

OLD MUTUAL

# INVESTING IN A POST-COVID PROPERTY PARADIGM

Evan Robins, Investment Forum March 2024

Portfolio Manager: Old Mutual SA Quoted Property Fund



INVESTMENT GROUP

CITYWIRE

SOUTH AFRICA  
FUND MANAGER  
AWARDS 2023  
WINNER

THE EUROPEAN  
*Global Banking & Finance*  
Awards 2023

Old Mutual Investment Group  
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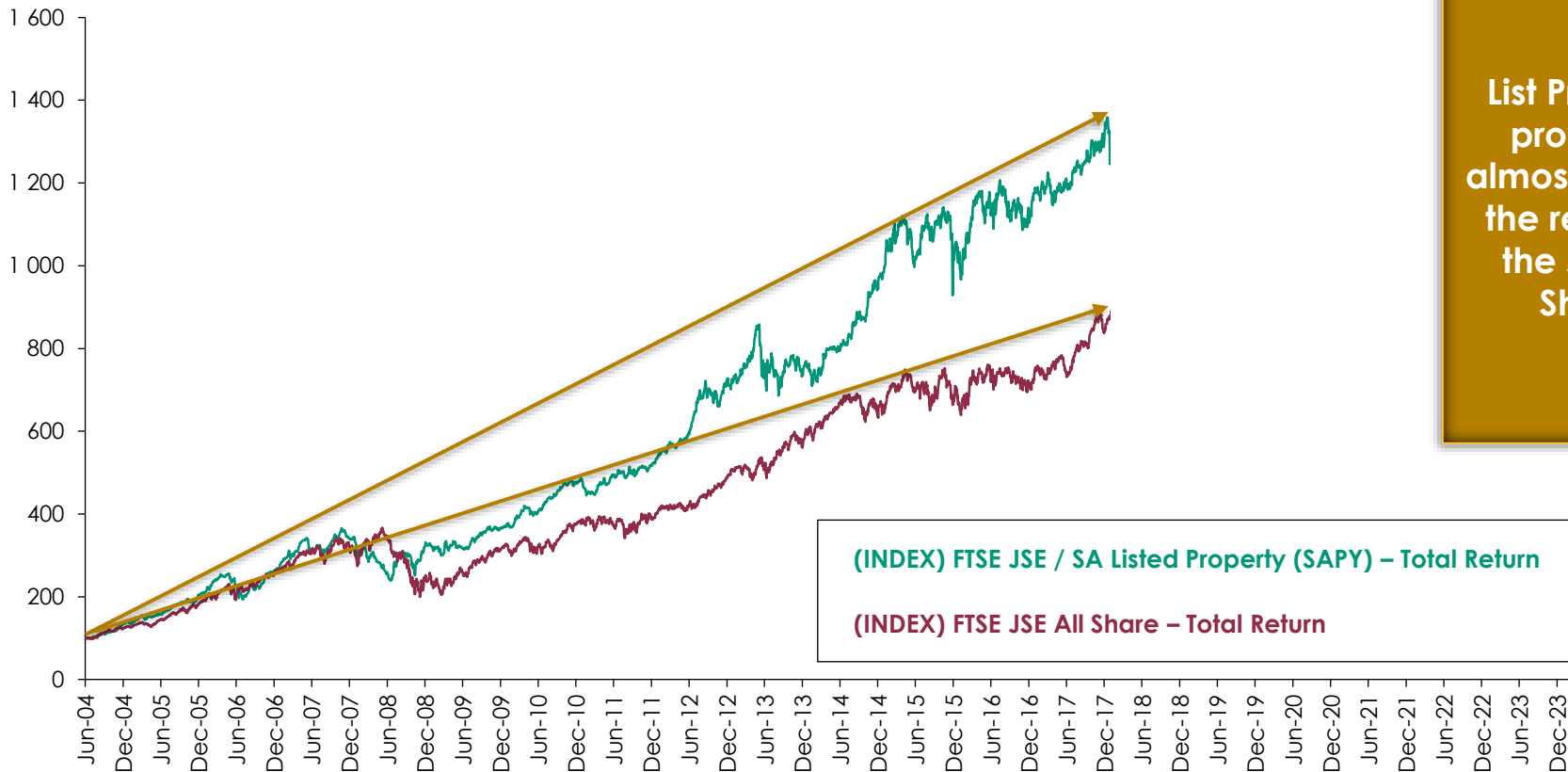
cfi.co 2023  
BEST  
ESG  
RESPONSIBLE  
INVESTOR  
WINNER AFRICA

