REIT Preferreds: High Tax Advantaged Income in a Low Yielding Market

Executive Summary

- REIT preferreds offer attractive dividend yields relative to the broader fixed income universe
- Attractive tax advantages to REIT preferred dividends
- REIT preferreds have historically generated higher annualized returns than the broader preferred and fixed income markets
- REIT preferreds have historically provided consistent dividends over the long term, even during times of financial and economic stress
- REIT preferreds sit senior to REIT common from an income and capital value perspective
- Equity REIT preferreds have experienced what we view as minimal defaults over the past 20+ years

We believe REIT preferred securities can be viewed as an alternative income resource for investors.

November 30, 2020

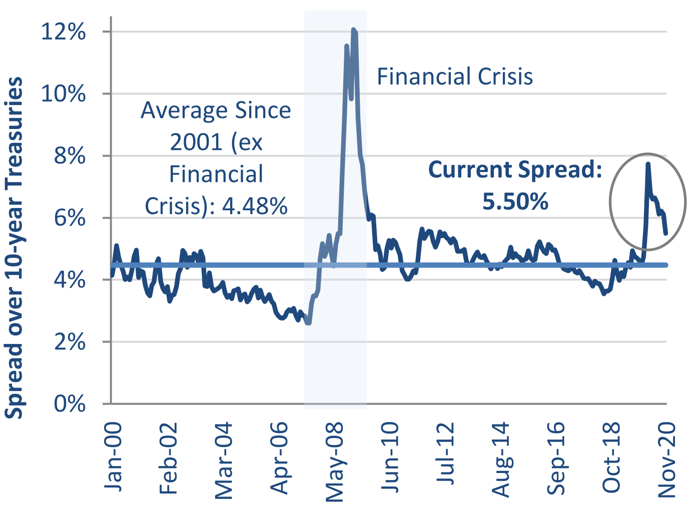
REIT Preferreds: High Tax Advantaged Income in a Low Yielding Market

LDR CAPITAL MANAGEMENT

The REIT preferred asset class currently offers attractive tax advantaged dividend yields in a low yielding market. REIT preferreds have historically paid sustained dividends over the long term, even throughout economic and financial crises. As a result, the asset class has historically produced higher annualized returns than the broader preferred and fixed income market. Further, during the current COVID-19 pandemic, the vast majority of REIT preferreds have continued to pay their quarterly distributions, and in our view, have a healthy cushion to spare. Given this asset class's long history of strong credit quality and sustained dividends, ***we believe REIT preferred securities can be viewed as an attractive alternative income resource for investors.***

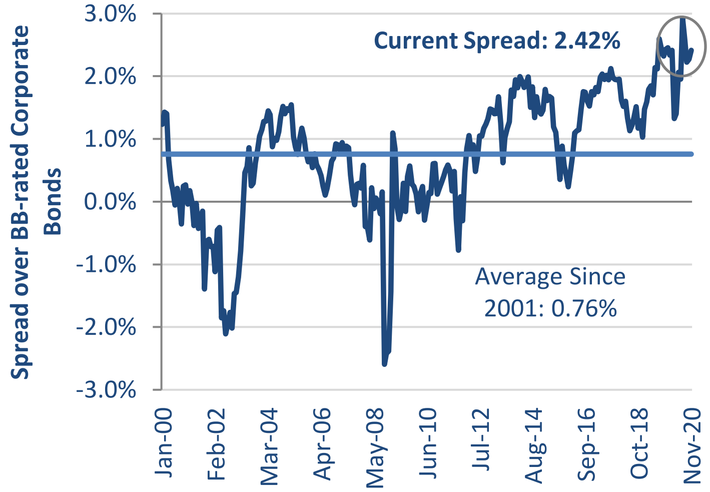
We additionally believe the REIT asset class currently offers investors an opportunistic entry point. With 10-year Treasury yields now standing at just 0.84%, inflation-adjusted real rates of return in many fixed income classes have dropped into negative territory. In contrast, REIT preferred securities still offer a weighted average current yield of 6.34%, which we view as a substantial 550 basis points yield premium over 10-year Treasuries[1]. This credit spread is 102 basis points wide over historical averages (excluding the 2008 financial crisis). We also note that REIT preferred yields stand a wide 242 basis points above BB-rated corporate bonds, 166 basis points above historical averages. We finally note that 62% of REIT preferreds still trade at or below par value, thereby presenting an opportunistic entry point to investors[2].

