

2019-2020

# REIT Quick Facts

For financial professionals

- Updates and insights
- Performance data
- Guidelines for setting portfolio allocations

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# Embracing the role of REITs in diversified investment portfolios

If you are among the vast majority of financial professionals who embrace the use of REITs for portfolio diversification, you already recognize that:

- Along with stocks, bonds and cash, real estate is a fundamental asset class
- REITs are an effective, liquid, and low-cost means of investing in the real estate asset class

## Acceptance is widespread and growing

Today, the REIT approach to real estate investing is embraced by:

- **80% of registered investment advisors**—who recommend REITs to their clients<sup>1</sup>



- **Leading investment management firms**—including BlackRock®, Fidelity® and State Street Global Advisors® who offer REIT-focused products
- **97% of target date funds**—nearly all target date funds have REIT allocations<sup>2</sup>



# Looking Closer

## WHY real estate?

### A key asset class

commercial real estate, like stocks, bonds and cash, is a fundamental part of a diversified portfolio that covers the entire U.S. investment market

### A distinct economic cycle

relative to the cycle for most other stocks and bonds due, in part, to supply inelasticity

### Long-term investment returns

that have provided high and growing income from rents plus moderate capital appreciation over time

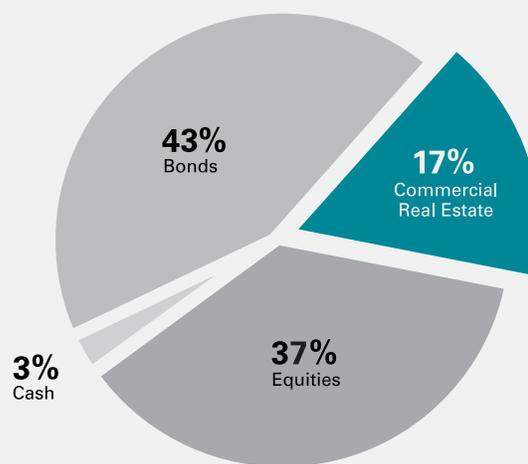
### Inflation protection attributes

due in part to the fact many leases are tied to inflation and that real asset values have tended to increase in response to rising replacement costs

At 17%, commercial real estate is the **third largest asset class**

in the U.S. investment market<sup>3</sup>

**Is it underrepresented in your clients' portfolios?**



## WHY REITs?



**Performance**—The real estate market is the primary driver of REIT returns, therefore REITs may be used as a liquid proxy for gaining access to the entire asset class<sup>3</sup>



**Liquidity**—Bought & sold like other stocks, mutual funds and ETFs



**Diversification**—Low correlation with other stocks and bonds<sup>4</sup>



**Dividends**—Reliable income returns<sup>5</sup>



**Simplicity**—Compared with alternatives, REIT investing is straightforward and transparent, so investors may be more likely to understand and utilize REITs in their portfolios<sup>6</sup>

Key performance statistics through December 31, 2018 include:

**9.9%**

The trailing 25-year annualized total return of the Index\*

**16**

The total number of years out of the past 25 that the Index\* has outperformed the S&P 500

**4.8%**

The dividend yield of the Index\* (which was more than double the S&P 500 dividend yield of 2.2%)

\* Key performance data for the FTSE Nareit All Equity REITs Index through 12/31/18. For the latest data, visit [reit.com/data-research](http://reit.com/data-research)



# WHAT is an appropriate REIT allocation?

The answer will vary based on each investor's goals, risk tolerance and investment horizon, but here are some guidelines that can help:

## 5% to 15%

Multiple studies have found that the optimal REIT portfolio allocation may be between 5% and 15%.<sup>7</sup>

David F. Swensen, PhD, noted CIO of the Yale endowment and author of *Unconventional Success: A Fundamental Approach to Personal Investment*, recommends a 15% allocation to REITs for most investors.

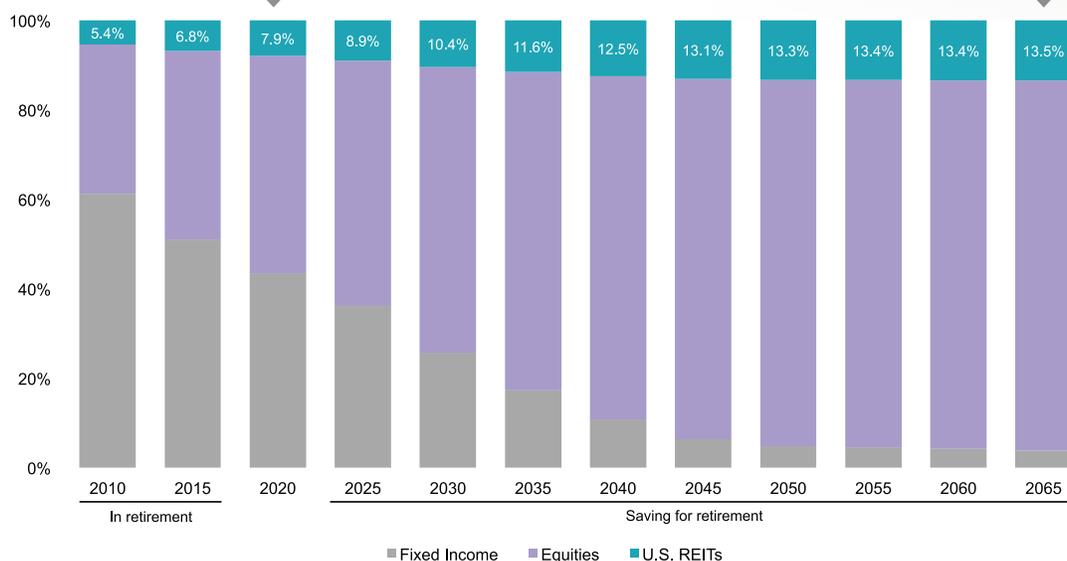
Not surprisingly, these percentages are in line with the 17% share of the U.S. investment market represented by commercial real estate.

