INREV

Fund Termination Study
2016

Research

INREV is the European Association for Investors in Non-Listed Real Estate Vehicles. Our aim is to improve the accessibility of non-listed real estate vehicles for institutional investors by promoting greater transparency, accessibility, professionalism and standards of best practice.

As a pan European body, INREV represents an excellent platform for the sharing and dissemination of knowledge on the non-listed real estate industry.

INREV
Ito Tower, 8th floor
Gustav Mahlerplein 62
1082 MA Amsterdam, The Netherlands
+31 (0)20 235 86 00 | research@inrev.org | www.inrev.org

© Vereniging INREV
This document, including but not limited to text, content, graphics and photographs, are protected by copyrights. You agree to abide by all applicable copyright and other laws as well as any additional copyright notices or restrictions contained in this document and to notify INREV in writing promptly upon becoming aware of any unauthorised access or use of this document by any individual or entity or of any claim that this document infringes upon any copyright, trademark or other contractual, statutory or common law rights and you agree to cooperate to remedy any infringement upon any copyright, trademark or other contractual, statutory or common law rights.

Contents

Executive summary

- > Between 2016 and 2018 72 funds will terminate putting €11.0 billion into the market
- > Over half (€6.4 billion) is due to hit the market in 2017
- > Liquidation is the most popular option

Commercial products tend to have a useful life cycle and closed end non-listed real estate funds are no different. Funds get launched, they attract capital, they generate returns for investors, they mature and then ultimately they reach the end of their useful lives and they are terminated, releasing assets back into the market and returning cash to investors. This study investigates the late life and end of life phase for such funds.

As a fund's planned termination date approaches, choices present themselves. This survey analyses the choices that have been taken, the timing of those decisions and the implications of those decisions.

Between 2016 and 2018 terminating funds will release €11.0 billion into the market. Over half (€6.4 billion) is due to hit the market in 2017, coming mostly from core and value added funds. Terminations in 2018 will be dominated by value added funds.

'Terminations in 2018 will be dominated by value added funds'

As one would expect, the closer the termination date, the more likely it is that the termination decision has been made. For funds terminating in 2016, 77.8% of funds have made the decision. For funds with a termination date of 2017, two-thirds (66.7%) of funds have decided their destiny.

For the third year running liquidation has been cited as the preferred form of termination. However, there are notable differences across different fund styles. For core funds liquidation is king, while for value added funds the group of other options (IPO, sale, merger and so on) takes first place, with 33.3% of funds selecting this termination option.

The choice between extending and liquidating a fund can affect performance. This was not the case in the period from 2007 to 2009 but since then a gap in performance has appeared and it has been widening over time. Over the five-year period from 2011 to 2015 the gap in average annual returns between funds in extension and liquidating funds has increased and in 2015 it was 14.2%, with extending funds delivering 8.0% return and liquidating funds delivering -6.2%.

The main drivers affecting the decision whether to liquidate or extend are existing market circumstances followed by terms set for termination options in the fund documentation and quality of the portfolio.

'Two-thirds of funds terminating in 2017 have already made the choice between termination options'

Section 1

Introduction

Introduction

This is the eleventh INREV Fund Termination Study, the latest in a series of reports examining preferred termination options and associated issues among European closed end non-listed real estate funds. The report also looks at trends in continuation strategies, the impact of current market conditions on fund managers' decision making process, as well as other issues related to fund terminations.

First, the study provides an overview of the funds within the INREV vehicles universe ('Universe') which are due to terminate over the 2009 to 2019 period. In total, the INREV vehicles universe from Quarter 1 2016 contains 497 funds totalling €226.6 billion Net Asset Value (NAV). Of those 296 are closed end funds collectively representing total NAV of €57.7 billion. Two-thirds (67.6%) have their termination dates between 2009 and 2019 representing €32.1 billion of NAV. Over the coming two years 72 of those funds (36.0%) will terminate putting €11.0 billion into the market.

Second, and following on from last year's study, the report examines survey responses of funds that are due to terminate in the coming two years. This section explores factors impacting their termination decision making process as well as the timing of these decisions. The analysis is based on the sample of 48 funds which completed the questionnaire-based survey of which 23 are due to terminate over the coming two years.

It is important to note that the sample size and completeness of responses vary year by year. As such, historical comparison should be treated with caution. Returns figures are calculated by INREV. The performance data presented in this report is not intended to serve as a benchmark and should be used for research and information purposes only.

INREV would like to thank fund managers for their contribution towards the Fund Termination Study 2016.

Section 2

Market overview

Market overview

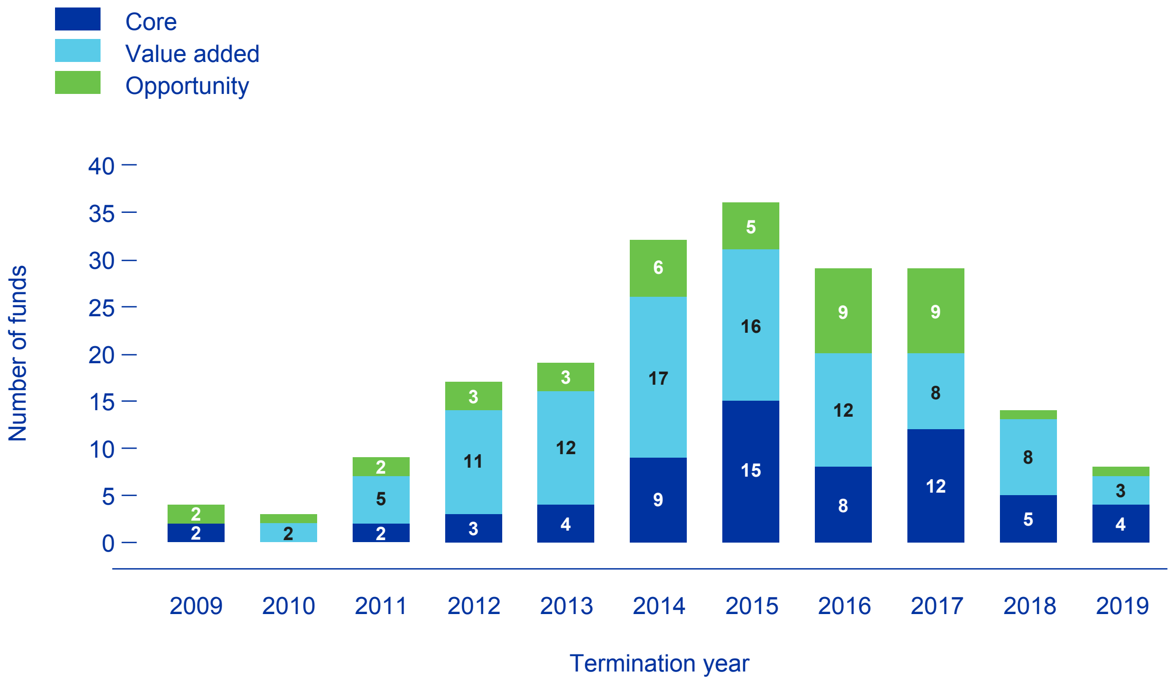
This section is based on data from INREV's vehicles universe. The universe contains key characteristics of non-listed real estate vehicles in Europe. It comprises 497 funds of which 296 are closed end vehicles collectively totalling €57.7 billion of NAV. Of those, 200 vehicles have their termination dates between 2009 and 2019 representing €32.1 billion of NAV. Over the 2016 to 2018 period 72 of those funds are due to terminate with €11.0 billion of assets entering the market.

