

What we liked



- Australia's retail sales surged past expectations in June, boosted by strong discretionary spending amid mid-year sales and discounts, with household goods leading the rise. Retail sales rose 1.2% month-on-month in June from a revised 0.5% growth in the prior month, and came in sharply above expectations of a 0.4% growth.
- Economic activity in the US service sector accelerated slightly in June, with the ISM Services PMI rising to 50.8 from 49.9 in May, above analysts' expectations of 50.5. A reading of above 50 marked a return to expansion for activity in the services sector.
- US retail sales experienced a significant rebound in June, surpassing expectations and indicating a slight upswing in economic activity. Retail sales increased by 0.6% in June, beating economist consensus expectations of 0.1%.
- The headline German ZEW Economic Sentiment Index jumped to 52.7 in July from 47.5 in June, beating the market expectations of 50. A positive as it exhibits a potential upward improvement in business sentiment for Europe's largest economy.
- Confidence among Japan's major manufacturers showed a modest recovery in Q4, breaking a two-quarter decline. The Tankan large manufacturing index rose to 14 from 13, slightly exceeding market expectations.

What we didn't like



- While anticipated, no rate was forthcoming from the RBA. Despite this, with inflation data coming in slightly below expectations since, a rate cut is now expected in the August meeting.
- The US Federal Reserve keeps rates unchanged as potential for upside on inflation from tariffs remains.
- A number of tariff levels have been announced by the US administration on major economies such as Japan, European Union and India. While not as high as the upper bands projected in previous announcements, we remain wary of the potential negative impacts of these tariffs on economic activity and company earnings over the coming 6-9 months.
- The number of job openings on the last business day of June stood at 7.43 million, the US Bureau of Labor Statistics (BLS) reported in the Job Openings and Labor Turnover Survey from June. This reading followed the 7.71 million openings (revised from 7.76 million) recorded in May and came in below the market expectation of 7.55 million. While openings remain solid, we are noting some weakness in the US.
- Prices in the UK rose by more than expected in the year to June, pushing inflation to 3.6%, the highest it has been since January 2024. The higher figure for June was unexpected, with economists having predicted the inflation rate would stay at the 3.4% it hit in April and May.
- China's official Manufacturing Purchasing Managers' Index (PMI) dropped to 49.3 in July, as against 49.7 reported in June. The market forecast was 49.7. Manufacturing activity remains in contraction as Chinese policy makers continue to battle to stimulate domestic economic activity.

BASE CASE

Our view of the most likely scenario for markets over the coming months, for which our portfolios are currently positioned.



76% Probability

The global economic landscape remains cautious in the short term, with mixed regional data and heightened uncertainty on impacts of U.S. tariff policies. While corporate earnings overseas have been notably resilient, and generally better than expected, volatility is anticipated as markets navigate significant geopolitical shifts, tariff changes and evolving monetary and fiscal policies globally.

Our forecast of subdued inflation in the first half of 2025 has materialised; however, we expect global inflation (excluding China) to remain elevated compared to the past decade over. This uncertain inflation trajectory could introduce further volatility in the latter half of the year, especially if we begin to see tariff impacts do begin to show up in global inflation data

The U.S. administration's recent tariff announcements have introduced additional downside risks to our base case. Conversely, the proposed "big, beautiful bill" appears more stimulatory than initially forecast, particularly when considered alongside ongoing deregulation efforts. Together, these developments support a constructive medium-term outlook for economic activity, albeit with persistently elevated government deficit risks.

Central banks, especially the U.S. Federal Reserve, face a challenging balancing act. Policymakers must decide between easing financial conditions to support growth and system stability, risking currency depreciation and higher yields, or continuing to tighten monetary policy to combat inflation, with the potential for economic contraction and stress in the bond and banking sectors. The RBA is expected to cut rates in August, which should add further impetus for growth to a domestic economy that remains in growth mode. This should support local company earnings. Overall, the direction taken by central banks on monetary policy is expected to be a critical driver of market performance in the coming months.

We remain flexible in our positioning, with the capacity to shift defensively if needed and maintain some cash reserves to capitalise on any market dislocations. Recent global liquidity growth offers some reassurance, though the pace has been uneven and remains a key variable in maintaining a constructive view on risk assets. With strong demand expected for both new and rollover debt through the remainder of 2025, continued liquidity support is essential to maintain our prevailing positive view on risk assets.

Accordingly, while we remain constructive on global economic activity and risk asset performance—particularly inflation hedges like precious metals—the risks to our base case would increase significantly should the U.S. tariffs be fully enacted or if substantial liquidity injections from the People's Bank of China or the U.S. Federal Reserve fail to materialise, as we expect.

Nonetheless, we anticipate further liquidity injections over the coming months, which should lend medium-term support to financial markets. While short-term volatility is likely to persist, we believe this liquidity environment will be broadly supportive of risk assets through year-end. Structural growth themes, such as spending on AI infrastructure and energy infrastructure build out, are expected to remain supportive of equity markets. While lower interest rates globally along with continued fiscal support would see earnings growth broaden out into other sectors.

