STIFEL

August 30, 2016

Real Estate
REITs

Market Commentary/Strategy

Funds Flows Update. Japanese Flows Strong. Generalist Investors the Key. SLIDES ATTACHED.

- *We will be hosting our year-to-date Funds Flows Update conference call tomorrow, Wednesday, August 31, at 11AM ET.*
  - *The Dial-in numbers are as follows: (888) 267-2848 (Domestic); (973) 413-6103 (International);*
  - *Conference ID #: 963578*
  - *The slide deck for this call is attached to the note, starting on page 2.*
  - *Replay dial-in information is as follows: (800) 332-6854 (Domestic); (973) 528-0005 (International);*
  - *Replay conference ID: 963578*
- *See our summary comments below and in the attached slide deck.*

SUMMARY

- Twice a year, we analyze the various types of funds flows including active and passively managed domestic mutual funds, exchange traded funds as well as Japanese funds flows into U.S. REITs.

- We do this to understand the funds flows overall and to project what may happen going forward.

CONCLUSIONS & RECOMMENDATIONS FOR INVESTORS

- Surprising strength of Japanese funds flows driven by domestic issues in Japan – appears steady – do not assume this changes

- Passive – index funds and ETFs – growing in dollar terms, and in 2016 as a percent of AUM – performance driven

- Per Jan. 15 – July 16 funds flows active managers (-$7.1B) likely sold holdings in 50-60 core REITs while passive managers ($10.8B) acquired 150 REITs on a market cap weighted basis

- Funds flows coming from yield and stock metrics-oriented investors rather than investors with a NAV bias

- Absent any material changes in global debt/equity markets, we expect these trends to continue

CONCLUSIONS & RECOMMENDATIONS FOR REIT MANAGEMENTS

- Increase the dividend

- Be mindful of ALL valuation metrics

- Net asset value metric is important to REIT-dedicated investors, but often ignored by generalist investors

- Complexity is the enemy; ‘Simplicity premiums’ are real

- Get to know the “ETF portfolio managers” (we jest . . .)

Prices within are as of the close 8/29/16 unless otherwise noted.

John W. Guinee	jwguinee@stifel.com	(443) 224-1307
Erin T. Aslakson	aslaksone@stifel.com	(443) 224-1350
Kyle E. McGrady	mcgradyk@stifel.com	(443) 224-1517
Stifel Equity Trading Desk		(800) 424-8870

All relevant disclosures and certifications appear on pages 21 - 22 of this report.

Funds Flows

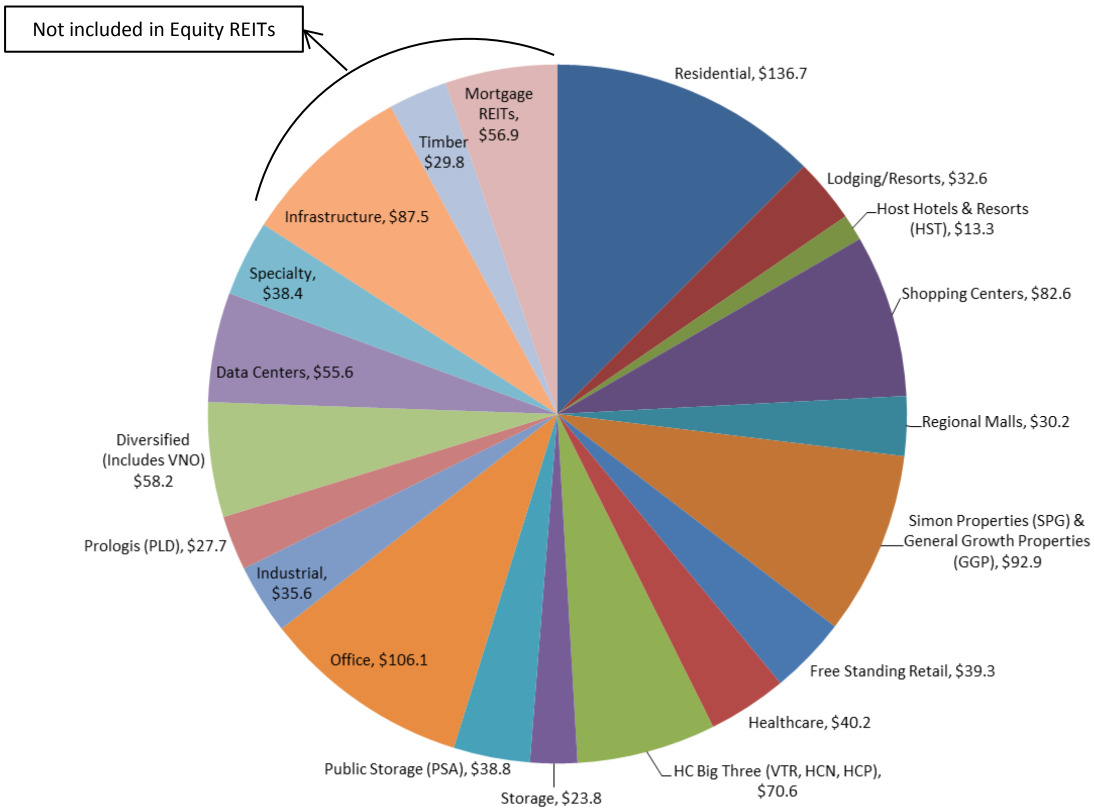
Ownership Concentration

August 2016

(Data through July 31, 2016)

REIT Universe

	All REITs	All Equity REITs	Equity REITs
Market Cap	$1,097B	$1,040B	$923B
Constituents	202	165	156



Source: NAREIT, FactSet Research
Data as of 7/29/2016; all $ in Billions

Where are REITs and Real Estate?

January 2015	August 2016	*January 2017*
➢ 10-year Treasury at +/- 2.10% with range bound forecast	➢ 10-year Treasury at 1.60% with neutral to downward bias	➢ *10-year Treasury at 1.50% with neutral to downward bias*
➢ Private Investors have cost of capital advantage	➢ Private investors have cost of capital advantage	➢ *Private investors still have a cost of capital advantage*
➢ Cap rates declining; all asset quality levels	➢ Cap rates bottomed in 3Q15, bidder pools thinning and cap rates have, depending on asset quality, moved up 0-100 bps	➢ *Cap rates expected to decrease for core assets, but may increase for lower quality assets*
➢ Spread investing perceived as 'difficult'	➢ Spread investing limited to select REITs; few REITs are actively acquiring	➢ *Spread investing limited to REITs with sizeable NAV premium and acquisition strategy*
➢ Risk-off trade globally; yield matters	➢ Real estate is late in its cycle for most property types	➢ *Increasingly late in the real estate cycle*
➢ Generalists involved, but reluctant	➢ Generalists, Japanese and ETFs are the incremental investors	➢ *Commitment of these incremental investors is of concern*

