



## **PSERS OPPORTUNISTIC REAL ESTATE PROGRAM**

### **Recommendation for Investment in DLJ Real Estate Capital Partners IV, L.P.**

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# **DLJ Real Estate Capital Partners IV, L.P.**

## **EXECUTIVE SUMMARY**

Credit Suisse is sponsoring DLJ Real Estate Capital Partners IV, L.P. (collectively, with related co-investment vehicles, "RECP IV" or the "Fund"), a global opportunistic real estate private equity fund managed by DLJ Real Estate Capital Partners, Inc. ("RECP" or the "Manager"). RECP is responsible for the successful performance of three predecessor funds with over \$3.0 billion of aggregate equity commitments, DLJ Real Estate Capital Partners, L.P. (collectively with related co-investment vehicles, "RECP I"), DLJ Real Estate Capital Partners II, L.P. (collectively with related co-investment vehicles, "RECP II") and DLJ Real Estate Capital Partners III, L.P. (collectively with related co-investment vehicles, "RECP III", and together with RECP I and RECP II, the "RECP Funds"). The strong performance of the RECP Funds demonstrates the Manager's ability to understand real estate fundamentals, acquire high-quality, attractively priced assets, execute a clearly defined plan to enhance value, and exit investments successfully on a global basis. The Manager will continue to employ its disciplined investment approach through RECP IV, with a continued focus on the U.S., Asia and Europe.

Credit Suisse, its affiliates and their employees have committed to invest \$200 million in RECP IV's investment program, of which at least \$20 million will be committed through a Credit Suisse-sponsored co-investment program for the RECP investment professionals. This substantial capital commitment demonstrates Credit Suisse's and the RECP investment professionals' belief that RECP IV is well positioned to achieve attractive risk-adjusted returns in the current real estate environment given the Manager's access to significant proprietary deal flow, substantial network of relationships, capital markets expertise, and operating and management experience. RECP IV will benefit from a global exclusivity arrangement with the Investment Banking Division of Credit Suisse.

The management and strategy of DLJ Real Estate Capital Partners IV, L.P. generally will be the same as those of its prior funds, of which PSERS is an investor in DLJ Real Estate Capital Partners II and III. The investment team consists of 29 dedicated real estate professionals, and is distinguished by the fact that its members have strong hands-on real estate backgrounds; including acquisition, asset management, development, rehab/redevelopment, leasing and repositioning.

## **THE SPONSOR**

Credit Suisse is a subsidiary of Credit Suisse Group, a leading global financial services company with a public market capitalization of \$74 billion and total assets of \$1,029 billion (as of December 31, 2006). As an integrated global bank, Credit Suisse provides its clients with investment banking, private banking and asset management services worldwide. Founded in 1856, Credit Suisse has a long tradition of meeting the complex financial needs of a wide range of clients. It provides companies, institutional clients and high-net-worth private clients globally, as well as retail clients in Switzerland, with advisory services, comprehensive solutions and innovative products. Credit Suisse is active in over 50 countries and employs approximately 45,000 people.

Credit Suisse Alternative Investments is a business unit of Credit Suisse's Asset Management Division, and is a leading global alternative asset manager involved in private equity, hedge funds, volatility management and related activities. With \$129 billion in assets under management, Credit Suisse Alternative Investments is one of the world's largest and most successful managers of alternatives, with dedicated private equity funds

that focus globally on leveraged buyouts (Merchant Banking Partners), real estate investments (Real Estate Capital Partners), mezzanine investments (Investment Partners), customized and other fund of funds products (Customized Fund Investment Group) and secondary purchases of interests in private equity funds (Strategic Partners). Credit Suisse has a long history in the private equity business starting with the formation of a venture capital fund in 1969 and merchant banking fund in 1985, both as affiliates of Donaldson, Lufkin & Jenrette (“DLJ”), which merged with Credit Suisse First Boston (now Credit Suisse) in late 2000.

