PERPETUA INVESTMENT MANAGERS

Multi Asset Class Outlook

2025

Contents

On my mind

The power of expectations

Expectations are probably one of the most powerful driving forces in investing, as it is in life. From the expectations we place on ourselves and others, especially at the start of a new year (we call them resolutions!), to the daily voice in our head which sets out our "to-do" lists for what we expect to accomplish on any given day. In investing, expectations are crucial as they shape asset prices, influence investment decisions and determine market dynamics, especially in the short-term.

At the start of 2024, we expected spend and usage on AI would continue to expand but we didn't expect that only a handful of mega-companies would continue (for a second consecutive year) to reflect all of this positive expectation in their stock pricing. When US President Trump lost the election to President Joe Biden in 2020, we certainly did not expect we would see Trump back in the Oval Office by January 2025, and yet there he is now!
In South Africa, while we expected the ruling party, the ANC to lose its majority following decades of under-delivering, we certainly did not expect the resulting coalition government would include its arch-nemesis, opposition party the DA. Just these three outcome "surprises" had a direct impact on respective markets and economies in the past year.

As we offer this comprehensive multi-asset class outlook, we are acutely aware that it is heavily influenced by how 2024 turned out versus our expectations going into it and then more critically how 2025 is likely to shape up given our expectations for a multitude of moving parts. The key thing in understanding the hidden driver of expectations is to go below the surface-level (the market) to uncover where the more likely outcomes will diverge from the market's current view. In the articles that follow we seek to build our case for how our portfolio positioning reflects our fundamentally derived expectations, and how market sentiment creates the opportunities we are seeking to exploit.

Setting the scene

The global macroeconomic picture is one of divergence. While growth in the U.S. is poised to outpace global peers driven by pro-growth policies and deregulation, the Eurozone and UK face sluggish growth due to inflationary pressures and weak demand. Emerging markets, particularly China, are grappling with deflationary challenges, while regions like South Africa show signs of cyclical recovery. These dynamics underscore the importance of regional nuances in investment strategy.

Geopolitics: a driving force

Geopolitical tensions remain a central theme. From the implications of U.S. tariffs on China to shifting trade alliances, these developments are shaping market sentiment and investment flows. In 2025, the potential for heightened trade disputes and policy uncertainties calls for a cautious yet opportunistic approach. For instance, while protectionist policies may disrupt global supply chains, they also create pockets of opportunity in localised industries. The unexpected nature of President Trump's style of governing ironically makes expectations management a particularly challenging exercise for citizens and investors!

...continued

Equities: a tale of two markets

The equities landscape reflects stark contrasts. In the US, valuations are stretched, particularly in large-cap technology stocks, prompting a cautious stance despite market expectations for this AI-based rally to continue through 2025. Conversely, international equities, including those in Europe and Japan, present attractive valuation discounts and opportunities for stock-specific gains. Emerging markets, while volatile, offer potential in consumer-driven industries and sectors benefiting from structural reforms.

Fixed income: navigating yield curves

In fixed income, the outlook is shaped by divergent monetary policies. While the U.S. Federal Reserve is likely to conclude its rate-cutting cycle by mid-year, South African bonds offer compelling real yields, driven by improving growth prospects and contained inflation. Positioning within fixed income portfolios requires balancing duration risk with the potential for yield compression in select markets.

Property: recovery in sight

The property sector is showing signs of recovery, particularly in regions where balance sheets have strengthened, and vacancy rates are declining. Retail and industrial properties stand out, supported by stabilising energy supplies and improving consumer sentiment. However, the office sector continues to face challenges due to oversupply and hybrid work trends.

Key themes for 2025

1. Divergence in growth and inflation: tailoring strategies to regional dynamics will be critical as growth and inflation trajectories vary widely.
2. Sector rotation: opportunities abound in undervalued sectors and those benefiting from macro tailwinds, such as infrastructure and clean energy.
3. Risk management: elevated geopolitical risks and market volatility necessitate a focus on diversification and resilience.

As investors, at the very heart of our endeavour is a focus on the future and formulating many assumptions about what we expect it will bring.
But a wise Japanese stoic once said “*Expectations are the greatest impediment to living. In anticipation of tomorrow. we lose today.*”
In that vein while I offer our investment outlook in earnestness, my hope for us all is that in 2025 we learn to appreciate the **now** as much as we do the future.

I hope you enjoy the read.

Delphine Govender
Chief Investment Officer

Key themes: 2025

Key themes: 2025

The past year was marked by a record-breaking year of elections that reshaped global politics, escalating geopolitical tensions, falling inflation and interest rates, as well as soaring equity markets. 2025 is set to be shaped by Trump's second term and U.S. policy changes that will have global ramifications. From pro-growth policies to geopolitical tensions characterised by conflicts and trade wars, the stage is set for what promises to be a headline-driven and volatile start to the year.

Trump's America

As Trump officially takes office, it's an opportune time to review his campaign promises and their potential impact. This section will focus on three key areas:

1. Tariffs
2. Growth
3. Immigration policy

1. Tariffs

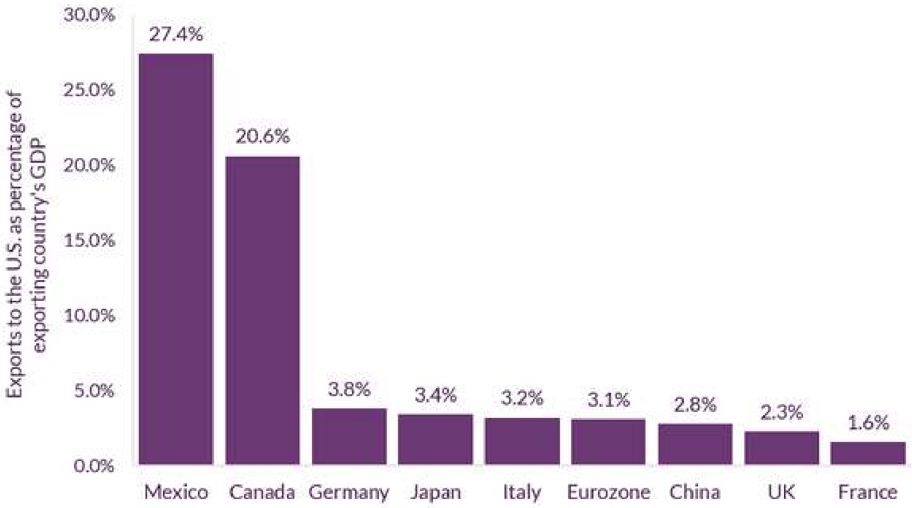
The potential tariff scenarios that could unfold under the new administration include:

- a tariff of 60% or more on Chinese goods
- a universal 10%-20% tariff on all imports to the U.S.
- an additional 25% tariff on imports from Canada and Mexico, unless these countries crack down on migrants and fentanyl crossing the border, with an extra 10% tariff on China if it does not block exports of the opioid.

The impact of these tariffs can be assessed by analysing goods exported to the U.S. as a percentage of GDP for various economies [Figure 1]. Unsurprisingly, Mexico and Canada look especially vulnerable, given their dependence on trade with the U.S., while some of the European economies are less exposed.

Although China's overall export exposure to the U.S. may appear modest at 2.8% of GDP, the U.S. remains its largest export destination, accounting for approximately 18% of China's total exports. To put this into context, this is three times larger than the percentage of exports received by China's second-largest importer, Japan. In 2023 China's exports represented 18.9% of its GDP, with 2.8% directly tied to exports to the U.S. Hence, the sheer volume of tariff hikes proposed by the U.S. makes China the biggest potential loser.

Figure 1: Restricted access to the U.S. could hit some trading partners hard



Source: IMF, Macrobond, Investec Economics

Tariff impact in Trump's first term was negligible

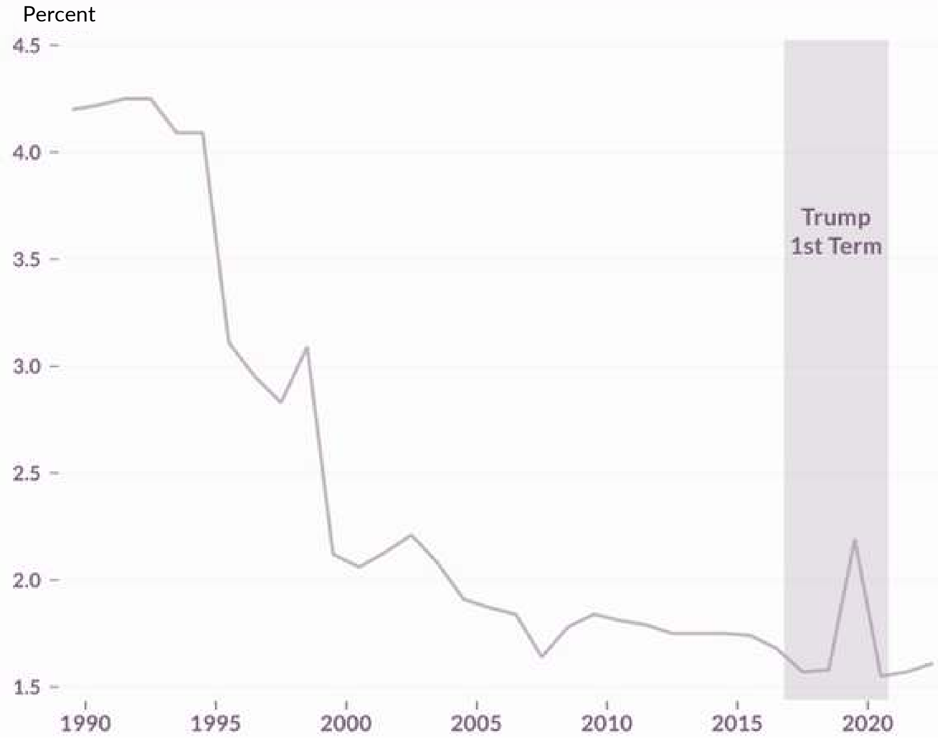
Reviewing Trump's first term, it's worth analysing the U.S. trade-weighted tariff, which was circa 1.7% for imported industrial goods (accounting for 94% of all merchandise imports) [Figure 2]. During his first term, Trump implemented the following tariff measures.

- **March/April 2018:** 25% on steel and 10% on aluminium products imported from most countries
- **July 2018:** 25% on aircraft parts, semiconductors and microscopes
- **August 2018:** 25% on motorcycles, steam turbines and railway cars
- **September 2018:** 10% on fabric, modems, chemicals, furniture and seafood (later raised to 25% in May 2019)
- **September 2019:** 15% on Agricultural products, antiques, clothes, kitchenware, footwear (reduced to 7.5% in December 2019 after coming to an agreement with China in which they promised a "corresponding" amount of tariff rollbacks)

These measures caused a jump of circa 1% in the U.S. trade weighted tariff rate to the current level of 2.6%.

However, if the new administration implements all proposed tariff plans, the average U.S. tariff rate could triple to approximately 8% by the end of 2026. This would result in:
- An 11% decline in overall U.S. trade.
- An 83% reduction in China's sales to the U.S., significantly impacting its export economy.

Figure 2: U.S. tariff rates as a percentage



Source: World Bank, Analysis © ETM

Potential timing of tariff implementation
Tariffs on China could be imposed within three months under Section 301 of the Trade Act of 1974, which allows sanctions for unfair trade practices, or Section 232 of the Trade Expansion Act of 1962, which addresses national security concerns.

The implementation timeline on universal tariffs remains somewhat unclear. It is uncertain whether they can be implemented quickly by invoking section 301 or if they would require congressional approval, in which case it would take more time to come to fruition.