Source: Stifel Research

Funds Flows Overview

- Domestic REIT Dedicated Inflows – Mutual Funds and ETFs

($ in Billions)	2010	2011	2012	2013	2014	2015	YTD 2016
Mutual Funds							
ACTIVELY MANAGED	**$2.5**	**$3.2**	**$2.9**	**$3.4**	**$1.2**	**($5.0)**	**($2.1)**
Passive (Index)	$0.7	$1.0	$2.2	$3.1	$3.2	$1.8	$1.6
Exchange Traded Funds	$1.5	$3.2	$8.1	$2.9	$6.4	$1.0	$6.4
	$4.6	$7.4	$13.2	$9.5	$10.8	($2.2)	$5.9

Assumes 50% of global funds flows invested domestically

Source: Morningstar, Stifel estimates

- Domestic Institutional – Modest REIT interest due to late real estate cycle; but potential for a flattening yield curve causing renewed interest – albeit via passive strategies

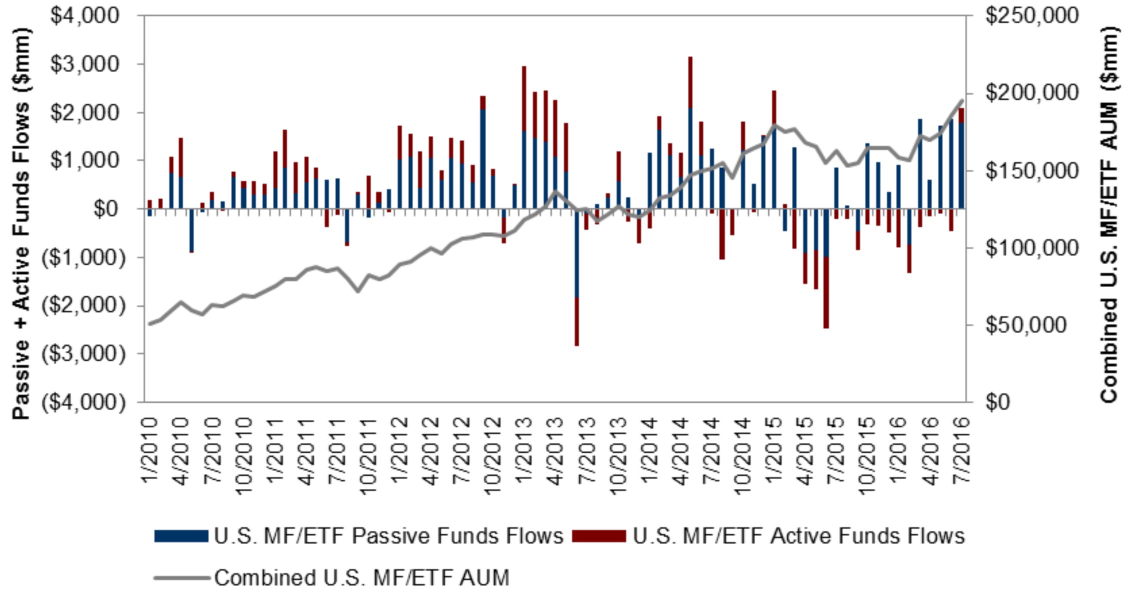
- Global Institutional – flight to safety; principal protection-oriented; countervailing force - fewer petro-dollars available

- Global Individual – Japanese funds flows very strong while flows from other nations remain minor

**Data above may not sum exactly due to rounding*

Domestic Funds Flows (FF) and Assets Under Management (AUM) Since Jan 2010

($B)	2010	2011	2012	2013	2014	2015	YTD 2016
U.S. MF/ETF Funds Flows	$4.6	$7.4	$13.2	$9.5	$10.8	($2.2)	$5.9

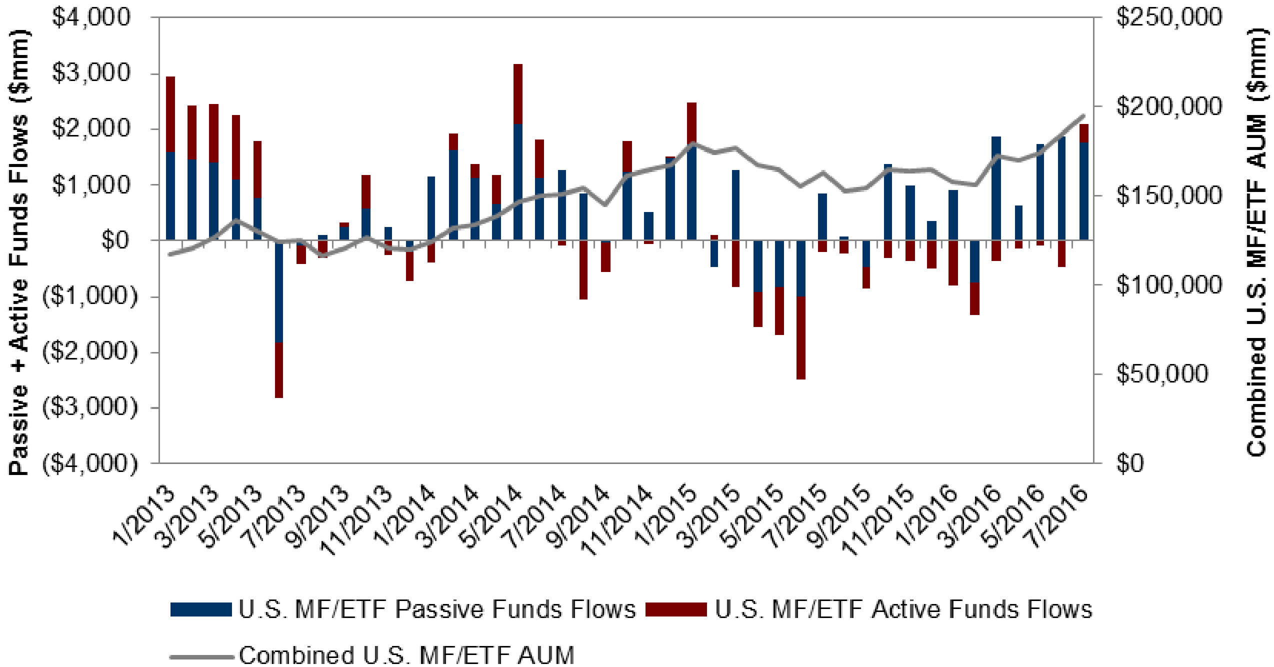


Source: Morningstar, Stifel estimates

- AUM increased from $52B in January 2010 to $165B at peak in Jan. 2015 (221%)
- As of July 2016, AUM has climbed to a new peak of $195B.
- Net outflows for a full year last occurred in 2007 when outflows totaled ($600mm)
- Funds Flow volatility is increasing
- From Jan. 2010 – July 2014, 9/55 months posted net negative Funds Flows
- August 2014-July 2016 10/24 months posted net negative Funds Flows

