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CIO Weekly Commentary
24 October 2022

CIO VIEWS: STRATEGY AND PORTFOLIO CONSTRUCTION

Revisiting REITs

Bottom line up top:

U.S. public REITs have taken their share of lumps in 2022, lagging both their private-market counterparts and most broad U.S. equity indexes. Like other asset classes, REITs have been laid low this year amid white-hot inflation that has the Federal Reserve pursuing an aggressively hawkish rate hike cycle. REITs have typically fared well in rising rate environments, but a combination of factors has conspired with the unprecedented Fed backdrop to thwart this advantage: lofty valuations following last year's record return for the asset class (+41%), a relative high correlation to broader equity markets and growing fears of a recession. The result: REITS are down nearly 28% as of 30 September, as measured by the FTSE Nareit All Equity REITs Index — on pace for their worst calendar year return since 2008.

Industrial, mall and office REITs (three of the four core property sectors in commercial real estate) have suffered some of this year's biggest declines, substantially underperforming the FTSE Nareit All Equity REITs Index as a whole (Figure 1). Apartment REITs, the fourth core property type, bucked the trend by finishing slightly ahead of the index. Demand for apartments remained elevated, translating into strong rental rates and occupancy throughout the year.

REIT returns have declined far more than the market value of private commercial properties themselves, as depicted in Figure 1. But supported by continued strength in their underlying fundamentals and fairly wide discounts to net asset values, we see compelling upside to several REIT property sectors once investors are confident that inflation has been tamed and the current rate hike cycle is complete.

Saira Malik, CFA
Chief Investment Officer

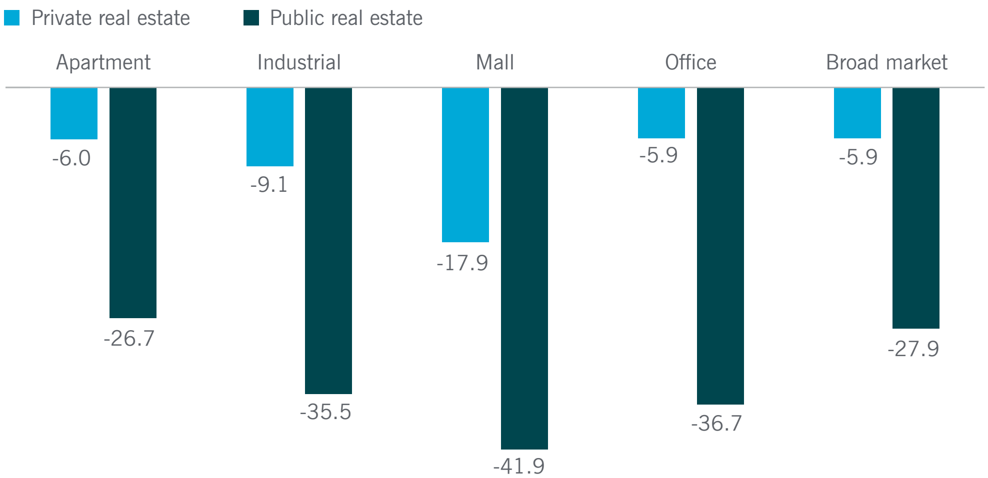
On behalf of Nuveen's Global Investment Committee

As Nuveen's CIO and leader of our Global Investment Committee, Saira drives market and investment insights, delivers client asset allocation views and brings together the firm's most senior investment leaders to deliver our best thinking and actionable investment ideas. In addition, she chairs Nuveen's Equities Investment Council and is a portfolio manager for several key investment strategies.

The selloff in public real estate may have created compelling value.

FIGURE 1: HARD-HIT PUBLIC REAL ESTATE COULD BE DUE FOR A TURNAROUND

Private market asset values versus public real estate returns (%)



Data source: Green Street Advisors, 01 Jan 2022 to 30 Sep 2022. **Past performance does not predict or guarantee future results.** Representative indexes: **Private real estate:** Green Street All Property CPPI; **Public real estate:** FTSE Nareit All Equity REITs.

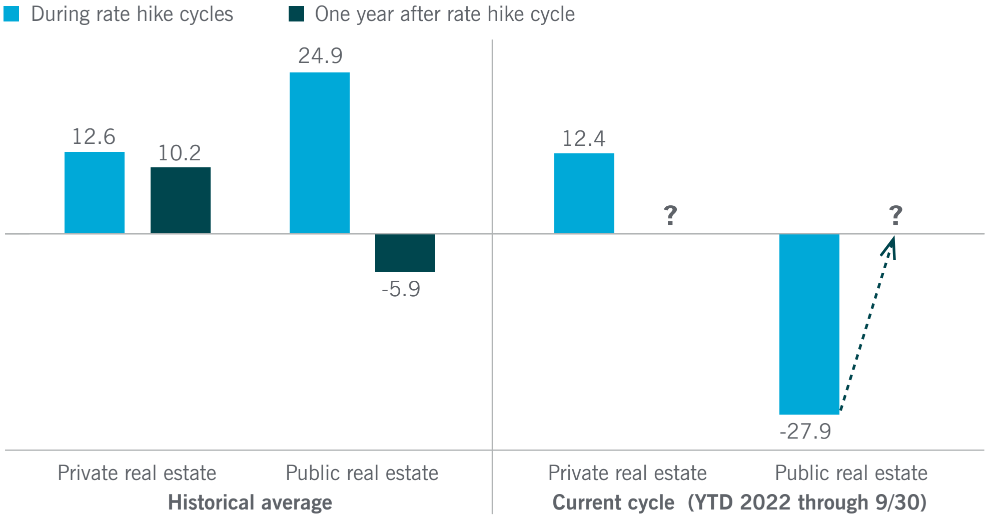
Portfolio considerations:

It might be time to consider taking some real estate allocations public. Both public and private real estate investments have provided healthy returns during past rate hike cycles. While public REITS have tended to do better while rates are going up, private real estate has outperformed in the 12-month periods immediately following the end of those cycles (Figure 2). This year, private real estate looks poised to repeat its history of strength in rising rate environments. Meanwhile, the historic decline in publicly listed REITs in 2022 so far could position the asset class for a brighter post-hiking future. Investors who believe we're closer to the end of the rate hike cycle may find public REITS an area worth examining for future real estate allocations.

We don't recommend buying sight unseen. While value may be found in several REITs sectors, we don't expect all property types (or individual REIT companies) to recover equally. Increases in real estate stock prices over time are tied to the growth in their earnings, as well as the value of the underlying real estate owned by the REIT. This means an emphasis on selectivity is paramount. In our view, **investors may be best served by seeking out high-quality, well-capitalized REITs with superior assets located in supply constrained markets**. These assets tend to benefit from lower construction rates, higher occupancy rates and high barriers to entry. On a sector basis, as with their private counterparts, **we currently favor publicly traded REITs in the apartment and industrials sectors**, thanks in large part to strong absorption rates and historically low vacancy levels in both sectors. **The retail property sector may present a compelling opportunity** as well, as store openings have outpaced closings for the first time in several years, due in part to a notable shift in consumer preference for brick-and-mortar retail in the post-pandemic environment.

FIGURE 2: CAN PUBLIC REAL ESTATE PERFORMANCE TAKE A HIKE?

Private and public real estate returns during and after rate increases (%)



Data source: Bloomberg, LP. Historical average is based on the annualized performance from the seven most recent rate hike cycles (Aug 1997 to May 1981; May 1983 to Aug 1984; Mar 1988 to Feb 1989; Feb 1994 to Feb 1995; June 1999 to May 2000; June 2004 to June 2006; Dec 2015 to Dec 2018. **Past performance does not predict or guarantee future results.** Representative indexes: **Private real estate:** NCREIF ODCE Index; **Public real estate:** FTSE Nareit All Equity REITs.

Selectivity is key — we favor high-quality REITs in the apartments, industrials and retail sectors.

About Nuveen's Global Investment Committee

Nuveen's Global Investment Committee (GIC) brings together the most senior investors from across our platform of core and specialist capabilities, including all public and private markets.

Regular meetings of the GIC lead to published outlooks that offer:

- macro and asset class views that gain consensus among our investors
- insights from thematic "deep dive" discussions by the GIC and guest experts (markets, risk, geopolitics, demographics, etc.)
- guidance on how to turn our insights into action via regular commentary and communications

For more information, please visit nuveen.com.

Endnotes

Sources

All market and economic data from Bloomberg, FactSet and Morningstar.

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Important information on risk

All investments carry a certain degree of risk and there is no assurance that an investment will provide positive performance over any period of time. Equity investing involves risk. Investments are also subject to political, currency and regulatory risks. These risks may be magnified in emerging markets. Diversification is a technique to help reduce risk. There is no guarantee that diversification will protect against a loss of income. Investing in municipal bonds involves risks such as interest rate risk, credit risk and market risk, including the possible loss of principal. The value of the portfolio will fluctuate based on the value of the underlying securities. There are special risks associated with investments in high yield bonds, hedging activities and the potential use of leverage. Portfolios that include lower rated municipal bonds, commonly referred to as "high yield" or "junk" bonds, which are considered to be speculative, the credit and investment risk is heightened for the portfolio. Credit ratings are subject to change. AAA, AA, A, and BBB are investment grade ratings; BB, B, CCC/CC/C and D are below-investment grade ratings. As an asset class, real assets are less developed, more illiquid, and less transparent compared to traditional asset classes. Investments will be subject to risks generally associated with the ownership of real estate-related assets and foreign investing, including changes in economic conditions, currency values, environmental risks, the cost of and ability to obtain insurance, and risks related to leasing of properties. Socially Responsible Investments are subject to Social Criteria Risk, namely the risk that because social criteria exclude securities of certain issuers for non-financial reasons, investors may forgo some market opportunities available to those that don't use these criteria. Investors should be aware that alternative investments including private equity and private debt are speculative, subject to substantial risks including the risks associated with limited liquidity, the use of leverage, short sales and concentrated investments and may involve complex tax structures and investment strategies. Alternative investments may be illiquid, there may be no liquid secondary market or ready purchasers for such securities, they may not be required to provide periodic pricing or valuation information to investors, there may be delays in distributing tax information to investors, they are not subject to the same regulatory requirements as other types of pooled investment vehicles, and they may be subject to high fees and expenses, which will reduce profits. Alternative investments are not appropriate for all investors and should not constitute an entire investment program. Investors may lose all or substantially all of the capital invested. The historical returns achieved by alternative asset vehicles is not a prediction of future performance or a guarantee of future results, and there can be no assurance that comparable returns will be achieved by any strategy.

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