CI GLOBAL REIT FUND

Commentary

MARCH 31, 2024

PERFORMANCE SUMMARY

For the quarter ended March 31, 2024 the CI Global REIT Fund (Class F) returned 0.40% net of fees.

Contributors to performance: Tricon Residential, Host Hotels, and American Homes 4 Rent were the top individual contributors to fund performance in the quarter.

Detractors from performance: Ventas, American Tower, and Axia Grocery Net Lease were the top individual detractors to fund performance in the quarter.

MARKET SUMMARY AND PORTFOLIO ACTIVITY

Broader stock benchmarks have shown reasonably strong performance year-to-date (YTD). From year-end 2023 to quarter-end March 2024, on a total return basis, the S&P 500 Index rose 10.6%, while the S&P/TSX Composite Index increased 6.6%. REITs generally underperformed the broader market. The FTSE EPRA/NAREIT Developed Total Return Index increased nearly 1.5% (in Canadian dollar terms), the MSCI U.S. REIT Index declined 0.3%, and the S&P/TSX Capped REIT Index declined 0.7%. Long bond yields rose, with 10-year bond yields ending the quarter at 4.2% in the U.S. (up 36bps sequentially) and 3.47% in Canada (also up 36bps).

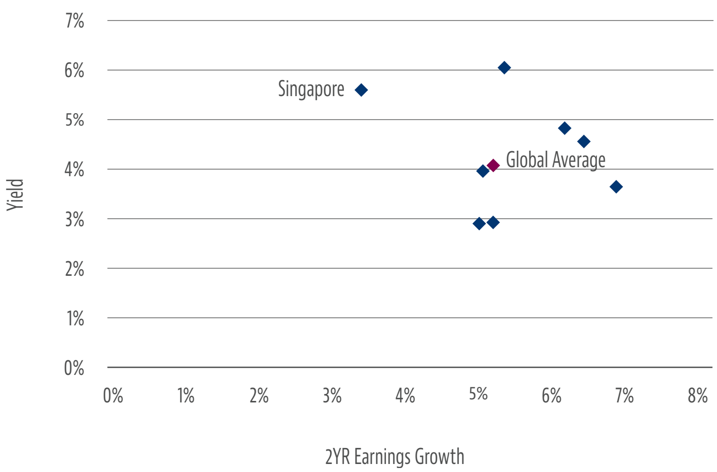
During the quarter, the fund sold its holdings in ESR Group and also sold out of Apartment Income REIT, while reinvesting some of the proceeds in Camden Property Trust. The fund initiated new positions in U.S. shopping centre REIT Brixmor, as well as German apartment owner LEG Immobilien and U.K. property owner Land Securities. The fund's top ten holdings as of March 31, 2024 included: Prologis, American Homes 4 Rent, VICI, American Tower, Chartwell Seniors Housing, Ventas, Equinix, Host Hotels, Alexandria and Kimco. The top ten holdings comprised approximately 39% of the fund.

BIFURCATION OF PERFORMANCE

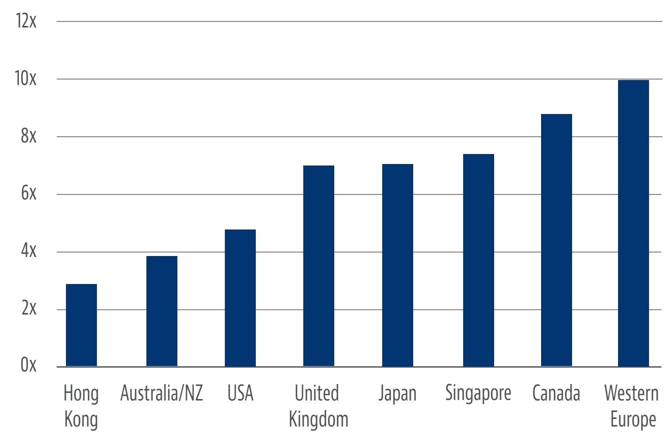
Within the U.S., there was reasonable dispersion between asset classes. Outperforming sectors included regional malls and lodging (partially driven by a stronger than anticipated consumer) and data centres (driven by the AI wave). Underperforming subsectors included towers (a high duration sector sensitive to interest rate moves), self storage (due to declines in market rents), and triple net lease (as a result of its reliance on interest rate spread investing).

