

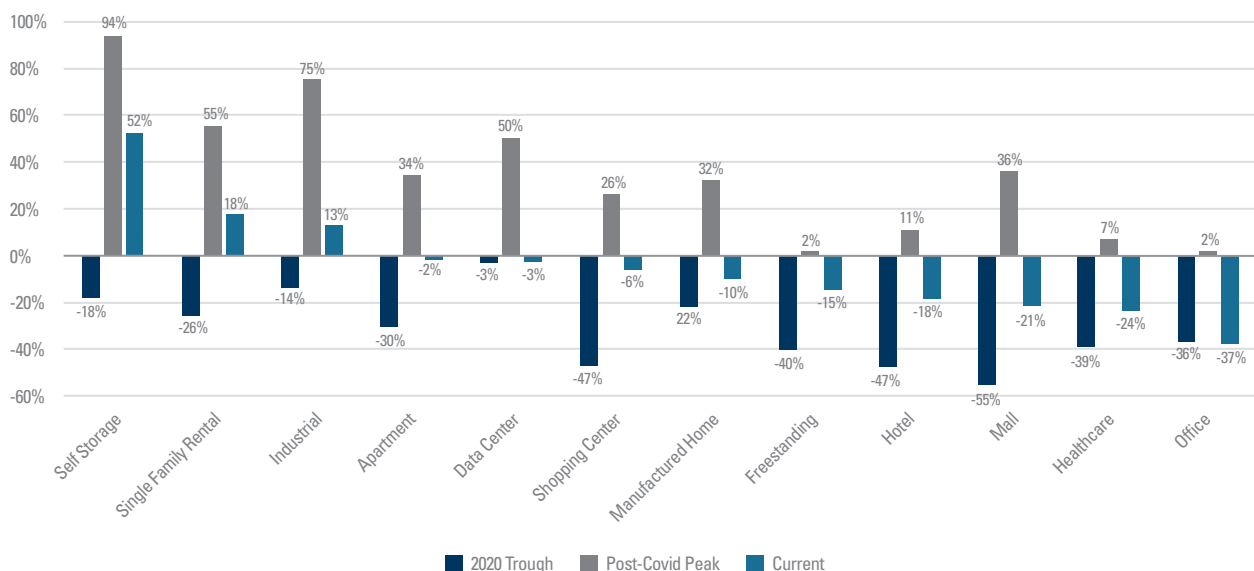
# Public REITs: Living in Interesting Times



The origin of the oft-quoted Chinese proverb “May you live in interesting times” is widely debated; less debatable, perhaps, is how well it applies to the past few years. Global health and geopolitical events have led to rising inflation, and the rapid interest rate response in the U.S. is creating an opaque pricing environment, where a wide bid-ask spread between buyers and sellers is leading to a pause in transaction activity. Many are looking to the public REIT market for transparency, where cap rates are up ~200 bps since September 30, 2022. Contrast this with private market appraisals, which have remained relatively flat in 2022.<sup>1</sup> While we’d agree that the public markets have been directionally more correct this year, investors should exercise caution when using these markets as a proxy for market value. Consider the following:

- » **Exhibit 1** shows the maximum decline in 2020 market values following the onset of the pandemic, the peak valuation in late-2021/early-2022 as the market recovered (and perhaps became overly exuberant), and where it stands today.
- » We’ve experienced a volatile three years across many sectors, and the following is instructive:
  - Industrial public REIT pricing fell 14% during COVID, had valuations 75% above January 2020 levels earlier this year, and now stands at 13% above January 2020 levels.
  - Office REIT valuations are below trough levels in 2020, though they briefly were positive earlier this year.
- » While public REIT pricing offers more immediate transparency, it also may reflect more temporary sentiment than private real estate, and the last three years demonstrate it often overshoots (in both directions). We saw this during the GFC as well, when public REIT pricing fell over 70% peak-to-trough, more than double the private markets, and quickly corrected in the subsequent two years.

**EXHIBIT 1:** Public REIT Sector Index Pricing vs. January 2020<sup>2</sup>



Source: NAREIT, USAA Real Estate Research

1. For the multifamily and industrial sectors, using NCREIF cap rates used as a proxy for private market.  
 2. Current as of September 2022.

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