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Financial markets outlook: July 2026

Key market takeaways

- Global equity markets have demonstrated notable resilience in 2026, despite geopolitical disruptions such as the escalation of the Iran conflict. The initial sell-off following the conflict was rapidly reversed, largely due to exceptionally strong United States (US) earnings growth and broad-based upward revisions to profit expectations.

- In contrast, global bond markets face structural headwinds. Rising inflation, elevated fiscal deficits, high issuance levels and significant US refinancing risks, with a large portion of debt maturing soon, are contributing to persistently high bond yields. These dynamics remain fundamentally negative for bond returns and undermine their traditional defensive role.

- Importantly, the relationship between equities and bonds has evolved. Rising bond yields are increasingly constraining equity valuations, with thresholds such as US 10-year yields above 4.5% historically associated with multiple compression. As a result, equity markets are becoming more sensitive to interest rate expectations.

- South African (SA) asset classes continue to stand out as offering undeniable value, with valuations remaining depressed relative to both history and emerging market (EM) peers. This creates a favourable risk-reward asymmetry for investors. SA equities are one of the most compelling opportunities in global markets in a post-Iran war environment, in our view, with a combination of attractive valuations, recovering fundamentals and structural positioning supporting a strong investment case going forward.

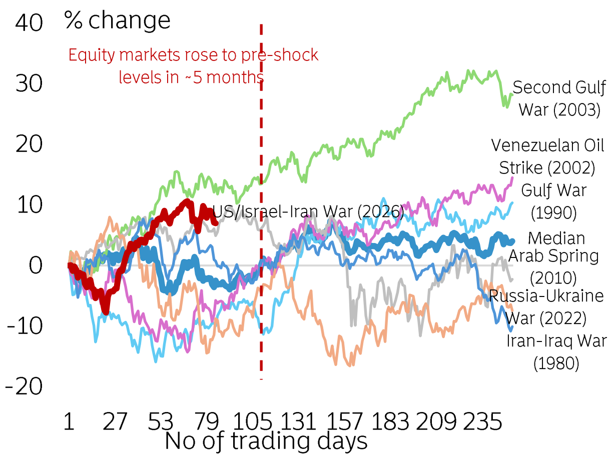
- Fundamental fair-value analysis suggests the potential for capital appreciation from SA nominal bonds, supplementing attractive income returns from the asset class. Conversely, SA inflation-linked bonds (ILBs) should receive only near-term fundamental support from temporary rising inflation due to the war-related spike in energy prices, with nominal bonds preferred beyond the very short term as inflation falls. SA cash, while offering positive real returns, remains less attractive compared to other asset classes. Operational fundamentals have improved significantly in the SA listed property sector, reflected in lower vacancies, positive base rental growth and broadly stable cost-to-income ratios, while the sector should also benefit from expected declining domestic bond yields and attractive valuations.

- Our overarching asset allocation positioning remains unchanged: a clear preference for SA equities, listed property and nominal bonds, complemented by selective exposure to EM equities and diversification assets like gold, while remaining cautious on global fixed income and global property.

Expected fundamentals should continue to favour global equities over bonds

Global equity markets have demonstrated notable resilience in 2026, despite geopolitical disruptions such as the escalation of the Iran conflict. Historically, oil-induced geopolitical shocks tend to cause short-term volatility, but US equity markets typically experience only modest drawdowns before recovering after a few months, provided there is no accompanying recession. Although this pattern has broadly repeated since the start of the Iran war, the US equity market recovery has been notably swifter than historical averages (see chart 1). The initial 8% US equity sell-off following the conflict was rapidly reversed, largely due to upward revisions in US corporate profit expectations.

