EPISODE 12: REAL ESTATE

Jeffrey Rich
Welcome to Careers in Finance, presented by the Boehly Center for Excellence in Finance at William & Mary's Raymond A. Mason School of Business. This podcast will explore various areas of the financial services industry, career paths in finance, and other practical insights that will help students better understand and prepare for professional success in the field of finance. Be sure to subscribe to the podcast and catch future episodes as we explore the field of finance. And now your host, Jad Howell.

Jad Howell
Okay, joining us today is Lange Allen, managing director with USAA real estate, where he oversees the domestic industrial logistics development platform. Lange, thank you for joining us today. It's good to have you.

Lange Allen
Well, thank you very much, Jad, really happy to be a part of this.

Jad Howell
So Lange, why don't you tell us a little bit about yourself and your background for our listeners.

Lange Allen
Yeah, sure, Jad. So I originally started my career off with CBRE in Dallas actually after graduating from SMU with a finance real estate finance double major started off in the brokerage business transition from that to Weinburg Realty Investors, where I also handled all of the industrial leasing throughout the Dallas Fort Worth area, did that for about five years and then transitioned into an asset management role with Weinburg out of the Houston office overseeing all of Texas except for Houston, Southern California and Memphis, and then actually joined USAA real estate about 12 years ago spent the first little over six years in the asset management group covering about half the country and then ultimately running the entire industrial logistics asset management team to the head-up or US development operations again, right around six years ago or so. And I'm responsible for all of our development activities in the Continental forty-eight.

Jad Howell
That's terrific. You know, I suspect, Lange, that you are quite busy these days. You know, if we read the headlines, especially related to commercial real estate, we typically are reading about the demise of all things retail and whether or not companies, employers are going to downsize, shrink their space requirements. It's this remote working model going to fundamentally shift a

demand for office products and commercial real estate asset class. But the darling is industrial. And again, that's your expertise. And tell us what you've been up to today.

Lange Allen

Yeah, I know, Jad. And I think, you know, first and foremost, well, there's no question that industrial and logistics properties are a focal point in a very active point in the code environment. And I honestly would point back to the end of the GFC as really a attention focusing time frame for industrial. You know, that's really when I think industrial as a whole became a recognized institutional asset class, whereas prior to that, it was really considered a more de minimis kind of diversification play. It didn't fall into the same categories as office, retail, and to some extent, hospitality. There's no question we're extraordinarily busy today as a byproduct of COVID. But I think we were also extraordinarily busy the past couple of years as we've seen tremendous growth from e-commerce in the post-GFC world and in more particularly, over the past three or four years.

Jad Howell

And you know, Lange, maybe tell our listeners a little bit about why we've seen that increased interest in all things industrial, greater acceptance as part of an asset class that an institution might want to invest in. But what has happened within that space that's led to this demand?

Lange Allen

Yes, it's a great question, Jad I think, you know, really what drove a lot of it was people's experiences during the GFC with other asset classes as compared to industrial to primary drivers being you know, you generally have mission-critical facilities with respect to industrial operations or logistics operations. So they're generally the last ones that are shed from a business operation perspective. Secondly, they are far less capital intensive, in most cases on a per square foot basis to reten as well as to carry. So the average operating expense carry for an industrial asset is somewhere between a dollar to two dollars a foot. And the average in re-tenanting cost is probably in the neighborhood of two to five dollars a foot. As compared to office properties, which can have operating expense carries well in excess of 15 to 20 dollars a foot a year and tenant improvement costs that can also be in excess of 40 to 60 or even eighty dollars a foot. So I think; furthermore, there was the industrial asset class specifically frappe was extraordinarily resilient from both an occupancy and a just an overall financial health during the GFC. While our portfolio did suffer some, as did everyone's, I think we bottomed out around eighty-seven or eighty-eight percent overall occupancy in the operating portfolio that USAA had at the time, and that was only for two quarters and then continued operating north of 90 percent. That has been the case since the GFC through today. Where we currently are operating, just shy of ninety-nine percent occupancy on our stabilized portfolio of assets, not including those assets that are actively under development that we could not actually lease.

