HANDS-ON INSTITUTIONAL INVESTOR

Kayne Anderson's Al Rabil is a former student housing developer turned investment banker, turned institutional investor. For him, the real deal is about doing business the right way.

Interview by Richard Kelley and Randall Shearin

Student Housing Business recently visited with Al Rabil, managing director of Kayne Anderson Real Estate Advisors, at the company's offices in Armonk, New York. Kayne Anderson has been an active investor in the student housing sector, known for its hands-on approach to investment. The company has been quietly making news this year by marketing a large portfolio of student housing assets for sale. It has also been a steadfast partner with entrepreneurial developers and an acquirer of top student housing assets for several years, with no plans to stop anytime soon, as *SHB* discovered when it visited in early June.

SHB: Let's start with the biggest news: Kayne is selling a large portion of its portfolio. Tell us about that and why you are selling?
Rabil: We have 32 properties for sale. We received the first bids last week; we're at a best and final rebate process now. The properties are well over $1 billion dollars in asset value. We've been very pleased with the market's reception, though not surprised. A lot of our strategy has always been to consolidate within the sector and then sell as a package because we think there are different valuation metrics for an individual asset versus a large portfolio. This will be the largest deal in the industry since ACC-GMH and, for obvious reasons, we're excited about it. There's no gun to our head to sell. So we'll either be very happy about the sale, or we won't be selling.

SHB: What was the process and the mindset to sell at this time? How did you choose the properties?
Rabil: The properties are every student housing property we owned as of March 1, 2012. It's all 22 student housing properties in Fund 1 and it's the 10 assets we owned as of March 1, 2012, from Fund 2. We now own additional assets as we continue to buy. There was no picking and choosing; it was basically the entire portfolio. In terms of the timing, it's definitely earlier than we thought we would be selling anything. There are a number of reasons for that: institutional interest, a lot of unsolicited inquiry, low interest rates and economic uncertainty in the world. If we can get a price we're happy with at this time, it may or may not prove to be the highest and best price we could get, but given everything going on, we think it's a good time to take some money off the table. We will continue to invest so it's not a strategic exit from the sector. The sale represents a little more than 25 percent of the equity commitments for Fund 2. So, 75 percent of Fund 2 is still there and we're still allocating. We would expect to have a portfolio from a valuation perspective bigger than the one we're selling within 12 months.

SHB: The size of this deal means that there are only a limited pool of buyers out there who can do such a deal. What's the strategy there versus breaking it up in chunks of five or 10 properties?
Rabil: It's a limited buyer pool, but it's not as limited as you might initially think. You have a fair number of institutional investors aligning with student housing players. The thought process is that you are going to achieve a higher valuation on consolidation. Looking at some publicly traded REITs, institutional investors and larger players, they may like student housing, but given that it's a niche sector and the average transaction value is small, how do they achieve critical mass? Here's critical mass. I don't think you need 20 bidders to have it make sense, you just need one or more highly motivated bidders to have it make sense. And that exists.

AL RABIL
Managing Partner
Kayne Anderson
Real Estate Advisors

SHB: And it's definitely going to go all together?
Rabil: I always hesitate to say definitely, so it's not definite that the sale is going to happen. However, I would say there's a very high probability. All of the partial bids from the first round, we said, no thank you; we're selling as a portfolio. We're not even looking at you unless you're interested in buying on a portfolio basis. It's safe to assume it will be done on a portfolio basis but it's done when it's done.

SHB: Who's helping you facilitate this process?
Rabil: Bank of America Merrill Lynch is our advisor. They know people and they're the most active on the investment banking side within the space. The represented ACC in their acquisition of GMH and they've been a lead underwriter for ACC and EdR on numerous offerings; they know the student housing space so we felt they were the best pick after interviewing numerous investment banks. We're going with an investment bank, not a property broker, because there are number of structuring options, and even 'go public' options that exist for the portfolio. It goes well beyond 'here's a group of assets; what's your bid.' We're looking at maximized value, but there are issues that enter in that are outside of the scope of just price.

