2013 Preqin Global Real Estate Report

Sample Pages

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2013 Global Real Estate Report Contents

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Private Real Estate in 2013 – Outlook for the Year Ahead

- Andrew Moylan, Preqin

Fundraising remained challenging in 2012 as a result of economic uncertainty, a lack of new commitments being made by investors and a large number of funds on the road. Closed-end private real estate funds that held a final close during the year raised an aggregate $55bn, a small decline on the $57bn that was raised by funds that closed in 2011. There were some notable fundraising successes, with 52% of funds that closed in 2012 doing so on or above target, including the $13.3bn final close of Blackstone Real Estate Partners VII, the largest closed-end private real estate ever raised.

For many firms however, securing commitments remained difficult. Fundraising is now a long process, with managers spending an average of just under 18 months marketing their funds. Raising a first-time fund is particularly difficult, with fewer investors now prepared to invest with new firms. Just 21% of investors will commit to first-time funds, compared with 41% in December 2009. More than ever, investors want to see evidence of a strong track record, and in particular that a firm performed well during the downturn, as well as in growing markets.

While the number of funds in market did fall during the final quarter of 2012, with 449 funds currently on the road targeting an aggregate $147bn in capital commitments, the fundraising market remains extremely crowded. Even with improving investor sentiment, there will likely continue to be a significant number of managers falling short of their fund targets or abandoning their fundraising efforts altogether.

Investor Sentiment

There are strong signs that investor confidence in private real estate funds is returning, with 53% of investors surveyed by Preqin in December 2012 planning to make new commitments to the asset class in 2013. In a similar study conducted in December 2011, just 36% of investors expected to make commitments in the following 12 months. The majority (54%) of investors also expect to commit more capital to the asset class in 2013 than they did in 2012.

Real estate remains an important part of many sophisticated investors' portfolios, with 93% of institutional investors active in the asset class targeting exposure to property of at least 5% of their total assets. As well as having the potential to generate strong returns, real estate portfolios can offer diversification, act as an inflation hedge, and provide a steady income stream; we have seen only a very small proportion of investors scale down their exposure to the asset class. In the longer term, just 9% of investors expect to reduce their allocations to real estate, while 39% expect their allocations to increase.

While a large proportion of investors focused primarily on core investments following the downturn, many are now increasingly looking at opportunities higher up the risk/return spectrum. Investor interest in core remained strong during 2012, but there was also increased appetite for core-plus, value added and opportunistic strategies. Real estate debt is also gaining more interest from investors, with a growing proportion believing it can add value to their real estate portfolios.

The use of separate accounts is also continuing to increase, with some investors viewing this as a way to invest significant amounts of capital, while retaining a greater level of control than they might have with a commitment to a blind-pool fund. These typically remain the preserve of larger, more experienced investors however, and many small- or mid-sized investors lack the additional resources required to invest through separate accounts.

Performance

Recent performance of the real estate asset class is also encouraging. Preqin's latest study of the performance of public pension funds' portfolios found that their real estate investments generated a median return of 10.0% in the 12 months to June 2012, more than any other major asset class. In each of the nine quarters to June 2012, there was an average increase in NAV for private real estate funds and there are positive signs for private real estate funds of more recent vintages. The median IRR of 2009 vintage funds stood at 12.9% as of June 2012, with three-quarters of funds generating IRRs of 9.5% or more.

This must of course be placed in context; many investors suffered significant losses in 2008 and 2009 and despite the improvements in recent quarters, many are still disappointed with the returns they have received. Forty-seven percent of investors surveyed by Preqin in December 2012 felt the performance of their private real estate portfolios had fallen short of their expectations.

Outlook for 2013

Fundraising looks certain to remain challenging in 2013. There are signs of improving investor appetite, with a growing proportion of institutions expecting to commit capital to private real estate in the coming year; however, a significant proportion still do not expect to be active. While a dramatic increase in fundraising is unlikely, 2013 may see more capital raised than was secured in 2012. Firms marketing new vehicles will need to demonstrate a strong track record, have competitive fee structures and an alignment of fund manager and investor interests, and be able to clearly differentiate themselves from the competition in order to be successful.

