

September 2020



TRADING PRIVATE REAL ESTATE #2: PRICING

PropertyMatch®

IN ASSOCIATION WITH

DOMINIC SMITH
SENIOR DIRECTOR, UK RESEARCH

CBRE

PRICING & PERFORMANCE: KEY FINDINGS



We are able to create PropertyMatch Indices for funds and groups of funds, using a mix of trade and pricing data.

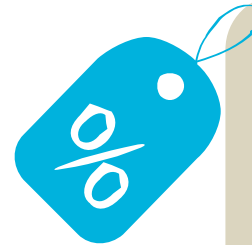


By comparing indices of direct property, REIT and secondary fund pricing, we observe that REIT indices lead the other two, which are strongly correlated.

The PropertyMatch UK Balanced Funds Index price appears cheap relative to the performance of the direct market and given the recent recovery in REITs.



Within the UK Balanced Funds cohort, pricing and performance is highly correlated, suggesting investors may benefit from an opportunistic approach to secondary market pricing rather than more rigid manager selection.



Historically, 1 and 3 year performance has arguably been a little better in periods following purchases at discount than at premium to NAV of UK Balanced funds.

Source: CBRE Research, PropertyMatch.

BACKGROUND

This report on Pricing aspects of the secondary market in private real estate funds is the second in our initial series.

Launching alongside this report are companion pieces looking at Liquidity and Strategy.

All draw on PropertyMatch's unique dataset of £10bn+ of deals and pricing information over ten years.

Further reports will follow in Q4 2020 on these and other aspects of the market, and regular pricing indices will be launched in 2021.



PRICING & PERFORMANCE: CREATING A PRICING SERIES FROM AVAILABLE DATA

With funds not always traded each month, it is necessary if creating a monthly pricing series to use other data where pricing gaps exist. Establishing a hierarchy and relative strength of different data points is important, not least for when fund series are combined.

Data Item(s)	Data Strength Score
Trade month ₀	10
Bid & Offer month ₀	9
Trade month ₁	8
Bid month ₀ and Bid & Offer month ₁ Offer month ₀ and Bid & Offer month ₁	7
Bid & Offer month ₁	6
Trade month ₂	5
Bid month ₁ and Bid & Offer month ₂ Offer month ₁ and Bid & Offer month ₂	4
Bid & Offer month ₂	3
Trade month ₃	2
Bid month ₂ and Bid & Offer month ₃ Offer month ₂ and Bid & Offer month ₃	2
Bid & Offer month ₃	2
Bid month ₃ Offer month ₃	1

In an ideal world, funds would trade every month (if not every day!) and creating a monthly price series at fund level would be simple.

This doesn't occur in reality, and so it is necessary to draw on other data – strong, but less so than actual trading data – to try to establish what pricing would have been had funds traded.

