Funds SA March 2025 Quarterly Comment

Investment update

The March quarter began with positive performance from the major developed market listed equities indices. US markets soared early on with the S&P500 hitting an all-time high in mid-February.

Good times often don't last and for equities in the March quarter they didn't. In February we learned of a new entrant in the Artificial Intelligence (AI) race, the Chinese company DeepSeek. DeepSeek is purported to have a superior large language model that would be made available to the market at a significantly lower cost relative to US peers. This sent the Magnificent Seven companies, most notably NVIDIA, into a tailspin and collectively, the group finished the quarter 16% lower.

President Trump then gave equity markets another black eye after he begun talking up his preference to implement an aggressive tariff regime and then put his billionaire friend in charge of cutting federal government spending. By the end of March, the US had announced tariffs on Canada and Mexico along with goods including cars, steel aluminium and Elon Musk had appeared on stage with a chain saw to signal the beginning of his cost-cutting crusade. These actions only served to add to already increasing uncertainty for companies, countries, and investors which translated into pronounced volatility in financial markets, particularly equities.

By the quarter's end the S&P500 finished down 4.6%, the NASDAQ and the broad-based Russell 2000 closed down 10.4% and 9.8% respectively. US treasuries benefitted from the equity selling, the 10-year treasury bond yield fell (values increased) by 0.4% to 4.2%. The move to less risky assets help pushed the spot gold price up 19.3%.

European equities moved higher early on, but unlike the US, European markets didn't look back. The broad European STOXX 600 index pushed 5.8% higher over the quarter, mostly on the back of Germany's election outcome which signalled a loosening in fiscal policy and fuelled expectations of increased defence spending. The local equity index, the DAX, index rose 11.3%. The European Central Bank made their fourth consecutive interest rate cut which added support to equities and bonds.

Asian equities markets were mixed over the period with China and its related markets including Hong Kong's Hang Seng index (+15.1%) moving higher after the DeepSeek AI reveal. Conversely, it was this reveal that sent South Korea, Taiwan markets lower while Trump's tariff rhetoric caused South-east Asian markets, including Australia to sell off.

Australia's ASX/S&P300 index fell 3.9% in the quarter. Company reporting season took a toll on the Australian equity market in February, led by the banks. Any earnings miss relative to expectations, small or large, resulted in meaningful stock price moves to the downside. The S&P/ASX300 sectors hit hardest during the period were Information Technology (-18.2%), Healthcare (-9.0%), Real Estate (-6.6%), and Energy (-5.5%). On the flip side, Industrials (+2.5%), Utilities (+2.2%), and Communication Services (+1.9%) rose over the quarter. The Australian government 10-year bond yield was steady at 4.4% as was the Australian dollar, which closed marginally higher at 0.6300 relative to the US dollar.

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Investment options

The SA Metropolitan Fire Service Superannuation Scheme (SAMFS) invests in Funds SA's Taxable investment options. Except for the Cash option, all other investment options had negative returns for the quarter.

Aside from the Cash option, all other options are well diversified across stocks, bonds, cash, property, and infrastructure. In volatile periods, diversification works and the impact to the option's performance is typically lower than the headline equity market decline.

The Australian and International Tax-Exempt asset classes fell 4.3% and 1.6% respectively over the March quarter. In contrast, the fixed interest asset classes delivered positive returns including Government Bonds (+2.0%), Australian Investment Grade Credit (+1.7%), and Global Investment Grade Credit (+1.8%). Unlisted asset classes such as Infrastructure (+1.8%), and Property (+1.3%) all delivered positive returns for the quarter. The SAMFS default investment option, High Growth, declined 1.6% in the quarter.

Table 1. Taxable investment options performance as of 31 March 2025
Returns are net of fees and tax, based on the post-tax unit pricing model detailed in the SAMFS MOA

Investment option	3 months %	FYTD %	1 year %	3 years % p.a.	5 years % p.a.	7 years % p.a.	10 years % p.a.
Cash	1.0	3.1	4.1	3.2	2.0	1.8	1.8
Capital Defensive	0.8	4.0	4.0	2.9	3.0	2.7	2.7
Conservative	0.2	4.2	4.0	3.4	4.6	3.7	3.7
Moderate	-0.4	4.1	3.6	4.0	6.2	4.8	4.7
Balanced	-1.1	4.2	3.6	4.5	8.1	6.1	5.9
High Growth	-1.6	4.7	3.8	4.8	9.3	6.9	6.9

Notes: Due to rounding, the excess return shown may not exactly equal the difference between the portfolio and benchmark returns.

