

NORTH CAROLINA
DEPARTMENT OF STATE TREASURER



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INVESTMENT MANAGEMENT DIVISION

Real Estate Update

May 25, 2022



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Real Estate Team

Troy March, CCIM, MBA
Director of Real Estate

9 Years with IMD
20 Years Industry Experience

Casey High
Portfolio Manager

9.5 Years with IMD

Chris Ward
Analyst

8 Years with IMD



Real Estate Sector Analysis

Risk: ● Higher ● Medium ● Lower

● Industrial

- Insatiable demand for infill distribution
- Industrial Outdoor Storage evolving into an institutional property type

● Self-Storage

- Unprecedented demand has outstripped high supply levels
- Diversified and sticky tenant base driving recent demand wave

● Multifamily

- Relative affordability ratios have improved in favor of apartment rentals over homeownership in the top-50 metros
- Chronic undersupply creating opportunities for SFR/BTR

● Data/Cell Tower

- Data center vacancy at record low levels
- Expanding 5G coverage driving demand that shows no sign of slowing

● Student Housing

- Campuses continue operating on a mix of remote and in-person basis
- Reduced levels of new supply & larger incoming student populations are tailwinds for the sector's rebound

● Office

- Flight to quality & migration from Gateway to Non-Gateway markets
- Flexible work plans still evolving & affecting Office demand

● Senior Housing

- Operationally intensive; NOI margins are narrower than other property types
- Demographics tailwinds expected to increase over the next decade

● Retail

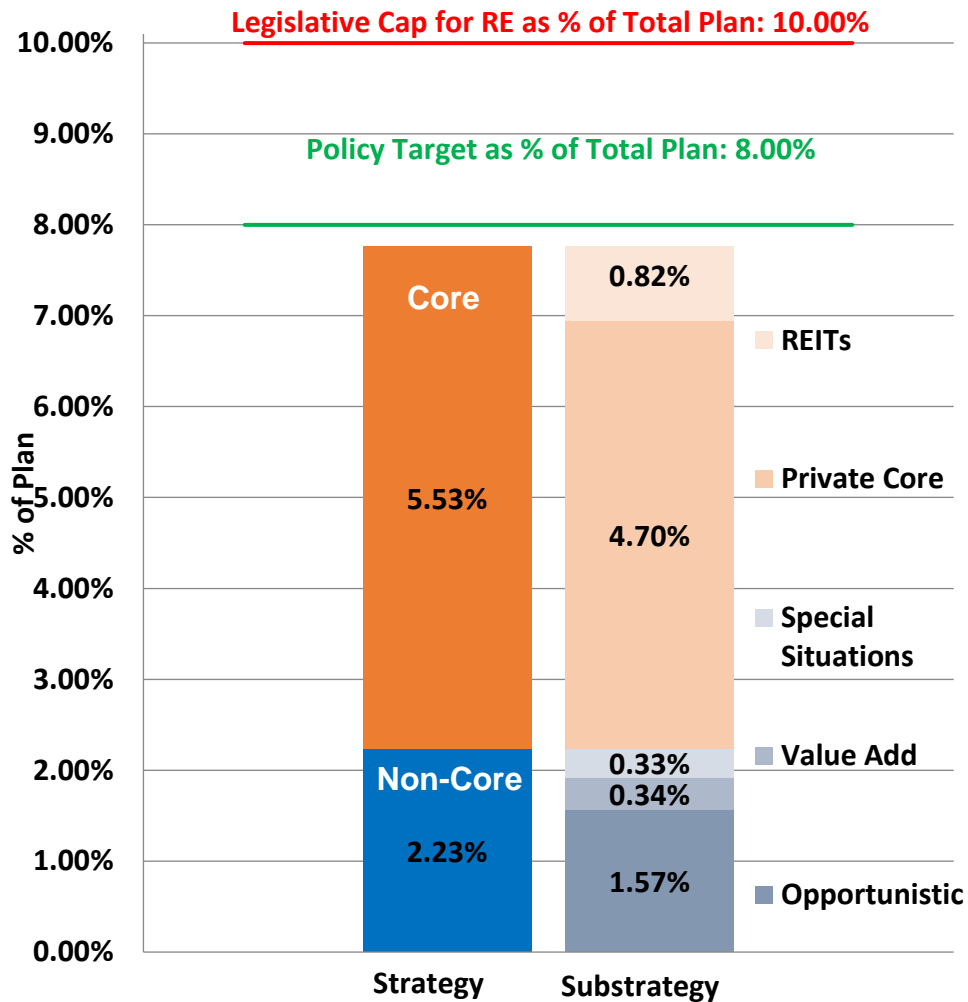
- Neighborhood, necessity-based retail still proving resilient
- Retail is bouncing back but supply overhang will hold down rent growth for years

● Hotel

- Business travel has increased but still lags pre-pandemic levels
- Leisure travel has picked up meaningfully, but staffing remains a challenge

