



## Financial market outlook: October 2025

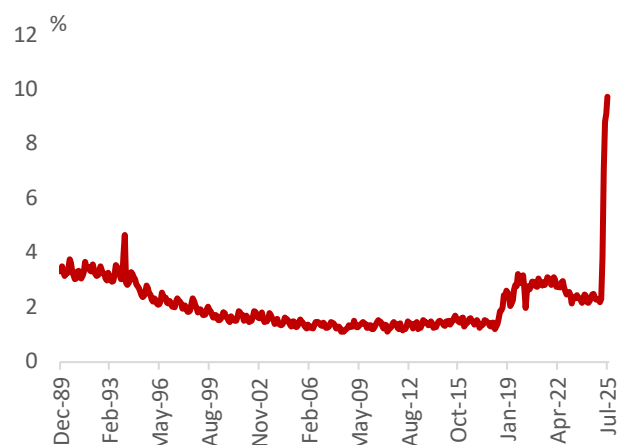
### Key market takeaways

- The combination of anticipated rising inflation, fiscal stimulus and the potential for Federal Reserve (Fed) meddling by the Trump administration to ensure lower policy rates, at the very least can be construed as less negative for the United States (US) equity market than the US bond market, if not outright positive for equities.
- The current low implied volatility levels in both the US equity and bond markets point to some level of complacency among investors. These markets could thus be at risk from any negative surprises when expectations are so sanguine in a very uncertain environment where there are many question marks about the sustainability of the narrow artificial intelligence (AI) equity rally, the magnitude of US rate cuts currently discounted by the market, the outcome of the tariff policy experiment and the durability of Fed independence.
- While South Africa (SA) remains in a falling local interest rate cycle, this continues to provide a positive backdrop for both local equities and vanilla government bonds going forward. Both these asset classes also remain attractively valued within the emerging market (EM) peer group, as well as relative to their own histories.
- SA listed companies have negligible revenue exposure to the US and should thus not experience a notable direct negative impact from the announced 30% tariff increase on SA imports by the US. The SA equity market remains under-owned within Global Emerging Market (GEM) funds – with the SA equity market one of the strongest global equity performers so far in 2025, this could put the overlooked market back onto the radar screens of foreign investors, as has often been the case in the past.
- An expected cyclical rise in local inflation in the remainder of 2025 should lead to widening breakevens in the coming months, supporting SA inflation-linked bonds (ILBs). Local rate cuts have reduced real cash yields from prior peaks, making future returns from cash now appear less compelling compared to particularly SA equities and bonds.
- There has been a positive recent trend in earnings guidance by SA listed property companies. This builds on the improvement in the operating and financial metrics that have been visible in the sector for some time.
- Elevated geopolitical risk and concerns about the security of assets in the global financial system since the onset of the Russia–Ukraine war continue to drive gold demand from central banks and investors, buoying the gold price.
- We still favour SA assets over global counterparts, supported by fundamental and valuation considerations.

## Fundamentals expected to be more negative for global bonds than equities

Prevailing low implied volatilities in the US equity and bond markets seem to indicate that these financial markets have been thankful that the impact of US tariff increases on US growth and inflation have so far been less than expected. However, it is typical that announced tariff changes take time before they are reflected in the economy due to pre-emptive inventory buildups and behaviour adjustments by economic agents. For instance, although it is estimated that the US effective tariff rate based on US President Trump's tariff pronouncements at the time of writing is in the mid-teens, data on the latest actual tariffs collected by US Customs implies a lower effective tariff rate of below 10% (see chart 1).

