



# Investec Property Equity Fund

As at 31 March 2011

## Market and portfolio review

The beginning of the year brought further market volatility, amid natural disasters and political tensions. The political turmoil in the Middle East has driven the oil price to well above \$100 per barrel. This has increased the likelihood of higher global inflation, which could threaten the economic recovery. In the midst of uncertainty in the Middle East, Japan experienced an earthquake of great magnitude. This led to concerns about the global recovery, as Japan is a major economic player in the world. In the aftermath of the quake, a tsunami, nuclear leakages and halts to manufacturing and production in affected areas, have added to concerns surrounding the possible long-term global impact.

Following the festive season and going into 2011, the South African economy has continued to show signs of improvement. At its most recent monetary policy meeting, the South African Reserve Bank raised its growth forecasts for 2011 from 3.4% to 3.7% and its 2012 figures from 3.6% to 3.9%. The decision to keep the repo rate unchanged at 5.5% was in line with market expectations. Expected average inflation for 2011 is now at 4.7% and 2012 set at 5.7% – a mere 0.3% off the upper end of the band, possibly indicating that ‘loose’ monetary policy in the near term may become difficult to maintain.

The listed property sector retreated at the beginning of the year due to profit-taking after its stellar run of 29.6% in 2010. The months of January (-4.2%) and February (-1.2%) were both weak. The main reason for the decline in the sector was on the back of bond weakness due to global uncertainty, expectations of rising inflation and the tentative economic recovery. Once results were released and investors were more comfortable with future prospects for the property sector, prices started to recover. The month of March was stronger, resulting in a positive return of 3.4%. The listed property sector had a subdued quarter, performing the worst over the period relative to other asset classes. Listed property returned -2.2%. Bonds lost 1.6% for the quarter, while equities and cash gained 1.1% and 1.4%, respectively.

Asset class returns	3 months to 31 March 2011	6 months to 31 March 2011	12 months to 31 March 2011
All Share Index	1.1%	10.7%	15.2%
All Bond Index	-1.6%	-0.8%	8.3%
SA Listed Property Index	-2.2%	0.9%	15.4%
Cash	1.4%	3.0%	6.5%

Source: Deutsche Bank

## Portfolio activity

After the first round of financial results and guidance on future income growth expectations, a number of the stocks started looking expensive on a relative basis. This meant that we had to review the portfolio's positioning, investing in those funds which were going to weather the storm even better. The current storm comprises higher rates and taxes, increasing pressure on the cost to income ratio of most funds. However, we were encouraged by Growthpoint's better-than-expected results, which indicate a significant improvement in fundamentals on all metrics. Although we like Growthpoint and its prospects, we took profits as we wanted to participate in the distribution re-investment programme (DRIP) which would realise more shares at better prices, in lieu of cash from distributions.

Portfolio purchases included Hyprop and Acucap, while the exposure to Emira, Growthpoint (as explained), Pangbourne and Redefine was reduced to deemed appropriate weights. Pangbourne was lightened as a result of its merger with Capital, which was finalised at the end of the quarter. We continue to maintain an overweight exposure to the merged entity, relative to the increased benchmark weighting. The portfolio disposed of its investment in Fortress B.

Over the quarter, positive contributors to performance were led by Premium (9.03%, with a 12.7% return in March), Fortress B units (7.92%) and Growthpoint (4.16%), while Redefine (-4.21%), Resilient (-4.06%), Hyprop (-3.13%) and Pangbourne (-2.58%) were the sector laggards.

## Portfolio positioning

Capital raising is in abundance through initial public offerings (Investec Property Fund and Rebois) and additional equity raising (Fountainhead). The portfolio had to increase the cash holding in order to participate, using the cash from the sales and distribution income. The result was a portfolio high in cash, especially towards the end of the quarter, and this created a drag on performance.

The portfolio will be well structured after participating in the capital-raising initiatives and reducing the cash exposure to become fully invested in the sector. We anticipate a total return for the sector of 14% to 16% for 2011. This is based on expectations of a stabilisation and in some cases a recovery in many of the major property variables, including vacancies and rentals, with further benefits being achieved from a lower interest rate environment. Increased municipal rates remain a concern and could put a dampener on distribution growth.

Collective investment schemes in securities (unit trusts) are generally medium to long term investments. The value of participatory interests (units) may go down as well as up and past performance is not necessarily a guide to the future. Fluctuations or movements in exchange rates may cause the value of underlying international investments to go up or down. Unit trusts are traded at ruling prices and can engage in borrowing and scrip lending. Forward pricing is used. Quantifiable deductions are the initial fee whilst non-quantifiable deductions included in the net asset value price may comprise brokerage, MST, auditor's fees, bank charges, trustee and custodian fees. Commissions and incentives may be paid and if so, would be included in the overall costs. A schedule of fees and charges and maximum commissions is available on request from the company/scheme. If required, the portfolio manager may borrow up to 10% of the market value of the portfolio to bridge insufficient liquidity. Unit trust prices are calculated on a net asset value basis, which is the total value of all assets in the portfolio including any income accrual and less any permissible deductions from the portfolio. Different classes of units apply to the fund and are subject to different fees and charges. Fund valuations take place at approximately 16h00 SA time each day. Purchase and repurchase requests must be received by the Manager by 16h00 SA time each business day. Performance figures are based on lump sum investment (if applicable). This portfolio may be closed in order to be managed in accordance with the mandate (if applicable). Please note that with effect from 1 February 2009 the annual management fee on B class units increased by 0.285% (incl. VAT). The risk profile is a measure of volatility, i.e. how the absolute return of the fund varies. Note that there are other risks in the fund, which are not reflected in this rating. The TER shows the percentage of the average Net Asset Value of the portfolio that was incurred as charges, levies and fees relating to the management of the portfolio. A higher TER ratio does not necessarily imply poor return, nor does a low TER imply a good return. The current TER cannot be regarded as an indication of the future TERs. A copy of our performance fees FAQ is available at [www.investecfunds.co.za](http://www.investecfunds.co.za). Investec Fund Managers SA Ltd is a member of the Association for Savings & Investment SA.

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