F&C UK Real Estate Investments

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Quarter 2 2017

Manager Commentary
Peter Lowe

Total returns for the UK property market as measured by the Investment Property Databank (IPD) Quarterly Universe were 2.4% in the second quarter of 2017. The annual total return improved to 5.6% with capital values up 1.3% over the quarter, moving above their pre referendum level. The income return was 4.7% over the year to June.

The political situation remains complex following the results of both the referendum and the general election, with increased fragility of the government's position leading to greater debate on the options for fiscal policy. The fall of sterling, rise in inflation and the increased growth in consumer credit, alongside relatively stagnant wage growth and a reduction in the savings rate, has led to concerns about the prospect for disposable incomes and consumer spending. Despite unemployment levels being close to record lows, wage growth has failed to respond, with the pace of GDP growth slowing. This position is at odds with the international picture where the economic outlook has been improving, particularly in the US and the Eurozone, where we look set to see monetary tightening in the coming months. The timing and pace of any interest rate rises in the UK is now on the agenda for domestic investors.

Despite the drop off from levels seen in 2012-2015, property investment activity remains above the long term average, though dominated by fewer large transactions and overseas investors buying in central London. Almost half of all Q2 market activity involved foreign buyers. Despite the number of recent specialist REIT launches, institutions generally remain net sellers, with Local Authorities active buyers. In aggregate, inflows to retail funds were modestly positive over the quarter.

The industrial and distribution sectors have continued to drive performance with City offices and central London continuing to demonstrate resilient pricing. Shopping centres and retail warehousing remain out of favour, though with the latter showing some signs of renewed investor interest as the year has worn on. The occupational market has been supported by a lack of supply in many locations however occupiers have proven to be a little more cautious than investors. While there is rental growth across the market as a whole (0.5% over the quarter) this is patchy subject to asset and sector, with the Industrial market and prime offices responsible for the vast majority.

The Company portfolio returned 2.8% over the second quarter, with total returns of 6.6% over the year (outperforming the IPD Quarterly Index of 5.6% over the same period), driven by a top quartile annual income return of 5.9%. Continuing the trend of recent quarters and in line with the market as a whole, the Company's best performing assets originated from the industrial sector. The initial yield on the portfolio is 5.4% and the average weighted unexpired lease term is c. 7 years. The portfolio remains well balanced both geographically and by sector split, with a 60% weighting to the South East, and just over 30% exposure to Industrials (all located within the South East) by sector.

The Company completed on the sale of the shop units at 41-49 Linthorpe Road, Middlesbrough during the quarter, continuing the policy of non-core asset disposals. No properties were purchased over the year; however post period the Company has exchanged contracts for the purchase of a south east located industrial asset, single let to a strong financial covenant for 9 years, at a price of £9.56m reflecting a yield of c.5.2%.

The yield gap between the All Property income return and the risk free rate narrowed slightly over the quarter as gilt yields edged higher but it remains well above the long term average. Long term secure income and Alternatives remain in favour as do industrial and logistics assets. Despite the general election result and continued geo-political uncertainty, UK commercial property has continued to deliver positive performance, driven by income, and supported by low interest rates, performance buoyed by a weight of money from a range of prospective purchasers.

Key facts

Trust aims: To provide ordinary shareholders with an attractive level of income with the potential for income and capital growth from investing in a diversified UK commercial property portfolio.