Domestic FF and AUM Since Jan. 2013

($B; Trailing X Mo's)	T12M Thru July 2016	T6M Thru July 2016
U.S. MF/ETF Funds Flows	$6.5	$5.8



Source: Morningstar, Stifel estimates

- From Jan. 2015-July 2016, actively managed funds saw ($7.1B) of outflows
- Over the same period, passive mutual funds and ETFs had $11.0B of inflows
- Overall, AUM of $155B in June 2015 increased to $195B in July 2016; up 26%

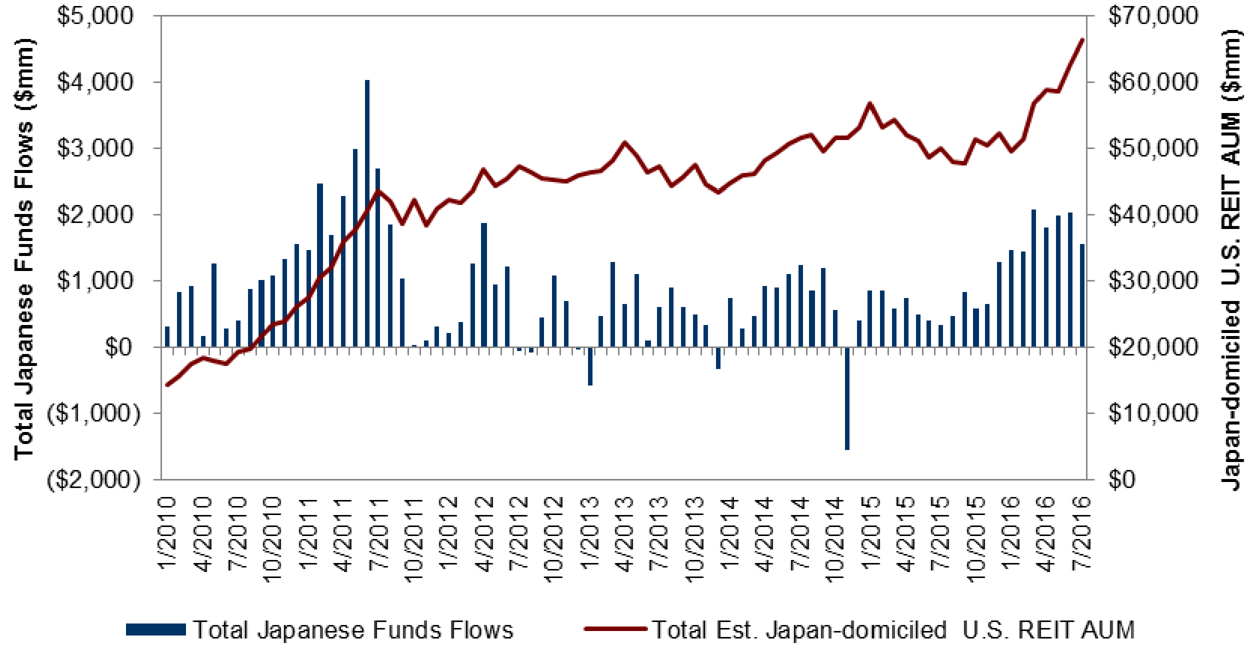
Japanese Individual Investor Summary

- Assets Under Management - $66.5B as of July 2016
  - 11 primary U.S. or Global REIT Funds exceeded $500mm of estimated U.S. AUM
- Sold through Japanese financial institutions to “Mr. & Mrs. Watanabe”
  - Yield critical, few alternatives
  - Know ‘dividend’ = return of capital as well
  - ‘Real net dividend’ of 2% will not sell
- Stated ‘dividend yield’ of 16%-33% in 2009-2010
  - Unlevered with reserves
  - Dividends or distributions paid monthly
- Able to pay ‘dividend’ via:
  - 17% average REIT total return 2010 – 2014
- ‘Dividend’ cuts started 2H11
  - Caused severe decline in funds flows
  - The weighted average dividend yield has averaged **18.3%** since January 2015
- Alternative investment environment
  - “Abenomics” commenced in 2013 but has yet to lift the Japanese economy
  - Aging population and few options for yield domestically
  - REITs appear to be an easy sale for Japanese financial advisors
- Primary risk:
  - Dividend cuts resulting in negative funds flows
  - Changes in domestically-driven Japanese investor sentiment

Source: Morningstar, Stifel estimates

Japanese FF and AUM Since January 2010

($B)	2010	2011	2012	2013	2014	2015	YTD 2016
Japanese Funds Flows	$10.1	$21.0	$8.0	$5.7	$7.2	$8.1	$12.4

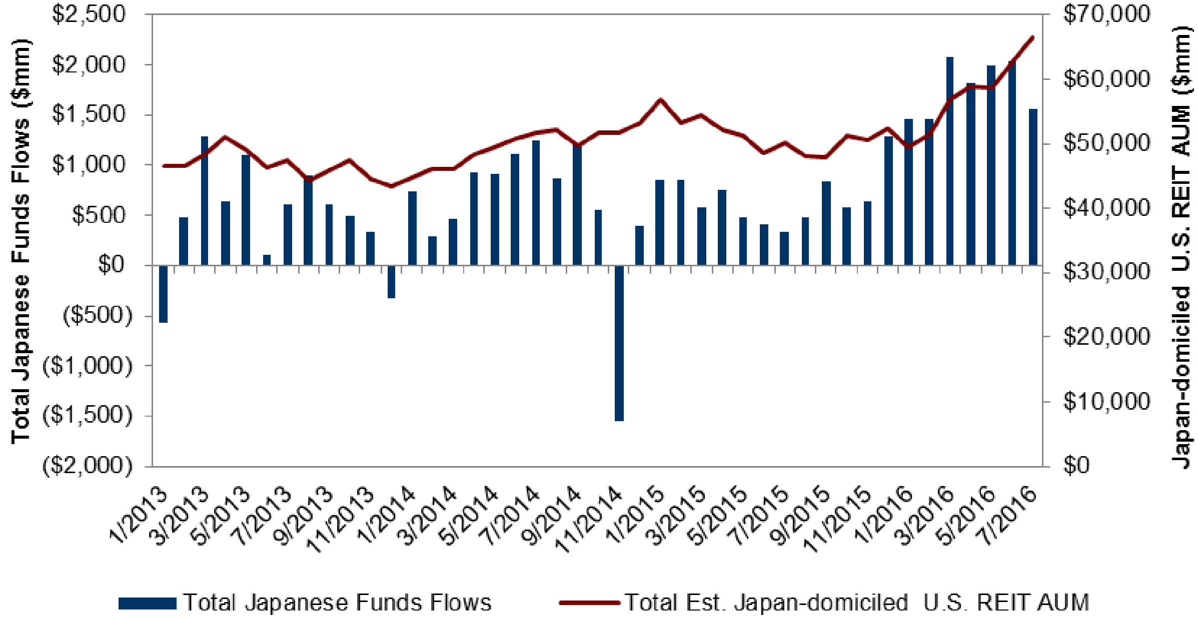


Source: Morningstar, Stifel estimates

- AUM increased from $15B in Jan. 2010 to $41B by June 2011; up $26B in 18 months
- Early cycle Japanese inflows helped spur the REIT recovery
- Constantly positive FF since June 2011; $41B of AUM increased to $52B by Dec. 2015
- 15%+ dividend (distribution, paid monthly) makes growing AUM difficult
- Additional monetary easing in Japan has spurred REIT inflows

