2020 PREQIN GLOBAL **REAL ESTATE** REPORT

SAMPLE PAGES

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Contents

Executive Summary

Private real estate enjoys another year of growth, but deal numbers decline as asset prices rise

Even as the global economy weakened in 2019, private real estate continued to grow. Investors seeking real estate's steady cash flows poured more capital into the sector, driving the total amount of funds raised to $151bn, an all-time high. The increase in dry powder – along with a 5.3% rise in unrealized value – boosted assets under management (AUM) to a record $992bn as of June 2019, marking the fourth consecutive year of AUM growth for the industry.

However, there are some cautionary indicators. First, fewer vehicles reached a final close in 2019. The number that did close fell to 295, the lowest total in a decade; in 2009, during the Global Financial Crisis (GFC), just 229 funds closed.

Second, capital consolidation in the industry deepened. Forty-four percent of the total capital raised was amassed by the 10 largest funds. Just two of those funds dominated the entire fundraising landscape: Blackstone Real Estate Partners IX, which secured $20.5bn to become the largest private real estate fund ever closed, and Brookfield Strategic Real Estate Partners III, which hoovered up $15bn to become the third largest such fund.

Third, deal volume and value fell amid concerns over rising valuations. Three-quarters of real estate fund managers we surveyed in November 2019 said that asset prices were higher than they were 12 months ago, and rather than pay too much for targets they perceived to be overvalued, some GPs stayed on the sidelines. As a result, the total number of private equity real estate (PERE) deals slid by 4.7% compared with the year before, while aggregate deal value slumped by more than 10%. Even as market conditions became more challenging, fund managers with massive amounts of financial firepower continued to put capital to work. In September 2019, the same month in which Blackstone Group set a record for raising private real estate's largest-ever fund, the firm set another one when it acquired Singapore-based GLP's US logistics portfolio for $18.7bn. This is the largest-ever PERE deal.

Fund Managers Turn to Higher-Risk Strategies and New Niches

Market participants adapted to tougher times in different ways. Some investors sought safety, helping core funds to secure more than 3x as much capital as the year before. Others opted for higher-risk strategies. The result was that aggregate capital raised by opportunistic funds surged by 38% to almost $70bn in 2019, while the amount raised by distressed funds rose by more than 8x to $8.4bn.

As competition intensified, fund managers went on the prowl for promising new niches. One such niche is PropTech, a sector comprising a broad range of businesses that are using technology in innovative ways (see page 28). These days, more real estate companies are looking to improve operational efficiencies with the help of new technologies. This has bolstered demand for the products and services offered by businesses operating in the PropTech space. Fund managers are well aware of the potential. In 2019, there were 209 real estate technology-focused buyout and venture capital deals, amounting to $13bn in total value; that is almost double the value recorded in 2018.

What's in Store in 2020

As 2020 kicks off, there are 918 funds on the road targeting an aggregate $281bn, an all-time high for both figures. The good news for fund managers is that investor appetite remains healthy. Ninety-three percent of the investors we surveyed plan to either maintain or increase their allocation to real estate beyond 2020. This is not a surprise, given that 87% of investors expressed satisfaction with the performance of their real estate portfolios over the past 12 months. For fund managers, the challenge will be maintaining that performance even if market conditions worsen.

Real Estate Megatrends

Key themes shaping the private real estate industry

Capital Consolidation

Established managers' share of capital raised is growing, with even larger funds coming to market.

Competition for Deals

Heightened competition for assets is driving up valuations, affecting potential returns.

Complex Niches

New niches such as PropTech and new avenues in retail are shaping the industry as they grow.

ESG

ESG is a key consideration when making investment decisions for investors and fund managers alike.

Expected Correction

Many agree that we are heading toward a market slowdown, but the timing of this correction is disputed.

Data Pack

The data behind all of the charts and tables featured in this report is available in Excel format at no extra cost. This data may be used in marketing materials, presentations, or company reports with appropriate accreditation to Preqin.

