

# Preqin Research Report

## Investor Attitudes to the PERE Secondaries Market (1)

As a result of the global economic downturn investors have had to review their investment portfolios in light of more testing circumstances. The viability, strengths and weaknesses of holdings within real estate private equity portfolios have come under scrutiny from investors looking to circumvent, soften or even benefit from instability caused by the economic downturn. This has led to a dramatic increase in the number of investors seeking to both sell and also buy interests on the secondary private equity real estate market.

### Sellers

Many investors have been hit by the denominator effect. With stock portfolios falling, allocations to real estate private equity have risen without extra investments necessarily being made. Those badly affected by the economic crisis have had to consider their positions not only with regards to future real estate investments, but also in relation to their current investments and their committed but as yet uncalled capital liabilities. Some investors need to reduce their commitments to real estate in order to meet internal or external real estate allocation guidelines or regulations, with those investors employing overcommitment strategies having been hit especially hard.

Initially, many of those worst hit sought relief via redemptions on their open-ended real estate commitments, however a growing number of investors are now also interested in selling private equity real estate fund stakes on the secondary real estate market to gain some form of liquidity, possibly off-set allocation regulations and halt further call-ups. Investors are also using the secondary market to rebalance portfolios, and to free up capital to reinvest in new funds following strategies deemed more appropriate for the current climate such as distressed investing.

Preqin has identified an unprecedented level of interest in the sale of private equity real estate fund stakes. A recent Preqin survey shows that 23% of investors with commitments to closed-ended commingled funds are interested in selling some of their stakes to third party investors (see Fig. 1). Of those investors, 81% are sure they would sell if suitable offers were made for the remainder of certain stakes. The other 19% were considering selling on the secondary market.

As Fig. 2 highlights, real estate fund of funds managers are the most prevalent investor group seeking to sell fund stakes on the secondary market. This is largely due to a desire to rebalance portfolios rather than out of need to release capital. Asset managers are the second most prevalent investor group accounting for 19% of those looking to sell. As they represent other institutional investors it is likely that at least one of their clients is going to need to find capital or be released from call-up obligations in the current market. Kleinwort Benson

Private Bank is one such example. The asset manager sold a stake in a vehicle targeting the UK accommodation sector on the secondary market on behalf of a client earlier in the year as its client needed liquidity and the fund was not set to mature until 2012.

The remaining institutions looking to sell private equity real estate funds on the secondary market are fairly evenly spread by type. Insurance companies, investment companies and superannuation schemes each make up 8% of investors looking to sell on the secondary market. Endowments comprise 4% of investors seeking to sell to third party investors, as do family offices/foundations, public pension funds and private pension funds.

### Buying

Whilst some investors are looking to sell private equity real estate on the secondary market, others are looking to take advantage of this opportunity to pick up funds at discounted prices to the net asset value of portfolios. Furthermore, acquiring stakes on the secondary market can be appealing to investors as they are able to mitigate the effects of the J-curve. By acquiring interests in vehicles on the secondary market, buyers can receive access to older vintages, enabling newer entrants to the asset class to assemble a more balanced portfolio.

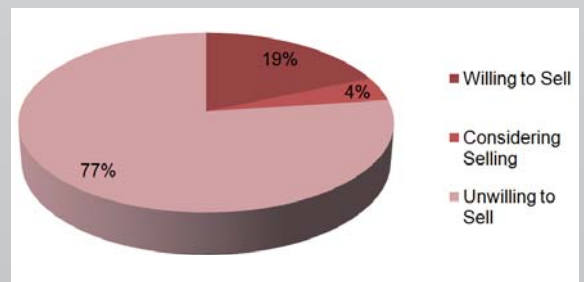
As seen in Fig. 3, 47% of those asked in a recent Preqin survey are interested in buying on the secondary market. Of that figure 85% expressed a clear desire to allocate to this strategy whilst 15% would consider doing so.

As with selling on the secondary market, buying is also the activity of a variety of investors. Interest is spread across the institutional spectrum. It would appear that this transaction is popular with those with liquidity and not specific to a particular type of investor.

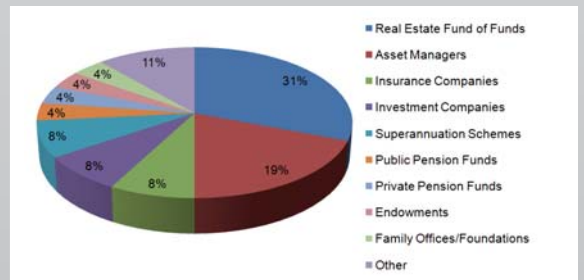
Just as with selling, the most prevalent investor type looking to buy on the secondary market is real estate fund of funds. Fig. 6 shows that public pension funds are the second biggest group interested in purchasing stakes with 14% of those willing to buy from this group. An example is the German public pension fund AEVWL. Although the pension fund has not yet bought a real estate fund on the secondary market, it believes opportunities exist in the current market to do so. It still wants to reach an unfulfilled target allocation and sees the secondary market as an excellent way to help achieve this at more favourable prices.