Overview of 2012 Fundraising Market

The private real estate fundraising market has stabilized in recent years, with the amount of capital secured by funds closed each year between 2009 and 2012 remaining around $50bn. There are signs that investor sentiment towards real estate is gradually improving, but many institutions did not commit capital to the asset class during 2012 and, with a large number of funds on the road, fundraising is likely to remain challenging in 2013.

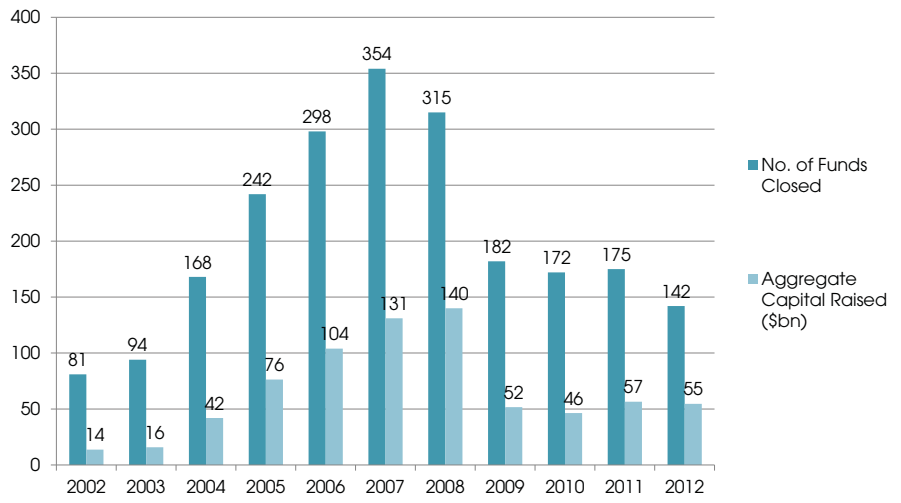
Fundraising by Quarter

Although 2012 saw a drop in the number of funds closed to 142 compared to the 175 closed in 2011 (Fig. 4.1), the aggregate capital raised remained fairly stable, with funds closed in 2012 raising $55bn compared to the $57bn raised by funds closed in 2011. Fig. 4.2 shows that Q4 2012 saw the highest quarterly aggregate capital commitments ($23bn) of any quarter in the past four years; however, it is important to note that the quarter included the $13.3bn close of Blackstone Real Estate Partners VII, the largest closed-end private real estate fund ever raised. The largest fund in market, Brookfield Asset Management's Brookfield Strategic Real Estate Partners is targeting a significantly smaller $3.5bn.

Manager Experience

More experienced managers accounted for a greater proportion of the capital raised in 2012, with many investors increasingly focused on investing with managers with a strong track record. Fig. 4.3, which measures experience by the number of funds a manager has raised, shows that 46% of capital raised in 2012 was secured by fund managers which have closed 10 or more funds. It is important to note the influence of Blackstone Real Estate Partners VII on this graph, with the $13.3bn committed to the fund included in the capital raised by fund managers which have closed 10 or more funds. Despite this, the number of funds raised by firms which have

Fig. 4.1: Annual Closed-End Private Real Estate Fundraising, 2002-2012



Source: Preqin Real Estate Online

Data Source:

Real Estate Online provides detailed profiles for over 4,000 unlisted real estate funds, including over 470 private real estate funds in market.

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Fig. 4.2: Quarterly Closed-End Private Real Estate Fundraising, Q1 2009 - Q4 2012