Investing in Tomorrow's World Real Estate

As the market evolves at an unprecedented pace, shaped by the rise of technology and ESG, managers have to flex and adapt to continue to add value

Mike Sales
Head of Real Assets and Real Estate, Nuveen

With high valuations leading to heightened competition for deals, which sectors in real estate investment are proving to be the most attractive?
We remain committed to the needs of our clients, occupiers, and consumers, with an investment focus on dynamic, sustainable cities that appeal from a demographic, infrastructure, and technology innovation perspective. In retail, this includes holding and repositioning only those assets fit for tomorrow's world and incorporating, where desired, more mixed-use elements and a greater emphasis on convenience, experience, and value. Our office strategy is embracing the growing demand for more flexible, innovative space, focusing on the wellbeing needs of the occupier, while an expansion into logistics, and principally last-mile distribution, is a structural not cyclical movement.

There are also structural tailwinds that support an expansion of commercial real estate debt, and an evolution in the residential sector, via the development of modern, purpose-built multi-family housing, and co-living and student accommodation, considering a global, more discerning demand base. Furthermore, incorporating sustainability and technology innovation upfront in investment management is imperative from an investor, occupier, developer, and corporate responsibility standpoint.

The general consensus is that we are currently at the late stage of the market cycle. What can fund managers do to achieve the highest level of value as the real estate landscape becomes increasingly complex?
Real estate pricing is historically keen, but we wouldn't go as far as to say late cycle. With any gradual normalization of global interest rates being postponed indefinitely, the once-deemed 'temporary' and 'extraordinary' monetary conditions look set to remain in place for an extended period. Against this backdrop, we are arguably 'mid' not 'late cycle' as the case for real estate investment vs. alternative asset classes is justified.

Furthermore, global real estate is multi-dimensional and as such can offer a core or value-add investor an array of risk-adjusted returns, security of income, and diversification across a spectrum of asset types, sub-sectors, and markets of varying maturity and quality. At present, core pricing for Grade-A properties in deep, liquid, sought-after markets, with a healthy supply/demand balance, should justify taking on development, repositioning, or letting risk as a route to enhance returns. Alternatively, identifying mispricing in locations or property types that can benefit from improved space optimization and enhanced ESG initiatives, or simply those sectors that are evolving or emerging from major structural changes in demand, will offer rewards to investors willing to embrace and adapt to tomorrow's world real estate needs.

What kinds of challenges does the evolving landscape of technology bring to investors in real estate?
From e-commerce to co-working, technological disruptors are permeating throughout real estate and their impact cannot be ignored. The rise of the internet and mobile devices has fundamentally changed the way consumers behave. What people want their built

environment to provide has fundamentally evolved. We are therefore closely monitoring technological trends to position our assets defensively against them while also identifying the opportunities that can be gained to create value.

For example, digital commerce is driving many changes to how consumers behave and we believe it is an opportunity for retail real estate to evolve into a more exciting and dynamic product. This means creating new experiences by blurring the lines between online and offline retail, capturing more data about how retail is used by brands and consumers, and embracing a new generation of digitally native brands.

At Xanadú, a super-prime shopping center we manage in Madrid, the asset's value proposition goes well beyond traditional retail, with an indoor ski slope, aquarium, and theme park. It also contains non-traditional retail tenants, such as Alibaba, the global retail online marketplace, which opened its first store in Europe at Xanadú in Autumn 2019.

