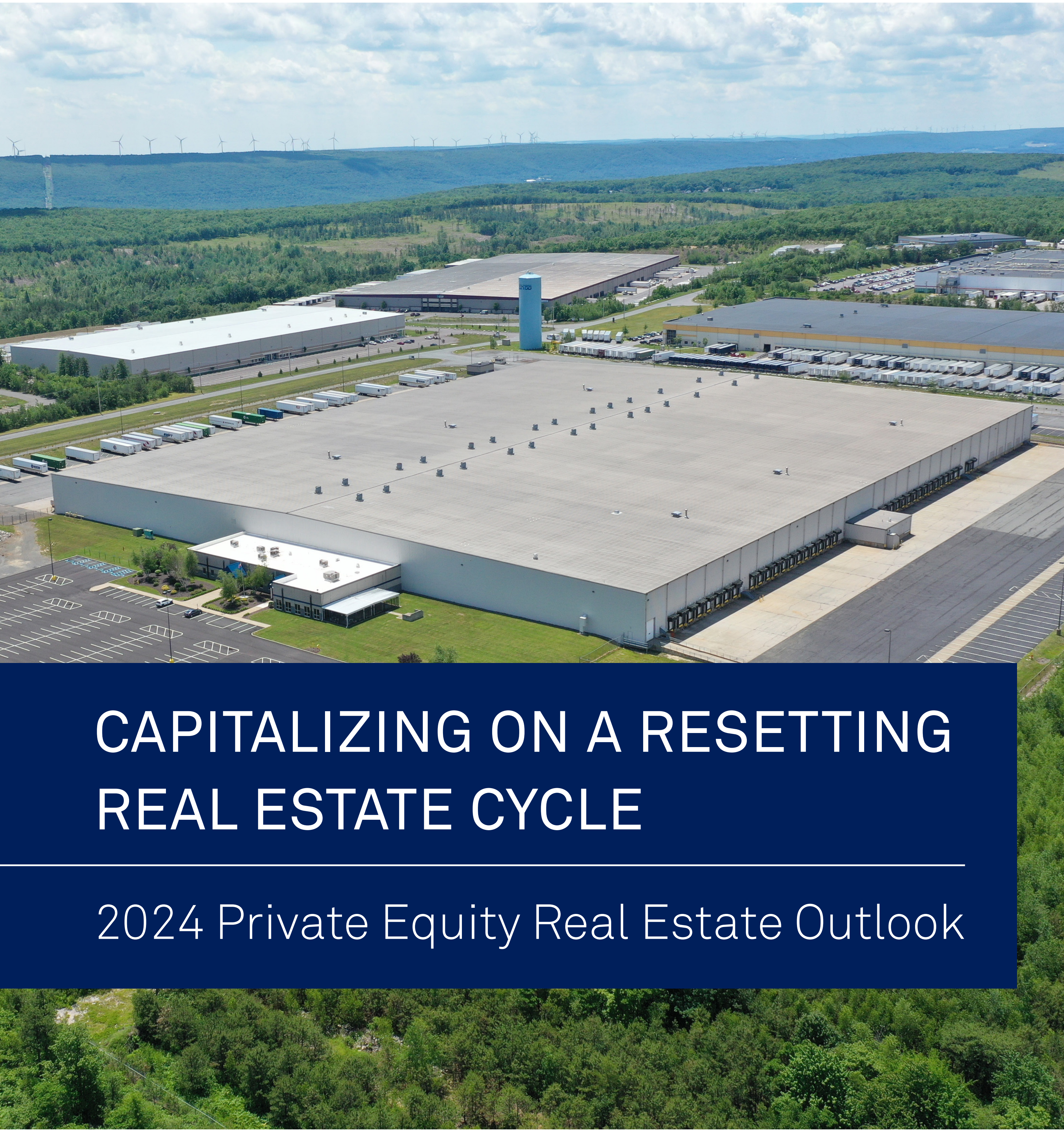
CenterSquare
REAL ASSET INVESTMENT LEADERSHIP



