Lazard Global Real Estate Securities

US Real Estate Indicators Report

APR
2017

Real estate investment trusts (REITs) returned 1.1% in April.[1] Year to date, performance has seesawed as investors assessed the strength of economic growth underpinning the Federal Reserve's plan for further interest rate increases. When prospects for economic growth were considered more modest (even tepid), REITs have rallied, as they did in December 2016 and February 2017. Conversely, when growth prospects appeared stronger, REITs sold off as they did in the fall and in January and March. While concerns about real estate in a rising rate environment are understandable conceptually, they are not supported by past behavior. As we have discussed over the last few years, near-term REIT market behavior is mixed in a rising rate environment. However, after the initial market response, REITs have shown strong relative performance as the real estate sectors are bolstered by a growing economy.

In general, REIT earnings remain solid (though moderating) as fundamentals are intact and companies take advantage of a strong capital markets environment to raise equity and improve debt structures. REITs generally met Wall Street estimates and provided measured 2017 guidance as companies hedge expectations due to the uncertain overall climate. Additionally, recent conversations with real estate practitioners have been positive. Most participants in the office and industrials sectors are confident about business prospects in 2017. Further, according to data from the Fed, banks continue to tighten lending standards across the commercial real estate loan spectrum, which is healthy for market discipline and helps curtail risk.

First-quarter earnings and other data seem to confirm that the real estate cycle is solidly in its mature phase, and is likely in the later stages of that phase for most of the core sectors as underlying property net operating income (NOI) growth is slowing across most core sectors. On average, the core property sectors are estimated to generate 3.25% property NOI growth in 2017 as compared to 3.9% in 2016. The positive exceptions are in the office, industrials, and in some of the specialty sectors such as data centers that are still showing strong organic growth and an acceleration in property NOI growth. However, regional mall REIT results have shown the potential for further weakness due to recent store closings, especially among lower-quality centers. Note, a mature phase of the overall cycle does not mean a cessation of growth, just a reversion to the mean after multiple years of above-trend growth.

We believe valuations are fair. While earnings and NOI growth suggest a benign-to-positive outlook for US REITs, the potential headwinds of higher interest rates from today's levels warrant caution as further interest rate spikes will unwind the alternative yield trade much to the detriment of REITs and the REIT preferred market.

US Real Estate Market Returns

(%; cumulative)	1 Month	3 Month	1 Year	3 Years	5 Years	YTD
FTSE EPRA/NAREIT US (USD)	1.1	0.8	3.6	27.7	53.1	0.1
MSCI US REIT (RMS)	1.5	1.3	4.9	29.8	55.3	1.2
S&P 500	1.2	4.4	17.3	35.9	89.1	7.2
Russell 3000	1.4	4.2	18.0	34.6	88.0	6.9

US Real Estate Market Returns by Property Type

(%; cumulative)	1 Month	3 Month	1 Year	3 Years	5 Years	YTD
Diversified/Other	2.8	5.3	13.1	25.7	53.2	7.1
Health Care	1.4	7.7	10.3	22.2	51.6	7.4
Hotel	1.7	-4.1	18.6	13.1	48.7	-3.1
Industrials	6.9	9.4	21.4	48.7	90.7	5.2
Multifamily	2.9	6.7	8.5	49.6	61.3	3.4
Office	0.1	-2.6	8.9	24.9	52.0	-0.2
Regional Mall	-2.1	-7.9	-17.2	6.2	25.6	-9.1
Community Retail	-4.6	-11.6	-15.6	10.5	40.3	-12.6
Self-Storage	-4.1	-0.1	-12.0	37.9	90.0	-3.7

As of 30 April 2017

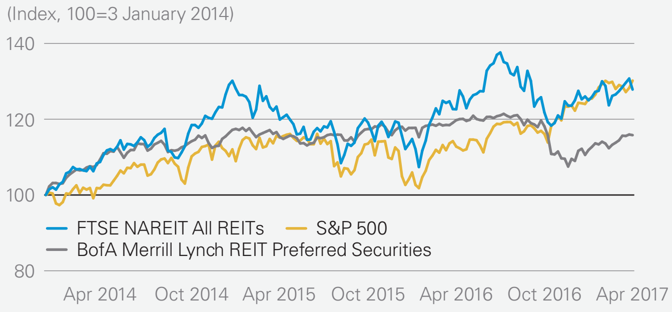
For illustrative purposes only. The performance quoted represents past performance. Past performance is not a reliable indicator of future results. This is not intended to represent any strategy or product managed by Lazard. The indices are unmanaged and have no fees. One cannot invest directly in an index.

