BDO GLOBAL REIT REPORT

JANUARY 2018

BDO

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INTRODUCTION FROM RUSSELL FIELD

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Like all real estate companies, REITs find themselves at a turning point at the beginning of 2018. Our survey of 35 companies from across the world with a combined market capitalisation of $130bn found that the majority felt the real estate cycle in their market was at or past its peak.

However, notwithstanding this, the REIT leaders interviewed were on the whole very confident about their ability to weather any oncoming headwinds for the real estate sector. Lowly geared and not overexposed to development, the sector looks much better placed to endure a downturn than before the onset of the last financial crisis.

As for where the sector as a whole heads from here, REIT leaders feel that the sector will continue the last decade's trend of expansion in spite of the fact that depressed share prices in some countries will inevitably lead to privatisations and consolidation.

But there was also a feeling that in order to appeal to shareholders beyond the traditional REIT specialists, companies in the sector need to be more true to their label and prioritise income returns over capital growth.

In terms of the specific issues occupying the minds of REIT senior management, the impact of interest rate rises was cited as the foremost short term issue. But again, while most felt that rates were set to rise soon, they also thought that REITs could stomach a rise of 100 basis points or more before this would start to have a significant effect on their business.

In the longer term, it is the impact of millennials' aspirations within the workplace that they feel will have the biggest impact on their business models. Conversations with some of those very millennials reveal that above all they want a workplace that helps to foster egalitarianism and gives them the ability to learn.

1 WHAT DOES THE FUTURE HOLD FOR THE GLOBAL REIT SECTOR?

The REIT leaders canvassed for this report are confident that the listed real estate sector will continue to grow and to thrive.

In the longer term there is a feeling that a more standardised global REIT regime could help the sector in both emerging and mature geographies.

In the more immediate term, REIT leaders felt that there are changes afoot that could make the sector more appealing to generalist investors; and that in some jurisdictions the discount to net asset value at which many REITs are trading at this point in the cycle will lead to merger and acquisition activity.

The REIT sector has grown significantly in the last decade; both in terms of REITs being introduced in new countries, and in terms of an increase in the size of the sector in existing jurisdictions.

Data from NAREIT shows that the market capitalisation of the US REIT sector has more than tripled to $1trn in the past 10 years, with the number of REITs growing from 152 to 224.

In Europe growth has been slower, but according to EPRA the market cap of the listed European real estate sector has grown by a third in the same period from €150bn to €200bn.

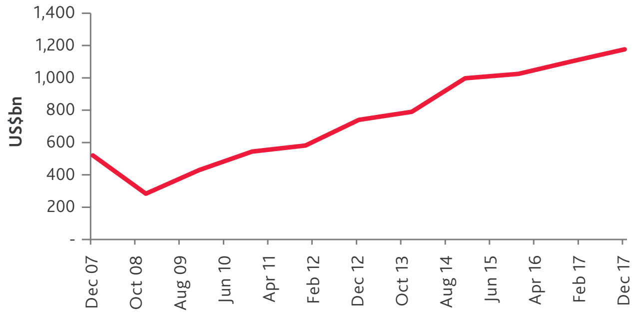
In Asia the REIT sector has grown by almost two thirds, from $135bn to $213bn, according to data from Consilia Capital.

And there is confidence among those canvassed that this pattern will continue. Slightly less than half of REIT leaders felt that the listed real estate sector will continue to grow in the next 12-24 months, with around a third feeling it will stay roughly the same size.

One respondent to our survey said:

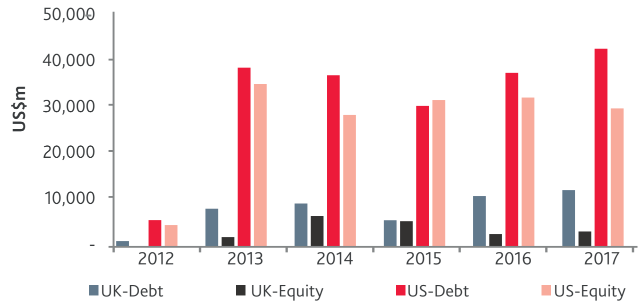
> "My guess is that the REIT sector will continue to expand. Via dividends and capital appreciation it has provided investors with attractive risk adjusted returns for quite some time now, and I think it will continue to grow."

Size of the REIT sector - 2007-2017
Index Market Cap (US$0,000's)



Source: Consilia Capital/EPRA

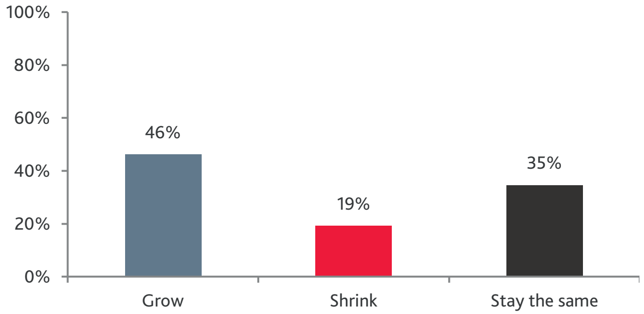
Capital Issuances (US$0,000,000's)



Source: SNL/ Green Street Advisors
Equity includes follow-on and convertible offerings and does not include IPOs

1.1 HOW THE REIT SECTOR WILL CHANGE

Will the listed sector grow or contract in the next 12-24 months?



