EuroProperty

Institutions tune in to Europe

US institutional investors have signalled their intention to target Europe and everything is fair game – be it development, non-core countries or buying platforms, they have deep pockets and plenty of ambition.

Much attention has been lavished on the private equity firms which have deployed billions of dollars of equity on huge deals in Europe - Blackstone, Lone Star and Starwood et al.

But Europe is also very much on the radar of US institutional investors – the pension funds and superannuation funds which, combined, control trillions of dollars of capital.

This cohort is looking to increase its exposure to Europe – a survey of 80 North American institutional investors by CBRE showed that 66% intended to increase their cross-border investment this year. Of that, 52% are choosing Western Europe as their preferred destination, with 19% picking Central and Eastern Europe.

What's more, many of these investors are accessing the European market in a manner not usually associated with traditional institutional investors. They are undertaking development, buying platforms and investing in territories that European institutional investors still consider too risky.

They are increasingly keen to set up offices in Europe to manage their investments on the ground, rather than simply allocating cash to fund managers and watching passively form the US. The Texas Teachers Retirement System, which manages $132bn of assets for education workers in the state, is understood to be setting up a London real estate office, joining fellow Texas investor USAA, which has established an office in Amsterdam.

Describing why TIAA CREF, which has assets under management of more than $550bn, around 10% of which is in real estate, bought the real estate arm of fund manager Henderson Global Investors, Tom Garbutt, global head of real estate, says: "One of the things we are bringing to the table in having a joint venture is the ability to have a deep localised understanding of the markets. We can put investors in touch with our people on the ground who know specific markets."

On the appeal of Europe to US institutional investors he says: "Most large investors here think globally, and they are looking at Europe as on the value-add part of the spectrum. Core property is pretty aggressively priced everywhere, including European gateway cities, but there are plenty of opportunities for value-add investment there because you can buy assets at or near replacement cost, and that is a great litmus test."

Macro appeal

Europe appeals to US investors from a macro and property point of view, according to Doug Weill, co-founder and managing partner at placement agent Hodes Weill.

"There are macro concerns that will affect not just real estate but all asset classes, like Greece and the volatility of the euro," says Weill. "But in general people are overcoming their fears about the geopolitical and macro risk because the real estate is fundamentally attractive. For those in the US they compare it to the US and are seeing it as an opportunity to find good value. The value of the dollar against the euro also makes it more attractive as an entry point.

"People are going out a bit further in terms of looking for value because they see core as a bit overpriced. They have liked the comfort of investing in the large allocator funds like Blackstone or Lone Star, or the more boutique firms that are closer to the ground.

"Some of the larger institutions are starting to put people on the ground in places like London, to buy direct assets and also to take an active role in fund governance. They see this as a two-to-four-year window – people are drawing parallels with the US market in 2011 and 2012, where liquidity has returned and markets have recovered."

One institution that has approached Europe in a different manner than one might expect is the Alaska Permanent Fund, which manages $50bn of assets, $5.9bn of which is in real estate. As with many institutions, it is working with global fund managers to make its first investments outside of its home market.

But it has moved much further up the risk curve than equivalent European or Asian institutions.

It teamed up with LaSalle Investment Management to spend £250m on UK regional retail, buying the Golden Square shopping centre in Warrington, north-west England, for £141m in June last year.

And on the Continent it has tasked CBRE Global Investors with buying European

US PUBLIC PENSION FUNDS WITH NOTABLE COMMITMENTS TO EUROPE-FOCUSED REAL ESTATE FUNDS

Majority of biggest pension funds invest with US-based fund managers

Public pension fund	Number of commitments	% with US headquartered real estate firms	% with Europe headquartered real estate firms
California State Teachers' Retirement System (CalSTRS)	23	57%	43%
California Public Employees' Retirement System (CalPERS)	18	78%	22%
New York State Teachers' Retirement System	13	100%	0%
Teacher Retirement System of Texas	12	67%	33%
New York State Common Retirement Fund	10	90%	10%
State Teachers' Retirement System of Ohio	10	50%	50%
North Carolina Department of State Treasurer	9	22%	78%
CPP Investment Board	8	75%	25%
New Jersey State Investment Council	8	62%	38%
Employees' Retirement System of Texas	7	0%	100%
Top 10 US Public Pension Funds	**118**	**60%**	**40%**
All US Public Pension Funds	**297**	**46%**	**54%**

