

NORTH CAROLINA  
DEPARTMENT OF STATE TREASURER



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INVESTMENT MANAGEMENT DIVISION

# Real Estate Update

May 31, 2023



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## Real Estate Team

Troy March, CCIM, MBA  
Director of Real Estate

10 Years with IMD  
21 Years Industry Experience

Casey High  
Portfolio Manager

10 Years with IMD

Chris Ward  
Analyst

9 Years with IMD



## Real Estate Sector Analysis

Risk: ● Higher ● Medium ● Lower

● Industrial	<ul style="list-style-type: none"><li>• Demand remains resilient despite economic uncertainty</li><li>• Industrial Outdoor Storage evolving into an institutional property type</li></ul>
● Data/Cell Tower	<ul style="list-style-type: none"><li>• 2022's record pace of absorption showing no signs of slowing for data centers</li><li>• AI innovation race is expected to boost demand from large global tech companies</li></ul>
● Self-Storage	<ul style="list-style-type: none"><li>• Supply starting to moderate as new development faces delays and high costs</li><li>• Occupancy has dipped below pandemic-era peak, but remains well above 10-yr average</li></ul>
● Multifamily	<ul style="list-style-type: none"><li>• Rent growth continues to be driven by prohibitively expensive for-sale market</li><li>• Tech-centric job markets pressured as layoffs continue to weigh on apartment demand in the near-term</li></ul>
● Retail	<ul style="list-style-type: none"><li>• Neighborhood, necessity-based retail still proving resilient</li><li>• A looming economic slowdown remains the largest threat to retailers</li></ul>
● Student Housing	<ul style="list-style-type: none"><li>• Reduced levels of new supply &amp; larger incoming student populations are tailwinds for the sector's rebound</li><li>• Power 5 Universities seeking Public-Private Partnerships for on- and off-campus development projects; supporting valuations</li></ul>
● Senior Housing	<ul style="list-style-type: none"><li>• Operationally intensive, but NOI margins improving as labor costs moderate</li><li>• Favorable long-term demographic tailwinds; location and quality are key</li></ul>
● Hotel	<ul style="list-style-type: none"><li>• Excess savings and pent-up business travel supportive of near-term demand</li><li>• Leisure travel has picked up, but a worsening economic backdrop and rising operating expenses are the primary risks to near-term performance</li></ul>
● Office	<ul style="list-style-type: none"><li>• Flight to quality &amp; flexible work plans for employees persist, weakening demand</li><li>• Lenders pulling away from Office resulting in muted transaction market</li></ul>



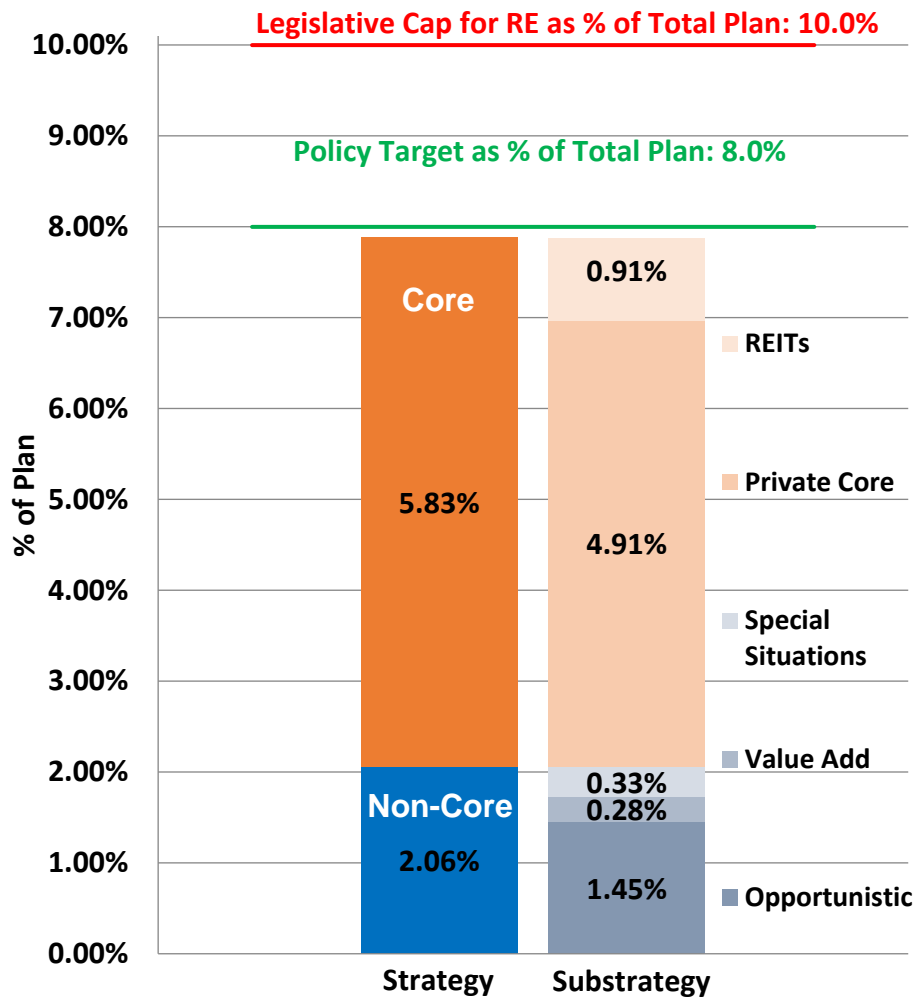
## Real Estate Investments since 3/31/2022

Closing Date	Fund Name	Commitment (millions)	Fund Type	Sector	Portfolio
Q2 2022	TPG Real Estate Fund IV	\$200	Closed-end Commingled	Global Diversified	Non-Core Opportunistic
Q2 2022	Blackstone Real Estate Partners X	\$500	Closed-end Commingled	Global Diversified	Non-Core Opportunistic
Q3 2022	BlackRock World REITs	\$300	Open-end Separate Account	Global Developed REITs	Core – Public RE
Q3 2022	Prime Storage NC	\$300	Open-end Separate Account	Self-Storage	Non-Core Value Add
Q4 2022	RXR NC	\$200	Open-end Separate Account	Mixed-Use Development	Non-Core Opportunistic