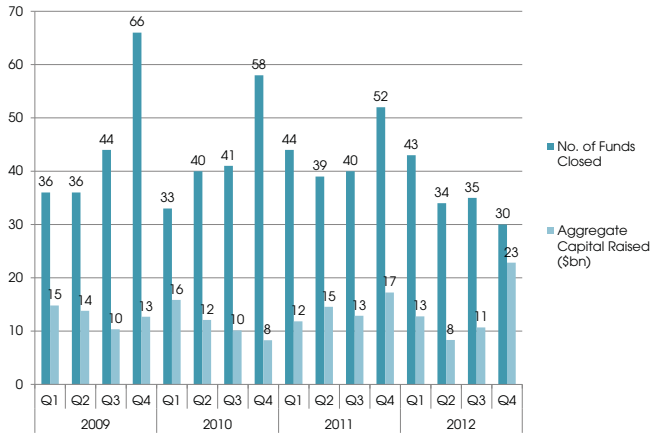

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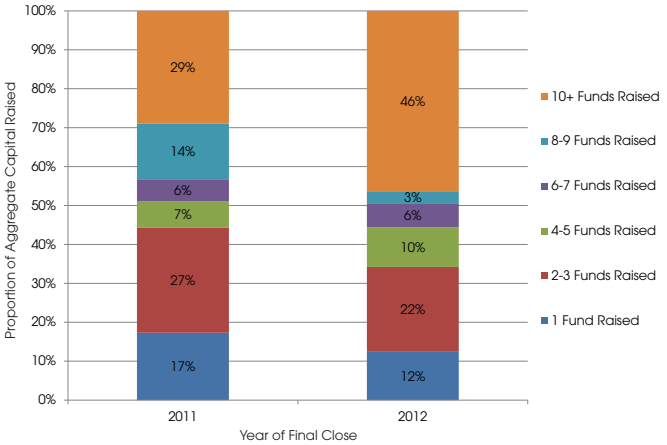
Fig. 4.3: Breakdown of Capital Raised by Closed-End Private Real Estate Funds by Manager Experience, Funds Closed 2011 – 2012



Source: Preqin Real Estate Online

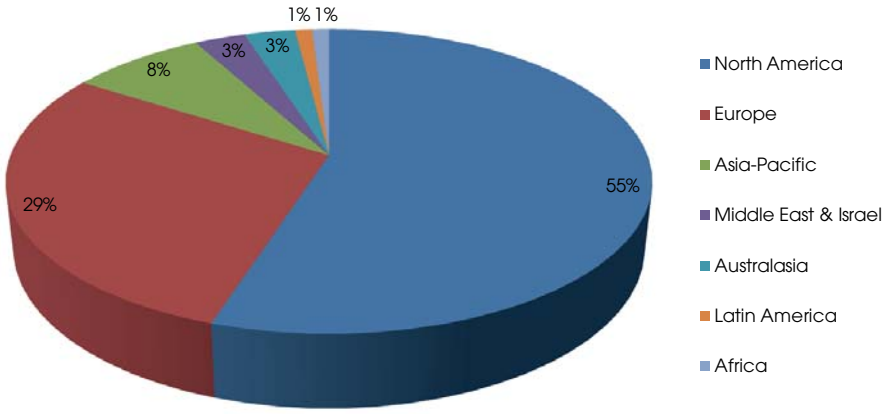
Overview of Private Real Estate Fund Managers

There has been considerable growth in the number of private real estate fund managers that are active in recent years, despite the tough fundraising environment. Preqin tracks more than 1,600 private real estate firms, including managers of both closed- and open-ended funds, which between them manage over 3,800 vehicles. Globally, the private real estate industry employs an estimated 14,500 people.

The closed-end fund model is the model most widely used by private real estate fund managers. In terms of fund types managed, 83% of firms only manage closed-end funds, and 10% manage only open- or semi-open-ended funds. The remaining 8% are managers of both closed- and open/semi-open-ended funds.

North America remains the base for the majority of private real estate firms, accounting for 55%, as Fig. 5.1 shows. Europe is the second most significant region for such firms, with 29% headquartered in the region; this is a one percentage point increase from a year ago. Of the remaining firms, 8% are based in Asia-Pacific, and 3% are in each of the Middle East and Israel, and Australasia. The final 2% is made up of Africa- and Latin America-based private real estate firms.

Fig 5.1: Breakdown of Private Real Estate Firms by Location of Headquarters



Source: Preqin Real Estate Online

New York and London are the two most important metropolitan areas for private real estate firms, with 183 and 171 firms respectively headquartered in these cities (Fig. 5.2). Sixty-nine private real estate firms are headquartered in Los Angeles, less than half the number based in London. US cities account for six of the top 10 locations for headquarters of private real estate fund managers, and Sydney, Mumbai and Toronto make up the remainder.

