

# NAREiM

SPRING 2022

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*dialogues*



*Making* **DEI**  
*data collection*  
**MATTER**

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# NAREIM

dialogues

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**Zoe Hughes, CEO**

**N**o matter what we are doing in our businesses or within our areas of expertise, if we don't have the data, we rarely can move forward. After all, as the business maxim goes: "If you can't measure it, you can't improve it."

Diversity, equity and inclusion needs good data. Collection is the place where it begins, and the foundation of all the meaningful work — and impact — ahead.

As our roundtable with Berkshire, Blue Vista, National, PGIM and USAA highlights only too clearly, collecting data related to gender, ethnicity and other metrics of diversity can be challenging in and of itself. After all, this is highly personal information and, even in the US, a majority of data is self-reported.

DEI data collection therefore comes down to trust and the organization's inclusive culture. The first step, the roundtable participants argue, is to get people comfortable with providing information and making it easy and accessible to do so.

Then it's about communication.

"[We communicate] to our team, 'We gave you this opportunity to provide us this voluntary data and the response has been great, thank you. This is what we've been able to do with it,'" said Jenn Llicardi, vice president, head of human resources at Berkshire Residential Investments. "Showing our teams the results of the data we collected and how it changes over time is impactful."

The most critical step, though, has to be linking DEI back to the business and aligning the DEI strategy or programs with the corporate or investment strategy. Lisa Kizina, chief human resources and administrative officer at National Real Estate Advisors summed it up well saying: "In real estate investment management, we are numbers people — HR can provide metrics, but if the people in the organization don't connect the corporate demographics to the business, or if we don't have adequate representation from people of color on the project, it's not going to make an impact on the bigger picture in the long term."

That's why DEI has to be an integral part of an organization's DNA. And that begins with data. As all our roundtable participants urged:

- Focus on the significant gaps, but don't get too caught up collecting every piece of data
- Get qualitative feedback from employees (existing and departing) on what matters to them
- Tie it back to the business and operations:
  - Highlight LP and RFP questions on DEI
  - How many people of color or women do you have on a project?
  - Excite employees on DEI by connecting it back to the deal or project and taking it outside of the corporate setting and numbers

As Erick Harris, general counsel and CCO at Blue Vista Capital Management said, the goal is fairly universal to good talent management practices and is not just DEI-specific: "[It's about] ensuring that everybody within the company has a voice in some way, shape and form. Anything we can do as a company to reinforce that inclusionary environment for our employees is a good thing."



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A light blue background with various icons: two stylized human figures (one blue, one yellow) at the top left, a blue wavy line, a yellow gear, a blue plus sign, a large purple and yellow pie chart, a blue gear, a magnifying glass with a yellow handle, and a small yellow circle at the bottom left.

# Data *for a* greater GOOD

*When it comes to DEI, we need data. We cannot improve what we cannot track. But how do you show you are taking steps toward — and seeing results from — having an organization that is diverse, equal and inclusive? It starts with data and strategy, but which comes first, and what? How do we prevent data overload among employees and how do corporations make sure what they collect is impactful to the objectives of company DEI programs and initiatives?*

*NAREIM speaks with **Berkshire Residential Investments, Blue Vista Capital Management, National Real Estate Advisors, PGIM Real Estate and USAA Real Estate** about DEI data collection and where data has the most impact on outcomes, not least employee engagement and inclusivity.*

By Zoe Hughes



## PARTICIPANTS

**Deena Goodman***Director and HR Business Partner of US Equity, PGIM Real Estate*

Deena is the HR Business Partner for the US Equity business at PGIM Real Estate where she partners with the investment, marketing and business development teams to support the achievement of organizational and business-related goals. Prior to joining PGIM Real Estate, Deena practiced independently as an executive coach and psychotherapist in the New York Metro area, where she coached executives across industries on establishing strong leadership presence and managing mental health in the workplace.

**Shannon Grenet***Director of Talent Strategy, USAA Real Estate*

Shannon has dedicated her 20-year career to the field of Human Resources, specializing in recruitment, talent development, talent management, employee relations and HR systems and project implementation. Shannon has been with USAA Real Estate for over 11 years and currently holds the position of Director, Talent Strategy. As a strategic human resources and talent strategy leader, she provides expertise in developing and deploying scalable human resource strategies, programs, solutions, policies and services.

**Erick Harris***General Counsel and Chief Compliance Officer, Blue Vista Capital Management*

Erick has responsibility for the company's legal and regulatory affairs at the fund and investment levels. Prior to joining Blue Vista, Erick was CFO for the Americas Division in the Abu Dhabi Investment Authority's Real Estate Department. In that role, he was responsible for the negotiation and execution of the Division's acquisitions, dispositions, financings and asset management matters; Erick was also responsible for management of the Division's debt portfolio, as well as development and implementation of Divisional best practice protocols.

**Lisa Kizina***Chief Human Resources and Administrative Officer, National Real Estate Advisors*

Lisa is a member of National's management committee and works in coordination with National's senior management team, serving as a strategic partner to lead all people, operations and technology functions supporting effective and innovative business operations for all of National's entities, departments and locations. Lisa has worked with National's senior management team since 2011 and she has over 20 years of business experience in the real estate and construction industry. She holds a Senior Professional in Human Resources certification.

**Jenn Licciardi***Vice President, Head of Human Resources, Berkshire Residential Investments*

Jenn has been with Berkshire for 15 years as Vice President, Head of Human Resources responsible for evolving human resources practices across all HR functions and talent management to position the company to be an employer of choice. Prior to joining Berkshire in 2006, Jenn was an Assistant Vice President in Human Resources for JPMorgan Chase overseeing and managing all HR management and delivery to assigned business. She holds a certification in Instructional Design/Development as a training professional and is a Certified Professional Coach.

**H**ow do you think about data as part of your DEI strategy? Do you start collecting it or does the strategy come first?

**Jenn Licciardi, Berkshire Residential**

**Investments:** We've been asking ourselves that question for a handful of years. We started with data, but in hindsight I would say that strategy needs to be first. Having a strategy gives structure and focus.

**Lisa Kizina, National Real Estate Advisors:** For National Real Estate Advisors, there was some simultaneous data management and research, and surveying and benchmarking. As a small company, we needed to be organic and focused on incrementally embedding the D&I strategy into our company DNA. When we look at our processes, we ask ourselves if we can make them more inclusive or extend opportunities outside of the current standard. With data collection, our HR team participated in surveys, while being intentional to have many conversations with the management team and staff to help them see the value in D&I.

**Deena Goodman, PGIM Real Estate:** It's similar for us. We start with the data. It needs a baseline, and then we set goals for our strategy around that. More organically speaking, things happen simultaneously because DEI is the kind of thing where you can observe a need and address a need, while also taking stock of the data through surveys and set long-term goals. As an organization, PGIM Real Estate has been integrating data into our DEI approach for years. We have measured progress around diversity through recruitment, retention and development. We also have well established goals which have gotten more granular over time. It is hard to parse out data from our strategy, but it certainly is a major component.

**Shannon Grenet, USAA Real Estate:** No one has the answer to which came first, the chicken or the egg. Similarly, with DEI, which came first — the data or the strategy? For USAA Real Estate, the data and the strategy

run in parallel. We are a federal contractor and an affirmative action employer. We proactively undergo an annual audit of our recruitment efforts and our internal promotions, transfers, terminations and pay equity that a third-party firm performs. The audit involves an in-depth analysis of the candidate and employee data, and provides recommended job-level goals that we should focus on increasing minority representation in.

DEI has to be an integral part of an organization's DNA. We must be intentional in our efforts and strategies to foster and sustain a diverse and inclusive culture. At USAA Real Estate, the data and strategy are collectively and simultaneously analyzed and evaluated. We slice the information in various ways and depths, which encompasses the protected classes, such as gender, race, veteran, disability and age, and expands into position levels, job groups, experience levels, education levels and so on.

Our firm's view on diversity is that it goes well beyond the protected classes. Diversity is a makeup of an individual, their work experience, education, background, thought processes, perspectives, personalities and life experiences. The moment more than one individual is in the room, diversity exists. Inclusion is present when those differences are bi-directionally welcomed, accepted, embraced and valued. In turn, employees will experience a strong sense of belonging.



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## FORMING A STRATEGY

What data do you think is the priority, and how does that inform your strategy?

**Erick Harris, Blue Vista Capital Management:** As a smaller company, we're not recruiting a lot of folks on a yearly basis and we don't typically have a lot of folks leave. Our HR department has requested data on a self-identification basis, and employees generally have been willing to self-identify. Our strategy as of last year has been to focus on inclusion as we think it will help us foster a more diverse culture and ensure everybody has a voice in the company's matters. Inclusion also helps us ensure employees are progressing in their careers in the way that we expect and hope.

**SG:** Erick is right; inclusion truly has to be ingrained in your firm's culture. If the culture is not prepared to embrace diversity, then the platform of merely hiring diverse people will not be successful. Again, it goes back to sharing the knowledge and data within the organization and being intentional about sharing it with your leaders. We ask our leaders to look at the diversity of their group today. Where is there a gap, whether it's gender, race, experience, thought process, interpersonal or technical skills? We recently formed a DEI committee to evaluate and identify various strategies, opportunities and activities that we could deploy to help improve and elevate DEI across the organization.

**JL:** One of the things we did was to get our managers and leadership to focus on gaps. It helped our leadership to understand the outcomes we wanted as an organization, and, by doing so, we got their buy-in and support of the importance of a strategy.

**DG:** By making a connection between the numbers we're seeing and the goals we have around the numbers we want to see, we've shifted our mindset. That is the key, and also the most challenging aspect. We are very specific about what we are measuring, and what the data is telling us. We work to marry data with what we are seeing on the ground through qualitative assessments, feedback from the recruiting process and exit interviews, formal surveys, informal touchpoints, etc.

**EH:** Jenn makes an interesting point about the data. The data helps develop the strategy, but, in some cases, the existence of the data can help shock management into saying, "We need a



strategy." Just seeing that data can have someone say, "You're right. I didn't think about that that way," or "I didn't think about it at all, but seeing this chart that you've put in front of me has shown me the light."

**LK:** What's worked well for us is when the operations teams could see how the numbers affect the business. For example, when the teams are looking to compete on acquiring or developing projects, one component is to report on their social responsibility efforts within their supply chain. The demographics of their vendors matter.

In real estate investment management, we are numbers people. HR can provide metrics, but if the people in the organization don't connect the corporate demographics to the business, or if we don't have adequate representation from people of color on the project, it's not going to make an impact on the bigger picture in the long term. We need to understand that, in making progress, there may be a lag between improving the mindset and the result of more diverse numbers.

Getting that buy-in and excitement and having the senior team lead their people in understanding the importance of it, connecting it outside of the corporate setting and numbers, have helped us.

It's putting DEI into the context of deals, doing good deals that get the returns and the IRRs for the investors, and getting corporate behind the idea. Erick raised a point on self-reporting — how do you collect the data? What should you be collecting?

**JL:** The first step for us was getting people comfortable with providing information and making it easy and accessible to do so. Building an inclusive culture ties closely to the trust our employees have in the organization. Once we started collecting





data, employees started watching and seeing what we were doing with that data.

The next phase for us was communicating to our team, “We gave you this opportunity to provide us this voluntary data and the response has been great, thank you. This is what we’ve been able to do with it.” Showing our teams the results of the data we collected and how it changes over time is impactful.

This is high-level aggregate data of course, so nobody is feeling exposed or recognized if they contributed data. It comes to that trust, which rolls into that inclusive culture. It is providing the ability for them to have the feeling of, “I can be vulnerable and provide this data, and I know that it’s being used appropriately and not going to be something that’s going to come back and negatively affect me later on.” We’ve been using that as our momentum to continue to collect and dive into other data.

We look into data we are missing and try to analyze if the missing data is still part of our strategy or if it will help our outcome. If the data is missing and it has nothing to do with our outcome or the impact we are looking for, there’s no reason to collect it. Sometimes people get caught up thinking about data they don’t have. It’s about focus and thinking about the data you have and what the story it tells you. We try to be thoughtful about asking for data and its purpose.

## CHALLENGES IN COLLECTION

**What are some challenges you have found when collecting data?**

**SG:** The US is the only country that tracks DEI data. We have worked with third-party labor attorneys in Europe to identify what we can collect; however, due to privacy laws, GDPR and

PII [personally identifiable information], the candidate and employee data collection and retention requirements are limited and tightly protected. It has been quite challenging to try to collect data in Europe, as well as in South Korea. Therefore, we have to carve out international employees from our data collection.

I would add that there are also challenges in aspects of pre-hire and post-hire data collection. We’re regulated by city, state and federal laws in terms of what we can ask and collect from candidates pre-hire. We are able to collect the basics — gender, race and ethnicity. Then we have voluntary disability and voluntary veteran status forms that candidates are asked to complete, but that information can be skewed because many candidates will opt out. They may not want to report on this data out of fear that they wouldn’t be considered. We find a more significant issue with collecting disability information. We find that most candidates do not disclose their disability status for fear it would place a bias against them and impact their candidacy.

From the post-hire standpoint, if the employee selected the opt-out option, we describe why we collect this data and how the data is utilized. We also ask the employee if they would like to make a change to their selection and remind them that they are able to at any time. Most of the time, the employee will provide us with an updated voluntary form. Every five years, we survey our employees on their disability and veteran status. The last time we surveyed our employees, because of the way we approached and described the purpose for collecting this data, we had 15 employees report that they had a disability that they had never disclosed before.

