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Please note that the commentary is for the retail class of the Fund.

After a strong and somewhat surprising run into the end of the year, listed property delivered a total return of 8.4% for the quarter, resulting in the asset class returning 38.6% for 2021. This has now been the fifth consecutive quarter of positive returns for the sector as it continues to recover from the Covid-19 induced operating pressures. The good return in 2021 follows the -35.5% return of 2020, making up for most of the losses experienced in that year. However, it is still down 10.6% since the start of 2020 from a total return perspective, illustrating the severity of the initial selloff in the first quarter of 2020 (Q1-20). From a relative performance viewpoint, the sector continues to gradually gain ground against both the JSE All Share Index (ALSI) and All Bond Index (ALBI) over the medium and long term and, due to the recovery from the post-Covid-19 lows, has outperformed both indices handsomely in 2021, especially the ALBI, with an outperformance of 30%. However, the underperformance over two years is still substantial, at 23% and 14% respectively on an annualised basis. The ALPI's one-year forward dividend yield is 7.7%, and that of the Property Equity Fund is 7.6%.

Besides the August/September results season concluding in early December, which generally provided support for the sector, the most relevant news flow out the sector related to the continued potential restructuring of the A & B capital structures, with Dipula dominating these headlines at present. Corporate action or capital injections remain on the radar, with the acquisition by Sirius of Bizspace and subsequent capital raise, Growthpoint supporting the Capital & Regional capital raise, Redefine offering a swap ratio to take EPP internal (with a complicated restructure) and the Arrowhead and Fairvest merger likely to be concluded soon (with smaller listings Heriot and Safari also working towards a merger). In turn, in Australia Irongate continues to defend a potential takeover from 360 Capital. The first Covid-19 'casualty', Tower Property Fund, delisted at the end of December after shareholders approved the company's take-out offer.

Delivering a return of 7.6% during Q4-21, the Fund underperformed the benchmark, with the bulk of the underperformance occurring early in the quarter due to, among other things, its A share exposure. The Fund lost marginal ground against the benchmark over return periods of more than 12 months. For 2021, it delivered a return of 35.5%, with the negative impact of the underweight in UK dominant companies in Q1-21 becoming the biggest detractor as these companies benefitted from the reopening trade at the time. For the quarter, the Fund benefitted from its overweight positioning in Equites, Investec Property, MAS and Attacq. The non-benchmark position in Arrowhead A also supported performance. Our relative positioning in Hyprop, Dipula A, Fortress A, Sirius and NEPI Rockcastle detracted value during Q4-21. During the period, the largest increase in exposure occurred in Capital & Counties, Attacq and SA Corporate. The largest reduction in exposure occurred in EPP and Redefine after the details of their prospective restructurings were announced, as well as Hyprop and Irongate. We also sold out of our positions in Spear REIT and Liberty 2 Degrees.

The reporting season during the quarter brought distributable earnings per share growth of 11.4% year on year (y/y) (excluding outlier Accelerate), with dividend per share growth at 8.5%, with an average payout ratio of 88.9%. The calculation is done in rands, so all euro or pound reported earnings have been converted by the exchange rate determined by the company. Although things remain tough operationally, there seems to be some light at the end of the tunnel. This contrasts with the risks that we pointed out last quarter, especially related to the lack of demand for office space and large negative reversion potential in, especially, the industrial/logistics sector. In our dealings with third-party sector participants, green shoots are appearing on the vacancy front, albeit still very limited, while many are referencing flat market rentals across the board rather than the declining rentals that have been experienced in the recent past, especially the last 18 months.

Two things stand out from the results season. First, although balance sheet risk has decreased substantially over the last 12 months, which we also referenced in last quarter's commentary, companies continue to actively look at various ways to derisk this element of their operations. This is not only in actual gearing levels (most commonly still via dividend reinvestment offerings or disposals) but also via looking to decrease the implied offshore gearing a company may have despite the negative impact this should have on distributable earnings. Secondly, some expansionary talk is starting to filter through once more now that Covid-19-related crisis management is not the sole focus of most management teams.

MSCI released its Bi-Annual Property Index for South Africa for H1-21 during the quarter. This Index captures the return of direct commercial property in the country. The total return for H1-21 came in at 1.3% (6 months' return), with capital growth at -2.6% and income return at 4.0%. This compares to the full year 2020 numbers of -3.0% total return, 7.2% income return and -9.6% capital return. What came through were better y/y total returns versus 2020, with smaller retail format especially strong, as were some industrial formats. There is an improvement in capital growth momentum, although still negative, but better than H1-20. Vacancies continue to increase (from 8.7% to 9.6%), and rental levels decrease.

Going forward, the sector has surprised with the strong run into the end of year as earnings are still lagging that of pre-Covid-19. Although global inflation pressure should be beneficial for property as an asset class, a period of share price consolidation should be expected as three sticking points remain besides rental levels and tenant demand. Costs have been very well contained over the last 18 months and, with a return to normality, we may see pressure start to creep in once more. The interest rate cycle has already turned into a hiking cycle, and although there should still be some benefit from higher hedges rolling off in the immediate future, the overall interest rate profile could start to creep higher. And lastly, although our base case is that property value write-downs are mostly out of the system, some more recent comments reflect a view that valuers have not been ruthless enough in reducing valuation assumptions, especially those related to market rentals. And that discounted cash flow valuations, which are still the most widely used, are not very relevant when buyers focus on year one yield or the value sitting in the actual bricks and mortar.

Portfolio managers
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as at 31 December 2021