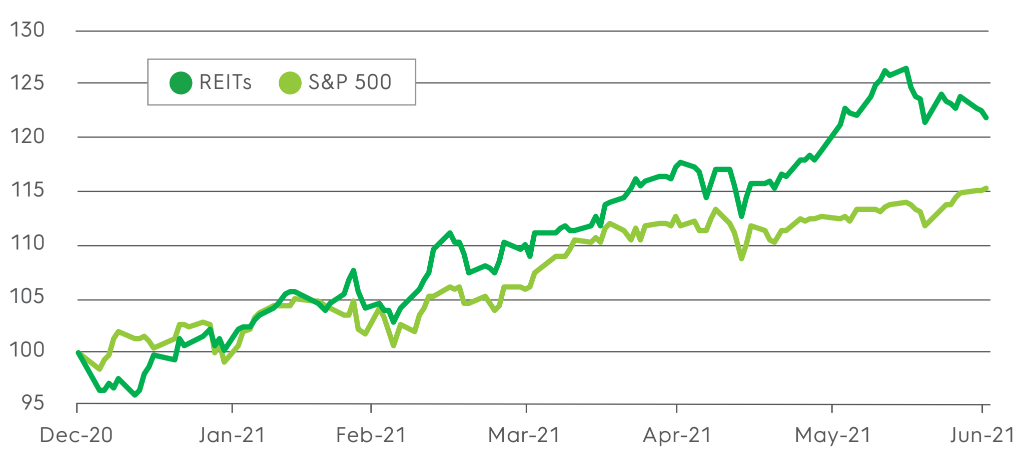
Rebound for REITs

Benefits and the outlook for Real Estate Securities

With pandemic restrictions waning coupled with strong pent-up consumer demand, real estate investment trusts (REITs) are feeling the love.

Real estate stocks are in favor again as the nation's "open for business" signs began to flash brightly. The current economic, monetary, and interest rate backdrop provides a sunny outlook for real estate. REITs, represented by the FTSE NAREIT Equity REITs Index, outpaced the S&P 500 in the second quarter of 2021, returning 12% compared to 8.5% for the S&P 500.

GROWTH OF $100



Source: Bloomberg. As of 06/30/2021. Data spans from 12/31/2020 to 06/30/2021. REITs represent the FTSE NAREIT Equity REITs Index.

REIT Benefits

Performance and diversification.

REIT stocks have low correlation with other equities and with fixed income investments. They can contribute to the benefits of a diversified portfolio.

Dividend growth as inflation hedge.

REITs are required by law to distribute at least 90 percent of their taxable income. This means that as inflation causes increased rental rates and property value, REIT income, cash flow and dividends are positioned to increase as well.

Liquidity and transparency.

Public REIT shares trade on the open market and can be sold relatively quickly compared to privately held real estate, which is generally brokered and can take several months to close.

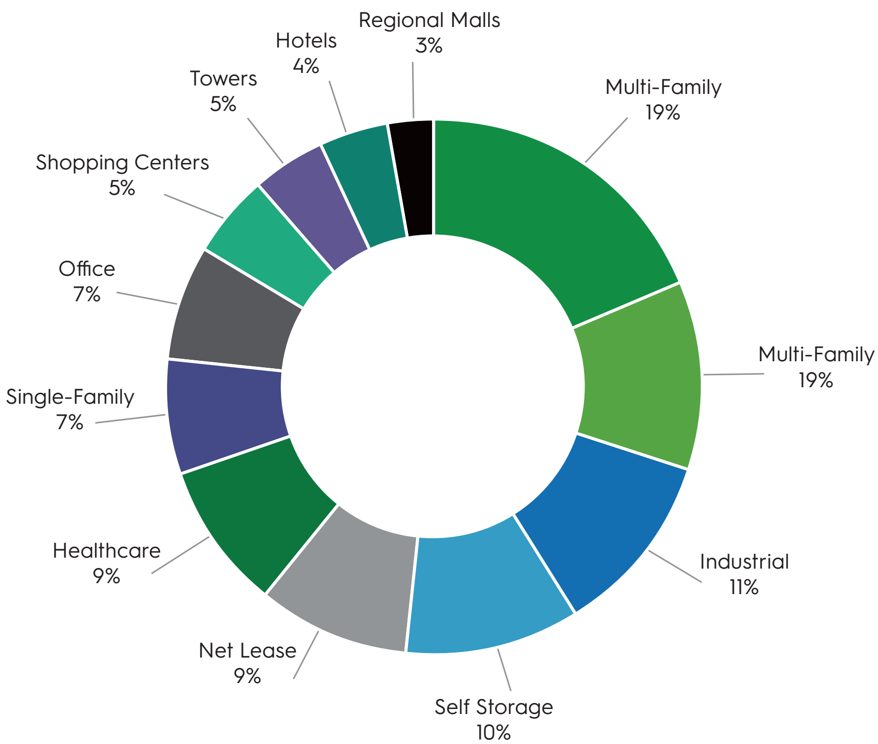
Experienced professional management.

