Kayne Anderson Real Estate

'The more noise, the better'

Volatility is creating a buying opportunity in alternative real estate sectors

Chase McWhorter, Institutional Real Estate, Inc.'s managing director, Americas, spoke in May with **Al Rabil,** CEO of Kayne Anderson and CEO and co-founder of Kayne Anderson Real Estate, about the implications of the current market conditions for investment in demographically driven property sectors. Following is an excerpt of that conversation.

How do you think about investing with all the volatility in the market? And what are the sources of volatility you're most concerned about?

This environment is beneficial to us. The more noise, the better. We deem ourselves to be in a dislocation – a slow-moving train wreck, I've been saying. While current conditions are not as severe – and, hopefully, will not become as severe – as the global financial crisis or the COVID-19 onset in March 2020, higher-for-longer interest rates have inflicted pain, creating investment opportunities for us. We continue to have unfettered access to equity and debt capital. With intentionality, we invest in medical office, senior housing, student housing and now light industrial, largely because these asset types are not highly correlated to the macro economy. Not surprisingly, not all our competitors have fared as well as we have. We do think there will be incremental competition in alternatives on a going-forward basis because of the rotation of capital into these sectors. But we see less competition today.

We welcome incremental competition because a lot of that competition will be buying from us. We look at it as an opportunity. We've been working for almost 20 years to socialize these property sectors. What can happen reasonably quickly in the right market environment – or even in a dislocated environment – is that qualified, well-known players can raise capital and decide to allocate it into the verticals in which we invest. What cannot happen quickly is replicating an operating platform like ours with strategic knowledge about these property sectors, that takes years and years to put in place.

We've been waiting for this dislocation to arrive, and we're ready to capitalize on the opportunity.

How do you think tariffs will affect the real estate sector?

Tariffs or the threat of them have caused dramatic uncertainty today, and probably for an extended period, in terms of pricing for a significant number of items – copper, aluminum, lumber – which makes planning very difficult. In the short term, the effect will be decreased new supply activity, which enhances the opportunity set from the perspective of existing assets. You can't come close to replicating existing assets at anywhere near the cost basis at which we've been acquiring them. The market was already down significantly in terms of new supply because of high interest rates and inflationary dynamics. Medical office is down 34 percent versus its last 10-year average; senior housing is down 68 percent versus its last 10-year average, but by more than 75 percent from its peak year of 2017. Industrial is down more than 70 percent from its peak in 2022. All these numbers are pre-tariff numbers, and we expect the trend to continue. All real estate is down in terms of new supply, and that is no surprise.

The difference about the verticals we're investing in is they have a massive decrease in new supply at a point in time when the market has dramatically escalated demand, mostly demographically driven, in terms of health care. From a public university education standpoint, it's the disparity in cost between a public and private university education. With light industrial, it's onshoring ecommerce. Although there could be some tariff-related dynamics, even short term, we see support for the small businesses that utilize light industrial. In these sectors, we have escalating demand on a long-duration basis and dramatically decreased supply today. The demand/supply imbalance that already exists is going to become more exacerbated during the next two to four years.

How is this environment for acquisitions?

It's a robust environment for us in acquisitions, not because others don't see this opportunity, but because some of our competitors haven't fared as well as we have from a fundraising perspective. They do not have the same strategic relationships we have with our finance partners, or lenders. We have become known as a certainty-of-close buyer, and higher-for-longer interest rates have created a dislocation for many sellers, which is requiring forced selling, whether from distress, duress or investor pressure in terms of redemption queues. Many assets that were built or bought from 2017 to 2022 have maturing debt caps or swaps that are massively more expensive than they were during that time frame. There is also a reduced denominator, meaning a decreased value, in most cases, even though there have been escalating rents, because we are in a different interest rate environment. When I say distress or duress, I'm talking about high-quality assets that have been performing extremely well. They were just bought or built under dramatically different assumptions.

This environment favors us significantly because, beyond just pricing terms and conditions, certainty-of-close and the time frame in which you can close become primary dynamics from an acquisition standpoint. This is close to an ideal environment for us, undergirded by long-duration demand trends, supply constraints and a buying opportunity that has been created by a dislocation. We have been waiting for this type of opportunity. It is the best opportunity we've seen since just after the GFC.

Has the first half of this year changed your perspective at all?

