Exhibit F - Private Real Estate FY 2022 Annual Tactical Plan

INVESTMENT GROUP

MEMORANDUM

TO: Investment Advisory Committee – Employees Retirement System of Texas
FROM: Meketa Investment Group ("Meketa")
DATE: January 25, 2021
RE: Private Real Estate Portfolio Annual Tactical Plan for Fiscal Year 2022

Preface

The proposed Private Real Estate Portfolio Annual Tactical Plan for Fiscal Year 2022 (September 1, 2021 through August 31, 2022) was prepared by Meketa Investment Group in collaboration with Staff during January 2021, while the COVID-19 pandemic raged globally. The future for almost all geographic real estate markets continues to be cloudy during the next 12-24 months. The pacing plan contained herein is highly subject to change. (Note: the previous agenda item dealt with adjustments to the current year's target commitments, reflecting the fluid market conditions and Staff's real time portfolio management in response to changes observed during the first year of the pandemic.)

We caution that the FY 2022 plan may be an exercise in "guesstimating," because it is still too early to draw reliable inferences concerning prospective market conditions, and managers' responses thereto, which will not be uniform. Like other asset classes, so much of the private real estate sector's future hinges on the delivery of the vaccine and therapeutics, mutations of the virus, and subsequent changes in behavior by real estate occupants and investors. As the second calendar quarter of 2021 unfolds, and a timetable for herd immunity is established by health officials, we expect to better understand future cash flow implications and have a better sense for temporary versus permanent value impairment. We will also better understand the investment landscape and opportunity set emerging from this unprecedented set of circumstances.

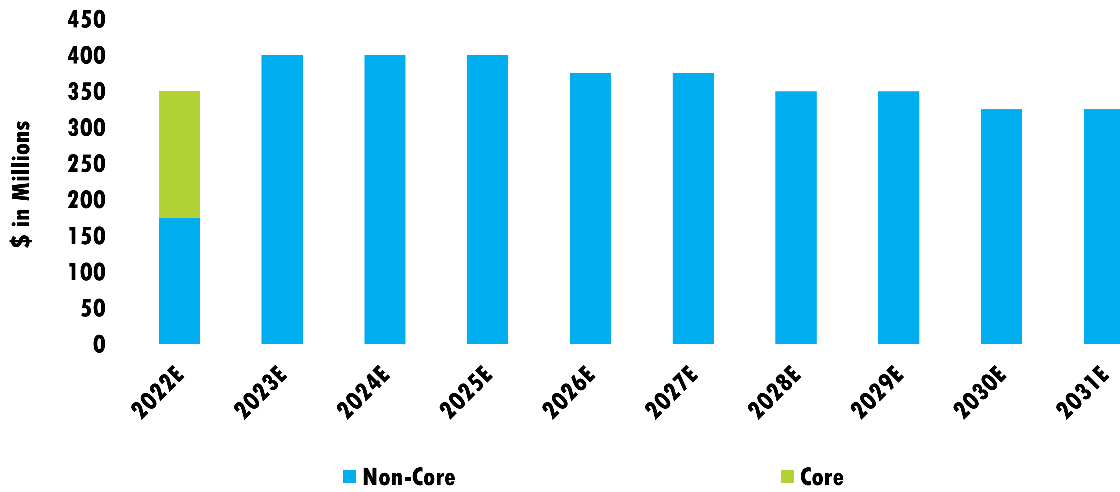
As if the pandemic was not enough of a second standard deviation event, the change in administrations in Washington, and the new policies that will be proposed, also have dramatic implications for landlords and tenants across most property sectors. Interest rates are widely expected to stay low for near to medium terms, notwithstanding the changes in leadership; however, influences on capital markets, and the markets' responses to unprecedented borrowings and deficits, will also play a role in Staff's decisions to deploy capital.

On the plus side, several factors mitigate these conditions and offer optimism for the vintage. The role of private real estate is clear within the overall System's portfolio construction. The System has the ability to take risks where the returns warrant. Finally, Staff is experienced, thoughtful and manages the real estate plan holistically through investments in well-structured, well-led commingled funds and associated co-investment vehicles.

