Morgan Stanley
INVESTMENT MANAGEMENT

Global Listed Real Estate: A Year in Review and Year-Ahead Outlook

INSIGHT | GLOBAL LISTED REAL ASSETS TEAM | February 2024

KEY TAKEAWAYS

- Steep market declines in 2022 and much of 2023 are rare, not witnessed since the global financial crisis (GFC), and have created an interesting opportunity for investors.
- In 2024, we are focusing on sectors with longer term and secularly supported characteristics underpinning demand.
- We believe the stabilization in interest rates globally will benefit REITs in 2024.

Looking back at 2023, we encounter a year marred by one of the most highly anticipated recessions that never came. Economic data has remained surprisingly resilient. Even as inflation has hovered stubbornly above central banks' targets for much of the past year, there are now strong indications that the Federal Reserve (Fed) and other big central banks are winning the battle against inflation and interest rate hikes are likely over.

During 2023, mortgage rates and the cost of debt rose to their highest levels since March 2000. Despite high-profile bank failures (Silicon Valley Bank, Credit Suisse) earlier in the year, the overall tenor of the equity markets remained markedly upbeat. Most recently, inflation has moderated, but remains elevated and economic growth has slowed, even as unemployment remains low. Against this economic backdrop, there are increasing expectations that the Fed and other central banks may begin cutting rates as early as the first half of 2024 and may successfully achieve a soft-landing.

Real estate securities reacted negatively to interest rate hikes for much of 2023, before reversing course with the rally that began in November upon signs of interest rate stabilization. U.S. and global real estate investment trusts (REITs) surged the last two months of the year, resulting in solid gains of 11.4% and 9.9% for 2023, respectively, following declines of

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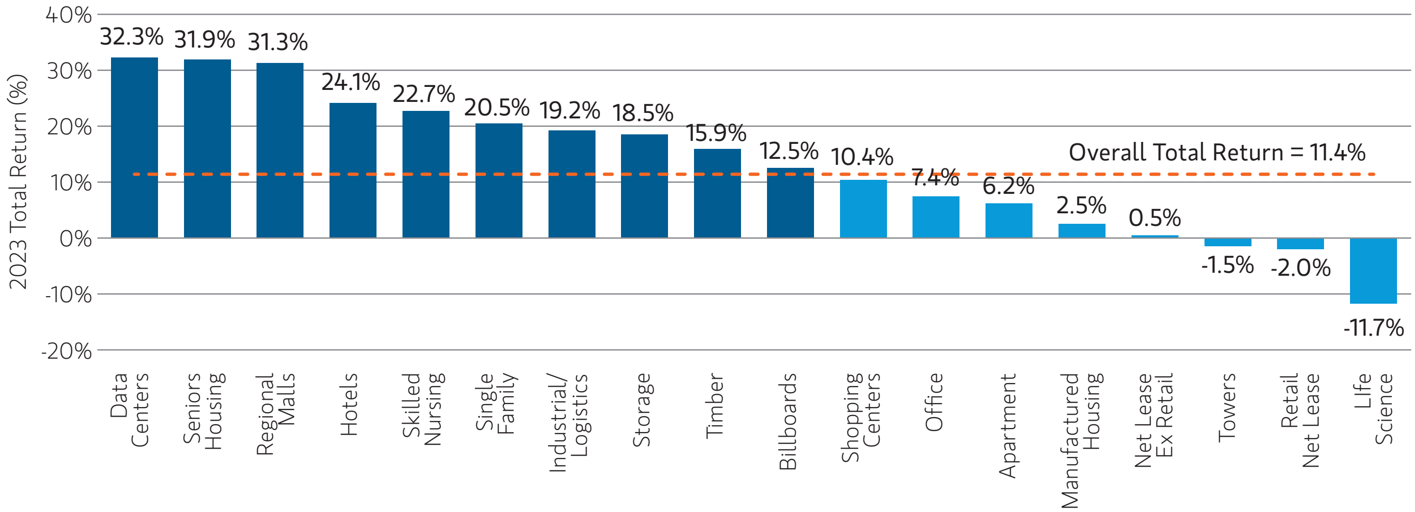
"More relevant than the longer-term benefits of adding REITs to a portfolio is the tactical opportunity that has manifested after relative underperformance of the asset class."