Source: BDO

> This sort of market and strategy was exactly what a REIT was supposed to do. Very few of the real estate companies that converted behave as true REITs. They got a tax break but didn't actually change their real estate strategy and are not focusing on income. The iPhone was launched at the same time as REITs in 2007 - one of those things has evolved considerably, the other hasn't.
>
> **ANDREW JONES**
> CHIEF EXECUTIVE, LONDONMETRIC
> *(Discussing the UK market in particular)*

REIT leaders were asked how the sector could grow and change, how the shareholder makeup of REITs was likely to change over the next few years, and in particular how more generalist investors could be attracted to a sector which has to some degree been the preserve of specialist real estate equities funds.

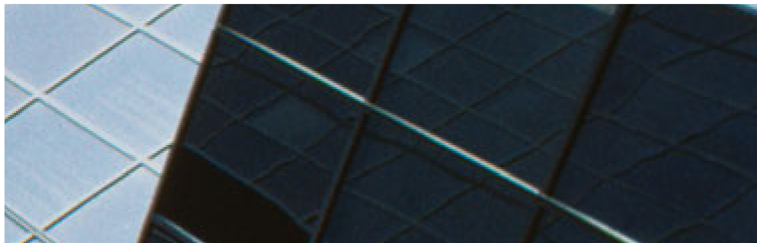
There was a myriad of responses to these broad questions, but they can be broken down into variations on three themes.

The first is that listed companies should "stick to their knitting", which is to say try as much as possible to be highly focused on particular sectors and geographies rather than pursuing a diversified strategy, or altering their overall strategy too much as the cycle evolves.

Secondly, there was a feeling that REITs needed to have a greater focus on income rather than capital appreciation or development. The appeal of real estate over the long term is the steady and stable return the sector provides, and listed real estate gives investors access to this via a liquid vehicle. But too many REITs have focused on growth from yield compression and development, creating more volatility in returns and turning investors off. At this point in the cycle, even as values begin to peak and perhaps fall in some markets, the income provided by listed real estate should be highly appealing, but that is not always proving the case.

The third main point was around liquidity and scale, and the need to create large and liquid companies so that generalist investors in particular could compare listed real estate companies to other sectors of the market.

> You can be compared to large companies in other sectors and be compared with the best companies in other sectors. At the moment you only have two REITs in Europe that have that kind of premium due to size and quality of management and that is Unibail and Vonovia. I think it will change as the companies get larger - with smaller companies it is harder to differentiate yourself.
>
> **MEKA BRUNEL**
> CHIEF EXECUTIVE, FRENCH RESIDENTIAL AND OFFICE FOCUSED REIT, GECINA



1.2 BDO VIEW: SHAREHOLDER APPEAL, A VIEW FROM THE UK

REITS ARE AN ACCEPTED FIXTURE IN THE CONTEXT OF UK REAL ESTATE INVESTMENT AND ARE INCREASINGLY VIEWED AS THE GLOBAL STANDARD FOR INVESTORS SEEKING EXPOSURE TO PROPERTY AS AN ASSET CLASS.

Whilst there are differences between individual country REIT regimes, a number of distinct hallmarks attach to the REIT "wrapper". These hallmarks specifically commend themselves to investors. The four key hallmarks of REITs are:

TAX EFFICIENCY AND PROFILE

This is a key benefit. In summary, provided that REITs are able to meet certain tests in relation to their business and corporate structure they will, for direct tax purposes, be treated as tax-exempt with the tax point being moved to the investor. Where the investor is exempt from tax (as in the case of a pension fund) then a tax liability is potentially avoided.

ACCESS TO SPECIFIC REAL ESTATE ASSETS AND EXPERTISE

REITs provide efficient access to specific classes of real estate asset including commercial offices, retail and healthcare. In addition, they provide investors with access to dedicated and expert property management teams.

PRODUCT LIQUIDITY

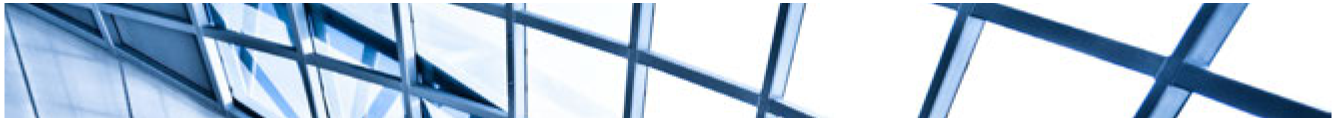
REITs can provide liquidity to an asset class which would, otherwise, be viewed as highly illiquid in nature and where transactional costs can be significant. This is a valuable attribute.

TRANSPARENCY AND PRODUCT QUALITY

REITs are perceived as a defensive asset class with low volatility and predictable, increasing revenue streams. In addition, REITs allow for a high degree of shareholder visibility over the underlying assets and permit meaningful comparisons of product performance.

The REIT regime has successfully existed in the UK market for over ten years and is well-established.

We see the depth of the market increasing with the introduction of more niche products; this trend will serve to enhance the appeal of this asset class and commend it to a wider circle of increasingly sophisticated and discriminating shareholders.



There are some broader trends in equities markets that were highlighted as having a potential impact on the REIT sector. One was the rise of passive investing and index funds. According to data from Bernstein Research by early 2018 around 50% of all financial assets under management in the US will be in passive funds.

The issue for real estate companies is that passive investing can amplify both upswings and downswings.

HIRA SHARMA
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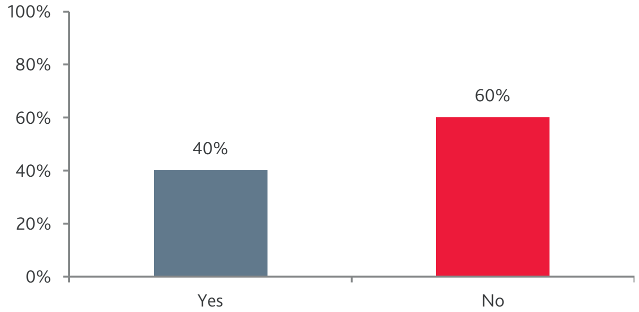
1.3 WHAT DOES THIS MEAN FOR M&A?