2. Growth

Trump campaigned on a strong growth mandate, with the following policies expected to have a positive impact:
- Deregulation: Trump's goal of removing 10 regulatory rules for each new regulatory rule will likely result in a 'risk on' environment for markets.
- Tax cuts: Trump will focus on extending and expanding the Tax Cuts and Jobs Act (TCJA) enacted in December 2017 during his first term. The TCJA aimed to stimulate economic growth by reducing tax burdens, particularly for high-income individuals and businesses. We anticipate the earliest this would take effect is 1 January 2026. Additionally, he is proposing to cut the top corporate tax rate for domestic manufacturers from 21% to 15%.

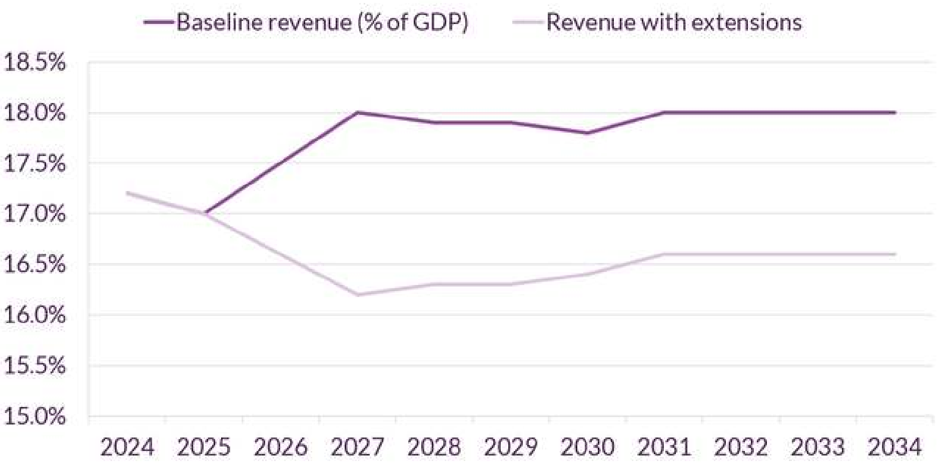
Fiscal implications
The fiscal implications of tax cuts could put an enormous dent in federal revenue [Figure 3]:

- Just extending the TCJA will require approximately $500bn in additional revenue.
- The original TCJA increased the fiscal deficit and government debt, as it was not fully offset by spending cuts or alternative revenue sources.

According to the Brookings Institution, the long-term impact of tax cuts depends heavily on how they are financed:

- **Positive growth impact:** tax cuts funded by reductions in unproductive government spending could increase output.
- **Negative growth impact:** cuts financed by reduced government investment or increased borrowing would raise the fiscal deficit, leading to slower long-term growth.

Figure 3: Baseline revenue vs. revenue with extensions



Source: Committee for a Responsible Federal Budget, Bloomberg

However, Trump's advisers argue that lower taxes and deregulation will drive investment, productivity and economic growth, eventually offsetting revenue losses.

Additionally, the proposed tariff plan would raise about $250bn in revenue. This coupled with spending cuts could go a long way in closing the revenue gap. While the long-term effects remain uncertain, the prospect of tax cuts is likely to sustain market optimism in the near term.

3. Immigration

Illegal immigration was another cornerstone of the campaign, with two primary objectives:

- Securing and closing the U.S. Southern border.
- Deporting undocumented people already living in the United States

Mass deportations could exacerbate labour shortages, particularly in the services sector which is already under strain, and the agricultural industry where undocumented workers make up an estimated 5% of the workforce.

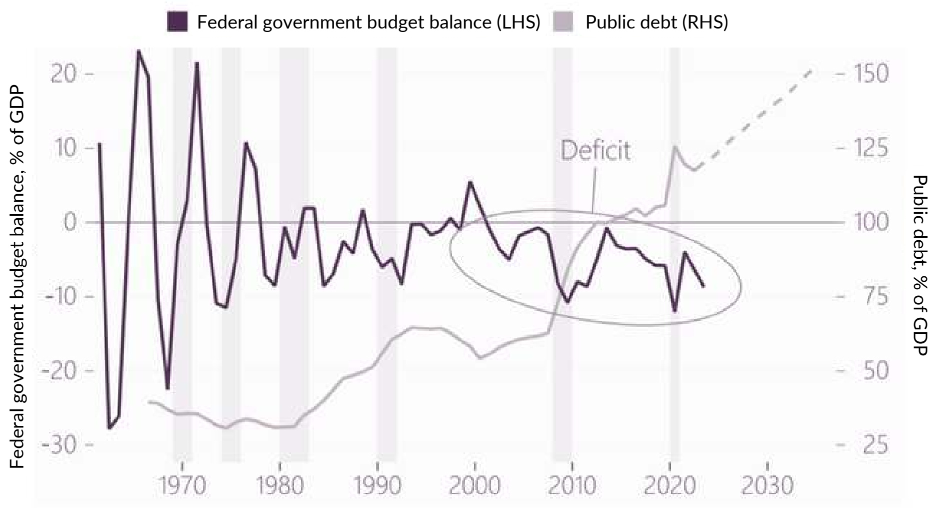
In a worst-case scenario, these policies could create a 'stagflationary' environment in which a smaller labour force reduces economic activity thus slowing growth, while inflation rises due to increased wage costs.

Timing
Closing the border could be implemented relatively quickly, but deportations are likely to take far longer and come at a substantial cost. Whether these goals can be fully achieved within Trump's four-year term remains uncertain.

What it boils down to

The combination of pro-growth policies and fiscal stimulus would need to be financed by further government spending, implying heavier bond issuance. This will further compound the ballooning budget deficit, currently at -6% and push debt-to-GDP from its current level of 100% to 150% by 2035 [Figure 4].

Figure 4: U.S. budget balance and debt to GDP, recessions shaded in grey



Source: U.S. Treasury, Analysis © ETM

Our assessment

Short term dynamics:

Trump's second term is already shaping up to be headline-driven, with recent weeks providing a glimpse of what is to come. We expect an increased level of volatility and in such instances, safe haven assets typically perform well. As Trump takes office over the next month, we expect the USD to remain strong, with bond yields acting as shock absorbers as trade wars intensify. This means that the prospect of U.S. 10-year bond yields exceeding 5% is not improbable. Meanwhile, as Trump implements pro-growth policies, stock markets may take this as a positive signal and rally in the very short term.

Long term dynamics:

As policies are implemented, timelines and long-term market effects will become clearer. However, rising fiscal deficits and growing government debt remain significant concerns, raising questions about the long-term sustainability of these strategies. We anticipate the following trends:

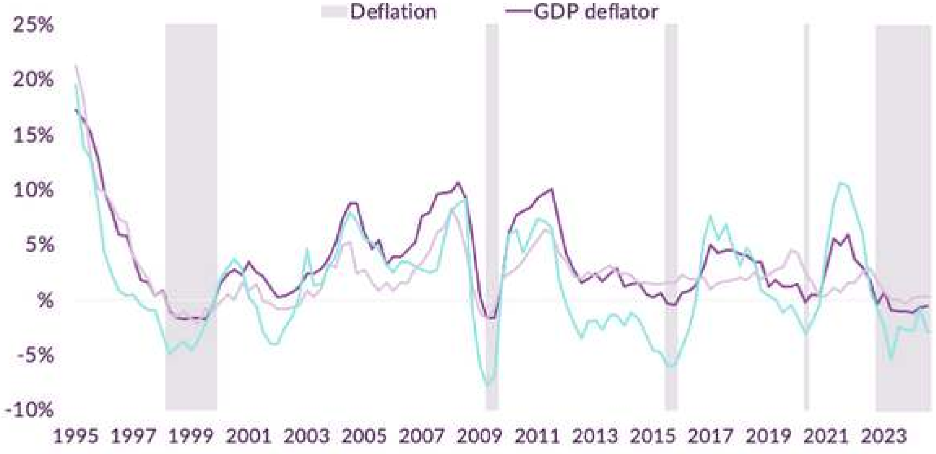
- **Bond yields:** expected to trade between 4-5% for the remainder of the year.
- **FED:** likely to cut rates by 25-50bps, ending the cutting cycle by June, as inflation risks re-emerge.
- **USD:** while the USD may remain strong in the near term, it is likely to weaken in the latter half of the year as Trump's administration actively seeks to devalue the dollar. A weaker dollar could enhance manufacturing competitiveness without imposing trade barriers, providing a viable alternative for businesses and investors. A key risk to dollar strength is the possibility of coordinated currency adjustments by major economies like Europe, Japan and China, which may allow their currencies to appreciate to avoid U.S. tariffs. This scenario could resemble the 1985 Plaza Accord[1], where global central banks intervened to weaken the dollar. Instead of raising interest rates, these economies may use foreign exchange interventions to curb the USD while supporting their own growth. Ultimately, the dollar's trajectory will depend on U.S. trade policies, FED rate cuts and geopolitical shifts, making USD volatility a key theme in 2025.

[1] The Plaza Accord was a joint agreement between the U.S., Japan, West Germany, France, and the U.K. to weaken the overvalued U.S. dollar through coordinated foreign exchange interventions. Signed in September 1985, it aimed to correct trade imbalances but later contributed to Japan's asset bubble and economic instability.

China's deflation to persist throughout 2025

China's deflationary spiral is proving hard to fix. Prices have fallen for six consecutive quarters, with further declines expected in the coming quarter. This marks the longest deflationary streak since the Asian Financial Crisis in the late 1990s [Figure 5].

Figure 5: China's deflation persists: GDP deflator was negative for the past six quarters



Source: Bloomberg

Real estate and manufacturing have been key drivers of this decline, with housing inventories at their highest levels in Chinese history. An estimated 60 million unsold apartments could take over four years to sell at current rates.

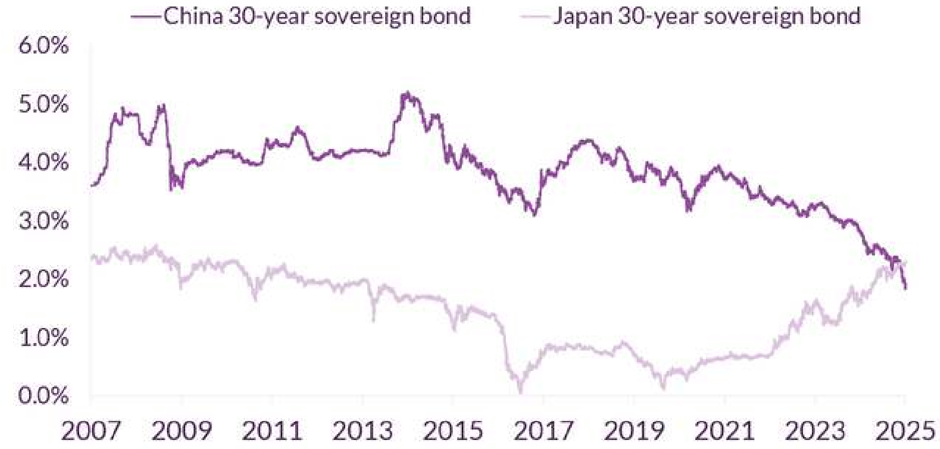
In response, China has announced several stimulus measures aimed at addressing the deflationary trend:

- **Interest rate cuts:** multiple reductions to encourage borrowing and boost demand.
- **Property market support:** relaxation of purchase restrictions, lowering of down payment requirements and reductions in mortgage rates.
- **Public housing initiative:** a 300-billion-yuan program to allow local governments to purchase unsold homes for conversion into public housing.
- **Subsidies:** financial aid for purchases of cars and home appliances, as well as extending aid to low-income families and students.

While these measures have alleviated some pressure, they have not been sufficient to arrest the decline in which China finds itself.

