

Market Review

Chairman Powell was under significant political pressure ahead of the annual economic policy symposium in Jackson Hole. The US administration had continuously slammed him for not reducing interest rates quickly enough and had called for a wholesale restructuring of the FED. Trump's criticism included social media attacks, actively searching for a "shadow chair" to replace him well before his term expires in May 2026, and nominating Stephen Miran, one of the President's top economic advisers and architects of the "reciprocal" tariffs policy, to occupy the vacant seat on the FED's board of governors through Adriana Kugler's remaining term, set to expire in January 2026. Hence, the stakes were high on August 23rd when Powell took the stage to deliver the final speech of his career, a "last stand" that could define his legacy in the years to come. He was finding himself in what Reuters had aptly described as a "no-win situation", with any statement potentially open to charges of political motivation. In fact, signalling openness to rate cuts could have been interpreted as capitulating to the pressure emanating from the White House, while upholding a hawkish stance despite deteriorating employment data could have been seen as a stubborn act of defiance aimed at proving the independence of the FED.

Powell opened by acknowledging the recent weakness in the labour market, observing that while "it appears to be in balance, it is a curious kind of balance that results from a marked slowing in both the supply and demand for workers". He cautioned that, in this "unusual situation", if downside risks materialise, "they can do so quickly in the form of sharply higher layoffs and rising unemployment". In other words, he indicated his awareness that, when the labour market turns, job losses can escalate rapidly, rather than in a linear way. He then directed his attention to inflation, commenting that "the effects of tariffs on consumer prices are now clearly visible" and expected "to accumulate over coming months". However, "a reasonable base case is that the effects will be relatively short lived, a one-time shift in the price level". In summary, Powell explicitly recognised for the first time that tariff-driven inflation may prove to be transitory, despite never uttering the (now infamous) word which, following the high inflation of 2021-2022, has become synonymous with a major policy misjudgement and a communication error on the part of the FED.

In his remarks, Powell reiterated multiple times the central bank's commitment to a 2% inflation target, despite the US Personal Consumption Expenditure (PCE) Core, its preferred measure, having been above it "for more than four years". Nevertheless, he opted to pave the way for a rate cut at the upcoming September FOMC stating that "with policy in restrictive territory, the baseline outlook and the shifting balance of risks may warrant adjusting our policy stance". After delivering the punchline, which sent the US stock market soaring, he made it clear that should the FOMC members decide to pivot in a dovish direction, they would do so "based solely on their assessment of the data and its implications for the economic outlook and the balance of risks", and not because of Trump's demands. The latter part of the argument was not openly articulated, but it logically follows from his premise. However, the shadow of the President loomed large over the event. While Powell was giving his keynote address, Trump publicly threatened to fire Governor Lisa Cook if she didn't resign over allegations that she committed mortgage fraud, significantly escalating his campaign to exert more control over the central bank. The renewed assault came despite the FED preparing to take an almost unprecedented step by easing its monetary stance with inflation not only close to 3% but also accelerating in the previous three months. In fact, most rate cuts in modern monetary history have occurred during periods of slowing inflation, economic slack or financial crisis. The last time before this cycle the central bank moved to

trim rates with core PCE inflation at or around the present-day level was in the early 1990s, before its (unofficial) adoption of the 2% target. As one astute commentator has observed, “perhaps 3% is starting to become the new 2%”.

International Equities

US equities broke to new all-time highs in August, with all three major averages notching their highest monthly close in history. The Dow Jones Industrial (+3.20% in USD terms) outperformed the S&P 500 (+1.91%) and the Nasdaq 100 (+0.85%) for the first time since “Liberation Day”. The Russell 2000 (+7.00%), the popular benchmark for smaller companies, exploded higher, but remained below the prior peak set in November 2024. Tariffs, AI and earnings dominated financial news. On August 29th, a US court of appeals ruled that most of Trump’s “reciprocal” tariffs imposed under emergency powers are unlawful on the grounds that Congress did not explicitly delegate the authority to impose such sweeping duties. However, the court delayed enforcement of its decision until October 14th, giving the US administration time to file an appeal with the US Supreme Court. A report from the Massachusetts Institute of Technology (MIT) found that approximately 95% of corporate generative AI pilot projects failed to deliver a measurable financial return, albeit due to poor execution, not flaws in the technology itself. Finally, market breadth improved decidedly during the month on the back of broad-based strength in earnings growth, particularly relative to consensus expectations. According to FactSet, earnings for the “Magnificent Seven” exceeded estimates by a wide margin in Q2, rising +26.6% versus an expected +13.9% as of June 30th. However, earnings growth for the rest of US large caps surprised on the upside as well, nearly tripling analysts’ initial projections (+8.1% compared to estimates for +2.5%). As a result, the tech behemoths interrupted a 4-month outperformance streak, although solid gains kept their combined market capitalisation firmly above 19 trillion USD. Market leadership rotated away from mega cap growth names, with value stocks catching a bid. Neglected sectors the likes of healthcare, materials and consumer discretionary topped the list, followed by communication services and energy. Utilities bucked the trend, while technology and industrials consolidated recent gains.