DISPLAY 1

FTSE Nareit All Equity REITs Index Calendar Year 2023 Sector Returns



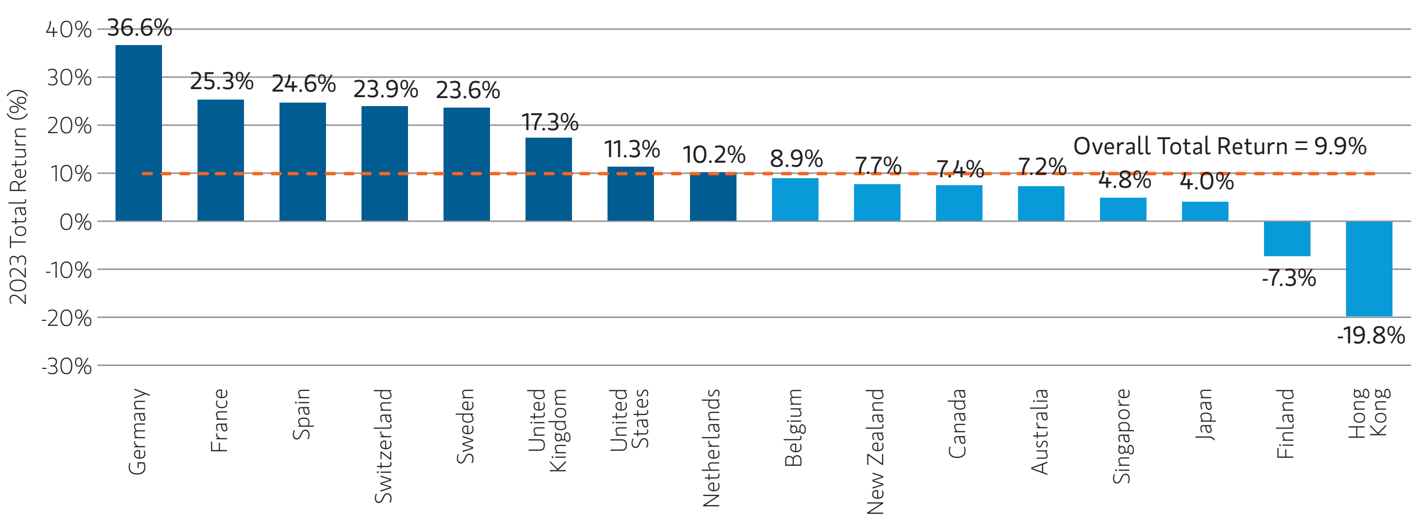
Source: FTSE Nareit and Morgan Stanley Investment Management

Returns provided in USD terms as of December 31, 2023. **Past performance should not be construed as a guarantee of future performance.** It is not possible to invest in an index. Groupings are based on how the investment team views the real estate securities universe and do not necessarily reflect official groupings. Provided for illustrative purposes only.

24.9% and 24.6%, respectively, in 2022.[1] Interestingly, although not necessarily unique to 2023, the divergence in performance among REIT sub-sectors has been significant. Secularly favored and more defensive segments of the REIT universe, that have demand drivers more insulated from macroeconomic noise, are up between 10% and 30%. Conversely, companies in sectors where growth is more exposed to changes in the cost of capital or negative secular headwinds have underperformed. A deeper look at U.S. REIT sector returns in *Display 1* and global REIT country returns in *Display 2* highlights this dichotomy.

DISPLAY 2

FTSE EPRA Nareit Developed Extended Index Calendar Year 2023 Country Returns



Source: FTSE EPRA Nareit and Morgan Stanley Investment Management

Returns provided in USD terms as of December 31, 2023. **Past performance should not be construed as a guarantee of future performance.** It is not possible to invest in an index. Groupings are based on how the investment team views the real estate securities universe and do not necessarily reflect official groupings. Provided for illustrative purposes only.

[1] U.S. REITs represented by FTSE Nareit All Equity REITs Index and Global REITs represented by FTSE EPRA Nareit Developed Extended Index.

This divergent performance is noteworthy for two reasons:

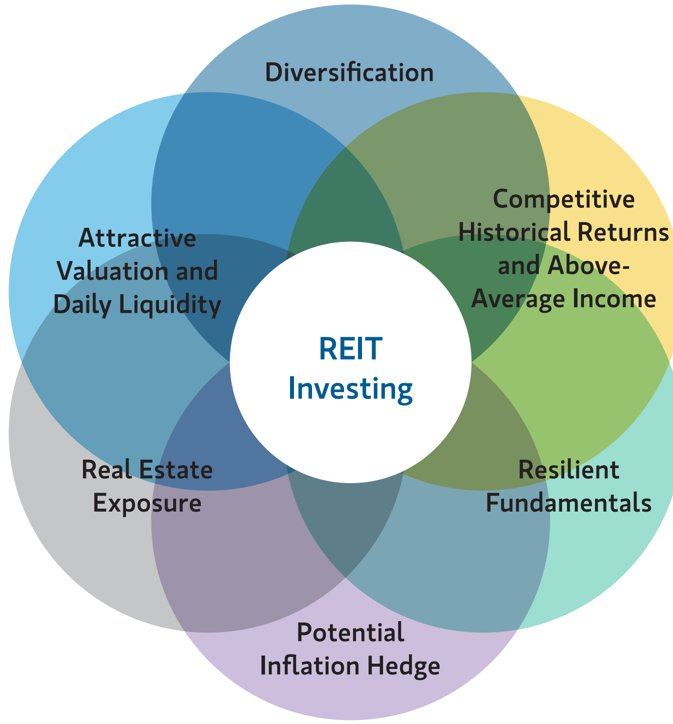
1. Not all commercial real estate (CRE) is created equal. Painting the entire sector with a broad brush is too simplistic and may result in overlooking compelling opportunities in many forms of CRE.
2. Secular themes driving demand for necessity-based real estate are powerful catalysts that may propel growth above expectations for years and ultimately reset warranted valuations higher.

