



---

---

Public Investment Memorandum

**Cabot Industrial Value Fund VI, L.P.**

Value-Add Real Estate Commitment

---

---

**Melissa A. Quackenbush**  
Senior Portfolio Manager

**July 3, 2019**



### **Recommendation:**

PSERS Investment Office Professionals ("PSERS IOP"), together with Hamilton Lane, recommend the Board commit up to \$100 million to Cabot Industrial Value Fund VI, L.P. Cabot Properties, L.P. ("Cabot" or the "Firm") seeks to continue to provide consistent real estate returns by value-add investing in industrial properties, located primarily in the United States, with up to 35% in non-U.S. investments.

### **Firm Overview:**

Cabot Properties L.P., based in Boston with a regional office in London, is a leading vertically integrated industrial property firm with over 30 years of history acquiring, developing, operating, leasing, financing and selling industrial properties through multiple market cycles.

Cabot was initially formed in 1986 as an affiliate of Cabot, Cabot & Forbes, at that time one of the oldest and most respected real estate development, investment, construction, and management firms in the U.S. In those early years, Cabot focused on providing real estate investment advice to a limited number of large, sophisticated investors. Registered with the SEC under the Investment Advisers Act of 1940, Cabot was able to offer complete advisory and fiduciary capabilities for buying, managing, improving, and selling real estate assets. Cabot provided investors the option to maintain their own separate account or invest in a highly selective partnership program. Of paramount importance was the fact that each portfolio was geared to fit prerequisites based on client objectives, market opportunities, and economic conditions.

Cabot grew this business to \$1 billion in assets under management by 1997. In early 1998, certain Cabot clients and other investors (including PSERS) contributed assets into an initial public offering to create Cabot Industrial Trust (the "Cabot REIT"). Beginning with the formation of the Cabot REIT, the Cabot team had the ability to invest on a fully discretionary basis.

Between January 1998 and December 2001, the Cabot REIT purchased 132 investments representing 266 properties. In December 2001, the Cabot team sold the Cabot REIT to a buyer in an all cash transaction valued at \$2.1 billion.

In November 2001, Cabot Properties L.P. was formed by certain senior officers of the Cabot REIT including Franz F. Colloredo-Mansfeld, Howard B. Hodgson, Jr., and Mark A. Bechard, among others. Since 2001 Cabot has continued focusing on acquiring, developing, redeveloping, operating, leasing and selling value-added and core industrial properties on behalf of investors via a series of limited partnership funds.

In 2017, Cabot also commenced a separate account program for a German-based pension fund. This separate account strategy is focused on industrial core plus properties in large North American markets. In 2018, after the sale of the remaining U.S properties of Value Fund IV was negotiated, the purchaser retained Cabot to provide asset management services for all the properties purchased in the transaction. Also in 2018, Cabot was awarded its second separate account with a long-time U.S. public pension fund client.

Cabot is now a privately-owned, registered investment adviser with assets under management of over \$2.0 billion as of December 31, 2018. Value Fund I, III & IV have been successfully liquidated at net IRRs and multiples well in excess of initial targets. Value Fund II was negatively impacted by the global financial crisis, but that notwithstanding, Value Fund II delivered a solid 1.3x multiple of capital.



**Market Opportunity:**

The current market opportunity is driven by consumerism, specifically the growth in eCommerce, and the consumer preference for faster delivery times. As consumers want quicker delivery of purchased items, this has resulted in a significant shift in the supply chain causing the number of warehouse/distribution facilities to increase in order to be closer to the population. The chart below illustrates this point.

