Global Real Estate Securities Market Update

Fourth Quarter 2024

January 9, 2025

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Before we get started

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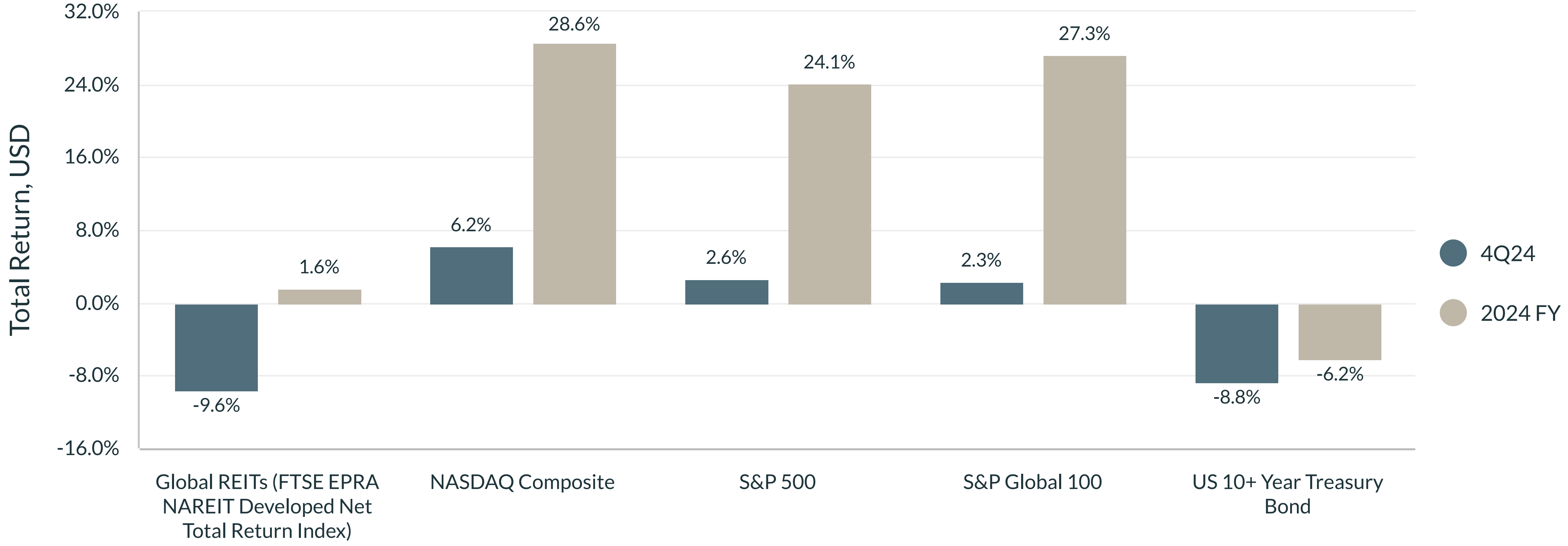
Global REIT Market Performance

REITs hit the brakes in the fourth quarter

REIT share prices plunge during Q4 2024, after Q3 2024 spike. Tech-heavy NASDAQ and S&P 500 pummeled real estate stocks, while bonds sagged, performing roughly in line with REITs

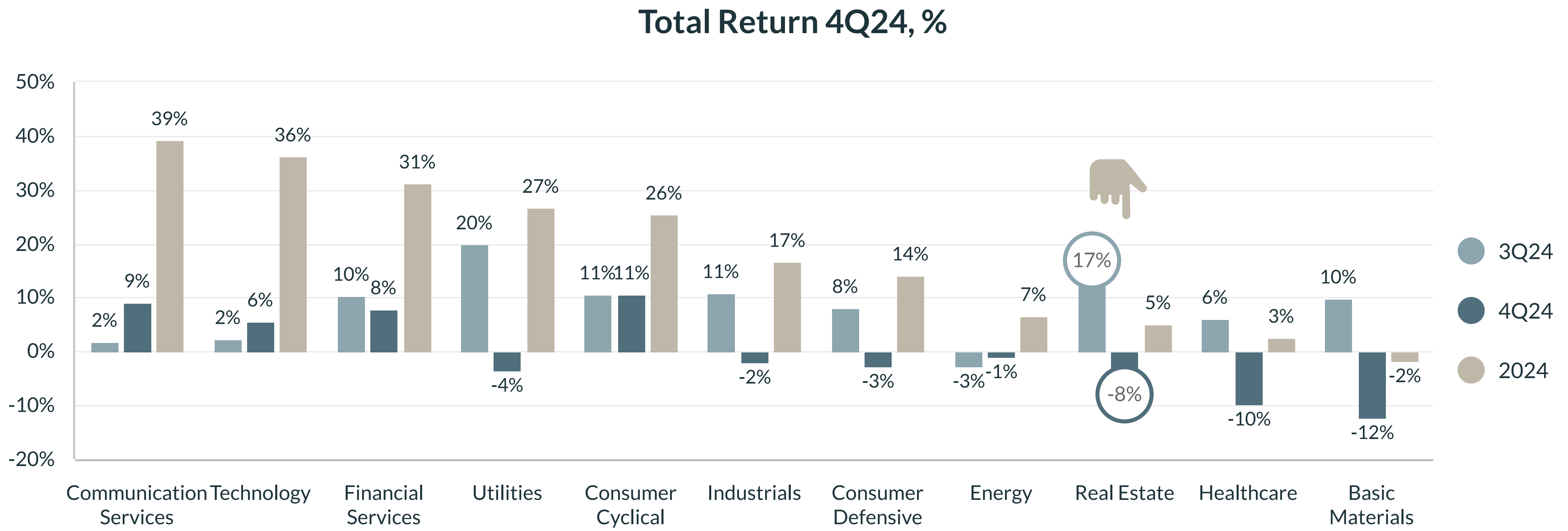
Total return of capital market indexes, USD returns



Sources: FTSE Russell and Bloomberg, LLC, January 1, 2025

4Q turnaround was especially sharp for real estate

In the fourth quarter, consumer cyclicals led the major stock sectors with gains of 10%, followed by communication services with 9%. Financial services rose sharply by 8% post-election, while technology stocks increased by 6%. In contrast, basic materials, healthcare, and real estate sectors declined by over 7%



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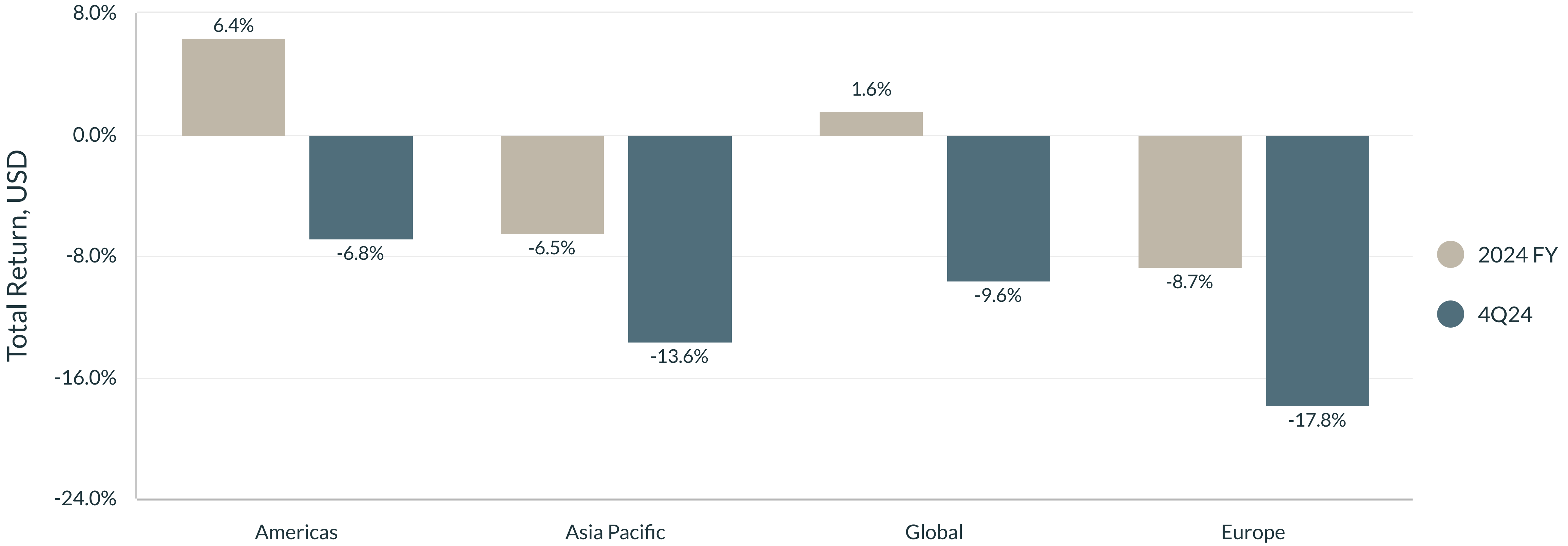
Sources: FTSE Russell and Bloomberg, LLC, December 31, 2024

A global rout to end the year

Globally, the REIT market was down ~10% in 4Q24. Europe (-17.8%) saw the most damage, but Asia Pacific (-13.6%) was likewise punished. Americas REIT stocks were the "winner", down -6.8%