Source: FTSE, NAREIT, Standard and Poor's

LAZARD
ASSET MANAGEMENT

Listed Real Estate Market Performance

Cumulative Returns



As of 30 April 2017

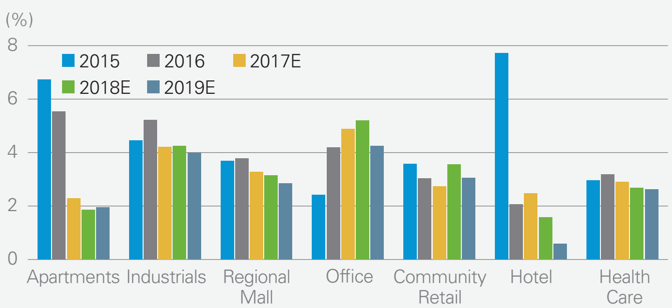
For illustrative purposes only. The performance quoted represents past performance. Past performance is not a reliable indicator of future results.

Source: Bloomberg

In April, REITs returned 1.1%, just shy of the 1.2% and 1.4% returns from the S&P 500 and Russell 3000 indices, respectively. The REIT market is essentially flat in 2017, substantially lagging the S&P 500 Index year-to-date return of 7.2%. Over the last 12 months, REITs have lagged the S&P 500 returns by almost 1,400 basis points (bps). While the short-term stabilization in 10-year Treasury yields has helped bolster REITs, we expect the sector to exhibit further weakness upon better economic data that drive interest rates higher. Historically REIT performance has not been tightly linked to interest rates, but that pattern has broken down and we expect near-term headwinds as interest rates spike.

Real Estate Fundamentals

Property Net Operating Income (NOI) Growth



As of 30 April 2017

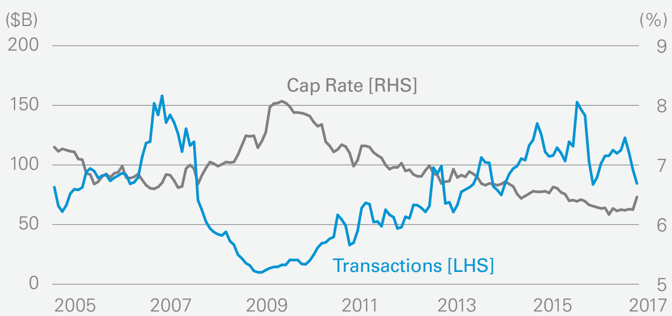
Forecasted or estimated results do not represent a promise or guarantee of future results and are subject to change.

Source: Green Street Advisors

Expected property level NOI growth has declined by an average of 30 bps in 2017. Reductions for 2018 and beyond are less notable. At current levels, underlying property growth is projected to average 3.3% across the core property sectors in 2017, which is approximately 100 bps above expected core inflation. The real estate sector is several years into the cycle and reversion to growth levels more closely aligned to underlying inflation is warranted. However, not all sectors are at the same point in the overall cycle and as such, growth leadership continues to shift, with business-oriented sectors (industrials, office, data centers) strong and earlier recovering sectors (hotel, apartments) slowing more dramatically. Overall, new construction levels generally remain below demand levels across most sectors and geographies, but construction increases in select segments is impacting the rate of growth.

