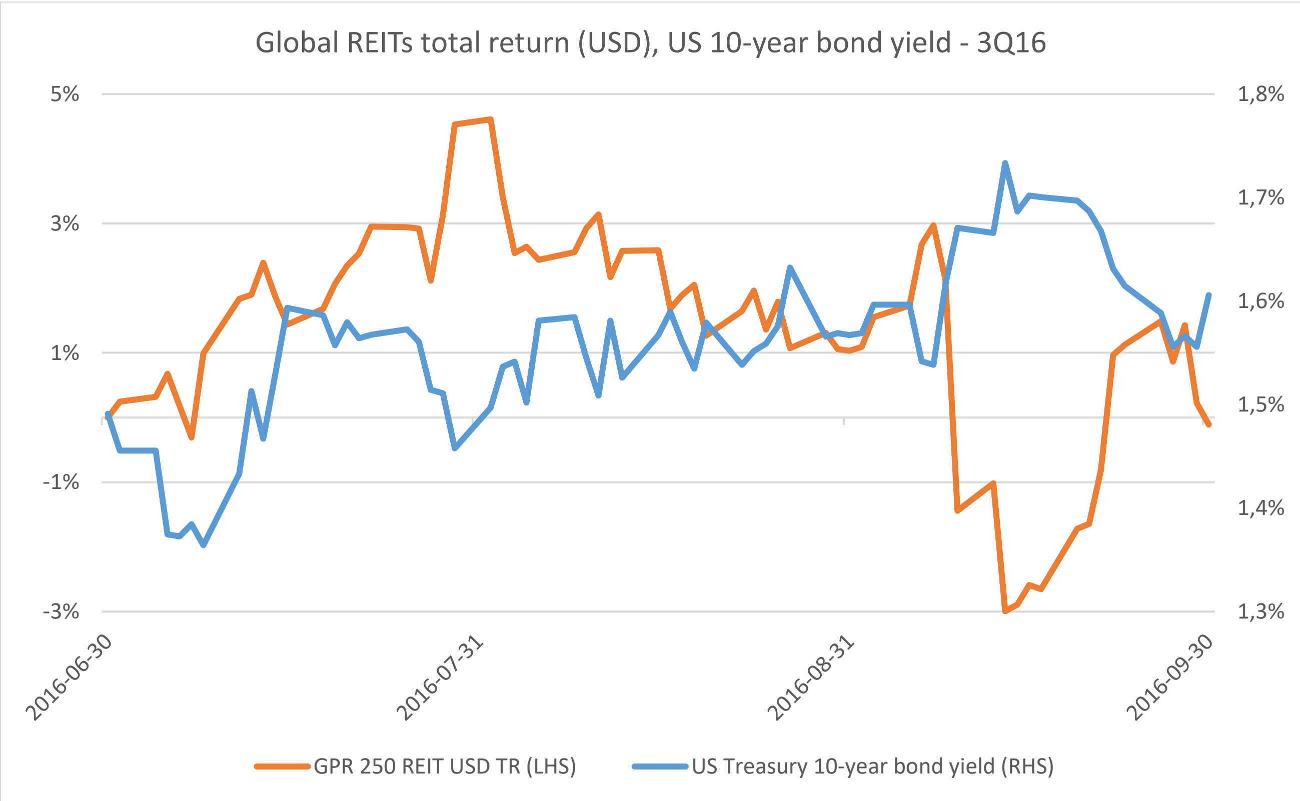
REITWAY REVIEW – EDITION 14

For quarter ended 30 September 2016

Global REITs, in US Dollar (USD) total return (TR) terms, retreated by 0.1% in 3Q16. This brings the year-to-date (YTD) TR of the global REIT market to 12.6%.

Unsurprisingly, once again it was a potential US Federal Reserve (Fed) rate hike that saw bond yields spike and the global REIT market drop in the period leading up to the Fed's 16 September policy interest rate decision. As indications became clearer that the Fed was not going to hike in September, bond market yields compressed and global REITs recovered in concert. The following chart of global REITs versus the US 10-year bond yield during 3Q16 reflects this.