Chart 1: Historical US equity market performance after oil-induced geopolitical shocks

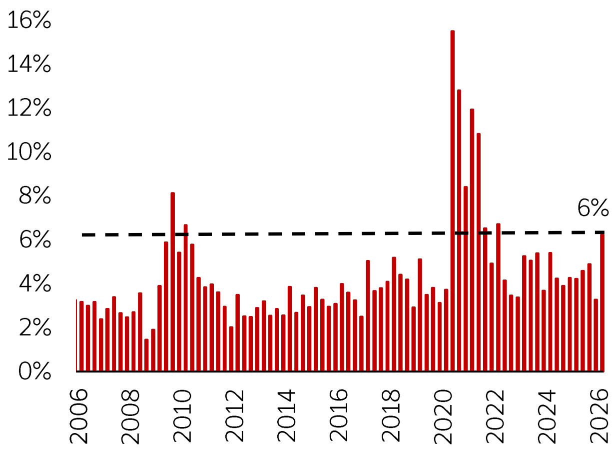


Source: UBS, Iress

A defining market feature so far in 2026 has been the dominance of earnings rather than valuation rerating as the primary driver of positive US equity market returns. Indeed, with profit expectation upgrades outpacing share price appreciation this year, forward multiples have contracted. Moreover, upward revisions across the US equity market have been broad-based and reflect both sector-specific drivers (notably artificial intelligence-related investment) and broader-based improvements across industries, extending beyond large-cap technology companies to include small-cap stocks.

Furthermore, positive earnings surprises have been substantial and widespread. The median US company delivered a positive earnings surprise of around 6% in the first quarter 2026 reporting period – a level comparable in magnitude only to the post-COVID recovery phase (see chart 2). Given that already-elevated expectations typically make such surprises harder to achieve, this underscores the strength of the current US earnings cycle.

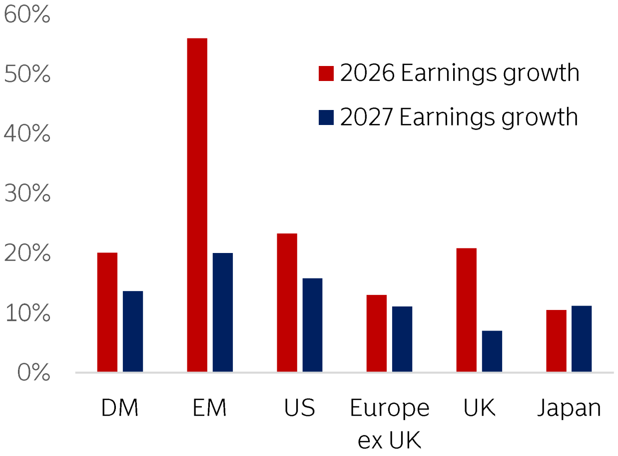
Chart 2: Strong S&P 500 median stock positive profit surprise in 1Q26



Source: Morgan Stanley

Moreover, corporate profit growth is expected to be robust worldwide in 2026-27, not just in the US. Following very high consensus regional earnings growth expected in 2026, profit growth rates in 2027 will naturally be lower from this high base but still anticipated to be above 10% in all regions bar the UK, where consensus nonetheless still expects high-single-digit growth (see chart 3).

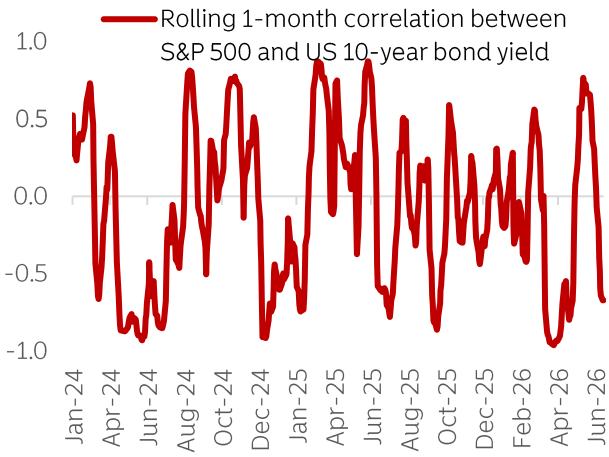
Chart 3: Consensus expectations are for synchronised solid positive regional global profit growth in 2026-27



Source: Factset, Citi

Despite a supportive fundamental environment for global equities, there are some risks. Valuations, particularly in the US, remain elevated, and the sustainability of returns is increasingly dependent on interest rate dynamics. With bond yields rising, the discount rate applied to future cash flows is increasing, placing pressure on equity valuations. This is reflected in the recent negative correlation between US equities and bond yields, indicating that rising yields would be a risk to equity market performance (see chart 4).