# HOW do lifestages affect the optimal allocation?



**13%+** for an investor with a 45-year investment horizon<sup>8</sup>

Gradually declining to **7%+** at retirement<sup>8</sup>



The optimal allocations to global REITs and other real estate companies were found to be even higher<sup>8</sup>

# WHAT do the enclosed Morningstar® Fact Sheets show?

Compared to  
other stocks,  
bonds and T-Bills

REITs provided  
**THE LARGEST INCREASE**  
in wealth over 47 years<sup>9</sup>

Adding REITs  
to a hypothetical  
portfolio

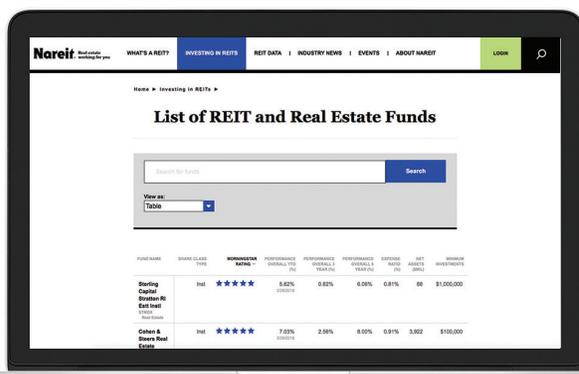
**INCREASED RETURNS**  
with no increase in risk<sup>10</sup>, and reduced the  
risk of retirees outliving assets<sup>11</sup>

REITs have  
provided

**STABLE INCOME**  
despite inflation and market fluctuations<sup>12</sup>

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- ▶ **RESEARCH** more than 300 REIT mutual funds and ETFs for your clients
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1. Source: Investment News' 2018 Outlook Survey of 344 advisers in December 2017.
2. Source: Nareit analysis using Morningstar Direct™.
3. Sources: Stock and bond data from Board of Governors of the Federal Reserve, Financial Accounts of the United States, 2018Q4; commercial real estate market size data based on Nareit analysis of CoStar property data and CoStar estimates of Commercial Real Estate Market Size, 2018Q4.
4. Source: CEM Benchmarking, 2018, available at <https://www.reit.com/sites/default/files/media/PDFs/Research/NAREITCEMUpdate2018Oct24.pdf>
5. Source: Nareit sponsored study by Wilshire Funds Management – Income Oriented Portfolios – Challenges and Solutions, October 2016.
6. Source: Cohen & Steers. "REITs: Answering the Call for DC Plan Diversification," January 2019.
7. Examples of studies within the stated range include: Ibbotson Associates, Morningstar, and Wilshire Funds Management.
8. Source: Nareit sponsored study by Wilshire Funds Management – The Role of REITs and Listed Real Estate Equities in Target Date Fund Allocations. Large-cap stocks – Wilshire U.S. Large Cap Index; Small-cap stocks – Wilshire U.S. Small Cap Index; International stocks – Morgan Stanley Capital International Europe, Australasia, and Far East (EAFE®) Index; Emerging Market Equities – MSCI Emerging Markets Index; U.S. bonds - Barclays U.S. Aggregate Bond Index; Non-U.S. bonds – Citigroup Non-USD World GBI; U.S. REITs – FTSE Nareit All Equity REIT Index.
9. For details, refer to Performance: Stocks, Bonds, Bills, REITs, a Morningstar® Fact Sheet available at [reit.com/quickfacts](http://reit.com/quickfacts).
10. For details, refer to The Role of REITs in a Portfolio, a Morningstar® Fact Sheet available at [reit.com/quickfacts](http://reit.com/quickfacts).
11. For details, refer to Retirement Portfolios, a Morningstar® Fact Sheet available at [reit.com/quickfacts](http://reit.com/quickfacts).
12. For details, refer to Dividends and Inflation, a Morningstar® Fact Sheet available at [reit.com/quickfacts](http://reit.com/quickfacts).

