Folkestone
MAXIM A-REIT SECURITIES FUND

FOLKESTONE MAXIM A-REIT SECURITIES FUND

MARCH 2017 REPORT

MARKET REVIEW

During March, the US Federal Reserve carried out one of the three anticipated Federal Fund rate hikes for 2017, taking the cash rate 25 basis points higher to a range of 0.75-1.00%. The outlook however, was perceived to be 'dovish' and generated concerns about the US economy going into a period of reflation.

Here in Australia, the Reserve Bank (RBA) left rates unchanged at 1.5% following its Board Meeting in March. The stronger than expected fourth quarter 2016 GDP and robust labour market gave the RBA confidence in holding rates steady in the face of house price strength, particularly in Sydney and Melbourne.

The Australian yield curve direction continues to mirror the US with Australian 10 year bonds reaching a 12 month high of 2.98% on 10 March before receding to 2.69% at month end.

On the last day of the month, the Australian Prudential Regulation Authority (APRA) released a new set of macro-prudential rules for mortgage lending in Australia. New measures include a limit of 30% of new mortgage lending to interest-only loans (previously 40%) and the current 10% cap on investor mortgage lending will remain, but banks are expected to manage this cap such that they remain comfortably below the benchmark.

Dwelling prices rose 3.4% in the March quarter taking the annual house growth to 12.9%. Price gains were concentrated in Sydney and Melbourne where prices are up 18.9% and 15.9% in the year, while prices in Perth continued to fall and are down 4.6% over the year.

The strength in the house prices can be partly attributed to the population growth with net overseas migration increasing by 8.9% over the year to September 2016. Whilst the national population growth is at 1.5%, 68% is concentrated in Sydney and Melbourne with Sydney growing by 109,605 and Melbourne by 127,498 people.

Retail sales grew 0.4% in January with non-discretionary spending growth steady at 3% year-on-year, while discretionary spending remained subdued mainly from weakness in department stores and apparel sales.

The S&P/ASX 300 Index gained 3.3% over the month of March, reaching a two-year high. Among the sectors, the largest gains were in Utilities (+6.3%), Health Care (+5.7%) and Consumer Staples (+5.7%).

Some of the larger discretionary retailers weakened over the month, with JB

KEY STATISTICS
as at 31 March 2017

Status	*Open*
Fund Maturity	*Open Ended*
Investments	*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

Asgard
BT Wrap
Macquarie Wrap Solutions
Netwealth
Powerwrap
Symetry
HUB24

TOP 5 HOLDINGS
(Active Overweight)

APN Property Group
Eureka Group Holdings
Rural Funds
Folkestone Education Trust
Industria REIT

Fund Performance to 31 March 2017

Folkestone Maxim A-REIT Securities Fund	March 2017 %	6 Months %	1 Year % p.a.	3 Years % p.a.	5 Years % p.a.	7 Years % p.a.	10 Years % p.a.	Since Inception % p.a.*
Growth Return	+0.55	-0.80	+5.57	+12.83	+12.02	+8.50	-1.13	+0.93
Income Return	+0.93	+2.27	+5.37	+5.56	+6.06	+5.27	+3.03	+3.77
Total Return (After Fees but Before Tax)**	+1.48	+1.46	+10.93	+18.39	+18.08	+13.77	+1.90	+4.70
S&P/ASX 300 A-REIT Accumulation Index	+0.71	-0.81	+6.31	+16.76	+16.87	+12.79	+0.48	+3.45
Value Add	**+0.77**	**+2.27**	**+4.62**	**+1.64**	**+1.21**	**+0.99**	**+1.42**	**+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.

Hi-Fi (-7.9%) and Harvey Norman (-12.0%) in particular, hit by fears over implications of a possible entry of Amazon into the Australian market. This was also evident in the A-REIT sector as Vicinity Centres (VCX) and Scentre (SCG) returning -2.1% and -1.6% respectively.

Over the month of March, the S&P/ASX 300 A-REIT Accumulation Index returned 0.7%, underperforming the Australian equities market (S&P/ASX 300), which returned 3.3%. For the March quarter the equities market returned 4.7% compared to the S&P/ASX 300 A-REIT Accumulation Index which fell 0.1%. For the rolling 12 months to March 2017, the S&P/ASX 300 A-REIT Accumulation Index returned 6.3%, underperforming the Australian equities market which rose 20.2% (Figure 1).

