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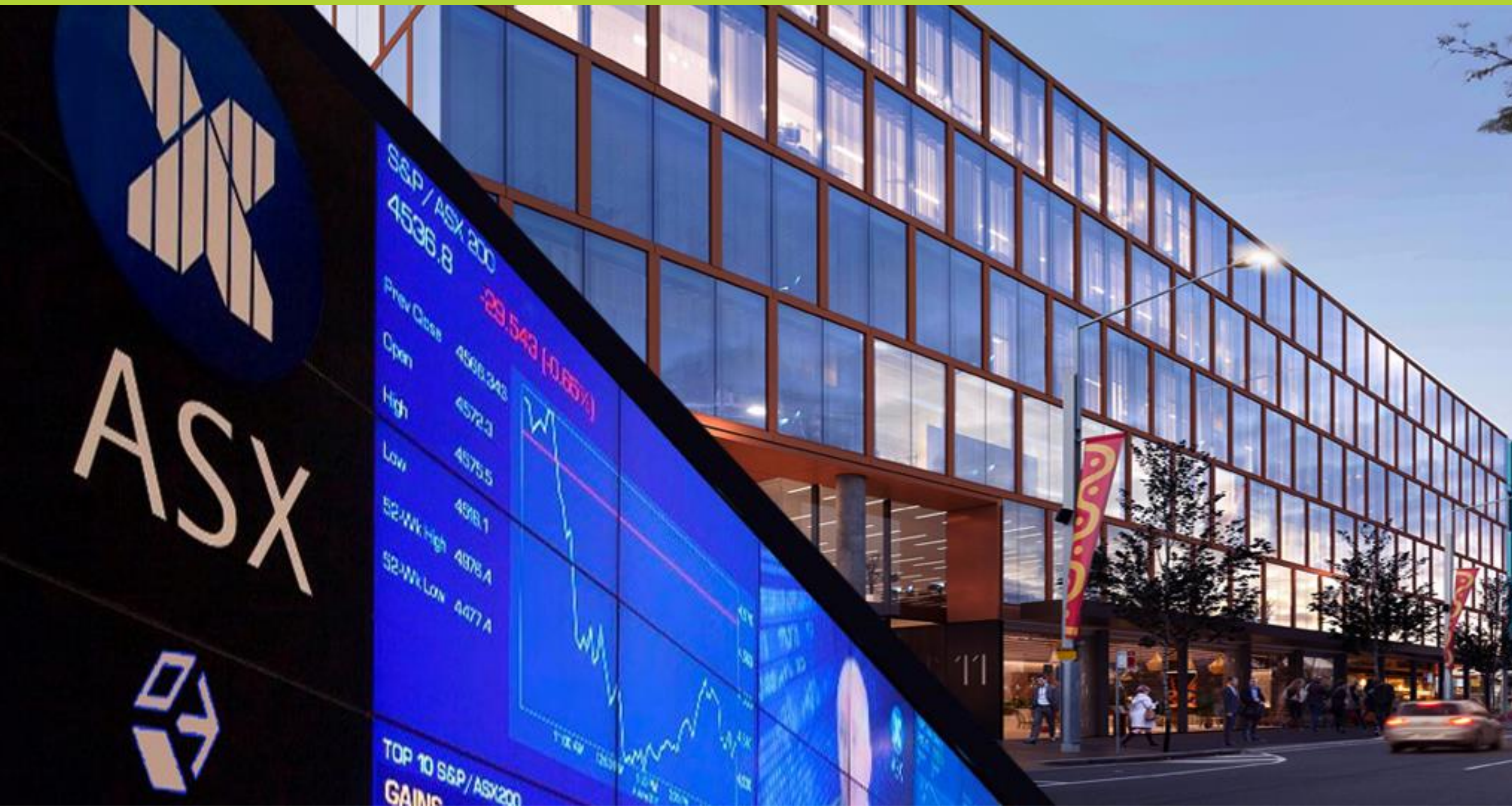
Folkestone
MAXIM A-REIT SECURITIES FUND