Fund type: Investment Trust

Launch date: 1 June 2004

Total assets: £346.25 million

Share price: 106.75p

NAV*: 100.06p

Discount/Premium (-/+): 6.69%

Dividend payment dates: Mar, Jun, Sep, Dec

Net dividend yield †: 4.68%

Net gearing:** 137.37%

Vacant property: 5.58%

Weighted average lease length: 6.57 years

Management fee rate*:** 0.60%

Ongoing charges**:** 1.30%

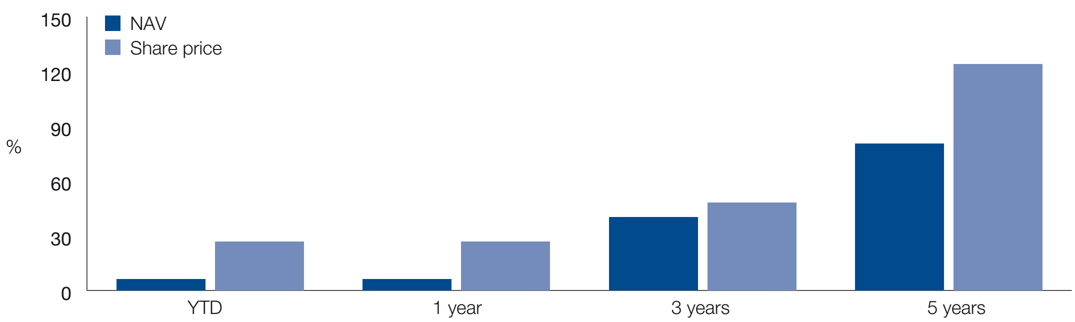
Year end: 30 June

Sector: Property Direct - UK

Currency: Sterling

Website:
www.fcre.co.uk
www.fcre.gg

Fund performance



Cumulative performance (%) as at 30.06.17

	3 Months	Year to date	1 Year	3 Years	5 Years
NAV	3.1	6.1	6.1	40.1	80.4
Share price	6.4	26.8	26.8	48.1	124.0

Discrete annual performance (%) as at 30.06.17

	2017	2016	2015	2014	2013
NAV	6.1	7.5	22.7	23.9	3.9
Share price	26.8	-6.5	24.9	23.2	22.8

Source: Lipper and F&C. Basis: Percentage growth, total return, bid to bid price with net income reinvested in sterling. Basis in accordance with the regulations of the Financial Conduct Authority. Past performance is not a guide to future performance. Values may fall as well as rise and investors may not get back the full amount invested. Income from investments may fluctuate. Income payments may constitute a return of capital in whole or in part. Income may be achieved by foregoing future capital growth.

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Trust codes

Sedol	
FCRE - GBP	B012T52

Top 10 property investments (%)

London W1, 14 Berkeley Street	7.7
Banbury, 3663 Unit, Echo Park	6.6
Colnbrook, Units 1-8 Lakeside Road	5.5
Eastleigh, Southampton International Park	4.6
Hemel Hempstead, Hemel Gateway	4.3
York, Clifton Moor Gate	3.7
Rotherham, Northfields Retail Park	3.2
Leamington Spa, 30-40 The Parade & 47/59a Warwick Street	3.1
Bracknell, 1/2 Network, Eastern Road	3.1
Edinburgh, 1-2 Lochside Way, Edinburgh Park	2.9
Total	**44.7**

Sector breakdown

Geographical breakdown

Net dividend distributions pence per share

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
March	1.80	1.80	1.80	1.80	1.80	1.80	1.25	1.25	1.25	1.25
June	1.80	1.80	1.80	1.80	1.80	1.80	1.25	1.25	1.25	1.25
September	1.80	1.80	1.80	1.80	1.80	1.25	1.25	1.25	1.25	
December	1.80	1.80	1.80	1.80	1.80	1.25	1.25	1.25	1.25	
Total	7.20	7.20	7.20	7.20	7.20	6.10	5.00	5.00	5.00	2.50

Structure

At launch on 1 June 2004, the Company had a capital structure comprising approximately 60 per cent Ordinary Shares and 40 per cent bank debt.

Ordinary shareholders are entitled to all dividends declared by the Company and to all the Company's assets after repayment of its borrowings. As at 30 June 2017, borrowings consisted of loans drawn down of £106 million: £90 million fixed term facility from Canada Life due to expire in November 2026 and £16 million of the revolving credit facility from Barclays due to expire in November 2020. The weighted average interest rate on the Group's current borrowings is 3.2%.

Past performance is not a guide to future performance. The value of property related securities are likely to reflect valuations determined by professional valuers. Such valuations are the opinion of valuers at a particular point in time and are likely to be revised and movements may cause the value of investments and the income from them to fall as well as rise and investors may not get back the amount originally invested. Property and property related assets can sometimes be illiquid. A fund investing in a specific country carries a greater risk than a fund diversified across a range of countries. If markets fall, gearing can magnify the negative impact on performance.

All data as at 30.06.17 unless otherwise stated.
All information is sourced from F&C unless otherwise stated. * The NAV is calculated under International Financial Reporting Standards. † Calculated with reference to projected annual dividends of 5.0 pence per share. ** Bank Debt (less net current assets) divided by investment properties. *** Please refer to the latest annual report as to how the fee is structured. **** Ongoing charges are total expenses (excluding direct property expenses) as a percentage of net assets. The share price may either be below (at a discount) or above (at a premium) the NAV. Discounts and premiums vary continuously. Performance information excludes any product charges which can be found in the Key Features document for the relevant product. The factsheet is issued and approved by F&C Management Limited authorised and regulated in the UK by the Financial Conduct Authority. CM11408

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