

## Real estate under pressure

The stock markets in general experienced a great deal of volatility in the first quarter and real estate companies were no exception. The sector came under pressure mainly in the US and Europe from surging yield curves, reflecting a rotation away from perceived 'bond proxies' as investors anticipate quicker rate rises. At the end of the quarter yields came down again, reinforcing the real estate sector, but this was counterbalanced by fears of a trade war. Further fears of rising interest rates will eventually drive the cost of capital higher. Normally this de-rates equity and real estate valuations as investors steer away from sectors they perceive as bond proxies. However, the fear of rising rates in the sector is mainly unwarranted in the longer run. The real estate sector is more than just a bond proxy. What makes real estate different from bonds is their intrinsic embedded growth rate. This growth is driven by rental growth, which is structurally driven by the inflation rate, the demand-supply imbalance, and the good health of the local economy, in particular employment and easy credit, where the assets are situated. Real estate stocks are a natural hedge against inflation, and more importantly a genuine asset class that has delivered good total return over time.

In the first quarter SKAGEN m2 lagged its benchmark slightly. The main reason for this was the strong performance in Japan where the fund has an underweight, in addition to unfavourable currency movements with a weak EUR and strong JPY. However, SKAGEN m2 continues to

outperform most global real estate peers.

### Key contributors

The best contributor during the period was Spanish commercial operator Inmobiliaria Colonial. Colonial reported good results and was successful in pursuing the acquisition of Axiare, which will provide the company with new sources of growth. The prospects for Madrid and Barcelona offices remain compelling, and Colonial is well-positioned to benefit through its quality portfolio and redevelopment ability. The second best contributor was Austrian commercial operator CA Immobilien Anlagen after a strong report but the main reason was a partial bid from Starwood, simultaneously also announcing a partial bid for another SKAGEN m2 holding, Immofinanz. The third best contributor was Indian residential developer Oberoi Realty which we exited at an all-time high level.

The largest detractor in the quarter was Argentinian IRSA after strong performance last year. This was despite a report in line with expectations, some positive news about land plot acquisition and a share buyback program from its parent company. Despite a decent report, the Norwegian retail operator Olav Thon was a poor performer in the quarter due to general pressure on the Norwegian real estate sector and retail segment.



SKAGEN m2 added a new position, German Aroundtown, which is the largest listed German commercial operator. Photo: Unsplash

### Portfolio activity

SKAGEN m2 added a new position, German Aroundtown, which is the largest listed German commercial operator also present in the Netherlands. The portfolio includes mainly offices, hotels and a 38% stake in the listed rental residential operator Grand City Properties. The strategy is to acquire value added assets, which are generally mismanaged or with funding difficulties in affluent locations, and turn around the cash flow and growth profile to maximise value and set up a stable cash flow stream. The company has now passed certain data points and appears more robust than before. With the majority of the portfolio clearly under-rented, Aroundtown is a key beneficiary of a potential market recovery in Germany. In an improving market environment, the strategy reduces operational risk and allows attractive returns through active asset management even without fast external growth. Indications of rental growth have been evident across some German cities to varying degrees, driven by declining vacancy rates, strong employment growth and significant office to residential conversion volumes.

At the same time as entering this position, we sold out of German office operator DIC Real Estate at very good levels. During the quarter, we also exited the Austrian residential operator Buwog after a bid from German residential operator Vonovia.



The best contributor during the period was Spanish commercial operator Inmobiliaria Colonial. Photo: Unsplash

### Outlook

The general conditions for real estate continue to be favourable with low interest rates and expanding economies synchronised globally. For real estate companies in general, underlying EPS and net asset value growth remains strong, supported by robust operating performance, falling financing rates and deleveraging. There are few signs that higher cost of capital has eroded asset values. SKAGEN m2 maintains its philosophy of investing in companies with embedded growth. 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 and listed real estate are still wide, implying that we will see further M&A transactions in the listed market during the year, already seen in two SKAGEN m2 companies so far. In many market or segments, company valuations are in line with or lower than historical averages relative to substance. Valuations in many companies are backed by good demand driven rental growth and low vacancies.

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.

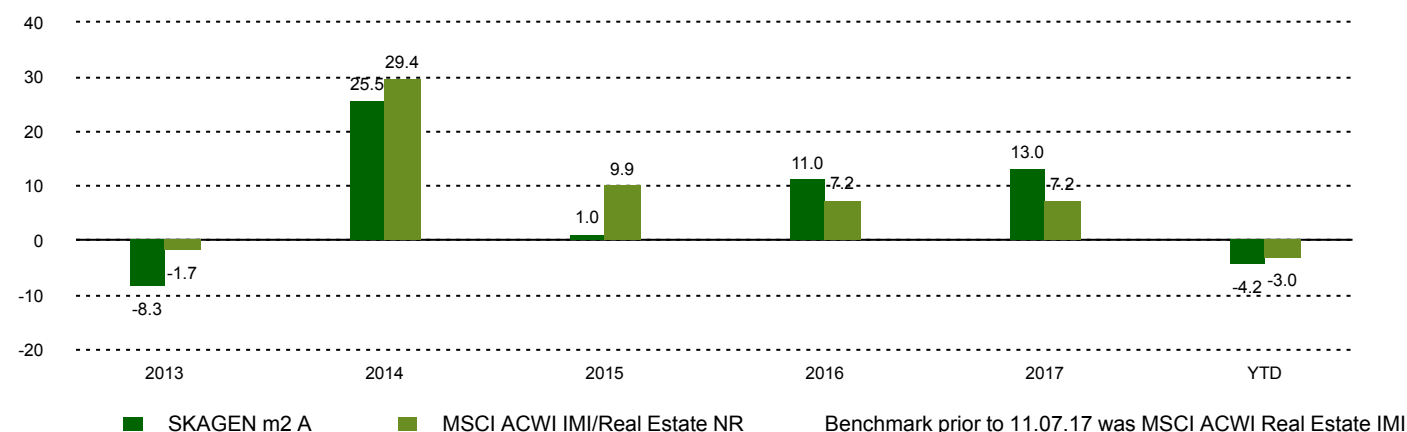
## Historical performance (net of fees)

