



Commonwealth
Private



August 2025

Market Outlook.

What comes after tariff progress?

Foreword

The unveiling of new reciprocal tariffs with dozens of countries opened the door for markets to consider what comes next on the policy front. Questions remain on the exact landing point for key countries like China, but the fundamental implications of higher tariffs on the economy and earnings are likely to come into focus as agreements continue to crystallise. As it stands, equity markets are pricing a continued de-escalation of trade tensions, moderating interest rates and a solid economic backdrop. Valuation multiples for US and Australian shares ended the month well above long-term averages.

An ongoing Market Outlook theme this year has been our belief that the next five years will look different to the last five years – when a passive approach yielded strong market returns. Our preference for active management revolves around the likely positive impact of AI on a broadening group of companies. The successful application of AI will be subject to differing fundamental earnings outcomes, depending on competitive positioning. We believe that the imposition of US tariffs will be similar – with highly competitive industries struggling to pass on tariffs. This can already be seen with tariff-impacted auto manufacturers, as profits are being hampered.

Despite the need for increased discernment in equity markets, active management should only be pursued by those with an identifiable edge. The concept of having an “investment edge” has been explored by US investor Bill Miller, who believes there are three sources of investment edge: informational, analytical, or behavioural. An informational advantage is when you know something material that someone else doesn’t.

An analytical advantage can arise from taking publicly available information and processing or weighing it differently to others. Machine Learning (ML) is an example of an attempt to apply an analytical advantage across large data sets. Finally, a behavioural advantage can occur when an investor exploits the market’s overreaction to news flow.

In an era of continuous disclosure, maintaining an informational advantage is unlikely, meaning that an investment edge is usually gained through an analytical or behavioural advantage. Behavioural opportunities can arise when there is a break down in market diversity that results in broad based fear or greed driving prices away from fundamentals. Essentially, herding. These behavioural opportunities can exist on a top-down (market wide) or bottom-up (stock specific) basis.

Market behaviour through most of July showed signs of becoming desensitised to tariff news flow, in sharp contrast to the reaction when tariffs were first announced. This was apparent in the volatility index (VIX) which traded below its 10-year average throughout most of July. Sentiment measures like the bull-bear spread devised by the American Association of Individual Investors (AAII) have also witnessed a substantial improvement from deeply bearish levels back in April.

Going forward, elevated equity market valuations further underscore the need to seek active exposures rather than mirror market aggregates. In our opinion, the current environment is conducive to stock-specific fundamental analysis, given the valuation challenges both across and within equity markets coupled with questions around the likely winners and losers – but the application of active positioning should only be done in cases where there is an identifiable edge. We also recognise that the future could take a multitude of paths, so having a mix of style and approach across a portfolio can deliver more durable long-term outcomes.

James Foot, Chief Investment Officer
Commonwealth Private

Global Economics:

Slowing growth

- Trade tensions ease as central banks globally tread carefully.
- Global economic growth has begun to lose momentum.

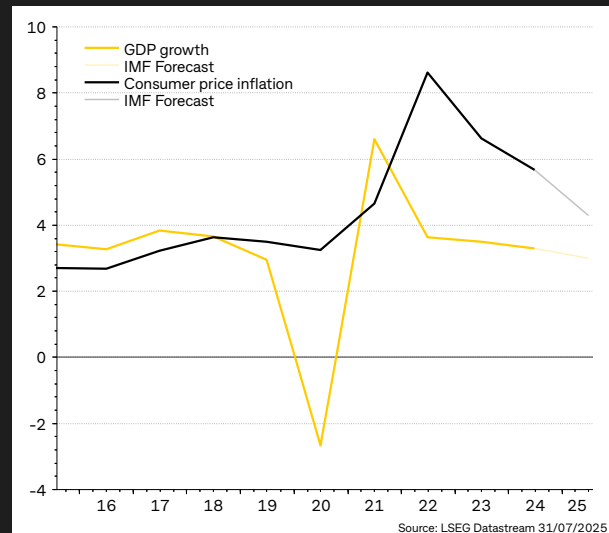
As highlighted in the Foreword, markets stabilised through July as key geopolitical and tariff risks subsided, allowing investor focus to return to core macroeconomic fundamentals. While global growth momentum is softening, inflation continues to moderate across major economies, affording central banks the flexibility to remain measured in their policy settings. The prevailing environment is one of cautious optimism, albeit with significant dispersion in regional dynamics and forward policy signals.

