Specialist Property Funds

Property fund expert Martin Gilbert of DTZ Investors takes a detailed look at three specialist strategies that have won the backing of local authorities.

Specialist property funds that local authorities love

When you drill down into the property fund investments of local authorities, many portfolios have a high weighting to core, balanced funds rather than funds specialising in a certain sector of the property market.

In the context of investors seeking diversification within their property exposure, the logic here is understandable; investment in the right balanced funds should provide an investor exposure to returns in keeping with the property market as a whole.

However investment in specialist vehicles allows the investor to target the stronger performing areas of the market and therefore achieve out-performance.

So which specialist funds should investors be targeting in today's market?

DTZ Investors source potential fund investments, carry out due diligence, and monitor fund and portfolio performance, repositioning portfolios periodically according to our market views. Clearly portfolios should be tailored to suit specific investment objectives, time horizon, liquidity needs and risk parameters. But, assuming an investor is seeking to achieve above benchmark returns, DTZ Investors would currently look to include the following three specialist unlisted property funds in their portfolio.

Market segment to tap: students

UNITE UK Student Accommodation Fund (USAF)

The student accommodation sector provides a yield advantage of close to 1% above the real estate market average. Student accommodation providers are reporting high occupancy rates despite tuition fee increases, with persistent demand both from domestic and international students, structural undersupply and a constrained future pipeline supports our expectation of rental growth. Legislative changes should also help. The government's decision to lift the cap on the number of students recruited for the 2015/16 academic year should result in increased student numbers going forward.

USAF aims to combine current income with long-term capital growth by managing and acquiring a diversified portfolio of institutional quality student accommodation properties within the UK. USAF is the largest UK unlisted student accommodation fund, has maintained its high portfolio occupancy rate in the 2014/15 academic year despite uncertainty surrounding affordability and has achieved impressive rental growth (averaging circa. 4.5% p.a. since fund launch). Despite the inward yield shift which has already been seen in the first half of 2015, we continue to classify USAF as a BUY.

Modern Investor note: this fund is a very popular choice among local authorities with nineteen of them owning it.

Market segment to tap: online shopping

Industrial Property Investment Fund (IPIF)

The changing retail landscape is playing into the hands of the industrial sector. The growth in online retail has led retailers to consolidate store portfolios and concentrate on improving the efficiency of their distribution networks. The industrial sector is the highest yielding of the core real estate sectors and given that we are at the tail end of the current capital growth cycle, property with an income advantage is likely to outperform the wider market over the next investment period.

IPIF invests in good quality, higher yielding, and predominantly multi-let industrial estates. The fund has had an extremely successful year and we rate the teams involved in running the fund highly. IPIF has a very well diversified tenant mix and an equally wide ranging portfolio, providing significant asset diversification with favourable weighting to the South vs. the North as well as an attractive level of exposure to London and the South East. IPIF has a strong track record, outperforming the benchmark at property level in every calendar year since launch in 1997, and a high level of both experience and continuity in the management team.

Modern Investor Note: we found a total of 24 local authorities owning this fund. Dundee has £25.4 million in it, the largest holding we have found to date, closely followed by East Sussex with £25.3 million. Rhondda Cynon Taf, the second largest council in Wales, has an exposure of £14.4 million.

Market segment to tap: leisure spending

Leisure Fund Limited Partnership (Leisure Fund)

The leisure sector has demonstrated resilience during and since the recession: leisure operators are continuing to trade well as the UK consumer prioritises leisure spend with their disposable income and we believe that this trend will continue, with leisure schemes able to maintain relatively low vacancy rates while rents are currently at affordable levels, providing high rent cover ratios and the prospect of strong rental growth. A high proportion of leases are also long and allow for fixed annual uplifts.

The Leisure Fund targets investment in good quality leisure schemes which dominate strong catchment areas, with preferred schemes anchored by multiplex cinemas. The fund has a good balance of core assets complemented by assets which deliver value add opportunities. The leisure sector itself remains attractive for investors, driven by the long leases and rental growth prospects. The market is underpinned by the strength of the occupational market and the growth of cinema, hotel, pub and restaurant operators and their expansion aspirations. The fund manager has a good track record and we believe that recent acquisitions should deliver outperformance against the wider sector, helping to deliver continued strong performance going forward.

Modern Investor note: Leisure Fund Limited is owned by at least seven local authorities. Again Rhondda Cynon Taf has the largest – or one of the largest - exposures at £11.1 million.

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