I would also add that we receive many DEI data requests from our investors. Investors have an increasing appetite for learning about our DEI strategies, policies and diversity stats. Although the data is similar, the type and depth of information that is being requested are inconsistent from one investor to the next. At USAA Real Estate, we analyze our DEI data in great depth, and there are many ways that we can slice and dice the data. We’re also seeing an increase in the questionnaires asking what tools and resources we are deploying and what programs have been implemented to support the DEI strategy.

**JL:** Our investors as well are asking more in-depth questions around our processes and programs around DEIB [diversity, equity, inclusion and belonging]. They want to understand our tools in place and networks we have grown to attract more diverse talent. The challenge is the competition for talent today.

**EH:** Our data collection process is primarily driven by two things: business efficiency and investor reporting requirements. With regards to ESG, it feels like there used to be more focus on 'E' versus the 'S,' and that has shifted over the past several years to a relatively equal focus on both from managers and investors. Programs focused on corporate responsibility, diversity and inclusion, giving back to communities, and even employee engagement, are becoming much more meaningful. The challenge going forward will be developing ways to quantify the results of these programs such that they meet investors' requirements.

Having said that, you do have to balance your anticipated investors' needs against the limitations of self-reporting, including survey fatigue. We're cognizant of every request we make to collect data or complete surveys. It's one more thing that people are going to have to think about. We also have to be respectful of privacy, even if the reporting request is anonymous; people, especially if they are in a smaller company, might be very hesitant to provide information because it can be easy for others to connect the dots and identify the respondents.

**LK:** Yes, there are limitations to what data the company can collect from job applicants, but for the most part I echo what everyone else said. Our DDQs, engagement surveys, corporate social responsibility awards and other documents we may be applying for are driving some of the metrics of active employees. Buy-in from senior management filters down to the rest of the team, and the reality of why the HR department is asking for certain data is helpful in the long run.

**Do investors understand that the data is self-reported and thus you may not have the data? And the failure or the inability to provide that data can be due to privacy.**

**JL:** During our conversations with investors, we try to make sure we have the right people in front of them talking about what we're doing to build an inclusive culture and community. Ultimately, I think they understand you only have what you have and that doesn't make you a good or a bad organization. It is about the steps we are taking to build an inclusive and belonging culture. It is not a sprint; it's a marathon, meaning growing a diverse and inclusive culture does not happen overnight.

We also will make sure we have supporting documentation to share when needed or when requested to

help with clarity on areas where there may not be data. Our investors value the willingness to partner and provide clarity; even if the numbers may not be exactly what they're looking for, they value the fact that we are continuously working to improve and evolve and we're as open and transparent as we possibly can be.

**SG:** I believe the investors understand and are aware of the challenges because they likely have the same requirements in their organizations. Investors like to see everything on paper, but having conversations allow them to confirm that the company is truly taking the steps and not just putting it on paper. The data can say one thing, but actually hearing first-hand, and knowing that the company is being intentional about it, makes a difference.

**LK:** During the conversations with investors, the senior team can add additional areas not inquired about on questionnaires. This opportunity is usually very helpful to have a more substantial conversation about our goals, privacy matters and related improvements on D&I.

## PUTTING STRATEGY INTO ACTION

**What are your DEI goals over the next 12 to 24 months?**

**LK:** I would like to see our demographics more balanced throughout the organization and build a more diverse pipeline and attract and retain qualified individuals from a wider talent pool.

**DG:** Our current DEI KPIs collect gender, ethnicity and sexual orientation on a voluntary basis. While we currently capture veteran status and differently abled, our goal in the next five years is to add disabilities, veteran status, socioeconomic background and mobility.

We're starting to think about how to collect more nuanced data. For disability, we're looking at both physical and neurological. We are also looking into how to collect data globally. DEI means something different in different regions of the world. Globally, steps are being taken in the UK to create a similar self-reporting structure to allow us to report; right now the only metric that can be done globally is gender — and we are even beginning to question if gender in a binary sense is an outdated approach.

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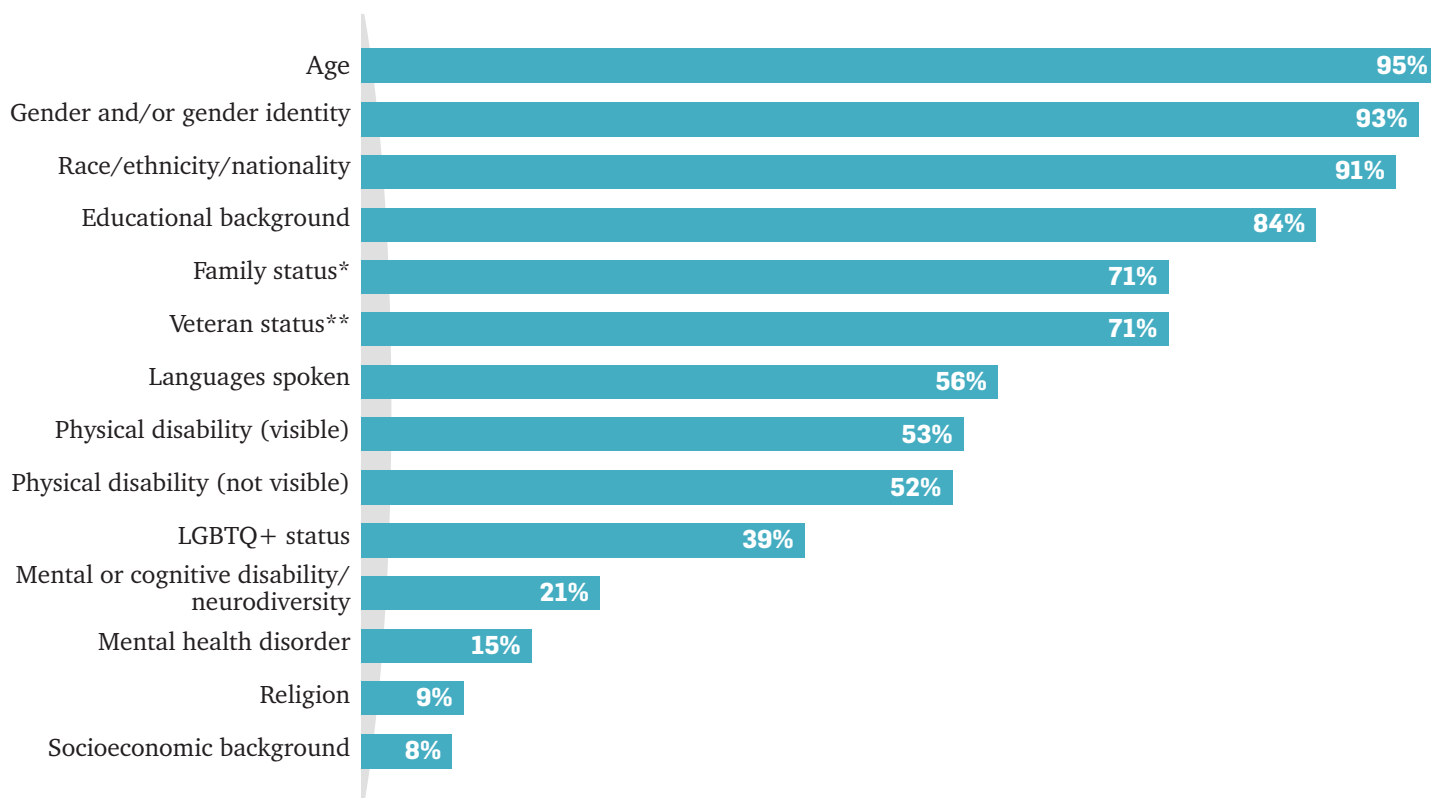
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**Which of the following demographic data does your organization attempt to collect?** Respondents chose all that applied



\* e.g., marriage/partnership status, parent/guardian status, caregiver status

\*\* Veteran status was only asked of participants completing the survey on behalf of their North American operations

Source: Global Real Estate DEI Survey 2021.

**SG:** Similar to what others have indicated, we are looking at how we can continue to increase diversity across the organization, concentrating on the mid-level and senior-level roles. We do a great job year-over-year, but how can we make more significant strides? We're also partnering with diversity-centric universities that have an interest or an investment in commercial real estate programs, and deepening those relationships with anticipation that they will increase the representation of diverse candidates.

**JL:** We're continuing to collect the data that is connected to our DEIB strategic goals to build an inclusive culture where our team members can bring their authentic selves to work every day. Making sure we're continuing to tell the story behind why we're asking for the data and why it's important, and then being able to show the impact year-over-year to celebrate together the successful efforts and programs in place.

We're also monitoring how diversity is changing. It has been tough to increase diversity in all areas of our business, but it is exciting now to see more colleges offering real estate investment management programs. Partnering with these

colleges is critical to build out and evolve our internship programs and brand awareness to attract talented, diverse candidates.

**EH:** Inclusion is critical, especially for a company like Blue Vista for a couple reasons. First, it's the right thing to do. Second, it's good company policy. And finally, realized inclusion allows a company to leverage everybody's talents on a consistent basis in order to execute on business activities and strategies.

The industry as a whole has realized its shortfalls with respect to having a diverse workforce. And as a result, if you don't have a diverse and inclusive workplace, your employees are inevitably going to get a call from some other company that may look that much more attractive to them.

One thing I'm always thinking about is finding ways to foster inclusion throughout our business processes, from routine operational process to acquiring and managing our assets — with the goal of ensuring that everybody within the company has a voice in some way, shape and form. Anything we can do as a company to reinforce that inclusionary environment for our employees is a good thing. ♦



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# Creating equity *for* UNDERREPRESENTED groups

*CREUnited was created to increase representation and AUM of underrepresented groups in the commercial real estate industry. **Jerome Nichols** of Standard Real Estate Investments and **TJ Edwards** of Walker & Dunlop speak with NAREIM about the alliance's efforts to move the needle forward for minority- and women-owned businesses, and how to create lasting change in the industry.*





## What is CREUnited and its core mission?

**TJ Edwards, Walker & Dunlop:** CREUnited is an effort to bring key players in the commercial real estate industry together to find sustainable solutions for all underrepresented groups. It is, in many ways, a response to what happened to George Floyd. We are intentional in understanding the systemic structural change that is needed and executing on that. Our view is that once we understand these hurdles, we can execute on our findings and create meaningful change.

There has been so much wealth creation through commercial real estate — and we want to ensure that underrepresented groups have equal opportunities in this space. As we are putting transactions together, we are being very thoughtful and mindful of what we're doing: is it creating a path to grow generational wealth for underrepresented groups? At the same time, we want to be aware of any unintended consequences that could have an adverse impact.

## How does the MWBE definition fit into this? What is it trying to achieve?

**TE:** Trying to define what is a woman- and minority-owned sponsor is challenging because it's not black and white. Do you look at the ownership percentage of the deal, operating company or guarantor? On the credit side, it's the guarantor.

I've heard a lot of different definitions and have yet to find one that works; I think there's always going to be a gray area. One thing I am focused on is giving my corporate partners in CREUnited an understanding of what they should be looking for when they are trying to engage with women- and minority-owned firms. It's not necessarily a financial metric, but it's control of the deal: Who's showing up to the meetings? Who's making the key decisions? A quantitative metric might not give us that. Part of this initiative is creating relationships and having conversations.

**Jerome Nichols, Standard Real Estate Investments:** At Standard, we don't have a prescribed definition of a minority business, particularly because these qualifications are too often defined by non-diverse bodies within non-diverse organizations. Defining who ought to play in what arenas from a place where there's a vacuum of diversity to begin with is backwards. Development is capital intensive and there can be various dynamics to partnership structures. Should you



### **Jerome Nichols, President, Standard Real Estate Investments**

Jerome co-founded Standard to identify and execute real estate development investments on behalf of institutions. Previously, he was senior director at CBRE Global Investors (now CBRE Investment Management) leading the sourcing and execution of new development in the Americas.



### **TJ Edwards, Chief Production Officer, Real Estate Finance, Walker & Dunlop**

TJ is responsible for overseeing multifamily loan origination and sourcing deal flow in partnership with debt financing teams across the firm. He was previously regional director of production and sales at Freddie Mac. TJ is also co-head of Walker & Dunlop's CREUnited diversity initiative.

CREUnited is working toward developing a standardized definition for minority- and women-owned businesses (MWOB). Their goal is to increase inclusivity in the commercial real estate industry by focusing on the percentage of ownership and the portion of net profits/losses accrued by individuals identifying as a minority or a woman.

automatically be penalized for not having 51% minority equity ownership? Maybe, maybe not. We take a more flexible approach to promoting better diversity outcomes through our business.

We invest on the basis that certain minority individuals have differentiated access in certain locations that lead to better investment outcomes. This may be driven by any combination of a proprietary relationship, a lower land basis or a better understanding of a diversifying user base. Then we report on what we do. It's less about defining what the box is and more about getting the work done.

The market has often underappreciated minorities within larger firms and those who own their own firms. This represents an opportunity for Standard and its investor clients with respect to both talent acquisition and investment opportunities.

“ The path forward might not be a straight and narrow one, but getting to a place where we can quantify minority participation in this space will be key to finding a solution. ”

## EXECUTING ON THE PLAN

How do we allocate more equitably?