RACE TO ZERO

SIGNATORY TO THE  
NET ZERO ASSET MANAGERS  
INITIATIVE



# UNTIL 2018 LISTED PROPERTY WAS THE MARKET DARLING...



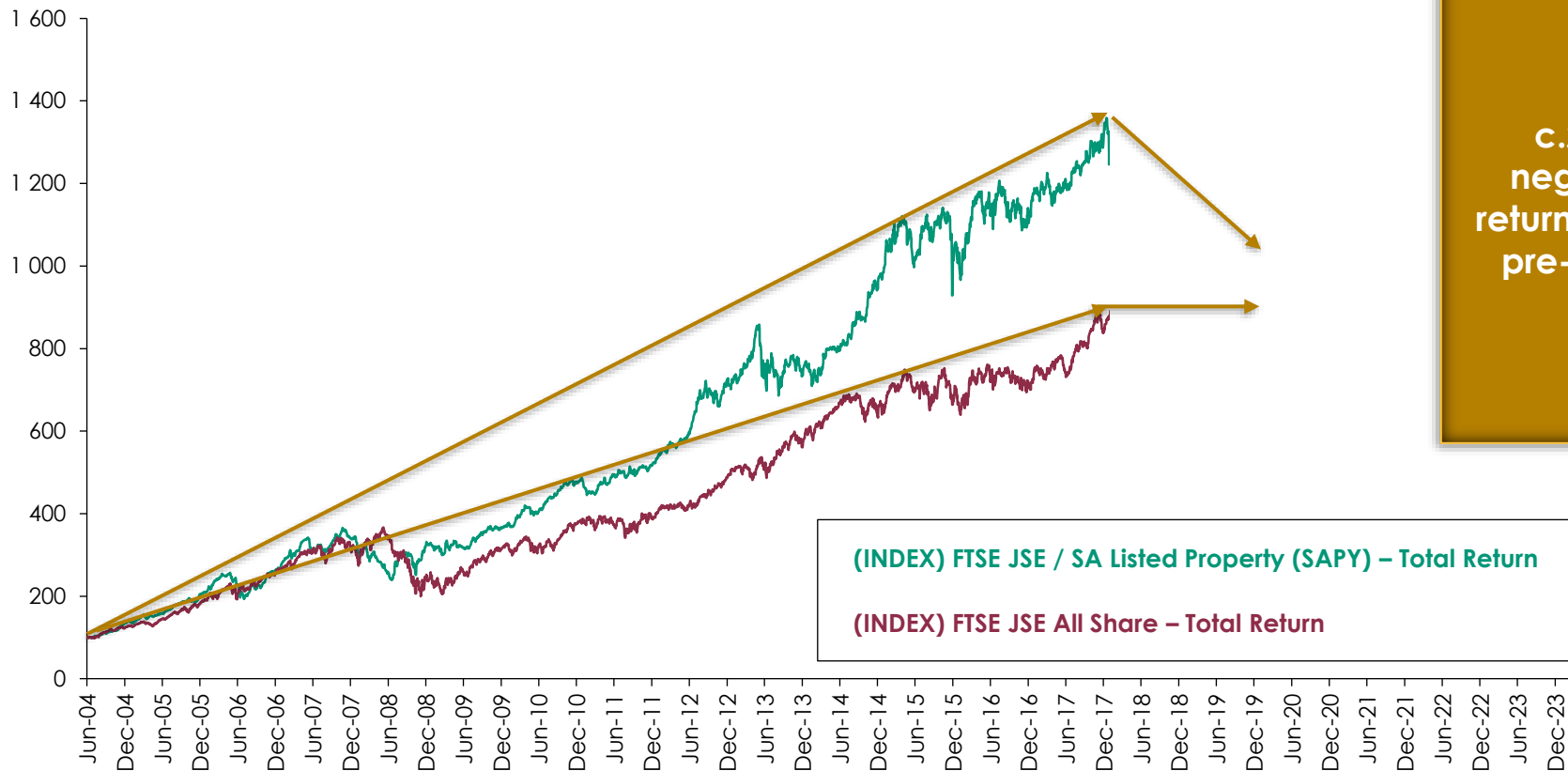
List Property provided almost double the return of the JSE All Share

(INDEX) FTSE JSE / SA Listed Property (SAPY) – Total Return

(INDEX) FTSE JSE All Share – Total Return



# ... BUT BEGAN DECLINING PRE-COVID (STRUCTURAL EXCESSES)



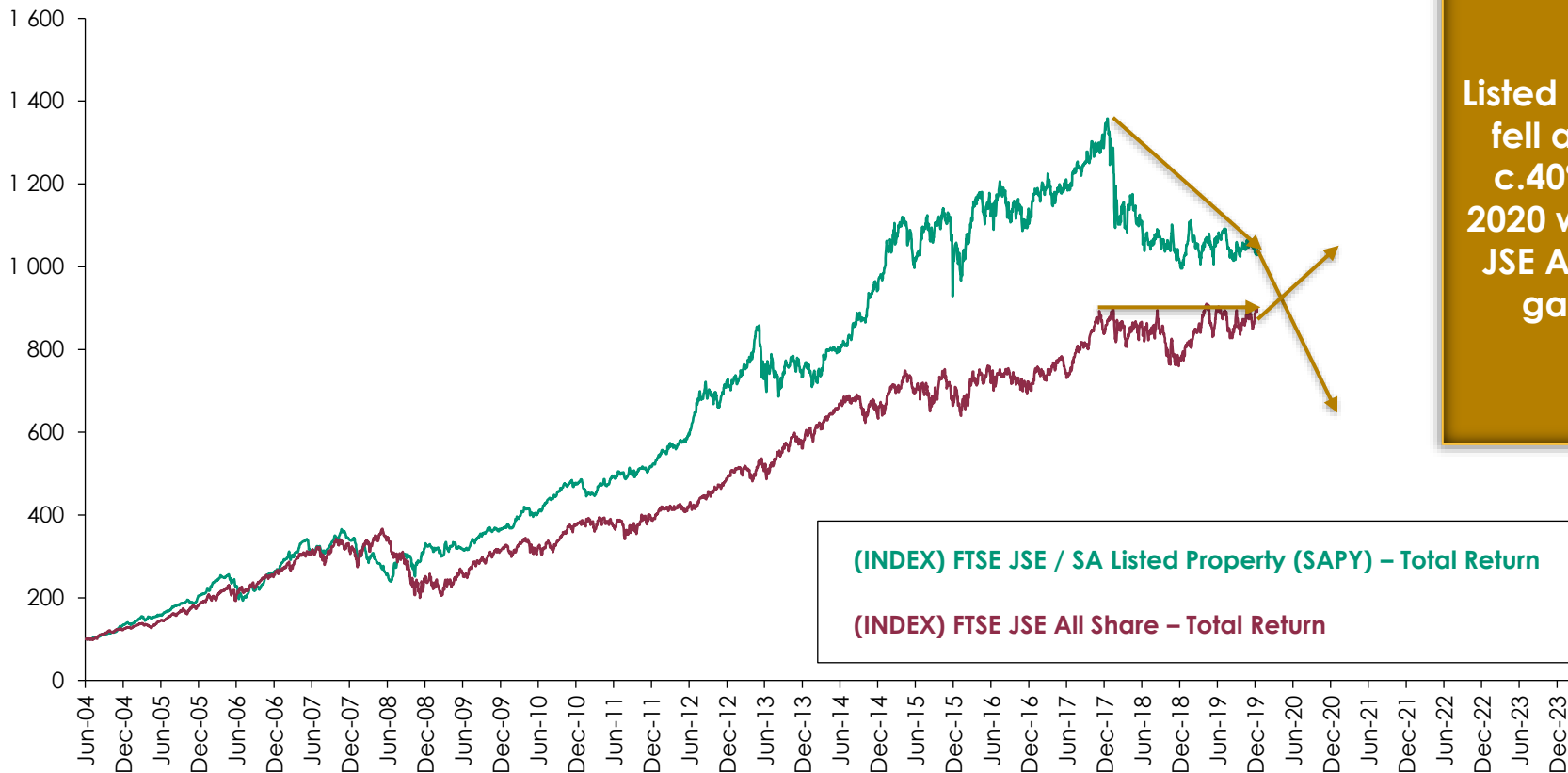
c.25%  
negative  
return 2-year  
pre-covid

