



Investor Insights

SEPTEMBER 2025 QUARTER

Smarter Investment Solutions
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In summary

Global financial markets have remained resilient, with improving investor confidence helping to support returns. While tariff tensions continue to create some uncertainty, steady progress in trade discussions and expansionary fiscal policies, particularly in the US and Europe, are helping to sustain global growth.

The current positive market momentum may continue, but after a strong run of returns, financial markets may be due for a period of consolidation. The global equity rally has, however, been underpinned by strong corporate earnings forecasts and ongoing structural themes, including Artificial Intelligence (AI) adoption and the energy transition. Global monetary policy is expected to remain accommodative, as central banks continue their monetary easing cycles.



In this edition

In this edition of Investor Insights, we explore the current economic and financial market dynamics and how they may impact future returns:

- Global economic growth is anticipated to slow in the coming quarters, but **growth expectations are set to improve in 2026**, supported by fiscal and monetary policy.
- **A solid Australian earnings season** showed a clear divergence between sectors, while many companies provided a cautious outlook. Companies that missed earnings expectations were harshly punished.
- Current global equity valuations may seem elevated, but this view is balanced by looking at forward valuations, which account for **expectations of strong future earnings growth**.
- **The bull case** for the global economy and financial markets is based on resilient corporate fundamentals, strong structural growth themes and more accommodative monetary and fiscal policy.
- **The bear case** is based on a combination of trade wars, unsustainable government deficits, and stubborn inflation, coupled with equity market vulnerability to high growth expectations.

A slower economic growth scenario

The outlook for the global economy remains finely balanced, with a mix of positive drivers and potential headwinds likely to shape future growth and investment returns. Considering this backdrop, our base case is a 'Slower Economic Growth' scenario.

In this scenario, we expect the widespread implementation of tariffs to act as a brake on economic activity, creating a small risk of a mild recession and a temporary spike in inflation. In response, we anticipate global central banks will cut interest rates to stimulate their economies, with potentially one to two cuts from the Reserve Bank of Australia (RBA) and three to four from the US Federal Reserve (FED), although persistent inflation could moderate this action.

Bond markets will likely balance the competing forces of slower growth against these inflation risks, while higher government

spending could cause the gap between short-term and long-term borrowing costs to widen.

Despite this tougher economic backdrop, the corporate sector appears resilient. Many companies boast strong financial positions and positive earnings expectations, providing a solid cushion against a slowdown. While tariff-affected sectors may face downgrades, the broader market is well-supported.

Furthermore, powerful long-term trends such as AI and supportive government policies should continue to provide a crucial foundation for the global economy and share markets.

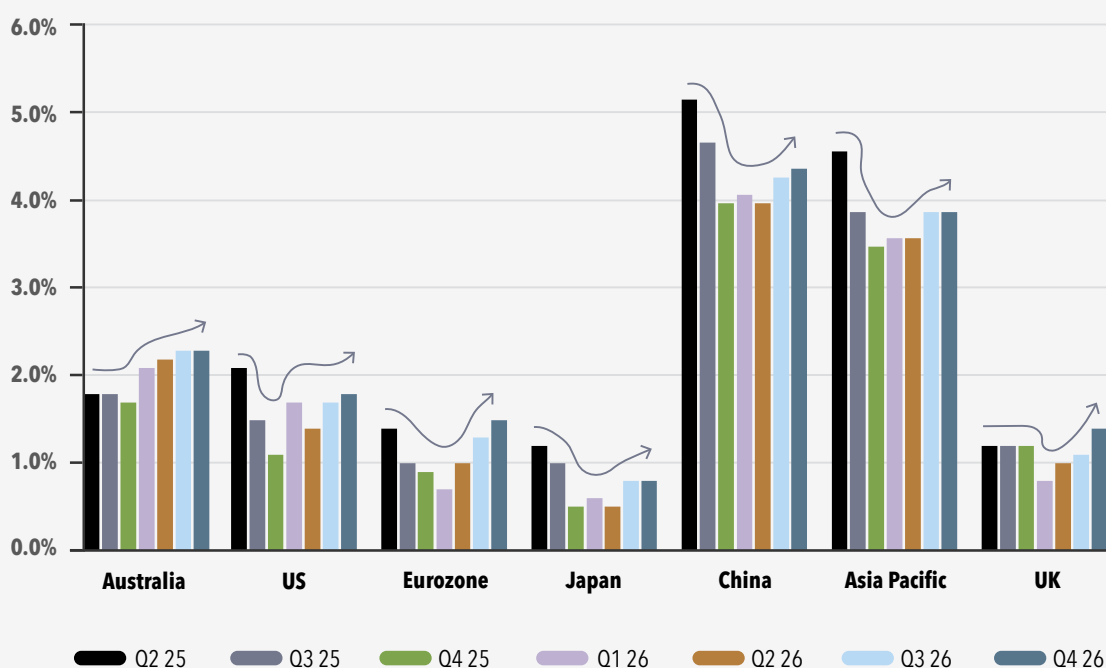
Broad expectations for slowing global economic growth

