Real Estate Update

Portfolio Presentation for IAC

November 16, 2016

North Carolina Department of State Treasurer
Investment Management

Learn. Invest. Grow. Prosper.

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U.S. Real Estate Market Conditions

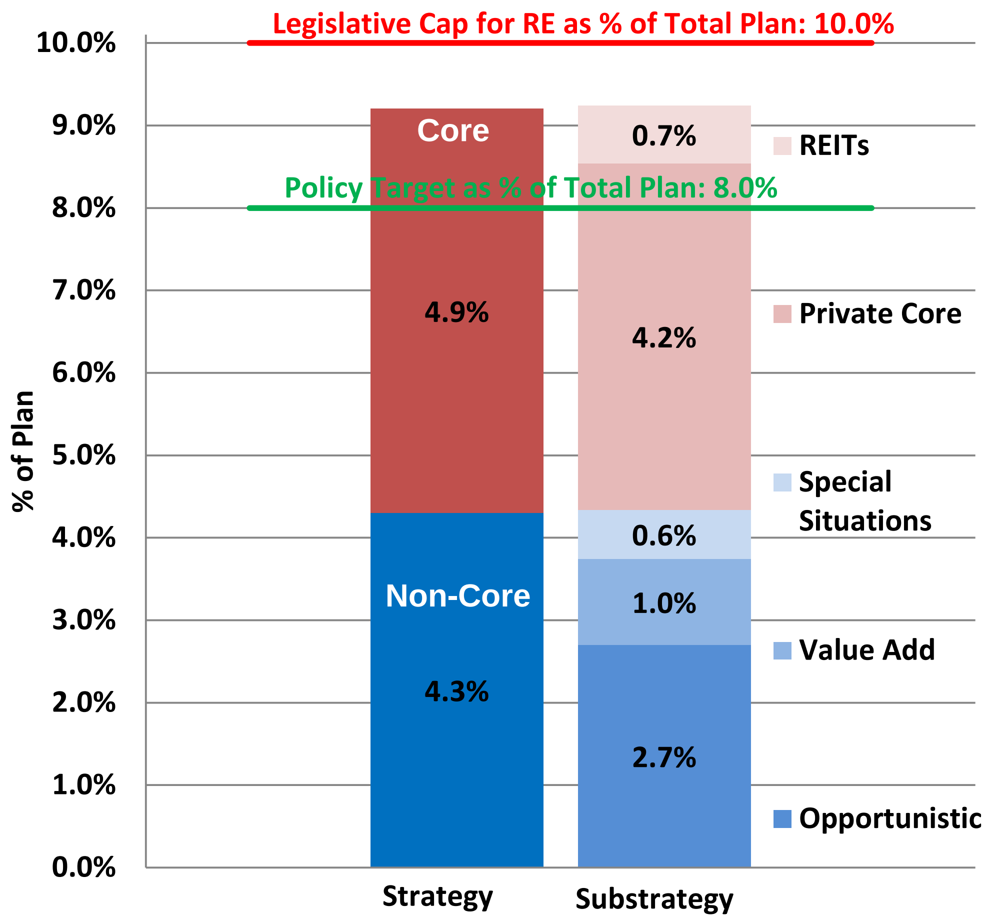
- Fundamentals are healthy despite lackluster U.S. growth
- Pricing remains strong and cap rates are flattening out in most sectors/markets
- Capital inflows to real estate are robust, but investors are moving cautiously
- Regulatory changes and debt market conditions are limiting the availability of credit

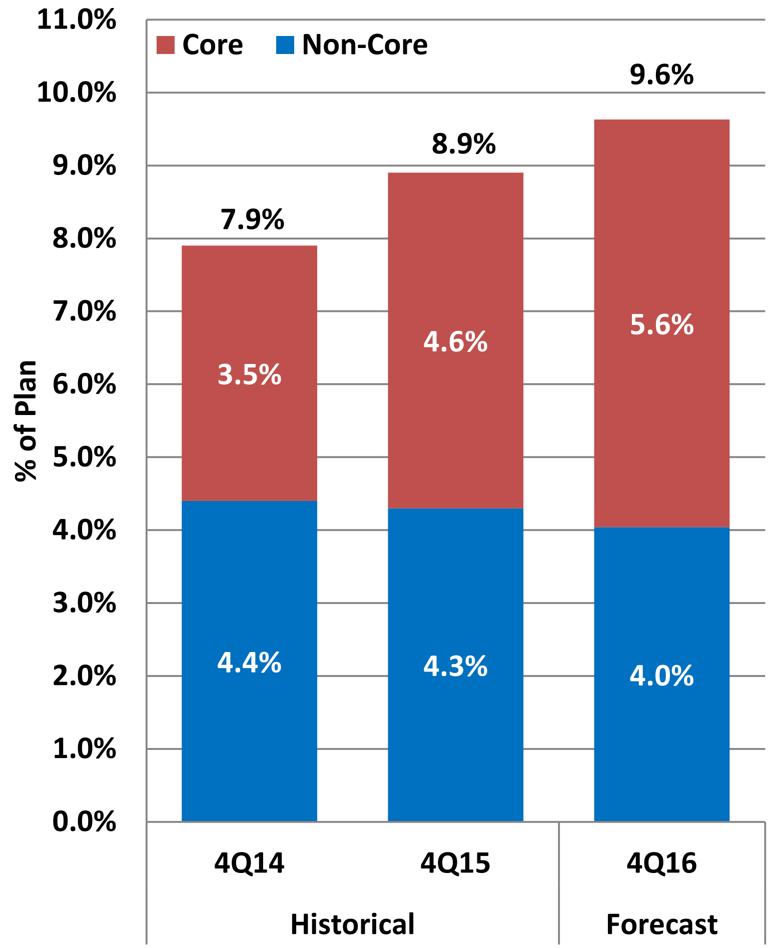
Multifamily	• Supply is a headwind, but vacancy remains low
Office	• Tech driven demand; absorption/rent respectable despite decelerating job growth
Retail	• Experiential and needs-based performing well; low-quality malls/strip centers struggling
Industrial	• E-commerce demand is a boon for rents and valuations, particularly infill and last mile
Hotel	• Dealing with CBD supply indigestion; fundamentals and values market-specific

