

Discovery Diversified Income

28 February 2026

Market background

Amid the volatile equity market backdrop, US Treasury yields declined, supported by their safe-haven characteristics. US economic data released during the month was mixed, with labour market and inflation prints sending somewhat conflicting signals. Inflation data was similarly uneven. Headline CPI printed lower-than-expected at 2.4% year-on-year, but core PCE inflation rose, pushing the annual rate to 3.0%. On the growth side, fourth-quarter GDP was weaker than expected, as the impact of the government shutdown proved larger than anticipated. Towards month-end, fiscal uncertainty resurfaced following the US Supreme Court ruling on tariffs. Overall, despite a mixture of signals, markets interpreted the overall backdrop as dovish and is pricing in at least two rate cuts by the end of 2026.

Locally, Finance Minister Enoch Godongwana delivered the 2026 National Budget, signalling a potential turning point in South Africa's public finances. The budget deficit has narrowed, and national debt is projected to have peaked, marking the end of 17 consecutive years of debt accumulation. The Minister highlighted stronger-than-expected revenue collection, ongoing fiscal consolidation efforts, and a commitment to expenditure discipline. These developments support an improving medium-term fiscal outlook and enhance policy credibility as the government continues to deliver a primary surplus. The bond market responded positively to the budget statement, with longer dated bond yields falling. The rand strengthened and remained relatively resilient on the back of improving fiscal indicators and broader positive sentiment towards South African assets, finishing the month at R15.94 to the US dollar.

Inflation edged slightly lower in January to 3.5%, partly due to reduced transportation costs, which is reflective of a decline in petrol prices. Food inflation, however, ticked higher, driven by elevated meat prices amid persistent supply constraints linked to the ongoing outbreak of foot-and-mouth disease affecting cattle in parts of the country. Overall, inflation remains well behaved, providing policymakers with some flexibility as they balance growth considerations against global inflation risks.

Performance review

The portfolio outperformed its benchmark over the month.

Performance was boosted by our position in long-term South African government bonds, where yields declined more sharply than those with shorter maturities. We also benefitted from the rebound in the listed property sector and from our holdings in investment-grade credit.



Outlook and strategy

The outbreak of war in Iran at the end of February underscores the fragile geopolitical backdrop and the speed at which regional tensions can escalate. The conflict has altered the near-term outlook, as heightened risks to energy supply, particularly through key transit routes, have pushed oil prices higher and introduced additional volatility. Should hostilities intensify or disrupt supply channels more materially, the resulting energy shock could place renewed pressure on inflation and weigh on global growth. We continue to monitor developments closely and will assess their implications for portfolio positioning as the situation evolves.

The added uncertainty may prompt the South African Reserve Bank (SARB) to err on the side of caution; however, this will depend on how long the conflict lasts and the extent of its impact.

Duration

Duration exposure was reduced during the month as we sold down some positions and took a coupon dilution.

Curve positioning

We continue to hold an overweight position in the long end of the yield curve, where we still believe there is potential for further flattening following the positive budget statement.

Currency

Our foreign exchange allocation remains low, although we are retaining portfolio optionality amid the ongoing geopolitical uncertainty.

Property

We trimmed some of the portfolio's exposure to the listed property sector, taking profits on our positions which have performed well in line with the sector's recovery.

Inflation-linked Bonds

We continue to maintain a preference for nominal bonds over linkers given the benign inflation backdrop.

Credit

There is no change to our view on investment-grade credit, which has benefitted the portfolio. We remain attentive to attractive opportunities and will add exposure selectively.