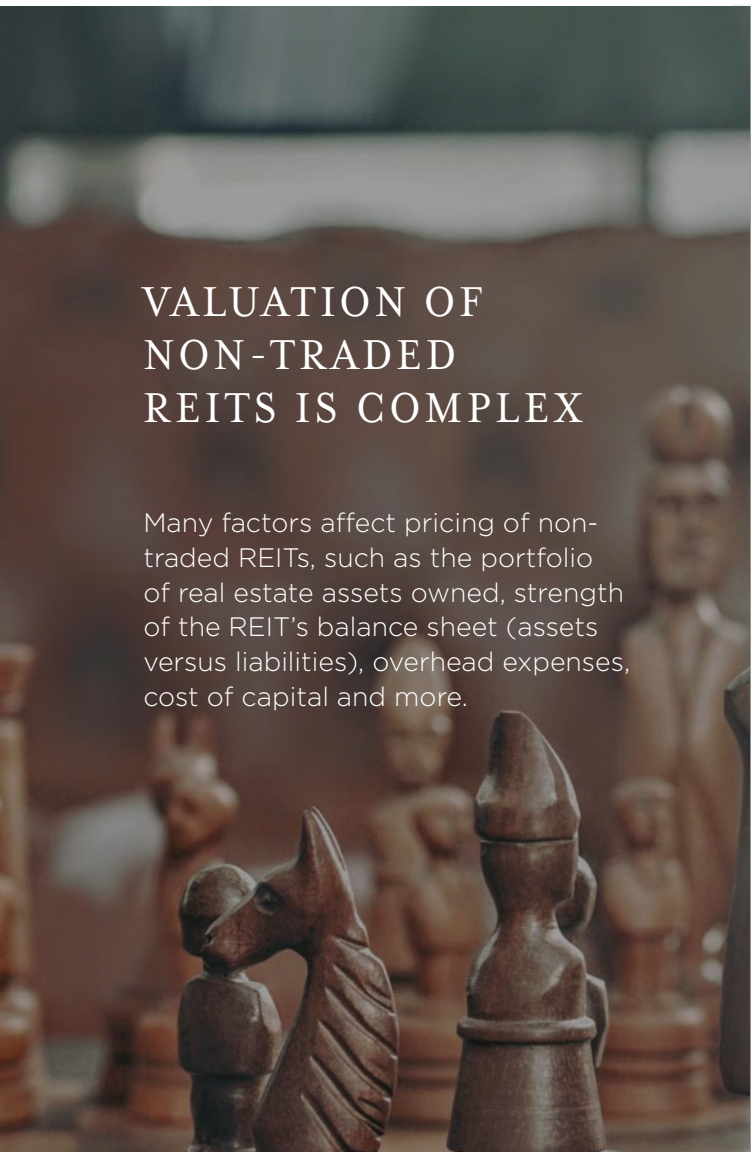




WHAT TO EXPECT WITH NET ASSET VALUE (NAV)

A GUIDE TO UNDERSTANDING HOW NAV MAY FLUCTUATE OVER TIME FOR DEBT AND EQUITY NON-TRADED REAL ESTATE INVESTMENT TRUSTS (“REITS”)



VALUATION OF NON-TRADED REITS IS COMPLEX

Many factors affect pricing of non-traded REITs, such as the portfolio of real estate assets owned, strength of the REIT’s balance sheet (assets versus liabilities), overhead expenses, cost of capital and more.

Net Asset Value, or NAV, is calculated by taking the total value of assets minus the total value of liabilities. NAV per share is calculated by dividing NAV by the number of outstanding shares. Although non-traded REIT shares are not liquid and NAV per share is not updated every day; you can think of NAV per share as similar to the price of a mutual fund.

Non-traded REITs are illiquid and thus have relatively stable NAVs when compared to publicly traded REITs (as discussed in a separate article [here](#)), where share prices can fluctuate daily. In other words, if the public markets decline resulting in a negative price/NAV environment, an illiquid non-traded REIT may be unaffected.

REITs that derive their income from investments in real estate debt or debt-like instruments differ from those that invest in real estate equity. Below, we will walk through the underlying actors that affect NAV, followed by two examples of NAV changes to non-traded REITs investing in debt or equity. We will also discuss how different REIT types can impact the stability of NAV.

FACTORS AFFECTING NAV



NET CAPITAL

Includes cash received from investors less offering costs. Net capital may decrease if investors redeem shares.



NET INCOME

Includes both taxable and non-taxable income* for the REIT. Net income can increase the NAV, while net loss can cause the NAV to decrease.



CASH DISTRIBUTED TO INVESTOR

REITs are required to distribute 90% of taxable income each year.

* An example of taxable income is cash received from investments. An example of non-taxable income is appreciation of investments. Net income also includes the operating expenses of the entity such as bank fees and annual audits. There is no guarantee the REIT will make a net profit and thus have a positive net income.

