American Realty Advisors

House View: H1 2021

Investment Outlook

AMERICAN REALTY ADVISORS
INSTITUTIONAL CAPITAL MANAGEMENT

U.S. Real Estate Investment Outlook – H1 2021

Invigorated by policy support and vaccine distribution, the U.S. economy is poised for growth

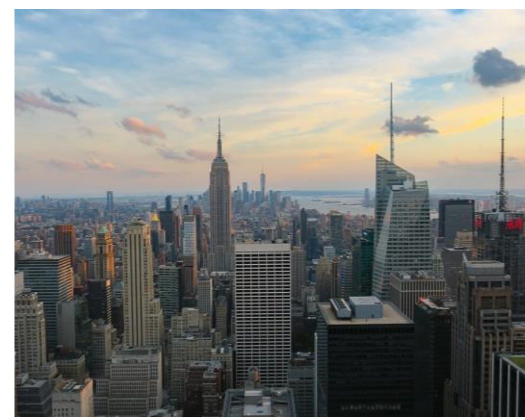
Macroeconomic Context

- As expected, the recovery received a double shot in the arm with the increased availability of vaccines and a further round of stimulus under the Biden administration.
- We expect U.S. GDP to expand by ~6.5% for the year.
- Divergences in the labor recovery (age, income, education level) remain a risk; how cities seek to solve increasing inequalities could drive policy for decades to come.

Real Estate Markets

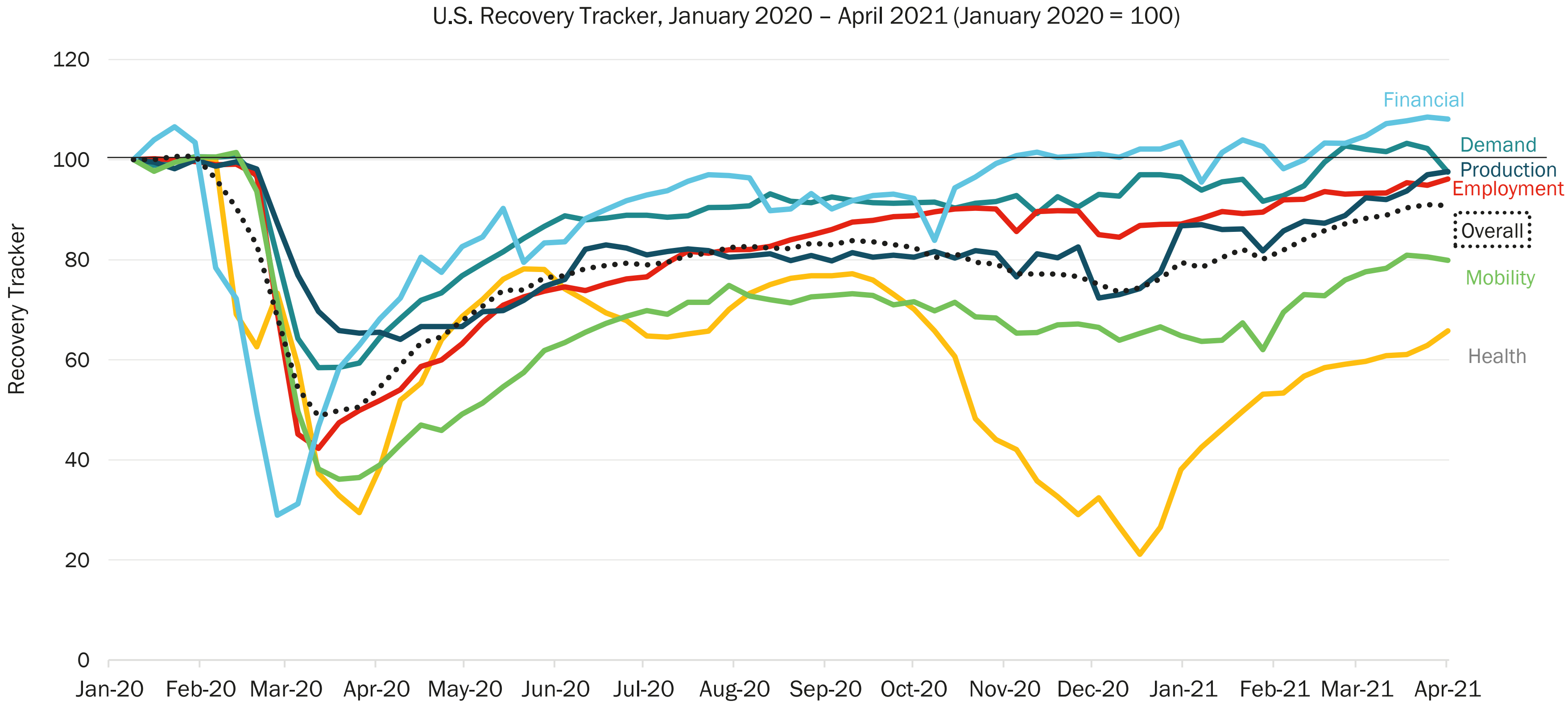
- Industrial fundamentals have continued their fiery streak unabated, as occupiers continue to shore up their inventories.
- Except for hotels, distressed real estate deals in other sectors have not materialized as some capital raisers had hoped.
- With a lower return environment expected across asset classes, many investors have increased their target allocations to real estate.

Images: (Above) Bolstered household finances from the latest stimulus round are driving a renewed resurgence in demand for goods. (Below) Companies are beginning to cautiously call employees back to the office.



Current State of Play

While health concerns remain the predominant constraint, many facets of the U.S. recovery are nearing pre-pandemic levels

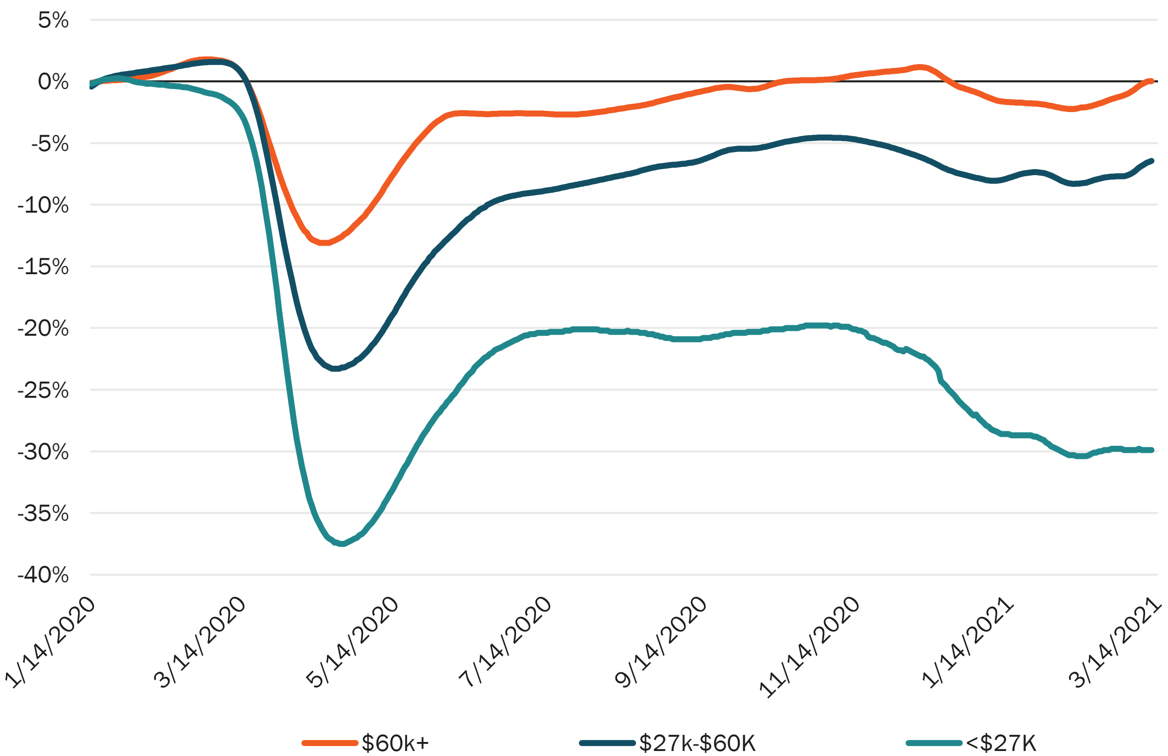


Oxford Economics' National Recovery Tracker examines six dimensions relative to their pre-pandemic state. Each index is calculated as the equal-weighted average of multiple high-frequency indicators.
Source: American Realty Advisors based on data from Oxford Economics as of May 2021

Employment Backdrop Strengthening, But Not For Everyone

Disparity in recovery for low-wage earners suggests there remains a ways to go to achieving full employment

Change in employment rates among workers by wage bracket, January 2020 – March 2021



- The national unemployment rate has improved meaningfully from the 14.8% peak recorded in April 2020, and currently stands at 6.1%.
- Yet gains have been uneven across the income spectrum.
- Relative to January 2020, employment among those making $60K+ was back to pre-pandemic levels as of March, while those making less than $27K remained 30% below pre-pandemic levels.
- While many of these roles are concentrated in services that are heavily reliant on in-person contact and thus should return as openings progress, it will take time to absorb the slack.

