

# Cohen & Steers Global Real Estate Securities Strategy

FEBRUARY 28, 2010

INVESTMENT COMMENTARY

We would like to share with you our review and outlook for the global real estate securities markets as of February 28, 2010. For the month, the FTSE EPRA/NAREIT Developed Real Estate Index had a total return of +3.0% in U.S. dollars. Year to date, the index had a total return of -2.9%.

## INVESTMENT REVIEW

Global real estate securities advanced in February, reflecting gains from North America and Asia Pacific. Europe had a decline amid concerns about possible sovereign debt defaults in Greece and other smaller markets.

U.S. REITs had a total return of +5.3% as measured by the FTSE NAREIT Equity REIT Index. The market was aided by a strong showing from regional malls (+11.9%),<sup>1</sup> which were buoyed by news that Simon Property Group and Brookfield Asset Management both expressed an interest in buying all or most of General Growth Properties (which is in bankruptcy). Simon's plan and ability to sell large portions of General Growth's lower-quality assets gave yet more evidence that there is abundant capital available for acquisitions, even for assets with negative near-term growth outlooks. Glimcher and CBL & Associates also had sizable gains in this environment.

The shopping center sector (+8.9%) also outperformed, lifted by Developers Diversified Realty (DDR), which bounced on a successful \$350 million capital raise. The industrial sector (+1.9%) was relatively lackluster, reflecting worse-than-expected operating guidance from ProLogis and EastGroup Properties. Health care REITs (+2.4%) underperformed, but rebounded sharply from January's decline.

### Property acquisition aided the U.S. apartment sector

The theme of external growth opportunities was visible when Equity Residential (a REIT) bought three high-quality New York City apartment buildings from Macklowe (which is unlisted) at attractive, but not distressed, pricing at the 5.6% cap rate level. Equity Residential's stock outperformed in the period, as did the apartment sector as a whole (+8.4%). The deal highlighted a means other than IPOs through which public market capital will be important in the re-equitization of the private commercial real estate sector.

In the United Kingdom (+0.9%),<sup>2</sup> there were additional signs of rebounding demand for office space in the City, London's banking district. Financial institutions leased more than 1.4 million square feet of space in the area during the second half of 2009, according to Knight Frank, a global property consultant.

France (-3.1%) was pulled down by Unibail Rodamco, Europe's largest mall operator. The stock sold off after management announced that 2010 profits were likely to be flat due, in part, to low-to-negative inflation index adjustments that are used to set rental rates. Earlier in the month, Unibail announced that it would pay \$976.6 million to acquire Simon Ivanhoe, a joint-venture company that owns seven European shopping centers.

Germany (-1.7%) was hindered by surprising declines in consumer confidence and the Ifo Business Climate index, a leading indicator of economic activity. The Netherlands'

## INDEX PERFORMANCE

| Period   | FTSE EPRA/<br>NAREIT Developed<br>Real Estate Index |
|----------|---|
| February | 3.0%  |
| YTD 2010 | -2.9%   |
| 1 Year   | 84.6%   |
| 3 Years  | -14.8%  |
| 5 Years  | 1.9%  |
| 10 Years | 9.8%  |

Total returns of the FTSE EPRA/NAREIT Developed Real Estate Index, an unmanaged market-weighted total return index which consists of many companies from developed markets whose floats are larger than \$100 million and derive more than half of their revenue from property-related activities. Periods greater than one year are annualized. Past performance does not guarantee future results. This information is not representative of any Cohen & Steers account and no such account will seek to replicate an index. You cannot invest directly in an index.

## INDEX CHARACTERISTICS

|                                     |          |
|-------------------------------------|----------|
| Premium to Net Asset Value          | 0.4%     |
| Dividend Yield                      | 4.2%     |
| Price/Cash Flow (est. '10)          | 14.9x    |
| Cash Flow Growth (est. '10 vs. '09) | -0.4%    |
| Cash Flow Growth (est. '11 vs. '10) | 6.8%     |
| Long-Term Cash Flow Growth          | 5.1%     |
| Weighted-Average Market Cap.        | \$9.0B   |
| Total Market Capitalization         | \$745.3B |
| Number of Securities                | 274      |

Source: Cohen & Steers

Characteristics are market capitalization-weighted averages of estimates for companies in the FTSE EPRA/NAREIT Developed Real Estate Index.

(1) Sector returns as measured by the FTSE NAREIT Equity REIT Index.

(2) Country returns are in local currency as measured by the FTSE EPRA/NAREIT Developed Real Estate Index.

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## INDEX PERFORMANCE BY COUNTRY