FOLKESTONE MAXIM A-REIT SECURITIES FUND

JUNE 2018 REPORT

Folkestone Maxim A-REIT Securities Fund	June 2018 %	6 Months %	1 Year % p.a.	3 Years % p.a.	5 Years % p.a.	10 Years % p.a.	Since Inception % p.a.*
Growth	+2.37	-0.74	+8.65	+7.95	+8.93	+3.19	+1.45
Income Return	+1.10	+1.76	+3.81	+4.54	+5.00	+3.25	+3.66
Total Return (After Fees but Before Tax) **	+3.47	+1.02	+12.46	+12.48	+13.93	+6.43	+5.11
S&P/ASX 300 A-REIT Accumulation Index	+2.27	+3.02	+13.20	+9.99	+12.19	+6.07	+3.86
Value Add	**+1.20**	**-2.00**	**-0.74**	**+2.49**	**+1.74**	**+0.36**	**+1.25**

*Fund inception date October 2005. **Please note the Fund's management fee was reduced on 16 May 2014. The Fund's after fees but before tax performance only reflects the new management fee from this date.

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HIGHLY RECOMMENDED ATCHISON CONSULTANTS

FUND MANAGER OF THE YEAR 2018
MONEY MANAGEMENT | Lonsec
WINNER
Australian Property Securities

MARKET REVIEW

The S&P/ASX 300 A-REIT Accumulation Index finished FY18 on a high, returning 13.2%, in line with the broader equities market, with the last three months delivering a strong return of 9.8%. The strength in the A-REIT sector coincided with rising concerns of an escalation in a trade war between United States and China, political tensions in Europe, a pullback in US bond yields and the flattening of the Australian yield curve. The spread between long term interest rates and short-term interest rates narrowed to just 50 basis points.

The Reserve Bank (RBA) left rates unchanged at 1.5%. This marked 23 months in a row that the RBA have held rates unchanged due to low inflation and weak wages growth. As a result, consensus estimates for the timing of the next interest rate hike have pushed out until late 2019.

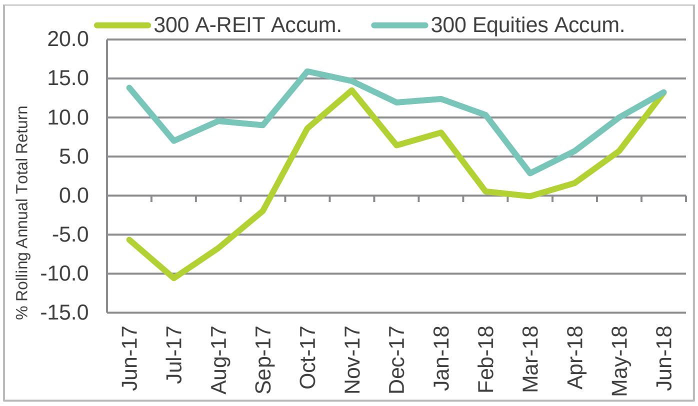
Economic data released in Australia during June was mixed. GDP rose 1.0% over the March quarter, taking the annual rate above trend to +3.1%. Growth was mainly driven by a rebound in net exports and an increase in public investment. However, consumption disappointed at 0.3% q/q, with the ABS noting that spending was concentrated on non-discretionary items such as insurance, food and utilities.

National dwelling prices fell 0.1% in May and 0.4% for the year; the first-time values have fallen across the nation since 2012. Of the major capital cities, Sydney's values fell the most over the year, down 4.2%.

Over the month of June, the S&P/ASX 300 A-REIT Accumulation Index returned +2.27%, underperforming the Australian equities market (S&P/ASX 300), which rose 3.02%. For the June quarter, A-REITs outperformed equities, with the S&P/ASX 300 A-REIT Accumulation Index returning +9.8% compared to +8.4% for equities. Despite significantly underperforming equities between December and February, off the back of concerns about rising global inflation and bond yields, for the 12 months to June 2018, the S&P/ASX 300 A-REIT Accumulation Index performed in line with the equities market at +13.2% (Figure 1).

