NEDGROUP INVESTMENTS

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NEDGROUP INVESTMENTS
Property Fund
Quarter Two, 2021

Nedgroup Investments Property Fund

Performance to 30 June 2021 (‘R)	Fund[1]	Benchmark[2]	Index[3]
3 months	16.6%	11.4%	12.1%
12 months	27.6%	24.3%	25.2%

Market Overview

South Africa’s listed property sector was the top performing domestic asset class in the second quarter of 2021. With rental collection rates improving, vacancies stabilising and valuations not falling as fast as last year, investor sentiment towards listed property has been steadily improving since the last quarter of 2020. Some companies have resumed dividend payments albeit at lower pay-out ratios (a South Africa REIT is required to pay out at least 75% of distributable earnings to retain REIT status and avoid paying taxes on any income that is withheld). While there are clearly still concerns around future cash flow growth from the large mall and office landlords, given the surge in online retailing and a move to hybrid work models, investors have recognised that current valuations are already discounting the difficulties these businesses are likely to face in the future, as well as the fact that there are several property companies whose property types and business models remain relevant to their tenants and who are likely to grow their cash flows at or above inflation as economic growth accelerates in 2021.

The significant increase in the number of new COVID cases during June and the announcement by President Cyril Ramaphosa of a move to Level 4 and the imposition of further restrictions, particularly on the food & beverage industry took the shine off what was otherwise a very good quarter for the sector. The new lockdown rules are likely to be in place for longer than the 2 weeks originally laid out by President Ramaphosa given the increased number of new cases, hospitalisations and deaths recorded in the first week of July. The impact on rent collections will be significantly less severe given that most restaurants will be able to operate as take-aways during this lockdown. Some rent relief will still be provided but the impact is likely to be non-material to most of the companies in South Africa’s listed property sector.

Portfolio Commentary

During the quarter, the Fund added positions in Emira Property Fund, Investec Property Fund and SA Corporate Real Estate Fund as these companies continued to recover from the impact of last year’s lockdowns. Importantly these companies have now resumed dividend payments but still offer investors the opportunity to buy in at double-digit initial income yields. The acquisition of these companies was funded through a combination of inflows into the Fund and dividends received (the majority of investors in the Fund reinvest their distributions and so all cash flows received from dividends are effectively available to be invested).

Several of the Fund’s positions are trading under cautionary and several are likely to be taken private and/or acquired by other REITs in the sector. Tower Property Fund, which was one of the Fund’s top performers in the second quarter, is being acquired by RDC Properties for R4 per share. Although that represents a discount to Tower’s net asset value, the offer is approximately 70% above the share price at which Tower was trading just before the first cautionary announcement was made. RDC Properties has irrevocable support from Tower’s largest shareholders, including the Fund, and the deal is likely to be concluded in the third quarter of this year. The cash proceeds from the transaction will likely be invested in a number of medium and larger property companies that continue to trade well below their intrinsic values and at higher yields than Tower (at R4 per share). This should result in slightly higher distributions than are currently being forecast and increased liquidity in the Fund.

[1] Net return for the Nedgroup Investments Property Fund, A class. Source: Morningstar (monthly data series).
[2] Benchmark is (ASISA) Real Estate General category average
[3] FTSE/JSE South African Listed Property Index

The Fund has continued to see an improvement in the outlook for distributions, with distributions now expected to grow by 50% in 2021 (admittedly off the much lower base created in 2020). The second quarter distribution of 1.51c for the A class and 1.55c for the A1 class was five times higher than the first quarter distribution and twice as large as the distribution in the comparable period last year.

