COHEN & STEERS
REAL ASSETS. REAL RETURNS.

Building Better Portfolios with Listed Real Assets

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We believe liquid real assets—including real estate securities, commodities, natural resource equities and listed infrastructure—offer an attractive way to enhance diversification, particularly as the market pivots away from quantitative easing and low interest rates to a policy-induced reflationary environment.

Summary

What's real is real. Tangible real assets have been an increasing focus for investors looking to diversify beyond traditional equities and fixed income. However, there is often a misconception that private, illiquid investments are the only "real" way to allocate to real assets. Not only does this often leave smaller investors underallocated due to the challenges of implementing private-market strategies, but even larger investors often struggle to implement a well-diversified real assets program and therefore miss out on some of the most compelling characteristics of the asset class.

Ease of access. Listed markets can reduce barriers to access so significantly that investors of any size can establish a broadly diversified real assets allocation—diversified globally and by real asset category. Diversifying in this way may help to balance the inherent tradeoffs of individual real asset categories and has historically offered attractive full-cycle returns, diversifying performance patterns and positive sensitivity to unexpected inflation.

Benefits of the blend. Individually, each of the above attributes has merit, but together they can offer tremendous utility to investors that are concentrated in traditional equities and fixed income, helping to maintain or potentially enhance portfolio returns while reducing risk.

Prospective Advantages of Listed Real Assets

- Similar historical investment attributes as privately held real assets
- Access to a large investment universe distinct from global equities
- Potential for a globally diversified portfolio of real assets across multiple categories
- Small investment minimums
- Daily pricing and liquidity
- Transparency into the underlying assets
- No lock-up periods
- Generally lower fees than private real assets

A New Era of Diversification

There was a time when a balanced mix of global equities and fixed income was generally sufficient to achieve attractive, stable returns over the long run. This success has been supported in large part by the secular bull market in bonds that began in the 1980s. However, bonds now face an uphill climb amid low yields, rising global inflation and the prospect of higher interest rates. Equities may likewise struggle to deliver high levels of return against this backdrop, especially in light of the market's demanding valuations. In our view, these trends are likely to shape global financial markets for years to come, arguing for a broader approach to diversification.

Conditions for both stocks and bonds could become more challenging, increasing the appeal of an allocation to real assets.

In recent years, more investors have looked to solve this challenge by carving out a portion of their portfolio for real assets. History shows that an allocation to real assets can be an effective complement to equities and fixed income, helping investors to achieve their long-term goals.

What Are Listed Real Assets?

Real assets are the structures and raw materials that economies rely on to function and be productive. That includes the properties where we live, work and shop; the infrastructure that provides power and water and enables transportation and communications; and basic natural resources such as food and heating oil.

Direct investments in real assets typically require significant upfront capital and a commitment to keep the money tied up for an extended period. For many investors, a more convenient way to access real assets is through products that invest in public equities and futures that capture the underlying economics of real asset industries, providing similar exposure as direct investments but with the added benefits of liquidity and daily pricing.

Because listed instruments offer underlying liquidity, we believe they are a natural match to liquid, daily traded investment vehicles, avoiding the pitfalls seen in the open-end property fund market, where many popular funds have "gated" in times of market stress to prevent forced selling.

At Cohen & Steers, our focus is on what we call the Core Four Real Assets, which share common characteristics but represent distinct markets with different risk and return drivers.

The Core Four Real Assets

Real Estate Securities	Commodities Futures	Natural Resource Equities	Listed Infrastructure
Offices, shopping centres, self-storage, apartments, industrial warehouses, medical facilities, hotels, data centres, student housing	Crude oil, natural gas, heating oil, petrol, gold, silver, copper, aluminium, zinc, wheat, corn, soybeans, sugar, cotton, coffee, cocoa, livestock	Companies that own agribusiness, energy and metals & mining businesses	Electric utilities, airports, toll roads, railways, midstream energy, cell towers, marine ports, water, gas distribution

Please see back page for additional disclosures.

Investment Characteristics

In framing the discussion of real assets and their investment attributes, we emphasise three key criteria for a long-term allocation:

1. **Attractive return potential** over full market cycles may improve risk-adjusted portfolio returns without sacrificing the potential for equity-like returns over time.
2. **Diversification potential** from distinct performance drivers generally results in differentiated behaviours from broad equities and fixed income.
3. **Positive inflation sensitivity** to protect against the potentially damaging effects of accelerating inflation on a portfolio concentrated in stocks and bonds.

