LaSalle
INVESTMENT MANAGEMENT®

LaSalle Mid-Year ISA Update **2019**

JULY 2019

The Global Outlook at Mid-Year 2019

Thus far in 2019, the roar of political strife all around the world has been deafening. Yet national economies, capital markets and property markets seem to be relatively impervious.

It's as though businesses, consumers and investors are all wearing sound-canceling headphones. Six months ago, we predicted that Goldilocks was likely to slow down and take a nap eventually. But, in the first quarter, China and America drank Red Bulls and stayed wide awake.[1] By contrast, other G-8 economies–Canada, Germany, France, Italy, Japan and the U.K. - all slowed down, but not as much as the rough politics in any of these countries might have led analysts to expect.

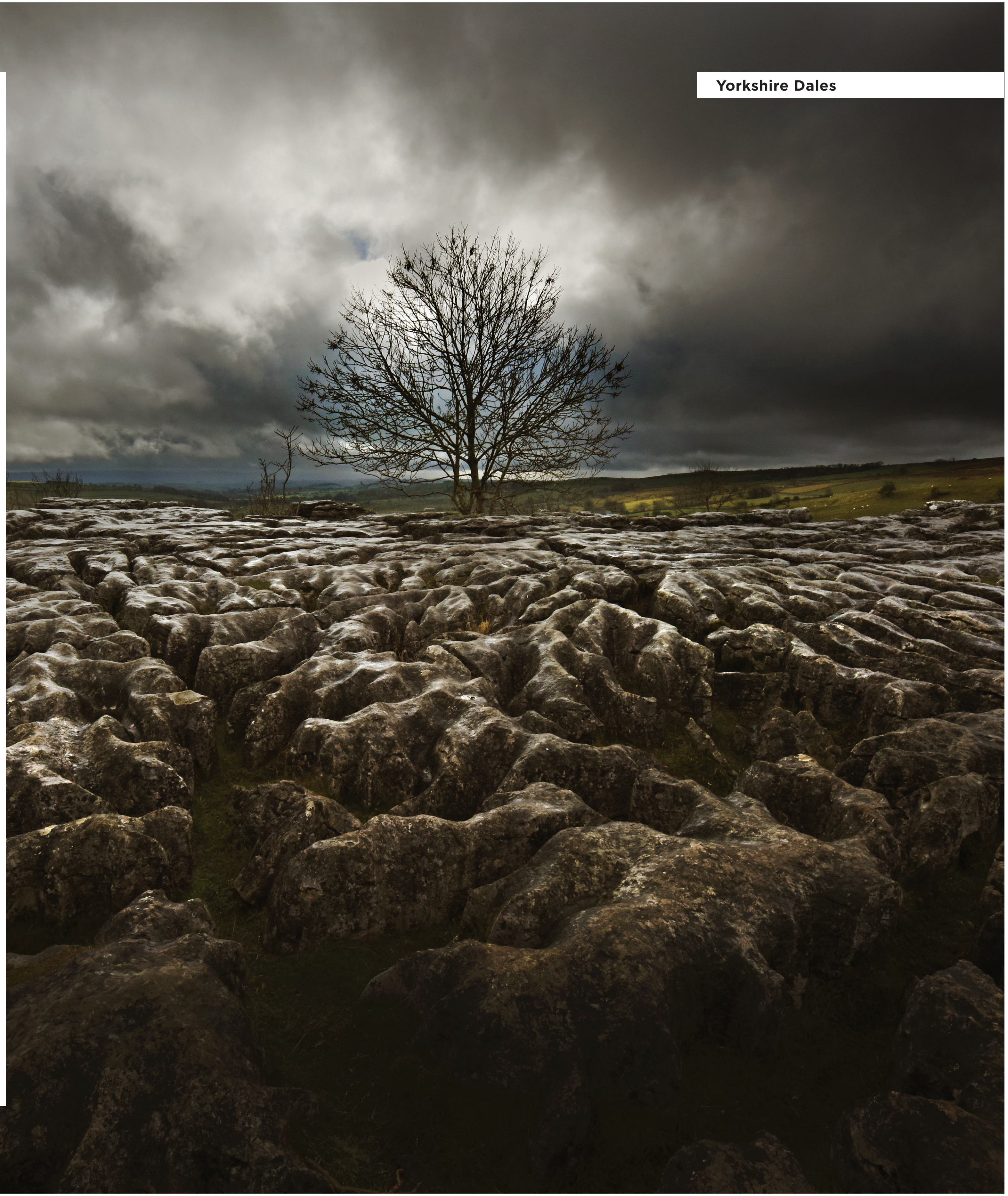
As the second quarter closes, momentum has shifted downward. Economists from the IMF, Oxford Economics, and the Bloomberg Consensus poll all believe the world is facing a global slowdown. The triggers for "Slowbalisation" include aging societies, the rise of nationalism, and trade disruption.[2] The IMF suggests that the halt in global trade growth will likely shave as much as 50 basis points from global growth rates. Yet, as our monthly macro decks have shown, the capital markets generally remain strong. Stock market indices have bounced back after taking losses when the U.S.-China trade wars escalated on May 10th. Debt is cheap and plentiful. Credit spreads are not gapping out anywhere, except in a few over-leveraged or weakening sectors around the world.[3]

1 Some of this economic activity was due to inventory adjustments--in anticipation, perhaps, of a coming trade war. Nevertheless, both economies out-performed expectations (China-6.4%, U.S.-3.2%)
2 The term was coined in 2015 by Adjiedj Bakas, a Dutch author and megatrend-watcher.
3 Examples of over-leveraged or weakening sectors around the world include: regional banks in China, brick & mortar retailers in the U.S., homebuilders in Australia, German automakers and suppliers, and industries that produce capital goods in many different countries. See: The World Economic Outlook April 2019, International Monetary Fund.

As the classic novel titles suggest, political sound and fury does not necessarily lead to economic destruction. So far, political hardball has not interrupted a Peter Pan economy that never seems to grow old.[4] By contrast, the capital markets are in the midst of a tense story.[5]

A gothic novel like ***Wuthering Heights*** represents the anxious view of peak pricing in the asset markets. The financial counterparts to the windswept Yorkshire moors are the swings in the securities markets which,for now, have no parallel in private equity real estate. The wild, untamed spirits of the capital markets are fed daily by accommodative monetary policy, rising leverage, computer trading, and a constant surplus of capital relative to assets.

4 A synchronized recovery has been underway in developed countries since the end of the Euro crisis in 2010-11. A Peter Pan economy is even better than a “Goldilocks” one. Peter Pan economies never grow old, while Goldilocks’ rest is eventually disrupted by returning bears. Australia and China are the best examples of Peter Pan economies. Four of the most productive economies in the world -- Germany, the U.S,. the U.K. and Singapore—are Goldilocks economies because they experience recessions, on average every 7 to 10 years.
5 Adam Tooze’s book, Crashed: How a decade of financial crises changed the world, Viking Press 2018, traces the fundamental mechanisms that create cross-border co-dependence in the financial markets.



Yorkshire Dales

Real Estate Markets

Real estate fundamentals and pricing have both performed well, regardless of which novel you pull off the shelf.

Political uncertainty has kept interest rates low on sovereign debt. One-fifth of all government bonds produce zero or negative interest rates. German bonds hit a record low negative yield in late May and early June. Investors remain starved for yield and real estate is one place they can still expect to earn positive dividends. This is a dependable story, but not without occasional adventures up and down the riverbank[6]. Private equity real estate investors have a way of avoiding calamity in much the same way that the characters in ***Wind in the Willows*** do—by avoiding confrontations, making friends, telling tall tales, and occasionally resorting to disguises. At this stage of the property pricing cycle, we know that there are real estate sectors, like weaker shopping centers or disconnected office buildings, that already are, or soon will be, in serious financial trouble. Yet, price discovery can take several years as owners avoid selling and memorializing any losses. In the meantime, banks will still lend money to owners who contemplate property makeovers, not all of which will be entirely successful.

In preparation for an inevitable cyclical downturn, as we stated in our 2019 ISA, “Even if a global slowdown occurs, investors in real estate can take a long-term perspective by building portfolios that survive down-cycles and thrive in up-cycles.”By combining both secular and cyclical themes in their investment strategies, investors can ensure a healthy income stream and value preservation regardless of the scenario.

As the year has unfolded, the space between real estate’s winners and losers is getting wider. Investors are putting record-high valuations on logistics properties all over the world, while investors shy away from retail properties and older offices that lack strong urban or suburban networks. The office sector has been propped up by co-working absorption and tech momentum, but the costs of leasing to tech tenants is high. The amenities they demand are expensive. Rental residential markets are generally faring well in many cities, but they are beset by new policy initiatives that may hurt their values in the future.

In our sidebar “Urbanization Reimagined”, we warned that the rising cost of rental accommodations in the world’s major cities was becoming a growing concern of policy-makers. By mid-2019, Berlin, New York City, and the entire state of Oregon all put residential rent control regulations in place. Similar regulations have been proposed in London, Los Angeles, Minneapolis, Philadelphia and Seattle. In many European cities, the rental sector is divided between “social housing” and the “private rental sector”. The backlash against the newer market-oriented stock of rental housing is a trend worth paying close attention to. Housing authorities in China, the Netherlands, and France are putting restrictions on apartment buyers to prevent them from renting out units. The idea behind this is to curb escalating housing costs and keep speculators out of the ownership market, but the unintended consequence is that this raises the pressure even more on the private rental sector to house young workers moving to cities. From an investment perspective, the high cost of living in gateway cities is a sign of thriving urban economies. The risk is that local officials will create rent control regulations that may lead to dis-investment, rather than the investment that is needed to create enough new stock for all the migrants to successful cities.

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6 The reference is to Kenneth Grahame’s classic The Wind in the Willows, first published in 1908. Grahame was the Secretary for the Bank of England at a tumultuous time. He was shot at by anarchists in 1903 and he quarreled frequently with the Governor of the Bank. His reaction to the stresses of the job was to retire at age 49 and launch a second career as an author of books for young adults.

After reviewing all the specific strategies within each country where we are active, we maintain our recommendation for investors to pursue both “low beta” and “positive alpha” strategies.

The core/beta strategies will withstand volatility in other asset classes best. A “positive alpha” strategy takes carefully calibrated risks and gets rewarded for doing so. These Alpha and Beta strategies serve a dual purpose. As volatility rises and global growth begins to slow, income stability and low responsiveness relative to the broader equity markets plays an important part in an investment portfolio. The second goal (positive Alpha) seeks specific assets and sectors within real estate capable of contributing to out-performance relative to the steadily declining core property indices in many countries.

Alpha strategies do not have to be highly-leveraged, risky adventures, like Mr. Toad’s Wild Ride[7]. Success is usually highly asset-specific and tactical. It is also dependent on buying at an attractive basis and executing on a clear, value-added leasing or re-positioning strategy. A global slowdown may mean that it will take longer to execute these strategies, but it need not derail the ones that have secular tailwinds to support them.

7 This is another Wind in the Willows reference.

Macro Risks and Opportunities

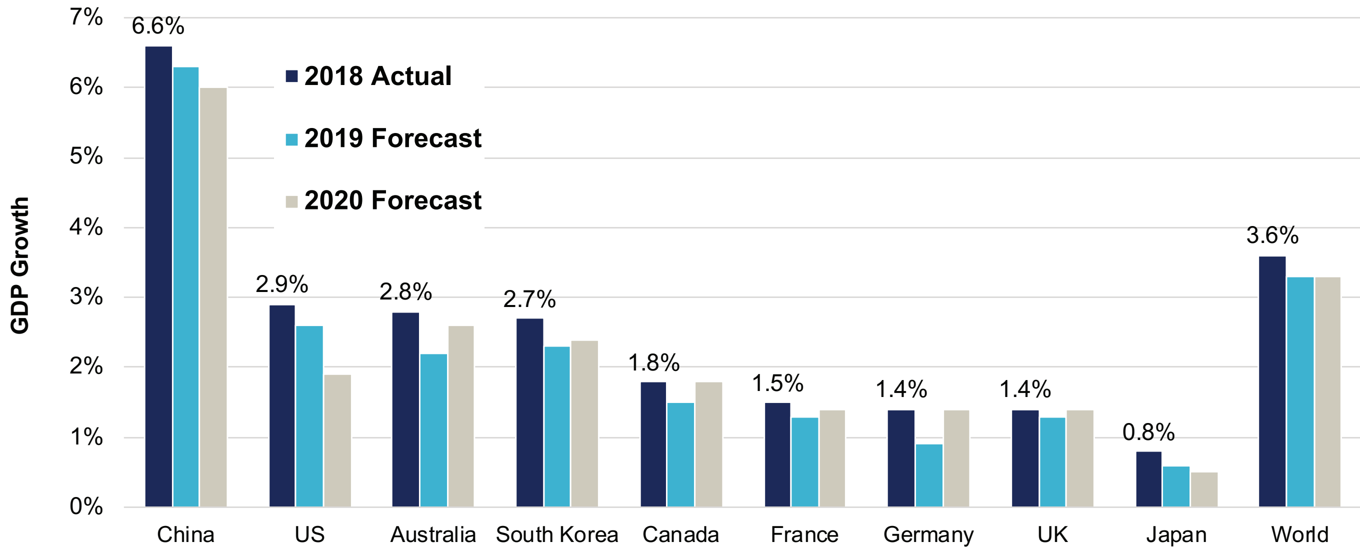
Our updated cycle charts show the fundamentals of real estate are relatively strong. Supply and demand are balanced in most major markets. Pricing is high in absolute terms, but yield spreads are generally within a "fair value" range. The recent rally in bond prices pushed sovereign yields lower and have brought more real estate sectors from the "expensive" back to the "fair value" range.

Both alpha and beta strategies should continue to produce strong returns through the end of the year. Lower bond yields create a strong foundation for real estate capital value stability, wherever they are found. As we reported six months ago, it will continue to be a market where selling will be easier than buying. Many of the country-specific strategies that we recommended in the 2019 ISA[8] still hold up as strong target sectors for investment. The regional strategy section that follows in Chapter 2, describes what, if anything, has changed as investors pursue strong core and non-core returns.

The downside risks to the current benign real estate outlook are many. They mainly come from the political sphere, which could cross over to economics, capital markets, and eventually to real estate. The uncertain future of trade alliances, geo-political tensions, and nationalistic responses to these disputes are difficult to assess. The risks are significant, but conciliatory political actions can remove the threats as quickly as they were put on the negotiating table[9]. LaSalle's recent round of House View discussions does not put another financial crisis or a global recession into the base case. But, they do put a slow ebbing of the global economy and a harder-edged drop in cross-border trade as two likely risks to consider when investing in and managing portfolios of real estate in the G-8 countries.

Consensus Forecasts for GDP Growth

BLOOMBERG CONSENSUS GDP GROWTH FORECASTS

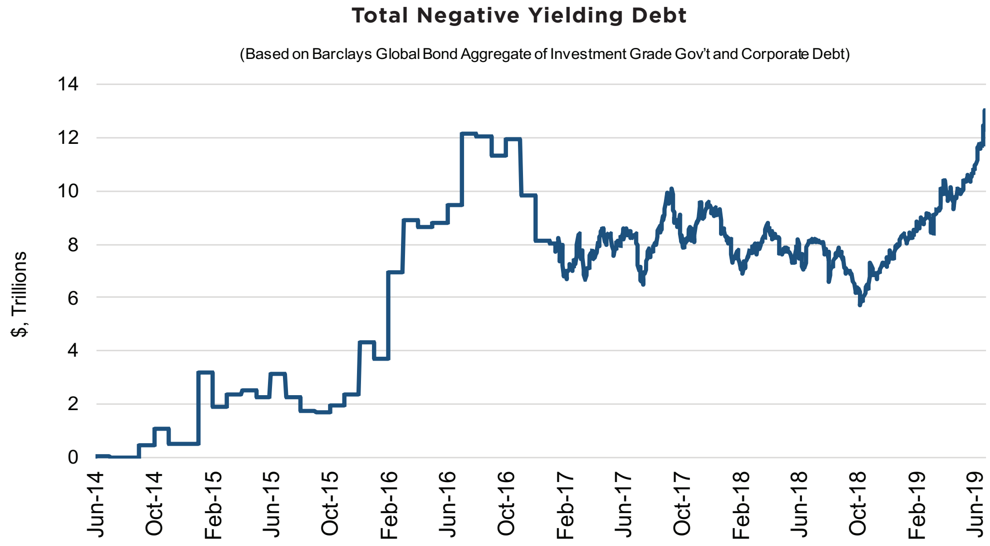


Source: Bloomberg survey of forecasters – Latest forecasts as of 29 May 2019

8 Investment Strategy Annual 2019.
9 A recent example in early June was the proposal by the U.S. to put tariffs on Mexico, a proposal that was then withdrawn a few days later. By mid-June, new examples surfaced with Iran-U.S. relations and with the possibilities for a China-U.S. summit back on the table.