Fundamental Investment Approach

Stay the course with our investment strategy…do not reach for yield	• Downside protection • Eye toward current income for core or speed to income for opportunistic strategies • Moderate leverage levels
Use thoughtful & deliberate portfolio construction	• Stabilize Core portfolio • Diversify by strategy, property sector and location • Balance asset risk and market risk by insisting on the highest asset quality and location • Target specific submarkets and streets
Leverage the size of our plan & skill set of our team	• Better terms & fees • More transparency and control • Ability to move quickly to capitalize on opportunities & dislocations • Be the founding investor for new strategies
Invest meaningful amounts with fewer best-in-class managers	• Separate accounts • Multiple strategies with single manager • Fee benefits
Take a long-term view toward investments and manager relationships	• Be involved, be nimble and follow through • Deliver results • Be a leader among LPs

Real Estate Allocation Overview





Valuation as of 9/30/16

Strategic policy transition to 5% Core achieved, while maintaining tactical overweight to Non-Core.

Non-Core Thesis

"To achieve attractive risk-adjusted net returns through appreciation and income from a diversified portfolio, planning for strategic exit optionality"

Office
Chicago, IL

Apartment
Jersey City, NJ

Hotel
Miami Beach, FL

Mixed-use
Brooklyn, NY

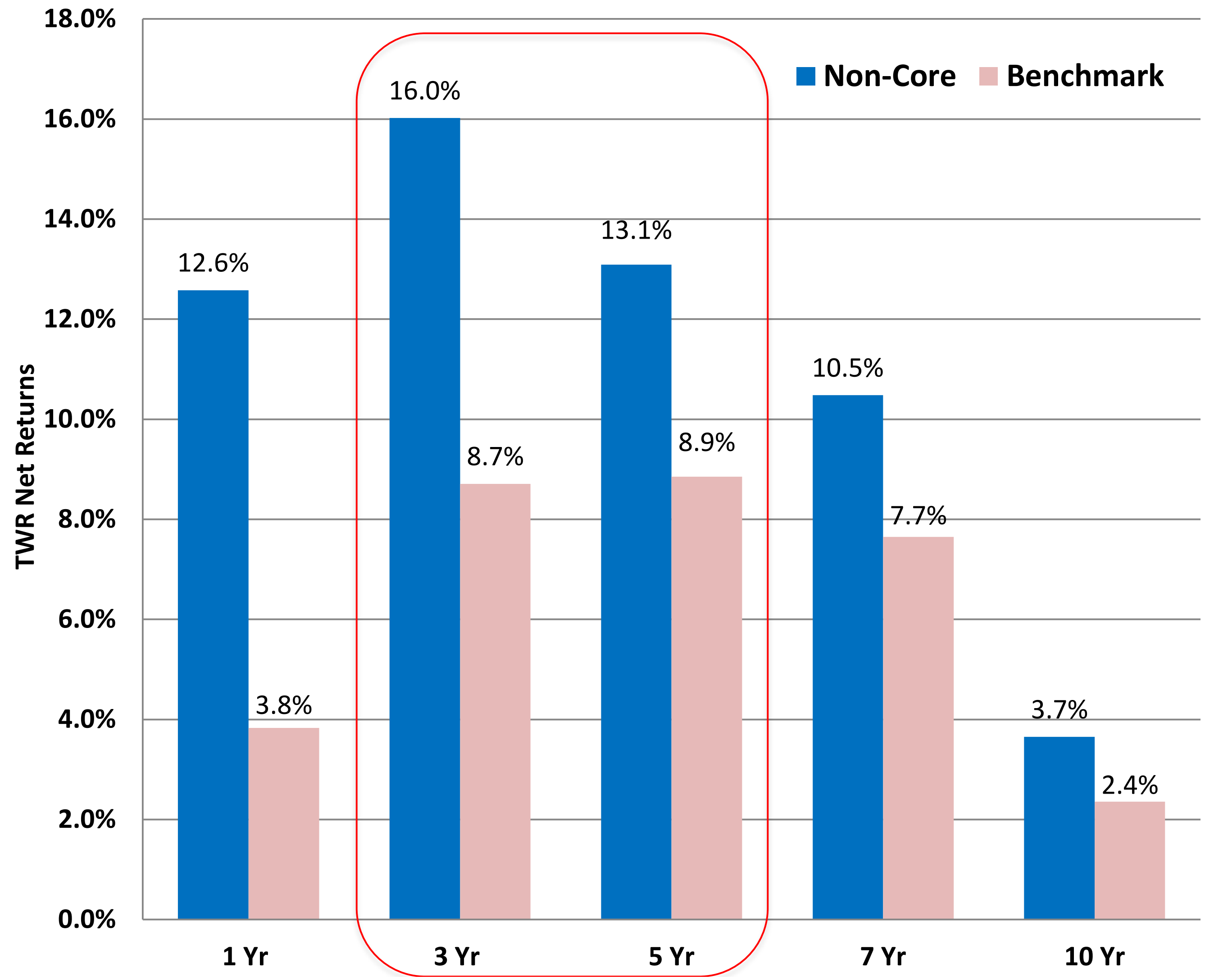
Non-Core RE Performance

Non-Core Contribution to Return

	3 Yr		Contribution
	Opportunistic		**9.6**
	Value Add		**6.4**
	Total Non-Core		**16.0**
	Major Drivers	*Vintage*	
O	NorthCreek	2011	1.9
V	NorthRock II	2012	1.4
O	BREP VII	2011	1.2
O	Lone Star II	2010	1.0
O	BREP VI	2007	1.0

	5 Yr		Contribution
	Opportunistic		**7.4**
	Value Add		**5.7**
	Total Non-Core		**13.1**
	Major Drivers	*Vintage*	
O	NorthCreek	2011	1.3
V	KTR II	2008	1.0
O	BREP VII	2011	1.0
O	BREP VI	2007	0.9
O	Lone Star II	2010	0.8

O = Opportunistic, V = Value Add



NCRS data through 9/30/16

Non-core outperformance achieved through concentration with high conviction managers utilizing lower than average leverage and risk compared to the overall industry.

Core Thesis

"To generate durable income and stable returns through strategic investments, with prudent use of leverage, in assets with long-term fundamental drivers that will endure for generations"

