hazelview
INVESTMENTS

BEYOND THE TRADITIONAL

UNCOVERING THE VALUE OF INVESTING IN SPECIALIZED REAL ESTATE PROPERTIES

Introduction

The concept of diversification is essential to investment portfolios. Diversification involves investing in a variety of assets to reduce risk, while increasing potential returns. Consequently, real estate has become an attractive asset class for investors looking to improve diversification and ultimately reduce risk without sacrificing returns. One of the best ways to invest in real estate is through publicly traded Real Estate Investment Trusts (REITs), which allow investors to access the benefits of this sector, while also maintaining liquidity.

The public REIT sector was launched in the early 1960s and has been traditionally categorized into five main sectors: office, retail, residential (mostly multi-family), industrial, and hotels. As the sector matures, real estate investors are becoming more specialized, seeking to capitalize on secular growth trends and cater to tenants with specific building/location requirements for their product or service offerings. This specialization includes targeting property types such as:

- **Life science**
- **Data centres**
- **Cell towers**
- **Self-storage**
- **Gaming**
- **Single-family rentals**
- **Manufactured homes**
- **Student housing**
- **Medical offices**

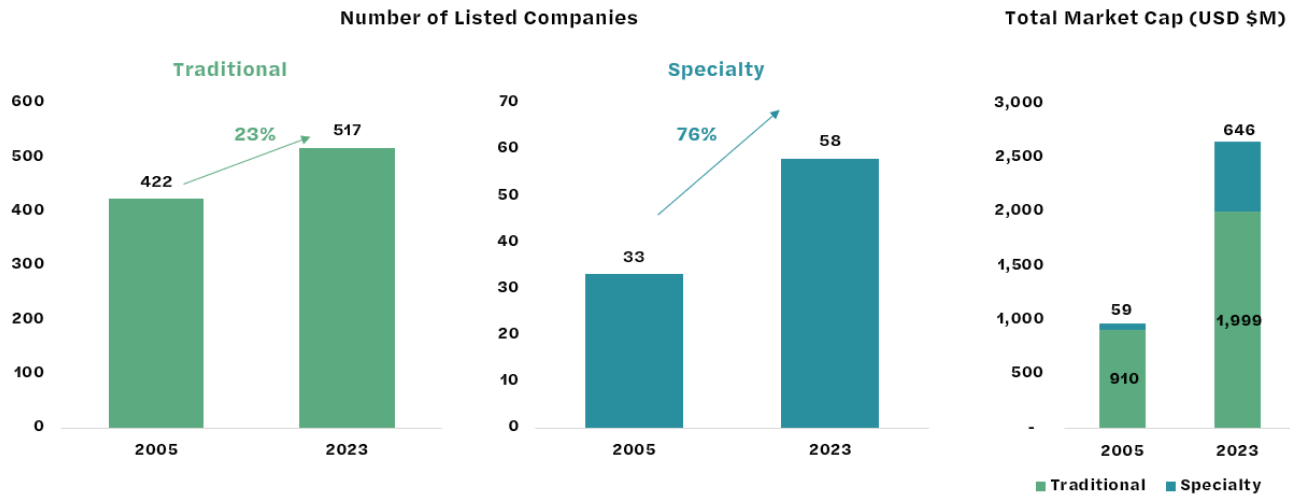
Specialty REITs have become a significant component of the overall global public REIT market in recent years, both from a size and performance perspective. We believe these companies should be considered in the construction of any real estate investment portfolio and any broader equity markets investment portfolio, to further improve diversification, to efficiently access secular growth trends, and to ultimately enhance portfolio returns. However, investing in specialty REITs requires careful consideration of each property type's unique drivers of success.

At Hazelview, we have devoted over a decade to analyzing and understanding the specialty REIT sector. Through our experience, we have gained valuable insights into the fundamentals of various property types. In this series of articles, we aim to share our knowledge and expertise, providing an in-depth examination of the sector as a whole and delving into specific property types. We trust that you will find our content both informative and engaging.