Negative Yielding Debt Grows as Sovereign Bond Rates Fall

INTEREST RATES LOWEST SINCE LATE 2016, AND LOWEST EVER IN GERMANY

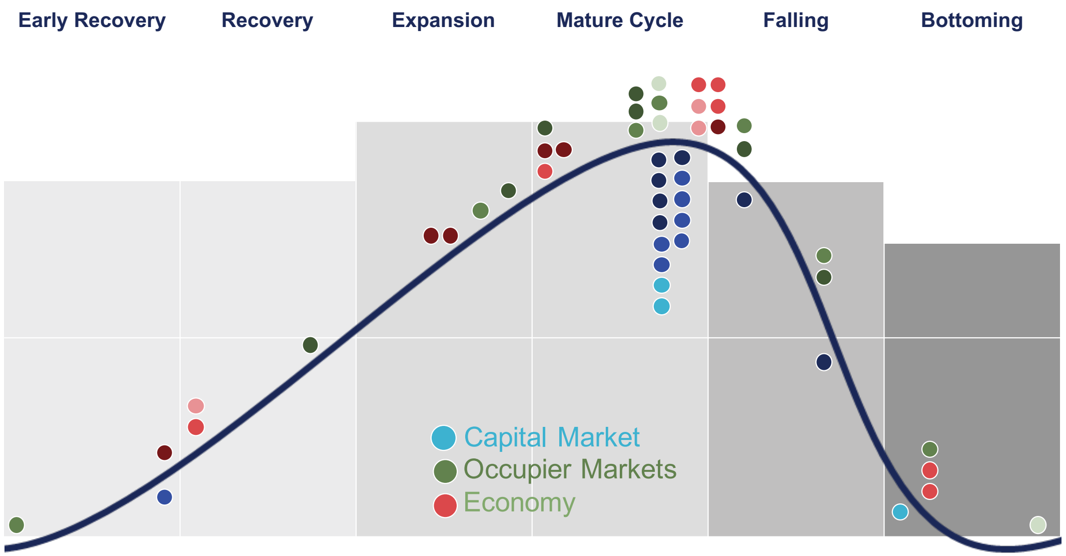


24% of debt securities in the Barclays Global Bond Aggregate now have a negative yield.

Source: Bloomberg, LaSalle. Data through 21 June 2019. Note: Past performance is not indicative of future results. There is no guarantee that any trends shown herein will continue.

Where Are We in the Cycle?

MOST CAPITAL MARKETS ARE MATURE BUT FUNDAMENTALS ARE MORE DIVERSE



Each bubble represents a single county's capital market or occupier market
Color shading: Europe (dark), Asia Pacific (medium) and North America (light)

Source: LaSalle (06/19)

North American Outlook

The U.S. and Canada both experienced benign real estate market conditions in the first half of the year. Even in a world of trade turmoil, the two countries moved towards closer integration and cooperation. For example, the 2018 steel and aluminum tariffs between the two countries were rescinded and the threatened Mexico/U.S. tariffs were also taken off the table. Because the three large North American countries are so integrated in terms of supply chains, exports and imports, this has been a welcome relief.

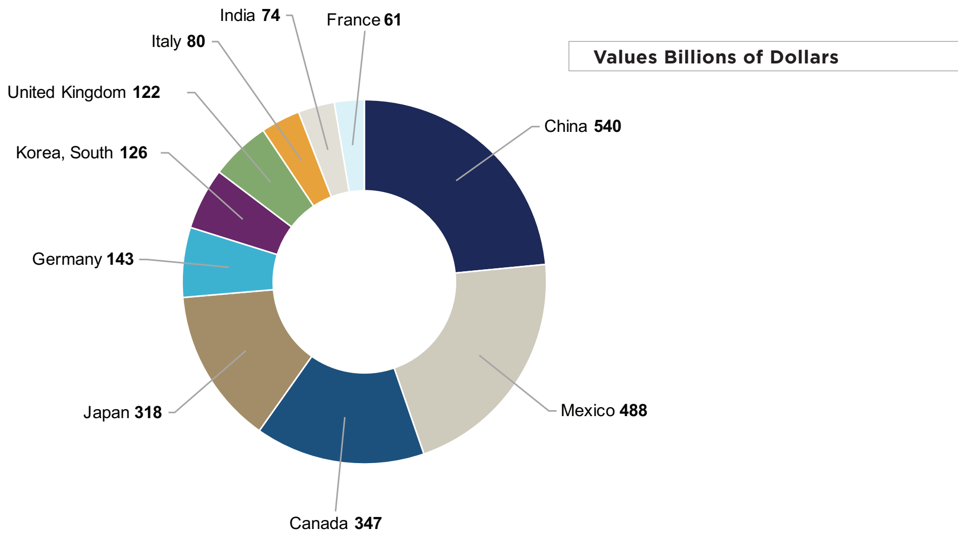
U.S. Stability Amidst Trade Uncertainty

The trends and themes highlighted in the 2019 ISA were largely reinforced in the first half of the year, with a few notable exceptions. The over-arching theme of our outlook was that real estate fundamentals and capital markets have been remarkably stable in macro and political environments that are volatile. This situation remains true at the halfway mark of 2019. Our U.S. outlook on trade, interest rates, and micro-driven investment strategies are updated on the right.

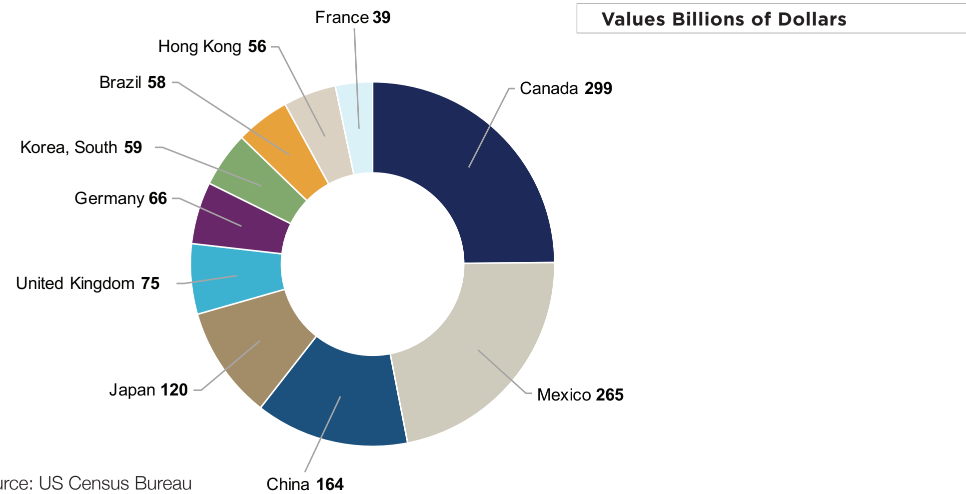
Trade news was relatively quiet for the first four months, but starting in May and accelerating into June, it again dominated the economic news. The U.S.-China trade dispute flared up in early May, as wide fissures between the parties emerged. President Trump initiated his earlier plan to put 25% tariffs in place on an additional \$200 BN of Chinese imports to the U.S. China responded in turn, but with over \$500 BN of goods going from China to the U.S. and less than \$150 BN going the other way, China is more vulnerable than the U.S. In addition, a new front opened in the U.S.-China trade war when the U.S. put restrictions on the operations of technology firm Huawei. This will have ramifications for technology firms up and down the supply chain and around the world. It remains to be seen how extensive the Chinese response will be. For now, an adversarial relationship between the

TRADE WARS
RE-IGNITING ON MULTIPLE FRONTS

Top 10 Sources of U.S. Imports
(Countries Shown 70% of Imports)



Top 10 Destinations for U.S. Exports
(Countries Shown 63% of Exports)



Source: US Census Bureau

U.S. and China is the status quo and there is limited optimism a broad agreement will be reached quickly, but as with all elements of U.S. policy today, things can change very quickly.

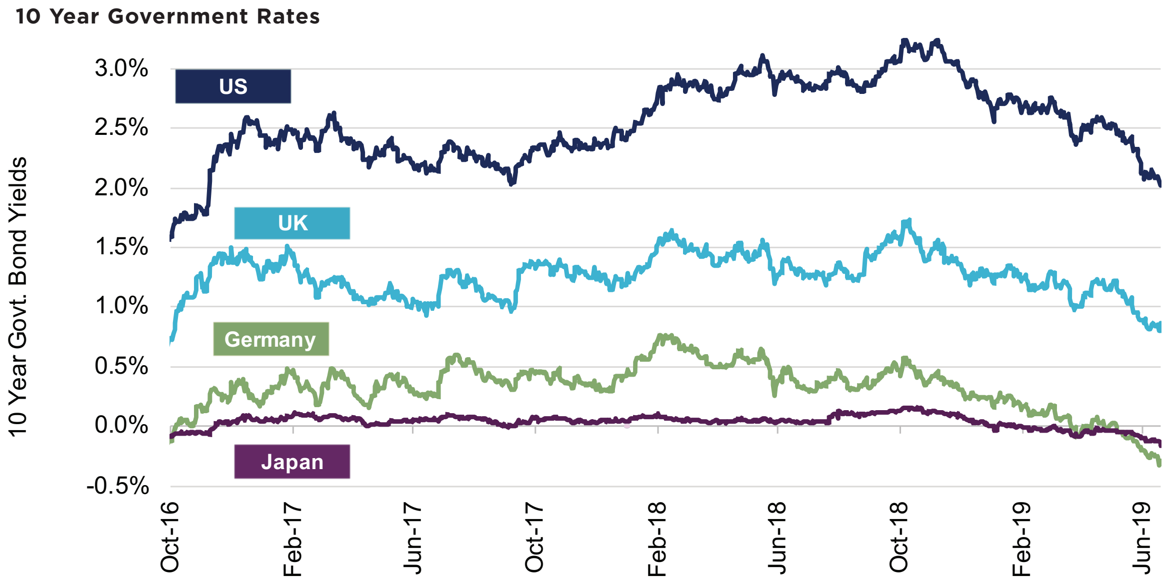
China is not the only U.S. trade partner where trade disagreements are in the news. U.S. trade with the E.U. has been tranquil since an agreement to work towards a solution last year. But as time passes without an agreement, the risk increases that new tariffs will be imposed. The potential implementation of automobile tariffs would have a significant impact on both U.S. consumers and European manufacturers. Intra-North American trade also burst into the headlines with a May 30 tweet the U.S. would implement tariffs on Mexico. Until then, the new North American trade agreement (USMCA) was facing an uncertain outlook in the U.S. Congress, but the legacy NAFTA agreement was still in effect. This apparent détente made the introduction of new tariffs against Mexico tied to controlling migrant flows to the U.S. even more of a surprise. The threat was rescinded on June 7, following a few weeks of market noise and talk from the Federal Reserve of rate cuts to pre-emptively offset the impact this could have on the U.S. economy. The heightened level of uncertainty that comes from erratic policies, even if never implemented, is a greater negative on U.S. economic growth than we expected, and it will negatively impact our outlook.

One thing learned in 2+ years of tariff-driven trade policy is that the direct impacts on specific goods and companies are not the most significant impact on the U.S. economy. More meaningful, especially on the larger U.S. metros where institutional real estate investors focus, is the undermining of confidence to make decisions, around both investment and consumption. As the tailwind from tax cuts starts to fade, the negative impacts of trade and policy uncertainty could weigh more on economic growth.

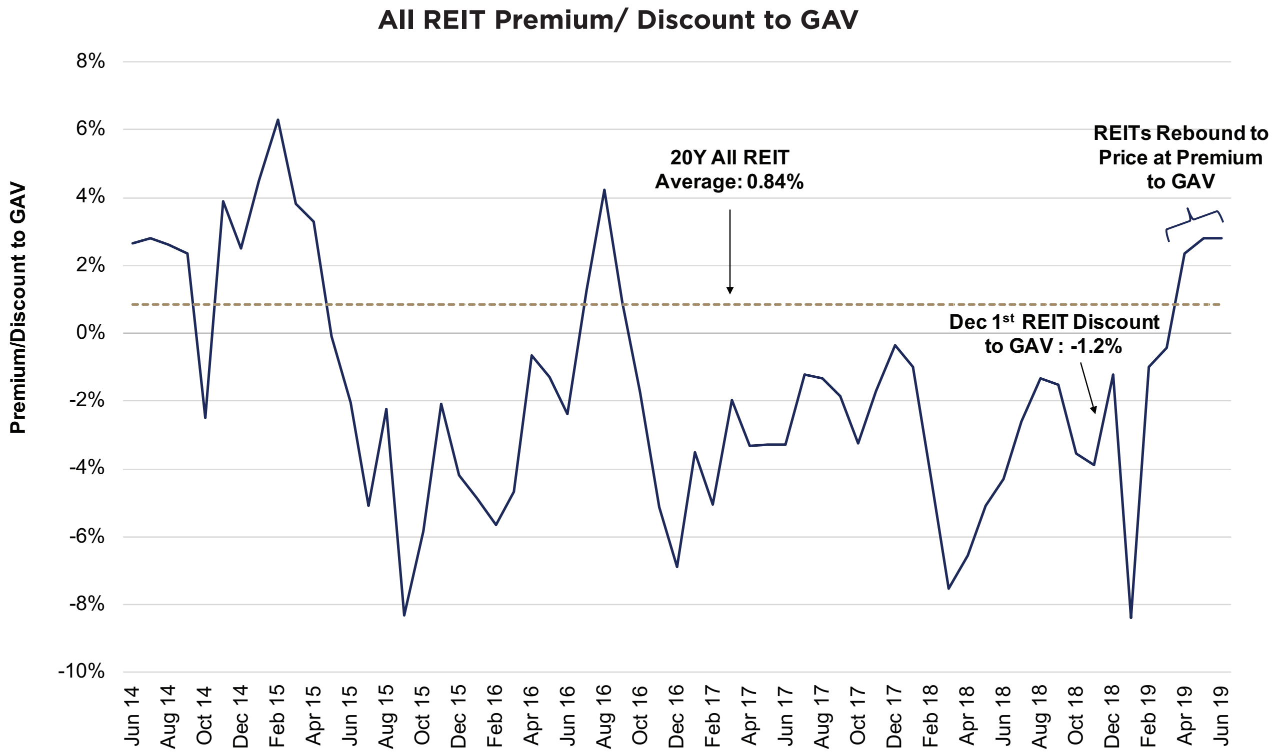
In the 2019 ISA, the U.S. discussion of interest rates focused on rates moving higher and what that means for the attractiveness of real estate relative to bonds, and the potential negative impacts higher interest rates could have on real estate values. Six months later, the situation and the focus are very different. The deterioration in the stock market and economic outlook in late November and December changed the outlook from rate hikes in 2019, to the Fed standing pat, and now to lower interest rates in the near future.

Long-term interest rates (tracked in this case by the 10-year U.S. Treasury Note) remain our guide for core real estate value comparisons. These have moved more than 100 bps lower from the 3.2% rate quoted in the ISA and have most recently moved below 2%. All other things being equal (which they never are…), lower interest rates are a positive for our outlook for real estate values. There were concerns about downward pressure on real estate values if the 10-year note were to rise above 3.5% towards 4.0%. With the 10-year note now close to 2.0%, lower

Interest Rates
LOWER FOR EVEN LONGER



Source: Bloomberg, LaSalle. Data through 21 June 2019. Note: Past performance is not indicative of future results. There is no guarantee that any trends shown herein will continue.