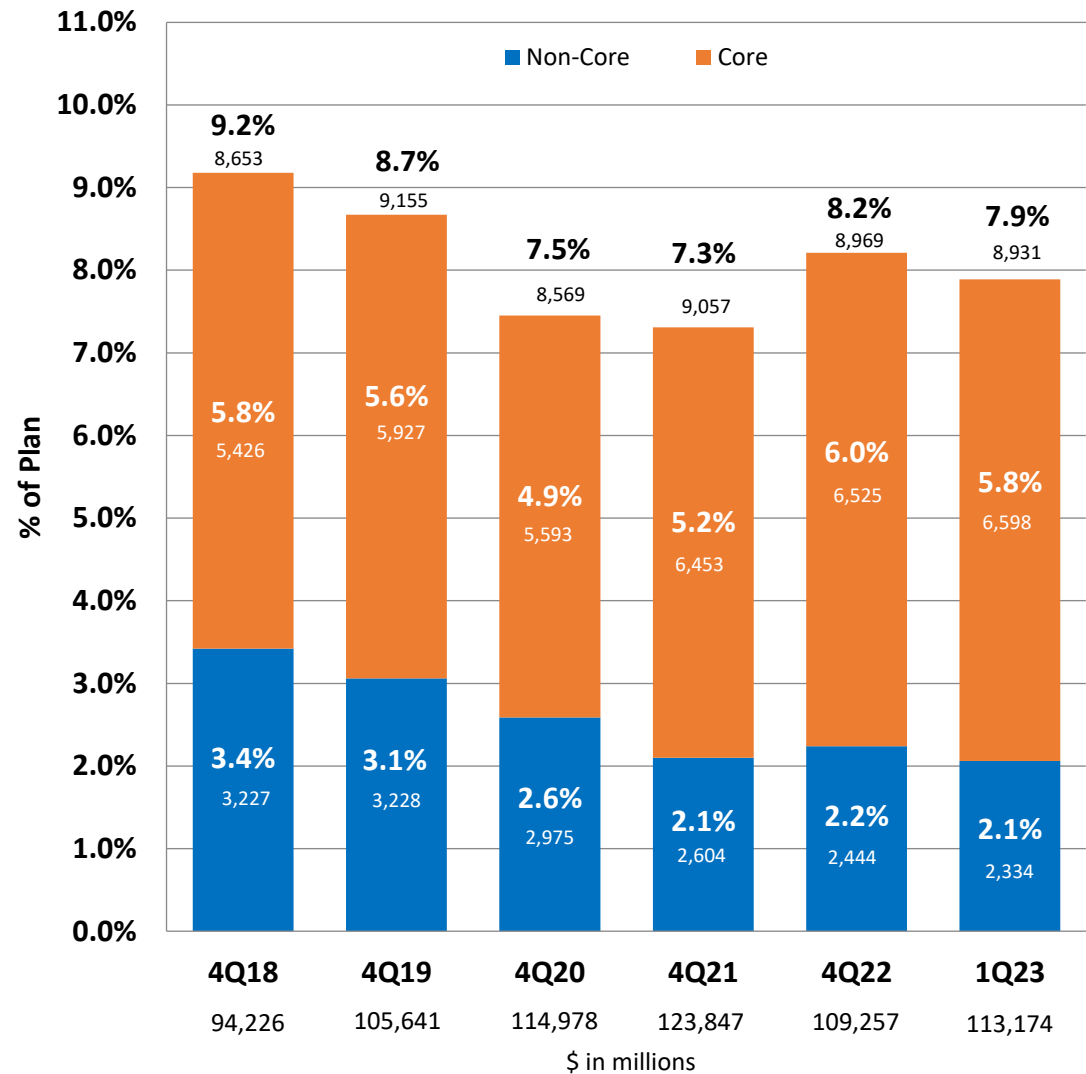
Since 3/31/2022, NCRS has made commitments totaling \$1.5B



## Real Estate Allocation



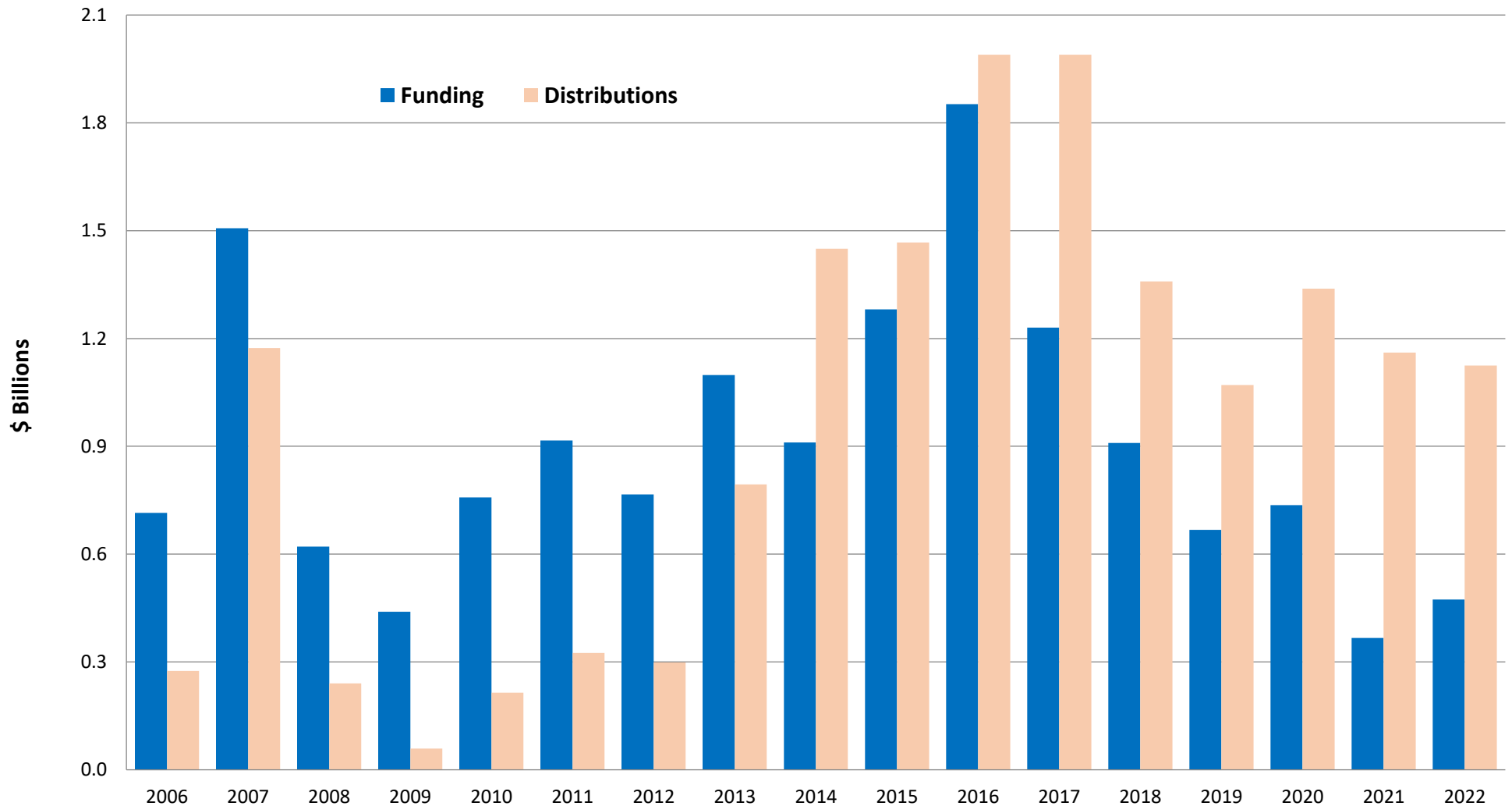
NCRS data as of 3/31/2023  
Special Situations – Build-to-Core Strategy