Executive Summary

Staff will continue committing capital to private real estate on a highly selective basis, and currently targets up to $350 million in commitments for fiscal year 2022 and $400 million in commitments in fiscal year 2023 as seen in Exhibits 1 and 2.

Exhibit 1 - ERS Commitment Schedule by Strategy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Non-Core
Core

Exhibit 2 - ERS Fiscal Year 2022 Tactical Plan

FY 2022Tactical Plan		
Category	Number of Investments	New Commitments in $ Millions (Range)
Core	2-3	$175 ($0-$350)
Non-Core	3-6	$175 ($0-$350)
TOTAL	**3-8**	**$350 ($300-$700)**

Given the role of real estate within the context of the overall System's Portfolio, capital will be deployed across both core and non-core strategies.

Meketa highlights the following near-term investment dynamics that are likely to inform the TX ERS (the System) Staff's investment activities in Fiscal Year 2022:

1. CORE RETURNS WERE GENERALLY FLAT DURING CALENDAR 2020, as income collections turned out to be stronger than anticipated at the end of March. There was significant disparity within returns based on property type and location. Hospitality, retail and office performance was severely impacted. Multifamily and storage results were mixed. Industrial, data centers and life sciences were strong. City centers suffered more than suburban locations generally. Valuations, which are highly contingent on rent growth and absorption forecasts, were generally lower, with industrial and tech related properties an exception. Expectations of flat rental rates and turnover in occupancies are expected through 2021 and 2022 as vaccinations and therapeutics are distributed and space patterns return to previous levels.

   Non-core risk investments in closed end funds, which deliver the bulk of their returns from sales proceeds, and whose interim valuations are determined by their sponsors, had mixed results during calendar quarters 2 through 4 in 2020.

2. TRANSACTION ACTIVITY HAS COME TO A NEAR HALT. Transaction volumes in Q2-Q4 were lower than the previous five years, and thus, there was very little price discovery, especially in those property types that were impacted significantly by the pandemic. Notwithstanding the uncertainties, lower interest rates predominated the transaction market and expectations. Many institutional investors have increased their private market asset allocations, and commitments to future funds have created a record amount of "dry powder" available for purchases. Lenders have not been required to force non-performing loans, and the attendant collateral, into the markets as was seen in the Great Financial Crisis in 2008-2010. As interest rates dropped, so did cap rates in those transactions that crossed in data centers, warehouse and life science properties. Most private equity real estate buyers, expecting distress and bargains to appear, have not been able to place capital easily. Sellers have generally refused to accept these reduced terms

3. FORWARD VALUATIONS ARE DIFFICULT TO ESTIMATE. Many industry participants expect a flat to 10% diminution in value reported overall in core funds during 2021. This will be partially offset by 0.5% to 1.0% quarterly income returns. For non-core funds,

whose performance is more dependent on higher levels of leverage, the values may decline in 2021 as much as 10% to 20%, depending on absorption and resale.

To review the different valuation policies between core and non-core funds: Core funds rely on (a small number of) third party appraisers to determine value. These firms generally overshoot in both directions: late on the way down and late on the way up. Changes were made in 2020 underwritings, and we expect more in 2021, to reduce rental growth rate assumptions, absorption rates, discount rates and cost of leverage, to try and reflect the changes in the perceived risks attendant to owning illiquid, operationally intensive assets. These adjustments are more art than science, since it is unlikely the market will produce nearly the same level of transaction volume as during the past several years. Nevertheless, these opinions of value will be primarily based on actual contracts, i.e., the signed leases, often from creditworthy lessees. Investors with appropriate liquidity and dry powder for private markets investing may find interesting acquisition opportunities at materially reduced basis.

4. REBALANCING AND REDEMPTIONS ARE OCCURRING ALBEIT IN A CONSTRAINED MANNER. Following custodians' reports for Q4 2020, most investors are reviewing their pacing plans for additional private real estate commitments, incorporating revised estimates of total plan size, delayed capital calls from newer real estate funds, and reduced distributions from earlier vintage funds.

