

ERSRI REITS INTRODUCTION

DECEMBER BOARD MATERIALS

December, 2019

Doug Moseley, Partner

Will Forde, CFA, CAIA, Consultant

Kevin Leonard, Partner



BOSTON | ATLANTA | CHARLOTTE | CHICAGO | DETROIT | LAS VEGAS | PORTLAND | SAN FRANCISCO

REITS EDUCATION

NEPC, LLC

WHAT IS A REAL ESTATE INVESTMENT TRUST “REIT”?

A REIT is a company that owns, and typically, operates income-producing real estate assets

REITs typically invest in several different real estate sectors:

- Shopping malls
- Apartment buildings
- Office buildings
- Hotels

REITs were originally created in the 1960’s to provide investors with the opportunity to invest in large, diversified income-producing real estate

The investors within a REIT earn a share of the income produced from the real estate investments without having to own/operate the individual properties

REITS derive 75% or more of its revenue from three main sources:

1. Rental income from real estate assets
2. Interest earned on investments through mortgages or mortgage backed securities
3. The sale of real estate assets



WHAT IS A REAL ESTATE INVESTMENT TRUST “REIT”? (CONT.)

The asset class has evolved since the 1960’s and has grown to a market cap of over \$1 trillion

REITs have become a popular investment in institutional portfolios

REITs use a similar valuation practice as private real estate funds

REITs will rely on cap rates, price per square foot, discounted cash flow analysis, and other metrics to value its real estate

Benchmarking REITs has become easier as different indices have come to market

The main indices used are listed below and additional information on the indices can be found in the appendix:

- Dow Jones Total Stock Market US RE Index
- FTSE NAREIT All Equity Reit Index
- FTSE NAREIT Equity Reit Total Return Index
- MSCI US REIT Index (SIC’s policy benchmark)
- Wilshire US Real Estate Investment Trust Index



REITS WITHIN THE SIC INCOME CLASS

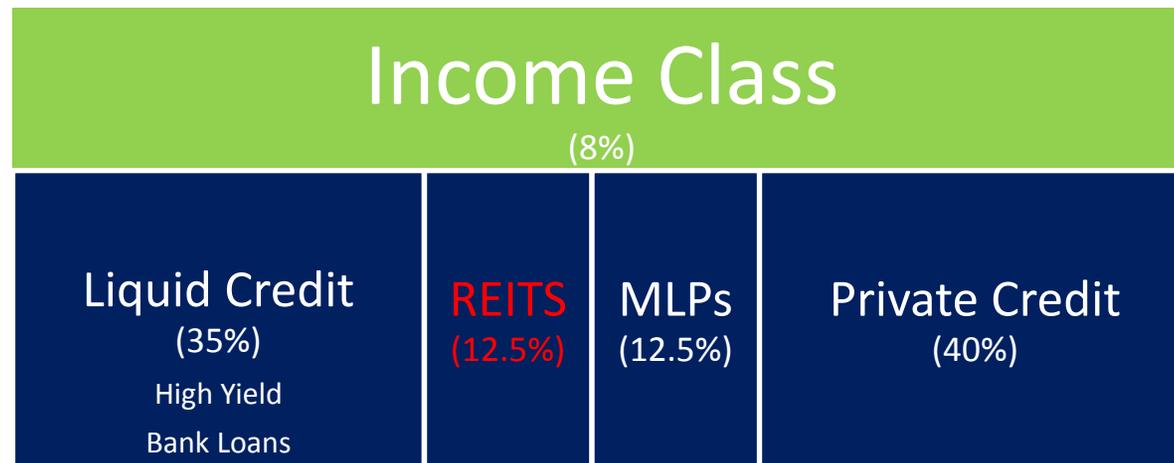
NEPC, LLC

THE ROLE OF THE **INCOME CLASS** PORTFOLIO

The Income Class portfolio is designed to provide a high and stable income stream to help offset the System's negative cashflow

As such, the Income Class consists of various yield focused investments across different asset classes and liquidity types

