



State of Rhode Island
Office of the General Treasurer

IPI Partners III L.P. - Staff Recommendation

August-2023

RECOMMENDATION:

- [Rhode Island Employees Retirement Systems Pooled Trust](#): **Approve a commitment of up to \$15 million to IPI Partners III L.P. (“IPI III”).** ERSRI previously committed \$30 million to IPI Partners III L.P. (“IPI II”), a 2020 vintage fund (exposure in *Appendix 1*, performance in *Appendix 2*).
- [Rhode Island OPEB System Trust](#): **Approve a commitment of up to \$450,000 to IPI Partners III L.P. (“IPI III”).**

ASSET CLASS: Non-Core Real Estate (ERSRI), Private Growth – Non-Core Real Estate (OPEB)

SUB-STRATEGY: Value-Add Data Center

ALLOCATION:

- [Rhode Island Employees Retirement Systems Pooled Trust](#): The target allocation for Non-Core Real Estate is 2.5% and the allocation as of 7/31/2023 is 2.2%. The preliminary pacing plan for the 2023 vintage is \$70 million committed to 3-4 funds at \$15-20 million per fund. Pending approval of this recommendation, ERSRI’s 2023 vintage commitments will be \$55 million.
- [Rhode Island OPEB System Trust](#): The target allocation for Private Growth is 5.0% and the Non-Core Real Estate sub-strategy is targeted to represent ~20% of the asset class (i.e. 1.0% at the OPEB Trust level). The actual allocation to Private Growth – Non-Core Real Estate as of 7/31/2023 is 0.05%. The preliminary pacing plan for the 2023 vintage is \$2 million committed to 3-4 funds at \$0.45-0.60 million per fund. Pending approval of this recommendation, OPEB’s 2023 commitments will be \$1.65 million.

PORTFOLIO FIT:

- [Rhode Island Employees Retirement Systems Pooled Trust](#): The ERSRI Non-Core Real Estate portfolio contains a mix of sector focused and diversified funds that bring operational expertise to value-add and opportunistic asset types (see *Appendix 3*). ERSRI allocates to sector focused funds that demonstrate specialized expertise and differentiated execution. IPI III will target the data center property type (mostly large, cloud hyper-scale data centers) and connectivity-related real assets, with a value-add/opportunistic risk-return profile, on a global basis. IPI saw increasing demand from cloud service providers (“CSP”) which increasingly sought capacity in Europe and Asia Pacific in IPI II and the firm expect to further expand within those regions in IPI III. This shift to international markets is driven by client demand and shows IPI’s capacity to be a solution provider for its clients. IPI has built strong relationships with its key end users – big cloud service providers who account for majority of the cloud market. ERSRI’s Real Asset (ex. Real Estate) portfolio has limited exposure to data centers which offer primarily colocation services (a colocation data center targets multiple tenants who wish to interconnect to one another within the same location) as part of broader diversified infrastructure strategies. IPI represents the only exposure to data centers within ERSRI’s Non-Core Real Estate portfolio. Pending approval of the recommendation, IPI II & III would represent ~11% of the Non-Core Real Estate Portfolio (see *Appendix 4*).
- [Rhode Island OPEB System Trust](#): The Private Growth portfolio allocates to Private Equity and Non-Core Real Estate (as described above) strategies and is ramping up to its target allocation through commitments made in tandem with ERSRI. Pending approval of the recommendation, IPI III would represent ~10% of Private Growth’s Non-Core Real Estate allocation within OPEB (see *Appendix 5*).

MERITS:

- **Stability & Predictability:** IPI targets investment grade tenants and rental income is contracted through long-term contracts (10-15-years) with annual escalators.
- **Vertical Integration:** IPI wholly owns STACK, a leading data center developer and operator. STACK provides development, sales, marketing, and property management to fund III and IPI III will benefit from STACK's research team who has real-time market knowledge. Fees paid by IPI III to STACK are at or below market rates that would otherwise be paid to a 3rd party. IPI is a joint venture between ICONIQ and Iron Point. Consistent with prior funds, ICONIQ, Iron Point and STACK will keep providing market intelligence and relationship to IPI III.
- **Sector Specialist & Strong Tenant Relationships:** IPI maintains close relationships with big cloud service providers ("CSP") who utilize IPI as a solution provider when expanding their global footprint. IPI is a preferred partner for large hyperscale data centers and offers 1) multiple solutions for capacity and timing, 2) strategic land holdings or relationship with landowners, 3) developer and operator experience from STACK and 4) deep industry experience and local presence in top markets. Big cloud service providers rely on large and reliable counterparties like IPI to navigate challenging and complex market environments (scarcity of land with power and fiber, complexity from local regulations, permitting, development, etc.).