Note: Percentages reflect employment percentage relative to January 2020 baseline. Data is not seasonally adjusted.
Source: American Realty Advisors based on data from the Opportunity Insights Economic Tracker, Earnin, Intuit, Kronos and Paychex as of April 2021

Considering the Backdrop for a "Roaring Twenties" 2.0

	1920's	2020's
Technological Advancement	• Progress in mass-production technologies post-WWI created new industries & increased productivity in existing ones.	• Acceleration in advancement and adoption of next-era technologies (biopharmaceuticals, AI, clean energy/electric).
Investment in Infrastructure	• Broader accessibility of the automobile prompted development of national highway network (~$1bn spent per year).	• Biden's green infrastructure package is an ambitious one (to the tune of $2tn) and would hasten shift to new, cleaner energy sources, though has many hoops to jump through before becoming reality.
Pent-Up Demand	• WWI and Spanish Flu curtailed activities; advent of affordable consumer conveniences (vacuum cleaners, washing machines, auto) prompted significant spending.	• In aggregate, U.S. households saved ~$1.6 trillion more than they otherwise would have – early indications are that pent-up demand, particularly for services, is already beginning to materialize in travel, F&B spending.
New Schools of Thought	• Greater prosperity brought about nouveau ideas and challenges to traditional norms; women gained the right to vote.	• Societal issues (racism, inequality, climate change) are at the forefront of public consciousness, prompting sweeping sociopolitical changes.

Capital Markets

Reading the Tea Leaves on Inflation

The recent retreat in long-term Treasury yields suggests bond market investors believe the forthcoming acceleration in inflation will be relatively short-lived

U.S. 10-Year bond yield, January 2020 – May 2021

- The unprecedented levels of stimulus, supply shortages and surging demand have prompted some to speculate the U.S. may be entering a new inflationary period.
- Yet despite what is sure to be higher inflation in 2021, Treasury yields have begun to modestly unwind from their March highs.
- It seems the persistent reinforcing of the Fed's new inflation policy framework is forcing market participants to back off expectations of additional rate hikes between now – 2023.
- We believe inflation to be a temporary factor over the next 1-2 years but does not present material downside risk to CRE.

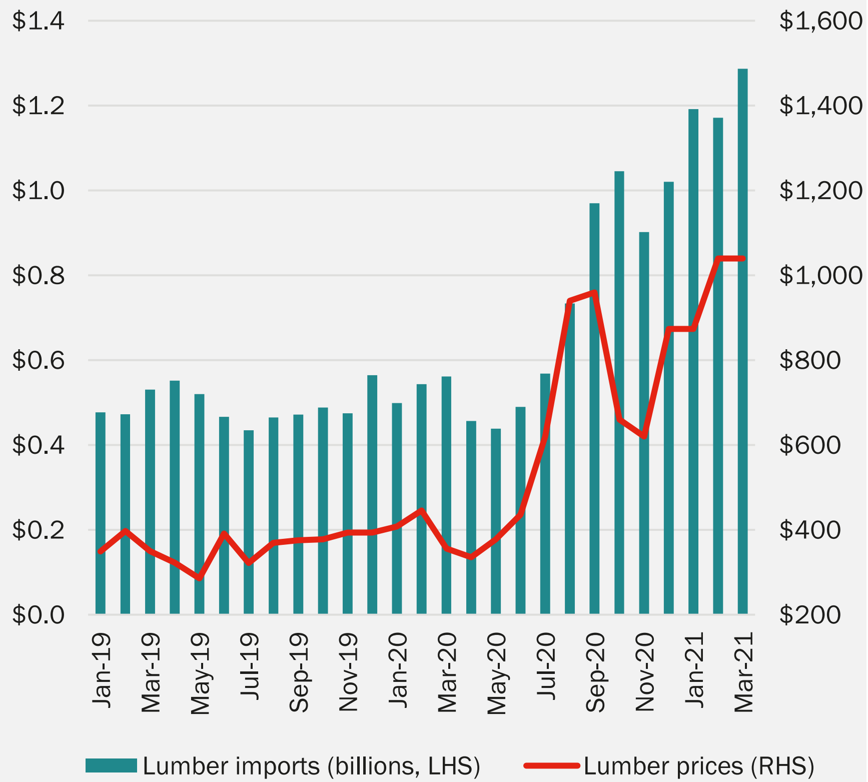
Source: American Realty Advisors based on data from Macrobond and Oxford Economics as of May 2021

Building Our Inflation Outlook: Lumber as a Proxy

Lumber costs are an oft-cited barometer of inflation given its specific impact on real estate, but pressures are expected to ease

- Lumber prices have skyrocketed in recent months, as strong demand + supply issues have culminated in a perfect pricing storm.
- Two supply valves are poised to release some of the pressure in the near- and medium-term:
  1) Lumber imports from Europe and Canada are on the rise given reduced tariffs and a strong USD, and
  2) Easing of domestic social distancing measures should allow mills to return to full capacity soon.
- It is these types of supply-demand lead-lag relationships that lead us to believe many price increases today are due to reopening adjustments that are expected to moderate as supply is allowed to catch up.

Lumber imports and prices, January 2019 – March 2021

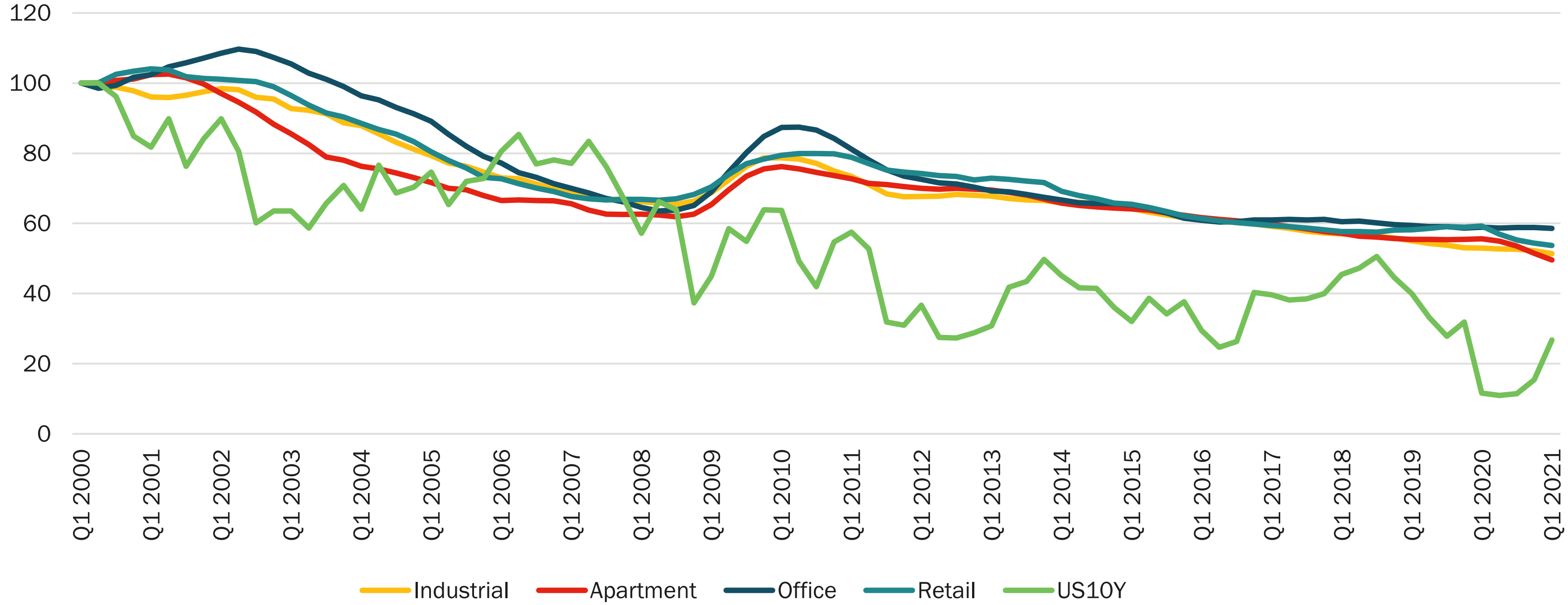


.Source: American Realty Advisors based on data from CoStar as of May 2021

What Impact Could Transitory Inflation Have on Cap Rates?