Funds terminating between 2009 and 2019

Of the 200 closed end funds with original termination years between 2009 and 2019, the majority (47.0%) are value added vehicles, followed by those with core (32.0%) and opportunity (21.0%) strategies. In any given year the funds that terminate will be a mixture of the three styles, although of course the precise proportion of each style will vary.

With regards to the 2016 to 2019 period, 72 funds are due to terminate. This year is likely to see 29 vehicles being terminated, and in 2017 the same number (29) are scheduled to terminate. In 2018, 14 funds are scheduled for termination.

Figure 1: Number of funds terminating between 2009 and 2019 by style



'2015 was the peak year for scheduled terminations'

Funds terminating between 2016 and 2018

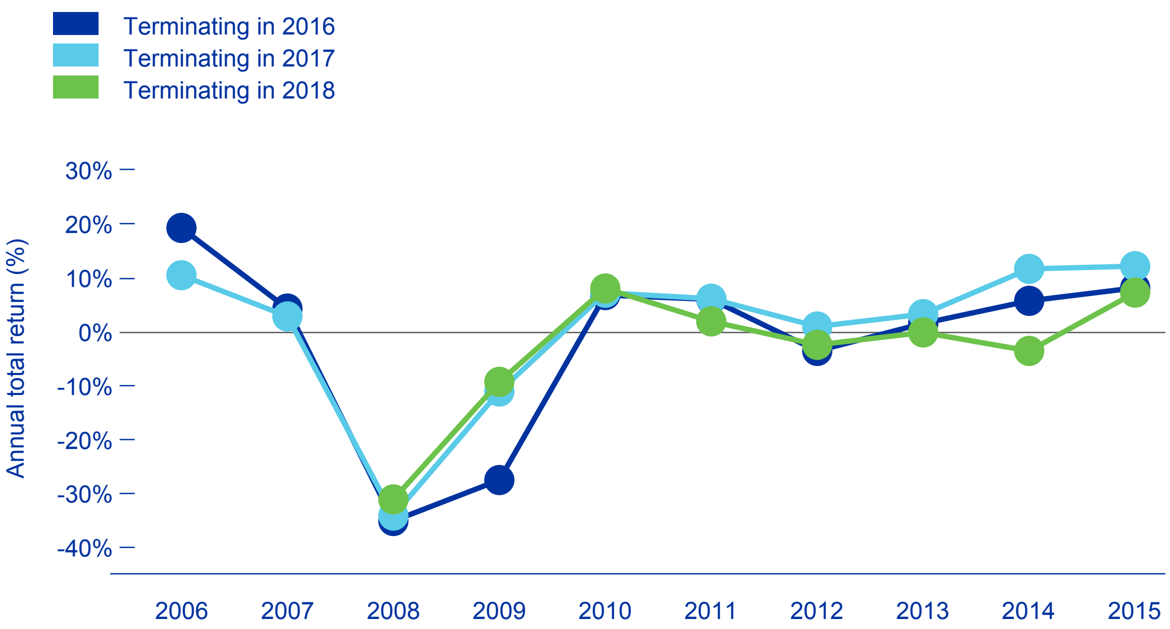
With regards to their performance, funds moved in different trajectories. On a 10-year annualised performance basis, funds that have their termination date scheduled in 2016 generated an average total return of -2.8% per annum. Over the last five years, this group of funds returned 3.7% per annum. In 2015, the return was 8.4%.

Funds which are due to terminate in 2017 delivered moderately better returns. Over the same 10-year period, this group of funds generated an average total return of 0.0% per annum. Over the last five years returns were 6.9% annually. In 2015 their return jumped to 12.4%.

Funds that have their termination date scheduled in 2018 generated lowest returns. Annualised 10-year returns stand at -4.3%. Over the last five years, their performance was 0.7% per annum. In 2015 their performance was 7.5%.

All three fund categories saw a significant drop in performance in 2007 and 2008 and an uplift thereafter. However, funds which have their termination scheduled for 2018 underperformed their peers in the period since 2010.

Figure 2: Performance by liquidation year

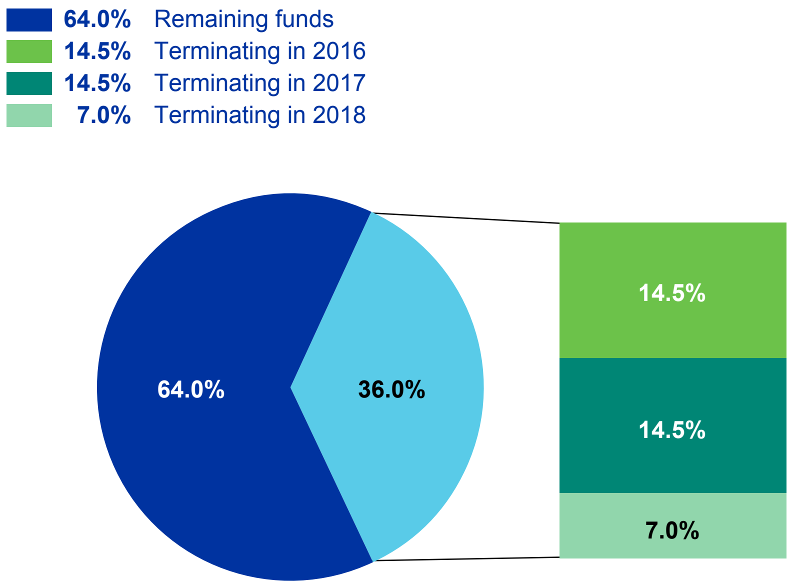


Of the total 72 funds which are due to terminate between 2016 and 2018, there are 29 funds terminating in 2016 and 2017 and 14 the year after.

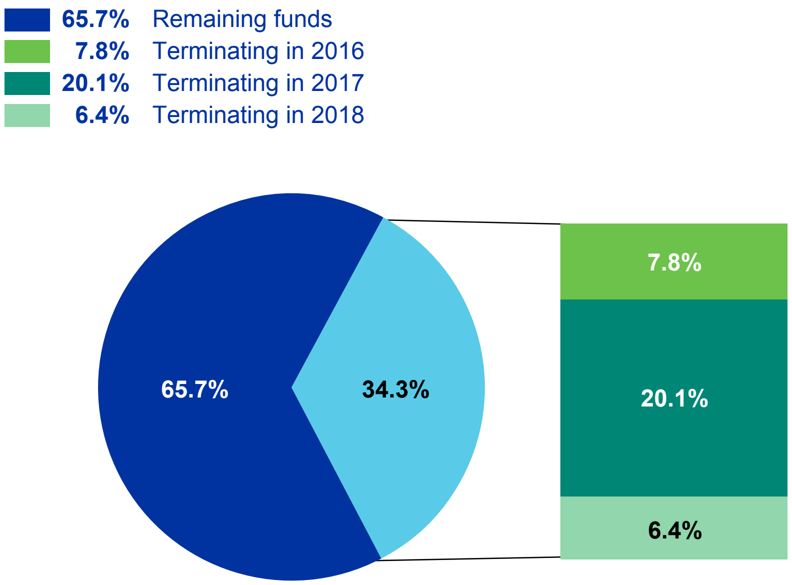
By size the NAVs are split as follows: €2.5 billion entering the market in 2016, €6.4 billion in 2017 and €2.1 billion in 2018. Funds terminating in 2017 are therefore much bigger on average than funds terminating in 2016.

