Blackstone Fiddles as BREIT Burns

By Craig McCann and Regina Meng

Introduction

In December, we argued that Blackstone Real Estate Income Trust ("BREIT") smoothed and inflated its reported returns for years, leading to large investor inflows.[1] We predicted that a run on the bank had started because of Blackstone's prior conduct, leaving it with two very bad options. BREIT could honor redemption requests at posted NAVs and see its NAV cut in half as the NAV mispricing became concentrated in remaining shares or it could limit redemptions for the foreseeable future as it slowly adjusted its reported NAV down to truthful values.

To many investors, advisors and finance columnists, Blackstone has the legendary Midas touch. Before we advance our argument based on recent developments, let's review the smart money's unanimous opinion of BREIT.

The 100 largest, actively managed, domestic stock mutual funds' portfolio managers manage $3 trillion. They search for mispriced assets and compete for investors by maximizing their net risk-adjusted returns. These portfolio managers can and do hold non-traded assets. These portfolio managers can and do hold REITs; collectively they hold $30 billion of REITs. **What the 100 largest actively managed domestic stock funds don't do is hold a single share of BREIT!** There is no trace of BREIT in the quarterly portfolio holdings for 2020, 2021 and 2022 of these 100 largest actively managed funds. BREIT is not just underweighted in the 100 largest actively managed stock funds - its portfolio weight is 0.0000000% of $3 trillion. Not even one of the 100 largest actively managed stock funds held a single share of BREIT.

If BREIT was a real estate juggernaut distilling Blackstone's special expertise, rather than a marketing success built on half-truths, these 100 actively managed stock funds would put some of their $3 trillion - $30 billion of which is invested in REITs - into BREIT. The market test confirms that BREIT is a bad investment. The facts we lay out below convince us both that BREIT is a bad investment and its Advisor and management lack basic candor.

[1] *Blackstone's Choice: Let BREIT Crash or Collapse It Slowly?* available here.

What We Learned Since December

After four months, we have significantly more information on Blackstone's crisis management strategy. Blackstone appears to have chosen to collapse BREIT slowly. Rather than being honest about its prior misleading public statements, Blackstone has doubled down on its obfuscation - obfuscation so complete that investors should not accept anything Blackstone and BREIT state as truthful.

We identify at least seven areas where Blackstone has lacked candor.

1) **Performance reporting.** BREIT's 10-Ks include a statement that its monthly NAV calculations can only be used to determine the price at which BREIT will redeem shares or sell shares are not reliable for calculating historical performance. Despite this clear admission, BREIT and Blackstone's SEC filings prominently include BREIT returns calculated based on the unreliable NAV.
2) **Performance touting.** BREIT's website continuously displays historical performance based on its unreliable NAV calculations on a page entitled simply "Performance". Many of BREIT and Blackstone's press releases and presentations include strong, unqualified statements about BREIT's historical performance based on NAVs BREIT's 10-Ks state are not a reliable basis for calculating historical performance.
3) **Asset and Performance Incentive Fees** Blackstone has received $4.2 billion in asset management and performance incentive fees based entirely on its calculation of BREIT's NAV. Blackstone justified nearly $2 billion in performance incentive and asset management fees in 2021 alone by claiming a 30% return for the year based on a NAV which BREIT's 10-Ks states can not be used to calculate historical performance.
4) **NAV calculations:** BREIT failed to disclose the critical revenue growth assumption - assumption just as critical as the discount rate and cap rate "key" assumptions it disclosed for 72 months - until November 2022 as things appear to be coming off the rails. Curiously, last month, BREIT amended its Registration Statement to substantially eliminate the claimed role of an independent valuation advisor.
5) **2022 Returns.** BREIT's 2022 monthly returns were smooth and positive while traded REITs' prices dropped 29%. BREIT falsely attributed this yawning gap to its

concentration in residential and industrial property sectors which fell by roughly the same amount in 2022 as the traded REIT market as a whole. BREIT also attributed its differential 2022 returns to traded REITs being oversold as a result of retail investor sentiment. As we explain below, this explanation doesn't hold up to minimal scrutiny.

6) **Redemptions** In December 2022, for the first time BREIT imposed redemption limits that it had waived three times before. BREIT chose to not enforce limits until BREIT's NAV was likely significantly overstated. Contrary to its justification for limiting redemptions, BREIT could easily have met redemptions without selling properties but, if the NAV was overstated, redeeming shareholders at stated NAVs would increase the mispricing in remaining shares.
7) **University of California Investment** Blackstone made a sweetheart deal with the University of California, effectively selling the University of California BREIT shares at a 20% discount. Blackstone would not make this deal if it was confident in BREIT's NAV and could defend the BREIT franchise without paying $1 billion. BREIT strategically announced the University of California investment to deflect attention from its announcement on January 3, 2023 that BREIT was only meeting 4% of the December 2022 redemption requests.

1) BREIT and Blackstone Use Baseless Returns in their SEC Filings

Each year, BREIT's 10-K states that its monthly NAV calculations can only be used to determine the price at which BREIT will redeem shares or sell shares during the current month and that the reported NAVs are not reliable for calculating historical performance. Page 16 of BREIT's December 31, 2022 10-K includes the following passage.[2]

> ***NAV calculations are not governed by governmental or independent securities, financial or accounting rules or standards.***
> The methods used by our Adviser and State Street or its affiliates to calculate our NAV, including the components used in calculating our NAV, are not prescribed by rules of the SEC or any other regulatory agency. Further, there are no accounting rules or standards that prescribe which components should be used in calculating NAV, and our NAV is not audited by our independent registered public accounting firm. <u>We calculate and publish NAV solely for purposes of establishing the price at which we sell and repurchase shares of our common stock, and you should not view our NAV as a measure of our historical or future financial condition or performance.</u> The components and methodology used in calculating our NAV may differ from those used by other companies now or in the future. [<u>emphasis added</u>]

[2] www.sec.gov/ix?doc=/Archives/edgar/data/1662972/000166297223000030/breit-20221231.htm

BREIT's disavowal of its NAV for calculating historical performance is unambiguous.

