

APN AREIT



Role in Portfolio:

Core

Risks:

- Will deviate from benchmark
- Reliance on broker inputs for models

Morningstar Analyst:

Mark Laidlaw

Morningstar Take

APN AREIT has most of the bases covered for those seeking dedicated Australian listed property exposure. Trusted skipper Michael Doble is one of the key strengths here. With over 20 years' experience in the sector, he's invested through multiple market cycles, something difficult to manufacture. Doble leads a well-informed team of six and has quality portfolio manager support from Damian Diamantopoulos, Peter Morrissey, and Andrew Smith. They also benefit from APN's direct property teams for market insights and trends. APN has a more conservative framework than most of its peers – the firm tends to take a long-term view with a distinct yield focus, as well as favouring property stocks with limited foreign exposure and corporate earnings. At first glance, the reliance on broker-built valuation models could be seen as a drawback. APN argues that more value can be added by focusing time and resources on factors such as pricing risks and sensitivity/scenario analyses. We agree that this has worked well for the shop historically when looking at the other portfolios the house manages. APN is also comfortable investing in the smaller property companies, a sizeable position in Carindale Property Trust a case in point. Investors should be aware that the portfolio on offer here will have a different shape to both its rivals and the wider market – for example, the maximum allowable position in Westfield Group is half its index weight. Our expectation is that over time APN AREIT is likely to lag in hot markets, but offer a welcome level of protection in down periods. APN does the right thing for investors when it comes to turnover and fees. This makes the strategy more tax-efficient and gives it a headstart over expensive alternatives. In a sector where the herd mentality is strong, APN is commendably willing to adopt a different perspective. We believe the team quality and investment process make APN AREIT one of the more attractive options available.

Strategy/Process

APN's Australian Real Estate Investment Trust (AREIT) strategy sets out to deliver a high level of distributable income each month, with a gross annual yield in excess of 110.0 percent of the yield of the S&P/ASX200 AREIT Accumulation Index. APN Funds Management also seeks to achieve capital appreciation in line with the Consumer Price Index. Unlike other APN property portfolios, AREIT invests solely in listed property securities, rather than being a listed/direct hybrid. APN has a conservative approach to investing. At the individual stock level, the team considers management quality, gearing levels, and sources of income, before valuing eligible stocks. Discounted cashflow models are used primarily to derive a net present value, while sum-of-the-parts valuation is also used for more complex business structures. Each stock is primarily ranked on the basis of its yield and valuation metrics, from which the team builds a portfolio with the desired yield traits. APN relies heavily on broker data for the firm's valuation models. The firm aims to limit exposure to stocks that generate significant earnings from corporate sources (20.0 – 30.0 percent) and restricts the total level of foreign assets in the portfolio. Stocks that don't meet APN's criteria that are key index components – such as low-yielding Westfield – may be held at a reduced index weight. Annual turnover is very low at around 10.0 percent, keeping transaction costs to a minimum. The long-term approach is also attractive from an after-tax perspective. AREIT will typically be fully-invested, but can hold up to 10.0

Flagship Fund: APN AREIT Fund

Investment Style 31 Jan 2011

Value	Core	Growth		
			Large	Pr/Pros Ern Rto 12.43
			Mid	Price/Book Rto 0.74
			Small	Price/Cf Rto 11.58
				Lt Ern Growth 9.53
				Mkt Cap (\$Mil) 2,626
				Dividend Yld % 5.95

Stock Sectors 31 Jan 2011

	%
Information Economy	0.00
Software	0.00
Hardware	0.00
Media	0.00
Telecommunications	0.00
Service Economy	100.00
Healthcare Services	0.00
Consumer Services	0.00
Business Services	0.00
Financial Services	100.00
Manufacturing Economy	0.00
Consumer Goods	0.00
Industrial Materials	0.00
Energy	0.00
Utilities	0.00

Top 10 Stock Holdings 31 Jan 2011

	%
Westfield Retail Trust	14.59
Westfield Group	12.77
CFS Retail Property Trust	11.61
Challenger Diversified Property Group	6.02
Dexus Property Group	5.91
Mirvac Group	5.76
Carindale Property Trust	5.38
Cromwell Property Group	4.35
Bunnings Warehouse Property Trust	3.95
Charter Hall Retail REIT	3.74

