

COURTLAND PARTNERS, LTD.

INSTITUTIONAL REAL ESTATE SERVICES

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November 11, 2014

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

Re: Senior Housing Partnership Fund V, L.P.

Dear Trustees:

Courtland Partners, Ltd. ("Courtland"), having been duly authorized by the Board of PSERS, has evaluated the Senior Housing Partnership Fund V, L.P., ("the Fund"). The Fund is sponsored Prudential Financial is a large, global financial institution, operating financial and insurance businesses worldwide. Prudential Real Estate Investors ("PREI"), the business unit in which the Fund's management team resides, is a global commercial real estate funds manager, with over \$59 billion in net AUM. PREI has been managing real estate investments for clients since 1970. The Fund will be PREI's fifth targeting the senior housing sector. PREI was influential in developing the dedicated senior housing investment strategy and has been making investments in the sector on behalf of institutional clients since 1998. There are few funds in the market with a dedicated senior housing platform like the Senior Housing Partnership fund series.

The Fund's investment strategy will primarily employ a few different investment approaches. The Fund will make direct acquisitions in existing communities either directly or through investments in wholly-owned subsidiaries or joint ventures. The Fund will invest primarily in stabilized income producing assets with occupancy levels typically not less than 50%. Forward equity commitments may be made by the Fund to acquire newly constructed communities, or interests in such communities, upon completion of construction as well. Under the terms of each forward commitment, the Fund will not accept exposure to development or property completion risk.

The Fund may also provide mezzanine and/or subordinate debt financing to communities and/or owners with potential property or operating company participation that may be secured by pledges of Fund interests or securities of borrowers or land, by other liens, or by guaranties.

The Fund intends to diversify by property type and will focus on investing in for-rent, for-profit, private-pay independent living, assisted living, and memory care communities, as well as properties that offer a combination of the three.

Fund investments shall be within the senior housing industry in markets throughout the U.S., and the Fund may invest up to 20% of the full commitment amount in investments outside of the U.S. in Canada, demonstrating a significant population of seniors within the age and income ranges for individuals that represent the targeted market for these types of senior housing.

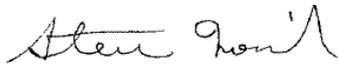
Courtland's recommendation is based upon the following factors and is made within the context of PSERS' investment guidelines.

- Detailed due diligence, including on-site interviews with key PREI management team members, and review of all relevant materials provided by PREI.
- Evaluation of the Fund's proposed investment strategy within the context of the current investment environment.
- Evaluation of PREI'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, Courtland recommends that PSERS commit up to \$100 million to the Fund. Courtland makes this recommendation considering PREI'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.



Value-Added Real Estate Commitment

Senior Housing Partnership Fund V, L.P.

December 8, 2014

See Last Page for Disclaimer

Laurann H. Stepp
Senior Portfolio Manager

Senior Housing Partnership Fund V, LP – Value-Added Real Estate

Overview

- Fund size is anticipated to be \$500 million
- Fifth in a series of closed-end commingled real estate funds targeting value-added returns, including a large component of income yield, through investments in senior housing real estate assets
- The investment adviser to this fund is Prudential Investment Management (PIM), which is an indirect wholly-owned subsidiary of PFI (Prudential Financial, Inc). PIM will fulfill its duties through a division known as PREI (Prudential Real Estate Investors), who oversees assets under management in excess of \$59 billion worldwide

Fund Strategy

- Invest in independent living, assisted living and memory care properties, focusing on acquisition of stabilized properties, and adding value through improving operations and developing properties
- Investments will be structured mainly as direct or joint venture acquisitions, and forward commitments, as well as potentially mezzanine investments. Up to 20% of the fund may be invested in Canada, whose senior housing market is very similar to the U.S. regarding demographics and operators, but where current prohibitive tax laws have historically eliminated investment opportunities

Senior Housing Partnership Fund V, LP– Value-Added Real Estate

Investment Team

- The fund will be managed by two Managing Principals, Noah Levy and Steve Blazejewski, in addition to six dedicated professionals located in Madison, NJ and Atlanta, GA. Additional operational support is provided by PREI

GP “Value Add”

- Proven experience with Noah Levy and Steve Blazejewski. Noah has been with Prudential for over 20 years building this concentrated niche platform in senior living real estate. They are able to evaluate situations to make the appropriate choice of the most effective operator; which is key to successful investments
- Performance for the first three funds has been above expectations, and those funds are in the top quartile of value-added funds in Courtland’s database
- Upon stabilization, annual income returns have on average exceeded 9%

Performance (as of June 30, 2014)

- SHP I (1998) returned a net 2.05x MOC and a 16.4% net IRR – 100% liquidated
- SHP II (2001) returned a net 3.44x MOC and a 29.7% net IRR – 100% liquidated
- SHP III (2006) currently has a net 1.74x MOC and a 8.57% net IRR. Projected net IRR = 9% and 1.8x net MOIC
- SHP IV (2011) currently has a net 1.13x MOC and a 7.43% net IRR. Projected net IRR 10-13%, and 1.5-2.0x net MOIC
- SHP V target will be to achieve a total return of 10-14% net of fees

Senior Housing Partnership Fund V, LP– Value-Added Real Estate

Market Opportunity

- There are approximately 19 million 75+ seniors in the United States today, and that age-group is expected to grow rapidly over the next decade. However, since 2007, senior housing construction starts have sharply declined, having been restrained by lack of financing during the financial crisis
- Fundamentals in the senior housing industry reflected resilience during the crisis, with effective rent growth remaining positive throughout the recession

Potential Risks

- **Small niche product within giant Investment Management Firm (PIM)**

Prudential has been involved with the Senior Housing sector since 1989, and Noah Levy has been leading the initiative since 1994. The niche created has been successful and the larger PIM continues to invest capital in the funds. Unfortunately individual employees are prohibited from investing in the fund due to structural/regulatory constraints. However, the compensation to the SHP fund employees is dependent on the success of the funds

- **Fund leverage increased to 65% from 50% in last fund**

When Fund IV was raised the leverage limit was cut back to 50% due to lingering LP concerns/issues. The first three funds used a 65% limit, although the average leverage was around 50%. The GP requested the limit be raised again to provide for flexibility in dealing with strong JV partners and to take advantage of the accretive leverage terms in the market today

Senior Housing Partnership Fund V, LP – Value-Added Real Estate

History with PSERS

- This will be PSERS second fund investment with Senior Housing Partners. At the December 2011 Board meeting a \$100M investment in Fund IV was approved
- Additionally, in 2006 PSERS invested \$100 million in PREI's Core Open-End fund, PRISA, and PSERS still holds three agriculture investments worth approximately \$30 million

Board Issues

- Pennsylvania Presence – SHP III owned 94% of a 171 unit project in East Norriton, PA through a joint venture with an operator, The Shelter Group until it was sold on July 31, 2014
- Placement agents – none
- PA political contributions – none
- Relationship with consultant – none

Recommendation

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

Notice: This document was presented to the Public School Employees' Retirement Board at the public meeting at which the Board acted on the resolution to which the information relates. The sole purpose for posting the presentation information on this website is to enable the public to have access to documents that were utilized at a public meeting of the Public School Employees' Retirement Board, and no other purpose or use is intended.