Residential
London, UK

Office
Sunnyvale, CA

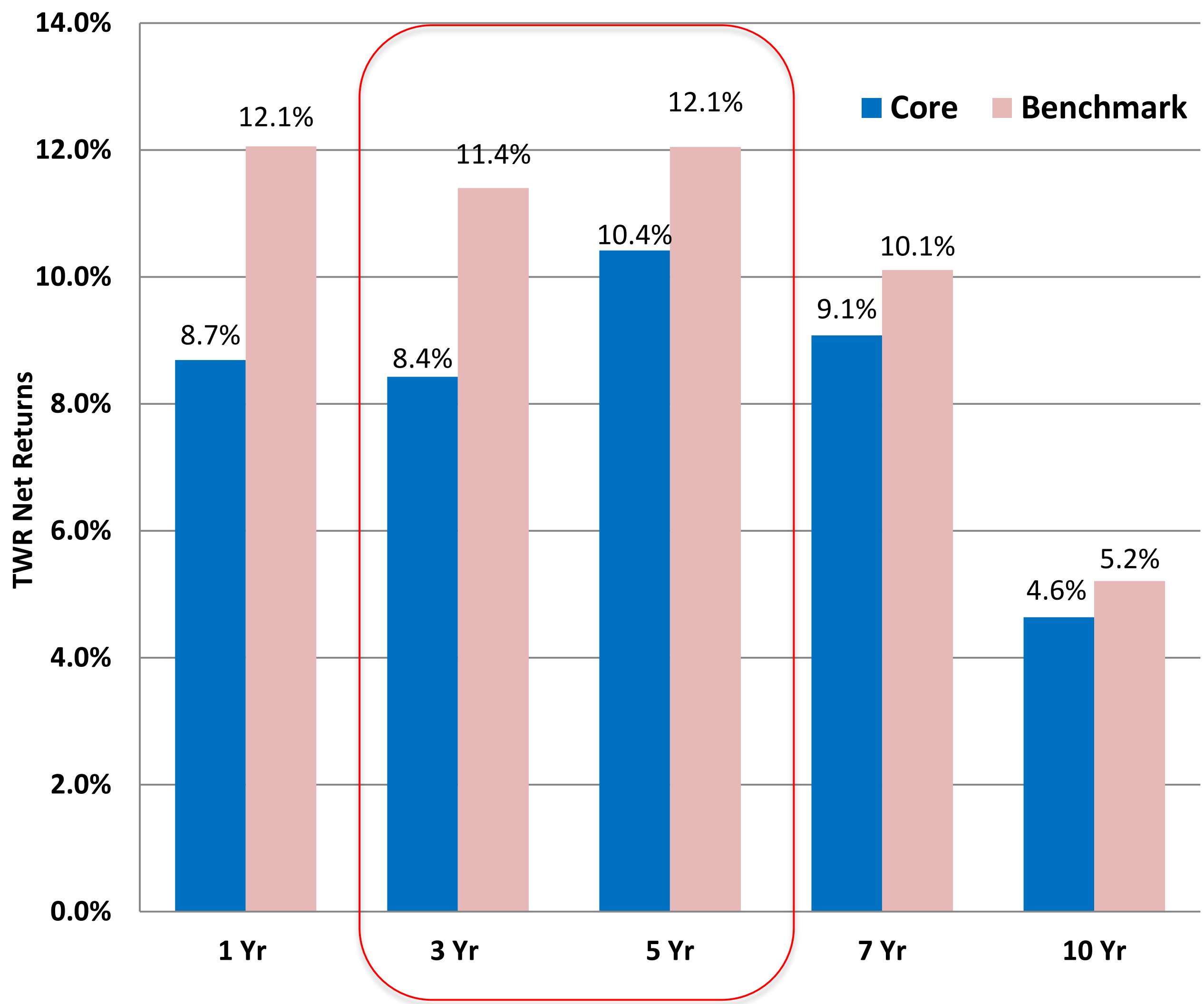
Office
New York, NY

Mixed-use
Fairfax, VA

Core Real Estate Performance

Core Contribution to Return		
3 Yr		**Contribution**
Private Core RE		**6.7**
REITs		**1.7**
Total Core		**8.4**
Major Drivers	*Vintage*	
PC NorthRock Core	2008	1.9
PC JP Morgan SPF	1989	1.8
PC Blackstone Edens	2013	0.8
5 Yr		**Contribution**
Private Core RE		**7.5**
REITs		**2.9**
Total Core		**10.4**
Major Drivers	*Vintage*	
PC NorthRock Core	2008	2.5
PC JP Morgan SPF	1989	2.1
PC UBS TPF	1984	0.9

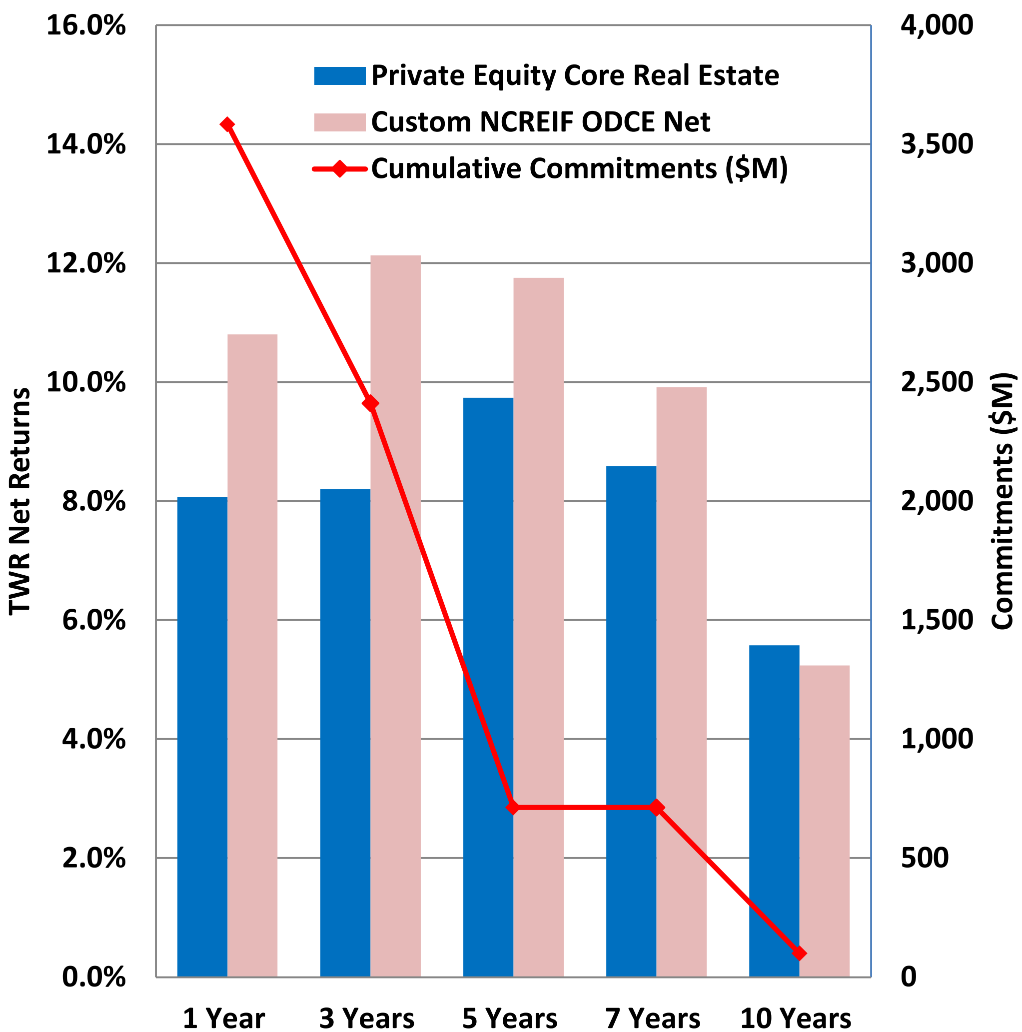
PC = Private Core Real Estate



NCRS data through 9/30/16

Generating solid absolute returns from an evolving Core portfolio against a mature benchmark.