Source: Green Street Advisors. Data through June 1, 2019. Latest data as of June 17, 2019.
Note: Past performance is not indicative of future results. There is no guarantee that any trends shown herein will continue.

bond yields, and the expectation they will remain low, are much more likely to be a tailwind than a headwind for real estate values. The public markets are picking up this tailwind, as the Public REITs have rebounded to price at a premium to estimated GAV for the first time in two years.

The dynamics of lower interest rates is not universally good news for real estate and real estate values though. The decline in the 10-year note coupled with instability in short-term rates has inverted the 3 month-10 year yield curve (the 2 year to 10 year curve remains barely positive sloping). An inverted yield curve has historically been the most reliable predictor of recessions, with each of the last 9 recessions preceded by an inverted yield curve (with an average lag of just over 12 months). While there are "this time is different" arguments that lower global yields or the falling long-end are contributing to the yield curve inversion, it is our view that this is not a signal to ignore. We take it as a signal to reiterate the recommendation in the 2019 ISA to take actions to insulate portfolios from the impact of a cyclical downturn.

Going Micro...with Secular Drivers

The 2019 ISA recommended investing alongside secular trends that have the potential to overcome cyclical factors. In the first half of 2019, we have focused on pursuing and understanding the tracking of retail customers with mobile phone data. While some analysis using the new data is often obvious (the shape of the trade area and where customers come from), other aspects are less intuitive and require benchmarking. This data is of greatest use in retail and residential properties, where the micro-movements of individual users are an important factor in understanding how well-located the property is.

DTU+E continues to frame our approach to investment strategy. Demographic shifts continue to drive real estate demand, and we remain focused on residential strategies that will take advantage of these demographic shifts. Meanwhile, our perennial under-weight recommendation in offices is reinforced by the slower growth in the workforce associated with the steady retirement of the baby boomer cohorts that will limit office demand.

Technology continues to shape the nature of space usage and the ways that we study that demand. The impact tech firms are having on office demand is a good example. Potential regulations of large tech firms and the impact of trade wars threaten to curtail this demand, but as of now we are more optimistic it will remain a long-term tailwind. And the "gig-work" associated with the delivery of entertainment content is becoming a major positive for office demand in Los Angeles. Tech also continues to impact what we consume, where we acquire it, and how it reaches us. The rising demand for experiences and the falling demand for ownership of cars and residences creates an opportunity for re-making retail places. But it is highly uncertain if experience delivery can be monetized by real estate owners in the same way consumption was monetized through sales productivity closely linked to rent levels.

One market risk mentioned in the 2019 ISA that has yet to materialize is the supply risk driven by Opportunity Zones. This still might lead to some over-supply, and it may have just been delays in creating clear regulations that has pushed back the impact. But as we look at investments, the supply pipelines in areas in or close to Opportunity Zones, and the discipline in developer's underwriting we are not seeing signs of rampant development driven by a flood of capital into this program.

Stability Still Reigns for Real Estate

A major theme of the 2019 ISA was remarkable and unusual stability of national real estate fundamentals, rents, returns, and capital markets activity. That stability has not changed in the last six months, even with the stock market on a roller coaster and global politics stirring the economic pot. Real estate fundamentals are playing out as expected and real estate capital markets remain highly active. Returns are stable, driven by income with limited appreciation and by income growth rather than cap rate compression. New supply is increasing in some markets, but as expected, not at a level that would drive up national vacancy rates. And demand has remained firm to start 2019, with the longer term, negative economic signals not yet hitting the real estate market.

Retail continues to be buffeted by secular changes driven by the growth of e-commerce. The impact is less than in some other markets around the world--in the U.S., the distress is concentrated in the mall and big box retailer segments. Industrial demand remains very strong and new supply is still muted in many markets relative to what might be expected given the very strong returns and pricing that is well above replacement costs. Apartments remain a target for core investors due to the stability they are expected to provide should economic growth slow. One cautionary note on apartments is that in several major investment markets, there is political momentum around rent control and other restrictive operating regulations, with the most notable implementation being new rent control regulations in New York City. Not all of these are major negatives for institutional investment in apartments. Regulations are often structured in a way that has little impact on Class A apartments, but workforce housing might be more directly affected and the direction of change is not a positive for investment.

Offices experienced weaker demand in the first quarter following a strong fourth quarter. The most significant trend in the office market is the growth of flexible office arrangements, and that continues to evolve, with some owners getting into the business, more management agreements, and the pending IPO of WeWork. These trends are impacting how we evaluate and value office investment opportunities. Questions related to how an office asset might appeal to flexible office operators or how its tenant base might be impacted by competition with other flexible office operations are high on the list when evaluating office investment.

Retail continues to be buffeted by secular changes driven by the growth of e-commerce.

Several of our investment recommendations--take advantage of repricing on urban apartments and lower values in high-quality retail--hinged on changes in capital market conditions. There is limited evidence of these shifts in the capital markets yet, and few opportunities to execute thus far. As highlighted in the 2019 ISA, the investment environment remains challenging, with risks and opportunities both fairly priced.

The capital market trends in the 2019 ISA have played out as expected with capital flows to real estate, but from a changing set of channels and types of funds. The traditional open-end core (ODCE) funds are treading water in terms of capital flows, but with shifting capital allocations across different funds. These funds are generally looking to increase industrial and apartment allocations at the expense of office and retail. Institutional investors have not had their allocations impacted by major denominator effects, as through the stock market's roller coaster, broader equity returns have out-paced private real estate returns. The growth of core and core-plus non-traded REITs is boosting the investor demand for some higher-risk, higher-yielding assets. The recovery in securities prices has brought REITs overall to a small premium to private values but it is very sector specific, so we expect more acquisitions by industrial, apartment, and niche REITs, while retail and office REITs are expected to remain on the sidelines and even be net sellers.

Looking Ahead to the Second Half of 2019

Broadly, we expect more of the same market trends in the second half of 2019 as experienced in the first half of the year. If economic risks are accelerated, the impact is more likely in 2020 than in 2019. There are no rumbles of major changes in the property markets, so we expect stability to continue to reign. Our Capital Markets Dashboard was designed to give a 6-12 month warning signal on downward shifts in property values. At mid-year, the dashboard shows an overall positive assessment with a few caution signals, as has been seen for the last several years. While the stock market is indicating broad investor optimism, we are mindful the bond market does not share that view; and the expectation that the Fed will cut interest rates is coming from a place of economic weakness, not strength. As we continue to invest and manage real estate, our activities are informed by a view that a slowdown could be coming in 2020, while the upside is that growth merely moderates and Goldilocks conditions persist with low interest rates, low inflation, and moderate economic growth.

Canada: ISA 2019 Mid-Year Update

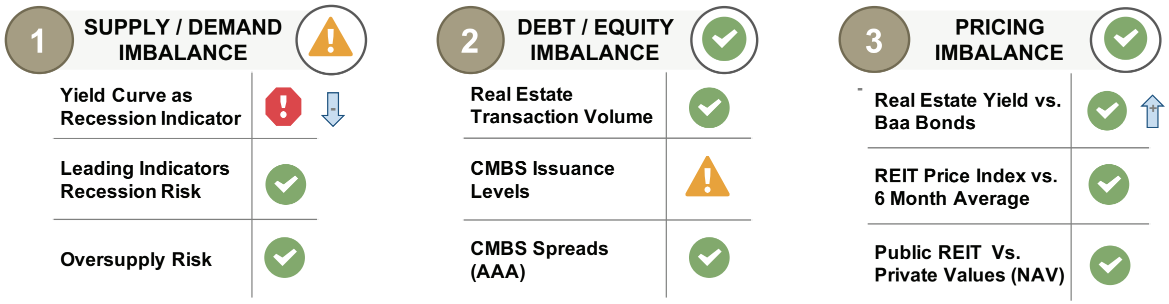
Canada's economy slowed to an annual rate of 0.4% in 1Q19 and is expected to finish the year with 1.1% growth, lower than anticipated in the ISA 2019. Reduced housing activity and slower retail sales, combined with weaker exports and tepid business investment, were the drivers of the slowdown. This did not, however, put a halt to the 'Goldilocks' real estate investment market conditions. Job growth has served as both an offset to slowing GDP and has been the key driver of real estate demand, fueled by rising immigration and strong tech sector expansion, pushing Canada's unemployment rate to a near a 45-year low of 5.7%. Rising immigration has also driven apartment demand to a 10-year high, while national industrial availability rates are at an all-time low, and high single-low double-digit annual rent growth continued in most markets. CBD office markets in Toronto, Vancouver and Montreal continued to tighten. Equity markets rebounded from their sharp December decline. Finally, 5-and 10-year bond yields have declined by 90-95 bps since 3Q18, supporting real estate values, reducing debt costs, and maintaining strong investor demand.

The steel and aluminum tariffs put in place between the U.S. and Canada in 2018 have recently been rescinded, paving the way for the expected ratification of the U.S.-Mexico-Canada (USMCA) trade agreement in the coming months. However, persisting global trade tensions, particularly between China and the U.S., have repeatedly been cited by the Bank of Canada as a reason for caution regarding future growth. Consequently, the Bank is likely to hold rates steady for the remainder of 2019.

Despite gyrations in some segments of the capital markets, most market indicators tracked by LaSalle in Canada are positive,

U.S.: Capital Markets Showing Warning Signs

1 OF 9 INDICATORS NOW SIGNALLING "CAUTION"; 1 SIGNALLING DANGER



Caution and Danger Signals:

- **Yield Curve:** The yield spread of 10-year to 3-month treasuries turned negative at -13 bps as of 27 June 2019, the lowest it has been since 2007. This puts the indicator in "Danger" territory. An inverted yield curve is a key recession warning sign and this signal merits attention and consideration.
- **CMBS Issuance:** In May, trailing year issuance fell by 10.1% in June, putting the indicator in "Caution" territory.

Source: LaSalle. Updated June 27, 2019. Note: Past performance is not indicative of future results. There is no guarantee that any trends shown herein will continue.

with the exception of brief yield curve inversions in March and June. While this is often a recession warning in the U.S., this has not always been the case in Canada. Our investment outlook has not changed as even with slower GDP growth, job growth remains strong and new supply remains muted (even in industrial). GDP is expected to rebound to trend levels beyond 2020. Canada's immigration policies which favour "economic category" immigrants, meaning those who are educated and highly skilled, are playing a strong role in tech job growth. This trend is expected to continue as higher immigration levels have been targeted beyond 2019-2020.

REITs in Canada have touched an all-time high in recent weeks, as measured by the S&P/TSX Capped REIT Index. Industrial and apartments have seen remarkably strong rental growth, with office rents also increasing due to low vacancy in the CBDs of Toronto and Vancouver.

Cap rates have remained largely flat from year-ago levels, with very modest (roughly 5 bps) upward moves for out-of-favour retail assets and non-investment grade offices. There remains strong investor demand and further downward cap rate pressure on best-in-class industrial, apartment and CBD office assets. In 2018, transaction volumes hit a record $49 billion in Canada, and while the first quarter of a year is typically slower (as it was in 1Q19), there has been a recent uptick in trades and new offerings which will support strong trade volumes again in 2019.

Our recommended Canadian 'best opportunities' in the ISA 2019 consisted of non-trophy CBD offices and major market warehouses, while secondary opportunities included urban apartments, urban grocery-anchored centres and high street retail. We have not changed these calls, but note that strong competition continues for the most desirable assets. Our call on non-trophy offices is driven by the fact that tightening vacancy and rising rents benefit all CBD office types, but cap rate premiums remain for non-trophy offices compared to aggressively-bid trophy offices. Office renovation and warehouse development also remain good higher return options. We remain cognizant of the changes and challenges facing retail and note the sector has been shunned by investors, with the lowest returns in the MSCI Canada Property Index in recent years. Despite this, mis-priced opportunities do arise on occasion, and astute investors should seek retail opportunities where they can add density, renovate or re-purpose underused mall space, or entitle excess land for residential zoning and development. These strategies are key ways to add value, enhance returns and outperform in today's retail environment.

For the remainder of 2019 and going into 2020, Canada's major markets continue to occupy three cycle phases: Early cycle (Calgary, Edmonton), Mid cycle (Ottawa, Montreal) and Late cycle (Toronto, Vancouver). The recovery in the early cycle markets is expected to be slow and gradual, but we note that in terms of fundamentals, these markets have shown modest occupancy improvements. The mid cycle markets have been driven by tech job growth, with added public sector hiring benefitting the Ottawa market. Meanwhile, the late cycle markets have seen fundamentals tighten further, driving strong rent growth.

North American Investment Recommendations: 2019

STRATEGIES ALIGN WITH DTU+E THEMES, INCORPORATING PRICING IMPACT

BEST OPPORTUNITIES | SECONDARY OPPORTUNITIES

LASALLE'S TOP US STRATEGY RECOMMENDATIONS

	CORE		HIGHER RETURN
MULTIFAMILY	**US: Suburban Income Strategy, Off-Price Urban**	**US and Canada: Mixed Use**	US: Select Development Strategies
	Canada: Urban		Canada: Suburban Repositioning, Build to Core
OFFICE	US: Medical Office, Creative/ Edge of Core Urban		**US and Canada: Renovation/ Lease-Up**
	Canada: Non-Trophy CBD		
RETAIL	**US: Top STARS* Centers, Urban Retail**		US: Mis-pricing situations
	Canada: Urban Grocery-Anchored, High Streets		Canada: Mis-pricing and Re-Positioning / Densification
WAREHOUSE	US: Locations Positioned to Serve Large Populations		**US and Canada: Modern Warehouse Development**
	Canada: Major Markets		Canada: Small-bay Lease-Up, Alberta

*Supermarket Trade Area Ranking System. Propriety LaSalle ranking of over 40,000 U.S. supermarket anchored shopping centers.
Note: The information shown herein is based on the research and market analysis of LaSalle Investment Management and nothing herein constitutes a guarantee with respect to performance.

European Outlook

U.K. key updates

- Despite tremendous political upheaval, the British economy was remarkably steady across many different macro indicators.
- CPI inflation rose 2.1% year-on-year in April. It is now above the Bank of England's 2.0% target for the first time in 2019.
- Property Data figures showed investment volume in Q1 across all sectors was at its lowest level since Q3 2016, at £10.4bn.
- Unemployment dropped to 3.8% in the three months to March. This is its lowest level since 1974.

Our overall risk assessment for the U.K. remains at "Caution" in May/June. The overall situation merits added scrutiny. Net lending to U.K. property rose substantially in May, though ongoing concerns around the retail sector make a sustained rise in lending this year unlikely.

U.K. Politics: What's changed?

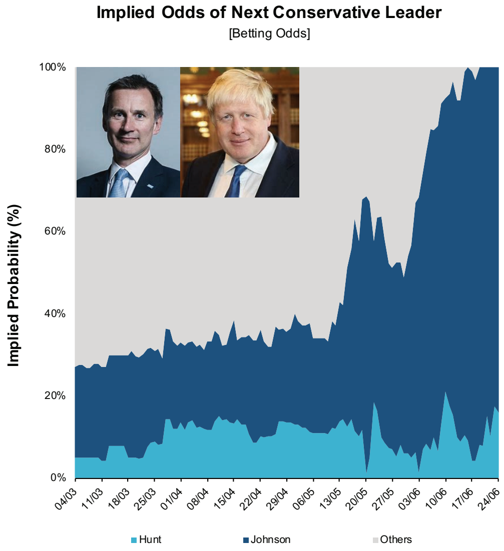
The Brexit debate continues to dominate the headlines. A series of historic confrontations between a resilient but impotent and largely unsupported Prime Minister occurred in the first six months of the year, leading ultimately to Theresa May's resignation, along with part of her cabinet. The original March 2019 deadline for Brexit was extended to April, and then again to the end of October. E.U. elections led to a rise in support for smaller parties with undiluted policies on Brexit, but there seems no fundamental shift in favour of either Leave or Remain amongst the U.K. population. Eventually Theresa May succumbed to calls for her to step down, and now the remaining time until the next deadline will be spent choosing a new leader and re-engaging with a reticent E.U. In this context, a delay beyond October seems almost inevitable, giving support to our long-held view that the extrication of the U.K. from the E.U. will be a protracted process.