Real estate cap rates have demonstrated an ability to absorb modest increases in the 10Y in the past

Rolling quarterly U.S. cap rates by property type and 10-Year U.S. Treasury yields, Q1 2000 – Q1 2021 (Q1 2000 = 100)



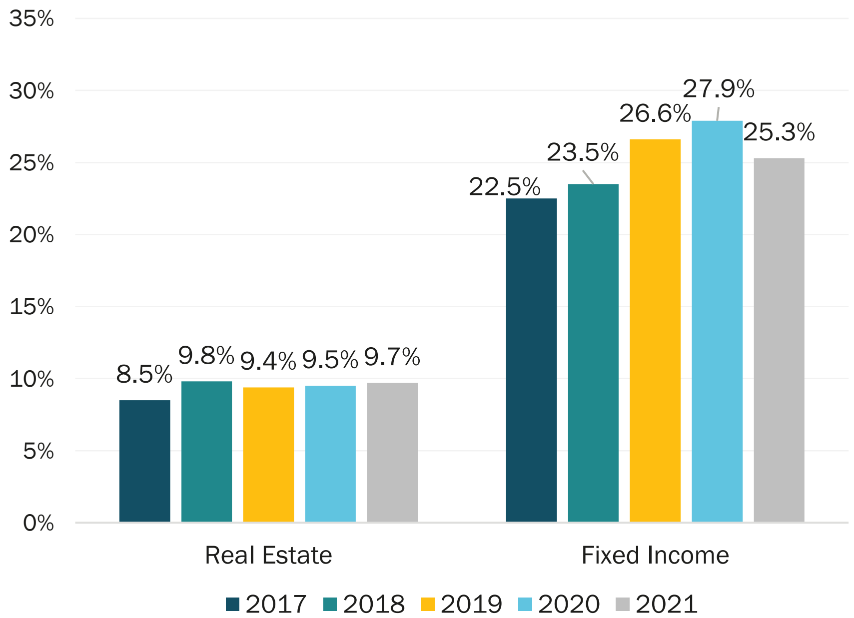
- Historically there has been the belief that when interest rates rise, real estate cap rates increase to account for the added cost to borrow capital; however, that has not always been the case.
- In fact, the U.S. 10-Year has had several bouts of short-term increases that have not produced a corresponding increase in cap rates.
- This is because cap rates are influenced not just by borrowing costs, but by other factors (capital dry powder, rising demand, reduced supply) that occur in a rising rate environment and keep values intact.

Note: Quarterly 10-Year Treasury data reflects the rate at the end of the quarter.
Source: American Realty Advisors based on data from Macrobond and NCREIF as of May 2021

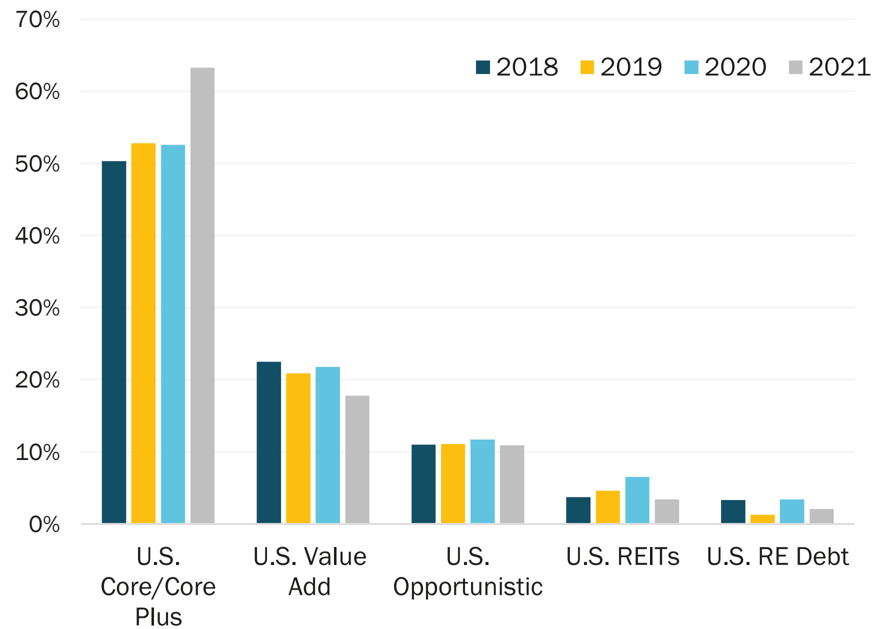
Appetite for Commercial Real Estate Continues to Grow

Target allocations to real estate continue to edge up, offsetting expected withdrawals from fixed income

Historical target allocations to real estate and fixed income, 2017-21



Historical target allocations by real estate strategy, 2018-21



- With expectations of low yields being offered in other perceived lower-risk asset classes (cash, fixed income), investors are increasingly looking to real estate to provide much-needed income.
- As a result, capital appetite for U.S. core/core-plus strategies has grown, serving as a value stabilizer throughout the recent uncertainty.

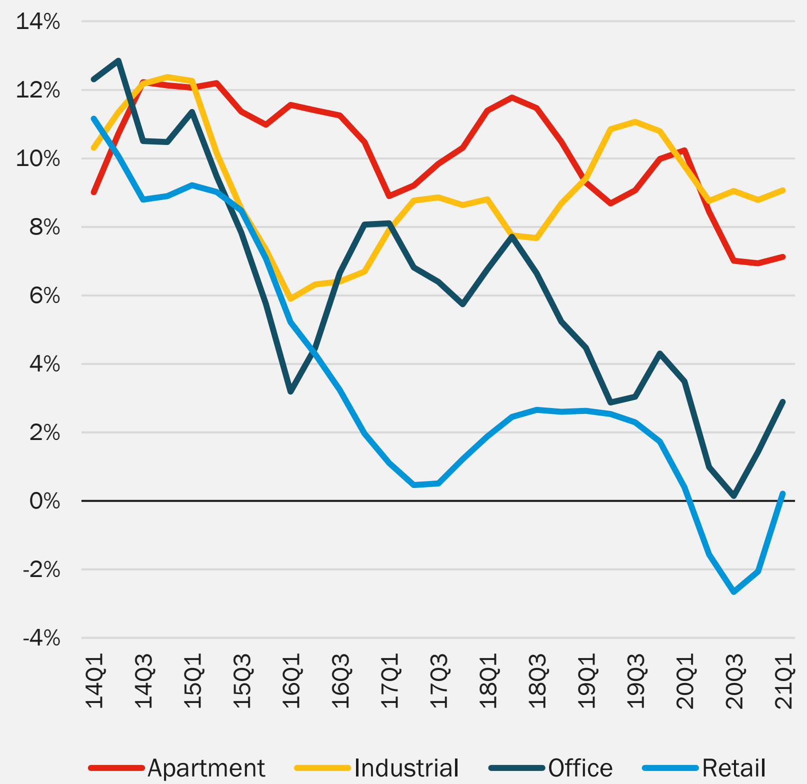
Source: American Realty Advisors based on data from the 2021 Institutional Investors Real Estate Trends report conducted by Kingsley and IREI as of May 2021

Real Estate Price Growth Continues

Property prices continue to expand, with growth firmly re-accelerating in hardest-hit sectors

- After the pause in transaction volumes in Q2/Q3 2020, volume surged in the fourth quarter as investors sought opportunities to deploy capital.
- This has had the effect of re-accelerating the pace of year-over-year price growth across sectors, buoying values (a phenomenon we anticipated in our H2 2020 House View).
- Given it seems that the lion's share of fundamental weakness is behind us and there remains significant dry powder earmarked for U.S. real estate ($250 billion), we expect values to continue to rise.

