M&G European Property Fund

Fund profile

Q2 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 will achieve its objective.

Key quarter-end figures

Gross asset value (GAV)
€3,570m

Net asset value (NAV)
€2,805m

Leverage as % of GAV
14.7%

Cash as % of NAV
2.3%*

*Average balance over quarter

Fund details

Fund manager
David Jackson

Deputy fund manager
Simon Ellis

Launch date
4 October 2006

Fund structure
Luxembourg SICAV-FIS

Status
Open-ended

Investment style
Core

Denomination
Euro

Valuations
Monthly

Dealing days
Monthly

Financial year end
31 July

Initial minimum Subscription
C and D shares: €2.5 million
X and Y shares: €25 million
E and V shares: €100 million
F and W shares: €200 million

Changes in currency exchange rates will affect the value of your investment.

Source: M&G Real Estate as at 30 June 2019. Performance is net of fees.

Risks associated with this fund

- Where market conditions make it hard to sell the fund's investments at a fair price to meet investors' sale requests, we may temporarily suspend dealing in the fund's shares.
- 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.
- Changes in currency exchange rates will affect the value of your investment.
- Further information about the risks that apply when investing can be found in the fund's prospectus.

Why invest in the M&G European Property Fund

The case for investing in core real estate across continental Europe is backed by the current strength of the occupier markets and our expectation for all property rental growth of 2.0% per annum over the next three years. Rental growth and income will drive returns in the medium term. Furthermore opportunities exist in supply constrained office markets as well as sectors offering structural opportunities such as residential and elderly care.

- A defensive diversified core portfolio of 72 assets across 12 countries (with no UK exposure).
- High allocation to the office sector, focused on core CBD (Central Business District) and edge of CBD locations, which is set to benefit from the accelerating economic recovery.
- A consistent and stable net income return.
- Moderate leverage; long-term target of 20-25%.
- Strong deployment track record; €907m of new acquisitions completed in 2018/19.

Investment objective

To invest in European markets to optimise long-term total return (the combination of income and growth of capital), primarily through investment in real estate investments.

Investment strategy

To invest in a diversified portfolio of commercial real estate in Europe seeking to add value through strategic asset allocation, stock selection and asset management. The principal real estate sectors in which the fund will invest are offices, retail, logistics and alternatives including mixed-use, residential and hotels/leisure.

Fund performance

Annualised performance	Current quarter	1 Year	3 years	5 years	10 years
Fund	0.8%	6.3%	6.5%	7.1%	5.4%

12 months to 30 June	2019	2018	2017	2016	2015
Fund	6.3%	5.5%	7.7%	8.6%	7.4%

Past performance is not a guide to future performance.

Portfolio overview

No. of investments
72

Average investment size
€45.4m

Estimate Rental Value (ERV)
€175.1m

Occupancy rate
96.3%

Weighted average lease terms (WALT)
7.3 years including breaks
6.1 years excluding breaks

No. of tenants
503

Net property yield
4.3%

GRESB 2018

Awarded a GRESB green star score of 80/100 versus a peer average of 69/100.

Fund commentary

During Q2 the fund recorded a total return of 0.78%, comprising an income return of 0.74% and a capital return of 0.05%. To this end, the fund continues to deliver a consistent income return of 3.33%, from a total return of 6.30% for the 12 months to 30 June.

In line with the fund's strategy of focussing on core Central Business District (CBD) offices, the fund completed the acquisition of an off-market freehold office building in the prime Milan CBD with a total commitment of €136m, reflecting a capital value of c.€9,400 per sqm.

As the fund looks to increase exposure to modern logistics assets, capitalising on the structural evolution of the sector driven by e-commerce, two logistics assets were purchased during the quarter for a combined purchase price of €50.6m.

The second quarter of 2019 saw much leasing activity within the portfolio, further enhancing the income profile of the fund. The French asset management team secured two key lease renewals at the recently acquired office buildings in Brussels, Avenue de Cortenbergh and Chaussée de Charleroi. This increased rental income from one tenant by 63% and 5% for the building. In addition the team also secured a prolongation of an existing lease at the Le Val Saint Quentin business park in Paris.

Two new lettings were signed at the Databankweg office building in Amersfoort significantly reducing the vacancy in the building from 77% to 52%.

