Chris Merrill:

That's what the value is. If you do one deal with a partner, that's a failure. The idea is let's go do a lot together, build relationships. That's the part of the business I really enjoy. How can you do things with partners where I love surprising and where, okay, tough times, we could go structure deals and we can hammer them, but no, let's not. Let's help them be successful too and then we'll all be successful together.

Matt Slepin:

Hi, this is Matt Slepin and welcome to Leading Voices in Real Estate. Today's interview is a conversation with Chris Merrill, the co-founder and CEO of Harrison Street, now a $53 billion family of real estate funds focused on what Chris calls demographically driven real estate niche sectors like student housing, seniors housing, self-storage, life sciences and infrastructure now in the US, Canada and Western Europe. We've been exploring the niches as differentiated from the main real estate food groups from an operating business platform perspective on Leading Voices for a while, including our last episode with Kevin Marchetti on cold storage. But this is the first conversation looking at the niches from a higher altitude fund level investment management perspective, I think a great conversation. We won't be able to stick with this rigidly, but I'm hoping during much of this year to try grouping episodes around themes.

So this episode with Chris will be followed in a few weeks with an interview with Jordan Sloan from Harbor Group, both investment managers, although with very different investment approaches. We'll then have conversations in April on affordable housing and then workforce housing and of course, August again on sustainability and carbon in the real estate business. And I'm working in some other pairings, particularly around cities like New York, San Francisco, and maybe different secondary market cities. You hear me all the time on Leading Voices referring back to prior interviews. I'm hoping that more back to back conversations will help us together deepen our insights from these great guests.

I just came back from the annual ZRG Partners meeting this year in lovely Jacksonville, Florida. Since we merged Terra Search into ZRG just last April, this was my first summit and a chance to meet my partners from all over the world and from all of our practice areas. I've always looked at my Search practice as to be an advisor and consultant to my clients versus "just a recruiter." What was double down for me at the ZRG Summit is that we are indeed broader advisors around talent advisory. Included but not limited to Search. The breadth of our solutions is actually amazing. We have a culture advisory firm called Walking the Talk, a leadership and business advisory group called Brimstone. We have interim and fractional solutions and we have RPO, which is outsourced embedded recruiters for when a client needs to staff a division up. And in Search, I get to partner with experts outside of my skillset in areas like chief human resources officer, legal, chief technology officer, marketing, et cetera.

I got to say, this is so cool since, as you know from listening in on our leading Voices conversations, I truly believe that the long-term success for a sustained real estate business is in the business platform, not just the real estate assets. These broad solutions let ZRG address these broader topics around business platform in addition to just traditional executive search. I love it. And if you're loving these conversations, please subscribe and share this and other favorite episodes with a friend or colleague. This is episode 139 and you can find all of them on our website at crgpartners.com/leadingvoices. Take a listen to some of the back episodes. If you have comments, questions, or guest suggestions or want to explore how the broad array of talent solutions at ZRG can help your business, please contact me at mslepin@zrgpartners.com. I hope that you enjoy this conversation with Chris Merrill from Harrison Street.

So Chris Merrill, welcome to Leading Voices in Real Estate and thanks so much for being on the show. You are part of our two in a row series on real estate investment management firms and a great counterpoint to both our next guest and our last guest. And next guest is Jordan Slone from Harbor Group who plays in some of the major food groups and you play in specialty classes. And then also the last guest was Kevin Marchetti from Bay Grove and they play in a specialty class and really exemplify some of the value that you get in having an operating platform and an operating business in a niche real estate product type. So that will be the theme of our conversation today, and I'm really thrilled to have you on the show.

Chris Merrill:

Well, it's great to be here. Thanks for having me.

Matt Slepin:

Yeah. So I want to dive into all kinds of things, but I'd like to start with the guest's overview of their business so our listeners understand the outlines of this. You started in 2005. Your first fund was 208 million, now you're at 53 billion of AUM. Just give us a quick history and then we'll dive into all kinds of things.

Chris Merrill:

Yeah, sure. Harrison Street founded the business in 2005, and really the focus when we started the firm was to try and be unique and different, and it's tough to come up with a unique business model in the real estate space. So we wanted to put a little bit of a different twist on the investment model. And so the idea was to focus on demographic real estate, areas of the market that we felt were more resilient, that really were not about trying to follow the economic ups and downs, but really where demand was consistent. And so the theme was let's focus on these highly fragmented segments around education, healthcare, et cetera. And that's really how the firm was born.

And really what happened a few years into the life of the business, we went through the global financial crisis and it highlighted the strength of these assets. Student and senior housing did better than multi-family, self-storage did better than industrial, medical office did better than office. So we realized we were onto something when we saw that resilience and we saw how well these asset classes did coming through the global financial crisis.

Matt Slepin:

So you wanted to be unique and different and then happened upon this. Did you happen upon specialty sectors or did you happen upon the demographic-driven nature of these? And then you were probably surprised with what the results were.

Chris Merrill:

My background has always been trying to do something a little bit different in the space. Prior to Harrison Street, I started Heitman's overseas business and created the first funds targeting Central Europe in the late '90s. And I realized while it might be difficult to launch something new, you had the space to yourself. And so when I came back to the states, I was doing some investment in some of the demographic segments and there was a lot of interest from investors, but they were just dabbling. They'd get five or 10% of their fund, would get exposure to student housing or storage. So I said, "Why don't I be the pure play guy just in that space?"

The idea being, hey, you got to build an ecosystem. You got to go dig up the acorns. You need to build one at a time assets and it's go do the hard work. And it just so happened because a lot of investors said, "Hey." I remember when I did Central Europe, they said, "You're nuts. That market's not going to develop." And I think even with some of these asset classes, people didn't really see an institutional market developing with student housing and senior et cetera. So we've certainly been pleasantly, pleasantly surprised by the level of interest. It's not shocking to me because we've seen how well these assets perform, but the amount of institutional interest now in these asset classes is really overwhelming.

Matt Slepin:

Yeah. And when you make a more focused bet, you may have more opportunity, but you may also have more risk. And have you seen that risk concurrent with that opportunity or not in these particular assets, specialty asset classes?