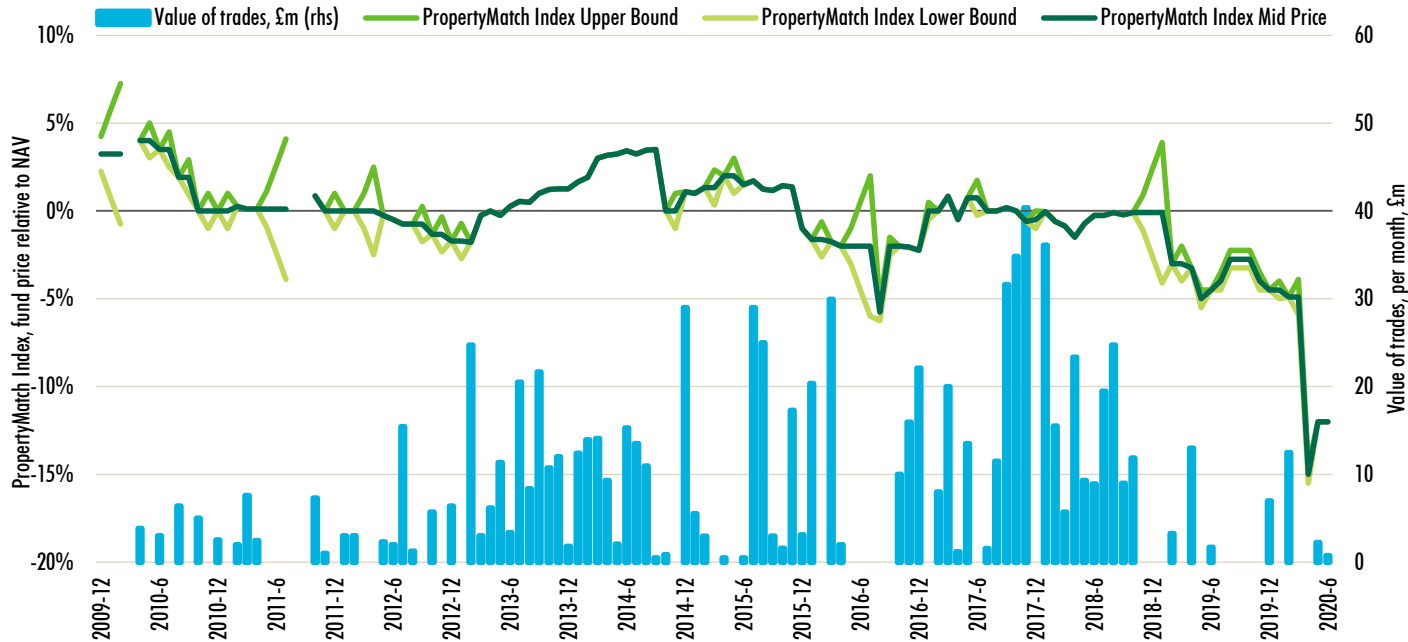
We have set out what we believe is the hierarchy of alternative data sources to a trade in the current month, as well as the relative value of those different data sources. This latter is useful to establish a margin of error around fund series and around amalgamated series seeking to combine a number of funds – it allows us to avoid false equivalencies by showing the extent to which data at different points for the same fund and / or different funds at the same time is more or less reflective of traded reality.

There is a danger of over-complicating matters in coming up with a methodology like this, and we have tried to combine rigour with simplicity. Overall, we have (as hopefully would be expected) placed greater value on trading data over pricing data, and greater value on current data rather than historic data.

Source: CBRE Research, PropertyMatch.

PROPERTYMATCH INDEX, FUND LEVEL, EXAMPLE OF BLACKROCK UK PROPERTY FUND

Using the example of BlackRock UK Property Fund, we can see (for a very liquid fund) how the PropertyMatch Index price has evolved over time, and how at certain points a lack of liquidity leads to an increase in uncertainty of the Index price