Funds terminating in 2018 are bigger on average than their 2016 peers, but smaller on average than funds terminating in 2017.

Figure 3: Funds terminating between 2016 and 2018 by number of vehicles and size



By number of funds



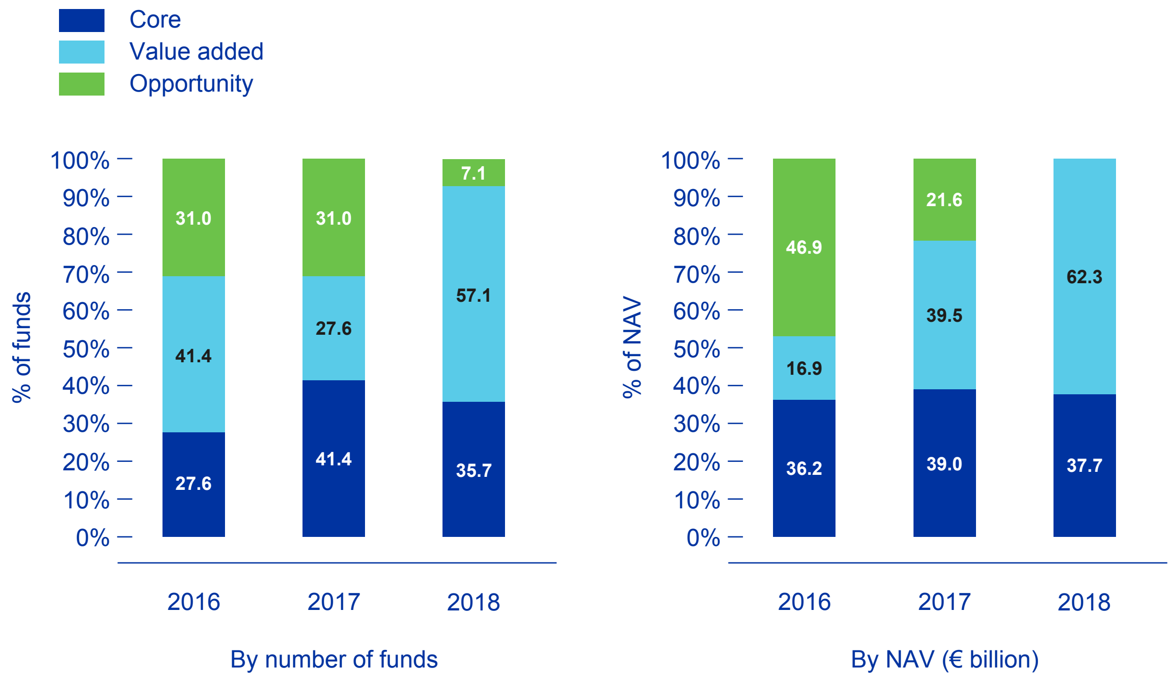
By NAV (€ billion)

Funds in termination by style

In terms of style composition, the majority of funds terminating in 2016 are value added (41.4%) followed by opportunity (31.0%) and core (27.6%) funds. In 2017, the trend reverses with more core funds (41.4%) being terminated, followed by opportunity (31.0%) and then value added vehicles (27.6%). The following year, very few opportunity funds are terminating (7.1%) with the majority of funds being value added (57.1%) followed by core (35.7%).

In terms of fund size (that is, measuring by NAV rather than number of vehicles) the picture is slightly different. Opportunity vehicles will make up the largest share of total NAV (46.9%) entering the market in 2016. In 2017, value added (39.5%) and core (39.0%) will take the spotlight. And the year after, value added funds (62.3%) will dominate.

Figure 4: Funds in termination by style



> ‘In 2017, 29 funds will terminate and 12 of these are core’

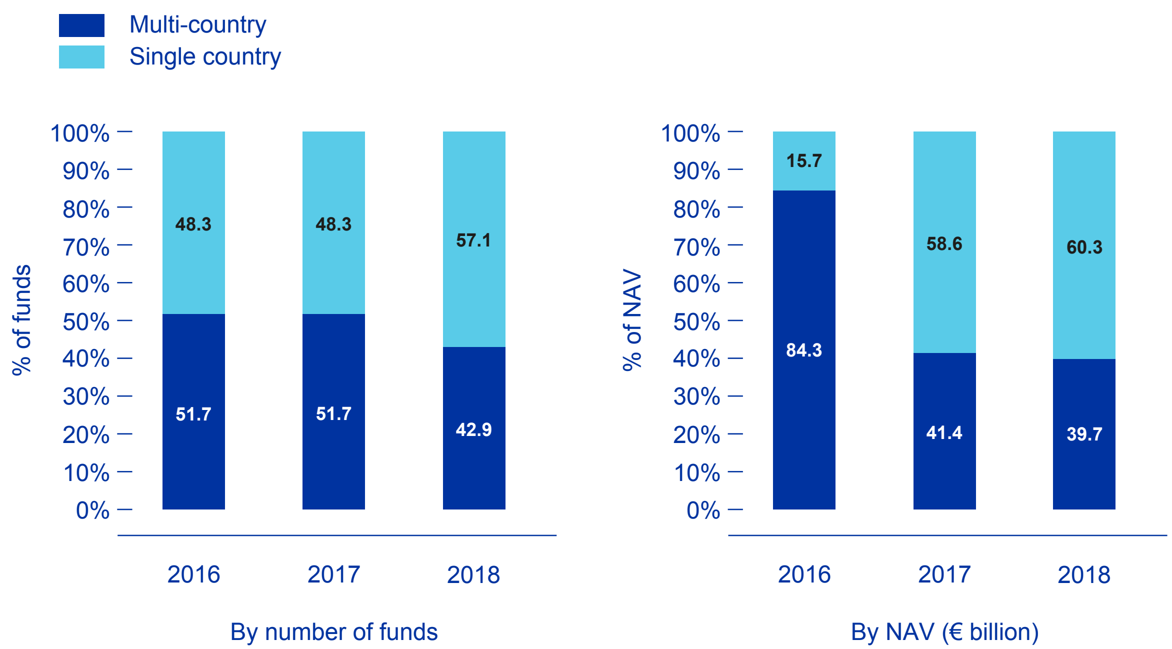
Funds in termination by country strategy

Funds in termination by country strategy are almost evenly split between multi-country and single country vehicles. In 2016 and 2017, 29 funds are scheduled to terminate in each year of which slightly more multi-country vehicles (51.7%) will terminate compared to single country funds (48.3%). In 2018, 14 terminations are scheduled with more single country funds terminating (57.1%) compared to multi-country funds (42.9%).

In terms of size, 2016 will see some large multi-country funds terminating. Of the total of €2.5 billion entering the market in 2016, 84.3% are attributed to multi-country funds and the remaining 15.7% is comprised of single country vehicles. During the following two years the ratio between multi-country and single country funds stands at around 40:60.