(INDEX) FTSE JSE / SA Listed Property (SAPY) – Total Return

(INDEX) FTSE JSE All Share – Total Return



# LISTED PROPERTY WAS THE LOSER DURING COVID (EFFECTIVELY SUBSIDISED TENANTS AND BACKSTOP FOR BANKS) ...



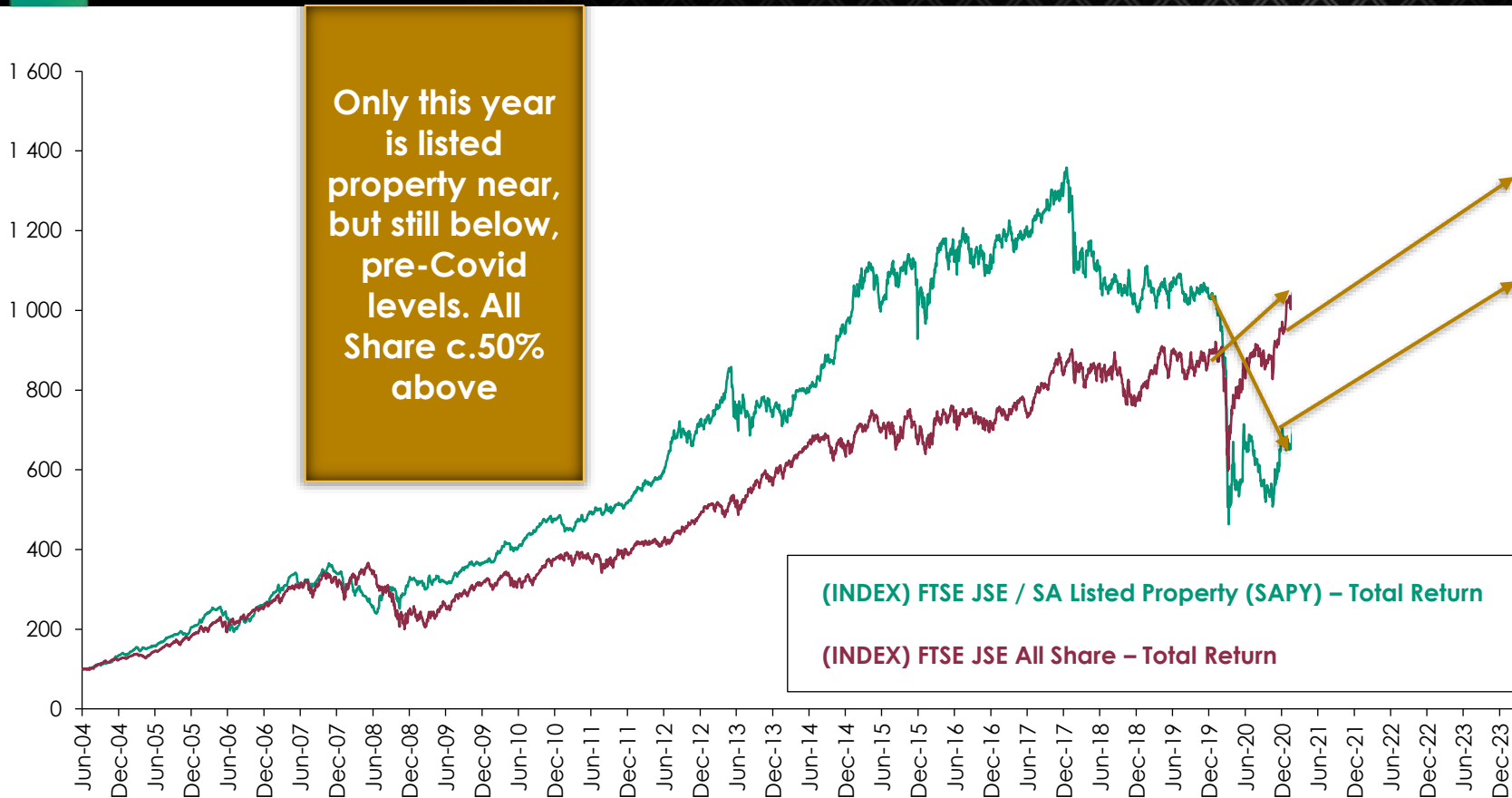
Listed property fell another c.40% over 2020 while the JSE All Share gained!