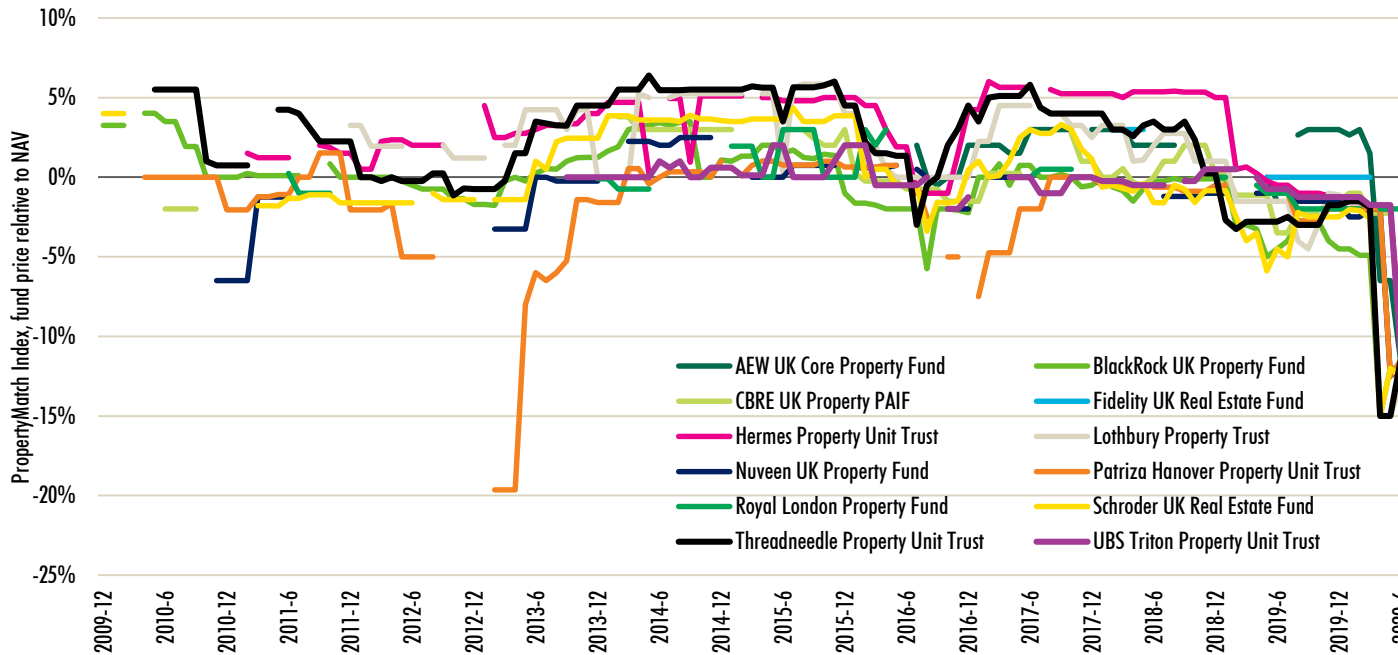
The chart demonstrates the PropertyMatch Index for the BlackRock UK Property Fund as it is arguably the most frequently traded, and it is therefore unsurprising to see only two very short periods at the beginning of the history where no Index can be produced.

Aside from these blips (in early 2010 and late 2011) there is a high degree of confidence in the Index mid price, as illustrated by the relatively narrow Upper and Lower Bounds. Two periods stand out as uncertain – the time around the Brexit referendum and early 2019. However, the current Covid-19 crisis has not heralded such a period – although it has seen pricing fall to a record low.

Source: CBRE Research, PropertyMatch.

PROPERTYMATCH INDEX, FUND LEVEL, 12 UK BALANCED FUNDS

The PropertyMatch Index for 12 UK Balanced funds shows a high degree of synchronicity in pricing movement, but a fairly wide range of premium/discount to NAV through time.



The chart shows the PropertyMatch Index for 12 UK Balanced funds for which there is sufficient trade, pricing and NAV data (the latter from MSCI/AREF). For reasons of clarity we only show the mid-point of each fund Index, not their Upper and Lower Bounds.