Geographically, the two positive outliers from a performance perspective were Japan and Australia. Japan was primarily driven by an ongoing re-rating in Japan broadly (especially property developers with activist involvement). Australia was mainly driven higher by large weightings to Goodman Group (which is in turn benefitting from AI euphoria) and malls (benefitting as discussed above). On the flip side, Hong Kong underperformed as investors continue to be cautious on the region. Singapore was also weak which we suspect is partly owed to the lower growth, higher yield and generally higher net debt to EBITDA nature of the companies, as illustrated in the charts below.

GLOBAL YIELD VS. EARNINGS GROWTH



NET DEBT TO EBITDA



Source Bloomberg, S&P Capital IQ, Company Reports and CI Global Asset Management as of March 27, 2024.

SUBSECTOR REVIEW

During the quarter, REITs reported year-end earnings and many companies also provided outlooks for 2024. REITs reported Q4 2023 results that were largely in-line with estimates, with 72% of North American REITs meeting or beating consensus estimates. The mid-point of U.S. REITs' guidance implies funds from operation (FFO) per share growth of 2.6% in 2024. Data centre REITs are guiding to the strongest FFO per share growth (average +7.5% on a small sample size), while office REITs are guiding to the weakest growth (-1.6% on average).

We provide a brief overview of some of the underlying themes from earnings season and broker commentary for some major U.S. real estate "food groups".

Retail

According to CoStar, the national average retail vacancy rate hit a new low of 4% at the end of 2023. The sector continues to benefit from fewer retailer bankruptcies than the past few years, and demand is being supported by resilient consumer spending. There has been little in the way of new development, with net deliveries falling to the lowest level since CoStar began tracking the measure.

In parallel with the overall market, operating performance from U.S. shopping centre REITs continued to be strong in Q4 2023 with leased occupancy rates up, on average, 20bps year-over-year to 95.5% and blended leasing spreads of 11%. The signed-not-occupied lease pipeline for U.S. shopping centre REITs stood at 250bps as of year-end and the majority of these leases will commence in H2 2024. Given a limited availability of space and strong retailer leasing demand, vacancies are generally a net benefit to shopping centre REITs in the current environment as the FFO drag from re-tenanting space is more than offset by substantial rent increases on new leases.

Despite strong underlying fundamentals, initial 2024 guidance from U.S. retail REITs was below expectations and called for low single digit same-property net operating income (NOI) and FFO growth. This reflected the timing of lease commencements, conservative credit loss assumptions, one-time items and higher interest costs.

Investor demand for grocery anchored shopping centres continues to be healthy.

Industrial

Industrial absorption in the U.S. slowed considerably to 270M square feet (sf) in 2023, roughly half the levels of 2021 and 2022, while a record 550M sf of new supply was delivered during the year. As a result, the national average vacancy rate increased 160bps year-over-year to 4.7%. Development completions will moderate considerably in 2024 and are expected to total 325M sf, compared to 310M sf of net absorption, resulting in relatively stable occupancy levels, according to Green Street. We do expect that vacancy will tick up in the first half of 2024 as new supply is delivered, with the market normalizing in the back half as supply growth falls.

Market rent growth was 7% in 2023, according to CoStar and growth is expected to remain positive over the next several years. Use of concessions, primarily free rent, has returned to pre-pandemic norms and is more prevalent in markets with an influx of supply. With most of the supply under construction expected to be delivered in H1 2024, the outlook is for flat to slightly declining market rents in the first half of the year, followed by a reacceleration of rent growth in late 2024 and into 2025.

Mid to high single digit organic growth should be achievable for U.S. industrial REITs over the next several years as rents on expiring leases are marked to market. Weighted average re-leasing spreads were 49% in 2023 and should remain elevated until 2027, according to Green Street.

Multifamily

Although the boom in household formation that occurred at the height of the pandemic has faded, residential demand in the U.S. continues to be supported by a healthy job market and higher barriers to home ownership as mortgage interest rates have risen.

The benefit of positive net migration trends in U.S. sunbelt markets is likely to be overwhelmed by the impact of elevated multifamily supply deliveries in 2024. U.S. sunbelt-focused multifamily REITs reported new lease spreads of, on average, -5.7% in Q4 2023 compared to -2.6% for coastal U.S. multifamily REITs. For 2024, sunbelt-focused multifamily REITs are guiding to slightly negative same property NOI growth compared to positive for coastal U.S. multifamily REITs.

Leasing concessions at competitive new-build properties will likely push vacancy rates higher and net effective rents in the sunbelt over the next 12-18 months. However, construction starts have fallen and fundamentals should improve gradually as new supply is absorbed.