Furthermore, we continue to raise capital and diversify the fund's investor base. Following a draw down post quarter end the fund's queue is €175m. We now anticipate draw down of new capital within six months.

Past performance is not a guide to future performance.

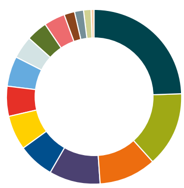
Top 10 assets

Investments	City/town	Region	Sector	% of portfolio
Blekholmen	Stockholm	Sweden	Office	7.2
Calle de Rios Rosas 26	Madrid	Spain	Office	6.9
LuisenForum	Wiesbaden	Germany	Shopping centre	4.0
Rue de Verdun 31-33	Greater Paris	France	Office	4.0
Alvar Aallon katu 3	Helsinki	Finland	Office	3.5
Market Central Da Vinci	Rome	Italy	Big-box retail	3.3
Badensche Straβe 23/24	Berlin	Germany	Office	3.2
Via Torino	Milan	Italy	High street retail	2.8
Rue de Rennes	Paris	France	High street retail	2.8
Kalvebod Brygge 47	Copenhagen	Denmark	Office	2.7

Sector weightings – by value*

Geographical weightings – by value*

Rental income – by group*



*Numbers may not sum due to rounding.
Source for all data unless otherwise stated, M&G Real Estate, as at 30 June 2019.

Transaction and development activity

The fund completed the acquisition of an off-market freehold office building in the prime Milan CBD with a total commitment of €136m. The first phase has been acquired for a total of €43.1m and the second phase exchanged with completion expected at the end of Q3 2019. Centrally located in Porta Nuova, the 16,500 sqm building is currently undergoing a high specification two phase refurbishment. The LEED gold-certified building benefits from excellent public transport links within ten minutes' walk of both Central and Garibaldi railway stations and is 83% let to tenants including Regus, WillisTowersWatson and Munich RE with a 30-month rental guarantee.

The fund acquired a newly built freehold logistics platform comprising two warehouses in a well-established strategic location of Getafe, Madrid for €32.6m. The 29,537 sqm LEED silver-rated platform is located in the prime 'first-ring' location of Getafe, one of the most important highways for distribution in Spain. Originally acquired with 16% vacancy the asset management team have reduced the vacancy to 8.5%. The warehouse is let to three tenants: food operator Mercadona, and logistic operators ADER and ATDL.

In addition, the fund acquired a modern freehold logistics unit in Brunna Logistics Park a well-established location of North-West Stockholm for €18m. The warehouse benefits from excellent distribution access along the E18 highway which connects Oslo and Stockholm. Constructed in 2018, the 12,811 sqm warehouse is let to three tenants on long-term leases; Orrvelin Group, Cosentino Scandinavia AB and Engelmanns Sweden AB with a WALT of 13 years.

Asset management activity

During the quarter, the team secured a lease renewal with German foundation, Friedrich Naumann at the Avenue De Cortenbergh office building in Brussels. They have taken a new nine-year lease at an annual rent of €128,707, which is 18% above ERV. Additionally within the building, terms have been agreed with European Security Body, Coreso to take a further 391 sqm which will expand their occupation to 1,726 sqm.

Furthermore, the team secured a prolongation of the current lease with American technology company Xilinx at the Le Val Saint Quentin business park in Paris. Xilinx have been moved within the Park in order to improve the marketability of the vacant buildings, and, at the same time, extended their lease on a 3,6,9-year basis at a headline rent of €88,774.

At the Data Club Offices building in Amersfoort, two significant lettings have been signed which will significantly reduce the vacancy in the asset to close to 50%. Bailiff company, Bosfeld has taken an eight-year lease on 1,540 sqm whilst construction company Heijmans has taken a five-year lease on 2,418 sqm.

At the LuisenForum shopping centre in Wiesbaden, the team secured three new leases. All three tenants have taken 10-year leases with a range of break options at 3,5 and 7 years all at rents above ERV.

Market outlook

Economic overview

Despite a pick-up in quarterly GDP growth across the Eurozone in Q1 (0.4% vs 0.2% in Q2 2018), the consensus expects the region to grow at a modest rate of 1.4% pa over 2019 and 2020. The strongest quarterly growth gains were seen in Germany and Italy (+0.4% and +0.2% respectively).