Top 5 winners and losers for Q2 2021:

Top contributors	Average weight	Performance contribution	Top detractors	Average weight	Performance contribution
Dipula B	7.68%	5.21%	**Grit Real Estate**	6.29%	-0.91%
Tower Property Fund	9.28%	3.26%	**Accelerate**	5.04%	-0.22%
Spear REIT	5.95%	2.30%			
Safari Investments	10.79%	2.03%			
Arrowhead B	5.23%	1.73%			

Current positioning and outlook

Very little has changed in terms of the Fund's positioning, except the addition of the three medium-sized REITs described in the portfolio commentary. The Fund continues to invest predominantly in rural and township neighbourhood and convenience retail centres; the Western Cape (with an emphasis on logistics properties in that region); warehouses and logistics properties in South Africa and the UK, and self-storage, also in South Africa and the UK. This property-type and geographic focus has led to the Fund significantly out-performing both the market (SAPY index) and the peer group in 2020 and the first of 2021. The reason for the out-performance is that the Fund, through its focus on relevant property types, has very little exposure to large malls and offices tenanted to the private sector (it does have investments in properties that are tenanted by national and local government). Mall and office valuations have come under significant pressure since the end of 2019 and this pressure is likely to persist as vacancies rise and rents fall in the face of online retailing and hybrid work models. Several very large global and South African office tenants have announced a move to hybrid models already that will see no more than 50% or 60% of their staff in offices in the future.

Based on a combination of Bloomberg, FactSet, IRESS and Counterpoint forecasts, the current one-year forward yield on the Fund is 15.5%, with growth in that income likely to match inflation over the next 2 to 3 years, although further lockdowns and the resulting lower economic growth will negatively impact that growth outlook. The current one-year forward income yield of the SAPY index, based on the same forecasts, is 8.6% while the yield on government's benchmark R2030 bond is 8.9%.

While the Fund's performance in the first half of 2021 (+23.6%) has been excellent, the prices of most listed property companies are still well below the levels in February last year and more than 30% below the re-based net asset valuations. Initial income yields are now comparable to or above the yields on government bonds even though income growth is expected to be at or above inflation in the medium-term. While volatility is expected to remain high until such time as the vaccination drive in South Africa has made a real impact, the Fund and the sector as a whole continue to offer long-term value, particularly for income-dependant investors who need to look beyond cash (and even bonds) to meet their income needs.

Disclaimer

WHO WE ARE
Nedgroup Collective Investments (RF) Proprietary Limited is an authorised Collective Investment Scheme and the representative of Nedgroup Investments Funds PLC in terms of the Collective Investment Schemes Control Act. It is a member of the Association of Savings & Investment South Africa (ASISA)..

OUR TRUSTEE
The Standard Bank of South Africa Limited is the registered trustee.
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HOW ARE OUR FUNDS PRICED
Funds are valued daily at 15:00. Instructions must reach us before 14:00 (12:00 for Nedgroup Money Market Fund) to ensure same day value. Prices are published daily on our website and in selected major newspapers.

FEES
A schedule of fees and charges is available on request from Nedgroup Investments. One can also obtain additional information on Nedgroup Investments products on our website.

DISCLAIMER

Unit trusts are generally medium to long-term investments. The value of your investment may go down as well as up. Past performance is not necessarily a guide to future performance. Nedgroup Investments does not guarantee the performance of your investment and even if forecasts about the expected future performance are included you will carry the investment and market risk, which includes the possibility of losing capital. Our funds are traded at ruling prices and can engage in borrowing and scrip lending.

Some funds may hold foreign securities including foreign CIS funds. As a result, the fund may face material risks, which could include foreign exchange risks, market conditions and macro-economic and political conditions.

A fund of funds may only invest in other funds, and a feeder fund may only invest in another single fund, both will have funds that levy their own charges, which could result in a higher fee structure.

The Nedgroup Investments Money Market Fund offering aims to maintain a constant price of 100 cents per unit. A money market fund is not a bank deposit. The total return to the investor is made up of interest received and any gain or loss made on any particular instrument held. In most cases the return will merely have the effect of increasing or decreasing the daily yield, but in an extreme case it can have the effect of a capital loss. Excessive withdrawals from the fund may place the fund under liquidity pressures and that in such circumstances a process of ring-fencing of withdrawal instructions and managed pay-outs over time may be followed. The yield is calculated using an annualised seven day rolling average as at the relevant dates provided for in the fund fact sheet. Nedgroup Investments has the right to close its funds to new investors in order to manage it more efficiently.

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