Total return of FTSE EPRA NAREIT Real Estate Equity Indexes, USD

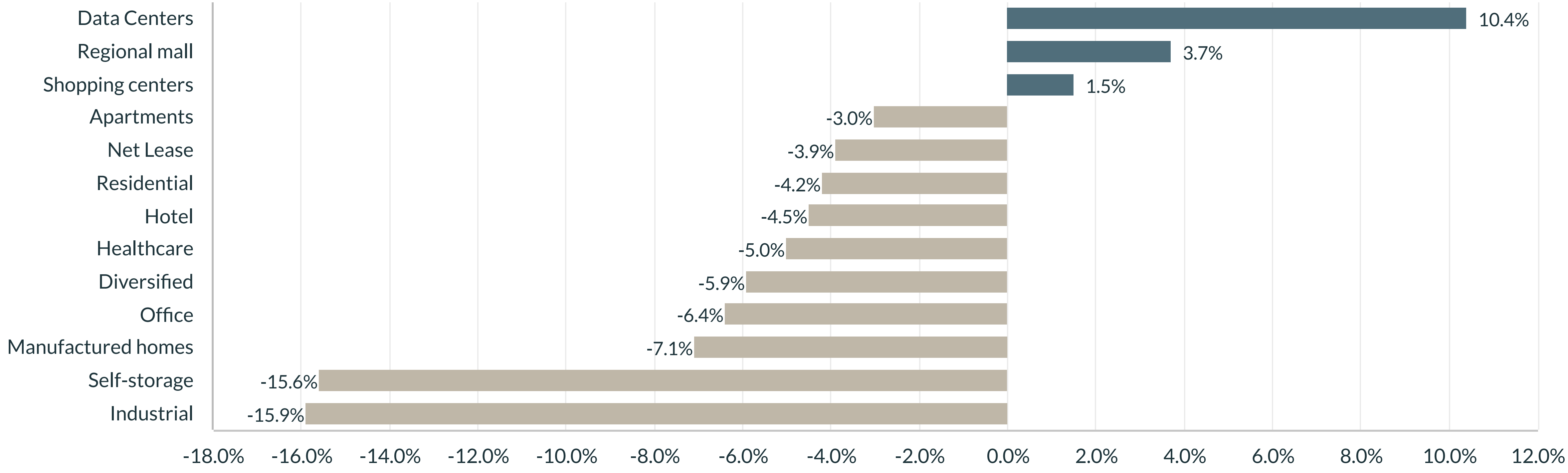


Source: FTSE™, EPRA®, Nareit® January 2, 2025. Returns based in U.S. Dollars

Data centers and retail REITs continue to run, while other sectors stumble

Data centers (+10.4%) and regional malls (+3.7%) outperformed (again!). Industrial and self-storage sectors suffered the most significant losses at -15.9% and -15.6% respectively

Total return of U.S. REIT property types, 4Q24



Source: NAREIT, market data as of December 31, 2024

Big REIT themes for 2025

Relative Pricing Power

Data centers, shopping centers, and healthcare sectors may see (even) better pricing. Life sciences and West Coast offices face challenges, with potential rebounds in industrial and multifamily

Government Policies and Regulations

The government's initiatives could drive up property values, yet potentially escalate inflationary pressures, presenting a complex economic landscape to navigate

Labor Costs and Tenant Credit

Tight labor markets and rising costs may squeeze margins in cold storage and retail. Consumer and tenant credit health remains crucial for retail, net lease, and warehouse REITs

Debt Capital and Transaction Volume

Debt costs may hinder, but transactions likely to recover if the Fed cuts rates. Increased capital deployment supports continued large transactions

CRE Fundamentals Rebound

A rebound in commercial real estate fundamentals is anticipated in late 2025, particularly in sectors like apartments and industrial, though caution is advised against expecting too steep a recovery

Cap Rate and M&A Activity Trends

Cap rates may stabilize in 2025 based on Fed policies and CRE performance. Consolidation possible in office and net lease sectors due to capital cost disparities

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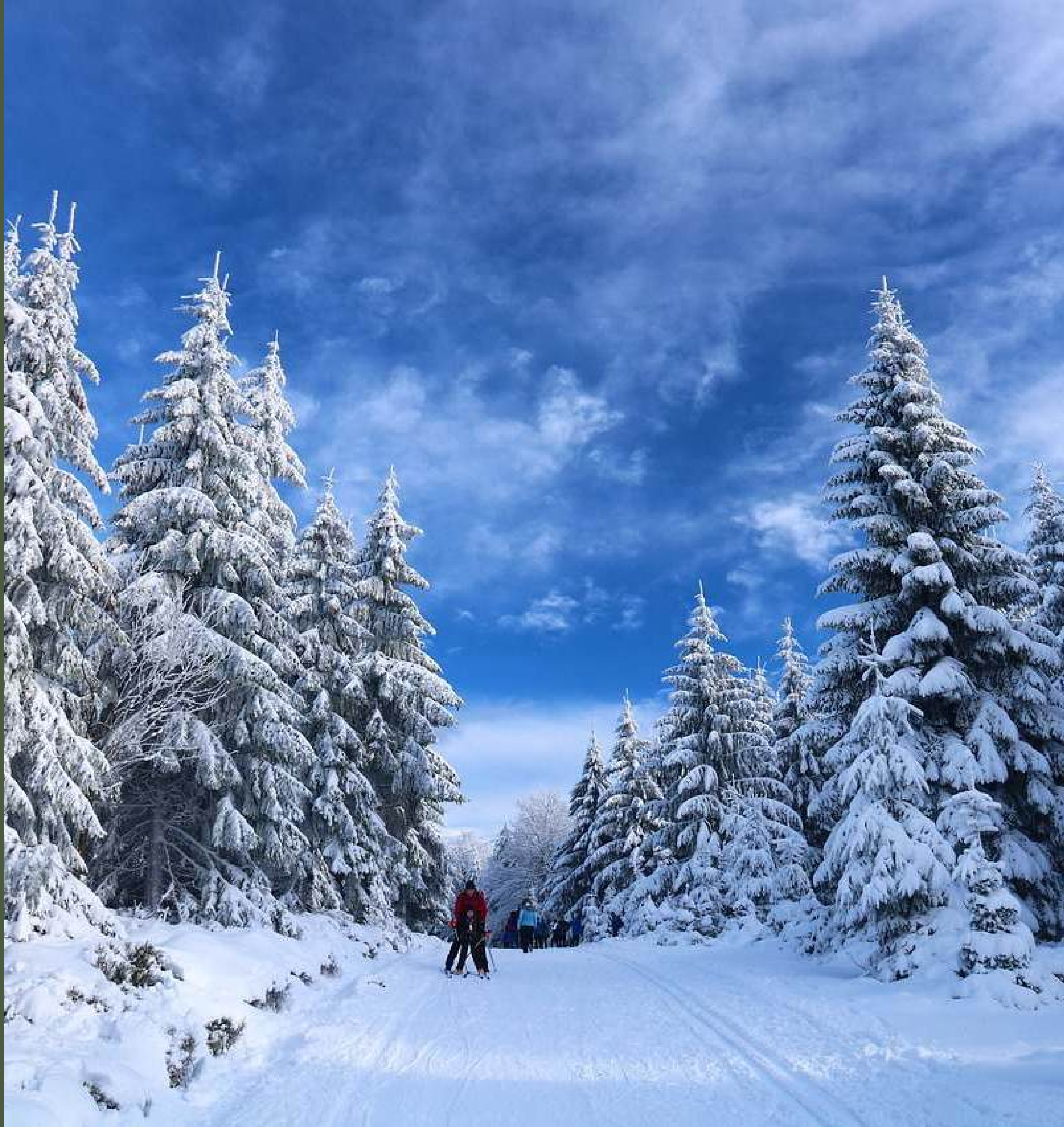
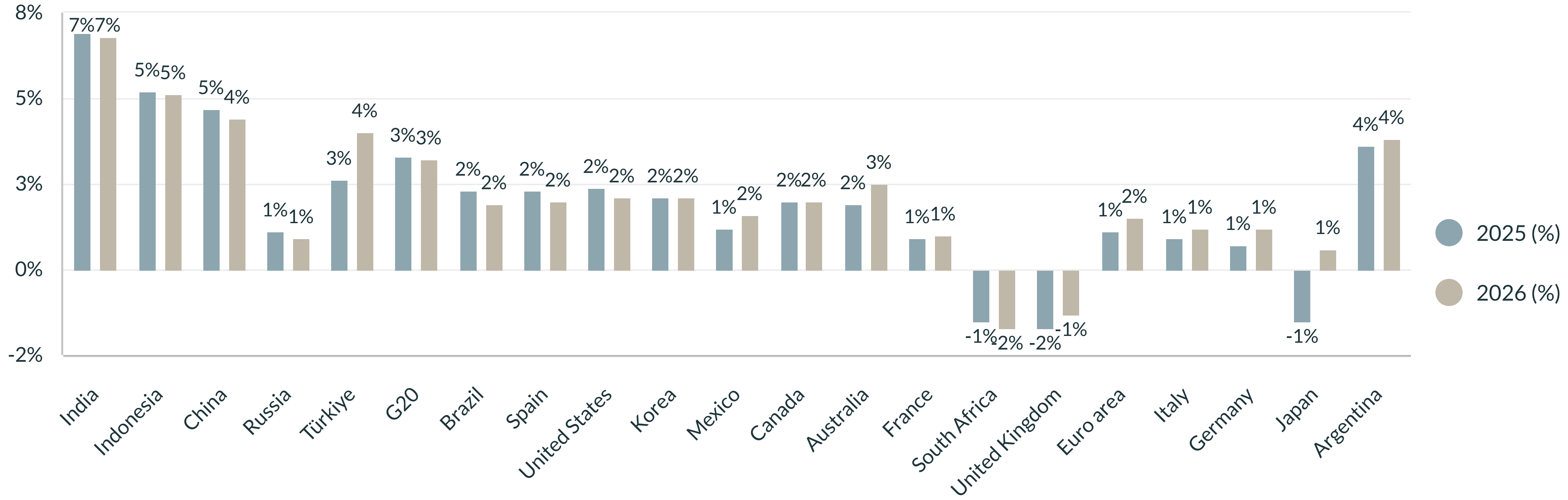
Investment Backdrop



