SCOTTISH WIDOWS
preparation is everything

Investing in REITs

There is now an array of property investments available within the UK. From January 2007, the introduction of REITs (Real Estate Investment Trusts) will add to this choice.

Investing in property

- Property continues to be a popular choice for investors – the generally lower risk of this asset class compared to equities, together with the potential for high-returns, is attractive to many.
- While equities have been volatile and fixed interest securities have become increasingly expensive in recent years, one asset class has stood out. Commercial property proved to be a popular asset class during the 'bear' market of 2000 – 2003, and has retained its popularity since.

  Why is commercial property investment attractive?

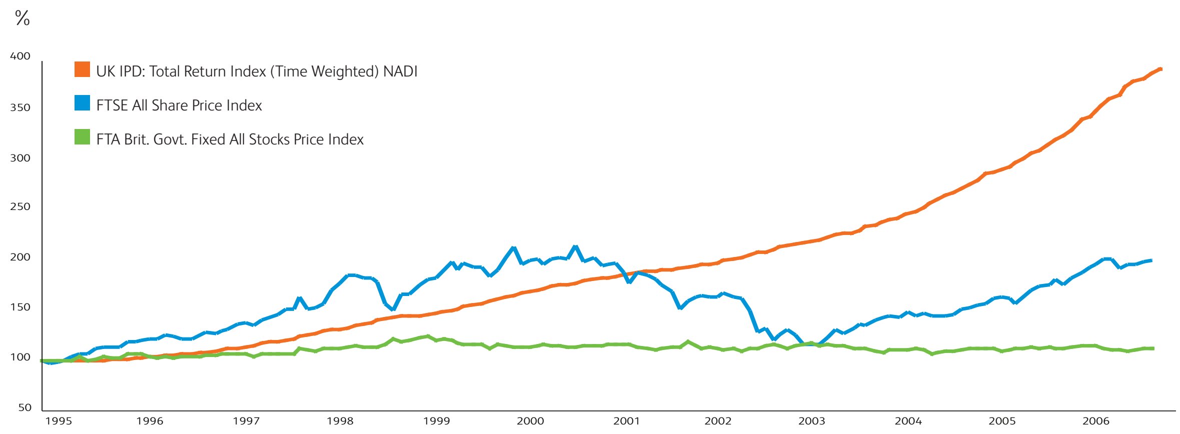
  - It has a low correlation with other asset classes
  - It offers diversification within its asset class
  - It has, over the last few years, offered lower volatility, yet higher returns, than equities.
- However, commercial property has not traditionally been accessible to all investors, particularly smaller investors. In addition to the inherent costs of property investment, a lack of liquidity, and potentially inefficient tax structures, have proven to be a barrier for many potential investors.

Funds that invest in property and land can be difficult to sell which means your client may not be able to cash in their investment when they want to, and we may have to delay acting on their instructions to sell the investment. Also, the value of property is based on the opinion of a valuer rather than fact.

The value of an investment in a REIT is not guaranteed and can go down as well as up depending on investment performance (and currency exchange rates where a fund invests overseas). An investor may not get back the amount they invest.

Commercial property outperforms equities and bonds

The graph below illustrates how UK commercial property investments have performed in relation to UK equities and Government bonds over the last ten years.



Past performance is not a guide to the future.