This backdrop supports maintaining a positive medium-term bias toward growth assets, albeit with the expectation of continued elevated volatility. In this scenario we would likely look to add further exposure to risk assets and companies leveraged to economic growth and structural growth tailwinds on a pullback. Overall, our asset allocation will retain a pro-growth tilt, underpinned by constructive views on corporate earnings and global economic activity, while tactical decisions will be guided by macroeconomic developments, valuations, and central bank policy.

BEAR CASE

Our worst-case scenario for the coming months, which we are prepared to position for should conditions deteriorate.



10% Probability

Global consumer demand weakens more than anticipated, with the U.S. economy showing signs of slowing and limited recovery elsewhere. If U.S. tariff policies prove more aggressive and enduring than expected, inflationary pressures could rise, potentially reversing the recent global trend toward interest rate cuts. Such developments will likely lead to corporate earnings downgrades, with the chance of a technical recession in either of Europe, the US and Australia some chance. In such a situation significant downside to risk assets is likely as current valuations are historically rich.

A resurgence of banking sector stresses, akin to those observed in March 2023, driven by credit market volatility, could tighten lending standards further. Rising concerns over sovereign debt sustainability may prompt bond markets to demand higher yield premiums, exacerbating financial stress. Any stall or decline in global liquidity growth would compound these pressures, potentially weakening currently robust employment conditions.

Further geopolitical instability may disrupt supply chains and energy markets, intensifying inflationary pressures and forcing central banks to maintain tight monetary policies. Simultaneously, rising wage demand's and housing costs may become embedded, further pressuring corporate margins as input and debt servicing costs rise amid softening demand.

This confluence of tightening financial conditions and elevated inflation could compel central banks to maintain or increase interest rates even as economic activity deteriorates. A premature withdrawal of central bank liquidity could destabilise financial markets, which have come to rely heavily on such support. Coupled with more constrained government spending than currently anticipated, due to elevated debt levels, this would likely erode consumer confidence and spending, especially in the absence of strong wage growth. Such a scenario would see a deterioration of corporate and household balance sheets from their current healthy situation.

In China, continued fragility in the property sector raises the risk of a deflationary debt spiral. If recent stimulus measures fail to support consumer confidence and property prices, high debt burdens may continue to suppress growth. Such a scenario would have negative implications for Australia, given its reliance on natural resource exports to China.

A sudden escalation in geopolitical tensions or a major credit event stemming from excessive leverage in a rising yield environment could trigger a rapid and widespread sell-off in risk assets. In this case, we would move decisively into defensive positioning, prioritising capital preservation through elevated cash holdings and reduced equity exposure. Renewed stress in systemically important global banks could also trigger liquidity events with materially negative effects on global growth.

Should these risks materialise, we would adopt a more defensive strategy, rotating away from equities and into cash and defensive sectors. In a scenario of rapidly rising bond yields, a more selective approach would be required, focusing on companies and industries best positioned to benefit from such a shift. Defensive allocations would likely include increased exposure to healthcare, consumer staples, and utilities, alongside elevated cash reserves.

BULL CASE

Our most optimistic view for markets over the coming months.



14% Probability

In a more favourable scenario, developed economies surpass growth expectations as policy clarity improves. Easing supply chain constraints, improved labour market dynamics, and rising productivity contribute to subdued and declining inflationary pressures. Diplomatic progress leads to shorter and less impactful trade tariffs, while regional geopolitical conflicts remain contained. Additionally, further signs of productivity amongst corporates, through faster deployment of technology advancements (Agentic an example). Such a scenario would be expected to see global economic growth prospects improve further along with upside risk to corporate earnings.

Lower input costs, combined with strengthening demand, drive resilient and possibly accelerating corporate earnings growth. Profit margins remain elevated or improve further, bolstered by the adoption of new technologies such as artificial intelligence, leading to more efficient use of labour and higher corporate profitability.

A shift away from fiscal austerity, characterised by increased government spending, catalyses through faster economic expansion. While this may reintroduce some inflationary risk, nominal growth likely outpaces inflation, creating a favourable environment for risk assets as nominal economic growth accelerates due to deregulation and fiscal stimulus from governments.

In Australia, sustained government spending supports along with rate cuts accelerate domestic economic growth. Globally, coordinated stimulus measures—including recent actions by China and Europe—paired with healthy household and corporate balance sheets, significantly accelerate recovery. Increased leverage, if managed prudently, further amplifies this trend.

Should central banks resume efforts to keep interest rates below inflation and enhance liquidity support, financial markets could see a renewed uptrend. Such conditions would likely stimulate further demand for growth assets in a low or negative real rate environment.

In this scenario, we would maintain a growth-oriented asset allocation with minimal cash holdings. Should leading indicators begin to surprise positively, we would likely shift further toward cyclical sectors that are more leveraged to economic growth.



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