UBS Property Securities Fund

July 2020

Fund description
The Fund is a portfolio of mainly Australian real estate securities that the Portfolio Manager believes are being undervalued by the market.

Investment strategy
The Fund uses a disciplined investment process that combines in-depth top-down and bottom-up fundamental market research with a disciplined and systematic approach to portfolio construction and risk management. Portfolio stock selection is driven by proprietary analytical techniques to conduct fundamental company analysis, which provides a framework for security selection through an analysis of individual securities independently and relative to each other.

The Fund will normally hold between 15–25 securities.

Investment return objective
The Fund aims to outperform (after management costs) the S&P/ASX 300 Property Accumulation Index over rolling five year periods.

Active security positions

<table>
<thead>
<tr>
<th>Overweight</th>
<th>Underweight</th>
</tr>
</thead>
<tbody>
<tr>
<td>Charter Hall Social Infrastructure REIT</td>
<td>Scentre Group</td>
</tr>
<tr>
<td>Home Consortium</td>
<td>Shopping Centres Australasia</td>
</tr>
<tr>
<td>Dexus</td>
<td>Charter Hall Long WALE REIT</td>
</tr>
<tr>
<td>Charter Hall Retail REIT</td>
<td>Charter Hall Group</td>
</tr>
<tr>
<td>Lifestyle Communities</td>
<td>BWP Trust</td>
</tr>
</tbody>
</table>

Investment portfolio (%)

- Industrial REITs: 30.8
- Diversified REITs: 26.9
- Retail REITs: 20.6
- Office REITs: 10.8
- Specialized REITs: 3.8
- Real Estate Development: 2.8
- Residential REITs: 2.4
- Cash: 2.0

Investment performance

<table>
<thead>
<tr>
<th>Fund</th>
<th>1 month</th>
<th>3 months</th>
<th>1 year</th>
<th>3 years % pa</th>
<th>5 years % pa</th>
<th>Since inception % pa</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total return</td>
<td>0.33</td>
<td>6.69</td>
<td>(19.38)</td>
<td>4.94</td>
<td>5.46</td>
<td>7.22</td>
</tr>
<tr>
<td>Benchmark**</td>
<td>0.63</td>
<td>6.41</td>
<td>(22.24)</td>
<td>2.59</td>
<td>3.70</td>
<td>7.68</td>
</tr>
<tr>
<td>Added Value</td>
<td>(0.30)</td>
<td>0.28</td>
<td>2.86</td>
<td>2.35</td>
<td>1.76</td>
<td>(0.46)</td>
</tr>
</tbody>
</table>

*Inception date: 1 February 1993. **S&P/ASX 300 Property Accumulation Index. Prior to 1 June 2012, the benchmark was 85% S&P/ASX 300 Property Accumulation Index, 15% EPRA NAREIT developed index (hedged in AUD).

Performance figures are net of ongoing fees and expenses. The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns.
Portfolio review
After fees and expenses, the portfolio increased by 0.33% over the month, underperforming its benchmark by 30bps. The fund’s performance benefited from overweight exposure to Goodman Group, Home Consortium and Charter Hall Social infrastructure (CQE). Strong results from global industrial peers helped lift Goodman. HomeCo’s capital raising to fund acquisitions in the convenience retail sector was well supported. CQE benefited from supportive government policies to the Childcare sector. Detractors from relative performance came from underweight exposure to fund manager Charter Hall Group, which announced several direct asset transactions and lifted the outlook for Funds Under Management. Overweight exposure to Dexus and Lifestyle Communities also detracted to performance with concerns around the work from home thematic and further lockdown restrictions in Victoria weighing on sentiment.

Market review
The Australian REIT market (S&P/ASX 300 A-REIT Index) was up a modest +0.6% in July, outperforming the broader equity market which rose +0.5% (S&P/ASX 200 Index). The second wave of COVID-19 cases across Victoria and subsequent increase in mobility restrictions weighed on the office and retail sectors over the month. Occupational conditions remain challenging in the office sector. Official vacancy is now above 7% in Sydney and Melbourne and sublease space is increasing rapidly. Physical occupancy of buildings in the CBD is estimated to be closer to 30% and even lower in Melbourne. Against this backdrop, effective market rents are expected to fall by 10-15% over the next 12 months. Cash collection remains high at ~90-95% and recent transaction evidence continues to remain supportive to asset valuations with GIC acquiring 50% of a Melbourne office tower on a 5% cap rate. Recently reported June valuations showed a modest 0-2% valuation fall across the office exposed AREITs. Discretionary retail continues to experience headwinds as lockdowns in Victoria are likely to see further cash abatements required by landlords. Ecommerce continues to take a greater share of retail sales. Transaction evidence is scarce, and Vicinity Group reported its valuations fell 12% over the 6 months to June and expected to fall further over the next 12 months. European listed retailer Unibail-Westfield reported a 28% fall in earnings in 1H20 with just 35% of rents collected in the June quarter. Earnings guidance remains withdrawn and further asset sales are planned to reduce leverage.

The backdrop is more favorable for industrial where tenant demand remains strong. Amazon recently committed to a 20-year lease with Goodman, while Woolworths committed to a new 75k sqm facility in Moorebank in Western Sydney. Investment demand for industrial is even stronger with Charter Hall and Dexus completing transactions at ~5% cap rates. Industrial now represents almost 30% of the AREIT index.

The residential sector continues to benefit from government stimulus with NSW removing stamp duty for first home buyers on land purchases up to $400k and new house purchases up to $800k, on top of the $25k federal homebuilder stimulus announced in June. Land lease community operators Lifestyle Communities and Ingenia Communities are both expected to benefit from this stimulus with Ingenia providing a strong sales update to the end of June despite the challenging economic backdrop.

Outlook
The AREIT market has recovered strongly from its lows in March but remains significantly down from its highs in February. Real estate securities should continue to fare relatively well in the current environment given comparatively stable cash-flows, attractive yields, and robust balance sheet positions. While the economic environment is likely to remain soft, particularly as some of the stimulus policies are unwound in 2H20 - 1H21, the listed market is already pricing in a material slowdown in activity. However, there are resilient regions, property sectors, and companies that we find very attractively priced after recent price declines.

The sector is currently trading at a ~7% discount to our assessment of Net Asset Value (already conservatively incorporating significant asset value falls), offers an attractive dividend yield spread over government bonds, and trades on a significant PE discount to broader equities. AREITs are in a much stronger balance sheet position with average gearing at ~28% vs almost 40% leading into the GFC. Liquidity is also significantly stronger with all major REITs having liquidity to meet upcoming debt expiries over the next 18 months.

The fund remains defensively positioned towards companies with low leverage, quality assets & management teams. The fund is positioned to take advantage of attractive long dated structural themes like industrial, essential services and childcare, and heavily discounted residential exposure that is likely to be best positioned to benefit from an eventual recovery aided by government stimulus. We remain cautious on discretionary retail. Should current discounts persist, we expect to see a pickup in corporate activity (M&A) given the wide arbitrage between the direct and listed property markets, lower $A, cheap cost of debt and relative attractiveness of the Australian property market which will help to support listed share prices.
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