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Real Estate in a post-Covid world

20 October 2020

This document is for investment professionals only and should not be relied upon by private investors.

About Sarasin & Partners

A staff of 217 including 89 investment professionals

Funds under management: c. £15.2bn*

A broad range of domestic and overseas private clients, charities, pension funds, institutions and retail investors

Combined local management team owns a significant portion of the equity of the firm

A committed team of investment professionals in the foreground

* Source Sarasin & Partners LLP as at 30.09.2020, updated quarterly

Sarasin Global Listed Real Estate

Our macro team helps define regional and sector exposure

REITs and global listed property companies have tax/cost efficient corporate structures with access to a variety of funding sources

Drawing on the expertise of a specialist **risk** team, managers ensure that risk within the portfolio is **managed appropriately**

Allows investors to move freely and cost effectively between regions and property sectors

Sarasin & Partners was one of the first European investors to develop a global listed real estate product

Some of the highest quality real estate is only available via listed stocks

Within the Real Estate franchise we have over *£270m* assets under management (as at 30.09.20)

Our Real Estate GBP Fund launched in *2004* A strong fund management team combining over 30 years of experience

JLL

Our direct research consultant, Jones Lang Lasalle has 200+ offices, operates in 1000 locations in 71 countries

Real Estate Team – Key members

Raymond Lahaut

Analyst / Portfolio Manager, Global Real Estate

- Over 15 years' experience as a portfolio manager in real estate sector
- Bachelor's degree in Marketing (Limburg Business School)
- Masters in Marketing and Marketing Research (University of Nijmegen)
- Chartered Financial Analyst (CFA)

Phil Collins

Co-Fund Manager, Global Real Estate

- Over 30 years' investment experience
- Lead manager of Sarasin's Multi-Asset Charity funds.
- Fellow of the Chartered Institute for Securities & Investment

Ben Elwes

Co-Fund Manager, Global Real Estate

- UK Equity Fund Manager & Analyst
- Nearly 30 years' investment experience
- Degree in Economics and Politics from Bristol University
- Member of the CFA Institute

Thematic & Strategic Analysts

Digitalisation | **Urbanisation** | **New Commerce** | **Self Storage** | **Healthcare** | **Student Housing**

Macro | **Strategy** | **Geopolitics** | **Jones Lang LaSalle** | **Risk Team**

Agenda

1. Listed Real Estate Performance Review YtD.
2. How we are different in our approach: Thematic Investing.
3. Topical: Real Estate in a (post) Covid world - and the impact this may have on our strategy.
4. Outlook Listed Real Estate.

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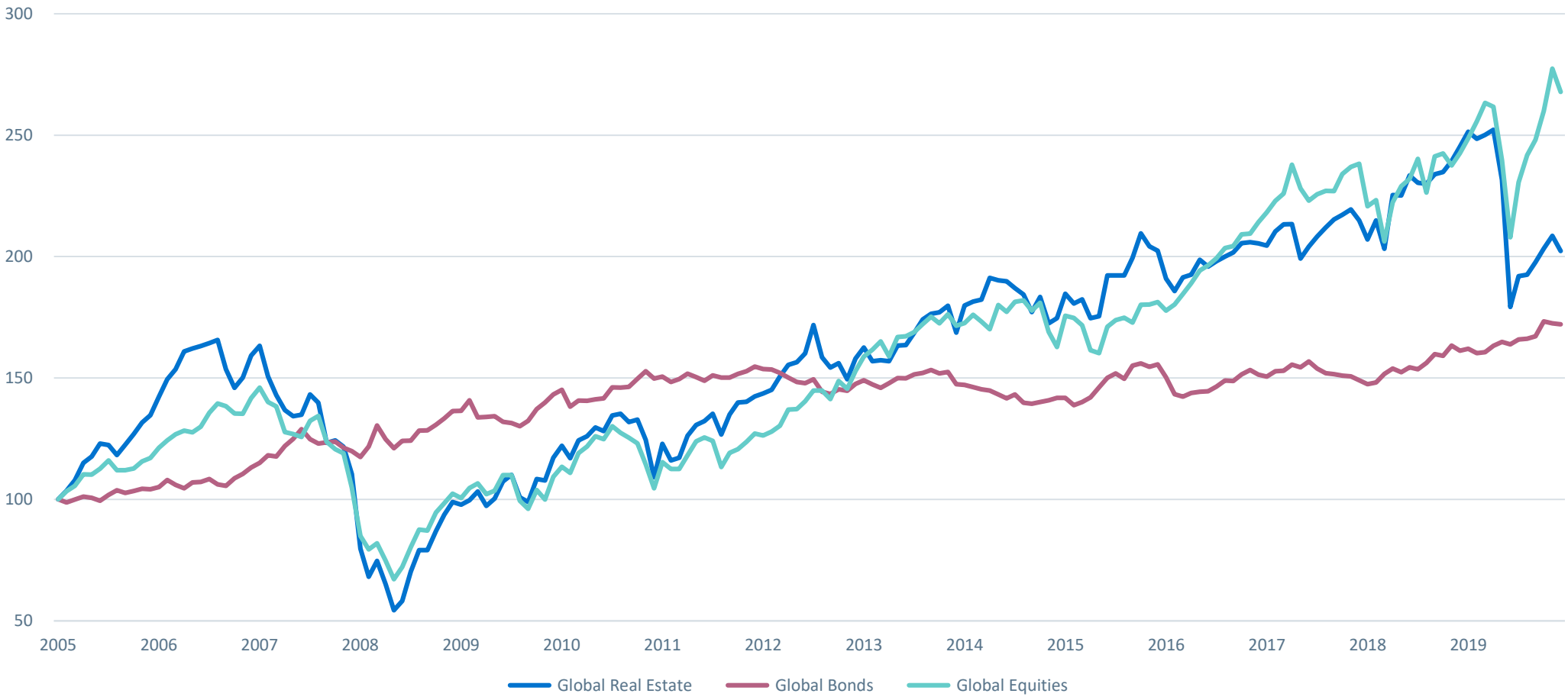
01 Review of 2020 YtD