Figure 1: A-REITs vs. Equity Performance

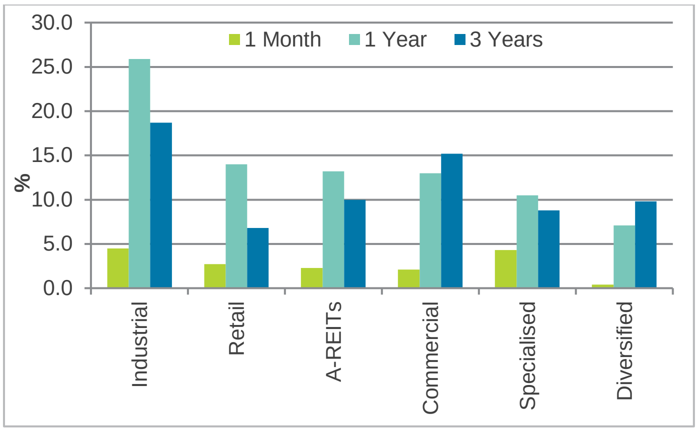
12 months to 30 June 2018



Source: IRESS

Figure 2: A-REIT Sector Performance

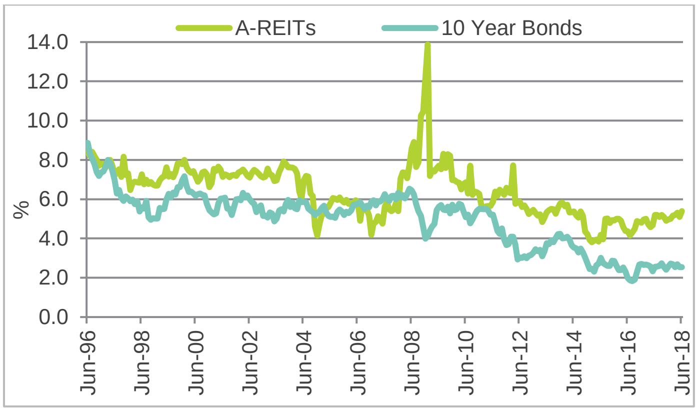
12 months to 30 June 2018



Source: Bloomberg

Figure 3: A-REITs Sector EPS & DPS Yields vs. 10 Year Bond Yields

1996 – 2018



Source: IRESS

For the June quarter, the Industrial A-REIT sub-sector provided the best performance with a return of +15.2%, led by Goodman Group (GMG +15.8%). The next best sub-sector comprised Retail A-REITs which returned +11.0%, followed by Residential A-REITs at +10.8%, Office A-REITs at +9.5%, Diversified A-REITs at +6.5%, Specialised A-REITs at +4.0% and Health Care A-REITs at 1.0%.

The three best performing securities in the S&P/ASX 300 A-REIT Accumulation Index for the June quarter were Investa Office Fund (IOF +23.7%) following a take-over bid by Blackstone, Charter Hall Group (CHC +16.6%) due to a growth in performance fees from its unlisted office funds and Goodman Group (GMG +15.8%) due to an uplift in earnings guidance to 8.0%.

The three worst performing securities were Rural Funds Group (RFF -4.7%) due to market expectations of a capital raising to fund acquisitions to grow its cattle farming portfolio, Folkestone Education Trust (FET -0.8%) and Arena REIT (ARF +1.0%), both due to uncertainty around the impact of changes to childcare rebates being introduced from 1 July 2018.

SECTOR ACTIVITY

In June 2018, a number of A-REITs undertook asset revaluations which revealed a very buoyant office market, particularly in Sydney and Melbourne. Investa Office Fund (IOF) independently revalued its portfolio, resulting in a $316m (+7.9%) valuation gain on book value. The new valuations resulted in a 17 basis point compression in cap rates to 5.48% and an uplift in Net Tangible Assets (NTA) from $4.95 cpu to $5.48 cpu.

Dexus Group (DXS) announced a 3.0% increase on prior book values for the six months to 30 June 2018, taking the annual increase to 9.3%; their Sydney office portfolio was a standout. Australian Unity Office (AOF) also announced a valuation uplift of 9.4% over the preceding book value for the six months to June, following revaluation of six of its assets.

Vicinity Centres (VCX) announced they have assigned JLL to sell 15 sub-regional and neighbourhood assets valued at $1.02 billion with an average cap rate of 6.63%.