Source: Preqin

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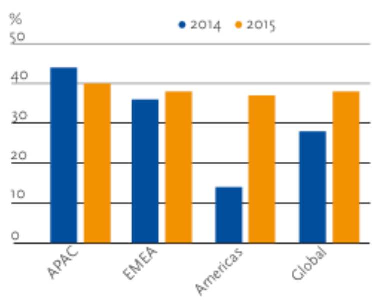
Tom Garbutt, TIAA CREF

Institutions' cross-regional investment intentions by region

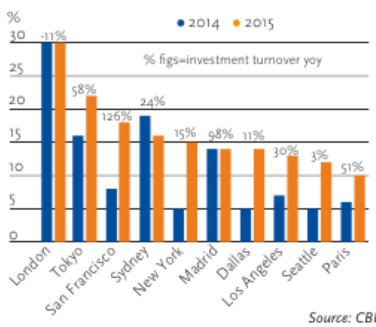
Sentiment towards the US grows in 2015



Source: CBRE

Institutions' preferred cities for investment

Funds head to cities other than London



Source: CBRE

retail assets, and became one of the first pension funds from anywhere in the world to buy in Iberia with the purchase of a 50% stake in two centres in Spain and Portugal valued at €280m in November last year.

"The high level of competition for core real estate in the US, along with the desire to increase diversification within the portfolio, led to the decision to seek properties in other promising parts of the world," says Rosemarie Duran, director of real estate investments for Alaska Permanent. "Prior to the recent purchases, the real estate portfolio's exposure to Europe was through the fund's global REIT portfolio. APFC has looked at properties in a number of locations, including London. Purchase decisions were based on the individual assessment of the properties, selecting those that were most advantageous to the fund's portfolio.

"Given the additional currency and tax exposure, European gateway cities do not currently provide risk-adjusted returns above US gateway cities, so since we're currently priced out of London, we'd rather invest in NYC at those levels. As long-term real estate investors, we will continue to add overseas investments when we are able to enter markets on favourable terms vis-a-vis the US."

Another investor doing things differently is USAA, the pension fund for US service men and women.

Last year it teamed up with Mountpark, the new developer set up by sheds guru John Cutts with a focus on logistics, backing the business to buy up and build out a European development pipeline.

It has established an office in Amsterdam, with three staff headed by David Buck, and will also undertake investment deals on its own. It is one of very few institutional investors currently willing to undertake development in Continental Europe.

Logistics move

The company's debut transaction in the region was the acquisition of a 33,955 sq m warehouse facility, a 4,080 sq m office building and a 19.70-acre parcel of land in Utrecht, The Netherlands, in October 2014. More recently in the UK it bought a one-acre plot near Manchester Airport for the creation of a 24,898 sq m unit and a six-acre plot for the creation of a 12,356 sq m logistics unit within Wakefield Europort in Yorkshire.

The joint venture with Mountpark also has deals lined up for sites in Poland, Czech Republic and Slovakia. Its portfolio could total 696,773 sq m, with a potential end value of $1bn, by the end of the year.

"We're perfectly comfortable doing this ourselves," says Len O'Donnell, USAA Real Estate's chief executive. "However, there's institutional capital that has been asking to participate with us. At some point this year, we may put together a strategy to entertain that."

"We've got some early intelligence on multi-family in Europe, and we've evaluated some retail. We'll consider any property type where we have a core competency and deep history in the US," says Buck. "But we only have a small percentage of our portfolio allocated to non-US investments at this time, so it's probably a 2016 discussion for us."

In terms of how and why TIAA CREF decided to buy a platform for Europe rather than expand organically, Garbutt says: "The most important things were scale and finding a partner with a like-minded philosophy. We started looking at how to collaborate in this market and what each partner could bring to the table, and found that the platforms meshed well and had a common philosophy.

"Geographically, TH Real Estate had a strong presence in Asia and Europe and a smaller presence in the US, where we were very strong. We currently have over $56bn in assets under management and $82bn worldwide with TH Real Estate.

"We didn't initially know that we would do a joint venture, but through the conversations with Henderson the answer started to crystallise and that turned out to be the best fit – there was no predetermined idea about how we would attain the growth that we wanted to achieve. The JV has since led to the full acquisition of TH Real Estate, so we have been able to grow both organically and inorganically. The acquisition allows us to deploy capital for internal clients but also presents opportunities to grow the amount of external capital we bring to different markets as well."

Timing the market right, doing innovative deals and using innovative structures to drive value for their investors – some would argue that there is a lot that European institutions could learn from those currently making the leap from the US.