abrdn UK Real Estate Fund

Quarterly Update – Q4 2023

For Professional Investors only – Not for Retail distribution.
Past performance is not a guide to the future.

The abrdn UK Real Estate Fund quarterly update provides an overview of the market; fund performance, positioning and portfolio changes; and the fund manager's outlook for the months ahead.

abrdn UK Real Estate Fund, a Sterling denominated sub fund of the abrdn UK Real Estate Funds ICVC. This fund is managed by abrdn Fund Managers Limited.

abrdn UK Real Estate Fund invests in assets that may at times be hard to sell. This means that there may be occasions when you experience a delay or receive less than you might otherwise expect when selling your investment. For more information on risks, see the prospectus and key investor information document.

OBJECTIVES AND INVESTMENT POLICY

Investment Objective

To generate income and some growth over the long term (5 years or more) by investing in UK commercial property. It is intended that the sub-fund will be a PAIF at all times and, as such, its investment objective is to carry on property investment business and to manage cash raised for investment in the property investment business.

Performance Target: To exceed the return of the IA UK Direct Property Sector Average return (after charges) over rolling three year periods. The Performance Target is the level of performance that the management team hopes to achieve for the sub-fund. There is however no certainty or promise that they will achieve the Performance Target. The ACD believes this is an appropriate target for the sub-fund based on the investment policy of the sub-fund and the constituents of the sector.

Economic Overview and Property Market

UK inflation unexpectedly ticked higher in December, with the headline consumer price index rate increasing from 3.9% year-on-year to 4%. The increase was largely driven by an increase in tobacco duty, while food prices were once again a drag on inflation. The bigger picture is that headline inflation is still set to fall further over the next few months. It could easily be below 2% by the second quarter of 2024, aided by favourable base effects.

At the Bank of England's (BofE) December meeting, there was a concerted effort to push back against recent market pricing for an earlier rate-cutting cycle. Indeed, the policy communication and voting pattern suggest the BofE wants to keep alive the possibility of further rate hikes. However, a 'Table Mountain' profile for rates is unlikely to prove sustainable as headwinds mount and underlying inflation pressures fade. We expect rate cuts to start in June.

UK real estate pricing has been stabilising during 2023, following the significant correction in the sector in late-2022. However, performance has been varied across sectors, with those benefiting from structural and thematic tailwinds proving more resilient in the face of a weaker macroeconomic environment.

While UK real estate capital values declined over the course of 2023, the pace of decline moderated. There were tentative signs of stabilisation for some sectors but not all.

There is a risk that further price discovery in the first half of 2024 will result in softer pricing, particularly for out-of-favour sectors.

UK real estate investment volumes for the calendar year 2023 reached £34.3 billion, representing a year-on-year decline of 47%. While we expect greater liquidity to return to the market in 2024, this will in part be driven by buyer and seller expectations becoming more closely aligned.

Monetary policy and the wider macroeconomic backdrop were in the driving seat in 2023 and we believe this will continue to be the case in 2024. With the increased prospect of interest-rate cuts in 2024, we expect an improvement in UK real estate performance as we move through 2024. This will be driven primarily by improved investor confidence and greater liquidity in the market.

A UK general election is mandated to occur no later than 28 January 2025. At this stage, an election date in November 2024 looks most likely. The Labour party has currently opened-up a 20-point lead in the polls, relative to the Conservative party. At this stage, it appears likely there will be a change of government in the UK over the next 12 months.

Real-estate refinancing poses a risk to our outlook in 2024. But we believe that the risk is more heavily skewed towards the office sector, given the amount of outstanding debt and lack of appetite for lending in this sector.

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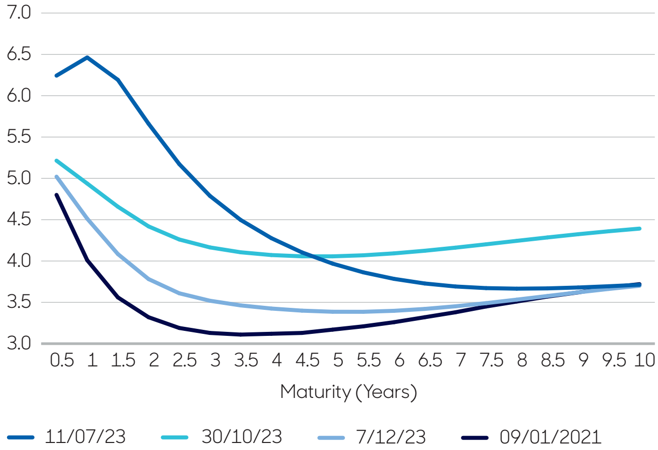
UK overnight index swap forward curve



Source: Bank of England, Bloomberg, abrdn January 2024.
Forecasts are a guide only and actual outcomes could be significantly different.