Global GDP growth is projected to remain stable

The OECD forecasts that global GDP growth will strengthen slightly to 3.3% in 2025 and remain stable at this level through 2026

Real GDP growth projections for 2025 and 2026, %, year-on-year

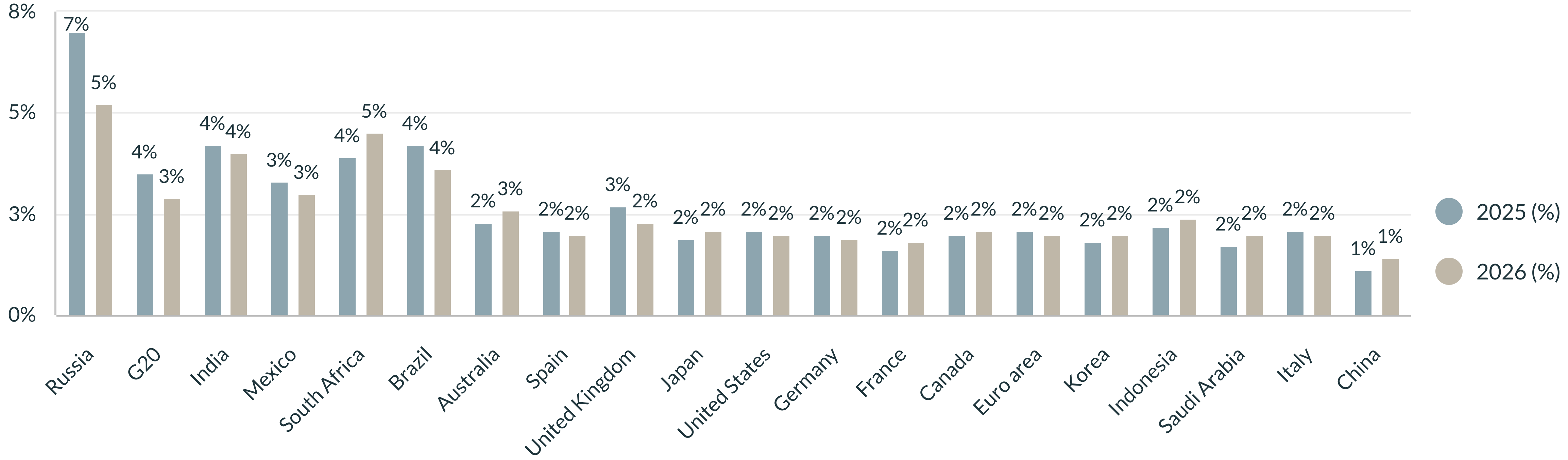


Source: OECD (2024), *OECD Economic Outlook, Volume 2024 Issue 2*, OECD Publishing, Paris, https://doi.org/10.1787/d8814e8b-en.

Inflation expected to fall further, but stickiness persists

Headline inflation continues to ease in most countries, driven by declining food, energy, and goods prices. **However, stubborn services inflation remains high** at around 4% in the OECD. Inflation in G20 economies is expected to return to target by 2025-2026

Headline inflation projections for 2025 and 2026, %, year-on-year

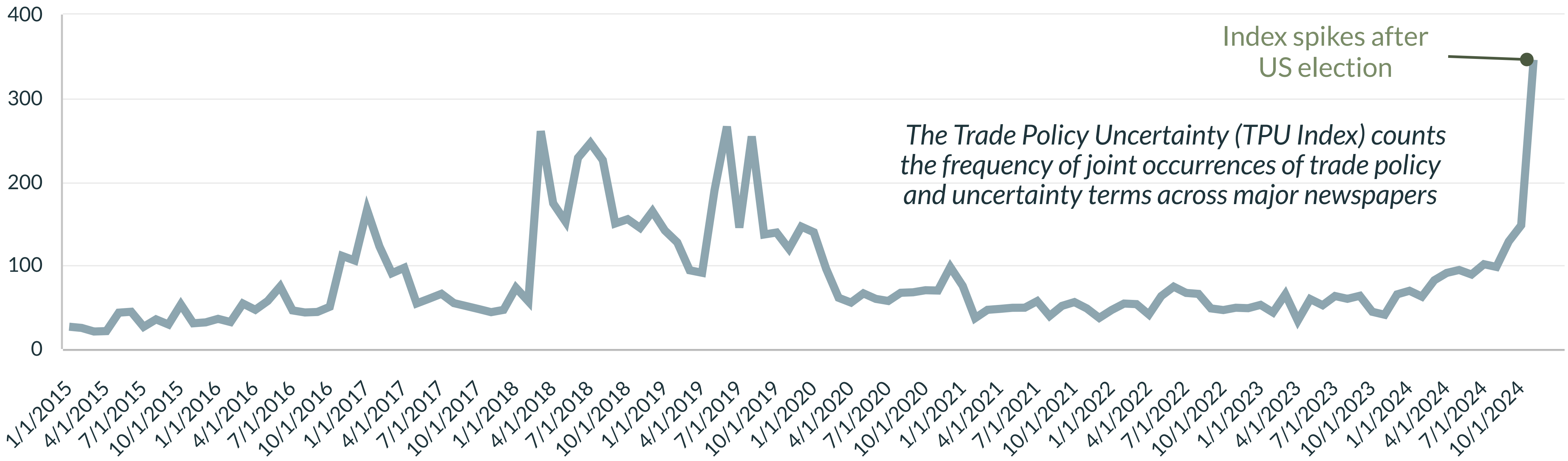


Source: OECD (2024), *OECD Economic Outlook, Volume 2024 Issue 2*, OECD Publishing, Paris, https://doi.org/10.1787/d8814e8b-en.

Trade policy uncertainty at an all-time high...

While the overall economic outlook suggests resilience, uncertainties persist, including trade. Geopolitical tensions disrupt energy and supply, fueling inflation and dampening growth. A fragmented, protectionist trade environment could negatively impact competition, prices, and productivity

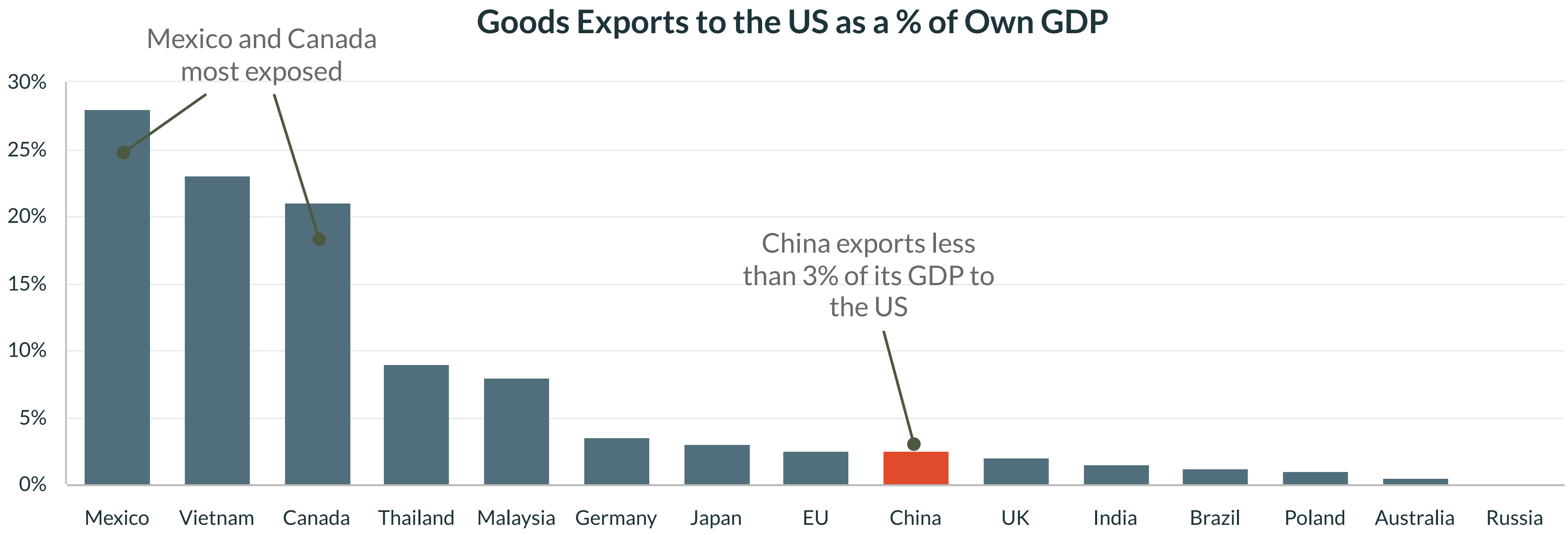
Trade Policy Uncertainty (TPU) Index, January 2015-November 2024



- Source: Caldara, Dario, Matteo Iacoviello, Patrick Molligo, Andrea Prestipino, and Andrea Raffo (2020), "The Economic Effects of Trade Policy Uncertainty," *Journal of Monetary Economics*, 109, pp.38-59.

