

# Real Estate

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Real estate represents a significant component of our portfolio mix and plays an integral role in the diversification benefits of the the 7Twelve strategy. Most investors were reluctant to consider entering this sector of the market in 2009 because of the sub-prime lending debacle. Toxic non-performing loans, generated by the sub-prime lending catastrophe, resided on the balance sheets of most banks causing a near financial meltdown. By contrast, utilizing the 7Twelve strategy, which provides a strong set of well researched and proven guidelines, enabled Tri Pillar investors to weather the storm by fighting the normal urge to flee a sinking ship. Our clients were able to take advantage of opportunities, which otherwise would have been missed, by offering portfolio diversification with low correlations to other asset classes.

Investing in real estate remains a somewhat precarious pursuit. Many pundits point to the dire state of the residential real estate markets, where recovery is regional and market specific. However, commercial real estate may be the next shoe to drop, with estimates of up to \$1.05 Trillion worth of “under-water” assets. In spite of these persistent problems, real estate has proven to be a lucrative investment. Even after a 48.9% global loss in 2008, Real Estate Investment Trusts returned a surprising 41.2% in 2009 and 15.6% in 2010.

It appears that real estate fundamentals finally bottomed in 2010. So, how has the recovery been going since then? Well, despite being oversupplied, the apartment sector has shown the strongest recovery. This is most likely due to a combination of reduced vacancies and a sharp decline in home ownership. The precipitous decline in construction has caused the investment in other property sectors (office, industrial and retail) to suffer as well. According to Colliers International, only 19 million square feet of industrial space was under construction last year, as compared to 107 million in 2008.

Real estate activity in major U.S. cities, such as New York, DC and San Francisco, has been strong. A lot of this activity is due to foreign investors, like the China Investment Corporation and the Chinese sovereign wealth fund. They have been busily scooping up bargain basement priced U.S. real estate. This has clearly buoyed the economies of those particular markets.

The recent buying frenzy, lead primarily by foreign investors, confirms the positive outlook for U.S. real estate. Results of a recent survey by the Association of Foreign Investors in Real Estate, showed that 72% of respondents indicated they planned to increase their investment in the U.S. and more than 60% ranked the U.S., as offering the highest potential for capital appreciation among all major economies. A decline of 44% in peak-to-trough prices brought property values back to the levels not seen since 2002. As of Dec 31, 2009, real estate represented 8% of global capitalization, which creates a significant buying opportunity!

TPI has always been a strong advocate of holding both domestic and international real estate in our portfolios, and we do not expect to change anytime soon.