Where do we stand today?

While 2023 was largely underwhelming for the global REIT universe, the steep market declines experienced in 2022 and much of 2023 are rare, not witnessed since the GFC, and have created an interesting opportunity for investors.

But even before reviewing the tactical opportunity today, we believe there is a strong case for the strategic benefits of including REITs in a diversified portfolio. Notably, REITs have competitive historical returns, contribute diversification benefits to portfolios, often display recession-resilient fundamentals given the necessity-based nature of demand, offer a potential inflation hedge given inflation linked rent escalations, high margins and operational efficiency and provide above-average income to portfolios.

DISPLAY 3
Why REITs: A Strategic Rationale



Diversification does not eliminate the risk of loss. There is no guarantee that these objectives / results will be achieved. The views, opinions and forecasts expressed herein are those of the investment team as of December 31, 2023, are not necessarily indicative of those of Morgan Stanley, are subject to change based on market, economic and other conditions, and may not necessarily come to pass. **Past performance is not indicative of future results.**

More relevant than the longer-term benefits of adding REITs to a portfolio is the tactical opportunity that has manifested after relative underperformance of the asset class. Resultant valuations for real estate securities are attractive when considering broader equities, private real estate and their own historical averages *(Display 6)*, and are actually in-line with average spreads compared to fixed income *(Display 7)*.