...but most countries have limited exposure to US trade

Most economies are less exposed to trade with the US than tends to be assumed. We expect that the size of tariffs will be curbed by negotiations and deals around other issues such as immigration, and that their impact will be reduced by an appreciation of the dollar



Source: Capital Economics, *Q1 2025 Global Economic Outlook*, January 2025

Global central banks moving from tight to loose

With few exceptions, global monetary policy is **transitioning from tightening to easing**. Central banks are considering rate cuts, but remain cautious to avoid reigniting price pressures

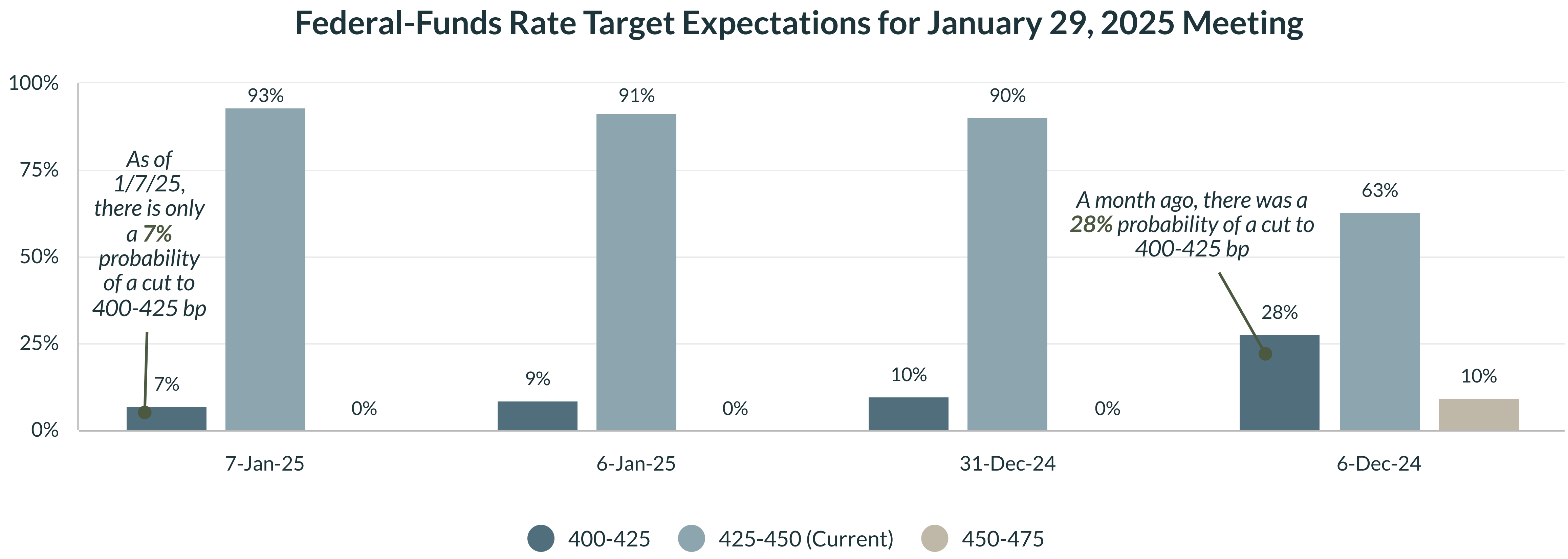
The U.S. and Eurozone face differing economic conditions, with the **Eurozone showing quicker declines in inflation,** suggesting the ECB may ease policy more assertively than the **Fed**. The **BoE** voted 6-3 to keep rates unchanged at the December meeting, with three policymakers preferring a rate cut

BoJ Governor Kazuo Ueda's recent comments didn't offer any hints about the timing of a rate **hike**

Source: CFR's Global Monetary Policy Tracker, https://www.cfr.org/global/global-monetary-policy-tracker/p37726

The Fed cuts the number of cuts

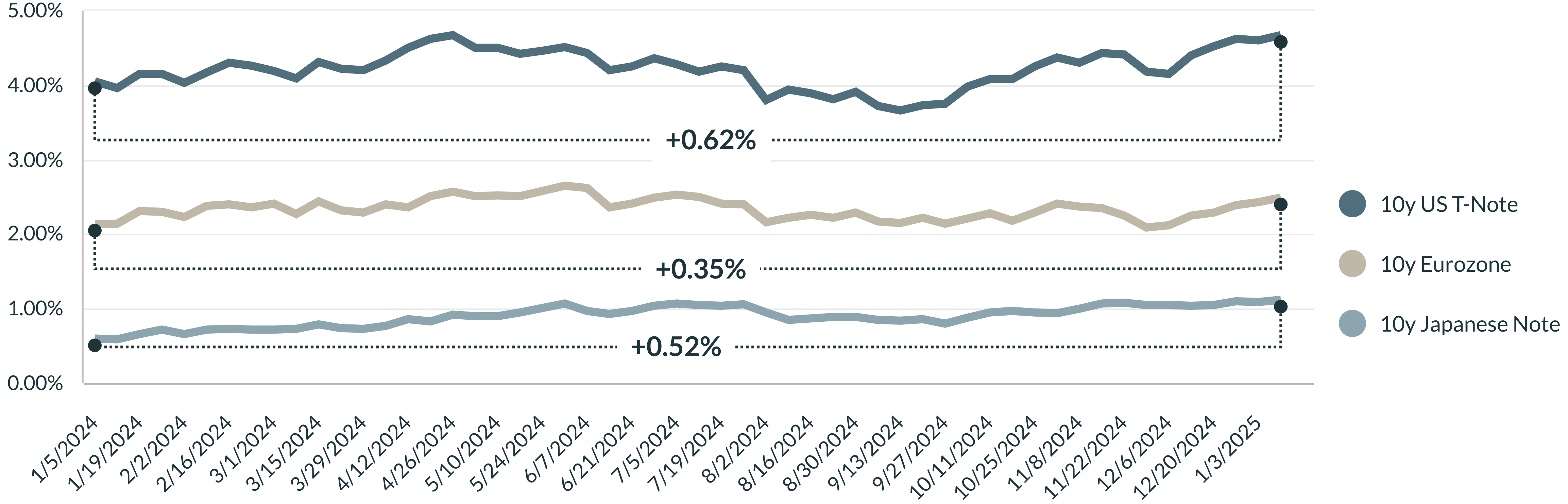
The Fed surprised the markets in December, not with a quarter-point cut, but by forecasting only two 2025 rate cuts, down from the previously projected four



Source: CME FedWatch, https://www.cmegroup.com/markets/interest-rates/cme-fedwatch-tool.html

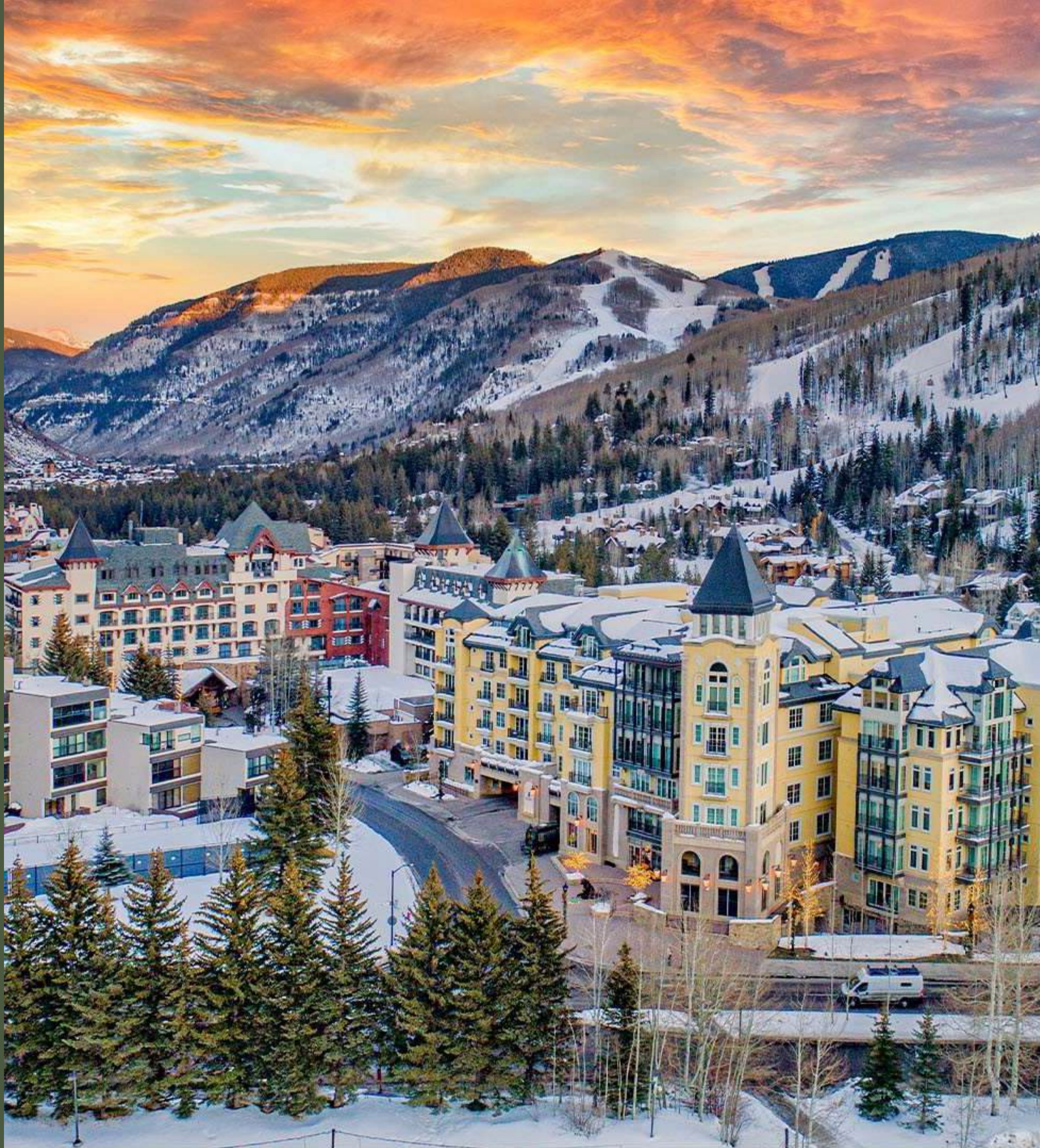
Long term interest rates have risen

10 year bond yields rose in the fourth quarter - nearly 100 bp in the U.S. Across the globe, the cost of borrowing is higher now than at the beginning of the year, flummoxing many investors who had expected rates to fall. Most notable run-up has been in Japan