**JN:** It is putting the investment dollars in the hands of folks who can relate, who can translate and who can bridge the gap. The people who have been allocating capital have not been from diverse communities and, in large measure, have difficulty relating to diverse developers. I have been pleasantly surprised by the reception that we've gotten from the development community, by the number of developers who are minority- or women-owned, and more so of their willingness to work with us, simply because they've never sat down at the table with someone who looks like them and who is writing a \$30 million check.

**TE:** There's a huge culture push for transparency and data sharing. I think what is causing a lag is anti-discriminatory statutes. These statutes are necessary but also create challenges and risk for corporations. For example, some of our partners within CREUnited lend a lot of capital to investors, but they aren't able to effectively collect data on whom they're lending to. We've got to find a solution and I agree with Jerome that it can't be a black and white definition.

At the end of the day, our goal is to move the needle forward for all parties involved. To my original point, are we being intentional and able to improve access and capital? And then, can we grow generational wealth? The path forward might not be a straight and narrow one, but getting to a place where we can quantify minority participation in this space will be key to finding a solution.

Are you seeing actual change in the industry among institutional players?

**JN:** I do think it's different this time. There's a credible effort by a broad set of different types of participants, but we're going to need a lot of different programs, actual individuals and

straight market rate actors. Real, sustainable change won't happen until the people who have the power to change it, perceive it to be beneficial to them. We are doing our part by executing on investments as our own minority-owned company and by allocating market-rate equity capital to other minority real estate firms.

## MAKING CHANGE LAST

This goes to the crux of CREUnited — real sustained change. How do you make it long term?

**TE:** What we're trying to do in CREUnited is to create the playbook. We're creating initiatives and programs. We're going to talk about the results and show how it has had a positive impact on the bottom line for all parties involved. Data collection is going to be key in reporting on successes.

We've been talking about DEI in the industry for a while now, but folks are getting exhausted with the conversation because they're not seeing real, quantifiable results. We are just now getting to first base and we are trying to figure out how to get to second base with CREUnited. We must show the positive outcomes from our efforts.

I'll share an example. One of CREUnited's corporate partners asked a minority-owned firm, "What do you need from us?" The leader responded with two things: first, "I need your best terms from a credit and pricing standpoint so I can execute on my deals;" and second, "In the position of power that you have in the industry, I need you to use your influence to ensure more bankers and brokers that look like me, are calling on me for my business." That is the commercial real estate ecosystem. Two weeks later the corporate partner was intentionally putting a program together to diversify their lending network.

What are your next steps?

**TE:** The next steps are putting together a database of women- and minority-owned firms that are part of CREUnited that span all different types of asset classes and roles, from development to acquisitions. Once the database has been completed, the CREUnited corporate partners can be intentional in engaging and developing relationships with these firms. We're focused on many areas to drive change; for example, addressing sponsor net worth and liquidity requirements to gain access to low-cost debt. ♦

# Benchmarking research

## 2021 NAREIM Compensation Survey Report of Findings

NAREIM | Ferguson Partners

## Compensation Survey

Released in October

Produced in collaboration with  
Ferguson Partners

More than 150 individual position compensation reports, including functions within:

- Executive management, accounting, asset management, capital markets, corporate marketing and communications, due diligence, engineering, environmental, finance, human resources, investor relations, capital raising, leasing, legal and compliance, portfolio management, property management, risk management, technology, transactions, valuations, debt and REIT securities.



## DEI Survey

Released in December

Produced in collaboration with  
ANREV, Ferguson Partners, INREV,  
NCREIF, PREA, REALPAC & ULI

First corporate benchmark for DEI metrics and best practices in commercial real estate globally. Covers more than 140 pages of individual data points, including:

- Gender and ethnicity composition by seniority and job functions.
- Best practice metrics relating to the implementation of DEI strategies and initiatives across investment management organizations, including issues relating to ownership & staffing, accountability, tracking & measurement, retention & recruitment, external partnerships and activities, pay equity & transparency.

## Global Management Survey

2021 Participant Report of Findings  
A comprehensive study of management practices and  
enterprise benchmarking metrics in the real estate  
investment management/private equity industry

Ferguson Partners | INREV | NAREIM

## Global Management Survey

Released in September

Produced in collaboration with  
Ferguson Partners

Covers more than 65 individual data points of benchmarking, including:

- *Capital raising and AUM:* Net and gross AUM growth capital raised as percentage of year-end AUM and investor concentration ratios.
- *Organizational metrics:* Headcount growth, employees per \$1bn AUM, employee breakdowns per function, per function and seniority, portfolio manager workloads (per account, psf, per GAV) acquisition officer workloads, asset manager workloads, outsourcing, average turnover, size and composition of executive committees and workloads and deal flows.
- *Financial metrics:* YOY financial performance, EBITDA (pre- and post-bonus) margins, bonus pools, revenue and expense breakdowns.



## Defined Contribution Survey

Released in September

Produced in collaboration with  
Defined Contribution Real Estate  
Council and Ferguson Partners

This report covers:

- *Manager survey:* 13 individual data points of benchmarking, including manager demographics, real estate DC capital flows, dedicated DC real estate strategies, and organizational strategies.
- *Investor survey:* 13 individual data points of benchmarking, including investor strategies, portfolio construction, target allocation and investment structures.

**For more information, please visit  
[www.nareim.org](http://www.nareim.org)**



# DEI and ESG metrics you should prioritize

*The Reporting Standards is introducing real estate KPIs for reporting on ESG and DEI.*

**T**he Reporting Standards has long dedicated itself to helping standardize how the industry reports the work of real estate investment management.

Now the NCREIF–PREA backed group has taken on the mammoth task of standardizing ESG and DEI reporting, by creating a prioritized list of the most important ESG and DEI key performance indicators (KPIs) the industry needs to consider for reporting to real estate investors and beneficiaries.

The KPIs are prioritized from hundreds of ESG and DEI questions across more than 10 industry frameworks, benchmarks and DDQ templates, and are recommended for use by managers and investors alike.

It was an undertaking like no other, according to Laura Craft, global head of ESG at Heitman and part of the Reporting Standards' ESG Think Tank of seasoned ESG professionals. "Consistent, transparent and scalable ESG information for the global real estate investment industry is no small task," she said.

“ The NCREIF–PREA backed group has taken on the mammoth task of ESG and DEI, by creating a prioritized list of the most important ESG and DEI key performance indicators (KPIs). ”

“The metrics are taken from both the Global Real Estate DEI Survey, sponsored by NAREIM, NCREIF, PREA and four other associations, and ILPA's Diversity Metrics template.”

“We know that every association, standard-setter and stakeholder brings a different and valuable perspective to the table,” added Craft. “But that also means there’s an abundance of questionnaires tackling the same and slightly different ESG priorities with no single standard.”

The metrics are taken from both the Global Real Estate DEI Survey, sponsored by NAREIM, NCREIF, PREA and four other associations, and ILPA's Diversity Metrics template. Split into three reporting priorities — those that are highest priority to have metrics around and report on, those that are recommended, and those that are optional — the KPIs are a guide to help managers and investors focus on impactful metrics in a world full of data.

On DEI, no metric is labeled as optional.

The KPIs are still in draft form, with the final version expected within the coming weeks. Here NAREIM and the Reporting Standards provide a preview of some of the corporate DEI metrics that have been highlighted as priorities for the real estate investment management industry. ♦

### Reporting Standards' proposed DEI and ESG KPIs to prioritize

*The KPIs below are in draft form and are awaiting feedback and approval by the industry*

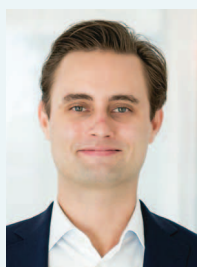
Reporting priority (draft)	Metrics
Highest priority	<b>Policy and practices:</b> Look to answer how your company addresses DEI and the formal and informal DEI policies, strategies and programs in place at the firm. Where firms are global, describe how DEI information is captured where regional differences exist.
Highest priority	<b>Organizational practices:</b> Provide details on whether your company has a formal DEI committee and who the committee reports to. Include the description of executive management's role in assessing and managing DEI and its importance to the firm.
Recommended	<b>Demographics by gender:</b> Provide metrics on the percentage breakdown of firm and/or investment leadership and senior professionals by gender.
Recommended	<b>Demographics by ethnicity/race:</b> Provide the percentage breakdown of firm and/or investment leadership and senior professionals by ethnicity/race.
Recommended	<b>Promotions, hires and departures by gender:</b> Provide metrics and trends on the number of firm and/or investment leadership and senior professionals who were hired, promoted or departed in the last 12 months by gender.
Recommended	<b>Promotions, hires and departures by ethnicity/race:</b> Provide metrics and trends on the number of firm and/or investment leadership and senior professionals who were hired, promoted or departed in the last 12 months by ethnicity/race.
Recommended	<b>Training and development:</b> Provide metrics on the number of employees that have completed diversity-related training.
Recommended	<b>Recruitment:</b> Look to answer how your company develops diverse pipelines of talent across seniority and into the C-suite. For example, diversity internships or hiring programs, contributions to diversity programs, etc.

*Notes: Firm/investment leadership equates to partners and C-suite executives.*

# The organizational glidepath for GPs in DC real estate

*There is a clear impetus for moving into the real estate defined contribution space. Having the right balance of resources including distribution and organizational, particularly in your finance team, and ensuring that you find the right fee structure are critical success factors.*

*DCREC and NAREIM members JPMorgan Asset Management, National Real Estate Advisors and Manulife Investment Management discuss the challenges and opportunities facing managers as they consider, enter and expand in the DC real estate space — and what it takes to become best-in-class post-Covid.*



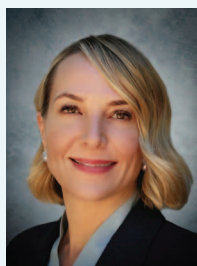
**Ben Kanne, Officer — Investments, Portfolio Management & Investor Relations, National Real Estate Advisors**

Ben contributes substantial efforts to sourcing, underwriting, evaluating, structuring, negotiating, and closing equity and debt investments for the firm. Previously, Ben was VP, Investment Banking at Bank of America Merrill Lynch.



**Kevin Ryan, CFA, Managing Director, Private Markets Business Development and Investor Relations, Manulife Investment Management**

Kevin is responsible for driving private markets real estate capital-raising and client relationship management for the real estate debt and equity platform globally. Previously, he was Managing Director at Barings.



**Jani Venter, Executive Director, DC Fund Management, JPMorgan Asset Management**

Jani is responsible for supporting the management and growth of DC private real estate solutions, and providing regular portfolio insights to investors. Previously, she was part of the senior leadership team within the real estate practice at Aon Hewitt Investment Consulting.



<sup>1</sup> The Department of Labor set out its opinion on DC plan innovation by setting out a roadmap for the inclusion of private equity or other similar investments, such as real estate and hedge funds, within a multi-asset class vehicle structure such as custom target date, target risk or balanced fund. See Information Letter dated June 3, 2020 at <https://www.dol.gov/agencies/ebsa/about-ebsa/our-activities/resource-center/information-letters/06-03-2020>

There is a clear trend within real estate investment management to move into the retail and defined contribution capital channels. When it comes to the defined contribution (DC) space, what has prompted that move for your firm and what has the journey been like to date?

**Ben Kanne, National Real Estate Advisors:** We see a large, growing and relatively untapped market with a tremendous amount of potential capital. As a platform, we are actively looking to diversify our investor base to include not only defined benefit (DB) investors, but also other non-DB institutional capital as well as retail and DC investors.

We currently have a handful of products that could potentially be well-suited for DC, but we continue to ask ourselves whether our existing vehicles are the best fit or if we would be better off tailoring a brand new product specifically for the DC channel.

**Kevin Ryan, Manulife Investment Management:** Australia has had great success with DC investment vehicles utilizing real estate in their portfolios. The same is true in Canada where public and private plans have integrated real estate and real assets into their defined contribution portfolios.

That's the backdrop of Manulife's expansion into DC real estate in the US. For us though, the main catalyst was the information letter that the Department of Labor issued in June 2020.<sup>1</sup> That really spurred an increased focus on the opportunity to launch a US DC product.

## ENTERING THE DC SPACE

What does it take to actually enter the DC space?

**Jani Venter, JPMorgan Asset Management:** Being part of a large organization has benefited the design and launch of our funds. In 2005, our off-the-shelf target date fund team recognized the value of including private real estate in multi-asset portfolios. As a result, they started investing directly in core real estate strategies with a separate allocation to REITs. We recognized the market opportunity to also launch a blended private/public vehicle where we manage the daily liquidity for investors. The DC real estate solution would offer private real estate benefits and liquidity and easily snap into investors' target date funds. We launched our first blended DC real estate fund three years later, in 2008.

We benefited from the knowledge and experience our DC and target date fund teams contributed in terms of liquidity management, structuring, guidelines and rebalancing considerations. At the end of the day, it's more complicated than you realize to effectively manage a blended private/public DC real estate solution.

We ran with that product until 2015, when a client request spurred the creation of a second vehicle, a pure core real estate solution with a lower allocation to REITs. It is interesting, because the market hasn't favored one DC real estate solution over the other. Both vehicles have continued to grow in parallel, which demonstrates investors' different appetites and different needs.

There are a lot of managers still in the early stages of considering the DC space. What advice do you have for managers not yet in the DC market?

