PRESS RELEASE

NATIXIS
GLOBAL ASSET MANAGEMENT

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Market Outlook Natixis Global Asset Management: The state of real estate: A global perspective

Return potential, diversification and the ability to generate attractive income tend to make real estate an asset class with a lot to offer. And while the global financial crisis has caused some hard times for many real estate markets, investors around the globe have begun to find value and opportunity once again. Experts from across Natixis Global Asset Management share diverse views on where recoveries are strengthening, what sectors are offering the most opportunity, and how the European debt crisis is impacting markets.

Diversification does not guarantee a profit or protect against a loss.

Real Estate Risk: Real estate investing may be subject to risks including, but not limited to, declines in the value of real estate, risks related to general and economic conditions, changes in the value of the underlying property owned by the trust and defaults by borrowers.

Jörg Knaf, Managing Director Northern Europe
Natixis Global Asset Management

It's not just about location, location, location. That would be too easy.
It should come as no surprise that in a low yield environment investors are turning to alternative investments such as real estate, to secure adequate long-term cash flows to fund their retirement and pension liabilities.

Michael Acton, Research Director
AEW Capital Management

Acton believes the U.S. Real Estate Investment Trust (REIT) market will have continued improvement in the year's second half, albeit with increased volatility. There are quite a few bright spots, and Acton believes one has gone largely unnoticed – the significant improvement in the federal government's budget position. Although still large, it is about half the size of last year's deficit, according to the U.S. Congressional Budget Office (CBO), and is expected to stay relatively stable over the next couple of years.
A few challenges accompany the bright spots, though. Acton would like to see a stronger economic recovery, as real estate can only do as well as local economies. And housing has a big multiplier effect, so its impact is significant. The National Association of Realtors estimates that each home sale generates more than $50,000 for local communities from an increased need for goods and services.*
Still, Acton believes opportunities are plentiful. Short-term and possibly medium-term real estate market fundamentals are strongest for apartments as the rental trend continues. "Another fundamental market recovery will likely begin in the office sector later this year and into 2014," said Acton. "And with its close connection to housing, the warehouse sector also could be very

bright." There are three main themes Acton is focused on for the remainder of 2013. U.S. housing, with its spillover effects, is the first one. Much of that demand is anticipated to be driven by the delayed formation of an estimated 2,000,000 households between 2007 and 2011. They are expected to enter the market in the next few years.

The second theme is energy. The U.S. is already largely able to satisfy its energy needs with energy produced in its own hemisphere – and by the end of the decade the U.S. is expected to be a net exporter of oil and possibly natural gas, as well. Acton believes there is potential opportunity in areas with a significant energy presence.

The third theme is also a risk – the most significant change in monetary policy seen in the U.S. for several decades. "The stronger economic activity associated with that change is particularly good for REITs," Acton acknowledged. "And, as investors seek REITs as a yield alternative, REIT companies will have to respond to the yields available to investors from corresponding products." REIT companies have begun to grow dividends, but dividend payout ratios are still at very low levels. Only a handful of companies have restored them to pre-crisis levels. They have a lot of cash flow, though, so as other rates rise and become competitive, many of the better REITs may respond by raising their dividends.

Acton recognizes that the REIT environment's flip side is that it doesn't go without risk. "Property is very capital-intensive," he notes. "People who invest in property use a lot of financial leverage, and obviously the cost of that is going to change as well."

*Average impact on local economy of a home sale is $56,464, according to National Association of Realtors study "Economic Impact of Real Estate Activity: United States, March 2013." Visit realtor.org.

Sam Martin, Director of Research & Strategy
AEW Europe

For a few years now, the euro-zone crisis has been preventing higher property investment volumes across much of Europe, especially for the crisis countries (Greece, Italy, Spain, Portugal and Ireland). However, Martin points out that investor sentiment appears to be changing, with the ongoing crisis actually stimulating property investment rather than dampening it in some crisis countries and Central and Eastern Europe.

