

A solid third quarter

Following a strong second quarter, SKAGEN m2 continued to deliver a solid absolute return in the third quarter. Although the fund is still ahead of its benchmark index, it did lose some ground in the quarter due to the strong performance of real estate stocks and currency in China and Hong Kong. These are both markets where the fund is substantially underweight versus the benchmark. Expected central banking initiatives, mainly in the US and Euro area, and low risk appetite in combination with strong demand-driven sector earnings continue to be the main drivers for the real estate market globally.

Global Logistic Properties was the best contributor in the quarter and year to date. The company received an offer in the second quarter from a Chinese consortium wanting to privatise it. Global Logistic Properties recently entered the European market for the first time by acquiring Gazley in a EUR 2.4 billion deal. This will be an entry point for continuous consolidation in Europe, which will lead to further yield compression in the European logistics sector. Eventually this will also benefit Catena, another SKAGEN m2 holding. E-commerce driven demand for modern logistics is growing in strength in all markets globally.

The second best contributor in the quarter was the Spanish office operator Colonial. The company has performed strongly over the year mainly

thanks to positive real estate fundamentals primarily in Madrid and Barcelona, but also in Paris where the company has assets.

Another strong contributor was Austrian CA Immobilien. The good performance was mainly driven by the strong underlying office markets primarily in Munich and Berlin, but also due to hidden land bank values that have been crystallised and will add to growth over the next few years. Immofinanz, another SKAGEN m2 holding, has a 26% stake in CA Immobilien and the intention is to merge these two companies next year subject to certain requirements.

In Europe the best performing real estate markets year to date are Italy, Spain and Austria. These are all markets where m2 has good exposure, including in the strong Italian performer Beni Stabili which SKAGEN m2 bought into last year at low levels.

The worst contributor in the fund was Japanese Mitsui Fudosan, not due to any company specific reason, but rather to a generally weak real estate market and a weak yen. SL Green was also a detractor on the back of continued fears about the rental growth in Manhattan. The US REIT segment also progressed slowly on fears of higher and faster than expected interest rate hikes, in addition to a weak USD.



Austrian CA Immobilien was a strong contributor to the fund's performance in the quarter. Photo: Bloomberg



Hong Kong based Sun Hung Kai Properties is a new position in the fund. Photo: Bloomberg

Portfolio activity

SKAGEN m2 initiated two new positions in the fund in the third quarter. One of these is Hong Kong based Sun Hung Kai Properties which has a diversified business model, an extensive land bank and a strong balance sheet. The company trades at a deep discount to substance; something that could be managed by share buy backs or increased dividends. The company has operations in Hong Kong and mainland China.

The other newcomer is the Japanese company, Sekisui House which focuses on the construction of detached houses, rental housing, and management fees in addition to its overseas operations in the US, China, Australia and Singapore. Sekisui has very diversified operations and its balance sheet is solid. The company is specialized, and at the forefront of building with advanced steel frame prefab construction and is well known for its progress within the eco/passive housing. Sekisui is in a good position to increase earnings and accelerate market share as it is more resilient to potentially rising labour costs given its advantages over conventional building techniques in terms of construction time and costs.

We sold out of Finnish Sponda due to the Blackstone acquisition. British Land, Ashford Hospitality Trust and Axiare were all sold as a result of the index change that took place in July.

Outlook

The foundations of real estate are still very good and transparent. Earnings and cash flow visibility for the sector as a whole is unique due to leasing and credit maturities. Balance sheets are solid and credits are diversified and refinanced at low levels with long duration. In many cases, companies have good rent reversion potential, like German residential and Spanish office properties, meaning the difference between current rent-roll and market rents. In some markets, real estate prices and stocks have been overinflated by positive fundamentals but also by speculation – we try to avoid these. The spread between valuations in direct real estate and listed companies are still wide, implying that we will see further M&A transactions on the stock exchange. In general, valuations are not overwhelming, with companies still trading at a discount to substance, backed by good demand driven rental growth.

The fund gives access to a normally inaccessible global real estate market. The fund selects low-priced, high-quality real estate companies from around the world.

The objective is to provide the best possible risk adjusted return.

The fund is suitable for those with at least a five year investment horizon.