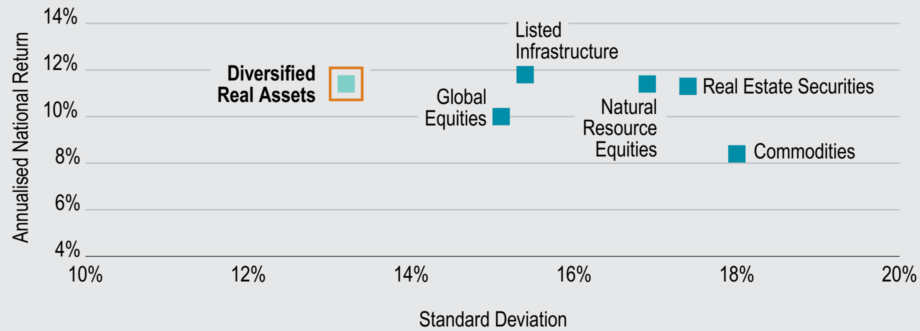
Total Returns

A balanced combination of key real asset classes generated better returns than equities, but with significantly lower volatility.

Real assets have historically generated strong returns across full market or economic cycles, with three of the four categories outperforming global equities since 1973, and commodities putting in solid returns as well (Exhibit 1). Individual categories of real assets also had somewhat higher volatility than global equities—but, with the exception of commodities, ultimately achieved higher risk-adjusted performance. Crucially, though, when combined together, an equal blend of real assets generated superior returns over time relative to global equities but with far less volatility, reflecting low intercorrelations within and across the sub-categories of real assets.

Exhibit 1: Risk-Return Profiles

1973–2017, in GBP



	Global Equities	Real Estate Securities	Commodities	Natural Resource Equities	Listed Infrastructure	Diversified Real Assets
Nominal Return (Annualised)	10.0%	11.3%	8.4%	11.4%	11.8%	11.4%
Real Return (Annualised)	4.0%	5.3%	2.5%	5.4%	5.8%	5.3%
Risk (% standard deviation)	15.1%	17.4%	18.0%	16.9%	15.4%	13.2%
Sharpe Ratio (Nominal)	0.26	0.31	0.16	0.32	0.36	0.37

At 31 December 2017. Source: Bloomberg, Dow Jones, FTSE, S&P, St. Louis Fed, Thomson Reuters Datastream and Cohen & Steers. See back page for index definitions and additional disclosures.

Diversification

The distinct performance drivers of real assets have historically resulted in diversifying correlations—both with each other and with stocks and bonds, as shown by the correlation matrix in Exhibit 2.

Exhibit 2: 20-Year Correlation Matrix
1998–2017, in GBP unhedged

	MSCI World	Global Aggregate Bonds	7–10 Year U.K. Gilts	Global High Yield Bonds	Real Estate	Commodities	Natural Resource Equities	Listed Infrastructure	Diversified Real Assets
MSCI World	**1.00**								
Global Aggregate Bonds	0.24	**1.00**							
7–10 Year U.K. Gilts	-0.10	0.58	**1.00**						
Global High Yield Bonds	0.71	0.49	0.06	**1.00**					
Real Estate	0.75	0.28	0.06	0.68	**1.00**				
Commodities	0.34	0.21	-0.07	0.37	0.32	**1.00**			
Natural Resource Equities	0.72	0.13	-0.19	0.52	0.57	0.61	**1.00**		
Listed Infrastructure	0.68	0.36	0.06	0.64	0.63	0.37	0.59	**1.00**	
Diversified Real Assets	0.79	0.30	-0.05	0.69	0.80	0.71	0.88	0.80	**1.00**

Real Assets

At 31 December 2017. Source: Morningstar.

Data quoted represents past performance, which is no guarantee of future results. Diversified Real Assets is an equal blend of the other four real asset classes in the exhibit. Correlation measures how closely two data series move in relation to one another, with 1 indicating perfect unison and -1 indicating perfect opposition. See back page for index definitions and additional disclosures.

Real assets have historically had diversifying correlations.

