Introduction to Real Estate JV & Fund Structures & Negotiation terms

Valyrian Capital

17 November 2015

Asset Owner Engagement Models

Models of Direct Investing

Key Process Steps	Research	Selection Sourcing & Diligence	Investment Decisions	Financing	Ongoing Asset Management	Asset Sale or Exit
Solo Investment	Internal	Internal	Internal	Internal	Internal	Internal
Separate Account	Internal or delegated	Internal or delegated	Internal or shared	Internal or shared	Internal or shared	Internal
Co-Investment	Delegated or internal	Delegated	Internal	Internal	Delegated or internal	Delegated or internal
Traditional Commingled Fund	Delegated	Delegated	Delegated	Delegated	Delegated	Delegated

Low – Owner Engagement – High

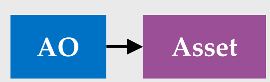
Models of Investing in Illiquid Assets

Traditional Delegated Model

Asset owner invests in a fund run by an asset manager

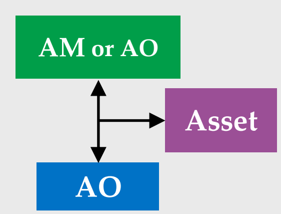
Models of Direct Investing

Solo



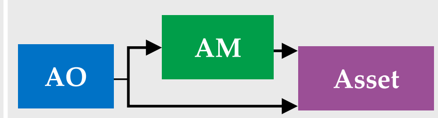
Asset owner acquires a stake in an asset without other deal partners

Partnership



Asset owner forms a partnership with one or more asset owner or, with an asset manager to invest together

Co-Investing



Asset owner invests in a fund run by an asset manager. In return for participating in the fund, the asset owners takes a stake in the asset directly

What Attracts Institutional Investors to Co-Investment?

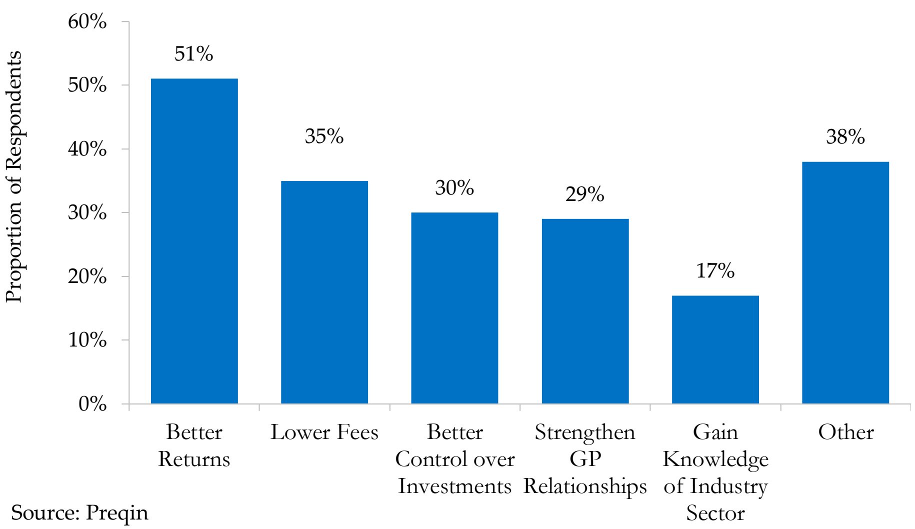
Co-investments often offer other incentives to LPs including reduced fees, better transparency, and more control over their investments

Exposure to deal-making when co-investing alongside a Fund gives LPs the opportunity to expand their internal capabilities, acquire valuable experience in direct commercial real estate investments, and gain exposure to asset classes they may not have access to otherwise

LPs appetite for co-investments is paired with a more flexible GP base, as many GPs are willing to allow investors access to co-investments in order to secure commitments to their funds. Using co-investor capital in deals alongside their funds also allows GPs to invest in large deals, which they may not be able to access with fund capital alone

As more LPs continue to look for new ways to invest their capital & co-investor deals become more widely reported, it is likely that we will continue to see investors setting up co-investment programs and looking for more exposure to direct private equity real estate deals