The Manager expects that RECP IV will benefit extensively from Credit Suisse’s global platform and relationships (within applicable regulatory constraints). Credit Suisse is a proven leader in corporate advisory, capital markets and financial services and has global relationships with leading financial institutions, corporations and senior executives. Credit Suisse has one of the most active real estate finance businesses, with approximately 400 dedicated real estate professionals focusing on investment banking, fixed income and research in New York, Los Angeles, London, Frankfurt, Tokyo, Singapore, Hong Kong and Sydney.

## **INVESTMENT STRATEGY**

**United States.** Despite steady increases in interest rates by the Federal Reserve during the period between mid-2004 and mid-2006, capitalization rates across most property types in the U.S. generally held steady or continued to decline in many markets. This compression in capitalization rates was driven by liquidity in the real estate sector and by expectations of continued improvement in property market fundamentals. Looking forward, capital will likely continue to be available for real estate, but investors will need to be highly selective and focus on market-specific growth dynamics, pricing inefficiencies, operating performance, asset management, and the long-term quality of the underlying real estate in order to generate attractive returns. RECP has an established track record of identifying attractive risk-adjusted investment opportunities and executing value creation strategies across different market cycles. RECP will continue to focus its investment activities on markets characterized by strong job growth and demographic trends, significant barriers to entry, and sound long-term real estate fundamentals.

**Asia.** RECP expects to continue to focus its Asia investment strategy in Japan and China, while expanding opportunistically in other high growth economies such as India. Industry experts predict real estate fundamentals in Japan will improve as the overall economy continues to emerge from more than a decade of stagnation, vacancies approach cyclical lows, and real estate capital markets experience increased liquidity. With this, China should continue to experience robust economic expansion, with continued demand growth for properties across most sectors. RECP is well-positioned to capitalize on opportunities in China based on the successful track record of RECP III and the leading presence of Credit Suisse’s banking operations in China.

**Europe.** The European Union (“EU”) includes 27 countries with an aggregate population of 490 million and a total GDP of \$13.7 trillion. Within the EU, economic fundamentals and real estate opportunities vary widely. In Western Europe, economic growth is starting to recover and GDP growth is projected to average 2% over the next two years, with stronger growth in Ireland, Spain and Greece, and slower growth in core economies like Germany, France and Italy. RECP IV will benefit from continued corporate and government divestitures of large assets or portfolios of assets in France, Germany and Italy. Tourism, leisure and second-home markets continue to grow throughout the continent, driven by rising disposable income and decreasing barriers to traveling. The

countries in Central and Eastern Europe continue to benefit from improved integration with Western Europe as these economies benefit from improved transportation, infrastructure, and legal systems. In addition, Central and Eastern Europe offer attractive investment opportunities driven by rising levels of disposable income, significant levels of foreign direct investment, and continued integration and convergence of capital markets.

## **INVESTMENT FOCUS**

**Asset Repositionings.** The Manager is an experienced real estate investor that is able to identify and execute value-creation plans through a program of careful acquisition due diligence and proactive asset management. The Manager will continue to focus on opportunities characterized by properties that are under-performing relative to comparable assets due to changing market dynamics, mismanagement, lack of capital, or unresolved conflicts among existing owners, lenders, tenants and managers. These situations often offer attractive risk-adjusted returns through recapitalization and the subsequent redevelopment or repositioning of the underlying real estate. The Manager is well positioned to continue sourcing and executing such opportunities on a proprietary or limited-competition basis due to its extensive industry contacts and network of local operating partners as well as Credit Suisse's global platform.

**Capital Market Dislocations.** The real estate markets are often characterized by dislocations between the private and public capital markets, and between real estate pricing and underlying real estate fundamentals. The Manager has extensive experience in creating customized financial structures that offer downside protection supported by fundamentally sound real estate. These transactions include private investments in public companies, recapitalizations of public companies during periods of illiquidity, structuring investments in companies when other capital sources are unavailable, and investing in large-scale single assets.

