Ten reasons to be invested in European Listed Real Estate

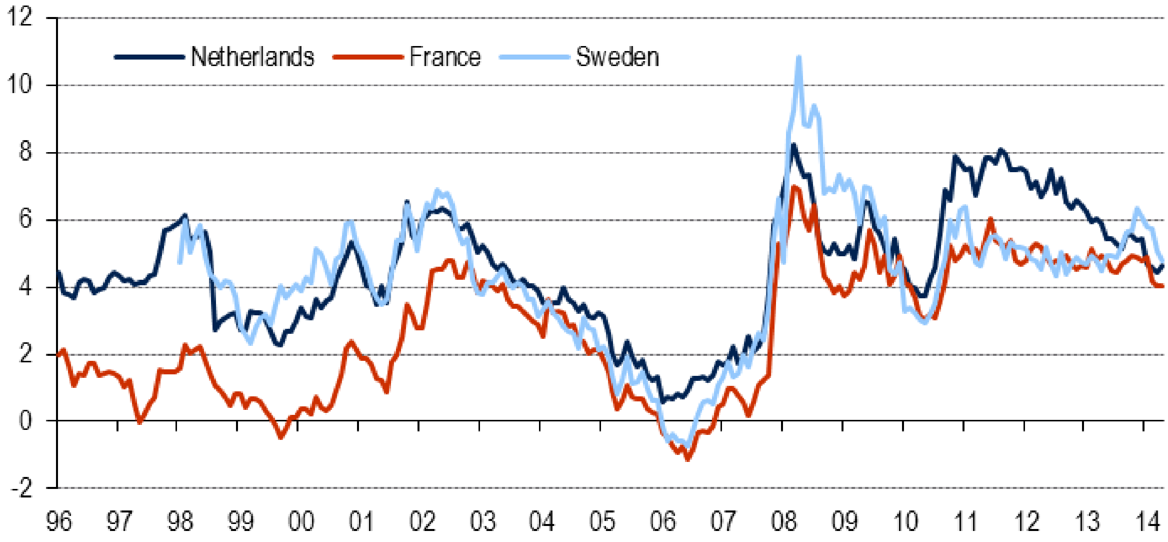
Executive Summary

At Petercam Institutional Asset Management, we are convinced that investing part of one's assets in European listed real estate makes sense. We hereby illustrate our view with a number of compelling arguments to invest in our dedicated products. The specific asset class of European listed real estate provides investors with an attractive risk return proposal with strong fundamentals, indirect but real exposure to the real estate markets and superior liquidity.

1/ Quest for yield

Listed property offers an **attractive answer to investors hunting for yield**. The yield gap between the implied yield of listed property companies and bond yields has been gradually declining but at a 400bps the risk premium is still reasonably high, especially since interest rates are likely to remain lower for longer.

Spread between Continental EPS yield and 5-yr SWAP rates (%)



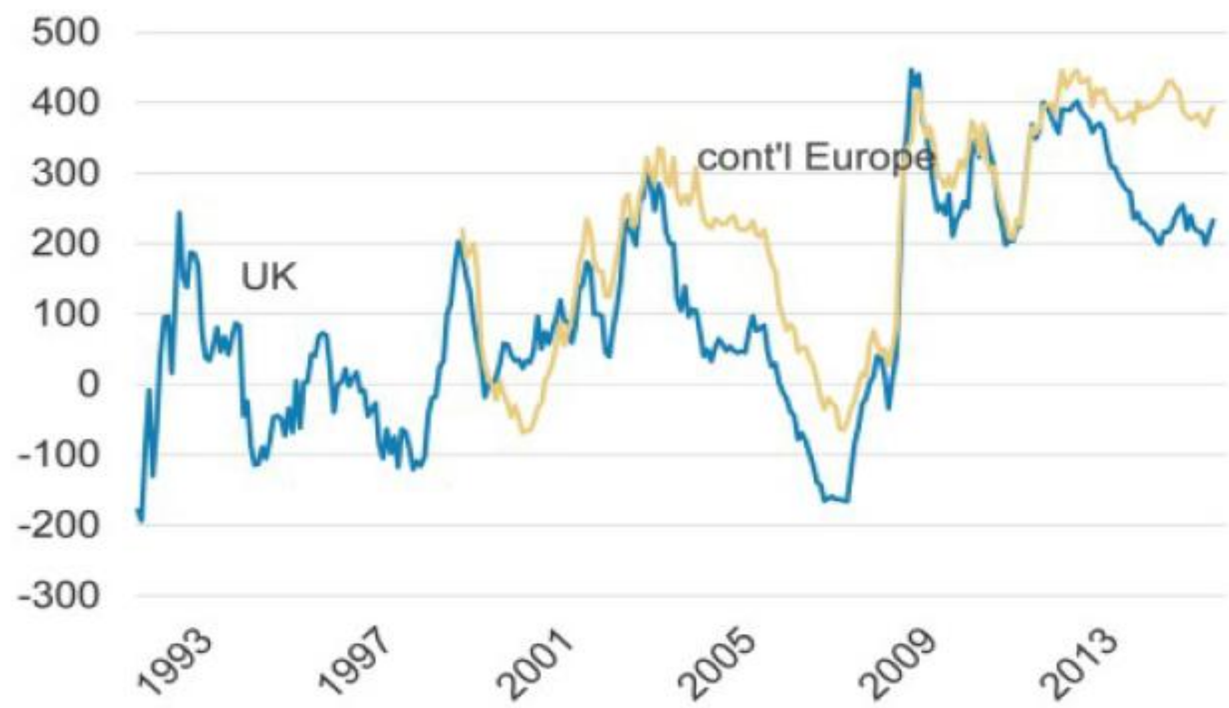
Source: Company data, Datastream, Kempen & Co estimates - last update: 01/05/2015