   Redemption queues at open-end funds did not gap out at year end. Most sponsors have suspended or significantly reduced any redemption payouts for an indefinite period, with quarterly reassessment and priority to preserving the value of the Portfolio's assets.

5. MAINTAIN FOCUS ON EFFECTIVE EXECUTION AND PORTFOLIO MANAGEMENT. Staff should use its well-established relationships with strong partners to (i) closely monitor existing portfolios and key investment professionals, (ii) assess emerging opportunities to co-invest and/or otherwise deploy capital opportunistically, and (iii) continue to use its scale and status as a reliable, oftentimes lead, investor, to effect lower fees and preferred operating terms with general partners compared to smaller institutions.

Introduction

This memo serves as the Private Real Estate Portfolio Annual Tactical Plan (Annual Tactical Plan) for the fiscal year ending 8/31/2022. Meketa creates this Annual Tactical Plan as a guiding reference only, and it is not intended to overrule prudent real estate investment decision-making, particularly in periods of extreme market volatility. Real estate and capital market conditions will be very fluid and dynamic during the remainder of this fiscal year ending 8/31/2021, and revisions to this 2022 plan may be warranted when additional data becomes available.

By Policy, the objectives of the System's Real Estate Portfolio include:

1. Preserving the System's capital;
2. Enhancing the System's Total Portfolio risk-adjusted returns;
3. Further diversifying the System's Total Portfolio;
4. Reducing the System's Total Portfolio volatility; and
5. Providing a hedge against inflation.

The primary risk controls of the Private Real Estate Portfolio include the annual pacing plan, regional diversification, strategy diversification, property type diversification and leverage considerations. As of December 31, 2020, the market value of the Private Real Estate Portfolio equaled approximately $2.4 billion or 7.8% of the System's assets, which is below the long-term target of 9% as specified in Exhibit 3.

Exhibit 3 - ERS Target Allocation

Asset Class Allocation	Long-Term Target	Min	Max	In Compliance
Private Real Estate	9%	4%	14%	Yes

The total economic exposure of the Portfolio, which includes (i) the market value plus (ii) the currently committed yet uncalled capital of $1. 4 billion, is approximately $3.8 billion or approximately 12.3% of the System's assets. Meketa believes this is appropriate. As with other private market asset classes, the ability to precisely time the actual investment of previously committed private real estate capital is difficult. In order to deploy at the target percentage levels, there is often a need to "over" commit capital, primarily due to timing as managers draw the capital during respective three- to four-year acquisition periods. In addition, the return of capital from investment distributions is also unpredictable. Thus, Meketa does not see the current difference between actual NAV as a percentage of assets, versus targeted percentage, as a concern. On a static basis, the System would have needed to have approximately $330 million, or approximately 24% of the unfunded commitments, more actively invested in real estate to reach the target allocation of 9.0%.

The real estate program has achieved many milestones in support of its role within the overall portfolio. It has committed and deployed capital at a strong and steady pace to closely approach its target allocation. It is currently well diversified by strategy (including core and non-core levels of risk and return), manager, property type and geography. The Portfolio metrics are all within program policy guidelines. Investments have been made on a relatively cost-effective basis compared to market investment management rates, in part due to scale, Staff's existing relationships and willingness to invest earlier in the capital formation process than other investors. Also, by participating in "club funds" and co-investments, Staff has negotiated favorable terms. While many investments remained unrealized, the performance of the Portfolio is meeting expected risk adjusted return expectations and exceeding its benchmark.

The Pacing Plan is prepared as part of the Tactical Plan. It presents potential ranges for both the core and non-core real estate commitment activity required to meet the target allocation during the next five years. With the Portfolio below its long-term target allocation of 9% but well within the target allocation range, Staff is not under undue pressure to continue to commit capital into today's volatile market. Indeed, Staff has the ability to gather additional market data as it becomes available and build conviction around timing and best ideas as the next fiscal year plays out. Data shows that investments made in the vintage years following an economic downturn tend to outperform; having extra dry powder to deploy in FY 2022 and 2023 may advantage the System by providing the opportunity to acquire quality assets at more attractive bases than have recently been available.

