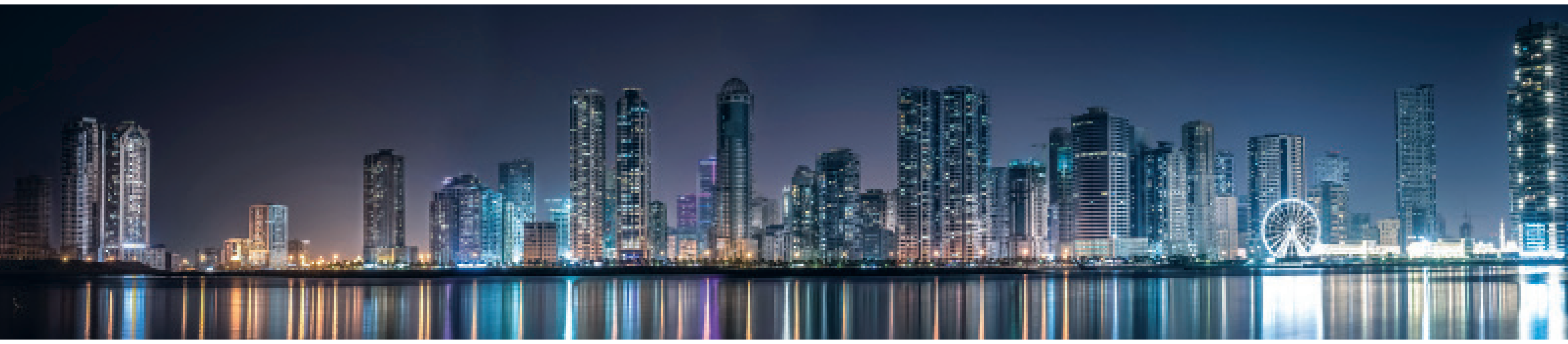
CATALYST
FUND MANAGERS

GLOBAL LISTED REAL ESTATE REPORT SEPTEMBER 2019



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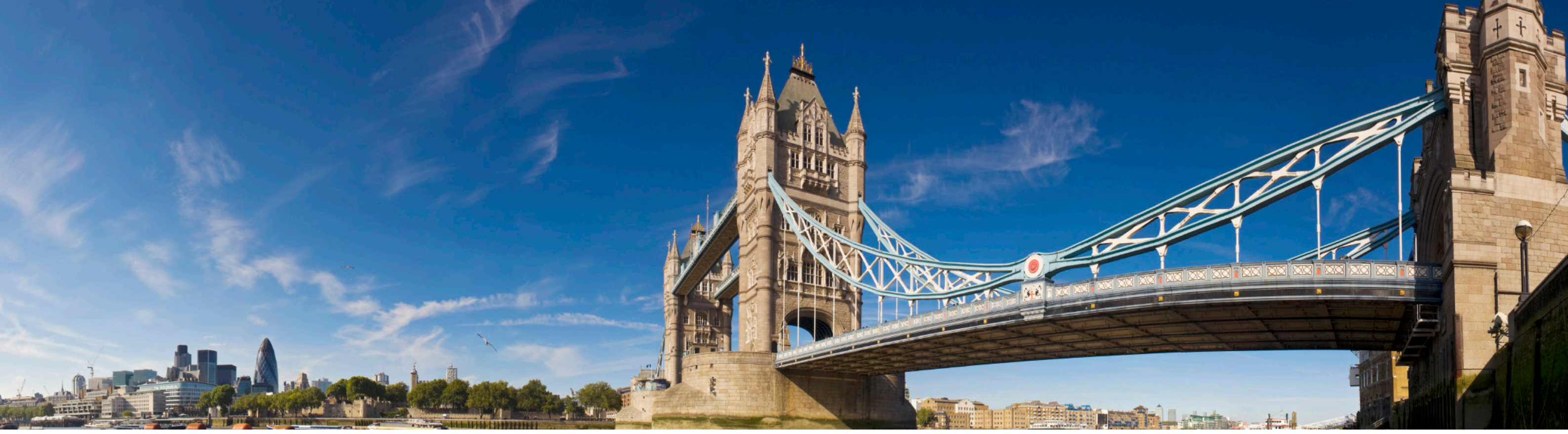

GLOBAL LISTED REAL ESTATE

Our fund benchmark, the FTSE EPRA/NAREIT Developed Net Rental Index, recorded a net total USD return of 2.48% in September. The best performing listed real estate market was the UK, which recorded a total USD return of 8.32% for the month. Australia recorded the lowest total USD return of -3.17%.