CAPITALIZING ON A RESETTING REAL ESTATE CYCLE

2024 Private Equity Real Estate Outlook

Capitalizing on a Resetting Real Estate Cycle

While public markets have rapidly repriced in alignment with borrowing costs, the private market remains sluggish in this regard. Transaction volumes remain low as sellers await a more hospitable transaction market, and buyers remain on the sidelines waiting for sellers to reset expectations. As a result, our outlook touches on both sides of the same coin. On one side, the rapid rise in interest rates doubled the cost of borrowing in just a few quarters, relegated bank lending to the sidelines, and left many property owners who overpaid for properties in the last few years underwater as valuations reset lower. On the flip side, however, we believe the coming year is setting up to be a fantastic entry point for real estate investors driven by the following market opportunities:

- Target high conviction sectors with asymmetric payoffs driven by strong real estate fundamentals (i.e., low supply, resilient demand).
- Capitalize on resetting valuations by acquiring high quality real estate at a lower basis.
- Take advantage of the lack of debt availability that is not only curtailing new construction starts, but also creating a powerful competitive advantage for the best borrowers who can access debt.

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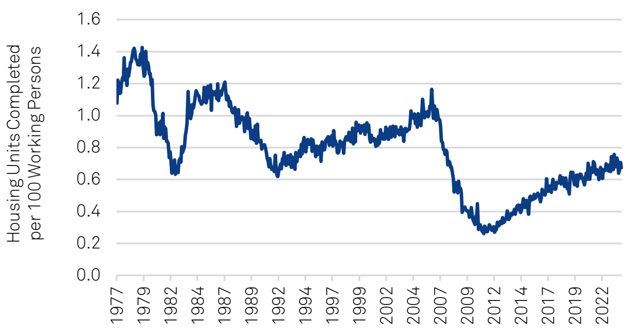
Focusing on Resilient Real Estate Fundamentals

Given our expectations for the broader economic setup in this coming year, it is particularly important to focus on identifying real estate investment opportunities with asymmetric payoffs to capture upside potential. These opportunities are underscored by identifying thematics we believe will drive positive real estate fundamentals – low supply and high demand – and by leveraging those thematics to deploy capital across high quality assets covering the residential, industrial, and retail sectors.

The National Housing Shortage

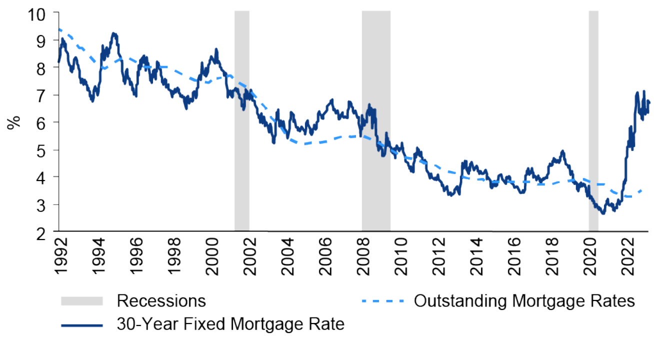
Total housing completions (for multi- and single-family homes) in relation to the working age population today are at the lowest level in a generation (Figure 1). Further exacerbating the structural undersupply of homes is the lock-in effect restricting existing home sales inventory levels due to outstanding mortgages at interest rates far below prevailing mortgage rates available today (Figure 2). Simultaneously, the demand for housing is increasing as the millennial cohort is aging into peak household formation years. Taken together, the housing market has remained resilient despite a historic rise in mortgage rates (Figure 3), resulting in the largest affordability gap between owning and renting a home in the current century, creating renters for longer (Figure 4).

Figure 1: Housing units completed per 100 working persons.