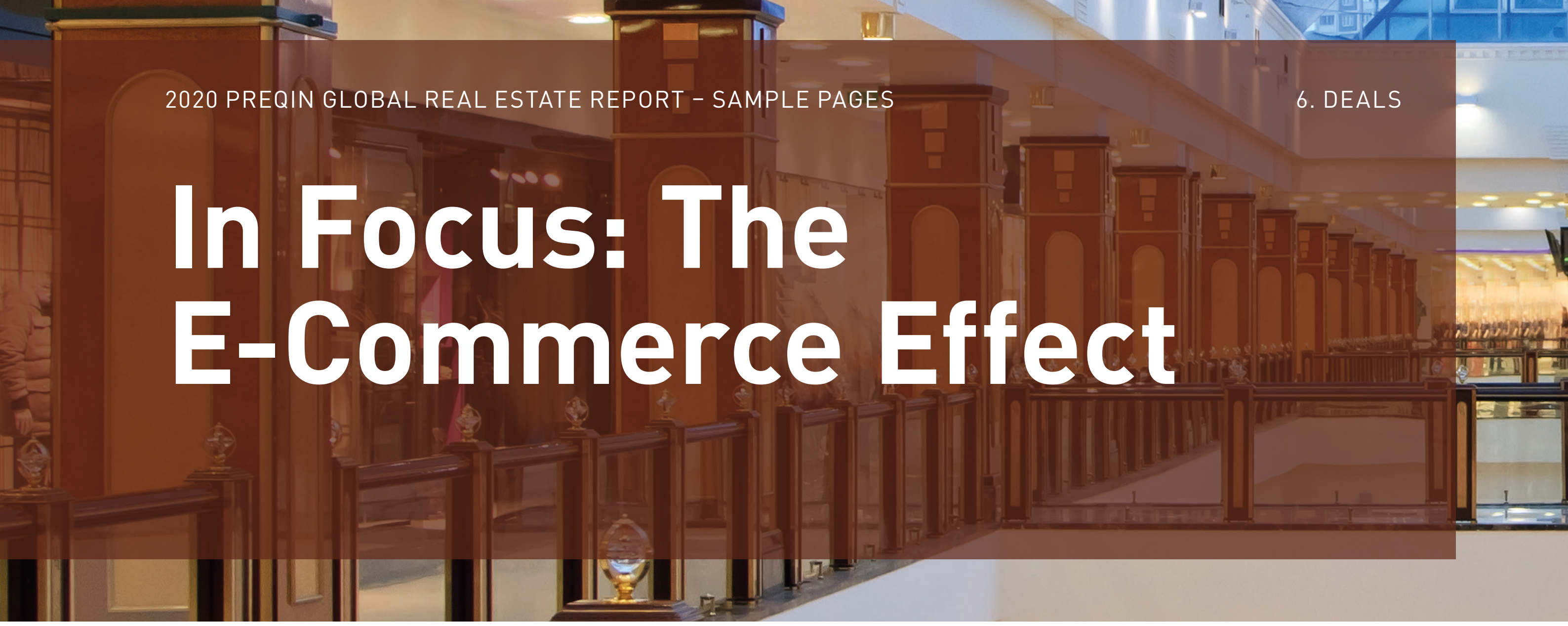
With the advent of 5G and the increasing affordability of sensors, the Internet of Things will accelerate and further increase the potential of Smart Buildings, helping them to become more operationally efficient as well as enhancing the user experience.

As well as trialing and rolling out solutions across our portfolio – from tenant engagement apps to energy efficiency technologies – we have partnered with Edge Technologies in Europe to create the "office of the future." EDGE Olympic is one of the healthiest buildings in the world – being one of the first buildings to receive WELL Platinum – is highly energy efficient, and is a Smart Building, with data from all aspects of the building's operation and user experience centralized into one digital platform.

With environmental and social governance remaining at the top of the real estate agenda, what do you believe to be the most important of these factors when considering new real estate investments?
Sustainability continues to be at the forefront for us when considering potential investments as we transition to the low-carbon economy. We strive to be leaders in responsible investing in the real estate market, not only to ensure that we are contributing toward a more sustainable future, but also because it makes business sense as in many cases investing in the most sustainable, forward-thinking, and advanced assets will have a positive return on investment for our clients too.

However, the changes our industry is now facing no longer just sit within the confines of environmental factors. We are seeing a structural shift with issues of sustainability, demographics, and technology all playing a part. All three overlap and have the potential to massively disrupt the industry, but they also present opportunities to create value. Demographic factors, for example, such as urbanization and generational shifts in consumer preferences, will change the needs of real estate in certain locations, offering savvy investors the opportunity to invest in real estate assets that will become more prevalent and necessary in those geographic areas.

Taking a strategic approach to these structural disruptors is part of our tomorrow's world philosophy, sitting at the core of our investment process and informing our long-term view of real estate investments for the enduring benefit of both clients and society.



In Focus: The E-Commerce Effect

The rise of e-commerce gives logistics real estate a boost, but plunges retail-focused real estate into an existential crisis

The world of retail is evolving. A combination of sustained growth in e-commerce, changes in consumer behavior, and rapid technological advancement has disrupted and reshaped an industry that once was dominated by the high street. The number of physical stores faces ongoing decline as consumers increasingly prefer to shop from the comfort and convenience of their own homes. In turn, private retail investment has been affected.