Global real Gross Domestic Product (GDP) growth indicates the rate at which economies are expanding or contracting.

The regional comparisons of quarterly GDP growth are illustrated in Chart 1, with forecasted growth set to slow in the coming quarters amid economic and trade uncertainties.

A modest reacceleration in economic growth is expected in 2026 as the effects of monetary policy easing, through interest rate cuts, and fiscal stimulus measures such as tax cuts and increased government expenditure take effect and provide support to global economies.

Chart 1: Quarterly real GDP growth and forecasts (year-on-year)



Source: Quilla Consulting, Bloomberg Financial LP

Australia is proving more resilient

The Australian economy appears more resilient than global peers, evidenced by a better-than-expected 1.8% year-on-year GDP growth in the second quarter (Q2) of 2025.

Domestic GDP growth is forecast to accelerate to 2.2% by the end of 2026.

This outperformance is supported by strong public sector demand, particularly in infrastructure, and a rebound in private sector activity as stronger household consumption is driven by interest rate cuts and rising consumer confidence.

While the outlook for the Australian economy is improving, this comes after several years of subdued growth. However, a key tailwind is the Australian economy's high sensitivity to interest rate cuts, which could accelerate a return to trend growth as the RBA continues to cut the cash rate.

Our base case

The current projections for global GDP growth support our base case for a period of slower, below-trend economic growth over the next 12 months for the global economy.



A solid reporting season that was harsh on earnings misses

The recent Australian reporting season revealed a two-speed economy, with a resilient surface masking underlying pressures. While aggregate earnings were stable, the results showed a clear divergence between sectors and a cautious outlook from company management.