**IMPORTANT:** These facts exclusively address stock exchange-listed Equity REITs. To learn how this type of REIT differs from a Mortgage REIT, and how listed REITs differ from non-listed REITs, see the SEC Investor Bulletin Real Estate Investment Trusts (REITs) available at <http://sec.gov/investor/alerts/reits.pdf>. REIT investments are not suitable for all investors. Past performance is no guarantee of future results.

Unless otherwise indicated, REIT data presented are historical performance data which are derived from, and apply only to, publicly traded securities. While such data are believed to be reliable when prepared or provided, such data are subject to change or restatement. Nareit does not warrant or guarantee such data for accuracy or completeness, and shall not be liable under any legal theory for such data or any errors or omissions therein. See <http://reit.com/TermsOfUse.aspx> for important information regarding this data, the underlying assumptions and the limitations of Nareit's liability therefor, all of which are incorporated by reference. Performance results are provided only as a barometer or measure of past performance, and future values will fluctuate from those used in the underlying data. Any investment returns or performance data (past, hypothetical or otherwise) shown herein or in such data are not necessarily indicative of future returns or performance.

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## About REITs

REITs are real estate working for you. Through the properties they own, finance and operate, REITs help provide the essential real estate we need to live, work and play. REITs of all types collectively own more than \$3 trillion in gross assets across the U.S. Public REITs own approximately \$2 trillion in assets and stock exchange listed REITs have an equity market capitalization of more than \$1 trillion. In addition, more than 80 million Americans invest in REIT stocks through their 401(k) and other investment funds.

## About Nareit

Nareit® is the worldwide representative voice for REITs and publicly traded real estate companies with an interest in U.S. real estate and capital markets. Nareit's members are REITs and other businesses throughout the world that own, operate, and finance income-producing real estate, as well as those firms and individuals who advise, study, and service those businesses. This information is solely educational in nature and is not intended by Nareit to serve as the primary basis for any investment decision. Nareit is not acting as an investment adviser, investment fiduciary, broker, dealer or other market participant. Past performance is no guarantee of future results. It is important to note that REITs may not be suitable for all investors.