Chris Merrill:

What we really thought about was how can we de-risk the model? And so when we really looked at it, it was we don't want to just be in one sector like a student housing fund or a senior housing fund. So we said, "Let's build it around a handful of these sectors so that we can, depending on some of the demand supply fundamentals or some market fundamentals, we can move in between but we can build a diversified portfolio of student housing, senior housing, medical office, self-storage, and I'll talk later about the expansion into other sectors.

And then we chose to do it through managing many different operating partner relationships. You mentioned some of the discussions you're going to have are with more vertically integrated firms that really do everything soup to nuts. What we recognize is in these fragmented asset classes, if we were going to build a highly diverse portfolio and de-risk it, well, we needed to venture with many different student housing companies, many different senior housing companies because that allowed us to lay off pre-development exposure, recourse risk. That allowed us to, if a partner didn't do well, to bring in another partner.

So we systematically went through and said, "Okay. Where is the risk in the business model and how can we de-risk it?" And I think that risk management has really been really the why we I think have grown to where we're today.

Matt Slepin:

Yeah. And it's interesting though because sometimes you think of concentration risk and you generalize by having multiple partners, but the concentrations all one day surprise you that they're all the same. But as some have gone up and others have gone down during COVID, during the GFC, have they all performed well or have some gone higher or lower than others?

Chris Merrill:

Well, we've been doing it for 17 years now, so we've certainly learned a lot. We've had a lot of partners. We have over 100 different operating partners in the US, Canada and Europe now. We've seen different levels of growth. We've seen firms make mistakes and we've learned a lot too on what firms we want to partner with. And we've had some partners today that we've been investing with for 17 years and have done 50, 60 investments. We have some that we turned over. And again, what we recognize though was having a model where you had these highly diverse operating partners, again, helps us manage that risk.

We even try and get them together to push them to be different. We'll do, for instance, a senior housing operating partner conference. We'll bring 20 or 30 senior housing companies together because it's such a local regional business, they don't necessarily compete with each other, but we get them in a room and we talk about best practices. What are the challenges they're facing? What can we do to help them?

So we've tried to take a more active role within their businesses and I think that's what we've learned over the years is let's be active. How can we help them with succession planning? How can we help them with technology? How can we help them with cybersecurity? How can we help them with things that are not just capital? Lender relationships? So that's really what has helped make, I'd say, these partners so sticky to us and it's built... It's what's created the mode around our business is that we've got these just world-class partners that we work with. And the whole idea is let's do multiple deals together and let's go build portfolios because that's where tremendous value is created.

Matt Slepin:

Yeah. And it must be that your portfolio manager in any one of those sectors actually has that broader view of that sector than any of your operators do. They have the granular view, but your portfolio manager's doing it either all over the country or maybe even all over the world with different types of niches, say in student housing, different types of campuses so they could see things that the operator gets blind to because they're too in the weeds.

Chris Merrill:

That's a great point, and I think sometimes, we know too much and we'll pass on investments because we're seeing, in a particular market, a number of developers bringing us opportunities. And so to your exact point, that one partner might be so rifle focused on their site, their location, when we can see the bigger picture. We can see what supply is coming down the pipeline or we've operated in this market before and we know what the challenges are. So sometimes, we know too much. And that's one of the reasons why when we've developed our metrics, it's the funnel on how we invest.

And frankly, the other point is we can bring investment opportunities to our partners. So because we're seeing so much, we'll go buy a distressed senior housing portfolio and we'll bring in what we think is the best senior partner. So they look at us as, "Okay. Harrison Street's not just giving me capital. They're not just helping my business through these operating partner conferences, but wow, they're bringing me into new investment opportunities as well." It's just really not getting back in your heels, but really saying how can we be a good long-term partner to these operators?

Matt Slepin:

Yeah. Well and it also sounds like conversations that I hear on podcasts all the time with the famous VCs who in venture startup businesses, they bring so much to the table beyond capital and they insist on doing so.

Chris Merrill:

I look at it's almost like we're like a private equity partner. We're not invested in their companies, but we really take a vested interest in their companies.

Matt Slepin:

Yeah, fair deal. Let's stay broad for a minute and then I want to talk about the asset classes because that's what we're here about. Just stick with the breadth of your company and how much is international now. And then are there alternatives to the real estate alternative, say an infrastructure or whatever?

Chris Merrill:

Sure.

Matt Slepin:

Do you play in both debt and equity?

Chris Merrill:

So the beauty for us is demographic real estate is a global issue. So we recognized that we could take this concept outside of the US. So we've expanded into Canada. We have a Canadian real estate fund doing the same demographic asset classes, and we now have a very big business in Europe. And we have a team of about 40 people in London and we probably manage 6 to 7 billion of assets in Europe. So it's a newer part of our business. It's been active for about five or six years, but it's really growing. And so we're doing a lot of work in the student housing space. We're the largest owner of life science in the UK.

So we've had the geographic expansion and then we've also had the asset class expansion that was really driven by very unique and synergistic relationships with... We're the largest off-campus owner of student housing when we started working with the universities and talked to them about their on-campus housing. And so we slowly have developed a very big business that works on public to private partnerships with universities.

And after we started doing that, we then got into discussions with the universities about their other assets on their campus, their district energy, their wastewater treatment plant. And we recognized, well, if we're going to go work with the University of Chicago or University of Central Florida or ASU or Kentucky, well why not try and bring them other solutions than just their dormitories because we're good at selecting partners. So we've now built this ecosystem. We brought on a infrastructure team from GE Capital that we can go and really help universities, hospitals. We do military housing. We can help them with not just housing but then with other real assets. So that's how we expanded into the social infrastructure world.

Matt Slepin:

And as you go into the social infrastructure world, it's still what you do is provide capital. You're not providing operations say to student dorms.

Chris Merrill:

Yeah. We bring in the partners. So we'll go sit down with a school and we'll say, "Listen. You want to do a life science project? We'll bring in the life science partner. You want to do a data center? We'll bring in the data center partner. You want to do a hotel on the campus? We're doing a hotel on University of Maine, we're doing a hotel convention." So what we want to do is be the solution and the capital provider, but then bring in all the different partners to the table. And there's tremendous amount of deferred maintenance at these universities. So the opportunity for these public-private partnerships is huge.

