FIRST ASSET CANADIAN REIT ETF
MANAGER COMMENTARY
September 2017
TSX: RIT

The S&P/TSX Capped REIT TR Index was flat on the month, lagging the S&P/TSX Composite TR Index, which was up +3.1% in September. Similarly, U.S. REITs tread water, lagging the broader index return, as the MSCI U.S. REIT Index gave back -0.1 for the month versus +2.1% for the S&P 500 TR Index (both in U.S. dollar terms). For the month, the First Asset Canadian REIT ETF (the "Fund") returned +0.25% net of fees. The Fund remains competitive year-to-date, up +7.4% net of fees, well ahead of the +3.8% S&P/TSX Capped REIT TR Index return.

The Canada 10-year bond yield jumped 25 basis points from 1.85% at the end of August to 2.10% at the end of September. As a group, Canadian REITs are now trading at a 371 basis point spread to the 10-year Canada bond yield, 29 bps above the long-term average of 342 bps and 58 bps above the normalized (ex-financial crisis) long-term average of 313 bps. Supported by a sound economic and fundamental backdrop, Canadian REITs have demonstrated resilience through periods of rising bond yields.

In late September, Avison Young published its Fall 2017 Commercial Real Estate Investment Review. Buoyed by a relatively strong economy, Canadian real estate has continued to enjoy healthy fundamentals across most markets and asset classes. Following a record $28.4 billion in commercial property transactions in 2016, Canada's six major markets saw sales of almost $19 billion in the first half of 2017 – up $4.3 billion or 29 per cent compared with the first half of 2016. With the exception of Ottawa, all major markets, including Calgary and Edmonton, saw higher investment activity year-over-year. Office and retail were the top investment sectors in the first half of 2017, accounting for a combined ~$10 billion of commercial real estate trades year-to-date. Notably, average cap rates have continued to compress across all markets and asset classes, with the exception of Class A office, which was flat compared with the prior year. Cap rate compression was most significant in Vancouver and Toronto, driven by strong investment activity in both markets.

On September 25-26th, we attended BMO's Real Estate Conference in Chicago. The conference was well attended. Industry players, speakers and panellists were constructive on real estate fundamentals in the U.S. and Canada, with some noting a growing disconnect between NAV and unit prices. Two panel discussions were of particular interest to us: 1) Amazon's impact on real estate and 2) rising activism in the REIT sector. While Amazon, and e-commerce more broadly, is undoubtedly shaping the way consumers shop, one panelist pointed out e-commerce distribution is less efficient than bricks-and-mortar retail and requires 3x the square footage. Every $1 billion in online sales is estimated to equate to 1.4 million square feet in industrial demand. Another panelist noted while retail front-of-store space needs may be shrinking, back-of-store (i.e. storage) space needs are increasing to allow retailers to accommodate click-and-collect and other like initiatives. With respect to activism, as public market valuations diverge from NAV, we have seen increased interest in the sector from activists. We echo panelist views in that activism doesn't have to be hostile to be effective.

For the month, the Fund's top performing equity holdings and approximate contributions to total return were: American Hotel Income Properties, contributing 17 bps; Agellan Commercial REIT, contributing 12 bps; and Morguard North American Residential REIT, contributing 12 bps. Equity holding that detracted from the Fund's performance in September included Tricon Capital Group (-22 bps), Pure Industrial REIT (-13 bps), and First Capital Realty (-9 bps).

Headlines of interest in September included:

- On September 14th, activist group Sandpiper announced that it had acquired a 10% stake in Agellan Commercial REIT (TSX: ACR.UN) and had engaged the board regarding strategy and future plans of the REIT as well as reconstitution of the Board. If you had asked us to identify a shortlist of Canadian REITs ripe for activism prior to Sandpiper's announcement, Agellan would not have been top-of-mind. On September 18th, Agellan announced that its board had considered and rejected Sandpiper's demands. Agellan's board viewed Sandpiper's value-surfacing proposals as redundant given that the initiatives identified by Sandpiper are currently being implemented by the REIT. Agellan's board also dismissed the proposed substantial reorganization of the board, which would result in majority control by Sandpiper's handpicked nominees, due to the fact that the REIT's existing trustees were recently elected by unitholders (June 12th) and included three new independent members. In its rebuttal, Agellan also announced that it had entered into an agreement with its external asset manager, Agellan Capital Partners ("ACPI") to internalize the REIT's asset management function. The internalization is expected to occur in Q4 2017 for total consideration of C$15M, including $3M cash and the balance in Class B Units (~3% voting interest in the REIT subject to contractual 3-year holding period). We continue to hold a position in Agellan and are actively monitoring the situation.

