MedicX Fund

Full year results

Strong investment pipeline to continue progress

Real estate

FY17 saw steady underlying growth in the investment portfolio and recurring earnings. Overall returns were further enhanced by positive revaluation movements reflecting continued tightening in market yields. Investment in development schemes had a limited impact on earnings in FY17 but completions and continuing acquisitions from a strong pipeline offer good growth prospects. The dividend has been increased and MedicX Fund (MXF) expects to pay 6.04p in respect of FY18, a yield of 7.1%, supported by growing highly secure, long-term income derived mainly from government sources.

Year end	Net rental income (£m)	Adj. earnings* (£m)	Adj. EPS* (p)	DPS (p)	EPRA NAV/ share (p)	P/NAV (x)	Yield (%)
09/16	34.3	14.2	3.8	5.95	73.2	1.15	7.0
09/17	35.9	14.9	3.6	6.00	76.5	1.11	7.1
09/18e	40.4	17.2	4.0	6.04	76.9	1.10	7.1
09/19e	45.9	18.8	4.4	6.08	77.9	1.08	7.2

Note: *Adjusted earnings and EPS exclude deferred taxation, revaluation gains, performance fees and exceptional items.

Continued growth in recurring earnings in FY17

The portfolio rose to £680m with £49.4m committed to new investment during the year. Net rental income and adjusted earnings (recurring "income earnings") both rose c 5%, but did not fully benefit from investment in properties under construction, particularly in the Republic of Ireland (RoI). As a result, with the share count increased by c 14% to part fund investment and meet scrip dividend demand, adjusted EPS at 3.6p was lower than in FY16 (3.8p).Including £18.7m of revaluation gains, a £5.3m deferred tax add-back resulting from REIT conversion, and £240k in REIT conversion costs, IFRS net earnings grew 45% to £38.6m. EPRA NAV per share rose 5% to 76.5p and including dividends paid, NAV total return was 12.7%.

Geared impact from further asset growth

Steady income growth from existing assets should be enhanced by acquisition growth, with the primary healthcare property markets in both the UK and RoI providing a strong medium to long-term growth outlook. MedicX ended FY17 with a strong pipeline of investment opportunities in both the UK and RoI, amounting to £175m. With investment adviser fees frozen until the portfolio rises above £782m, growth should have a geared impact on earnings and dividend cover. Our FY18 forecasts are little changed and we have introduced an FY19 forecast.

Valuation: Continuing high distributions

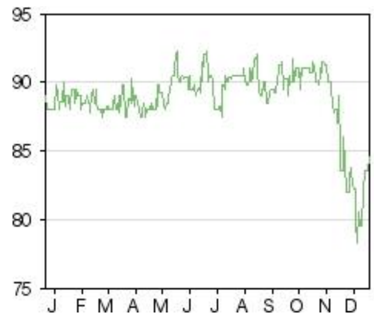
MedicX offers one of the highest yields in the sector with a 10-year record of growth. Distributions have regularly exceeded income earnings (cover in FY17 was 59.2%) but this has been more than made up by capital earnings. EPRA NAV has increased over five years with an annual compound NAV total return of 13.5%. We expect a continuation of the progressive dividend policy with growing, secure income from existing assets and portfolio growth gradually improving cover.

19 December 2017

Price	**84.5p**
Market cap	**£362m**

Net debt (£m) as at 30 September 2017	340.7
Net LTV as at 30 September 2017	49.5%
Shares in issue	428.6m
Free float	100%
Code	MXF
Primary exchange	LSE
Secondary exchange	N/A

Share price performance



%	1m	3m	12m
Abs	1.2	(6.1)	(4.0)
Rel (local)	(0.9)	(9.6)	(11.7)
52-week high/low		92.2p	78.2p

Business description

MedicX Fund is a specialist investor in primary care infrastructure in the UK and Republic of Ireland. It holds a portfolio of 152 properties, of which four are in the Republic of Ireland. The properties are let mainly to government-funded tenants (c 90%) and pharmacies (c 8%) on long leases.

Next events

Quarterly dividend payment	29 December 2017

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Edison profile page

MedicX Fund is a research client of Edison Investment Research Limited

Investment summary

The modern, purpose-built primary healthcare assets, in both the UK and the Republic of Ireland (RoI), that MedicX invests in form part of the core healthcare infrastructure in these countries, for which there is an increasing need. They offer strong covenants and provide long-term secure and rising cash flows to support high and growing dividend distributions. With investment advisor fees frozen until the portfolio reaches £782m, further portfolio growth should have a geared impact on earnings and dividend potential. Strong investor competition for these assets has pushed up the cost of acquisitions, requiring investment discipline. But the prospects of increased new build commissioning are improving, providing investment opportunities and potential support for open-market rent increases on existing stock. The Fund offers a highly attractive dividend yield and although it distributes more than its income earnings, capital growth has more than accounted for the difference, and EPRA NAV per share has continued to increase. We expect dividends to increase further over the next couple of years, albeit modestly, and for dividend cover to increase with asset and rent growth and operational gearing.

Valuation: High payout of total returns

The Fund's prospective dividend yield of c 7.1% is the highest among its immediate peers. Distribution represents c 8% of the EPRA NAV per share (76.5p), and although not covered by income earnings, is covered by the 12.7% NAV total return generated in FY17 and the 13.5% pa compound growth in NAV total return in the five years to end-FY17. Given the secure nature of the Fund's income stream, we expect the board will maintain a modestly progressive dividend policy while continuing to grow assets, earnings, and dividend cover. With investment advisor fees currently frozen, asset growth should have a geared impact on earnings. In line with other listed property investors specialising in long leases, MedicX trades at a premium to EPRA NAV, although this premium has recently narrowed.

