RESOLUTION CAPITAL

QUARTERLY INVESTMENT REPORT

RESOLUTION CAPITAL GLOBAL PROPERTY SECURITIES FUND (UNHEDGED) – SERIES II

SEPTEMBER 2018

Global Real Estate Securities

Fund Investment Performance

The Resolution Capital Global Property Securities Fund (Unhedged) – Series II (the 'Fund') outperformed the FTSE EPRA/NAREIT Developed Index (AUD) Net TRI by 16 basis points for the quarter ending 30 September 2018.

Period Ending 30 September 2018*

	Quarter %	1 Year %	3 Years % p.a.	5 Years % p.a.	Since Inception[#] % p.a.
Fund(after fees)^	1.97	13.11	6.00	11.97	14.70
Benchmark+	1.81	12.41	5.13	10.97	14.15
Difference	*0.16*	*0.70*	*0.87*	*1.00*	*0.55*

* Net returns are expressed after deducting investment management costs. Past performance is not a reliable indicator of future performance.
[#] 30 November 2011.
^ Please note this Fund was previously known as the Perennial Unhedged Global Property Trust. Resolution Capital was appointed manager of the Fund effective 1 November 2014.
+ Benchmark is FTSE EPRA/NAREIT Developed Index (AUD) Net TRI.

Resolution Capital Global Property Securities Fund (Unhedged) – Series II Unit Price

	Net Entry	Net Exit
30 September 2018	$1.3218	$1.3139
30 June 2018^	$1.2962	$ 1.2885

^ Ex distribution of 3.4386 cents per unit as at 30 June 2018.

Market Performance

Market Overview	30-Sep-18	30-Jun-18	Quarterly Total Returns
FTSE EPRA/NAREIT Developed Index (unhedged in AUD Net TR)	4,118	4,045	1.8%
FTSE EPRA/NAREIT Developed Index (hedged in AUD Net TR)	2,600	2,592	0.3%
S&P/ASX 300 (GICS) Property (Accum)	49,352	48,392	2.0%
S&P/ASX 300 Index (Accum)	63,210	62,275	1.5%
US 10 Year Bonds	3.05%	2.85%	
AU 10 Year Bonds	2.67%	2.64%	
A$/US$	0.72	0.74	-2.1%

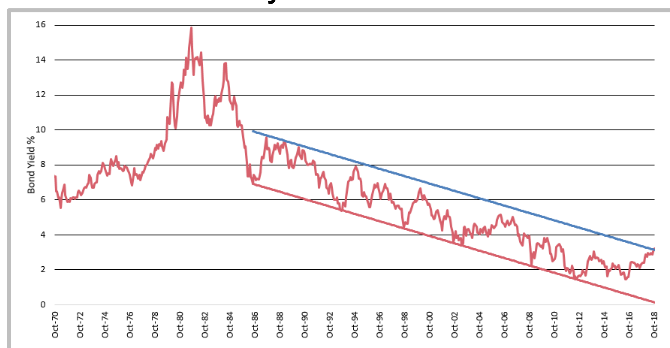
Source: Factset

Commentary

In local currency terms the global listed real estate sector experienced positive but more moderate returns after a strong uplift in the previous quarter. The FTSE EPRA/NAREIT Developed Index produced a total return of 1.8% in A$ Unhedged terms in the quarter, and the portfolio outperformed the benchmark.

Strength in the U.S. economy relative to other developed markets, coupled with mounting trade tensions between the world's two largest economies, the United States and China, were important undercurrents in the most recent quarter. Interest rates in the U.S. were on an upward trajectory, boosted by strong economic conditions, with the 10-year U.S. treasury yield finishing at 3.05%, threatening to break through a 30 year trading band of declining bond yields.

U.S. 10 Year Treasury Yield



Source: Bloomberg

During the quarter, the price of brent crude rose 4%, adding to cost pressures elsewhere including wages.

As the quarter ended, stronger economic news in the U.S. and the prospect for higher interest rates dominated headlines. The U.S. Federal Reserve raised rates 0.25% on concerns about above trend economic growth and the Bank of Japan increased its 10 year JGB yield tolerance 20bps.