So for us, we started the business in student, senior, medical, self-storage. We've expanded into the life science space. You think of universities, you think of education and healthcare merging. Life science has been a great expansion for us. We've been doing that for six, seven years now. Then we also got in the digital business and the data center business. And again, we're constantly looking for asset classes that have these consistent demand drivers, need based that do well in good and bad times. We're not just trying to time the market. And that resilience has been the key success factor for us.

Matt Slepin:

So I'm curious about the demographic drivers, but also a business that needs that level of specialized expertise, has an operating business that has a moat around it because they're hard to compete with. Is that a coincidence or is that also a driver to those particular niches?

Chris Merrill:

It's a driver. I think there is a level of expertise that's needed in these asset classes, and we've had to build a big ecosystem here because of the fragmented nature. And really what it comes down to is you've got these asset classes that... We've been through two black swan events now, the global financial crisis, we've been through COVID and these asset classes have outperformed traditional real estate. Their occupancies have held, and at the same time, we can get better yields than traditional real estate. So one always says, "Well, why is that there?" Well, when we first started, people said, 'Well, you get better cap rates in these because there's no liquidity. No one's buying so there's risk." Well that's been debunked. There was 70 or 80 billion of liquidity last year. So liquidity is there. People will then say, "Well, maybe it's the operating nature of these assets. It's a little bit more difficult." Again, over the past two decades, we've seen a lot of expertise, a lot of wonderful companies come into the space. So the operating expertise has been reduced as well.

So I really think the opportunity is really due to this highly fragmented segments and it's hard to find these deals.

Matt Slepin:

It's highly fragmented from a capital standpoint because say in the apartment business, that was and still is a highly fragmented business with lots of mom and pops owning smaller prop. Now it's smaller properties. The real estate world, as it institutionalized, came into highly fragmented businesses. But there was a lot of competition after say multi-family and much less competition on the niche businesses.

Chris Merrill:

Yeah. And I think you can move larger amounts of capital into big multi-family projects and big office buildings, but these, on average, are smaller equity investments. And so again, that has kept a lot of the bigger firms away because they're not going to go waste time on a 5, 10, 15, 20 million transaction. So what we've tried to do and what we've seen, and again, we talked about it when we started and it's really fun seeing it come to pass, but this idea of a portfolio premium. Do the hard work. And so 80% of our investments are individual asset acquisition or developments, but almost 90% of our sales are portfolios.

And so in addition to the yield arbitrage you get just on a repositioning your development, but you also get an extra pop because of this portfolio premium and it's this hard to access nature and that's why look, you've seen-

Matt Slepin:

Double burner.

Chris Merrill:

... there's no public student housing rates anymore. You saw Blackstone take a ACC private. And again, trying to find portfolios in these asset classes is not easy. And so that's been a great execution strategy for us.

Matt Slepin:

Yeah, makes sense. I always quote Bill Stein from Digital Realty Trust from our podcast, but his team is largely not a real estate team. His team is largely a technology team because that's the sector they play in and their customers, so they have to optimize how they work with those customers. Does your team wind up being specialized to each of those asset classes and then even specialized outside of the real estate investment decision into, "Hey, your platform's working this well. How do we analyze it? How do we help you do your work better?" Which you talked about before?

Chris Merrill:

Well, I think it depends on the area of expertise within our group. But yeah, I would say they are domain experts in these spaces. So we have asset managers and transaction managers that are absolute experts in this space. They've been doing it for two decades. We've done 70 billion within these spaces. So they've become real experts in terms of underwriting, evaluating these assets. Then we've got a legal department that has specialized in doing joint ventures. We've got a wonderful ESG and a chief impact officer where we've got an ESG program that we bring that out to all of our operating partners and try and help them with ESG. And then we've also become very deep in terms of how do we help these companies and how can we provide other things to them? The whole goal is if these partners are successful, we'll be successful.

Matt Slepin:

Yeah. And when you talk about public-private partnerships, which is a business I love and believe in deeply, but I'll ask a cynical question. A specialty asset class is prisons. I watched Orange is the New Black and maybe you watched that TV series, but have you played in that asset class where in some ways, the interests become disaligned because you're going to save money and not do it well? Or nose under the tent with the bad guys getting in there in a college dorm? Now I'm comparing a college dorm to a prison, but just riff on that subject for secs. I'm curious.

Chris Merrill:

Well, let me tell you, the college dorms are not prisons anymore.The stuff we're building is off the charts.

Matt Slepin:

The one I was in was.

Chris Merrill:

I know. Now the stuff, it's unbelievable, the amenity packages. We haven't gotten into the prison business we have done, when you talk about government type investing, we're the largest owner of housing on a number of air force bases. So we have a business there. We're doing some district energy at an army base on the East Coast. I can't really comment on the prison business. It's not something we've really gotten into. That one might be a tough one to scale, but I think for us, we're looking for what the is the off take? What are the demand drivers and how do you create that alignment? So for instance, we just built 2000 beds on the campus at the University of Chicago, or we own all of the on-campus housing in University of Kentucky or we own housing at ASU. And the relationship there with the school is, it's a simple one.

It does take a lot of time. It's basically, look, instead of a capital campaign, instead of taking on debt, we will provide that long-term capital. We'll do it in an open-ended structure. So it's a long dated strategy. It's not something we have to come in and flip. And what we'll do is we'll provide the capital. We'll provide the operator. You can control the resident's life. You can control the resident's life of the student. You can control the leasing of the student. We'll create parameters around how much we can move rents, and we'll give you some upside. We'll share in the success of the project. So now the rating agents would look at the project and say, "Boy, this will help their credit rating, the school." They were able to get this project done with no capital and they can generate additional income.

So I think every deal's a little bit different, but for us, we're always trying to make it a win-win, really get the school involved, get them in that partnership with us.

Matt Slepin:

And are those also different capital sources? Because capital source for a long-dated dorm may be a low risk, lower return, but low risk vehicle-

Chris Merrill:

For sure. Our social infrastructure trade is more of an open-ended wrapper where it's low leverage. It's about income. So as a firm, what I didn't touch on is we've got all the asset classes, different locations, then we have a European fund, a US fund, a Canada fund, and then we've got both open end, closed end funds so that our real focus is trying to be a solution. Then when you start talking about our LP base, we have 550 LPs from 20 different countries, pension funds, corporate plans, sovereign wealth, insurance companies, endowments, foundations, high net worths. So it's a great mix of LPs and what we want to do is really be able to go to them and offer multiple solutions. If you want to get exposure to the alternative sector, we can help that through... If you want exposure to Europe or US, open or closed, whatever your return profile is, that's what we've tried to create here. Tried to be how can we be the leader in these segments? And a lot of it is we want to give people different products to invest in.