2/ Attractive property yields and cheap financing = sound and accretive business

We are comfortable with the current level of **implied property yields which provide a nice and healthy spread compared to the base rate for financing** as the 5y swap rates.

Quality and well managed property companies with healthy balance sheets have easy access to the equity and debt markets at a cost well below yields on new acquisitions or developments. A recent example of this cheap financing was the 10 year bond issue of Unibail-Rodamco priced at 1% with a 0.5% margin over the mid swap rate. This will finance the development pipeline yielding around 7% on cost price.

EBITDA/EV yield margin over local 5-yr swap rates

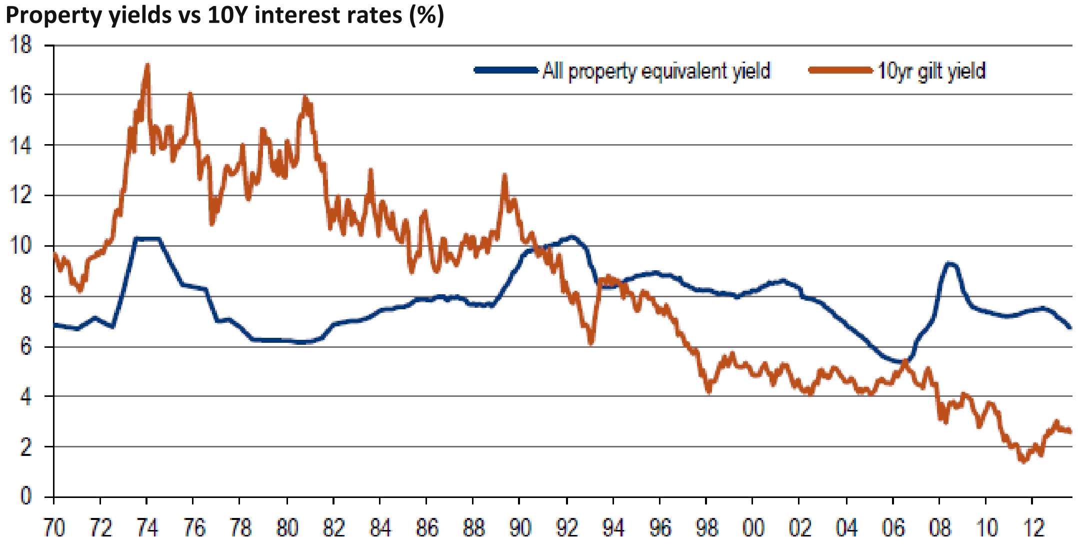


Source: Company date, Datastream, Morgan Stanley Research, Date: 30/9/2015

3/ Listed real estate and interest rates

Some investors fear that higher bond yields would hamper the performance of listed real estate. Over the long term we see no significant correlation between both. One of the reasons being the inflation hedge of real estate when interest rates increase. In a growing economy tenants take up more space for offices and higher retail sales meaning lower occupancy cost ratio for retail properties and room to increase rents. In addition, if interest rates have entered "unchartered territory" for quite some time, property yields haven't and are not far from historical average, so the risk premium is at historical highs. A recent illustration is the development of an logistic platform in Bavaria by VIB Vermögen yielding an 8.7% on cost with 70% financed at a fixed cost of debt of 2.9 % for a 10 year loan.

