NEW MEXICO STATE INVESTMENT COUNCIL

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Real Estate Portfolio Investment Policy Statement

May 2018

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I. EXECUTIVE SUMMARY

The New Mexico State Investment Council (the "SIC") has been authorized to allocate a portion of the New Mexico Land Grant Permanent Fund and the Severance Tax Permanent Fund (collectively the "Funds") to a selection of real estate investments.

This Real Estate Portfolio Investment Policy sets forth the objectives, investment guidelines, and processes governing the SIC Real Estate Portfolio. This Investment Policy also sets forth the standard of care governing the management of the Portfolio.

This Investment Policy also sets forth the roles and responsibilities of the Council, the SIC's investment staff (the "Staff"), and the SIC's external consultant(s) (the "Consultant(s)") relating to the oversight and management of the Real Estate Portfolio.

II. MISSION

The Real Estate Portfolio Investment Policy will be executed in a manner that is consistent with the SIC's Mission, Vision and Values.

The SIC's Mission is "to protect and grow the state's permanent endowment funds for current and future generations". The Real Estate allocation will play a key role in delivering on this objective by providing stable and reliable income, capital preservation, diversification and measured growth. Section 3 expands further on the objectives of the allocation.

III. OBJECTIVES OF THE REAL ESTATE PROGRAM

The key objectives of the SIC's Real Estate Portfolio are as follows:

- Generate stable, reliable income;
- Produce an attractive risk-adjusted return;
- Provide diversification of return generation from other asset classes;
- Reduce the overall SIC portfolio volatility;
- Provide an inflation hedge; and
- Capital preservation.

IV. PORTFOLIO ALLOCATION

The long-term target allocation for Real Estate is 12% of the Funds' assets. The table below sets out the broad allocation ranges by risk classification within the real estate portfolio. The target percent of each Real Estate Portfolio Component is based on achieving the Overall Target Allocation. The portfolio may be outside the stated ranges as the Real Estate Portfolio is built out.

Real Estate Risk Component	Investment Characteristics	Percentage of Real Estate	Overall Target Allocation
Core	• Stabilized, income-producing • Equity and equivalent • Well-leased • Modest capital expenditures • Minimal obsolesce • Primary markets • International investments • Leverage 50% or less (generally less than 35%) • Longer investment holding period • Senior real estate debt	40% - 70%	12%
Core-Plus	• Same as Core, but with more vacancy (up to 25%); more near-term lease expirations; and more required capital improvements		
Value-Added	• Leasing risk • Partial obsolescence • Rehab risk • High yield net lease • Forward commitments / New construction • Ownership restructuring and recapitalization • All markets • International investments • Leverage 40%-65% • Shorter hold than Core/Core-Plus • Senior mezzanine real estate debt	30%-60%	
Opportunistic	• Significant redevelopment risk • International investments and more non-OECD exposure • High leasing risk • Development • Functional/Economic obsolescence • Entity investments • Leverage 65%+ • Shorter hold than Value Added • Junior mezzanine real estate debt		

In general, the Core and Core-Plus total exposure will be more heavily tilted towards Core, whereas the Value-Added and Opportunistic components will be approximately balanced, recognizing that investment decisions are in the hands of the Investment Managers and the SIC has very limited control over risk other than by selecting funds based on the Investment Managers' stated risk tolerance.

A. Portfolio allocation by Real Estate Property Type

The SIC intends to construct a portfolio of investments that are diversified by property type. The SIC prefers to establish broad ranges for each property type. The ranges will ensure prudent diversification among the property types but will enable the SIC to capitalize on opportunities caused by shifts in the real estate and capital markets and allow for strategic under- and over-weights to property types. The ranges are intended to provide flexibility for overall management of the portfolio and to allow a more tactical approach when strategies of interest are in and out of favor. Again, the portfolio may be outside the stated ranges as the Real Estate Portfolio is built out.

The benchmark for property type diversification is the NCREIF (National Council of Real Estate Investment Fiduciaries) ODCE (Open Ended Core Diversified Equity) index. The ODCE index is comprised of contributing U.S. open ended core funds pursuing diversified strategies. The following represent the ranges for property types in the Strategic Portfolio:

Property Type	Range *
Office	ODCE +/- 15%
Industrial	ODCE +/- 15%
Multifamily	ODCE +/- 15 %
Retail	ODCE +/- 15 %
Hotels	ODCE +/- 15 %
Other (specialty and other)	ODCE +/- 15 %

* For example, a 25% weighting to a particular property type in the NCREIF ODCE Index would allow a range of 10% to 40% in the Plan.