Over the quarter, most A-REITs provided FY18 earnings guidance with few surprises. Mirvac Group (MGR) tightened its FY18 earnings guidance to 15.6 cps, at the top of its 15.3-15.6 cps target range as a result of a strong residential division; Ingenia Communities Group (INA) revised its FY18 guidance to 17.2 cps from 15.6 cps on the back of higher forecast home settlements and Aveo Group (AOG) increased its underlying EPS guidance from 20.4 cps to 21.6 cps due to higher than expected development profit at its Newstead, Brisbane retirement community.

Transaction activity at the asset level continued, with Mirvac assigning its pre-emptive rights over Blackstone's 50% interest in 275 Kent Street, Sydney to ISPT for $721.6m, well above Mirvac's stated book value of $550m for their 50% interest. Charter Hall Retail (CQR) acquired Gateway Plaza in partnership with the Charter Hall Prime Retail Fund for $117m, while GPT pulled the sale of Wollongong Central after it failed to attract an acceptable offer.

MERGERS & ACQUISITIONS

M&A activity continued to be a major theme in June, with manufactured homes estate owner and operator Gateway Lifestyle (GTY) receiving a distribution adjusted $2.35 per share all cash offer from Hometown America, above Brookfield's prior offer of $2.30 per share and their initial $2.10 per share offer. Thus far, GTY has not made any recommendation to its shareholders.

In addition, Investa Office Fund (IOF) announced it has entered into a scheme of arrangement with Blackstone (BX), in relation to the private equity group's indicative bid of $5.15 (ex-distribution) from the month prior. The only sticking point is that the offer is now 6.4% below IOF's revised NTA of $5.48 cpu. This increases the risk of an Independent Expert opinion that the BX proposal is not fair and reasonable, allowing the IOF board to withdraw its recommendation without triggering the break fee (A$20m or 3.3cpu).

At the close of trade on 8 June 2018, Westfield (WFD) was removed from the ASX following implementation of the takeover by Unibail-Rodamco.

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DEBT AND CAPTIAL MARKETS

New equity issuance by the A-REIT sector was muted over the year.

Capital management strategies in the form of buybacks were announced by some of the A-REITs trading at or below NTAs, including; Mirvac Group (MGR) buying back up to 2.6% of capital, Dexus Group (DXS) buying up to 5.0% of issued securities, and Scentre Group (SCG) buying up to $700 million of its securities. As at 30 June 2018, Charter Hall Retail (CQR) had purchased 9.0% of their stated buy-back, Dexus Group (DXS) zero, Investa Office Fund (IOF) 51%, Scentre (SCG) 4.0% and Mirvac Group (MGR) just 1.0%.

Debt issuance was strong in the past year, increasing by 78% in FY18 to $8.5 billion. The average spread over BBSW was +175 basis points, up 17 basis points on FY17, while the average tenure was 9.1 years

SECTOR VALUATION

As at the end of June, the A-REIT sector was trading at a FY18 estimated distribution yield of 5.4%, representing a 329 bps premium to the RBA Cash rate and a 276 bps premium to 10 Year Bonds (Figure 3).

The sector's look-through gearing currently stands at an acceptable 27%, whilst it is trading at a premium to NTA of 23.2% compared to the 25 year average of 15.7%.

FUND PERFORMANCE REPORT

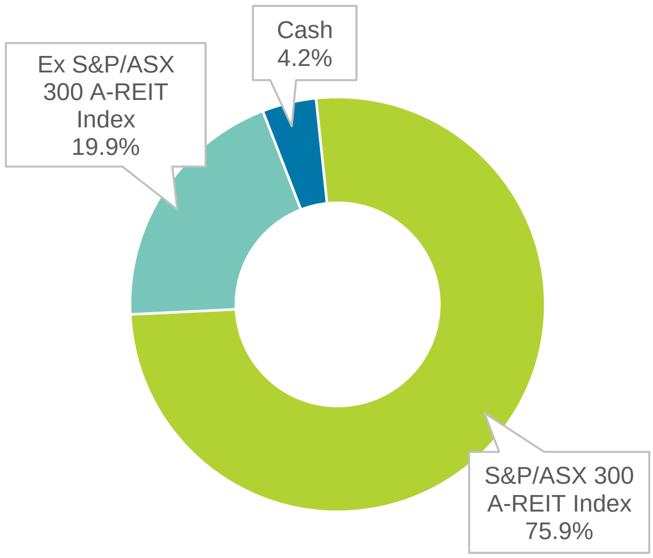
June 2018

For the month of June 2018, the Fund returned +3.47% (on an After Fee but Before Tax basis), outperforming the Fund's Benchmark (S&P/ASX 300 A-REIT Accumulation Index) by +1.20%.

