CBRE Investment Management

The real estate secondaries market

A Q&A with CBRE IM's Real Estate Partners strategy team leaders

Kilian Toms *is fund manager and managing director of CBRE Investment Management's Real Estate Partners strategy. Based in London, Toms is responsible for all aspects of the strategy, which focuses on enhanced-return secondary-market executions. Toms is supported by an experienced global secondary portfolio management team that includes* ***Chris Dickson,*** *deputy fund manager of the Real Estate Partners strategy, who is based in Boston and has been with CBRE IM Indirect for 10 years. The following is a question-and-answer session with them both.*

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– Chris Dickson

There are a lot of definitions out there of the term "secondary" in private real estate, so to start, can you help define the secondary market from CBRE IM's perspective?

Kilian Toms: At CBRE IM, we have defined a secondary as any transaction where equity is exchanged in the capital stack, but the operator or sponsor stays in place and maintains control over the real estate. Secondaries can occur within multiple deal types – for example, at an asset level or within a programmatic venture, portfolio or fund. This definition is purposefully broad and reflects the evolution of the secondary market, which has broadened in scope during the past decade. Historically, the secondary market focused on buying limited partnership interests in funds. Following the trend in private equity, the real estate secondary space has evolved to also include general partner–led secondaries or recapitalizations, which now make up the bulk of annual transaction volume.

What is driving the growth of the secondaries market?

Chris Dickson: The secondaries market is experiencing continued remarkable growth and becoming a prominent segment of the private real estate investment landscape. This growth is driven by a broadening definition of what can be classified as a secondary and, more importantly, the acceptance that executing a secondary is a vital tool for both operators and investors of real estate alike. It has become clear that having a healthy secondary market is a benefit to all market participants.

The bottom line is that private real estate is still highly inefficient. The structures commonly used to own real estate, whether through closed-end funds, open-end funds or joint ventures, all place unique limitations on an operator's or investor's ability to effectively manage their portfolio. When the market turns, as we have seen during the past 18 months, pressure begins to build because of these limitations. The secondary market is the "release valve".

We understand the secondaries market is growing. How large do you think it is?

Toms: That is a great question, and frankly, a difficult one to answer. Our team has spent quite a bit of time searching for a data set we felt captured the depth of the market, and it has become clear that one does not currently exist. What we can do is look at our internal deal log, transactions that are announced in the press and others we hear about through our operator relationships, globally.

The conclusion we have come to is that the market is multiples larger than figures that are commonly referred to, and we estimate transaction volume to be between $50 billion and $100 billion annually. It is important to note this fairly wide range captures an evolving transaction opportunity set, across the risk spectrum, from core through opportunistic – this opportunity set is way too big to ignore.

Our research team has recently launched an initiative to put together a more accurate data set, which we hope to be able to share soon.

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– Kilian Toms

How has CBRE IM's participation in the secondary market evolved over time?

Dickson: Our group has been active in the secondary market on both the buy and sell sides since just following the global financial crisis. On behalf of our clients, we seek to explore a broad range of investment and divestment opportunities.

There are many times in a cycle when secondaries may offer great relative value at entry or provide the best path to liquidity. As the market matures, it is increasingly clear secondaries are not a peripheral alternative investment avenue, but rather a vital component to optimize liquidity, as well as manage preferred allocations and investment strategies.

Why now?

Toms: While the secondaries market is large and growing, the capital dedicated to this strategy is still limited. Secondaries are experiencing another leap in utilization, as operators are now seeking to recapitalize their best assets, instead of selling them directly on the primary market.

At the same time, we think the heightened illiquidity in the current environment makes this an incredibly attractive secondaries execution vintage. As investors at all points in the capital stack grapple with the impacts of higher interest rates and an uncertain macro-outlook, asset values have begun repricing. This has led to a broader impact on their portfolios, which has created a pool of motivated sellers.

Valuations are approaching a trough point in the near term, which feels like a great time to be deploying capital into private real estate. We see opportunities to arbitrage these shifting valuations and invest into our preferred sectors, often at a discount to our view of intrinsic value. With this approach, we are finding opportunities that drive outsized risk-adjusted returns.

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About CBRE IM Indirect

CBRE Investment Management is a leading global real assets investment management firm with $147.6 billion in assets under management as of June 30, 2023, operating in more than 30 offices and 20 countries around the world.

CBRE IM's Indirect Strategies provide customized global real estate investment solutions through investment in programmatic ventures, co-investments, secondaries and funds operated by specialist partners. Our market-leading platform has a 15-year track record of executing approximately $12.0 billion of secondaries transactions across risk profiles.

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