Discovery

Discovery Balanced, Moderate and Cautious Balanced Funds

30 September 2026

Market context

Markets diverged in the third quarter. Equities held firm while bonds sold off as yields rose. A renewed US-Iran escalation lifted Brent crude by 42% from its end-June low, reviving inflation concerns. Central banks in the US, Eurozone and Japan raised rates in September.

Global equities made modest gains, supported by resilient growth and robust earnings. The MSCI ACWI returned 1.6% and the S&P 500 returned 2.2% in USD. US equities led, reaching a record in August as the Magnificent Seven rose and investors rotated from semiconductors towards “hyperscalers” and software names. The conflict re-escalation in September tempered risk appetite.

Europe lagged. The Stoxx 600 also hit a record in August but ended the quarter down 1.1%, as rising bund yields and energy-driven inflation concerns weighed in September. South Korea fell more than 20% after a very strong second quarter, as global semiconductor stocks unwound in July. Energy and technology led by sector, while utilities and real estate lagged as bond yields surged.

South African markets were shaped by the same forces. Equities ended the quarter marginally lower, with early gains unwinding later in the quarter. The FTSE/JSE All Share Index fell 0.3%: a rotation into precious metals lifted resources 12.8% over the quarter, but a rate hike by the South African Reserve Bank (SARB), surging oil prices and rising global yields weighed on markets in September.

Performance

Over the quarter, the portfolio delivered a flat absolute return. July and August added value, but September gave much of it back as a bond sell-off and the extension of the war pushed markets into risk-off mode.

Key contributors:

- Global equity: technology hardware, software, and large-cap technology, as the AI technology trade recovered after lagging in July. Energy and healthcare stocks also performed well.
- Diversified miners and precious metals stocks
- European banks: stellar results and sound fundamentals. They fell less than US banks in September and were not caught in the AI scare.
- Brazilian bonds: benefitted from high real yields and early election gains in the polls by Flavio Bolsonaro
- SA cash: earned a steady return while SA bonds and property sold off.

Key detractors:

- SA property: bond yields rose sharply and the sector gave back its early-year gains.
- SA bonds: renewed Iran-US escalation lifted Brent prices, renewing global inflation fears and triggering a global bond sell-off.
- SA equity: Naspers and Prosus fell on AI capex fears, MTN on negative headlines, and ‘SA Inc.’ stocks on higher bond yields.
- Offshore interest-rate-sensitive holdings: utilities and industrials in particular.

Discovery Life Investment Services Pty (Ltd): Registration number 2007/005969/07, branded as Discovery Invest, is an authorised financial services provider.

Moves in the quarter were extreme, and we traded around overbought and oversold positions rather than chasing the market. We sold Richemont to zero early on, after a strong run, and Goldman Sachs to zero as we rotated within financials. We also rotated within mining. We added to British American Tobacco, where our earnings expectations were ahead of the market and the share had been particularly weak, and topped up healthcare, Google and Meta on weakness. We also increased our Japanese equity exposure.

Outlook and strategy

The third quarter was eventful, even by this year's standards, and Q4 looks set to follow a similar pattern. Elections in Brazil, the US and South Africa are likely to bring significant noise and volatility. However, trying to anticipate and position for election outcomes and their policy implications is not in line with our process.

Instead, we continue to assess the outlook through our growth, inflation and policy framework. We remain somewhere between Goldilocks and Reflation. Earnings revisions remain positive, guidance remains sound, and there have been few signs of deterioration in company fundamentals. Oil prices have remained sticky, but without the second-round effects that would make this more concerning. That is important for next year, when more favourable base effects should help bring inflation lower.

The policy backdrop also remains supportive. Fiscal spending continues, China is signalling further accommodation, and the Fed is reassessing how it conducts monetary policy. Its five task forces are looking at inflation, the balance sheet, data, productivity and jobs, including the impact of AI. This is not about near-term rate moves, but it reinforces our view that the Fed is thinking about a changing growth and inflation environment. We continue to expect the hiking cycle to be shallow.

We remain constructive, although the backdrop is volatile. While our equity exposure is high, we do have cash to deploy if opportunities emerge. South African equities have had a particularly difficult period and now look oversold. Our current bias is therefore towards trimming global exposure and adding locally.

The case for doing so is consistent with our framework: fundamentals remain sound, valuations have derated and market behaviour points to a high degree of caution. Sentiment and positioning indicators are weak, with discretionary investors underweight and short positions building in many cyclical areas of the market. The market is still climbing a wall of worry, with many investors concerned that the wheels could come off. That is not our base case.

We have also not been tempted into global bonds despite the recent sell-off. We continue to see better opportunities in South African and Brazilian bonds, where we believe the risk of capital loss is relatively low. Rather than adding to global duration, we are looking for other ways to diversify the portfolio and the considerations around the relative value between developed-market bonds and commodity opportunities continue.