

For investment professionals only



## UK Commercial Property

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September 2018

# M&G Property Portfolio

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## Risks associated with this fund

The value of investments and the income from them will rise and fall. This will cause the fund price, as well as any income paid by the fund, to fall as well as rise. There is no guarantee the fund will achieve its objective, and you may not get back the amount you originally invested.

The fund is valued daily on both an 'offer' basis (how much its assets would cost to buy) and a 'bid' basis (how much the fund would receive if assets were sold). The difference between the two is known as the 'spread', which is currently around 6.25%.

The fund invests mainly in one type of asset. It is therefore more vulnerable to market changes for that specific type of asset. This type of fund can carry a higher risk and can experience bigger price gains and falls when compared to a fund which invests in more types of assets.

If significant numbers of investors withdraw their investments from the fund at the same time, the manager may be forced to dispose of property investments. This may result in less than favourable prices being obtained in the market for those investments.

Property valuations are provided by an independent valuer and are subject to the judgement of the valuer.

Where market conditions make it hard to sell the fund's investments at a fair price to meet customers' sale requests, we may temporarily suspend dealing in the fund's shares.

The fund manager will place transactions, hold investments and place cash on deposit with a range of counterparties (opposite parties). There is a risk that counterparties or tenants of properties may default (fail to pay) on their obligations or become insolvent.

All of the above risks could have an adverse effect on the value of your investment.

For any performance shown, please note that past performance is not a guide to future performance.

# Agenda

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Lay of the land

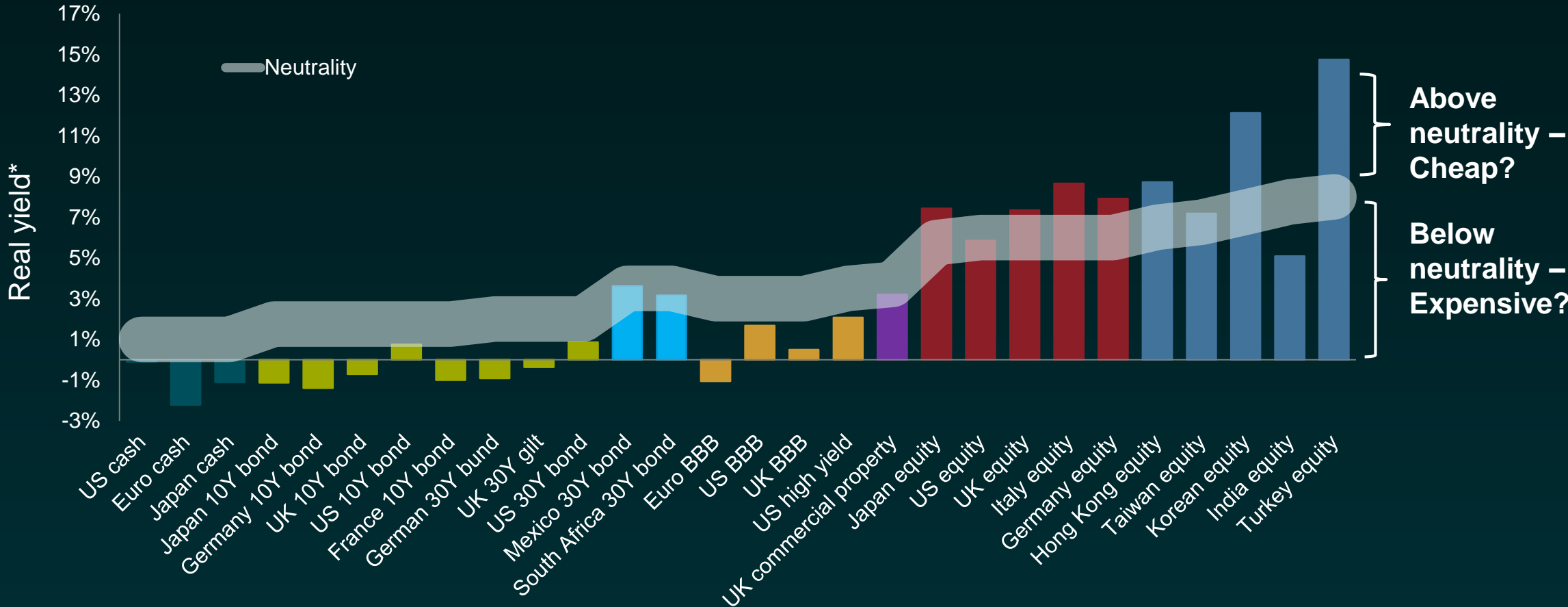
Sector views

Fund update

# Lay of the land - an objective view

## Multi-Asset team valuation framework

Sample of assets, showing real yield against an assessment of neutrality

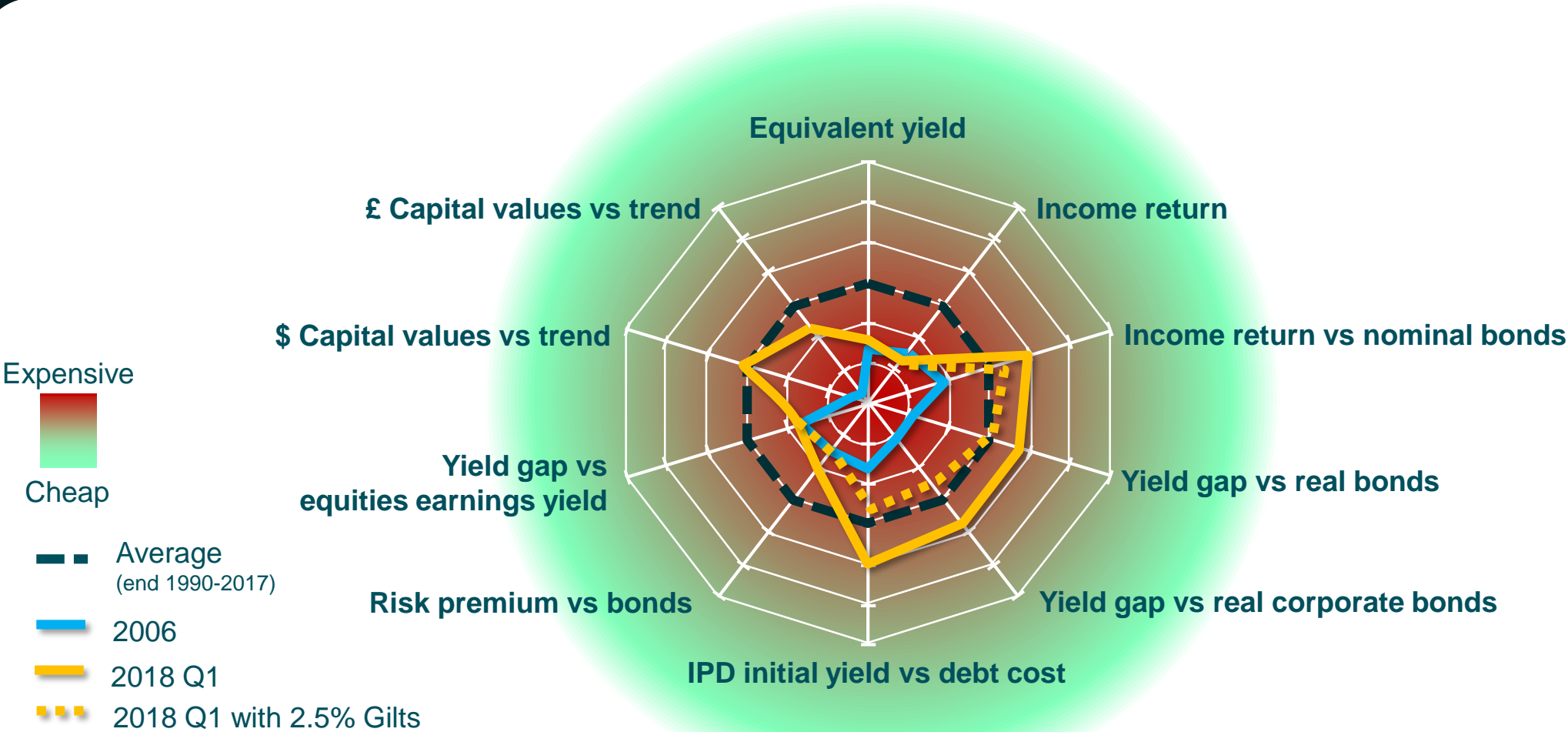


## Fair value, so what are the risks?

Source: M&G, Thomson Reuters Datastream, 31 July 2018. \*Real yield for equity is defined as an inflation-adjusted inverted p/e ratio, using forward consensus data