Sources: Bloomberg, LLC, January 7, 2025

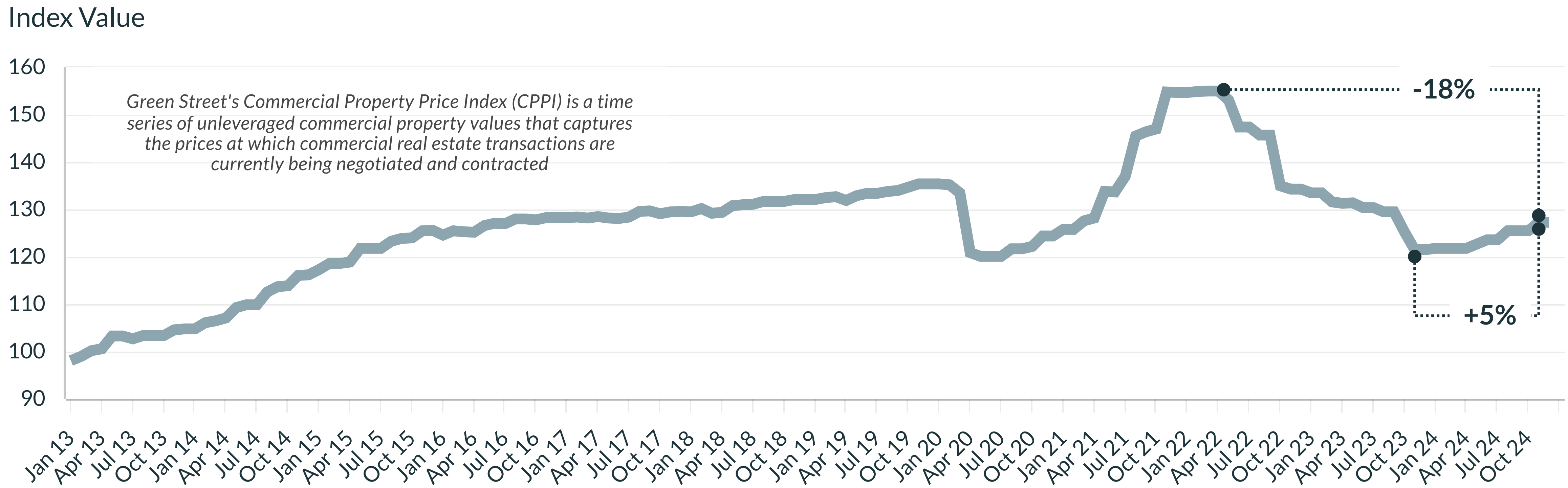
Global Real Estate Markets



Commercial property prices up 5% this year

Property prices have fallen 18% from their 2022 peak but increased about 5% in 2024, per Green Street. But "**the outlook for this year is not as bright**. The run-up in Treasury yields over the past few months is likely to cause property prices to stagnate”

Green Street U.S. Commercial Property Price Index (CPPI)



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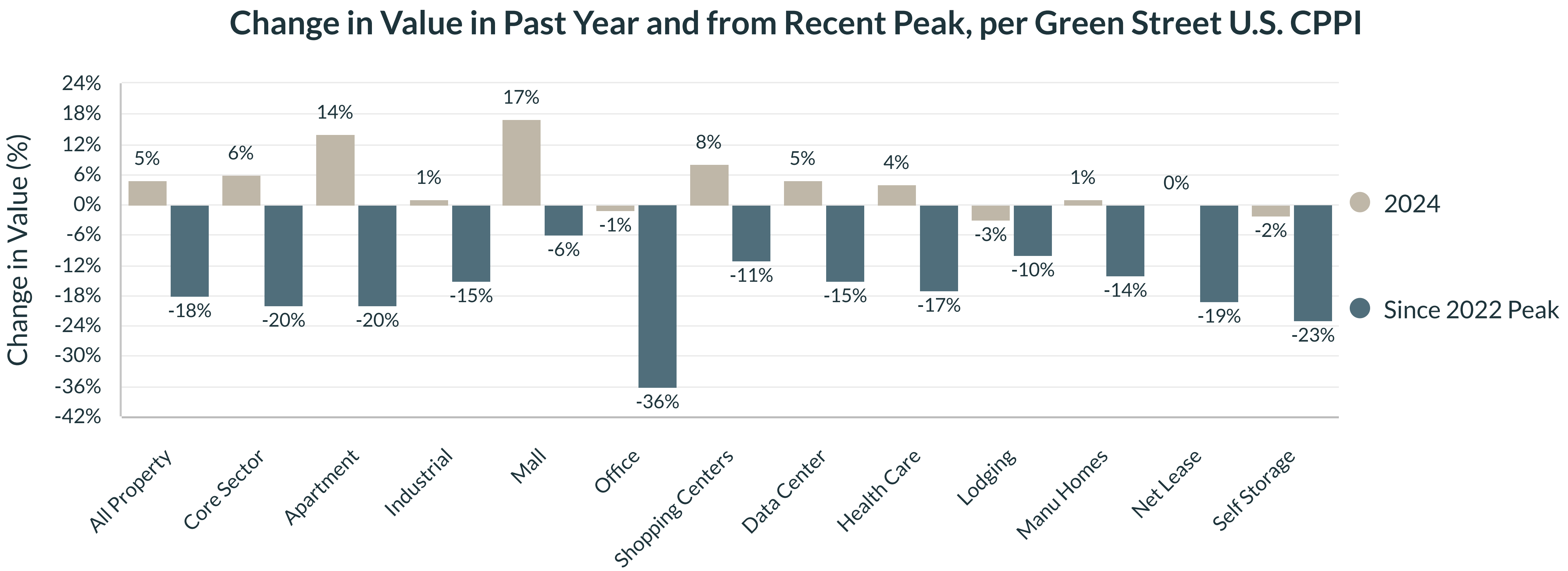
Source: Green Street Advisors, LLC, January 7, 2025

Retail and apartments rise above the rest

In 2024, **malls** were up 17%, **strip retail** was up 8%, and **apartments** were up 14%. On the downside, **office** was down 1%, **self storage** was down 2%, and **lodging** was down 3%. All sectors are below their 2022 peaks



Source: Green Street Advisors, LLC, January 7, 2025

Transaction outlook improving despite evolving risks

Transaction volumes appear to have turned a corner. However, risks persist from geopolitics, conflicts, and supply chain threats

Investment volumes annual change by region, 2007– 3Q24

- Global investment volumes rose 26% to $182 billion in the third quarter, reflecting a 6% year-to-date increase
- Investors are prioritizing growth sectors, particularly alternative properties. Diversification remains a priority

Source: JLL Global Real Estate Perspective - Highlights, November 2024

Private investments in data centers reach all-time high

In 2024, digital infrastructure GPs struck a record-breaking **$108.1 billion** in deals for data centers and related markets—over three times as much money as they spent in the previous year

Company name	Select investors	Deal size ($B)	Deal date	Deal type
AirTrunk	Blackstone, Canada Pension Plan Investment Board	$16.0	9/4/2024	Buyout
Vantage Data Centers Management Company	DigitalBridge Group, GiantLeap Capital, Pantheon Infrastructure, Silver Lake	$9.2	6/13/2024	PE Growth
DataBank (Dallas)	Ardian, AustralianSuper, DigitalBridge Group, Swiss Life Asset Management	$2.0	10/15/2024	PE Growth
EdgeCore Internet Real Estate	Partners Group	$1.9	9/6/2024	PE Growth
Echelon Data Centres	Starwood Capital Group	$1.9	2/15/2024	Buyout
eStruxture Data Centers	Fengate Asset Management, Pantheon, Partners Group	$1.3	6/18/2024	Buyout
ST Telemedia Global Data Centres	KKR, Singtel	$1.3	6/1/2024	PE Growth
Cellnex Austria	EDF Invest, MEAG, Vauban Infrastructure Partners	$0.9	8/9/2024	Buyout
SummitIG	SDC Capital Partners	$0.8	4/30/2024	Buyout
DC BLOX	Bain Capital Credit, Post Road Group	$0.7	10/8/2024	PE Growth

