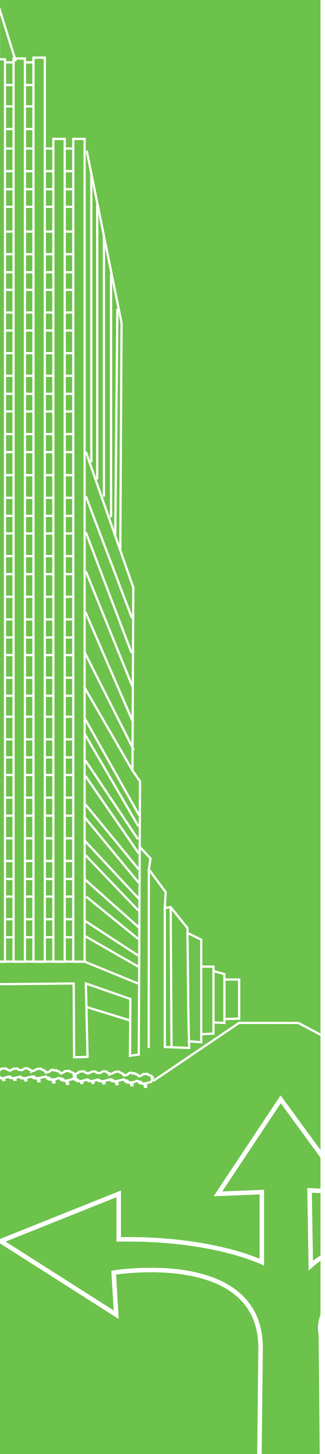

Funds Termination Study
2017

Research

INREV is the European Association for Investors in Non-Listed Real Estate Vehicles. Our aim is to improve the accessibility of non-listed real estate vehicles for institutional investors by promoting greater transparency, accessibility, professionalism and standards of best practice.

As a pan European body, INREV represents an excellent platform for the sharing and dissemination of knowledge on the non-listed real estate industry.

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Contents

Executive summary

- There are 47 funds with €8.5 billion in assets scheduled to terminate between 2017 and 2019
- Funds terminating in 2017 are larger than average
- Extensions are a popular choice

Commercial products tend to have a useful life cycle and closed end non-listed real estate funds are no different. Funds get launched, they attract capital, they generate returns for investors, they mature and then ultimately they reach the end of their useful lives and they are terminated, releasing assets back into the market and returning cash to investors. This study investigates the late life and end of life phase for such funds.

As a fund's planned termination date approaches, choices present themselves. This survey analyses the choices that have been taken, the timing of those decisions and the implications of those decisions.

Between 2017 and 2019, 47 funds with €8.5 billion in assets are scheduled to terminate. Two thirds of this amount (€5.6 billion or 65.6%) is scheduled to terminate in 2017, coming mostly from non-core funds (62.9% of funds and 67.0% of NAV). In contrast, terminations in 2018 and the year after will be dominated by core vehicles.

'Single sector and single country funds dominate termination volumes'

There are 24 multi sector and 23 single sector funds that are due to terminate over the coming two years. In terms of volume, however, single sector funds dominate terminations. Of the total €8.5 billion that is scheduled for termination over the coming two years, single sector vehicles make up two thirds (65.3%) of the total.

In terms of country strategy, a similar picture emerges. Single country and multi-country funds are broadly similar by number. In terms of size, however, there are some large single country funds due for termination in 2017. Zooming closer into single country strategies, numbers suggest that in 2017 UK funds will dominate (80.6% of the NAV comes from funds targeting the UK).

In terms of style, opportunity vehicles will comprise the largest share of total NAV (46.4%) scheduled for termination in 2017. In 2018 and 2019, core will dominate terminations.

For the first time in four years, extension has been cited as the preferred form of termination (liquidation was the preferred option in the previous three years). Driven perhaps by steady real estate returns, managers are choosing to extend the life of their funds. Likewise, funds in extension were up 9.9% in 2016. Liquidating funds were more modest with their performance, returning 5.6% last year. Over the five-year period from 2012 to 2016, the former group of funds generated 5.3% per annum while the latter left their investors in red delivering -3.1% on average per year.

'Current market conditions drive extensions'

Current market conditions were cited as being the main driver behind extension. Among the other key drivers, terms set for termination options in fund documentation are more important than quality of the portfolio. Extensions also facilitate strategic and structural changes being made to extending funds, as noted by one-third of respondents.

Section 1

Introduction

Introduction

This is the twelfth INREV Funds Termination Study, the latest in a series of reports examining preferred termination options and associated issues among European closed end non-listed real estate funds. The report also looks at trends in continuation strategies, the impact of current market conditions on fund managers' decision making process, as well as other issues related to funds terminations.

First, the study provides an overview of the funds within the INREV Vehicles Universe ('Universe') and which are due to terminate over the 2009 to 2020 period. In total, the INREV Vehicles Universe as of Q2 2017 contains 461 funds totalling €209.3 billion Net Asset Value (NAV). Of those, 279 are closed end funds, collectively representing total NAV of €52.9 billion. Two-thirds (65.2%) have their termination dates between 2009 and 2020 representing €31.1 billion of NAV. Over the coming two years (2017 to 2019) 47 of those funds are due to terminate putting €8.5 billion onto the market.

Second, and following on from last year's study, the report examines survey responses of funds that are due to terminate in the coming two years. This section explores factors impacting their termination decision making process as well as the timing of these decisions. The analysis is based on the sample of 45 funds which completed the questionnaire-based survey of which 34 are due to terminate over the coming two years, i.e. funds that are due to terminate over the period from 2017 to 2019.

It is important to note that the sample size and completeness of responses vary year by year. As such, historical comparison should be treated with caution. Returns figures are calculated by INREV. The performance data presented in this report is not intended to serve as a benchmark and should be used for research and information purposes only.

INREV would like to thank fund managers for their contribution towards the Funds Termination Study 2017.

Section 2

Market overview

Market overview

This section is based on data from INREV's Vehicles Universe. The universe contains key characteristics of non-listed real estate vehicles in Europe. It comprises 461 funds of which 279 are closed end vehicles collectively totalling €52.9 billion of NAV. Of those, 182 vehicles have their termination dates between 2009 and 2020 representing €31.1 billion of NAV. Over the 2017 to 2019 period 47 of those funds are due to terminate with €8.5 billion of the assets potentially scheduled for termination.

