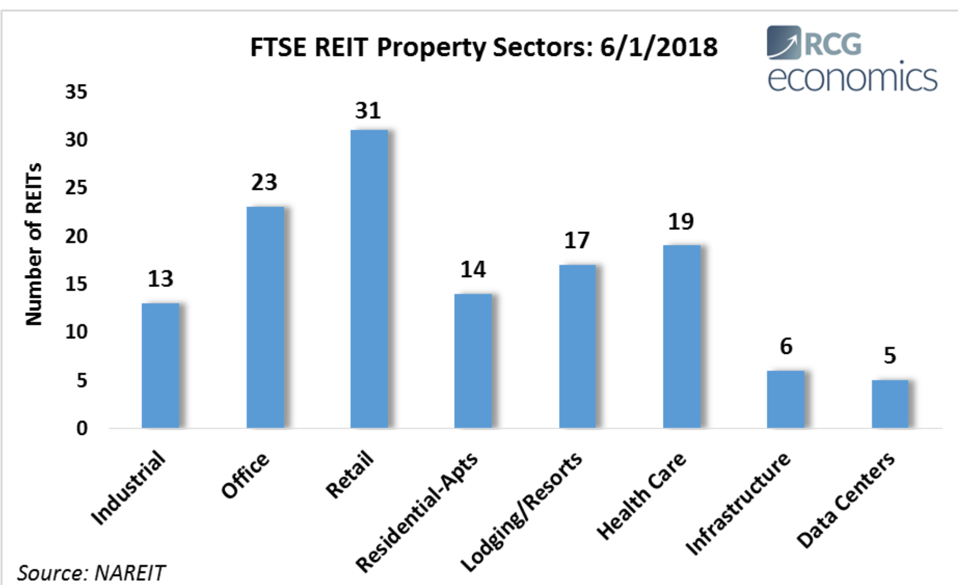
RCG Economics ("RCG") introduces a new bulletin that highlights monthly national real estate investment trust ("REITs") activity to broaden our clients' understanding of current real estate market trends. While we understand that REITs are not the biggest players in the Southern Nevada commercial real estate landscape, secondary markets like Las Vegas provide some enticing fundamentals for investors. Between 2016 and 2017, Las Vegas' population growth (2%) was more than twice the rate of the U.S. (.9%), while from 2017 to 2018 jobs grew 4.7% in the MSA versus 2.7% in the U.S. It is precisely this relatively high growth that distinguishes a secondary market like Las Vegas from the larger gateway markets like Los Angeles, Atlanta and Houston. Above average growth is likely to attract REITs to Southern Nevada looking for value and growth opportunities. According to *Raymond James*, "since the spring of 2016, non-gateway REITs have pulled ahead [of REITs in gateway markets] in total return.[1]"

For our readers unfamiliar with the term REIT, a REIT is a regulated "real estate investment trust" that owns, and often operates, a pool of income-producing real estate assets. Think of REITs as mutual funds for real estate. Large and small investors are able to purchase a liquid stake in these real estate portfolios, which are divided by commercial real estate market type such as Industrial REITs or Office REITS, thus gaining exposure to real estate while spreading out the risk over a bundle of properties.

REIT PROPERTY SECTORS

Since REIT portfolios are divided by market sector, we can glean some general insight into the performance of these sectors nationally, and locally, based on how well, or how poorly, the corresponding REIT portfolios are doing. We have chosen to focus on the property sector types we believe are most interesting or relevant to our readers.

According to NAREIT, Retail has the most FTSE REITs[2] at 31 (31 different bundles of Retail properties), followed by Office with 23 and Healthcare with 19. In this bulletin, we have separated Apartment REITs, of which there are 14, from the broader "Residential" category. Infrastructure and Data Centers have the smallest number of REITs with 6 and 5, respectively.