REIT sector returns

Listed Real Estate vs. Global Equities and Bonds



Source: Sarasin, Bloomberg 30.09.2020

2020 YtD Review

Lagging general equity (in GBP); Outperformance YtD

	Relative	Fund	Benchmark
Q3 Performance	-2.4%	-4.1%	-1.7%
YTD Performance	+1.0%	-14.6%	-15.6%

Positives:

- Being overweight the Industrial sector (Goodman in AU and Prologis in US)
- Being overweight German Residential (Deutsche Wohnen and LEG Immobilien)
- Being overweight Digitalisation theme (Equinix and American Tower in US)
- Being underweight Hotels
- Being underweight Healthcare

Negatives:

- Being overweight US Residential
- Being overweight European Retail
- Being underweight Self Storage

Source: P Share Class/Net of Fees from I Shares

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02

How we are different in our approach: Thematic Investing

Investment philosophy

Thematic	Maximises exposure to structural growth trends across sectors and geographies
Sustainable	ESG embedded, active ownership, impactful policy outreach improves financial outcomes and contributes responsibly to society
Active	Best approach to delivering on objectives over the long-term

The best of both worlds

Solid dividend yield combined with NAV growth

Dividend plus NAV growth

Income

- Best real estate assets around the world
- Most attractive locations/sectors
- Best REIT management teams
- Stable and growing income
- Total return target: 5% - 8%

Thematic

- Exposure to long-term themes
- Growing companies/ NAVs
- Total return target: 10% - 15%

Allocation

	Allocation	Yield
Diversified	12.3%	2.69%
Office	11.1%	5.14%
Residential	12.0%	3.25%
Retail	9.2%	7.51%
	44.6%	4.44%

	Allocation	Yield
Digitalisation	10.7%	
Healthcare	6.5%	
Industrial	14.2%	
Self Storage	2.1%	
Student Housing	2.6%	
Urbanisation	18.0%	
	54.1%	2.8%

Best opportunities, best-in-class real estate managers

- Income portfolio focused on stable dividend generation and global exposure.
- Thematic part of the portfolio focuses on stronger NAV growth.
- Portfolio construction based on conviction not on benchmark.
- Expected dividend yield: 3.0% - 4.0% (now 3.7% vs Benchmark yield of 4.4%).

Source: Sarasin & Partners LLP, September 2020

Real Estate investment process – Thematic pillar

1

Theme

The identification of:

- Long-term themes (mobility of population, ageing population, etc.)
- Special situations (industry contacts, conferences, etc.)
- Turnaround situations (undermanaged portfolio, new management team, etc.)

2

Company analysis

- Narrow the universe of as a result of Step 1
- Qualitative research on the quality of the portfolio (location, quality, etc.)
- Qualitative research on the quality of the management team
- Financial analysis on the stock and its valuation.

3

Portfolio construction

- Allocation based on risk/return expectation
- Constant review

Step 1: The identification of long-term themes

Identifying the long-term inexorable trends that will shape the world in which we live and invest.

Uncovering the real estate companies best placed to benefit from these long-term themes.

Filtering these ideas down to the very best investment opportunities in real estate.

A philosophy which has been at the heart of Sarasin's process for over 15 years.

