Top 10 with...

Interview with Benoit Delaby on Real Estate Customized Mandates

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RECM facts

2000

business established

USD
2.4bn

invested[1]

~USD
1.5bn

in AuM[1]

Assets across
11

countries

Benoit Delaby, Head Real Estate Customized Mandates, Real Estate & Private Markets

Client-driven innovative solutions

The growing appetite for real estate among Ultra High Net Worth (UHNW) investors has grown intensely over the last decade especially after the COVID-19 crisis. In these uncertain times, the Real Estate Customized Mandates (RECM) business is re-engineering its tailor-made investment solutions in real estate for private clients to make them even more appealing to clients. Benoit Delaby, Head of RECM, explains to us how.

1

What led to the establishment of the RECM platform in Switzerland?

We first established our business in Switzerland around 20 years ago to see how best we can serve UHNW real estate investors and provide them with investment solutions in direct real state. For decades, real estate has formed a major part of UHNW investors' portfolios, as part of their strategic asset allocation. However, the whirlwind of the 2008 global financial crisis (GFC) caught some of these investors off guard (lack of liquidity, loss of equity) a consequence of the risk they had taken while investing.

Consequently, the GFC revealed some investors' demand for higher transparency and control over their investments and we started to see an increasing shift towards more bespoke, interactive and flexible investment solutions. RECM's platform was the perfect storm, and set aside commingled funds by offering UHNW clients both the confidence of an institutional-like service, whilst enjoying the benefits of a personal and tailor-made solution with a broad global reach which leverages on our wider Real Estate & Private Markets (REPM) global platform.

2

What are you offering to clients?

Our extensive European core platform provides individual clients with access to bespoke, interactive and flexible investment solutions. We launched an innovative direct real estate co-investment solution targeting private clients together with UBS's global Wealth Management business in August 2013. And, with continued interest from clients to access European direct real estate, we launched the successor strategy in 2015. Clients are given the choice to invest in different types of pan-European strategies including, core, core-plus and value-add. This exclusive co-investment solution offers attractive direct commercial real estate investment opportunities providing investors with the choice and flexibility to choose from a consistent deal flow of high-quality properties. In addition, clients have unfettered access to the team that manages the assets on their behalf. We provide an end-to-end service, covering the whole investment life cycle, while the client retains full decision-making power on the purchase of the suggested assets.

For segregated mandates, we offer clients both international and pan-European programs tailored to meet the needs of individual investors including translating their investment expectations and risk appetite into strategies, geographic and sector allocations. Our strategies are based on our understanding of the market and asset cycles backed by specific market data and research provided by our in-house real estate research & strategy team. Mandate investors mainly focus on income generation, which typically leads to capital preservation with potential for long-term growth. Obviously for this offering, clients need to give up on diversification in order to gain full control as this strategy targets larger lot sizes which come close to institutional size.

In addition, we invest in desirable locations and target top-tier cities. In our experience, these assets often attract occupiers that provide consistent cash flows, which can lead to stable performance for our investors. Through leveraging our wider global network, we believe we have the expertise, network and local knowledge to stay on top of any market developments, whilst actively managing assets to provide the best results.

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How is the COVID-19 crisis going to impact investors and commitments?

In our view, global real estate values will decline in 2020, before rebounding in 2021/22. The exact magnitude and timing will largely depend on how the virus evolves. Though we do expect this movement to impact existing investors, the forecast for the re-pricing of risk will provide an attractive entry price and create a window of opportunity for new entrants. For example, our club deal offering is an existing structure which enables immediate deployment of equity in line with deal origination. New investors will not be impacted by NAV or performance legacy as they would only participate in new rebased deal flow. Investors will still retain full discretion on which strategy, geographic location and deal they wish to participate in. This would be aligned to their investment objectives and risk appetite as this is in the DNA of the offering.

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Have you made any changes to your club deal offering following the crisis to make it more attractive to investors?

The concept and philosophy of the club deal offering stays the same. It provides exclusive access to direct real estate investment with full selection capacity and the discretion to participate in a proposed investment. However, we have simplified access to deal flow by giving investors visibility of the deal pipeline after subscribing. In addition, investors can defer payment of upfront capital upon commitment to the first deal or latest after one year.

We are also allowing investors with a lower total allocation for real estate to get on-board by limiting the minimum commitment amount to EUR 10m. Therefore, we have designed higher flexibility on the minimum deal commitment to still allow for reasonable diversification.

Our extensive European core platform provides individual clients with access to bespoke, interactive and flexible investment solutions.

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Over the last 3 years, RECM has been seeing strong client inflows – why is that?

Most UHNW will tell you that that they are quite fond of real estate. According to a recent PWC survey, approximately 1 in 2 would have a 20-40% allocation to real estate. This is a long-lasting love affair with an asset class that acts as a transferrable, long-term store of value. Real estate has an above average mindshare with clients and can be a useful door opener with prospects. Today, it is seen as one of the only asset classes that can deliver predictable and sustainable revenues with some sort of inflation hedge.

UHNW investors are playing an increasingly significant role in commercial real estate investments in what was once a predominantly intuitional group space. There are many reasons for the growing appetite from UHNW investors including capital growth and diversification, and the income accessibility which offers attractive benefits for larger portfolios of individuals and family offices. In today's low-yielding environment, real estate is becoming more and more attractive given the wide diversification not only through property investment, but geographically especially as our business has been seeing in Europe, APAC and other developed markets. Private investors are also becoming increasingly attracted to the stable cash flow income component of real estate. For many private investors, it's just as much about growing capital as it is to preserve it. A business such as ours, which offers a well-diversified pipeline across geographies, sectors and currencies, means we are truly a one-stop shop providing access to invest in diverse markets across the entire risk-return spectrum.