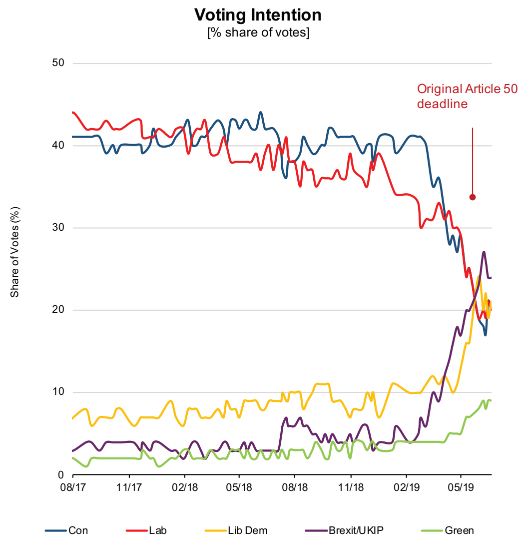
U.K. retail demise: no end in sight

The creative destruction transpiring in the retail sector continued apace in 2019 despite relatively sound retail economic conditions. Debenhams, a department store and the highest profile casualty, had an air of inevitability about it, particularly following the collapse of BHS in 2016 and House of Frasier in 2018. Debenhams, one of the largest and best-known brands on the high street, entered into a CVA (company voluntary arrangement) which affected its 165 department stores and more than 25,000 employees. Even more concerning to both investors and local councils will be the capitulation of shopping centre values, as not only will many of them be unavoidably exposed to multiple CVAs, but they may also be unfit for today's consumer. We may ultimately see shopping centre values fall by 30-40% before a bottom is reached, and survivorship bias emerge. Retail Parks have been impacted in a similar way, although for many their location and tenant type will result in a buying opportunity in due course.

Boris Johnson the Front-runner to Replace May in Race Against Hunt

SURGE IN VOTES FOR SMALLER PARTIES WITH CLEAR VIEWS ON BREXIT

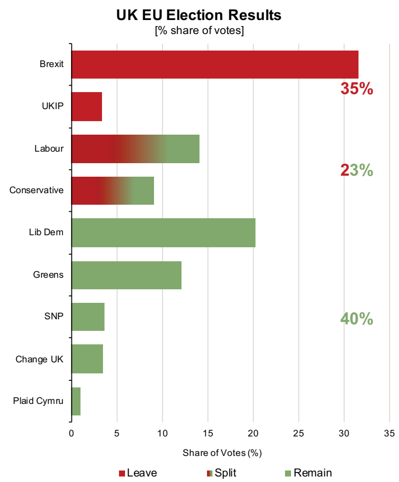


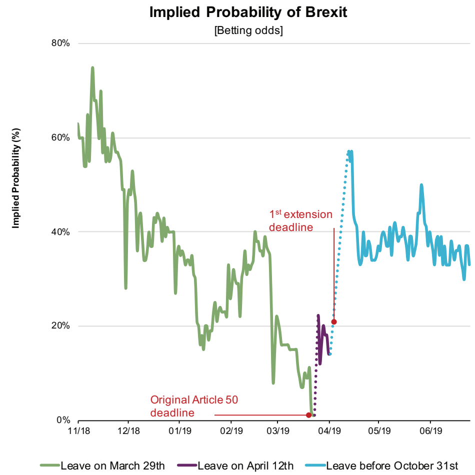


Source: LaSalle (06/19) Predictit (06/19) YouGov (06/19)

Public Opinion Still Sees Short Brexit as Unlikely but Rising

RISE OF GREEN PARTY POINTS TO GATHERING MOMENTUM OF ESG ISSUES

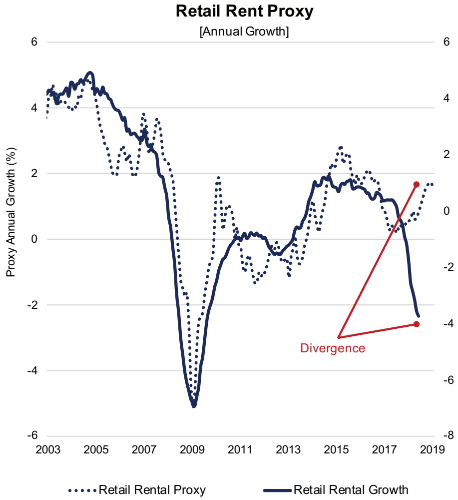


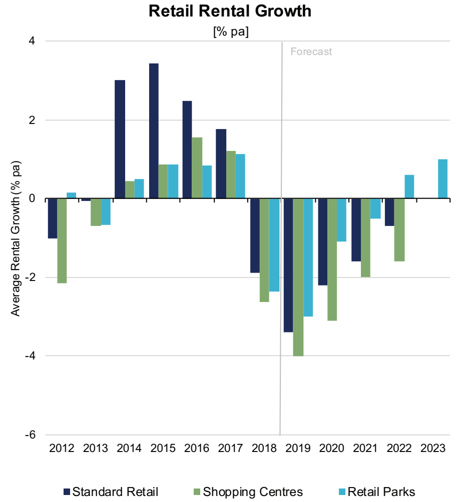


Source: LaSalle (06/19) Predictit (06/19) BBC (05/19)

Retail Rents Diverge Significantly from Macroeconomic Fundamentals

RENTS TO FALL CUMULATIVELY BY 7% TO 15% OVER MEDIUM TERM





Proxy retail rental growth = real wage growth + retail sales + house price growth + household deposit growth
Source: LaSalle (06/19) ONS (03/19) Nationwide (04/19) Building Societies Association (03/19) MSCI (04/19)

Main forecasting scenarios

Looking Ahead: Most Likely Outcome is a Long, Hard Brexit

MAPPING THE FOUR MAIN BREXIT SCENARIOS

LONG HARD BREXIT
HIGH PROBABILITY

U.K./E.U. agree loose framework of future trade agreement but details will be worked out during transition period to 2020. Further extensions may be forthcoming

Framework will be customs union / free trade agreement, excluding financial services

Long duration dilutes the Hard impact

SHORT HARD BREXIT
MODERATE PROBABILITY

Unwilling to cross red lines during negotiations, U.K./E.U. fail to agree withdrawal agreement

Transition period becomes void, so the U.K. leaves the E.U. in or before October 2019 with no deal

LONG SOFT BREXIT
LOW PROBABILITY

Scenario combines transition period (of the Long) with closer integration (of the Soft)

SHORT SOFT BREXIT
VERY LOW PROBABILITY

Brexit cancelled before October 2019

Proxy retail rental growth = real wage growth + retail sales + house price growth + household deposit growth
Source: LaSalle (06/19) ONS (03/19) Nationwide (04/19) Building Societies Association (03/19) MSCI (04/19)

Scenario for the U.K.

- We believe that LONG HARD BREXIT is most likely. The Long duration dilutes Hard impact
- Structural factors will drive Retail, Logistics & Alternatives, whilst cyclical factors characterise Offices
- Expect few forced sellers, limited repricing or additional currency advantage for foreign investors
- Investors can remain active, focussing on stock selection and secular drivers
- Cyclical opportunity to exploit strong fundamentals at attractive price

Major changes to the outlook for U.K. property as measured by MSCI incorporate further downgrades to the beleaguered retail sector, albeit with the prospect of recovery in the medium- to longer-term. City offices are still expected to benefit from their attractive yield spread as Brexit uncertainty evolves, though with the ongoing political instability, this is now viewed as likely to take place later and be less pronounced

Major changes to the outlook for prime U.K. property incorporate the outward yield shift already seen in the data by end-2018. Though prime retail suffers from higher adverse yield impact due to lower initial pricing, prime property is broadly more defensive than average over the short term, and opportunities exist in prime offices across London, the Big 6 regional centres, and the broader South East.

The short Hard Brexit scenario (U.K. crashing out of the E.U.)

- Moderate probability of SHORT HARD BREXIT, with U.K. leaving E.U. with no deal in March 2019
- More forced sellers and greater repricing of assets and currency advantage for foreign investors
- Few negative effects in the longer term
- Favours fleet-of-foot value-add investors
- Pricing opportunity for value-add investors with dry powder

Insights from the indirect funds market: Performance, flows, and queues:

- Performance of U.K. indirect holdings is mirroring the wider market with industrial, student accommodation and healthcare leading the way. Logistics funds do have some risk that isn't fully factored in though where larger tenants aren't renewing.
- Pricing: Secondary market pricing is deteriorating with no demand for retail specialist funds, so the market is stagnant in this sector (hypothetical discounts would be -25% or deeper but no investor wants to sell at that price), the alternative and industrial funds are trading at NAV and for one of the industrial funds, you could probably buy in at a small discount. Discounts for the balanced funds have moved over Q2 and are at c. NAV -5%. Demand remains very strong for long lease funds where premiums are c. NAV +4-5%.
- Pipeline: In terms of new fund offerings, this seems still to be focused on residential (PRS, social housing) and logistics portfolio deals but generally new fund offerings have slowed over Q2.

Changes made to the November 2018 Recommendation Matrix

- Moved the Affordable housing, healthcare, educational facilities (including impact investing) from Other Opportunity to Best Opportunity.
- Changed "Brexit Watch" in Value Add / Opportunistic to "Distressed Retail with high site value", as we believe any Brexit-related distress will likely be short-lived, and the retail distress is here to stay and will attractive risk-adjusted opportunities.

Key Continental European mid-year updates

- The results of the European elections confirm that pro-European parties will continue to have a clear majority in the European Parliament.
- German 10-year Bund yields have seen increasing demand in response to renewed trade tensions between the U.S. and China
- Office vacancy across the major European cities fell further in Q1 2019.
- European investment volumes are likely to have peaked in 2018.
- LaSalle's May 2019 forecasts for 2019-23: lower for longer yield environment supportive to real estate returns.

The overall risk assessment for Germany's capital markets is stable and positive in May, suggesting a low likelihood of an imminent downturn. The ZEW index of economic confidence is improving but has yet to re-emerge above zero, at -2.1. Ongoing concerns around the stability of large German banks may weigh on lending activity.

The overall risk assessment for French capital markets remains in the "Caution" category in May – the balance of risks merits added scrutiny. After a downward slide of over a year, the INSEE index of economic confidence is now trending better, and a further improvement next month could see this signal upgraded to Positive. French REITs ceased converging with the CAC40 in dividend yield terms, retaining a historically-large pricing disconnect, and Caution remains our assessment.

U.K.: 2019-2020 Investment Recommendations

<table>
<tr><th rowspan="2"></th><th colspan="2">Core</th><th rowspan="2">Value-Add</th><th rowspan="2">Opportunistic</th></tr>
<tr><th>Defensive</th><th>Income</th></tr>
<tr><td rowspan="5">Best Opportunities</td><td rowspan="2">UK Residential*</td><td colspan="2">Mezzanine debt & whole loans</td><td rowspan="2">Urban Regeneration
incl. development or planning risk</td></tr>
<tr><td>Retail parks in urban locations</td><td>London & key regional city offices refurb/build-to-core</td></tr>
<tr><td rowspan="2">Inflation-linked with high site value
incl. ground leases & income strips</td><td rowspan="2">Income-producing assets with high site value</td><td colspan="2">Special situations
incl. pref equity, development finance, recaps</td></tr>
<tr><td colspan="2">Distressed Retail with high site value</td></tr>
<tr><td colspan="3">Affordable housing, healthcare, educational facilities
incl. for Social Impact</td><td></td></tr>
<tr><td>Other Opportunities</td><td>Long hold irreplaceable assets</td><td></td><td colspan="2">Urban logistics/multi-let industrial developments</td></tr>
</table>

* Predominantly but not exclusively BTR (Build to Rent)
Source: LaSalle (05/19)

The Outlook for the German Economy Isn't All That Bad

GDP GROWTH OUTLOOK SUPPORTED BY DOMESTIC DEMAND AND STRONG WAGE GROWTH

On the downside

- Germany faced **near recession in H2 2018**
- Continued **uncertainties** posed by U.S. car tariffs, Brexit and the ongoing U.S.-China trade tensions
- **Subdued** external demand for German goods; March 2019 manufacturing orders were down by 6%, orders from non-eurozone countries by 8%

On the upside

- GDP grew by 0.4% q/q, with **buoyant domestic demand** the standout feature
- Unemployment rate at an all-time low of 4.9%, supporting strong **wage growth**
- Recovery of German car sector evident in February **industrial production** (+0.7% growth m/m)
- New car registrations rebounded in Q1 (+15% q/q) reflecting strong Q1 **private consumption**

1. H2 2018 economic standstill mainly caused by temporary factors
2. External headwinds will continue to drag on the economy in 2019, but are not expected to be carried into subsequent years
3. GDP growth outlook remains modest at 1.0% (y/y) for 2019 but 2020 expected to edge back to 1.5% (y/y)

Continental Europe Real Estate outlook: Slower economic growth but lower yields ahead of us – real estate remains attractive asset class

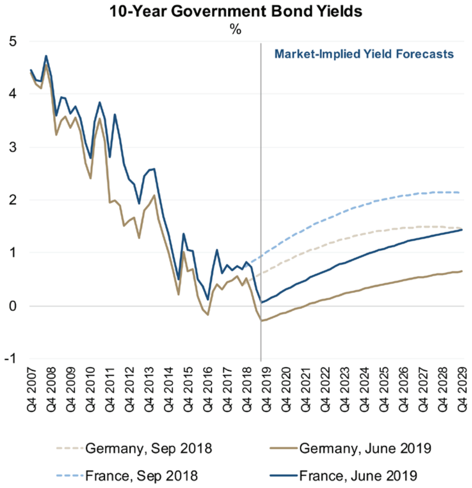
Macroeconomic highlights

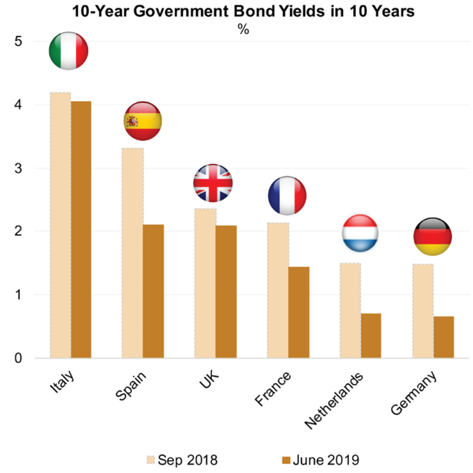
- Lower growth in 2019 and H1 2020 and small recovery after that.
- ECB likely to ease in H2 2019 and try and stimulate bank lending.
- Base case assumes Hard Brexit, but over many years and in an orderly manner and some escalation of U.S.-China trade war until appeasement.
- Robust employment growth filtering through to strong office demand.
- Robust wage growth will provide support to household spending (logistics and selectively retail).