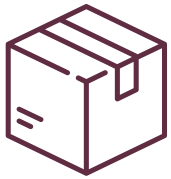
DIGITALISATION

URBANISATION

NEW COMMERCE

HEALTHCARE

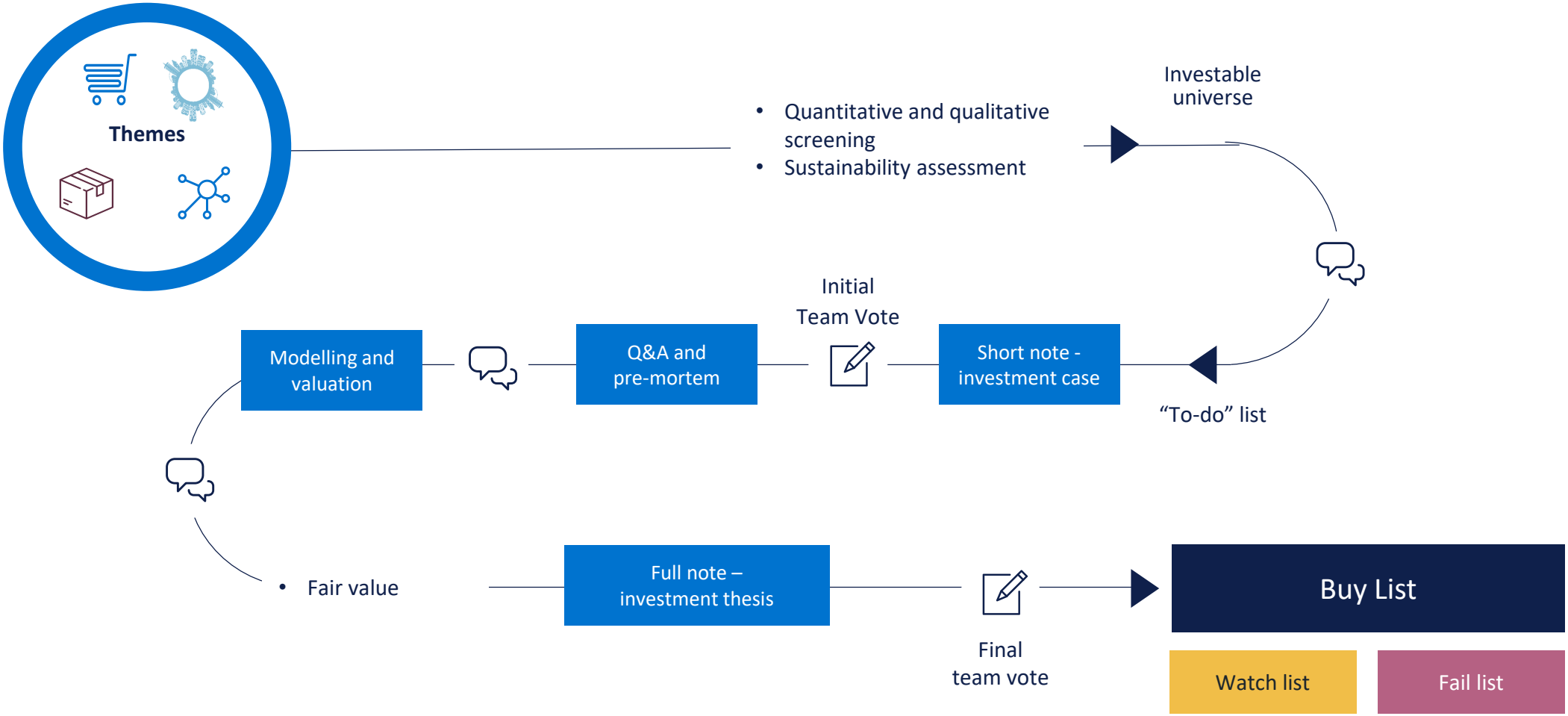
SELF STORAGE



STUDENT HOUSING

Step 2: Company Analysis

Research process



Real estate buy list

- c.80 companies under coverage
- c. 30-35 companies in portfolio

Step 3: Portfolio construction

Review and sell discipline

Review and monitoring

Continuous investment case review

- Thematic credentials
- Investment edge
- Sustainable advantage
- Analyst rating and valuation
- Quantitative trigger

Ownership monitoring

- Engagement outcomes
- Material ESG risks
- Escalation protocols

Penalty box process

- Financial re-model
- Fresh-eyes analyst
- External inputs
- Quant analysis
- Re-state investment case

Sell discipline

- Stock fails penalty box
- Share prices exceeds fair value
- Unsatisfactory company engagement

Holdings may be sold in favour of superior ideas

Factor, style or correlation risk may necessitate adjustments to holdings

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03

Topical: Real Estate in a (post) COVID world - and the impact this may have on our strategy

The best of both worlds

Solid dividend yield combined with NAV growth

Dividend plus NAV growth

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Source: Sarasin & Partners LLP, September 2020

Will income provide income?

Offices: Not 'The End', but demand could decrease and drive polarisation.

Source: iStock, February 2020

For the office sector, the key question is how the lockdown-accelerated trend of working from home (WFH) alters corporates' long-term real estate strategies. There is no doubt that WFH will continue to grow, with many corporates already announcing changes to their real estate strategy. The impact may be stronger where commute times are typically longer and homes typically bigger (e.g. the US).

But…

1. Workspace density now may need to decrease to allow increased social distancing.
2. Shared workstations or 'hot-desking' is now less appealing, and in some cases may be regulated against.
3. A long-term trend in office demand has been for corporates providing quality space to attract and retain talent. This 'flight to quality' is likely to drive polarisation within the market, with lower-grade, grey (i.e. non-sustainable buildings) and peripheral assets likely to lose.
4. WFH will not appeal to all employees
5. There will be many roles that aren't allowed to move to a home location for security and insurance purposes.
6. On top of these factors are the 'softer' social benefits that draw us to office working: team building, bonding, relationships, talent mentoring, corporate culture building, efficiency, management oversight, creative collaboration etc.

