

Global property securities market total returns

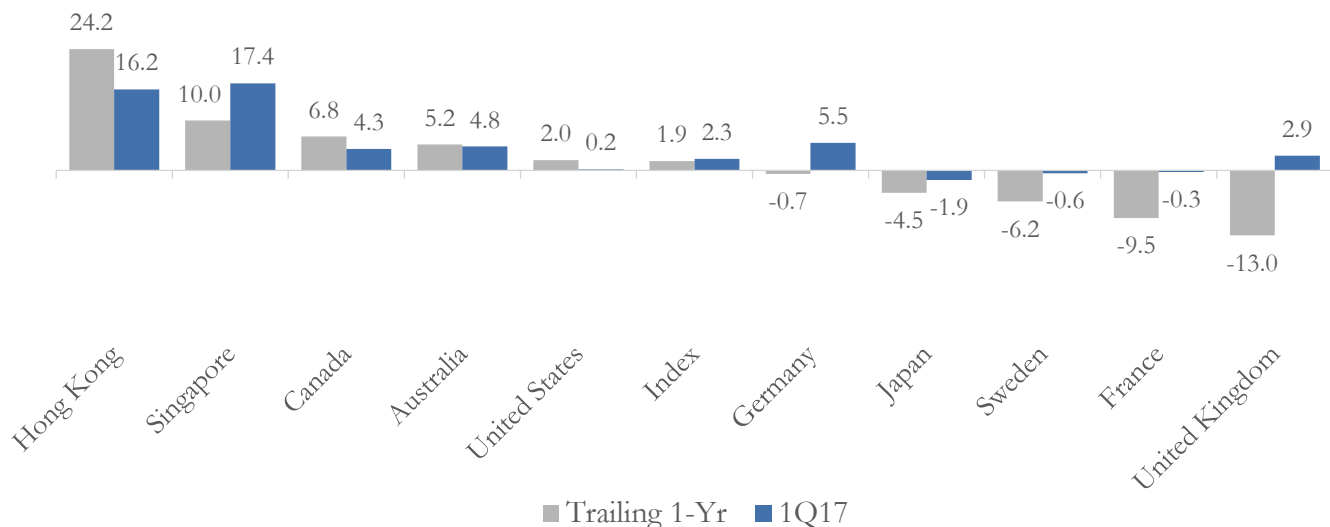
Index/region	1Q17	Trailing 1-Year
FTSE EPRA/NAREIT Developed Index ("Index")	2.3%	1.9%
Asia-Pacific	6.0	6.3
Europe	3.0	-6.4
North America	0.4	2.3
FTSE All World Developed Index	6.5	15.6
JP Morgan Global Aggregate Bond Index	1.5	-1.9

Source: Bloomberg, FTSE EPRA/NAREIT, and FactSet in USD.

Global property securities produced a 2.3% total return to start 2017, lagging the broader equity market, but outperforming bonds. A weaker USD provided a boost to returns outside of the U.S. in the quarter. While there was a focus on Donald Trump’s initial months in office and prospects for policy change to boost economic growth, the quarter ended with some doubts about the “Trump bump” since little has been accomplished thus far. To be fair, expectations regarding the timing for change and realizing any impact may have been unrealistic. Although the unpredictability of geopolitical events around the world remains a risk, global growth has continued to hold up and the current environment of steady growth and low rates can still be favorable for real estate provided that demand and supply remain balanced. **Worries about rising interest rates remain a potential headwind, but changes thus far have not been significant and to the extent future increases are measured and a result of improving growth, it would not necessarily be all bad news for real estate.**

Performance by Country (% in USD)

FTSE EPRA/NAREIT Developed Index



Source: FTSE EPRA/NAREIT and FactSet in USD for countries representing at least 1.0% of Index weight.

North America (57.1 % of the Index)	1Q17 Total Return		
	North America	U.S.	Canada
Index Weight	57.1%	54.2%	2.9%
Local Currency	0.4	0.2	3.7
USD	0.4	0.2	4.3

Source: FTSE EPRA/NAREIT and FactSet.

**North America was the weakest performing region globally in the quarter.** While Canada got off to a good start to the year, the U.S. was little changed overall, however there was a wide divergence in performance between property sectors.

The year started off in the U.S. with a wave of optimism that the newly elected Trump administration would be able to implement policy changes to provide an added boost to the economy and that interest rates were likely heading up given an improved outlook. After a failed attempt to “repeal and replace” the Affordable Care Act in March, the quarter came to a close with investors beginning to question President Trump’s ability to deliver on other campaign promises such as tax reform and increased infrastructure spending. While the FOMC delivered an expected rate hike in March, the U.S. 10-year Treasury yield actually fell 5 bps in the quarter to 2.396%, providing some indication of the uncertain outlook for the pace of economic growth.