The US economy delivered stronger than expected results in the second quarter, with real GDP rising at a 3.0% annualised rate. This marked a sharp recovery from the Q1 contraction and outpaced consensus expectations of 2.3%. The rebound was supported by improved trade balances and resilient consumer spending, although certain sectors continued to feel the drag from renewed tariffs. Inflation remains elevated but is gradually easing. Headline CPI rose to 2.7% year-on-year in June, while core inflation (excluding food and energy) edged up to 2.9%.

The US Federal Reserve (Fed) left its policy rate unchanged at 4.25%–4.50% for a fifth straight meeting, reiterating its data-dependent approach. Chair Powell emphasised persistent economic uncertainty and inflationary pressures, particularly from tariffs as key considerations, offering no indication of near-term easing.

Global growth & inflation expectations

Annual % change



The European Central Bank (ECB) also kept rates unchanged in July, pausing its easing cycle as inflation stabilised near its 2.0% target. The ECB reinforced its commitment to a meeting-by-meeting, data-driven framework, with signs of easing wage pressures and slower domestic momentum. Despite external headwinds, the Eurozone economy has thus far demonstrated resilience.

In China, GDP growth slowed to 5.2% year-on-year in Q2, down from 5.4% in Q1. While domestic consumption remains soft, industrial production and exports held firm, supported by policy initiatives and a temporary trade truce with the US. Authorities have signalled a more proactive fiscal and monetary policy stance, aiming to stabilise growth in the face of deflationary pressures and external volatility.

Overall, central banks globally are treading carefully balancing softer growth trajectories against easing, but still elevated, inflation. For investors, this warrants a selective and risk-aware approach. Opportunities lie in quality assets, geographic diversification, and sectors likely to benefit from stabilising inflation and supportive, albeit restrained, monetary policy.

Australia Economics:

RBA to resume easing

- While the Reserve Bank of Australia (RBA) held rates in July, the subsequent quarterly inflation, and a cooling labour market, has paved the way for a rate cut this month.
- With CBA forecasting two additional cuts, but now spaced out, this year, this has important implications for key asset classes and sectors including positive impacts for residential and commercial property, and fixed income credit.

The RBA surprised the market by remaining on hold in July, joining the Fed and ECB who also maintained steady rates last month. Communications reinforced a cautious RBA Board seeking to wait and see key inflation data before resuming its rate cutting cycle, with Governor Michelle Bullock highlighting that the official quarterly inflation data (not the monthly CPI Indicator) is watched more closely by the RBA.

To this end, with the quarterly CPI report on 30 July of 2.7% (annual trimmed mean inflation) showing the inflation rate is moderating and within the RBA's 2% to 3% target, the RBA should be able to resume its easing cycle this month.