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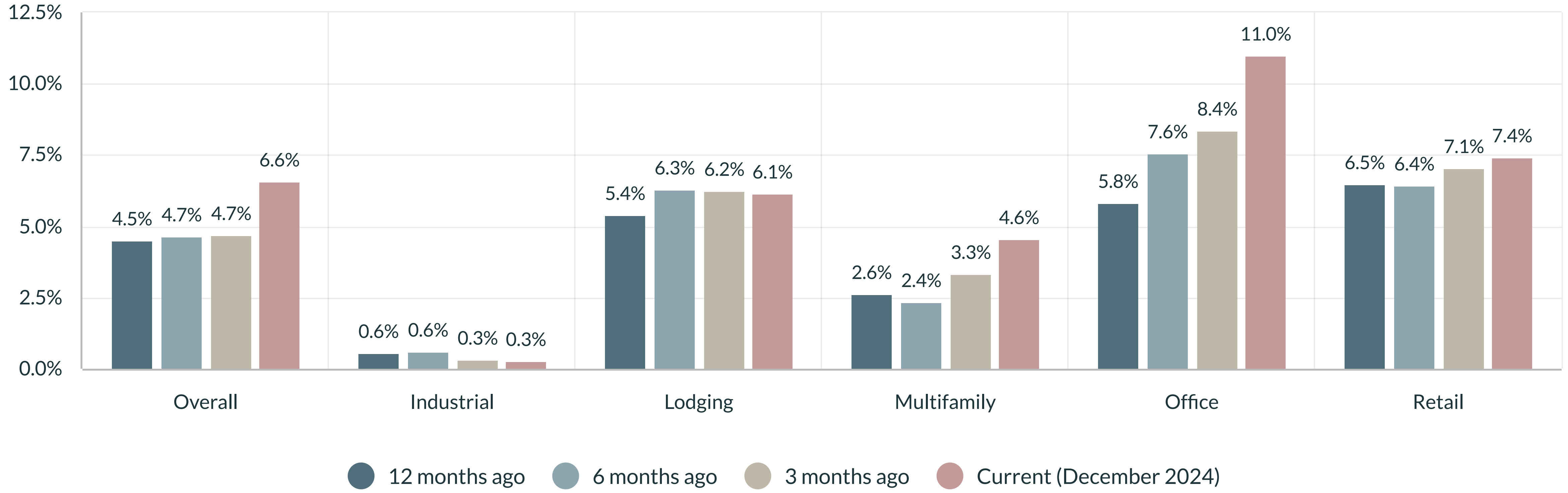
Source: PitchBook, *PE takes pick-and-shovel approach in AI gold rush*, January 8, 2025

CMBS delinquency rate rises, led by office

The Trepp CMBS delinquency rate climbed 191 basis points in 2024, with the office rate reaching 11%. Paradoxically, CMBS issuance surpassed $100 billion, nearly tripling the prior year

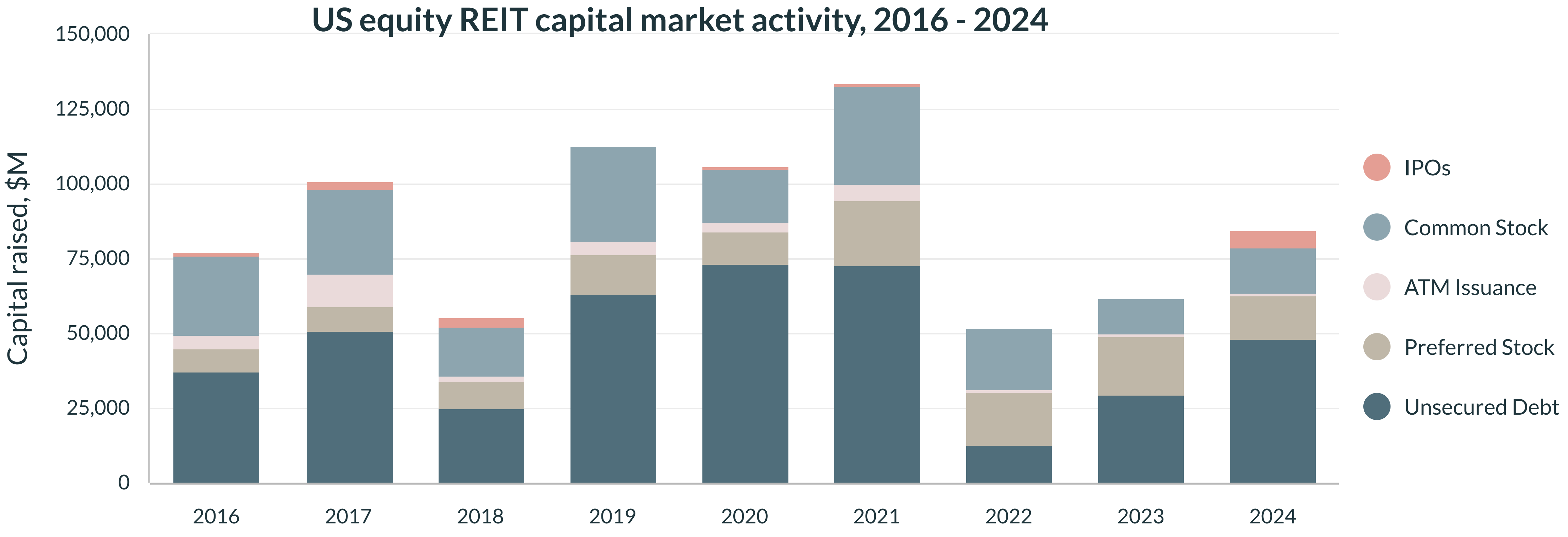
Special servicing rate by property type (%)



Source: Trepp CMBS Research, January 2025

REIT capital raising broke through in 2024

In 2024, a total of $85 billion was raised through 167 **public** offerings. Note that this does not include **private** debt and equity raised by public REITs. Capital raising peaked in 3Q with $30.5 billion raised, followed by a notable slowing in 4Q

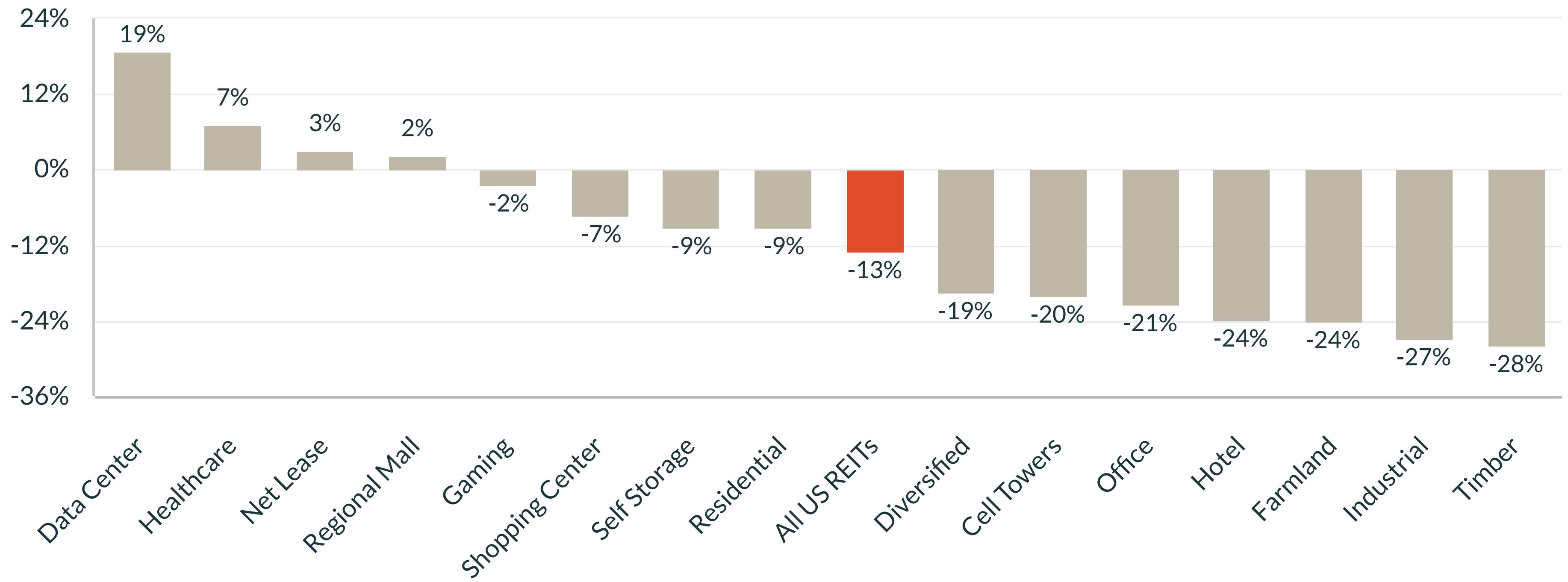


Source: Nareit, S&P Global Market Intelligence, January 2025

REIT rout reveals notable discounts

Share prices for REITs plunged in December, closing the year at a median 13% discount to NAV. The timber sector faces the steepest discount at -28%, followed by industrial at -27%. Conversely, data centers are trading at the highest premium, +19%

Premiums / discounts to REIT NAV by U.S. sector



Source: S&P Global Market Intelligence LLC, December 31, 2024

U.S. REITS TRADE AT A **13% DISCOUNT** TO PRIVATE MARKET VALUES

Positioning: hurry up and wait

Three months ago, the REIT market seemed poised for a breakout after a +16% return in the third quarter, raising year-end expectations. However, the fourth quarter proved disappointing as the Fed executed its hawkish cut and new administration policies emerged, leading to rising long-term interest rates. While data centers and retail REITs delivered positive returns, most other sectors struggled. Nevertheless, key sectors like data centers, seniors housing, shopping centers, and high-quality office buildings continue to experience strong demand. Looking ahead, we remain optimistic that a Goldilocks economy will emerge, with moderating interest rates and sustainable growth creating a favorable environment for REITs.

