Invesco

QUARTERLY COMMENTARY

Invesco Global Real Estate Fund

As at June 30, 2023

Key takeaways

1 The fund underperformed its benchmark

The Portfolio underperformed its benchmark as defensive positioning was generally not rewarded during a period of higher investor confidence and risk taking. Sector allocation and stock selection among US REITs were the primary detractors due to shortfalls across industrial, manufactured housing and healthcare positioning.

2 The fund is defensively positioned

The Portfolio holds relatively cautious positioning, with modest exposure to cyclical real estate and a focus on sectors with more stable cashflows, above-average growth and below-average financial leverage. U.S. REITs and Japanese real estate are key regional overweight exposures. Industrial and health care are held overweight. Office and retail are underweight.

3 REITs continue to screen attractive

Capital market volatility is likely to continue, but REIT earnings show relative stability as slower economic conditions play out. Public real estate market valuations have largely reflected a higher interest rate environment, offering attractive pricing. Sustainable cash flow growth will likely be a key differentiator.

Investment objective

The Invesco Global Real Estate Fund seeks to generate a total return through capital growth and income by investing primarily in real estate securities from around the world.

Portfolio managers*

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*As of July 05, 2023, Chip McKinley is no longer part of the Invesco Listed Real Assets Team.

Manager perspective and outlook

- Volatility in capital markets is likely to continue with uncertainty over the path of inflation, interest rates and global economic growth. Opinions are widely dispersed regarding recession expectations. However, we believe that a period of slower or negative growth is inevitable as the lagged effect of interest rate increases on consumer and corporate profits impact risk appetite. Interest rates appear to be close to peaking, however, a change to falling interest rates is unlikely to be a near-term event
- The re-pricing process for private real estate assets in the new environment of higher interest rates will continue over coming months. We anticipate that private real estate transaction volumes will remain low
- We anticipate better capitalized REITs will ultimately be able to take advantage of mispricing opportunities. Moderating economic growth, reduced consumer activity and rising unemployment rates are likely to stunt demand from cyclically exposed real estate tenants. Real estate property types with structural tailwinds, including industrial, data centres, cell towers and residential segments such as manufactured housing and student accommodation should retain pricing power over tenants
- As such, we expect a wider dispersion between good and weaker earnings reports in the coming quarters to provide stock selection opportunities

Portfolio positioning

- The Portfolio holds a defensive bias, most notably reflecting underweight exposure to higher leveraged REITs and greater focus on investments with higher quality, more predictable rental income and positive earnings growth prospects. Overall positioning reflects a view that the impact of increased interest rates will continue to be a drag on the performance of higher leverage real estate with respect to earnings and net asset values. Higher leveraged REITs will also be limited in their ability to take advantage of investment opportunities as markets recover. The Portfolio ended the period with overweight exposure to the U.S., Hong Kong/China, Japan and the United Kingdom. Larger country underweight exposures are in Continental Europe, Canada and Singapore
- U.S. REITs are held overweight to reflect their balance sheet quality. Japan is also held overweight in reflection of the more limited changes in domestic interest rate policies and expectations of economic stability. Europe and Singapore, which are held underweight, appear more vulnerable to a combination of still low real estate cap rates and their higher financial leverage. Overweight exposure to the U.K. reflects a view that current real estate valuations, implied by REIT stock prices, are overly discounting underlying asset value declines and growth opportunities. The U.K. real estate

market is one of the most transparent globally and appears to be most advanced in reflecting realistic real estate asset pricing

- From a property type perspective, the Portfolio shows overweight exposure to health care, industrial, residential and lodging. Underweight property type exposures are most notable among data centres, office, retail and self-storage. Office and retail underweight exposure reflects a view that structural challenges facing both property types are not yet reflected in share price valuations and that sentiment may still trend negatively. Data centre and self-storage underweight exposures reflect a view that stocks currently fully value the growth opportunity in both sectors. With a view that wider global economic growth trends are deteriorating, the long-term lease and historically low beta characteristics of U.S. health care REITs are attractive. Structural demand trends for industrial remain intact with significant under-renting in the sector, which may be positive for earnings growth. The Portfolio's lodging exposure is focused in Japan, where tourism activity is recovering well. Recent changes to the Portfolio have seen exposure to Hong Kong, and China moderated, recognizing that post-COVID re-opening strength in the economy may now have passed and that growth prospects have diminished.

For more information, including the Investment process, prospectus, and commentary, please visit Invesco.ca

Performance highlights

The Portfolio underperformed its benchmark in the period of relatively flat absolute performance. Sector allocation and stock selection among U.S. REITs were the primary headwinds for performance due to shortfalls across industrial, manufactured housing and healthcare positioning.

Contributors to performance

- The Portfolio had positive performance impacts from underweight exposure to highly leveraged Swedish real estate, favourable stock selection in Canada and underweight exposure to Singapore. The Portfolio also benefited from overweight exposure to diversified companies in Japan and underweight exposure to U.S. self-storage, which is a property type where growth is deteriorating.

Detractors from performance

- The Portfolio underperformed its benchmark in the quarter as defensive positioning was generally not rewarded during a period of higher investor confidence and risk taking
- The Portfolio remains positioned for a deceleration in economic conditions and tighter financial conditions. At the country level, the performance shortfall was focused among U.S. REITs, with some additional underperformance from Hong Kong, the U.K. and Germany
- During the quarter, the defensive characteristics of industrial and manufactured housing were not appreciated by investors and their below-market returns detracted from performance. U.S. industrial REITs may have been negatively impacted by modest deceleration in their historically high growth rates, which may have created headwinds for this higher multiple sector
- U.S. manufactured housing REITs experienced some expense pressures and deceleration in the more operationally sensitive components of their business; however, the sector is expected to show more resilient revenue in a more challenged economic environment
- Underweight exposure to U.S. data centres impacted performance during a period where strong share price performance was recorded among technology companies who may stand to benefit from artificial intelligence (AI). Data centres will have some role in housing AI data, however, any incremental benefit to demand for data centre space is likely a mid to long-term impact
- Residential exposures in Germany also detracted from performance. These companies have excellent earnings resilience, but high leverage levels and steeply discounted valuations, which make them volatile
- Overweight exposure to the U.K. detracted from overall performance. While REIT valuations in the U.K., alongside relative balance sheet strength, are attractive characteristics, the market has been driven by sentiment surrounding U.K. interest rate levels as inflation remains persistently strong

Performance of Invesco Global Real Estate Fund, Series I, as at June 30, 2023:

	1-Year (%)	3-Year (%)	5-Year (%)	10-Year (%)
Invesco Global Real Estate Fund (Series I)	**-1.90**	**2.50**	**0.19**	**5.54**
FTSE EPRA Nareit Developed Index- (gross of withholding taxes)	-1.10	3.30	0.95	6.19

Important information

Sources: Invesco Canada Ltd., Morningstar, as at June 30, 2023.

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The FTSE EPRA Nareit Developed Index is a composite of the existing EPRA Europe Index, EPRA Nareit North American Index and EPRA Nareit Asia Index. This composite index contains publicly quoted real estate companies that meet the EPRA rules in 21 countries throughout Europe, North America and Asia.

The views expressed above are based on current market conditions and are subject to change without notice; they are not intended to convey specific investment advice. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Although we make such statements based on assumptions that we believe to be reasonable, there can be no assurance that actual results will not differ materially from our expectations.

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