AEVWL like so many other interested buyers, views the secondary market opportunistically. It has not devised a particular strategy for purchasing from other investors. It is open to various geographies, fund strategies and even vintages and will consider funds on a case-by-case basis. In talking to a range of institutions, it is evident that investors

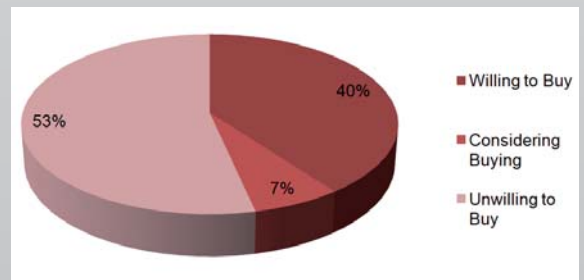
**Fig. 1:**  
**Investor Positions - Selling PE Real Estate Funds on the Secondary Market**



**Fig 2:**  
**Make-up of Investors Looking to Sell on the Secondary Market by Type**



**Fig. 3:**  
**Investor Positions - Buying PE Real Estate Funds on the Secondary Market**



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## Investor Attitudes to the PERE Secondaries Market (2)

of varying types have this case-by-case outlook on the secondary industry.

Again asset managers are high in the list of interested investors due to their representation of a variety of investors. They make up 9% of those with a firm interest in buying private equity real estate on the secondary market, as do endowments, and superannuation schemes. Insurance companies represent 7% of the total with examples of those interested including Gothaer Versicherungsbank, Liberty Mutual Insurance and Phoenix Insurance Company.

The US-based Employees' Retirement System of Texas is one such investor interested in buying on the secondary market. The USD 20 billion public pension has a 7.5% target allocation to real estate, but has only invested 1.5% in the asset class. Advised by RV Kuhns & Associates, Texas will look to acquire secondary fund stakes to help it get nearer to its target allocation.

### Fund of Funds and Secondary Specialists

Despite the recent growth in interest in the real estate secondary market from institutional investors, the secondary real estate market is still driven by those that make it their primary business to pursue secondary market investments. Five secondary real estate fund of funds managers dominate the secondary real estate scene. Belveron Real Estate Partners, CS Strategic Partners, Landmark Partners, Liquid Realty Partners and Madison International Realty have closed a combined USD 2.6 billion from investors across eight funds since 2005 to allocate to the secondary market.

Liquid Realty Partners have raised the most capital since 2005, committing a potential USD 1.5 billion to the secondary market from capital raised from other investors. It garnered this capital across three vehicles. The largest of these funds was Liquid Realty III, which raised USD 772 million. It has committed to UK Property Unit Trusts as well as Limited Partnerships on a secondary basis. Investors in the vehicle include CPP Investment Board, Virginia Retirement System and University of Michigan Endowment. Liquid Realty III is the largest secondary fund of funds to be closed in the real estate secondary market to date.

Four firms currently have a secondary real estate fund of funds in market. These vehicles are targeting a total of USD 2 billion. In addition Aviva Investors Real Estate Multi-Manager has announced that it will soon be raising a secondary real estate fund of funds. The biggest fund on the road is again a fund managed by Liquid. Liquid Realty Partners V is

seeking to raise USD 800 million from investors. The vehicle will acquire interests in real estate funds, partnerships and trusts globally. It considers a range of funds, including core, core-plus, value added and opportunistic vehicles. It will acquire between ten and thirty fund interests.

In addition to secondary specialists, other real estate fund of funds are also significant players in this market, with many firms in this space allocating a portion of their funds towards secondary deals, and many others using it to rebalance portfolios. They represent the most numerous investor group in regards to the secondary private equity real estate market both in terms of those looking to buy and looking to sell. 29% of potential buyers are real estate fund of funds and 31% of those looking to sell are real estate fund of funds.

In total, 42% of real estate fund of funds surveyed by Preqin are interested in selling on the secondary market, while 84% are looking to buy. Clearly secondary activity is an integral tool for fund of funds managers, as evidenced by the almost 50% that are looking to both buy and sell on the secondary market.

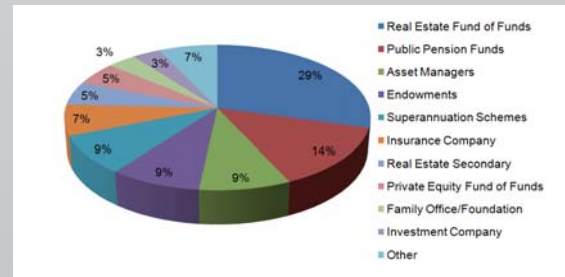
### All Talk and No Action?

As stated, there has been a fairly dramatic increase in the number of investors expressing clear interest in selling real estate fund stakes on the secondary market. With the number of interested buyers outweighing that of sellers, the potential for deals is significant. However, activity levels are some way behind interest levels, and this can be attributed to three main factors

- **Uncertainty:** with December 2008 valuations only just coming through, potential buyers and sellers are still uncertain as to whether the large discounts on historic NAVs will represent good value relative to NAVs later in 2009;
- **Discounts:** the high level of discounts has deterred all but the most forced of sellers from the market. Investors wishing to rebalance their portfolios may find the current prices prohibitively low, and are unwilling to crystallize a loss;
- **Opaqueness:** sellers and buyers alike have limited reliable information to help them make strategic decisions, and may be unwilling to initiate discussions without more information on likely values.