REIT Preferred Dividend Yield Spread over the 10-Year Treasury at Wide Levels



Source: Wells Fargo Hybrid & Preferred Securities REIT Index. Bloomberg as of 11/30/2020.

REIT Preferred Dividend Yield Spread over BB-rated Corporate Bonds



Source: BB-rated corporate bonds represented by ICE BofA BB US High Yield Index Option-Adjusted Spread. Bloomberg as of 11/30/2020.

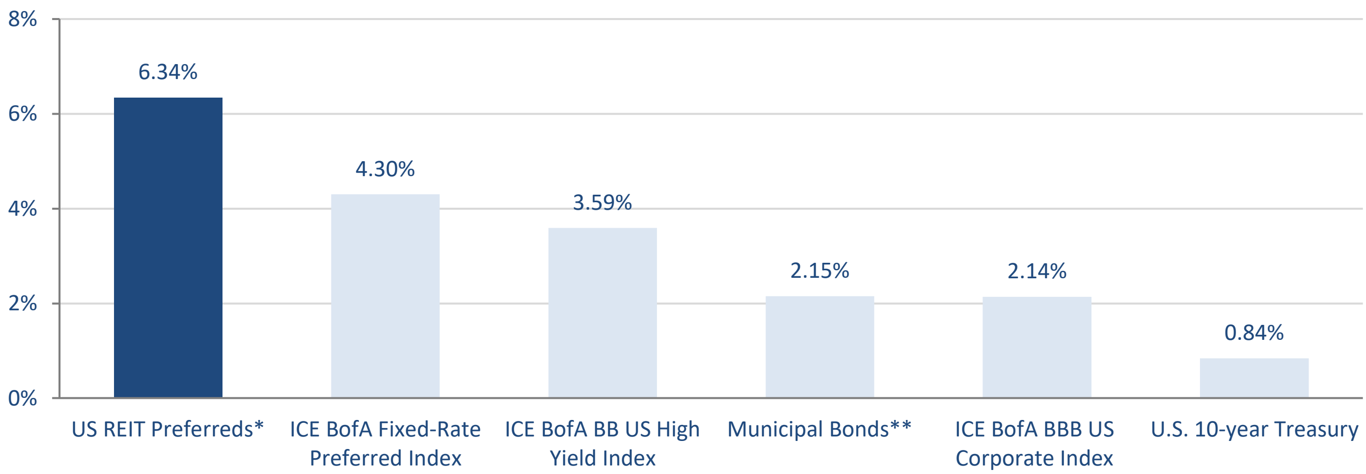
[1] Wells Fargo Hybrid & Preferred Securities REIT Index. Bloomberg as of 11/30/2020.
[2] Based on price less accrued dividend as of 11/30/3030. LDR Capital Management proprietary database.

ADVANTAGES OF REIT PREFERRED SECURITIES:

Attractive Relative Value vs. Broader Fixed Income Universe

REIT preferreds offer attractive alternative income in an income-starved marketplace. REIT preferred weighted average current dividend yields now stand at 6.34%[3]. This dividend yield compares quite favorably to Treasury bonds, investment grade corporate bonds, municipal bonds – and even high yield corporate bonds.

REIT Preferreds Currently Offer High Yield Among Domestic Fixed Income Asset Classes



*US REIT preferred universe based on Wells Fargo Hybrid & Preferred Securities REIT Index.
**Municipal bonds based on iShares National Municipal Bond ETF (MUB).
Source: Bloomberg as of 11/30/2020.

