



Real Estate

# Why REITs, why Principal?

## Why listed REITs?

- 1 Historically a long-term total return enhancer relative to stocks and bonds
- 2 Liquid, with immediate exposure to real estate and lower beta than stocks
- 3 Potential dividends from a durable and often growing income-stream, plus capital appreciation tied to real asset ownership
- 4 Diversification through low correlations to other asset classes, and within real estate across geographies and property types

## Why Principal?

- 1 Consistent track record of attractive returns
- 2 Quality at a reasonable price investment style identifies long term opportunities
- 3 Portfolio construction process that seeks to deliver consistent excess returns through a large number of medium-sized active weights

Since their establishment in the U.S. decades ago, publicly traded REITs have offered investors the combined benefit of commercial real estate investment along with the advantages of investing in publicly traded stocks. REITs have grown in size, impact and market acceptance around the world. REITs, REOCs, and other real estate stocks own or operate trillions in real estate assets across all major global markets.

REITs are a total return investment, typically providing current income with the potential for long-term capital appreciation. REIT dividends and earnings are generated by a steady stream of contractual rents paid by tenants of their properties. The historical track record of REITs has demonstrated low correlations to stocks and bonds, a lower equity beta than stocks, and competitive long-term total returns. This is why investors should appreciate the differentiated behavior of REITs and the benefits they can offer their portfolio.

## Increase total return potential

Most investors seek a well-diversified portfolio that maximizes risk-adjusted total-return potential. It's clear public REITs have a long-term track record of enhancing returns (evidenced by chart below). Public REITs offer numerous opportunities to invest in physical real estate operated by quality management teams with strong balance sheets. These companies can take advantage of opportunities in private real estate markets and some can provide access to unique areas of the property market.

