HODES WEILL
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Cornell
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Survey Highlights

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2019 Institutional Real Estate Allocations Monitor

INTRODUCTION

Cornell University's Baker Program in Real Estate and Hodes Weill & Associates are pleased to present the findings of the seventh annual Institutional Real Estate Allocations Monitor (the "**2019 Allocations Monitor**"). The 2019 Allocations Monitor focuses on the role of real estate in institutional portfolios, and the impact of institutional allocation trends on the investment management industry. Launched in 2013, the Allocations Monitor is a comprehensive annual assessment of institutions' allocations to, and objectives in, real estate investments. This report analyzes trends in institutional portfolios and allocations by region, type and size of institution.

The 2019 Allocations Monitor includes research collected on a blind basis from 212 institutional investors in 24 countries. The 2019 participants hold total assets under management ("**AUM**") exceeding US$12.3 trillion and have portfolio investments in real estate totaling approximately US$1.1 trillion. Our survey consisted of 24 questions concerning portfolio allocations to the asset class, current and future investments in real estate, investor conviction, investment management trends and the role of various investment strategies and vehicles within the context of the real estate allocation (e.g., direct investments, joint ventures, private funds). We also included questions regarding historical and target returns as well as environmental, social and governance ("**ESG**") policies.

2019 GLOBAL INSTITUTIONAL PARTICIPANTS

212 participants in 24 countries representing US$12.3 trillion in AUM

KEY FINDINGS OF THE 2019 ALLOCATIONS MONITOR

1. **Target allocations to real estate continue to rise globally, although the pace of year-over- year growth is moderating.** Average target allocations to real estate increased 10 bps to 10.5% in 2019, up approximately 160 bps since 2013. However, the annual pace of increase appears to be moderating, with 10 bps representing the lowest annual change in six years, during which time the annual change ranged from 20 bps to 40 bps.