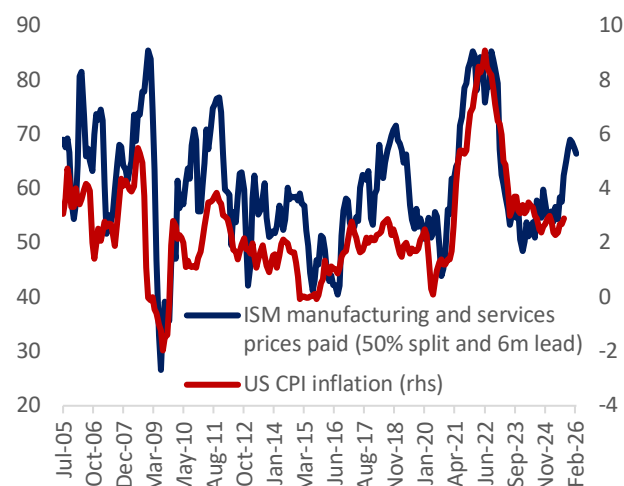
**Chart 1: The actual effective US tariff rate still lags the announced rate**



Source: Nedbank, US International Trade Commission

As the actual effective tariff rate drifts up towards the announced policy rate going forward, there should be more discernable negative impacts on US inflation and economic growth (even considering that there could be a sharing of the total tariff impact between suppliers, importers and the final consumer), with corresponding adverse readthroughs for both US bonds and equities. On inflation, leading indicators from price surveys point to upside inflation risk in the coming months, with unfavourable implications for US bond yields (see chart 2).

**Chart 2: US leading indicators point to upside inflation risk in the coming months**

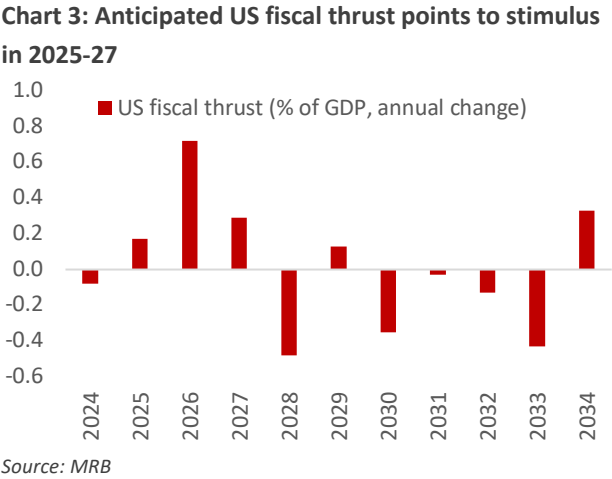


Source: Bloomberg, Iress, Momentum Investments

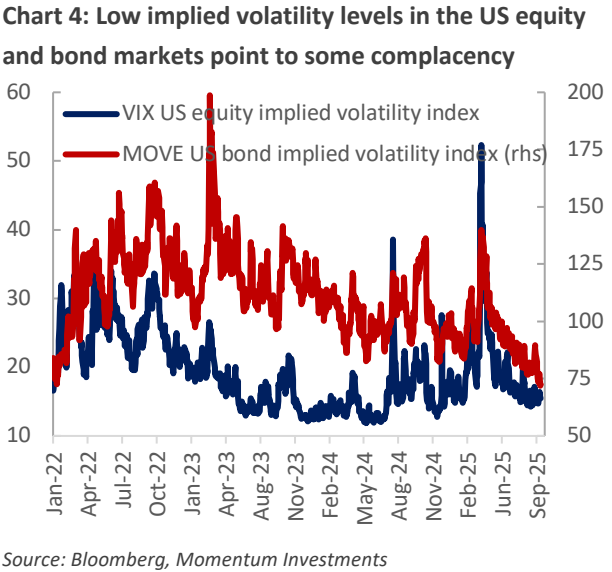
Research from MRB shows that an environment of slowing growth and rising inflation (some variant of stagflation thus) has historically been negative for both US equity and bond returns. Against this backdrop, it may seem surprising that the aggregate US equity market has been so vibrant this year. However, it should be recognised that the growth-negative elements of the Trump policy package (higher tariffs and immigration clampdown) are mainly headwinds for the smaller market capitalisation sectors such as consumer discretionary, retail and health care, while the positive elements (lower taxes and deregulation) are mainly tailwinds for the higher market capitalisation sectors, like technology and financials.

