Quarterly Commentary

M&G Enhanced SA Property Tracker Fund

Property

Q1 2024

Market overview

The first quarter of 2024 (Q1) brought a continuation of the relatively bullish investor sentiment towards global equities seen in the last months of 2023, as prospects for growth in the US were buoyed by positive company earnings reports and supportive economic data that increased the likelihood of a "soft landing" for the economy. On the other hand, global bonds were weaker as inflation proved higher than expected and major central banks kept interest rates on hold, prompting pundits to move out their rate cut expectations to the second half of the year. Still, they and the US Federal Reserve are roughly aligned in their forecasts of a 25bp interest rate cut in each of Q2, Q3 and Q4, starting at the Fed's 11-12 June FOMC meeting.

The Japanese and US equity markets were the stand-out performers, while the UK disappointed and China continued to experience losses, although the magnitude of these fell as the quarter progressed, helped by small gains in March. Emerging markets were broadly in the red, with the exception of India, and South African equities remained in the doldrums on the back of slow growth and the approaching May national elections.

Global equity (as measured by the MSCI ACWI) delivered a total return of 8.2% in Q1 compared to 11.0% in Q4, while developed market equities produced 8.9% and emerging market equities returned only 2.4% (MSCI Emerging Markets Index – all in US$). Global bonds posted -2.1% (Bloomberg Global Aggregate Bond Index, in US$). In South Africa, the FTSE/JSE All Share Index and Capped SWIX Index underperformed, both delivering -2.3% in rand terms. The local market was dragged down by a 7.6% loss in Financials, while Industrials returned 0.6%, Resources 0.8% and Listed Property 3.5%, the latter continuing its rally from the previous quarters.

South African bonds recorded a -1.8% return for the quarter. This saw the yield on the 10-year SA government bond rise to 12% by quarter-end. Meanwhile, the rand lost 3.5% against the US dollar, 2.7% versus the UK pound and 0.9% against the euro.

At its March policy meeting the SA Reserve Bank voted unanimously to keep the repo rate steady at 8.25%, as expected. Governor Lesetja Kanyago remained hawkish regarding stubbornly high inflation (with CPI rising to 5.6% y/y in February from 5.3% y/y in January, well above the expected 5.4% y/y) and relatively high inflation expectations for 2024 among businesses and consumers. The economy managed to eke out growth of 0.1% (q/q annualised) in Q4 2023, worse than expected, for an annual rate of 0.6% for 2023 as a whole. The SARB has projected GDP growth at 1.2% in 2024 and 1.3% in 2025, the acceleration due largely to improved electricity supply. Equity returns remained depressed by the country's low growth prospects and uncertainty over the upcoming national elections, both of which are keeping foreign investors on the sidelines.

Performance

The M&G Enhanced SA Property Tracker Fund returned 3.3% for the quarter, compared with 3.8% for its benchmark. For the one-year period, the fund delivered 19.5% versus the benchmark's 20.5%.

Positive contributors to relative performance include the underweight position in Equites and overweight positions in Nepi Rockcastle and Stor-Age.

Underweight positions in Attacq, Lighthouse and Burstone detracted from relative performance, as did the overweight position in Dipula.

Strategy and positioning

Our fund positioning favors offshore names with strong property fundamentals, such as NEPI Rockcastle, Sirius Real Estate and Hammerson. Locally, we find good value in high-yielding mid-caps such as SA Corporate, Octodec and Dipula.

South African property fundamentals are stable, with vacancy levels steadily declining across all sectors. However, sectoral rental growth has diverged. Office rents remain under pressure due to an oversupply of space. Retail rent affordability ratios are at decade lows, and we've seen reported rental reversion turn positive. This positive momentum is somewhat countered by a constrained SA consumer and distress in one South Africa's largest retail anchor tenants, Pick 'n Pay. Industrial property has delivered the strongest growth, benefitting from favourable supply demand dynamics and the pass-through of rising construction costs.

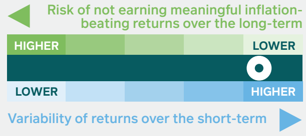
Prevailing headwinds such as rapidly rising property costs and higher interest rates are reflected in earnings expectations that show limited short- to medium-term growth. Therefore, our preferred South African stocks are high yielding mid-caps where prospective returns exceed that of the SA government bond yield.

Offshore property fundamentals vary by region and sector. Here we favour stocks with strong balance sheets and enduring growth prospects. Favored sectors include retail property in Central Eastern Europe and Spain where the robust performance is underpinned by resilient consumer spending. Other favored high growth stocks include Sirius and Stor-age who have flexible leasing business models supported by sophisticated operating platforms capable of dynamically capitalising on customer demand trends.

With interest rate cuts approaching and less load shedding expected in South Africa, we anticipate that previous headwinds will turn into tailwinds, and that the listed property sector stands to surprise on the upside over the medium term. We've positioned our portfolio to benefit from these dynamics, while not compromising on our quality criteria – picking stocks with high free cash flow

Annualised performance	A class	Benchmark	T class	D class
1 year	19.5%	20.5%	19.5%	19.7%
3 years	13.6%	13.9%	13.6%	13.8%
5 years	-0.1%	0.7%	-0.1%	0.1%
7 years	-2.4%	-1.4%	-2.4%	-2.2%
10 years	2.6%	3.1%	-	2.8%
Since inception	8.9%	9.3%	-	-

Risk profile



Fund facts

Fund managers

Yusuf Mowlana
Rahgib Davids

ASISA category

South African - Real Estate - General

Benchmark

FTSE/JSE South African Listed Property Index (J253)

Inception date

2 December 2005

Fund size

R596 226 615

Awards

Morningstar/Standard & Poor's: 2011

Sources: M&G Investments, Morningstar & Deutsche Securities generation and strong balance sheets.

We are pleased that the merger between the M&G Enhanced SA Property Tracker Fund and M&G Property Fund will go ahead and is expected to be completed by the end of May 2024. We're pleased to share that the M&G Property Fund won the Raging Bull Award 2023 for the "Best SA Real Estate General Fund" for its straight performance over the three-year period to 31 December 2023. We are excited about the merger and would like to thank clients for their ongoing support. We look forward to continue delivering value for all clients under the strategy pursued by the M&G Property Fund.

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Invest now

Application forms

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