

36th Annual Cornell Real Estate Conference Recap

INTRODUCTION

On October 19, 2018, the Cornell Real Estate Council (CREC) hosted the 36th annual Cornell Real Estate Conference in New York City. The conference brought together hundreds of industry professionals, alumni and current students for a day of networking and panel discussions surrounding recent trends. Cornell's unparalleled alumni network within the real estate community facilitated a broad exchange of innovative ideas applicable across the industry, from design and construction to development and finance. Highlighting a "Focus on the Future," five panel discussions, including keynote Speaker Seth Klarman (CAS '79) and 2018 Industry Leader Award Recipient Kenneth Himmel (JCB-Hotel '70), shed light on some of the most pressing questions currently facing the real estate industry.

THE FUTURE OF RETAIL SPACE: HAS THE DEATH OF RETAIL BEEN GREATLY EXAGGERATED?

Moderator: Alan Riffkin (JCB-Hotel '88), Managing Director, Lazard

Panelists: Ken Bernstein, President and CEO, Acadia Realty; Terry Brown, Managing Partner, Asana Partners; Philip Krim, CEO, Casper; Liza Landsman (CAS '90), Partner, New Enterprise Associates (former President of Jet.com)

The retail sector has faced significant challenges over the past few years. The rise of e-commerce and changing consumer preferences have forced retailers, owners, and investors to adapt in a rapidly evolving marketplace. Some

of the most prominent national retailers have failed to adjust to this dynamic retail landscape. Toys R Us, Sears, and RadioShack are among the many legacy retailers who have announced store closures or bankruptcy filings. Panelists discussed if the often discussed "Retail Apocalypse" has been greatly exaggerated?

Despite challenges in the industry, many retailers, owners and investors possess an encouraging outlook on the sector. At this year's Cornell Real Estate Conference, industry leaders shared promising sentiments regarding the future of retail. The collapse of legacy retailers has dominated market headlines and created false and sometimes misguided perceptions of the retail marketplace. E-commerce has emerged as a large disruptor of the retail sector concerning the real estate industry leading to the question of whether shopping will exclusively transition to online. Amid the recent store closures and bankruptcies, however, many physical retailers and landlords have been able to achieve success and thrive in the market.

Physical retailers have adopted new and innovative strategies based on consumer preferences to attract customers and improve the experience component of stores. The panelists believe there is a profound focus on connecting with the consumers and creating authentic experiences. Today, the most successful retailers are smarter and better capitalized while real estate investors are investing in prominent and historic locations to draw the most active and influential retailers. Digitally native brands,



Figure 1. The 36th Annual Cornell Real Estate Conference begins. Participants from left to right: Alan Riffkin, Liza Landsman, Terry Brown, Ken Bernstein, and Philip Krim.



Figure 2. Terry Brown, Ken Bernstein, and Philip Krim discuss retail innovation.

such as Warby Parker, Bonobos, and Outdoor Voices, have also recognized the value of brick and mortar stores.

Casper, an e-commerce company that sells sleep products, exemplifies how online retailers are embracing this trend. The company has committed to opening 200 stores over the next few years. Initially launched online in order to circumvent the highly insulated mattress industry, Casper was founded on the belief that the internet was the best channel to connect with the consumer. After establishing a strong and loyal customer base, Casper has found significant value in physical retail locations and believes opening retail stores is a logical next step in its growth and trajectory.

The year 2017 was uncertain for the retail sector as questions abounded challenging the existence of the retail market landscape. Retailers and owners have embraced these challenges resulting in newly successful approaches. Based on conversations of the panel and others at the Cornell Real Estate Conference, there are many encouraging signs for the trajectory of retail.



Figure 3. Participants from left to right: Alan Tantleff, Adam Flatto, Chris Kelly, and Peter Smith.



Figure 4. Roe Adams responds to a question from the audience.

