

Q3 2025 INVESTMENT LETTER

OCTOBER 2025



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EXECUTIVE SUMMARY

South African assets delivered strong returns in Q3, driven by a favourable combination of global and local factors.

A **weaker US dollar and surging gold prices** improved South Africa's terms of trade, supported the rand, and strengthened fiscal outcomes.

The upcoming MTBPS will be a key event, with markets watching for signals of continued fiscal discipline and reform momentum.

The South African Reserve Bank's move toward a **lower inflation target** has anchored expectations and supported fixed income markets.

Equity market gains were highly **concentrated in a handful of resource and tech-linked stocks**, making it a challenging environment for diversified active managers.

Foreign investor flows returned to the bond market, while equity flows remained negative overall, with selective buying in certain sectors.

The political landscape remains fluid, with the ANC facing internal challenges and **coalition politics likely to shape the outlook ahead of the 2026 local elections**.

Our approach remains deliberately diversified, **prioritizing capital preservation and risk management** as we navigate an environment of both opportunity and uncertainty.



INTRODUCTION

A confluence of events this year has led to a continued weakening of the US dollar and marked rally in the price of gold¹. Expectations for interest rate cuts by the Fed, elevated geopolitical risks, and concerns about the US fiscal situation all coupled with central bank (notably China and other EMs) diversification away from US dollar into gold colours the backdrop.

The weaker US dollar and the gold rally have been a major boost for South Africa's economy this quarter, providing improvement in our terms of trade (ratio of export prices to import prices), a strengthened fair value of the rand, and helped government revenues outperform expectations. The result is a healthier fiscal position and a more resilient current account.

Looking ahead, the upcoming MTBPS is a key event where we expect Treasury to bank these cyclical gains while continuing to reinforce fiscal discipline.

Chart 1a: Gold price higher; US dollar lower



Chart 1b: Improved Terms of Trade

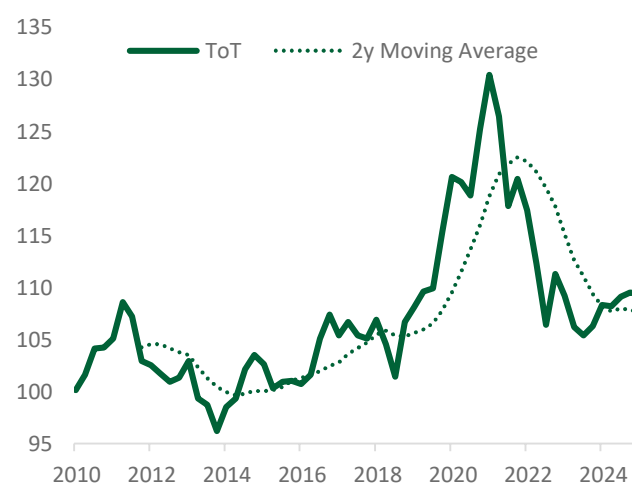
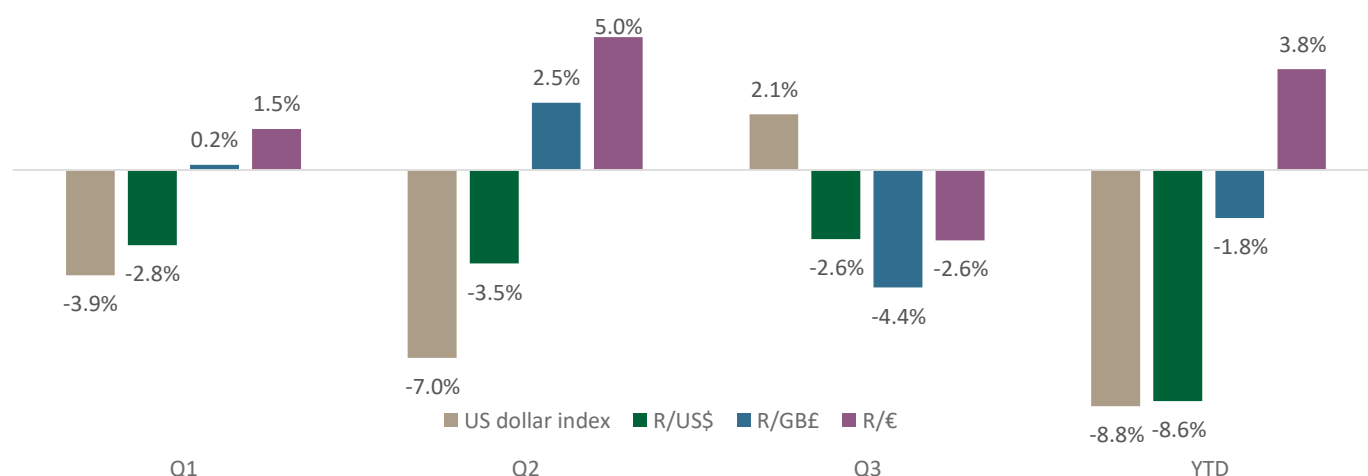