- ## Valuation
  - REIT Price/FFO multiples (19x on a weighted average basis, 14x straight average) are trading below the S&P 500 P/E multiple (30x).
  - Price/NAV -26% globally and -13% in the U.S.
  - Small caps trading at notable discounts to larger peers
  - Sectors have gapped out

- ## Fundamentals
  - REITs should generate ~3-4% NOI growth in 2025
  - Supply remains below average levels, except for pockets such as Sunbelt multifamily and industrial
  - Demand for most property types remains steady; self storage remains an exception; office coming back, especially at the high end
  - Industrial may see an inflection point upward
  - Senior housing continues to thrive
  - In residential, manufactured housing looks to be best positioned relative to multifamily and SFRs

- ## Growth
  - Consensus REIT FFO estimates remain at ~4-5% earnings growth in 2025

- ## Capital
  - Borrowing rates rose this quarter as spreads remained high and base rates went up
  - Fed cutting overnight rate by 25 bp but reducing the number of expected 2025 cuts from 4 to 2 weakened sentiment and activity
  - REIT balance sheets in the best shape in recent memory, with average leverage ~33%
  - REIT capital raising in 2024 marked the second year in a row of significant expansion
  - We expect more M&A in 2025

- ## Portfolio preferences
  - **Data centers**: Strong demand for data centers continues to outpace supply
  - **Health Care**: The healthcare sector is growing rapidly, fueled by demand for senior living facilities and skilled nursing centers
  - **Shopping Centers**: Shopping centers have resilient tenants and are seeing strong leasing despite bankruptcies; valuations still appealing
  - **Digital infrastructure (e.g. billboards)**: Digital billboard stocks are attractively priced and the industry is set for notable growth
  - **Industrial**: The industrial REIT market is stabilizing despite increasing vacancies and low demand; hope for a 2025 recovery
  - **Residential**: Residential REITs thrive as demand for multifamily, manufactured housing, and single-family rentals rises due to housing affordability challenges
  - **Net Lease**: Companies are on the hunt for new assets; cap rates have risen but so has costs of capital

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Sector Outlooks

Industrial: inching toward an inflection point

Industrial REITs were hammered in 2024. Now, despite near-term uncertainty, we believe these risks are largely priced in. Deliveries are expected to decline, while demand drivers remain stable, supporting occupancy rates. Absorption is anticipated to return to pre-pandemic levels later this year

- **Market overview**
  - We see modest growth for the industrial sector. Stable interest rates would be supportive of valuations
  - We anticipate a slight increase in vacancy rates due to new developments, especially in major hubs like Los Angeles, but remain optimistic about absorption rates
  - Uncertainty remains on where tariffs will shake out
- **Leasing and occupancy**
  - Quarterly net absorption has cooled significantly and continues to trend below its 20-year average. As a result, market rent growth has cooled significantly and is expected to remain muted near term
  - Our forecasts suggest above-average annual net absorption of 750-850 msf over the next three years, with a national vacancy rate of 5.4-6.0%, supporting some market rent growth
- **Investment market**
  - Industrial real estate valuations are down 15% from the 2022 peak but up 1% in 2024. Private market transactions suggest, though, that there is significant capital awaiting deployment into industrial assets
  - REITs have been active; Indus Realty Trust, for instance, acquired a majority interest in 4.3m ft logistics portfolio valued $575m in the Carolinas
- **Valuation**
  - Industrial REITs are trading at a 5.4% implied cap rate. The sector's price per square foot is around $160
  - The 2025 estimated AFFO multiple for industrial REITs is 24x, while the FFO multiple stands at 18x

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Sources: Company reports, Citi Research, Baird Research, Sugi Capital Management

Residential: new leadership

While the long term set up is clear, the short term is murky. Of the subsectors, manufactured housing looks to be in the pole position, with improving earnings. Apartment REITs face low demand, but we see potential growth in some of the coastal names. SFRs have weakened in the last quarter

- ## Market overview
  - **Manufactured housing** is showing improving earnings
  - **Multifamily** is still seeing the impact of low new jobs-to-supply (3.4x in '24 vs. 5.0x historical average)
  - **Single-family rentals** are suffering decelerating pricing
- ## Leasing and occupancy
  - **Manufactured housing**: We see fundamentals bottoming
  - **Multifamily**: Coastal multifamily markets are likely to fare better than the Sunbelt in 2025, but demand could be sluggish in select markets like LA, DC (DOGE), and Washington State faces layoffs at Boeing
  - **Single-family rentals**: SFR investors have become more concerned with rental rate deceleration, in particular for INVH
- ## Investment market
  - Institutional investors are increasingly focusing on multifamily and single-family rental properties
  - Manufactured housing is drawing investment from a different set of buyers. Its lower capital intensity and stability during economic downturns enhance its appeal as a long-term investment
- ## Valuation
  - **Manufactured Housing**: The sector is trading at lower cap rates, ~4.9%, with a higher 2025E AFFO multiple of 24x
  - **Multifamily**: Implied cap rates are ~5.3%, with 2025E AFFO multiple of 22x
  - **Single-Family Rentals**: Implied cap rates are ~5.5%, with 2025E AFFO multiple of 21x

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Sources: Company reports, Morgan Stanley Research, AlphaWise Data, CBRE Research, NAREIT Data, Sugi Capital Management

Shopping centers: on a roll

Burgeoning demand and constrained supply have fueled robust leasing and rental gains across shopping center REITs. With strong balance sheets, these companies are primed for strategic transactions and redevelopment projects. The sector's defensive nature and growth prospects continue to entice private investors

- **Market overview**
  - Shopping centers are enjoying strong fundamentals and accelerating earnings growth, supported by limited new supply and high construction costs
  - Shopping center REITs are pillars of stability, with impressive balance sheets. They have maintained operational efficiency and capital flexibility

- **Leasing and occupancy**
  - The sector benefits from strong tenant demand and limited new entries, which bolsters leasing strength and supports favorable rent renegotiations and renewals
  - Despite near-peak fundamentals with strong tenant retention, there are concerns about the sustainability of current occupancy levels, primarily as future leasing is likely to involve lower rent spreads

- **Investment market**
  - There has been a notable uptick in transaction activities, driven by stabilized financing costs and strong market fundamentals, enabling shopping centers to attract significant investor interest
  - Shopping centers are trading at lower cap rates due to their defensiveness and growth potential
  - Blackstone buying ROIC at a 34% premium was a watershed monent

- **Valuation**
  - Shopping centers are trading at a 6.3% implied cap rate
  - The 2025E FFO multiple for shopping center REITs is 15x
  - The AFFO multiple is 19x

Sources: Company reports, BMO Research, Sugi Capital Management

Regional malls: more re-rating, more bifurcation

The mall sector has recovered from its post-GFC struggles, with top-tier malls performing well, benefiting from higher foot traffic and occupancy rates now exceeding pre-pandemic levels. However, lower-tier malls continue to face challenges, with ongoing vacancy issues and refinancing risks

- **Market overview**
  - A-rated malls thrive with increased traffic and spending, while B and C-rated malls struggle with high vacancies and declining footfall.
  - The rise of luxury retail has stabilized top-tier malls, while lower-tier malls struggle with changing consumer demands
- **Leasing and occupancy**
  - Regional malls are experiencing robust leasing demand across diverse sectors including apparel, food and beverage, and entertainment, leading to a significant occupancy growth (+60 basis points YOY in 3Q) and rent spreads in double-digit territory
  - Management is actively converting temporary or short-term leases to permanent ones, continuing a trend post-COVID
- **Investment market**
  - **Investor Interest in Prime Locations**: Investors flock to thriving regional malls with stable footfall and earnings in volatile retail
  - **Redevelopment and Diversification**: Underperforming malls are being redeveloped into mixed-use spaces with housing, offices, and entertainment in high-value areas
- **Valuation**
  - Malls are trading at a ~7% implied cap rate
  - The 2025E FFO multiple for mall REITs is 15x
  - The AFFO multiple is 16x

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Sources: Company reports, JP Morgan, Sugi Capital Management

Office: back to work

The office stocks have witnessed a notable comeback YTD, bolstered by the recent political shifts. New York City re-emerged as the nation's preeminent office hub, experiencing robust leasing activity. In a positive shift, more employers are requiring employees to spend the majority of workweeks in the office

- ## Market overview
  - The pandemic's impact prompted caution, but office REITs now have an optimistic outlook, with occupancy expected to recover by 2026/2027
  - Strengthening capital markets spur growing real estate transactions and loan refinancing, boosting office building liquidity and potentially benefiting REITs through valuations or acquisitions
- ## Leasing and occupancy
  - An increase in leasing activity is leading to significant capital expenditures, potentially constituting over 30% of NOI, which could strain cash flows due to upfront costs well into 2026/2027.
  - Top-tier office REITs are thriving, drawing tenants to high-quality assets in prime locations, hinting at a positive outlook as the market stabilizes, particularly in the West Coast tech sector
- ## Investment market
  - Transactions of office buildings are picking up, indicating a resurgence in investor interest and confidence in the sector's potential
  - The banking system and CMBS markets are addressing office loan issues. Troubled loans are being restructured, enabling new investments and improving the financial health of office properties
  - With a high proportion of debt refinancing on the horizon (about 30% maturing by end of 2026), office REITs are positioned to face significant earnings pressures compared to an average 20% in the broader REIT sector
- ## Valuation
  - Implied cap rates are at 8.1%
  - Office REITs are trading at a 13x 2025E FFO multiple and a 18X AFFO multiple

Sources: Company reports, JP Morgan, Sugi Capital Management

Healthcare: still running strong

Healthcare real estate is experiencing solid growth, particularly in senior housing and outpatient medical facilities, driven by strong operational improvements and favorable supply-demand dynamics. Accretive acquisitions are prevalent, enhancing sector vitality. Weakness continues, though, in life science