HOW WE LIVE, WORK AND PLAY...IN 2028

Moderator: Alan Tantleff (JCB-Hotel '87), Senior Managing Director, FTI Consulting

Panelists: Roe Adams, Chief Product Officer, WeWork; Adam Flatto, President and CEO, the Georgetown Company; Chris Kelly, Co-founder and CIO, Convene; Peter Smith, Director of Global Real Estate, Bloomberg

Real estate professionals take a sober interest in future trends because their products are inherently durable and long-lasting. Decisions made in the design and development phase, indeed all phases, will be passed on to future tenants and owners. A priority of developers is to market products that appeal to the changing demographics of the workforce. With the uncertainty of near-term transportation and retail behavior, flexibility in the uses of space has increasingly become an important consideration.

The diversity of the panelists was a tribute to the wide-ranging implications of future uncertainty in real estate, but it was dominated by a refrain of “out with the old, in with the new”. Bloomberg’s Peter Smith noted that the world of corporate real estate is complacent with aging leadership and time-tested habits, but he also conceded that large corporations like Bloomberg cannot hope to understand the changing nature of office space without making allowances for the input of young professionals who will ultimately use the space. Leaders in corporate real estate must be stewards of their company’s assets, and by extension, their company’s culture. Smith acknowledged that the best talent is coming from universities. To acquire that talent, corporate real estate professionals must cultivate an environment that offers competitive amenities and social benefits.

This environment is where WeWork’s Roe Adams, a native of Israel with a self-described “inherent disrespect for authority,” excels. WeWork’s business is modelled around the behavior of the next generation of office workers demanding a higher quality of life and greater access to amenities within the workspace. While traditional offices are characterized by maximally productive spaces, Adams explains, “we try to create spaces with greater purposes.” An office designed thoughtfully with consideration of the well-being of its users can promote emergent ideas serendipitously. The commingling of people in an office is in stark juxtaposition with the stuffy cubicles of yesteryear. As Adams explains, “people thrive when they are around other people.”

Adam Flatto of the Georgetown Company agreed with that sentiment. He described a hospitality trend in which hotel operators are hoping to get business travelers out of the solitude of their suites and into the common areas of the hotel. Consequently, designers of new hotels catering to business travelers are designing smaller guest rooms with shared amenities. Typical guestrooms are around 330 square feet, but Marriott's Moxy line of hotels features rooms half this size that are more technologically advanced and appealing to the recreational needs younger travelers.

Chris Kelly of Convene elaborated on the expectations of the younger demographic entering office spaces, suggesting they may, as "digital natives," not know anything different. Millennials and Generation Z office workers have been using smartphones and personal computers for the majority of their lives and often depend on integrated technology to drive their productivity. As Kelly notes, however, the fact remains that anyone can integrate with the changing behavior of office work. The global nature of business has created a class of office employees that work remotely or travel often, such as those in business development or sales. Adler emphasized these "digital nomads" as a major factor in WeWork's success. Companies with significant office assets discovered that WeWork presents an opportunity to greatly economize how office space sits on these companies' balance sheets. Prior to the advent of coworking spaces, office space was grossly underutilized.

The changing nature of how we live, work, and play factors significantly into corporate decision-making as companies seek to redefine their culture—or perhaps their retail models. On the public side, however, cities ought to be continually adapting to these trends with planning and incentives. The most iconic American brands are uprooting from the suburbs and moving to cities in order to attract the best talent. Cities would be wise to become flexible to changing behavior if they hope to remain relevant.

VENTURE CAPITAL AND TECHNOLOGY

Moderator: Clelia Peters, President of Walburg Realty, MetaProp

Panelists: Meghan Cross Breeden HumEc '08, Partner, Amplifyer Ventures; Marshall Cox, Founder and CEO, Radiator Labs; Raffi Holzer, CEO, Avvir; Edward Liew (MPS '09), Senior Director, DivcoWest

The panel started off by highlighting proptech, a term that is often misunderstood. As noted by the panel, proptech includes the use of technology in any aspect of

the construction, operation and maintenance of the built environment. One panelist used the term "from dirt to disposition" to explain what is encompassed by the term.

The panel highlighted that technological advancements in the building industry provide immense opportunities for investment. Components that make certain technologies possible, such as sensors and lasers, are cheaper today and readily available. Data exchange platforms also have fewer limitations, allowing for greater ease in data collection and transfer. This has great implications for the construction industry, traditionally one of the least innovative industries in the U.S.

