Over the past three years, we have observed a meaningful anomaly in the relationship between overall global equity returns and the performance of high-beta versus low-beta stocks. While broad index returns have been substantial over this period, the more cyclical, growth-sensitive stocks that tend to lead a rising market have lagged far behind more defensive, low-beta sub-sectors.

In our view, a strong stock market return led by low-beta stocks is likely reflecting an unusual emphasis on factors other than the underlying global economic growth backdrop that normally dominates in importance to investors. Ultimately, we believe the underpinnings of these dynamics will have implications for the future performance of core real asset categories—real estate, commodities, natural resource equities and infrastructure.
Executive Summary

We do not view the generally below-average returns of real assets over the past few years as altogether unexpected, given the backdrop of sluggish economic growth and widespread disinflationary pressures. However, global stocks have performed extremely well under these conditions, to the surprise of many investors. More remarkable, in our view, are the types of market sectors behind this performance: it has not been driven by growth-sensitive or high-beta stocks, as is typically the case in upward-trending markets, but instead, by traditionally more defensive, low-beta subsectors.

Our research suggests that this breakdown in the relationship between overall market returns and the relative performance of high-beta versus low-beta stocks is, in fact, a meaningful historical anomaly. Furthermore, we find a positive relationship between the returns for diversified real assets and past periods of deviation from the “normal” relationship between global market returns and the relative performance of high-beta versus low-beta stocks.

Our advocacy for real assets is, for the most part, rooted in longer-term research conclusions, and it is driven by a focus on broader asset allocation considerations. However, we believe these findings serve to further bolster our longstanding conviction around the merits of allocating to real assets.

Our research suggests that the breakdown in the relationship between overall market returns and the relative performance of high-beta versus low-beta stocks is, in fact, a meaningful historical anomaly.
Following the publication of our research whitepaper, *Exploring the Real Benefits of Real Assets*,(1) we have received supportive comments from investors on both our research framework and our conclusions making the case for a permanent, strategic allocation to listed real assets. At the same time, some have suggested that the strategic case for real assets may be “broken” in some way, given their relative three-year underperformance versus global equities. Exhibit 1 illustrates this point with a comparison of the Diversified Real Assets Blend(2) to global equities(3) from January 2011 through December 2013.

A Market Divided

Does this observed performance differential in real asset vs. broad market performance weaken our research-driven case for real assets investing? Our answer is an emphatic, “no.”

While it is common to see dispersion in returns between real assets and stocks—the diversification benefits from lower correlations are, after all, an artifact of precisely this kind of de-synchronization of returns—the degree of underperformance seen in recent years is relatively rare over the period since 1973 for which we have index data available. So, does this observed performance differential in real asset vs. broad market performance weaken our research-driven case for real assets investing? Our answer is an emphatic, “no.”

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(1) *Exploring the Real Benefits of Real Assets* is available on the Cohen & Steers website, www.cohenandsteers.com under the “Insights” tab.

(2) The Diversified Real Assets Blend is represented by an equally-weighted blend of Real Estate, Commodities, Natural Resources Equities, and Infrastructure. Real Estate is represented by the FTSE NAREIT Equity REIT Index through December 1989 and the FTSE EPRA/NAREIT Developed Real Estate Index thereafter. Commodities are represented by the S&P GSCI through December 1990 and the Dow Jones-UBS Commodity Index thereafter. Natural Resource Equities are represented by a 50/50 Blend of Datastream World Oil & Gas and Datastream World Basic Materials through December 2002 and the S&P Global Natural Resources Index thereafter. Infrastructure is represented by a 50/50 Blend of Datastream World Pipelines and Datastream World Gas, Water & Multi-Utilities through December 2002 and the Dow Jones Brookfield Global Infrastructure Index thereafter.

(3) Global equities are represented by the Datastream World Market Index. Subsectors are represented by the Datastream World Market subsector total returns. See page 10 for index definitions.
Two main factors lend continued support to our strategic case for real assets.