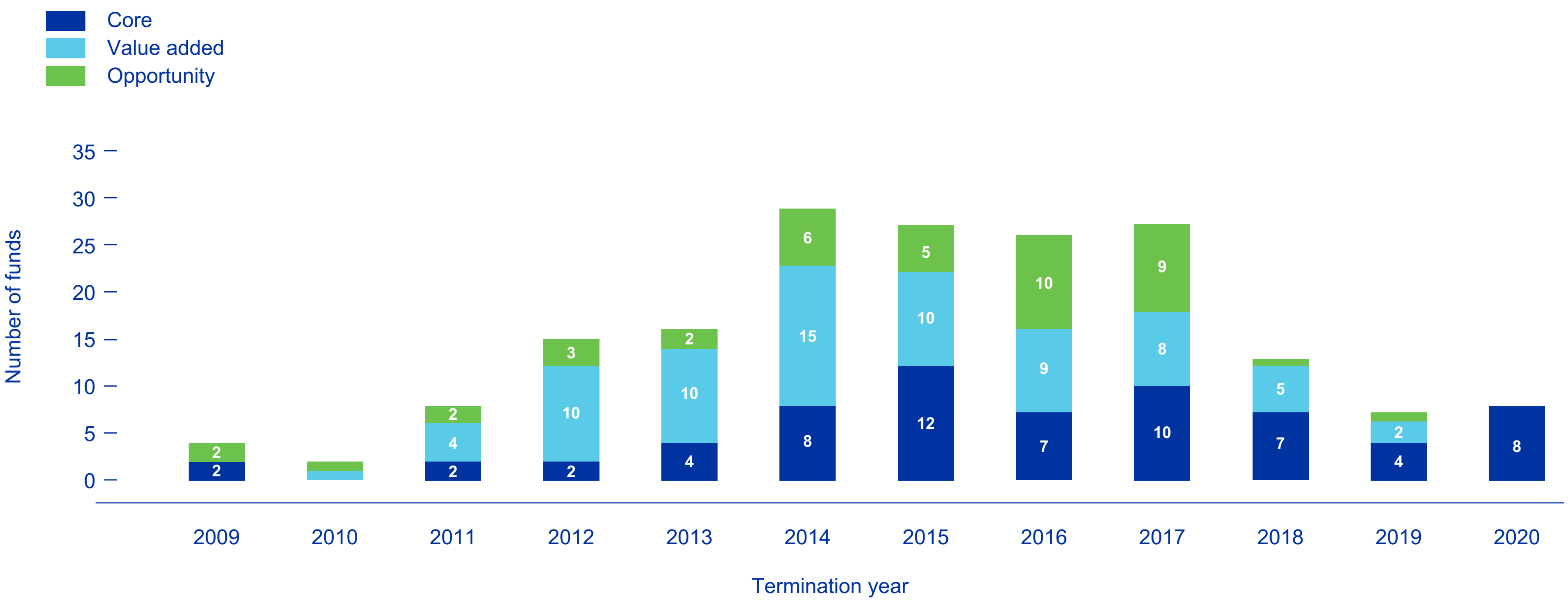
Funds terminating between 2009 and 2020

Of the 182 closed end funds with original termination years between 2009 and 2020, the majority (40.7%) are value added vehicles, followed by those with core (36.3%) and opportunity (23.0%) strategies, although of course the precise proportion of each style will vary from year to year.

With regards to the 2017 to 2019 period in which 47 funds indicated their termination dates, more than half (27 or 57.4%) of this group are scheduled to terminate in 2017. Next year is likely to see 13 funds being terminated, and in 2019 the number will taper to seven funds.

> 'The funds terminating in any given year have a mixture of styles'

Figure 1: Number of funds terminating between 2009 - 2020 by style



Funds terminating between 2017 – 2019

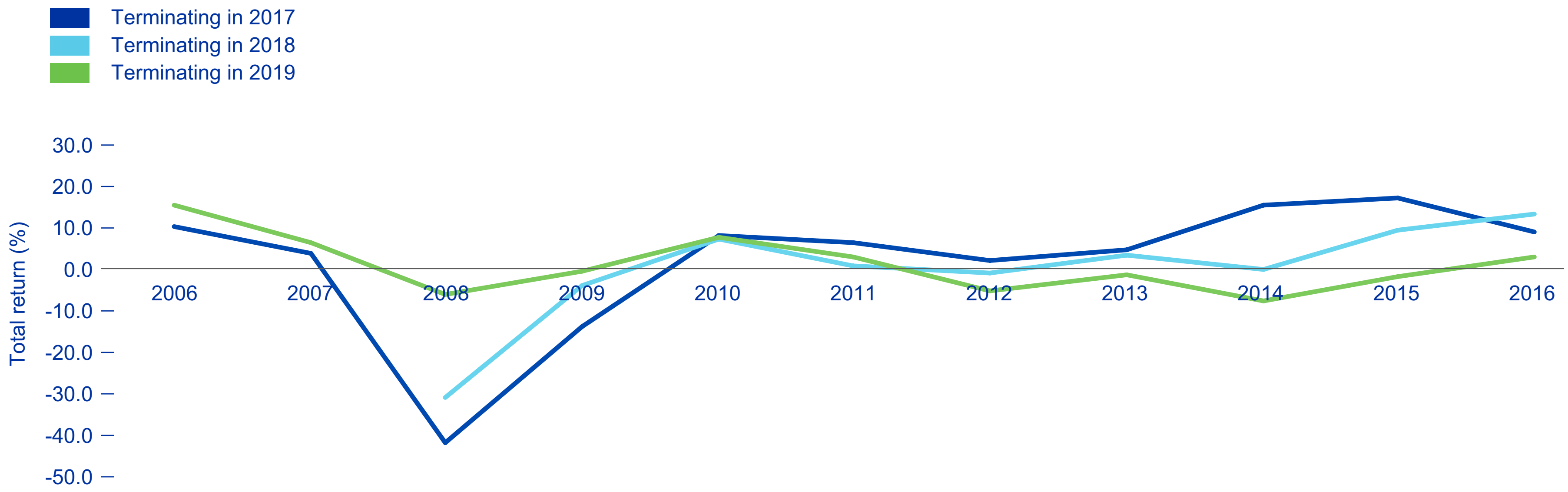
With regards to their performance, funds delivered different outcomes for their investors. On a shared 9-year annualised performance basis, funds that have their termination date scheduled in 2017 generated an average total return of –1.2% per annum. Over the last five years, this group of funds returned 9.4% per annum. In 2016, the returns stood at 8.7%.

Funds that are scheduled to terminate in 2018 delivered a somewhat different picture. Over the shared 9-year period, which is the longest available, this group of funds generated the same average total return of -1.2% per annum. The last five years saw returns averaging at 4.7% annually. Last year their return jumped to 13.3%.

Funds that have their termination date scheduled in 2019 generated a third pattern of returns. Their annualised 9-year returns stand at -1.2%. Over the last five years, their performance was -2.8% per annum. In 2016 their returns stood at 3.0%.

Funds terminating in 2019 withstood the market correction in 2008 better than their peers. However, their performance deteriorated starting from 2010, while those scheduled to terminate in 2017 and 2018 saw a pick-up in their performance. Although, overall in 2016, all three fund groups were in positive territory.

Figure 2: Performance by liquidation year



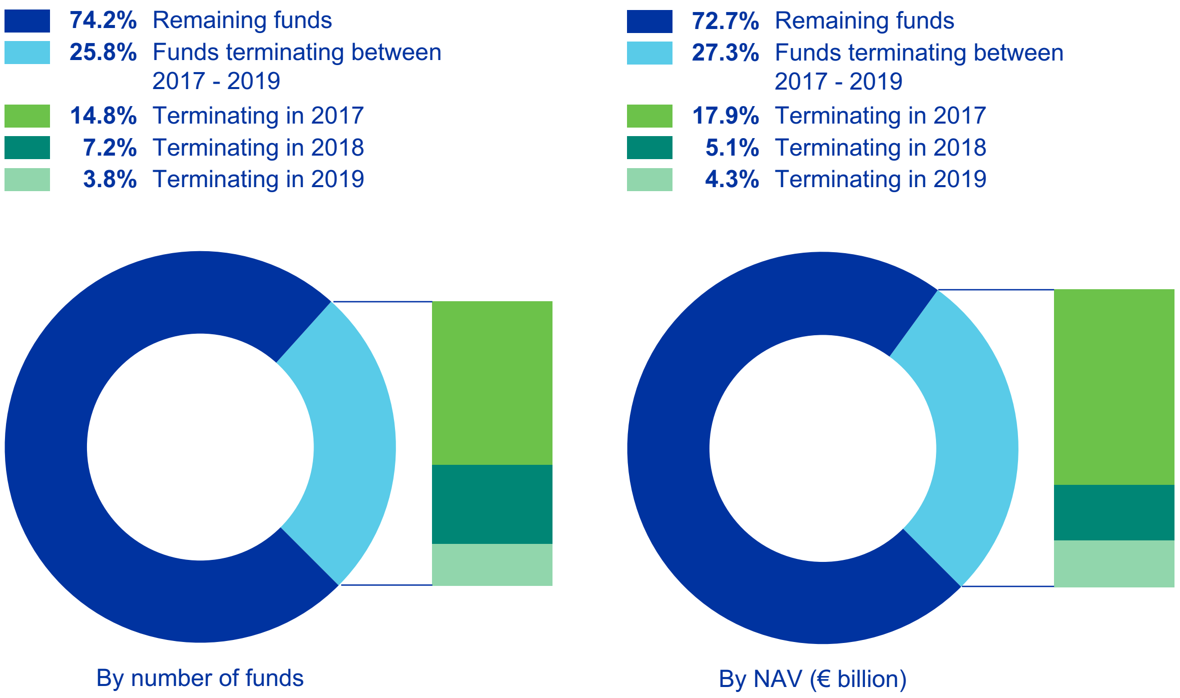
Of the total 47 funds, which are due to terminate between 2017 and 2019, there are 27 funds terminating in 2017, 13 in 2018 and seven the year after.