Reporting overview

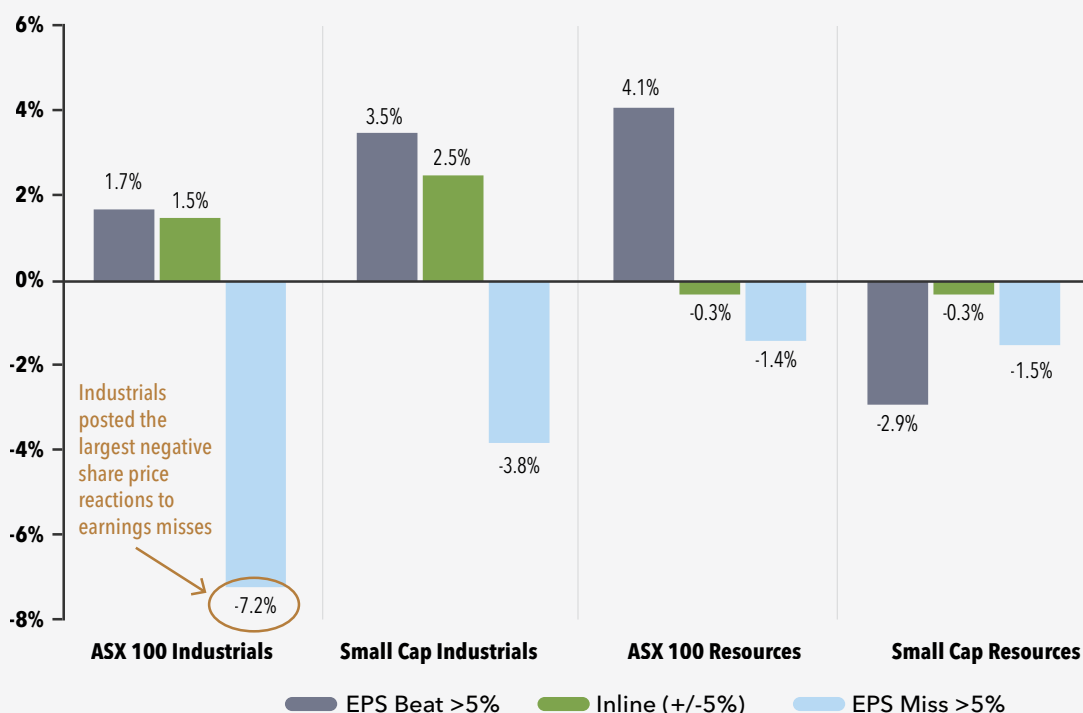
The Materials sector, led by major miners and Consumer Discretionary companies, namely Wesfarmers and JB Hi-Fi, posted resilient results, showing that consumers are still spending, though selectively. In contrast, firms with significant US exposure provided downbeat forecasts, citing concerns about a slowing American economy. The local tech sector was a bright spot, with companies generally producing solid earnings growth.

A key theme was the cautious outlook for the 2026 financial year. Instead of investing heavily in new projects, many boards opted to reward shareholders. This resulted in dividends and

share buybacks that positively surprised the market, signalling a focus on shareholder returns amid economic uncertainty.

A particularly striking feature of the earnings season was the market's unforgiving reaction to earnings misses (Chart 2), which were punished far more severely than beats were rewarded. This was most pronounced for ASX 100 Industrial companies, which saw their share prices plummet by an average of 7.2% after missing earnings forecasts by more than 5%. This severe negative reaction to bad news underscored the nervous sentiment prevailing among investors.

Chart 2: Share price reactions to earnings (EPS) beats and misses by sector and market cap group



Source: Factset, Visible Alpha, Macquarie Research

Notes:

The percentage change shows the 2-day relative percentage return following the earnings announcement.

Company and sector specifics

Materials: The sector had a challenging reporting season, with performance split between miners and other materials companies. BHP Group delivered a strong result, with earnings beating expectations, while Rio Tinto reported an in-line result. The most disappointing results came from Materials (ex-mining), which underperformed the market by an average of 10.3%. These companies were heavily punished for their exposure to international headwinds, including a weak US housing market and tariffs. Building materials company James Hardie was a notable example, with its stock falling 36% after its results.

CSL: The biotech giant suffered its largest single-day sell-off in decades. The market reacted harshly to a triple disappointment: weaker-than-expected results, underwhelming forward guidance, and a major restructuring plan that failed to inspire confidence. Concerns centered on the slower-than-expected margin recovery in its core plasma business.

Consumer Staples: The divergent financial performance of supermarkets was also a highlight of the reporting season. Woolworths saw its heaviest one-day stock decline since 1994 after revealing a challenging outlook, rising costs, and an apparent loss of market

share to competitors. Conversely, Coles rallied after beating earnings expectations. Its success was driven by a sharp rise in e-commerce sales and strong operational performance as it successfully managed costs and attracted budget-conscious shoppers.

Financials: Commonwealth Bank reported steady profit growth and a record dividend, highlighting the robust health of Australia's major banks. However, the results also showed that net interest margins (the profitability of their lending) are being squeezed by

intense mortgage competition. A slight increase in loan arrears (late payments) was also noted, indicating that some households are beginning to feel the strain of higher living costs.