- Blackstone is not using a methodology prescribed by the SEC or any regulatory body.
- Backstone is not adhering to any accounting rules or standards.
- BREIT's NAV is not being audited by an independent public accounting firm.
- Blackstone's calculates BREIT's NAV solely to determine the price at which it will redeem shares and at which it will sell new shares.
- Investors can not rely on BREIT's NAV to measure historical performance.

Despite BREIT's statement about NAV not being reliable for calculating historical performance, Blackstone and BREIT prominently include BREIT returns calculated based on the NAV in their SEC filings.

BREIT reported historical performance, based on NAVs which BREIT knows are not reliable for that purpose, to investors through the SEC every month for 89 months on Form 424(b)(3). BREIT's Form 424(b)(3)s lead with a section reporting the prior month's historical performance based on the NAV Blackstone calculated. For example, BREIT's 424(b)(3) filed October 19, 2022 reads:[3]

Portfolio Update

For the month ended September 30, 2022, BREIT's Class I NAV per share increased from $15.09 to $15.11. The total return for Class I shares in September was 0.5% (not annualized).[1]

[1] BREIT's Class D NAV per share increased from $14.78 to $14.79, Class S NAV per share increased from $15.09 to $15.10 and Class T NAV per share increased from $14.87 to $14.88. BREIT's Class D total return was 0.4%, Class S total return was 0.4% and Class T total return was 0.4% for September 2022.

BREIT's Form 10-Ks have similarly false or misleading statements reporting returns based on its NAV which is not reliable for calculating historical returns. For example, BREIT's December 31, 2021 Form 10-K at p. 93 includes the following Table reporting total returns based on the NAV Blackstone calculated and which BREIT states elsewhere in the same Form 10-K is not reliable for calculating returns.[4]

[3] www.sec.gov/Archives/edgar/data/1662972/000166297222000127/breitnavseptember2022.htm

[4] www.sec.gov/ix?doc=/Archives/edgar/data/0001662972/000166297222000027/breit-20211231.htm

Figure 1 Excerpt from BREIT's December 31, 2021 Form 10-K

2021 Highlights

Operating Results:

- Declared monthly net distributions totaling $1.6 billion for the year ended December 31, 2021. The details of the average annualized distribution rates and total returns are shown in the following table:

	Class S	Class I	Class T	Class D
Average Annualized Distribution Rate(1)	4.3%	5.2%	4.4%	5.0%
Year-to-Date Total Return, without upfront selling commissions(2)	28.7%	30.2%	29.4%	29.0%
Year-to-Date Total Return, assuming maximum upfront selling commissions(2)	24.4%	N/A	25.0%	27.1%
Inception-to-Date Total Return, without upfront selling commissions(2)	12.4%	13.4%	13.0%	13.5%
Inception-to-Date Total Return, assuming maximum upfront selling commissions(2)	11.6%	N/A	12.2%	13.1%

BREIT's Form 10-Qs have similarly false or misleading statements. For example, BREIT's September 30, 2022 Form 10-Q at p. 46 includes the following Table reporting total returns based on the NAV Blackstone calculated and which BREIT acknowledges elsewhere in the same Form 10-K is not reliable for calculating total returns.[5]

Figure 2 Excerpt from BREIT's September 30, 2022 Form 10-Q

Q3 2022 Highlights

Operating Results:

- Declared monthly net distributions totaling $694.9 million for the three months ended September 30, 2022. The details of the average annualized distribution rates and total returns are shown in the following table:

	Class S	Class I	Class T	Class D
Average Annualized Distribution Rate(1)	3.6%	4.5%	3.7%	4.3%
Year-to-Date Total Return, without upfront selling commissions(2)	8.5%	9.3%	8.4%	8.9%
Year-to-Date Total Return, assuming maximum upfront selling commissions(2)	4.9%	N/A	4.8%	7.3%
Inception-to-Date Total Return, without upfront selling commissions(2)	12.3%	13.3%	12.8%	13.3%
Inception-to-Date Total Return, assuming maximum upfront selling commissions(2)	11.6%	N/A	12.1%	13.0%

Blackstone's own SEC filings prominently feature historical BREIT returns based on the NAV Blackstone calculates for BREIT and which BREIT says is not reliable for calculating returns. For example, Blackstone's December 31, 2021 Form 10-K reports BREIT returns based on the unreliable NAV.[6]

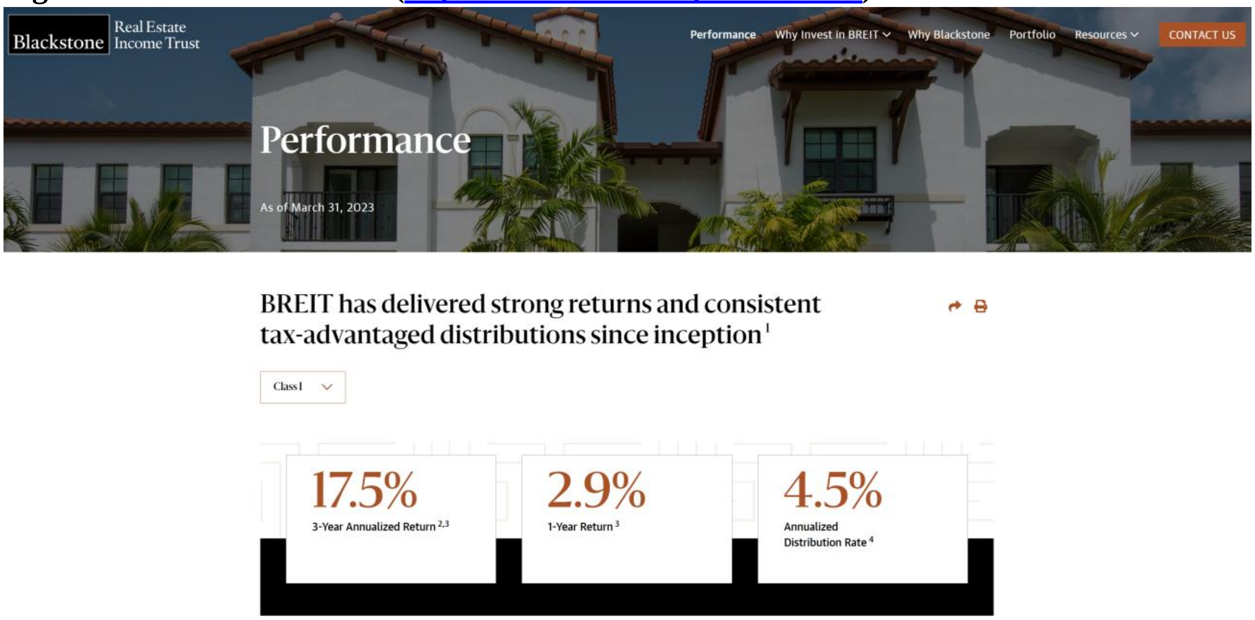
2) Blackstone and BREIT Tout Baseless Performance Numbers in Their Public Statements