Matt Slepin:

You've talked a lot about student housing so far, so maybe talk about a different asset class to give an example of then how you behave, how you get a beachfront, what you do there, and then develop the expertise in.

Chris Merrill:

It starts with a theme. So it starts up above at education. How can we get involved in the real asset space around education? Started with off-campus student housing, then it morphed into on-campus student housing. Healthcare was another big theme. Okay, how can we invest in the healthcare space? We all know about the aging demographics. We all know what's happening. The level of 80+ aging is going to double in the next 10, 15 years and supply is really not there. So you've got this aging population, you've got people, as they live longer, memory issues, so we do a lot of assisted and memory care. This same aging cohort tends to go to the doctor more and with technology advances, there's more things moving to the outpatient setting in medical office. Then that led to we started working with some of these universities in the life science space and we do a lot of work with universities that now are partners with us in the life science business. And that was a perfect synergistic expansion of our education and healthcare business.

So there's a story with each asset class. Self-storage, we then started thinking about what about data storage? And that got us into that theme. And then as we were talking to the schools in one of the RFPs they said, "Could you help us with our power plant? Could you help us with district energy?" And we said, "Well, sure. Let's see if we can do that." And so all the growth was very much not grow to just grow, but very synergistic in making the relationships even stronger for all the other asset classes. And then what we do is we try and build... Our funds are not a sector specific fund, so it's not a student fund or a senior fund. It's a highly diversified fund of these asset classes. And we'll either do it, like I said, in a closed-end wrapper or open-ended wrapper, different risk profiles, different return profiles.

But the idea is to really just focus on these themes of resilience, better incomes, less volatility. And so that's really how this has grown. And to me, it becomes very simple. It's much easier to go underwrite, is University of Michigan going to be successful versus look at a multi-tenant office building and try and guess what's going to happen to all the businesses in there. So what I like about it is get me near a great university, get me near a great hospital system and that's really been the theme for us. And the nice thing is too, it allows us to be in 48 different states. Most real estate strategies are in five main cities. So that's how the growth developed. So it's these big macro themes and then okay, now we got to go develop teams, expertise, relationships and just go dig those acorns up and it's a lot of hustle.

Matt Slepin:

Yeah. And each of the businesses you've described, there's public real estate companies. There's REITs who play in those spaces that are vertically integrated operating platforms. Are you the alternative to those who aren't public to be able to get funded to do this? So you're providing the capital to the players in those spaces?

Chris Merrill:

It's interesting. Some of the sectors, like I said, student housing doesn't have any public REITs anymore. Self-storage has a few. Healthcare, there's a handful. In a lot of cases, they'll buy from us, we'll buy from them. In some cases, we'll joint venture with them. We'll do some off balance sheet stuff with them. The market's so big in terms of our sectors, it's trillions. We can work with them. And so yes, investors can get exposure to this space through those means, but you can't build the kind of diversification that we think can be done through our funds. There's some very good companies out there and some, like I said, that we work with, we joint venture with, we buy assets from. Sometimes, we find they have to move based on the public market, based on some of the analyst concerns.

So for instance, senior housing during COVID, people panicked. And so a lot of the REITs were getting out of the senior housing space. I couldn't get enough of it. We bought a tremendous amount of senior housing because to me, the fundamentals didn't change. The front door was just closed. And so for me, it was a great time to be buyers. And we've seen unbelievable rebound in that sector in the past two years.

Matt Slepin:

Drill down on senior's housing and the niches of that for a few minutes.

Chris Merrill:

Sure.

Matt Slepin:

So talk about do you play in independent or congregate care? And there's huge risks associated with it, although maybe not in a diversified portfolio as much.

Chris Merrill:

When you say senior housing, you can paint it with a pretty broad brush. Big picture for us is we're private pay rental. We focus most in independent assisted memory care. We don't get involved in skilled nursing, end of life, public pay. There's a lot of headline risk. There's a lot of risk in that asset class so we don't really play in that space. Market rate apartments for seniors, we don't really play in that either. Mom doesn't sell her house because of bad economy, she might not move in yet.

So where we really want to be is that need-based where very difficult to take care of a parent or loved one that has health and memory issues. And so that's the area that we're focused on. And frankly, what we have seen is as a result of COVID even, those places were safer than the home. They've dealt with infectious diseases for a long time. They know how to keep vendors out. They know how to keep people safe. And so we've seen a lot of people where are saying, "Boy, I'd like to get my mom or dad in one of these facilities," because they were safer during the pandemic.

Matt Slepin:

My mom was in one of them then. Half the people were terrified thinking that these were incubators versus they're safe in their home. I think they were less safe in their home, but it's really interesting because the initial backlash-

Chris Merrill:

It's who runs it. It's very important and that's why we choose operators that have been doing it for decades because they deal with infectious disease. They deal with flus going around. It's not the first time that you've had flu outbreaks at a senior housing facility. For us, it's about the partner and then frankly, when you really drill down to it, they can control who comes and goes. So the challenge with mom or dad at home is the Amazon person shows up, the cables guys show... So there's no way to really control who comes in and out of that house. So from a controlling, they did a much better job.

Now again, there's operators that didn't do a very good job. And again, that's really why it comes down to you got to pick partners because there's many people that, "Hey, I'm a multi-family builder. I can build a building. I'll go build senior housing and manage it." Well, they learned real quickly that doesn't work.

Matt Slepin:

Yeah. I have too many follow up questions to this, but one question is when you have an operating partner, then you have the chance and the risk that they're so small that they don't have good internal succession planning. Do you get into that kind of weeds as you work with someone over the years?

Chris Merrill:

100%.100%. We have a whole checklist we go through. We're not going to partner with someone who's a one man band, so they've got to have succession planning. We talk about how they're enumerating their team. What's their hiring plan? We go through their balance sheet, cybersecurity. We go through a whole host of things just because frankly, we made mistakes early on. But we do have the ability if there are key man issues with our partners, that's the other thing from a risk management standpoint, we can swap out partners. And so if something happens with a partner... And that's where I think risks are when you're just an operator only business or operator only fund, there is lies and more risk because of that what happens if something happens to that operating partner? And they're not going to fire themselves either.