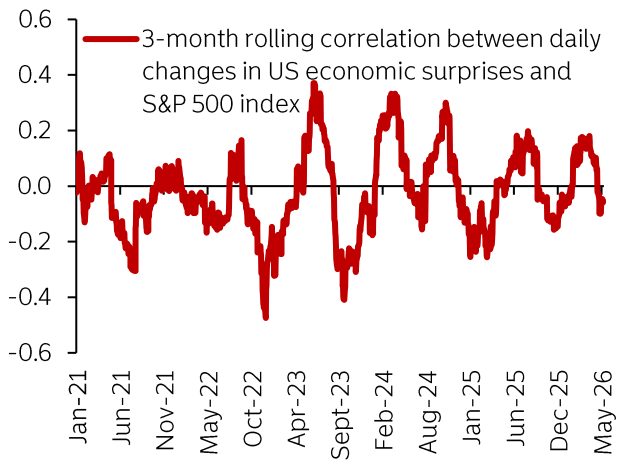
Chart 4: Correlation between US equities and bond yields has turned negative



Source: Iress, Momentum Investments

Research by Morgan Stanley shows that whenever the US 10-year bond yield has risen above 4.5% in the last couple of years, the rating of the US equity market has come under pressure. Furthermore, chart 5 shows the correlation between US economic surprises and the US equity market flipped in recent weeks from positive previously (where growth surprises were still being viewed as profit trend indicators for the equity market) to negative (where growth surprises are now viewed as indicative of future Fed policy direction). In practical terms, strong economic data, often supportive of equities via the profit driver, currently triggers market declines amid expectations of tighter future monetary policy.

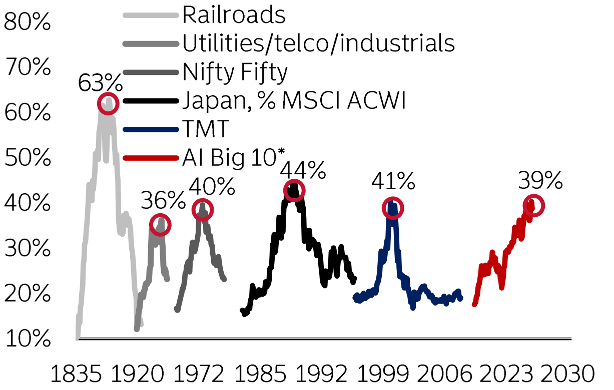
Chart 5: Fed rate policy expectations now driving the US equity market



Source: Bloomberg, Momentum Investments

Bank of America highlights that there are some bubble signs in (parts of) the US equity market that need to be acknowledged from a risk perspective. Firstly, US equity market concentration linked to the size of the AI-themed stocks is now at comparable levels to previous bubble concentration ranges and subsequent to the mega listings of SpaceX in June and Anthropic and OpenAI from late this year (estimated to push the AI market concentration to around 48%) will be surpassed only by the 1840s railroad bubble (see chart 6). Furthermore, Bank of America also shows that the strength of the recent US semiconductor rally at its peak, measured in relation to 200-day moving averages, is comparable in magnitude only to the 1720 French market peak during the Mississippi bubble and the 2000 Nasdaq peak during the dotcom bubble.

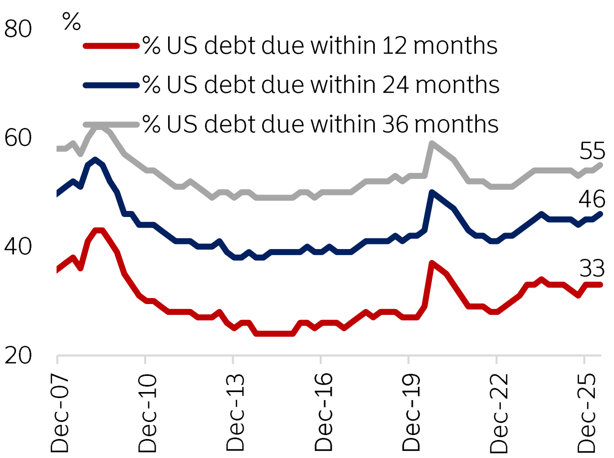
Chart 6: US stock market concentration (% of market cap) at historical bubble peaks



*AI Big 10 = Magnificent 7 + Broadcom + AMD + Micron. Reprinted by permission. Copyright © 2026 Bank of America Corporation ("BAC"). The use of the above in no way implies that BAC or any of its affiliates endorses the views or interpretation or the use of such information or acts as any endorsement of the use of such information. The information is provided "as is" and none of BAC or any of its affiliates warrants the accuracy or completeness of the information.