LPs' Reasons for Co-Investing



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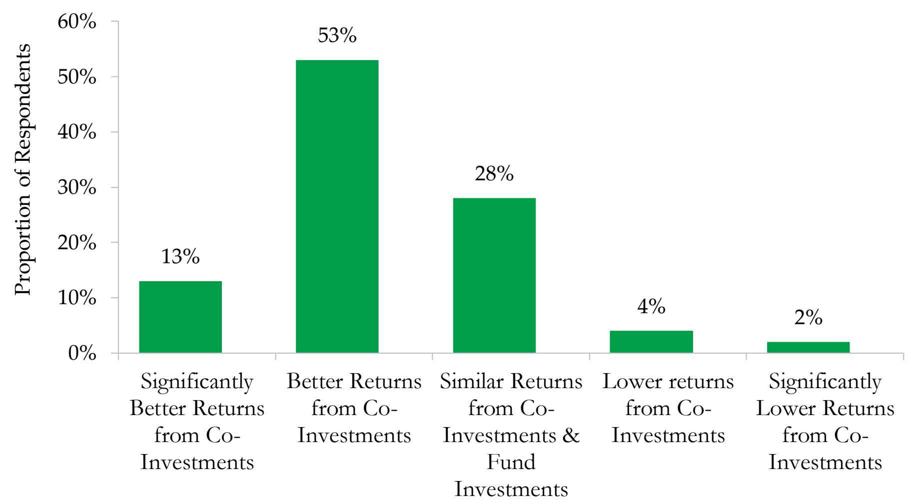
Co-Investment vs. Fund Investment Performance



Structuring RE Investment Vehicles & Joint Ventures

Structure Type	Description
Single Asset Joint Ventures	▪ Each joint venture is idiosyncratic; there are no pre-set terms and conditions ▪ **A joint venture may be formed to**: ‣ Acquire a specific property or a portfolio of properties ‣ Recapitalize an existing partnership ‣ Develop or redevelop a property ▪ **Terms to be negotiated include**: ‣ Co-investment (e.g. 90%/10%, 95%/5%) ‣ Preferred returns, total returns, clawbacks ‣ Promotes ‣ Governance ‣ Guarantees (development: completion; payment; environment; non-recourse carveouts ‣ Exit Buy/Sell (may include buy/sell provisions where properties are liquidated through acquisition by one JV partner or sale to a third party ‣ Transaction costs, fees and expenses
Strategic / Programmatic JVs	▪ Establish terms on which a series of investments may be made with a single investor or a small number of investors ▪ Terms may vary widely and are individually tailored (discretion within a box vs. deal by deal approval) ▪ Can offer a more certain funding source for projects within specific parameters ▪ Sponsor can contribute existing assets and/or close around pipeline assets
Entity / GP Investment	▪ Investments by one or more investors at the operation company (entity) or sponsor equity (GP) level ▪ Involves sale of a portion of all income streams generated by the entity of the GP ▪ Investments can take form of common or preferred equity and can vary with respect to governance ▪ Can provide permanent capital and a long term / global solution for the sponsor ▪ Creates alignment of interest; typically aids in raising additional JV capital
Comingled Funds	▪ Group of investors pool their resources to create a large investment ▪ Money is gathered from various sources that are managed together in one account ▪ Include a wide variety of entities including insurance companies, group trusts, limited partnerships, LLCs and private or untraded REITs

Joint Venture Key Terms & Concepts

Term	Description
Waterfall Structure	Portfolio returns crossed vs project or deal-by-deal returns
Preferred Returns	Calculated from the day capital is distributed to the point of distribution. Development: 9-12%
Promote	Waterfall distributions: Preferred return pari-passu; return pf capital; remaining proceeds split TBD based on return requirements (consider two separate waterfalls – strategy determined) of Investor
Target Returns	Leveraged returns a function of acquisition / development strategy
Investment Period	Generally now being scaled back to 1-3 years, 2-3 years for deep value-added and development
Exit Period	Evidence suggests shorter JV durations, now 5 years on average (based on real estate strategy)
Clawback Provision	The period may extend beyond the term of the venture, including liquidation and any provision for LP giveback of distributions (clawback typically to preferred return plus)
GP Commitments	LPs expect aggregate GP commitments to be "meaningful". Contributed through cash and not through a waiving of fees (95.5 or 90/10 is market)
Fees	As Managing Member, provide services to the JV entitled and entitled to receive market fees (e.g. property management, leasing, development management, acquisition)
Leverage Maximum	Averages in the 60-70% range
Governance / Discretion	Will manage the day-to-day affairs of the JV subject to decision-making authority guidelines to be set forth in a JV Operating Agreement and an approved annual business plan. The Investor will have the right to control all major decisions that would affect the property (e.g., contributions/distributions of cash flow, capital transactions, major capital programs, inter-company payments or contractual relationships, etc.)