DISPLAY 4

REITs: History of Attractive Returns

Annual Global and U.S. REIT Performance Since 2002

2002 %	2003 %	2004 %	2005 %	2006 %	2007 %	2008 %	2009 %	2010 %	2011 %	2012 %	2013 %	2014 %	2015 %	2016 %	2017 %	2018 %	2019 %	2020 %	2021 %	2022 %	2023 %	Annualized Total Return %
Commodity 25.9	Emerging Market 56.3	Global REIT 38.0	Emerging Market 34.5	Global REIT 42.4	Emerging Market 39.8	Global Inv Grade 4.8	Emerging Market 79.0	US REIT 28.1	Private Real Estate 16.0	Global REIT 28.7	US Small Cap 38.8	US REIT 30.4	Private Real Estate 15.0	US Small Cap 21.3	Emerging Market 37.8	Private Real Estate 8.4	US Large Cap 31.5	US Small Cap 20.0	US REIT 42.8	Commodity 16.1	US Large Cap 26.3	US Large Cap 8.8
TIPS 16.6	US Small Cap 47.3	US REIT 33.8	Commodity 21.4	US REIT 36.7	Commodity 16.2	TIPS -2.4	Global HY 59.4	US Small Cap 26.9	TIPS 13.6	Global HY 19.6	US Large Cap 32.4	Global REIT 15.9	US REIT 3.0	Global HY 14.3	Developed Market 23.1	Global Inv Grade -1.2	Developed Market 28.4	Developed Market 16.5	US Large Cap 28.7	Private Real Estate 7.5	Developed Market 24.4	US REIT 8.6
Global Inv Grade 16.5	Global REIT 40.7	Emerging Market 26.0	Private Real Estate 21.4	Emerging Market 32.6	Private Real Estate 16.0	Private Real Estate -10.0	Global REIT 38.3	Global REIT 20.4	US REIT 7.8	Emerging Market 18.6	Developed Market 27.4	US Large Cap 13.7	US Large Cap 1.4	US Large Cap 12.0	US Large Cap 21.8	TIPS -1.3	US Small Cap 25.5	US Large Cap 18.4	Global REIT 27.2	TIPS -11.8	US Small Cap 16.9	Emerging Market 8.4
Private Real Estate 5.5	US REIT 37.0	US Small Cap 18.3	Global REIT 15.4	Developed Market 20.7	TIPS 11.6	Global HY -26.9	Developed Market 30.8	Emerging Market 19.2	Global Inv Grade 5.6	US REIT 18.0	Private Real Estate 13.9	Private Real Estate 12.5	Global REIT 0.1	Commodity 11.8	US Small Cap 14.7	US REIT -3.9	US REIT 24.3	Emerging Market 18.7	Commodity 27.1	Global HY -12.7	Global HY 14.0	US Small Cap 8.1
Global HY 4.1	Developed Market 33.8	Developed Market 15.3	US REIT 12.4	US Small Cap 18.4	Developed Market 9.6	US Small Cap -33.8	US REIT 28.6	Commodity 16.8	Global HY 3.1	Developed Market 16.5	Global HY 7.3	Developed Market 5.5	Developed Market -0.3	Emerging Market 11.6	Global REIT 11.4	Global REIT -4.7	Global REIT 23.1	TIPS 11.0	Developed Market 22.4	Global Inv Grade -16.2	US REIT 13.3	Developed Market 7.9
Global REIT 2.8	Global HY 32.4	Global HY 13.2	Developed Market 10.0	Private Real Estate 16.3	Global Inv Grade 9.5	Commodity -35.7	US Small Cap 27.2	Private Real Estate 16.4	US Large Cap 2.1	US Small Cap 16.4	Global REIT 4.4	US Small Cap 4.9	TIPS -1.4	Private Real Estate 8.8	Global HY 10.4	Global HY -4.1	Emerging Market 18.9	Global Inv Grade 9.2	Private Real Estate 22.2	Developed Market -17.7	Global REIT 10.9	Global REIT 7.8
US REIT 2.0	Commodity 23.9	Private Real Estate 13.1	US Large Cap 4.9	US Large Cap 15.8	US Large Cap 5.5	US Large Cap -37.0	US Large Cap 26.5	US Large Cap 15.1	US Small Cap -4.2	US Large Cap 16.0	US REIT 2.5	TIPS 3.6	Global HY -2.7	Developed Market 8.2	Private Real Estate 7.6	US Large Cap -4.4	Global HY 12.6	Global HY 7.0	US Small Cap 14.8	US Large Cap -18.1	Emerging Market 10.3	Global HY 7.4
Emerging Market -6.0	US Large Cap 28.7	US Large Cap 10.9	US Small Cap 4.6	Global HY 13.7	Global HY 3.2	US REIT -39.6	Commodity 18.9	Global HY 14.8	Developed Market -5.0	Private Real Estate 10.9	Emerging Market -2.3	Global Inv Grade 0.6	Global Inv Grade -3.2	US REIT 7.6	Global Inv Grade 7.4	Developed Market -8.2	TIPS 8.4	Private Real Estate 1.2	TIPS 6.0	Emerging Market -19.7	Global Inv Grade 5.7	Private Real Estate 7.2
Developed Market -19.5	Global Inv Grade 12.5	Global Inv Grade 9.3	Global HY 3.6	Global Inv Grade 6.6	US Small Cap -1.6	Developed Market -40.3	TIPS 11.4	Developed Market 12.3	Global REIT -5.8	TIPS 7.0	Global Inv Grade -2.6	Global HY 0.0	US Small Cap -4.4	Global REIT 5.0	US REIT 3.9	US Small Cap -11.0	Commodity 7.7	Commodity -3.1	Global HY 1.0	US Small Cap -20.4	TIPS 3.9	TIPS 4.4
US Small Cap -20.5	Private Real Estate 9.3	Commodity 9.2	TIPS 2.8	Commodity 2.1	Global REIT -7.0	Global REIT -47.7	Global Inv Grade 6.9	TIPS 6.3	Commodity -13.3	Global Inv Grade 4.3	TIPS -8.6	Emerging Market -1.8	Emerging Market -14.6	TIPS 4.7	TIPS 3.0	Commodity -11.3	Global Inv Grade 6.8	Global REIT -8.2	Emerging Market -2.2	Global REIT -24.4	Commodity -7.9	Global Inv Grade 3.4
US Large Cap -22.1	TIPS 8.4	TIPS 8.5	Global Inv Grade -4.5	TIPS 0.4	US REIT -16.4	Emerging Market -53.2	Private Real Estate -29.8	Global Inv Grade 5.5	Emerging Market -18.2	Commodity -1.1	Commodity -9.5	Commodity -17.0	Commodity -24.7	Global Inv Grade 2.1	Commodity 1.7	Emerging Market -14.2	Private Real Estate 5.3	US REIT -9.6	Global Inv Grade -4.7	US REIT -24.8	Private Real Estate -12.0	Commodity 1.9

