

CRE Students Benefit from Unique Opportunity to Learn from Leaders

When Michael Falcone told students and faculty at the MIT Center for Real Estate (MIT/CRE) that “interest rates in the United States are lower than they should be,” it was both an observation and a warning. Falcone, chief executive officer of MuniMae (Municipal Mortgage & Equity, LLC), sounded this note of caution during his presentation as part of the Center’s *Learning from Leaders* program on December 2. The program, featuring senior executives from leading real estate and investment companies, was the first in a planned series of visits by the Center’s sustaining partners.

The lower interest rates are a consequence, Falcone said, of increasingly prosperous Asian countries gobbling U.S. debt in order to maintain favorable trade arrangements, and he predicted there will be no increases in cap rates for at least a couple of years. That, of course, is good for the real estate, but Falcone tempered the good news with a caveat. “Cap rates will stay low,” he predicted, “as long as there’s not a geopolitical event.”

“Capital is driving a lot of product generation these days,” added Frank Creamer, executive vice president of MMA Financial, who participated with Falcone in a panel discussion on innovations in housing and housing finance, moderated by Professor Lynn Fisher. “Real estate is now getting more involved in new technologies and much of the paper being issued is being bought from outside the United States.” And, said Creamer, companies like MMA are now increasingly engaged in solving problems faced by developers. “We have to do more innovative transactions,” he added.

Falcone and Creamer were among representatives of four large companies who took part in the inaugural sustaining partners visit. Other guests included MIT alumnus Jacques Gordon Ph.D., global investment strategist for LaSalle Investment Management; Andre Collin, First Vice President of Canada’s Public Sector Pension Investment Board (PSP); and Richard Dansereau, president and chief operating officer of Caisse de Dépôt Capital Real Estate Advisory.

Observing that mortgage investment has grown dramatically – from \$14 billion in 1990 to approximately \$120 billion in 2001 and 2002 – Creamer noted how dramatically the composition of the debt market has changed during that same time period. While pension funds hold the lion’s share of debt today, they were just barely a player – amounting to a tiny 6.5 percent – in 1993, when commercial banks led the pack.

Observing that it is an exciting time, Creamer said, “Commercial mortgage-backed securities are getting larger and there is a great desire to have representation by

multi-families in these securities.” A brisk flow of capital – from all over the world – is responsible for a lot of product generation, but the risk, said Falcone, “is that the supply of capital will create assets that exceed demand.”

Addressing recent trends they were monitoring, Falcone and Creamer said they were paying particular attention to the growth of the shared equity market abroad, especially in the United Kingdom, in which non-profits – typically quasi-government agencies – help home owners buy property. While this model has yet to catch on widely in the United States, where legal and tax complications have prevented it from taking root, Falcone noted that many of today’s mortgage market components are dramatically different from those that prevailed during the 1990s.

He noted, as well, the trend toward condominium conversion, which has saturated some markets, notably San Diego and Miami. Even in those markets, he predicted, converted condos will eventually return and compete with multi-family development, which is currently in ascension.

Managing Risk During the Capital Flood

Gordon, who spoke after Falcone and Creamer’s presentation, addressed global strategies in real estate, a topic of increasing interest at the CRE, and noted that his company, LaSalle Investment Management, is stressing risk management. “Given the rush of capital into the market, is real estate still attractively priced relative to the attendant risks?” he asked, providing a segue from Falcone and Creamer’s presentation. “What are the longer-run ‘secular’ shifts to build into a portfolio? And what are the shorter-run cyclical movements to watch out for?”

Among the important prevailing themes Gordon highlighted were in-migration of vehicles from wider capital markets, such as general-limited partnerships from private equity; hedge funds and high leverage; and derivatives; infrastructure overlap with real estate, such as owner-occupied assets transfer to the investment market; and cross-border real estate portfolios.

Addressing the growth of global real estate investment trusts (REITs), currently a \$400 billion market, France and Japan, the dominant players, will soon be joined by the United Kingdom, Germany and Mexico, Gordon said.

What are the leading investment opportunities? Gordon said airports and facilities for air cargo handling, deep water ports and intermodal facilities, power and energy facilities and even toll roads and bridges, which could be privatized, all offer potential. The key is to be able to predict the attendant risk.

Through 2008, he predicted, global expansion will continue, characterized by a diversity of global office yields. “There will be ongoing opportunities to find better relative value versus a domestic-only approach,” he said, “but the challenge is to understand the different risk profiles that go with those yields.”

Andre Collin and Richard Dansereau wrapped up the day of activities with a dialogue on leadership, which was attended by a large number of students.