For Investment Professionals only

M&G Real Estate UK Enhanced Value Fund

Fund profile

Q1 2019

The value of investments will fluctuate, which will cause fund prices to fall as well as rise and you may not get back the original amount you invested. There is no guarantee the fund objective will be achieved.

Fund facts

Fund manager
Paul Crosbie

First close
29 January 2018

Sponsor co-investment
£45m

Alignment of fund manager
Yes

Subsequent closings
Through 2019

Structure
Scottish limited partnership

Status
Closed-end; seven-year term

Investment style
Value-add

Target equity
£250m

Target leverage
50% LTV across the portfolio

Target returns[1]
12%+ IRR gross
10%+ IRR net
Equity multiple 1.6x

Management fee
1.25% pa on invested capital

Carried interest
20% over 9%

Risks associated with this fund

- The fund is a closed ended fund with a seven year term which may be extended. Investors are advised to refer to the fund's Private Placement Memorandum for further details, but investments in the fund are likely to be illiquid, other than when periodic distributions are made by the fund.
- Real estate values can be affected by a number of factors beyond the fund's control and may be subject to long-term cyclical trends that can give rise to volatility in values.
- Please note this is not an exhaustive list, you should ensure you understand the risk profile of the products or services you plan to purchase.

Why invest in M&G Real Estate UK Enhanced Value Fund

At a time of record low bond yields and diminishing core real estate returns, forecast to be 4.3% per annum over the next five years[2], the case for investing in a value-add strategy backed by a strong component of income, we believe, is compelling.

The fund has assembled a diversified, income producing portfolio with a capital value of £111m. The portfolio has ten assets and has:

- A high allocation to offices focused on supply-constrained city centres, set to benefit from the macro-economic trends of urbanisation, connectivity and regeneration;
- An exposure to the mid-box logistics submarket, set to benefit from increasing occupational demand due to the continued growth of e-commerce; and
- An active asset management programme to enhance income and reposition assets to core ahead of disposal.

The fund has a three-year investment window to take full advantage of any further dislocation in pricing as we move through the Brexit process.

Investment objective

To deliver a target IRR[3] of 10%+ net of fees through a value-oriented investment strategy across the primary UK real estate markets.

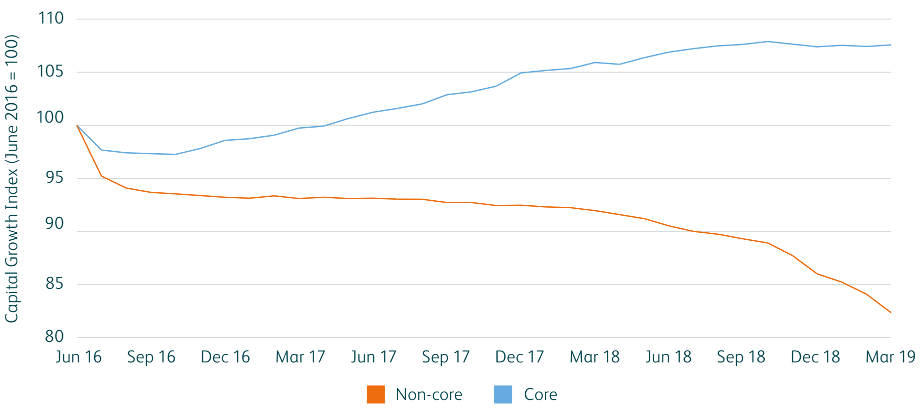
Investment strategy

Heightened risk aversion during Brexit uncertainty is creating a divergence of pricing between core and non-core real estate. Consequently, there is a cyclical buying opportunity for experienced investors. The fundamental demand/supply imbalance across the occupational markets supports the case for taking income risk, whether it be day–one vacancy or near term lease expiries.

We strongly believe that by targeting fundamentally well–located non-core assets we can:

- Actively asset manage to add income, extend lease term and enhance capital value; and
- Dispose of an enhanced asset into an improved economic and market condition.