So that is something we saw and frankly, we've seen it. We've seen it through natural disasters and hurricanes, how did partners operate? We've seen it now through the pandemic, how did partners operate? So the one positive that came out of it was for many years, we were passing on a lot of opportunities and working with a lot of operators because it didn't fit our box. And frankly, they were doing fine. In an upmarket, it was things were clearing. But once the market turned and you had the pressure of COVID and temporary nursing and all of that, it really highlighted the strength of having these good partnerships. And frankly, now what you're seeing is very hard to get financing unless you've got a great partner. Lending is there, but it's much less. And it's only going to groups that have good track records, good histories, good balance sheets.

Matt Slepin:

Totally different subject and question about this is how much have the niche sectors developed in the United States? But they aren't yet there in Europe so therefore, there's a lot of running room to develop self-storage, student housing and bring our technology and institutional techniques to other countries.

Chris Merrill:

You're 10 to 15 years behind the US and Europe. And that's really where we started, was in the student space. And so we brought a lot of the techniques in student housing to Europe. And so we've taken a lot of our partners from the UK and Europe and brought them over here. We've got some partners that have moved businesses and expanded their business so that we stayed with them and we do work in the US and now they're in Europe and they're in Canada. But healthcare's a little different in certain markets, in Europe. Different in terms of ownership of assets. And then for instance, something like a self-storage asset. I think Americans, we consume and save a little bit more than some of the Europeans. So storage is a little bit of a different market.

So you have to go through country by country and look at it. But what we found, what we've really expanded on right now in our business in Europe, we've done a tremendous amount in the student accommodation space, the build to rent space, the life science space. Those are areas... We're just now getting into the healthcare space a little bit. So every market's a little bit different and we're doing the same thing in Canada as well. But it's fun to bring not just capital, but lessons learned. To us, I think that makes us a little bit of a different capital partner for these groups in Europe because again, we bring capital, but we can bring those cycles of learning.

Matt Slepin:

Yeah. And it's interesting as the niches have become more predominant and investment has become more predominant in mainstream and the niches, maybe you have more competitors. But on the podcast, couple weeks ago, Chris Hartung from Berkeley and a REIT investor spoke and he said 50% of the Nareit members are now in niche sectors, which is really interesting. I didn't know that was the case. It's not the four food groups at all.

Chris Merrill:

And then look at NCREIF the NPI. It's 6 to 7% alternatives. The Odyssey index, the open-ended fund index, you can't be in the Odyssey index if you don't have at least 75% of your assets in traditional. So the public market has 50% exposure to alternatives. The private market has 6 to 7% and that gives us obviously tremendous running room.

Matt Slepin:

Right. And talk about returns and talk about the Odyssey index because I'm curious as the private markets start getting into this and then how do you both compare in terms of returns and returns on risk in that as well?

Chris Merrill:

The Odyssey index is 75% traditional, probably about 22% leverage. The nice thing about our asset classes is we get a higher cap rate for our real estate segments than traditional historically. At the same time, our borrowing costs are very similar and our asset classes don't have as much CapEx, TIs, LCs as you see in assets like large office buildings. So we can invest in our asset classes and generate very strong income returns. And a lot of it is we've gone through these black swan events and you can see how resilient these asset classes are.

And so I think that's been the hallmark for us, like I said. Not a lot of volatility, very resilient, good income. We're seeing very good appreciation in our asset classes because more and more buyers of traditional real estate are starting to leak into these sectors. And so the Odyssey index used to be 85% traditional, now it's 75%. There was a point in time where multi-family wasn't part of the core fund world. So we're going to see over time more and more of our asset classes part of core portfolios. And I think that's going to further drive more appreciation in the space.

Matt Slepin:

100%. And the core allocators are now jumping into niche spaces-

Chris Merrill:

100%.

Matt Slepin:

... so just hear it. Every time I see one of these guys on a panel, they're saying, "Okay. Now we're doing build to rent or we're doing manufactured housing or self-storage or whatever. So talk about capital a little bit. And in 18 years, you've raised $65 billion. I know you can't fully talk about returns, but just talk a little bit more about the appeal to different types of investor groups, the diversification of your investors, and then also as you get into particularly European investors, they really care about e ESG these days. So what influence does that have on how they invest with you and in your behaviors?

Chris Merrill:

We've invested 65 billion in real estate. We've raised about a little bit over 30 billion. The investor class really, it's interesting. When we first started it was investors that were a little bit discerning about their real estate portfolio. They wanted something a little bit different, a little bit unique. They were concerned about traditional real estate. And so really, they liked the idea of this demographic strategy. It's really evolved over time. And like I said, it's pension funds, corporate plans, sovereign wealth funds. We've got 25 investors from Japan and Korea. We've got investors from China, Middle East, Europe, Scandinavia. So it's been a lot of fun. We've done it ourselves and a lot of our growth was investors introduce us to other investors and trying to get a lot of like-minded investors in the products.

And our funds don't get some of the big funds out there. You'll read about the 20, $30 billion fundraisers and the closed-end funds. We like to do more bite sized funds just based on how much capital we think we can put to work around the segment. So we have multiple products, but the investor base has, really the expansion has really just been outside the US. We started with really just initially in the US and it's really expanded. We have offices now in Tokyo, we have a team in London, we've got an office in Toronto, we've got an office in San Francisco. So we've expanded to get closer to our LPs.

And again, we've been very fortunate. Again, the story for us is we want to be unique. We want to be different. We want to be a first mover. We are a first mover in the closed-end fund in this sector. We're a first mover and an open-ended fund in this strategy. I think we have the only social infrastructure of its kind doing what we're doing. We've got a Canadian fund. We've got a very unique European fund. So I don't mind investors passing on our funds, but what I don't want to have happen is walk in and say, you're the 30th person to present this fund idea to me. So we really push to try and be unique.