- The first lies in the very nature of real asset categories, which historically tend to exhibit their strongest performance during mid-cycle and late-stage economic expansions. Yet, the past several years have been characterized by a sluggish global economy, widespread disinflationary pressures and periodic fiscal crises that would normally lead us to expect, all else equal, a period of below-average performance from real assets. In our view, the kind of meaningful cyclical expansion that historically has favored real assets is yet to come.

- Second, all else has not been particularly equal in recent years. Above all, stimulus measures emanating from central banks around the world and, in particular, the U.S. Federal Reserve’s zero-interest-rate policy (ZIRP) and quantitative easing (QE) programs stand out as exceptional, mostly unprecedented interventions. Only time will tell whether the objective of delivering sustained economic growth will be achieved. But there is little doubt in our minds that these programs have led investors to migrate further out on the risk spectrum—from fixed income to equities, for example—to seek higher returns. Importantly, the search for higher returns appears to have generated an unusual split within the equity markets, driving a wedge between the performance of more cyclical, growth-sensitive sectors of the market and the typically lower risk, defensive groups. Ultimately, we believe an exploration of these dynamics has implications for understanding both the recent past and the potential future for real assets. These concepts are explored below in more detail.

Exhibit 2 on the following page breaks down the global stock market into 19 primary subsectors and ranks them according to their measured three-year beta(1) to the global stock market return through December 2013. We also note the annualized three-year total return of each subsector. To the extent that broad market returns reflect changes in expectations around underlying profit and cash-flow-growth potential, we’d expect to see rising markets coincide with the outperformance of higher beta stocks versus lower beta stocks, and vice-versa. However, whereas the global stock market has returned almost 9% annually over the past three years, we have seen widespread underperformance of high-beta versus low-beta sectors.

One possible explanation for this outcome is that the broad market has been driven higher by a QE-driven re-rating of stocks and sectors perceived (rightly or wrongly) as “bond proxies.” Evidence of such a re-rating is apparent in the 20% price-to-earnings (P/E) multiple expansion seen in the low-beta group detailed in Exhibit 2, from an average of 16.6x at the beginning of 2011 to 19.9x at the end of 2013. In contrast, the average high-beta group P/E multiple contracted by 7% from 16.8x to 15.7x. As a next step, though, we believe it’s important to determine whether the experience of the past several years is actually as unusual as it seems at first glance.

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(1) Beta is a measure of the volatility, or systematic risk, of a security or a portfolio in comparison to the market as a whole.
The search for higher returns appears to have generated an unusual split within the equity markets, driving a wedge between the performance of more cyclical, growth-sensitive sectors of the market and the typically lower risk, defensive groups.

Exhibit 2: High-Beta Stocks Have Underperformed Low-Beta Stocks
January 2011 through December 2013

