



COMMONWEALTH OF PENNSYLVANIA
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

Public Investment Memorandum

Exeter Core Industrial Club Fund II, L.P.

Real Estate Commitment

Laurann H. Stepp
Senior Portfolio Manager

December 7, 2015



Recommendation:

Staff, together with Courtland Partners, recommends to the Board a commitment of up to \$100 million to Exeter Core Industrial Club Fund II, L.P. ("Fund II" or the "Fund"). Exeter Property Group ("Exeter" or the "Firm"), a northern Philadelphia headquartered private investment firm, is sponsoring the Fund to make investments in a diversified portfolio of cash flowing industrial properties.

Firm Overview:

Exeter Property Group was founded in 2006 by Ward Fitzgerald, CEO and Tim Weber, CFO and is 100% owned by ten Exeter professionals. The Firm's primary focus is investing in industrial properties in the United States and Europe. The Firm has approximately 65 employees, and is fully integrated, with in-house property and construction management, accounting, leasing, and asset management. Exeter manages three types of investment vehicles focusing only on industrial properties; core, value-added and European properties. Current assets under management ("AUM") are estimated to be \$2.7 billion. The Fund will be managed by Exeter Core Platform II, LLC. , ("Investment Manager") which is controlled by the Firm's Senior Principals through their ownership of Exeter Core Industrial Club Fund Management II, LLC (the "General Partner").

Investment Strategy:

The Fund will build a diversified portfolio of single asset properties and small multi-building packaged industrial property transactions. These cash-flowing facilities will be located within 34 major distribution markets across the United States, with at least 66% invested in prime markets and no more than 20% in one market. The Investment Manager expects to allocate Fund II as follows:

Strategy	Allocation
Bulk Distribution facilities (Big box warehouse)	75%
Last Mile Distribution (Light Industrial)	25%
17 Premium/Prime markets	66%
Initial property occupancy	93%
Minimum lease term	4 years

Additionally, the Fund may invest in forward-funded development transactions where there is a signed lease with terms congruent with the fund. These may require partial funding up to ten months prior to lease commencement, but will have minimum returns 25-100bp higher than the rest of the portfolio.

Investment Team:

Exeter's investment activities are led by Ward Fitzgerald and Tim Weber, and the Portfolio Manager for the Core Fund will be Tim Walsh. In total, Exeter has an experienced team of 31 dedicated investment professionals located in Plymouth Meeting (headquarters), DC, Louisville, Memphis, Tamarac, Atlanta, Dallas, Chicago, San Francisco, Phoenix, Indianapolis, Columbus and Los Angeles.

Investment Instruments:

Investments are expected to be wholly owned real estate industrial properties.

Investment Structure:

Delaware Limited Partnership, with several tax efficient subsidiaries, including REITs for the real estate investments.



Market Opportunity:

Favorable supply-demand environment supports additional income growth, as trade and population growth continue to drive warehouse demand. Following several years of rent growth, in-place leases are substantially below market and will boost industrial property NOI as renewed. National vacancy levels have fallen to 6.1% as of 6.30.15, the lowest level in fifteen years. Net absorption of supply in the first half of 2015 nearly doubled the level of completions. The developers in the early recovery markets that were first to provide supply in 2014 have already pulled back, most likely due to better availability of data, stricter lending sources, and rising construction costs. Strong investor demand for diversified, income-producing portfolios of large scale continues to drive robust exits.

Investment Highlights:

Experienced & Cohesive Senior Management Team
Management team has been together over an average of fifteen years, and has 25 years' experience, which covers multiple market cycles since the late 1980's. Exeter has not lost any members during or after the financial crisis. The firm is privately owned by ten employees, and approximately half of the firms' employees participate in the carry of the Funds.
Track Record / Strong Cash Flow
Throughout multiple market cycles Exeter has displayed strong results, with returns in the 1 st quartile. Exeter capitalizes on local market knowledge, in-house asset management, strong tenant relationships and full ownership control. Their reputation has instilled a sense of confidence in their markets regarding their integrity and performance.
Market Knowledge
Leasing success with national tenant relationships as well as local market knowledge and relationships give Exeter the ability to favorably source, lease and price deals. Due to extensive relationships, historically over 50% of the Exeter investments have been sourced off-market or were limited competition situations.