Year to date, our fund benchmark has recorded a net total USD return of 21.20%. The best performing listed real estate market for the nine months was the US, with a net total USD return of 25.55%. Hong Kong recorded the lowest total USD return of 3.44% for the nine months.

Global debt and equity market returns have been strong so far this year. The MSCI World Index is up just over 18% and the 10-year US Treasury note has decreased by 100bps. Investment grade corporate bonds, as measured by the Moody's BAA Index, are trading below 3.9%, the lowest yield ever. Most of the government debt in Europe, as well as in Japan, is trading at negative yields. This low-yielding environment has been a tailwind for real estate returns, as demand for assets that deliver positive cash flow with growth prospects has been high.

However, it goes without saying, that not all listed real estate has performed equally well. There is a wide range in the best and the worst company returns this year. Some of the highest returns for companies on our radar are (all returns are in USD): Equinix 66% (Data Centres), Rexford 52% (Industrial), and Invitation Homes 50% (Single Family Homes). The stocks that have delivered the lowest returns are all retail names, with Intu (UK) delivering -62%, CBL & Associates (US) -30%, and Wereldhave (Continental Europe) -23% year to date.

The wide range of returns reflects how drastically different the fundamentals and outlook can be for various real estate sectors. In our August report we wrote extensively about Data Centres and Towers, which continue to experience secular tailwinds from the ever-increasing consumption, storage and transmission of data to and from smart devices. However, attractive development profit margins have led to increased supply in some data centre markets, notably in Northern Virginia – the largest and most important data centre market. CBRE estimates that around 55% of new data centre developments in Northern Virginia is pre-leased. Leasing transactions can be lumpy in the data centre business. Due to strong demand, expectations are for the remaining available space to be leased without causing significant disruptions in market rents.

Secular changes in the retail industry have resulted in significant underperformance of retail landlords compared to other real estate sectors. Changing consumer behaviour, like shopping more online and spending more on experiences, has led to lacklustre sales growth in physical stores. Many retailers are struggling and rationalising store counts by closing unprofitable stores. Declining occupancy and increasing capital investment requirements are both significant headwinds for mall landlords. The outlook for rental growth in the medium term is muted, with only the highest productivity malls expected to maintain or grow rent. However, all retail portfolios are not affected equally, and we expect the divergence in performance between high-productivity and low-productivity retail to continue. Not surprisingly, the retail landlord stocks that have performed the worst this year are also the companies with the highest leverage, illustrating the risk of utilising too much debt in a cyclical business.

Another sector with favourable fundamentals and a positive outlook is Industrial. Growing e-commerce and retail sales coupled with a continuous drive to lower supply chain costs, of which transportation makes up roughly half of the cost, have resulted in strong demand for logistics warehouses located close to dense urban locations. Historically low vacancies and strong market rental growth have led to continuing compression in industrial cap rates as more investors look to gain exposure to the sector. In many of the major markets prime industrial cap rates are now similar or lower than prime mall cap rates. Industrial production and trade volume throughput are economic indicators that warrant close monitoring, as a meaningful deceleration in these would result in reduced demand for warehouse space.

Another underperforming sector this year has been Offices. It has recently been reported in the media that the flexible office space provider WeWork has formally withdrawn its IPO (initial public offering), after it failed to drum up the necessary support from prospective investors. It's refreshing to see that prospective real estate investors in the public market were more sensible about WeWork's business model and valuations than its original tech-focused backers. We have long been sceptical about WeWork's business model of leasing space from landlords on long terms and reletting the space on much shorter leases. The mismatch in term of contractual income and expenses is extremely risky, especially in a sector where rents are cyclical, such as offices.

In the real estate investment business cash flows matter. It is reported that WeWork lost roughly one dollar in net income for every dollar in revenue it collected, which does not sound like a great real estate investment to us. Admittedly the company has spent a lot of capital on expanding and on physical fit-out of its locations. Many office landlords have told us that WeWork has raised the bar for what tenants expect for fit-out packages on new office leases. The office sector was already one of the sectors that required the highest capital expenditure to keep assets in a competitive state before WeWork came along. Post the WeWork era, it seems like the need for capital expenditure will only be ticking up. The low cash flow multiples that the office sector trades at, combined with average medium- and long-term rental growth prospects, translate to some of the lowest prospective buy-and-hold returns for all real estate sectors we cover.

A relatively new sector in the listed real estate market is Single Family Homes, which are institutionally owned individual homes for rent. Favourable demographic trends, stable homeownership rates, and a balanced supply outlook bode well for the sector. The population bracket that is more likely to rent single family homes (35 to 44 years old) is forecasted to grow for several decades. A growing portion of families in this age bracket is choosing to rent rather than own their homes. Larger down payment requirements and higher indebtedness levels make it harder for more families to buy their own homes compared to previous generations.