Chart 2: While the rand broadly stronger over Q3, it has been US dollar weakness driving R/US\$ this year



Alongside these favourable macroeconomic trends, recent changes in the South African Reserve Bank's inflation targeting framework are set to influence both inflation expectations and interest rates.

¹ Source: For all data on this page. Bloomberg. As of 30 September 2025.



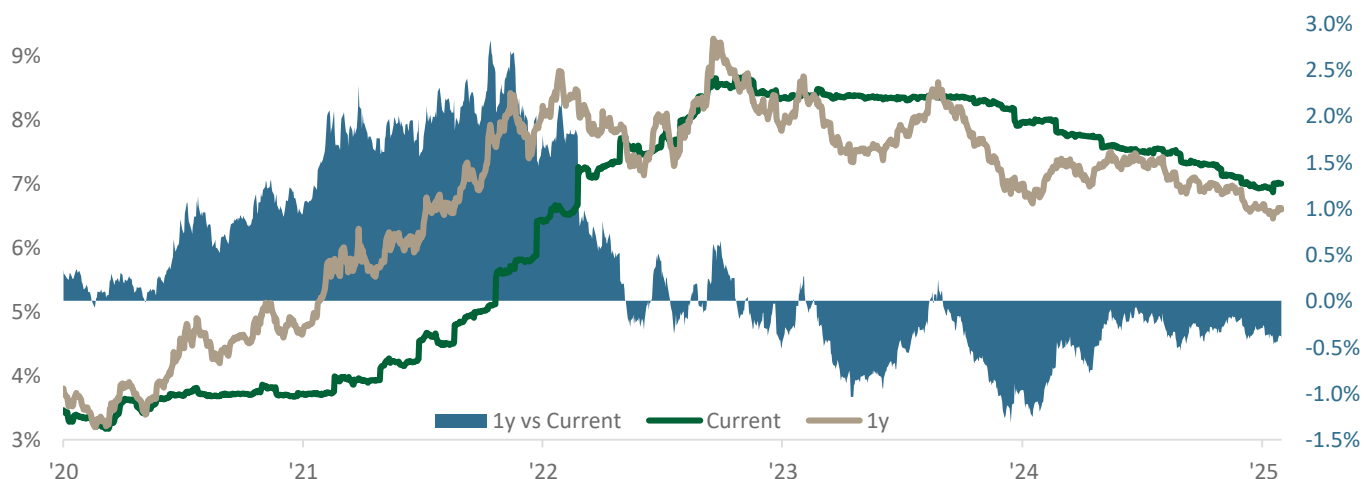
Section 1. Inflation and Interest Rates

At its July MPC meeting, the SARB announced it would start aiming to achieve a 3% annual inflation target. This is at the lower end of its current 3% to 6% mandate – with it having emphasised achieving the midpoint of this range since 2017. Modelling by the SARB indicates that this shift should lower inflation expectations and, ultimately, inflation and interest rates all supportive of real returns and a steadier rand. A steadier rand should also translate into reduced imported inflation.

While the mandate still needs to be formalised by Treasury, which we think is likely at the MTBPS in November, this is a step change in monetary policy that aligns with what has been done by other emerging market central banks (moving from a range to a single target) over the past decade.

Regarding the impacts on realised inflation, we expect the adjustment lower to be gradual, with sticky categories (electricity, medical aid, municipal tariffs) keeping inflation above 3.5–4% in the medium term. For context, average annual headline and core inflation this year has been 3.1%². This allowed the MPC to cut the repo rate to 7.0% (by 0.25%) in July, while its focus on anchoring inflation expectations kept the repo rate unchanged at the September meeting. Its modelling currently indicates the repo rate could be 0.5% to 1.0% lower by the end of next year³. For its part, the market (as seen in [chart 4](#) below⁴) is currently pricing around 0.4% worth of cuts over the next 12 months.