Attractive Tax Advantages

The Tax Cuts and Jobs Act of 2017 created a new tax exclusion for REIT dividends. Section 199A offers investors up to a 20% tax exclusion on Qualified Business Income (QBI) for those real estate pass-through entities (including REITs) that meet certain requirements. As such, only 80% of the ordinary income from REIT preferred dividends is now subject to taxation. In addition to the Section 199A exclusion, a component of REIT preferred dividends is often characterized as capital gains distributions and/or return of capital, also offering potential tax advantages to investors. All in all, 100% of REIT dividends now contain some sort of potential tax advantage to investors.

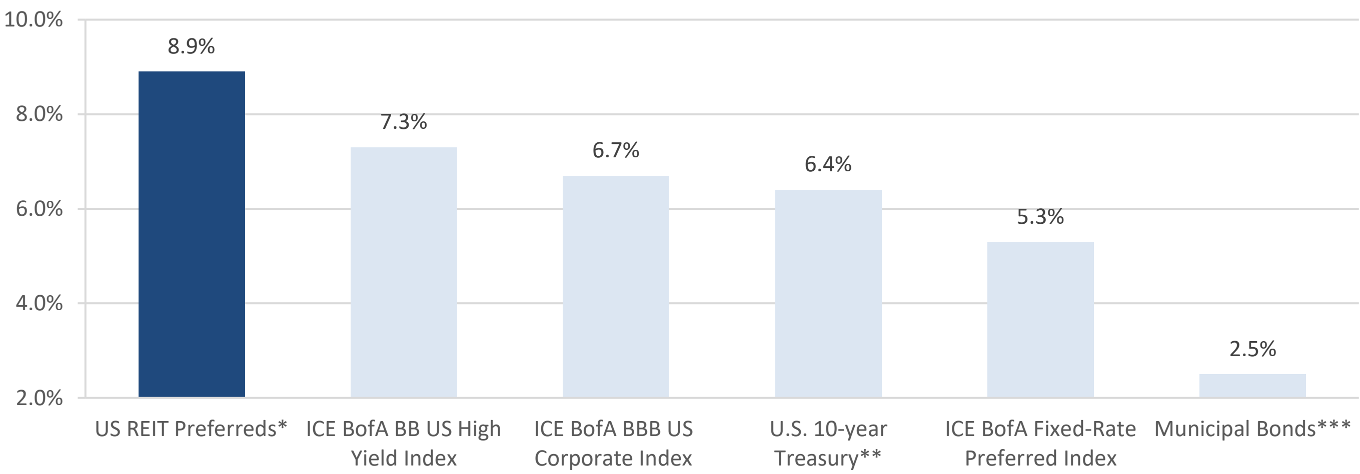
[3] Proprietary database (LDR Capital Management) as of 11/30/2020.

Long-Term Returns Historically in Excess of Corporate Preferreds and Other Segments of Fixed Income Market

Historically, REIT preferreds have generated long term total returns in excess of broader corporate preferreds and other segments of fixed income markets. Specifically, the REIT preferred asset class has generated annualized returns of 8.9% since January 1st, 2000. This performance has far outpaced the broader corporate preferred market, which returned 5.3% per annum over that same time period. We also calculate that REIT preferreds have generated excess returns over investment grade and high yield cooperate bonds over the same time period.

REIT Preferreds Have Generated Solid Relative Returns Over the Past 20 Years

Annualized return since 1/1/2000 to 11/30/2020



Source: Bloomberg as of 11/30/2020.
*US REIT preferred universe based on Wells Fargo Hybrid & Preferred Securities REIT Index.
**U.S. 10-year Treasury based on iShares 20+ Year Treasury Bond ETF, which has an inception date of 7/22/2002.
***Municipal bonds based on iShares National Municipal Bond ETF (MUB), which has an inception date of 9/7/2007.
Past performance is not indicative of future results. See attached Disclaimers and Disclosures regarding indexes.

