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SATURDAY STAR - PERSONAL FINANCE 2016/09/24 Page: 3

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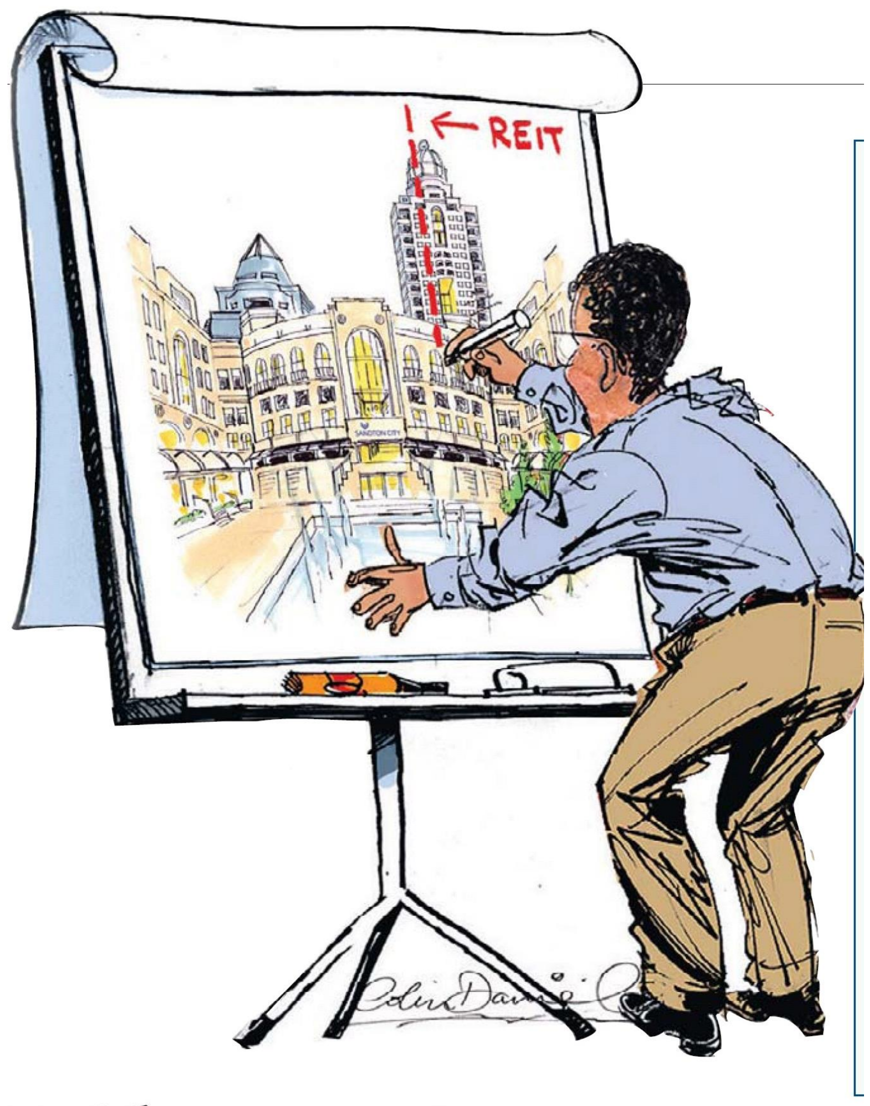

Liberty's property fund sprouts a Reit

Investors in Liberty's unlisted property portfolio are being asked if they want to switch to a listed property vehicle that will initially reflect the same holdings. **Laura du Preez** reports

Liberty clients who have policies invested in its unlisted property portfolio are being offered an opportunity to switch their investment, either wholly or partially, into a new portfolio which will hold shares in a listed property trust exposed to the same blue-chip properties.

When Liberty's Two Degrees real estate investment trust (Reit) lists on the JSE in early December, the properties in the portfolio will move to a market valuation, and Liberty expects policyholders who switch to the new Reit portfolio, as well as those who do not switch, to enjoy a three- to five-percent increase in the valuation of their portfolio.

