06%

"The biggest mistake you could have made in real estate in the past four years was simply that you did not buy."
*— **Joseph Robert Jr.**, J.E. Robert Companies (2005)*

2006

Pension funds such as CalPERS, CalSTRS, SWIB and PSERS report real estate returns in excess of 30%

2007

CMBS new issuance in the United States hits a record $228.6 billion

"Thus, everything else being equal, the bigger the boom — the greater the excesses of the capital markets in the upward direction — the greater the bust. Timing and extent are never predictable, but the occurrence of cycles is the closest thing I know to inevitable. And usually, the air goes out of the balloon a lot faster than it goes in."

*— **Howard Marks**, Oaktree Capital Management (2007)*

Subprime mortgage crisis — more than 25 subprime lenders declare bankruptcy — fuels the collapse of the U.S. housing bubble, and contributes to the global financial crisis

"We are facing a financial crisis as profound as any we have faced since the Great Depression. As a result, your jobs, your savings and your economic security are now at risk. This week, we must work quickly, in a bipartisan fashion, to resolve the crisis and avert an even broader economic catastrophe."

*— **Sen. Barack Obama**, D-Ill. (speaking at a rally in New York City, Sept. 17, 2007)*

July 2007

The Blackstone Group acquires Hilton Hotels for $26 billion

"The market is going back to a time when you had to earn your money. The past three years, it has been a momentum rather than a value market. Cap rate compression has not only topped out, it's now going in the other direction."

*— **Jerry O'Connor**, O'Connor Capital Partners (December 2007)*

GRAVY TRAIN

Fueled by low interest rates, the economy roared back — annual GDP was above 6 percent in the three years from 2003 through 2005 — as did space demand in the commercial real estate markets. In fact, the four-year period 2004–2007 was a "heyday" of sorts for institutional real estate investors and investment managers.

Prior to this period, the philosophy on real estate of many institutional investors, after being burned by real estate investments in the early 1990s, was "Never again."

But the industry had learned some lessons along the way — improved fund and fee structures as well as greater transparency and alignment of interests — and the asset class slowly edged its way back into investors' favor. In the early 2000s as the stock market suffered volatility and poor performance, real estate performed admirably, generating income and producing solid, stable returns. Industry pundits rewarded real estate with the moniker of "tallest midget in the circus," referring to the fact that it offered a relatively higher yield than other assets in a yield-starved environment.

The asset class really started to put on a show mid-decade. In the period 2005–2007, the NPI registered returns of 20.06 percent, 16.59 percent and 15.84 percent, and keep in mind these are *unleveraged* returns. The REIT market was also going gangbusters during the years 2003 through 2006, producing eye-popping returns of 37.13 percent, 31.58 percent, 12.16 percent and 35.06 percent, respectively. Real estate, the former "midget," started to look more like the circus strong man.

For the fiscal year ended June 30, 2006, for example, Pennsylvania Public School Employees Retirement System and the State of Wisconsin Investment Board reported real estate portfolio returns of 38.6 percent and 38.5 percent, respectively. CalPERS' real estate portfolio produced a return of 38.4 percent, and CalSTRS weighed in at 35.7 percent.

During this period, real estate really "earned its place at the table" and the asset class grew in size and sophistication. Real estate's strong performance attracted new investors, promoted higher allocations and produced a vibrant transaction market. The tidal wave of capital lifted property prices and compressed cap rates.

During this time, investors' appetites expanded from a strict diet of core properties to a smorgasbord of offerings across equity and debt, public and private. They invested in joint ventures, funds of funds, global funds, debt and niche property types. The globalization of the asset class was evident; for 2006, Jones Lang LaSalle reported cross-border investment represented 44 percent of total transaction volume.

Things were going great, everyone was making money … until the proverbial shit hit the fan in 2007 in the form of the subprime mortgage meltdown, which eventually resulted in a financial markets death spiral, otherwise known as the global financial crisis.

APOCALYPSE NOW

2007 was indeed a market inflection point. After a lightning fast start to the year, real estate's momentum game ground to an abrupt halt, the music stopped and investors were scurrying for chairs. In a matter of months, investment sentiment did a complete reversal from too much greed to too much fear.

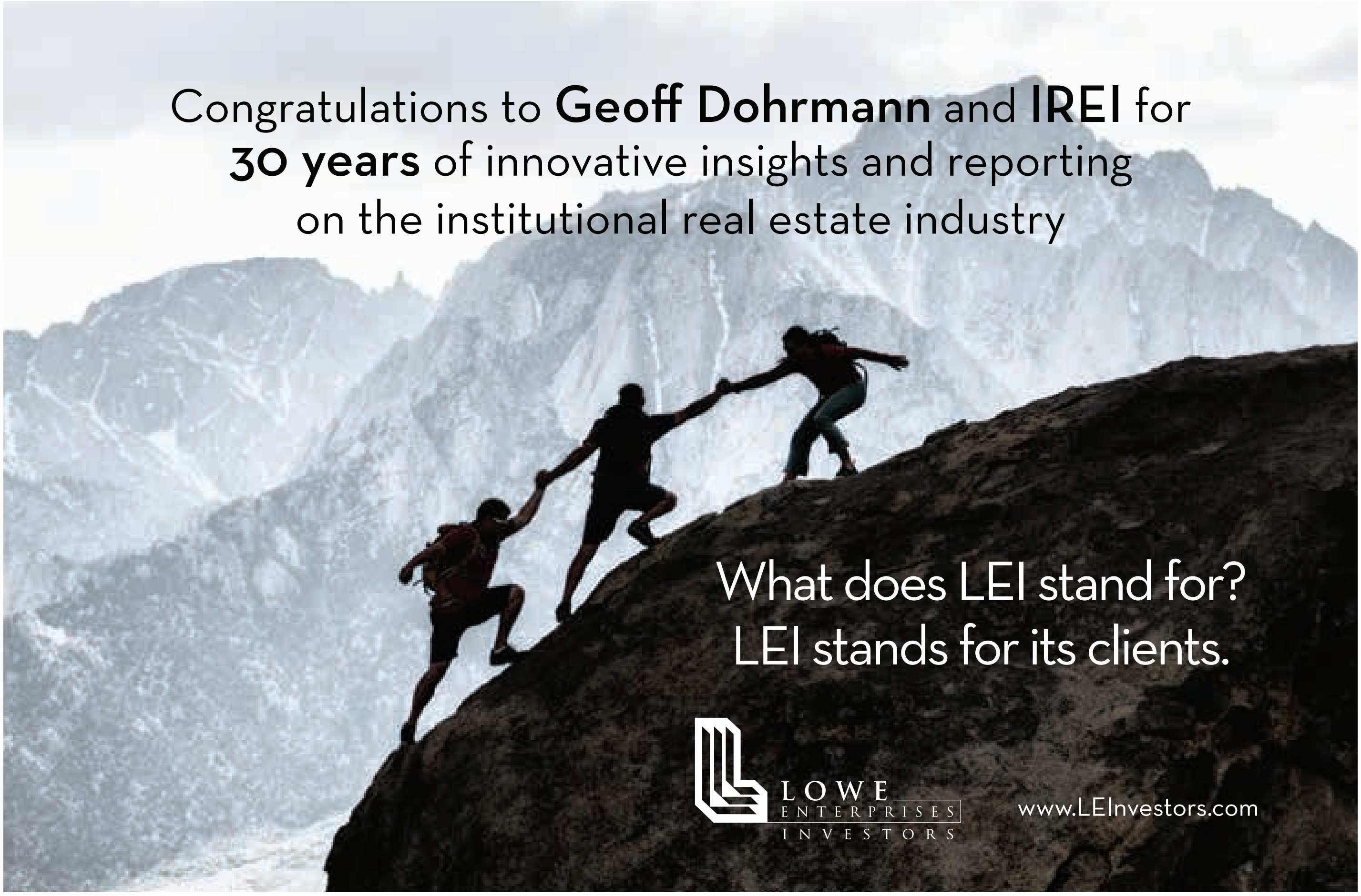
The subprime mortgage implosion in the residential sector started the snowball rolling, but the real problem that made the snowball so big was the overleveraged capital markets and the overleveraged banking system. Wall Street investment banks were faced with the prospect of billions of dollars of write-downs due to bad mortgage debt.

How bad was it?

At an emergency cabinet meeting in September 2008, referring to the U.S. financial system, President George W. Bush summed things up pretty well when he exclaimed, "If money isn't loosened up, this sucker could go down."

Years later in a 2014 court document, former Federal Reserve Chairman Ben Bernanke was quoted as saying, "September and October of 2008 was the worst financial crisis in global history, including the Great Depression." He added that of the 13 "most important financial institutions in the United States, 12 were at risk of failure within a period of a week or two."

When Lehman Brothers declared bankruptcy in September 2008, it compounded the panic in the financial markets. On Sept. 29, after Congress rejected a $700 billion



Congratulations to Geoff Dohrmann and IREI for
30 years of innovative insights and reporting
on the institutional real estate industry
What does LEI stand for?
LEI stands for its clients.
LOWE
ENTERPRISES
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"There's a lot of fear out there. Normally markets are driven by fear and greed. Now it's fear and fear."
*— **Brian Gendreau,** ING Investment Management (2008)*

Start of the Great Recession *(officially from December 2007 – June 2009)*

2008

Private equity real estate fund sponsors raise a record $134.9 billion

Real Capital Analytics announces worldwide acquisitions of commercial property surpasses $1 trillion in 2007, a record figure

REIT market slump: Equity REITs post record worst annual return of –37.73%, equity REIT market cap falls to $176 billion.

Wall Street rescue plan, the Dow Jones Industrial Average plummeted 778 points, its largest one-day drop ever.

Because of the complex chain of debt between counterparties, there was a real possibility of a domino effect of bank failures. Governments around the world had to act quickly to stem the tide. And they did, crafting massive rescue plans that included direct equity infusions, comprehensive fiscal stimulus packages and highly accommodative monetary policy.

The subprime mortgage crisis sent the U.S. residential market into a tailspin, and subsequent contagion caused commercial real estate capital markets and investors around the globe to move to the sidelines to reassess and reprice risk.

In the face of global financial market turmoil, property values crumbled, credit evaporated and the economic recession that came on the heels of the credit crisis put investors into a full-out defensive mentality.

During October 2008, following a series of government-sponsored bank bailouts, REIT prices declined 30 percent, amounting to a 47 percent drop from the market peak in February 2007. Property values and portfolios values were being written down as much as 30 percent to 40 percent. Although seasoned real estate investors had seen market downturns before, they had never seen anything like this.

INTO THE UNKNOWN

Institutional real estate investors enjoyed a nice run during the first decade of the new millennium ... at least until the global financial crisis sent financial markets reeling. Given the market turmoil and tremendous uncertainty regarding the depth of the recession and the outlook for recovery, 2008 and 2009 was a time of asset repricing, deleveraging and heightened caution for institutional investors.

In March 2009, Normandy Real Estate Partners and Five Mile Capital Partners acquired The John Hancock Tower in Boston for $660.6 million — nearly half the price paid by Broadway Partners in 2006 — at a foreclosure auction. In December 2010, Normandy and Five Mile sold the 62-story skyscraper to Boston Properties for $930 million.

However, despite its adverse effects, market volatility also creates buying opportunities, especially for savvy, opportunistic investors in commercial real estate.

In an April 2009 article, industry veteran Joe Azrack summed up the current market environment: "It's important to bear in mind that this is not your run of the mill recession, and one needs to be prepared for an extended financial and economic cycle compared to previous recessionary experiences. It is also true that the near-term adversity will yield eventually to what should be the mother of all buying opportunities."

Larry Gray is vice president, editorial director of Institutional Real Estate, Inc.

Sept. 15, 2008
Not "too big to fail"; Lehman Bros. investment bank files for bankruptcy, triggering a panic in global financial markets

Sept. 29, 2008
Congress rejects $700 billion Wall Street rescue plan; DJIA falls 778 points, its largest one-day point drop ever

Oct. 3, 2008
Congress passes a revised version of the Troubled Asset Relief Program (TARP)

"Real estate throughout history has been the investment of choice in the midst of any crisis."
*— **Thomas Barrack**, Colony Capital (2009)*

2009

Foreclosures filed on nearly 2.9 million single-family properties during the year

HEITMAN

Five Decades

INVESTING FORWARD

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By Mike Consol

2010–PRESENT

On the Comeback Trail

It began with core investing in gateway markets, then got stronger when the foreign capital started to flow

The U.S. economy entered the second decade of the new millennium with serious questions about its ability to resuscitate from the most devastating economic collapse since The Great Depression. Now widely referred to as The Great Recession, between December 2007 and January 2009 billions of dollars in government funds were used to bail out and buttress the country's largest banks and other critical financial institutions, and the Federal Reserve Bank continued furiously printing American currency (so-called quantitative easing) in an effort to stimulate the economy and restore trillions of dollars in lost asset value — much of it from real estate holdings.

Fortunately, it did not take long for the telltale questions to get answered, as the institutional real estate business hit the comeback trail in 2010, shaking off the economic and financial market turmoil of 2008 and 2009 with real estate assets posting a total return of 13.1 percent during 2010, and annual double-digit returns through the first half of the decade. Indeed, from 2010 through 2016, annual returns averaged 11.7 percent, according to tabulations supplied by the NCREIF Property Index. As of this writing, annual real estate returns for the 12-month period ending June 30, 2017, was 7.0 percent, indicating the industry's recovery was still in progress but slowing.