**JV:** I don't think managers need multiple DC solutions to be successful, because it depends on your scale and the private real estate strategies that you have available as building blocks. DC investors are looking for the benefits associated with core private real estate and a core risk profile.

You also have to consider the impact of fees. A flat fee structure with tiered breakpoints can more easily be attributed daily than a structure with an incentive component. Also consider what benefits you're looking to offer the DC investor. And then evaluate the building blocks you have available that can give you variations of that option.

Investors today invest with multiple DC real estate managers for diversification. Ten years ago, they invested in one manager which represented a core beta solution. Today, investors and consultants are thinking beyond that and looking at the quality and the allocations of the real estate strategy.

As earlier stage entrants, how do you think about the right way for your firms to break into the industry?

**BK:** We currently have three primary products on our platform; our DC building blocks if you will. Our largest product probably makes the most sense. It is a build-to-core open-ended diversified offering that invests up and down the capital stack, primarily focusing on development equity and then holding the assets for the long-term. We have a diversified portfolio of new technologically advanced assets across the United States in that vehicle, which is about \$4 billion of gross

assets under management (AUM). This is one that I think could potentially make sense in this space.

There are a number of things to consider. In our thinking, we look at the building blocks that we have on our plate and wonder if it would make sense to try to use one of these as the point of entry into the space, or as we're looking and evaluating other opportunities to structure new vehicles whether or not we should pursue a completely new path and go down that route instead.

**KR:** Our Canadian product has a large sleeve of liquidity and includes fixed income as well as listed real estate. Over time, we've seen investor demand shrink for that type of product. We're still in the development and research phase, but we are inclined to allow the investor to ultimately control their own liquidity sleeve and provide pure real estate.

I think the question that we are still trying to answer is the one of real assets vs real estate. Should we be providing a holistic solution for that real assets sleeve, rather than a piece of that sleeve?

### How do you think about fees?

**KR:** As an industry, we need to address pricing. The struggle for any private market vehicle, including real estate and real assets, is the impact of its own fees on the target date fund in which it is included. Our biggest hurdle to the broad adoption of [DC] vehicles and strategies is the fear that private offerings are too costly, especially in comparison to ETFs.

## WHAT ABOUT THE ORGANIZATION?

### Where are the biggest challenges for smaller, emerging players in DC to build out a program?

**BK:** Staffing in general has been the challenge, particularly when resources are generally pulled toward other fundraising initiatives for other institutional-focused vehicles that have had a lot of success.

We're still in the market evaluation phase, but if our team can get comfortable, we will be at the point where it makes sense to consider making those hires, particularly on the distribution side which will require substantial investment. Of course, we'll need to demonstrate to our leadership team that there is a viable fundraising channel despite the issue of fees.

### What have been the biggest challenges for larger organizations?

**KR:** As we are still in the planning stage of a product launch, the biggest challenge is determining how best to position ourselves based on where we see demand. As a larger organization, we have set up a team with DC and private market resources to canvass and analyze the market.

**JV:** Our challenge as a large organization is managing and keeping DC private real estate a priority and at the top of the conversation list. We have a broad DC sales team, but they're also selling a range of different products across asset classes.

### One question that is critical to all investment managers as you build out the DC products and platforms within your organizations is, how do you integrate DC into the wider real estate investment management business?

**JV:** We focus on two ways of integrating the DC real estate solutions. On the real estate platform side, the DC funds are positioned alongside any other solutions that we offer. And on the DC side, we actively engage with the DC team to schedule market updates and education sessions to keep the solutions front of mind.

**KR:** We believe DC is a real estate product that should live in and have equal footing within the real estate infrastructure. However, the DC world has a completely different language than the traditional institutional DB market and the ability to translate between the two is critical. We view it as a real estate product with a DC distribution force. ♦

**Submissions for the 2022 DC Survey close on May 13. Please contact Zoe Hughes at [zhughes@nareim.org](mailto:zhughes@nareim.org) to participate.**

**To view the results of the Defined Contribution Survey 2021, please see [www.nareim.org/dc](http://www.nareim.org/dc)**



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## Q&amp;A

# Outposts *become in* DEMAND

For **Graceada Partners**, a value-add investor which has been operating in secondary and tertiary markets in California since before the Covid-19 pandemic, gig economy and freelance workers are institutionalizing these outpost economies. NAREIM speaks with **Ryan Swehla**, principal and co-founder, on the opportunities that

have led to the firm's reported net IRR of 67% and net equity multiple of 1.94 across nine realized assets.



## What is the opportunity in secondary and tertiary markets?

What we're seeing is this idea of the outpost economy, which is a concept of a more dispersed work environment with an emphasis on flexibility across the United States. People are moving out of primary markets for a high quality of life in secondary and tertiary markets. High quality of life is a key component, because this is not being driven by, "My employer needs me in Milwaukee." This is being driven by, "I want to live in Boise and I no longer need to be tethered to my office."

Pre-pandemic, there was already a trend toward remote work. It wasn't a huge part of the work environment, but its growth was significant. One driver is remote work, and the other one is the gig economy. The gig economy didn't exist 10 or 15 years ago. Today, with Upwork and other similar platforms, freelance and consulting work have become more mainstream. The Covid-19 pandemic accelerated this trend.

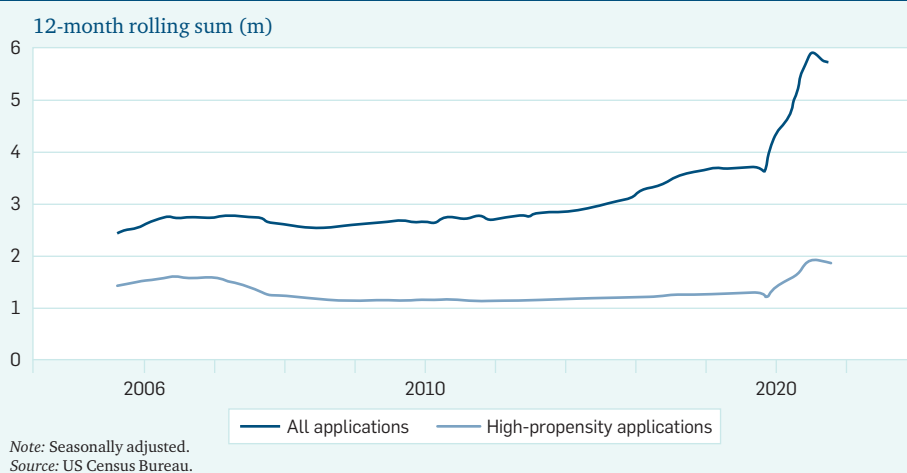
## People on the move

### What are the underlying factors driving the move to outpost economies?

The broader theme is that we had existential questions, such as, "What am I doing?" "Where am I going?" "Is this where I want to be?" "Is this what I want to be doing?" Many people sheltering at home had questions about work-life balance. "Is this the work-life balance that I want?" "Is this what I want for my family?" An outpouring of that for many people was getting up and moving.

We have heard of the term the Great Resignation, but my business partner Joe Muratore calls it the 'Great Renegotiation.' We're in the tightest job

**Exhibit 1: Gig economy workers are driving a jump in business applications for tax IDs**



“ New business licenses are the highest they've been since on record, almost hitting 6 million in 2020. That's almost double the historical average. The businesses that have low propensity to have additional employees — the gig economy — are the ones driving that jump. ”

market we've been in in decades. Employees have the upper hand in negotiation. New business licenses are the highest they've been on record, almost hitting 6 million in 2020. That's almost double the historical average. The businesses that have low propensity to have additional employees — the gig economy — are the ones driving that jump. (see Exhibit 1)

What that tells us is the gig economy is driving these changes. There are more people moving out of the labor market because they're now becoming independent contractors.

For others already on the cusp — those who hated their commutes or couldn't buy a home they wanted for

their kids — the pandemic accelerated the move. This group — perhaps 10% to 15% of people who were working in primary markets — made a permanent move to secondary and tertiary markets. They bought a home and relocated their family. This is the group that we're talking about.

### Are the secondary and tertiary markets winning at the expense of primary markets?

I would say this is a story of secondary markets being winners, but it's not a story of primary markets being losers. We're only talking about a 10% to 15% shift. That's neither seismic nor secular; that's just a small percentage of people.

“ We’re going to the markets with a high quality of life and lower relative cost of living. These are places where people are choosing to move. Interestingly, more people moved within California, than out of California. ”

**This is transformative for working age parents, the early 30- through 50-year olds who comprise most of the workforce, who want a better work-life balance.**

There are three flexible work modes. The first is hybrid work. You can work from home a couple of days a week but you need to go into the office. The second is remote or gig work, where you’re truly geographically distant. And then the third is corporations opening up satellite offices in smaller markets.

The secondary markets nearby the major metros are seeing a lot of activity since hybrid work is an alternative. Even if employees go back to the office part time, they can handle the commute.

It’s the Salt Lakes, the Denvers, the Boises, that are getting more of either the gig/remote work or satellite offices that are opening up in those markets.

## Where opportunity lies

### Which markets are you excited about?

We’re going to the markets with a high quality of life and lower relative cost of living. These are places where people are choosing to move. Interestingly, more people moved within California, than out of California. Even though population actually declined in California in 2021, more people migrated within California than out, and where they moved was inland.

We’re certainly excited about the growing inland markets in the Western United States. We are particularly interested in the secondary and tertiary markets there — those where institutional capital has had a hard time accessing due to small average asset size. Growth and momentum are there, but it has been almost exclusively the purview of private capital. We love operating in Martinez versus Oakland, Carmichael versus Sacramento, Fort Collins versus Denver.

### What is the size of the opportunity?

Fifteen years ago, multifamily was not considered an institutional asset class. It is now the fourth major asset class. Today, data storage, self-storage and single-family rentals are all getting institutionalized. When you look at secondary and tertiary markets as a broad segment, it’s pretty significant. The greater Northern California secondary and tertiary markets alone have almost \$500 billion in real estate value, according to Costar. So the broader secondary and tertiary markets nationwide represent a substantial market.

It’s a lot like single-family rental; we’re not creating a new asset class. Single-family rentals were mom and pop and they are becoming institutionalized. Outpost markets have been almost exclusively under private ownership. The market is mature.

### Everyone wants to get in, but there’s only so much scale.

Institutional capital wants large deal sizes. You will not find large deals in secondary and tertiary markets. Our operating size is \$10 million to \$50 million. We’ve looked at some that are \$70 million and it’s very hard to find deals that are much larger than that. So, by definition, you are operating in a smaller asset size.

What happened pre-Global Financial Crisis (GFC) is that institutional capital started to get into these markets because they were looking for yield when the primary markets got too expensive. The problem is that institutional capital helicoptered into those markets and they lost the most. They were buying the largest assets in the market. By definition, they’re going to have a hard time finding their exit buyer for those assets.

The big difference between the GFC era and today is we do not rely on institutional capital to be the exit strategy. Often our buyers may be private buyers. We rely on our deep, entrenched market knowledge, but we operate our value-add strategy at an institutional sophistication. We’re able to find a lot more opportunities for value than less sophisticated regional competitors — the parochial ‘cowboy.’

### Which asset types are most attractive?

There’s huge demand for multifamily, single family for sale as well as single-family rental. Because of that demographic move toward family formation, we think single-family rental will continue to be a robust market. The big driver for those is supply and demand. I don’t think we’re going to see the crazy rent increases that we’ve seen



over the last 18 months, but I do think we'll continue to see rent growth until supply and demand come more in equilibrium. I would add that markets where it's easier to develop will be the markets that probably end up with an oversupply and hypersupply, whereas the markets where it's a little harder to develop, like California or Colorado probably won't overshoot as much.

Office is an interesting asset class right now. In the primary markets, hybrid work is not going to affect square footage that much because you still need space for employees to collaborate. Where it gets impacted is remote work and the gig economy. Google is a good bellwether because they announced that they anticipate being permanently hybrid — three days in, two days flex, with 10% to 20% remote. The 10% to 20% remote will have a lasting impact on office.

Offices in outpost markets aren't as affected, as they tend to be lower density and more suburban, less reliant on heavy public transit or commute times, and relatively low real estate cost. Consequently, we've found that businesses already in our markets are returning to work to a higher degree than in the primary markets. In addition, many people who move into these markets get an independent office, either a small office or coworking space. Then you have businesses that are opening up satellite offices. To use the California Central Valley market as an example, we never saw negative rent growth in the office sector. The lowest we got was zero in Q4 of 2020, and we have seen positive rent growth since then. That should be a huge indicator of these markets.

This is a good mental picture to think about primary versus secondary markets

and how they've been affected: San Francisco Bay Area, New York and Los Angeles have a fire of economic activity that is white hot. You cannot replace the nexus of business and opportunities in those areas. What has happened is the embers have spread across the United States, and smaller embers have landed in other places. The way to think of it is not that the fire's gone out; the primary markets will continue to thrive, but high quality of life secondary and tertiary markets will continue to draw untethered knowledge workers.

### Outlook on outposts

#### What are the key challenges?

I'd say where we've been a little more cautious is the single-tenant office building. We have found multi-tenant offices to be the winner versus large floor tenants. If you're vertically integrating, you have property management, and it's not hard to manage a multi-tenant office building. But we're moving toward flexibility, and having a very flexible office building is very good.