The Evolution of the Specialty REIT Sector

Over the past 18 years, publicly traded REITs targeting specialty property types have grown substantially. The number of publicly traded REITs that have specialized strategies increased by 76%, relative to 23% growth of traditional property type REITs. Specialty REITs now represent almost 25% of the global REIT market.

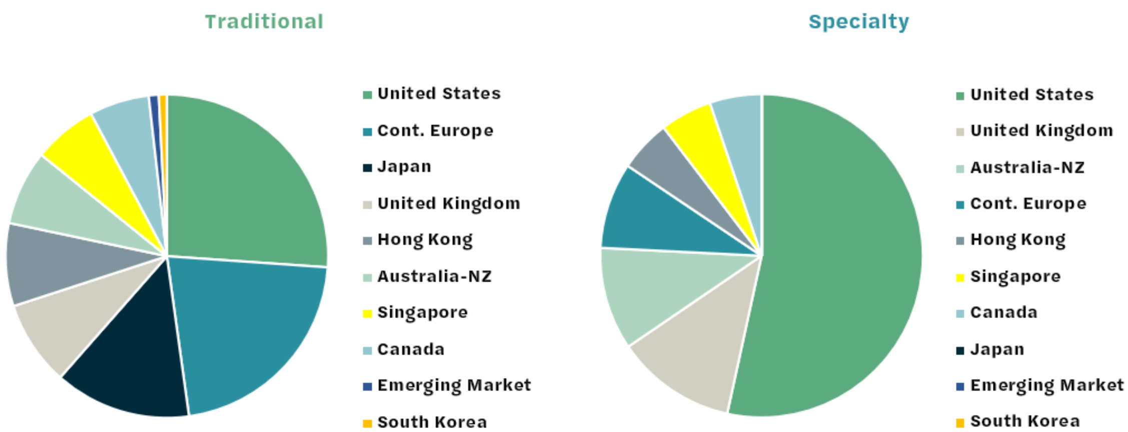
Growing Market Share



Source: Bloomberg, Data from 2005 to September 30, 2023.

In fact, the average market cap for specialty REITs is now higher than traditional REITs. While specialty REITs made their debut in the United States, more recently, the sector has expanded to other global markets including the emergence of cell towers and data centres in Europe and Asia, life science in Europe, student housing in the United Kingdom, and self-storage in Australia and Europe.

Geographic Exposure

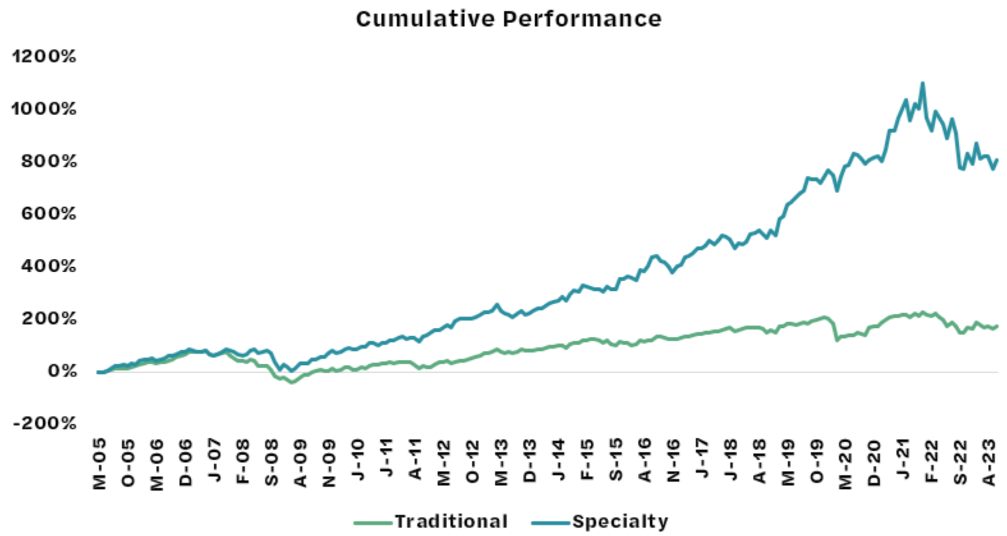


Source: Bloomberg, Data as of September 30, 2023.