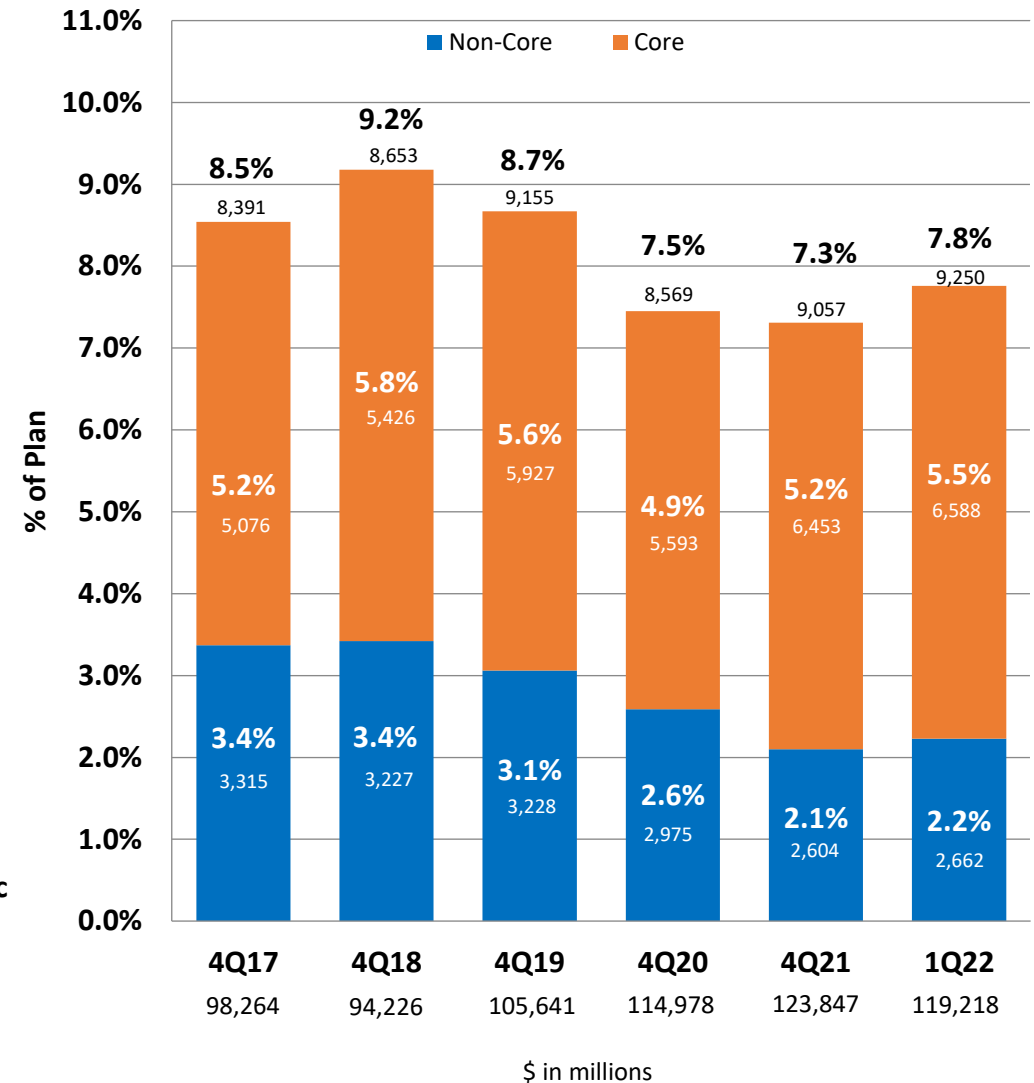


Real Estate Allocation



NCRS data as of 3/31/2022

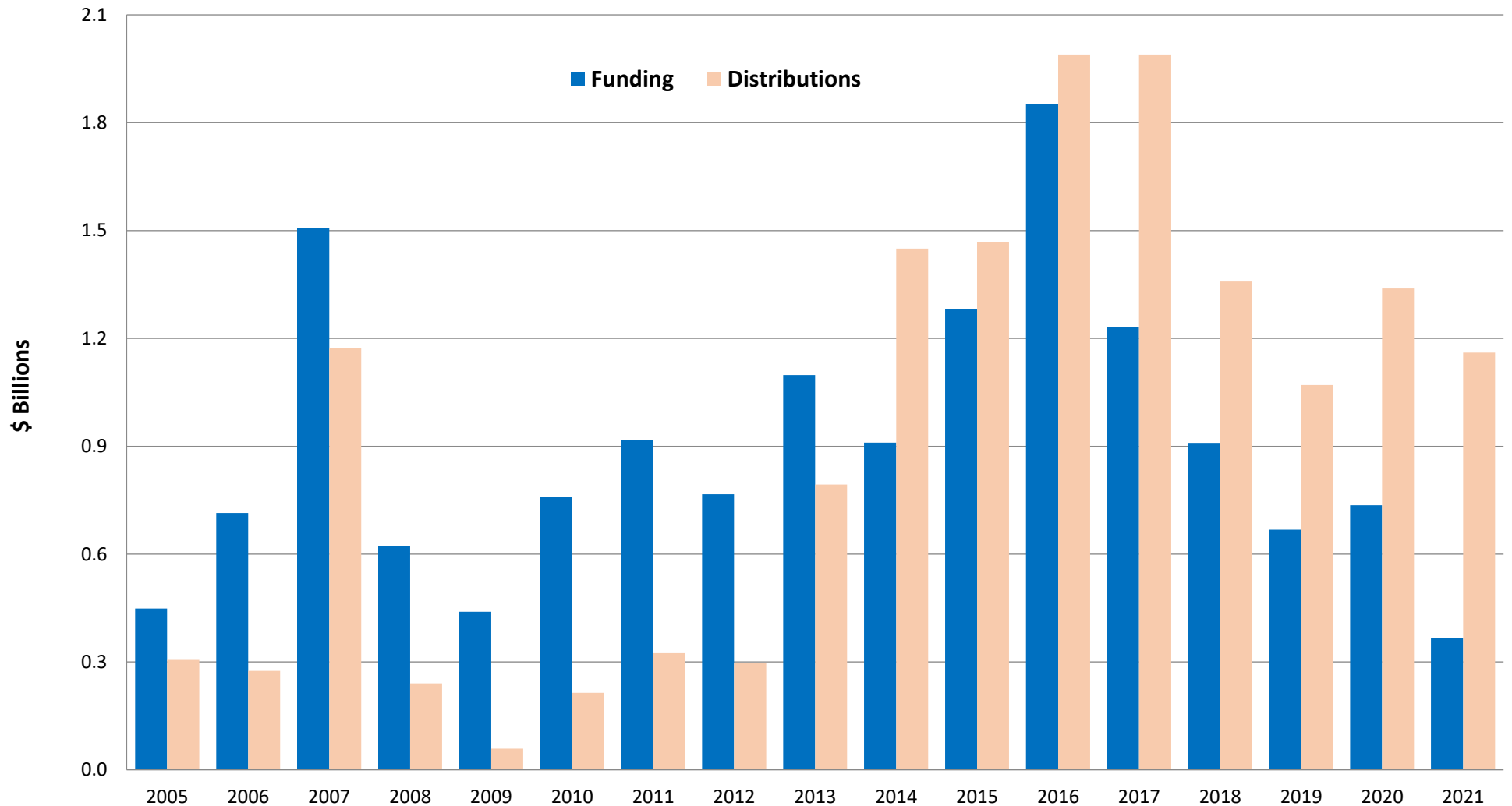
Special Situations – Build-to-Core Strategy



As of 5/6/2022, Real Estate was 8.04% of the Total Plan. RE Allocation has grown in 2022 due to Denominator Effect.



Real Estate Cash Flow



Net Cashflows (\$M):	(143)	(440)	(336)	(381)	(381)	(544)	(591)	(468)	(304)	539	186	138	759	449	403	602	794
Year	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021

Year-To-Date net distributions were \$423 million as of 5/6/2022. Pent up demand to transact likely to result in significant return of capital in 2022.

