ZRP

ZIFF REAL ESTATE PARTNERS

2022 Mid-Year Letter

Ziff Real Estate Partners
2022 Mid-Year Update and Outlook

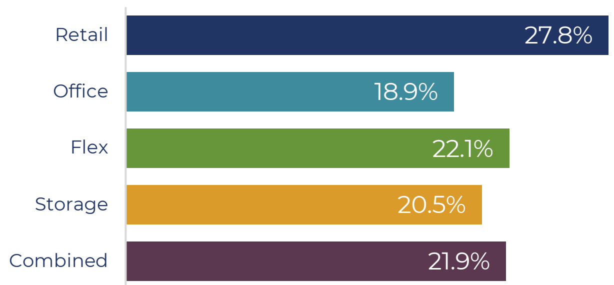
We would like to take the opportunity to provide an update on our investing activities year to date and our outlook for the commercial real estate market overall. Detailed second quarter 2022 reports for each individual Ziff Real Estate Partners (ZRP) investment or fund will be distributed in early August.

Investment Updates

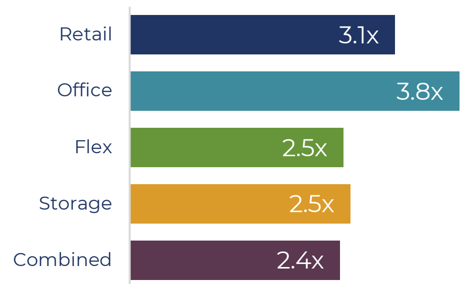
With the year-end valuation of our existing investments complete, we can report that the consolidated IRR for all owned properties was 27.8% in 2021. Last year presented ideal conditions for commercial real estate investing including high occupancy, growing rents, and declining cap rates.

While every year will not be this strong, our disciplined, value-add strategy utilizing in-house property management has allowed us to compound capital at attractive rates of return throughout the numerous economic and real estate cycles we have experienced over the past 31 years. Since our founding and through year-end 2021 our net realized leveraged IRRs and MOIC (Multiple on Invested Capital), overall and by asset type, are as follows:

Internal Rate of Return (IRR)



Multiple on Invested Capital (MOIC)



Acquisitions

We closed on the acquisition of Crosspointe Plaza in Greenville, SC for $18.5mm in June. Crosspointe is a Class A retail center in a high-traffic location with strong demographics and is adjacent to two newly constructed luxury multi-family projects. The center is occupied by several high-quality national tenants such as TJ Maxx and Chipotle, and our base case projections include an average yield of 8% and a mid-teens net IRR. The debt portion of the capital structure consisted of a 5-year fixed rate loan at 3.75%.

Crosspointe Plaza in Greenville, SC

Our Storage Opportunity Fund acquired three storage properties in the first half of this year; an existing facility in the Atlanta MSA, and two adaptive reuse projects, with one in Roanoke, VA (see rendering below) and the other in Waldorf, Maryland which is in the D.C. MSA. The total investment in these projects will be ~$24mm when complete. Debt financing for the Atlanta and Roanoke properties include 5-year fixed rate loans bearing an average interest rate of 3.95%, and we are currently in the process of vetting numerous proposals from lenders for the Waldorf project.

Storage Rendering for Roanoke, VA Conversion

Our Storage Opportunity Fund has drawn approximately 1/3 of committed equity and has acquired six properties; the pro-forma returns for investments made to date are in line with our initial projections. We are pleased with the investments we have made to date and are hopeful that tighter lending conditions will reduce competition from less well-capitalized acquirors and further expand the acquisition opportunity set for existing storage properties.

Dispositions

Our disposition decisions are driven by a disciplined asset management process involving regular assessments of remaining upside vs. risk, with sales initiated when properties approach full valuation.

We closed the sale of Galleria Commons in June, just over a year after the acquisition. Galleria was acquired 40% vacant and the Ziff property management team quickly executed various physical and signage upgrades while the leasing team led an aggressive and strategic approach that took occupancy up to 82% in less than a year. We were approached by several unsolicited buyers and after a thorough marketing process, **we closed on the sale of the property at 93% of our 5-year target upside case, generating a net IRR of 77% and an MOIC of 1.82x.** This hold period is much shorter than typical for Ziff, but we felt it was prudent to exit the investment at this time.