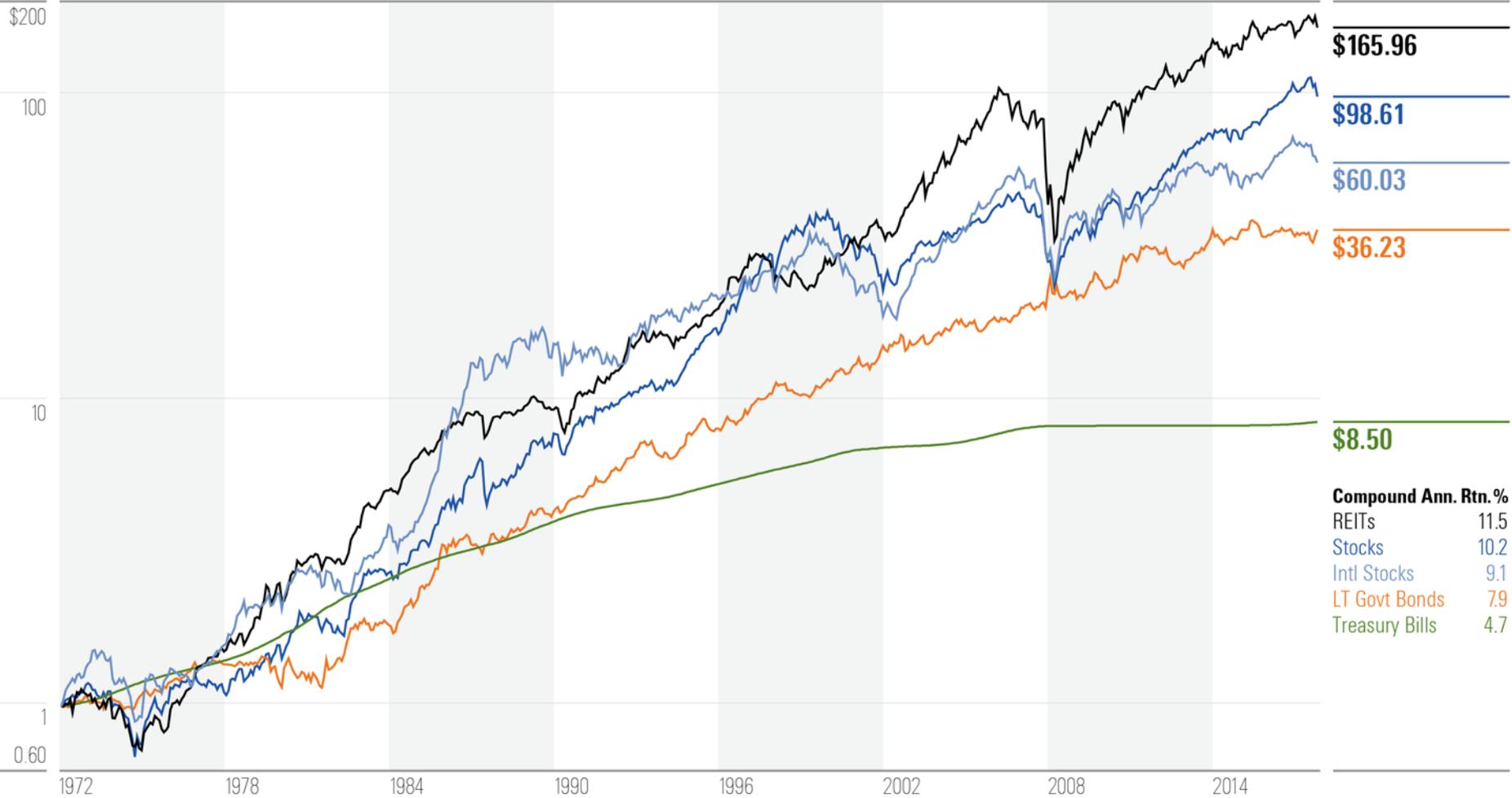


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# Performance: Stocks, Bonds, Bills, and REITs 1972–2018



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# Performance: Stocks, Bonds, Bills, and REITs

A 47-year examination of past capital market returns provides historical insight into the performance characteristics of various asset classes. This graph illustrates the hypothetical growth of a \$1 investment in five asset classes over the time period January 1, 1972 to December 31, 2018.

REITs and stocks have provided the highest returns and largest increase in wealth over the time period analyzed. As illustrated by the image, REITs provided the largest growth, followed by domestic and international stocks. Among fixed-income investments, bonds appreciated considerably, but still finished behind stocks, and Treasury bills offered only a fraction of the growth provided by REITs and stocks. However, the higher returns achieved by stocks and REITs also come with certain risks, which can be identified by the volatility or fluctuation of the graph lines.

Government bonds and Treasury bills are guaranteed by the full faith and credit of the U.S. government as to the timely payment of principal and interest, while returns and principal invested in stocks are not guaranteed. Stocks have been more volatile than other asset classes.

Returns and principal invested in REITs are not guaranteed. REITs typically provide high dividends plus the potential for moderate, long-term capital appreciation. A REIT must distribute at least 90% of its taxable income to shareholders annually. Real estate investment options are subject to certain risks, such as risks associated with general and local economic conditions, interest rate fluctuation, credit risks, liquidity risks and corporate structure. International investments involve special risks such as fluctuations in currency, foreign taxation, economic and political risks, liquidity risks, and differences in accounting and financial standards.

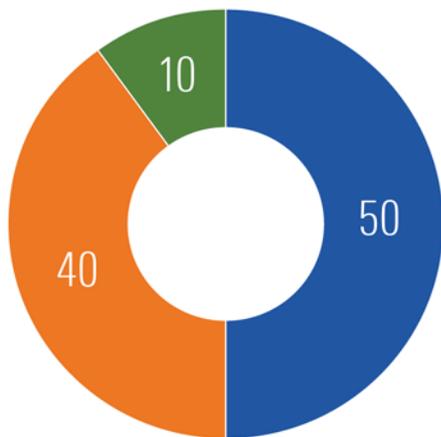
## About the data

REITs are represented by the FTSE NAREIT All Equity REIT Index<sup>®</sup>, stocks by the Standard & Poor's 500<sup>®</sup>, which is an unmanaged group of securities and considered to be representative of the U.S. stock market in general, international stocks by the Morgan Stanley Capital International Europe, Australasia, and Far East (EAFE<sup>®</sup>) index, bonds by the 20-year U.S. government bond, and Treasury bills by the 30-day U.S. Treasury bill. Inflation is represented by the Consumer Price Index. An investment cannot be made directly in an index.

# The Role of REITs in a Portfolio

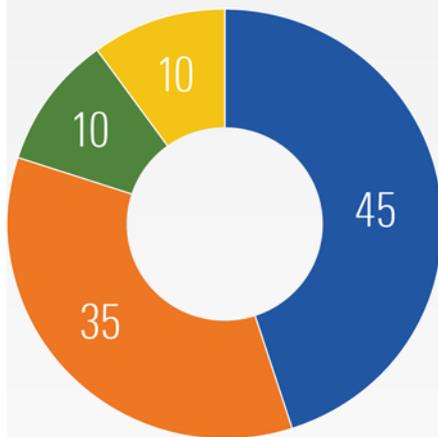
## Potential to increase returns (1972–2018)

Stocks and Bonds



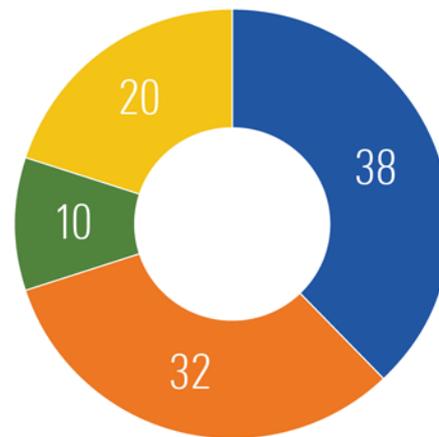
Return (%) 9.8  
Risk (%) 10.1

With 10% REITs



Return (%) 10.1  
Risk (%) 10.0

With 20% REITs



Return (%) 10.3  
Risk (%) 10.1

- Stocks
- Bonds
- Treasury Bills
- REITs

	Past	3 Year	5 Year	10 Year
Return (%)		5.8	7.1	9.0
Risk (%)		7.7	8.3	6.0

# The Role of REITs in a Portfolio

Real Estate Investment Trusts (REITs) have unique characteristics that may make them attractive to both income and growth investors. REITs trade like stocks and can fluctuate in price, but they also pay out a large part of their income in the form of dividends. REITs may be used to help provide income in conservative portfolios or long-term growth in more aggressive portfolios. Some portion of a portfolio may be appropriately allocated to REITs for a broad range of investor types.

