A new chapter for real estate: Rate cuts and the rise of tech

Published 5 November 2024

Baoqi Zhu
Associate Director, Quantitative Research & Multi Asset Solutions

Key Takeaways

- Federal Reserve (Fed) rate cuts historically boost real estate, with a strong negative correlation between rates and real estate indices in recent years.
- Tech-focused real estate, including data centres, is poised for significant growth due to rising tech segments.
- Broader real estate gains from falling rates, but tech assets may lead future performance.
- Investors can capitalise on both rate cuts and technological advancements through tech-driven real estate opportunities.

- Related Products WisdomTree New Economy Real Estate UCITS ETF – USD Acc Find out more

With the US Federal Reserve (Fed) announcing a rate cut on 18 September 2024, we have entered a new phase of monetary policy. While this decision aligns with market expectations, it could significantly impact various sectors. Historically, real estate indices have shown a negative correlation with interest rates in recent years. Furthermore, as technology continues to integrate into the real estate sector, areas such as data centres, modern logistics, and telecom towers exhibit strong growth potential. We believe that tech-focused real estate could emerge as a key growth area within the broader real estate market.

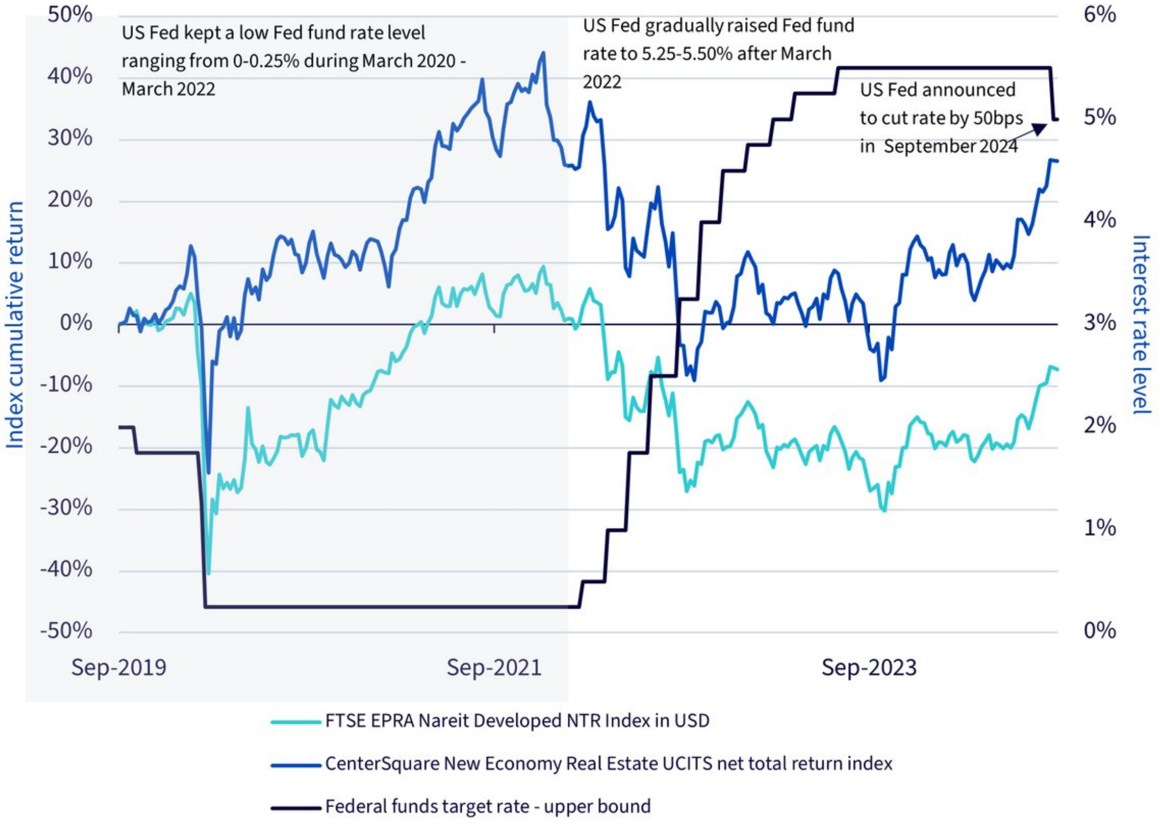
Rate cuts: A boost for real estate?