Financials: Steady progress in FY17

With the Fund maintaining a disciplined approach to investment in a competitive market, FY17 commitments were a little lower than we had assumed, and investment in development assets did not fully contribute in the period. However, the impact on net rental income versus our forecast was largely offset by lower interest expense and lower than forecast direct property costs. Adjusted earnings and EPS were as forecast, with the former ahead by c 5% and adjusted EPS slightly lower as a result of equity issuance. Reflecting the impact of government policies in both the UK and RoI aimed at enhancing primary care infrastructure, the pipeline of investment opportunities is strong (c £175m). We have made little change to FY18 forecasts and introduced FY19 forecasts.

Sensitivities: Investment volume and yield spread

MedicX's portfolio has a low-risk profile and relatively predictable income. Around 90% of rents are government backed with much of the rest represented by pharmacy tenants. Debt funding is fixed rate with an average maturity of 12.7 years, similar to the average unexpired lease length of 14.1 years. Key sensitivities (see page 11) include:

- The ability to source and execute investments at an appropriate yield premium to funding costs.
- The ability to attract sufficient debt funding at appropriate cost.
- The ability to generate rental growth on the c 70% of leases that are subject to open-market review on a rolling three-year basis.

2017 results

Exhibit 1: Summary of FY17 financial performance

Year to 30 September (£000s)	2016	2017	
Net rental income	34,322	35,947	5%
Expenses	(7,309)	(6,085)	-13%
Operating profit before valuation movements	27,013	29,862	11%
Net revaluation gain/(loss) on investment property	15,523	18,654	
Profit/(loss) on disposal of investment property	31	(65)	
Operating profit	42,567	48,451	14%
Share of profit of JV	0	10	
Net finance expense	(14,380)	(15,149)	
Profit before tax	28,187	33,312	18%
Tax	(1,556)	5,312	
IFRS net profit	**26,631**	**38,624**	**45%**
Adjust for:			
Fair value movements	(15,523)	(18,654)	
Investment adviser performance fee	1,523	0	
Deferred tax	1,556	(5,312)	
REIT conversion fees and costs	0	240	
Adjusted net profit	**14,187**	**14,898**	**5%**
IFRS EPS (p)	7.1	9.3	31%
Adjusted EPS (p)	3.8	3.6	-5%
DPS declared (p)	5.95	6.00	1%
Dividend cover	63.8%	59.2%	
EPRA NAV per share (p)	73.2	76.5	4%
Net LTV	50.8%	49.5%	

Source: MedicX Fund data

The FY17 year saw continuing underlying growth in the investment portfolio, with its value further enhanced by positive revaluation movements that substantially reflect additional tightening in market-wide valuation yields. Recurring earnings, adjusted for revaluation movements and non-recurring items, grew in absolute terms but were lower in per share terms, failing to keep pace with the increased number of shares resulting from issuance to fund investments, with forward funding development projects yet to fully contribute. As discussed in the Financials section of this report, FY17 earnings were slightly lower than we had forecast (adjusted EPS by c 1%) as a result of slower growth in rent producing assets during the period; however, the investment advisor reports a strengthening pipeline of investment opportunities (c £175m at end-FY17). Including the impact of revaluation gains on NAV, NAV total return was 12.7% in the year (FY16: 11.8%). The main points from the results are below:

- Rents receivable continued to increase, rising by 5.7% to £37.1m (FY16: £35.1m). The year-end rent roll, assuming completion of assets under development, was £40m.
- IFRS profit after tax of £38.6m was 45% higher than the £26.6m reported for FY16, and included slightly higher revaluation gains (£18.7m versus £15.2m) as well as a positive deferred tax add-back of £5.3m resulting from entry to the UK REIT regime (FY16: negative £1.6m) and an absence of investment adviser performance fees (FY16: £1.6m).
- Adjusted earnings, calculated on an EPRA basis (adjusted for revaluation movement and deferred tax) and further adjusted for investment advisor performance fees, and REIT conversion costs of £240k, increased by 5% to £14.9m. Reflecting the increase in share count during the year, adjusted EPS was slightly lower at 3.5p (FY17: 3.8p).
- EPRA NAV per share increased by 5% to 76.5p and including dividends paid, the NAV total return was 12.7% (FY16: 11.8%). Including the 1.5p per share dividend declared on 1 November, quarterly dividends amounting to 6.0p per share will have been paid in respect of FY17 and the company expects to pay 6.04p per share in respect of the current (FY18) financial year.

- A total of £49.4m was committed to new investment in both the UK and RoI during the year with an average cash yield of 5.22%. The value of the property portfolio increased by 11% to £680.4m and the investment manager reports a strong pipeline of acquisition opportunities of c £175m.
- Drawn debt facilities amounted to £372.8m at year-end at an average all-in fixed rate cost of 4.3% with an average unexpired term of 12.7 years, not materially different to the weighted average unexpired lease term of 14.1 years. Continued demand for the shares during the year saw 39.75 new shares issued under the block listing facility at an average price of 87.9p, and average 18% premium to EPRA NAV. With £34.6m net proceeds from share issuance, net gearing of 49.5% was similar to the previous year (50.8%) and well within the fund's self-imposed limit of 65%.

In the following sections of this report we provide a full overview of MedicX, its strategy and portfolio, and the markets in which it operates. An update on our financial forecasts and an assessment of the current valuation of MedicX shares can be found later in the report, beginning on page 8.