Capital Markets Activity

Rolling 3-Month US Commercial Real Estate Transaction Volume



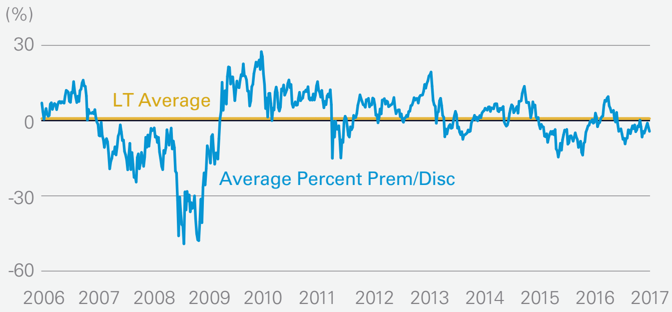
As of 30 April 2017

Source: Real Capital Analytics

Commercial real estate transaction volume has continued to decline throughout 2017. However, recent survey results point to still-large amounts of "dry powder" for real estate investment. The problem is that there is a lack of product for sale, which has led to lower deal volume. Transaction volumes were in the mid-$400 billion annually and have subsequently dropped to the mid-$300 billion range, on a month-to-month basis. In addition, due to a mix change in sector volumes, capitalization rates have moved up slightly. At current levels, capitalization rates are at a 400 bps spread to the 10-year Treasury. Interestingly, this spread is within 5 bps of the spread at year-end 2015. While this is still 220 bps wider than at the last peak (2007), it is generally in line with the market's average since 2005.

Listed Real Estate Valuations

Premium/Discount to Underlying Net Asset Value



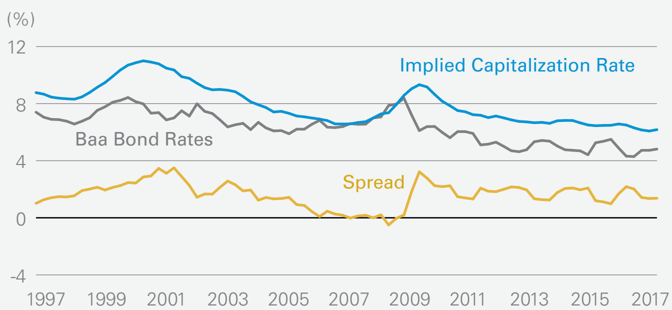
As of 30 April 2017

Source: SNL Financial. The REIT market as represented is a basket of 53 large and investable REITs across all sectors, as identified and selected by SNL Financial. The basket also includes companies that over time have gone private or merged in order to avoid survivor bias in the historical data.

With REIT prices (excluding dividend returns) slightly down year to date, REITs are now trading at a 4%–5% discount to underlying net asset value (NAV). This is still below the sector's 2%-3% average premium, which has been viewed historically as a reasonable "cost" over private real estate values given listed real estate's higher liquidity and favorable capital markets access. While REITs were slightly above NAV for a few months, the general trend is that the REIT market has been trading below NAV as investors are assessing the state of the real estate cycle and expecting that asset pricing will erode somewhat as rates rise.

Looking forward into 2017, there remains solid demand for US assets from both foreign and domestic investors.

REIT-Implied Capitalization Rate Spread to Baa-Rated Bonds



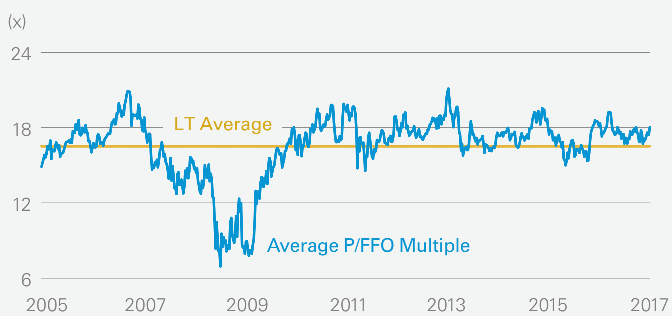
As of 30 April 2017

Source: SNL Financial. The REIT market as represented is a basket of 53 large and investable REITs across all sectors, as identified and selected by SNL Financial. The basket also includes companies that over time have gone private or merged in order to avoid survivor bias in the historical data.

Corporate Baa bond yields have been generally flat (+/-10 bps) for a few months as economic and inflation growth expectations have moderated from the initial election euphoria. Since the beginning of the year (through April), both the 10-year Treasury yield, Baa bonds yields, and REIT share prices have been essentially flat. This has kept the spread between REIT implied cap rates and the yield on Baa bonds at approximately 140 bps. This is approximately 45 bps higher than at the beginning of 2016.