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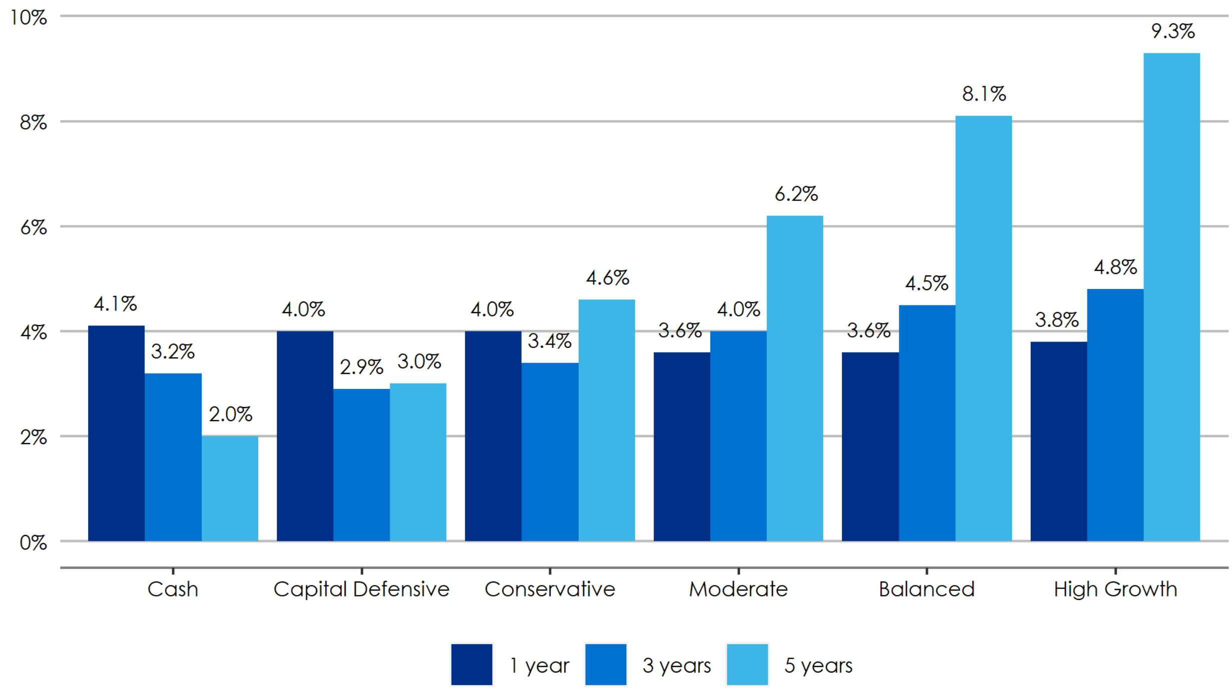
Chart 1. Taxable investment options annualised returns to 31 March 2025 [1.]

Returns are net of fees and tax, based on the post-tax unit pricing model detailed in the MOA



Note: 1. 2025 is the financial year to 31 March 2025, i.e., part year.

Post the end of the March quarter

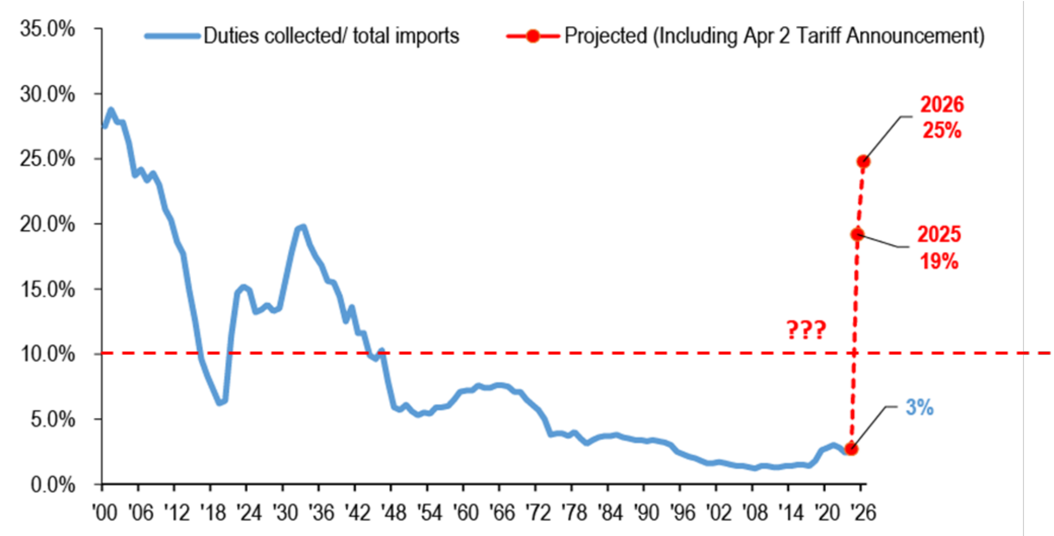
At the time of writing, the US President's self-proclaimed 'Liberation Day' on 2 April has been and gone. The US President has announced a swathe of tariffs on many countries and within days, some of these tariffs have been increased, then decreased, or postponed. We now know that, for the time being at least, some products have been carved out from the tariffs, for example smartphones, computers and electronic components.

