

Global Family Office Community Real Estate Roundtable

Thoughts on Commercial Real Estate Investing

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Introduction

FORE Partnership is a transformational real estate investment firm that addresses the specific needs of private investors for greater alignment with their property investments. FORE achieves this firstly through the direct co-investing platform it has developed which sources, manages and realises value using hands-on, creative real estate strategies in the UK and Western Europe. And via a principled investment approach, FORE drives returns with a holistic view on sustainability, design, occupational trends, community and the built environment. The firm calls this approach “responsible real estate”. Complementing this philosophy, FORE has a fundamental value investment mindset and employs a highly thoughtful investment process. The team has a successful €5 billion track record spanning three decades. Since setting up FORE in 2012 out of Capricorn Investment Group, a single family office, FORE has grown to represent more than a dozen families and has acquired more than €300 million of commercial property.

The big question...it's not what you think

I've been working at cross-section of real estate and family offices for best part of two decades, and I was going to talk to you all about shifts in yields and prices, deals done in the market, and rental growth, all to try and address the big question on everyone's mind: Where are the best opportunities in commercial real estate today?

But I'm not going to do that. I want to talk about something much more important, and that is the following: How can you maximise your chance of success in the real estate market as a private investor? It's perhaps the single thing we think about the most. Especially as we exit the benign investment market of the last seven years post-financial crisis and enter more turbulent times.

As we've looked at families and what makes for a successful real estate strategy, we've noticed a few consistent points. Let me frame it as a series of three questions.

Property's purpose

What do you hope to achieve by investing in real estate? Why do you invest in real estate? What purpose does it serve? That's one question not three!

The most successful families we know – and indeed the best investors pretty universally – understand why they do what do. And they start with a clear objective and purpose, then execute. In that order.

What purpose does RE serve for you? Again I think there's a degree of consistency among top family office investors here. For them, real estate (i) is a long-term store of value, (ii) provides inflation protected income, and (iii) is a mechanism to transfer wealth from generation to generation (often tax efficiently).

That's it. That's all you want it to do.

In its purist form, real estate's function is not to generate huge alpha; it's not there to deliver 20% or 30% IRRs. Let me remember some basic facts about what real estate is. First it's stable. We've done a lot of analysis looking across markets and cycles, and over the very long term – 80+ years – commercial property has had only a handful of down years in terms of total returns, five or six depending on what geography and sector you look at. Second and following on from this, it is uncorrelated to equities (corr. of -0.2 to +0.2 in our analysis). Over the long term, it provides 6% to 8% total nominal returns (3% to 4% real) with low dispersion around this level. It's illiquid. It's leveraged.

Successful families tend to see real estate's purpose as the ballast in portfolio. Or as I think about it, like a Fiat 500. Great at getting you from A to B in a stylish manner; just don't ask it to do 200 kph down the motorway.

Execution alignment

The second question I would pose is: Does your current approach – end to end, how you are investing in real estate, who with, and finally what – line up with question 1? Is your activity consistent with the outcomes you hope to achieve?

Sometimes we talk to families that say they would like real estate to serve as a ballast or for income. And then when we unpack their strategy, we find the bulk of their “real estate” exposure consists of hotels, personal residences, resort development. Or REITs. Or expensive, over-structured funds.

That's not so say that a successful investment strategy can't be formed around racier strategies and operationally leveraged asset types like hotels, student housing or care homes. It's just that we should not necessarily call that real estate in the sense above. It's something else; more correlated to equities, to operational skill or the economy at large. Entirely legitimate investments to be sure, but they serve a different purpose in the portfolio and should sit in a different bucket.

Nor am I advocating boring core, dry income, trophy assets. Indeed, we are focused on value-add opportunities, classic bricks and mortar driven strategies that we can use to enhance the value of what we buy. Real estate is unique in this way; among asset classes, there are very few that you can do something physically with in order to change it into something else, or simply to unlock value. Try that with your shares of Vodaphone, or your Picasso painting. Our approach at FORE is to make that Fiat 500 work pretty hard, but not ask it to do something it is not designed for.

And don't forget about the how and the who. Which means of execution is consistent with your vision? Should you invest via funds, directs, on your own? What kinds of partners understand your objectives? We find more and more that families and institutions are tacking in opposite direction in this regard.

In short, start with a strategy and execute it. If the barrage of investment opportunities hitting your desk is anything like mine, it's tempting to execute first and backfill a series of deals with a strategy. But don't.

Be true to your purpose

Third and final question: Is what you are doing in real estate consistent with your values as a family?

Part of this is about the partners you pick, and how you invest. But here I'm really talking more about sustainability. We firmly believe that there is no trade off of “value for values”; you don't need to sacrifice financial return on capital in order to have a social return on capital. You can and should use sustainability as a tool to unlock value just like any other asset management strategy. We call our version of this “Responsible Real Estate” because it embodies a wide range of strategies beyond the traditional narrow focus on energy, water and waste. Community, placemaking, the built environment, health, wellness and future office design all are important and often unconnected strands in the sustainability conversation. Occupiers as well as investors are increasingly drawn to this approach, practically as it drives down operating costs, improves productivity, and strategically firms are using their offices to attract and retain talent, as an extension of their own brand and an expression of *their* values.

Conclusion

Especially as we exit the benign investment market of the last seven years and enter more turbulent times, important to pause and reflect on what we are doing with real estate. We may well need it to perform that purpose it has as ballast in the portfolio.

If you have difficulty answering any of the three questions I posed above – and in the case of question two or three, the answer is not an emphatic yes – you need to stop what you are doing and make some dramatic changes.