INTUITION

5 DECEMBER 2025

Outlook for 2026: the road ahead

A casual discussion over lunch a few weeks back turned into a music quiz as we debated the outlook for 2026. Was it a case of "The Road to Hell" by Chris Rea, "The Road to Nowhere" by Talking Heads, or could we justify the "Road to Heaven" by Five for Fighting? In the end, we would be happy to settle on "The Bright Side of the Road" by Van Morrison as an indication of our thoughts regarding the prospects for local investments in 2026. There is no doubt that conditions have improved since the middle of the year, underscored by the positive news contained in the Medium-Term Budget. Coupled with the official announcement from National Treasury that we are moving to a new inflation target, we believe the outlook for 2026 is the brightest it's been in years. This article summarises our recent Insight seminar.

SPEED READ

- **When measured in local currency, SA has been one of the best performing markets this year, outperforming its US, UK, and European peers. Much of this performance though, has come from resurgent gold and platinum sectors.**
- **Looking ahead, we continue to see precious metals prices being underpinned by political uncertainty and softening goals towards climate change. In addition, despite uncertainty, we expect agriculture to have another solid year.**
- **The Medium-Term Budget was positive – it signalled a peak in debt, an improvement in interest costs, and a reprioritisation away from consumption towards infrastructure.**
- **Confirmation from National Treasury on the move to a lower inflation target was the final cherry on top. This is a positive, once-off change that should result in a step change lower in SA interest rates, and consequently, a structural rerating of local investments.**
- **If inflation targeting is successfully implemented, equities, bonds and property will be the winners. Markets have already priced some of this in, but there is more to come. Cash will be the loser.**

Michael Porter

Few would have predicted that SA equities would be amongst the best performing equities globally this year. Yet, at the time of writing, the All Share Index had gained 37% on a total return basis, despite the plethora of negative headlines that we read every day. Unfortunately, this performance has not been widespread. It is largely due to a surge of almost 120% in the mining index, itself driven by the gold and platinum sectors, and a contribution from selected industrials like Naspers and the telecommunications stocks. The rest of the market has been lacklustre – a better reflection of the tougher operating environment in the country.

After such a stellar year, it always raises the question of whether this is firstly, sustainable, and secondly, repeatable? Mining, and forecasting commodity prices, are notoriously prone to error, but we take heart from the fact that the world is undergoing a political shift. Old alliances and established methods are being challenged, especially when it comes to national sovereignty. Central banks globally are actively diversifying their foreign reserves away from Dollars and into alternatives, one of which is gold. This is due to shifting political alliances and the perception that the US is no longer the stable, reliable, and trustworthy partner it once was. We are hesitant to predict gold prices at $6,000 or $7,000 per ounce like some commentators, but even prices stable at current levels of $4,000 would imply continued benefits for SA – in tax revenue, positive terms of trade, and a stable currency.

Equally, much has been written about US tariffs and the impact on SA agriculture. Yet despite all the doom and gloom, SA citrus exports grew 22% this year to a new record of over 3 million tons. Equally encouraging, spring rains have been widespread (and I know some will complain it's too soggy). At this stage, the maize crop forecast for 2026 is near record levels, whilst sentiment across the farming community remains positive.

The above paragraphs are important. Whilst the primary sector (mining and agriculture) is not a large proportion of our economy, it can have a disproportionate impact on GDP given its volatility. Our analysis suggests that these sectors should contribute positively to GDP in 2026, rather than detracting from it.

Let us now turn our attention to the Medium-Term Budget. Willie covered the key aspects of the Budget in his article a few weeks ago, but this was the turning point in SA's fiscal outlook that markets have been waiting (and hoping for) for years. Thanks to a R20 billion revenue overrun and good cost control, SA will record a primary surplus (revenue less expenditure before interest costs) for the third year in a row. Consequently, debt as a percentage of GDP should peak this year, and interest payments as a percentage of revenue will also peak this year and fall steadily over the forecast period. To back this up, Treasury has reduced the amount it borrows weekly from R4 billion to R3.5 billion, and further benefit will accrue to government from the substantial rally in local bond yields.

INTEREST COSTS AS % OF REVENUE

Thanks to a combination of improving revenue collection and reduced bond issuance, interest costs as a percentage of revenue will peak this year and fall steadily thereafter. This is a major turning point for our long-term fiscal sustainability.

While the improvement in fiscal metrics was the key focus of the Budget, the announcement that Government is achieving cost savings through various programs was equally welcome. Importantly, these cost savings are being reinvested back into infrastructure, not consumption, a first for many years. The market was also encouraged by the fact that spending on infrastructure is earmarked as an enabler for future private participation. For example, almost R9 billion has been earmarked for Transnet, but these funds will go to preparing key rail lines for private participation in 2026 and beyond. That is sensible spending and is providing the assurance to the private sector

The government has managed to surprise the markets with a concerted effort to achieve cost savings and will, in fact, achieve a primary budget surplus.

that government is committed to the reform process.

The final highlight of the Budget was the endorsement of the new inflation target. Markets had been worried that a rift was developing between the Reserve Bank and National Treasury over the move to a lower target. That has been dispelled. Whilst there is a short-term negative impact on debt ratios from a lower target (due to a lowering of nominal growth assumptions), this is more than outweighed by the longer-term benefits of structurally lower inflation and interest rates – which in itself will save government a significant amount on interest payments should the new target be achieved.