2010

Greece economy goes bust

April 20, 2010
BP Deepwater Horizon oil spill in the Gulf of Mexico

July 21, 2010
The Dodd-Frank financial reform bill enacted by Congress

"I'm supposedly the grave dancer, so everybody comes and talks to me and says, 'Well, when are the opportunities going to come up?' I answer them by saying that you don't have opportunities unless there is volume, and there is no volume."
*— **Sam Zell**, Equity Group Investments (2010)*

2011

Occupy Wall Street movement swarms the New York City financial district

BRIGHT LIGHTS, BIG CITIES

Not surprisingly, the road back for commercial real estate was led by core property investing in the country's gateway markets, chiefly New York City and San Francisco, in what was labeled a "flight to quality." But the revival quickly fanned out to other first-tier markets, and the definition of what qualified as a core investment gradually broadened as investors and managers became more convinced of the recovery's durability. That further encouraged them to also begin devoting modest sums to niche property types such as student housing, senior housing, medical office and self-storage facilities.

Overall, transaction activity accelerated substantially in 2010 as debt markets opened up and the attractive yield offered by the real estate asset class lured both traditional and nontraditional investors to the market. The activity, however, was concentrated on top-quality core properties located in a few select metros, primarily 24-hour gateway cities with economic fortitude. This flight to quality produced a spike in prices in these prime markets and a widening pricing divide based on asset quality and location.

That is not to say investors and managers had overcome all timidity. The annual plan sponsor survey produced by Institutional Real Estate, Inc. indicated that new commitments by pension funds to real estate were still somewhat muted in 2012 due to a variety of inhibiting factors, including domestic and global political and financial market uncertainty, limited liquidity in the debt capital marketplace and the transaction marketplace, and a narrowing gap between target real estate allocations and actual allocations. What's more, some $68 billion in uncalled capital had piled up, down from a whopping $89 billion the previous year, a surreal amount of money just sitting and waiting for the right opportunities. Then again, there has always been uncalled capital, and there always will be, as managers reserve "dry powder" to strike when the situation is opportune. Despite some residual hesitancy, the annual plan sponsor survey concluded that real estate commitments would see a 17 percent increase in 2012. Some of that capital

"When everyone is running for core, you should be running away."
*— **Barry Sternlicht**, Starwood Capital Group (2011)*

March 11, 2011
Japan earthquake and tsunami

Aug. 5, 2011
Standard & Poor's strips United States of top credit rating

Oct. 5, 2011
Steve Jobs, Apple founder, dies

The Arab Spring topples several Middle East governments

A handful of investment managers started ramping up and designing programs for single-family rentals — including players such as Apollo Global, Blackstone, Colony Capital and Starwood Capital Group.

2012

The LIBOR rate scandal

Gas prices soar to an average of $3.60 per gallon

"The banking sector has not yet returned to 'normal' despite two years of earnings growth. With increased regulation and the temptation for banks to take additional risks in order to preserve margins, 2012 should be a very interesting year."
— ***Matt Anderson**, Trepp LLC (2012)*

October 2012
Hurricane Sandy causes billions in damages along East Coast

started migrating to secondary and tertiary markets, as evidenced by an uptick in transaction activity in those markets and signaling the start of a broader recovery in commercial real estate.

GOING HOME

Among the other opportunities that grabbed the attention of some institutional investors was the single-family housing wreckage of 2008–2009. After housing prices deflated by nearly 14 percent during 2008, scads of homes were foreclosed on and left vacant. Considerable institutional capital started targeting the budding business of operating foreclosed single-family homes as rental properties. A handful of investment managers started ramping up and designing programs to take advantage of the distress in the single-family housing market — including players such as Apollo Global, Blackstone, Colony Capital and Starwood Capital Group. Naysayers argued that single-family rentals were too maintenance-intensive to scale and make profitable. Proponents asserted that naysayers argued much the same years prior about multifamily housing, only to see apartments become a new real estate asset class — and the same might come to pass for the single-family rental market.

The timing was fortuitous, because by the start of 2013 a fledgling rebound in the single-family housing market was under way, and the total value of the United States' housing stock hit an all-time high of $29.6 trillion in 2016, according to Zillow. Not bad for a housing market whose cumulative value plummeted by $6.4 trillion from 2006 to 2012 during the housing market's collapse.

On the debt side of the ledger, commercial mortgage-backed securities (CMBS) were striving for a comeback in 2012, but a steady stream of troubled assets from past issuances kept falling into foreclosures. Things would slowly get better for the CMBS market, as its delinquency rate shrank to 5.49 percent in July 2017, according to Trepp, a vast departure from its all-time high delinquency rate of 10.34 percent in July 2012.

2013

Edward Snowden leaks trove of U.S. intelligence secrets

"Our business is a very data-rich environment, so we can do things like compare the performance of our tenants' operations and our expenses across properties and locations. Being able to identify best practices and apply them quickly makes a major difference."
— ***Steve Sterrett**, Simon Property Group (2013)*

Oct. 1, 2013
Jeff Bezos buys *The Washington Post*

"Consolidation is a negative for investors. Big investment firms have to push vast sums of money out the door quickly, and that changes the way they invest."
— ***Scott McArtor**, Hawkeye Partners (2013)*


CBRE Global Investors congratulates Geoff Dohrmann and his team at Institutional Real Estate, Inc.
on 30 years of outstanding performance in the industry.
PERFORMANCE.
The pursuit of world-class performance requires intense focus. For more than 40 years, we have been solely focused on real assets as part of the world's largest real estate platform. Through our deep, global experience, we have learned that performance is achievable through constant innovation, active management and understanding the risks ahead. But above all, we believe performance is achieved by putting the investor first.
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INDUSTRY CONSOLIDATION

As the real estate investment business recovered and pension funds and other institutional investors boosted their commitments, a small number of huge investment managers started to dominate the business. Consider that by 2013 the 10 largest managers controlled 36 percent of total real estate investment dollars, or $682 billion, according to research conducted by Institutional Real Estate, Inc.'s data services department and Property Funds Research. To put that in perspective, the top 20 firms collectively controlled more assets under management than the next 100-plus firms combined. It was not the first time the industry consolidated in such a significant way. IREI founder and CEO Geoffrey Dohrmann pointed out that between 1990 and 2000, 48 of IREI's sponsoring firms shrank to 13 because of mergers that consolidated the industry.

"So this is a process that's been going on for a long time," Dohrmann said.

But perhaps never with such ferocity. Consider that in 2003 a real estate investment manager with $20 billion in assets under management would have ranked among the largest firms in the industry. By 2013, $20 billion worth of business would not have managed to land your company among the top 20.

While the majors are feeding off larger and larger platters – Blackstone raised a record $13.3 billion for its Blackstone Real Estate Partners VII last year, and Brookfield Asset Management raised $4.4 billion for its Brookfield Strategic Real Estate Partners during 2012 – there were those who argued that mass consolidation was creating a situation where the small and emerging managers were increasingly getting starved out of the fundraising derby.

Sovereign wealth funds – an emerging class of institutional investors – were among some of the leading sources of investment dollars being sought by managers. A decade earlier, few people had scarcely heard of SWFs; but now they had more assets under management than hedge funds and private equity firms combined, with coffers that had swelled well past $5 trillion, with assets predicted to grow by $1 billion per day, according to a report issued by TheCityUK, an organization that promotes the United Kingdom's financial and professional services industries. Add to that a forecast by UBS Global Asset Management that, in the next three years alone, SWFs would increase their assets by 60 percent, as revenue from the sale and taxation of commodities – predominantly fossil fuels – remained strong. If accurate, SWFs would have been tipping the scales at $8.6 trillion in assets under management come 2016. Though that forecast was a bit over-enthusiastic, no doubt in part because of the collapse of commodity prices, the Sovereign Wealth Fund Institute counted $7.4 trillion in SWF assets as of July 2017.

The major SWFs investing money in North American real estate are located in foreign lands such as Abu Dhabi, China, Kuwait, Norway and Singapore. Those and other foreign capital flows buttressed

Mary Barra named CEO of General Motors

Jan. 15, 2014

2014

"U.S. commercial real estate is the cleanest dirty shirt in the closet."
*– **Chris Ludeman**, CBRE (2014)*

"It's not just who is going to pay the most; it's whether it is structured in a way that I get to eat what I kill. You want to get paid based on your success."
*– **Hillary Shine**, principal, Shine Associates (2014)*

Feb. 3, 2014
Janet Yellen named first woman to lead the Federal Reserve

" As a rule, people spend less as they age. They tend to move into a replacement mode rather than acquisition mode."
*– **Mary Ludgin**, Heitman (2014)*

2015

Commodity prices collapse

July 2015
Amazon market capitalization surpasses Walmart

Volkswagen is busted for installing software designed to evade environmental regulations in millions of its diesel-powered cars

December 2015
The Federal Reserve raises interest rate for first time in nearly a decade

"The U.S. real estate cycle is in the seventh inning, but we hope it's a doubleheader, and we don't want to get rained out."
*– **Roy March**, Eastdil Secured (2015)*

2016

Among the prize real estate possessions acquired by Chinese investment dollars that began flooding the United States was the Waldorf Astoria in New York City.

June 2016
British citizens vote to withdraw from the European Union

November 8, 2016
Donald Trump elected president of the United States, pulling off one of the biggest upsets in political history

"Size alone doesn't create poor alignment; the key issue is whether the manager is sufficiently focused on the fund's success."
*— **David Gilbert**, Clarion Partners (2016)*

"Part of the confusion in the marketplace is that there are many, many real estate debt strategies, but there is no common nomenclature, and the strategies are quite disparate from a risk-and-return perspective."
*— **Steve Bailey**, PGIM Real Estate (2017)*

June 1, 2017
Trump administration withdraws the United States from the Paris Climate Accord

2017

Global ransomware attacks temporarily paralyze many companies and government agencies

U.S. real estate markets and drove prices in gateway cities to new heights.

A special report on cross-border capital flow produced by Real Capital Analytics said that by mid-2011, cross-border investors had made $10.1 billion of U.S. direct commercial property investments since mid-2010. (That number did not include an additional $6.6 billion in foreign investment made through the acquisition of minority interests in U.S. property, as well as growing activity in indirect investments and mortgage originations, according to the report.) A report from Cushman & Wakefield showed Chinese investors were the single largest group of foreign investors in commercial real estate in the United States during 2016, with deal volumes reaching a record high of $19.2 billion, up 10 percent from $17.3 billion in 2015. Chinese investment accounted for 29 percent of total foreign investment in U.S. commercial real estate, followed by Canadian investors who committed $13.1 billion. Chinese investors, like those in other foreign countries, saw the United States as both a safe harbor and a place to diversify their holdings.

Some $16.3 billion found a home in New York City during 2016 alone, making the Big Apple the number one recipient of foreign investment, followed by London, $15.9 billion, and Paris, $9.7 billion. Knight Frank, which supplied those figures, predicted more than 30 percent of total global transactions will be cross-border as the globalization of real estate continues into 2018.

MORE MOMENTUM, PLEASE

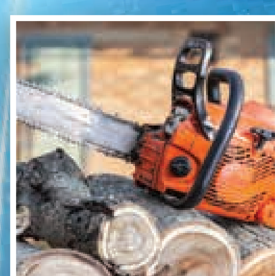
All the while, there were many business and political leaders bemoaning the sluggishness of the overall U.S. economic recovery, yet anyone would have been hard-pressed to find another country whose economy the United States could envy. Soon, it became undeniable that the U.S. economy was in its best shape since the global financial crisis. Job growth was up, the unemployment rate down, and the technology sector was again on a fast rise. It was no coincidence the property markets where tech jobs were being created were showing some of the strongest property fundamentals. The usual suspects included San Francisco, San Jose, Seattle and Austin, as well as suburban Boston and Northern Virginia.

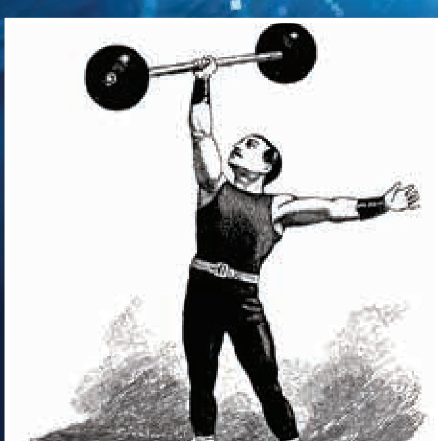
"Tech-driven markets are experiencing a tremendous amount of growth based on the new jobs that industry has created. Tech is also the fastest-growing industry as it relates to generating jobs for office space occupancy," observed Colin Yasukochi, director of research and analysis with CBRE.

As 2016 drew toward a close, Donald Trump was unexpectedly — according to polls, pundits and conventional wisdom — elected president of the United States, throwing a new round of unpredictability into the mix. Many commercial real estate investors are reacting the way they often do to uncertainty: taking a wait-and-see approach. The stock market reacted by setting a series of new record highs, the Dow eclipsing 22,000, inspired perhaps by Trump administration policies for cutting regulations, healthcare and tax reform, and a $1 trillion infrastructure spending program.

