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Family Offices Hungry For Real Estate Investments

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March 7, 2018

The ways in which ultra-high net worth, HNW and other investors can play the real estate sector continue to expand, and practitioners discuss sectors they see as hot and those less in favor.

Solid yields, inflation-resistant income streams and a lack of fancy-pants jargon or rocket-science cleverness are qualities explaining why good old brick-and-mortar investments aren't going out of style.

Whether it is privately-held real estate, listed trusts, development projects and forms of infrastructure, real estate investment continues to tick some of the boxes family offices and high net worth investors have. Rising equity volatility and the need for diversification means real estate's attractions - with some caveats - remain, practitioners say.

Sectors in residential real estate, such as multi-family housing seem to be common points of interest among investment firms *Family Wealth Report* has spoken to; another "hot" area appears to be student housing, as mentioned by several managers.

Waypoint Residential is a Boca Raton-based real estate investment management firm that has closed approximately 70 deals since 2011. The vertically-integrated company focuses on the acquisition and development of rental housing assets across the US, including conventional multi-family student housing and senior housing properties. In addition to its single real estate asset transactions, the firm also has a real estate fund.

Since inception, the firm has invested in approximately 22,000 units with a total capitalization of approximately $2.6 billion. Waypoint's owned assets are generating a current yield of approximately 7 per cent and the disposition of twenty-five assets have resulted in a 22 per cent internal rate of return.

"We seek to invest in assets and markets that are overlooked by others. We structure our investments with low leverage; the resulting high debt service coverage ratios mean that we are well positioned to withstand a major market downturn – it is our 'sleep well at night' strategy," said Scott Lawlor, Waypoint's CEO.

Waypoint's direct ownership investment model potentially provides a number of tax benefits, such as accelerated depreciation and capital gains treatment on sale. The firm also utilizes 1031 exchanges on sold asset which can defer gains on sale.

Understandably, perhaps, managers of real estate portfolios give upbeat messages about the asset class (it is rare for such investors to sound grumpy on the record). This year's survey of views among the world's ultra-high net worth investors by Knight Frank, the global real estate consultancy, found that while equities remained the darling asset class, 56 per cent of UHNW individuals on average reporting an increase in interest for holding real estate across the globe.

In the US, an issue to watch is how and when lenders tighten standards amid any further rises in US interest rates. The share of US banks reporting tightening standards for multi-family loans began rising sharply in early 2016, according to the Federal Reserve's senior loan officer survey, which tracks the activity reported by about 60 large US banks and two dozen US divisions of foreign banks (source: Forbes, other). Of course, if rates rise because the economy is improving, then real estate investors might still prefer such a scenario to one where rates are low because the economy – and therefore real estate sectors – are weak.

Cycles

"Investors realise we are at a mature part of the [economic] cycle and they tend to look for opportunities which present the most compelling and durable risk-adjusted returns," Philip McAndrews, head of real estate equity for the real assets team within Aegon Asset Management, told this publication. (He joined the firm at the start of January.) Aegon Asset Management oversees $375 billion of assets across different sectors. His focus is on private equity investment real estate (as opposed to listed real estate) and likes the multi-family housing sector at this point in the cycle. McAndrews noted that there is a currently a supply shortage in the workforce housing market and, based on demographic projections, it will remain supply constrained for years to come.

As a result of lacking new supply addressing the workforce housing demand, this is a tranche of the multi-family market where there are opportunities to refurbish buildings and eventually increase rents. Complementing their private equity investment program, Aegon Asset Management is also actively engaged as a commercial mortgage lender and has a substantial tax credit financing business, McAndrews said.

Family offices and organizations such as Registered Investment Advisors (RIAs) are interested in investing in multi-family properties, he continued. The yield and return characteristics as well as the diversification benefits, appeal to such clients, he said.

A different, but in some ways equally optimistic view on real estate comes from Frank Haggerty, who is portfolio manager at Duff & Phelps Investment Management. He co-manages the firm's Global Real Estate Securities investment strategies. The firm's Global Real Estate strategy has holdings in a number of countries, with US-based properties accounting for 54.5 per cent of the total, according to the fund's end-December, 2017 factsheet, with Japan in second spot, at 7.8 per cent. His firm also manages purely US real estate and an ex-US global portfolio.

Perhaps unsurprisingly, Haggerty, a veteran of real estate securities for 21 years, is positive on the listed property market, noting that listed real estate has lagged listed equities in general for more than two years and suggesting that, given some recent stock market volatility, now is a smart opportunity to consider REITs. "We are at a good moment in time," Haggerty said. History appears to bear him out when it comes to liking REITS: listed equity REITs delivered higher net returns than any other asset class from 1998 to 2015 according to a November 2017 report by CEM Benchmarking.

Haggerty said share price discounts to net asset values in US REITs can be in the low double digits – currently, the NAV discount/premium has swung within a corridor of plus/minus 20 per cent, or thereabouts. With a strong US economy and demand for property, the backdrop for US REITs is positive, he said.

Outside the US, markets such as those in Spain and Ireland – countries which had seen real estate sectors hit in 2008 – show signs of growth and promise, said Haggerty. In the UK, student accommodation is a property sector with attractive growth profiles, as is the case with self-storage and flexible workplace/office facilities. Another sector of note are logistic warehouses, such as those supplying e-commerce business models. And the rise of e-commerce has, by contrast, been a negative for traditional retail commercial real estate, he continued.

There are a variety of ways that HNW and UHNW investors can tap into real estate, and evidence appears to show that enthusiasm for one of the most traditional of asset classes hasn't dimmed yet. Of course, to coin a phrase, while history doesn't repeat itself exactly, it does rhyme, so investors will be mindful of previous episodes of when enthusiasm for real estate got out of hand. What does appear to be the case is that the options for how to play the market appear wider than ever before.