Furthermore, the combination of anticipated rising inflation, fiscal stimulus (see chart 3) and the potential for Fed meddling by the Trump administration to ensure a lower policy rate environment, at the very least can be construed as less negative for the US equity market than the US bond market, if not outright positive for equities. However, this doesn't imply that the US equity market would be totally immune should US bond yields rise meaningfully due to a deteriorating fundamental backdrop of higher inflation, fiscal deterioration or a less independent Fed. In this regard, Morgan Stanley has pointed out in recent research that US equities have

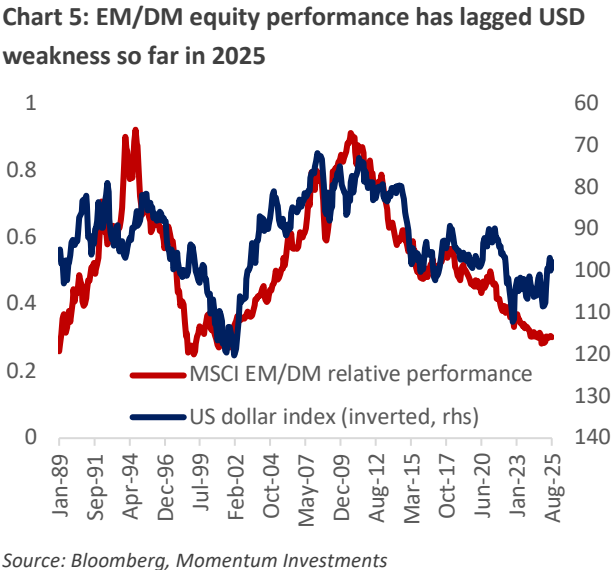
derated each time in 2024-25 whenever 10-year US yields rose above 4.5%, while there is currently a negative correlation between US bond yields and the US equity market.



The current low implied volatility levels in both the US equity and bond markets point to some level of complacency among investors (see chart 4). Markets could thus be at risk from any negative surprises when expectations are so sanguine in a very uncertain environment. Not only are there question marks about the sustainability of the narrow AI equity rally, but also about the magnitude of Fed rate cuts currently discounted by the market, the outcome of the tariff policy experiment and the durability of Fed independence. There was already some indication of the US equity market’s response to elevated expectations during this year’s second quarter corporate earnings results. Research from UBS shows that where companies beat profit expectations in the second quarter, share price rises were half of the historical norm, whereas reported results in line with or below expectations resulted in share price declines of four times the historical precedent. This shows that when markets are already discounting a favourable outcome, there is little scope for disappointment.



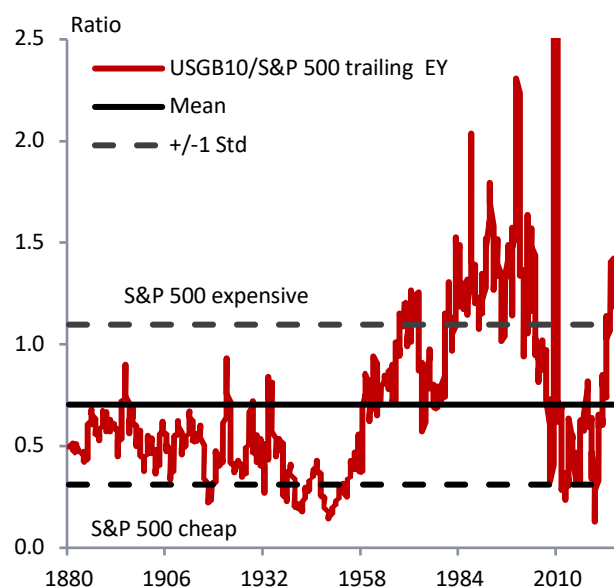
Several fundamental forces are simultaneously conspiring negatively against the outlook for the US dollar. A slowing US economy that is closing the positive economic growth gap with the rest of developed markets (DM), anticipated Fed policy rate cuts in excess of those in other DMs and question marks about the US as a safe-haven investment destination all point to a weak dollar environment going forward. While dollar weakness has historically been associated with an outperformance of emerging markets (EM) over DM equity markets, this has not been the case so far in 2025, pointing to some future catchup potential for EM (see chart 5).