Period	SKAGEN m2 A	Benchmark index
Last month	-1.8%	-1.3%
Quarter to date	-4.2%	-3.0%
Year to date	-4.2%	-3.0%
Last year	5.8%	1.1%
Last 3 years	1.2%	1.3%
Last 5 years	4.8%	7.1%
Last 10 years	n/a	n/a
Since start	6.8%	9.2%

## Fund Facts

Type	Equity
Domicile	Norway
Launch date	31.10.2012
Morningstar category	Property - Indirect Global
ISIN	NO0010657356
NAV	19.32 EUR
Fixed management fee	1.50%
Total expense ratio (2017)	2.05%
Benchmark index	MSCI ACWI IMI/Real Estate NR
AUM (mill.)	129.81 EUR
Number of holdings	29
Lead manager	Michael Gobitschek

## Performance last ten years



## Contributors in the quarter



### Largest contributors

Holding	Weight (%)	Contribution (%)
Inmobiliaria Colonial Socimi S	4.91	0.35
CA Immobilien Anlagen AG	4.15	0.19
Oberoi Realty Ltd	0.69	0.07
Aroundtown SA	1.60	0.05
Deutsche Wohnen SE	6.44	0.04



### Largest detractors

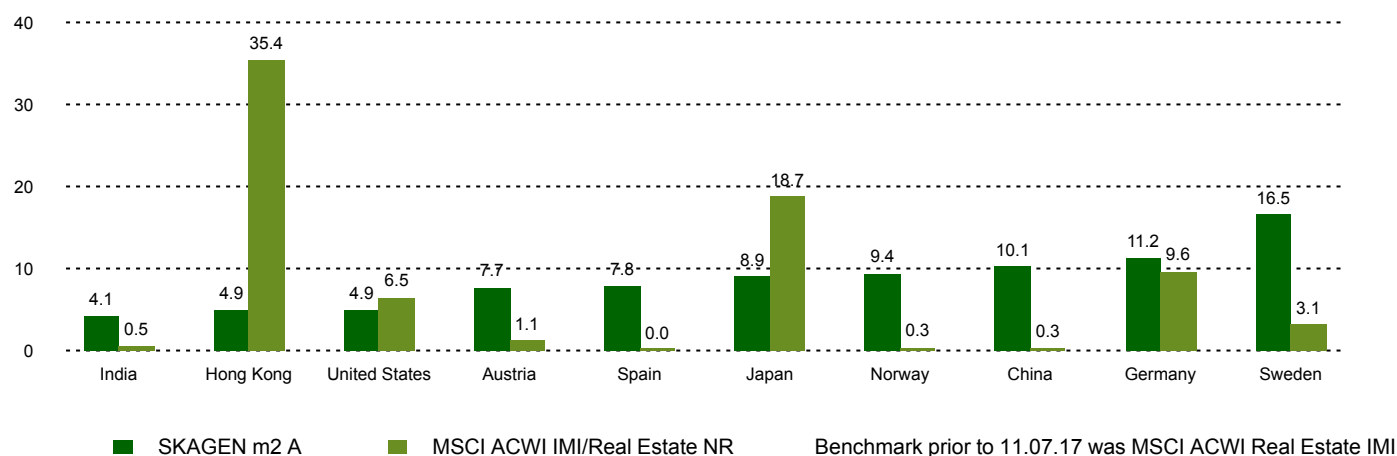
Holding	Weight (%)	Contribution (%)
IRSA Inversiones y Representac	3.54	-0.94
Olav Thon Eiendomsselskap ASA	3.87	-0.48
Shangri-La Asia Ltd	2.35	-0.47
Catena AB	7.08	-0.42
Columbia Property Trust Inc	2.53	-0.41

Absolute contribution based on NOK returns at fund level

## Top ten investments

Holding	Sector	Country	%
Deutsche Wohnen	Real Estate	Germany	7.2
Catena	Real Estate	Sweden	6.9
Mitsui Fudosan Co	Real Estate	Japan	6.4
D Carnegie & Co	Real Estate	Sweden	6.0
Inmobiliaria Colonial	Real Estate	Spain	4.9
CA Immobilien Anlagen	Real Estate	Austria	4.9
Aroundtown SA	Real Estate	Germany	4.0
Sun Hung Kai Properties	Real Estate	China	3.7
CK Asset Holdings	Real Estate	Hong Kong	3.7
CapitaLand	Real Estate	Singapore	3.7
Combined weight of top 10 holdings			51.4

## Country Exposure (top ten)



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