



COMMONWEALTH OF PENNSYLVANIA  
PUBLIC SCHOOL EMPLOYEES' RETIREMENT SYSTEM

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Public Investment Memorandum

**Brookfield Strategic Real Estate Partners III - A L.P.**

Real Estate Commitment

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**Melissa A. Quackenbush**  
Senior Portfolio Manager

**September 28, 2018**



## **Recommendation:**

Staff, together with StepStone Real Estate, recommends to the Board a commitment of up to \$300 million to Brookfield Strategic Real Estate Partners III - A L.P. ("BSREP III", "Fund III" or the "Fund"). Brookfield Asset Management ("BAM", "Brookfield" or the "Firm"), an investment services firm headquartered in New York and Toronto, is sponsoring the Fund to make real estate investments primarily in North America, Europe, Australia, Brazil and India.

## **Firm Overview:**

Brookfield Asset Management is a publicly-listed global alternative asset manager with approximately \$285 billion in assets under management. Founded in 1899 as an infrastructure developer in Brazil, BAM has diversified into property, infrastructure, renewable energy, private equity, and sustainable resources and is now one of the world's largest owners, operators and investors in real estate.

The early 2000's marked the beginning of Brookfield's asset management business when Brookfield invited other private investors to partner with them. Since 2001, Brookfield has an established private funds platform which has raised over \$107 billion of commitments, including \$32 billion from Brookfield.

The Firm currently has approximately \$285 billion of assets under management ("AUM"), including \$160 billion of global real estate assets, managed by approximately 750 investment professionals and approximately 80,000 employees in over 100 operating locations globally.<sup>1</sup>

Brookfield's business model utilizes its global reach to identify and acquire high quality assets at favorable valuations, finance them on a long-term, low-risk basis, and then enhance the cash flows and values of these assets through the company's established operating platforms to achieve reliable attractive long-term total returns.

Brookfield is publicly listed on the NYSE, TSX and Euronext Amsterdam under the symbol BAM, BAM.A and BAMA, respectively.

## **Fund Size:**

Brookfield Strategic Real Estate Partners III - A, L.P. is expecting capital commitments of \$15 billion, including a 25% commitment from Brookfield Property Partners ("BPY"). BAM owns 52% of BPY.

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<sup>1</sup> Employee figures as of December 31, 2017. Covers investment professionals and operating professionals across all of Brookfield's business lines (e.g., private funds, listed entities, and public securities vehicles) and investment sectors (e.g., real estate, infrastructure, and private equity), including related operating businesses and portfolio companies. Investment professionals include all personnel involved in the investment and related processes, including research, investment analysis, risk analysis, performance measurement analysis, and other personnel.



## **Investment Strategy:**

In keeping with its established investment approach, BSREP III seeks to generate attractive opportunistic risk-adjusted returns by acquiring positions of control or influence in real estate companies, by making direct acquisitions and by leveraging its operating capabilities to unlock value. BSREP III will continue the successful opportunistic investment strategy the Firm has developed and implemented since 2006.

The Fund will make opportunistic real estate investments globally, primarily focused in North America, Europe, Australia, Brazil and India.

While the Fund could commit to deals above or below the specified ranges, the Fund will typically target investments ranging in size from ~\$150 million to over \$2 billion in gross asset value and investments ranging in size from \$50 million to \$800 million of equity. The BSREP investing platform will endeavor to achieve the following:

- Acquire positions of control or influence in real estate assets, portfolios and corporate entities
- Invest in North America, Europe, Australia, Brazil and India and selectively in other markets where Brookfield believes it has informational, operational, financial or other competitive advantages
- Target a range of real estate transaction with significant allocation (70%) to large scale/corporate acquisitions and the balance into direct acquisition
- Implement an operational-oriented approach, leveraging Brookfield's operating platforms to enhance transaction sourcing and execution and create value post-acquisition
- Target 20.0% gross/16% net IRR and 2.0x gross/1.7x net multiple of capital ("MoC")
- Make prudent use of leverage guided by a healthy respect for the cyclical nature of real estate markets
- Structure investments to provide downside protection

There are very few alternative asset managers who have the real estate experience, depth of expertise and scale of operating businesses to execute an investment strategy like that of BSREP III.