Mike Consol is editor of *Real Assets Adviser.*

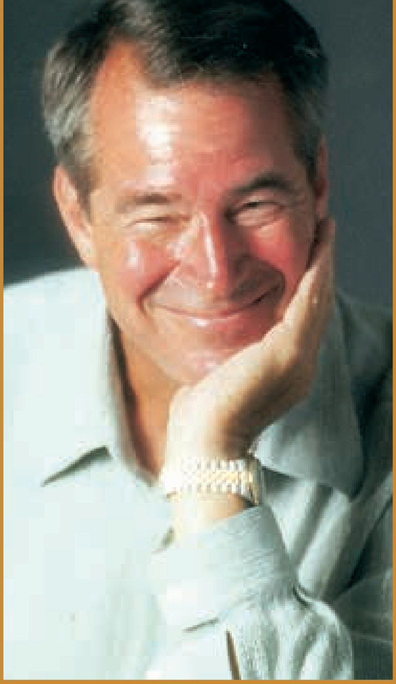
BLAST FROM THE PAST





January 1994

Be Careful What You Ask For; You May Get It



By Geoffrey Dohrmann

All my 6-year-old son Andrew wanted for Christmas was a chainsaw. Now, I'm not an expert on child development, but I certainly know it's not advisable to give in to such demands, particularly with Andrew. (Those of you who know my son can only imagine what he had in mind.)

The point is, 6-year-olds don't always have the experience needed to make good judgments about what is really in their best interest. But that's not the child's fault. When you've only lived in a world for six years (or 10 years, for that matter), there are bound to be a few experiences you will have missed along the way.

Which brings me to the issue of pension funds. Over the past six or seven years, pension funds have been getting increasingly involved in the decision making surrounding their real estate. That's all well and good, but right now, the real estate business is a tough one indeed.

Certainly assets have been repriced. But marking down a worthless piece of goods doesn't make it more valuable. Today more than ever, it takes real experience and exceptional judgment to find the assets that will continue to perform well over the long haul.

Furthermore, it takes an incredible amount of effort and skill to compete for tenants in what is becoming an increasingly competitive environment – an environment where there are fewer tenants than ever, and those tenants are all attempting to downsize a great deal of their existing space.

The recent flurry of REIT investment activity provides a case in point. REIT operators are flush with cash and aren't restricted by the level of bureaucracy that hamstrings the abilities of most institutional real estate investment advisers. Furthermore, REITs have not yet subjected themselves to the same level of due diligence and property underwriting that advisers have become subjected to. To make matters worse, REITs enjoy a wider spread between their current cost of capital (dividend yield) and the yields available in the underlying real estate markets. Consequently, they can afford to pay up for property, and are able to close faster, than most institutional real estate advisers. This has placed advisers at a distinct competitive disadvantage, particularly in those sectors of the market where the REITs are most active – apartments, for example, and retail property.

The point is, the current predominant form of investor/adviser relationship – nondiscretionary separate accounts – may be hampering institutions' ability to participate in a very interesting marketplace, and at a very opportune time. Worse, some pension funds may be ill equipped to participate in the decision making, and therefore may not only be slowing the process down, but actually may be undermining sound decision making.

The message for boards and staffs that don't have sufficient in-house experience, expertise or skill to compete effectively in this market: think twice before asking to retain discretion. You may be handing yourself a chainsaw.

P.S. Andrew got a Sega Genesis for Christmas.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September 1995

The Answer Is Nine

By Steve Steppe

Because his comments at our recent conference in New York define what's going on in the markets far more eloquently and humorously than I ever could, I'm giving my "space" this month to my colleague Steve Steppe at RREEF. — Geoffrey Dohrmann

In 1972, when I was still a young leasing broker for Coldwell Banker in Southern California, I signed up for my first investment training class. The class was being taught by a very bright Harvard MBA who ran the newly formed investment department at Coldwell Banker.

Bob Ellis started the class by asking the question, "How many of you would like to make a lot of money selling the properties you have been leasing?" Obviously, everyone's hand went up.

At that point, Bob said that the answer to the final exam for the class would be "nine." Now, to say the least, it was a little unusual to be given the answer to a final exam before the class even began. So we waited patiently for an explanation.

The next two weeks were spent on case studies of actual sales. And in every case we studied, the cap rates were always over or under "nine." So much for getting the answer to the final exam upfront.

As we soon learned, however, the answer to all of these cases really was "nine." For example, whenever we researched and analyzed a property that sold for a reported 7 percent cap rate and brought the rents to current market, the actual cap rate at current market rents would be "nine." If transactions were completed at 10 percent to 11 percent cap rates, we found it invariably was due to over market leases that would adjust down or, at best, remain at the same rent when they were renewed. And, whenever we made those adjustments, the answer was always "nine."

Eventually, we came to understand Bob's point; success when selling property is determined by having a price at current market rents that reflects a 9 percent capitalization rate.

During the 14 years I was with Coldwell Banker, I discovered that Bob was right, of course. No matter what may be going on in the markets with interest rates, inflation rates and economic conditions — the answer is always "nine."

In 1986, however, I called Bob and told him the answer no longer was "nine"; it was "six." Buyers were paying 6 percent cap rates at current market rates.

Bob laughed, of course, and replied that the answer was still "nine"; just because people were willing to overpay by 300 basis points, it didn't change the answer.

I'm now looking at a cap rate chart recently published by the Real Estate Research Corporation in its first quarter 1995 report, which reads:

Suburban Office	**9.0%**
Industrial	**9.0%**
CBD Office	**9.0%**
Retail (non-mall)	**9.0%**
Apartments	**8.8%**

Bob may be deceased now, but 23 years after my first investment training class, the answer is still "nine."

Steve Steppe is a principal with the San Francisco office of **RREEF**.

The above comments are based on excerpts from his presentation at the First Annual Summit on Real Estate Portfolio Management, held at the Waldorf-Astoria in New York, July 11 and 12, 1995.

January 1996

Portfolio Management — A Beautiful Concerto

By Glenn Mueller

Much like the conductor of a large orchestra, the portfolio manager (PM) must make sure that all members are playing together in harmony. A single member playing out of synch can ruin the entire piece.

In most cases, the portfolio manager is an accomplished musician with past experience in playing some of the instruments. Although no longer a performing musician, the PM must know how to direct each player to match the overall score, but must also be a manager capable of motivating each member of the group to focus on the common themes of the performance. If the acquisition specialist practices jazz music instead of classical, the possibility of his playing well at the next Mozart concert diminishes. What is the best style of leadership? One who commands or one who encourages group decision making? There's no one right answer or formula, but good leadership will show through in the long run performance.

Portfolio managers, like conductors, must choose a strategy (or score) that plays to the strengths of the performers and that fits into the management companies' perspective. If the team has experience and depth in a particular property type or region, the PM should implement a strategy that best plays on those strengths.

Today's PM must understand his strengths clearly, since there are too many specialists to compete against. Trying to appeal to all musical tastes is difficult and may lead to smaller audiences. PMs should not be afraid to specialize, as even die-hard Bach fans will buy "country" on occasion to diversify their collection. Why not do what you do best and wait for the crowd to come to you? Only through the addition of new musicians or the training of existing ones can new types of music or investments be added. Remember that investors have the choice of buying singles (separate account investments) or complete albums (commingled funds) from a group. They also can choose to attend the concert through private investments (with little liquidity once the show has started) or by electronically reproduced words more easily traded (such as public vehicles).

> *"Today's portfolio manager must understand his strengths clearly, since there are too many specialists to compete against. Trying to appeal to all musical tastes is difficult and may lead to smaller audiences."*

New works are being introduced again this season. The new-age music offers such vehicles as venture capital funds (oh, excuse me — to be politically correct, make that "opportunistic funds"). Many still like the old favorites (a core fund by any other name still sounds as sweet). Some now believe CDs have that lifelike quality of a live concert (yes, many believe REITs do derive their long-term returns from real estate).

So, what is your favorite musical masterpiece?

My son has re-ignited my enjoyment of the Grateful Dead (yes, I believe in the resurrection of The Dead, life everlasting and that real estate is once again in an upcycle). But my neighbor also has me hooked on Jimmy Buffet, who recently released a new album, *Fruitcakes*, that urges us not to take past problems too seriously. If you are not having fun with your current music portfolio, trade it in on something new — or try something old. You may find the oldies can be as profitable as new offerings, and that you have a better chance of singing along to something you know and understand.

Glenn Mueller is national director of real estate research at **Price Waterhouse LLP** and a faculty member of the Berman Real Estate Institute at Johns Hopkins University.

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March 1997

The Big Suit

By Geoffrey Dohrmann

Like a lot of middle-aged baby boomers, I'm not the thin, svelte, athletic young thing I used to be. It's hard to admit it, but those ads that promote jeans with "just a skosh more room in the thighs and seat" were written precisely with guys like me in mind.

The odd thing I've learned about middle-age spread is that I still think of myself as thin. Most of my life – at least, for the first 30 years or so of my life – I was thin. No more. So at least two or three times a year, I go on a silly soup diet that my associate, Michael Mollo, got me started on. (I've lost at least 500 pounds over the past 10 years this way. The only problem is, they're the same 500 pounds.)

On the other hand, I'm not above catering once and a while to my own conceit. Which is why I keep "The Big Suit."

The Big Suit is about three inches too big for me at the waist (two inches too big when I'm on the high side of my weight loss roller coaster). And when I put it on, I always feel at least 20 pounds lighter. Now, obviously, wearing The Big Suit doesn't really make me any thinner. But it does make me feel thinner, and that's a nice feeling. Although I've learned I can't wear The Big Suit every day, it can be comforting to delude myself this way from time to time. And it really doesn't do much harm.

That's not always the case with other things, however. A number of REIT market analysts are purporting that REIT stocks are cheap right now, for example, because their multiples are significantly below earnings and cash flow multiples for the S&P and other broader market indices. And REIT multiples are lower than the multiples for most non-real estate companies, of course, but this isn't really news; REIT stock multiples always have been lower than the multiples for non-real estate companies.

Consequently, pointing out that REIT prices have room to grow because the multiples are so much lower, is a little bit like putting on The Big Suit. It might make you feel more comfortable about current pricing, but it does nothing to change what's really going on.

Just as my Big Suit doesn't really make me thinner, the fact that the spreads between the multiples on REIT stock cash flows vis à vis alternatives remain wide doesn't mean they're cheap.

REITs are companies, not real estate, granted. But that's where the analogy ends. Most companies own some real estate; some even lease all or a portion of their surplus space to third parties. But the only thing that REITs own is real estate, and the only thing they really have to sell is space. Consequently, their cash flows ought to be – and generally are – more homogenous and stable than the cash flows of most companies trading in the broader markets. This gives them a fixed-income characteristic that historically had positioned them primarily as income vehicles rather than growth vehicles.

The emergence of a whole new crop of REITs following the Kimco IPO in 1991 introduced a new spin to the market. Wall Street investment bankers and their clients (the companies they were taking public, not the investors in those companies) began talking about REITs as operating companies and growth stocks, rather than as investment vehicles and income stocks.

For my money, the "growth" part of this story is now and always has been balderdash. The REITs that have come public post-1992 still have to pay out 95 percent of their operating income, and therefore, they can't be growth vehicles over the long haul.

This is not to suggest REITs can't grow because, clearly, many of them have been growing of late, and some at a fairly nice clip. But what's driving that growth?

In the short run, there's no question a well-managed REIT can grow earnings through accretive acquisitions (so long, that is, as market pricing differentials allow). REIT executives also can grow earnings by taking advantage of rising rental rate markets. And, to a limited extent, they can grow through development, they can grow earnings through engineering of operating efficiencies, and they can grow earnings from expansion of multiples, due to excessive capital flows.

The reality, however, is they can't sustain long-term growth from any of these sources indefinitely. If you look at NCREIF returns on an inflation-adjusted basis – the proxy for unlevered private equity real estate market returns – over time, you'll see what amounts to a bell curve. The rise in value reflected by the curve almost always is eroded over time. In other words, depreciation is real – it reflects real capital obsolescence, not just accounting conventions.

Another way of saying this is: In the private markets, the answer is nine. According to Steve Steppe's private market pricing principal, any deviations in pricing from a nine cap rate can be attributed to one of three factors: rents in place that either are over or under current market, operating costs that are significantly above or below market, or capital market effects.

Since REIT operating cash flows are tied to the rents and operating expenses of their underlying property portfolios, over the long run, the pricing of REIT cash flows also have to be linked to these dynamics. There's no question that the public markets will place a premium – or discount – on franchise value and management. But those premiums or discounts almost always are fairly priced in the long run by the market, and can be explained in part by the spreads that develop from time to time between public and private market pricing.

This isn't to say that there aren't anomalies in pricing within the markets. Anomalies are what investment management professionals like you are paid to uncover. That's where value always is added, and that's why they pay you the big bucks. But don't confuse temporary property or capital market effects – rising rental rate markets or too much money chasing too few stocks – with long-term trends in pricing.

It's a free country; you can even believe that this means there still is a lot of value left in the market, if you want to. But don't kid yourself. All you'll be doing is putting on The Big Suit.