Source: Oxford Economics (05/19) LaSalle (06/19)

Even Lower for Longer Yield Environment

MARKET-IMPLIED 10-YEAR GOVT BOND YIELDS HAVE COME DOWN, ESPECIALLY OVER THE SHORTER TERM

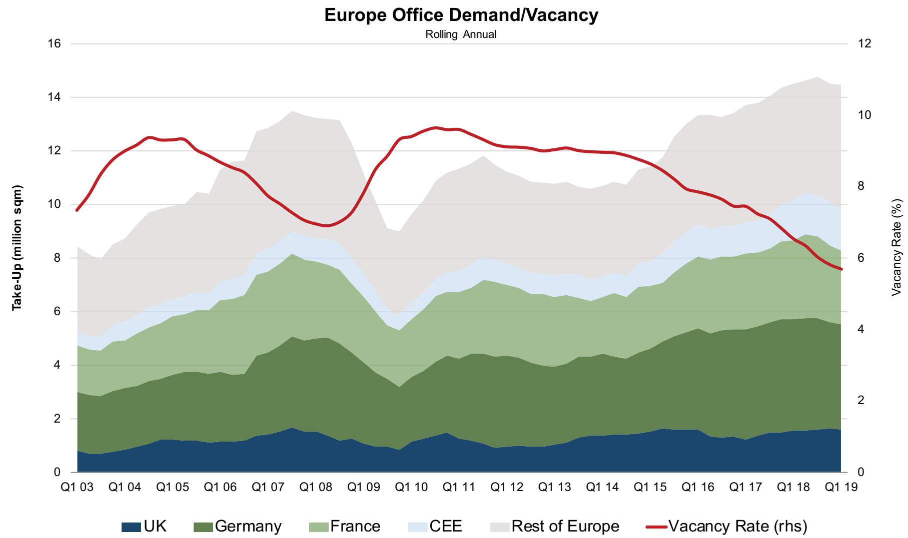




Source: Thomson Reuters Datastream (06/19)

Robust Employment Growth Filtering Through to Strong Office Demand

VACANCY HAS FALLEN BELOW 6.0%, THE LOWEST LEVEL SINCE 2002



Source: LaSalle (05/19), JLL (Q1 19)

Real estate highlights

- Limited speculative development provides downside protection to rental growth.
- ECB rate increase no longer expected for 2019: sovereign yields will remain extremely low for much longer and keep real estate yields very low too.
- Well-functioning real estate capital markets with still significant domestic and international capital.
- Continental European real estate remains an attractive investment proposition despite high investor competition.
- Urban logistics, offices, and residential/ lodging are expected to outperform.

Insights from the indirect funds market: Performance, flows, and queues:

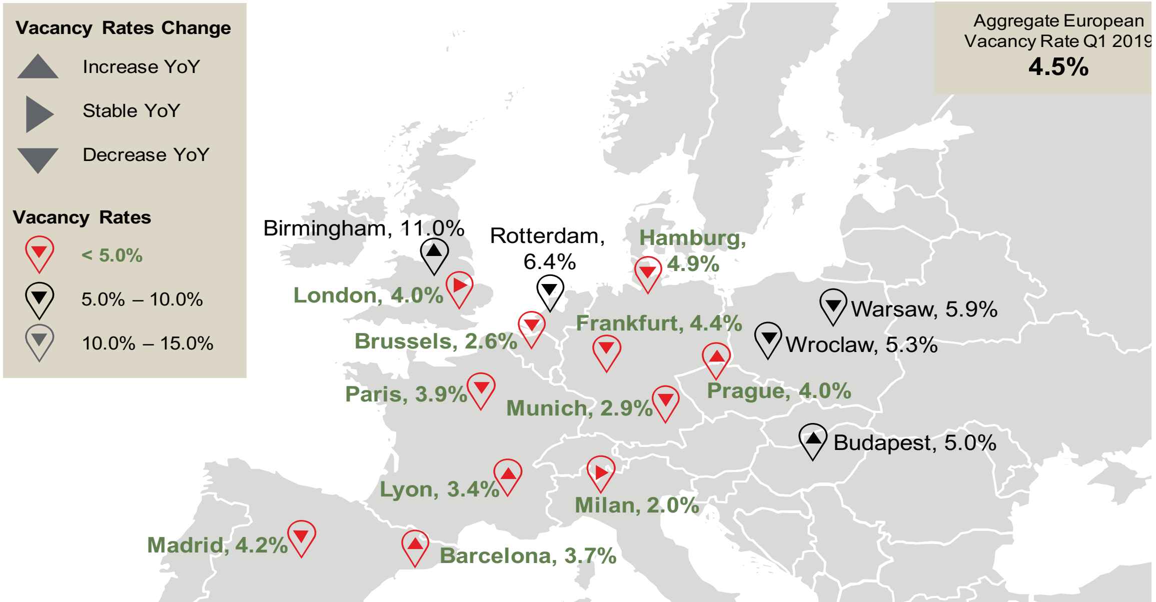
- We are now seeing some slowing in retail performance. NOI and rental growth remains very strong for offices in gateway cities and industrials across the board. The European funds still have subscription queues.
- Pricing: The larger open-ended funds are still trading at premiums, albeit lower now of c.1-2%. Pan European funds with U.K. exposure now out of favour where they have exposure to U.K. retail.
- Pipeline: We are still seeing new fund offerings in the value-add space and debt funds, and residential and logistics funds are still popular but with some planning and development risk.

Changes to our Continental Europe Prime Forecasts since the ISA

- Major changes to the Continental European forecasts incorporate a lower-for-longer yield outlook for prime offices, and enhanced rental growth prospects for scarce prime urban logistics assets. Retail is expected to fare worse with the exception of the best high street pitches in top cities.

Extremely Tight Supply in core Logistics Markets

RENTAL GROWTH INCREASING AND BECOMING MORE WIDESPREAD, ESPECIALLY FOR URBAN LOGISTICS



Source: LaSalle (05/19) JLL (Q1 19)

Continental Europe: 2019-2020 Investment Recommendations

MID-YEAR 2019

Changes made to the November 2018 Recommendation Matrix

- Moved the Senior Loans strategy from Other Opportunities to Best Opportunities.
- Moved the Urban Retail to Other Opportunities because of current pricing not reflecting structural risks and hence lack of rental growth (or even rental erosion in the future).
- Also added “prime” in front of urban and added high street: today, we really prefer the best high streets and urban locations, and would not recommend straying away from these at the moment.

	Core		Value-Add	Opportunistic
	Defensive	Income/Core+		
Best Opportunities	Well Connected Offices in DTU+E rich* locations	Short Leased / light refurbishment offices *Well connected locations in Germany, France, Netherlands and Spain*	Significant office refurbishments *Well connected locations in Spain, France, Netherlands and Germany*	Office: Urban regeneration via build-to-core *Incl Grand Paris and German top 6*
	Senior Loans *France, Germany Iberia, BeNeLux*	Flexible living concepts *Micro apartments, aparthotels, student housing*		Assets with high change of use optionality *Incl. planning risk*
		Mezzanine debt & whole loans		
	Urban logistics *incl. sites with potential future e-commerce use*	Modern logistics (incl. development) *Urban locations or dominant hubs*		
Other Opportunities	Prime urban or high street retail in DTU and/or tourist cities	Master leased hotels *Combined tourist and business destinations*	Special situations *Incl. pref equity, development finance, recaps*	

DTU+E = Demographics; Technology; Urbanisation + Environmental Change
Source: LaSalle (05/19)

Asia Pacific Outlook

Uncertainty over the U.S.-China trade war is running high. In the meantime, stock market volatility in Asia Pacific has increased, although it remains substantially lower than the level during the Global Financial Crisis (GFC). This phenomenon could be explained by the assumption that equity markets are complacent, or equity investors have fully priced in these geopolitical and economic uncertainties as the new norm going forward.

Looking ahead, we expect capital market volatility to increase, driven primarily by these factors:

- Potential headline news from the trade tension between the U.S. and China could swing sentiments from positive to negative or vice versa on an ongoing basis;
- Central banks in the region are likely to face a more challenging environment in managing their interest rate and currency regimes against the U.S. movements;
- The late cycle investment behaviour that tends to tilt towards risk-off with occasional revival of risk-on as investors seek evidence to justify the fear of missing out on attractive opportunities.

Our outlook over the next 12 to 18 months does not include a global or regional financial crisis or a recession, but takes into consideration the possibility of an economic slowdown, and a material impact of the trade war on export growth in the region. Under an environment of slow growth, low inflation, low interest rates, and rising volatility, investors will need to focus on protecting the durability of cash flows for core strategies, and seek real estate sub-sectors or micro-locations that could outgrow the broad economy for higher return strategies. The possibility of steeply discounted or financially distressed portfolios coming to the market is still very low, as liquidity is ample in Asia Pacific.

Trade Tariffs Have Not Yet Materially Impacted Real Estate

Looking back over the last six months, a few areas have changed or surprised us:

- How quickly trade rhetoric between the U.S. and China has escalated – a drastic turn from the optimistic outlook of a potential trade deal in March to the collapse of trade talks in May. As shown in the chart Export Growth Consensus Forecast vs. Actual, the impact of trade tariffs that the U.S. imposed on the first $50 billion of Chinese exports during the summer of 2018 was worse than what most economists projected. The impact took about six months to filter through the Chinese economy and other major Asia Pacific economies that also rely highly on China for economic growth.
- In order to offset some negative impact from trade, most central banks in Asia Pacific shifted from a neutral stance to an easing bias on monetary policies over the past six months. In particular, the Reserve Bank of Australia (RBA) cut the cash rate by 25bps in early June for the first time in 34 months.
- Nonetheless, the impact on real estate demand has been limited, even in markets with high tenant exposure to export-oriented industries; for example, Osaka office. Where we have seen weaknesses are in those markets that have not only high export exposure, but also high levels of new supply or vacancy rates; for example, the Perth office market and a few remote decentralized office submarkets in Shanghai.
- One area where the news was more positive than expected was the lower-than-anticipated new supply delivered over the last six months in a majority of Asia Pacific markets/sectors. Despite some pockets of demand weaknesses due to trade, the lower-than-projected new supply has kept occupier fundamentals healthy in the region.

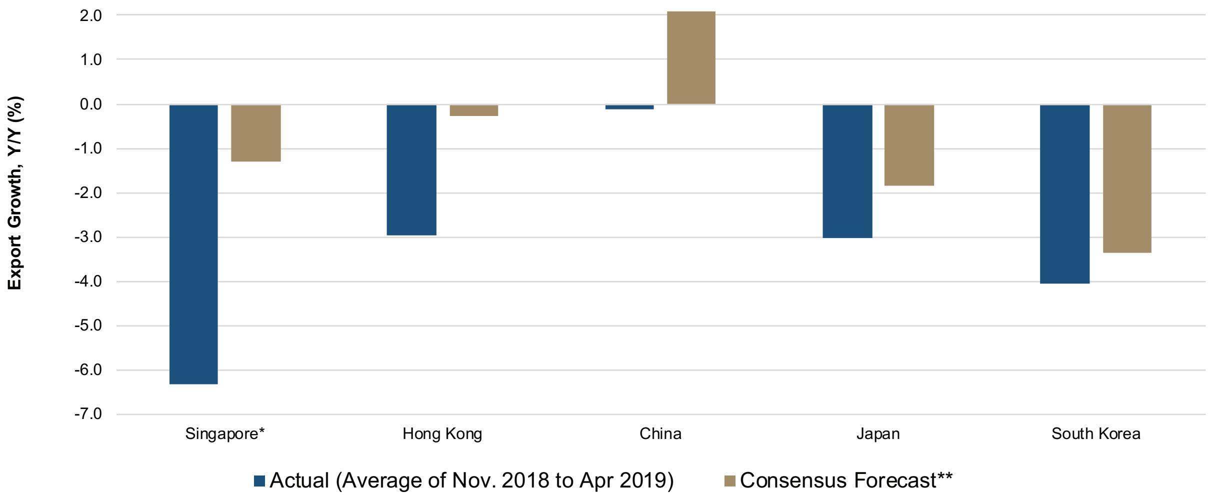
The areas that have played out generally as we expected include:

- Most countries in the region maintain an accommodative bias in monetary or fiscal policies to offset the negative impact of trade on their economic growth.
- Most Asia Pacific real estate occupier market fundamentals remain healthy. Vacancy rates in about 74% of Asia Pacific markets/sectors[10] that we track are currently below 10%, while vacancy rates in 60% of Asia Pacific markets/sectors[11] that we track are below 5%. As a result, rental growth in 68% of Asia Pacific markets/sectors[12] either continued to accelerate or remained steady over the past six months.
- As anticipated, divergence in the office sector performance was the most apparent. For example, net effective rent growth in Tokyo 5-ku, Osaka 2-kus, Singapore CBD, and Hong Kong accelerated over the past six months, making them the strongest office markets in the region. However, we do not expect the trend to persist. In the meantime, Sydney and Melbourne CBD office markets edged down from the top spots, as tenant incentives plateaued over the past six months. At the other end of the spectrum, Perth and Seoul office markets remained weak.
- The regional capital markets are generally strong and liquidity remains abundant. Strong investor demand continues to keep cap rates at historical low levels in major office markets in the region, while cap rates edged down slightly in most China logistics markets.

Worse-than-anticipated Impact from Trade War

EXPORT GROWTH CONSENSUS FORECAST VS. ACTUAL

Reflecting direct and indirect impact on major AP countries when the U.S. imposed 25% tariff on the first $50bn Chinese exports

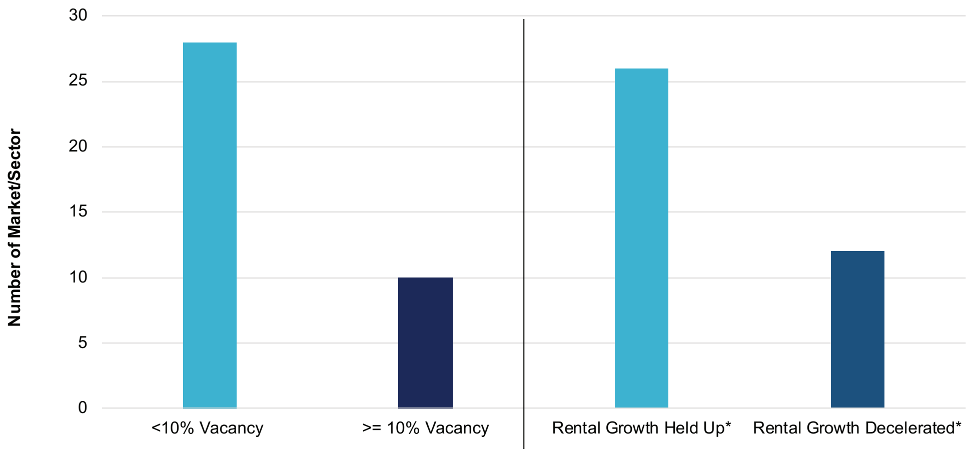


Note:
* Singapore export growth, Y/Y is based on the Non-oil Domestic Exports (NODX).
** Bloomberg Consensus Forecast was an average of all forecasts ranging from a month to a day before the release of the actual data.
Source; Bloomberg, as of 6th June 2019

10 A total of 38 markets/sectors are included in the above analysis. Data for Japan rental apartment and shopping centres in Tokyo is sourced from ARES, as of Q1 2019. Data for Japan logistics is sourced from CBRE, as of Q1 2019. Other data in this analysis is sourced from Jones Lang LaSalle, REIS, and LaSalle Investment Management, as of Q1 2019.
11 Same as footnote 10
12 Same as footnote 10

Most Asia Pacific Markets/Sectors Remain Healthy

VACANCY AND RENTAL GROWTH IN ASIA PACIFIC MARKETS/SECTORS



A total of 38 markets/sectors are included in the above analysis. The market coverage as below:
Office – Sydney CBD, North Sydney, Parramatta, Melbourne CBD, Brisbane CBD & Fringe, Perth CBD, Beijing CBD, Shanghai CBD & Fringe, Hong Kong Central, Hong Kong Kowloon East, Tokyo 5-Ku Grade A and Grade B, Osaka, Singapore CBD, Seoul CBD, Yeouido and Gangnam;
Retail – regional malls in Brisbane, Sydney, Perth and Melbourne, Prime retail in Beijing, Shanghai, and Hong Kong; Shopping centers in Toyo, suburban malls and Orchard road malls in Singapore;
Logistics – Beijing, Hong Kong, Shanghai, Tokyo, Osaka and Singapore
Rental Apartment -- Tokyo Nagoya and Osaka
*A markets/sector is categorized as "rental growth held up" if rental growth in Q4 2018 & Q1 2019 is higher or equal to the same period a year ago. A markets/sector is categorized as "rental growth decelerated" if rental growth in Q4 2018 & Q1 2019 is lower than a year ago.
Source: Data for Japan rental apartment and shopping centres in Tokyo are sourced from ARES as of Q1 2019. Data for Japan logistics is sourced from CBRE, as of Q1 2019, The rest of the data is sourced from Jones Lang LaSalle REIS, LaSalle Investment Management, as of Q1 2019.

