ASI Global Real Estate Fund

Quarterly Update - Q4 2019

Aberdeen Standard Investments

The ASI Global 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.

ASI Global Real Estate Fund, a Sterling denominated unit trust - This fund is managed by Aberdeen Standard Fund Managers Limited.

OBJECTIVES AND INVESTMENT POLICY

Investment Objective

To generate income and some growth over the long term (5 years or more) by investing in global commercial property markets.

Performance Target: To exceed the return of the MSCI Global Custom Property/MSCI World Real Estate Custom Index over rolling three year periods (before charges). The Performance Target is the level of performance that the management team hopes to achieve for the fund. There is however no certainty or promise that they will achieve the Performance Target.

The Manager believes this is an appropriate target for the fund based on the investment policy of the fund and the constituents of the index.

Economic overview

- Global investment volumes remain subdued and continue to be affected by uncertainty and a lack of suitable product. With a pause in trade tensions between China and the US, more certainty around the Brexit process and an easing of the confrontation in Hong Kong, global uncertainty has moderated. It is likely that there could be a slight pick-up in investment activity over the year ahead. There continues to be a significant amount of 'dry powder' on the sidelines, which is targeting real estate, with the expectation that interest rates are likely to stay at low levels for some time yet. On a relative basis, the yield on real estate continues to look attractive. In line with previous quarters, we don't anticipate there being a near-term catalyst in the absence of a global recession that will lead to global real estate pricing weakening significantly at present. Signs of price declines continue to be limited, apart from the UK market and specifically the UK retail sector.
- In the occupier markets, supply pipelines continue to be subdued and well below the peaks of the last cycle across most core developed markets. The risk of a supply induced correction remains relatively low. At a local level, some supply risks are materialising. This means that local knowledge and bottom-up asset selection are as critical as ever for strategy implementation. Positive global growth should continue to support occupier demand as the real estate cycle moves to a period of lower total returns. Net income growth, rather than falling yields, will be the main driver of future return expectations.
- At this point in the cycle, core prices appear stretched relative to estimates of long-term worth. Where market prices are above long-term worth, this implies that investors are not being adequately compensated for risk. In turn, this suggests investors may want to adopt a lower-risk profile at this stage and make selective sales to re-position portfolios accordingly. In this environment, seeking out value opportunities has become more challenging.

Real estate markets

North America

- Gross Domestic Product (GDP) growth in both the US and Canada slowed in 2019. The services sector has continued to expand; however, the trade war with China has disrupted global supply chains, which has negatively impacted the manufacturing sector. The manufacturing index from the Institute for Supply Management (ISM) in the US dropped sharply in 2019, signalling the sector's deepest contraction since the global financial crisis. Canadian sector trends were more positive, but Purchasing Managers' Index (PMI) readings suggest that activity remains sluggish. Activity is expected to decrease further next year, with GDP forecasts of less than 2%. That said, reduced trade tensions offers some upside potential. The phase-one trade deal with China includes cuts in certain tariffs on Chinese imports and increased Chinese purchases of US goods and services. The services segment of the US economy has strengthened recently, with the non-manufacturing ISM index rebounding in the final quarter of last year. Private-services sectors continued to produce solid job gains. The unemployment rate fell to a new 50-year low, supporting broad-based wage and consumption growth. Hiring in Canada accelerated last year, outpacing the US, particularly among office-using sectors. Weaker global growth, disruptive trade policies and muted inflationary pressures led to an additional 25 basis point (bps) rate cut by the US Federal Reserve (the Fed) in October. The Fed has signalled a pause, suggesting stable policy rates in the near term.
- Vacancies across all sectors remain tight relative to history, but we have also seen decelerating demand and rental growth. In 2019, industrial vacancies rose for the first time since the last recession. This was due to a slowdown in demand and accelerating supply. Leasing activity has likely been restrained by weak industrial production and imports, coupled with a tight labour market that has limited hiring. Rental growth has moderated, but the sector continues to strongly outperform from very low vacancy rates. Although the national office vacancy rate is stable, it is at its lowest level since 2001. Net absorption persisted at a steady pace, while supply was measured. Rental growth was tepid but secondary and tech markets with outsized job growth, such as

Charlotte and Seattle, posted robust gains. The retail sector is still under significant pressure. Demand growth reached its lowest level since the last recession, as store-closure announcements rose to a record level in 2019 (according to Coresight Research). Neighbourhood centres are performing relatively well – buoyed by grocery-anchored centres – as they have been resilient to e-commerce. Vacancies have steadily improved in the apartment sector. Development activity remains high, but supply has begun to moderate. This has led to a drop in concession rates, supporting effective rental growth. Canadian real estate markets are benefiting from attractive demand drivers and subdued supply. Outsized population and job growth have buoyed real estate demand. This has led to the tightest vacancies and rental growth in North America for apartment, industrial and office property types. However, the Calgary office market continues to suffer from the beleaguered energy sector.

