STRICTLY FOR PROFESSIONAL INVESTORS

Listed real estate

A VALUABLE ADDITION TO YOUR PORTFOLIO

Kempen

Take a digital platform containing data on 300 real estate companies and 200,000 properties worldwide. Add our investment expertise on the real estate market. This is how we reach rational, well-argued and transparent investment decisions. Welcome to the world of listed real estate. Allow us to tell you more.

'With big data we can accurately analyse the quality of real estate and select the best real estate funds.'

JORRIT ARISSEN
Co-head real assets of the Kempen Real Estate team on the bottom-up approach.

Listed real estate is an umbrella term for listed companies that invest in real estate. Income is derived from the rental of these buildings. The companies often specialise in a specific type of real estate, such as shops, offices, homes or distribution centres. These four types make up about 90 percent of the real estate market. The remainder comprises smaller types, such as healthcare real estate, storage units, data centres and hotels.

Many real estate funds pay out annual dividends to their shareholders. This dividend yield can be appealing, especially to private investors, as it provides a periodic income. At this moment[1] average dividend yields on real estate funds have been about 3 to 3.5 percent a year.

A large proportion of real estate funds are REITs (Real Estate Investment Trusts). These REITs are not subject to corporation tax. In exchange, they are legally obliged to pay out a specific percentage of their profits as dividends.

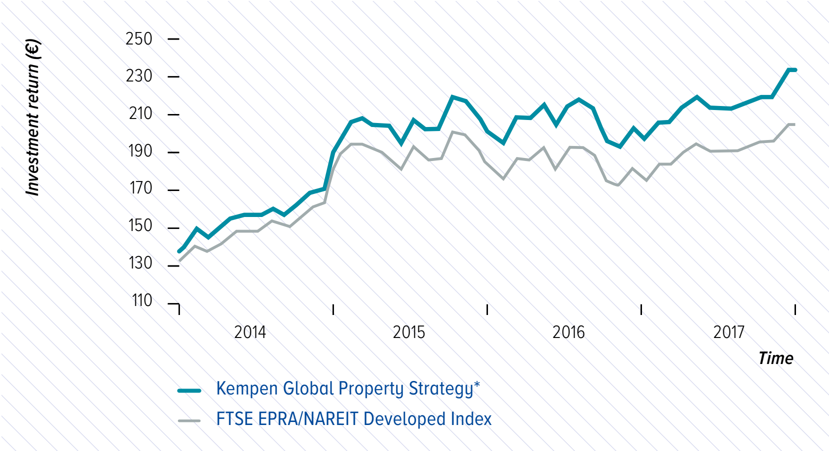
The REIT status has led to enormous growth in listed real estate around the world. Back in 1990, less than 1 percent of the MSCI World global equities index was invested in real estate, nowadays this percentage stands at 2.8 percent1.

How profitable is listed real estate?

When you look at the medium term – between three and seven years – an investment in listed real estate generally yields a stable and predictable return. The risk/return ratio of listed real estate tends to fall somewhere between that of bonds and equities. Kempen Capital Management (Kempen) has applied a bottom-up strategy based on big data

1 *August 2016.*

analysis and information technology for about five years. Via this strategy we aim to earn a higher return than the benchmark (FTSE EPRA/NAREIT Developed Index), but at a considerably lower risk. We call this Alpha by control[2].



Source: Kempen Capital Management, 31 December 2017.

FIGURE 1. Kempen has applied a bottom-up approach to its global strategy for the past two years, and in doing so has achieved a lower risk profile.

‘We can demonstrate in detail what investments are doing with respect to sustainability.’

EGBERT JAN NIJMEIJER
Co-head real assets of the Kempen Real Estate team on big data.