> The rise of index funds puts us in uncharted territory. I have every reason to believe that markets will find an equilibrium. But the rise of index funds creates a certain level of disequilibrium for extended periods of time. Again, if that's the case and certain companies are not trading at NAV or a premium then at some point those companies and their boards will figure out how to close that gap.
>
> **KEN BERNSTEIN**
> CHIEF EXECUTIVE, US RETAIL REIT, ACADIA

ONLY AROUND A THIRD OF THE REIT LEADERS WE INTERVIEWED SAID THEY THOUGHT THEY WOULD BE LOOKING AT M&A IN THE NEXT 12-24 MONTHS.

Will you look to undertake an M&A transaction in the next year?



Source: BDO

But there is an expectation that consolidation and privatisations will occur at this point of the cycle. Ken Bernstein highlights the fact that companies trading at discounts to NAV for a persistent period of time can expect to draw interest in from private equity looking to take advantage of the strong demand that exists for good quality assets in the private market.

One executive interviewed added that some REITs operating in emerging real estate asset classes could also see consolidation.

> For M&A activity I see it more in the newly emerging spaces in the REIT market rather than traditional sectors like office, industrial, residential and retail. You have already seen it in single-family homes for rent and I think you will see it in tech areas like data centres and cell-phone towers. Some of those new areas will see consolidation.

REIT leaders were asked how companies could close discounts to NAV. The answers must of course be judged against a backdrop of the fact that, in some countries like Australia, REITs are on the whole trading at premiums to NAV; and the fact that in many cases those discounts will be narrowed when the value of assets in the private market fall and come closer into line with the value of shares.

Again there was a wide variety of responses, with many interviewees touching on issues such as focusing on income rather than capital values and development.

But an answer that also cropped up consistently related to the quality of the management of REITs, and the fact that if senior management could demonstrate a strong track record of stable returns, primarily driven by income, then shareholders would reward them with a premium compared to their peer group.

Gecina's Brunel touched on this with her comments on why Unibail and Vonovia are highly rated among investors.

> It is not just the size of your assets but the capacity of your team, your leadership and putting in place a structure. Really what are we saying when we say WeWork is overvalued? They don't own the assets, real estate companies do, but they are valued more highly because they are better managers of real estate.
>
> **MEKA BRUNEL**
> CHIEF EXECUTIVE, GECINA

CREATING NEW REIT REGIMES

In terms of encouraging the creation of new REIT regimes around the globe, there was a feeling that the creation of a global REIT regime would help the sector expand, with almost three quarters of those interviewed saying this would be a good thing. Even if a global REIT regime would be difficult to achieve, greater standardisation of regulations regarding REITs was seen as positive for both companies and investors.

> If a country is setting up a REIT regime without that standardisation it will make it hard to attract investors. Real estate already has a challenge in that it is different to a lot of other sectors, so anything you can do to make it easier for investors is important.

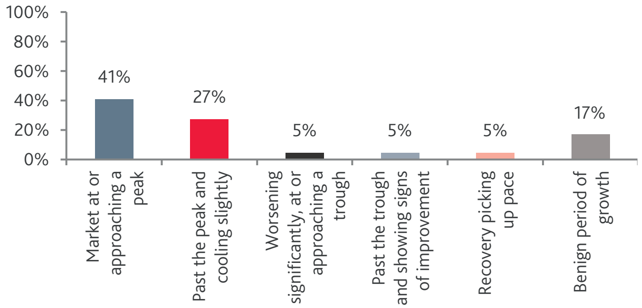
A GLOBAL VIEW

An example is the Philippines. REIT legislation has been in place since 2009 but no companies have so far converted to REITs. This is because of both push and pull factors. The free float companies are required to have is lower than in other countries, reducing the appeal for investors. And the amount of tax REITs have to pay annually would be higher than in other jurisdictions, reducing the incentive for companies to convert. So a country with a strongly performing real estate market has no REIT sector and therefore becomes harder for International capital to access.

