NYU STERN

Center for
Real Estate
Finance Research

Fourth Annual Fall Symposium: The Nexus Between Real Estate and Infrastructure Investing
Thursday, October 8, 2015

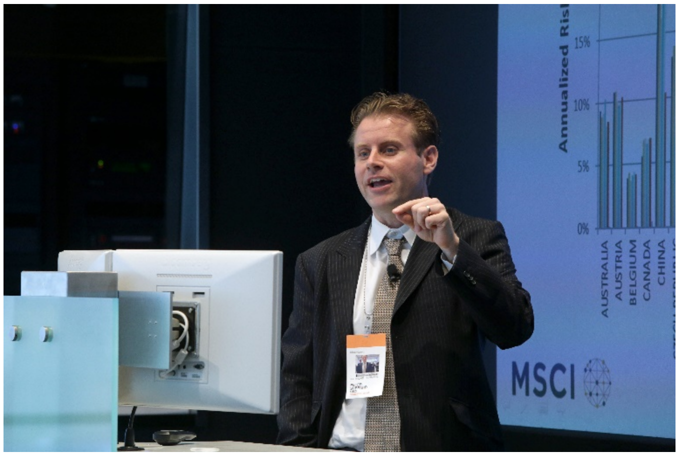
Conference Summary

On Thursday, October 8, 2015 over 200 industry professionals, academics, and students joined us for our half-day Conference on The Nexus Between Real Estate and Infrastructure Investing.

Our conference took place at Bloomberg headquarters and consisted of three panels: Real Estate and Infrastructure Assets, Institutional Investors in Real Estate and Infrastructure, and Green Building, New Energy and Green Finance. We were thrilled to welcome former mayor of San Antonio and former Secretary of Housing and Urban Development, Henry Cisneros, as our Keynote Speaker.

Panel 1: Real Estate and Infrastructure Assets: Risk & Return Characteristics

The first panel explored the risk and return properties of real estate and infrastructure assets in more depth.



Peter Shepard

Peter Shepard, Executive Director at MSCI, focused on the differences between listed and direct investment in real estate and infrastructure assets. He cautioned about extrapolating too much from appraisals. He also argued that many people have mistakenly put real estate towards the bond end of the spectrum. While the cash flows may be bond-like, risk in real estate is driven 90% by capital appreciation rates, which is a much more equity-like source of risk. Finally, he argued that different real estate sectors showed a lot of commonality within countries but not so much across countries. There is still a lot to gain from international diversification in real estate, a situation not unlike the one in equity markets 30-40 years ago.

Lars Dahl

Lars Dahl, Chief Risk Officer at Norges Bank Investment Management explained the real estate investment strategy of NBIM. The long-term goal of the fund is to preserve the international purchasing power of the Norwegian people. Real estate is an asset class which moves with growth in the world economy. The fund has invested in real estate since 2011 and currently allocates 2.7% of its portfolio to the asset class. About a quarter of the real estate portfolio is in listed assets with the rest in direct property; the fund does not use leverage. It has offices in 10 cities and collaborates with local partners. The focus is on high-quality assets in large cities that offer both size and future growth potential. They study metrics at the individual property level and then aggregate them up to the portfolio level.

Paul Tice

Paul Tice focused on infrastructure debt markets. Infrastructure will provide steady cash flows if contracts are structured correctly, but Paul argued that infrastructure is arguably more risky than real estate. The typical infrastructure deal has 70% debt and 30% equity. Infrastructure loans are illiquid investment grade assets, but with attractive diversification benefits with other asset classes. Not all institutional investors have the skill-set to analyze infrastructure debt, because of the complex covenants involved. Energy and renewables comprise about 60% of the sector. 75% of the market is in public hands, 25% is in the form of direct investment. The 12% default rate for projects in the U.S. is high – similar to the level of defaults found in Latin America.

As institutional investors continue to increase their allocations to global real estate and infrastructure and focus on core assets in top-tier markets, the benefits from international diversification will be exploited, and assets in the top locations will begin to co-move more strongly with each other.

Panel 1 (left to right): Stijn Van Nieuwerburgh (moderator), Lars Dahl, Peter Shepard, Paul Tice

Panel 2: Institutional Investors in Real Estate and Infrastructure

The second panel discussed the role of institutional investors in real estate and infrastructure investment. The discussion started with where we currently are in the real estate market cycle.