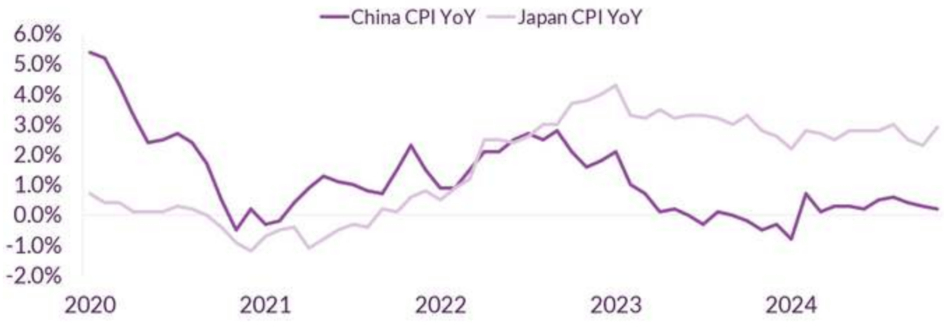
Chinese bond yields have tumbled to all-time lows [Figure 6], reflecting investor concerns about a possible "Japanification" of China's economy where prolonged deflation leads to stagnation and balance sheet recession.

Figure 6: China's 30-year bond yield has fallen below Japan's



Ultra-low yields are a hallmark of deflation, as markets expect central banks to maintain low interest rates to revive domestic demand. China's inflation is hovering near zero while Japan's is rising [Figure 7].

Figure 7: Inflation divergence

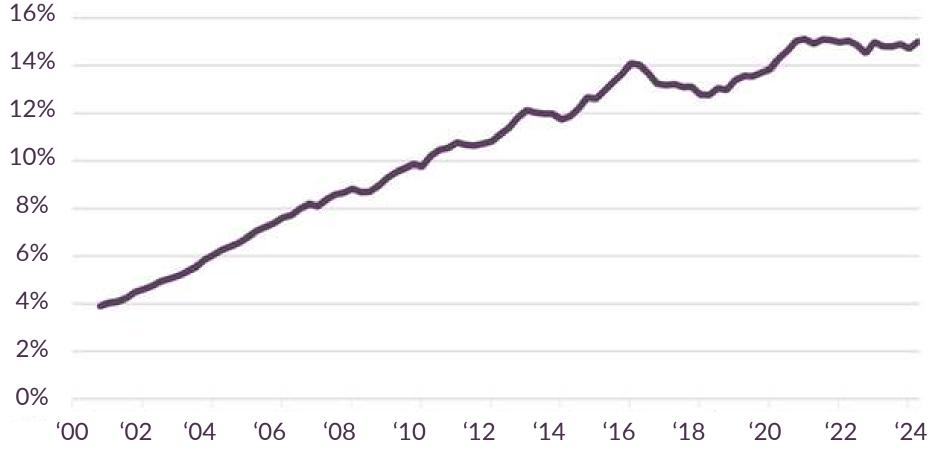


Source: Bloomberg

If the bond market is correct, the implications could be severe. An extended bout of deflation would hobble one of the world's largest economic growth engines, add new strains on social stability in the world's second-most populous country and exacerbate capital outflows that led to a record exodus from Chinese financial markets at the end of 2024.

On a positive note
China has increased its share of global exports in the past decade, despite increasing trade tensions [Figure 8]. They have exported deflation globally with their trade surplus, while moving up the industrial chain.

Figure 8: China's share of world exports have risen despite trade tensions



Source: Bloomberg, IML estimates

Global impact
An extended deflationary period in China would reverberate globally. Lessons from Japan's economic recovery suggest that direct financial support to households, rather than infrastructure and corporate bailouts, could be a more effective solution. As Jesper Koll of Monex Group Inc. points out, it took Japan nearly 20 years to adopt this approach effectively. The hope is that Chinese policymakers will act faster to boost consumer purchasing power.

Tariff impact on China
The proposed U.S. tariffs on China could have significant implications for the country's economy under two potential scenarios:

	Scenario 1: 60% Targeted tariffs on China	Scenario 2: 60% Targeted tariffs on China +10% tariffs on RoW
Impact on Real GDP Growth	Possible less tariff impact than 2018-19 (~1ppt during 1Q18-3Q19), given Chinese manufacturers and multinational corporations' (MNCs') supply chain rewiring over the past 7 years.	Growth impact to be similar to, or even larger than in 2018-19, given softer global demand, increased difficulty for China's export re-routing, and weaker global corporate confidence on rising risk of more fragmentation in the global supply chain.
Impact on Nominal GDP Growth	Possibly higher deflation pressure with U.S. tariff shock further exacerbating excess capacity issue and Beijing's continued focus on supply-chain self-sufficiency.	Even higher deflation pressure than in scenario 1 as the ability to export excess capacity is further constrained.

The overall impact of these tariffs is forecast to subtract almost 0.7% from growth in China.

Trump's proposed tariffs on Chinese imports will likely be phased in [Figure 9], with the full impact expected to materialise only in the fourth quarter of 2026. To counteract this, China is expected to scale up fiscal and monetary stimulus to mitigate the tariff impact.

Figure 9: Phasing in of U.S. trade-weighted tariffs on imports from China over 2025 and 2026

Source: Ian Doyle, Morgan Stanley

Our assessment

Global impact of China's deflationary spiral

- **Weakened global growth:** as one of the world's largest economic engines, prolonged deflation in China would reduce global demand for goods and services, slowing growth in export-driven economies. This will be compounded by the tariffs introduced by the U.S.
- **Commodity price declines:** lower demand from China, a major importer of raw materials, could lead to further declines in global commodity prices, impacting resource-dependent economies.
- **Capital outflows:** increased capital flight from China could destabilise emerging markets and create volatility in global financial markets.
- **Supply chain disruptions:** deflation could force Chinese manufacturers to cut costs, potentially leading to supply chain disruptions and weaker profitability for global companies reliant on Chinese production.

A forceful, consumption-based fiscal stimulus holds the key to decisively breaking this debt-deflation loop. The desired stimulus package of RMB 10 trillion over two years could support social welfare and help address the housing inventory crisis.

The balance of risks, however, have tilted towards the downside. China's apparent reluctance to deploy a large-scale "bazooka" stimulus, coupled with the potential of incoming U.S. economic policies (particularly tariffs) creates a precarious outlook. Without decisive policy action, China's deflationary spiral risks becoming a persistent drag on global growth.

Divergence to remain a theme throughout 2025

Divergence in growth, CPI and monetary policy remains a key theme in 2025.

Growth

The global economy is forecast to grow between 2.7% and 3.3% in 2025, with notable disparities across regions [Figure 10]:

- The U.S. is expected to outperform global peers with projected growth rates ranging from 2.4% to 2.7% for 2025, driven by pro-growth policies such as deregulation and tax cuts. However, the effects of tariffs, fiscal impudence and mass deportations are likely to slow growth heading into 2026.
- In the Euro Area, growth is forecast to remain stagnant, with projections ranging from 0.8% to 1.3% for 2025. A recovery in real household incomes, tight labour markets and decreasing interest rates are bolstering growth, but this is being offset by weak domestic demand and a negative tariff backdrop, which could subtract as much as 0.9% from GDP.
- In China, growth is expected to slow to 4.5%–4.7% due to insufficient stimulus and deflationary pressures. This will be further compounded once the impact of tariff increases materialises.
- Japan is projected to grow by circa 1.5% in 2025, supported by domestic demand and accommodative fiscal policies. Potential headwinds could include structural issues such as an ageing population and an appreciating yen, which limits export competitiveness.

- Emerging Markets (EMs):

    - Growth remains uneven across EMs.

    - India is expected to experience a slowdown with projections for 2025 around the 6.4% mark, well below the average of 8% seen in the last three years. This is largely due to a slowdown in business and consumer spending, as inflation remains high, and wages slide. Corporate profits have also taken a hit.
    - South Africa is poised to enter a cyclical upswing, with GDP growth forecast at 2.0%-2.5% for 2025, more than double the 10-year average of 0.8%. This is largely being driven by lower interest rates, a drawdown of circa R50bn from two-pot retirement savings, and higher consumer confidence and disposable income. However, risks include infrastructure bottlenecks and possible disruptions within the GNU.
    - In LATAM, Brazil's growth is projected to decelerate from the highs of 3.0%+ in 2024 to between 1.8% - 2% in 2025. This slowdown is primarily driven by tighter monetary policy and reduced fiscal stimulus. Similarly, Mexico is expected to experience slower growth in 2025 as U.S. policies keep volatility high and negatively impact investor sentiment.

Figure 10: Forecast growth rates across various markets

Region	2024E	2025E	2026E
World	2.7	2.7	2.6
U.S.	2.8	2.5	2.3
Euro zone	0.8	0.8	1.0
Germany	-0.1	0.3	0.8
France	1.1	0.7	1.0
Italy	0.5	0.6	0.9
Spain	3.0	2.0	1.5
China	4.9	4.5	4.0
Japan	-0.2	1.2	1.1
UK	0.9	1.3	1.3
Canada	1.1	1.9	2.0
India	6.7	6.3	6.7
Brazil	3.1	2.0	2.3
Russia	3.5	1.2	2.1

Source: Goldman Sachs

Inflation disparities

- **U.S:** core inflation is forecast to hover around 2.4%–3.0%, driven by tariffs and a tighter labour market due to restrictive immigration policies. Inflation pressures may ease mid-year before rising again in late 2025.
- **Euro area:** inflation is expected to moderate to 2.0%, aligning with central bank targets.
- **China:** deflation persists with a GDP deflator below 0%, reflecting excess capacity and trade disruptions. Core CPI remains modestly positive.
- **Japan:** inflation is anticipated to slow slightly, stabilising below 2.0%, impacted by yen appreciation.
- **Emerging markets:**
    - **India:** inflation is expected to rise modestly in late 2025 before stabilising around the 4% level.
    - **South Africa:** inflation is anticipated to remain contained at approximately 4%.
    - **LATAM:** the region is projected to continue experiencing disinflation, with Brazil estimating an average inflation rate of 4.5% for 2025 and Mexico at 3.9%.

Monetary policy

- **Fed:** the Fed is expected to cut rates by 25-50bps, targeting a terminal rate of between 3.75%–4% by mid-2025, pausing thereafter as inflationary pressures return. Further rate cuts are anticipated in 2026 if growth weakens.
- **European Central Bank (ECB):** the ECB is expected to cut rates by at least 100bps in 2025, bringing the deposit facility rate to 2%, which is considered to be the “neutral” level. However, should the worst-case scenario transpire involving severe tariff impacts, the ECB may be forced to cut rates below the neutral level, potentially targeting a deposit rate of 1.5%.
- **China:** authorities are expected to follow a gradual rate cutting path as they battle deflation.
- **Bank of Japan (BoJ):** a cumulative 50-75bps in hikes is expected from the Bank of Japan this year, taking the benchmark to 1% for the first time in three decades.
- **Emerging markets:**
    - **Brazil:** restarted the hiking cycle, with rates expected to peak at 14.25% (a further 200bps in hikes as per the guidance by Brazil’s central bank) in early 2025 before holding steady for the rest of the year.
    - **South Africa:** the SARB is expected to cut rates by a further 50bps in the first half of 2025, targeting a terminal rate of 7.25%.
    - **Mexico:** gradual easing continues targeting a terminal rate of 8.5% (circa 150bps of cuts), with potential for more aggressive cuts.

Geopolitics shaping 2025

Geopolitical outlook

In 2024 the global economy demonstrated resilience, surviving a series of macro shocks such as high interest rates, fiscal challenges, climate issues and a struggling Chinese economy. Global inflation provided some relief, falling from the peak levels of 2023 resulting in monetary policy loosening.

However, trade tensions escalated, debt burdens rose, and geopolitical risks increased, potentially requiring structural adjustments in many parts of the globe. We hold the view that these developments would mostly likely dominate the outlook for this year and beyond.

The return of Trump

Last year was named the "voters' year", with at least 70 countries, representing nearly half of the world's population, holding national elections. The most consequential for the global economy and political affairs was the outcome of the U.S. presidential election, during which former President Donald Trump made a return to power. Several policy proposals that he campaigned on, if implemented, will accelerate protectionism, the fragmentation of the global economy which will encourage localisation and accentuate international frictions, with potentially siginficant negative spillovers for various economies and markets.