(INDEX) FTSE JSE / SA Listed Property (SAPY) – Total Return

(INDEX) FTSE JSE All Share – Total Return

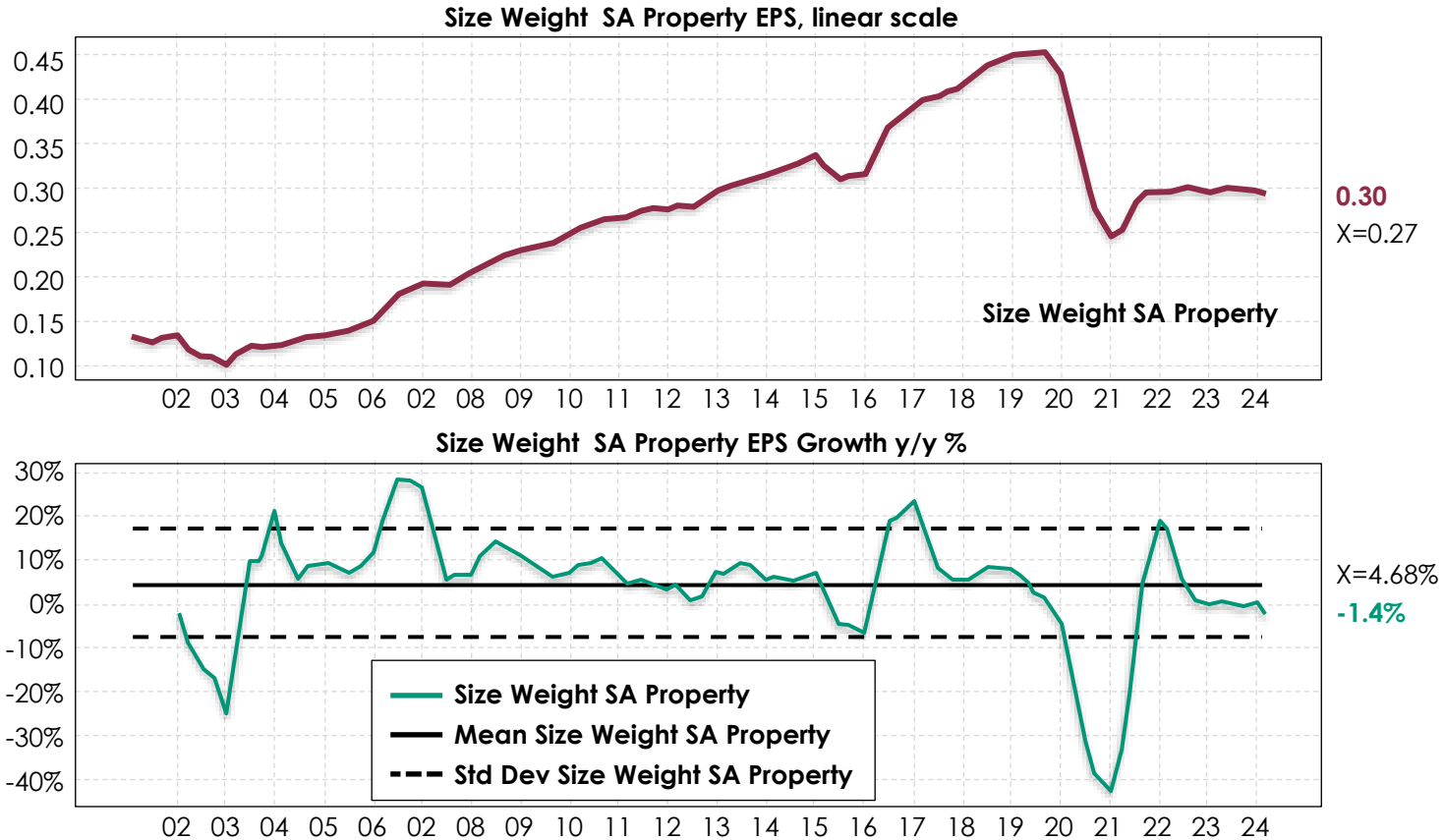


# ...AND SUBSEQUENTLY RECOVERED BY LESS ('PERMANENT' REDUCTIONS IN RENTAL BASE LEVEL, NOT GETTING IT BACK SOON)





# EARNINGS FELL SHARPLY DURING COVID AND HAVE NOT RECOVERED





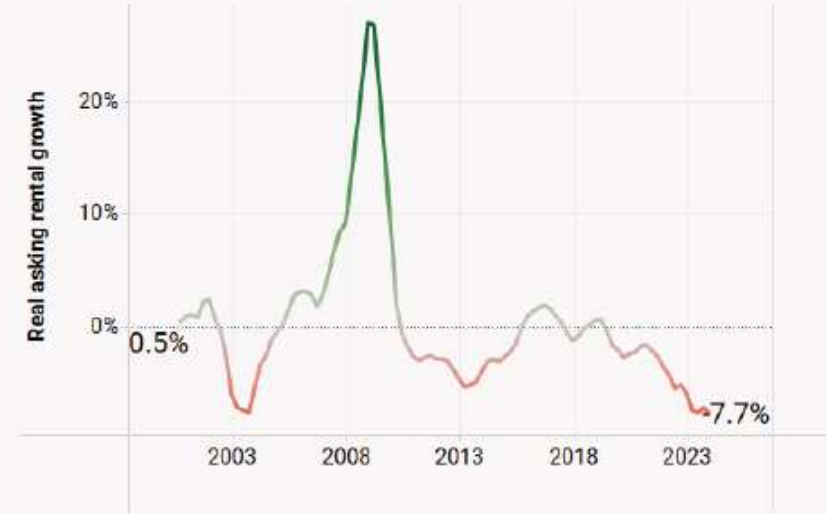
# RENTAL BASE (AND VALUATION) PERMANENTLY LOWER

## Gross Rent to Sales

### Gross Rental Growth vs. Sales Growth



Source: MSCI Real Estate



Source: MSCI Real Estate, SAPOA Office Vacancy Survey



# HOW PROPERTY INCOME WORKS

- Leases of varied remaining tenure, some 5 years or longer
- SA norm: annual fixed rental escalations (often above cpi but trend reduction)
- Only on lease expiry does rental resets to the new prevailing market level –smooths
- New rental cash flow will be lower by both the fall in market rentals and the cumulative impact of escalations
- Much of existing leases have already reverted lower, so negative reversions tapering off except in tail.

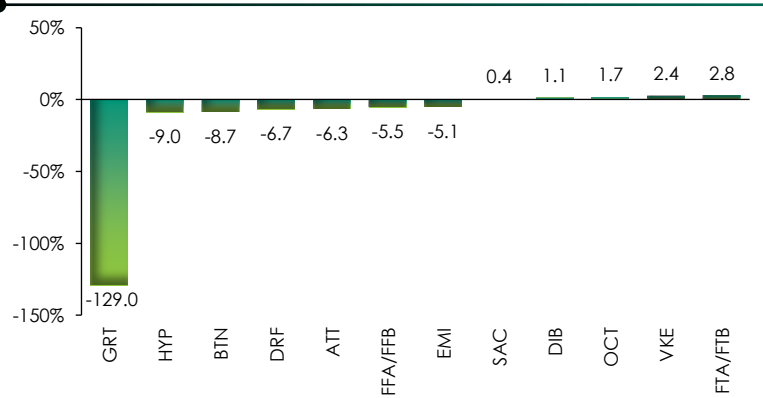






# LAST REPORT COMPANY REVERSIONS – WE THINKS THESE WILL IMPROVE

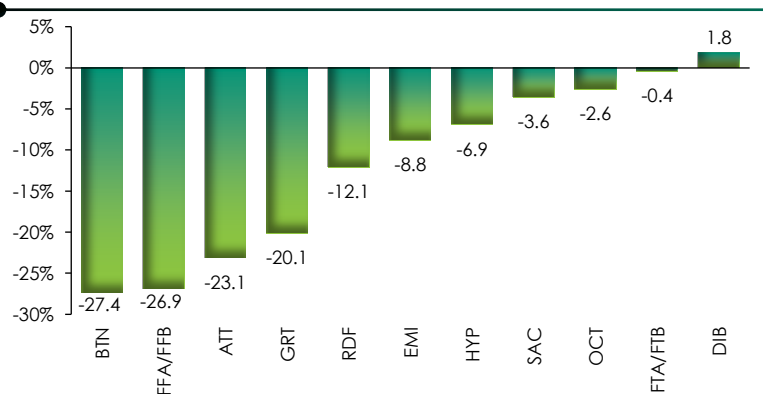
### OVERALL RENTAL REVERSION RATES – LAST REPORTED