**NET CAPITAL
(INVESTOR CAPITAL LESS OFFERING COSTS)**

**+ NET INCOME
(TAXABLE AND NON-TAXABLE)**

**- DISTRIBUTIONS TO INVESTORS
(90% OF ANNUAL TAXABLE INCOME)**

**= NET ASSET VALUE
(TOTAL EQUITY)**

As illustrated, changes in net capital and net income can increase or decrease the equity of the REIT, which in turn increases or decreases the NAV. Changes to investor capital or offering costs can also affect the NAV. Offering costs are any costs associated with the offering itself, or selling the shares. Offering costs do not run through the income statement and are a direct hit to equity. Some examples are legal fees incurred to create and update the offering circular, audit fees incurred to review the offering circular, and costs associated with marketing the offering to investors.

HOW NAV FLUCTUATES IN DEBT AND DEBT-LIKE INSTRUMENTS

(For illustrative purposes only)

Investors seeking income may benefit from a REIT that invests in debt and debt-like instruments. Since distributions are paid from investment income, if cash received is relatively stable over time, distributions will be relatively stable over time as well. Investors in debt REITs typically look for steady payments of distribution income. See below for an example of how NAV per share is calculated in a debt instrument:

Debt Example:

Capital Raised from Investors (100 shares x \$10 each)	\$1000
Less offering costs (up to 3%)	- \$30

NET CAPITAL	\$970
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Cash received from investments (taxable)	\$12
Less Operating expenses (taxable)	- \$2

+ NET INCOME (TAXABLE)	\$10
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- DISTRIBUTIONS (AT LEAST 90% TAXABLE INCOME FROM REIT)	- \$10
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NAV (Net capital + net income - distributions)	\$970
Divided by outstanding shares (100)	100

= NAV PER SHARE	\$9.70
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There is usually little opportunity for appreciation in the underlying investments. Debt instruments are designed to return the original investment, par value, plus a pre-determined interest rate on the investment. The investor may not expect to earn more money than the par value but could potentially earn less if the underlying property is unable to repay the debt instrument. REITs must distribute at least 90% of their taxable income each year and most, if not all, of the income from these instruments is taxable, which is why NAV will not increase.

HOW NAV FLUCTUATES IN EQUITY INSTRUMENTS

(For illustrative purposes only)

Investors seeking long-term appreciation typically consider equity REITs. It is common for the underlying investments in an equity portfolio to increase or decrease in value over time, depending on the property, which directly affects the NAV. A REIT that invests in real estate equity could potentially receive more than the original investment but does not benefit from a pre-determined interest rate. As such, NAV fluctuations in a debt REIT typically are asymmetrical, with likelihood of NAV increases being less likely.

For example, if an equity REIT owns a multifamily apartment building, completes renovations and then earns higher rents, the underlying asset is likely to appreciate in value. As a result, the NAV per share increases. See the calculations in the chart on the following page to see how NAV increases and decreases depending on whether the asset value of the investment increases or decreases.

Increase in Asset Value

With an equity REIT, if the underlying assets increase in value, the NAV is directly impacted and is likely to increase, which can push the new NAV per share to an amount that is higher than the offering price (which comes out to \$10.20 in the following example).

Decrease in Asset Value

If the underlying assets decrease in value, the resulting NAV may be lower than the offering price (\$9.20 in the following example). In an equity REIT where the underlying assets do not appreciate, it is unlikely that the NAV will go higher than the offering price (\$10 in the example).

HOW NAV FLUCTUATES IN EQUITY INSTRUMENTS (CONT.)

Equity Example:	Increase in Asset value	Decrease in Asset value
Capital Raised from Investors (100 shares x \$10 each)	\$1000	\$1000
Less offering costs (up to 3%)	- \$30	- \$30
NET CAPITAL	\$970	\$970
Cash received from investments (taxable)	\$12	\$12
Appreciation/depreciation of investment value (non taxable)	\$50	- \$50
Less Operating expenses (taxable)	- \$2	- \$2
+ NET INCOME	\$60	- \$40
Taxable net income	\$10	\$10
Non-taxable net income	\$50	- \$50
- DISTRIBUTIONS (AT LEAST 90% TAXABLE INCOME FROM REIT)	- \$10	- \$10
NAV (Net capital + net income - distributions)	\$1,020	\$920
Divided by outstanding shares (100)	100	100
= NAV PER SHARE	\$10.20	\$9.20

FOR MORE INFORMATION

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Investments are risky and are not suitable for all investors. Before investing, consider the "Risks" associated with each investment. Important information about risks, fees and expenses are outlined in the official offering documents. Investing in REIT common shares is speculative and risks include illiquidity, complete loss of capital, limited operating history, conflicts of interest and blind pool risk.

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