Japanese FF and AUM Since Jan. 2013

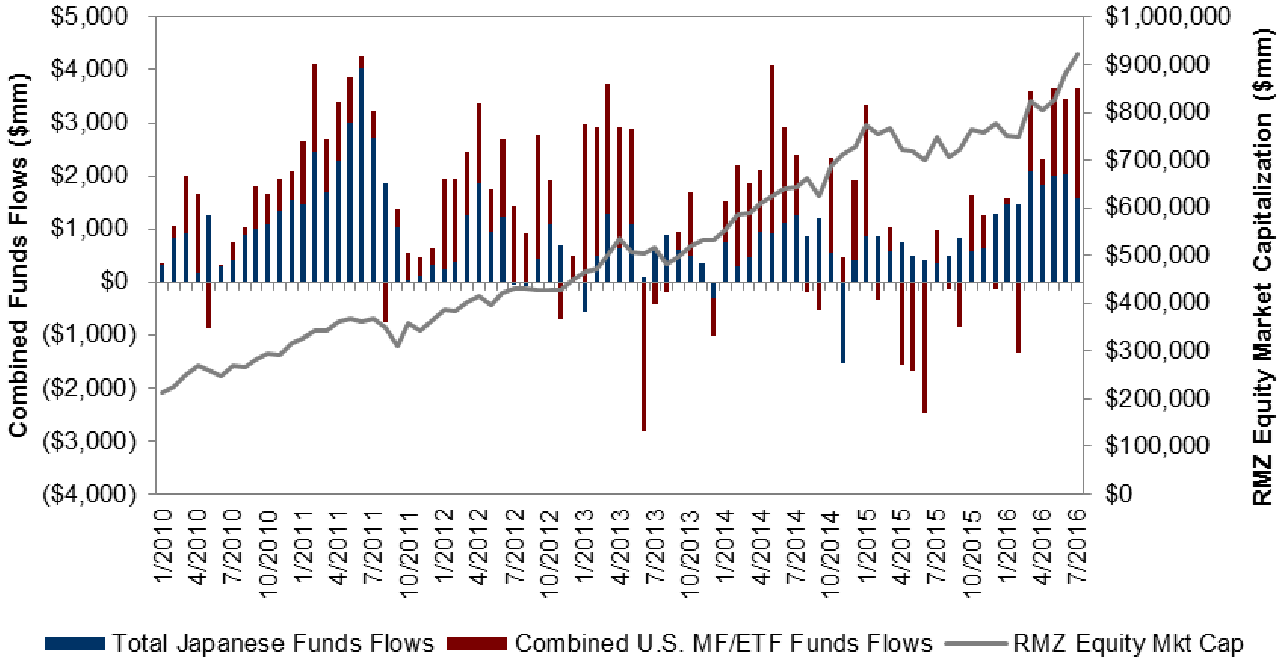
($B; Trailing X Mo's)	T12M Thru July 2016	T6M Thru Feb 2016
Japanese Funds Flows	$16.3	$11.0



Source: Morningstar, Stifel estimates

- FF from Japan slowed to a trickle by June 2015 and ramped dramatically since then
- $12.4B of Japanese FF through July 2016; Annualized, that equates to $21.3B
- Peak to peak (Jan. 2015-July 2016), AUM has increased $10B while funds flows totaled $20B
- Resulting from a 13.6% increase in the RMS REIT index less an average 18.3% distribution
- Over the same period, the U.S. Dollar has declined (12.7%) vs the Yen

Combined Domestic & Japanese Funds Flows and AUM



Source: Morningstar, Stifel estimates

- The RMZ equity market cap ranged from $700-$775B in 2015; now at $923B
- The RMZ EMC has climbed $148B in 2016; appreciation plus inflows
- For 2015 and YTD 2016, domestic U.S. inflows were $3.7B while Japanese inflows were $20.5B
- A reflection of subdued interest rate expectations in the U.S. and capital flight out of Japan

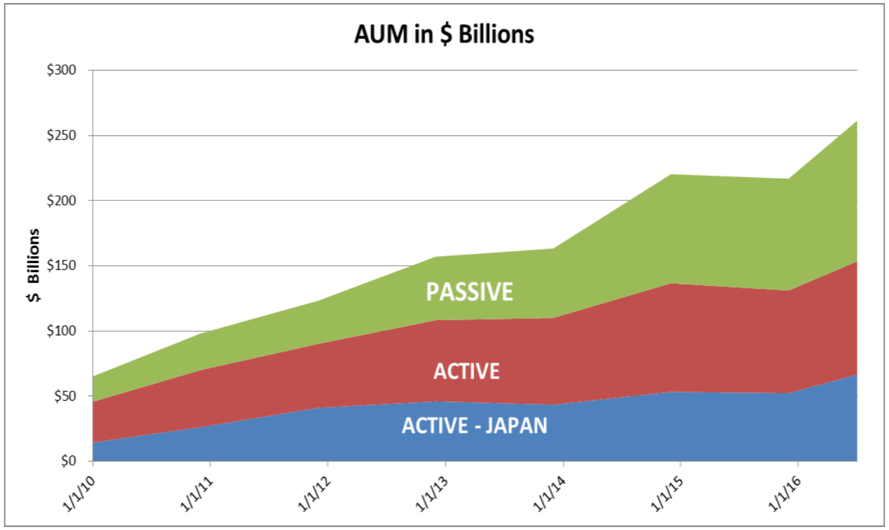
AUM as a Percentage of RMZ Market Capitalization

