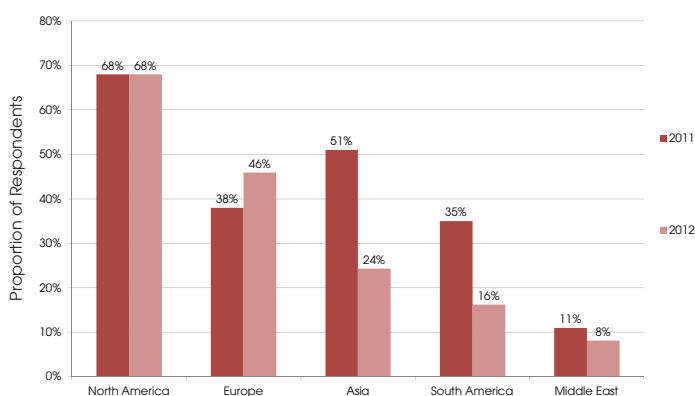




Changing Consultant and Investor Attitudes to Private Real Estate

Dami Sogunro and Andrew Moylan examine the changing strategies and geographic preferences of investment consultants and institutional investors and the implications for the private real estate fund market.

Fig. 1: Regions Viewed by Consultants as Presenting the Best Opportunities in Private Real Estate, 2011 - 2012



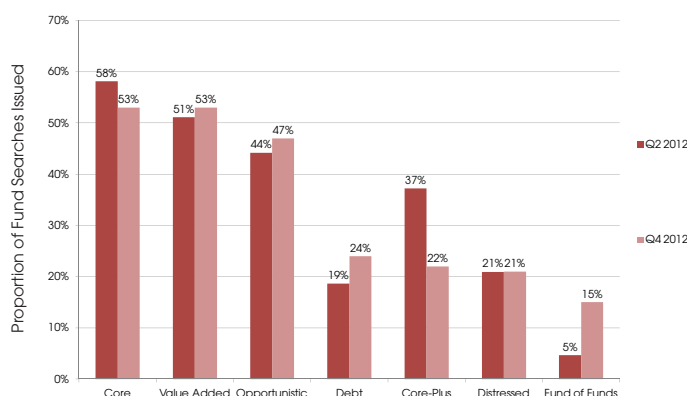
Source: Preqin 2012 and 2013 Alternatives Investment Consultant Review

Ongoing economic uncertainty in the eurozone and global markets has made raising capital for investments in European real estate very challenging. Perhaps more significantly, the current fundraising levels in the European private real estate market appear to suggest that investor interest in the region remains fairly low. In 2012 so far, only 22 funds have closed, raising an aggregate €5.2bn in capital commitments, compared with the aggregate €8.1bn raised by funds which reached a final close in 2011. Preqin's survey of real estate investors at the start of 2012 in Preqin Investor Outlook: Real Estate, H1 2012 showed that only 33% of surveyed investors planned to target investments in Europe in 2012.

However, alternatives investment consultants active in the private real estate universe have expressed a different opinion on private real estate opportunities in Europe. Within the private real estate asset class, a significant proportion of investors (51%) employ the services of an investment consultant to assist in fund selection, making these consultants an important group to consider when assessing the current private real estate market. Preqin recently surveyed 80 alternatives investment consultants from around the world in the 2013 Preqin Alternatives Investment Consultant Review; collectively, these consultants have over \$1.5tn worth of alternative assets under advisement.

Forty-six percent of consultants interviewed stated that they believe there are good opportunities for investment in Europe (Fig. 1). This is an increase from the 38% which expressed the same opinion in 2011. While many investors have been reluctant to invest in Europe given the ongoing uncertainty, it is clear that consultants expect there to be good opportunities in the region in the coming months, with more distressed opportunities and an expanding debt fund market.