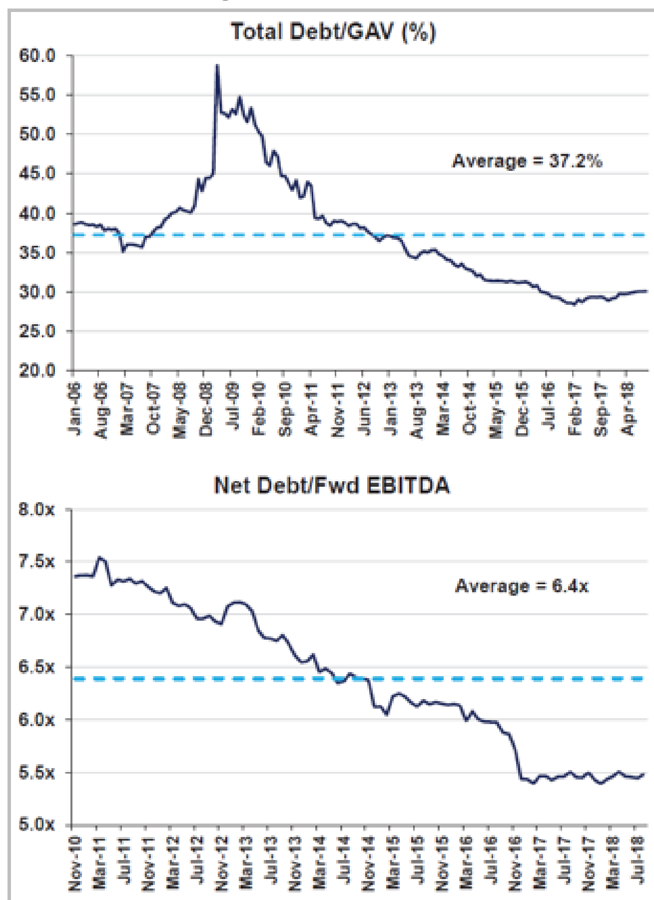
Ten years since the GFC – REIT Capital Structures improved

September marked the tenth anniversary of the Lehman Brothers bankruptcy, a memorable date in the Global Financial Crisis (GFC) that plunged global markets and economies into a sharp and severe recession in late 2008-2009.

REITs, which were punished during the crisis, have travelled quite a distance in the past decade. In the 10 year period, 30 September 2008-2018, Global REITs have produced compound annual returns of 8.4% p.a. (A$ Hedged), far out pacing inflation and global bonds (6.7% p.a.).

In the past decade, REITs have taken advantage of Q.E. and an accommodating interest rate environment to improve their credit profile by reworking their debt books. In most REIT markets, leverage levels are lower, as measured on a Net Debt/EBITDA basis, as well as on a loan-to-market value basis as illustrated in the graphs below which describe the U.S. REIT case.

U.S. REIT Leverage



Source: Citi Research, Citi coverage universe

Debt maturities have been lengthened, reducing refinancing risks in shorter timeframes. Taking advantage of lower and flatter curves, REITs have used more fixed rate debt than before. By embracing unsecured borrowings and reducing secured debt, REITs have gained greater flexibility over their portfolio composition. Many have divested lower quality assets and exited non-core markets and activities.

REIT credit profiles have been upgraded, which also contributed to lower spreads and improved borrowing costs. Additionally, dividend payout ratios have reduced to more sustainable levels after considering recurring capex needs, and the contribution from more volatile development profits has reduced.

As a result, listed real estate today has lower leverage of a longer duration with fixed rate costs and corporate, not asset level, guarantees. For REIT shareholders, the historic risks associated with financial leverage are greatly improved from a decade ago.

September 2008 also marks the tenth anniversary of the launch of Resolution Capital's first pooled Funds, providing a wide range of investors with the opportunity to gain exposure to our flagship global listed real estate investment strategy as well as our domestic focused A-REIT strategy. In light of the high-water starting point for the Fund and subsequent turbulent investment market conditions, we are particularly pleased with the exceptionally strong absolute and relative returns we have been able to deliver for clients. Low financial leverage in the overall portfolio has been one of the hallmarks of our investment strategy and we continue to screen vigorously for excessive leverage and poor capital management structures, which can have a significant negative impact on investment returns.

Earnings – better for now

U.S. REIT second quarter earnings season shone a bit brighter than expected, particularly in retail and apartments. Retail property fundamentals continued to bounce gingerly along the bottom, benefitting from stronger retail sales that were bolstered by jobs growth and contributing some improvement in leasing demand. Shopping centre REITs reported better than expected occupancy; although, this is partially attributable to delayed Toys-R-Us store closures. Shopping centre leasing fundamentals feel fragile. On the mall front, Unibail-Rodamco-Westfield (URW and henceforth, Unibail) surprised the market with a disappointing 3.0% decline in same store Net Operating Income (NOI) in the U.S. operations of its recently acquired Westfield portfolio. Some of the decline likely resulted from distractions caused by the Unibail takeover of Westfield that closed earlier this year, and presumably will bounce back in the future. However, when speaking with the company after its results, it is apparent that the non-flagship properties acquired are truly struggling in their respective markets. URW underperformed over the quarter with a total return of -8.1% in local currency terms. Concerns also remain around the increased leverage levels taken on by the company in the Westfield acquisition despite making some good early progress on its planned asset sales.

Residential was the top performing sector in the quarter with a 5.9% total return, in local currency terms, powered by strength in the U.S. Rent growth in U.S. apartment REITs have been stronger than expected, with solid demand from job growth and income growth. Construction activity remains elevated, but supply growth is set to moderate over the next 12-18 months.