BREIT's website continuously displays historical performance based on its unreliable NAV calculations. The top of BREIT's "Performance" webpage currently leads with the information in Figure 3. The 3-year annualized return of 17.5% and the 1-year return of 2.9% shown on this page reflect the percent change in the NAV per share from the beginning of the 3-year or 1-year period, plus the amount of any distribution per share declared, assuming reinvestment of all distributions.

[5] www.sec.gov/ix?doc=/Archives/edgar/data/0001662972/000166297222000027/breit-20211231.htm

[6] www.sec.gov/ix?doc=/Archives/edgar/data/0001393818/000119312522054433/d299999d10k.htm

Figure 3 BREIT Performance (https://www.breit.com/performance/)



BREIT also uses strong and misleading language when it says here, as it frequently says elsewhere, "BREIT has delivered strong returns .." BREIT has not *delivered* any returns except distributions to 80% of its investors. BREIT has sold 5,334,884,198 shares since inception and has met redemption requests for only 1,094,017,970 shares. The investors who bought and then redeemed shares have experienced both distributions and changes in NAV. 80% of investors who bought BREIT shares have only received dividends and have been told they can not receive the change in the NAV which BREIT repeatedly claims as returns *delivered* to investors.

Many of BREIT and Blackstone's press releases and executives' presentations include strong, unqualified statements about BREIT's historical performance based on NAVs which BREIT says are not a reliable basis for calculating historical performance. BREIT and Blackstone's public statements repeatedly refer to returns having been *delivered* to investors when 80% of investors who ever invested in BREIT have not *received* anything except dividend distributions.

3) Blackstone Takes Asset and Performance Incentive Fees Based on NAVs it Knows are Unreliable

Blackstone has taken $4.2 billion in asset management and performance fees based entirely on its calculation of NAV; $3.4 billion in fees in the past three years. The 30% return

BREIT claimed for 2021 based on its NAV was used to justify $1.8 billion in performance incentive and asset management fees in 2021.

Table 3 displays BREIT as a percentage of Blackstone's total fee-earning assets under management, based on net asset value, management fee, and performance allocation revenue. For the year ended December 31, 2022, BREIT accounted for 9.5% of Blackstone's fee-earning asset under management (AUM) while generated 13.3% of total management fees and 12.6% of total performance revenue.

Table 1. BREIT compared to Blackstone Fee-Earning Assets Under Management

In Thousands of USD

	2017	2018	2019	2020	2021	2022
Blackstone Fee Earning Assets Under Management	$335,343,998	$342,527,507	$408,074,852	$469,433,114	$649,969,058	$718,386,888
BREIT NAV	$1,800,272	$4,848,319	$13,101,304	$21,050,253	$54,080,976	$68,524,356
BREIT %	*0.5%*	*1.4%*	*3.2%*	*4.5%*	*8.3%*	*9.5%*
Blackstone Management & Advisory Fees, Net	$2,770,791	$3,036,452	$3,484,236	$4,111,165	$5,167,242	$6,282,946
BREIT Management Fee	$8,867	$42,659	$108,115	$224,776	$445,291	$837,687
BREIT %	*0.3%*	*1.4%*	*3.1%*	*5.5%*	*8.6%*	*13.3%*
Blackstone Performance Revenue	$3,741,071	$1,935,607	$1,872,643	$2,244,669	$5,908,356	$5,910,835
BREIT Performance Allocation	$16,974	$37,484	$141,396	$192,648	$1,378,959	$742,670
BREIT %	*0.5%*	*1.9%*	*7.6%*	*8.6%*	*23.3%*	*12.6%*

4) Blackstone's BREIT NAV Calculation Has Hidden Lever Used to Smooth and Inflate Returns

For 72 months BREIT told investors "the key assumptions in the discounted cash flow methodology used in the [previous month end] valuations" were the discount rate and the exit cap rate. Every monthly Form 424(b)(3) up to and including the one BREIT filed in October 2022 includes these two paragraphs and tables.[7]

Figure 4 Excerpt from BREIT's October 19, 2022 Form 424(b)(3)

Set forth below are the weighted averages of the key assumptions in the discounted cash flow methodology used in the September 30, 2022 valuations, based on property types.

Property Type	Discount Rate	Exit Capitalization Rate
Rental Housing	6.8%	5.4%
Industrial	6.7%	5.5%
Net Lease	6.9%	5.8%
Hospitality	9.4%	9.0%
Data Centers	7.2%	6.1%
Self Storage	7.1%	5.6%
Office	6.5%	5.2%
Retail	7.0%	5.9%

These assumptions are determined by the Adviser, and reviewed by our independent valuation advisor. A change in these assumptions would impact the calculation of the value of our property investments. For example, assuming all other factors remain unchanged, the changes listed below would result in the following effects on our investment values:

Input	Hypothetical Change	Rental Housing Investment Values	Industrial Investment Values	Net Lease Investment Values	Hospitality Investment Values	Data Centers Investment Values	Self Storage Investment Values	Office Investment Values	Retail Investment Values
Discount Rate	0.25% decrease	+1.9%	+2.0%	+1.8%	+1.7%	+1.3%	+1.9%	+1.9%	+1.9%
(weighted average)	0.25% increase	(1.9)%	(1.9)%	(1.8)%	(1.6)%	(1.2)%	(1.8)%	(1.9)%	(1.8)%
Exit Capitalization Rate	0.25% decrease	+3.1%	+3.5%	+2.5%	+1.4%	+1.6%	+2.8%	+3.7%	+2.8%
(weighted average)	0.25% increase	(2.8)%	(3.2)%	(2.3)%	(1.3)%	(1.6)%	(2.6)%	(3.3)%	(2.6)%

[7] www.sec.gov/Archives/edgar/data/1662972/000166297222000127/breitnavseptember2022.htm

BREIT failed to disclose the critical revenue growth assumption - assumption just as "key" as the discount rate and cap rate assumptions it disclosed for 72 months - until November 2022 as things appear to be coming off the rails. BREIT has since, belatedly and still only partially, disclosed material information about its discounted cashflow model valuations.