Using the Jim Collins analogy, we like to fire off bullets and test the market and make sure we understand it and know it well, and then go big. It requires a long period of time to really get to know and understand a market. Getting to that comfort level in secondary and tertiary markets is a very slow-moving

process. And you really can't accelerate it, unless you work with sophisticated operators that already are based there.

#### Where is capital going to come from?

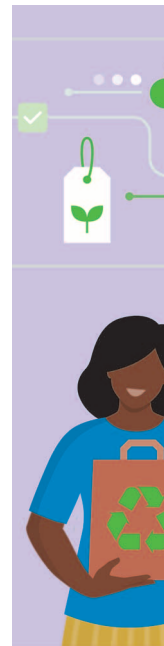
It's private high net worth, and that market is very liquid and robust. I would say it's more robust than the primary markets. Because of the GFC when institutional capital bought large assets and got burned, it's going to take a little bit of relearning for them. The reality is that secondary and tertiary markets are highly liquid if you're operating in the right asset size and you're not reliant on the institutional exit.

#### What do you think things are going to look like in around 10 years' time? Will there be more institutional players with smaller deal sizes?

We're seeing it already, the institutional focus on real estate operating companies that are vertically integrated. I believe you can't access a niche market without vertical integration. Because of the size of these markets, I think we're going to look back like we did on multifamily and we're going to say, "This is a huge market." It's learning how to do it. And the way it'll happen is investors and allocators investing with vertically integrated operators. Ultimately, secondary and tertiary markets will become institutionalized just as self-storage and other niche assets have. It's too big of a market not to. ♦

“ We have found multi-tenant offices to be the winner versus large floor tenants. If you're vertically integrating, you have property management, and it's not hard to manage a multi-tenant office building. ”

# A HOLISTIC approach drives ESG results



**The opportunity to affect ESG change is significant in the multifamily sector, but structural hurdles and a lack of uniform regulation present challenges.**

**H**ow do you integrate environmental, social and governance (ESG) considerations into multifamily assets on a national basis when there is no standardization to provide clear direction for success? For Sentinel, the integration of ESG into the operation of our multifamily communities is an evolving process, driven by investor interest, risk management concerns, and a growing body of statistical evidence supporting the long-term societal and performance benefits of adopting these practices. Operating as both a value-driven and values-driven entity presents us with a path toward policies that, when adopted holistically, provide us with distinct returns on investment, both fiscally and with respect to social responsibility.

## ESG in multifamily

Implementing ESG strategies across a diverse, national portfolio of multifamily properties is complex, and there is no

one-size-fits-all approach to integrating these efforts. Wide variability in municipal regulations, construction standards and investment strategies require that each community is addressed individually. This evaluation is most effective if it commences in conjunction with acquisition due diligence and continues through every stage of the investment lifecycle.

In Australia, we were an early entrant into the rapidly growing build-to-rent sector, where, given the absence of purpose-built multifamily assets in the country, our strategy is focused on ground-up development. We were the first to develop and operate Australia's first build-to-rent development, Element 27 in Subaico, Perth, in 2019, which set a precedent last year as the first apartment building in Australia to achieve carbon-neutral certification by the Green Building Council of Australia. The property was also designed to a 5 Star Green Star rating and achieved a 7 Nationwide House Energy Rating (NatHERS), making

By Nicholas Stein,  
Sentinel Real Estate Corporation



it one of the most energy-efficient apartment buildings in Perth. Our intention is for our entire Australia portfolio to be carbon-neutral certified.

In the role of developer, the opportunities to manage sustainable outcomes are much more ingrained in the structure of the development itself. Environmental approaches can be applied in a progressive, holistic way, from building strategies aimed at water and energy conservation, to reduction in greenhouse gas emissions and minimal maintenance and waste through the use of durable products. With added policies and operational procedures, this makes achieving a certification as significant as carbon neutral more feasible.

In the US, Sentinel primarily acquires existing assets, with a focus on core, core-plus and value-add strategies. As such, we've found that asset-level ESG initiatives must be informed by a number of factors, including the vintage of the property, its location and its existing infrastructure. In order to drive

optimal results, assessments must take into account climate risks, local regulatory environments and existing building systems, among other things. We must also balance the cost implication of improvements relative to investment goals in order to identify the appropriate strategies.

With an existing property, we are working with established infrastructure to make improvements, and, as a developer, we have full control over the upfront decisions that impact long-term sustainability and performance of the properties. These efforts include selecting durable materials and installing high-performance systems, finishes and fixtures that extend the lifecycle of the original investment and reduce maintenance requirements for both the resident and the management team. We also place a strong emphasis on the design of the communities and carefully consider the layout of common areas and amenities to enhance the social interaction and well-being of residents.

“ Installation of LED fixtures in the common and amenity areas at our Lantern Woods property in Indiana reduced common area electrical usage by 41%. ”

Across our portfolio, as properties are refurbished during the course of their holding period, we replace lighting systems with LED fixtures throughout common areas and apartments; add EV charging stations; install low-flow shower heads, water efficient toilets and drip irrigation systems to reduce water usage; and utilize ENERGY STAR appliances to conserve energy. These simple steps can translate into meaningful returns. For example, installing LED fixtures in the common and amenity areas at our Lantern Woods property in Indiana reduced common area electrical usage by 41%.

As demolition waste accounts for approximately 90% of the construction industry's waste generation, we have taken measures to reduce our waste generation such as specifying cradle-to-cradle recycled flooring content. An example is Shaw EcoWorx®, which has upfront sustainability benefits in how the product is manufactured and can also be reclaimed and recycled at the end of its useful life to create more EcoWorx® flooring products.

An important operational consideration is our residents' awareness and collaboration in responsible consumption. Sentinel's property managers are responsible for

## Value in certification

For investment managers the directive is clear; however, there is no definitive framework for implementing ESG programs. Benchmarks and certifications like GRESB, LEED and the Institute of Real Estate Management's (IREM) Certified Sustainable Property (CSP) Program provide reporting templates and have helped to drive greater adoption by providing guidelines for how to structure an ESG program — but none of these systems have provided a comprehensive blueprint for investment managers.

Even so, we recognize the value of such certifications. World Green Council Building in 2021 found that assets with green building certifications benefited from rental premiums of up to 12%, and that new buildings' asset value was expected to increase by 6% or more for green buildings. Sentinel Real Estate Fund, Sentinel's core, open-end apartment vehicle, commenced a portfolio-wide effort to obtain asset-level certifications in 2020, working within the IREM CSP Program. In evaluating certification systems, we determined that IREM — an alternative to LEED certification — presented the best path given that it is more customized to property managers, whereas LEED's requirements are tailored toward developers and contemplate items that are often beyond a property manager's control. IREM CSP certification itself is also more cost-efficient, supporting our efforts to control costs as a responsible fiduciary to our investors.

### Sentinel Portfolio Highlight



01

Nona Park Village Apartments  
Orlando, Florida > 302 units

IREM Certified Sustainable Property  
National Green Building Standard® (NGBS) Bronze

- 87 ENERGY STAR® Score
- 30.5% year-over-year water reduction
- Water reuse in property irrigation
- Bike storage
- EV charging available
- Community garden, bocci ball, and other wellness amenities
- Use of native landscaping; replaced mulch with river rock
- On-site recycling programs
- "Model minders" to deactivate lighting when not in use in models, community restrooms, and other spaces
- LED lighting installed in individual apartments
- Programmable thermostats in enclosed common areas
- Screens on balconies as barriers, furthering integrated pest management goals
- We Connect community service program

Nona Park Village Apartments located in Orlando is the first property to receive IREM CSP certification within the Sentinel Real Estate Fund, and we continue to methodically work to certify each asset in our core portfolio, obtaining 14 more certifications to date. The certification represents assessments of the properties' capital programs, daily operations, operation audits, our Sentinel Green Program — which details sustainable practices, materials and equipment — and resident outreach. IREM highlighted Sentinel's efforts and this property, in particular, as a case study in its ESG in Action publication, shown at the left.

In addition to environmental efforts, there is tremendous opportunity for strengthening the social pillar of ESG platforms by increasing the amount of programming and education provided to support community engagement and wellness. Fitness centers, outdoor spaces, community events and pet-oriented amenities provide the opportunity for improving personal health and social engagement. These efforts are also taken into account in programs like IREM CSP certification.

In either case, as an investment manager or developer, critical to the success of an ESG program is the ability to report to stakeholders, including investors. The third-party validation that comes with certification helps to increase confidence among these audiences that we are holding ourselves accountable to verifiable standards and are putting in place a framework that enables us to report our progress and demonstrate measurable results.



communicating with new and existing residents, providing them with the tools and education they need to practice more sustainable living within their homes. To that end, Sentinel has developed a Sustainable Living Guide and a quarterly *Living Green* newsletter that are provided on each property's website. We also populate our social media outlets with sustainable living tips. Where appropriate, residents sign the National Apartment Association Sustainable Lease Addendum, which addresses aspects of energy efficiency, water efficiency, waste and recycling, indoor environments and wellness.

Beyond sustainability initiatives, we have addressed the social aspect of ESG by initiating a community service program called 'We Connect' to promote volunteerism and the support of local service providers. We encourage regular community involvement through events with a larger societal benefit, such as Earth Day activities or donation drives for local food banks, Toys for Tots, the Ronald MacDonald House and local veterans hospitals.

We have also examined how our highly amenitized communities can have social benefits, from enhancing dog walks and pet parks, to converting traditional chlorinated pools to more healthful saltwater systems. We have properties with community gardens, hammock lounges, loaner bicycles, bocce ball, frisbee and putting courses to encourage outdoor activities and socialization beyond the typical pool areas.

### Challenges to sustainability efforts

While the growing attention on sustainable investment is promising, the multifamily housing industry in the

United States continues to face structural hurdles that impact adoption and implementation of sustainability initiatives. For example, it is particularly challenging to collect whole-building data for benchmarking and tracking a property's overall energy usage. The vast majority of US municipalities still do not have benchmarking ordinances in place that provide landlords access to tenant utility data on an anonymous basis in order to measure the property's overall energy usage.

Since most tenants in the US pay their own utilities and manage their own consumption, a significant amount of usage is generated by the residents themselves. We make every effort to educate and encourage responsible utility usage, but without metrics to review and report outcomes, it is an open-ended endeavor that makes the capital investment in unit upgrades a challenge to justify to investors — when the savings generated by those initiatives will not be recognized at the asset level. Fortunately, residents have demonstrated their appetite for sustainability in housing; according to ApartmentData.com, 61% of renters say they would pay more each month in rent for an eco-friendly apartment.

Additional challenges stem from the varying regulatory regimes that exist across the country, which impede efforts to adopt a uniform nationwide approach to sustainability. Just 16 US states have fully deregulated their energy markets, allowing the landlord to select a green energy option as its source of energy for common areas in their communities. Building codes also vary widely across the nation. In some municipalities, building to LEED standards is required while much of the country does not place sustainability-

based constraints on new construction. Many cities and some states require commercial buildings to benchmark their energy use or even prescribe reductions in greenhouse gas emissions over time based on building size, while others do not require any such steps. Further, incentive structures vary widely with regard to encouraging investment in green energy such as on-site solar panels. Even something as simple as trash recycling faces a wide variety of rules across the country.

### Refinement, evolution and the future

As science and technology advance, and the practical application of sustainability at our properties changes, we must continue to focus on driving better outcomes by leveraging new information to refine our programs and revise our procedures to remain in step with best practices. Throughout that process, we will continue to measure our success in these areas through recognized global programs, including GRESB, United Nations Principles for Responsible Investment (UNPRI) and IREM's CSP Program. Ultimately, corporate ESG programs cannot and should not be simply a means to check a box. They should represent a concerted and cohesive organizational effort that balances impact and investment while making a meaningful difference to the environment, to our communities and to our investors. ♦

**Nicholas Stein** is a Managing Director and Chair of the ESG Committee at Sentinel Real Estate Corporation.

# Alts on the RISE

**Despite challenges in accounting for returns and benchmarking performance, alternative asset classes offer defensive or yield-oriented core strategies associated with large institutions along with lower macroeconomic and real estate correlations.**

By Zach Mallow and Terrell Gates,  
Virtus Real Estate Capital

Investors have generally come to alternatives for robust returns and a reputation of cycle resilience. Most widely followed alternatives like medical office, senior living, student housing and self-storage have compelling historical outperformance in real estate fundamentals (that is, occupancy, rate growth and NOI), and Virtus has published extensively over the years explaining the firm mandate to concentrate in these sectors.

However, despite the rising allocations and increasing prevalence of major institutions in the space, the measurable performance advantage for alternative property types has been difficult to account for in the most central metrics: total returns. While much of this difficulty stems from the general lack of data transparency that characterizes commercial real estate, it has also come from a lack of obvious benchmarks suited to the needs of more core-oriented investors.

In this article, we summarize the most applicable sources of data covering the historical returns of alternative sectors against ‘basic food groups’ within institutional portfolios. There is ample evidence of both higher returns and lower correlations within alternative asset classes, but the entire industry still has progress to make before investors can better account for the impact of leverage or resilience of income returns in benchmarking alternative property sectors.

