

What we liked



- Australia's central bank cut its benchmark lending rates by 25 basis points (0.25%). The country's benchmark rates are now at 3.6%, the lowest since April 2023, which is expected to help in improving consumer discretionary spending.
- NAB business confidence survey produced a strong reading in July. It continues recent improved readings and is now just above its long run average.
- US consumer price index (CPI) increased a seasonally adjusted 0.2% for the month of July and 2.7% That compared with the respective Dow Jones estimates for 0.2% and 2.8% and the market increased the likelihood of rate cuts in September. All said inflation rates remain above target rates, so confidence in a rate cut remains uncertain.
- China's trade balance shrank more than expected in July, as imports surged unexpectedly while exports came in stronger than expected. Increased exports and imports were highlights indicating some strengthening demand, with Imports jumping 4.1% year-on-year in dollar terms in July, in contrast with expectations of a 1% decline, and picked up from a 1.1% rise in June. China's exports climbed 7.2% year-on-year in July, much more than expectations of 5.4% and higher than the 5.8% rise seen in the prior month.
- Japan's economy expanded faster than expected last quarter, led by solid domestic demand. Gains were led by business investment, which rose 1.3% from the previous quarter, surpassing the consensus estimate of 0.7%.

What we didn't like



- The monthly consumer price index (CPI) in Australia rose 2.8% in the 12 months to July, up from 1.9 % in the year to June, and higher the expected 2.3% increase. Monthly data plays less of a part in determining interest rate policy than the quarterly numbers. Despite this it does raise the possibility of sticky inflation levels inhibiting the RBA from more aggressive rate cuts to support economic activity.
- US Services PMI nearly stagnated in July due to weak demand and rising costs, with businesses starting to reduce their workforce. The index for July was 50.1, falling short of the expected 51.5 and below the previous month's reading of 50.8.
- US wholesale inflation accelerated in July by the most in three years, suggesting companies are passing along higher import costs related to tariffs. The producer price index (PPI) increased 0.9% in July, the largest advance since consumer inflation peaked in June 2022. This measures the change of prices of goods and services of producers, indicating inflationary pressures could remain sticky.
- Retail sales in China grew 5.1% over the year, slower than the 5.9% recorded in March and below analysts' forecasts. While a solid number, it continues to show the challenges Chinese policy makers are having in stoking domestic consumer demand to higher levels after a period of relative weakness.
- Japan's factory output fell 1.6% in July from the previous month, worse than a median market forecast for a 1.0% fall. Separate data showed Japanese retail sales rose 0.3% in July from a year earlier, less than the median market forecast for a 1.8% rise. This exhibits volatility in economic activity, some of which are likely to be continued effects from US tariffs implemented earlier this year.

BASE CASE

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



79% Probability

Markets remain cautiously optimistic—supported by resilient global earnings, fiscal stimulus, and strong liquidity—though elevated volatility is expected in the short term, driven by tariff risks, inflation dynamics, geopolitical shifts, and seasonal patterns.

Our forecast for subdued inflation in the first half of 2025 has proven accurate. Nevertheless, global inflation—excluding China—is likely to remain elevated compared to the past decade. This uncertain trajectory may spark further volatility later in the year, particularly if the effects of tariffs begin to show up in global inflation data.

The US administration's recent tariff announcements have heightened downside risks to our baseline forecast, as they create headwinds for global growth and market sentiment. On the other hand, the "One Big Beautiful Bill"—a sweeping tax and spending package in the US—appears more stimulatory than initially anticipated, particularly when paired with deregulation efforts. Together, these developments support a constructive medium-term outlook for economic activity, though elevated government deficit risks remain a concern.

Central banks—especially the US Federal Reserve—face a delicate balancing act. Easing supports growth and stability but risks weaker currencies and higher yields; tightening curbs inflation but threatens contraction and strains financial systems. In Australia, the Reserve Bank cut the cash rate by 25 basis points in August to 3.60%, its third easing of the year, signalling further cuts may follow depending on upcoming data. This move should bolster domestic momentum and support local company earnings. Overall, central banks' policy direction—likely shifting toward lower rates—will be a critical market driver in the months ahead.

We remain flexible in our positioning—able to pivot defensively and hold cash reserves to seize market dislocations. Though global liquidity has grown unevenly, this provides some reassurance and remains a key factor underpinning our constructive stance on risk assets. With strong demand for both new and rollover debt expected through the rest of 2025, continued liquidity support is essential to sustaining our positive outlook.

We remain constructive on global economic activity and risk assets—especially inflation hedges like precious metals—but our baseline case faces greater risks if U.S. tariffs are fully implemented or if significant liquidity support from the People's Bank of China or the U.S. Federal Reserve fails to materialise.

We expect additional liquidity injections in the coming months, offering medium-term support to financial markets. Although short-term volatility may persist, this supportive liquidity backdrop should remain favourable for risk assets through year-end. Structural growth themes—particularly AI infrastructure and expanding energy infrastructure—are likely to bolster equity markets. At the same time, globally lower interest rates and continued fiscal stimulus should broaden earnings growth across sectors.

This environment supports a pro-growth, medium-term bias toward risk assets, accepting elevated volatility as opportunity. On pullbacks, we will increase exposure to sectors tied to economic and structural growth. Our asset allocation remains tilted toward growth, guided by macro 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.



8% 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.



13% Probability

In a more favourable scenario, developed economies exceed growth expectations as policy clarity improves. Easing supply-chain constraints, stronger labour market dynamics, and rising productivity help drive down inflationary pressures. Diplomatic progress shortens and reduces the impact of trade tariffs, and regional geopolitical conflicts remain contained. Additionally, corporate productivity is boosted by faster deployment of technology advances (with “Agentic AI” as one example). This scenario would further improve global economic growth prospects and provide upside to consensus potential for corporate earnings.

Lower input costs and rising demand are driving robust corporate earnings growth. Profit margins remain elevated or are improving, fuelled by the adoption of new technologies like artificial intelligence, which enhance labour efficiency and boost profitability.

Governments are moving away from fiscal austerity by increasing spending, which is accelerating economic growth. Although this may introduce some inflationary pressures, nominal growth is expected to outpace inflation, creating a favourable environment for risk assets. This acceleration is supported by deregulation and fiscal stimulus measures.

In Australia, increased government spending and recent interest rate cuts are supporting domestic economic growth. While global economic recovery remains fragile, coordinated stimulus measures—such as China's new economic stimulus package —and healthy household and corporate balance sheets are contributing to a significant acceleration in recovery. Prudent use of increased leverage amongst households and corporates further amplifies this trend.

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

We will maintain a growth-focused asset allocation with minimal cash holdings. If leading indicators begin to show positive surprises, we will likely increase exposure to cyclical sectors more sensitive to economic growth.



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