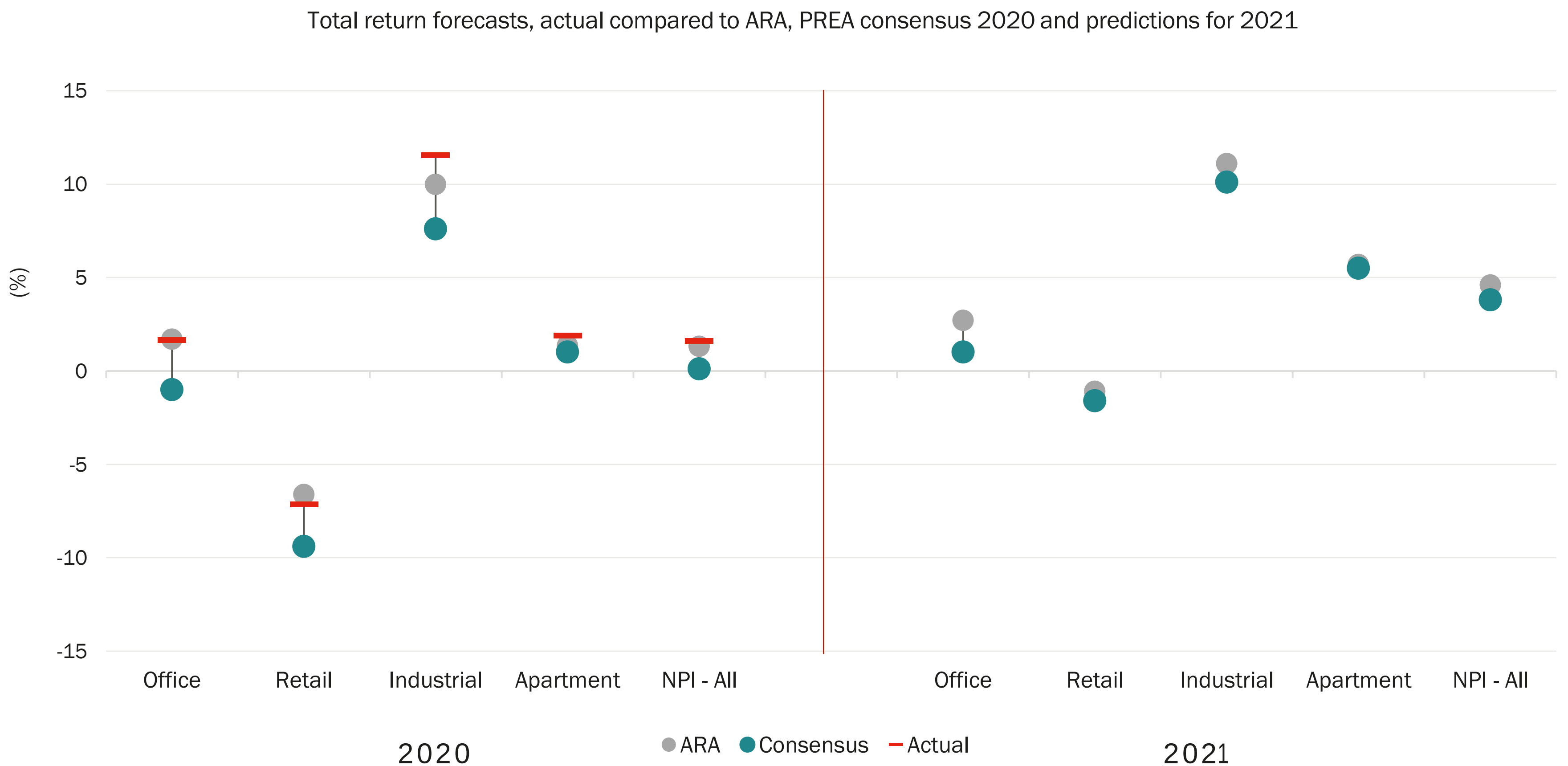
Year-over-year change in RCA CPPI by sector, 1Q 2014 – 1Q 2021



Note: Data reflects transactions of US $2.5 million and greater and includes individual, portfolio and entity-level transactions.
Source: American Realty Advisors based on data from Real Capital Analytics and Preqin as of May 2021

Leading With Conviction: The Outlook for Property Type Total Returns

ARA Research forecasts of total returns have been more accurate than the consensus, and suggest there is increasing reason for optimism



2020 total return forecasts are based on the November 2020 submission by ARA and the PREA Consensus Survey results. 2021 projections reflect the ARA submission as well as the overall consensus as of the February 2021 survey.

Source: American Realty Advisors based on data from the PREA Consensus Survey, November 2020 and February 2021

Property Markets

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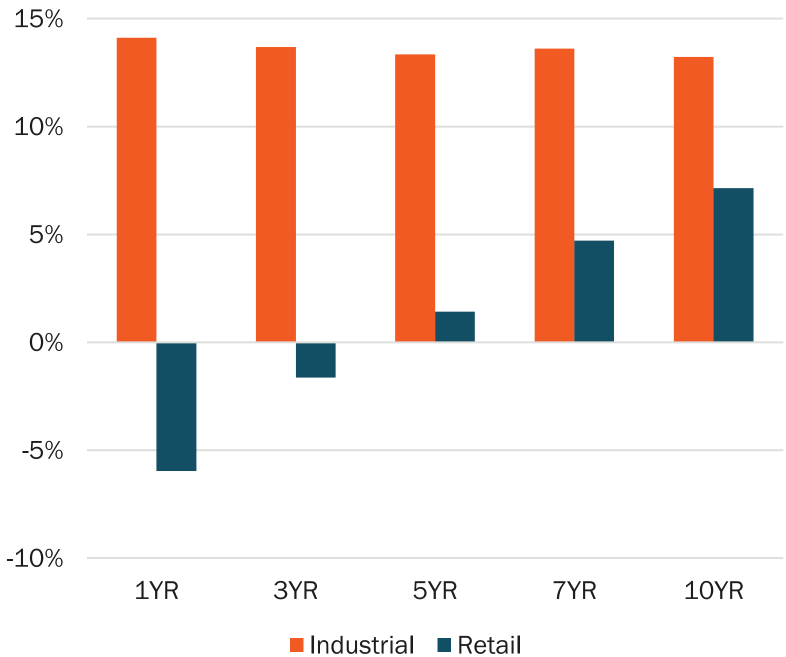
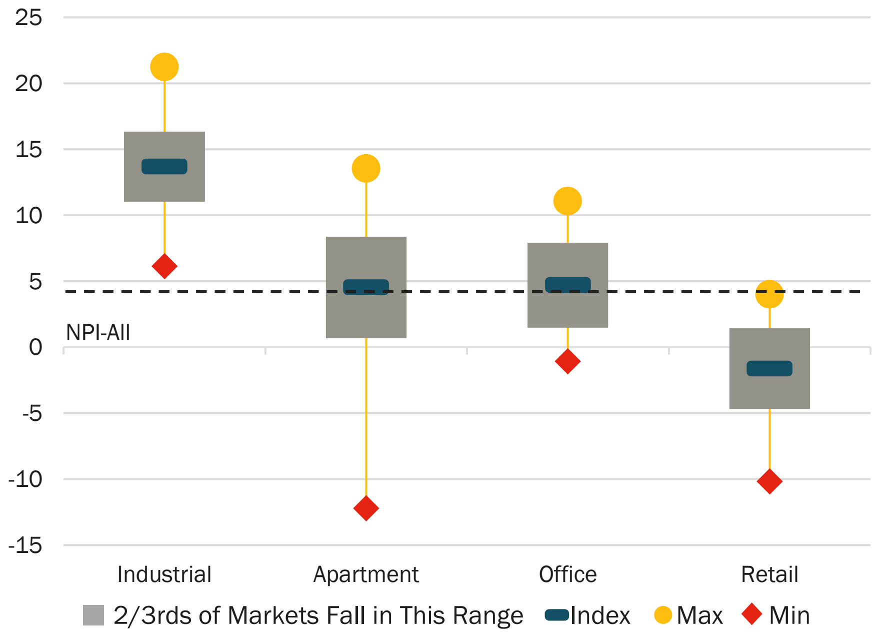
Growing Bifurcation Between and Within Property Types Continues

