REAL ESTATE 101 | U.S.

Considerations for a Global Approach to Property Investing

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Publicly traded property stocks, including real estate investment trusts (REITs) and real estate operating companies (REOCs), can allow investors to gain exposure to real estate, which is generally an illiquid asset class, without sacrificing the liquidity benefits of listed equities. Property stocks also typically offer higher yields than other equities, they may serve as an effective inflation hedge, and they could help diversify a portfolio made up of other asset classes.

While the REIT structure originated in the U.S., many countries around the world have adopted similar legislation over the years, which has led to an increase in the global opportunity set for listed property companies. However, despite the fact that the U.S. now represents less than one-half of the available global market capitalization of listed real estate securities, it remains relatively rare for U.S. investors to make dedicated allocations to international property investments.

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WHAT IS THE DIFFERENCE BETWEEN A REIT AND A REOC?

A REIT is a company that owns and, in most cases, operates income-producing real estate. These investment vehicles were designed to provide a structure for real estate similar to the structure that mutual funds provide for investment in stocks. REITs were initially created in the U.S. through the Real Estate Investment Trust Act of 1960 with the intention of providing individual investors with access to a diversified portfolio of commercial real estate, an asset class formerly only accessible to large institutional investors. Through REITs, investors can gain exposure to properties such as office buildings, shopping malls, hotels, apartment buildings, and other forms of commercial real estate.

To qualify as a REIT, a company must have most of its assets and income tied to real estate investments, and it must pay out almost all of its taxable income to shareholders in the form of dividends. In the U.S., a REIT must meet the following four requirements.

1. The REIT must distribute at least 90% of its annual taxable income, excluding capital gains, as dividends to its shareholders.
2. The REIT must have at least 75% of its assets invested in real estate, mortgage loans, shares in other REITs, cash, or government securities.
3. The REIT must derive at least 75% of its gross income from rents, mortgage interest, or gains from the sale of real property. Also, at least 95% of gross income must come from these sources combined with dividends, interest, and gains from securities sales.
4. The REIT must have at least 100 shareholders, and less than 50% of the outstanding shares must be concentrated in the hands of five or fewer shareholders.

Today, 23 markets are represented in the S&P Global REIT, including several emerging market countries.

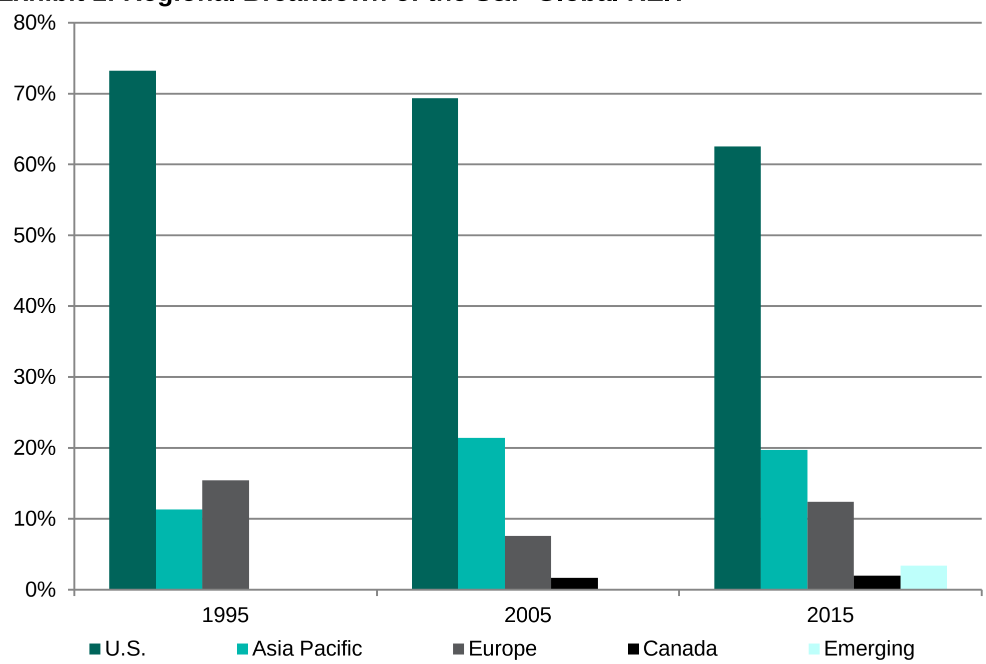
If a REIT meets all of these requirements, then the income used to pay dividends will be exempt from corporate income taxes, so investors can avoid double taxation on their earnings.