Global bond markets present a contrasting fundamental picture to equities. While yields are at their highest levels in decades, presenting improved income opportunities, the underlying fundamental bond drivers are largely negative. Fiscal expansion in developed markets (DMs) has led to increased bond issuance, while US refinancing risks are adding to supply pressures, with roughly one-third of US debt approaching maturity in the next year and almost half in the next two years (see chart 7).

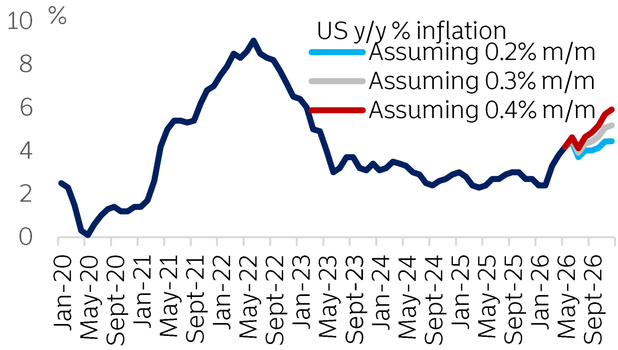
Chart 7: Roll-over risk from approaching debt maturity wall in US



Source: Nedbank

At the same time, inflation remains a key concern for global bond markets due to the war in Iran. Since the start of the conflict, US month/month consumer inflation increases have averaged 0.8%. Assuming a 0.3% average monthly increase for the remainder of this year would push year/year inflation to above 5% by the end of 2026, while an average 0.4% monthly increase would result in close to 6% year/year inflation by year end (see chart 8).

Chart 8: Upward risk for US inflation in rest of 2026



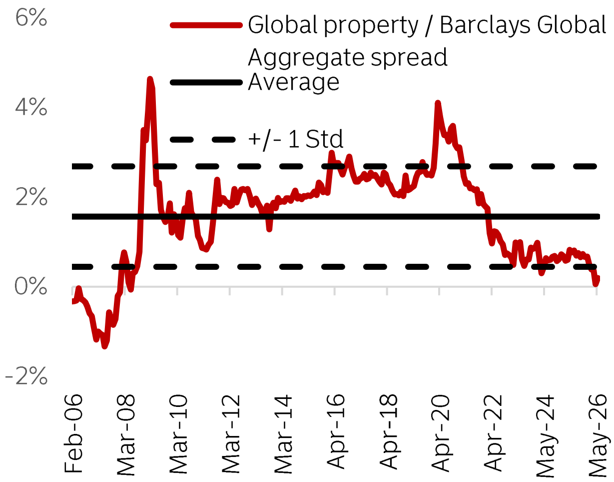
Source: Iress, Momentum Investments

While companies can often pass through higher costs to consumers, bondholders do not benefit from such pricing power. As a result, rising inflation reduces the real value of fixed-income returns, making bonds less attractive on a fundamental basis. These dynamics are fundamentally negative for bond returns and undermine their traditional defensive role. Furthermore, with US equity and bond returns predominantly positively correlated in recent years, US bonds have become less attractive as a consistent diversifying asset within portfolios, particularly in an environment of higher inflation. As such, real assets such as infrastructure, commodities and real estate have become more suitable to fulfil this diversification role.

Overall, the global asset allocation case remains firmly in favour of equities over bonds. However, increasing sensitivity to interest rate movements suggests that equity returns may become more volatile and dependent on macroeconomic conditions going forward.

Global listed property continues to face macro challenges, primarily related to interest rate sensitivity. The risk of rising bond yields would increase financing costs and reduce the relative attractiveness of property income yields compared to fixed-income assets even more from current already expensive levels (see chart 9).

Chart 9: Global listed property remains expensive relative to global investment-grade bonds



Source: Bloomberg, Momentum Investments

Although certain property segments, such as data centres, senior housing and logistics, benefit from strong structural demand and limited supply growth, these positive fundamentals are offset by valuation concerns and macro headwinds. The sector also faces ongoing refinancing risks, particularly in regions with high leverage. As funding costs rise, profitability and dividend sustainability come under pressure. Consequently, while selective opportunities exist, the overall risk-return profile of global listed property remains less attractive relative to other asset classes, in our view.

