

*Please note that the commentary is for the retail class of the Fund.*

#### Performance and fund positioning

The Fund returned 0.75% in August, bringing its 12-month total return to 10.61%, which is ahead of cash (7.65%) and its benchmark (8.44%) over the same period. We believe the Fund's current positioning offers the best probability of achieving its cash +2% objective over the medium to longer term.

Local bonds delivered subpar returns in August. The FTSE/JSE All Bond Index (ALBI) returned 0.75%, with the long end of the curve (bonds maturing in 12+ years) up only 0.35%. The belly of the curve (maturing in 7-12 years) closed 0.90% higher, while medium-term bonds (maturing in 3-7 years) posted 1.05%, and short-term bonds (1-3 years) returned 0.90% in August. Cash came in at 0.59%, while inflation-linked bonds (ILBs) were up 1.50% for the month.

US headline inflation remained unchanged at 2.7% year on year (y/y) in July, while core inflation ticked up to 3.1% y/y from 2.9% y/y. Inflation was supported by increases in used and new vehicle prices, high food prices and sticky shelter and air transportation costs. Energy costs declined and partly offset the increases from the other sectors. The Federal Reserve Board (Fed) is due to meet at the end of September, and the market is expecting a 25 basis points (bps) rate cut.

The Bank of England cut the deposit rate by 25bps at the August Monetary Policy Committee (MPC) meeting, moving the deposit rate to 4% from 4.25%. The MPC noted substantial disinflation over the past two years as a result of the restrictive monetary policy stance, although new price pressures have surfaced. While services inflation has been flat in the past few months, inflation is expected to tick up on the back of rising food and energy prices before returning towards the 2% target.

UK headline inflation increased to 3.8% y/y in July from 3.6% y/y in June, while core inflation accelerated to 3.8% y/y from 3.7% y/y. The main driver of the increase was a rise in transport costs and energy prices. Food and non-alcoholic beverages, restaurants, and hotels also contributed to price increases. Elsewhere, housing utilities, healthcare, and apparel costs were soft.

Euro area headline and core inflation were unchanged at 2% y/y and 2.3% y/y, respectively, in July. There were slight increases in non-energy industrial goods, food, alcohol, and tobacco prices, but broader pressures remained muted. This balance of stable headline inflation and elevated core inflation pressure reinforces the European Central Bank's cautious stance, with the door still open for potential rate cut action if inflation drifts below target.

China's headline inflation flatlined in July following an increase of 0.1% y/y in June, while core inflation rose to 0.8% y/y from 0.7% y/y. Food inflation remains a big detractor, decelerating for the sixth consecutive month. Modest price increases were observed in apparel, healthcare, and household items. Producer price inflation continued to fall, down 3.6% y/y in July.

The rand ended the month at R17.650/US\$1, stronger than its close in the previous month but weaker than its Emerging Market peer group. Offshore credit assets and certain developed market bonds continue to flag as relatively attractive. The Fund has utilised a significant part of its offshore allowance to invest in these assets. When valuations are stretched, the Fund will hedge/unhedge portions of its offshore exposure back into rands/dollars by selling/buying JSE-traded currency futures (US dollars, UK pounds, and euros). These instruments are used to adjust the Fund's exposure synthetically, allowing it to maintain its core holdings in offshore assets.

South African (SA) headline inflation ticked up to 3.5% y/y in July from 3.0% y/y in June, while core inflation marginally increased to 3.0% y/y from 2.9% y/y. The acceleration was driven by increases in food, energy, and administered prices. Vehicle prices were flat for the month of July, while broader transport costs fell. Base effects and lingering pressure on food prices are likely to see headline inflation drift towards 4% in the coming months. This will be a challenging trajectory for the South African Reserve Bank to navigate, and we expect policy rates to remain on hold into 2026. However, moderate core pressures, combined with a downward adjustment to expectations, might open the window for another cut, especially if oil prices become more supportive of lower fuel prices going forward.