Labour markets continue to look strong with unemployment in the Eurozone currently at its lowest rate for a decade (7.5%). Although Germany's unemployment rate has remained stable at 5% for the last three quarters, suggesting that labour shortages have levelled off[1]. This trend is reflected across the wider region with Eurozone hiring intentions slowing.

The European Union appointed Christine Lagarde as president of the European Central Bank. Ms Lagarde has generally supported negative interest rates and asset purchases. Thus, the consensus expects further interest rate cuts and quantitative easing to counter an economic slowdown and bolster inflation up to the bank's target rate of 2%. Until such time, upward pressure on government bond yields is likely to be subdued, thus continuing to highlight European property as an attractive asset class.

Property overview

On the supply side, the volume of completions across the Eurozone is expected to rise this year and next. However taking into account withdrawals, this is not expected to lead to an oversupply of office space. Opportunities remain in supply-constrained CBDs with exceptionally lower vacancy rates compared to the wider city including Milan, Barcelona and Stockholm[2]. Germany produced the strongest office rental growth across the region in Q2 led by Berlin (4.4% q-o-q). Conversely the rate of job creation in Spain is expected to outperform the Eurozone. This was reflected in the Q2 q-o-q prime office rental growth figures for both Barcelona (2.9%), and Madrid (2.1%)[3].

Relatively more European logistics markets saw q-o-q rental growth in Q2 driven by e-commerce and supply-chain rationalisation by retailers. Warsaw saw positive growth of 2.8% q-o-q for the first time since 2010.

Several retail shop, office and logistics markets recorded healthy inward yield movements over the quarter of up to 10bps in the retail shop sector (Lyon) and 25bps in the office sector (Lisbon and Paris). A broader, albeit modest evidence of yield compression across all European markets was seen in the logistics sector (up to -10bps in Spain, Germany and The Netherlands).

In Spain, housing prices are rising due to a national supply shortage according to CBRE (18.4% y-o-y in 2017). The market imbalance is more acute in Madrid and Barcelona. The Spanish Private Rented Sector (PRS) market is becoming more professional. In 2017 alone, 19 new PRS SOCIMIs were launched on the alternative stock exchange.

In summary, while we expect rental growth to moderate across the Eurozone, low vacancy and limited pipelines mean that rents will hold. Our expectation is for all property rental growth to average 2.0% pa over the next three years[4]. Opportunities can be found in supply constrained markets as well as in sectors offering structural opportunity such as residential and elderly care.

[1] Source: Bloomberg, Q2 2019.
[2] Source: PMA, April 2019.
[3] Source: JLL, Q2 2019.

About us

M&G Real Estate, the property fund management arm of M&G, is a specialist investor in all major real estate sectors across the globe. We focus on generating long-term, income driven returns through active management and offer institutional investors exposure to real estate through both pooled vehicles and segregated mandates.

- £33.5 billion of assets under management incl. cash (as at 30 June 2019)
- Top-30 global real estate investor*
- Responsible for managing property investments for over 260 institutional investors
- Invested in over 960 properties across 29 countries
- £6.5 billion of transactions completed globally in 2018-2019 Q2.

We also have a dedicated Responsible Property Investment team that enables us to respond to the growing range of environmental and social issues that can impact property values. Nine of our funds (including the M&G European Property Fund) have been awarded Green Stars in the 2018 Global Real Estate Sustainability Benchmark (GRESB) Survey – meaning they are amongst the most highly-ranked for sustainability globally.

Fund manager profiles

David takes the lead in strategy formation, as well as overseeing the management of the investment team. Since joining M&G Real Estate's parent company, Prudential Plc., in 1978 he has undertaken a variety of investment, asset, and fund management roles in global real estate. He has been part of M&G Real Estate's fund management team since 1991. David is a member of the Royal Institution of Chartered Surveyors (RICS), the Investment Property Forum, and the European Association for Investors in Non-listed Real Estate (INREV). He also sits on the board of the Association of Foreign Investors in Real Estate.

Simon is the deputy fund manager. He has worked on the fund since inception and is responsible for property investment and real estate asset management in continental Europe. Prior to joining M&G Real Estate in 2004, Simon worked in the investment field at King Sturge and CBRE, including a year in their Paris office. Simon is a member of RICS and has an MSc in Land Management from the University of Reading. He is fluent in French.

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*Global real estate ranking according to PFR/IREI Global Real Estate Investment Manager Report 2018.

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