And I guess that goes to the second part of your question, ESG, and we've been doing it now for 13 years. We've got a chief impact officer and we've got a pretty big team around the sustainability. But for us, it's about not just the E but the S and the G. And for us, the E has to make sense. If we're going to drive spending, it's got to have an economic benefit to us. And so we've seen that get better and better over the years. So we spend a lot of time showing how much money we've saved on our portfolio by doing things around the E. Then the S is important. We work with FITWELL standards, we want to make buildings more healthy, living standards stronger. And then we focus on governance and G and how can we focus on succession planning and things.

So for us, ESG is a big deal. We have an investor council, some of the largest investors around the world that participate with us and we work with them. And really, we're just trying to move the ball forward for the whole industry from that standpoint.

Matt Slepin:

How much have you seen E move in terms of payback over the last five years, let's say?

Chris Merrill:

Tremendous. Tremendous. We're investing in solar wind assets within our social infrastructure fund because the economics are there now. So we're doing solar, wind, hydro within our social infrastructure fund because there's really solid returns now.

Matt Slepin:

Are any of the social infrastructure investments to put solar panels on dorms, specifically to fund that particular use versus to fund the overall thing?

Chris Merrill:

We will work with companies that do that, but it's not our funds investing and our assets doing that. It's just a separate relationship. But again, my solar team helps make those decisions, helps those contracts so I can use the experts I have on the clean energy side help me and help our ESG team make those decisions for our real estate assets.

Matt Slepin:

And so let's totally change the subject. How did you get into this? How did you get into real estate? When did you get into real estate? And I think you went to Roanoke College. So talk about your pathway a little bit.

Chris Merrill:

So I guess my path is I ended up at a small school called Roanoke College in Virginia by way of a boarding school outside of Boston called Tabor Academy. I grew up in Chicago and really became interested in real estate as a teenager. And Heitman was a wonderful firm and given me an opportunity as a young man. And I was a summer intern for Heitman for three summers. One summer, I was in property management, one summer I was in construction and one summer, I was in acquisitions. The now CEO of Heitman hired me to be in the transactions group after my internship and it was a great experience. And so I always wanted be in real estate.

Matt Slepin:

What during high school got you to say, "Hey, real estate's a cool thing,"?

Chris Merrill:

Chicago is an interesting market from the [inaudible 00:41:46]. I would come down to the city, see the architecture, the buildings, and I just was fascinated by it. And had met someone, a family friend, who was at Heitman and I said, "Boy, I'd love to learn more about it." And just that's how it started. And to me, it's a career that fits me well from a you got to be patient, you got to take your time, you got to play the long game. And to me, that's what I like. And so for me, I liked that about the asset class.

The challenge for me was I wanted to... I've always had this bit of, I don't know if it's innovation or trying to be entrepreneurial or do... So while at Heitman, I went and worked for the chairman of the board at the time and started working on some of their special projects and that led to me making a trip to Central Europe in the mid '90s. I went to Russia and Ukraine and Poland, Hungary, Czech Republic with a developer and came back and basically asked Heitman if I could move to London and see if I could start a business in Europe when I was 27. And they said, "Go for it." And so I was the first employee and did that. So that was a lot of fun. I did that for many years. That market really developed fast. And I won't go into details, but cap rates can press like crazy and everyone thought I was crazy at first, but then it became a real business and I wanted to get back to Chicago.

And the challenge for me was I had gotten that entrepreneurial bug in me. I wanted to do something again I had done in Central Europe. And for me, it was how could I go create [inaudible 00:43:19] culture? But how could you come up with that idea? And that's what fed into, "Okay. You know what Central Europe, fragmentation, people had dabbled maybe only five or 10% of their portfolio. Well, why don't I do the same thing here?" And that's how it all came together.

Matt Slepin:

What was it that got you that idea of demographic driven real estate? That's the word you've been using through the conversation. You come back from Europe, which is a different thesis, it's a niche, it's different, but how did you get to that kernel of a thought?

Chris Merrill:

I was doing some of those asset classes. I was doing some work in that space. It was the redheaded stepchild of real estate, small fragmented deals and very interesting fundamentals, but not the big sexy office buildings, malls, et cetera. So it has that same feel as what I was doing in Central Europe, this idea of there's good fundamentals. People, if presented the opportunity, might want a pure play strategy. Like I said, when I was in Europe, many of the European funds had a small allocation in Central Europe and I said, "Well, I'll be the pure play guy and maybe there's capital there." And that came. So my feeling was, okay, if I become the pure play in demographics, okay, it might take a while to get that message out there, but I think people will see the benefits.

And so a lot of it was just luck. A lot of it may be I was naive-

Matt Slepin:

Thank you.

Chris Merrill:

... luck, whatever. And then for me, I had been through a first fund colonoscopy before and so I knew that there were certain things I needed. I needed a capital partner. I needed to build a team. I needed a good team I could trust. I needed to really build my policies and procedures. Needed to go out and execute the strategy and start building a portfolio. So obviously, starting businesses is difficult. I was very lucky. I had a great mentor, a guy by the name of Chris Galvin who was the chairman of Motorola. And as he was leaving Motorola, the business is family founded, I sat down with him. He had been a mentor in since I was a teenager and was just telling him, "Hey, my desires and dreams were to start a new business around this demographics." And we talked for a while and he said, "Well, let's do it together and I'll help capitalize it."

Just so fortunate that Chris has been such a strong mentor of mine since I was young and said, "Let's do it." And then that's where the name Harrison Street comes from, because Motorola started on Harrison Street in Chicago.

Matt Slepin:

So finding Chris, having Chris as your mentor for many years, and Chris was probably both a mentor and someone with capital to help you start this. So just talk a little bit more about that.

Chris Merrill:

So Chris was the chairman and CEO of Motorola. His grandfather Paul Galvin had founded Motorola. So he has always, and again, another fortunate, he was a family friend, very close to my mother. I got to know him when I was 10, 11 years old and would meet with him a couple times a year and just talk about my life and he would always make time for me. He's just the most wonderful man. And even when I said, "Hey. Should I go to Europe?" He sort of said, "Look, go get global experience." And he just taught me a lot about life and innovation's in his blood. It's in the blood in terms of what he's done. And so thinking differently and how do you take risks?

