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

Performance and fund positioning

The Fund returned 1.93% over the last quarter (Q1), which was ahead of the STeFI composite benchmark return of 1.89%. Since inception, the Fund has returned 9.18% p.a., which is ahead of the benchmark return of 8.35% p.a.

Economic developments over the last quarter presented a mixed picture, influenced by ongoing global economic uncertainty and domestic developments surrounding the revised national budget. On the growth front, real GDP showed a weak recovery in Q4-24, with 0.6% quarter-on-quarter (q/q) growth, bringing the annual growth for 2024 to just 0.6%. While there was a rebound in agricultural output, services, and trade, this was offset by weakness in mining, manufacturing, utilities, and transport. Inflation continued to disappoint to the downside with the February print coming in lower than expected at 3.2% year-on-year (y/y). This was driven by softer food and discretionary goods prices and weaker-than-expected pass-through from the annual insurance survey, with core inflation at 3.4% y/y.

Despite subdued growth and inflation figures, the South African Reserve Bank's (SARB) Monetary Policy Committee maintained the repo rate at 7.5% during their March meeting, following January's 25 basis points (bps) reduction. The committee adopted a more conservative approach in response to heightened global economic uncertainties, despite revising inflation forecasts downward and noting subdued domestic economic activity. For 2025, the SARB projects headline inflation at 3.6%, with risk factors balanced but possible upward pressure in the longer term. Their GDP growth forecast for 2025 was moderately adjusted downward to 1.7%. The committee continues to monitor divergent global monetary policy trends carefully, with particular attention to the US Federal Reserve's prudent approach. While current economic indicators might support further monetary easing, our analysis suggests the SARB will likely maintain prevailing rates throughout the year, particularly considering the current fiscal environment.

A review of recent developments provides valuable context to the current fiscal predicament. The initial budget submission included proposals for incremental VAT increases of 0.5% over two consecutive fiscal years, combined with bracket creep adjustments. These measures were intended to support new expenditure initiatives, primarily focusing on infrastructure development, public sector compensation, essential services, and social grant continuation. National Treasury also made a commitment to fiscal discipline through enhanced expenditure monitoring and personnel reviews. While the initial budget framework showed promise, significant implementation hurdles emerged as key areas of concern. Current indications suggest the proposed revenue enhancement measures will proceed, though they may face challenges through various committees and judicial processes. In short, the budget outlook remains unclear.

Unfortunately, the budget details have been overshadowed by broader political dynamics. What should have been a demonstration of the Government of National Unity's (GNU) collective economic management has instead raised questions about the coalition's sustainability. It seems that all partners share some responsibility for this predicament. The ruling party undermined its relationship with the DA by seeking support from other parties for the budget. The DA, in response, attempted to leverage this situation to advance other priorities, such as concessions on the Expropriation Act and greater involvement in economic policymaking. While there is more certainty on the budget outcome despite opposition concerns, the lack of progress on other issues clearly remains problematic. Markets are likely to remain cautious until there is greater clarity on the GNU's future, and sadly, the actual impact of the budget on the future fiscal trajectory of the country seems to be a secondary consideration at this point.

The quarterly returns of fixed income asset classes were mixed. The FTSE/JSE All Bond Index (ALBI) returned 0.7% for the quarter. Within the ALBI, the one- to three-year and three- to seven-year buckets showed stronger performance, returning 2.08% and 2.02% respectively (both ahead of cash), while longer duration bonds (12+ years) underperformed cash significantly at -1.18%. The Fund's position remains concentrated in the shorter-dated areas of the curve, with holdings focused on the R186 and R2030, both of which outperformed cash. Given the continued attractiveness of government bonds relative to cash over the medium term, we view the sub-10-year portion of the curve as offering the optimal risk/reward opportunity for a cash-cognisant mandate. Consequently, our nominal duration increased marginally by 10bps over the quarter.

Inflation-linked bonds (ILBs) underperformed their nominal counterparts, with the index returning 0.7%, below cash returns. However, our short-dated ILB holdings, concentrated in the I2029, delivered a return of 2.44%. This exceeded cash returns, partly due to higher inflation carry over the next three months. While the subdued inflation outlook may constrain ILB returns in the medium term, real rates remain compelling, particularly if the SARB does become more dovish on monetary policy. Combined with our expected inflation profile, we project the I2029 return at around 9.5%, which remains attractive relative to cash. Though nominal bonds appear more attractive, ILBs serve as important portfolio diversifiers, especially in volatile environments. The Fund therefore maintains an approximately 15% allocation to short-dated ILBs, which decreased significantly following the maturity of our I2025 holdings in January 2025.

Money market opportunities were limited, with NCDs contracting further across the curve, reflecting tight credit market conditions and abundant banking system liquidity. Based on our view of unchanged repo rates, we increased exposure to two-year floating rate NCDs. We also found value in government floating rate notes up to five and a half years in maturity, with spreads exceeding 100bps. The Fund now maintains close to a 2% position in these instruments.

Credit market opportunities remain scarce as spreads continue to compress. Despite finding some small opportunities in the secondary market, our overall credit allocation will likely gradually decrease.

Outlook

We maintain a cautious stance for the year ahead, given continued political volatility and economic uncertainty, both locally and globally, alongside concerns about the central bank's high real rates potentially dampening domestic demand amid exceptionally subdued inflation. While the Fund invests in risk assets that may temporarily underperform cash, we remain focused on valuation and will invest only in instruments offering appropriate risk-adjusted returns. We expect domestic inflation to remain well controlled, averaging 3.5% for 2025. Key risks include the government's commitment to fiscal reform while maintaining growth stimulus.

Given the current Fund yield of 8.93% and its modest duration positioning, we believe it remains on track to deliver its target of cash +1.5% over the medium term.

Portfolio managers
Nishan Maharaj and Mauro Longano
as at 31 March 2025