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Real Estate Fund Terms and Conditions

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Real Estate Fund Terms and Conditions: Fluctuating Fees?

As a result of the slow fundraising market, there has undoubtedly been a change in the balance of negotiating power from General Partners (GPs) towards Limited Partners (LPs), which has precipitated shifts in certain areas of fund terms and conditions.

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All the latest news on real estate investors:

Including...

- Ohio Public Employees' Retirement System
- VersAM
- Case Western Reserve University Endowment

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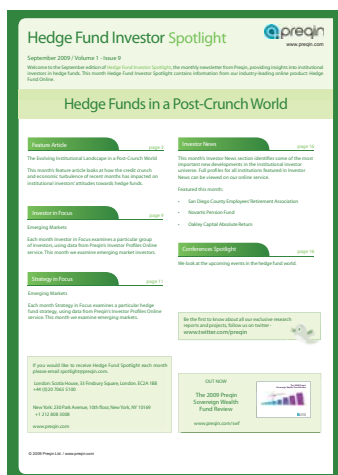


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Real Estate Fund Terms and Conditions: Fluctuating Fees?

There has been a significant fall in the number and aggregate value of funds successfully raised in the private equity real estate market since the onset of the global economic downturn. Fig. 1 demonstrates how significant this decline has been, with just \$48.3 billion being raised in 2009, compared with \$136.7 billion in 2008. Investors that are making new commitments are carrying out even greater due diligence on potential investments and this extends to the terms and conditions of funds they are considering investing in. As a result of the slow fundraising market, there has undoubtedly been a change in the balance of negotiating power from General Partners (GPs) towards Limited Partners (LPs), which has precipitated shifts in certain areas of fund terms and conditions. Using data taken from our newly released publication, the 2010 Preqin Fund Terms Advisor, this month's feature article examines some of the key trends in this important area.

Management Fees

The management fee during the investment period is generally calculated as a percentage of the total commitments made by LPs to the fund. The rationale

behind this is that the major part of the GP's workload at this stage is the search for potential investments, which is driven by the aggregate size of commitments to the fund and not the amount invested at this point in the fund's life.

Fig. 2 shows the split of management fees charged during the investment period by real estate funds with a 2009 or 2010 vintage, or those still raising capital as of Q2 2010. Nearly half of all such funds have a management fee of 1.50-1.74%, and nearly a quarter have a fee of 2.00-2.24%. Just over one-tenth of funds have a 1.75-1.99% management fee, and 12% use a rate of 1.00-1.24%.

While the largest proportion of private equity real estate funds charge a management fee of between 1.50-1.74%, which is generally considered to be the industry standard, there has been some movement in the fees charged by the largest funds. Fig. 3 shows that the largest real estate funds of the most recent vintages have had significantly lower average management fees than vintage 2007 and 2008 funds. The mean management fee for vintage 2010 funds

(including those still fundraising and yet to begin investing as of Q2 2010) of \$1 billion or more in size is 1.25%.

Managers of the larger funds are most likely to be in a position to reduce management fees, or to have come under pressure to do so from investors because of the economies of scale involved. A firm that raises a \$1 billion fund is unlikely to have twice the costs in terms of wages and other expenses that a firm managing a \$500 million fund does. It is clear that for these funds, there has been a shift in the balance of negotiating power towards LPs. For funds under \$1 billion however, there has been very little movement in management fees. Funds which raised under \$500 million have a mean management fee of just over 1.6% for 2008, 2009 and 2010 vintage years, while funds which fall into the \$500-\$999 million bracket, have management fees just under the 1.6% mark.