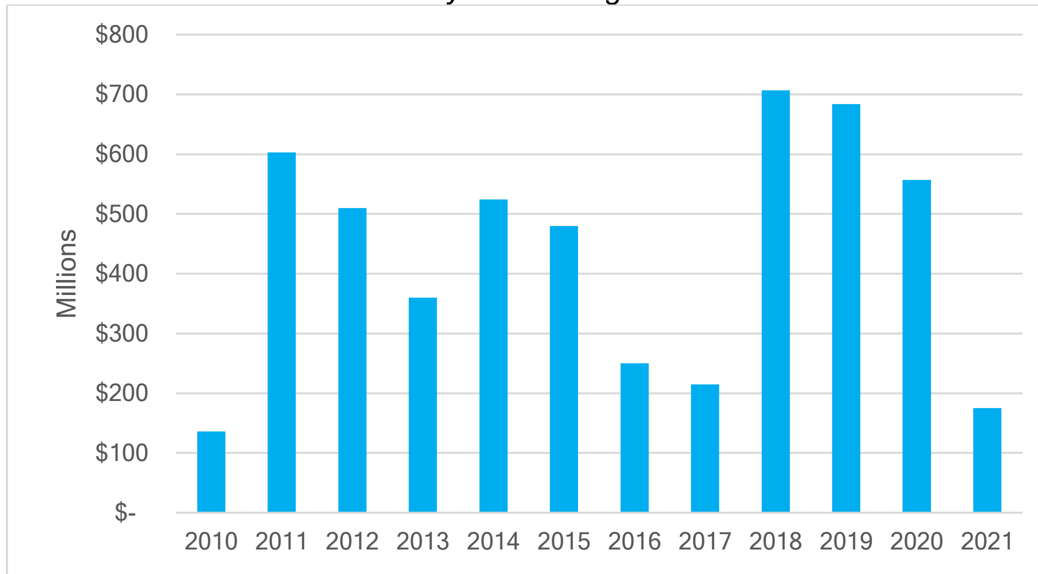
In March 2019 the System approved a 3% allocation to opportunistic credit, of which commercial real estate is a viable option for investments. Any allocation to commercial real estate debt in the opportunistic credit portfolio is considered separate from the Private Real Estate allocation. To date, no investments have been made in commercial real estate private credit; however, this is an area under consideration currently by the real estate Staff for potential commitments.

Portfolio Snapshot

The Private Real Estate Program was initiated in fiscal year 2009. Since then, the System has made 83 commitments, investing approximately $5.3 billion, to open-end funds, closed-end funds, separate accounts and co-investments, through more than 40 third-party managers, as seen in Exhibit 4. The System does not manage private real estate directly but employs a variety of structures in order to enhance returns, maximize efficiency of resources, achieve diversification and manage risk.

Exhibit 4 - ERS Commitment Amounts by Fiscal Year

Fiscal year end August 31



Note: Commitments for FY 2021 through December 31, 2020.

In May 2020, the ERS Board of Trustees approved the Tactical Plan for FY 2021, which included a target of $300 million in new capital commitments, split evenly between core and non-core strategies. As shown in Exhibit 5 below, through December 31, 2020, the System has committed $175 million to three new investments, all of which are non-core strategies. Recent commitments to technology oriented real estate services (data centers) and life sciences strategies have added to the System's stable of resilient real estate portfolios. As seen in Exhibit 6, currently the Portfolio is within risk policy guidelines, although continued attention will be needed to maintain policy compliance across risk buckets.

Exhibit 5 – Fiscal Year 2021 Commitments
Commitments since September 1, 2020

Fund	Risk Category	Commitment
Marcus Capital Partners Fund III	Non-Core	$50,000,000
Principal Digital Real Estate Fund	Non-Core	$50,000,000
Divco West VI	Non-Core	$75,000,000
TOTAL		**$175,000,000**

Exhibit 6- Portfolio in Compliance

Private Real Estate Asset Category	Risk/ Return Strategy Allocation	Allocation as of December 30, 2020	In Compliance
Core	21% to 64%	25.5%	Yes
Non-Core	36% to 79%	74.5%	Yes

The program is diversified by risk profile, investment manager, property type and geography. New investments should be diversification- and/or benchmark-aware but are expected to be more tactical and take advantage of more specific opportunities as they present themselves to complement existing holdings.