By size the NAVs are split as follows: €5.6 billion is scheduled for termination in 2017, €1.6 billion in 2018 and €1.3 billion in 2019.

Funds terminating in 2017 are therefore much bigger on average than funds terminating in the next two years, with funds terminating in 2018 being the smallest of the group. The average NAV of funds terminating in 2017 is €206.3 million, it is €121.9 million for funds terminating in 2018, and €191.8 million for vehicles terminating a year after.

> 'Funds terminating in 2017 are larger than their 2018 and 2019 peers'

Figure 3: Funds terminating between 2017 - 2019 by number of vehicles and size



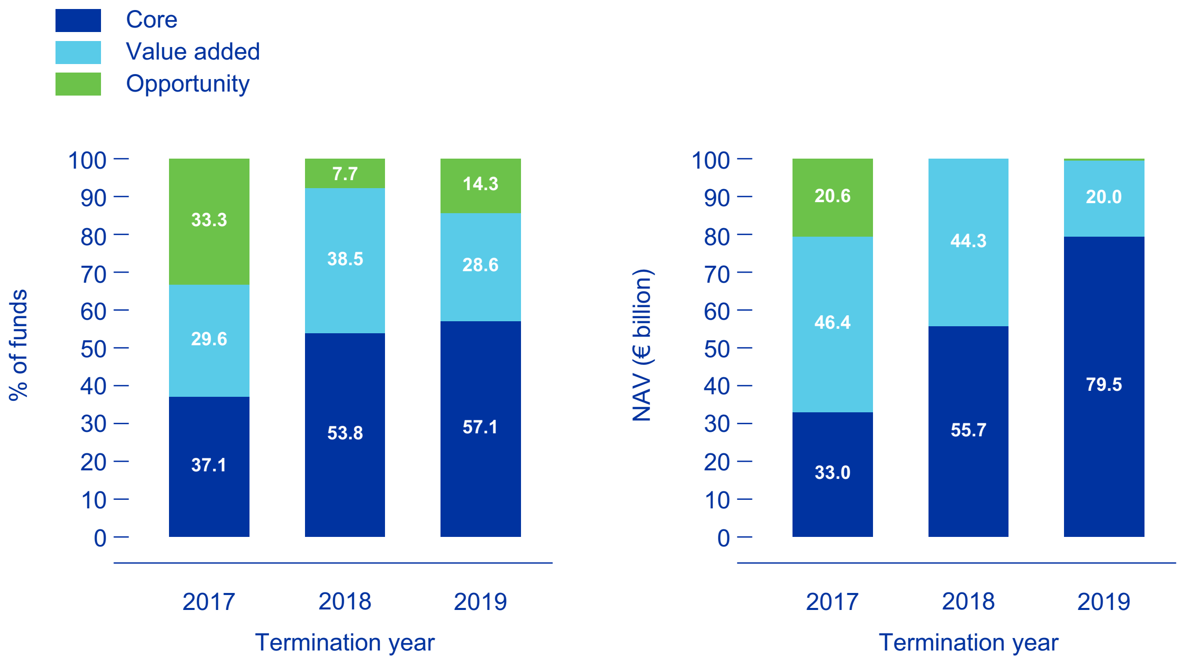
Funds in termination by style

In terms of style composition, the funds terminating in 2017 are evenly spread: 37.1% are core, followed by opportunity (33.3%) and value added (29.6%) funds. In 2018, more core funds are scheduled to terminate (53.8%), followed by value added (38.5%) and opportunity vehicles (7.7%). The following year, proportions remain almost unchanged from 2018 - just a few opportunity funds are terminating (14.3%) with most funds being core (57.1%) followed by value added (28.6%) vehicles.

In terms of fund size (that is, measuring by NAV rather than number of vehicles) the picture is slightly different. Value added vehicles will comprise the largest share of total NAV (46.4%) scheduled for termination in 2017. In 2018 and 2019, core will dominate terminations.

> ‘Core is the dominant style for funds terminating over the coming two years’

Figure 4: Funds in termination by style



By number of funds

By NAV (€ billion)

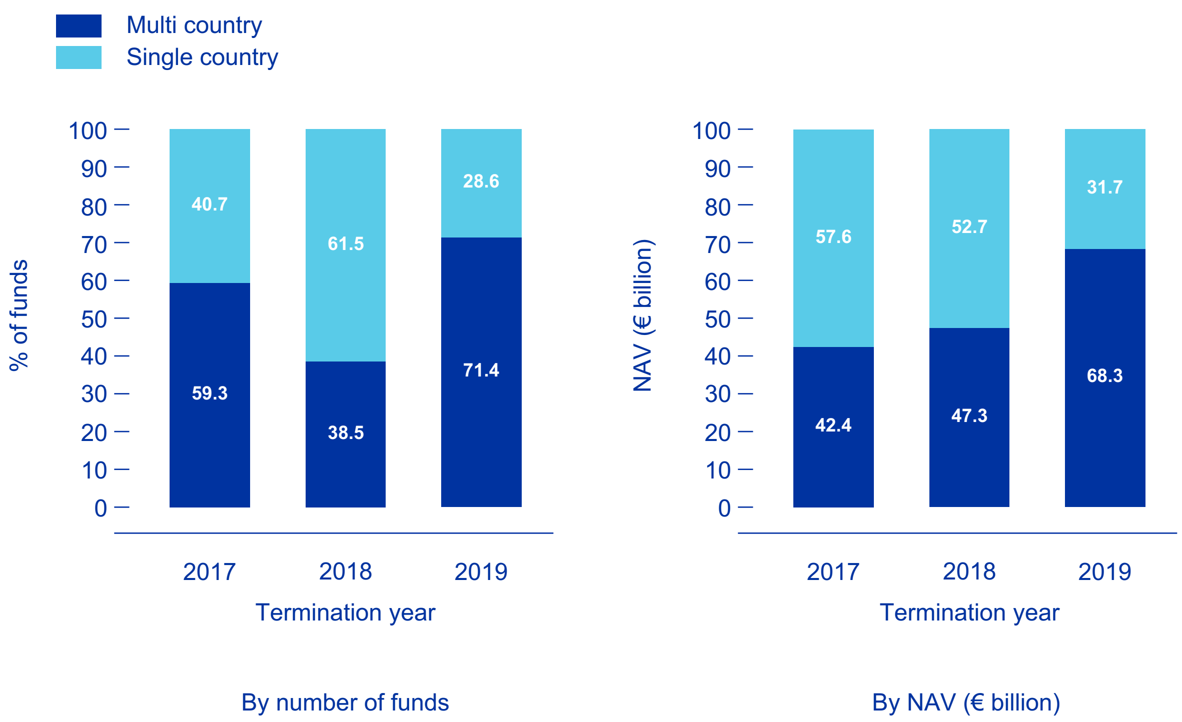
Funds in termination by country strategy

The split between single country and multi-country strategies varies from year to year. In 2017 there are more multi country (59.3%) funds scheduled to terminate compared to single country vehicles (40.7%). Next year, the trend reverses, with most terminating funds being single country (61.5%) vehicles. The year after terminations numbers mirror those of 2017 with 71.4% of funds in termination being multi country.

