

REAL ESTATE INCOME MONTHLY COMMENTARY

September 30, 2020



So far in 2020, real estate investment trusts (REITs) continue to underperform the market overall with a return of -22.4% for the TSX REIT index as at September 30, compared to a return of -3.1% for the TSX index. Both the trust index and Canadian market index (S&P/TSX) remained stable in September. The S&P/TSX now almost at the same level as at the beginning of the year. As we know, the effects of the pandemic continue to be felt among the main real estate trust sectors, including residential (apartments), retail (stores and shops), office and industrial (warehouses) trusts. Longer-term, we expect some asset classes to continue to benefit more than others.

Even apartment REITs, long thought of as defensive by investors, have not been immune. Despite outperforming the TSX REIT index since the Covid-crisis began, apartments have seen greater weakness of late, due primarily to concerns over lower near-term immigration and government intervention. As a reminder, the Ontario government recently proposed keeping rents at the same level in 2021 as in 2020, which led to a negative perception by the market. However, it should be noted that the increase projected by the government in 2021 was only 1.5%. The impact on REIT profits will therefore be minimal. In addition, the Canadian apartment REITs generally have assets that are more affordable than the market average, with rents below market-average, so are

better positioned to withstand continued economic weakness. In general, given long-term fundamentals remain intact, we see the situation in this sector as a long-term opportunity and we have added to our current holdings.

The impact of telework on office building trusts is yet to be defined; however, we can already tell that it will be significant. It will, however, take some time for things to fall into place because of the long-term nature of leases. It is also important to consider that the office market in Toronto and in Vancouver was already well below the average vacancy threshold before the crisis and this should make it possible to support rents, even in the face of a slowdown in demand. All the same, we remain under-invested in this sector as we await details about the impact of telework.

Retail trusts are clearly suffering because of the situation caused by the pandemic. In terms of performance, the retail trusts have suffered the most-to-date and have not yet begun to recover. Given the "second wave" is now upon us, we think some of the more distressed retail trusts could out-perform near-term as we expect rent collection will continue to improve as we enter the holiday season. But given concerns around long-term NOI visibility due to potential changes in consumer behaviour, we remain cautious longer-term. Once again, in the Fund, we are underweight in this sector and target investments in companies with tenants that have only been slightly impacted by the pandemic, like grocers, and in trusts invested in better quality assets.

Finally, the industrial real estate trust sector is the sector that has performed the best since the slowdown caused by the pandemic. Some of the companies have exposure to e-commerce, as they invest in storage and distribution centres needed to deliver these goods. The Fund is well exposed in this sector, with a weight higher than the index.

We have also begun to build a position in Storage Vault (SVI-TSV), Canada's only public self-storage real estate company. Although the asset class is smaller and less well-known than in the U.S., we think fundamentals are arguably better, and the sector is well positioned to benefit from recent emerging trends, including increased telework, and greater short-term inventory requirements by companies. All of which we expect to result in greater demand for self-storage space in the near-term.

Overall, this leads us to believe that the Fund is well positioned for an eventual recovery, which could, however, be gradual. We also believe that the current situation calls for a focus on selecting high quality REITs that have fallen in line

with the rest of the industry, and that there is an opportunity to add some of them to the portfolio at very attractive valuations on a historical basis.

Additionally, we have continued to earn profits in the Canadian equities portion of the Fund, as several names have performed well over the last few months. This diversification in Canadian equities is very important as it allows the Fund to add value and surpass the TSX REIT index over the long term. Moreover, it is a major reason why the Fund has performed better than the REIT index since the beginning of the year.

As at September 30, the Real Estate Income Fund earned a return year to date of 5.8% higher than the return of the TSX REIT, on a gross return basis. The Fund's annual distribution rate was 5% as at the same date and the 10-year Canadian bond rate was 0.56%. REIT distributed returns are attractive to investors who are seeking income, which will support an eventual revaluation, especially in an environment where interest rates are so low.

We must remember that REITs are as risky as the equity market overall, as measured by the standard deviation because of, among other things, their high debt level. As a result, the Real Estate Income Fund may experience a certain level of volatility in these financially turbulent times.



MARC GAGNON, M. Sc., CFA

- Principal Portfolio Manager, North American Equities
- Joined iAIM in 1998
- More than 25 years of investment experience
- MBA in Finance, Université Laval
- Bachelor's degree in Business Administration, Université Laval

Main funds managed by the team

✓	Canadian Equity Growth
✓	Real Estate Income
✓	Global True Conviction
✓	Canadian Equity Growth Hybrid 75/25
✓	Global True Conviction Hybrid 75/25
✓	IA Clarington Canadian Leaders Class

iAIM snapshot

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- Major player in the asset management industry
- Manages \$97 billion in general portfolios and segregated and mutual funds
- A team of 184 people, including 108 investment professionals (including 44 CFA charterholders)
- Composed of experienced managers who emphasize fundamental analysis, identification of value and long-term investing

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