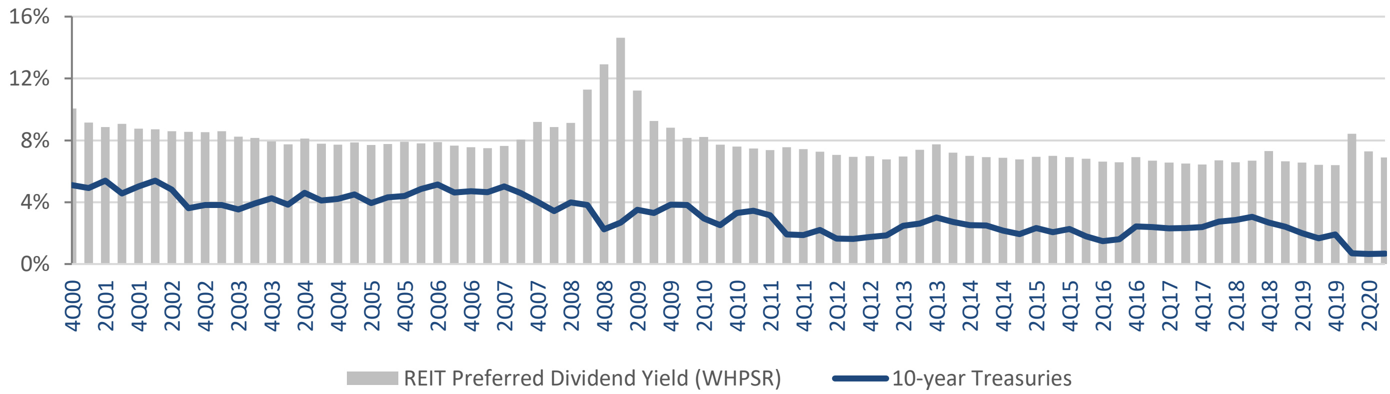
Consistent Dividends

The REIT preferred asset class has provided generally consistent distributions over its 20+ year history. These income distributions have historically held up relatively well during times of financial and economic stress. For example, during the global financial crisis from 2007-2009, we calculate that distribution levels for REIT preferreds fell by just 9% while REIT common stock distributions fell by a more significant 37%[4]. Further, coming out of the global financial crisis, approximately 39% of the cumulative REIT preferreds that were suspended were eventually "cured."

[4] Represented by the FTSE NAREIT All REITs Index (FNAR). Annual dividend distribution calculated by using 12-month trailing dividend yield.

To date, over the course of the COVID-19 pandemic, REIT preferred distributions have held up better than in the financial crisis. Specifically, we count just 4 REITs that now carry suspended preferred dividends since the outset of the pandemic, as compared to the 81 REITs that have implemented downward revisions to their common stock dividends. We believe REIT preferred dividends have shown solid stability as the industry entered the COVID-19 pandemic with its strongest balance sheet standing in a decade. According to J.P. Morgan Research, median net debt / LTM EBITDA levels at year-end 2019 were approximately 6.4x and debt service levels were at a high of approximately 4.5x[5]. These leverage levels should continue to enable REIT preferreds to largely withstand the current COVID-19 pandemic, in our view.

REIT Preferreds Provide Consistently Wide Dividend Yields Over 10-Year Treasuries

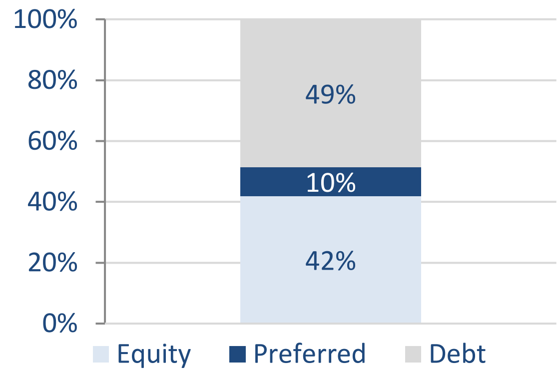


Source: Wells Fargo Hybrid and Preferred Securities REIT Index as of 3Q 2020.