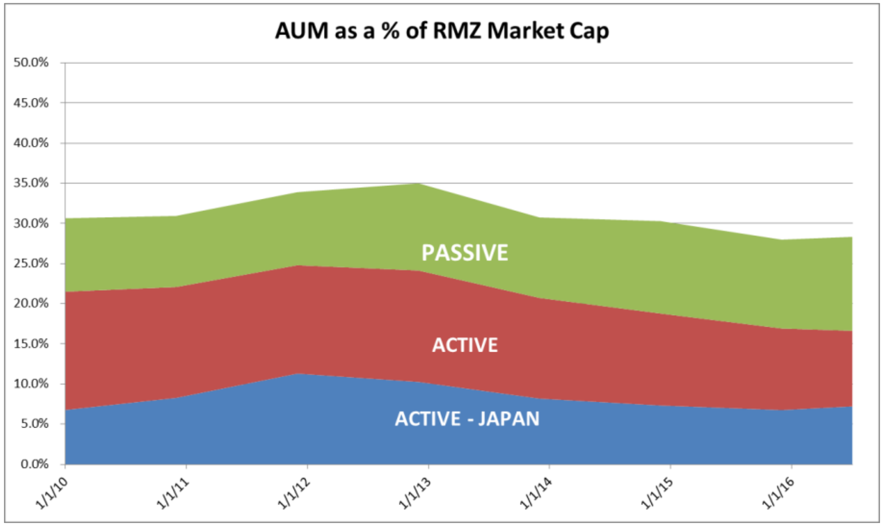
	1/29/10	12/31/10	12/30/11	12/31/12	12/31/13	12/31/14	12/31/15	7/29/16
RMZ Equity Market Capitalization ($ Billions)	**$212**	**$317**	**$363**	**$449**	**$531**	**$727**	**$775**	**$923**
Japan-Domiciled U.S. REIT AUM **(ACTIVE)**	6.8%	8.3%	11.3%	10.3%	8.2%	7.3%	6.7%	7.2%
U.S. MF/ETF AUM **(ACTIVE)**	14.7%	13.8%	13.5%	13.9%	12.5%	11.5%	10.2%	9.4%
U.S. MF/ETF AUM **(PASSIVE)**	9.1%	8.9%	9.1%	10.9%	10.0%	11.5%	11.1%	11.7%
All Three Combined	30.7%	31.0%	33.9%	35.0%	30.8%	30.3%	28.0%	28.3%

Source: Morningstar, Stifel estimates

- Japanese funds flows peaked in 2Q11, while AUM as a percentage of the RMZ market cap peaked in 2H11
- Strong funds flows from Japan returned in 2016; AUM as a percentage of the RMZ is on the rise
- Active AUM as a percentage of the RMZ market cap peaked in September 2011
- Passive (Index and ETF) AUM as a percentage of the RMZ market cap has been rising steadily
- Combined, AUM in these buckets declined from 35% at YE12 to 28.3% in July 2016

Passive and Actively Managed AUM Comparison



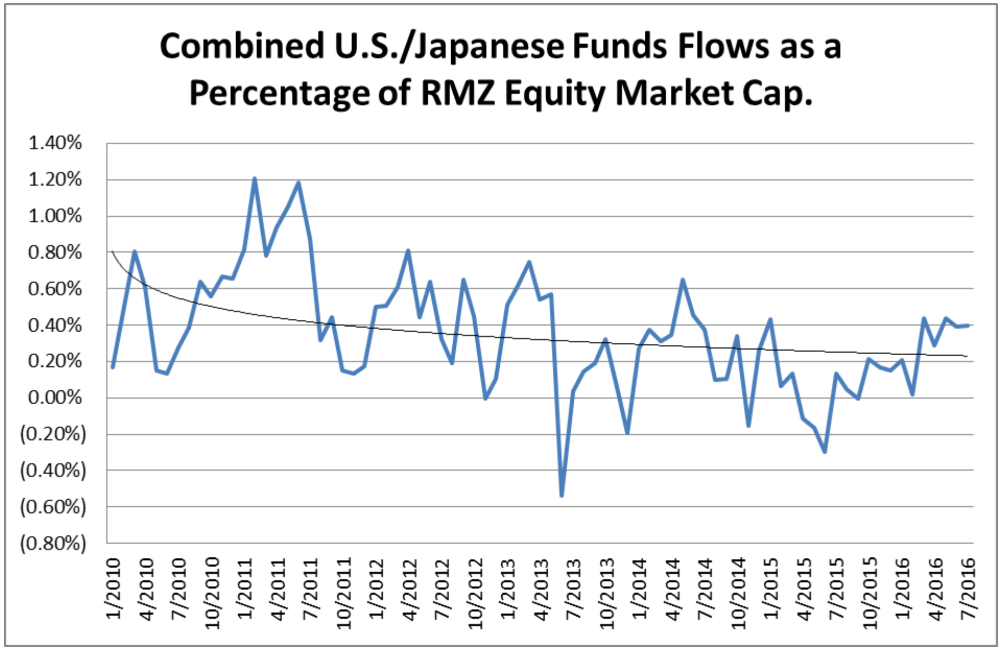


Sources for both charts: Morningstar, Stifel estimates

- REIT-dedicated AUM growing in dollar terms
- REIT-dedicated AUM as a percentage of the RMZ may have bottomed at 28% in early 2016
- Japanese and passive funds as a percentage of RMZ AUM are climbing
- Actively managed funds as a percentage of RMZ AUM – mostly in decline since 2011

Combined Funds Flows vs RMZ EMC

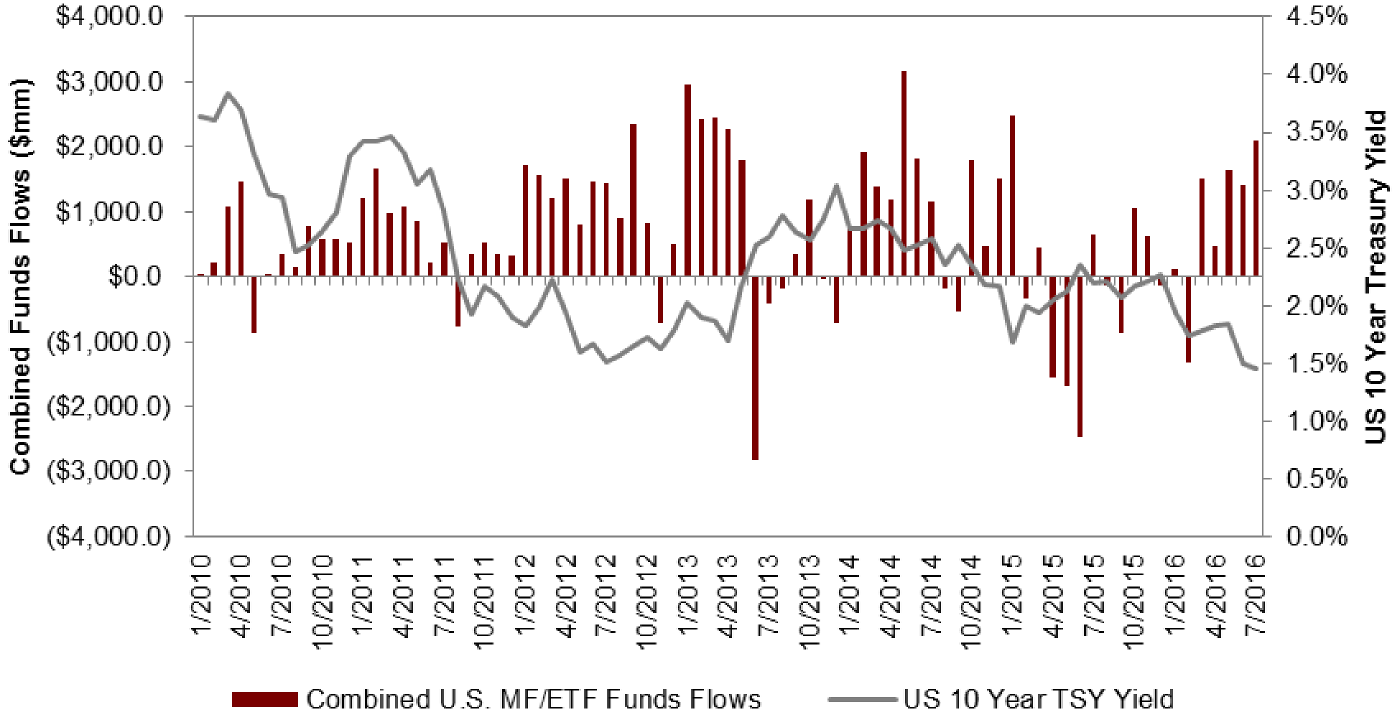
($B; Trailing 12 Mo's)	2010	2011	2012	2013	2014	2015	2016 FF YTD Annualized
Combined U.S. MF/ETF & Japanese Funds Flows	$14.7	$28.5	$21.2	$15.2	$18.0	$5.9	$31.5