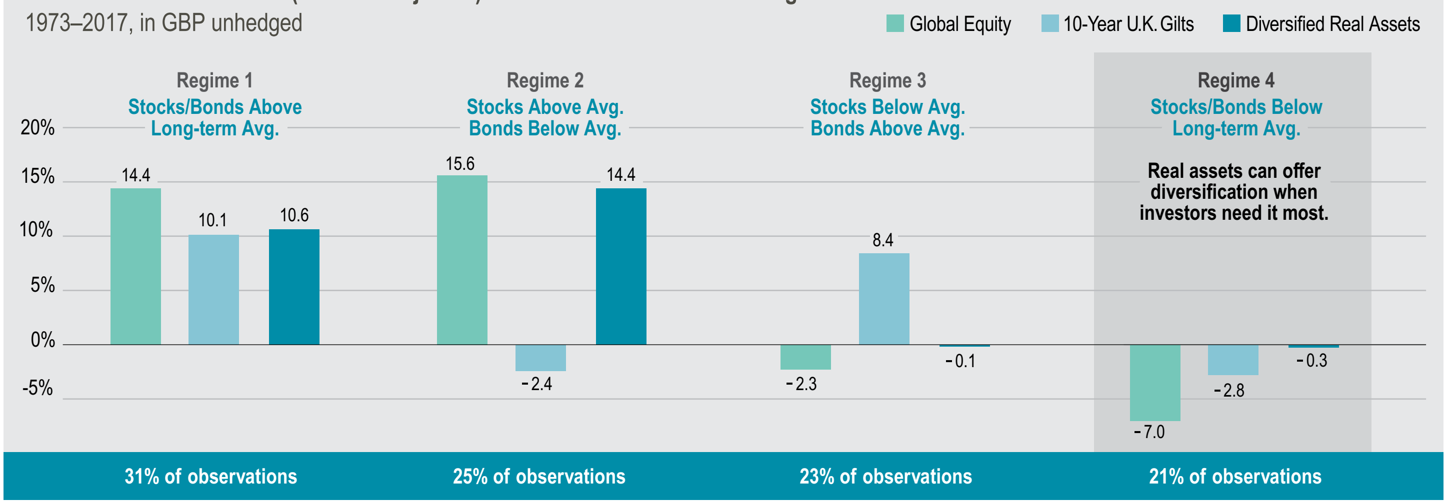
However, correlation only measures the average relationship over an arbitrary period of time, and therefore offers little insight into different market regimes. We believe that real assets' attractive long-term risk-adjusted returns partly reflects its tendency to be more correlated with other classes during generally favourable investment periods, and less correlated in difficult environments. Specifically, we believe investors that are concentrated in traditional equities and fixed income can most benefit from asset classes that may perform well in challenging periods when both equity and fixed income markets deliver below-average returns at the same time.

Historically, joint or simultaneous underperformance by stocks and bonds has happened relatively often. Going back to 1973, representing the longest period of common available history in our database, such periods occurred in 21% of rolling one-year periods (Exhibit 3 on the next page). Real assets have been relatively more resilient in such times, outperforming bonds and global equities. We believe this indicates the potential for real assets to provide an important buffer during one of the more challenging market conditions for most portfolios, while still offering solid return potential in more favourable times.

Inflation Sensitivity

While it remains a common misconception, listed real assets have not been dependent on significant 1970s-style inflation shocks to generate attractive full-cycle returns. As indicated in Exhibit 1 on page 3, real assets as a group delivered significantly greater annualised real (inflation-adjusted) returns than equities over a multi-decade span. While this period saw elevated inflation in the early years, for the most part inflation was relatively benign. However, if there is one common factor for real assets, it is their sensitivity to inflation surprises, making them potentially valuable in helping to protect a portfolio's future purchasing power.