|                      | February     |              | YTD 2010     |              |
|----------------------|--------------|--------------|--------------|--------------|
|                      | USD          | Local        | USD          | Local        |
| <b>North America</b> | <b>5.4%</b>  | <b>5.5%</b>  | <b>0.3%</b>  | <b>0.2%</b>  |
| Canada               | 3.5%         | 4.4%         | 5.6%         | 4.7%         |
| United States        | 5.7%         | 5.7%         | -0.3%        | -0.3%        |
| <b>Asia Pacific</b>  | <b>2.5%</b>  | <b>3.2%</b>  | <b>-4.7%</b> | <b>-3.8%</b> |
| Japan                | -1.8%        | 0.2%         | -2.3%        | 2.4%         |
| Australia            | 1.3%         | 2.1%         | -1.5%        | -1.9%        |
| New Zealand          | 0.0%         | -1.0%        | -2.9%        | -6.8%        |
| Hong Kong            | 7.5%         | 7.5%         | -7.0%        | -7.1%        |
| Singapore            | -1.3%        | -1.4%        | -8.2%        | -8.3%        |
| <b>Europe</b>        | <b>-0.3%</b> | <b>-3.0%</b> | <b>-3.0%</b> | <b>-7.6%</b> |
| Switzerland          | 3.7%         | 1.9%         | 7.0%         | 3.1%         |
| Italy                | 8.3%         | 6.3%         | 8.2%         | 2.9%         |
| Sweden               | 4.0%         | 7.4%         | 2.4%         | 2.8%         |
| Germany              | -1.7%        | -3.5%        | 1.8%         | -3.1%        |
| Finland              | -0.6%        | -2.4%        | -0.2%        | -5.0%        |
| Belgium              | 1.1%         | -0.7%        | -0.7%        | -5.6%        |
| Netherlands          | 1.6%         | -0.3%        | -1.5%        | -6.3%        |
| France               | -3.1%        | -4.9%        | -2.4%        | -7.2%        |
| Austria              | -4.0%        | -5.8%        | -6.7%        | -11.3%       |
| United Kingdom       | 0.9%         | -4.2%        | -6.2%        | -11.6%       |
| Norway               | -15.7%       | -15.9%       | -15.6%       | -17.5%       |
| Greece               | -4.1%        | -5.9%        | -14.3%       | -18.5%       |
| <b>Overall</b>       | <b>3.2%</b>  | <b>3.0%</b>  | <b>-2.4%</b> | <b>-2.9%</b> |

Source: Wilshire Atlas

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(+1.6%) outperformance occurred amid little company-specific news in February. Belgium (+1.1%) was lifted by office owner Cofinimmo, which reported solid results for its 2009 fiscal year.

### Hong Kong developers recovered

Hong Kong (+7.5%) paced Asia Pacific's gain. The stocks of developers rebounded from last month's sell-off. Strong bidding at the year's first land auction and milder-than-expected policy measure proposals in the finance secretary's budget speech were positive drivers. The policy measures centered on cooling the ultra-hot luxury residential market by encouraging the development of small- and medium-size residences.

In Japan (-1.8%), most developers languished during the month, while J-REITs rose slightly as they continued to demonstrate access to capital through secondary market equity issuances. Property market fundamentals softened in January as vacancy rates rose 0.2%, and now approach 8.3%.

Australian property companies (+1.3%) reported earnings that were generally in line with expectations, although shopping center owner Westfield Group's 2009 operating income was at the low end of its guidance range. The disappointing results were attributable to Westfield's overseas holdings; occupancies and rental rates in Australia's major markets held firm. Singapore (-1.3%) was pulled down by residential developers, which sold off after the government announced measures to curb speculative activity in the residential market.

### Portfolio performance

Our portfolios outperformed their benchmarks in the month, aided by favorable stock selection in the United States, particularly within the retail sector, as we had a significant overweight in DDR. Stock selection in Canada (which had a total return of +3.5% within the index) also contributed to performance; we were overweight companies operating in the country's Western housing market, where home prices rose in January.

We had an overweight in Hong Kong, which helped relative return, although stock selection in that market offset most of the benefit; we did not own a developer that was among the best overall performers for the month. Our allocations to Brazil and Australia were likewise positive.

Our stock selection and overweight in the United Kingdom modestly detracted from performance. That notwithstanding, we maintain a positive long-term view on the market, and valuations, in our opinion, are compelling. As the financial services sector emerges from the difficulties of 2007-2009, we expect to see greater demand for office space and rising rents and valuations.

### INVESTMENT OUTLOOK

We expect moderate U.S. economic growth to continue in 2010, and job growth to emerge in the middle of the year. This should translate into improving real estate fundamentals in 2011. Our focus is on companies with attractive valuations that stand to outperform in this environment. We see a number of such companies in the apartment, hotel and shopping center sectors. Within shopping centers, we believe the big box anchor

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stores have put the worst behind them, but smaller retailers still face challenges.

Over the next few years, real estate companies are in a position to grow their dividends in the low double digits from current historically low levels. We may see significant cash dividend increases this year as certain U.S. companies retreat from emergency measures taken during the financial crisis, such as paying dividends in stock.

## A turn in the U.K. cycle

The acquisition phase of the new total-return cycle in the United Kingdom has begun, and we are seeing an increase in transactions and stabilization in values. Office owners may benefit from a 20-year-low development pipeline in London. We remain cautious on the country's retail sector; consumer spending is likely to remain sluggish through 2010 amid rising taxes and high unemployment.

We are somewhat cautious on the Paris office market. While vacancies are currently at acceptable levels, new supply is growing and rents are beginning to come under pressure. The retail and residential sectors offer better value, in our view. The Netherlands' office market suffers from long-term structural issues: an oversupply of space and high proportion of outdated properties.

## Signs of economic growth in Asia Pacific markets

Hong Kong's economy continues to improve, with fourth-quarter 2009 gross domestic product growth coming in at 2.6%, compared with -2.4% in the third quarter. There are also signs that the office market is bottoming, with recent demand recovery coming chiefly from companies in China.

Japan's residential market is showing signs of recovery due to improved affordability. Office leasing activity is also picking up as a result of falling rents. J-REITs have begun to issue equity to fund acquisitions, and this improvement in liquidity could benefit developers.

We expect Australia's central bank to continue to raise short-term interest rates. Strong economic growth, however, could counter rising rates, and we remain positive on the country's property market fundamentals. In Singapore, we are turning positive on sectors driven by external demand recovery, notably office and hotels.

If real estate companies are at the beginning of a new acquisition cycle, as we believe, those with the strongest balance sheets, greatest liquidity and best management teams have the potential to see significant increases in profitability. We will continue to focus our investment strategies on these companies.

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