In terms of size, 2017 will see some sizeable single-country funds terminating. Of the total of €5.6 billion scheduled for termination in 2017, 57.6% is attributed to single country funds. In the following year, single country funds will also form the majority. In 2019, multi country funds will dominate.

> '2017 will see some sizeable single country funds terminating'

Figure 5: Funds in termination by country strategy



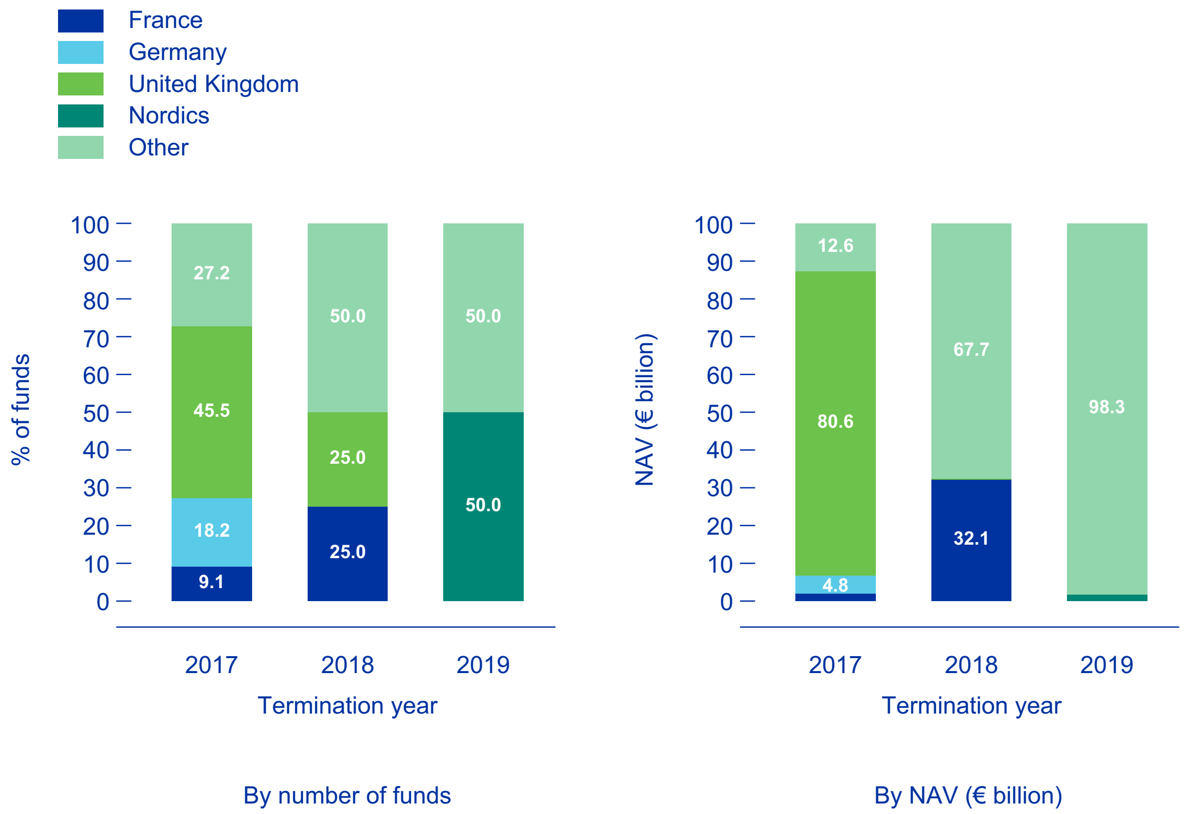
Funds in termination by single country strategy

With regards to single country funds, there is a mix of vehicles that are due to terminate over the coming two years. In 2017, 11 single country funds will terminate with 5 vehicles (45.5%) being UK funds. Next year, half of the funds that are scheduled to terminate fall into the "other" category (not France, Germany, the UK or the Nordics). The year after, the split is even between the Nordics and "other" country vehicles.

In terms of single country funds size, there will be €3.2 billion, €0.8 billion, and €0.4 billion scheduled for termination in 2017, 2018 and 2019 respectively. UK funds dominate 2017 terminations, indicating that some notable size UK targeting funds are scheduled for termination this year. In 2018 the size effect can again be seen. This time, however, it is "other" country funds that prevail.

> 'There is a mix of single country funds that are due to terminate over the coming two years'

Figure 6: Funds in termination by single country strategy



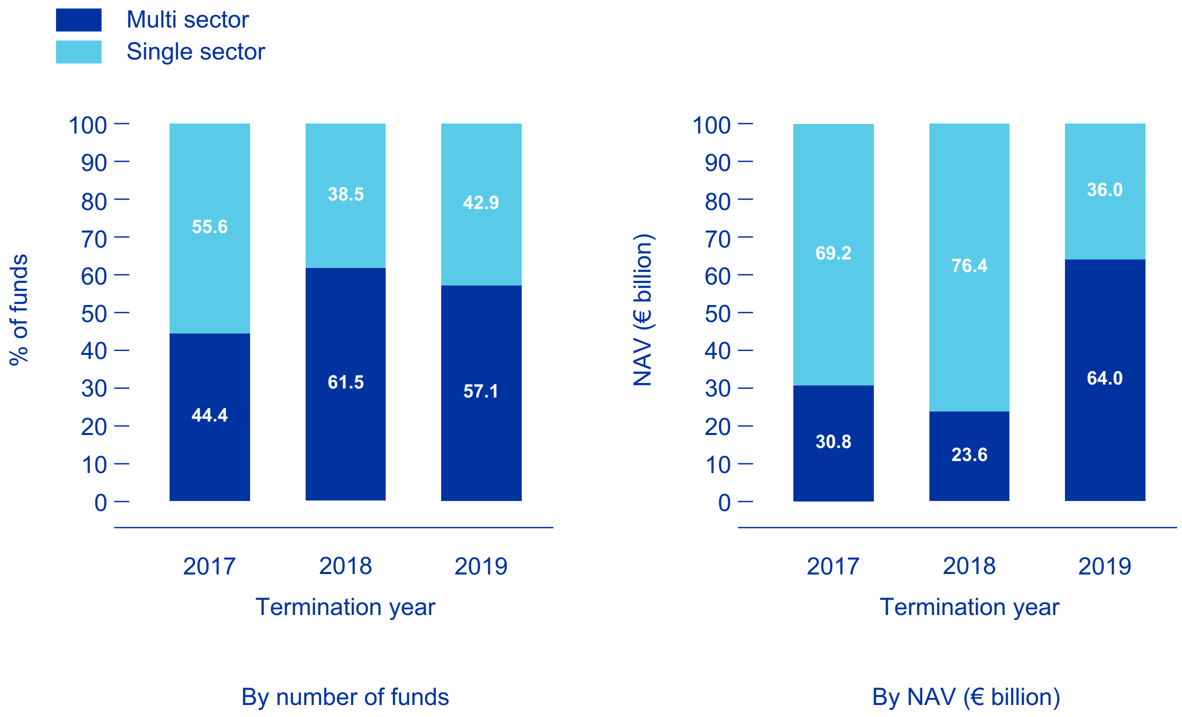
Funds in termination by sector strategy

When looking at funds termination by sector strategy, there is a notable difference between the pattern this year and the pattern in the following two years. There are 24 multi sector and 23 single sector funds that are due to terminate over the coming two years. Of the 27 funds terminating in 2017, 44.4% are multi sector and 55.6% are single sector. In 2018, 13 funds have their terminations scheduled and of those 61.5% are multi sector and 38.5% are single sector. The year after 7 funds are scheduled for termination with the split between multi and single sector being 57.1% and 42.9% respectively.