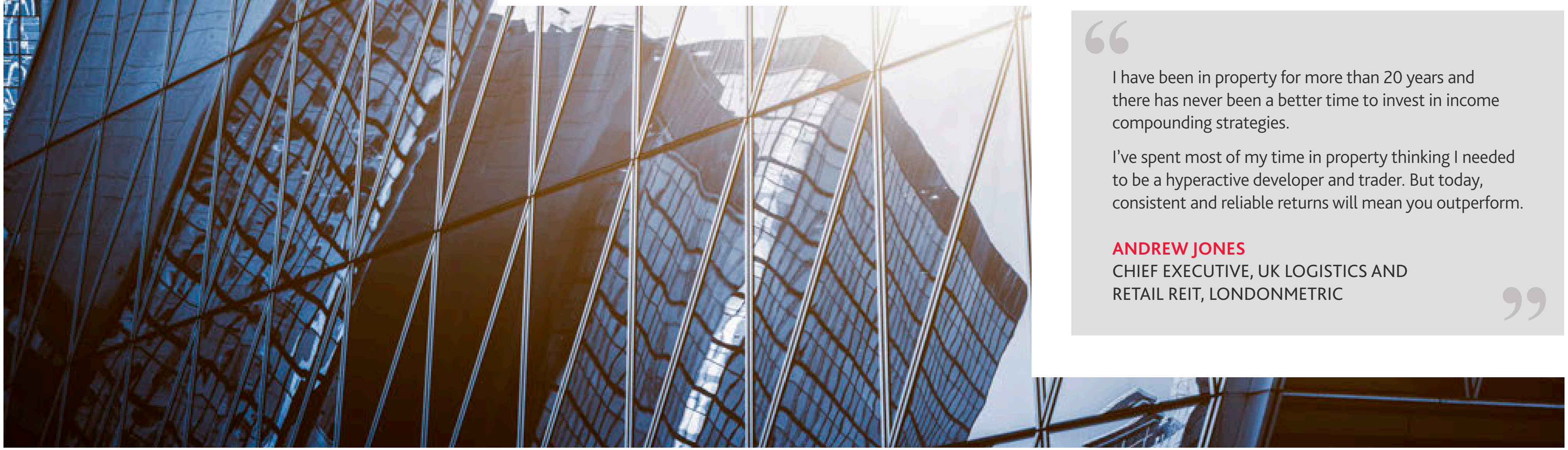
2 CONFIDENCE AND THE PROPERTY CYCLE

The majority of REIT leaders canvassed for this report think that the real estate cycle in their market is at or past the peak - but they do not feel overly worried about this, and remain confident about the prospects for their business. The leaders of companies in developed markets like the UK, US and Australia were the most likely to exhibit this view.

Where is your local REIT market in the real estate cycle?



Source: BDO



It is not hard to see why REITs might take this view - yields are at record lows in many markets, with little prospect of further capital value appreciation, economic growth in many markets is patchy and rising interest rates could erode the appeal of real estate.

What is perhaps surprising is that even though there is a clear feeling that real estate is late in the cycle, this is not particularly hampering the confidence of REIT leaders with regards to the prospects for their business or making them dramatically alter their strategy.

What factors might explain this potential paradox between a cycle coming to or beyond its peak and the confidence exhibited by those running REITs at this time? The answer seems to lie in the fact that REITs as a whole are set relatively fair to withstand the peaks and troughs of the cycle.

> I have been in property for more than 20 years and there has never been a better time to invest in income compounding strategies.
>
> I've spent most of my time in property thinking I needed to be a hyperactive developer and trader. But today, consistent and reliable returns will mean you outperform.
>
> **ANDREW JONES**
> CHIEF EXECUTIVE, UK LOGISTICS AND RETAIL REIT, LONDONMETRIC

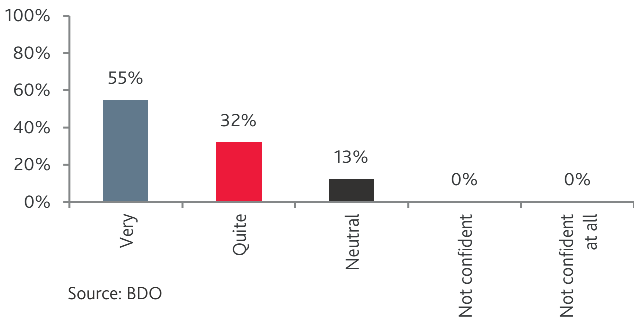
2.1 BUSINESS CONFIDENCE AND ATTITUDES TO RISK

On the development side, about a fifth of REIT leaders interviewed said they were looking to take on more development exposure, while just 5% said they were looking to reduce development exposure - a sign that on balance more REITs are confident about the prospects for rental growth in their market than not.

Finally, there is a balanced view of whether the large amounts of capital flowing into real estate have made the sector inherently more volatile - those surveyed were split precisely 50/50 over whether real estate prices will see significant volatility in future.

As a result, a slightly greater proportion of those surveyed envisage themselves being net buyers rather than net sellers, which demonstrates their confidence in the markets in which they operate. The majority of those buying feel they will invest up to around US$250m during the next 12 to 18 months.

How confident are you about the prospects for your business over the next 12-18 months?



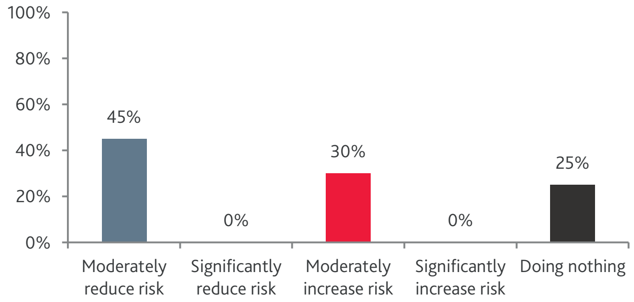
Source: BDO

Furthermore, many of those surveyed do not necessarily feel excessively inclined to reduce risk as a result of real estate's position in the cycle.

Of those surveyed the largest proportion, almost half, said they were looking to moderately reduce risk, but a further third said they were looking to moderately take on risk. The remainder said they were happy to keep things just as they are.

In terms of how they go about achieving their stated aims, BDO asked respondents about their attitudes to debt levels, development exposure and asset sales. It was pretty much balanced between those that said they wanted to reduce leverage against those that would maintain current debt levels or increase them.

Are you looking to reduce or increase risk in the current market?



Source: BDO

2.2 EQUITY, DEBT AND CROSS-BORDER INVESTMENT

Real estate values are high in most developed markets indicating compressed capitalisation rates. This has made it more difficult to locate and execute profitable acquisitions.

Those surveyed by BDO are not targeting excessively high returns - they ranged from 7-12%. With yields compressing these returns are difficult, but not impossible to achieve.

REITs in markets like the UK and Australia seem particularly to have learned the lesson from the last crisis. In the UK and Australia many of the largest REITs had to undertake "rescue" rights issues caused by high gearing and the subsequent devaluation of properties that occurred during the Global Financial Crisis (GFC).