Private Core Performance

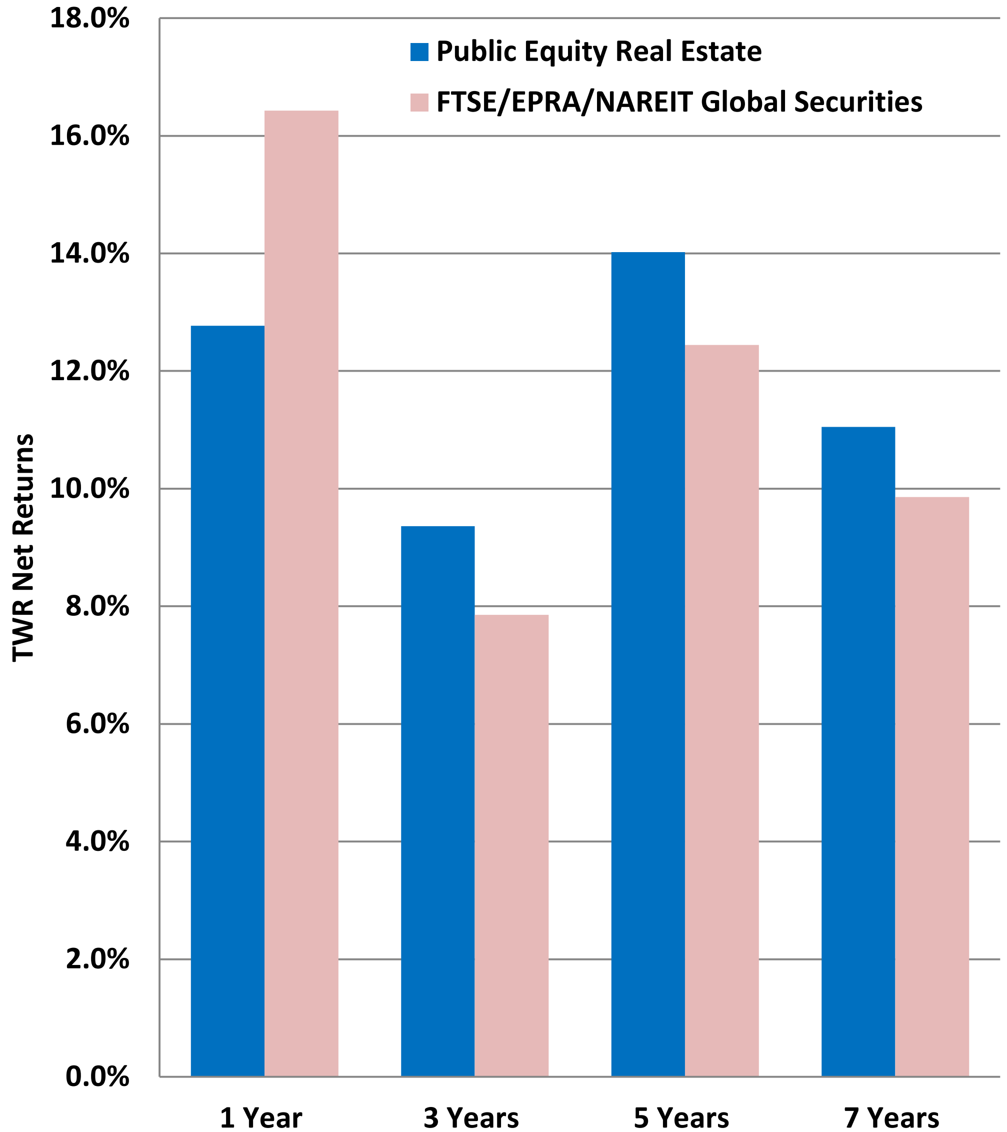


Source: NCRS data through 9/30/16

- Committed $2.9B in Core over the past 3 years
  - $1,040M in separate accounts
  - $940M in commingled funds
  - $890M in club deals
- Producing 8% returns even while going through the J-curve
- Strong current income will support returns even during periods of low appreciation

We expect core returns to converge with, and eventually outperform, the benchmark as recent commitments move through the J-curve.