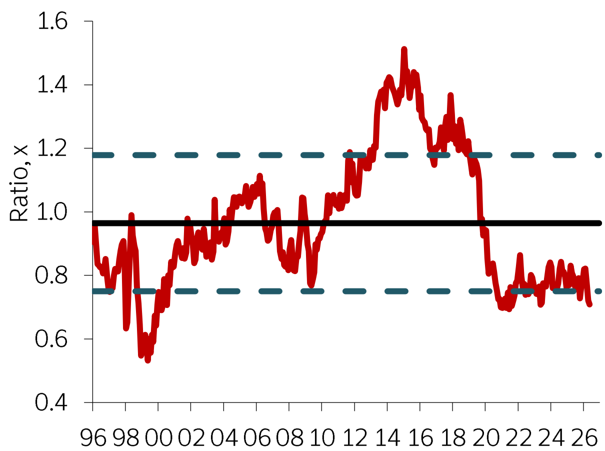
Constructive fundamentals and valuations for SA equities, listed property and nominal bonds

SA asset classes continue to stand out as offering undeniable value, with valuations remaining depressed relative to both history and EM peers. This creates a favourable risk-reward asymmetry for investors.

SA equities are one of the most compelling opportunities in global markets in a post-Iran war environment, in our view. A combination of attractive valuations, recovering fundamentals and structural positioning supports a strong investment case going forward.

Valuations are particularly noteworthy. SA equities trade at a significant discount to both EMs (see chart 10) and even more so DMs, with forward price-to-earnings multiples well below historical averages. Even after adjusting consensus earnings forecasts downward to account for historical positive bias among analysts, the SA equity market remains attractively valued, providing a substantial margin of safety for investors.

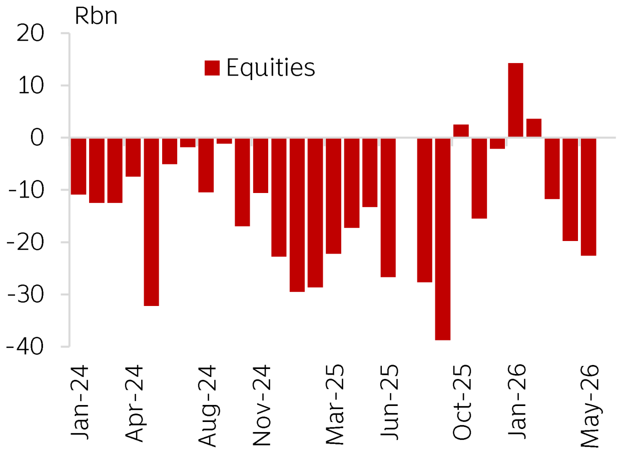
Chart 10: SA's forward P/E discount to EM remains large



Source: SBG Securities

This discount is partly due to persistent underownership by global investors, reflecting historical concerns about poor local growth and policy uncertainty. However, this positioning creates the potential for significant inflows should sentiment improve. Recent investor behaviour highlights this dynamic. Foreign investors, after tentatively buying SA equities in early 2026, withdrew during the escalation of the Iran conflict, becoming consistent net sellers of SA equities again (see chart 11). This underscores the high-beta nature of SA markets to global risk sentiment.

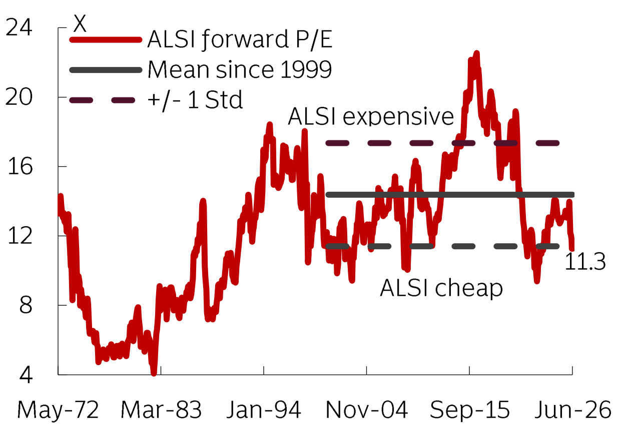
Chart 11: Foreign net purchases of SA equities



Source: Absa

Despite this, the underlying fundamentals remain supportive. SA earnings growth expectations are strong, driven largely by the resources sector, although there is acknowledged downside risk from commodity price volatility. However, even under conservative (below-consensus) profit assumptions, valuation metrics remain attractive, with the SA equity market forward P/E one standard deviation below its long-term average (see chart 12).

