

Another strong quarter

SKAGEN m2 had another strong quarter and beat its benchmark index in the period. For the first time in the fund's history, SKAGEN m2 is ahead of benchmark over a five-year period.

Emerging market volatility continued during third quarter with enduring trade war fears, a strong US dollar and significant currency movements. The US central bank raised rates for the third time this year and signalled that it would do so again in December. The US economy is strong which has gone a long way in compensating for the higher interest rates among US real estate companies. However, the US interest rate hike has negatively affected the Hong Kong real estate market on top of fears of a Chinese economy slowdown. Japanese and European real estate markets are strongest year to date, while Singapore and the UK are the laggards (in USD terms). Despite volatility in emerging markets, the fund has held up well, mainly due to its overweight in solid European names.

Swedish names on top

Our three Swedish portfolio names were among the best performers in Q3, with D Carnegie and Catena coming out on top. The Swedish real estate space rebounded during the quarter on strong rental and capital value growth in first half of the year. D Carnegie, which has changed its name to Hembla, was driven by revaluation gains and the take-out of its peer Victoria Park. Catena continued to perform well on strong underlying fundamentals, driven mainly by e-commerce growth, and hit a new price record at the end of the quarter. Logistic yields are under 6% in Europe for the first time since data collection started in 1992. However, on the positive side, the yield gap for logistics, relative to office and retail, is higher than in the previous cycle. Catena is set to take advantage of increased penetration of e-commerce in Sweden with its strategically located and technologically advanced logistic facilities. The German commercial operator and consolidator Aroundtown also performed well during the period, driven by strong rental growth especially in Berlin where supply fails to meet demand. In Germany's seven big cities, vacancy came down to 4.3% on average in Q3, with Berlin at 3.4%. After many years of flat development, rental growth is in a strong rebound phase.

Aroundtown's assets are under-rented with clear upside in leasing revision and vacancy reduction. The company is a good example of SKAGEN m2's strategy of investing in portfolio companies that actively work with value creation in the assets backed by stable cash flow streams from standing assets. Among the top ten best contributors, only one was a non-European name.

Hong Kong and emerging markets weak

The worst contributor in the period was Hong Kong based hotel operator Shangri-La. The Hong Kong real estate market has been sluggish in Q3 due to a number of factors including Chinese trade war fears, tightening of credits in China, further sector tightening policies and interest hikes in the US. Shangri-La's operational metrics have trended in the right direction in the most important markets, however unfavourable currency developments have been a drag.

The second worst performer is also a hotel operator, namely Spanish Melia hotels. The main reason for the decline is that Spain's tourist sector is showing signs of a slowdown. The Indian shopping mall operator Phoenix Mills had a tough quarter, mainly due to unfavourable movements in the Indian rupee but also due to concerns around higher interest rates and credit tightening. Five of the worst performers in the quarter were Hong Kong listed names, all with even deeper discount to substance value.

Hiked interest rates but real estate still going strong

The general conditions for real estate continue to be favourable despite rising interest rates, primarily due to healthy and expanding economies in selective markets. In these markets, of which Europe and the US are good examples, underlying EPS and net asset value growth remain positive, supported by robust operating performance, falling financing rates and deleveraging. With some exceptions, like the Hong Kong residential market, yield spreads are still very wide seen from a historical context. An increasing trend of capital management initiatives, like share buy backs and hiked dividends are also positive.



Although Shangri-La's operational metrics have trended in the right direction, unfavourable currency developments have been a drag. Photo: Unsplash



The Swedish real estate space rebounded during the quarter and D Carnegie was one of the top performers in Q3. Photo: D Carnegie

Outlook

SKAGEN m2 maintains its philosophy of investing in companies with embedded growth models less affected yield movements. There is still good rent reversion potential in many companies, meaning the spread between the companies' current rent-roll and market rents. The difference between valuations in direct real estate and listed are still wide, implying that we will see further M&A transactions in the listed market during the year.

Transactions are increasingly driven by private equity with deep pockets and a long-term perspective. A good example is SKAGEN m2's US holding Columbia Property Trust that is said to have been approached by parties with a take-out interest. This comes after several US real estate company take-outs over the last twelve months. Company valuations in m2 are mainly in line with or lower than historical averages relative to substance value.

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.

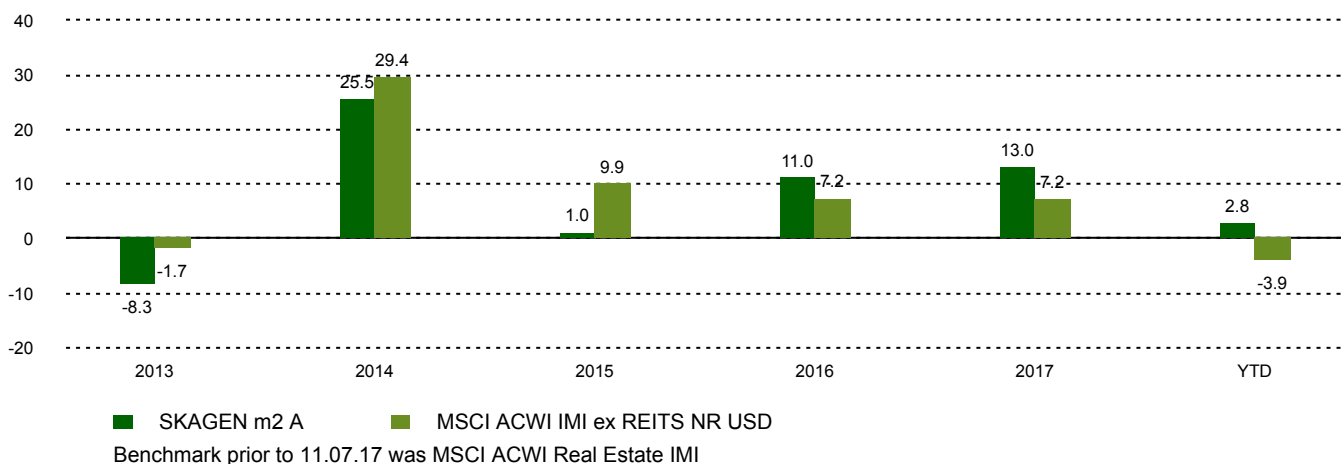
Historical performance (net of fees)