Sovereign bond markets in developed economies outside the US continue to offer materially lower yields relative to their domestic equity market's earnings yields, reinforcing a valuation bias in favour of equities. For instance, the German 10-year government bond yield, at around 2.7%, remains significantly below the German equity market's earnings yield of roughly 5.3%. The disparity is even more pronounced in Japan, where the 10-year bond yield of 1.7% compares with an equity earnings yield of 5.6%.

In contrast, US bonds screen as attractively valued relative to US equities on a historical basis (see chart 6). However, this relative attractiveness could persist if inflationary outcomes or fiscal deterioration were to exceed current market expectations, keeping US bonds undervalued versus equities.

**Chart 6: Fundamental risks could keep US bonds cheap against equities**



Source: Iress, Momentum Investments

Occupancy levels across most US commercial property sub-sectors, excluding Retail, continue to decline,

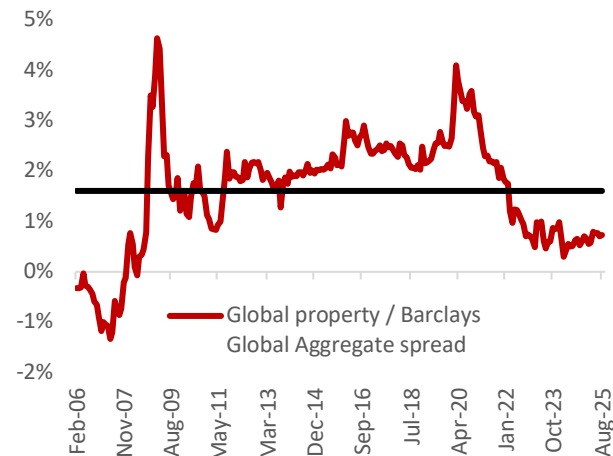
## Fundamental and valuation support for SA equities and nominal bonds

Recent research by UBS shows that SA listed companies have negligible revenue exposure to the US and should thus not experience a notable direct negative impact from the announced 30% tariff increase on SA imports

underscoring that demand has yet to absorb the current supply. At the same time, there is little evidence of a slowdown in new development, despite rising replacement costs that should, in theory, temper supply growth. Importantly, the composition of the global listed property investable universe has shifted significantly over the past decade, with Retail and Office now representing a smaller share, while Data Centres, Telecommunications, and Health Care have become more prominent.

Looking ahead, the potential for rising sovereign bond yields, driven by deteriorating fiscal positions and higher US inflation, represents a key risk to the global listed real estate sector. While global listed property continues to trade at a discount relative to global equities, valuations appear stretched compared to most fixed-income alternatives, including nominal and inflation-linked Treasuries as well as global investment-grade bonds, with yield spreads currently sitting well below their long-term averages (see chart 7).

**Chart 7: Global listed property looks expensive relative to global IG bonds**

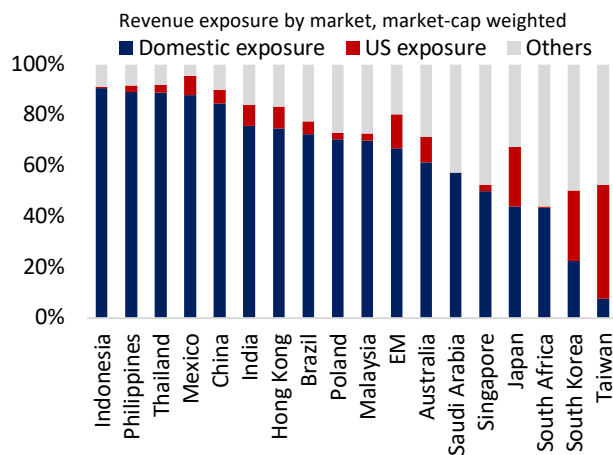


Source: Bloomberg, Momentum Investments

by the US (see chart 8). This is in sharp contrast to the EM heavyweights Taiwan and South Korea that are much more prone to higher US tariffs due to larger direct US revenue exposures by their listed corporates.