The following key factors clearly differentiate Brookfield from other global alternative asset managers:

- An operations-oriented approach to create value
- A global real estate investment business with investment teams located in key markets across North America, Europe, Brazil, Australia, India and Asia



- Deep deal sourcing networks
- Experienced investment and asset management teams with significant resources
- Established ability to execute large-scale and complex transactions
- Significant financial commitment by Brookfield demonstrating an alignment of interest with its private fund investors

### **Investment Team:**

The Brookfield real estate platform has over a 100-year history of investing in, owning and operating real assets. With a global presence, Brookfield’s real estate platform has ~17,000 employees under management and 250 real estate professionals with real estate offices and operating locations in North America, Europe, Brazil, Australia, China and India.

The Fund will be led by Brookfield Property Group’s Chief Executive Officer (“CEO”) Brian Kingston, Chief Operating Officer (“COO”) Bill Powell, and Chairman (“Chairman”) Ric Clark. Together, these senior investment professionals have on average approximately 30 years of real estate, finance and operating experience and on average 23 years of experience with Brookfield. Brookfield Property Group (“BPG”) is a wholly owned division of Brookfield Asset Management that is responsible for managing all of Brookfield’s real estate investments and operations including those in BPY, BSREP III’s predecessor funds, BSREP I and BSREP II, as well as Brookfield’s other private real estate funds.

The chart below outlines the members of the Investment Committee and the senior members of the Investment Team.

Name	Title / Function	Relevant Yrs. Experience	Years with Brookfield	Prior Experience
<b>EXPERIENCED INVESTMENT OVERSIGHT TEAM</b>				
Bruce Flatt <sup>1</sup>	Senior Managing Partner, CEO Brookfield Asset Management	31	32	Clarkson Gordon (now Ernst & Young)
Jeff Blidner	Vice Chairman, Brookfield Asset Management, CEO Private Funds Group	45	18	Goodman & Carr LLP
Brian Kingston <sup>1</sup>	Senior Managing Partner, CEO Brookfield Property Group	17	20	Ernst & Young
Ric Clark <sup>1</sup>	Senior Managing Partner, Chairman Brookfield Property Group	38	34	O&Y
Barry Blattman <sup>1</sup>	Vice Chairman, Brookfield Asset Management	33	16	CRIIMI Inc. / Merrill Lynch
Brian Lawson	Senior Managing Partner, CFO Brookfield Asset Management	34	29	Partners Value Investments LP / West Street Capital Corp
Bill Powell <sup>1</sup>	Senior Managing Partner, COO Brookfield Property Group	35	16	Clarion Capital / Prudential Investment Management
<b>INVESTMENT TEAM LEADERSHIP</b>				
Lowell Baron	Managing Partner, CIO Brookfield Property Group	20	13	Deutsche Bank
Dan Teper	Managing Director, U.S. Investments	20	2	Wells Fargo/Eastdil Secured
Bruce Wiles	Managing Partner, Hospitality Investments	44	4	Alcor
Michael Speer	Senior Vice President	20	16	Cadillac Fairview
Brad Hylar	Managing Director, European Investments	18	7	O’Connor Capital Partners
Jonathan Moore	Managing Director, Multifamily Investments	21	8	Value Companies. Inc.