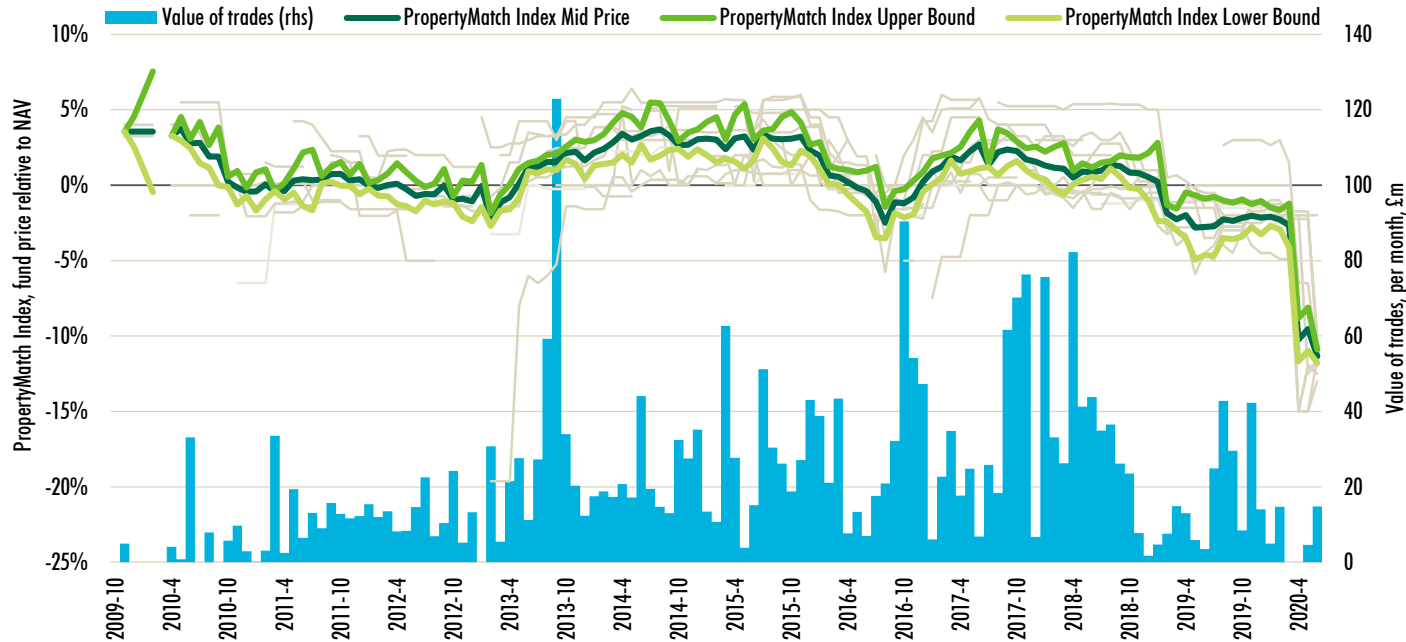
The chart shows that while there are continuous fluctuations in pricing at the fund level, overall the funds broadly move together, particularly in times of significant market movement (e.g. post Brexit Referendum and onset of Covid-19).

The range of pricing was typically NAV-5% across the cohort, although this arguably tightened, and declined a little, in 2018-19.

Source: CBRE Research, PropertyMatch.

PROPERTYMATCH UK BALANCED FUNDS COMPOSITE INDEX

Combining 12 UK Balanced funds into a single Index (weighted by NAV) gives a clearer, broad picture of the path of the market over the last ten years or so. In the immediate aftermath of Covid-19, pricing is as discounted (relative to NAV) as it ever has been.



The weighted composite of 12 UK Balanced funds shows more clearly the evolution of pricing for this fund type.

Having been at or just below NAV for much of 2010-12, 2013-18 saw UK Balanced fund pricing move to a small premium (c1-3%) – excluding 6-9 months either side of the Brexit Referendum.

In early 2019, pricing shifted downwards to a discount of roughly -2.5% to NAV, until the onset of Covid-19 saw a sharp drop to -10.2% in April and -11.4% at the end of June. This apparent further fall is driven by more funds having updated pricing, rather than ever weakening sentiment; transaction prices have in fact been tightening since April.

Source: CBRE Research, PropertyMatch.

PROPERTYMATCH UK BALANCED FUNDS COMPOSITE INDEX, CORRELATIONS

The investment performance of UK Balanced funds is strongly correlated, so it is unsurprising to also see very high correlation of PropertyMatch Index history. Larger size tends to bring with it better trading and pricing data and higher correlation with other funds.