CONCERNS:

- **Limited Track Record:** IPI has limited track record in realized investments. IPI I (a 2016 vintage fund) has about 50% capital distributed and IPI II is still in the investment period and it's still too early to judge performance.
 - **Mitigant – Robust Demand in Data Center:** Supply is constrained due to lack of power availability. Strong demand is driven by massive explosion of data as a result of remote work, cloud computing, gaming, content streaming and Artificial Intelligence (AI). Imbalance between supply and demand for data center drives low vacancy rate/high absorption rate and healthy increase in rental rates. As a result, IPI is confident in its underwriting and its unrealized assets have performed at or above expectations to-date. IPI II is still in the J-Curve, and it's driven by management fees and holding development projects at cost.
- **Expansion to International Markets:** On top of challenges that are faced in the U.S markets such as lack of land with power and fiber and complexity of permitting and development planning, expansion to international markets comes with additional risks and challenges such as local ESG regulations, unfamiliarity with local markets and currency risks.
 - **Mitigant –** To meet the demand from existing clients, expansion to international markets started in IPI II. IPI works with large, highly experienced local landowners and developers. With predictable revenue and cash flow after stabilization, hedging positions are reviewed at least monthly to mitigate currency risks.

ESG: IPI is categorized as ESG Leader.

- **ESG:** IPI has a formal Responsible Investment Policy and a ESG committee comprised of professionals from different functions including investment, business development and asset management. IPI is a signatory to the UN Principles for Responsible Investment (UNPRI) and the Climate Neutral Data Center Pact. IPI recognizes its special obligation to considering environmental impact given the nature of this energy intensive business. This obligation of ESG is also driven by investors' expectation and tenants' demand. IPI operates its Americas, Nordics and Italy portfolio on 100% renewable energy. IPI has established long-term net zero targets near 2030 with interim reduction goals.
- **DEI:** IPI is committed to Diversity, Equity, and Inclusion ("DEI") and it formalized its DEI Policy in 2021. IPI conducts training focusing on DEI and unconscious bias and requires that at least 50% of interview candidates from diverse backgrounds. IPI reviews the DEI Policy annually to identify areas for improvement and expansion. 56% of IPI employees are women or minorities.

FEES: Fees for IPI III are in-line with industry standards.

- **Management Fees:** IPI III charges a 1.5% management fee for commitments less than \$75 million. ERSRI & OPEB will pay a maximum of 1.20% (as a result of consultant fee discount) during the investment period and a 1.5% fee on invested capital thereafter.
- **Carried Interest:** Carried interest is 20% over an 7% hurdle with a 50% catchup to the GP. 7% hurdle is less favorable compared to 8% industry standards but is consistent with terms offered in IPI II. Carry is distributed on a total fund basis.

Appendix 1: ERSRI Prior Fund Exposure

Fund Exposure*								
Current Partnerships	Vintage	Type	Amount Committed	Amount Called	Amount Distributed	Amount Unfunded	Valuation	Exposure (Unfunded + Valuation)
IPI Partners II	2020	Non-Core	\$30,000,000	\$19,408,255	\$220,011	\$10,811,756	\$18,962,683	\$29,774,439

*Data as of 3/31/2023

Appendix 2: ERSRI Prior Fund Performance

			Net Performance*		Public Market Equivalent (PME)	
Current Partnerships	Vintage Year/Initial Investment	Type	Net IRR (%)	Net Multiple of Investment	MSCI US REIT Net PME IRR**	Fund Excess Return (Fund IRR - PME IRR)
IPI Partners II	2020	Non-Core	-1.4%	0.99	-12.0%	10.7%

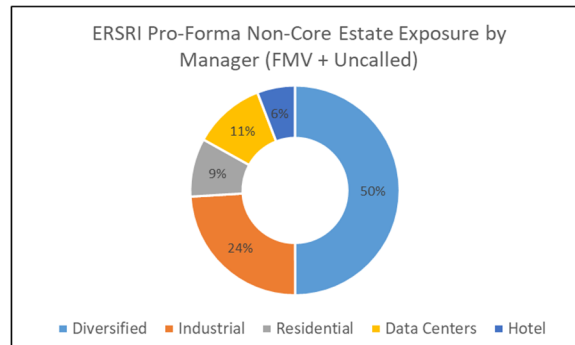
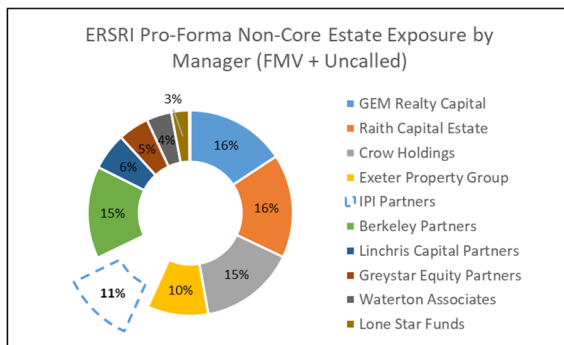
*Data as of 3/31/2023

**Long Nickels PME Methodology

Appendix 3: ERSRI Non-Core Real Estate Managers

ERSRI Non-Core Real Estate Managers		
Manager	Sub-Strategy	Sector
Crow (Diversified)	Value-Add	Diversified
GEM	Value-Add/Oppportunistic	Diversified
Raith	Opportunistic	Diversified
Lone Star	Distressed	Diversified
IC Berkeley	Value-Add	Industrial
Exeter	Value-Add	Industrial
Crow (Retail)	Value-Add	Retail - Food & Service
Waterton	Value-Add	Residential
Greystar	Value-Add	Residential
Linchris	Value-Add	Hotel
IPI	Value-Add/Oppportunistic	Data Centers

Appendix 4: ERSRI Portfolio Fit



Appendix 5: OPEB Portfolio Fit