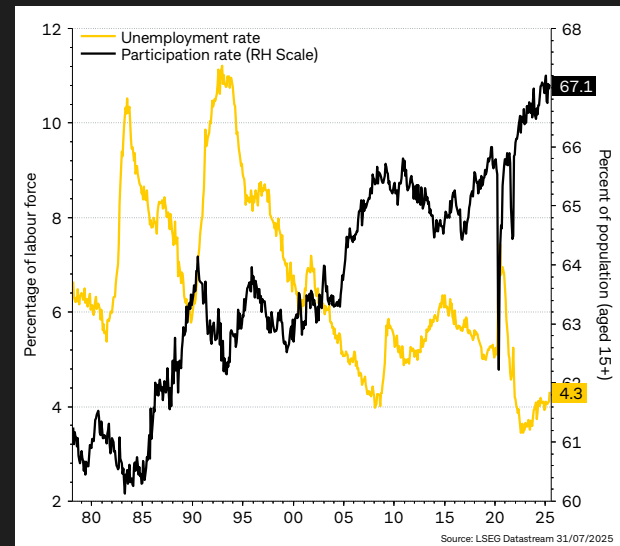
Despite signs that the labour market is cooling from tight levels (as we flagged in our previous Market Outlook), employment increased by only ~2k in June, with the unemployment rate, according to Australian Bureau of Statistics, also rising from 4.1% to 4.3%. While the latter is still a historically low number, it represents a new high that both CBA and the RBA expected this cycle.

Elsewhere, the recent survey-based economic data indicated a modest rebound in confidence and conditions with the CommBank Household Spending Insights index rising by 0.3% in June following gains of 0.4% in April and May.

Overall, with policy-relevant core inflation now within the RBA's target range, early signs

Australian employment and participation rates

Australia's unemployment rate rises



of a slowdown in non market employment (which has been a key buffer for the broader labour market in recent years), and generally subpar economic growth (partly reflecting the continuing uncertain policy and growth environment offshore), there is scope for further easing from the RBA.

To this end, CBA is forecasting two additional rate cuts this year taking the cash rate to 3.35% but now has spaced these out to August and November (absent a real shift lower in economic, notably labour data) coinciding with release of the quarterly inflation data.

Further policy easing from the RBA has important implications for key asset classes and sectors (which will be fleshed out further in this current August reporting season).

Rate cuts are generally supportive for residential and commercial property and fixed income credit, albeit it is likely to result in further reductions in term deposit (TD) rates.

Equities:

Macro still dominates

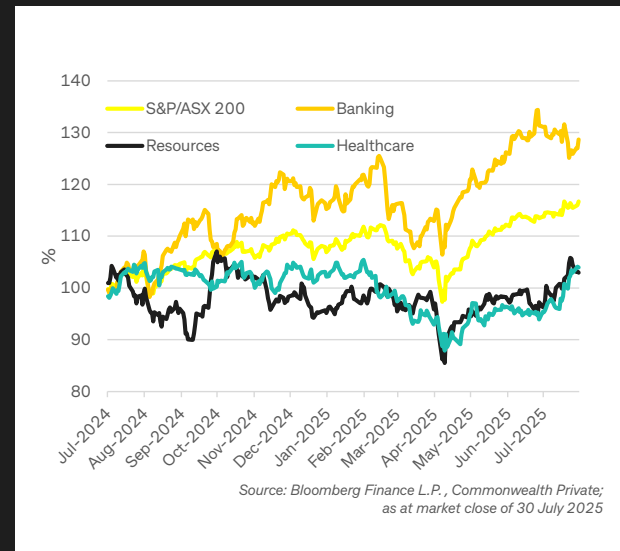
- US equities June-quarter earnings season is one third of the way with mixed yet generally positive results.
- Domestic market is to kick off FY25 reporting season at elevated valuations despite soft earnings momentum.
- Valuation dispersion provides opportunities for alpha generation.

As at 26 July, 34% of companies in the S&P 500 Index have released June-quarter earnings, revealing a mixed but generally positive picture. On one hand, the percentage of S&P 500 companies reporting positive earnings surprises is above average levels (80% vs five-year average at 78%), according to FactSet. On the other hand, the magnitude of earnings surprises is below average levels (6.1% vs five-year average at 9.1%). Sector wise, positive earnings surprises were concentrated in the Communication Services and Financials sectors, which have been the largest contributors to the increase in the overall earnings growth rate for the index since the end of June.