Strong Relative Performance

The exceptional growth of speciality REITs can also be attributed to their strong relative performance where, over the past 15 years, they have outperformed traditional REITs by 5x.

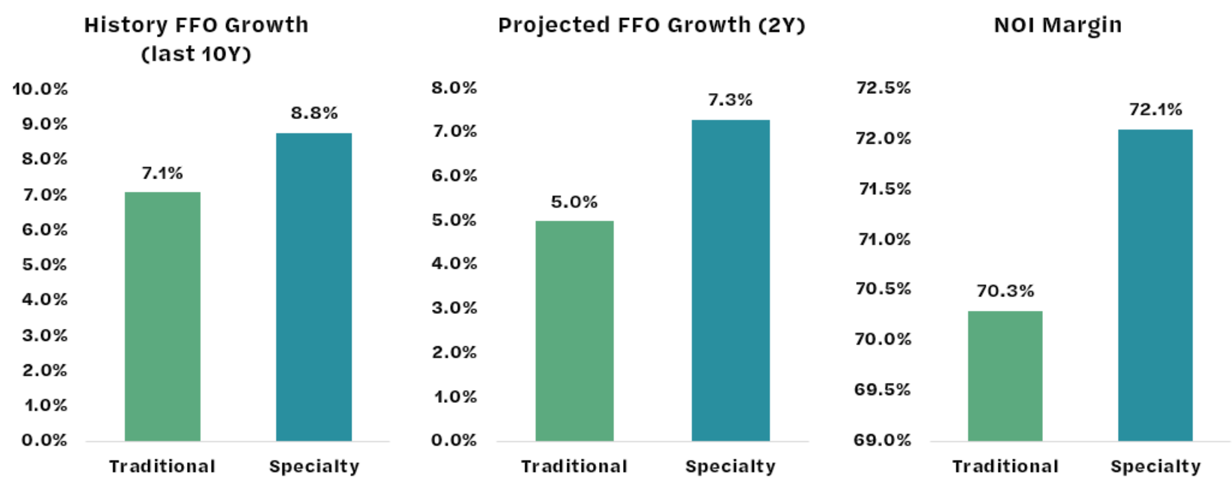
Correlation



Source: Bloomberg, Data from 2005 to September 30, 2023.

This strong performance is driven by the fact that specialty REITs have historically demonstrated higher margins and better income growth, making them more profitable.

