



ANALYST QUICK NOTES

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Real Estate ETFs

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Investment Thesis

- After being left behind in the immediate aftermath of the November election, income-oriented strategies have since gained some traction:
 - The Real Estate Select SPDR (XLRE) bottomed on December 1, and has since climbed 4.9%.
- In general, we expect Trump administration policies to be favorable to the real estate sector.
 - One exception may be hospital REITs, such as Ventas and HCP. These could be negatively affected by a potential repeal and replacement of the Affordable Care Act, although recent efforts to repeal were not successful.
- The economy has been expanding fast enough to increase demand for real estate, though supply is growing more slowly.
- On the negative side, REIT stocks are sensitive to rising interest rates, as their dividend yields appear less attractive when government bond rates rise.
 - Mortgage financing for properties also becomes more costly in a rising-rate environment.
- We like the positive trends in same-store net operating income in storage and retail REITs, and note that housing REITs are benefiting from improvement in household formation.
- Shopping center REITs, however, are in a poor position, facing tenant bankruptcies and having turned to redevelopment and asset improvement to generate net operating income. In general, we would avoid them.
- Low cap rates have contributed to high asset prices, and M&A may stay muted until better deals can be found.

- Argus recently raised its rating on the Real Estate sector to Market-Weight from Under-Weight.
 - We believe that concerns about rising interest rates are now largely priced into the REIT sector, which may be able to translate these increases into higher rental rates.
 - To mimic the 3% market weighting of Real Estate in the S&P 500, in our ETF Model Portfolios we recommend iShares US Real Estate (IYR), where the top 10 holdings include a number of Buy-rated names from Argus, such as American Tower Corp. (AMT), Public Storage (PSA) and Weyerhaeuser Co. (WY).
 - Other favored Real Estate ETFs with Argus BUY-rated names as prominent positions include Vanguard REIT Index Fund (VNQ), which sports a very low expense ratio of 0.12%, and Schwab US REIT ETF (SCHH), with an expense ratio of 0.07%.
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