- **Market overview**
  - Healthcare REITs show significant variances due to different focuses on property types, ownership structures, and leverage profiles
  - Senior housing is anticipated to remain a central area of focus within the healthcare REIT sector in 2025, reflecting its critical role in driving sector trends and investor interest
- **Leasing and occupancy**
  - Strong SS NOI growth is expected, particularly in senior housing, due to operational efficiencies and a strong supply/demand balance
  - Despite individual company challenges, outpatient medical properties are expected to continue providing stability to healthcare REIT portfolios. Ongoing acquisitions and developments tied to this property type are anticipated to bolster this trend further
- **Investment market**
  - Accretive acquisitions that became more prominent in 2024 are expected to continue into 2025, particularly in senior housing and outpatient medical facilities
  - Life sciences REITs are focusing on managing significant development and redevelopment pipelines to enhance value, with operational efficiency being a key goal
- **Valuation**
  - Healthcare REITs are trading at wide range of implied cap rates, 4-8%, with senior housing stocks at the low end and life science at the higher end
  - Healthcare REITs are trading at a 14x 2025E FFO multiple on average, 15x on an AFFO basis
  - The sector's premium valuations, especially for Welltower, introduce potential downside risks if growth expectations moderate

Sources: Company reports, Deutsche Bank Research, Sugi Capital Management

Self storage: leasing season's coming

The self-storage sector is showing signs of recovery, with fundamentals expected to improve. Occupancy and move-in rate trends are stabilizing, reflecting a seasonal traffic rebound. However, growth in net operating income remains modest, and industry fragmentation, high valuations, and potential expense increases could impact performance

- **Market overview**
  - After a two-year slowdown, self-storage fundamentals are expected to stabilize and improve in 2025, with core growth indicators showing early signs of recovery
  - The self-storage industry remains highly fragmented, suggesting potential for consolidation and increased competition among operators
- **Leasing and occupancy**
  - Occupancy is expected to remain relatively flat in 2025, slightly below historical levels, as the sector recovers
  - Year-over-year changes in move-in rates are anticipated to turn positive around the second quarter of 2025, driven by seasonal traffic increases and easing year-over-year comparisons, which should support better occupancy and street rate trends
- **Investment market**
  - Self-storage stocks are trading at slight discounts to private market values, but with a lower implied cap rate than the REIT average
  - Investment volumes are down as a significant bid-ask spread exists
- **Valuations**
  - Implied cap rates are at 5.3%
  - The 2025E FFO multiple for storage REITs is 18x
  - The AFFO multiple is 19x

Sources: Company reports, BMO Research, Sugi Capital Management

Net lease: on the hunt

The net lease sector is on the hunt for acquisitions. Most REIT players can make accretive investments, though tenant creditworthiness remains crucial, with some cushion factored into industry projections. The sector's headline earnings exhibit higher quality and closer alignment to cash flow compared to other REIT segments.

- **Market overview**
  - Net lease REITs underperformed the REIT group in 2024 due to external growth and tenant credit concerns, but internal growth met early estimates at 1.4%
  - While some companies like WPC encountered tenant credit issues earlier in the year, others experienced less than expected credit losses
- **Leasing and occupancy**
  - Leasing activity remains stable, though organic growth is limited due to the nature of long-term leases
  - Some deterioration in tenant credit has been observed, with particular caution around investment-grade (IG) and non-IG tenants
  - Some REITs, such as VICI, are benefiting from inflation-linked rent increases, providing protection against rising costs
- **Investment market**
  - External growth picked up in the second half as cap rates moved higher and stock valuations improved
  - Current cap rates for acquisitions are in the high 7s, with blended capital costs in the high 6s, resulting in positive investment spreads
  - Net lease REITs maintain strong balance sheets with mid-5s debt/EBITDA and ATM programs to fund deals. Future dealmaking is sensitive to 10-year yields
- **Valuation**
  - Implied cap rates for net lease REITs are around 6.7%
  - Triple net lease companies trade at 12x FFO multiple and a 12x AFFO multiple on 2025 earnings
  - Despite valuations trading at a 30% discount to the broader REIT market, earnings are in line with the group average

Sources: Company reports, Sugi Capital Management, Sugi NAREIT meetings

Data centers: extended bull run

Data center performance remained strong in 2024, a trend expected to continue in 2025. Robust demand, driven by AI investments, coupled with limited availability and power constraints, has fueled rising prices. We anticipate these favorable dynamics to persist

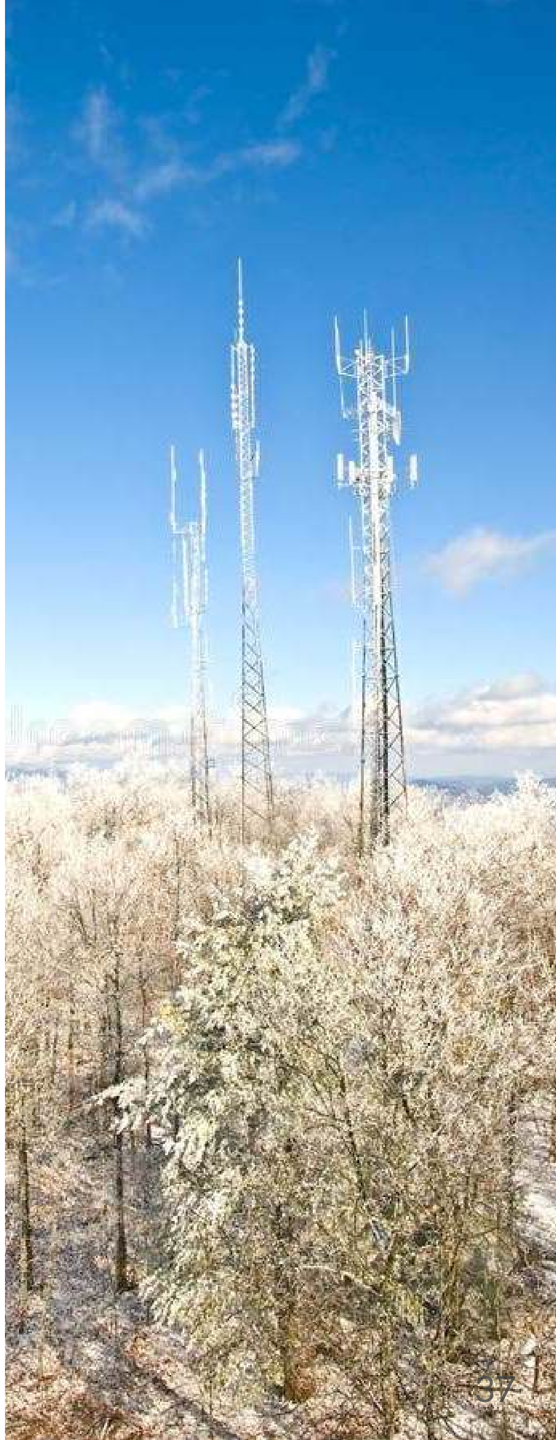
- **Market overview**
  - Surging demand fuels data center growth, as digital era transforms industries
  - Data centers will continue to be driven by strong demand from hyperscalers investing in AI, which is pushing leasing to new highs amidst dwindling availability and power constraints
  - The integration of AI and the deployment of latency-sensitive AI inference models are significantly boosting the data center sector
- **Leasing and occupancy**
  - Data center leasing reached record levels in 2024 despite the challenges of limited power availability and high demand, particularly from AI-driven needs, with no slowdown anticipated in 2025
  - With primary markets nearing full capacity, data centers are expanding into secondary and tertiary markets, accounting for a significant portion of new leasing activities, indicating a strategic shift to accommodate continued demand growth
- **Investment market**
  - Cap rates for data center acquisitions are broadly in the 7s, with blended capital costs moving to the high 6s, creating positive investment spreads
  - The data center sector experienced a surge in external growth during the latter half of 2024 as cap rates and stocks improved, leading to heightened acquisition activity and robust deal pipelines for the year ahead
  - Private market players like Blackstone are all in; GP investments in data centers tripled in 2024 to $108b
- **Valuation**
  - Data center REITs trade at implied cap rates of around 6.3%
  - Data center REITs trade at ~31x 2025E FFO multiples
  - Stocks still trading at notable premiums to NAV

Sources: Company reports, Sugi Capital Management

Cell towers: slow go

Despite solid underlying business models and attractive valuations, sector sentiment is dampened by interest rate concerns and limited growth catalysts. Growth in carrier spending could offer some uplift later in the year, but ongoing issues like Sprint churn and currency risks continue to pose significant challenges

- **Market overview**
  - Although carrier capex is expected to grow for the first time since 2022, the increase is seen as incremental rather than a major inflection, likely benefiting the latter half of 2025 more significantly
  - Sprint-related churn continues to be a challenge in 2025, compounded by a strong US dollar impacting international revenues, particularly for AMT and SBAC which have significant foreign exposure
- **Leasing and occupancy**
  - Sprint churn will affect CCI with an anticipated 500 basis points of incremental churn. Despite these challenges, the fundamental demand for tower space driven by ongoing 5G rollout and other telecommunications needs offers some stability
  - Cell tower REITs are expanding into secondary and tertiary markets to find new revenue and mitigate risk, though these areas pose different challenges compared to prime locations
- **Investment market**
  - The longer-term investment outlook remains favorable due to the sector's resilient business model and low capital intensity, though near-term headwinds such as high churn and interest rate sensitivity persist.
  - CCI disappointed the market with the sale of its fiber business
  - Tower companies are well-positioned defensively, benefiting from weakening macroeconomic conditions. Their high negative correlation to the 10-year suggests they would thrive with lower rates
- **Valuation**
  - Tower REITs are trading at 17x 2025 AFFO
  - All three Tower REITs are trading below their five-year average AFFO multiples with AMT at 18.4x versus its five-year average of 23.0x, CCI at 13.8x versus 20.7x, and SBAC at 16.4x versus 23.7x



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Sources: BMO Research, Sugi Capital Management

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