Fig. 2: Investor Fund Searches Issued by Strategy, Q2 2012 vs. Q4 2012



Source: Preqin Real Estate Online

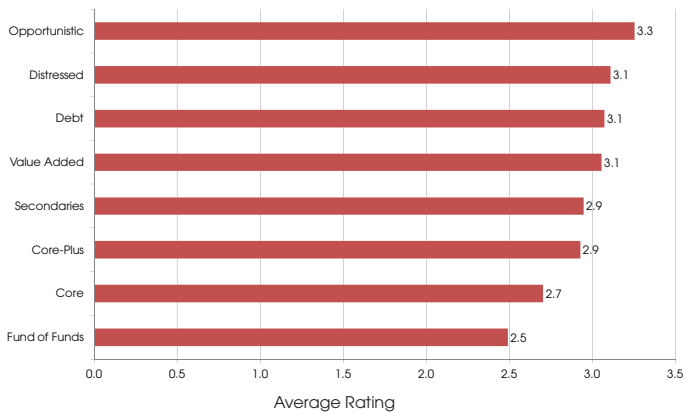
These results suggest consultants may recommend that their clients make more commitments to Europe-focused funds over the next few months.

With investment consultants acting as important gatekeepers for such a significant proportion of private real estate investor capital, exploring their opinions about investment opportunities across various strategies and geographies can provide an insight into the current private real estate market and outlook for the asset class. When compared with Preqin's most recent surveys of investors in the asset class, they can also reveal contrasting changes in consultant and investor sentiment towards particular investment strategies or aspects of the market. Investment consultants can provide an important access point for fund managers looking to raise capital for their private real estate funds, particularly given the current challenging market conditions.

The dominant opinion among investment consultants is that the more established markets present the best opportunities at present, and there is less interest in real estate in emerging economies. As shown in Fig. 1, over two-thirds (68%) of consultants named North America as the region presenting the best opportunities, a proportion which remains unchanged since 2011. In contrast, sentiment towards emerging markets has dropped significantly. Investment consultant appetite for Asia dropped from 51% of surveyed consultants naming the region as presenting good opportunities in 2011 to 24% in 2012. The proportion of investment consultants naming South America as a region with good investment opportunities as fell from 35% in 2011 to 16% in 2012.



Fig. 3: Private Real Estate Investment Consultant Attitudes to Different Fund Types at Present



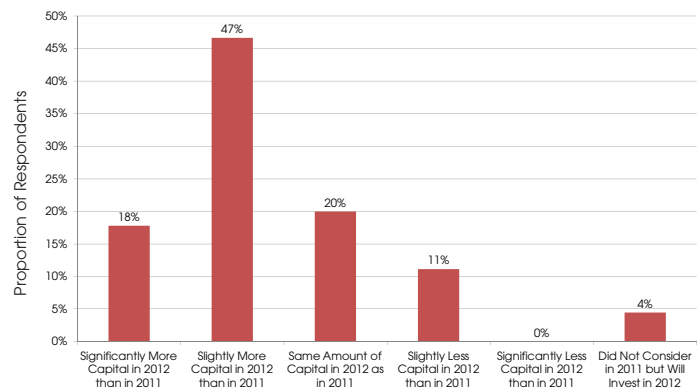
Source: Preqin 2013 Alternatives Investment Consultant Review

Key Strategies

Preqin's most recent research shows that core funds remain one of the most commonly targeted strategies; however, appetite for this strategy seems to be declining. As is shown in Fig. 2, 53% of institutional investors searching for funds in Q4 2012 are targeting core funds, with the same proportion targeting value added funds and 47% targeting opportunistic strategies. As of Q2 this year, 58% of investors searching for new funds were targeting core strategies, a larger proportion than the 51% and 44% that were targeting value added or opportunistic investments respectively.

However, this may continue to change in the coming months as many investment consultants believe that the better opportunities are in funds with higher risk/return profiles. In the 2013 Preqin Alternatives

Fig. 4: Amount of Capital Consultants & Their Clients Plan on Committing to Private Real Estate in 2012 compared to 2011



Source: Preqin 2013 Alternatives Investment Consultant Review

Investment Consultant Review, investment consultants were asked to rate which real estate fund types present the best investment opportunities on a scale of one to five, with five representing the most attractive opportunities and one representing the least. Investment consultants view core as one of the least attractive strategies, with the fund type receiving an average ranking of 2.7.

