

# Global Real Estate: Thoughts on Portfolio Structure, Global Markets & US Outlook

**Congreso Inmobiliario 2016**

October 4, 2016

**PGIM** Real Estate



# Strength & Stability

Deep Financial Strength and a Long History of Real Estate Experience



## Prudential Financial, Inc. (PFI)

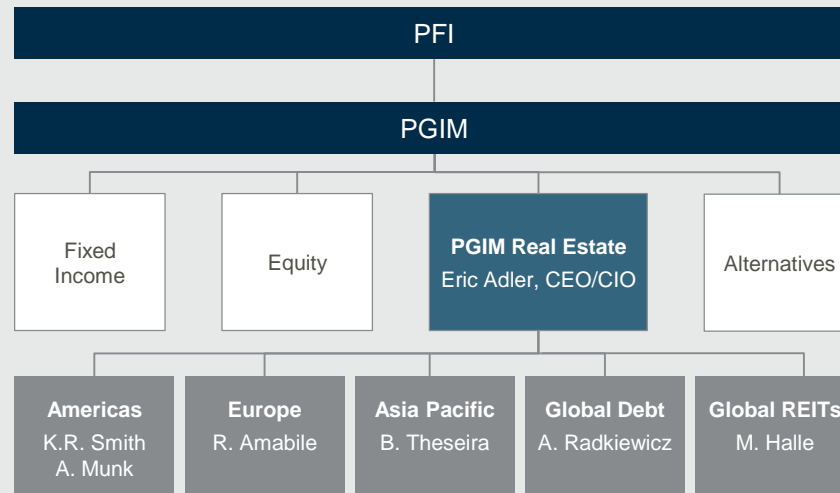
- 140 years of managing assets
- Listed on the NYSE (New York Stock Exchange, NYSE: PRU)
- US\$1.27 Trillion<sup>1</sup> of AUM
- One of the largest insurance companies in the United States
- A rated (Issuer Credit Rating)<sup>2</sup> by Standard & Poor's

## PGIM

- Global Asset Manager with US\$1.05 Trillion<sup>3</sup> of AUM
- Top 10 Worldwide Institutional Money Manager<sup>4</sup>

## PGIM Real Estate

- US\$66.5 Billion<sup>5</sup> gross AUM globally



<sup>1</sup> As of June 30, 2016. <sup>2</sup> As of August 3, 2016. Source: Standard & Poor's. <sup>3</sup> Includes all assets managed by PGIM, Inc., the principal asset management business of PFI. Assets include public and private fixed income, public equity – both fundamental and quantitative and real estate) as of June 30, 2016. <sup>4</sup> As of May 30, 2016. Source: Pensions and Investments, Top Money Manager's List. Based on PFI total worldwide institutional assets under management as of December 31, 2015. <sup>5</sup> As of June 30, 2016, total net assets under management equal \$49.0 billion.

# Global Platform with Deep Local Knowledge and Expertise



Cavendish Square (London)



International Place (Boston, MA)



Nex Mall (Singapore)

## Overview

Assets Under Management: \$66.5B gross<sup>1</sup>

Established in 1970

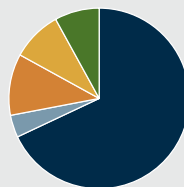
600 Professionals<sup>2</sup>

18 cities in the Americas, Europe and Asia Pacific

500 institutional clients<sup>2</sup>

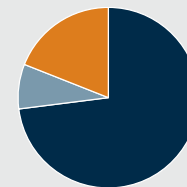
169 clients invested in multiple strategies

## GLOBAL INVESTMENTS (BASED ON GAV)<sup>1</sup>



- 68% Americas: United States
- 4% Americas: Latin America
- 11% Europe
- 9% Asia Pacific
- 8% Global Real Estate Securities

## FUND STRUCTURES (BASED ON GAV)<sup>1</sup>

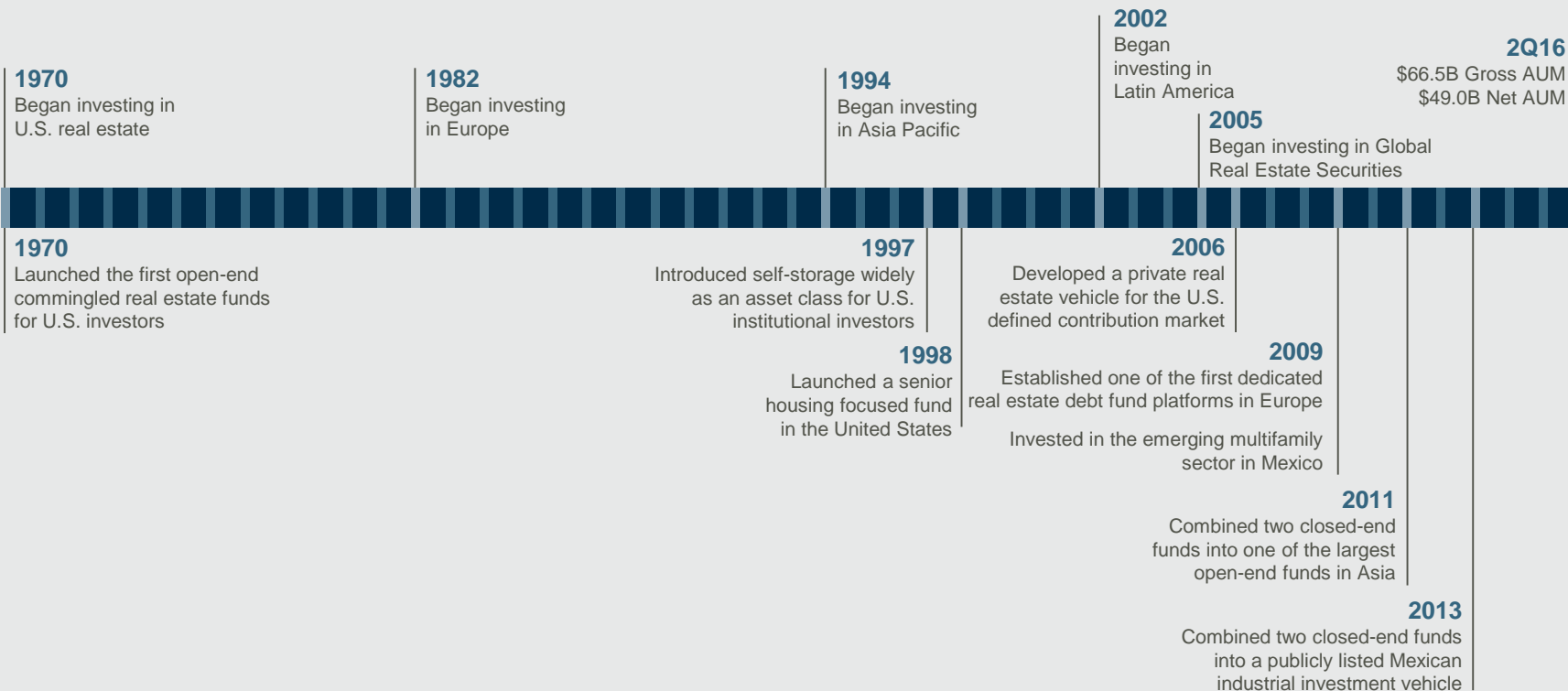


- 73% Open-End Funds
- 8% Closed-End Funds
- 19% Single Client Accounts

<sup>1</sup> As of June 30, 2016. \$49.0 billion net. <sup>2</sup> Approximately.

# Pursuit of Innovation

Pioneering Investment Strategies for More Than Four Decades



Note: Past performance is not a guarantee or a reliable indicator of future results.

# What is Commercial Real Estate?



- Apartments
- Shopping Centers
- Office Buildings
- Warehouses
- Senior Housing
- Self-Storage
- Medical Offices
- Hotels

# How does Commercial Real Estate Make Money?



## Income

- Rents from tenants
- Re-lease vacant space by attracting new tenants
- Manage Expenses – staff, maintenance, etc.