Exhibit 3: Annualised Real (Inflation-Adjusted) Returns in Different Market Regimes
1973–2017, in GBP unhedged



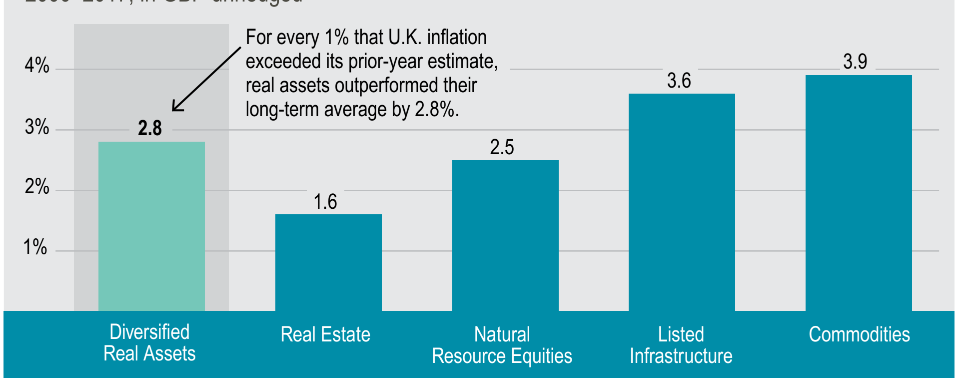
At 31 December 2017. Source: Bloomberg, Dow Jones, FTSE, S&P, St. Louis Fed, Thomson Reuters Datastream and Cohen & Steers. Based on monthly observations of rolling 12-month real returns of the MSCI World Index and Constant Maturity 10-year U.K. Gilts, adjusted for inflation using the U.K. Retail Price Index. Returns in each quadrant represent periods of over/underperformance by global equities and bonds relative to their respective long-term averages of 4.3% and 3.3%. See back page for index definitions.

History shows that the impact of inflation tends to be most damaging to stocks and bonds when it is unexpected. Our analysis suggests that real assets tend to experience strong returns precisely during those periods, when realised inflation exceeds prior expectations.

Exhibit 4 shows the impact of unexpected inflation using a metric we call “inflation beta.” Inflation beta measures the sensitivity of returns to a 1% upside surprise in realised inflation relative to the inflation estimate from a year before. For example, an asset class with a positive inflation beta should generally react favourably to inflation surprises.

The results below show that a diversified real assets blend historically outperformed its long-term average by 2.8% for every 1% that inflation exceeded its prior-year estimate. We believe this is a strong indicator that real assets can serve as an effective inflation hedge without being dependent on inflation to produce strong returns.

Exhibit 4: Sensitivity to Unexpected Inflation
2000–2017, in GBP unhedged



At 31 December 2017. Source: Bank of England, Bloomberg, Dow Jones, FTSE, S&P, St. Louis Fed, Thomson Reuters Datastream and Cohen & Steers. Annualised nominal. See back page for index definitions and additional disclosures.

Real asset classes have inherent inflation-sensitive features.

The reasons for the inflation sensitivity of real assets stem from their distinct economics:

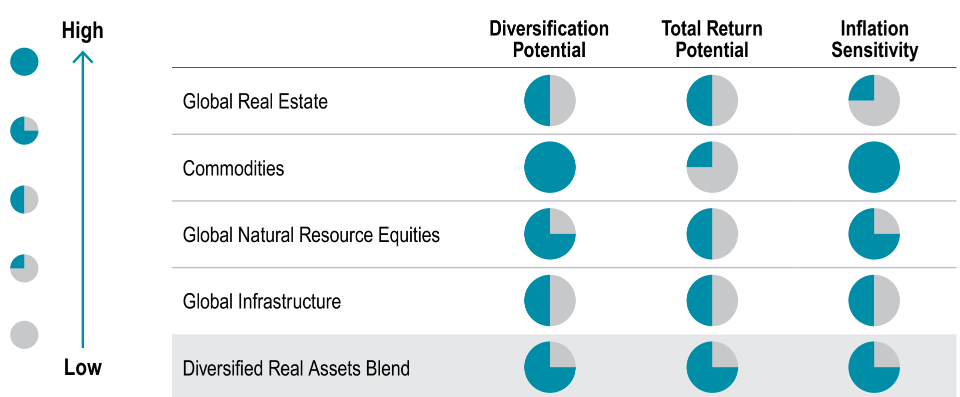
- **Commodities** are often direct inputs to inflation measures and generally respond to the same forces that drive prices for other goods higher, including supply constraints and stronger demand from increased economic activity.
- **Natural resource producers** tend to benefit from higher prices for raw materials, leading to potentially higher profits on their capital base.
- **Real estate owners** may benefit from higher inflation due to their ability to raise rents, increasing the value of their property. Higher inflation can also reduce the incentive for new construction due to higher costs for labour, land, materials and financing.
- **Infrastructure** cash flows and asset values may have direct or indirect links to inflation, such as rate escalators tied to inflation measures often seen in utilities and toll roads. Long-term economic growth may also drive higher throughput for infrastructure assets.