"Despite the difficulties the European capital markets face, private and institutional investors are increasingly regarding property assets outside the super prime category as attractive, with some resilience to any future market disruptions from the euro-zone crisis," said Martin. Considerable Sovereign Wealth Fund investment activity seen in 2012 and early 2013 is one example of this emerging trend. Also, as price expectations between potential sellers and buyers converge, investment volumes in the crisis countries are expected to increase. For the last several years, the price buyers were willing to pay for a property in these regions was often lower than sellers would accept.

Martin also mentions that the crushing of income yields across most classes of risk assets from governments' fiscal policies and quantitative easing has rendered real estate a relatively attractive investment proposition in Europe. That said, he does point out that there are certain risks associated with real estate investments that investors should be aware of, including less liquidity and fluctuating real estate values.

Another factor contributing to increased real estate investment activity in 2013 is an improvement in the availability of debt finance. "The emergence of alternative sources of financing from insurers and dedicated debt funds should similarly be supportive of increasing activity, as will the continuing very low levels of interbank rates and five-year swap rates," said Martin.

Residential Markets

In the residential space, London and German markets are expected to see continued price increases, while prices in France remain on the decline.

“We expect the UK housing market to continue to grow, and sales volumes are forecast to rise further during 2013. The Funding for Lending scheme is having a positive effect on the number of mortgages approved and has lowered mortgage interest rates. However, disparities in regional market performance are unlikely to abate in the short to medium term, with the divergence between northern and southern housing markets expected to widen further, in favor of the latter,” said Martin.

French sales volumes are likely to continue falling throughout 2013, despite a mild price correction in house prices and historically low mortgage interest rates. Rising unemployment and a weakening job market, together with ongoing fiscal consolidation and a recession, are exerting downward pressure on residential property prices in France.

Office Markets

Office space demand in Europe is likely to remain low in the near term, according to Martin. Considering the causes of the euro-zone crisis have yet to be conclusively dealt with and much of Europe remains in recession, lease events and renegotiations are likely to dominate take-up activity in the near term. Occupiers are expected to continue to focus on cost reduction and efficiency improvement initiatives. As such, vacancy rates are expected to remain at current levels, with risks weighted toward an increase (particularly in the crisis countries) if a deviation occurs. However, vacancy rates for space in highly sought-after locations (such as Munich and Paris) are likely to continue to decline.

Retail Markets

The retail sector remains strongly focused on core western Europe, according to Martin. Opportunities for prime property in prime locations are arising in a number of areas in the large southern European markets. However, the greater investment risk involved in those markets continues to keep activity low.

Sovereign Wealth Fund is a pool of money derived from a country's reserves, which are set aside for investment purposes that will benefit the country's economy and citizens. The funding for a sovereign wealth fund (SWF) comes from central bank reserves that accumulate as a result of budget and trade surpluses, and even from revenue generated from the exports of natural resources.

Interbank rate is the rate of interest charged on short-term loans made between banks. Banks borrow and lend money in the interbank market in order to manage liquidity and meet the requirements placed on them. The interest rate charged depends on the availability of money in the market, on prevailing rates and on the specific terms of the contract, such as term length.

Interest rate swap is an agreement between two parties (known as counterparties) where one stream of future interest payments is exchanged for another based on a specified principal amount. Interest rate swaps often exchange a fixed payment for a floating payment that is linked to an interest rate (most often the LIBOR). A company will typically use interest rate swaps to limit or manage exposure to fluctuations in interest rates, or to obtain a marginally lower interest rate than it would have been able to get without the swap.

Swap rate is the rate of the fixed portion of a swap as determined by its particular market. This is the rate at which the swap will occur for one of the parties entering into the agreement.

Dmitri Rabin, Senior Securitized Asset Analyst
Loomis, Sayles & Company

For the most part, the U.S. housing market has had good news in the past year, according to Rabin. In fact, through April 2013, prices are up 11.9%, as measured by the CoreLogic® Home Price Index Report, excluding distressed sales.** Rabin points out that this measure excludes house sales that have recently been through foreclosure or other types of distressed sales, and shows that recent increases are broad-based and not just seasonal.