## Appreciation

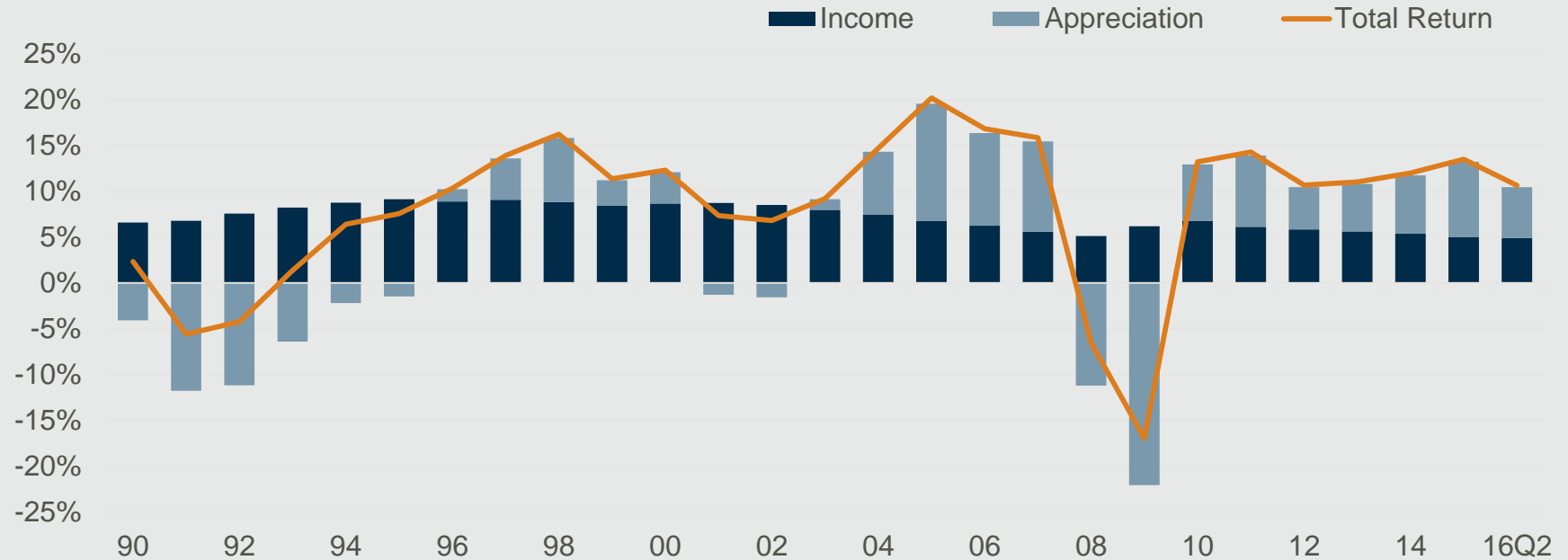
- Overall Economic Growth
- Demographic trends
- Neighborhood Improvements
- Renovations to the property
- Capital markets



# Real Estate Provides Both Income *and* Appreciation



## HISTORICAL PERFORMANCE



Sources: NCREIF, PGIM Real Estate. As of June 30, 2016.

# Many Economic Factors Impact Real Estate



## Key Economic Demand Drivers

- GDP Growth
- Job Growth
- Retail Sales
- Consumer Confidence
- Demographics
- Lifestyle Preferences
- House Prices
- Labor Force Growth
- Income Growth
- Auto Sales
- Domestic Migration Patterns
- Industrial Production
- Construction Costs
- Technological Developments
- Structural Economic Change

## Key Drivers of Investment Demand

- Interest Rates
- Bank Lending Appetite
- Inflation
- Corporate Bond Yield Spreads
- Global Capital Flows
- Equity Markets Performance
- Risk Appetite



# Major Property Sectors: Apartment



## Major Economic Drivers

- Employment and income growth
- Demographic trends
  - Rise in Millennial population
  - Geographic migration patterns
- Homeownership rates
- Construction lending
- Urbanization / Lifestyle preferences

## Investment characteristics

- Short-term leases offer a hedge against inflation.
- Perceived stability during economic cycle.



# Major Property Sectors: Office

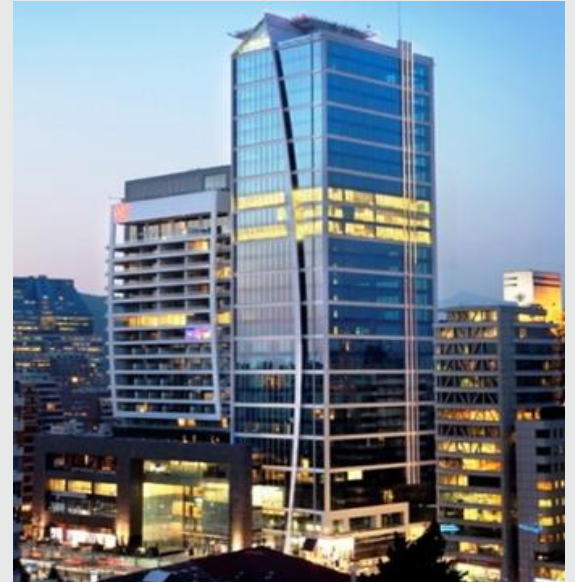


## Major Economic Drivers

- Job growth
- Technological change
- Educational attainment

## Investment characteristics

- Rents demonstrate most volatility during the economic cycle. Market timing matters.
- Most globally consistent property type.



**Isidora 3000**  
Santiago, Chile

# Major Property Sectors: Retail



## Major Economic Drivers

- Employment and income growth
- Retail sales growth
- Population and household growth
- Housing market

## Investment characteristics

- Very micro-location and asset specific – least ‘commodity like’ property sector
- Asset management very important
- Consumer-oriented asset class versus corporate-oriented asset class.



# Major Property Sectors: Industrial



## Major Economic Drivers

- Global trade patterns and port traffic, e.g., Panama Canal expansion
- Manufacturing & industrial production
- E-commerce & retail sales

## Investment characteristics

- Infill locations near ports & airports in demand and more supply constrained.
- Typically built in low-supply constrained areas with high obsolescence on cheaper land.
- Low rental or capital value growth over the long term; mostly an income play.



# Why Is Real Estate Attractive to Institutional Investors?



**Long-Term Performance.** Private real estate has exhibited significantly lower volatility and competitive returns compared with bonds and stocks. Direct property investments have proven effective in preserving capital over a complete market cycle.

**Asset Class Diversification.** Low correlations to other asset classes such as stocks and bonds, including European stocks and bonds, make commercial real estate an effective diversifier in a mixed-asset portfolio.

**Inflation Hedge.** Commercial real estate has been a better store of wealth than stocks or government bonds in periods of high inflation.



Source: PGIM Real Estate. As of 2016.

# Real Estate is a Durable Asset



## **Class-A Midtown Manhattan Office Building**

Core Asset held by  
Institutional Fund  
Purchased for \$35M in 1974



## **Class-A Midtown Manhattan Office Building**

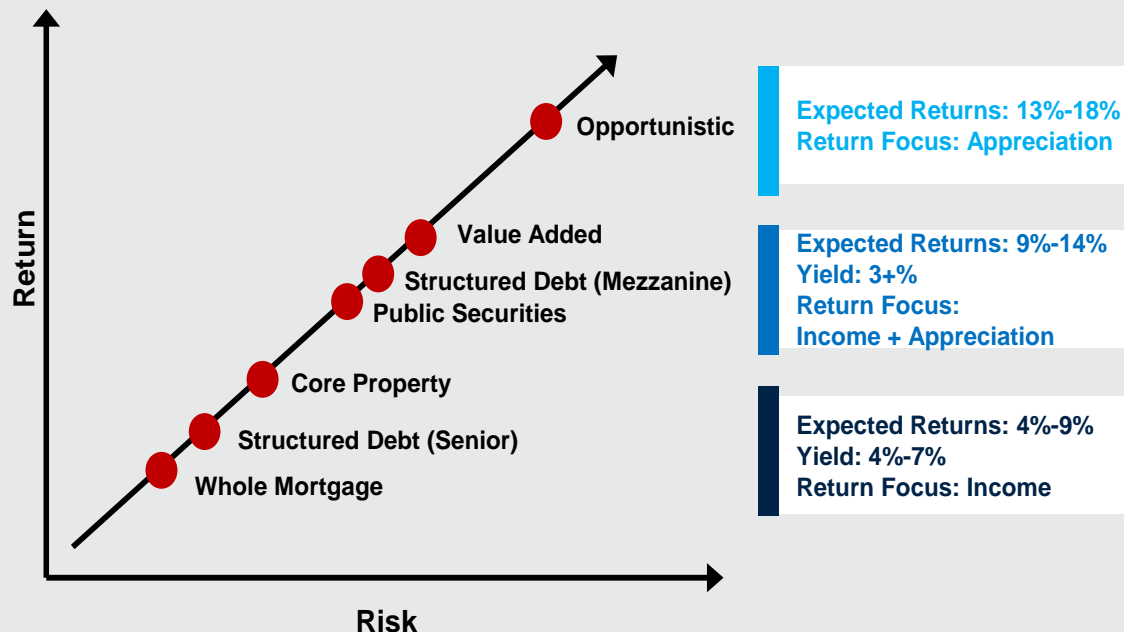
Core Asset held by  
Institutional Fund  
Valued at \$825M at 12/31/15

# Many Ways To Have Real Estate Exposure



- As an asset class, commercial real estate offers a diverse range of opportunities to target varying degrees of return and risk.
- The opportunity set includes direct and indirect equity and debt investments.