US equities trailed the rest of the world (as exemplified by the MSCI AC World Index ex USA TR Index), extending their underperformance since the beginning of the year to double-digits in AUD terms. Resilient corporate results and a jump in the value of the Japanese Yen (JPY) prompted by stronger-than-expected economic growth in Q2 buoyed Japan. Europe outperformed the general index amid some progress in security talks towards ending the war in Ukraine. Conversely, emerging markets were weak, as India declined following the US’ decision to raise tariffs to 50% from 25% in retaliation for the country’s purchase of Russian oil. All in all, the MSCI AC World Daily TR was up +2.47% in USD terms and +0.65% in AUD terms.

Australian Equities

Australian equities broke to new all-time highs in August amid modest earnings growth and stock price volatility hitting new highs as well on the day of quarterly results. In general, value stocks outperformed growth stocks by the largest amount since November 2020, while domestically focused companies outperformed internationally exposed companies on the back of improving consumer sentiment. The S&P/ASX 300 jumped +3.16%, buoyed by resources, consumer discretionary, utilities, A-REITs and banks, with the latter sector propelled higher by Westpac, ANZ and NAB. Conversely, CBA fell for the second month in a row despite reporting a record profit for FY25, as investors locked in gains and raised doubts about the absence of additional upside to justify its price-to-earnings ratio of over 30x.

Healthcare and technology bucked the trend, the former on the back of CSL disappointing on guidance, while weakness in the latter was concentrated in AI and data centres related stocks, with investors rotating away from those names into cheaper stocks. Mid-caps and smaller companies outperformed the Top 20. The S&P/ASX Small Ordinaries Index (+8.50%) was the standout performer of the month, rising the most since July 2022. Despite the catch-up, the small cap benchmark was trading at a 15% discount to the S&P/ASX 300 at the end of the month, with the latter index closing in on 20x forward earnings, two standard deviations above its long-term average.

International Fixed Income

On August 6th, the Bank of England (BOE) lowered its official bank rate by 0.25% to 4%. The cut itself was widely anticipated by markets, but the vote was unexpectedly tight, requiring two rounds to pass for the first time since the formation of the Monetary Policy Committee (MPC) in 1997. In the first round, there was no majority as one member voted for a larger cut of 50 bps. In the second round, that member switched to support the 0.25% reduction, enabling the narrow 5-4 majority, as four members wanted to keep the rate at 4.25%. On August 14th, the Norges Bank, Norway's central bank, held interest rates steady at 4.25%. On August 20th, the Riksbank, Sweden's central bank, adopted the same approach, judging that the recent deterioration in the economy does not require a policy response. On the same day, the Reserve Bank of New Zealand (RBNZ) reduced its Official Cash Rate (OCR) by 0.25%, from 3.25% to 3%, a 3-year low. The monetary policy committee was split between a 0.25% and 0.50% cut, indicating a dovish shift. The decision was a balancing act between addressing accelerating headline inflation and the need to counteract a stalling economy hindered by weak household consumption, rising unemployment and declining house prices. The dovish tone and guidance surprised markets as the central bank's official mandate is price stability, that is, targeting inflation of 1-3%, with a focus on the midpoint (2%) over the medium term.

The Bloomberg Barclays Global Aggregate Index hedged back to AUD rose +0.49% for the month as the US yield curve transposed lower and steepened, with the differential between the 30 year and the 5-year reaching 1.23%, its highest level since July 2021. In addition, the so-called "term premium" which is the compensation required to buy and hold a 10-year Treasury as opposed to simply rolling over short term paper at prevailing rates, pushed to new highs for this cycle at 0.80%.