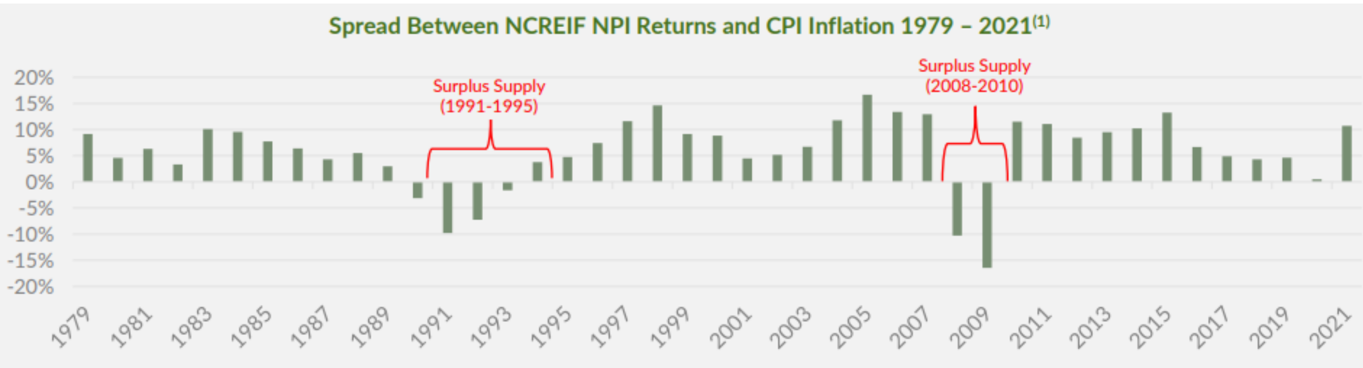
Galleria Commons in Charlotte, NC

77%	1.82x	13 months
Net Realized IRR	Net Realized MOIC	Ownership Period

Commercial Real Estate Market Outlook

For the past several years, commercial real estate values have been increasing, driven by both growing net operating income (NOI) and lower cap rates. Given inflation, higher interest rates, and a possible recession, what should investors expect from commercial real estate in this new climate?

Commercial real estate is often described as a hedge against inflation because returns have usually exceeded the CPI (Consumer Price Index), as shown below. Rent growth has tended to exceed expense growth and sectors with short-term leases that can increase rents more frequently (such as self-storage) typically fare particularly well. Regarding cap rates, while a sustained upward move in interest rates could pressure cap rates to move higher, in the past the spread between cap rates and the 10-year US Treasury has often compressed, with cap rates increasing less than the increase in interest rates.



When there is strong demand for CRE coupled with a limited supply, CRE's ability to hedge against inflation is amplified.

As you can see above, commercial real estate returns have lagged CPI in periods of "surplus supply" brought on by financial distress and selling by lenders who have foreclosed on defaulted real estate loans. The two periods above relate to the S&L crisis and ensuing liquidation of one-third of the savings and loan institutions in the US in the early 1990's, and the Great Financial Crisis in 2008 and 2009.

While there have no doubt been some excesses in real estate lending in this current cycle, at this time we do not foresee an episode of forced selling similar in magnitude to these prior crises. Although, as a well-capitalized investor with dry powder to invest, we would seek to take advantage of these opportunities should they occur.

Stagflation (inflation and an economic slowdown) is a risk, and a severe recession could certainly impact leasing activity, rent increases and NOI growth although we believe the affordable retail, industrial and self-storage space we provide to consumers and necessity-based businesses is insulated from economic downturns.

Where does the commercial real estate market go from here? While much depends on the path of interest rates and the economy, we will first see a significant slowdown in transaction volumes, and we are beginning to see that already.

Sellers want yesterday's prices and buyers want lower valuations to reflect higher cost debt, more restrictive terms from lenders and the possibility of a recession. Private real estate markets obviously react more slowly than liquid public markets and it will be several quarters before we see the degree to which cap rates and valuations adjust to the higher interest rate environment.

Possibly offsetting the pressure of higher interest rates is what we believe will be continued strong demand from both individual and institutional investors to allocate to the commercial real estate asset class. The consistently positive returns commercial real estate has produced for decades, with low volatility and low correlation to other assets continue to attract capital. Further, rising land, labor and construction costs continue to increase replacement costs and reduce developers' ability to bring new supply, leaving many asset types with a favorable supply/demand balance that should support steady rent growth.

Overall, the outcome of higher interest rates and moderating economic growth may be a healthier commercial real estate market, with a better balance between supply and demand and cap rates widening a bit from their all-time lows. This should improve the playing field for disciplined, well-capitalized investors like ZRP. For the immediate future, investors will rely more on NOI growth rather than cap rate compression to deliver returns.

ZRP Approach and Strategy

As a value-add investor, the primary driver of our investment returns has been NOI growth, driven by investing in and physically improving the properties we own and by providing outstanding service to our tenants with our in-house property management and leasing teams.

This approach will not change, and we will maintain our acquisition discipline by adjusting the prices we will pay to reflect the current terms of financing and market conditions.

The conservative modeling assumptions we use (for rent growth, lease up time and exit cap rates) give us comfort that our existing investments will deliver the returns we have forecasted. For our exit cap rates, we usually assume a certain expansion of our entry cap rate; for example, when self-storage assets are trading in the 4-5 cap range as they have been recently, we use 6-6.5% exit cap rates, giving us cushion from upward pressure on cap rates.

Tighter lending standards may reduce competition and create opportunities for us; an increase in defaulted loans by stressed borrowers could result in more compelling acquisition values.

Overall, we feel well prepared for the current environment and will employ our strong balance sheet, talented team, and 30+ years of experience operating in good times and more challenging times, to carefully navigate whatever comes our way.

As always, feel free to contact us if there are any questions we can answer. Thank you for your partnership.

If you are an existing investor and would like to speak in more detail, we are always available for a call. If you are a prospective investor who would like additional information about Ziff, or you would like to refer a friend, please contact Sarah Brantley, Partner, Finance & Investments.

We wish you and your family a healthy and enjoyable summer.

Ziff Real Estate Partners

Tim Walter, Chairman & Managing Partner **Curt Schade, Managing Partner**

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