## YIELD COMPARISON ACROSS STRATEGIES



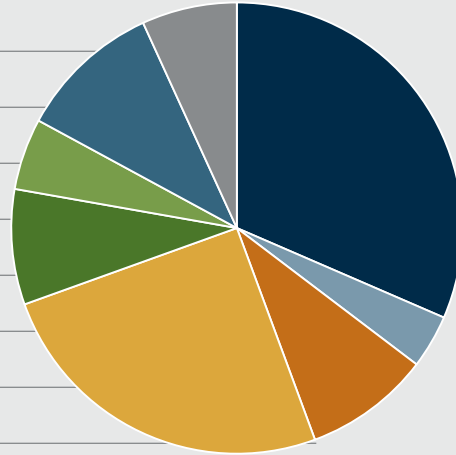
Source: PGIM Real Estate. As of 4Q15 Returns are net; There is no guarantee that expectations will be met.

# Investment Universe of Global Commercial Real Estate



## ESTIMATED REAL ESTATE INVESTED UNIVERSE, 2014

■	32% U.S.
■	4% Canada
■	9% UK
■	25% Europe
■	8% Japan
■	5% China
■	10% Asia Pacific
■	7% Rest of World



Globally, there is over \$8 trillion of invested institutional real estate.

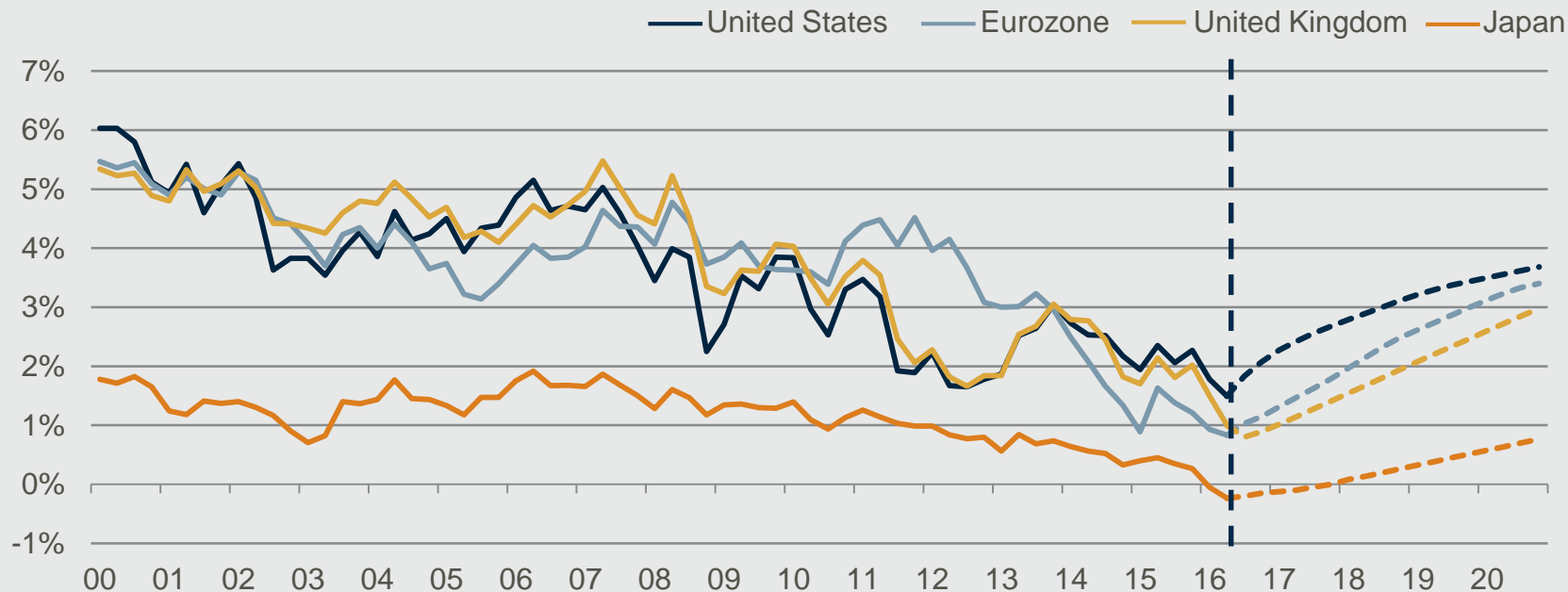
Source: IPD, PGIM Real Estate. As of March 2016.



# Rates Remain Low in an Easy Monetary Policy World



## YIELDS ON 10-YEAR GOVERNMENT BONDS AND FORECASTS

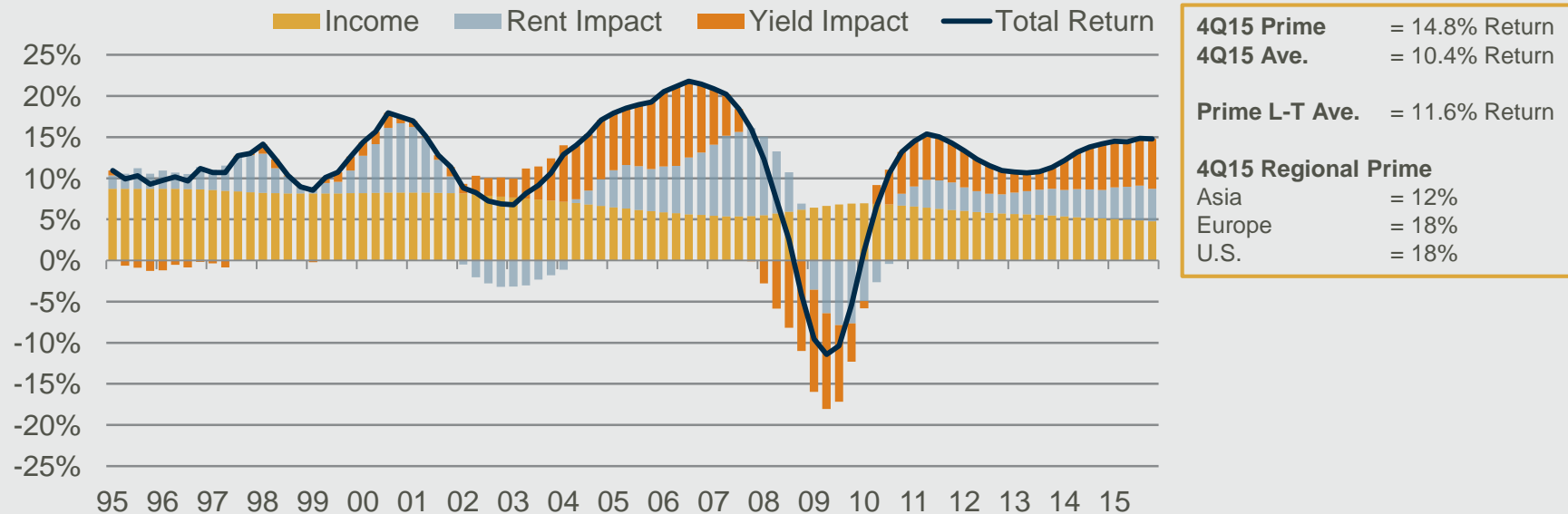


Sources: Oxford Economics, Federal Reserve, ECB, Bank of England, Bank of Japan, PGIM Real Estate. As of July 2016.