REOCs are similar to REITs in terms of business activities, but they are not required to distribute most of their income or invest minimum levels of assets in defined categories. Since REOCs can retain more of their earnings than REITs, they may have more of an ability to fund growth internally, rather than through capital markets. However, REOCs do not enjoy the tax exemption that REITs do, which may make them less appealing to investors seeking current income from their portfolios.

THE INCREASING SIGNIFICANCE OF INTERNATIONAL REAL ESTATE SECURITIES

While the REIT market in the U.S. has garnered a lot of attention in recent years and become quite a popular investment category among both domestic and global investors, comparatively little attention has been paid to real estate securities based outside of the U.S., despite significant development in international markets. In February 1995, just three markets—Australia, the Netherlands, and the U.S.—were represented in the S&P Global REIT. By 2005, this had increased to 10 markets, and today, 23 markets are represented in the index, including several emerging market countries. As depicted in Exhibit 1, U.S. REITs have decreased from representing about 73% of the global REIT market in 1995 to 63% in 2015. This has occurred despite significant outperformance of U.S. REITs over the past several years.

Exhibit 1: Regional Breakdown of the S&P Global REIT



Source: S&P Dow Jones Indices LLC. Data from February 1995 to February 2015. Chart is provided for illustrative purposes.

THE IMPORTANCE OF INCLUDING REOCs IN GLOBAL PROPERTY INDICES

In the U.S., virtually all public companies with businesses focused on real estate investment are structured as REITs. However, many countries around the world either do not have legislation authorizing REITs or REIT-like structures, or the REIT structure has not become as ubiquitous, which leaves many property companies outside of the scope of indices that only include REITs. As a result, more inclusive property indices, such as the S&P Global Property, are widely utilized in global markets because they include REOCs and other diversified real estate companies. These indices screen individual companies to ensure that the majority of their business activities involve the ownership and operation of real estate.

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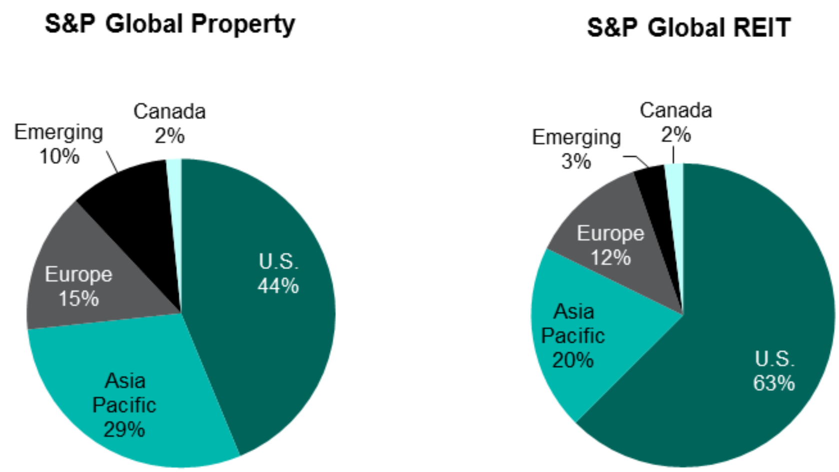
Exhibit 2: Inclusion of REOCs Leads to Greater Geographic Diversification

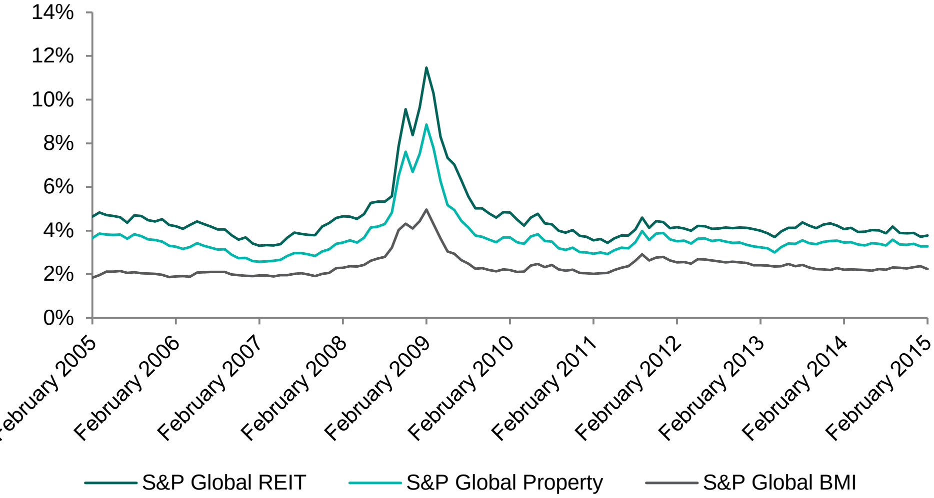


Source: S&P Dow Jones Indices LLC. Data as of Feb. 27, 2015. Chart is provided for illustrative purposes.

