



TO: Employees' Retirement System of Rhode Island
FROM: Meketa Investment Group
DATE: April 15, 2022
RE: GEM Realty Fund VII

On behalf of the Employees' Retirement System of Rhode Island (ERSRI), Meketa Investment Group has conducted due diligence on GEM Realty Fund VII (the Fund or Fund VII) and its sponsor GEM Realty Capital (GEM). The opportunity is being considered as part of the non-core real estate portfolio. Based on ERSRI's investment strategy, the merits of the Fund and the information provided in this summary, Meketa is of the opinion that an investment in the Fund is a prudent investment for the Employees' Retirement System of Rhode Island (ERSRI). Meketa's opinion is limited to the merits of the Fund and does not constitute, nor shall it be considered as tax, legal or transaction-structuring advice. In making any investment decision with respect to this Fund, ERSRI may rely on this report but must also make its own examination and assessment of the Fund and the terms of the offering, including the merits and risks involved.

Investment Overview

GEM Realty Fund VII, LP is a value-added/opportunistic closed-end Fund targeting mid-sized real estate properties, debt, and operating companies primarily across major primary and secondary U.S. cities.

Organization

The Firm was founded in 1994 by Norm Geller, Michael Elrad, and Barry Malkin as a real estate investment company with two different lines of businesses, private and public-market real estate assets. GEM invests in real estate within the private markets through GEM Realty Properties that was formed in 1994 and in publicly traded real estate securities through GEM Realty Securities, formed in 1998. GEM has \$6.0 billion of AUM as of 1Q22. The firm has a total of 65 professionals, of which 17 are dedicated to the private Realty Properties business. All GEM employees are based in Chicago, IL.

The value-added/opportunistic fund series is GEM Realty Property's flagship vehicle. GEM raised approximately \$3.0 billion in its first six funds and has raised \$475 of its \$1.0 billion target for Fund VII. GEM also manages GEM Realty Evergreen Fund, an open-ended core fund established in 2015.

Fund Strategy

Fund VII will continue a similar strategy as executed in previous funds. GEM VII seeks to create a portfolio consisting of a mix of 20 to 30 value-added and opportunistic investments diversified by property type, and geographic location. The Fund will focus on property types such as residential, hotel, office, retail, and specialty sectors, including data centers, and may invest in distressed real estate debt and real estate operating companies. GEM will seek to acquire assets that it perceives to be undervalued due to tenant rollover risk, physical issues, mismanagement, undercapitalized ownership, and/or onerous leverage. GEM will use various value creation strategies, including redevelopment, renovation, asset management, capital injection, leasing, and property repositioning to improve underperforming real estate assets. GEM will focus on primary and secondary MSAs, particularly in the Sun Belt and Mountain regions. Priority will be given to innovation-oriented sub-markets and select suburban hubs as well as coastal gateway markets.

The Fund is targeting a 20% gross IRR (16% net) and a 1.5x to 2.5x gross multiple, utilizing up to 70% leverage. Much of the return is expected to be achieved through appreciation.

As of April 2022, Fund VII has committed \$52.5 million to two investments. The investments are consistent with the stated strategy and are summarized below:

Charlotte, NC

- \$32 million commitment
- Entitlement and construction of a 300-unit mid-rise apartment within a short walk to Charlotte's Lynx Light Rail
- Underwritten fund-level 20% IRR and 2.0x equity multiple

Santa Clara, CA

- \$20.5 million commitment
- Acquisition and reposition of two R&D properties adjacent to Santa Clara Square and in close proximity to Apple, Amazon, Applied Materials, Intel, and Nvidia. The site has existing power capacity to be converted to a data center use.
- Underwritten fund-level 20% IRR and 1.8x equity multiple

Performance

As of December 31, 2021, GEM has invested approximately \$2.6 billion across its six value-added/opportunistic funds. The first four funds are fully realized, generating net equity multiples ranging from 1.6x to 2.0x. Fund V has returned nearly 90% of invested capital and is valued at 1.3x. Fund VI completed its investment period in 2021 and is already valued at 1.3x invested equity.

ERSRI committed \$50 million to Fund V and \$20 million to Fund VI.

Terms

Fund VII is targeting \$1.0 billion of equity commitments and has a \$1.2 billion hard cap. The target equity raise is similar to the \$1.0 billion raised for Fund VI. Economic terms are consistent from Fund VI to Fund VII including a 1.35% effective annual management fee on committed capital during the investment period and a 1.50% annual fee on unreturned capital thereafter. The Fund has a 9% preferred return followed by a 50% GP catch-up until it has received 20% of profits. Thereafter, distributions will be split 80% to limited partners and 20% to GEM. The total partnership term is nine years, inclusive of a four-year commitment period, plus two one-year extensions.

Recommendation

Meketa believes that GEM has generated solid performance for ERSRI and recommends that an investment of \$25 million be considered for Fund VII as part of the non-core real estate portfolio. This recommendation adds diversification and is consistent and in context with the existing investments and the role of non-core real estate within the Private Growth section of the total fund.