The aggregate value of retail PERE deals has declined since 2017. In fact, 2017 was a record year for retail, with deals amounting to an aggregate $58bn (Fig. 6.6); since then, however, the sector has observed a dramatic decline in deal-making, recording $32bn in aggregate deal value for 2019.

Fundraising in retail-focused real estate has also suffered. The number of real estate funds closing each year that are focused exclusively on retail has been declining since 2016, falling from 41 to just 14 in 2019 (Fig. 6.7). In the same period, aggregate capital raised also decreased from $6.9bn to $1.7bn. Retail has been forced to contend with the rise of e-commerce; according to TechCrunch, e-commerce sales during Thanksgiving 2019 posted a 14% rise compared with Thanksgiving 2018[1].

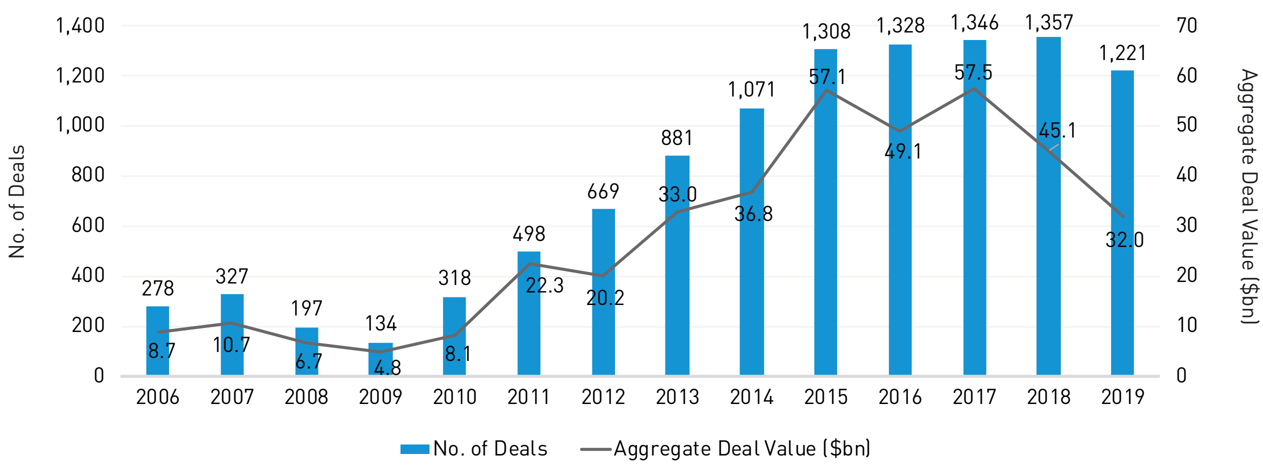
As e-commerce grows, the need for an adequate supply chain to meet demand becomes more prevalent. While PERE deals focused on retail have fallen, the number and value of logistics deals have generally increased for the past 10 years. This has been emphasized over the past four years, culminating in a record 207 deals for an aggregate $32bn in 2019, more than double the total in 2018 (Fig. 6.8).

This sharp rise in value was largely attributed to Blackstone Group's acquisition of Singapore-based GLP's US logistics portfolio for $18.7bn, making it the largest PERE deal ever recorded. Growth in e-commerce is heavily benefiting the logistics sector, as demand for fast delivery and product availability rapidly increases.

The changing shape of consumer behavior is creating new opportunities, and this is where technology will continue to play a key role. Demand for multi-purpose retail properties will grow as consumers immerse themselves in retail 'experiences,' such as the use of virtual reality in clothing stores. According to PwC, the evolution of retail in Asia is predominantly led by technology and innovation, where consumers are now able to walk into a store and pay for items via their smartphones, negating the need for a checkout.[2] What is clear is that opportunity in retail real estate exists; the challenge will be to find the value in that opportunity.