‘2016 will see some large multi-country funds terminating’

Figure 5: Funds in termination by country strategy

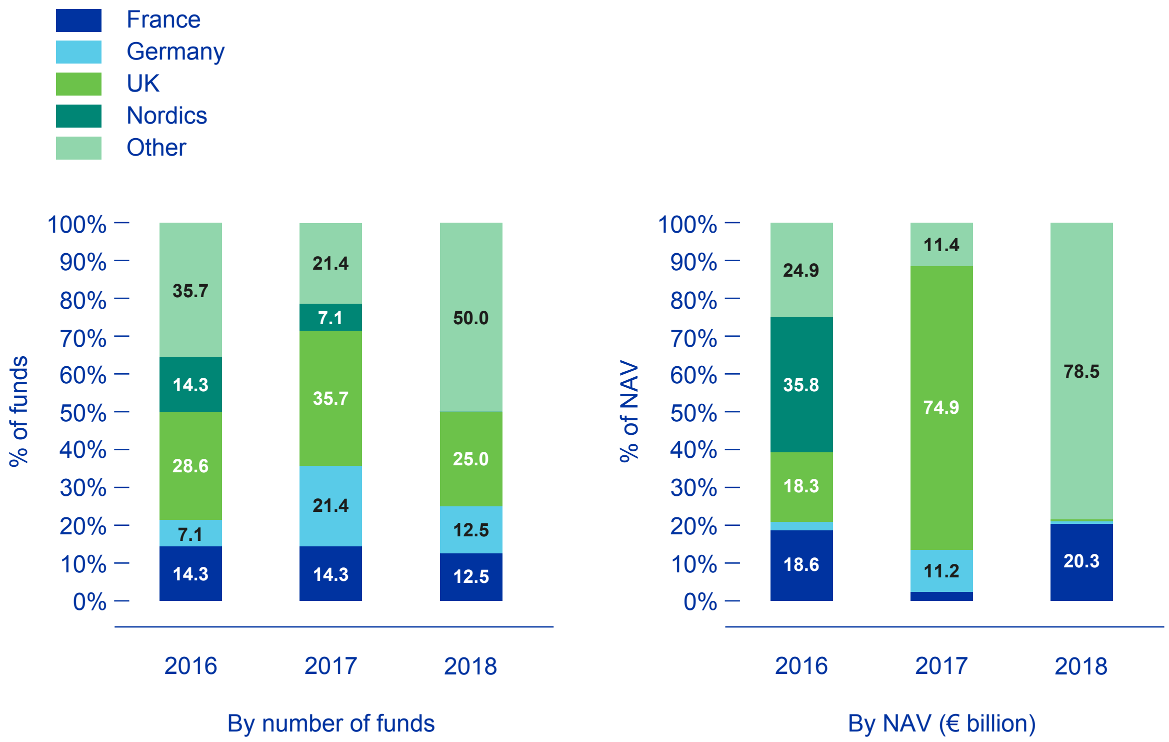


With regards to single country funds, there is a mix of funds that are due to terminate over the coming two years. In each of 2016 and 2017, 14 single country funds will terminate with 8 vehicles seeing the end of their life in 2018. Of the total number of 14 single country funds scheduled to terminate in 2016, 28.6% target the UK, 14.3% target France, the same number (14.3%) target the Nordics and 7.1% target Germany. The remaining 35.7% have assets in other European countries.

In 2017, the situation is broadly similar but with a higher concentration on the UK and Germany. The following year looks a bit more like 2016, with the UK and German allocations falling back closer to where they started.

In terms of single country funds size, there will be €0.4 billion, €3.8 billion, and €1.2 billion entering the market in 2016, 2017 and 2018 respectively. Nordic funds dominate in 2016, indicating that some large Nordic funds are scheduled for termination. In 2017 the size effect can again be seen, but this time it is UK funds that are dominating, indicating that some large UK funds are on the termination list next year.

Figure 6: Funds in termination by single country strategy

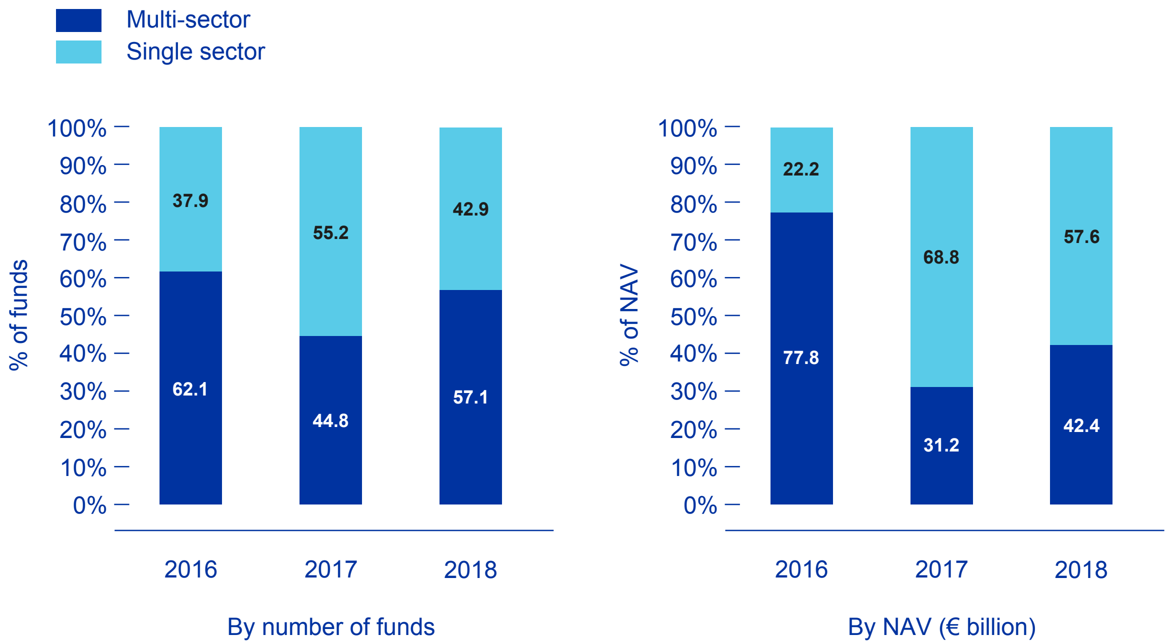


Funds in termination by sector strategy

When looking at fund terminations by sector strategy, more multi-sector funds than single sector funds are being terminated over the coming two years. Of the 29 funds terminating in 2016, 62.1% are multi-sector and 37.9% are single sector. In 2017, the same number of 29 funds have their terminations scheduled and of those 44.8% are multi-sector and 55.2% are single sector. The year after 14 funds are being terminated with the split between multi- and single sector being 57.1% and 42.9% respectively.

In terms of size, of the €2.5 billion being released to the market in 2016, multi-sector vehicles (77.8%) dominate. The trend reverses for 2017 with single sector funds representing 68.8% of the total of €6.4 billion of NAV. For 2018 the NAV of €2.1 billion is split as follows: 57.6% for single sector and 42.4% for multi-sector.