Many factors influence the real estate sector, but interest rates have played a critical role recently, especially since the Fed began its rate hike cycle in March 2022. Figure 1a illustrates the recovery of real estate indices from the pandemic lows in early 2020, during which the Fed funds rate remained near zero (0-0.25%). We compare two key real estate indices:

- FTSE EPRA Nareit Developed NTR Index (TRNGLU) – A global benchmark in USD
- CenterSquare New Economy Real Estate UCITS NTR Index (CSNEREUN) – A tech-focused real estate index

Both indices posted considerable returns when the interest rate was low, while the global benchmark was hit more severely than the CSNEREUN in early 2020. At this stage, the zero-interest rate policy provides abundant liquidity, greatly boosting the real estate sector.

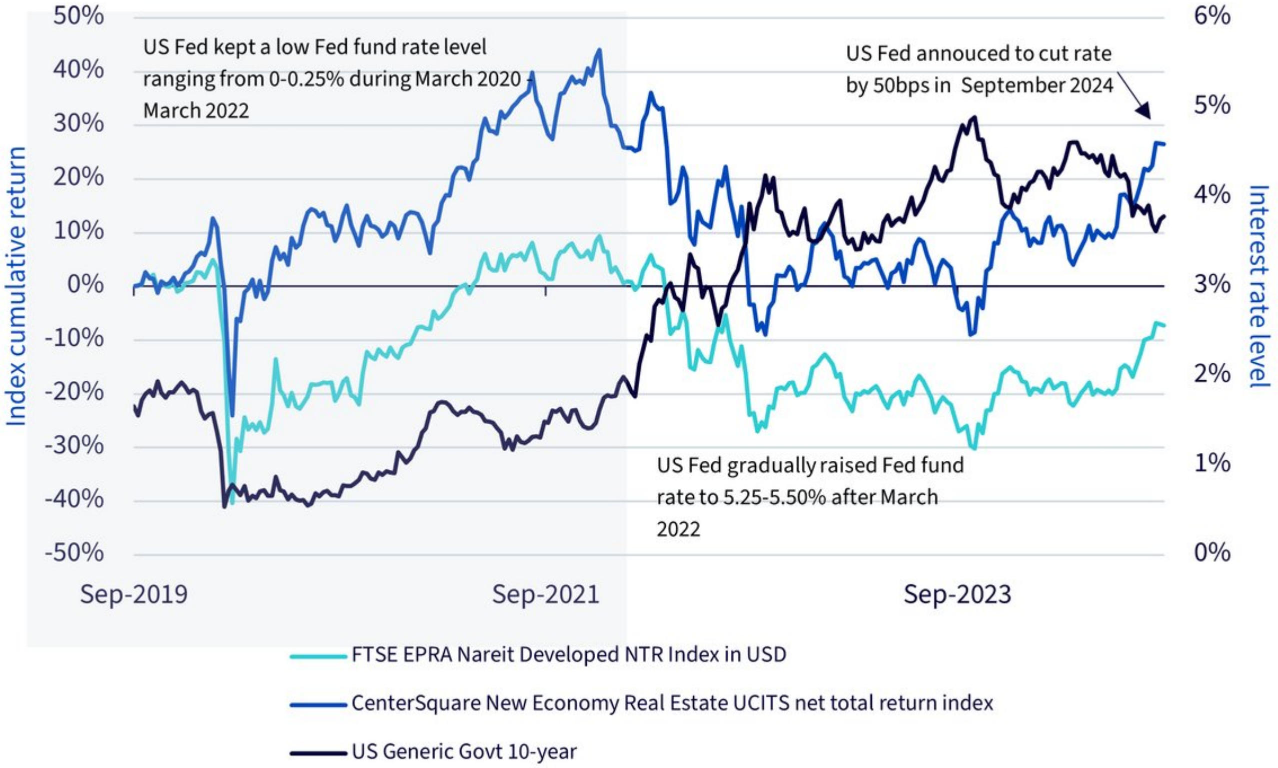
Figure 1a: Performance of real estate indices and the level of the Fed funds target rate