# Strong Global Real Estate Returns Since 2011



## ESTIMATED UNLEVERED ALL COMMERCIAL PROPERTY PRIME MARKET RETURN (% PA)



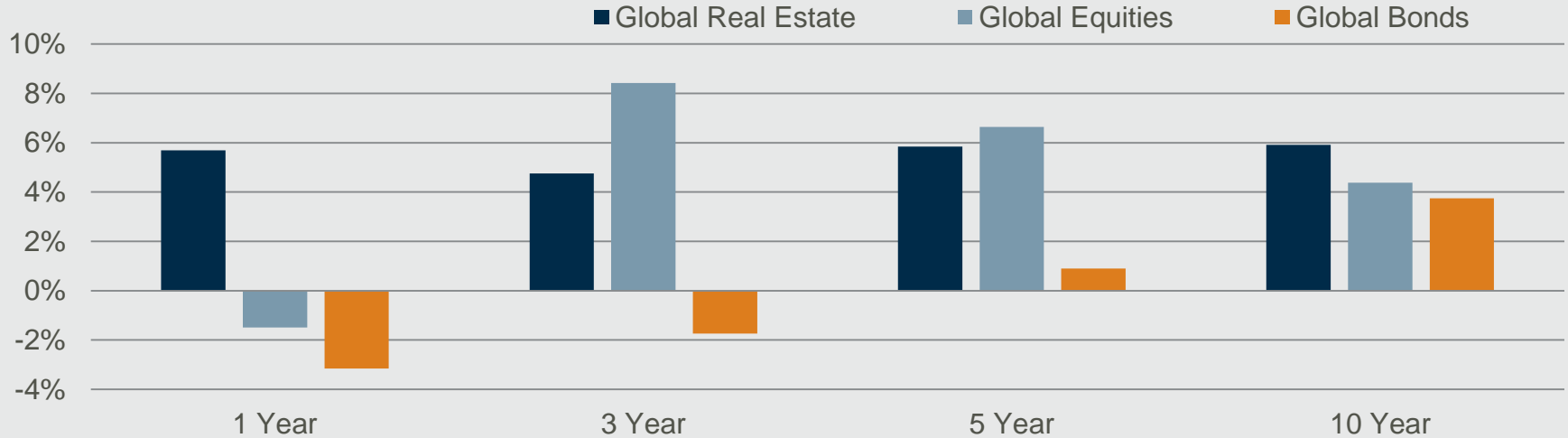
<b>4Q15 Prime</b>	= 14.8% Return
<b>4Q15 Ave.</b>	= 10.4% Return
<b>Prime L-T Ave.</b>	= 11.6% Return
<b>4Q15 Regional Prime</b>	
Asia	= 12%
Europe	= 18%
U.S.	= 18%

Sources: Cushman & Wakefield, CoStar, JLL, CBRE, Colliers, PGIM Real Estate. As of July 2016.

# Global Real Estate Performance Holds its Own



## GLOBAL HISTORICAL PERFORMANCE



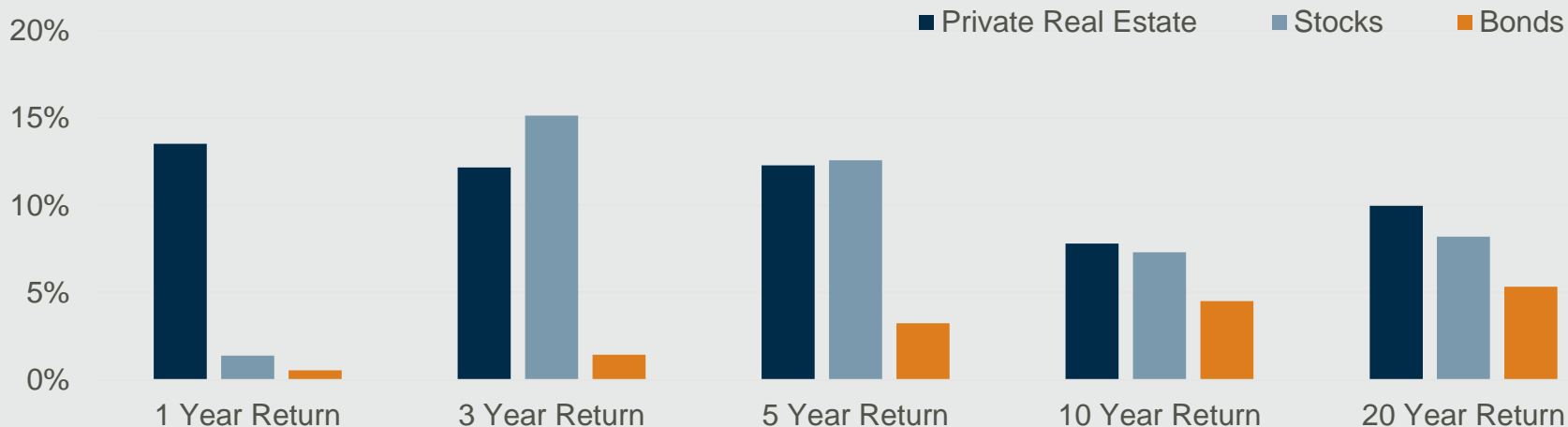
	Private RE	Equities	Bonds
Private Real Estate Correlation with	1.00	.41	.23

Sources: Barclays, S&P, MSCI, PGIM Real Estate. As of June 30, 2016.

# U.S. Real Estate Performance Holds its Own



## U.S. HISTORICAL PERFORMANCE



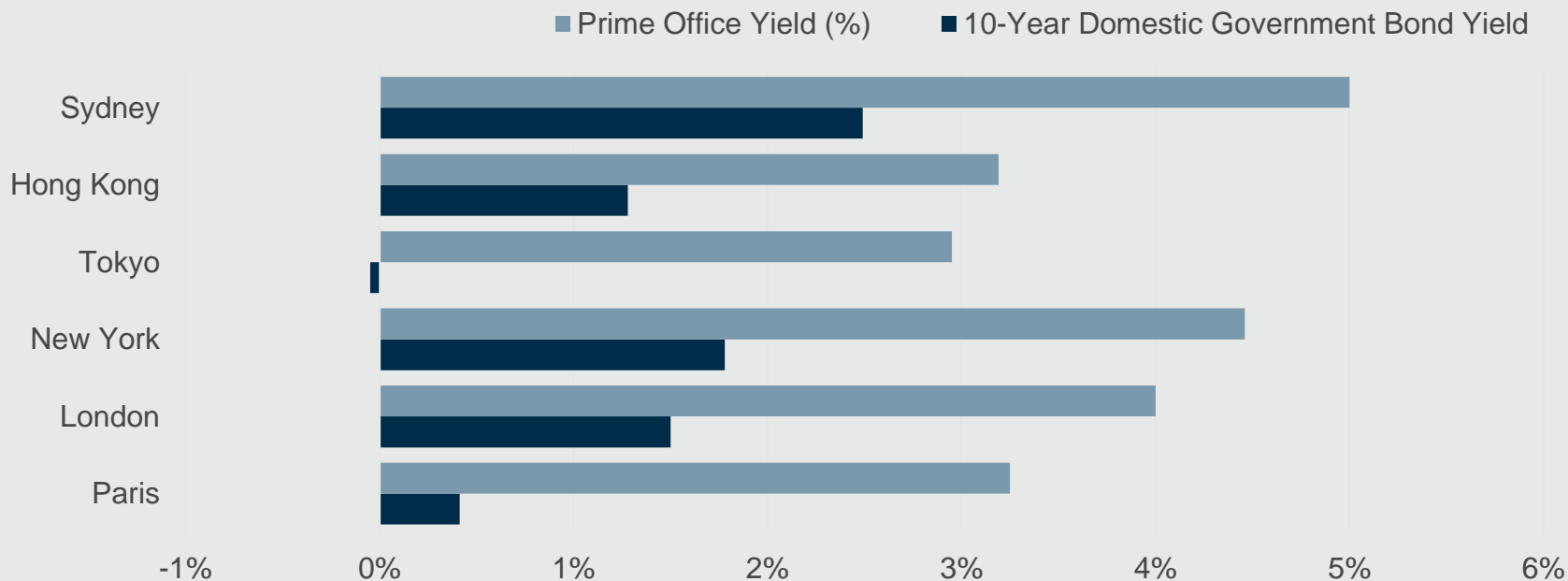
	Private RE	Stocks	Bonds
Private Real Estate Correlation with	1.00	0.18	(0.11)

Sources: NCREIF, NAREIT, S&P, Barclays quarterly return data as of June 30, 2016.

