Hines

Hines

Buying, building and managing to core

Chase McWhorter, Institutional Real Estate, Inc.'s managing director, Americas, recently spoke with **Adriana de Alcantara,** senior managing director and fund manager for Hines U.S. Property Partners (HUSPP), Hines' flagship core-plus open-end real estate fund. Following is an excerpt of that conversation.

Would you give us an overview of your investment strategy?

I am the fund manager for Hines U.S. Property Partners, our open-end core-plus fund. It is our flagship fund. It is diversified, and we target a 9 percent to 11 percent net return.[1] We buy well-located assets in the best U.S. locations with high barriers to entry, and we add value through active asset management and repositioning. We also do up to 20 percent in build-to-core.

What is your definition of core-plus?

We think of core-plus as a blended approach, blending to a core-plus return. We don't have a levered-core strategy. Sixty percent of the portfolio is core assets, 20 percent comprises value-added assets, and 20 percent is build-to-core, our ground-up development. It is a very dynamic portfolio. For example, we have a development in Boston that is two miles away from Boston's Logan Airport. We started construction in summer 2023 and plan to complete it [as of this conversation] in summer 2024. Once it's complete and leased, it turns into core.

What are the benefits of having a core-plus approach in today's market, versus simply a core approach?

There are two main benefits: flexibility and keeping the portfolio young. In terms of flexibility, we can take advantage of market dislocation, as we are seeing right now. And we can benefit from the whole cycle – secular dynamics and shifting demand – in any style or sector. Right now, we're selectively looking to take advantage of market dislocation when possible, then adding value to the assets through tailored capex and management.

The second point is keeping the portfolio young. We don't have a specified benchmark as a core-plus fund, so we look at the NFI-ODCE index as a guideline. The average age of properties in the index is 27 years, and investors are talking about redemptions. But because of the lack of liquidity, the ODCE funds are not investing in their assets, and these assets are getting even more obsolete. Properties in our portfolio are 12 years old on average.

What is your sector allocation, and what are your high-conviction sectors?

Eighty percent of the portfolio is in industrial and living sectors as of second quarter 2024, which is in line with our strategy: overweighting the living, industrial and alternative sectors and underweighting office and most retail. With industrial, we like locations close to irreplaceable infrastructure and with access to labor. In the living sector, we like transit-oriented apartments and build-to-rent communities. We just acquired one large BTR community in Charlotte, N.C., which is the first BTR community Hines has ever acquired. We also like student housing. The alternative sectors we target are data centers, self-storage and medical office buildings. We have two small medical office buildings, and in the past, we have developed and managed U.S. data centers. I don't think there is a place for acquisitions of data centers currently, as the market is frothy, and these are usually very long-term leads that act more like a bond. So, we're thinking about data centers more on the development side. We want to build, lease and sell, as demand for data storage continues to grow.

Can you tell me how you are set up to work on all these sectors?

We have a fully integrated platform with more than 3,000 people in the United States. I travel every single week, and everywhere I go, there is a Hines office. Our property managers, asset managers and local market experts know their locations and know the buildings. To us, that means access to a pipeline, which makes the difference for me with a diversified fund. I don't think any other U.S. company has this kind of powerful platform. I'm fortunate to have great number of resources and a fully dedicated fund management team.

We also have a full research, portfolio management and finance team, all working to put the best of Hines together in a fund. I have more than 25 years of real estate experience and have seen research used in different ways. Some people use it as a marketing tool. We use it as a guide for investment decisions, and it makes a difference in adding value to the asset and accessing the pipeline.

What are your views on the current market, and how is your investment strategy evolving to adapt?

The past 18 months have been challenging for anyone in the real estate market, with dropping transaction values, significant value declines across all sectors and tighter financial conditions. We have kept our strategy consistent, however, and have avoided style drift. We have kept our leverage very low, especially for a core-plus fund. At Hines, we have been extremely careful with leverage, and it's paying off right now. A third point is our patient deployment. With an open-end fund, we are constantly raising money and constantly deploying. We have no redemption queue. We are probably one of the very few funds in the market that has an entry queue.

Tell me more about your strategy for financing. How are higher interest rates impacting it?

As I mentioned, low loan-to-value [LTV] is very important to us. An environment where, in principle, interest rates will eventually stabilize from where we are today should be a very good environment for a core-plus fund. Our LTV target is 40 percent with a limitation of 50 percent, and we were at 32 percent in the second quarter. We have equity, and we just expanded our credit line in the first quarter to more than $400 million. And it was oversubscribed, with five banks funding it.

Can you talk about your most recent acquisitions in the living, industrial and alternatives sectors?