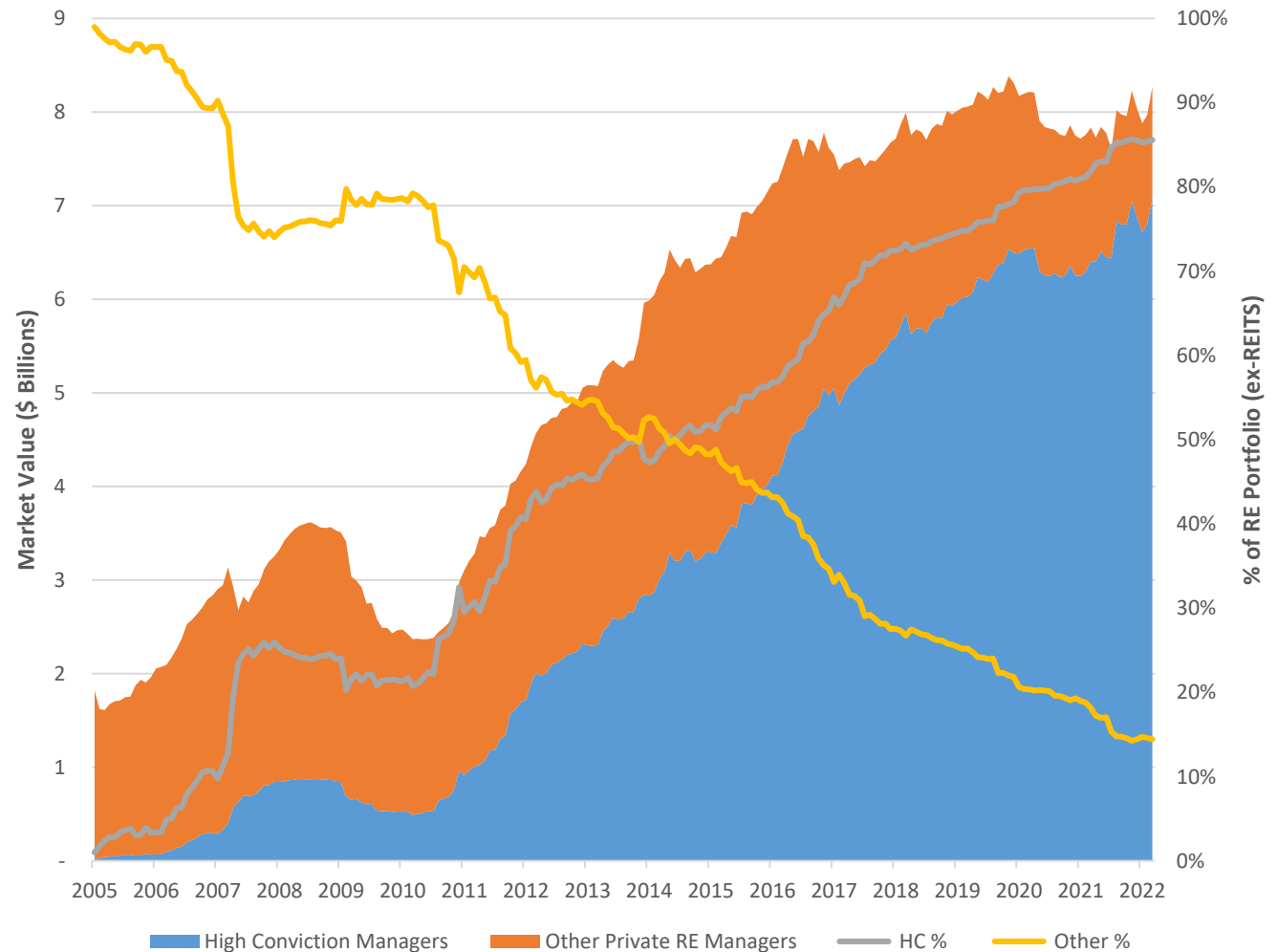


Manager Concentration (excludes REITs)

Contribution to Return			
	3 Year	5 Year	7 Year
Private Core	8.9	8.3	8.6
High Conviction	8.9	7.7	6.5
Others	0.0	0.6	2.1
Non-Core	10.0	10.9	11.7
High Conviction	9.5	9.8	9.7
Others	0.5	1.1	2.0

* "High Conviction" Managers are identified by the Real Estate Team as General Partners with the highest probability of meeting/exceeding expected fund-level returns