Company description: Specialist long-term investor

MedicX Fund is a specialist primary healthcare property investor, focusing on modern, purpose-built primary healthcare assets in both the UK and RoI. It is traded on the London Stock Exchange (LSE) premium segment, converted to REIT status as of 1 October 2017, and targets a rising rental income and capital growth. Primary healthcare assets form part of the core healthcare infrastructure, for which there is an increasing need. They offer strong covenants and provide long-term secure and rising cash flows to support high and growing dividend distributions. Similar to many other investment funds, MedicX has no employees but is overseen by the company's board of directors, which appoints an external investment adviser to provide investment advice and to manage the property portfolio as well as the day to day activities of the company. Octopus Healthcare Adviser Ltd is the external investment adviser to the Fund and Octopus AIF Management Limited is the manager. Both companies are associates of the Octopus Healthcare Group ("Octopus Healthcare").

Octopus Healthcare

Octopus Healthcare is a specialist investor, developer, and manager of healthcare properties. It currently manages more than £1.2bn of healthcare investments across a number of platforms, with a focus on five core areas: GP surgeries, care homes, special education schools, retirement housing, and hospitals. It has a structured approach to acquisitions, preferring healthcare facilities that are, or can become, dominant in their catchment areas and utilising a proprietary database and analysis of GP practices, associated services and local demography to identify opportunities.

New investments come from a variety of sources:

- tenders in the open market;
- Octopus Healthcare's own development pipeline;
- General Practice Investment Corporation (GPI), a leading developer in the sector with which MedicX has a framework agreement; and
- other developers with which the fund has either a framework agreement or a strong working relationship; this is often the case in the ROI, where the fund made its first investment in 2015.

The investment adviser is remunerated according to the formulae below, which when implemented effectively froze the investment advisory fee until the portfolio reaches £782m. The formulae cover four types of fees:

- **Investment advisory:** 0.5% on healthcare property assets up to £750m, 0.4% on assets from £750m to £1bn, and 0.3% on assets over £1bn, subject to a minimum fee of £3.878m.
- **Property management:** 3% of gross rental income up to £25m and 1.5% above £25m.
- **Corporate transaction:** 1% of the gross asset value of any property-owning subsidiary company acquired.
- **Performance:** 15% of the amount by which total shareholder return exceeds a compound hurdle rate of 10% from the 69p issue price at 8 April 2009. A high-water mark is recorded in years in which a performance fee is earned and the deficit in any years in which the hurdle is not reached must be recouped in subsequent periods before a performance fee can be earned. The high-water mark is currently 92.25p and no performance fee was earned in FY17 (FY16: £1.553m).

Total fees payable to the adviser in FY17 amounted to £4.792m (FY16: £6.362m) and comprised the investment advisory fee of £3.867m and property management fees of £925k. Octopus Healthcare Adviser owns c 2.3m shares of the fund.

The board of directors

The board of MedicX Fund is solely comprised of non-executive directors. David Staples has led the board as chairman for more than nine years since October 2008 but has decided not to stand for re-election at the next AGM in February 2018. The board has chosen Helen Mahy, an experienced chairman and investment company director, as his replacement. In other board changes, Shelagh Mason retired from the board at the end of FY17 after 11 years of service and was replaced by Laure Duhot. The other board members are John Hearle and Steve Le Page. Brief biographies can be found on page 13.

Market update

With an ageing population, suffering increasing levels of chronic illness, demands on the healthcare services look set to increase for many years to come. In both the UK and the RoI, primary care is the foundation of the healthcare system and GPs act as the “gatekeepers” or first point of access to healthcare services. In addition to simply meeting this expected additional demand for healthcare services, both the NHS and the HSE seek to increase the range of services that GPs are able to provide in local community settings, outside of the hospital system, and integrated with other healthcare services. In addition to improving the patient experience there is a widespread acceptance that increasing the role and capabilities of the primary care sector will create much needed efficiency savings in healthcare provision.

In the UK, the strategy for change was set out in the NHS Five Year Forward View and Sustainability and Transformation plans, and cross-party support for these remains in place. Sir Robert Naylor’s review of NHS property and estates and how to make best use of the buildings and land was published in March 2017. The report highlights the important role that the private sector can play in driving forward the desired changes. The recent autumn budget has made available additional resources for NHS capital investment. Independently, GPs themselves, under pressure from regulation and workload, are increasingly open to working collaboratively in larger groups in order to be able to provide enhanced services from typically larger, modern, and purpose-built premises.

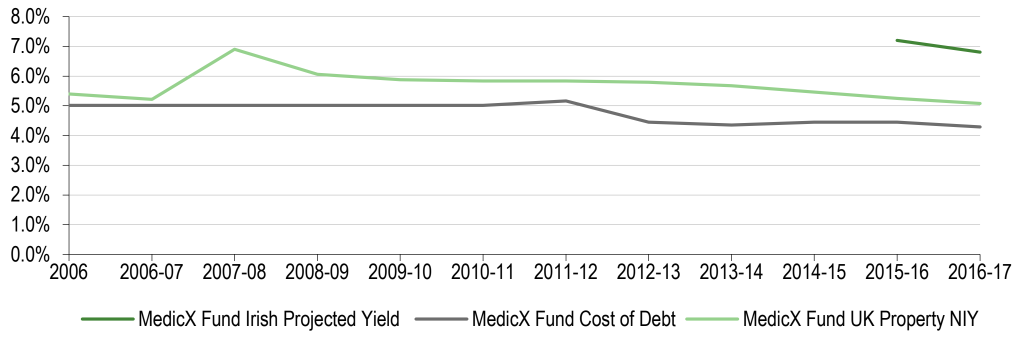
The RoI faces similar demographic pressure and the Irish government continues to support the Primary Care Strategy, aimed at delivering similar modern, high-quality premises within local communities.