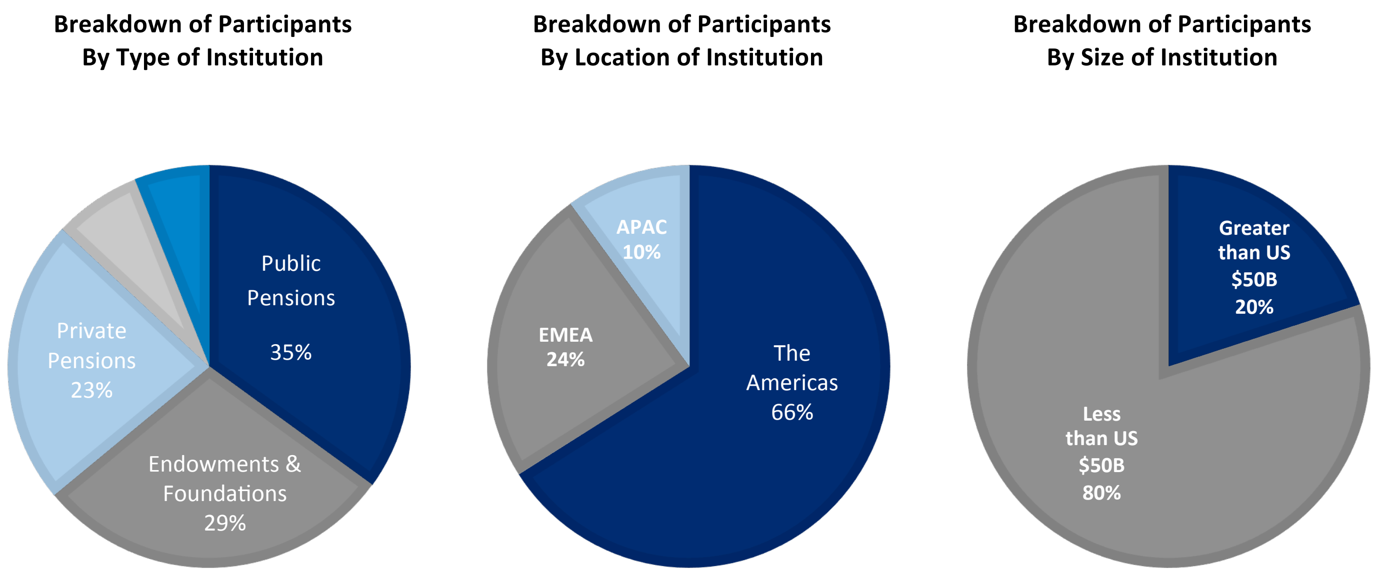

Figure 1. Key Findings of the 2019 Allocations Monitor

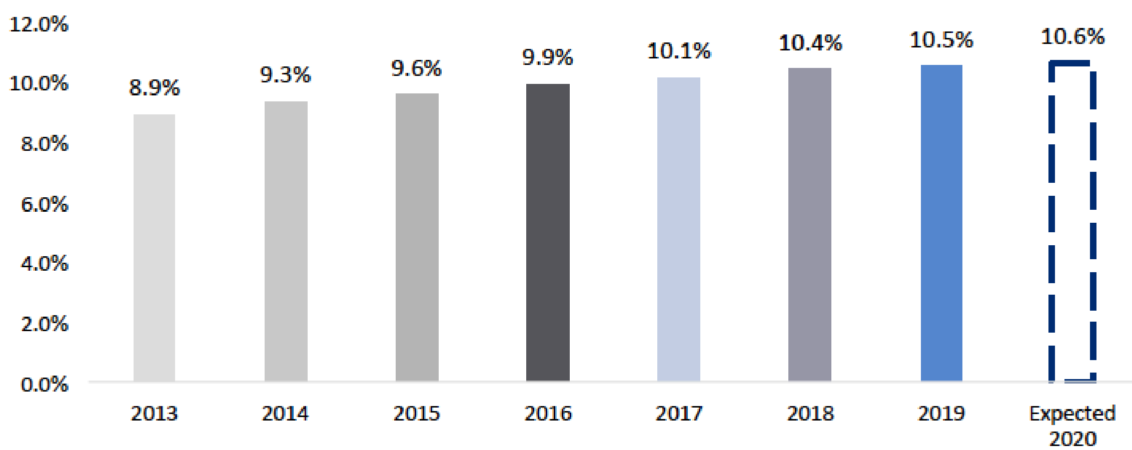

Figure 2. Weighted Average Target Allocation to Real Estate, All Institutions

2. **Led by institutions in the Americas and Asia Pacific, growth in target allocations is forecasted to continue in 2020.** On average, institutions are expecting to increase target allocations by an additional 10 bps over the next twelve months. This expected increase is being driven by institutions based in the Americas and Asia Pacific, with each region forecasting increases of 20 bps, while target allocations for EMEA-based investors are expected to remain flat.