- Healthy occupier fundamentals have continued to attract strong investor demand. Transaction volumes moderated in the final half of 2019, but remained well above historical levels. Industrials continued to experience rapid growth in sales and pricing during this period. Institutional capital is flowing into the industrial sector as a result of robust performance and a positive outlook. However, retail annual transaction volumes fell by nearly one-third and pricing remained below 2015–16 levels. Sales trends were stable among apartments and offices, but pricing continued to rise at a moderate pace.
- With the significant appreciation in prices over the past few years, overpricing risks remain evident in the North American market. This is particularly the case in the office sector where yields have fallen to low levels and an increase in construction levels is likely to dampen rental demand in the future. Market pricing suggests that the US residential and industrial sectors continue to be more attractively priced than the office and retail sectors, and are likely to offer better prospects for locating value opportunities. The retail sector, particularly secondary malls, continues to experience issues with structural demand that are unlikely to abate. In Canada, our indicators suggest that the office sector is not as overpriced as some of the other global office sectors. We remain positive on the forecast outlook for the North American markets. We continue to expect the market to deliver an income-type return in the medium term, although the downside risks have risen with yields hovering around new lows.

Continental Europe

- Eurozone economic activity remains weak, but may be finding a trough. Indeed, with Germany and the Netherlands set to use some of their fiscal headroom, we have made modest upward revisions to our growth forecasts. Nevertheless, the outlook is still for weak growth and sub-target inflation, which means that the ECB will probably have to ease policy again in 2020. The cyclical growth data in the Eurozone are not speaking with one voice. Measures of industrial activity, business confidence and trade volumes are extremely depressed, but may have stopped getting worse. On the other hand, measures of consumer confidence, spending and the labour market are more elevated, but starting to turn lower.
- Helpfully, the policy environment is set to turn slightly more supportive. European fiscal policy is loosening– the change in the Eurozone structural budget deficit is likely to add up to 0.5% to GDP in 2020. We therefore think that the bulk of the Eurozone growth slowdown is in the past, and expect a relatively flat profile for GDP growth over our forecast horizon. However, even with growth stabilising, the economy is set to expand around or just below trend – which means that inflation pressures should remain subdued. We therefore expect modest additional easing from the ECB, and have pencilled in a single 10 basis point rate cut in each of 2020 and 2021.There are two-way risks to our forecasts. Additional fiscal expansion represents a rare upside risk. But given the low starting point for growth, and the uncertain global trade policy environment, most risks are to the downside.

Asia-Pacific

- The economic slowdown in Asia during 2019 was worse than initially expected. The Asia-Pacific region is on track to register an average real gross domestic product (GDP) growth of just 4.4% in 2019. This compares with 5.2% the year before and the forecasted 5% at the start of the year. This would mark the slowest growth since 2010. A sharper-than-expected fall in exports and manufacturing was the key drag on economic growth last year, largely as a result of the trade dispute between the US and China.
- Social unrest in Hong Kong was a negative surprise in 2019. Coupled with the negative impact from the US-China trade war, which had already weighed on exports prior to the social unrest, Hong Kong is now on track to report a full year real GDP contraction of 1.1% for 2019 (from +3.8% in 2018). We believe political uncertainty will likely remain an overhang on investment in 2020, considering the legislative council election is scheduled to be held in September this year.
- In our base case, we expect growth to stabilise at a low rate in 2020. We expect the slowdown in manufacturing to stabilise with a small rebound in exports in 2020. Coupled with the delayed impact from tax and interest rate cuts in Australia and India, we expect real GDP in Asia-Pacific to grow an average of 4.5% in 2020 (from 4.4% in 2019). The upside risks to this forecast include a faster-than-expected turnaround in the global tech cycle, which will likely benefit markets such as Taiwan, Korea and Singapore. The downside risks include ramifications from potential geopolitical conflicts, a faster-than-expected pick-up in inflation (and by extension, the implication for monetary policy), and a significant deterioration in the situation in Hong Kong.

