Discovery Flexible Property

30 June 2026

Market background

Conflict in the Middle East dominated sentiment over the quarter, with the closure of the Strait of Hormuz and associated oil market disruption stoking fears of a resurgence of inflation.

In the US, headline CPI climbed to a three-year high of 4.2%, fuelling expectations of rate hikes and driving a sharp bond market sell-off mid-quarter, with the 30-year Treasury yield rising to a level last seen in 2007. An abrupt shift came towards quarter-end as a 60-day ceasefire took hold, sending oil prices sharply lower and easing inflation fears. Against this backdrop, the US Federal Reserve (Fed) kept rates unchanged over the quarter.

South African markets were not insulated from the geopolitical events, with the Middle East conflict the dominant driver across asset classes. Domestic bonds sold off sharply mid-quarter in response to rising inflation expectations and geopolitical uncertainty, before recovering strongly as ceasefire negotiations progressed, leaving the ALBI in positive territory for the full period. The macro backdrop provided further support: GDP growth in the first quarter came in ahead of expectations, and South Africa received sovereign credit rating upgrades from both Moody’s and Fitch.

The South African Reserve Bank (SARB) raised the repo rate by 25 basis points to 7% at its May meeting. The decision was driven primarily by headline CPI moving toward the upper end of the target band and concerns over potential second-round inflation effects stemming from the energy shock. The rand initially weakened but retraced much of the sell-off by quarter-end as terms-of-trade conditions stabilised.

Performance review

The portfolio outperformed its benchmark for the quarter.

The largest contributor to performance was the portfolio’s overweight position in SEGRO, following a takeover approach from Prologis, which resulted in a significant re-rating of the share price and improved sentiment across the broader UK listed property sector. Hammerson also benefitted from this positive market backdrop.

Locally, our overweight positions in Hyprop, Redefine and Vukile contributed positively as declining bond yields, improving property fundamentals, and attractive valuations supported a broad-based recovery across the South African listed property sector.

On the negative side, Prologis detracted from relative performance following a softer June after delivering strong year-to-date returns. Despite the short-term weakness, we continue to view the company favourably, supported by its high-quality logistics portfolio and growing exposure to the structural demand for data centre infrastructure.

Our overweight position in Resilient REIT also detracted after a period of strong share price performance resulted in a modest valuation-driven pullback. Having reduced the position following its strong run, we believe the recent weakness has improved the valuation and may present an opportunity to rebuild the position over time.

Our underweight position in Lighthouse Properties also detracted during the quarter. While the share price recovered over the period, we continue to favour alternative offshore property companies that offer stronger liquidity, broader portfolio diversification and more attractive relative value.

Outlook and strategy

Following a strong performance in 2025, the listed property sector has continued to benefit from firmer operational delivery and improved balance sheet discipline. The anticipated improvement in the domestic bond environment has provided further support to the sector. Looking ahead, we expect this positive momentum to persist, underpinned by resilient fundamentals and no imminent interest rate headwinds.

Although valuations have recovered meaningfully, the sector continues to offer a compelling combination of income yield and growth. On a relative basis, listed property remains favourably positioned within the context of the domestic bond market.

Underlying fundamentals continue to improve. Tenant demand is normalising; vacancies are trending lower and rental reversions are stabilising across most retail and industrial segments. The office sector remains more challenged; however, pockets of recovery are emerging, particularly in well-located, energy-efficient buildings.

Encouragingly, several REITs are normalising towards higher payout ratios as balance sheets strengthen and interest cover ratios improve. This supports both dividend yield sustainability and future growth prospects.

Macro conditions remain an important driver of sentiment. While geopolitical risks continue to rise, the sector's bottom-up fundamentals remain constructive. Combined with a stable rand and contained inflation, the ratings outlook for SA-listed property should remain stable, with potential for further improvement. Selective offshore exposure continues to provide diversification benefits alongside solid operational momentum.

Against this backdrop, the portfolio remains positioned towards domestically focused counters offering sustainable income visibility, strong management execution and disciplined capital allocation, while maintaining selective exposure to higher-growth international opportunities.