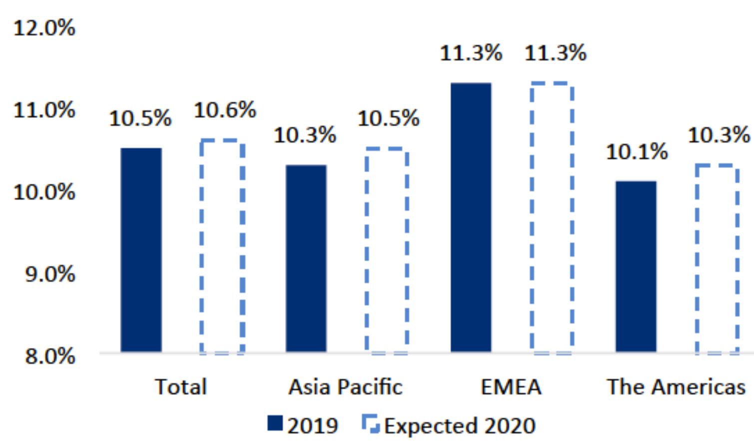

Figure 3. Weighted Average Target Allocation, By Location of Institution

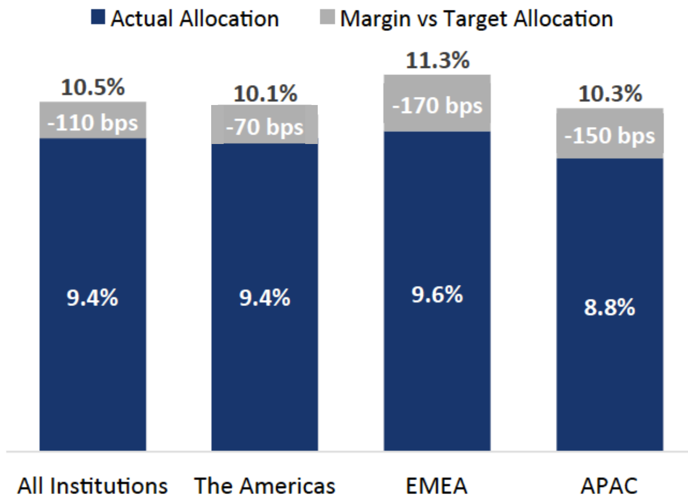

Figure 4. Actual vs. Target Allocation, By Location of Institution

3. **While institutions have been actively investing in real estate, the "denominator effect" continues to contribute to portfolios lagging target allocations.** Actual allocations remained flat year-over-year, with institutional portfolios 9.4% invested in real estate on average. Overall, institutions are 110 bps under-invested relative to target allocations. Institutions in EMEA and APAC remain significantly under-invested, at margins of 150 bps and 170 bps, respectively. Approximately 50% of institutions overall are under-invested relative to target allocations by an average of 190 bps.

4. **While actual investment returns declined moderately in 2018, results continue to outpace target returns.** As capital appreciation has slowed in recent years, returns have moderated to high single digits. Institutions reported an average return of 8.8% in 2018, down 30 bps from 9.1% in 2017. While institutions continue to express concerns regarding asset valuations and weakening economic growth, operating fundamentals remain broadly favorable which is contributing to a continuation of strong returns for the asset class.

	2018 Target Return	*2019 Target Return*	*Actual 2014*	*Actual 2015*	*Actual 2016*	*Actual 2017*	*Actual 2018*	*Actual 3-Year Average*	*Actual 5-Year Average*
All Institutions	8.2%	8.3%	11.8%	10.9%	8.7%	9.1%	8.8%	8.9%	9.9%
By Type									
Public Pension	7.6%	7.5%	11.7%	11.4%	8.8%	9.2%	8.4%	8.8%	9.9%
Endowment & Foundation	8.8%	9.7%	13.0%	11.0%	9.1%	8.9%	9.1%	9.0%	10.2%
Private Pension	8.4%	8.3%	12.6%	11.1%	8.2%	8.9%	9.0%	8.7%	10.0%
Insurance Company	8.2%	8.4%	8.3%	9.3%	9.1%	9.9%	8.7%	9.2%	9.1%
SWFs & GEs	7.2%	7.2%	11.4%	9.7%	8.1%	8.9%	9.3%	8.8%	9.5%
By Location									
The Americas	8.5%	9.0%	12.6%	11.7%	8.7%	9.3%	9.2%	9.1%	10.3%
EMEA	7.3%	6.9%	10.4%	9.3%	8.4%	8.5%	7.5%	8.1%	8.8%
Asia Pacific	8.1%	7.6%	9.5%	10.1%	9.2%	9.1%	9.1%	9.1%	9.4%
By Size									
Greater than US$50 billion	7.5%	7.9%	11.1%	11.0%	9.4%	9.6%	9.2%	9.4%	10.0%
Less than US$50 billion	8.3%	8.5%	12.0%	10.9%	8.6%	9.0%	8.7%	8.8%	9.8%

Figure 5. Historical and Target Returns

5. **Investor sentiment increased for the second straight year, reaching a 5-year high.** Between 2018 and 2019, our "Conviction Index", which measures institutions' view of real estate as an investment opportunity from a risk-return standpoint, increased from 5.1 to 5.7, the highest reported since 2014. Despite rising investor sentiment, institutions report an increase in focus on positioning portfolios more defensively for a potential market downturn.

