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THE CIO PERSPECTIVE

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Commentary | Quarter 3 2025

Macroeconomic Overview

The liberation day volatility concerns seem a distant memory as markets continue to perform well. Geopolitical issues, war, and trade tensions have all taken a sideline to an artificial intelligence (AI) led market boom.

Key observations over the last six and twelve months were:

- Emerging markets, propelled by China continue to perform strongly. India continues to be a laggard with MSCI India showing negative returns over the year in USD terms. After a period where valuations were stretched, the Indian market has seen disappointing corporate earnings, a drop in domestic consumption, fears of adverse tariff outcomes, and a weakening currency.
- The Chinese market has seen a sharp rally this year, driven in part by retail investors shifting some of their bank deposit to equity markets amid optimism of AI, chip manufacturing and supportive government policy.
- The broader global equity market continues to perform well year to date with weakness in the US dollar assisting hedged returns.
- The S&P 500 continues to improve with strong six month returns driven by technology driven mega-cap companies, with the top ten having more expensive valuations than the broader universe.
- The ASX 200 had a strong six months despite mixed results in the most recent earnings season.
- Global infrastructure continues to outperform global real estate driven by US utilities.
- Core fixed income markets continue to perform with high yield markets showing strong returns amid tight credit spreads.

Index Returns to 30 September 2025 (sorted by year-to-date, highest to lowest)

Index	6 mo	YTD	1yr	3yr	5yr	10yr
	%	%	%pa	%pa	%pa	%pa
MSCI China NR USD	15.77	32.31	36.88	18.26	2.00	7.39
S&P/ASX Small Ordinaries TR AUD	25.25	22.75	21.50	15.54	9.27	9.62
MSCI EM NR AUD	16.50	19.14	22.81	17.02	8.71	8.62
MSCI Europe NR AUD	8.51	19.11	20.46	21.68	13.96	8.77
MSCI AC Asia Ex Japan NR USD	17.12	18.48	22.67	17.58	8.12	9.13
MSCI ACWI ex Australia 100%Hedged NR AUD	18.08	15.59	17.02	21.13	12.93	N/A
S&P Global Infrastructure NR Hdg AUD	10.78	14.59	15.68	14.28	12.28	7.84
S&P 500 Hedged NR AUD	19.30	14.03	16.43	22.60	14.08	13.34
MSCI Japan NR AUD	13.11	12.76	21.80	19.99	10.70	8.87
S&P/ASX 200 TR AUD	14.66	11.45	10.56	15.17	12.98	10.11
S&P/ASX 200 A-REIT TR	18.90	10.79	4.10	19.85	11.91	8.69
MSCI ACWI Ex Australia NR AUD	12.87	10.68	23.02	22.01	15.37	12.61
MSCI World Ex Australia NR AUD	12.44	9.73	23.03	22.63	16.27	13.14
S&P 500 TR AUD	12.79	7.28	23.10	23.68	18.31	15.97
Bloomberg AusBond Composite 0+Y TR AUD	3.04	4.37	4.09	4.25	-0.23	2.12
FTSE EPRA NAREIT Developed NR AUD	2.16	3.12	4.35	8.20	7.17	4.35
RBA Cash Rate Target	1.98	3.06	4.21	4.11	2.59	1.98
Bloomberg AusBond Bank 0+Y TR AUD	1.94	3.04	4.19	4.05	2.53	2.08
Bloomberg Global Aggregate TR AUD	-1.14	0.81	7.19	4.39	0.00	1.73
MSCI India NR USD	-5.11	-8.51	-9.09	9.19	14.88	9.73

Key issues

At a macroeconomic level our current focus is on the following:

- **Asset valuations.** Markets continue to be driven by AI, showing no signs of slowing. The 12 month forward looking PE of the top 10 S&P 500 stocks is 1.5 times the remaining stocks. This is reminiscent of the late 1990s and early 2000s and has the hallmark of a bubble but an immediate catalyst for a burst is difficult to pinpoint. Concentration remains a feature of the market.
- **Yield Curve Steepening.** Yield curves are steepening in the US and Australia with rate cut expectations pointing to short-term yields falling further. Yields on longer dated US government bonds remain somewhat elevated on inflation fears and concerns surrounding the federal deficit.
- **Inflation and interest rate trajectory.** Despite the US government shutdown, latest CPI data shows annual inflation rate at 3% which was lower than expected. Markets anticipate the US Federal Reserve will cut 125 basis points between now and the end of 2026. Markets are more sanguine about RBA rate cuts over the same period.

Reflections from USA research trip

During October I attended a research trip to the USA. The purpose was to visit US based fund managers and do a deep dive on their strategies. We visited fund managers in Austin, New York, LA and San Diego covering sixteen strategies during the two-week trip. Key observations form the trip were:

- **AI boom or bust**. It was difficult to get a strong view one way or another on whether we are in an AI led bubble and if so, what the catalyst will be to burst the bubble. The bear case is that the capex required to continue developments in AI is substantial and that a return on investment will be difficult to achieve. The bull case is that this will lead to significant improvements in productivity spurring economic growth justifying current market valuations.
- **Growth in Private Assets**. We saw no fewer than eight private asset strategies during the trip suggesting that we are at the top of the cycle on product issuance. Whilst private equity and private credit are legitimate asset classes, issues such as liquidity, lack of transparency, and the heterogeneous nature of strategies require greater caution for retail investors.
- **Geopolitics and Tariffs**. Notably this was not a wide topic of conversation. Market participants are largely underplaying the impact of geopolitics and tariff led trade tensions.

Views across the asset classes

Equities

On a relative basis we continue to favour international equities. We are of the view that opportunities exist outside of the concentrated areas of the market globally, including outside of the US.

We are slightly negative for both Australian and international small cap equities despite strong recent performance in Australian small caps.

Fixed Interest

Treasury yields have dropped from their elevated levels with the US 10-year treasury hovering around 4%, down from 5% highs earlier in the year. Tight credit spreads are a feature of the market.

We continue to favour Australian fixed interest over international fixed interest providing attractive yields and credit quality. We are still positive on income assets and retain a shorter interest rate duration position across portfolios.

Property and Infrastructure

Global infrastructure continues to be our preference with a smaller allocation to global real estate. A longer-term argument can be made for real estate, but allocation based on recent performance is hard to justify. Our preference remains for global over Australian listed real estate.

Alternatives

Issuance of products in the private asset space shows no sign of slowing down. Our preference continues to be towards more liquid and multi-strategy alternative products. Gold prices are at record highs, albeit with some recent softness, suggesting investors are concerned about the macroeconomic environment. Broader market performance suggests otherwise.

Portfolio Implications

We remain cautious, anchoring to our long-term strategic asset allocation. We remain diversified and maintain our preference for active management across most of the asset classes.

Summary of current asset class view

Asset Class	Current View
Australian Equities	Neutral
Australian Small Caps	Slightly Negative
International Equities	Slightly Positive
International Equity Small Caps	Slightly Negative
Australian Listed Property (AREIT)	Slightly Negative
Global Listed Property (GREIT)	Slightly Negative
Infrastructure	Positive
Alternatives	Selectively Positive
Australian Fixed Interest	Positive
International Fixed Interest	Neutral

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