Portfolio developments and overview

Investment pipeline strengthening

The market for primary healthcare properties remains highly competitive, with a wide range of investors attracted to the secure long-term yields that the asset class can provide. As a result, the spread between the yields at which the Fund can acquire properties and the cost of long-term debt and government gilts remains significant, but had narrowed noticeably. The spread between the 5.08% net initial yield of the UK portfolio at end-FY17 and the Fund's average 4.29% cost of debt was 0.79%. Although not much changed on end-FY16 (0.80%) it is well below the level of five years ago. The projected yield on the Fund's Irish assets is higher at 6.8%, but this is lower than the 7.2% at end-FY16.

Exhibit 2: Property yields versus borrowing costs



Source: MedicX Fund data

In this environment it is important for the long-term success of the portfolio that the properties acquired are able to provide more than just near-term income, but are of a high quality and able to adapt to the changing needs of the tenants. We believe that the acquisition of larger and newer properties is a good indication that investment quality is being maintained. The Fund has continued to source suitable acquisitions through its established relationships with investors, developers and agents in the sector, and acquired a total of six properties during the year with two smaller properties disposed of. At the 30 September year-end, the MedicX portfolio comprised 156 properties, up from 152 at end-FY16. Of these, 151 were operational and fully let and five were under development. The acquisitions represented a total commitment of £49.4m, an average £8.2m per property, almost double the £4.4m portfolio average lot size. A total of four development properties were completed, all within budget under fixed-price contracts, with an initial value of £22m. Included within these was the Fund's first forward funding scheme in the RoI, at Mullingar. A second RoI forward funding scheme (Crumlin) is due to complete in December 2017, with the two remaining RoI forward funded developments, at Tallaght and Rialto, due for completion in early 2018 and 2019, respectively. The outstanding commitment in respect of all five properties currently under development was £19.1m at end-FY17 with all of the properties, except Rialto, expected to complete within six months.

During the current FY18 year to date, the Fund has completed the sale of five smaller properties with relatively shorter leases at an aggregate gross sale price of £5.6m (an average £1.1m lot size), representing a gain of c £250k over the end-FY17 book value. It has also contracted to acquire, by way of a forward funding agreement, a new primary healthcare medical centre in South Wales. The centre is expected to cost c £4.6m and is the fourth acquisition made under a framework agreement with Healthcare Property Company Ltd, a leading developer of primary healthcare centres, which gives MedicX first refusal over the forward funding of its new schemes.

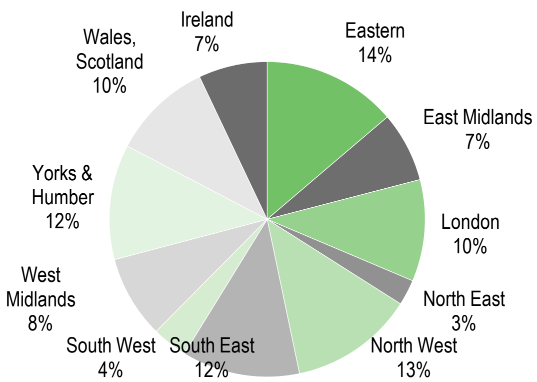
The Fund currently has access to a growing property pipeline of potential acquisitions. At 30 September the UK pipeline was £85m and the Irish pipeline was the equivalent of £90m. Since then, c £38m has moved into legal due diligence, in addition to the completed commitment in South Wales referred to above.

Portfolio overview

At 30 September 2017, the portfolio was valued at £680.4m, which excludes the construction costs required to complete the development assets and is net of purchaser's costs of 6.1%. The increase from £612m at end-FY16 includes net £49m invested in the portfolio (acquisitions, disposals, asset management initiatives at existing assets, and that portion of development commitments drawn in the period), and £19m of revaluation gains. The revaluation gains substantially reflect a further tightening of yields as well as a smaller contribution from rent growth. The net initial yield for the UK assets reduced to 5.08% from 5.25% at end-FY16. The RoI assets, mostly still under construction at end-FY17, accounted for c 5% of the total portfolio value.

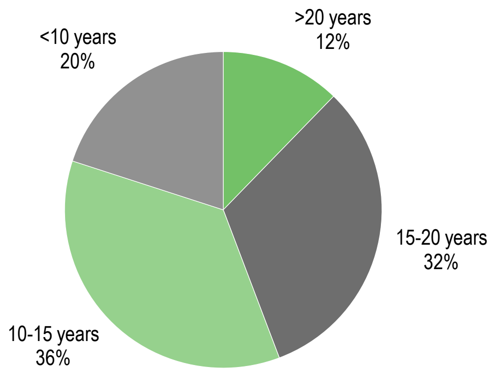
Mostly reflecting acquisitions, the passing rent on the portfolio increased to £40.0m at end-FY17 from £37.2m a year earlier. The portfolio is geographically diverse (Exhibit 3) and the largest asset comprises only 2.7% of the portfolio value (FY16: 2.9%), with the top 10 assets representing 17.5% of the total. The averaged unexpired lease length was 14.1 years, with the decline from 15.5 years at end-FY16 broadly representing the passage of time.