Source: WisdomTree, Bloomberg. Weekly data sourced from 30 September 2019 to 30 September 2024. Index performances are based on the USD term. You cannot invest directly in an index. **Historical performance is not an indication of future performance, and any investments may go down in value.**

However, as the Fed started to increase rates in March 2022, this upward trend slowed. Figure 1b highlights how real estate indices moved in tandem with the US 10-year government bond yield, which better reflects market expectations regarding interest rates. Initially, the indices declined as rates rose, but as inflation stabilised and expectations of rate cuts increased, the sector regained some drivers. The correlation between real estate indices and interest rates, shown in Figure 1c, has been around -50%, suggesting that the new rate cut cycle could provide a tailwind for the sector.

Figure 1b: Performance of real estate indices and the level of US 10-year government bond yield



Source: WisdomTree, Bloomberg. Weekly data sourced from 30 September 2019 to 30 September 2024. Index performances are based on the USD term. You cannot invest directly in an index. **Historical performance is not an indication of future performance, and any investments may go down in value.**

Figure 1c: Correlation between real estate indices and US 10-year government bond yield

Source: WisdomTree, Bloomberg. Periods from 30 September 2019 to 28 March 2022 and from 28 March 2022 to 30 September 2024 respectively. Based on weekly returns for the indices in USD. You cannot invest directly in an index. Historical performance is not an indication of future performance and any investments may go down in value.

Tech-driven real estate growth

While interest rate cuts can boost the broader real estate sector, tech-focused real estate assets, such as data centres and telecom towers, are uniquely positioned to capitalise on technological advancements. Both the broader real estate index (TRNGLU) and the tech-focused index (CSNEREUN) have rallied this year and posted similar returns over the past few years (see Figure 2a). However, a closer look at the industry breakdown reveals notable differences.