Seniority in REIT Capital Stack

Preferred shares sit senior to common shares in the capital stack. That means all preferreds carry priority over underlying common equity from both an income perspective as well as capital value perspective. As such, REIT preferred capital values must be repaid in full before common shareholders receive any liquidating distributions. As seen to the right, we calculate that as of the end of the third quarter of 2020, REIT preferreds sat atop a healthy 42% equity cushion (calculated on cost-basis of real estate, not market value), which we believe offers stability to REIT preferred dividend levels and capital values.

REIT Preferreds Sit Atop a Healthy Equity Cushion



Source: *Proprietary database (LDR Capital Management). As of Q3 2020 (latest data available). REIT capital stack composition for equity REIT issuers only and calculated on cost basis of real estate.

[5] J.P. Morgan Commercial Real Estate Update September 2020.

Low Historic Default Levels

Underpinning the quality of REIT preferred dividends are a few main characteristics. From a structural perspective, REIT preferred dividends are cumulative in nature, and must be paid fully in cash before common shareholders receive any dividends. If not, any unpaid preferred dividends will be accounted for as a growing liability on a REIT's balance sheet. Preferred dividends can also be counted against REIT distribution requirements for tax purposes (REITs must pay out 90% of taxable income each year), and thereby help to fulfill an important corporate tax criteria. Lastly, cash strapped REITs are allowed to pay up to 90% of their common dividend in stock in lieu of cash, which provides additional support to preferred dividends during stressed time periods. For those reasons, many REIT management teams view their preferred shares as senior securities, and consider the preferred dividends as part of their recurring fixed charges

We calculate that equity REITs have experienced a historical cumulative credit loss of just 1.44% over the past 23-years (earliest data available). Separately, we calculate that mortgage REIT preferreds, which comprise approximately 17% of total REIT preferred issuances have experienced 11.41% in cumulative credit loss over the same period. Of note, one mortgage REIT issuer represents approximately 57% of total mortgage REIT credit loss. Even the mortgage REIT preferred area, aside from one issuer, has experienced relatively few credit issues. Taken in total, the REIT preferred asset class has historically experienced what we view as a small number of credit issues. In aggregate, we calculate the historical cumulative credit loss experienced by the entire REIT preferred asset class (including both equity REITs and mortgage REITs) to be just 3.09%, or just 12 basis points per annum of default loss.

	Historical Credit Loss of REIT Preferreds				
	Partial Credit Loss*		Total Credit Loss*		Cumulative*
	# of Issuers	Loss as a % of Total Par Value of Preferred Issued	# of Issuers	Loss as a % of Total Par Value of Preferred Issued	Loss as a % of Total Par Value of Preferred Issued
Equity REIT Preferreds	3	0.38%	5	1.06%	**1.44%**
Mortgage REIT Preferreds	2	0.88%	8	10.53%	**11.41%**
Total REIT Preferreds	5	0.46%	13	2.63%	**3.09%**

Source: Proprietary database (LDR Capital Management) as of 11/30/2020.
* Loss is calculated as the amount of the loss as a percentage of total par value of preferred issued.
Past performance is not indicative of future results. See Disclaimers and Disclosures for further information.

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LDR Database Definitions

LDR's calculations regarding REIT preferreds that are described in this letter are derived from its proprietary database of REIT preferreds, which is described in this paragraph. LDR seeks to track performance and various valuation metrics for all REIT publicly-traded preferreds issued in North America that are currently outstanding. This database does not include $1000-par preferreds, as they are not exchange listed. Otherwise, LDR believes that its database captures the universe of publicly-traded REIT preferreds in North America that are currently outstanding. However, the LDR proprietary database does not include historical data, so references to historical yields and returns prior to 11/30/20 are based on relevant indices as noted. Overall issuance data, where noted, includes U.S. and Canada-issued fixed-rate and convertible REIT preferreds. Yield data includes only U.S.-issued fixed-rate preferreds. All pricing and trading data for the database are derived from Bloomberg.

