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Allan Gray Property Trust: Annual results and the South African property market in context

Allan Gray Property Trust Performance and Financial Results
Our purpose is the creation of long-term wealth for our unitholders. To this end we are pleased to announce the results for Allan Gray Property Trust for the year to end of September 2006.

Over the last six years to September 2006 the total return per annum generated by Allan Gray Property Trust compared with inflation has been as follows:

	2001	2002	2003	2004	2005	2006	6-year compound % p.a.
Allan Gray Property Trust	39.3	1.3	36.9	39.9	57.1	9.7	29.2
Inflation	4.4	11.2	3.7	1.3	4.4	5.3	5.0
Real Return	34.9	-9.9	33.2	38.6	52.7	4.4	23.7

(Source: I-Net Bridge)

Total distributions for the year to 30 September 2006 were R388 457 million, equivalent to 39.0 cents per unit (2005: 35.0 cents). The total distribution comprised an interim distribution of 19.3 cents (2005: 17.4 cents) and a final distribution of 19.7 cents (2005: 17.6 cents) paid on 27 November 2006. This is an 11.4% increase for the year.

Allan Gray Property Trust participates in the IPD South Africa annual benchmark survey, which measures the performance of its underlying direct property portfolio against other listed funds. For 2005 Allan Gray Property Trust's total return was 53.9 % compared with the benchmark of 33.8%. This was the second best performance out of 17 participants. In addition, Allan Gray Property Trust won the annual award for the best three-year performance for its office and industrial portfolios, making it the first fund to win in all three categories.

Valuation of the Trust's Portfolio
The net asset value per unit (as valued by independent valuer Rode and Associates CC) is 24.9 % higher than that of last year, as a result of improved valuations. The market rating of the property portfolio in terms of the anticipated forward earnings yield has improved from 9.5% last year to 8.7%. The portfolio is concentrated significantly in 14 properties with these 14 making up 80% of the portfolio by value.

Looking back at factors that have affected property performance and ahead at some indicators
Against the backdrop of an increasing current account deficit, a weaker rand and mounting inflationary pressures, bond yields have been higher in the South African market. The monetary authority's response in the form of repo rate increases have affected the pricing of listed property adversely and has also had the effect of increasing capitalisation rates for direct property as well.

There are however positive indicators for the industrial sector of the property market as nominal rentals in this sector have achieved superior earnings growth. Vacancy rates in the office market have continued to decline, with the South African Property Owners Association reporting national decentralised office vacancies at 4.5%, down from 5.7% in the previous quarter. This positive trend is also evident in the industrial market, where, apart from the Cape Peninsula, vacancies are below 5%.

Building completions in the office and shopping sectors have risen strongly over the last year. While industrial building completions have declined substantially, it is evident that this could turn sharply upwards given the level of plans passed. Reportedly, building cost inflation as measured by a Bureau of Economic Research building cost index is running currently at a meagre 5%, which is difficult to explain given the strength of the market. Our expectation is for this to be revised upwards.

In the retail market, sales in July grew 9.7% in real terms over the previous year, an improvement on the 3.2% growth of a year ago. Given the recent increase in short rates and the prospect of further rate hikes, we would expect retail growth to soften. Mean escalations in rentals have softened already to around 8% from the 9-10% range a year ago.

Given the popularity of property as an asset class for many South Africans, we are often asked why we don't offer a retail (open ended) unit trust that invests in property. In answer to this: firstly, clients have the option to invest in Grayprop already. Secondly there are a number of property "fund of funds" that do include Allan Gray Property Trust as an underlying investment and finally, at Allan Gray we do not believe that the size and liquidity of the listed property market is sufficient to offer such a fund ourselves and would rather, when we see a case for investments in listed property, include these in either our Stable or Balanced funds as part of a diversified portfolio.

Commentary by John Rainier, Managing Director, Allan Gray Property Trust Management Limited