Wharton UNIVERSITY of PENNSYLVANIA Samuel Zell & Robert Lurie REAL ESTATE CENTER

2014 Fall Members' Meeting Summary

More than 400 members, guests and students attended the Zell/Lurie Real Estate Center's 2014 Fall Members' Meeting at The Inn at Penn on Penn's campus.

Roy Hilton March, CEO of Eastdil Secured and Chairman of the Zell/Lurie Advisory Board, opened the meeting and detailed the afternoon's breakout sessions. **Joe Gyourko**, Director of Zell/Lurie, delivered the State of the Center report, joined by **Asuka Nakahara**, Associate Director of Zell/Lurie; and **Todd Sinai**, Professor of Real Estate and Business Economics and Public Policy at Wharton.

Gyourko reminded the audience about Zell/Lurie's mission, saying, "We want to be a thought leader for the industry… to facilitate a partnership with the industry, faculty and students and to educate future leaders of the industry." Although the Center is not trying to expand, Gyourko said excellence and diversity are always Center goals, along with maintaining a balance in the quality of existing programs and adding new ones — for instance, in California and London — to address the changing face of the industry. "The student body has globalized and jobs are globalizing," Gyourko said, noting "One-third of our real estate students are foreign nationals."

Sinai addressed the Center's new communications strategies. "We will be making information and knowledge that we generate more accessible and mobile-friendly," he said. "We will develop additional content and provide insights into issues that are timely and important. You can expect over the next year or two for us to develop and meet people's preferences and expectations." Participants were encouraged to send in ideas for content and issues that they would like to see analyzed.

The day's first panel, **Investments and Investment Vehicles**, was moderated by **Peter Linneman**, Sussman Professor Emeritus of Real Estate at Wharton, with panelists **Eric Adler**, CEO of Prudential Real Estate Investors; **David Simon**, CEO of Simon Property Group; and **Michael D. Fascitelli**, Founder of MDF Capital.

Linneman began the discussion with: “Forty years ago, real estate business was mainly family-owned enterprises that did their local thing and developed, holding on to what they developed.” He asked: “Where are we today? What is permanent?”

Fascitelli noted that different vehicles at different times serve a purpose. “There is no one right vehicle. You have to look at what happens over time, not just in the moment… There will always be a place for multiple vehicles.”

Adler agreed, yet pointed out that the challenge today, seen more clearly in Europe, is that all strategies are competing for the same deals at the same time. “There is new money coming in… private equity players plus new ones, and a rise of the sovereign wealth funds,” he said. The strategy is to find a good deal and see how much money can be made. He also cautioned about the Asian sovereign wealth funds, saying, “They’re knocking a lot of traditional players out of the zone in Europe.”

The panel briefly discussed open-ended vehicles, describing them as being close to REITs in the private space, and providing some liquidity. Linneman questioned why someone would invest in this, to which Adler responded that it is, again, international money. “There are challenges to investing in the U.S. from a tax perspective,” he said. “Be a minority holder in a REIT vehicle, and that’s one way around it. We have to think about private REITs to accommodate our international investors.”

Linneman then asked about defined benefit programs. “Are they in favor, or out?”

“They are good in the long-term,” said Simon “and beneficial for us generally, although we don’t really know the definition of what a separate account is any more. The capital we have in our little sector is driven by sovereign wealth guys today.”

The panel discussion closed with comments about foreign money flowing into the United States. “Is there enough money out there to matter?” asked Linneman. “Is global instability making us more or less attractive?” “People come here for safety,” asserted Fascitelli. “If you have tons of money, you park it in the U.S. At least it’s safe, but I don’t know if it’s sustainable.”

Linneman asked the panelists what they believe will be the canary in the coal mine. Adler replied that it is debt; Simon said, “It’s supply in my sector.” Fascitelli said it is “excess and greed,” and concluded, “It will be something we have no idea is coming.”

The day's **Farash Distinguished Speaker** was Angela Lee Duckworth, Ph.D., professor in the Department of Psychology at the University of Pennsylvania, who spoke on "True Grit: How to Make Our Children, Firms and Communities More Successful." According to Duckworth, who won a MacArthur "genius" grant in 2013, it is "grit," not just a high IQ, that drives a person beyond merely being good in their field to being truly great, saying, "Tenacity and perseverance; stamina in your area of interest; consistency in your interest and having a focus in it that you maintain for decades. Grit is perseverance over the long term and sustained passion over the long term."

She advised, "Surround yourself with those who understand the situation, but will remind you to not give up," she said. "Don't quit when you're down or on a bad day. Create the mindset you're going to succeed and you can overcome a lot."

Enjoy Dr. Duckworth's TED talk

This meeting featured two breakout sessions.

Asuka Nakahara moderated the session on **CEO Challenges — Running a Real Estate Company**. He distributed two case studies and led a "classroom" session based on the handout to get the participants thinking about what it might be like to be a CEO of a real estate company — strategy, succession planning, capital needs, compensation and firm culture.

The second case examined succession planning: Whose job is it? Who decides if there is enough capital? Does your growth strategy have enough base capital structure to withstand a downturn? How do you build a culture? Nakahara said, "As a leader, you have to demonstrate the kind of company you want to have, even if it's inconvenient. You want your successors to understand all your values of and for the business… Any time anything uncomfortable comes up, it's a teaching moment, and offers you the ability to communicate across the board, and what you do will tell everyone else what is OK."