Soft earnings growth expectations

Looking ahead, the earnings outlook for Australian companies is expected to improve, but less so than global peers, while concurrently valuations appear stretched. As such, we still maintain an overweight position in global versus Australian equities.

Reasonable valuations and strong earnings growth expectations

Some market participants have expressed concerns that global equities are expensive and that valuations are unjustifiably high. Using backward-looking data may justify this view, but incorporating future earnings growth expectations provides a more nuanced assessment.

Global earnings and dividends

Global uncertainties have created a mixed earnings outlook for 2025 earnings across global equity markets. However, as Table 1 shows, forward earnings growth is expected to improve materially in 2026 and 2027.

This recovery in earnings is anticipated to be widespread, fueled by expectations of supportive fiscal policy, easing monetary policy, and the underlying strength of corporate and consumer balance sheets.

Earnings growth for the calendar year 2025 shows a challenging environment for some developed markets, with Australia (ASX 200) now expected to see a slight earnings contraction of -0.8%, and the UK (FTSE 100) -2.7%. In contrast, the forecast for Emerging Markets (excluding China) remains exceptionally strong at 17.9% growth.

Looking ahead, the MSCI World Index is projected to grow by 11.8% in 2026 and 10.7% in 2027. Most global equity markets are also set to grow earnings strongly, with only Australia and Japan expected to grow by less than 10% in 2026. Expectations are similar for 2027.

For income investors, dividends are expected to increase marginally in the coming years but do remain modest relative to historical levels, with notable divergence in income potential across markets. European markets have the most attractive dividends, with the STOXX 600 and FTSE 100 offering forward dividend yields of 3.4% and 3.6% for 2026, respectively. Australia's ASX 200 also provides a reasonable yield of 3.2%. These contrast sharply with lower-yielding markets such as the S&P 500 (1.3%) and MSCI India (1.4%), where the investment case is more heavily reliant on capital growth.

Table 1: Regional annual earnings growth expectations and relative valuation measures

Regional Equity Market	2025		2026		2027		Historical Valuation Premium*	PEG Ratio**
	Forward Earnings Growth	Dividend Yield	Forward Earnings Growth	Dividend Yield	Forward Earnings Growth	Dividend Yield		
MSCI World Index	8.2%	1.7%	11.8%	1.8%	10.7%	1.9%	7.3%	1.7
ASX 200 (Australia)	-0.8%	3.1%	8.7%	3.2%	8.3%	3.4%	13.0%	2.2
S&P500 (US)	8.5%	1.2%	12.9%	1.3%	11.2%	1.4%	5.1%	1.7
S&P500 Equal Weight (US)	4.5%	2.0%	11.2%	2.1%	10.8%	2.2%	-11.8%	1.5
STOXX 600 (Europe)	-1.8%	3.2%	10.4%	3.4%	10.0%	3.8%	-5.7%	1.4
FTSE 100 (UK)	-2.7%	3.3%	10.2%	3.6%	8.7%	3.9%	-8.9%	1.3
Nikkei 225 (Japan)	8.0%	1.7%	5.8%	1.8%	11.5%	1.9%	11.1%	3.9
MSCI India	4.8%	1.4%	16.4%	1.4%	11.8%	1.6%	-3.0%	1.3
MSCI Emerging Markets ex China	17.9%	2.6%	17.0%	2.9%	13.2%	3.2%	2.6%	0.8
MSCI China	-0.9%	2.0%	15.6%	2.2%	13.8%	2.4%	-0.5%	0.8
MSCI Asia Pacific ex Japan	7.0%	2.3%	15.6%	2.5%	12.9%	2.7%	2.3%	1.0

Source: Quilla Consulting, Bloomberg Financial LP

Notes:

*Historical Valuation Premium refers to the percentage above or below that the 2026 price-to-earnings ratio trades at compared to the 10-year historical average.