In terms of size, of the €5.6 billion potentially being scheduled for termination in 2017, single sector vehicles (69.2%) dominate. The trend continues into 2018 with single sector funds representing 76.4% of the total of €1.6 billion of NAV suggesting that some sizeable single sector funds will come into the market in 2017 and 2018. For 2019 the split changes, with NAV of €1.3 billion being split as follows: 64.0% for multi sector and 36.0% for single sector.

‘Some large single sector funds will come into the market in 2017 and 2018’

Figure 7: Funds in termination by sector strategy



Funds in termination by single sector strategy

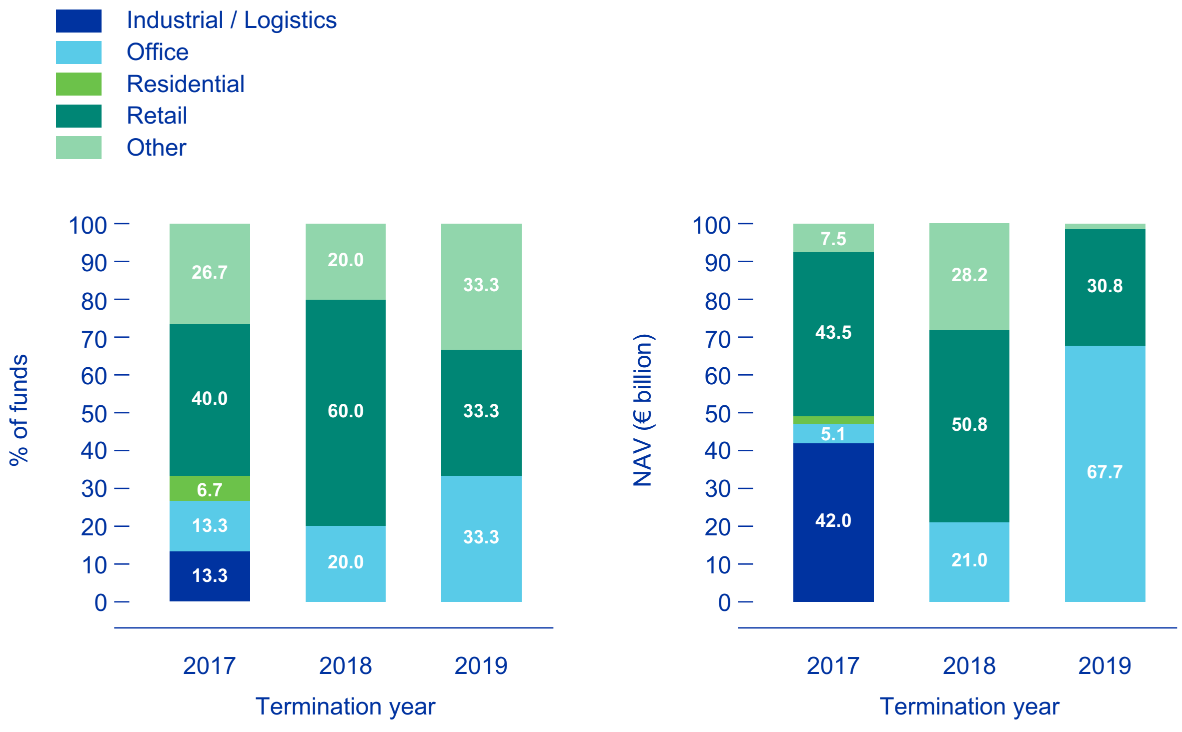
In terms of specific sector strategies, funds targeting retail make up the largest share of vehicles terminating over the coming two years. Of the 15 single sector vehicles terminating in 2017, 40.0% are retail. The remaining 60.0% is split between industrial / logistics (13.3%), office (13.3%), residential (6.7%) and other sectors (26.7%).

In 2018, 5 single sector funds are scheduled to terminate and retail vehicles still dominate, accounting for 60.0% of the sample. The year after, the split is even between office, retail and the "other" sector group.

By value, the picture is not dissimilar, in the sense that retail dominates each year, though less so in 2019 when office funds make up 67.7% of NAV. Likewise, industrial / logistics funds in termination make up 42.0% of the total of €3.9 billion of terminations in 2017. This indicates that some large industrial / logistics funds are due to terminate in 2017.

'Funds targeting retail make up the largest share of terminating vehicles'

Figure 8: Funds in termination by single sector strategy



By number of funds

By NAV (€ billion)

Section 3

Funds termination survey

Funds termination survey

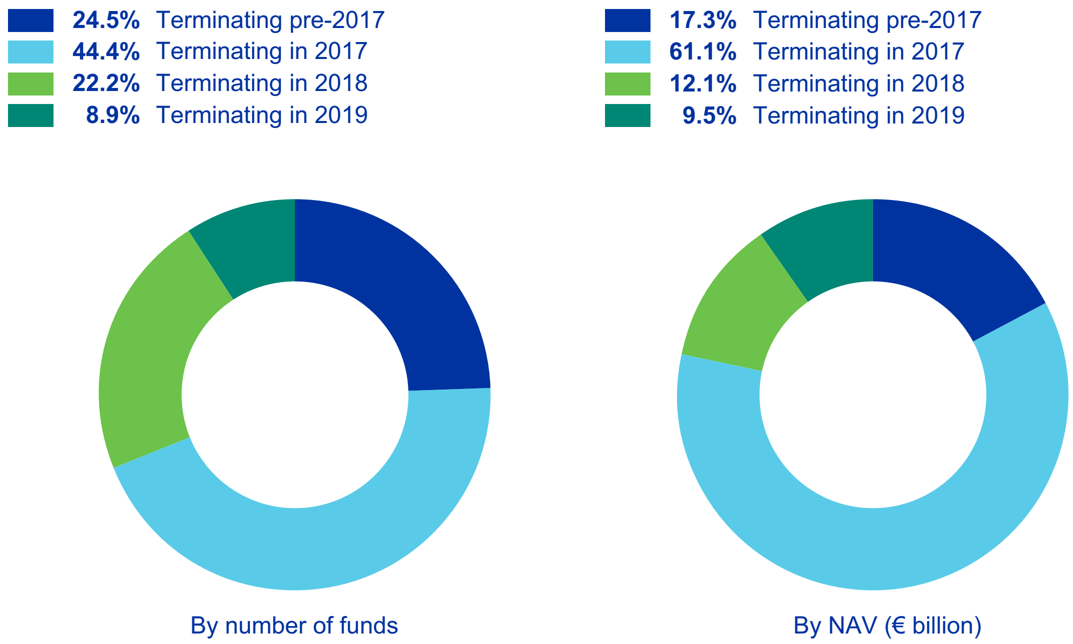
This year's annual funds termination survey is based on responses collected from 45 funds of which 34 are due to terminate in 2017, 2018 or 2019.

The survey explores the choices considered for termination as well as a range of factors affecting the decision-making process, the timing of the decisions and how specific continuation strategies are likely to affect the structure of the funds themselves.

The funds contributing to this year's survey have a range of different termination dates. Funds that are due to terminate in 2017 is the largest group, making up 44.4% of the total. Funds scheduled for termination in 2018 make up 22.2% of the sample. Those that have their terminations scheduled the year after comprise 8.9% of the total with the remaining 24.5% being funds with their termination scheduled at some point before 2017.

