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Pension Pledges Nose-Dive in 3rd Quarter

U.S. public pension pledges to commercial real estate vehicles are down 48% through the first nine months of the year, dropping to a six-year low.

Commitments totaled just $26.63 billion, down from $51.18 billion in the same period a year ago and $38.74 billion in 2021, according to **Ferguson Partners,** which is expected to release a report of its findings next week. It's the lowest nine-month total since 2017, when only $25.19 billion was pledged.

From July to October, pensions committed just $8.18 billion to funds and separate accounts. While that was up slightly from the second-quarter tally, it was down significantly from the $18.61 billion **pledged** in the third quarter of 2022. That three-month haul for investment managers was the largest since Chicago-based Ferguson began tracking the market in 2011.

The third-quarter drop marked the fourth quarter of year-over-year decreases — and the rate of descent has increased each quarter.

"If nothing else, it's consistent," said **Scott McIntosh,** a Ferguson director. "I would expect Q4 to be similarly slow. The same capital-markets challenges are persisting, in terms of elevated interest rates and a continued bid-ask spread that's resulting in a lack of liquidity in the market."

Placement agents have **continued** to see reticence from institutional investors who invest in real estate. There is optimism — and an expectation — that a wave of distress will provide high-yielding opportunities over the coming years, but until that materializes, pensions mostly are taking a wait-and-see approach.

"It's going to take time for that to unwind and liquidity to enter the market," McIntosh said. "It's not terribly surprising to see investors take a slower approach to allocations."

Those pensions that are committing to real estate vehicles are choosing the ones chasing the highest yields. Through the first nine months, 74% of commitments, by dollar amount, have gone to value-added and opportunistic strategies, up from 57% for full-year 2022.

Value-added vehicles have seen the most growth, taking home 47% of all committed dollars through the first three quarters, up from 29% for all last year. That comes at the expense of core and core-plus strategies, which saw their combined total through the first three quarters drop to 25% of pledges, down from 43% in full-year 2022.

McIntosh said that in today's environment, where Treasury bonds and other safer investments are providing yields unseen in 15 years, it's difficult to make the case for core real estate. "It's just tough to justify given the risk-adjusted returns for core strategies versus alternative-investment strategies," he added.

The migration to higher-yielding vehicles accounts for the drop in pledges to open-end real estate funds, which typically chase lower returns. Commitments, by dollar amount, to such vehicles fell to 7% through the first nine months of the year, down from 17% for full-year 2022.

The number of commitments also was halved through the third quarter, with pensions making 226 pledges, versus 471 for all of last year. Market pros said that's a sign of how difficult it is for all but the most established investment managers to raise money at scale today. To that end, the top 20 firms by dollars raised through the third quarter corralled 57% of commitments, up from 50% last year.

Investors pledged fewer dollars to vehicles dedicated to a single property type, with 44% of commitments going to such funds and separate accounts, down from 53% in 2022 and 49% in 2021. That could be a result of the largest investment managers — who typically run vehicles that invest across property types — taking home a larger slice of the pie.

Among dedicated vehicles, those buying industrial properties continue to take home the lion's share, with 38% of pledged dollars, up from 32% in 2022. Multifamily-focused vehicles were the only other category of single-focus vehicles to see an increase, collecting 28% of committed dollars, up from 25% last year. Niche funds ticked down to 30% of pledged dollars, from 31% in 2022. Ferguson defines niche vehicles as those focused on life-science properties, single-family rental properties, healthcare properties, data centers, cold-storage properties, debt and others.

The 307 pension systems tracked by Ferguson have approximately $5 trillion under management. ❖