The result of the announcements has been increased market volatility. Fear, uncertainty, and unpredictability are now firmly embedded in the global economy and markets. The era of 'globalisation' has looks to have now been replaced by global trade wars which, in turn, has triggered a broad sell off across global equities markets which has extended to bond markets and the US dollar.

Chart 2 below illustrates the extent of the tariffs. The tariff levels recently announced are as high as those that were prevalent just prior to the onset of the Great Depression and approaching those in place at the turn of the nineteenth century.

Chart 2. US Tariffs – increasing protectionism

These are interesting times

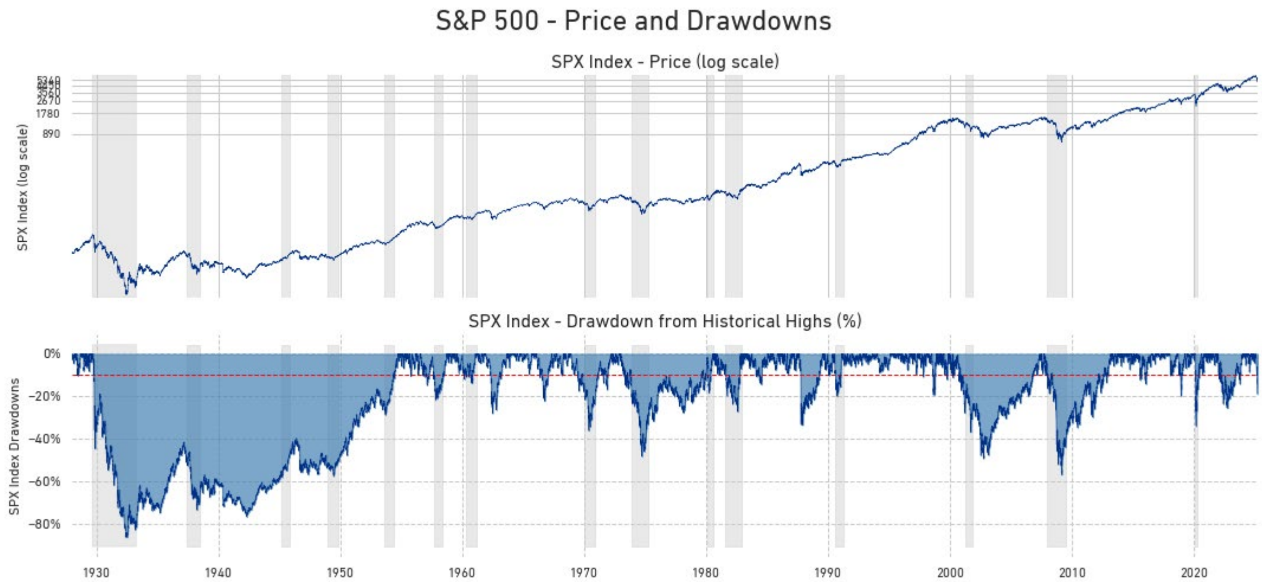


Source: JP Morgan

Volatility and down markets are part of investing and occur with a degree of regularity, but history demonstrates that over the long-term equity markets typically trend upward. This is illustrated in Chart 3 which charts the S&P500 performance since 1930.

Chart 3. US S&P 500 historical drawdowns

Long-term investing is rewarded



Source: S&P, FactSet, Funds SA

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What have Funds SA been doing during this period?

In recent months, we have adjusted portfolios by reducing global equities and to a lesser extent, Australian equities to bring the asset allocation in line with the Strategic Asset Allocation target. We'd previously held slightly overweight positions to the equity asset classes. The proceeds have been used to increase exposures to Cash, Property and the Alternative asset classes.

The Chief Investment Officer and the investment team at Funds SA are comfortable with the recent adjustments do not believe a change in investment strategy is warranted at this point. As market volatility impacts the asset class exposures across the investment options, Funds SA will continue to rebalance and maintain the strategic asset allocation.

Diversification is key and it works. The allocation to defensive assets such as fixed interest (bonds) and infrastructure is working well in this volatile environment. Equities is the asset class that is most exposed to the current volatility.

The team continues to meet daily and will continue to monitor and review portfolios as global markets digest the implications of the tariff announcements. The portfolios will be rebalanced to maintain the overall Strategic Asset Allocation commensurate to the risk profile of the investment options.