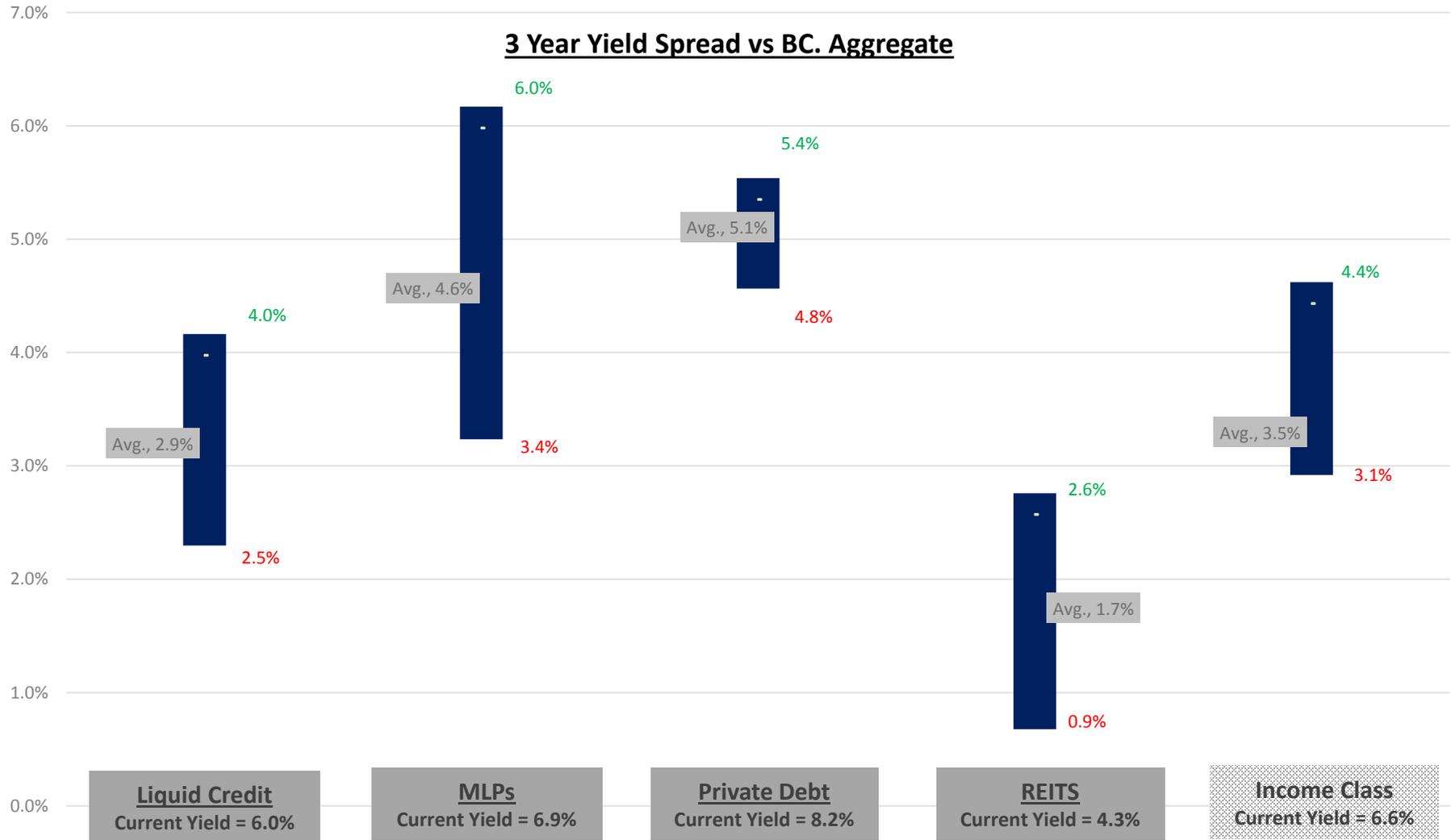
The explicit goal of the Income Class portfolio is to produce a 400 bps yield premia above the Barclay's Aggregate, over a full market cycle