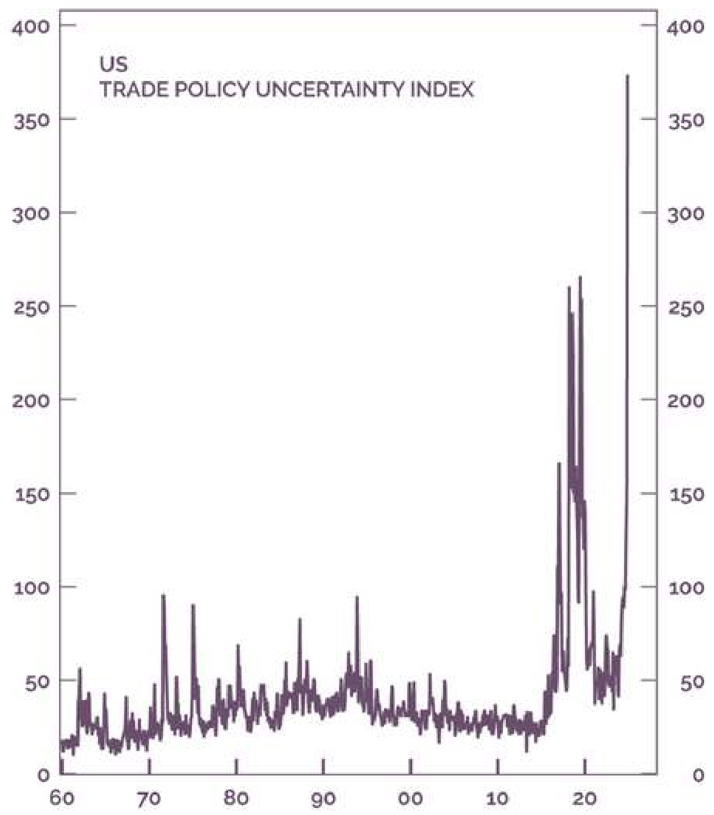
Tariffs and trade uncertainty

In an interview with Meet the Press earlier this year, President-elect Trump said that "tariffs are the most beautiful tool". He bemoaned the fact that he never really got the chance to go all out on tariffs in his first term due to the pandemic and he continued to criticise China for weakening its currency unfairly to gain a competitive advantage over the U.S. and other developed nations. If implemented as proposed, higher tariffs could severely disrupt China's export-driven economy, which is already grappling with structural challenges. For the EU, U.S. tariffs on European goods may slow GDP growth further by limiting export opportunities and increasing production costs.

"The U.S. Trade Policy Uncertainty Index hit a record high in November 2024, surpassing even the levels reached during Trump's first trade war."

In response, the U.S. Trade Policy Uncertainty Index compiled by Baker, Bloom and Davis hit a record high in November 2024, surpassing even the levels reached during Trump's first trade war [Figure 1].

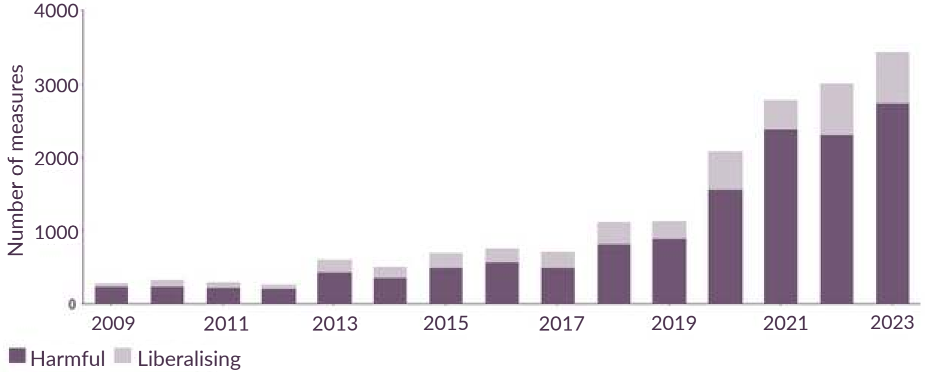
Figure 1: After the election, U.S. trade uncertainty surged



Source: BCA Research

CEOs globally rank intensified trade wars as the top geopolitical risk to their companies. According to a new survey from The Conference Board, tensions between the U.S., EU, China, Mexico and Canada will have the greatest geopolitical impact. The increase in trade interventions highlight the increasing complexities of global trade dynamics [Figure 2].

Figure 2: New trade interventions globally (2009 - 2023)



Source: BCA Research, Global Trade Alert

The IMF has pointed out that, when companies are highly concerned by uncertainty, they tend to adopt a wait-and-see approach. This depresses business investment and investors, who are wary of such volatility, prefer to be defensively positioned and cautious.

Regrettably, these global policy challenges also tend to affect emerging and vulnerable countries, where low growth threatens progress toward meeting sustainable development goals. Many low-income countries face unsustainably high fiscal debt levels, rising debt-servicing burdens and limited access to international funding. Compounding these issues are rising global income inequalities, which have reached uncomfortable levels.

Broader geopolitical flashpoints

Other major geopolitical risks that we are closely monitoring, given their potential implications for our investment strategy, include:

- **China-Taiwan tensions:** A potential Chinese invasion of Taiwan could trigger a global economic crisis, as Western nations are likely to respond with severe economic and military countermeasures, as previously warned. Recently, China has escalated its military intimidation against Taiwan and attempted to unilaterally alter the status quo across the Taiwan Strait.
- **Middle East conflict:** The ongoing military confrontation between Israel and Palestine is now expanding to other countries in the region. A further escalation in the Middle East could drive up uncertainty, push oil prices higher, and disrupt global efforts to contain inflation, ultimately slowing global GDP growth.
- **Russia-Ukraine war:** Trump has claimed he would broker peace between Russia and Ukraine, but we believe this will be a major challenge, given the deep geopolitical and economic implications for European countries and the NATO alliance.
- **US foreign policy uncertainty:** Trump's past rhetoric regarding Greenland, Canada and Panama raises concerns about the direction of U.S. foreign policy and international alliances. NATO leadership is expected to intervene to prevent further geopolitical instability.

Should any of these risks materialise, they could have profound implications for the U.S. dollar, oil prices, global inflation and economic growth across both advanced and emerging markets. Consequently, we are demanding a higher-than-normal risk premium for investments included in our portfolios. Additionally, we are limiting exposure to regions most vulnerable to these geopolitical escalations.

We have also been implementing currency hedging strategies to mitigate potential volatility by utilizing zero-cost collars, which involve simultaneously buying put options and selling call options at different strike prices. This strategy allows us to hedge against adverse currency movements while minimizing hedging costs, ensuring downside protection without additional upfront expenses.

Outlook and positioning

In summary, Trump's protectionist stance could stifle global economic integration, challenge supply chain efficiencies, raise global inflation and create growth bottlenecks for both advanced and emerging economies. This disruptive impact could be amplified by inevitable retaliation and a global sentiment slide which would be a major threat to the global economic progress achieved thus far. These developments threaten economic growth, political stability and can potentially elevate global recession risks later this year.

Given these uncertainties we favour the following strategies when considering allocation decisions:

- **Leaning towards defensive over cyclical stocks:** value-oriented equities tend to perform better in volatile environments.
- **Avoiding speculative positions:** heightened uncertainty makes high-risk investments less attractive.
- **Holding some cash early in the year:** provides flexibility to capitalize on opportunities as market conditions evolve.
- **Shifting to bonds as yields peak:** fixed income markets may present attractive entry points as rates stabilise.
- **Maintaining an underweight corporate credit:** elevated uncertainty and potential economic slowdown could impact corporate debt performance.

Market outlook

Global equity

Global equities: 2024 (another) year of concentration

When it comes to global markets, in order to work out where we are heading it is essential to assess where we have come from. In terms of global equity returns, suffice to say 2024 yielded surprising and polarised outcomes.

There are very few global investment managers who have not highlighted the extreme concentration in the source of equity returns in 2024. This narrow sourcing has been evident on a few levels, though the underlying cause boils down to the same fundamental contributors: significant outperformance of a handful of technology-related shares, almost all in the USA.

Notable facts to point out for 2024 include (in US$ total return terms):

- The AC World ex-US delivered 6.1% while the US market S&P 500 returned 25% (price return of 23%)
- The EAFE region returned 4.3%, underperforming Emerging Markets at 8.1%
- China returned 19.7%, rebounding from a decline of 11% in 2023
- Japan's performance of 8.7% in $ was diminished as a result of the Yen weakening materially against the US $ (in Yen the Japanese market delivered 21.2%)

Within the U.S. market, in 2024:

- Only 19% of companies within the S&P 500 outperformed the index
- The now widely acclaimed "Magnificent 7*" (Mag 7) stocks delivered a price return of 48% (after delivering 76% in 2023)
- The Mag 7 accounted for a 55% share of the S&P's returns in 2024 (after accounting for 63% in 2023)
- Excluding the Mag 7, the S&P 500 delivered a price return of 10%
- The 25% total USD return for the S&P 500 follows a 26% total return in 2023.

The last point above is particularly poignant as there have been only 5 prior occasions since 1951 where the S&P 500 rose by more than 20% per year over two consecutive years. 2024 therefore will go down as a significant and notable year in terms of US market returns, in part due to the high base that was already created in 2023.

The meaningful outperformance of the Mag 7 vs the S&P 500 is best graphically represented [Figure 1].

*Magnificent 7 includes Apple, Amazon, Alphabet (parent of Google), Meta, Microsoft, Nvidia, Tesla

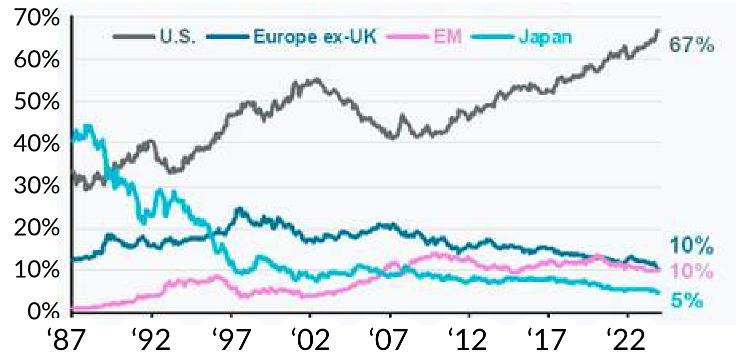
Figure 1: S&P 500 and Mag 7 cumulative total return
Cumulative total return, Based to 0 at Jan 2023

Source: Bloomberg, JPMAM (27 December 2024)

An imbalanced baseline for 2025

The sharp outperformance of the US market versus the rest of the world has resulted in further imbalances across global equity markets. Firstly, at 67% share of the MSCI ACWI, the US market is now at a 40+ year high in terms of its share of global market capitalisation [Figure 2], completely dwarfing all other markets.

Figure 2: Share of global market capitalisation
% weight in the MSCI All Country World Index, USD, monthly



Source: Bloomberg, JPMAM (27 December 2024)

Global equity

Secondly, at 21.5x, the valuation of the U.S. market as reflected in the P/E ratio is more than one standard deviation above the 30 year average multiple of 16.9x. In fact, on every standard valuation measure, the S&P 500 stands out as being in expensive territory [Figure 3].

