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RISING ALLOCATIONS TO REAL ESTATE

The U.S.-China trade war progresses at an unpredictable pace and the resultant global financial market volatility has made it increasingly difficult to navigate for investors and central bankers alike. With little expectation for a firm trade resolution any time soon, waning economic outlooks have set indicators flashing warnings of an impending recession. The U.S. 10-year and 2-year Treasury yield curve, widely considered a historically accurate predictor of downturns, has inverted with each escalation in trade tensions. A recent survey by the Bank of America Merrill Lynch found that a third of asset managers expect a global recession within the next 12 months, the highest probability the survey has seen since 2011. In fact, multiple countries are already showing signs of economic damage as a result of this prolonged trade war.

As investors pile into safe haven assets in response to these recession fears, bond yields have plunged to unprecedented levels worldwide. Yields have fallen so low that traditional investment paradigms are becoming reversed with investors seeking income returns from stock dividends and capital gains from rising bond prices. As well, the value of global negative-yielding debt has now risen to an estimated US$17 trillion, a record high that represents nearly a third of all global debt. Some analysts believe that this phenomenon is evidence of the "Japanification" of the world economy, bringing in an era of weak growth, deflation and ineffective monetary stimulus. However, a coordinated deployment of fiscal stimulus may still prevent this scenario from playing out as it did for Japan nearly 30 years ago.

In this current ultra-low yield environment, pension funds in particular are facing serious difficulties as returns fall and deficits grow. Pension funds have begun to trade in liquidity for higher returns and allocations to alternative assets such as private debt and direct real estate are on the rise. As recently highlighted by MSCI, over the last two decades, direct real estate as an asset class has appreciably matured and property type offerings have expanded and diversified. In Canada, pension fund allocations to real estate have steadily been on the rise and reached a record high of 12.8% in 2018 according to the Pension Investment Association of Canada. The historically stable income returns, diversification benefits, long-term liability matching and higher returns of direct real estate will continue to attract capital, especially so in today's volatile environment.

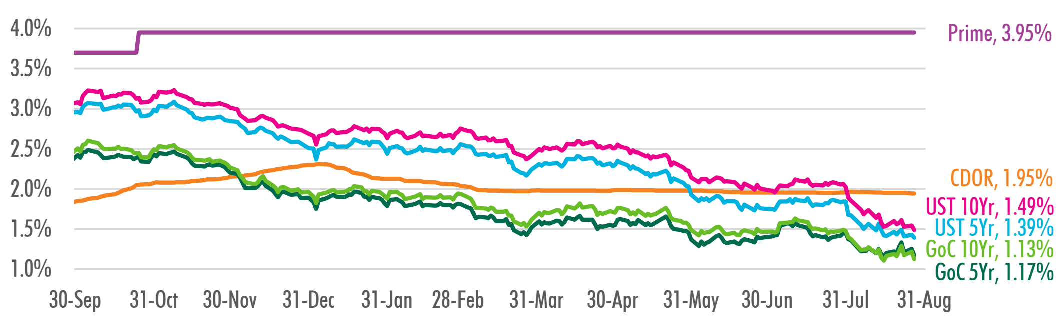
Key Indicator	Current	30 Days
5Yr Mortgage Spread	1.55-2.05%	
10Yr Mortgage Spread	1.70-2.30%	
5Yr Canada Housing Trust Spread	33 bps	1 bps
10Yr Canada Housing Trust Spread	43 bps	2 bps
USD/CAD	$0.7528	-0.90%
WTI Crude	US$54.93	-3.41%
S&P/TSX REIT Index	191.61	2.16%

Source: Thomson Reuters, August 27, 2019.

Economic Highlights:

- Employment fell by 24,200 jobs in July 2019 and the unemployment rate rose to 5.7%.
- Inflation in July 2019 held steady at 2.0%.
- Overall retail sales were flat in June 2019, however, retail sales excluding cars and gas rose by 1.7%.

Benchmark Yields



Source: Thomson Reuters, August 27, 2019.

ViewPoints:

- The Japanification Of Bond Markets
- Pension World Reels From 'Financial Vandalism' Of Falling Yields
- The Changing Face Of Real Estate Portfolios

Contact

MARC MEEHAN
Director, Canada Research
+1 647 943 4205
marc.meehan@cbre.com

EVAN LEE
Research Manager, Canada Research
+1 647 943 3654
evan.lee@cbre.com

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