Chart 4: Money market pricing for further interest rate cuts



These developments have been supportive of SA fixed income assets in general and longer duration government bonds in particular. Reflective of the reduction in this risk premium (and reflected in [charts 5a and 5b](#) below⁵), the yield on the 10-year SA government bond shifted 1.0% lower (from 10.3%) since the end of last year.

² Source: StatsSA – as of August 2025.

³ Source: SARB MPC – as of September 2025.

⁴ Source: Bloomberg. 30 September 2025. Chart shows current 3-month interest rate and 3-month interest rate in 1-year

⁵ Source: Bloomberg – as of 30 September 2025



Chart 5a: SA government yield curve

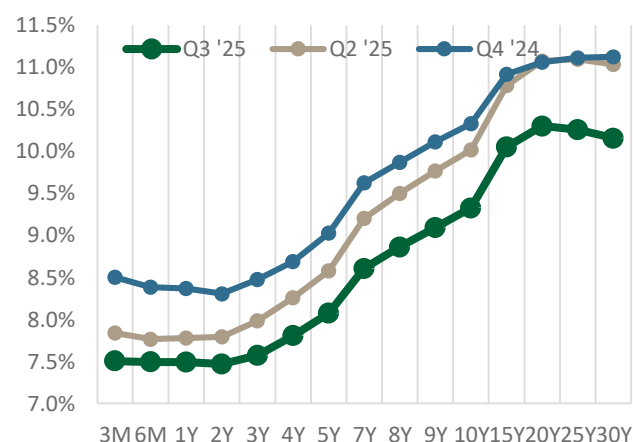
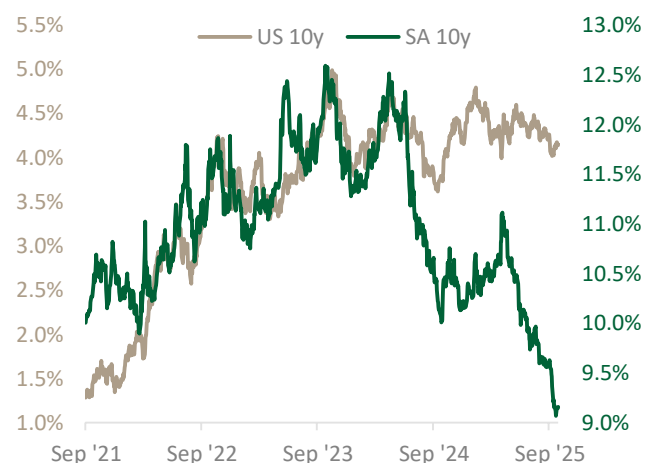


Chart 5b: US 10y & SA 10y government bond yields



It has also led to the SA government bond market continuing to attract the interest of foreigner investors. They were large net buyers in September (+R77bn), with holdings up R164bn this year. While still well below the 42.8% peak seen in 2018, foreign ownership is now 26.8% of total outstanding government bonds.