Performance Fees

The performance fees charged by private equity real estate funds are in the form of carried interest. The carried interest charged by funds shows little variation, with

Fig. 1:

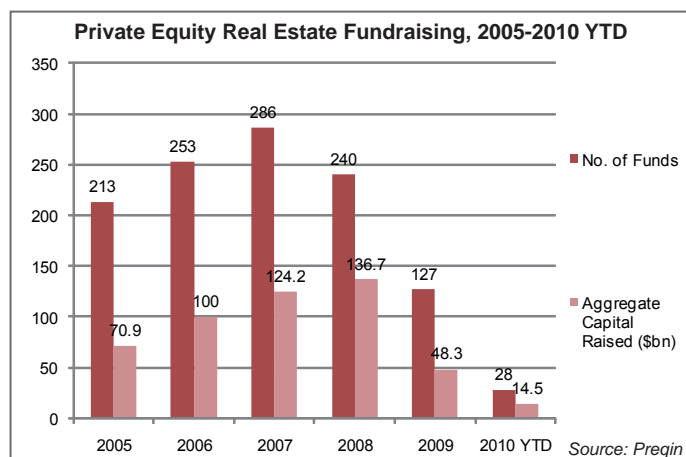
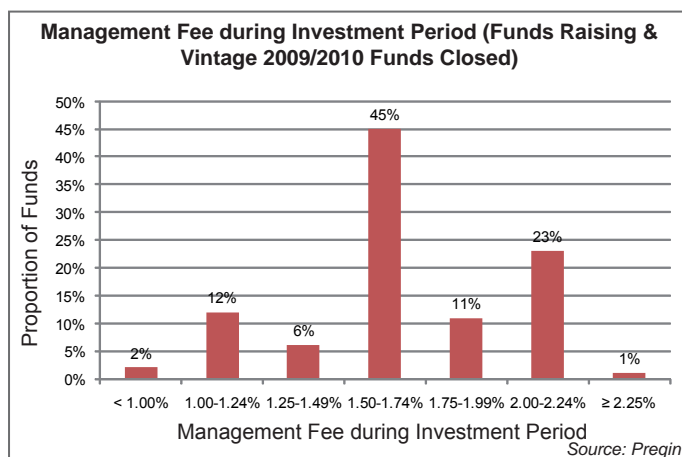


Fig. 2:



91% of private equity real estate funds in market or with 2009 or 2010 vintage years charging 20% carried interest. Where there may be a shift however is in the hurdle rate (or preferred return), the threshold after which GPs start earning carried interest. As Fig. 4 shows, real estate funds with a 2008 vintage have the lowest average hurdle rate of all real estate fund vintages considered, with a mean of 8.55% and a median of 8%. The median hurdle rate has since moved back up to 9% for vintages 2009 and 2010. Interestingly, the hurdle rate moved in favour of the GP for funds of 2008 vintage, but has subsequently moved back to similar levels to funds of 2006 vintage. It may be that GPs adjusted their return targets and hurdle rates in line with declining property prices. The recent shift in negotiating power towards the LP however, has resulted in hurdle rates increasing for funds of 2009 and 2010 vintages.

Conclusions

Preqin data clearly demonstrates that the difficult fundraising environment has resulted in a change in the terms of private equity real estate funds. Fund managers that have recently launched funds have responded to LP calls for a change in fund terms. The largest funds have reduced management fees and hurdle rates have increased for funds of more recent vintages. With the private equity real estate fundraising market remaining very competitive, LPs will continue to wield influence when negotiating fund terms. Additionally, with increased investor interest in the range of fund terms, it is more important than ever to ensure that all proposed fund terms, not just the headline management fee and carried interest rates, are aligned with the latest industry standards.