BREIT values its properties each month using a discounted cash flow ("DCF") model, assuming net operating income growth rates over some forecast period, valuations multiples applied to net operating income at the end of the forecast period, and discount rates to bring the terminal values back to the present. Because Blackstone does this exercise every month with very slight changes in assumptions about growth rates, and cap rates and discount rates, BREIT's NAV is smoothed. Also, since as we learned only recently. Blackstone has built in very substantial assumed future capital appreciation into its model, the NAV just keeps climbing with each passing month even if property values are falling.

BREIT's 424(b)(3)s illustrate the sensitivity of its valuations to the assumed exit cap rate and assumed cap in the tables excerpted above. Roughly speaking, if the exit cap rate Blackstone assumes is too low by 0.25% it inflates the investment values by over 3%. If the discount rate is too low by 0.25% it inflates the investment values by 2%. If both the assumed exit cap rate and discount rates are too low by 0.50% it inflates the investment values by 10%. Since BREIT is levered almost 2 to 1, those modest differences in assumptions would inflate BREIT's NAV by 20%.

On November 14, 2022, for the first time, BREIT also identifies the growth rate in net operating income as an important determinant of the NAV but does not itemize the assumed growth rate by property type or provide any sensitivity as it does for the discount rate and the capitalization rate. BREIT is partially disclosing this heretofore undisclosed key assumption. Being fully candid, admitting the growth rate is "a key assumption" and providing detailed disclosure and sensitivity analysis would highlight that BREIT had not been candid with investors every month for 6 years.

Figure 5 Excerpt from BREIT’s November 14, 2022 Form 424(b)(3)

Set forth below are the weighted averages of the key assumptions in the discounted cash flow methodology used in the October 31, 2022 valuations, based on property types.

Property Type	Discount Rate	Exit Capitalization Rate
Rental Housing	6.9%	5.4%
Industrial	6.8%	5.5%
Net Lease	6.9%	5.8%
Hospitality	9.4%	9.0%
Data Centers	7.2%	6.1%
Self Storage	7.1%	5.6%
Office	6.6%	5.2%
Retail	7.1%	6.0%

These assumptions are determined by the Adviser, and reviewed by our independent valuation advisor. In addition, the valuations for our two largest sectors (rental housing and industrial) assume high single digit net operating income growth in the near term given our below market rents and short duration leases. A change in these assumptions or factors would impact the calculation of the value of our property investments. For example, assuming all other factors remain unchanged, the changes listed below would result in the following effects on our investment values:

Input	Hypothetical Change	Rental Housing Investment Values	Industrial Investment Values	Net Lease Investment Values	Hospitality Investment Values	Data Centers Investment Values	Self Storage Investment Values	Office Investment Values	Retail Investment Values
Discount Rate	0.25% decrease	+1.9%	+2.0%	+1.8%	+1.7%	+1.3%	+1.9%	+1.9%	+1.9%
(weighted average)	0.25% increase	(1.9)%	(1.9)%	(1.8)%	(1.6)%	(1.2)%	(1.8)%	(1.9)%	(1.8)%
Exit Capitalization Rate	0.25% decrease	+3.1%	+3.5%	+2.5%	+1.4%	+1.6%	+2.9%	+3.6%	+2.8%
(weighted average)	0.25% increase	(2.8)%	(3.2)%	(2.3)%	(1.3)%	(1.6)%	(2.5)%	(3.3)%	(2.6)%

This previously undisclosed assumption is critical because high assumed growth generates higher terminal values at the end of the forecast periods. BREIT’s long run valuations have to imply net operating income growth rates that are lower than the discounts rates used in the DCF. In fact, the exit cap rates assumed by BREIT are the amount by which the discount rate exceeds the long run rate of growth of net operating income growth. Despite acknowledging the discount rate will be 5% higher than the growth rate at the end of the forecast period in its DCF, BREIT is assuming growth rates greater than the discount rate over its projected future periods.

BREIT’s disclosed discount rates and undisclosed high net operating income growth rates have symmetric impacts on valuations. Using BREIT’s sensitivities to discount rates, we know that if BREIT’s assumed growth rate is too high by 0.25% it inflates the investment values by 2%. There is good reason to believe BREIT’s assumed but non-disclosed growth rate is a full 2% too high. Correcting BREIT’s assumption of substantially above market growth rates, lowers its property values 15% and its NAV by 30%.

As of December 31, 2022, residential properties represent 57% of BREIT’s asset value. We put BREIT’s valuation assumptions for residential properties in a simple DCF model as shown in Table 1. To arrive at an asset value of $73 billion from $2.1 billion NOI and to match BREIT’s reported discount rate and cap rate sensitivities, we have to project a constant 9.5% NOI growth rate for 10 years. While the assumptions for each individual residential property could be different, this simple DCF model using aggregated value and weighted average rates shows that Blackstone is very optimistic about the rental housing properties held in BREIT.