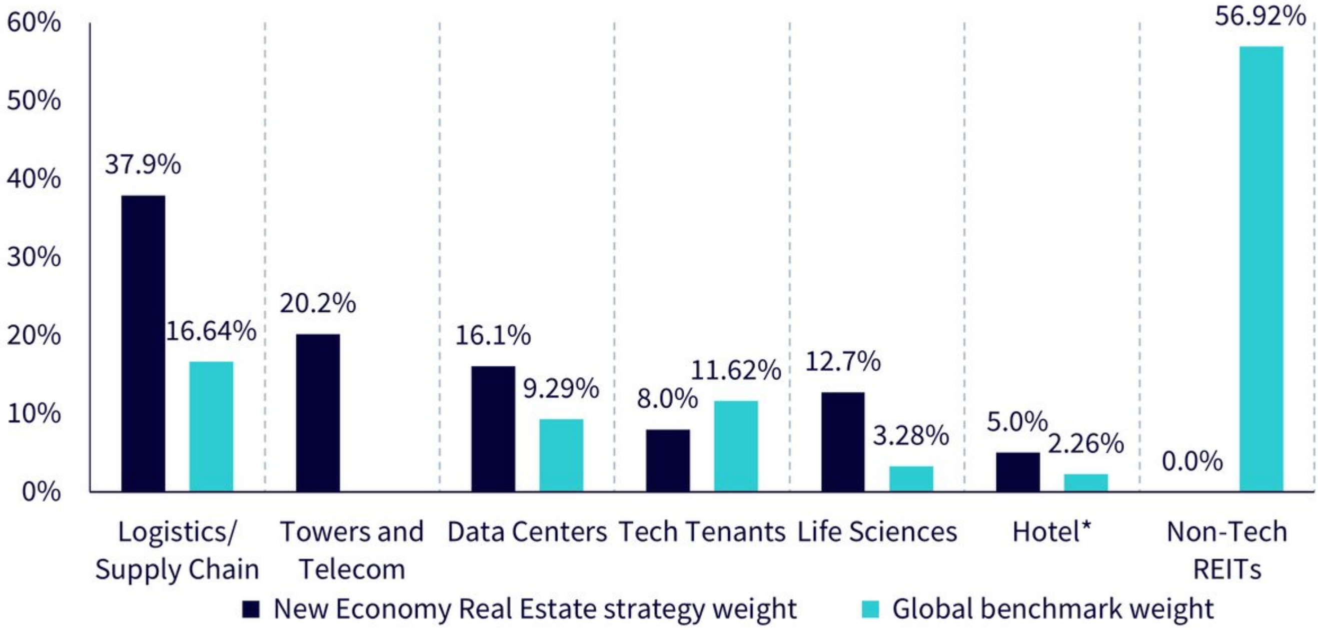
Figure 2a: Performance comparison

Source: WisdomTree, Bloomberg. As of 30 September 2024. Calculations include backtested data. The CenterSquare New Economy Real Estate UCITS Index started its live calculation on 15 September 2021. Indices are computed in the US Dollar terms and on NTR (net total return) basis. Returns for periods over 1 year are annualised. You cannot invest directly in an index. Historical performance is not an indication of future performance and any investments may go down in value.

The broader real estate index includes a significant portion of non-tech REITs (e.g., residential and retail properties, see Figure 2b). While these sectors may benefit from falling rates, they are less likely to capture the growth opportunities associated with technology megatrends. On the other hand, tech-focused real estate, represented by the CSNEREUN index, is built to capture several key trends driven by technological innovation:

- Generative AI Cloud computing is transforming how software and computer resources are used, with data centres requiring specially designed warehouses to operate
- 4G and 5G connectivity is gaining momentum, but it depends on telecommunication tower sites for expansion
- Logistics and supply chains rely on specialised warehouses for fast delivery, including refrigerated storage, which ensures food is transported within regulatory guidelines
- The life sciences industry is growing, with laboratories being essential real estate for supporting biotech advancements

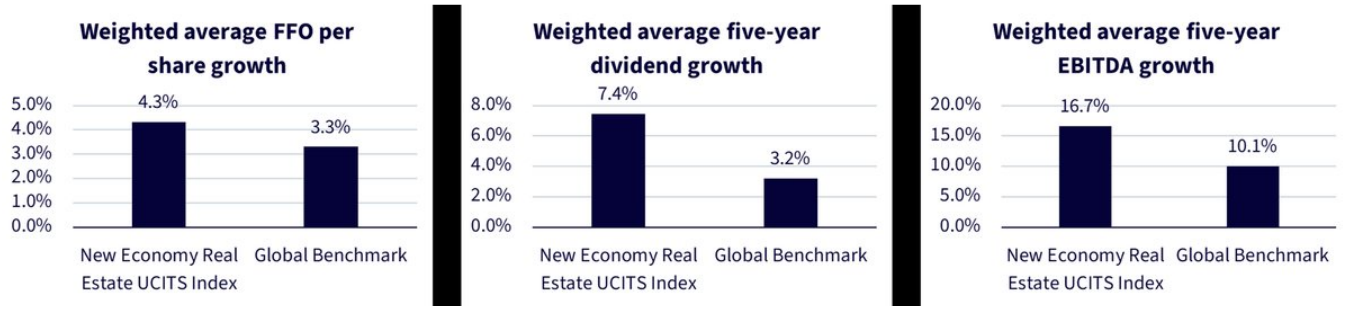
Figure 2b: Segment breakdown



Source: CenterSquare, Bloomberg. As of 19 September 2024. The Global benchmark is the **FTSE EPRA Nareit Developed Index**. The New Economy Real Estate Strategy is **CenterSquare New Economy Real Estate UCITS Net Total Return Index**. Tech Tenants are represented by the “Office” and “Diversified” sectors within the New Economy Real Estate UCITS Index. *Companies within the “Hotel” sector classified as having low sensitivity to technology are reflected under “Non-Tech REITs” category. **You cannot invest directly in an index. Historical performance is not an indication of future performance, and any investments may go down in value.**

Although the performance of the CenterSquare New Economy Real Estate UCITS Index and the FTSE EPRA Nareit Developed Index has been similar over the past few years, the former has shown stronger growth in terms of FFO1 per share, dividends and EBITDA2 (see Figure 2c). This indicates the strong potential of tech-focused real estate and highlights the alignment between technological progress and real estate performance.