Source: Thomson Reuters Datastream, Reitway calculations

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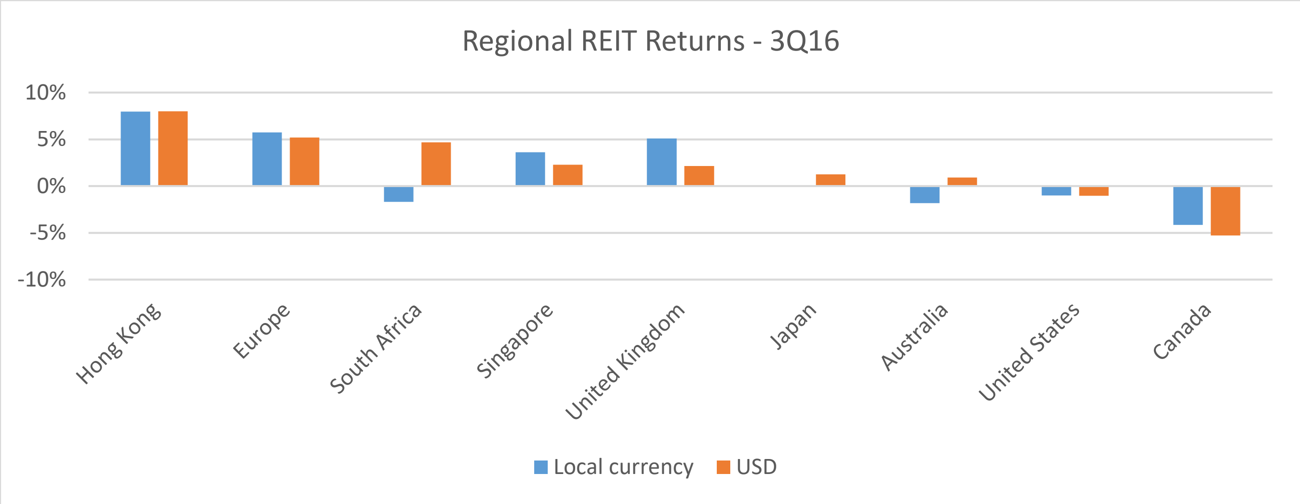
The chart below shows the TR for the respective regional global REIT markets in 3Q16.



Source: Global Property Research, Reitway calculations

Hong Kong (8%), Europe (5.2%) and South Africa (4.7%) were the top performing markets during 3Q16 in terms of USD TR performance. The European market and UK REIT markets recovered off Brexit lows during the quarter, with the Euro holding fairly steady relative to USD. The British Pound (GBP), however, lost further ground against USD. In South Africa, even though REITs achieved negative returns in local currency, the strengthening of ZAR resulted in solid USD performance for SA REITs. After a strong 1H16, Canadian and Australian REITs underperformed during 3Q16.

PORTFOLIO PERFORMANCE – 3Q16

The Reitway BCI Global Property Fund outperformed its benchmark by 1.96% during the third quarter of 2016, taking the fund's rolling 1 year return to 18.85% in USD terms.

For the quarter, the fund benefitted from superior stock selection in most regions. For example, our Australian holdings (LendLease and Mirvac) gained 15.78% over the quarter compared to 0.90% for the Australian sub-index of the benchmark.

Our objective is to remain disciplined and opportunistic in terms of REIT price movements relative to fundamentals, with the aim of generating alpha and wealth for our clients over the long term. Our performance versus our peers can be seen below.

Reitway BCI Global Property Fund vs Peer Group Average (ZAR)

	1 year to 26/09/16	2 years to 26/09/16	3 years to 26/09/16	4 years to 26/09/16
Reitway BCI Global Property Fund	16.81%	20.21%	19.41%	21.85%
Peer Group Average (Morningstar)	11.16%	18.32%	18.72%	20.77%
Excess Return	5.65%	1.89%	0.69%	1.08%
Peer Group Rank	1/9	2/7	3/7	1/6

Source: MoneyMate

Note: all performance figures are denominated in ZAR. Periods longer than one year are annualised.

REIT MARKET OUTLOOK

Asia

As much as anywhere else globally, the Japanese REIT (J-REIT) market continues to be a reflection of central bank policy. Over the last year, J-REITs have been 90% inversely correlated versus the Japanese 10-year government bond yield, i.e. as a group, J-REITs effectively serve as proxies for Japanese bonds.

In terms of the Singaporean REIT market, according to Macquarie research published in August 2016, Singapore office rents were on the cusp of a turnaround. Their latest estimates suggest an even more positive outlook.

Australia

According to J. P. Morgan, the highlight of the latest earnings season has been the robust performance of residential Australian REITs (A-REITs). Our A-REIT holding, Mirvac (MGR), has substantial residential operations. Their latest results revealed that they achieved the "earnings trifecta," i.e. higher sales, increasing prices and expanding margins. Earnings visibility is also great, with MGR having achieved record pre-sales.

Canada

The Canadian REIT (C-REIT) market has experienced decelerating organic growth, with a deteriorating outlook as well. C-REIT earnings growth trends and expectations can be seen below.

Exhibit I: "Trend Line" growth in earnings/unit, quarterly - Q1/97 to Q4/16E

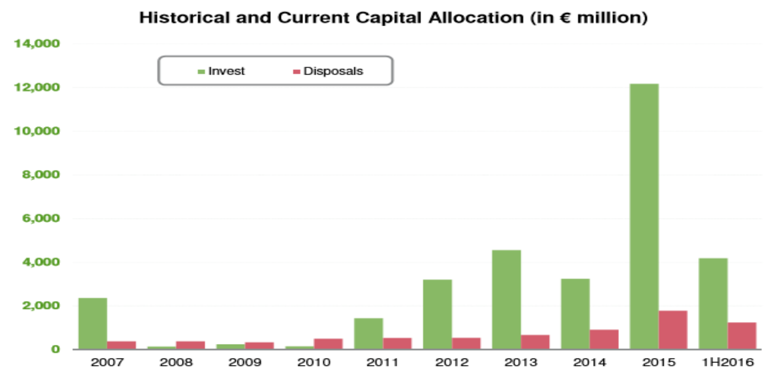
Source: RBC Capital Markets estimates

The outlook for slower growth can be attributed to softer macroeconomic conditions, particularly in the "oil provinces." Even though the Canadian REIT market has recovered somewhat from its horrific performance last year, investors can't escape the fact that the decline in oil prices since 2014 has had a real economic impact, particularly in certain Canadian provinces. RBC Canada expects continued divergence in provincial economic performance, which is likely to remain a vital consideration in terms of investing in Canada.