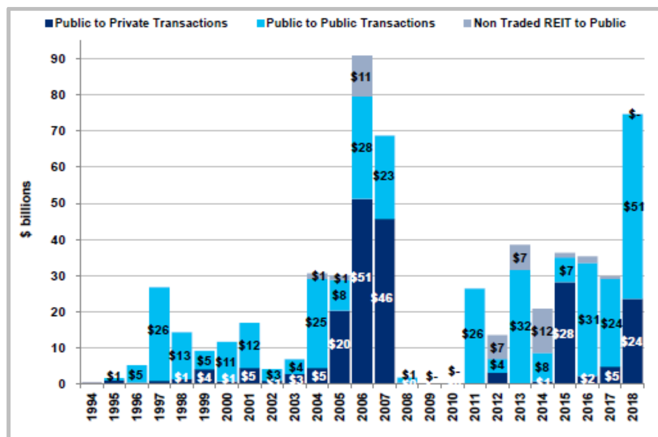
Self storage – no wealth stored here this quarter

Self storage was the worst performing sector in the quarter, declining 8.0% in local currency terms. The portfolio has no exposure to self storage due to concerns about its moderating growth profile from heightened supply and from its premium valuation relative to net asset value (NAV). Continued new construction deliveries are having an adverse impact on market rents, although storage landlords report they are still able to obtain positive rent increases on renewal tenants - for now perhaps. For most of the quarter, storage REIT valuations were not conducive for investment in our view. The shares traded at premiums to underlying asset value at a time when the operating fundamentals were increasingly pressured.

Discounted listed real estate driving M&A

We are not surprised to see more M&A occur at this point in the cycle. In fact, U.S. REIT M&A volumes have reached their highest level since before the GFC in 2018. This resulted from a range of public-to-public and public-to-private deals closing this year.

U.S. REIT M&A Volumes



Source: Citi Research

Anecdotal reports suggest there is considerable capital being assembled in private vehicles to invest in real estate. Listed REITs could present an opportunity for private equity, which appear to have plenty of *dry powder*, to deploy capital fairly quickly and at discounts to direct market transactions. Indeed, at its recent investor day, Blackstone (BX), one of the world's largest private equity investors, identified core real estate as a strategic growth area for the firm. Indeed, if real estate were to be inefficiently priced in the public markets, for instance, signaled when REITs trade at significant discounts to underlying asset value, those portfolios may be recapitalised elsewhere, and private equity may be standing at the ready.

As we discuss below, it is noteworthy that there were two heated bidding wars for listed REITs in the last quarter. In both instances, Blackstone, a private equity behemoth which has had its fingerprints all over the real estate market since taking Equity Office and Hilton Hotels private in mega deals at the peak of the market in 2007, has seemingly been outbid by other investors, including public and private companies.

LaSalle Hotel saga coming to an end

Pebblebrook (PEB) appears to be victorious in its dogged pursuit of LaSalle Hotels (LHO). Earlier in the year, Pebblebrook had made an unsolicited offer to acquire LaSalle, who rebuffed it and went in search of a white knight, finding one in Blackstone. There is history between the management teams of Pebblebrook and LaSalle. Jon Bortz, Pebblebrook's CEO, had previously been the CEO of LaSalle before being nudged aside by LaSalle's current CEO, Mike Barnello. No love lost here.

LaSalle has done the right thing in this takeover battle. It has caused the buyer to increase price significantly and to use more cash and less stock as consideration. Pebblebrook may be victorious, but Blackstone doesn't leave the field empty handed. It will pocket a US$112 million break fee, equal to 2.5% of the combined company's NAV.

Investa Office Fund – the object of multiple affections

In Australia, the A$4.3 billion battle for Investa Office Fund (IOF) shifted into high gear during the quarter. Blackstone, which had previously reached an agreement to acquire IOF but one that was still subject to a shareholder vote, faces serious competition from Oxford Properties, the real estate arm of the Canadian Pension Plan - Ontario Municipal Employees Retirement System. Blackstone was forced to raise its bid for IOF a few times, and even so, the shareholder vote, scheduled for September 6th, was postponed at a late stage. Oxford has now been granted access to IOF's books to allow for proper due diligence. The fact

that two sophisticated, globally active real estate investors are battling over IOF speaks to the scarcity of assets in this attractive market. Recall, our portfolio had a position in IOF that was eventually liquidated following the bid earlier this year.

Prologis/DCT and Brookfield/GGP complete

During the quarter, two large M&A transactions completed. In mid-August, Prologis (PLD) completed the US$8.4 billion acquisition of DCT Industrial Trust (DCT). In this all-stock transaction, Prologis had underperformed the U.S. industrial REIT sector by 6.0% from the deal announcement through its close and has since begun to regain ground. We expect Prologis shares to benefit from the deal's closing, its increased operational scale and better-than-expected deal synergies. The portfolio increased its weighting in Prologis on deal-related weakness. Stay tuned.

