PREQIN SPECIAL REPORT:
REAL ESTATE CO-INVESTMENTS AND SEPARATE ACCOUNTS

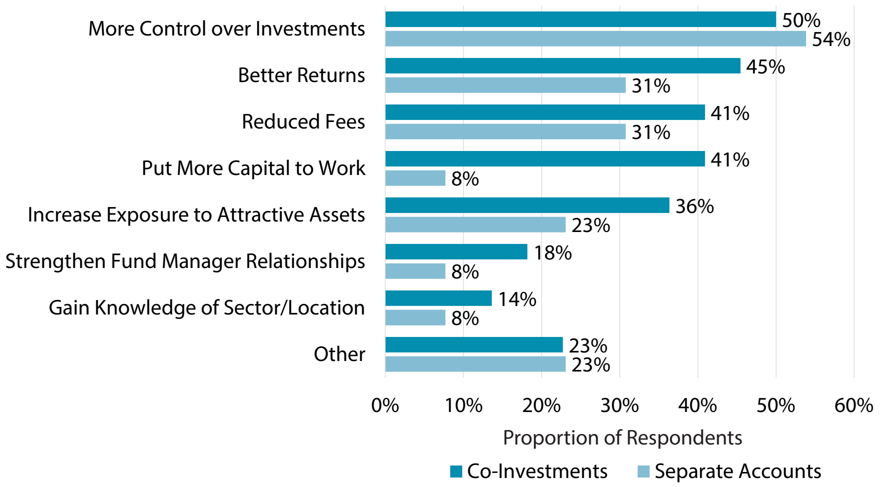
MARCH 2017

alternative assets. intelligent data.

Recent years have seen institutional investors increasingly looking for alternatives to the blind pool fund model. For some, this has been through increased use of direct investments, but this remains impractical for many investors, particularly when investing outside their own markets. Structures such as co-investments, separate accounts and joint ventures can offer investors the opportunity to gain more exposure to attractive assets, with more control and potentially lower fees, while still accessing a third-party manager's skill and pipeline of potential deals.

Drawing on the results of a series of in-depth interviews with institutional investors and fund managers in Q4 2016, and the profiles for thousands of GPs and LPs on Preqin's **Real Estate Online**, this report explores how institutional investors and fund managers are using these alternative structures.

Fig. 1: Key Attractions of Co-Investments and Separate Accounts for Institutional Investors in Real Estate