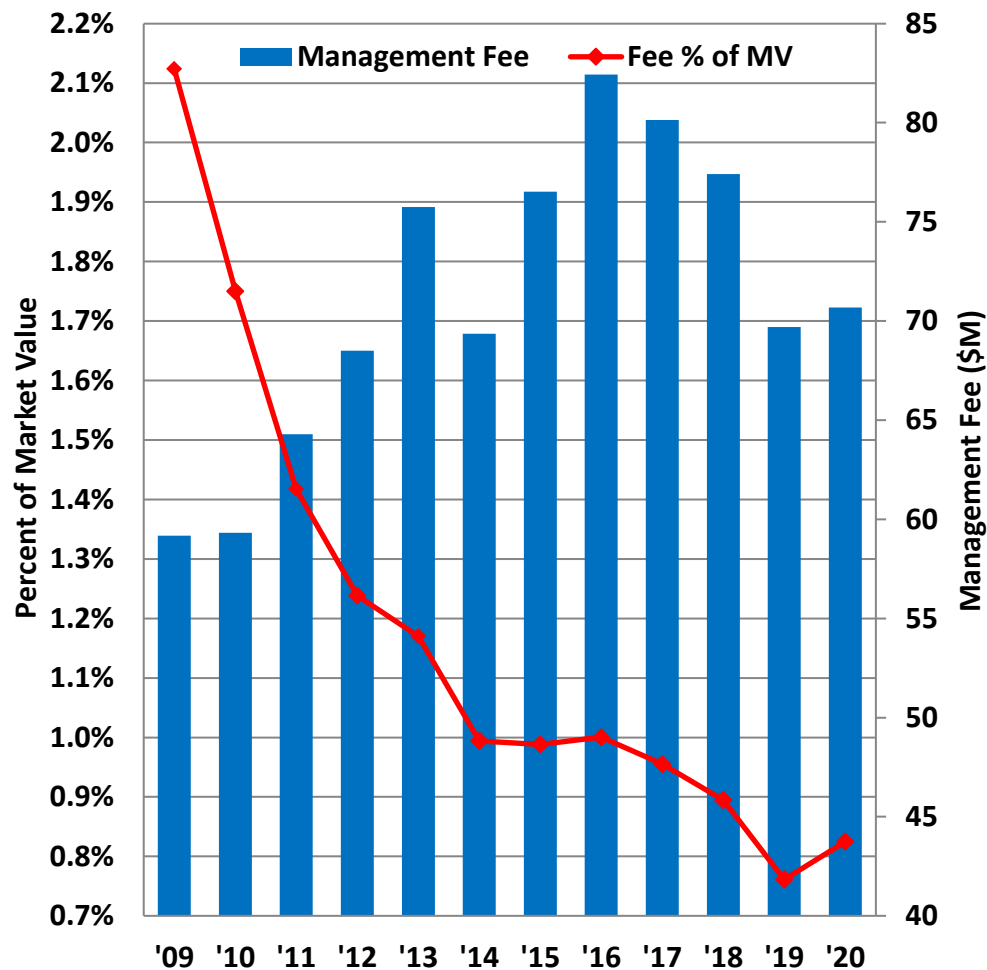
NCRS data through 3/31/2022



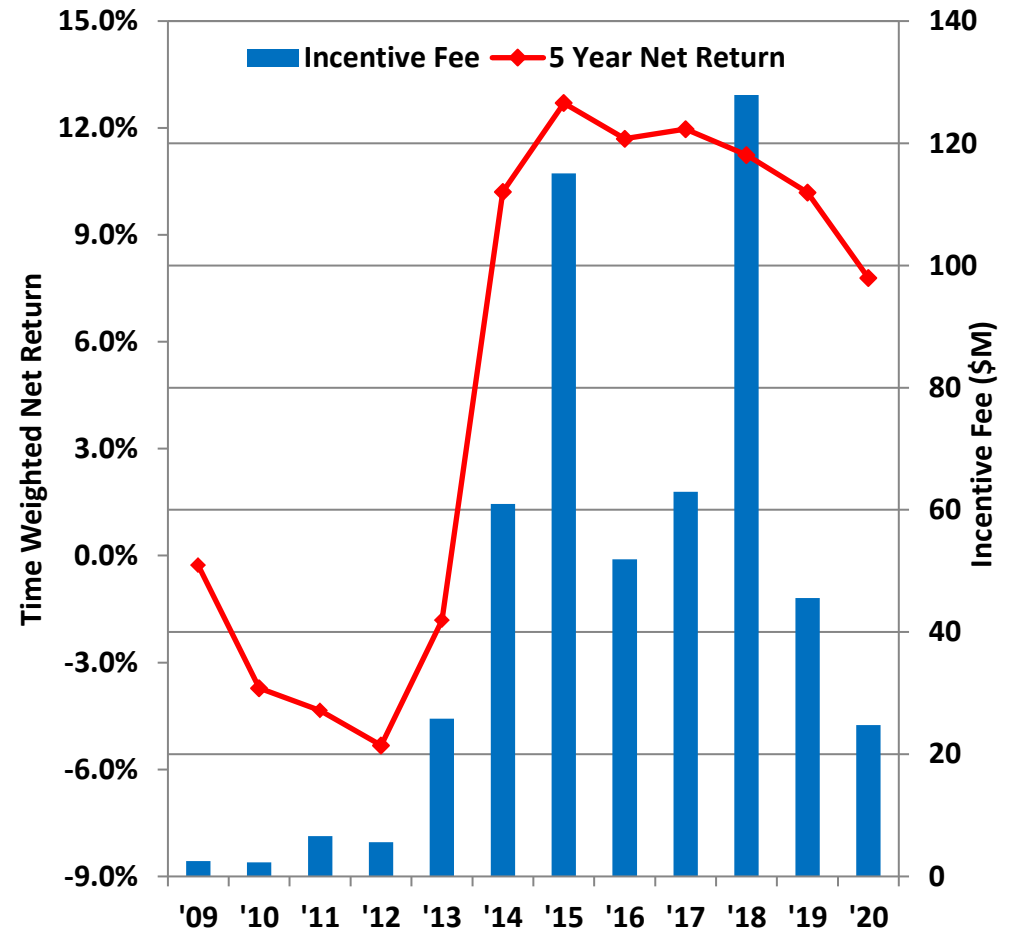
86% of private market value is with high conviction managers –
Concentration helps reduce complexity and fees, increases transparency, and improves returns



Cost Efficiency



NCRS data through 12/31/2020



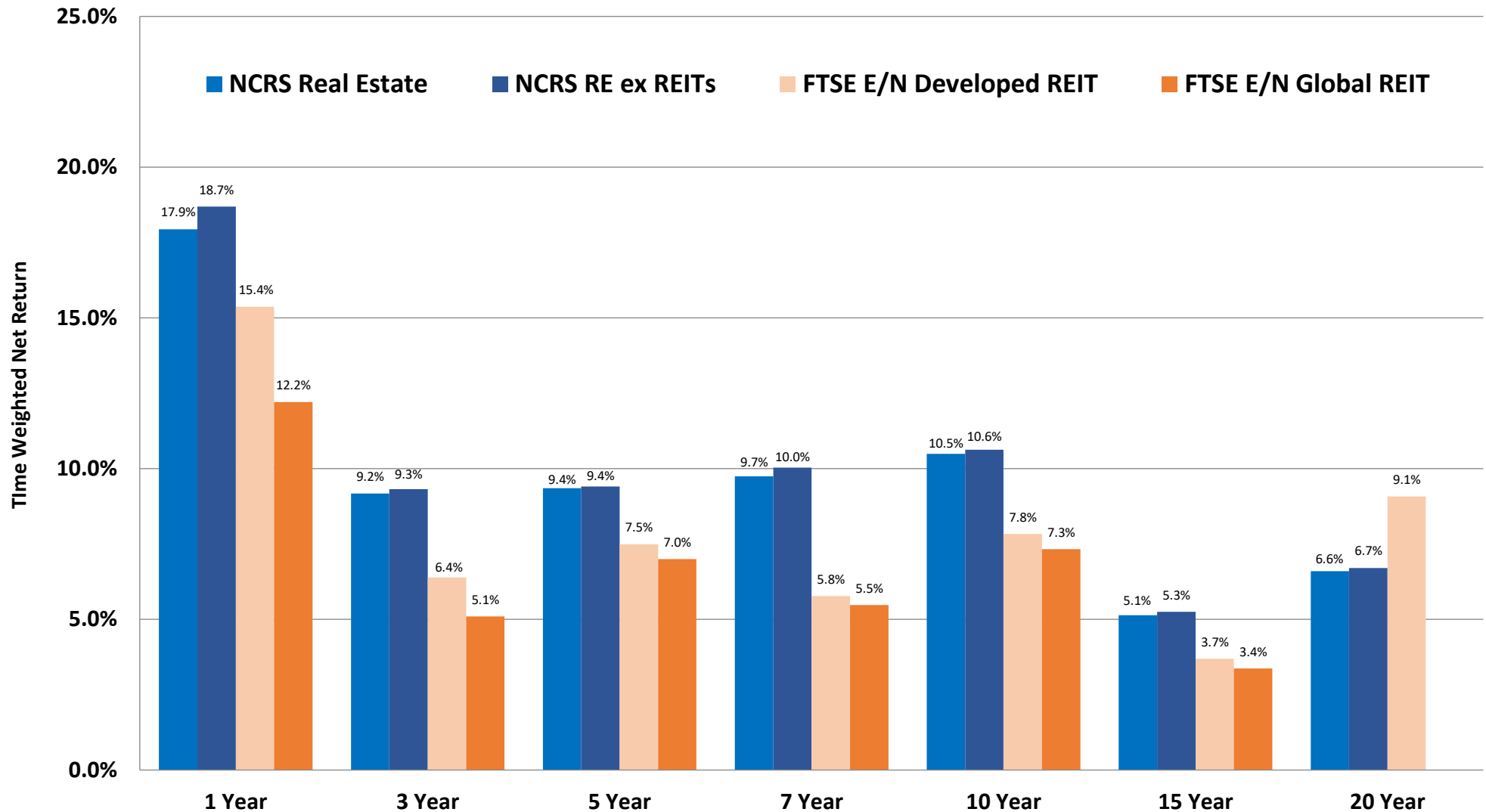
2015: Convergence of delayed realization of GFC funds, early realization of post-GFC funds, and an Industrial manager selling their entire platform

2018: Realization of a large, successful, platform investment

Fees remain low as we leverage relationships and scale to minimize costs and enhance alignment



