Finance Invest Insure

# Merchant West SCI Cautious Fund

Quarterly Report
Quarter ending 31 March 2026

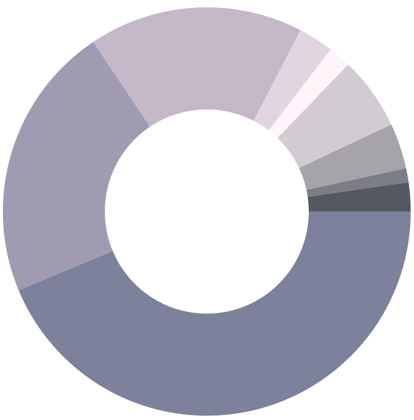
## FUND DETAILS

| Benchmark | ASISA Category | Portfolio Managers | Suitable Investor |
|---|---|---|---|
| ASISA Category Average: SA Multi Asset Low Equity | South African Multi-Asset Low Equity | Merchant West Investments Team | The Merchant West SCI Cautious Fund is suitable for investors seeking capital growth over the long term within the constraints of regulations governing retirement funds. Investors have a cautious to moderate risk profile and are prepared to accept some capital volatility in the short term. Investors are prepared to invest for a minimum period of three years and longer. |

## Top 10 Holdings

| Top 10 Holdings | % |
|---|---|
| Merchant West Global Equity Fund USD Class A | 18.5 |
| RSA Govt Bond R2040 9.0% 31012040 | 12.6 |
| RSA Govt Inflation-Linked Bond R202 3.45% 07122033 | 7.7 |
| RSA Govt Bond R2035 8.875% 28022035 | 7.2 |
| RSA Govt Inflation-Linked Bond I2038 2.25% 31012038 | 6.0 |
| RSA Govt Bond R2032 8.25% 31032032 | 2.6 |
| RSA Govt Bond R213 7.00% 28022031 | 2.5 |
| NewGold ETF | 2.3 |
| RSA Govt Bond R214 6.50% 28022041 | 2.0 |
| RSA Govt Bond R2030 8.00% 31012030 | 2.0 |

## Asset Allocation: Portfolio Date: 31/03/2026



| Asset Allocation | % |
|---|---|
| SA Fixed Income | 43.7 |
| Global Equity | 21.9 |
| SA Equity | 17.0 |
| SA Cash | 2.8 |
| Global Fixed Income | 1.8 |
| SA Property | 5.8 |
| Global Property | 3.6 |
| Global Cash | 1.1 |
| SA Commodities | 2.3 |
| **Total** | **100** |

## Performance

| Performance | Fund % | Benchmark % |
|---|---|---|
| 3 months | -2.5 | -1.0 |
| 1 year | 14.7 | 13.2 |
| 3 years | 12.7 | 11.2 |
| 5 years | 10.8 | 9.6 |
| 10 years | 7.7 | 7.7 |
| Since Inception (January 2012) | 8.2 | 8.4 |

*Annualised after one year*

## Highest and Lowest Annual Returns

| Highest and Lowest Annual Returns | % |
|---|---|
| Highest annual return | 17.5 |
| Lowest annual return | -0.4 |

*By calendar year*

## PERFORMANCE REVIEW

The Fund returned -2.5% in the first quarter of 2026, underperforming the peer group benchmark (ASISA SA Multi-Asset Low Equity) which returned -1.0%.

The Fund's higher weight to equities dragged on returns as the asset class struggled under the uncertainty of the Iran conflict. Fund returns were aided by its overweight exposure to diversified miners and global property, as well as stock selection within listed property. Our fixed income exposure detracted from performance due to the sharp rise in South African long bond yields in March. These rose on the back of inflationary fears due to the oil price spike and global risk retracement as a result of the Iran conflict. In the offshore portion of the Fund, exposure to offshore oil majors aided performance while exposure to select global technology counters detracted from performance.

## MANAGEMENT ACTIONS

Over the quarter we initiated a new position in Clicks. We have admired the business over the years, but the valuation provided a stumbling block to initiate a position. Clicks is a high-quality business with exceptionally high returns on capital and free cash conversion. While the business faces headwinds from Dischem's renewed loyalty strategy, we are confident in Clicks' management team to navigate the environment.