This information is for professional clients and investment professionals only and should not be relied upon by retail investors.
Past performance is not a guide to the future.

ASI Global Real Estate Fund

Quarterly Update - Q4 2019

Aberdeen Standard Investments

Fund positioning

Top 10 direct assets	Fund %
432 St Kilda Rd, Melbourne	7.9
WTC Almeda Park Building 4, Barcelona	7.6
44 Esplanade, St Helier, Jersey	7.2
DC Goossens, Veghel, The Netherlands	7.1
3 & 5 Custom House Plaza, Dublin	7.1
Galeria Gniezno, Poland	6.5
Niu Fury Hotel Messe München	4.8
Fleming Court, Dublin	4.3
Retail Park Hana, Kafkova, Czech Republic	3.9
11 Amour Street, Milperra, NSW	3.7

Source: Aberdeen Standard Investments, 31 December 2019.
Figures exclude Cash.

Top 10 tenants (Direct only)	% Contracted Rent
Ogier	12.1
Goossens	8.9
Revlon	7.0
Citco	5.4
Novum Hotels Süd GmbH	5.3
Jamestrong Packaging Australia Pty Ltd	4.6
Dutch Heart Foundation	4.1
Mainfreight Logistics Pty Ltd	3.0
Coil Steels Group Pty Ltd	2.7
Maxol Ltd	2.4

Source: Aberdeen Standard Investments, 31 December 2019.
Figures exclude Cash.

Fund facts

Fund size	£520.0m
Average lot size	£20.7m
Average lease length	4.7 years*
Number of direct properties	16
Number of tenancies	144
Distribution Yield	2.37%**
Standing Void	4.08%

Source: Aberdeen Standard Investments, 31 December 2019.
*Average Unexpired lease term (to first break) - Yrs

**Yields are historic based on the preceding 12 months' distributions as a percentage of the mid market unit/share price at date shown. Yields will vary, do not include any preliminary charges, and investors may be subject to tax on distributions. Based on institutional income shareclass.

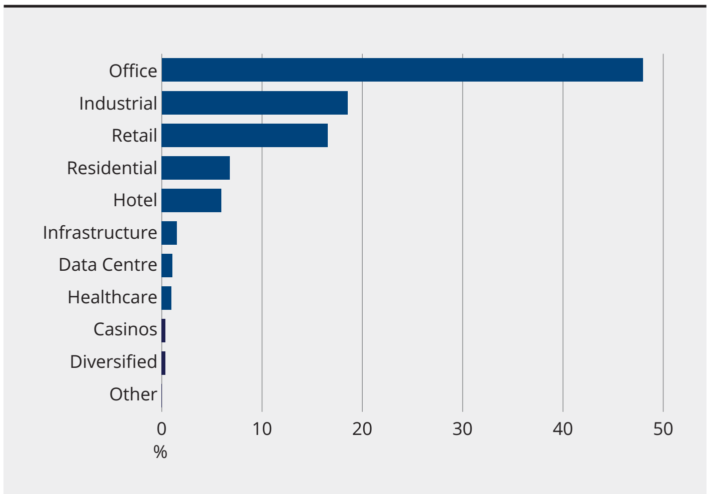
Top 5 listed holdings	Fund %
Equity Lifestyle Properties	1.30
Duke Realty	1.28
American Tower	1.26
Prologis	1.23
Alstria Office	0.96

Figures exclude Cash.

Performance - % growth	3 mths	6 mths	1 yr	3 yrs*	5 yrs*
ASI Global Real Estate Fund	-0.2	5.7	10.2	5.4	6.6

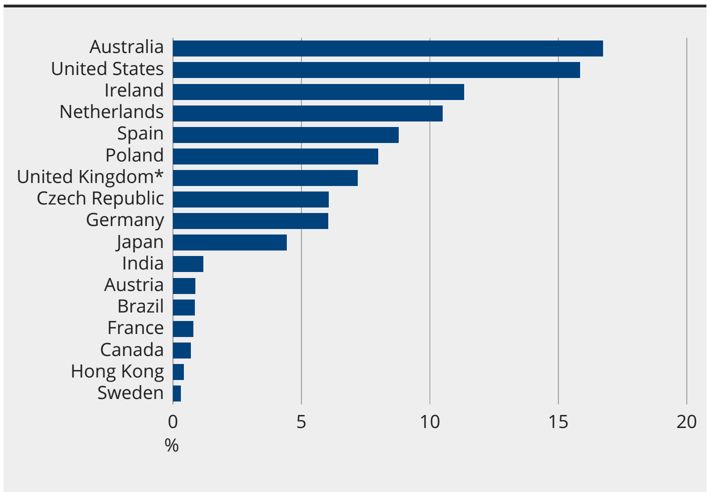
Source: Aberdeen Standard Investments, 31 December 2019.
Fund performance is quoted net of institutional fees (GBP).
*Returns are annualised

Sector allocation



Source: Aberdeen Standard Investments, 31 December 2019.