Positive contributions to returns in June 2018 came from the Fund's overweight holdings in Carindale Property Trust (CDP +9.2%), Lifestyle Communities (LIC +10.8%) and Centuria Metropolitan REIT (CMA +6.2%).

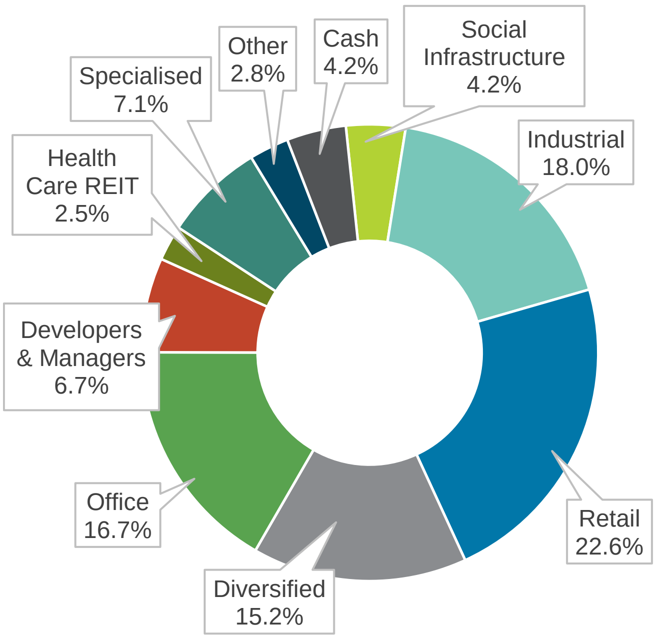
Fund Asset Allocation

As at 30 June 2018



Fund Sector Split

As at 30 June 2018



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Detracting from returns, included zero holdings in Investa Office Fund (IOF 5.6%) and GPT Group (GPT 3.1%) and an underweight exposure to Scentre Group (SCG 5.0%).

June Quarter 2018

Over the June 2018 Quarter, the Fund returned +7.26% (on an After Fee but Before Tax basis), compared to the S&P/ASX 300 Accumulation Index of +9.82%.

Positive contributions to returns in the June Quarter came from the Fund's exposure to Lifestyle Communities (LIC +16.1%), Carindale Property Trust (CDP +10.6%) and Centuria Metropolitan REIT (CMA +10.8%).

Detracting from returns can be attributed to zero exposures to Investa Office Fund (IOF +23.7%) and Vicinity Centres (VCX +10.9%) and an underweight exposure to Scentre Group (SCG +14.6%).

Year to June 2018

For the 12 months to June 2018, the Fund returned +12.46% (after Fees but Before Tax), underperforming its benchmark by 0.74%.

The table below highlights the Fund's key active positions, which have contributed most to its outperformance over the year to June 2018.

Rural Funds Group	
Lifestyle Communities (LIC)	Overweight
Rural Funds (RFF)	Overweight
Industria REIT (IDR)	Overweight

At the end of June 2018, the Fund's investments comprised 19 ASX listed securities totaling 95.8% of the portfolio, 12 of these securities were constituents of the S&P/ASX 300 A-REIT Index, whilst the remaining 7 securities were Ex-Index securities. The remaining 4.2% was held in cash/liquid investments.

A June 2018 Quarter distribution of 0.9755 cents per Unit (paid to investors early in July 2018), took total distributions for the year ended 30 June 2018 to 3.1697 cents per Unit.