October 2006

Taking on a New Role

By Larry Gray

Real estate enjoys its moment in the spotlight

Maybe every dog does have its day, as the old expression goes. Little more than a decade ago, the real estate asset class – and many debated at that time whether or not it was a separate asset class – not only didn't get any respect, it didn't get any capital. Real estate was about as popular as a villain in a vaudeville play. The boos rained down, and deservedly so. But times change, and so has the real estate asset class and the real estate industry. Given a second chance, real estate was recast, earning the role of the handsome hero.

THE EARLY DAYS

In the late 1980s and early 1990s, the real estate industry suffered from flawed investment structures and a lack of liquidity in the market. Many pension funds were invested in closed-end commingled funds. When the market started to deteriorate, there was no exit door; pension funds couldn't get their capital back. Managers who were compensated with asset-based fees had little incentive to sell properties into a declining market.

Investors were dismayed, disgruntled and disillusioned. The end result, however, was the birth of the secondary market to increase liquidity and the introduction of incentive-based fee structures.

"Investor dissatisfaction was partially in response to performance, but also the recognition that investors had little or no control over the money," explains John McClelland, principal investment officer, real estate, at the $34.5 billion Los Angeles County Employees Retirement Association. "The industry went through a learning curve or realization of what this all meant as far as a need for better liquidity and alignment of interests."

WELCOME TO THE SHOW

Lessons learned, real estate slowly edged its way back into the investment mainstream.

"There has been an increased acceptance of REITs, and investors have gained a greater familiarity with the real estate asset class because of the public market," notes Robert Maynard, chief investment officer at the $9.8 billion Public Employee Retirement System of Idaho. "This has helped to integrate the asset class into the broader capital markets, and it is not siloed off like it was in the 1990s."

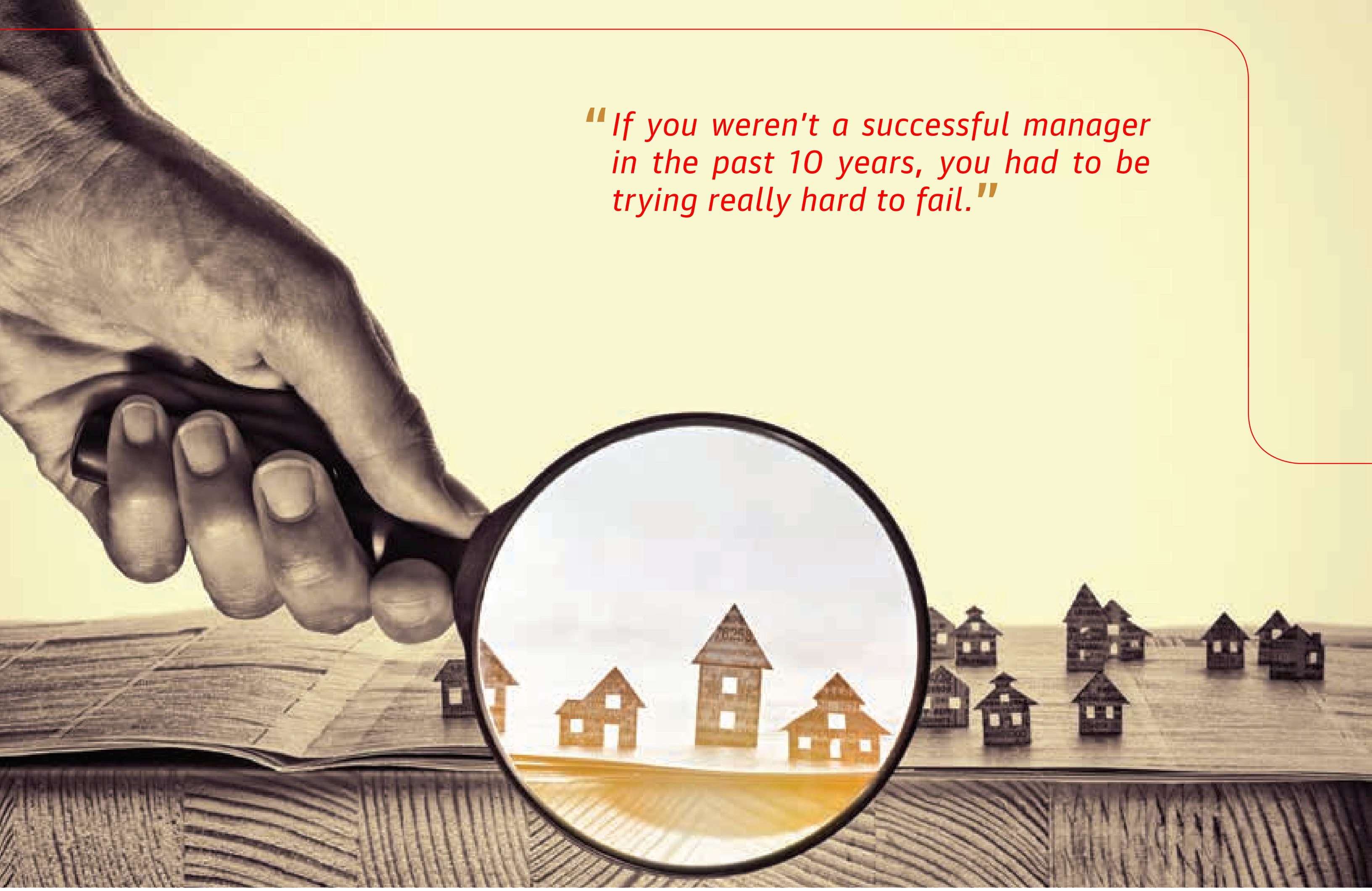
Given a second chance when the equities market took a nosedive earlier this decade, real estate was there to offer investors steady, stable returns.

"From the mid-1990s, real estate performance has been quite strong, while performance in other asset classes, at different times, has been quite volatile," says McClelland. "Obviously the stock market went screaming through the roof, and the public equity market was the jewel of the business, and then it sucked wind for a couple of years after the tech wreck.

"In the midst of the stock market's volatility, real estate looks like the plodder, the tortoise in the tortoise and the hare race," adds McClelland.

Industry pundits rewarded real estate with the moniker of "tallest midget in the circus," referring to the fact that it offered a relatively higher yield in a yield-starved environment. In the past few years, however, real estate's performance compares more favorably to the circus strong man; the asset class has produced phenomenal returns and done some heavy lifting for many a pension fund's portfolio.

For the 12-month period ended June 30, for example, CalPERS, CalSTRS and the Pennsylvania Public Schools Employees' Retirement System all reported that real



> “If you weren’t a successful manager in the past 10 years, you had to be trying really hard to fail.”

estate was the top earner for their respective funds with total returns exceeding 35 percent in each case.

Increased investor allocations to the real estate asset class and a much wider expanse of real estate investment strategies in search of higher returns have resulted in more capital being invested in value-add, opportunistic and offshore strategies.

“Real estate’s performance has elevated its stature and garnered more attention,” states Micolyn Yalonis, principal at The Townsend Group. “It seems to be more broadly accepted as an established asset class. Across our client base, we have seen increases in allocations, as well as new clients with new allocations because of the relative returns.”

In the past several years, a number of plan sponsors have made the decision to add real estate to their asset mix. Some of these funds never had real estate in their portfolios, while other funds include themselves among the “burn victims,” who swore off real estate after suffering through the market’s dismal returns and lack of liquidity in the early 1990s.

Funds that recently have added equity real estate include the Arizona State Retirement System, New York City Retirement System, District of Columbia Retirement Board, New Mexico Public Employees’ Retirement Association, New Jersey Division of Investment and Teacher Retirement System of Texas.

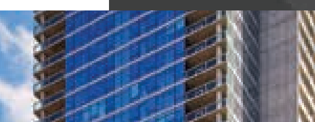
EXPANDING ROLE

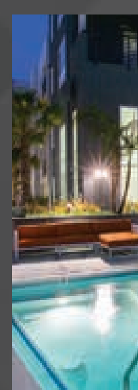
A certain comfort level comes from experience. Pension funds have been advancing along the real estate learning curve over the past 20 years. CIOs have become more comfortable with real estate and can better understand what the asset can and cannot do.

“In 1987, when I went to work at CalSTRS, they were not comfortable with any property that had a bed in it,” relates McClelland. “They didn’t want to own any apartments or hotels. They did not want calls from teachers whose plumbing was stopped up; they didn’t want to face the prospect of evicting a teacher from an apartment. Now, pension funds own a lot of apartment properties and hotels. They have gained a comfort level with a broader range of property types and types of investments.”

Many pension fund CEOs and CIOs are under the gun to deliver annual returns of 8 percent or more to meet their target actuarial expectations. In today’s investment environment it is very difficult to squeeze out those types of results with stocks and bonds. Under the current market conditions, real estate offers a lot of alpha opportunities, which are being attractively packaged and marketed.

“It no longer seems to be about diversification,” relates Yalonis. “The diversification is a side benefit. The objective has changed. If you look at our client base, we used to be predominantly a minimum of 70 percent to core and a maximum of 30 percent to noncore. At this time, our clients are adopting allocations of up to 80 percent noncore and 20 percent core; that’s reflective of the need for more returns out of the asset class





for it to be accretive to the portfolio at the portfolio level."

"Real estate can be used for both portfolio diversification and to generate alpha," says Maynard. "Those aren't necessarily mutually exclusive. The old artificial distinctions are clearly being broken down and the old, more rigid forms of investment have clearly been expanding. As a result, the usual sharper edges of real estate investments have been blurred, so at the edges you can't tell whether certain real estate investments are different than private equity or different than pure high-return plays."

ENCORE, ENCORE!

For the past five years, real estate has recorded an 11.7 percent return, according to the NCREIF Property Index. The market has exceeded its long-term average of 9 percent. Many pension funds have enjoyed annual returns north of 20 percent from their real estate portfolios, while some have surpassed 30 percent.

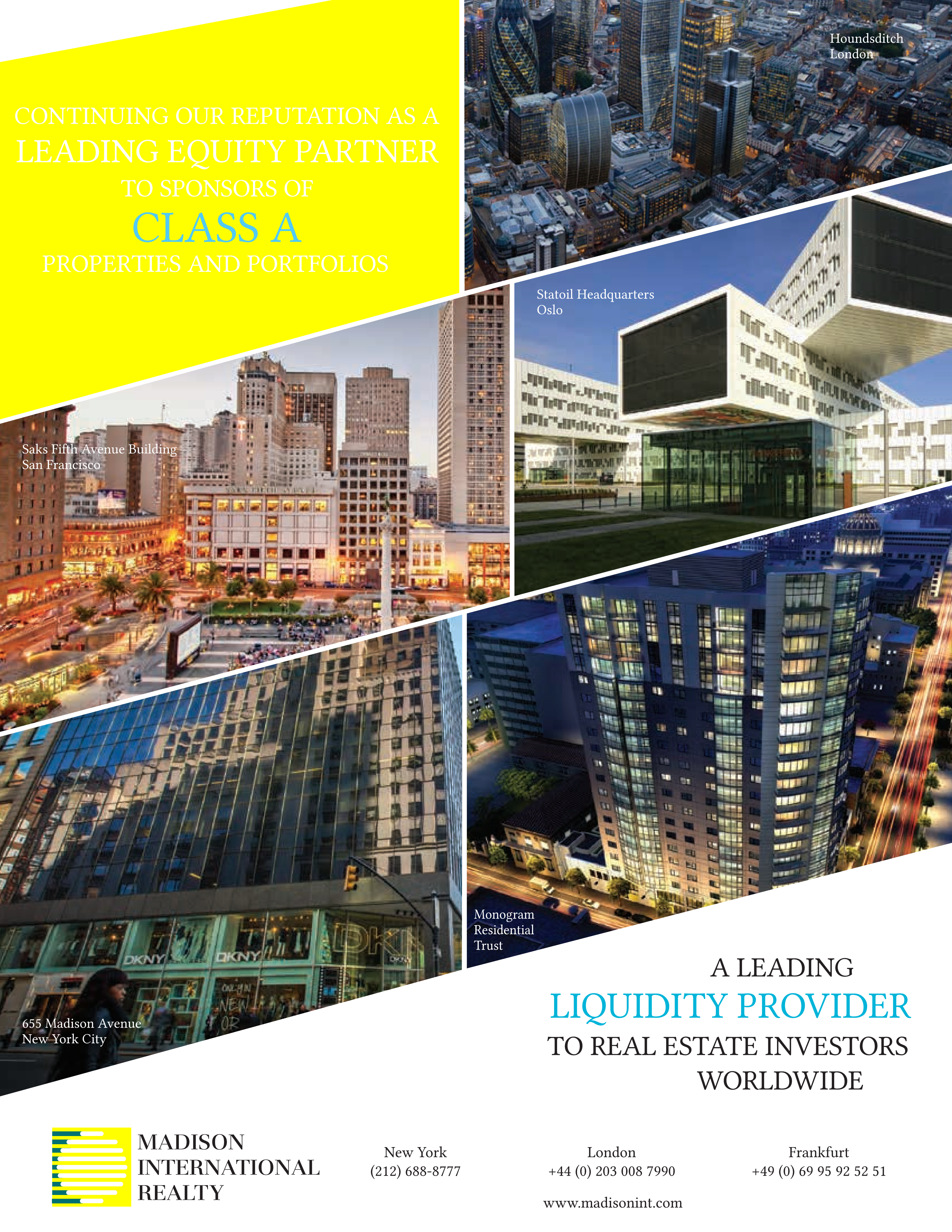
Alas, as many performers know all too well, it's hard to stay on top.