## Accounting for alternative returns

The relatively recent institutionalization of these sectors — since the Global Financial Crisis (GFC) — means historical performance benchmarks tend

“ Alternatives like medical office, senior living, student housing and self-storage have compelling historical outperformance in real estate fundamentals. ”

to be meager from both a timeline and thoroughness standard. For instance, NCREIF’s ODCE benchmark — the largest and longest running account of open-ended core funds — has fewer than 50 total assets classified as healthcare (including medical office and senior living) in it, representing less than half of 1% of the total index. In addition, property subsectors like medical office and workforce housing are only recently recognized as distinct investment verticals (with wide recognition largely a post-GFC phenomenon), so historical benchmarks tagging them distinctly are generally unreliable past a few years looking back.

As such, the most frequent and available sources of data for performance benchmarks generally come from sources that are distanced from a typical open-ended core fund investment structure. Many proponents of alts have pointed toward REIT portfolios as evidence from large, high quality stabilized properties. However, there are very few pure-play REITs in alternative properties, and most of them were formed too recently for full cycle records. (There is no true pure-play medical office REIT formed before the GFC). Moreover, public equities are inherently disconnected from private investments (in portfolio goals if not

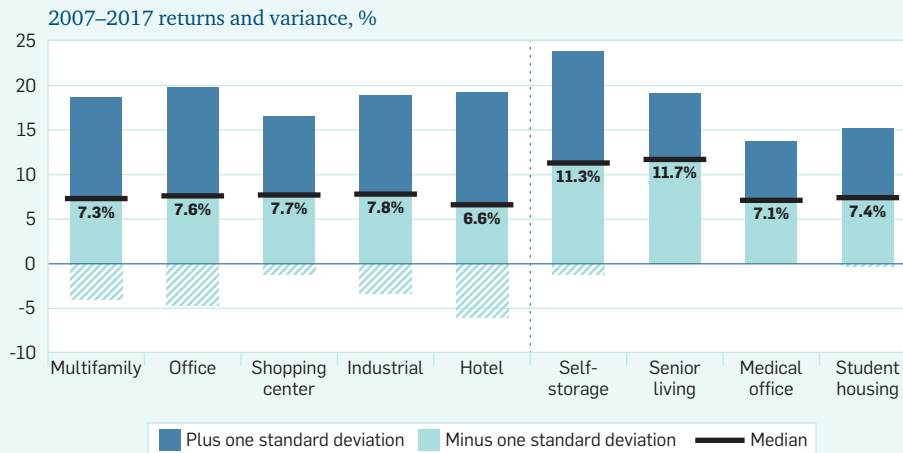
always correlations), so REIT evidence will always be an interesting but not totally compelling evidence source.

This was generally the problem that NCREIF’s NPI-Plus sub-benchmark was originally formed to solve. While NCREIF’s ODCE benchmark is generally too thin for statistically valid analysis, the NPI dataset has a greater share of alts, and NCREIF began tagging more of its data set with subsector designations a few years back. While the NPI-Plus index itself is no longer published regularly, the practice of subsector designation has remained within NPI itself. Therefore, funds and assets from the NPI dataset form the most thorough evidence available for institutionally held alternative assets, and most of the figures cited here and elsewhere derive from it. The obvious caveat is that the investment horizons, leverage amount and income portion of returns do not perfectly match a typical open-ended core structure. Nonetheless, NCREIF NPI is currently the best overall evidence for the topline potential of alternative investments.

## Full cycle evidence

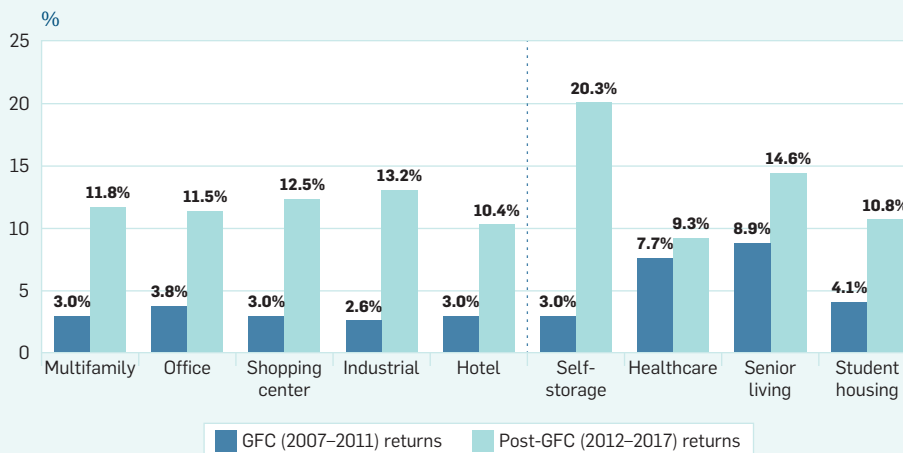
The most exhaustive benchmarking done on alternative asset classes within an institutional portfolio is likely still “Non-Traditional Property Types: Part of a Diversified Real Estate Portfolio?” by Will McIntosh, et al., published in 2017. This time frame made the 10-year total return lookbacks especially ideal for studying the full cycle of value erosion and subsequent recovery during the GFC. The authors were also able to access more granular property-level returns than are typically reported from the NCREIF NPI database, so their aggregation of sectors was both more

**Exhibit 1: Alts have exhibited higher returns and lower correlations to macroeconomic swings and other real estate asset types**



Notes: Figures cited from “Non-Traditional Property Types: Part of a Diversified Real Estate Portfolio?” by Will McIntosh, Mark Fitzgerald and John Kirk, published in *The Journal of Portfolio Management*. Student housing data began in Q4 2007. Source: NCREIF NPI Index and NPI-Plus Index.

**Exhibit 2: Alternative assets outperformed traditional assets during the GFC and post-GFC recovery periods**



Notes: Figures cited from “Non-Traditional Property Types: Part of a Diversified Real Estate Portfolio?” by Will McIntosh, Mark Fitzgerald and John Kirk, published in *The Journal of Portfolio Management*. Student housing data began in Q4 2007. Source: NCREIF NPI Index and NPI-Plus Index.

“ The largest alternative asset classes had returns that were both higher *and* less widely dispersed than institutional mainstays like office and retail. ”

statistically rich and detailed than previous efforts.

The findings were compelling: alternative asset classes were both higher returning than conventional sectors like office, and were less correlated to both macroeconomic swings as well as other classes of real estate (which largely correlate highly to each other). Exhibit 1 shows the 10-year total return distributions (25<sup>th</sup> to 75<sup>th</sup> quartiles) from the McIntosh study, with the alternative asset classes to the right having higher average returns, as well as much lower shares of negative returns (seen in green stripes).

Exhibit 2 separates this time period to show alternatives outperforming through both the immediate downturn environment of the GFC, as well as the subsequent recovery — meaning the alternative asset sectors were both more resilient to distress but did not perform solely as a ‘defensive’ strategy. Essentially, the authors confirmed that the largest alternative asset classes had returns that were both higher *and* less widely dispersed than institutional mainstays like office and retail.

In short, the McIntosh study finds that alternative asset classes were an integral part of the efficient frontier for commercial real estate portfolios — at least through the lead up and aftermath of the GFC. What about more recent evidence?

### Updated benchmarks/ Covid-era returns

According to the more recent figures from NCREIF, the relative advantage for alternative properties has held true through the Covid pandemic. There have been only five years since publication of the McIntosh paper



## The alternative opportunity

For longtime investors in alternative properties, the groundswell of institutional interest that started shortly after the Global Financial Crisis (GFC) has felt transformative, and the more recent Covid environment has only accelerated this trend.

Historically, 'alts' have been associated mostly with either higher-octane or diversification strategies; property types like self-storage and senior living have been justly valued for outsized returns, even in the historically strong post-GFC market where all sectors have been buoyed by the search for yield.

Nonetheless, many alternative asset types are equally valued for their lower macroeconomic correlations, as well as lower correlations to major real estate sectors. These qualities, combined with the rapidly maturing capital markets for such assets, suggest that alternative sectors could be equally valued for more defensive or yield-oriented core strategies associated with large institutions, rather than private investors seeking the highest risk-adjusted returns.

While alternative sectors are smaller than the conventional big five asset types, they still comprise a larger investable opportunity than many generalists expect. A following question is how much potential still exists in these niche sectors. The most obvious evidence for excess potential is the vastly different sector allocations seen between public and private real estate markets. While alts are very different from publicly traded REITs, they share a common appetite for high quality stabilized assets oriented more for current cash flow than capital appreciation. Simply put, REITs allocate over 10 times as much portfolio share toward alternative asset classes as institutional investors do.

Admittedly, many individual sectors have characteristics making them more difficult for institutions — chief among them small investment sizes and management teams that are either unsophisticated or entirely vertically integrated (as in self-storage or manufactured housing). However, the following sectors are ideal matches for institutions seeking greater exposure to real estate returns that are less correlated to macroeconomic downturns yet partake equally in economic expansions.

- **Medical office (MOB).** These are offices tenanted by physician groups, many of which require specialized buildouts. The sector is also quite vast at 1.5 billion square feet of space in top 50 MSA markets and benefit from the rapid 'graying of America' and rising healthcare costs it entails.

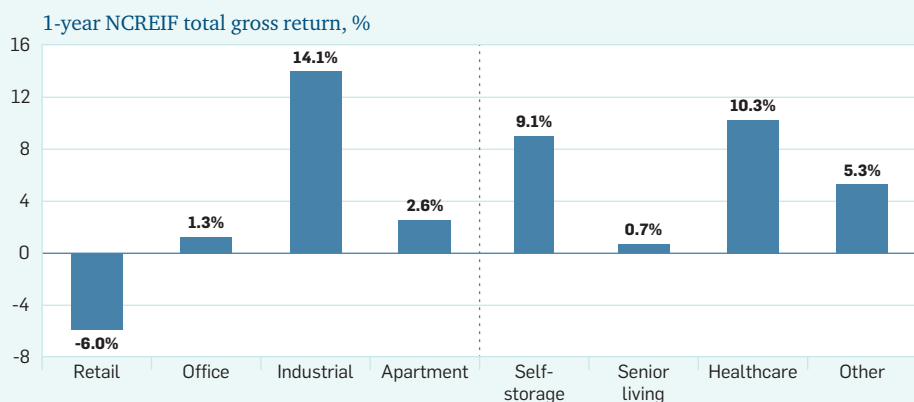
Medical office buildings have historically shown greater occupancy resilience and rental rate retention during downturns compared to conventional office, and their liquidity has also been comparably strong in downturns. The recent Covid environment has been no different, with transaction volume quickly retaking pre-Covid levels within a year. MOB assets are an ideal match for institutional investors: they demand large investments due to asset size, and their leases tend toward regular, modest escalations more conducive to core-type than value-add strategies.

- **Life sciences.** Both the upheavals of the pandemic and general biomedical progress are creating increased demand for innovative forms of health-related space. Life sciences facilities generally demand customized, state-of-the-art facilities with significant development demands, and there is commensurate effort required to understand the nature and trajectory of individual tenant firms, whose activities are complex from both a scientific and regulatory framework.

This sector offers both potential for greater institutional ownership, as well as robust sector-wide growth given the rapid expansion of venture capital funding and transformative medical advancements it drives. Clustered in major markets, there are currently nearly 175 million square feet of product, with national space demand growing at nearly 19.7%.

- **Workforce housing.** Institutions have historically opted for newer, class A trophy assets tenanted by affluent renters, but more investors are realizing that assets targeting the larger bulk of average income renters have shown greater performance in fundamentals, both during and after economic downturns.

The workforce housing opportunity was more ideally suited toward private, value-add investors only a few years ago, but greater liquidity, rising valuations and institutionalized management have changed this opportunity dramatically. Unlike shifting sectors such as retail, there is simply no way to digitally 'disrupt' the demand for rental housing in economically dynamic job centers, resulting in historic double-digit levels of rent growth during 2021.

**Exhibit 3: Alts performed strongly post-Covid**

Source: NCREIF NPI Index and NPI-Plus Index quarterly updates.

“ It is natural that more institutions are seeking greater sector diversification or access to property types with fewer headwinds from macroeconomic forces or technologically disruptive trends like e-commerce and telecommuting, which have upended retail and office portfolios. ”

results above, so while wholesale change in the results would be unlikely, there are still important developments. For instance, during the immediate post-GFC period, senior living assets had both the highest returns and lowest volatility *even among* alternative properties, but that time series fails to account for both the full crest of the sector’s record supply wave, as well as the outsized impact the Covid-19 pandemic had on the sector (especially in headline perception of risk). As such, it is not surprising that the 1-year total returns in Exhibit 3 show weaker performance for senior living assets compared to other alternatives.

Nonetheless, the previous pattern has held through the current environment — which is unsurprising considering

how much the pandemic disrupted both office and retail properties. Since these two asset types comprise 46% of the ODCE index, it is natural that more institutions are seeking greater sector diversification or access to property types with fewer headwinds from macroeconomic forces or technologically disruptive trends like e-commerce and telecommuting, which have upended retail and office portfolios.

According to the best available evidence, alternative properties are well matched to these needs, with lower instances of value erosion during economic downturns, yet equally robust exposure to economic growth. This pattern extends as far back as NCREIF benchmarks are available for the largest alt sectors, as well as for

public equities, again with the caveat that both data sets were not originally set up around these growing sectors, and as such their grouping of property types is suboptimal. For instance, the index aggregates both skilled nursing assets and outpatient medical office buildings into ‘healthcare’ real estate, despite their very different operational realities and supply/demand dynamics. Moreover, the leverage ratios and income portion of returns from NPI portfolios are not perfect matches to the overall lower risk structures and longer time horizons that characterize core portfolios.