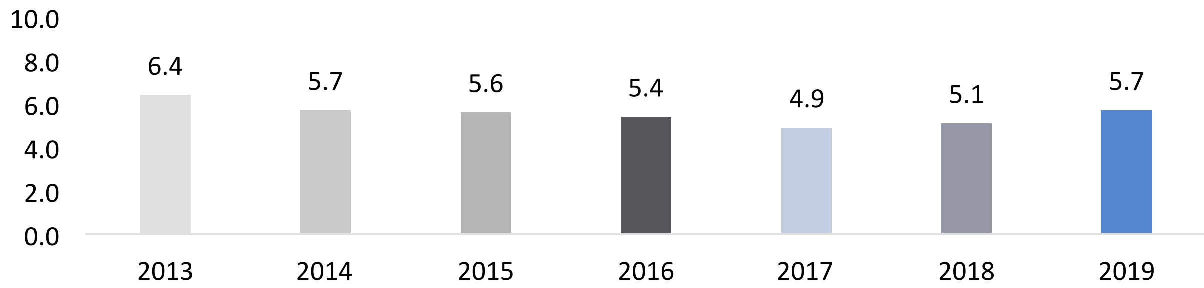

Figure 6. Conviction Index, All Institutions

6. **Allocations to third-party managers continued to trend upward in 2019, driving double-digit growth in global AUM for fund managers.** Institutions continue to allocate a substantial majority of their new investment allocations to third-party managers. Rising target allocations and an increase in cross-border investing continue to drive the outsourcing of portfolio management.

7. **Value add strategies remain the strongest preference for institutions globally, while interest in opportunistic strategies declined for the first time in five years.** Approximately 91% of institutions reported that they are actively allocating to value add strategies, while 66% are allocating to core strategies and 69% to opportunistic strategies. Opportunistic strategies were the only type of strategy that garnered a decline in interest in 2019, as compared to 2018.

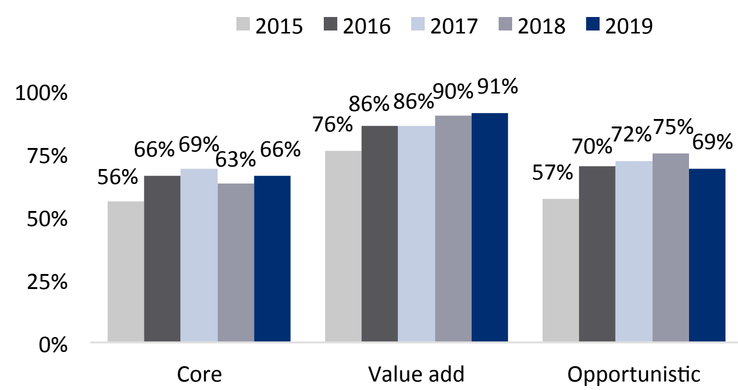

Figure 7. Risk Preference, All Institutions

8. **While cross-border capital flows remain strong, the percentage of institutions investing outside of their domestic region has decreased, led by EMEA-based institutions that are increasingly favoring intra-regional allocations.** North America continues to be the largest recipient of capital allocations, followed by Continental Europe. Investor demand remained largely consistent year-over-year with the exception of the UK and Asia. Investors are citing currency exchange rates, uncertainty regarding BREXIT, Hong Kong protests and the impact of global trade wars as significant risks.

9. **Closed- and open-end private funds remain the preferred investment products for institutions, but popularity has declined slightly after several years of growth.** Closed-end funds continue to be the most favored investment product for institutions, although the percentage of investors allocating capital to closed-end funds decreased 13 percentage points in 2019. Appetite for direct investments and separate accounts increased in 2019, led by larger institutions with an objective to maintain greater discretion over their capital (and to lower portfolio management costs).