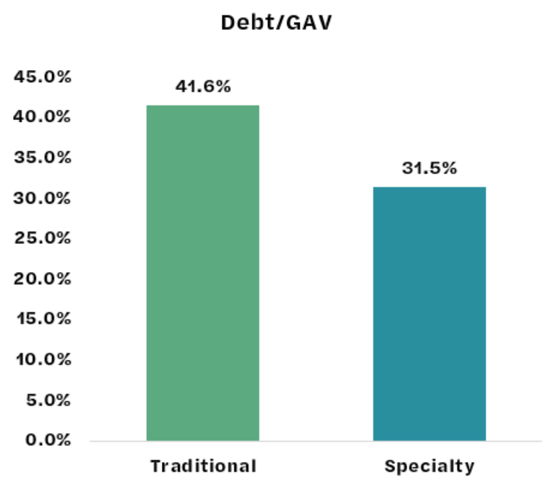
More Profitable and Faster Growth

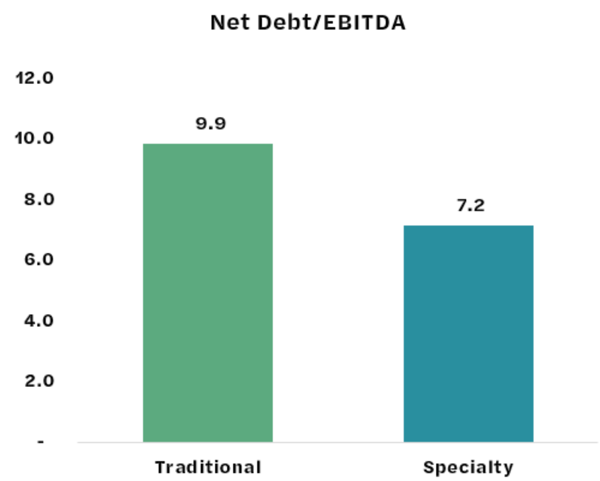


Source: Bloomberg and Hazelview's Underwriting, Data as of September 30, 2023.

Specialty REITs have also traditionally been more conservatively capitalized, with lower levels of debt and better debt service coverage. These strong underlying fundamentals have historically resulted in specialty REITs trading at a higher multiple than REITs that are focused on traditional real estate property types.

More Conservatively Capitalized





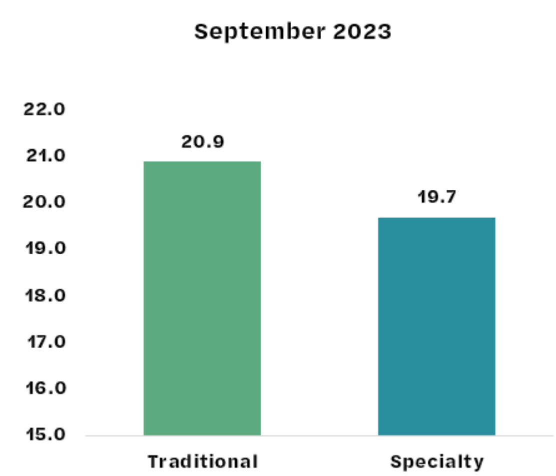
Source: Hazelview's Underwriting, Data as of September 30, 2023.

Recent market conditions, however, have that scenario reversed. We believe there are numerous reasons why specialty REITs trade at lower trading multiples today, some of which are technical in nature (i.e., fund outflows, investor positioning, and style preferences such as growth sectors being out of favour), while others are valuation specific (i.e., influence of rising real interest rates on trading multiples).

Better Value Relative to Growth

EBITDA Multiples

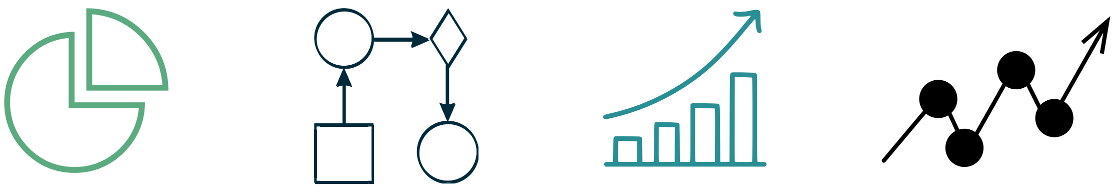
Source: Hazelview's Underwriting, Data as of January 1, 2023.



Source: Hazelview's Underwriting, Data as of September 30, 2023.

Conclusion

Growing Importance | **Provides Diversification** | **Financial Benefits** | **Proven Outperformers**



Whether you are a public REIT investor looking to outperform, a private real estate investor looking to complement your existing portfolio, or a broader equity markets investor looking to take advantage of secular growth opportunities, adding specialty REITs to your investment portfolios can provide meaningful benefits, which ultimately enhance returns.

To gain a deeper understanding of the distinct characteristics of these investments, we invite you to follow our upcoming series of articles.