For the March quarter, the Health Care A-REIT sub-sector provided the best performance with a return of 11.1%. The next best sub-sector comprised Industrial A-REITs which returned 8.1%, followed by Specialised A-REITs at 4.0%, Diversified A-REITs at 3.0%, Residential A-REITs at 2.7%, Office A-REITs at 1.3% and Retail A-REITs at -4.2%.

The three best performing securities in the S&P/ASX 300 A-REIT Index for the March quarter were Charter Hall Group (CHC +16.5%), Arena REIT (ARF +13.9%) and Folkestone Education Trust (FET +10.1%). The three worst performing securities were Vicinity Centres (VCX -5.4%), Scentre Group (SCG -5.3%) and National Storage (NSR -4.3%).

ACTIVITY

Mirvac Group (MGR) released stage one of its Sydney Olympic Park apartment development, selling 75% of the 260 apartments released on the first day.

During the month, both Charter Hall Long WALE REIT (CLW) and PropertyLink Group (PLG) were added to the S&P/ASX 300 Index which brings the total number of securities in the Index to 32.

National Storage (NSR) announced it had entered into JV with Leyshon Group to acquire and develop a site on Bundall Road, Bundall on the Gold Coast. NSR also announced the acquisition of two freehold storage centres in Dunedin, New Zealand.

MERGERS & ACQUISITIONS

There was little news on mergers during the month except for the continued takeover bid from Cromwell Property Group (CMW) for Investa Office Fund (IOF) and Astro Japan Property Group's (AJA) offer from Lone Star Real Estate to acquire 100% of its portfolio which it subsequently rejected.

DEBT AND CAPTIAL MARKETS

There were several debt issuances during the month including Westfield Corporation's (WFD) £800m of senior guaranteed notes in the UK plus a further US$500m of five year US Senior Guaranteed notes. Scentre Group (SCG) issued US$500m of 10 year senior guaranteed notes at a margin of 170 basis points. In addition, ALE Property Group (LEP) issued $150m Aussie MTN's at a fixed coupon of 4.0%; whilst Growthpoint Property Group (GOZ) issued A$208m USPP's at an average margin of 213 basis points.

Villa World (VLW) completed a $20m placement at an issue price of $2.25 per share, representing a discount of 5.5% to the closing price. The proceeds will be used for future acquisitions and joint venture opportunities.

SECTOR VALUATION

As at the end of March, the A-REIT sector was trading at a FY17 estimated distribution yield of 5.2%, representing a 343 bps premium to the RBA Cash rate and a 283 bps premium to 10 Year Bonds (Figure 3).

The sector's look-through gearing currently stands at an acceptable 29%, whilst it is trading at a premium to NTA of 23% compared to the 25 year average of 14%.

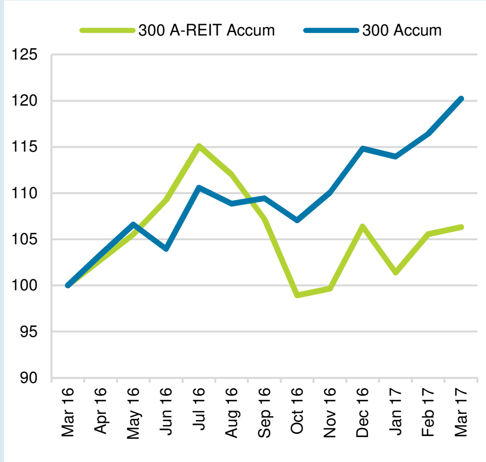
PERFORMANCE REPORT

March 2017

For the month of March 2017, the Fund returned +1.48% (on an After Fee but Before Tax basis), outperforming the Fund's Benchmark (S&P/ASX 300 A-REIT Accumulation Index) by +0.77%.