Performance: Total Real Estate vs. REITs as of 3/31/2022



NCRS data through 3/31/2022

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

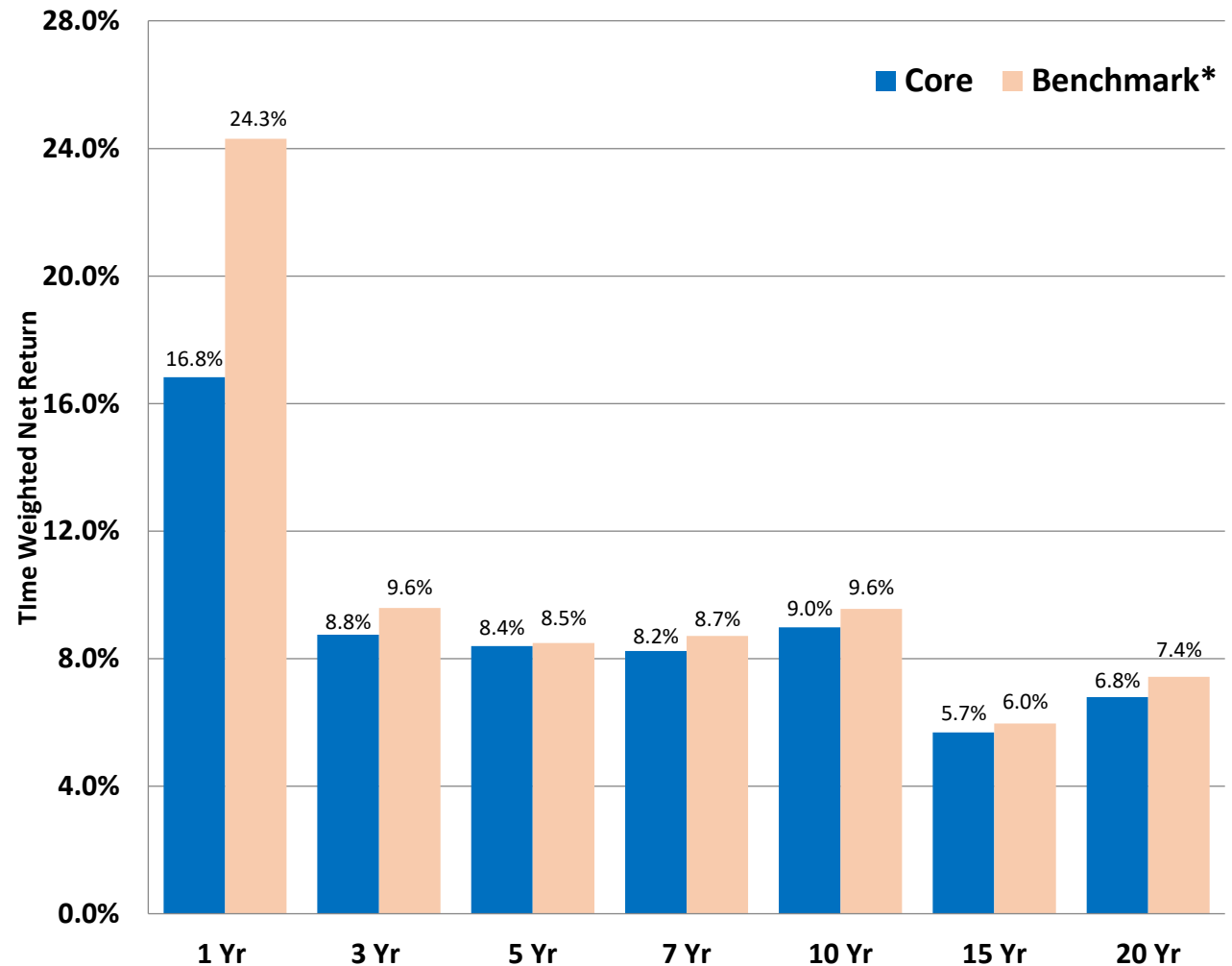
FTSE EPRA/NAREIT Global Index: The index is designed to track the performance of real estate equities in both developed and emerging markets.



Performance: Core Real Estate

Core Contribution to Return			
3 Year			Contribution
Private Core RE			7.5
REITs			1.3
Total Core			8.8
<u>Major Drivers</u>		<u>Vintage</u>	
LBA NC Core			
PC	Industrial	2016	1.4
REIT	BR World REIT	2016	1.3
PC	NorthRock Core	2008	1.1
5 Year			Contribution
Private Core RE			7.0
REITs			1.4
Total Core			8.4
<u>Major Drivers</u>		<u>Vintage</u>	
PC	NorthRock Core	2008	1.2
LBA NC Core			
PC	Industrial	2016	1.0
REIT	BR World REIT	2016	0.9

NCRS data through 3/31/2022



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

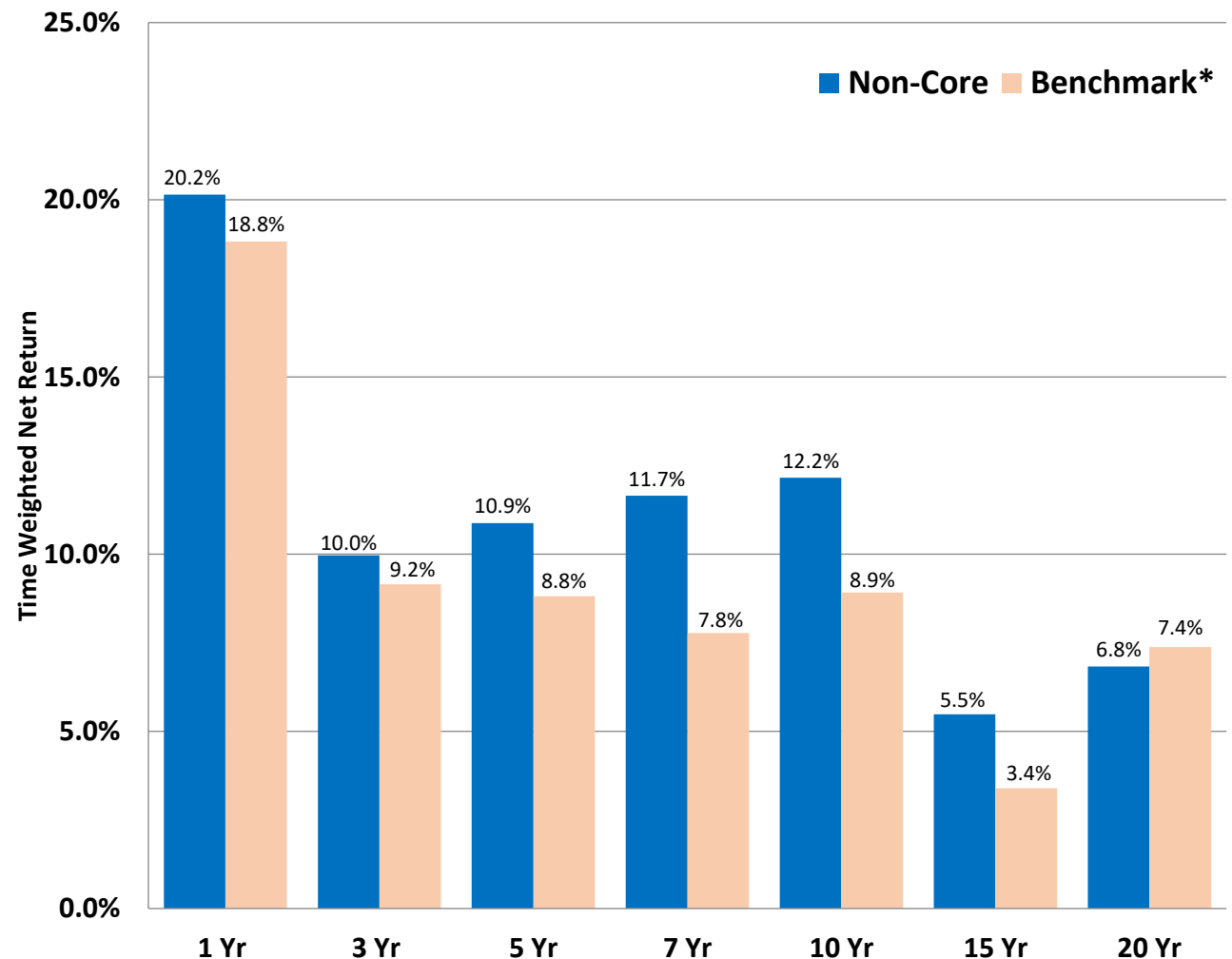
Significant underweight to Industrial was the primary detractor to performance