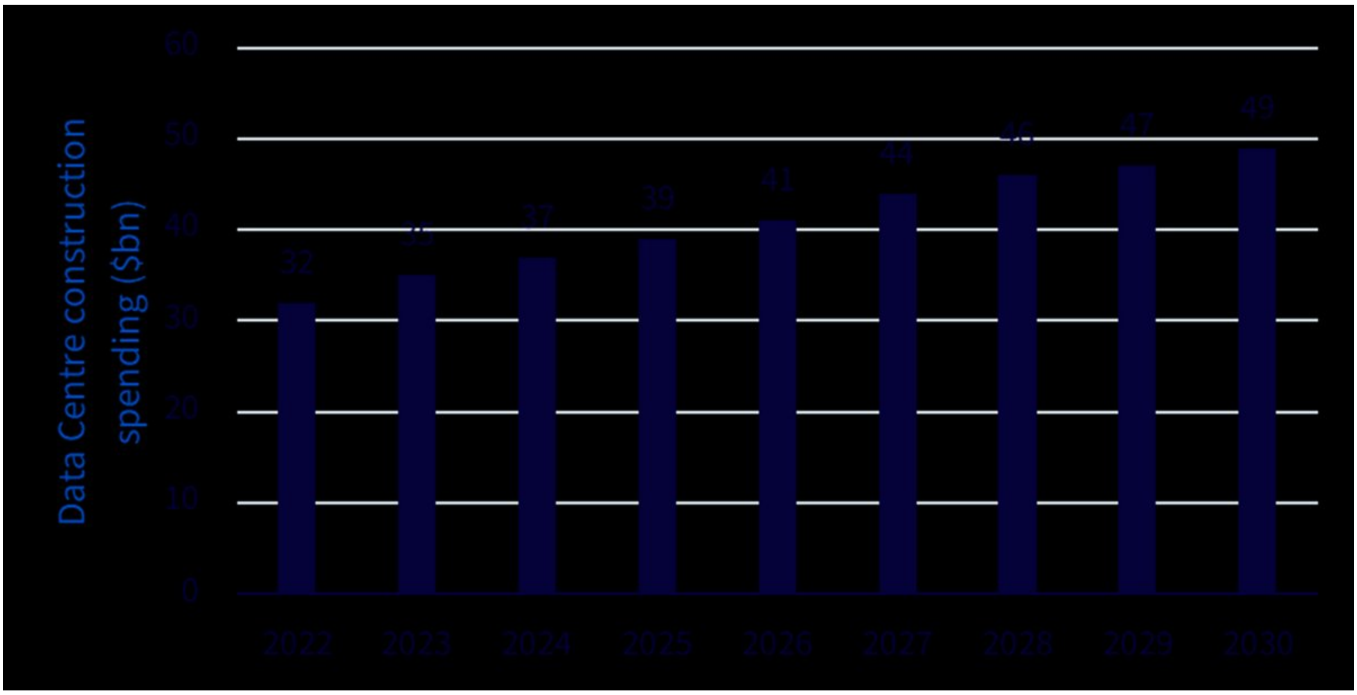
Figure 2c: Segment breakdown



Source: CenterSquare, Bloomberg. As of 19 September 2024. New Economy Real Estate Strategy is represented by the **CenterSquare New Economy Real Estate UCITS Index.** The Global benchmark is the **FTSE EPRA/Nareit Developed Index.** EBITDA is earnings before interest, taxes, depreciation, and amortization. **You cannot invest directly in an index. Historical performance is not an indication of future performance, and any investments may go down in value.**

One clear example of tech real estate's growth potential is the increasing demand for data centres. McKinsey forecasts global spending on data centre construction to reach $49 billion by 2030. This significant investment stems from the need for advanced infrastructure to support the expanding AI ecosystem. As tech giants engage in an arms race to develop large language models (LLMs), the demand for state-of-the-art data centres continues to grow, reinforcing the importance of tech-focused real estate in the evolving market.