Return profiles continue to provide stark contrasts between property types and metros within each sector

NCREIF annualized returns, industrial and retail through Q1 2021



NCREIF annualized 3-YR returns through Q1 2021 range by sector %



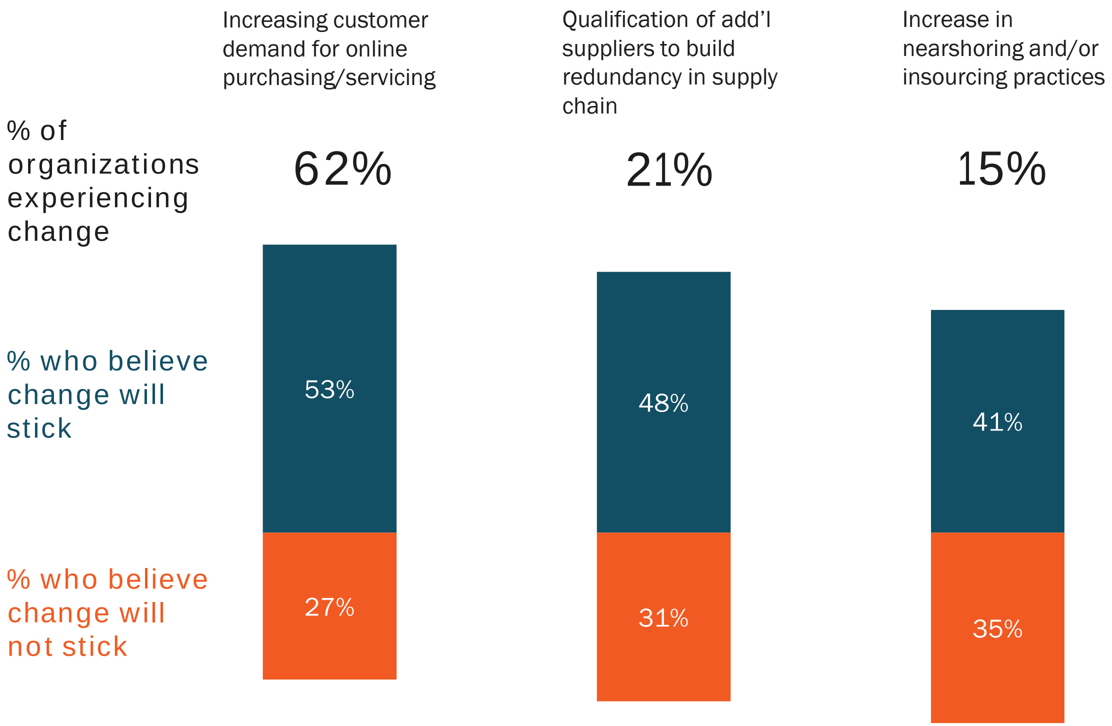
- Given a widening bifurcation between and within property types, sector, market/submarket and asset selection are the levers that, when pulled correctly, can drive return outperformance.
- Some sectors, like industrial, in aggregate have a greater share of markets that outperform the NPI ("go wide"), whereas the markets that outperform in others, like retail, are considerably smaller ("go narrow").

Source: American Realty Advisors based on data from NCREIF Property Index as of April 2021

Pandemic-Spurred Shifts in Supply Chains Boosting Industrial

Major shifts during the pandemic are increasingly likely to stick through the recovery, creating further tailwinds for the industrial sector

Shifts resulting from the pandemic by % of organizations experiencing the change and what share believe the changes will/will not stick



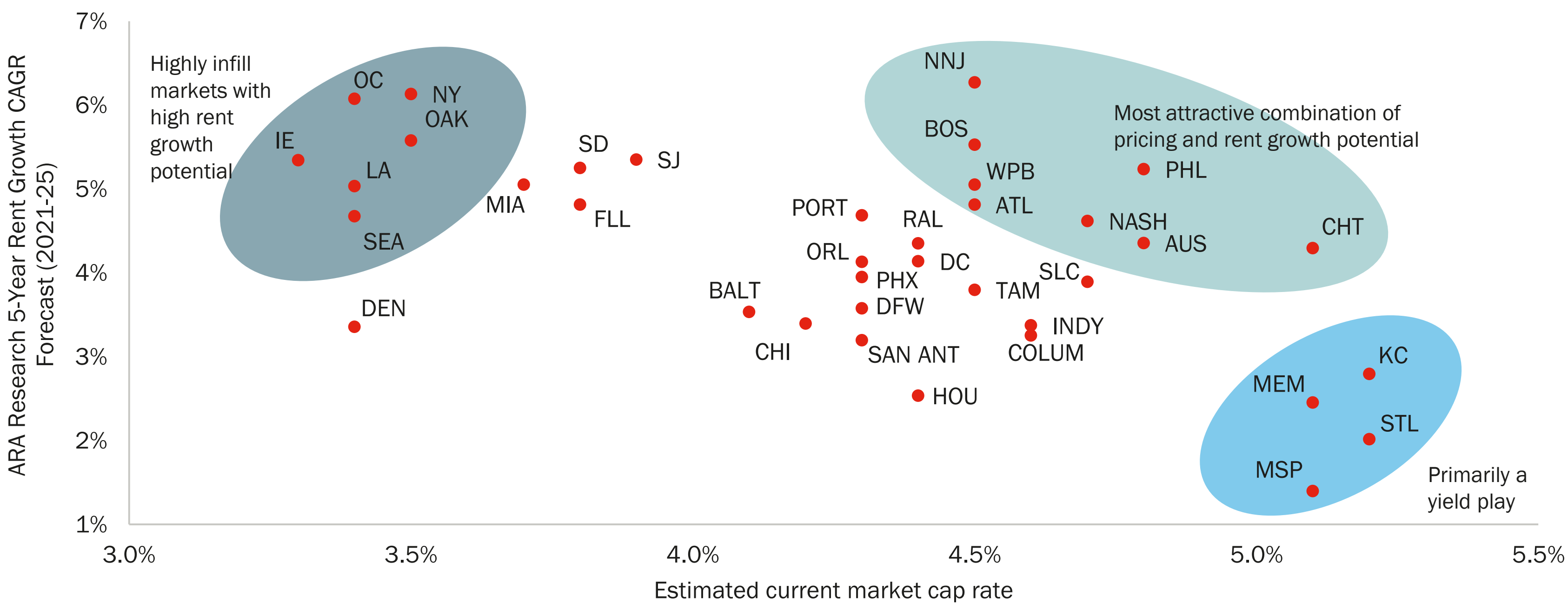
- The pandemic spurred major changes in the way consumers and goods suppliers interact, but also highlighted the fragility of "just-in-time" supply chain models.
- As a result, companies are being forced to re-evaluate their models with the long term in mind.
- Companies are preparing for increased demand for online purchasing, greater supply chain redundancies and increased near-shoring, all of which should serve to boost demand for warehouse space.