REIT Performance

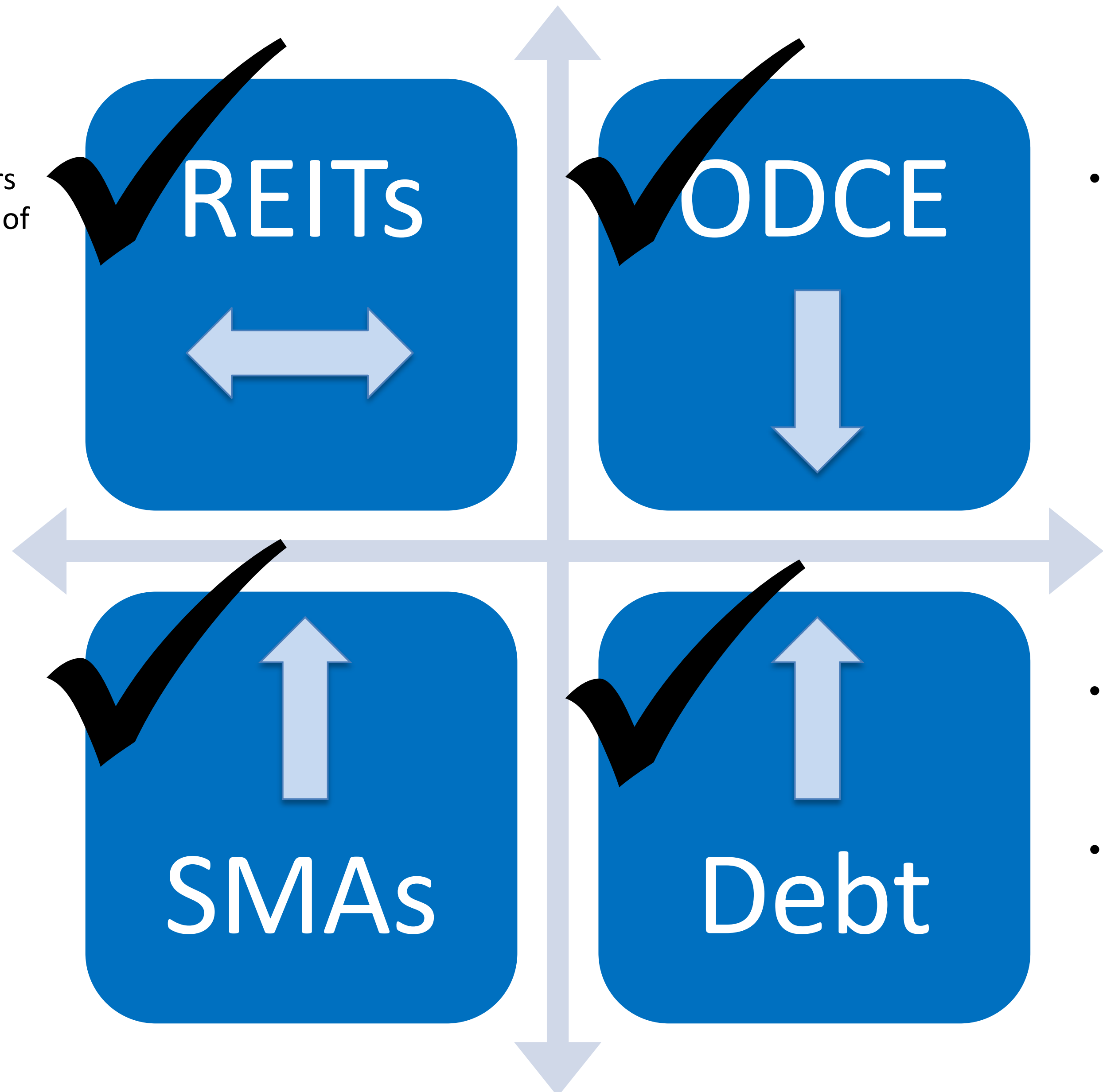


Source: NCRS data through 9/30/16

- Completed consolidation to a new REIT manager in April to enhance performance and significantly lower fees
- Moved from 100% active to 50% active and 50% passive
- 1-Year returns impacted by transition period and negative performance of a large single stock position we sold during the year. Performance of that position overall was strong, but it underperformed the benchmark in the last 12 months.