At the end of August, shorter-dated fixed-rate negotiable certificates of deposit (NCDs) traded at 7.55% (three-year) and 8.00% (five-year), with both maturities lower compared to the end of the previous month. Our inflation expectations suggest that the current pricing of these instruments remains attractive due to their lower modified duration and, hence, high breakeven relative to cash. In addition, NCDs have the added benefit of being liquid, thus aligning the Fund's liquidity with the needs of its investors. The Fund continues to hold decent exposure to these instruments (fewer floating than fixed), but we will remain cautious and selective when increasing exposure.

ILBs have continued their underperformance over the last quarter, primarily due to the SARB maintaining the real policy rate at elevated levels and realised inflation being below expectations for an extended period. However, inflation is currently close to, if not at, its trough, and we expect it to average 4%-4.5% over the next 12 months. This, combined with high starting real yields makes ILBs quite attractive relative to certain nominal bonds. ILBs are also less correlated to nominal bonds, given their inherent risk-protection attributes. These are present since inflation in SA has historically been very closely tied to the currency performance and because the currency is the release valve for any SA- (and global risk-off) specific difficulties, it has a direct feed through to inflation. This makes ILBs a good risk-offset to hold in a portfolio, specifically in uncertain times. The valuation argument for owning ILB's with a maturity of less than six years is still very strong as they provide a decent uplift relative to their nominal counterparts.

The global landscape remains uncertain; however, emerging markets have continued to outperform developed markets. SA Government Bonds have flourished as local anxiety has eased and expectations for a lower inflation target have bolstered prospects for a lower repo rate. These bonds are now trading at or close to fair value, and to see a further rerating, one would need to see a significant change in fiscal prospects or monetary policy accommodation. Anchoring inflation at 3%

will take longer, thus delaying any tailwinds for bonds from further policy easing and achieving substantial fiscal consolidation would require growth in excess of 2%-3% p.a. Global bond flows have turned more supportive of emerging markets, given their relatively cleaner balance sheets, and could support further compression in bond yields if that trend gains momentum. Valuation suggests that the best value on the yield curve sits in the 10- to 15-year band and in ILBs with a maturity of less than six years.

The local listed property sector was up 2.04% over the month, bringing its 12-month return to 18.47%. The durability of the operational performance will remain in the spotlight as an indicator of the pace and depth of the sector's recovery. The current increase in the cost base, due to higher administered prices and second-round effects on deteriorating infrastructure in much of the country, will weigh on the sector's earnings in the coming year. We believe that one must remain cautious given the high levels of uncertainty around the strength and durability of the local recovery.

Local credit spreads are at historically tight levels due to low issuance volumes and a large amount of capital seeking a home with reduced volatility. The use of structured products, such as credit-linked notes (CLNs), has become ubiquitous within the local market. This sector has experienced exponential growth over the last five years, reaching a market size of over R100 billion. However, only a third of this market reprices, creating an inaccurate representation of asset volatility and pricing. CLNs mask the underlying/see-through credit risk as the issuing entity (predominantly local banks) is seen as the primary credit risk.

The increased usage of CLNs has not expanded the pool of borrowers; rather, it has only served to concentrate it. This is due to the ability to limit the volatility of these instruments by not marking them to market based on the underlying asset price movements. The combination of attractive yields and no volatility is an opportunity that not many would pass up, unless, of course, transparency of pricing is important to the underlying investor. As a result, there can be significant unseen risks within fixed-income funds. Investors need to remain prudently focused on finding assets of which the valuations are correctly aligned to fundamentals and efficient market pricing. Except for a few opportunities, we view the local credit market as unattractive relative to other asset classes.

#### Outlook

We remain vigilant of the risks from the dislocations between stretched valuations and the local economy's underlying fundamentals. However, we believe that the Fund's current positioning accurately reflects the appropriate level of caution, while its yield of 8.60% (gross of fees) remains attractive in relation to its duration risk. We continue to believe that this yield is an adequate proxy for expected portfolio performance over the next 12 months. As is evident, we remain cautious in our management of the Fund. We continue to invest only in assets and instruments that we believe have the correct risk and term premium to limit investor downside and enhance yield.

#### Portfolio managers

**Nishan Maharaj and Mauro Longano**

as at 31 August 2025