B. Performance Benchmarks

The performance benchmark for the real estate portfolio is the NCREIF ODCE Index, net of fees, over a market cycle. While the ODCE index is widely used by institutional investors, there are limits on the inclusion of value added and opportunistic assets and there are no international investments are in the index.

In addition to the performance benchmark, the real estate portfolio will be structured with an aim to produce a level of aggregate return that is accretive to attaining the targeted rate of return to the SIC over the long-term, while still satisfying the goals and objectives for including real estate in the SIC's investment portfolio. Currently, the SIC's target rate of return is 7.0% for Land Grant Permanent Fund and 6.75% for the Severance Tax Permanent Fund.

V. PORTFOLIO CONSTRUCTION

A. General principles

Portfolio construction will be guided by the following general principles:

- Diversification between core/core-plus and value-add/opportunistic strategies;
- Asset class allocations based on return and risk profile over a full market cycle;

- Market opportunities and conditions;
- Geographic availability of various sub asset classes;
- Timing of various strategies being in market versus portfolio needs;
- Building sustainable and aligned relationships with managers and other investment partners and leveraging those relationships across strategies; and
- Securing governance rights (e.g., Advisory Board seats) to maximize the protection of the Funds' investments, where possible.

B. Specific portfolio construction parameters

The following section discusses specific portfolio parameters in more detail that are intended to apply to the Real Estate portfolio at an aggregate level.

1. *Core/core-plus ("Core") strategies versus value-add/opportunistic ("Non-Core") strategies*

Core and Core-Plus investments will provide the Portfolio's foundation exposure. In general, these investments have the objective of generating a meaningful (but not necessarily majority) portion of the total return from current income (i.e., cash yield), and the balance from capital appreciation. The risk-return profiles for core and core-plus investments represent the low- to mid-range.

In general, value-add and opportunistic investments will target higher risk-return profiles with little or no current income and generate the majority or all the total return from capital appreciation.

The Council recognizes that pure core and core-plus exposure is difficult to execute outside of direct investments and often managers will pursue both core/core-plus as well as value-add/opportunistic investments within their portfolios. Further, depending on the asset class and the cycle, there may be other reasons to allocate differently across the risk spectrum. A manager may not be considered for inclusion in the Real Estate Portfolio if SIC staff, in consultation with its Consultant(s), believes the proposed commitment would result in an over- exposure to risk parameters.

As stated above, it is expected that Core and Core Plus will make up 40-70% of the total real estate portfolio, while Value-Added and Opportunistic will make up 30-60%.

2. *Asset Type Diversification*

The guidelines for diversification by property type are set forth in the table in Section 4. The ranges will ensure prudent diversification amount the property types but will enable the SIC to capitalize on opportunities caused by shifts in the real estate and capital markets. The overall Real Estate Portfolio will seek diversification by asset type, perceived risk, revenue drivers, and geography to mitigate portfolio volatility. The SIC recognizes that real estate assets are relatively illiquid and individual assets are not of uniform size and quality. Furthermore, the Real Estate program will be implemented primarily through vehicles where the SIC has limited control over the asset type distribution other than through selection of the strategy itself.

3. *Geographic Diversification*

The Real Estate Portfolio is intended to be diversified globally. Not less than 60% of the portfolio will be in the U.S. While there will be no specific constraints on diversification across U.S. cities and regions, Staff and Consultant(s) will endeavor to maintain prudent diversification by geography and economic drivers, recognizing that in most cases the commingled fund manager has broad authority to make investments in geographies that they consider advantageous to their strategy.

Not more than 40% of the Real Estate Portfolio will be invested outside of the U.S., and not less than 80% of the 40% cap on non-U.S. investments will be in developed economies (generally, those member nations in the OECD). Investments in emerging economies will be permitted, provided that the combined total exposure to non-OECD regions remains below 8% of the Real Estate Portfolio (measured by market value exposure).