Thomas Garbutt

Thomas Garbutt, Senior Managing Director and Head of Global Real Estate, TIAA-CREF argued that markets are certainly tougher than last-year and require a high-level of investment discipline. However, compared to other asset-classes, the spread of cap-rates to Treasuries still tell a story of acceptable risk-return tradeoffs, combined with supply-constraints and upward pressure on rents. TIAA takes a holistic portfolio perspective when investing in real estate deals. Garbutt believes that building large real estate allocations may increasingly require acquisitions of other platforms rather than going building by building.

Barry Blattman (left) and Martin Cohen (right)

Barry Blattman

Barry Blattman (MBA ’86), Senior Managing Partner, Brookfield argued that there are always opportunities for investors of certain size and scope. He sees opportunities in countries such as Brazil, China and India for transformational deals while the U.S. and U.K. provide access to more “block and tackle” opportunities; however, there are always unique opportunities such as their recent $4B deal to take control of London’s Canary Wharf. Also, his team follows a vertically integrated approach for growth and looks to own dominant platforms in the cities where they operate. Brookfield is focused on the best portfolio not necessarily the most diversified.

Martin Cohen

Martin Cohen, Chairman of Cohen & Steers, is attracted to real estate due to the upward sloping value over time for well-located and managed properties. With $300B in dry-powder for real estate funds putting a floor under the market, he believes there remains considerable value in real estate today for long-term investors. REITs are trading at a 5% to 15% discount to Net Asset Value, suggesting they could be attractive take-over targets.

He also thinks there will be an M&A wave in the real estate sector.

Nicolas Firzli

Nicolas Firzli, CEO of the World Pension Council, believes that QE is at the root of the current investor demand since central banks have set interest rates at all-time lows and printing money. Investors are looking at real estate as a place to park their money. The average pension fund or sovereign fund is looking at their funds and seeing that they are currently earning 0% on up to 50% of their assets while having to meet investment mandates of 8%, so their quest for yield is pushing them into real estate and infrastructure.

Panelists also shared their views on the opportunities in the infrastructure space over the next twenty years and shared a belief that the sector would outpace the growth experienced by real estate. Several argued that infrastructure today is at the same point in its development as real estate was twenty years ago. Finally, panelists shared the skills they believed are necessary for success in the infrastructure investment space. The skill sets overlap strongly with those of successful real estate investors.

Cohen argued that regulation adds another level of complexity to infrastructure deals and warrants additional consideration, but when you consider the $30T in infrastructure investment needed and the limitations of current governments to fund it, then public markets are well-positioned to provide financing for this opportunity. He believes infrastructure financing may go the way of REITs in the future.

Firzli sees the future as more club-deals between governments and asset managers and as co-investment opportunities between the World Bank and governments/investors. One benefit is that given the huge amount of financing required for infrastructure assets, it may be beneficial to have large anchor investors.

Blattman observes that infrastructure deals were originally marketed as private equity-type deals with 20% return targets. Then the returns moved to the 15-18% range; they are coming down further still as investors start to become aware of the lower levels of risk in many assets. He expects infrastructure to grow at a much faster pace than real estate did. The more the infrastructure investor has to be exposed to politics, the higher the risk. The future is being written now.

In terms of the skills students will need in infrastructure, Cohen emphasized a good foundation of finance. Keep your mind and eyes open for opportunities while you start in real estate. Garbutt thinks that the growth curve will be steeper than in real estate. Students should try to get exposure to a wide range of transactions rather than being knee-deep in one so as to experience the full learning cycle.

Panel 2 (left to right): Stijn Van Nieuwerburgh, Martin Cohen, James Stolpestad (moderator), Barry Blattman, Thomas Garbutt, Nicolas Firzli

Panel 3: Green Building, New Energy, and Green Finance

The “Green Building, New Energy, and Green Finance” panel was comprised of professionals representing the public, private, nonprofit, and higher education sectors who presented on how their organizations are addressing sustainability issues in real estate and infrastructure.

Ethan Zindler (left) with Nilda Mesa (right)

Ethan Zindler, Head of Americas, Bloomberg New Energy Finance moderated a discussion between Nilda Mesa, Director of the NYC Mayor’s Office of Sustainability, Constantine Kontokosta, Deputy Director for Academics at the NYU Center for Urban Science and Progress (CUSP), Nils Kok, CEO of GRESB and Associate Professor of Finance at Maastricht University, and Douglas Durst, Chairman of The Durst Organization.