We expect corporate activity to remain elevated in the year ahead, reflecting renewed focus on alternative growth levers and heightened international interest in A-REITs

OUTLOOK

FY18 was a strong year for the Australian direct property market in terms of both valuations and transactions. A-REITs took advantage of the capital chasing assets and continued to be overall net sellers in office and retail assets, seizing the opportunity to reposition their portfolios and deleverage their balance sheet.

Office fundamentals continue to strengthen in Sydney and Melbourne, with limited supply and stock withdrawals (particularly in Sydney) pushing vacancies to below 5.0% and rents higher, in both markets.

JLL data to March reveals that prime office capital values increased by 15.0% in Sydney and 17.0% in Melbourne over the past year. Prime office capitalisation rates compressed by approximately 31 basis points with rents increasing 16.0% over the same period. Brisbane and Perth however, continue to experience weakness due to oversupply and the on-going effects of the mining downturn.

The retail operating environment remains difficult with weak earnings sentiment, due to increased competition from online retailing and foreign retailers. As a result, the number of retailers going into administration is on the rise. The leasing environment will continue to be challenging with many retailers rationalising their store footprint, seeking shorter term leases and larger fitout incentives from landlords.

The industrial sector remains strong, with on-going demand for quality distribution centres in metropolitan locations that could potentially service the growing online sector.

Sentiment towards the residential sector continues to deteriorate as lending curbs impact on investor and offshore buyer activity, making pre-sale hurdles challenging for new apartment projects. This should see the apartment supply reduce from record highs over the next few years. We remain positive about the medium prospects for the residential sector, given strong population and employment growth, and the slowdown in supply.

We expect corporate activity to remain elevated in the year ahead, reflecting the inability for many of the A-REITs to acquire assets on market at reasonable prices, the lower Australian dollar making the valuations of A-REITs increasingly attractive to foreign acquirers (note the Unibail-Rodamco acquisition of Westfield Group (WFD), Blackstone's bid for Investa Office Fund (IOF) and Blackstone and Hometown's fight for Gateway Lifestyle (GTY)) and renewed focus on alternate growth levers such as synergies. A-REITs that are trading at the smallest premiums or discounts to NTA will be most prone to this activity.

The earnings outlook remains robust, driven by the strong office and industrial sectors, and the development books of many of the A-REITs. Gearing levels remain acceptable, with few A-REITs looking to gear-up, despite the low cost of debt. A-REIT balance sheets continue to benefit from cap rate compression (pushing asset values higher) as well as from asset sales and more conservative payout ratios.

Overall, we expect the A-REIT sector to deliver relatively attractive returns given the continued low domestic interest rate environment. The two wildcards being the impact of M&A activity and A-REITs, like other defensive sectors, being susceptible in the short-term to a major sell-off in the bond markets (i.e. bond yields move higher).

In such an environment, as a high conviction, active manager, we continue to favour those A-REITs with exposure to the social infrastructure and specialised property sub-sectors, selected real estate developers and managers that have growing funds management platforms, and those securities with quality management and relatively attractive yields that have the ability to actively manage their portfolios to drive income growth in the years ahead.

TOP 5 ACTIVE OVERWEIGHTS

By Portfolio Weight

Industria REIT
Centuria Metropolitan REIT
Rural Funds Group
Carindale Property Trust
Folkestone Education Trust

FUND OVERVIEW

As at 30 June 2018

Status	Open
Fund Maturity	Open Ended
Investment	Primarily A-REITs
Investment Horizon	3-5 Years
Distribution Frequency	Quarterly
Fund Inception Date	October 2005
Pricing	Daily
Buy/Sell Spread	0.25%/0.25%
Total MER	0.95% up to $50m Then 0.85% >$50m
ARSN	116 193 563
APIR Code	COL0001AU

PLATFORMS

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QUANTITATIVE RATING

MORNINGSTAR ★★★★

Overall rating out of 127 Equity Australia Real Estate funds as of 31 May 2018.

FE CROWN FUND RATING

Folkestone Maxim Wins Industry Leadership Award

In December 2017, Folkestone Maxim won the inaugural Financial Standard Investment Leadership Award for Australian Listed Property.

The Financial Standard award recognises *"investment strategies that showcase all the qualities investors - whether they be advised or self directed - are looking for in a manager".*

CONTACT US

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