

LIQUIDITY AND PRICING CONSIDERATIONS RELATED TO COVID-19

Professional Standards Briefing

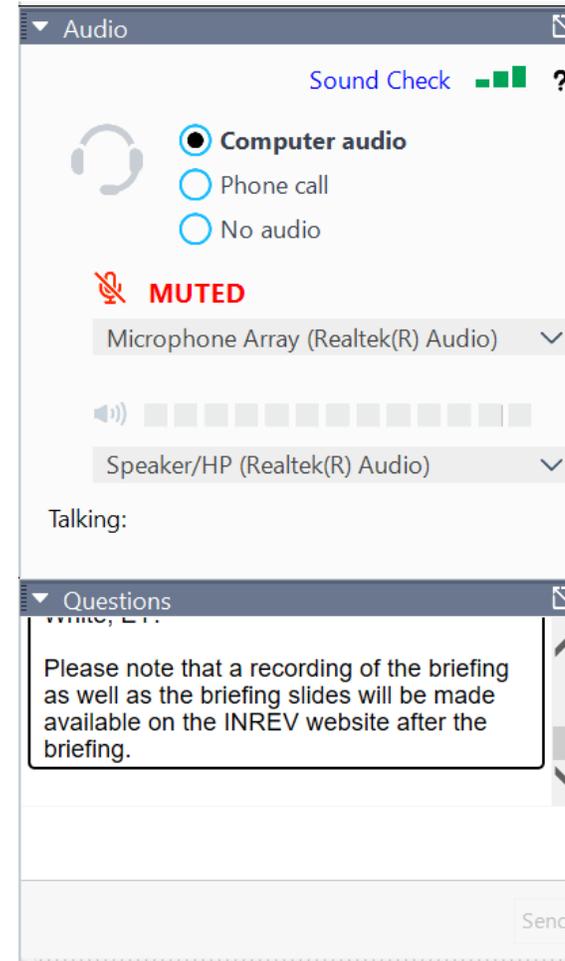
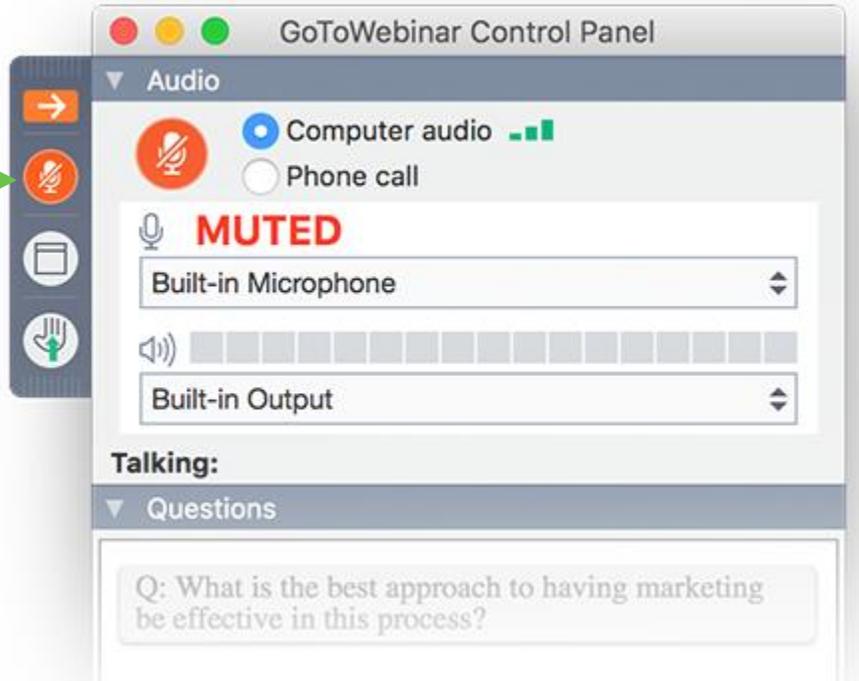


INREV Online Briefing

2 April 2020

Housekeeping

Mute Mic



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Recording of the webcast available after the session inrev.org

The New Wave of Market Challenges

Investment managers are faced with increased pricing uncertainty related to COVID-19

Should they or shouldn't they keep vehicles open for trading? How do they ensure prices remain fair?

Earlier this week, Reporting Briefing on disclosures and INREV NAV.

Scope of this webinar:

- Practical liquidity and pricing considerations; not prescriptive guidance
- Regulators guidance always takes precedence
- INREV AREF open end fund pricing recommendations on governance – first preview

Speakers

- Thomas Kallenbrunnen, Managing Director, PGIM Real Estate
- John Ravoisin, Partner at Audit and Advisory Services, PwC
- Nick Brown, Finance Director, M&G Real Estate
- Robert White, Partner and Real Estate Assurance Leader, EY
- Constantin Sorlescu, Director of Professional Standards, INREV

Considerations for institutional open end vehicles

- Remaining open or suspending trading is normally a **case-by-case** management decision
- Vehicles that can service redemptions and remain open should set out appropriate disclosures to ensure **full transparency and fairness** on pricing
- Under exceptional circumstances, suspending trading temporarily allows for **balancing of interests** between leaving, remaining and prospective investors
- Active use of secondary markets may **stabilise** vehicles with increased redemption requests



To trade or not to trade

Management decision to be made on a case-by-case basis for any given vehicle based on:

- nature and type of the real estate portfolio
- fund documentation
- regulator guidance which should always take precedence

Decision to remain open and trade in an uncertain environment should go alongside:

- robust governance
- additional disclosure regarding property valuation, pricing changes and assumptions used
- full transparency as a principle

Suspensions are not a bug – they are a feature

Only under exceptional circumstances:

- “conditions beyond the control of the affected party (akin to a force majeure clause)”
- Redemption window should only be extended temporarily, until the shock of the crisis and its effects become manageable, by a maximum of two years

Recommendations for Vehicle Documentation

- Clearly define the nature of exceptional circumstances in the fund documentation
- If the redemption window is extended on these grounds, explain these transparently to the investors

Consistency and transparency

- Be consistent between terms and rights of redemptions and subscriptions
- Ensure timely and relevant information to investors on the liquidity planning of the vehicle
- If you decide to remain open, prioritise drawdown of existing capital commitments to service current redemptions and clarify implications with the investors who have committed to subscribe to the vehicle
- Active use of secondary markets may stabilise funds with increased redemption requests

INREV Liquidity Guidelines

INREV Guidelines are designed to help in case of material market changes

Existing guidelines on Redemptions of Equity

- Disclose rights to use discretion in setting the redemption price or the assumptions adopted by others in key components of the redemption price (e.g., property valuation)
- Disclose all its rights to defer payment of redemption proceeds
- Communicate to investors without delay any changes to normal practice as a result of the exercise of these rights and provide reasons
- In the event a manager exercises these rights, the redeeming investors should have the right to withdraw their redemption request within a defined period

Reporting on liquidity issues

- Additional disclosures during these exceptional market circumstances
- Describe and analyse principal risks:
 - Market risks
 - Credit and counterparty risks
 - **Liquidity risks**
 - Interest rate risks
 - Operational risks
- Comment on the overall financing structure of the vehicle
- Describe the vehicle's current key financing ratios and current compliance with covenants
- Describe the vehicle's overall financing income and charges



How to provide sufficient information on INREV NAV

- Carry on accounting for INREV adjustments
- Clarify INREV NAV calculation in case of material uncertainty
 - Fair value of assets and liabilities, particularly investment properties
 - Liquidity, including cash sources and uses
- The disclosures are expected to be clear and transparent to allow investors to understand the impact of current market conditions on the performance of the vehicle



Q&A

INREV – AREF Open End Fund Pricing project

Background Information

- INREV and AREF have jointly developed recommendations on best practice governance over the operation and maintenance of pricing models which are due to be issued for consultation in Q2
 - Not Guidelines or Codes of Practice but emerging thinking on best practice
 - Don't replace regulatory or legal obligations
- The proposals that relate to pricing policy under **exceptional market circumstances** are released early
- The aim is to aid investors and managers of open end real estate investment vehicles to respond to the impact on fund operations of COVID-19

INREV – AREF Open End Fund Pricing project

Pricing in dislocated markets – Recommendations for investment managers

- Adjust pricing where markets are dislocated, to ensure there is no material transfer of value between remaining and exiting investors
- Recommendation against redemption penalties as a mechanism to penalise exiting investors
- The interests of the majority take precedence where there is a conflict of interest between remaining and exiting investors that cannot be resolved

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Pricing in dislocated markets - Recommendations for investment managers

- Have consistent governance processes across a Manager’s platform that apply to pricing under exceptional circumstances - a “house policy” . Any change in pricing policy decisions should be consistent with that house policy
- Include in the constitutional documents provisions to enable the investment manager to take appropriate and pre-determined actions to amend pricing mechanisms during periods of exceptional circumstances
- Disclose promptly to investors when a temporary change has been made to its pricing mechanism and the nature of the amendment
- Management Boards and Independent Representatives should scrutinise actions take on pricing as IACs may not be able to respond sufficiently quickly and may also be conflicted

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Secondary Markets

- Information should be disclosed on the published NAV, quoted prices in the primary market, any unamortised transaction costs and any significant asset or liability incorporated within NAV that is not fair valued and may otherwise distort the secondary market price

Issue of units for less than the normal set offer price

- Existing investors should have the right of first refusal, proportionate to their existing holding. If the equity raise target is not reached, third parties can then be invited to subscribe
- Relevant disclosures should be provided to investors to enable them to fully evaluate the implications

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Pricing when closing an investment vehicle

- Include provisions so appropriate and pre-determined actions to amend pricing mechanisms are possible
- Consult firstly with independent representatives before the decision to close a vehicle is finalised. IAC should only be consulted once a vehicle has been suspended to avoid conflicts of interest
- Costs of closing a vehicle should be borne by all investors and the pricing mechanism should be adjusted as necessary to ensure this occurs
- Full disclosure of the investment manager's future proposals for the vehicle and proposed amendments to the pricing policy should be made available promptly to all investors when a vehicle is being closed

Q&A

Concluding remarks

- Remaining open or suspending trading - normally a case-by-case management decision
- Ensure full transparency and fairness on pricing
- Under exceptional circumstances, suspending trading allows for balancing of investors' interests
- Secondary markets can help



INREV is here to support

The INREV logo, consisting of the letters 'INREV' in a bold, blue, sans-serif font. The logo is positioned in the bottom right corner of the slide, partially overlapping a stylized illustration of a building facade with windows and potted plants.

INREV