This is not to say that there would be zero negative tariff impacts on SA listed corporates, as there may be some adverse indirect effects through the domestic growth driver for those corporates linked to the local economy. However, it should be emphasised that less than half of the aggregate revenue base of the overall SA equity market is generated from the local economy.

**Chart 8: SA equity market has a low direct revenue exposure to the US**

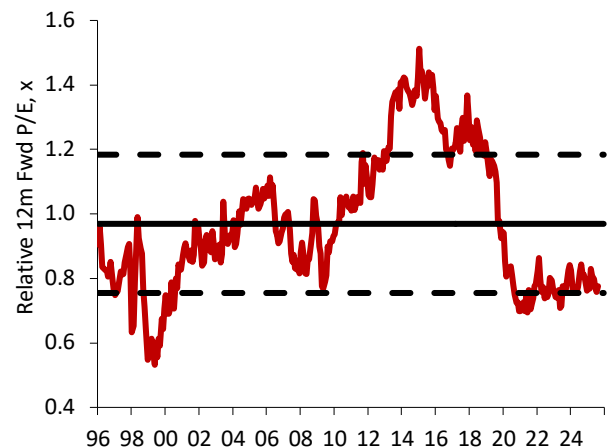


Source: UBS

While SA remains in a falling local interest rate cycle, even if further rate cuts are postponed to 2026, this continues to provide a positive backdrop for both local equities and government bonds. Historically, SA equities outperformed SA bonds in falling rate cycles.

SA equities remain attractively valued within the EM universe, trading at roughly a one standard deviation discount to their historical average relative forward P/E since the onset of Covid (see chart 9). In addition, SA continues to stand out as a superior dividend market, with forward dividend yields currently 27% above the EM average, slightly above its long-term premium of 25%.

**Chart 9: SA's forward P/E discount to EM remains large**



Source: Iress, Momentum Investments

Given SA equities' high-beta characteristics relative to broader EM (see table 1), coupled with their significant valuation discount, we continue to prefer SA equities over the wider EM peer group.

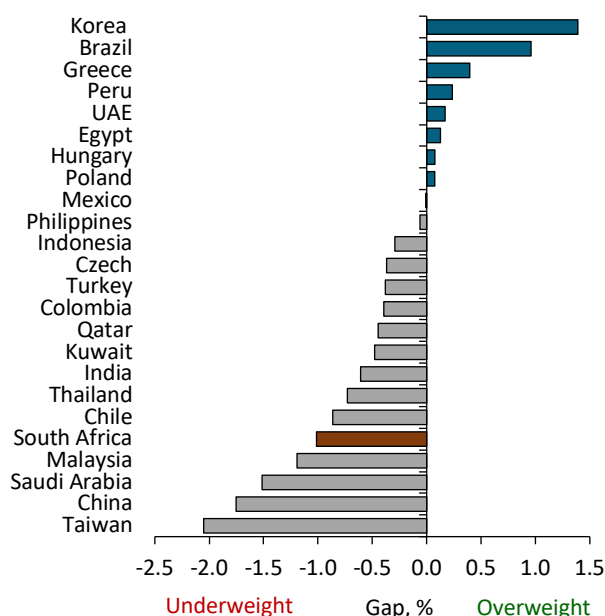
**Table 1: SA equities a high-beta play on EM equities**

