AREITs earnings yield update – April 2020

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Australian real estate investment trusts (AREITs), as represented by the S&P/ASX 200 REITs Index, returned 13.7% in the month ending 30 April 2020. The AREIT index outperformed the S&P/ASX 200 return of 8.8% over the month. These returns represent a modest recovery after the record declines in the market due to the coronavirus restrictions in March.

Over the 12 months to April 2020, AREITs posted a total return of -20.3% (11.2% lower than the S&P/ASX 200 return of -9.1%).

Sector Performance

Table 1 below shows the performance of AREITs for various periods ending 30 April 2020.

Table 1 – S&P/ASX 200 AREIT Accumulation Index Performance: Total Returns (30 April 2020)

	1 Month (%)	3 Months (%)	6 Months (%)	1 Year (%)	3 Years (% p.a.)	5 Years (% p.a.)
Total Return	13.7	-29.8	-27.0	-20.3	-1.8	3.0
Volatility				41.0	24.7	20.9

Source: S&P/ASX 200 AREIT Accumulation Index (2020)

The restrictions arising from the pandemic have had a substantial impact on the medium-to-long term performance of the AREIT sector. Over the 3 years and 5 years to the end of April, the sector produced total returns of -1.8% and 3.0% per annum respectively.

Sector returns in April were led by Retail AREITs with 29.6%, followed by Industrial AREITs with 8.4%, Office AREITs with 1.7% and Diversified AREITs with -11.4%. These returns reflect the recovery after the steep declines in March. Retail AREITs led the other sectors this month after declining -46.3% in March.

Table 2 below shows the income performance of AREITs for various periods ending 30 April 2020.

Table 2 – S&P/ASX 200 AREIT Accumulation Index Performance: Income Returns (30 April 2020)

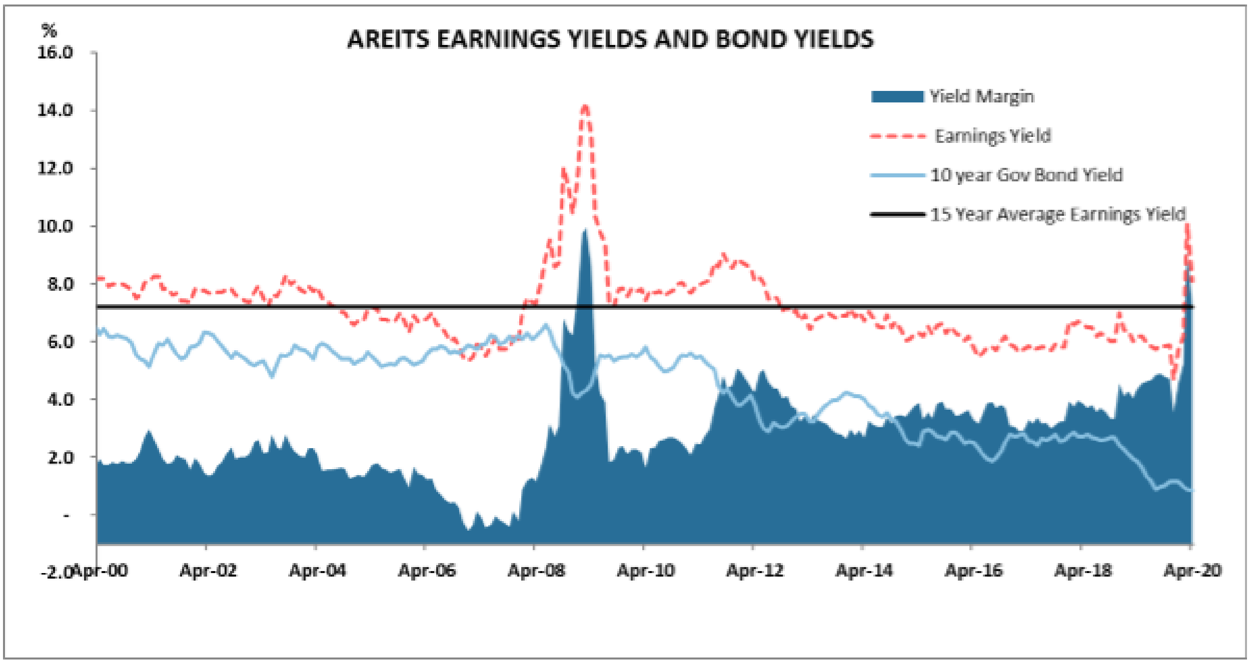
	1 Month (%)	3 Months (%)	6 Months (%)	1 Year (%)	3 Years (% p.a.)	5 Years (% p.a.)
Income Return	0.0	0.6	2.1	4.5	4.8	4.8
Volatility					2.1	2.1

Source: S&P/ASX 200 AREIT Accumulation Index (2020)

The income component of the total return was 4.5% for the 12-month period to April 2020. The annual volatility of income returns was 2.1%, which is low when compared with other asset classes.

The AREIT sector was trading at an earnings yield of approximately 8.1%, which was higher than yields of both cash and Commonwealth Government bonds at the time. The premium to Australian 10-year government bonds was 7.24%.

Chart 1– AREITS Earnings Yields Compared to Bond Yields



Source: RBA, UBS (2020)

The change over time of the spread between the earnings yield of AREITs and the 10-year government bond yield is shown in Chart 1.

Market Review

April saw a modest recovery for the ASX200 as the Federal Government, state governments and businesses implemented policies to limit the spread and navigate the economic difficulties of the pandemic. The AREIT Retail sector saw a 29.6% increase in its return after the 46.4% decline in March. Its significant decline was likely due to the immediate closing of stores due to the implementation of restrictions, while the increase in April was likely due to plans for the economy's reopening and investors seeing potential value in retail AREITs which were mostly trading at a heavy discount to NTA.

The swing in the earnings yield as depicted in Chart 1 is to be expected due to the large swing in AREITs prices over March and April. Earnings yields are heavily impacted by strong changes in the price as earnings are reported twice per year. Therefore, in March, the steep drop in the price boosted the earnings yield and it will slowly decline as both AREIT prices recover and earnings adjust after reporting at the end of June. Reported earnings are likely to decrease due to store closures and state government policies implemented to protect tenants (i.e. codes of conducts, rent waivers). Chart 1 supports this idea, with the sharp decline in the earnings yield over April. A similar impact can be observed over the GFC, where 2008-2009 saw a sharp increase in the earnings yield, followed by a sharp fall in 2009-2010. The earnings yield is seemingly following the same pattern during this market crisis.