In a slight reversal of the post-election reflation trade within U.S. REITs from the prior quarter, **relative performance during the quarter resulted in short duration property types such as Hotels giving back some of their 4Q16 gains and interest rate sensitive sectors like Health Care and Manufactured Housing bouncing back to be among the better performing sectors.** Data Centers also had a strong quarter, benefitting from a modest acceleration of leasing trends after a couple of quarters of softer bookings.

**One continuing trend in relative performance in the U.S. has been the underperformance of the Retail sector.** Investor sentiment on malls and shopping centers remains weak. Tepid holiday sales, news of department/retailer store closures, and the on-going threat of e-commerce are all valid concerns that investors are continuing to fully digest. The threat of e-commerce is also causing

some weakness in performance of retail property companies elsewhere around the globe, but the weakness is most pronounced in the U.S. given that America is far more over-retailed (i.e. much higher retail sf per capita) than other parts of the world. **While internet resistant formats like grocery anchored neighborhood centers and “A” quality malls are likely to outperform weaker retail assets and prevail over time, there may be little differentiation in retail for some investors until the rationalization of retail space has run its course.**

**The First Quarter may also have been an inflection point for the growth and investor acceptance of a burgeoning asset class that had its public market debut four years ago in the U.S. – rentals in the Single Family Housing Sector (SFHS).** The quarter witnessed the high-profile \$1.8 bn IPO of Invitation Homes, Inc. (INVH), Blackstone’s single family rental platform with a GAV of ≈ \$13 bn. M&A was also in the headlines with Silver Bay Realty Trust being acquired by Canadian listed Tricon Capital Group for \$1.4 bn in a transaction that made it the fourth largest public company in the nascent sector. Operating trends had already been on an uptrend, but the two transactions also highlighted the importance of scale as a driver of future efficiency/margin expansion. **With the improved visibility and solid operations, it is not too surprising that SFHS proved to be one of the best performing sectors in the quarter.**

**Canadian REITs had a solid quarter, benefitting from a slightly improved economic outlook for 2017 and a continued dovish monetary policy stance from the Bank of Canada.** Despite some better data in the quarter, the BOC kept rates unchanged at its two policy meetings in the quarter, noting both material excess capacity in its economy in contrast to the U.S. and uncertainty about the global outlook.

Asia-Pacific (27.1% of the Index)	1Q17 Total Return				
	Asia-Pacific	Japan	Hong Kong	Australia	Singapore
Index Weight	27.1%	10.6%	8.0%	6.0%	2.4%
Local Currency	2.7	-6.3	16.5	-0.6	13.5
USD	6.0	-1.9	16.2	4.8	17.4

Source: FTSE EPRA/NAREIT and FactSet

**Asia-Pacific was the best performing region in the quarter on both a local currency and USD basis.** Reversing weakness from the prior quarter, strengthening local currencies versus the USD benefitted USD total returns for most countries. Both Hong Kong and Singapore stood out in delivering the best total returns for the quarter.

**Hong Kong rebounded strongly from a weak 4Q16 on the back of strong results from Hong Kong developers.** Although the government has recently taken measures to cool segments of the residential market, such as foreign speculators, the natural demand growth in Hong Kong continues to exceed supply. This supply-demand imbalance has created natural pricing tension across the housing spectrum with residential condo prices continuing to have an upward bias. Sun Hung Kai delivered strong total returns in the quarter as investors reacted favorably to strong net profit growth that resulted from the completion of a large Hong Kong condo project. Wharf Holdings was the best performing stock in Hong Kong (+32.1% total return), boosted by the news the company was considering spinning off its investment portfolio to separate it from its property development activities. The announcement came in conjunction with 2016 results which delivered core profit growth of 25%, reflecting strong bookings in its development segment and stabilizing retail conditions in Hong Kong.

**Singapore property securities also delivered strong performance in the quarter with developers having exposure to the Singapore residential market benefitting from a surprise easing of housing policy by the government.** The regulatory tweaks came after almost five years of declining house prices and represented the first relaxation of measures in the private residential sector since the current tightening cycle began in February 2010.

