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Analysts tip bounce for REITs

Winston Sammut, managing director of Folkestone Maxim Asset Management. Picture: Britta Campion

ELIZABETH REDMAN THE AUSTRALIAN 12:00AM April 5, 2018

Share prices of Australia's largest REITs have been under pressure in recent months on the back of adverse bond moves and fears over the health of some tenants, particularly in the retail sector.

But analysts tip the sector's performance to improve given that the property trusts have solid balance sheets and reported upbeat results during the most recent earnings season.

The S&P/ASX 200 A-REIT index has dropped almost 12 per cent since December 13, with concerns surfacing around the start of this year about currency and interest rate impacts.

Some of the largest names have been hit hard: over the same timeframe Vicinity Centres dropped almost 20 per cent, GPT shed more than 15 per cent, Scentre fell 13 per cent, Dexus lost 12 per cent and Westfield fell almost 12 per cent, even as a takeover offer is on the table from European mall giant Unibail-Rodamco.

Shaw and Partners research noted that the REITs had performed worse than the broader index over the financial and calendar year to date but beat the index in March.

"The concern started in January, when (yields on) bonds looked like they were going to go through the 3 per cent level," Folkestone Maxim Asset Management managing director Winston Sammut told *The Australian*.

Rising bond yields in the US made bond proxy stocks such as real estate investment trusts less attractive for investors.

"At that time, the Aussie dollar was around the US80c level," Mr Sammut said.

"The investors from offshore thought it was going to go lower, and also were concerned about interest rates, so they sold stock."

The sector is also digesting the announcement of new measures to limit tax concessions for foreign investors in stapled structures, although analysts at this stage expect the impact to be limited.

Mr Sammut is optimistic that the sector will recover as worries about interest rates recede, the recent earnings season was free of disasters and the trusts are set to maintain their dividends.

Citi analysts were also upbeat, saying in a note to clients that the Australian yield curve was flattening, which could be bullish for local REITs, while a note from Core Property Research tipped some trusts that were trading at a discount to NTA to buy back stock.

CLSA head of Australia real estate Sholto Maconochie said despite "pretty good results" in February, the bond proxy sell-off and the weak sentiment in the retail sector had been weighing on the property trusts.

Mr Maconochie tips share prices to improve as bond rates have now come off but warns that expectations of future bond yields can move in a volatile fashion, adding that on the retail front there were no real catalysts that would spark a pick-up in retail sales. He also predicts more merger and acquisition activity.

"Things are mispriced, at a big discount to NTA," Mr Maconochie said. "There's a lot of interest in the smaller names … if the discount to NTA persists you could see mergers, privatisation."

Resolution Capital portfolio manager Andrew Parsons noted worries about the health of some retail tenants as consumer preferences change.

General equity funds seemed to be moving out of the sector, he said, but if the Westfield takeover proceeded it would free up some investor cash that could be reinvested into other REITs that largely had "pretty reasonable balance sheets".

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"You're seeing a rotation (by investors) out of the REITs into faster earnings growth stories. And obviously that hasn't been helped by the interest rate environment but it's not about interest rates alone," he said.