Historical performance (net of fees)

Period	SKAGEN m2 A	Benchmark index
Last Month	0.0%	2.3%
Quarter to date	2.4%	3.8%
Year to date	8.0%	4.1%
Last year	11.1%	4.5%
Last 3 years	9.3%	10.8%
Last 5 years	n/a	n/a
Last 10 years	n/a	n/a
Since start	7.5%	10.2%

Fund Facts

Type	Equity
Domicile	Norway
Launch date	31.10.2012
Morningstar category	Property - Indirect Global
ISIN	NO0010657356
NAV	19.27 EUR
Fixed management fee	1.50%
Total expense ratio (2016)	1.85%
Benchmark index	MSCI ACWI IMI/Real Estate NR
AUM (mill.)	112.30 EUR
Number of holdings	30
Lead manager	Michael Gobitschek

Performance last ten years



Contributors in the quarter

Largest contributors

Holding	Weight (%)	Contribution (%)
Global Logistic Properties	4.60	0.53
Inmobiliaria Colonial	5.95	0.51
CA Immobilien Anlagen	3.65	0.38
Beni Stabili	3.12	0.37
Catena	6.64	0.35

Largest detractors

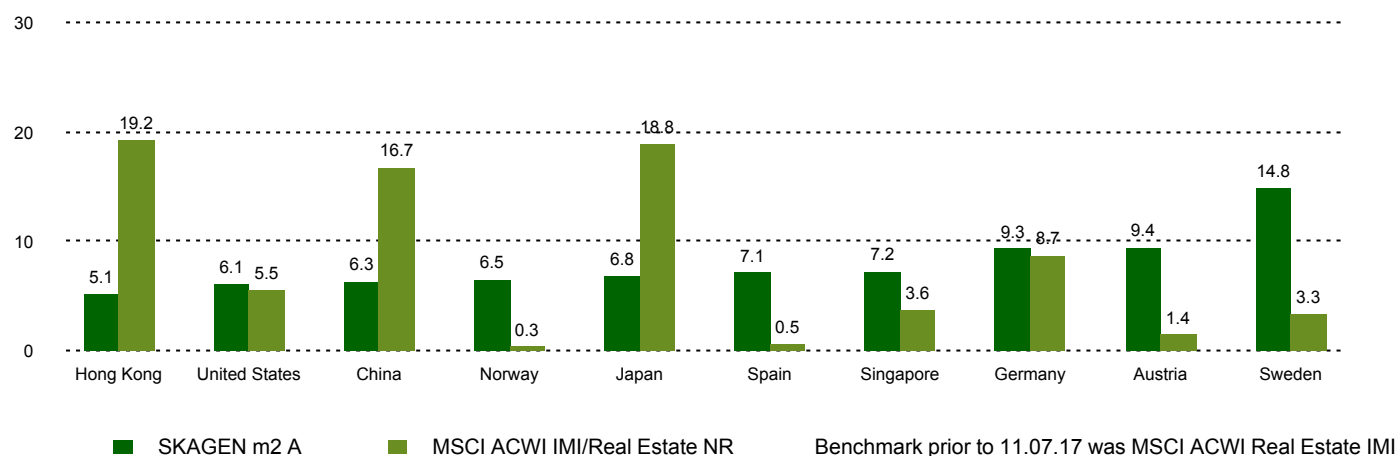
Holding	Weight (%)	Contribution (%)
Mitsui Fudosan	5.34	-0.67
SL Green Realty	3.97	-0.38
D Carnegie & Co	6.49	-0.25
Columbia Property Trust	2.87	-0.20
Ascendas India Trust	1.82	-0.17

Absolute contribution based on NOK returns at fund level

Top ten investments

Holding	Sector	Country	%
Catena	Real Estate	Sweden	6.0
D Carnegie & Co	Real Estate	Sweden	6.0
Deutsche Wohnen	Real Estate	Germany	5.9
Mitsui Fudosan Co	Real Estate	Japan	5.2
Inmobiliaria Colonial	Real Estate	Spain	5.1
Olav Thon Eiendomsselskap	Real Estate	Norway	4.5
Global Logistic Properties	Real Estate	Singapore	4.0
CK Asset Holdings	Real Estate	Hong Kong	3.9
CA Immobilien Anlagen	Real Estate	Austria	3.5
IRSA	Real Estate	Argentina	3.5
Combined weight of top 10 holdings			47.6

Country Exposure (top ten)



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Important information

Unless otherwise stated, performance data relates to class A units and is net of fees. Except otherwise stated, the source of all information is SKAGEN AS. Historical returns are no guarantee for future returns. Future returns will depend, inter alia, on market developments, the fund manager's skills, the fund's risk profile and subscription and management fees. The return may become negative as a result of negative price developments. You can download more information including subscription/redemption forms, full prospectus, Key Investor Information Documents (KIID), General Commercial Terms, Annual Reports and Monthly Reports from our local websites or our local representatives. Statements reflect the portfolio managers' viewpoint at a given time, and this viewpoint may be changed without notice. This report should not be perceived as an offer or recommendation to buy or sell financial instruments. SKAGEN AS does not assume responsibility for direct or indirect loss or expenses incurred through use or understanding of this report. Employees of SKAGEN AS may be owners of securities issued by companies that are either referred to in this report or are part of a fund's portfolio.