Source: American Realty Advisors based on data from McKinsey & Company survey report *How COVID-19 has pushed companies over the technology tipping point – and transformed business forever* dated October 2020

Balancing Price and Growth

With industrial a key sector focus for many, pricing relative to growth continues to be a critical lens

Estimated current market cap rate compared to ARA research 5-year rent growth forecast

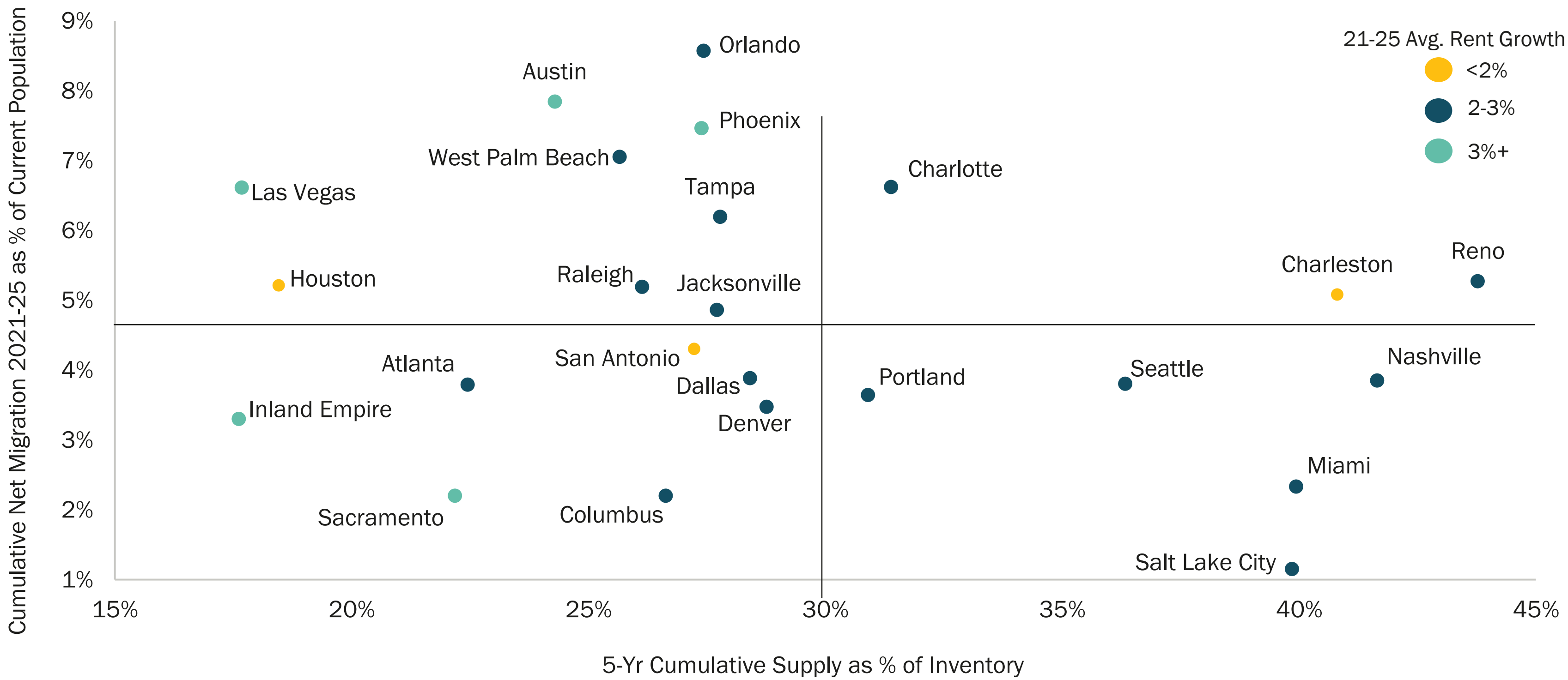


- Industrial cap rates continue to compress given the seemingly insatiable investor and occupier demand.
- While the outlook for the sector remains robust, investors should hedge going-in pricing relative to prospects for future rental rate growth.
- At a 3.37% rent growth CAGR, a going-in cap rate of 4.6% in Indianapolis is relatively less appealing than a 4.5% cap rate in Atlanta with a 4.8% rent growth CAGR – so market selection, even in a hot sector, is still key.

Note: Estimated market cap rates are based on CBRE-EA estimates as of Q4 2020, adjusted downward by 50 bps to account for actual transaction cap rates.
Source: American Realty Advisors based on data from CBRE-EA and CoStar as of May 2021

Multifamily Market Selection: Measuring Migration (and Supply)

The magnitude of in-**migration and level of supply exposure vary meaningfully across the "Smile" markets**



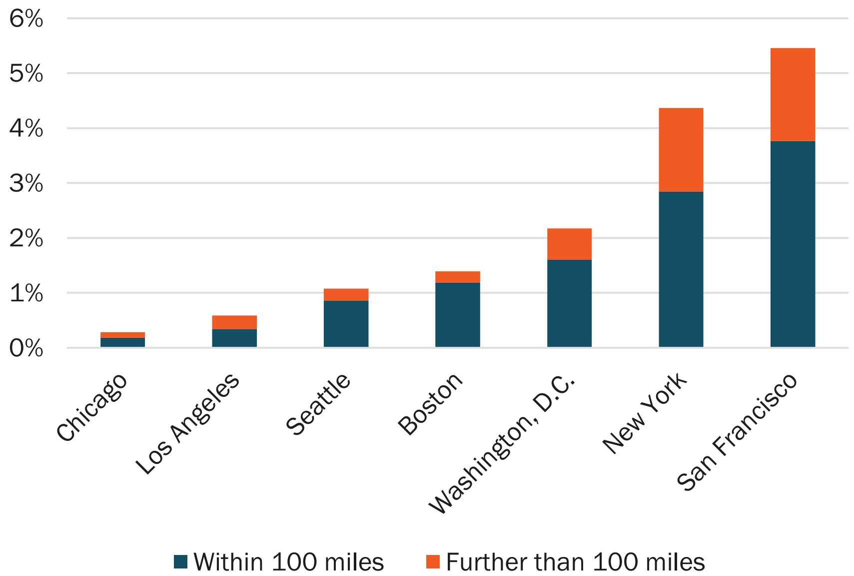
- There continues to be significant capital pursuing multifamily deals in Sun Belt/ "Smile" markets as investors follow renters south and west; yet not all these metros are created equal.
- We prefer a strategy that is focused primarily on those markets that have a supportive combination of both high in-migration and relatively less supply growth (like Austin, Phoenix and Raleigh), with a narrower focus in markets where market-level supply is expected to be higher.

Source: American Realty Advisors based on data from CoStar and ARA proprietary forecasts as of May 2021

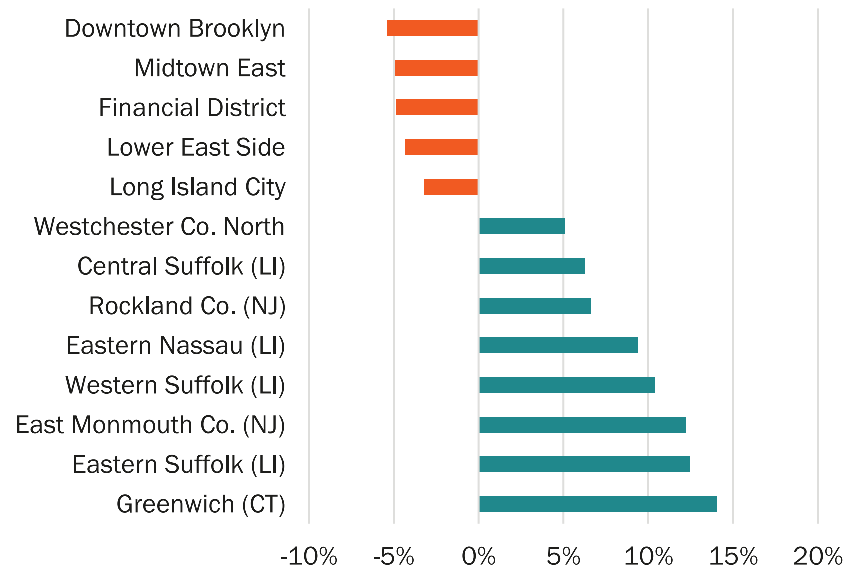
Urban Exodus? More Noise than Sound!

