2022 Fundraising Year in Review

Pension fund commitments to managed real estate vehicles

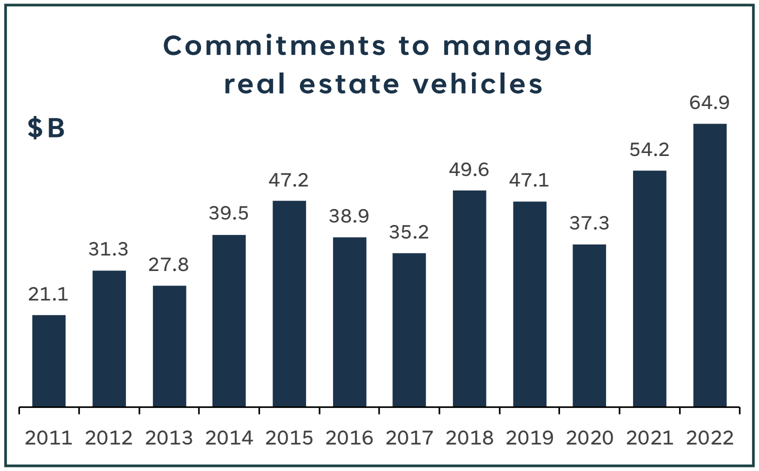
Ferguson Partners

FERGUSONPARTNERS.COM

Commitments to private real estate reach all time highs in 2022

Commitments to private real estate managers from U.S. public pensions started strong before slowing in Q4

Capital commitments from U.S. public pension funds to privately managed real estate vehicles totaled $64.9 billion in 2022, which is the largest annual fundraising volume since the inception of Ferguson Partners' proprietary commitment database in 2011. The total commitment volume in 2022 increased 20% year over year, coming in well above the previous high watermark of $54.2 billion in 2021. Driving this uptick was a 16% increase in the number of unique commitments and a 3% increase in average commitment size over 2021.



2022 was a true tale of two cities, as the first half of the year saw unprecedented levels of capital raising. Coming off an extremely strong 2021, investors eagerly flocked to real estate to provide a hedge against inflation and diversify their portfolios with strong, stable returns. As a result, Q1 through Q3 led to some of the largest quarterly fundraising volumes seen in the history of FP's commitment database.

However, geopolitical concerns, the inflationary environment, and rising cost of debt gave investors pause in a "wait and see" period as 2022 unfolded. In Q4 2022, fundraising was down 11% as compared to Q4 2021, underscoring investor caution as they waited for the typical economic indicators: actions from the Federal Reserve to fight inflation, labor reports, and trends in the stock market and bond yields.

The news was not what investors were hoping for. In Preqin's November 2022 investor survey, 74% of investors believed real estate to be overvalued.[1] Moreover, macroeconomic headwinds and corrections in the public equity markets ramped up denominator effect pressures, further curbing the appetite for new commitments to real estate. As the Fed continued raising rates in an effort to tamp down inflation, sponsors were forced to reckon with their cost of capital for funding new deals and development projects. All of these factors led to a slowdown in the real estate market with stricter underwriting among sponsors and greater investor due diligence measures as confidence in the overall state of the economy waned.

It is suspected that this caution will continue heading into 2023 as the broader investment community waits for further economic signals on inflation and unemployment, and the real estate market continues to see a tepid transaction market with wider bid-ask spreads and a greater emphasis on operational performance at the asset level.

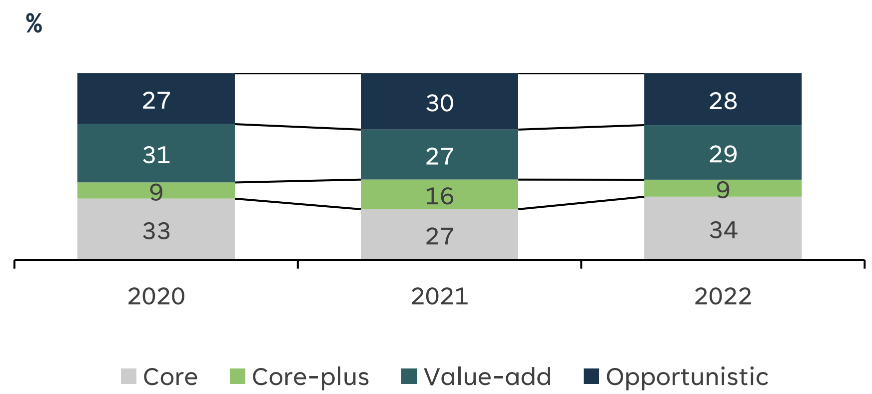
1. 2022 Preqin Global Real Estate Report

