NEDGROUP INVESTMENTS

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NEDGROUP INVESTMENTS
Property Fund
Quarter Four, 2022

Nedgroup Investments Property Fund

Performance to 31 December 2022	Fund[1]	Peer group[2]	Index[3]
3 months	11.3%	17.0%	19.3%
12 months	-0.9%	-2.5%	0.5%

Market Overview

To slow the pace of rapidly rising consumer prices, central banks throughout the world started raising interest rates at the beginning of 2022. A combination of supply chain bottlenecks, increased geopolitical tensions and an energy crisis in Europe pushed global consumer price inflation to multi-decade highs, forcing central banks to respond. The US Federal Reserve has been very aggressive in its efforts to curb inflation, raising official interest rates by 425 basis points in 2022. In the fourth quarter, the Federal Open Market Committee met twice to set policy rates, raising the Federal Funds rate by 75 basis points following the conclusion of their November meeting, before slowing the pace of rate hikes to 50 basis points at their December meeting. Interest rates are expected to rise further although there is growing evidence that consumer inflation has peaked and is expected to fall towards 3% by the end of 2023. The likelihood of a recession in the US remains high, given the sharp rise in short-term interest rates and the prognosis is no different for the UK and Europe. China's economy is likely to buck the global trend and grow faster in 2023 as the country emerges from very strict COVID restrictions which hampered growth in both 2021 and 2022.

During the fourth quarter, global bond yields responded to the aggressive rate hiking by central banks. Having risen sharply since the start of the year, the yield on 10-year US Treasuries only rose by 5 basis points between September and December. In response to the 125 basis points of official interest rate hikes in the fourth quarter, the move in 2-year US Treasuries was a little more pronounced at 15 basis points. In the United Kingdom, the yield on 10-year gilts continued to fall as Rishi Sunak replaced Liz Truss as Prime Minister and leader of the Conservative Party, immediately reversing controversial economic policies announced by Truss and her Chancellor of the Exchequer, Kwasi Kwarteng, in September.

South African bond yields dropped approximately 70 basis points in the fourth quarter, despite the onset of regular loadshedding towards the end of the quarter. Consumer inflation appears to have peaked in South Africa and the South African Reserve Bank is only expected to hike interest rates by a further 50 basis points in the first quarter of 2023. Economists are expecting official interest rates to start falling again in the second half of the year as inflation moves back into the targeted range and economic growth slows in the face of a global economic slowdown and persistent loadshedding. The sharp decline in bond yields and an increase in institutional investor appetite helped fuel a rally in South African listed property securities, although most of the gains were limited to the three industry heavyweights, Growthpoint (up 29.8% in the fourth quarter), NEPI Rockcastle (up 27.2%) and Redefine (up 24.8%).

Portfolio Commentary

The Fund under-performed the peer group and the market in the fourth quarter of 2022. The under-performance during the fourth quarter was driven primarily by the Fund's large under-weight positions in Growthpoint, NEPI Rockcastle and Redefine, which together were responsible for 13.1% of the FTSE/JSE SA Listed Property (SAPY) index's 19.3% return during the quarter. It was somewhat of a relief rally, following three consecutive quarters of negative returns at the start of 2022. For the year, the SAPY index was up just 0.5%, while the Fund was down 0.9% and the peer group was, on average, down 2.5%.

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

There was very little movement on the portfolio itself as, apart from the three heavyweights, most of the stocks moved in tandem on the back of lower bond yields and despite the onset of persistent loadshedding. The total distribution for 2022 came in shy of estimates due entirely by Accelerate Property Fund's decision to defer the payment of their interim dividend, which was expected to be paid in the fourth quarter. As a result, the income return on the portfolio in 2022 was 10.0%, versus a forecast of 10.5%. Despite not receiving the Accelerate dividend in the fourth quarter, distributions for the full year were more than 15% higher than the distributions paid in 2021.

Top 5 winners and losers for Q4 2022:

Top contributors	Average weight	Performance contribution	Top detractors	Average weight	Performance contribution
Indluplace	5.60%	1.73%	**Delta**	1.85%	-0.31%
Growthpoint	4.80%	1.30%	**Investec Prop**	3.77%	-0.12%
Dipula B	8.81%	1.08%			
NEPI Rockcastle	4.09%	1.00%			
Octodec	5.00%	0.95%			

Current positioning and outlook

The Fund continues to maintain a thematic approach to portfolio construction, favouring property types and geographic locations where fundamentals remain strong or are improving. The Fund's largest single theme exposure remains to convenience and neighbourhood shopping centres in South Africa, with very little exposure to regional and super-regional shopping malls. The Fund has also maintained a high exposure to logistics properties (through Equites and Investec Property Fund) and self-storage properties (through Stor-Age), while the large position in Spear maintains the Fund's above-average exposure to the Western Cape as a region. The Fund has very little exposure to the UK and Western or Eastern Europe, where rising discount rates are likely to put significant downward pressure on property values over the next 12 to 18 months.

The Fund's exposure to residential property in South Africa is also relatively high. As home ownership becomes increasingly less affordable in the face of rising interest rates and utility costs, rental demand for well-located residential properties is likely to increase, reducing vacancies and driving up market rental levels in the medium-term.

The Fund's overall exposure to office remains below the market average and is expected to remain at these lower levels given the sector's declining market rentals which are expected to persist for the next 2 to 3 years, despite more employees returning to an office environment.

The Fund's geographic exposure remains heavily weighted towards South Africa (79%) versus the SAPY index weight of just 50%. The SAPY index weight to South Africa has increased since the end of last year following the exclusion of EPP and Industrials REIT from the index and the inclusion of Fairvest into the index. The relative under-performance of the UK-centric companies in the SAPY index has also seen the SA exposure in the benchmark increase from below 50% at the start of the third quarter.

This approach to portfolio construction, favouring relevant themes and property fundamentals over the size and make-up of the various market benchmarks, means the Fund can and often does look very different to the market and the peer group. This differentiation has contributed to the Fund's significant out-performance since 2020 as the pandemic accelerated the rapidly emerging trends of online shopping (negative for large shopping malls but positive for logistics and self-storage properties) and changing office behaviour (work from home and hybrid models).

Based on a combination of Bloomberg, FactSet, IRESS and Counterpoint forecasts, the current one-year forward yield on the Fund is 11.5%, with growth in that income likely to approximate inflation over the next 2 to 3 years. Distributions are likely to decline moderately in 2023 because of declines in the dividends paid by Dipula B and Fairvest following corporate restructurings during 2022. Although the restructurings are dilutive to profits and dividends in 2023, they do position the companies for stronger growth beyond 2023. The current one-year forward income yield of the SAPY index, based on the same forecasts, is 8.8% while the yield on government's benchmark R2030 bond is 9.8%.

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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