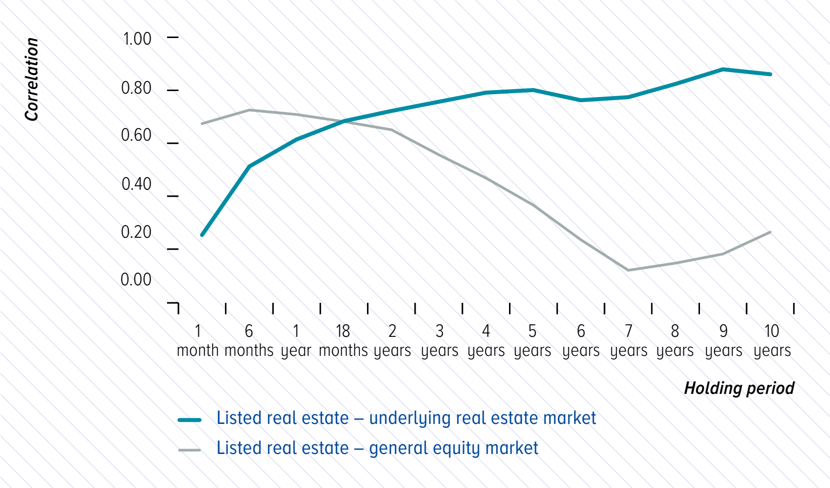
What are the characteristics of listed real estate?

We distinguish four main characteristics of listed real estate that make it an attractive investment:

1. A low correlation to other asset classes

There is a low correlation between listed real estate and other asset classes (see figure 2). This makes it a distinctive asset class that can provide risk diversification within a portfolio. Portfolios are constructed so that any lesser performance in one part can be compensated by a sound performance elsewhere. This so-called diversification benefit mainly works in the longer term.

2 *‘Alpha’ stands for the portfolio return minus the benchmark return. ‘By control’ means that the periodic diversification of the return and the risk, remains within set values..*



Source: Kempen Capital Management, data range December 1989 - December 2017, listed real estate = FTSE/EPRA Europe Dev., general equities = Euro Stoxx 600, non-listed real estate = Degeared EPRA Europe (NAV).

FIGURE 2. Listed real estate correlates to the equity market in the short term.

2. The real value of real estate

Real estate is what is known as a real asset class, i.e. an asset class with a physical core: buildings. These have a price in their day-to-day use (rent), which is generally adjusted to inflation. This makes listed real estate an inflation hedge: rent indexation provides full or partial protection against monetary depreciation, one of the risks of longer-term investment.

3. A relatively stable cashflow

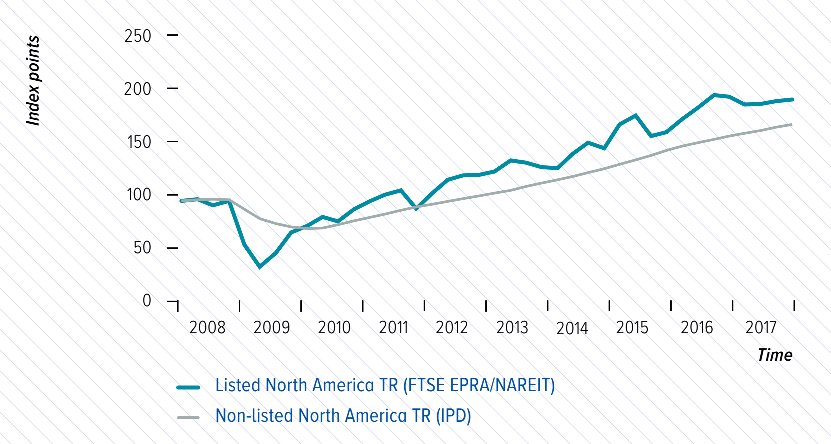
Cashflows from real estate, such as rent, operating expenses and maintenance, are more reliable and stable than is the case for general equities. Cashflows are reasonably predictable in the medium term of three to seven years.

4. Benefits compared to direct real estate

Compared to direct real estate, listed real estate offers more options for diversifying investments. Say that an institutional investor wishes to allocate 100 million euros to physical real estate, then that sum is reached with only two to three shopping centres, depending on their size. That same 100 million euros can be used across a wider range of investments in a property investment fund. Moreover, listed real estate is more liquid and pricing is consequently also transparent. Real estate company equities can be traded on a daily basis, while investment in direct real estate is more or less ‘set in stone’. Furthermore, REITs usually have easier access to the (public) capital markets and are able to arrange efficient financing.

