REDWOOD | CREMX TICKER

Beyond sector rotation: Private real estate equity vs. private real estate debt

Within traditional real estate equity portfolios, sector rotation has long been a central tool for navigating market cycles. Allocators or managers may tilt allocations toward multifamily during periods of housing undersupply, shift toward industrial amid logistics demand, or reduce exposure to office as fundamentals weaken. The objective is straightforward: Reposition capital toward segments of the market with more favorable supply/demand dynamics while avoiding those facing structural or cyclical headwinds.

This approach reflects a practical reality – real estate is not a monolithic asset class. Property types respond differently to economic conditions, tenant demand and capital availability. As a result, thoughtful sector allocation can play an important role in shaping portfolio outcomes over time.

At the same time, sector rotation operates within a shared return framework. Whether capital is allocated to industrial, multifamily or retail, performance remains largely tied to property-level fundamentals: rental growth, occupancy trends and changes in asset valuations. While rotating exposures may improve relative outcomes, the underlying drivers of return – and risk – are broadly consistent across sectors.

The limits of rotating within a single return framework

Even well-executed sector rotation depends on the ability to anticipate changes in market conditions and reposition capital efficiently. In practice, cycles are often less discrete than expected. Different property types may be influenced by common macro factors, including interest rate movements, capital market liquidity and financing conditions.

In these environments, correlations across sectors can increase, reducing the effectiveness of rotation as a risk-management tool. Allocators may find that shifting between property types does not fully mitigate drawdowns when the broader real estate market is repricing. Further, liquidity may limit the allocator's ability to redistribute the allocation across equity sectors.

This dynamic highlights a structural consideration: Rotating exposures within real estate equity primarily redistributes risk, rather than fundamentally changing the drivers of return. An alternative approach is to complement sector positioning with diversification at a more fundamental level: the *source* of real estate returns.

Introducing a distinct return driver: Real estate credit

Private real estate credit offers a differentiated return profile that is not directly dependent on property appreciation. Instead, returns are primarily derived from contractual cash flows – loan coupons and spreads relative to floating benchmark rates – along with the return of principal at maturity.

This structure introduces a different set of underlying drivers. Performance is more closely tied to underwriting discipline, borrower behavior and collateral coverage than to cap rate movements or leasing trends. While credit risk remains central, it manifests differently than in equity-oriented strategies.

Portfolio return correlations (1/1/2010–3/31/2026)

	Commercial real estate private debt	Commercial real estate private equity	REIT Index
Commercial real estate private debt	1.00		
Commercial real estate private equity	0.29	1.00	
REIT Index	0.17	-0.33	1.00

Sources: Bloomberg, Giliberto-Levy, Redwood. Data as of 3/31/26. Date range from 1/1/2010–3/31/2026. Commercial Real Estate Private Debt is represented by the Giliberto-Levy 2 Index, REIT Index is the Dow Jones Equity REIT Total Return Index, Commercial Real Estate Private Equity is represented by the NCREIF Property Index.

In this context, diversification is achieved not by reallocating among sectors, but by incorporating a complementary return stream – one that is based on income generation and capital structure positioning.

Reframing portfolio construction

From a portfolio construction standpoint, this distinction can be meaningful. Rather than relying solely on sector rotation to manage cyclicality, allocators can combine exposures that respond to different market forces.

In practice:

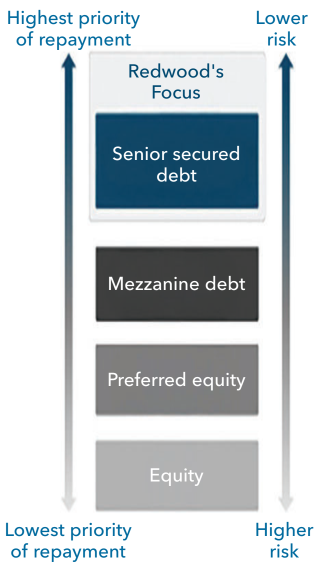
- Real estate equity strategies provide participation in long-term income growth and asset appreciation.
- Real estate credit strategies provide exposure to contractual income streams with defined maturities.

Blending these approaches introduces diversification along an additional dimension. Instead of attempting to optimize outcomes through sector selection alone, the portfolio incorporates multiple mechanisms for generating returns.

A RiskFirst® implementation

The Redwood Private Real Estate Debt Fund (CREMX) reflects this framework through its focus on senior secured bridge lending across a diversified mix of property types, including multifamily, industrial, retail, residential and mixed-use assets.