Australian Fixed Income

On August 12th, the RBA reduced the cash rate to 3.60% after just one month of pause, delivering the third 0.25% cut of 2025. The central bank downgraded its estimates for medium-term growth on the back of revised down productivity and weaker than expected public demand. Conversely, it left the inflation outlook unchanged with the CPI projected to peak at 3.1% in Q2 2026, before declining to 2.5% by Q4 2027. During her press conference, Governor Bullock noted that the central bank's forecast for inflation to return to the midpoint of the target band is contingent on "a couple more rate cuts". At the end of the month, the cash futures were pricing one additional cut in the remainder of the year, while pushing out a second, final reduction to Q2 2026. As the Australian bond market had fully priced in a 100% probability of a cut ahead of the meeting, reactions to the decision were muted, with the 2-, 5- and 10- year yields ending the month at 3.34%, 3.64% and 4.27% respectively. The Bloomberg AusBond Composite 0+ Yr added +0.33% as investors continued to snap up good quality credits, pushing spreads to record tight levels. The

Australian Dollar caught a bid vis-à-vis the greenback and the Chinese Renminbi (CNY) but dropped against major European currencies and the Japanese Yen (JPY).

Real Assets

Global property rallied +4.49% in USD terms and +2.67% in AUD terms in August. At the regional level, Asia topped the list, followed by Australia. The US outperformed the general index despite data centres posting negative returns for the month following public remarks from OpenAI CEO Sam Altman, who cautioned against speculative excess in the sector. Europe continued to consolidate the strong gains recorded in Q2, with the UK weighing on the region.

Global infrastructure was up +2.02% in USD terms and up +0.24% in AUD terms for the month. Transportation stocks led gains, driven by robust passenger growth during the summer travel season (in the Northern Hemisphere). Electric utilities remained resilient, while renewables and communication infrastructure underperformed.

Alternatives

Alternatives (+1.80%) delivered strong, broad-based positive returns in August 2025. Long/Short equities and event driven were the best performing strategies, while trend following mandates increased their exposure to equities to the highest level since January 2020, benefiting from the global stock market rally.

Market Outlook

On September 17th, the FED lowered its target rate by 0.25% to a range of 4.00%-4.25%, its first reduction since December 2024, and signalled a gradual easing cycle in response to mounting labour market concerns. The move was largely in line with market expectations. While there were isolated calls for a more aggressive 0.50% cut, we considered such an outcome to be unlikely. In his press conference, Chairman Powell characterised the measure as a “risk management cut”, and, on the surface, which appears to be the only possible rationale in light of the continued economic strength exhibited by headline data. In fact, US GDP growth rebounded to +0.8% QoQ in the second quarter, from a -0.1% contraction in the first quarter, with the unemployment rate only ticking up to 4.3%, the inflation rate remaining stubbornly above target at 3% and equity markets grinding higher. In its summary of economic projections, the central bank itself recognised this reality by revising its growth and inflation forecasts higher, while downgrading its estimates for unemployment. It is entirely possible that the FED thinks its swift and sharp action over coming months will deliver positive results for the economy. The alternative is that the central bank may have re-embarked in its easing cycle at a time the economy is already showing early signs of re-acceleration. Powell asserted that the FED was “right to wait and see how tariffs and inflation and the labour market evolved” before lowering rates. We would not be so sure about that. There is a reason Trump labelled the Chairman of the FED “Too Late”, and in our view there is a strong argument to be made that such a nickname may come true in a not-so-distant future.

As recently as June, the FED had indicated it would cut rates three times, twice in 2025 and once in 2026. However, in the lead-up to the September meeting, markets were already pricing in three cuts for 2025 and an additional three for 2026. This created a clear dislocation between practitioners’ expectations and the central bank’s official stance. The

anticipation was that the FED would move closer to the market's pricing. In some respects, this occurred. It delivered the first 0.25% cut and pencilled two more for the remainder of the year, aligning its new 2025 projection with expectations. That said, the divergence for 2026 persists, with the newly released Dot Plot continuing to telegraph just one rate cut for next year. It seems the central bank is attempting to strike a balance by beginning to ease without fully caving in. While its conservative posture is understandable, we continue to believe that the FED will move further toward the market's pricing over time. Our long-standing base case of 0.75% to 1.00% of rate cuts in 2025 is gaining traction, and we remain confident in that forecast. We also expect more easing in 2026. However, inflation remains a central concern. The FED reiterated its 2% target but now foresees that it will not be achieved until 2028. Should it finally get there, it would imply an eight-year stretch during which the inflation target was consistently missed, calling into question the credibility of the institution. We remain sceptical of the FED's inflation commitment and assess the likelihood of sustainably reaching the 2% target to be remote in the current economic environment, which has undergone a fundamental shift following the pandemic.