Will income provide income?

Retail: Accelerating downward trends

The Ten Plagues of Retail

1. Online retail
2. CVAs
3. Lockdowns
4. Tenants not paying the rent
5. Rents going down
6. Values going down
7. LtVs going up (=issue new shares)
8. Retailers downsizing
9. Most retail REITs are trying to sell
10. The 'must hate' sector

Source: Pixabay, October 2020

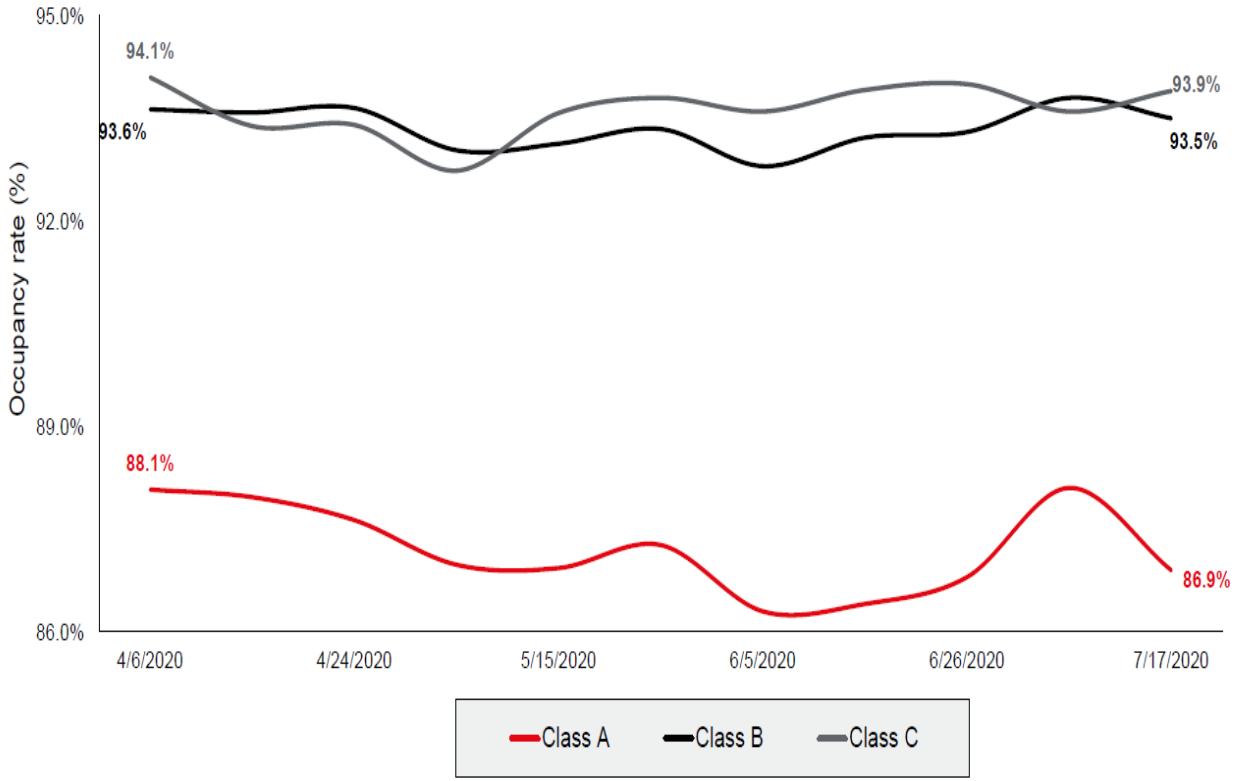
Never again retail?

Although retail real estate is (and has been) hardest hit by structural changes and by the impact of Covid, it is perhaps too easy (and unwise) to disregard the sector altogether. We should remember that although online retail is on the up, more than 70-75% of all sales are still done in bricks and mortar shops. Retail as we know it has definitely changed and that change has not yet finished but some retail landlords will come out on top once the dust has settled.

Will income provide income?

Residential: Steady as you were

Although there are many challenges in the housing market (ageing of society, (de-)urbanisation and energy efficiency to name but a few), COVID is not one of them. Across the developed world, residential landlords have seen limited impact on their portfolios, be it on occupancy, rent collection or values. The sector is still going strong.



Source: Occupancy rates US Residential stock, JLL (July 2020).

Has Covid impacted our six themes?

The Good

DIGITALISATION

Datacentres and Towers: The lighthouse in the storm

The data centre providers have been by far the best performing real estate subsector due to:

1. The sector's **growth profile**, coupled with solid balance sheets.
2. While some other sectors have sold off aggressively due to concerns over tenant issues/liquidity, data centres have been untouched in this regard as their largest **tenants are of the highest credit quality** (Microsoft, Salesforce, Facebook etc.).
3. The sectors are likely to continue to benefit as **workplaces become more agile, flexible and cloud-based** in a post-Covid world, with rising data usage and increased carrier activity.

NEW COMMERCE

I = R * -1

The same e-commerce trends that threaten the retail sector are likely to benefit logistics. The growing of ecommerce is actually only one of the upside themes providing the industrial sector with a tailwind and Covid has made that tailwind a tail storm.