Property yields vs 10Y interest rates (%)

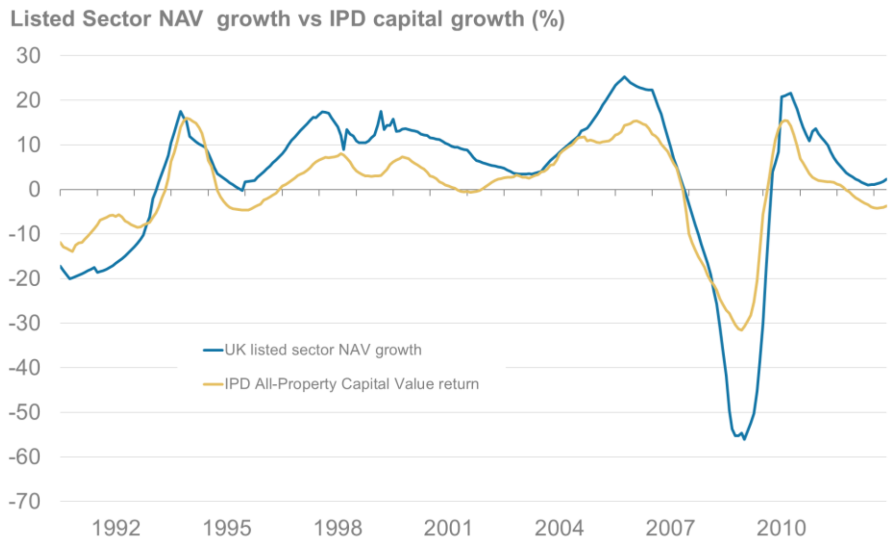


Source: Datastream, IPD, Kempen & Co estimates

4/ Better quality assets

On average, the **listed property sector owns the better quality real estate assets** compared to the market on average.

- We see that on evolution of NAVs, listed property companies beat their respective IPD benchmarks, except in the post-Lehman liquidity squeeze.
- We also see that the average vacancy rates of our listed property universe are systematically lower than the market's, which is a good measure for quality.
- For most companies owned in Petercam funds it would be impossible to replicate similar portfolios in current markets and at reported NAVs. This is also a sign that listed real estate offers good value compared to direct real estate.