Exhibit 1: Total returns by asset class since 2000

2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	YTD 2021	Annualized total return
Commodity 49.74%	Global REIT 13.02%	Commodity 32.07%	Emerging Market 56.28%	Global REIT 33.80%	Emerging Market 34.54%	Global REIT 38.79%	Emerging Market 39.82%	Global Inv Grade 4.79%	Emerging Market 79.02%	US REIT 28.48%	Private Real Estate 15.99%	Global REIT 23.73%	US Small Cap 38.82%	US REIT 30.38%	Private Real Estate 15.01%	US Small Cap 21.31%	Emerging Market 37.75%	Private Real Estate 8.35%	US Large Cap 31.49%	US Small Cap 19.96%	Commodity 38.27%	US REIT 10.88%
US REIT 26.81%	US REIT 12.83%	TIPS 16.57%	US Small Cap 47.25%	US REIT 31.49%	Commodity 25.55%	US REIT 35.92%	Commodity 2.35%	TIPS 2.35%	Global HY 59.40%	US Small Cap 26.85%	TIPS 13.56%	Global HY 19.60%	US Large Cap 32.39%	Global REIT 22.81%	US REIT 2.52%	Global HY 14.27%	Developed Market 23.07%	Global Inv Grade -1.20%	Developed Market 28.40%	Emerging Market 18.69%	US REIT 22.99%	Global REIT 10.17%
Global REIT 23.53%	TIPS 7.90%	Global Inv Grade 16.52%	Global REIT 38.96%	Emerging Market 25.95%	Private Real Estate 21.40%	Emerging Market 32.55%	Private Real Estate 15.96%	Private Real Estate -10.00%	Global REIT 33.68%	Global REIT 23.44%	US REIT 8.69%	Emerging Market 18.63%	Developed Market 27.36%	US Large Cap 13.69%	US Large Cap 1.38%	US Large Cap 11.96%	US Large Cap 21.83%	TIPS -1.26%	US REIT 25.84%	US Large Cap 18.40%	Global REIT 17.70%	US Small Cap 8.43%
Private Real Estate 14.28%	Private Real Estate 5.63%	Global REIT 7.88%	US REIT 36.74%	US Small Cap 18.33%	US REIT 12.13%	Developed Market 20.65%	TIPS 11.64%	Global HY -26.89%	Developed Market 30.79%	Emerging Market 19.20%	Global Inv Grade 5.64%	US REIT 17.77%	Private Real Estate 13.94%	Private Real Estate 12.49%	Global REIT 0.59%	Emerging Market 11.60%	US Small Cap 14.65%	Global HY -4.06%	US Small Cap 25.52%	Developed Market 16.50%	US Large Cap 15.92%	Private Real Estate 7.83%
TIPS 13.18%	US Small Cap 2.49%	Private Real Estate 5.54%	Developed Market 33.76%	Commodity 17.28%	Global REIT 10.41%	US Small Cap 18.37%	Developed Market 9.57%	US Small Cap -33.79%	US REIT 28.61%	Private Real Estate 16.36%	Global HY 3.12%	Developed Market 16.54%	Global HY 7.33%	Developed Market 5.50%	Developed Market -0.32%	Commodity 11.37%	Global HY 10.43%	US Large Cap -4.38%	Global REIT 24.49%	TIPS 10.99%	Developed Market 13.43%	Global HY 7.68%
Global Inv Grade 3.17%	Global HY 2.26%	Global HY 4.13%	Global HY 32.42%	Developed Market 15.25%	Developed Market 10.02%	Private Real Estate 16.32%	Global Inv Grade 9.48%	US Large Cap -37.00%	US Small Cap 27.17%	US Large Cap 15.06%	US Large Cap 2.11%	US Small Cap 16.35%	Global REIT 2.81%	US Small Cap 4.89%	TIPS -1.44%	Private Real Estate 8.76%	Global REIT 8.63%	US REIT -4.57%	Emerging Market 18.90%	Global Inv Grade 9.20%	US Small Cap 12.41%	Emerging Market 7.24%
Global HY 1.04%	Global Inv Grade 1.57%	US REIT 3.64%	US Large Cap 28.68%	Global HY 13.17%	US Large Cap 4.91%	US Large Cap 15.79%	US Large Cap 5.49%	US REIT -37.97%	US Large Cap 26.46%	Global HY 14.82%	Global REIT 1.70%	Private Real Estate 16.00%	US REIT 2.47%	TIPS 3.64%	Global HY -2.72%	US REIT 8.60%	Private Real Estate 7.61%	Global REIT -4.77%	Commodity 17.63%	Global HY 7.03%	Private Real Estate 6.12%	US Large Cap 7.10%
US Small Cap -3.02%	Emerging Market -2.37%	Emerging Market -6.00%	Commodity 20.72%	Private Real Estate 13.07%	US Small Cap 4.55%	Global HY 13.69%	Global HY 3.18%	Developed Market -40.33%	Commodity 13.48%	Developed Market 12.34%	Commodity -1.18%	Private Real Estate 10.94%	Commodity -1.22%	Global Inv Grade 0.59%	Global Inv Grade -3.15%	Global Inv Grade 8.15%	Global Inv Grade 7.39%	Developed Market -8.20%	Global HY 12.56%	Private Real Estate 1.19%	TIPS 3.51%	Developed Market 5.97%
US Large Cap -9.10%	US Large Cap -11.89%	Developed Market -19.54%	Global Inv Grade 12.51%	US Large Cap 10.88%	Global HY 3.59%	Global Inv Grade 6.64%	US Small Cap -1.57%	Global REIT -45.04%	TIPS 11.41%	Commodity 9.03%	US Small Cap -4.18%	TIPS 6.98%	Emerging Market -2.27%	Global HY 0.01%	US Small Cap -4.41%	Global REIT 6.90%	Commodity 5.77%	US Small Cap -11.01%	TIPS 8.43%	US REIT -7.57%	Global HY 1.70%	TIPS 5.72%
Developed Market -12.92%	Developed Market -16.52%	US Small Cap -20.48%	Private Real Estate 9.28%	Global Inv Grade 9.27%	TIPS 2.84%	TIPS 0.41%	Global REIT -11.13%	Commodity -46.49%	Global Inv Grade 6.93%	TIPS 6.31%	Developed Market -5.02%	Global Inv Grade 4.32%	Global Inv Grade -2.60%	Emerging Market -1.82%	Emerging Market -14.60%	TIPS 4.68%	US REIT 5.07%	Commodity -13.82%	Global Inv Grade 6.84%	Global REIT -8.11%	Emerging Market -0.99%	Global Inv Grade 4.32%
Emerging Market -30.61%	Commodity -31.93%	US Large Cap -22.10%	TIPS 8.40%	TIPS 8.46%	Global Inv Grade -4.49%	Commodity -15.09%	US REIT -16.82%	Emerging Market -53.18%	Private Real Estate -29.76%	Global Inv Grade 5.54%	Emerging Market -18.17%	Commodity 0.08%	TIPS -8.61%	Commodity -33.06%	Commodity -32.86%	Global Inv Grade 2.09%	TIPS 3.01%	Emerging Market -14.25%	Private Real Estate 5.34%	Commodity -23.72%	Global Inv Grade -4.06%	Commodity -0.06%

