Alternatives April 15, 2019

At Pension Bridge: Finding Opportunity in Real Estate

What's working now and how to take advantage of what isn't.

When in doubt about asset allocation, real estate is a sector that is coming in handy for institutional investors.

"I actually think we're in a great real estate cycle," said Anthony Breault, Oregon State Treasury's senior real estate investment officer, at the Pension Bridge conference in San Francisco. "It's a renaissance, quite frankly," he said, citing an abundance in multi-family housing and work office development.

The $77 billion sovereign wealth fund used to be a much more aggressive investor until about 2015, when it shifted to core real estate in a bid to be less risky. And it has paid off. "From a risk standpoint, I think we're a pretty good girl at the dance," Breault said. "I don't lose sleep at night whatsoever looking at core." Oregon Treasury has roughly $9 billion in the property space.

Other panelists, such as Paul Nasser, chief financial officer and chief operating officer of Boston-based Intercontinental Real Estate Corp., pointed out that evidence about any slowdown is scarce.

"I sort of come at things with a risk perspective, and yet, it's really difficult for me to see a lot of warning signs out there," he said, noting that a slowing from 5% growth to 3% is still growth.

The increasing speed of technology and other trends mean that real estate investors need to be nimble these days, the panelists contended.

"Real estate strategies that worked very effectively 10 or 15 years ago do not necessarily work very well today given changes," said Brian Nottage, managing director and head of research for US real estate at JP Morgan Asset Management. He pointed to a midtown Manhattan office building that once was a cash cow. Now, not so much.

"One big reason is the way that tenants use their space is changing, so they want to densify their space, they're willing to be in more places than they ever have been before," he said. "That is just a sea change, which has meant that a lot of buildings built during the ’60s and ’70s that have been traditional ‘A’ buildings are not ‘A’ buildings anymore, and they have to fundamentally re-price where they are.”

Another change Nottage noted was how warehouses were traditionally purchased in the middle of nowhere and are now being bought closer to the population, thanks to Amazon and other online retailers, who need to make fast deliveries to customers.

Regardless of change, there is always opportunity. Retail, a sector being disrupted by technology, is not looking too hot at the moment, but the Pension Bridge panelists believe the market will evolve and that there is always a way to revamp existing properties.

“I think you do buy retail right now, and I do think you take it, and I think you do invest it, and you change it,” said Tim Bellman, head of global research for Invesco Real Estate in the US, which has purchased old Sears department stores and repurposed them into hotels and apartments. “The challenge in the risk is that in the underwriting of those projects, you don’t allow for the incredible capex that you’re going to have to continue to put into those properties to make them continue to be successful.”

Other areas of interest include smaller, creative-type offices, multifamily apartments, and industrial developments.

By Chris Butera