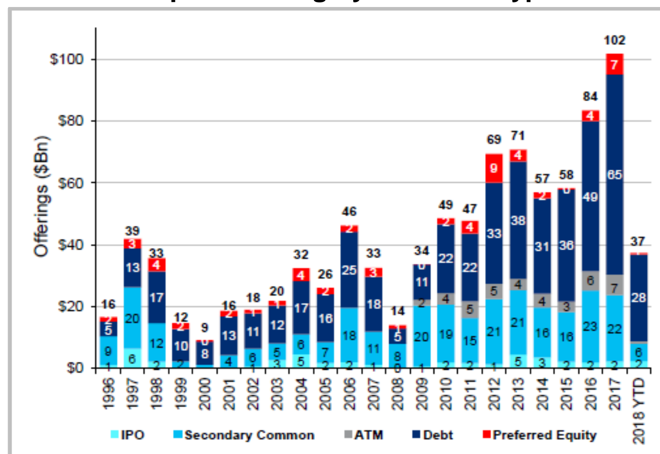
Brookfield Property Partners (BPY) also closed the US$30 billion acquisition of mall company, GGP, acquiring the remaining 70% of the company it did not already own. As part of this transaction, a new public security, Brookfield Property REIT (BPR) was created to provide U.S. REIT equivalent exposure to the Canadian parent, Brookfield Property Partners (BPY). BPY's Bermuda domicile had proven to be a stumbling block for some of GGP's U.S. REIT investors, and hence a more U.S. domiciled security was created to facilitate support for the transaction.

Equity spigot opens

While YTD equity raising has been relatively subdued, the recent quarter saw several equity capital raises across markets as companies locked in financing sources for current and prospective investment spend.

As the chart below illustrates, U.S. REITs are on track to raise significantly less debt and equity capital in 2018 than in previous years.

U.S. REIT Capital Raising by Year and Type



Source Citi Research and SNL 28 Sept 2018

In August, Kilroy Realty (KRC) raised US$415 million via a forward equity sale. Kilroy has one year to call the equity, locked in at the share price fixed in August. This structure gives the company surety about its funding costs while enabling it to avoid any earnings dilution from holding excess cash on its balance sheet awaiting deployment. Kilroy intends to use the proceeds to fund its West Coast office development program.

In September, Digital Realty (DLR), raised US$1 billion via a forward sale with the proceeds earmarked to finance its first acquisition in South America. DLR is partnering with Brookfield Asset Management, one of the largest global real estate and infrastructure investors, to jointly acquire Ascenty, a Brazilian data center portfolio for US$1.8 billion. At the same time but separately, Digital Realty is acquiring 425 acres of land in Northern Virginia in an important data center market and growth corridor near Dulles Airport.

Another data center company, CyrusOne (CONE), also did a US$500 million equity raise. Although there was no immediate use of proceeds identified, the company did receive an upgrade to investment grade by S&P.

In Canada, Allied Properties (AP) raised C$155 million in a September equity offering, which follows a C$299 million equity capital raise in June. Allied owns a portfolio of 11 million square feet of offices in major Canadian markets, principally Toronto and Montreal. The Allied portfolio is characterised by repositioning and expanding older, infill locations, often with a mixed-use component. We believe Allied is building office environments that have broad appeal as live-work-play spaces. The capital raises will be used to fund its well leased development program over the next few years.

In recent years, REITs have been able to raise equity on demand via their ATM (At-The-Market) programs, and we have detailed various issuances in past commentaries. In the most recent quarter, Terreno Realty (TRNO), which owns a concentrated portfolio of industrial warehouses in coastal U.S. markets, raised US$106 million via its ATM. The company's shares trade at a slight premium to NAV, and with this equity raise, the company raises capital to fund its investment activities in a non-dilutive manner. We expect to learn of other REITs having pursued a similar strategy once the third quarter disclosures are filed.

Residential rent control - clouds forming in California

Possible regulatory changes in California have cast a shadow of uncertainty over residential and commercial landlords. On the November ballot in California is Proposition 10, which calls for a repeal of the 1995 Costa-Hawkins Rental Housing Act (Costa-Hawkins). Costa-Hawkins prevents local municipalities from enacting rent control measures over housing built after February 1995. Housing built prior is not subject to the Costa-Hawkins limitations, although it is governed by local laws, and there are 15 municipalities in California with rent control legislation on their books. Costa Hawkins also mandates *vacancy decontrol*, by which a landlord can move rents on a rent-controlled unit to market rates upon vacancy.

A cloud of uncertainty has hung over residential landlords in California, including REITs with significant exposure to the state. We do not believe the passage of Prop 10 spells the death knell for California rental housing ownership. First, the repeal of Costa Hawkins and the removal of its prohibition against rent control does not mean that new rent control immediately becomes a statewide phenomenon. New legislation is neither immediate nor a certitude. Rent control can only be mandated at the local government level, and it will take time for cities to consider and decide if and when to proceed. Many cities in areas where rent control is permitted choose not to enact this legislation because it can be viewed as discouraging residential investment overall. In fact, one municipality in California, Thousand Oaks, is phasing out its rent control laws.