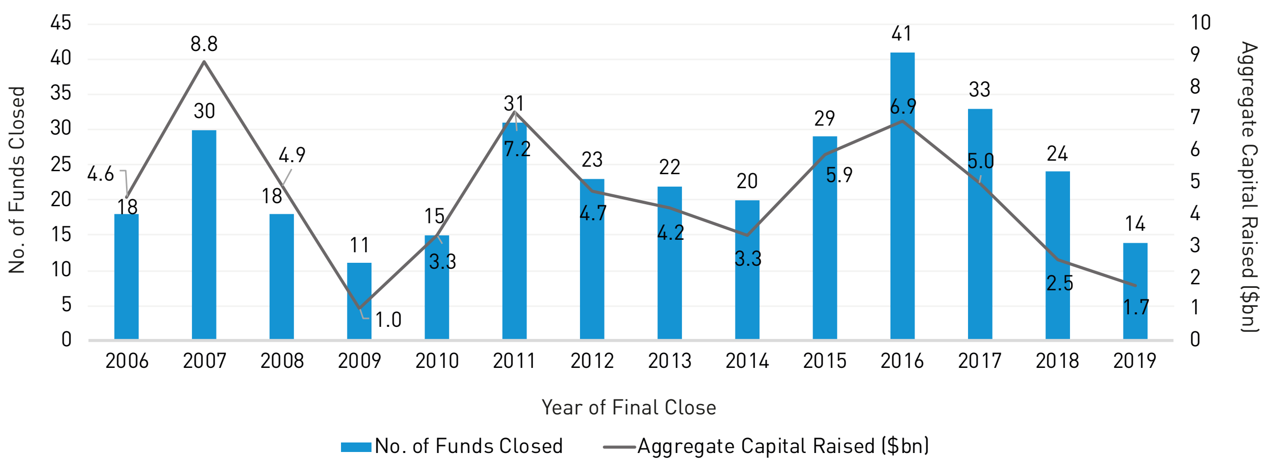
[1] *https://techcrunch.com/2019/11/28/thanksgiving-2019-online-shopping-stats/*
[2] *https://www.pwc.com/gx/en/industries/financial-services/assets/pwc-etre-global-outlook-2019.pdf*

