High returns on property may be over

By Nick Hedley

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The days of high returns on property portfolios may be over - although analysts and industry leaders believe the sector is still investor friendly, with indices which provide more exposure to smaller, faster-growing property companies tipped to provide the best returns.

According to Catalyst Fund Managers, South African listed property provided total returns of 35.9% last year and the sector "remains an attractive alternative to cash and bonds over the long term".

However, major companies in the sector are not expecting listed property to maintain returns above 30%, unless interest rates are unexpectedly cut.

Stanlib property funds head Keillen Ndlovu says the days of the 26% annualised total returns seen over the past 10 years "are behind us".

"We believe that about 10%-12% average total returns per year over the next five years could be achievable. So we would not stay away from listed property, but we would rather have realistic expectations," he said.

Bonds "are at their lowest levels" but Stanlib is still fairly comfortable with current levels.

Ndlovu says while listed property income has "'guaranteed' annual escalations of about 8%, equities do not have that privilege as equity companies may alter their dividend policies, while listed property companies have fairly predictable earnings.

The PropTrax Sapy index, an exchange-traded fund which tracks the performance of the FTSE-JSE Sapy index, is heavily weighted in favour of a few big companies, with Growthpoint Properties making up almost a quarter of the index.

The PropTrax Ten index, on the other hand, consists of the top 10 property companies by investable market capitalisation, but they are held in equal weightings of 10% each (at the quarterly rebalancing date).

For the 12 months to November 30 last year, the PropTrax Sapy index grew 36.8% - out-performing the PropTrax Ten index which managed 34.4% growth, although large foreign inflows into the Sapy index early in the year distorted the index, says etfsa.co.za managing director Mike Brown.

He says the PropTrax Ten is attractive because of the exposure to those companies "where most of the action and growth has been".

The Sapy index gives 50% weighting towards Redefine and Growthpoint, while some of the smaller and fast-growing companies in the index only receive a 1% weighting, Brown says.

"The benefits should show up over time - the calculations indicate that the PropTrax Ten index should outperform the Sapy 20," he said

The PropTrax Ten also pays about a half a percentage point higher dividend yield, adding to its attraction, he says.

Property analyst at value asset manager RE:CM John Rainier says listed South African property is overpriced and investors should avoid the industry until prices are reduced to their fair values.

He says the listed property market has been trading at about a 45% premium to reported net asset value of underlying property values.

"The sector is more expensive than it has been for a number of years and there is therefore no margin of safety to offer investors protection from a permanent loss of capital."

Rainier says the listed property index has been trading at a historic dividend yield of 6.32% compared with the earnings yield of the all share index of 7% - indicating the market expects listed property to grow earnings into perpetuity faster than the all share index.

The time to invest in listed property will be "after a few years of disappointing earnings growth, which will effectively change pricing perceptions", Rainier says.

Source: *Business Day* via I-Net Bridge