UK Economic Outlook

Activity: UK gross domestic product (GDP) growth rebounded in November, expanding 0.3% month-on-month, which was slightly better than the consensus of 0.2%. Services activity was the main contributor. The Office for National Statistics also noted that fewer strikes in November helped boost growth. Meanwhile, construction activity was weak in part due to weather effects. The monthly profile of GDP remains extremely volatile after a contraction of 0.3% in October, with the broad trend remaining one of sustained stagnation. Recession-like conditions look set to continue into 2024, but the prospect of further fiscal easing to be announced in March should help to limit the extent of the downturn.

Inflation: UK inflation unexpectedly ticked higher in December, with the headline CPI rate increasing from 3.9% year-on-year to 4%. The consensus was for UK headline inflation to drop to 3.8% in December.
The increase was largely driven by an increase in tobacco duty, while food prices were once again a drag on inflation. Underlying inflation pressures were also slightly stronger than expected. Core inflation was flat at 5.1% year-on-year. Inflation may move higher again in January, following a slight uptick in the Ofgem price cap. However, the bigger picture is that headline inflation is still set to fall further over the next few months. It could easily be below 2% by the second quarter of 2024, aided by favourable base effects. Meanwhile, cooling wage growth should help to bring underlying inflation pressure down too.

Policy: At the BofE's December meeting, there was a concerted effort to push back against recent market pricing for an earlier rate-cutting cycle. Indeed, the policy communication and voting pattern suggest the Bank wants to keep alive the possibility of further rate hikes. This signalling is not surprising as the combination of elevated wage growth and modest fiscal stimulus means policy makers are particularly sensitive to an easing in financial conditions. However, a 'Table Mountain' profile for rates is unlikely to prove sustainable as headwinds mount and underlying inflation pressures fade. We expect rate cuts to start in June.

UK Economic Outlook

(%)	2020	2021	2022	2023	2024	2025
GDP	(11.0)	7.60	4.10	0.40	0.00	1.50
CPI	0.90	2.60	9.10	7.30	2.70	2.20
Policy Rate	0.10	0.25	3.50	5.25	4.00	2.50

Source: abrdn December 2023.
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Fund positioning

Top 10 holdings	Value range (£m)
24/26 Minories, London	50m - 75m
Leamington Shopping Park, Leamington Spa	50m - 75m
Masthead Industrial Estate, Dartford	25m - 50m
Solar Park, Birmingham	25m - 50m
G&V Royal Mile Hotel, Edinburgh	25m - 50m
Io Centre & Tradeway, Sutton	25m - 50m
Axis Park, Peterborough	25m - 50m
The Old Dairy, South Ruislip	25m - 50m
1 America Street, London	25m - 50m
Bligh's Meadow Shopping Centre, Sevenoaks	10m - 25m

Source: abrdn, 31 December 2023.

Top 10 tenants	Contracted rent (%)
Motel (One) UK Limited	5.66
Radisson Hotel Edinburgh Limited	4.55
Tesco Stores Limited	4.45
ASDA Stores Ltd	4.31
T P Bennett LLP	3.17
Cine-UK Limited	2.36
Marks & Spencer plc	2.25
Technip UK Limited	2.20
Manchester Airport Plc	2.07
British Telecommunications plc	2.00

Source: abrdn, 31 December 2023.

Fund facts

Fund size	£921 m
Average lot size	£20.2m
Average lease length	7.6 years
Number of properties	39
Number of tenancies	350
Distribution yield[1]	4.66%
Unencumbered cash[2]	12.63%
Vacancy rate	4.69%

Source: abrdn, 31 December 2023.

[1] Historic Distribution Yield at 31/12/23. This represents the income generated by the assets in which the Fund has been invested over the last twelve months, expressed as a percentage of the Fund's value for the Institutional Income share class. Please note that this income stream may be subject to taxes and charges.

[2] The unencumbered cash figure includes cash or cash equivalents plus any short term assets and liabilities within the fund less any future committed capital expenditures.