While we have been patient deploying capital, we have deployed more than $1 billion in the past 18 months in 11 transactions, with an average cap rate of more than 6 percent. These are primarily in the industrial and living sectors. Our most recent acquisition is a multifamily property, Lennox & Quinn in Jersey City, N.J. Built in 2018 and located 15 minutes from Manhattan, the asset is 96 percent leased with roughly 400 multifamily units, and it offers unobstructed views of Jersey City and the Statue of Liberty. We purchased it for $222 million, well below replacement cost, with a cap rate in the high mid-fives. Also in the living sector, in the first quarter, we bought our first BTR community in Charlotte, N.C. It is quite large, with 550 units over 75 acres. There are two components: 365 units were built in the past year, and they are fully stabilized. Then, we're buying on a forward agreement for 185 units. With this property, we really reach a very broad base. The property offers everything from studios to four-bedroom units. It has attracted single people and families, and it's south of downtown with easy access to the Blue Rail Line to Charlotte Uptown. It's a very nice property in an area we really like. We are looking at additional BTR communities, primarily in the Sun Belt.

In industrial, we were awarded a large transaction that we closed in July. Prior to that, we acquired an asset in Chicago in December from an open-end fund, which is our first industrial property in Chicago. We have been very patient buying industrial in the large distribution hubs — Dallas, Atlanta and Chicago — where it is much easier to build. That acquisition was all about market timing. It's 100 percent leased, 10 miles south of Chicago O'Hare International Airport, and we purchased it for 50 percent of replacement cost.

Are you doing any development? Does it make sense to develop right now?

Of course, when you can buy, for example, the Chicago property so far below replacement cost, it doesn't make sense to develop. The fund has a 20 percent allocation for development. Right now, we are well below 10 percent. We only develop when it makes sense for us. We have a couple of developments in an irreplaceable location. As an example, we are developing an industrial asset in Boston, which is the last site close to the airport. From the site, it's two miles to the airport. That makes sense in this environment. That is an irreplaceable location. We bought another piece of land that is 15 minutes away from Harvard University and is opposite to the Harvard Enterprise Research Campus, and between Boston College and Harvard. This site has been retitled for multifamily. We believe Boston is very pro-multifamily right now. That is another irreplaceable location, and that's where development makes sense right now.

Let's shift to capital flows. Tell me about your investor base.

Our investor base for the open-end fund is already very diversified. It's still a growing fund at $2 billion in gross asset value, but we already have 33 investors, with about one-third of those from the United States, and one-third, Europe. We even have a U.K. public fund invested in our fund. We also have a number of Asian investors from Japan and South Korea.

How has it been raising money in this environment?

2023 was a difficult year for everyone, including for us. But toward the end the year, we started seeing the light at the end of the tunnel. We did close two new investors in fourth quarter 2023. Year to date, we have an additional five new investors. We believe the market is getting better. Returns have started to turn the corner, going up in the first quarter of this year, and the second quarter is positive, as well, and well above the NFI-ODCE index. The appetite for core and core-plus real estate is coming back.

Notes: [1] The target return is net of fees, expenses and taxes within the structure and carried interest, but gross of any tax payable by investors in the fund on receipt of, or withheld from, any distributions. The target returns are based on models, estimates and assumptions about performance believed to be reasonable under the circumstances. Target returns are not intended to be viewed as indicators of likely performance returns but rather to provide general insight into the fund's objectives, risk profile and strategy. Actual returns may differ materially from target returns. The use of leverage may magnify the opportunities for gain and the risk of loss.

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Adriana de Alcantara joined Hines in January 2020 as senior managing director for HUSPP, Hines' flagship core-plus open-end fund, for which she is responsible for developing and executing the investment strategy. De Alcantara brings more than 20 years of global experience in the real estate industry across all asset classes including, office, multifamily, retail and industrial. Before joining the firm, she served as managing director, senior portfolio manager, at Nuveen Real Estate based in New York, where she was the lead portfolio manager for the TIAA-CREF Real Property Fund LP. Prior to that, she served in a variety of lead roles at TIAA in both London and New York, at Lehman Brothers Global Real Estate Group in Luxembourg and London, and at O'Connor Capital Partners in Luxembourg and London.

COMPANY OVERVIEW

Hines is a leading global real estate investment manager. We own and operate $93.2 billion* of assets across property types and on behalf of a diverse group of institutional and private wealth clients. Every day, our 5,000 employees in 30 countries draw on our 65-year history to build the world forward by investing in, developing and managing some of the world's best real estate. To learn more, visit www.hines.com and follow @Hines on social media.

* Includes both the global Hines organization and RIA AUM as of Dec. 31, 2023

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