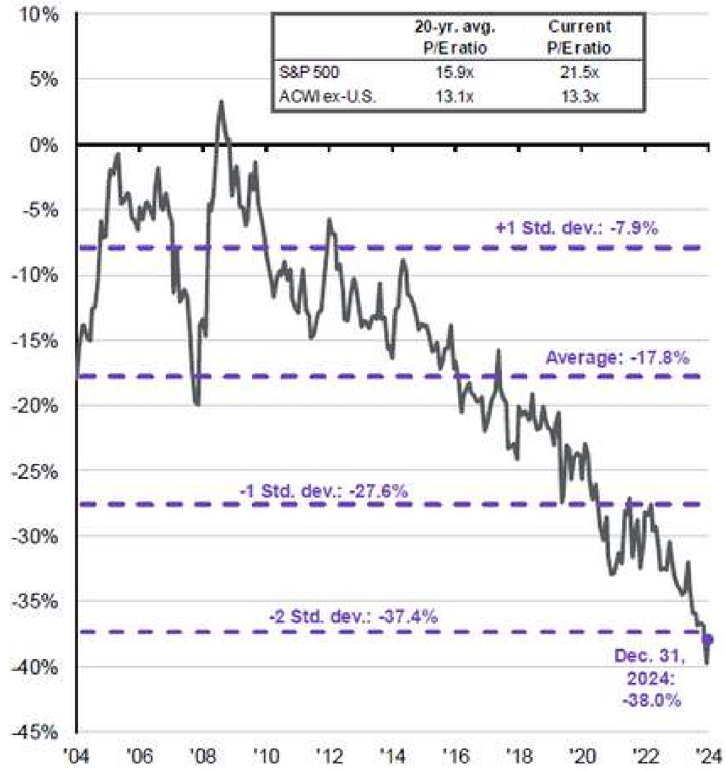
Figure 3: S&P 500 Index: Forward P/E ratio

Source: Factset, MSCI, Standard & Poors, JPAM

Conversely, global equity markets (ex-U.S.) are now trading at a P/E multiple discount versus the U.S. of 38%. This is more than two standard deviations away from the 20-year average P/E ratio discount of circa 18% [Figure 4].

This relative valuation gap is represented across all eleven key sectors in the MSCI ACWI, with international ex-U.S. Healthcare trading at the smallest discount to the U.S. and international ex-U.S. Financials and Consumer Discretionary sectors trading at significant discounts of circa 40-50% of their respective U.S. sector forward valuation multiples.

Figure 4: International: Price-to earnings discount vs. U.S.
MSCI All Country World ex-U.S. vs. S&P 500, next 12 months



Source: Factset, MSCI, Standard & Poors, JPAM

There is no doubt therefore that the fortunes of global investors have been tied intimately with the US market. The investment managers who outperformed either the S&P 500 or the MSCI World or MSCI ACWI were closely clustered among those who were overweight the US Mag 7 stocks (and also including software company SAP in Europe). This resulted in 2024 being a tough year for the majority of active managers.

Global equity

2025: Looking beneath the index hood

For bottom-up fundamental investors like Perpetua, while we are earnest in assessing the risks (absolute and relative), opportunities and valuations of each global equity market at a headline level, what always interests us more is how the component parts to each regional index are faring.

Unsurprisingly, it is the U.S. market that offers wide divergences in performance. The 21.5x current P/E multiple on the S&P 500 is derived as a result of the top 10 stocks trading at 29.8x and the remaining 490 stocks trading at 18.2x. This >10 point valuation gap reflects the opportunity that may still exist in the US market outside of the largest shares. This divergence within the U.S. is not a two-year phenomenon. If we go back a decade, we can see that the past ten years have really been all about U.S. large cap growth shares. On the lagging end, both in terms of price return and current valuation, we see everything else:

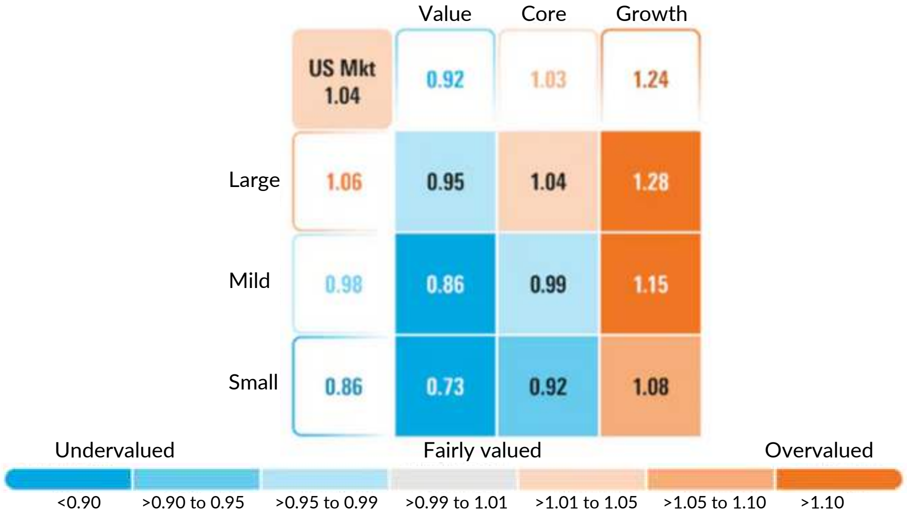
- US large cap value
- US small caps
- EAFE and EM all caps

For example, according to Morningstar's Price/Fair Value style box, there is a >30% valuation differential between US large cap growth vs US large cap value [Figure 5].

Many global investors justifiably argue that the reason for the superior performance of the US equity market is directly attributed to the better relative performance of the US economy; the US' superior level of widescale innovation resulting in stronger returns and higher levels of profit for US companies. However, what is often missed for international equity markets is that the larger developed markets such as the UK, Europe and Japan are much more exposed to the global economy rather than their own domestic economies. The UK equity market is the one global stock market that is least representative of the domestic UK economy with close to 80% of revenue of companies listed in the UK stock market being earned outside the UK [Figure 6].

This is an important factor to consider as several companies listed in the developed markets ex-US could perform well, even if their respective domestic economies do not. Companies listed in emerging markets are however much more representative of their domestic economies, with listed EM companies deriving just over a third from foreign economies [Figure 6].

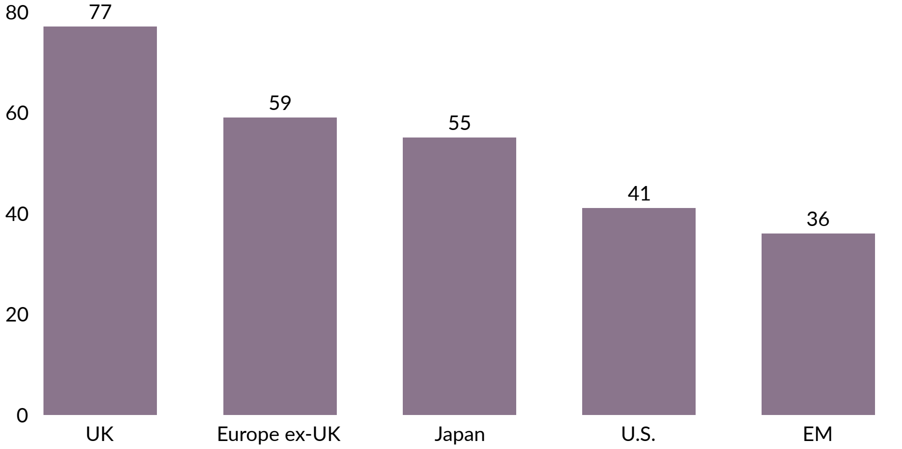
Figure 5: Price/Fair Value by Morningstar Style Box



Source: Morningstar Research Services, LLC. Data as of January 6, 2025

Figure 6: Revenue exposure vs. country of listing

% of total revenue derived from foreign countries



Source: Factset, MSCI, Standard & Poors, JPAM

Global equity

Outlook and positioning

Against an intriguing backdrop, global equity investing presently is shaped as much by a blend of risks as it is by a range of opportunities. With the context of rapid technological advancements, geopolitical tensions and divergent monetary policies, we expect moderate global growth but with significant regional variations. Our positioning is reflective of the combination of our top-down assessments and bottom-up analysis and insights. Within our multi-asset class portfolios, our total global exposure is below the Regulation 28 maximum of 45%. This reflects a reduction versus a year ago, mindful of the overheating of the US market and the extent to which it drives overall global equity returns. Within our global equity exposure, we have taken active positions given our outlook for the regions and how we see this evolving through the year.

Equity market	Outlook	Positioning
U.S. and North America	With valuations in overvalued territory and the meaningful contribution that ratings changes (P/E multiple) expansion having played in overall U.S. equity returns, we remain cautious on the outlook for the S&P 500 in 2025. Given current price and valuation levels, we believe a correction is likely for the overall US market in 2025. and this could be precipitated by evidence of the difficulty for AI giants (mega cap tech) struggling to deliver the levels of revenue required to justify vast amounts of AI-related capex, leading to declining returns. The Trump wild card also creates an environment of geopolitical uncertainty for how China and rest of the world will react to U.S. positions and threats.	We remain meaningfully underweight the U.S. market versus its weight in the MSCI World and All Country World benchmarks. Specifically we are underweight the U.S. large cap technology shares as we believe share prices reflect a stretched reality even on very optimistic assumptions. Within the U.S. we favour financials, healthcare and communication services as well as select consumer shares. We are particularly interested in parts of the market which have lagged.
UK and Europe	In terms of the macro-economic outlook, the Eurozone and UK continue to face economic uncertainty and growth challenges given a combination of inflationary pressures, energy price volatility and overall weak corporate earnings momentum. We see this sluggish outlook remaining in 2025. This leaves the region as highly neglected by global investors.	We are finding meaningful mispricing in international equities ex-US and they represent a material active regional position. These opportunities are not constrained to specific sectors but are driven more by individual stock-specific opportunities whose investment cases are more driven by management action and industry shifts.
Japan	In local currency terms, the Japanese market has been on a positive trajectory over the past two years. This has been driven by the onset of sticky inflation (after decades of deflation) resulting in pricing power for companies and an environment of meaningful corporate governance reforms. The largest detractor has been the Yen. We are constructive on the Yen expecting it to strengthen.	Investing in the Japanese market is a combination of two cohorts of companies: the exporters and the domestically-oriented companies. The former, typically larger, have benefitted from both more active value- unlocking corporate restructuring activities and the weaker Yen. We are finding interesting opportunities in companies exposed to the domestic consumer, who is proving to be resilient. We expect to increase our exposure to Japan in 2025.
China and Emerging Markets	China as an equity market is likely to be range bound as the benefits of economic policy stimulus will be tempered by regulatory uncertainty and geopolitical risks, together with weak consumer sentiment. Other emerging markets offer a mixed outcome and will perform more in line with their prospects for domestic demand.	The poor investor sentiment around China has generated several investment opportunities and we remain exposed to Chinese companies that we believe will benefit from economic recovery specifically in consumer industries. We remain vigilant on our overall regional exposure. Latin America is a region we expect to add to in 2025.

Domestic equity

Domestic equities: a fine balance

The Capped ALSI returned 13.4% for 2024, underperforming the ALBI's 17.2% return. This continues a three-year trend which has seen the ALBI outperforming the ALSI by 1.6% p.a. [Figure 1]. The underperformance is largely due to weakness in the Resources sector, while Financials and Industrials have performed better.