This time around REIT's have been capitalising on rising real estate values by selling non-core assets at record high prices to reduce gearing and in some cases to return cash to shareholders.

REITs on the whole are not highly leveraged or long on development - the two situations which have historically led to issues during real estate downturns. Development exposure is capped by regulation in most REIT regimes. And in terms of debt levels, REITs typically have lower than average gearing – data from Green Street shows that UK listed property companies have an average loan to value ratio of just 32%, with the US at 33% and Continental European firms slightly higher at 44%. Australia is also low at around 30%.

When asked specifically about debt, slightly more than half of investors said they were looking to decrease leverage. Debt levels are already low but companies are realising that continued investment in their stock or the sector generally hinges on the stability and risk management of assets. Clearly, it cannot hurt to have gearing lower, especially in a market where high values can make it difficult to reinvest the proceeds of asset sales.

> We're as lowly geared as we've ever been, which means if values do fall it won't affect adversely affect us. Gearing is great in an upward market but negative in a downward or flat market, so we are prepared if the market does turn.
>
> **TOBY COURTAULD**
> CHIEF EXECUTIVE, UK REIT,
> GREAT PORTLAND ESTATES

REITs are, on balance, looking to reduce debt and also to diversify it. Of those surveyed, almost all currently use bank debt and half use bonds. That latter number is set to grow, with around half of those who said they were looking to use new forms of debt saying they are looking to tap the corporate bond markets. UK and European companies are also looking at the US private placement market and the German loan note market (Schuldschein). Many REITs have also taken advantage of Sovereign Wealth capital to help reduce debt and increase capacity for acquisitions.

A key focus of gearing has been to increase the term of the debt and to effectively hedge the debt. This is viewed favourably by investors as it reduces the perceived risk of the investment.

REITs seem in little need of new equity capital according to the responses of those questioned. Less than half said they were looking to raise new equity. Of those that would look at raising new equity, around a third would do so via a share placement, and a fifth would do so via asset sales. This is in spite of the fact that equity raising levels in the secondary market are buoyant.

REITs also seem happy currently to go it alone - almost two thirds said they were not currently looking to set up joint ventures for either investment or development. The likely rationale for this is that most companies have focused on de-risking their operations, increasing weighted average lease expiry, locking in longer term debt and ensuring the debt is effectively hedged. This is to ensure that any geo-political or macro-economic factors that are prevalent in the world are mitigated somewhat should they occur.

> The interest from private capital in the kinds of buildings we own continues to be high, from both domestic and offshore investors. If we had a need to raise capital for new investment we would consider joint ventures, but right now we are able to fund this ourselves.

To better understand this situation, it's important to understand the context of the previous foray abroad. At that time with soaring asset values, increased gearing to increase yield, fund managers looked off-shore for "bargain" assets that would assist the continued growth of the investment. Some of the countries invested in were hit particularly hard during the GFC and this had a devastating effect on the performance of the REITs during that time and there is an unwillingness from investors to repeat that situation.

One of the key factors is that investors entrust management to invest on their behalf and that management needs in-depth experience of their market. When local fund managers started looking abroad they didn't have that in-depth knowledge of the market and suffered as a result. Thus, investors made it very clear that they backed local expertise and local investment.

In fact, this tendency to stay at home is exhibited in the results of the survey and common to REITs from all parts of the world. Just a fifth of those surveyed said that they were considering undertaking a cross-border strategy. As several investors pointed out when asked how REITs could increase their appeal to investors, "sticking to the label" and presenting a focus in a single sector or geography is very much valued in the current market.

To illustrate this point, the Australian REIT market has seen some stellar performance from niche or specialist REITs investing in rural, pubs and healthcare to name a few.

One area of cross border transactions that is likely to continue in 2018 is the prevalence of cross border M&A. Merging with a larger entity or acquiring their key management effectively eliminates one of the key stress points of cross border work; the risk of local management not having the skills to manage an overseas portfolio if the entity buys the cross border target.

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2.3 BDO VIEW: REGULATION, A VIEW FROM THE EU

The GFC that shook the world from 2007 caused regulators everywhere to recognise the importance of the 'real estate' sector to modern economies. By most measurements, it constitutes anywhere between 7 to 20% of emerging and developed economies GDP. Taken in its totality, the real estate and construction sector is now generally recognised to be of systemic importance, particularly when leveraged investment is included.

The GFC triggered a number of reactions among policymakers and regulators to systemic sectors that were seen to have contributed to the crisis. One of those reactions was to bring forward a tsunami of regulation, some of it absolutely necessary and overdue, but elements of it now seen to have been ill-thought out and poorly coordinated with other jurisdictions. The listed property sector was one of the industries affected by this regulatory reaction and the rules that the industry must follow (or not, as the case may be) continue to be of chief concern to those we surveyed for this report.

Over 10 years on, much of the regulation that affected the sector in its widest sense, including that around REITs has proven to be overly complex, fragmented across jurisdictions, occasionally in conflict with other domestic regulation and all too often designed to dampen investment rather than facilitate it. Regulation of REITs lending, governance, transparency, Basel 3 capital requirements rules as well as new financial reporting standards have changed the environment considerably. Taken with the societal expectations around environmental, sustainability and governance (ESG) issues as well as the now universal concerns in the cybersecurity space, the aggregate effect has been to militate against a cohesive globally consistent regulatory and investment environment for REITs.

Complex and lengthy pieces of legislation such as Dodd-Frank in the US, the AIFMD in the EU and changes brought about through new fair value accounting standards coupled with uncertainty around tax laws and regulatory compliance costs shape the environment for REITs, particularly for global investors.