Source: Morningstar, Stifel estimates

- Combined Funds Flows have averaged $1.6B/month since 2010
- Peaked at > 1% of the RMZ equity market cap in 1H11
- Volatility increased in 2015, resulting in little net funds flow impact
- The $31.5B of YTD funds flows annualized hypothetically exceeds $28.5B in 2011

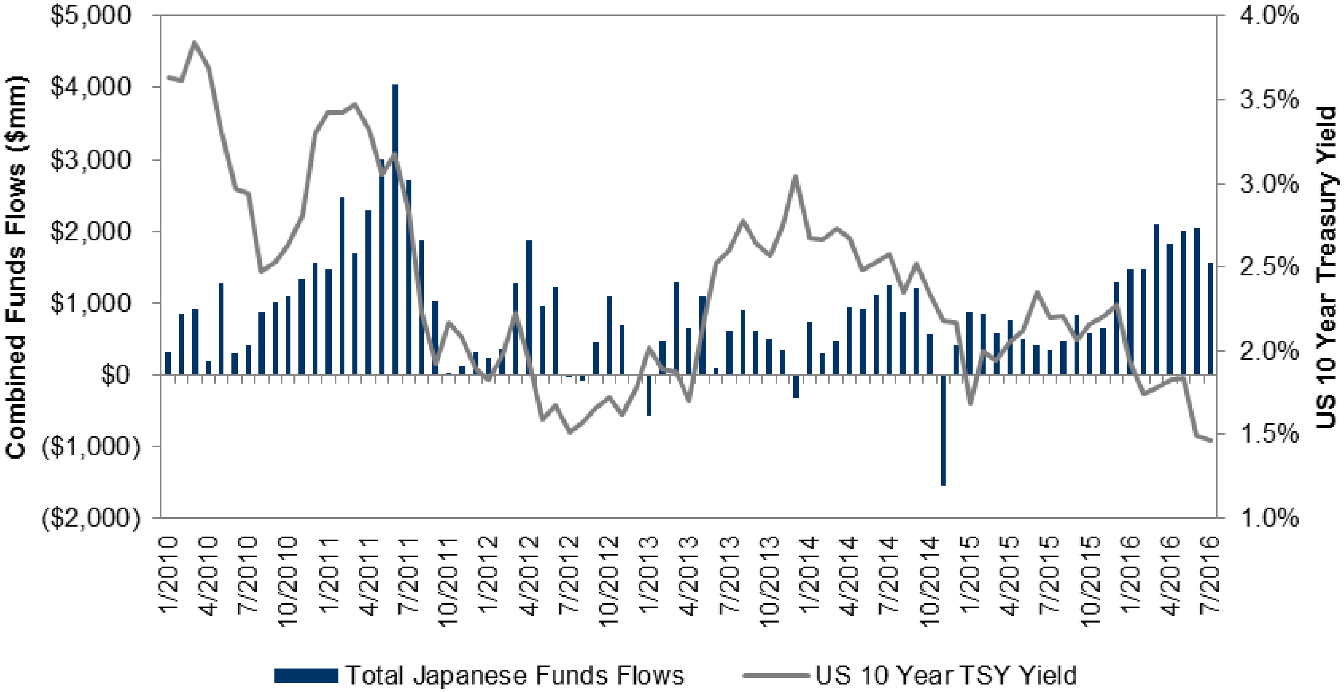
Domestic U.S. FF vs. the 10-Year Treasury



Source: Morningstar, Stifel estimates

- Funds flows Jan. 2010 – Dec. 2012 had little correlation – driven by fundamentals
- U.S. funds flows in REITs have been quick to turn negative when interest rate expectations shift (June-August 2013), debt capital markets tighten (April-June 2015)
- The RMS with a ~3.7% yield remains attractive in a low and negative global yield environment