	AEW UK Core Property Fund	BlackRock UK Property Fund	CBRE UK Property PAIF	Fidelity UK Real Estate Fund	Hermes Property Unit Trust	Lothbury Property Trust	Nuveen UK Property Fund	Patrizia Hanover Property Unit Trust	Royal London Property Fund	Schroder UK Real Estate Fund	Threadneedle Property Unit Trust	UBS Triton Property Unit Trust	PropertyMatch Balanced Fund Composite	Total PropertyMatch Index Strength Score	Aver. PropertyMatch Index Strength Score	MSCI / AREF NAV, Jun-2020
AEW UK Core Property Fund	1.000	0.818	0.728	0.152	0.622	0.796	0.792	0.681	0.357	0.849	0.760	0.745	0.849	218	5.6	277
BlackRock UK Property Fund	0.818	1.000	0.677	0.617	0.697	0.887	0.590	0.307	0.504	0.882	0.882	0.604	0.933	1,139	9.1	3,139
CBRE UK Property PAIF	0.728	0.677	1.000	0.763	0.754	0.747	0.752	0.592	0.481	0.807	0.673	0.755	0.778	540	7.6	1,474
Fidelity UK Real Estate Fund	0.152	0.617	0.763	1.000	0.884	0.644	0.646	0.590	0.733	0.477	0.747	0.435	0.704	60	3.3	..
Hermes Property Unit Trust	0.622	0.697	0.754	0.884	1.000	0.726	0.590	0.291	0.647	0.729	0.757	0.694	0.818	757	7.2	1,382
Lothbury Property Trust	0.796	0.887	0.747	0.644	0.726	1.000	0.747	0.321	0.581	0.864	0.904	0.615	0.929	670	7.0	1,593
Nuveen UK Property Fund	0.792	0.590	0.752	0.646	0.590	0.747	1.000	0.519	0.457	0.767	0.677	0.725	0.729	425	5.1	165
Patrizia Hanover Property Unit Trust	0.681	0.307	0.592	0.590	0.291	0.321	0.519	1.000	0.492	0.368	0.380	0.701	0.457	704	6.3	486
Royal London Property Fund	0.357	0.504	0.481	0.733	0.647	0.581	0.457	0.492	1.000	0.572	0.552	0.434	0.583	218	4.2	381
Schroder UK Real Estate Fund	0.849	0.882	0.807	0.477	0.729	0.864	0.767	0.368	0.572	1.000	0.911	0.627	0.953	959	8.4	2,255
Threadneedle Property Unit Trust	0.760	0.882	0.673	0.747	0.757	0.904	0.677	0.380	0.552	0.911	1.000	0.555	0.952	1,011	8.4	1,447
UBS Triton Property Unit Trust	0.745	0.604	0.755	0.435	0.694	0.615	0.725	0.701	0.434	0.627	0.555	1.000	0.692	487	6.3	876
PropertyMatch Balanced Fund Composite	0.849	0.933	0.778	0.704	0.818	0.929	0.729	0.457	0.583	0.953	0.952	0.692	1.000	1,020	8.0	13,475
Total PropertyMatch Index Strength Score	218	1,139	540	60	757	670	425	704	218	959	1,011	487	1,020			
Aver. PropertyMatch Index Strength Score	5.6	9.1	7.6	3.3	7.2	7.0	5.1	6.3	4.2	8.4	8.4	6.3	8.0			
MSCI / AREF NAV, Jun-2020	277	3,139	1,474	..	1,382	1,593	165	486	381	2,255	1,447	876	13,475			