Divergence of pricing between core and non-core



Source: CBRE valuation data, indexed to the date of the EU referendum (June 2016), to March 2019.

[1]Targeted returns are based on subjective assumptions and circumstances and there can be no assurance that the fund will be able to achieve its objective.
[2]Source: MSCI Annual Index, M&G Real Estate forecast as at 31 March 2019. Index comprises institutionally owned stock weighted towards core real estate.
[3]This is a forecast return to investors net of all property costs and fund expenses. There is no guarantee the fund objective will be achieved.

Portfolio overview[4]

Portfolio value
£111m

Number of assets
10

Average asset size
£11.1m

Estimated rental value
£8.3m

Occupancy rate
88.4%

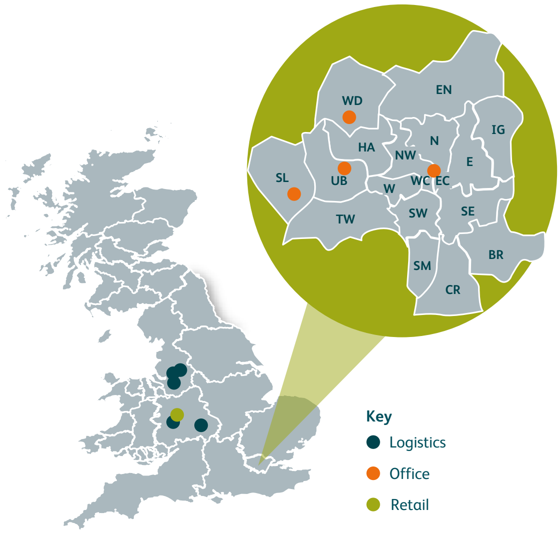
Number of tenants
27

Geographic weight[4]

Greater London:	38%
North West:	14%
South East:	27%
West Midlands:	21%

Sector weights[4]

Logistics:	22%
Office:	65%
Retail:	14%



Active management in action:
Gate House, 1 St John's Square, Clerkenwell

Multi-let office situated in St John's Square, a prime location within Clerkenwell, London. The area is popular with a diverse range of tenants including fashion, architecture, technology and design. Connectivity will be improved significantly with the opening of Crossrail in 2019, reducing journey times from west to east. Farringdon station is within five minutes' walk. A number of nearby office buildings have undergone redevelopment and conversion to higher alternative uses, namely hotels and residential. This has kept office supply levels constrained and maintained upward pressure on rents. Gate House offers an exciting opportunity to improve the overall appearance through the application of capex and increase the floor area at the upper levels by extending the third to sixth floors using currently redundant terracing.

Gate House, 1 St John's Square, Clerkenwell

Mispricing of risk:
Pebble Logistics Portfolio, various locations

A portfolio of five mid-box logistics buildings, comprising seven units and a total of 302,365 sq ft of logistics accommodation spread across established locations in the North West and West Midlands. There is strong forecasted growth in the mid-box sector driven by increasing occupational demand and limited levels of supply. The portfolio is well-placed to capture this growth. High build costs for units of this size, combined with current rental unviability to justify new development, further compounds the lack of supply. Less competition in this target lot size range results in more attractive relative pricing and returns. There is an opportunity to take advantage of upcoming lease events to drive rental tone on a number of assets and increase the average lease length through lease re-gearing.

