

# TIAA-CREF Asset Management

*In August, **Geoffrey Dobrmann**, publisher and editor-in-chief of The Institutional Real Estate Letter – North America, spoke with **Philip J. McAndrews**, **Chris McGibbon** and **Scott Kempton** of TIAA-CREF. The following is an excerpt of their conversation.*

*Most people know that TIAA-CREF is a large institutional investor, but they don't always think of TIAA-CREF as providing third-party investment management services.*

**McAndrews:** TIAA-CREF Asset Management, our institutional asset management division, was formed in 2004, so we have been providing third-party investment management services for the past five years. We seek to offer products and services that satisfy our clients' individual portfolio needs and deliver consistent and leading performance. In terms of our real estate offerings, we provide our clients with access to a broad spectrum of solutions, which includes a variety of funds and separate account strategies. Our investment team employs various strategies, spanning the risk/reward spectrum, that focus on specific regions and sectors.

*So, an important distinction is that while TIAA-CREF Asset Management is a relatively young player in the third-party space, the global real estate investment team offers years of experience in constructing and managing client portfolios?*

**McAndrews:** Yes, our more than 60 years of real estate investment experience has allowed us to gain expertise in driving investment performance through complete market cycles to create value for our clients. Our consistent ranking as one of the top ten real estate managers of U.S. tax-exempt assets (based on assets under management) for the past five years, as reported by *Pensions & Investments*, illustrates our commitment to the asset class. More importantly, however, we believe that the extensive industry relationships

we have developed over the years will serve as a solid foundation to enhance performance in the strategies we manage. Our established relationships serve to facilitate our access to deal flow and the capital markets, which provides an opportunity to secure competitive pricing and financing for our portfolios; for our clients, this translates to improved performance potential.

*In terms of real estate investing, what do you think sets you apart from other managers?*

**McGibbon:** In the current market, as a relatively new player in the third-party space, we can offer clients an opportunity to invest in "young" funds, which are likely to be a fraction of the average size of our competitive set. As other managers with more established funds may be faced with liquidating portfolios to meet redemption requests and financing obligations, we are positioned to buy into the market. We believe this provides a significant opportunity to offset today's declines with tomorrow's recovery. We are committed to delivering value to our clients and we see opportunity as it relates to acquisition capacity, current pricing, and market distress and recovery.

**McAndrews:** Clients need to know that they are investing with a financially stable firm that operates with prudence and sensitivity to minimizing risk. We understand the importance of risk management and we focus on it. We have a dedicated risk management unit that evaluates the operational, market and credit risk of all the major asset classes. The team provides risk analysis, develops innovative risk measurement models and tools, and regularly monitors and reports on portfolio risks. We appreciate the difference between risk aversion and risk management. We are not averse to risk; rather our risk management capabilities help us to appropriately price risk.

**Kempton:** Investors are becoming increasingly interested

in green and responsible property investing. We have played a significant role in this area and are committed to increasing the energy efficiency of our investments on a portfolio-wide basis. We are an active participant in the EPA Energy Star Program and the only financial services firm to be recognized by the EPA as an Energy Star Partner of the Year. We are pleased to have been awarded this important distinction for the past two years. We proactively evaluate each property to identify capital expenditure programs that will result in increased energy efficiency, while providing an appropriate investment return.

*Are you structured in a way that promotes a positive alignment of interests with your third-party clients?*

**Kempton:** We establish an alignment of interests through several means. First, and most importantly, we have made significant co-investments in all of our third-party investment vehicles. In addition, we are accountable to our senior management team, who are just as demanding as our investors when it comes to delivering performance. Finally, our portfolio managers' compensation is closely tied to performance. A significant amount of their total compensation is variable and based on the performance of the strategy they manage versus its relevant benchmark.

*How are deals allocated between your real estate accounts?*

**McGibbon:** This is a very common question, since we are managing multiple products spanning our core retirement and third-party investment management businesses. To ensure that new real estate investments are fairly allocated among our different accounts, we maintain a stringent deal allocation process. Simply put, we adhere to a strict rotation policy for any new real estate investments.

*I understand that your unique portfolio construction process is a*

*key differentiator for you; can you tell me about this approach?*

**McAndrews:** We are committed to building portfolios, regardless of mandate, based on a uniform top-down, bottom-up approach. We believe that returns are driven primarily through market selection and sector allocation. We are committed to a rigorous market selection process and prefer to take style risk at the property level and avoid market risk in our portfolios. We complement our top-down strategy by driving the bottom-up returns through our seasoned team of acquisition and asset management professionals. We believe this approach creates the synergy that can elicit the outperformance investment managers seek to achieve.

**McGibbon:** Execution at the asset level is very important, but we believe it should be done in carefully selected markets that have historically outperformed and have good prospects for continued outperformance. We have found that supply constraints are more important than demand in driving total return, so we limit our investment universe to markets with historical outperformance and high barriers to entry. We believe we are starting with the wind at our back by simply operating in such markets.

**Kempton:** Sector allocation is very important, as well. The most significant driver of overall return is market selection, but the second most important driver is sector allocation. We dedicate a lot of time analyzing how sectors perform in a relationship with each other. For example, retail and office sectors are negatively correlated in terms of their outperformance in the National Council of Real Estate Investment Fiduciaries (NCREIF) Property Index (NPI), so there are certain times in real estate cycles when you

should be longer in office properties than in retail.

*How are you navigating the current downturn?*

**McGibbon:** Portfolio construction and the appropriate market and sector allocations are absolutely critical in navigating the current downturn. In fact, I think our approach has gained traction with investors as they see the importance of operating in markets with sound fundamentals and a track record of performance. Market turbulence has served to expose the underperforming market shortcomings and return volatilities.

*In closing, what is your outlook moving forward in this cycle?*

**McAndrews:** We are optimistic and plan to strategically create value by acquiring assets that have experienced distress caused by the capital market dislocation. There is significant stress in real estate funds that are burdened by their current leverage positions on both a portfolio and property level basis. There is clearly potential for significant reward for those who enter the market toward the bottom of the cycle. The key is to have dry powder and the capacity to invest. We feel that we are well-positioned to capitalize on opportunities that exist as we emerge through this down cycle. ♦

#### INTERVIEWEES



**Philip J. McAndrews**, managing director, is head of portfolio management for the TIAA-CREF organization and Teachers Advisors, Inc. McAndrews is responsible for overseeing portfolio investment strategies. He has more than 26 years of investment experience.



**Chris McGibbon**, managing director, is a portfolio manager for the TIAA-CREF organization and Teachers Advisors, Inc. McGibbon is the portfolio manager for a core investment strategy. He has more than 11 years of investment experience.



**Scott Kempton**, managing director, is a portfolio manager for the TIAA-CREF organization and Teachers Advisors, Inc. Kempton is the portfolio manager for a value add investment strategy. He has more than 21 years of investment experience.

#### FIRM OVERVIEW

TIAA-CREF Asset Management®, a division of Teachers Advisors, Inc., provides institutional investors with access to the TIAA-CREF® organization's sophisticated investment management, research and analytical capabilities. Its investment strategies cover a wide spectrum of asset classes, from traditional equity and fixed income to real estate and other alternatives.

With \$374 billion in combined assets under management as of June 30, 2009, TIAA-CREF is best known as the leading provider of retirement services in the academic, research, medical and cultural fields and one of the largest institutional real estate investors in the U.S. with approximately \$58 billion invested in real estate assets.

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