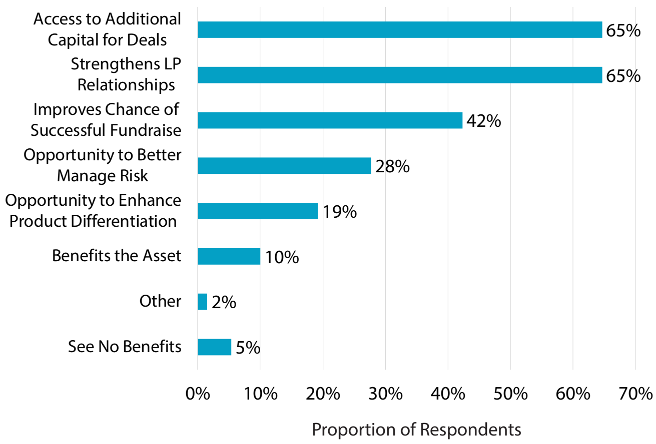


Source: Preqin Investor Interviews, December 2016

KEY ATTRACTIONS

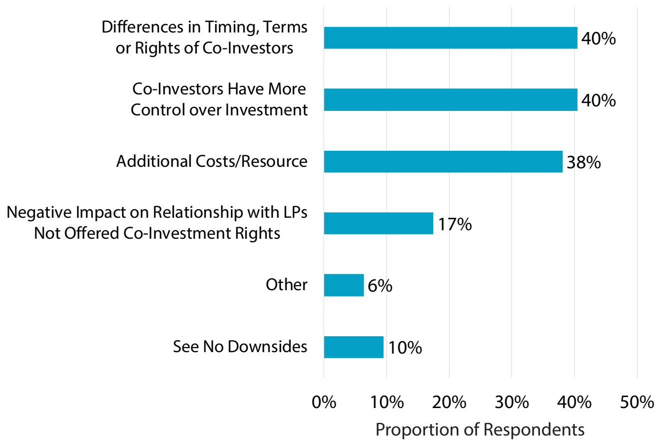
Fig. 1 shows that the key benefit of separate accounts for investors is the additional control over the direction of their capital that comes with a bespoke vehicle, while reduced fees and the prospect of better returns are also key factors. Added control is the most attractive feature of co-investments, but the opportunity to put more capital to work is also an important reason why investors look to co-invest alongside managers.

Fig. 2: Key Benefits for Private Real Estate Fund Managers of Offering Co-Investment Opportunities to Investors



Source: Preqin Fund Manager Survey, November 2016

Fig. 3: Key Downsides for Private Real Estate Fund Managers of Offering Co-Investment Opportunities to Investors



Source: Preqin Fund Manager Survey, November 2016

> Increased control for the investor is the biggest attraction for institutions looking for co-investments or separate accounts – and a major drawback for managers offering them

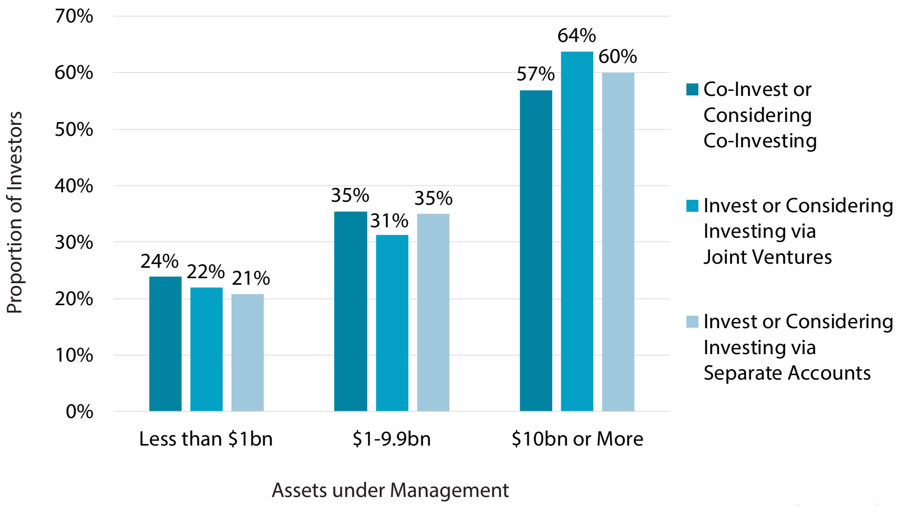
For firms managing private real estate funds, it is the opportunity to raise additional capital and to build relationships with their LPs that are the key attractions of offering co-investment rights, as shown in Fig. 2. Many also stated that offering co-investment opportunities could help the fundraising process, suggesting that this is something many institutions are factoring into their decision-making process when evaluating fund managers. The most commonly stated downsides were the challenges associated with managing a deal with multiple investors that may have different timelines for their decision-making processes or different co-investment terms, as well the reduction in control over a particular investment (Fig. 3). The additional cost of reporting and structuring these co-investments is also a potential negative for many firms.

WHICH INVESTORS ARE TARGETING THESE ROUTES?

The ability of an investor to allocate capital through separate accounts, joint ventures and co-investments is closely linked to its size, with larger institutions more likely to have more staff and the experience needed to source, review and monitor these investments. As illustrated in Fig. 4, around 60% of investors with assets of $10bn or more invest, or are considering investing, through these routes to market, while less than one-quarter of those that manage up to $1bn in AUM are considering these structures.

