



LISTED PROPERTY – where to now?

By Warren Ingram

I was recently part of a series of panel discussions on the merits of property as an investment class for Auction Alliance. As the lone opponent of property on a panel of property specialists, I hope I did the other asset classes some justice. The debates did provide some great food for thought and left me feeling even more concerned about property investments than I did before. I think property is facing some severe headwinds and prospective investors should be very cautious.

LARGE PROPERTY INVESTMENTS HAVE DONE VERY WELL RECENTLY

Over the last three calendar years, commercial and industrial property has certainly been the best performer of the major asset classes. This is illustrated in Table A below - you would have earned nearly 6% a year more from property than the stock market over the three years to February 2011. If you had been in listed property in 2010, your average return would have been near 30% for the year. This was substantially better than other asset classes: the share market returned 18%, the bond market 15% and cash, a meagre 6.5% for the year. This situation changed dramatically in the first part of this year with shares comfortably outperforming property again.

TABLE A: RETURNS OF SHARES, BONDS AND PROPERTY TO FEB 2011

	Year to date	1 year	3 years Per year	5 years Per year	10 years Per year
All Share Index Total Return	0.59%	23.59%	4.58%	14.09%	17.16%
Domestic Real Estate Unit Trusts*	-4.68%	13.14%	10.42%	11.46%	18.83%
Domestic Bond Unit Trusts*	-1.74%	10.27%	9.82%	7.30%	10.92%

Source: Morningstar Inc

* Average returns of the sector

WHAT DRIVES PROPERTY?

All property investments are heavily influenced by interest rates. When interest rates fall substantially, property prices usually increase a great deal. Similarly, when interest rates increase, property prices suffer. A country's economic growth has a major influence on property although the effects of this influence are often delayed. If the economy grows substantially, it normally drives property prices upwards but there are major lag times between this growth and the resulting price appreciation. Similarly, the economy could stagnate and property could still continue to go up in price. Last year was a great example of this, our economy was struggling yet listed property returned more than 29%! Most large properties or developments are valued according to the level of income they generate rather than the actual value of the land or of the building. Any factors that hamper rental income are likely to have a direct impact on large prices of commercial and industrial properties. Other factors such as population growth, electricity costs, the political environment, legislation changes, crime and sentiment are also factors that affect property prices.

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WHAT IS GOING TO HAPPEN TO PROPERTY NOW?

The last year was pretty tough for property companies. Normally, they have more than 90% of their properties rented at all times, this is called occupancy rates. Last year, 15% of their properties were vacant, nearly double the average. In addition, the rate of Eskom increases has started to impact their tenants and this has made rental increases more difficult. So tenants have more negotiating power as there is an oversupply of property meaning rental increases are lower than in previous years. Going forward, it is going to be very difficult for landlords to justify 10% rental increases when there is low inflation and an oversupply of property. These problems will be compounded by the prospect of interest rate increases in the near future. Some property economists are anticipating that inflation pressure might result in rising interest rates by the end of the year. If this does not happen, potential property investors will still start to factor interest rate increases into their calculations which will dampen property prices. The Eskom price increases will also continue this year which will add to the pressure on tenants and this will have a knock-on effect on property prices.

We think the cheap money that flooded our economy due to the lowest interest rates in 34 years created an artificial boost to the listed property market in particular. Cheap money always makes investors too bullish as evidenced by the strong performance of listed property last year. The correction that we saw in the first two months of this year was justified but there is still room for more downside.

CONCLUSION

We have always preferred listed property to residential property for long term investors. We like the diversification benefits of this asset class however; we are concerned about growth prospects for the next three years. There might be some good buying opportunities once interest rates start rising.

GALILEO NEWS

WE MOVE INTO LIFE ASSURANCE SERVICES

Since Galileo Capital first started, we have studiously avoided offering our clients any life or disability insurance products. We have always been uncomfortable with the way the industry charges initial fees for long term products. In addition the products are overly complex, which we feel is contrary to the way financial services, should work. At the same time, over the last two years, we have had an increasing number of requests from clients asking for life assurance, especially from business owners and other entrepreneurs. At the end of 2010, we finally met a life assurance specialist that we felt had the necessary experience, expertise and ethics to fit in with the Galileo Way. Her name is Brigitte Tamine and she was working in a family run insurance brokerage called Renate Faltermair Insurance Consultants (RFIC). We merged with RFIC at the end of 2010 and so brought Brigitte into the Galileo family.

Brigitte started in the financial services industry in 1997 at RMB Unit Trusts as a consultant. In January 2000, she started an independent financial planning business within RFIC. In 2001, Brigitte completed the CFA and CFP qualifications which makes her one of the most qualified Financial Advisors in South Africa. She has been married for 7 years and has two boys aged 4 and (nearly) 2 years old. Her hobbies (when she gets a chance) are: off-road cycling, swimming and Pilates.