The overall feeling in the market is that secondary volumes will expand significantly at some point, but that these factors are currently frustrating the potential growth.

**Fig. 4**  
**Make Up of Investors Looking to Buy on the Secondary Market by Type**



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### Calling all LPs

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# Preqin Research Report

## Investor Attitudes to the PERE Secondaries Market (3)

In order to provide both buyers and sellers with a tool to help them find opportunities in this market, Preqin has recently launched the Private Equity Secondary Market Monitor, which has now been expanded to include information on real estate private equity. Fig. 5 shows how the service works:

LPs: can benefit from three key features of the service:

- Preqin Price Indication: the LP can enter a fund or portfolio at any time, and Preqin's powerful online pricing model algorithm calculates an instant indication of the likely current secondary market value;
- Buyer and Advisor Profiles: the LP can find profiles of all significant players in the market, helping them decide who they should be contacting if they wish to pursue buying or selling opportunities; and
- Third Party Price Indication: if the LP is interested in selling, they can submit their portfolio for a price indication from one of the buyers and advisors using the service. The buyers and advisors can see the portfolio and decide whether to submit a (non-binding) indication of likely price, but cannot see the identity of the LP. The LP therefore benefits from these further indications of likely value, and can contact the buyers and advisors for further discussions, potentially leading to a transaction.

Buyers and Advisors: also benefit from using the service, giving them information and generating potential dealflow:

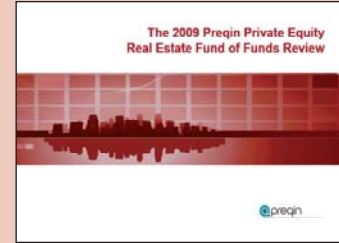
- Preqin Price Indication: this is also available to these users, giving them an initial indication of current price levels for any fund or portfolio;
- LP Strategies and Contacts: Preqin's researchers are speaking with over 100 LPs per week, understanding who are the potential sellers and buyers. This vital information on potential dealflow, together with contact details and the LP's program and strategy, is available only to users of the Secondary Market Monitor;
- LP Pricing Requests: LPs submit their requests for Third Party Price Indications through the service. If the Buyer or Advisor wishes to respond with a (non-binding) price indication, then this price indication is submitted to the LP, together with the Buyer's / Advisor's profile and contact details. The LP can then initiate direct contact with the Buyer / Advisor if they would like to discuss the portfolio in further detail. The Buyer / Advisor can also send messages to the LP through the system.

In summary, the Preqin Secondary Market Monitor aims to give LPs unique and vital information on current pricing and counterparties, and to give Buyers and Advisors unique access to potential dealflow. Significantly, the service is free for LPs.

Please contact us if you would like to know more about the service, or alternatively, please view our product page at:

[www.preqin.com/SMM](http://www.preqin.com/SMM)

### Out Now: 2009 Preqin Real Estate Fund of Funds Review



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**... Preqin's researchers are speaking with over 100 LPs per week, understanding who are the potential sellers and buyers...**

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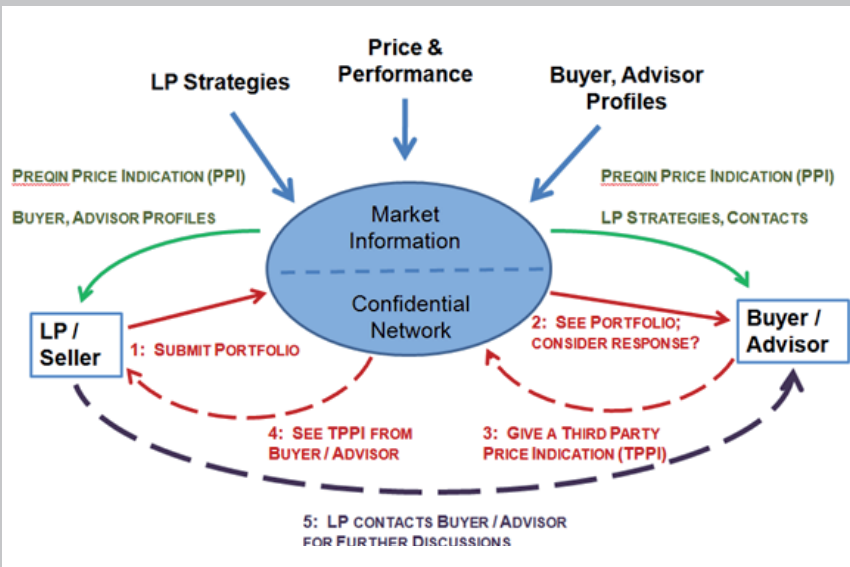


#### RE Spotlight

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**Fig. 5:**  
**Structure of Preqin's Secondary Market Monitor**



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