Japanese FF vs. the 10-Year Treasury

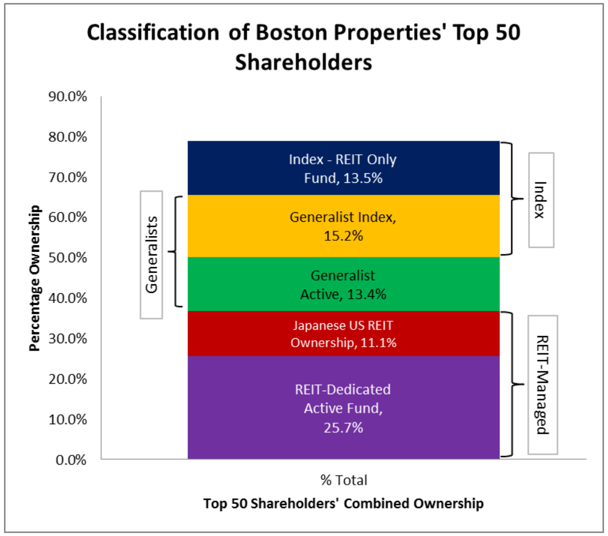


Source: Morningstar, Stifel estimates

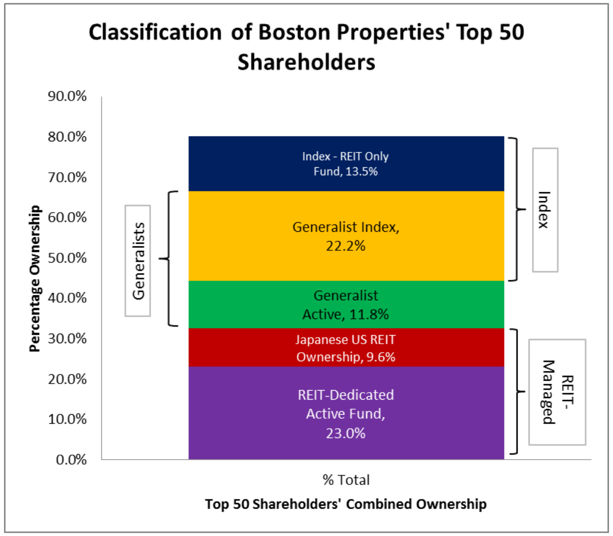
- Little correlation to the 10 year U.S. Treasury – until 2016
- Yield enhanced, sold product
- We believe Japanese funds flows into U.S. REITs are driven primarily by domestic issues in Japan
- And strong funds flows from yield-oriented investors helped “yield rally” in 2016

REIT Ownership Concentrated (BXP)

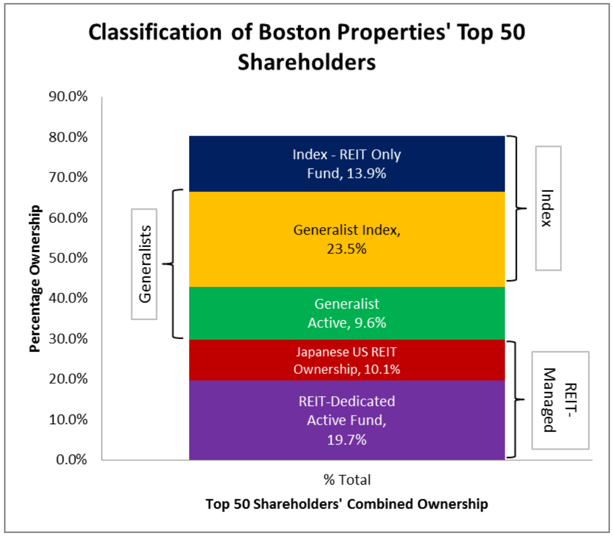
Report Date: 9/30/14



Report Date: 12/31/15



Report Date: 6/30/16

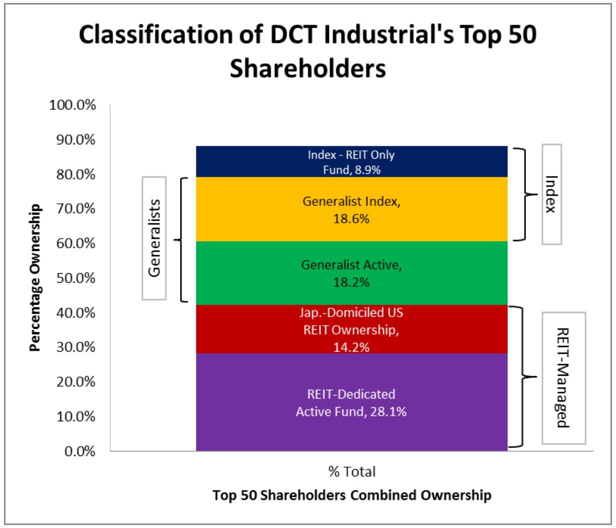


Source: FactSet Research Systems, Stifel estimates

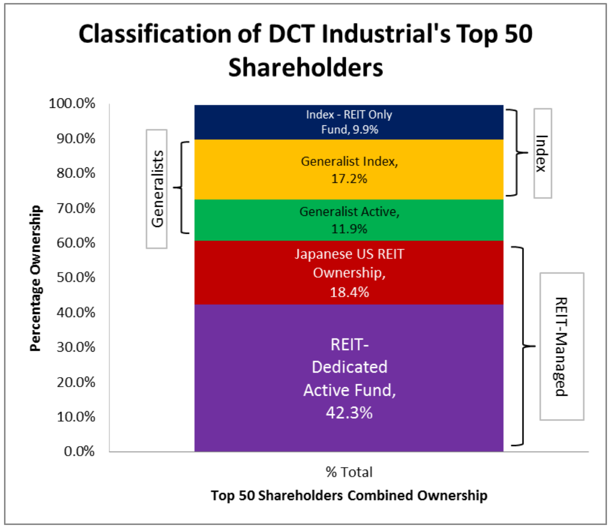
- Typical S&P 500 Stock Top 50 owns 40-45% and Index of 15-20%
- Top 50 shareholders own nearly 80% of all shares of Boston Properties
- Three “active” investor groups declining in ownership
- Index ownership is now over 37%

REIT Ownership Concentrated (DCT)

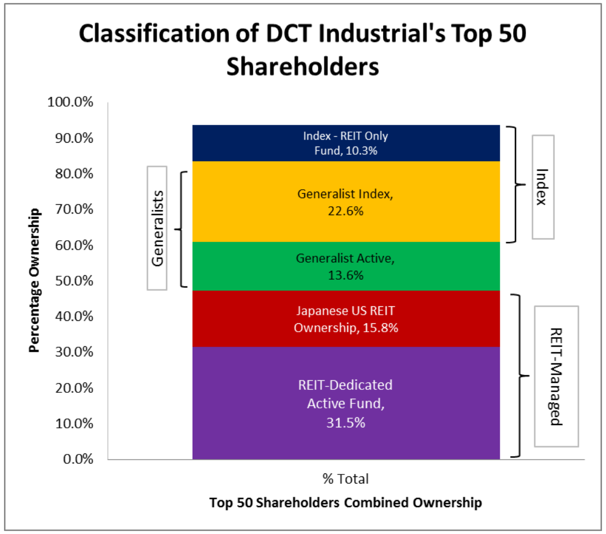
Report Date: 9/30/14



Report Date: 12/31/15



Report Date: 6/30/16



Source: FactSet Research Systems, Stifel estimates

- Top 50 shareholders own 95% of all shares of DCT Industrial
- REIT-dedicated investors ownership has changed dramatically
- Generalist active ownership of DCT increased by over 500 bps in six months

--- Investors ---
Conclusions & Recommendations

- Surprising strength of Japanese funds flows driven by domestic issues in Japan – appears steady – do not assume this changes
- Passive – index funds and ETFs – growing in dollar terms, and in 2016 as a percent of AUM – performance driven
- Per Jan. 15 – July 16 funds flows active managers (-$7.1B) likely sold holdings in 50-60 core REITs while passive managers ($10.8B) acquired 150 REITs on a market cap weighted basis
- Funds flows coming from yield and stock metrics-oriented investors rather than investors with a NAV bias
- Absent any material changes in global debt/equity markets, we expect these trends to continue

--- REIT Management Teams --- Conclusions & Recommendations

- Increase the dividend
- Be mindful of ALL valuation metrics
- Net asset value metric is important to REIT-dedicated investors but often ignored by generalist investors
- Complexity is the enemy; ‘Simplicity premiums’ are real
- Get to know the “ETF portfolio managers” (we jest . . .)