The possibility of *vacancy decontrol* being eliminated is potentially more troublesome for residential landlords because it more significantly impacts the long-term revenue potential of rental housing by creating a very tenant friendly framework. The City of Berkeley has a ballot measure that, if passed could become effective if Costa-Hawkins were repealed, which would eliminate vacancy decontrol. We expect that active landlords would seek to avoid these jurisdictions, and those REITs would sell their holdings in these markets over time.

Commercial real estate taxes could also climb in California

In the "When it rains, it pours" department, commercial landlords in California are also facing a possible change to real estate tax calculations, although this one is further in the future. There is a rumored ballot initiative – allegedly for 2020 – that would reform Proposition 13 in California by creating a "split tax roll" and require commercial properties to be taxed based on annual assessments. Backing up, under the current Prop 13 legislation, in effect since 1978, real estate taxes on both commercial and residential properties in California are set at 1% of the value of the property, as determined by that property's last sale price. Property taxes are indexed to inflation, subject to a 2% max annual cap. Under Prop 13, property taxes are only reassessed upon a sale of a property and given strong asset value appreciation over the past 30+ years, many properties enjoy a tax bill that is far lower than current value assessment.

The move to reform California's property tax methodology targets commercial not residential properties, which are home to many voters. It is not clear if this proposal will ever make it onto a statewide ballot, when this might happen or if it would be successful. Nonetheless, the possibility of a statewide increase in commercial property taxes is becoming a louder concern for real estate investors. Some REIT management teams have been dismissive by saying it would be hard to implement, while others are beginning to quantify the possible impact in 3-4 years.

UK – Brexit saga continues

Uncertainty over the timing and scope of Brexit continues to create a high level of uncertainty for the investment and business community in the UK. It is most certainly not business as usual as UK based companies are shifting more operations offshore. The moves abroad are anecdotal and granular. Headline

moves can be met with resistance, such as Unilever's announced HQ move from London to the Netherlands, which following much UK public and investor discussion, was retracted. However, at the next level down, we are hearing many anecdotes of lower profile roles shifting abroad. Examples include investment bankers responsible for the Spanish market relocating from London to Madrid and Japanese banks adding mainstream offices in Frankfurt and Paris, leading to an eventual rebalancing of staffing away from London. The uncertainties surrounding Brexit are creating wobbles outside of London as well. The lack of clarity on trade flows in a post Brexit world is creating real uncertainties for UK based car manufacturing, and this delays additional investment and cap ex spend up and down the manufacturing supply chain. In the UK, the air is slowly coming out of the balloon.

The retail environment in the UK seems to be worsening. Consumer confidence and retail spend is under pressure. Retailers continue to rationalise their store networks through the use of CVAs (Corporate Voluntary Agreements, which we wrote about in previous commentaries), creating greater uncertainty for UK landlords.

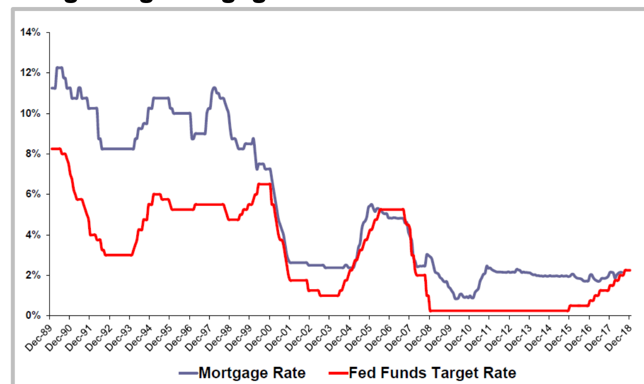
Capital is fleeing the UK listed retail real estate sector. Shares of Intu (INTU), orphaned after Hammerson's (HMSO) aborted attempt to acquire the company, plummeted -14.5% in the quarter to £1.54/share. Intu's stock has been a shockingly bad performer, down 31% over the past year and down 8% annually in the past 5 years in local currency terms. As the quarter ended, local UK press reports that Peel, Intu's largest shareholder, and Brookfield Property were preparing to mount a bid to take Intu private. If this were to occur, it would be interesting to see how Intu's directors respond to a bid that could fall far short of the £6.25/share internal valuation it had once used as a defence for rejecting Simon Property Group's (SPG) £4.25/share bid nearly a decade ago.

In July, Hammerson, having previously rejected Klepierre's (LI) unwanted advances, announced a strategy update that was more of a whimper than a new way forward. The company announced its intention to sell £1.1 billion of assets, exit retail parks, put its long-needed Brent Cross redevelopment on ice and to conduce a £300 million share buyback. Senior management to remain in place, other than the CIO, a sacrificial lamb. Since then, Hammerson, has sold £530 million of retail assets at 5-10% discounts to previous valuations. It also has embarked on a share buyback, however, at prices above where the stock currently trades and with leverage uncomfortably high for this stage of the cycle. Humm… Retail assets values in the UK are under pressure, and while Klepierre could return with another bid, surely the next one would be lower than what Hammerson rejected so quickly earlier this year.