**Government and Corporate Divestitures.** Governments, financial institutions and large corporations often face pressure to divest non-strategic assets such as real estate and focus financial resources on core competencies. The Manager has demonstrated success buying real estate from corporate and government sellers throughout the 1990's. European corporations are continuing to adapt to the expansion of the European Union and deregulation of their economies, resulting in an ongoing process of real estate divestiture. In Japan, divestiture has accelerated as the government, financial institutions, and corporations struggle to reduce excessive leverage and restructure balance sheets after more than a decade of economic stagnation. Credit Suisse and the Manager's extensive international platform and network of government and corporate relationships will be beneficial in sourcing these transactions.

**Distressed Debt.** Financial institutions periodically become involuntary owners of real estate and non-performing and sub-performing loans due to financial and real estate market volatility. Often institutions are forced to sell these assets as a result of an inability to manage the underlying real estate and/or recapitalize the assets, corporate balance sheet pressures, and regulatory constraints. The Manager is experienced in evaluating both real estate fundamentals and complex bankruptcy processes, thereby creating investment opportunities to either acquire assets from financial institutions or team-up with under-capitalized borrowers who have opportunities to acquire their own debt at an attractive discount.

**Development.** Certain local markets experience shortages of new office, residential, retail and hospitality products, even in difficult economic times. The Manager has a

strong track record of successfully developing and subsequently selling numerous residential, retail, hotel and office projects. The Manager continues to focus on development opportunities in situations characterized by strong long-term fundamentals, significant barriers to entry, and operating partners with execution expertise.

## **EXECUTION OF STRATEGY AND MITIGATION OF RISKS**

**Proprietary Deal Flow.** RECP generates significant proprietary deal flow through relationships that have been developed by its senior partners and its existing global network of strategic operating partners, as well as Credit Suisse's investment banking group and other real estate professionals. Through these proprietary opportunities, the Manager seeks to invest capital efficiently and take advantage of limited competition to acquire assets with attractive pricing. Approximately 80% of the RECP Funds' investments were sourced through proprietary transactions, situations characterized by limited competition or exclusive arrangements with local operating partners. Substantially all of the current pipeline transactions for RECP IV were generated from existing partner relationships and proprietary opportunities sourced through the Credit Suisse network.

**High Quality Local Partners.** RECP professionals work with experienced local operating partners who have specific geographic or product expertise, provide proprietary deal flow and contribute meaningful equity to align their interests with those of the Fund. Several of these partners work with RECP in exclusive joint-venture relationships, securing future proprietary deal flow. These relationships also enhance the Manager's ability to react quickly to market dynamics and to successfully implement complex value enhancement programs. The Manager has ongoing arrangements with more than 20 local operating partners that are expected to continue to provide RECP IV with proprietary deal flow.

**Diligent Investment Review and Structuring.** RECP engages in a detailed due diligence process, including the rigorous review of risk factors, the structuring of efficient capital and tax vehicles, and the evaluation of multiple exit strategies. The Manager places particular emphasis on mitigating downside risks while maximizing upside potential through creative financial structures. RECP actively manages risk through tax planning, insurance, currency and interest rate hedging, and cash management.

**Proactive Asset and Risk Management.** Asset management is a critical element of RECP's investment process and the senior investment professionals retain responsibility for their investments from acquisition through disposition. At the time of acquisition, a comprehensive asset management plan is created which serves to benchmark each investment's performance. Thereafter, RECP carefully adapts business plans to changing local market conditions and to actively identify attractive exit opportunities.

**Alignment of Interests.** Credit Suisse, its affiliates and their employees have committed to invest \$200 million in RECP IV's investment program, of which at least \$20 million will be committed through a Credit Suisse-sponsored co-investment program for the RECP investment professionals. Moreover, a significant component of the investment professionals' compensation will be tied to their participation in the carried interest received by the General Partner of the Fund.

**Global Presence.** RECP expects to continue to benefit significantly from the global platform of Credit Suisse. These benefits include Credit Suisse's strong presence in the U.S., Asia and Europe. In Asia, Credit Suisse has a leading franchise with offices in China, Hong Kong, Japan, India, Korea, Taiwan, Indonesia, Malaysia, the Philippines, Singapore and Thailand. In the EMEA region (Europe, Middle East and Africa), Credit Suisse has a presence in 28 countries. Globally, Credit Suisse is active in over 50

countries and employs approximately 45,000 people. Finally, Credit Suisse's industry-leading real estate debt and equity banking businesses, along with the firm's extensive financing capabilities, provide further unique opportunities to source attractive transactions.