"If you weren't a successful manager in the past 10 years, you had to be trying really hard to fail," observes Yalonis. "In today's market, going forward in a much more competitive environment, selecting the right funds is going to be the key to success in any investor's program. It's just not going to be as easy to pick the winners."

"Over the past five years, it has been a stunning performance for real estate," admits Maynard. "However, there's no way on this green earth real estate can maintain the level of absolute performance it has enjoyed over the past five years. On the other hand, is that a harbinger of doom for the next five years? You look at reproduction cost vs. existing product. Even at these low cap rates, you still can buy property at a fraction of the cost of building something similar nearby. It's not just land cost; it's also escalating construction costs. How that plays out over the next four or five years could affect liquidity in the market and performance."

Real estate has enjoyed a nice run. But how long can it last? There are no signs that capital flows will slow; quite the opposite, allocations to the real estate asset class continue to grow in response to relatively weak performance in the U.S. stock and bond markets. Maybe the asset class' exceptional performance will be derailed by rising interest rates or a slowing economy. What does seem certain is that real estate eventually will take a step back out of the spotlight.

"We are hopeful that clients are heeding our warning that we expect a reversion to the mean," says Yalonis. "Equities are *supposed* to do better than real estate. When the market starts to turn, the ideal result will be that some of the more fringe capital sources will exit the market and prices will be less competitive. Also keep in mind that we are just starting to see property fundamentals improving, so even if you have a little dip in capital, improving property performance could hold returns."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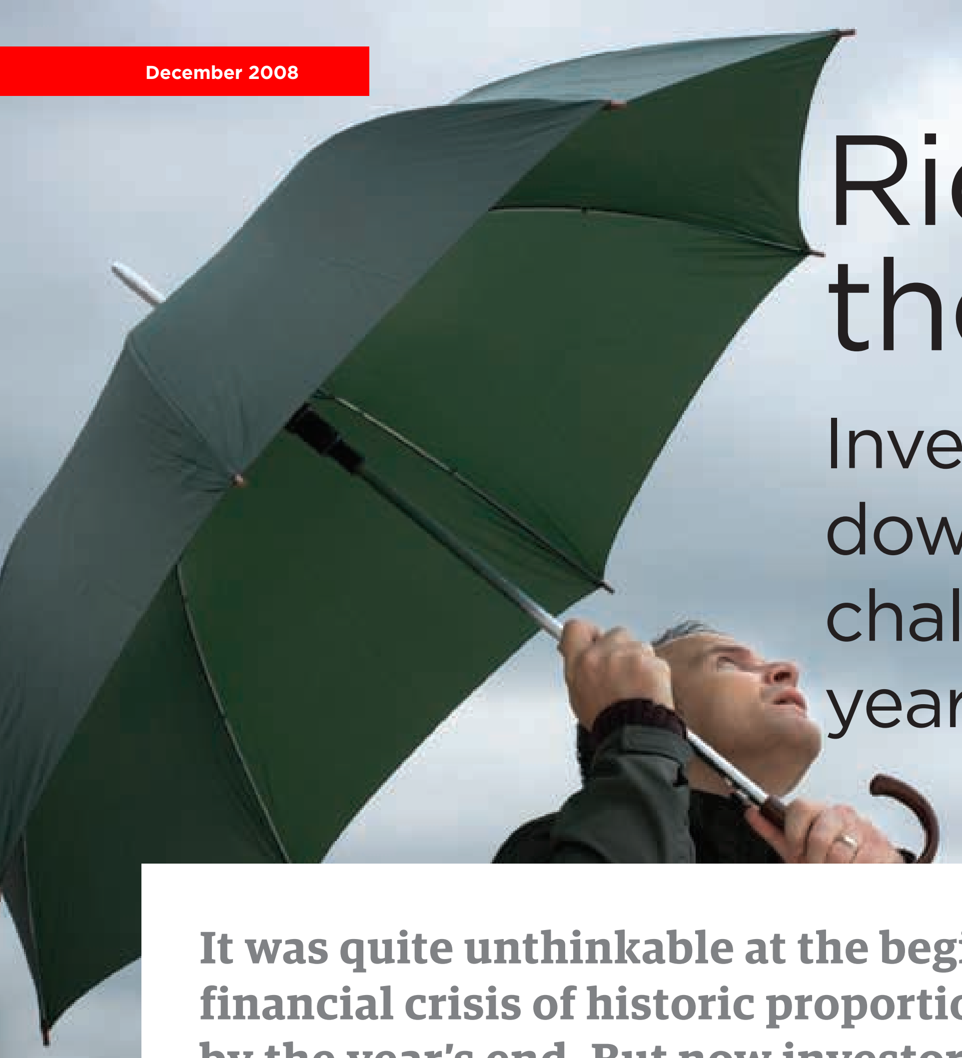

Riding Out the **Storm:**

Investors hunker down for a challenging year ahead

By Rachel Speirs

It was quite unthinkable at the beginning of 2008 that a financial crisis of historic proportions would be a reality by the year's end. But now investors are beginning to understand the severity of the situation they're in, and they're preparing for the realities ahead.

Before September, investors might have said they were cautiously optimistic about commercial real estate's near future. Many took comfort that supply had been kept in check and capital seemed plentiful. It was the common view that a downturn, should there be a downturn, would be mild. But all that changed with Lehman Bros. When the $600 billion investment bank filed for bankruptcy protection on Sept. 15, it set off a domino effect of global proportions. In the weeks that followed, stock markets worldwide crashed and entered a period of high volatility, while a considerable number of banking, mortgage and insurance companies failed.

"It was a little bit of a perfect storm," says Micolyn Yalonis, principal at real estate consulting firm The Townsend Group.

In fact, Lehman wasn't the first domino to fall. It had been a precarious situation all along. Investors' confidence in the value of securitized mortgages had been sinking since the middle of last year. Banks that held these securitized loans on their balance sheets were scrambling to cover their debt obligations, and the result was a liquidity crisis, which prompted the federal government to inject capital into the financial markets. That all worsened in September, however, when the world found out what happens when a big bank closes its doors.

For commercial real estate investors, the collapse of Lehman and the failure and consolidation of other large investment banks meant a complete shutdown of lending, the key element of the business that greases the wheels of buying and selling. An already tightened lending market now ground to a halt.

New CMBS issuance dropped precipitously. According to CBRE, year-over-year new issuance has gone from $137 billion in 2007 to a mere $12 billion in 2008, leaving a large void in commercial real estate financing that simply cannot be met by balance sheet lenders.

The result has left the real estate market in limbo. The spread between what sellers are asking and what buyers are willing to pay has widened, and cheap debt, which helped to bridge the divide in the past, has quickly become a thing of the past.

By the second half of 2008, year-over-year transaction volume had fallen 71 percent from the $62.4 billion of commercial property that traded in second quarter 2007, according to data compiled by Institutional Real Estate, Inc. The situation grew even worse for leveraged investors as many of the large balance sheet lenders put their lending on hold for the duration of the year.

"We've seen a complete shutdown of the transaction markets," says Townsend's Yalonis. "The absence of transactions coupled with the absence of debt has already begun to impact pricing. Limited liquidity and the additional effect of the denominator decline will only exacerbate decreases in transaction volume," she explained. "It permeates everything."

With unemployment mounting, stocks tumbling and liquidity evaporating, investors are bracing for a challenging year ahead.

THE ROAD TO MELTDOWN

It wasn't that long ago that commercial real estate was enjoying a heyday of easy credit and escalating property values. Those days, from 2005 to early 2008, were "almost like living in Disneyland," says Susan Smith, editor of PricewaterhouseCooper's *Korpacz Real Estate Investor Survey*. "Tenants wanted all this space, landlords were happy to accommodate, and it was great that demand was ahead of supply, buyers and sellers moved in synch, everybody agreed on pricing."

But investors sensed the good times were quickly coming to an end Smith says. "I remember investors saying to me, 'This is eventually going to stop;' and lo and behold it has."

The turnaround came during the second half of 2007, when rating agencies downgraded the ratings of billions of dollars of residential mortgage-backed securities, turning AAA bonds to junk status overnight. Even then, investors maintained a cautious optimism through the first half of 2008, but when the investment banks fell, investor optimism fell with it.

During October, following a series of bank bailouts, REIT prices declined 30 percent, amounting to a 47 percent drop from their peak in February 2007.

"I don't think anybody foresaw the crisis," PricewaterhouseCooper's Smith said. "It all just kind of imploded, and on a daily basis you were holding your breath to see what would happen."

During those tense days in the last week of September, industry leaders gathered in Chicago for the Pension Real Estate Association's (PREA) fall conference, where they discussed the implications of the latest abrupt economic downturn on real estate investments.

Mike Kirby, chairman and director of research for Green Street Advisors, told the audience that public real estate returns, which had posted declines for most of the year, would continue to sink.

"When I made a prediction earlier this year that the values would fall by as much as 30 percent, people thought I was off-base," he said. "The latest predictions are more than this. … If General Electric and Goldman Sachs are stressed, it would be naive to think real estate won't go through the same thing."

Private real estate prices have fluctuated widely throughout the year, CBRE noted in its September report.

"There have been buildings sold at healthy discounts, but also transactions where pricing has held up nicely," the report says, concluding, "This situation is indicative of a market where there is no broad consensus as to where prices should be."

Analysts are now saying that private real estate market prices could decline between 20 percent and 30 percent from their peak. The California Public Employees' Retirement System (CalPERS), the nation's largest public pension fund, announced in November, that, as of June, the value of its real estate holdings had declined 35 percent from its original cost of $9.3 billion to $6.1 billion. Currently, fund administrators are restructuring certain outstanding debt arrangements and reducing leverage where appropriate, while planning to keep the majority of its assets and be patient.

Investors who can wait it out, are doing so, says Yalonis.

"People don't know what pricing is going to look like going forward. We don't know exactly where cap rates are going, but we do know they are going up. In the absence of any clarity, the ability to wait for the market to be more transparent is an advantage."

But because so few transactions are taking place, investors remain uncertain about where pricing should be.

At the recent PREA conference, Jeffrey Horowitz, managing director and head of global real estate banking at Merrill Lynch, summed up the sentiment of many investors: "[Investors] don't want to look stupid. There is a lack of confidence."

PricewaterhouseCooper's Smith adds that the latest economic news means investors will have to grapple with changing growth projections and increasing vacancy rates as well.

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"On top of this price correction, you also have a big shift in fundamentals happening in all sectors," says Smith.

In the next year, commercial vacancies for the New York metropolitan area, for example, are expected to surge to 17.6 percent, an increase from today's 12 percent vacancy rate, according to a revised forecast issued Oct. 27 by Property & Portfolio Research. The new projection was considerably higher than the 13 percent peak that the firm projected in August.

Across the nation, the results could be similar. According to RREEF Research, between 2 million and 2.5 million jobs could be lost between 2007 and year-end 2009, producing a peak unemployment rate of more than 8 percent. That, their report says, will translate to weak property sector performance, especially in the office and retail sectors. Despite a tempered construction pipeline, which has kept supply in check, the firm does not expect recovery until 2011.

A NEW ORDER

Going forward, investors expect an era of tighter lending and tempered investing. Many are taking a "back-to-basics" approach. The days of relying on leverage and cap rate compression to fuel returns have been replaced by a focus on adding value at the property level and improving tenant retention. The result is a new world for investors, one with new sets of challenges but also new opportunities.

"It's an excellent time to think outside the box in terms of traditional solutions as well as traditional access to the opportunities," says Townsend's Yalonis. Though she says her firm is not rushing to push capital to any quick decisions, Yalonis notes, "there's time, and patient capital will still do well."

The opportunities could be huge. In an October report, Goldman Sachs estimated that nearly $1.3 trillion of 2005 to 2008 vintage loans held on banks' balance sheets and within CMBS structures would need to be refinanced through 2016, potentially requiring around $209.1 billion of additional equity. Those refinancings could lead to substantial defaults, which may turn into bargain deals as distressed sellers look to offload properties they can no longer afford. Additionally, pension fund investors may find opportunities in mezzanine debt and whole loans, which traditionally were not a part of most pension funds' investment strategies.

"Today, we're finding better opportunities in the debt space than in the equity space because debt investors have been much quicker to react to the current market realities, whereas private owners of property have not felt the same levels of urgency or distress yet," says Timothy Ballard, CIO and COO of Buchanan Street Partners.

But the opportunities are not without risk, Ballard warns: "Just as I think we will see cap rate expansion between primary and secondary markets, I believe we'll see cap rate expansion between primary and secondary food groups."

Whether the year ahead proves to be a challenge or a fantastic opportunity largely depends on whether or not you have cash on hand. Cash is king, says Ballard: "If you have capital and you're trying to invest, you're pretty happy. If you own a large portfolio of assets purchased during 2006 and 2007, you've got a lot of work to do."

He also notes that while some investors may see the opportunities ahead, some may not be able to take advantage of them because many are trying to rebalance their portfolio allocations.

At least for now, no one is rushing for the exits, but many questions remain.