Marcelo Vainstein	Senior Vice President, Brazil Investments	20	2	Deutsche Bank / JP Morgan
<b>REGIONAL HEADS</b>				
Zachary Vaughan	Managing Partner, Europe	15	6	Canada Pension Plan Investment Board
David Arthur	Managing Partner, Canada & Brazil	40	26	Cadillac Fairview
Roberto Perroni	Managing Partner, Brazil	30	6	Cyrela Commercial Properties
Ankur Gupta	Senior Vice President, India	11	6	Godrej Properties Ltd.
Stuart Mercier	Senior Vice President, Asia Pacific	15	6	Maxsen Capital Group
Sophie Fallman	Managing Partner, Australia	14	8	Investa Property Group
<b>PORTFOLIO MANAGEMENT</b>				
Bryan Davis	Managing Partner, CFO - BPG	21	19	Deloitte
Brett Fox	Managing Partner, General Counsel - BPG	20	16	Cahill Gordon & Reindel
Cristiano Machado	Managing Director, CFO - Real Estate Funds	23	23	N/A
Juan Jimenez	Senior Vice President, Client & Strategic Initiatives	26	5	The Praedium Group / Merrill Lynch
Jan Sucharda	Managing Partner, Office	30	13	O&Y Properties / O&Y REIT
Jay Cornforth	Managing Partner, Industrial	23	5	Prologis / AMB Property Corporation / Cabot
Ashley Lawrence	Managing Director, Retail	13	12	Wittington Properties Ltd.
Matt Smith	Managing Director, Multifamily	25	1	Related/Avalon Bay / Archstone
Shai Zelering	Managing Director, Hospitality	20	4	Blackstone LXR Luxury Hotels and Resorts

(1) Represents an Investment Committee Member

### **Investment Instruments:**

The Fund may invest through a variety of structures, including direct property acquisitions, equity positions in real estate and real estate related companies, distressed debt, recapitalizations, toe-hold positions in debt and equity securities and opportunistic loan investments.

### **Market Opportunity:**

#### North America

- Identify off-market opportunities where returns can be derived through actively managing assets and making operational improvements and not depend on continued low cap rates and interest rates to drive returns
- Capitalize on asset owners seeking liquidity of assets held since the financial crisis
- Identify public or private owners looking to exit a specific geography or sector

#### Europe

- Take advantage of opportunities that might arise from Brexit, particularly in the office REIT market and multi-family sectors
- Search for value in select markets and identify pockets of situational distress
- Position Brookfield as the preferred partner to execute large-scale and complex transactions



## Australia

- Australia continues down the path towards a more diversified economy and the current environment of positive growth, low interest rates and low volatility are expected to continue resulting in less distress than in previous cycles
- Identify opportunities where value creation can be driven through operational improvements and focus on markets that can deliver better value
- Explore opportunities in non-traditional asset classes where there is increased institutional demand

## Emerging Markets

- Opportunity to acquire prime assets in Brazil from distressed owners that are unable to wait out the long lease-up periods resulting from the challenging political and economic environment or from foreign owners seeking to exit the market. Areas of focus include Sao Paulo and Rio de Janeiro office product and industrial assets. Given Brookfield's long history of investing in Brazil, the company believes that it is well positioned to identify and make compelling investments in the Brazilian marketplace.
- Deleveraging is a top priority for Chinese policy makers and opportunities may emerge from state owned enterprises looking to divest their non-core holdings. The continued rise of the Chinese middle class will drive demand for retail and logistics while investment grade office space in Shanghai and Beijing and high quality cold storage facilities are also anticipated to yield attractive opportunities.
- Moderate inflation, a stable currency, and the passage of key structural reforms in conjunction with a progressive economic policy is creating a positive business environment for foreign institutional investors in India. Brookfield sees opportunity in the overleveraged banking sector's high level of non-performing loans as a way to acquire the underlying real estate. Office, logistics and hotel sector are key areas of focus.

## **Investment Highlights:**

- Experienced and cohesive senior management team
- Large and experienced team of investment professionals
- Proven track record
- Powerful and highly regarded platform

## **Investment Risks/Considerations:**

- Use of leverage
- Foreign country/currency risks
- Preferred co-investment rights
- Allocation policy
- Economics/compensation
- Use of affiliates



## **PSERS History & Performance:**

PSERS has made two commitments to the BSREP series of funds: \$200 million to BSREP I in 2012 and \$200 million to BSREP II in 2015. While PSERS would like a \$300 million allocation to BSREP III, only \$150 million is available at this time.

The table below summarizes PSERS' historical performance with this partnership. All data is as of December 31, 2017.