Period	SKAGEN m2 A	Benchmark index
Last month	-0.8%	-2.9%
Quarter to date	0.8%	-3.5%
Year to date	2.8%	-3.9%
Last year	7.6%	-1.1%
Last 3 years	11.1%	5.9%
Last 5 years	9.6%	8.9%
Last 10 years	n/a	n/a
Since start	7.5%	8.2%

Fund Facts

Type	Equity
Domicile	Norway
Launch date	31.10.2012
Morningstar category	Property - Indirect Global
ISIN	NO0010657356
NAV	20.73 EUR
Fixed management fee	1.50%
Total expense ratio (2017)	2.05%
Benchmark index	MSCI ACWI IMI ex REITS NR USD
AUM (mill.)	143.22 EUR
Number of holdings	30
Portfolio manager	Michael Gobitschek

Performance last ten years



Contributors in the quarter



Largest contributors

Holding	Weight (%)	Contribution (%)
D Carnegie & Co AB	7.36	1.12
Catena AB	7.47	1.00
Aroundtown SA	4.44	0.36
Atrium Ljungberg AB	2.82	0.33
CA Immobilien Anlagen AG	4.89	0.30



Largest detractors

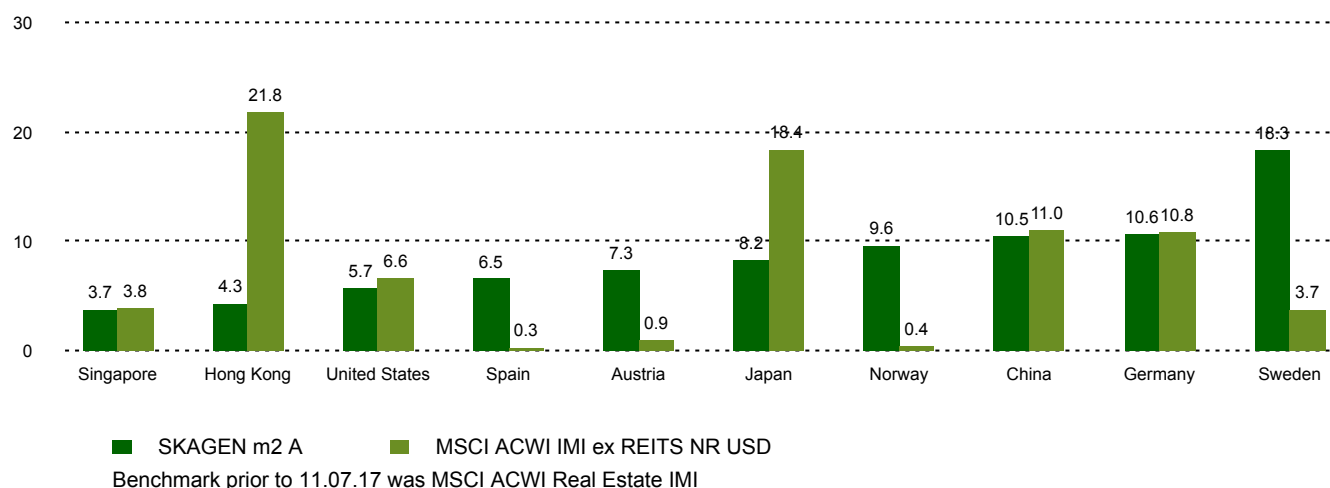
Holding	Weight (%)	Contribution (%)
Shangri-La Asia Ltd	2.36	-0.55
Melia Hotels International SA	2.72	-0.55
Phoenix Mills Ltd/The	1.92	-0.46
Sekisui House Ltd	2.25	-0.30
Inmobiliaria Colonial Socimi S	3.93	-0.25

Absolute contribution based on NOK returns at fund level

Top ten investments

Holding	Sector	Country	%
Catena	Real Estate	Sweden	7.9
D Carnegie & Co	Real Estate	Sweden	7.8
Mitsui Fudosan Co	Real Estate	Japan	5.9
Deutsche Wohnen	Real Estate	Germany	5.8
CA Immobilien Anlagen	Real Estate	Austria	5.0
Aroundtown SA	Real Estate	Germany	4.8
Inmobiliaria Colonial	Real Estate	Spain	3.8
CapitaLand	Real Estate	Singapore	3.7
Kojamo Oyj	Real Estate	Finland	3.6
Olav Thon Eiendomsselskap	Real Estate	Norway	3.5
Combined weight of top 10 holdings			51.9

Country Exposure (top ten)



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Important information

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