As of 5/16/2023, Real Estate was 7.79% of the Total Plan



## Real Estate Cash Flow

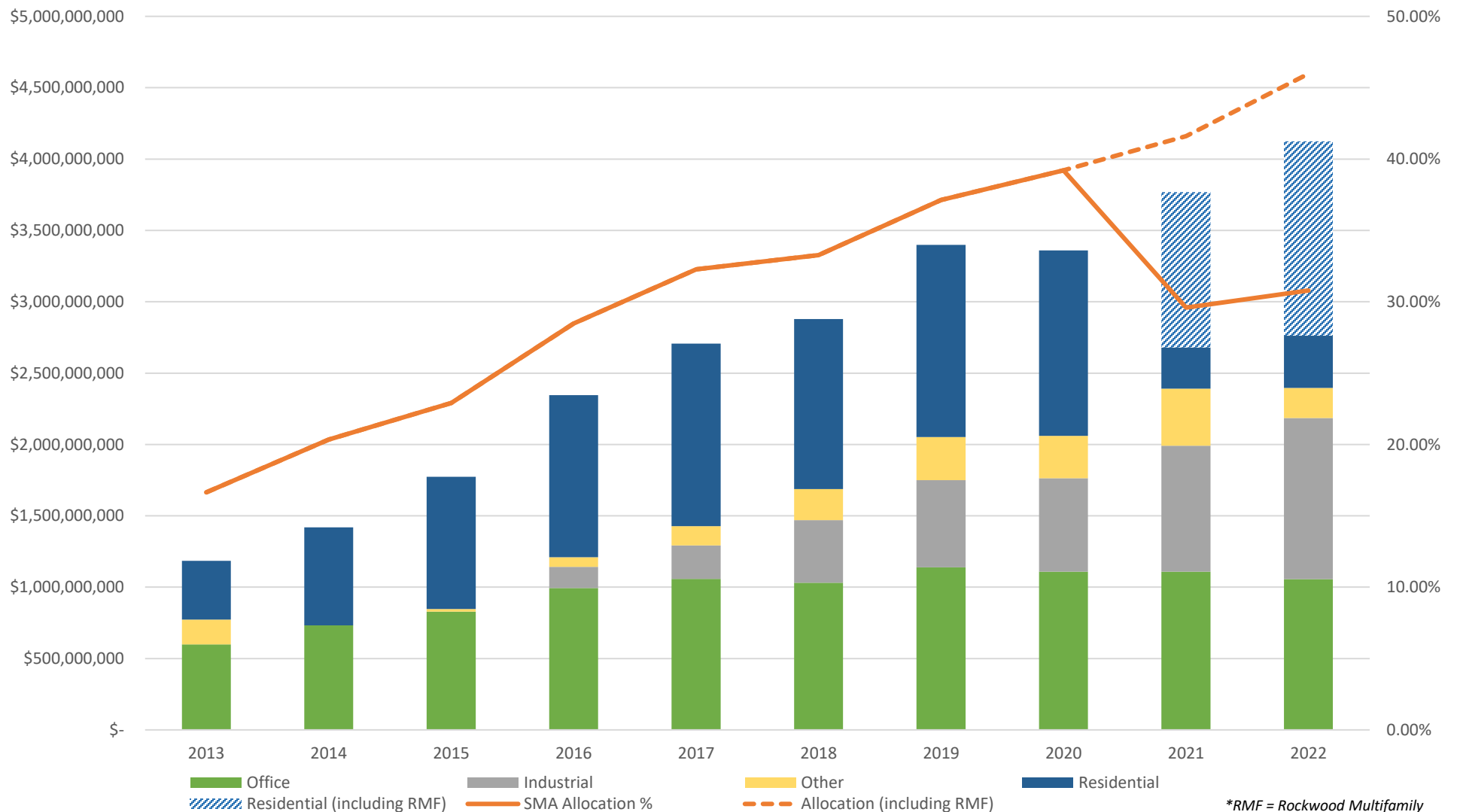


Net Cashflows (\$M):	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	(440)	(334)	(381)	(381)	(544)	(591)	(468)	(304)	539	186	138	759	449	403	602	794	651

Year-To-Date net contributions were \$225 million as of 5/16/2023. There is pent up demand to transact but frozen capital markets are limiting both investment and divestment