Andrew Moylan & Sam Meakin

Fig. 3:

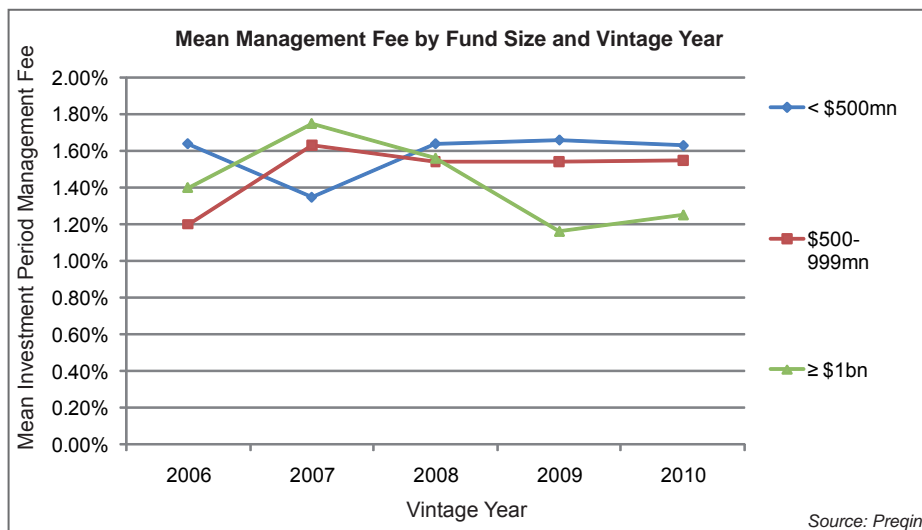
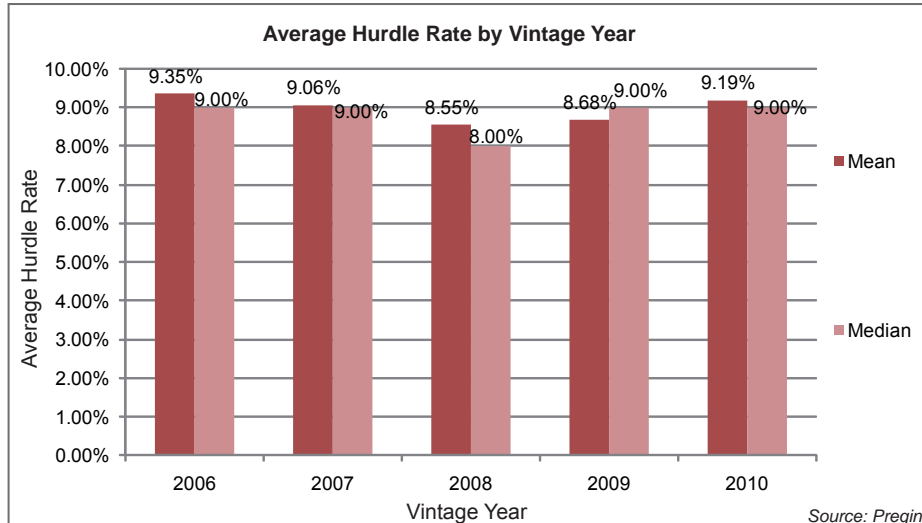


Fig. 4:



The information contained within this article is based on data from [The 2010 Preqin Fund Terms Advisor](#)

For more information, sample pages and details on how to order your copy, please visit:

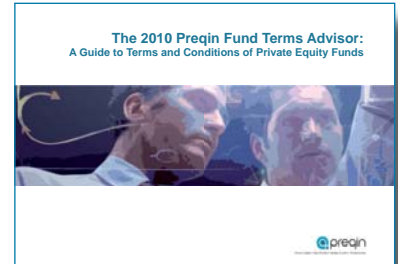
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2010 Preqin Fund Terms Advisor: Order Form

The Fund Terms Advisor is a vital tool for all fund formation lawyers and for private equity firms and placement agents involved with the fund formation process. It also contains valuable intelligence for all those investing in private equity, and for those advising LPs. Key features include:

- Actual terms and conditions data for over 1,400 funds, including management fees and mechanisms for reduction after the investment period, carry, carry distribution methods, hurdles, preferred return, fee rebates, no-fault divorce clause, GP commitments, investment period.
- Benchmark terms and conditions data for funds of all different types: buyout, venture, real estate, distressed, mezzanine, fund of funds, secondaries and more...
- Results of our LP and placement agent surveys - the most comprehensive studies of current opinions on fund terms and conditions ever conducted.
- Data and analysis on the actual fees and costs incurred by LPs, with listings showing costs for 1,200 named vehicles.
- Full access to our updated Fund Terms Advisor Online product, which enables you to model the real economic impact of fund terms and conditions, and download detailed fund terms for further analysis.
- Comprehensive analysis on all aspects of private equity fund terms and conditions including how conditions have changed over time and what variations exist amongst funds of different type, size and region.
- Listings for 100 leading law firms involved in the fund formation process, including contact details and sample previous assignments.



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Fundraising Spotlight

Fig. 1:

Funds on the Road				
	North America	Europe	ROW	Total
Number of Funds	218	102	77	397
Aggregate Target Size (\$bn)	75.7	35.2	27.6	138.4
Average Target Size (\$mn)	366	395	399	379

Source: Preqin

Fig. 2:

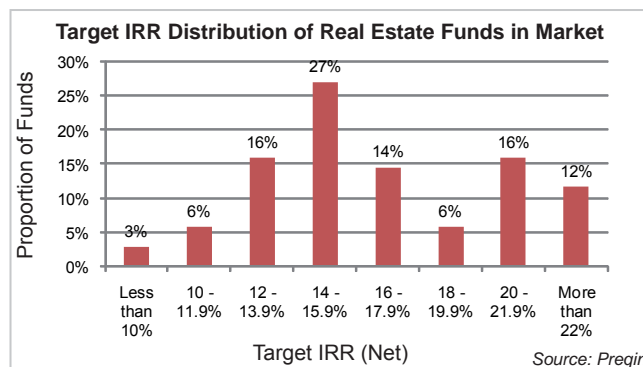


Fig. 3:

10 Largest Primarily Europe-Focused Real Estate Funds on the Road			
Fund	Manager	Target Size (mn)	Strategy
Meyer Bergman European Retail Partners	Meyer Bergman	600 EUR	Debt, Distressed, Opportunistic and Value Added
ING REIM European Shopping Centre Fund	ING Real Estate Investment Management	750 EUR	Core-Plus
LaSalle European Ventures III	LaSalle Investment Management	750 EUR	Opportunistic
Moor Park Real Estate Fund III	Moor Park Capital Partners	700 EUR	Opportunistic
Duet European Real Estate Debt Fund	Duet Private Equity	500 GBP	Debt
Legal & General Limited Price Inflation Income Property Fund	Legal & General Property	500 GBP	Opportunistic
Pramerica Real Estate EuroMezz Fund I	Pramerica Real Estate Investors	500 GBP	Debt
Aberdeen European Shopping Property Fund	Aberdeen Property Investors	525 EUR	Core-Plus and Value Added
NCH New Europe Property Fund II	NCH Capital	700 USD	Distressed
The Avingstone Fund	Avingstone	500.0 EUR	Distressed

Source: Preqin

Recently Closed Funds:

Fortress Japan Opportunity Fund

Manager: Fortress Investment Group
Strategy: Opportunistic, Distressed
Geographic Focus: Japan
Final Close (mn): 75,000 JPY (Jun-2010)
Sample Investors: Ohio Police and Fire Pension Fund, Penn Square Real Estate Group

Rockspring UK Value Fund

Manager: Rockspring Property Investment Managers
Strategy: Core, Core-Plus, Value Added, Distressed
Property Types: Industrial, Office, Retail
Geographic Focus: UK
Target IRR (net): 13%
Final Close (mn): 336 GBP (Jun-2010)
Law Firm: Clifford Chance



Fund Manager Spotlight: UK-Based Fund Managers

Fig. 1:

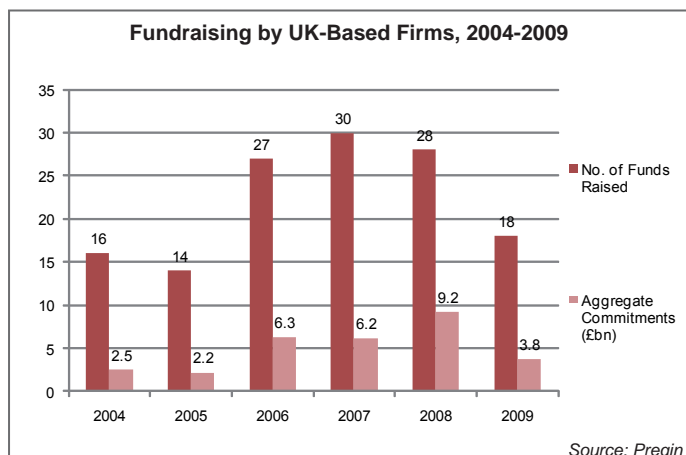


Fig. 2:

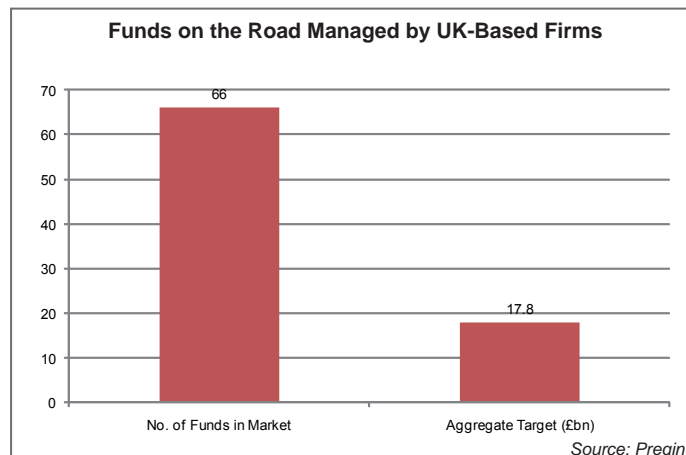


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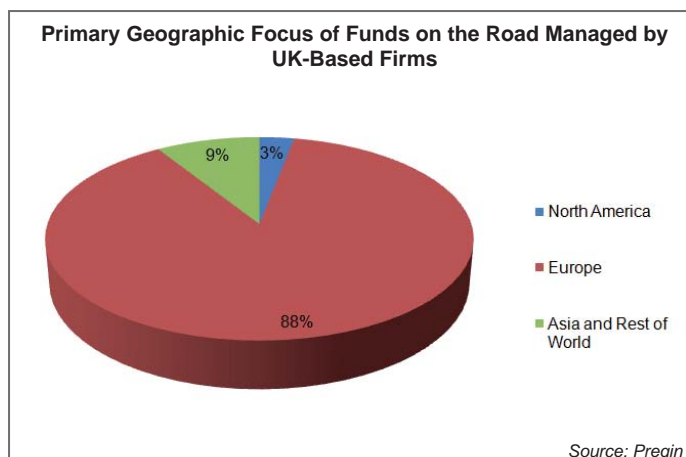


Fig. 4:

10 Largest UK-Based Firms by Capital Raised for Private Equity Real Estate Funds in the Last 10 Years

Firm	Total Capital Raised for Private Equity Real Estate Funds in Last 10 Years (£bn)
MGPA	5.2
Orion Capital Managers	2.0
Terra Firma Capital Partners	1.8
Resolution Property	1.2
Patron Capital	1.1
Highcross Strategic Advisers	1.1
HSBC Specialist Investments	1.0
Moorfield Group	0.8
Pradera Europe	0.8
Benson Elliot Capital Management	0.7

Source: Preqin

The information in Fund Manager Spotlight is taken from Preqin's Real Estate Online product. There are currently profiles for over 139 fund managers based in the UK.