As of 30 September 2021.

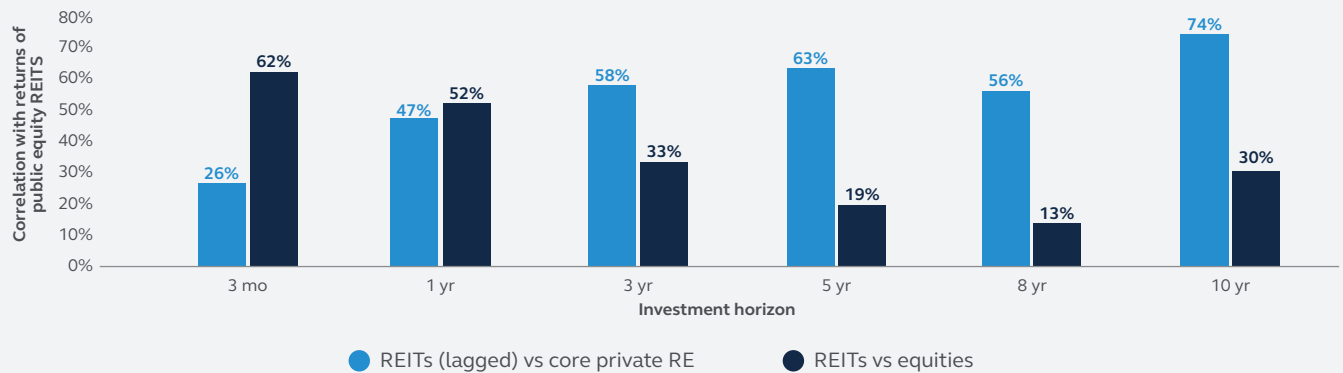
Source: Morningstar. This material has been obtained from sources generally considered reliable. No guarantee can be made as to its accuracy. Not intended to represent the performance of any particular investment. Indices are unmanaged and do not take into account fees, expenses and transaction costs and one cannot invest directly into an index. \*Please refer to the disclosures section for more detailed index information. Past performance does not guarantee future results.

## Low correlations to other public equities

The behavior of REIT stocks also leads to important diversification benefits through low correlations. Although many investors assume public REIT prices move in tandem with public equities, global and U.S. REITs are not perfectly correlated to equity markets, despite offering the same benefits of liquidity. In fact, when an investor increases their time horizon for holding REITs, as shown in charts below, REIT returns behave less like equities and more like underlying private real estate. That type of behavior can add important diversification to a portfolio of equities and bonds.

### Exhibit 2: REITs behave like private real estate, not stocks, over the long term

Over time the correlations of REITs rise with direct real estate and fall with equities