Figure 7: Funds in termination by sector strategy

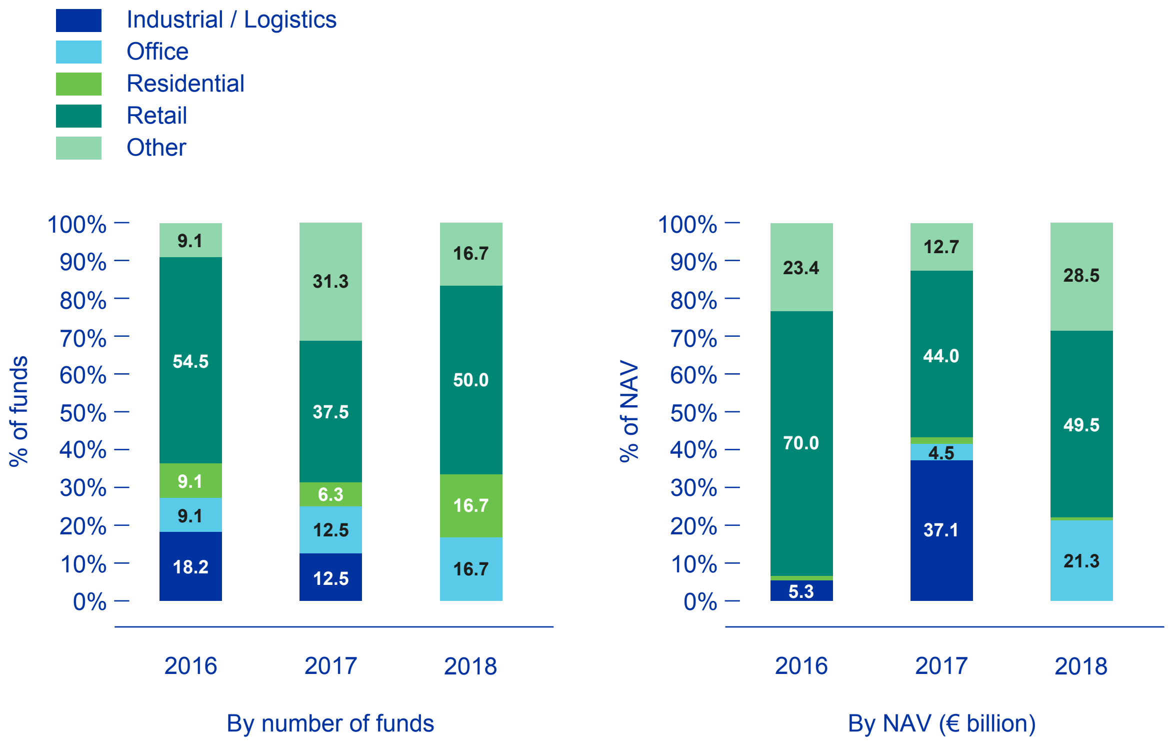


In terms of specific sector strategies, funds targeting retail make up the largest share of vehicles terminating over the coming two years. Of all 11 single sector vehicles terminating in 2016, 54.4% are retail. The remaining 45.5% is split between industrial / logistics (18.2%), with the three remaining categories of office, residential and other sectors each representing 9.1%.

In 2017, 16 single sector vehicles are scheduled to terminate and the dominance of retail is slightly reduced, accounting for 37.5% of all terminations. But in 2018 retail bounces back to make up half of all 6 single sector funds that are terminating. It is worth noting that no industrial / logistics funds are terminating in 2018.

By value, the picture is not dissimilar, in the sense that retail dominates each year, though less so in 2017 when €0.6 billion enters the market. However, an interesting pattern can be seen in 2017, where the industrial / logistics funds in termination make up 37.1% of the total of €4.4 billion. This indicates that some large funds targeting that sector are due to terminate in 2017. The next year sees the trend reverse to retail with 49.5% of €1.2 billion of single sector terminations being retail.

Figure 8: Funds in termination by single sector strategy



Section 3

Fund termination survey

Fund termination survey

This year's annual fund termination survey is based on data collected from 48 funds of which 23 are due to terminate in 2016, 2017 or 2018. The survey explores the choices considered for termination as well as a range of factors affecting the decision making process, the timing of the decisions and how specific continuation strategies are likely to affect the structure of the funds themselves.

The funds contributing to this year's survey have a range of different termination dates. Funds that were due to terminate at some point before 2016 are the largest group, making up 52.1% of the total. Funds due to terminate in 2016, in 2017 or in 2018 make up the remaining 47.9% of the survey.

The funds that participated in this survey differ in terms of their termination status. Of the 25 funds with terminations prior to 2016, 13 (52.0%) are already in liquidation. The next largest category comprises funds that are in extension, which make up 24.0% of the total. The remaining 24.0% fall into a mix of categories.

Of the 23 funds terminating over the coming two years, the majority (52.2%) are in liquidation. Around one fifth (17.4%) of vehicles had their status unspecified. The remaining third (30.4%) fall into a mix of categories, including extension, sale or other options.

Figure 9: Composition of funds by termination date

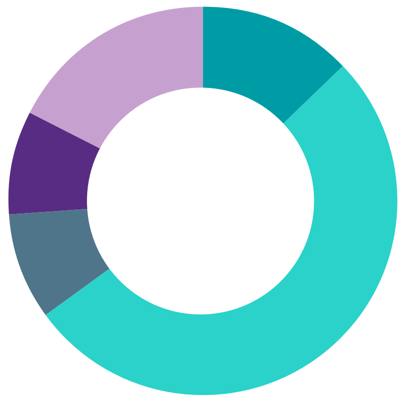
20.8% 2016
25.0% 2017
2.1% 2018
52.1% Pre-2016

Figure 10: Composition of funds by status

24.0% In extension
8.0% Liquidated
52.0% In liquidation
8.0% Other
8.0% Sale of the fund

Funds terminating prior to 2016

13.0% In extension
52.2% In liquidation
8.7% Other
8.7% Sale of the fund
17.4% Unspecified



Funds terminating in 2016 - 2018

Performance by liquidation status

Liquidation status can at times have a connection to performance. This was not the case in the period from 2007 to 2009 but since then a gap has appeared and it has been widening over time. Over the five-year period from 2011 to 2015 the gap in average annual returns between funds in extension and liquidating funds has increased and in 2015 it was 14.2%, with extending funds delivering 8.0% return and liquidating funds delivering -6.2%.

Timing of decision making

The responses show that the majority of fund managers have made a decision as to the termination strategy they will follow for those funds that are scheduled for termination this year or next.

As one would expect, the closer the termination date, the more likely it is that the termination decision has been made. For 10 funds terminating in 2016, 77.8% of funds have made the decision (one fund did not specify whether decision has been made).

For 12 funds with a termination date of 2017, two-thirds of funds have decided their destiny. Funds do not wait until the last minute to make termination decisions, although there is some variability evident from year to year.