**PEG Ratio: (Price/Earnings-to-Growth ratio) is a valuation metric that divides a company's price-to-earnings (P/E) ratio by its earnings growth rate, providing a more comprehensive view than the P/E ratio alone by factoring in future growth. A figure below 1 is deemed good value. Values starting with a 1 are close to fair value.



Valuations incorporating future earnings

Global equity market valuations may be considered stretched, especially for the US. However, when we factor in expected 2026 earnings growth, the picture becomes more reasonable. Using the Price-to-Earnings (P/E) ratio, a measure of the price paid for every dollar of earnings, valuations look less expensive when considering future earnings.

Table 1 (on the page 11), illustrates these dynamics, showing that the S&P 500's valuation is trading at a modest 5.1% premium to its 10-year average, which is not as high as may be expected. However, the S&P 500 Equal Weight Index reveals a different picture of the US market, trading at a -11.8% discount (cheaper) than its historical average. This significant gap highlights that the average US large-cap is more fairly valued and that value may be found outside of the mega-cap stocks that dominate the market-cap-weighted index.

For Australian investors, the outlook is more modest with the ASX 200's valuation premium being the highest of those in Table 1 at a 13.0% premium. At the other end of the spectrum, markets such as Europe (-5.7%) and the UK

(-8.9%) continue to trade at cheaper valuations compared to historical averages.

These dynamics can be further highlighted using the price/earnings to growth ratio (PEG). The PEG ratio adjusts the P/E ratio for future growth, thereby adjusting the valuation to incorporate forward earnings. A lower value is more attractive and a higher value less so.

Using this measure, Emerging Markets (excluding China) stand out with a ratio of 0.8, suggesting the sector is attractively priced given the high growth potential. In contrast, Japan's Nikkei 225 seems most expensive with a PEG ratio of 3.9, followed by Australia (ASX200) at 2.2, with these markets appearing the least attractive.

Equity market outlook

Overall, the strong earnings outlook combined with reasonable forward-looking valuations provides a supportive backdrop for equity markets. The key risk is a failure to meet these future earnings estimates. Therefore, monitoring macroeconomic developments that could impact corporate profitability remains crucial.



The bull and bear cases for the global economy and financial markets

While the global economy faces a complex web of headwinds from policy uncertainty and regional divergences, a compelling bull case rests on a foundation of powerful cyclical and structural tailwinds. However, an equally credible bear case argues that the headwinds faced are more potent and could easily derail the global economy.