Figure 1: SA equity performance over 1 and 3 years

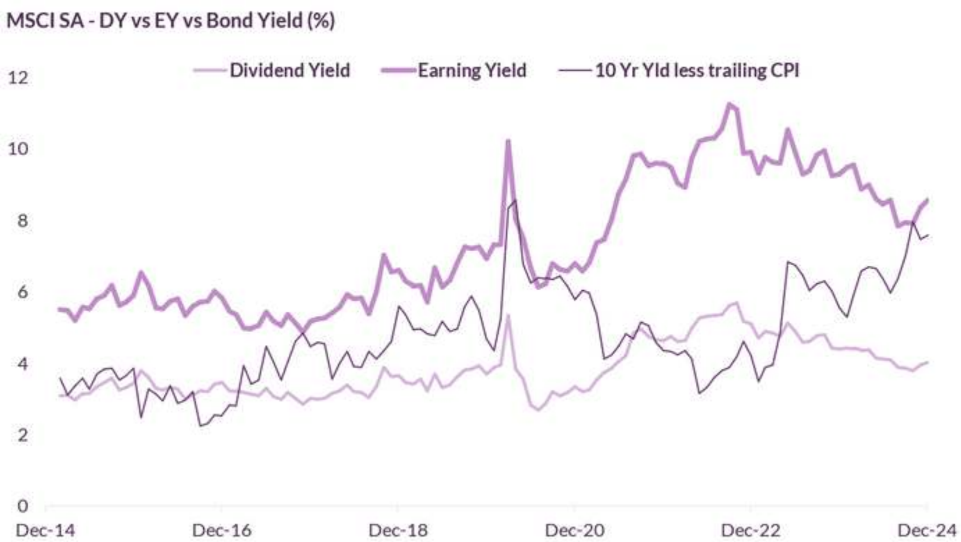
Source: FactSet, SBG Securities analysis

Over the past decade, the return differences between the ALBI and ALSI have been negligible. This often raises a key question during asset allocation discussions: What happened to the equity risk premium? Currently, the spread between the real 10-year bond yield and equity yield is unusually narrow, whereas equity yields are typically 3-4% higher [Figure 2]. This aligns with our observation that, as the market rebounded from the 2024 pre-election lows, projected returns compressed.

In determining optimal asset allocation, we consider macroeconomic factors alongside bottom-up forecasts, and then make tactical adjustments to strategic asset allocations. For instance, when the S.A 10-year bond yield exceeded 12% in early 2023, we limited equity purchases to those expected to deliver returns above 17% p.a. — a notably high hurdle rate.

Relative to our peers, we estimate that our current domestic equity exposure is approximately 8% lower.

Figure 2: SA equity yields vs bond yields

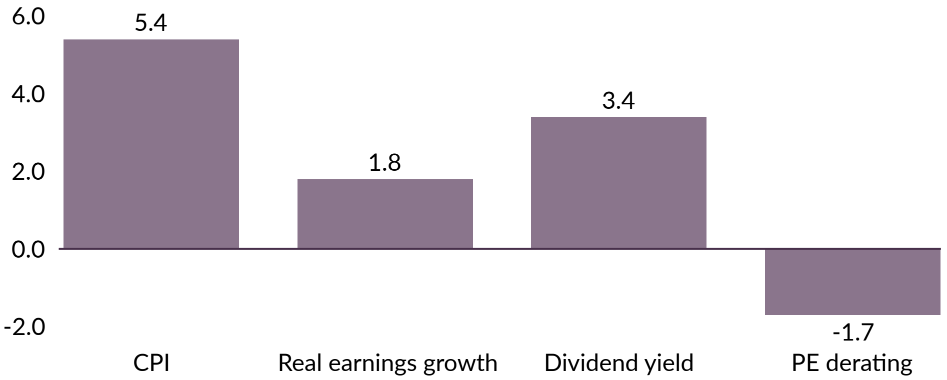


Source: RMB, Morgan Stanley

Domestic equity

The implication of the chart above [Figure 2] is that equities really must deliver (above average) earnings growth in order to outperform bonds. A decomposition of the lacklustre 9% p.a. return over the past decade reveals that the earnings growth was not enough to offset the de-rating in investor sentiment (using the P/E ratio as a proxy) [Figure 3].

Figure 3: Decomposition of ALSI returns over the past decade



Source: Perpetua Research

Given these conditions, the key question is whether earnings growth will improve. While it remains uncertain whether the post-election recovery marks a turning point, we are skewed toward the following drivers:

Resources sector that has de-rated

Commodity prices are largely fair relative to our expectations of normal, except for PGMs (25% below) and Gold (20% above). Notwithstanding this, the current share prices are attractive relative to our valuations, with the sector on average at 0.7x fair value. The market is pricing in a worsening outcome for commodity prices. It has become increasingly clear that China is facing a multi-year property sector slowdown and can no longer rely on infrastructure investment to fuel GDP growth. Should President Trump follow through on the US's pre-election tariff threats, this is likely to further dampen metal demand. All this has implications for many of the commodities that were used to accelerate China's growth over the past two decades. Perhaps the narrow channel that iron ore now trades in provides the best depiction of this - the good days of iron ore at $150+ are long behind us [Figure 4].

Figure 4: Iron ore spot price

Source: Bloomberg

We started 2024 underweight the resources sector but increased exposure as valuations became attractive. However, the extent of the overweight is marginal. The reason for this is that our Global Macro-economic heatmap is showing a heightened level of risk. Since the resources sector is economically sensitive, the sector may underperform if these risks materialise, notwithstanding more attractive valuation levels. This will present a potential buying opportunity.

Recovery in domestic consumption

While long-term employment trends have constrained consumption growth, 2024 saw a 1.2% increase in employment, particularly in Construction. The Pnet Job market Trends report highlights employment opportunities in the Architecture and Engineering fields. These are typically leading indicators for further construction sector jobs growth. However, the environment is still precarious as the private sector recorded a broad-based reduction in the number of employed people. We do, however, expect a near-term improvement in disposable income. The Repo rate peaked at 8.25% in September 2024 and has declined by 0.5% since. In the last quarter CPI was reported at 2.8%, below the bottom end of the inflation range. Real interest rates are high, even if inflation increases from the current lows. There is room for further interest rate cuts which will likely boost consumer sentiment and spending.

Domestic equity

The Consumer discretionary sector returned 11.3% vs ALSI's 7.3% over the six month period after the national elections. Following a 90% gain in Mr Price's stock, we reduced our position as its forward P/E doubled to 20x. Nonetheless we continue to identify promising opportunities, particularly in gaming stocks like Tsogo Gaming and Sun International, as well as companies that are exposed to the vehicle sales value chain.

However, we do remain cautious that a sustained recovery in domestic demand requires a fundamental improvement in household incomes. Consequently, we have maintained cautious exposure to counters that also exhibit defensive characteristics such as Consumer Staples, our current largest active position. These counters have not displayed their defensive qualities for various reasons over the past few years. These include weaker balance sheets (AB Inbev and Spar), as well as changes in technology and consumer tastes (BATS). We believe that all these companies have taken steps to address the challenges they have faced. Importantly the share prices don't reflect these ongoing improvements as all these counters are attractively valued.

Companies with improving shareholder returns and payouts

Over the past decade, South African businesses made significant capital allocation errors. Some of the major write downs, totaling more than R1trn are listed below.

Significant impairment write downs over the past decade

Company	Total impairment write down	Cause of write down
BATS	R641bn	$50bn acquisition of Reynolds. $30bn impaired.
Steinhoff	R280bn	Fraud and corruption.
Sasol	R140bn	$13bn Lake Charles Chemical project. Subsequently 50% was sold for $2bn.
Anglo American	R110bn	Minas Rio Iron ore project capex and $2.9bn investment into the crop nutrients division.
BHP	R78bn	Write downs relate primarily to the Jansen Potash project. Once fully ramped up BHP would have spent $13bn on the project.

Whilst we have focused on the more eye-watering sums, there are many instances of companies that made bets that were disproportionate to their size that subsequently did not deliver the expected outcomes. In most cases, the companies incurred additional debt, and curtailed shareholder returns to finance these expansions. With the benefit of hindsight, these turned out to be a massive cost, including the opportunity cost of these mostly not delivering returns. British American Tobacco's ROICs declined from a 15-year average of 16% to a 3-year average of 6%. As we look ahead, we see less instances of companies that are gearing up and embarking on these large-scale capital allocations. There are some businesses that are structurally challenged. For example, in the Top 40, the Telcos have recorded amongst the largest declines in asset turnover (a measure of how efficient assets are in generating revenue).

This is in part due to the capex intensity and low revenue growth nature of the industry. Nonetheless, in most cases, as the JSE has de-rated, we see a greater number of companies that have significantly deleveraged and are increasing shareholder distributions. The recent decision by Super Group to sell the Australian business unit (SG Fleet) and return 70% of the pre-deal market capitalization is a good illustration of this trend. We believe that these increased distributions, coupled with more prudent capital allocation will result in improved shareholder returns.

Outlook and positioning

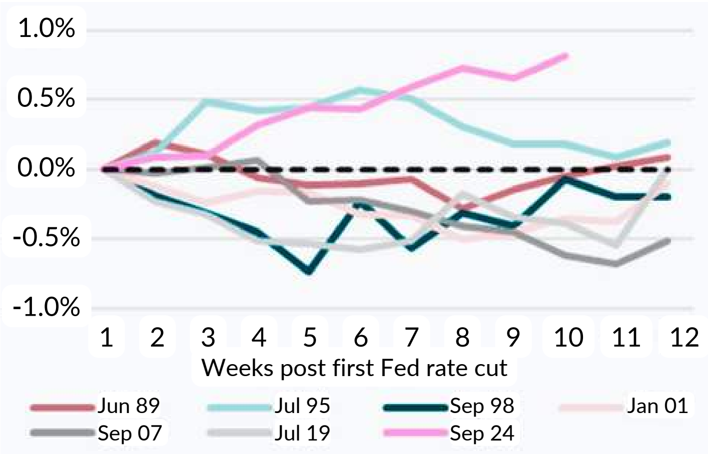
The South African equity market was not a happy hunting ground for investors over the past decade. While prospects for improvement exist and the market is cheap, the preconditions for improving earnings growth are still pending. The reduced political uncertainty's impact on policy implementation is unclear, and SA Bonds offer compelling real yields, demanding higher equity return thresholds. In addition, global market concerns persist. Our current positioning across asset, stock, and sector allocations reflects a balanced approach of exposing clients to a cheap market with the potential for a recovery, while mitigating the threats to such a recovery. We believe that this strategy will deliver on the mandate under varying scenarios.

Fixed income

Yields moving higher

In sharp contrast to previous rate-cutting cycles, the U.S. 10-year yield has increased by approximately 100bps since the Fed's first rate cut in September 2024 [Figure 1]. This reflects expectations around Trump's proposed economic policies, fears of an inflation resurgence and ongoing strength of the U.S. economy.

Figure 1: U.S. 10-year yield increases sharply after the first Fed rate cut in Sep 24, in contrast to previous rate-cutting cycles



Source: Bloomberg, IML estimates

Inflation differential to narrow

Domestically, we expect the narrow inflation differential of 1.5% between South Africa and the U.S. [Figure 2] to persist. South Africa's risk premium, as defined by the 5-year Credit Default Spreads (CDS), is currently trading at a premium compared to other sub-investment grade countries, suggesting potential scope for convergence [Figure 3].