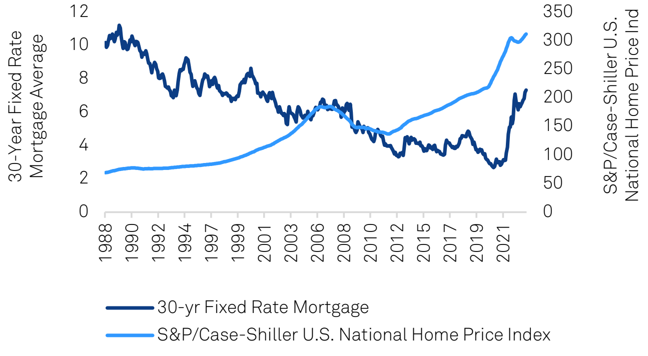
Source: Federal Reserve Bank of St. Louis, as of October 2023.

Figure 2: Average rate on outstanding mortgages and the current 30-year fixed mortgage rate.



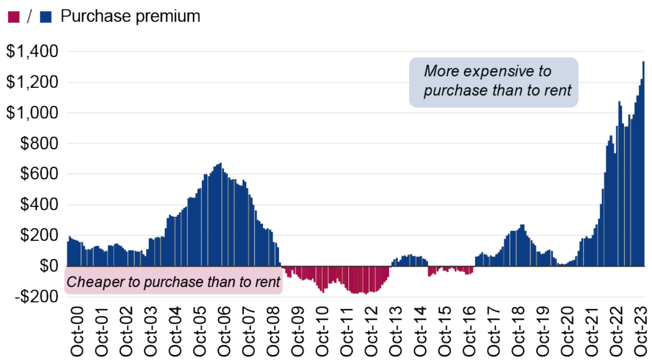
Source: Federal Reserve Bank of St. Louis, Empirical Research Partner's Analysis, as of June 2023.

Figure 3: Historical home prices and mortgage rates.



Source: Federal Reserve Bank of St. Louis, as of September 2023.

Figure 4: The homeownership premium is at historic highs.



Source: John Burns Research and Consulting, as of December 2023.

We maintain high conviction in deploying capital around this theme across various residential subsectors in the coming year:

- Purpose-Built Rental Communities – Partnering directly with national home builders, these purpose-built rental communities are helping address housing undersupply by adding new single-family housing units into the marketplace. This subsector of amenity-rich single-family rental communities, located in under-supplied suburban submarkets, is ideally suited for millennials aging into the single-family lifestyle, as well as baby boomers trying to move out of home-ownership responsibilities.

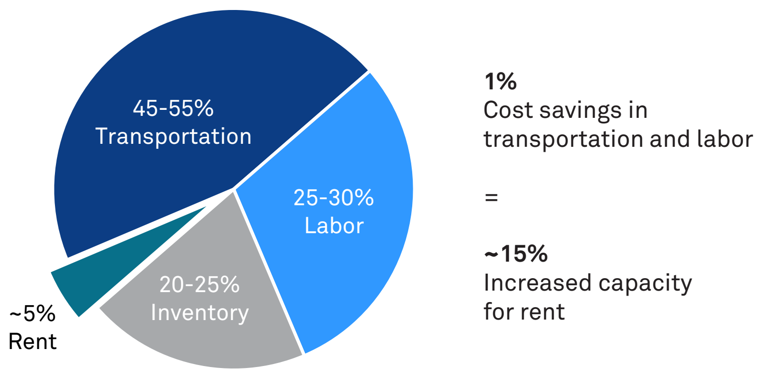
- Manufactured Housing Communities – Partnering directly with manufactured home community developers, these investment opportunities are focused on developing well-located affordable housing alternatives in high-growth suburban submarkets.

- Opportunistic Multifamily – As a function of exuberant underwriting in an era of cheap capital, core multifamily assets and development projects are likely to experience a reckoning as existing low-rate loans must be refinanced at prevailing interest rates, upending previous underwriting assumptions. Here, while the asset itself may not be troubled, the reconstitution of the capital stack is likely to provide opportunities for new investors.