Overall, real estate fundamentals remain healthy, mainly due to manageable supply levels relative to demand. The estimated forward FAD (Funds Available for Distribution) yield for the sector is 4.46%, and medium-term growth prospects are decent. Listed real estate has performed well this year and, on the whole, appears to be fairly priced given our USD real return requirement of approximately 4.8% and current global bond yields. Within the real estate universe, more attractively priced opportunities exist in specific real estate sectors and stocks.

THEODORE FREYSEN
INVESTMENT ANALYST

GLOBAL LISTED PROPERTY REVIEW

Country	Market Cap USD Million	10 Year Govt Bond Yield	Current Dividend Historical Yield	Debt % Local Currency
US	940 244	1.70%	3.42%	29.59%
Canada	54 602	1.36%	3.77%	41.31%
Total North America	994 846	1.68%	3.43%	30.19%
UK	74 503	0.49%	3.49%	28.29%
Continental Europe	256 844	-0.38%	3.82%	31.54%
Total Europe	331 348	-0.16%	3.73%	35.87%
Japan	163 271	-0.15%	2.56%	35.42%
Australia	44 557	0.97%	5.17%	30.91%
Hong Kong	68 393	1.42%	3.88%	14.61%
Singapore	42 795	1.74%	4.53%	35.33%
Total Asia	319 016	0.50%	3.44%	31.42%
Total	1 645 210	1.16%	3.49%	31.39%

Region	SEPTEMBER 2019 Return % (USD)	SEPTEMBER 2019 Return % (Rand)	YTD Return % (USD)	YTD Return % (Rand)
Global Investors Index (NTR)	2.48%	2.35%	21.20%	27.79%
North America	2.77%	2.64%	25.59%	32.43%
Europe	3.71%	3.58%	13.62%	19.80%
Asia ex Australia	1.64%	1.52%	21.46%	28.06%
Australia	-3.17%	-3.29%	5.35%	11.08%
SA Listed Property Index	0.4%	0.30%	-3.89%	1.34%

INFORMATION SOURCE AND METHODOLOGY

Data:	Bloomberg unless stated otherwise
Calculations:	Catalyst Fund Managers
Clean Price:	Adjusts the closing price for distribution accrued since last distribution date
Rolled yield:	Time weighted current 12 month historic distribution divided by the clean price
Debt %:	These are loan to value numbers.
Date:	All data taken on 1 October 2019
Universe:	Companies included are only those companies that form part of the Catalyst core universe

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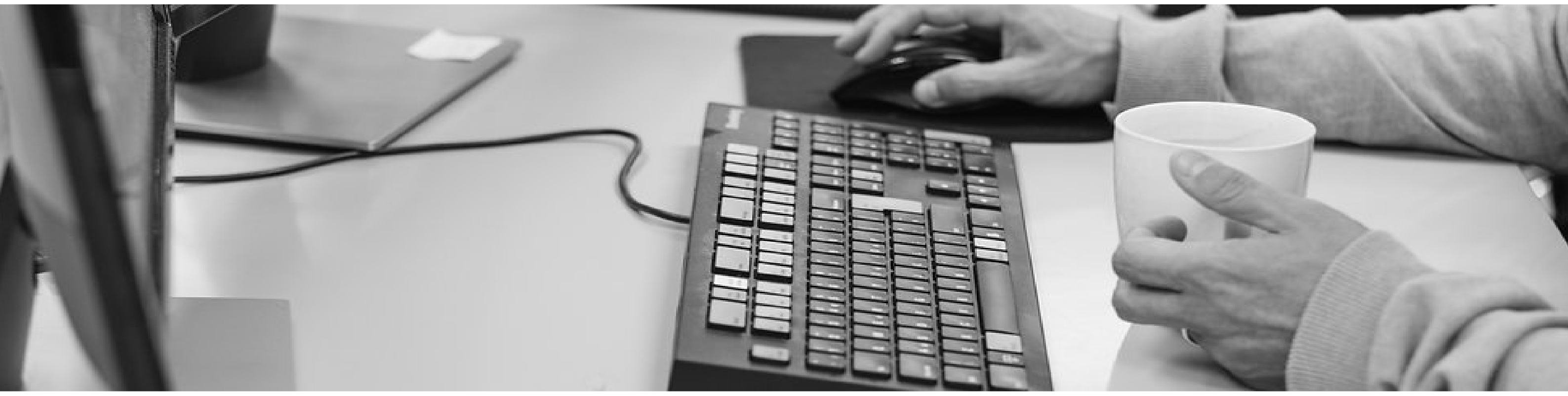

IMPORTANT INFORMATION

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