Nonetheless, evidence suggests deployment will continue growing, benefiting both alternative sectors and portfolios including them. This was evident in 2021, when ODCE saw the highest recorded annual total return, partly due to rising shares of alternative sectors, but also aided by equally record levels of liquidity that boosted all asset classes, even troubled ones. If that liquidity proves short-lived, a rapid differentiation between sectors may arise. This is especially true for alternatives with obvious structural tailwinds and greater demand inelasticity due to their needs-based nature. Since the more direct fundamentals advantage of alternative property sectors is already better established, the emerging evidence suggests a holistic advantage for alternative sectors in direct performance, valuation resilience and total returns. ♦

**Zach Mallow** is Director of Research and **Terrell Gates** is Founder and CEO at Virtus Real Estate Capital.

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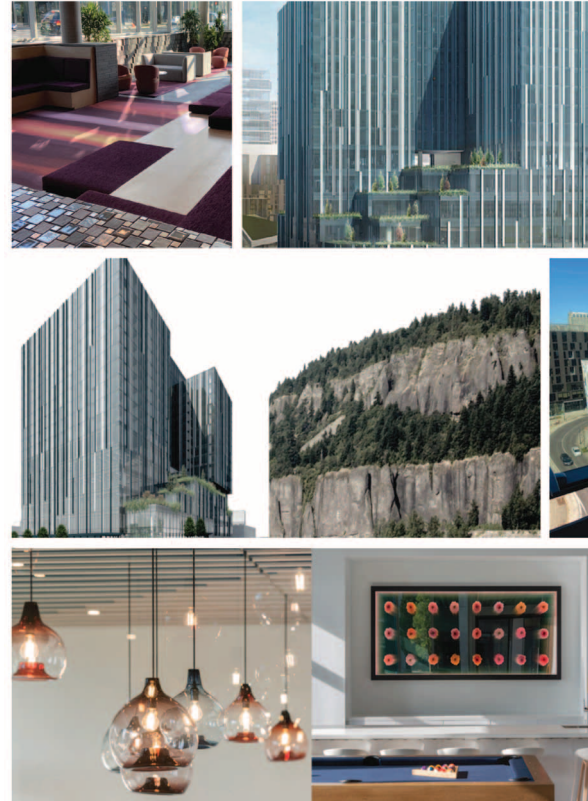
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# *Taking* **INSPIRATION** *FROM* **BIOPHILIC** *design*

**Using design strategies inspired by a connection to nature can improve multifamily tenant health & well-being, and thus outcomes.**

By Lauren Winkler,  
The Green Cities Company



**A**s the world is emerging from the Covid-19 pandemic, much is being said in the real estate investment universe of the need to prioritize the health and well-being of property occupants. In fact, the Spring 2021 issue of Dialogues featured a roundtable on building health and well-being, where arguments were made for adopting a variety of physical health-supportive strategies, from enhanced cleaning protocols to indoor air quality. The value of these initiatives for tenants and communities was undeniable during the pandemic.

What The Green Cities Company seeks to explore, however, is what can be gained for real estate investment managers, tenants and communities when the lens of health and wellness is expanded from physical health to





include psychological and mental well-being? Taking our cues from the serenity and inherent order of nature, we incorporate biophilic design into the value-add strategies for our properties to advance tenant health and well-being in even more powerful ways.

Coined by biologist and naturalist Edward O. Wilson in 1984, the philosophy of 'biophilia' proposes that there is an inherited human need to connect with nature and other biological forms for survival and personal fulfillment. In design, considerations of biophilia focus on innovative building elements like connections with the outdoors, acoustic and visual serenity, sensations of both safety and mystery, and biomorphic patterns. We have found that these perspectives deliver not only embedded value, but also tangible






“ When evaluating investments, we consider renovations and construction from the perspective of humans as a biological organism, respecting the mind-body systems as indicators of health and well-being. ”

results which deepen our ability to positively impact our residents and upgrade the multifamily environment.

### Expanding definitions of health

In commercial real estate markets, the intersection of sustainability and holistic well-being are well-documented as important return-driving factors for tenants in other real estate sectors. A

January 2022 Fitwel collaboration recommended the optimization of industrial spaces for tenant wellness to attract and retain top talent, reduce injury and absenteeism, lower stress levels and increase job satisfaction. Tying these recommendations to investment value, a 2021 study at The Real Estate Innovation Lab at MIT indicated buildings that are WELL- or Fitwel-certified command 4.4% to 7.7% more

Exhibit 1: The Green Cities Index's five pillars defines and measures the firm's commitment to ESG factors				
				
Environmental impact	Climate change mitigation	Resilience	Health and well-being	Equitable communities
Focus on optimizing the energy, emissions, water, waste and materials and furnishings used by our properties.	Action-oriented look to the future, taking bold steps to reduce fossil fuel usage and reduce emissions of greenhouse gases.	Enhancing the preparedness of our properties and tenants to withstand and recover from challenges like climate risks, social unrest and large-scale health threats.	Commitment to safety, comfort and physical and emotional wellness to improve the quality of life for our tenants.	Engagement to create a positive, inclusive impact within our properties and on the neighborhoods where they reside, driving opportunity, justice and anti-discrimination.

rent per square foot than comparable nearby, uncertified buildings.

At multifamily residential properties, the definition of healthy buildings is evolving from largely environmental factors to the intersection of these elements with tenant engagement and community impact. To address this promising interplay of sustainability with well-being and community, we developed our proprietary Green Cities Index (GCI). The GCI's five pillars (see Exhibit 1) seek to define, measure and report on progress toward a cleaner, healthier world — expanding our commitments to well-being far beyond bodily and viral safety.

Through the measured performance indicators of the GCI, we have the ability to create and track operational savings and to optimize leasing and rents, while also driving sustainable, healthy and equitable communities.

**Biophilia in real estate design**

The underlying ethos supporting this approach to residential health and well-being is inspired by nature, which is inherently health-promoting and inclusive, and encapsulated in the principles of biophilic design. When evaluating investments, we consider renovations and construction from the

**Biophilic design in action: View Smart Windows at Bower**

The Green Cities Company owns the first residential building in the city of Boston to utilize View Smart Windows, a revolutionary technology that uses artificial intelligence to automatically adjust in response to the sun. By increasing access to natural light and unobstructed views through the elimination of both blinds and heat/glare, View Smart Windows improve occupant health and productivity, as well as reducing building energy usage.

In a thermal comfort study conducted on our property, living rooms with this technology experienced no hours of discomfort relative to close to 12 hours on hot sunny days and temperatures up to 5°F above the comfort threshold.

perspective of humans as a biological organism, respecting the mind-body systems as indicators of health and well-being. Through this lens, we believe we can activate spaces that are inspirational and restorative to our employees, tenants and community, by using our biological associations with nature to integrate biophilic design with the built environment. This principle has driven our work at Green Cities since our inception, and the possibilities and impact of biophilic design continue to inspire new ways to enhance the tenant experience and drive tenant retention.

There are over 70 identified mechanisms for designing with a biophilic experience, and we take inspiration from Terrapin Bright Green's 14 'patterns' of biophilic design. The expression of these mechanisms becomes at once a value-enhancing aesthetic as well as a uniquely impactful promoter of well-being. The key is diversity in execution — not every pattern is appropriate for every property — and fitting these concepts of biophilia uniquely to reflect the property's occupants, neighborhood, priorities and culture (see Exhibit 2).

**Driving value through biophilic design**

We have found that the holistic integration of these biophilic design principles has a tangible impact on tenant health and well-being, as well as a property's sustainability. Bower, a Green Cities property near Fenway Park in Boston, uses 21% less energy (which equates to 32% energy cost savings), consumes 33% less water, and has reduced irrigation demand by 83% compared to a conventional multifamily property. Projected operational cost

**Exhibit 2: Biophilia can be executed in multiple ways in multifamily residential buildings**

Biophilic principle	Expression possibilities
Visual connection with nature	Indoor atriums connecting residents to the outdoors, mechanical water flows like fountains, green walls
Non-visual connection with nature	Auditory, haptic, olfactory or gustatory stimuli: digital simulation of nature sounds, highly textured fabrics/textiles, audible or physical connection to water, music with fractal qualities (jazz)
Non-rhythmic sensory stimuli	Unpredictable elements like billowy fabrics, reflections, changing shadows or dappled light
Thermal and airflow variability	Subtle changes in air flow like HVAC delivery strategies, systems controls, window glazing/operability, cross-ventilation
Presence of water	Seeing, hearing or touching water through elements like water walls, aquariums, fountains, artwork
Dynamic & diffuse light	Varying intensities of light and shadow such as ambient/diffuse lighting, task and personal lighting, accent lighting, dimmer controls, circadian color reference (white light during the day, lack of blue light at night)
Connection with natural systems	Seasonal and tempo simulations: daylighting systems, wildlife habitats, rainwater storage and social convergence, natural patina of materials (leather, stone, copper, bronze, wood)
Biomorphic forms & patterns	Symbolic references to natural patterning in building forms, acoustic paneling, railings, fencing, hallways
Material connection with nature	Materials and elements from nature that, through minimal processing, reflect the local ecology or geology and create a distinct sense of place
Complexity & order	Creating spatial hierarchy through wallpaper and carpet design, material texture and contour, window details, and landscaping
Prospect	Unimpeded views over a distance, for surveillance and planning
Refuge	Small gathering spaces for withdrawal from environmental conditions or the main flow of activity, providing protection from behind and overhead
Mystery	The promise of more information, achieved through partially obscured views, artwork or installation, form and flow, translucent materials
Risk/Peril	An identifiable threat coupled with a reliable safeguard like infinity edges, transparent railing or floor plane

savings related to these efficiency strategies is just under \$300,000 annually. Together, these approaches led Bower to receive Fitwel's 2021 Best in Building Health award, as well as the 2021 Massachusetts Achievement Award for Sustainability.

Broadly, the National Multifamily Housing Council reports 65% of renters say healthy building certifications would

positively influence their leasing decisions. Multifamily Executive cites 61% of renters would pay more each month for apartments with some of these features. And a 2021 survey by the US Department of Energy reveals higher levels of satisfaction among multifamily residential occupants with improved, better-quality lighting as well as longer duration daylighting. This same study

also found that for every \$1 invested in weatherization, participants received \$2.78 in non-energy benefits. Creating 'more livable' homes through a focus on air flow, thermal comfort, refuge and many of these biophilic design concepts led survey participants to miss fewer days of work and have decreased out-of-pocket medical expenses by an annual average of \$514.

Certainly, challenges to integrating these principles and patterns exist. As with most elements of the 'S' in ESG, the direct impact is often not as quantitatively measurable such as energy efficiency. Further, many of the most important impacts are indirect, such as stronger tenant retention and leasing, making direct measurement around these strategies even more challenged. With lack of precise measurement comes a lack of direct benchmarking — and, broadly, a risk of invisibility. Done thoughtfully and with creative execution, biophilic design can be so organic that tenants may be entirely unaware of the subtleties of its effectiveness.

As asset owners and managers, we hope the real estate investment industry continues to find ways to consider the confluence of environmental, social and investment value. Through advancing concepts such as biophilic design, we can increase the inclusivity of our properties and promote our tenants' health and well-being, while driving enhanced returns. Let nature continue to inspire us to create healthier, more sustainable spaces, for ourselves, our tenants and our world. ♦

**Lauren Winkler** is the Senior Director of ESG at The Green Cities Company.

# Securing *the* FUTURE

**Real estate investment managers, both mid-sized and increasingly large, have been looking to insurance companies as a new source of permanent capital for business longevity and value creation.**



By Deborah Smith,  
The CenterCap Group



**A** conversation about permanent capital is also one about creating enterprise value; it is not just about making money. But aren't value creation and making money the same thing? Not necessarily. The challenge many investment managers have is what we affectionately call the 'treadmill' problem. It is very difficult to create sustainable value for a company if the manager is simply raising capital for one fund, deploying it, selling assets and then starting all over again. You can make a lot of money and amass a lot of wealth with such a strategy, but it doesn't necessarily translate to long-term platform value creation, or, put another way, long-term business growth.

A discussion about permanent capital isn't just about the middle-market managers. In fact, for those paying attention, it has been the bigger firms that have led the recent wave of securing it.

### What is permanent capital?

Permanent capital is the holy grail of the investment manager business. Securing it can be a godsend to the one-fund manager, or it can be the catalyst to take a manager's business to the next level, or both.

Historically, permanent capital was thought of in terms of accessing the public markets. REITs — listed or non-traded, internally or externally managed — have access to the public markets, which, in theory, provide a permanent source of capital.

The internal vs. external managed REIT is interesting in the context of permanent capital. The internally managed REIT is straightforward, but the manager of the externally managed REIT effectively secures the benefits of

**“ Permanent capital is the holy grail of the investment manager business. Securing it can be a godsend to the one-fund manager, or it can be the catalyst to take a manager's business to the next level, or both. ”**

permanent capital (as the REIT PropCo is public) while the manager itself (OpCo) can be private, and arguably gets to keep the value creation associated with the REIT growth and performance.