# Office Yields Have Compressed Globally But Spreads Remain Relatively Wide



## PRIME OFFICE YIELDS VS 10-YEAR BONDS (Q1 2016)

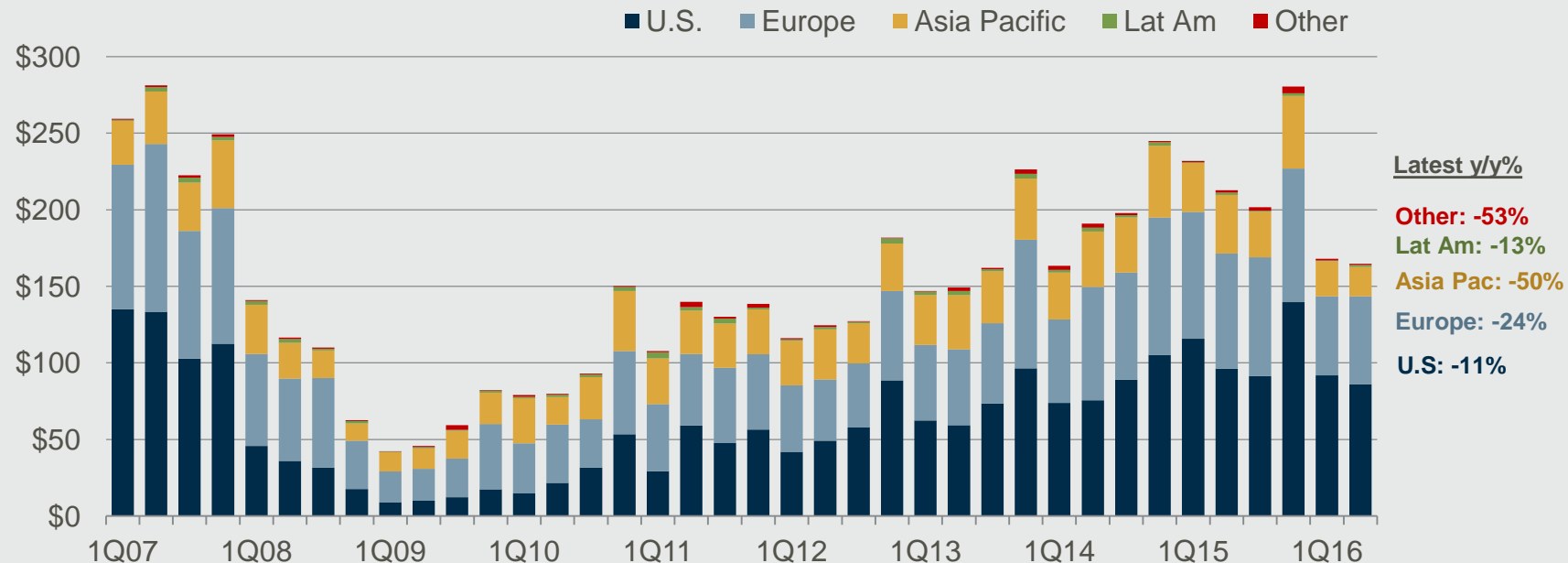


Sources: JLL Real Estate Intelligence Service 1Q16

# Transaction Volume Slowing Globally



## GLOBAL TRANSACTION VOLUME, QUARTERLY, (\$BILLIONS)

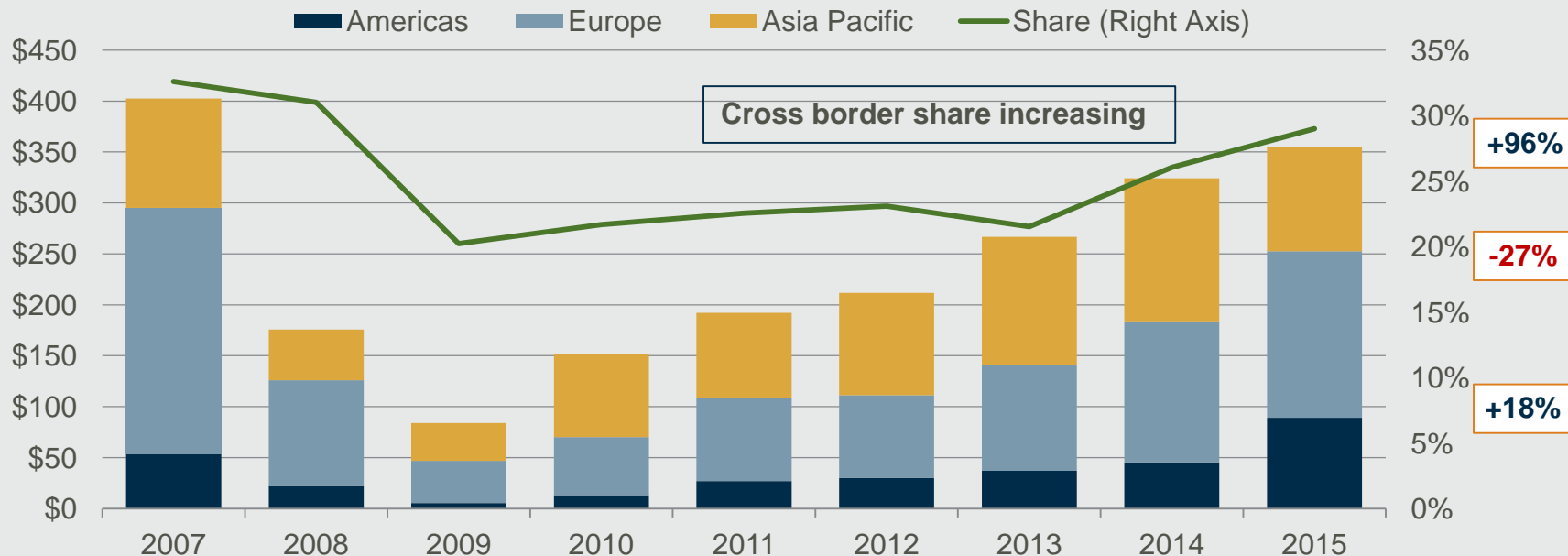


Sources: Real Capital Analytics, PGIM Real Estate. As of October 2016.

# Cross-Border Investments Accounted For Nearly 30% in 2015



## CROSS-BORDER INVESTMENT VOLUME BY DESTINATION (\$ BILLION)

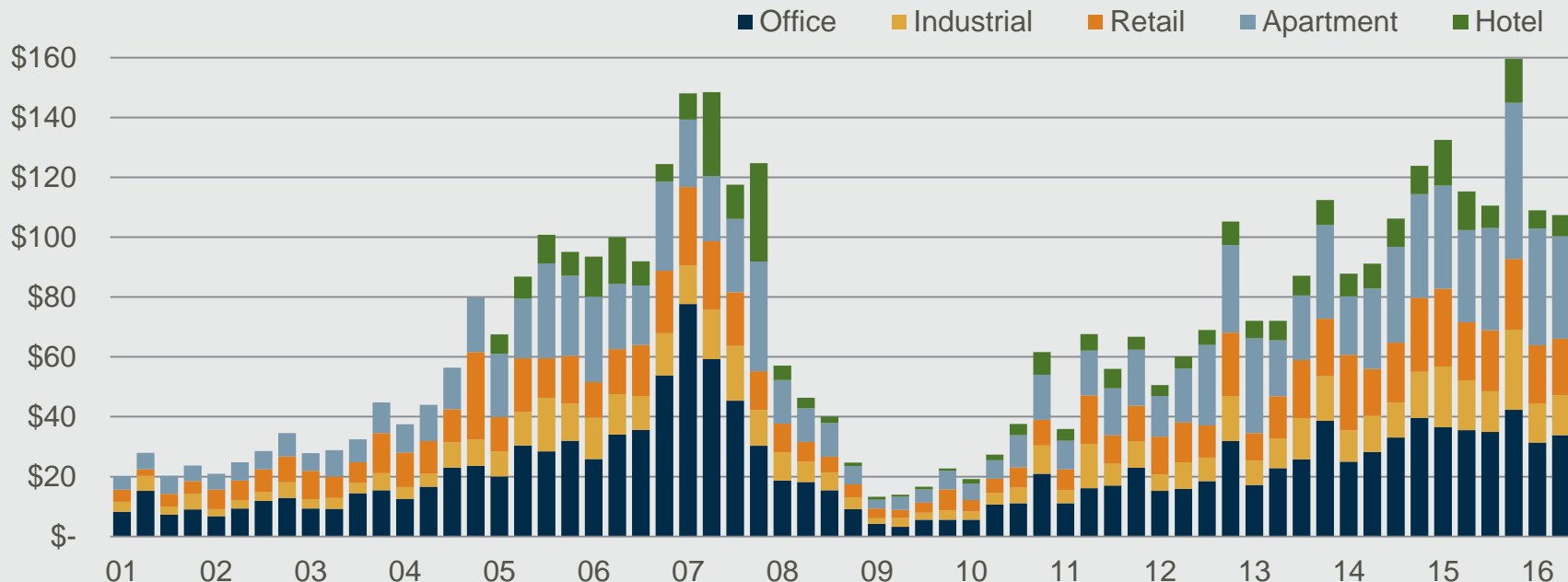


Sources: Real Capital Analytics, PGIM Real Estate. As of May 2016.