The image illustrates risk-and-return profiles for three hypothetical portfolios from 1972 to 2018, and for the 10% REIT portfolio over the last 3, 5, and 10 years. Adding a 10% allocation to REITs in a stock, bond, and cash portfolio increased return from 9.8% to 10.1%. Adding a 20% allocation to REITs further increased return to 10.3% while maintaining the similar level of risk.

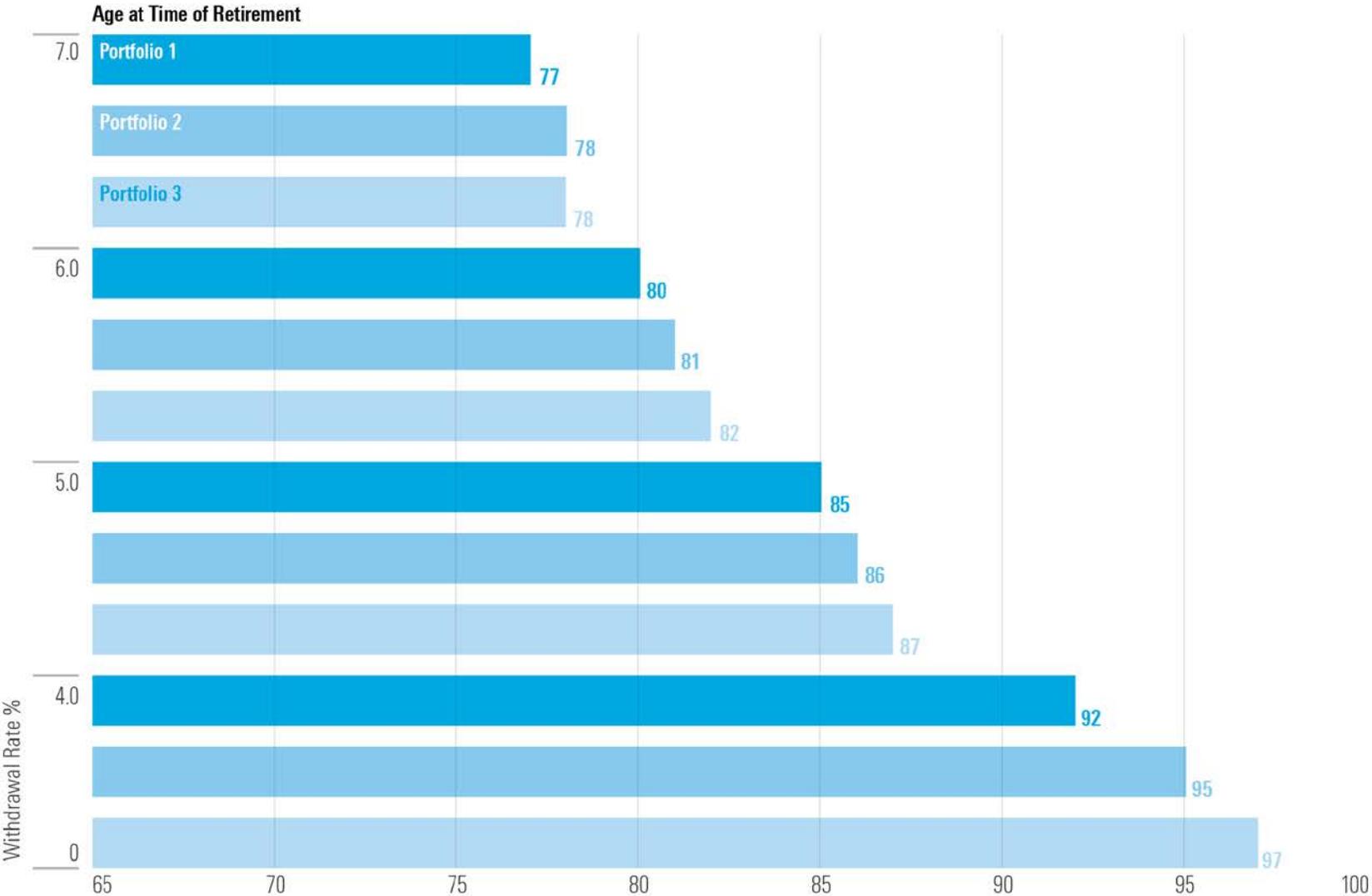
Because stocks, bonds, cash, and REITs generally do not react identically to the same economic or market stimuli, combining these assets may produce a more appealing risk-and-return trade-off. This makes REITs a potentially good candidate for investors looking to build a diversified portfolio, whether for long-term growth or for income.