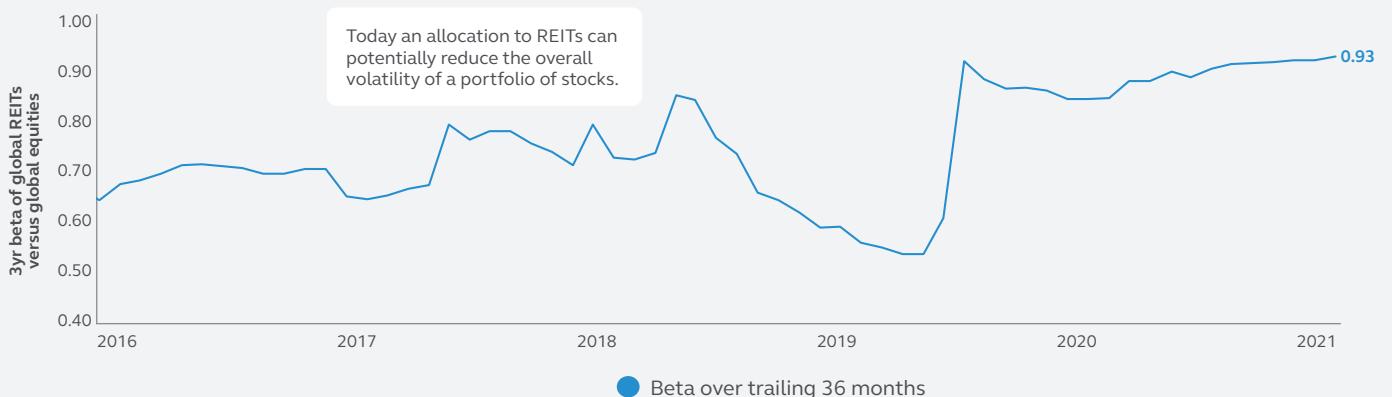
As of 30 September 2021.

Source: Analysis of data from FTSE NAREIT Equity REITs Index, NCREIF National Property Index, and S&P 500 Index from 1 January 1990 through 30 September 2021. Public REIT returns are lagged 4 quarters relative to private real estate returns to adjust for the return lag private equity funds experience due to less frequent measurement compared to public markets.

## Public REITs are a relatively low beta equity investment

When building a portfolio of different assets, an asset's beta is critical in understanding the impact on portfolio volatility. While standard deviation will explain the volatility of an asset's return compared to its expected mean return, beta will explain how much an asset return will fluctuate relative to another asset. With global REITs possessing a beta typically less than 1.0 versus global stocks, REITs tend to perform differently relative to equities in various environments. An allocation to REITs can help smooth out the overall volatility of your portfolio. REITs exhibit durable cash flow streams, high return on capital (dividends), and real asset ownership that can contribute to their defensive (i.e. lower beta) nature.

### Exhibit 3: REITs are often low beta compared to equities



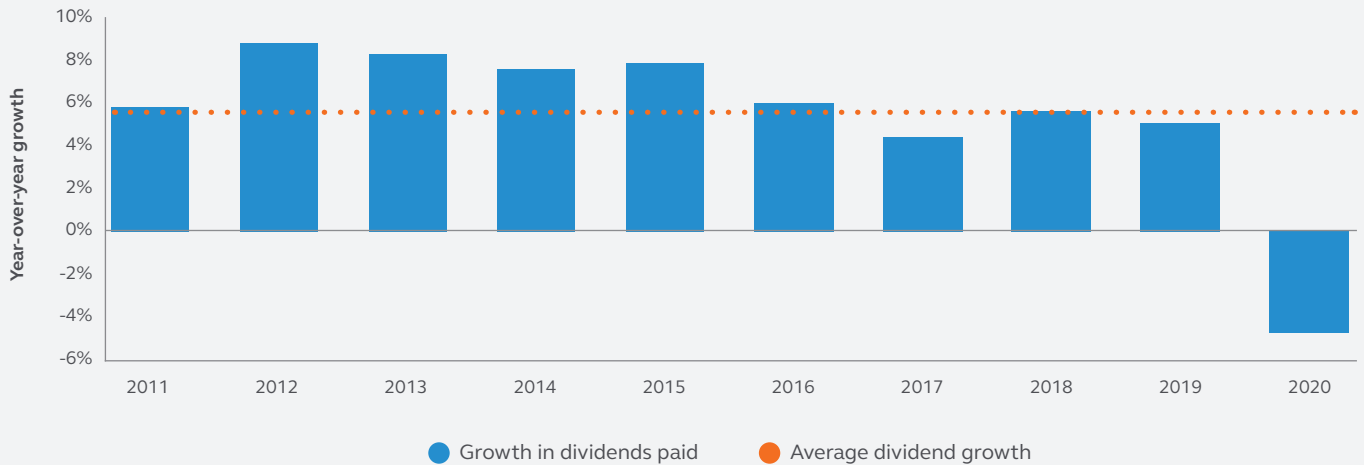
As of 30 September 2021.