## Real Estate Separate Accounts (SMA)

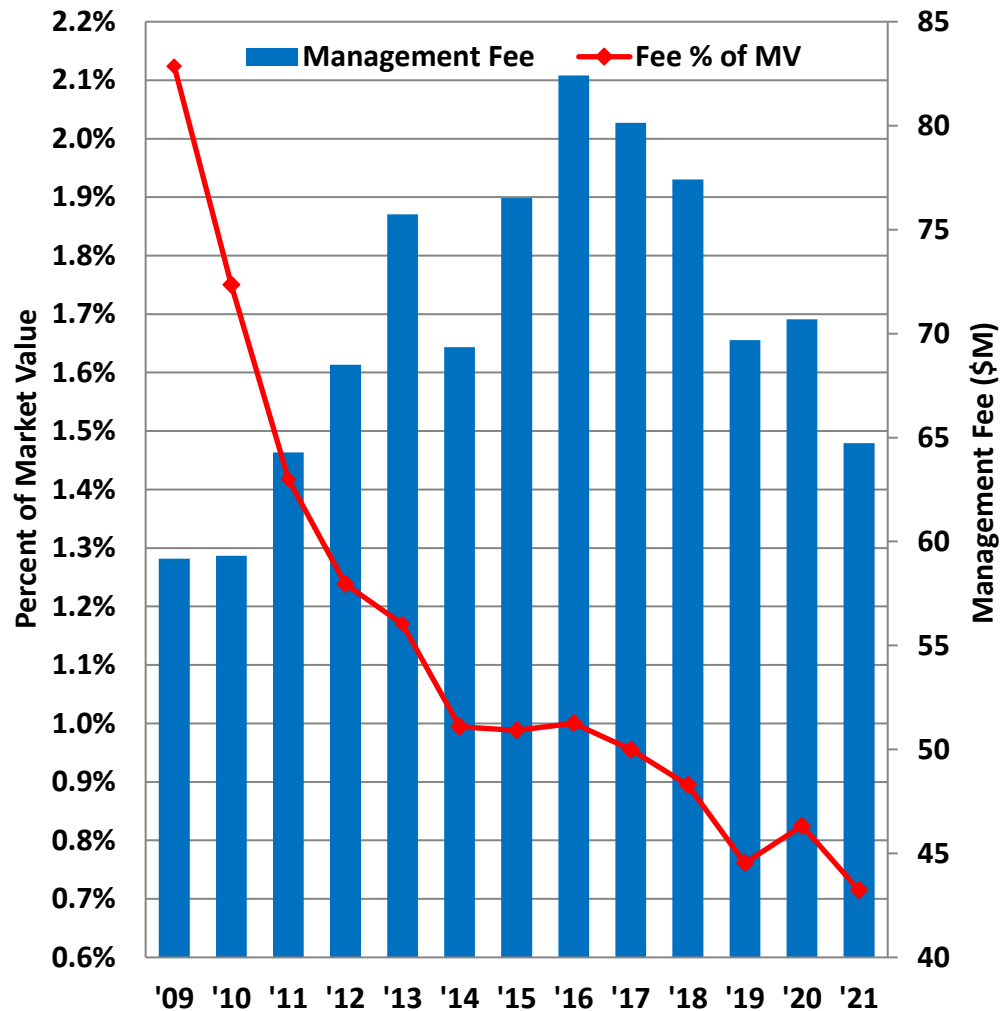


Decline in 2021 due to restructure of Multifamily SMA into Open-end Fund

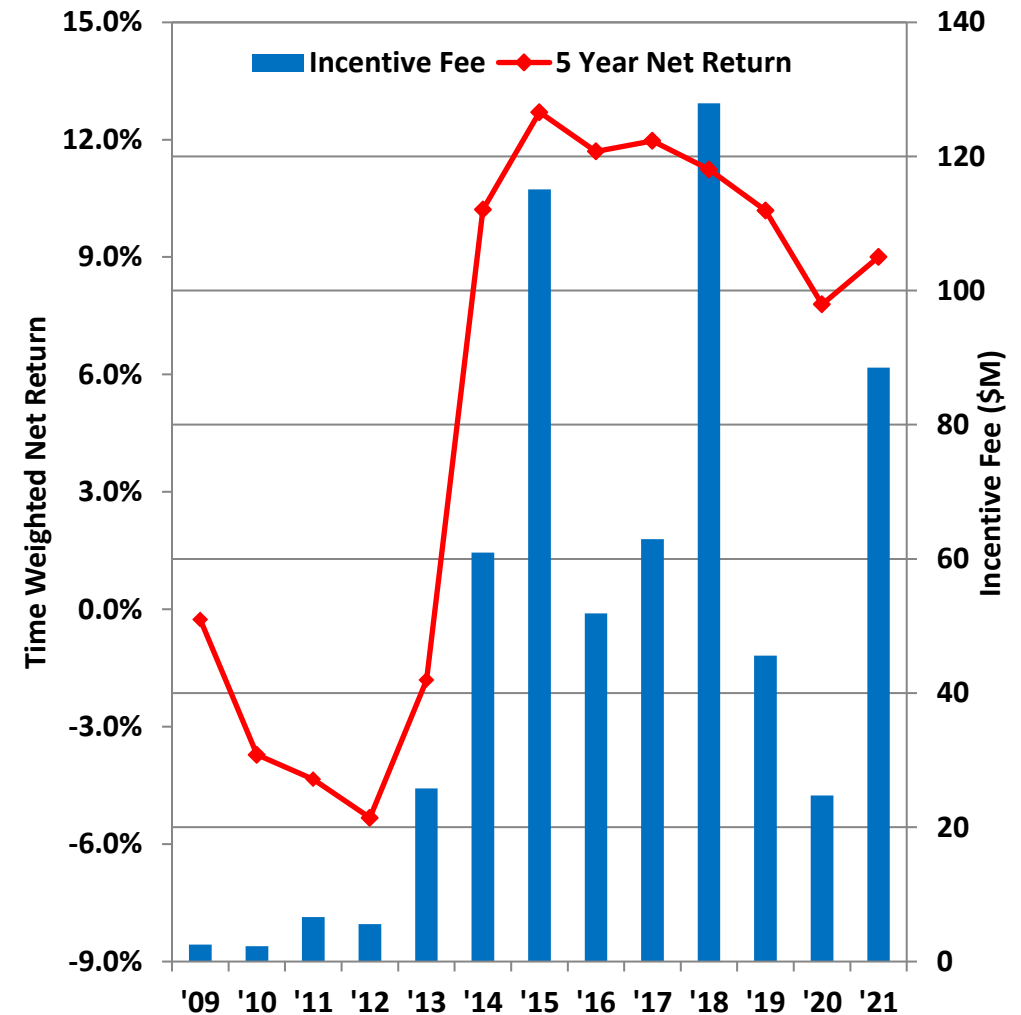




## Cost Efficiency



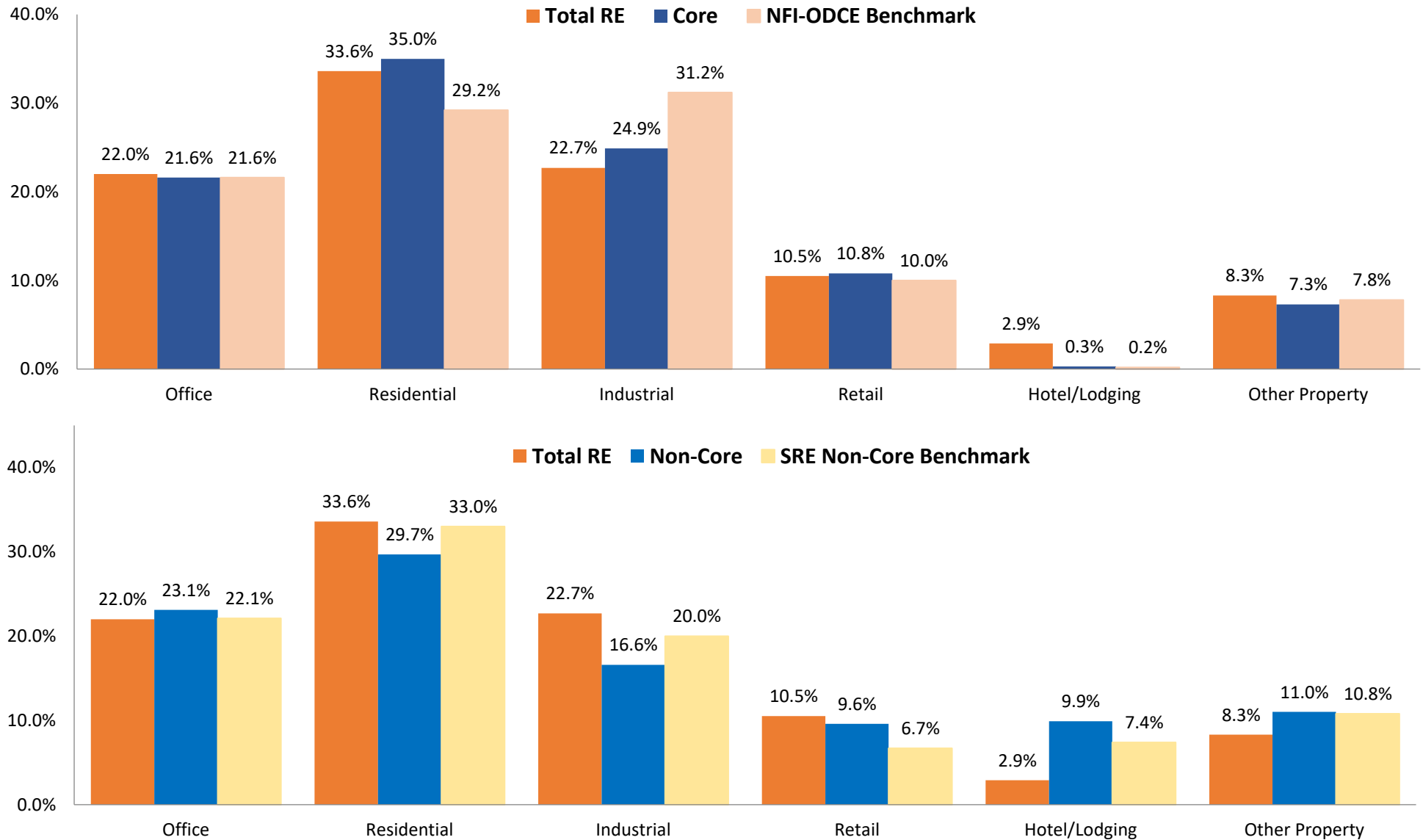
NCRS data through 12/31/2021



Fees continue to move lower as we leverage relationships and scale to minimize costs and enhance alignment