REITS provide the opportunity to benefit from their yield and appreciation



3 YEAR LOOK BACK AT INCOME CLASS YIELD SPREAD COMPONENTS



*Above information is as of 9.30.18

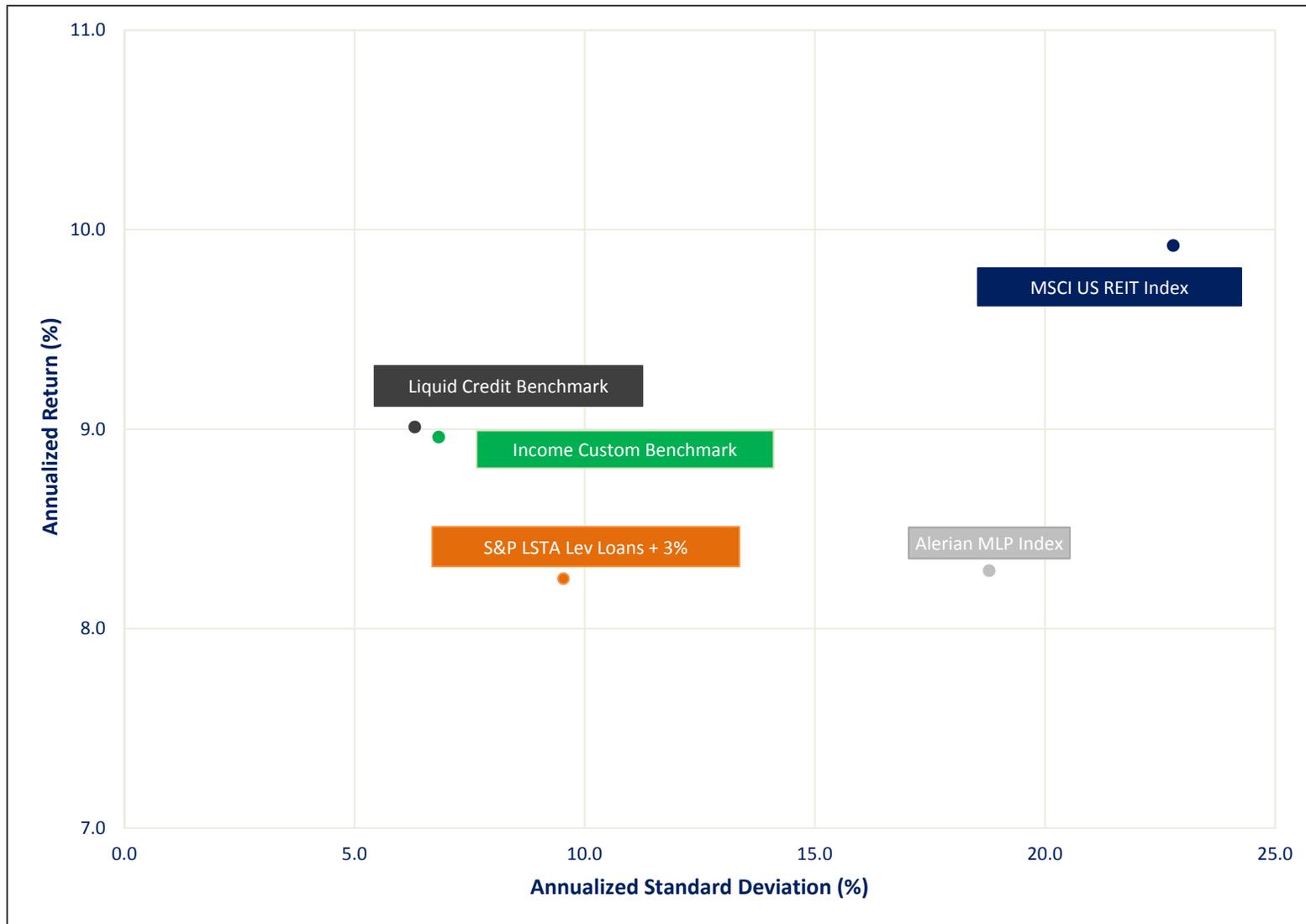
**The REIT yield is based on the MSCI US REIT index as the SIC REIT mandate has yet to be funded

***The Private Debt yield is based on its policy benchmark

**** The current yield of the BC Agg.. is 3.46% as of 9.30.18



10 YEAR RISK/RETURN CHART (AS OF 10/31/18)



10 YEAR CORRELATION

	Liquid Credit Benchmark	Alerian MLP Benchmark	Private Debt Benchmark	MSCI US REIT
Liquid Credit Benchmark	100%			
Alerian MLP Benchmark	51%	100%		
Private Debt Benchmark	17%	8%	100%	
MSCI US REIT	68%	33%	39%	100%



NEXT STEPS

NEPC will work with Staff on identifying a REIT manager to bring to the SIC in January or February

NEPC will leverage its Focused Placement List as a starting point to consider potential managers to interview

While the REIT funding is a priority, we do have flexibility to interview a REIT candidate(s) later in 2019, if necessary

NEPC will work with Staff to determine the appropriate timing of next steps considering other priorities