Further rate hikes can jeopardize this cushion, but for now suggests that relative value remains solid within the real estate space.

Price-to-Funds from Operations (P/FFO)



As of 30 April 2017

Source: SNL Financial. The REIT market as represented is a basket of 53 large and investable REITs across all sectors, as identified and selected by SNL Financial. The basket also includes companies that over time have gone private or merged in order to avoid survivor bias in the historical data.

REIT P/FFO valuations remain slightly above long-term averages, but are below recent highs. Currently, REITs are trading at an approximate 18.0 P/FFO multiple, which is 1.5 multiple points above the sector's long-term average of 16.5. The first-quarter earnings season was generally solid with 2017 earnings guidance feeling overly conservative due to the uncertain policy environment. However, the results continue to demonstrate that overall REIT earnings remain very stable and are growing in the mid-single digits annually. This should translate into comparable dividend growth.

Note: P/FFO is the standard REIT equivalent of the price-to-earnings (P/E) ratio.

Notes

1 Source: FTSE NAREIT All REITs Index

Important Information

Published on 12 May 2017.

Information and opinions presented have been obtained or derived from sources believed by Lazard to be reliable. Lazard makes no representation as to their accuracy or completeness. All opinions expressed herein are as of 30 April 2017 and are subject to change.

This report is being provided for informational purposes only. It is not intended to be, and does not constitute, an offer to enter into any contract or investment agreement with respect to any product offered by Lazard Asset Management, and should not be considered as an offer or solicitation with respect to any product, security, or service in any jurisdiction or in any circumstances in which such offer or solicitation is unlawful or unauthorized or otherwise restricted or prohibited.

The performance of investments in real estate and real estate related securities may be determined to a great extent by the current status of the real estate industry in general, or by other factors (such as interest rates and the availability of loan capital) that may affect the real estate industry, even if other industries would not be so affected. The risks related to investments in realty companies include, but are not limited to: adverse changes in general economic and local market conditions; adverse developments in employment; changes in supply or demand for similar or competing properties; unfavorable changes in applicable taxes, governmental regulations, and interest rates; operating or development expenses; and lack of available financing. An investment in REITs may be affected or lost due in part to the fluctuation with the value of the underlying properties of the investment. An investment in REITs may be affected or lost if the REIT fails to comply with applicable laws and regulations, including tax regulations, specifically, the failure to qualify as a REIT under the Internal Revenue Code of 1986, as amended.

Equity securities will fluctuate in price; the value of your investment will thus fluctuate, and this may result in a loss. Securities in certain non-domestic countries may be less liquid, more volatile, and less subject to governmental supervision than in one's home market. The values of these securities may be affected by changes in currency rates, application of a country's specific tax laws, changes in government administration, and economic and monetary policy. Small- and mid-capitalization stocks may be subject to higher degrees of risk, their earnings may be less predictable, their prices more volatile, and their liquidity less than that of large-capitalization or more established companies' securities. Emerging markets securities carry special risks, such as less developed or less efficient trading markets, a lack of company information, and differing auditing and legal standards. The securities markets of emerging markets countries can be extremely volatile; performance can also be influenced by political, social, and economic factors affecting companies in emerging markets countries.

Fixed income and preferred securities are subject to credit risk, interest rate risk, and call and reinvestment risk. The strategy's investments in lower-rated, higher-yielding securities are subject to greater credit risk than its higher-rated investments. Junk bonds tend to be more volatile, less liquid, and are considered speculative, and a strategy may not be able to sell certain securities at the time and price it would like.

Non-domestic securities carry special risks, such as exposure to currency fluctuations, less developed or less efficient trading markets, political instability, a lack of company information, differing auditing and legal standards, and, potentially, less liquidity. The strategy may invest in a smaller number of issuers than other, more diversified, investment portfolios, and therefore the strategy's net asset value may be more vulnerable to changes in the market value of a single issuer or group of issuers and may be relatively more susceptible to adverse effects from any single corporate, industry, economic, market, political, or regulatory occurrence.

Derivatives transactions may cause a strategy to experience losses greater than if the strategy had not engaged in such transactions. Investments in derivatives are subject to many of the risks of, and can be highly sensitive to changes in the value of, the related security or index. As such, a small commitment to derivatives could potentially have a relatively large impact on a strategy's performance.