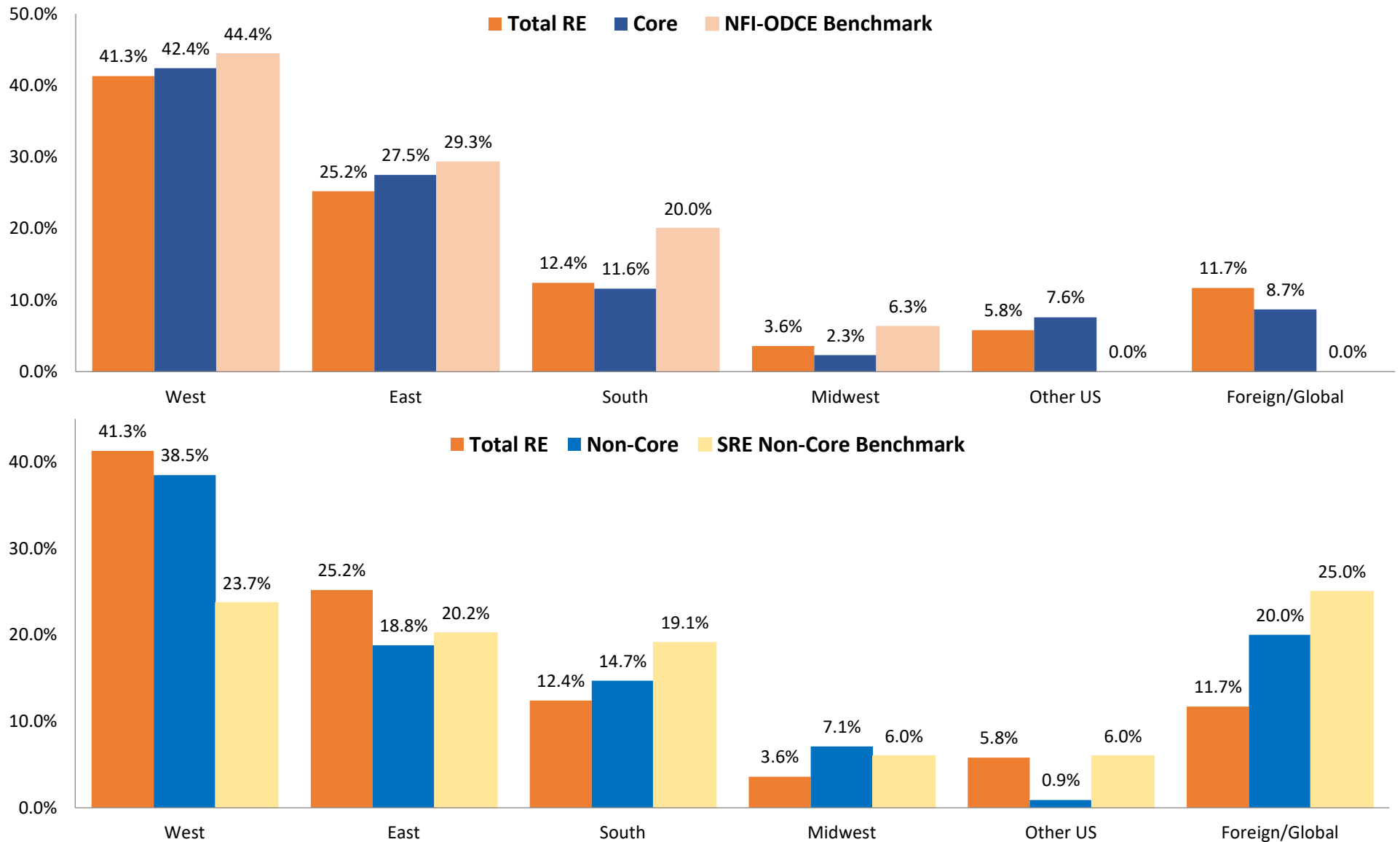


## Property Type Diversification





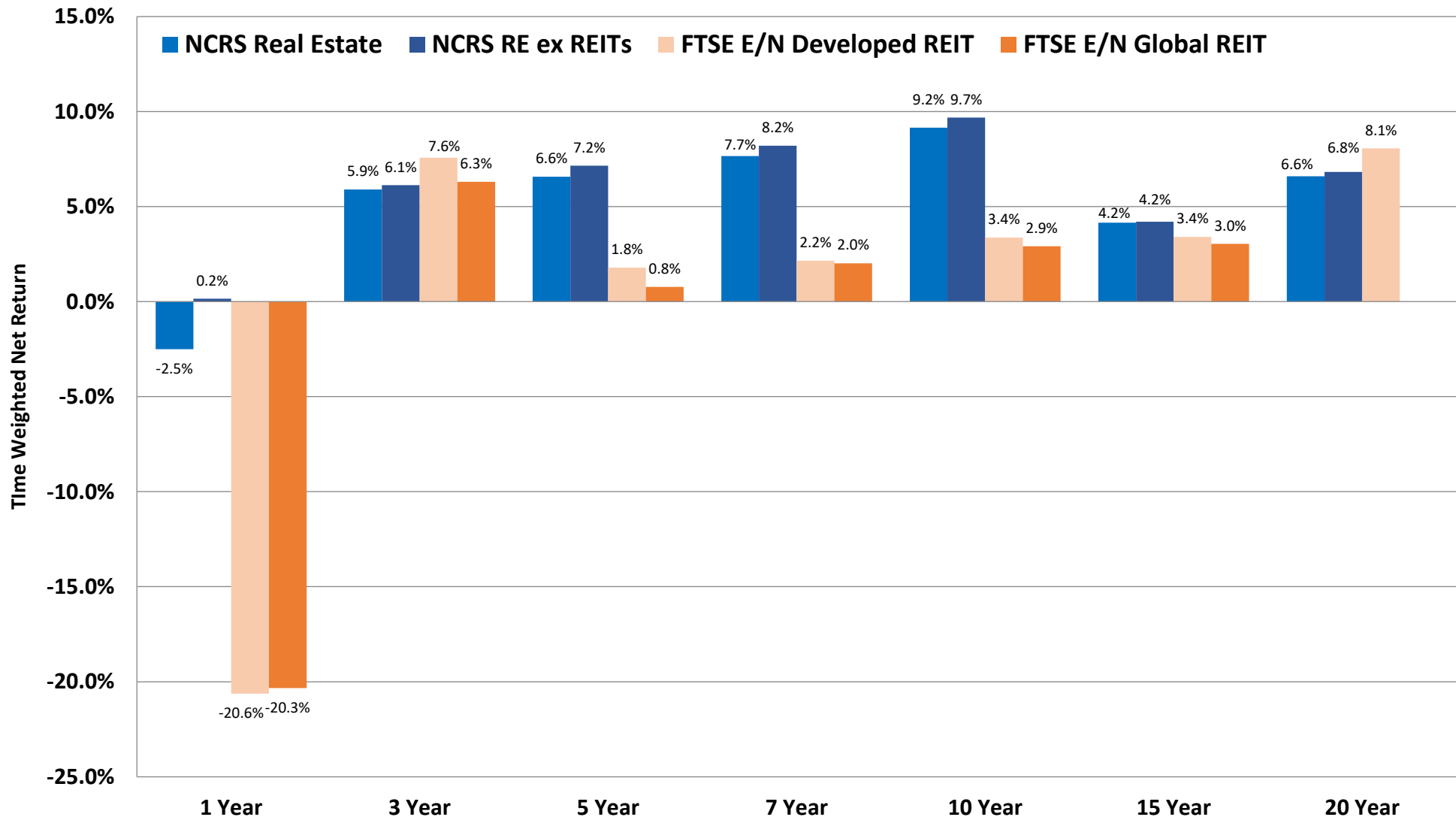
## Geographic Diversification



Source: SRE StepStone NCRS 4Q22 Portfolio Monitoring Report



## Performance: Total Real Estate vs. REITs as of 3/31/2023



NCRS data through 3/31/2023

FTSE EPRA/NAREIT Developed Index: The index serves to represent real estate equities across developed markets of North America, Europe and Asia.

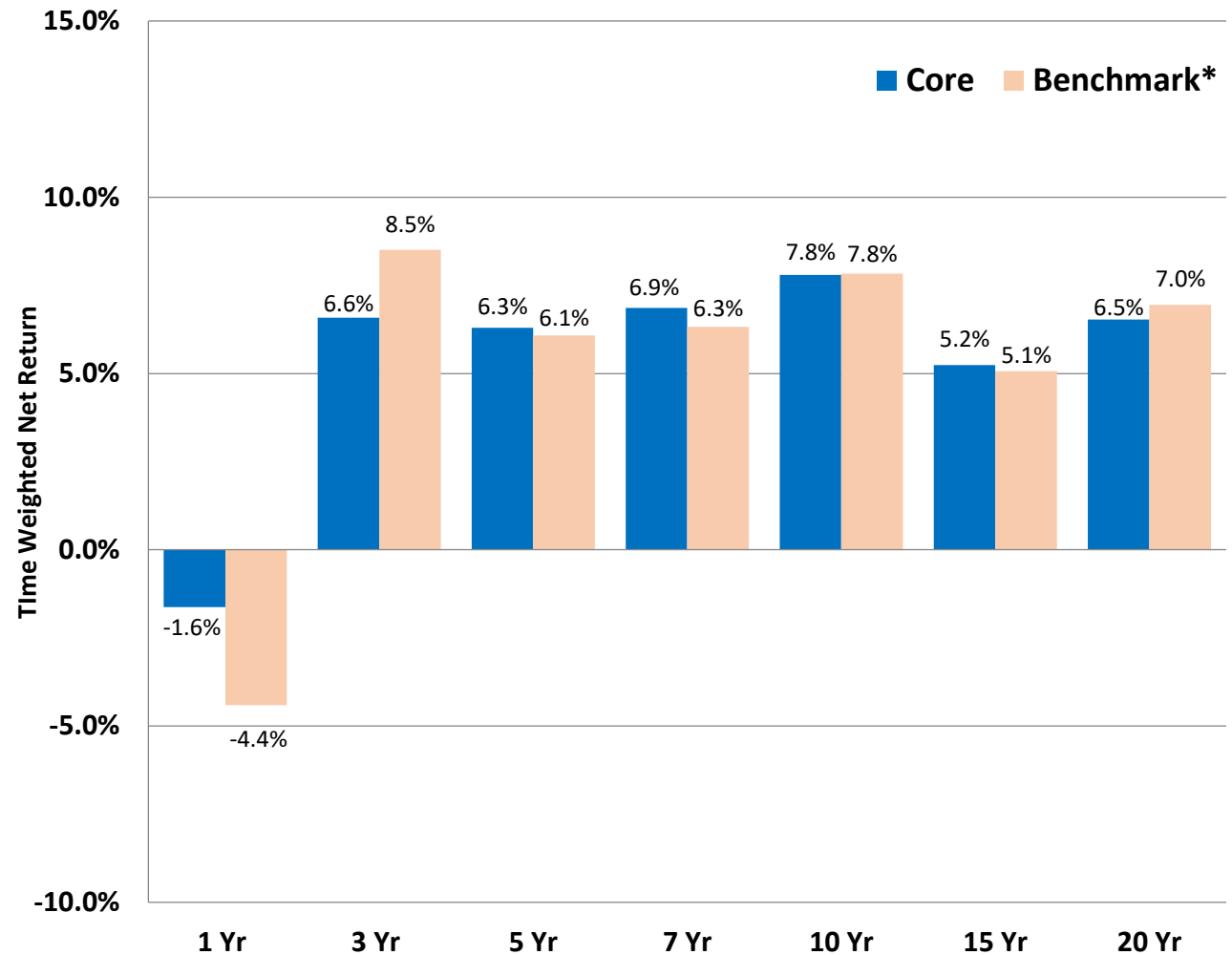
FTSE EPRA/NAREIT Global Index: The index is designed to track the performance of real estate equities in both developed and emerging markets.



## Performance: Core Real Estate

Core Contribution to Return				
3 Year			Contribution	
Private Core RE			5.5	
REITs			1.1	
Total Core			6.6	
Major Drivers		Vintage		
REIT	BR World REIT	2016	1.2	
	LBA NC Core			
PC	Industrial	2016	1.0	
	Rockwood			
PC	Multifamily	2021	0.9	
5 Year			Contribution	
Private Core RE			5.8	
REITs			0.5	
Total Core			6.3	
Major Drivers		Vintage		
	LBA NC Core			
PC	Industrial	2016	1.0	
	Blackstone			
PC	Property Partners	2008	0.7	
PC	NorthRock Core	2008	0.6	

NCRS data through 3/31/2023



\* The Core Real Estate Benchmark is comprised of 80% NCREIF ODCE Net and 20% FTSE EPRA NAREIT Global Index.