[1] *http://www.raymondjames.com/forefront/real-estate/text/non-gateway-reits-offer-new-horizon-for-investors*

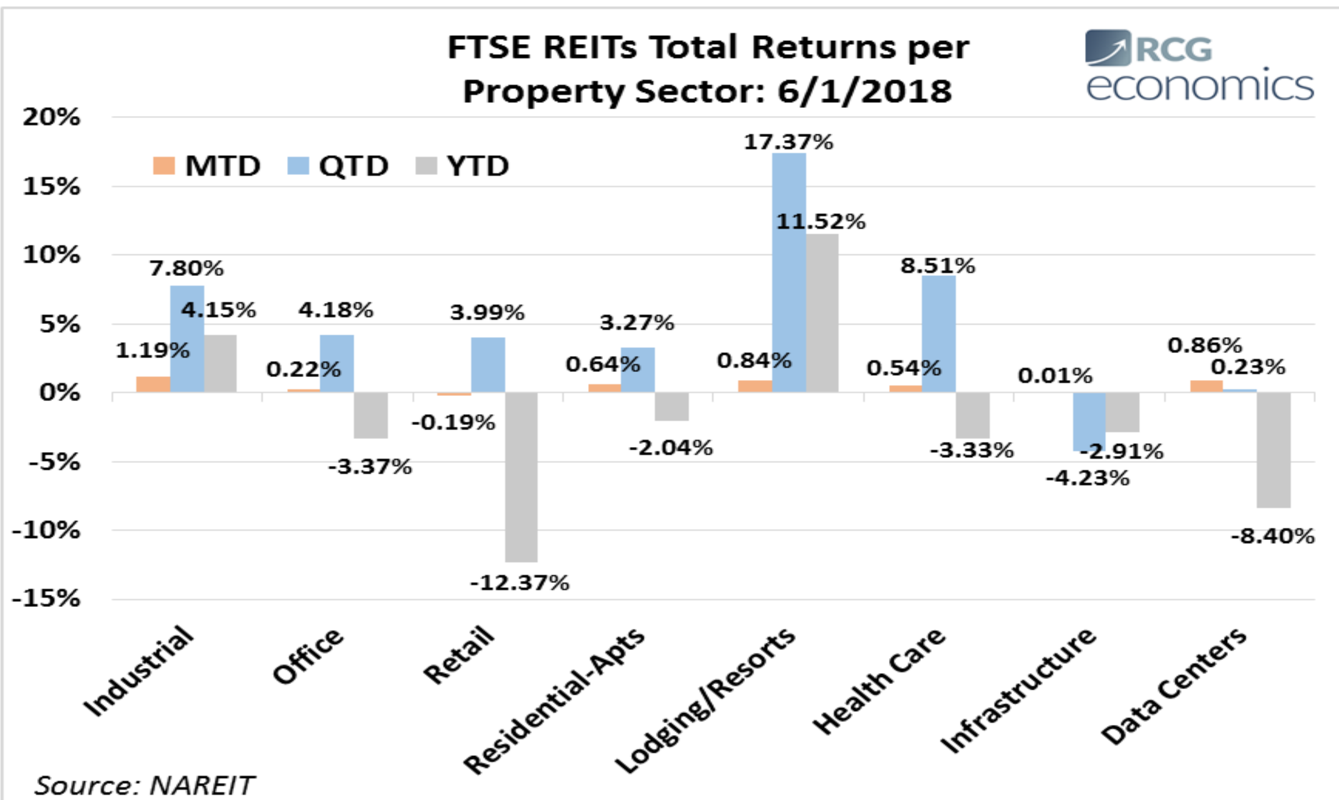
[2] *REITs that are tax-qualified and can be found on the New York Stock Exchange, the American Stock Exchange, or the NASDAQ.*

REIT TOTAL RETURNS

Over the year period ending on the June 1, 2018, returns of 11.52% for Lodging/Resort REITs more than double the returns for Industrial (4.15%), the only other property type to see positive YTD returns. All other REIT property sectors saw negative returns YTD, with Data Centers (-8.40%) performing more poorly than most and Retail (-12.37%) performing worst of all. Retail properties are having a hard time nationally (and in Las Vegas) with the continued growth of online retailers like Amazon, which just saw its stock soar to a new all-time high after posting better than expected sales growth in Q1 2018.