Exhibit 3: Portfolio distribution by rent region



Source: MedicX Fund

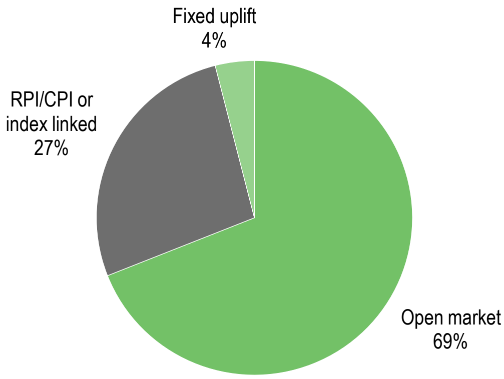
Exhibit 4: Portfolio by lease length to expiry



Source: MedicX Fund

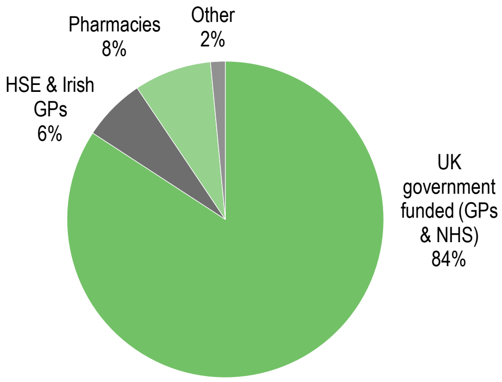
New leases are typically for a term of 20 or 25 years and in the UK are effectively subject to upwards only rent reviews at the option of the landlord. Exhibit 5 shows the split of the MedicX portfolio by rent review process and, as is typical of the industry, the majority (69%) are subject to open-market rent review, while the balance of leases are predominantly RPI or CPI linked (27%) and a small element (4%) are subject to fixed uplifts. Rents in the ROI are reviewed every five years rather than the three years that is typical in the UK, and unlike in the UK may fall as well as rise. In recent years, rents reviewed by open-market comparison have risen less than those assessed using other methods and this continued in FY17. An average overall uplift of 1.02% pa was achieved on reviews concluded during the year (FY16: 1.2% pa), with the average of 0.52% achieved on open-market rent reviews continuing to decline (FY16: 0.8%). The average was lifted by the contributions from RPI-based reviews (average 1.7%) and fixed uplift reviews (2.38%). Open-market rent reviews continue to significantly lag the rise in land and building cost inflation and there is a general expectation across the industry that this will soon change. For the new buildings needed by health authorities to attract the required investment, rental levels will need to increase, with a knock-on impact for existing assets.

Exhibit 5: Rental value by type of review



Source: MedicX Fund

Exhibit 6: Rent profile by tenant type



Source: MedicX Fund

The quality and predictably of the portfolio income stream is not simply the length of the leases and the effectively upwards-only rents that apply to the vast majority of the assets. It can also be seen in constant levels of pretty much full occupancy and an almost complete absence of speculative new building, and in the credit quality of the tenant base. As at end-FY17, 84.2% of the rent roll was effectively UK-government backed, being attributable either to UK GPs for whom the NHS provides rent reimbursement or directly to the NHS itself. In the RoI, the Health Service Executive provides a similar quality of covenant and although RoI GP tenants do not receive rent reimbursement, we believe they are of good quality, as are pharmacy tenants, who are mostly co-located within the healthcare facilities.

Financials and estimate revisions

For the FY17 year, valuation gains and EPRA NAV were ahead of our forecasts, although rent producing asset growth was lower than we had expected with a small negative knock-on effect to net rental income and adjusted earnings.

We have made only modest adjustments to our current year (FY18) forecasts, with the shortfall in end-FY17 rent earning assets feeding through to gross rental income, but this is slightly more than offset by lower interest expense (less debt being the flipside of lower assets) and a reduction in forecast direct property expenses.

Exhibit 7: Performance versus forecast and forecast changes

	Net rental income (£m)			Net earnings (£m)			Adjusted EPS (p)			DPS (p)			EPRA NAV/share (p)		
	Forecast	Actual	% diff.	Forecast	Actual	% diff.	Forecast	Actual	% diff.	Forecast	Actual	% diff.	Forecast	Actual	% diff.
09/17	36.8	35.9	-2.4%	14.9	14.9	0.3%	3.6	3.6	0.3%	6.00	6.00	0.0%	75.1	76.5	1.8%
	Old	New	% change	Old	New	% change	Old	New	% change	Old	New	% change	Old	New	% change
09/18e	42.0	40.4	-3.7%	16.9	17.2	1.5%	3.9	4.0	1.4%	6.05	6.04	-0.2%	75.4	76.9	1.9%
09/19e	N/A	45.9	N/A	N/A	18.8	N/A	N/A	4.4	N/A	N/A	6.08	N/A	N/A	77.9	N/A

Source: MedicX Fund accounts, Edison Investment Research

With the current debt being long term and fixed, and with a substantial share of the cost base being formula driven in the form of investment advisory and property management fees, the key driver of forecasts are the assumptions made about the scale and mix of commitments to new property assets and the marginal cost of debt.

We continue to assume £100m in new commitments in FY18 and look for an increase to £114m in the newly forecast FY19. Around 70% of the forecast commitments over the period are assumed to be forward funding of development schemes, not all completed by end-FY19 such that cash investment is forecast at £164m and requiring a similar amount in new debt funding. The additional debt is assumed to cost 4.45% pa, slightly above the current average cost of debt of 4.3%. FY18 reported earnings benefit from a continuation of the fixed investment advisor fees, a non-repeat of the £240k REIT conversion costs, and rising net rental income. It is only in FY19 that we expect investment advisor fees to show a small increase as investment property assets rise above £782m and reach £866m by end-FY19. In aggregate, over FY18 and FY19 we look for net rental income growth of 28% and total administrative expense growth of just 5% to generate a 30% increase in operating profits before valuation movements.