4. *Investment Concentration*

The Funds will diversify to reduce the impact of a single investment on the performance of the Real Estate Portfolio. In order to mitigate the risk of a single investment, the amount of equity that may be invested in a single investment is limited to no more than 5% of the overall total long term Real Estate Portfolio Target, that is, 5% of the Real Estate Allocation (which, in turn, is 12% of the Fund's total NAV). "Single investment" is defined as any: a) direct investment or co-investment in a single underlying asset; or b) any commingled investment vehicle which focuses on a single asset. Assets held in commingled investment vehicles, such as open-end or closed-end funds, partnerships, and other investment vehicles which hold or intend to hold multiple investments are not considered a "single investment".

In addition, SIC staff and its Consultant(s) will review each manager's proposed underlying investment concentration limit in considering selection of the manager and the strategy. Typically, SIC prefers managers to limit targeted concentration to any single asset within their portfolio to less than 20% of the fund strategy.

5. *Manager Diversification*

Manager relationships are very important in the Real Estate class due to the difficulty and cost of accessing transactions, and the illiquidity of most of the fund structures. The SIC will, however, take a measured approach to its concentration to individual manager/fund sponsor or its affiliated entities.

As a result, the SIC will limit a single fund sponsor to managing no more than 30% of the total Real Estate Program (by commitment), which represents approximately 3.6% of the overall SIC portfolio.

The Real Estate manager selection process will also consider any current manager exposures outside the Real Estate portfolio that may exist, however, no specific cross-asset class limits will be established.

6. *Leverage*

The use of leverage by fund sponsors is particularly relevant to the Real Estate allocation and will be monitored by the SIC Staff and Consultant(s) on a quarterly basis to avoid incurring imprudent risks. The Real Estate Portfolio leverage in aggregate is not intended to exceed 65% (by market value of debt to Gross Asset Value) at any quarter end measurement date. To ensure compliance with this limitation, no manager will be selected for the portfolio if the addition of the commitment at maximum permissible leverage would cause the Real Estate Portfolio to exceed this limitation.

In general, leverage in the core and core plus portfolio will be less than 50% and less than 80% in the value-add and opportunistic portfolios. Note that the overall leverage cap of 65% could be breached in a market dislocation. SIC Staff and its Consultant(s) will review each manager's intended use of leverage at the fund level within Real Estate strategies to ensure its appropriateness in the market cycle.

7. *Commitment Sizing and Governance Rights*

Governance Rights and voting power are important considerations in sizing Real Estate investments due to their lack of liquidity. Fund strategies in Real Estate typically vary in size from $250 million dollars to multi-billion-dollar funds.

For Real Estate strategies, the SIC will generally seek to be less than 25% of a comingled fund (excluding GP commitment) as a method to ensure the strategy is more broadly supported by the institutional investment community. However, this limit will not apply to club transactions. In addition, for larger Real Estate fund strategies, the SIC will consider sizing its commitment so it is positioned to secure an Advisory Board seat to enhance the protection and value of the Funds' investment. Advisory Board seats enhance the visibility and monitoring ability for Limited Partners on the General Partner's strategy and enable input into a range of decisions the General Partner may make from time to time. The Advisory Board typically also plays a key role if the Key Man clause is triggered or in the event of a suspension of the Investment Period and in some cases bankruptcy of the General Partner.

It may not always be possible or practical to secure an Advisory Board seat, thus other factors that will be considered in considering the investment include considering the extent of the SIC's relationship with the Manager, the actual voting power in the fund, the uniqueness of the strategy, and the extent of the market opportunity.

The following table summarizes the key parameters for portfolio construction discussed above:

Investment Allocation	
U.S.	**>60%**
Developed (OECD)	**<40%**
Emerging (Non-OECD)	**<8%**
Investment Concentration	**No greater than 5% of the Real Estate Portfolio in a single asset**
Manager Concentration	**No greater than 30% of Real Estate Portfolio**
Leverage	**65% maximum in**
Single Commingled Fund % Interest	**25% maximum**

C. Program Implementation

The Funds shall acquire exposure to Real Estate Assets primarily through commingled fund vehicles (open end and closed end) and, to a lesser extent, co-investments, club structures, joint venture limited partnerships and separate accounts. The appropriate structure shall be determined by the Council, Staff, and Consultant(s) in developing and managing the performance and liquidity of the Real Estate Portfolio.

