



Capital markets: Trends in pension fund investment in real estate – Focus on the Arizona Retirement System

The panel for the REIAC Southwest April 25 capital markets program was quite a collection of experts on the topic: The Chief Investment Officer for a large pension fund. The fund's real estate consultant. A top placement agent that raises funds for a variety of managers. An operating partner that is putting pension fund capital to work.

"The starter kit for this, and the business surrounding all four is Karl Polen, CIO of the Arizona Retirement System," said moderator Joe Blackburn of Everest Holdings. "He's a real estate guy. And I would wager to say that it's quite rare that a real estate guy is the CIO of a major pension fund. I'm sure he approaches the world a bit differently than his peer group."

Joining Polen on the panel were Gadi Kaufmann, Managing Director/CEO, RCLCO; Douglas Weill, Managing Partner, Hodes Weill & Associates; and William C. MacDonald, CEO and President, Mill Creek.



As CIO, Polen oversees the public pension fund investment portfolio for the state of Arizona that currently totals 500,000 members.

"Running the investment program is a very serious responsibility," Polen said. He gave a breakdown of the state's investment portfolio:

- >> Equities, 50 percent;
- >> Real estate, 20 percent;

>> Credit, 20 percent;

>> Interest rate sensitive bonds, 10 percent.

“The goal is to develop a portfolio of real estate investments,” Kaufmann said, “as part of a diversified portfolio. One of the basic truths: most institutions have investments through close-ended funds, and their performance is not all that good. It was an expensive program; for large investors, it is a way to deploy the funds. It would have been a great advantage in early in this cycle to have the ability to dictate where to invest and when to sell.

“Our recommendation was let’s get back to the plan and think about a more flexible investment program and more direct investing,” Kaufmann said. “In those days, 2010, 2011, it was a novel idea. Most institutional lenders did not have the program. They needed a fund manager to be the intermediary.”

Said Weill: “It’s a pretty deep market, about 1,500 institutional lenders. Karl and Arizona are unique.”

Added MacDonald: “The big adjustment for us is communication. But having access to the capital helps us find and compete for real estate sites for an all cash transaction. We had to adjust our thinking that way.”

Kaufmann said the end result is “we work fortuitously on both sides of the transaction; working with Bill and his folks on the strategy.”

Polen wrapped up the discussion by sharing a couple of core ideas.

“Invest directly and take out the middle man whenever you can. Market expertise and relationships are an important skill set. Also, part of the special sauce to accomplish this is how we structure our relationships and the nature of how we delegate decision making authority.”