Important Disclosures and Certifications

I, John W. Guinee, certify that the views expressed in this research report accurately reflect my personal views about the subject securities or issuers; and I, John W. Guinee, certify that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this research report. Our European Policy for Managing Research Conflicts of Interest is available at www.stifel.com.

The equity research analyst(s) responsible for the preparation of this report receive(s) compensation based on various factors, including Stifel's overall revenue, which includes investment banking revenue.

Our investment rating system is three tiered, defined as follows:

BUY -We expect a total return of greater than 10% over the next 12 months with total return equal to the percentage price change plus dividend yield.

HOLD -We expect a total return between -5% and 10% over the next 12 months with total return equal to the percentage price change plus dividend yield.

SELL -We expect a total return below -5% over the next 12 months with total return equal to the percentage price change plus dividend yield.

Occasionally, we use the ancillary rating of **SUSPENDED** (SU) to indicate a long-term suspension in rating and/or target price, and/or coverage due to applicable regulations or Stifel policies. **SUSPENDED** indicates the analyst is unable to determine a "reasonable basis" for rating/target price or estimates due to lack of publicly available information or the inability to quantify the publicly available information provided by the company and it is unknown when the outlook will be clarified. **SUSPENDED** may also be used when an analyst has left the firm.

Of the securities we rate, 49% are rated Buy, 42% are rated Hold, 3% are rated Sell and 6% are rated Suspended.

Within the last 12 months, Stifel or an affiliate has provided investment banking services for 15%, 7%, 0% and 13% of the companies whose shares are rated Buy, Hold, Sell and Suspended, respectively.

Additional Disclosures

Please visit the Research Page at www.stifel.com for the current research disclosures and respective target price methodology applicable to the companies mentioned in this publication that are within Stifel's coverage universe. For a discussion of risks to target price please see our stand-alone company reports and notes for all Buy-rated and Sell-rated stocks.

The information contained herein has been prepared from sources believed to be reliable but is not guaranteed by us and is not a complete summary or statement of all available data, nor is it considered an offer to buy or sell any securities referred to herein. Opinions expressed are subject to change without notice and do not take into account the particular investment objectives, financial situation or needs of individual investors. Employees of Stifel, or its affiliates may, at times, release written or oral commentary, technical analysis or trading strategies that differ from the opinions expressed within. Past performance should not and cannot be viewed as an indicator of future performance.

As a multi-disciplined financial services firm, Stifel regularly seeks investment banking assignments and compensation from issuers for services including, but not limited to, acting as an underwriter in an offering or financial advisor in a merger or acquisition, or serving as a placement agent in private transactions.

Affiliate Disclosures

"Stifel", includes Stifel Nicolaus & Company ("SNC"), a US broker-dealer registered with the United States Securities and Exchange Commission and the Financial Industry National Regulatory Authority and Stifel Nicolaus Europe Limited ("SNEL"), which is authorized and regulated by the Financial Conduct Authority ("FCA"), (FRN 190412) and is a member of the London Stock Exchange.

Registration of non-US Analysts: Any non-US research analyst employed by SNEL contributing to this report is not registered/qualified as a research analyst with FINRA and is not an associated person of the US broker-dealer and therefore may not be subject to FINRA Rule 2241 or NYSE Rule 472 restrictions on communications with a subject company, public appearances, and trading securities held by a research analyst account.

Country Specific and Jurisdictional Disclosures

United States: Research produced and distributed by SNEL is distributed by SNEL to "Major US Institutional Investors" as defined in Rule 15a-6 under the US Securities Exchange Act of 1934, as amended. SNEL is a non-US broker-dealer and accordingly, any transaction by Major US Institutional Investors in the securities discussed in the document would need to be effected by SNC. SNC may also distribute research prepared by SNEL directly to US clients that are professional clients as defined by FCA rules. In these instances, SNC accepts responsibility for the content. Research produced by SNEL is not intended for use by and should not be made available to retail clients, as defined by the FCA rules.

Canadian Distribution: Research produced by SNEL is distributed in Canada by SNC in reliance on the international dealer exemption. This material is intended for use only by professional or institutional investors. None of the investments or investment services mentioned or described herein is available to other persons or to anyone in Canada who is not a “permitted client” as defined under applicable Canadian securities law.

UK and European Economic Area (EEA): This report is distributed in the EEA by SNEL, which is authorized and regulated in the United Kingdom by the FCA. In these instances, SNEL accepts responsibility for the content. Research produced by SNEL is not intended for use by and should not be made available to non-professional clients.
The complete preceding 12-month recommendations history related to recommendation(s) in this research report is available at https://stifel2.bluematrix.com/sellside/MAR.action

Brunei: This document has not been delivered to, registered with or approved by the Brunei Darussalam Registrar of Companies, Registrar of International Business Companies, the Brunei Darussalam Ministry of Finance or the Autoriti Monetari Brunei Darussalam. This document and the information contained within will not be registered with any relevant Brunei Authorities under the relevant securities laws of Brunei Darussalam. The interests in the document have not been and will not be offered, transferred, delivered or sold in or from any part of Brunei Darussalam. This document and the information contained within is strictly private and confidential and is being distributed to a limited number of accredited investors, expert investors and institutional investors under the Securities Markets Order, 2013 ("Relevant Persons") upon their request and confirmation that they fully understand that neither the document nor the information contained within have been approved or licensed by or registered with the Brunei Darussalam Registrar of Companies, Registrar of International Business Companies, the Brunei Darussalam Ministry of Finance, the Autoriti Monetari Brunei Darussalam or any other relevant governmental agencies within Brunei Darussalam. This document and the information contained within must not be acted on or relied on by persons who are not Relevant Persons. Any investment or investment activity to which the document or information contained within is only available to, and will be engaged in only with Relevant Persons.

In jurisdictions where Stifel is not already licensed or registered to trade securities, transactions will only be affected in accordance with local securities legislation which will vary from jurisdiction to jurisdiction and may require that a transaction carried out in accordance with applicable exemptions from registration and licensing requirements. Non-US customers wishing to effect transactions should contact a representative of the Stifel entity in their regional jurisdiction except where governing law permits otherwise. US customers wishing to effect transactions should contact their US salesperson.

The recommendation contained in this report was produced at 30 August 2016 17:07EDT and disseminated at 30 August 2016 17:07EDT

Additional Information Available Upon Request