

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

Performance and Fund positioning

After an initial stutter, the sector recovered strongly in the latter two thirds of the quarter on the back of the good performance from global counterparts as investors started to discount a much softer landing in the interest rate cycle of major global markets. Inflation rates in many markets have been moving lower faster than anticipated, which some investors believe will result in a quicker and more aggressive interest rate cutting cycle than what central banks have been indicating thus far. The result was a return of 16% for Q4-23 from the FTSE/JSE All Property Index (ALPI), the second-best quarterly return of the last three years, leading the sector to a positive return of 11% for 2023. Capital flows into the sector continue to be negative although the turn in flow momentum continues to gather steam. From a relative performance viewpoint, the sector gained ground against the FTSE/JSE All Share Index (ALSI) over most time periods, while against the FTSE/JSE All Bond Index (ALBI) the gain was less consistent, mostly over longer time periods. The ALPI's one-year forward dividend yield is 7.9% and that of the Fund is 7.7%.

Delivering a return of 14.3% for Q4-23, the Fund did not fully keep pace with the strong run of the market, thereby underperforming the benchmark. This resulted in the Fund also now underperforming the benchmark over 12 months. A major reason for the underperformance over the quarter is the Fund being underweight some of the larger, more SA-centric stocks, which benefited the most from a more general stance to interest rate-sensitive asset classes. In addition, positioning in what one can deem more defensive stocks detracted from performance. Relative positions that detracted from performance include Lighthouse, SA Corporate, Fortress B, Dipula, Fortress A, Hyprop, MAS and Attacq. On the opposite end of the spectrum, the Fund did benefit from its relative positioning in NEPI Rockcastle, Equites, Hammerson, Vukile and Resilient. During the period, the largest increases in exposure occurred in Growthpoint, similar to Q3-23, as well as Equites and Resilient. The Fund also participated in a Sirius capital raise. The largest decreases in exposure occurred in NEPI Rockcastle, Redefine and Dipula.

The most noticeable corporate announcement of the quarter was (once again) the potential collapse of the Fortress dual share structure into a single share through the buy-out of all Fortress B shares in exchange for NEPI Rockcastle shares (in which Fortress is the largest shareholder). Key this time is that it is a shareholder-led transaction, thereby making the likelihood of success higher. Thus far, official shareholder support for the proposal is at 55% for Fortress A and 63% for Fortress B, with both sets of shareholders required to reach a 75% support level. The general meeting is to take place in the third week of January with Coronation supportive of such a transaction at the time of writing.

This quarter also saw the delisting of two property companies, namely Liberty 2 Degrees (L2D) and Transcend, and the granting of REIT status to the renamed The Collins Property Group (formerly Tradehold). L2D was taken back to its in-house roots by its majority shareholder Standard Bank (previously within Liberty), while Transcend remains within the listed sector via Emira, which took out minorities after already being a majority shareholder in its listed peer. The Collins Property Group comes out of a restructured Tradehold, with the core portfolio now comprising the previously majority-owned private portfolio from the Collins family. We believe the opportunity for corporate action is gradually closing, with those still most likely being legacy transactions of which the legwork has already been done (i.e., Heriot and Safari). However, management teams are gradually more prepared to be on the offense rather than defense as commentaries out of various company stables point to a belief that the market is approaching a turning point in the interest rate and property cycle. Management teams are starting to refer to potentially expansionary actions, with individual asset acquisitions likely the first foray into the expansionary mode, although we may see some unsolicited corporate transactions. Sirius has already concluded an equity raise during November to act on an acquisition pipeline, while Texton announced a rights issue early in December to be partly used to expand its offshore exposure. In turn, Lighthouse confirmed the acquisition of its second asset in Spain, this time in a 50/50 partnership with Resilient, similar to a partnership that the two companies has in France.

Results season for companies with an August or September reporting period concluded in December. Although key names like Equites and Redefine have negatively impacted the reported distributable earnings per share (DEPS) and dividend per share (DPS) growth, which resulted in the DEPS growth and DPS growth when excluding offshore names Sirius and Schroders to be -5.6% and -1.9% respectively, there was a promising tone with regards to underlying property operating metrics. Similar to companies reporting June numbers during the previous quarter, the negative impact of average higher interest rates will still be felt well into 2024 from a distributable earnings point of view. However, more important for the overall health of the sector is the general

improvement in rental reversions and vacancies, as well as more efficient cost management, especially when it comes to the recovery of diesel costs and the way in which the increased utilisation of solar energy impacts the electricity cost base, with some funds even admitting openly that solar is a clearcut additional income stream rather than a cost centre.

MSCI released its bi-annual SA property index, which gives an indication of direct property returns for the first six months of the year, during October. Although returns were fairly similar to 1H22, there was a slowdown in returns from the second six months of 2022. The total return for 1H23 came in at 3.5%, compared to 3.9% for 1H22 and 5.1% for 2H22. There was a slowdown in capital value momentum across all sectors during the sequential six-month periods. Per sector, the total return came in at 5.5% for Industrial, 4.2% for Retail, 2.8% for Residential and 1% for Offices. The index's y-o-y net operating income growth of 1.9% was heavily supported by Industrial at 6.1%. In comparison, the other sectors delivered weak growth at 1.9% for Offices, 0.9% for Retail and -0.1% for Residential. There was a marginal improvement in total vacancies across all sectors to 7.2%, supporting base rental growth (especially for residential, where vacancies improved substantially; base rental growth incorporates the movement in vacancies).

Outlook

As mentioned last quarter, the sector is at the mercy of macroeconomic and geopolitical factors, which turned out, against the momentum of Q3-23, to have a very positive impact in Q4-23. The risk of higher-for-longer interest rates globally seems to have abated, although geopolitical and broader election outcome risks in various geographies may, once again, sway investor sentiment during the coming year. In addition, sector prospects will remain closely tied to interest rate-related investor sentiment.

After the strong run in November and December, it remains to be seen how sustainable the current share price levels are. The ALPI has now recovered close to 23% from its most recent lows during the last week of October, reaching a post-Covid-19 total return index high, driven mostly by the dual- and inward-listed companies and larger more liquid South African-centric names. Although the run has been strongly supported by an increase in general risk appetite and supportive bond markets, a rerating relative to the bond market has also occurred, indicating a likely return of more general investors to the sector.

The sector is likely to take a breather in the coming weeks, with the latter part of February into the end of March as important milestone dates. The anticipated trading updates or results releases during this period will provide a good barometer of the operational state of the sector, which will likely still be supportive of a continued recovery in net operating income growth.

Portfolio managers

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as at 30 December 2023