Lease expiry profile	Contracted rent (%)
0 - 5 years	34.3
6 - 10 years	35.1
11 - 15 years	17.3
16 - 20 years	10.8
21 - 25 years	2.5

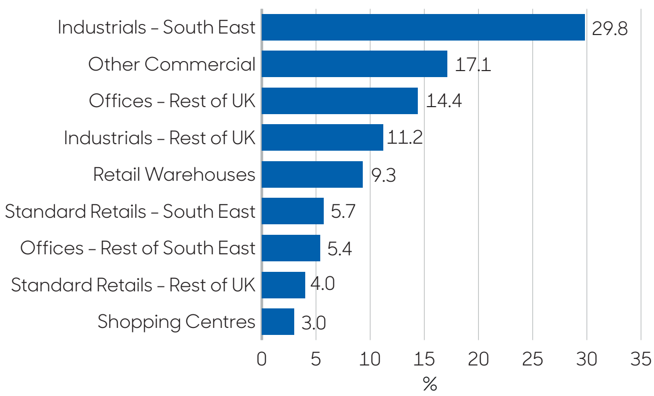
Source: abrdn, 31 December 2023.

Performance - % growth	3 mths	6 mths	1 yr	3 yrs	5 yrs
Fund Retail Acc	(2.97)	(4.21)	(2.33)	(1.27)	(1.93)
Fund Institutional Acc	(2.85)	(4.13)	(1.98)	(0.90)	(1.57)
Fund Platform One Acc	(2.90)	(4.12)	(2.04)	(0.94)	(1.60)
IA UK Direct Property[3]	(0.40)	(0.56)	0.30	0.19	(0.52)

Source: abrdn (Fund) and Morningstar (Target), 31 December 2023.

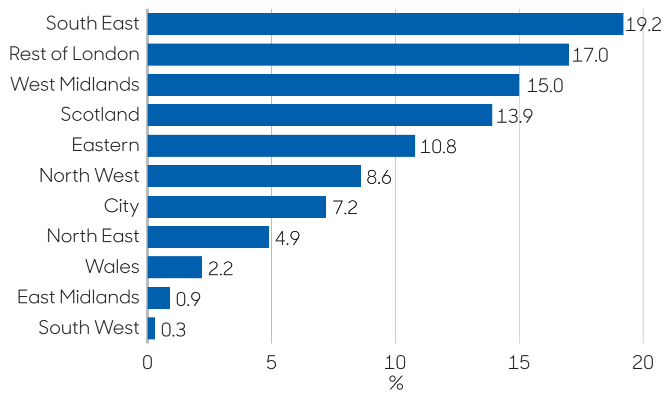
[3] Benchmark includes both master and feeder funds in the IA UK Direct Property Peer group.

Sector allocation



Source: abrdn, 31 December 2023.
Figures ex Cash.

Geographical breakdown



Source: abrdn, 31 December 2023.
Figures ex Cash.

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Portfolio Update

Transaction and Asset Management Activity

The Fund completed the sale of Raiths House Complex, Dyce, Aberdeen, for a headline price of £7 million during the quarter. The Fund also entered into agreements to acquire land adjoining its existing holding at Hydehurst Lane, Crawley, and develop a circa 62,000 square foot parcel hub pre-let to DPD at an initial rent of some £1.4 million per annum on a 25-year lease.

Focusing on income, several successful asset management initiatives completed during the period. In the office sector, at New Clarendon House, Edinburgh, where the Fund is undertaking a comprehensive refurbishment of a grade two listed office building to provide modern, open-plan office accommodation with an ESG/sustainability focus, agreement for leases with TLT and Atkins exchanged, securing a 10-year term at initial rents of £136,000 and £261,000 per annum respectively. At Hobart House, Edinburgh, a new lease to Teneo completed providing a 10-year term at an initial rent of £58,344 per annum. At Annandale House, Sunbury, a rent review was completed with BT Communications settling at a reviewed rent of £980,925 per annum, an uplift of 17%.

In the industrials sector, at Trilogy, Concorde Way, Fareham, a new lease was entered into with SAAB, securing a 10-year term at an initial rent of £481,050 per annum, equating to £11.25 per square foot). The estate is now fully let. At Axis Park, Peterborough, a new lease completed with De Raat Security Products, securing a 10-year term at an initial rent of £67,901 per annum (£6.80 per square foot). At Woodside Industrial Estate, Bishop Stortford, rent reviews with Cornelius Group, which occupies two units at the estate, provided a combined rent of £436,352 per annum, an uplift of 39%.

At 31st December 2023 the unencumbered liquidity in the Fund was 12.7% of net asset value.

Performance Review

Industrials was the only sector to record positive returns during the fourth quarter at 0.5%. This sector continued to record the strongest capital growth during December at -0.4%, with both south-east England and the rest of UK experiencing such a decline. Offices continued to see the weakest capital growth at -1.5%, driven by a decline of 2% for rest of UK offices. Retail recorded negative capital growth for the seventh consecutive month at -1.1%, with retail warehouses seeing a decline of -1.3%.