Investment Strategy and Vehicle Structure

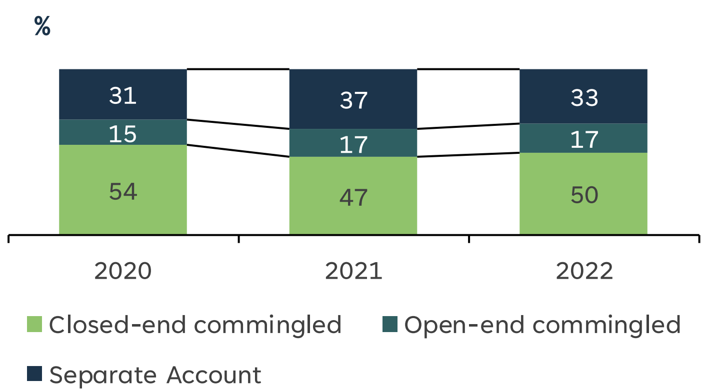
High-yield strategies continued to remain attractive to investors throughout the year, with commitments to opportunistic and value-add vehicles representing roughly 57% of total 2022 volume, on par with 2021 levels. Even with the multitude of macroeconomic uncertainties, investors are still gravitating towards high-yield strategies. According to a recent Preqin survey, investors believe value-add and opportunistic funds present the best opportunities in the next 12 months, closely followed by distressed funds.[1]

In 2022, Blackstone continued high-yield fundraising dominance and was joined by others including EQT Exeter, TPG Real Estate, CBRE IM, Rockpoint, and Brookfield, who all secured material commitments for their high-yield strategies.

Commitments by investment strategy



Commitments by vehicle type



On the other end of the risk/reward spectrum, commitments to core-oriented vehicles increased from 27% to 34% of total commitment volume in 2022, while core-plus commitments decreased year over year. IDR Investment Management's fund of funds (IDR Core Property Index Fund) topped the list of core-focused funds, followed closely by products from Clarion Partners, Principal Real Estate Investors, and PGIM. These private ODCE funds offer institutional investors the chance to diversify their real estate portfolio and act as a safe bet as inflation continues to dominate discussions. On the JV/separate accounts side, First Washington Realty, GI Partners, BentallGreenOak, and GID all received considerable commitments to their core products.

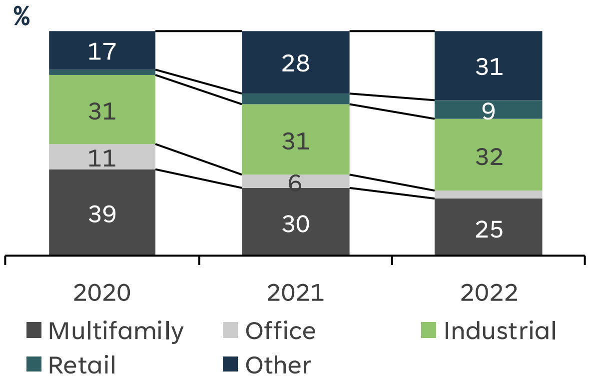
Lastly, for core-plus commingled funds, Cortland Partners, Clarion Partners, DWS, and Fairfield Residential received sizeable commitments in 2022, despite the decreasing core-plus share of total commitments.

Examining 2022 commitments by vehicle type, closed-end commingled vehicles remained the top choice for investors and its share of total volume of commitments rose from 47% in 2021 to 50% in 2022. On the flip side, the percentage of volume dedicated to separate accounts decreased year over year with 33% of the total volume flowing into this vehicle type. Open-end commingled vehicles remained stable year over year, comprising 17% of total volume.