The Global Financial Crisis (GFC) opened the door to create public REITs that were managed by private companies, allowing the manager to reap the rewards of access to permanent capital without having to become public themselves. Externally managed REITs are not new; the mortgage REIT industry has had rebirths and progression too, more so since 2009. Investment managers such as Starwood, Apollo, Blackstone and TPG, were able to create value for their own organizations by generating fee streams associated with permanent capital courtesy of the public markets while remaining private themselves. In addition, many of the largest managers have created permanent capital vehicles geared toward the retail investor courtesy of non-traded REITs.

While the non-traded REIT space has been around for decades, the adoption and capital raising by institutional firms

has been meaningful. These vehicles are permanent and many have annual promote calculations. Given the retirement needs of the aging population and the current paucity of current income investment options, we believe non-traded REITs raised a staggering \$35 billion in 2021, led by Blackstone Real Estate Income Trust. These vehicles have created the pathway to long-term platform value creation.

Then there is the business development companies (BDCs), another public vehicle catapulted to notoriety after the GFC. BDCs provide a way for retail investors to participate in private operating companies that they otherwise wouldn't have access to. Within the real estate space, there are some familiar names such as Prospect Capital, Golub and Solar to name a few, but Ares, Apollo, KKR, Blackstone and Oaktree all sponsor BDCs too. BDCs don't need to be publicly traded either.

In the fund construct, permanent capital is often liberally thought of in the context of evergreen or open-end funds, which balance the desire for liquidity with the ability to hold assets much longer than the normal 10-year closed-end fund vehicle. With an open-ended structure, there is no termination date where capital can be raised, repaid or transferred on an ongoing basis.

### A new source of permanent capital

Insurance companies have become a newer source of permanent capital. Since the end of 2019, there have been at least six large strategic partnerships between insurance companies and investment managers announced or closed.

Apollo Global Management was the first public alternative investment firm to

“ It is more efficient for managers if they can find and solidify a stable, long-term relationship that has the capacity to orchestrate capital inflows in scale. ”

invest in an insurance business as a permanent source of capital by backing Athene in 2009. It completed the buy-in of Athene in 2020 in a deal valued at \$11 billion. In 2021, three big deals were announced: Adams Street Partners announced it was forming a \$2 billion strategic partnership with American Equity Investment Life Insurance, Blackstone Group announced it was acquiring Allstate's life insurance business for \$2.8 billion, and AFLAC announced it was committing \$1.5 billion to a new real estate credit partnership with Sound Point Capital Management. This was on the heels of three other megadeals — Sun Life Financial acquired a majority stake in Crescent Capital, KKR announced its \$4.7 billion acquisition of a 60% stake in Global Atlantic Financial Group, and Carlyle led a group that acquired 97% of AIG's reinsurance business, Fortitude Group Holdings LLC, for \$1.8 billion. Permanent capital is going to drive massive AUM growth going forward.

What's an interesting outcome as the industry continues to evolve and permanent capital occupies a growing proportion of a manager's capital sources, is that arguably institutional investors will ultimately have less clout with the investment managers to negotiate terms.

### Why insurance company dollars are so attractive

It is easy to simply focus on the megafirms and their deals involving insurance companies; but, given we traffic in the investment management space every day, we can assure you these conversations aren't just happening among the bigger managers. Middle-market managers are waking up to the value creation story too. Whether creating a new insurer, or acquiring a shell or a smaller player in the insurance space, the logic is very much the same — access to permanent capital. The marriage between asset managers, real estate and insurance companies is not new; the likes of Prudential and Metropolitan Life have been big players in the real estate sectors for decades, but today it's the asset managers that are aggressively pursuing insurance capital.

Insurance companies have to hold a lot of capital over long periods because their liabilities are long dated, so they have a lot of capital to put to work. Asset managers can offer attractive yield-based investment options and return on equity. For the asset manager, permanent capital vehicles provide a boost in key metrics — consistent management fees, earning stability and AUM growth — while reducing managers' fundraising costs and reliance on realized performance fees. The fundraising cycle and negotiations with investors around due diligence, terms and economics take time and resources. It is more efficient for managers if they can find and solidify a stable, long-term relationship that has the capacity to orchestrate capital inflows in scale. It also means asset managers aren't under the same types of pressures to exit investments prematurely based on a duration limitation.

However, management fees may be calculated off a percentage of assets (as opposed to a percentage of equity as in traditional funds), and incentive fees may provide greater upside off a lower threshold, depending on the source of investments. For example, Apollo at an investor day presentation in 2020 reported that it collects 40bps of Athene's invested assets plus 100% of return above a 2.5% hurdle (for a relative comparison, Blackstone's non-traded BDC economics are 1.25% on NAV plus 12.5% on the upside). While the megafirms duke it out over the pros and cons of which are the more value-enhancing sources of permanent capital, one thing that's been reported about Apollo's retirement services is, about 10% of Apollo's workforce show up every day to work in retirement services supporting organic capital inflows from Athene of \$35 billion annually. How's that for value creation?

The industry is continuing to evolve and an increasing volume of AUM is dedicated to perpetual or permanent capital in nontraditional ways. And it will continue to grow. Insurance companies join the group of vehicles — along with REITs and BDCs — that offer the opportunity for investment managers to move away from the treadmill of returning capital to limited partners and to focus on reinvesting funds, business longevity and value creation. It can be a growth business. It will be a growth business. One casualty may be traditional institutional investors, which arguably will have less clout sometime between now and the future. While no one has a crystal ball to see how that plays out, more change is on the horizon. ♦

**Deborah Smith** is Co-founder and CEO of The CenterCap Group.

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# After the **RESILIENCE** assessments

**With climate-related hazards growing in frequency and severity, evaluating resilience when doing PCAs can determine the success, or failure, of a property acquisition.**

By Justin M. Lia,  
Partner Engineering and  
Science

**T**he ESG+R lens is a fairly new addition to the host of ways that acquisition teams assess a property. Climate data and the recent increase in frequency and severity of weather events have made it apparent that an accurate estimation of the future performance of an asset must include its ability to withstand climate-related hazards.

By incorporating ESG+R evaluations into their due diligence process, investment managers get not only the data they need early enough to develop an accurate pro forma based on informed assumptions, but also the opportunity to correct their strategy should the data warrant a change. For this reason, resilience assessments are becoming a frequent component of, or addition to, equity-level property condition assessments (PCAs).

In the pragmatic world of real estate, the 'R' in ESG+R — resilience — is critical to building value and performance. Property resilience is the ability of a facility to adapt to, and

withstand, disturbances while retaining its basic structure, function and self-regulation. Resilience includes the capacity of an asset to adjust to, and recover from, various external forces including severe weather events and the gradual effects of climate change. Structural concerns, as well as business interruption, are important: how quickly can the building be safely re-occupied and returned to its intended use?

Resilience assessments provide qualitative and quantitative data to address this question and expose weak points in a building's performance. This approach has been considered for many years when analyzing buildings with a high importance factor such as hospitals, emergency services facilities and critical infrastructure. Far from an exact science, resilience assessments attempt to weigh many variables regarding the size, age, condition, use, location, management and environment of a site in the context of the vast spectrum of possibility for future disruptions.



In other words, resilience consultants ground their evaluations on both the known characteristics of the building and an educated guess based on available data, of what could possibly happen in the future: storms, floods, earthquakes, hurricanes, fires, extreme temperatures and variations in severity of each. They consider the data available and write a range of scenarios for would-be investors to consider.

Investors review their evaluations from a range of perspectives shaped by more variables, such as risk tolerance, business objectives and stakeholder influence. It is no wonder, then, that resilience assessments can yield varied results, and investors respond differently to resilience assessment findings.

When a resilience assessment identifies significant risk, investors have a range of options available. Backing off the acquisition is one option, but not a common choice. Instead, they are more likely to implement risk mitigation measures or pivot strategies to reduce their exposure. The following are several real-world examples of how different investors chose to respond to their resilience assessment findings.

### OPTION ONE: Proceed with clarity

A global real estate investment firm with \$50 billion in AUM sought to acquire a newly constructed multifamily complex in Texas. The project had a winning combination of demographics and location, and, with proper management, could be positioned to capitalize on the rapidly growing local rental market. The plan was to hold the asset for three to five years until occupancy was stabilized, rent growth realized and seasoned financials could

“ In the pragmatic world of real estate, the ‘R’ in ESG+R — resilience — is critical to building value and performance. ”

be presented to prospective buyers for a profitable sale.

It was a promising enterprise, but with one significant caveat: the complex was located in an area prone to sinkhole activity. During construction, the contractor encountered two active sinkholes on the site which had been remediated. Would there be more? The likelihood of future sinkholes developing was initially unknown. All parties knew this could be a deal killer. How could the buyer get comfortable with the risk? Would they have time to properly assess the risk within the purchase and sale agreement due diligence period?

While many investors might have walked away at the mention of sinkholes, this deal had a lot going for it — with one known weakness. There is a lot of pressure to place capital in the current real estate investment environment, but no one wants a bad deal. The buyer needed an in-depth evaluation of the geologic hazard potential at this site to move forward with the acquisition.

In addition to standard due diligence reports, the buyer requested a resilience assessment that reviewed geologic hazard. The scope of this report leveraged the most technical scientific resources available and local knowledge compiled over the past 60 years. A team of geotechnical engineers, civil engineers and geologists performed a geologic peer

review of the pre-construction geotechnical investigation and the repair and closure of the sinkholes, which included an opinion of exposure to risk from future sinkhole development.

The geologic review involved LIDAR, an advanced aerial imaging technology that facilitates large-scale topographic studies to identify risk indicators of major sinkhole activity. Local experts provided information regarding historic activity, as well as the geological nature of the site and surrounding region. There was no evidence of large-scale sinkhole activity within 15 miles of the property.

Using a regional geographic information system (GIS), the geotech consultants were able to evaluate the location and scale of all known cave systems in the area. No significant known cave systems were found to be within 19 miles of the property. While it is impossible to rule out the possibility of future sinkhole activity at the site, all available data indicated that major issues were unlikely. In this case, a thorough assessment of risk allowed the investment firm to proceed with acquisition and implement their original business plan for the site.

### OPTION TWO: Strategy pivot

Risk assessment findings will sometimes trigger a reevaluation of original objectives for the target acquisition. Recently, a private equity investor ordered an extreme weather and natural hazard risk evaluation to supplement a PCA on a 260,000-square-foot, three-level warehouse building in New Jersey.

The investment objective for the site was a land-carry play, where the investor would hold the property for about five years and collect rent from a

warehouse operator tenant. However, the risk evaluation determined that the site was at risk for storm surge flooding. Storms of similar severity to Hurricane Sandy would cause the basement level to flood, but the upper floors would likely remain dry. A category 4 or 5 hurricane could flood the ground floor. The probability of such a storm at this location was very small, but, if one did occur, the outcome was projected to be devastating to this property.

Presented with these findings, the investor determined that the site was not ideal for warehouse use, and likely would not command the rent rates necessary to fulfill their original investment objective for the site. However, the building was priced well enough for the investor to complete the purchase and flip the property to a multifamily developer, which planned to clear and fill the site and build an apartment building that could be designed to withstand storm surge.

### OPTION THREE: Mitigation

A global private equity group planned to acquire a large, historic building in New York City. The site, as large as a city block and listed at about \$900 million, was being used as a storage facility. The private equity group planned to invest another \$500 million to convert about half of the property, from self-storage to office use. Existing tenants would stay in the remaining half of the property and provide cash flow during the redevelopment.

The evaluation was complicated. The construction project, about 40% complete when the building was being evaluated for acquisition, was on its fourth program iteration. Due to the building's historic

### More options for resilience Improve design above code minimum

If cost-effective improvements are identified in pre-development, design changes may be implemented to improve resilience. Properties designed for resilience may command higher rents from tenants who are particularly sensitive to business disruption.

#### BORP

Building occupancy resumption programs, or BORPs, are response plans designed to facilitate rapid re-occupancy after events such as earthquakes or severe windstorms. BORPs typically require an engineer on retainer who will commit to prioritizing response to the subject building after a disruptive event, when the demand for city or deputized inspectors is often high and so they may not be able to prioritize your asset or inspect it with due care.

#### Insurance

Insurance, including business disruption insurance, may be used to offset risk. Some insurers will recognize a discount for customers with resilience measures or certified ratings, such as BORPs, in place.

nature and previous uses, some of its critical infrastructure — original and current — was poorly located and prone to flooding. During Hurricane Sandy, an underground electrical room flooded and failed, causing 45% of tenants in the building to lose power.

Review of historic documents during site due diligence revealed that New York City utility provider ConEdison had cited the problematic electrical room and would not restore it if it failed again; the electrical room would need to be decommissioned. Left as it was, the underground electrical room presented significant risk: a storm event could not only cause tenants to lose power, but the outage could potentially go unresolved for an extended period.

Armed with this information, the private equity group elected to relocate the electrical room to the fourth floor to proceed with their redevelopment plan. They determined that the cost of mitigation was less than the risk posed

by potential loss of power, and therefore rental income, from remaining tenants, while half the building was vacant during redevelopment. Although not insignificant, the cost of relocating the electrical room was minor relative to the size of the project; in this case, mitigation was a viable option.

These are far from the only options available to would-be buyers who uncover resilience risk during due diligence. Resourceful and creative investors find ways to keep their deals on track. The common denominator is that after a resilience assessment, each firm had the data and perspective required to make an informed decision and determine the best course of action for their desired outcome. ♦

**Justin M. Lia, PE, LEED AP** is Managing Director with Partner Engineering and Science, Inc.



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