Optimizing the Last Mile of the Supply and Service Chain

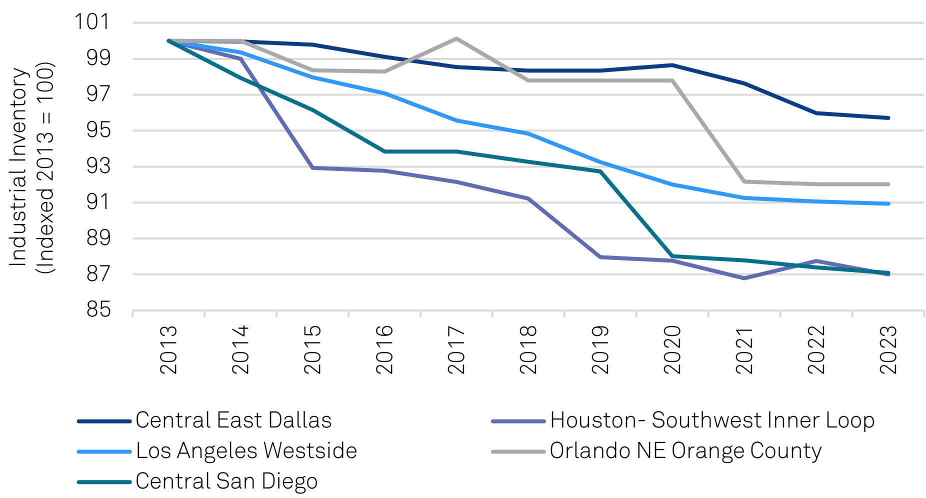
For years, retailers have focused on optimizing their supply chain for the last-mile delivery of goods to consumers. Industrial spaces in infill submarkets closest to the consumer have experienced strong pricing power as occupiers focus on optimizing costs across their entire supply chain, of which transportation and labor make up the largest components. In contrast, rent makes up only about five percent of their total cost structure (Figure 5). Strategically, these infill spaces have shifted from being considered simply "cost centers" to full-fledged value propositions for fulfilling last-mile logistics requirements for tenants. While demand has remained resilient for this product type, our target infill submarkets have experienced net negative supply as existing industrial spaces are converted to higher and better uses such as multifamily (Figure 6). Given the elevated levels of industrial supply nationally, we remain focused on product we believe has resilient demand and is insulated from competitive supply, especially as we anticipate an economic slowdown on the horizon.

Figure 5: Supply chain cost structure.



Source: Prologis, as of March 6, 2023.

Figure 6: Infill submarkets have seen negative supply of industrial product.



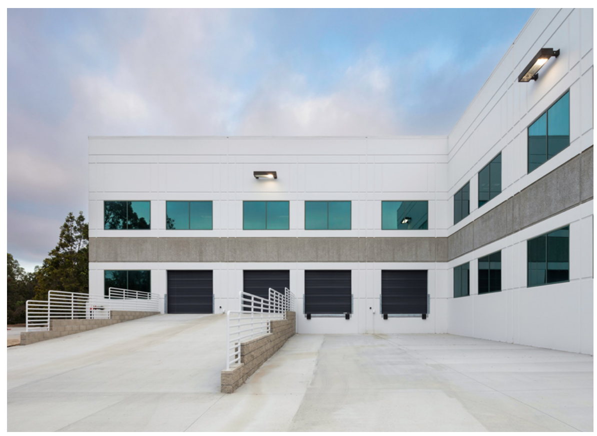
Source: CoStar, as of September 30, 2023.