And so he knew I wanted to have my own business. He knew I had this entrepreneurial bug and he pushed me on that differentiation, innovation. He was very much a believer in what they call Six Sigma quality control. His father really invented Six Sigma and Jack Welsh made it famous. So the way you think about Six Sigma is how do you avoid defects and how do you work through models? And so it was a fascinating process for me. I actually missed the days of us planning the business because it was so much fun to work with a great mind like him and just kept pushing me on risk and differentiation and how do we make something that's unique? The idea was let's go find great developers and operator and we'll come at it as we're family capital. We'll be your partner for the long haul of Mr. Student Housing or Mr.

Senior housing. And then it evolved into us talking to investors and saying, "Here's what we're doing." They said, "Boy, we'd love to be part of that."

Matt Slepin:

It's so interesting because you've talked about the niches and your thesis and how you play and how you position the company. Nothing starts at its mature phase. And so it starts with you as a 30... How old were you when you started the firm?

Chris Merrill:

35.

Matt Slepin:

Oh, you're 35. You start this thing. You have an idea. He really pushes you to those niches and that differentiation and that innovation and together, you get there.

Chris Merrill:

So it was started education, healthcare, storage. So those were the themes. And yeah, it certainly evolved. He wasn't a real estate investor. So where he pushed me on, and that's what I think was the real benefit, is as we would talk about the sectors, he kept pushing me on where have you made mistakes? Where have mistakes been in the industry? What lessons have you learned? And so he came at it from a non-real estate thinking and so just kept pushing and pushing and pushing down to how do we build the team? How do we align the team? How do we align the operating partners? What asset classes? How do we think about financing?

We've never taken recourse and cost overrun risk. We've laid that off. So we went through all these things and he just kept pushing and pushing and pushing and saying, "Hey, just think through. Where have all the mistakes made? Where have firms gone wrong?" Having someone think that was really, really cool. And it really, I think, solidified our model.

Matt Slepin:

That's like the co-president model, but not really because you're running it, but he's helping you-

Chris Merrill:

He's the chairman of my life. He helps me. He sold his interest in the company about five years ago when we brought in a new partner, but I still talk to him weekly. He really helps me with many things and he's just a wonderful human being. He recognized that we needed to create a liquidity event. We needed to bring an institutional balance sheet, really to have the move equity to the next generation, start thinking about the future. So he recognized, as much as he probably did not want to sell the business, he recognized that the evolution of the financial services model was bringing in more the evergreen institutional capital.

Matt Slepin:

So talk about that.

Chris Merrill:

Sure. So we got to a point about five years ago. We were about 14, 15 billion of AUM. And really, the discussion, it really came up because discussion with many investors and consultants really were pushing on what is your succession plan? What is succession plan? What are you doing to incentivize the next generation? We want to see more capital invested in the funds, et cetera, et cetera. So it led to really doing a deep dive in the industry around this idea of bringing on a partner. And so when you looked at many firms had brought on big investor partners. Firms had sold minority deals. Firms went public. So really, we went and found an investor in Colliers who was in the real estate service business, but they really wanted to add an investment management sleeve just like Jones Lang or CBRE.

And so I got to know the chairman who really controls the business, very interesting gentleman, very successful man, and said, "Look. What I'm looking for is a partner that will give us our autonomy, that's not going to sit on our investment. You're not going to change our pace of growth, but will provide capital so that I can buy out the original partners, sell some of my position so that I can move equity to the next generation." But I also now know I've got a evergreen partner in the business and I can go to my investors and say, "There's no volatility. There's no issue with partners now." I think it's solved a big risk factor in some of these firms. And how do you keep talent, how do you retain talent? And they've been a very good partner and we've had pretty solid growth since then from 15 to 55.

Matt Slepin:

So are there are synergies with them that have allowed you to get there beyond capital?

Chris Merrill:

There are synergies. They are a real estate services firm, so they do understand the business and there's different areas where they can assist, whether it's certain levels of research, financings, relationships. If they're doing some advisory work for universities or something, there might be some doors that open. The idea that they are aligned and growing in investment management business and understand the need to create incentives for the team and equity ownerships and how do we use our balance sheet. All those things have really helped us and they've just been a very good partner.

Matt Slepin:

So then the second question is the one that you keep referring to, which is with your team, with succession. Ego and stuff changes after you've had a capital event like that. And then you can share in different ways with your team. Succession can mean different things. Their ability to play in the capital stack.

Chris Merrill:

I'm 51 now. So this was not a do it when I'm 65 and I want to retire and I want to go sales [inaudible 00:52:01]. I wanted to do it while we were in our second or third inning of the business because I love this business. The stuff we're doing around ESG, the stuff we're doing around a lot of things now. We have 28 interns every year now because I was an intern. We have a big internship program, so I love hiring. So I love the business and so I wanted to do it at a time not when it was the end of my career, but he middle of my career where I could say, "Okay. Let's get the next generation some more equity, some more incentives."

I didn't want the 35-year-old walking into my office like I did, just go start a new business. By the way, that's okay if they do, but for me, I wanted to do everything I could to get the platform really solid. And so it was again, lucky, fortunate. I met this gentleman. The chairman of because is a guy named Jay Hennick. He's fascinating. He's really talented. So for me, it was a perfect, perfect relationship for us.

Matt Slepin:

Wonderful. And then also since, because you love the business so much, do you get to change your focus on what you work on to the things you like the most or is the most strategic for you to be involved with?

Chris Merrill:

Yeah, and that's really... Because what I've recognized, I think with the business and the people around here and at most companies, money's one piece of it, but it's growth opportunities. It's intellectual curiosity. And so I've been able to take the analyst, the gentleman who was my analyst when I started the business is now our global CIO. Our first intern is now a senior vice president. So I've been able to elevate a lot of people that really have carried this company for a long time. I've been the band leader and for me, I'm spending more time on getting people in different seats, pushing people on management and leadership. I love to spend time with our clients, meet our clients. A lot of what I'm doing is I'm bringing in good talent, meeting our clients and supporting the growth. And it's been a lot of fun to see a lot of people just grow here and take on really solid areas of the business.

Matt Slepin:

Yeah. Well, it's interesting because you could take any of your subject areas and you could grow a team or a person to become stellar in that area.

