American Assets Capital Advisers

A SPECIAL REAL ESTATE MARKET COMMENTARY

Buy the Dip

NOTEWORTHY BEHAVIOR IN THE REAL ESTATE SECURITIES MARKET, AND HOW TO POTENTIALLY BENEFIT

MARCH 15, 2021

AUTHORS

Burland East, CFA: PM and CEO

Creede Murphy: PM and COO

Evan Elig: Analyst

Madeline Reber: Analyst

THEMES

Market drawdowns, annual corrections

READ TIME

15 minutes

Corrections occur, even in bull markets. On a purely probabilistic basis, fewer than 20% of the broader equity market corrections turn into a full-blown bear market, creating opportunities to capitalize on the bounce-back. Thus, the odds are for a temporary correction.

Observations from Public Real Estate Markets

In the public real estate market (as measured by the Dow Jones US Real Estate Total Return Index ("index" or "DJUSRET")), corrections have occurred once per year, every year, for the last 29 years.

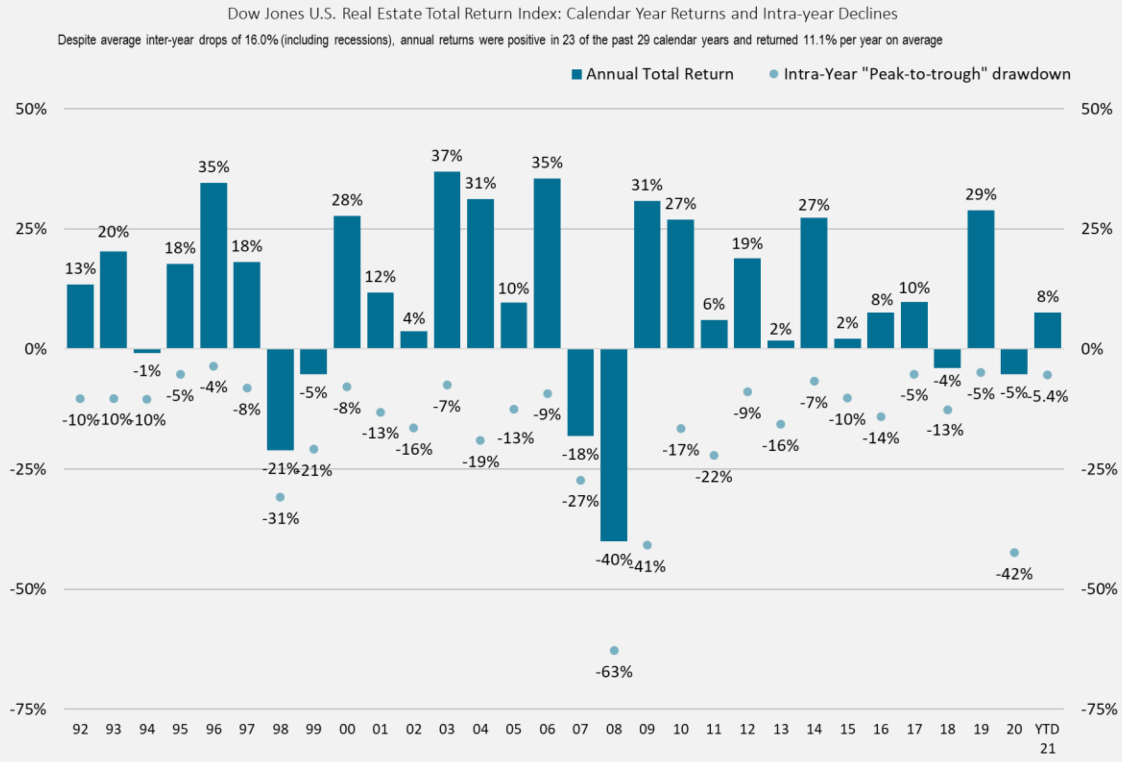
Even in years where the index's return was strongly positive or when the economy was growing, the market saw high single digit or even double-digit returns inclusive of the intra-year corrections *[Figure 1]*. It's almost like one's birthday; it comes around once a year, whether you want it to or not.

Figure 1

Dow Jones U.S. Real Estate Total Return Index: Calendar Year Returns and Intra-year Declines

January 2, 1992 – March 17, 2021

Despite average inter-year drops of -16.0% (including recessions), annual returns of the DJ US Real Estate Total Return Index were positive in 23 of the past 29 calendar years and returned +11.1% per year on average.



Source: S&P Dow Jones Indices, American Assets Capital Advisers ("AACA"). Past performance is not indicative of future results. There is no guarantee any investment will achieve its objectives, generate profits, or avoid losses.