Hong Kong – macro concerns dominate strong property level performance

Rising interest rates, a stronger USD and trade tensions weighed on Hong Kong stocks over the quarter. Notably, after absorbing successive official rate increases, major Hong Kong lenders raised their prime rate for the first time in twelve years, effectively increasing mortgage rates by 12.5 bps to 5.125%.

Hong Kong Mortgage Rate & U.S. Fed Funds Rate



Source: CEIC, Citi Research

Despite macro headwinds, Hong Kong property companies continued to report solid residential development results and positive office and retail rent growth during the period. Sun Hung Kai (16 HK) reported a 16.9% increase in underlying EPS and increased its dividend per share by 13.4% for the year ended June 2018. The company achieved 18% higher residential sales revenues at a higher margin (39% vs 32.8% in the previous corresponding period) and has already achieved 60% of its targeted FY19 contracted sales in the first quarter. Even with strong operating performance, Sun Hung Kai delivered a total return of -3.7% in local currency terms.

Singapore surprise tightening

Property companies with exposure to Singapore residential development were sold heavily when the

government tightened housing policy settings in response to rising home prices. The tightening appeared to catch investors by surprise, coming only 18 months after the city-state first began easing its policy stance. City Developments (CIT) share price fell 15% on the first trading day after the announcement and continued to trade down for the balance of the quarter.

Meanwhile, the offshore expansion of Singapore property companies continued. CapitaLand (CAPL), no stranger to overseas investing, acquired a 3,800 unit multifamily portfolio in the United States for US$838 million. The assets are located in four western U.S. markets, including Denver, Seattle, Portland and Los Angeles. They are generally characterised as B/C quality and were sold by a private equity firm that had only acquired the bulk of them from a REIT in 2015-2016. We suspect these older, suburban assets may contain more operational challenges over time than the buyer may currently appreciate.

As the quarter ended, Mapletree Investments acquired 16.5 million square feet of industrial properties in Europe and the U.S. from a joint venture between Prologis (PLD) and Norges. The US$1.1 billion portfolio contained 9.9 million square feet in Poland, France and Hungary and 6.6 million square feet in Seattle, Dallas and Chicago. With this transaction, Mapletree continues to build up its industrial asset base while Prologis and Norges were able to exit slower growth submarkets.

Real estate remains well bid but transaction volumes slowing

Direct market transactions continue, but the pace of activity has slowed and become more laser focused on quality properties in core markets. CBRE reports transactions volumes are flat in the U.S. and Europe and down in AsiaPac. In the UK, gross transactions volumes are flat, but the number of transactions is down, suggesting that fewer, larger deals are supporting the current market. Clearly, as declining values in UK retail demonstrates, challenging assets in out-of-favor markets are not highly sought after anymore.

Modern, well leased office assets in central London continue to see strong investor demand, particularly from Asian based investors. In August, the National Pension Service of Korea bought the new Goldman Sachs headquarters for £1.16 billion, equating to a 4.1% initial yield. It is a forward sale as Goldman Sachs will lease the building for 25 years once it is completed in 2019.

In July, Unibail announced the pending sale of its Capital 8 building in Paris for €789 million. Unibail recently renovated and fully leased the asset before its sale to a multinational investment advisor.

Back in London, Facebook announced plans to build a new London headquarters at Kings Cross, more than doubling its footprint in the capital. It agreed to acquire 611,000 square feet across three buildings to be delivered in 2021. Big tech's continued expansion in London, as in New York and San Francisco, further validates the workforce attraction of major global cities. While London office has seen effective rent declines this year, the market has maintained its attraction for large technology and creative-type employers who need to make a 15+ year commitment.

Conclusion – stable value is a sea of volatility

Entering the final quarter of 2018, listed real estate faces a varied growth terrain ahead. In the U.S., strong economic growth is supporting tenant demand and keeping commercial building occupancy at elevated levels. Supply is responding, and while in some sectors and markets it has become quite impactful on rent levels, in overall terms the market appears to be in equilibrium.

However, REIT share prices are being whipped around by fears of higher interest rates. We continue to believe that higher rates that result from stronger growth will benefit REIT operations over time. REITs are well capitalised today compared with the financial crisis a decade ago, and dividends are well covered.

Outside the U.S., the growth profile is less obvious. The UK remains mired in a to-the-death battle with itself over the nature and timing of Brexit. There may still be time to work a deal with the Europeans, but the uncertainty is dampening investment in the UK. We retain an exposure in the UK as value reemerges. In Asia, China is pressured as its economy slows, its currency weakens and as trade war fears with the United States build. Interestingly, while a stronger U.S. dollar is adversely impacting Hong Kong property shares (note, share values not cash flow per share), it

helps to support Japanese developers. Strange times indeed because the fundamentals in both markets remain good.