While headlines declared a mass migration from urban cores, most movers remained close to major metros

Total 2020 moves as a percent of 2019 population by distance



Effective 12-month rent growth, Q1 2021, NY/Tri-state submarkets



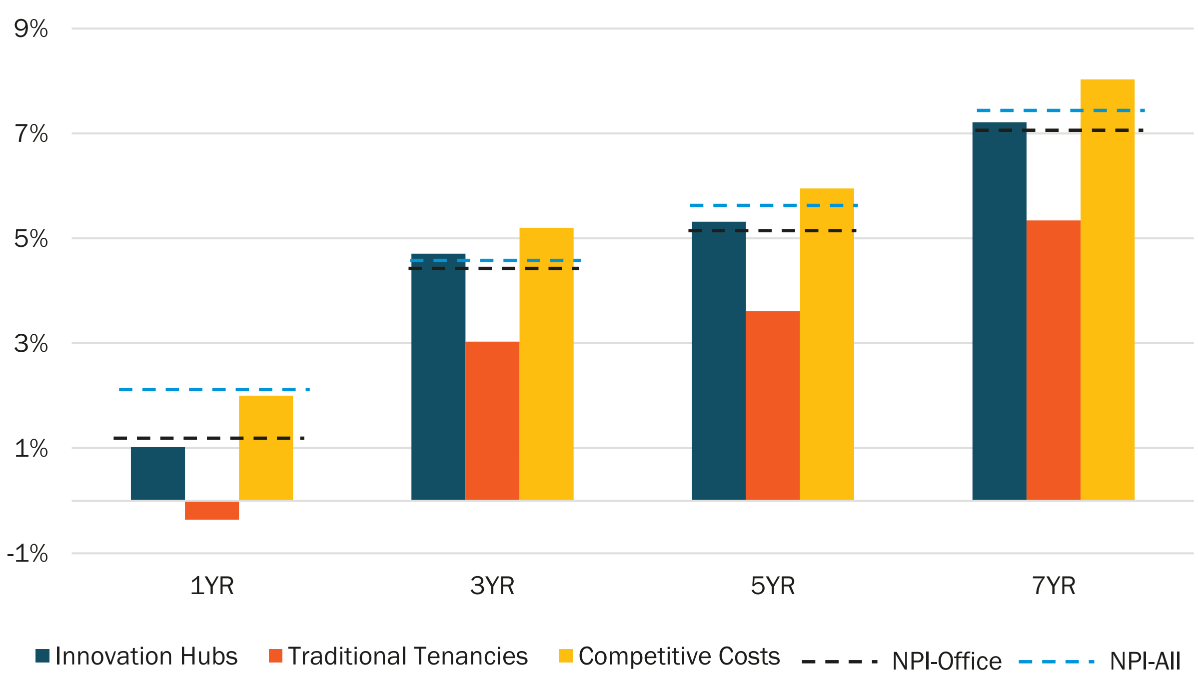
- As the pandemic wore on, residents' desire for larger dwellings and less density, prompted calls for the "end of the city".
- The data, however, shows that more movers stayed within 100 miles of the city, suggesting a more benign shift.
- We believe this widens the investable opportunity set in these markets, and hints that professionals are expecting employers to call workers back to the office imminently.

Source: American Realty Advisors based on data from CBRE, "COVDI-19 Impact on Resident Migration Patterns" and CoStar as of May 2021

Office Opportunities Beyond the Tech Heavyweights

Lower-cost office markets may also offer a compelling return profile

Value-weighted aggregate total returns of office markets by primary driver through Q1 2021



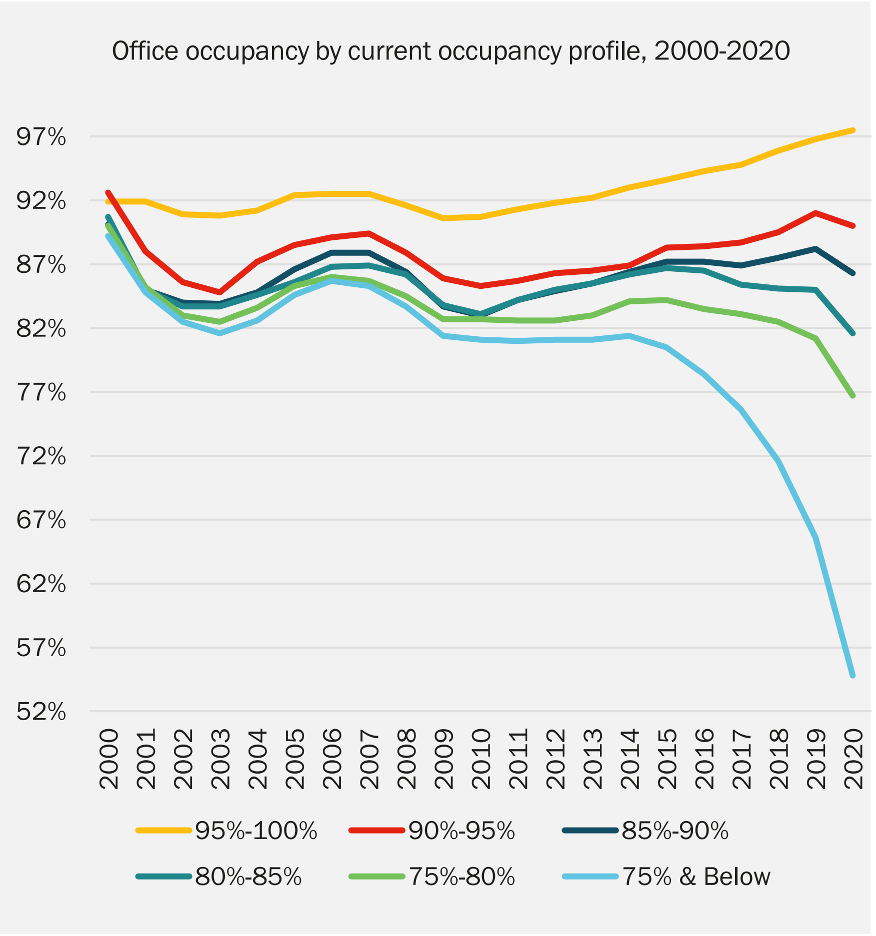
- Many office strategies over the last cycle have been centered on Innovation Hubs, with investors focused on capturing the growth from tech demand.
- Yet markets primarily driven by firms seeking lower cost structures have also offered a compelling total return profile.
- Markets in this category (such as Atlanta and Charlotte) consistently lead the pack, frequently beating out NPI-Office and NPI-All returns.
- While helpful in crafting thematic strategies, these groupings can mask meaningful variation in performance even within the same set – so market (and asset) selection is key.

Innovation hubs are markets where tech/biotech/creative are larger share of office-using employment growth than the national average. Traditional tenancy markets are those where FIRE employment growth represents a larger share of office-using employment growth than the national average. Competitive costs are markets with growth in a variety of office-using employment sectors with strong in-migration.
Source: American Realty Advisors based on data from NCREIF as of May 2021

Offices: The Best and the Rest

There seems to exist a persistency in office occupancy for best-in-class buildings; for others, it's a slippery slope

- The pandemic has reinforced bifurcations in performance between and within sectors, with the best doing better and the rest falling further behind.
- Knowing which assets have the staying power to continue to be "the best" then is critical to creating outperformance.
- Office assets that are currently highly-leased historically retain their elevated occupancy levels; however, this same persistency in performance is also true at the bottom, as buildings with occupancy below 75% today have seen a sharp erosion since 2014 that looks to be accelerating.
- Investors should aim to purchase only best-in-class office assets, which provide steadier demand performance, or acquire office product that lends itself to top-tier repositioning plays.