<b>Fund (\$ millions)</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>MoC</b>
BSREP II	2015	9,000.0	200.0	121.8	7.6	132.3	12.8%	1.1x
BSREP I.	2012	4,350.0	200.0	223.7	198.8	204.2	21.7%	1.8x
<b>Total</b>			<b>\$400.00</b>	<b>\$345.5</b>	<b>\$206.4</b>	<b>\$336.5</b>	<b>20.6%</b>	<b>1.6x</b>

## **Portfolio Fit:**

A commitment to the investments will be allocated to the opportunistic Real Estate portion of PSERS' Real Assets portfolio. Using the net market value from December 31, 2017 and adjusting the unfunded to include commitments from the prior and current Board meetings, the Real Estate portfolio would be 21.7% Core, 42.1% Opportunistic, and 36.2% Value-Added.

The table below summarizes PSERS' projected exposure inclusive of a recommended \$300 million commitment to the Fund as of December 31, 2017 and excludes exposure to the open-end redemptions:

<b>Investment Type (\$ millions)</b>	<b>Market Value<sup>(1)</sup></b>	<b>%</b>	<b>Unfunded</b>	<b>%</b>	<b>Total Exposure<sup>(1)</sup></b>	<b>%</b>	<b>Long Term Target (%)</b>
Core	1,677.1	28.4%	262.4	8.7%	<b>1,939.6</b>	<b>21.7%</b>	<b>20%</b>
Opportunistic	2,540.4	43.0%	1,219.7	40.4%	<b>3,460.2</b>	<b>42.1%</b>	<b>30%</b>
Value-Add	1,689.9	28.6%	1,540.4	51.0%	<b>3,230.3</b>	<b>36.2%</b>	<b>50%</b>
<b>Total</b>	<b>\$ 5,907.4</b>	<b>100%</b>	<b>\$ 3,022.6</b>	<b>100%</b>	<b>\$ 8,930.0</b>	<b>100%</b>	<b>100%</b>

<sup>(1)</sup> Includes Gross PTRES Exposure

## **Finance Committee Disclosure:**

<b>Relationship with StepStone:</b>	None
<b>Placement Agent:</b>	None in respect to PSERS' commitment. Brookfield utilizes a registered in-house broker/dealer for private fund placement services in connection with investment funds sponsored by Brookfield. Brookfield may engage third-party agents in countries where it does not have a



	fundraising presence and/or in the US with respect to high net worth investors.
<b>PA Political Contributions:</b>	<p>Pursuant to Brookfield's U.S. Political Contributions Policy (the "Policy"), Brookfield advisory entities and their supervised personnel may not make direct or indirect political contributions to restricted recipients in accordance with the prohibitions set out in Rule 206(4)-5 under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act"). Contributions to non-restricted recipients must be pre-cleared by the Compliance Department.</p> <p>As a Registered Investment Adviser, Brookfield Asset Management Private Institutional Capital Adviser US, LLC ("BAMPIC US" or the "Manager") has adopted policies to comply with Rule 206(4)-5 under the Advisers Act. BAMPIC US, the Brookfield Strategic Real Estate Partners III GP L.P. (the "General Partner"), and each Supervised Person (as defined in the Advisers Act) of BAMPIC US (as well as immediate family members residing in the same dwelling) are prohibited from making direct or indirect political contributions to certain "restricted recipients," which includes campaigns of candidates running for U.S. state or local political office, campaigns of candidates running for U.S. federal office who currently hold a U.S. state or local political office, U.S. state or local political parties, and Political Action Committees that contribute to campaigns of candidates as outlined above. In addition, BAMPIC US's policy requires that political contributions made by Supervised Persons and their immediate family members be precleared.</p>
<b>PA Presence:</b>	Brookfield-sponsored investment vehicles have invested in the following: <ul style="list-style-type: none"><li>• Retail property – Bensalem, PA</li><li>• Retail property – Lancaster, PA</li><li>• Industrial property – Carlisle, PA</li></ul>
<b>Conflicts:</b>	None Disclosed
<b>History with PSERS:</b>	Yes, this will be PSERS' third investment with Brookfield.
<b>PSERS Asset Implementation Committee Approval:</b>	September 28, 2018