Asia Pacific Macro-economic Outlook – Risks and Opportunities

Trade rhetoric is evolving by the day. The outcome of the trade war remains a moving target. Although the U.S. has raised tariffs to 25% on a total of $250 billion of Chinese goods[13] , a possible positive outcome could be a tariff reduction on the list of goods if trade talks take a turn for the better. The opposite, however, is also a possibility. The tensions between the U.S. and China are beyond economic considerations. Even if both parties agree upon the principle of moving forward in the G-20 Summit, it will most likely take longer than anticipated to close the differences between the two economic giants.

As discussed earlier, the impact of trade tariffs that the U.S. imposed on the first $50 billion of Chinese exports was worse than most economists projected. By the same measure, the 25% tariff on the next $200 billion of Chinese exports to the U.S. (which was announced and implemented recently) could have a more severe impact on most Asia Pacific economies. The impact is unlikely to filter through the economy until late 2019 to early 2020.

Since China remains the key economic growth driver of Asia Pacific countries, the trade war between the U.S. and China is expected to directly and indirectly impact all economies in the region. Our base case assumes that the 25% tariffs on a total of $250 billion Chinese exports remain in place during the next two to three years. We estimate that the gross impact on GDP growth cumulatively over the next two to three years could range from 100 to 500 basis points among the six major countries in the region. Most Asia Pacific economies are expected to implement further fiscal stimuli and easing monetary policies (e.g., rate cuts) to offset the negative impact from trade. The good news is that most Asia Pacific countries have more ammunition than the U.S.

In addition, most countries would speed up the process of diversifying trade partners by adjusting supply chains, which usually takes up to three years. Most importantly, weak Asian currencies against the USD would benefit exports. We estimate all of these factors would provide positive offsets and will substantially reduce the net impact on GDP growth. There are also other regulatory or geopolitical approaches to support growth in several Asian countries, which are difficult to quantify but with potentially profound impact. In particular, China has the most room among major Asia Pacific countries to implement some of these approaches.

Taking all of the above into consideration, the U.S.-China trade war is expected to have the most severe short-term impact on South Korea and Australia, as these two economies are the most vulnerable due to the impact on trade and domestic

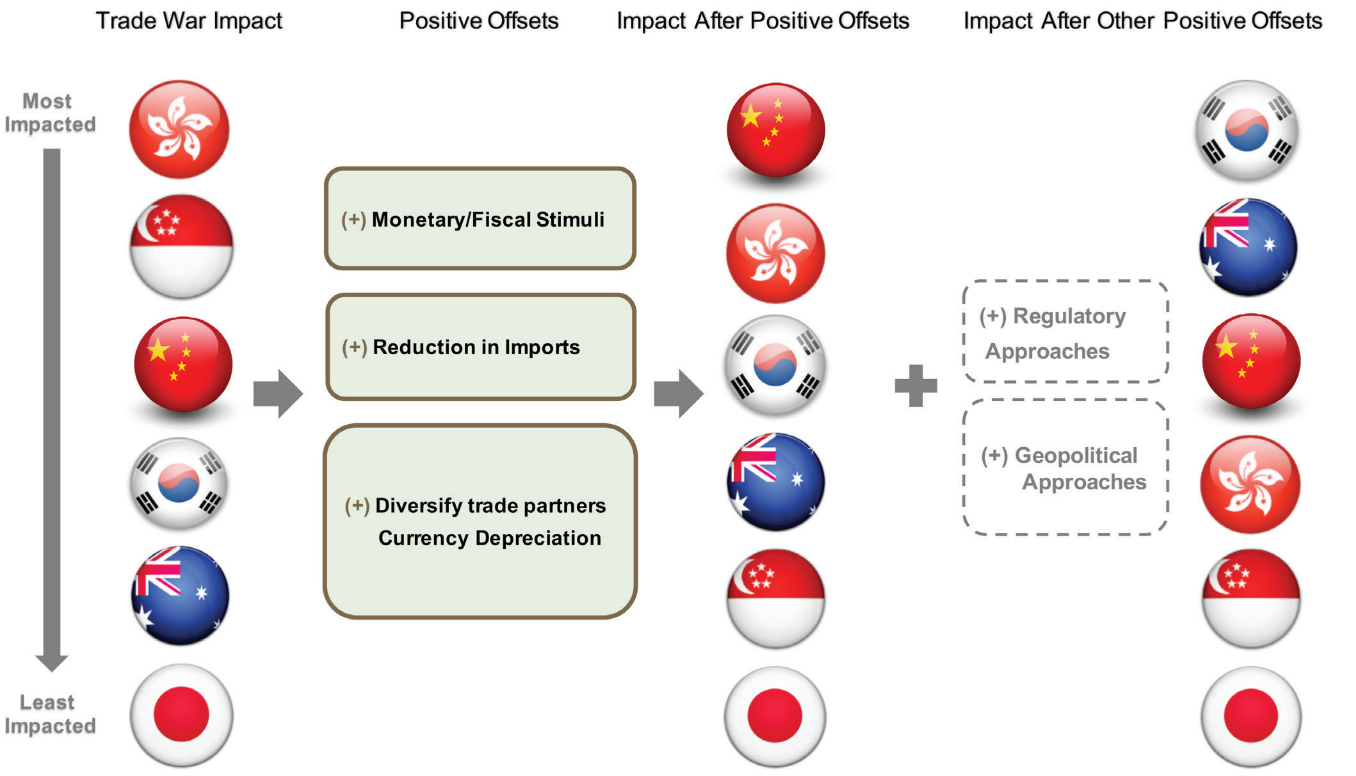
13 as of June 18, 2019

weaknesses. China is expected to experience some short-term weaknesses, but remain positive on the medium- and long-term, as the country has adequate ammunition. Hong Kong and Singapore, being open economies. are susceptible to capital market volatility. However, China is likely to be the backstop for Hong Kong. Singapore, backed by its flexibility in adapting changes in the global supply chain, is likely to experience a sharp decline but also a fast recovery. Our analysis shows that Japan is likely to be more resilient than the other major Asia Pacific countries, despite the slow growth on a relative basis. This is one of the key reasons why we continue to favor Japan. Nonetheless, an all-out trade war between the U.S. and China is not in our current base case. If a full-blown trade war occurs, it is a lose-lose situation for both China and the U.S.

Despite the trade concerns, labor markets in major Asia Pacific countries are healthy. In particular, unemployment rates in China, Hong Kong, and Japan are currently at historical lows. Australian and South Korean labor markets are weaker in the regional context, primarily reflecting domestic weaknesses. However, 4%-5% unemployment rates in Australian and South Korea are considered healthy among developed economies globally. In all, 2%-5% unemployment rates in major Asia Pacific countries provide some cushion to near-term volatile and some weaknesses in the macro environment.

Currency Depreciation & Stimuli May Partly Offset the Drag on Exports

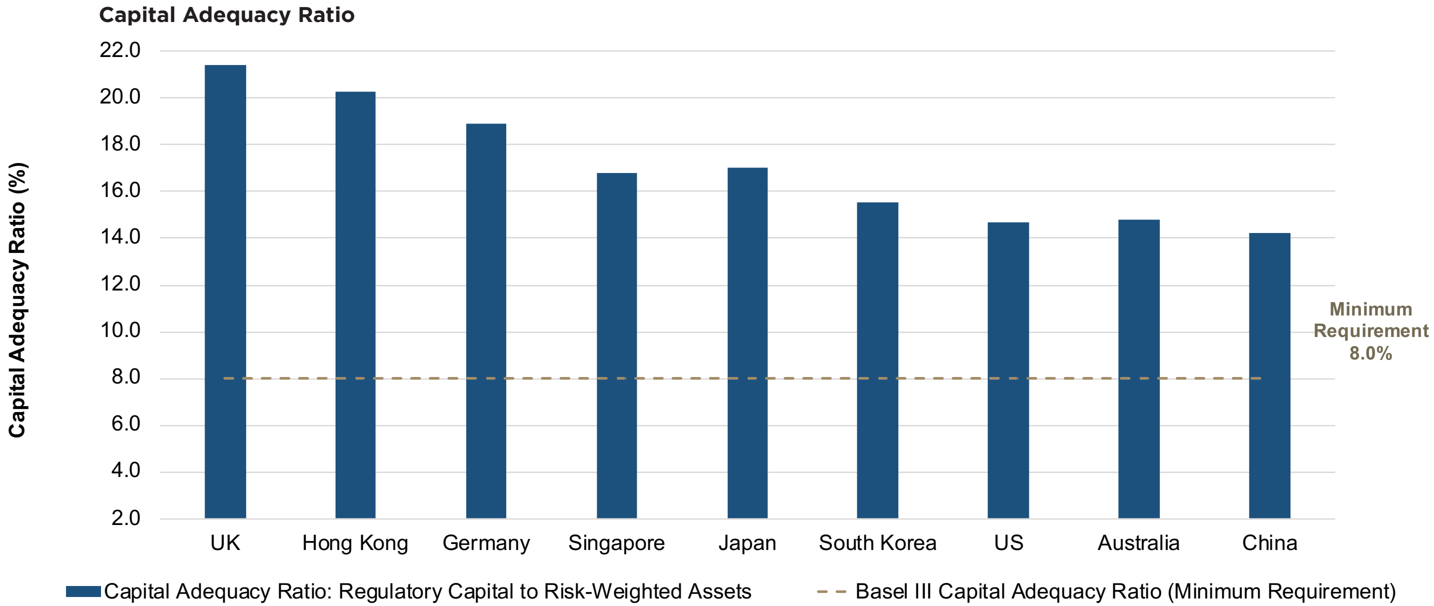
ESTIMATED CUMULATIVE IMPACT OF TARIFFS* ON GDP 2019-2022



*Note: The above analysis is based on the direct and indirect impact of the U.S. imposing 25% tariffs on a total of $250billion of Chinese goods, Australia, Hong Kong, Japan, Singapore, and S. Korea's 2018 GDP. Additionally, in Japan, we also assume a 30% reduction on automobile exports to the U.S.
Source: LaSalle Investment Management as June 2019

Financial system is healthy

BANKS GLOBALLY HOLD CAPITAL IN EXCESS OF THE REGULATORY REQUIREMENT



Note: Regulatory capital to risk-weighted assets is the amount of capital a bank or financial institution is required to hold by the financial regulator, which is usually expressed as the capital adequacy ratio of equity that a bank is required to hold as a percentage of its risk-weighted assets.
Source: Data for Australia (as of Q4 2018), China (as of Q4 2018), Germany (as of Q4 2018), Japan (as of Q3 2018), Singapore (as of Q4 2018), and U.S. (as of Q3 2018) is sourced from International Monetary Fund; data for Hong Kong (as of Q4 2018), and South Korea (as of Q4 2018) is sourced CEIC; data for the U.K. (as of Q4 2018) is sourced from the Bank of England, as of Q4 2018

Capital adequacy ratios of Asia Pacific banks continue to exceed the Basel III requirement. The health of the banking system partly explains why current debt covenants in the real estate sector have been favorable. Despite several Reserve Requirement Ratio (RRR) increases last and this year, Chinese banks on average are still holding capital in excess of the Basel III requirement. However, the balance sheets of some small regional banks in China could be problematic. The People's Bank of China (PBOC) has been injecting liquidity in targeted areas without causing more debt problems. The bottom line is that the financial system in China is unlikely to break down. One-off real estate equity or debt opportunities could emerge in China, if some small regional banks encounter liquidity challenges. However, the window of opportunity is likely to be short-lived, even if it occurs.

In addition to banks, governments and households in most Asia Pacific countries are not highly levered, with the exception of Australia's household debt and Japan's government debt. We are less concerned about Japan's government debt, as the savings rates among households and corporations are still high. In Australia, we are most concerned about the high household debt level, as this is concentrated in residential mortgages. Equity or debt opportunities in the Australian residential sector could emerge if global capital market volatility increases further.

Market expectations have recently shifted towards an easing bias for the U.S. Fed. Central banks in Hong Kong and Singapore generally follow the U.S. Fed. The Bank of Japan governor Kuroda recently commented that the Bank could deliver additional monetary stimulus if necessary. As a result, we expect interest rates to remain low in Japan for the next two to three years. Due to the external and domestic challenges in Australia, the Reserve Bank of Australia (RBA) is expected to cut interest rates further. In China, the PBOC could cut RRRs, seven-day repo rates or benchmark rates. All of these indicate an easing monetary policy environment going forward, which is supportive of real estate capital values. However, abundant liquidity also presents a tough environment to place capital, barring any exogenous shocks.

Real Estate Opportunities under a Slow Growth Environment with Rising Volatility

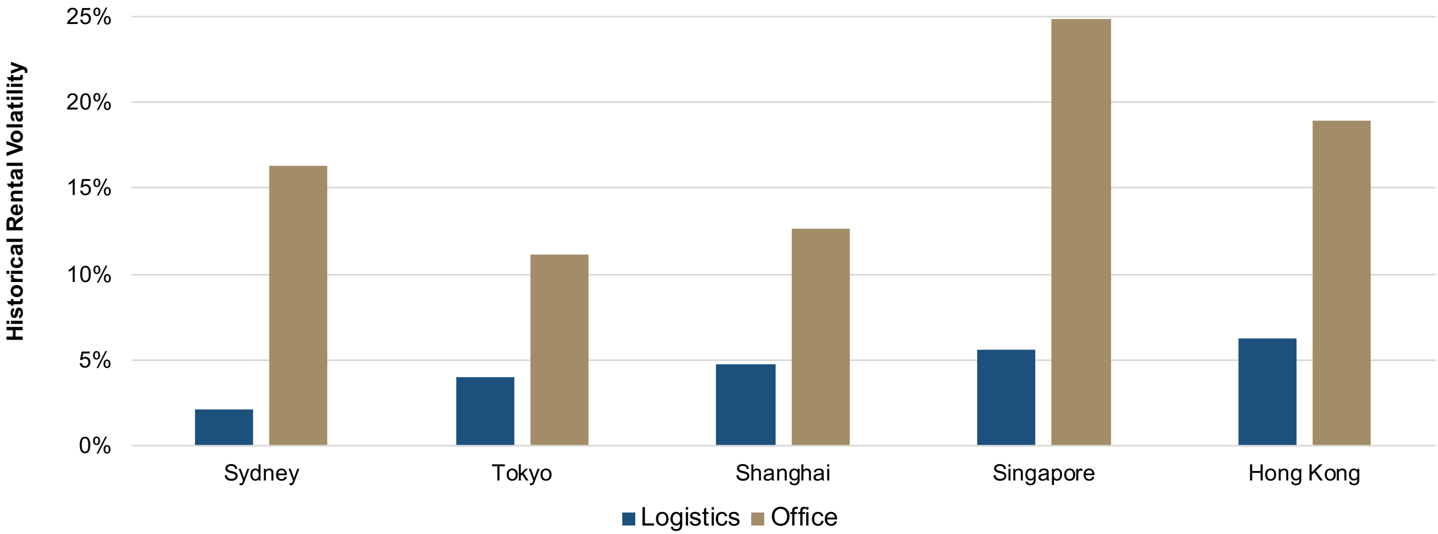
Looking ahead, the region is expected to experience slower growth and more volatility than anticipated six months ago. We are not projecting a severe recession in the base case. However, even if a recession comes, we expect capital value declines in major Asia Pacific markets to be less severe than those during the GFC, as the real estate sector is generally less leveraged than the GFC period, and capital remains abundant. Under our base case assumption, most real estate investors will continue to invest, but at a slower pace with discipline. Broad-based distressed opportunities are unlikely, barring any exogenous shocks.