"At the state and local levels, prices also appear to be strong. House prices were up in 49 out of 50 states, with the largest increases in states that experienced the largest housing bubbles and subsequent declines (CA, AZ, NV and FL)," said Rabin. He expects states with the slowest foreclosure process and largest remaining pipeline of distressed properties to go up more slowly, such as NJ and IL.

"It is important to note that even after the recent increases, U.S. national home prices are still down 22% from the peak. So there is significant room to recover," said Rabin. Loomis Sayles expects the growth of home prices to begin to slow over the next 18–24 months to mid-single digits. The increases of 8%–12% in 2013 and 5%–7% in 2014 that Rabin anticipates would still be healthy.

Home mortgage rates on the rise

The 30-year fixed mortgage rate has recently risen sharply, resulting in an estimated 10%–15% increase in the monthly mortgage payment for new borrowers. However, even with that, Rabin believes affordability remains better than at any time from 1980 to 2010. "Even if home prices increase another 10% and mortgage rates move 2% higher, affordability would be approximately average for the 1981–2010 period. We therefore expect the impact of the recent rate increase to be small, causing price improvement to moderate slightly but not reverse. Finally, rising rates and affordability have not been great short-term predictors of home prices. We think the supply-demand balance is much more valuable, and we think that is very bullish," said Rabin.

Inventories near record lows

Both new and existing home inventories are near record lows. New home construction is finally increasing, but the process of building houses will take several years. The biggest concern in existing home inventories is the inventory of foreclosed homes. That is declining, while the rate of availability for the sale of foreclosed properties has been very slow.

In the last five years, many people in their 20s and 30s delayed moving out, creating a lag in housing demand. Improving economic conditions should help this trend reverse, according to Rabin. In the short run, he expects mortgage underwriting will slowly become less restrictive, allowing more consumers to get mortgages, which should add to the price growth of houses. "We view borrower expectations as very important in determining short-term house prices. When prices are rising, consumers expect them to continue rising, and when prices are going down, consumers expect them to fall further, at least in the short term," said Rabin. Therefore, if consumers expect home prices to drop, they will likely opt to wait before buying, even if mortgage rates stay low. "On the other hand, if consumers expect home prices to increase, they will opt to buy now rather than waiting, even if mortgage rates go up. During 2009–2011, borrowers scared by the housing bust expected prices to drop more, and so delayed buying, causing home prices to fall far below trend," said Rabin.

In Loomis Sayles' view, the biggest risk to U.S. house prices would be a sudden tightening of credit via government policy. Today, various government-guaranteed entities (Fannie Mae, Freddie Mac, and FHA) still provide four out of every five mortgages in the United States. FHA

(Federal Housing Administration) is particularly important as a lender for first-time home buyers and those with smaller down payments. Rabin believes the policymakers are aware that the transition of mortgage underwriting back to private markets needs to be done gradually, but he will continue to monitor this area closely.

"Implications of house price increases are significant. Housing-sensitive sectors, such as homebuilders and non-Agency RMBS, will benefit directly from stronger housing demand. More broadly, we expect higher house prices to help repair consumer and bank balance sheets, and add to GDP growth through greater construction activity and higher consumer confidence," said Rabin.

**The CoreLogic® Home Price Index, introduced in 2008, is a repeat-sales index that tracks increases and decreases in sales prices for the same homes over time, including single-family attached and single-family detached homes. The CoreLogic® HPI provides a multi-tier market evaluation of repeat sales transactions based on price, time between sales, property type, loan type (conforming vs. nonconforming) and distressed sales. Released once a month, the CoreLogic® HPI has a lag time of roughly two months.

"Bullish" market is a financial market of a group of securities in which prices are rising or are expected to rise.

Residential Mortgage-Backed Security (RMBS) is a type of security whose cash flows come from residential debt such as mortgages, home-equity loans and subprime mortgages. This is a type of mortgage-backed securities that focuses on residential instead of commercial debt.

Philippe Waechter, Chief Economist
Natixis Asset Management

Real estate recoveries in the U.S., China and Europe are progressing at different stages, according to Philippe Waechter, Chief Economist at Natixis Asset Management.

