Financial Mail, Property Handbook 2023: Fairvest

Fairvest is a diversified real estate investment trust (Reit) listed on the JSE, with a South African-focused portfolio worth R11.9bn. It holds a 5.1% interest in Dipula Income Fund and a 60.9% interest in Indluplace Properties.

The group is geographically well diversified, with the portfolio covering all nine South African provinces. However, Gauteng, Western Cape, KwaZulu-Natal and Eastern Cape contribute about 78% of the revenue. In terms of sectoral diversification, the Reit was predominantly exposed to the retail sector before the merger in October 2021 between Arrowhead and Fairvest. The merger diluted the retail exposure but has resulted in a larger, more tradable company from which value can be unlocked - both operationally and through capital allocation.

Fairvest now generates 67% of its revenue from retail, while offices and industrials contribute 22% and 11% respectively. The company ultimately wants to recycle out of the office, industrial and residential assets to become a retail specialist Reit. It will look to refocus towards lower LSM and convenience retail assets in rural and nonmetropolitan areas. This sub-sector proved resilient during Covid and has continued to deliver robust results. The lower LSM consumer market, supported by grants and the impressive informal economy dynamics, underpins the portfolio’s turnover growth. This has driven demand for rental space from strong tenants such as Shoprite and Checkers, Pick n Pay, Boxers, Pepkor and The Foschini Group. The retail portfolio has built-in escalations of about 6.5%, a 90.1% tenant retention rate, a 4.3% vacancy rate and 2.3% reversions.

The Reit’s industrial assets have delivered a positive performance. However, the office portfolio continues to be a drag on overall performance. The portfolio vacancies are at 5.96%, driven primarily by the elevated (but improving) office vacancy of 13.6%. Tenant retention is at 90.7%, which is a focal point for the company. The reversions are positive at 1.8%, up from -6.4% in September 2022 and escalations are robust at 6.6%. Continued positive performance will be driven by management’s focus on improving vacancies, disposing of noncore assets and capital investment.

The company’s investment portfolio valuations are anchored by a 9.5% average yield and recent disposals achieved a premium to book values. Fairvest’s loan-to-value (LTV) ratio has increased to 38.4%, but this still meets the market preference of below 40%. It is targeting a hedged percentage of 70% and, with 58% of those hedges expiring this year, the company would be exposed to substantial interest rate risk.

This risk has, however, been mitigated as the proceeds of R651.4m from the sale of its stake in Indluplace to SA Corporate Real Estate will be used to cut its LTV ratio by at least 5%. Apart from de-risking the balance sheet, the proceeds from the recycling of assets will be used to reinvest in existing assets and solar installations as well as to buy back shares, which are income accretive. In March, Fairvest bought back 32.5-million B shares. It has reaffirmed a distributable earnings per B share of 40.5c42c a share for the 2023 financial year on a 100% payout ratio against a backdrop of a weak South African economy, higher interest rates and sustained load-shedding. ***Ross Reid, equity analyst, Metope Investment Managers***