Methodology: The allocations herein are intended to represent simplified portfolios for moderate (50% equity/50% fixed-income to 60% equity/40% fixed-income) investors. The portfolios represented are not Morningstar recommendations and should not be viewed as investment advice. The 1972 start date is constrained by the maximum available historical data for REITs. In order to analyze the impact of REITs on the portfolio's risk and return, 10% and 20% REIT allocations were added to the initial portfolios. Return was calculated by the arithmetic annual return and risk by the annual standard deviation. Standard deviation measures the fluctuation of returns around the arithmetic average return of the investment. The higher the standard deviation, the greater the variability (and thus risk) of the investment returns. No optimizations were used in this analysis. Portfolios were rebalanced annually. The result of this analysis illustrates that adding REITs to a portfolio has the potential to increase return through diversification.

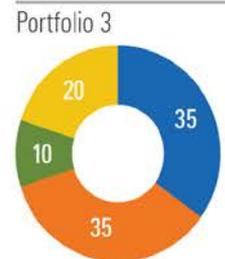
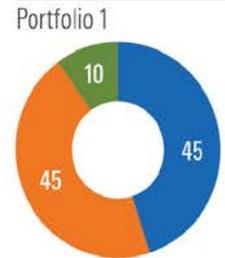
**REIT investments are not suitable for all investors. Past performance is no guarantee of future results.** Diversification does not eliminate the risk of experiencing investment losses. An investment cannot be made directly in an index. This is for illustrative purposes only and not indicative of any investment. The data assumes reinvestment of all income and does not account for taxes or transaction costs. Capital gains and dividends received may be taxed in the year received. Government bonds and Treasury bills are guaranteed by the full faith and credit of the United States government as to the timely payment of principal and interest. Bonds in a portfolio are typically intended to provide income and/or diversification. U.S. government bonds may be exempt from state taxes, and income is taxed as ordinary income in the year received. With government bonds, the investor is a creditor of the government. Stocks and REITs are not guaranteed and have been more volatile than bonds. Stocks provide ownership in corporations that intend to provide growth and/or current income. REITs typically provide high dividends plus the potential for moderate, long-term capital appreciation. A REIT must distribute at least 90% of its taxable income to shareholders annually. REITs involve special risks such as management quality, corporate structure, the ability to increase revenues from rents, and the balance of the supply of new buildings with demand for space. Additional risks include general and local economic conditions, interest rate fluctuation, credit risks, and liquidity risks. Holding REITs for the long term does not ensure a profitable outcome and investing in REITs always involves risk, including the possibility of losing the entire investment. The information, data, analyses and opinions contained herein do not constitute investment advice offered by Morningstar and are provided solely for informational purposes.

# Retirement Portfolios

Age to which portfolio may last (90% confidence level)



## Asset Allocation %



● Stocks
 ● Cash
 ● Bonds
 ● REITs

**IMPORTANT:** Projections generated by Morningstar regarding the likelihood of various investment outcomes using the Ibbotson Wealth Forecasting Engine are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. Results may vary over time and with each simulation. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. © Morningstar. All Rights Reserved.

# Retirement Portfolios

The inclusion of REITs in a retirement portfolio may increase the age to which the portfolio may last. The image illustrates the estimated age to which portfolios (\$1,000,000 initial value) with various allocations to REITs may last given a withdrawal rate. Consider a scenario where an investor retiring at age 65 withdraws 4% of his or her initial portfolio amount each year. A portfolio consisting of 45% stocks, 45% bonds, and 10% cash would last until age 92. This number increases by three years for a portfolio comprised of 40% stocks, 40% bonds, 10% cash, and 10% REITs. Furthermore, the portfolio with a 20% allocation to REITs would last until the investor is 97 years old. While including REITs may potentially improve the ability of a portfolio to support required withdrawals over a longer time period, it is also important to note that a higher rate of withdrawal would exhaust retirement savings sooner.

It is assumed that a person retires at 65 and withdraws an inflation-adjusted percentage of the initial portfolio wealth each year beginning at that age. The image was created using Monte-Carlo parametric simulation that estimates the range of possible outcomes based on a set of assumptions including arithmetic mean (return), standard deviation (risk), and correlation for a set of asset classes. The inputs used herein are hypothetical, based on historical long-term figures. The hypothetical risk and return of each asset class, cross-correlation, and annual average inflation follow. Stocks: risk 20.2%, return 12.1%; Bonds: risk 9.8%, return 5.9%; REITs: risk 18.4%, return 13.5%; Inflation: return 3.0%. Annual investment expenses assumed were 0.73% for stock mutual funds and REITs and 0.60% for bond mutual funds. Other investments not considered may have characteristics similar or superior to those being analyzed. The simulation is run 5,000 times, to give 5,000 possible 35-year scenarios. While simulation can produce results that show probabilities of an outcome, the analysis presented herein is at the 90% confidence level. A 90% confidence level indicates that there is a 90% chance of the outcome being as shown or better. Higher confidence levels are chosen in order to simulate tougher market conditions. A limitation of the simulation model is that it assumes a constant inflation-adjusted rate of withdrawal, which may not be representative of actual retirement income needs. This type of simulation also assumes that the distribution of returns is normal. Should actual returns not follow this pattern, results may vary.