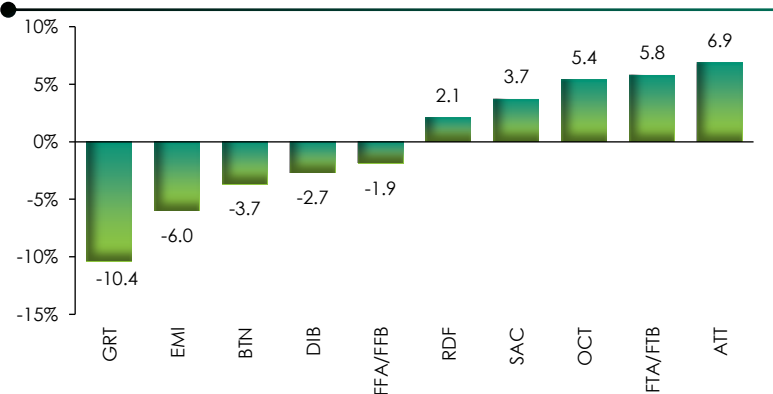
### RETAIL RENTAL REVERSION RATES – LAST REPORTED



### OFFICE RENTAL REVERSION RATES – LAST REPORTED

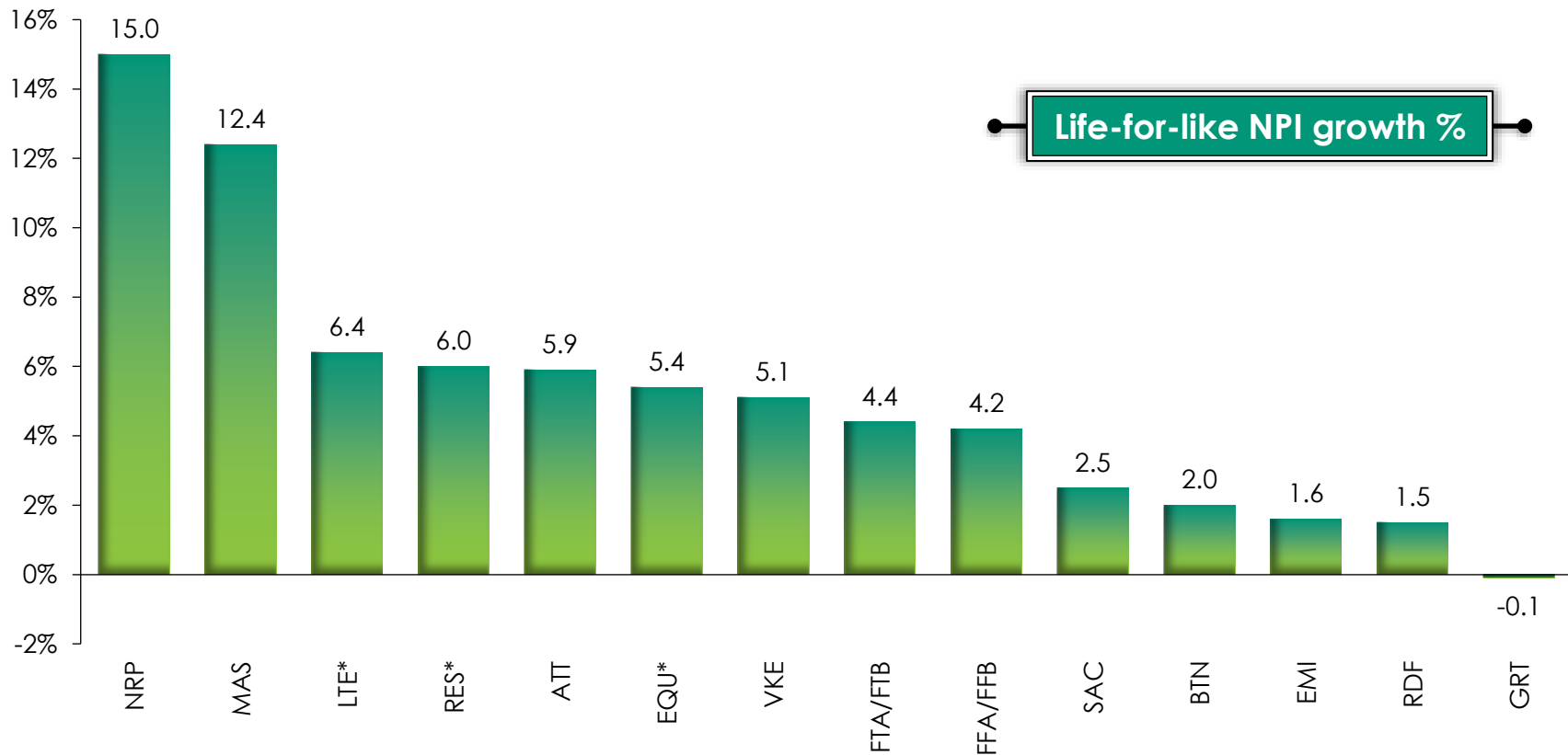


### INDUSTRIAL RENTAL REVERSION RATES – LAST REPORTED





# NET RENTAL GROWTH IS A FUNCTION OF THESE REVERSIONS BUT ALSO ESCALATIONS, VACANCY CHANGES AND OPERATING COSTS

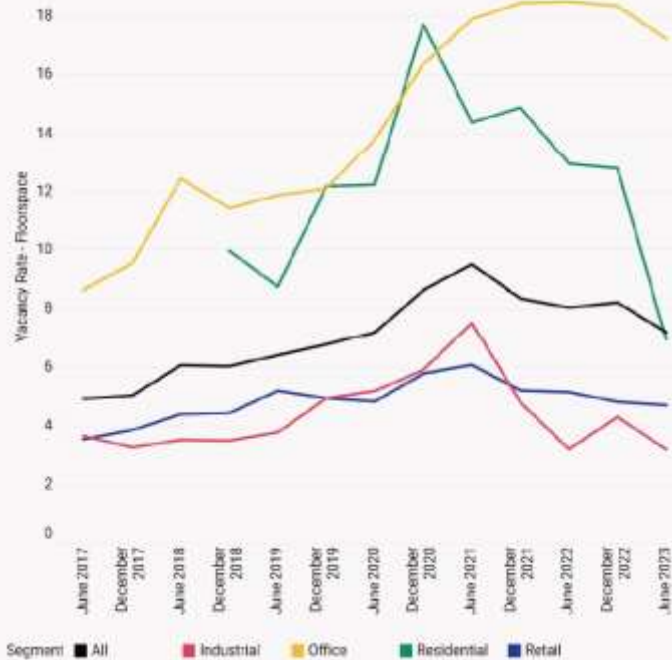




# FUNDAMENTALS HAVE STABILISED...

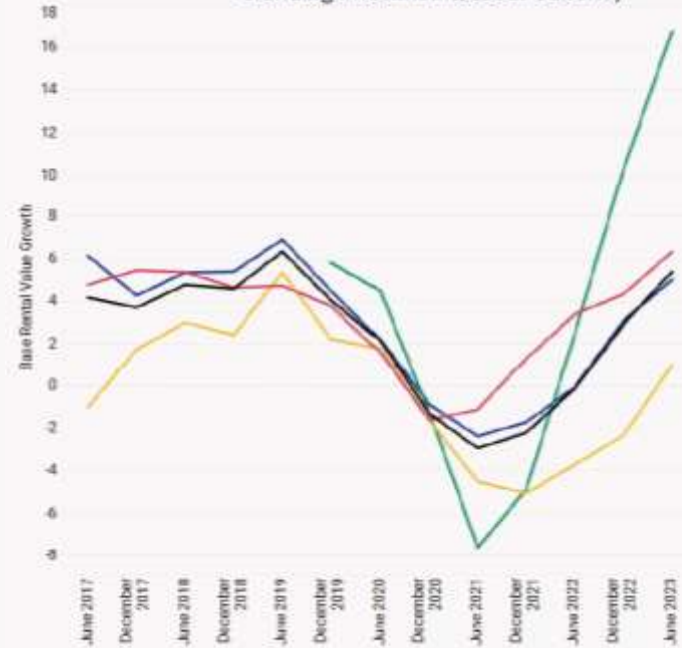
## VACANCIES PEAKED

Vacancy Rate by Sector  
Standing Investments; Local Currency



## MARKET RENTALS POSITIVE AGAIN

Base Rental Growth by Sector  
Standing Investments; Local Currency

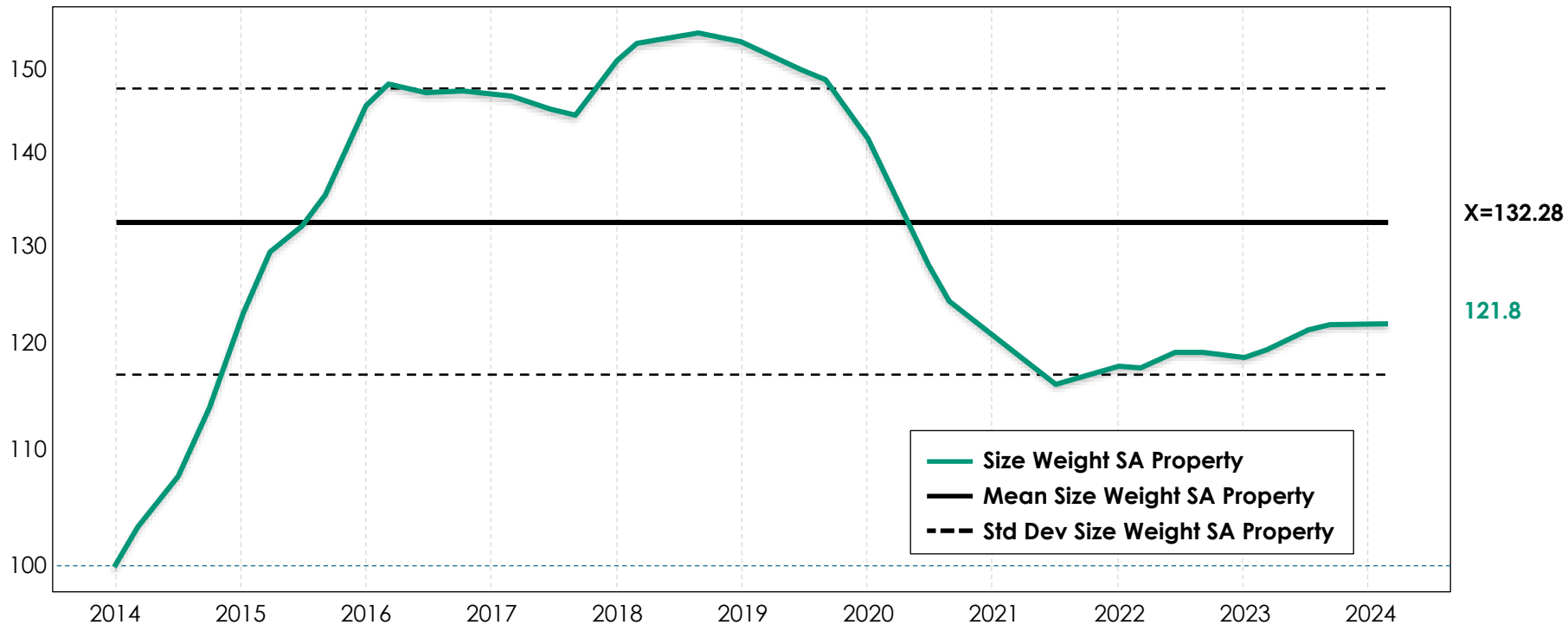