The panel noted that because the traditional workforce is beginning to retire, more space is being created for new generations of construction workers adept at using technology. The industry is also seeing disruption from entrepreneurial-minded individuals entering from the outside of the industry with innovative ways of solving problems. The panel cited the case of Urban Umbrella, which has become an alternative to the traditional scaffolding widely used throughout the construction industry since the 1950s. The technology was created in a design competition sponsored by former NYC Mayor Michael Bloomberg to reimagine the traditional and unsightly sidewalk shed often seen throughout large cities. After winning the design competition in 2010, the company created a prototype which led to it receiving millions of dollars in venture capital funding.

The panel discussed the various challenges of adapting technology. Regulations in many cities affect the usage and implementation of these types of new technologies. For example, the use of drones, which has great potential to affect the built environment, is often restricted in heavily-populated urban areas. Another challenge of new technologies is the need to prove efficiency before scaling. In the case of Radiator Labs, founder Marshall Cox



Figure 5. Participants from left to right: Clelia Paters, Raffi Holzer, Meghan Cross Breeden, Edward Liew, and Marshall Cox.

noted that it was initially a challenge for him to approach commercial real estate companies. Despite this, he was able to foster strategic relationships with local universities. Substantial reductions in the heating costs for older dorms allowed him to approach established commercial real estate companies with proven results.

Globally, the proptech industry is expected to reach \$20 billion by 2020. Many investment and venture capital firms are seeing the potential for technology in all industries related to the built environment. The panelists noted several elements that can aid in the expansion of the proptech industry. The ability of startups to collaborate with established commercial real estate firms on finding creative ways to solve specific industry problems is essential. Overall, the panel provided unique insights into the unlimited potential of technology.

KEYNOTE SPEAKER – ONE ON ONE DISCUSSION WITH SETH KLARMAN (CAS '79)

Moderator: David Hodes, Managing Partner, Hodes Weill & Associates

The Cornell Real Estate Council was pleased to welcome alumnus Seth Klarman (CAS '79) to the 36th annual Cornell Real Estate Conference as the keynote speaker. Mr. Klarman is the CEO of The Baupost Group, a privately

held investment management company with approximately \$30 billion in assets. Mr. Klarman has been at the helm of Baupost since its founding in 1982, and is widely recognized as one of the most successful practitioners of value investing. Not known for speaking publicly and participating in numerous interviews, Mr. Klarman sat down for a one-on-one discussion with David Hodes, Managing Partner of Hodes Weill & Associates.

Mr. Klarman began by discussing how he was first drawn to value investing. Throughout his studies it was apparent that the idea of an efficient market was largely incorrect. Opportunities exist within markets to take advantage of pricing discrepancies brought about by events that clouded the true value of many enterprises. This often leads one to unpopular or overlooked opportunities granting “margin of safety,” a term coined by the “father of value investing” Benjamin Graham, that allow for assets or firms to be purchased at a discount to intrinsic value. In other words, as Mr. Klarman put it, “why wouldn’t I buy a dollar for fifty or sixty cents?” While these types of investments typically unfold in distressed or ignored areas of a market, value investors in the mold of Mr. Klarman see low risk opportunities. From a real estate perspective, value investing, among many aspects, is aligned with the idea of buying an asset for less than the replacement cost.



Figure 6. Seth Klarman, left, and David Hodes, right, discuss value investing.

After these points, Mr. Hodes invited Mr. Klarman to discuss the current market. They discussed lessons learned from 2008 and the correction of today's market. Mr. Klarman noted that, while you can worry from the top-down, you must always invest from the bottom up. The fundamentals of a deal should not change relative to the overall market. If an opportunity makes sense on an individual basis, the investment is merited. He noted that despite the current market being overextended on a cyclically adjusted basis, this is not the case nominally. Interest rates are still low, a result of policies that were successful in stemming the fallout from 2008-2009. As we move forward in what has seemed like a "benign decade" characterized by low defaults, narrowing credit spreads, and potential inflation, Mr. Klarman pointed to the writings of economist Hyman Minsky, specifically to his point that sustained periods of stability eventually lead to periods of high volatility. Recently, this has transpired internationally, and while that volatility has largely shied away from U.S. markets, a tipping point will come. According to Mr. Klarman, there are more dubious offerings today than ever. As large VC funds continue to grow ever larger, e.g. Softbank, things could change for the worse.