**Oversight Responsibility:**

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

## Brookfield Strategic Real Estate Partners III

**September 25, 2018**

To: Board of Trustees  
Pennsylvania Public School Employees' Retirement System ("PSERS")  
5 North 5<sup>th</sup> Street  
Harrisburg, PA 17101

From: StepStone Group LP ("StepStone")

Subject: Brookfield Strategic Real Estate Partners III

StepStone believes that a commitment to BSREP III is an attractive investment opportunity for investors looking to gain exposure to opportunistic real estate investments in various global markets and property sectors including office, multifamily, industrial, hotels and retail via an established real estate firm with strong leadership, an experienced team, sector expertise and extensive platform capabilities. This document summarizes our review and evaluation of the proposed Fund.

### Opportunity Overview:

Brookfield Asset Management ("BAM") is a publicly traded global alternative asset manager with approximately US\$285 billion in assets under management ("AUM"). BAM was founded in 1899 as an infrastructure developer in Brazil and has since diversified into property, renewable power, infrastructure and private equity investments. Brookfield Asset Management offers both public and private investment products and services which leverage its experience in its target markets. With approximately US\$160 billion of real estate AUM and interests in over 400 million square feet of commercial space globally, the Firm is one of the world's largest owners, operators and investors in real estate.

Brookfield Property Partners ("BPY," "Brookfield" or the "Firm") is BAM's most significant investment platform, which is made up of sector-specific portfolios in the office, retail, multifamily, industrial and hotel sectors. Brookfield has built its property platforms through both the integration of portfolio acquisitions as well as single asset acquisitions. The Firm's approach to investing has been successful throughout several real estate market cycles.

Brookfield Strategic Real Estate Partners III ("BSREP III," "Fund III" or the "Fund") is the Firm's flagship real estate fund, seeking to continue the Firm's track record of opportunistic investments. The Firm has raised five prior opportunistic vehicles including two smaller investment focused funds, a turnaround fund and two global funds which have invested US\$16.2 billion of capital and generated a net TVM/IRR of 1.7x/24%, as of June 30, 2018. The Firm's flagship real estate opportunity funds, which began in 2012, BSREP I and BSREP II, have generated a net TVM/IRR of 2.0x/22% and 1.2x/13%, respectively. Fund III is seeking to raise US\$15.0 billion in commitments and will target a gross return of 2.0x TVM and 20% IRR. The Fund expects to provide significant co-investment opportunities given the size and scale of investments it intends to pursue.

Brookfield's 250 real estate professionals include approximately 140 portfolio management and investment employees who are supported by approximately 17,000 staff primarily located at the Firm's investments around the world. Brookfield's operational expertise and in-house property management, leasing, brokerage, development and construction capabilities will all assist in acquiring and operating assets on behalf of the Fund.

## StepStone Assessment:

### Organization

#### Merits

- ▲ **Large, Experienced Team of Real Estate Professionals:** The Fund will be led by a group of senior professionals who have long tenure in the real estate industry as well as with Brookfield. Together, the senior members of the Fund's Investment and Portfolio Management Team have on average 25 years of real estate, finance and operating experience and 13 years with Brookfield. This team of senior professionals is supported by approximately 140 investment and portfolio management professionals located across North America, Europe, Australia, Asia and Brazil. This team has invested throughout multiple investment cycles and possesses a complementary set of strategic, investing, operating, financial and transactional skills and has demonstrated the ability to manage risk at all stages of the investment process.
- ▲ **Dedicated and Sector-Focused Affiliated Operating Teams:** Brookfield has specialized integrated platforms that can enhance operational efficiencies and provide on-the-ground information to improve underwriting and asset managing across many property types. Each affiliated operating partner has its own niche, which include office, industrial, retail, multifamily and hotel. These affiliates add approximately 17,000 operating professionals across the globe.

#### Risks

- ▼ **Potential Conflicts of Interest:** Brookfield is a vertically integrated real estate platform and does not typically invest alongside non-affiliated third-party operating partners. This presents the possibility for conflicts of interest to arise as Brookfield is not obligated to use outside operating partners who can provide the same or better oversight for a lower cost and fees paid to affiliates will feed back into BAM, the Fund's publicly traded parent company.