Optimum Facility Count for Required Service Levels in U.S. (to cover 90% of population) <sup>1</sup>			
Target Service Level	2-3 days	Next day	Same day
Radius Covered by 1 Facility	~650 miles	~150 miles	~90 miles
Number of Facilities Needed	~5	40-50	80-100

<sup>1</sup>Source: inboundlogistics.com; Data as of 1/17/2017

As the demand for facilities continues to grow, this puts downward pressure on vacancy and upward pressure on rents. Vacancy rates across nearly all of Cabot's U.S. target markets remain below pre-recession levels and new supply accounts for just 1.9% of the total amount of industrial property capacity overall, an indication that supply and demand should remain in balance. As of Q3 2018, demand has exceeded supply for 32 out of the last 33 quarters. Rent growth, while having slowed somewhat, continues to be positive. Average year-over-year rental growth rate was 6.2% across the industrial sector nationally in 2018.

Cabot believes the outlook for the industrial sector is positive. While much of the logistics demand will be centered around major markets with large population centers and complex supply chains, secondary markets with strong demographics are playing an increasingly more important role reflecting the new supply chain paradigm. Cabot's proven ability to assemble institutional quality portfolios in target markets will complement increased investor demand for this product type and drive a more robust exit strategy.

**Portfolio Fit:**

A commitment to the Fund will be allocated to the Value Add Real Estate portion of PSERS' Real Assets portfolio. Using the net market value from December 31, 2018, and adjusting the unfunded to include commitments from the prior and current Board meetings, the Real Estate portfolio would be 20.7% Core, 38.9% Opportunistic, and 40.3% Value-Added.

The table below summarizes PSERS' projected exposure inclusive of a recommended \$100 million commitment to the Fund as of December 31, 2018 and excludes exposure to the open-end redemptions:

Investment Type (\$M)	Market Value <sup>(2)</sup>	%	Unfunded	%	Total Exposure <sup>(1)</sup>	%	Long Term Target (%)
Core	1,436.0	26.8%	307.5	10.1%	1,743.5	20.7%	20%
Opportunistic	2,231.1	41.7%	1,041.6	34.1%	3,272.7	38.9%	30%
Value-Add	1,688.7	31.5%	1,701.4	55.8%	3,390.2	40.3%	50%
<b>Total</b>	<b>\$ 5,355.8</b>	<b>100%</b>	<b>\$ 3,050.5</b>	<b>100%</b>	<b>\$ 8,406.3</b>	<b>100%</b>	<b>100%</b>

<sup>(2)</sup> Includes Gross PTRES Exposure

### **Investment Strategy:**

The Fund strategy will focus on accretive acquisition, development, redevelopment, operating, leasing and selling of industrial properties. Targeted investments will be value-add in nature and tend to be smaller in size from both physical and capital perspective. Target markets will be thoughtfully selected to maximize residual value and expose the portfolio to long term income growth driven by attractive demographic and supply chain trends.

The Fund will pursue industrial deals based on (i) locations with growing demand, (ii) disciplined underwriting and valuations, (iii) ability to enhance value through active management, (iv) maximizing distributable current income, and (v) multiple exit options for harvesting gains.

### **Investment Structure:**

The Fund is a Delaware Limited Partnership that is operated in Boston. The General Partner will be Cabot Industrial Value Fund VI Manager, Limited Partnership, a Massachusetts limited partnership.

The Fund's sponsor, Cabot Properties L.P., was formed in 2001 as a Delaware Limited Partnership and is registered as an investment adviser with the SEC. The firm is an employee-owned private partnership.

### **Investment Instruments:**

Investments are expected to primarily be interests in real estate properties. The Fund is also authorized to invest up to 5% in mezzanine debt or publicly traded securities.

### **Investment Team:**

Cabot headquarters is in Boston, where they employ 51 individuals, including the six senior partner members of the Fund VI Investment Committee that have worked together at Cabot an average of 22 years. The average tenure at Cabot for the entire investment professional team is 12 years (AVP and above).