The **Housing Finance Reform** breakout session was moderated by **Susan M. Wachter**, Albert Sussman Professor and Professor of Real Estate and Finance at Wharton, with panelists **Mitchell Resnick**, Senior Vice President, Capital Markets, Freddie Mac, Washington, D.C.; **Josh Rosner**, co-author of *Reckless Endangerment: How Outsized Ambition, Greed and Corruption Led to Economic Armageddon* and the Managing Director at Graham Fisher & Co.; and **Peter Carroll**, Senior Vice President, Capital Markets, Wells Fargo.

Wachter noted that housing finance reform is still at a stalemate six years after the onset of the financial crisis. The most significant recent legislative effort was the Johnson-Crapo proposal to reform government sponsored entities (GSEs). “There is nearly universal agreement that bringing private capital back to housing finance is necessary,” she said. “But why have government involvement at all? Should we really encourage home ownership? Haven’t we learned that subsidies for home ownership almost brought the economy to its knees? Should we let the market decide?”

Carroll said there has been a marked shift in the last six years. “The tone today is one of broadening credit access to people in the lower-middle income segments,” he said. “How do you do that without getting back to the boom and bust cycle? There needs to be a balance.” The Johnson-Crapo proposal had considerations for both single family and multifamily, but ended abruptly for various reasons, and it will probably be about four years before the conversation gets going seriously again, he added.

Rosner said one of the fundamental problems with the proposal was that it didn’t address why Fannie and Freddie failed. “That proposed regulation doesn’t make sense on various levels,” said Rosner. “We need competition, where participants in the market compete on price based on their efficiencies. Fannie and Freddie were utility markets… will they remain in limbo? We still don’t have a definition of delinquency or default… Does there need to be a government guarantee?” he asked. “Fannie and Freddie have existed a long time and did so without problems until they got off-track leaving utility model to growth model.”

An audience member commented on CMBS—that it started with multifamily and moved to commercial, because it set pricing at a level that investors were willing to risk; if there were no guarantee, pricing would be higher.

Resnick explained that CMBS is a smaller number of loans. “The problem is that people forget that multi and single are different product types. With single, you’re betting on if a person has a job and can maintain income. With multi, it’s a commercial asset with income. That’s completely different,” he said. “The intention — for affordability in the multifamily market so low-income markets have units to rent — is a good one. The credit losses were a result of underwriting. If you look at Fannie and Freddie portfolios, the default numbers there are very low,” he added.

The day’s final panel on **Technology and Real Estate** was moderated by **Joe Gyourko**. Panelists were **William P. Hankowsky**, Chairman, President and CEO, Liberty Property Trust; **Neil H. Shah**, President and COO, Hersha Hospitality Trust; **Elie**

Finegold, Senior Vice President, Global Innovation, CBRE; and **Jeff Brodsky**, President, Related Management.

Gyourko noted the widespread adoption across all age groups for new technological advancements such as Uber and AirBnB. He claimed that, in general, people believe these new approaches will make the economy more efficient.

Shah agreed that in his market — the hotel industry — AirBnB and other such services have had an impact. “It is a substitute for getting a bed somewhere, and we’ve seen a lot of offerings in New York in the last few years,” he said. “But we have also seen new hotel supply during that period. There has been no noticeable financial impact on hotels in New York City; maybe on long-term corporate apartments or extended stay, or for bookings for more than three people, but not on our hotels.”

Brodsky said that from a residential standpoint—from a multifamily viewpoint in the New York City area—there are two sides: regulatory and security. “We have to be consistent with zoning requirements,” he said. “Zoning says you can’t use apartments for short-term occupancy, and we’re responsible as the owner of that asset, not the resident.”

Finegold believes that each of these new technologies is really a series of technologies that are changing things and causing some friction. “It’s here, and we’re on the cusp,” he said. “Imagine that background checks could be made instantly, maybe changing current policy (in multifamily rentals), creating a collaborative economy.”

Hankowsky, who concentrates on B-to-B environments, said, “We believe it’s pervasive and having big impacts on industrial spaces, in different ways. Technology is a net plus on industrial places, creating demand; but more negative on office space.”

Hankowsky described the building he recently finished for Glaxo in the Philadelphia Navy Yard. The space has no dedicated server rooms, because all electronic files are kept in the “cloud,” and hence no need for filing cabinets. “There are no desk phones or assigned seats, cubicles or offices. Employees do everything from their laptops, sometimes at standing desks. There is rooftop green space, and people have real conversations instead of sending email,” he said.

“How widespread is this?” asked Gyourko.

“Everyone is doing something. It varies, but technology is having some impact on everyone,” said Hankowsky. It even can dictate how buildings will be built, according to tech needs.

Finegold agreed, saying the set-up was similar at his worldwide offices. “People want what they can get at home, at work. The workplace becomes a more holistic environment,” he said.

Shah added that disruptive technology (so-called because it changes the status quo) can be a great marketing tool, but it’s important to recognize just what is being disrupted. “In my business, our value proposition isn’t a bed, it’s hospitality,” he said. “You differentiate on location and price and on accessing those customers and disrupting how they may have been accessed in prior years.”

Brodsky added that collaborative spaces appear across all facets. “The breakdown between residential and workspace is clearly the trend,” he said. “The expectation now is seamless connectivity and a sense of community. It’s not defined the same way by everyone, and delivering the right amount and choice is not easy.”

Discussion continued about how location of employees has been driving business choices and how the “millennial” generation and its increasing use of technology is pushing its impact and influence through all parts of real estate.

Roy March closed the meeting by reminding members the Spring Meeting will be Wednesday and Thursday, April 29-30, 2015.

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