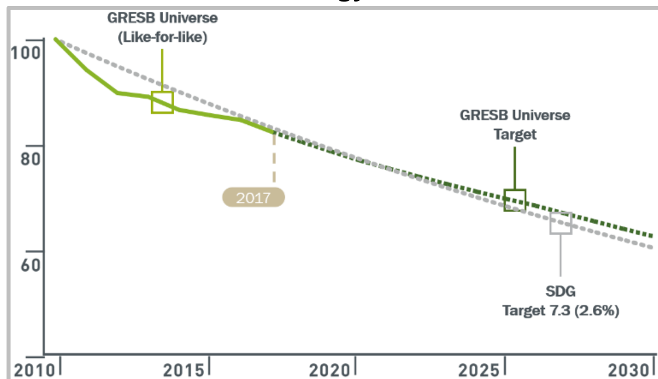
REIT earnings multiples remain elevated but not extremely so. With the market decline into quarter end that has extended into October, value is emerging. Discounts to private market values are becoming more prevalent; in the past, this has led to share buybacks and more M&A. As market volatility seems set to return, the diversification benefits of global REITs should become ever more apparent.

2018 GRESB survey results

During the quarter, GRESB (Global Real Estate Sustainability Benchmark) published the results of its annual Real Estate Assessment, which benchmarks environmental, social and governance (ESG) performance of real estate companies.

This year like-for-like energy consumption of participating companies fell on average by 2.5%, while greenhouse gas emissions (GHG) reduced by 4.9%.

GRESB Like-for-Like Energy Reduction



Source: GRESB 2018 Real Estate Results

Once again listed companies overall ranked better than their unlisted peers. For listed companies around 58% of the FTSE EPRA NAREIT Developed index takes part in the survey, up two percentage points compared to last year. Pleasingly, 63% of our portfolio holdings (by weight) participated in the survey. Furthermore, our portfolio GRESB score is 74, significantly above the benchmark average of 70.

Of note, the portfolio owns the top four ranked REITs that are in the FTSE index. These stocks represent ~13% of the total portfolio.

We continue to engage with portfolio companies to improve their ESG disclosure and performance, particularly with companies not participating in the survey.

Notes from our recent European Tour

We recently toured some cities in Europe which included a trip to Berlin to attend Europe's Public Real Estate Association (EPRA) conference. Generally, Europe remains in a positive mindset, but the situation is brittle. The mood of the attendees was generally upbeat against an economic environment of steady growth and a real estate backdrop of intense competition for commercial real estate, except for retail.

That said, the positive tone on the continent was not echoed by those attending from the other side of the channel. Ironically, whilst the UK might be leaving the EU, its language will persevere as the accepted form of communication on the continent (handy for those of us who struggle with mother language). More on the UK later.

From our site visits, Paris and Berlin continue to be performing strongly but perhaps the most surprising economy was Milan. Given the well-publicised backdrop of the challenges facing the Italian banking sector, we did not get the feeling that the economy was greatly affected, at this point at least. There was a general belief that Milan Expo in 2015 had given the city greater confidence in its ability to organise itself effectively (by way of interest the site now is controlled by Lend Lease for future mixed-use development). Overall the city's infrastructure was as good as many other leading cities in Europe with an extensive underground system and at least 2 major airports servicing the city. The tragic events of the Genoa bridge collapse, and a less well publicised roadway failure outside Milan due to a major fire, did not feature in discussions. Given the food and the relatively affordable housing, it didn't seem a bad place to live a life.

Perhaps the most sobering discussion at EPRA came in an interview with Joschka Fischer, Germany's former foreign minister and Vice Chancellor in the Schroder government (if you are keen to learn more about an interesting character, we suggest you take a look at him through Wikipedia). Focused on the geopolitical situation, Herr Fischer spoke candidly of the challenges facing Europe, of it feeling abandoned by the U.S., of

China's warming embrace as an outreach of its belt and roads program (this latter topic covered extensively in The Economist October 8 edition). Hence the Continent is at an intersection where it is considering turning east or west, i.e. China or the U.S.? The refugee situation also was addressed. In response to some social unrest, Herr Fischer observed that those who were part of the old East Germany, less than 30 years since reunification, have not had time to properly reintegrate before being asked to accept a surge of refugees into what had long been an economically constrained area and which was effectively mono-cultural. Clearly a delicate topic, and in a city where there are monuments apologising to just about every walk of life (except the Nazis), it did not come across as anything other than pragmatic.

There was genuine disappointment with the UK's impending departure, and I did not sense it was simply because of the UK's financial strength. There was a feeling Europe and the EU is better for the inclusion of the UK, the long period of peace since 1945 in no small part due to its presence. When he declared that he admired the UKs defiance of the Nazi's it was a genuinely emotional moment in the room that earnt a surprisingly emotional candid response from the English host who reciprocated to the applause of the audience. Clearly this was not the type of cross section which decided the Brexit vote or are confronted by the day to day issues associated with the refugee crisis.