Source: Datastream, UBS. Beta calculated using the slope coefficient of monthly REIT returns (FTSE EPRA/NAREIT Developed Index) vs monthly returns of equities (MSCI World Index) over rolling 36 month periods. This beta explains how much REIT returns fluctuate relative to broader equities. A beta of less than 1.00 means REIT returns do not go up or down as much as equities and vice versa for a beta over 1.00.

## Historical trend of rising income stream

Historically, REITs have been sought after for their higher dividend yields compared to most equity products. Due to their structure, REITs are not subject to taxes at the corporate level, and they distribute the majority of their taxable income to shareholders as dividends. Importantly, REIT dividends may provide a source of growing income for investors, with an average growth of 5.4% annually the past ten years. These growing cash flows are tied directly to the REIT's physical assets, with steadily improving occupancies and rents from leasing assets.

### > Exhibit 4: Over the last decade, Global REITs have had an average annual dividend growth rate of 5.4%



As of 31 December 2020.

Source: Factset. Index represented: FTSE EPRA/NAREIT Developed NTR.

Past performance does not guarantee future results. Dividends are not guaranteed.

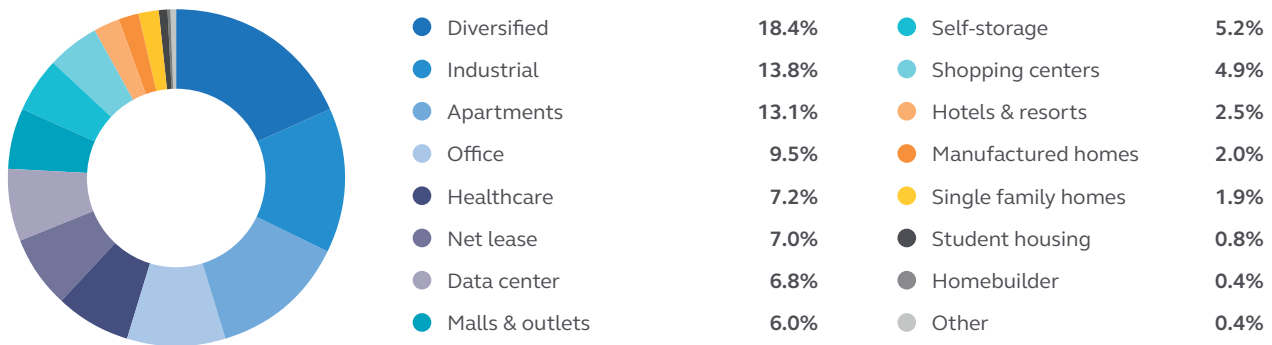
## Immediate exposure to real estate

As publicly traded entities, REITs are priced daily and are sometimes perceived as more volatile when compared to private equity real estate investments. However, the lagging appraisal method used by private real estate investments may not reflect large changes in real estate prices as they occur. The publicly traded nature of REITs reflects immediate changes in investor-required returns for real estate. Public REITs also offer transparency to operations and investor scrutiny of management. REITs provide an alternative to investing in physical real estate, which often requires a large capital and time commitment, by allowing immediate exposure to commercial real estate with a relatively small amount of initial capital investment.