Performance and Benchmark

The ERS real estate program contributed a strong net total return of 9.2% over the trailing five years as of September30, 2020; It continued to benefit from solid partnership and strategy selections many of which proved particularly resilient during COVID, increased demand for current yield in the face of insufficient fixed income returns and lower than historic new supply. Per Exhibit 7 below, the System's real estate Portfolio has posted strong performance both gross and net of fees across all time periods, on both an absolute basis and relative to the System's benchmark, outperforming on a net basis the NFI-ODCE by approximately 350 basis points over the trailing five-year period and 190 basis points since inception.

Exhibit 7 – Time Weighted Returns as of September 30, 2020

Time Weighted Gross Total Returns as of September 30, 2020	1 Year	3 Years	5 Years	Since Inception	Inception Date
Core Composite – Gross	4.4	8.0	9.4	11.9	07/01/2010
Non-Core Composite – Gross	2.2	9.9	13.2	17.5	06/30/2011
Texas ERS Total Plan Composite - Gross	2.8	9.3	11.8	14.1	07/01/2010
NCREIF Fund Index-ODCE (VW) (Gross)	1.4	5.2	6.6	10.6	07/01/2010
Over/Under Performance	**1.4**	**4.1**	**5.2**	**3.5**	

Time Weighted Net Total Returns as of September 30, 2020	1 Year	3 Years	5 Years	Since Inception	Inception Date
Core Composite – Net	3.8	7.0	8.3	10.5	07/01/2010
Non-Core Composite – Net	1.3	7.2	9.9	11.6	06/30/2011
Texas ERS Total Plan Composite - Net	2.0	7.1	9.2	11.5	07/01/2010
NCREIF Fund Index-ODCE (VW) (Net)	0.5	4.2	5.7	9.6	07/01/2010
Over/Under Performance	**1.5**	**2.9**	**3.5**	**1.9**	

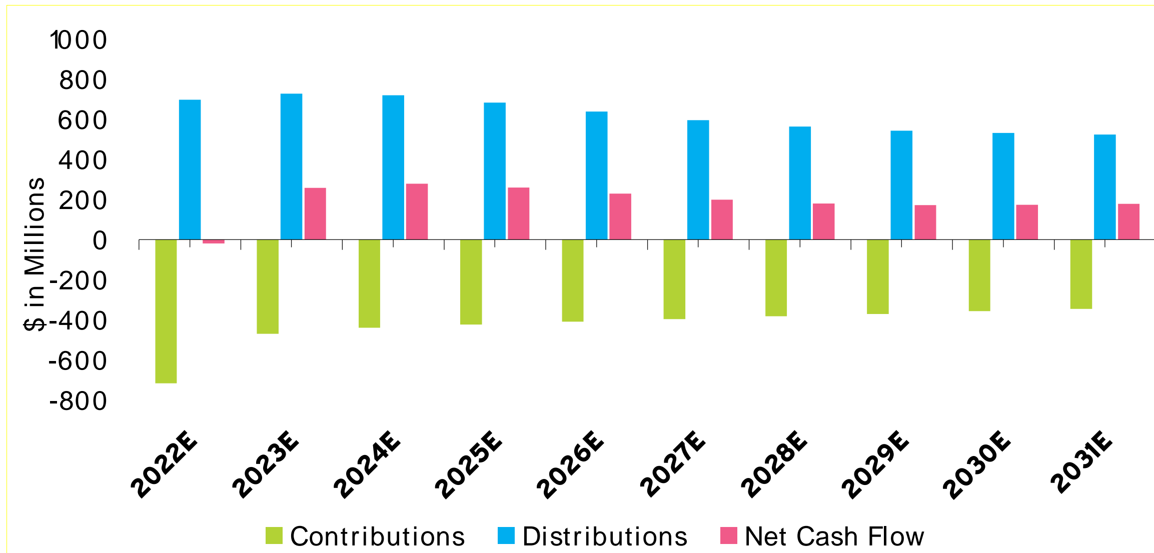
ERS Staff has been able to accomplish significant progress towards growing and rebalancing the System's real estate portfolio to approach the long-term 9% target allocation in FY 2021. Some ground was lost over the last year as real estate transaction activity sputtered at best against the backdrop of surprisingly strong public market performance. However, as mentioned previously, the System may well benefit from having extra room in its private real estate allocation to deploy into post-pandemic markets. Forced rebalancing in other investors' core holdings and distressed situations in the non-core space may present the System with attractive opportunities across the risk spectrum.

