IPERE

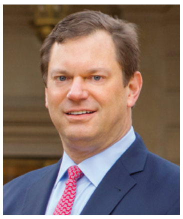
20 YEARS

PEI

FIVE QUESTIONS

SPONSOR **CROW HOLDINGS CAPITAL**

Specialty real estate surges as investors chase demographic-driven demand



BOB MCCLAIN
chief executive officer

Specialty assets like convenience stores, food-and-service retail assets and manufactured home parks are trading hands more often in a shift that reflects a broader transformation in private real estate: alternative sectors once overlooked are now central to institutional demand. Crow Holdings Capital CEO Bob McClain explains how long-term demographic trends, the rise of e-commerce and structural market shifts are converging to reshape the investment landscape across the fast-growing US Sun Belt. The forces defining the next decade in real estate are unfolding today and a disciplined approach can help weather the unknown.

What are the most significant changes you have seen happen in the private real estate industry over the past decade?

Over the past decade, one of the most significant shifts I have observed in private real estate has been the institutionalization of specialty sectors. Our firm has been at the forefront of this transformation, having acquired over 600 convenience and gas sites, more than 130 manufactured housing communities and almost 200 food and service retail assets.

By focusing on macro changes in the market environment – such as major oil companies divesting large portfolios of owned gas stations in the 2010s, the persistent shortage of affordable housing across the US and the structural transformation of retail driven by e-commerce, which has reinforced the resilience of needs-based tenancy – we have capitalized on early opportunities in these specialty sectors.

We also recognized early signs of risk in the office sector, making our last fund investment in office in April 2016, well ahead of the pandemic. Our ability to identify secular trends, observe tenant demand and exit strategically ahead of headwinds reflects the flexibility and foresight that are central to our investment philosophy.

In that context, how has your firm's approach to capital formation evolved over that period?

We have been intentional about broadening our investor base and have strategically expanded our reach among foreign and private wealth investors. The private wealth channel is currently one of the fastest-growing segments of private equity investing, with significant infrastructure being built to support it, and it has been a dedicated focus of our capital formation team over the past few years.

We believe our leadership and track record within specialty sectors of real estate have attracted interest from a wider set of investors who are looking for more unique capabilities from their managers.

Similarly, how has your firm's approach to dealmaking evolved?

Our approach to investing has remained consistent since we started our investment management business in 1998. While the high-growth Sun Belt has drawn investor interest from outsiders in recent years, we have always maintained a focus in these markets – an advantage rooted in our longstanding presence in Dallas since the late 1940s.

We generally target property sectors with strong, predictable tenant demand and minimal tenant acquisition costs and capital expenditures. We execute on smaller investment sizes that offer diversification and the potential for an aggregation premium upon exit. Our financing strategy is disciplined, aligning the duration of debt with the underlying asset profile and typically avoiding cross-collateralization to reduce portfolio risk.

We typically allocate based upon market events that create unique, sector-specific opportunities, and our strategy has long focused on three secular trends: US domestic migration to the Sun Belt, demographic shifts supporting rental housing and e-commerce, and evolving supply chains fueling industrial demand. These trends continue to converge in the Sun Belt markets and traditional sectors, like multifamily and industrial, that the firm has prioritized from the start.

And how has the composition of your team changed?

The primary changes in the composition of our team have been in response to shifts in property sector allocations. For instance, Crow Holdings Capital's allocation to the industrial sector grew significantly with the expansion of e-commerce, and so did the team. Similarly, with office allocations across our fund business at zero, our office team has been scaled down and redeployed to other sectors.

Overall, the specialty sector team has had the most growth, enabling us to aggregate in sectors where the equity checks are typically smaller – primarily in the manufactured housing, self-storage and food-and-service retail sectors. Additionally, our fundraising team has grown to support the broader scope of product offerings and investors.

Crow Holdings began in 1948, when founder Trammell Crow developed this 11,250-square-foot warehouse in Dallas, Texas

“Rather than trying to predict these events, I focus on preparing for the unknown”

What are the biggest risks for the industry today, and which risks should be monitored closely for the future?

The biggest risks we face are the unknowable and unpredictable risks that are certain to emerge in our future. Over the years, Crow Holdings Capital successfully navigated through the dot-com crash, the global financial crisis, the pandemic and, most recently, a rapidly rising interest rate environment.

Rather than trying to predict these events, I focus on preparing for the unknown. We will continue to manage and mitigate risks as we have in the past by maintaining appropriate leverage levels, avoiding cross-collateralization, ensuring adequate fund reserves and investing in sectors with minimal capital and tenant costs, supported by strong, demographic-driven demand.

Our experience has shown that staying disciplined and adhering to these principles has allowed us to successfully weather past unknown events, and that same discipline and approach will have us well-positioned for whatever comes next. ■