Jad Howell

That's amazing. Ninety-nine percent off. Talk to me a little bit about, obviously, COVID, and it's been called in so many things, one of which is moving all things online. In particular, groceries, shopping, Amazon, and others have really been the beneficiaries. And I know you got a key relationship with Amazon that will be here in a moment. But talk to our listeners, if you would, about how e-commerce has been accelerated as a result and its impact on the investment space.

Lange Allen

Yeah. So, you know, obviously, you know, COVID presented a challenge for all of us, right? I mean, the concept of going into a grocery store and picking up goods at your leisure was basically completely inhibited. Shutdowns took place across the country, and consumers were forced to buy and procure assets through different mediums. I think many of the large retailers were building out, with the exception of Amazon, as you mentioned, you know, e-commerce execution platforms, but had, for the most part, and in many cases struggled. Many of them were focused on click and collect, which is, you know, order online will pick up in-store or some sort of other multi-channel medium for e-commerce. COVID really required them to shift that entire model, not to say that they couldn't pull up in a store and pick things up, but there weren't dedicated online pick-up delivery that didn't exist in restaurants for the most part. They're very few of the grocery stores had a dominant share of their parking area dedicated to that type of execution. And so it really forced the retailers and the consumers to adopt different ways to shop. The analogy that I use is, I mean, I can't imagine how many different parents and grandparents and including my own, that I have had to teach how to use Amazon. And the e-commerce adoption rate, as it's referred to in the industry, grossly accelerated as a bipart of COVID many times exceeding what the out-year projections were for three, four, or five years from January of twenty-twenty.

Jad Howell

It's just remarkable to think about. You mention Amazon, and I know you have a deep relationship with them. Can you describe what Amazon's response has been as kind of a leader in this space, right? For all things e-commerce and distribution. Talk to us a little bit about how they've responded and what has trickled down to you and USAA real estate to support what they're trying to accomplish through and beyond this pandemic.

Lange Allen

Yeah. So, you know, it was actually very interesting, Jad. You know, early portions of the pandemic, I think, you know, Amazon and most retailers, you know, hit what was the pause button. Right. They evaluated what is this going to mean for our business? I don't think anybody necessarily was able to calculate and whether it would be positive or negative. So we did see across our industrial portfolio what I would say was a pause in that March and April timeline where companies evaluated what was viable, what was not viable, transactions were placed on hold. We did the same thing. If we were committed to projects and under construction, we continued with it. If we had the ability to somehow delay them, that's what we did. So our industry as a whole did that for about 60 or 90 days. And once we started to see specifically many of the e-tailers and even some of the conventional retailers acknowledging that their ordinary distribution networks and models that to execute on e-commerce didn't work or were inadequate for the amount of demand they were experiencing, they committed to expanding that network significantly. And I think you may have alluded to it a little earlier on the call. We are seeing an unprecedented demand from the e-commerce users, as well as traditional retailers and just general industrial users, third-party logistics providers, and others in terms of their need and demand for warehouse space. Through service, not just e-commerce, but also increased inventory levels. I always used to joke early in my career. I said my entire industry would be obsolete if Just-In-Time delivery were capable and worked right. We would not have to warehouse anything. Right. If everybody had a 3D printer, we could eliminate all the warehouses across the world. And we would just get what we wanted when we wanted it. You know, what COVID proved is that, you know, these one-month safety stock that was pretty common throughout the industry was grossly inadequate to meet a COVID type demand. We all know about the shortage of toilet paper. We all know about the shortage of paper towels. We all know about the shortage of essential goods. And that was largely based upon the fact that safety stocks were at truly, ridiculously low levels, inadequate to support what happened. So what we have heard and what we are seeing is that whereas a two or three-month safety stock may have been a pre-COVID norm. Six months safety stock is now what they need. And even an industrial estate guy can conclude that if three was what was required before and six is what's required now, you need twice as much.