Table 2 Discounted Cash Flow Model for Residential Properties (in thousand $)

Property Type	Residential
Discount Rate	7.0%
Exit Cap Rate	5.4%
Asset Value	$73,727,145
Segment NOI	$2,149,765

				Discount Rate		Exit Cap Rate	
Year	**Growth**	**NOI**	**DCF**	**+0.25%**	**-0.25%**	**+0.25%**	**-0.25%**
0.5	9.5%	$2,251,879	$2,176,973	$2,174,435	$2,179,521	$2,176,973	$2,176,973
1.5	9.5%	$2,465,807	$2,227,837	$2,220,052	$2,235,668	$2,227,837	$2,227,837
2.5	9.5%	$2,700,059	$2,279,890	$2,266,627	$2,293,261	$2,279,890	$2,279,890
3.5	9.5%	$2,956,565	$2,333,158	$2,314,178	$2,352,338	$2,333,158	$2,333,158
4.5	9.5%	$3,237,438	$2,387,671	$2,362,728	$2,412,937	$2,387,671	$2,387,671
5.5	9.5%	$3,544,995	$2,443,458	$2,412,295	$2,475,097	$2,443,458	$2,443,458
6.5	9.5%	$3,881,769	$2,500,548	$2,462,903	$2,538,858	$2,500,548	$2,500,548
7.5	9.5%	$4,250,538	$2,558,972	$2,514,572	$2,604,262	$2,558,972	$2,558,972
8.5	9.5%	$4,654,339	$2,618,761	$2,567,325	$2,671,351	$2,618,761	$2,618,761
9.5	9.5%	$5,096,501	$2,679,947	$2,621,185	$2,740,168	$2,679,947	$2,679,947
9.5			$49,628,648	$48,540,470	$50,743,853	$47,432,690	$52,037,806
Value			**$73,835,863**	**$72,456,770**	**$75,247,316**	**$71,639,905**	**$76,245,021**
			Sensitivity	-1.9%	1.9%	-3.0%	3.3%
			Reported Sensitivity	-1.8%	1.9%	-2.8%	3.1%

We also tested the same model for net lease properties. As shown in Table 2, the growth rate used to value net lease properties seems to be more conservative.

Table 3 Discounted Cash Flow Model for Net Lease (in thousand $)

Property Type	Net Lease
Discount Rate	6.8%
Exit Cap Rate	5.8%
Asset Value	$10,021,960
Segment NOI	$497,906

				Discount Rate		Exit Cap Rate	
Year	**Growth**	**NOI**	**DCF**	**+0.25%**	**-0.25%**	**+0.25%**	**-0.25%**
0.5	3.0%	$505,375	$489,021	$488,450	$489,595	$489,021	$489,021
1.5	3.0%	$520,536	$471,622	$469,971	$473,282	$471,622	$471,622
2.5	3.0%	$536,152	$454,841	$452,190	$457,514	$454,841	$454,841
3.5	3.0%	$552,236	$438,658	$435,083	$442,271	$438,658	$438,658
4.5	3.0%	$568,804	$423,050	$418,622	$427,535	$423,050	$423,050
5.5	3.0%	$585,868	$407,998	$402,785	$413,291	$407,998	$407,998
6.5	3.0%	$603,444	$393,481	$387,546	$399,521	$393,481	$393,481
7.5	3.0%	$621,547	$379,481	$372,884	$386,210	$379,481	$379,481
8.5	3.0%	$640,193	$365,978	$358,777	$373,342	$365,978	$365,978
9.5	3.0%	$659,399	$352,957	$345,203	$360,903	$352,957	$352,957
9.5			$6,085,462	$5,951,782	$6,222,467	$5,833,996	$6,359,582
Value			**$10,262,548**	**$10,083,293**	**$10,445,930**	**$10,011,082**	**$10,536,668**
			Sensitivity	-1.7%	1.8%	-2.5%	2.7%
			Reported Sensitivity	-1.8%	1.8%	-2.4%	2.6%

BREIT recently disclosed interesting changes to its net asset value calculation and valuation guidelines in its March 28, 2023 prospectus amendment. Prior to this recent modification BREIT's characterization of the independent valuation advisor can be paraphrased as follows.

(1) a third-party appraisal firm conducts appraisals and renders appraisal reports annually;

<u>(2) an independent valuation advisor reviews the appraisal reports for reasonableness;</u>

(3) the advisor (Blackstone) receives the appraisal reports and based in part on the most-recent appraisals, renders an internal valuation to calculate NAV monthly;

(4) the independent valuation advisor reviews <u>and confirms</u> the internal valuations prepared by the advisor.

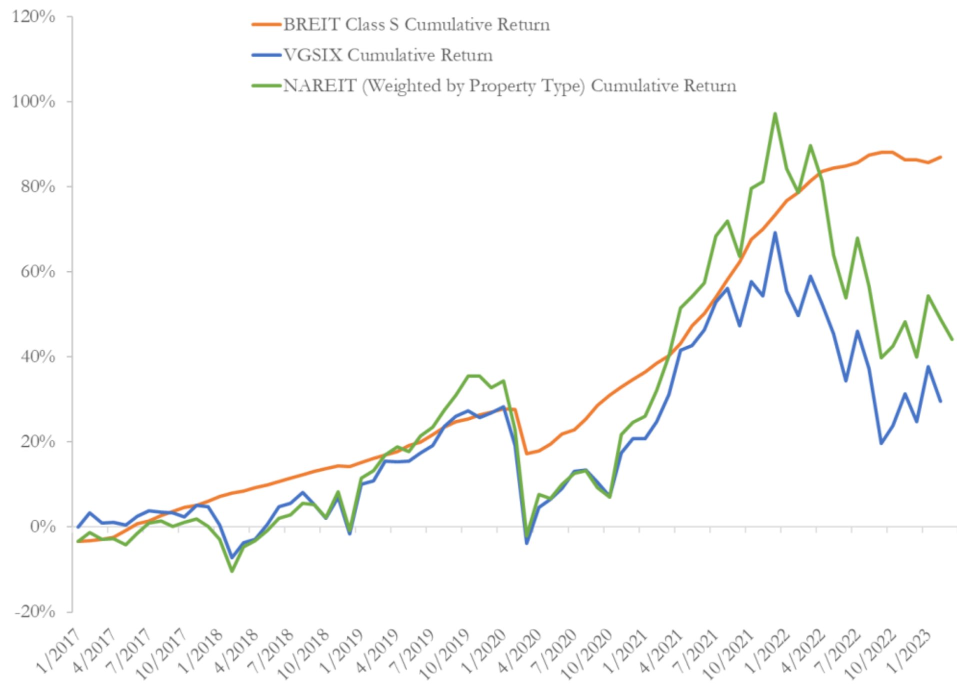
<u>(5) BREIT will promptly disclose any changes to the identity or role of the independent valuation advisor in its reports publicly filed with the SEC.</u>

With the prospectus amendment dated March 28, 2023, BREIT removed the underlined steps. BREIT may be considering a change in its independent valuation advisor or may just belatedly be truthfully describing what little its independent valuation advisor actually did.