Chart 12: SA equity market forward P/E



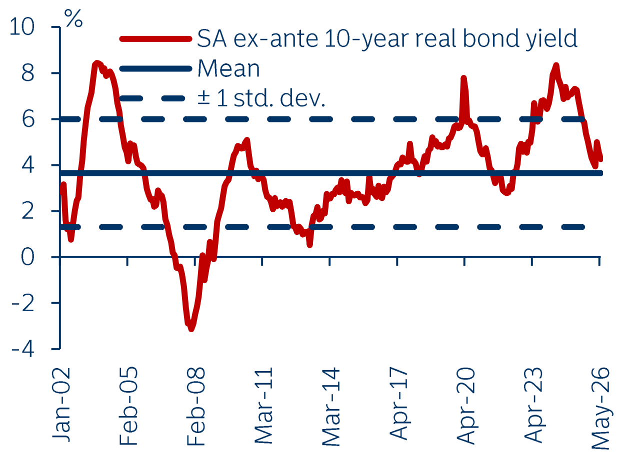
Source: Iress, Momentum Investments

The domestic macroeconomic environment should improve after the war in Iran. Once inflation has peaked and expectations for a resumption of a falling interest rate cycle take hold, both consumer activity and corporate profitability should be buoyed. Separately, progress on structural reforms and improved policy credibility are gradually enhancing the investment climate.

Taken together, these factors point to significant re-rating potential for the SA equity market. Unlike DMs and EMs, where equities are expected to de-rate due to elevated valuations, SA equities are positioned for valuation expansion, providing a powerful driver of future returns.

SA nominal government bonds continue to offer attractive real yields, making them a standout fixed-income opportunity globally. Real yields remain elevated relative to both historical norms (see chart 13) and international peers, reflecting the high risk premia still attached to SA bonds.

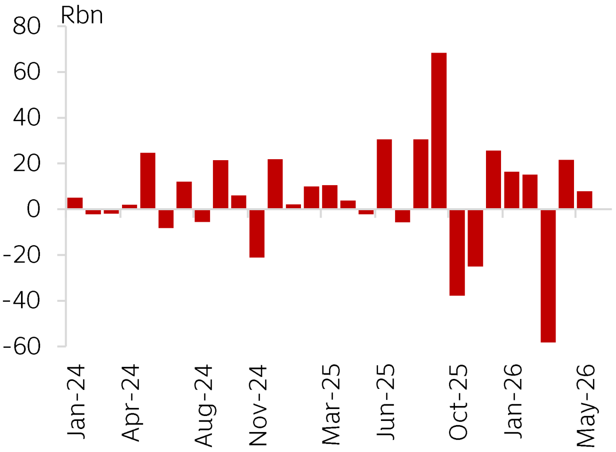
Chart 13: SA ex-ante 10-year real bond yield



Source: Iress, Momentum Investments

Foreign investor behaviour provides additional support for SA bonds. After briefly exiting during the early stages of the Iran conflict, foreign investors have returned to the SA bond market as buyers (see chart 14), attracted by the high yields and improving fiscal credibility. This consistent foreign demand should underpin bond valuations.

Chart 14: Foreign net purchases of SA bonds

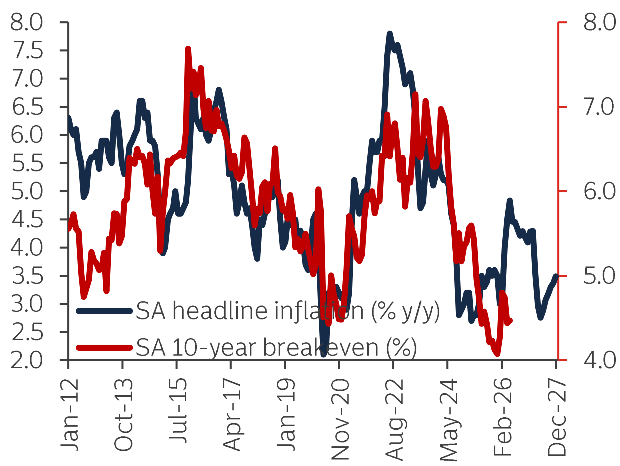


Source: Absa

Fundamental fair-value analysis suggests the potential for capital appreciation from SA nominal bonds. As local inflation first stabilises and then retraces after the Iran war, policy rates should decline again. Bond yields are hence expected to fall, resulting in capital gains supplementing income returns from the asset class.