# Risk 1: rising bond yields

## Relative attractiveness

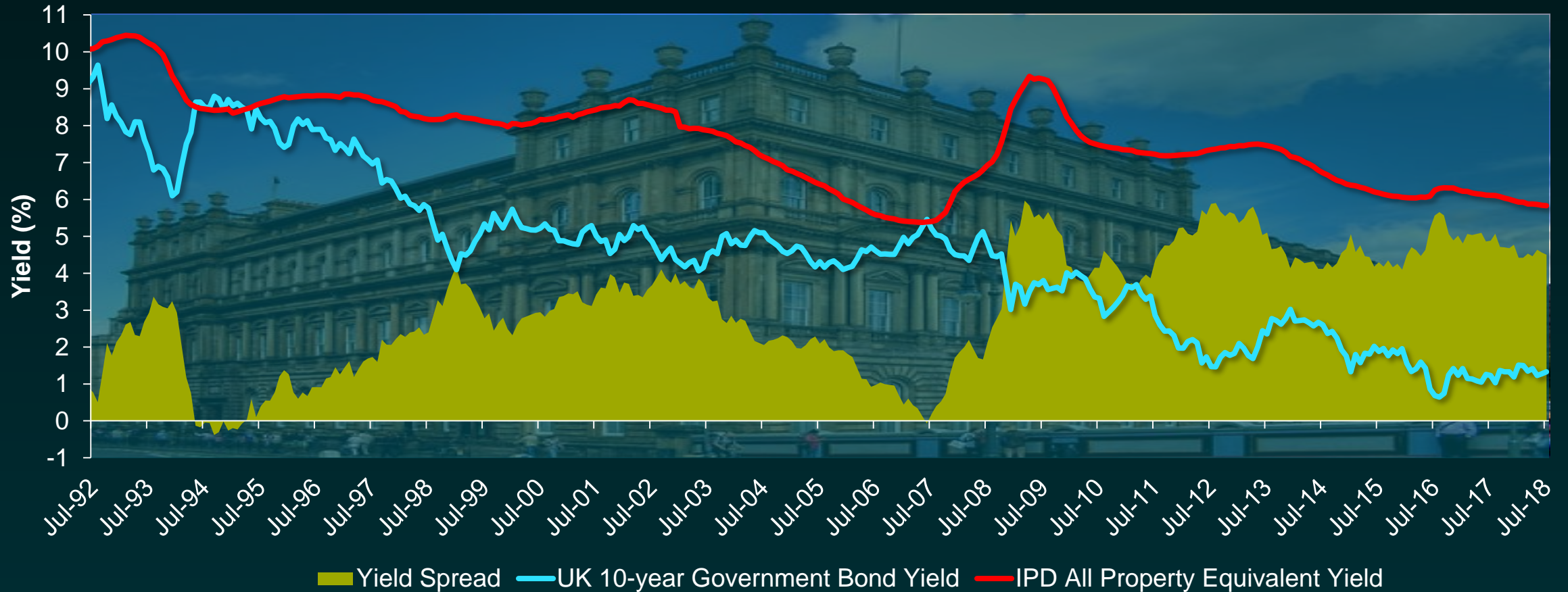




# Risk 1: rising bond yields

Property offers significant premium versus bonds

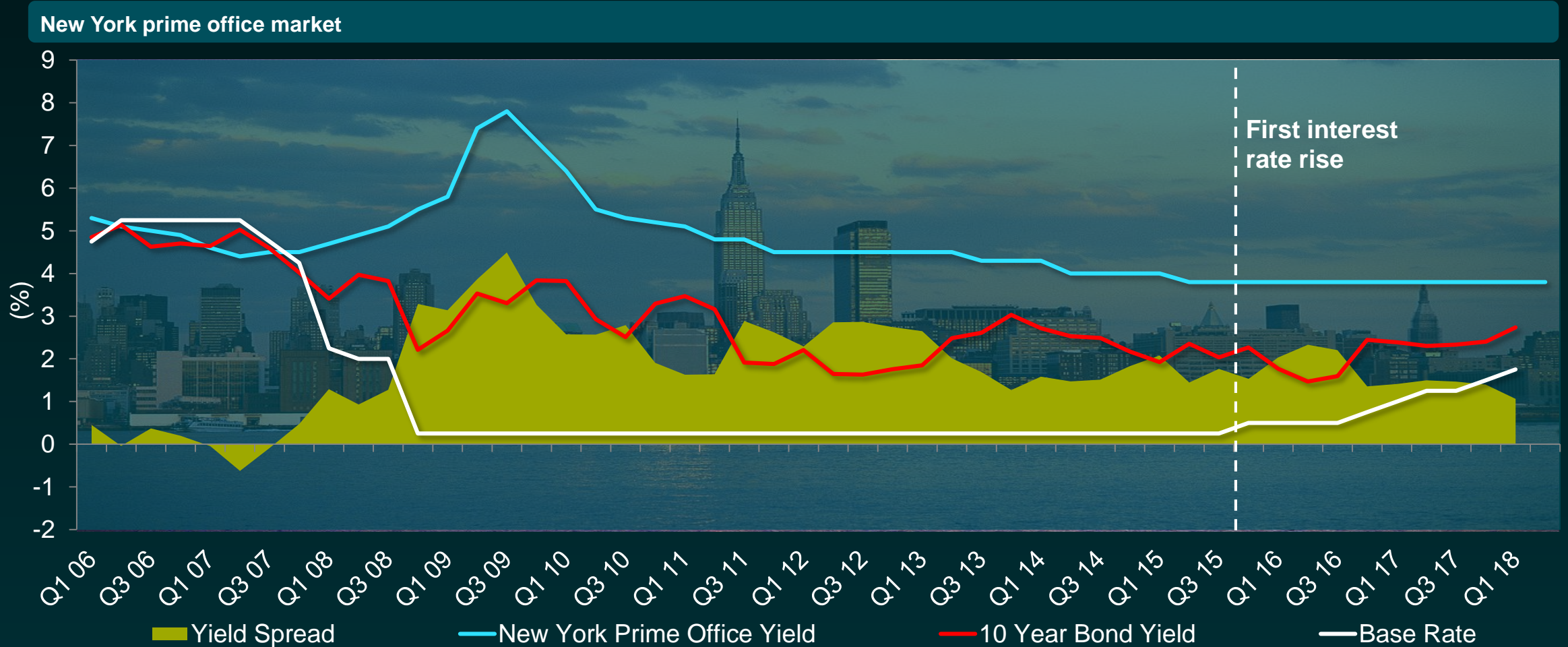
IPD Equivalent Yield Vs. 10-year Government Bond Yield



**Healthy spread protects property from significant upwards pressure on yields**

# Risk 1: rising bond yields

## Fed has been raising rates since 2015

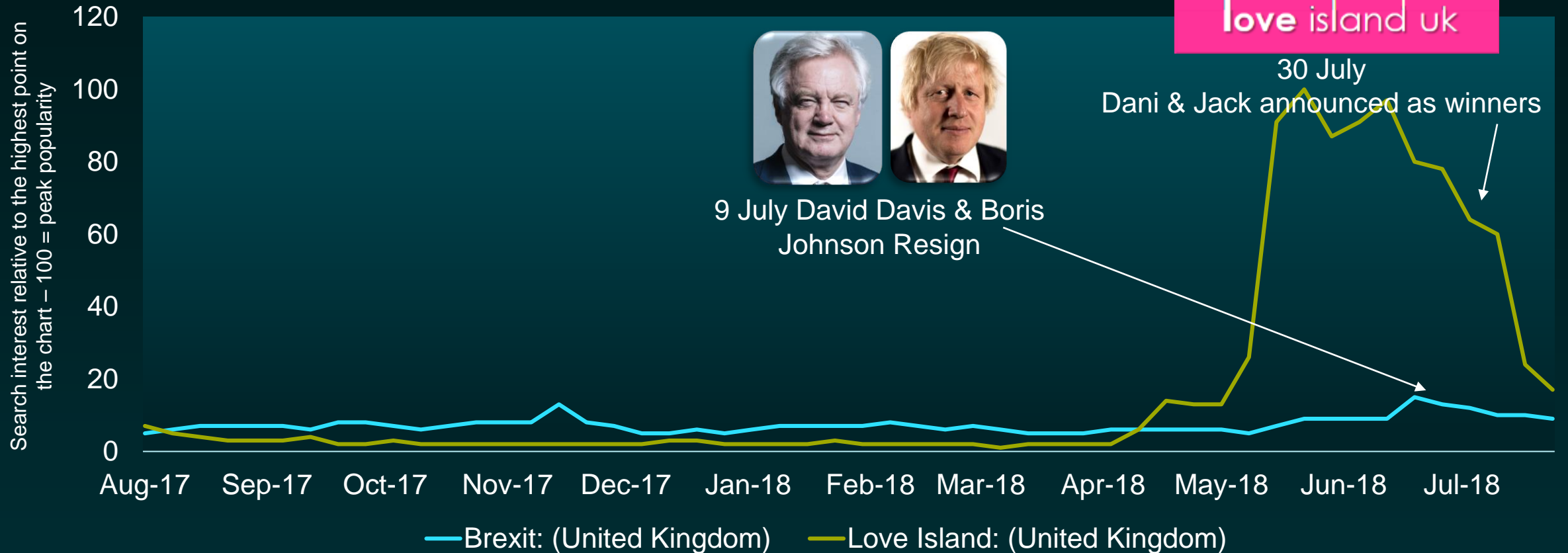


***Minimal impact so far but upwards pressure building***

# Risk 2: Brexit?

## What does Love Island tell us about Brexit?

### Google trends



***Voting to leave has become more important on Love Island than Brexit***



# Risk 2: Brexit?

## What does commercial property tell us about Brexit?



### Referendum aftermath

- Sterling weakness attracted overseas buyers
- Limited leverage reduced forced sellers
- UK market characteristics withstood uncertainty
- The impact will likely be gradual
- Political turmoil failed to derail the sector

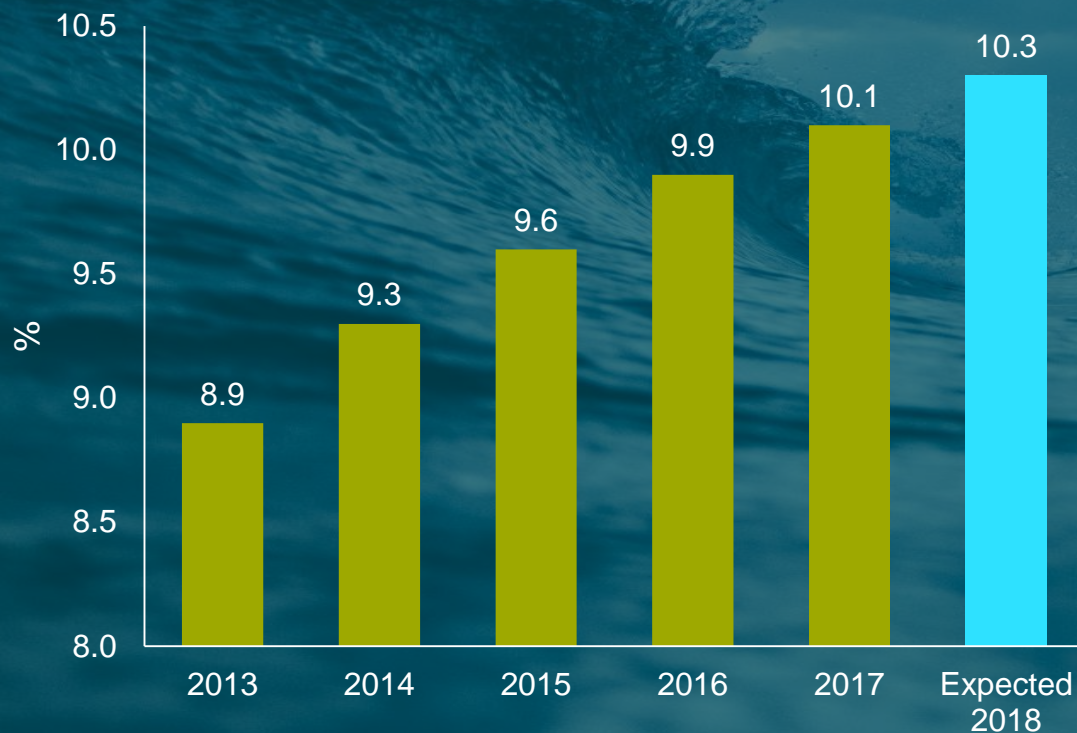
### What's happening today

- SMEs continue taking space
- Overseas investment YTD above 15 year trend
- UK and Pan European occupiers are less concerned about the impact
- PMI data remains positive for services and manufacturing