"There are a lot of managers with dry powder who did not invest the capital they raised from funds in '07, '08 and even some from '06," says Yalonis. "We're already dealing with when windows expire and deciding how to handle unfunded commitments that haven't been called yet. Do we want to expand windows to allow managers to finish investing in the new market cycle? How do you reward the manager who chose not to invest at the peak, and how do you make sure their window still works, while balancing that with some clients who are saying, 'I appreciate the fact that you didn't invest, but I have to have my money back because I'm so overallocated?' It's a challenge and it will certainly be something we'll be working a lot on in 2009."

For investors, she says, the biggest challenge will be what it has always been, distinguishing the good investments from the bad.

"The other day, an advice manager summarized the challenges before us very well. They said, 'It's very important to be discerning between temptation and opportunity.' That's the hard part right now," notes Yalonis. "It's knowing which investments are opportunities and which are temptation."

Investors will have to navigate the new waters carefully. Both Ballard and Yalonis say that it's not only the investments that face challenges, but the corporate real estate firms as well. Ballard says that because of a lack of transaction flow — and some poor decisions people have made in previous years — some level of corporate distress within the commercial real estate business is likely.

"It's not on most people's radar yet," he said, but potentially it could cause, "some messy situations."

Yalonis says that consolidation is part of a pattern of the industry. Because the industry has seen expansion during the past few years, investors now should expect some level of consolidation among the management firms.

Ballard cautions, "Investors just should be very sensitive to this to make sure they're protecting their investments." But the flip side, he notes, is that the firms that do survive will be stronger and have the opportunity to find talented employees.

At Oaktree Capital Management, company chairman Howard Marks sent a memo to his investors in November noting that despite the pessimism prevalent in today's market, "the greater long-term risk probably lies in not investing."

He, like others, expects a financial market of the future that will be less leveraged, less risk prone, less profitable, slower growing and more regulated.

"That will make it less exciting, less glamorous and less the employer of choice," he writes. "But the beauty of the free market system is that most developments entail pluses as well as minuses. I've believed for many years that just as success carries within itself the seeds of failure, so does failure carry the seeds of success."

MSCI measures one-quarter of the world's investment real estate spanning **32 Countries** and capital values of approximately **US $2.0 trillion**[1]

REAL ESTATE ASSET FACTORS AND METRICS

90 Financial & operating metrics

30 Asset risk & life cycle combinations

120 Property sectors & sub-sectors

11 Geographic Classifications

1,406 Portfolios

74,082 Assets

~17 years Track record

Global Intel PLUS

Providing Insights for Performance

Global Intel PLUS adds unprecedented dynamic capabilities to MSCI's industry leading real estate market information offering, Global Intel. With this enhanced functionality users can now generate tailored analyses utilizing custom filters on asset specific characteristics such as property type, location and risk profile to create the appropriate comparisons that are essential to managing performance and risk.

realestate@msci.com

[1] Based on 2016 year end capital value figures of MSCI measured Real Estate

MSCI

By Lauren Parr

The Global **Hunt for Yield:**

Investors are going further afield and exploring alternatives in a low-return environment

Five years into the global economy's recovery, interest rates remain low by historical standards. As such, investors' hunt for yield is intensifying. Fixed-income returns are low, and stock market returns are volatile, pushing investors into alternatives such as real estate.

As the recovery in the global economy and real estate markets transitions into a broader cyclical upswing — with activity supported by improving underlying growth prospects, a favorable policy environment, lower energy prices and stronger U.S. consumer spending — the weight of capital targeting property continues to increase and transaction volumes continue to grow.

Institutional Real Estate, Inc's FundTracker database reflects five years of steadily increasing amounts raised for real estate funds around the world, crowned by 2014's \$91.7 billion — nearly twice the \$46.8 billion raised in 2010. In addition, global property deal flow rose by 9 percent to \$770 billion in 2014, according to Real Capital Analytics. And prime cap rates have declined to pre-crisis lows in several major markets. For example, yields in London, Hong Kong and San Francisco are now lower than they were prior to the global financial crisis.

"It's becoming increasingly difficult, with interest rates as low as they are and investors having turned to property several years ago now, to replicate the fixed-income yields that they were used to achieving," says Russell Chaplin, chief investment officer - property of global investor Aberdeen Asset Management. "Yields have moved lower for better-quality stock across the globe. There doesn't seem to be a top-down free lunch."

WHERE TO NOW?

The question is, with so much liquidity pushing down returns, where can investors find the yields that they need to fulfill their requirements?

In terms of pricing, the United States and the United Kingdom are broadly ahead of the pack. Europe is some way behind, and Asia and emerging markets are lagging further. While higher yields are on offer across Asia, it is not a like-for-like comparison because different risks are associated with investing in those markets.

Investors agree that life is tougher at this point in the cycle than it was two years ago. But despite record-low cap rates, real estate remains a good place to be relative to other lower-yielding asset classes.

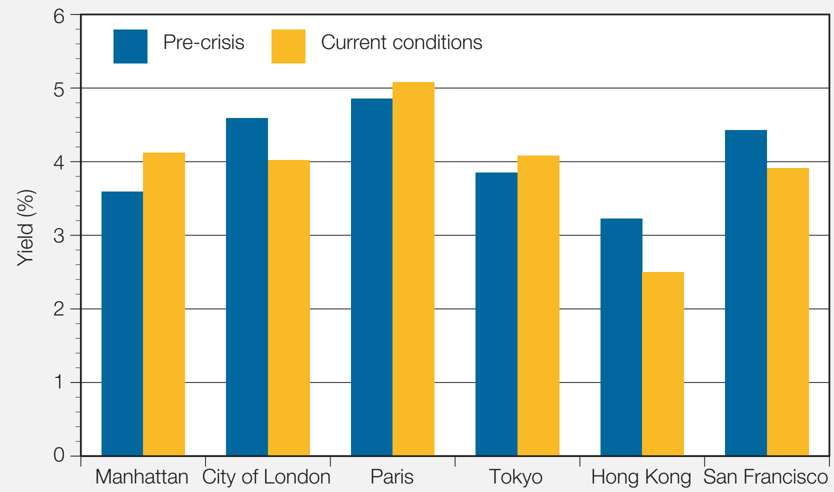
"We're into the second half of the real estate cycle, which means that the low-hanging fruit is gone," says Kye Joon Lee, director - Asia with Clarion Partners. "You can still find opportunities, but you need to put in more work to uncover value."

CORE OR HIGHER?

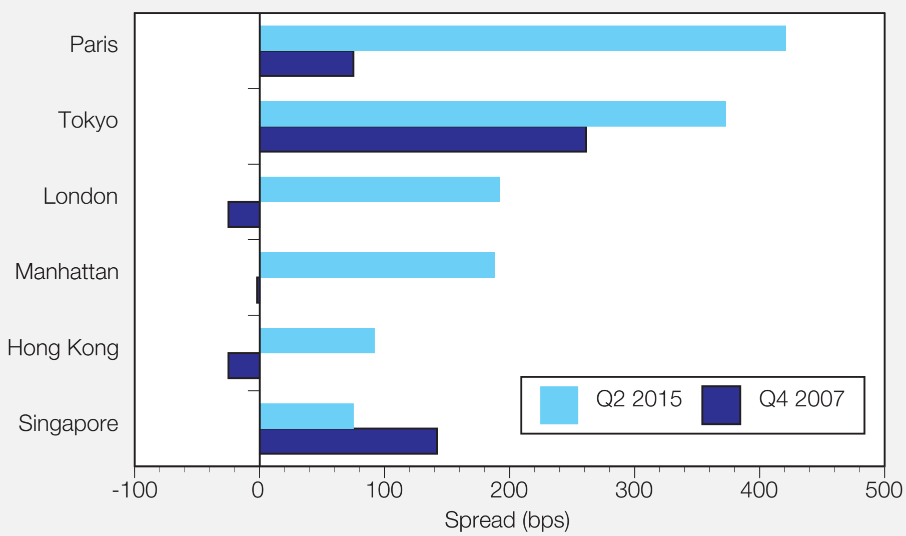
Investors face a dilemma: to invest in the core end of the market, where returns look low in a historical context, or push for higher returns by taking on greater risk. An ongoing focus on stable income in gateway cities based on the prospect of rent increases, coupled with a move toward secondary assets, peripheral markets, alternative sectors and debt products as part of a broader search for yield over the past 18 months, provides evidence of both strategies.

"The way we try to do this is by looking bottom-up at assets, which means that we're more concerned about the micro of an asset — where it is within a particular locale," explains Chaplin. As a long-term value investor, Aberdeen leans toward lower-risk

Prime office yields in selected global cities



Office yields minus 10-year government bonds in selected global cities



Source: Real Capital Analytics

positions when the market looks stretched, while honing in on "less obvious assets" that can deliver a pricing advantage.

"We're not necessarily looking for long leases but a durability aspect, which means that an investment can be characterized by a series of very short leases as long as it provides us comfort that people will re-lease if a tenant left," he says.

As risk appetite grows, investors are increasingly looking beyond traditional mainstream sectors to alternatives such as student housing, healthcare, hotels and leisure.

"We see a huge amount of opportunity in the residential private rented sector in the United Kingdom, which is establishing itself as a future mainstream opportunity for institutional investors. The nation hasn't built enough housing so, with an attractive supply/demand imbalance, the prospect for rents going up is compelling," says Richard Gwilliam, head of M&G Real Estate's property research.

With little cap rate compression on the horizon in developed markets, investors have an increasing reliance on rental-rate growth prospects to drive returns.

Core/core-plus investor TH Real Estate is another focusing on maximizing rental income. Says Mike Keogh, an associate director of research and strategy, "It isn't so much a global hunt for yield today; it's a hunt for rental growth. If you've got that, you get outperformance and are cushioned from a potential pricing adjustment as borrowing rates start to normalize."

Investing in faster-growing, late-recovery markets that offer potential for accelerated rental growth is one of the three best risk-adjusted opportunities today, as identified by a Pramerica Real Estate Investors research paper, *The Search for Yield*. PREI, which operates as Prudential Real Estate Investors in the Americas, Japan and South Korea, recommends that investors target office and retail assets in government centers and housing-bust markets such as Madrid, Miami and Phoenix, where low supply growth has created potential for rents in CBD areas to grow quickly from a low starting point.

PREI also advocates value-add investing in core markets as a means of earning excess returns via income growth. Little pipeline stock and an ongoing lack of capital expenditure across northern European cities and established markets in developed Asia Pacific, including Hong Kong, Japan and Singapore, imply a significant opportunity to refurbish and reposition city center office assets, explains the report. Strong leasing conditions in U.S. office markets mean that value can be found in taking on vacant space in the country's gateway markets.

DEVELOPING STORY

"Some of the best-yielding opportunities now, if an investor is willing to go up the risk curve further, is on the development side, which can provide an extra 200 basis points of yield on mature assets," notes Presima's Vincent Felteau, a portfolio manager for the Asia Pacific region. He sees value in master-planned developments, which often combine an office complex with ground-level retail, anchored by good transport connectivity.

"Because these projects are planned by a group of experienced developers, usually taking a longer-term investment perspective, we find that they provide a very attractive yield over time versus buying one-off assets, which in this environment are getting very expensive," explains Felteau.

The development model is attracting growing investor interest across established global markets.

Build-to-core "is a good area to be looking," in Gwilliam's book. "It's a cheaper way to do it than buying off the shelf, and you're creating a core product at the end of it, with the caveat that this only works in stronger locales with solid fundamentals, where demand is coming back and where there is not much in the way of supply of new prime space."

U.S.-based National Real Estate Advisors' managing director Kevin Verdi questions, however, whether "it may be time to shift away from more equity-oriented build-to-core investing toward types of debt: construction loans, mezzanine debt and preferred equity," given that development yields for core projects have compressed.

"At this stage in the economic cycle, in which stronger supply/demand fundamentals and increased rents have been mostly offset by increased land prices and rising construction costs, a more secure position in the capital stack can result in a lower risk and a higher return outcome when compared to an equity investment," argues Verdi.

DEBT AND DISTRESS

Many investors have turned to debt investing in their hunt for yield; private debt funds raised $23 billion globally in 2014, according to the FundTracker database.

An opening for alternative lenders has been generated by rising transaction volumes, a stronger growth outlook and regulatory changes such as Basel III, which restricts bank financing at higher loan-to-value ratios. Yet even in this realm, available returns are diminishing as pricing is driven down by continued low interest rates and increased competition among debt providers.

"Debt investing was a better opportunity two or three years ago. Today, LTVs are gradually moving up and opportunities are drawing in; the window of opportunity is slowly closing," acknowledges Gwilliam.

One sector where Rocaton Investment Advisors still feels positive on returns is European distressed real estate. "If you're an investor who doesn't require an immediate yield, buying distressed assets from a bank, bad bank or other motivated seller relatively cheaply, fixing and repackaging them before eventually selling off can be one of the best investments that you can make on a global basis," says founding partner David Morton.

CHANGING TRENDS

Another area of capitalization for investors, notes PREI, relates to changing market patterns driven by structural trends, which provide an opportunity to tap into long-term growth potential. The *Search for Yield* highlights ongoing urbanization as a basis for converting older, low-value office, retail or light industrial space to residential use in major cities such as Frankfurt, London, San Francisco, Sydney and Tokyo. Growing discretionary income across developing Asia and Latin America provides another incentive for development of modern residential and retail assets.