SA ILBs should receive near-term fundamental support from rising inflation due to the war-related spike in energy prices. However, this support is expected to diminish soon as inflation moderates, reaching the 3% target by the second quarter of 2027 (see chart 15), reducing ILBs' relative attractiveness compared to nominal bonds beyond the very short term.

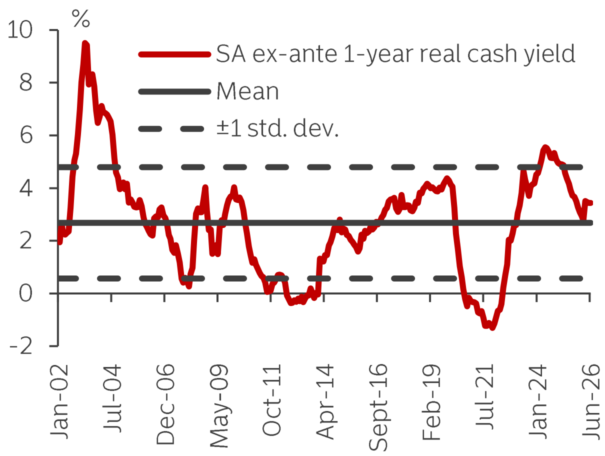
Chart 15: Only very near-term fundamental inflation support for ILBs



Source: Iress, Momentum Investments

SA cash, while offering positive real returns (see chart 16), remains less attractive compared to other asset classes, particularly with equities and bonds offering far superior expected returns from much more depressed valuations.

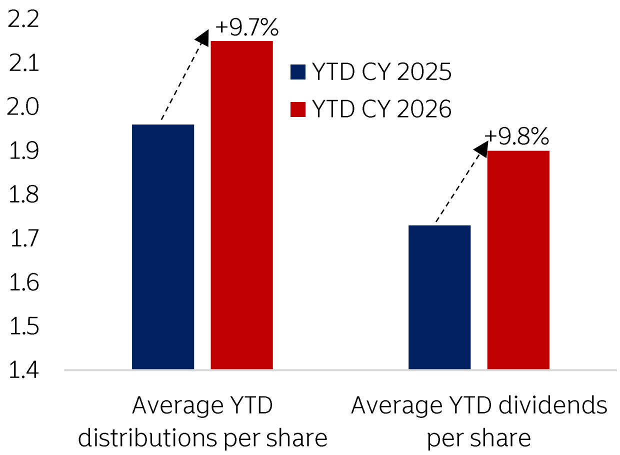
Chart 16: SA ex-ante one-year cash yield



Source: Iress, Momentum Investments

SA listed property companies continue to report strong results, with improving distributions and dividends reflecting firmer operational performance and lower funding costs (see chart 17). Operational fundamentals have improved significantly, supported by lower vacancies, positive base rental growth and broadly stable cost-to-income ratios. The operating recovery is further supported by constrained supply. While retail property development has been muted, meaningful retail store rollouts confirm demand for retail space from dominant grocers.

Chart 17: Strong recent reported SA listed property company results



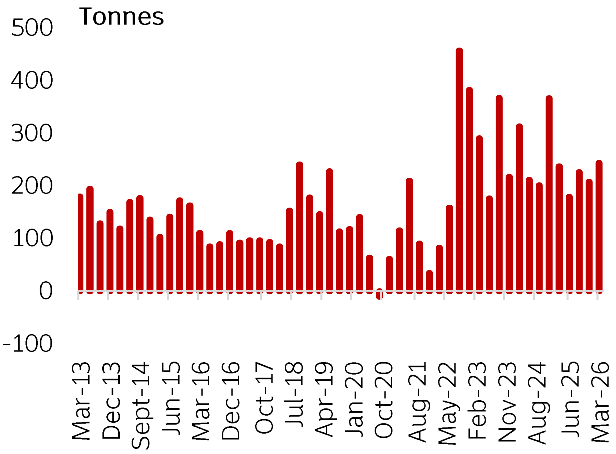
Source: Meago, company results

Importantly, the sector should benefit from our expectation of declining domestic bond yields. As yields fall, property valuations are likely to improve, creating scope for capital appreciation in addition to income returns. Overall, SA listed property offers a compelling combination of improving fundamentals, attractive valuations and supportive macro conditions.