Source: Morgan Stanley Investment Management

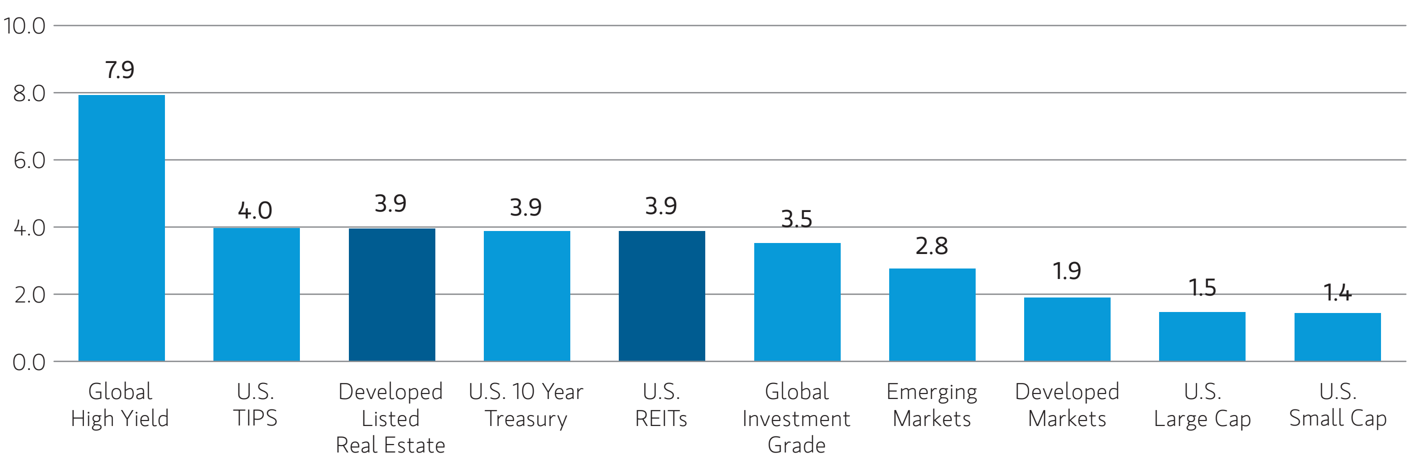
Data provided in USD as of December 31, 2023. Asset classes are represented by the following indexes: U.S. Large Cap: S&P 500 Index; U.S. Small Cap: Russell 2000 Index; Developed Market: MSCI World Index; Global Investment Grade: Barclays Global Aggregate Bond Index; Global High Yield: Bloomberg Barclays Global High Yield Total Return Index; Emerging Market: MSCI Emerging Markets Index; Commodity: Bloomberg Commodity Index; Global REIT: FTSE EPRA Nareit Developed Index; U.S. REIT: FTSE EPRA Nareit U.S. index; TIPS: Bloomberg Barclays TIPS Index; Private Real Estate: NCREIF NFI-ODCE Index.

Past performance should not be construed as a guarantee of future performance. Index returns are gross of withholding tax. It is not possible to invest in an index. Provided for illustrative purposes only. Annualized returns provided for the period from December 31, 2001 through December 31, 2023.