We are very comfortable that she has all the necessary experience to offer our clients expert life and disability insurance advice. In addition, we have negotiated with every insurance company to pay us on an as-and-when basis rather than on upfront commissions. This is important because we will only earn income for as long as you are a client. This ensures that your advisor is incentivised to service you for the life of the policy and does not encourage a hit-and-run mentality. Whilst this is a new field for us, we are very confident that we have the perfect people using the right processes to advise our clients. Should you require any advice on life or disability insurance, please feel free to contact Brigitte directly on or brigitte@galileocapital.co.za. Alternatively, you can speak to your advisor at Galileo who will put you in touch with Brigitte.

GALILEO CLIENT PROFILE

This is a new section in our newsletter where we profile one of our existing clients. The idea is for you to get to know more about some of our other clients and at the same time it provides them with some profile for their businesses. We feel it is always better to deal with someone you know or who has been referred to you by someone you trust.

TELL US ABOUT YOUR BUSINESS?

Corporate Connections (Pty) Ltd is a business that is owned and run by Stuart and Kim Hockly. We specialise in the sales, distribution and installation of modular power systems for the modern office environment. Founded 27 years ago by members from the office furniture industry the company grew with the knowledge of the need for power, voice and data requirements at the workstation. As the sole distributor of The Power Logic range of modular electrics, who are world leaders and export to over 60 countries worldwide, Corporate Connections remain abreast of modern trends and bring to you, the valued client, an impressive range of office connectivity systems. Added to this impressive product range is an experienced energised sales team, followed by a skilled service and installation teams who will ensure a neat and tidy cable installation. With the head office in JHB and branch offices in CT, PE and Durban, Corporate Connections ensures a complete solutions based office fit out backed up by guarantees and quality service throughout the country and into Africa. With the continued injection of youthful, energetic ideas we remain committed to DYNAMIC OFFICE TECHNOLOGIES – keeping you ahead and maximising your productivity.

For more information please visit www.powerlogic.net

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Top Clients:

Banking Sector: Investec, Standard Bank, Absa, Nedbank. Insurance: Liberty Life, Old Mutual.

Telecommunications: Vodacom, MTN, Cell C. Mining: BHP Bulletin, De Beers, Anglo American.

Government: SARS, Telkom, Eskom. Many small businesses and independent electricians

TELL US ABOUT YOURSELVES?

Stuart from Natal and Kim, a Capetonian met at Stellenbosch University in 1991. We were married in 2002 and are now the proud, hectic parents of 3 boys.

WHAT GALILEO CAPITAL DOES FOR THEM

The Hockly's are true Galileo Capital clients, we manage their investments, insure their business and personal assets. In addition we arranged their life and disability insurance so they have experienced the full range of services offered by us.

WHY GALILEO CAPITAL?

In today's age it is paramount to do business with people, not products. We find the staff at Galileo extremely friendly, reliable and efficient. It is all about building relationships which one can trust and this has been easy with the team at Galileo. They are very knowledgeable in their respective fields and will always discuss all options available and are never forceful in making the final decisions. It is a pleasure to work with Galileo and we look forward to many more successful years together.

GALILEO STAFF NEWS

MORE BABIES AT GALILEO

We are happy to announce that Yolande Botha had a healthy baby boy, Daniel Botha who weighed 3.5kg at birth. Mom and baby are both well and are at home starting their new life with a very proud father, Louis.

THE NEW VOICE AND FACE OF GALILEO

Those of you who have visited our offices very recently will have met our new receptionist, Natasja Mollentze. Natasja used to work for a dive charter business before joining the financial world and her biggest hobby is scuba diving. She is currently doing her dive masters and studying for a BA Business Administration through UNISA part time after having moved to Johannesburg from Potchefstroom where she grew up.

OUR SERVICES

WEALTH MANAGEMENT

We offer our clients dedicated Wealth Management and Retirement Planning services. We focus on clients who have a minimum of R1 million to invest with us either in retirement funds or in discretionary assets such as shares, unit trusts or overseas investments. We are an independent advice-based practice, which means we are not tied to a specific product supplier. This allows us to offer objective independent advice. We use world-class financial planning solutions that allow our excellent financial planning staff to provide our clients with optimal solutions.

CORPORATE ADVISORY SERVICES

The focus of this division is on developing and maintaining best practice in:

- Risk Management Analysis
- Balance Sheet Management
- Corporate Finance Advice

SHORT TERM INSURANCE BROKING

We provide full domestic and commercial short term insurance solutions as well as specialized commercial risk solutions. This means that we provide insurance broking services for companies and private individuals. We arrange insurance cover for buildings, vehicles, business risks, household contents etc.

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