Benefits of a Diversified Real Assets Blend

Investors have generally targeted just one or two categories of real assets—most commonly, real estate and infrastructure. Historically, however, no one type of real asset has excelled equally across all three criteria of diversification, total returns and inflation sensitivity. Each has had periods of success and disappointment in one aspect or another. Only by combining them into a coherent and properly managed investment framework do we believe that investors can effectively navigate those tradeoffs (Exhibit 5).

A diversified blend of real assets may help investors navigate the tradeoffs of standalone categories, potentially delivering better results over the long run.

Exhibit 5: How Different Real Assets Have Met Our Criteria



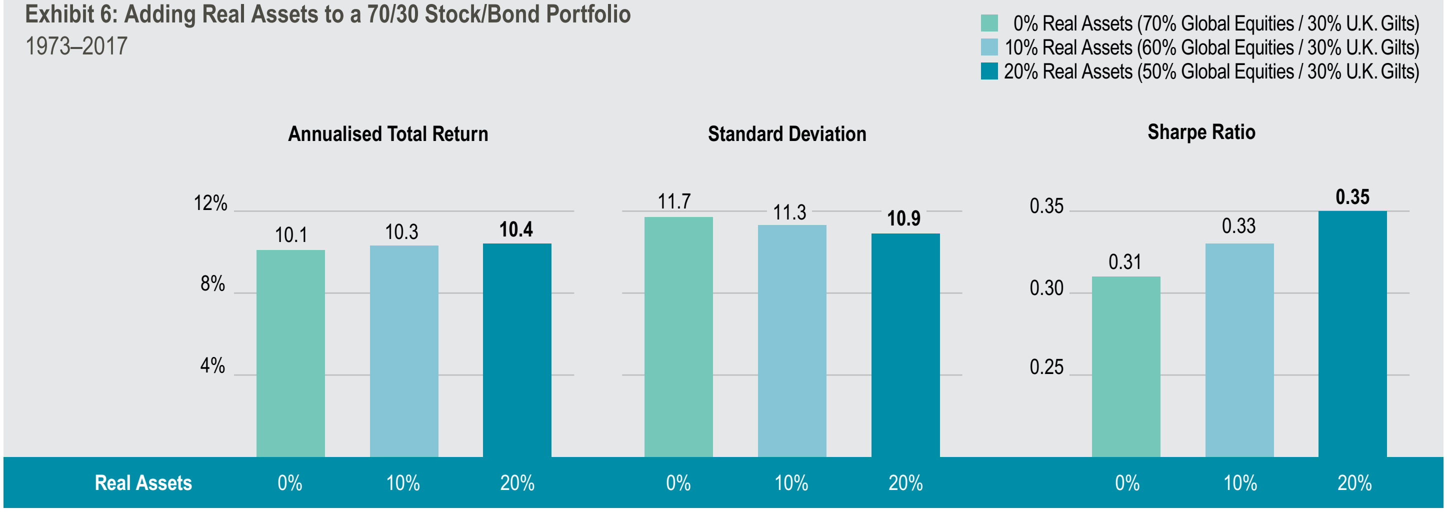
At 31 December 2017. Source: Cohen & Steers.
See back page for index definitions and additional disclosures.

Our research suggests that the potential for a more consistent experience and lower volatility offered by a diversified real assets portfolio can be an important factor in the long-term success of a real assets allocation. This approach also affords active managers the opportunity to add value through dynamic asset allocation, providing an additional means of enhancing return potential.

Portfolio Perspective

If the past is any indication, listed real assets may help to enhance a portfolio's risk-return potential. Historically, adding 10–20% of a diversified equal-weighted real assets blend to a 70/30 portfolio of global equities and U.K. Gilts would have produced stronger returns with lower volatility, resulting in higher risk-adjusted performance as measured by the Sharpe ratio (Exhibit 6).

Exhibit 6: Adding Real Assets to a 70/30 Stock/Bond Portfolio
1973–2017



At 31 December 2017. Source: Bloomberg and Cohen & Steers.