	Beta vs. EM	Correlation to EM
China	1.48	80%
South Africa	1.42	75%
Taiwan	1.10	73%
Korea	1.07	74%
Poland	0.98	54%
Colombia	0.91	46%
Chile	0.87	56%
Peru	0.84	49%
Mexico	0.83	53%
Greece	0.81	54%
Brazil	0.72	54%
Indonesia	0.72	50%
Philippines	0.65	51%
Thailand	0.64	52%
Malaysia	0.57	65%
Hungary	0.56	39%
India	0.52	53%
Qatar	0.35	37%
Türkiye	0.31	16%
Saudi Arabia	0.31	32%
Czech Republic	0.28	24%

Source: J.P. Morgan

The SA equity market remains under-owned within GEM funds, currently ranking as the fifth-largest underweight position (see chart 10). A renewed allocation to EM equities, potentially supported by shifting dynamics in a new Trump policy environment and expected dollar weakness, could translate into meaningful flow support for SA equities, whether through a partial closing of the GEM underweight or selective off-benchmark positioning by global investors. This is particularly pertinent after the SA equity market has been one of the strongest global equity performers in 2025, potentially putting the overlooked market back onto the radar screens of foreign investors, as has often been the case in the past.

**Chart 10: GEM fund exposure versus benchmark**



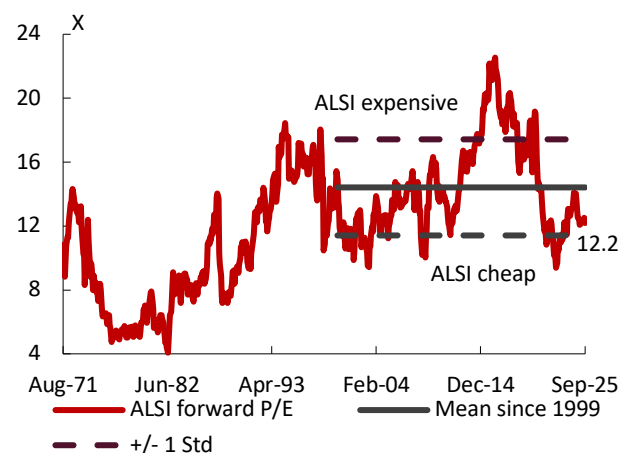
Source: SGB Securities

In addition, domestic structural selling pressure has eased, with local multi-asset funds now largely aligned with their higher foreign allocation limits following the February 2022 increase in Regulation 28's offshore cap to 45%.

Although SA equities have rallied strongly over the past 18 months, concurrent and continual earnings upgrades over the period have kept valuations in the attractive territory. SA equities are still trading below their long-term historical forward P/E average, even on a conservative one-year profit growth assumption of 17%

relative to the current consensus number of around 22% (see chart 11).

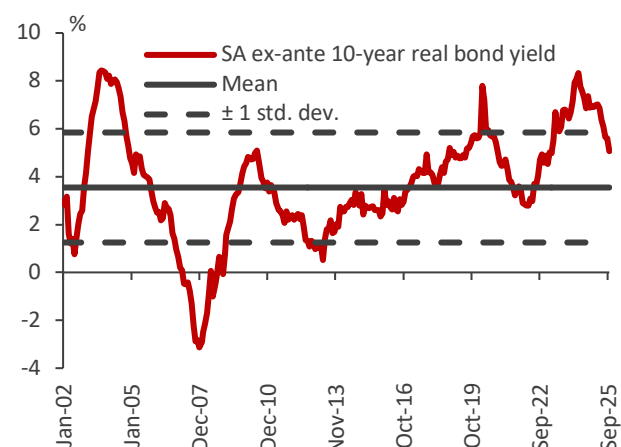
**Chart 11: SA equity market forward P/E**



Source: Iress, Momentum Investments

SA vanilla government bonds continue to offer among the highest real yields globally, surpassed consistently only by Brazil within the EM universe. On a forward-looking basis, the current SA real bond yield of more than 5% is around 0.7 standard deviations above its historical average since the adoption of inflation targeting (see chart 12).

