



Commentary | Quarter 2 2025

Macroeconomic Overview

The first half of 2025 saw bouts of volatility across equity and fixed income markets driven by macroeconomic and geopolitical factors. Yet looking at index returns at the end of the financial year would suggest a largely benign environment. Key observations over the half and the financial year were:

- Equity markets performed strongly led by China and the broader global indices. Chinese equity markets were driven by a combination of policy stimulus, valuation recovery and improving economic fundamentals.
- Chinese equities also propelled emerging markets although India was a notable laggard, driven by foreign capital outflows, weak corporate earnings and valuation concerns.
- The defensive characteristics and secular tailwinds such as AI -driven energy demand helped global listed infrastructure perform strongly.
- Supportive monetary and fiscal policy such as increased defence spending helped European equities to outperform global indices.
- IT and financials helped the Australian equity market post a respectable double-digit return.
- The S&P 500 was a slight laggard, dented by the Liberation Day announcements and President Trump's attack on the Federal Reserve Chair, Jerome Powell.
- Global and domestic bond markets delivered strong single digit returns assisted by central bank easing although volatility persisted due to tariff impacts and fiscal concerns.

Index Returns to 30 June 2025

Index	6 mo	1 yr	3 yr	5 yr	7 yr	10 yr
	%	% pa	% pa	% pa	% pa	% pa
MSCI China NR AUD	10.9	36.3	4.7	0.0	1.8	3.8
S&P Global Infrastructure NR Hedged AUD	10.4	23.7	10.0	11.3	7.0	6.9
MSCI World Ex Australia NR AUD	3.4	18.6	20.4	15.8	13.6	12.5
MSCI EM NR AUD	8.9	17.5	11.5	7.9	6.3	6.5
S&P 500 TR AUD	0.3	17.4	21.6	17.8	16.4	15.5
S&P/ASX 200 TR AUD	6.4	13.8	13.6	11.9	8.8	8.9
MSCI World ex Australia NR Hedged AUD	6.6	13.5	16.7	13.6	10.7	10.4
S&P/ASX Small Ordinaries TR AUD	6.5	12.3	10.0	7.4	4.6	7.6
FTSE EPRA NAREIT Developed NR Hedged AUD	3.3	8.4	2.2	4.5	1.4	3.5
Bloomberg AusBond Composite 0+Y TR AUD	4.0	6.8	3.9	-0.1	1.8	2.3
Bloomberg Global Aggregate TR Hedged AUD	2.7	5.5	2.3	-0.6	1.3	2.0
Bloomberg AusBond Bank 0+Y TR AUD	2.1	4.4	3.9	2.3	2.1	2.0

Key issues

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

- **Expanding tariff regime** and the implementation of 1 August tariffs for European Union, Mexico, Canada, copper, pharmaceuticals, and semiconductors. The current effective tariff rate for the United States is circa 20% and we are watching where this rate will settle. Some observers view that an effective tariff rate of around 15% may be palatable for markets and the US Fed.
- **Inflation and interest rate trajectory.** Goods inflations had cooled but services inflation remains sticky. Central banks have exercised caution on their current easing cycle due to the uncertainty of the inflation outlook, the impact of tariffs and a resilient labour market.
- **Fiscal policy and rising sovereign debt.** Whilst equity markets appear to be impervious, the bond market continues to express concern about the lack of fiscal discipline and inflation risks. During the last six months yields on longer dated US treasuries have increased with the US 30YR nearing or exceeding 5% on a few occasions.
- **Geopolitical risks.** Wars in several regions and tensions over Taiwan continue to cast a shadow over world affairs. At this stage the markets are largely ignoring geopolitical risks, but we may be entering what has been described as the most fundamental global restructuring politically, militarily, and economically since WWII.
- **Asset valuations.** Equity market valuations, notably in the US to some extent in Australia appear to be stretched. Correction risks abound although catalysts may not be that easy to find. Focussing on data appears to be the best course of action.

Views across the asset classes

Equities

Assuming a neutral 50/50 allocation to Australian and international equities, we are in slight favour of international. The risks outlined above are a potential headwind for markets, but we are of the view that better valuation opportunities exist globally, especially in China, Europe and Japan.

We are slightly negative for both Australian and international small cap equities. A weaker growth outlook is likely to be a headwind for the sector.

Fixed Interest

Treasury yields reflect inflation and fiscal concerns with 10-year yields remaining elevated. Moderate widening in investment grade credit, more in high yield but more caution than panic.

We consider Australian fixed interest better value over international fixed interest providing attractive yields and credit quality and providing some respite from global volatility. We are still positive on income assets.

Property and Infrastructure

Headwinds of high interest rates abating and attractive valuations are favourable for infrastructure assets. Global real estate is showing attractive valuations, but it is too early to say if this sector is out of the woods. Our preference remains for global over Australian listed real estate.

Alternatives

Private markets are not immune to the trials and tribulations of the listed market. Any illiquidity premium may be harder to achieve in the current environment. Liquid and multi-strategy alternatives are preferred.

Portfolio Implications

Our overall view remains cautious, and our current asset allocation is largely in line with long-term strategic asset allocation positions. We remain diversified watching for clear positive or negative signs. We note that uncertainty and volatility can be happy hunting grounds for active management.

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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