**Market Opportunity.** The current market environment continues to offer extensive opportunities consistent with RECP IV's investment approach. Strengthening real estate fundamentals in select U.S., Asian and European markets present attractive opportunities to target asset repositionings, capital market dislocations, government and corporate divestitures, distressed debt and development opportunities.

## **MANAGEMENT OF THE FUND**

RECP benefits from a seasoned team of 29 dedicated real estate private equity professionals located in New York, Los Angeles, Tokyo, and London. The team is led by Andrew Rifkin, a founding member of RECP, who, together with his partners, is responsible for sourcing, analyzing, negotiating, acquiring and disposing of investments. Other senior partners include Robert Cavanaugh, Thomas Pulley and Carla Giannini, who are responsible for RECP's Los Angeles, Tokyo and London offices, respectively. Carmine Fanelle and William Helm are Managing Directors based in the New York office responsible for asset management and acquisitions, respectively. Collectively, RECP's six Managing Directors have 109 years of real estate industry experience and have been with the Manager for an average of 8 years. In addition, 11 of the 13 Directors and Managing Directors in RECP have been with the Manager since 2001 or before. The team has extensive expertise in the U.S., Europe and Asia across a comprehensive range of disciplines, including investment sourcing, operating partner selection, underwriting, due diligence, finance, structuring, and asset management:

**Andrew Rifkin, Managing Director.** Mr. Rifkin is managing partner of the RECP IV Investment Committee and oversees the Manager's overall acquisitions and asset management activities. Mr. Rifkin has been a senior member of RECP since its inception in 1995 and has been responsible for many of the successful investments in the RECP Funds. Prior to joining RECP, Mr. Rifkin was a Vice President at Goldman, Sachs & Co. in the Real Estate Principal Investment Area, where his responsibilities included asset management for various Whitehall portfolios. Mr. Rifkin was a recipient of Goldman's 1992 Innovation Award as a member of the Whitehall team that created and negotiated the original joint venture relationship between Goldman and the J.E. Robert Companies. Mr. Rifkin graduated with honors from the State University of New York at Binghamton with a B.S. in Mathematics and received an M.S. in Computer Science from Cornell University. He previously served on the Board of Directors of Anthracite Capital, a New York Stock Exchange listed mortgage REIT.

**Robert Cavanaugh, Managing Director.** Mr. Cavanaugh is a member of the RECP IV Investment Committee and oversees the Manager's acquisition and asset management activities in the western U.S. He is primarily responsible for sourcing, structuring and executing new investments, in addition to managing a number of RECP's existing partner relationships. Prior to joining RECP, Mr. Cavanaugh was responsible for overseeing the real estate investment banking and lending activities of Deutsche Bank (which had acquired Bankers Trust) in the western U.S. for a five-year period. Prior to Bankers Trust, he spent a total of ten years working in the real estate investment banking groups of LaSalle Partners and Goldman, Sachs & Co., first in New York and then in Los Angeles. Mr. Cavanaugh received a B.S. in Economics with honors from The Wharton School of the University of Pennsylvania and an M.B.A. from Harvard Business School.

**Thomas Pulley, Managing Director.** Mr. Pulley is a member of the RECP IV Investment Committee and is based in Tokyo, where he oversees the Manager's acquisition activities in Asia. Mr. Pulley began his career at Bankers Trust, where he founded the CMBS group and was responsible for acquiring over \$2.4 billion in sub-performing and non-performing real estate assets, which were ultimately securitized. Mr. Pulley was a member of Bankers Trust's Real Estate Equity Investment Committee and Management Committee. Mr. Pulley's experience in Asia and Europe includes his position as Head of Asian Principal Finance for UBS, based in Tokyo, and Head of Distressed Debt for Dresdner Kleinwort Benson, based in London. Mr. Pulley has successfully invested in distressed debt and real estate assets located in Germany, Eastern Europe, Thailand, Malaysia, the Philippines and Japan. Mr. Pulley received a B.A. from the University of California at Berkeley and an M.B.A. from The Wharton School of the University of Pennsylvania. Mr. Pulley passed the fourth level of the Japanese language proficiency examination administered by the Japanese government.