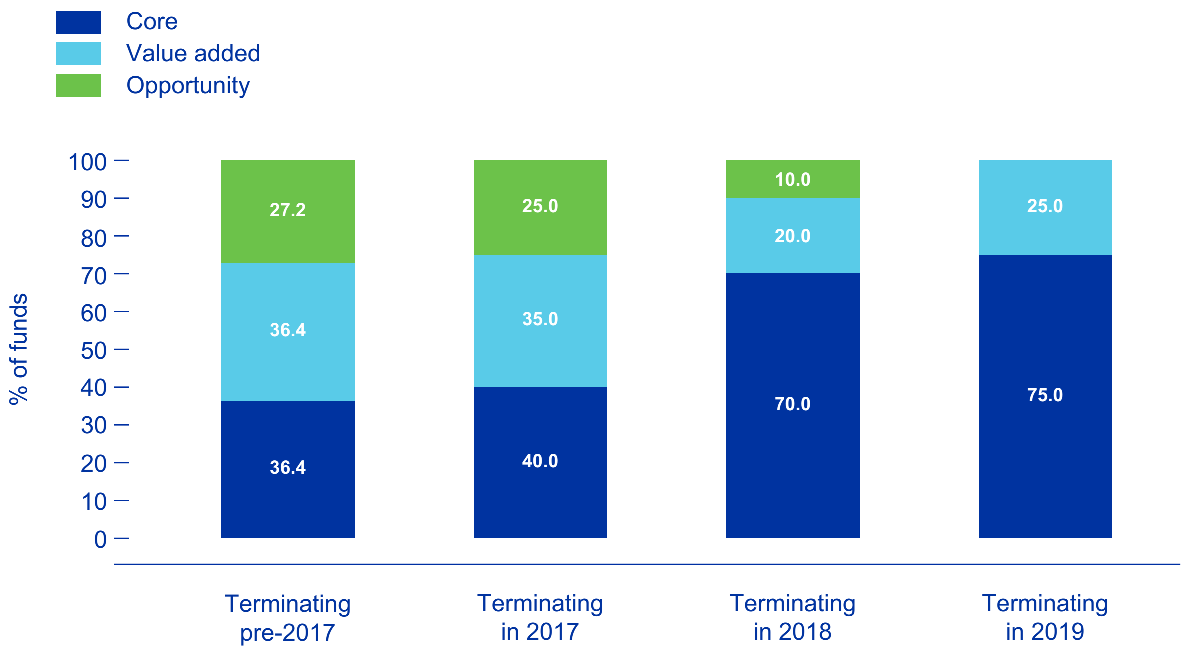
Size wise, 45 funds that completed the survey total to €9.4 billion in NAV of which €7.8 billion (82.7%) relates to funds terminating over the coming two years.

Figure 9: Composition of funds by termination date



With regards to style composition, most funds that completed this year's survey are core. Of the 20 vehicles that have their termination date scheduled in 2017, 40.0% are core. The number of core vehicles rises to 70.0% the year after, or seven out of ten vehicles. Participating funds with their termination date scheduled in 2019 are also mostly (75.0%) core.

Figure 10: Composition of funds by termination date by style



Composition by liquidation status

The funds that participated in this survey differ in terms of their termination status. Of the 11 funds with terminations prior to 2017, seven (63.6%) are already in liquidation. The next largest category comprises funds that are in extension, which make up 27.3% of the total. The remaining 9.1% have already been liquidated.

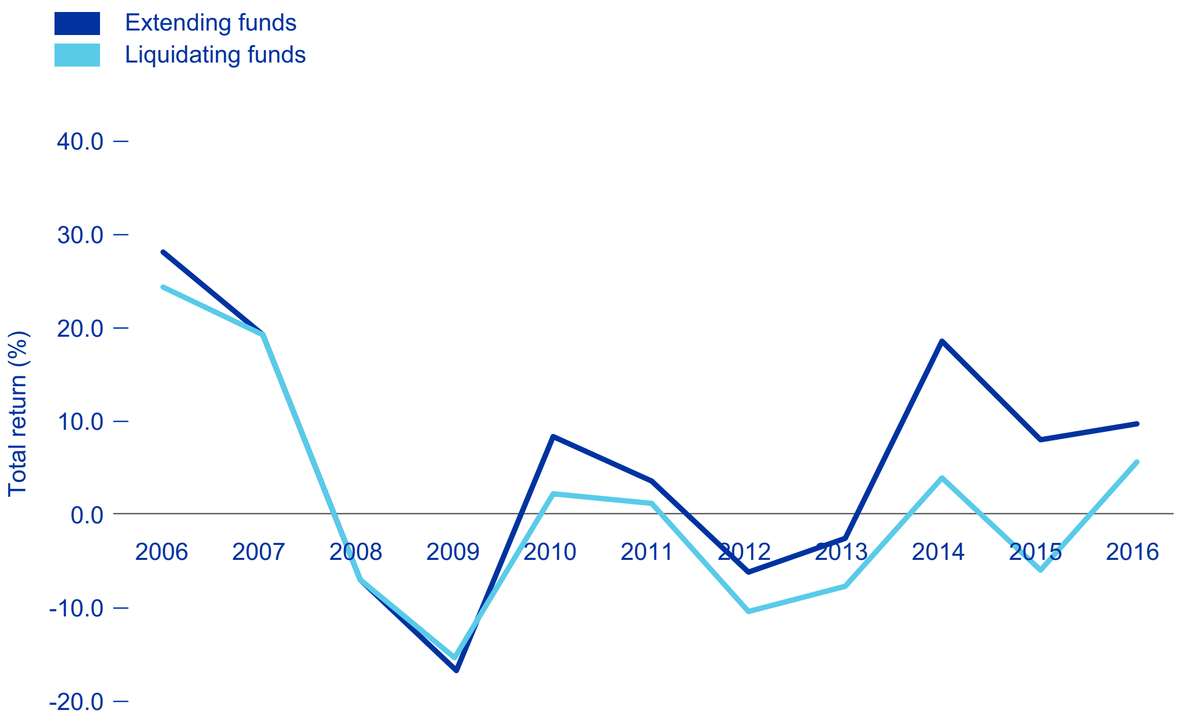
Of the 34 funds terminating over the coming two years, the majority (44.1%) are in liquidation. Close to one quarter (23.5%) of vehicles are in extension. The remaining funds fall into a mix of categories, including liquidated, other options or left their status unspecified.

Figure 11: Composition of funds by status

Performance by liquidation status

Liquidation status can at times have a connection to performance. This was not the case in the period from 2007 to 2009 but since then a gap has appeared and it has continued to exist. Over the five-year period from 2011 to 2015 the gap in average annual returns between funds in extension and liquidating funds was on an increase. However, in 2016 the gap narrowed to 4.3%, with extending funds delivering 9.9% return and liquidating funds delivering 5.6% last year. The former group of funds returned 3.0% and 5.3% per annum over the last decade and five-year period respectively. For the latter group, corresponding numbers are as follows: -1.9% and -3.1%.

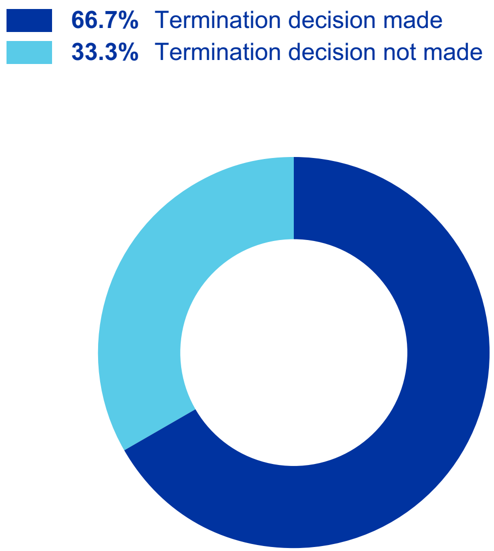
Figure 12: Performance by liquidation status



Decision making

The responses show that fund managers have generally decided on a termination strategy, when termination is due to occur within two years. In previous years, this study could split the sample according to the imminence of the planned termination (that is, distinguishing between funds due to terminate this year and funds due to terminate in later years). However, this year the sample was too small to facilitate such a detailed analysis. However, the sample does support a straightforward division between funds that have and funds that have not made a decision: two-thirds of funds had decided in the two year lead up to planned termination.