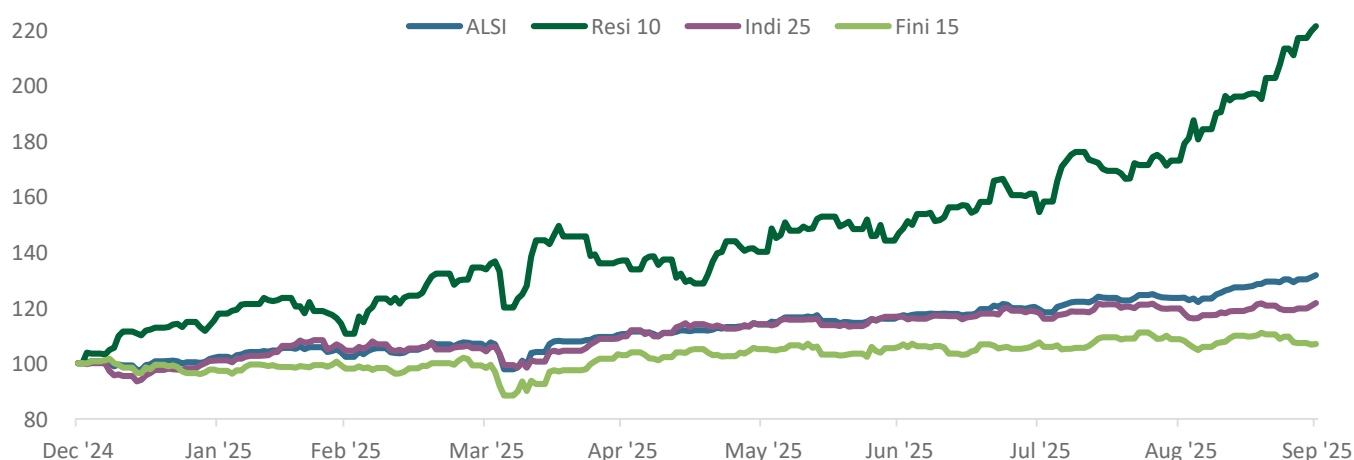
Section 2. Equity Market

With the price of gold rallying this year, the SA equity index (ALSI), which has roughly one third made up of commodity-oriented businesses, is up 31.7% in rand. The Top 40 index, which currently has almost 20% exposure to gold miners, is up 37.2%. For context, the FTSE/JSE Resources 10 subindex is up 121.4% this year (and 50.8% over the quarter) ⁶.

Returns this year have been concentrated in a handful of companies exposed to the sectors. Gold miners contributed roughly 13.4% and PGM miners a further 5.6% (19.0% in total) to the returns of the ALSI. To further accentuate the point, Gold Fields (up 204.0% this year) contributed around 7.1% and AngloGold (up 189.6% this year) 4.4%.

Taken together, gold and PGM miners and Naspers and Prosus made up around 26.6% of the 31.7% ALSI return this year (or 84.0%).

Chart 6a: Selected sector performances this year

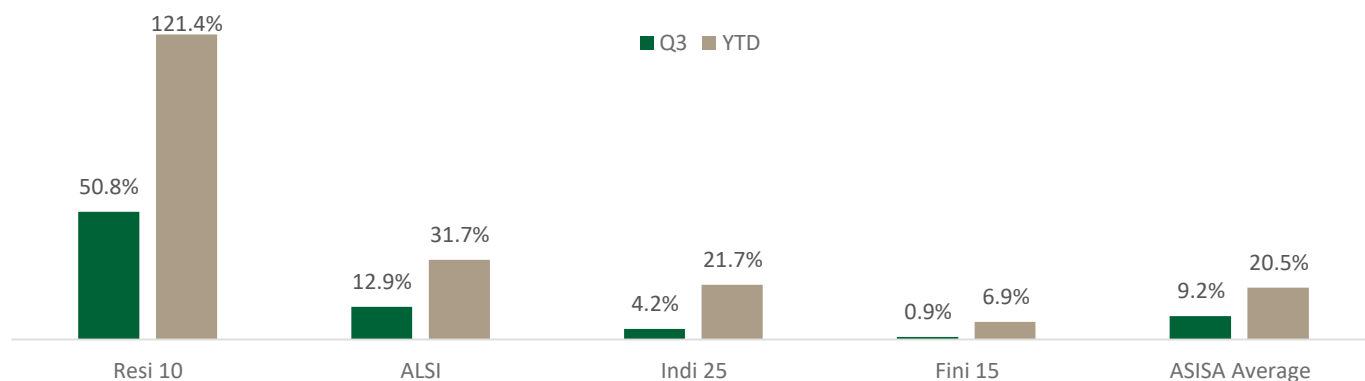


⁶ Source (for all data in this section): Morningstar. As of 30 June 2025. All figures in ZAR.



Conversely, returns from Industrials and Financials were relatively muted. Industrials returned 4.2% over the quarter and 21.7% this year, while Financials eked out 0.9% and 6.9%, respectively.

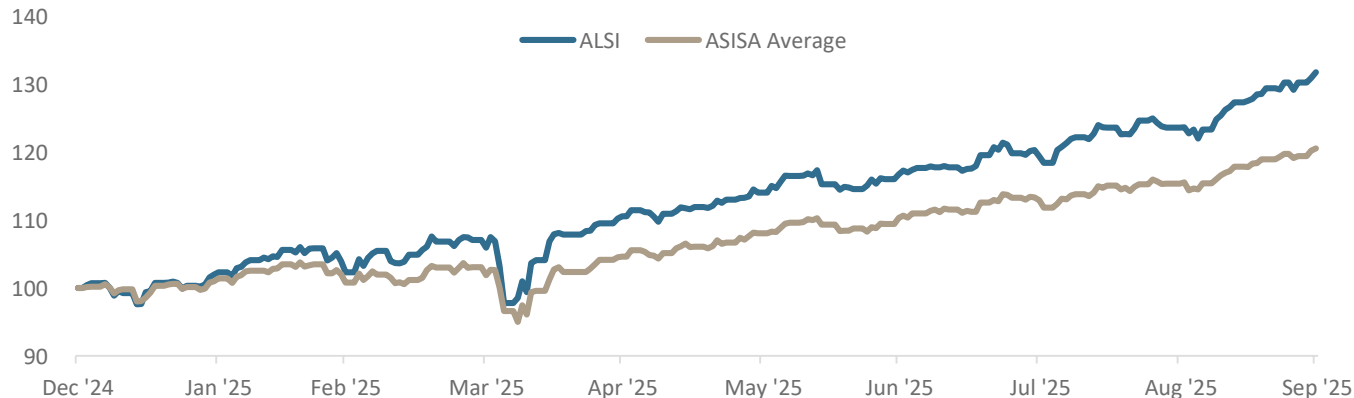
Chart 6b: Selected sector performances this year



