



State of New Jersey

DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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State Treasurer

May 18, 2012

MEMORANDUM TO: The State Investment Council

FROM: Timothy Walsh
Director

SUBJECT: **Proposed Investment in Northwood Real Estate Partners L.P
& Northwood Real Estate Co-Investors, L.P.**

The New Jersey Division of Investment ("Division") is proposing an investment of \$75 million in **Northwood Real Estate Partners L.P (Series III) and \$75 million in Northwood Real Estate Co-Investors, L.P. ("Northwood") for a total of \$150 million.** This memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.9.

The Division is recommending this investment based on the following factors:

Impressive Track Record: Northwood is led by John Kukral, former CEO and co-founder of Blackstone Real Estate Advisors. During his tenure at Blackstone from 1994 to 2005, Mr. Kukral oversaw the firm's real estate investment activity totaling \$5.8 billion across 160 separate transactions. Mr. Kukral's impressive investment track record at Blackstone consisted of a 37% gross IRR on realized and partially realized investments as of December 31, 2005. It is important to note that out of \$5.8 billion invested equity, only \$40 million in principal losses were realized (0.7% of invested capital).

Demonstrated Investment Discipline: While Northwood finished its initial capital raise of \$1.25 billion (\$750 million and \$502 million in the Series I Main Fund and Co-Investment Fund, respectively) in 2008, the manager demonstrated an exceptionally disciplined investment approach by only investing in one transaction during this period marked by substantial declines in the real estate and real estate debt markets. By maintaining stringent underwriting standards, the manager was able to take advantage of many attractive investment opportunities in 2010 and 2011 with very limited competition.

Prudent Use of Leverage: Since the firm's inception, the management team has demonstrated a very conservative approach regarding the use of leverage to execute the Fund's investment objectives. Specifically, of the fourteen transactions completed between August 2008 and December 2011, seven of the deals were funded entirely with equity. The current total portfolio leverage is approximately 42% on an LTV basis. Northwood only utilizes leverage in specific instances where the manager believes that the downside risk is limited.

Alignment of Interests: To date, Northwood has committed \$85 million to the Funds (\$75 million to Series I Main Fund and \$10 million to Series I Co-investment Fund), to be invested on a pro rata basis with the LP commitments.

A report of the Investment Policy Committee ("IPC") summarizing the details of the proposed investment is attached.

Division Staff and its real estate consultant, R. V. Kuhns, undertook extensive due diligence on the proposed investment in accordance with the Division's Alternative Investment Due Diligence Procedures.

The fund utilized UBS (the "placement agent") as third-party solicitor in connection with the potential investment. Staff has determined that the placement agent and its representatives met the registration, licensing and experience requirements set forth in the Division's Placement Agent Policy (the "Policy"). Pursuant to the Policy, the fund has disclosed the contract between the fund and the placement agent, specifying the scope of services to be performed by the placement agent and the fee arrangement between the placement agent, the general partner and any other third party.

We will work with representatives of the Division of Law and outside counsel to review and negotiate specific terms of the legal documents to govern the investment. In addition, the proposed investment must comply with the Council's regulation governing political contributions (N.J.A.C. 17:16-4).

Please note that the investment is authorized pursuant to Articles 69 and 71 of the Council's regulations. The Fund will be considered a non-core opportunistic real estate investment, as defined under N.J.A.C. 17:16-71.1.

A formal written due diligence report for the proposed investment was sent to each member of the IPC and a meeting of the Committee was held on May 10, 2012. In addition to the formal written due diligence report, all other information obtained by the Division on the investment was made available to the IPC.

We look forward to discussing the proposed investment at the Council's May 24, 2012 meeting.

Attachments

Fund Name: Northwood Real Estate Partners, L.P. & Northwood Real Estate Co-Investors, L.P. (Series III)

May 24, 2012

Contact Info: Vivian Tongalson, Managing Director, 575 Fifth Avenue, 23rd Floor, New York, NY 10017

Fund Details:

Total Firm Assets (\$bil.):	\$2.3 billion	Key Investment Professionals: - John Z. Kukral, President and Chief Executive Officer: has been an active real estate investor for over 29 years. He serves as the Chairman of the Investment Committee and approves all commitments by the firm. Prior to Northwood, he was the former President and CEO of Blackstone Real Estate Advisors from 2002 to 2005. - Erwin K. Aulis, Chief Operating Officer: has been active in the real estate investment management business for over 26 years. He is responsible for the day-to-day operations of Northwood, including asset management, capital markets, finance and control, investor relations and human resources. - Michael P. Sullivan, Chief Financial Officer and Chief Compliance Officer: has overall responsibility for financial reporting, tax compliance and property accounting.
Strategy:	non-core opportunistic real estate	
Year Founded:	2006	
Headquarters:	New York	
GP Commitment:	\$85 million	

Investment Summary

Northwood Investors, LLC, a privately-owned, private equity real estate investment firm headquartered in New York. Northwood is led by John Kukral, who while he was at Blackstone from 1994 to when he retired in 2005, ran five funds: BREP I-IV and BREP International. Northwood expects to opportunistically pursue real estate investments on a global basis by investing in various levels of the capital structures of assets and companies, with a particular focus on major metropolitan areas of the U.S. and super-regional markets in Europe. Within these markets, Northwood expects to focus on assembling a portfolio that is diversified across multiple product types and fits the Sponsor's investment strategy of seeking investments that have limited downside risk, while generating superior risk-adjusted returns with upside potential through capital appreciation or repositioning.

Existing and Prior Funds

<u>Funds</u>	<u>Strategy</u>	<u>Returns</u>
Blackstone Track Record	Non-core real estate	37% Gross IRR 2.2x MOIC
Series I	Non-core real estate	17.4%Gross IRR 2.2 x (Projected)

Vehicle Information:

Inception:	2008	Auditor:	Ernst & Young LLP
Fund Size (\$bil.):	\$2.3 billion	Legal Counsel:	Simpson Thacher & Bartlett LLP
Management Fee:	2% on committed, 1% on invested after initial commitment period	Accounting Firm:	Internal
Carry:	75% LP, 25% GP - LPs receive all invested capital, fees/expenses and preferred return before GP can take carry		
Hurdle Rate:	6%		
Additional Expenses:	100% fee offset		

NJ AIP Program

Recommended Allocation:	\$150 million: \$75 Main/Co-Invest each	LP Advisory Board Membership:	TBD
% of Fund:	6.5%	Consultant Recommendation:	Yes
		Placement Agent:	Yes
		Compliance w/ Division Placement Agent Policy:	Yes
		Compliance w/ SIC Political Contribution Reg:	Yes

*This review memorandum was prepared in accordance with the State Investment Council rules governing the Alternatives Investment Program and the policies and procedures related thereto.