A Recurring Theme: Annual Troughs and Performance

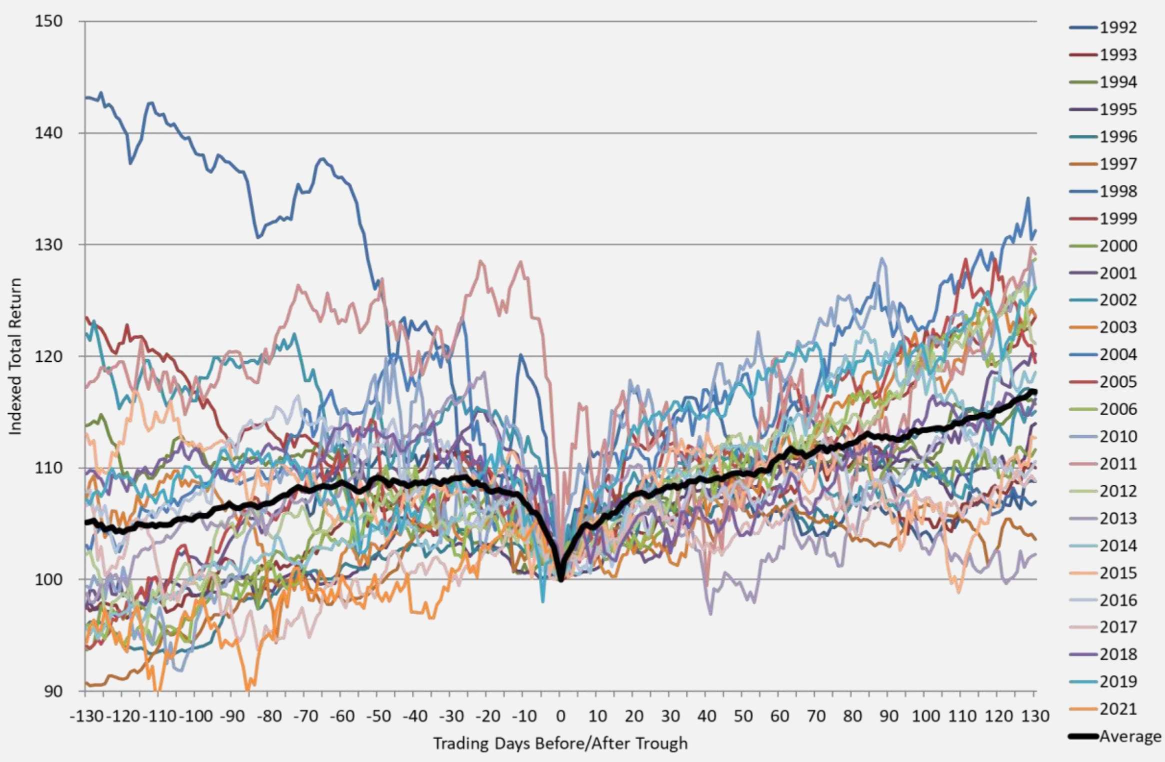
Corrections have been a yearly occurrence. To analyze this, we synchronized the annual troughs of the Dow Jones US Real Estate Total Return Index by lining up these troughs to a "Day 0" *[Figure 2]*. This helps to visualize any patterns that may exist both in the trading days preceding and following the bottom of a correction. Average performance over the time period is shown by the dark bolded line in *Figure 2*.

Figure 2

Dow Jones U.S. Real Estate Total Return Index Indexed to Annual Correction Trough

January 2, 1992 – March 17, 2021 (Excluding 2007, 2008, 2009, and 2020)

Annual corrections of the index have been synchronized (or "lined up") to a single theoretical point in time at each trough to more easily discern trends.



Source: S&P Dow Jones Indices, AACA. Past performance is not indicative of future results. There is no guarantee any investment will achieve its objectives, generate profits, or avoid losses.

This exercise revealed a few interesting stats of market behavior:

- 88% of the time after hitting an annual trough, the forward 130-day return never dropped below the prior trough.
- At 130 days after the annual trough, the index was higher in every instance.