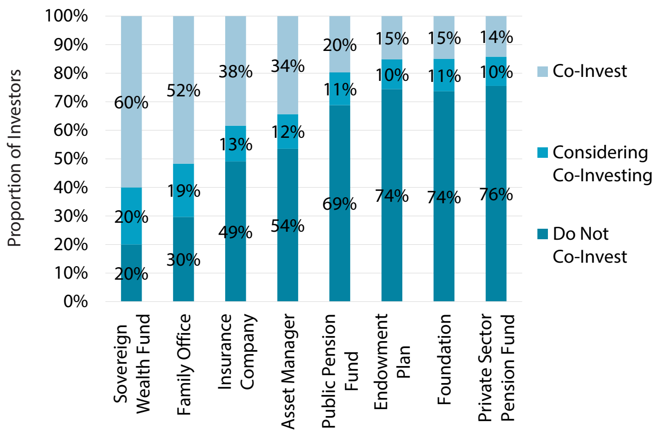
Fig. 5 and Fig. 6 show how the likelihood of allocating capital through co-investments

Fig. 4: Institutional Investor Appetite for Co-Investments, Joint Ventures and Separate Accounts by Assets under Management



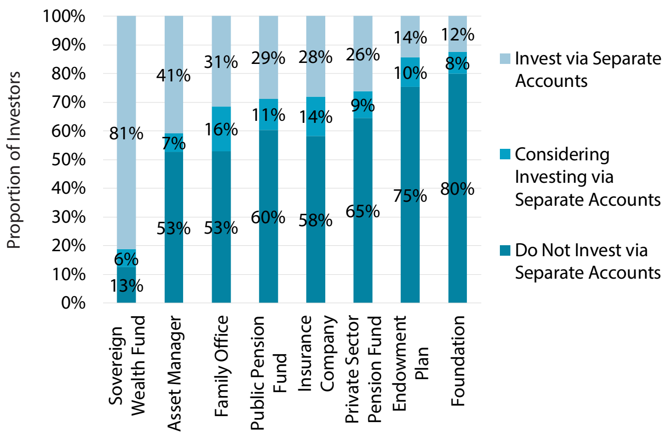
Source: Preqin Real Estate Online

Fig. 5: Institutional Investor Appetite for Real Estate Co-Investments by Type



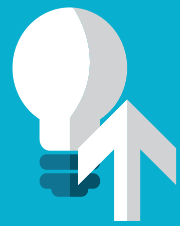
Source: Preqin Real Estate Online

Fig. 6: Institutional Investor Appetite for Real Estate Separate Accounts by Type



Source: Preqin Real Estate Online

67%
of fund managers offered co-investment opportunities to their investors in 2016.



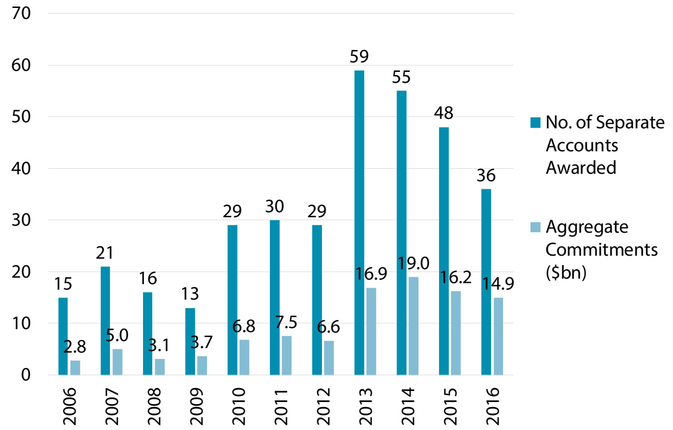
44%
of fund managers expect to offer their investors more co-investment opportunities in 2017; just 3% will offer fewer.

and separate accounts changes with the type of investor. Sovereign wealth funds, which typically have very large amounts of capital to put to work and sizeable internal teams (often in multiple locations), are very likely to be active through these routes. Other groups such as family offices or asset managers, which are typically more experienced in making direct real estate investments, are also more likely to make co-investment or separate account commitments. Groups such as endowment plans and foundations, which in many cases have less AUM and smaller investment teams, are less likely to consider these routes to real estate.

