Green Street
Real Estate Alert
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Pension Pledges ‘Probably at the Bottom’

Just a year after hitting their peak, pledges to commercial real estate vehicles from U.S. pensions in 2023 dropped 50% year over year to their lowest level in a decade.

Commitments to funds and separate accounts last year totaled just $32.68 billion, down from the record $65.09 billion notched in 2022. It’s the lowest tally since 2013, when pensions gave $27.77 billion to real estate vehicles, and the fourth-lowest year since Ferguson Partners began tracking the sector in 2011. The Chicago-based firm will release its findings in a report next week.

The 2023 haul is nearly 25% below the 10-year average of $44.19 billion of pledges. Momentum slowed sharply in the second half in particular: Just $14.23 billion of pledges were made in the third and fourth quarters of last year, 25% less than the record $18.61 billion of commitments in the third quarter of 2022 alone.

“It’s really a stark, stark recalibration … from the upward trend we’ve seen over the last five or six years,” said Scott McIntosh, a director with Ferguson. “In terms of fundraising, we’re probably at the bottom.”

McIntosh said illiquid markets, falling property values and overall uncertainty kept pensions on the sidelines in the second half of last year. And while there is buzz around interest-rate cuts and green shoots for increased sales volume, pensions likely will be slow to return.

“We’ll probably see a little bit more momentum as we move into 2024,” McIntosh added. “I don’t think we see an immediate rebound or correction to 2021 or 2022 fundraising figures. But I think managers and investors are cautiously optimistic that markets will open up, and we’ll see more activity than ’23.”

As investors look to take advantage of distressed situations, pensions favored higher-yielding strategies. Roughly 76% of commitments, by dollar volume, went to value-added or opportunistic plays, up from 57% in both 2021 and 2022.

Just 20% of dollars committed went to core strategies, the lowest annual tally since 2016 saw 18%. Core-plus commitments fell to 4%, down from 16% just two years ago.

Most of the pledged dollars went to closed-end funds, which took home 59% of commitments last year, up from 49% the year before and 47% in 2021. It’s the highest share for that category ever. Separate accounts garnered 32% of pledged dollars, roughly even with 2022, while open-end funds, which typically target lower returns, saw their share plummet to 8% from 18%.

Pensions also favored the biggest players more last year, with 37% of committed dollars going to the top 10 managers. That’s up from 33% in each of the last two years.

“When there’s so much uncertainty, those blue-chip organizations or those organizations with which investors have long-term relationships are going to see more activity,” McIntosh said. “It will be interesting to see if that ‘haves and have-nots’ story materializes more in the data in 2024.”

Some 44% of overall pledges went to vehicles dedicated to a specific property type, down from 53% in 2022 and 49% in 2021. Industrial-property funds took home the largest share of committed dollars (35%, up from

32%), followed by vehicles targeting niche sectors (33%, up from 31%) and multifamily funds (27%, up from 25%). Vehicles focused on retail properties took home just 5% of pledged dollars, down from 8% in 2022, while office-centric vehicles corralled just 1%, its lowest annual figure, following last year's 3% and 2016's 2%.

While investors also favor niche-focused funds, the relatively small number of established operators in those sectors presents a challenge. Ferguson defines "niche" as property types including life-science, single-family rental and data-center properties.

"Data centers are a great example," McIntosh said. "There's acknowledgment that the asset class is going to be critical and foundational to elements of the economy, similar to how industrial has been over the course of the past 10 years. But you have to be able to execute."

Some 137 managers secured commitments in 2023, down from 173 in 2022 and 165 in 2021. The number of individual commitments fell 49%, to 295 from 578 the year before and 497 in 2021. The average commitment size in 2023 was $287 million for separate accounts, down from $259 million in 2022 and the record high of $343 million in 2021; $85 million for closed-end funds, up from $84 million; and $131 million for open-end vehicles, down from $139 million.

Ferguson Partners' database tracks 308 U.S. public pensions, representing more than $5.5 trillion under management and the vast majority of pension assets under management.