During the quarter, the Fund's overall capital movement was negative. The Fund's industrial assets saw the narrowest decline. The retail sector saw the greatest movement, driven by a single asset within south-east standard retail.

Forecasts and Outlook

UK commercial real estate returned -1.0% over the three months to the end of November (the latest data available), according to the MSCI UK monthly index. Industrial (+1.2%) was the strongest sector, while offices (-4.4%) were the weakest. Rapid disinflation in the UK means that real wages are now growing very strongly, which should limit the extent of any economic downturn. It has been the weakest year for UK real estate investment activity since 2009 given a significant gap between seller and buyer aspirations. Meanwhile, UK prime yields remained largely flat in December across the vast majority of sectors.

Discrete annual returns to 31 December 2023 (%)

	2023	2022	2021	2020	2019
Fund Retail Acc	(2.33)	(10.74)	10.39	(3.97)	(1.82)
Fund Institutional Acc	(1.98)	(10.39)	10.80	(3.61)	(1.53)
Fund Platform One Acc	(2.04)	(10.43)	10.78	(3.71)	(1.46)
IA UK Direct Property[1]	0.30	(7.63)	9.05	(2.67)	0.05

Source: abrdn, 31 December 2023.
[1] Peer Group includes both master and feeder funds in the IA UK Direct Property Peer group. Fund returns are net of fees.

Risk profile

Investors should be aware of the following risk factors:

- (a) Commercial property is less liquid than other asset classes such as bonds or equities. Selling property can be a lengthy process so investors in the fund should be aware that they may not be able to sell their investment when they want to.
- (b) Commercial property transaction charges are higher than those which apply in other asset classes. Investors should be aware that a high volume of transactions would have a material impact on fund returns.
- (c) Property valuation is a matter of judgement by an independent valuer and is therefore a matter of the valuer's opinion rather than fact.
- (d) The use of derivatives carries the risk of reduced liquidity, substantial loss and increased volatility in adverse market conditions, such as a failure amongst market participants. The use of derivatives may result in the fund being leveraged (where market exposure and thus the potential for loss by the fund exceeds the amount it has invested) and in these market conditions the effect of leverage will be to magnify losses. The fund does not make extensive use of derivatives.
- The fund employs a single swinging pricing methodology to protect against the dilution impact of transaction costs. A change in the pricing basis will result in movement in the fund's published price.
- All investment involves risk. This fund offers no guarantee against loss or that the fund's objective will be attained.
- Past performance is not a guide to future returns and future returns are not guaranteed. The price of assets and the income from them may go down as well as up and cannot be guaranteed; an investor may receive back less than their original investment.
- Inflation reduces the buying power of your investment and income. The value of assets held in the fund may rise and fall as a result of exchange rate fluctuations.
- The fund could lose money if an entity (counterparty) with which it does business becomes unwilling or unable to honour its obligations to the fund.
- In extreme market conditions some securities may become hard to value or sell at a desired price. This could affect the fund's ability to meet redemptions in a timely manner.
- The fund could lose money as the result of a failure or delay in operational processes and systems including but not limited to third party providers failing or going into administration.

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Important Information

The following risk factors should be carefully considered before making an investment decision:

- The value of investments and the income from them can fall and investors may get back less than the amount invested.
- The abrdn UK Real Estate Fund invests in assets that may at times be hard to sell. This means that there may be occasions when you experience a delay or receive less than you might otherwise expect when selling your investment. For more information on risks, see the prospectus and key investor information document.
- The use of derivatives carries the risk of reduced liquidity, substantial loss and increased volatility in adverse market conditions, such as a failure amongst market participants. The use of derivatives may result in the fund being leveraged (where market exposure and thus the potential for loss by the fund exceeds the amount it has invested) and in these market conditions the effect of leverage will be to magnify losses. The fund does not make extensive use of derivatives.
- Commercial property is less liquid than other asset classes such as bonds or equities. Selling property can be a lengthy process so investors in the fund should be aware that they may not be able to sell their investment when they want to.
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- Property valuation is a matter of judgment by an independent valuer and is therefore a matter of the valuer's opinion rather than fact.
- The fund employs a single swinging pricing methodology to protect against the dilution impact of transaction costs. Due to the high transaction charges associated with the fund's assets, a change in the pricing basis will result in a significant movement in the fund's published price.

To help you understand this fund and for a full explanation of risks and the overall risk profile of this fund and the share classes within it, please refer to the Key Investor Information Documents and Prospectus which are available on our website www.abrdn.com. The Prospectus also contains a glossary of key terms used in this document.

The fund's Authorised Corporate Director is abrdn Fund Managers Limited.

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