

A very alternative source of yield

Weekly Digest

13 August 2018

– David Lashbrook, CFA

When thinking about high yield investments, I suspect that Africa ex SA property does not sit high in many people's minds.

However, we believe this asset class has the potential to provide investors with an attractive hard currency yield. For example, our Momentum Africa Real Estate Fund (or "MAREF") is currently completing two office block developments in the city of Accra, Ghana. We forecast that the initial rental yields on these projects will exceed 10%. Lease agreements are dollar-denominated and annual escalations are 3 – 4%. We therefore anticipate that these cash flows will provide a healthy contribution to the total return for MAREF's investors.

The institutional real estate market in Africa outside of South Africa is still in its infancy and is not presently in a suitable state for largescale retail investor flows. This will change in time: South Africa's listed property market was in a similar state at the turn of the century (not long after Nelson Mandela was voted in). The market cap was only \$1bn and it was trading at double digit yields. Today that market has matured – the market cap is at least twenty times larger and yields have dropped into the high to mid-single digits. We believe that the property market in Africa ex SA will follow a similar trend over the next 20 years as liquidity deepens and the quality of assets improves.

Whilst not being without risk, we believe that it is possible to sustain attractive hard currency yields. Commercial rentals in Africa ex SA are often charged in US dollars. However, earning rentals in hard currency doesn't necessarily protect investors from Africa's sometimes infamous currency volatility. If a tenant earns its income in

local currency, it will struggle to pay hard currency rentals when the local currency plummets. In contrast, tenants earning US dollars (such as international oil or financial services companies) are well positioned to withstand local currency volatility.

A healthy yield is scant consolation if there is a simultaneous erosion of the capital base. In the real estate sector this means that assets need to be of a high and sustainable quality and they need to be properly managed. We are fortunate that fellow MMI subsidiary Eris Property Group oversees the development and management of MAREF's assets. Eris has a 30 year history in African property, so it can apply its considerable experience to MAREF's assets for the benefit of our investors. The importance of factors such as designing practical yet aesthetically pleasing buildings and paying meticulous attention to cost control cannot be over emphasised. These skills are unique to the real estate sector and they can only be learned through hard lessons over a considerable period of time.

Another key factor in creating a sustainable portfolio yield from Africa is geographical diversification. While it is often viewed as a single bloc, Africa is a continent of 54 countries with very different economies and political cycles which provides a degree of diversification.

Due to the challenges inherent in the market, MAREF is currently an institutional fund. However, we hope that the future funds will be accessible to sophisticated retail clients. The market will adapt slowly but as early adopters in this space we will be very well placed to provide access when the local markets – and our investors – are ready.

The Marketplace

- Brent crude oil finished the week at \$72.9 a barrel, down 0.5%
- Gold was down 0.3% to \$1211.7 an ounce
- Market sentiment turned risk-off last week
- Trumps ever expanding tariff regime dominate the global picture

Market Focus

US

- The Dow Jones index fell 0.6% closing at 25313
- The Nasdaq 100 rose 0.2% to 7408.3
- US CPI rose 2.4% from a year earlier: the highest core inflation rise in ten years. Over the past month, both main and core CPI rose 0.2%. Points to continuing quarterly rate hikes
- The S&P heading towards 3000 and almost back to its all-time high

UK

- GBP at 11 month low Tuesday at \$1.292 as Liam Fox puts chances of a no-deal Brexit as high as 60%, though some EU member states have signalled a willingness to allow the UK to remain in the single market for goods

- UK GDP rebounded to show an increase of 0.4% between April and June. Unemployment at a 40 year low
- Retailer House of Fraser is rescued from administration by Mike Ashley of Sports Direct. He purchased the ailing retailer for £90m
- The FTSE 100 finished the week flat at 7667

Europe

- The Eurostoxx 50 fell 1.6% to 3426
- The Turkish Lira fell to an all-time low of 6.3 on Friday (-19.2% intraday) after a surge in inflation and deteriorating relations with the US. Trump to double steel and aluminium tariffs
- European banks came under pressure last week, with BBVA, Uni Credit and BNP all falling more than 3% as a result of their exposure to the Lira
- New sanctions against Russia were announced by the US administration, destabilising the ruble

