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DEPARTMENT OF THE TREASURY
DIVISION OF INVESTMENT
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April 13, 2006

MEMORANDUM TO: State Investment Council

FROM: O. Ike Michaels, Jr.
Associate Director

SUBJECT: **Proposed Real Estate Investment in Funds to be Managed by CIM Group, Inc. and Deutsche Bank's Real Estate Opportunities Group**

This due diligence memorandum is presented to the State Investment Council (the "Council") pursuant to N.J.A.C. 17:16-69.12 (a) to report on two proposed real estate investments: a $50 million commitment to the CIM Urban REIT, LLC (the "REIT") managed by CIM Group, Inc. ("CIM"), and an $100 million commitment to the RREEF Global Opportunities Fund II ("Fund II") managed by Deutsche Bank's Real Estate Opportunities Group ("REOG").

Please note that these investments will be authorized pursuant to Articles 69 and 71 of the Council's regulations, which became effective on June 20, 2005. These investments will be considered real estate investments as defined under N.J.A.C. 17:16-71.2 (a).

The Alternative Investments Procedures adopted by the Council on January 20, 2005 require any potential alternative investment opportunities to be identified and initially evaluated by the Head of Alternative Investments of the Division (Bill Clark in an acting capacity) and the applicable Asset Class Consultant (The Townsend Group for Real Estate, or "Townsend") in coordination with the DOI Investment Committee (myself acting as Deputy Director and Bill Clark).

As a result of internal and external sourcing, the DOI Investment Committee identified these proposed investments. As a result, Townsend and Division staff proceeded to undertake extensive due diligence on the proposed investments. We completed the same due diligence process as with all the other alternative investment opportunities presented to the Council.

Based on this due diligence, the Division has determined that the proposed investments meet the criteria for investments set forth in the Alternate Investment Procedures.

The CIM Urban REIT, LLC (the "REIT") is our first real estate investment utilizing a "core plus" strategy which seeks to invest in substantially stabilized assets in core property types

primarily multifamily residential, retail, office, parking and mixed-use properties in urban areas throughout the United States. Since 1994, the fund manager, CIM Group, Inc. ("CIM") has invested approximately $2.2 billion in "qualified" urban areas primarily in California and the D.C. metro area for the California Public Employees Retirement System ("CalPERS"), the California State Teachers Retirement System ("CalSTRS") and Federal Realty Investment Trust in California.

For this fund, CIM has qualified 72 urban communities (including the New Jersey cities of Newark, Harrison, Long Branch, and Jersey City) for opportunistic investments using a stringent proven qualification methodology that takes about three years to complete. This methodology is focused on population density, improving demographics, barriers to entry, complex land-use regulations and entitlement processes, underserved niches, and strong public and private commitment, to mention but a few. To date, CIM has invested in 21 different communities.

We consider CIM a seasoned urban real estate manager that has attracted significant support with other institutional investors. The Founding Principals (3 individuals) and other employees (about 140 individuals) are committing $20 million (or 5% of the fund). A favorable sliding scale investment management fee is based on gross asset value of the Fund, and all other legal and economic terms associated with this Fund are fair and consistent with market standards.

The RREEF Global Opportunities Fund II ("Fund II") is managed by the Real Estate Opportunities Group of Deutsche Bank ("REOG"). Fund II is a successor to a previous successful fund with a strong track record, and will execute fundamentally the same investment strategy under the direction of the same senior management team which has remained intact for the last 12 years. Consistent with the prior fund, REOG is exploring several diversified strategies for Fund II including: single asset and asset portfolios, international joint ventures, private equity platform investments with strong operating partners, and entity recapitalizations distributed across Europe (50-55%), Asia (20-25%) and the Americas (25%).

The investment manager ("REOG") employs regional teams staffed by local individuals with extensive experience with similar types of investments and strategies, and their track record is strong dating back to 1991. As of December 31, 2005, REOG has invested $3.2 billion in 199 investments (51% in Europe, 22% in Asia and 27% in the Americas). One hundred and twenty six of these investments have been realized generating a 25.8% gross weighted average IRR.

Deutsche Bank ("DB") will invest 9.9% of third party equity up to $100 million with REOG employees investing roughly $10 to $15 million of the total co-investment. The management fees are reasonable (1.5% on committed capital under $75 million; 1.25% for contributions of $75-$150 million, and 1.0% for commitment above $150 million); and all the legal and economic terms associated with this Fund are fair and consistent with market standards.

Formal written due diligence reports for these proposed investments were sent to each member of the Investment Policy Committee of the Council on Friday, April 7, 2006, and a meeting of the Committee was held on April 11, 2006. In addition to the formal written due diligence reports, all other information obtained by the Division on these investment was made available to the Investment Policy Committee.

After review of the extensive due diligence, the Investment Policy Committee of the Council decided to report on these proposed investments to the full Council pursuant to Step 4 of the Alternative Investments Procedures. Under these procedures, the Council may adopt or otherwise act on this report.

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 these investments. In addition, these proposed investments must comply with the Council's "pay to play" regulation (N.J.A.C. 17:16-4). While we are confident that we will work through these issues, the potential exists that a successful resolution will not be reached with the general partners.

We look forward to discussing these proposed real estate investments at the Council's April 20, 2006 meeting.

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Attachments