SHB: What do you see going forward? What are your acquisition goals for the rest of 2012 and beyond?
Rabil: We don't really set goals in terms of dollars placed or transaction volume. We're not motivated by how quickly or slowly we're deploying the capital; we're motivated by achieving very high-risk adjusted returns. Unlike most private equity funds, we are more than 10 percent of our own equity capital in these funds so we back it up by putting our money where our mouths are. We'll get it out faster rather than slower if we see deals that make sense. We've got strong underwriting criteria and we stick to that. What we do see is increasing recurring volume from strategic partners. Understanding the market is understanding the business: bringing capital, bringing solutions, acting entrepreneurially, doing things in time frames other people can't, that's where our acquisition talent lies. We have a host of transactions right now, all of

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which present difficulties and have extremely short time frames. We're all sitting here, arm to arm with our developer partners, problem-solving and saying there's no one else who would do this — meaning no one else would spend the time and take appropriate risks. If there's a timing concern on funding, we have taken down land for our partners with a guarantee from them just because it's a liquidity issue. What that has led to is very strong loyalty from people that we're doing business with. It goes beyond them liking us; it's what we bring to the table.

SHB: Give us an example of that.
Rabil: One very specific example is this: we're a select sponsor with Freddie Mac, and Frank [Duemmler, KAREA's chief investment officer] has spent five years building relationships, primarily through transparency, attention to detail and intelligence, which he's bringing to the table more than our competitors. That doesn't give us better pricing than anyone else, but it has given us structural flexibility and deal priority. One of the things that we can do for our developers and potential partners is early rate lock on development deals seven to 10 months prior to construction completion. As long as we're involved, based on our backing, Freddie Mac is willing to forward rate lock for us. With rates where they are today, reducing interest rate risk from the development process is a huge benefit. A lot of our business for 2012 is booked, a fair number of 2013 is as well. In some cases, we are acquiring existing assets, in others we are developing. In most development transactions there is a buyout option in which upon completion, we can take our developer partner out of the deal.

SHB: How do you structure those buyout deals?
Rabil: In some cases now, we're simply the takeout, we're just doing a forward buyout for September 2013 with agreed upon metrics with adjustments for actual in place rents, interest rates, and real estate taxes. We'll agree on the metrics, but we're not going to take the risk that the real estate tax assessment is double what our projections are. No reason to argue about it; let's just come up with a formula, so we're buying you at X cap rate and adjusting for every dollar that we're losing in operating income to real estate taxes, increased interest rates, or rents that aren't there, there's just a multiplier effect where you're reducing the purchase price. What we've got at this point is a strong recurring bulk of business and the number of strategic relationships that we have continues to increase, but it's not starting at ground zero. Right now, we're doing $1 billion gross per annum without having to go out and find it. We're just responding to our partners essentially and doing recurring business. I don't know the statistics, but we probably account for approximately 25 percent of the overall deal volume of this sector. A lot of that is because we play in larger properties, so certainly not on a property level basis.

SHB: Where do you see Kayne Anderson in the industry? Where do you see yourself falling within the spectrum?
Rabil: I leave the definitions to others. What we try to say is: tell us what you need and we'll structure around that. We've sat in the shoes of people that we do business with. I was an investment banker for 15 years but then I had two of my own companies in student housing prior to joining Kayne Anderson, so I was doing exactly what the entrepreneurial developers we work with are doing. I was using my own capital, building a portfolio of student housing. Adam Hird, who is our head of acquisitions, was an engineer initially then an architect, then a developer for 11 years. Craig Zogby was a developer with United for seven years before joining us. Marco Cedrone on our asset management side was a site superintendent for Bovis for eight years. I'm not trying to bore you with résumés, but that's not your typical private equity shop. When we're dealing with a development deal, we're actually looking at plans and the specs, giving input and insight, saying how are we going to react to change, not act like an institutional venture partner. We've been on the other side of the table so we know how it works. What I think we really bring to the table is trying to make other people's lives easier. When you shake hands

Al Rabil (left), managing director of Kayne Anderson Real Estate Advisors, and Frank Duemmler, KAREA's chief investment officer.

with us, you don't have to worry, we're not going to come on day 29 of a 30-day period and say the deal's changed. Our MO is we do what we say and we say what we do. I'd rather take a hit on that basis, but build credibility. It sounds cliché but we don't want to just make money, we want to do business the right way. Life's too short. We've all been around. We want to deal with the right people. It doesn't matter what the economics are if it's not the right people. I love this group and the team here. It's fun for them and for me to come into work every day. That's how I want my life. I want financial gain to be the result that happens when you're not thinking about it. When I was an investment banker, I knew that anytime I started worrying about how much money I was or was not making, personally, that I was not happy. That's not where your mind goes when you're having fun. Your mind goes to creating value, doing things that make sense, and you make money as a result. If you're asking how much you're making, you're just doing time.