SEPARATE ACCOUNTS

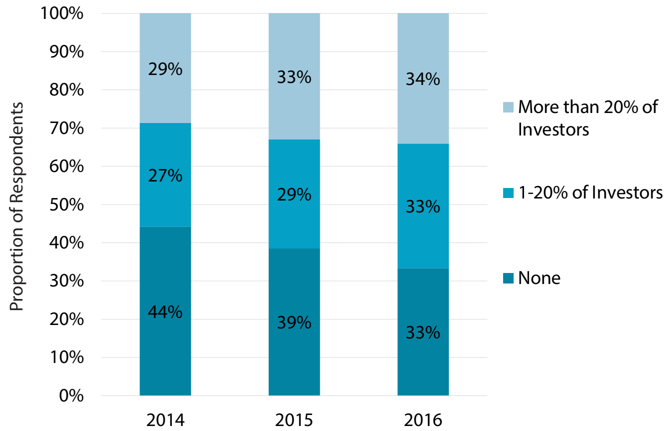
As illustrated in Fig. 7, both the number of separate accounts and the total capital secured by real estate managers for these vehicles have fallen slightly over 2015-2016 compared with 2013-2014. Despite this, capital raised for separate accounts remains well above that secured prior to 2013: a total of $67bn was raised through separate account structures between 2013 and 2016, compared with $25bn from 2009 to 2012. The decline in fundraising over 2015-2016 reflects a small decline in appetite for these structures among investors in recent years: 30% of respondents stated they would invest in

Fig. 7: Private Real Estate Separate Accounts Awarded, 2006 - 2016



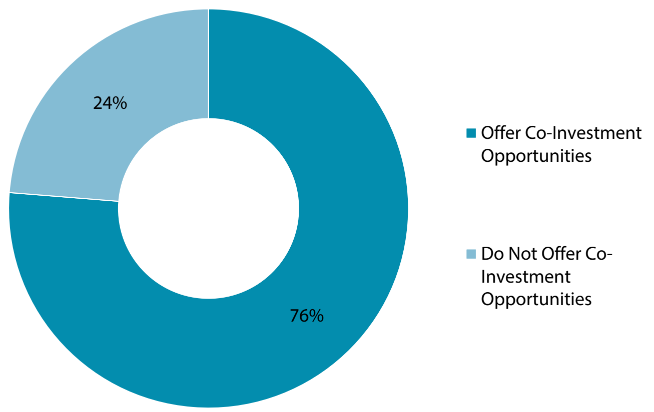
Source: Preqin Real Estate Online

Fig. 8: Proportion of Fund Managers that Offered Co-Investment Opportunities to Their LPs, 2014 - 2016



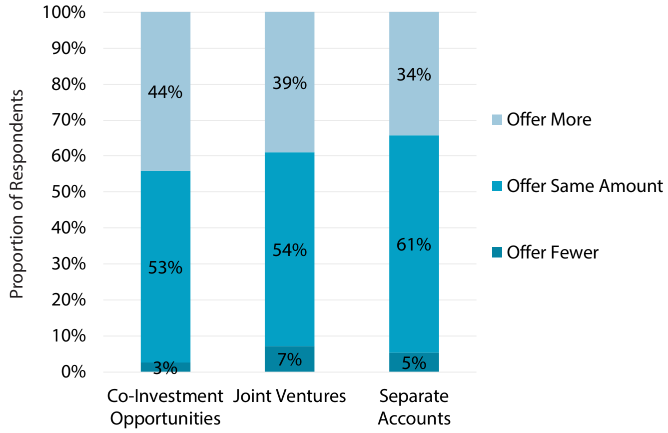
Source: Preqin Fund Manager Survey, November 2014 - November 2016

Fig. 9: Private Real Estate Funds in Market Currently Offering Co-Investment Opportunities



Source: Preqin Real Estate Online

Fig. 10: Fund Managers' Plans to Offer Co-Investment Opportunities, Separate Accounts or Joint Ventures in 2017 Compared to 2016



Source: Preqin Fund Manager Survey, November 2016

81%

of sovereign wealth funds invest in separate accounts.