Traditional Sources	Institutional Sources
Owner / developer personal resources Friends & Family HNW investors	Multi-family Family offices Co-mingled dedicated real estate equity funds Pension funds (public and corporate) Endowments & Foundations Life Insurance Companies Sovereign Wealth Funds Listed and unlisted REITs Hedge Funds

Real Estate Joint Venture Equity Structures (continued)

Joint Venture Economics

Capital / Limited Partners

- **Structure of hurdles and promotes can be dependent on the following:**
  - Asset type / inherent risk
  - Leverage
  - Operating experience of partner
  - Market competitive dynamics

Operating partners

- Operating Partners are paid through promoted interests and management fees
- **Sample JV terms:**
  - 95% / 5% deal to a 12% return for Capital Partner
  - 75% / 25% deal to a 18% return for Capital Partner (Operator receives a 20% promoted interest on top of their 5% initial contribution)
- Hurdles are based on IRR of one cash flow stream (generally that of the Capital Partner)
- Short term investments may have an equity multiple hurdle as well

Joint Venture Management

Capital / Limited Partners

- **Typical Major Decisions:**
  - Sales, financings & refinancing, leases, budgets / approvals of expenditures, additional capital contributions, litigation / bankruptcy, any matters outside ordinary course of business
  - Generally for 90%+ partners, most major decisions are unilateral (vs. unanimous)

Operating partners

- Management & Control is governed by an operating agreement on how to make major decisions
- Breach of other key management issues can result in removal / forfeiture events (loss of promote, punitive dilution, etc.)
- **Other key management issues:**
  - Key Man provisions
  - Duties of the operating member (General Partner)
  - Non-compete

Typical Fee Structures by Fund Type

Investment Form	Typical Fees/Structure
Real Estate Private Equity - Closed-End Pooled Vehicles	▪ 3 year investment period; 7-10 year total fund life ▪ Asset Management Fee: 150-200 bps on committed/developed equity (preferential terms available for seed investors/larger commitments) ▪ Manager typically receives a promote, or carried interest, ie an increased share of residual cash flows above an IRR/preferred return hurdle when the fund is liquidated ▪ Asset acquisition or disposition fees may be included (100-200 bps) ▪ All-in annual cost*: 250 – 400 bps
Real Estate Private Equity - Separate Accounts	▪ Asset Management fee charged as a percentage of invested/committed capital, ~100bps ▪ Acquisition or disposition fees may be included (50-200 bps) ▪ Incentive fee typically based on returns from sale of portfolio asset; tested at portfolio level ▪ All-in amount cost: 100-200 bps
Pooled investments in Directed Real Estate – typically Open-Ended	▪ 100-200 bps on net asset value ▪ Exit and entrance fee implicit in wide bid/ask spread
Real Estate Securities Funds / Separate Accounts	▪ 100-200 bps on net asset value; lower for larger accounts ▪ Some separate accounts offer performance fee structures with a significantly lower base fee and an incentive fee based on benchmark outperformance

Private Equity Expenses and Fee Structures

A private equity fund's fee structure should align investor and manager interests by incentivizing the investment manager to maximize returns for the limited partners

Customary Fees and Expenses

- Private equity funds charge an investment management fee and a performance incentive fee
  - Historically, funds charged a 2% management fee and 20% incentive fee, referred to as "2 and 20"
- The management fee covers operational management expenses, such as salaries and is usually calculated on committed capital during the investment period
  - After the investment period, the management fee is calculated on invested capital
- The performance fee is calculated based on profits and paid is paid out according to a waterfall
  - Performance fees are only paid after investor capital has been returned
  - Typically, a return hurdle must also be achieved prior to distribution
  - Performance fees can be calculated on a deal-by-deal basis or at the fund level
- Other customary fees include administrative and startup expenses
  - Administrative fee of 0.2%
  - Startup costs are shared proportionally among investors and typically capped at $1mm
- Some funds may also charge additional fees such as acquisition or sale fees

Distribution Waterfall Flow Chart

Gross fund distributions
(includes income and liquidations)

Administrative fees and fund expenses
(includes administrative fee of 0.2% and startup costs)

Management fee
(Typically 1.5% - 2.0% of committed capital)

Distributions paid to investor until original capital investment has been repaid in full

Distributions paid to investor until preferred return hurdle has been achieved

Performance fee
(Typically 20% of returns in excess of the preferred return)

Excess returns paid to investor

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