Investment Considerations:

Competition From Other Capital Sources
Although there are multiple capital sources searching for yields, access to the industrial marketplace at the level that Exeter enjoys is hard to replicate. Their sole industrial focus that is executed through regional offices provides a competitive advantage. Expertise in repositioning, redeveloping and developing properties has allowed them to select investments that others may avoid, at more attractive pricing. After developing, renovating and leasing, Exeter has created core portfolios to extract disposition premiums upon exit. Exeter uses its diverse tenant and owner connections to respond quickly to opportunities.
Term of Partnership
PSERS has identified Exeter as a highly regarded key Partner within the real estate portfolio. The most efficient way to maintain an exposure to the Core industrial real estate market is to aggregate and hold a portfolio of key properties that provide a net income return of 6.5-7% annually until the market pricing is accretive to sell. This twelve year fund, with two three-year extension periods will allow Exeter to return a higher multiple of invested capital while allowing for the ability to work through market cycles without pressure to sell.
Development Risk
While there is always risk in real estate associated with potential development, industrial property has the added risk of the short period of time required to develop the projects. Although the market to date seems to be self-moderating the developments in progress, in this Fund Exeter will only fund forward commitment developments. These commitments will only be made with a signed lease at a rate above the stabilized market rate, for a longer term (approximately seven years) and are funded after the owners' equity investment.



PSERS History & Performance:

Since 2011, PSERS has committed \$150 million to two Exeter Value partnerships. The following table summarizes PSERS' historical performance with Exeter Value funds as well as the first Exeter Core Fund as of June 30, 2015:

Fund (\$M)	Vintage	Fund Size	Commitment	Contributions	Distributions	NAV	Net IRR	MOIC
Exeter Value Fund II, LP	2011	615.0	75.0	73.5	34.8	77.6	22.8%	1.5x
Exeter Value Fund III, LP	2014	832.8	75.0	22.5	0	23.4	7.1%	1.0x
PSERS Sub-Total (Value Add funds)		\$150.0		\$96.0	\$34.8	\$101	22.11%	1.4x
Exeter Core Club Fund I, LP	2012	404.0	0.0	369.0	59.4	433	16.0%	1.29x

Portfolio Fit:

A commitment to this fund will be allocated to the Core bucket of PSERS' Real Estate portfolio. As of June 30, 2015, the Real Estate portfolio (based on total exposure) was invested 56.3% Opportunistic, 32.7% Value-Added, 11.1% Core. The Fund's strategy will increase PSERS' core exposure, which is currently below a long term target of 20%.

The table below summarizes PSERS' projected exposure, as of 9.30.15, inclusive of a recommended \$100 million commitment to Core Fund II:

Investment Type	Active Commitments (1)	%	Market Value	%	Unfunded (1)	%	Total Exposure (1)	%
Opportunistic	\$9,661.4	58.6%	\$3,314.0	62.4%	\$1,117.7	43.5%	\$4,431.7	56.3%
Value-Add	\$5,225.6	31.7%	\$1,474.4	27.8%	\$1,099.5	42.8%	\$2,573.9	32.7%
Core	\$1,592.8	9.7%	\$522.7	9.8%	\$350.0	13.6%	\$872.7	11.1%
Total	\$16,479.8	100.0%	\$5,311.1	100.0%	\$2,567.2	100.0%	\$7,878.3	100.0%

(1) Includes post Q2'2015 pending/closed commitments.