SHB: How does your unit operate within Kayne Anderson?
Rabil: Kayne is about a $15 billion company today. It was about $8 billion when I joined five years ago. It has publicly traded closed-end funds that are focused on the energy sector. It has hedge funds that are focused on all aspects of the energy sector. And there's private equity, which accounts for approximately 35 percent of Kayne; there are four private equity platforms. There is an energy platform which is in the midst of raising its sixth fund now; it's been incredibly successful and has been the driver of the PE side to some extent. We are leveraging off of their success. Real estate is the private equity platform I run. There's also a middle market credit platform, which focuses on $20 million to $100 million mezzanine deals; deals that are too small for the Blackstones and KKRs of the world and too big for some of the smaller players. We've got Kayne Partners Fund, which is the growth private equity group of Kayne Anderson. Kayne Partners Fund generally invests via preferred equity/non-controlling stakes in companies that have $5 million to $150 million in EBITDA. These are established companies that are making money, but fall into the capital markets no man's land. Most of Kayne's businesses are focused on middle market sectors and exploiting opportunities where you can have a knowledge advantage and a capital advantage, which is why Kayne is interested in student housing. They looked at the space and concluded that there are not a lot of well capitalized companies and/or proficient specialized operators. You're not competing everyday with the best and the brightest; not because it's not a great sector, but because the large players just can't allocate enough capital to the space to make it worthwhile.

SHB: How do you see competition in the student housing space?
Rabil: I don't think for what we do, we're really looking at a lot of new

competition rushing in. I have to explain this to investors. As markets have rebounded and people see returns, they look at numbers from 2008 and say student housing is recession resistant, why isn't there more competition? Because the size of the total market is $300 billion, plus or minus. If you are a large institutional investor, you may love the idea of student housing, but you've got to find a home for billions of dollars. You can't do it in student housing. That's the good news and the bad news. The good news is the competitive advantage. The bad news is in the exit, because your cap rates are obviously wide of where multifamily and other more capital extensive spaces trade. That gap is wide and has been narrowed at different times. But like anything else, returns to a large extent are based on your entry point, the price you're paying and your expertise. Players who've gotten hurt in student housing, nine out of 10 times it comes from price paid. If you paid 30 percent too much, you have a good chance of losing even if you have property that's 99 percent occupied and getting great rates. We love the space; we're very bearish on the global economy, and we're generally bearish on the U.S. economy, but very bullish on student housing.

SHB: Going back to your student strategy, would you look at private schools?

Rabil: We've done deals at two private schools, one last year at the University of Southern California and one at the University of Rochester. However, our primary focus remains public universities.

SHB: How should someone approach you who has never done business with you before or think they can't get involved with private equity?

Rabil: That's easy, call us. There's no one who isn't available. Private equity is just a name. What we try to do is figure out what our partners need. We have a saying, 'A quick no is the next best thing to a yes.' We are accessible. We never suffer from thinking we're too big or too good. We respond to everyone. We're focused on larger deals, so it's not solely about the return, it's about efficiency of execution and what is our size at this point. We love what we do and we are not planning on going anywhere. I think one of the neat things about this place is that we all want this to be our last stop. I'm not looking for what's the next thing, I'm looking for now. We may expand what we do and morph in time depending on how the world changes, but I love being at Kayne Anderson; I love what we're doing, and this team; and I love coming into work. That's why we built this place. Let's get a bunch of like-minded people where we don't have employees; we're partners. We want to grow the pie and be a part of it. We want people to be motivated and excited about what they're doing every day. It sounds like Management 101, but it's true. I've never understood anyone who says 'I never sell.' Why would that be? I'll buy at the right price, and sell at the right price. Always. Everything I have is for sale, always, anytime. It's about the entry and exit price. If someone offers twice what I think it's worth, I'm a seller. Don't fall in love with the real estate. It's an asset and produces a yield and a return and that's it. We plan on being a big part of the student housing space for a long time and hopefully we will be. **SHB**

Kayne Anderson acquired West 27th Place, an off-campus property at the University of Southern California in Los Angeles last year. The property holds the distinction of being the first student housing project to achieve LEED Platinum certification. The complex has 392 beds in 161 units.

Kayne Anderson acquired The Province, located a half-mile from the University of Louisville campus in May 2010. The 858-bed, 366-unit property was built in 2008.