

## Know Your Occupier

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Seventy percent of returns from real estate come from income; therefore, it's absolutely important to know your occupier. We've developed a suite of tools that we've called KYO that ensure that we understand the risks around our occupiers and can deliver that long, stable income return for our investors.

What we've seen during the pandemic is that we cannot rely on occupiers paying their rent. We've seen rent recovery going from normally 99% and just being a regular part of real estate asset management to falling down to 50-60% in some cases during the pandemic. Therefore, understanding which occupiers can pay their rent, which occupiers can't pay their rent and which occupiers we should work with is really important. And if you don't know your occupier, you can't be sure that you're making the right decisions around the long-term security of your fund.

Fidelity real estate has always had a strong focus on occupier risk and understanding who the occupier is. We've developed a due diligence process which looks more like a fixed income approach to income risk than the traditional real estate approach. We undertake the typical cash flow model which looks to base case an upside and a downside scenario. We layer our own quants tools which enable us to look at the whole risk-adjusted cash flow, understanding all the risks around the tenancy, be it leasing risk, tenant bankruptcy, or market risk.

During the pandemic, we have been developing our income risk tools even more, working with our fixed income and equity colleagues to understand sector risks and building what we call our FIRS model – Fidelity Income Risk Score. This enables us to look at each tenant at the current point and understand how much risk we face from that tenant in that sector both in terms of financials and also in terms of some of the broader sectoral issues that that tenant might be facing.

The great example of this approach in action is our acquisition of Mirai House in Leiden in the Netherlands. This was a sale and lease back to a Japanese Pharmaceuticals company called Astellas, who were willing to sign a long lease in exchange for us acquiring the building. But to be sure that this was a good income play for us, we needed to have high conviction that Astellas was a good company to be investing in. So, we started by talking to the fixed income analyst about the sort of things that they think about when they look at fixed income in pharmaceutical sectors.

We then went on to talk to the equity analyst who specifically covers Astellas in Japan. From that we gained a high degree of confidence that Astellas was a good company to be investing in because of their drug pipeline, because they're largely developing these drugs on their own and therefore, they are regarded as one of the leading pharmaceuticals not just in Japan but globally.

Therefore, we believed it was worth bidding aggressively for this asset to acquire this long income from a very strong pharmaceuticals company. We ran this company through our FIRS model, and again they scored very favourably both from a sector perspective but also from their own financials perspective as well. So, we had a high degree of confidence going into the deal and we're very pleased that this deal adds a lot of income security to our portfolio.

Fidelity's approach to real estate investing has stable income at the heart of it and we use our quants tool to ensure that we really can deliver that stable income to our investors and deliver best-in-class performance.

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