Jad Howell

You know, let's go over a little bit out of the pandemic and COVID. Can you describe for the listener Amazon's facilities and maybe differentiate between those facilities that you construct.

Lange Allen

Yeah, no, it's a good question. And I think, you know, oftentimes people see a concrete rectangle and called an industrial or logistics facility and think that that's, you know, it's just trucks going in and trucks going out. You know what's interesting about Amazon's network or, quite frankly, any e-commerce company is it differs from a traditional warehouse. And in a traditional warehousing environment, products were generally brought in a full pallet load. They were somehow reorganized and left the building in a full truck on a full pallet. The fulfillment center network, which is what e-commerce companies do, including Amazon, is effectively in a fulfillment center building. They take that palletized product and break it down into the unit level, whereby when you click on that product to purchase it, that singular unit or multiple units can then move throughout the building and be placed into a box that is sealed for your individual shipment and delivery. So it is a far different process inside of that concrete building than what you would have in a traditional retail environment, which is why many of the traditional retailers have had a significant struggle trying to take a conventional warehouse building and make it e-commerce capable. If you think about it in a very simplistic way, Jad, if I'm Wal-Mart and I have a pallet of size large socks, it doesn't make any economic sense to accept an individual order in that warehouse and send a singular forklift driver over to pull a pallet of size large socks and pull one unit out to then have them carry it across the building and put it in a box. So when you think about it in that context, what it requires companies to do is really build out a completely separate facility and network to accommodate the ability to take a pallet, break a pallet into a unit and fulfill an individual order that you have placed, hence the term fulfillment center.

Jad Howell

I've been inside these facilities with you and others. Can you describe a little bit for the listener what the inside of these facilities look like in order to accomplish what you've been describing it and processing it?

Lange Allen

Yeah, it's a great question. And we've certainly seen the evolution of buildings over the course of time for first-generation buildings, including somebody with, you know, for lack of a better description, look like a grocery cart going down an aisle, picking individual items to highly automated facilities today that can, in fact, have automated conveyor systems totaling 15 or 20 miles. Many of the facilities are equipped with advanced robotic technology, which will allow inventory to actually be moved by robots. And to the extent they can be even pulled, picked and packaged by robots, you know, just the individual package sortation capabilities, the automatic label reading on conveyor systems is quite frankly astonishing, such that as packages are packaged, and they are labeled, the individual outbound boxes are separated by conveyor systems into individual semi-trucks that service certain specific areas of the region or the country for that matter.

Jad Howell

You know, and with the potential for driverless vehicles, potentially fully automated robotic process. And eventually, tell me a little bit about your thoughts on how this impacts for you seen these robotics and advancements in technology ultimately cannibalizing what otherwise would have been a job for actual individuals.

Lange Allen

So it's a great question. And I would say that in general, many of these e-commerce facilities, while they have added significant robotics capabilities, we have not seen a significant decrease in the human FTE count. In fact, we've actually seen the FTE counts in many of these buildings increase because what the robotics has actually enabled them to do is increase productivity. And with that increased productivity of total volume of packages, even though you that would naturally say if I was using the same number of packages, I could have reduced my employment count. What we've seen, however, is the inverse, which is they've increased the employment, increase the number of packages and increase the number of employees along with it. To use less employees per package. But you have a significant number more employees or the same number of employees that you may have had in an older, more traditional type of building because you still need the employees.

Jad Howell

I just want to go back a little bit to maybe for the listener. Describe, you know, typically in the field of finance, investment banking, consulting, corporate finance, and these are the traditional career paths for our listeners and for the students. And talk a little bit about the commercial real estate, alternative asset class, how you found your way. You mentioned earlier that you also have a finance degree and how, you know, that career path that you have chosen has led you to industrial development.