Figure 2: South Africa – U.S. inflation differential. Currently at 1.4% vs. long term average of 2.9%

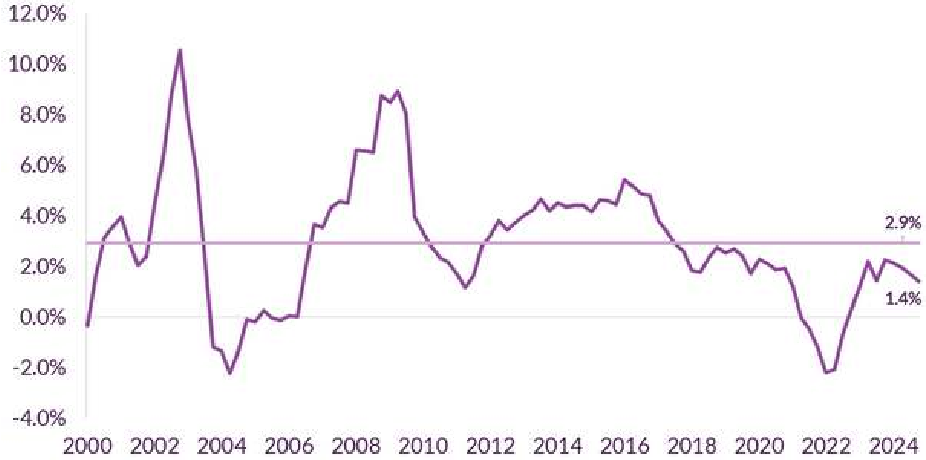
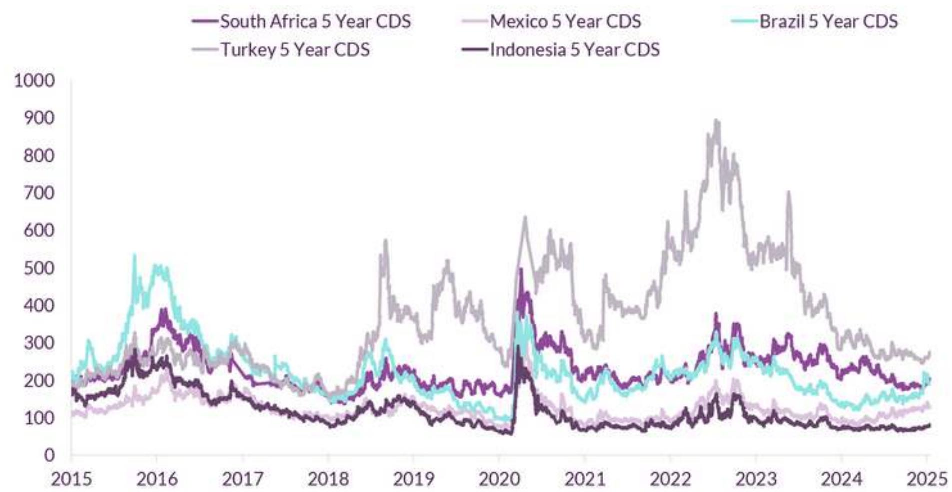


Figure 3: Scope for lower S.A risk premium



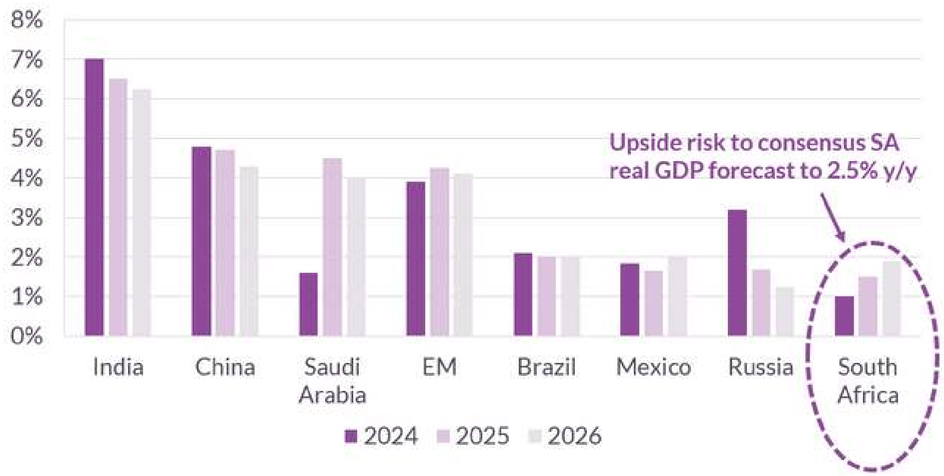
Source: Bloomberg, IML estimates

Fixed income

Improved growth outlook

South Africa's growth outlook is showing signs of improvement, with an uplift in real GDP growth forecast to reach approximately 2.5% in 2025, outperforming EM peers like Mexico (1.6%) and Brazil (2.0%) [Figure 4].

Figure 4: South African GDP improving relative to Brazil and Mexico



Source: Bloomberg, IML estimates

This optimism is driven by several key growth drivers:

Real Gross Fixed Capital Formation (GFCF): expected to grow by 4% y/y, potentially lifting real GDP growth to 2.5% y/y in the medium term. This is driven by:

- A R200 billion catch-up on the backlog in infrastructure and rolling stock maintenance across Transnet Freight Rail.
- Eskom's projection of R200 billion in grid expansion spending over the next decade.
- South Africa's renewable energy pipeline with a combined capacity of 22.5GW and an estimated investment value of R390 billion, is expected to increase energy availability by approximately 20% by 2026. This would raise the Energy Availability Factor (EAF) to 75%.

Two-pot retirement reform: the anticipated R50 billion in retirement savings withdrawals for 2025 is expected to contribute an additional 0.5% or more to GDP growth.

Lower interest rates: expected to boost disposable income, encourage consumer spending and stimulate corporate investment.

Scenarios

Based on the above factors we forecast bull, base and bear case scenarios for SAGBs, assuming an inflation differential of 2.5% and a S.A. sovereign risk premium of 3.5% (the average risk premium between 2011 – 2019 was 2.6%).

	Bull-Case	Base-Case	Bear-Case
US 10-year govt bond yield	3.8%	4.3%	4.6%
Inflation differential (SA - US)	2.0%	2.3%	2.5%
Risk premium	3.2%	3.5%	4.5%
SA 10-year govt bond yield	9.0%	10.1%	11.6%
SA Bonds 12-month total return expectations	15.9%	10.3%	2.0%

Source: Perpetua Research, IML estimates

South African Government Bonds (SAGBs): pricing vs. fair value

There has been a significant widening in the short-end of the curve as uncertainty grips the market, causing front-end bonds to cheapen considerably.

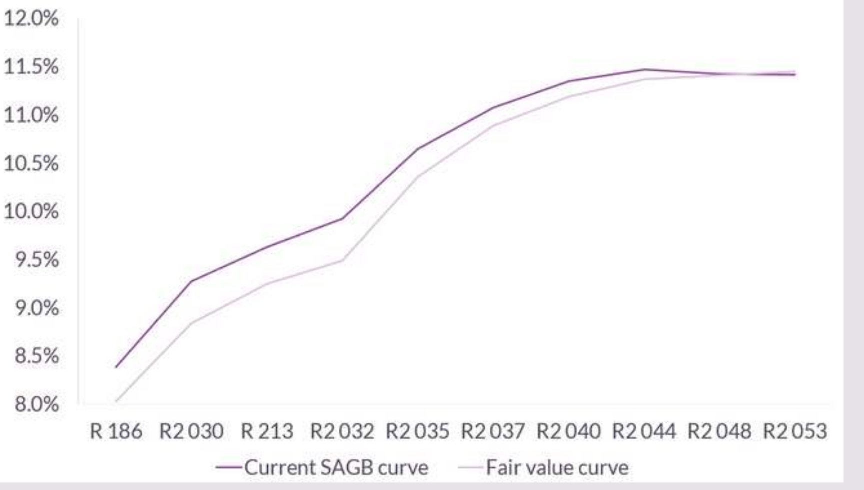
The SAGB curve is currently higher than our fair value curve, particularly in the shorter end [Figure 5]. This analysis assumes a Fed terminal rate of 3.75%, a SARB rate of 7.25%, a debt-to-GDP ratio of 75% and a current account deficit of -2.5%.

Under our base case scenario, SAGBs have some room to rally further. However, if our bear case materialises, the current curve looks to be at fair value or possibly slightly expensive.

Fixed income

That having been said, given the positive outlook on growth, coupled with contained inflation and lower interest rates, the domestic outlook appears decidedly more favourable than the global picture [Figure 6].

Figure 5: Our fair value curve is projected lower than the current SAGB curve, indicating potential for SAGB's to rally



Source: Bloomberg, Perpetua Research

Figure 6: 12-month expected forecast for 10 year government bonds

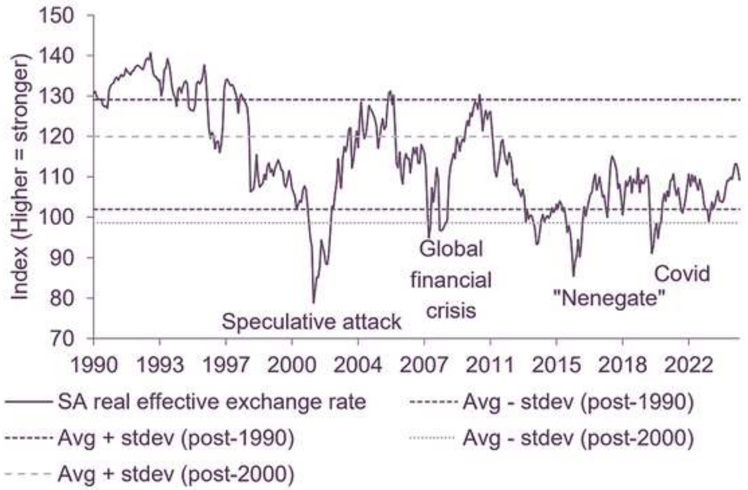
Source: Trading Economics

Fixed income

USDZAR

We firmly believe the rand is undervalued against the dollar and we expect this trend to reverse in the coming months as U.S. policies become more evident. This undervaluation is largely a function of dollar strength rather than ZAR weakness, as the rand is still somewhat resilient against its peers and on a trade weighted basis [Figure 7].

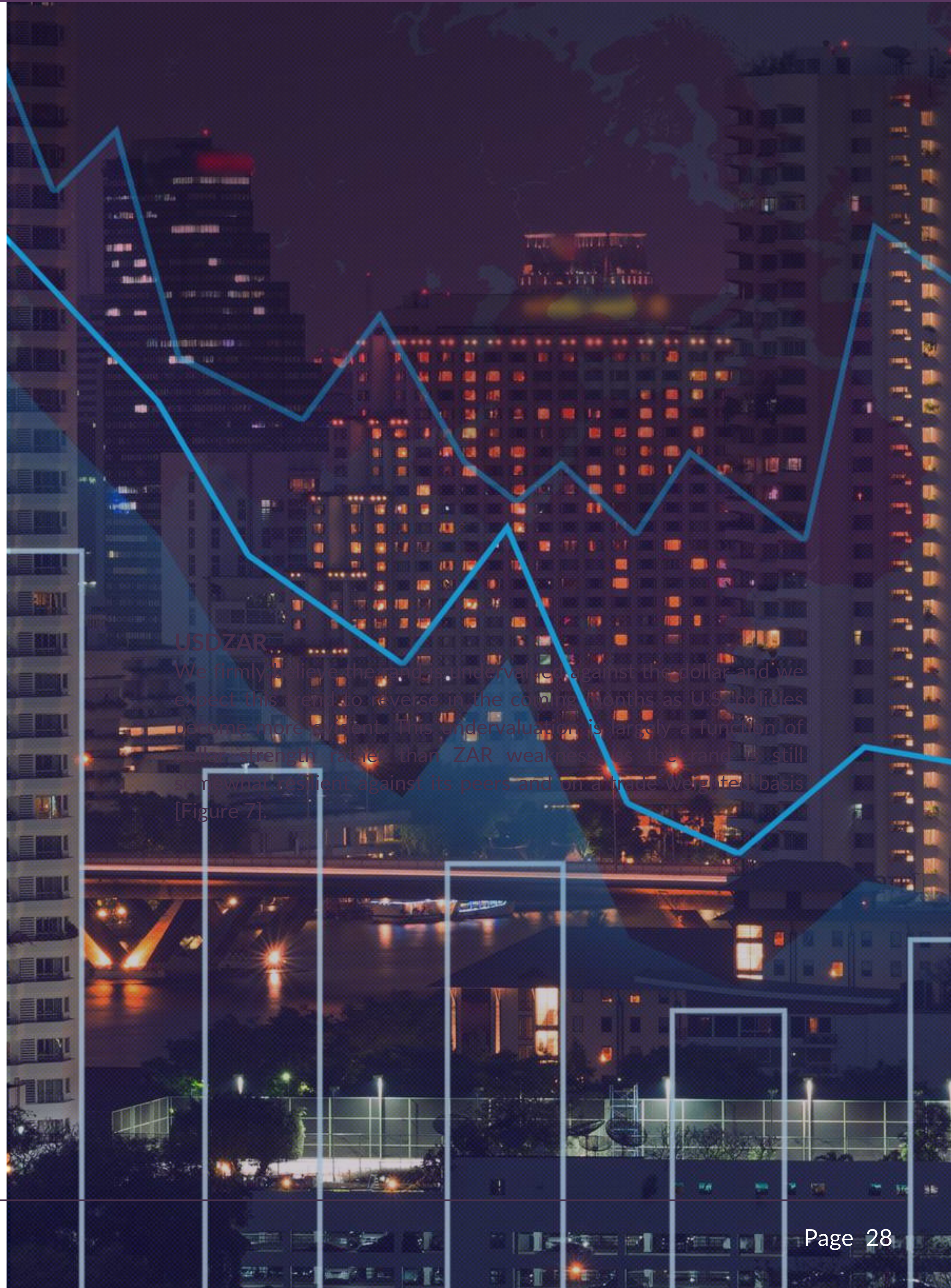
Figure 7: South African real effective exchange rate (REER) benchmarked against its long-term average, with one standard deviation above and below the post-2000 average



Source: Standard Bank

Positioning

- We maintain our long position in SAGBs, primarily in the belly of the curve.
- Given the expected heightened volatility in the U.S., we maintain our cash (3 month T-bills) position in terms of offshore fixed income and remain underweight U.S. Treasuries relative to our strategic asset allocation.
- We expect the rand to strengthen in the months ahead. Therefore, we will take advantage of its current weakness to institute fresh currency hedges, mitigating any currency exposure.