Instead, investment consultants ranked opportunistic as the strategy presenting the best opportunities, with an average ranking of 3.3. Opportunistic was ranked slightly higher than the other highly ranked strategies of debt, distressed private real estate, and value added, all of which have an average ranking of 3.1. Some commentators have suggested that the increased demand for core assets has meant these are now overpriced, and it seems that consultants now believe there are better opportunities elsewhere. However, many investors

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remain extremely risk-averse and it may prove difficult to convince these institutions to move up the risk/return ladder.

Capital Outlay

The majority of investment consultants responded in Preqin's September 2012 survey that they expected capital committed to private real estate funds in 2012 to end up exceeding the amount they committed in 2011, as Fig. 4 shows. Sixty-nine percent of consultants will either be significantly or slightly increasing their commitment level to private real estate, or will be investing in the asset class after having not invested in the previous year.

Among those consultants which expected to increase their commitments this year as of September 2012, a notable 47% will make slightly more capital commitments in 2012 in comparison to 2011. With many investment consultants looking to make new private real estate commitments on behalf of their clients in the near future, these consultants can be an important target group for fund managers looking to raise fresh capital commitments. A slightly larger proportion of investment consultants expected to slightly reduce their level of commitment to the asset class this year, with 11% stating so this year compared to 9% in 2011. However, no consultants will be making any significant reductions. In a similar study of institutional investors, Preqin found that 37% of investors expected to commit more capital in the next 12 months.

Key Issues Facing the Real Estate Market

When asked about the key issues facing the real estate market, the valuation of investments has again been named by private real estate investment consultants as the single most important issue, with almost a quarter (24%) of consultants citing this as the most prominent issue facing those investing in the asset class.

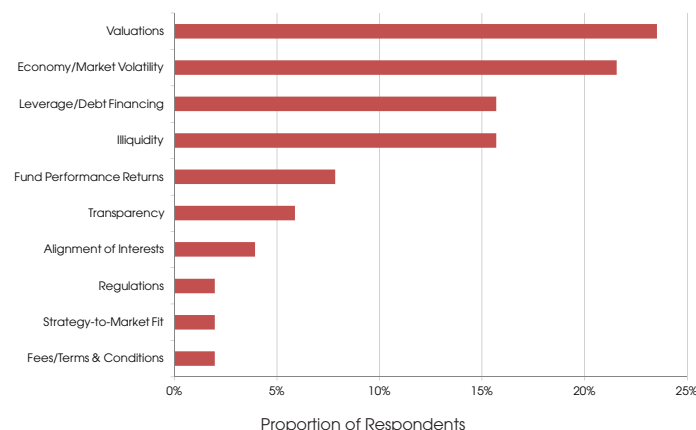
The economic climate and the resulting volatility was named by 22% of consultants as the single most important issue facing investors in the private real estate market. Market illiquidity and levels of leverage and debt financing were two other issues given equal importance by surveyed consultants, with each rated as the single most important issue in the market by 16% of private real estate investment consultants.

Industry regulations, strategy-to-market fit, and fees/terms and conditions were cited by the smallest proportion of investment consultants as the single most important issue in the private real estate market, with each issue named by only 2% of investment consultants.

Outlook

The results of the 2013 Preqin Alternatives Investment Consultant Review are encouraging for many fund managers, with consultants and their clients expecting to invest more capital in private real estate funds in the future. Within the consultant community, many view higher risk/return profile strategies as offering the best opportunities in the current market, with core investments proving less attractive to many consultants. In the current tough fundraising environment, this

Fig. 5: Investment Consultants' Perception of Key Issues in the Private Real Estate Market



Source: Preqin 2013 Alternatives Investment Consultant Review

will be encouraging news for fund managers seeking capital for these types of funds. However, with lower risk investments remaining a focus for a large proportion of institutional investors, fund managers looking to raise capital for opportunistic and value added will likely struggle in the coming months.

While Europe's economic challenges are well documented, investment consultants have growing confidence in the real estate investment opportunities that exist in the region; therefore, it seems likely that Europe-focused fundraising will increase in the coming year. However, for managers of Asia or Latin America-focused funds, fundraising could be extremely challenging, with consultants seemingly set to concentrate more on the established, liquid markets in North America and Europe than in previous years.

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This article draws upon information from the [Preqin 2013 Alternatives Investment Consultant Review](#). Click [here](#) to find out more, or to purchase your copy.

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