

Time for a re-rating?

Conservative approach pays off in turbulent times

THE SHARE PRICE PERFORMANCE of retail-focused property stock Fountainhead hasn't exactly shot the lights out in recent years. However, the counter is now starting to appear on fund managers' stock pick lists. Ironically, the very reasons why some investors shunned Fountainhead during the bull market – its rather conservative management approach and low gearing – are now key attractions.

Analysts say currently turbulent times are prompting a move away from high risk, high growth funds towards lower risk counters with solid, albeit less exciting, real estate portfolios. As Coronation Fund Managers' property analyst Anton de Goede puts it: "In an uncertain market certain income streams become more important."

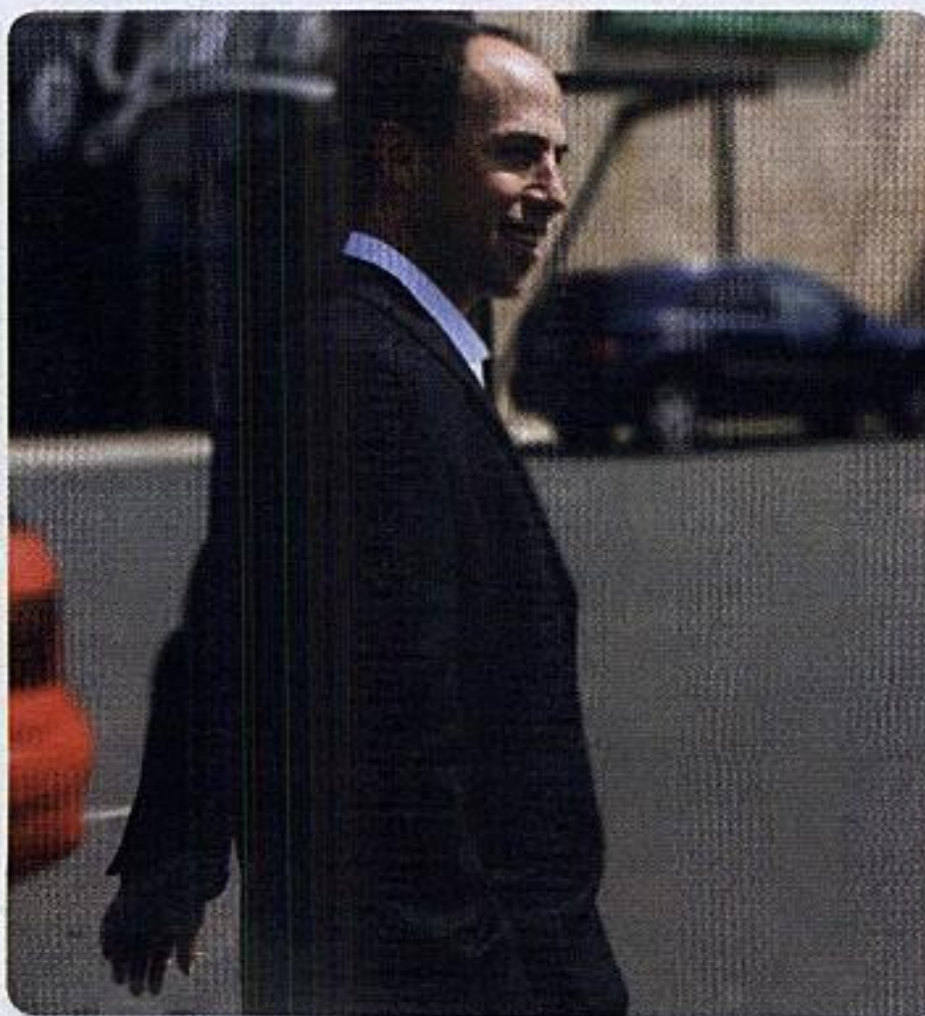
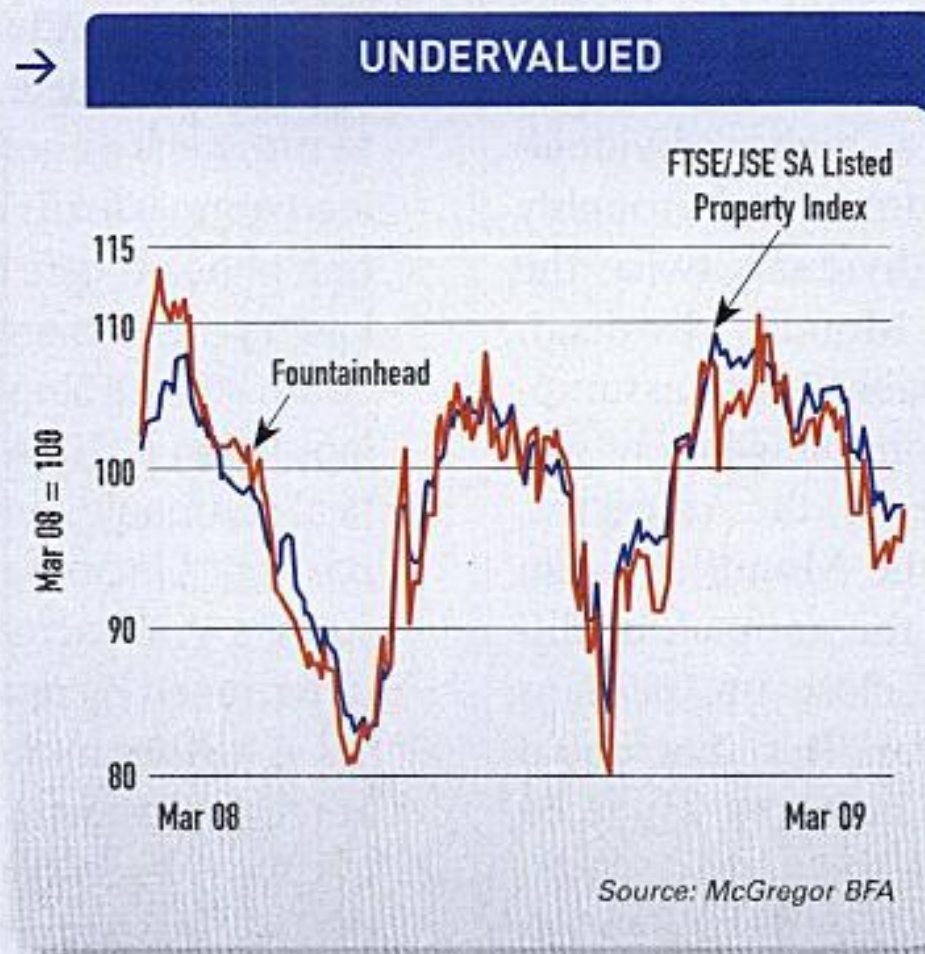
De Goede says the fact Fountainhead offers a sizeable exposure to regional shopping centres negates the risk of any negative income surprises over the short term. Fountainhead's R7,3bn property portfolio includes Centurion Mall, Westgate Shopping Centre (Roodepoort), Kenilworth Centre (Cape Town), The Boulders (Midrand), Benmore Shopping Centre (Sandton) and Brightwater Commons (Randburg).