**Chart 12: SA ex-ante 10-year real bond yield**



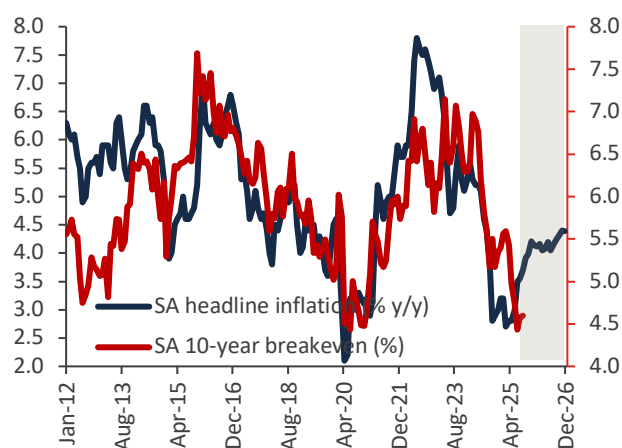
Source: Iress, Momentum Investments

Market expectations that SA's inflation target will be lowered (confirmed by the SARB's acknowledgement at the end of July that 3% is now their *de facto* preferred target), supported a strong rally by SA nominal bonds during May-July 2025, but undermined the performance



of ILBs. However, since then, ILBs have recovered on the realisation that there is likely to be a cyclical rise in local inflation in the remainder of 2025 which should lead to widening breakevens in the coming months (see chart 13).

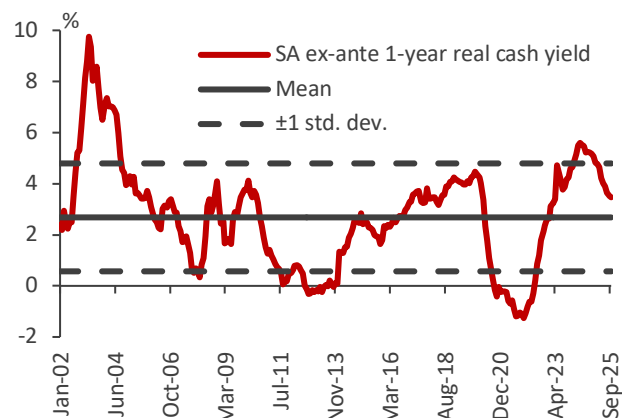
**Chart 13: ILBs should be supported near term by widening breakevens in line with higher inflation**



Source: Iress, Momentum Investments

SA cash continues to offer investors an above-average prospective real yield, underpinned by our expectation that inflation will average around 4% over the coming year (see chart 14). However, as the SARB's rate-cutting cycle since September 2024 and rising inflation have reduced real cash yields from prior peaks, future returns from cash now appear less compelling relative to opportunities in other asset classes, particularly SA equities and nominal bonds.