The rest of our Insight presentation dealt in more detail with the structural once-off opportunity for investors of moving to a lower inflation target. Inflation targeting was first introduced to SA in 2001, when we implemented the current target of 4.5% with a tolerance band of between 3% - 6%. Despite a choppy start in the first decade of the century due to strong growth and rampant commodity prices (thanks to China's rapid growth), inflation has settled into a far more predictable range, only really moving outside of this target recently in line with the global inflationary spike post the Covid pandemic. Importantly, the stability in inflation led to a structural decline in local interest rates. If history is a guide and we assume that the Reserve Bank targets a 2% real interest rate, it implies that interest rates should fall by 2% permanently over the next few years – and remain structurally lower into the future.

This has enormous implications for investors. There is a very clear relationship between lower inflation and market valuations. The lower inflation, the higher valuations tend to be.

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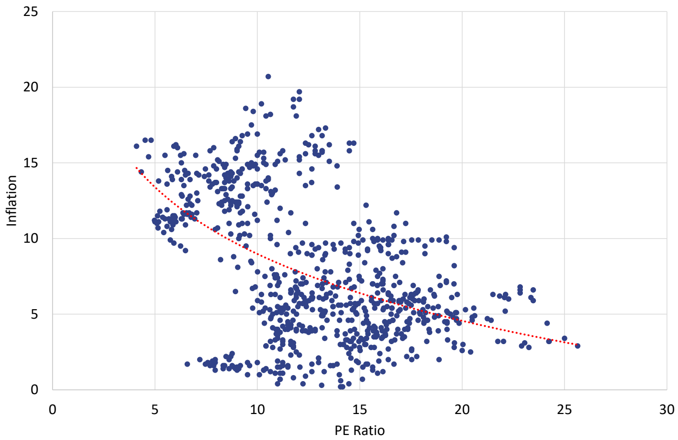
This makes intuitive sense. Lower inflation implies lower interest rates. However, interest rates are a key variable in the calculation of the fair value of an investment. As interest rates go lower, valuations go higher. This relationship is highlighted in the chart below. Interestingly, we did the same analysis for the US market, and the outcome was exactly the same.

RELATIONSHIP BETWEEN INFLATION & VALUATIONS



There is a clear inverse relationship between inflation and market valuations. As inflation trends lower, so too do interest rates, which in turn results in higher valuations.

Our presentation went through the mechanics of a rerating and the potential for outsized returns therefrom. We used our old favourite, Standard Bank, as an illustration. Over the past five years, Standard Bank has grown its earnings and dividends at an annual rate of 8.8% and 8.7%, respectively. Based on current consensus forecasts, earnings and dividends are forecast to grow by 9.9% and 9.3%, respectively, over the next 3 years.

Using the current price and based on the current PE ratio of 9.6x, the table below highlights the potential return from Standard Bank should the earnings growth be delivered. The table shows the change in return should the valuation move from the current level of 9.6x to a slightly higher level of either 10.5x or 12x. It is worth noting that the change in return is due solely to an improved valuation – the result of lower inflation and lower interest rates. It makes no allowance for the fact that GDP growth would also accelerate, thereby driving higher earnings growth, which would create a virtuous cycle and even greater returns.

STANDARD BANK: POTENTIAL RETURNS

Metric:	Current	Average	Improving
PE Ratio	9.61	10.50	12.00
Future Price	34,298	37,475	42,828
Dividends	5,462	5,462	5,462
Return (incl Div)	47%	58%	78%

A successful move to a lower inflation target holds enormous potential benefit for equity investors, as valuations move permanently higher.

The road is winding but SA may be going in the right direction.

In summary, the move to a lower inflation target is a structural, once-off opportunity for local investors. Markets have already started to discount some of this good news – bonds and listed property, in particular, have rallied hard. There is more to come, especially from equities, as this new regime is achieved over the next three years. Investors should understand that opportunities like this are rare and only come along a few times in one investment lifecycle. Equities, bonds, and property are the winners. Cash investments will be the loser as interest rates steadily decline. Being too cautious could be a very costly mistake.

Whilst SA still has a long road to travel to regain its former glory, one cannot help but feel that things are starting to move in the right direction. S&P upgraded our sovereign credit rating after the Budget – the first time they have upgraded us since 2005.

Yes, we are still below investment grade, but momentum is moving in the right direction. We have been removed from the grey-list, and GDP growth next year will be stronger than this year. There is so much work still to be done, but don't wait for the headlines to improve before you act. By then it will be far too late.

Another year has come and gone, a year that has thrown up its fair share of surprises. Please join us for our year end seminar which will see us dusting off the crystal ball and looking into 2026 for clues as to what the new year might hold."

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CONTACT DETAILS:

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Topic: Outlook for 2026

Natal Midlands

Date:	Thurs, 4th of December, 2025
Venue:	Christ Church Howick, 23 Mare Street, Howick
Morning Time:	10am for 10.30am
Evening Time:	5.30pm for 6pm

Johannesburg

Date:	Thurs, 27th of November, 2025
Venue:	Rosebank Union Church, Cnr Winne Mandela Drive and St Andrews Road, Hurlingham
Time:	7am for 7.30am

Cape Town

Date:	Tues, 25th of November, 2025
Venue:	SSISA Conference Centre, Boundary Road, Newlands, Morne du Plessis Boardroom, 4th floor
Time:	7.30am
Venue:	ABRU Motor Studio, Lourensford Wine Estate, Somerset West
Time:	5.30pm for 6pm

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