Core Transition Plan

- Consolidated managers and moved to a blend of active and passive

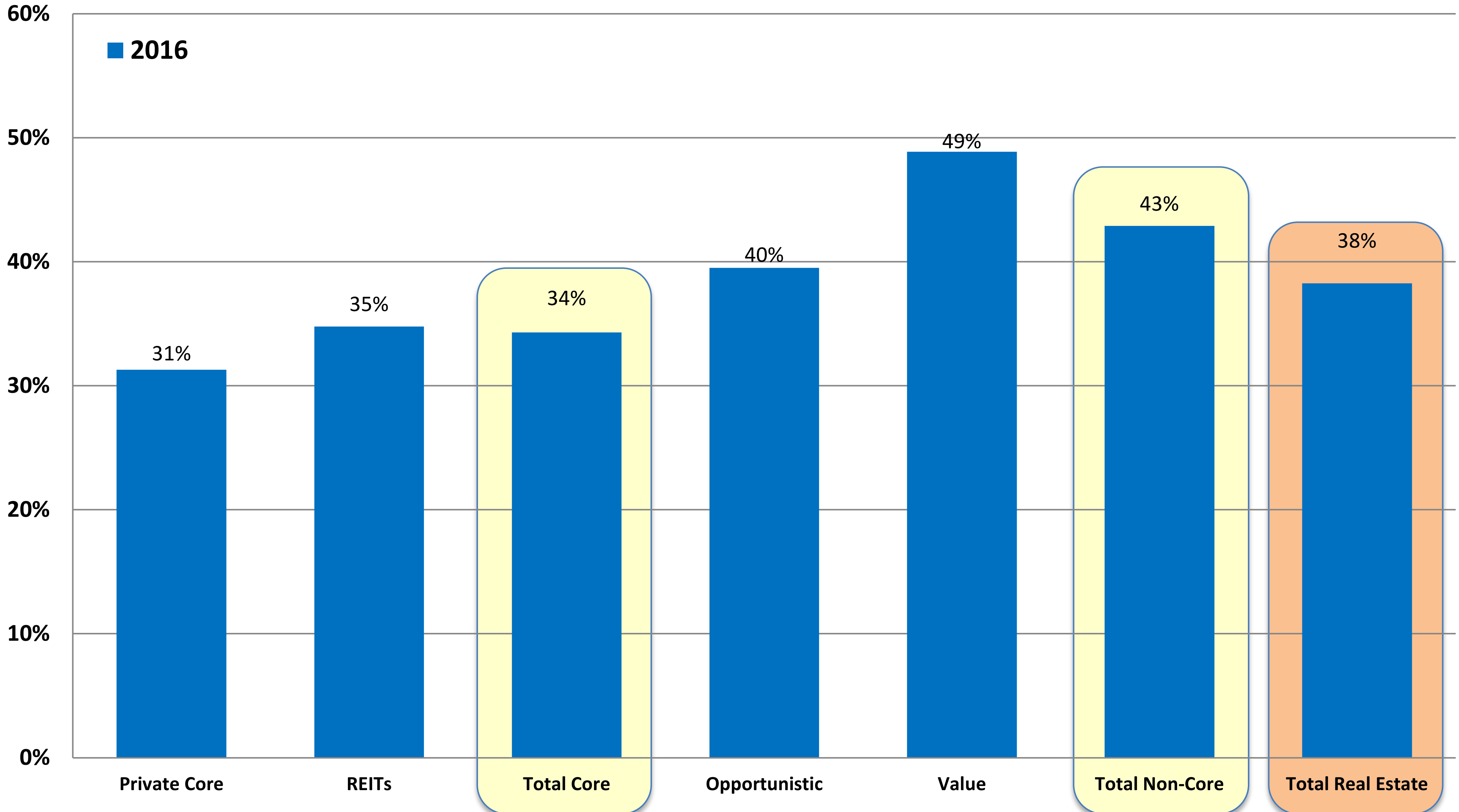


- Exercised redemptions to reduce ODCE exposure by approximately 50%

- $300M to a core industrial separate account
- Other opportunities under review

- Committed $200M to an open-ended debt fund
- Additional club debt fund is in process