Performance: Non-Core Real Estate

Non-Core Contribution to Return			
3 Year			Contribution
Opportunistic			5.9
Value Add			4.1
Total Non-Core			10.0
<u>Major Drivers</u>		<u>Vintage</u>	
Rockwood Dev			
V	Partners	2016	1.9
O	BREP VIII	2015	1.2
O	BREP IX	2019	1.2
5 Year			Contribution
Opportunistic			7.2
Value Add			3.7
Total Non-Core			10.9
<u>Major Drivers</u>		<u>Vintage</u>	
Rockwood Dev			
V	Partners	2016	1.0
O	NorthCreek	2011	1.0
O	BREP VIII	2015	0.9

NCRS data through 3/31/2022

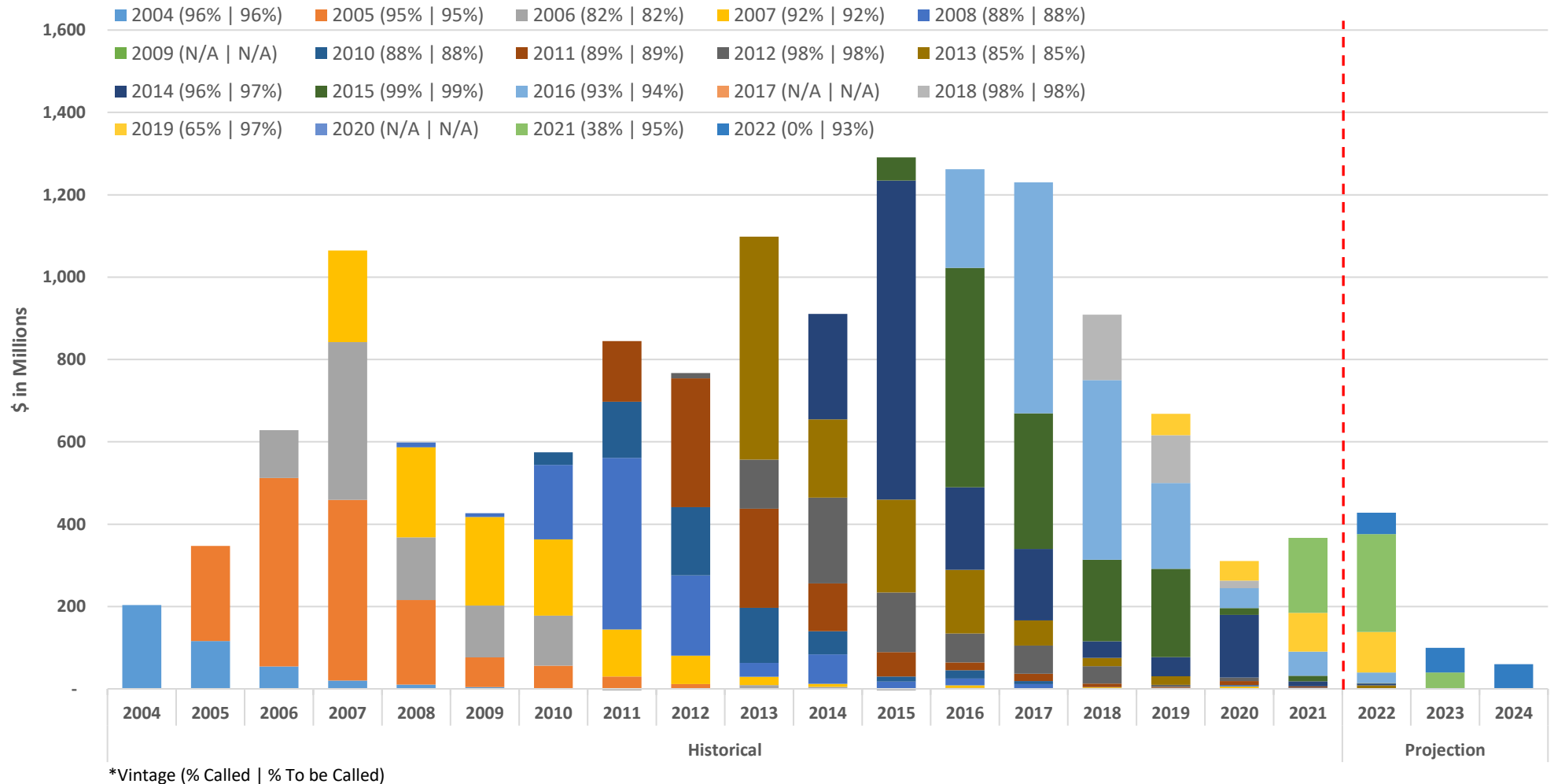


* Non-Core Real Estate Benchmark is comprised of the following Burgiss Group Private iQ indices: 80% U.S. Non-Core Real Estate (Opportunistic and Value-Added) and 20% Non-U.S. Non-Core Real Estate (Opportunistic and Value-Added).

Non-Core performance bounced back strong after a lackluster year prior



Unfunded Commitment Pacing by Vintage Year (excludes REITs)



Commits (\$M): 430 1,567 1,077 1,641 1,057 0 653 1,052 695 1,417 1,769 1,367 2,265 0 300 300 0 482 200