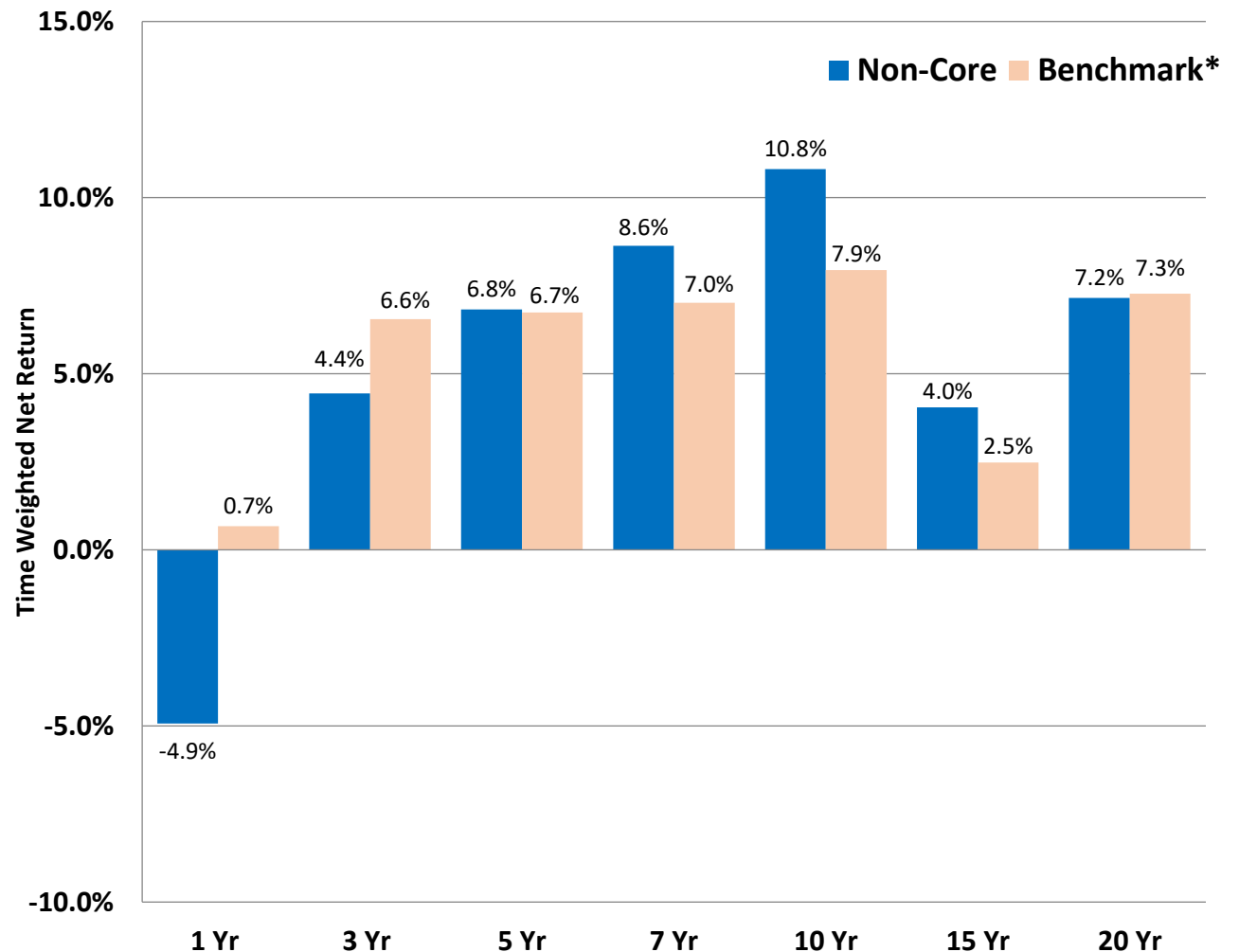
Strong performance from Industrial, Multifamily, & Retail in the 1-Year period helped to offset poor performance of Office & Global REITs



## Performance: Non-Core Real Estate

Non-Core Contribution to Return			
3 Year		Contribution	
Opportunistic		2.7	
Value Add		1.7	
Total Non-Core		4.4	
<u>Major Drivers</u>		<u>Vintage</u>	
O	BREP IX	2019	1.7
O	BREP VIII	2015	1.0
Rockwood Dev			
V	Partners	2016	1.0
5 Year		Contribution	
Opportunistic		4.2	
Value Add		2.6	
Total Non-Core		6.8	
<u>Major Drivers</u>		<u>Vintage</u>	
Rockwood Dev			
V	Partners	2016	1.0
O	BREP IX	2019	0.9
O	BREP VIII	2015	0.9

NCRS data through 3/31/2023

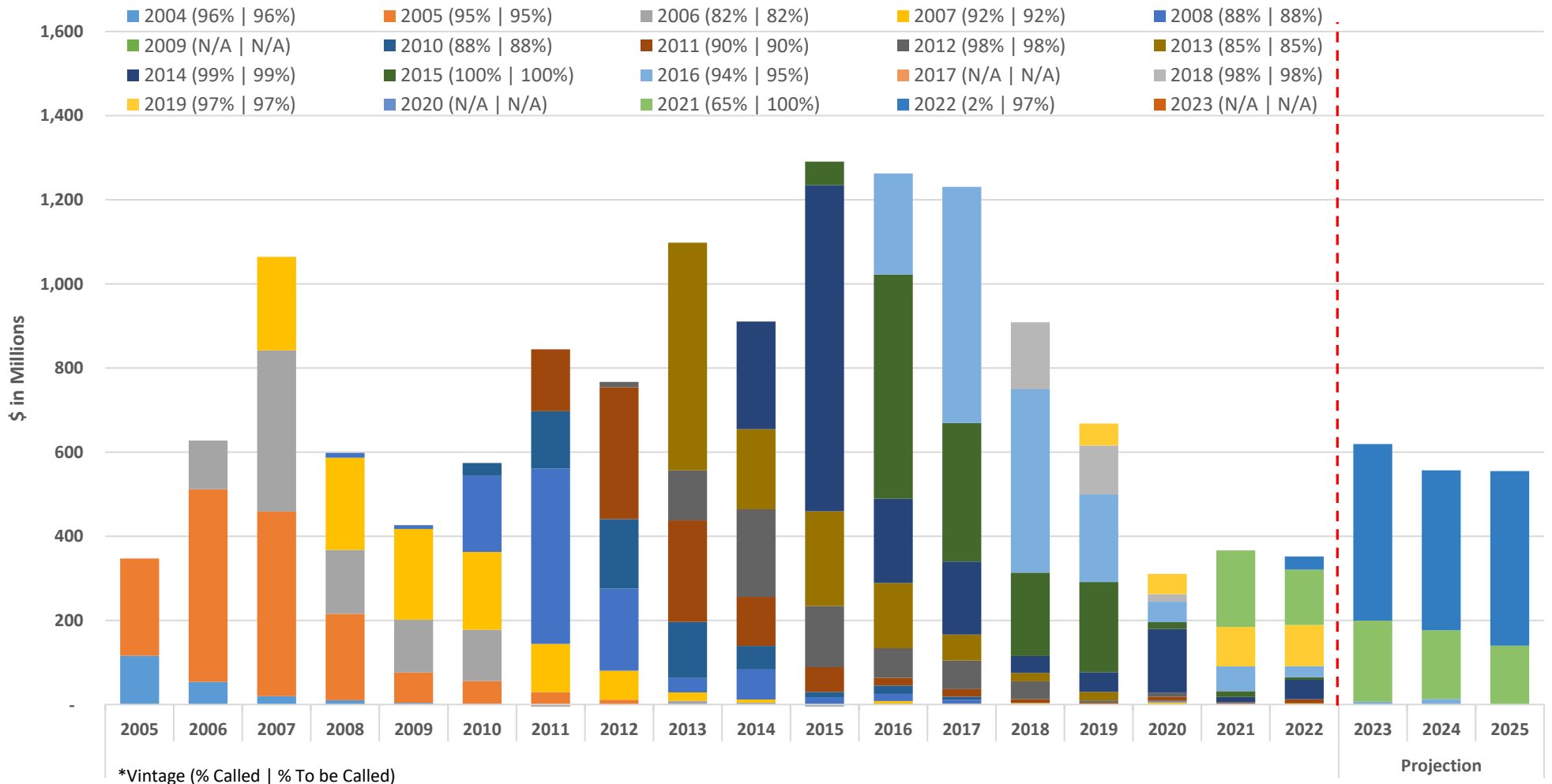


\* Non-Core Real Estate Benchmark is comprised of the following Burgiss Group Private iQ indices: 80% U.S. Non-Core Real Estate (Opportunistic and Value-Added) and 20% Non-U.S. Non-Core Real Estate (Opportunistic and Value-Added).