Liquidity & Leverage Profile:

The Fund is expected to be invested within four-years of its final closing (the "Investment Period"), with the ability to recycle proceeds within this period. After the Investment Period, upon a super-majority vote of the Limited Partners, the Fund will be permitted to recycle proceeds. The Fund will make quarterly distributions, and expect to generate current income returns of 6.5-7%. The Investment Manager will employ up to 50% fund-level leverage.



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Finance Committee Disclosure:

Relationship with Courtland:	N/A
Placement Agent:	Not used
PA Political Contributions:	None Disclosed
PA Presence:	22 investments totaling 5.3 million square feet, \$445M mkt value
Conflicts:	None Disclosed
First Time Fund With PSERS:	No
PSERS Internal Alpha Committee Approval:	November 20, 2015

Oversight Responsibility:

Investment Office:	Charles J. Spiller	Managing Director
	Laurann H. Stepp	Senior Portfolio Manager
External Consultant:	Courtland Partners	

COURTLAND PARTNERS, LTD.

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November 11, 2015

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

Re: Exeter Core Industrial Club Fund II, L.P.

Dear Trustees:

Courtland Partners, Ltd. ("Courtland"), having been duly authorized by the Board of PSERS, has evaluated Exeter Core Industrial Club Fund II, L.P. (the "Fund"). The Fund's investment strategy is to create, and hold for the long-term, a diversified core portfolio of well-leased, modern, Class A industrial properties in primary population centers and high-growth e-commerce fulfillment hubs across the United States. Exeter's real estate operator team will assemble the Fund portfolio through multiple one-off acquisitions. Approximately 75% of the portfolio will be bulk distribution facilities (big box warehouse) and 25% last-mile distribution (light industrial) facilities. This mix is intended to provide an efficient, logistics-oriented portfolio that is diversified across market types (regional/local consumption, air cargo, and intermodal distribution) and tenant bases.

It is the Manager's thesis that both consumption and population growth drive warehouse demand. The Fund has chosen 17 markets that account for the majority of both these drivers in the U.S. The Manager is targeting distribution markets that service: A) the region from New York to Philadelphia to Washington, DC in the Northeast/Mid-Atlantic; B) the Atlanta and Central Florida markets; C) the Texas Triangle, particularly Dallas, Houston and Austin; D) the Chicago/Mid-South markets that have benefited from the migration of population and commerce from mature Mid-Western metropolitan areas; and E) the Western markets of Los Angeles/Long Beach, San Francisco and Phoenix. Exeter believes in investing in the most stable or high-growth emerging primary distribution markets whose sustained industrial product demand is driven by strong demographic trends. The Manager will also focus on major intermodal (rail/truck) and air/e-commerce transportation hubs, which are increasingly important to the U.S. distribution network, as the large scale movement of goods continues to create industrial real estate demand.

The portfolio will be designed to generate stable income, as the Fund will acquire fully leased assets (minimum 93% occupancy), with initial yields on cost ranging from 5.75% to 6.75% and long-duration leases in place (minimum 4 years remaining term). This stabilized profile provides for steady cash flows and minimal capital requirements for new tenant improvements, leasing commissions and lost operating expenses. The security of the cash flows will be further augmented through the aggregation of a large portfolio that will provide for staggered lease expirations and the diversity of a large base of regional, national, international tenants which will reduce the impact of any one lease on the total income stream.

The strategy also provides for secure net cash flows by minimizing and controlling property operating expenses. All or nearly all the leases will have a triple net rent structure; as a result tenants take

responsibility for any increases in operating expenses. Furthermore capital improvements will be limited given the targeted modern construction. Capital expenditures will also be lessened due to the assets' low office finish (maximum 10% of rentable square feet) and desirable generic modern design. Further, the large scale distribution/logistics nature of the assets will provide for economies of scale in portfolio maintenance, leading to a low average per square foot operational cost structure.

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 Exeter management team members, and review of all relevant materials provided by Exeter.
- Evaluation of the Fund's proposed investment strategy within the context of the current investment environment.
- Evaluation of Exeter'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 Exeter'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.