Nilda Mesa

Nilda Mesa presented an overview of how the NYC Mayor’s Office of Sustainability is focusing their efforts on addressing climate change in the built environment. In 2014, Mayor Bill DeBlasio committed the city to reducing carbon dioxide emissions 80% by 2015. Nilda noted that buildings, responsible for 70% of NYC’s carbon emissions, are essential to accomplishing this goal. Existing buildings have been a focus of Nilda’s team. The City of New York has retrofitted a quarter of city-owned buildings with energy saving improvements resulting in over $40M in energy savings to date. The city has also has developed a Building Retrofit Accelerator to assist building owners in doing the same.

Constantine Kontokosta

Constantine Kontokosta shared CUSP’s research with the audience. CUSP has been aggregating massive amounts of data on New York City’s energy consumption and greenhouse gas emissions. CUSP is working to use technology and data to understand building and neighborhood-level performance with a view towards targeting efforts where the largest energy efficiency gains can be reaped. CUSP is also developing the city’s first “Quantified Community” with The Related Companies at their Hudson Yards project. This initiative will be using sensors to collect a vast amount of information on everything from air quality to trash receptacle usage. The goal is to use data to improve quality of life and the efficiency of the built environment.

Nils Kok

Nils Kok presented on three emerging sustainability trends for real estate investors. First, Nils discussed how governments, like the EU, are phasing out inefficient buildings. Regulation in the US is also moving in this direction as required disclosure of building performance is becoming commonplace. Second, investors should consider how real estate relates to important issues of water, public health, resiliency, and labor practices. Lastly, he found that high sustainability (GRESB score) buildings command a pricing premium.

Douglas Durst

Douglas Durst spoke about how the Durst Organization has pioneered Environmentally Responsible development. When they build 4 Times Square, Durst and their development team focused on reducing energy consumption. 1 Bryant Park was designed to improve the health and wellbeing of its occupants and is now a case study for the benefits of improved tenant health and productivity. Currently, Durst is working to develop a central power production and distribution plant at Hallets Point, a 2.4 million square foot residential development in Queens. Durst plans to reduce energy consumption with highly efficient equipment, controls, and technology.

Panel 3 (left to right): Stijn Van Nieuwerburgh, Ethan Zindler (moderator), Nils Kok, Nilda Mesa, Constantine Kontokosta, Douglas Durst

Keynote Speech

Henry Cisneros

Henry Cisneros, current Chairman of CityView and longtime politician, provided the conference's much-anticipated keynote address. Touching upon his past experiences as the Mayor of San Antonio, Texas and the Secretary of Housing and Urban Development under President Clinton, Mr. Cisneros blended a profit-seeking businessperson's perspective with a macro-level view towards the sustainability and growth of urban environments across the country. Perhaps most notably, Mr. Cisneros posited that real estate professionals must tie themselves to the future success and progress of urban environments. Improved infrastructure is imperative for the future success and security of the country, and, he argued, there is an economic incentive to pursue that path.

Reiterating and reinforcing the concepts of many of the preceding panelists, Mr. Cisneros noted the pervasive physical similarities between real estate and infrastructure. He noted that infrastructure and real estate both have large scale public effects, alter the physical landscape of the country, have a drastic impact on environmental issues and sustainability, and that developments in both are integral in the shaping of cities. Smart investors, he added, are including infrastructure in the traditional list of real estate asset types. The definition of infrastructure is evolving and now includes support systems for the technology economy and the social economy it makes possible.

Mr. Cisneros additionally pointed out a number of items that require new thinking in order to serve constantly evolving, high-tech urban communities. We need to build for sustainability, energy conservation, water and building materials. Technology must become embedded into the fabric of development - building sensors in roadways to determine congestion levels, for example. Infrastructure that supports advanced industries such as universities and medical centers are vital in new, urban economies, and we must turn a keen eye towards density and walkability, designing comprehensive new communities complete with well thought-out public amenities.

Turning towards the current environment, Mr. Cisneros noted that much existing infrastructure is old, slow, unkempt and out of date. In order to remain relevant, cities must focus on repairing existing infrastructure, replacing and modernizing existing infrastructure with new technologies, and installing completely new infrastructure for the future, such as ultra-high speed communications. Mr. Cisneros closed with the notion that while the gridlock in Washington can make it nearly impossible to act, individuals who are forward looking and want to build for the future can find a lifelong career path at the intersection of real estate and infrastructure.

Henry Cisneros (left) and Stijn Van Nieuwerburgh (right)