Figure 3: Data centre construction spending forecast ($bn)



Source: McKinsey & Company, “Investing in the rising data centre economy”. **Historical performance is not an indication of future results and any investments may go down in value.**

Conclusion

The CenterSquare New Economy Real Estate UCITS Index is heavily weighted toward tech-related real estate, such as logistics, telecom towers, and data centres. In contrast, broader benchmarks like the FTSE EPRA Nareit Developed Index include more non-tech REITs, such as residential and retail properties. In addition to the potential boost from falling interest rates, tech-driven catalysts – such as increased AI and robotics applications in logistics and growing demand for data centres – could drive further growth in this sector. For investors looking to capitalise on both falling interest rates and the ongoing technology boom, WisdomTree New Economy Real Estate UCITS ETF may present a compelling opportunity.

What WisdomTree offers its investors

The WisdomTree New Economy Real Estate UCITS ETF tracks the CenterSquare New Economy Real Estate UCITS Index, offering investors exposure to high-growth opportunities within tech-driven real estate. The fund posted 15.2% of return in Q3 2024 and is the best performing thematic ETF in WisdomTree’s thematic family. This ETF is designed to capture the benefits of megatrends such as cloud computing, 5G connectivity, and advancements in logistics and life sciences. With a strategic asset allocation focused on tech-integrated real estate assets like data centres and telecom towers, the ETF provides diversification while adapting to evolving market dynamics. Its stock selection process emphasizes companies poised to benefit from technological advancements, offering a differentiated portfolio compared to traditional real estate indices.

Source

1 FFO, short for funds from operations

2 EBITDA, short for earnings before interest, taxes, depreciation, and amortisation

Important Risks Related to this Article

Important Information

Marketing communications issued in the European Economic Area ("EEA"): This document has been issued and approved by WisdomTree Ireland Limited, which is authorised and regulated by the Central Bank of Ireland.

Marketing communications issued in jurisdictions outside of the EEA: This document has been issued and approved by WisdomTree UK Limited, which is authorised and regulated by the United Kingdom Financial Conduct Authority.

WisdomTree Ireland Limited and WisdomTree UK Limited are each referred to as "WisdomTree" (as applicable). Our Conflicts of Interest Policy and Inventory are available on request.

For professional clients only. The information contained in this document is for your general information only and is neither an oer for sale nor a solicitation of an oer to buy securities or shares. This document should not be used as the basis for any investment decision. Investments may go up or down in value and you may lose some or all of the amount invested. Past performance is not necessarily a guide to future performance. Any decision to invest should be based on the information contained in the appropriate prospectus and aer seeking independent investment, tax and legal advice.

The application of regulations and tax laws can oen lead to a number of dierent interpretations. Any views or opinions expressed in this communication represent the views of WisdomTree and should not be construed as regulatory, tax or legal advice. WisdomTree makes no warranty or representation as to the accuracy of any of the views or opinions expressed in this communication. Any decision to invest should be based on the information contained in the appropriate prospectus and aer seeking independent investment, tax and legal advice.

This document is not, and under no circumstances is to be construed as, an advertisement or any other step in furtherance of a public oering of shares or securities in the United States or any province or territory thereof. Neither this document nor any copy hereof should be taken, transmitted or distributed (directly or indirectly) into the United States.

Although WisdomTree endeavours to ensure the accuracy of the content in this document, WisdomTree does not warrant or guarantee its accuracy or correctness. Where WisdomTree has expressed its own opinions related to product or market activity, these views may change. Neither WisdomTree, nor any ailiate, nor any of their respective oicers, directors, partners, or employees accepts any liability whatsoever for any direct or consequential loss arising from any use of this document or its contents.