# U.S. Transaction Volume Easing



## U.S. PROPERTY TRANSACTION VOLUME, QUARTERLY, (\$BILLIONS)



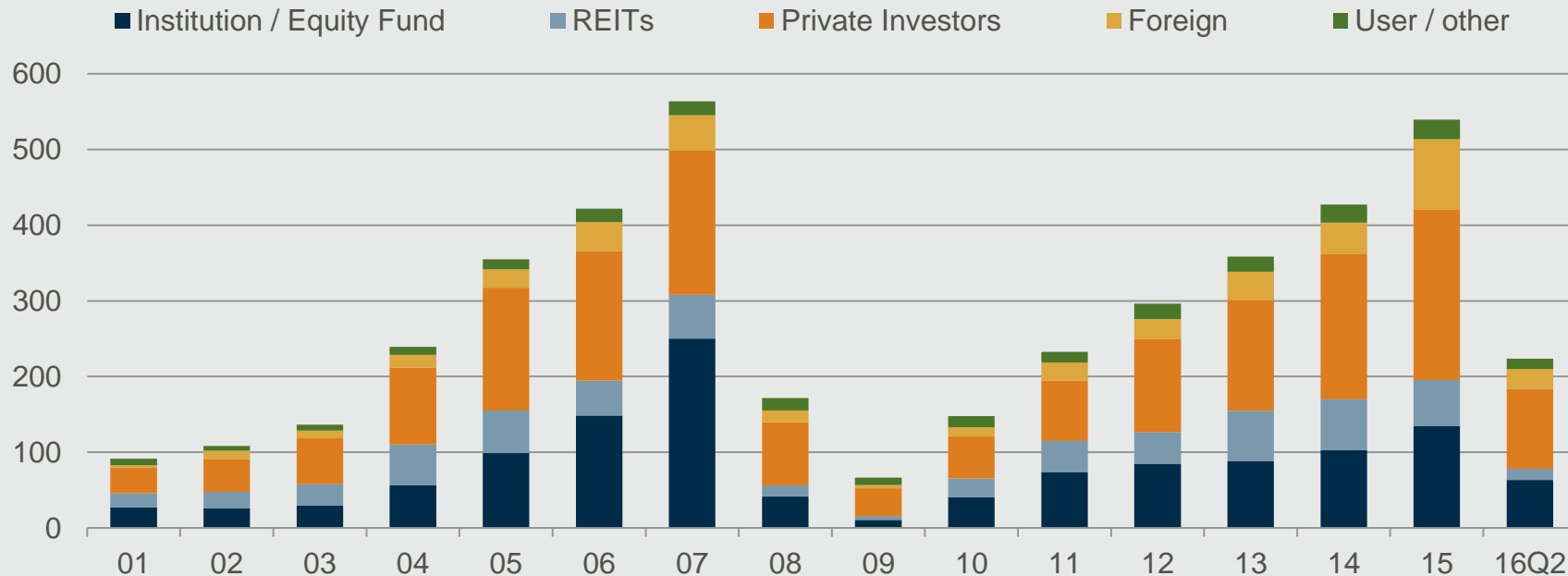
Sources: Real Capital Analytics, PGIM Real Estate. As of June 30, 2016.



# Variety of Participants in U.S. Commercial Real Estate



## TOTAL INVESTMENT IN U.S. COMMERCIAL REAL ESTATE \$ BIL, 2001-2016Q2

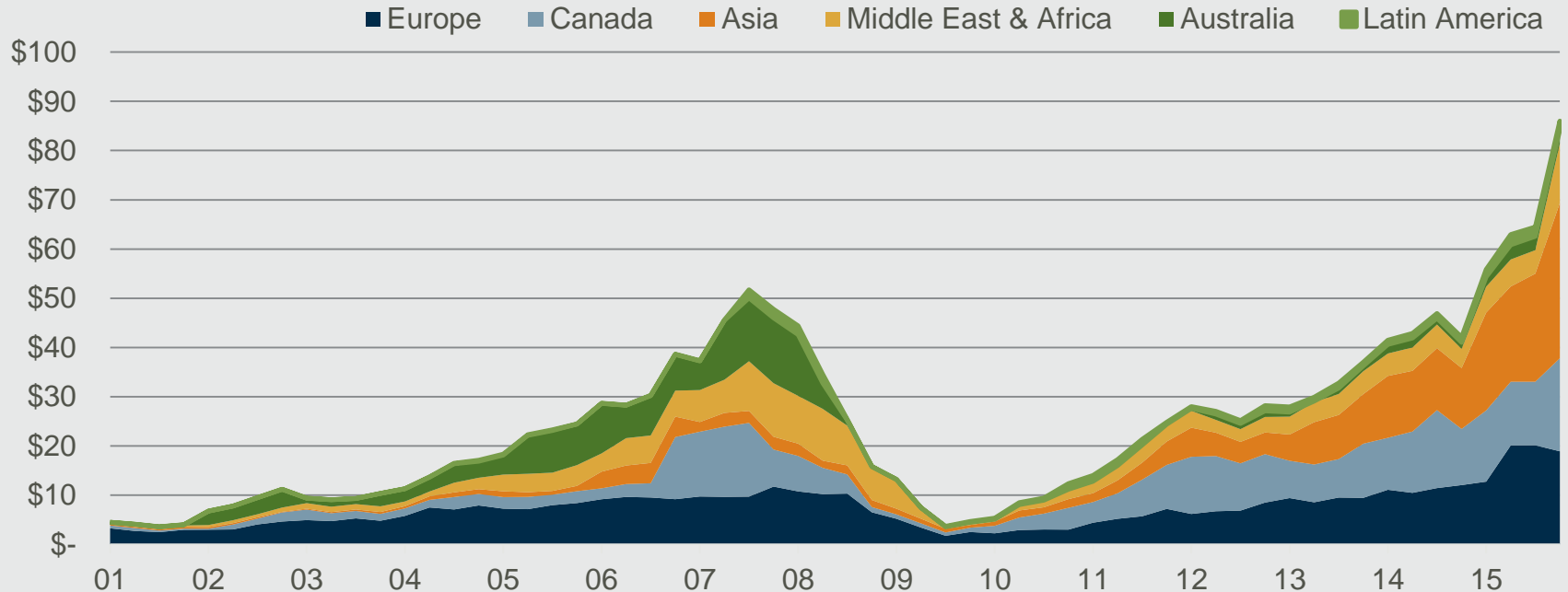


Source: Real Capital Analytics, PGIM Real Estate. As of June 30, 2016.

# Cross-Border Capital Flows to U.S. Reach New Highs



## CROSS-BORDER CAPITAL FLOWS INTO THE UNITED STATES BY REGION OF ORIGIN (\$BILLIONS)

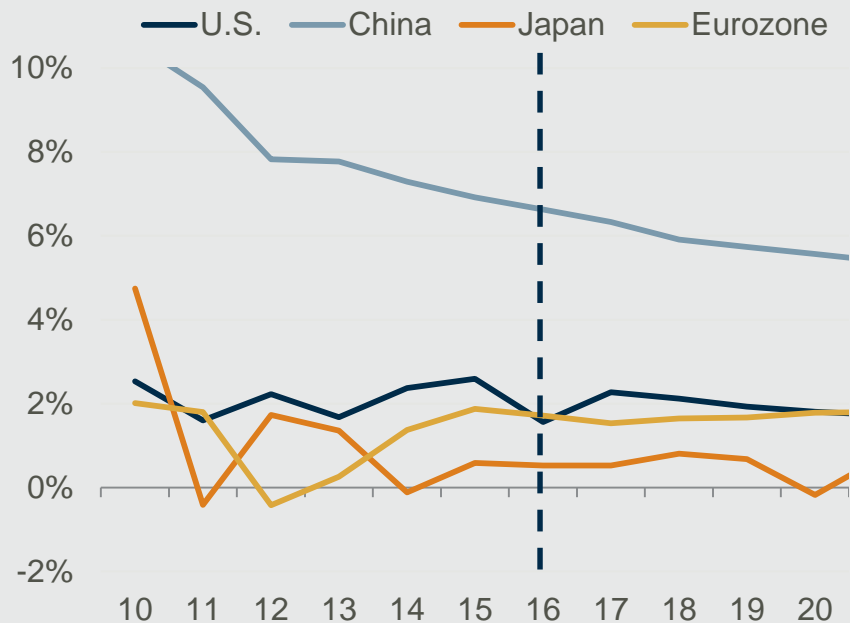


Sources: Real Capital Analytics, PGIM Real Estate. As of 4Q15.