As Mr. Hodes steered the conversation more towards Baupost's real estate investments, Mr. Klarman continued to reference potential downturns, stressing that while bottoms are hard to find, the important thing is to buy on the way down. Baupost's flexible mandate allows it to move money to the best opportunities regardless of asset class—and sometimes that means holding significant amounts of cash. When it comes to real estate, Baupost first entered the market in the wake of the S&L crisis. It realized that opportunity existed from the pools of loans being sold off by the Resolution Trust Corporation. This has led to Baupost's continued involvement in real estate over the last twenty-five years. When pushed by Mr. Hodes to answer whether real estate is still a value proposition in today's market, in true value investor style, Mr. Klarman responded that the externalities of individual opportunities always exist, despite market conditions.

Asked if there was any advice he may have for students in the audience interested in a career in finance, Mr. Klarman stated the investment business, invigorating and meritocratic, is bigger and more competitive now than ever and requires a 24/7 dedication. The investing profession, he said, is wrongly portrayed and encouraged its pursuit. When Baupost seeks talent, it looks for team players, stating

"nobody's name is on the door". Outside the box, ideational thinking should accompany strong ethical foundations. Being "intellectually honest" is essential.

In closing, Mr. Hodes asked how value investing might change in the future. Upon reflection, Mr. Klarman stated that the core idea of value investing, a "basic value concept," is the idea of mean reversion. This idea is less applicable today, however, due to market disruptions from technology. Technology has the potential to change markets faster than humans may be capable of adapting. This will create problems in the future, but also potential opportunities. As a value investor, it is better to have a few well-founded opinions, not opinions on everything.

KENNETH HIMMEL (JCB-HOTEL '70) – RECIPIENT OF CORNELL REAL ESTATE REVIEW'S 2018 INDUSTRY LEADER AWARD

Moderator: Richard Baker (JCB-Hotel '88), Governor and Executive Chairman, HBC

Each year at the Cornell University Real Estate Conference in New York City, the editors of the *Cornell Real Estate Review* honor a leader who has made a demonstrable impact on the real estate industry at a global scale, as well as a service-minded contribution to society. The 2018 recipient of the Industry Leader Award was Kenneth Himmel (SHA '70), the President and Chief Executive Officer of Related Urban, a developer of large-scale mixed-use properties, as well as the Managing Partner of Gulf Related, an Abu Dhabi based joint venture between Related Companies and Gulf Capital.

During his distinguished career, Mr. Himmel has led significant real estate developments throughout the world, including Hudson Yards and Time Warner Center in New York, New York; CityPlace in West Palm Beach, Florida; Related Santa Clara in Santa Clara, California; Water Tower Place in Chicago, Illinois; and The Galleria and Central in Abu Dhabi, UAE. These projects have become destinations in their own right and have enhanced the communities in which they are located.

After accepting the award, Mr. Himmel engaged in a lively discussion with Richard Baker (SHA '88), the Governor and Executive Chairman of Hudson's Bay Company as well as the namesake benefactor of Cornell's Baker Program in Real Estate. This discussion touched on numerous subjects, including Mr. Himmel's start in the real estate industry, his experience developing the Time Warner Center, and the characteristics of successful real estate

developers. Mr. Himmel first reflected on his education and early career in the real estate industry. He explained how he developed a deep interest in hospitality that led him to Cornell's Hotel School. Mr. Himmel subsequently worked for a Boston-area developer on hotel projects in the Boston and New York markets before moving to Cabot, Cabot & Forbes, a prominent real estate development firm, where he received his first significant assignment working on the Ritz-Carlton Hotel at Water Tower Place. Mr. Himmel recounted how he sought this assignment and encouraged young professionals in the real estate industry to take the initiative to forge their own career paths.