Many of the country-specific strategies that we recommended in the 2019 ISA still hold up. For core strategies, investors will need to focus on protecting the durability of cash flows. For higher-return strategies, seek out areas that could outgrow the broad economy. For example, we continue to favor Japan, and the regional logistics sector. We are in favor of exposures to growth sectors such as pharmaceutical and bio-tech as demand drivers, while we are cautious of exposures to export-oriented industries. Additionally, we recommend emphasizing the importance of location/sub-sector/asset strength and stringent underwriting criteria for new acquisitions. For existing assets in higher-return portfolios, maintain flexibility on holding periods, and look for early lease renewals where possible. Consider speeding up the disposition process as soon as asset-level business plans are fully executed. Be aware that some of these alpha strategies could take longer to execute. The focus is shifting from maximizing returns to narrowing the dispersion of return outcomes. However, as volatility increases in the capital market, preserve some capital when possible. Be ready to take advantage of potential pockets of dislocations in the region; for example, in the Australian residential sector or Chinese developers with weak balance sheets.

Office: Office market performance is expected to continue to diverge in the region. We recommend being highly selective on submarket, location and asset quality. We continue to favor Grade B over Grade A offices in DTU-rich locations of Tokyo for value-add strategies, due to the relatively muted supply outlook and low exposure to export-oriented industries. We remain convinced of Shanghai Fringe CBD, as the submarket has low exposure to the export-oriented tenant, with a lower pipeline than decentralized business districts and more affordable rents than offices in Shanghai Core CBDs. In Australia, our analysis shows that Melbourne CBD Office rental growth is less correlated with economic growth than Brisbane. We therefore favor Melbourne CBD offices for core strategies in a slow growth environment. Sydney offices have experienced significant value run-ups when compared to those of Tokyo, Singapore and Shanghai offices. The potential downside risk in Sydney office capital values could be higher than that of other major office markets in the region.

AP Logistics Rents Less Volatile than Office

CONTINUE TO FAVOR AP LOGISTICS



Note:
Historical rental volatility is measured by the standard deviation of the annual rental growth of the respective markets from Q4 2007 to Q1 2019. The analysis is based on net effective rents (excluding all property expenses, taxes and incentives) with the exception of Sydney and Melbourne, where rents exclude all property expenses, taxes but not incentives.
Logistics sector: Shanghai non-bonded warehouse, Hong Kong warehouse, Singapore logistics, Sydney Outer Central West precinct logistics , Seoul logistics and Tokyo logistics.
Office sector: Shanghai CBD, Hong Kong Central, Singapore CBD, Tokyo Central 3 wards, Sydney CBD, and Seoul CBD.
Source: Jones Lang LaSalle REIS, CBRE, LaSalle Investment Management, as of Q1 2019
Past performances is not a guarantee of future results. No assurances are given that these trends will continue or materialize as expected. Nothing herein constitutes a guarantee or prediction of future events or results.

Logistics: We continue to favor the logistics sector in the region. This conviction is not only because of the fact that logistics demand is supported by domestic consumption and the growth of e-commerce, but also logistics rents are generally less volatile than those of offices. We view low rental volatility to be favourable in an environment of rising volatility. Furthermore, stabilized market yields for logistics are about 100-200 basis points higher than those of office properties. Development yields on cost offer another 100-200 basis points above those stabilized market yields in the region, with China and South Korea at the higher end of the range. We therefore continue to favor logistics developments in China and South Korea.

Retail: While the rise of e-commerce presents opportunity to the logistics sector, it presents threat to the retail sector. We are cautious of the overall retail sector. However, not all retail markets are created equal. As shown in the chart Asia Pacific Logistics/Retail: opportunity vs. threat, Japan and Singapore retail sectors are expected to be less adversely affected by e-commerce, while China and South Korea retail sectors are faced with more challenges. This reinforces our conviction of selective non-discretionary retail in strong catchment areas in Singapore and Japan. However, due to negative investor sentiment towards the overall retail sector, liquidity of the sector has been reduced over the past 12-18 months. Tenant mix, location selection, and entry pricing are increasingly important when considering retail investments.

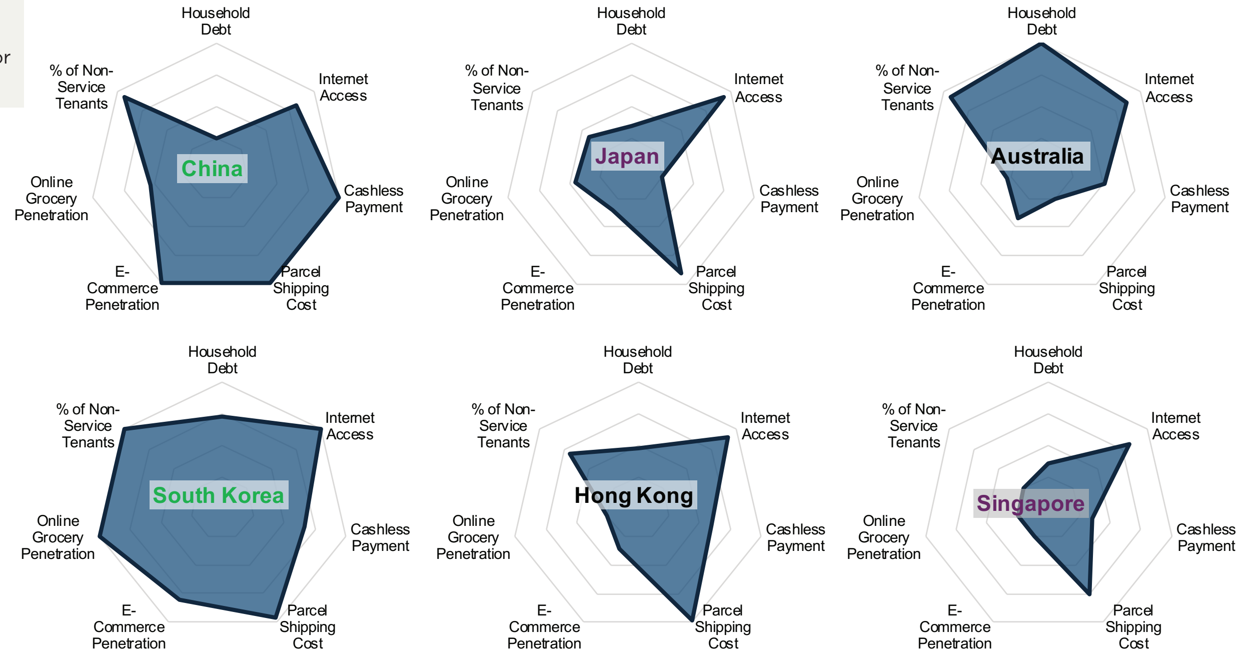
Residential: For-sale residential prices have had strong run-ups from their respective troughs, particularly in markets such as Hong Kong, Sydney and Shanghai. As expected, residential prices have been gradually trading down in these markets over the past 9-18 months. However, we do not expect a sharp correction in Hong Kong and China in the near term, as household balance sheets remain strong. On the contrary, the residential sector is expected to gradually bottom out over the next 12-18 months. However, we do not expect residential prices in Australia to rebound sharply post-bottoming, due to high household debt levels, tepid wage growth, withdrawals

E-Commerce Threat / Opportunity

(the larger the shaded area is, the more adverse impact on bricks-and-mortar retail, but the better the opportunity for logistics)

AP Logistics/Retail: Opportunity vs. Threat

SELECTIVE RETAIL PROPERTIES IN JAPAN AND SINGAPORE IS RESILIENT



Note: Shipping cost is based on the price of sending a package via local express shipping around the globe. The study uses 'Express Shipping' defined as within 1-2 business days or less in all cases, assuming that an e-commerce business would want to stay competitive with their customers who are used to fast, often next-day delivery. For the purpose of this study, a standard package is defined as 46cm (L), x 31.5cm (W) x 9.5cm (H) with a weight of 2kg. Online Grocery based on % on online FMCG sales to the total FMCG. Source: Bank of International Settlement (Household Debt, Cashless Payment), The World Bank, International Telecommunication Union, World Telecommunication/ICT Development Report (E-commerce access data is proxy by internet penetration rates), Sellics Global Shipping Price Index 2018 (Shipping Cost for all markets except for Hong Kong and Singapore), Singapore Post (Singapore Shipping Cost), Hong Kong Post (Hong Kong Shipping Cost), Urbis Shopping Centre Benchmark (Australia % of Non-Services in Malls), Japan Council of Shopping Centre (Japan % of Non-Services in Malls), JLL (South Korea % of Non-Services in Malls), CMT REIT (Singapore % of Non-Services in Malls), LIMS based on Chinese Developers (China % of Non-Services in Malls), Link REIT (Hong Kong % of Non-Services in Malls), Kantar Worldpanel (Online grocery for all markets except Australia and Singapore), AC Nielson (Online grocery for Australia and Singapore) of foreign buyers (particularly Chinese) and high expected supply (particularly in condominiums). There could be potential entry opportunities if residential and land prices adjust in Australia.

We continue to favor the Japan multifamily sector. In-migration has been and is expected to continue to drive occupier demand for urban multifamily properties in Tokyo, Osaka, Nagoya, and Fukuoka. The resiliency of Japan multifamily provides support for core and lease-up strategies.

Hotel: Another area of strength under a slow-growth environment is Asian tourists, particularly Chinese tourists. Our analysis shows that depreciation of the Chinese yuan is unlikely to deter Chinese from traveling to other major Asia Pacific tourist destinations. While the demand driver is supportive of the sector, supply is high in several markets, such as Sydney and Seoul. The key focus going forward is location selection, as well as identifying the hotel segment that has a potential mismatch of demand and supply. For example, 87% of the supply pipeline in Tokyo from 2019 to 2021 are limited service hotels that mainly target single travellers.[14] However, 84% of Asian tourists traveling to Japan are families, partners, or groups of friends. We therefore favor Tokyo hotels targeting multiple guests near tourism attractions for higher return strategies.

Asia Pacific Investment Recommendations

MID-YEAR 2019

<table>
<tr><th></th><th>CORE</th><th>VALUE-ADD</th><th>OPPORTUNISTIC</th></tr>
<tr><td rowspan="3">LaSalle's Best Opportunities</td><td colspan="3">Modern warehouses in well-located and supply-constrained submarkets</td></tr>
<tr><td>(China Tier 1 & satellites cities, Seoul)</td><td colspan="2">(China Tier 1 & satellites cities, Select China Tier 2 cities, Seoul)</td></tr>
<tr><td>Offices with secured income
(Melbourne and Sydney CBDs)</td><td>Selective office locations with flexible exit timing
(Tokyo Grade-B, Osaka Grade-A, Melbourne and Sydney CBDs, Shanghai CBD and Fringe)</td><td></td></tr>
<tr><td rowspan="5">Other Opportunities</td><td colspan="3">Modern warehouses</td></tr>
<tr><td>(Australia Eastern Seaboard, Hong Kong, highly selective in Singapore and Tokyo)</td><td>(Hong Kong, highly selective in Singapore and Tokyo)</td><td>(Tokyo)</td></tr>
<tr><td>Urban multifamily
(Japan)</td><td rowspan="2"></td><td rowspan="2">Highly selective hotel refurbishment/lease-up near tourism attractions
(Japan)</td></tr>
<tr><td>DTU-rich locations
(Tokyo Grade-B, Osaka Grade-A)</td></tr>
<tr><td colspan="2">Selective non-discretionary retail in strong catchment areas
(major cities in Japan, Singapore, Hong Kong)</td><td>Distressed residential, if repriced
(Australia)</td></tr>
</table>

Source: LaSalle Investment Management, as of June 2019

14 Source: Japan Tourism Agency (Asian inbound tourists by group in 2017, the number of tourists by country as of 2018), LaSalle Investment Management, as of 2018.

Real Estate at Mid-Year 2019: A Performance Perspective

Real estate has produced 9 years of strong, sustained performance in nearly all markets around the world. Investors are generally very pleased with how their real estate positions have performed in a portfolio context (relative to stocks, bonds, private credit, private equity, and other real assets).

The strong results have come from nearly all forms of real estate—listed securities, debt products and private equity. The look-back numbers are satisfying to review, but it is the look-forward numbers that we urge clients to focus on. LaSalle's analysis of this performance suggests the following:

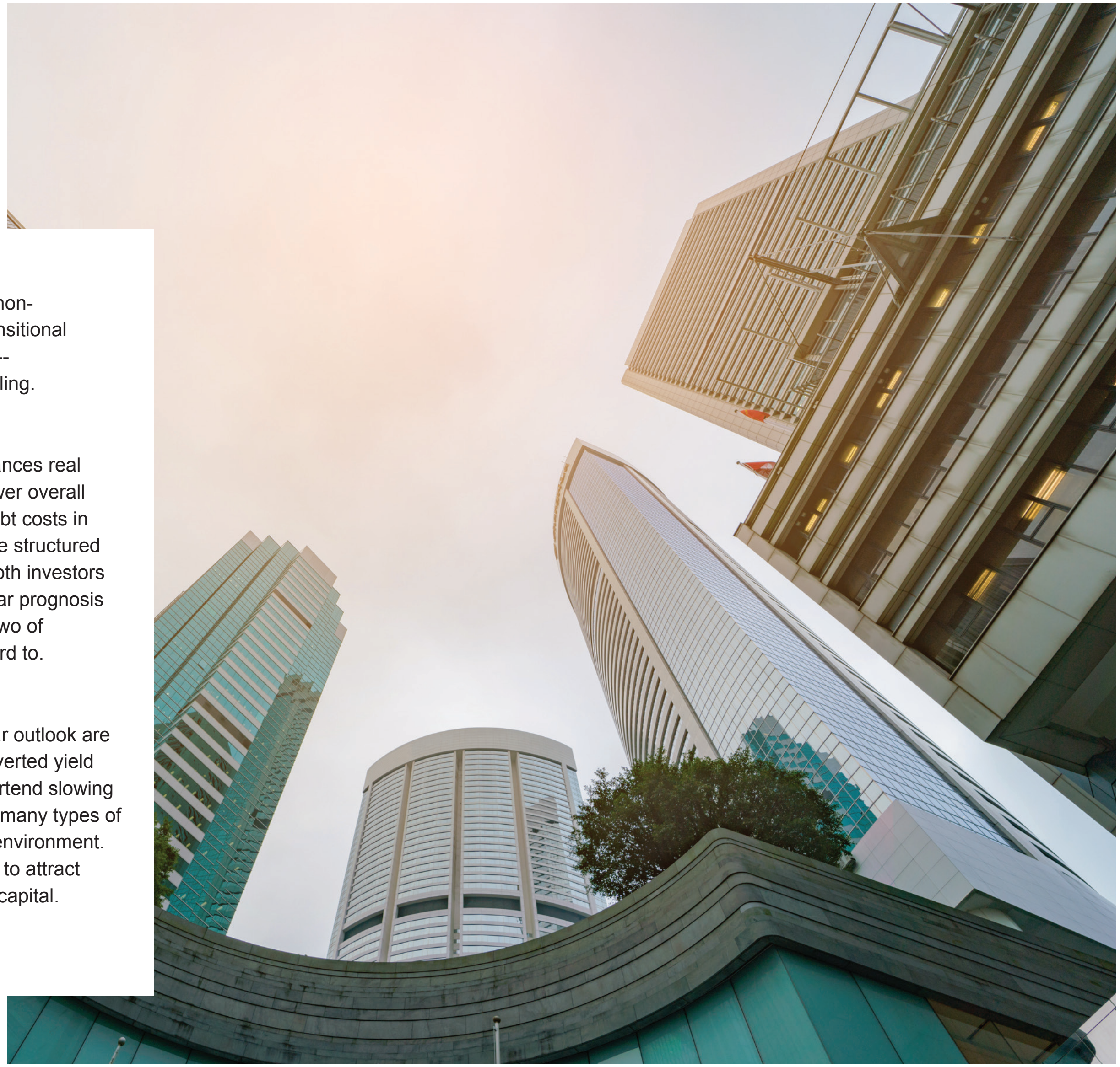
1. Core real estate performance peaked in 2012-2016. But, barring any rapid outward movement in interest rates, it is likely to produce lower, steady positive returns over the next three years.