<table>
<thead>
<tr>
<th>Subsector</th>
<th>Beta to Global Stocks</th>
<th>Three-Year Total Return</th>
</tr>
</thead>
<tbody>
<tr>
<td>Basic Resources</td>
<td>1.41</td>
<td>-15.6%</td>
</tr>
<tr>
<td>Banks</td>
<td>1.32</td>
<td>4.7%</td>
</tr>
<tr>
<td>Construction &amp; Materials</td>
<td>1.25</td>
<td>5.2%</td>
</tr>
<tr>
<td>Chemicals</td>
<td>1.24</td>
<td>7.1%</td>
</tr>
<tr>
<td>Oil &amp; Gas</td>
<td>1.21</td>
<td>3.8%</td>
</tr>
<tr>
<td>Financial Services</td>
<td>1.17</td>
<td>13.0%</td>
</tr>
<tr>
<td>Insurance</td>
<td>1.16</td>
<td>13.2%</td>
</tr>
<tr>
<td>Auto &amp; parts</td>
<td>1.13</td>
<td>12.5%</td>
</tr>
<tr>
<td>Industrial Goods &amp; Services</td>
<td>1.06</td>
<td>11.2%</td>
</tr>
<tr>
<td>Real Estate</td>
<td>1.05</td>
<td>6.3%</td>
</tr>
<tr>
<td>Media</td>
<td>0.96</td>
<td>20.5%</td>
</tr>
<tr>
<td>Technology</td>
<td>0.87</td>
<td>11.9%</td>
</tr>
<tr>
<td>Travel &amp; Leisure</td>
<td>0.84</td>
<td>14.0%</td>
</tr>
<tr>
<td>Utilities</td>
<td>0.76</td>
<td>1.0%</td>
</tr>
<tr>
<td>Personal &amp; Household Goods</td>
<td>0.75</td>
<td>12.4%</td>
</tr>
<tr>
<td>Retail</td>
<td>0.71</td>
<td>14.9%</td>
</tr>
<tr>
<td>Food &amp; Beverage</td>
<td>0.64</td>
<td>12.9%</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>0.64</td>
<td>10.3%</td>
</tr>
<tr>
<td>Health Care</td>
<td>0.60</td>
<td>19.9%</td>
</tr>
</tbody>
</table>

At December 31, 2013. Source: Bloomberg, Thomson Reuters Datastream and Cohen & Steers. Performance data quoted represents past performance. Past performance is no guarantee of future results. The information presented above does not reflect the performance of any fund or other account managed or serviced by Cohen & Steers, and there is no guarantee that investors will experience the type of performance reflected above. An investor cannot invest directly in an index and index performance does not reflect the deduction of any fees, expenses or taxes. Returns over the study period are compound annual returns. Global Stocks are represented by the Datastream World Market Index. Subsectors are represented by the Datastream World Market subsector total returns. See page 10 for index definitions.
Exhibit 3 below plots the historical rolling three-year annualized total return of global stocks (the orange line) against the relative performance of high-beta versus low-beta subgroups over the same time period (the blue line). For this analysis, returns for the high-beta group reflect average returns across the five highest-beta sectors, as measured over the prior three years; similarly, the low-beta group reflects the average return of the five lowest-beta groups. Two observations are apparent from this chart:

- First, there does appear to be a strong relationship between the overall market return and the relative high-beta/low-beta performance, with high-beta stocks typically outperforming during rising markets and low-beta stocks taking the lead during falling markets, as expected.
- Second, the more recent observations on the far right-hand side of the display—with strong market returns coinciding with significant underperformance of the high-beta group—do appear unusual with respect to the prior history.

**Exhibit 3: Returns of Global Stocks Strongly Related to High-Beta vs. Low-Beta Relative Performance**

January 1973 through December 2013

At December 31, 2013. Source: Bloomberg, Thomson Reuters Datastream and Cohen & Steers. Performance data quoted represents past performance. Past performance is no guarantee of future results. The information presented above does not reflect the performance of any fund or other account managed or serviced by Cohen & Steers, and there is no guarantee that investors will experience the type of performance reflected above. An investor cannot invest directly in an index and index performance does not reflect the deduction of any fees, expenses or taxes. Returns over the study period are compound annual returns. Global Stocks are represented by the Datastream World Market Index. Subsectors are represented by the Datastream World Market subsector total returns. See page 10 for index definitions.

Strong market returns coinciding with significant underperformance of the high-beta group appears unusual with respect to the prior history.
However, determining the extent to which the recent period is a true outlier event
requires us to 1) more formally identify the statistical relationship between global
market returns and relative high-beta/low-beta returns, and 2) examine the deviation
of the current-period observation from that statistically “normal” relationship.

Lasting structural breaks are far more the exception
than the rule in investing, and the lessons of history
suggest to us that mean-reversion is a powerful,
equalizing force.