#### Mitigants:

1. **Fees will be Paid at Market Rates or at Cost:** The Firm's affiliates may receive fees (a) at rates customarily charged for similar services by persons engaged in the same or substantially similar activities, or at cost, or (b) at any other rates with consent from the LP Advisory Committee.
2. **Limited use of Affiliates in the Opportunistic Fund Series:** Brookfield only used affiliates in 33% of the transactions in Fund I and 40% in Fund II, by invested equity, as of June 30, 2018. Furthermore, total fees for affiliates used in Fund I and Fund II totaled only 2.6% and 1.5%, respectively, of invested equity for those investments.

- ▼ **Multiple Fund Series and Investment Vehicles:** In addition to the BSREP fund series, Brookfield oversees a multifamily-only value add fund series, a mezzanine credit fund series and a core plus fund. The Firm recently closed its multi-family only fund with US\$1 billion in commitments, closed its debt fund with US\$2.5 billion in commitments and seeking US\$2 billion in commitments for its core plus fund. Brookfield can also acquire properties for Brookfield Property Partners, a publicly-traded subsidiary that invests in, owns and operates real estate, as well as purchase properties for its own balance sheet.

**Mitigants:**

1. **Allocation Policy:** While the Firm has various vehicles of real estate capital, the BSREP opportunity funds will have priority on all real estate higher-returning opportunistic investments across the Firm. Brookfield doesn't have defined parameters defining an opportunistic investment but the Firm has a Conflicts Committee which oversees any conflicts or potential conflicts in allocating investments.
- ▼ **Distribution of Fund Economics:** BSREP III will not employ a traditional carried interest program; however, the Fund will award performance based compensation, annually. Investment professionals at the Vice President-level and above will be allocated economics that are tied to the performance of the Fund. These awards will follow a five-year vesting period. This mixed carried interest program which includes incentives based on fund performance and options on Brookfield's stock is consistent across the Firm's verticals and keeps mid-level investment professionals motivated by the performance of the Fund versus the performance of BPY's publicly-traded share price. While the majority of carried interest will be awarded to investment professionals focused on the Fund, senior investment professionals, including Investment Committee members, will receive compensation in the form of options and stock grants.

## Strategy

### Merits

- ▲ **Strong Sourcing Capabilities:** Brookfield has established a large network of relationships through which it generates deal flow. In addition to traditional channels such as broker run auction processes, the Firm relies heavily on its operating affiliates to generate unique and proprietary deal flow.

### Risks

- ▼ **Brookfield's Strategy Entails Exiting Large Portfolios:** One facet of Fund III's acquisition strategy will be to build portfolios of assets, through individual purchases, and subsequently exit those portfolios to strategic buyers. Assembling a portfolio of individual assets demands a significant amount of time and may result in concentrated sector risk. Additionally, asset gathering may also lead to potential conflict from fee generation based on gross assets. However, BPY has experience in exiting these type of investments.

**Mitigant:**

1. **Alternatives to Public Exits:** Large institutions may also be interested in purchasing large, specialized portfolios together with management teams in place. A recent example of this is CIC's €12.3 billion bid to preempt Logisor's IPO. Large institutions, such as sovereign wealth funds, are continuing to look to large portfolio purchases to offer greater yield. The continued interest by sovereign wealth funds could provide BSREP III with another active avenue to exit its investments.

- ▼ **Highly Competitive Environment for Larger Funds:** Brookfield will compete against a small universe of large real estate-focused funds (US\$1.0+ billion) that are charged with mandates similar to BSREP III. Fund III's competitors include Blackstone, Carlyle, Lone Star, Starwood and Morgan Stanley.

**Mitigant:**

1. **Active Proprietary Pipeline:** Brookfield has cultivated an active pipeline, which includes a collection of potential deals sourced through proprietary sources and auctions. The pipeline shared with StepStone includes 10 opportunities, representing more than US\$5.3 billion of equity, which covers a broad mix of Brookfield's core geographies and real estate sectors.