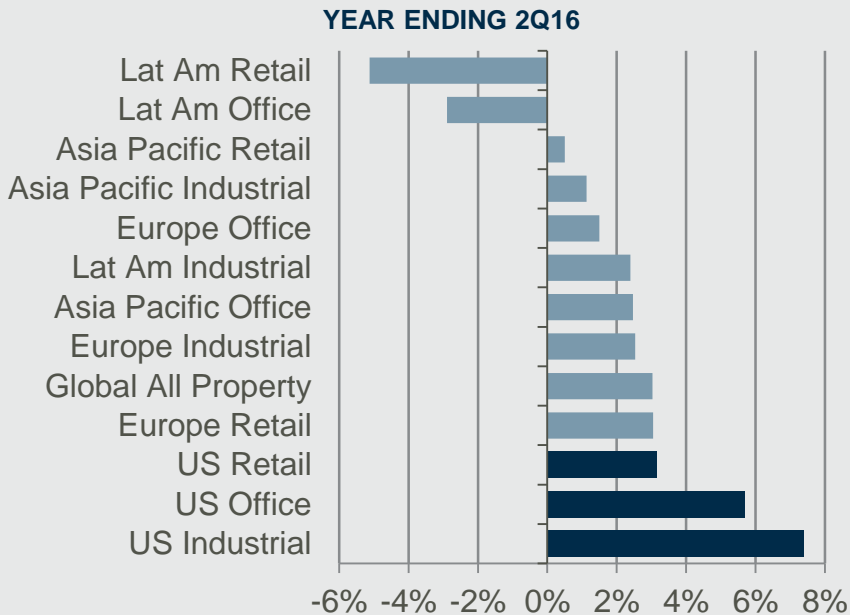
# Slow, but Steady U.S. Growth is Relatively Attractive



## ANNUAL REAL GDP GROWTH, %



## ANNUAL PRIME RENTAL GROWTH BY MARKET

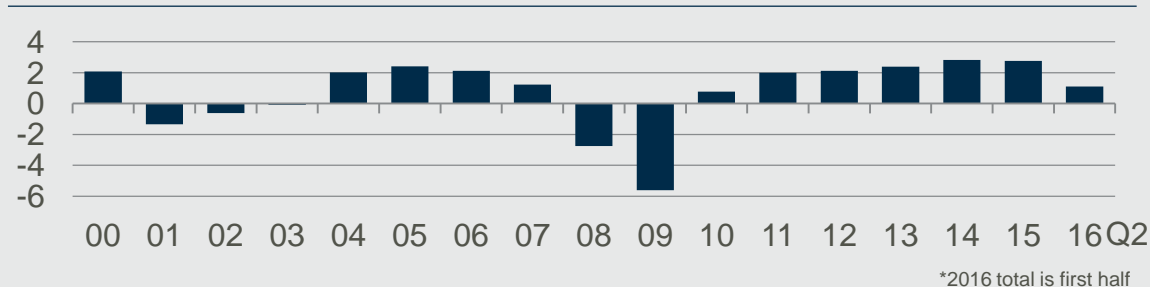


Source: Oxford Economics; Cushman & Wakefield, CoStar, JLL, CBRE, Colliers, PGIM Real Estate. As of 2Q16.

# Strong U.S. Labor Market

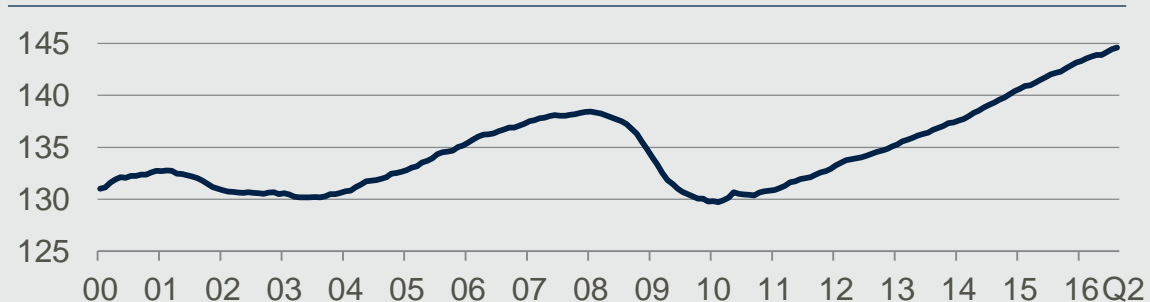


## U.S. ANNUAL EMPLOYMENT GAINS (MIL)



Strengthening labor market is leading to better wage prospects, which will support consumption.

## TOTAL EMPLOYMENT (MIL)

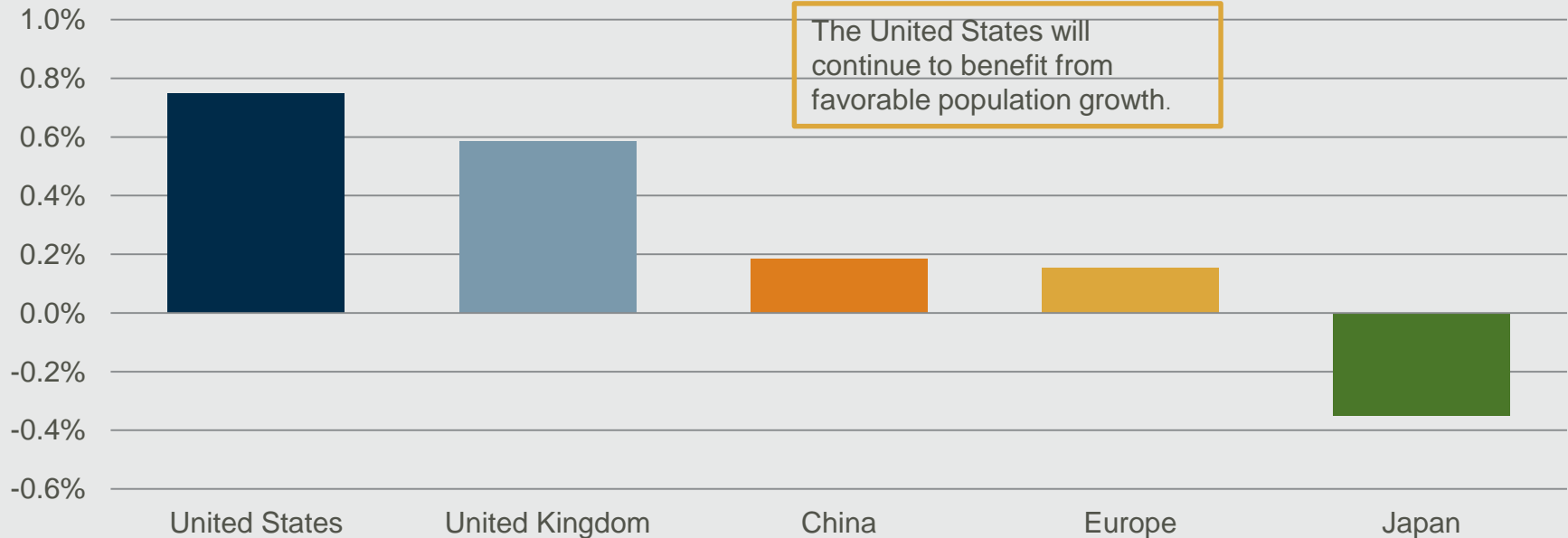


Sources: U.S. Bureau of Labor Statistics, NCREIF, Moody's Analytics, PGIM Real Estate. As of September 2016.