Exhibit 4 below shows the results of this analysis, plotting the actual high-beta/
low-beta relative return against what would be predicted by actual, realized
global market returns in such a model.\(^{(1)}\) Notably, the most recent period plots the
difference between the realized and predicted performance of high- versus low-beta
sectors at about -1.7 standard deviations below normal. This, in our view,
provides evidence that the low-beta-driven market of the past several years is, in
fact, a meaningful anomaly.

Said differently, based on historical experience, we should expect to see a deviation
of this magnitude in fewer than five-percent of historical three-year periods. In fact,
as shown in Exhibit 4, we have seen an event like this only a few times since the
early 1970s—most recently during the mid- to late-1990s as enthusiasm for the
“new economy” took hold, leaving much of the higher-beta, “old economy” universe
lagging behind the broader market for several years.

Exhibit 4: High-Beta vs. Low-Beta Relative Performance Compared to “Normal” Global Stocks Relationship
January 1973 through December 2013

Performance data quoted represents past performance. Past performance is no guarantee of future results. The information presented
above does not reflect the performance of any fund or other account managed or serviced by Cohen & Steers, and there is no guarantee that investors will
experience the type of performance reflected above. An investor cannot invest directly in an index and index performance does not reflect the deduction of
any fees, expenses or taxes. Returns over the study period are compound annual returns. Global Stocks are represented by the Datastream World Market
Index. Subsectors are represented by the Datastream World Market subsector total returns. See page 10 for index definitions.

\(^{(1)}\) Our methodology relies on a simple linear regression with the three-year total return to Global Stocks as the independent
or explanatory variable and the three-year relative return of high-beta vs. low-beta groups as the dependent variable.
For a wide variety of reasons, market dynamics may depart from historical norms from time to time, and they may do so for extended periods. But lasting structural breaks are far more the exception than the rule in investing, and the lessons of history suggest to us that mean-reversion is a powerful, equalizing force. In our assessment, the historical returns to our Diversified Real Assets Blend detailed in Exhibit 5 below reinforce precisely this intuition. In this analysis, we’ve sorted the observed historical high-beta/low-beta deviations detailed in Exhibit 4 into four groups ranked from the most negative to the most positive deviation from the normal statistical relationship. The downward-descending bars in Exhibit 5 reflect the average annualized returns to the Diversified Real Assets Blend over the ensuing three years for each of these groupings. Clearly, there appears to be a relationship between periods when low-beta sectors have experienced unusual levels of outperformance—such as seen over the past few years—and future periods of above-average returns to real assets. For example, a -1.7 standard deviation from “normal” (as observed today) would fall into the far left-hand group (highlighted in orange), which is consistent historically with an average 18.0% annualized return from the Diversified Real Assets Blend over the following three years.

Exhibit 5: Historical Returns of Real Assets Following Past Deviations from the “Normal” High-Beta/Low-Beta Relationship
January 1973 through December 2013

