MEDIA RELEASE FROM SA REIT ASSOCIATION

12 March 2014

New property listings become challenging as the sector moves to consolidation

2014 has confirmed that the listed property sector is moving from a cycle of new listings, into one of consolidation.

This trend is typical of the listed property sector in current market conditions, reports the SA REIT Association, and creates a unique set of opportunities.

The SA REIT Association represents South Africa's listed REIT (Real Estate Investment Trust) sector. SA REIT members comprise all listed SA REITs and represent around R233 billion worth of real estate assets.

"This cycle has seen nine new JSE listings, and while there may be a few more attempts to bring new companies onto the exchange, it will be exceptionally difficult. Equity and debt pricing has made it more demanding on vendors. The prices they will be able to fetch are no longer feasible," says Evan Jankelowitz of Sesfikile Capital.

Contributing to this challenge is the good value already available to investors in the listed property sector from established companies with solid track records.

"The listed property sector offers many cheap options to invest in the current market, as prices have come off sharply," explains Jankelowitz. "However, new listings will have to differentiate their offering considerably to entice investors."

And, using price as a differentiator will be difficult. "If a potential new listing wants to differentiate themselves on price, they would need to list north of a 10% yield, however this is unlikely to induce the owners to bring their portfolio to market."

Providing a unique investment proposition is one way to achieve a successful listing in this market. Jankelowitz cites Attacq with its development bias and Investec Australia with its pure Australian exposure as examples with sufficient differentiation to attract investor appeal.

With the high costs of bringing relatively small companies to market coupled with the existing appetite of the incumbents to grow, new listings have clearly become a challenge. But there are attractive alternatives for property portfolio owners seeking liquidity from their investment.

"In this market, it is preferable to transfer the portfolio into an existing listing. This would ultimately be a more efficient and effective mechanism," says Jankelowitz. "However, we often find that management's attachment to their assets and business may lead to a more subjective thought process. The core reasons behind listing are providing means of funding and liquidity. Both these outcomes are generally enhanced when selling into an already established entity. But, if it's the incumbent's ability to deliver future growth and profit off their success that is driving the proposed listing, the seller's control and managerial direction would be marginalised."

When satisfying the sector’s appetite for growth, consolidation is likely to replace new listings in the coming years because substantial physical property portfolios are hard to come by.

“In addition, the listed property market by nature corrects far quicker than physical property assets. Mergers are a better buying opportunity than growth through acquiring physical assets and developments,” says Jankelowitz.

But, consolidation also comes with challenges. “Onerous management contracts will provide a hurdle for consolidation. The risk is that companies will overpay for these management agreements at the expense of shareholders’ best interest.”

Jankelowitz believes smaller companies that have failed to grow substantially and have a lack of liquidity reflecting in a depressed price, will become takeover targets. “A strong rating should be a natural deterrent, as the price makes it difficult for predators to stomach, however this takes time.”

News of corporate action already in the market includes the three-way consolidation talks between Delta, Rebosis and Ascension, as well as Arrowhead’s acquisition of a substantial stake in Vividend together its outright acquisition of its management company. Vukile is potentially seeking to acquire Synergy after having bought a 34.5 stake in the company in December last year. Most recently, it was announced that Redefine Properties will acquire the entire issue capital of Annuity Properties by way of a scheme of arrangement, and Annuity’s asset and property management companies.

In addition, those companies with a legacy and strategic relationships will find merging attractive in this market, such as Sycom and Acucap, and Premium and Octodec.

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