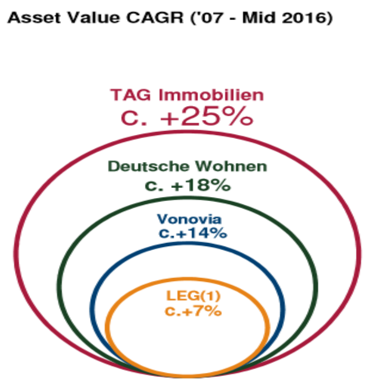
Europe

Green Street Advisors research indicates that there continues to be exciting internal growth prospects in the German residential sector. Low supply, due to replacement costs being higher than current property values, will continue to drive bargaining power for landlords.

External growth has also been important for German Residential companies. The graphic below (left) shows the quantum of merger and acquisition activity in the industry over the respective periods, alongside an illustration of asset value compound annual growth rates for selected German Residential companies over the stated period.



(1) LEG CAGR growth in assets since 2010.
Source: Company disclosures, Green Street Advisors

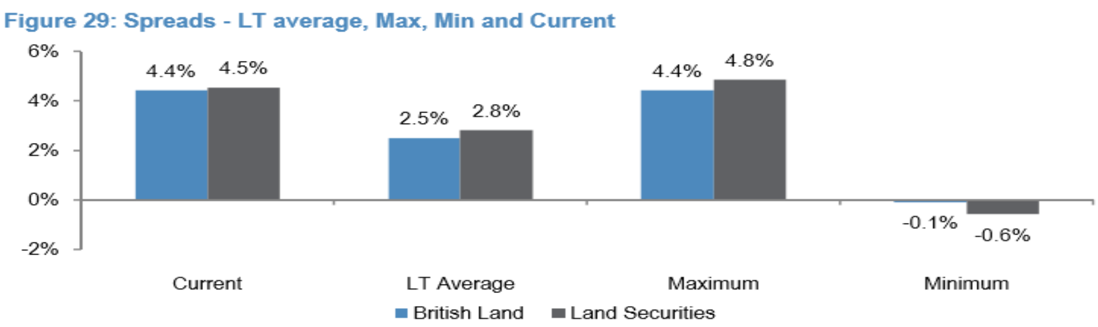


Note: CAGRs exclude re-valuation & capex contributions.

It is likely that consolidation in the German Residential space will continue, as companies take advantage of the attractive spread between acquisition yields and low financing costs.

United Kingdom

There may appear to be value in UK REITs. British Land and Land Securities, for example, are trading at or near record spreads to the gilt.



Source: J. P. Morgan research

However, 2017 UK GDP growth expectations have declined and Brexit uncertainty remains. UK REITs are less bond-like than REITs in other regions. This means that the bond yield compression that is generally associated with economic weakness provides less of a cushion to UK REIT prices compared to REITS in other regions. This does not bode well for UK REIT outperformance in global terms. As we have previously stated, the less economically-sensitive UK REIT sectors are likely to be the most robust.

United States

The IMF recently lowered global/US growth forecasts. Growth has been lagging largely due to a decrease in the amount of investment being undertaken. This is apparent in the US property market, where the high level of construction inflation is crimping supply.

However, this has generally been a positive for US REITs, with landlords being able to capitalise on strong demand in order to persistently apply robust rental increases where tenants have less bargaining power due to the abovementioned limited supply growth. The result is that US REITs are expected to achieve funds from operations (FFO, a proxy for free cash flow) growth of 7%-8% in 2016.

As of 1 September, US real estate was carved out of the Financials sector (which now includes only banks and insurance companies), to became the 11th standalone Global Industry Classification Standard (GICS) sector. This is the first time a sector has been added since GICS creation in 1999.

According to our discussions with US REIT experts, this has two main implications. Firstly, generalist equity investors may increase their weights to REITs, although some may opt not to. More importantly, however, is the fact that REIT stock selection will become more important as awareness of the asset class continues to increase. As investors who, first and foremost, consider ourselves to be bottom-up stock pickers, we see the abovementioned environment as one in which we at Reitway can add the most value.

Conclusion

Although our investment performance is subject to movements in the global REIT market, we strongly think that our benchmark agnostic and opportunistic approach enables us to generate superior returns. We are also of the view that fund managers spend too much time bemoaning market volatility. We need to embrace uncertainty as a market constant and use market movements opportunistically. Due to the fact that we value our investors, we aim to consistently apply the aforementioned principles at Reitway in order to generate alpha and create wealth for our clients.

Regards,
The REITWAY team

For more information about the performance of our funds and investment methodology, please visit our website at www.reitwayglobal.com.