As Exhibit 2 illustrates, the inclusion of REOCs in the S&P Global Property leads to a dramatic decrease in concentration to the U.S. market (from 63% to 44%) and a substantial increase in exposure to international markets. Particularly noteworthy is the increase in weight to emerging markets (from 3% to 10%), where few countries have REIT-like structures in place.

Although the inclusion of REOCs leads to significant geographic diversity, it also has historically resulted in some decrease in yield, as expected. This is because REOCs are not legally required to pay out nearly all income via dividends. However, as illustrated in Exhibit 3, the yield spread between the S&P Global Property and S&P Global REIT has been modest and has actually shrunk in recent years. REOCs generally maintain high payout ratios, despite not having a legal obligation to pay dividends. Additionally, both the S&P Global Property and the S&P Global REIT have had higher yields than a typical benchmark might, like the S&P Global BMI (Broad Market Index).

Exhibit 3: Historical Dividend Yield for the S&P Global Property, the S&P Global REIT, and the S&P Global BMI



Source: S&P Dow Jones Indices LLC. Data as of Feb. 27, 2015. Index performance based on total return in USD. Past performance is no guarantee of future results. Chart is provided for illustrative purposes.

Both U.S. REITs and international real estate securities have historically shown relatively low correlations to traditional U.S. and international equity benchmarks, respectively.

THE DIVERSIFICATION BENEFITS OF GLOBAL REAL ESTATE SECURITIES

As shown in Exhibit 4, both U.S. REITs and international real estate securities have historically shown relatively low correlations to traditional U.S. and international equity benchmarks, respectively. For example, the correlation over 20 years between global ex-U.S. property and U.S. stocks (0.70) is less than that of global ex-U.S. equities and U.S. stocks (0.84). Likewise, the S&P U.S. REIT and the S&P Global ex-U.S. Property have modest correlations to each other. This suggests that adding international real estate securities to a portfolio comprised of U.S. REITs may reduce the level of risk as a result of additional diversification.

Exhibit 4: 20-Year Correlation Matrix of Major Asset Classes

Index	S&P Composite 1500®	S&P Global Ex-U.S. BMI	S&P U.S. REITs	S&P Global ex-U.S. Property	Barclays U.S. Aggregate	Barclays Global Ex-U.S. Aggregate
S&P Composite 1500	1.00	-	-	-	-	-
S&P Global Ex-U.S. BMI (USD)	0.84	1.00	-	-	-	-
S&P U.S. REIT	0.57	0.55	1.00	-	-	-
S&P Global ex–U.S. Property	0.70	0.85	0.61	1.00	-	-
Barclays US Aggregate	-0.02	.01	0.16	.15	1.00	-
Barclays Global ex-US Aggregate	0.16	0.38	0.29	.42	.47	1.00

Source: S&P Dow Jones Indices LLC, Barclays. Data as of Feb. 27, 2015. Index performance based on total return in USD. Past performance is no guarantee of future results. Table is provided for illustrative purposes and reflects hypothetical historical performance of the S&P Composite 1500. Please see the Performance Disclosures at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

Exhibit 5 illustrates the risk/return characteristics over several time periods of a hypothetical portfolio comprising 50% S&P U.S. REIT and 50% S&P Global ex-U.S. Property, compared with the individual component indices. Because U.S. REITs have outperformed non-U.S. markets by such a wide margin in recent years, the addition of the S&P Global ex-U.S. Property clearly has detracted from overall total returns. However, the combined portfolio has historically had substantially lower volatility than either of the indices, and in most cases, its risk-adjusted return comes close to or exceeds the U.S., despite lower absolute returns.

Relatively low correlations between property indices and traditional equity benchmarks suggests that the addition of international real estate securities may reduce risk and improve risk-adjusted returns in a total portfolio context.