Use of Indices

Market index information shown herein is for illustrative purposes only and is included to show relative market performance and other metrics for the periods indicated. The indices presented herein are not representative of any LDR account and no such account will seek to replicate an index. Market participants cannot invest directly in an index, the index is not actively managed, not subject to management fees, broker commissions or other expenses, and investors should not rely on them as accurate means of comparison.

DISCLAIMERS AND DISCLOSURES CONTINUED

Index Definitions

Wells Fargo Hybrid and Preferred Securities REIT Index (WHPSR) tracks the performance of preferred securities issued in the US market by Real Estate Investment Trusts. The index is composed of preferred stock and securities that, in Wells Fargo's judgment, are functionally equivalent to preferred stock including, but not limited to, depositary preferred securities, perpetual subordinated debt and certain capital securities.

Bloomberg Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market.

FTSE Nareit All Equity REITs Total Return Index is a free-float adjusted, market capitalization-weighted index of U.S. equity REITs. Constituents of the index include all tax-qualified REITs with more than 50 percent of total assets in qualifying real estate assets other than mortgages secured by real property.

iShares 20+ Year Treasury Bond ETF seeks to track the investment results of an index composed of U.S. Treasury bonds with remaining maturities greater than twenty years.

iShares National Municipal Bond ETF (MUB) seeks to track the investment results of an index composed of investment-grade U.S. municipal bonds.

ICE BofA Fixed-Rate Preferred Index tracks the performance of fixed-rate USD-denominated preferred securities issued in the U.S. domestic market.

ICE BofA BBB US Corporate Index is a subset of the ICE BofA US Corporate Master Index tracking the performance of US dollar denominated investment grade rated corporate debt publicly issued in the US domestic market. This subset includes all securities with a given investment grade rating BBB.

ICE BofA BB US High Yield Index Option-Adjusted Spread represents the Option-Adjusted Spread (OAS) of the ICE BofA US Corporate BB Index, a subset of the ICE BofA US High Yield Master II Index tracking the performance of US dollar denominated below investment grade rated corporate debt publicly issued in the US domestic market. This subset includes all securities with a given investment grade rating BB.

Coronavirus and Other Global Health Events Risk

Epidemics, pandemics and other widespread public health problems could adversely affect the performance of REIT equity and preferred securities. For example, in late 2019, a novel virus started causing a disease ("COVID-19") with severe acute respiratory syndromes in humans, at times with serious health complications that sometimes result in death. What began as a local outbreak in Wuhan, China, spread globally over the course of weeks, stressing advanced healthcare systems of Western countries and resulting in financial disruptions to an extent that remains unclear. On March 11, 2020, the World Health Organization assessed that the outbreak can be characterized as a pandemic. Many countries imposed restrictions on travel and strict measures of social distancing.

As the potential impact on global markets from COVID-19, or future epidemics, pandemics or other health crises, is impossible to predict, the extent to which any such crisis may negatively affect the performance of specific securities or the duration of any potential business disruption is uncertain. Precautions or restrictions imposed by governmental authorities and public health departments related to this pandemic are expected to result in indeterminate periods of decreased economic activity throughout the U.S. and globally, including reduced or ceased business operations, decline in international trade and shortages of supplies, goods and services. An outbreak such as COVID-19, and the reactions to such an outbreak, are expected to cause uncertainty in the markets and businesses and are generally expected to adversely affect the performance of the U.S. and global economy, including due to market volatility, market and business uncertainty and closures, supply chain and travel interruptions, the need for employees to work at external locations and extensive medical absences among the workforce. As a reaction to such an outbreak, it is possible that governmental fiscal and economic measures will lead to an increase in spending and other forms of financial stimuli, and it is difficult to predict what effect such measures will have on the U.S. and global economies.

The impact that pandemics and other public health events will have on the performance of REIT equity and preferred securities, in particular, is uncertain, and it will depend to a large extent on future developments and new information that may emerge regarding the duration and severity of the coronavirus or other health crisis, and the actions taken by authorities and other entities to contain such crisis or treat its impact, all of which are beyond the LDR Capital Management's control.