REITs typically have experienced teams of professionals in place to manage, maintain and run the properties.

Sector diversification within REITs

REITs can provide both liquidity and diversification for investors within the hard-asset, inflation-hedging qualities of commercial real estate. One is hard pressed to find a property sector which doesn't stand to benefit from a "return to normal" post-Covid. Consumer sentiment has rebounded causing pent up demand for, well, nearly everything. Shoppers have returned to retail centers, hotel occupancies have rebounded, single family residential occupancies are at record highs, multi-family remains positive, and senior housing demand has decidedly turned the corner. Self-storage has remained incredibly resilient throughout the pandemic.

SECURIAN AM REIT PORTFOLIO SECTOR BREAKOUT
AS OF 6/30/2021



Source: FactSet, Securian Asset Management, Inc. As of 06/30/2021. Investment characteristics shown are of the Securian AM-selected representative account that invests its assets pursuant to the Real Estate Securities strategy. See additional disclosure at the end of the materials.

The office sector was among the beneficiaries of the early re-opening, along with retail and hotels. While office usage certainly isn't dead, we believe its full post-pandemic recovery is certainly in question. Hybrid work arrangements will likely become the norm and alter office demand and operating costs in significant ways. Demand for datacenter space remains strong, but increased competition is leading to lower lease rates. We expect that the build-out of 5G networks could act as a tailwind for leasing and earnings growth with the towers sector.

Outlook for Real Estate Securities

The Federal Reserve's (Fed) commitment to rock bottom short-term rates is amplifying easy financial conditions. Despite what appears to be building price pressures and worries about valuations, interest rates remain well-anchored to the Fed's narrative. Expectations for above-trend growth and inflation have steadily increased this year, but rates remain well behaved with the 10-year US Treasury rate trending back below 1.5%. The net effect is that investors appear to continue to accept Treasury rates that don't exceed expected inflation, as measured by 10-year Treasury inflation-protected securities (TIPS) breakeven rate of 2.34% as of 6/30/2021.

In the second quarter, we experienced a commercial real estate recovery that has begun in earnest. We doubt that all property types will return to pre-pandemic cash flow levels in lockstep. Those with short duration lease profiles such as apartments, single family rentals, and self-storage should fare well in a rising inflation environment. The pandemic accelerated trends that were already in place and focused a spotlight on sectors with both strong and with bleak futures. Hybrid work arrangements are here to stay, causing demand for office space as well as business travel to likely face a long recovery. As will bricks and mortar retail. We believe strongly in "new economy" sectors such as data centers and cell towers.

In our view, REIT stocks remain attractively valued, particularly against the backdrop of Fed actions, improving economic growth, and historically low interest rates. As was our view in the first quarter, we believe an environment where the 10-year US Treasury remains range-bound, coupled with steadily improving economic growth serves as a nirvana for real estate. However, new vaccine-resistant strains and potentially higher 10-year US Treasury rates represent two primary risks that could cause the group to come under pressure in the second half of the year.

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