"One of the things that we definitely see as an opportunity globally is tied into a very big-picture trend of shifting consumer sales from bricks and mortar retail to online sales, benefiting the logistics markets in most of the world," adds Mike McMenomy, CBRE Global Investors' global head of investor services.

He lists emerging economies in Europe, such as Poland, where there is a burgeoning market for e-commerce, as well as the emerging market of China, where logistics infrastructure is beginning to develop, as among locations that reflect a strong investment thesis.

"Strategies that are buying into the prospect of stable and growing income, whether through rental growth or repositioning, from core to improving or developing assets, all make sense today," says Robert Gilchrist, chief executive of European asset manager Rockspring Property Investment Managers.

Opportunities in aggregate are becoming scarcer as yields have come in over the past year or two. But, because of low inflation, the real rate of return is still fairly high, and property as an asset class remains good value compared to fixed-income investments. "There are still attractive pockets of value out there; you just have to know where to look," insists Gilchrist.

GLOBAL BACKDROP AT A GLANCE

Even with extreme cap rate compression in the United States, where the economy is in expansion mode and interest rates are likely to rise first, the outlook for real estate is strong, given high tenant demand yet muted new development. The market's transparency, stability and liquidity will continue to attract investors from around the globe, particularly from Asia as domestic markets are too shallow for investors to remain focused there.

The U.K. economy looks particularly healthy, with GDP growth forecast to be the strongest of the G7 nations for the second year running. With greater confidence among businesses and consumers, in an environment where little new stock has been delivered over the past seven to eight years, rental growth is picking up strongly and spreading out across the country.

Dramatic variation can be seen across continental Europe's economies. France is still trying to get into recovery mode, for example, while Spain has made enormous strides but is nowhere near regaining what it lost during the global financial crisis. Yet it is difficult to ignore what is an important economic block, despite recent issues surrounding a potential exit from the euro zone by Greece. Europe is expected to continue to draw global capital in search of relative value.

Set against a backdrop of ultra-low interest rates, Asian markets are very difficult at present. Following stellar performances in core markets such as Tokyo, Australia, Singapore and select provinces in China, yields have come in in line with very strong rental growth. Gaining exposure is one of the biggest hurdles, and markets often are accessed via investing in listed companies or taking a partnership approach.

Standout performers include Sydney and Melbourne, where cap rates are still higher, rental projections are steady, and institutional-quality investments are aplenty.

COLONY NORTHSTAR

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1987 Then and Now 2017

	1987	2017
CalPERS AUM	$50 billion (as of 1990)	$331 billion
U.S. GDP	$4.9 trillion	$18.8 trillion
U.S. Unemployment Rate	6.20%	4.30%
U.S. REIT Market Cap	$9.7 billion	$1.1 trillion
Super Bowl Champion	Washington Redskins	New England Patriots
NBA Champion	Los Angeles Lakers	Golden State Warriors
Stanley Cup Champion	Edmonton Oilers	Pittsburgh Penguins
Price of Gasoline	$0.90	$2.72
U.S. Population	242.3 million	326.5 million
Dow Jones Industrial Average	1,738.74	22,381.35
Average Cost of a New Home	$127,200	$313,309
Most Popular Television Show	The Cosby Show	Game of Thrones
Top Selling Movie	Three Men and a Baby	Beauty and the Beast
Bestselling Book	Patriot Games	Harry Potter and the Cursed Child, Part 1&2
President of the United States	Ronald Reagan	Donald Trump
Forbes Richest Person	Yoshiaki Tsutsumi	Bill Gates


Q2/2017 Fundraising Summary
Institutional Real Estate
FundTracker


2017 Institutional Investors
Real Estate Trends
21st Annual Investor Survey
Conducted by:
Kingsley Associates
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Institutional Real Estate, Inc.

PORTFOLIO


September 2017 | A publication of Institutional Real Estate, Inc.
REAL ASSETS
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The Best Unmade Plans
Chevy Chase Trust CIO Amy Raskin
never drafted a professional blueprint,


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The investor-focused global infrastructure investment publication
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We’ve Come a **Long Way**

A lot has changed, but some things remain the same

A lot has changed since Institutional Real Estate, Inc. started operations in 1987. Technology has greatly transformed all facets of our world, from our daily personal lives to business operations. Political, social, economic and demographic changes have altered maps, as well as capital flows. Today’s global marketplace presents investors with new challenges and new opportunities.

Since we published the premiere issue of *The Institutional Real Estate Letter* in 1989, we have seen the breakup of the former Soviet Union, the emergence of China as an economic power, the formation of the euro zone (and more recently, the Brexit referendum in the United Kingdom), the exponential growth of the Internet and related e-commerce, and a major global financial crisis. During that same time, real estate slowly gained acceptance as an asset class. Real estate AUM by tax-exempt investors in the United States mushroomed from approximately $120 billion to approximately $600 billion today. The U.S. REIT market equity cap jumped from $5 billion to more than $1 trillion.

During the past three decades, IREI’s coverage of the institutional real estate industry has expanded as well. We now publish three regional monthly magazines: *Institutional Real Estate Americas* (the original publication, retitled), *Institutional Real Estate Europe* (launched in 2007) and *Institutional Real Estate Asia Pacific* (launched in 2009). Each publication is investor focused, with contents that provide institutional investors in each region with information, perspectives and insights on regional and global investment trends.

Way back in 1994, we launched a weekly subscription news service, *Institutional Real Estate Newsline* (IREN), which was a digest of the week’s top news stories, gleaned from hundreds of news sources. The fax publication evolved with advancing technology to become a daily email newsletter.

In addition, IREI offers industry participants 24/7 access to news, videos, podcasts and special reports on its website, irei.com.

While the world has changed dramatically in the past 30 years, and IREI’s menu of products has expanded to meet the needs of institutional investors worldwide, the company’s publishing mission has remained the same: to be the most reliable source of industry data and intelligence on the institutionalization and globalization of real estate.

Bigger Is Better

At least investors seem to think so as they fuel the "mega-fund" trend

Institutional Real Estate, Inc. has been tracking fund offerings and fundraising data since the 1980s and has been publishing news and data on these activities since the first issue of *The Institutional Real Estate Letter* published in 1989. It wasn't until 2009, however, that the firm started publishing its quarterly fundraising summary, *Institutional Real Estate FundTracker*.

Today, the firm's robust database of historical and current funds includes information on more than 1,340 investment managers from around the globe and data on approximately 4,450 fund offerings. The FundTracker database also includes information on institutional real estate investors, including public and corporate pension funds, endowments, foundations, sovereign wealth funds, and insurance companies.

Similar to the rest of the institutional real estate investment world, the scope, size and diversity of real estate fund offerings have changed dramatically during the past several decades. In January 1990, for example, *The Institutional Real Estate Letter* reported 76 closed-end funds were currently in the market seeking to raise a total of $18.4 billion. Today, there are nearly 600 closed-end funds currently in the market.

Fifteen to 20 years ago, so-called "mega-funds" — funds raising $1 billion or more of equity — were a rarity, something that generated "oohs" and "aahs" from industry participants and observers; today they've become commonplace. Examples of some "early" big fund closings included Goldman Sachs' Whitehall Street Real Estate Fund IV, which wrapped up fundraising in 1996 with $1.35 billion; Westbrook Partners' Westbrook Real Estate Fund III, which closed in 1998 with $1.2 billion; and Lone Star Partners' Lone Star Fund III, which closed in 2000 after raising $2.3 billion.

Fast forward to the real estate cycle market peak of 2007–2008, when the real estate asset class was riding a wave of popularity and setting record levels of fundraising activity. Fund sponsors raised $134.7 billion of equity in 2007 and followed that up with a record $134.9 billion in 2008. Mega-funds were abundant. During 2008, for example, 41 mega-funds reached a final closing, including the largest fund ever at the time, Blackstone's $10.9 billion Blackstone Real Estate Partners VI.

Fundraising registered a marked slowdown in fourth quarter 2008 due to the developing global financial crisis, and then completely hit the brakes in 2009. That year saw fundraising volume plummet to a record low $41.9 billion as investors moved to the sidelines due to market uncertainty.

As governments around the world addressed the crisis, property markets slowly recovered during the ensuing years, and fundraising embarked on an upward trend until eclipsing the $100 billion mark in 2015 with a total of $110.0 billion. Blackstone attracted more than its share of capital, breaking its own fundraising record by collecting $14.5 billion for Blackstone Real Estate Partners VIII.

And mega-funds have again taken center stage as investors flock to these large investment firms with global strategies and proven track records.

When we look back at capital raised by year, it is possible that 2015 will turn out to be the peak in this current cycle. In 2016, fundraising dipped to $99.1 billion and continued to slow in the first half of 2017, totaling only $46.7 billion.

In 2013, mega-funds accounted for about 58 percent of the capital raised. In 2014, that percentage rose to 61 percent, with these large funds bringing in 65 percent of the total capital in 2015. Last year, the percentage of capital raised by mega-funds fell to 59 percent of the total capital raised. The trend line, however, turned up again in the first half of 2017, with mega-funds accounting for 62 percent of the total capital raised.

Whether or not the mega-fund will be a mainstay of the fundraising landscape for years to come, only time — and *FundTracker* — will tell.

Global Infrastructure Market Continues to Evolve


INSTITUTIONAL INVESTING IN INFRASTRUCTURE

September 2017
SPECIAL PRINT EDITION

The investor-focused global infrastructure investment publication

www.i3-infrastructure.com

Institutional investors seek to fill funding void

When IREI launched *Institutional Investing in Infrastructure (i3)* in 2008, the financial world was in the midst of a crisis, and the timing for making commitments to infrastructure was not ideal. Now, nearly 10 years later, markets are back and real assets investing is gaining a larger share of institutional portfolios as an opportunity to acquire investments that are uncorrelated to traditional equities and fixed income.

The issue infrastructure is having now is not too little interest but perhaps too much. Capital flows to the asset class have rebounded, and funds are reaching record levels. Competition for investments is intense, too, and infrastructure investment in the United States has become a focal point for the Trump administration.

i3 was launched in anticipation of this growing interest in infrastructure investing, first as a quarterly print publication and supplement for IREI's infrastructure conference, and then as a monthly digital publication in 2009. Currently, the *i3* publication is offered to subscribers in a digital format, but there are also four special print editions per year.

Beginning in 2010, several investment managers and a placement agent became sponsors of the publication, which expanded *i3's* coverage and readership with the support of an editorial advisory board. Today the roster of sponsoring firms has grown to 11 organizations, all leaders in the industry who are helping to underwrite the *i3* publication and deliver this valuable information on the asset class and investment markets to institutional investors.

Our annual editorial advisory board meeting — which includes investors, consultants and investment managers — gives the institutional investment community an opportunity to speak openly about the challenges and opportunities of investing in global infrastructure markets with an emphasis on the point of view of the investors — the public and corporate pension plan sponsors, the insurance company investors, sovereign wealth funds, foundations and endowments. It is at these meetings where the *i3* publication develops its ideas for future feature stories and other content within the publication.

Today's market looks a lot different than the one in which *i3* was launched. Investors have a host of new benchmark tools — listed, unlisted, equity and debt — at their disposal as well as new funds and investment structures, including investor clubs and specialized investment funds targeting middle-market investments, infrastructure debt and alternative energy. They also have the benefit of hindsight as investment managers launch the next iterations for funds, and investors can see a roundtrip from commitment to capital call and investment to exit and the return of capital.

Perhaps over our next 10 years, the market will have segmented further and several more specialist investment managers in the different sectors will be operating billion-dollar funds. And *i3* will continue its evolution to provide information and insights to institutional investors and their managers who are seeking to access the diverse and growing opportunities within the asset class.

IREI Enters Private Wealth Advisory Market

Making the case for alternatives in individual investor portfolios

Real Assets Adviser — the latest publication among the seven titles published by Institutional Real Estate, Inc., and the only non-institutionally-focused of our magazines — is now three years in the making. It is the product of two landmarks: 1) Research, such as that outlined by Casey, Quirk & Associates and Merrill Lynch & Co. in their landmark study, *The Brave New World: Winning Product Strategies for a Changing Global Market*, which built an almost irrefutably strong case for including alternatives in the portfolios of institutional and individual investors alike, and 2) a strategic decision made by the IREI board of directors to expand the company's operations to serve a broader market, the professionals advising the individual investor marketplace.

The Brave New World research report noted that including alternatives in investor portfolios was particularly beneficial in the low-return, higher-risk environment that was emerging at the time, which, the report argued, was undermining the effectiveness of the traditional 60 percent equities/40 percent fixed-income allocations to which most investors and advisers had become accustomed. *Real Assets Adviser* has taken up this cause, though, rather than covering the full spectrum of alternatives (which includes virtually anything beyond stocks and bonds), the magazine is focused on the subset of alternatives known as real assets. In other words, tangible hard assets such as real estate, infrastructure, energy systems and commodities ranging from oil and natural gas to precious metals and farmland crops and beyond. These are assets that tend to protect investor portfolios during times of high inflation, rising interest rates and market volatility — the very market forces so many advisers and investment officers worry about today.

