OLD MUTUAL Investment Group | Equity Research

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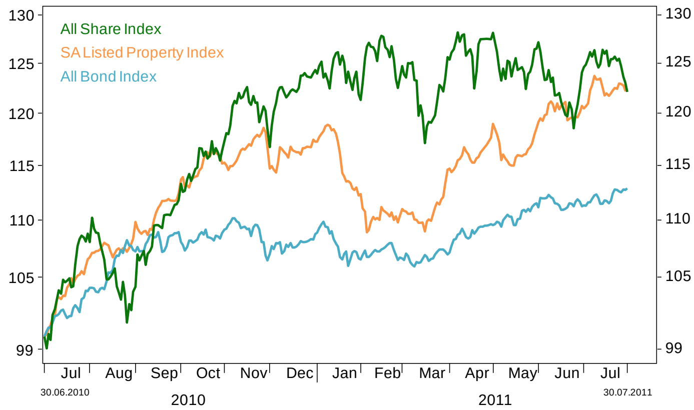
OMIGSA Comment – Evan Robins, Sector Head: Property

Property sector may get a boost from equity investors looking for shelter

In July the FTSE/JSE SA Listed Property Index (SAPY) provided a 1.6% total return, in line with the All Bond Index (1.5%). Property prices tracked the slight decline in bond yields. The FTSE/JSE All Share Index lost 2%, but the general retailer sector, which is often similar to property, was strong (+2.7%).

In July, as in previous down-markets, the sector's defensiveness was evident, with listed property prices oblivious to equity market weakness. The sector may get a boost from equity investors looking for shelter. At some stage continued equity weakness must flow through to put pressure on listed property prices, if this is reflective of a deteriorating economic environment.

JSE All Share, SA Listed Property & All Bond Indices



Source: I-Net

In August, two new property companies should list. Results season also begins and we will get an indication of conditions in the still-challenging environment.

The sector offers a one-year forward yield of 8.4%, exceeding the 10-year bond yield, and distribution growth approximating inflation. Downside operational risk has declined and funding conditions are easier. Commercial building plans passed have fallen, which will facilitate rental increases in the recovery. Vacancies are plateauing. A genuine recovery in property conditions may take longer than many anticipate, with higher electricity and rate costs constraining net rental growth, and over-rentals possibly developing in time (a key concern). The direct commercial property market remains resilient. On a long-term secular view, property is attractive as existing rents are below feasibility rentals for developments but building costs have softened.

08 – 11 August 2011 in a nutshell

Global: Global markets dipped this week amid continued US and European debt concerns, aggravated by the downgrading of the US credit rating, and threatened downgrading of the credit rating of France. The S&P 500 fell 2.28%, while its European counterpart plummeted 8.15%, and emerging markets slid 7.74%.

South Africa: The FTSE/JSE All Share Index was slightly lower, falling 0.38%. Bleak data released reflected a drop in both employment and manufacturing numbers. All sectors showed negative returns for the week, although Small Companies dipped the most, down 2.92%

Markets and Economics – Highlights

Global

- The US economy generated mixed news this week. Standard & Poor's downgraded the US credit rating from AAA to AA+ with a negative outlook, jolting global capital and commodity markets and intensifying worldwide economic pessimism. After a week of sliding markets, the outlook for the US economy got a welcomed boost as jobless claims fell to a four-month low, from 402 000 to 395 000, helping to allay fears of a new recession. However, optimism generated by the claims report was short-lived due to news of a widening trade deficit, which jumped $53.1bn, the largest since October 2008, from $50.8bn in May.
- European stocks, particularly French bank stocks, were battered by renewed fears over debt concerns, false information suggesting France might lose its top-notch credit rating, as well as speculation on the strength of French banks holding troubled Greek and Italian debt. The concern about the French banks sent shock waves through credit markets, pushing interbank borrowing rates higher and triggering a 3-month high of €4 billion in emergency overnight borrowing from the European Central Bank. Meanwhile, European regulators announced a short selling ban on financial stocks for an unspecified period in Italy and Belgium, for 15 days in France and Spain – a possible signal of lower confidence of a market recovery. These recent developments tapped into investors' worst fears of contagion from euro zone debt troubles and led European markets lower.
- Russian manufacturing contracted in July for the first time since December 2009 as slowing growth in China and the Euro area damped demand for the country's exports. The Purchasing Managers' Index fell to a seasonally adjusted 49.8 from 50.6 in June, according to HSBC. A reading below 50 indicates contraction. The weak reading may demonstrate the strong dependence of Russian manufacturing growth on the global economic cycle through Russian exports. Gross domestic product expanded 3.7% from a year earlier in the second quarter, less than the 4.1% increase in the first three months of 2011, according to the Economy Ministry.

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South Africa

- South African annual manufacturing growth slowed to 0.9% in June from 1% in May, according to Statistics South Africa, indicating a recovery in Africa's biggest economy is faltering. The median estimate of 10 economists surveyed by Bloomberg was for an expansion of 0.4%. The slower growth may ease pressure on the Reserve Bank to increase its benchmark interest rate after leaving it unchanged at a 30-year low of 5.5% this year to help spur consumer spending. The Purchasing Managers Index, an indicator of factory output, dropped to a two-year low of 44.2 in July. A reading below 50 indicates a contraction in manufacturing production.
- Despite growth in public sector jobs, South African employment numbers in July were down for the third consecutive month, according to the Adcorp Employment Index. Overall employment was down at an annual rate of 0.4% in July. This equated to annual losses of 270 504 permanent and 79 380 temporary workers. Employment declined most sharply in the mining (7.7%) and manufacturing (8.6%) sectors, in spite of sharply rising export prices for commodities and basic beneficiated manufactured products. Government employment rose by an annual rate of 1.4% in July. Restrictive and increasingly obsolete labour laws suggest that employment will continue to slide. Adcorp predicted that South Africa would lose 468 192 jobs in the remaining months of 2011 and in 2012.

Key Indicators:

Market	Index	Movement for the period		Year to Date
		%	Index Value @ 11.08.2011	% Performance Return
United States	S & P 500 (US$)	-2.28%	1,173	-6.79%
Europe	Euro Stoxx 50 (Euro)	-8.15%	2,215	-20.86%
Emerging Mkts	MSCI Emerg Mkts (US$)	-7.74%	990	-13.99%
South Africa	FTSE/JSE All Share (ZAR)	-0.38%	29,490	-8.18%
Global	MSCI (US$)	-3.43%	1,167	-8.86%
ZAR/Dollar	Rand/US $ (ZAR)	3.53%	7.19	8.70%
ZAR/Pound	Rand/£ (ZAR)	3.61%	11.66	13.05%
ZAR/Euro	Rand/Euro (ZAR)	4.86%	10.22	15.66%
JSE	Industrials	-1.20%	26,288	-13.56%
JSE	Financials	-0.40%	20,301	-6.22%
JSE	Resources 20	-1.04%	48,090	-14.59%
JSE	Small Companies	-2.92%	30,560	-9.37%
JSE	Listed Property	-2.16%	389	-2.16%
JSE	RAFI® 40	-0.29%	6,087	-8.53%
JSE	RAFI® ALSI	-0.49%	5,865	-9.31%
JSE	SWIX	-0.54%	6,238	-7.50%

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