We have not assumed further equity issuance under the block listing facility or otherwise, although this seems likely. As a result, our forecast net LTV is just under 60% by end-FY17, above the medium-term target of 50% but still below the Fund's self-imposed 65% maximum.

Of less significance to the forecasts than the commitment assumption, we are forecasting 1.5% pa average rent growth over the next two years. Partly reducing the forecast rise in net LTV, we also assume that capital values will broadly follow the rent growth (assuming no change in yields) such that revaluation gains continue, but at a slower pace (c £11m pa over FY18 and FY19 compared with an average c £20m pa over the past three years).

Valuation

A key attraction of MedicX shares is the progressive dividend policy and attractive yield on a growing asset base that is a source of secure, long-term income. The board intends to continue the company's progressive dividend policy in the current year, and barring unforeseen circumstances expects to pay quarterly dividends amounting to 6.04p per share (FY17: 6.00p). This represents a yield on the share price of 7.1%, which is among the highest of a broad universe of property investment companies and REITs, as well as compared with a closer subset of peers.

As a result of increasing dividend payments and what we consider to be a temporary depressing impact on adjusted (or income) earnings from the development skew in investment activity, dividend cover reduced from 63.8% in FY16 to 59.2%. Our analysis concurs with the board's view that as the Fund continues to grow, achieve rental increases, and complete properties under construction, the expected increase in income combined with the cap on the investment adviser base fee should see dividend cover improve (FY19e: 70.7%). As things stand, the investment adviser estimates that adjusting the current portfolio for the completion of properties under construction (assuming a full year of rental income as well as interest and other costs) would see dividend cover at 69.5%, an increase on the 68.5% at end-FY16 on the same basis. We do not estimate underlying dividend cover, but note that our forecast of 70.7% for FY19 would be higher on this basis.

In Exhibit 8 we show the Fund's total return on EPRA NAV over the past five years. It adjusts the annual change in NAV for dividends paid out in the period but does not assume dividend reinvestment.

Exhibit 8: Five-year total return on EPRA NAV

	Sep-13	Sep-14	Sep-15	Sep-16	Sep-17	5 years to Sep-17
Opening EPRA NAV (p)	63.7	62.5	65.4	70.8	73.2	63.7
Closing EPRA NAV (p)	62.5	65.4	70.8	73.2	76.5	76.5
Dividends paid in period (p)	5.6750	5.7750	5.8750	5.9375	5.9875	29.3
Total return on EPRA NAV	7.0%	13.9%	17.2%	11.8%	12.7%	65.9%

Source: MedicX Fund data, Edison Investment Research

Although dividend distributions have regularly exceeded income earnings (ie earnings adjusted primarily for property valuation movements) over the period this has been more than made up for by capital earnings. EPRA NAV per share has increased over the period and the cumulative total return of 65.9% over the five-year period represents an annual compound return of 13.5% pa. Property revaluation gains over the period have been substantially driven by yield compression, with the net initial yield (NIY) on the portfolio tightening from 5.8% at end-FY12 to 5.08% at end-FY17. Our forecasts assume some continuing revaluation gains driven by our estimate of the impact of rent growth at an unchanged NIY. On this basis, our forecasts imply a total return on EPRA NAV of 8.4% in FY18 and 9.2% in FY19 with both DPS and EPRA NAV per share showing modest increases year over year.

Exhibit 9: Peer comparison

	Share price (p)	Market cap (£m)	Current year DPS (p)	Prospective yield (%)	P/NAV (last published) (x)
Assura	61	1,445	2.60	4.3%	1.15
Primary Health Properties	114	696	5.25	4.6%	1.19
Secure Income	362	793	14.00	3.9%	1.02
Target	110	277	6.45	5.9%	1.06
TRITAX	145	1,974	6.40	4.4%	1.09
Average (ex MedicX)		**1,037**		**4.6%**	**1.10**
MedicX	84	347	6.04	7.2%	1.09

Source: Company data, Edison Investment Research. Note: Prices as at 14 December 2017.

In Exhibit 9 we show a summary comparison of MedicX with a selection of companies specialising in long-let assets, including direct peers Primary Health Properties (PHP) and Assura Group.

MedicX shares have seen some de-rating in recent weeks, a period that has seen the first UK interest rate rise in 10 years and continuing substantial new equity issuance in the broad REIT sector and also within the primary healthcare sector. It is now trading on a below average P/NAV despite offering the highest prospective dividend yield, albeit not fully covered by income earnings. Its two closest peers, PHP and Assura, have maintained premium P/NAV ratings. The tendency of the primary care property companies to trade at higher P/NAVs can in part be explained by the strength of their tenant covenants; with mainly government-funded income and long-term leases their yields invite comparison with UK government gilt yields. With a weighted average unexpired lease length of 14.1 years, backed 90% by the UK and RoI governments, and substantially matched fixed rate debt of 12.7 years' average maturity, MedicX has locked in cash flows for many years. The comparison of its dividend yield (or even its current recurring income yield of c 5%) with the c 1.3% yield to maturity available on the 2028 UK gilt is striking.