## MARKET OVERVIEW

Global equity markets began the year on a cautiously optimistic note despite questions around AI disruption and elevated valuations before the joint US-Israeli military campaign against Iran, launched on 28 February, transformed the investment landscape. Iran's subsequent closure of the Strait of Hormuz – though which roughly 20% of global oil and a fifth of the world's LNG is transported – triggered the largest supply disruption in modern oil market history. Brent crude surged from the mid-$60s to above US $110 per barrel by late March, injecting acute stagflationary risk into an already uncertain macro environment.

Global equities declined broadly, with the MSCI World Index returning -3.6% in US dollar terms (-1.0% in rand) for the quarter. The S&P 500 fell 4.3%, led lower by mega-cap technology stocks (-7.0% for the Nasdaq Composite Index) that were already under pressure from AI disruption concerns. A sharp rotation from growth to value defined the period, with dividend-yielding, cash flow-secure businesses strongly outperforming. Energy (MSCI World Energy: +36.9%) was the standout sector globally, while the technology, consumer discretionary and growth-oriented sectors bore the brunt of the sell-off.

Emerging markets entered the quarter with positive momentum, supported by AI-related enthusiasm in Taiwan and Korea and ongoing policy stimulus in China. However, Asia's outsized dependence on Middle Eastern energy – over 80% of oil and gas through the Strait of Hormuz is destined for Asian markets – created acute vulnerability in emerging markets with the MSCI Emerging Markets Index shedding 13.1% in March in US dollars (-7.0% in rand). The steep drop was cushioned by the solid gains seen in January (+8.9%) and February (+5.5%), resulting in a negative return of just 0.2% for the quarter, in US dollar terms. Emerging Markets ex-China (+3.2% in USD) significantly outperformed, while the MSCI China Index fell -8.3% in HKD terms (-6.5% in rand) as the energy shock compounded concerns about China's dependence on imported hydrocarbons.

The US economy entered 2026 with moderate momentum. GDP growth estimates for Q1 were revised down from around 3.0% at the start of the year to approximately 2.0% by quarter-end, as the energy shock weighed on activity. The labour market showed signs of cooling as the unemployment rate rose modestly to 4.4%. Consumer spending continued, supported by the wealth effect from strong 2025 equity returns and solid wage growth, though with less vigour as fuel costs climbed.

Inflation, which had been moving steadily towards the Fed's 2% target, saw renewed upside risk. CPI ran at 2.4% year-on-year in both January and February, with core CPI holding at 2.5%. However, the oil shock threatened to push these readings higher in the coming months. Against this backdrop, the Federal Reserve held rates steady at 3.50–3.75% at both its January and March meetings, adopting a "wait and see" posture after delivering three consecutive 25 basis point cuts in late 2025. Market expectations for further rate cuts were significantly scaled back, with 10-year US Treasury yields climbing to over 4.3% at quarter end, after dipping to below 4% before the Iran conflict started.

In Europe, the first two months of the quarter saw a continuation of the European equity rally that had been building since Germany's historic fiscal pivot in early 2025. The €500 billion infrastructure fund, exemption of defence spending from the constitutional debt brake, and broader European rearmament spending continued to support sentiment, particularly for industrials, defence and materials stocks. However, the Iran conflict and European gas price spike rattled markets in March. The MSCI Europe ex-UK Index fell by 2.4% in euro terms (-1.4% in rand) for the quarter as elevated energy costs revived concerns about the region's growth outlook. The ECB left rates unchanged at its March meeting but signalled the possibility of hikes, with updated staff projections showing headline inflation reaching 3.1% year-on-year in Q2 2026 even before accounting for the peak in energy prices.

While the UK equity market (MSCI UK: -5.9% in GBP) did not escape the route in March, it managed to produce a solid first quarter gain of 4.1% in British pounds (+4.9% in rand). This performance was primarily driven by attractive valuations, a rotation into value stocks away from high-priced US tech, and robust earnings from traditional, defensive-style sectors like banking, mining, and defence. Annual inflation in the UK came in at 3.0% in February 2026. The Bank of England kept interest rates unchanged at 3.75% after four 25-basis points reductions last year. Higher energy prices due to the Middle East conflict are expected to push CPI to between 3% and 3.5% over the next few quarters, though a slowdown in economic activity from rising costs could limit second-round effects.