The bull case

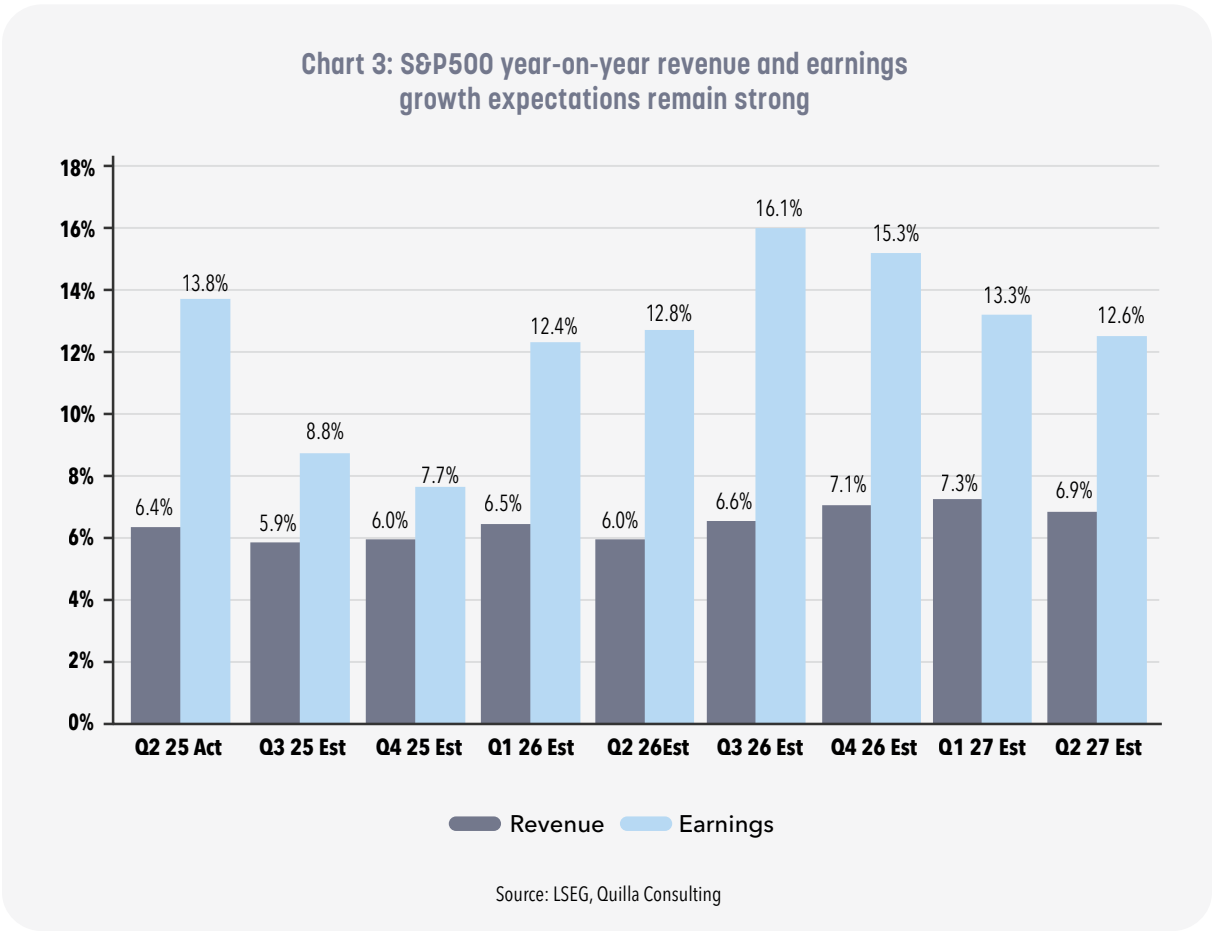
This optimistic scenario envisions an improving economic growth outlook and a continuation of the global equity rally supported by resilient corporate and consumer fundamentals and more accommodative monetary and fiscal policy.

Reduced trade and geopolitical risk: While trade policy remains a significant source of uncertainty, worst-case scenarios have been averted, and recent developments have pointed toward de-escalation. Progress on the trade front has been made with the European Union, the United Kingdom, Japan, and, to a large extent, China, amongst others. While there may be some further trade disagreements in the near term, a calmer trade rhetoric has reduced the risk of market destabilising conflicts.

Accommodative global monetary policy: With inflation broadly contained, most major central banks have pivoted toward policy easing through interest rate cuts to support economic growth. The US FED cut rates in September for the first time in 2025, with expectations for another three to four cuts over the coming 12 months. The RBA has cut the cash rate three times this year, with markets expecting a further one or two cuts. The reduction of interest rates across the globe should support growth assets and investor confidence.

Strong earnings and market momentum: Corporate earnings have remained remarkably resilient, providing a solid fundamental underpinning for equity markets which have continued to reach all-time highs. Global earnings expectations are also robust, supported by US equities, which make up a significant portion of global investor portfolios.

Chart 3 illustrates the quarterly year-on-year growth of US revenue and earnings represented by the S&P 500 Index. Revenue growth is expected to remain steady while earnings are expected to accelerate heading into the second half of 2026. This earnings momentum is supplemented by shareholder return programs as S&P 500 companies are expected to spend \$1 trillion on buying back shares in 2025.