1. 2022 Preqin Global Real Estate Report

Property Type, Vehicle Focus, and Geography

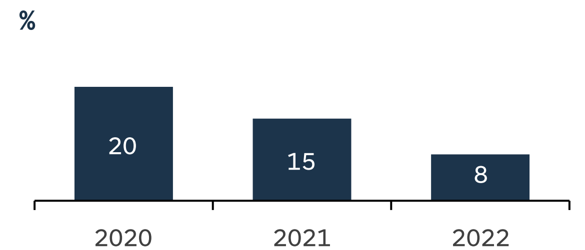
Commitments by property type (among property-specific vehicles)



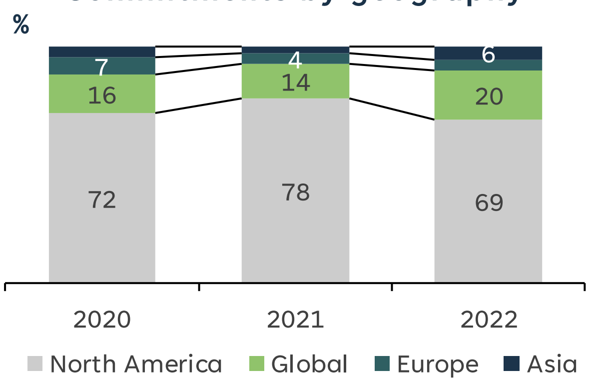
Vehicles dedicated to a specific property type continued to garner interest, with 52% of overall volume committed to property-specific vehicles in 2022. This is a material gain from 2021 and 2020 when 49% and 42% of commitment dollars were dedicated to property-specific vehicles, respectively. Once again, industrial was the most popular property type, representing 32% of total property-specific commitment volume. Multifamily decreased slightly from 2021 with 25% of the volume but remained a strong asset class. There was a renewed interest, albeit a small one, in the retail asset class with 9% of the capital commitments flowing to property-specific vehicles dedicated to this rebounding sector. Appetite for office investments continued to follow a downward trajectory from 2021 with only 3% of the commitments. On the other hand, the "Other/Niche" property types continued to gain attention with vehicles focused on life sciences, single family rentals, healthcare, data centers, and cold storage, among others, receiving 31% of the commitments from investors.

In 2022, the portion of total commitments to debt-focused vehicles retraced back to 2019 levels, with 8% of the total volume flowing into such vehicles. Compared to the peak of 20% of the volume in 2020, debt-focused vehicles sunk below the five-year average in 2022. The allocations to debt-focused vehicles, however, are predicted to increase in the coming year. As traditional lenders tighten their underwriting assumptions and the availability of debt declines, private real estate investment funds will be eager to step in for traditional lenders. According to Preqin's database, 13% of funds currently in market are dedicated towards debt strategies already, indicating enhanced interest in the strategy.