Data Source:

Real Estate Online features detailed profiles of over 1,680 fund managers from around the world.

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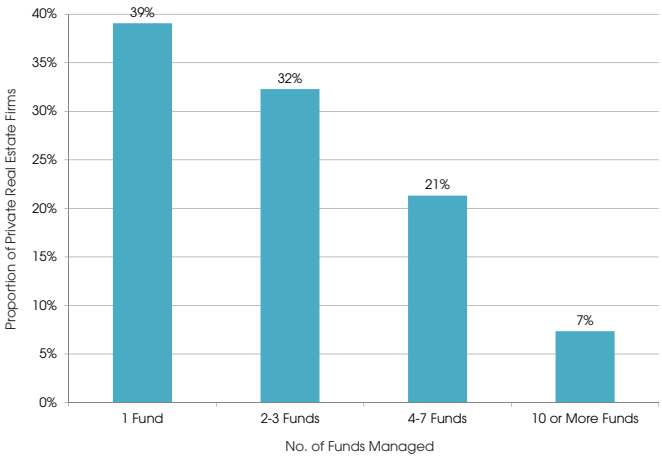
Fig. 5.2: Top 10 Metropolitan Areas for Private Real Estate Firms (Based on Headquarters)

Metropolitan Area	No. of Firms
New York	183
London	171
Los Angeles	69
Chicago	56
San Francisco	42
Boston	38
Dallas	36
Sydney	29
Mumbai	24
Toronto	19

Source: Preqin Real Estate Online

Fig. 5.3: Breakdown of Private Real Estate Fund Managers by Number of Funds Managed



Source: Preqin Real Estate Online

Investor Appetite for Private Real Estate in 2013

During Q4 2012, Preqin conducted a series of extensive interviews with over 100 institutional investors in private real estate funds from around the world in order to examine their attitudes towards the asset class and their outlook for 2013.

Investor Activity in 2012

Of the investors surveyed, 49% had made at least one private real estate fund commitment during 2012. The level of new investment activity seen in 2012 differed by geographic location, as seen in Fig. 7.12. Asia-based institutions were the most active in 2012, with 86% of those surveyed by Preqin committing to private real estate funds during this period, compared with 48% of North America-based investors and 45% of Europe-based institutions. Institutional investors based in Asia have become more important sources of capital for the real estate asset class over the last few years. A shift in investor attitudes and changing regulations has allowed many Asia-based institutions to move away from traditional investments to focus more on alternative investments, and as a result many institutions based in the region are investing more capital in the real estate asset class.

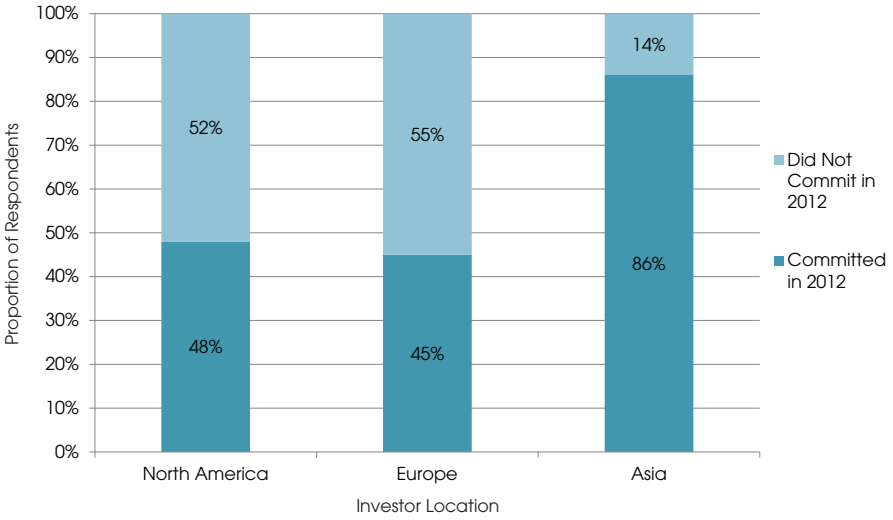
Prospects for 2013

Investor appetite for private real estate has grown over the course of 2012, with the proportion of investors likely to commit to private real estate now at a higher level than at any point since January 2010, increasing from 36% in January 2012 to 53% in January 2013 (Fig. 7.13).