There are examples of progressive jurisdictions in this regard however, notably India among the larger economies, where focussed changes in REITs regulation has enabled a substantial pool of new investment avenues to be tapped and for the sector to be now seen to be supporting overall economic development. I would hope that other jurisdictions would seek to follow suit to secure the benefits of a well-regulated but vibrant REITs and real estate sector for their economies.

NOEL CLEHANE
GLOBAL HEAD OF REGULATORY AFFAIRS AND PUBLIC POLICY

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3 INTEREST RATES

WHEN INTEREST RATES WILL RISE AND HOW FAST IS THE OVERWHELMING TOPIC OF CONCERN FOR REIT LEADERS ACROSS THE GLOBE.

Fully two thirds of those surveyed said the movement of interest rates would be the biggest influence on REITs in the next 12 to 24 months. CEOs from Mexico to Malaysia said that central bank policy decisions would exert the largest influence on the performance of their sector, and it's not difficult to see why.

REITs have been a significant beneficiary of the huge flow of capital which the real estate sector as a whole has received as global interest rates and bond yields have tumbled in the wake of the financial crisis.

Central banks lowered interest rates to near zero in major economies like the US, UK and Europe between 2009 and 2013, and prime real estate yields in comparison look attractive.

Even though real estate yields are themselves at record lows in many countries, and that spread has narrowed in the past year, the spread is still well above historic norms according to Real Capital Analytics.

Listed real estate has been a major beneficiary. In the seven years after central banks slashed interest rates in 2009, US real estate stocks returned an average of 16%, the UK 11% and Continental Europe 9%, in spite of the latter facing a currency crisis in 2011 and 2012.

So while it is not the only factor affecting the sector, it is clear that the trajectory of interest rates is of major importance to REITs. And as is so often the case, the listed sector will be a leading indicator for real estate as a whole, with equity valuations pricing in movements in rates in advance of the private market.

For example in 2015, as it became clearer that the US Federal Reserve would raise interest rates, the MSCI REIT Index fell 20% after five consecutive years of gains, whereas in the private market 2015 was the second largest year for transactions on record.

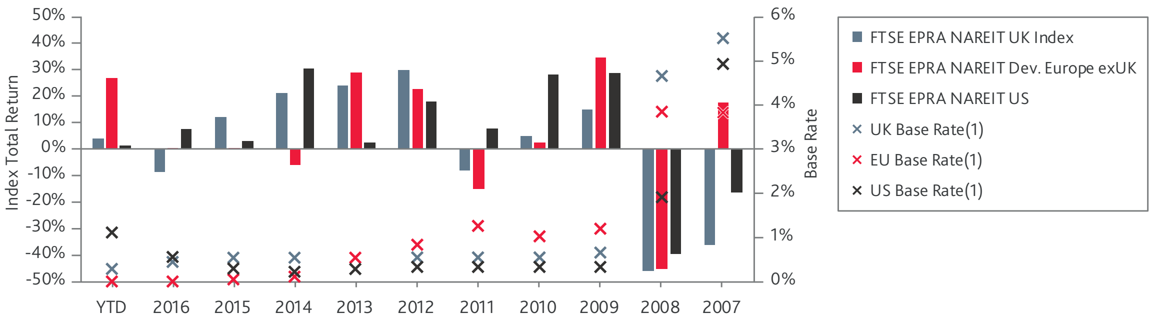
So how worried are REIT leaders about rising interest rates? How big of an increase do they think the sector can absorb before the attractiveness of real estate is eroded and prime yields begin to rise?.

Of course there was a range of answers from our survey respondents. One made the point that "if rates are up because the growth outlook is better and rents rise, then the increase could be substantial in rates before current yields are impacted. If rates rise with no corresponding increase in the growth outlook, then there isn't much room for rates to increase before current yields would also need to rise."

Rounding up slightly, the median answer from those surveyed was that interest rates could rise by 100bps points before real estate yields started to come under upward pressure.

Survey respondents were also keen to point out a distinction which could be described as a difference between 'good' interest rate rises and 'bad'; "real estate valuation is never about a simple correlation between the cost of debt and the valuation yield…
If rates rise at a time when there is GDP growth or a strong prospect of it, then a hefty increase in rates could be tolerated."

Regional Real Estate Indices Annual TR vs. Base Rates



Source: Green Street Advisors, FTSE Russell, Bloomberg

Of course different jurisdictions have different forward curves projecting interest rate movements which means differing outlooks for their respective REITs. In the UK the Bank of England recently raised interest rates for the first time in a decade and may raise them again, albeit slowly, against a backdrop of subdued growth as Brexit uncertainty continues.

In Europe there is little indication that the European Central Bank plans to stymie any economic recovery by raising rates. In the US the Fed chairman has indicated that rates will continue to rise gradually, and in China rates have also been rising. Hong Kong has the narrowest spread between interest rates and yields, according to Real Capital Analytics.

And it is also the case that REIT leaders have not bought into the idea that prime real estate has undergone a paradigm shift, as has been suggested in some quarters, with such assets now trading at permanently lower yields as institutional investors become more knowledgeable and exposed to the sector. Just a fifth of those surveyed feel that real estate yields have taken a permanent shift down and will stabilise at current levels. The real estate cycle is still present and correct.

US TAX REFORM

While the trajectory of interest rates was cited as the most important factor impacting REITs over the next 12-18 months on a global level, for US REITs one other factor was also consistently referenced - the tax reforms proposed by president Donald Trump and the Republican Party.

On the whole markets appear to believe that the proposals put forward are broadly favourable for US REITs - the sector rose on November 3 2017, the day after the reforms were announced. Measures seen as positive include the 25% cap on the tax rate payable on REIT dividends, bringing the sector into line with other equity sectors. The overall cut in tax rates is seen as positive for business and therefore for real estate, although the fact that corporation tax will be cut makes tax exempt sectors like REITs less attractive.