1. **Higher Inventory Levels**: each 100bps of growth in inventories is estimated to require an additional 57M Sft of US logistics demand.
2. **Modernization of logistics supply chains**: Faster e-commerce adoption should require greater supply chain investments from low-penetration industries such as grocery.

Has Covid impacted our six themes?

The Mixed Bag

HEALTHCARE

Senior Housing

1. Increased number of ‘involuntary move-outs’.
2. Increasing cost base.
3. Vacancy may remain high due to hesitance of people moving in.

MOB

1. Increasing demand for specialized office buildings (e.g. laboratories).
2. Not effected by WFH-trend.

Triple Net

No impact

Has Covid impacted our six themes?

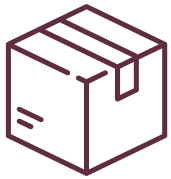
The Question Marks

URBANISATION

Potentially, increased adoption of WFH could change attitudes to commute lengths, changing the location desirability: a longer commute may be more tolerable if only required 2-3 days a week rather than 5. Early indicators show three key trends:

1. **De-densification:** Home sharing may become less popular.
2. **De-urbanisation**: Commuting less often may justify a longer commute.
3. **Sun Belt migration**: Specifically for the US there might be a trend to move to sunnier Sun Belt states like Texas and Florida.

SELF STORAGE



The Self-Storage sector has performed well in 2020, mostly based on its perceived resilient cash flows. Back in the 2009 financial crisis, the Self-Storage REITs were also among the best performers given their strong balance sheets and resilient cash flows. But:

1. **Supply growth** is still near peak levels.
2. **Costs** may continue to go up as Self Storage companies try to outbid one another on marketing for a decreasing number of consumers along with modest growth in labour costs due to increased cleaning/personnel costs as a result of Covid.

STUDENT HOUSING

Binary outcome: will universities offer onsite classes or online classes? The former will result in students moving back to campus. The latter will result in students moving back home.

Conclusion

Change of strategy?

No, but slowly moving to more thematic in the medium to long term.

- Prime office space, safe residential stock and surviving retail should provide solid income/ dividend.
- Bar a few slight changes in long term trends, our thematic approach should continue to deliver above average NAV growth.

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04 Outlook Listed Real Estate

Global Listed Real Estate Outlook

The outlook for most real estate sectors remains cautiously optimistic:

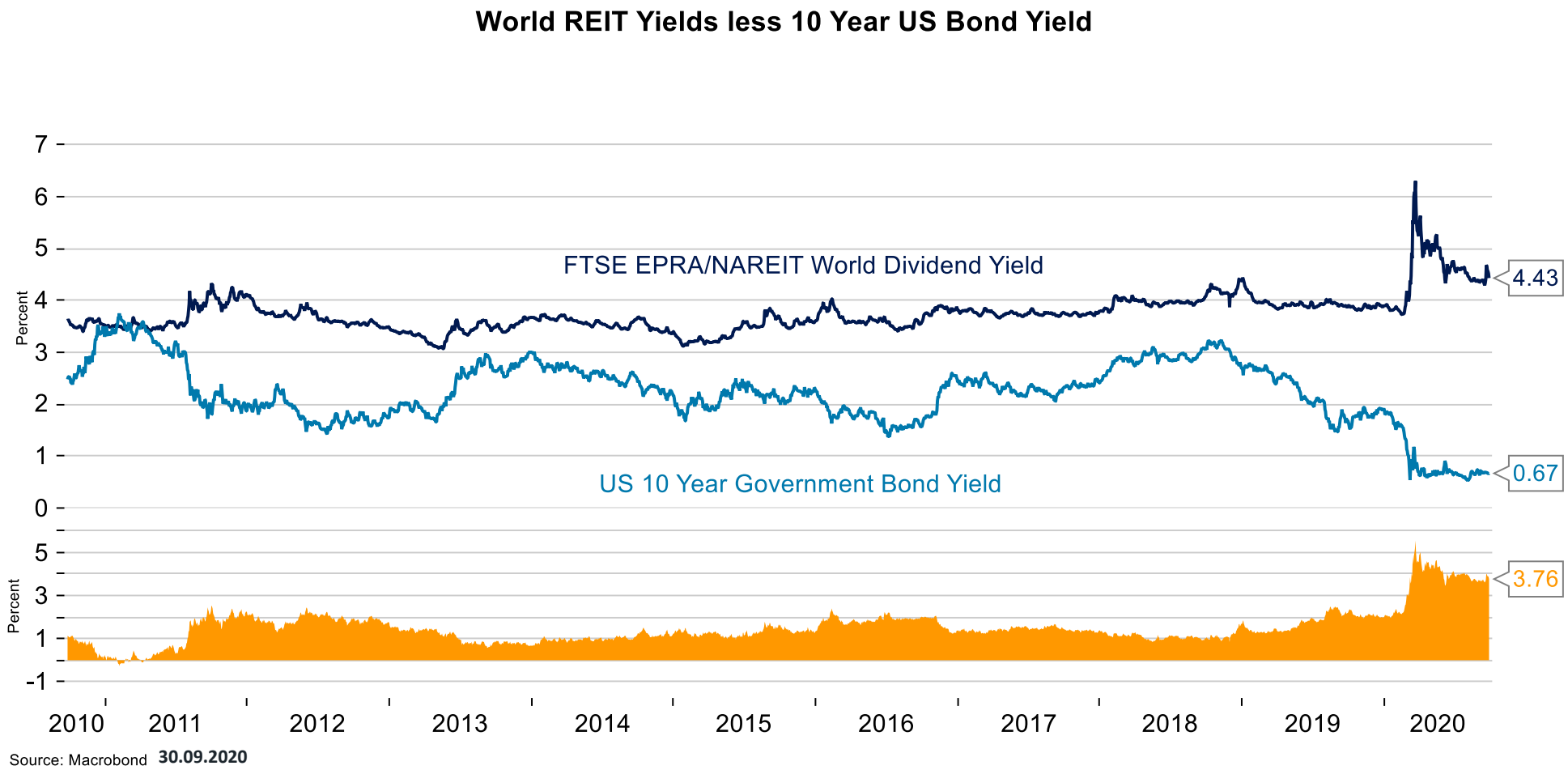
- Real Estate **Office** markets between WFH and social distancing forces.
- Growing emphasis on agility and technology supports rise of flexible office space.
- **Retail** focuses on new ways to differentiate.
- **Logistics** markets maintain strong performance.
- Investors look for scale and target logistics and **Alternative Real Estate** sectors.
- **Non Real Estate Risks** increased: Social unrest in HK, governmental intervention Berlin residential market, Covid-19