Diversification does not eliminate the risk of experiencing investment losses. Government bonds and Treasury bills are guaranteed by the full faith and credit of the U.S. government as to the timely payment of principal and interest, while returns and principal invested in stocks are not guaranteed. Stocks have been more volatile than other asset classes.

Returns and principal invested in REITs are not guaranteed. REITs typically provide high dividends plus the potential for moderate, long-term capital appreciation. A REIT must distribute at least 90% of its taxable income to shareholders annually. Real estate investment options are subject to certain risks, such as risks associated with general and local economic conditions, interest rate fluctuation, credit risks, liquidity risks and corporate structure.

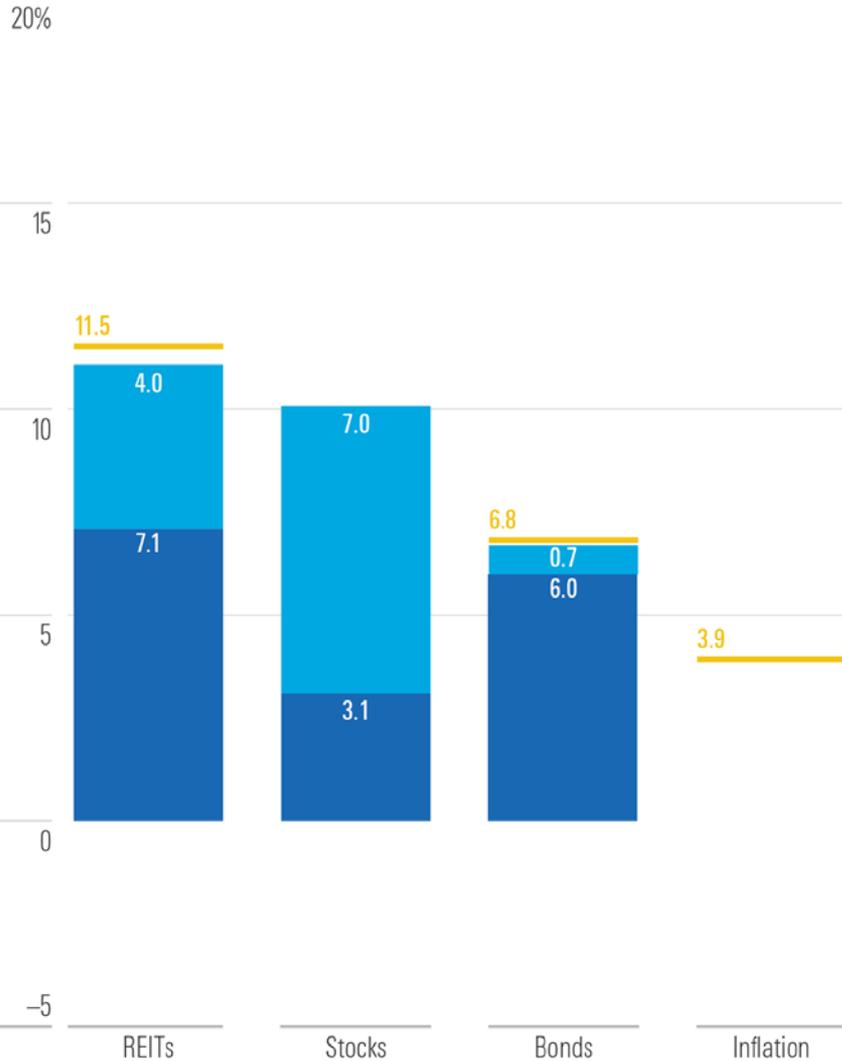
## About the data

Stocks are represented by the Ibbotson® Large Company Stock Index. Bonds are represented by the 20-year U.S. government bond, cash by the 30-day U.S. Treasury bill, REITs by the FTSE NAREIT All Equity REIT Index®, and mutual fund expenses from Morningstar. An investment cannot be made directly in an index. The data assumes reinvestment of income and does not account for taxes or transaction costs.