Property

Asset class performance

South African listed property returns have been highly volatile in recent years, primarily due to negative sentiment stemming from excessive debt levels, corporate governance issues and unsustainable distributable earnings, all exacerbated by the global pandemic in 2020. However, 2024 marked a turning point with slowing inflation, easing interest rates, stable energy generation, a favourable election outcome and a re-rating of local bonds. These factors sparked renewed investor interest, leading to a significant re-rating of the sector. The sector outperformed equities and bonds in 2024, delivering returns of 29%, compared to 17% for bonds and 13% for equities [Figure 1].

Improving property fundamentals

Property fundamentals are on an upward trajectory, driven by several key factors:

- **Improving balance sheet strength**: the pandemic pushed the sector's debt-to-assets ratio to a peak of 42%, largely due to falling property valuations and increased financial risk. To address this, many funds had to decrease their balance sheet risk through a combination of asset sales, scrip dividends, lower pay-out ratios and equity bookbuilds. The sector's financial position has improved, with the current debt-to-assets ratio at 38%, well below the regulatory limit of 50%.
- **Declining interest rates:** lower borrowing costs reduce financing expenses for property developers and landlords, encouraging investment and supporting rental growth.
- **Stabilising energy supply:** reduced load-shedding and increased investment in renewable energy projects are creating a more stable operating environment for businesses and tenants.
- **Improved economic conditions:** easing inflation and higher consumer confidence are boosting retail performance and demand for industrial spaces.
- **Rising occupancy rates:** vacancy rates, particularly in retail and industrial sectors, have declined significantly, enabling landlords to negotiate better rental terms.
- **Cost management:** a healthier cost of occupancy and declining municipal and utility cost pressures are improving profitability for landlords.
- **Targeted investments:** the focus on high-demand sectors like logistics and warehousing is driving growth in industrial properties, while retail fundamentals are supported by improved trading densities.

Figure 1: Asset class performance

Source: Bloomberg

Property

While the retail and industrial sectors have shown signs of improvement, the office sector remains challenged by oversupply and structural shifts such as hybrid work models. Specifically, we see the following elements driving the property segments respectively:

- **Retail:** strong performance with declining vacancies (2%) and growing trading density (+6.2%). The cost of occupancy, a leading indicator for rental growth, is at its healthiest in over a decade. The lower-income and higher-income segments are proving to be better positioned.
- **Industrial:** the standout performer with robust rental growth (+6.5%) and ultra-low vacancies (3%-5%), driven by demand for logistics and warehousing.
- **Office:** continues to struggle with high vacancies (13.7%) and negative rental trends due to oversupply, with limited new development activity. We envisage that it will still take a few years for rental growth to return to this market segment.

Outlook and positioning

We believe that the bond market re-rating drove the sector's outperformance in 2024. The property sector is sensitive to this variable. While the interest rate cutting cycle has commenced, many companies have hedged interest rates at a higher level, and it will take time to reap the benefits of lower interest rates. Nonetheless, we have noted the improved underlying fundamentals for some counters over the past year. Specifically in better quality retail. We are underweight the sector in our funds but have started to increase exposure to counters that exhibit the following characteristics:

We favour property counters with the following characteristics:

- High-quality retail exposure;
- Low and stable vacancies;
- Attractive dividend yields on low earnings;
- Negligible office exposure;
- Offshore exposure that will diversify earnings and not detract;
- Manageable or improving loan-to-value (LTV) ratios; and
- An accretive development or growth pipeline.

Portfolio Management Team

Delphine Govender is Perpetua's CIO and has ultimate responsibility over the entire investment function and capability; this includes accountability over investment performance; ensuring that the integrity of the investment philosophy is maintained; the investment process is consistently applied (and refined where required) and that team succession planning is considered. Delphine has portfolio management responsibilities over all asset classes as well as leading the global equity capability. She has 27 years' investment experience is a qualified CA(SA) and CFA charterholder.

Lonwabo Maqubela is Perptua's Deputy CIO and one of Perpetua's equity and balanced portfolio managers. He has over 18 years' investment management experience. He joined Perpetua as one of the firm's first team members in 2012. Lonwabo began his journey with Perpetua as a senior analyst and was promoted to a portfolio manager in 2014. Lonwabo is responsible for leading all growth assets at the firm. He is a qualified CA(SA) and CFA charterholder.

Patrick Ntshalintshali is one of Perpetua's equity and balanced portfolio managers. He is responsible for the portfolio risk management aspects of the equity portfolios and direct mentoring of analysts. He is also a Director of Perpetua and fills the role of Portfolio Risk Manager. Patrick has over 28 years' experience in the investments industry spanning primarily listed equity investments as well as private equity. He holds a BCom Hons degree and an EDP.

Pooja Tanna is the portfolio manager for Perpetua's fixed income products which include the following strategies - Enhanced Cash, Domestic Bond Fund, and Flexible Fixed Income Fund. She also manages the fixed income assets within Perpetua's multi-asset class funds and is responsible for leading income assets at the firm. Pooja has over 19 years' financial services experience of which the past 18 years has been spent directly in the field of fixed income – across fixed income trading, interest rate structuring, derivatives trading and portfolio management. She holds a BSc and BSc Hons degree in Mathematical Statistics.

Ryan van Breda is the portfolio manager for credit (Public and Private markets). Ryan has over 18 years' working experience in the financial services industry, of which 11 years has been spent in the positions of being a portfolio manager in credit and structuring at Prescient Investment Management and Ngwedi Investment Managers. He also launched the Prescient Clean Energy and Infrastructure Debt Fund. He has a B Com (Hons), M Com and also is a FRM.

Invest with us

Mandate	Fund strategy
Perpetua Domestic Focused Equity	The Perpetua Domestic Focused Equity portfolio aims to deliver superior risk-adjusted returns relative to the market benchmark in the medium to long term by using Perpetua's bottom-up research and stock selection, and high conviction portfolio construction within a defined risk-conscious investment process. The portfolio is suitable for investors who are seek long term alpha generation from a strategy benefiting from strong stock selection while seeking to minimise permanent capital loss.
Perpetua Domestic Core Equity (SWIX)	The Perpetua Domestic Core Equity portfolio aims to deliver superior risk-adjusted returns relative to the market benchmark in the medium to long term by using Perpetua's bottom-up research and stock selection while controlling the risk of underperformance in the short term through portfolio construction. The portfolio is suitable for investors who seek long term alpha generation while limiting the risk of short-term underperformance.
Perpetua Domestic Core Equity (Capped SWIX)	The Perpetua Domestic Core Equity portfolio aims to deliver superior risk-adjusted returns relative to the market benchmark in the medium to long term by using Perpetua's bottom-up research and stock selection while controlling the risk of underperformance in the short term through portfolio construction. The portfolio is suitable for investors who seek long term alpha generation while limiting the risk of short-term underperformance.
Perpetua Global Focused Equity	The Perpetua Global Equity UCITS Fund aims to outperform the benchmark MSCI All Country World Index in the medium to long term by using Perpetua's bottom-up research and stock selection to build a high conviction portfolio within a defined risk-conscious investment process, consisting of shares listed on developed and emerging market stock exchanges. The Fund is suitable for investors who accept short term volatility in the pursuit of long-term alpha generation. The strategy is available as a segregated portfolio for clients investing in excess of $25m.
Perpetua Global Core Equity	The Perpetua Global Core Equity portfolio aims to deliver superior risk-adjusted returns relative to the MSCI World Index in the medium to long term by using Perpetua's bottom-up research and stock selection while controlling the risk of underperformance in the short term through portfolio construction, limiting the tracking error. The portfolio is suitable for investors who seek long term alpha generation while limiting the risk of short-term underperformance.
Perpetua Developed Market Focused Equity	The Perpetua Developed Market Focused Equity portfolios aims to outperform the benchmark MSCI World Index in the medium to long term by using Perpetua's bottom-up research and stock selection to build a high conviction portfolio within a defined risk-conscious investment process, consisting of shares listed on developed market stock exchanges. The Fund is suitable for investors who accept short term volatility in the pursuit of long term alpha generation.
Perpetua International Focused Equity	The Perpetua International Focused Equity portfolios aims to outperform the benchmark MSCI EAFE or MSCI World ex-US Index in the medium to long term by using Perpetua's bottom-up research and stock selection to build a high conviction portfolio within a defined risk-conscious investment process, consisting of shares listed on developed market stock exchanges outside of the USA. The Fund is suitable for investors who accept short term volatility in the pursuit of long term alpha generation.

Mandate	Fund strategy
Perpetua Domestic Balanced	The Perpetua Domestic Balanced portfolio is a multi-asset class portfolio investing in equities, bonds, cash and commodities in South Africa, subject to the restrictions of Regulation 28. The Fund is managed in a manner to deliver returns above long term target of SA CPI+5%. The strategy benefits from Perpetua's top-down macro-driven asset allocation process combined with bottom-up fundamental asset class research and stock-picking.
Perpetua Global Balanced	The Perpetua Global Balanced portfolio is a multi-asset class portfolio investing in equities, bonds, cash and commodities in the domestic and global markets subject to the restrictions of Regulation 28. The Fund is managed in a manner to deliver returns above long term target of SA CPI+5%. The strategy benefits from Perpetua's top-down macro-driven asset allocation process combined with bottom-up fundamental asset class research and stock-picking.
Perpetua Cash Enhanced	The Perpetua Cash Enhanced portfolio is designed for investors who have a need for a competitive return while avoiding any capital loss in the short term. It will aim to deliver returns 1.0% per annum above the Short-Term Fixed Interest rate (SteFI) benchmark before fees, and will do so by investing in short-term credit opportunities, notes, derivatives, short-dated government bonds and collective investment schemes/funds.
Perpetua Flexible Fixed Income	The Perpetua Flexible Fixed Income portfolio provides investors with a blend of stability, income and capital appreciation. The fund aims to deliver outperformance against the BEASSA ALBI benchmark by investing in credit opportunities, duration positions, structured notes, derivatives and alternative strategies. The fund aims to minimise volatility by utilising the various instruments in the fixed income universe.
Perpetua Domestic Bond portfolio	The Perpetua Domestic Bond portfolio seeks to generate capital and interest returns by investing primarily in South African government, parastatal and corporate bonds. The portfolio aims to deliver excess returns by investing in fixed income instruments offering superior yields which actively managing duration and credit, thereby limiting downside risk.

For more information on our products, view them on our website.

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