It still remains to be seen however whether the reforms can make their way through Congress in the current volatile US political environment.

3.1 BDO VIEW: INTEREST RATES, A VIEW FROM THE USA

The US Federal Reserve is set to continue implementing gradual interest rate increases under the incoming chairman Jerome Powell. While US interest rates remain relatively low compared to the broader global market, today's rates are a far cry from their seven-year stint at 0.25%—a rate of effectively zero—during the Recession.

REIT senior management are among those evaluating the impact of rate increases to their earnings and valuations. While REITs rely to varying degrees on debt to finance their investments, all REITs could be impacted if the expected increase in interest rates result in more than minimal increases in capitalisation rates.

Despite the potential for short-term strain, the Fed's decision to implement gradual rate increases suggests renewed economic confidence, which should benefit REITs in the long term. Strong economic fundamentals historically trigger a positive chain of events for REITs, leading to increased rents and occupancy rates, which could offset the steeper cost of financing and the impact of rising capitalisation rates on valuation.

However, a positive impact for REITs is predicated upon whether the forecasted economic recovery is realised, and all eyes are on inflation, which is a key economic indicator. The US core inflation rate is not expected to hit the Federal Reserve's 2% goal until 2019. How inflation evolves will be the X-factor for the market and REITs moving forward.

It is also worth pointing out that, with prime yields at record lows, it would be lower yielding assets that would be hardest hit by any rise in rates.

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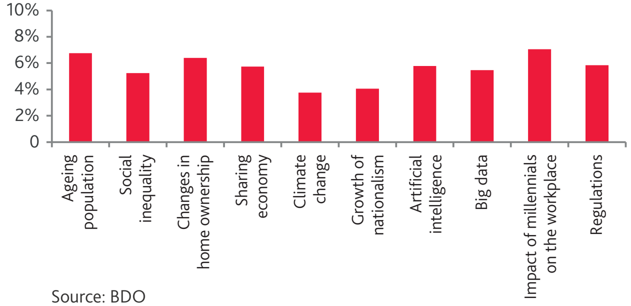
4 THE TRENDS THAT WILL AFFECT REAL ESTATE LONG TERM

What change in social behaviour, demographics or technology will have the biggest influence on real estate in the coming years?



Source: BDO

To conclude the report, interviewees were asked to play the role of prognosticator, and rank a series of societal, demographic and technological trends according to which they felt would have the biggest influence on their business over the coming years.

Looking first to what worried interviewees the least, the bottom two ranked trends were the rise of nationalism and climate change. This perhaps reflects the short-term waning of the growth of nationalism that dominated the headlines particularly in Europe at the beginning of 2017. Elections in France, the Netherlands and Germany did not turn out as badly as some feared, and in the US talk of rolling back NAFTA has receded - for now.

A lack of focus on climate change is perhaps a result of the opposite - an inability to extrapolate the long-term consequences of a very real phenomenon and apply that to businesses that look to maximise shareholder returns over the short to medium term. The same is perhaps behind the low ranking of the consequences of growing social inequality.

Towards the middle to bottom of the list of trends that will impact REITs in the next few years was big data and artificial intelligence, two technological trends which are constantly in the headlines. REIT leaders are still at the stage where they can see that such technology will have an influence, but the precise manner this takes is still very far from clear.

Towards the top of the list was the ageing population, a long-term trend which REITs can already get their heads around. Its affect for listed real estate is two-fold. First there is the impact on the real estate itself - the need for more senior living and healthcare facilities and more housing as people live longer.

And there is also the fact that as populations age, pension funds and insurance companies have an ever greater need for secure and stable long-term income to match their growing liabilities. REITs should be an excellent vehicle to provide this, especially in a low interest rate environment.

But it is to the other end of the age spectrum which REITs have particularly turned their attention. The impact of millennials on the workplace was deemed the change that would have the biggest impact on REITs over the next few years.

There are various characteristics that are common to the people in their late teens and 20s that are entering the workforce in urban locations around the world. These will impact the kind of real estate that REITs are looking to buy and develop.

Myriad issues are feeding in to what millennials want from the workplace, touching on factors as varied as technology, health and wellbeing and good food and coffee. The need for companies to have real estate that attracts the most talented new staff is something of a cliché, but that does not make it any less true. What does it mean in practice?

For this report we interviewed four of BDO's own millennials from around the world - in the UK, US, Australia and India, to give a snapshot of the social and emotional issues that will have a direct impact on the way the workplace of today and tomorrow operate.

What people want from a workplace can be incredibly geographically specific, but there were also interesting themes that seem to cross international boundaries.

It is worth focusing on one point which interviewees from across the world all raised as the most important element of their working environment.

When discussing modern, open-plan offices, and the positives of corporates adopting strategies like activity-based working and hot desking, collaboration is often cited as the primary benefit. And this is clearly important.

> We have just transferred to a new office, and in the old office you had cubicles and offices. You wouldn't see people if you weren't going to their desk directly or didn't see them in the lunch room. Now people are a lot more interactive, you bump into people, everyone gets to know each other and works with each other.
>
> **MATTHEW FULLER**
> AUDIT ASSOCIATE, REAL ESTATE AND HOSPITALITY SERVICES
> NEW YORK, BDO USA

But there is another factor, not spoken about in reporting on this subject as much as collaboration but which perhaps alludes to something deeper and more important that millennials want from the workplace. Egalitarianism and the opportunity to learn.