5) BREIT's pre-2022 Returns Smoothed, 2022 Was Pure Fantasy

There is very little difference in BREIT's cumulative returns compared to traded REITs for BREIT's first five years. If an investor purchased BREIT Class S shares at $10.35 per share in January 2017 ($10.00 transaction price plus 3.5% selling commissions) and reinvested all distributions by December 2021, her total return would be 73.4% or 14.8% per year. During the same period, Vanguard's Real Estate Index Fund (VGSIX), a liquid mutual fund holding a diversified portfolio of publicly traded REITs, posted a total return of 69.28% or an annualized return of 14.1%. See Figure 5.

Figure 6. Cumulative Returns of BREIT compared to Vanguard Real Estate Index Fund, January 2017 to February 2023



In 2022, traded REIT prices dropped significantly and BREIT continued to smoothly increase its NAV each month until late in the year.

BREIT claimed its returns exceeded those of traded REITs in 2022 because BREIT concentrated in residential and industrial property sectors. BREIT started 2022 with 29% invested in industrial properties and 53% in residential properties. Prologis, the largest traded industrial REIT, had a -31.3% total return in 2022. Equity Residential, the largest residential REIT, had a -32.5% total return in 2022. Prorating BREIT's 29% and 53% sector weights to sum to 100%, the weighted average residential/industrial sector return in 2022 is -31.7%.

The green line in Figure 6, presents a more sophisticated implementation of this analysis. We calculated the cumulative returns of the various NAREIT sector indices weighted by BREIT's reported sector allocations. This BREIT-weighted NAREIT composite declined by 29.0% in 2022. Clearly, BREIT's 2022 returns are not because it concentrated in the residential and industrial property sectors.

The enormous differential in BREIT's claimed 2022 returns and the returns to traded REITs is simply the result of Blackstone and BREIT calculating the 2022 returns based on an inflated, DCF model-based NAV which Blackstone and BREIT acknowledge is not reliable for calculating historical returns.

Smart Money Doesn't Believe Traded REITs are Oversold

BREIT and its supporters have argued that traded REITs were oversold in 2022 as retail investors irrationally soured on real estate. There is a simple market test for BREITs assertion that traded REITs are oversold and their prices are depressed and will revert to higher prices in the future reflecting the actual value of their holdings.

If BREIT and its supporters were correct that the 2022 returns reflect a 30% undervaluation of traded REITs, portfolio managers of large actively managed stock funds should be loading up on REITs. As portfolio managers look for underpriced securities, they evaluate Boeing, Tesla or Amazon against some vague and uncertain measure of their true value. Accepting BREIT's explanation of 2022 returns for the sake of argument, the largest actively managed domestic stock funds have a precise and certain estimate of traded REITs' true value – traded REITs' December 31, 2021 NAV's adjusted for the change in BREIT's NAV in 2022. This implies an enormous arbitrage opportunity. Retail investors might be driven by ignorance and emotion as suggested by BREIT and its apologists but there is no reason to think that portfolio managers at American Funds, Fidelity and Vanguard are not objectively evaluating traded REITs.

The 50 largest actively managed domestic mutual funds held **1.07%** of their portfolios in REITs as of December 31, 2020 and **1.04%** of their portfolios in REITs as of December 31, 2022. Professional managers of the largest actively managed domestic mutual funds do not believe traded REITs are oversold and therefore underpriced at the end of 2022.

Interestingly, these sophisticated portfolio managers also do not believe BREIT is a good investment. The 100 largest, actively managed, domestic stock mutual funds' portfolio managers manage over $3 trillion. They search for mispriced assets and compete for investors by maximizing their net risk-adjusted returns. These portfolio managers can and do hold non-traded assets. These portfolio managers can and do hold REITs collectively they hold $30 billion of REITs. **What the 100 largest actively managed domestic stock funds don't do is hold a single share of BREIT!** There is no trace of BREIT in the quarterly portfolio holdings for 2020, 2021 and 2022 of these 100 largest actively managed funds. BREIT is not just underweighted in the 100 largest actively managed stock funds - its portfolio weight is 0.0000000% of $3 trillion.

None of the 100 largest actively managed domestic stock funds owns a single share of BREIT - word from the wise.

A last word (for now) on BREIT's 2022 returns based on its unreliable NAV. We've seen hundreds of DCF models over the years. We've consumed them, taught them, wrote about them and testified about them. What we have never seen is the claim that DCFs are superior to market prices when estimating the market value of a security but that is exactly what Blackstone, BREIT and their proponents claim.

What is the best measure of the value of a share of Apple stock? We could create a DCF model or find DCFs in an analyst report. We could fuss with the assumptions and get something more or less than today's price but if someone were to ask us the value of a share of Apple stock, we would consult Yahoo Finance not your DCF spreadsheet. If the market price is a more reliable indication of the value than a DCF model for all securities we can imagine, why would the DCF model be a better indicator of the value of BREIT shares than the market price of large, traded REITs with similar sector concentrations?

