OFFSHORE INVESTMENT

Going big on global property

Three new offerings aimed at cashing in on undervalued global real estate markets head for the JSE's ETF platform

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● Looking for a hedge against the rapid implosion of South African earnings?

Then it may be time to take a fresh look at the JSE's growing pool of exchange traded funds (ETFs) that invest in offshore real estate markets.

Cape Town-based boutique property asset manager Reitway Global, in partnership with investment administrator Prescient Fund Services, is listing three new global property ETFs early in June.

Reitway Global CEO Greg Rawlins says offshore real estate investment trusts (Reits) took a big hit last year on the back of higher interest rates, which pushed up property owners' debt funding costs.

"So investors ran scared. That led to an indiscriminate sell-down of global real estate stocks, which has created a huge value opportunity in international Reit markets."

Rawlins, who founded Reitway Global 11 years ago, refers to Bloomberg data which underscores the value proposition on offer relative to global equities. At end-March, the S&P 500 index of global equities was trading 3.1% above its historic 10-year mean p:e ratio. In stark contrast, the FTSE Nareit real estate index was trading 20.5% below its 10-year mean price to funds from operations ratio, which is the equivalent measure used to value property stocks (see table).

"This implies that general equities are still overvalued while listed property is undervalued," says Rawlins. "So if ever there was a good time to invest in global

REITS RELATIVE TO EQUITIES

March 31 2023

Relative price ratio	S&P 500	GPR 250 Reit index
Historic 10Y mean	19.1 P/E	17.6 P/FFO
Current	19.7 P/E (+3.1%)	14 P/FFO (-20.5%)

Source: Bloomberg

Reits, it's now."

Besides, global Reits offer South Africans the benefit of diversification and scale. There are about 1,500 listed Reits globally that invest in close to 30 subsectors. That compares to the JSE's 30-odd domestic Reits that are largely exposed to three key real estate sectors: office, retail and industrial/logistics.

He says: "Investors have such a broad universe of choice offshore that investing in South Africa-focused Reits only is not compelling from a relative risk-return point of view."

A tie-up with Prescient, a so-called white-label administrator, has paved the way for smaller players to enter the ETF fray. Rawlins says that until now the platform, much as collective investment schemes (or unit trust funds), was initially dominated by large institutions.

He says the advent of these white-label administrators has opened the universe to niche offerings. "It will similarly be a big game-changer for the ETF market."

Though the global Reit sector has performed poorly over the past 18 months, Rawlins says it will be foolish not to allocate a portion of your investment portfolio to the asset class, given its long-term outperformance of general equities.

According to Bloomberg, in the 25 years to April 3 the GPR 250 Reit index delivered an annualised total return of 7.5% vs the MSCI world index's 6% (see graph).

So how do Reitway's new ETFs differ from the JSE's other offerings?

Rawlins says the latter mostly track existing indices such as the S&P top 40 global property index. In contrast, Reitway has created three of its own indices in collaboration with Amsterdam-based benchmark administrator Global Property Research (GPR).

An ESG-biased index, a diversified index and a concentrated, high-performance index were developed. The last-mentioned is more volatile than the other two and therefore aimed at investors with a higher risk appetite.

"We used GPR's flagship liquidity-based GPR 250 Reit index, which has historically outperformed other real estate indices, as a starting point and tweaked it to our liking," says Rawlins.

Though ETFs are generally viewed as a more passive investment than actively managed unit trusts, given that they track a particular index, he notes that ETFs are becoming increasingly performance driven.

"When ETFs were first introduced globally, the key attraction was cost savings. But the lower fee structure is now a given. The second wave of ETFs coming to the market is now also focusing on performance."

He stresses that global real estate is not one homogeneous asset class. "Individual subsectors and geographic locations have different drivers. That's why it makes sense to invest in ETFs run by specialist operators with intimate knowledge of the global Reit market."

Rawlins cites US-founded Simon Property Group as an example. Six years ago, when physical retail stores were still in vogue, the market cap of the world's then biggest retail-focused Reit sat at $50bn.

The company's value has since shrunk to $33bn. Over the same period, logistics-focused Reit Prologis, which is a major beneficiary of the shift to online shopping, saw its market cap balloon from $30bn to nearly $112bn.

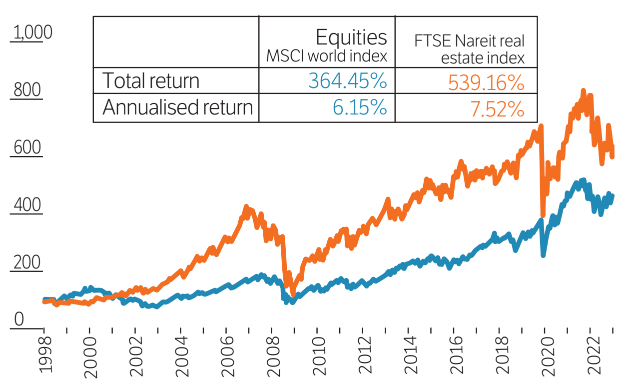
Rawlins is placing his bets on nontraditional real estate such as data centres, wireless communication infrastructure, gaming/casinos, self-storage, health care, residential (US in particular) and logistics.

"We're not going near general office buildings and remain significantly underweight in retail property," he says.

In terms of regional exposure, Rawlins is "substantially" overweight to the US and "significantly" underweight to the UK and Europe.

REITS TRUMP GENERAL EQUITIES

25 years to April 3 2023



Source: Thomson Reuters

He says: "The US offers huge choice and there are signs that it's getting on top of inflation and nearing interest rate peaks. However, the UK and European economies potentially face further pressure from still-rising inflation and interest rates."

Rawlins also likes Japan's Reit sector, which has a history of relative outperformance during global economic downturns.

Other fund managers seem to agree that global Reits are now a better bet than their local counterparts. Anchor Capital says in its latest quarterly review that uncertainty around the domestic earnings outlook is weighing on the local Reit sector.

The report reads: "Over the past 12 months, the average South African property share has gone broadly sideways, with returns coming from distributions rather than capital. We expect the outcome for the next year to be similar, as South African property companies are stuck in a no-/low-growth environment."

Jacques de Kock, quantitative analyst and portfolio manager at discretionary fund manager MitonOptimal, says while investors should have exposure to both local and offshore property for diversification reasons, the general outlook for global Reits appears more compelling.

"Historically, real estate investment did well when interest rates started to level off, bond yields reverted downward, and economies started to grow again. We believe within the next three to six months the situation could change, and the timing will be right to climb back into offshore Reits."

De Kock says the domestic listed property sector, on the other hand, still faces plenty of bad news, including the potential for further rate hikes, a weaker rand and ongoing load-shedding.

He says: "Though local Reits are trading at attractive yields, global Reits offer more scope for growth." x