### **Investment Highlights:**

- Strong, consistent value add performance results
- Cycle tested Manager with single asset focus and demonstrated investment discipline
- Experienced and cohesive Senior Management Team/Team of Investment Professionals
- Return profile weighted more towards current income
- Favorable market conditions



**Investment / Risk Considerations:**

- Competition for deals
- Slowing of the industrial real estate sector
- Possible geographic expansion
- Use of leverage

**PSERS History & Performance:**

PSERS relationship with Cabot began in 1998, when PSERS' directly held industrial properties valued at \$110 million, were traded for 5.5 million shares of the public Cabot REIT. The shares were tendered in 2001 for a gain of \$22 million and a net IRR of 11.3%.

PSERS has committed to five Cabot funds, and the table below summarizes these investments and performance as of December 31, 2018. Not reflected in the table is a £50 million commitment to Cabot UK Core-Plus Industrial Fund SCSp which was approved at the March 2019 Board meeting; this deal is still in legal negotiation and has not yet closed.

<b>Fund (\$M)</b>	<b>Vintage</b>	<b>Fund Size</b>	<b>Commitment</b>	<b>Contributions</b>	<b>Distributions</b>	<b>NAV</b>	<b>Net IRR</b>	<b>Net MoC</b>
Cabot Industrial Core Fund, L.P.	2015	443.0	150.0	147.3	14.9	174.3	13.9	1.3
Cabot Industrial Core Fund II, L.P.	2018	600.0	100.0	-	-	N/A	N/A	N/A
Cabot Industrial Value Fund III, L.P.	2008	679.6	100.0	81.7	123.2	-	21.9	1.5
Cabot Industrial Value Fund IV, L.P.	2013	712.0	75.0	72.7	116.7	0.3	28.1	1.6
Cabot Industrial Value Fund V, L.P.	2016	775.0	100.0	36.1	0.8	38.6	20.0	1.1
<b>Total</b>			<b>\$525.0</b>	<b>\$337.8</b>	<b>\$255.6</b>	<b>\$213.2</b>	<b>20.7%</b>	<b>1.4x</b>

**Finance Committee Disclosure:**

<b>Relationship with Hamilton Lane:</b>	None Disclosed
<b>Introduction Source:</b>	Fund Sponsor
<b>Placement Agent:</b>	No
<b>PA Political Contributions:</b>	None Disclosed
<b>PA Presence:</b>	As of December 31, 2018, Cabot has three investments in PA which have a market value of approximately \$49 million. Eastern and central PA are two of Cabot's target markets.
<b>Potential Conflicts:</b>	None disclosed to PSERS
<b>First Time Fund With PSERS:</b>	No, this will be PSERS seventh fund investment with Cabot.
<b>PSERS Allocation Implementation Committee Approval:</b>	July 3, 2019

**Oversight Responsibility:**

<b>Investment Office:</b>	Charles J. Spiller Melissa A. Quackenbush	Deputy CIO, Non-Traditional Investments Senior Portfolio Manager
<b>External Consultant:</b>	Hamilton Lane	



# Hamilton Lane

June 20, 2019

Board of Trustees  
Commonwealth of Pennsylvania  
Public School Employees' Retirement System  
5 North 5<sup>th</sup> Street  
Harrisburg, PA 17101

Re: Cabot Industrial Value Fund VI, L.P.

Dear Trustees:

Cabot Properties, L.P. ("Cabot") was formed in 2001 by certain former members of Cabot Industrial Trust, a public REIT that was launched in 1998 with assets contributed by clients of an affiliate of Cabot, Cabot & Forbes. At the end of 2001, Cabot Industrial Trust was sold, with senior members of the REIT forming the General Partner. Cabot is a vertically integrated industrial property firm that oversees approximately \$2 billion in assets as of December 31, 2018; the General Partner is comprised of 51 professionals in aggregate, split between 6 senior professionals, 12 other investment professionals, 12 asset management professionals and 21 additional employees. Cabot has focused on industrial assets across risk types since inception, which has provided it with a reputable brand as an active platform that is able to transact efficiently, enabling it to competitively source and exit opportunities. Additionally, Cabot's exclusive focus on industrial properties allows for efficient oversight and business plan execution. The General Partner has executed on a value-add strategy since inception, providing it with expertise across a wide range of projects. Cabot is targeting \$800 million in commitments for its sixth value-add industrial fund, Cabot Industrial Value Fund VI, L.P. (the "Fund"). Cabot expects to hold a first close in October 2019. The General Partner will commit at least 2% of commitments (up to \$15 million) to invest in the Fund.