At December 31, 2013. Source: Bloomberg, Dow Jones, FTSE, S&P, Thomson Reuters Datastream and Cohen & Steers. Performance data quoted represents past performance. Past performance is no guarantee of future results. The information presented above does not reflect the performance of any fund or other account managed or serviced by Cohen & Steers, and there is no guarantee that investors will experience the type of performance reflected above. An investor cannot invest directly in an index and index performance does not reflect the deduction of any fees, expenses or taxes. Returns over the study period are average annual returns. The Diversified Real Assets Blend is represented by an equally-weighted blend of Real Estate, Commodities, Natural Resource Equities, and Infrastructure. Real Estate is represented by the FTSE NAREIT Equity REIT Index through December 1989 and the FTSE EPRA/NAREIT Developed Real Estate Index thereafter. Commodities are represented by the S&P GSCI through December 1990 and the Dow Jones-UBS Commodity Index thereafter. Natural Resource Equities are represented by a 50/50 Blend of Datastream World Oil & Gas and Datastream World Basic Materials through December 2002 and the S&P Global Natural Resources Index thereafter. Infrastructure is represented by a 50/50 Blend of Datastream World Pipelines and Datastream World Gas, Water & Multi-Utilities through December 2002 and the Dow Jones Brookfield Global Infrastructure Index thereafter. See page 10 for index definitions.
While this analysis is reflective of a basic statistical relationship rather than a riskless prediction, and the future is always uncertain, we believe the interpretation of this phenomenon is relatively straightforward and intuitive: simply put, a strong stock market return led by low-beta stocks is likely reflecting an unusual and unsustainable emphasis on factors other than the underlying global economic growth backdrop that normally dominates in importance to investors. Real assets, being generally sensitive to growth and inflation trends in the real economy, have historically suffered lagging performance during such periods, much as they have in recent years. But history also suggests that today’s underperformance has, more often than not, only paved the way for tomorrow’s outperformance. And while it is not our intention to call a turning point in the markets, we do believe, to employ an old straw, that though history never repeats itself, it does often rhyme.

A strong stock market return led by low-beta stocks is likely reflecting an unusual emphasis on factors other than the underlying global economic growth backdrop that normally dominates in importance to investors.

In our view, those looking to better understand the recent relative performance of various asset classes will be well served to focus their attention on two things: the forces at work that have driven the strong returns of low-beta market sectors, and, by extension, the risks and potential opportunities generated by these anomalies. This perspective could prove relevant to the extent the global economy transitions from its extended recovery process to a more self-sustaining expansion, and it could bring some clarity to the frequently asked question, “why now?” However, we would caution that the decision to make a real assets allocation should be rooted in a far broader set of long-term goals-based objectives, based on the entirety of the investor’s asset and liability picture. With our research conclusions pointing to the demonstrable benefit potential of a strategic real assets allocation, we are more inclined to ask the obviously rhetorical question, “why not now?”
Index Definitions

An investor cannot invest directly in an index, and index performance does not reflect the deduction of any fees, expenses or taxes.

The Dow Jones Brookfield Global Infrastructure Index measures the stock performance of publicly listed infrastructure companies. The index intends to measure all sectors of the infrastructure market.

The Dow Jones-UBS Commodity Index is a broadly diversified index composed of commodities traded on U.S. exchanges, with the exception of aluminum, nickel and zinc, which trade on the London Metals Exchange.

The FTSE NAREIT Equity REIT Index is an unmanaged, market-capitalization-weighted index of all publicly traded REITs that invest predominantly in the equity ownership of real estate.

The FTSE EPRA/NAREIT Developed Real Estate Index (net) is an unmanaged market-capitalization-weighted total return index which consists of any companies from developed markets who derive more than half of their revenue from property-related activities.

The S&P Global Natural Resources Index includes 90 of the largest publicly traded companies in natural resources and commodities businesses that meet specific investability requirements, offering investors diversified, liquid and investable equity exposure across three primary commodity-related sectors: Agribusiness, Energy, and Metals & Mining.

The S&P GSCI Energy and Non-Energy Indexes represent the energy and non-energy components, respectively, of the S&P GSCI Index (a benchmark for investment in the commodity markets and as a measure of commodity market performance over time).

The S&P 500 Index is an unmanaged index of 500 large-capitalization, publicly traded stocks representing a variety of industries.

Gold is represented by gold spot price.

Correlation is a statistical measure of how two securities move in relation to each other. Standard Deviation is a commonly used statistical measure of volatility. Beta is a measure of the volatility, or systematic risk, of a security or a portfolio in comparison to the market as a whole.

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Founded in 1986, Cohen & Steers is a leading global investment manager with a long history of innovation and a focus on real assets, including real estate, infrastructure and commodities. Headquartered in New York City, with offices in London, Hong Kong, Tokyo and Seattle, Cohen & Steers serves institutional and individual investors around the world.

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