Source: MSCI



# ...AS HAVE NAVS (WE HAVE CONCERNS ON VALUATIONS)

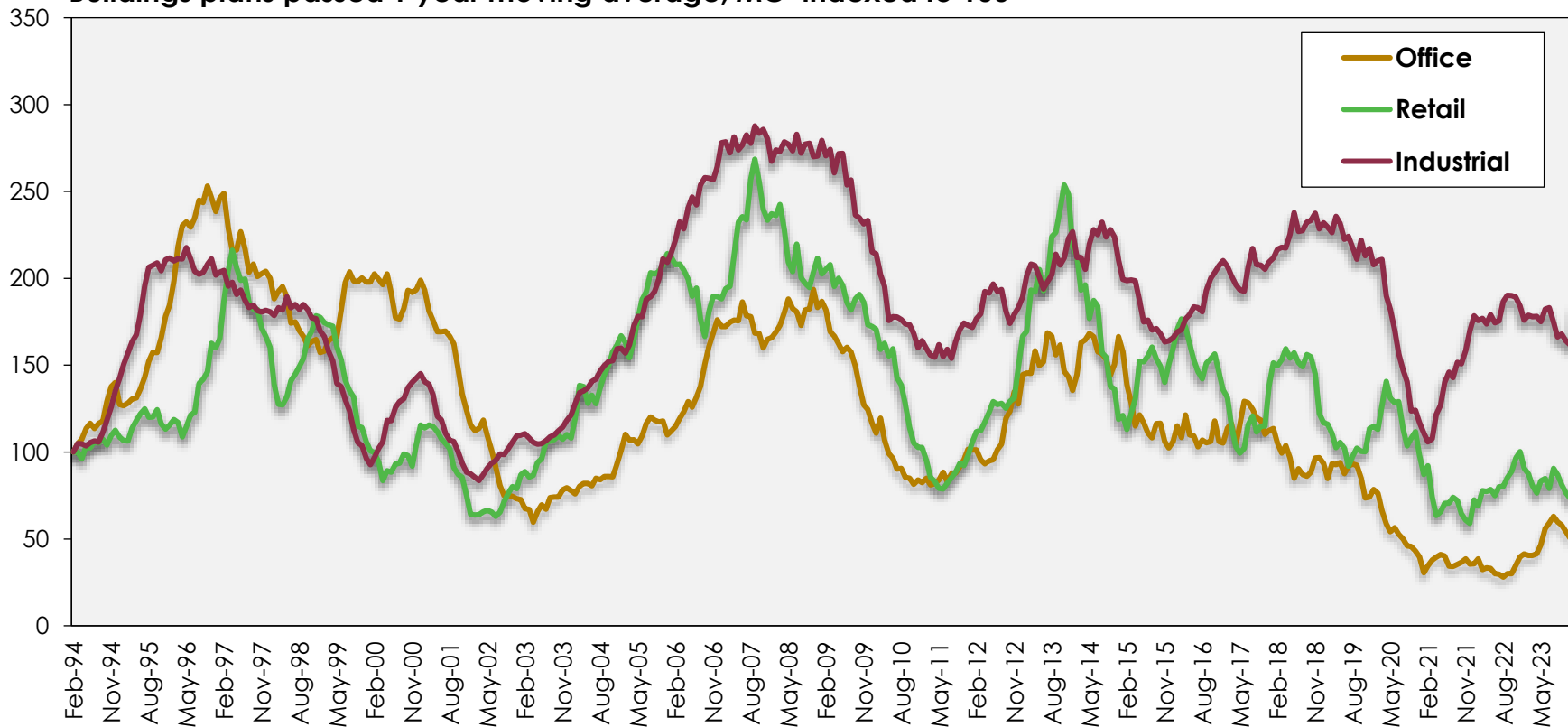
Size Weight SA Property NAV based 100 at START, log scale





# VERY LITTLE NEW SUPPLY IN THE PIPELINE (AND SOME SUPPLY LEAVING MARKET) IS SUPPORTIVE

Buildings plans passed 1 year moving average, MC<sup>2</sup> indexed to 100



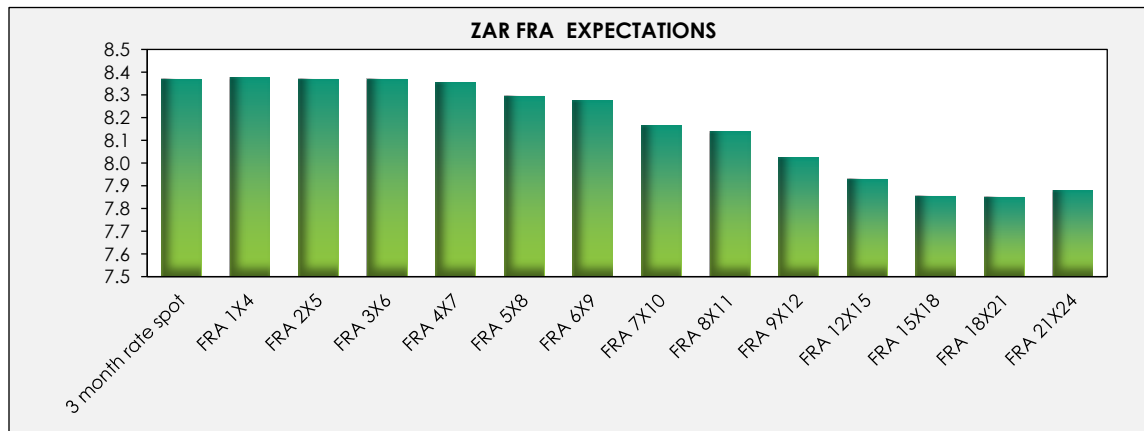
# HEADWINDS THAT DE-RAILED THE STABILIZATION ARE ABATING

## ● Loadshedding

- From → Initially landlords in effect 'subsidized' tenants, poor recovery process
- To → Recovering more, loadshedding (hopefully) peaked so fully in the base, opportunity for profit from solar

## ● Interest Rates

- From → Rising, impacting debt cost (as facilities/ swaps expired) and valuations
- To → Expectations of rate cuts, more debt now floating





# EXPECTATIONS

- Above market Improvement in earnings growth apparent from FY2025 (FY2024 results are still impacted by the headwinds)
- Property normalizes –property behaving more like it is “supposed” to behave with income growth
- Modest earnings growth which may fall short of cpi – not talking boom times – but organic growth when market used to decline is a positive





# CONCERNS



- SA economy
- Rising utility costs and rates taxes, declining infrastructure
- SA direct property valuations
- Refinancing funding of off-shore investments