As we look forward into the coming year, we believe the following subsectors across the industrial property type will provide compelling investment opportunities to deploy capital:

- **Service Industrial –** What we have coined as "service industrial" is a niche subsector that consists of shallow-bay multi-tenant industrial product in high-population growth infill submarkets with average tenant suite sizes below 5ksf and short lease duration. Tenants occupying these spaces typically provide services tailored to the surrounding market or submarket, such as HVAC contractors, auto repair technicians, suppliers, etc. – and their spaces are mission-critical for their business. Acquiring stabilized service industrial product in strong submarkets and institutionalizing operations to capture 30-70% or higher mark-to-market rents across the entire rent roll within three years offers a compelling value-add opportunity for investors today.

- **Value-Add Last-Mile Industrial –** While pricing for stabilized industrial product remains a challenge, there still lies an opportunity to deploy capital in traditional last-mile industrial product in the right submarket (i.e., with low vacancy and supply) with a value-add business plan such as the repositioning of excess corporate real estate into functional, class A last-mile distribution facilities.

- **Opportunistic Industrial –** Like multifamily, industrial at large has been a beloved property type for real estate investors, attracting an abundance of cheap capital for core and development deals that might not be functional at today's prevailing interest rates. As a result, we anticipate opportunities to participate in the reconstitution of not necessarily broken assets but broken capital structures across the industrial property type to arise.

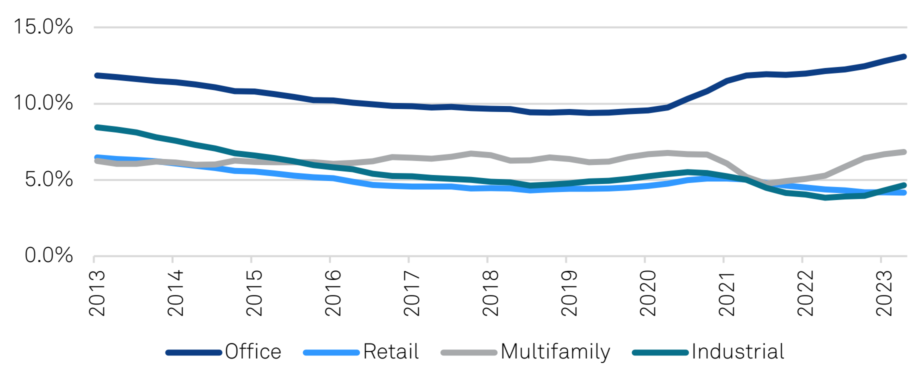


Following the Consumer

A decade into the technological disruption caused by e-commerce that has brought on many predictions concerning the death of retail real estate, the national retail vacancy rate currently sits at just 4.7% (Figure 7), which is the lowest among the "core" property types due to lack of new retail supply. Many regions have even experienced negative supply as older, obsolete centers have been redeveloped into multifamily or self-storage facilities. During that time, the U.S. population has grown, especially across sunbelt markets, resulting in retail productivity increasing significantly (Figure 8). As an outcome of these externalities, the retail sector finds itself in an unanticipated golden era of fundamentals, boasting record low vacancy rates, record high rental rates, and twelve quarters of positive absorption[1].

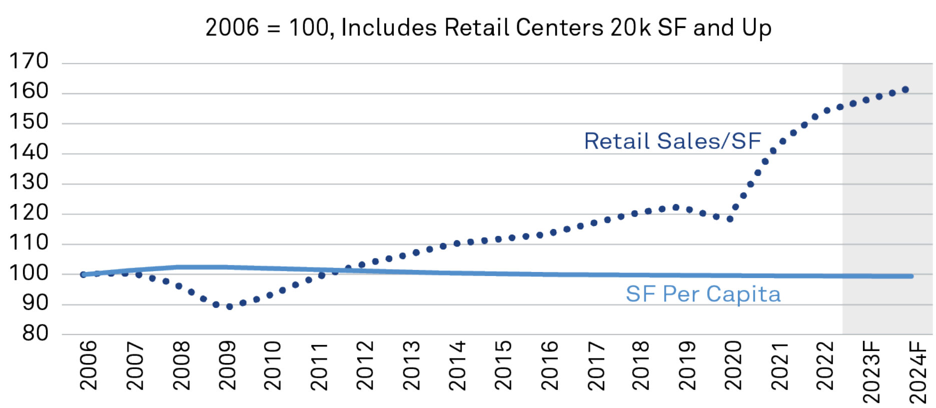
However, not all retail is created equal, and we anticipate the greatest opportunity for investors in the coming year is likely to be concentrated in neighborhood shopping centers, particularly in high-growth suburban submarkets with tenants focused on providing essential services. As investors look to redeploy proceeds and diversify away from traditional sectors such as office, we anticipate investors will revisit retail as a compelling investment opportunity. In fact, we recently published a white paper on the topic and invite you to explore the fundamentals driving our strong conviction for the retail sector [Revisiting Retail].