Chris Merrill:

And that's what we do. We have leaders in LR sectors. We have leaders in our P3 business, infrastructure business. We've got leaders in portfolio. So yes, and I can even take someone and move them to our London office and I can give them opportunities. We just had a gentleman move and open our Tokyo office that came from our LA office. And so for me to be able to offer people that are, "Hey, you're a rockstar. You're a great culture keeper of the business." "You know what? I lived overseas for a while. It was fantastic. Why don't you go give it a shot?" That's the thing I enjoy the most with this.

Matt Slepin:

Yeah, it's interesting. And I rarely see someone doing this, as you say, when they were 46, if I'm doing the math right, versus when they're, "I just did it at 65 and I have runway. I'm enjoying this. I love what I do too. But I'm definitely doing it as the last chapter, not a long last chapter or a second book, part two."

Chris Merrill:

Well, it just went to the whole Chris would always push me and tell me where mistakes are made. What happens. And I think some of the businesses, they don't recognize some of the need to really get the experts, get the people that are really running the business, get them involved, get them aligned.

Matt Slepin:

It's also hard because the CEO is the genius, and we know this in our business. The CEO is irreplaceable.

Chris Merrill:

Not me. I'm not the genius. Not at all. I've got got geniuses on the team here that are amazing. It's been fun. And again, the past few years have been challenging and it's really been rolling up the sleeves. I say to them all the time, you realize who do you want to be in a foxhole with? And I love some of the partners around here.

Matt Slepin:

Two last questions in this. One is in this exact marketplace right now, which is a challenge. Marketplace, transaction volume is really slow and closed in large part. What are you doing now and what are you doing now to prepare for what's going to come next? And what do you think's going to come next?

Chris Merrill:

So I love this environment right now for us to invest. I feel like we've got huge, huge tailwinds because what's happening is demographics are not changing. Enrollments are up at university. The aging population and supply is just choked off. And so we're seeing huge, huge tailwinds, huge opportunities. So we're not investing as much as maybe two years ago, but we probably made 13, 14 billion in new investments last year. And so we're very excited. Working with public to private partnerships with universities, our clean energy business, our digital business and data.

And so when you go through each of our sectors right now, you just get really fired up that there's great tailwinds because a lot of our competitions on the sidelines, they're facing a lot of headwinds with the economy, et cetera. So our asset classes can support a little bit higher interest costs with some of the interest rate rises because probably 60, 70% of what we do is assets we can reprice. And so with inflation, we've been able to reprice our assets. So the economics have been good.

So look, and I think what happens is there's going to be more and more continued interest in our asset classes. So if we just stay the course, high quality, great assets deal by deal, build portfolios, there's going to be a lot of demand over the next few years. I think the recovery's going to be a little bit tougher, maybe a harder landing than people think, but I think interest rates are going to get to a level here where maybe one or two more increases and then should level off. But I just want to follow these demographics and great demand and then do it in a way where we're not over-leveraging the assets. We try and fix our rates, do those sorts of things. That long game will pay off for us and our investors.

Matt Slepin:

Yeah. It's interesting, the long game. If you talk to someone who doesn't know who they are, when they hit really choppy seas like this, the who am I really comes up because you got to go figure it out. If you know who you are and you just keep your eye on the horizon and keep going in your direction, particularly when you have a thesis as strong as yours, then choppy times are just fine because you're going to get through them. You have lots of capital and you have businesses that make ultimate sense.

Chris Merrill:

Yeah, and that's what I said. I said to the company and at a town hall meeting, I said, "Listen, we're very lucky. I'm standing here telling you we don't have to change our strategy." Many firms are out there saying, "Okay. What the heck do we do now?" I said, "Our strategy is solid for the next 20 years. Okay. Now how do we just get better at it? And how do we keep thinking about innovation and differentiation? Because more and more people are going to come in and compete with us." So that's fun, is I can say, "Look it. We don't have to change our strategy. Let's just keep executing."

Matt Slepin:

Beautiful. Okay. Last question on Leading Voices is always your advice for a young person getting into the real estate business.

Chris Merrill:

It's interesting. I do this. I sit with our interns and our first year analysts a lot, and I try and just use that word, patience. Real estate can be a great career, but if you're going to go benchmark this to your friends who are in technology and it's just different. This is a career where you put your time in. It's about repetition. It's about seeing how transactions get done. Your value becomes seeing more and more transactions, learning lessons. So I said, "Look, if this is a career and a business you want to be in, and I think it's a great career and I think it's a great business, you just got to be patient. Put your head down. Be part of a good organization and just listen and soak it up but just be patient."

Matt Slepin:

It's wonderful advice. It's interesting. As I think about it, when I started in recruiting, people would say to me, "Hey, I don't want to just do multi-family. I don't want to just do industrial because I like doing everything. I think there's safety in diversification." And I always look at those people and say, "You're nuts." Because I think most people that I know have been really successful in a niche. Now you're in niches of niches.

And then the other thing that I think is really true in the long game, which you just talked about, besides repetition, is relationships. And I think in niches, repetition and relationships become even more important. And those people went into technology businesses or the healthcare generalist business outside of real estate, relationships don't mean as much.

Chris Merrill:

Yeah. For sure. [inaudible 00:59:52].

Matt Slepin:

Repetition might, and then in niches, relationships can become huge, much huger than it is in the big world.

Chris Merrill:

Huge, huge, huge because that's what the value is. If you do one deal with a partner, that's a failure. The idea is let's go do a lot together, build relationships. That's the part of the business I really enjoy. How can you do things with partners where I love surprising and where, okay, tough times, we could go structure deals and we could hammer them, but no, let's not. Let's help them be successful too, and then we'll all be successful together.

Matt Slepin:

Cool. Huge number of lessons in this conversation. I've really enjoyed this. So Chris, thank you so much for being on Leading Voices.

Chris Merrill:

It's been fun.

Matt Slepin:

I hope that you enjoyed today's episode. Please remember, if you're enjoying Leading Voices to share an episode with a friend or get them to subscribe. If they're podcast weary and not sure how to find and subscribe on their phone, go ahead and take their phone in your hand and subscribe for them and add another few of your favorite podcasts to their list to get them started. They'll thank you for it.

You can also find episodes of the show on our website, which you can find at zrgpartners.com/leadingvoices. And if you have comments or discussion about this episode, or Leading Voices in general, or if you're seeking help in real estate human capital solutions, recruiting or consulting especially, please contact me at mslepin@zrgpartners.com. Thanks for being a listener to Leading Voices.