**Chart 14: Prospective SA real cash yield still above its historical average but declining**

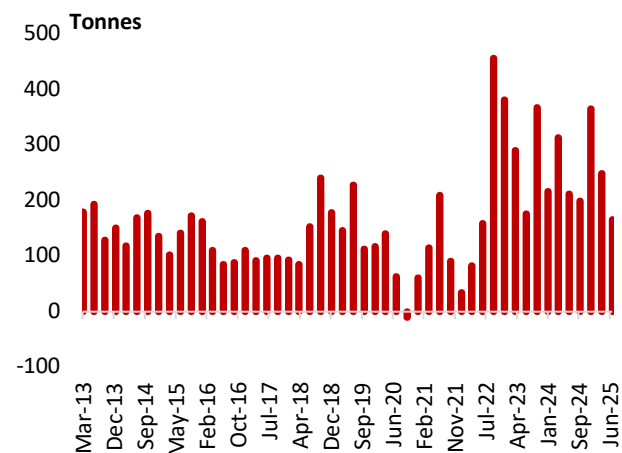


Source: Iress, Momentum Investments

There has been a positive recent trend in earnings guidance by SA listed property companies. This builds on the improvement in the operating and financial metrics that have been visible in the SA listed property sector for some time. Not only are operating costs coming down due to solar investments but the cost of debt is also falling as property companies start to see the benefits of interest rate cuts. As a result, interest cover ratios have improved from historical lows. Net property income growth is the strongest in the Retail sector, followed by the Industrial sector but is still not positive in the Office sector. On the supply side, development activity has been much lower than in the pre-Covid period in both the Office and Retail sectors, while on par in the Industrial sector.

Since the onset of the Russia–Ukraine war in February 2022, EM central bank gold purchases have been the dominant driver of the higher US dollar gold price (see chart 15). Elevated geopolitical risk and concerns about the security of assets in the global financial system, given the precedent of sanctions imposed on Russia, have driven this trend. More recently, heightened uncertainty around US policy in the Trump era has reinforced global central bank and investor caution over concentrated exposure to US dollar assets, further underpinning demand for gold as an alternative asset class.

**Chart 15: Central bank gold buying continuing unabated**

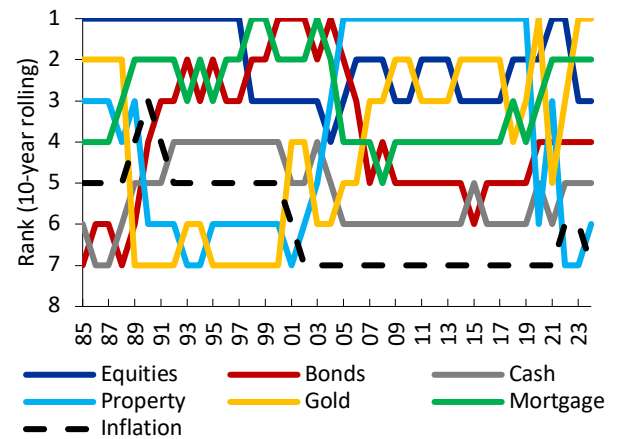


Source: Bloomberg

Despite this, EM central banks still maintain only a modest allocation to gold within their reserves (see table 2). This suggests further potential upside for the gold price if large reserve holders such as Russia, China, India and Türkiye were to increase their gold holdings toward the significantly higher ratios seen in DM.

From a portfolio construction standpoint, allocating to gold via an exchange-traded fund (ETF) enhances diversification due to its low correlation with most other asset classes. If US Treasuries were to lose some of their safe-haven appeal amid questions about the reliability of the US as an investment destination, gold would likely be a direct beneficiary. This would also reduce the correlation between gold and Treasuries, further strengthening its diversification role. Additionally, research from SBG Securities highlights that the rand and gold price has consistently ranked among the strongest-performing domestic asset classes in recent years, albeit aided by persistent rand depreciation (see chart 16).

**Chart 16: Gold has been a recent stellar performer amongst SA asset classes**



Source: SBG Securities

**Table 2: EM central bank gold exposure is still very low relative to DM central banks**

	<u>Tonnes</u>	<u>% of Reserves</u>
United States	8,133	77.8%
Germany	3,350	77.5%
Italy	2,452	74.2%
France	2,437	75.0%
Russia	2,330	36.3%
China	2,299	6.7%
Switzerland	1,040	11.2%
India	880	13.1%
Japan	846	6.8%
Türkiye	635	50.1%
Netherlands	612	68.1%
Poland	515	22.0%
ECB	507	46.1%
Taiwan	424	7.0%
Saudi Arabia	323	6.9%
United Kingdom	310	16.6%
Spain	282	25.4%
Iraq	163	16.8%
Brazil	130	4.0%
South Africa	125	19.4%
Mexico	120	5.1%

Source: World Gold Council



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