Components of *agio*

In real estate funds, there is usually a positive differential between market price and the net asset value. There are *objective reasons,* which relate to factors other than market interest rates, for this so-called agio.

The term "agio" has its origins in Italian and means "comfort". People are prepared to pay a higher price for convenience and this is evident everywhere from the food industry to the financial sector.

In the context of listed real estate funds, the agio represents the differential between market price and the net asset value of the unit certificates. The historic average of this premium is approximately 15 percent and fluctuates based upon market interest rates. This means that investors are evidently prepared to pay a premium for the added benefits of real estate funds as opposed to direct investments. There are three objective reasons that support this positive differential.

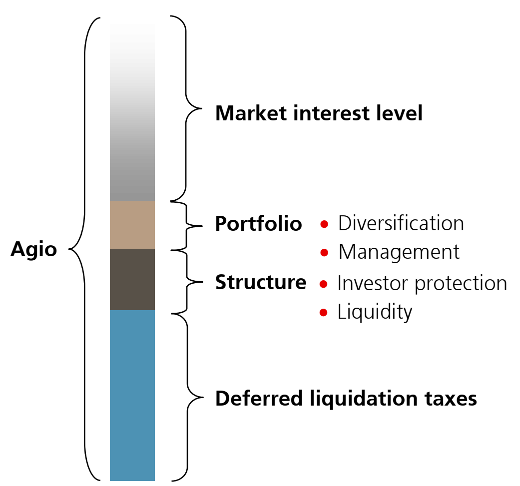
Three components of the added value

The first justification for agio relates to the *portfolio properties* of a listed real estate fund. The net asset value of a real estate fund is based upon the total of the individual asset valuations. However, the market price reflects the valuation of the overall portfolio, which benefits from risk diversification across regions and sectors. Therefore, compared with each individual property the overall fund offers *diversification benefits*, for which investors pay a premium.

A second component of agio is explained by the *investment vehicle structure*. A Swiss real estate fund, being listed on the stock market, offers *higher liquidity* compared with direct investment. Furthermore, real estate funds are subject to the Swiss Federal Collective Investment Act (KAG) as well as the Swiss Financial Market Supervisory Authority (FINMA), providing investors with appropriate investment protection and a right of termination at the net asset value. Since these two features offer investors added value, investors are prepared to pay a price above the net asset value.

The third and perhaps the most substantial component is attributable to *deferred liquidation taxes*. When calculating the net asset value, the deferred liquidation taxes are deducted from the calculated portfolio market value. This hypothetical amount would be incurred only in the event of liquidation of the portfolio. If however one assumes that the real estate fund is not going to be liquidated, then the net asset value used to calculate the agio is too low. This is particularly noticeable with funds that have existed for decades: in a liquidation scenario high property gains taxes would be due, so the *deferred liquidation taxes* can amount to more than 10% of the fund's overall net asset value: i.e. in many older funds, around 10 percentage points of the agio can be ascribed to current accounting rules relating to deferred taxes.

Components of Agio



Source: Global Real Estate Research & Strategy - Switzerland; February 2013

The stated factors argue for a natural, positive differential between market price and net asset value and support the long-term average of approximately 15 percent.

For more information please contact

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