Global fiscal stimulus: Expansionary fiscal policy is providing a direct boost to economic growth in key regions. In the US, recently passed legislation is expected to provide significant support to the US economy through 2026.

In Europe, Germany is notably increasing its federal budget deficit to fund significant investments in infrastructure and defence, with €1.4 trillion in spending expected. Meanwhile, China is also deploying fiscal support measures to offset the impact of trade tensions and stabilise its economy.

Enduring structural investment themes:

Powerful, long-term structural growth drivers are creating investment opportunities that are less dependent on cyclical economic shifts. A massive investment cycle is

underway, centered on the energy transition, rising defence and security spending, and particularly the adoption of AI technologies.

An AI-driven boom: The global economy may be on the cusp of a significant productivity boom driven by AI. Many market analysts and economists have raised their forecasts for US economic growth, explicitly citing the surge in AI-related investment as a key driver. The capital expenditure related to AI development has already provided a boost to economic growth.

A sustained increase in productivity driven by AI would be a powerful economic catalyst, allowing for stronger non-inflationary growth, higher corporate profit margins, and a more durable economic expansion.



The bear case

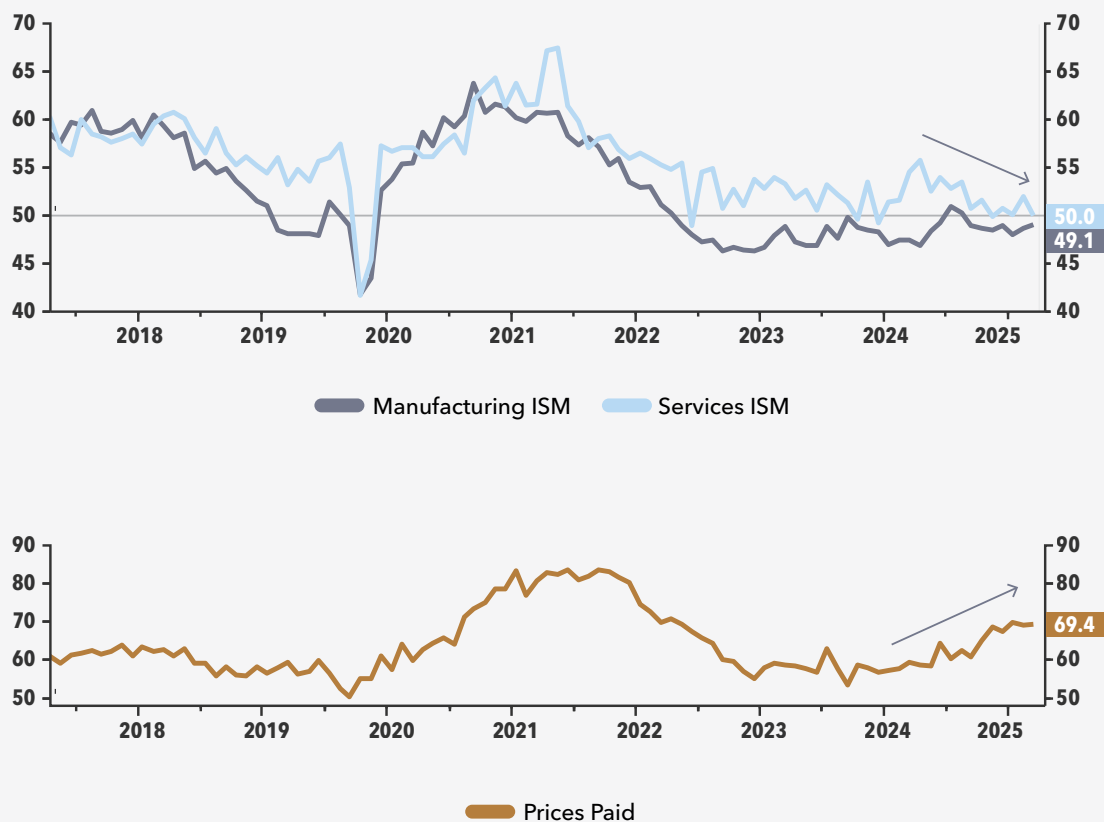
The negative view contends that a combination of trade wars, unsustainable government deficits, and stubborn inflation could lead to “stagflation”, which is a difficult environment of low economic growth and rising prices. Equity markets may also face challenges with expectations for company profits already high, share markets could be vulnerable to a selloff if those lofty forecasts are not met.