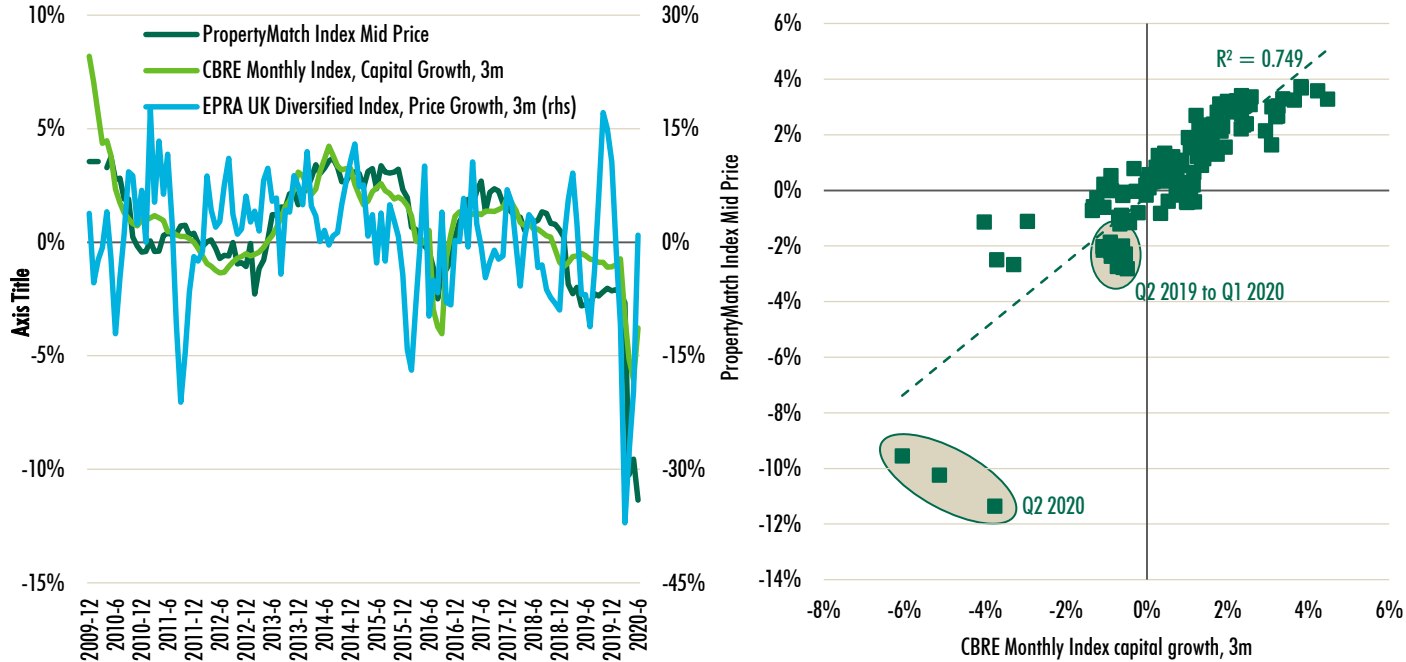
The table shows Dec-09 to Jun-20 correlations between the PropertyMatch Index of 12 UK Balanced Funds and the Composite Index, and data on fund size and Index Strength Score (a higher figure indicating more and more accurate trading and pricing data over time).

The funds are highly correlated with each other and with the overall Index, with size tending to increase correlation as well as data quality. This suggests that investors may be rewarded for having a flexible outlook on the specific funds they invest in; if (particularly large) funds are interchangeable, tactical pricing opportunities on entry and exit may drive out-performance more than fund selection.

Source: CBRE Research, MSCI, PropertyMatch. Note: Correlation coefficients >0.75 are in bold.

PROPERTYMATCH UK BALANCED FUNDS COMPOSITE INDEX VS COMPARABLES

The PropertyMatch UK Balanced Fund Index is strongly correlated with the CBRE Monthly Index. By historic standards, this relationship suggests the recent correction in pricing may be overdone, a view backed up by the recovery in REIT pricing, a leading indicator of both.



Source: CBRE Research, EPRA, PropertyMatch.

The chart to the left plots the PropertyMatch UK Balanced Funds Index, CBRE Monthly Index and the EPRA UK Diversified Index. The first two are very strongly correlated, while the latter is a leading indicator of both; thus, what happens to REITs usually also happens within a couple of months to direct property and secondary fund pricing.

