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Global Investors Pour Billions Into Hudson Yards in Major Bull Market Bet

Much of the capital behind the mixed-use project on Manhattan's far west side is foreign

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Architect A. Eugene Kohn recalls touring a windswept rail yard on Manhattan's far west side in 2005 and being doubtful about its potential for commercial development.

"Who in the world would want to live over here or work over here," Mr. Kohn, whose firm went on to become the master planner of the site, recalled thinking at the time. "Who is going to put the money up?"

Last month, lead developer Related Cos. took another big step toward answering those questions by announcing it had completed the $3.8 billion financing of 50 Hudson Yards, what will be the development's biggest tower.

The deal increased to $18 billion the total amount of equity and debt raised for the first seven buildings in the proj-

ect, the first phase of which spans several blocks from West 30th to West 34th streets between 10th and 11th avenues. The anchor tenant for 50 Hudson Yards, asset manager BlackRock Inc., is the latest blue-chip firm to agree to move to the 28-acre development.

Meanwhile, the capital sources for the development that is rising like a new Manhattan mountain range reads like a who's-who list of big-name global financial institutions.

The roster speaks volumes about the sources of capital for megaprojects at what seems to be a late stage in a lengthy bull market in commercial real estate.

For starters, most of the debt and equity capital sources are from overseas. U.S. banks Wells Fargo & Co. and Bank of America Corp. were the lead banks on the construction financing for two of the seven buildings in the first phase of development. But foreign lenders from 11 countries have provided the bulk of the debt. The list includes Deutsche Bank AG , Bank of China Ltd. , HSBC Holdings PLC, Credit Agricole SA and Children's Investment Fund of the U.K.

U.S. banks have been more wary than foreign institutions of construction financing since the 2008 financial crisis. "With all the regulatory burdens on U.S. banks these days, they are very cautious about having too much commercial real estate exposure," said Jeff Blau, Related's chief executive.

Foreign banks held $71.6 billion in loans backed by U.S. commercial real estate at the end of the second quarter of this year, according to debt tracker Trepp LLC. That is up from $59.3 billion at the same time in 2016 and $38.3 billion in the second quarter of 2015, Trepp said.

Much of the equity capital for Hudson Yards also is coming from foreign investors, with the exception mostly of Related and some of the project's tenants that have bought their spaces, like Time Warner Inc. and KKR & Co. For example, Related's main partner on the project is Oxford Properties Group, the real estate investor for OMERS, one of Canada's largest municipal pension plans.

The other equity investor in 50 Hudson Yards is the U.S. unit of Mitsui Fudosan Co. , one of Japan's largest real estate companies. Mitsui also provided the lion's share of the equity for 55 Hudson Yards, an office tower under development where tenants will include hedge fund Third Point LLC and law firm Cooley LLP.

The lopsided participation of foreign investors partly reflects the appeal of the U.S. as a haven for investments and of construction projects as a source of higher yield in a low-interest-rate world. Some major financial institutions, like

Oxford, have been active investors globally because their home markets are too small to provide enough opportunity.

“You can very quickly grow out of Canada,” said Blake Hutcheson, Oxford Properties Group’s chief executive. “Most of our growth has been in foreign markets.”

Also, some of the traditional U.S. providers of equity capital in real estate development, like some pension funds, have had less of an appetite for such risk after getting clobbered during the last recession.

“They had to write down a lot of those assets,” said Chris Ludeman, global president of capital markets at CBRE Group Inc.

Overall, foreign appetite for U.S. commercial property has increased during this decade. In the second quarter of 2017, Canadian investors purchased $4.1 billion of property, up 39% from the same period last year, according to data firm Real Capital Analytics Inc.

Investors outside of North America accounted for close to $50 billion in deals in the first quarter. Those represented 13% of all U.S. transaction volume by midyear 2017, down from 16% one year earlier, but still above the 10% hit at the end of 2014, Real Capital said.

Analysts said the high foreign participation in projects like Hudson Yards could be a sign that a downturn isn’t imminent. It shows “an increased confidence that the business cycle is not likely to roll over and therefore the underlying economics of projects like these remains viable,” said Larry Hatheway, chief economist of GAM Holding AG , a global asset management firm.

Of course, the high level of recent foreign investment in the U.S. could be a danger sign. Japanese investors infamously purchased Rockefeller Center and other trophy U.S. assets just before the commercial property market collapsed in the recession of the early 1990s.

Still, many don’t think a sharp downturn is on the horizon. John Macomber, a senior lecturer at Harvard Business School, points out that the market hasn’t seen the kinds of surge in leverage or new supply that often precedes a downturn. “I don’t see a huge systemic correction,” he said in an email.

But he also added: “Of course, I didn’t see 2008 coming either.”