Source: SWIP/Datastream, Oct 2006

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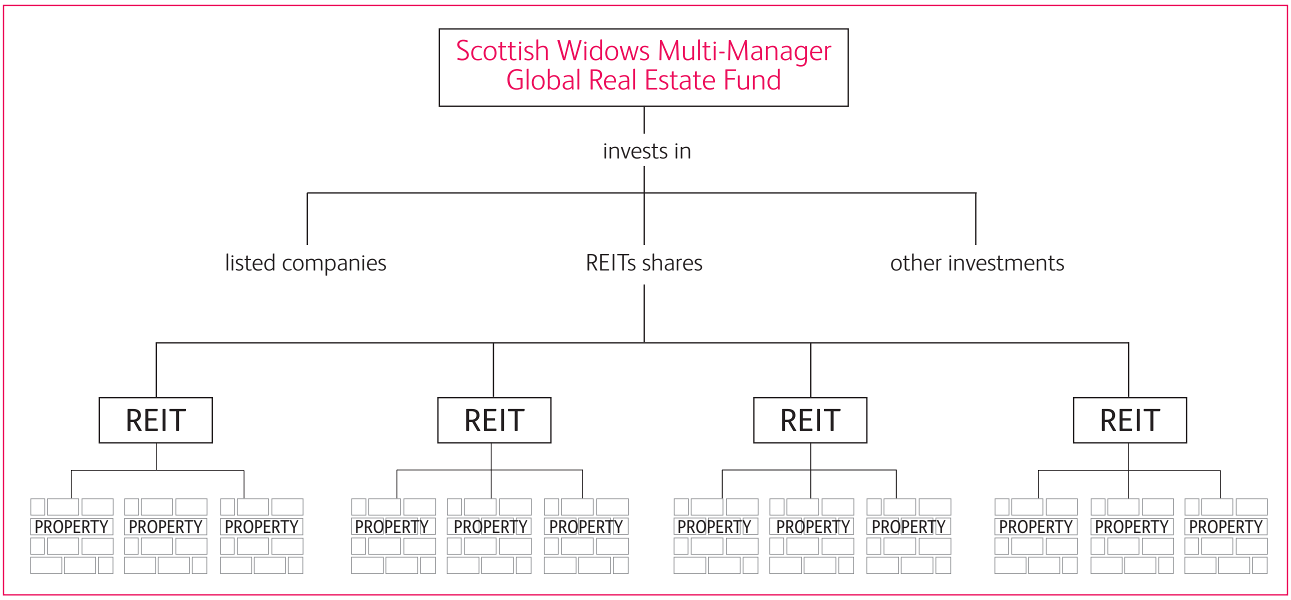
Investing in Real Estate Investment Trusts (REITs)

- With the introduction of UK REITs in January 2007, investors will have access to a tax transparent, listed real estate investment vehicle.
- By investing in a fund which investors themselves can invest in REITs and other property investments, they have the flexibility to move in and out of the asset class on a tactical basis due to lower liquidity and trading costs.
- However, while such funds can provide liquidity, they are also more influenced by short term movements in the stockmarket than direct property investments, and therefore see higher volatility.
- In markets where REITs are well established, like the US and Australia, they have become a separate asset class offering good portfolio diversification benefits.
- UK REITs will be exempt from tax on income received and on capital gains made on the properties in which they invest.
- UK REITs will normally be legally obliged to pay out at least 90% of rental income received to shareholders.
- Dividend yields are backed up by rental income, which should contribute to stability.
- There are restrictions on borrowing by REITs, and total returns will be driven more by dividends and less by share price movements in the long term, which should also help to make returns more stable.
- Remember, tax legislation can change.

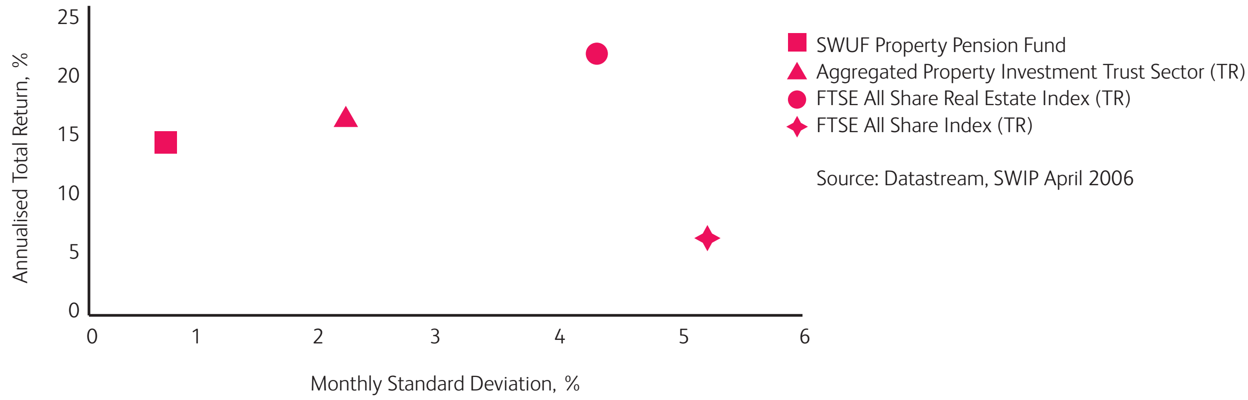
Example of a fund that invests in REITs – Scottish Widows Multi-Manager Global Real Estate Fund



Risk and Return Characteristics

UK REITs will be structured similarly to other UK property investment trusts. Historically, such investments have offered a combination of return and risk (measured by the standard deviation of return) more similar to 'bricks and mortar' than equities as a whole, as demonstrated by the chart opposite.