In essence, *Real Assets Adviser* is an educational tool and information infrastructure to support advisers incorporating real assets into their client recommendations. In doing so, the company is supporting the creation of a market for the investment managers who are offering real-asset product solutions to the clients of those advisers.

This effort has received the backing of industry-leading firms such as AI Insights, Argosy Real Estate Partners, CBRE Clarion Securities, Deutsche Asset Management, EPUS Global Energy, KBS, Mick Law P.C., Morgan Stanley, Pender Capital and Preferred Apartment Communities, all of which are currently sponsors of the magazine. This sponsorship program underwrites the publishing and delivery of this monthly magazine to more than 65,000 RIAs, broker-dealers, family offices, and other industry participants. That is just a start. We expect sponsorship support and involvement to broaden, particularly among organizations from the investor and investment manager communities that stand to benefit the most from the march from traditional two-dimensional portfolios to multi-dimensional portfolios constructed with real assets and other alternatives, in addition to stocks and bonds.

There are great things ahead for the private wealth advisory business and its growing involvement with real assets, and we expect *Real Assets Adviser* magazine to facilitate this important evolution of diversification and portfolio theory.


CONGRATULATIONS
TO IREI FOR 30 YEARS
OF EXCELLENCE.
KINGSLEY
ASSOCIATES
Kingsley is a proud partner of IREI for over 20 years.
Together, we produce the annual Global Investor Survey, the leading source for institutional real estate investment trends.
To learn more about Kingsley, visit www.kingsleyassociates.com.


Courtland Partners, Ltd. is pleased to celebrate IREI's 30 years in publishing and to Geoffrey Dohrmann's success and foresight, envisioning the growth of an industry that Courtland is proud to be a part of.
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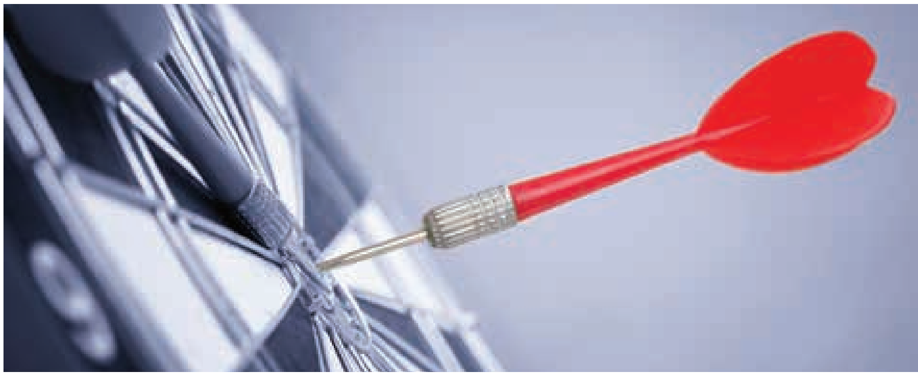
Investor-Focused Events Hit the **Mark**

IREI conferences promote high-quality content, networking opportunities

About 10 years ago, at the urging of a number of institutional real estate industry participants, Geoffrey Dohrmann, president and CEO of Institutional Real Estate, Inc., developed the concept for a new conference. At the time, there were already many real estate events in the industry; however, they were typically geared to investment managers and marketing (what is know in the industry as "pay to play"). The focus of the new event would be on the *investor*; it would feature a highly interactive format; it would be held at a high-quality venue conducive to creating an environment of learning, networking and relationship building; it would maintain a strict ratio of three investment managers to one investor, thus providing a more comfortable environment for investors; and, most importantly, the conference would be a "marketing free" zone, with the focus instead on high-caliber content and speakers.



The new conference was named Visions, Insights & Perspectives (VIP), and the first event took place in February 2007 at the Arizona Biltmore Resort in Phoenix. There was a sizeable crowd of more than 150 attendees. It was a high-energy event that created a lot of industry buzz. Since then, the annual event has grown to more than 350 attendees, and the past few years, it has been sold out with a waiting list to attend.

Early on, the event was designed to be dynamic and interactive with the audience. One element was the creation of peer-to-peer sessions or roundtable discussion sessions. These discussions are structured networking sessions that are designed for attendees to discover new insights and build relationships. This part of the program has become one of the highlights of the event.

Since the beginning, IREI has kept with the focus of serving the institutional real estate investor community with programing and structure evolving over time. The conference has had excellent speakers and content throughout the years, while developing a more focused program that delivers value to attendees. The event's topical agenda and timely insights are due to the guidance and input of a dedicated conference advisory board, which results in quality content and speakers each year.

A few years ago, VIP decided to change the structure of the conference advisory board from being a blend of managers and investors to an all investors board. This shift has helped to create an event that's even more investor driven and focused.

With the success of VIP Americas, IREI launched VIP Europe in 2012. The event also has gained a strong following and attendance continues to grow. In addition, IREI's conferences division produces several other annual events: IREI Springboard, an exclusive, invitation-only gathering of some of the institutional real estate industry's brightest, young executives; IREI CEO Summit, an exclusive, intimate, invitation-only gathering of some of the chief executives at the industry's leading investment management firms; and Institutional Investing in Infrastructure, a conference designed for institutional investors and investment managers investing or interested in investing in the infrastructure asset class.

We look forward to seeing you at our next VIP America's conference, which takes place Jan. 24–26, 2018, at Monarch Beach Resort in Dana Point, Calif.

Twenty-One Years and Counting

A report for investment managers and other real estate organizations

The *Institutional Investors Real Estate Trends* survey/report is published by Institutional Real Estate, Inc. in conjunction with Kingsley Associates on an annual basis.

The survey/report, which was launched in 1996 and was originally known as the *Tax-Exempt Real Estate Investment* survey, is prepared for investment managers and other real estate organizations that sponsor Institutional Real Estate, Inc. publications, and for the nonsponsoring editorial advisory board members of *Institutional Real Estate Americas*, who support our efforts with their time and advice.

The purpose of the annual investor survey is to provide relevant data and analysis to help tax-exempt funds and the organizations that serve them (investment advisers, REITs and consultants) pinpoint and understand the implications of the important investment trends that are most likely to drive the markets during the year ahead.

Kingsley Associates and Institutional Real Estate, Inc. work together to design and implement the annual investor survey, utilizing feedback from the members of *Americas'* editorial advisory board, who suggest changes to the survey design. The questionnaire includes quantitative, open-ended and categorical questions focusing on the following topics:

- Plan type and fund size
- Allocations and risk/return assumptions for investment vehicles
- Allocations and risk/return assumptions for real estate investments
- Satisfaction with and future plans for real estate investments
- Expected capital flows to real estate and search plans for investment managers
- New capital allocations by global real estate strategies
- Property type and region interest for real estate investments

Institutional Real Estate, Inc. establishes a database of potential respondents, and Kingsley Associates distributes an invitation email with a link to the web survey to potential respondents. As the survey responses are collected, Institutional Real Estate, Inc. and Kingsley Associates verify the responses.

Institutional Real Estate, Inc. and Kingsley Associates received 71 responses to the inaugural survey and that number has grown to 164 responses to the 2017 survey.

The survey initially collected responses from only U.S. investors, but now it covers a global universe of investors and has grown to 113 U.S. investors and 51 foreign investors for the most recent edition.

The **Best** of Both Worlds

iREOC seeks to enhance the relationship between institutional investors and REOCs

In 1992, relationship counselor, lecturer and author John Gray published his book *Men Are from Mars, Women Are from Venus*, which went on to spend 121 weeks on the *New York Times* bestseller list. The book's thesis is relationship problems between men and women are rooted in fundamental psychological differences between the sexes.

Similar "relationship issues" are inherent in joint ventures between institutional investors (typically represented by their investment managers) and real estate operating companies. A match between the two interests makes perfect sense: The operator gets access to capital, and the investor (via an investment manager) can tap into the operator's expertise, local market knowledge and deal flow. But, like men and women, these two interests come from different planets. One is tax-exempt; one is taxable. One is institutional; one is entrepreneurial. Institutions invest, via their investment managers, on behalf of the investor's beneficiaries; real estate operating companies invest to maximize profits for the REOC's owners.

Enter the Institute for Real Estate Operating Companies (iREOC), a membership organization launched in 2016 by Institutional Real Estate, Inc. The group's mission is to facilitate and enhance relationships between institutional capital providers and real estate operating companies through a program of training, education and consulting services, as well as networking events.

The original subtitle for John Gray's book also could describe the purpose of iREOC: *A Practical Guide for Improving Communication and Getting What You Want in Your Relationship.*

The underlying premise of the iREOC is to help real estate operating companies understand the distinct language, culture and fiduciary requirements associated with serving institutional capital, while promoting the creation of more efficient, more effective, more profitable and more collaborative real estate operating partnerships.

The iREOC seeks to serve as a catalyst for meaningful and positive industry change focused on improving the quality of service provided to institutional investors by their investment managers and real estate operating company partners, while delivering value to all its members and sponsors.

The organization's mission is to accelerate the development and adoption of workflow process improvements in:

- information standards
- proven practices
- collaboration
- transparency

These improvements will enable institutional investors and investment managers to increase returns, lower costs and reduce risk in their partnership investments with real estate operating companies.

For more information on the iREOC, visit **www.ireoc.com**, or contact executive director **David "Mac" McWhorter** at +1 970-300-8024.

IREI's unique publishing model is based on underwriting — or sponsorship — from many of the industry's top investment advisory firms and service providers. It is through this program that qualified institutional investors are able to receive our publications free of charge. Over the past three decades, the list of sponsor firms in the real estate, infrastructure and real assets arenas is a virtual Who's Who of investment managers.

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American Realty Advisors
American Realty Capital
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AMRESCO Advisors
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Andersen
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Madison International Realty
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The Mayer Group
Mellon/McMahan Real Estate Advisors
Meridiam Infrastructure
Mesa West Capital
MetLife Real Estate Investors
Metric Institutional Realty Advisors
MGPA
Mick Law PC
Midland Advisory Services
The MIG Companies
MIG Realty Advisors/Associated Estates

MIM Property Services
MMA Realty Capital
Monday Capital Partners
Morgan Stanley
Morgan Stanley Dean Witter Investment Management
Morrison Foerster
MSCI
National Association of Real Estate Investment Managers
National Real Estate Advisors
Net Lease Partners
New City Asia Fund Management
Newland Capital Advisors
Newmark & Co. Real Estate
O'Connor Capital Partners
The O'Connor Group
Orrick, Herrington & Sutcliffe
Pacific Pension & Investment Institute
PaineWebber Real Estate Fund Management
Paladin Realty Partners
Paramount Group
Parmenter Realty Partners
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PCCP
Pearlmark Real Estate Partners
Pembrook Capital Management
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Presima
PRICOA Property Investment Management
Principal Real Estate Investors
Prologis
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PGIM Real Estate
Prudential Real Estate Investors
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UBS Global Asset Management Global Real Estate
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USA Capital Realty Advisors
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The Yarmouth Group
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About Institutional Real Estate, Inc.

Founded in 1987, Institutional Real Estate, Inc. (IREI) is a global media firm recognized as a critical nexus for the sharing of industry intelligence, knowledge and insights on the institutional real estate, infrastructure and real assets marketplaces through its publications, events and consulting services.

PUBLICATIONS

IREI publishes a diversified portfolio of news publications, special reports and investment guides for the benefit of the global institutional investor community. Each publication provides subscribers with news, insights and perspectives on the trends and events shaping the investment landscape. We also offer daily news, speical reports, videos and podcasts on our website, www.irei.com.

The firm's flagship publication, *Institutional Real Estate Americas*, has covered the industry for 29 years. Other IREI titles include:

- *Institutional Real Estate Europe*
- *Institutional Real Estate Asia Pacific*
- *Institutional Real Estate Newsline*
- *Institutional Investing in Infrastructure*
- *Institutional Real Estate FundTracker*
- *Real Assets Adviser*

CONFERENCES

In 2006, the firm launched a conference and seminar division. IREI's events have quickly gained a stellar reputation and solid following within the industry. The firm's menu of events includes:

- Visions, Insights & Perspectives (VIP) Americas
- Visions, Insights & Perspectives (VIP) Europe
- Institutional Investing in Infrastructure (i3)
- IREI Springboard
- IREI CEO Summit

RESEARCH & CONSULTING

IREI has more than two decades of experience providing research and advice to the investment management, brokerage, development and infrastructure communities. Services include:

- Strategic information and advice on presentations
- Organizational structures
- Product development
- Proposal responses

ONLINE DATABASES

IREI's data services department manages a number of proprietary real estate and infrastructure databases that track hard-to-find industry information. In addition, a good portion of the information housed in our databases is tracked exclusively by IREI. Our most popular databases include:

- Investments Database
- Investors Managers Database
- Consultants Database
- Placement Agents Database
- Funds Database
- Fees Database
- Commitments Database
- Transactions Database

You can access information from these databases anytime with a subscription to our FundTracker database.

OTHER INITIATIVES

IREI launched the Institute for Real Estate Operating Companies (iREOC) in 2016. This membership organization was formed to bring together and engage leading professionals from across the institutional real estate investment and built environment industries to focus on helping institutional investors, investment managers and real estate operating companies to form more collaborative and effective investment partnerships through thought leadership, improved information standards and proven practices in workflow processes, and education.

For more information, visit **www.ireoc.com**.


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Congratulations, IREI, on your 30th anniversary!
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