Geographical breakdown



Source: Aberdeen Standard Investments, 31 December 2019.

*MSCI classify the Channel Islands as part of the UK for benchmarking purposes, this is the reason the asset in Jersey falls under the UK.

ASI Global Real Estate Fund
Quarterly Update - Q4 2019

Portfolio update

As reported last quarter terms were agreed to extend Castorama's lease by a further 5 years. The lease extension was documented and became legally binding during the quarter positively impacting the asset's valuation. A key objective for H1 2020 at this asset is to extend the lease of Helios, who are a cinema operator and have a lease expiry at the end of 2020. This is the only cinema in Gneizno and therefore the retention of this tenant is considered an important differentiator.

At the Barcelona office the lease extension (10 years with a break at year 5) was completed with Revlon. The rent is stepped over the duration of the lease but on average represents a 15% increase on the passing rent and is 6% above the valuers ERV. This de-risks the lease expiry of the Fund's 3rd largest tenant and positively impacted the valuation. We are now negotiating with the other tenant in the building, Biomet, to extend their lease term. The financial terms are likely to closely mirror those achieved with Revlon.

At Ostrava we are in the final stages of negotiating new leases with on Electroworld"s old unit (they vacated in November). We will be splitting and re-letting the unit to Sinsay (a subsidiary of the Polish LLP Group), Bandi (men's fashion retailer) and expansion space for existing tenant SuperZoo.

At Customs House Plaza we have agreed terms with Afilias Ltd to lease the space recently vacated by Abtran. The letting is at a new benchmark rent and is expected to be accretive to valuation. Separately we are discussing extending Citco's occupation by a further 5 to 10 years, their current lease expiry is in 2023.

Finally the Fund has agreed to purchase a mixed use office and retail asset in Singapore. This is expected to exchange towards the end of January and conclude in the first few days of February. This purchase will take the Fund's cash weighting to around 6%.

At the end of Q4 the Fund's listed weighting was 22%. During the quarter a number of changes were made within the listed portfolio, the most significant of which included adding exposure to Allied Properties (favoured Canadian office name, held across the other listed real estate funds). We initiated a position in Gaming & Leisure Properties (favoured Casino name held across other listed real estate funds) and sold out of Link REIT due to concerns over the outlook for the Hong Kong retail sector.

Properties in Focus

Purchase - Niu Hotel, Munich

- Lot size of circa €27m, IY 4.5%
- Located close to the Munich exhibition centre (a world leading international trade fair facility)
- 3-star hotel, 170 bed hotel providing an attractive offering to business clients for short-mid term stays.
- Leased for 20 years to a German hotel operator Novum, a brand with 180 locations across Europe
- Munich is a buoyant hotel market with the highest occupancy rates & revenues per room rates in Germany
- The asset provides CPI linked long dated income

Purchase - 11 Armour Street, Milperra, Sydney

- Lot size of £17m, Initial yield of 5.0%, net initial yield of 4.7%
- Asset is situated in a good location, 24kms south west of the Sydney CBD in close proximity to Sydney's major orbital road network
- Constructed in the 1980s however the spec remains suitable for a number of uses (distribution, e-commerce, final mile delivery) and can be easily subdivided
- We expect this asset to deliver a 6 to 7% IRR over a 5 year time horizon, furthermore given its land constrained location we expect general rental growth outperformance
- Let to a manufacturing tenant for a further 7.5 years, annual rent escalations of 3%
- Strong south Sydney submarket that will benefit from Government infrastructure projects
- Increases the Fund's industrial weighting to 22%

ASI Global Real Estate Fund

Quarterly Update - Q4 2019

AberdeenStandard Investments

Performance review

- During the fourth quarter the Fund returned -0.19% taking 2019 returns to 10.19%. During the period the Fund's listed holdings returned -3.12% versus a return of -5.15% for the FTSE EPRA Nareit Developed benchmark. The strengthening of GBP versus USD was a key detractor given the unhedged nature of these assets. The listed portfolio is outperforming its benchmark over all timeframes to 3 years.
- Within the direct portfolio there were valuation increases at the logistics asset at Veghel, the office building at Barcelona and the shopping centre at Gneizno, Poland. However these increases were offset by the impact of the strengthening pound on the listed portfolio. The purchase costs associated with the Munich and Sydney purchases have also been factored into the Q4 unit price performance.