Japan's acute vulnerability to the Hormuz closure – with approximately 70% of its oil imports transiting the strait – weighed heavily on sentiment in March. However, the MSCI Japan Index still managed to close the quarter up 2.9% in yen terms (+3.8% in rand), supported by yen weakness, governance reforms, and an improving earnings trajectory. The Bank of Japan left the door open to near-term rate hikes at its March meeting, indicating greater concern about upside inflation risks than downside growth risks from the energy shock.

Global bond markets faced a tug of war between rising inflation expectations (pushing yields higher) and slowing growth concerns (pulling yields lower). The inflation impulse from surging oil prices won out in the short term, with yields rising across most markets. The Bloomberg Global Aggregate Bond Index returned -1.1% in USD for the quarter. The US dollar continued to regain some ground against the major currencies over the quarter (US Dollar Index +1.7%), benefitting from safe haven flows and the repricing of rate cut expectations following the oil shock.

After a strong start to the year, the global listed real estate sector (GPR 250 REIT Index) declined by 7.8% in March to end the quarter marginally in the red (net Total Return in USD -0.04%) as higher bond yields and uncertainty about the global economy affected sentiment negatively.

South Africa entered 2026 with improving economic fundamentals: inflation had moderated significantly, reaching the SARB's 3% target by February; the economy had expanded for four consecutive quarters – the longest unbroken growth phase since 2018; and the rand had appreciated over 13% against the dollar through 2025. Eskom's improved performance and an S&P credit rating upgrade in November 2025 had bolstered investor confidence.

The SARB held the repo rate at 6.75% at both its January and March meetings. The January hold was not unanimous (four members voted to hold, two preferred a cut), reflecting the benign inflation backdrop and scope for further easing. However, the Iran conflict fundamentally altered the monetary policy calculus. At the March meeting, the decision was unanimous to hold, with the SARB raising its 2026 inflation forecast to 3.7% (from 3.3%) and projecting fuel inflation exceeding 18% in Q2. The central bank now projects only one rate cut in 2026, down from two previously, and presented adverse scenarios where inflation rises above 5% under a prolonged conflict.

Governor Kganyago noted that before the war, conditions had been favourable for inflation to settle around the 3% target quickly, but the negative shock would delay that process. The Eskom tariff hike of 8.76% for direct customers, effective 1 April, added a further domestic inflation headwind.

The FTSE/JSE All Bond Index declined -3.4% for the quarter, with March representing the second-worst month in the Index's 25-year history at -6.8%. South Africa's 10-year government bond yield spiked 120 basis points to 9.3% during March. The bond sell-off was exacerbated by the largest foreign outflow from SA's bond market in at least six years, as global investors reduced risk in the face of the Iran conflict, and took profits after a very strong performance from SA bonds over the last two years. Inflation-linked bonds proved slightly more resilient at -1.1% for the quarter, reflecting their implicit inflation protection in a potential rising price environment.

The rand was the worst-performing major currency in March, including amongst emerging markets, falling 5.9% against the US dollar over the month as investors fled to the perceived safety of the dollar. For the quarter, the rand depreciated 2.2% against the dollar, erasing its gains from earlier in the year.

The FTSE/JSE All Share Index returned -0.6% in ZAR for Q1 2026, a number that masks significant intra-quarter volatility. Following an incredibly strong 2025 and a strong start to 2026, the Index was upended in March, falling 10.5% in the month and narrowly avoiding its deepest monthly drawdown since the global financial crisis.

Precious metal miners, the largest driver of Index returns in 2025, were the largest detractors in March, with gold miners falling 18% and platinum miners 25% month-on-month, contributing more than six percentage points to the JSE's March drawdown as precious metals prices corrected sharply. The pain was broad-based as SA economy centric equities, including banking stocks, fell 10% in March, erasing year-to-date gains, leaving the group down 1% for the quarter. The JSE Financials Index returned -0.2% for the quarter, SA Listed Property fell -4.9%, and the All Share Industrials Index declined -8.4%, with index heavyweights Naspers and Prosus falling 22% and 25% respectively over the quarter.

