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Unlisted funds bullish after a good 2015

Investment

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Investor demand for higher returns will continue to drive outperformance of unlisted property funds this year, particularly if global market turbulence leads to lower interest rates and bond yields, say fund managers.

Projected returns of more than 7 per cent over the next 12 months will be a popular choice against 2 per cent cash rates, 3 per cent term deposits and ASX 200 dividend yield at 4.5 per cent, the fund managers say.

Managers are urging investors to look beyond first-year yields to the quality of the underlying assets, such as lease profiles and tenants' covenants, as well as to gearing, to maximise capital growth and total returns over the term of the investment.

"Recent market turbulence further dampening economic growth and demand for space will be a pretty modest negative," said Shane Oliver, AMP head of investment strategy and chief economist.

"To the extent it means lower interest rates and bond yields for longer, then it is a slight positive for property as it will add to 'search for yield' demand," he said.

The unlisted sector includes core and non-core sectors.

Core funds offer lower risk, with constraints such as a 20 per cent limit on development property and a 50 per cent limit on gearing. Total return – income and capital – for the year was 26.4 per cent, shows the Property Council/IPD *Unlisted Core Retail Property Fund index.*

Non-core funds are unrestricted by any of those investment conditions. Total return for 2016 on the $2 billion of funds in Property Council/IPD *Unlisted Non-Core Retail Property Fund index* was 37.6 per cent.

Charter Hall dominated the performance tables in the Core sector with 12-month total returns from 28 per cent for its industrial fund to 58per cent for the direct office fund.

Richard Stacker, head of Charter Hall Direct, said the issue over coming months would be to identify "high-quality investment products with long leases and strong tenant covenants in growing markets."

Adrian Harrington, head of funds management for Folkestone, a real estate funds manager and developer, whose Altona North income fund returned 28 per cent, said, "Investors will continue to seek capital growth and reasonable yield. But it is getting hard to find quality property at a reasonable price."

Jason Huljich, chief executive of Centuria Property Funds' unlisted funds division, which has about $700 million in 12 funds, said, "Strong demand from investors will continue during the year. Equity markets are extremely volatile and some investors are cashing out and looking for yield."

Sentinel Property Group produced six of the top-10 performing, unlisted non-core retail property funds during December with its flagship Homemaker Trust returning about 130 per cent.

Managing director, Warren Ebert, set up the group in in 2010 to buy property bargains in the global financial crisis. He said Sentinel would continue "buying things others do not want", particularly from the institutional fund managers.

"We are looking for properties with troubles, such as vacancies, that we can fix and turn around," he said.

Shane Oliver urges investors to share his long view. PHOTO: LOUIE DOUVIS

Bumpy year

The Property Council/IPD Unlisted Core Retail Property Fund Index – 12-months total return

SOURCE: MSCI