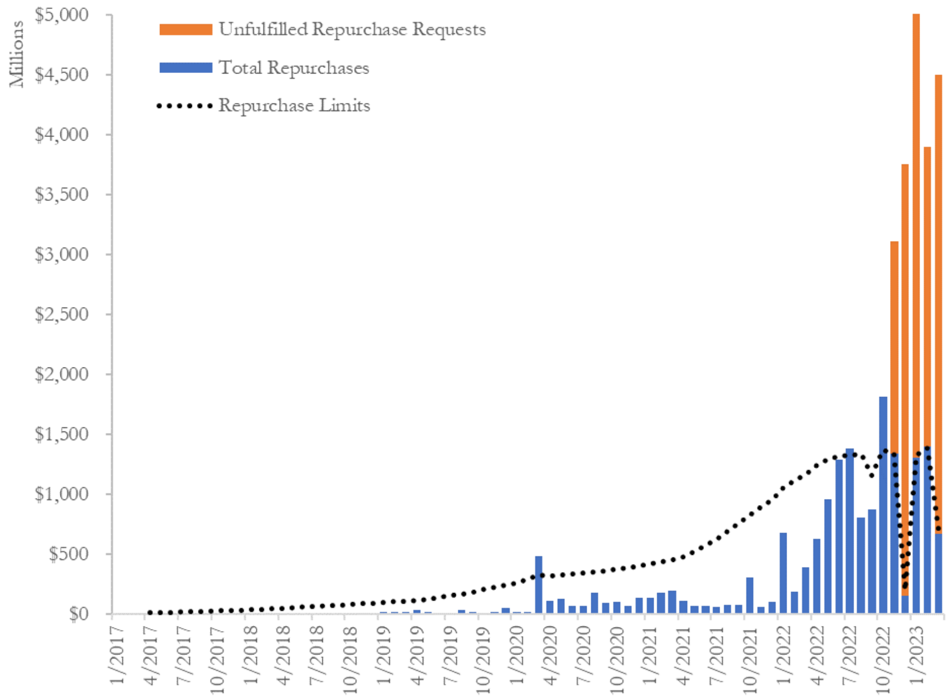
6) BREIT Limits Redemptions to Slow the Coming Trainwreck

In December 2022, for the first time BREIT imposed redemption limits that it had waived three times before. While BREIT has the right but not the requirement to limit redemptions to 2% of NAV per month and 5% of NAV per quarter it chose not to exercise this right and limit redemptions until, we believe, BREIT's NAV was significantly overstated. BREIT could easily have met redemptions without selling properties but, if the NAV was overstated, redeeming shareholders at stated NAVs would increase the mispricing in the remaining shares and just defer the day of reckoning.

If BREIT's NAV is real, it would have met redemptions for a few months - stopping the bank run - and protecting the franchise. It is not doing so precisely because meeting redemptions will dilute the NAV further – not because of forced property sales but because the current posted NAV is not real. If the posted and real NAV were both $15 and the debt ratio is 50% but can go to 75%, Blackstone can redeem 50% of investors without selling any assets and without depressing the NAV. If the true NAV is $10 and Blackstone levers up buying shares back at the posted $15 NAV, and then the truth value of its portfolio holding is revealed the NAV will drop to $5. This is a nightmare scenario but the one we think Blackstone faces and so has decided to limit redemptions indefinitely, effectively turning BREIT into Hotel California.

Before BREIT announced to cap investors' withdrawals in November 2022, it had hit monthly limit 3 times – in March 2020 and July and October 2022. BREIT honored these repurchase requests, perhaps because it did not want to draw attention to the true illiquidity of BREIT shares and the suspect NAV it had been reporting.

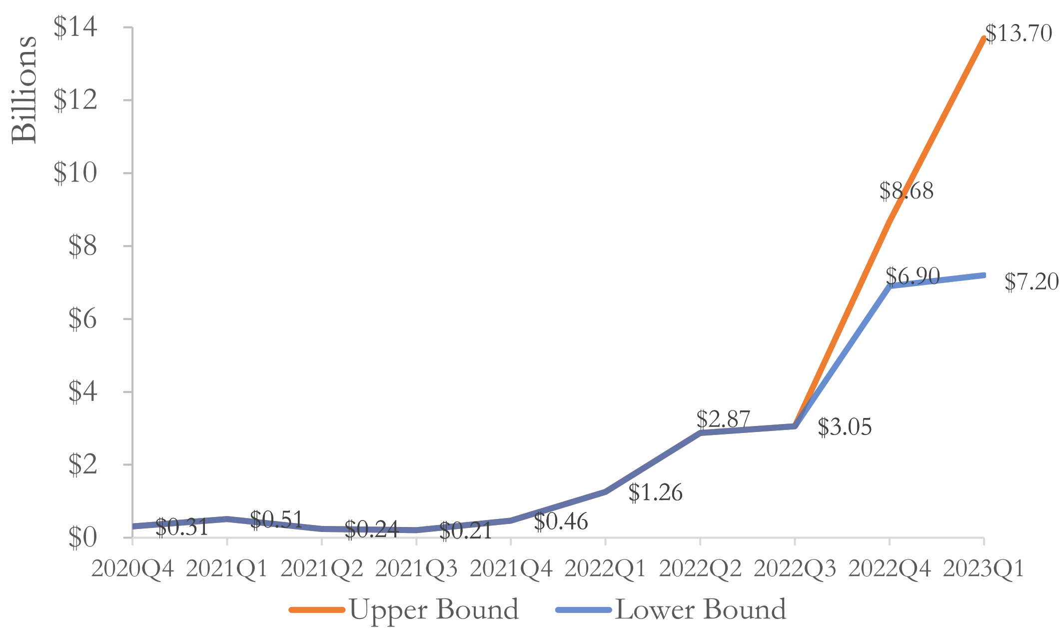
Figure 7 BREIT Monthly Repurchases, January 2017 to March 2023



BREIT puts a misleading gloss on recent redemption requests. It has said that recent monthly redemptions reflect working through unmet redemption requests from December. As Figure 7, illustrates redemption requests in March 2023 significantly exceeded redemption requests and unmet redemption requests in December 2022. BREIT also touted that March 2023 redemption requests were 16% lower than January 2023 but is silent on the clear upward trend in redemptions requests. March 2023 redemption requests were 15% higher than in February.

Investors might consider the likelihood of a redemption request filled and vary their behavior in the first and second month of a quarter compared to the third month. BREIT's published data doesn't allow us to know how many redemption requests are being renewed from unfilled requests the previous month. We plot upper and lower bounds on unique redemption requests by quarter in Figure 8. The lower bound assumes unmet redemption requests are rolled forward to the next month. The upper bound assumes all requests each month are new and unique (at least during the trailing three-month period). Up through the third quarter of 2022 all redemption requests were honored so the upper and lower bound numbers are the same. There were $3.05 billion in redemption requests in the third quarter 2022, between $6.90 billion and $8.68 billion in the fourth quarter 2022 and between $7.20 and $13.70 billion in the first quarter of 2023. These results tell us recent months' redemption requests are not carryovers from November and December.

