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Cohen & Steers built its name on public real estate. Its CEO says the future is proving private markets need public ones, too.

By JAMES VAN BRAMER

Cohen & Steers built its reputation investing in publicly traded real estate. Now, four decades after the firm's founding, CEO Joe Harvey sees some of its biggest opportunities in bringing that expertise to the private market.

Harvey, who joined Cohen & Steers as its sixth employee when the firm managed roughly $250 million, believes real estate is entering a new investment cycle, supported by improving property fundamentals and a slowdown in construction. But he sees a market where opportunities vary considerably by sector, with grocery-anchored shopping centers and select office properties presenting attractive investments while financing pressures threaten to create further challenges for apartments.

Underlying those investment calls is a conviction that listed and private real estate are most effective when used together, he says. As Cohen & Steers expands its private real estate business, Harvey argues that institutional investors have become too reliant on illiquid investments and too willing to assume that private markets deliver superior returns.

In this face-to-face interview with Pensions & Investments, Harvey and Seth Laughlin, senior vice president and head of real estate strategy and research, discussed the firm's evolution, the real estate recovery, opportunities across property sectors and how institutional investors should approach listed and private allocations.



Seth Laughlin, left, senior vice president and head of real estate strategy and research, and Joe Harvey, CEO, of Cohen & Steers. (Buck Ennis)

Answers have been edited for conciseness and clarity.

Q: Joe, you joined Cohen & Steers as its sixth employee. What drew you to investing and to the firm?

Harvey: I worked briefly as an engineer, then went to Robert Stanger & Co. as an analyst covering real estate and other industries. We worked on a closed-end fund, and I knew I wanted to get into asset management.

This was in the middle of a terrible recession in the late '80s and early '90s, and nobody was hiring somebody without a business school degree or a CFA. But I had real estate knowledge. Marty Cohen and Bob Steers anticipated an IPO boom and hired two analysts. I was one of them.

From 1992 to roughly 1998, it was an extraordinary learning experience. We were evaluating new companies, sectors and markets sometimes several times a week. It was a very rich investment experience that also became a rich business experience.

Q: How did Cohen & Steers grow beyond its original U.S. listed real estate strategy?

Harvey: As our REITs business grew, we launched a preferred securities strategy in 2004 and a utility strategy that developed into our infrastructure business.

Around that time, REIT structures were spreading internationally and clients wanted global strategies. We ac-

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quired a European-based manager with global capabilities rather than building everything from scratch. We opened investment offices in London and Hong Kong and built client relationships in other markets. Today the real estate and infrastructure businesses are global, and preferred securities also have an international element.

What's exciting is that we're still seeing markets, particularly in Asia, where institutions are only beginning to make meaningful real assets allocations.

Q: Fast forward to today, many describe the asset class as struggling to recover post-pandemic. How would you describe the current real estate market?

Laughlin: We're in the early part of the cycle, but real estate is the landlord of the economy, and every property type has a different story. After the pandemic, demand moved toward apartments and industrial properties, and supply followed. Then rates rose sharply in 2022, just as that new supply was arriving.

Now construction is slowing across much of the market, while some sectors, including shopping centers and office, have very little new supply. Data centers have extraordinary demand. Listed REITs have performed positively even with inflation elevated and Treasury yields rising. That's a different backdrop from 2022.

Q: We did get a recent rate hike from the Fed, and some would point to higher-for-longer prospects. Can the recovery hold if interest rates remain elevated?

Harvey: Inflation has made replacement cost more important. Construction costs keep rising, and that makes the economics of new development less attractive. If demand continues to grow while supply is constrained, that eventually puts upward pressure on rents.

I look at an index of replacement costs and compare it with REIT share prices. In the years after the global financial crisis, REITs generally traded above that measure, which I think reflected extraordinarily low interest rates. Now share prices are roughly 20% below it. That's a broad comparison, but with improving fundamentals it gives me confidence there is a new return cycle ahead.