Fund Outlook

- The Fund has made significant progress with de-risking forthcoming a number of lease expiries with a further programme of asset management to work through in the early months of 2020.
- The three direct purchases will take the cash weighting to around 6% however if the strong inflows that we have experienced during the first weeks of 2020 continue then this level is likely to rise necessitating further purchases. To this end we continue to work with Wise Capital to source opportunities in the Sao Paulo office sector.
- We envisage keeping the listed exposure, which has been a strong source of performance, around 22% to 23% of Fund value. The Collective Investment Scheme exposure is currently 2.4% of Fund value and we would hope that the majority of this will be distributed during 2020 but as noted before we are beholden on the Manager's ability to dispose of the underlying assets.
- Encouragingly, the global economic backdrop that provides the underlying support for the real estate occupier and investment markets looks to have stabilised this quarter. Global uncertainty has reduced with the pause in the US-China trade war and central bank easing measures have loosened financial conditions. However, global growth remains lacklustre and our expectations are for growth to be below the consensus of economic expectations. Furthermore, the real estate cycle is at a late stage and pricing remains stretched compared with earlier in the cycle. Despite this, the fundamentals for the asset class are encouraging with future supply significantly below the level it reached at similar points in previous cycles. Occupier markets remain well supported and vacancy rates are below average in a range of different markets. Additionally, there is an expectation in the current environment that interest rates are likely to remain at historically low levels for a significant period of time yet. The margin that real estate provides over the risk-free rate is at elevated levels. Investors do need to be cautious with this metric as the risk premium associated with real estate should arguably be higher now as lease lengths get shorter and as the propensity to break leases is higher than it was in the past.
- In the current and forecast low-yielding environment, we expect demand for real estate to continue to be robust and we think that pricing will remain resilient. In terms of our sector and structural preferences, we continue to like specific sectors and segments in our favoured markets that are continuing to benefit from long-term structural trends. These include industrial assets that are benefiting from changes in shopping habits. The private rented sector is also expanding on the back of the growing propensity to rent and a lack of future supply to meet projected population growth. We also like long-duration income, which has seen significant demand, offering investors a safe haven amid wider market volatility. With the cycle being elongated and in the context of the heightened geo-political and economic uncertainty at present, we remain risk averse and continue to pursue 'sustainable' income in our target markets and we maintain a forensic approach to seeking value in our favoured markets.

ASI Global Real Estate Fund

Quarterly Update - Q4 2019

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 fund invests in equities and equity related securities. These are sensitive to variations in the stock markets which can be volatile and change substantially in short periods of time.
- (e) Dividend payment policies of the REITs in which the fund invests are not representative of the dividend payment policy of the fund.
- (f) The fund may invest in emerging market equities and/or bonds. Investing in emerging markets involves a greater risk of loss than investing in more developed markets due to, among other factors, greater political, tax, economic, foreign exchange, liquidity and regulatory risks.
- (g) 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.

Annual returns to 31 December 2019 (%)

	2019	2018	2017	2016	2015
ASI Global Real Estate Fund	10.2	2.3	3.8	16.2	1.2

Source: Aberdeen Standard Investments, 31 December 2019

Fund performance is quoted net of institutional fees (GBP).

ASI Global Real Estate Fund

Quarterly Update - Q4 2019

Important information

This document is intended for use by individuals who are familiar with investment terminology. To help you understand this fund and for a full explanation of specific risks and the overall risk profile of this fund and the shareclasses within it, please refer to the Key Investor Information Documents and Prospectus which are available on our website - www.aberdeenstandard.com.

Aberdeen Standard Investments has not considered the suitability of investment against your individual needs and risk tolerance. If you are in any doubt as to whether this fund is suitable for you, you should seek advice. An advisor is likely to charge for advice. We are unable to provide investment advice.

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GB-170220-110232-1