Monthly Standard Deviation and Total Returns, March 2002 – February 2006



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Investing in REITs can offer the same diversification benefits to a portfolio as direct property investments

- Analysis in the USA by Ibboston Associates of the period between 1972 to 2004 shows that US REITs improved returns and reduced risk to investors
- The same research identified that, historically, dividends accounted for ⅔rds of the total return from REITs
- Historically, REITs have had low correlation with other asset classes. Between 1992 and 2004 the correlation was:
    - S&P 500 0.27
    - Long Bond 0.05

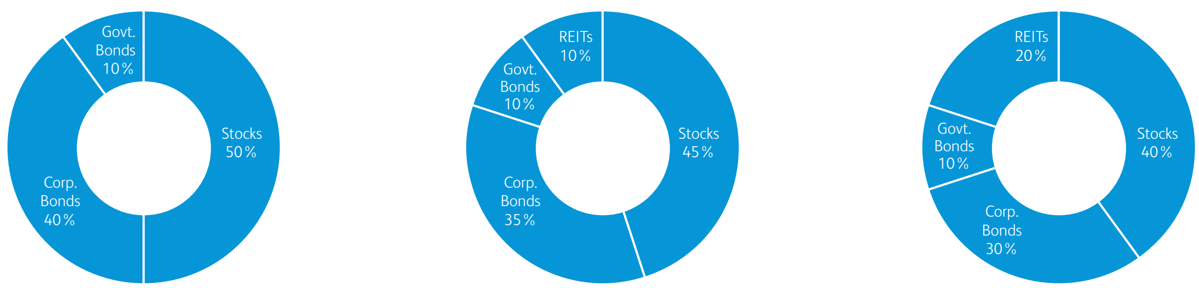
Source: Ibboston Associates

REITs have helped US investors to diversify to reduce risk and increase potential returns

Diversify to Reduce Risk and Increase Return

Stock and Bond Investors: 1972 – 2004

With No REITs · With 10 % REITs · With 20 % REITs



	With No REITs	With 10 % REITs	With 20 % REITs
Return	10.9 %	11.2 %	11.6 %
Risk	10.6 %	10.3 %	10.1 %
Sharpe Ratio	0.44	0.49	0.53

Source: Stocks – Standard & Poor's 500 which is an unmanaged group of securities and considered to be representative of the stock market in general; Bonds – 20 year US Government Bond; Treasury Bills – 30-day US Treasury Bill; REITs – National Association for Real Estate Investment Trusts® (NAREIT) Equity REIT Index.

As the level invested in REITs increased, the potential returns also increased, while the level of risk decreased.

Past performance is not a guide to the future.

REITs – Part of a balanced portfolio

Once a decision has been made to invest in property, investors will have to consider whether to invest in direct property investments, or indirectly via funds which invest in REITs and other property.

In this document, we've tried to highlight some of the distinctive investment features of REITs. Any investment decision, however, is likely to depend on the level of risk the investor is willing to accept, the degree of diversification required, and the amount the investor has available to invest. Ultimately, an investor may decide to invest in a combination of direct and indirect property investments.

How to invest in property through Scottish Widows

Your clients can access REITs through the Scottish Widows Flexible Options Bond which has one of the broadest range of property funds available in the market. There is a total of six property funds available, four* of which invest in REITs. Three of these are managed by Scottish Widows Investment Partnership (SWIP) which also manages direct property assets worth £6.2 billion** across the UK, Europe and North America.

The full range of property funds available through the Flexible Options Bond are:

- Scottish Widows UK Real Estate Fund*
- Scottish Widows European Real Estate Fund*
- Scottish Widows Multi-Manager Global Real Estate Fund*
- Scottish Widows Property Fund (currently restricted to investment of a maximum of 15% in the Flexible Options Bond)
- SW Schroder Global Property Securities Fund*
- SW New Star Property Fund.

For further details, please contact your usual Scottish Widows Account Manager or visit our adviser extranet at www.scottishwidows.co.uk/extranet

**Source: SWIP, as at 30 September 2006

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