Figure 11: Performance by liquidation status

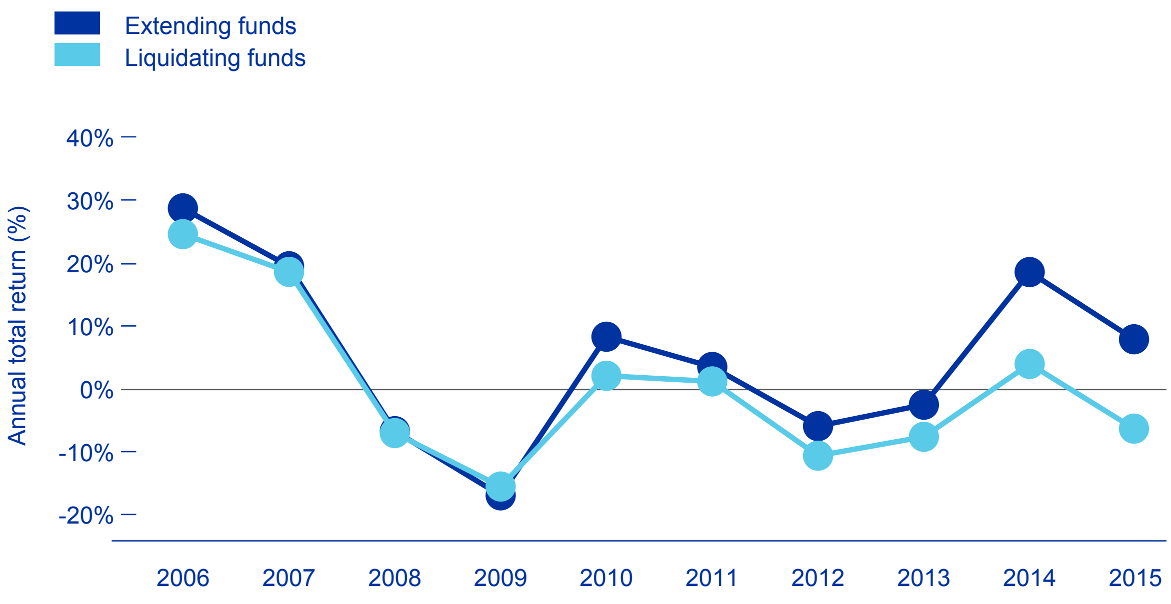
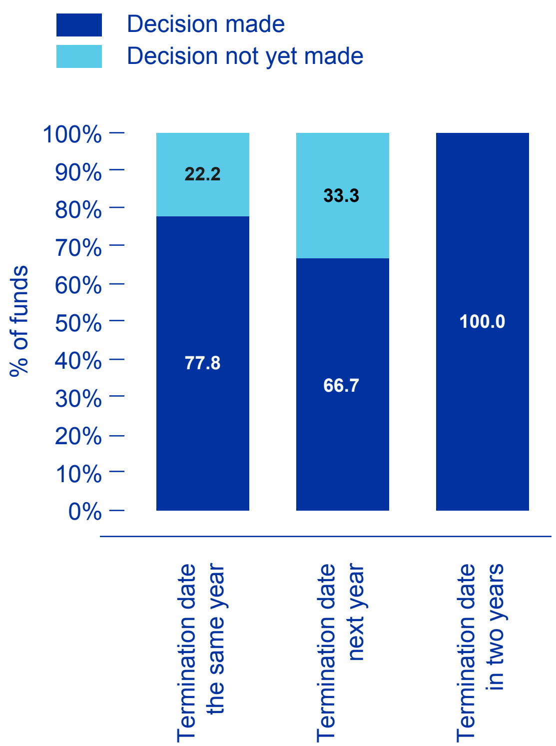


Figure 12: Timing of decision making



Looking back at decision-making trends over time, it seems 2015 was the year of being decisive. In that year 82.4% of respondents had decided what was to become of their funds that had termination dates in 2015, and 80.0% of respondents had made a decision for funds due to terminate the year after.

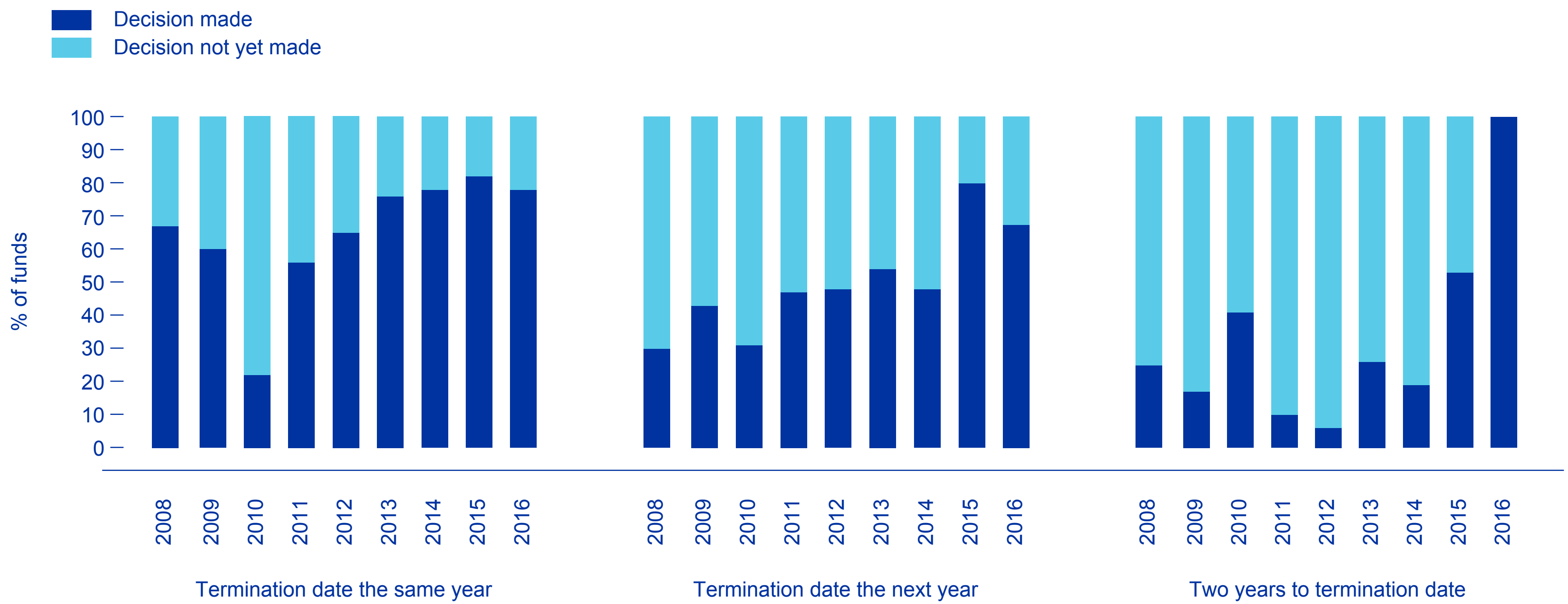
In the 2016 survey the level of decisiveness has slipped a little, and this applies to both funds expiring within the year of the survey (moving from 82.4% to 77.8%) and funds expiring the following year (moving from 80.0% to 66.7%).

For funds expiring within the year, this slippage reverses a trend that has been evident since 2011. For funds that were due to terminate the year after the survey, the pattern of decisiveness is slightly less clear since 2011, given that there was a dip in decisiveness in 2014.

In this year's survey we do not comment on funds with termination dates that are two years in the future, because the sample size is too small.