At Mr. Baker's urging, Mr. Himmel discussed the complex development process for the Time Warner Center, a 2.8 million square foot mixed-use project. The Time Warner Center is emblematic of the developments Related undertakes: projects in markets with high barriers to entry that limit competition and raise standards. While now considered one of the preeminent developments in Manhattan, the company faced a number of challenges during the development process, including a short period that required around-the-clock work in order to finalize its proposal, the need to secure a lead tenant as part of this proposal, and the September 11th attacks occurring during construction of the project. This project, Mr. Himmel mused, was indicative of the fact that for each "up" a developer experiences during a project there will be four or five "downs."

Mr. Himmel next reflected on the characteristics of successful developers. Developers must be smart and obsessive about details. Further, developers must build meaningful relationships with other stakeholders, including tenants and municipalities. With respect to tenants, Mr. Himmel emphasized the importance of developers understanding tenants and their businesses while, with respect to municipalities, Related seeks "win-win" outcomes

and avoids litigation as a tool to achieve its objectives. Additionally, developers must possess good judgment when confronting risks in the real estate development industry. To mitigate these risks, Mr. Himmel recommended that developers do all of the necessary homework on deals and stay up-to-date on industry trends. Finally, developers should possess superior taste—which cannot always be taught—and be well-traveled. Mr. Himmel relayed to the audience how many family vacations throughout his life involved visiting buildings and other areas with his family in tow in order to derive inspiration for current or future projects.

Mr. Himmel is truly a worthy recipient of the Industry Leader Award. His industry accomplishments are legion and his dedication to Cornell includes serving on the Hotel School's Advisory Board and as a mentor to Cornell real estate students. The Cornell real estate community thanks Mr. Himmel for his many contributions to the real estate industry and university, and we wish him and Related continued success in the future.

DESIGN MORE IMPORTANT THAN EVER

Moderator: Robert Balder (AAP '89), Director of AAP NY, Cornell University

Panelists: Kate Bicknell (AAP '99), Vice President, Oxford Properties; Gary Handel (AAP '77), Founder and Managing Partner, Handel Architects; Jerry Zeitner, Chief Operating Officer, The Gettys Group

With advances in technology disrupting every sector, intelligent design is a driving factor in attracting and retaining tenants and building user traffic. The fourth conference panel explored the importance of design in moving the industry forward, whether it be the residential sector evolving to attract millennials, offices shifting to house co-working spaces, or warehouses incorporating new technology to adapt to the needs of e-commerce.



Figure 7. From left to right: Jennifer Spritzer (Baker/MBA '19), Richard Baker (JCB-Hotel '88), Kenneth Himmel (JCB-Hotel '70), Dustin Jones, Ershad Chagani (Baker/MBA '19), and Christopher Trahan (Baker '19).



Figure 8. Robert Balder (AAP '89), left, Kate Bicknell (AAP '99), center, and Gary Handel (AAP '77), right, discuss the future of design.

Technology is especially important in this context as it impacts how space is envisioned and utilized. With the inclusion of Augmented Reality (AR) and Virtual Reality (VR), architecture has evolved to showcase building designs as experiential software models. With the use of over 30 software programs, and aided with hundreds of plug-ins, designs are not just tweaked, but are also presented to clients and potential users through virtual reality platforms. This aids in user appreciation of space during the configuration process, leading to better inclusion and engagement. Today, the sector has moved from a consumer of design software to a producer. This has immensely helped in reducing the friction of the design process by improving stakeholder communication, helping them to instantly understand limitations and possibilities.

The availability of large amounts of analytical data has also been impactful, allowing decisions to be made on a much more granular level. Data sources span not only comparable projects already built, but also real-time feedback data loops in order to examine user behaviour. Open data and big data have created problems of overabundance; it is up to the industry to sort through and educate itself with the information. The art of the science is not just having the data but knowing how to utilize it.

While technology is a definite game-changer, the future of design is also heavily invested in the future user. The biggest disrupter among the various user groups is, of course, millennials. A major differentiator of this user group is the need to be alone, but never lonely. This has

brought about the advent of shared space in almost every sector possible, where larger public spaces are combined with shared private spaces to offer a flexibility of sizes and usage possibilities. Convenience and amenities are in high favour among millennials and are usually valued more than the amount of per capita space provision, bringing about a cross-pollination of sectors and a mix of uses at every possible level. It was suggested, however, by the panel that the robustness of design for the built space should span generational differences, especially with aging populations.