# Risk 3: investor demand wanes

## Ongoing global allocation to property

Weighted average target allocation to real estate, all institutions



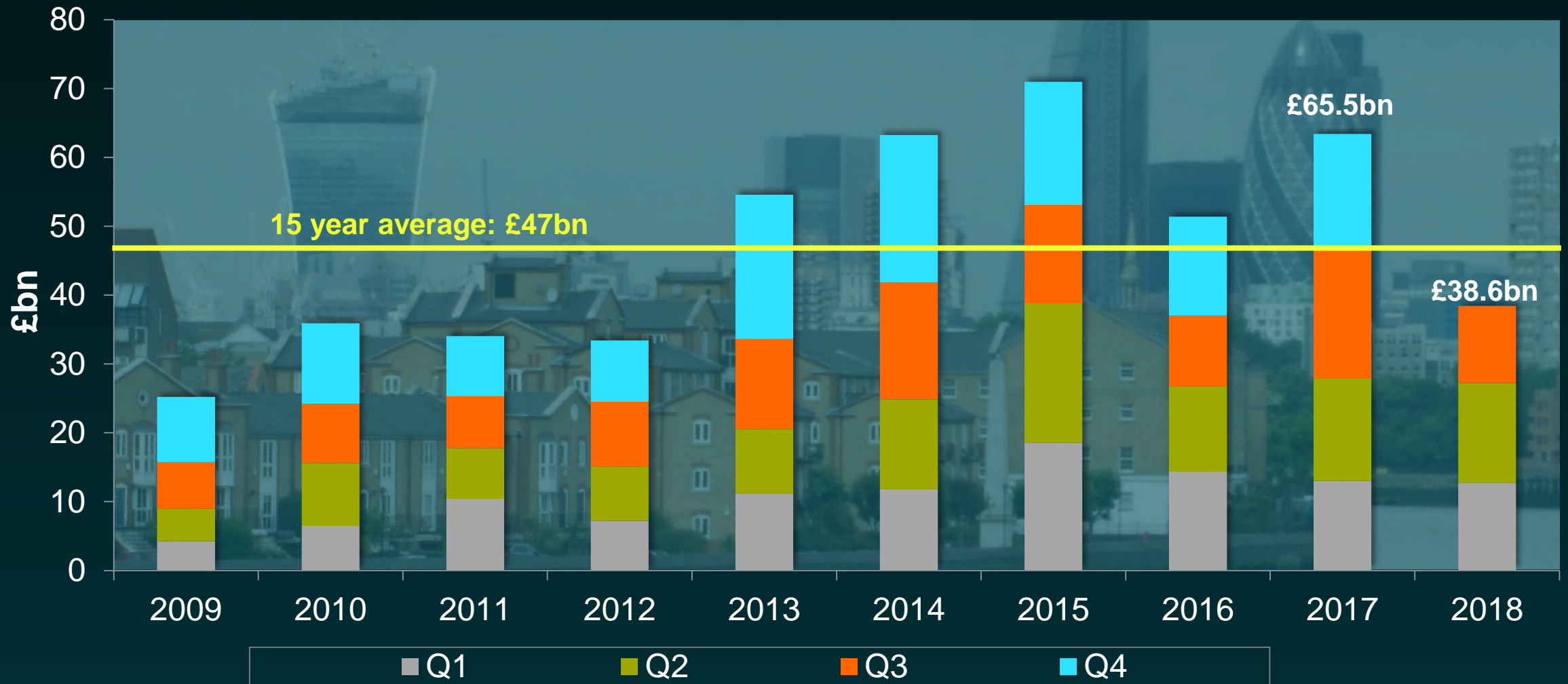
Percent invested vs target allocation by location of Institution



**1% = \$700bn, half of the \$1.4tn annual property market**

# Risk 3: investor demand wanes

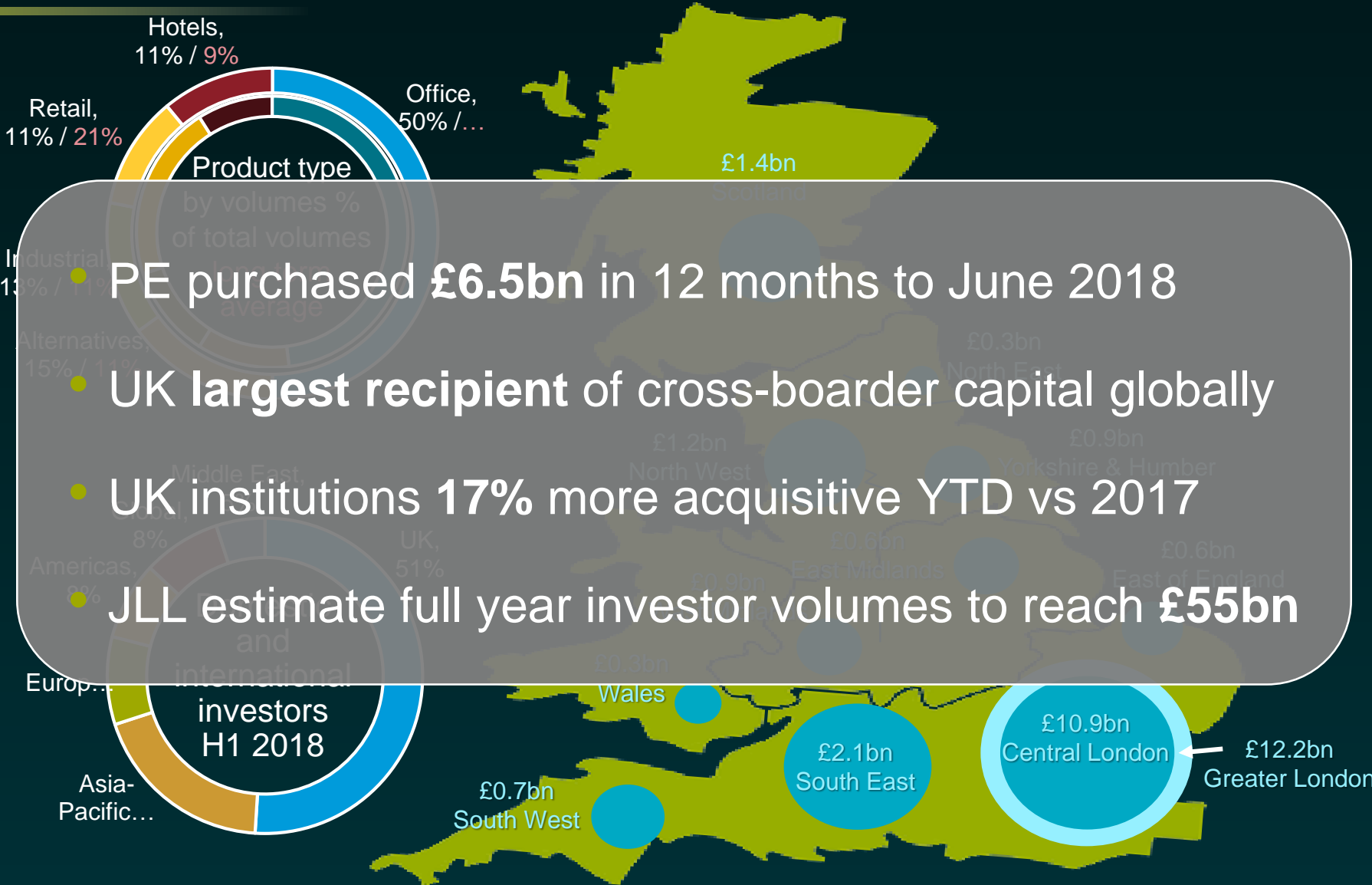
Transaction volumes remain buoyant



***Overseas still active, domestic institutions net buyers***

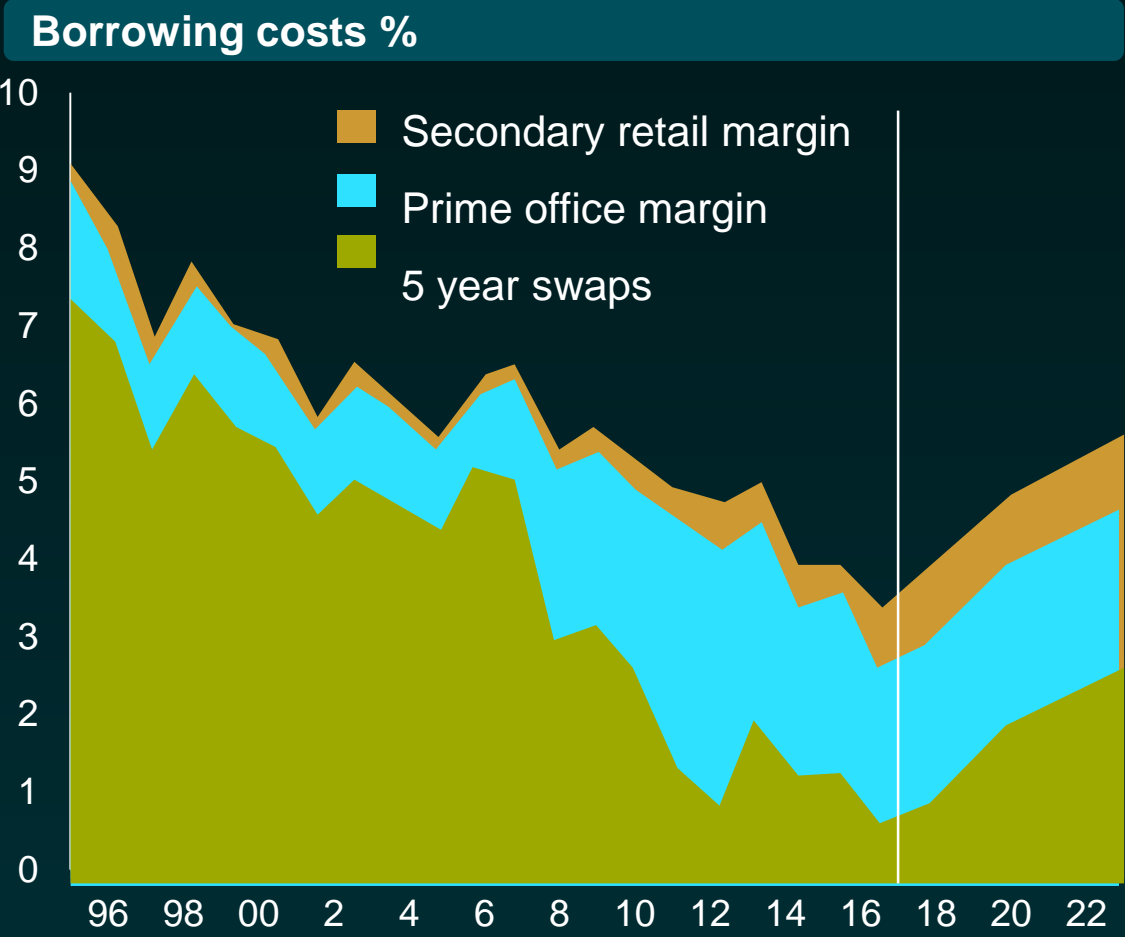
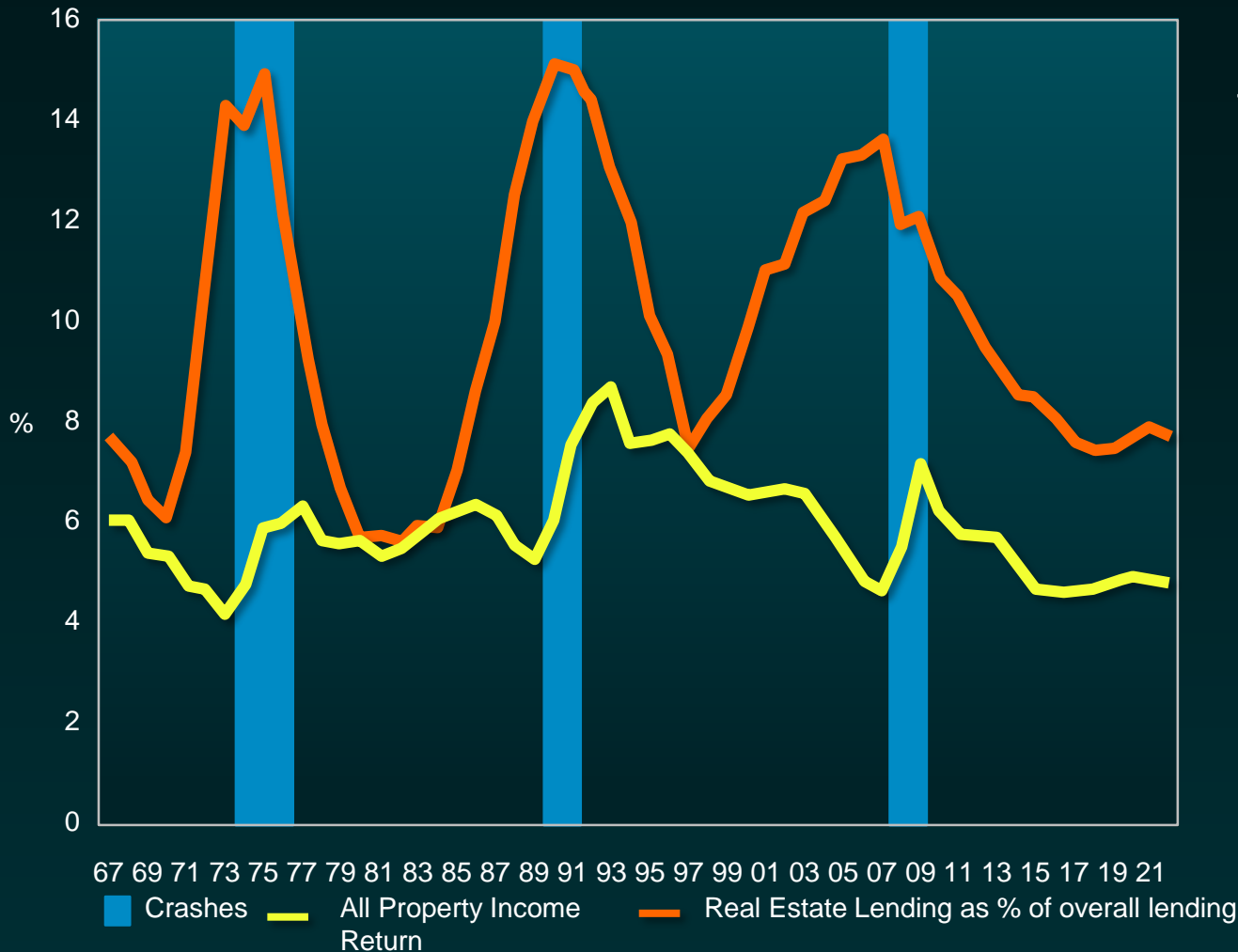
# Risk 3: investor demand wanes