For purposes of this Real Estate Portfolio Investment Policy Statement, “real estate” includes, but is not limited to debt and equity investments where the underlying asset is or is intended to be rent-producing or for-sale real estate, including, but not limited to: office, industrial, retail, for rent multi- and single-family residential, storage, student housing, hotel, marina, medical office, lab, elder care, manufactured/mobile home park and recreational vehicle park.

The real estate investments of the Funds may be either direct (i.e., interests in a real estate property asset, such as an office building) or indirect (i.e., interests in owning and operating entities such as REITs and REOCs, or investment through commingled funds). Direct investments may include those identified by (1) investment managers granted separate account allocations or (2) the Staff with advisory assistance from the Consultant or a Staff-approved investment manager.

Commingled fund investments by nature are discretionary relationships, where the sponsor or manager of the fund has ultimate control over the investment decision-making process and the investor typically has limited rights with respect to the management of the commingled fund. The term for a traditional commingled fund in the real estate universe ranges from 10 to 20 years and may also be open ended.

The table below identifies the most common methods of access among the permissible investment vehicles for the Real Estate Portfolio.

Real Estate Portfolio Implementation			
Permitted Investment Vehicles			
Private Fund	**Direct / Indirect**	**Listed Public Companies**	**Other Special Partnerships and Trusts**
- Unlisted - Closed-End or Open-End - "Club" structures	- Direct ownership of Real Estate Assets - Joint venture - Co-invest interest - Separate account (discretionary or non-discretionary) - Real estate operating companies	- Engaged in real estate-related business(es) or assets (i.e. Real Estate Investment Trusts) - Individually or collectively listed (e.g., ETFs)	- Publicly traded - Privately traded

D. Risk Management

Consultant(s) and Staff shall monitor diversification of the portfolio and fund performance quarterly through the performance measurement process, and periodically report to the Council on the policy items below, as provided for under Section 6.B.

VI. PORTFOLIO OVERSIGHT

The portfolio oversight procedures set forth below are divided into roles and responsibilities, and reporting.

A. Roles and Responsibilities

The Real Estate portfolio will be planned, implemented and monitored under the oversight of the full Council, with the coordinated support of the Investment Committee, Staff, fund sponsors and Consultant(s). The description of the major responsibilities of each participant is set forth below.

1. Council and Investment Committee

The role of the Council is to ensure that the assets of the Funds are effectively managed in accordance with the laws of the State of New Mexico and the Investment Objectives and Policies of the Council. The responsibilities of the Council and Investment Committee are listed below.

- Establish the objectives and risk management policies for the Real Estate Portfolio. The Council will perform this role by reviewing and approving, or amending and approving as appropriate, the Real Estate Investment Policy submitted by SIC Staff or its Consultant(s) from time to time.

- Review and approve, or amend and approve, the Investment Plan for Real Estate.
- Review the performance of the Real Estate Portfolio and the fund sponsors. Review compliance of the Real Estate portfolio with the objectives and policies established by the Council/Investment Committee. For this review, the Consultant(s) will provide the Council and Investment Committee with quarterly Performance Measurement Reports.
- Review and approval all new investments.

2. Staff

The Staff reports to the Council and its role shall be to monitor the activities and work in conjunction with the Consultant(s) to provide input to the Council and Investment Committee on all such matters concerning Real Estate investments. The Staff's role and responsibilities shall include the following:

- Prepare the Real Estate Investment Policy and Annual Investment Plan in consultation with its Consultant(s) and submit these to the Council and Investment Committee for approval;
- Work with the Consultant(s) to evaluate and recommend commingled fund, co-investments, club, joint venture, direct and separate account investments to the Council and Investment Committee;
- Work with the Consultant(s) to monitor fund sponsors and issue Requests for Proposals (RFPs) or Invitations to Bid (ITBs) for manager searches where relevant;
- Work with the Consultant(s) to develop specific capital allocation recommendations contained in the Investment Plan;
- Attend Limited Partner Advisory Committee ("LPAC") and similar committee meetings and vote on matters brought to the LPAC for consideration;
- Subject to review by counsel and/or consultant(s) where appropriate, amend fund documents as requested by the general partner;
- Prepare funding procedures and coordinate the receipt and distribution of capital with the fund sponsors with the assistance of Consultant(s); and
- Monitor the performance of the Real Estate Portfolio, its fund sponsors, Consultant(s), and the compliance of the Program with the investment planning and management documents and this Policy.

