

## Summary

- We continue to observe higher inflation prints and the economic outlook remains uncertain.
- In this environment, secure income real assets are increasingly attractive to investors seeking long-dated, inflation-linked income to meet liabilities and diversify their portfolios (this accords with the survey findings – see later for a summary and key takeaways).
- The growing European long income property market provides a good source of such assets, with greater than EUR1bn of pipeline to a diversified set of sectors and pan European geographies.

## Macro picture

10 year nominal Bund yield 2.39%

Irish CPI (y/y) 6.1%

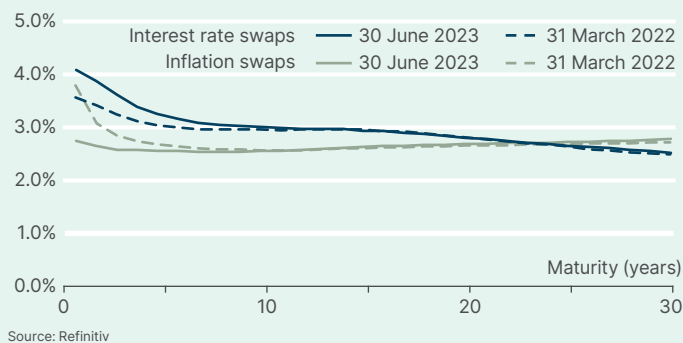
German CPI (y/y) 6.4%

Dutch CPI (y/y) 5.7%

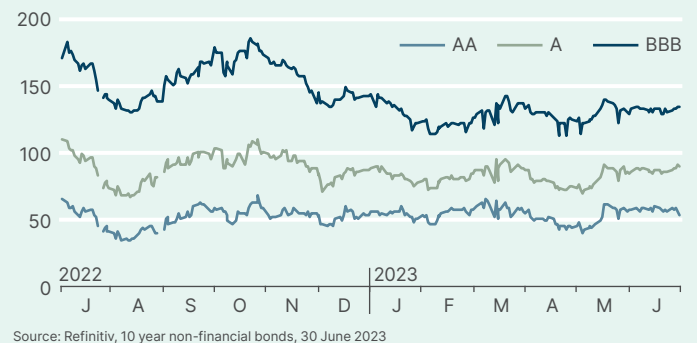
Sources: Bloomberg, 30 June 2023

## Euro area rates, inflation expectations and credit

### Interest rates and inflation expectations



### Credit spreads



### Rates and inflation

- European interest rates have continued to increase at shorter tenors over the last quarter, while they stabilised for longer tenors. This reflects the central bank action to combat inflation.
- Inflation expectations have correspondingly fallen, significantly so at shorter maturities.

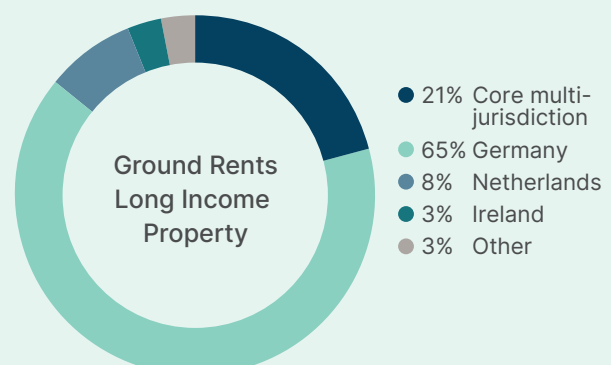
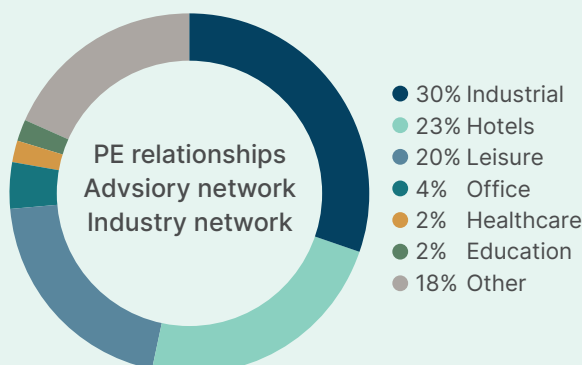
### Credit

- Credit spreads have reduced from the heights seen in recent times, however risks of a potential economic downturn remains a driver of credit risk.

## European Long income – a large and diverse opportunity set

### Priority pipeline of opportunities across diverse range of sectors and countries.

- >€1 billion identified pipeline of multi-sector opportunities in target countries
- Short capital queue, estimated deployment c.3-6 months



Source: AlphaReal metrics 31 December 2022

# AlphaReal recently released our first major survey of European pension funds. We interviewed more than 100 pension fund investment professionals in Europe who collectively oversee €324bn in assets.

### Key takeaways

1. Most funds have inflation-linked return objectives and contractual inflation-linked returns will help them meet those targets.
2. Reducing portfolio volatility is the top priority for European pension funds.
3. Inflation continues to be high but most funds hedge less than half their liability risks.
4. Nearly half of European investors allocate more than 10% to illiquid assets.
5. More than three-quarters of European investors expect to increase allocations to long-dated inflation-linked income solutions.

### Key findings

- 46% of pension funds want to increase portfolio diversification, with 18% wishing to increase portfolio hedging.
- Nearly 80% of European pension funds hedge their inflation exposure to some degree, with 56% hedging less than 50% of their liability inflation risk.
- 98% of respondents have some allocation to illiquid assets, with nearly half allocating more than 10%.
- 85% of respondents want to increase their exposure to long-dated, index-linked income assets.
- The survey found that three-quarters of investors expect a yield of 2.5%-3.0% per annum from long-lease, index-linked real estate assets.

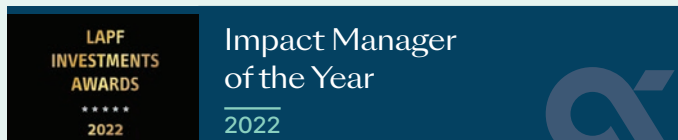
### AlphaReal comment

Secure income real assets, such as our European commercial ground rents fund ELIF, could be an attractive option for European pension funds who want diversification to reduce portfolio volatility and inflation protection to help them meet their targets. These assets can also provide attractive risk-adjusted returns for an investment grade asset.

Investing in real assets with secure income flows that do not respond in the same way as traditional assets to rising inflation and interest rates can help to minimise the effects of market volatility, while simultaneously delivering strong inflation linkage. We believe European investors could continue to increase their illiquid allocations over

the next few years; if inflation remains higher for longer, inflation-linked products could continue to become more attractive. We believe the investment focus will be on areas such as long-income real estate, social infrastructure and renewable infrastructure.

In the UK for example, commercial ground rents have been one of the fastest growing segments of the long income real estate market in recent years, growing from virtually nothing to circa £5 billion in just over five years. We are now seeing potential for similar growth in Europe with pension funds and insurers across Europe evaluating this opportunity.



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