The chart to the right plots observations on the PropertyMatch UK Balanced Funds Index against the CBRE Monthly Index. The strength of the relationship is clear, though it has strained a little of late. Arguably, secondary fund pricing has corrected further than would be expected – a view perhaps backed up by the recent sharp upturn in REIT prices.

PROPERTYMATCH UK BALANCED FUNDS INDEX, PERFORMANCE CORRELATIONS

In general, PropertyMatch Index pricing moves with performance of the underlying fund, suggesting secondary market pricing moves synchronously with fund performance.

	Quarterly total return correlation with PropertyMatch Index				Quarterly total return correlation with quarterly change in PropertyMatch Index			
	PropertyMatch Index 1Q Lead	No lead/lag	PropertyMatch Index 1Q Lag	PropertyMatch Index 2Q Lag	PropertyMatch Index 1Q Lead	No lead/lag	PropertyMatch Index 1Q Lag	PropertyMatch Index 2Q Lag
AEW UK Core Property Fund	0.059	0.675	0.745	0.380	0.207	0.655	0.608	0.260
BlackRock UK Property Fund	0.776	0.729	0.771	0.417	0.329	0.265	0.315	-0.202
CBRE UK Property PAIF	0.662	0.812	0.590	0.397	0.080	0.489	0.357	0.046
Fidelity UK Real Estate Fund	0.651	0.821	0.955	0.528
Hermes Property Unit Trust	0.463	0.692	0.597	0.457	0.288	0.682	0.373	0.139
Lothbury Property Trust	0.488	0.600	0.638	0.288	0.136	0.328	0.355	-0.059
Nuveen UK Property Fund	0.385	0.400	0.600	0.353	-0.139	0.209	0.480	0.181
Patrizia Hanover Property Unit Trust	0.086	0.465	0.721	0.576	0.297	0.410	0.130	-0.256
Royal London Property Fund	0.434	0.486	0.360	0.782	-0.006	0.257	-0.224	0.361
Schroder UK Real Estate Fund	0.784	0.778	0.812	0.611	0.198	0.299	0.288	0.045
Threadneedle Property Unit Trust	0.670	0.804	0.677	0.473	0.171	0.431	0.134	-0.012
UBS Triton Property Unit Trust	0.484	0.680	0.529	0.458	0.078	0.555	0.417	0.442

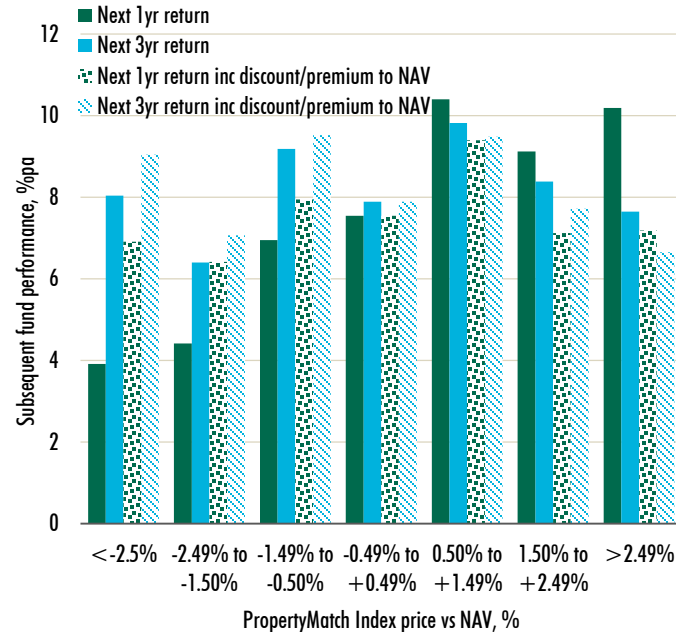
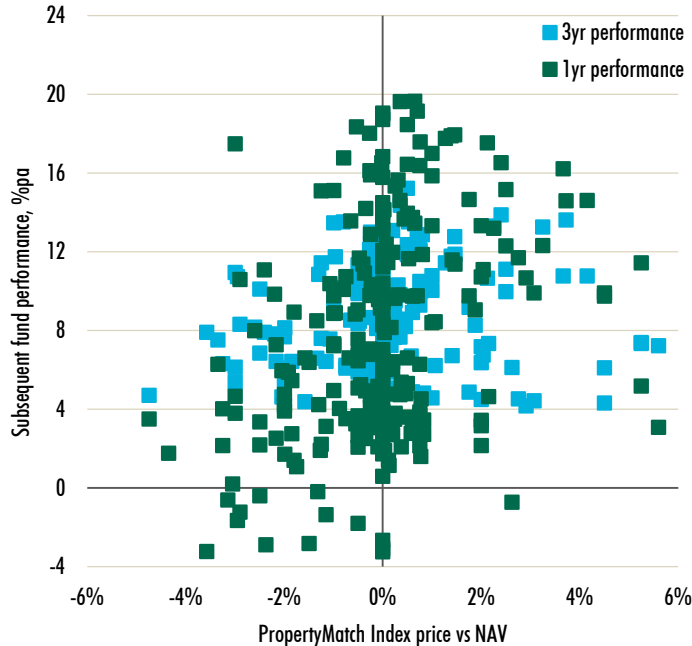
For the 12 UK Balanced Funds the table shows the correlation with fund performance (total return from MSCI / AREF) and each fund's PropertyMatch Index price. Correlations are shown with the Index price as both lead and lag indicator.