APPENDIX

NEPC, LLC

Index

	DWRSF Dow Jones Total Stock Market US Select Real Estate Securities Index	FNER FTSE NAREIT All Equity REITs Index	FNRETR FTSE NAREIT Equity REITs Total Return Index	RMZ MSCI US REIT Index	WILREIT Wilshire US Real Estate Investment Trust Index
Inception Description	Jun-08 Represents equity real estate investment trusts (REITs) and real estate operating companies	Mar-06 Provides investors with exposure to all investment and property sectors	Mar-06 Designed to present comprehensive family of REIT performance indexes that spans the US commercial real estate space	Dec-94 Based on MSCI USA Investable Market Index, which captures large, mid and small caps	Sep-91 Measures US publically-traded REITs; developed to offer a market-based index that is more reflective of RE held by pensions
Number of constituents	98	173	162	154	114
Top 10%	43.50%	36.78%	35.08%	35.57%	41.70%
Limitations	Excludes Mortgage REITs, net-lease REITs, brokers, hybrid REITs, and timber	Contains all tax-qualified REITs with more than 50% of total assets in qualifying real estate assets other than mortgages secured by real property that also meet the criteria	Contains all Equity REITs not designated as Timber REITs and Infrastructure REITs	Excludes most Mortgage Reits and Specialized	Excludes mortgage reits, net-lease reits, home builders, timber reits, brokers, and hybrid reits
Weighting	Free float adjusted market cap	Free float adjusted market cap	Free float adjusted market cap	Free float adjusted market cap	Free float adjusted market cap
Reviewed	Quarterly	Quarterly	Quarterly	Quarterly	Monthly after close of trading on 3rd Friday of month
Market Cap (Average)	\$6.7 billion	\$5.7 billion	\$5.0 billion	\$5.5 billion	\$6.8 billion
Market Cap (Full)	\$657.48	\$987.92	\$825.02	\$849.93	\$772.40
Dividend Yield	4.03%	4.11%	4.33%	4.32%	3.88%
Other comments	Heavier weight to large cap stocks, top 10 have highest weighting of indices. As a result, tends to have lower yield	More diverse representation of large, mid, and small caps. Tends to have a higher yield as a result	More diverse representation of large, mid, and small caps. Tends to have a higher yield as a result	Based on MSCI USA Investable Market Index, which captures large, mid and small caps	Subset of Wilshire 5000 Total Market Index.

FIRM AND PRODUCT SUMMARY

Firm/Product	Firm/Team Comments	Investment Style/Strategy	Performance Expectations	Portfolio Positioning	Other Comments	Preferred Benchmark
REITs						
Adelante Capital - TRS Composite	Originally named Rosen Financial Services, the firm went through several acquisitions until 2004 when ACM Acquisition LLC, an entity controlled by CEO Michael A. Torres purchased 100% interest from Lend Lease Corporation Limited.	Investing based on price to NAV. Concentrated portfolio so as to drive value from conviction in fundamental stock selection. Sector weights remain similar to the benchmark. Less emphasis is placed on macro analysis. Research is driven by real estate expertise.	Should stay consistently close to the benchmark with moderate yet sustainable outperformance. Good opportunity for long term investors.	25-35 holdings, diversified across sectors. Aiming for a 3-4 year hold on each name. Seeks active opportunities outside the benchmark where possible with a 15% active cap on the total portfolio. rebalancing occurs monthly.	Adelante Capital Management LLC is a minority owned boutique investment manager specializing real estate securities.	Wilshire REIT index
Barings - U.S. REIT Total Rtn	Barings Real Estate Advisers founded in 1994 as Cornerstone Real Estate Advisers to manage MassMutual's equity real estate investments. Large Global presence with resources from internal, parent and affiliate companies. Team based approach to decision making.	Opportunistic approach attempting to take advantage of distortions in warranted valuations throughout the Macroeconomic, Capital Market, and Real Estate Market Cycles.	Aiming for excess returns backed by multi-layered research platforms and careful risk policies. Should achieve this moderately and consistently.	The strategy guidelines are to hold between 35 and 45 securities in the portfolio. Barings' U.S. REIT Strategy employs policy ranges and specific restrictions in regards to security weights. Cash is not typically used as a means of risk control.	This is a good strategy for clients with low risk tolerance and long-term performance goals.	FTSE/NAREIT Equity index
Brookfield IM - Value Income	Highly skilled, very experienced team of real estate experts. Brookfield Investment Management conducts public market activities as a sub-set of Brookfield Asset Management, a global alternative asset manager focused on property, renewable power, infrastructure and private equity.	Highly concentrated with a focus on excess returns. Seeks to exploit market inefficiencies and temporary dislocations. All positions will be selected based on best ideas through fundamental analysis. Dynamic and benchmark agnostic.	Expects to drastically outperform the benchmark consistently. Considerations should be made for potential short-term risk.	20-30 positions, high conviction names across the cap spectrum and diversified across sectors. Active weights generally make up 100% of the total portfolio.	This is a bet on the ability and expertise of the two lead portfolio managers. The product's managed assets are capped at \$2 Billion therefore capacity can be limited.	MSCI US REIT index