Underweight to Industrial and legacy vintage year exposure contributed to near term underperformance



## Unfunded Commitment Pacing by Vintage Year (excludes REITs)



Committed Amounts (\$M): 1,584 1,077 1,641 1,057 0 653 1,052 695 1,417 1,769 1,367 2,265 0 300 300 0 482 1,200

NCRS data through 12/31/2022

\*Commitments are considered "Vintage" the year in which the first \$ of capital is drawn

Of the \$2.1 billion of unfunded commitments, we expect ~\$1.5 billion to be called and the remainder held as reserves



### Investment Strategy Objectives

- Continued focus on Separate Accounts and reducing manager count
- Minimize costs and maximize returns by favoring partnership structures that optimize alignment of interests
- Increase exposure to public real estate while security prices are still trading below net asset values
- Increase exposure to both high growth and low capex sectors: Industrial, Multifamily, Self-Storage, Small Strip Center Retail
- Decrease exposure to high capex and macro-challenged sectors: Office, Retail, and Hotel





## Appendix

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## Role and Objectives

### Core Thesis

*"To generate durable income and stable returns through strategic investments, with prudent use of leverage, in assets with long-term fundamental drivers that will endure for generations"*

### Investment Strategy

High Quality  
Well-Located  
Strong Risk-Adjusted Returns

### Non-Core Thesis

*"To achieve attractive risk-adjusted net returns through appreciation and income from a diversified portfolio, planning for strategic exit optionality"*

## Core

Inflation hedge

High current income

Stabilized occupancy

Credit tenancy

Long-term return > fixed income

Minimal risk/downside protection

## Non-Core

Growth diversifier

Opportunity to add value

Renovation, development, leasing

Stabilized upon completion

Long-term appreciation and returns

Low correlation to fixed income



## Investment Approach

Stay the course with our investment strategy...do not reach for yield

- Downside protection
- Eye toward current income for Core or “speed to income” for Opportunistic strategies
- Moderate leverage levels

Use thoughtful & deliberate portfolio construction

- Stabilized Core portfolio
- Diversify by strategy, property sector, size, vintage year and location
- Balance asset risk and market risk by insisting on the highest asset quality and location
- Target specific submarkets and streets

Leverage the size of our plan

- Better terms and fees
- More transparency and control
- Ability to move quickly to capitalize on opportunities and dislocations
- Be the founding investor for new strategies with high conviction managers

Invest meaningful amounts with fewer best-in-class managers

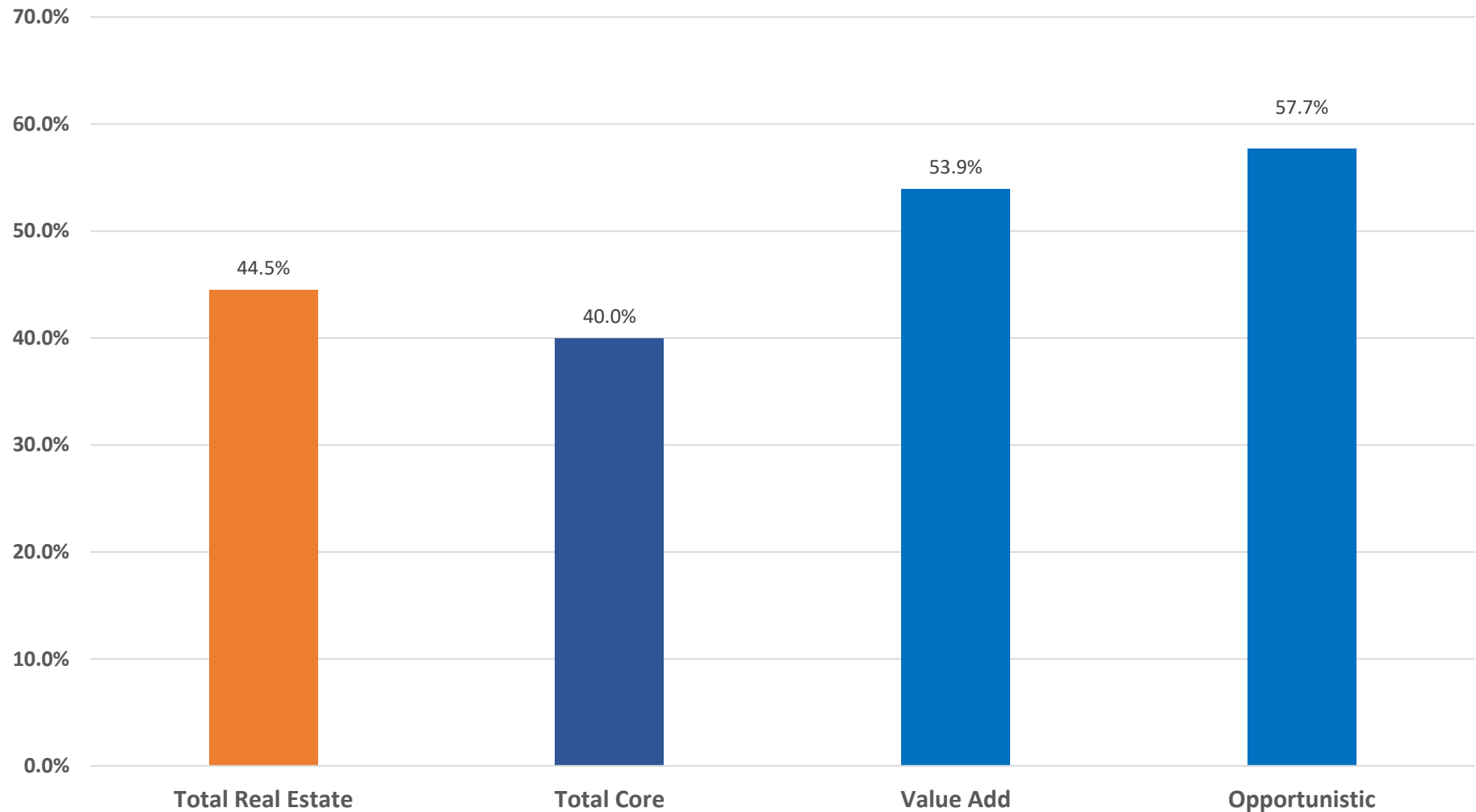
- Separate accounts
- Multiple strategies with single manager
- Fee benefits

Take a long-term view toward investments and manager relationships

- Be involved, nimble and follow through
- Deliver results
- Be a leader among Limited Partners



## Leverage



Source: SRE StepStone NCRS 4Q22 Portfolio Monitoring Report

Maintain prudent levels of leverage and retain ability to adjust through our separate accounts