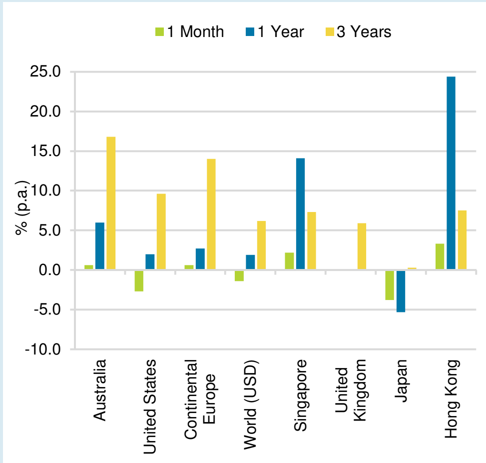
Positive contributions to returns in March 2017 came from the Fund's overweight holding in Rural Funds Group (RFF +7.0%), APN Property Group (APD +2.4%) and a

Figure 1: A-REIT vs. Equity Performance: 12 months to 31 March 2017



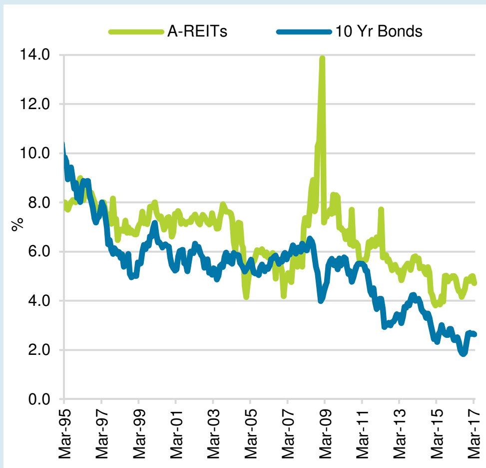
Source: IRESS

Figure 2: Global REIT Performance: to March 2017



Source: UBS, returns in local currencies

Figure 3: A-REIT Sector EPS and DPS Yields vs. 10 Year Bonds Yields: 1995 – 2017



Source: IRESS

zero weighting to Stockland Group (SGP -1.7%) and Vicinity Centres (VCX -2.1%).

Detracting from returns, included zero holdings in Charter Hall Group (CHC +4.9%) and Abacus Property Group (ABP +4.5%) and an underweight exposure to Westfield Corporation (WFD +0.9%).

March Quarter 2017

Over the March 2017 Quarter, the Fund returned +1.65% (on an After Fee but Before Tax basis), compared to the S&P/ASX 300 Accumulation Index of -0.08%.

Positive contributions to returns in the March Quarter came from the Fund's exposure to Folkestone Education Trust (FET +10.1%) and Rural Funds Group (RFF +8.5%) and a zero exposure to Vicinity Centres (VCX -5.4%).

Detracting from returns can be attributed to a zero exposure to Stockland Group (SGP +1.3%), Charter Hall Group (CHC +16.5%) and Abacus Property Group (ABP +10.6%).

Year to March 2017

For the 12 months to March 2017, the Fund returned +10.93% (after Fees but Before Tax), outperforming its benchmark by 4.62%.

The table below highlights our key active positions which have contributed most to the Fund's outperformance over the year to March 2017.

Contributions to Returns: 12 Months to 31 March 2017	
Folkestone Education Trust (FET)	Over weight
APN Property Group (APD)	Over weight
Rural Funds Group (RFF)	Over weight

At the end of March 2017, the Fund's investments comprised 15 ASX listed securities totaling 95.4% of the portfolio, 10 of these securities were constituents of the S&P/ASX 300 A-REIT Index whilst the remaining 5 securities were Ex-Index securities. Unlisted securities comprised 0.1% of the portfolio and the remaining 4.5% was held in cash/liquid investments.

A March 2017 Quarter distribution of 0.9309 cents per Unit (paid to investors early in April 2017), took total distributions for the year ended 31 March 2017 to 4.30 cents per Unit.

OUTLOOK

Markets are likely to continue to be volatile in the short to medium term whilst US president Trump plays out his first 100 days and beyond. The market will keep a close watch on whether the newly elected president is able to deliver on his campaign promises, in particular tax cuts.

In the first quarter 2017, Australia's 10 year bond rate traded in a range of 2.58% to 2.92% and finished the quarter at 2.69%. After a 6.75% rise in the S&P/ASX 300 A-REIT Accumulation Index in December 2016, the Index fell 4.7% in January 2017, rose 4.1% in February and was relatively flat in March, rising 0.7% post the February reporting period.

Office fundamentals continue to improve, for Sydney and Melbourne with limited supply and stock withdrawals (particularly in Sydney) pushing vacancies to below 5.0%. Brisbane and Perth however, continue to experience weakness due to the on-going effects of the mining downturn.