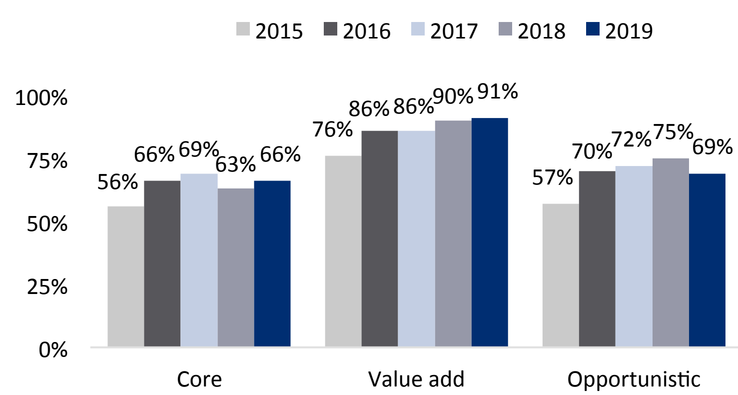

Figure 8. Institutions Investing Outside of their Domestic Region, By Location of Institution

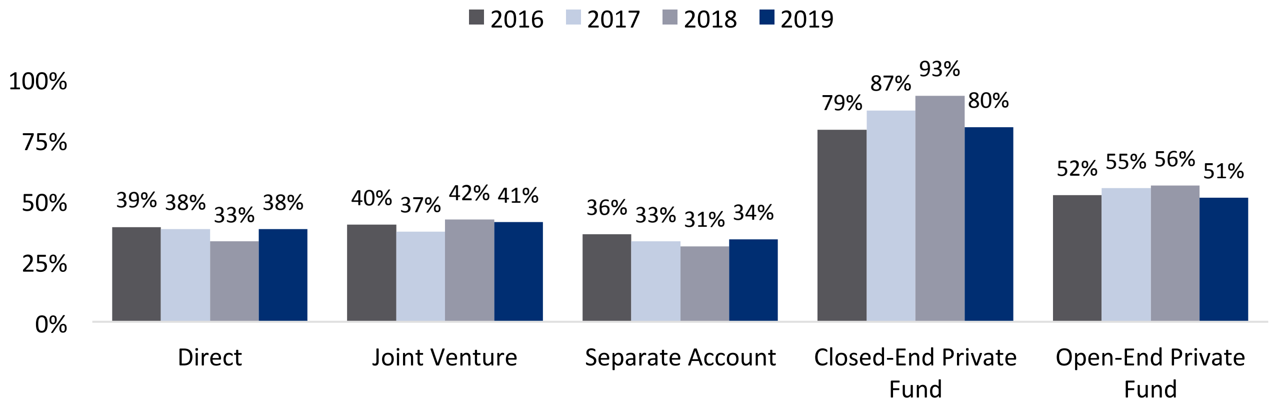

Figure 9. Investment Product Preferences, All Institutions

10. **ESG policies are increasingly important for institutions, and investment managers are positioning their organizations and product offerings to accommodate their clients' objectives.** The focus on ESG policies has continued its trend upwards in 2019. Institutions are showing an increasing preference for investments that not only meet their return expectations but also satisfy their objectives for environmental sustainability, social responsibility, and governance. EMEA-based institutions continue to lead the industry in implementing ESG policies.

The 2019 Allocations Monitor leverages the academic resources of Cornell University and the global institutional relationships and real estate expertise of Hodes Weill & Associates. We hope this report provides unique insight into the institutional investment industry, serving as a valuable tool for institutional investors in the development of portfolio allocation strategies and peer benchmarking of returns, and for investment managers in business planning and product development. With this goal in mind, please feel free to contact us with any comments, questions or suggestions.

For a copy of the full 2019 Allocations Monitor, please contact Kathy Terry, Program Assistant for the Baker Program in Real Estate, at kcr2@cornell.edu or (607)255-7110.