

Viewpoints: A New Normal?

I recently returned from the ULI Fall Conference in D.C., the UC Berkeley Fisher Center meeting in Pebble Beach, and a two week vacation in China. I am overly traveled, thoughtful from these different experiences, and back to business. As, generally speaking, the Great Recession continues, what do my recent experiences suggest as the prognosis for the coming months on the human capital side of the real estate business?

My last column was entitled “The Long Bottom”(www.terrasearchpartners.com/news/index). I think we're clearly still there, except for the apartment industry, which is coming back ahead of the curve. It seems to me that we are looking at a New Normal, defined by a period of extended recovery, slouching along the bottom, and little chance of a happy-times bounce back for another several years. I've heard no prognosis of a sustained jobs recovery and we still have the several year impact of the debt maturities overhang as well as the slow rebuilding of the real estate debt markets. A continuing long, slow grind.

Our business can be seen as the proverbial canary-in-the-coal mine and the good news is that, unlike last year, companies are indeed hiring and making moves with their teams. Our search business has recovered somewhat and we've have a high multiple of revenue growth, but a multiple of zero isn't good on an absolute scale and business is still a fraction of several years ago. Like my colleagues in other businesses, we've taken advantage of the downturn by adding key team members, opening new offices, and working hard to gain market share.

We still see no net new hiring in the real estate business, just a thaw in the market in which companies are now again planning for the future, taking some advantage of the available talent pool, and building their bench for succession. But overall, companies are still staying lean and mean.

Much of our recent work has been the result of assets and portfolios trading – one the result of CalPERS switching advisors on a major portfolio and another, the result of an opportunistic investor taking over a major asset. We've also been helping several clients on leadership transitions. As compared to the deep freeze of 2009, this reflects that hiring is taking place, but these do not reflect net new positions – in fact maybe the opposite.

We do a lot of work in the apartment sector, both on the conventional and the affordable side of the business. We are lucky to be sharpshooters on this side of the business, since the sector is bouncing back with demographics and pent up demand as major drivers. We helped one of our clients, traditionally a merchant builder, form an acquisitions group and we also recently helped them grow their development team -- yes, on the multifamily side of the business, companies are breaking ground and hiring development people! In this case, our client reached out into the marketplace and found a strong candidate pool on their own; we helped them pick among a group of finalists.

The mood at ULI and at the Fisher Center meeting was reflective of these overall themes. Apart from the apartment people, other sectors echo these general sentiments – that it will be at least several years to a normalized environment. Cap rates, particularly on A properties, are oddly low, but price per pound is low as well. Rates are historically low, so making a buy is dangerous and counts on the recovery coming sooner rather than later. Everyone is skittish, although the titans at the Fisher Center meeting, Neil Bluhm and Barry Sternlicht, each describe this as “their type of market.” With their capital base, these guys will succeed in raising dough and getting it out. For average size players, however, who will do several versus dozens of deals, it is hard to know when to put the chips on the table.

Transaction volume is slowly gaining momentum. The REITs are strong and on a buying spree. One of our clients, Raintree Partners, a newly established apartment investor, has put together a portfolio of nine properties in the past 18 months. Hudson Pacific Properties successfully IPO'd and has acquired several office properties in Northern California, expanding beyond their Southern California base. My wife's group, W3 Partners, announced its successful capitalization by a venture between Hunt Realty and Teachers Retirement System of Texas; a big feat for an emerging manager. And the private REITs have continued to rake in the dough and make acquisitions. Overall transaction volume has still not hit “market repair” mode, but more business is happening and marks are being made.

“Unsolicited” resumes continue to come into our shop unabated and we've even seen weary job seekers using recruiter-representatives to e-blast their resumes. Neither are a good sign. The only real solution for these folks will be when there are meaningful gains in employment. Patience is still the watchword; job seekers need to continue to find ways to stay relevant through consulting, networking, and refusing to give up that spot under the hoop.

What about my trip to China? Although I read the headlines, it took being there to truly open my eyes to the amount of growth and dynamism in that country. The amount of development, particularly to a real estate person, was actually astonishing. It felt like we were coming from a mature (and currently stagnant) economy and visiting a sprinting adolescent. No surprise reading in the San Francisco Business Times last week about six Bay Area-based architects who are currently doing most of their work in China. The article spoke not just about the amount of their work in China, but also the scale, speed and level of innovation in their projects. They are building world class, cutting edge buildings and infrastructure that would be impossible in our country; we are hobbled by cost as the major driver, lack of ambition, and a political system that drives consistently towards compromise versus excellence. The benefit of a centrally planned economy is that they can see where to go and just get stuff done -- expeditiously.

We kept asking “what does it mean?” The flip side of the exciting, dynamic development scene is a system that is making lots of mistakes, piling up environmental tragedies, and which has a lack of personal freedoms. All are very serious matters. The flip side for us is an abundance of personal freedoms in a political and economic system that is polarized and gridlocked at a time of multiple urgent issues. Also, all serious matters. It would have been nice to come away with black-and-white-isms about their system and circumstances versus ours, but no such luck. The contrasts themselves are lessons as well as a heightened understanding that an America-centric (or California-centric) worldview is dead-end.

So, back to work. Our firm is not about to enter the China market for real estate recruiting, which might be the obvious response, but I do come back with additional perspective on the New Normal of our still stagnant economy. I suspect a secular change will come from our sharing of world economic leadership and the significant constraints of together addressing our global environmental challenges. Our real estate economy will recover slowly, new fortunes will be made, and most of our friends in the business will be back to work and enjoy successful careers in the business. But it will be at a different level, in a more globalized economy, and with more difficult, complex challenges in the business than in the 80's, 90's and 00's heydays.

Matt Slepín and the Team at Terra Search Partners