## Transaction volumes remain buoyant



# Risk 4: weak property fundamentals

Where are we in the debt cycle?



**Leverage to remain contained; subdued development to continue**



# Risk 4: weak property fundamentals

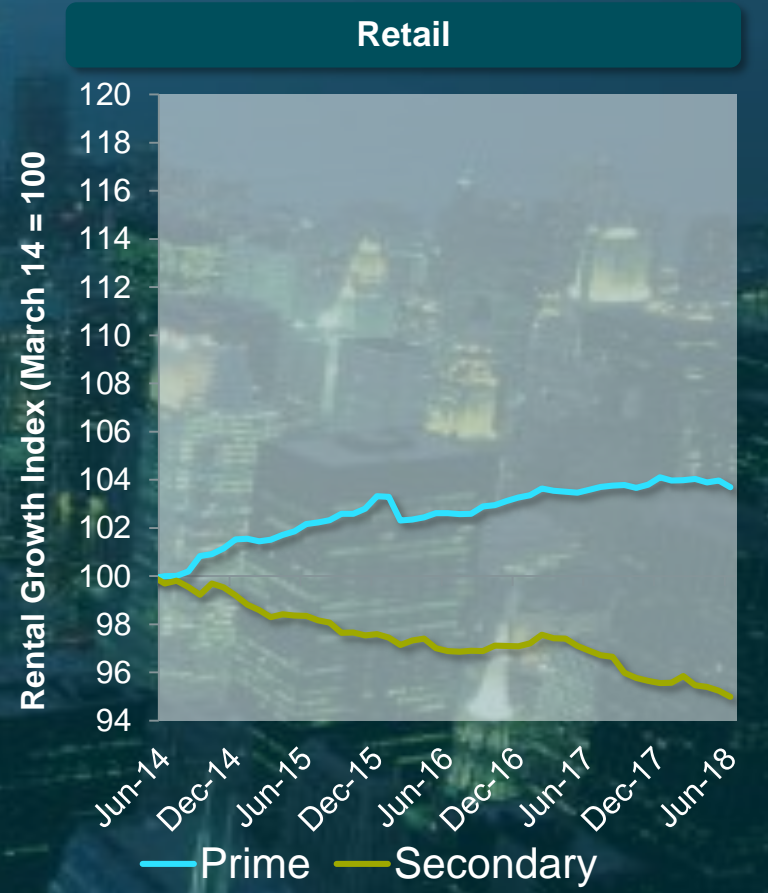
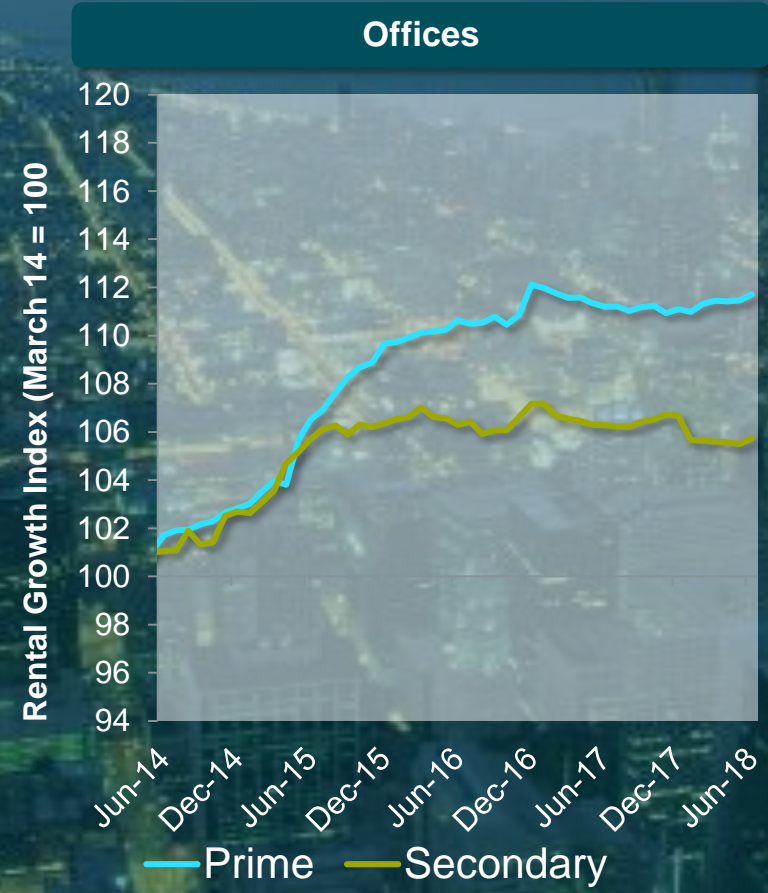
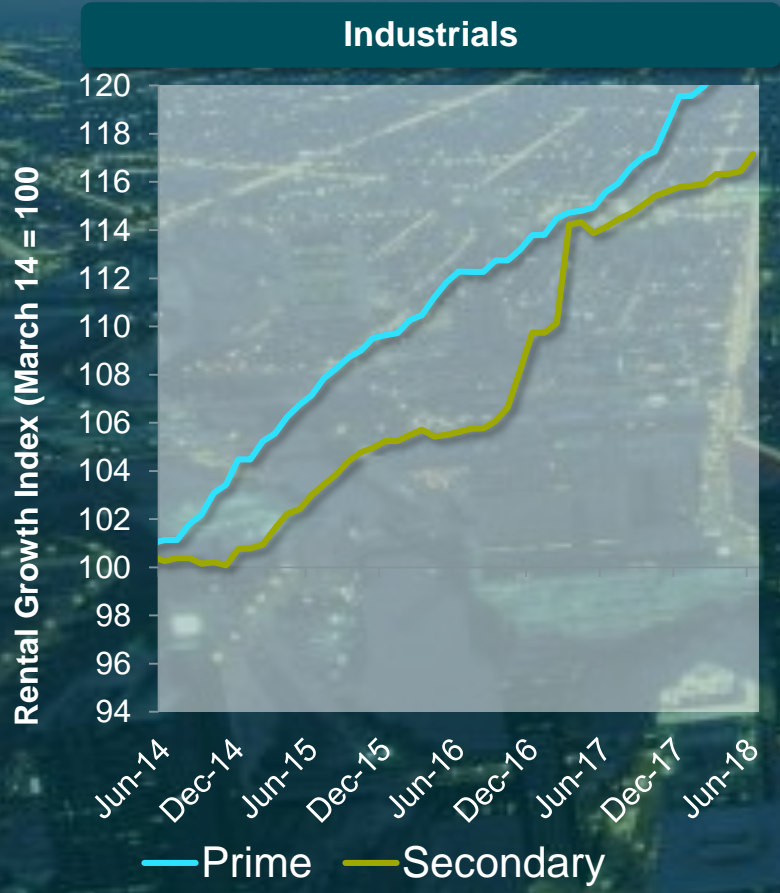
## Construction activity below long-term average



# Risk 4: weak property fundamentals

## Positive demand/supply dynamic persists

CBRE rental Growth Index (March '14 = 100)