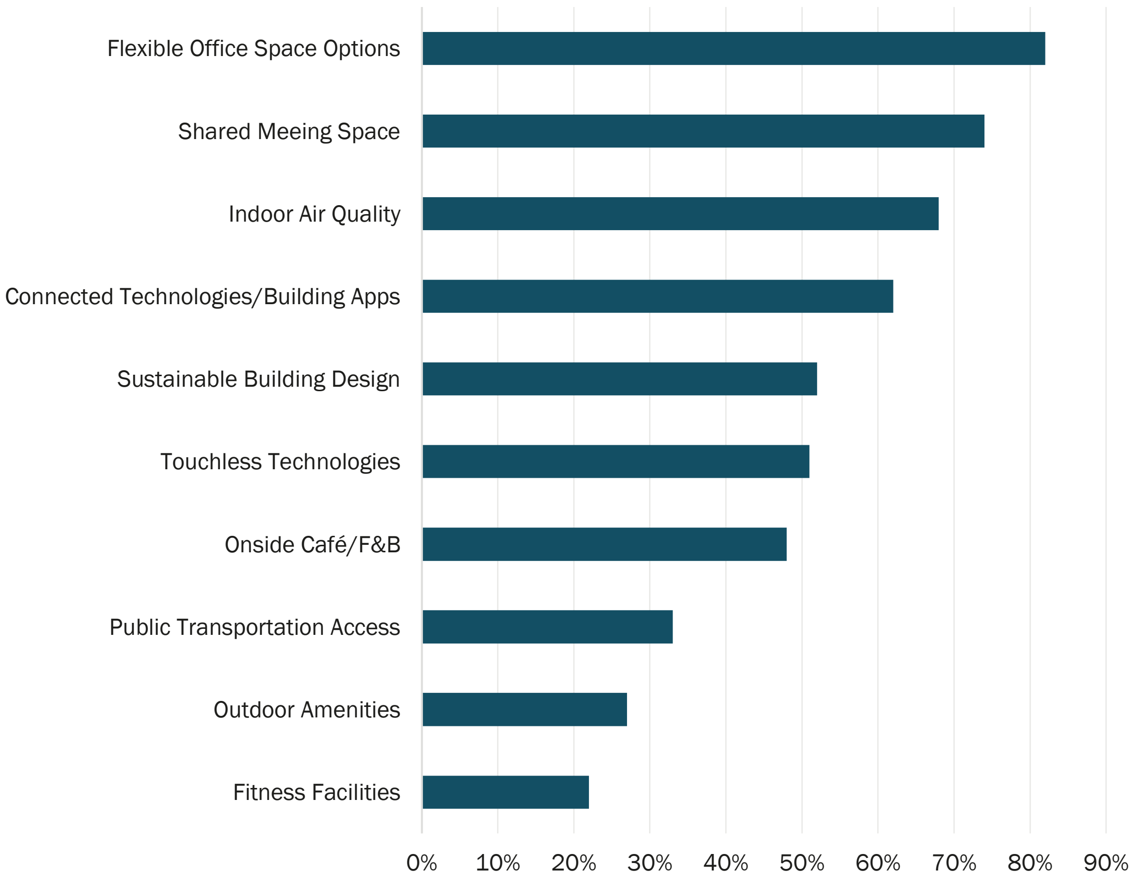


.Source: American Realty Advisors based on data from CoStar as of May 2021

Tenants Want More From Their Offices

The pandemic has increased focus on building offerings, creating obstacles and opportunities for owners

Percent of respondents – "What will be the most in-demand building attributes in the future?"



- Companies have now had a year to consider the role offices will play in their future.
- With an even greater emphasis on spaces that promote collaboration and culture, tenants are requiring more of their spaces to entice employees to return and justify the cost.
- Buildings that offer the ability to flex into/out of space as needed (coworking, shared meeting rooms) are expected to be in higher demand, as are those that maintain a high standard of health and sanitation.
- With ample space available, tenants can be picky.
- We believe the current environment creates opportunities for owners of differentiated, best-in-class office product to capture the lion's share of future leasing, though will create obstacles for lower-quality buildings that struggle to adapt.

Note: Data reflects the responses of 77 respondents who responded to the CBRE survey that closed September 21st, 2020, 50% of which are Fortune 500 firms.
Source: American Realty Advisors based on data from CBRE's *The Future of the Office* survey dated September 2020

Selecting a Specialty Sector: Why We Favor Single-Family Rentals

Confluence of strong foundational demand + cyclical cost elements + potential for cap rate compression-driven appreciation makes SFR an increasingly attractive complement to our existing residential strategies

Investment Case for Single-Family Rentals

- Significant capital appetite for the space, yet institutional penetration in segment still early innings (~2%) creates ability to ride capital compression wave.
- Construction, land prices rising (rents trend higher to account for costs)
- Limited for-sale availability driving rapid home price appreciation
- Student loan burdens, disadvantaged earnings potential post-GFC and pandemic prevent would-be buyers from being able to sufficiently save for a down payment
- Millennials getting married, having children (4.7MM)
- Downsizing Baby Boomers (4MM)
- COVID fuels demand for outdoor space

Source: American Realty Advisors based on data from Real Capital Analytics, NCREIF, John Burns Real Estate Consulting and CoStar as of May 2021

Outlook for Property Sectors

Industrial

- Increase in domestic stockpiling will further increase demand in the "too-hot-to-stop" sector.
- Demand for industrial assets in infill locations will continue to expand as growing e-commerce market heightens need for last-mile logistics centers.

Multi-Family

- As cities retained the lion's share of their residents, landlords are expected to be able to recoup pandemic-induced concessions.
- Sun Belt strategies should target cities with high in-migration and low incoming supply, which are likely to offer the strongest return opportunities.

Office

- Migration trends show most workers expect to return to the office, indicating WFH may be less disruptive in the long term.
- Best-in-class assets will remain in high demand as quality considerations evolve to encompass sanitation and space flexibility.

Retail

- Retailers will receive a boost as vaccination efforts and better weather allow officials to ease business restrictions.
- With the personal savings rate still significantly exceeding pre-pandemic levels, consumers are well equipped to act on pent-up demand this summer, particularly for services.

With post-pandemic optimism on the rise, opportunities are beginning to emerge in all real estate sectors.

Single-Family Rental

- Though SFR received a boost from the pandemic, demand is expected to persist long term as the segment fulfills the needs and wants of both downsizing Baby Boomers and upgrading Millennials.
- Investors will look toward build-for-rent neighborhoods as opposed to scattered purchasing strategies, as management of contiguous communities more closely mirrors that of traditional multi-family.

Implications for Core and Value-Add Strategies

Core

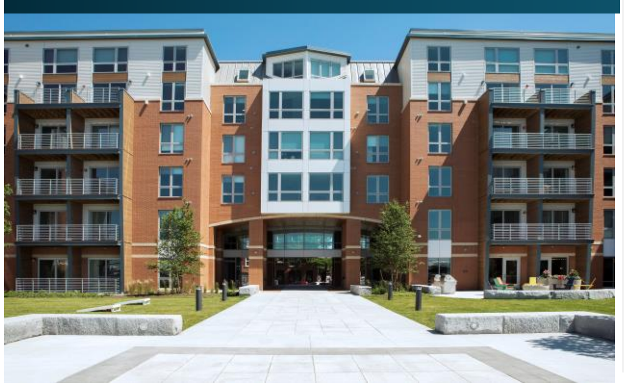
Asset Management

- Increase leasing rates in industrial and residential to drive income growth while continuing to “blend and extend” office and retail tenants.
- Control operating/capital costs and focus on re-engaging building services and tenant amenities for occupancy ramp up in 2H 2021.

Portfolio Construction

- Wide market focus on outperforming sectors, highly selective in others where strike zone for outperformance is narrower.
- Pivot office offerings to capture stronger life science demand.
- Add purpose-built single-family rental communities in high-growth markets as diversifier in residential allocation.

Value-Add



Asset Management

- Timely executive renovation and development business plans for residential and industrial assets to meet robust tenant demand.
- Continue to focus on leasing strategies for office/retail to increase occupancy, extend WALT and drive cash flow.
- Remain flexible and responsive to disposition opportunities where high buyer demand results in pricing premium.

Portfolio Construction

- Build, lease and sell stabilized single-family rental projects into deep capital pool.
- Move contrarian to office uncertainty for assets that have the potential to be best-in-class.
- Industrial demand expected to increase by 850 million sf by 2023, continue to pursue development/lease-up plays.

Summary and Strategy Implications

The pandemic era has intensified existing trends, reinforcing bifurcations between relative winners and losers.

- The U.S. economy's recovery in the first half of 2021 was stronger than we originally anticipated, enhanced by an accelerated vaccine distribution and further governmental stimulus.
- We expect full-year 2021 to be one of the strongest for GDP growth in recent memory, with a period of above-trend growth for 1-2 more years.
- While this should serve to boost real estate fundamentals overall, we believe the pace of structural change has been accelerated, widening the performance gap between and within sectors.
- Pricing and fundamentals may send opposing signals of where the opportunities lie; which to pursue depends on strategy (core vs. value-add) and hold period.
- Though the current backdrop is not without risks, we are focused on orienting our assets to best capitalize on accelerating fundamentals' momentum and identifying mispriced opportunities that offer enhanced return potential.

Disclosures

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