Exhibit 5: Performance Characteristics of Diversified Portfolios

Metric	S&P U.S. REIT (%)	S&P Global ex-U.S. Property (%)	Global Property Portfolio (50/50) (%)
3-Year Return	15.43	11.04	13.41
3-Year Risk	13.54	13.25	11.95
3-Year Risk-Adjusted Return	1.14	0.83	1.12
5-Year Return	17.71	10.50	14.27
5-Year Risk	16.60	17.29	15.70
5-Year Risk-Adjusted Return	1.07	0.61	0.91
10-Year Return	9.24	6.64	8.39
10-Year Risk	25.78	21.14	21.73
10-Year Risk-Adjusted Return	0.36	0.31	0.39
15-Year Return	13.20	9.69	11.86
15-Year Risk	22.65	19.27	19.18
15-Year Risk-Adjusted Return	0.58	0.50	0.62
20-Year Return	11.81	7.21	9.91
20-Year Risk	20.50	19.50	17.96
20-Year Risk-Adjusted Return	0.58	0.37	0.55

Source: S&P Dow Jones Indices LLC. Data as of Feb. 27, 2015. Index performance based on total return in USD. Past performance is no guarantee of future results. Table is provided for illustrative purposes.

Relatively low correlations between property indices and traditional equity benchmarks suggests that the addition of international real estate securities may reduce risk and improve risk-adjusted returns in a total portfolio context. The three hypothetical portfolios in Exhibit 6 contain different combinations of global equities and fixed income. Portfolios A.1 and A.2 both comprise a 60% equity allocation and a 40% fixed income allocation. Portfolios B.1 and B.2 each have 70% stocks and 30% fixed income, and C.1 and C.2 both have 80% stocks and 20% fixed income. In all three portfolio sets, we start with allocations to international (global ex-U.S.) equities, with no allocation to international property (portfolios A.1, B.1, and C.1). We then reallocate 5% of each hypothetical portfolio away from international stocks to international property (portfolios A.2, B.2, and C.2).

All values listed are percentages, apart from the risk-adjusted returns.

In most of the cases studied, modest allocations to the S&P Global ex-U.S. Property, in combination with global stocks, bonds, and U.S. REITs, generated higher absolute returns.

Exhibit 6: Performance Characteristics of Diversified Portfolios

Asset Category	Index	60/40 Portfolios		70/30 Portfolios		80/20 Portfolios	
		A.1 (%)	A.2 (%)	B.1 (%)	B.2 (%)	C.1 (%)	C.2 (%)
Domestic Stocks	S&P Composite 1500	35	35	42	42	49	49
International Stocks	S&P Global ex-U.S. BMI	20	15	23	18	26	21
Domestic Listed Property	S&P U.S. REIT	5	5	5	5	5	5
International Listed Property	S&P Global ex-U.S. Property	0	5	0	5	0	5
Domestic Bonds	Barclays US Aggregate	35	35	25	25	15	15
International Bonds	Barclays Global ex-US Aggregate	5	5	5	5	5	5

Metrics	60/40 Portfolios		70/30 Portfolios		80/20 Portfolios	
	A.1 (%)	A.2 (%)	B.1 (%)	B.2 (%)	C.1 (%)	C.2 (%)
3-Year Return	9.05	9.25	10.15	10.36	11.25	11.46
3-Year Risk	6.08	6.03	7.00	6.93	7.96	7.87
3-Year Risk-Adjusted Return	1.489	1.534	1.450	1.495	1.414	1.456
5-Year Return	9.84	10.00	10.75	10.92	11.64	11.81
5-Year Risk	8.40	8.38	9.79	9.76	11.21	11.16
5-Year Risk-Adjusted Return	1.171	1.194	1.098	1.119	1.039	1.058
10-Year Return	6.86	6.90	7.10	7.14	7.32	7.35
10-Year Risk	10.17	10.23	11.66	11.72	13.18	13.23
10-Year Risk-Adjusted Return	.675	.674	.609	.609	.555	.556
15-Year Return	6.26	6.50	6.18	6.43	6.07	6.32
15-Year Risk	9.69	9.93	11.20	11.18	12.74	12.71
15-Year Risk-Adjusted Return	.646	.655	.552	.575	.477	.497
20-Year Return	8.24	8.27	8.51	8.54	8.75	8.79
20-Year Risk	9.30	9.32	10.75	10.76	12.24	12.23
20-Year Risk-Adjusted Return	.886	.887	.791	.794	.715	.718

Source: S&P Dow Jones Indices LLC, Barclays. Data as of Feb. 27, 2015. Index performance based on total return in USD. Past performance is no guarantee of future results. Table is provided for illustrative purposes and reflects hypothetical historical performance of the S&P Composite 1500. Please see the Performance Disclosures at the end of this document for more information regarding the inherent limitations associated with backtested performance.