# Risk 5: fear factor

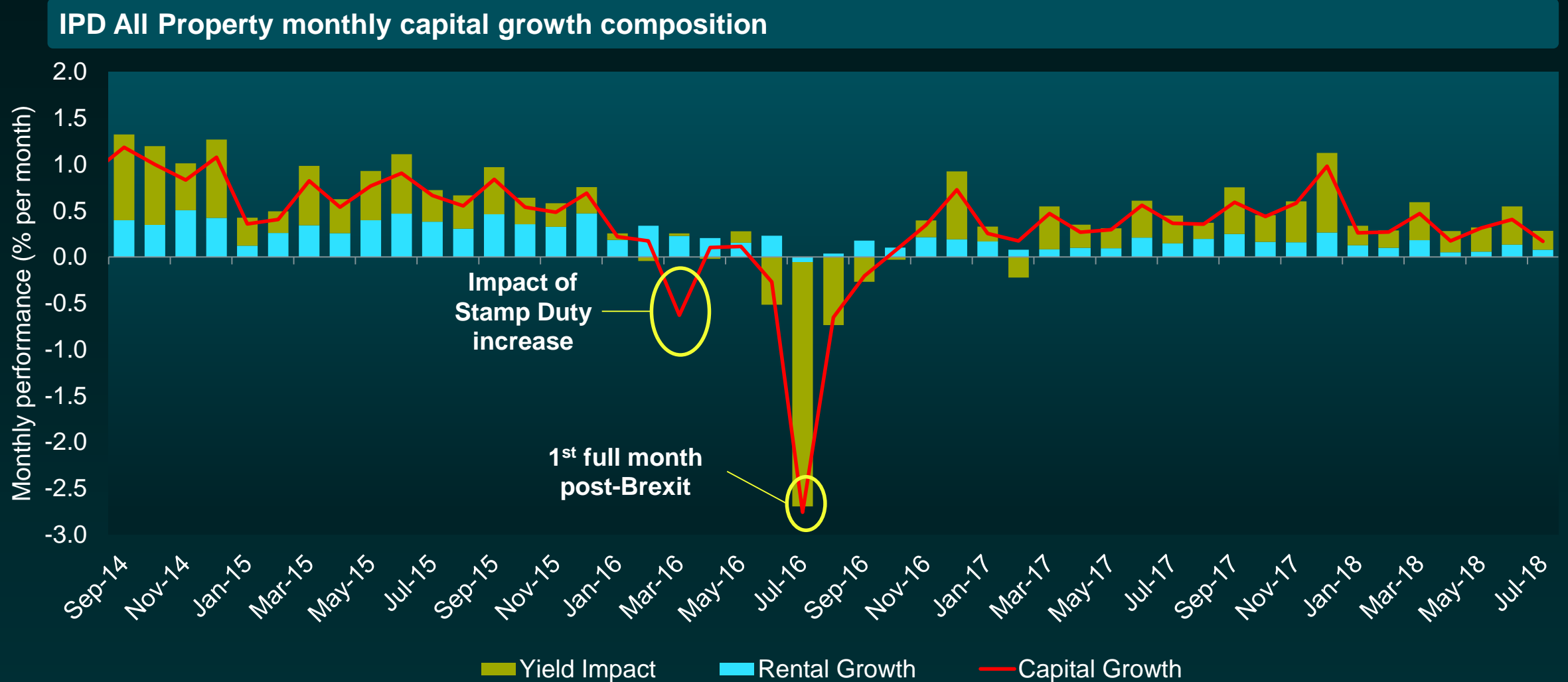
Unprecedented coverage & reaction



**BBC Six o'clock news**

# Risk 6: limited downside or unexpected upside risk?

## Dire predictions unfounded?





# Risk 6: limited downside or unexpected upside risk?

## M&G RE UK commercial property total return forecasts





# Agenda

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Lay of the land

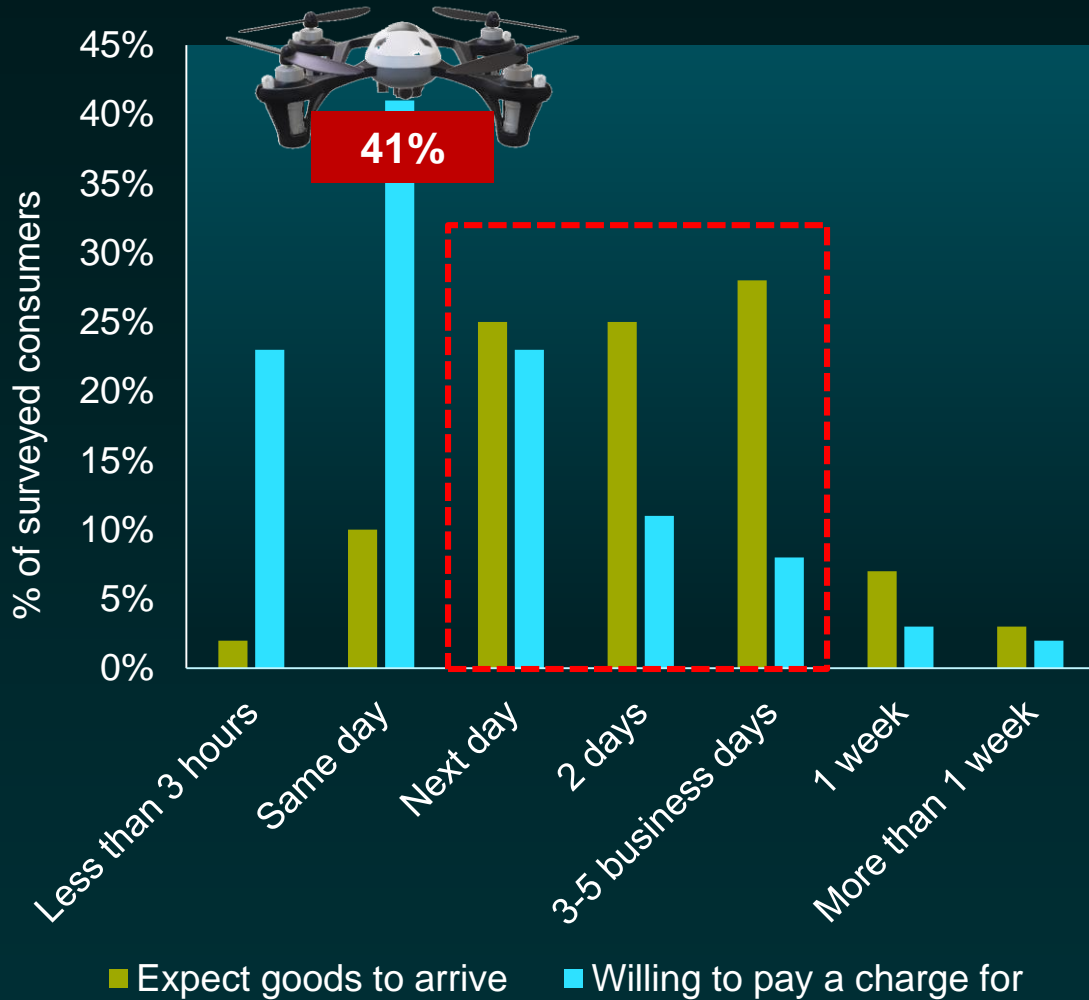
**Sector views**

Fund update

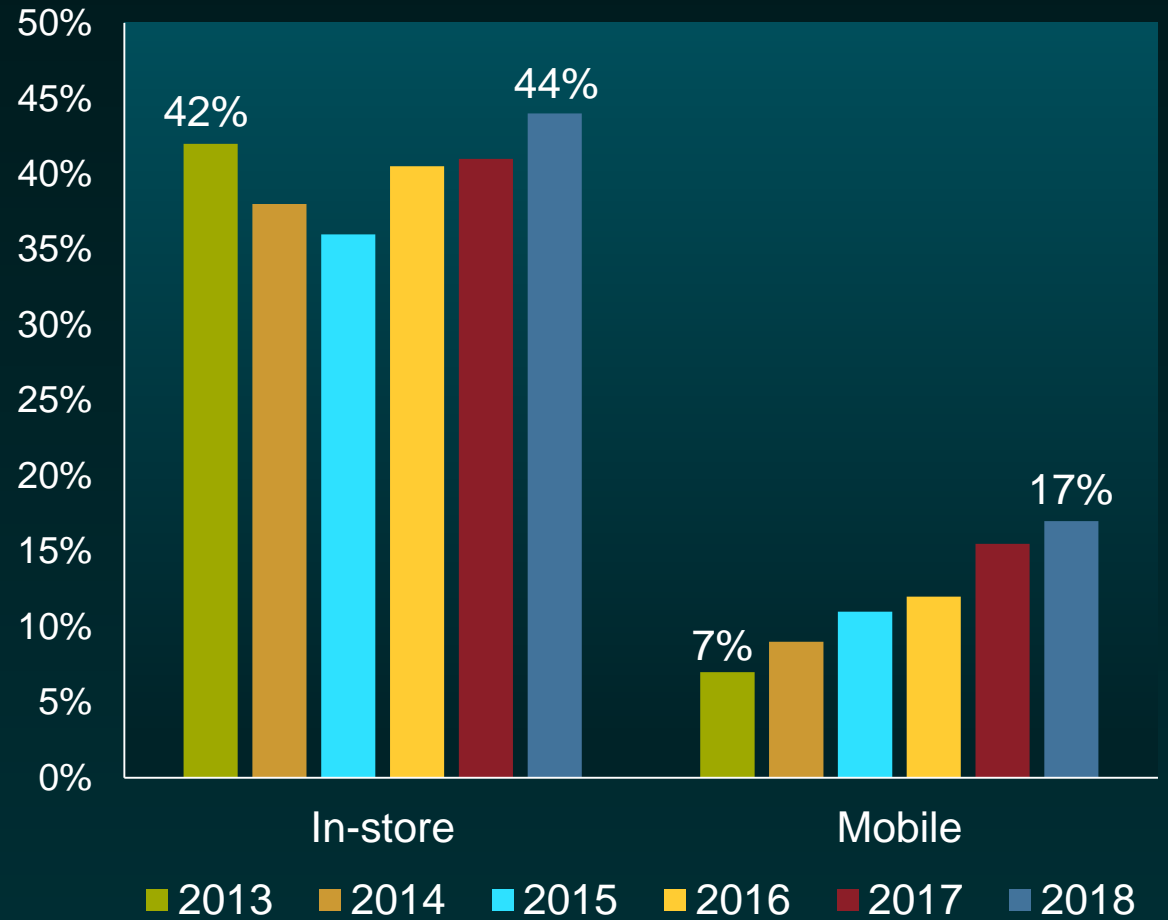
# Global retail trends

## Meeting consumer expectations

Consumer expectations of delivery and willingness to pay

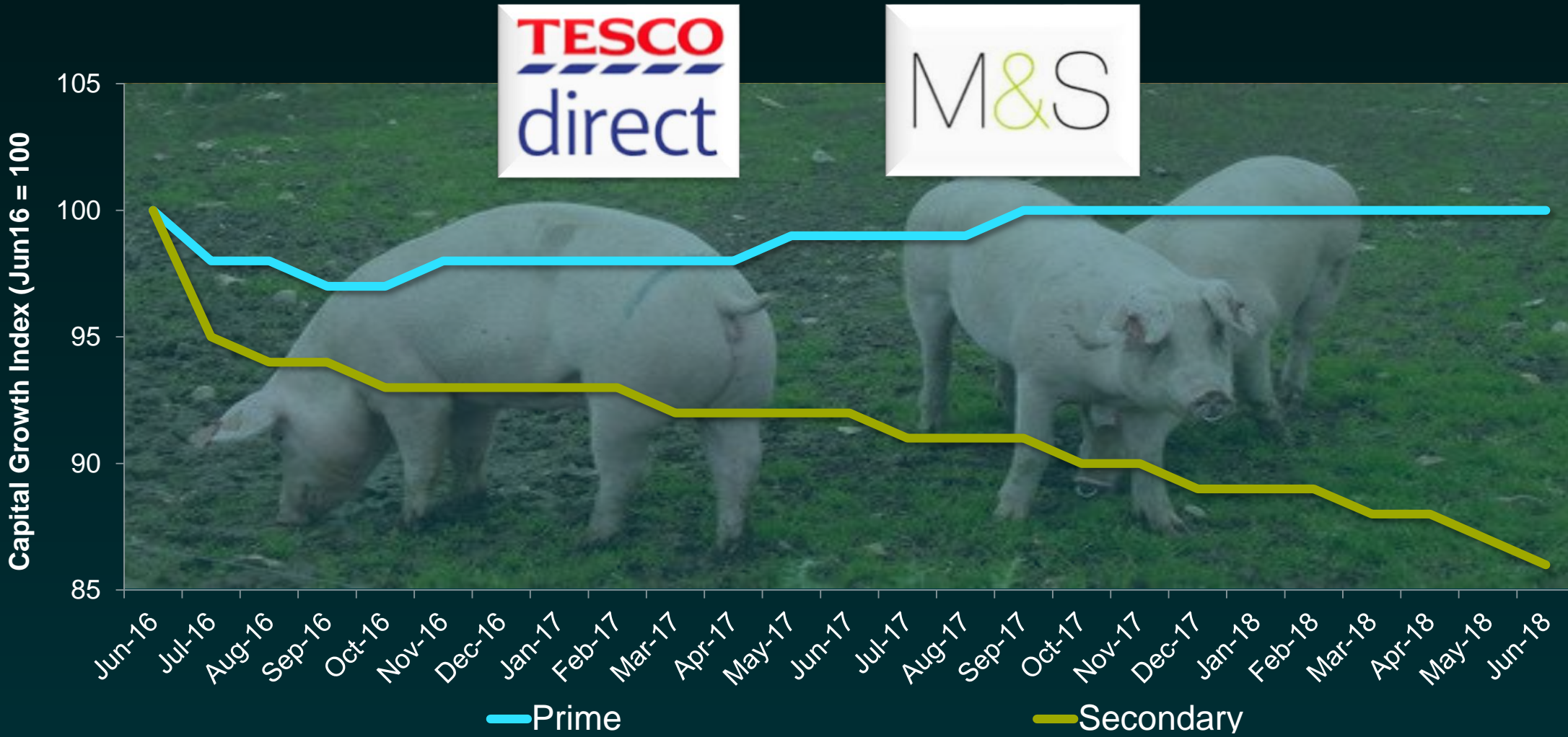


How often do you buy products using the following shopping channels?