The retail operating environment remains challenging as sales slowed markedly, with downside risk to retail portfolios impacted by recent tenant administrations (e.g. Dick Smith) that is likely to continue throughout 2017.

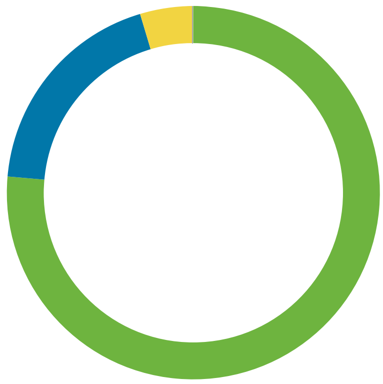
In the absence of corporate activity, we are forecasting a total return range of 7.0% to 9.0% for the A-REIT sector for the 2017 year. Should M&A activity become a feature, returns in excess of 10.0% could possibly be achieved.

However, the wildcard is bond yields. As we saw last year, the sudden uptick in bond yields drove an A-REIT sell off, and any further upward movement in bond yields could see further short-term pressure on A-REIT pricing.

The earnings outlook remains robust with consensus forecasts showing growth of circa 4.6% in FY18. The positive outlook is being driven by the office A-REITs which

ASSET ALLOCATION

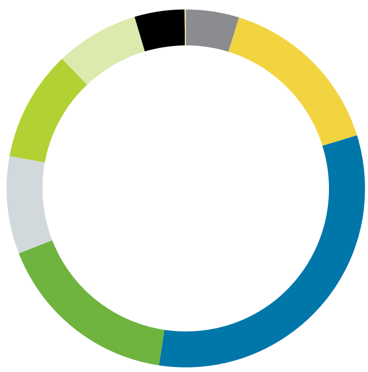
As at 31 March 2017



- S&P/ASX300 A-REIT - 76.4%
- Ex S&P/ASX300 A-REIT - 19.0%
- Cash - 4.5%
- Unlisted - 0.1%

SECTOR SPLIT

As at 31 March 2017



- Social Infrastructure - 4.8%
- Industrial - 15.4%
- Retail - 32.2%
- Diversified - 16.7%
- Office - 8.8%
- Developers & Managers - 10.0%
- Specialised A-REITs - 7.5%
- Cash - 4.5%
- Unlisted - 0.1%

Please note: Numbers in the graphs may not add up to 100 due to rounding.

are benefiting from the strong Sydney and Melbourne office markets. The active A-REITs who have strong development pipelines (Goodman, Mirvac) or funds management platforms (APN, GPT, Charter Hall, Goodman) and social infrastructure A-REITs (Folkestone Education Trust and Ingenia Communities) are benefiting from demographic and social changes.

Gearing levels remain reasonable, despite low interest costs. The balance sheet of A-REITs have clearly benefited from cap rate compression (pushing values higher), asset sales and more conservative payout ratios. Gearing levels could be at risk if cap rates increase (values fall), but we don't foresee any material upward movement in cap rates just yet; the weight of money from both domestic and offshore investors chasing assets should continue in the next year.

We continue to favour those A-REITs with exposure to the industrial and social infrastructure property sub-sectors, and those securities with quality management and relative attractive yields that have the ability to actively manage their portfolios to drive income growth in the year ahead.

CONTACT US:

Winston Sammut
Managing Director
Folkestone Maxim Asset Management
e: wsammut@folkestone.com.au
t: + 61 2 8667 2825

Lula Liossi
Investor Relations Manager
e: lliossi@folkestone.com.au
t: + 61 3 9046 9946

Harry Horwitz-Rourke
Distribution Manager
e: hhorwitz@folkestone.com.au
t: + 61 2 8667 2830

Celebrating MONEY MANAGEMENT 30 Years
FUND MANAGER OF THE YEAR 2017
Lonsec
FINALIST
Emerging Manager

Celebrating MONEY MANAGEMENT 30 Years
FUND MANAGER OF THE YEAR 2017
Lonsec
FINALIST
Property & Infrastructure Securities

ATCHISON CONSULTANTS RECOMMENDED

Recommended Lonsec Research

MORNINGSTAR ★★★★★

★★★★★ Superior SQM research