"The U.S. market is probably in its revival period, after a long period of adjustment. Prices are up, as is volume, as gauged by home sales and housing starts," said Waechter. He also points out that the contribution of real estate investment to GDP also is positive now, whereas between Q2 2006 and Q2 2011, it was a drain on the economy. "To date, though, the economic benefit of real estate's acceleration has been limited because it has less of an impact on GDP that in it did in the past. As of Q1 2013, real estate investment represented 2.9% of U.S. GDP compared to 6.1% in 2005," said Waechter.

Waechter believes that China's overall real estate market remains strong. Prices are up in most major cities and investment is high. Real estate helped drive growth when the economy was booming because people were moving to big towns and needed real estate. Waechter notes, though, that the link between economic activity and real estate growth has weakened since 2009, resulting in varying levels of strength in different parts of the country.

China's cities are categorized into five different tiers. While there is no official formula for determining these tiers, common views are that they are based on size as determined by GDP and/or population, and development of services and infrastructure.

Tier 1 areas, such as Beijing, Shanghai, Shenzhen and Guangzhou, are still experiencing strong demand but have little or no capacity to build. These markets could become more speculative because they're already so tight, according to Waechter. And the adjustments could be severe if, as analysts speculate, central bank policy becomes more restrictive and financial system regulations increase. In contrast, Tier 2 areas – provincial capitals and affluent cities – have a more balanced situation. Though smaller than their Tier 1 counterparts, they are still sizable cities. These areas are growing from economic expansion and job gains, and demand is matched by construction.

"In Tier 3 and Tier 4 areas, which are smaller cities in China with populations of less than one million people, the situation is more complicated and potentially problematic," said Waechter. There is overcapacity from the construction of so many buildings since 2009 and demand remains weak. There is little activity today and the situation is likely to get worse. Plus, much of the development was from “shadow banking,” financed credit. In Waechter’s opinion, the combination of these factors could lead to non-performing loans.

In China, traditional banks are state-owned and lend primarily to big state-owned companies. “Shadow banking” is lending that comes from non-traditional, informal sources such as trust companies, insurance companies, leasing firms and pawnbrokers. They are not subject to the same restrictions as traditional banks and provide funds to borrowers that may not qualify for traditional bank lending. Because these lenders can take on more risk, there’s the potential for non-performing loans. Waechter noted that the Bank of China has started moving toward being more restrictive, which would reduce the impact of shadow banking and have a negative effect on Tier 3 and Tier 4 towns.

Location is also a factor in Europe, although the real estate market struggles to gain traction across most countries. Property prices are down in 8 out of 14 countries, including Spain, Italy, France and Ireland, but are higher in Estonia, Luxembourg, Malta, Belgium and Finland. The strongest market, though hardly robust, is in the UK. “We do not see a strong recovery there,” stated Waechter, “but it’s getting better.”

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Headquartered in Paris and Boston, Natixis Global Asset Management, S.A. has assets under management totaling $779.3 billion (€591.2 billion) as of December, 2012.[2] Natixis Global Asset Management, S.A. is part of Natixis. Listed on the Paris Stock Exchange, Natixis is a subsidiary of BPCE, the second-largest banking group in France. Natixis Global Asset Management, S.A.'s affiliated investment management firms and distribution and service groups include: Absolute Asia Asset Management; AEW Capital Management; AEW Europe; AlphaSimplex Group; Aurora Investment Management; Capital Growth Management; Caspian Private Equity; Darius Capital Partners; Gateway Investment Advisers; H2O Asset Management; Hansberger Global Investors; Harris Associates; IDFC Asset Management Company; Loomis, Sayles & Company; Natixis Asset Management; Ossiam; Reich & Tang Asset Management; Snyder Capital Management; Vaughan Nelson Investment Management; and Vega Investment Managers. For more information visit www.ngam.natixis.com

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[1] Cerulli Quantitative Update: Global Markets 2012 ranked Natixis Global Asset Management, S.A. as the 13th largest asset manager in the world based on assets under management as of December 31, 2011.
[2] Assets under management (AUM) may include assets for which non-regulatory AUM services are provided. Non-regulatory AUM includes assets which do not fall within the SEC's definition of 'regulatory AUM' in Form ADV, Part 1.