Not at all. We've seen more uncertainty, obviously, inserted into the market. We have not seen a material drop – or any drop, really – in interest rates, either short term or long term. I do believe short-term rates will drop in the near term by the end of this year. But I cannot predict when and what that will look like. My view is, directionally, we're headed to a lower interest rate environment, but the 10-year Treasury has been sticky around the 4.3 percent or 4.4 percent range, and I don't see a catalyst for that diving down anytime soon. The buying opportunity in 2023 and 2024 has continued into 2025, and we have invested nearly $7 billion of gross transaction costs since July of 2023. Looking forward, we see this opportunity set continuing through at least the middle of next year, if not the end of next year. It may taper off some, however, if interest rates decrease.

The market is forward-looking to some extent. Once we have validation that the Federal Reserve is going to cut rates, that may entice more buyers to enter the market, and institutional capital may get more comfortable investing. But we've seen a very similar market from a buying perspective in the past. Vintage matters, and we were very disciplined investing in 2020 to 2022. We invested, on a relative basis, very little of our available capital during those three years. Then we started leaning in beginning in the fourth quarter of 2022, and we have really leaned in from 2023 through today. We see no change in the environment near term. Paralysis might be an overstatement, but there is a wait-and-see approach from many investors – "We were going to do something, but let's just wait the next 90 days. Let's see if any tariff deals get done. Let's see what the world looks like. Let's see if there's a denominator effect and watch what happens with the stock market." There are a lot of reasons for institutional capital to hit the pause button for now.

What advice are you giving investors with whom you meet?

I don't know that I'm giving investors advice. Rather, we're talking about the opportunity set in front of us and saying that this is an ideal time to be leaning in and to be investing capital with us and in these verticals. Get comfortable being uncomfortable because, historically, that is when the outsized returns are created. Human emotion plays a huge role in investing, as we all know. Disciplined investing is really fighting that fear to a large extent and saying, "Yes, it feels better to buy a stock when the stock is going up every day. It's much harder when, while the fundamentals haven't changed, the stock is down 20 percent or 40 percent."

We're saying, "Look at the fundamental set up here in these property sectors where you have escalating demand for the next 20 years, massively reduced new supply and a buying opportunity created by both interest rates as well as external uncertainty." Essentially: Hold your nose and invest.

This is the time for outsized risk-adjusted returns, rather than when we get the all-clear signal and everybody jumps in the pool. I'm certainly not giving investors advice. I'm not looking at their balance sheets. That is their call. But I am laying out what we do and how we do it, the outsized opportunity set we're seeing and the strong belief we have that the last two years, this year and next year have potential to be the best vintage years in real estate overall, but specifically for demographically driven real estate.

How long do you see this buying opportunity existing? More specifically, is it across all real estate sectors, or do you zero it in on the demographic?

There are certainly opportunities in other property sectors that are not demographically driven, such as office or retail. Those are different opportunities, and I'm not the one to address those price-driven opportunities. Those opportunity sets, generally speaking, are different from the buying opportunity I'm describing.

We certainly expect the outsized opportunity to last for the next 12 months and probably through the end of 2026. My view stays firm that the next 18 months continue to be an outsized buying opportunity, and that we will get greater liquidity and lower interest rates starting later this year and into next year. Investors will be forward-looking to some extent. While there will continue to be opportunities, they may not continue to be as outsized as they are today.

There are a lot of question marks. People, in general, are pretty good at dealing with good news or bad news, but not as good at dealing with uncertainty. What do these tariffs mean? What's going to happen to the stock market? With pension plans and sovereign wealth funds, money is coming in, and it is not going to sit in cash forever, but we are coming off of two years of very tepid investment. In 2025, we are seeing a loosening of that dynamic and a more favorable fundraising environment.

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CORPORATE OVERVIEW

With approximately $17 billion of assets under management, **Kayne Anderson Real Estate's** investment objectives are to create strong risk-adjusted returns by focusing on current cash yield and increasing value through cash-flow growth, while remaining sensitive to capital preservation. Since 2007, Kayne Anderson Real Estate has invested in alternative real estate sectors, including medical office, high-end senior housing, off-campus student housing/multifamily and self-storage. Our vertically integrated team brings expertise in all aspects of real estate investing and management to each of our investments, thereby maximizing operating capabilities.

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