## Performance

### Merits

- ▲ **Consistent First Quartile Performance of Opportunistic Fund Series:** Brookfield's five previous opportunistic-focused funds have generated first quartile returns relative to Burgiss' Private iQ benchmark of opportunistic real estate funds on a net TVM and IRR basis, as of June 30, 2018. The Firm's opportunistic fund series, which represents US\$16.2 billion in capital, has returned 94% of invested capital and generated a cumulative net TVM/IRR of 1.7x/24%, as of June 30, 2018.
- ▶ **Shorter Large-Scale Opportunistic Track Record:** Since 2006, Brookfield has raised US\$19.4 billion in commitments and invested US\$16.2 billion in equity across five predecessor global, large-scale, diversified opportunistic vehicles in its flagship fund series. These funds have generated a net TVM/IRR of 1.7x/24% and have returned 94% of invested capital as of June 30, 2018. While initial performance for the fund series has been positive, StepStone recognizes that Brookfield's track record of investing and managing third-party capital in large-scale, diversified opportunistic funds is shorter than that of other firms.
- ▶ **BSREP II Initial Performance:** As of June 30, 2018, the Firm's second Strategic Real Estate Partners fund, BSREP II, has invested or committed to invest 93% of its US\$9.0 billion of committed equity in 27 investments. The fund has generated a net TVM/IRR of 1.2x/13%, placing it in the first quartile. As of June 30, 2018, US\$354 million has been distributed from the fund to its limited partners.

### Risks

- ▼ **Substantial Unrealized Value in Recent Funds:** The Firm's prior Strategic Real Estate Partners funds consist of meaningful amounts of unrealized capital. 47% of BSREP I's total value is realized as of June 30, 2018, representing US\$5.0 billion of gross realizations from US\$5.1 billion of invested capital. Similarly, 6% of BSREP II's total value is realized, having generated US\$486 million in realizations from US\$6.7 billion of invested capital.

**Mitigant:**

1. **Near-Term Recapitalization and Realizations:** Fund I continues to realize investments including five assets under contract in the Suburban office portfolio as well as additional dispositions at IDI. Furthermore, subsequent to the end of the second quarter, Brookfield sold a portfolio of self-storage assets out of the Simply portfolio for a gross sale price of US\$1.3 billion.

## Structure

### Merits

- ▲ **Management Fee Discounts:** The Fund will include fee discounts for the life of the Fund based on commitment size and timing. For commitments between US\$200-299 million, the management fee will be reduced to 1.3%, to 1.25% for commitments between US\$300-499 million and to 1.2% for commitments larger than US\$500 million. For investors participating in the first close, the management fee will be further reduced to 1.175%, 0.95% and 0.9% based on the same size breaks, respectively.

### Risks

- ▼ **On- Going Litigation in Brazil:** A Brazil state prosecutor has filed a lawsuit against BPY based on accusations from a former employee who was fired in 2010 that bribes were paid to authorities in order to obtain permits for a mall expansion in São Paulo. Recent developments have provided some incremental wins in favor of BPY; however, no substantial progress towards a final decision has been made. Subsequent to the filing of charges BPY has participated in numerous transactions in Brazil including the purchase of a significant stake in Vale S.A., one of the largest logistics operators in Brazil.

#### Mitigants:

1. **SEC Declined to Take Action:** In June 2015, the SEC concluded their investigation into the accusation and concluded that they would not bring any charges to the Firm.
2. **Enhanced Code of Conduct and Training Program:** BPY, without admitting culpability, has instituted an enhanced code of conduct and training program for its employees and partners in connection with bribery and improper payments. In addition, BPY prohibits facilitation payments and requires enhanced due diligence and representations and warranties from counterparties with respect to improper payments. BAM was fully accessible, transparent and cooperative in connection with this matter throughout the diligence process.

### Conclusion:

Taking into account the merits and risks, we believe that the Fund offers a potentially attractive risk-adjusted return and is suitable for PSERS. StepStone recommends that PSERS commit up to US\$300 million to the Fund.



Partner,  
StepStone Group Real Estate, LP