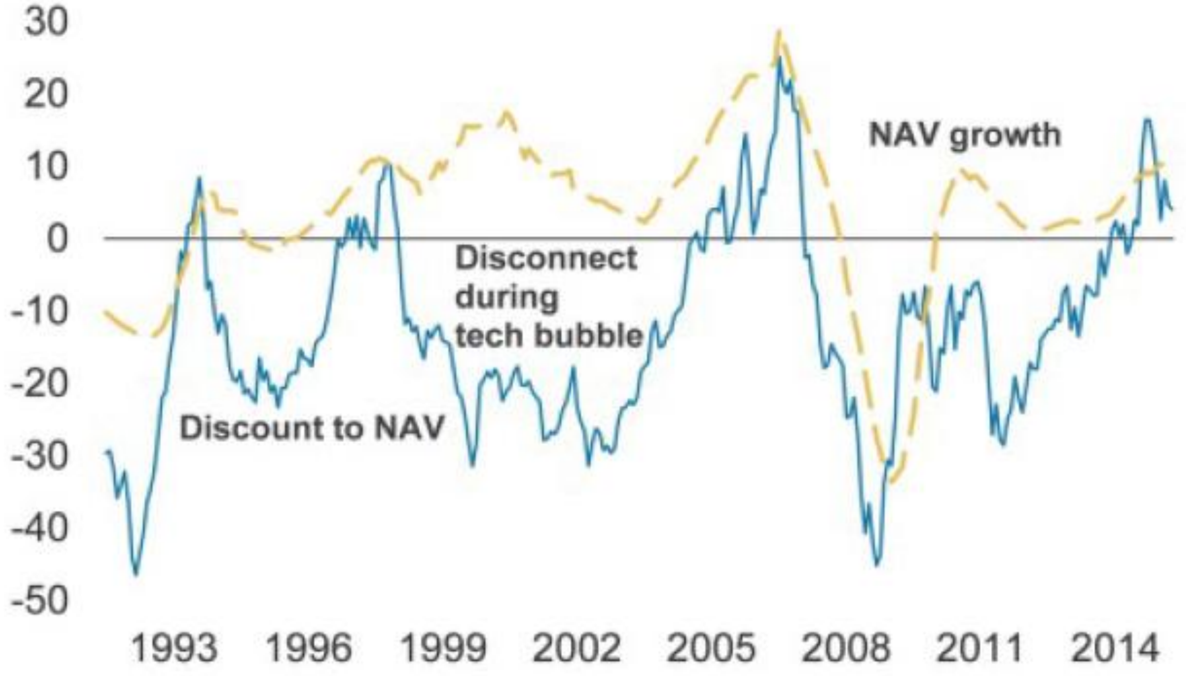


Source: Investment Property Databank, Petercam IAM

5/ Prime assets and NAV growth

The current average premium to the expected NAV's is around a of 0 to 4%; Based on latest direct real estate market information we argue that latest reported NAV's are lagging the investment market. **We anticipate that NAV's will continue to grow,** not only for prime assets but now also for more secondary assets. We see the listed market as fairly valued with prospects for normal listed real estate returns of around 8% for the next 12 months, in a base case scenario.

Discount or premium to NAV and NAV growth for the European listed property sector