Company balance sheets are robust, and financing easy to access at attractive rates.

Yield spreads remain well above average versus 10 year government bonds around the world.

Yield premium on Global REITs approaching decade highs

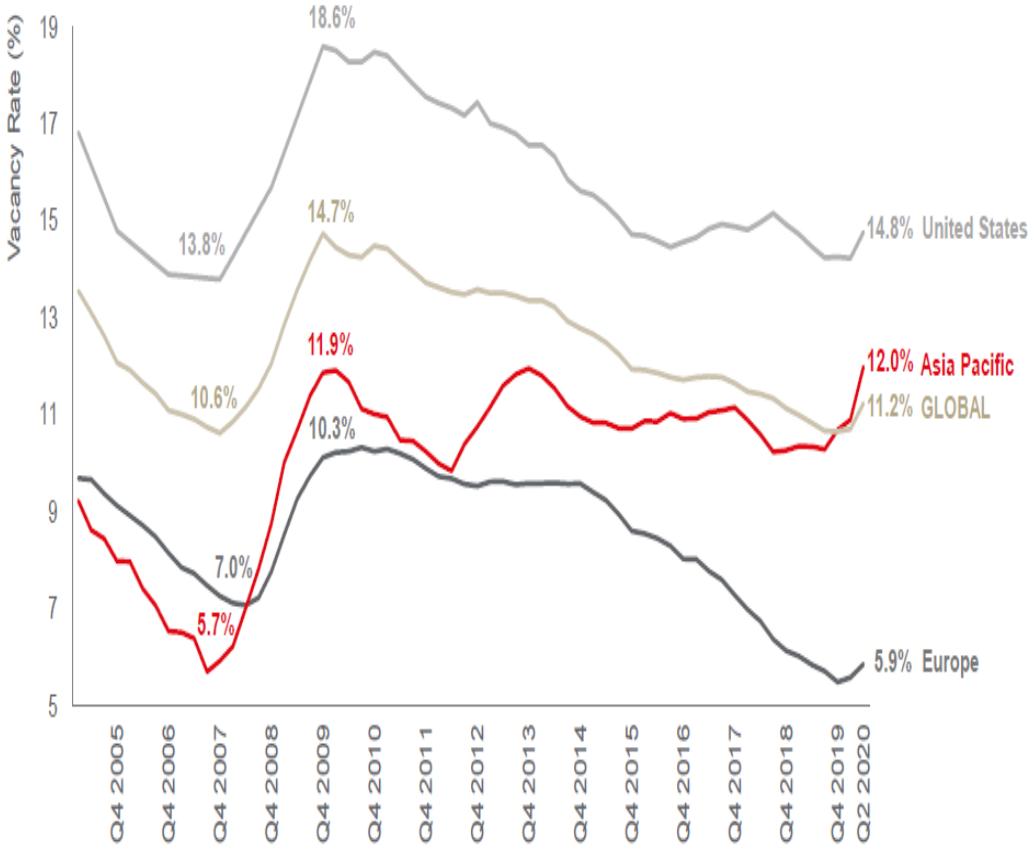
Global REIT and Bond Yields



Outlook and Opportunities

Office

- Vacancy moves higher in all regions. Polarisation between prime and secondary locations.
- Steady office rental growth (indexation) expected for 2020/21.
- Office vacancy rates expected to tick up slightly from historic lows as new developments comes online and due to the impact of Covid-19 and the expected recession.



Portfolio Implications

- Overweight US West Coast, European and developed Asia office sector.
- Underweight Mid America and UK office sector.