Units 202/204, Stonebridge Cross, Droitwich

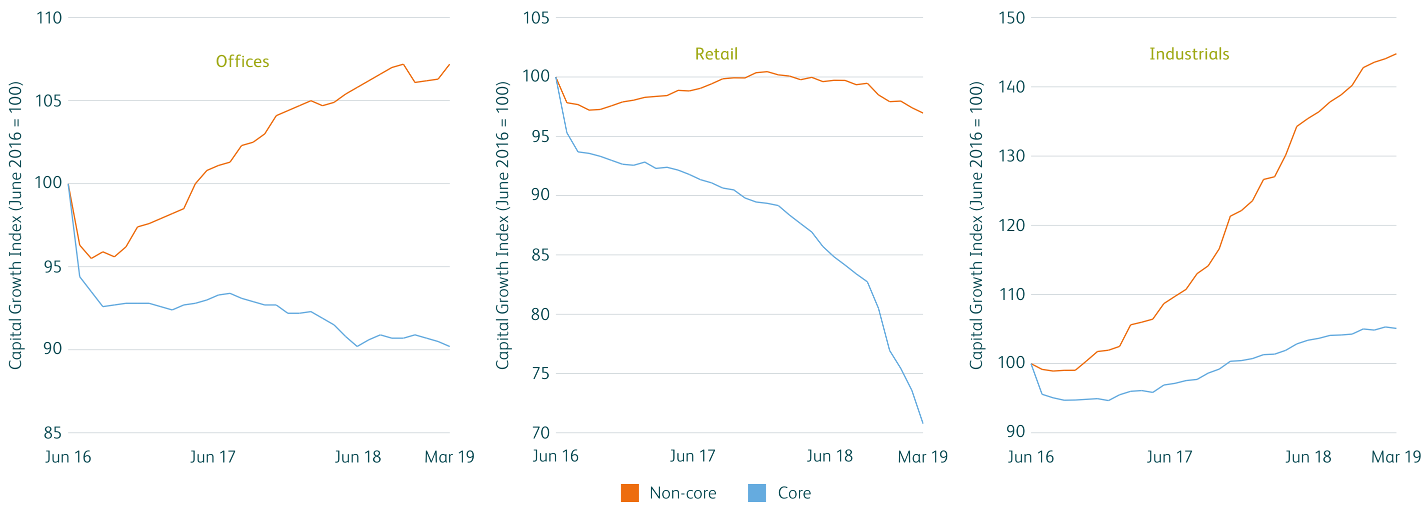
May not add up exactly to 100% due to rounding effects.
[4]Source: M&G Real Estate, as at 31 March 2019.

Outlook

Brexit negotiations and the resulting uncertainty continue to weigh heavily on investor sentiment and decision making. Investors remain firmly focused on core real estate, with the divergence between pricing of core and non-core assets widening. Despite this heightened level of risk aversion, transaction activity in all sectors, with the exception of retail, is still running above trend. The UK recorded £58 billion of investment volumes on a rolling annual basis to Q1 2019, well above its long run average. With the scope for further yield compression now limited however, core real estate returns have been slowing, with MSCI's All Property annual index returning just 6.0% in 2018, with income the key driver. M&G Real Estate's house view forecast for total returns over the next five years is for further softening, estimating 4.3% per annum during this period. This creates a unique window of opportunity for a value-add approach, to pursue a target return of 10% per annum through selectively acquiring mispriced real estate, enhancing the income profile and repositioning these assets to core through an active asset management programme.