What do you need to be aware of?

Listed real estate has a relatively high level of volatility: prices fluctuate sharply. Yet this only applies to the short term: the market dynamics of listed real estate can be compared to those of the equity markets. In the longer term of five to seven years, prices evolve in the same way as non-listed real estate and yields are similar: see figure 3.



Source: KCM, FTSE, MSCI.

* *The value of your investment may fluctuate. Past performance provides no guarantee for future returns.*

FIGURE 3. Historically, listed and non-listed US real estate enjoy similar yields in the medium term.

A second aspect worth noting is the valuation of real estate: real estate companies have their properties assessed by valuers. These do not always apply uniform valuation standards. Kempen conducts its own assessment of the underlying properties owned by these companies. We do so using up-to-date and reliable data from prestigious and specialist data suppliers.

How do we select companies?

Kempen applies a bottom-up approach. This means that we examine the quality of the approximately 200,000 buildings owned globally by 280 listed real estate companies. Big data and a disciplined investment process are essential here. To this end, we work together with data vendors, such as GeoPhy and CACI, and process their data into our digital platform. This might include data on aspects such as ceiling height, footfall, accessibility and energy consumption of the buildings. This allows us to take into account the heterogeneous characteristics of properties.

'We know the financial leverage of each fund in which we invest.'

LUCAS VUURMANS
Portfolio manager of the Kempen Real Estate team on accountability.

We select our sources carefully and regularly verify the reliability of data. For instance, we might take a look for ourselves in a shopping centre which a source claims has high-quality tenants. The platform we use needs to be properly programmed in order to support an investment decision. The experienced real estate team specialists have therefore worked out several scenarios and inputted these into the platform.

In addition, we examine the modus operandi of real estate companies, for instance, in relation to their debt positions and corporate governance. We then combine this information with our continuous analysis of relevant trends on the real estate market, such as the impact of online shopping on physical stores and distribution centres: which remain competitive and which do not? We call this active approach data-based property investment.

Why active management?

The market for listed real estate is relatively inefficient. Different types of investors apply different strategies. Institutional investors, such as pension funds and insurers, sometimes allocate a fixed portion of their assets, while there are also investors who mainly respond to macro-economic trends. As a result, not all investors value market information in the same way. This provides opportunities for identifying companies of which the price and quality diverge and in doing so earn an above-average return.

Tracking down undervalued real estate companies requires an active approach. As soon as we suspect that a real estate company is undervalued, we conduct an analysis. If this analysis confirms our suspicions, we zoom in on the financial data and the quality of the company. Among other things, we examine its management, ESG (Environmental, Social and Governance) factors and the robustness of its balance sheet. Finally, the entire real estate team discusses the company as an investment case. We then conduct a joint assessment of the price/quality ratio of the property and the real estate company. And together we decide whether we wish to invest in the company. This focused approach means that we only invest in companies with the best-possible risk/return ratio.

Why choose real estate at Kempen?

Thanks to our experienced international real estate team, our consistent investment process and our data infrastructure, we lead the way in our field and are able to:

- accurately analyse ourselves the quality and rental growth potential of buildings around the world;
- reach rapid but rational investment decisions;
- offer clients complete transparency into their real estate investments at any time;
- offer clients a fully customised service;
- if applicable, offer clients a total real estate analysis with a view to combining listed and non-listed real estate.

The real estate team specialists themselves invest in our real estate investment funds, because we believe in the alignment of interests at Kempen.

IN SUMMARY

Listed real estate is a stable and relatively predictable strategy which can introduce greater diversification to your portfolio. Thanks to the application of big data and information technology, Kempen can accurately analyse the quality of global real estate and in doing so select the best real estate funds for you.

About Kempen Capital Management

We are a specialist asset manager that operates with a strong focus and clear investment vision. We focus on investment strategies in which we aim to be a world-class player. In addition to listed real estate, these strategies include small-caps, high dividend equities, euro credits and hedge funds solutions.

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