Percentage of commitments to debt-focused vehicles

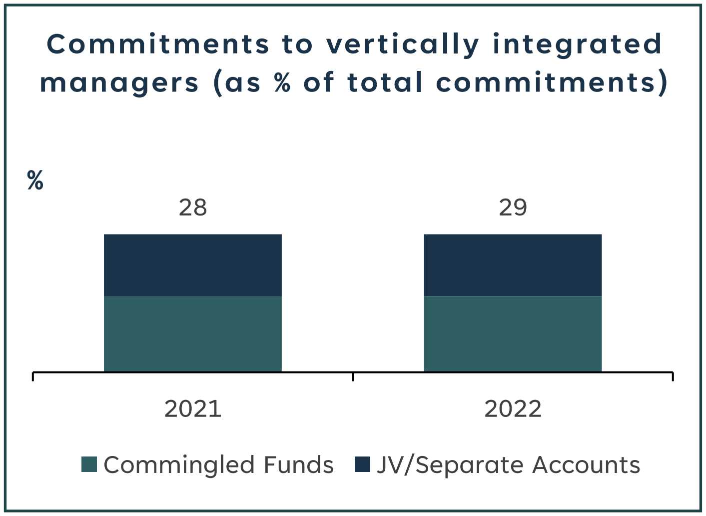


Commitments by geography



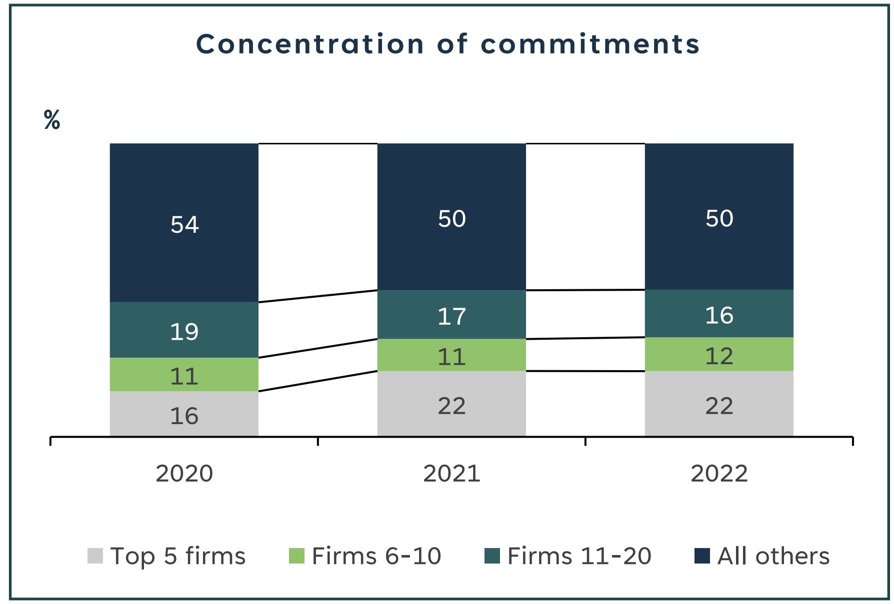
Continuing past trends, commitments from U.S. public pensions flowed predominantly into North America-focused vehicles (69%), even though the share fell year over year. Global strategies, on the other hand, rose from 14% of the total volume in 2021 to 20% in 2022 as institutional investors looked to diversify their portfolios. Additionally, despite major geopolitical concerns, commitments to European-focused strategies rose modestly from 4% in 2021 to 5% in 2022. Asia-focused strategies attracted more interest from U.S. public pensions as they harnessed 6% of total volume. The growing trend of geographic diversification is not slated to end soon, with investment managers looking to take advantage of China's reopening, Japan's relatively low cost of debt, and other emerging real estate markets.

Vertical Integration and Manager Concentration



Vertically integrated managers attracted 29% of committed capital in 2022, which is roughly consistent with 2021. Commitments to vertically integrated managers were more skewed toward commingled funds than JV/separate accounts. However, 43% of commitments to JV/separate accounts went to vertically integrated managers. Further, when segmenting by strategy, value-add mandates were most likely to be committed to vertically integrated managers, with 39% of total value-add commitments flowing to vertically integrated managers in 2022.

As in 2021, the largest players dominated the fundraising cycle with the top 20 managers (by aggregate fundraising volume) receiving half of overall commitments. Relative weighting of commitments at the top end of the market was remarkably consistent year over year. Blackstone, GI Partners, First Washington Realty, BentallGreenOak, and EQT Exeter topped our list of top managers in 2022 and are building on this momentum heading into 2023. Blackstone has a new fund in market dedicated to real estate debt targeting $8B in commitments, suggesting a renewed interest in debt strategies. Additionally, BentallGreenOak has new APAC-focused and Europe-focused funds in market allowing investors to diversify across geographies.



2022 Top 10 Managers	
Blackstone*	GID*
GI Partners*	IDR Investment Management
First Washington Realty	TPG Real Estate
BentallGreenOak	Clarion Partners
EQT Exeter	CBRE IM

*Top 10 manager in 2021

Looking Forward

While 2022 started strong thanks to a combination of low interest rates, an abundance of dry powder, and renewed interest in real estate in a post-COVID world, the narrative quickly shifted. The second half of 2022 saw worsening macroeconomic conditions, heightened geopolitical concerns, and inflation worries. As a result, transactions slowed, the price of debt increased substantially, and many began preparing for what appeared to be a looming recession. Pensions, in turn, slowed their real estate contributions throughout the year but not before having committed nearly $65 billion to real estate.