Figure 7: Vacany rates across core U.S. property sectors.



Source: CoStar, as of September 30, 2023.

Figure 8: Annual retail sales/sf and sf/capita.



Source: CoStar, St Louis FRED, CBRE Research, as of Q4, 2022. The above chart includes forward looking information. Actual results may be materially different.

[1] CoStar, as of September 30, 2023.

As we look forward into the coming year, we believe the following retail subsector will provide compelling investment opportunities to deploy capital:

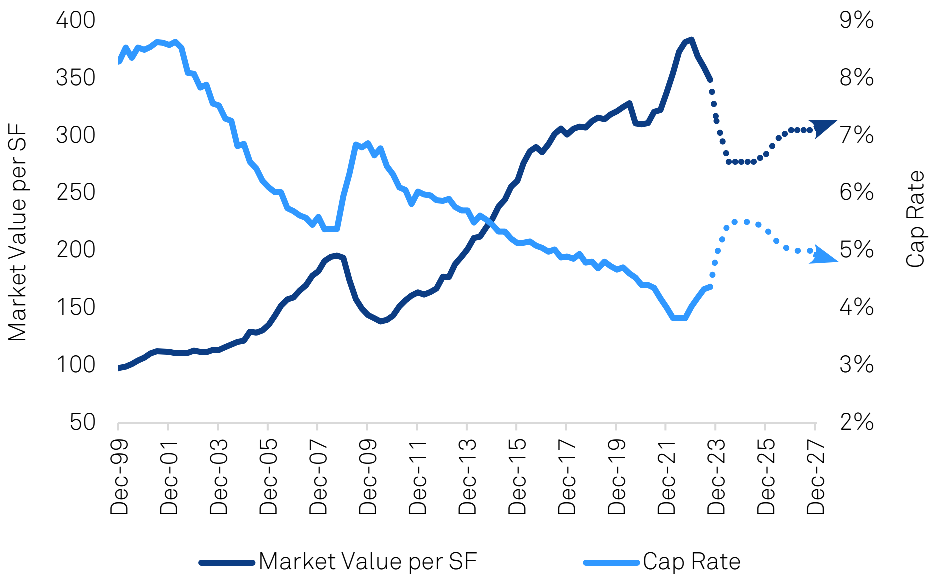
- **Essential Service Retail (ESR) –** Consumers are spending more dollars online and prefer services and experiences over goods. Essential Service Retail is comprised of e-commerce resistant tenants whose customers have to visit a physical location in order to consume the service (i.e., food and beverage, fitness, beauty, health and medical, and business services). ESR is a niche sector of retail that has been overlooked by institutional investors and offers attractive cap rates and strong fundamentals.

Capitalizing on Reset Valuations

When markets shift dramatically, as they have over the last year, transaction volumes plummet, only further exacerbating the delay with which these dynamics influence valuations across the private equity market. By comparison, forward-looking expectations are rapidly incorporated into the public market's implied pricing for real estate. While the public markets tend to overreact to shifts, their response provides directional guidance for private market valuations. By leveraging the implied cap rate of publicly traded REITs, we can gain beneficial insight, informing expectations for pricing across the private real estate market.

