

Opportunities offered by interest rate increase

Interest rates have begun to increase after a period of record lows that have seen the listed property sector outperforming all asset classes. An increasing interest rate cycle brings opportunity to property funds as private property owners tend to have far higher loan to value profiles and increases in interest rates exert tremendous pressure on these owners.



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Marc Edwards, CEO of Tower Property Fund explained that increasing interest rates could see a correction in pricing in the private property space. "In the second quarter of last year the listed property sector experienced a pricing correction due to the announcement of the tapering or quantitative easing in the US. This sent a shock wave through emerging markets, resulting in certain property sectors falling by as much as 30% in May of last year. This pricing correction, however, did not flow through to the private market where property prices remained at all-time highs. Interest rate increases should put pressure on over-borrowed private owners, forcing them to sell at realistic prices."

Attractive properties at more realistic prices

Edwards advised that Tower is starting to see some attractive properties at more realistic prices, although he feels that pricing could still be more competitive. "Investors could see new private properties being purchased by funds in the next 12 months, due to the interest rate pressure."

Given the exposure to debt for property companies, investors often get nervous when interest rates increase. However, most listed property companies have excellent "fixing" profiles where their interest rates are fixed for fairly long periods - normally two years, so the effect of interest rate volatility is limited.

"Tower recently took advantage of a lower yield curve to fix a larger percentage of its debt and Tower now has 71% of its debt fixed, which management considers prudent," concluded Edwards.

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