NCRS data through 12/31/2021

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

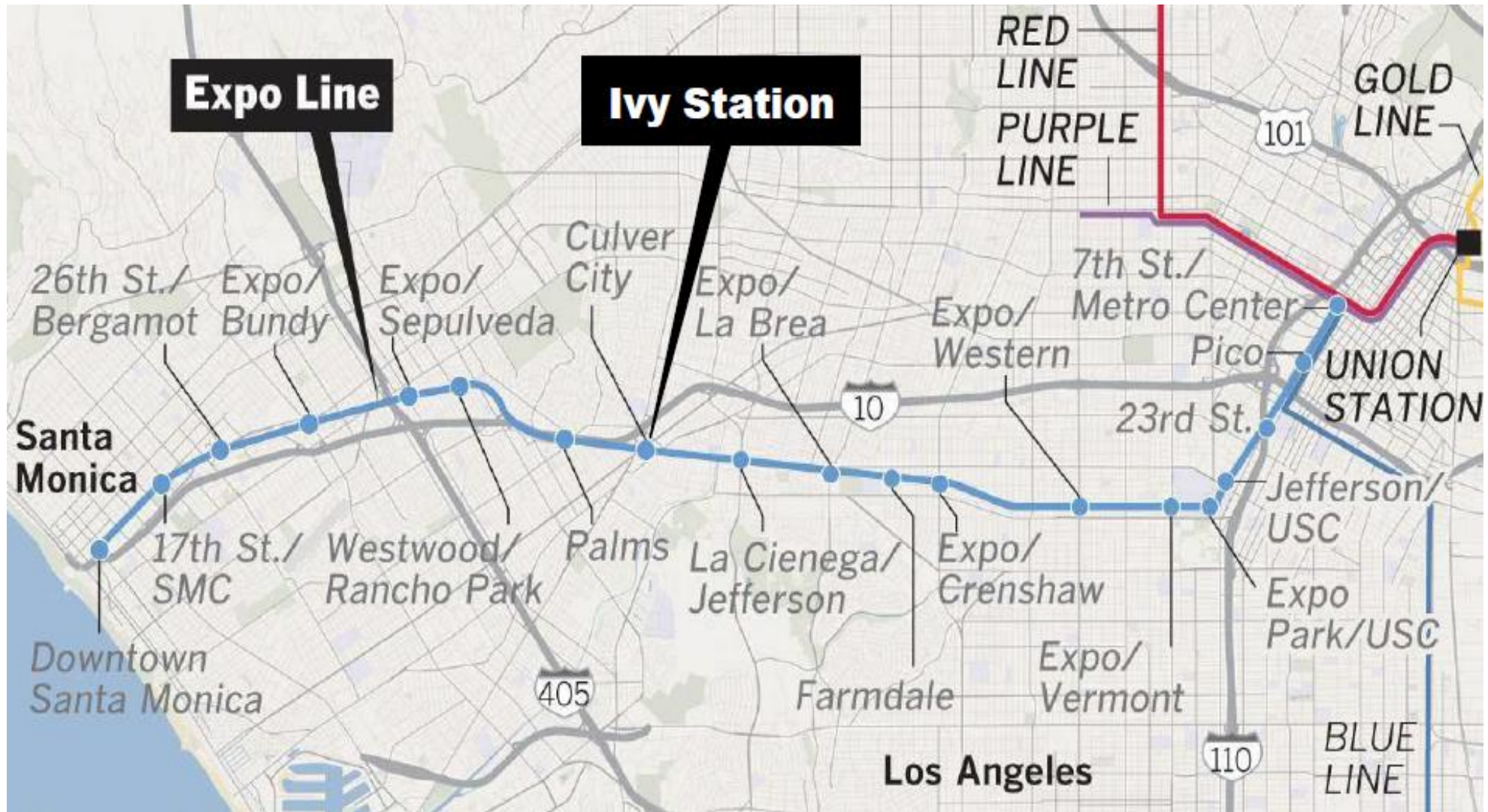
Of the \$1.4 billion of unfunded commitments, we expect ~\$600M to be called and the remainder left as reserves



Build-To-Core Program Case Study: Ivy Station

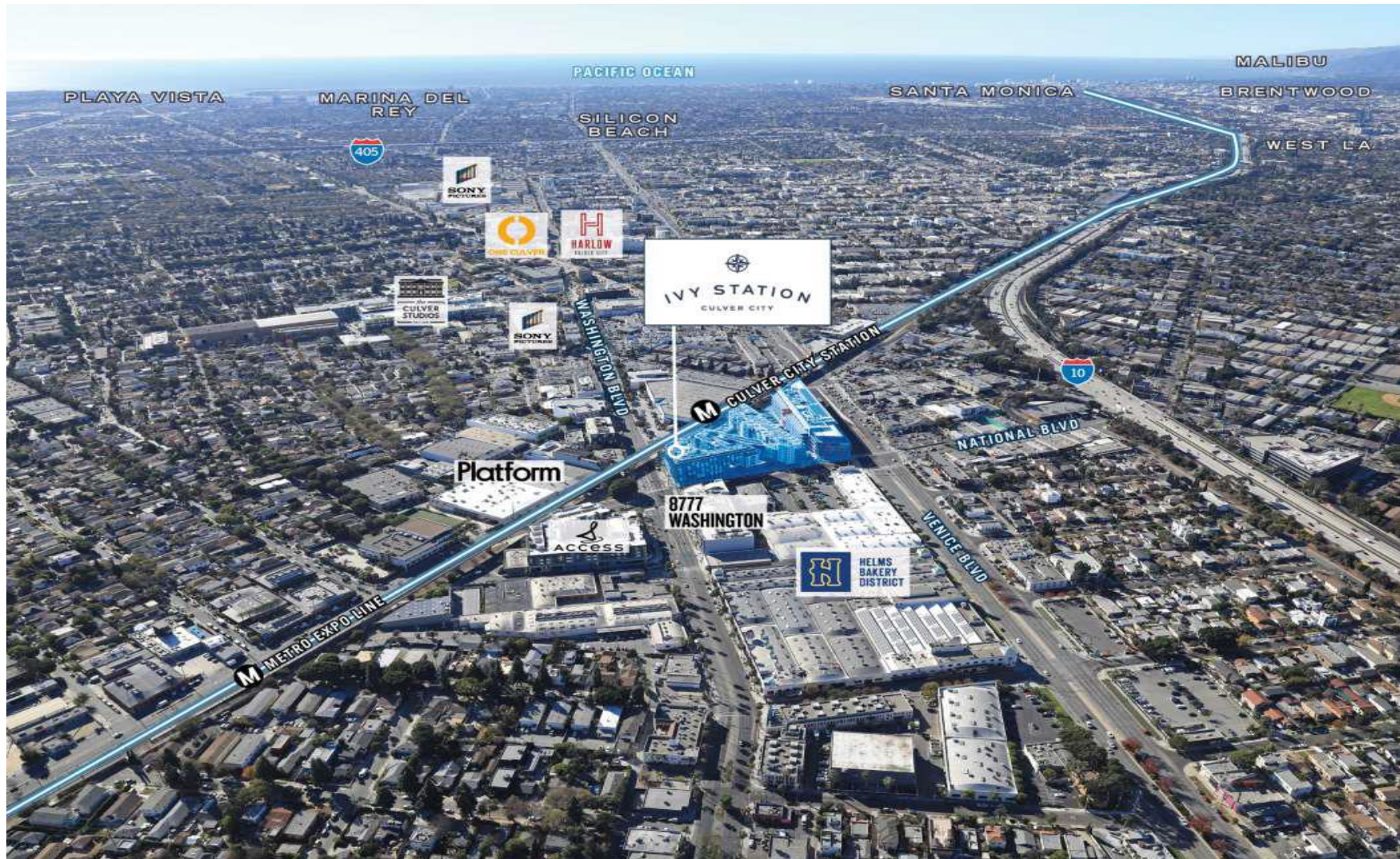


Ivy Station Development – Expo Line Map





Ivy Station Development – Aerial View





Ivy Station Development – Plaza-Level Site Plan



Source: Rockwood Capital Partners



Ivy Station Development – Completed Project



Source: Rockwood Capital Partners



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 through a “completion portfolio” concept for public REIT investment to help gain exposure to sectors where we are underweight
- Increase exposure to both high growth and low capex sectors: Industrial, Multi-family, Self-Storage
- Decrease exposure to high capex and macro-challenged sectors: Office, Retail, and Hotel



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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