> 'A termination strategy has been decided for over three quarters of funds due to terminate in 2017'

Figure 13: Timing of decision making over the period 2008 to 2016



Termination options under consideration prior to making a decision

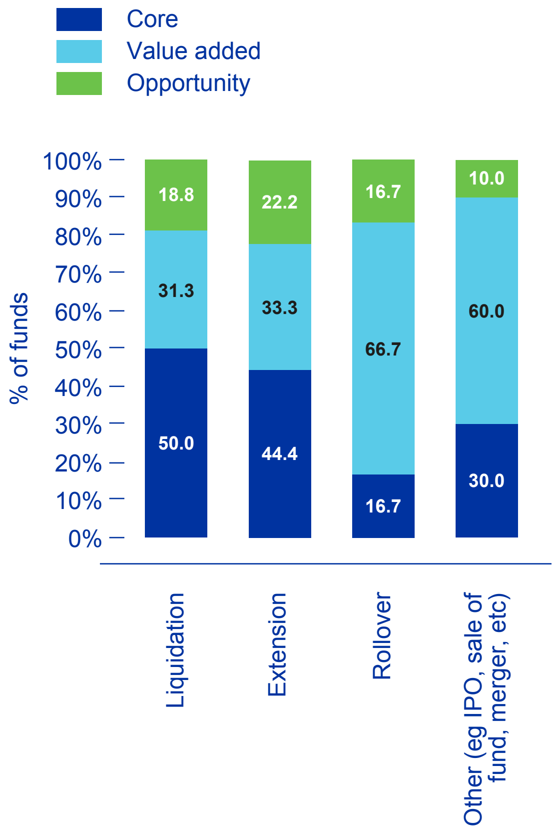
For the 23 funds which are due to terminate, the managers were asked to select the termination strategies under consideration for their funds. In this instance they were able to select more than one option under consideration.

There are notable differences across termination options and fund styles. Where liquidation was mentioned (16 funds), half of those were core. Where extension was chosen (nine funds), the majority was also core (44.4%) following value added (33.3%) and opportunity (22.2%) vehicles.

Rollover (six funds) was predominantly chose by value added vehicles (66.7%). Out of 10 funds which opted for other options (IPO, sale, merger and so on) the majority (60.0%) were also value added vehicles.

There are some noteworthy changes since last year's survey. All four options continue to be seen as viable for all three styles, but the emphasis has changed in some ways. Value added funds were more interested in extensions in last year's survey, ranking it ahead of terminations. The same is true for opportunity funds, where extensions were also more popular than terminations. However, the overall picture across all styles has not changed dramatically since last year.

Figure 14: Termination options under consideration



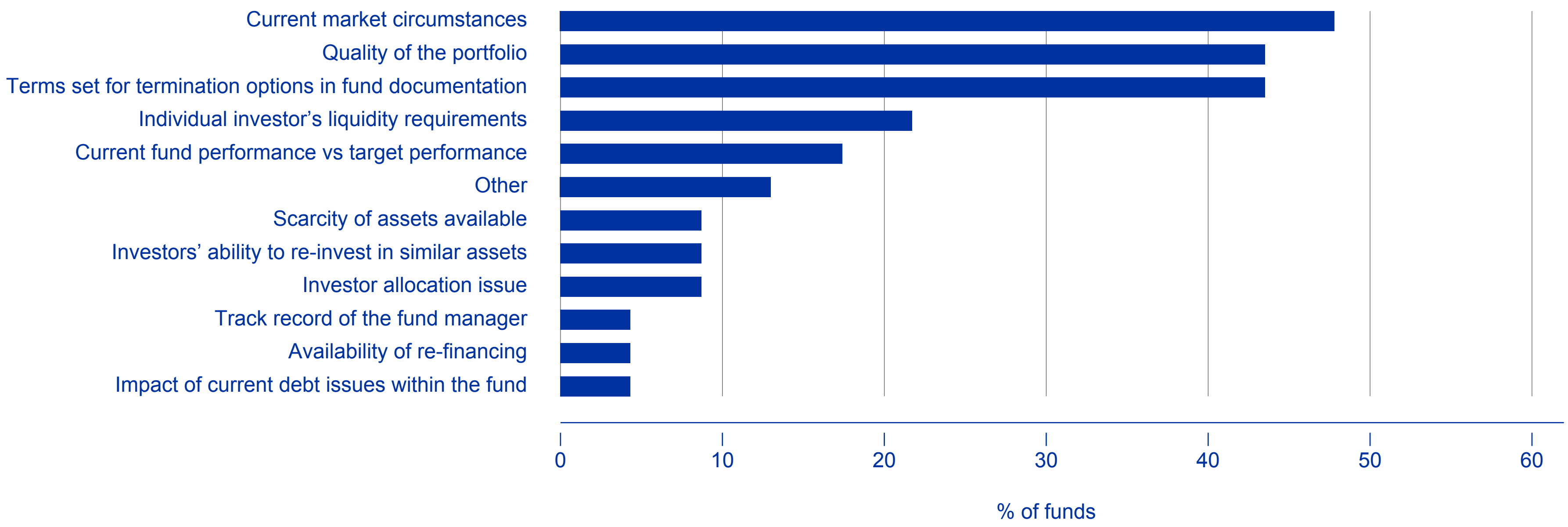
Issues affecting termination decisions

The factors affecting termination decisions were also explored, and here fund managers were able to indicate one or more reasons that drive their termination strategy.

In this context 47.8% of the 23 respondents stated that current market circumstances are the most important driver. The quality of the portfolio and terms set for termination options in fund documentation jointly occupied the second top spot with 43.5% of respondents indicating both issues as being important drivers when determining their termination decisions. This marks a continuation in respondents' opinion compared to last year with market circumstances occupying the top slot again.

> 'Choice of termination strategy is driven by current market circumstances'

Figure 15: Issues affecting termination decisions



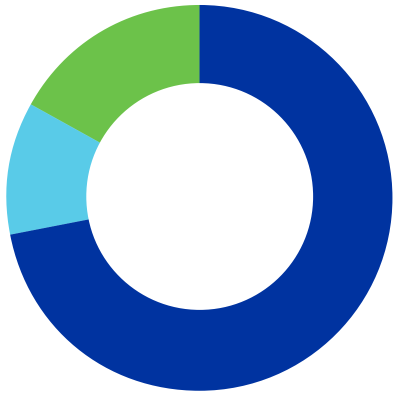
Preferred termination strategies

Fund managers were asked which termination strategy was finally chosen or most likely to be chosen. Only fund managers who had made a choice were invited to share their decision.

Therefore, of those that have made a decision, 72.2% consider liquidation as the preferred termination strategy. Liquidation was followed by rollover and extensions, as indicated by 16.7% and 11.1% of respondents respectively.