DISPLAY 5

REITs Yield vs. Equities and Bonds

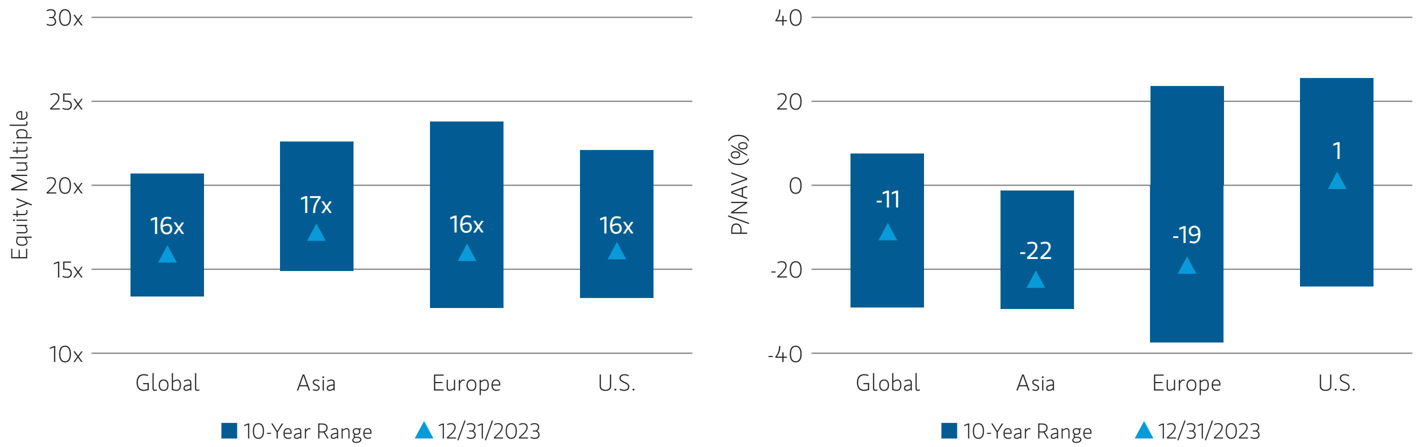
Yield of Investable Alternatives



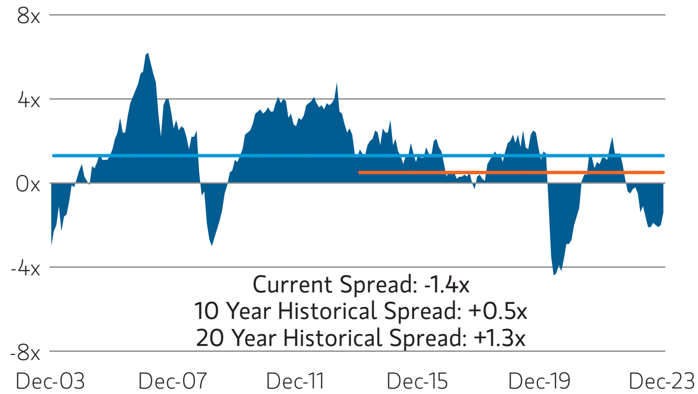
Source: FactSet for Equity Index Dividend Yield; BlackRock Aladdin for Fixed Income Index Nominal Yield; Bloomberg for 10 Year U.S. Treasury Yield. Data as of December 31, 2023. Asset classes represented by the following indexes: U.S. Large Cap: S&P 500 Index; U.S. Small Cap: Russell 2000 Index; Developed Markets: MSCI World Index; Global Investment Grade: Bloomberg Barclays Global Aggregate Bond Index; Global High Yield: Bloomberg Barclays Global High Yield Index; Emerging Markets: MSCI Emerging Markets Index; Developed Listed Real Estate: FTSE EPRA Nareit Developed Extended Index; U.S. REITs: FTSE Nareit All Equity REITs Index; U.S. TIPS: Bloomberg Barclays TIPS Index. **Past performance should not be construed as a guarantee of future performance.** It is not possible to invest in an index. Provided for illustrative purposes only.

DISPLAY 6

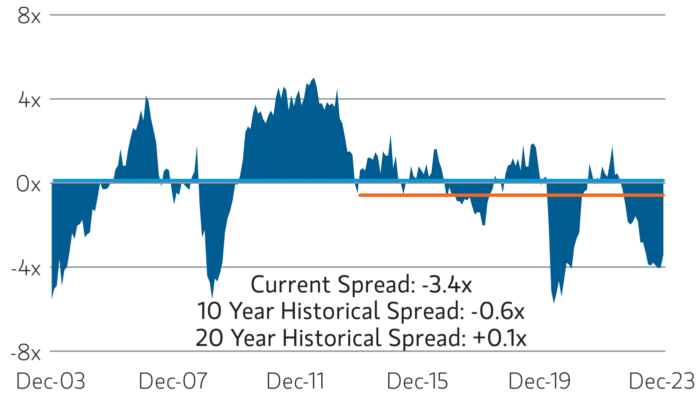
Real Estate Valuations



Global Real Estate Multiple vs. MSCI World P/E Multiple



U.S. REITs FFO Multiple vs. S&P 500 P/E Multiple



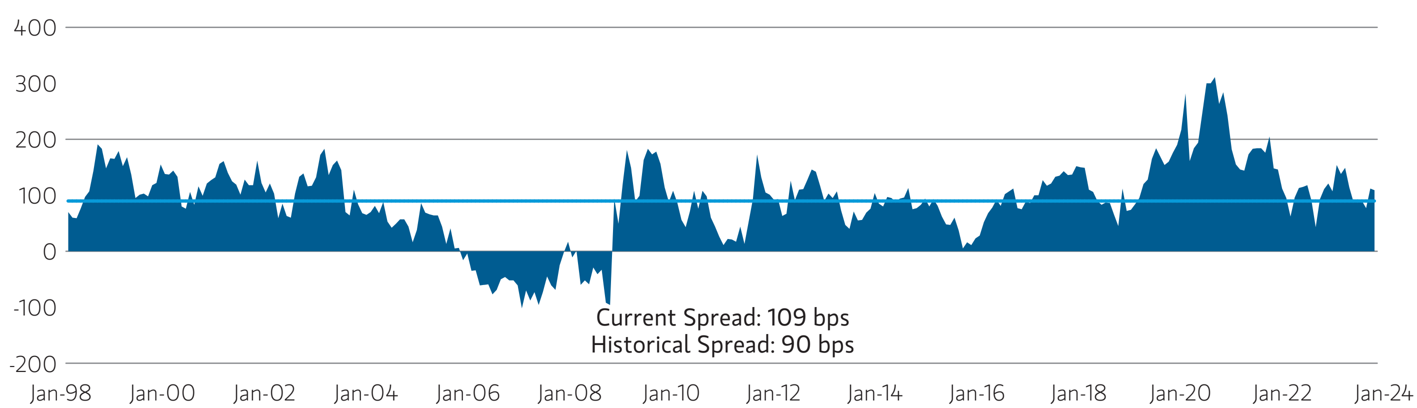
Source: UBS Global Real Estate Research, Datastream

P/FFO provided for U.S. REITs. P/E provided for S&P 500 and for non-U.S. markets. Groupings are based on how the investment team views the real estate securities universe and do not necessarily reflect official groupings. **Past performance is not indicative of future results.** Provided for informational purposes only and should not be deemed as a recommendation or offer to buy or sell any security or to participate in any trading strategy.