Figure 13: Timing of decision making

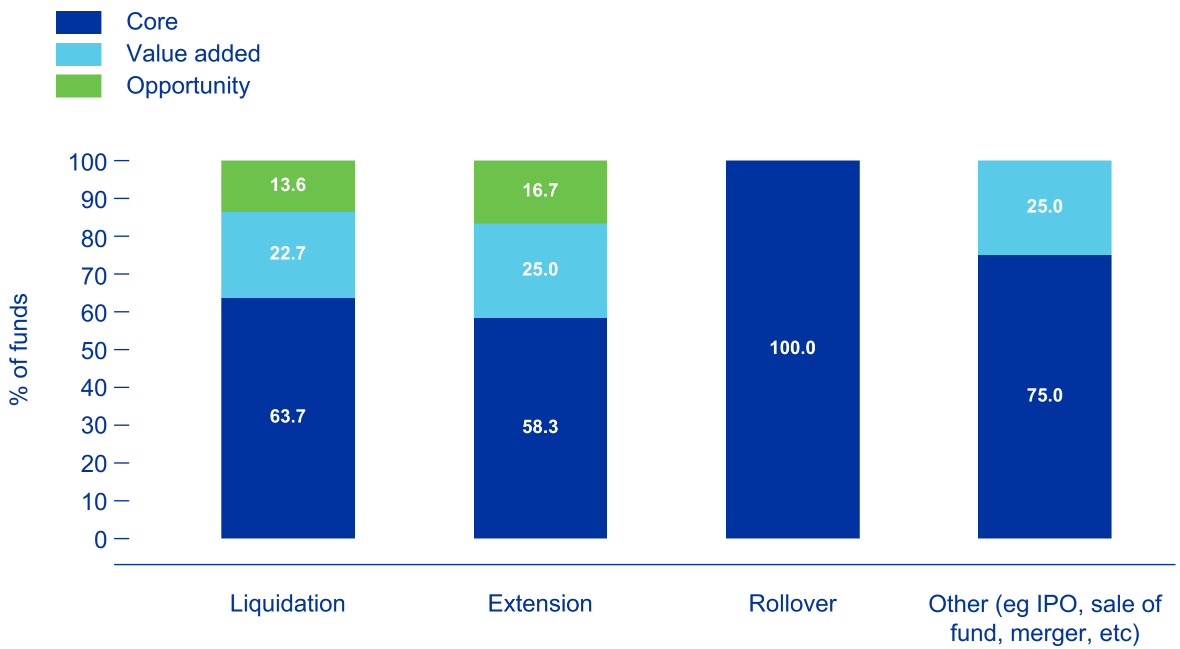


Termination options under consideration prior to making a decision

For the 34 funds which are due to terminate over the coming two years, managers were asked to select termination strategies under consideration for their funds. In this instance, they could select more than one option.

There are notable differences across termination options and fund styles. Where liquidation was chosen (22 funds), the clear majority were core funds, accounting for 63.7% of the total. Rollover was very popular for core funds too. Where extension was chosen (12 funds), the majority was also core (58.3%) followed by value added (25.0%) and opportunity (16.7%). For all styles, liquidation and extension were the most popular choices.

Figure 14: Termination options under consideration



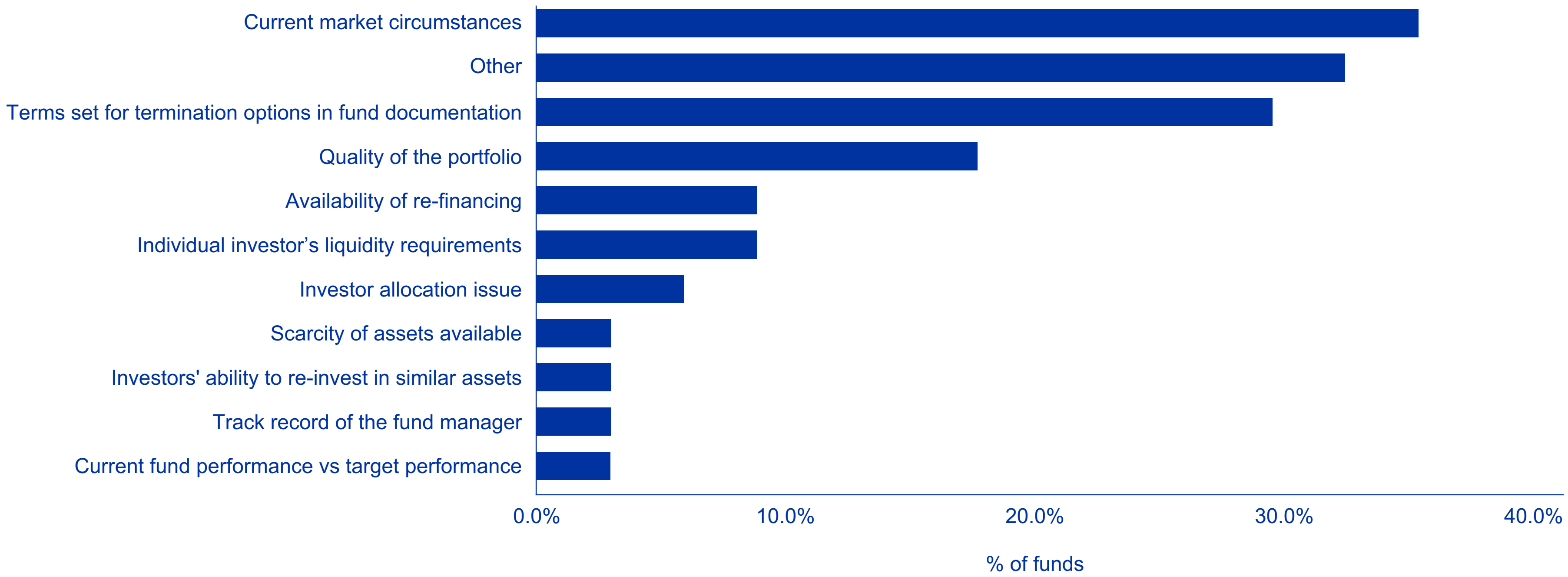
Issues affecting termination decisions

The factors affecting termination decisions were also explored, and here fund managers could indicate one or more reasons that drive their termination strategy.

In this context, 35.3% of the 34 respondents stated that current market circumstances are the most important driver. Terms set for termination options in fund documentation are more important than quality of the portfolio. Last year both issues jointly occupied the second top spot. Interestingly, debt issues were not considered as being relevant in deciding on termination options this year.

> ‘Current market circumstances are the biggest driver of termination decisions’

Figure 15: Issues affecting termination decisions



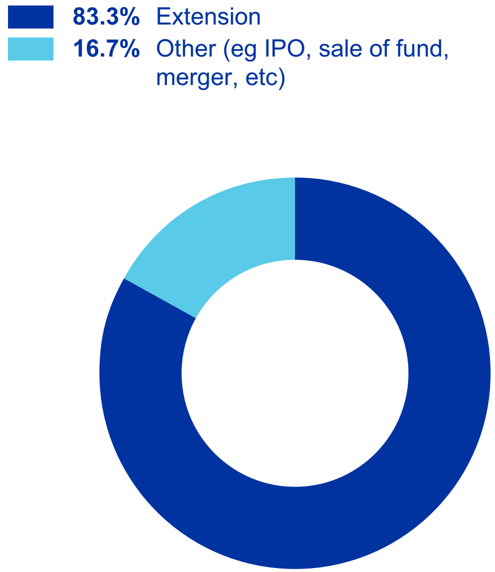
Preferred termination strategies

Fund managers were asked which termination strategy was finally chosen or most likely to be chosen. Only fund managers who had made a choice were invited to share their decision.