Lange Allen

Yeah, no doubt. It's a great question. It's one that, quite frankly, I have rather frequently as I interview analysts and rotational analysts and new people join the firm. You know, the natural progression for most people, at least what they think when they come out of graduate school or undergraduate with a finance degree, is that they want to be focused on development or acquisition activities. My personal recommendation to them is to gain some level of ground floor operating experience within the real estate because that really provides them a much more well-balanced foundation to do the appropriate level of underwriting for both development and acquisitions. And what I mean by that is really what we have USAA real estate refer to as asset management, which is the physical operation and running a real estate, a real estate asset, or a portfolio. And what I remind people constantly is the development and acquisition underwriting is only as good as the people that can actually do it on the ground floor. And the people that actually have to do it are the people in asset management. So one of the things we've implemented in USAA real estate a number of years ago, which is I was instrumental in influencing, is what we refer to as a rotational analyst program because I think it's very important for young people entering the commercial real estate industry to understand and have some level of experience with all the different components. So we actually take our individuals and rotate them every six months through various departments in our company so that they can better understand the different phases of commercial real estate, what different departments operate, and how they fit together. And quite frankly, I think it has generated a tremendous education for those people. And we have seen a far better, more well-rounded group of people come into permanent employment with us. And those departments are generally development acquisitions, portfolio management, and asset management, which are the three key food groups to operating commercial real estate properties.

Jad Howell

That's terrific a concept that we should program allowing entry-level employees as well to understand what their preferences are and how these various job descriptions align with their own skill sets and specialties, and strengths. That makes a lot of sense. So so how did you break through this industry? What did your first job look like? How did you find it, especially for students today who's living in these unprecedented moments of time of a pandemic and they're looking to secure employment, desired employment? How did you breakthrough? And and and then from there, we can talk a little bit about what they've been thinking about doing to really separate themselves, distinguish themselves to secure their desire.

Lange Allen

Yeah, I know. And so, you know, the answer that I always give people is how did I get an industrial real estate? It was the shortest line, and that is the honest truth. No, no, I having graduated from SMU. I had some exposure to the brokerage business and other peers that had gone into the brokerage business. And so I, I went to work for CBRE. After a series of interviews, I was hired, and I remember sitting with Ran Holman, and Ran was like, I'm hiring you. What do you want to do? And the only thing I knew at the time was, as I said, well, I'll do office or retail. And he said, well, I had no, no, no openings in either of those two disciplines. What do you know about industrial? And I said, I don't know anything, but I guess that's where you have an opening. That's where I'm going to work. And quite frankly, today, I count myself as blessed as to having the opportunity to do that. I was an engineering major for the first two years of my career. So stepping into something that was industrial actually worked out very well for me. I then progressed and continued in a brokerage capacity, really cutting these transactions on a day-to-day basis, working for Winegrowing Realty. I think both of those experiences on the brokerage side of the business were invaluable because you actually get to appreciate and understand that somebody on the ground has to sit across the table from somebody else and try to make a reasonable deal and each situation a little bit different. I always remind people that every piece of real estate is unique and finite. And so somebody and every person is a different individual. So somebody may be willing to pay you a little bit more. To have a corner spot here or a little bit more to be in a different location. So in a brokerage capacity, you're really tasked with managing that individual personality, the ownership needs and desires, and return thresholds. And then you are doing it a little bit higher level in an asset management capacity whereby you're actually overseeing the property manager personnel and the leasing personnel. So my career path, I think, was not overly unique in that, you know, I went from brokerage down to management, which is something I am seeing far more frequently today. And, you know, the asset management development role was one that came fairly naturally to me because I understood and dealt with most of our tenants on a day-to-day basis in an asset manager role. And I had understood what their needs were coming out of the brokerage business, or I was comfortable dealing with them in that respect. And then shifting that over and adding the complexity of building a building just adds another layer to it.

Jad Howell

Kind of building blocks, right?