3. Fund Sponsors

Fundamentally, the fund sponsors will acquire, sell and manage Real Estate investments consistent with the respective documents governing the relationship between the SIC and fund sponsors and any other program documentation developed by Consultant(s) and/or Staff and approved by the Council and Investment Committee. The fund sponsors shall provide the Council and Investment Committee, Staff and Consultant(s) with such information as may be required to properly monitor the fund sponsors and its investments.

A fund sponsor may serve the SIC as a fiduciary or may serve as fiduciary to the pooled vehicles in which the Funds invest. Fund sponsors are required to perform this role in compliance with the investment planning and management documents created by the SIC. Each quarter the fund sponsors shall provide performance measurement data in the form and substance as required by the SIC and its Consultant(s) and in compliance with this Real Estate Investment Policy.

4. Consultant(s)

While the Staff has the active day-to-day role of managing the Real Estate Portfolio, the Consultant(s) works for and reports to the Council. Thus, the Consultant(s) shall perform the following services:

- Work with Staff to prepare the Real Estate Investment Policy and Investment Plan and provide the Consultant(s)'s review and recommendation to the Council, Investment Committee and Staff;
- Work with Staff to develop shortlists of fund sponsors and perform searches for fund sponsors and other professionals, and report on such searches with Staff to the Council and Investment Committee as required under the applicable search policy;
- Work with Staff to evaluate and recommend commingled fund, joint venture, co-investment, club and separate account investments to the Council and Investment Committee;
- Present recommended investments to the Council Investment Committee and State Investment Council;
- Prepare quarterly Performance Measurement Reports for relevant measurement periods for assigned components of the Real Estate Portfolio;
- Review and monitor the investment activity in the Portfolio and the performance of the fund sponsors and the Portfolio; and
- Perform such other duties as contemplated by the applicable consulting services agreement.

The Consultant(s) will promptly advise the Council, Investment Committee and Staff of any material changes in the capital markets that would materially influence its Real Estate Investment Policy or Annual Investment Plan. The Consultant(s) will inform the Council, Investment Committee, and Staff of any significant changes with respect to the fund sponsors that are likely to influence the fund sponsors' ability to continue to provide services to the Funds. The Consultant(s) shall provide the Council, Investment Committee, and Staff with relevant research materials as needed or as directed by the Council/Investment Committee or Staff. The Consultant(s) will serve the New Mexico State Investment Council as a fiduciary to the Funds.

B. Reporting

The Council, Investment Committee and Staff will receive reports from its fund sponsors and Consultant(s) that will contain information to enable the SIC to evaluate the performance of the Real Estate Portfolio.

1. *Quarterly Report*. The fund sponsors will submit to the Council, via Staff, and Consultant(s) its quarterly report within 60 days of the end of each quarter and 90 days of year end. The report will record the performance for the relevant measurement periods, cash flow information, fees, costs and market value. The Consultant(s) shall report any major issues to the Council, Investment Committee and Staff.

2. *Audited Annual Financial Statements*. Each fund sponsor will submit a consolidated annual financial statement to the Council, via Staff, and Consultant(s) within 120 days of the end of the fourth quarter.

3. *Performance Measurement and Portfolio Analytics Report*. Following each quarter, the Consultant(s) shall submit to the Council and Staff a performance measurement report, which contains quantitative performance of the Real Estate Portfolio using data as provided by the fund sponsors.

   The Consultant(s) will submit its portfolio management report to the Council, Investment Committee, and Staff within 90 days of the end of the quarter or 10 days after last manager submission (latter of). It will evaluate the compliance of the Real Estate Portfolio with the Policy and Investment Plans; the performance of the Real Estate Portfolio and its fund sponsors for the relevant measurement periods and relative to indices and benchmarks; a statement of significant initiatives being undertaken; a statement of relevant capital market information; and a statement of significant events in the Real Estate program.

4. *Other Reports*. The Consultant(s) and fund sponsors shall provide, in a timely manner, such other reports as the SIC may determine useful to the administration of the Real Estate Portfolio. The fund sponsors shall provide reports and other disclosures as set forth by the documents governing the Funds' investment with each fund sponsor.