Smaller households and a competition for convenience have brought about a shift towards micro-spaces. Battling regulatory barriers and the cost of land in premium locations, in addition to an emphasis on better transport connectivity, the housing sector is attempting to satisfy micro-home demand. They provide less margin for error, necessitating precision in fabrication and construction. As a result, modular designs are perceived as a solution to bridge the gaps. It is evident that this is no longer a trend with the arrival of micro-hotels. As brands enter this market there is a renewed push in the hospitality sector towards more public spaces at the expense of private areas.

With such increases in density, however, nature has become even more essential as drivers of building typologies. The connection to green is necessary at all scales, from the individual space to urban design. Dense urban living is only made possible by the relief offered by open space. Consequently, design has responded at all levels by exploring green spaces through biophilic design in



Figure 9. Moderator Robert Balder (AAP '89), left, asks panelists Kate Bicknell (AAP '99), center, Gary Handel AAP '77), center, and Jerry Zeitner, right, about the inclusion of AR and VR in design.

site selection, setback terraces, or individual floors. Such design strategies have blended in well in branding spaces to give them unique identities and make them social media-worthy to lend an authenticity to a virtual vision.

Overall, the panel emphasized design aiding the revenue productivity of a space and recalled traditional lobbies and excess parking as design fallacies that weren't worth the cost. The ever-changing landscape needs expert management of risk and action towards a resilient future.

WALL STREET AND THE CAPITAL MARKETS

Moderator: Andy Jonas, Co-Head of Real Estate, Goldman Sachs

Panelists: Mark Fawer, Partner, Greenspoon Marder LLP; John Kukral, President and Chief Executive Officer, Northwood Investors; Darcy Stacom, Head of NYC Capital Markets, CBRE; Jonathan Pollack, Senior Managing Director and Global Head of the Blackstone Real Estate Debt Strategies

Our esteemed panel of Wall Street and capital markets professionals represent some of the largest and most influential real estate investment firms in the world. The panel gave valuable insights into key changes impacting capital markets, shifts in real estate fund structures, and future performance in the face of rising interest rates.

The panel kicked off with a discussion about the effects of increases in asset valuation on asset selection for investment managers, and on how the state of the real estate cycle has created pressure on equity investors to change strategies. The panelists all noted a trend in firms redefining the categorizations of value add and opportunistic assets. One panelist noted that while more money chases more expensive assets, broad return targets of around 20

percent have not changed. This market dynamic is causing the assets held in some value-add funds to look more like properties fit for an opportunistic strategy. A value-add fund that traditionally seeks light upgrades on properties, signs higher-credit tenants and sells on ten-year holds, might now shift towards riskier development-heavy investments held for longer durations than a typical opportunistic fund.

In addition to this shift on the equity side of real estate investments, all panelists noted a large increase in the number of debt funds over the past two years. Driven by strong returns, rising rates and a desire to be closer to first lien position, debt funds address growing appetites for lower risk and high upside (often double digit returns on an unlevered basis) without taking excess equity-like risk. The financing markets have become very competitive and the covenants that would be required until recently are often not attainable by lenders today. Panelists have seen higher equity contributions across several markets from investors, even in the face of .25 to .50 decreases in cap rates over the last year. Rising rates have also put pressure on holding periods as investors seek to sell properties bought at high valuations and financing becomes more expensive.

The panel finished by discussing the possible consolidation of managers as an after effect of the late cycle environment. Large pension funds have outlined desires to consolidate the number of managers in their portfolios during the last few years. The emphasis to limit the number of relationships is seen as the impetus for consolidation. To meet the desired investment styles and risk profiles of each large capital provider, funds might have to acquire new capabilities by recruiting other managers to gain competitive product offerings for clients.



Figure 10. From left to right: Andy Jonas, Jonathan Pollack, Mark Fawer, Darcy Stacom, and John Kukral.



Figure 11. Jonathan Pollack, left, discusses shifting investment strategies next to Mark Fawer, right.