Pacing Plan Analysis

The annual pacing plan is a tool to help the System update its estimate of the annual investment volume needed to meet target allocations. The pacing plan is a model based on assumptions and estimates and should be used as a guide rather than a directive. To prepare the pacing plan, data is collected on the Portfolio from the System's managers, both those to whom the System has funded capital and those to whom the System has committed but who have not yet drawn capital. Meketa aggregates these to see a range of what may remain for Staff in a "budget" for new commitments during the next several years. Exhibits 8 and 9 present the estimated cash flows for the System and the commitments needed over the next ten years to approach the target allocation. Input from Staff informs the relative size of the annual commitments within the ten-year pacing plan window. The "budget" also gives consideration to the number of relationships which can be managed by Staff resources and tries to show conviction with larger commitments to proven partners when possible while avoiding unnecessarily high levels of concentration.

The caveats to the pacing plan include, but are not limited to, the number and size of transactions that the managers can acquire; the required capital necessary to execute the individual assets' business plans; the appetite for the purchase of the managers' finished product to effect a "round trip" exit; changes in capital market and property market conditions which change the timing of deployment and return of capital; whether the manager requires extensions of the acquisition period or the disposition period and other factors. Thus, the tool is not intended to be and should not be relied on for any specific quarter's or year's cash flow projections.