2. Non-core real estate is proving to be more challenging. As core returns erode, more investors gravitate to non-core strategies to "solve" for the higher returns that they have come to expect from real estate in the past.

3. With more capital crowding into non-core products, the market for transitional real estate is getting fully priced -- compensation for risks is also falling.

4. In sum, the capital stack that finances real estate must allocate across a lower overall return. Fortunately, with lower debt costs in our major markets, and with more structured finance products available (for both investors and users of capital), our mid-year prognosis is that we have another year or two of positive returns still to look forward to.

5. The risks outlined in this mid-year outlook are rising. Falling bond yields, flat/inverted yield curves, and trade disputes all portend slowing global growth. At the same time, many types of real estate thrive in a rising risk environment. And the asset class will continue to attract a steady flow of equity and debt capital.



Performance Summary

The performance of private equity real estate can be tracked now in about 26 countries. In about half of these countries, the time series can be tracked for over ten years. As shown in the table on the right, the results are uniformly strong over the last 5 and 10 years. Historic returns range from 4.4% (or 4.0% real) in Japan, to 9.3% in Australia (7.2% real). Global returns across the biggest 12 countries have averaged 6.8% in nominal returns and 4.9% in real terms. In most countries, real estate values bottomed in 2010 and then grew steadily upward in an uninterrupted fashion. In many countries there has been only one or possibly two years of negative returns embedded in the ten-year averages.

All these indices show real estate performance unlevered and before fees -- two conditions that no investor ever faces. However, with low/falling debt costs over this period, the effects of conservative leverage and a steady fee drag of approximately 75 to 100 basis points, these two uncaptured elements of return approximately cancel each other out[15].

Average Annual Private Real Estate Returns

TEN LARGEST COUNTRIES IN MSCI GLOBAL REAL ESTATE INDEX

	2018	5yr	10yrs
Australia	10.2%	11.7%	9.3%
Canada	7.9%	7.2%	8.5%
France	7.1%	7.7%	6.5%
Germany	9.9%	8.3%	6.2%
Global	7.6%	8.8%	6.8%
Japan	6.6%	7.6%	4.4%
Netherlands	14.8%	10.0%	5.7%
Sweden	10.7%	11.6%	9.3%
Switzerland	6.1%	5.9%	6.2%
UK	5.2%	9.8%	9.0%
US	7.3%	9.2%	7.1%

* Global includes other countries that are not shown.
Source: MSCI Global Annual Property Index (unlisted property -asset level)

15 This assumption is typical of the many "work arounds" that investors deal with when they try to measure their performance. Fund-level benchmarks, published net of fees and leverage, are becoming much more useful to investors and are gradually getting organized in many different countries.

Real Estate Securities Have Recovered

Global real estate securities (GRES) have started 2019 on a strong track, driven by solid fundamentals and declining interest rates throughout the world. Although the sector cooled in April/May after a strong first quarter, the FTSE EPRA Nareit Developed Index posted a 13.2% return through five months of 2019, compared to 10.1% for the global equity index and 3.3% for global bonds (all reported in USD). GRES outperformance is even more pronounced over the past year, outpacing the MSCI World Index by 8.2% and Global Bonds by 5.4%.

Over longer time periods, GRES returns have been similar to those of Global Equities, with GRES ahead over the past 10 years. GRES returns have benefited over the past decade from:

- Increasing transparency in global real estate markets[16], which lowers required returns.
- Improving governance by many companies, with some examples cited below.
- Increasing urbanization and densification across the world, which leads to higher land (and asset) values.
- Improved real estate technologies that improve tenant experience and reduce operating costs.

Table 1. GRES Performance Relative to Global Equities and Bonds
(AS OF 5/31/2019, IN USD)

			Annualized Returns			
Index		**2019 YTD**	**1-year**	**3-year**	**5-year**	**10-year**
GRES	**EPRA Developed**	13.2%	8.5%	6.2%	5.7%	11.3%
Global Equities	**MSCI World**	10.1%	0.3%	9.6%	6.2%	10.6%
Global Bonds	**Bloomberg-Barclays Aggregate**	3.3%	3.1%	1.9%	0.9%	2.7%

Source: FTSE EPRA Nareit, LaSalle Investment Management

16 See JLL Real Estate Transparency Index

We expect these trends to continue and, in some cases (technology), accelerate over the coming decade.

For 2019 and most of the past ten years, GRES returns have been led by North America, particularly the U.S. Through the first 5 months of 2019, U.S. REITs have led all countries with a total return of 15.5%, as strong fundamentals and a decline in both current interest rates and expected interest rates have boosted values. Asia Pacific returns have been ahead of Europe so far this year and for the past year, as well as three and five years. Australia has had the best performance in Asia Pacific, consistent with strong private equity returns in that country. European returns have lagged in recent years, brought down by Brexit-driven concerns in Britain.

This ranking is based on returns denominated in USD. Returns in local currencies are more variable as exchange rates shift rapidly across countries and across time. Over 10 years, returns based in local currencies are generally similar to USD results. The main differences are in the commodity countries of Canada and Australia, where falling oil prices have negatively affected local currencies, and the U.K., where the GBP has fallen due to Brexit concerns. On the other hand, Japanese companies have performed better in USD, as the JPY has appreciated over the past 10 years.

Table 2. Country/Region GRES Performance

		Annualized Returns			
	2019 YTD	1 Year	3 Year	5 Year	10 Year
EPRA Developed	13.2%	8.5%	6.1%	5.7%	11.3%
North America	15.4%	13.5%	5.8%	7.2%	14.6%
U.S.	15.5%	13.7%	5.7%	7.4%	14.8%
Canada	14.4%	9.2%	8.8%	3.8%	11.9%
Europe	9.7%	-2.7%	3.7%	3.7%	10.3%
Continent	10.5%	0.4%	7.4%	6.4%	10.9%
Britain	7.7%	-10.8%	-4.3%	-2.2%	8.2%
Asia Pacific*	10.7%	6.1%	8.3%	4.1%	7.8%
Australia	12.8%	9.8%	7.2%	7.5%	12.4%
Hong Kong	10.8%	3.2%	15.6%	7.1%	6.7%
Singapore	10.1%	2.8%	10.8%	3.9%	7.7%
Japan	9.9%	7.3%	3.7%	0.7%	7.1%
Global Ex-US	10.6%	3.0%	6.7%	3.9%	8.7%

Source: FTSE EPRA Nareit, LaSalle Investment Management. Data as of 5/31/2019.

Within the U.S. REIT universe, property sectors with the strongest fundamentals and resilient demand drivers, such as cell towers, life sciences, single family homes, and industrial sectors, have outperformed. After a slow start, the self storage sector has improved, owing to better than expected operating fundamentals and as revenue growth may be stabilizing. Regional mall performance has been quite weak this year, as retail sentiment has turned more negative with an accelerated number of retailer store closures and weaker outlooks from the retailers themselves. In Canada, REITs outperformed in the first quarter, along with the broader equity market, but performance cooled in the past few months. Slowing economic growth has driven a more dovish action from the Bank of Canada, similar to central banks around the world.

Despite the growth slowdown in Europe, real estate fundamentals have remained healthy, particularly in the prime CBD office markets. London office demand and leasing activity remains resilient despite lingering Brexit uncertainty. The industrial sector continues to benefit from robust fundamentals, while specialty sectors like self storage and student housing have also outperformed, benefitting from increased investor awareness following strong operating fundamentals and healthy internal growth outlooks. The German residential sector has come under pressure of late due to a potential referendum aimed at expropriating residential assets from current landlords or freezing rents for such assets. The retail sector continues to be hindered by well-documented headwinds, valuation downgrades and cautious outlooks which are contributing to further bifurcation between higher and lower quality assets.

With solid office demand, European office companies have been increasing dispositions to fund ramped up development pipelines. Other notable transactions or events include Unibail-Rodamco-Westfield's sale of its Paris trophy office asset, Majunga office tower, as well as Ireland's Green REIT's decision to sell its portfolio of office assets to realize a meaningful premium to net asset value for its shareholders.

Property companies in Asia Pacific have outperformed the region's broader equity markets in 2019. However, slowing economic growth and the escalation of trade tensions is a concern and has prompted stimulative monetary and fiscal measure from China, as well as the Reserve Bank of Australia's first cut to its cash rate in 3 years. The Bank of Japan has reiterated its commitment to accommodative policy, especially ahead of the upcoming consumption tax increase.

Real estate fundamentals remain broadly healthy in the region, as does investment demand, with strength in the office and industrial markets. Australian real estate companies have led the region higher, buoyed by strong performance from the industrial and office sectors. The Australian residential sector rallied following the unexpected re-election of the ruling conservative coalition and Prime Minister, as well as increased expectations for more accommodative monetary policy in the region. Tokyo and Hong Kong office fundamentals also remain strong with tight vacancy levels. Real estate companies with exposure to the non-Central Hong Kong office market and markets of regional Japanese cities have produced the strongest performance this year.

Similar to many countries, the Aussie retail sector has been pressured by e-commerce disruption and housing market weakness. Additionally, a high volume of retail assets are expected to be marketed over the short term, raising concerns about the depth of the investor market.

Global Real Estate Securities Outlook

Leading economic indicators continue to align with a more muted, but positive pace of expansion (Slowbalisation) as governments and central banks continue to provide stimulative fiscal and monetary policies. As discussed in Chapter 1, escalating global trade tensions and pockets of softening economic data have reignited fears of a material slowdown in global economic growth, but the Peter Pan economy should persist into 2020.

The expectation for modest, but positive economic growth and a lower interest rate environment is a sweet spot for real estate (both public and private), and should remain sufficient to support both real estate fundamentals and values. LaSalle continues to project solid earnings and dividend growth from real estate securities, provided a recessionary environment is averted.

Global real estate securities are trading largely in line with their historical average trading ranges with alternatives - private real estate, bonds and equities, while certain sectors and countries continue to offer significant pricing discounts. As we have discussed previously[17] , allocations to GRES provide similar returns to private real estate over the long term with far superior liquidity, access to high quality properties and management teams, and exposure to niche property types, many of which have superior risk/return characteristics and are difficult to access in the private market.[18]

17 See Public and Private Real Estate: The Sum is Greater than the Parts.
18 See Completion Strategies for Real Estate

Non Core Private Equity Returns

A consistent and quantitative approach to fair value analysis (required vs expected returns) is not easily extended to value-add and opportunistic (broadly non-core) investment styles. There are many reasons why reporting on both achieved and prospective performance of non-core strategies is much more difficult.

- One headline challenge to extension to non-core are issues of data availability.
- Another challenge is the lack of clarity of what investment strategies fit into the non-core investment buckets.
- Another issue is the stated objective of the investment vehicle. While core investment is typically through separate accounts or open-end funds, these are generally targeting a return relative to a benchmark. Non-core, closed-end funds, however, are typically communicating their return target to investors during fund raising and then will make investments to achieve that return.
- These issues inter-connect to create a situation where non-core investment is often defined by the return objective rather than a fixed set of risks or investment strategies.
- Closed-end fund managers are communicating a target return to their investors, and the expectation is that they will make investments that will achieve that. There can be leverage, income, or development restrictions that could constrain the risk profile to some degree…but overall the goal will be to deliver a return. IF the return they are promising is too low, they will not be able to raise capital; too high, and it would communicate too much risk-taking to the investment community.

The graph below shows the trends in Target IRRs for U.S. Value-Add and Opportunistic funds. This data shows that generally the target returns are stable year-to-year, but over time they have exhibited some decline, with the decline largely occurring in the last several years. Since 2003, the average return target has fallen by 2.5% for Value-Add funds and 3.0% for Opportunistic funds. This decline mirrors the decline in core required returns that we have seen…which largely mirrors the decline in the risk-free rate. It is reasonable to assume that these vintage year return targets lag the time in which they are set by at least a year. So, we see a parallel trend between declining 10-year bond rates, in the two years just ahead of a fund launch, and lower target returns by non-core funds when sorted by vintage year.

As the regional comparison table (above right) shows, the results for non-core funds over various time periods are uneven. If the analysis period includes the GFC (=>10-year performance) non-core funds as a group were simply not able to match the stronger performance of core funds in any region, except the U.S. If analysis could be done on a risk-adjusted basis (taking into account higher leverage or development), even the U.S. non-core funds would have a hard time competing with the performance of core funds. Although not shown, the top quartile of non-core funds was able to outperform core returns by a significant margin in all three regions. The challenge for an investor is to find these "positive alpha" producers amongst a wide range of fund sponsors and strategies.

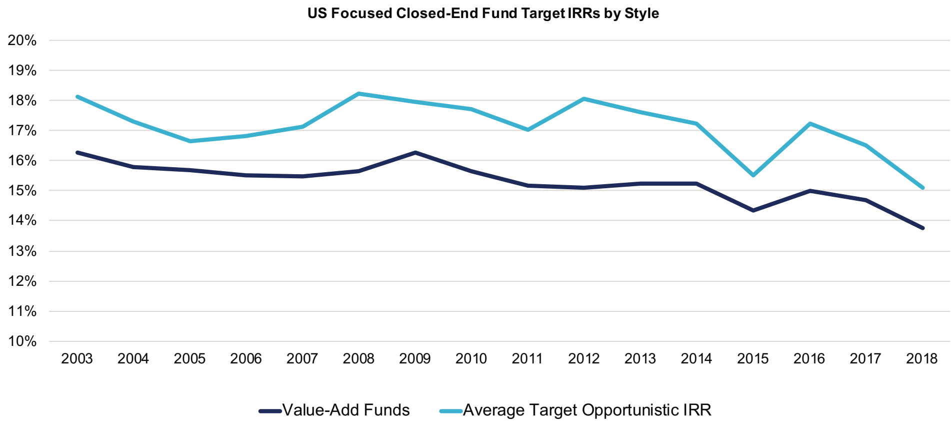
Comparison of Core, Value-Add, and Opportunistic Returns by Region

	U.S. Core Funds[1]	U.S. Value-Add Funds[2]	U.S. Opportunistic Funds[3]	Asia-Pacific Core Funds[4]	Asia-Pacific Value-Add Funds[5]	Asia-Pacific Opportunistic Funds[6]	Europe Core Funds[7]	Europe Value-Add Funds[8]
1 Year	7.4%	8.7%	5.9%	10.2%	7.2%	5.0%	8.1%	5.2%
3 Year	7.3%	11.1%	8.5%	12.2%	12.6%	7.5%	7.8%	7.5%
5 Year	9.4%	12.5%	9.6%	12.6%	11.1%	6.5%	8.1%	8.8%
10 Year	6.0%	7.7%	8.0%	9.0%	3.9%	7.8%	5.2%	2.2%
15 Year	7.2%	7.0%	7.0%				5.2%	3.6%
20 Year	7.5%	7.3%	7.2%					

Notes and Sources
1 NCREIF ODCE Index Return. Net time-weighted returns in USD. Data as of 4Q 2018.
2 Cambridge Real Estate Benchmark. Data as of 4Q 2018. Net time-weighted returns in USD.
3 Cambridge Real Estate Benchmark. Data as of 4Q 2018. Net time-weighted returns in USD.
4 ANREV Annual Fund Index. Gross Time Weighted Returns in USD. Data as of 12/31/2018
5 ANREV Annual Fund Index. Gross Time Weighted Returns in USD. Data as of 12/31/2018
6 ANREV Annual Fund Index. Gross Time Weighted Returns in USD. Data as of 12/31/2018
7 INREV Annual Fund Index. Net Time Weighted Local Currency Returns. Data as of 12/31/2018
8 INREV Annual Fund Index. Net Time Weighted Local Currency Returns. Data as of 12/31/2018

Target IRRs for Non-Core Funds Trending Lower

U.S.-FOCUSED FUND TARGET RETURNS TRENDING LOWER, MIRRORING INTEREST RATES AND CORE RETURNS



Source: Prequin. Return Targets are based on data gathered by Prequin and are reflective of stated fund objectives rather than any realization of investments.

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