Trade policy uncertainty: A primary risk is the rise in global protectionism, with the effective US tariff rate reaching its highest level in decades, rising from approximately 3% to 18%. This uncertainty acts as a drag on the global economy by disrupting supply chains and weakening business confidence. The rising tariffs and the uncertainty around the implementation of trade policy have pressured economic activity while also placing upward

pressure on consumer and business prices.

This potentially “stagflationary” environment is illustrated in Chart 4, where US manufacturing and services activity, measured by the Institute of Supply Chain Management (ISM) survey, has been trending weaker, with US manufacturing activity in particular contracting. At the same time, the ISM survey data points to rising prices paid.

Chart 4: US business activity across services and manufacturing is weakening, while prices paid have trended higher



Source: LSEG Datastream, Quilla Consulting

Deteriorating fiscal health in developed

nations: The worsening fiscal outlook for many developed countries poses a significant threat to global financial stability, with rising budget deficits and increasing debt-to-GDP ratios. The US alone is expected to add \$2.5 trillion to their debt over the next decade, lifted by recent legislation.

Other developed nations also face fiscal pressures. In the Eurozone, Germany plans to increase its federal deficit to fund infrastructure and defence, while France is contending with a large deficit that they are unable to rein in. Meanwhile, Japan continues to manage the highest public debt-to-GDP ratio among developed nations, at over 230%.

Slowing global growth: Major international institutions have revised their global growth forecasts downward to below the long-term average. This slowdown is compounded by weakening labour markets in some regions and mounting pressure on consumers, who face further headwinds from potentially higher tariff-induced prices.

Volatile economic cycles: The global economic recovery is uneven, with significant divergences in growth and inflation between

regions such as the US and the Eurozone. This desynchronization creates a more complex and volatile landscape, making the global economy more susceptible to shocks.

High expectations and stretched equity

valuations: After a strong period of returns and buoyant earnings growth expectations, global equity valuations have trended higher, with the US and Australian large-cap valuations trading at historically elevated levels. These dynamics could increase market sensitivity to negative economic news or policy shifts and may also increase the magnitude of potential market corrections in the event of negative economic data or below expected company earnings.

Risk of persistent inflation: A key risk is that inflation proves more stubborn than anticipated. In the US, this could be driven by tariff pass-through and persistent services inflation. Similarly, Australia is experiencing upside surprises in its monthly inflation data. Persistent inflation could force central banks to maintain a “higher-for-longer” interest rate policy, delaying the monetary easing that markets are anticipating and creating a headwind for both stocks and bonds.

Outlook heading into the fourth quarter

As we move into the final quarter of 2025, the outlook for global markets is balanced. A solid foundation of resilient corporate and consumer fundamentals is being tested by several emerging headwinds. These include weakening labour markets in key economies such as the US and Australia, the risk of stubborn inflation, and persistent trade policy uncertainty. Furthermore, after a strong period of returns, financial markets may be due for a period of consolidation.

A key positive is the significant policy support being provided by governments. Expansionary fiscal policy is providing a direct boost to economic growth in key regions. At the same

time, the global monetary easing cycle provides a significant tailwind. The shift to lower interest rates by major central banks is intended to bolster economic activity and investor confidence. However, the risk that inflation proves more stubborn than anticipated could challenge the path of monetary easing.

Enduring structural themes such as AI adoption and the energy transition continue to create compelling investment opportunities, but investors will need to continue to navigate an uneven global economic climate, which will require maintaining a disciplined, diversified, and flexible investment strategy.



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