To find out more information about this product, or to arrange a demo, please visit:

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Andrew Herman



Investor Spotlight: US Public Pension Funds

Fig. 1:

Key Facts: US Public Pension Funds	
Average Allocation to Real Estate	\$1,035mn (7.8% of Total Assets)
Average Target Allocation to Real Estate	\$1,496mn (8.6% of Total Assets)
Average Allocation to Private Real Estate	\$454mn (5.4% of Total Assets)

Source: Preqin

US-based public pension funds are major investors in private real estate funds and as of June 2010, the average real estate allocation of such an institution active in private real estate is \$1 billion. The average target allocation to real estate is approximately \$1.5 billion, while the average allocation to private property funds is \$454 million.

73% of US public pension funds that invest in private vehicles have total assets under management of less than \$10 billion. 20% have assets of \$10-49.9 billion and only 2% have over \$100 billion under management. In terms of overall allocations to real estate, 66% have less

than \$500 million invested in the asset class, 14% have between \$0.5-1 billion allocated to property, and 7% have real estate portfolios worth more than \$4 billion.

The most favoured fund strategies are value added and opportunistic, with 85% and 63% of US public pension plans committing to these vehicles respectively. Lower-risk core and core-plus funds are also very attractive to these investors, with 62% and 47% showing an interest in such strategies respectively. These

funds have recently grown in popularity due to the volatility and uncertainty in the market, with investors reasoning that such vehicles will provide some stability to their portfolios. Debt funds have also grown in prominence and half of all US pension funds investing in real estate have a preference for such vehicles.

In terms of geography, 99% of public pension funds active in private equity real estate invest in North America. The

Fig. 2:

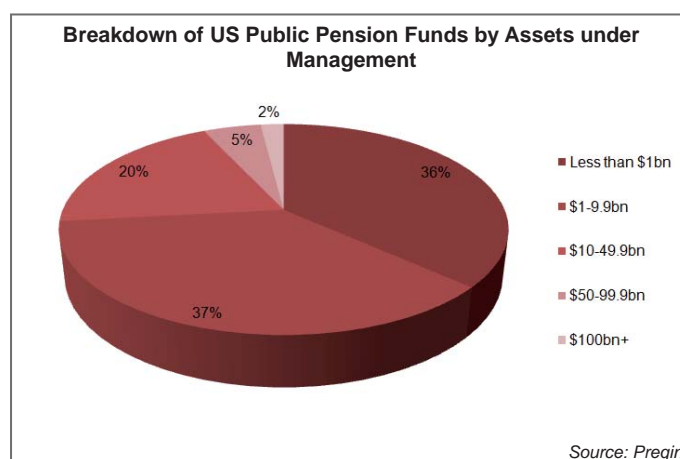


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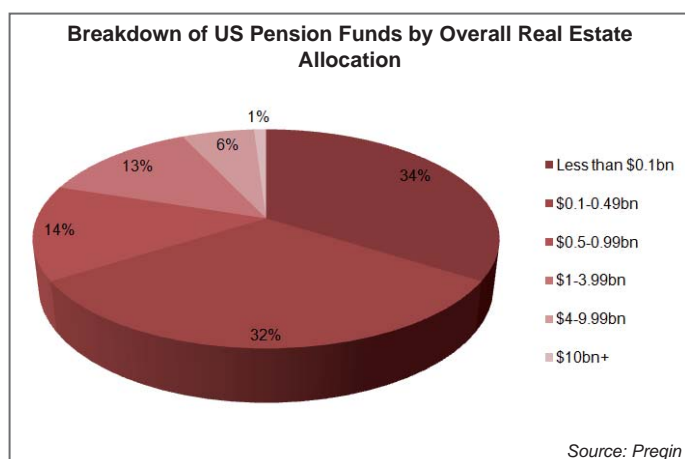


Fig. 4:

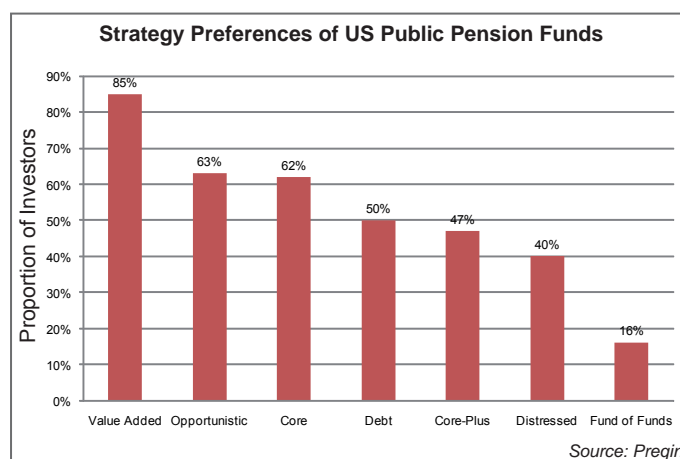
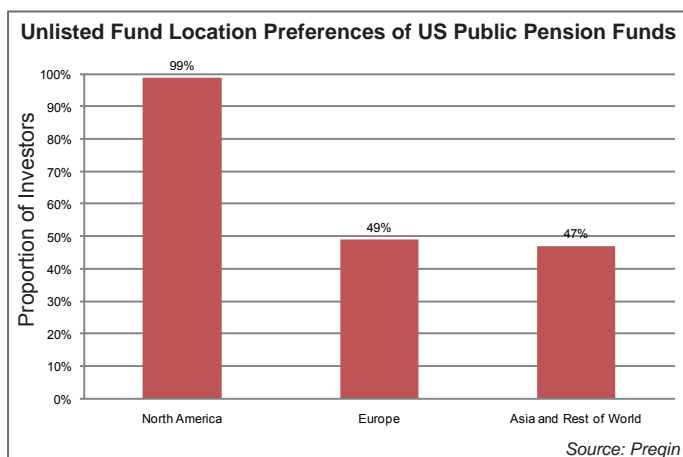


Fig. 5:



select few that do not commit to domestic funds may have direct property holdings in the US and only utilize funds to access international markets. 49% are interested in European markets and 47% in Asia and Rest of World funds.

Forena Akthar

The information in Investor Spotlight is taken from Real Estate Online. There are currently profiles for 300 US public pension funds with an active interest in real estate.

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Conferences Spotlight: Forthcoming Events

Conference	Dates	Location	Sponsor
Property Investment Conference 2010	29 - 30 July 2010	Cape Town	IPD
Malaysia REITs 2010	2 - 5 August 2010	Kuala Lumpur	Asia Business Forum
Real Estate Investment World Australia 2010	10 - 12 August 2010	Sydney	Terrapinn
3rd Distressed Commercial Real Estate EAST	13 - 15 September 2010	New York	Infocast
Real Asset Investing Forum	15 - 16 September 2010	San Francisco	Opal Financial Group
IPD RealWorld Conference	22 - 23 September 2010	Cambridge	IPD
The 2nd Annual Distressed Commercial Real Estate Forum	23 - 24 September 2010	New York	IMN
Expo Real 2010	4 - 6 October 2010	Munich	Messe Munchen
Real Estate Investment World Australia 2010	6 - 8 October 2010	Sydney	Terrapinn
CEE Real Estate 2010	14 October 2010	Warsaw	EastEuro Link
Real Estate Investment World Japan 2010	18 - 19 October 2010	Tokyo	Terrapinn
4th Real Estate Private Equity Summit	20 October 2010	New York	iGlobal Forum
Real Estate Investment World Latin America 2010	25 - 27 October 2010	Coral Gables, FL	Terrapinn
PERE Forum: New York	26 - 27 October 2010	New York	PEI Media
AIS 2010 Abu Dhabi Showcase of Alternative Investment Funds	3 - 4 November 2010	Abu Dhabi	Leoron Events
European Real Estate Opportunity & Private Fund Investing Forum	8 - 9 November 2010	London	IMN
Real Estate Investment World India 2010	22 - 24 November 2010	Mumbai	Terrapinn