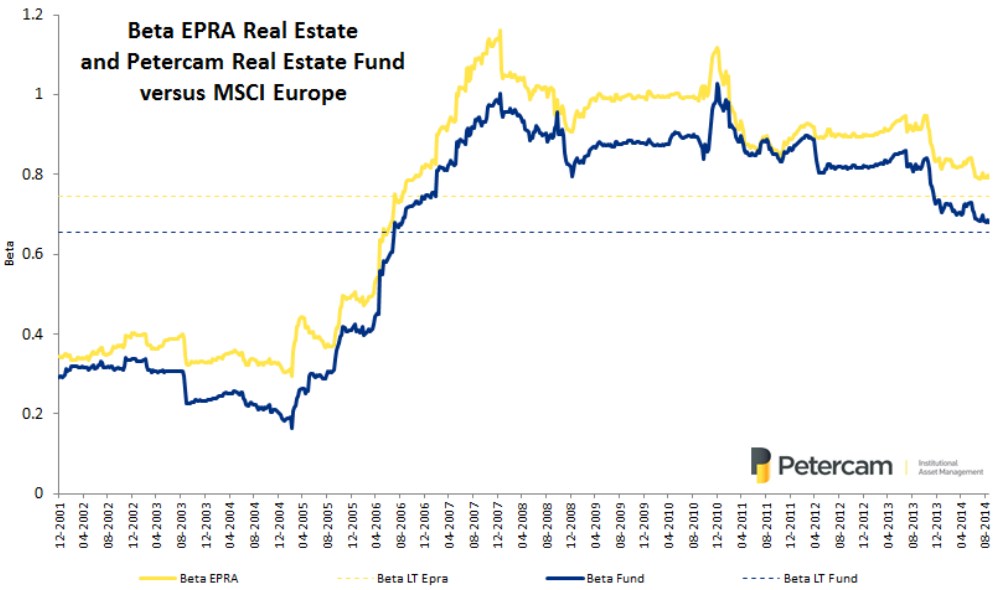


Source: Company date, Datastream, Morgan Stanley Research, Date: 30/9/2014

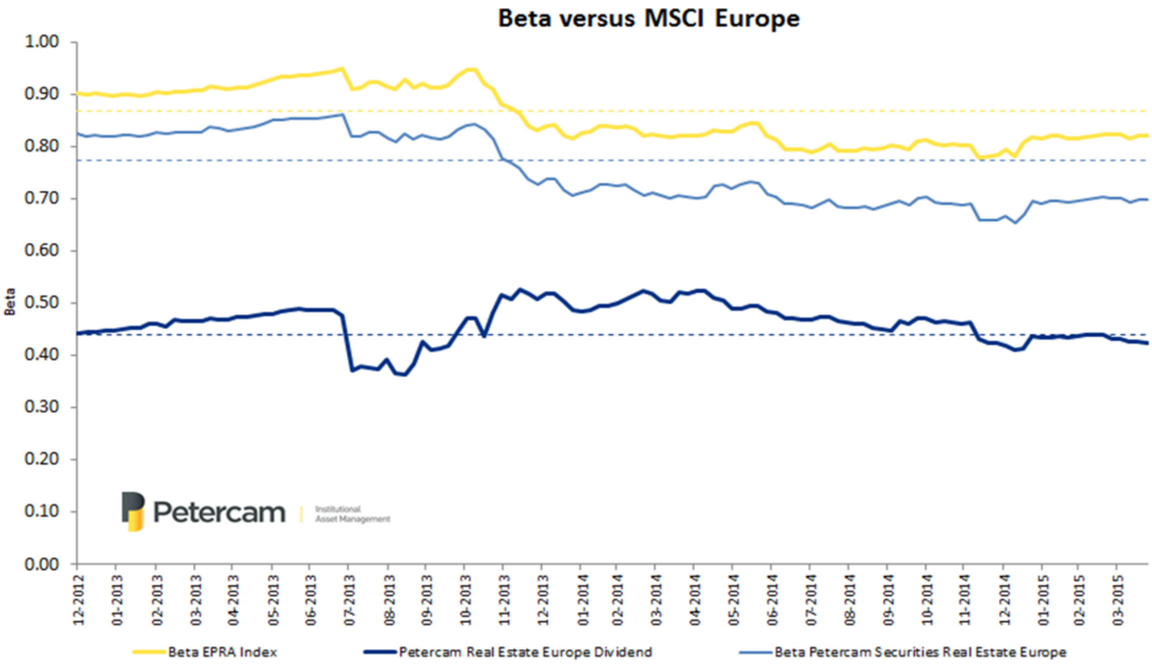
6/ Lower sector volatility

Another key point is the **sharp decline of sector volatility**. Listed real estate's beta compared to that of overall equities has historically averaged 0.60x. In the 2nd half of the 2000 decade, the sector Beta started to shoot up even well above 1x. This was entirely due to the levering up in the sector which initially fuelled NAV growth before witnessing a severe downturn in the 2007-08 crisis. With the deleveraging under way in the sector, volatility has fallen sharply while the sector Beta reverts to historic levels. This makes timing of investing in the asset class much less vital than before.

Long time Beta of Petercam Securities Real Estate Europe (blue) and EPRA Index (yellow) both against MSCI Europe



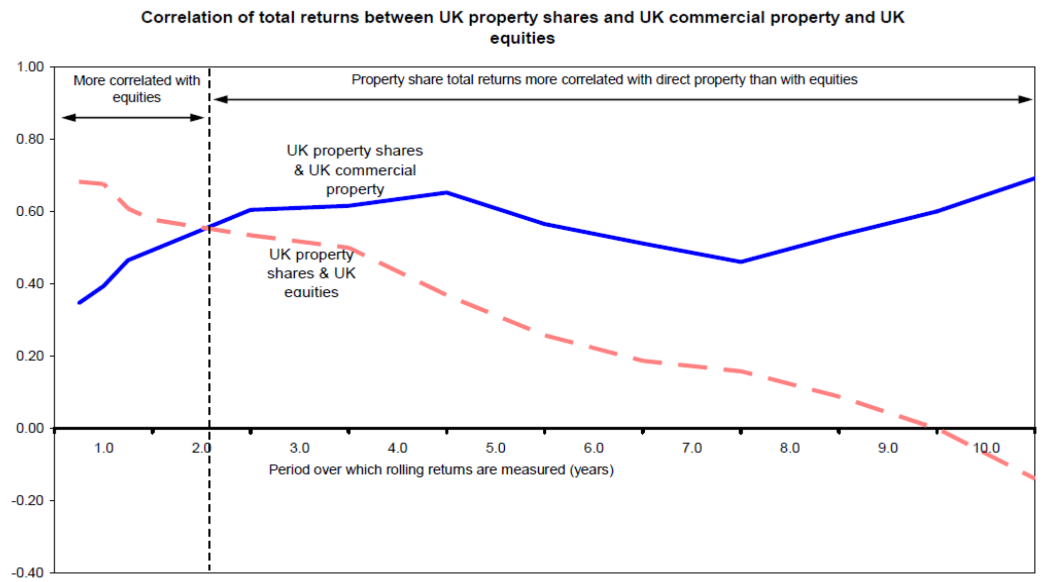
Beta of Petercam funds Securities Real Estate Europe (light blue), Real Estate Europe Dividend (dark blue) and EPRA Index (yellow) all against MSCI Europe



7/ Higher correlation with direct real estate and lower correlation with equities

When analysing returns of listed property we find a **higher correlation with direct real estate**, expressed by the IPD Index (Investment Property Databank) when holding period is longer which is a confirmation of the lower Beta with equities. It also confirms that the fundamental goal of listed real estate - being invested in the alternative asset class real estate but with a higher liquidity and through well managed companies – is achieved.

