CapRock Partners

A nimble middle-market, western U.S. industrial strategy gives flexibility, control

Recently, **Jonathan A. Schein,** senior vice president and managing director of global business development for Institutional Real Estate, Inc., spoke with **Jonathan Pharris,** president and co-founder of CapRock Partners, about the firm's value-add industrial and logistics development platforms. Following is an excerpt of that conversation.

What distinguishes CapRock from its competitors?

We are geographically focused and only invest in a single product: industrial. We are focused on the western United States — most specifically California, Arizona and Nevada — and every one of our assets is within an hour and a half from our headquarters in Orange County. That might mean an hour flight to Phoenix or Northern California, or an hour drive to the U.S.-Mexico border, or an hour to the Inland Empire. As a result of our focus, we know the industrial submarkets incredibly well and develop very deep networks directly with sellers and brokers. The company tagline is *Institutional Quality, Entrepreneurial Approach.* We consistently execute on thoughtful investment opportunities quicker than others and often view investment opportunities through a different lens than others. At our core, we are an entrepreneurial company, but with the sophistication, capital support and back office of larger institutions.

How would you describe your strategy within the overall industrial market?

We invest in two strategies throughout the western United States: middle-market, value-add industrial and class A logistics developments. Our middle-market focus usually results in high-quality, value-add investment opportunities valued less than $50 million. The buildings within that category can look very different — a single-tenant, 300,000-square-foot building; a business park with 20 different tenants; an asset with excess land that, given our development expertise, we could re-entitle, monetize and develop; or a multitenant, mid-bay building — the point is that we have a lot of flexibility within our value-add platform to create individual business plans for each asset in order to generate value for each specific project.

Our second platform is focused on large-scale logistics developments in California, Arizona and Nevada. In the Inland Empire, we are currently building the largest speculative industrial project in the country on behalf of global real estate investor Ivanhoé Cambridge: the 150-acre, approximately 3,000,000-square-foot Colony Commerce Center. In 2020, we are slated to commence construction on upwards of an additional 4,000,000 square feet throughout the western United States, with a similar pipeline for 2021.

Ground-up development is usually considered opportunistic. Do you still call that value-add in your strategy?

No, we distinguish our value-add platform from our development platform. In our viewpoint, development is cyclical. We are one of the leading developers in our geography, but we are very cognizant of the fact that development ebbs and flows. Our focus since CapRock's inception in 2009 has been on value-add investments — more than 70 percent of all the deals we have done are value-add deals, and that will continue to be our strong core focus as a company.

Why industrial / logistics?

I view industrial and logistics as two distinct platforms and product types. The term logistics has replaced "big-box industrial." Our logistics platform is focused on new construction with class A amenities for projects larger than 400,000 square feet that are usually leased to *Fortune* 2,000–type companies, with 32-foot to 40-foot clear heights (or larger), excess trailer parking stalls, and direct access to major freeway systems.

On the other hand, I define general industrial as smaller-box buildings that are less than 300,000 square feet and do not need to be new construction. The two investment types have very distinct risk-and-return profiles. Even with the growth of e-commerce and advent of last-mile logistics — and that growth continues to be incredibly strong across different companies — we still need to provide traditional industrial buildings throughout the West for entrepreneurial companies who may not need class A amenities or large clear heights. These traditional industrial buildings are still the bread and butter of the overall 3.1 billion square feet of industrial space in California, Arizona and Nevada.

You have a very specialized, focused team. How do you go about recruiting them?

One of the key ways we are able to differentiate ourselves is our speed to execution because all of our investment specialists are just that — specialists. They only do industrial, and they only do it in our territories. We have multiple investment specialists within CapRock, and we are very big about hiring and promoting from within. We have created a unique culture at CapRock — there are no private offices; everything is open. My business partner, Pat Daniels, and I sit in the middle of the bullpen just like everybody else, so there is constant flow of communication on deals that we should be either passing on, or taking a deeper dive on. From a hiring perspective, our brand recognition and our collegial environment set us apart.

Can you give us a high-level overview of your growth strategy and investment strategy?

As we look at where CapRock is going to be in three years, in five years, in 10 years, we will continue to be industrial specialists focused on our two platforms: value-add and logistics development. Geographically, an expansion into the Pacific Northwest is logical since we are a port-centric company, and there are three main ports on the West Coast: Los Angeles/Long Beach, Oakland and Seattle. We are already active in the Oakland and Los Angeles/Long Beach port areas, and the next geographical investment opportunity will be Seattle and Portland, Ore. Approximately 60 percent of all goods that come into the United States come in through the West Coast ports of Seattle, Oakland, and the combined Los Angeles/Long Beach, so we will continue to be specialists in those areas.

You are about to close your third value-add fund, which makes that your fifth fund overall. What are the goals and objectives for this particular fund?

Our value-add fund III will focus solely on middle-market industrial properties within the western United States and small infill land parcels, where we can utilize our development expertise to build buildings that are generally less than 100,000 square feet. The vast majority of the focus will be on repositioning existing industrial buildings throughout California, Arizona and Nevada. The typical investment size is between $25 million and $50 million, with a hold period of less than five years. Most will have a significant repositioning component, and nearly all assets will have some sort of impaired cashflow at acquisition. We anticipate this fund will invest in more than 25 properties, which will provide appropriate diversification for our investors. While investing is not an exact science, we are targeting approximately half of our investments in California, with the balance split between Arizona and Nevada.

Do you have a certain amount you limit yourself to per fund?

We intentionally keep our fund size small. There is often the temptation to raise bigger and bigger funds, but if we did that, it would change the dynamic of our company. We feel it is more prudent to keep our fund sizes appropriate, so that we can continue to invest in the middle-market space. We recently held our first close and, based on the strength of that close and additional investor interest from top-tier institutional investors, it seems that this fund will be oversubscribed. This fund's hard cap is $250 million which, given our middle-market focus, translates into a range of 25 to 35 properties in our portfolio. Many of the larger funds are not in a position to invest in these middle-market opportunities, given their need to acquire portfolios or buy larger deals in order to efficiently deploy their capital. We have a strategic advantage with our fund since we can continue to focus on the relatively inefficient middle-market investment segment and not stray from our track record.

Finally, can you tell me a little about the investors in your funds?

We view our investors as partners. We are in constant communication with them. Our communication and reporting have helped us attract some of the marquee investors in the United States. Today's investors are not passive. They want a deeper understanding of each investment, why we view one investment as a wise investment and why we pass on others, and how we will create value. They want to understand supply-and-demand drivers in each submarket as they relate to each investment, and so the communication is very robust.

CONTRIBUTOR

Jonathan Pharris

President

CapRock Partners

Jonathan Pharris is co-founder and president of CapRock Partners, where he spearheads all acquisitions for the firm's investment funds, overseeing a team of best-in-class commercial real estate professionals. Upon full build-out of CapRock's current portfolio, Pharris will have successfully directed CapRock's acquisition and development of more than 17.5 million square feet of industrial product totaling more than $1.9 billion in value since 2010.

COMPANY OVERVIEW

CapRock Partners is one of the leading industrial investors and developers in the Western United States. The firm specializes in acquiring middle-market, value-add industrial properties, generally between $20 million and $50 million per acquisition, and large-scale, class A logistics developments in California, Arizona and Nevada. Since 2009, CapRock has acquired, successfully developed, or has in its immediate pipeline more than 17.5 million square feet of industrial real estate, totaling more than $1.9 billion.

CONTACT

Tel: +1 (949) 342-8000

1300 Dove St., Suite 200 | Newport Beach, CA 92660

www.caprock-partners.com

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