The comfort of shopping from home, the variety of online options and deals are posing an existential threat to many struggling brick and mortar retailers. This phenomenon of retail disruption has also contributed to the strong performance of Industrial properties. The growing need for eCommerce fulfillment centers (generally large Warehouse/Distribution spaces) are driving down vacancy rates, driving up land prices and fueling development around “industrial-powerhouse” metro areas - locales where online retailers can strategically position their distribution facilities near important transportation routes and major population centers.

Many industry observers attribute the poor YTD performance of REITs to the possibility of rising interest rates. According to Forbes, “First-level investors – those who buy and sell on headlines – mistakenly believe that real estate investment trust (REIT) profits will suffer if rates rise[3].” These investors assume that landlords need cheap loans in order to expand their property holdings. However, landlords of strong performing REIT properties with growth in funds from operations (“FFO”) can also raise rents to finance their expansion.



[3] *https://www.forbes.com/sites/brettowens/2018/01/25/rates-up-reits-down-buy-this-dip-now/#14720c566da2*

When we consider REIT property sectors on a QTD and MTD basis, it appears the industry analysts are right. Real estate investments are doing better with every property sector seeing positive returns, except for Retail MTD and Infrastructure QTD.

While Retail is facing a steep climb to overcome the evolving market landscape, Infrastructure may have a better outlook. America's deteriorating infrastructure receives considerable political attention, and President Trump has shown interest in mobilizing the private sector for its repair. A political focus on, and public commitment to, fixing the nation's crumbling dams, water treament plants, power suppliers, etc. could be the boost Infrastructure REITs need to grow in productivity. In fact, a turnaround for Infrastructure REITs might already be in works with a tiny, but positive, 0.01% MTD return.

On a QTD basis, Lodging/Resorts REITs soar above the rest with QTD returns of 17.37%, followed by Health Care (8.51%) and Industrial (7.80%). The positive QTD returns for Retail REITs might be explained by investors correcting for a heavy-handed devaluation of those properties in the past. Infrastructure is the only property type with negative returns QTD (-4.23%).

On a MTD basis, Industrial is best at 1.19%, trailed by Data Centers (0.86%), with Lodging/Resorts (0.84%) rounding out the top three. As mentioned above, Retail is the only property type to see negative returns MTD (-0.19%), while Infrastructure is just barely above zero.

CONCLUSION

Despite interest rate increases and fear of more to come resulting in negative YTD returns for all but two REIT property types, the data suggests REITs are beginning to rebound with positive returns across nearly every sector on a QTD and MTD basis.

For the year period ending on June 1, 2018, Lodging/Resorts REITs had the strongest performance QTD (17.37%) and YTD (11.52%), leading both time frames by more than double the next closest property type. According to the investment website *Seeking Alpha*, while hotels had a strong year in 2017, growing corporate demand and cooling supply growth[4] are expected to make 2018 even better. This bodes well for Las Vegas as hotels are the foundation of the city's economy.

Industrial real estate have been unstoppable in recent years and they continue to outperform most other REIT property types as one of only two with positive YTD returns (4.15%), robust QTD returns of 7.80% and top MTD returns of 1.19%. Much of Industrial's success comes at Retail's expense, with Retail losing the most for investors YTD with -12.37% returns.

Generally, REITs have underperformed when compared to the broader economy, so there does appear to be room for continued improvement. The hits REITs have taken from fear of continued interest rate hikes are much bigger than during comparable rate increases in the past, suggesting many REITs might be undervalued. Also, the Tax Cuts and Jobs Act contains a 20% deducation on pass-through entity income, a direct benefit for REITs according to Daniel Milan of Cornerstone Financial Services[5]. Various financial publications including Forbes, Seeking Alpha and Barron's are recommending investors take another look at REITs in 2018.✓

[4] https://seekingalpha.com/article/4161896-hotel-industry-booming-reits-get-memo
[5] https://money.usnews.com/investing/real-estate-investments/articles/2018-02-02/3-reasons-to-revisit-reits-in-2018