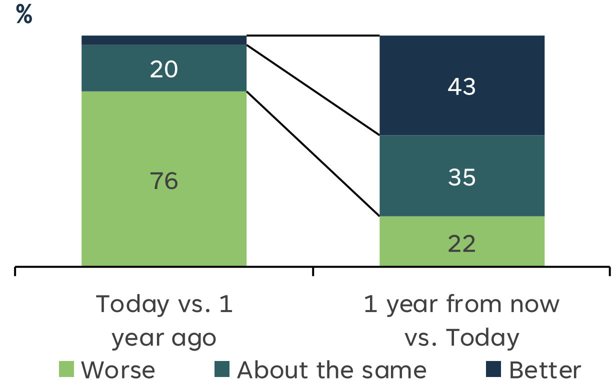
While current conditions remain challenged, market participants are optimistic moving forward. 76% of respondents in the Q4 2022 Real Estate Roundtable sentiment survey indicated that equity capital availability today was worse than Q4 2021. However, survey participants were more optimistic about the availability of capital in the future, with 43% of respondents believing that capital availability will be better in Q4 2023.[1]

There is good reason to remain optimistic. According to the Hodes Weill & Associates and Cornell University's annual Real Estate Allocations Monitor Report, institutional investors are expecting to raise their weighted average target allocation to real estate by 30 bps in 2023.[2] Further, in contrast to the Global Financial Crisis, most experts acknowledge that in today's market firms are not overleveraged and still have dry powder to deploy. As inflation is tampered and other macroeconomic headwinds come to a plateau, there is a belief that activity in the sector will resume.

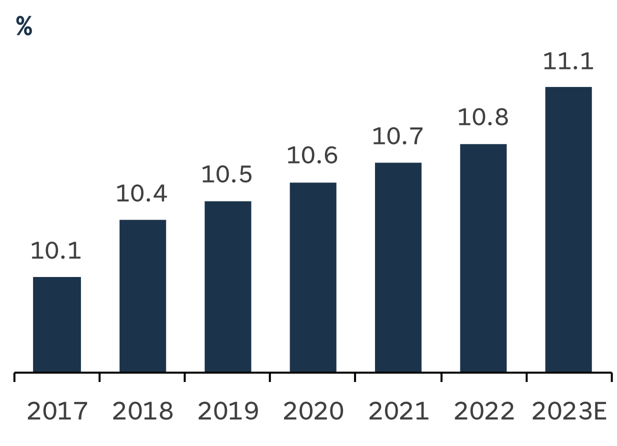
It will not be easy to achieve the capital raising highs of 2021 and 2022, however. Public pensions are down year over year on the real estate conviction index, from 6.6 in 2021 to 6.1 in 2022 with concerns about the denominator effect still weighing.[2] Not to mention, the percentage of institutional investors who overallocated to real estate in 2022 was 32%, over triple the amount from 2021.[2] While pensions will continue to allocate to real estate, they will be doing so with greater due diligence. Many investment managers are still waiting on the sidelines to deploy capital as valuations catch up with the ever-changing market and the gap between the expectations of buyers and sellers decreases.

Overall, it would be surprising if 2023 capital raising surpassed the high mark of 2022, but there is still time for macroeconomic headwinds to shift with an economic "soft landing".

Availability of Equity Capital[1]



Average investor target allocations to real estate[2]



Graph accounts for all institutional investors, not just pension funds

1. Q4 2022 Real Estate Roundtable Survey conducted by Ferguson Partners
2. Weill, D. (2022). 2022 Institutional Real Estate Allocations Monitor. Ithaca, NY: Cornell University's Baker Program in Real Estate and Hodes Weill & Associates, LP, November 2022.

About the Database

Ferguson Partners' database, which has tracked capital flows since 2011, includes commitments to 515 managers from 306 U.S. public pensions representing over $5 trillion in assets under management. Data comes from a variety of sources including pension websites and industry news sources.

Contact

For more information on this report or Ferguson Partners' practice more broadly, please contact:

SCOTT MCINTOSH
Director
smcintosh@fergusonpartners.com
(312) 893-2366

Ferguson Partners

Ferguson Partners is the leading talent management and strategic advisory firm for the global real assets industries.

fergusonpartners.com | **Americas • Europe • Asia Pacific**