Figure 16: Termination option chosen or most likely to be chosen

72.2% Liquidation
11.1% Extension
16.7% Rollover



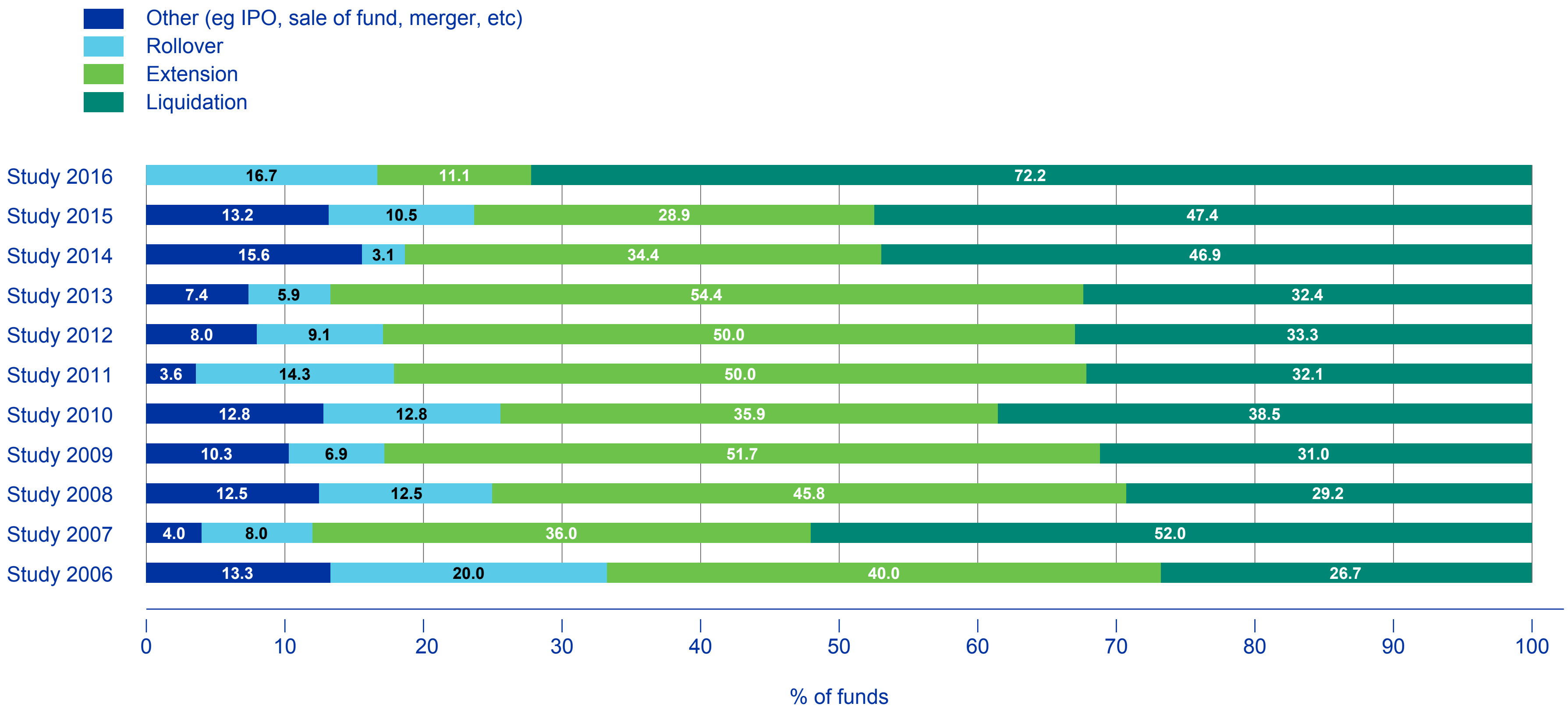
‘Liquidation is the preferred termination strategy’

Liquidation is the most likely chosen termination strategy, just as it was in 2015 and 2014. This has not always been the case – extensions were seen as the preferred option in every other year except 2007 and 2010.

Liquidation and extension remain the dominant terminations options. Other options (rollovers, IPOs, sales or mergers and so on) are of course relevant but have not attracted more than 30% of respondents in any year except 2006.

It is worth noting that in this year's survey no respondent chose other options (IPOs, sales or mergers and so on).

Figure 17: Termination option chosen or most likely to be chosen over 2006 - 2016



When looking across the funds' investment styles there are some distinct differences in approaches taken at the point of termination.

Liquidation is the preferred form of termination for core and value added funds. This is particularly true for core funds, where 87.5% of respondents chose liquidation as the favoured option for termination. The corresponding figure for value added funds is 62.5%.

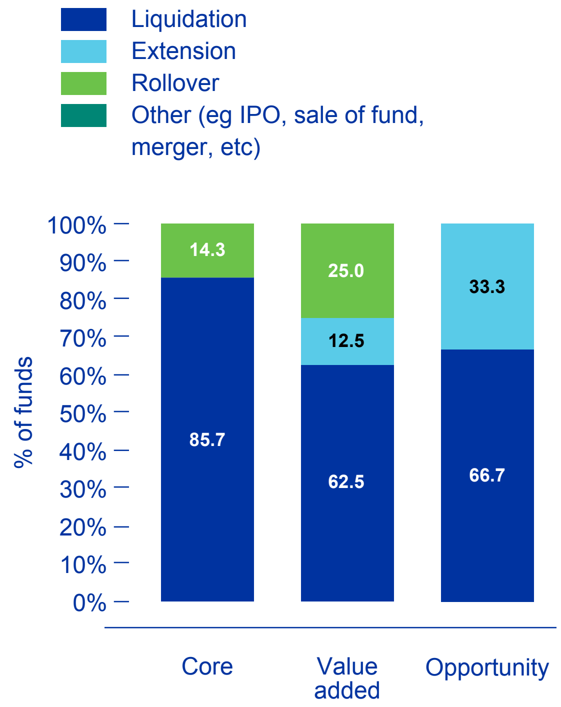
For opportunity funds the liquidation option is also important – more than half of the respondents chose liquidation as the preferred option (66.7%), with the remaining funds (33.3%) indicating that extension of the fund's life would be preferable.

The rollover strategy is of most interest to value added funds, and 25.0% of respondents in this category indicated it as a relevant termination option.

Strategies such as an IPO, sale or merger did not feature in this year's responses.

Extension of a fund's life may sometimes lead to structural or strategic changes in a fund. For example, a change in governance structures or fees might accompany the decision to extend. However, this is not necessarily the case if the original structure is sufficiently flexible.

Figure 18: Termination option chosen or most likely to be chosen by style



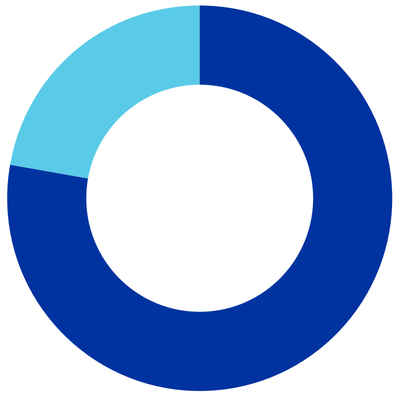
Structural changes to extended funds

In this year's survey 22.2% of respondents stated that strategic or structural changes would be made on foot of the decision to extend the fund's life. The remaining 77.8% stated that no such changes would be needed.

Prior editions of this survey reveal that the pattern is the same for funds that have already decided to extend and for funds that have not yet made a decision to extend but are most likely to, so in this year's survey the two were grouped together.

Figure 19: Termination option chosen or most likely to be chosen

77.8% No changes will be made
22.2% Yes, strategic or structural changes will be made to the funds' fees, governance, etc



'Structural or strategic changes are not expected for the majority of funds in extension'

CORPORATE

RESEARCH

INDUSTRY DATA

PUBLIC AFFAIRS

PROFESSIONAL STANDARDS

www.inrev.org