To start the year, cap rates across the U.S. REIT market were 5.7% while appraisal cap rates across the private market, as represented by the ODCE Index, were just at 4.25% as of the third quarter[2]. In our base case scenario, where we anticipate the 10-year treasury yield to settle somewhere near 4% for the foreseeable future, we believe that cap rates in the public market are more accurate, and real estate needs to be repriced across the private market. We anticipate the debt market will continue to drive this needed revaluation across the real estate sector, as highlighted in our 2024 Real Estate Debt Outlook. This revaluation, which has started to take shape in 2023, is likely to materialize more meaningfully throughout 2024, resetting the basis for investments made during this period of the real estate cycle (Figure 9).

Figure 9: U.S. Real Estate Market Cycles



Sources: NCREIF, CSIM, as of December 31, 2023.

There is growing confidence that we are at the end of the rate hiking cycle in the U.S., setting the stage for a critical period of price discovery and valuation reset across private real estate markets. This presents a unique opportunity for investors to deploy capital across high-quality assets at substantial discounts to replacement cost. Heading into 2024, we believe the winning strategy will be to identify asymmetric payoffs by maintaining a focus on resilient fundamentals and deploying capital at a reset basis. As market dynamics continue to unfold, investors able to adapt to these changes can strategically position themselves to succeed in what we see as one of the best investment eras of the past decade.

[2] Please refer to CenterSquare REIT Cap Rate Methodology at the end of this document.

About the Authors

Jeffrey Reder

Managing Director, Private Real Estate

Jeffrey Reder is a Managing Director in the Private Real Estate Group. He joined CenterSquare in 2006. As Managing Director – Private Real Estate, Jeff serves as a Portfolio Manager for i) the Value-Added Fund strategy and ii) a Separate Account relationship while overseeing a team focused on sourcing, underwriting, closing, financing and executing business plans for real estate transactions across a variety of property types nationwide. Jeff brings many years of experience in both real estate and investment banking to his position. Immediately prior to joining CenterSquare, he served as Vice President for a private real estate investment firm where he was responsible for underwriting acquisitions, financing, asset management and disposition of properties. Jeff began his career as an investment banker at Salomon Brothers in New York eventually leaving Wall Street as a Vice President of Corporate Finance before returning home to his native Southern California.

Jeff holds a B.A. in both Economics and Psychology from Northwestern University graduating magna cum laude. He is also professionally affiliated with the Urban Land Institute, International Council of Shopping Centers, National Association for Industrial and Office Parks and National Multi Housing Council. He serves as a member of the Investment Committee for CenterSquare's Private Real Estate and Essential Service Retail groups.

Robert Holuba

Managing Director, Private Real Estate

Rob Holuba serves as a Managing Director for CenterSquare's Essential Service Retail (ESR) Strategy. In this capacity he is responsible for leading all aspects of ESR equity and debt investments including the sourcing and acquisition of new investments, implementation of business plans, leasing agents and other third-party resources, and dispositions.

Prior to joining CenterSquare, Rob worked for Lubert-Adler Real Estate Partners performing acquisitions and investment management functions on behalf of the Lubert-Adler Real Estate Funds. Rob began his career at Apartment Investment Management Company (ticker: AIV) where he worked with the development finance team.

Rob holds a B.A. in History from Princeton University and an MBA from the McDonough School of Business at Georgetown University. He is an active member of ICSC and NAIOP and currently serves on CenterSquare's Private Real Estate Equity Investment Committee, the Associate Advisory Board for the Steers Center for Global Real Estate at Georgetown University and the Board of Directors for the Princeton Football Association.