Gold has a valuable role as a portfolio diversifier

Gold remains an important diversifier within portfolios, although its price dynamics are complex and somewhat unpredictable. A key driver of the gold price in recent years has been aggressive central bank buying (see chart 18). This reflects a strategic shift away from the dominance of US dollar assets in central bank reserves since the weaponisation of the US dollar in the global financial system as a response to the 2022 Russian invasion of Ukraine. As a result, strong central bank demand has significantly increased gold prices and weakened traditional relationships with global (US) real bond yields.

Chart 18: Central bank gold buying continuing at historically high levels

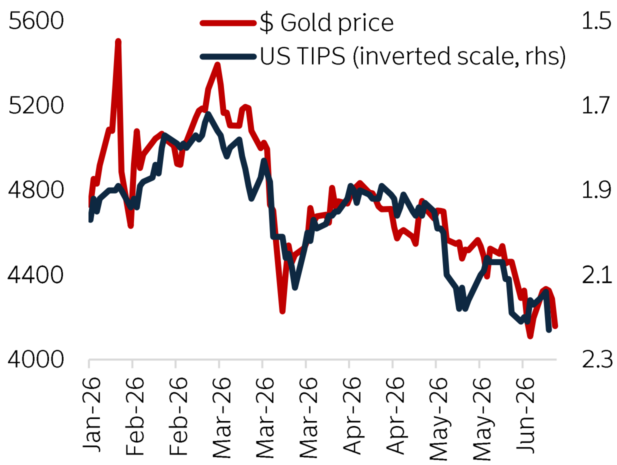


Source: Bloomberg, Momentum Investments

Gold exchange-traded fund (ETF) inflows have accentuated upward gold price moves since 2025. This originated from both investors looking to hedge overexposure to US dollar assets and speculators, with even stablecoin cryptocurrencies becoming large gold buyers in 2025. However, speculators are, by nature, weaker asset holders and were early gold sellers with the advent of the Iran war, putting additional downward pressure on gold prices since then.

The negative traditional relationship between gold and real bond yields has re-emerged in 2026 (see chart 19). Higher US real yields, in line with rising inflation and more negative Fed rate policy expectations due to the impact of the Iran war, have put downward pressure on gold prices, highlighting the asset's sensitivity to interest rate dynamics. Only once expectations flip from tighter to easier Fed policy will lower US real yields become a tailwind for gold prices again.

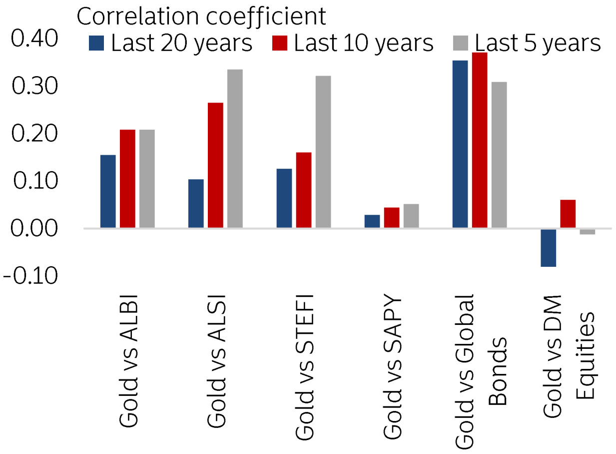
Chart 19: Gold's negative relationship with real bond yields has been re-established in 2026



Source: Iress, Momentum Investments

Despite its volatility, gold continues to play a valuable role as a portfolio diversifier. Its low correlation with traditional asset classes enhances overall portfolio resilience, particularly in periods of heightened uncertainty (see chart 20).

Chart 20: Gold has little correlation with other asset classes



Source: Iress, Bloomberg, Momentum Investments