Asset Allocation 31 Dec 2010

	%
Domestic Equity	0.00
Int'l Equity	0.00
Listed Property	98.96
Unlisted Property	0.00
Mortgages	0.00
Dom Fixed Interest	0.00
Intl Fixed Interest	0.00
Cash	1.04
Other	0.00

Portfolio Stats

Mgr Bmark: S&P/ASX200 AREIT
 Accumulation Index
 No. Stocks: 20 - 30
 Max Weight: 20.0 percent of net assets
 Min Weight: Zero
 Expd Track Error %pa: Not targeted
 Expd Turnover %pa: Low, typically 10.0-20.0%pa

People Stats

Lead Manager: Michael Doble
 Appointed: June 2003
 Years Experience: 24
 Team Size: 6
 Average Years Experience: 15
 Average Years Tenure: 5

percent in cash.

Role in Portfolio

Core. We believe that this is a Core Australian listed property holding, albeit one with an income focus.

People

APN has a deep and experienced bench running its Australian listed property strategies. Head of Investments Michael Doble oversees APN's range of investment capabilities, as well as the direct property funds. Doble has more than 20 years' experience and is someone we hold in high regard. He's the lead manager on this strategy, although Portfolio Managers Damian Diamantopoulos, Peter Morrissey, and Andrew Smith all have strong influence on the AREIT strategy. APN's direct property team is also a resource used by the team for market insights and trends. Remuneration is based on individual performance along with performance of the funds overall. Senior staff hold equity stakes in the parent company, as an incentive and mechanism for encouraging long-term staff retention.

Performance

APN AREIT has only been around since January 2009, so the short track record means that it's difficult to make any meaningful performance conclusions. That said, it's been so far, so good for investors. The annualised return to the January 2011 was 19.32 percent, 8.90 percent above the S&P/ASX200 AREIT Index. The strong showing in 2009 can be attributed in large part to APN's willingness to invest down the market-cap, names here having led the recovery after the slump in 2008. This strong relative showing continued in 2010, the 3.56 percent return putting APN AREIT in the top quartile of its peer group. This was assisted by positive attribution from names like Challenger Diversified Property and Cromwell Corporation. Investors should be aware that this level of outperformance is unlikely to be sustainable over the long term. We expect given APN's conservative nature that AREIT is likely to struggle in hot markets but should offer a greater level of resilience when markets are tumbling.

Parent

APN Funds Management is a Melbourne-based boutique fund manager specialising in property, fully-owned by ASX-listed APN Property Group. The shop had A\$940.0 million in real estate securities assets at 30 June 2010.

Fees

APN charges 0.85 percent per annum for AREIT, making it considerably cheaper than the retail peer average.

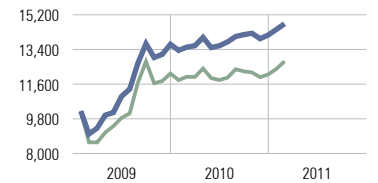
Top 5 Funds by Net Assets

	Ticker	Net Assets (\$Mil)	Quartile Rank 3yr	Total Ret 3yr
APN AREIT Fund	17006	118.23	NAv	--

Flagship Fund: APN AREIT Fund

Performance 28 Feb 2011 Fund Index

Growth of \$10,000 **\$14,530**



	1Yr	3Yr	5Yr	10Yr
Quartile Rank	█	NAv	NAv	NAv
Total Ret%	9.08	--	--	--
Income Ret%	9.18	--	--	--
Growth Ret%	-0.10	--	--	--
Index%	6.85	-13.86	-8.90	2.94

Index: S&P/ASX 200 A-REIT Acc
 Category: Australia Real Estate

Performance Analysis 3 Years to 28 Feb 2011

Value Add vs Cat Index%	N.Ap.
Tracking Error	N.Ap.
Information Ratio	N.Ap.

MPT Statistics 28 Feb 2011

	3Yr%	5Yr%	10Yr%
Beta	--	--	--
Alpha	--	--	--
R Squared	--	--	--
Sharpe Ratio	--	--	--

Risk Meter (3 Year Standard Deviation)

Not Available

All figures and stats relate to the Flagship Fund, and all performance figures are shown as % per annum, net of fees.

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