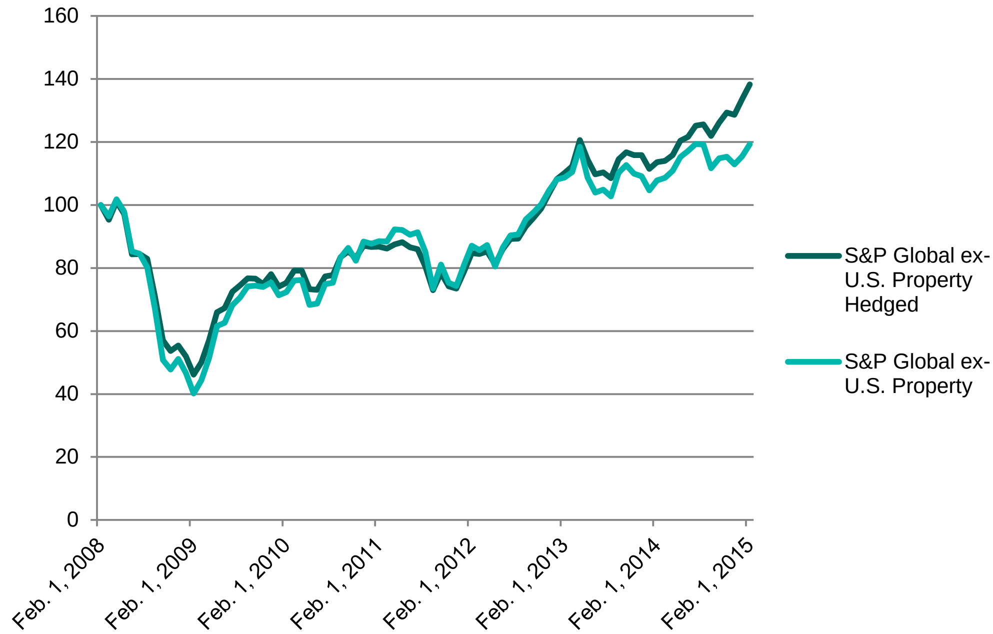
In most of the cases studied, modest allocations to the S&P Global ex-U.S. Property, in combination with global stocks, bonds, and U.S. REITs, generated higher absolute returns in conjunction with less return variability. Consequently, in all cases except two (portfolio A and B’s 10-year history), reallocating 5% to the S&P Global ex-U.S. Property from the S&P Global ex-U.S. BMI resulted in higher risk-adjusted returns.

TO HEDGE OR NOT TO HEDGE?

Some investors use hedging in an attempt to reduce uncertainty associated with currency fluctuations in foreign markets. By investing in an index fund that tracks a hedged index, U.S. investors may better mimic the returns realized in foreign markets by local investors, because currency fluctuations, as a component of returns to U.S. investors, are mitigated.

In recent years, the S&P Global ex-U.S. Property Hedged has provided higher returns than the S&P Global ex-U.S. Property (unhedged) because of the substantial appreciation of the U.S. dollar relative to most foreign currencies since early 2013.

Exhibit 7: Hedged Versus Unhedged Returns of the S&P Global ex-U.S. Property



Source: S&P Dow Jones Indices LLC. Data as of Feb. 27, 2015. Index performance based on total return in USD. Past performance is no guarantee of future results. Chart is provided for illustrative purposes.

Some investors use hedging in an attempt to reduce uncertainty associated with currency fluctuations in foreign markets.

However, hedging does not always result in higher returns, as illustrated by Exhibit 8, which shows annual returns by calendar year. In 2009 and 2010, the unhedged version of the S&P Global ex-U.S. Property produced higher returns than the hedged version, as the U.S. dollar depreciated significantly relative to most other currencies during this time. As previously mentioned, this trend reversed sharply in 2013, when the U.S. dollar began a period of rapid strengthening.

With the U.S. representing less than half of the available universe of listed property stock globally, focusing on U.S. REITs alone can be viewed as a restrictive and undiversified approach to asset allocation.