Therefore, of those that have decided, 83.3% consider extension as the preferred termination strategy, with the remaining respondents opting for other options. Interestingly, last year liquidation was the preferred option, just as it was in the previous two years too.

> 'Extension is the preferred termination strategy this year'

Figure 16: Termination option chosen or most likely to be chosen



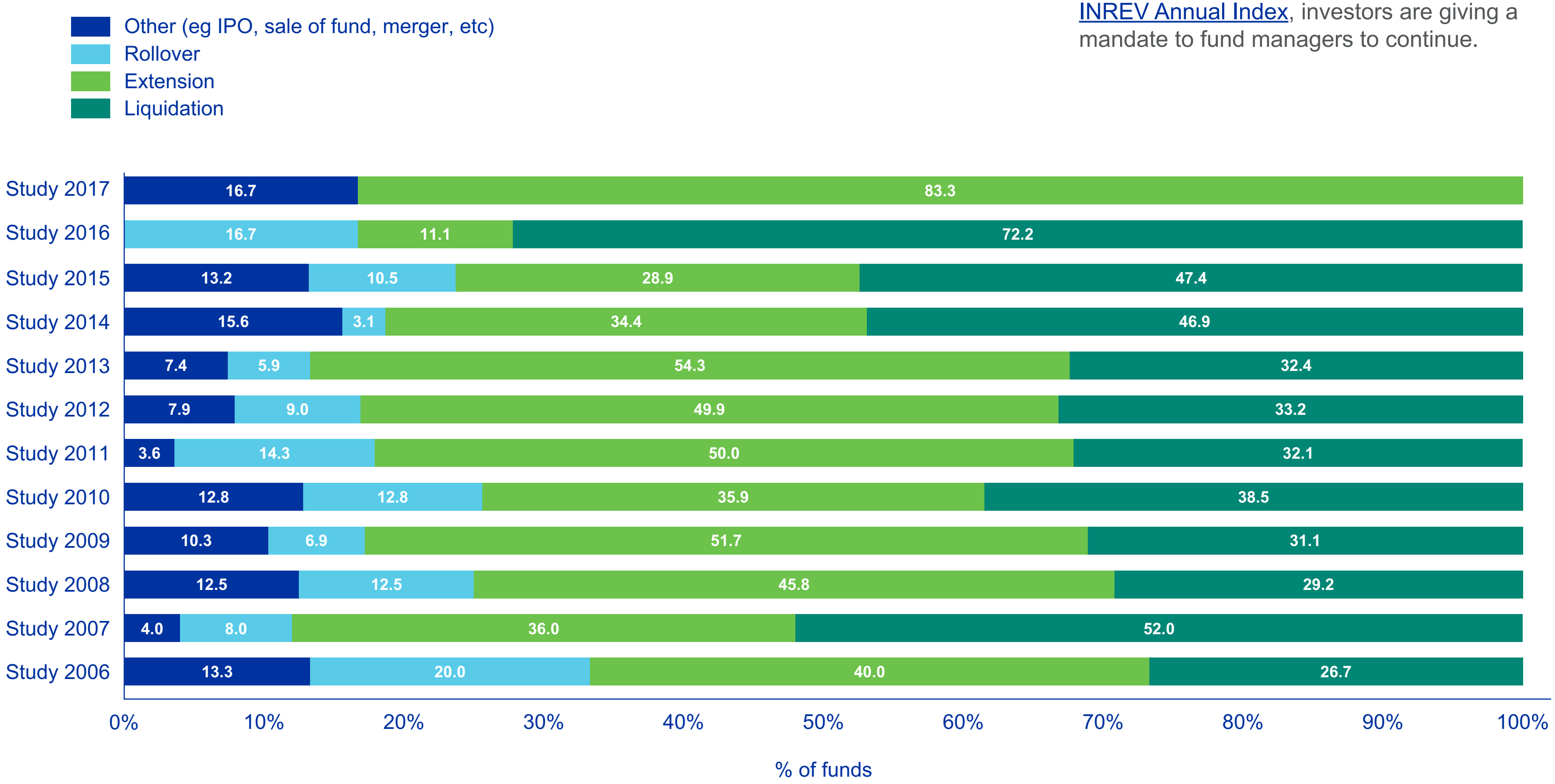
Some yearly variability notwithstanding, extension and liquidation have been the dominant termination options over the years. Other options (roll overs, IPOs, sales or mergers and so on) certainly remain relevant. However, termination avenues other than liquidation and extension have not attracted more than 30% of respondents in any year except that of 2006.

With liquidation dominating the sample over the previous three years, this year is clearly a year of extensions. Neither liquidation nor roll over received votes from respondents.

The majority (83.3% to be precise) of respondents opted for extension. This does not come as a surprise. With extending funds delivering healthy returns to their investors and with the overall non-listed real estate market exhibiting solid returns of 6.0% in 2016, as estimated by the INREV Annual Index, investors are giving a mandate to fund managers to continue.

‘2017 is the year of extensions’

Figure 17: Termination option chosen or most likely to be chosen over 2006 to 2017



‘Extension dominates termination options’

In previous years, this study could examine how investment style affected the termination options that were chosen. However, this year the sample for non-core funds was too small to facilitate this analysis. As such the study shows the termination options for core funds only.

The numbers reflect the general sentiment expressed by respondents - extension dominates with the minority of funds opting for other strategies such as an IPO, sale or merger.

Figure 18: Termination option chosen or most likely to be chosen by core funds

75.0% Extension
25.0% Other (eg IPO, sale of fund, merger, etc)

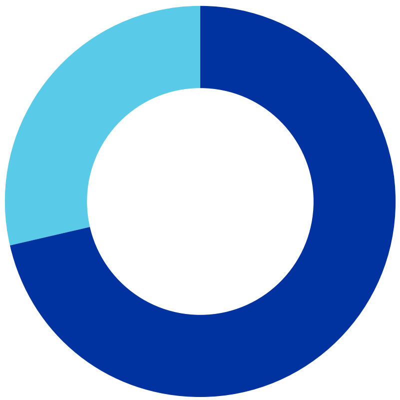
Structural changes to extended funds

Extension of a fund’s life may sometimes be accompanied by structural or strategic changes in a vehicle. For example, a change in governance structures or fees might accompany the decision to extend. However, this is not necessarily the case if the original structure is sufficiently flexible.

In this year’s survey, 28.6% of respondents envisage some strategic or structural changes being made to extending funds. The remaining 71.4% stated that no such changes would be needed. Last year, 22.2% of respondents indicated that they expect some structural changes to be made to their funds with the majority suggesting that no changes are planned.

Figure 19: Structural changes to funds in extension or most likely to extend

71.4% No changes will be made
28.6% Yes, strategic or structural changes will be made to the funds’ fees, governance, etc



‘Over one quarter of respondents envisage some strategic or structural changes being made to extending funds’

Appendix

Appendix: List of participants

The following is a list of fund managers who participated in the Funds Termination Study 2017 and gave permission for their company names to be published.

Aberdeen Asset Management
Amundi Real Estate
AXA Investment Managers - Real Assets
Barings
BlackRock
Bouwfonds Investment Management
CapMan
CBRE Global Investors
Clearbell Capital LLP
COIMA SGR
Cromwell Property Group
East Capital
First Property Group
Generali
GLL Real Estate Partners
Harbert Management Corporation
Heitman
Invesco
Kames Capital
Legal & General Investment Management
Meyer Bergman
NIAM AB
Rockspring PIM
Rynda Property Investors LLP
Società di gestione del risparmio (SGR)
Sonae Sierra

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