The strategy targets short-duration exposures, which allow capital to be recycled as loans are repaid or refinanced. This ongoing turnover results in a continual refresh of underlying portfolio-level exposures rather than active sector-rotation decisions. Further, the enhanced income from the debt can be deployed toward other sectors opportunistically, as sector returns determine, in a total real estate portfolio management approach.



Senior secured debt has the highest priority of repayment in case of default and thus, the lowest level of risk.

Mezzanine debt sits below senior secured debt in the capital stack and above equity. It has a lower priority of repayment than senior debt and therefore carries a higher level of risk, typically compensated by higher return potential.

Preferred equity is an equity investment that ranks above common equity but below all debt in the capital stack. It does not have a direct claim on the property like debt, but typically receives priority over common equity for distributions, reflecting a higher risk profile than debt.

Equity represents the ownership of a company's net asset value or cash that remains after all assets are liquidated minus liabilities.

Sources: Redwood. For illustrative purposes only.

An investment in secured debt does not guarantee that the fund will receive principal and interest payments according to the investment terms or at all, or that the fund will be able to collect on the investment if it is forced to enforce its remedies.

At the same time, the emphasis on senior secured positions places the strategy higher in the capital structure, with a focus on collateral coverage and income generation. The return profile is therefore driven less by changes in property valuations and more by the performance of the underlying loans.

From a broader allocation perspective, this creates exposure to real estate through a different lens – one that is aligned with income and duration management rather than appreciation and sector timing.

Complementing, not replacing, equity allocations

Sector rotation remains a relevant and widely used tool within real estate equity portfolios. However, its effectiveness may vary depending on market conditions and the degree to which sector performance diverges.

Incorporating a credit-oriented allocation does not replace the role of equity. Instead, it can complement it by introducing a return stream with different drivers and sensitivities. This combination may help moderate portfolio variability, particularly in environments where sector-level distinctions are less pronounced.

Conclusion

For allocators, the question is not simply which sectors to emphasize at a given point in the cycle. It is also how those allocations generate returns – and how they interact within the broader portfolio.

Expanding the focus beyond sector positioning to include the differentiated return sources of real estate debt allows real estate allocations to be built with greater structural diversification. Sector rotation remains one tool for managing cyclicality. Real estate credit is another – one that works through income and collateral rather than appreciation and timing.

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CORPORATE OVERVIEW

Redwood Investment Management brings institutional-grade investment processes to all individual investors through its **RiskFirst®** solutions. By prioritizing risk management, Redwood believes investment success naturally follows. These innovations include democratizing access to private debt secured by real estate with a single ticker symbol and offering turnkey asset allocation models that blend public and private investments. Redwood partners with financial advisers to deliver these solutions via Redwood mutual funds, **LeaderShares®** ETFs and Engineered Risk-Budgeted Model portfolios. With no minimums, accreditation or paperwork, investors gain access to short-duration, first lien secured real estate loans – making sophisticated investing available to all.

Important Information

RiskFirst® is a registered trademark of Redwood Investment Management, LLC. The Redwood Private Real Estate Debt Fund ("CREMX") is registered as a non-diversified, closed-end management investment company that is operated as an interval fund. **The Fund's investment program is speculative and entails substantial risks. There can be no assurance that the Fund's investment objective will be achieved or that its investment program will be successful.** The Fund is an appropriate investment only for those investors who can tolerate a high degree of risk and do not require a liquid investment. The Fund does not intend to list the Shares on any securities exchange and the Fund does not expect a secondary market in the Shares to develop. Because you will be unable to sell your Shares or have them repurchased immediately, you will find it difficult to reduce your exposure on a timely basis during a market downturn.

Investors should carefully consider the investment objectives, risks, charges and expenses of the Redwood Private Real Estate Debt Fund. This and other important information about the Fund are contained in the prospectus, which can be obtained at redwoodmutualfunds.com or by calling 888.570.0805. The prospectus should be read carefully before investing.

The Fund invests in commercial mortgage loans subject to risks of delinquency, foreclosure, and loss. Additional risks include reliance on participation interests that depend on lead lenders' decisions, exposure to fixed-income market fluctuations and liquidity constraints, as well as sensitivity to inflation or deflation affecting property values and borrower repayment capacities. Secured debt is not guaranteed and may still be insufficient if collateral values decline. Holdings in subordinated debt may suffer greater losses during defaults. SOFR interest rate benchmarks are variable and may affect income and borrower costs. Operational challenges such as sourcing quality loans and competitive pressures can impact portfolio performance.

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