Liberty's Two Degrees Reit will initially hold portions of the properties in Liberty's unlisted R27 billion property portfolio. These blue-chip properties include Sandton City Shopping Centre, Eastgate Centre, Melrose Arch, Nelson Mandela Square and Liberty Midlands Mall, the Botshabelo Mall development and Liberty's head offices in Century City and Umhlanga, among others. The Reit will also invest in developments in South Africa and the rest of Africa.

Despite these being very successful properties, the Liberty Property Portfolio returns have lagged those generated by the FTSE/JSE Listed Property Index (see table, above right). The index returned an average of 18.78 percent a year over the past 10 years to the end of June, according to Profile Data and 14.32 percent a year over the past three years.

However, comparing unlisted property investments with listed ones is misleading, because listed investments are valued in line with investor demand and sentiment and the liquidity of the investment.

Reits are entities that invest directly in property and enjoy a unique tax dispensation. These structures are recognised in a number of different countries and are available on their stock exchanges.

The Two Degrees Reit will take up an increasing share of the returns of the existing properties as policyholders invested in the unlisted Liberty Property Portfolio exit that portfolio. Liberty is allowing policyholders with exposure to the property portfolio to switch up to R3 billion in total into its life portfolio, the Real Estate Portfolio, which will, in turn, invest in the Reit.

Policyholders making the switch will enjoy a five-percent discount on the listing price, which has yet to be determined. There will be no costs for the switch and the portfolio costs will be the same.

David Lloyd, the managing director of Liberty Innovate, says the advantage of the switch is that normally a Reit takes a long time to build up a portfolio of good properties, but by buying into Liberty's existing property portfolio, the Reit gets the immediate benefit of an already-established blue-chip portfolio.

Over and above any switches, Liberty clients, regardless of whether they are currently exposed to the Liberty Property Portfolio or not, are being offered an opportunity to invest up to R1 billion in the Reit on a first-come-first-served basis ahead of the listing, also at a five-percent discount to the listing price.

Liberty is expecting the Reit will buy up to R6 billion of the R27 billion in the Liberty Property Portfolio and it is expecting to raise R10 billion in the Reit at the listing, providing it with R4 billion to invest in other properties. The proportion of the existing blue-chip portfolio to new properties will depend on how many policyholders exit the unlisted portfolio and how much new investment the Reit receives.

The investment transferred from the property portfolio to the Reit will constitute a portion of the whole property portfolio, ensuring that existing policyholders are not prejudiced and will maint ain their exposure to the full property portfolio.

Policyholders who remain in the original property portfolio will also enjoy a once-off revaluing of their investments, because the Reit will buy the properties from the original portfolio at market value.

If your Liberty policy is exposed to the property portfolio and it includes a guarantee on the capital or the returns, and you decide to switch, you will lose the guarantee. If you had valid reasons for taking out the guarantee in the first place, it may not be worth your while switching to the Reit, which is exposed to the ups and downs of the market.

Also be careful if you have a retirement annuity (RA) that must comply with regulation 28 of the Pension Funds Act. The switch and the increase in the value of the Reit could affect your asset allocation.

If you have an RA that you took out before 2011, you may be entitled to higher equity and listed property exposure than a newer RA, because these policies were allowed, individually, to exceed the regulation 28 limits, as long as the RAs as a group complied with the regulation. However, a switch will trigger the need for your RA to comply individually.

UNKNOWN QUANTITY

Ian Anderson, chief investment officer at Grindrod Asset Management, says there's no doubting the quality of the property portfolio, but the problem for policyholders is that they do not know what price they will pay for their investment in the Reit, even though it will be at a discount to the price other shareholders will pay.

The price at listing will be based on demand from the market for the initial public offering of the shares in the Reit.

Despite this, Anderson says policyholders should consider participating in the new Reit.

Another real estate fund manager, who did not want to be named, said Liberty's property portfolio has some unique assets that do not often come onto the market, but investors still need to weigh up the value relative to the price at listing. He said asset managers were waiting for more information about the yields and capital appreciation of the properties in the portfolio.