DISPLAY 7

U.S. Real Estate Valuations vs. Fixed Income

U.S. Major Sector Implied Cap Rate Spread to Baa (bps)[2]



Source: Green Street. Data availability begins February 1, 1998 and provided through January 1, 2024.

As per Green Street, U.S. Major Sectors represent the equal-weighted average of the asset-weighted averages for the five major property sectors (Apartment, Industrial, Mall, Office, and Strip Center). **Past performance is not indicative of future results.** Provided for informational purposes only and should not be deemed as a recommendation or offer to buy or sell any security or to participate in any trading strategy.

[2] Baa Obligations rated Baa are judged to be medium-grade subject to moderated credit risk and such may possess certain speculative characteristics.

Additionally, there is historical precedent to illustrate that after periods of significant increases in interest rates, once stabilization occurs, REITs outperform the broader equity market as shown in *Display 8*.

Themes to Play for the Year Ahead

When contemplating trends for 2024, the team is focused on sectors with longer term and secularly supported characteristics underpinning demand.

TECHNOLOGY AND INNOVATION: Data growth facilitating the digital economy and new technologies, including artificial intelligence (AI), the Internet of Things (IoT), virtual reality (VR), and autonomous driving, continue to provide a robust backdrop for new data center demand. New supply is more limited than historically, given power availability challenges, which has resulted in a favorable environment for landlords to increase rents. We expect power availability challenges to remain a critical issue going forward, and we believe advancements in AI and other technologies may be incremental demand drivers for the sector. We believe data center REITs provide a compelling opportunity for investors not only over the short term, but potentially for the next decade, as the sector is likely to benefit from the strongest long-term secular growth drivers within the REIT universe.

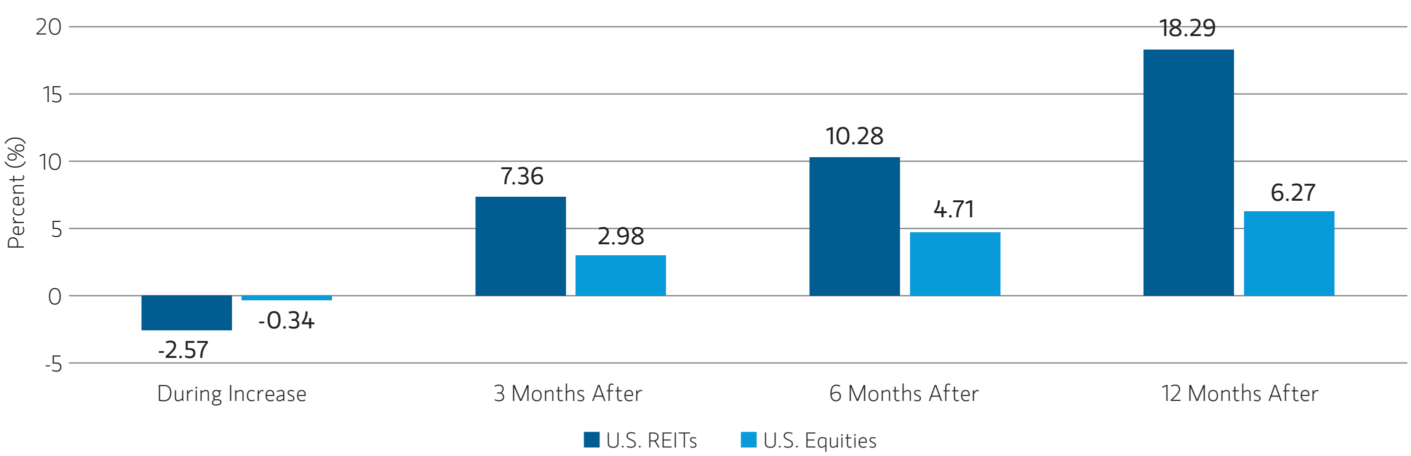
AGING DEMOGRAPHICS: The 80+ age cohort is expected to grow over 4% annually in the U.S. through 2030, versus 1.7% annually over the past 12 years,[3] which is likely to drive significant demand for the seniors housing sector through the remainder of the decade. The necessity-based nature of seniors housing demand is anticipated to insulate fundamentals from macro headwinds.