Figure 8 BREIT's Redemption Requests Continue to Increase Dramatically in 2023

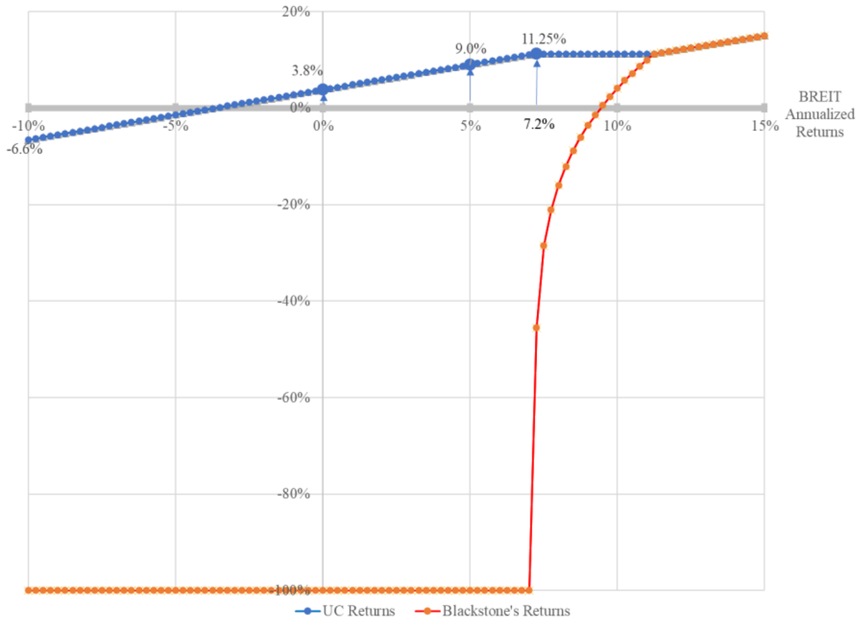


7) University of California Bought BREIT Only After Given a 20% Discount

Blackstone made an extremely generous deal with the University of California, in most states of the world ultimately selling the University of California BREIT shares at a 20% discount. Blackstone would not make the offer if it was confident in its NAV or felt it could defend the franchise without paying $1 billion. Blackstone made a public relations splash claiming the University of California's imprimatur on BREIT's Class I shares but actually sold the University of California something very different. Blackstone announced the University of California investment in a manner so misleading as to fool for a time sophisticated market professions. It timed the release of this manipulative investment to strategically to deflect attention from it only meeting 4% of the redemption requests.

Figure 9 illustrates the returns earned by the University of California on its $4 billion and the returns earned by Blackstone on its $1 billion investment plotted against BREIT returns.

Figure 9 Blackstone Investors Heavily Subsidize UC's Investment in BREIT



For any annualized BREIT return less than 7.2%, Blackstone shareholders turn over the $1 billion in current BREIT shares plus whatever their returns are over 6 years to the University of California and the University of California gets $5 billion of BREIT for $4 billion – a 20% discount and Blackstone shareholders suffer a 100% loss. If BREIT's return is between 7.2% and 11.25% the University of California is getting BREIT shares at an effective discount grading down from 20% to 0%.

There are two very big problems with Blackstone and BREIT's suggestion 11.25% cumulative returns over the next 6 years are likely and so the deal with the University of California is not likely to cost Blackstone shareholders based on BREIT's 12.5% annualized returns over the prior 6 years. BREIT's reported 12.5% annualized returns are based on NAVs calculated by Blackstone which are not reliable for calculating returns. Moreover, the 12.5% annualized return becomes 9.3% when BREIT's 2021 claimed return of 30% is excluded. As we have argued, BREIT's returns based on dubious NAVs should be heavily discounted. BREIT tracked smoothed VGSIX returns until December 31, 2021. VGSIX's annualized returns over the six years ending December 31, 2022 were 3.8% and BREITs true annualized returns over the six years ending December 31, 2022 were not likely much more than 5% or 6%. It seems extremely likely that Blackstone's shareholders will lose 100% of their investment as a result of the side letter Blackstone gave the University of California to induce it to invest in BREIT.

Contrary to Blackstone's spin, the University of California investment strongly supports the view that BREIT is a terrible investment. The University of California had a long relationship with Blackstone and invested in other Blackstone products but didn't invest in BREIT as it grew to $70 billion over 6 years. The University of California was not willing to invest in BREIT until Blackstone gave it a 20% discount - a discount available to no other investor.

Conclusion

In November and December, we were BREIT skeptics among a sea of true believers. The bank run on BREIT is underway and Blackstone has apparently decided to limit redemptions and slowly adjust BREIT's NAV down.

Blackstone and BREIT have not been candid about their use of unreliable NAVs in historical returns presented in SEC filings and other public statements. Blackstone has inappropriately used these unreliable NAVs to pay itself $4.2 billion in fees. Blackstone and BREIT have partially revealed their NAV sleight of hand but continue to hide the ball. BREIT posted 2022 returns which defied the gravitational forces operating on real estate property values in the sectors BREIT invested 80% of its portfolio and falsely attributed its differential 2022 returns to traded REITs to irrational retail investors. BREIT imposed redemption limits that it had waived three times before until BREIT's NAV was likely significantly overstated. Blackstone made a sweetheart deal with the University of California, effectively selling the University of California BREIT shares at a 20% discount.

Blackstone's zealots could be right; maybe BREIT is a great investment. We didn't think so in November 2022. Surveying some of the ways that Blackstone has misled investors over the past 5 months, we are more convinced than ever that BREIT is a bad investment created for the benefit of Blackstone.

In the end, Blackstone's BREIT seems not much different than Nicholas Schorsch's various offerings 15 years ago. This should not be a huge surprise as externally-managed, non-traded REITs were well known to harm investors for the benefit of sponsors of the trusts.

Returning to the market test. Those 100 largest, actively managed domestic stock mutual funds which combined manage over $3 trillion – the smart, unconflicted money – hold $30 billion of REITs and not $0.01 in BREIT do hold significant investments in Blackstone. Word from the wise.