This growth in appetite followed a period of decline from January 2010 to January 2012 in the proportion of investors that expected to make commitments. The results suggest that investors are starting to regain confidence in the asset class and, as a result, fundraising may increase in 2013.

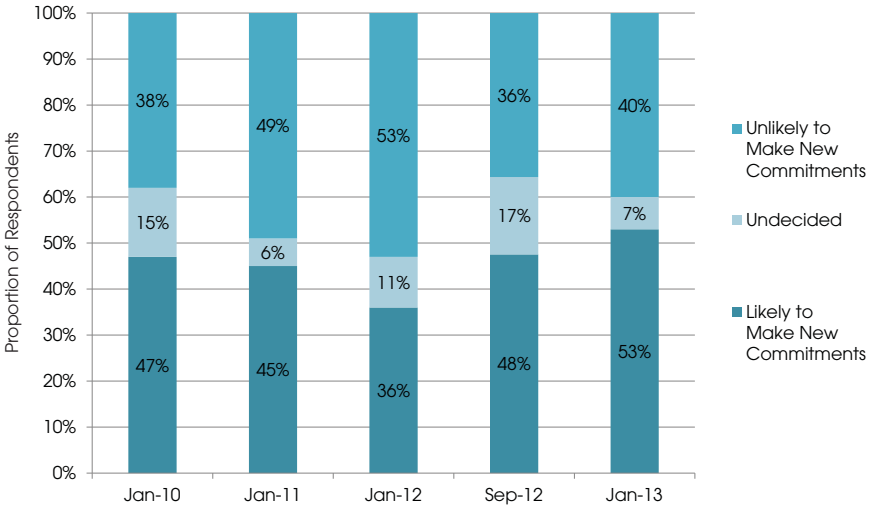
Investors based in Asia are again set to be the most active, with 83% expecting to make new commitments in 2013 (Fig. 7.14), a similar proportion to the number that invested in private real estate funds in 2012. Forty-eight percent of investors surveyed based in North America were planning to commit to private real estate funds in 2013. Thirty-nine percent of Europe-based investors interviewed said that they would invest in private real estate funds in 2013, while a further 9% based in the region remain undecided as to whether they will

Fig. 7.12: Proportion of Investors that Committed to Private Real Estate Funds in 2012 by Investor Location



Source: Preqin Investor Outlook: Real Estate, H1 2013

Fig. 7.13: Investor Intentions for Private Real Estate Investments in the Following 12 Months, January 2010 - January 2013



Source: Preqin Investor Outlook: Real Estate, H1 2013

Data Source:

Real Estate Online features detailed profiles of over 3,500 investors, including current fund searches and open mandates, direct contact details, and more.

Real Estate Debt Fund Market

Recent years have seen debt funds feature more prominently in the private real estate industry, with many firms diversifying their businesses to include specialist debt platforms and a growing number of fund managers incorporating the acquisition or origination of real estate debt into their existing investment strategies. As the availability of bank financing has fallen in the US and Europe, many fund managers, alongside other non-traditional lenders, are increasingly stepping in to help fill the funding gap.