Uma Moriarity, CFA

Senior Investment Strategist and Global ESG Lead

Uma Moriarity is the Senior Investment Strategist and Global ESG Lead for CenterSquare Investment Management. She focuses on investment strategy and leads thought leadership across the Firm's public and private real estate platforms. She is part of the listed real estate investment team and serves on CenterSquare's Private Real Estate Debt Investment Committee. Uma leads the Firm's Environmental, Social, and Governance (ESG) strategy to incorporate ESG into the decision-making and management of listed and private real estate investments to create long-term value, reduce risk, and generate superior risk-adjusted investment returns. Prior to joining CenterSquare, she spent three years in corporate strategy and planning at ExxonMobil in Houston. Uma graduated from The Pennsylvania State University with Interdisciplinary Honors and High Distinction and holds a B.S. in Finance with a minor in International Business, B.S. in Accounting, and Master of Accountancy. She is a CFA charterholder and member of the CFA Institute, a LEED Green Associate, and a member of the ULI San Francisco Sustainability Committee. She currently serves on the Board of Directors for Green Building United, the Penn State Smeal Sustainability Advisory Board, and the FTSE EPRA Nareit Americas Regional Advisory Committee.

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Definition of Indices

FTSE Nareit All Equity REITs Index "FNER"
The FTSE Nareit All Equity REITs Index is a free-float adjusted, market capitalization-weighted index of U.S. equity REITs. Constituents of the index include all tax-qualified REITs with more than 50 percent of total assets in qualifying real estate assets other than mortgages secured by real property.

This benchmark is a broad-based index which is used for illustrative purposes only. The investment activities and performance of an actual portfolio may be considerably more volatile than these indices and may have material differences from the performance of any of this index.

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A direct investment in an index is not possible.

CenterSquare REIT Cap Rate Perspective Methodology

CenterSquare REIT Implied Cap Rates are based on a proprietary calculation that divides a company's reporting net operating income ("NOI") adjusted for non-recurring items by the value of its equity and debt less the value of non-income producing assets. The figures above are based on Q4 2023 earnings reported in September 2023.

The universe of stocks used to aggregate the data presented is based on CenterSquare's coverage universe of approximately 200 U.S. listed real estate companies. Sector cap rates are market cap weighted. Sectors and market classifications are defined by the following:

Apartment: REITs that own and manage multifamily residential rental properties; Industrial: REITs that own and manage industrial facilities (i.e. warehouses, distribution centers); Office – REITs that own and manage commercial office properties; Retail – REITs that own and manage retail properties (i.e. malls, shopping centers); Hotel – REITs that own and manage lodging properties; Healthcare – REITs that own properties used by healthcare service tenants (i.e. hospitals, medical office buildings); Gateway – REITs with portfolios primarily in the Boston, Chicago, LA, NYC, SF, and DC markets; Non-Gateway – REITs without a presence in the gateway markets.

The REIT ODCE Proxy is a universe of REIT stocks built to resemble the NCREIF Fund Index – Open End Diversified Core Equity (ODCE). The ODCE, short for NCREIF Fund Index - Open End Diversified Core Equity, is the first of the NCREIF Fund Database products and is an index of investment returns reporting on both a historical and current basis the results of 36 open-end commingled funds pursuing a core investment strategy, some of which have performance histories dating back to the 1970s. The REIT ODCE Proxy is proprietary to CenterSquare and uses gateway/infill names in apartments, retail, industrial and office, and then weights them according to the ODCE index to create a proxy.

Private Market Cap Rates represent the cap rate achievable in the private market for the property portfolio owned by each company, and are based on estimates produced by CenterSquare's investment team informed by various market sources including broker estimates.

About CenterSquare

Founded in 1987, CenterSquare Investment Management is an independent, employee-owned real asset manager focused on listed real estate, private real estate equity and private real estate debt investments. As a trusted fiduciary, our success is firmly rooted in aligning our interests with those of our clients, partners and employees. CenterSquare is headquartered in suburban Philadelphia, with offices in New York, Los Angeles, London and Singapore. With approximately $13 billion in assets under management (December 31, 2023), our firm and subsidiaries are proud to manage investments on behalf of some of the world's most well-known institutional and private investors.

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