Asia

- The Nikkei was down 1% to 22298
- Both China's imports and exports were up in July . US to go ahead with additional 25% tariffs in late August and China will retaliate at the same levels
- Iran to face cuts in oil exports of 1M barrels per day, roughly 50%, as the US plans to introduce new sanctions
- The Hang Seng rose 2.5% to 28366

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Asset Class/Region	Currency	Currency returns			
		Week ending 10 Aug. 2018	Month to date	YTD 2018	12 months
Developed Market Equities					
United States	USD	-0.2%	1.2%	6.8%	17.8%
United Kingdom	GBP	0.6%	0.1%	2.4%	7.3%
Continental Europe	EUR	-1.1%	-1.4%	1.1%	4.1%
Japan	JPY	-1.3%	-2.7%	-4.3%	8.6%
Asia Pacific (ex Japan)	USD	0.8%	-1.1%	-4.1%	5.3%
Australia	AUD	0.7%	0.0%	5.7%	13.8%
Global	USD	-0.7%	-0.3%	3.0%	12.4%
Emerging markets equities					
Emerging Europe	USD	-7.5%	-9.1%	-14.0%	-6.0%
Emerging Asia	USD	0.9%	-1.1%	-5.2%	5.5%
Emerging Latin America	USD	-6.7%	-6.1%	-7.7%	-4.3%
BRICs	USD	-0.4%	-2.6%	-5.5%	5.8%
MENA countries	USD	-0.5%	-0.5%	10.2%	9.4%
South Africa	USD	-5.1%	-6.7%	-17.6%	-2.2%
India	USD	-0.2%	0.3%	1.3%	9.4%
Global emerging markets	USD	-1.0%	-2.5%	-6.7%	2.9%
Bonds					
US Treasuries	USD	0.6%	0.7%	-1.0%	-1.2%
US Treasuries (inflation protected)	USD	0.6%	0.7%	0.0%	1.0%
US Corporate (investment grade)	USD	0.3%	0.6%	-2.1%	-0.4%
US High Yield	USD	0.1%	0.4%	1.5%	3.5%
UK Gilts	GBP	0.8%	1.1%	0.8%	0.5%
UK Corporate (investment grade)	GBP	0.6%	1.1%	-0.8%	-0.4%
Euro Government Bonds	EUR	0.3%	0.2%	0.2%	0.4%
Euro Corporate (investment grade)	EUR	0.3%	0.5%	0.1%	0.6%
Euro High Yield	EUR	0.1%	0.1%	-0.2%	1.2%
Japanese Government	JPY	0.1%	0.0%	-0.2%	0.2%
Australian Government	AUD	0.9%	0.5%	2.5%	3.4%
Global Government Bonds	USD	-0.1%	-0.5%	-2.0%	-1.6%
Global Bonds	USD	-0.2%	-0.5%	-2.1%	-1.3%
Global Convertible Bonds	USD	-0.2%	-0.2%	-0.7%	0.8%
Emerging Market Bonds	USD	-2.2%	-2.5%	-6.7%	-5.4%

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Asset Class/Region	Currency	Currency returns			
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Property					
US Property Securities	USD	-1.5%	1.5%	1.0%	3.4%
Australian Property Securities	AUD	1.1%	1.9%	3.0%	9.3%
Asia Property Securities	USD	0.7%	-3.0%	-4.5%	0.2%
Global Property Securities	USD	-1.0%	-0.6%	-1.3%	4.2%
Currencies					
Euro	USD	-1.7%	-2.7%	-5.2%	-3.0%
UK Pound Sterling	USD	-2.1%	-3.0%	-5.7%	-1.8%
Japanese Yen	USD	0.5%	0.2%	1.7%	-1.3%
Australian Dollar	USD	-1.5%	-1.5%	-6.6%	-7.5%
South African Rand	USD	-5.5%	-6.4%	-11.9%	-4.6%
Swiss Franc	USD	-0.3%	-0.7%	-2.2%	-3.2%
Chinese Yuan	USD	-0.1%	-0.6%	-5.1%	-3.0%
Commodities & Alternatives					
Commodities	USD	-0.7%	-1.6%	2.3%	11.7%
Agricultural Commodities	USD	-2.1%	-1.7%	-0.8%	-2.2%
Oil	USD	-0.5%	-2.9%	8.9%	40.3%
Gold	USD	-0.3%	-1.0%	-7.2%	-5.6%
Hedge funds	USD	0.1%	0.1%	-0.9%	2.2%

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