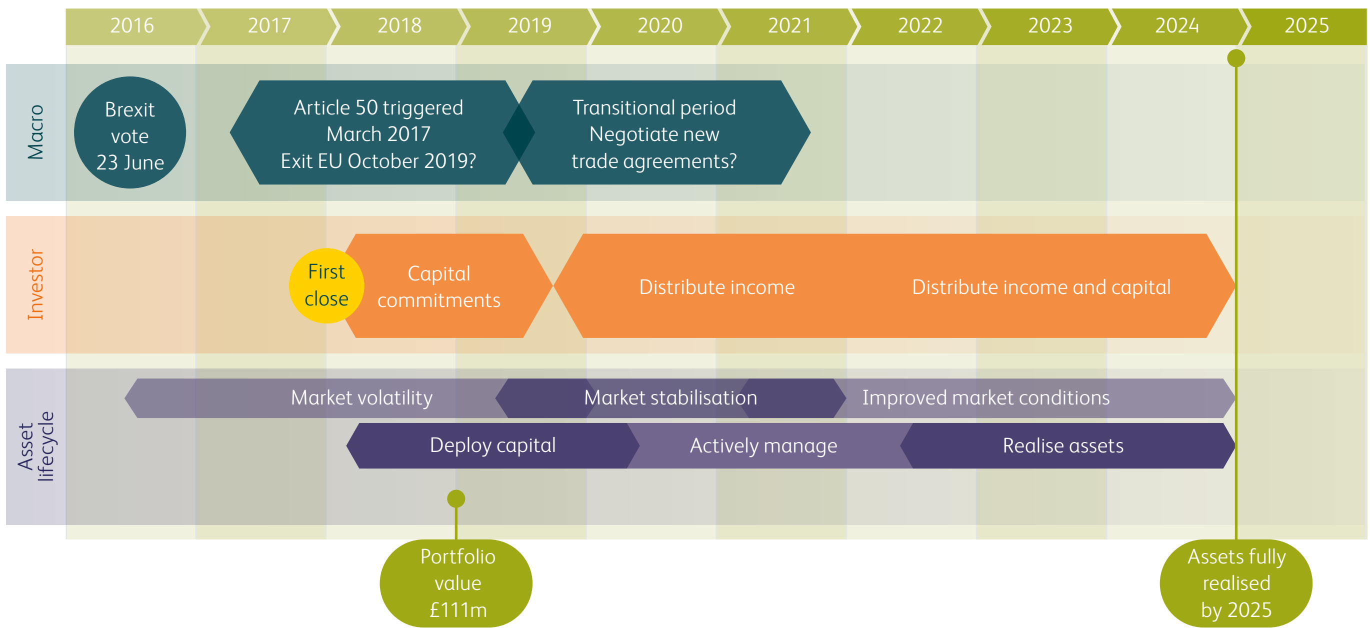
Underlying all this, the UK economy and the real estate occupational markets are holding firm. GDP increased by 0.3% in the three months to November 2018, with consensus economic forecasts expecting moderate growth of 1.3% for 2018, before picking up slightly to 1.5% over 2019-20. Employment in the UK reached a record high in November at 75.8%, with wages now growing at the fastest level in over a decade. Against this backdrop, the occupational markets remain broadly positive, particularly for the logistics and office sectors. Both markets are characterised by a shortage of good quality, modern accommodation and continued business investment. We expect this to be supportive of robust levels of rental growth over the medium term. The lack of development activity across the sectors for the past ten years has severely restricted supply levels; vacancy levels are at historic lows for Grade A quality space in the 'Big 6'/regional office markets and multi-let logistics space in the small to mid-box market. This provides us with the confidence to target well located real estate with either day one vacancy or near-term lease expiries that can be repositioned and upgraded through the application of asset management and capital expenditure.

CBRE Property Valuation Capital Growth, Index June 16 = 100



Source: M&G Real Estate, CBRE, data to March 2019.

Targeted investment timeline



Key UK stats

£22.3 billion
invested in over 775 assets[1]

£2.1 billion
total construction value[2]

c.3,790
leases managed[3]

c.925
lease events in 2018

Source: M&G Real Estate, [1]As at 31 March 2019 unless otherwise stated.

[2]Construction value of pre-construction and on-site developments, but excl. St Edwards JV.

[3]Excludes externally managed real estate.

Strong market knowledge, access and resource

M&G Real Estate is a specialist real estate investor headquartered in London with £33.1 billion of assets under management including cash (31 March 2019). We invest in all major sectors across the UK, continental Europe, North America and Asia Pacific.

Fund manager

Paul Crosbie

Paul is responsible for delivering the overall strategy and performance, and overseeing the investment team to meet the fund's objectives. Paul joined M&G Real Estate in 2015 as head of the Industrial & Logistics team. With responsibility for £2.5 billion of industrial assets, the team successfully transacted c.£300 million of assets under Paul's leadership, including the development of some 1.5 million sq ft. Paul has over 20 years' industry experience. Before joining M&G, he worked at Rockspring in a fund management and asset management capacity across a range of their property funds. Prior to this, Paul worked at CBRE both in London and Dubai, focusing on investment valuations and development across all sectors. Paul graduated with a BSc (Hons) in Land Management from the University of Portsmouth. He is a member of the Royal Institution of Chartered Surveyors and the Investment Property Forum.

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