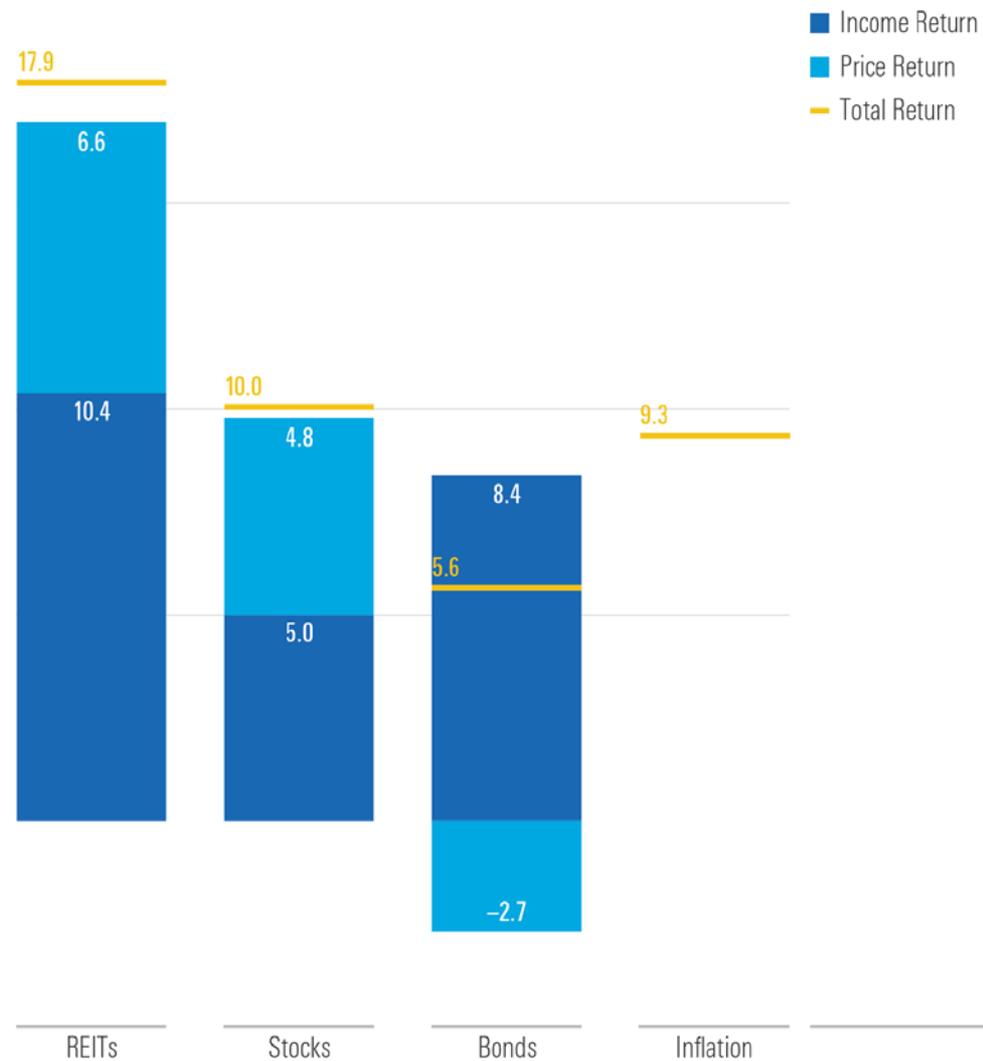
# Dividends and Inflation

## Stocks, bonds, and REITs, 1972–2018

Historical (1972–2018)



High Inflation (1974–1980)



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# Dividends and Inflation

As an investor nearing retirement, you may ask whether an allocation to dividend-paying stocks or REITs in your retirement portfolio will help counter high inflation. Examining stock and REIT returns during periods of high inflation may help answer this question. Investors often think of stocks and REITs as a capital appreciation vehicle or a tool for growing portfolio wealth. Little do some investors realize, however, that dividend-paying stocks or REITs can also be an income tool. This is especially relevant for investors seeking to manage their portfolios in retirement, when the need for current income takes precedence over the need for capital accumulation.

The image illustrates the income potential for bonds, REITs, and stocks historically (1972–2018) as well as during a period of high inflation (1974–1980). The figures in the bars represent the portion of total return that can be attributed to income return (versus capital appreciation). While stocks and REIT prices tend to be volatile, dividends serve as a stable component of total return and may provide better inflation protection compared with bonds. Between 1974 and 1980 (high inflation), the average rate of inflation was 9.3%, much higher than the historical rate (1972–2018) of 3.9%. During this time, bonds yielded 8.4% from income but prices declined by 2.7%, resulting in a total return of 5.6%—way short of inflation. On the contrary, stocks returned a total of 10.0%: 5.0% from dividend income and 4.8% from price return, outpacing inflation for this time period. The income return of REITs alone was 10.4%, higher than the 9.3% rate of inflation. REITs returned a total of 17.9% for this time period.

Dividend-paying stocks and REITs can serve as part of a growth investor's strategy, while also helping to seek the income return requirement for income-oriented investors. These investments can also play an important role in retired investors' portfolios because of their high potential to generate income.

Dividends are not guaranteed and are paid at the discretion of the stock-issuing company. Diversification does not eliminate the risk of experiencing investment losses. An investment cannot be made directly in an index. Government bonds are guaranteed by the full faith and credit of the United States government as to the timely payment of principal and interest, while stocks and REITs are not guaranteed. REITs are subject to certain risks, such as risks associated with general and local economic conditions, interest rate fluctuation, credit risks, liquidity risks and corporate structure. It is important to note that REITs may not be suitable for all investors.

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