Fig. 6.6: Global Retail PERE Deals, 2006 - 2019



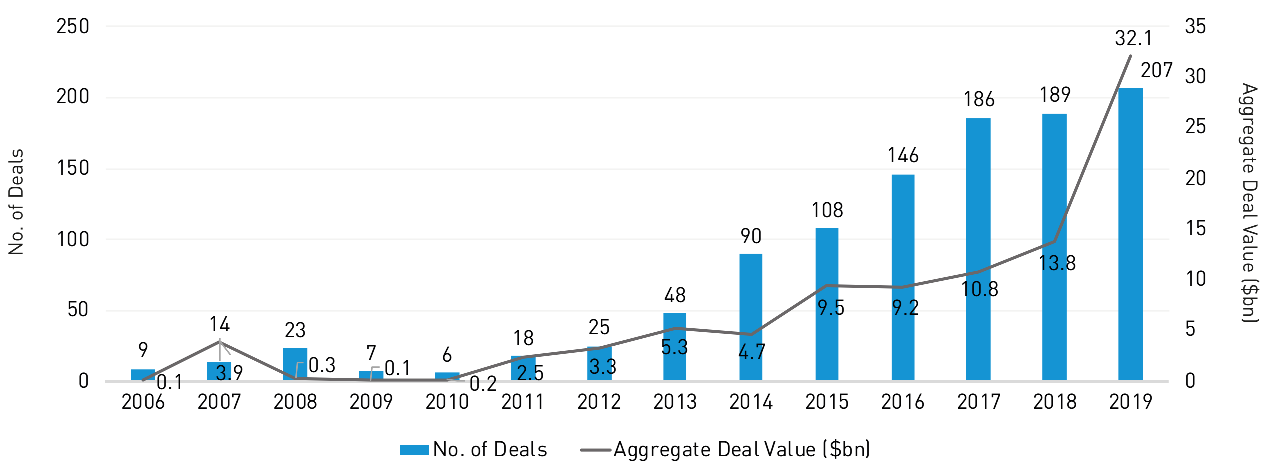
Source: Preqin Pro

Fig. 6.7: Global Retail-Focused Private Real Estate Fundraising, 2006 - 2019



Source: Preqin Pro

Fig. 6.8: Global Logistics PERE Deals, 2006 - 2019

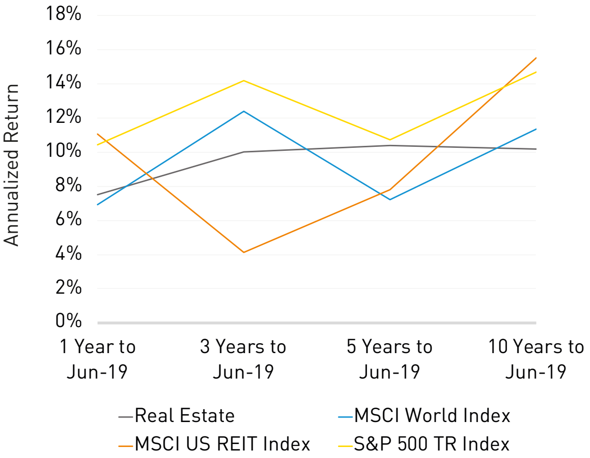


Source: Preqin Pro

Horizon IRRs

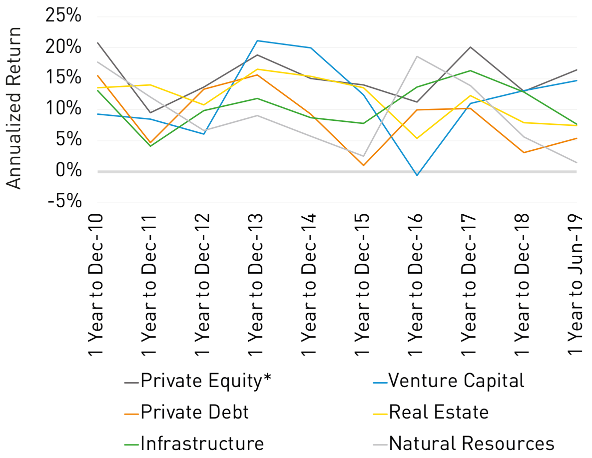
Real estate has underperformed over the one- and 10-year horizons, but outperformed over three and five years

Fig. 7.9: Horizon IRRs: Real Estate vs. Public Markets



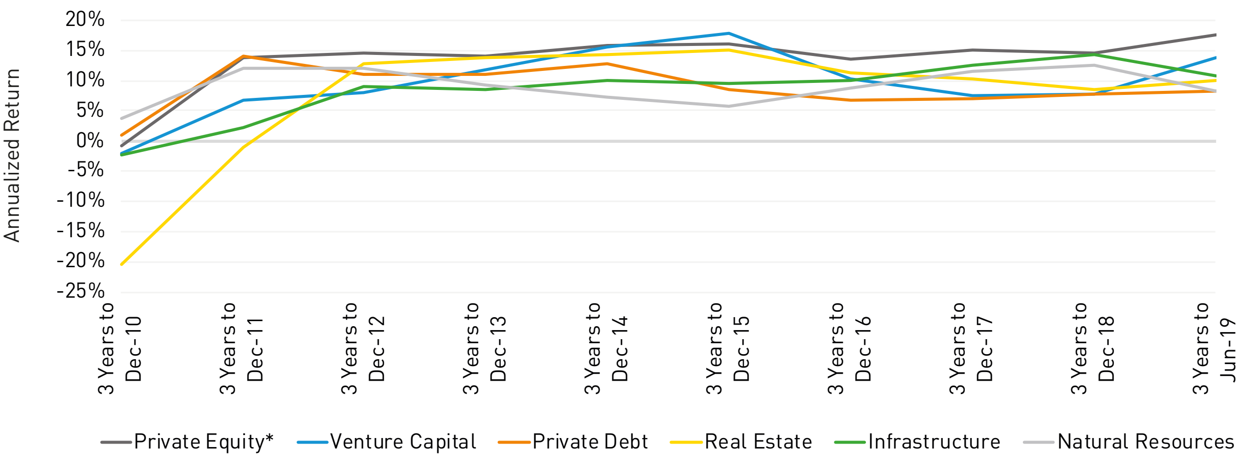
Source: Preqin Pro. Data as of Most Up-to-Date

Fig. 7.10: Private Capital: Rolling One-Year Horizon IRRs by Asset Class



Source: Preqin Pro. Data as of Most Up-to-Date

Fig. 7.11: Private Capital: Rolling Three-Year Horizon IRRs by Asset Class



Source: Preqin Pro. Data as of Most Up-to-Date

*Excludes Venture Capital.

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