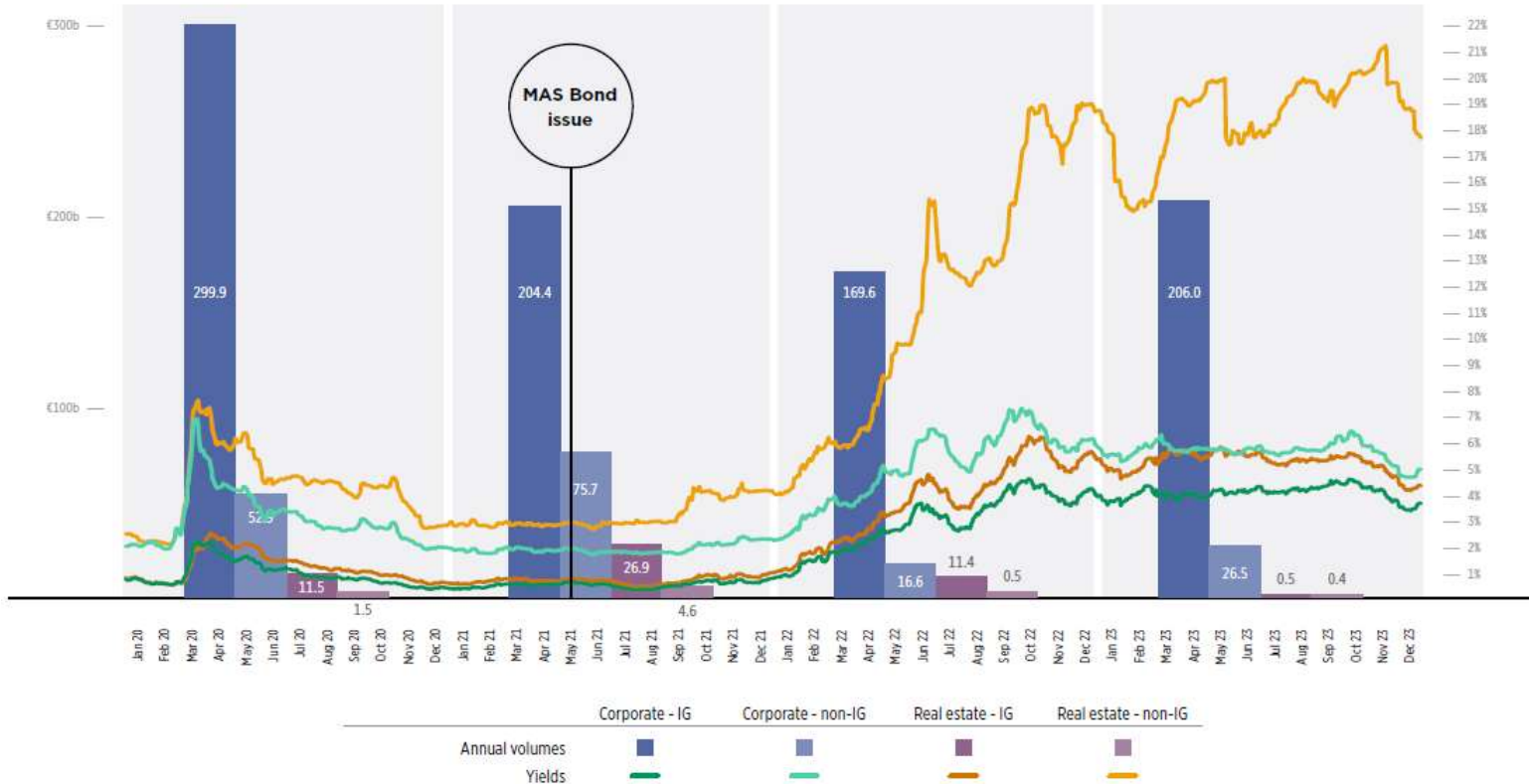




# EUROPEAN PROPERTY FINANCE COSTS AND AVAILABILITY

(inflation index on many rentals offset this impact to some extent)

Annual bond issue total volumes and yields





# SA LISTED PROPERTY (ALL PROPERTY INDEX): MORE GLOBAL AND LESS SA OFFICE THAN OFTEN PERCEIVED

Offshore Asset exposure	50%
Offshore NAV exposure	42%
% of ALPI by value non-SA property companies	26%
SA office as % of SA direct property only portfolio	21%
SA office exposure as % of ALPI assets	6%
SA office exposure as % of SA-REIT assets	11%



# VALUATION (SA PLUS OFFSHORE LISTED ON JSE, ALPI)

Forward Dividend Yield	9.1%
Forward Distributional Income yield	10.6%
Our expected total return pa(medium term)	c.14.5%
FY25 + DIPS growth expectations medium term	c.4%
FY25 + Divi growth expectations medium term	c.7%
Price to NAV	0.65%
Replacement cost to implied value (SA only)	c.>2 times
Fair (Not cheap) on spread to bonds (government bonds crowding out)	

Estimates subject to rapid change and revision



# CONCLUSION

- Stabilisation and nominal distribution growth from FY25 = return to partial inflation hedge
- Headwinds (eg rates, loadshedding) have muddied signs of the stabilization in company results
- Bad news now stale with negative fundamentals already in the base -> look forward
- Offshore holdings funding could be a drag – depends on Euro rates and debt capital markets
- Not a growth story but a stabilization story in an unloved sector

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# THANK YOU



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A money market fund is not a bank deposit account. Its unit price aims to be constant but investment capital is not guaranteed. The total return is primarily made up of interest (declared daily at 13:00) but may also include any gain/loss on any particular instrument. In most cases this will merely have the effect of increasing or decreasing the daily yield, but in the case of abnormal losses, it can have the effect of reducing the capital value of the fund. The published yield is calculated using the average of the fund's previous seven days' net income (and assumes all income was reinvested).

This figure is then annualised, which is the weighted average compound growth rate. Excessive withdrawals from the fund may place the fund under liquidity pressures. In such circumstances a process of ring-fencing of withdrawal instructions and managed pay-outs over time may be followed. Income funds derive their income primarily from interest-bearing instruments as defined. The yield is a current yield and is calculated daily. A fund of funds is a portfolio that invests in other funds which levy their own charges, which could result in a higher fee structure for the fund of funds. Some funds hold assets in foreign countries and therefore may have risks regarding liquidity, the repatriation of funds, political and macro-economic situations, foreign exchange, tax, settlement, and the availability of information. Please contact us for risks specific to each country.

The Net Asset Value to Net Asset Value figures are used for the performance calculations. The performance quoted is for a lump sum investment. The performance calculation includes income distributions prior to the deduction of taxes and distributions are reinvested on the ex-dividend date. Performances may differ as a result of actual initial fees, the actual investment date, the date of reinvestment and dividend withholding tax. Annualised returns are the weighted average compound growth rates over the performance period measured. Performances are in ZAR and as at 31 January 2024. Sources: Morningstar and Old Mutual Investment Group.

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