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BLUEROCK 2020 VISION

Market & Industry Outlook

Key Themes for 2020 and Beyond:

- Individual investors, in their quest to invest properly for retirement, will increasingly join institutional investors in seeking appropriate alternative assets to build more efficient portfolios with higher risk-adjusted returns and lower volatility than is possible with the traditional 60%/40% stock/bond portfolio.
- The U.S. is an attractive investment destination relative to other developed world economies.
- U.S. institutional real estate is attractively valued vs. domestic stocks and bonds.
- The multifamily and industrial real estate sectors, driven by household formation and the expansion of e-commerce and consumer expectations of shorter delivery times, respectively, should continue to outperform the overall real estate market.
- Credit markets are attractive investments in a maturing investment landscape.
- Next generation investment solutions must balance appropriate risk-adjusted returns, income, access to traditionally institutional asset classes, prudent fee structures, and liquidity.

2019 was an exceptional year for stocks and bonds, however, lofty valuations can leave individual investors feeling uneasy about future prospects. U.S. Treasury bond yields spent much of 2019 under the 2% rate threshold, roughly equivalent or slightly below the current inflation rate. Stock valuations are approaching historical peaks by many measures including price/earnings ratios, cyclically adjusted price/earnings ratios, and the total stock market capitalization/GDP ratio. We believe it is prudent for individual investors - given these valuations, combined with a history of high volatility and large drawdowns - to seek alternative investments not correlated to the broader markets while providing higher income and lower volatility.

While the global economic backdrop has been defined by uncertainty and slow growth, the U.S. economy continues to post strong job and wage growth. In some sense, the U.S. has benefitted from the slow growth of other developed nations as their central banks have been active in pushing interest rates to new lows. Near zero and negative interest rates make Treasury yields attractive by comparison, fueling stronger economic growth and higher asset prices. While other developed nations struggle with aging demographics and population stagnation, the U.S. economy exhibits positive demographic forces led by the Millennial generation, the largest cohort in U.S. history. This generation has helped create the longest economic expansion in the nation's history. Due to the tempered nature of the growth rate and continued positive demographic trends, we expect this expansion to continue.

While many daily liquid investments reflect, in our opinion, rather high valuations, U.S. institutional real estate pricing remains attractive relative to its public REIT counterpart. Driven by rental rate increases reflecting strong aggregate demand and solid market fundamentals, real estate performed well throughout the past decade. However, many public REITs now trade at premiums to their underlying net asset values indicating that relative value can be found in select private equity real estate sectors.

With respect to private equity real estate, we have conviction that higher risk-adjusted returns will be best realized with active management capitalizing on economic forces, demographic trends, and changing consumer preferences, in order to capture and realize relative value.

Despite a sound overall market with historically low vacancy rates, not all real estate sectors warrant the same outlook. We continue to believe that the apartment and industrial sectors deserve a significant overweight in investors' real estate portfolios with corresponding underweights in the retail and office sectors. The growth of e-commerce and associated need for industrial space has spurred industrial returns to more than double the nearest other sector [1]. Household formation, particular among Millennials, continues to drive the apartment sector with higher rents. We see these as long-term secular trends that will provide tailwinds for the respective sectors for a long period to come, versus typical shorter-term cyclical considerations. We are also optimistic about emerging, non-traditional real estate sectors such as senior housing, medical office, self-storage, and life science properties due to fundamental shifts in technology, domestic industry, and demographics.

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As the investment landscape matures, we believe there are attractive opportunities in the credit markets for both real estate and corporate credit. Current treasury and investment grade bond yields offer little in the way of inflation protection and carry interest rate risk. We believe there are numerous opportunities in the credit markets which present a combination of attractive yields and senior positions in real estate and corporate capital stacks which can limit downside risk. Many of these types of investments are not available directly to individual investors due to large investment minimums and difficult to access structures. We anticipate that access to these institutional quality, income-oriented options in easy to invest structures will enable the prudent investor to build a more efficient portfolio, with higher risk-adjusted returns, and lower overall volatility than provided by traditional stock and bond investments.

Today's investors stand at a critical juncture. The majority of U.S. individual investors have moved beyond their growth stages of portfolio construction and into the capital preservation and income generation mode, emblematic of an aging investor base. At this same time, liquid, easily-accessible investments offer historic low yields, a history of high drawdowns, and historically high volatility. Guided by cautiousness, we believe investors will find it prudent to add well structured, transparent alternatives that seek to preserve capital, generate income, limit drawdowns, and offer resiliency through economic cycles. We look forward to being at the forefront of offering next generation solutions to meet the diverse needs of today's investors.

[1] NCREIF Property Index, a leading institutional private real estate index, as of Q3 2019

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