



Investing beyond the tax benefits: Opportunity Zones enter their next chapter

Since the Opportunity Zone program was introduced in 2018, the market has changed meaningfully. Many first-generation Opportunity Zone investments ("Opportunity Zone 1.0") were underwritten during a period of historically low capitalization rates and abundant capital, only to encounter rising interest rates, construction cost inflation and tighter financing conditions. Today, investors considering the now-permanent "Opportunity Zone 2.0" program beginning in January 2027 have nearly eight years of experience and a clearer understanding of what drives long-term performance in Opportunity Zones.

Real Assets Adviser spoke with David Butler and Andy Stewart, co-CEOs of Argosy Real Estate Partners, about how the Opportunity Zone market has evolved, why the program was a natural extension of Argosy's lower middle market allocator strategy, and how investors should evaluate the next generation of Opportunity Zone managers. Argosy invests through opportunistic, core-plus and Opportunity Zone strategies across alternative and traditional property sectors.

Argosy began investing in Opportunity Zones in 2019. What initially attracted the firm to the program?

David Butler: Our interest developed organically. We were evaluating a ground-up development opportunity when our operating partner noted the project sat in a newly designated Opportunity Zone (OZ). That prompted us to examine the legislation and the map of designated census tracts.

One surprise was the quality of the underlying real estate. Many designated tracts were near established neighborhoods, employment centers, universities and other long-term demand drivers – the program didn't require investors to choose between tax efficiency and strong fundamentals.

It also aligned with what Argosy already did well: partnering with specialized operating partners through joint ventures to pursue acquisitions and ground-up development in the lower middle market. Evaluating development risk, selecting experienced partners, structuring investments and building diversified portfolios were capabilities we'd developed well before the program existed.

Our core principle was straightforward: An Opportunity Zone investment should make sense before considering the tax benefits. The tax treatment should enhance a sound investment thesis, not substitute for one.

Why does today's market present a more attractive entry point?

Andy Stewart: Today's market is a fundamentally different starting point than when the first OZ funds launched. That early capital was deployed amid low cap rates, elevated land values, aggressive development assumptions and abundant financing – then hit rapidly rising rates, significant construction cost inflation and a much tougher lending environment.

Today, development sites can often be acquired at more attractive bases, cap rates have expanded and new construction has slowed meaningfully across many markets. For projects with multi-year timelines, that can mean delivering into a more favorable supply/demand environment.

Financing remains challenging and costs remain elevated. But reduced transaction activity and tighter capital availability can

create opportunities for managers with patient capital, strong operating-partner relationships and disciplined structuring. Access to experienced local partners and appropriate capitalization are especially important in this environment.

Investors also now have a track record to evaluate managers against – how they sourced deals, managed development risk, selected partners, built portfolios and executed through a difficult phase of the cycle. Success depends on the quality of the real estate and the manager's execution, not solely the tax benefits.

No environment eliminates risk, but we believe today's combination of more defensible entry bases, reduced new supply in selected markets and a more favorable development backdrop provides a stronger foundation than existed when much of the first generation of capital was deployed.

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– David Butler, Co-CEO

How should investors evaluate managers after nearly eight years of Opportunity Zone investing?

Butler: Investors should start with the manager's investment process, organizational capabilities, alignment of interests and ability to execute over a long horizon.

They should assess development experience, underwriting discipline, established investment and asset management infrastructure, and relationships with experienced operating partners – and understand how the manager addresses entitlement, permitting, construction, lease-up, financing and exit risk, since most Opportunity Zone investments involve development or substantial rehabilitation.

For us, that often means focusing on opportunities where key development milestones are already achieved before we commit capital. We favor joint venture structures where operating partners make a meaningful co-investment and, where negotiable, provide protections like cost-overrun or loan guarantees.

Operational capabilities matter, too. OZ strategies require ongoing tax administration, compliance oversight, valuation, audit and tax-return coordination, and investor reporting throughout an investment expected to last more than a decade. Investors and advisers should confirm the manager has the personnel and processes to support that over the full holding period. For RIAs, this is particularly relevant, since the adviser may need to coordinate among the client, fund manager, custodian, accountant and tax

attorney. A manager should clearly explain what information it will provide, and when and where the investor's own tax adviser must make an independent determination – tax consequences depend on each investor's individual circumstances.