# Local retail trends

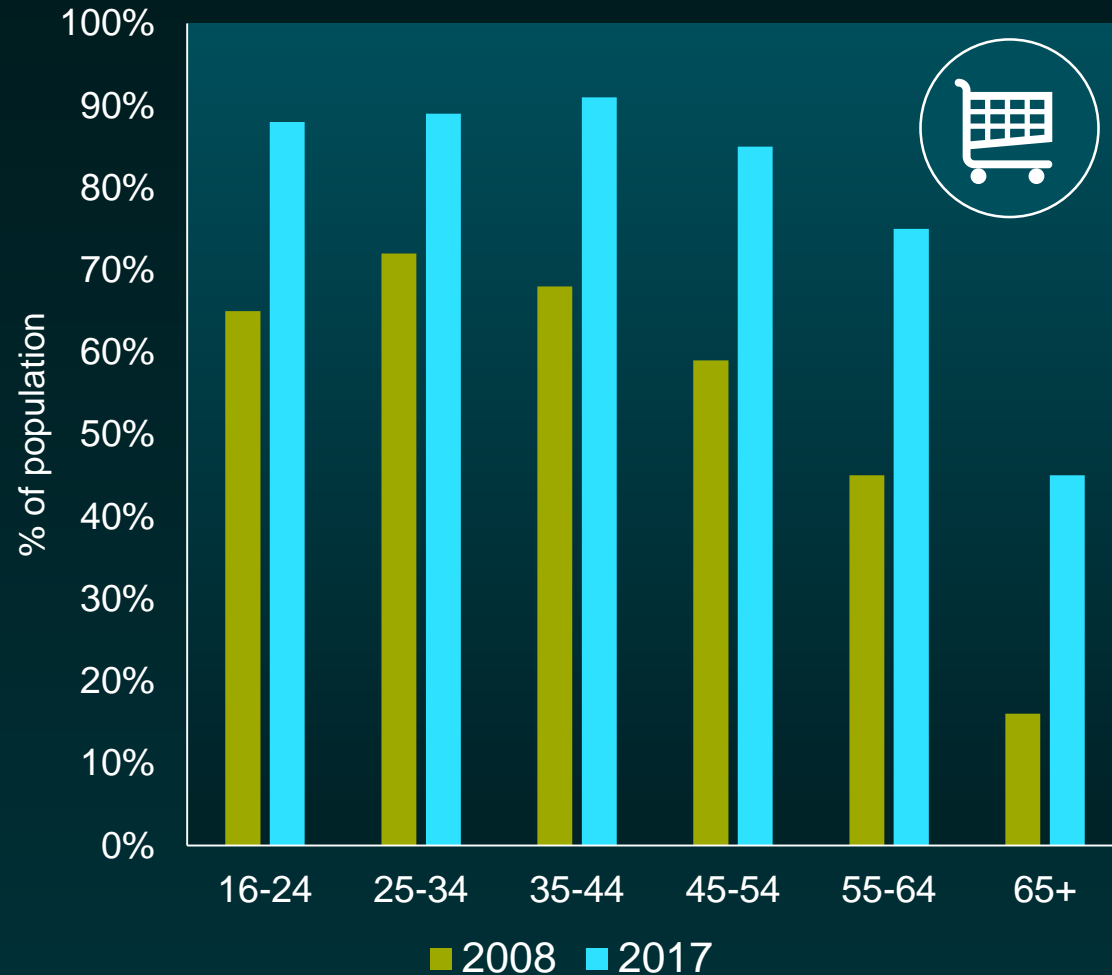
Not all retail is created equally



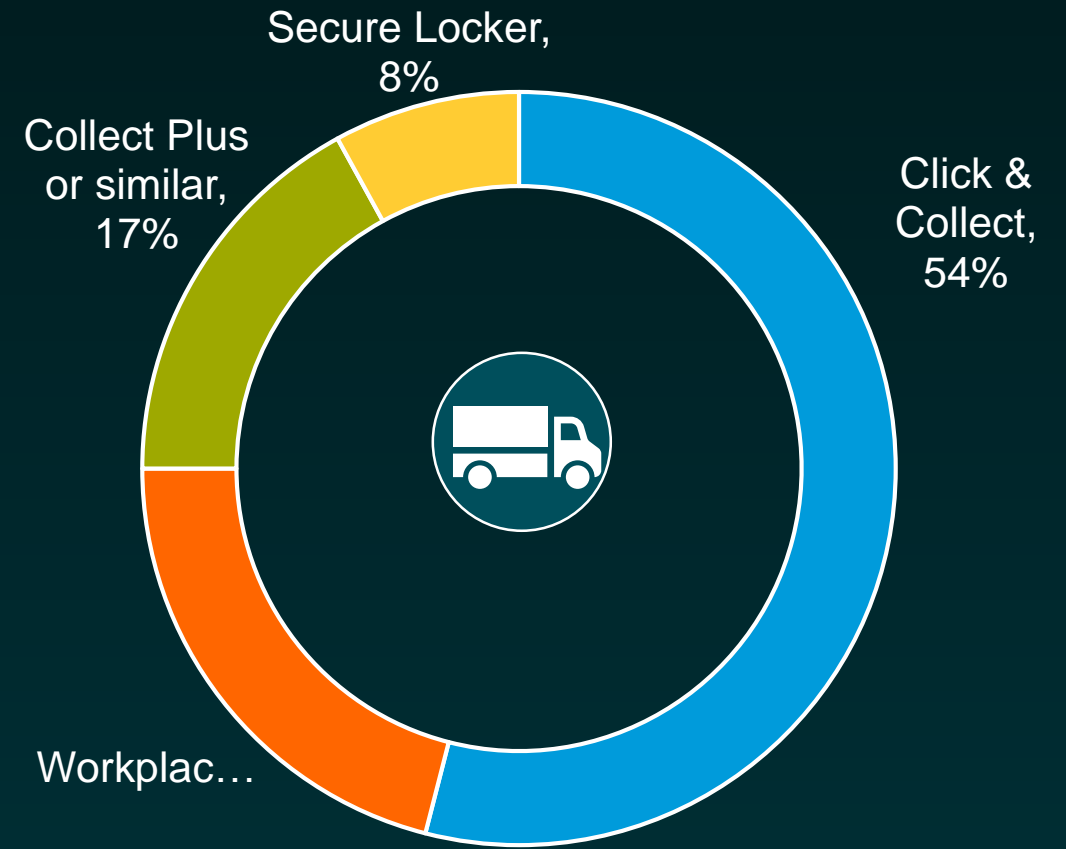
# Local retail trends

## How people shop

People shopping online in last 12 months by age



Consumer preferences for delivery location other than home, 2017



# Local retail trends

## Adapt or bust?

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### Try something new



### Getting physical





# Industrial: Overpaying?

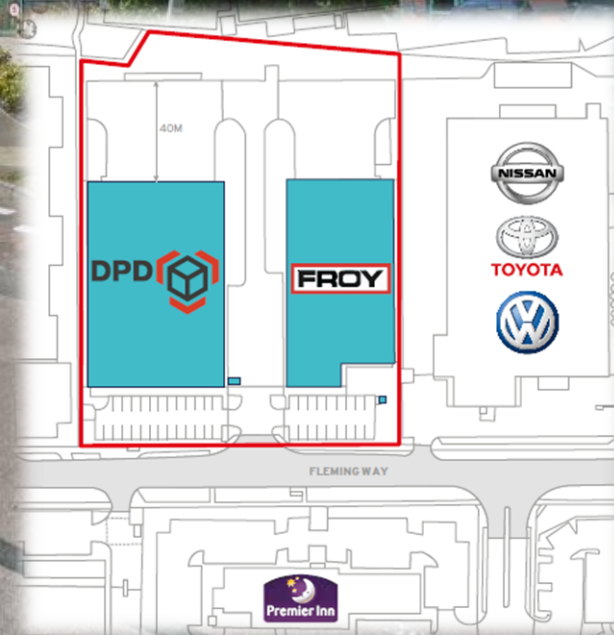
Little margin for error

**Focal Point, Crawley**  
**Quoting price:**

£12,760,000 / 4.25% NIY

**Sold at:**

£17,200,000 / 3.15% NIY



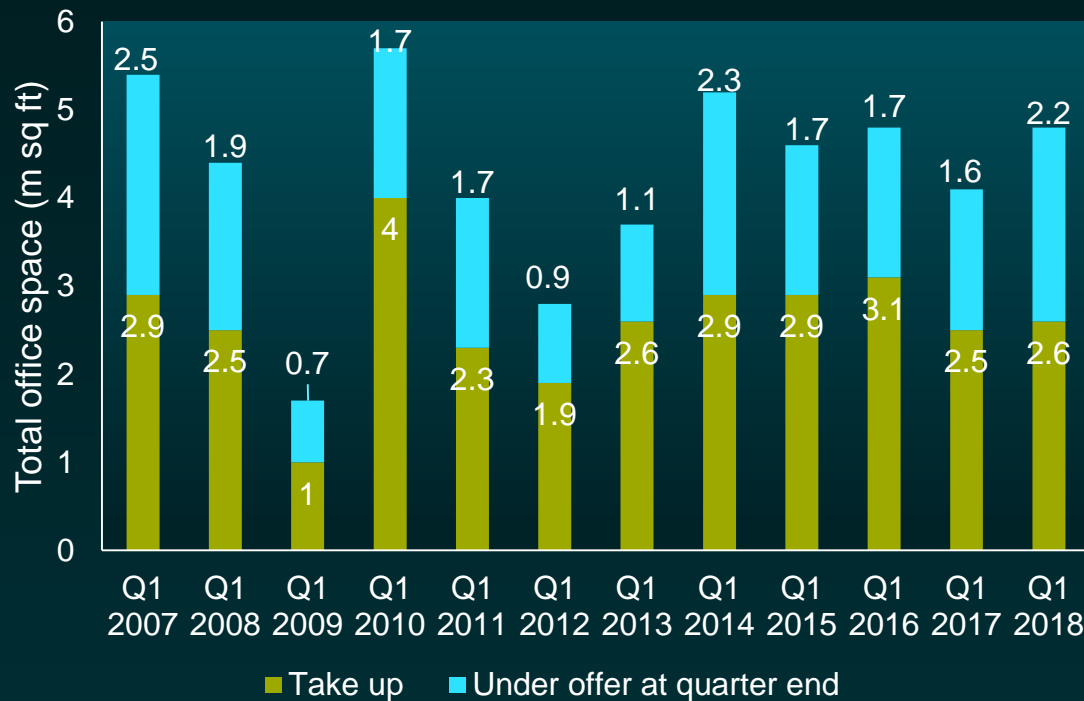
# Offices: misperception of risk?