Growth in the investment adviser's discounted cash flow

On behalf of the Fund, the investment adviser also carries out a discounted cash flow valuation (DCF) of the assets and associated debts at the end of each period. The basis of preparation is similar to that utilised by certain infrastructure funds, deriving the value of each asset from the net present value of expected future cash flows, after allowance for debt and taxation. At end-FY17 the DCF value per share was estimated at 98.5p (FY16: 96.6p), increasing over the year primarily as a result of capturing the expected future cash flows on acquisitions made, unlike adjusted earnings per share, which saw a drag from investment in predominantly investment schemes. The key DCF assumptions have remained unchanged, with discount rates of 7% for completed and occupied assets, and 8% for developments (a weighted average of 7.07%); an average 2.5% annual increase in rents and residual values based on 1% capital growth from current value to lease expiry. The adviser reports that for DCF NAV to match the 30 September share price of 91p, it would have to assume separately either a 7.9% discount rate, a 1.2% increase in rents per year or 0.1% capital growth.

Additionally, the investment adviser has provided an analysis of how the EPRA NAV would look if the investment properties were to be valued as a collective portfolio rather than as standalone investments. In the market, portfolios change hands at a premium because they allow larger investors to immediately benefit from the greater scale and easier access that they bring. Additionally, the acquisition of a corporate portfolio-owning entity reduces the purchasers' costs (including stamp duty), increasing the value of the portfolio to the buyer. The alternative NAV format, provided by the investment adviser and shown in Exhibit 10 is highly illustrative and would require the sale of the fund to be realised. It does, however, provide an interesting bridge between the published NAV and the investment adviser's DCF valuation.

Exhibit 10: Investment adviser's alternative NAV per share

EPRA NAV per share	**76.5p**
Adjust for purchasers' costs from 6.8% to 2.3%	7.2p
Portfolio premium of 5%	7.9p
Alternative NAV per share	91.6p

Source: MedicX

Sensitivities

MedicX's portfolio has a low-risk profile and relatively predictable income. Around 90% of rents are government backed, and the balance predominantly pharmacy tenants. Debt funding is fixed rate with an average maturity of 12.7 years, which is similar to the average unexpired lease length of 14.1 years. Key sensitivities include:

- The ability to source and execute investments at an appropriate yield premium to funding costs. As noted above, the Fund through its investment advisor has a variety of sources from which to source new investments. Meanwhile the prospects for new build commissioning are improving. The spread between property yields and funding costs has narrowed but remains positive, and is wider in the RoI.
- The ability to attract sufficient debt funding at appropriate cost. While interest rates are at cyclical lows and may be expected to increase over time, existing borrowing has an average duration of 12.7 years and is all fixed rate. Higher rates on their own may reduce the ability of the Fund to grow its existing base unless reflected in higher cash yields on acquisition.
- The ability to generate rental growth on the c 70% of leases that are subject to open-market review on a rolling three-year basis. We have noted above that there is a widespread industry view that open-market reviews will need to increase to take account of historical land and build cost inflation. This would have a positive effect on rental income and would provide capital value protection against any future widening in market valuation yields.

