

Discovery Global Real Estate Securities Feeder Fund

Q1 2023 Performance Commentary

During the first quarter of 2023, the fund outperformed the benchmark by 161bps, increasing by 2.39% while the benchmark increased by 0.78%. The positive performance was driven mostly by the first and second bites of the apple, namely country and sector, which increased by 82bps. The third bite, namely stock selection, increased relative performance by 67bps. Currency effects had a marginal positive impact of 12bps. REITs started the year with stellar performance on positive macro data, including lower inflation and higher than expected GDP growth in the US. However, REITs corrected during February and March as the data became less favourable and the markets became concerned with the ability of REITs to roll over debt, alongside concerns over bank CRE exposure.

For the first bite of the apple, outperformance was driven by our overweight positions in the UK and Australia. We maintain our overweight position in the UK and Europe as valuations are attractive, and interest rates are likely to peak in the next 3-6 months. We are overweight Hong Kong as the SAR should benefit from China reopening. We remain underweight the US and Japan as valuations are relatively less favourable, and economic headwinds persist. We are keeping a close watch on peak inflation and interest rates, and we expect that there will be opportunities in the medium term as markets trough.

For the second bite of the apple, our overweights in healthcare, industrials and data centres worked well as demand in these sectors remains strong and supply is quite tight. We are also marginally overweight malls as the sales data remain solid and valuations attractive. We remain cautious on the residential sector as affordability is poor given higher mortgage rates and prices, while supply remains elevated. We are underweight net leases, offices, shopping centres, storage and lodging as fundamentals are less favourable as highlighted during the recent earnings season. We recently increased our weighting on offices as valuations were over three standard deviations below their mean, but this has yet to add positively to performance.



Leading the fund's individual stock contribution was Life Storage, the US storage company, which rallied 33% on the news of it being acquired by Extra Space Storage. The second-best performer was CubeSmart, another US storage stock, which appreciated by 15% as the sector outperformed. The third best performer was Hammerson, the British retail stock, which appreciated by 12%. The worst performer in 1Q23 was Hudson Pacific, a US office company, which was down 32% as its Silicon Valley tenants faced the fall-out from the Silicon Valley Bank implosion. German residential giant Vonovia fell 20% as they cut their dividend in half and investors fretted about their ability to roll over their debt. Boston Properties, the blue-chip US office stock, also fell 20% as office vacancies across the US remain elevated due to work from home and office job losses.

Inflation data continue to weigh on the markets as rates could be higher for longer, and bank lending growth is unlikely to pick up in the near-term. That said, valuations in many cases are close to Global Financial Crisis (GFC) lows, and stocks tend to bottom when GDP growth is most negative, which will likely be 2H23. We expect markets to remain volatile and quality assets to outperform in these uncertain times. We remain nimble, and will try to take advantage of the opportunities presented.

*Commentary is based on USD returns, gross of investment charges, as at close of US markets (16h00 EST) on the last trading day of the month. This may differ from ZAR returns, which is shown net of investment charges, as at 15h00 CAT on the last trading day of the month.