**Carla Giannini, Managing Director.** Ms. Giannini is a member of the RECP IV Investment Committee and is based in London where she oversees the Manager's acquisition activities in Europe. Ms. Giannini joined RECP in February 2006 from Invesco Real Estate in London where she was Chief Investment Officer for Continental Europe. Prior to that, she worked at Parkes and Company, which was acquired by Invesco Real Estate, where she managed the European principal and advisory business activities of the firm. Previously, Ms. Giannini spent fifteen years at Lend Lease Real Estate as an Executive Vice President and Board Director, and was a founding partner of its predecessor company, the Yarmouth Group. Ms. Giannini holds a B.A. with Honors in Economics from Harvard University.

**Carmine Fanelle, Managing Director.** Mr. Fanelle is the Chief Operating Officer for the RECP Funds and is based in New York. Mr. Fanelle worked for RECP since its inception in 1995 and worked with Mr. Rifkin since 1992. He completed numerous single asset, portfolio, and development transactions in both the U.S. and Europe. From 1998 to 2002, Mr. Fanelle lived in London and was responsible for several of the RECP Funds' European investments. In 2003, Mr. Fanelle returned to New York and became Head of Asset Management for the RECP Funds. Prior to joining RECP, Mr. Fanelle worked at Goldman, Sachs & Co. as a member of the Whitehall team and a member of the CMBS group. Mr. Fanelle graduated magna cum laude with a B.S. in Economics from The Wharton School and a B.S.E. in Computer Science Engineering from the University of Pennsylvania and later received an M.B.A. from The Wharton School of the University of Pennsylvania.

**William Helm, Managing Director.** Mr. Helm joined RECP in 1995 and is based in New York. Mr. Helm has been responsible for a broad range of investments including various property and portfolio acquisitions, operating partner relationships, development situations and structured financings. He has been particularly involved in RECP's New York City development transactions, as well as a number of distressed debt transactions and asset repositionings. In addition, Mr. Helm is actively involved in the ongoing asset management and oversight of a series of portfolio investments. Prior to joining RECP, Mr. Helm worked at Jones Lang Wootton Realty Advisors, a New York real estate advisory firm, as a member of the acquisitions and asset management groups. Mr. Helm received a B.A. in Economics from the University of Pennsylvania.

**James Allen, Chief Financial Officer.** Mr. Allen joined RECP in 1999 and is the Chief Financial Officer for the RECP Funds. Previously, Mr. Allen was Controller and oversaw all accounting, reporting, treasury and tax matters for RECP. Prior to joining RECP, Mr.

Allen was a Director and member of the Investment Committee in the real estate advisory group of UBS Brinson, with responsibilities that included all aspects of finance, treasury, accounting and investor reporting for the group's real estate advisory activities. Prior to joining UBS Brinson, Mr. Allen worked for seven years with the public accounting firm Ernst & Young focusing on large real estate clients. Mr. Allen received a B.S. in Accounting from Fordham University. Mr. Allen is also an active member of the National Association of Real Estate Investment Fiduciaries where he was previously the Chairman of the Accounting Committee.

## **CONCLUSION/RECOMMENDATION**

Based upon the successful track record and experience of the principals and the recommendation of PSERS' consultant, Courtland Partners, Ltd., staff recommends that the Board invest an amount equal to 25 percent of the committed capital, but not to exceed \$250 million plus reasonable normal investment expenses, in DLJ Real Estate Capital Partners IV, L.P. The final terms and conditions of the investment must be satisfactory to the Investment Office, the Office of Chief Counsel, and the Executive Director.