Lange Allen

Yeah, I mean, I look at them now, Jad, as we're talking through this in hindsight, you know, the brokerage side of it gives you the experience of how to negotiate with people. The asset management side gives you the experience to operate the real estate and while still negotiating with people, and then the development side of it just brings yet another piece to that puzzle that now you can take a relationship with a person and understanding of what the needs and returns parameters need to be from an asset management perspective and what the pitfalls of operating real estate to make the best possible development transaction deal.

Jad Howell

We've been talking a lot about relationships and have the ability to able to interact face to face. Talk to me a little bit about how relationships and developing those relationships, both before your entry-level position into this industry and throughout. How has it impacted your career?

Lange Allen

Yeah, so I would tell you, you know, especially in the industrial space and true across the commercial real estate industry as a whole, it is an extraordinarily small world. I mean, today I was on the phone with a gentleman that I sat next to in nineteen ninety-nine at CB. Who was handling leasing for them in Dallas. So I can't stress the importance of relationships across the industry, even across commercial property types. There are many participants that are active in office, active in industrial, active in multifamily, although there has been a trend and a shift towards specialization by asset type. I would tell you that whether it's developers that participate in different segments of the market, capital partners, much like USAA real estate is all the way through brokerage firms. The relationships that you build over the course of your career are instrumental in helping your career. So I always what I always advise younger people is they're looking at entering the commercial real estate business is don't be afraid to cold-call somebody. Don't be afraid to reach out. Don't ever burn a bridge where at all possible. That's where I've seen, quite frankly, some people make some of the largest mistakes in their careers is fighting over the two thousand dollar commission on a deal that you just didn't need to, or it wasn't right to do so. Sometimes, especially early in your career, that can be a very hard thing because two thousand dollars is the rent for that month or rent for the next two months. But I would always suggest and advise people that air on the air on the side of good behavior as opposed to bad behavior or air on the side of do the right thing as opposed to the wrong thing, even though it may in the short term cost you something.

Jad Howell

Very much, especially once in your career. An additional question that I have for you. What will be the top-performing sector within the commercial real estate space in five years?

Lange Allen

Wow, Jad, that's a loaded question. It's going to be industrial, without question. Look, I think it's that's a hard one to answer. I think there's so much uncertainty as a byproduct in many respects of COVID to be able to say that office will outperform hospitality or outperform multifamily retail. What I can, however, say is I do think that those assets are going to look somewhat different in a post COVID environment. I think we do have some level of systemic change. I think the norm of the office building is going to be a little bit different. I think the expectation is for retail, and what that looks like will also be different. I do think that, you know, industrial is, you know like I said this a little bit before the pandemic that we were peaking already and may have been a little overpriced or a little bit too aggressive. I look now at where we are, and I, I certainly think industrial has some room to run. Does it run another five years at the pace that it's running right now? I honestly don't know. But I can tell you that we are in the midst of a systemic change is the way consumers buy products today. And if you believe that we are continuing down the path of higher e-commerce penetration rates, higher e-commerce acceptance, then I think the bet is likely to be made in industrial as opposed to retail, for example. Look, I'm not saying there's there aren't some fortress retail properties that will stand the test of time, irrespective of what the world looks like after COVID. But I think they're there likely. And everybody brings up malls in my industry, the redevelopment of malls. I think this situation has shown where the weaknesses existed before COVID and is just accelerating the process of getting rid of them.

Jad Howell

Lange, this has been incredibly helpful. It's been a real pleasure to speak with you and hear your perspectives, knowledge and share that with our students and all of our listeners and just really appreciate it. Thank you so much for your time today.

Lange Allen

Yeah, well, thanks, Jad. And as you know, I'm always happy to share information, and industrial when I was in school was not something that was even talked about for the most part. And so I, you know, given everything that's going on in the world and the change of its asset class and perception, you know, I, I welcome the opportunity to share this knowledge with your listeners and you in particular, as you know.

Jad Howell

Absolutely. I can't wait for the next time. Thanks so much.

Lange Allen

Alright, Jad, take care.

Jeffrey Rich

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