Discovery Flexible Property

30 November 2024

Market background

It was a mixed month for global capital markets. In the US, President-elect Donald Trump's decisive victory at the polls propelled US equities to new highs. In China, capital markets faced downward pressure due to concerns over the possibility of trade tariffs under the new Trump administration. Sentiment towards South African equities also declined, given the strong trade relations between the two economies, which was further compounded by weaker-than-expected domestic indicators. Other noteworthy events in South Africa included the SARB cutting its key interest rate by 25 basis points and S&P Global upgrading the country's credit rating outlook to 'positive'. In commodity markets, gold declined on the prospect that Trump's policies could re-stoke inflationary pressures and cause US interest rates to remain higher for longer. In energy markets, OPEC+ members postponed their plan to increase oil production until the end of the year. Despite the conflict in the Middle East threatening supply, oil has declined in recent months on the back of lingering macro concerns, specifically over the outlook for Chinese demand.

Performance review

For the month, the portfolio outperformed its benchmark.

Among the largest contributors to relative performance for the month was the portfolio's overweight exposure to the dominant, high-quality retail player, Hyprop Investments REIT, following the restructuring of its African exposure and simplification of its Eastern European business. Conversely, the portfolio's overweight exposure to Resilient REIT, another high-performing retail-focused business, detracted from performance.

Outlook and strategy

The sharp increase in interest rates over 2022 and into 2023 resulted in a steep derating of the listed property sector, both locally and abroad. However, as increased rhetoric regarding monetary policy easing entered the fray in late 2023, property globally benefitted as interest rate sensitive instruments rerated. The property market has been further supported by the US Federal Reserve (Fed) initiating its rate cutting cycle, together with soft but not collapsing economic data out of the US.

In our view, the improving fundamentals support current valuations. However, the total return outlook depends heavily on ratings remaining stable on the back of a loosely predictable cutting cycle without massive geopolitical surprises. Looking forward, total returns will be underpinned by income yield and growth, with the sector having enjoyed significant rerating in the second half of the year. We believe the sector offers attractive value over a medium- to long-term time horizon, primarily underpinned by a more sustainable cash-covered yield, together with a supportive valuation that reflects near-term operational and balance sheet concerns.

In the current environment, we continue to assess the portfolio risks and actively screen for opportunities that market dynamics such as these are likely to offer. Ultimately, we aim to provide our clients with the best risk-adjusted medium- and long-term outcomes.