



Platform

10 August 2011 Plexus Asset Management

Independent Insight in an Uncertain World

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LISTED PROPERTY'S PERFORMANCE: IS IT CORRELATED MORE WITH BONDS OR EQUITIES?

Real estate unit trust funds have been in the limelight of late owing to their strong performance numbers at the end of the June quarter. Not only did the sector take top position for the June quarter, but it was also the top-performing sector over the past three and five years.

This prompted the Plexus research team to analyse the relationship between the domestic equity market (the FTSE/JSE All Share Index), JSE-listed real estate (the FTSE/JSE SA Listed Property Index) and local bonds (the BESA All Bond Index). Year-on-year returns based on total return data were calculated for each asset class on a rolling monthly basis for the period from the end of March 2003 to the end of July 2011, amounting to 101 observations. These were then grouped based on year-on-year equity market performance figures. The group ranges were: less than -10%; between -10% and +10%; between +10% and +20%; between +20% and +30%; between +30% and +40%; and more than +40% (see table below), amounting to a more or less even dispersion of observations for each.

As can be expected the correlations between the equity (ALSI) and bond (ALBI) markets proved to have the weakest relationship, especially during periods in which equities performed well, as is most apparent for performance figures in the 20% to 30% range. What can also be observed is that the correlations between the bond (ALBI) and real estate (SAPI) markets proved to be much greater than those witnessed between equities and real estate. For the bond/real estate pair, the relationship proved to be strongest during negative equity markets, and gradually weakened as year-on-year equity performance increased.

The opposite proved to be true for the real estate/equity pair, which exhibited weaker correlations during negative equity markets and stronger correlations during positive periods, specifically between the 10% to 20% range, which exhibited the strongest relationship among the positive periods. This implies that real estate is generally affected by factors similar to those of bonds, but starts behaving slightly more like equities as equity markets start exhibiting highly favourable returns.

The current uncertainty in global financial markets has resulted in more subdued performance from equity markets, with year-on-year performance gearing down to 13,1% as at the end July 2011 from June's 24,6%. And if the current global climate of risk aversion results in a continuation of the recent bouts of relatively weak month-on-month performances, it is not unlikely that year-on-year equity returns could be confined to the three lower bands of the study (i.e. those below the 20% level). If this proves to be the case, this study would imply that bond-related factors could play a much greater role than equity-related factors in determining real estate

returns over the next couple of months,, especially so for year-on-year equity returns below the 10% level.

With the Monetary Policy Committee expected to tighten monetary policy in roughly six to eight months' time, this could prove to be the case as the related interest rate hikes could impact both bond and equity markets negatively. Drawing inference from the results of the study, and if historical findings are anything to go by, real estate returns could possibly show a stronger correlation to those of bonds (bearing in mind that real estate return fluctuations could prove to be much larger than those witnessed in the bond market space), and end up losing some of their recently strong equity-like performance.