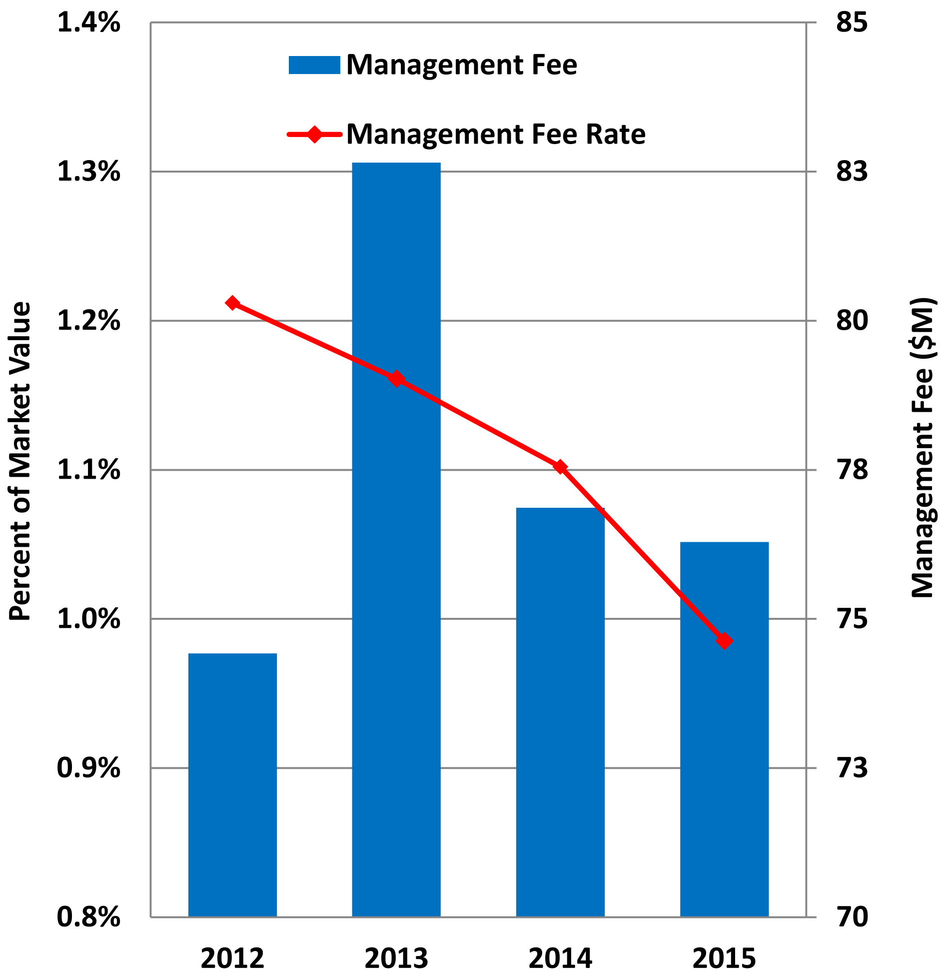
Leverage

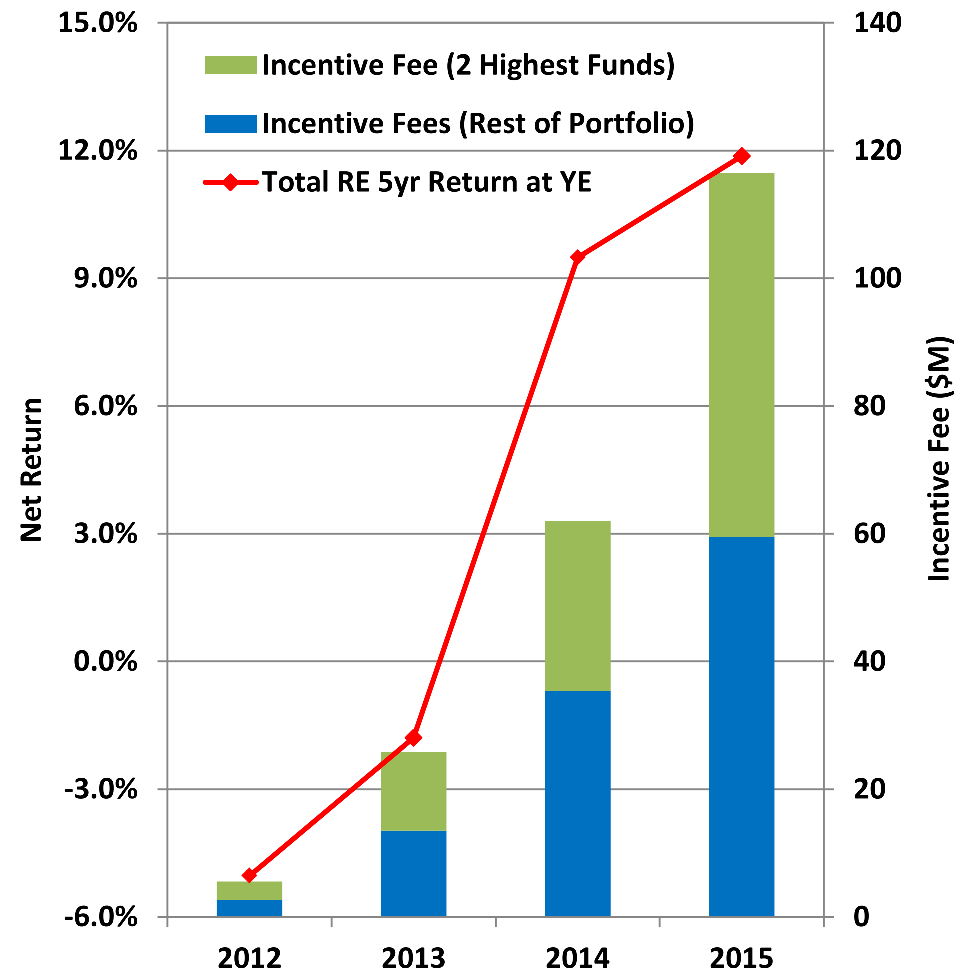


Source: Courtland Partners NCRS 2Q PMR

Maintaining prudent levels of leverage and retaining ability to adjust through our Separate Accounts.

Fees





Source: NCRS data through 12/31/15

Leveraging our size and increasing separate accounts have generated more favorable fees. Incentive fees have been driven by outperformance from a handful of top-tier managers.

Topics for Discussion

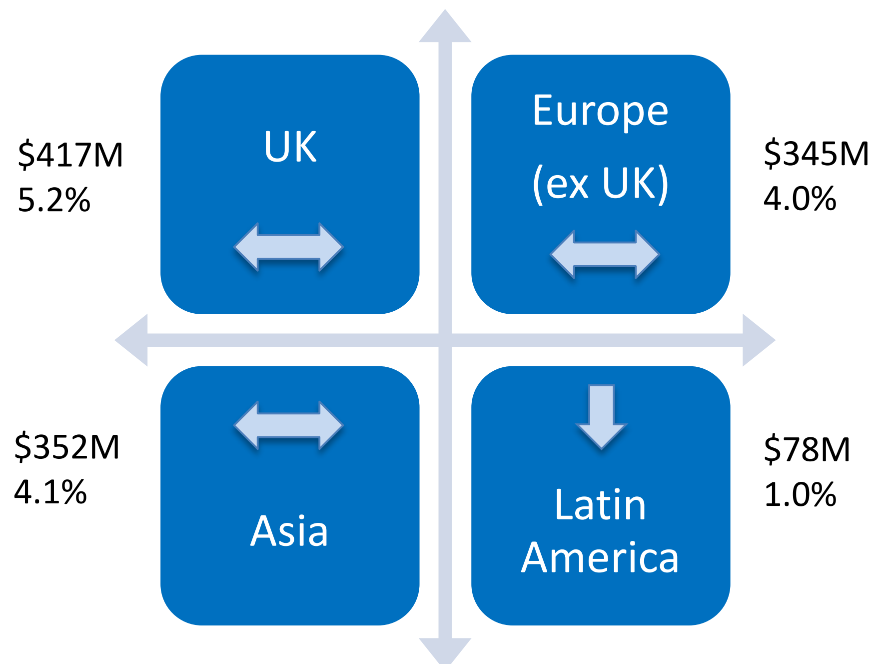
Investing Within Statutory Allocation Limits

- We maintain a robust, bottoms-up Cash Flow Model that guides us to invest within allocation boundaries
- Allocation constraint risks going-forward:
  - Loss of future fee breaks by skipping a fund with a high-conviction manager
  - Vintage year diversification risk
  - Inability to create additional separate accounts, which require a significant amount of seed capital

Topics for Discussion

International Exposure

- Foreign exposure totals $1.3B (approx. 15% of real estate portfolio)
- Additional diversification across markets and sectors
- Exposure to both large international funds and niche investments
- Investing abroad does not come without risks
  - Uncertainty and volatility (Brexit, Chinese growth, geopolitical, etc.)
  - Currency impact on returns can be significant



Source: Courtland Partners NCRS 2Q PMR

Thank You!

Together we can build and maintain a fiscally strong and prosperous North Carolina.

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