Property shares make a good proxy for direct property

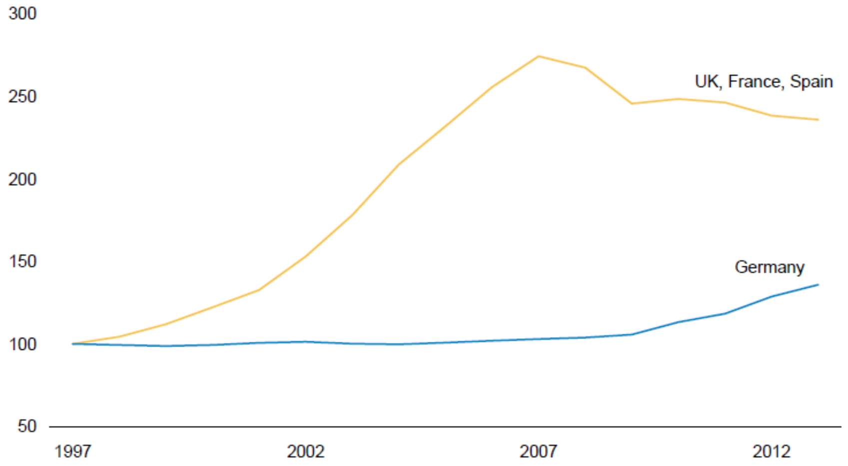


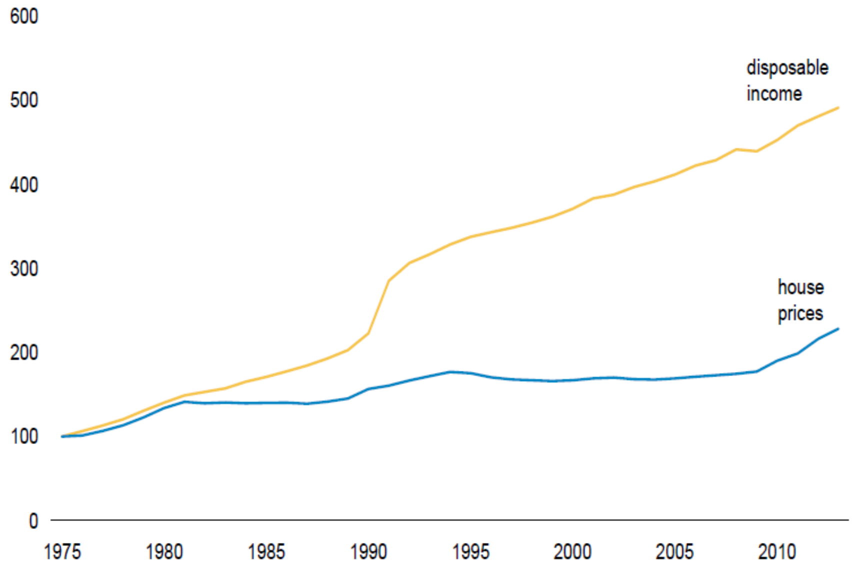
Based on monthly total return data from January 1986 to December 2008
Source: Datastream, IPD, Morgan Stanley Research

8/ Diversification over countries and sub sectors

European listed real estate offers a good diversification to the underlying countries and regions, each with its own macroeconomic picture and also on a subsector level having its own specificities. The companies we invest in are by no means a proxy for the European economy but biased to very local economic drivers. With this universe one can build a portfolio that favours the most attractive combination of macro and micro parameters in order to give investors the best possible risk return combination. As an example we would highlight the German residential sector that is, in our view, an attractive investment theme for the next 10 years.