Liberty's Two Degrees Reit will be managed by the same team within Stanlib, under chief executive officer of Liberty Two Degrees, Amelia Beattie, who has managed the Liberty Property Portfolio for many years.

A PENSIONER'S PLIGHT

MARTIN HESSE

Buying a pension with your retirement savings is one of life's most critical financial decisions, and the true test of your decision may become apparent only many years later, perhaps once your income has rapidly started to lose its buying power.

Mr H, a Cape Town pensioner in his late eighties, contacted Personal Finance through his financial adviser because he was concerned about the recent low annual escalations on his Liberty Life pension (annuity), which he bought in 1991, and which is linked to Liberty's Property Portfolio. He said that, compared with the portfolio's returns, the property returns published in the media outperformed the portfolio, especially over the past five years.

Mr H bought the annuity in 1991 for R103 193. It is a compulsory purchase life annuity, which participates annually in any investment surplus over eight percent from Liberty's Property Portfolio.

Mark Lapedus, the divisional director of proposition enablement at Liberty, explained to Personal Finance how the annual escalations are calculated. "Each year, in April, the annuity is adjusted positively or negatively in accordance with the property bonus declared by Liberty. The annuity is adjusted by the difference between the declared bonus and eight percent. The annuity could therefore either increase or decrease. At no time, however, will the annuity be less than the guaranteed [initial rate]."

Liberty also subtracts its management fee (1.62 percent) from the return.

In this way, Mr H's annual income from the annuity increased from R9 344 in 1992 to R30 468 in 2015, which represents an average increase of 5.3 percent a year, Lapedus says.

Mr H complains that up until 2010, increases averaged above six percent, but since then, he says, they have been below two percent a year.

Lapedus provided a table showing the returns, which reflect Mr H's concerns (see table) .

"The Liberty Property Portfolio has holdings in high-quality direct (unlisted) property investments," Lapedus says.

LIBERTY PROPERTY PORTFOLIO RETURNS AND SURPLUSES vs SAPY OVER 10 YEARS

Year ending 31/12	Property portfolio return	Bonus rate declared after 1.62% fees	Surplus above 8% (annual escalation)	SA Listed Property Index return
2006	19.46%	17.84%	9.84%	28.23%
2007	20.16%	18.54%	10.54%	26.54%
2008	14.95%	13.33%	5.33%	–4.39%
2009	11.47%	9.85%	1.85%	14.11%
2010	11.89%	10.27%	2.27%	29.51%
2011	10.51%	8.89%	0.89%	8.98%
2012	10.33%	8.71%	0.71%	35.89%
2013	10.85%	9.23%	1.23%	8.39%
2014	10.86%	9.24%	1.24%	26.67%
2015	10.37%	8.76%	0.76%	7.98%

"As at December 31, 2015, the average annual return over the last 10 years was 13.12 percent. The portfolio has delivered on its mandate to provide investors with steady, reliable returns with low volatility over the longer term. It continues to deliver on this objective and its performance target of inflation (as measured by the Consumer Price Index) plus five percentage points a year over a rolling five-year period, before costs."

It is likely that, in comparing returns, Mr H referred to the FTSE/JSE SA Listed Property Index (Sapy). The Sapy delivered average annual returns of 17.02 percent over five years to the end of 2015. However, the Sapy does not track the returns on physical properties. It tracks the share prices of 22 property companies listed on the JSE, which may be volatile and may be over-valued in terms of the companies' earnings, and some of the listed companies have extensive foreign property holdings.

A fairer comparison may be with the IPD SA Property Index, which tracks returns on commercial properties across South Africa. This index returned 13.5 percent a year, on average, in the five years ending December 2015, compared with the Liberty portfolio's 10.62 percent.

"The IPD SA Property Index doesn't correspond exactly to the Liberty Property Portfolio. I suspect that it is more volatile than the Liberty portfolio," Lapedus says.

Mr H's product is no longer sold by Liberty, Lapedus says. It has been overtaken by inflation-linked annuity products. He says there are about 2 000 holders of this type of annuity still on Liberty's books. They are welcome to switch into another type of Liberty annuity, but are likely to get a lower rate.