Office

The U.S. national office vacancy rate increased 110bps year-over-year to 13.8%, according to CoStar. Concerns regarding an economic recession led to tenants delaying leasing decisions in early 2023 and despite an improvement in the macroeconomic outlook as the year progressed, total gross leasing volume was 13% below the average from 2015-2019. Space requirements also decreased with the amount of space leased in an average deal down 16% below the 2015-2019 average.

Nearly US$400 billion of office-backed loans will mature over the next three years including US$206 billion in 2024. A material decline in values since 2021 and higher interest rates will likely necessitate equity injections or other forms of recapitalizations as these loans mature. Capital remains scarce within the office sector, with declining rents, negative net absorption and a lack of available debt financing making acquisitions difficult to underwrite.

Recent financial results and 2024 guidance from office REITs suggest the operating environment will remain challenging over the next year. Occupancy rates for U.S. office REITs declined 40bps year-over-year to 88% in Q4 2023 and while headline rental rates have been relatively stable, tenant incentives and leasing costs increased 10% year-over-year. For 2024, office REITs have guided to occupancy declines of, on average, 110bps and low single digit declines in same-property NOI.

OUTLOOK AND POSITIONING

REIT M&A activity has picked up, with quarterly volumes of closed and pending deals involving public real estate companies back to 2021 levels on a quarter-to-date basis, according to Bloomberg. The largest announced transaction was Blackstone's offer for Tricon Residential in January, which was an overweight position of the fund heading into the new year. We believe it is possible that further consolidation could happen this year, primarily in subscale REITs with stretched balance sheets and a disadvantaged cost of capital.

Underlying fundamentals for most property types are healthy and, barring an economic slowdown, market rents should continue to climb over the next year. Excess supply within certain property types should abate later this year and into 2025 as construction starts have fallen materially since early 2023. Higher interest rates and tighter availability of credit, as well as still elevated construction costs should continue to act as constraints on new supply starts. As a result, barring a collapse in demand, the fundamental backdrop for many asset classes should improve in 2024, and strengthen into next year.

While the number of Federal Reserve rate cuts expected by the market has fallen from six at the start of the year to between two and three, it is largely agreed the global central bank hiking cycle is over and an easing path is unfolding. For example, among major central banks, Switzerland cut its policy rate in March owing to lower inflation and lower economic growth. The actual rate cuts by central banks (as opposed to just market expectation) could be symbolically important to investors in determining when to re-enter yield sensitive sectors, leading to positive fund flows into REITs. Lower short-term rates could also lead to positive fund flows into rate-sensitive sectors as yields from money market instruments and GICs decline.

We estimate the FTSE EPRA/NAREIT Developed Total Return Index is trading at roughly a 5% discount to NAV, with markets like the U.S. trading closer to parity. Markets like Canada, Singapore and certain asset classes in Europe are still offering discounts in the 15% range. There is reasonable dispersion across subsectors globally. On a simple average basis, benchmark constituents globally in the data centre, single family rental and health care subsectors are on average trading above NAV. Office, life sciences and shopping centres are trending towards the 20% and above discount range.

In terms of fund positioning, we generally remain underweight office and malls, and are relatively underweight data centre primarily on valuations that appear stretched. Our overweight positions remain tilted toward sectors with resilient fundamentals and reasonable valuations. These include residential (primarily Canadian multifamily, single family housing, and seniors housing), necessity based retail shopping centres, and towers (on belief of long term structural tailwinds and anticipation of a re-rate should interest rates fall).

It is anticipated inflation will continue to be contained and central bank rates may need to be lowered. While long-term yields have surged YTD, it is believed by economists that 10-year yields should end the year close to where they started. With a narrower 10-year interest rate band, private market real estate investors are gaining more confidence in their cost of capital which should lead to a resumption in transaction activity. This should help to inform market pricing which appears to be in the bottoming process. With REITs already trading at discounts to NAV, we believe public real estate values are more attractive than private market pricing.

Figures in Canadian dollars unless otherwise stated

GLOSSARY OF TERMS:

Duration: A measure of the sensitivity of the price of a fixed income investment to a change in interest rates. Duration is expressed as number of years. The price of a bond with a longer duration would be expected to rise (fall) more than the price of a bond with lower duration when interest rates fall (rise).

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CI GLOBAL ASSET MANAGEMENT

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