Source: Jones Lang LaSalle Global Real Estate; August 2020

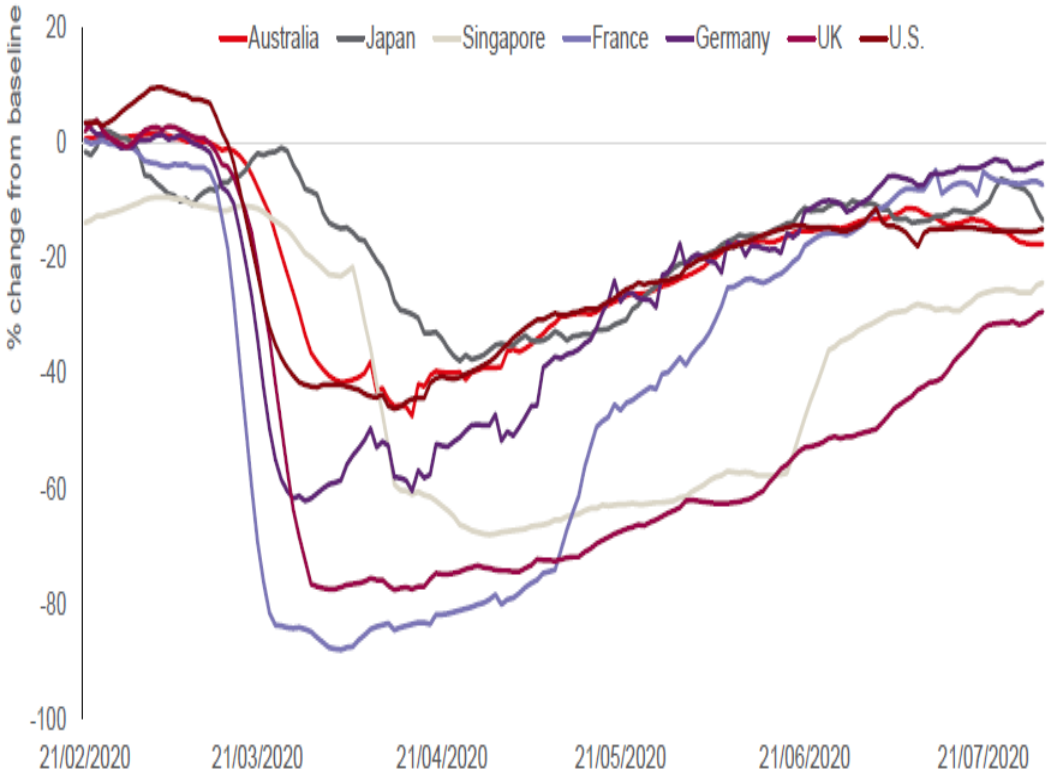
Outlook and Opportunities

Retail

- Longer term looking to offset the loss of revenue from their physical store portfolios (more 'experience' and f&b).
- Increased adoption of online grocery shopping.
- Sector slowly recovering from lockdowns

Portfolio Implications

- Decreased our underweight with focus on long term winners.