All of the young BDO staff interviewed mentioned the way in which an open-plan office with a hot desking system rather than cubicles or fixed desks meant that the most junior associate could be seated next to and work alongside a senior partner. This meant that traditional corporate structures were broken down, and made them feel a much greater part of the team much more quickly as well as giving them the chance to tap into the experience of senior staff.

> You're able to talk to people and work together without being disturbed.
>
> **PANKHURI SHAH**
> SENIOR ASSOCIATE, BUSINESS CONSULTING
> MUMBAI, BDO INDIA

> The structure here changed and we're no longer allocated desks. Not having fixed desks really breaks down barriers and hierarchy. You feel like you can learn from the partners and talk to them about anything. You don't feel like you have to go through a chain of command.
>
> **MEGAN VAN DER LINDE**
> AUDIT TRAINEE, TECHNOLOGY AND MEDIA GROUP
> LONDON, BDO UK

Millennials are a generation that feel they want to learn as much as possible as quickly as possible, and also to prove that they can give something back right now. The right real estate can help foster this, and help companies to reap the benefits.

> The benefits can flow both ways. I think senior members of staff realise that young people have something to offer. It helps to create a really open, accepting, friendly culture.
>
> **DAVID ZYCHSKI**
> SENIOR CORPORATE FINANCE ANALYST
> SYDNEY, BDO AUSTRALIA

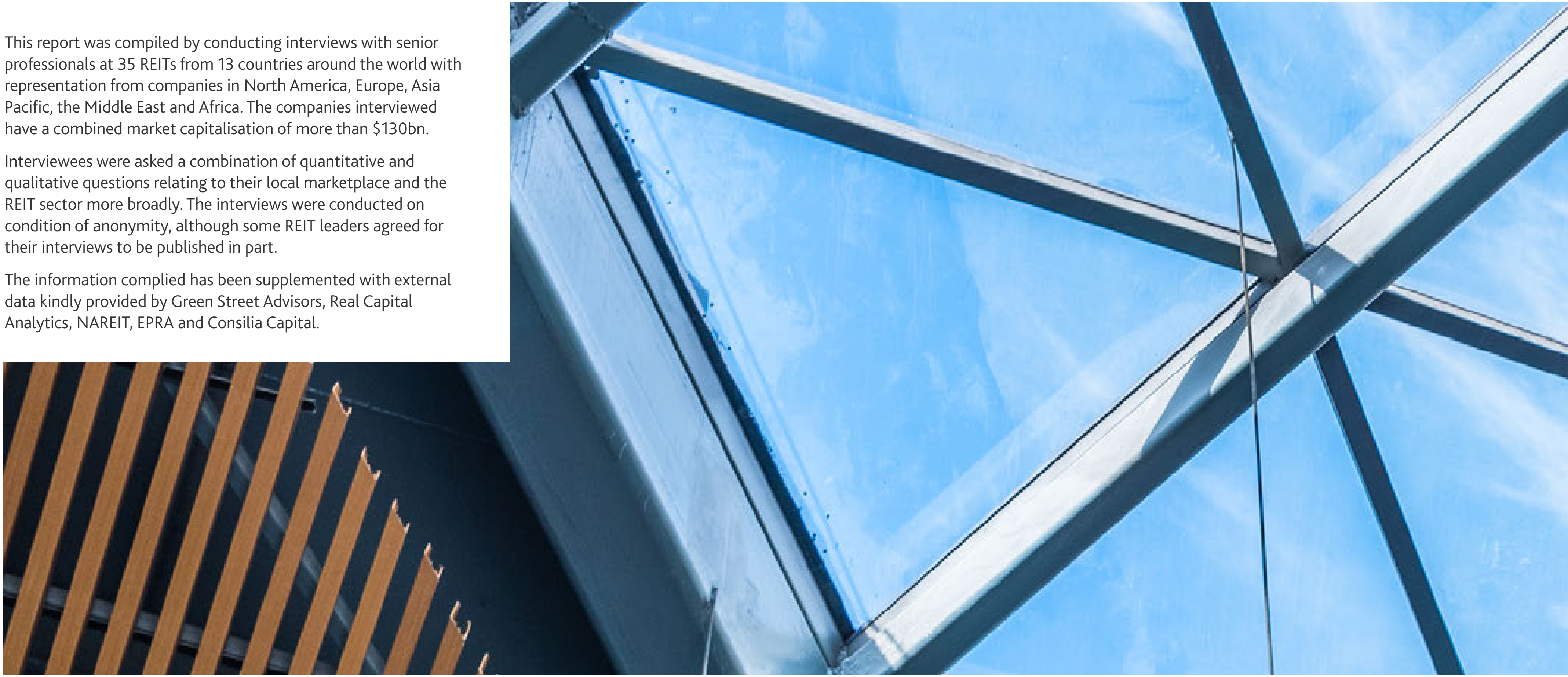
> Talking to my friends, we feel its incredibly important that junior staff feel that their chances at work depend on their capabilities, and not on tenure.
>
> **MEGAN VAN DER LINDE**
> AUDIT TRAINEE, TECHNOLOGY AND MEDIA GROUP
> LONDON, BDO UK

METHODOLOGY

This report was compiled by conducting interviews with senior professionals at 35 REITs from 13 countries around the world with representation from companies in North America, Europe, Asia Pacific, the Middle East and Africa. The companies interviewed have a combined market capitalisation of more than $130bn.

Interviewees were asked a combination of quantitative and qualitative questions relating to their local marketplace and the REIT sector more broadly. The interviews were conducted on condition of anonymity, although some REIT leaders agreed for their interviews to be published in part.

The information complied has been supplemented with external data kindly provided by Green Street Advisors, Real Capital Analytics, NAREIT, EPRA and Consilia Capital.



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