Investor Spotlight: Investor News

Ohio Public Employees' Retirement System to invest USD 1 billion in real estate over next 12 months

The USD 70 billion pension plan intends to invest USD 1 billion in private real estate funds over the next 12 months. It aims to take advantage of the recent decline in real estate prices and adopt a more opportunistic approach to investments. It is currently deciding the types of funds it will invest in. The pension fund has already committed USD 1 billion to both open and closed-end funds this year. It allocated USD 300 million each to JP Morgan Strategic Property Fund and UBS Trumbull Property Fund, which are both open-ended funds. USD 200 million was also committed to Och-Ziff Real Estate Fund II and USD 200 million to a fund managed by Partners Group.

VersAM to commit to two core and core-plus funds by the end of the year

The EUR 38 billion asset manager is hoping to make two new commitments to private real estate funds utilizing core and core-plus strategies in the next six months. VersAM initially planned to commit to two or three funds in 2010, but has yet to invest in a single vehicle this year. It will invest in one European fund and one Asian fund, and these vehicles have already been selected. It has targeted core and core-plus vehicles because it feels that these offer a low-risk route to reduced property prices.

BVV not looking to invest in real estate in the next 18 months

The EUR 18.8 billion pension fund does not expect to add further investments to its real estate portfolio until the end of 2011. It has been inactive in the asset class since the onset of the financial crisis. BVV will analyze the market and discuss the most appropriate investment opportunities in Q4 2011. It is interested in investing in Asia and other European countries when it returns to the market, so that its portfolio is no longer restricted

to Germany. But, this will depend on its circumstances and the state of the real estate market closer to the time of its return. 99% of its real estate allocation is gained via vehicles that are specially established for BVV, pooled vehicles, club deals, closed-end funds and Spezialfonds.

Tennessee Consolidated Retirement System decides against core open-ended real estate funds

The USD 29.8 billion pension fund had considered allocating USD 200 million across two open-ended core real estate funds earlier this year, but it has decided not to commit to such vehicles. Its real estate advisor, Townsend Group, had recommended JP Morgan Strategic Property Fund and UBS Trumbull Property Fund back in March, when the pension plan decided to invest up to USD 1 billion in real estate in the next five years. The pension fund is not anticipating making any fund investments in the next 12 months.

Employees' Retirement System of Texas makes maiden commitments to private real estate funds

The USD 21.4 billion pension fund has made commitments to two real estate funds, gaining its maiden exposure to private funds. Employees' Retirement System of Texas has committed USD 100 million to the open-ended core vehicle LaSalle Property Fund, and USD 100 million to Cornerstone Core Mortgage Fund I, which makes core and debt investments. Both vehicles invest in the US. This is part of its plan to invest up to USD 2.1 billion in private real estate in the next four to five years and around USD 1 billion will be allocated to private vehicles over the course of 2010 and 2011. Even though it will invest in the US at first, it aims to gain exposure to property markets across the globe. It is interested in all fund types, including funds of funds to gain a diversified portfolio.

Case Western Reserve University Endowment to invest in two high-risk strategy funds in 2010

The USD 1.4 billion Case Western Reserve University Endowment is close to finalising a USD 20 million commitment to an opportunistic vehicle making investments in domestic property. The endowment, which has a target allocation to real estate of 11%, is currently under allocated to the asset class and is likely to make another USD 20 million commitment to a second high risk/return vehicle by the end of 2010. Case Western believes there are a variety of opportunities available in the current market and was interested in all fund strategies excluding fund of funds.

Forena Akthar

Each month Spotlight provides a selection of the recent news on institutional investors in real estate. More news and updates are available online for Real Estate Online subscribers.

In the last month, Preqin analysts have added 47 new investors and updated 369 existing investor profiles.

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