FIRM AND PRODUCT SUMMARY

Firm/Product	Firm/Team Comments	Investment Style/Strategy	Performance Expectations	Portfolio Positioning	Other Comments	Preferred Benchmark
REITs						
CenterSquare - US REIT Strategy	Team approach with several PMs involved with input and research. Two lead PMs and CEO make the main decisions. Entrepreneurial culture with institutional support from BNY Mellon.	Diversified portfolio including REITs and REOCs. Identifies stocks seen as undervalued vs. their peers to provide high, risk-adjusted returns.	Seeks to outperform the benchmark FTSE NAREIT Equity REITs Index and should do this marginally but consistently.	Based on industry-specific analyses that evaluate stock values as well as operational and qualitative factors, CenterSquare selects approximately 40-60 stocks that they believe offer the most promising total return potential. The portfolio is diversified across sector, region and company.	Suitable for clients who do not want high tracking error but do want to beat the benchmark.	FTSE/NAREIT Equity REIT index
Heitman - Focused Composite	Heitman is 100% owned and controlled by senior officers of the firm following a redemption of OM Asset Management plc's ownership interests in 2017	Concentrated portfolio that seeks to identify security mispricings, targets greater active share, and larger position sizes	Stock selection should be the primary driver of returns, complimented by active management of allocations across sectors	The portfolio targets holding 25 positions, with positions being allowed to grow to a maximum of 10% or +/- 7.5% of the securities weight in the benchmark. Cash is held to a minimal level, generally less than 5%.	Concentrated version of the US Real Estate Securities Strategy	Wilshire US Real Estate Securities index
Heitman - Diversified A/C	Heitman is 100% owned and controlled by senior officers of the firm following a redemption of OM Asset Management plc's ownership interests in 2017	Total return approach seeking to take advantage of mispricings as a result of cyclical conditions, secular trends and/or structural catalysts	Strategy should provide excess return over benchmark attributable to bottom stock selection overlaid with macro environment and capital markets analysis	The typical number of holdings is 30-40 securities. Strategy sector limits are +/- 500 bps relative to the benchmark sector weighting.	Includes real estate operating companies, excludes mortgages, home builders, and real estate management and brokerage firms, as well as micro-cap REITs	Wilshire US Real Estate Securities index



NEPC INVESTMENT THESIS

Firm/Product	NEPC Investment Thesis
REITs	
Adelante Capital - TRS Composite	The Total Return Strategy seeks to build a concentrated portfolio of diversified U.S. real estate securities that are undervalued relative to their NAV. This is a research driven process utilizing a bottom-up fundamental approach with a preference for core, institutional property types and strong management teams. Adelante has used the same investment strategy since the inception of the firm. Adelante's offerings are based on the premise that real estate securities are the most efficient means of investing in commercial real estate.
Barings - U.S. REIT Total Rtn	An opportunistic approach with an emphasis on value investing for short-term results and seeking long-term potential growth opportunities in order to outperform traditional REIT indices. Valuations will consider all aspects of the private real estate and capital markets as well as changes in macro-economic environments on local and global levels. Outperformance will be achieved within the confines of extensive risk controls.
Brookfield IM - Value Income	Performance is driven through the knowledge and skills of the investment team, particularly lead PMs Jason Baine and Bernhard Krieg. The key differentiator in this strategy is their skill in finding under-followed, out of favor securities that drastically outperform the benchmark, and their ability to dynamically shift the portfolio in favor of both short term and long term real estate opportunities. They focus on value investing and take controlled risks to assemble their high conviction, concentrated, opinion based portfolio. A multi-asset, global and regional research model is used in their decision making, which analyses data across the real estate and capital market spectrum.
CenterSquare - US REIT Strategy	The firm seeks to achieve consistent relative outperformance using a top-down, macro-theme driven process accompanied by a consistent bottom-up framework for decision making and implementing careful risk measures. This process aims to achieve long-term, risk-adjusted outperformance on an annual basis while maximizing information ratio with reduced volatility and low tracking error.
Heitman - Focused Composite	The Heitman valued add is attributable to an informational advantage generated from the combination of fundamental insights across the firm's real estate investment management businesses: direct property ownership, public real estate securities, and real estate debt. The team based nature of decision making also provides for higher-quality decision making, as pros and cons of various opportunities are debated, decreasing the likelihood of individual bias. The Focused strategy represents a concentrated, higher conviction version of Heitman's US Real estate strategy with particular emphasis paid to security selection.
Heitman - Diversified A/C	The Heitman valued add is attributable to an informational advantage generated from the combination of fundamental insights across the firm's real estate investment management businesses: direct property ownership, public real estate securities, and real estate debt. The team based nature of decision making also provides for higher-quality decision making, as pros and cons of various opportunities are debated, decreasing the likelihood of individual bias.