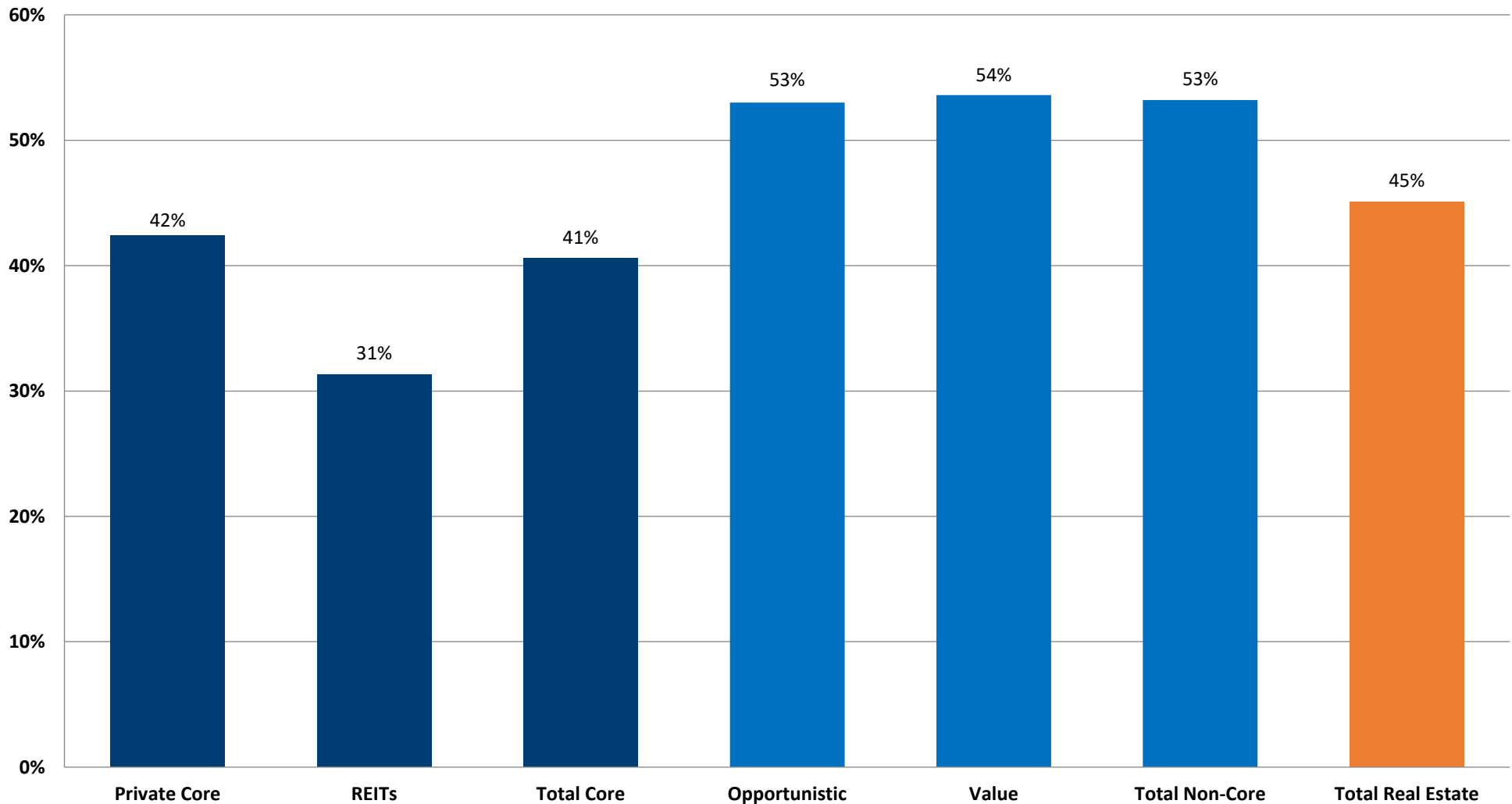
- Separate accounts
- Multiple strategies with single manager
- Fee benefits

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

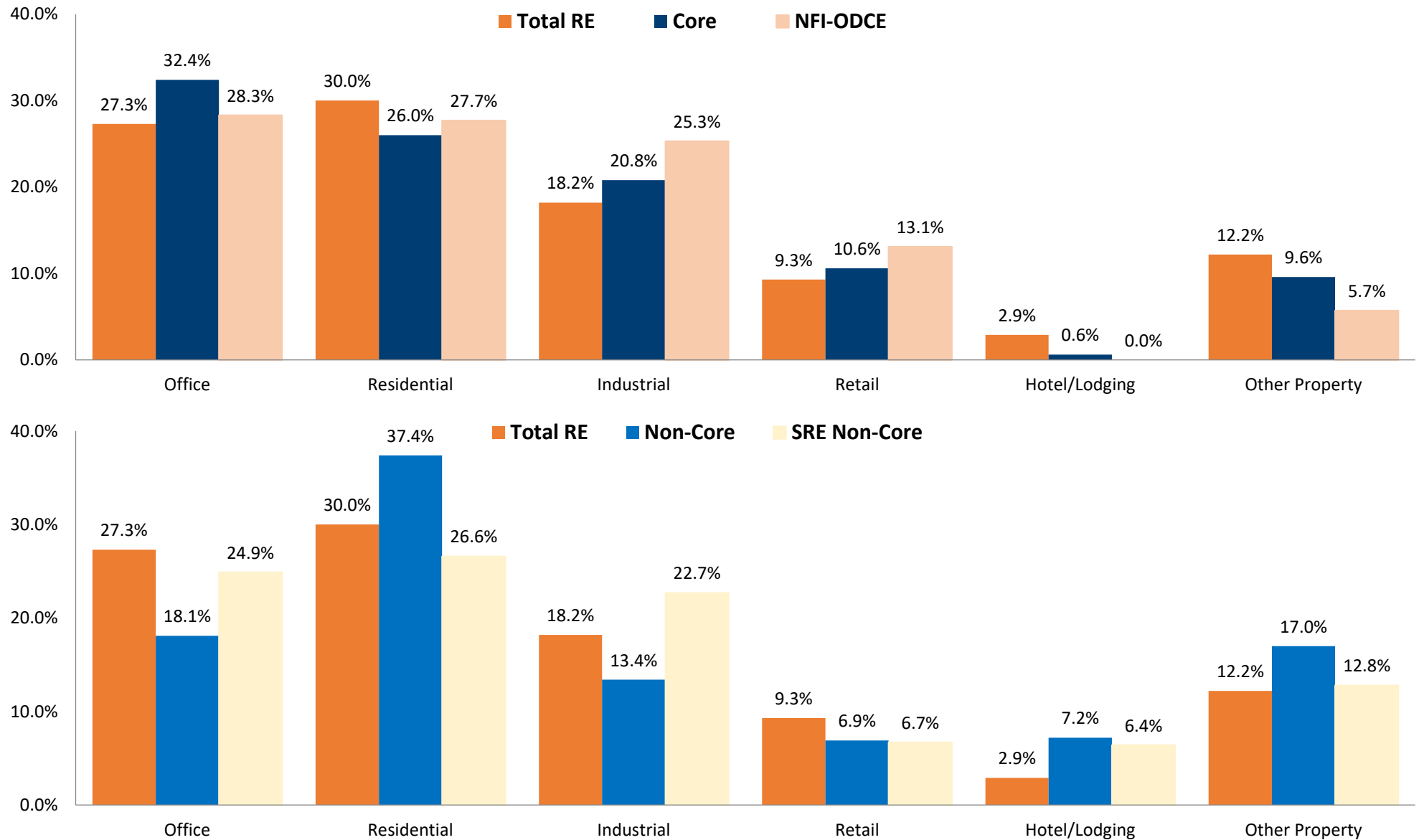


Source: StepStone NCRS 3Q21 Portfolio Monitoring Report

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



Property Type Diversification



Source: StepStone NCRS 3Q21 Portfolio Monitoring Report



Geographic Diversification

