

Multi Manager Update

November 2009

Enjoy a second bite of the 'property' cherry?

It's not often that you get to enjoy investment performance more than once but that is exactly what the F&C Multi Manager Team are looking to do within a commercial property market widely tipped for recovery. In this update we look at how the Team have already added considerable value through property selections and have recently been locking in gains in a number of top performing positions, and reinvesting the proceeds in property assets that we believe still offer upside potential from here.

Cause for optimism?

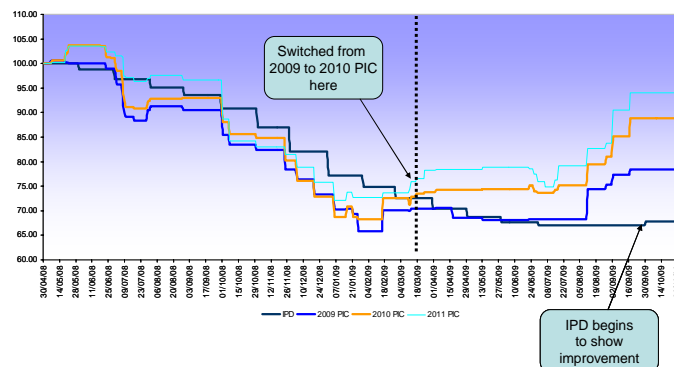
The bursting of the property bubble was painful with the IPD falling over 40% from its peak and many popular property vehicles dropping considerably further than that. More recently there are tentative signs and a growing consensus that property is set to enjoy something of a turnaround in its fortunes. Property funds are once again beginning to enjoy positive inflows as investors see the asset class as an attractive source of income.

The PIC of property

We have been negative on property relative to equity and credit for some time with the portfolio's weighting at the lower end of its historical range for much of 2008 and 2009. Within the asset class wherever possible we rotated away from closed ended property vehicles and focused our property exposure on Property Investment Certificates (PICs). These instruments offer access to property like returns – delivering performance (capital and income) akin to the IPD index over a defined period. Unlike bricks & mortar vehicles, or the IPD itself, which reflects actual property prices, PIC performance is a function of the market's expectation of future returns for property assets.

Tactical trading

A key benefit of PICs is that we can use them to tactically adjust our property exposure as and when we believe it to be appropriate. This contrasts with real 'bricks & mortar' investments where you have to adopt more of a buy and hold mentality. Our preference for PICs within property has added value relative to other property instruments and has accounted for around a third of our outperformance over the course of 2009 as their price increased to reflect upward revisions in expectations for commercial property as an asset class.



Source: Datastream

In mid March this year we switched our 2009 PIC into the 2010 – a lengthening of duration that reflected our view that property was likely to trough during this year and then enjoy some recovery in 2010. With economic data showing some improvement markets have become more optimistic, giving the 2010 PIC a strong uplift.

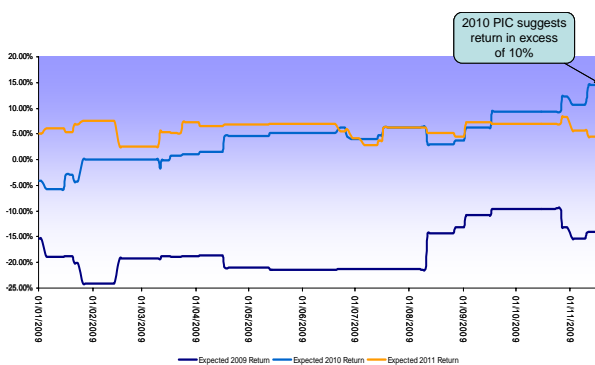
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A second bite of the same cherry?

The current price of the 2010 PIC now reflects an expected return in excess of 10% for the IPD before the end of next year - a situation which suggests to us that much, if not all, of the good news is currently priced in. This in turn leaves little scope for further upside. Real property has also seen some improvement with the IPD generating a positive return during July, August, September and October after a 23 consecutive month losing streak. There remains however, a considerable gap between where property prices currently stand and where investors expect them to be in a year or so.



Source: Datastream

With this in mind we have locked-in our PIC gains and reinvested the proceeds into real 'bricks & mortar' through a new holding of 5% in the SWIP Property Trust within the F&C Multi Manager Distribution portfolio – an open ended vehicle investing in high quality UK commercial property assets across a range of industry sectors. With an experienced team at the helm and plenty of liquidity (cash stood at around 30% of the portfolio in October) we believe that the SWIP Property Trust is well placed to benefit from a broader improvement in the fortunes of commercial property. It boasts an initial yield of 7.9% (historic yield 4%).

Portfolio positioning update

Property now accounts for around 10% of the portfolio's assets and sits within the Alternative portion of the Fund. Whilst the running yields available on property funds such as SWIP are attractive given F&C Multi Manager Distribution's 4.5% target yield, we believe that the total return opportunity for the asset class remains very compelling, on a risk adjusted basis, relative to fixed interest.

Summary

- Property is looking more attractive
- PICs have enjoyed benefit of improving sentiment
- Switch into 'bricks & mortar' offers potential
- Property = yield and total return opportunity

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