Ongoing fiscal stimulus, large-scale investments driven by artificial intelligence and broader changes in global supply chains all suggest that nominal growth, and inflation, will remain elevated. Whereas the pre-pandemic world was characterised by an inflation range of 0% to 2%, with 2% serving as a ceiling, we believe we are now entering a regime where 3% is the baseline and the range is more likely to be between 2% and 4%. In this environment, the 2% target becomes a floor rather than a ceiling, attainable only under recessionary conditions. This structural shift is particularly evident when examining the components of inflation. While tariffs have introduced a modest amount of goods inflation, lifting that segment from deflation into low positive territory, the more persistent issue is services inflation. At the end of August, the US CPI Urban Consumers Services Less Energy Services remained stuck at +3.6% YoY, showing little sign of an imminent retreat. Historically, falling goods prices offset higher services costs, allowing the headline inflation rate to stabilise around 2%. With both goods and services now contributing positively, the mathematics no longer support a return to the 2% target. Given this macroeconomic backdrop, we continue to maintain a constructive view on fixed income in the short term, but our positioning is purely tactical. The FED's pivot toward easing should support returns, particularly in the global space. However, if economic activity begins to rebound more robustly in 2026, as we suspect it might, the environment for bonds could deteriorate, especially if inflation proves more persistent than the FED anticipates.

The central bank's stated rationale for easing is centred on softness in the labour market. Recent data revisions demonstrated that the job market was significantly weaker than initially reported. Between April 2023 and March 2024, the US economy created 600,000 fewer jobs than previously thought. A preliminary revision for the subsequent twelve-month period suggests an additional 900,000 jobs were overestimated. In short, a total of 1.5 million jobs presumed to exist did not, pointing to a much softer labour market than headlines had indicated. However, it is critical to recognise that these revisions only reflect conditions through March 2025. We are now in September, and conditions may have already improved. Tariff-related uncertainty, which had been a major source of business hesitation, is now resolving. At the same time, asset prices have rebounded strongly. Equity indices, real estate markets and even cryptocurrencies are at or near all-time highs, producing a substantial wealth effect. In Q2 alone, US household net worth increased by 7.086 trillion USD, the largest dollar increase since Q4 2020. Furthermore, as rates begin to decline, consumers and businesses may be able to unlock additional liquidity through refinancing,

especially in property, which has been stagnant due to previously elevated rates. Indeed, mortgage refinance applications jumped +58% WoW ahead of the FOMC meeting as the 30-year fixed rate mortgage fell to the lowest level in a year. These dynamics suggest that the FED may be easing into an economy that is no longer weakening but actually regaining momentum. In this context, we share the view that the FED may have been late to intervene, and that, once again, it may be reacting to outdated data. The deterioration in the labour market likely occurred months ago. More recent trends, wealth effects, clarity on trade policy and the prospect of future fiscal stimulus indicate that the economy may be in recovery.

This leads to an important implication for asset allocation. Fixed income remains attractive for now, but if the economy accelerates in 2026, bonds may underperform. Cutting rates into a rising inflation environment is an unusual policy decision and could eventually backfire, creating issues for interest-rate-sensitive assets. At the same time, the outlook for equities remains positive. Despite demanding valuations and concerns about concentration in the technology sector, the broader backdrop is promising. Economic growth is improving, inflation is still within a manageable range, and the FED is easing. This creates what can be described as a “Goldilocks” environment, where conditions are supportive for growth assets. While some seasonal volatility is possible going into Autumn (in the Northern Hemisphere), we remain constructive on equities over the medium term. We also believe that international diversification is increasingly important. US equities have massively outperformed in recent years, largely driven by the technology sector. However, the FED’s easing cycle and the weakening of the greenback may provide a catalyst for performance to broaden. For this reason, we have advocated an overweight exposure to the Rest of the World (RoW), particularly to European markets, while remaining neutral on emerging markets until now. However, the latter region is approaching a turning point as it stands to benefit from a number of tailwinds, of which improving sentiment in China is the first and foremost. While some investors have long preferred “ex-China” strategies, we do not think that emerging markets can deliver sustained returns without the participation of its most prominent member, which remains a large component of the asset class. Moreover, the group includes several technology-heavy indices such as South Korea and Taiwan, which benefit from the structural growth trends seen in AI. We currently maintain an exposure to emerging markets through a broader ex-US allocation, but we are actively considering a shift to an overweight position by adding a dedicated exposure to the region.

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Important information

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ESG pillar scores are displayed as a number between 0 and 100 with most scores range between 0 and 25. It is the asset-weighted average of the company environmental, social, governance risk scores for the covered corporate holdings in a portfolio. The scores measure the degree to which a company's economic value may be at risk driven by environmental, social, and governance factors. The risk represents the unmanaged risk exposure after taking into account a company's management of such risks.*

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