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Results put trusts in firing line

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The interim reporting season for listed property trusts is expected to be one of the most divided the sector has experienced, as many developers are tipped to report weak corporate earnings. Trusts such as Multiplex Group and Mirvac Group as well as developers like Lend Lease and Australand Property Group will be in the firing line. But the property analysts at UBS expect double-digit growth in earnings per security from GPT Group, stemming from its internalisation of the trust management and joint venture with Babcock & Brown. Macquarie Goodman Group is also expected to post earnings growth above 10 per cent, and the UBS analysts are also tipping upgrades from Centro Properties Group and Stockland.

UBS has forecast strong growth in distributions per security for the sector of 4.9 per cent, against 4.4 per cent last year, but weaker growth in earnings per security of just 1.3 per cent compared with 6.9 per cent last year. The UBS team has also predicted disparity across the different sub-sectors, forecasting that growth in earnings per security would be solid in retail (up 4.3 per cent), strong in industrial (up 7.2 per cent), while the office sector (up 2.2 per cent) would recover. There is nervousness, however, about the performance of property developers.

Australand reports today. It is expected to post flat year-on-year group net profit of about \$146million. Investors will be looking hard at sales and margins. "We're still expecting development profits will be down for a lot of companies in this reporting period," Macarthur Cook's head of property securities, Craig Turnbull, said.

Mr Turnbull said investors had also been worried about retail trusts, as sales had slowed over the course of last year. "However, there have been reports from Centro and [Macquarie] CountryWide that suggest that people who know what they're doing are still getting good growth," he said. Mr Turnbull said the listed property sector was still reasonable value relative to the broader market.

UBS estimates it is trading on a forward yield of 7.1 per cent, with distributions per security likely to grow at 3.8 per cent a year over the next five years. Michael Doble, manager of property securities at APN Funds Management, said: "The themes to date are a weakening residential cycle ex-west coast ... [and] we're probably expecting a better outlook for the office market." Mr Doble said retail trusts had been "steady as she goes" and Centro had given investors an inkling of a broadly solid performance. But he cautioned that "the bogey in the background is corporate earnings risk".

Macarthur Cook's Mr Turnbull agreed there had been excitement about office markets, as Perth and Brisbane had been "flying" for a while and Sydney and Melbourne were getting moderate rental growth. But he did not expect a big impact on earnings. "We don't think it's going to come through quickly because of the long-term lease structures," Mr Turnbull said.

Investors looking for the earnings surprises - on the upside - should instead look to trusts with growing funds management businesses. Mr Turnbull said that Centro and

Stockland were experiencing a lot of demand for their funds, which was a positive story. Looking further ahead, Maxim Asset Management's investment director, Winston Sammut, said he expected a 9 per cent return for the listed property securities for calendar year 2006.

He said commercial property should deliver returns of between 10per cent and 12per cent for the year, followed by hotels and then industrial trusts.

He expects the retail subsector and diversified trusts to lag.

High-yielding US-invested trusts are not expected to be the usual safe haven for investors. CSFB analyst Andrew Rosivach has identified US interest rate levels as a risk to the trusts' future earnings. He expects the biggest hits to come with the longer-term rollover of debt and capital hedges set when US long-term rates were lower. "Most listed property trust offshore debt was originally issued as medium-term fixed-rate debt, creating interest-cost time bombs in the balance sheets of offshore-listed property trusts," Mr Rosivach said.

He said that across trusts which had borrowed in US dollars, earnings per security would grow a measly 1 per cent per annum after 2006. Mr Rosivach said that the risks to the earnings of US-invested trusts would also increase. Macquarie CountryWide had the highest sensitivity to US interest rates, followed by Macquarie DDR Trust and Galileo Shopping America Trust, he said.