Consistent with prior funds, Cabot expects the Fund to primarily concentrate on value-add industrial opportunities located in a concentrated set of supply-constrained markets that are supported by large and dense populations. The General Partner intends to primarily focus on investments within the United States, allocating approximately 80% of the Fund in North America, and may not invest more than 20% outside of North America. Cabot maintains a flexible approach to portfolio construction and intends to invest in a mix of stabilized assets, repositioning investments and development projects. The General Partner expects to invest 60% of the fund in stabilized properties, 25% in repositioning investments and 15% in development properties. When pursuing a development opportunity, Cabot targets occupied industrial parks with one to two undeveloped sites. The General Partner targets high-quality buildings that appeal to multiple tenant profiles and that have been designed for efficient transfer and storage of inventory with multiple access points. Cabot also emphasizes appropriate external characteristics, such as appropriate truck courts and parking, while targeting limited office space, in order to further appeal to its targeted tenant base. The General Partner has developed a repeatable value creation approach, primarily focusing on light value-add initiatives across operating and repositioning investments. Cabot's asset management team, in tandem with its property managers, develop a yearly plan to track key growth initiatives and expectations for each asset's expected net operating income and occupancy growth. Value creation has historically been driven through annual cash yields, complemented by modest asset appreciation. The Fund will target 80 to 100 equity investments in the range of \$5 million to \$20 million, targeting properties valued between \$5 million and \$20 million. Cabot has consistently outperformed top-quartile peers and benchmarks on a net IRR basis.

Cabot Industrial Value Fund VI's investment thesis can be summarized as follows:



# Hamilton Lane

- Longstanding platform with exclusive focus on industrial sector
- Consistent approach to portfolio construction and value creation initiatives
- Top-quartile performance across prior funds driven by consistent cash yields and appreciation at exit

Hamilton Lane's recommendation is based upon the following analytical factors and is made within the context of Commonwealth of Pennsylvania, Public School Employees' Retirement System's ("PSERS") investment guidelines.

- Detailed due diligence, including interviews with industry peers and private equity professionals. The initial review was completed April 11, 2019; the on-site due diligence was conducted May 21, 2019; the Fund was approved by Hamilton Lane's Investment Committee on June 3, 2019 and the recommendation to PSERS was issued June 20, 2019
- Evaluation of the composition of the investment team, how they work together, compensation structure and other factors that help determine whether a group is likely to be able to replicate past successes as currently configured
- Detailed operational due diligence, including interviews with Cabot's back office team to review the controls and processes surrounding the firm's finance, fund administration, tax, legal, compliance, IT, HR, and accounting functions
- Evaluation of the Fund's proposed investment strategy within the context of the current investment environment
- The strategy proposed for the Fund is appropriate for the Private Real Estate component of the portfolio

The individuals at Hamilton Lane who were involved in the due diligence process for the Fund are:

Radhika Cobb – Vice President, Bala Cynwyd Office

Samuel Sugarman – Analyst, Bala Cynwyd Office

Chelsea Yasgur – Analyst, Bala Cynwyd Office

Based on the above, Hamilton Lane recommends that PSERS commit up to \$100 million in Cabot Industrial Value Fund VI, L.P. Hamilton Lane makes this recommendation considering the General Partner'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. Hamilton Lane does not provide legal or other non-investment-related advice.

Sincerely,

Michael Koenig,  
Chief Client Officer

Corina English,  
Principal