

Discovery Flexible Property

31 January 2025

Market background

It was a dramatic start to the year as Donald Trump's inauguration was swiftly followed by a record number of executive orders reinforcing his "America First" agenda. Despite rising trade tensions, financial markets navigated a volatile month to end broadly higher, with gains across gold, government bonds, and global equities.

Global equities started strong, though leadership shifted, with Europe outperforming the US. However, the month was punctuated by three distinct bouts of volatility, reflecting the caution that tempers optimism. Inflation concerns resurfaced early on, casting doubt on the number of rate cuts the US Federal Reserve will deliver this year. Sector performance was largely positive, with communication services and health care leading gains, while technology lagged. In South Africa, the FTSE/JSE ALSI delivered a positive return, driven by a significantly stronger resources sector. Gold benefitted from heightened geopolitical uncertainty, while China's latest round of economic stimulus provided additional support for commodities, lifting South Africa's resources sector to an impressive 16.1% return. The South African Reserve Bank continued its rate-cutting cycle, lowering the repo rate to 7.50%.

Performance review

For the month, the fund outperformed the benchmark.

Offshore listed names outperformed local counters in January, reversing the trends seen in 2024. Contributing to performance was the portfolio's exposure to off-benchmark offshore counters across subsectors and geographies, such as European retail player Unibail-Rodamco-Westfield and logistics name Tritax Big Box REIT. In South Africa, underweight exposure to predominantly domestic companies, such as Growthpoint Properties, also contributed positively to performance.

Outlook and strategy

We expect a decent year for local listed property in 2025. While the majority of the rerating has probably already occurred, fundamentals for the sector appear reasonably favourable. Prospects are clearly very closely tied to the anticipated economic recovery in South Africa, which is continuing to make progress. Any disruptions or noise, as we saw in the early part of this year, will impact sentiment in the short term. However, fundamental trends such as higher competition for space in light of limited supply are likely to persist and lead to reduced negative reversions and, therefore, growth in rental income.

Dividend sustainability also looks much improved with many companies having restructured their balance sheets, and current dividend streams are well covered by operational income. Against the backdrop of moderately declining local interest rates, this should provide a favourable environment for decent returns in 2025. With anticipated income returns in the region of 8-9% on average, which is likely to be bolstered by some growth and marginal rerating, we see low double-digit returns as an achievable target for the sector this year. We continue to see select opportunities in domestically orientated names exposed to retail and industrial subsectors, while the UK retail names also offer an attractive combination of yield, growth, strong balance sheets and accelerating improvement in fundamentals.