Exhibit 11: Financial summary

Year ending 30 September	2015	2016	2017	2018e	2019e
£000's					
Net rental income	32,767	34,322	35,947	40,416	45,916
Investment advisory fee	(3,725)	(3,852)	(3,867)	(3,878)	(4,229)
Investment advisory performance fee	0	(1,553)	0	0	0
Property management fee	(849)	(889)	(925)	(977)	(1,056)
Other administrative expenses	(938)	(1,015)	(1,293)	(1,102)	(1,116)
Total recurring administrative expenses	(5,512)	(7,309)	(6,085)	(5,957)	(6,400)
Operating profit before valuation movements	27,255	27,013	29,862	34,459	39,516
Net revaluation gain/(loss) on investment property	25,603	15,523	18,654	10,407	11,733
Profit/(loss) on disposal of investment property	0	31	(65)	0	0
Operating profit	52,858	42,567	48,451	44,866	51,249
Share of profit of JV	0	0	10	20	20
Net finance expense	(13,736)	(14,380)	(15,149)	(17,319)	(20,739)
Profit before tax	39,122	28,187	33,312	27,567	30,530
Tax	(3,293)	(1,556)	5,312	0	0
Net profit	35,829	26,631	38,624	27,567	30,530
Adjust for:					
Net revaluation gain/(loss) on investment property	(25,603)	(15,523)	(18,654)	(10,407)	(11,733)
Deferred tax	3,293	1,556	(5,312)	0	0
Other	(88)	(56)	0	0	0
EPRA earnings	13,431	12,608	14,658	17,160	18,797
Investment advisory performance fee	0	1,553	240	0	0
Other	0	0	0	0	0
Adjusted earnings	13,431	14,161	14,898	17,160	18,797
Average f.d. number of shares outstanding (m)	361.3	374.5	413.1	429.1	430.0
Basic IFRS EPS (p)	9.9	7.1	9.4	6.4	7.1
Fully diluted adjusted EPS (p)	3.7	3.8	3.6	4.0	4.4
DPS declared (p)	5.90	5.95	6.00	6.04	6.08
Dividend cover	63.3%	63.8%	60.2%	66.3%	72.0%
Expense ratio*	2.23%	2.11%	1.94%	1.81%	1.92%
BALANCE SHEET					
Investment properties	553,479	612,264	680,355	756,012	866,495
Investment in equity accounted JV	0	0	1,035	1,035	1,035
Total non-current assets	553,479	612,264	681,390	757,047	867,530
Cash & equivalents	56,910	20,968	32,145	20,237	16,873
Trade & other receivables	6,778	8,519	7,176	8,520	9,787
Total current assets	63,688	29,487	39,321	28,756	26,660
Loans due after one year	(336,412)	(334,307)	(370,583)	(430,583)	(530,583)
Deferred tax liability	(4,331)	(5,887)	(575)	(575)	(575)
Other non-current liabilities	(1,465)	(1,490)	(1,456)	(1,456)	(1,456)
Total non-current liabilities	(342,208)	(341,684)	(372,614)	(432,614)	(532,614)
Loans due within one year	(1,896)	(1,983)	(2,213)	(2,213)	(2,213)
Trade & other payables	(18,966)	(19,923)	(18,682)	(21,299)	(24,467)
Total current liabilities	(20,862)	(21,906)	(20,895)	(23,512)	(26,680)
Net assets	254,097	278,161	327,202	329,677	334,896
Adjust for:					
Deferred tax	4,331	5,887	575	575	575
EPRA net assets	258,428	284,048	327,777	330,252	335,471
Adjustment to debt at fair value	(25,212)	(59,134)	(42,574)	(42,574)	(42,574)
EPRA NNAV	233,216	224,914	285,203	287,678	292,897
Period end f.d. number of shares outstanding (m)	365.1	388.1	428.6	429.6	430.5
Basic IFRS NAV per share (p)	69.6	71.7	76.3	76.7	77.8
Fully diluted EPRA NAV per share (p)	70.8	73.2	76.5	76.9	77.9
Fully diluted EPRA NNAV per share (p)	62.7	56.4	66.4	66.8	67.9
CASH FLOW					
Cash flow from operating activity	10,152	11,408	15,104	18,434	20,698
Cash flow from investing activity	(23,316)	(36,281)	(50,668)	(65,250)	(98,750)
Issue of equity (net of costs)	6,816	18,962	34,526	0	0
New loan facilities drawn/debt repaid	52,077	(1,895)	37,070	60,000	100,000
Dividends paid (net of scrip)	(19,247)	(21,582)	(24,013)	(25,092)	(25,312)
Other financing activity	(697)	(6,554)	(859)	0	0
Net cash flow from financing activity	38,949	(11,069)	46,724	34,908	74,688
Change in cash	25,785	(35,942)	11,160	(11,908)	(3,364)
FX	0	0	17	0	0
Opening cash	31,125	56,910	20,968	32,145	20,237
Closing cash	56,910	20,968	32,145	20,237	16,873
Debt	(338,308)	(336,290)	(372,796)	(432,796)	(532,796)
Net debt	(281,398)	(315,322)	(340,651)	(412,559)	(515,923)
Net LTV	50.2%	50.8%	49.5%	53.9%	59.5%

Source: MedicX Fund data, Edison Investment Research. Note: *Recurring admin expense (excluding direct property expense) as % average EPRA NAV.

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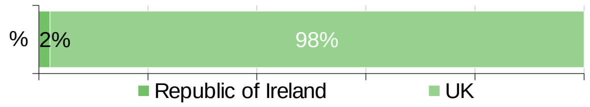
Revenue by geography



The board

Non-executive chairman: David Staples

Mr Staples is a fellow chartered accountant and chartered tax adviser. He was a partner at PwC for 13 years, running that company's tax practice in South-East England. He is a non-executive director of five other listed companies, HSBC Private Bank and certain private equity funds run by Apax Partners. Mr Staples will not stand for re-election at the AGM in February 2018 and will be replaced as chairman by Helen Mahy.

Non-executive director: John Hearle

Mr Hearle is a fellow of the Royal Institution of Chartered Surveyors and a member of the Chartered Institute of Arbitrators. Until October 2015 he ran the healthcare division of Aitchison Raffety and was group chairman. He runs a company called Medical Premises Consultants, which continues to do work for Aitchison Raffety. He has previously worker for the District Valuer's Office, and TSB Property Services. He is resident in the UK.

Non-executive director: Laure Duhot

Ms Duhot currently acts for a number of property firms and investors across Europe, providing strategic advice and transaction support, with a focus on alternative real estate assets. She has previously held senior executive roles with Grainger plc, Pradera, and Sunrise Living Inc. and is an experienced non-executive director. She is currently on the boards of MIC Ltd. and The Guinness Partnership.

Non-executive director: Steve Le Page

Mr Le Page is a chartered accountant and chartered tax adviser, having been a partner at PwC from 1994 until 2013. He is a non-executive director of two listed funds. He is resident in Guernsey.

Non-executive director: Helen Mahy

Helen Mahy is chairman of The Renewables Infrastructure Group, a FTSE 250 investment company, and is a non-executive director of SSE and of Bonheur, a company listed on the Oslo Stock Exchange. Ms Mahy has also been a non-executive director of Aga Rangemaster, Stagecoach Group and SVG Capital. In 2015, Ms Mahy was awarded a CBE for services to business and voluntary service, particularly to the legal profession and diversity in the workplace. Helen was formerly group company secretary and general counsel of National Grid until she retired in 2013. Ms Mahy is resident in the UK.

Principal shareholders	(%)
Architas Multi-Manager	8.79
Investec Wealth & Investment	7.88
CCLA Investment Management	7.47
Brewin Dolphin Securities	6.83
Valu-Trac Investment Management	5.60
BlackRock	5.09

Companies named in this report

Assura Group (AGR), Primary Health Properties (PHP), Secure Income REIT (SIR), Target Healthcare (THRL), Tritax Big Box REIT (BBOX)