"Real estate managers are seeing the advantages of offering alternative structures to investors, with 76% of private real estate funds in market also providing co-investment opportunities

separate accounts in 2014, compared to 27% in 2016.

Among the notable separate accounts formed in 2016 is the €1.3bn European retail mandate secured by Hines from Germany-based pension fund Bayerische Versorgungskammer and GLP Japan Development Venture II, as well as the $900mn partnership between Global Logistics Properties and CPP Investment Board, which targets opportunistic investments in Japanese logistics assets.

CO-INVESTMENTS

Fund managers are increasingly offering co-investment opportunities to their investors; the number of managers that do not offer co-investments has fallen since 2014 (Fig. 8). In many cases, these are only offered to a small sub-set of LPs, but one-third do offer co-investments to more than one-fifth of their investors, and a not insignificant 13% of fund managers offered co-investment deals to all their investors in 2016. In most cases, relatively few investors choose to take up these opportunities, with 39% of fund managers reporting that none of their investors offered co-investments did end up making a co-investment, while a further 21% reported that only 10% or less of the investors they offered a co-investment did choose to invest.

As illustrated by Fig. 9, over three-quarters (76%) of private real estate funds currently in market are also offering co-investment opportunities. This demonstrates fund managers' positive response to investor demand for these alternative structures and will enable managers to attract more capital commitments.

OUTLOOK FOR 2017

Fund managers are clearly seeing the benefits of offering investors access through these routes: Fig. 10 shows that sizeable proportions of respondents will offer more of these opportunities to investors in the coming year, and small proportions expect to offer fewer. This is most notable for co-investments: 44% expect to offer their investors more co-investment deals, suggesting managers are seeing the potential benefits of these structures in terms of gaining extra capital and cementing their LP relationships.

Fig. 11: Notable Private Real Estate Separate Accounts Awarded in 2016

Separate Account	Firm	Investor	Initial Equity Size (mn)	Strategy	Geographic Focus	Industry Focus
BVK - Hines Value Added Separate Account	Hines	Bayerische Versorgungskammer	1,300 EUR	Core, Value Added	Europe	Retail
GLP Japan Development Venture II	Global Logistic Properties	CPP Investment Board	900 USD	Opportunistic	Japan	Logistics
BVK - Deutsche Asset & Wealth Management Real Estate Debt Separate Account	Deutsche Asset & Wealth Management	Bayerische Versorgungskammer	750 EUR	Debt	North America, West Europe	Diversified
Goldman Sachs - Blue Sky Private Real Estate Separate Account	Blue Sky Private Real Estate	Goldman Sachs	1,000 AUD	Opportunistic	Australia	Student Housing
WSIB - Calzada Capital Partners Core-Plus Separate Account II	Calzada Capital Partners	Washington State Investment Board	750 USD	Core-Plus, Value Added	North America	Operating Companies
SFERS - CIM Group Diversified Separate Account	CIM Group	San Francisco Employees' Retirement System	700 USD	Core, Value Added	US	Diversified
NYSTRS - Blackstone Separate Account	Blackstone Group	New York State Teachers' Retirement System	500 USD	Debt	US, UK	Diversified
BVK - CapMan Real Estate Residential Separate Account	CapMan Real Estate	Bayerische Versorgungskammer	400 EUR	Core	Nordics	Residential
UBS (I) Zurich Italy - Real Estate Fund	UBS Asset Management	Zurich Insurance Group	400 EUR	Core, Core-Plus	Italy, Europe	Diversified
BVK - PATRIZIA Residential Separate Account	PATRIZIA Immobilien AG	Bayerische Versorgungskammer	400 EUR	Core, Core-Plus, Value Added	Europe	Residential

Source: Preqin Real Estate Online

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