Stanlib Property Franchise's Evan Jankelowitz has a similar view. "Quality of earnings has now become first prize. Fountainhead has notoriously been ultra conservative from both a balance sheet perspective and what it recognises as profits. While the company may have lagged in the bull market, this play will be more robust in a slower economic environment."

"It's becoming increasingly important for investors to focus on the quality of underlying property portfolios and strength of management teams instead of short-term stock market performance."

Jankelowitz says the involvement of the Liberty Property Group in the management of Fountainhead, as well as recent board changes, are also likely to unlock value. Liberty bought a 50% stake in Fountainhead's management company from Standard Bank in March 2008.

More recent management reshufflings include the appointment of Anton Raubenheimer in November last year to replace long-standing MD John Rainier. It appears Raubenheimer has a more opportunistic approach



In search of buying opportunities.
Anton Raubenheimer

than his predecessor, with plans to bulk up Fountainhead's existing portfolio through new acquisitions. That's a clear shift away from its former investment strategy, where money was spent primarily on expanding and improving existing properties.

Raubenheimer concedes he's looking for new growth opportunities and hopes to spend around R1bn over the next 12 months to expand Fountainhead's existing portfolio of 66 properties. Says Raubenheimer: "Over the past few years property was too expensive, so Fountainhead didn't grow through acquisitions. Besides, investing in your own properties

– where you know exactly what the demand for floor space is – offered better returns than adding unfamiliar stock to the portfolio."

But the fact that commercial property prices are starting to come down has necessitated somewhat of a change in strategy, says Raubenheimer. He's now looking to add large properties valued at a minimum of R100m to Fountainhead's existing portfolio. Raubenheimer is quick to add that growth will be pursued in a measured way and notes management won't forego its conservative accounting and gearing policies. "We won't be buying any old building just for the sake of growth. We're looking for value propositions with quality leases in place."

Unlike most other retail-focused property funds that expect an increase in vacancies over the next six to 12 months, Raubenheimer is confident that the vacancy rate of the fund's properties (around 6%) will improve. That's mainly on the strength of new leases signed at the struggling Brightwater Commons (former Randburg Waterfront).

Vacancies at what Raubenheimer describes as one of Fountainhead's more "challenging" properties have been halved with the introduction of new tenants towards late 2008, including Woolworths, Ackermans and a state of the art Virgin Active gym. Vacancies are down from 30% to 16%. Foot traffic has already increased, which Raubenheimer hopes will act as a catalyst for a further uptake of empty space over the next few months. The fact Fountainhead doesn't have a development pipeline of new properties that need to be filled also places less pressure on vacancy levels.

Fountainhead declared 12% growth in distributions for the year to end-September 2008. Management expects distribution growth to slow to 8% for the 2009 financial year, which is roughly in line with analysts' 8% to 10% growth forecast for the sector as a whole this year.

However, at a forward yield of around 10%, Fountainhead looks cheaper than some of its retail-focused peers, such as Hyprop Investments and Resilient Property Income Fund that are trading at yields closer to 8%.