- On September 25th, Tricon Capital Group (TSX: TCN) announced that it had received a subpoena from the Securities and Exchange Commission (SEC), requesting documentation and communications related to Tricon American Homes' securitization transactions, including materials related to broker price opinions ("BPOs") provided on properties included in those transactions. For those who aren't familiar with BPOs, they are a cheaper and less stringent way to estimate a home's value versus a full appraisal. This news did not come as a surprise to us. Here's why:

  Earlier this year, Radian Group (NYSE: RDN), the indirect parent of Green River Capital, a service provided of broker price opinions to Starwood Waypoint Homes (NYSE: SFR), American Homes 4 Rent (NYSE: AMH), Invitation Homes (NYSE: INVH), among others, disclosed in its March 31st , 2017 quarterly report on Form 10-Q that Green River had received a letter from the SEC stating that the SEC was conducting an investigation relating to certain single-family rental securitizations and was requesting information from market participants. The SEC letter asked Green River to provide information on broker price opinions that it had provided on properties included in single-family rental securitization transactions. On September 13th, AMH, INVH, and SFR also received subpoenas from the SEC requesting documents and communications related to single-family rental securitizations. The investigation is expected to take some time and will add noise to the group. Tricon has completed 3 securitization transactions since 2015 for a total value of US$1.2B secured by ~10,400 single-family rental properties. A recent discussion with Tricon's management team downplayed fears, noting that BPOs are a politically-charged issue, and that the SEC is believed to be investigating how providers of broker price opinions compete for business and whether users of broker price opinions shop for BPO providers willing to assign the highest value to their properties. Referencing a September 22nd Bank of America Merrill Lynch report, management highlighted that BPO implied home price appreciation and Case Shiller U.S. home appreciation were comparable.

The Fund's top ten holdings at September 30th included First Capital Realty, Morguard North American Residential REIT, Killam Apartment REIT, RioCan REIT, Canadian Apartment Properties REIT, H&R REIT, Tricon Capital Group, Canadian REIT, Pure Multi-Family REIT and Pure Industrial REIT. Combined, these holdings represent ~41% of the Fund. Consistent with prior periods, the Fund remains biased towards REITs with quality assets, value add development and intensification potential, exposure to higher growth markets, low payout and leverage ratios, and less dependence on the capital markets to execute their strategy.

Fund Performance (%)

	1 Month	3 Month	6 Month	YTD	1 Year	3 Year	5 Year	10 Year	SI
First Asset Canadian REIT ETF	0.24	-0.64	1.38	7.40	8.09	11.65	9.39	8.03	10.02
S&P/TSX Capped REIT TR Index	0.01	0.19	0.15	3.82	4.45	5.67	4.14	6.38	8.65
MSCI U.S. REIT Index	-0.27	0.63	1.98	2.68	-0.69	8.28	8.23	4.40	5.93
S&P/TSX Composite TR Index	3.06	3.68	1.99	4.45	9.18	4.54	8.06	4.06	6.72
S&P 500 TR Index	2.06	4.48	7.71	14.24	18.61	10.81	14.23	7.44	8.36

Source: Morningstar as at September 30, 2017

Inception date: Nov 15, 2004[1]

Lee Goldman, CFA
Senior Vice-President & Portfolio Manager
First Asset Investment Management Inc.

Mr. Goldman actively manages the:

First Asset Canadian Convertibles Fund
First Asset Diversified Convertible Debenture Fund
First Asset North American Convertibles Fund
First Asset Canadian Convertible Bond Fund
First Asset Canadian Energy Convertible Debenture Fund
First Asset Canadian REIT ETF
First Asset REIT Income Fund
First Asset Canadian Convertible Bond ETF

Kate MacDonald, CFA, MFin
Portfolio Manager
First Asset Investment Management Inc.

Ms. MacDonald co-manages the:

First Asset Canadian REIT ETF
First Asset REIT Income Fund

S&P/TSX Capped REIT Total Return Index is a capitalization-weighted index designed to measure market activity of the real estate sector issuers listed on the Toronto Stock Exchange. The Index is used as a benchmark to help you understand the Fund's performance relative to the general performance of the Canadian real estate sector.
The S&P/TSX Composite Total Return Index is a capitalization-weighted index designed to measure market activity of stocks listed on the Toronto Stock Exchange. The Index is used as a benchmark to help you understand the Fund's performance relative to the general performance of the broader Canadian equity market.
The S&P 500 Total Return Index tracks 500 large-cap U.S. stocks representing all major industries. The Index is used as a benchmark to help you understand the Fund's performance relative to the general performance of the broader U.S. equity market.
MSCI USA IMI Real Estate Index is designed to capture the large, mid and small cap segments of the US real estate equity universe.

[1]The indicated rates of return are the historical annual compounded total returns, including changes in unit value and do not take into account sales, redemption or optional charges or income taxes payable by a security holder that would have reduced returns.Performance is calculated net of fees. The Fund was originally launched as a TSX-listed closed-end fund on November 15, 2004, and converted into an exchange traded fund on July 14, 2015. Performance shown is since inception of the closed-end fund. In connection with the conversion, and pursuant to unitholder approval, the annual management fee payable by the Fund to First Asset, as manager, was reduced to 0.75% (from 1.05%) of the NAV per unit and certain changes were made to the investment objectives, strategies and restrictions applicable to the Fund. Material among these changes is the ability for the Fund to invest up to 30% of its portfolio in securities of real estate issuers listed on non-Canadian stock exchanges and the Fund will no longer be permitted to use leverage. Had these changes been in effect prior to this date the performance of the Fund could have been different. On August 17, 2007, pursuant to unitholder approval, the Fund`s mandate was changed from that of a passively managed fund to that of an actively managed fund including the elimination of the market cap size restriction and the annual management fee payable by the Fund to First Asset, as manager, was increased to 0.75% (from 0.45%) of the NAV per unit. Had these changes been in effect prior to this date the performance of the Fund could have been different.

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