22 July 2011

OMIGSA Comment – Evan Robins, Sector Head: Listed Property

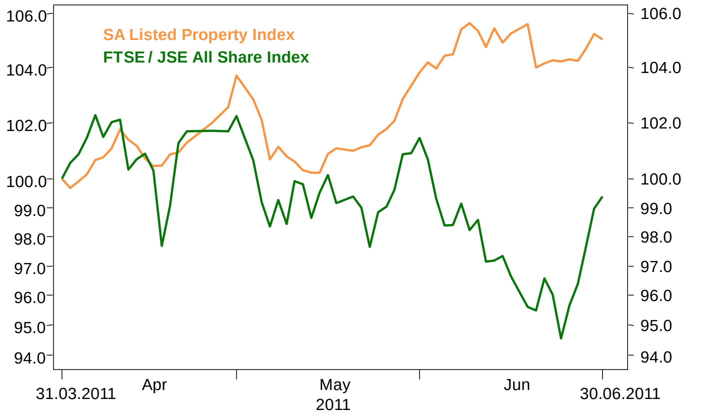
Listed property outperforms, but genuine recovery in property conditions may take longer than expected

The FTSE/JSE SA Listed Property Index (SAPY) provided a 5% total return (3.8% capital, 1.2% income) for the second quarter of 2011. This exceeded the FTSE/JSE All Share Index (ALSI)'s-0.6% return, and the All Bond Index (ALBI)'s 3.9%.

The capital gain was a function of the 37 basis point (bps) fall in bond yields. Absent the strong bond market, there would have been little capital gain in listed property. This has been the pattern over the past two years.

Property again demonstrated its defensiveness, as it barely budged when equities sold off (and recovered) in June. On a short-term measure against bonds, property yields are currently at the more expensive end of their recent trading range.

FTSE/JSE All Share Index vs. SA listed Property Index



Source: I-Net

News over the quarter on balance was unsupportive, with companies continuing to find conditions tough. Funds with high office exposure (e.g. Sycom Property Fund which reported in June) have struggled, often having to reduce rentals on net lettings.

The sector offers a one-year forward yield of 8.3%, equaling 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 materially, which will facilitate rental increases in the recovery. 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). Large capital raisings may constrain prices. The direct commercial property market remains resilient. On a long-term secular view, property is attractive as existing rents are below feasibility rentals for new developments but building costs have softened.

08 – 14 July 2011 in a nutshell

Global: Global markets improved this week in response to positive news out of the Eurozone. The S&P 500 rose 2.67%, while its European counterpart gained 2.52%, and emerging markets were up 0.70%.

South Africa: The FTSE/JSE All Share Index slipped 0.20%. The biggest winner was listed property, up 0.52%, while industrials were the biggest loser, down 1.34%.

Markets and Economics – Highlights

Global

- New data released in the U.S. may signal that its economic recovery will be restrained until the end of 2011, largely due to the shortage of auto and electronic parts from Japan after the earthquake, the damaging tornado and flooding activity, as well as the debt ceiling issue. The index of U.S. leading economic indicators rose at a slower pace in June. The Conference Board's gauge of the outlook for the next three to six months climbed 0.3% after a 0.8% gain in May. Economists projected a 0.2% rise in June, according to the median forecast in a Bloomberg News survey. Cheaper fuel costs, an easing of supply bottlenecks after the Japan earthquake and better weather may combine to help give the recovery a boost.
- European Union (EU) leaders agreed on a new bail-out package for Greece - a temporary default to ease Greece's debt burden and erect a firewall around Spain and Italy. The total official financing for the second Greek assistance package will be about €109 billion, while the private sector will provide a net €37 billion to the package. World stocks and the euro rallied following the announcement.
- China's inflation escalated to the highest level in three years in June to 6.4% year-on-year, well above the government's target of 4% for this year. However, due to tighter liquidity, slower economic growth, lower international commodity prices and adequate grain supplies, consumer prices will likely fall in the second half of the year. China, however, still faces imported inflation as crude oil prices are expected to remain high, and there will also be long-term pressures on prices due to higher labour and material costs.

South Africa

- Retail sales plunged unexpectedly by 4.7% in May, unchanged from a year earlier, suggesting that consumer spending is slowing. This is the worst annual performance since December 2009, when they contracted. Consensus forecasts had predicted a rise of 7.2% compared with May last year. Coming on the heels of news that manufacturing output slowed in May, the disappointing retail data signalled that overall growth in the economy slowed in the second quarter of this year.
- Consumer prices rose by 5% in June compared with June last year — the highest level since last March — and accelerated from 4.6% in May, according to Statistics South Africa. The main drivers of the annual increase were higher costs for rented housing, transport and food prices. During the month itself, inflation rose by 0.4%, also in line with consensus forecasts. Core inflation, which excludes food and non-alcoholic beverages, petrol and energy, quickened to 3.5% last month from 3.2% in May.
- The South African Reserve Bank has left the repo rate unchanged at 5.5%, despite expressing concern over rising inflation. In response, government bonds extended gains, pushing yields to their lowest levels in about two weeks. The Bank's Monetary Policy Committee has now left rates on hold at its last four policy meetings after a two-year loosening cycle that ended in November 2010 and saw 650 basis points taken off the repo rate, bringing it to an historic low of 5.5%.

Key Indicators:

Market	Index	Movement for the period		Year to Date
		%	Index Value @ 21.07.2011	% Performance Return
United States	S & P 500 (US$)	2.67%	1,344	6.84%
Europe	Euro Stoxx 50 (Euro)	2.52%	2,763	-1.07%
Emerging Mkts	MSCI Emerg Mkts (US$)	0.70%	1,143	-0.70%
South Africa	FTSE/JSE All Share (ZAR)	-0.20%	32,140	0.07%
Global	MSCI (US$)	2.52%	1,344	5.00%
ZAR/Dollar	Rand/US $ (ZAR)	-1.02%	6.76	2.27%
ZAR/Pound	Rand/£ (ZAR)	0.18%	11.03	6.98%
ZAR/Euro	Rand/Euro (ZAR)	0.62%	9.74	10.18%
JSE	Industrials	-1.34%	28,423	-6.53%
JSE	Financials	-0.09%	21,742	0.44%
JSE	Resources 20	0.15%	53,969	-4.14%
JSE	Small Companies	-0.61%	32,307	-4.19%
JSE	Listed Property	0.52%	388	0.26%
JSE	RAFI® 40	-0.16%	6,694	0.59%
JSE	RAFI® ALSI	-0.12%	6,458	-0.14%
JSE	SWIX	-0.04%	6,746	0.03%

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