# Demographic Trends Are a Key Support for U.S. Economy



## 15-YEAR FORECAST POPULATION GROWTH, CAGR 2015-2030

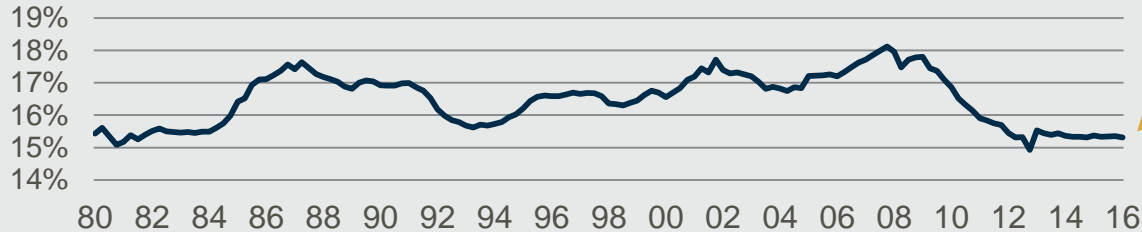


Sources: Oxford Economics, PGIM Real Estate. As of September 2016.

# Consumers Are in Strong Shape

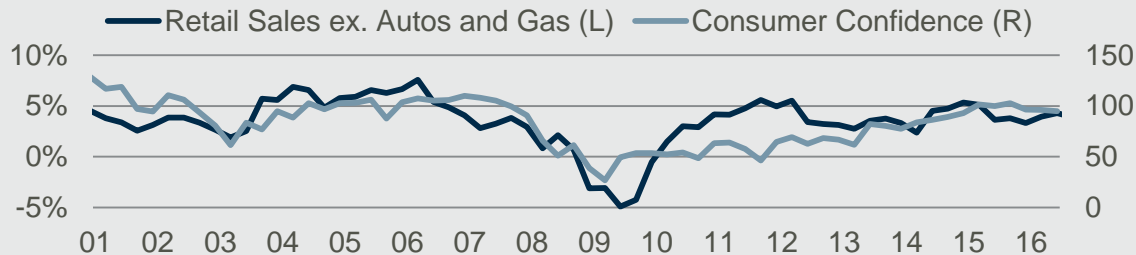


## HOUSEHOLD FINANCIAL OBLIGATIONS, % OF DISPOSABLE INCOME



Consumer financial obligations close to historical lows.

## RETAIL SALES EXCLUDING AUTOS AND GAS VS. CONSUMER CONFIDENCE



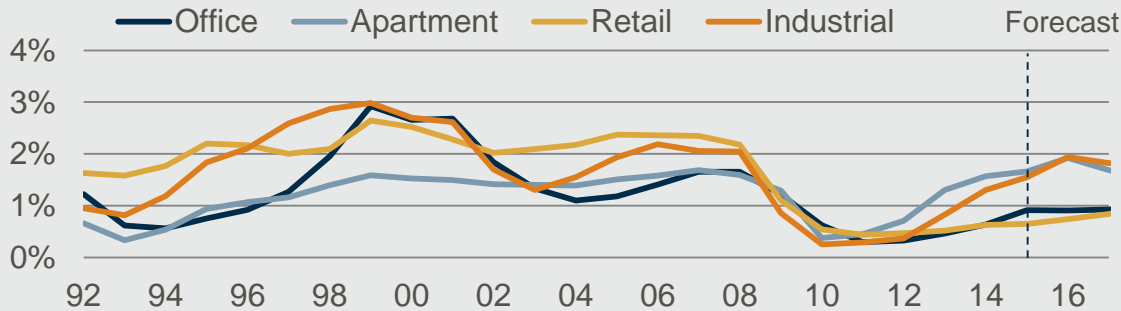
Consumer spending and confidence are holding up well.

Sources: Moody's Analytics, Bureau of Census, PGIM Real Estate. As of September 2016.

# U.S. Development Pipeline in Historical Context



## NET ADDITIONS AS A PERCENTAGE OF EXISTING STOCK



### Averages by Property Type

	Office	Apartment	Retail	Industrial
10-Year	0.9%	1.2%	1.1%	1.2%
20-Year	1.4%	1.3%	1.7%	1.7%
5-Year Forecast	1.0%	1.4%	1.0%	1.7%

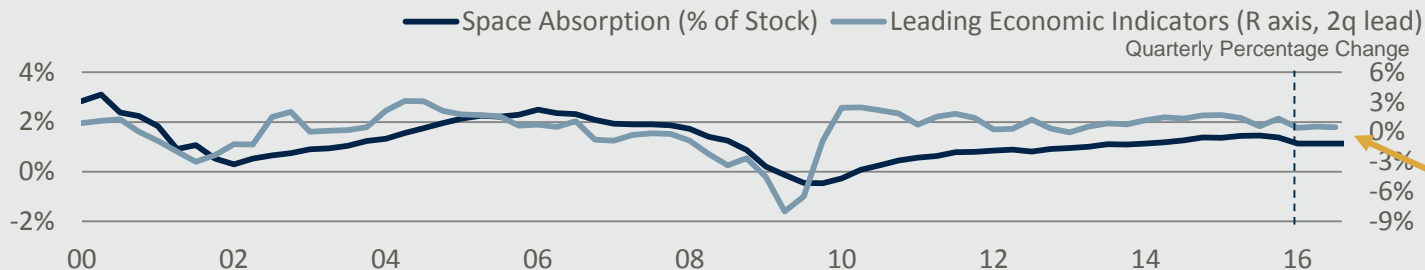
- Apartment vacancies have plummeted, creating a strong need for new supply.
- Office development pipeline remains limited in the near-term.
- Strong demand for more efficient warehouse space driving new supply.
- Targeted retail development as firms adapt to e-commerce demands.

Sources: PGIM Real Estate, Axiometrics, CoStar Portfolio Strategy. As of September 2016.

# Healthy Demand + Limited Supply = Strong Income

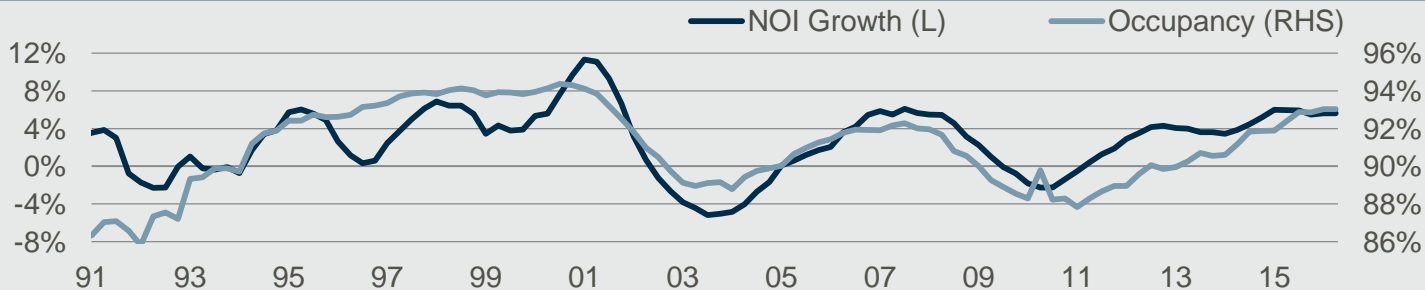


## LEADING ECONOMIC INDEX AND ABSORPTION OF RETAIL, OFFICE, INDUSTRIAL SPACE (% OF STOCK)



Leading indicators still suggest slower pace of absorption this year.

## NCREIF PROPERTY INDEX NOI GROWTH (4-QTR. ROLL) & OCCUPANCY – U.S. ALL PROPERTY TYPES



Sources: Moody's Analytics, NCREIF, PGIM Real Estate. As of September 2016.





## History of Real Estate Investment

- Institutional real estate investment in the U.S. is a mature market with depth and significant transparency. Major European markets are broadly just behind. Institutional investment in Asia and Latin America has increased over the past decade.

## Why is Real Estate Attractive?

- Real estate provides a compelling yield and the opportunity for capital appreciation
- Commercial real estate can also provide inflation protection

## Different Ways to Invest in Real Estate

- There are a variety of ways to gain exposure to U.S. and global institutional real estate

## U.S. Market Outlook

- The economic fundamentals appear healthy, supporting continued growth in tenant demand. Supply remains limited but is picking up in selected sectors and metros. We expect continued growth in rents and incomes.
- With yields already at very low levels, the strongest gains in appreciation are likely past and returns are likely to be income-driven. We expect further healthy total returns, though likely not matching recent double-digit performance.

**PGIM** Real Estate



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