With less than 2 years till the next German federal election there is pressure for Angela Merkel, the most enduring leader in Europe, to resign now in order for new leadership to establish itself before the election.
A change in German leadership would produce some interesting dynamics at the same time as the UK is seeking to leave the EU. Whilst a Brexit deal is expected to be thrashed out before the official deadline, it is not a given, particularly with Boris Johnson playing the role as the Callithumpian conductor. Whatever the case, given the UK maintained its own currency, it is plausible the Brexit transition will be an extended transitional process. In any case, one cannot easily sense what the positives for London are.

Unilever's decision during the quarter to move its listing from the London to Amsterdam Stock Exchange is a sign of the growing concerns among corporates. The decision was subsequently overturned after a revolt by many of its UK domiciled shareholders, this too a sign that London remains a major steward of capital, a role it will not give up without a fight. But it is a sign of broader corporate moves including several banks shifting capital and operations from London to major cities on the continent, and to Dublin.

Whilst office tenants are upgrading to more efficient, desirable space in London, they remain circumspect with recognition that, in order to close the deal, they require more flexibility around lease term and greater incentives, typically in the form of longer rent-free periods.

Interestingly occupation in the London office market has remained stable thanks largely to the out sized growth of co-working operators. WeWork is now the largest private tenant in London. Perhaps this growth is a reflection of the growing lack of confidence of larger tenants taking space in the market.

And then there's Scotland which is already pushing for another vote on independence as part of the "devolution" movement. The last referendum on the matter in 2014, almost two years before the Brexit vote, was narrowly defeated, although any new poll would likely be strongly resisted by Westminster. Already grappling with what to do about the Ireland/Northern Ireland border, Scotland's breakaway and desire to remain in the EU would further complicate border security, one of the major issues in the Brexit debate.

UK retail is in a world of pain with several leading department stores battling solvency issues and pressure on profits. The e-commerce challenge is not helped by waning consumer confidence as well as rising costs including business rates (tenants pay property rates, called business rates, which recently increased dramatically as the prior review took place in the depths of the GFC) and finance costs. These conditions have encouraged several private retailers including department stores and specialty chains, to trigger Corporate Voluntary Arrangements (CVAs) which allow them to renegotiate rents and/or terminate select leases. Shopping centre cap rates are showing some signs of weakening, that they haven't already perhaps the most surprising aspect.

The view from Europe about Australia

Without downplaying Australia's challenging relationship with its northern neighbours, one can't help but feel how our geopolitical situation is blissfully naïve if not absurdly self-indulgent. Bemusingly, in most European countries visited, there was a great level of

interest in Australia's political situation, the common observation: with an economy that looks to outside observers to be relatively stable, why all the changes of our Prime Minister? That coming from the Italians was a touch embarrassing.

Other little curiosities

Europe is discussing abandoning daylight saving (maybe Joh Bjelke Peterson was right after all).

Meanwhile, the new London taxis have hit the streets. After a debate a couple of years ago about a new design I think they have settled on a good outcome, keeping the character and improving the comfort (improved ride and seating for six) and environmental aspects, a new hybrid engine which runs on petrol as opposed to the old diesels. And the London cabbies seem very happy with their new work environment.

Old and New

Source: www.uk.motor1.com

Contact Details

Marco Colantonio
Portfolio Manager
Email: marco.colantonio@rescap.com

Andrew Parsons
Managing Director - Portfolio Manager
Email: andrew.parsons@rescap.com

Robert Promisel
Portfolio Manager
Email: robert.promisel@rescap.com

Jan de Vos
Portfolio Manager
Email: jan.devos@rescap.com

Resolution Capital Limited
Level 38
Australia Square Tower
264 George Street
Sydney NSW 2000

GPO Box 553
Sydney NSW 2001

Tel: +61 2 8258 9188
Fax: +61 2 8258 9199

Interests in the Resolution Capital Global Property Securities Fund (Unhedged)- Series II ('Fund') (ARSN 118 076 529) are issued by Pinnacle Fund Services Limited, ABN 29 082 494 362, AFSL 238371, as responsible entity of the Fund. Pinnacle Fund Services Limited is not licensed to provide financial product advice. You should consider the Product Disclosure Statement of the Fund available at https://www.rescap.com/funds/ in its entirety before making an investment decision. Resolution Capital Limited ('Resolution Capital', 'RCL') (ABN 50 108 584 167 AFSL 274491) is the investment manager of the Fund. Pinnacle Fund Services Limited and Resolution Capital believe the information contained in this communication is reliable, however its accuracy, reliability or completeness is not guaranteed. Any opinions or forecasts reflect the judgment and assumptions of Resolution Capital and its representatives on the basis of information at the date of publication and may later change without notice. The information in this communication is not intended as a securities recommendation or statement of opinion intended to influence a person or persons in making a decision in relation to investment. This communication is for general information only. It has been prepared without taking account of any person's objectives, financial situation or needs. Any persons relying on this information should obtain professional advice before doing so. Past performance is not a reliable indicator of future performance.