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Listed property sector could be poised for another wave of corporate action

Speculation about further consolidation in 2014 for the most active sector on the JSE for corporate action, the SA REIT (Real Estate Investment Trust) sector, is rife yet again.

The latest wave of speculation was triggered when Redefine Properties acquired an 11% stake in Emira Property Fund in late September.

“This is never a dull sector,” says Keillen Ndlovu, Head of Listed Property Funds for Stanlib.

Ndlovu is one of the high-profile panelists set to speak at the first-ever SA REIT Conference, taking place next week (22 October) at the Sandton Convention Centre, and sponsored by Nedbank Corporate Property Finance. He will be joined by Evan Jankelowitz of Sesfikile Capital, and more than 10 other industry heavyweights on what will be insightful panel discussions at the conference.

Ndlovu says, when it comes to mergers and acquisitions in the REIT sector, there’s still lots of activity, notwithstanding Redefine’s failure to take over Fountainhead and the collapse of the tripartite merger of Rebosis, Delta and Ascension.

Ndlovu lists the latest activity in the market: “The Premium and Octodec merger and the Acucap and Sycom merger are on the cards. Growthpoint is pursuing Acucap. Redefine acquired Annuity a couple of months ago. Redefine has to start the process all over again with Fountainhead. Arrowhead bought Vividend. Arrowhead has not given up on Dipula. Vukile will relook at Synergy despite the collapse of their talks recently. Rebosis is now going solo and looking to acquire the rest of Ascension. So there’s still so many things to look forward to.”

While more merger and acquisition action may still be on the cards this year, Evan Jankelowitz of Sesfikile Capital does not necessarily agree. He advises that the market shouldn’t see all activity in the listed property sector as consolidation moves.

“What we are seeing is not necessarily value creating transactions at asset level. Instead, some REITs are using the market and their balance sheets in an attempt to optimise value through corporate measures,” he points out.

Jankelowitz adds that corporate action has to make sense and it cannot be a case of acquisition for the sake of it. “There are few obvious transactions in this market. Even with an appetite for growth and access to funding, a REIT must be responsible with its acquisitions. At the end of the day, investors care about earnings growth not asset growth.”

Taking Redefine's new stake in Emira as a case, Jankelowitz says it seems unlikely this is a takeover bid as Redefine could add little value to Emira's management, as it is already well managed. "The management at Redefine are quite innovative in this arena, and I'm sure they are eyeing other means to extract value."

The listed property sector certainly has access to funding. Ndlovu notes the amount of equity raised so far this year has been phenomenal for listed property, both REITs and capital growth funds. "At the beginning of the year we were forecasting about R7 billion to R8 billion. However, we have seen over R27 billion being raised through new listings, rights issues, private placements and book builds."

Moreover, this number is likely to increase soon driven by potential new listings together with more REITs adopting Growthpoint's model of distribution or dividend re-investment programmes, which results in more equity being issued on a regular basis.

Equity raised in 2014 greatly exceeds the R18 billion raised in 2013, R11 billion in 2012 and R16 billion in 2011. "In simple terms, this reflects an increased appetite for listed property. It has firmly established itself as a separate asset class," says Ndlovu, who points out the market capitalisation of listed property has grown more than 10 times over the last 10 years to above R300 billion.

He adds that all results recently reported from the sector generally surprised on the upside, including Growthpoint at 8.3%, Capital Property Fund at 10.2%, Resilient at 21%, SA Corporate at 8.6%, Texton at 10.6%, Fortress at 14.4%, Hospitality at 14.5%, Synergy at 9%, Hyprop at 11.3%, Ascension at 10% and Emira at 7.5%.

The outlook for the sector is generally positive too. Ndlovu says: "We are expecting income growth to average 8.5% over the next 12 months. This results in a forward yield of 7.4%. This may be lower than 10-year bond yields at 8.2% and similar to cash (one-year NCD) at 7.4% as well. However, listed property provides income growth whereas cash and bonds do not."

Jankelowitz notes that for the last three years the listed property sector has averaged 22% in total returns, including capital growth, per annum. "This level can't be sustained year in and year out. It's been a great year so far, but may be more subdued in the final months of 2014. Property should have a good year, but we're not expecting fireworks. We still see good value for the medium- to long-term investors. Listed property is a relatively high-yielding and growing yield product that should be a part of most balanced portfolio."

Ndlovu notes listed property has been the best performing asset class over the last 10 years. "It has delivered better risk-adjusted returns," says Ndlovu. "Yes, it has a higher correlation to bonds of 0.7 to 0.8 over the last 5 years, but listed property will beat bonds over time mainly because it provides growing income whereas cash and bonds do not. Most importantly, it is different compared to equities as reflected by its low correlation of 0.1 over the last 5 years. Listed property's earnings are less volatile and can be predicted with reasonable certainty."

What can investors expect to see from this highly active sector in future? “We are likely to see more and more offshore exposure outside South Africa’s borders, as most REITs are increasing their exposure to the rest of Africa, UK, Western and Eastern Europe and Australia,” reports Ndlovu.

Offshore earnings now make up almost 20% of the SA listed property sector. “Around eight years ago, local companies had no offshore exposure at all,” states Ndlovu. “We may see more diversification locally too, as residential property exposure is starting to pick up. There’s talk of a couple of funds looking to create a 100% residential focussed fund. There are other sectors that could be added to the SA listed property sector over time, such as Storage.”

**** For more information on the SA REIT Conference on 22 October 2014 at the Sandton Convention Centre visit www.sareit.com and follow @SA_REIT on twitter.***

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