German house prices and disposable income evolution are the base of an interesting investment theme



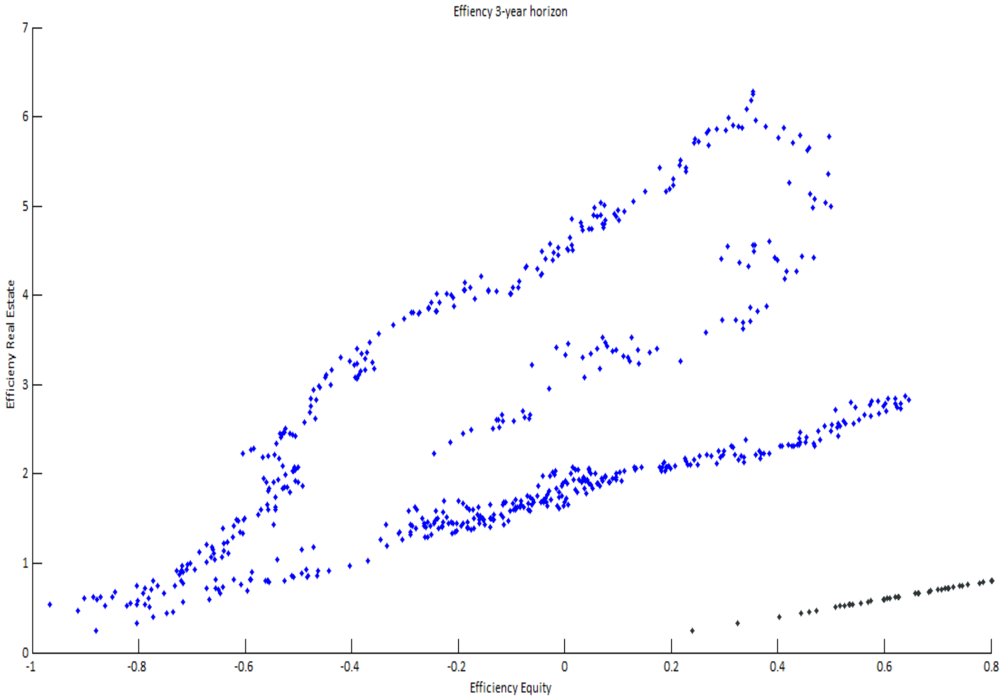


Source: Datastream, Bulwien Gesa, MS Research, Petercam IAM, Date August 2014

9/ Good efficiency (risk return) compared to equities

When measured by units of risk, listed real estate offers a higher efficiency compared to equities. Good visibility on earnings and dividends, fairly stable property yields the advantageous fiscal regime are probably the main reasons that lead to **higher efficiency of the risk taken when investing in listed real estate.**

This is illustrated by dividing the return/risk ratio of listed real estate by the same ratio for equities for 3 year investments for the period end 1995 to now. All of the data points are positive for real estate being left of the 45° line.



10/ Higher efficiency of listed real estate compared to direct real estate

Investors seeking exposure to real estate have to decide whether to invest directly or indirectly through listed property. According to a study of the University of Maastricht in the Netherlands, **returns have been higher and managements cost have been lower for listed real estate** compared to direct real estate for marginally higher volatility.

	All Assets	REITs	Direct RE	Other RA	Internal	External	FoF
Panel A: Gross returns (percent)							
All funds	7.00 [9.41]	10.92 [10.21]	6.70 [8.40]	9.99 [18.57]	7.77 [11.20]	6.82 [9.17]	6.72 [7.85]

	Median	Mean	StDev	# Funds	# Obs
Panel A: Costs in basis points by region					
All funds	67.24	76.19	84.61	662	3815
U.S.	83.48	91.12	90.61	407	2353
Canada	44.97	55.54	51.55	161	1144
Europe	30.31	37.62	33.74	77	259
Aus/Nzd	42.9	44.82	18.79	17	59
Panel B: Costs in basis points by subcategory and investment approach					
REITs	32.75	41.45	57.18	213	917
- Internal	8.35	12.06	14.04	50	286
- External	52.61	62.75	68.37	181	698
Direct real estate	72.47	82.89	100.3	635	3595
- Internal	22.81	31.40	31.63	129	675
- External	78.52	88.09	85.73	567	2941

Source: "Value Added From Money Managers in Private Markets? An Examination of Pension Fund Investments in real Estate" May 2012, University of Maastricht, The Netherlands, based on a survey on the behaviour of 880pension funds over 20 years 1990-2009

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