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More private investors are opting for club deals, can you attest to this?

Some of our clients want to invest alongside a small number of other like-minded investors – particularly where they can have influence over financings, business plans, dispositions and other major decisions. Over the past few years, we have been seeing a growing appetite from larger investors seeking alternatives to the traditional fund model to keep control of the investment decision and gain access to larger, and a much broader set of deals, than if they had invested on their own. Since 2014, our business has developed two club deals focusing on European real estate markets which have attracted over 40 clients from across the globe. By the end of 2Q19 the clubs will have successfully invested into 11 properties across 5 countries.

The first club acquisition which took place in July 2014 was a brand new office development in the east of Cologne's central business district in Germany. This asset is strategically located in the newly to be developed suburb earmarked by our local acquisition team as one of Cologne’s growing submarkets. Upon disposition of this asset at the end 2018, investors realized an IRR of around 16%[2].

Club deals give our investors access to ongoing deal flow thanks to their membership of an exclusive investment club. We focus on core / core-plus assets in key European real estate market. We've been seeing club deals as an effective way for investors to deploy large amounts of capital with a sense of diversification while giving them the enhanced discretion they desire. These types of deals normally require a greater degree of trust. But, we understand that a key to the success of any club deal is bringing together truly like-minded investors.

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How are segregated mandates addressing the needs of your clients?

Segregated mandates allow for us to undergo a fully tailored investment approach to meet our clients' specific risk-return and management needs. Typically, segregated mandates address the expectations of our largest investors that are willing to retain control in exchange for limited liquidity and diversification. In doing so, we develop customized portfolio strategies that balance the protection of capital with the provision of a sustainable growing stream of income, particularly in various challenging economic scenarios.

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What are the key themes you will be focusing on post-COVID-19?

Going forward, we expect even more investors to be focused on the income component of real estate. These investors will be looking for managers with capacity to generate net operating income growth in their property portfolios. Modern core office properties, in markets with a global status should be less affected and are expected to bounce back more quickly, particularly in locations with a diverse occupier base. With this in mind, we will focus on well-connected markets and assets offering flexible occupation. Our goal is to adapt to changing corporate occupiers' requirements and the anticipated reduced footprint.

The expected re-pricing of risk premia for core and grade B office buildings will create a greater need for value-add strategies. In the past, pricing differences made less sense given the associated additional repositioning and leasing risks. However, there is now an opportunity to deliver office space in supply constrained markets to match post-COVID-19 requirements. Post-pandemic structural change in the logistic and industrial sector should continue to drive capital values. Fast e-commerce growth facilitated by lockdowns, relocation of production closer to the end consumer, and the increased awareness of self-reliance on "strategic" production are just some of the themes we expect to contribute to the strength of the real estate sector.

Lastly, ESG has become a key focus for both occupiers and investors post-COVID-19. We expect ESG to continue to be a driver for long-term performance, especially with regulators putting more attention on the topic.

Overall, COVID-19 is accelerating trends that were already observed before the crisis. In addition to the increased focus on ESG, some of these trends include increased digitization, increases in remote working, reduction of office space per employee and accentuated difficulties in the retail sector.

> Structural change will reshape the real estate investment universe providing opportunities for repriced investments.

9

What are the benefits of an entrepreneurial approach in comparison to a typical asset allocation approach?

Our business is driven by an entrepreneurial, independent and creative mindset, leveraged by our deep expertise, disciplined value-generation approach and our strong global network. This allows us to identify both strengths and weakness in any deal and begin assembling the missing pieces to form something truly worthwhile. Our detailed underwriting focuses on those all-important strategic considerations in rebalancing including transaction costs, risk aversion, correlations among asset classes, volatility, and beliefs concerning momentum, taxation, and asset class liquidity.

In today's market, investors are increasingly attracted to the high income that real estate can offer in comparison to other traditional asset classes, as well as its low correlation to traditional markets.. In light of the market changes, an entrepreneurial mindset works to support our wider efforts to select the right priced opportunity in view of changing market dynamics and take on proactive asset management and ongoing analysis as a key part of the portfolio management process. A constant focus on value helps us to accumulate and maintain the wealth of our clients' portfolios – across various economic cycles – to meet their needs and aspirations.

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How do you differ from your competitors?

Investors are now investing with both head and heart, many of whom bring with them a range of practical and personal investment needs. We offer our clients a highly personalized, interactive service where they have a hand on the steering wheel for making those all-important investment decisions into real estate. Firstly, we start by defining personalized strategies according to investors' individual risk-return profiles.

Our investment offering is a one-stop shop supporting clients from structuring, sourcing to financing through our established network of reliable national and international lenders until management and exit. Our business can facilitate complete structuring solutions and provide access to the relevant property market, expertise and skills. We monitor all dimensions of investment management, whether it be legal structuring, tax, due-diligence, financing or tactical asset and portfolio management. Our playground is global, supported by the extensive UBS Asset Management, REPM global platform of 500 professionals which enables us to have local reach in key developed markets.

Finally, our range of tailor-made real estate products and offerings works to meet the needs of clients with a range of profiles and needs. Over the past five years, RECM has grown successfully via its two European Property club deal vehicles which provide our clients with access to ongoing deal flow. We equally provide investment solutions for those investors who are looking for more bespoke, interactive and flexible investment solutions. Our service is tailor-made and puts the client at the center of all activities.

Notes: **1** All data as at 31 December 2018 unless otherwise stated. Assets under management stated on gross asset value basis, reflecting property values as at 31 December 2017, where available. **2** Past performance is no guarantee for future results.

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