Laughlin: Higher rates still matter. The listed market has already adjusted valuations and financing assumptions. Another 100 basis points on the 10-year Treasury would hurt assets dependent on borrowing, but 25 or 50 basis points isn't necessarily a death knell for REITs. You have to assess the exposure sector by sector.

Q: Where could higher financing costs produce opportunities?

Harvey: Apartments concern us. A lot of capital went into them over the past five to seven years, and private valuations have stayed high even as rent and cash flow growth flattened. If you're refinancing at borrowing costs around 6.5% on an asset valued at a capitalization rate in the mid-4% to 5% range, the math becomes difficult. Owners may have to contribute more equity or sell. That could create attractive acquisition opportunities.

Industrial is different. We've been frustrated by private-market pricing there, too, but its growth has held up better. Some owners may be able to grow into their valuations without the same disruption.

Q: You've spoken before about your enthusiasm for grocery-anchored and other open-air shopping centers. Why have they been such a focus of the firm?

Harvey: It's more of a secular opportunity than an early-cycle trade. E-commerce hurt retail, investors turned away and developers largely stopped building shopping centers. Meanwhile, retailers learned that stores and online operations can work together.

The centers we've bought have generally been priced around two-thirds of replacement cost. They're about 97% occupied, and retailers are looking for available space. That gives landlords pricing power, while the cost of building competing properties remains prohibitive. We like the cash yields and the growth prospects. It's difficult to find that combination elsewhere.

Q: How does that retail conviction fit into your expansion into private real estate?

Harvey: We began building a private real estate capability about five or six years ago, hiring people with experience in that market. We've had a traditional drawdown fund, and we have a nontraded evergreen REIT for high-net-worth investors and smaller institutions. So far, that vehicle has invested exclusively in shopping centers, although it is intended to become more diversified.

We also have closed-end vehicles dominated by listed real estate that can allocate up to 10% to private properties. The idea is to draw on our knowledge of public companies and sectors to identify opportunities in the private market. There are things we can do today that we couldn't express through a private investment five years ago.

Q: What about other sectors, like office, data centers and senior housing?

Harvey: In data centers, we prefer listed exposure. It's a major AI-related opportunity, but it requires specialized expertise, and the listed market allows us to change our position if valuations get too frothy. We also participate in the power demand theme through listed infrastructure, including utilities and generators.

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We're bullish on health care, particularly senior housing, because of demographics. But operating risks and margins make us less inclined to own those properties privately.

Office is more interesting than the broad narrative suggests. In parts of New York, Dallas and San Francisco, demand is improving and little new construction makes sense economically. We've moved overweight in listed office after being underweight for years, and we may make selective private investments. But office is very specific to the building, location and tenants. You have to think about the exit from the day you buy.

Q: What do institutions get wrong about the balance between listed and private investments?

Harvey: I think it's best to own both. They tend to be out of phase in returns, and they offer different exposures. Yet institutional real assets portfolios have been dominated by private investments.

Investors talk about a return premium in private markets as though it's guaranteed. It isn't. In areas like core real estate, investors haven't necessarily earned a premium for going private. They need to put a better price on illiquidity. What's the cost of being unable to pivot into AI-related opportunities because so much of your portfolio is locked up?

That becomes even more important for institutions adopting a total portfolio approach. To shift exposures across the portfolio effectively, you're going to need more liquidity.

Q: As Cohen & Steers enters its fifth decade, what opportunities excite you most?

Harvey: Asset management is changing faster than I've ever seen. Active ETFs offer new ways to deliver strategies. Private assets are coming to the wealth market, although I think some of the industry's allocation forecasts are too ambitious.

What interests me is combining listed and private more intelligently. In our evergreen REIT, we use listed investments in the liquidity sleeve as a potential source of alpha rather than simply holding Treasuries. We also have an institutional core real estate strategy with a base allocation of roughly 65% private and 35% listed, designed to improve liquidity without fundamentally changing the volatility profile.

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