Portfolio construction is equally important. Diversification across markets, operating partners, property types and individual investments helps manage concentration risk over a full cycle. Investors should examine exposure to any single project, market, sector or operating partner.

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Experience across traditional and alternative sectors can expand the opportunity set, but diversification shouldn't come at the expense of expertise – confirm the manager and its partners have relevant experience in each sector the fund intends to pursue.

Finally, examine fund size and deployment discipline. Because Qualified Opportunity Funds are subject to statutory asset tests and timelines, a very large fund may need to chase larger projects or a narrower group of transactions, potentially increasing concentration or reducing selectivity. Confirm the target fund size is supported by the manager's sourcing volume, operating-partner network, staffing and demonstrated ability to deploy capital without compromising underwriting standards.

Why has the lower middle market remained attractive for Opportunity Zone investing?

Stewart: The lower middle market is highly fragmented, and many compelling projects are developed by experienced operators with deep local knowledge but limited access to institutional capital. That creates an attractive opportunity for institutional capital to partner with experienced developers who'd rather focus on executing a select number of projects than build their own fund management organizations. Institutional investors can provide capital and oversight while operators focus on execution.

The segment also lends itself well to Opportunity Zone investing. Smaller equity requirements let a fund assemble a broader, more diversified portfolio rather than concentrating in a handful of large developments. Smaller projects may also involve less entitlement complexity, shorter timelines and more manageable construction costs than larger-scale developments, though this varies by project and market. This approach also provides flexibility to shift capital among markets and sectors as relative opportunities change, rather than committing to a single theme.

What are the most meaningful changes under OZ 2.0?

Butler: Opportunity Zone 2.0 makes the incentive permanent and establishes recurring 10-year designation cycles, with the next designations effective January 2027. For qualifying investments, tax on eligible gains generally may be deferred for five years. Investors meeting the five-year holding requirement may receive a basis step-up equal to 10 percent of the deferred gain, with an enhanced 30 percent step-up for qualifying investments in Qualified Rural Opportunity Funds.

This recurring framework should let investors, advisers and managers treat OZ investing as a continuing part of long-term tax and portfolio planning rather than a program approaching a fixed sunset – and let advisers build the strategy into broader planning rather than reacting only after a client realizes a gain.

Qualified Rural Opportunity Funds also broaden the opportunity set. Under the new legislation, at least one-third of each state's designated zones must be rural, or a share equal to the state's rural population, whichever is higher. Qualifying rural investments receive enhanced incentives, including a larger basis step-up and a lower substantial improvement threshold – generally 50 percent of adjusted basis in a rural zone, versus 100 percent for non-rural investments.

These incentives may make a broader range of redevelopment projects economically viable, but they shouldn't drive the investment decision. Long-term outcomes still depend on the quality of the underlying real estate, underwriting discipline, capital structure and execution. Investors should apply the same standards here as to any other long-duration real estate strategy.

For RIAs, the permanent framework should make it easier to build Opportunity Zone strategies into deliberate, long-term client planning rather than evaluating them mainly in response to a near-term tax event. Ultimately, Opportunity Zone 2.0 strengthens the framework, but long-term success will still come down to manager selection, portfolio construction and consistent execution.

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Argosy Real Estate Partners is a real estate investment manager focused on opportunistic, core-plus, and Opportunity Zone strategies within the lower middle market (generally \$5 million to \$25 million equity investments). The firm invests primarily in emerging and established alternative property sectors, including build-to-rent, industrial outdoor storage, cold storage, lodging, life sciences, data centers, and residential land, while maintaining significant expertise in traditional sectors such as multifamily, industrial, retail, and office. Argosy has approximately \$4.0* billion in gross real estate assets under management and invests on behalf of institutional investors, family offices, and high-net-worth individuals across the U.S., Europe, and Asia. The firm has a 38-person team operating across three offices in Wayne (Philadelphia), San Francisco and Denver.

* Gross AUM includes \$4.0 billion of gross assets where AREP holds controlling interests and \$72.2 million of unfunded equity commitments as of Dec. 31, 2025.

CORPORATE OVERVIEW

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