Data quoted represents past performance, which is no guarantee of future results. See back page for index definitions and additional disclosures.

Economic Backdrop Shifting in Favour of Real Assets

Many investors have come to rely on asset allocations modelled on the old economic order: decades of globalisation, falling inflation, slowing economic growth and declining interest rates. We believe the old order is transitioning and that the global macro environment may now be moving in favour of real assets.

Economic growth, employment and inflation readings are on the rise and could accelerate in the wake of U.S. tax cuts and a more active mindset by policymakers globally. After a long period of unexpectedly low inflation—during which certain real assets have broadly underperformed—the transition to a new market regime of higher inflation risk represents a potential multiyear tailwind for real assets.

This turning point comes at a critical juncture for investors. Whether they choose to target a specific asset class or a multi-strategy solution, we believe real assets are likely to play a vital role in anchoring the potential for attractive risk-adjusted returns in the years ahead. To continue the discussion on how real assets may play a role in your investment strategies, please contact your Cohen & Steers representative.

Index Representations. *Unless noted otherwise, all returns and investment characteristics discussed in this report are based on the indexes below.* Global Equity: MSCI World Index; Global Bonds: Barclays Capital Global Aggregate Bond Index; 7-10 Year U.K. Gilts: Subset of the ICE BofAML U.K. Gilt Index; Global High Yield Bonds: Barclays Capital Global High Yield Index; Real Estate: FTSE NAREIT Equity REIT Index through February 2005 and FTSE EPRA/NAREIT Developed Index thereafter; Commodities: S&P GSCI through July 1998 and Bloomberg Commodity Total Return Index thereafter. Natural Resource Equities: 50/50 Blend of Datastream World Oil & Gas and Datastream World Basic Materials through May 2008 and S&P Global Natural Resources Index thereafter; Infrastructure: 50/50 Blend of Datastream World Pipelines and Datastream World Gas, Water & Multi-Utilities through July 2008 and Dow Jones Brookfield Global Infrastructure Index thereafter. Diversified Real Assets Blend: Equal-weighted blend of real estate, commodities, natural resource equities and infrastructure.

Index Definitions. *An investor cannot invest directly in an index and index performance does not reflect the deduction of any fees, expenses or taxes.* MSCI World Index is a free-float-adjusted index that measures performance of large- and mid-capitalisation companies representing developed market countries. Barclays Capital Global Aggregate Bond Index is a broad-market measure of global investment-grade debt from many different currencies. ICE BofAML U.K. Gilt Index includes all securities with a remaining term to final maturity greater than or equal to 7 years and less than 10 years. Barclays Capital Global High Yield Index covers the universe of fixed rate, non-investment grade debt. Credit Suisse Hedge Fund Index measures performance of a group of hedge funds identified by Credit Suisse according to a proprietary methodology. Credit Suisse Long/Short Equity Hedge Fund Index is an asset weighted index that measures performance of a group of long/short hedge funds identified by Credit Suisse according to a proprietary methodology. The FTSE EPRA/NAREIT Developed Real Estate Index (net) is an unmanaged market-weighted total return index which consists of many companies from developed markets who derive more than half of their revenue from property-related activities. The FTSE NAREIT Equity REIT Index is an unmanaged, market-capitalisation-weighted index of all publicly traded U.S. REITs that invest predominantly in the equity ownership of real estate, not including timber or infrastructure. The Bloomberg Commodity Total Return Index, formerly known as the Dow Jones-UBS Commodity Index, is a broadly diversified index composed of commodities traded on U.S. exchanges, with the exception of aluminium, nickel and zinc, which trade on the London Metals Exchange. The Datastream World Index Series encompasses global indexes of companies in their respective sectors (Gas, Water & Multi-Utilities; Materials; Oil & Gas; and Pipelines) compiled by Thomson Reuters Datastream. 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 S&P Global Natural Resource Equities 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 is a composite index of commodity sector returns representing an unleveraged, long-only investment in commodity futures that is broadly diversified across the spectrum of commodities.

About Cohen & Steers

Cohen & Steers is a global investment manager specialising in liquid real assets, including real estate securities, listed infrastructure, commodities and natural resource equities, as well as preferred securities and other income solutions. Founded in 1986, the firm is headquartered in New York City, with offices in London, Hong Kong, Tokyo and Seattle.

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