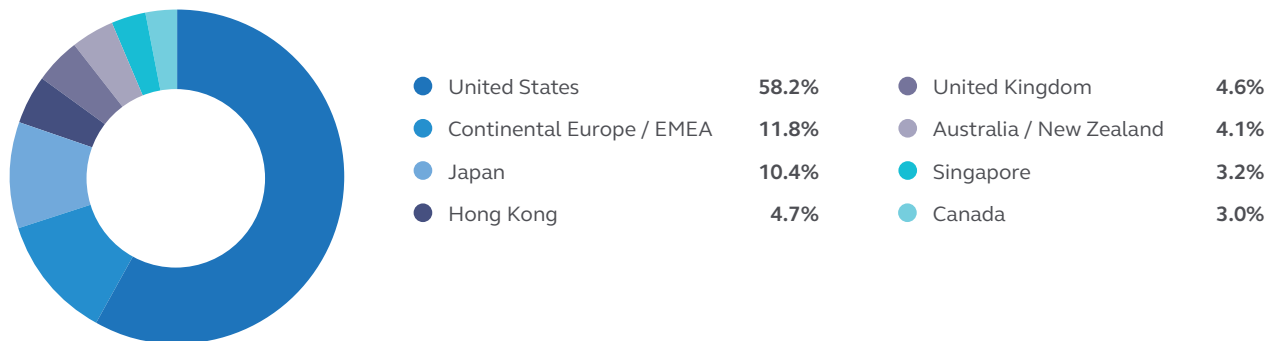
## Multiple layers of diversification

Market volatility illustrates the importance of deep diversification for investors. With REITs, investors have access to a variety of property markets, each market with its own demand and supply profile. Investors can also access property types that are not prominently available in the private commercial market: hotels, healthcare, data centers, and self-storage. A global REIT strategy offers an additional layer of diversification by providing access to countries with different currencies, monetary policies, and economic cycles.

### Global sector allocations



### Global country allocations



30 September 2021.

Source: FactSet. FTSE EPRA/NAREIT Developed Index country and sector. Due to rounding, percentages may not equal 100%.

# Why Principal?

## ✓ **The Principal Real Estate Investors advantage**

Our dedicated REITs capability was founded in-house by lead portfolio manager and chief investment officer, Kelly Rush. Kelly has led the team and strategy since the inception of the U.S. strategy in 1998, and has been with Principal for 34 years. Kelly and team are backed by a \$98.4 billion global real estate company<sup>1</sup> with over six decades of history investing in real estate. In their fundamental research work the REIT team can leverage the substantial in-house resources from private equity and debt real estate professionals, professionals in other asset classes across Principal, a team of global economists and top-notch technology and systems.

## ✓ **Quality at a reasonable price investment style**

When selecting stocks for the portfolio we emphasize owning quality companies at a reasonable price (QARP). Our experience has demonstrated, over long periods of time, portfolios with an emphasis on high quality companies may deliver attractive results.

## ✓ **Portfolio construction technique**

Our Global and U.S. Real Estate portfolios are constructed with high active share ratios and our sources of alpha diversified across a relatively large number of medium-sized active weight positions.

Importantly, this investment approach strives to deliver consistent and attractive risk-adjusted returns to our clients and attractive information ratios, a key metric in measuring the ability of an active manager.

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## **Points to consider**

Past performance is no guarantee of future results. Investing involves risk, including possible loss of principal. Potential investors should be aware of the many risks inherent to investing in real estate, including: value fluctuations, default risk, liquidity risks, leverage, credit risk, occupancy risk and legal risk. All these risks can lead to a decline in the value of the real estate, a decline in the income produced by the real estate and declines in the value or total loss in value of securities derived from investments in real estate. REIT securities are subject to risk factors associated with the real estate industry and tax factors of REIT registration. International and global investing involves greater risks such as currency fluctuations, political/social instability and differing accounting standards. Asset allocation and diversification do not ensure a profit or protect against a loss. Dividends are not guaranteed.

<sup>1</sup>As of 09/30/2021. Experience includes investment management activities of predecessor firms beginning with the investment department of Principal Life Insurance Company.

\* Small-cap stocks are represented by the Russell 2000 Index. Large-cap stocks are represented by the S&P 500. Global high yield bonds are represented by the BBgBarc Global High Yield TR USD; U.S. REITs are represented by the MSCI US REIT GR USD Index; Emerging markets are represented by the MSCI EM GR USD Index; Global REITs are represented by the S&P Global REIT Index; Private U.S. real estate is represented by the NCREIF ODCE Index; Developed markets are represented by the MSCI World GR USD index; Commodity is represented by the S&P GSCI TR USD index; Global investment grade is represented by the BBgBarc Global Aggregate TR USD; TIPS is represented by the BBgBarc US Treasury US TIPS TR USD.

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