

Opportunistic Real Estate Fund Commitment



Blackstone Real Estate Partners Europe IV, L.P.

December 9, 2013

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Portfolio Manager, Real Estate

Blackstone Real Estate Partners Europe IV, L.P. - Opportunistic Real Estate

Overview

- Fund size: €5 billion (hard cap)
- Opportunistic real estate fund targeting a broad range of real estate and real estate-related investments, focused in the UK and Continental Europe
- Founded in 1985, Blackstone Group has total assets under management of approximately \$230 billion, across real estate, private equity, credit and marketable alternatives
- Blackstone employs 775 investment professionals globally, of which 131 are Senior Managing Directors

Fund Strategy

- Focus on acquiring high quality assets by targeting large, complicated situations where competition is limited:
 - high quality properties at significant discounts due to distress
 - purchase debt at significant discounts to par or sponsor basis
 - execute a strategy to fix the issues and then sell to core buyers at higher values

Investment Team

- London office staffed by 50 real estate professionals
- Vast majority of team investing today is same team that invested in predecessor funds

Blackstone Real Estate Partners Europe IV, L.P. – Opportunistic Real Estate

GP “Value Add”

- Consistent Team – the senior real estate professionals in Europe have an average tenure at Blackstone of 13 years
- Consistent Strategy – “buy it, fix it, sell it”
- Consistent Investment Process – limits risks and allows team to take advantage of the intellectual capital across the firm
- Ability to move in speed and scale to capitalize on larger fund size

Performance

- BREP Euro III (2009) net 1.4 MOIC and a 21.6% net IRR

Market Opportunity

- Asset values have been dramatically impacted by the distress in Europe resulting from the global credit crisis and European sovereign debt crisis
- European banking system still recovering and just beginning to address its credit issues, which has resulted in limited new lending
- Limited Opportunistic Capital, especially for large transactions
 - many competitors have either downsized or exited the market, or are focused on legacy issues

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History with PSERS

- PSERS has previously committed to BREP V, BREP VI, BREP VII, BREP Europe III and BREDS II

Board Issues

- Pennsylvania Presence – None
- Placement Agents – No placement agent used in respect to PSERS' commitment; however Blackstone utilizes an affiliate, Parkhill Real Estate, to raise other 3rd party capital
- PA Political Contributions – None
- Relationship with Consultant - No

Recommendation

- Staff, together with Courtland Partners Ltd., recommends that the Board invest an amount not to exceed \$100 million plus reasonable normal investment expenses

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November 14, 2013

Board of Trustees
Pennsylvania Public School Employees' Retirement System
5 North 5th Street
Harrisburg, PA 17101

Re: Blackstone Real Estate Partners Europe IV, L.P.

Dear Trustees:

Courtland Partners, Ltd. ("Courtland"), having been duly authorized by the Board of PSERS, has evaluated Blackstone Real Estate Partners Europe IV, L.P. (the "Fund"). The Fund will pursue an investment strategy that continues the strategy of Blackstone's predecessor European Fund. PSERS is an investor in the prior European fund. The Fund will invest in a broad range of real estate and real estate-related investments. The focus will continue to be on acquiring high quality assets by targeting large, complicated situations in which competition is limited and Blackstone's ability to move quickly is an advantage. The Fund will have the flexibility to invest in different property types and regions.

The investment themes that the Fund expects to pursue are as follows:

- **Purchase Debt in Order to Gain Control of Assets.** Blackstone expects to invest in debt securities at or near the position in the capital stack deemed to be the "fulcrum," or the cut-off point for current value, in order to position the Fund to take control of the assets or company through a debt restructure.
- **Equity Investment in Restructuring / Recapitalization.** Blackstone expects to be a capital provider to overleveraged owners of real estate who need capital to pay down debt and restructure their investments.
- **Dispositions by Motivated Sellers.** Blackstone expects to make investments where financial institutions and owners of real estate need to de-lever, clean up their balance sheets, or sell non-core assets.
- **Bankruptcy Situations.** Blackstone benefits not only from its extensive experience working through bankruptcies, but also from the Blackstone Advisory & Restructuring team's presence.
- **Public-to-Private Transactions.** Blackstone has a successful track record of converting publicly traded companies to private companies and subsequently creating value through a number of different avenues. The team has cultivated significant expertise through thirteen privatizations of public companies and Blackstone believes it can apply its "technology" to create significant value in the underlying assets. Blackstone has unlocked value in public real estate and real estate-related companies that it privatized by selling individual assets and/or geographically concentrated portfolios, trimming corporate overhead expenditures, borrowing more flexible and cost effective

debt capital, implementing more efficient tax structures, and uncovering “hidden assets” in the form of undervalued assets.

Blackstone believes that, similar to the U.S., leverage put in place between 2005 and 2007 on European real estate will lead to attractive debt investment and restructuring opportunities. With over \$800 billion of European property loans maturing over the next five years, Blackstone’s European team expects to pursue similar investment themes as in the U.S., as described above.

Some of Blackstone’s primary competitors have downsized or exited the real estate opportunity fund management business. There is likely to be less competition for the large deals typically favored by Blackstone. With an estimated €5.0 billion of capital, the Fund will be the largest European dedicated opportunity fund. The size of the Fund will give Blackstone the ability to purchase deals that would exceed the investment limit for competitor funds.

Courtland’s recommendation is based upon the following factors and is made within the context of PSERS’ investment guidelines.

- Detailed due diligence, including interviews with key Blackstone management team members, and review of all relevant materials.
- Evaluation of the Fund’s proposed investment strategy within the context of the current investment environment.
- Evaluation of Blackstone’s track record and organizational resources.
- Discussion and review of the market conditions in markets relative to the proposed investment strategy.
- The strategy proposed for the Fund is appropriate for the real estate component of the portfolio.

Based on the above factors, Courtland recommends that PSERS commit up to \$100 million to the Fund. Courtland makes this recommendation considering Blackstone’s qualifications and PSERS’ overall investment guidelines.

This recommendation is given solely for the benefit of PSERS and cannot be relied upon by other investors considering an investment in the Fund, since their needs, objectives and circumstances may not be identical to those of PSERS. The scope of this recommendation is limited to the investment merits of the Fund. Courtland does not provide legal or other non-investment-related advice.

Sincerely,



Steven Novick
Principal-Chief Operating Officer

COURTLAND PARTNERS, LTD.