## Central London - occupier activity resilient

Brexit could lead to loss of 100,000 financial services jobs, PWC Apr '16

City job losses likely to be nearer to 5,000, Reuters poll, Mar '18

Q1 London office take up & under offer



Availability rate (% of stock on the market)



**Sectors driving Q1 take-up: TMT (23%), Finance (18%), Professional (16%)**

# Offices: pernicious risk?

**A word on serviced office space: overhyped?**



*18,000 business leaders, in 96 countries said:*

## **FLEXIBLE WORKING...**

**91% - MORE PRODUCTIVE**

**89% - BUSINESS GROW**

**87% - COMPETITIVE**

**87% - MAXIMISE PROFITS**

**87% - RECRUIT & RETAIN TOP TALENT**



*WeWork's future UK rent bill tops £3bn in UK across 3m sq ft*

**PRIVATE**

**EST. VALUE £20bn**

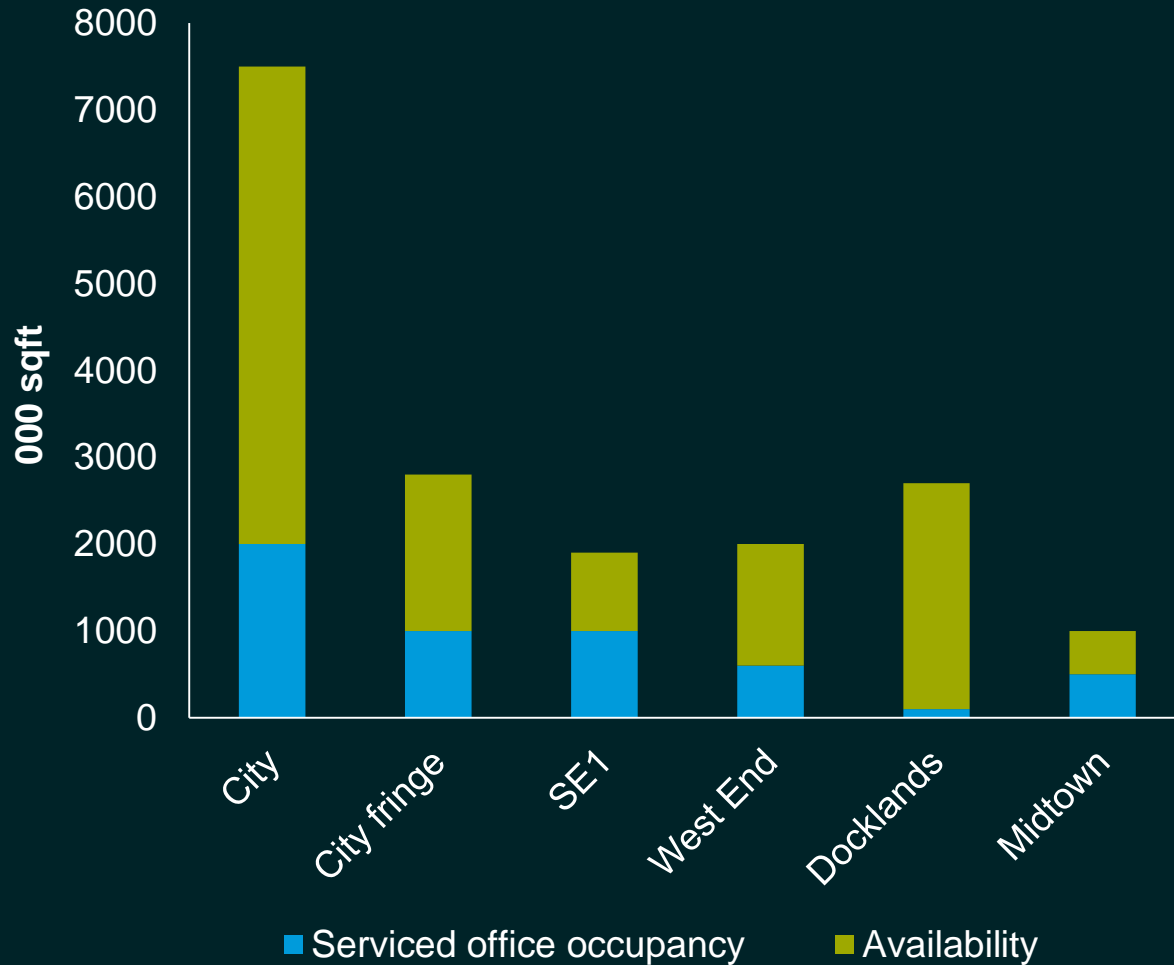
**LOSS MAKING**



# Offices: pernicious risk?

## Grey space vs. low vacancy and development

### Serviced office providers



### Vacancy rates



City  
down to

4.6%  
↓  
4.7%



West End  
stable

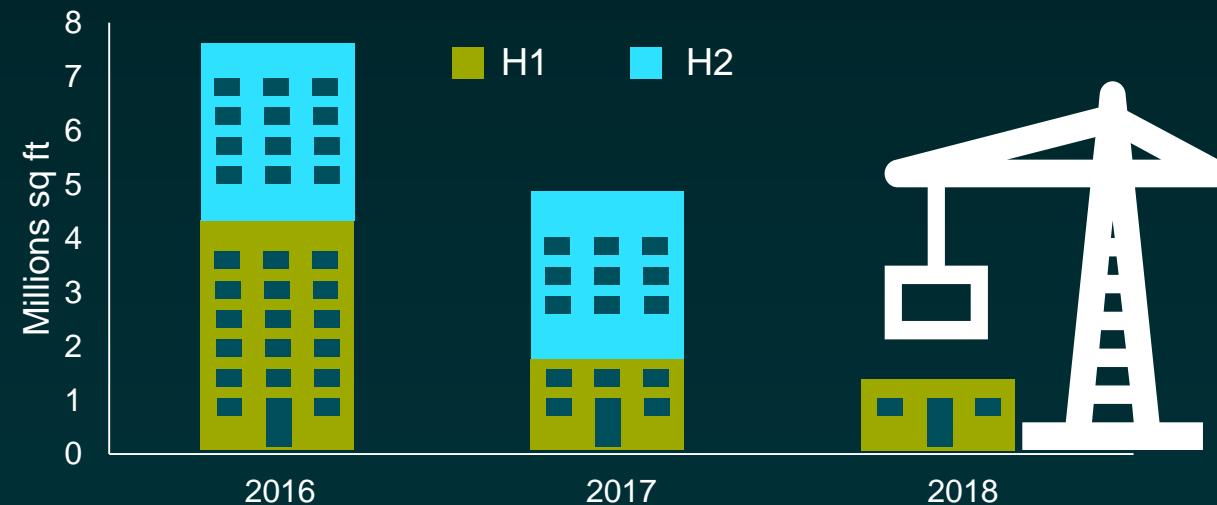
4.0%  
↔  
4.0%



East London  
down to

8.7%  
↓  
9.0%

### Development starts



# Agenda

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Lay of the land

Sector views

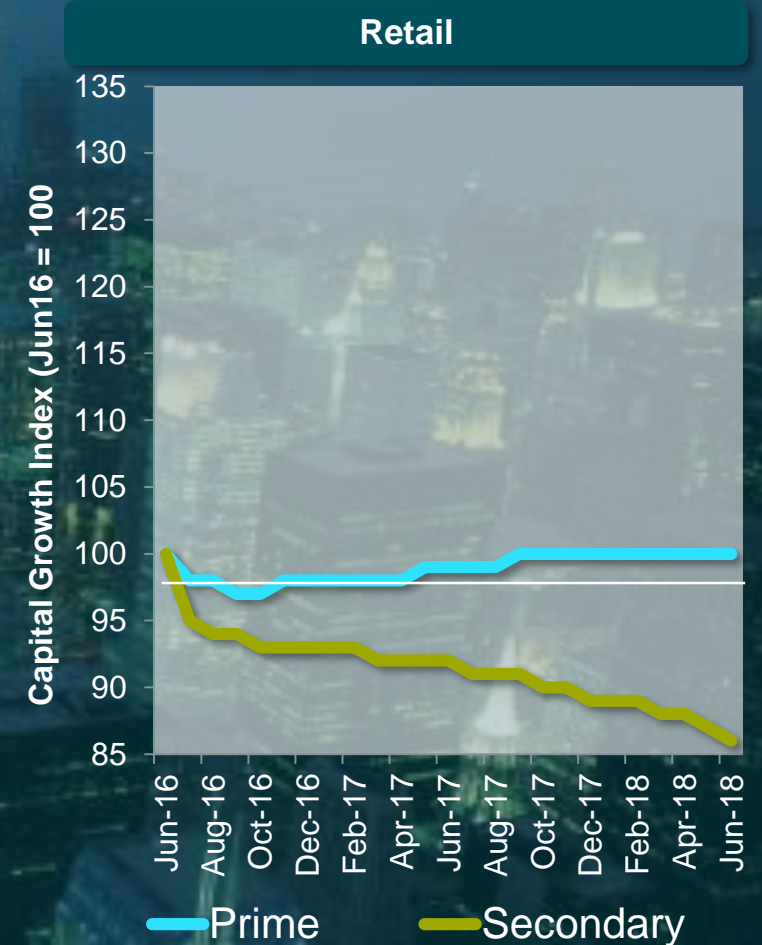
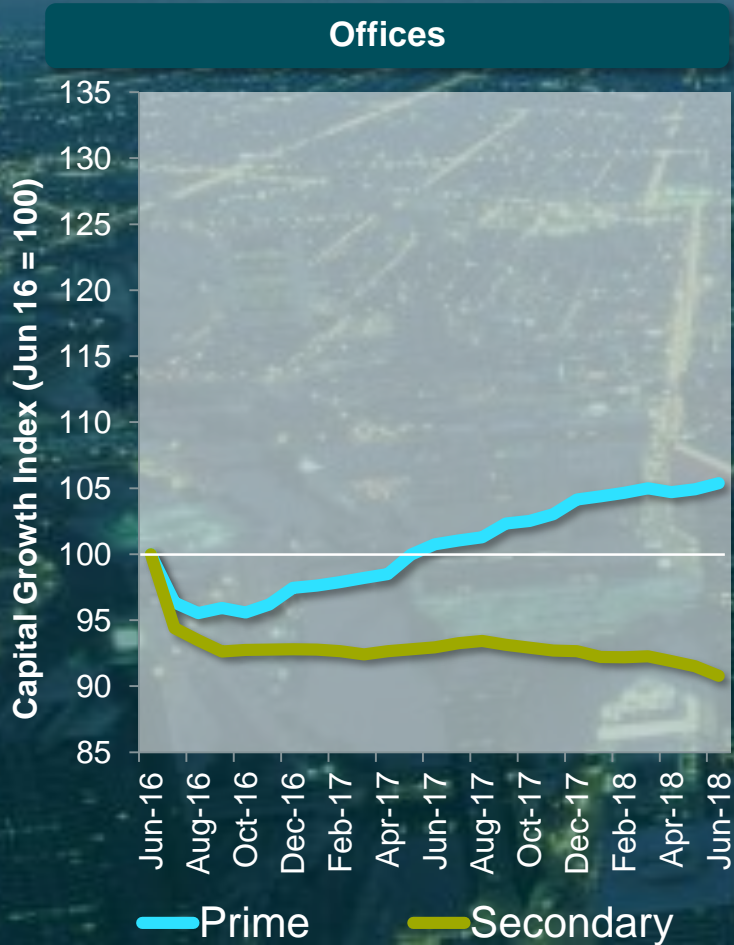
**Fund update**