Exhibit 8: Annual Returns by Calendar Year

Year	S&P Global ex-U.S. Property Hedged (%)	S&P Global ex-U.S. Property (%)	Federal Reserve U.S. Dollar Index (%)
2008	-50.76	-52.98	11.2
2009	40.80	47.54	-9.2
2010	11.60	17.23	-1.3
2011	-15.61	-16.01	0.6
2012	41.14	40.88	0.4
2013	11.67	4.35	4.7
2014	11.61	5.61	13.3
2015 YTD	7.47	5.62	4.9

Source: S&P Dow Jones Indices LLC, FRED. S&P Dow Jones Indices data from Dec. 31, 2007, to Feb. 27, 2015. FRED data from Jan. 1, 2008, to March 1, 2015. Index performance based on total return in USD. Past performance is no guarantee of future results. Table is provided for illustrative purposes.

CONCLUSION

With the U.S. representing less than half of the available universe of listed property stocks globally, focusing on U.S. REITs alone can be viewed as a restrictive and undiversified approach to asset allocation. Taking a global approach to property investing may reduce risk through increased diversification, while providing similar investment characteristics to U.S. REITs, such as high current income generation and the potential for long-term capital appreciation. The choice of a global property benchmark is also key, as the use of a REIT-only index can be highly limiting from a geographical diversification standpoint. Finally, for those concerned about foreign currency risk, hedged indices and associated index-linked investment funds could be utilized to mitigate adverse currency movements.

PERFORMANCE DISCLOSURES

The S&P Composite 1500® was launched on May 18, 1995. All information presented prior to the launch date is back-tested. Back-tested performance is not actual performance, but is hypothetical. The back-test calculations are based on the same methodology that was in effect on the launch date. Complete index methodology details are available at www.spdji.com.

S&P Dow Jones Indices defines various dates to assist our clients in providing transparency on their products. The First Value Date is the first day for which there is a calculated value (either live or back-tested) for a given index. The Base Date is the date at which the Index is set at a fixed value for calculation purposes. The Launch Date designates the date upon which the values of an index are first considered live; index values provided for any date or time period prior to the index's Launch Date are considered back-tested. S&P Dow Jones Indices defines the Launch Date as the date by which the values of an index are known to have been released to the public, for example via the company's public Web site or its datafeed to external parties. For Dow Jones-branded indices introduced prior to May 31, 2013, the Launch Date (which prior to May 31, 2013, was termed "Date of Introduction") is set at a date upon which no further changes were permitted to be made to the index methodology, but that may have been prior to the Index's public release date.

Past performance of the Index is not an indication of future results. Prospective application of the methodology used to construct the Index may not result in performance commensurate with the back-test returns shown. The back-test period does not necessarily correspond to the entire available history of the Index. Please refer to the methodology paper for the Index, available at www.spdji.com for more details about the index, including the manner in which it is rebalanced, the timing of such rebalancing, criteria for additions and deletions, as well as all index calculations.

Another limitation of using back-tested information is that the back-tested calculation is generally prepared with the benefit of hindsight. Back-tested information reflects the application of the index methodology and selection of index constituents in hindsight. No hypothetical record can completely account for the impact of financial risk in actual trading. For example, there are numerous factors related to the equities (or fixed income, or commodities) markets in general which cannot be, and have not been accounted for in the preparation of the index information set forth, all of which can affect actual performance.

Additionally, it is not possible to invest directly in an Index. The Index returns shown do not represent the results of actual trading of investable assets/securities. S&P Dow Jones Indices maintains the Index and calculates the Index levels and performance shown or discussed, but does not manage actual assets. Index returns do not reflect payment of any sales charges or fees an investor may pay to purchase the securities underlying the Index or investment funds that are intended to track the performance of the Index. The imposition of these fees and charges would cause actual and back-tested performance of the securities/fund to be lower than the Index performance shown. For example, if an index returned 10% on a US $100,000 investment for a 12-month period (or US$ 10,000) and an actual asset-based fee of 1.5% was imposed at the end of the period on the investment plus accrued interest (or US$ 1,650), the net return would be 8.35% (or US$ 8,350) for the year. Over a three-year period, an annual 1.5% fee taken at year end with an assumed 10% return per year would result in a cumulative gross return of 33.10%, a total fee of US$ 5,375, and a cumulative net return of 27.2% (or US$ 27,200).

GENERAL DISCLAIMER