HOUSING SHORTAGES AND AFFORDABILITY: Higher-for-longer mortgage rates are dragging coincident affordability to near 50-year lows, and it is approximately 52% more expensive to buy a home than to rent.[4] Higher rates coupled with the undersupply of single-family homes in the U.S. should serve as a long-term growth driver for single-family rentals, as well as the broader rental housing spectrum. Traditional multi-family supply in the U.S. is elevated compared with historical averages, and the sector will need to work through this excess supply before experiencing true growth. However, other country markets (Germany, Australia) are experiencing supply shortages and may post resilient fundamental results. Given the necessity-based nature of housing,

DISPLAY 8

REIT Returns and Rising Interest Rates

U.S. REIT Performance versus Equities During and After Significant Increases in 10-Year Treasury Yield



Sources: Bloomberg, MSIM

Rising-yield periods are the 10 largest 1-month increases in the yield of the U.S. 10-Year Treasury since 2000 and through December 31, 2023. These rising-yield periods are 4/5/00-5/8/00; 11/7/01-12/7/01; 6/25/03-7/29/03; 3/23/04-4/23/04; 12/30/08-1/30/09; 4/27/09-5/27/09; 11/10/10-12/14/10; 3/7/22-4/7/22; 8/26/22-9/27/22 and 8/29/23-10/3/23. Average is calculated as the simple average of relative returns of REITs and equities over the time periods shown.

U.S. REITS: FTSE Nareit All Equity REITs Index; U.S. Equities: S&P 500 Index. Returns shown during subsequent periods are calculated as an average cumulative return from the ending dates of the 10 rising-yield periods shown above, over the subsequent 3, 6 and 12 months.

Past performance should not be construed as a guarantee of future performance. Returns provided in USD terms. There is no guarantee that any historical trend illustrated above will be repeated in the future, and there is no way to predict precisely when such a trend might begin. It is not possible to invest in an index. Provided for illustrative purposes only.

[3] Source: U.S. Census Bureau and Organization for Economic Co-operation and Development

[4] Source: John Burns Research and Consulting as of July 31, 2023

dry powder raised for real estate will likely shift to multi-family and serve as a floor on valuations. In the U.K., student accommodations continue to see a supply/demand imbalance driven by domestic and international student numbers, which may fuel robust levels of rental growth off very reasonable cap rates.

GLOBAL SUPPLY CHAIN REORGANIZATION AND ONSHORING: Rising offshore production costs, supply chain disruptions, and the desire to seek greater control of supply chains has propelled the onshoring trend which is expected to benefit the industrial/logistics sector. While new supply in the U.S., U.K., Japan, and Australia will likely remain elevated through the first half of 2024, it should then begin to dissipate and allow for real strength in the sector late in 2024 and into 2025. In Continental Europe, new supply remains subdued and underpins strong operations and further rental growth. Nearshoring and onshoring trends are especially evident in Eastern European markets.

EXTERNAL GROWTH OPPORTUNITIES: In addition to the secularly favored sectors noted above, we believe companies that have been able to maintain a reasonable cost of capital with a strong balance sheet, low leverage, and limited debt maturities may be able to reactivate external growth in a meaningful way, which could provide an upside surprise to earnings. For example, certain companies within the net lease sector, which have been reliant on acquisitions to fuel growth, are cyclically well positioned to seize opportunities, given stabilizing interest rates and resultant cap rates, and stronger access to the unsecured debt markets.

Conclusion

While REITs may have underperformed in 2022 and 2023, we believe the stabilization in interest rates globally will benefit REITs in 2024. Furthermore, the sectoral composition and differentiation among the REIT universe is vital when analyzing the underlying risk/reward profile and performance of real estate securities, and helps to create opportunities for active managers within listed real estate investing, such as the Morgan Stanley Investment Management (MSIM) Global Listed Real Assets (GLRA) team.

Our team seeks attractive long-term, risk-adjusted returns by utilizing internal proprietary research to invest in public real estate companies that may offer the best value relative to their underlying assets and earnings. The investment approach is based on three core principles: relative value support, downside risk protection through integration of risk factors, and high conviction positioning with an identifiable investment thesis and positive trajectory on critical factors for companies. These principles, as well as an evaluation of trends unfolding within the real estate sector, facilitate portfolio positioning.

Risk Considerations

The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the U.S. and global markets. The value of equity securities is sensitive to stock market volatility. Real Estate Risk: The risks associated with ownership of real estate and the real estate industry in general include fluctuations in the value of underlying property, defaults by borrowers or tenants, market saturation, decreases in market rents, interest rates, property taxes, increases in operating expenses and political or regulatory occurrences adversely affecting real estate. Real estate investment trusts (REITs) are subject to risks similar to those associated with the direct ownership of real estate and they are sensitive to such factors as management skills and changes in tax laws. Concentration Risk: Concentration in a single region may make the portfolio more volatile than one that invests globally.

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