**Japan was the weakest performing country in the region in the quarter as both the Japanese Developers and JREITs delivered negative local currency total returns of -4.3% and -9.9%, respectively.** The developers reversed some of their strong outperformance of the previous quarter and were also negatively impacted by a strengthening Yen versus the USD. Expectations of rising interest rates in the U.S. are also raising questions as to how long the Bank of Japan can persist with its QE program and continue to peg the 10-year interest rate near 0%. JREITs are finding it more difficult to invest as the spread between property acquisition yields and the marginal cost of debt narrows.

**Australian property stocks delivered mixed returns in the quarter. A-REITs with residential exposure and office exposure fared better than those with retail exposure.** The residential markets in Sydney and Melbourne are experiencing continued strength despite attempts by regulators to temper price growth. The Sydney office market also continues to benefit from limited supply and the withdrawal of stock for redevelopment, residential conversions and the new Sydney metro train line. Conversely, retail REITs reported mixed results with improving leasing spreads and NOI growth tempered by continued slowing in tenant sales growth. Some of the weakness may also be related to the increasing market speculation that Amazon is preparing to set up an Australian retail platform in the not too distant future. Given the disruption that Amazon and e-commerce has been causing in the U.S., investors are likely being cautious. **Notwithstanding some structural differences between Australia and the U.S. (i.e. half the retail space per capita and lower exposure to department stores and apparel), e-commerce is affecting retail globally and will be closely watched in Australia.**

Europe (15.8% of the Index)	1Q17 Total Return					
	Europe	U.K.	Germany	Sweden	France	Europe (ex U.K.)
Index Weight	15.8%	4.9%	3.2%	1.2%	3.2%	10.9%
Local Currency	1.6	1.7	4.0	-2.3	-1.7	1.5
USD	3.0	2.9	5.5	-0.6	-0.3	3.1

Source: FTSE EPRA/NAREIT and FactSet.

After a difficult 2016 in which the region was impacted by the surprise outcome of the Brexit referendum, Europe had a positive overall start to the year. USD returns were positively impacted in the quarter by some strengthening of most local currencies versus the USD, reversing a trend that persisted in 2H16 following the Brexit vote.

Reversing their relative underperformance in 4Q16, German residential companies had a solid quarter that enabled Germany to lead the way in Europe in the quarter. An increase in the spread between the French and German 10-yr bond yields in the quarter provided some measure of fluctuating French election worries. The spread was as high as 84 bps in February, but managed to end the quarter at 66 bps, a 12 bps increase since the start of the year. The residential sector's defensive characteristics, together with sound operating fundamentals and steady growth, proved attractive to investors in an uncertain political climate.

The spread in total return between U.K. property securities and Europe (ex U.K.) was tight relative to recent quarters; however, there was dispersion in performance among countries within Continental Europe. In the nine months since the Brexit referendum vote, the U.K.'s economy has held up reasonably well relative to the more bearish expectations at the time. With the U.K. just recently triggering Article 50 to commence formal negotiations with the E.U. on the terms of its exit, it remains too early to fairly assess what the long term impact will be to the U.K. economy. Despite continued stable operating results and some headline sales at better than expected pricing, the London office sector remains the most discounted in the U.K., while the logistics and self-storage sectors were the best performing in the quarter in the U.K.

While economic data has shown signs of improvement across parts of Europe, political

risk remains a potential disruption to sustained growth. Investors got some relief in March when the incumbent conservative government prevailed over the far-right populist candidate in the Dutch general elections. Ahead of the French general election in April, the Dutch election was viewed as a test of the anti-Euro, populist sentiment that had been gaining across parts of Europe since the surprise outcome in the Brexit referendum last summer. Although they recovered some late in the quarter after the Dutch elections, worries about the potential threat posed by far-right candidate Marine Le Pen in the French elections were likely a factor in the relative underperformance of many French companies. Share prices of retail focused real estate companies on the continent were also weighed down by the added concern of the changing retail landscape that has hurt the share performance of many U.S. retail REITs of late. Investors were caught off guard by the unexpected change in CEO at Paris office focused Gecina S.A. early in the quarter, but the share price experienced some recovery late in the quarter.

Swedish listed real estate companies were notable underperformers for a second consecutive quarter despite a mostly healthy operating environment and continued healthy economy in Sweden. The group has lagged in relative performance versus much of the region since the latter part of 2016 over the impact of potential changes in Swedish tax legislation. The proposed legislation was announced late in the quarter and would eliminate loopholes that allow parties to defer/eliminate transfer and capital gains taxes on property sales, potentially slowing the transaction market and causing some adjustment in property values. News subsequent to quarter end that the timing for implementation of the proposed changes may be in question and delayed beyond 2018 added some confusion of the potential near term impact for share prices.