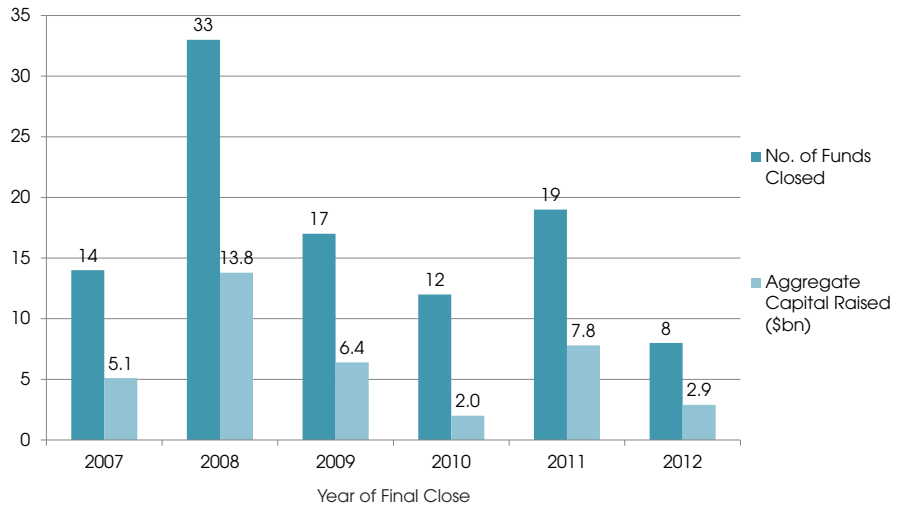
Institutional investors are also increasingly interested in the value that real estate debt can add to their existing real estate portfolios. A growing number of institutions believe that these funds can generate returns with a lower level of risk than equity investments in real estate, and a significant number of investors plan to commit to funds with a debt strategy in 2013. Thirty-four percent of real estate investors interviewed by Preqin in December 2012 were targeting debt funds in the following 12 months compared to just 8% in the 12 months following December 2011.

Solely Debt-Focused Fundraising

The most successful year in terms of fundraising for solely debt-focused funds was 2008, with 33 solely debt-focused funds raising an aggregate $13.8bn (Fig. 10.1). Fundraising has been slower since then and while 2011 was a relatively successful year, with 19 solely debt-focused funds raising an aggregate $7.8bn, 2012 saw only eight solely debt-focused funds close on an aggregate $2.9bn.

Although the proportion of capital raised by solely debt-focused funds has fluctuated in recent years, demand for debt exposure has consistently increased. Fig. 10.3 shows that the proportion of capital raised by funds solely making equity investments has decreased considerably in the last five years, with a growing proportion of funds incorporating debt investments to some extent. Since 2007 there has been a large decrease in the proportion

Fig. 10.1: Annual Solely Debt-Focused Closed-End Private Real Estate Fundraising, 2007-2012



Source: Preqin Real Estate Online

Data Source:

Subscribers to Preqin's **Real Estate Online** can view detailed profiles for over 350 firms globally with an interest in investing in real estate debt.

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Fig. 10.2: 10 Largest Solely Debt-Focused Closed-End Private Real Estate Funds Closed, 2011-2012

Fund	Firm	Geographic Focus	Size (mn)
Blackstone Real Estate Special Situations Fund II	Blackstone Group	US	2,900 USD
Fortress Japan Opportunity Fund II	Fortress Investment Group	Japan	130,000 JPY
CRE Senior 1	AXA Real Estate	Europe	1,000 EUR
Pramerica Real Estate Capital I	Pramerica Real Estate Investors	UK, Germany	492 GBP
Prudential U.S. Real Estate Debt Fund	Pramerica Real Estate Investors	US	805 USD
M&G Real Estate Debt Fund	M&G Investments	West Europe	343 EUR
European Real Estate Debt Fund	DRC Capital	Europe	300 GBP
Selene Residential Mortgage Opportunity Fund II	Selene Investment Partners	US	476 USD
Longbow UK Real Estate Debt Investments II	ICG-Longbow	UK	242 GBP
Cornerstone Enhanced Mortgage Fund	Cornerstone Real Estate Advisers	North America	315 USD

Source: Preqin Real Estate Online

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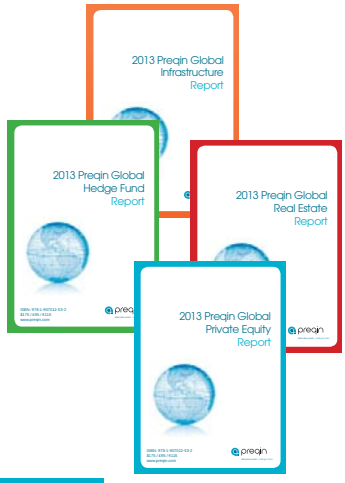

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