# Quality bookends: prime vs. secondary

## Asset performance

CBRE Property Valuation Capital Growth, Index June 16 = 100



# Performance

## In sterling

Performance	YTD %	1 year %	3 years % pa	5 years % pa
<b>M&amp;G Property Portfolio</b>	<b>3.7</b>	<b>6.7</b>	<b>2.0</b>	<b>5.9</b>
Peer group average*	3.5	6.7	3.3	6.5

- Price swings distort data
- Peer group influenced by holdings in securities

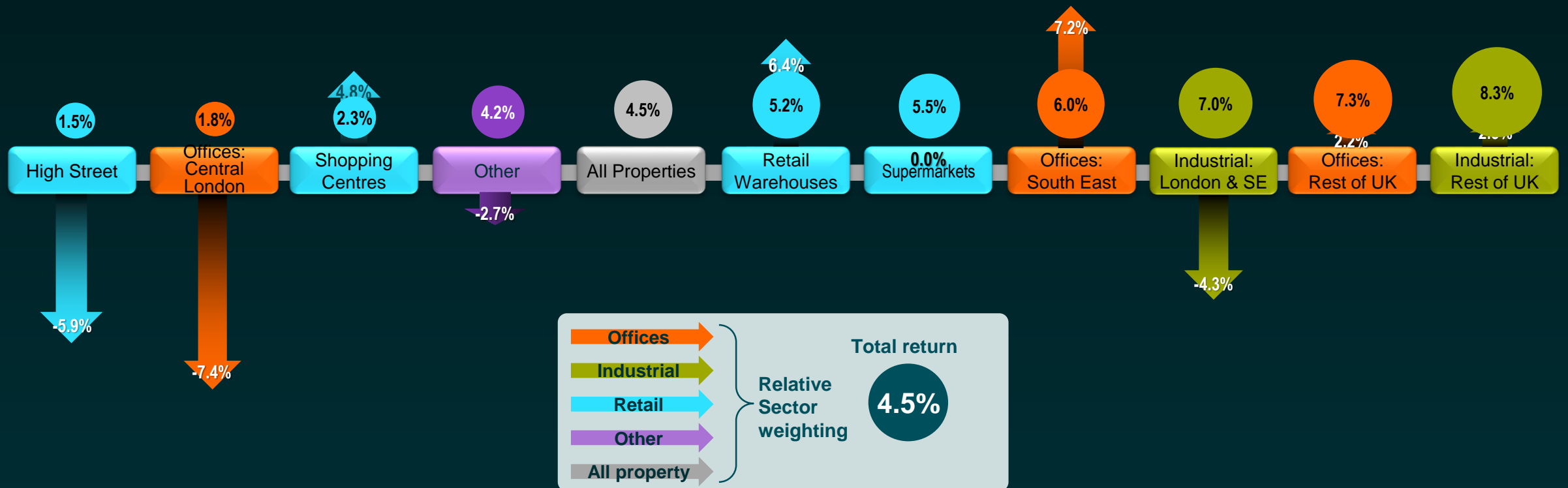
Performance <sup>2</sup>	2017 %	2016 %	2015 %	2014 %	2013 %
M&G Property Portfolio	6.9	-7.1	8.9	14.4	6.5

Past performance is not a guide to future performance

# Well positioned

Impact on total return (%pa) : Jul 2018 – July 2021

Ranked by total return (%pa)



Past performance is not a guide to future performance

# Income quality

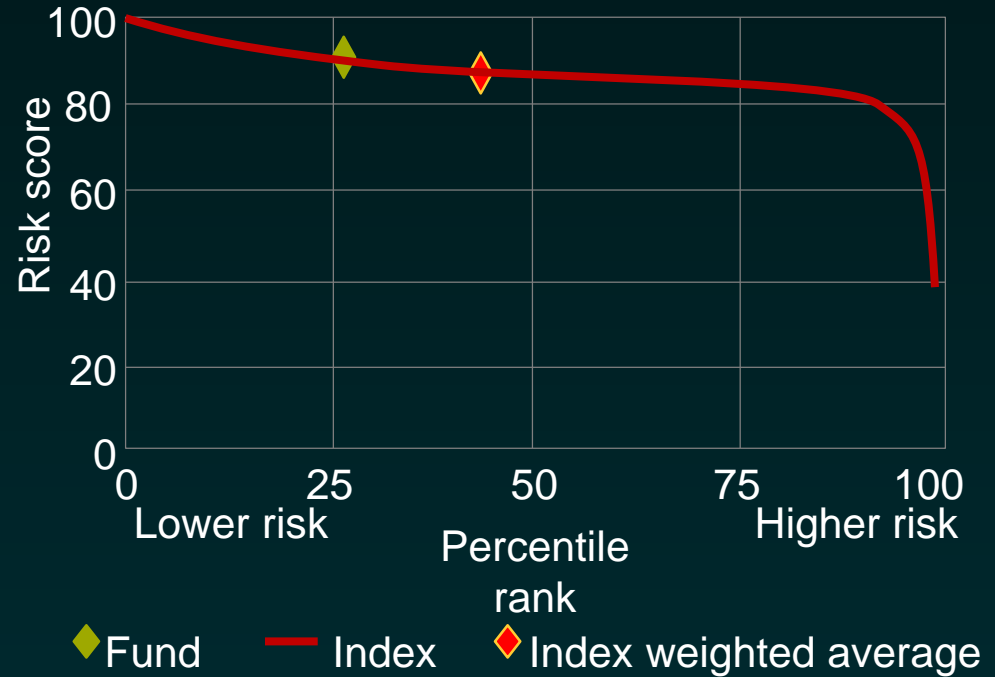
## Tenant mix



Fund quartiles from safest (green) to riskiest (orange)



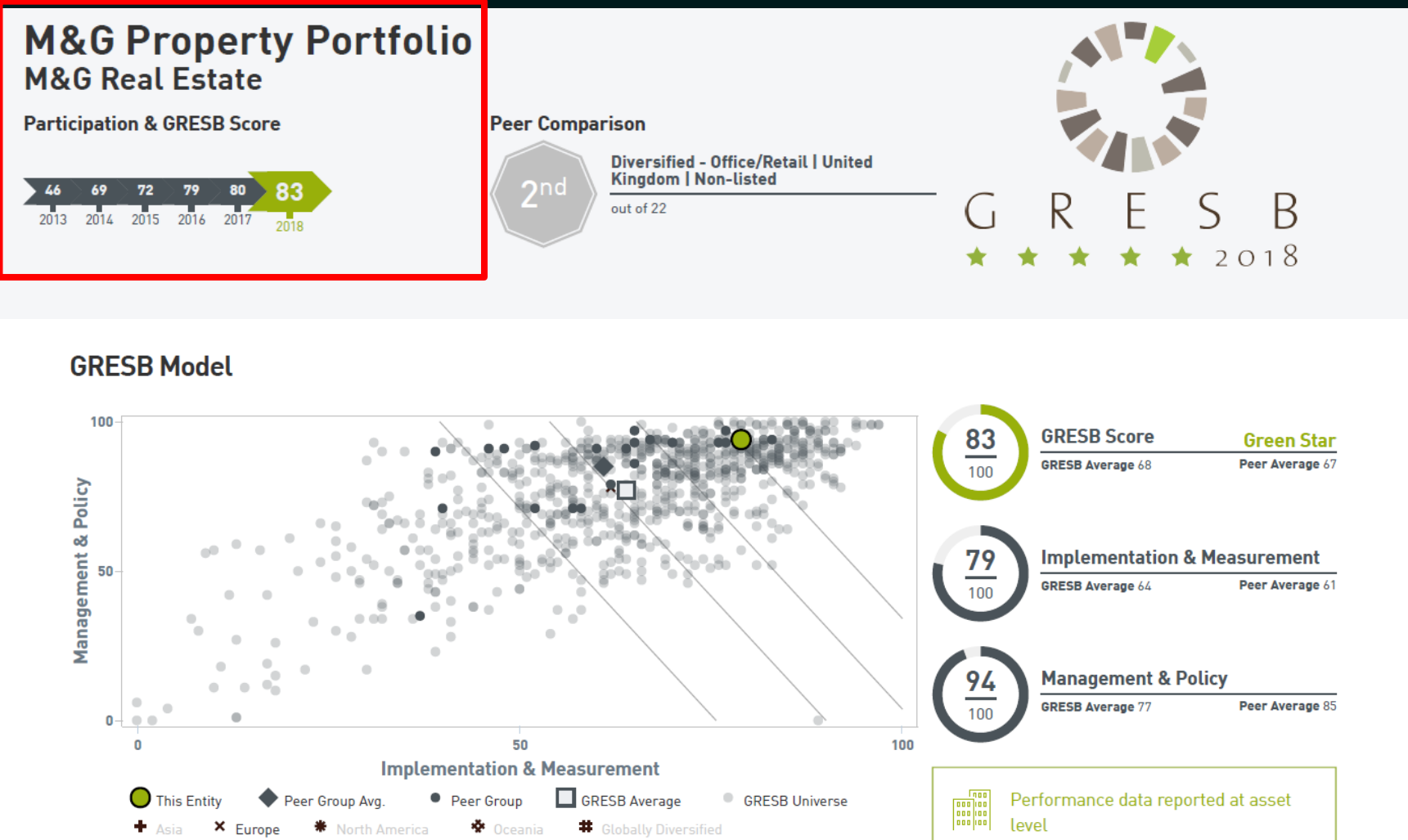
Ranking of weighted risk score



	Q1 2018
Fund percentile rank	26.9
Index percentile rank	45.9

# Responsible Property Investing - fit for purpose

## GRESB Real Estate Assessment 2018 – 5 star rating





# Summary

## Stick, not twist

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- Property funds continue to offer a secure income and a key portfolio diversifier
- The investment market remains resilient supported by property fundamentals
- Income to drive returns in the medium term

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# Q&A

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