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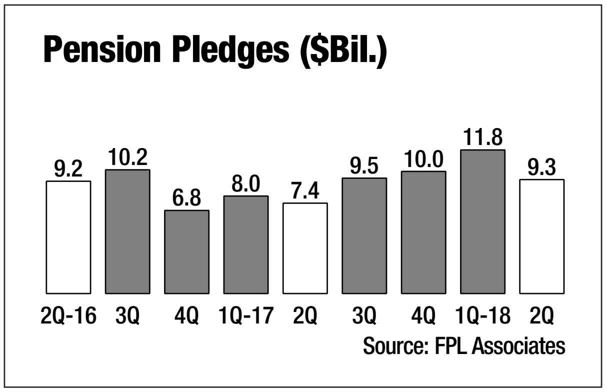
THE WEEKLY UPDATE ON THE INSTITUTIONAL MARKETPLACE

Pledges by Pensions Surge by 35%

Commercial real estate commitments by public pension funds jumped by a surprising 35% in the first half, putting pledges on pace for the second-highest annual level since the market crash.

Pensions continued to plow equity into the sector even though investment managers are sitting on a record hoard of uninvested capital because of the difficulty of finding suitable investments. That factor had contributed to declines in pledges for the past two years, and observers did not predict a strong rebound this year.



"I'm pleasantly surprised where we're tracking thus far through the year," said **Erin Green,** a senior director at **FPL Associates,** which compiles the data.

While pensions poured $11.8 billion into real estate funds and separate accounts in the first quarter, up 48% year-over-year, one system — **California State Teachers** — accounted for 37% of the total. But commitments in the second quarter came from a broader mix of pensions, totaling $9.3 billion, up 21% from a year earlier.

"What's really promising and interesting about the second quarter is that there is no single investor who is driving this result," said Green. "That says to me that across the board, investors are still active in real estate and are still looking to make new allocations."

The first-half total of $21.1 billion, up from $15.7 billion a year earlier, puts commitments on pace to exceed $42 billion this year. The post-crash record was $47.2 billion, in 2015.

Market watchers have been wary of the rising amount of uninvested equity. **Preqin** reported last week that dry powder at closed-end funds stood at $290 billion at midyear, up from $249 billion at yearend.

Green said that managers are expanding their scope to line up investments. Examples include looking at more suburban or secondary markets, and increasing allocations to different asset classes. Managers "are starting to find ways to expand the parameters of their investment strategy," she said. "They are finding creative ways to place their capital."

At the same time, most sponsors are continuing to use reasonable debt levels, so she isn't overly worried about a 2008-style correction. "Last cycle, where people got into trouble was the use of leverage," Green said. "But what we're hearing is that, by and large, people are being prudent now."

Core-plus strategies attracted a growing share of pledged dollars. That category accounted for 16% of pledges by dollar amount in the first half, up from 11% for full-year 2017. Value-added and opportunistic strategies attracted 61% of committed equity, down from 64%. Core plays dipped to 23% from 25%.

Closed-end funds remained investors top choice, garnering 51% of committed dollars in the first half, up from 46% for full-year 2017. The other pledges went to open-end funds (17%) and separate accounts (32%).

The number of closed-end funds that held final closes slowed in the second quarter, but that was largely because the prior six months posted the highest totals since 2015, according to a Preqin report. "It was by no means a bad quarter as much as it was a return to more-typical levels," wrote **Oliver Senchal,** Preqin's head of real estate products. "We should see fund raising pick up" in the second half.

FPL found that the percentage of commitments to debt-focused vehicles fell in the first half. Some 15% of pledged dollars went to such vehicles, down from 19% in full-year 2017 and 20% in 2016.

The 228 pension systems tracked by Chicago-based FPL have $341 billion of real estate assets and $4.2 trillion of total assets under management. They are believed to account for the vast majority of assets held by public pension systems. FPL will release a report summarizing its findings this week. ❖