In general it can be seen that the strongest relationships are generally observed with no lag or when the PropertyMatch Index price is lagged by a quarter. This suggests that secondary market pricing either moves with or slightly after fund performance; an improvement in pricing for example likely means a recent or current improvement in fund return, not necessarily (sadly) a future one.

Source: CBRE Research, MSCI, PropertyMatch. Note: Strongest correlation coefficients in each section are in bold.

PROPERTYMATCH UK BALANCED FUNDS INDEX, ENTRY PRICE AND PERFORMANCE

There is only a weak relationship between the PropertyMatch Index price and subsequent performance. Indeed, when factoring in the pricing gain, arguably investors receive better performance from buying when funds are priced at a discount to NAV.



The charts show performance over 1yr and 3yr following purchase of UK Balanced Funds at all available end-quarter PropertyMatch Index prices over time. The bar chart additionally factors in the accounting impact of buying at a discount or premium (e.g. a 3% discount is worth 1%pa over three years or 3% over one year).

Without this factored in it is difficult to discern a pattern, however with this accounted for the returns earned after buying at a discount are higher than those earned when buying at a premium (8.5%pa versus 8.0%pa on a three year basis).

This will perhaps encourage investors in the current pricing climate.

Source: CBRE Research, MSCI, PropertyMatch.



DISCLAIMERS AND WAIVERS

IMPORTANT INFORMATION

This material has been prepared by CBRE Indirect Investment Services Limited trading as PropertyMatch, in association with CBRE Research (CBRE) employing appropriate expertise, and in the belief that it is fair and not misleading. Although CBRE believes its views reflect market conditions on the date of this presentation, they are subject to significant uncertainties and contingencies, many of which are beyond CBRE's control.

Nothing in this document constitutes accounting, legal, regulatory, tax or other advice.

CBRE does not accept any responsibility to any person for the consequences of any person placing reliance on the content of this information for any purpose. The information contained in this document, including any data, projections, and underlying assumptions are based upon certain assumptions, management forecasts, and analysis of information available as at the date of this document, and reflects prevailing conditions, and our views as of the date of the document, all of which are accordingly subject to change at any time without notice, and we are not under any obligation to notify you of any of these changes.

Past or projected performance is not necessarily indicative of future results.



CONTACTS

Paul Robinson, Executive Director paul.robinson@cbre.com

Michael Levi, Head of PropertyMatch Desk michael.levi@cbre.com

Dominic Smith, Senior Director UK Research dominic.smith@cbre.com