Exhibit 8 – Projected Total Cash Flows



Note: Year-end represents December 31st

Exhibit 9- Commitment Schedule

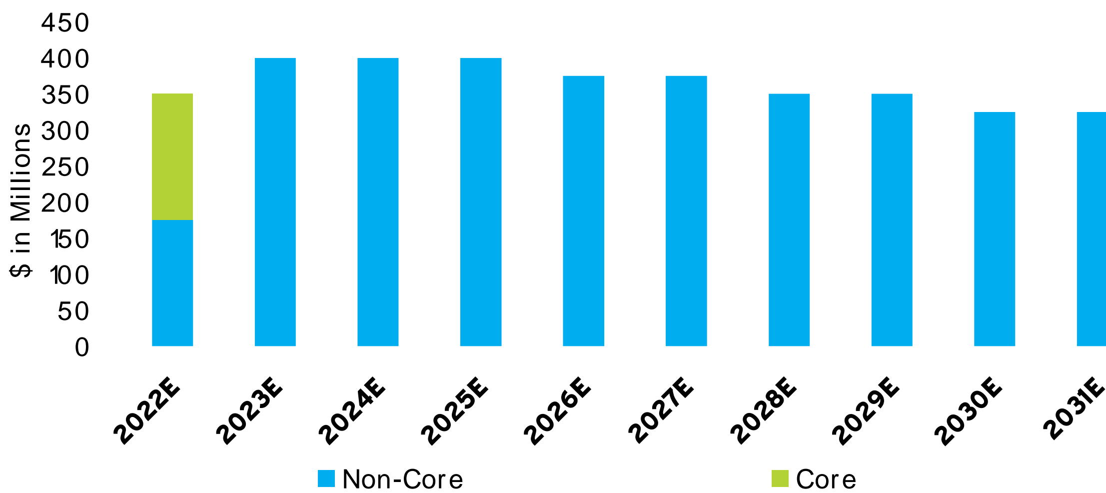


Exhibit 11 - ERS Fiscal Year 2022Tactical Plan

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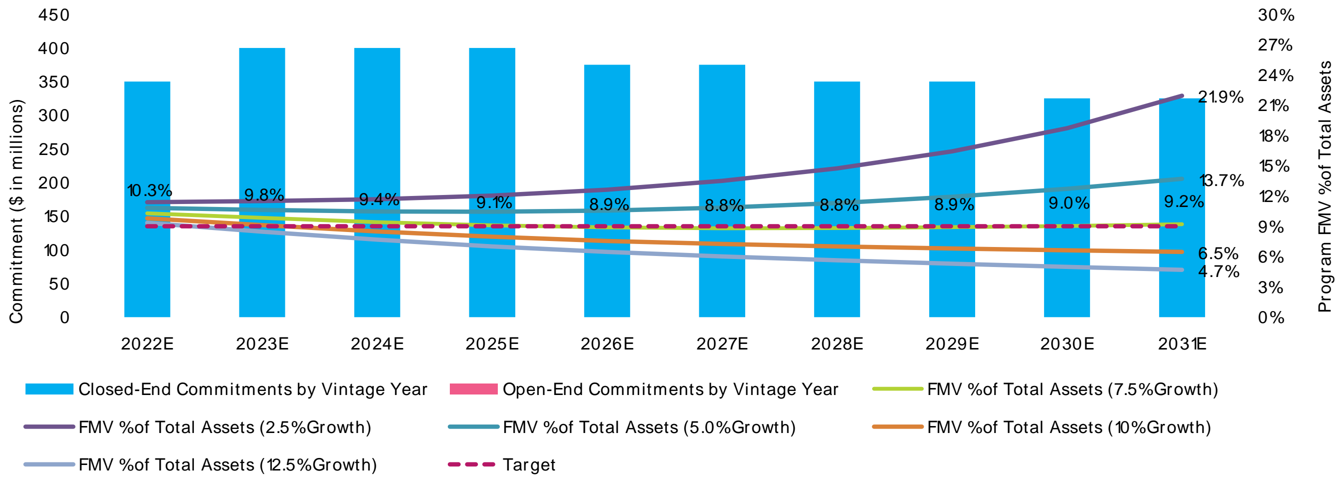
TOTAL	**3-8**	**$350 ($300-$700)**

Meketa expects significantly greater volatility in the markets during the next 12-24 months. This compounds the need for flexibility and ranges around total new commitments for FY 2022 and beyond, as the value of the real estate Portfolio and of the total Portfolio experience historic year-to-year fluctuations.

The following Exhibit 12 displays a sensitivity analysis around the expected real estate allocation relative to total plan growth rates. The purpose of this Exhibit is to demonstrate the projected real estate weight relative to the Systems assets assuming no changes to real estate commitments or cash flows. However, Staff would adjust course (increasing or decreasing commitments) based on changes to the System's total returns and in response to changing market opportunities and concerns.

Exhibit 12 - Real Estate Portfolio Allocation Model

Private Market data as of December 31, 2020



Real Estate Market Outlook and Investment Implications

While real estate fundamentals were sound and leverage levels generally moderate pre-COVID, the unprecedented short-term effects of the pandemic on the operation of and valuation of commercial real estate have been undeniable.

As this memo is being written, the country is on the cusp of a change in Federal Administration, and control of the Congress held by one party. Many of the same “known unknowns” that arose a year ago are still not resolved and may be even less clear. Delivery of vaccines has not occurred broadly yet, and there is currently confusion as to when it is reasonable to expect that it will be widespread. Until the pandemic is brought under control, it is not realistic to expect orderly market transactions at scale. The levels of Federal intervention and stimulus, to individuals, companies and cities and states, is also unknown. We still have, in our view, a period of 12-24 months to endure before investors gain clarity around demand for space, particularly office and retail locations, rent collection, rent abatement, eviction moratoria and other policy impacts, leverage stress, and liquidity. There will be opportunities to pursue. Staff is keenly seeking and investigating them. The long-term nature of the asset class will reward those with patient and disciplined capital. But it may not reward them just quite yet!

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