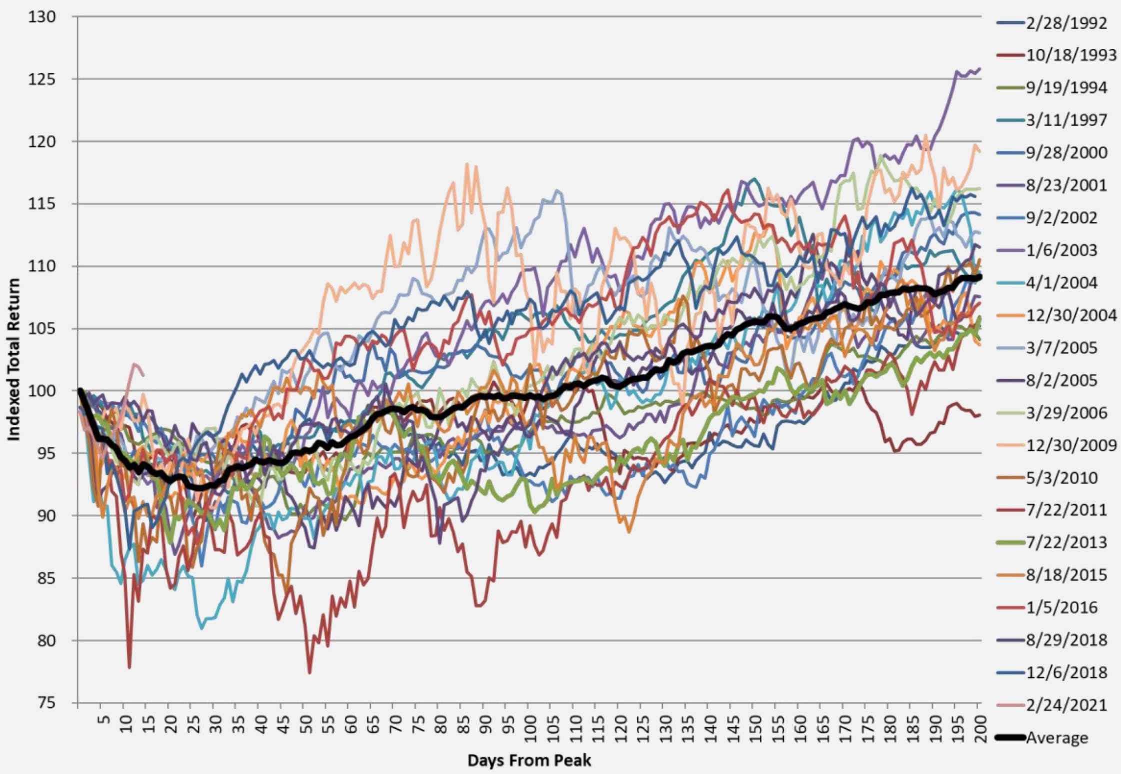
Figure 3 illustrates the performance path of the same DJUSRET but this time the annual peaks prior to annual troughs are synchronized. Furthermore, the performance of the following 200 trading days has been averaged to achieve a mean performance path, as noted by the dark bolded line.

Figure 3

What Typically Happens After a Sell-off?

Annual corrections of the Dow Jones US Real Estate Index | January 2, 1992 – March 17, 2021

Annual corrections have been synchronized to theoretical peak prior to the trough, showing the subsequent 200 trading days.



Source: S&P Dow Jones Indices, AACA. Past performance is not indicative of future results. There is no guarantee any investment will achieve its objectives, generate profits, or avoid losses.

While the performance path is theoretical and not indicative of future results, we believe it illustrates a consistent pattern:

- Corrections are sharper than recoveries; corrections, on average, last a bit over a month.
- Recoveries are more gradual, and (again, on average) typically take 3-4 months to completely exit the correction.
- Even if you had bought the DJUSRET at its annual peak and then experience the annual drawdown thereafter, your investment would, on average, have yielded positive returns at the 100-day mark.

An Opportunity During a Storm?

The preceding graphs have shown some repeated themes in historical corrections: they come often, occur quickly, but typically swing back and continue into positive territory.

The current COVID-19 correction is one of the few outliers in this situation. The US equities market fall on a level that was near unbelievable. However, even when the DJUSRET fell by 42.48% in March 2020, one year later it is only 6.52% below that original peak. So even if an investor entered the market right before one of the worst drawdowns in recent history, a positive yield would have been in reach just one year later.

As Warren Buffett described, “The stock market is a device for transferring money from the impatient to the patient.”

Risks and Other Important Considerations

This material is being provided for informational purposes only. The author's assessments do not constitute investment research and the views expressed are not intended to be and should not be relied upon as investment advice. This document and the statements contained herein do not constitute an invitation, recommendation, solicitation or offer to subscribe for, sell or purchase any securities, investments, products or services. The opinions are based on market conditions as of the date of writing and are subject to change without notice. No obligation is undertaken to update any information, data or material contained herein. The reader should not assume that all securities or sectors identified and discussed were or will be profitable.

Past performance is not indicative of future results. There is no guarantee that any forecasts made will come to pass. Due to various risks and uncertainties, actual events, results or performance may differ materially from those reflected or contemplated. There can be no assurance that any investment product or strategy will achieve its objectives, generate profits or avoid losses. Diversification does not ensure profit or protect against loss in a positive or declining market. It is important to note that all investments are subject to risks that affect their performance in different market cycles. Equity securities are subject to the risk of decline due to adverse company or industry news or general economic decline. Bonds are subject to risk of default, credit risk, and interest rate risk; when interest rates rise, bond prices fall. **Real Estate Investment Trusts ("REITs") are affected by the market conditions in the real estate sector, changes in property value, and interest rate risk.**

Alternative investments involve a high degree of risk and can be illiquid due to restrictions on transfer and lack of a secondary trading market. They can be highly leveraged, speculative and volatile, and an investor could lose all or a substantial amount of an investment. Alternative investments may lack transparency as to share price, valuation and portfolio holdings. Complex tax structures often result in delayed tax reporting. Compared to mutual funds, hedge funds, commodity pools and other vehicles such as separate accounts are subject to less regulation and often charge higher fees. Mutual funds involve risk including possible loss of principal. Alternative investment managers typically exercise broad investment discretion and may apply similar strategies across multiple investment vehicles, resulting in less diversification. Trading may occur outside the United States which may pose greater risks than trading on U.S. exchanges and in U.S. markets.