Wells Fargo Hybrid and Preferred Securities and "WHPS" are service marks of Wells Fargo & Company. Wells Fargo & Company does not guarantee the accuracy or completeness of the Wells Fargo Hybrid and Preferred Securities REIT Index and shall have no liability for any errors, omissions, or interruptions to publication. Wells Fargo & Company does not sponsor or advise any product or service that references WHPS, nor does Wells Fargo & Company represent that any use of WHPS by any person is appropriate, suitable, or fit for the uses to which it is put.

This material is provided by Lazard Asset Management LLC or its affiliates ("Lazard"). There is no guarantee that any projection, forecast, or opinion in this material will be realized. Past performance does not guarantee future results. This document is for informational purposes only and does not constitute an investment agreement or investment advice. References to specific strategies or securities are provided solely in the context of this document and are not to be considered recommendations by Lazard. Investments in securities and derivatives involve risk, will fluctuate in price, and may result in losses. Certain securities and derivatives in Lazard's investment strategies, and alternative strategies in particular, can include high degrees of risk and volatility, when compared to other securities or strategies. Similarly, certain securities in Lazard's investment portfolios may trade in less liquid or efficient markets, which can affect investment performance.

Australia: FOR WHOLESALE INVESTORS ONLY. Issued by Lazard Asset Management Pacific Co., ABN 13 064 523 619, AFS License 238432, Level 39 Gateway, 1 Macquarie Place, Sydney NSW 2000. Dubai: Issued and approved by Lazard Gulf Limited, Gate Village 1, Level 2, Dubai International Financial Centre, PO Box 506644, Dubai, United Arab Emirates. Registered in Dubai International Financial Centre 0467. Authorised and regulated by the Dubai Financial Services Authority to deal with Professional Clients only. Germany: Issued by Lazard Asset Management (Deutschland) GmbH, Neue Mainzer Strasse 75, D-60311 Frankfurt am Main. Hong Kong: Issued by Lazard Asset Management (Hong Kong) Limited (AQZ743), Unit 7, Level 20, One International Finance Centre, 1 Harbour View Street, Central, Hong Kong. Lazard Asset Management (Hong Kong) Limited is a corporation licensed by the Hong Kong Securities and Futures Commission to conduct Type 1 (dealing in securities) and Type 4 (advising on securities) regulated activities. This document is only for "professional investors" as defined under the Hong Kong Securities and Futures Ordinance (Cap. 571 of the Laws of Hong Kong) and its subsidiary legislation and may not be distributed or otherwise made available to any other person. Japan: Issued by Lazard Japan Asset Management K.K., ATT Annex 7th Floor, 2-11-7 Akasaka, Minato-ku, Tokyo 107-0052. Korea: Issued by Lazard Korea Asset Management Co. Ltd., 10F Seoul Finance Center, 136 Sejong-daero, Jung-gu, Seoul, 04520. People's Republic of China: Issued by Lazard Asset Management. Lazard Asset Management does not carry out business in the P.R.C. and is not a licensed investment adviser with the China Securities Regulatory Commission or the China Banking Regulatory Commission. This document is for reference only and for intended recipients only. The information in this document does not constitute any specific investment advice on China capital markets or an offer of securities or investment, tax, legal, or other advice or recommendation or, an offer to sell or an invitation to apply for any product or service of Lazard Asset Management. Singapore: Issued by Lazard Asset Management (Singapore) Pte. Ltd., 1 Raffles Place, #15-02 One Raffles Place Tower 1, Singapore 048616. Company Registration Number 201135005W. This document is for "institutional investors" or "accredited investors" as defined under the Securities and Futures Act, Chapter 289 of Singapore and may not be distributed to any other person. United Kingdom: FOR PROFESSIONAL INVESTORS ONLY. Issued by Lazard Asset Management Ltd., 50 Stratton Street, London W1J 8LL. Registered in England Number 525667. Authorised and regulated by the Financial Conduct Authority (FCA). United States: Issued by Lazard Asset Management LLC, 30 Rockefeller Plaza, New York, NY 10112.