Despite March weakness the Resources Index gained 8.1% for the quarter – buoyed by the oil price surge and industrial metals, as well as strength in gold and platinum stocks before the March sell off.

## PORTFOLIO STRATEGY

The Fund's objective is to outperform the average fund in its category (SA Multi-Asset Low Equity) over a full market cycle (trough to trough or peak to peak). The Fund seeks to achieve its objective by applying long-term asset allocation and stock selection views across domestic and global markets.

The major market mover in the first quarter of 2026 was the joint US-Israeli military campaign against Iran and the subsequent closure of the Strait of Hormuz. This triggered the most significant disruption to global energy markets since the 1970s oil embargo, with crude prices nearly doubling in a matter of weeks, injecting acute stagflationary risk into an economic backdrop already contending with shifting trade policies.

At such moments, the temptation is to make large, geopolitically driven directional bets – to position entirely for a prolonged conflict, or conversely, to assume a swift resolution. History suggests neither approach serves long-term investors well. Markets tend to be myopic and overreact to unexpected political or policy events, only to snap back quickly after the headline news has been digested. Such overreactions frequently create opportunities to acquire robust businesses at attractive valuations. Maintaining valuation discipline is critical, especially in the current market environment, as competitive and structural dynamics are shifting quickly. We remain vigilant and are prepared to act counter-cyclically, investing when valuations are compelling, where this is aligned with the objective of generating attractive, risk-adjusted long-term returns. Importantly, we insist on conservative balance sheets across the portfolio. We avoid businesses where the debt structure could impair the equity value in a downturn.

We look to allocate a relatively full equity weight through the cycle to benefit from the asset class's attractive long-term return generation potential. Other asset classes (such bonds, property, gold, or cash) that possess attractive uncorrelated characteristics are used to manage downside risk and optimise risk-adjusted returns. Within asset classes, we look for securities that possess attractive valuations attractive in relation to their safety and growth attributes. Within equities our preference remains for strong franchises, able to take control of their own destiny and adapt to changes while creating value, even in challenging environments. We look for pricing power in the businesses we own as it provides valuable protection against stagflationary risks.

In South Africa GDP growth is gradually improving off a low base, as logistics and energy bottlenecks ease. Early signals of reform in certain sectors, such as rail, bode well for future growth prospects. Exiting the FATF grey list and S&P upgrading South Africa's foreign currency sovereign rating with a positive outlook (the first upgrade in nearly two decades) are encouraging moves that build confidence. The US Supreme Court's striking down of Trump's tariff regime helps ease pressure on South African exports, although policy volatility remains. Inflation is at its 3% target, although upside risks due to the oil price spike are holding back rate cuts. The significant strength in precious metals prices over the last few years is providing a boost to government finances and seems to be trickling down to the real economy. Unfortunately, the GNU is fragile, and a breakup or departure of the official opposition would be undecidedly negative and is still a risk at this stage. Furthermore, uncertainty on the global front, especially relating to the Iran conflict and its knock-on effects, will continue to have a direct impact on the local economy and financial markets.
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Balancing the factors above, taking a long-term view, and considering the undemanding valuations and depressed earnings of SA Inc. equities, we continue to hold a meaningful allocation to SA economy centric securities. Little positivity is priced into most of these equities, which we believe provides an attractive opportunity to benefit from the ongoing, albeit gradual, improvement in the direction of the country. Puzzlingly, the reduction in the South African 10-year bond yield, from 10.3% at the end of 2024 to 9.3% at the end of the last quarter (after a large spike in March), as well as rand strength over the last year, seems to have had little to no positive effect on the valuation of SA Inc. stocks. Counterintuitively, most of these stocks have in fact derated, despite the long bond yield being the largest component of their cost of capital. We believe it is only a matter of time before the collective rating of SA Inc. stocks adjusts to this lower cost of capital and re-rates upwards.

Given the various downside and upside risks present we are careful to construct the portfolio to achieve sensible diversification. Our approach stives to enable the Fund to benefit from long-term structural growth drivers, while remaining resilient through varied economic and geopolitical conditions. We are monitoring the investment landscape across domestic and globally listed securities for the opportunities that present themselves during these uncertain

**Merchant West Investments Team**
*Portfolio Manager*