This environment has been particularly tough for active managers. Unless portfolios were heavily overweight the handful of top-performing resource stocks, it was extremely difficult to keep pace with the index. Many active managers, especially those with risk conscious diversified approaches, underperformed the ALSI.

The same phenomenon has played out in the US, where S&P 500 returns have been driven by a small group of mega-cap tech stocks ("Magnificent 7"). Most active US equity managers have also struggled to outperform the index, as gains were concentrated in a few names.

Chart 7: All Share Index (ALSI) versus ASISA General Equity Category Average⁷



For us, this concentration raises important questions about the sustainability of returns and the associated risks – specifically, how these indices would perform if the current market leaders experienced a significant reversal. Our approach remains deliberately diversified, with a strong emphasis on capital preservation and risk management over chasing short-term performance, ensuring that portfolios are resilient across different market environments.

Continuing the trend of the past few years, foreigners were net sellers of SA equities in Q3, but after adjusting for dual-listed stocks and special transactions, net outflows were much smaller, with selective buying in chemicals, precious metals, and energy.

While economic and market dynamics have been favourable, the evolving political landscape remains a critical factor for investors to monitor.

⁷ Source: Morningstar. As of 30 June 2025. All figures in ZAR.



Section 3. Politics

The past quarter has underscored just how complex South Africa's political and economic environment remains. The Madlanga Inquiry into police corruption is bringing to light the extent of political interference and organised crime within the SAPS. These revelations are likely to further erode confidence in the ANC's ability to deliver effective governance and may accelerate calls for meaningful security sector reform. The Inquiry also places pressure on key figures, notably Senzo Mchunu, whose future as police minister and ANC succession candidate is now uncertain.

The ANC continues to grapple with a series of corruption scandals and financial pressures, including high-profile cases such as the SIU's findings on Tembisa Hospital and the court ruling against the late Deputy President David Mabuza. These underscore the scale of institutionalised corruption and the risks to public trust, with potential implications for the party's performance in the 2026/27 local government elections.

Despite these headwinds, there are credible signs of resilience and reform. Structural reforms led by the Presidency and National Treasury – supported by the private sector – are progressing. Of note is the forthcoming "GAIN" growth strategy, developed under Operation Vulindlela. GAIN is expected to provide a coherent and actionable framework for accelerating structural reform, focusing on unlocking investment, improving infrastructure, and addressing key bottlenecks in the economy. Early indications suggest that GAIN will be open for public comment soon, and it is anticipated to serve as a central pillar for South Africa's medium-term recovery efforts.

While growth expectations for 2025 have been revised down to 1%, recent data points to green shoots, including improved corporate credit growth and a rebound in manufacturing activity. Political volatility remains elevated, with shifting opposition coalitions and ongoing US-SA trade negotiations. However, South Africa's efforts to diversify trade and investment – particularly with Gulf and Asian partners – are gaining momentum, offering potential buffers against external shocks. Notably, recent diplomatic incidents, such as the landing of a blacklisted Russian cargo plane, have had a muted market impact, suggesting that investors are increasingly pricing in geopolitical risk.

As we look ahead, the interplay between political developments and economic fundamentals will be central to shaping South Africa's investment outlook.

CONCLUSION

South African assets have delivered exceptional returns this year, supported by a favourable alignment of global and local factors. However, the outlook remains nuanced: while macroeconomic tailwinds and ongoing reforms provide reasons for optimism, political uncertainty and market concentration require continued vigilance.

As stewards of client capital, our approach remains anchored in diversification and disciplined risk management, ensuring portfolios are resilient across a range of scenarios and focused on long-term value creation.

We will continue to monitor key economic, political, and market signposts as we head into 2026, maintaining our focus on capital preservation and long-term value creation for our clients.

We thank you for your continued support.

Stonehage Fleming Investment Management (South Africa) Investment Committee
October 2025



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