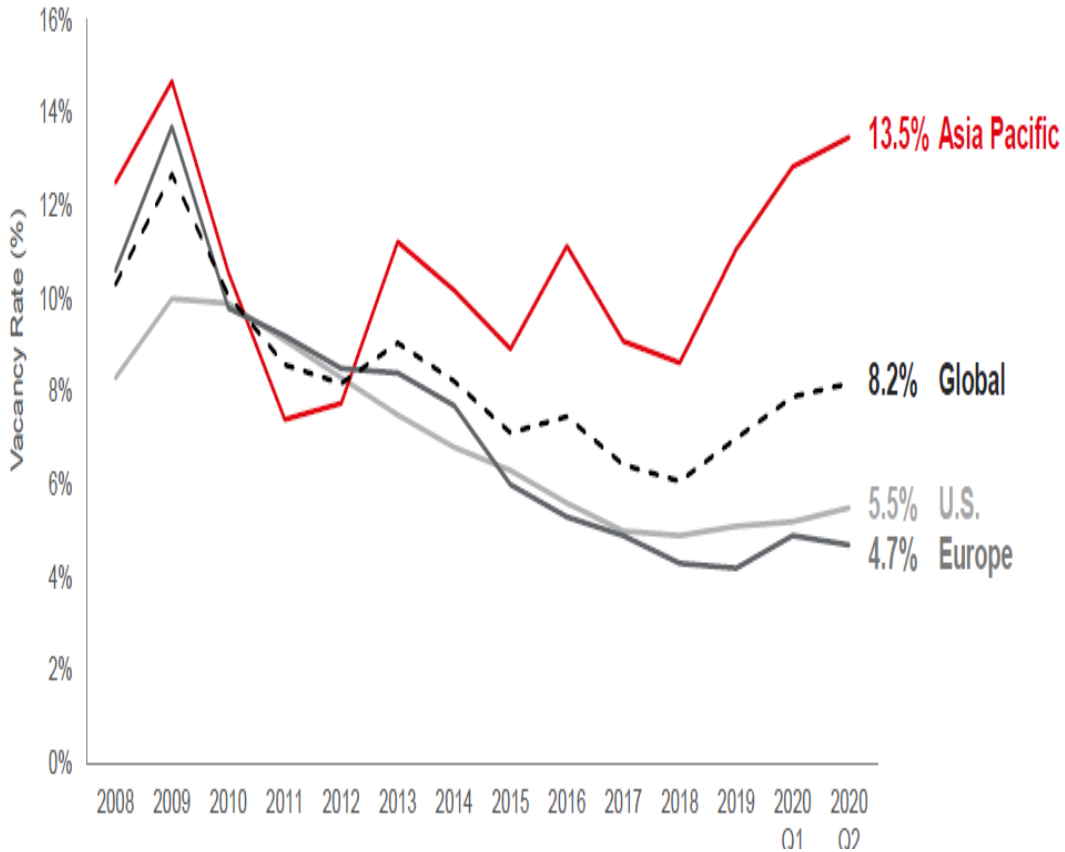


Source: Jones Lang LaSalle Global Real Estate; August 2020

Outlook and Opportunities

Industrial

- Companies with lean supply chains may increase inventories
- Acceleration of existing trend:
  - Online retail (especially grocery)
  - Integration of technology
  - Higher specification
- Supply chain rethink creates additional regional demand:
  - Re-shoring/ near shoring
  - Diversification of sourcing
  - Diversification of transport modes



Portfolio Implications

- Overweight selective logistics stocks due to stock valuations

Source: Jones Lang LaSalle Global Real Estate; August 2020

Outlook and Opportunities

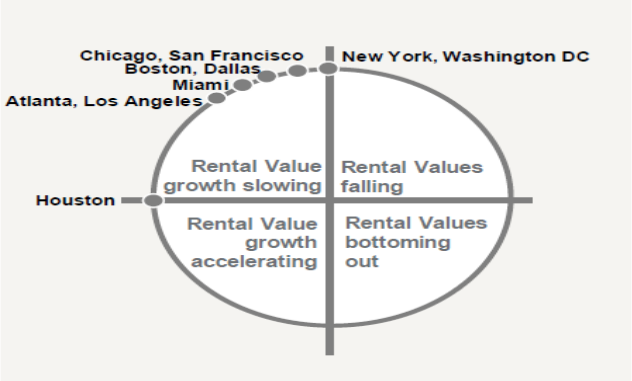
Residential

- Residential sector keeps showing strong rental growth; impact from Covid-19 limited.
- New legislation to cap rents a risk.

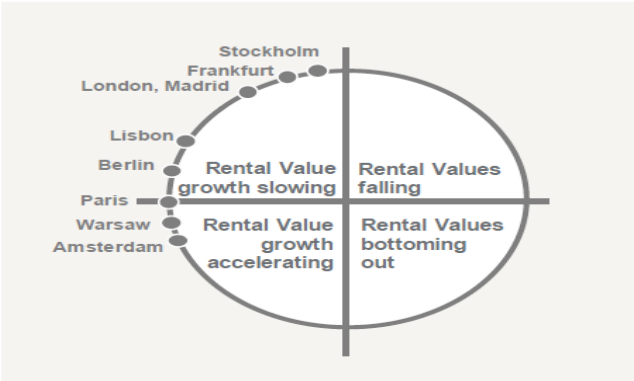
Portfolio Implications

- Overweight East/ West Coast and Sunbelt US and German residential

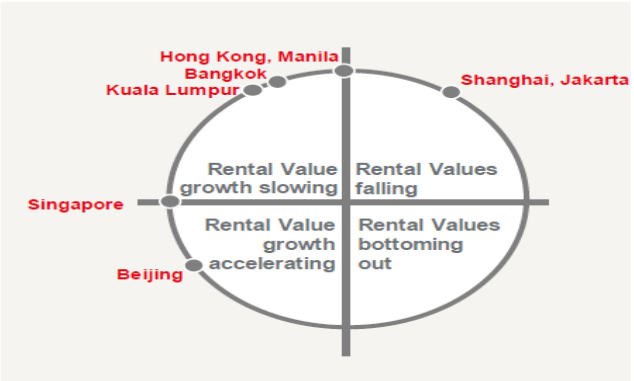
U.S.



EMEA



Asia Pacific



Source: Jones Lang LaSalle Global Real Estate; August 2020

Open, Liquid & Prime

UK Property Funds

Home truths: 80% of open-ended property funds suspended as 'history keeps on repeating itself'
Aviva, Kames and BMO GAM among names to gate products
(source: Investment Week; March 24th).

UK Property Funds Begin to Lift Suspensions
One of the largest open-ended funds in the sector, Threadneedle Property, is to open to investors next week after six months of being gated (Source: Morningstar; September 17th).

Property funds stay shut amid fears of liquidity crunch
Many vehicles remain suspended as managers examine looming redemption requests (source: FT; September 19th).

Sarasin Sustainable Global Real Estate Fund only invests in listed real estate. The fund will always meet redemptions. The Fund also mainly invests in prime real estate globally, whereas the UK property fund are focused on the UK only and have a mix of primary and secondary assets.

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Q&A

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