The S&P 500 Index, which ended July trading near record highs, was boosted by the largely positive reporting season discussed above, and also less fear towards the US trade policies as more deals have been signed. The forward 12-month Price to Earnings ratio (P/E) expanded further to 22.4 times (x) as at 26 July (against 22.1x at the end of June and 10-year average at 18.4x). The Australian equity market was also hovering near new highs. However, unlike the positive earnings outlook seen in the US, the S&P/ASX 200 Index houses many mature and cyclical businesses, such as banks and miners, which are expected to deliver limited earnings growth. In fact, at the index aggregate level, the forward 12-month EPS forecast of S&P/ASX 200 Index was largely unchanged from a year ago, as the downgrade in recent months has largely offset the initial improvement during the period, according to the Bloomberg

Varied performances of key sectors on the ASX market (rebased to 28/06/2024)

Total returns



consensus. While the index price has staged a “V-shaped” recovery from the sharp sell-off in April, the earnings outlook hasn’t moved the same direction. Instead, the uncertain business environment has made analysts more cautious on the earnings expectations.

While the Australian equity market valuations look high compared to its trading history, we note there is large dispersion among sectors and stocks. While some good-quality, large-cap stocks have already been bid up strongly and are trading at significant premium to their own history and/or peers, there are pockets of opportunities in other parts of the market, such as mid-cap companies with a positive and/or improving earnings growth outlook.

The upcoming reporting season is not only for companies to showcase their past performance but also to provide insights on various parts of the economy, laying an updated foundation for active investors, like us, to look out for the next opportunities and/or threats. We believe active management of equity portfolios is particularly valuable in current market conditions.

Fixed Income:

US bond yields re-rise on a watchful Fed

- July's re-rise in US bond yields reflects revised forecasts for Fed easing amid sound US economic settings and emerging inflation concerns.
- Global credit spreads are now historically low again, driving our preference for liquid, investment-grade-oriented bonds and portfolios that are actively managed.
- Fixed income investors face key challenges of lower term deposit rates and riskier bank hybrids that are now being phased out.

US bond yields increased in July as investors wound back their expectations for near-term Fed rate cuts given constructive US economic data and trade negotiations but also some tariff-led inflation concerns. Indeed, the Federal Open Market Committee left the Fed Funds rate steady last month, citing inflation and tariffs risk, recent weakness in consumer spending, but an overall solid US household.

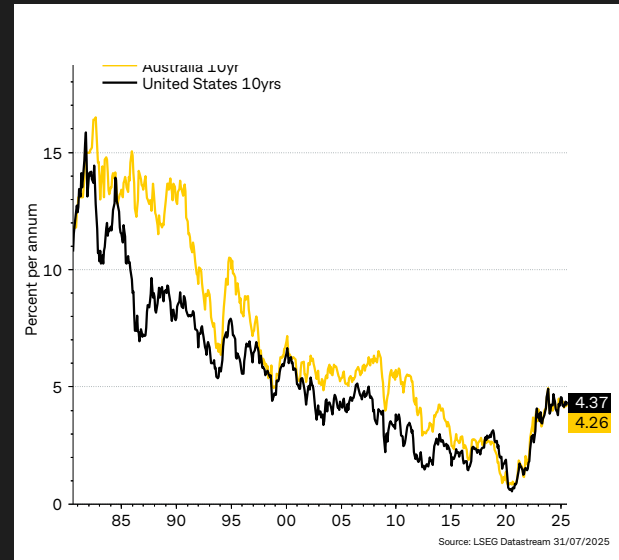
With the RBA unexpectedly remaining on hold at their early July meeting, domestic bond yields saw a similar rising trajectory for most of last month before declining following the weaker than expected inflation data in late-July.

In credit markets, driven by these US macroeconomic factors, as well as strong inflows into USD investment-grade (IG) debt funds, US and global credit spreads continued to drift lower. Having now fully retraced from their 'Liberation Day' wides in April, credit spreads for the IG-based US corporate bond index are now at ~20-year lows and are vulnerable to widening pressure should supportive macroeconomic/credit fundamentals and/or risk sentiment weaken. While AUD IG credit spreads show better relative value, they've reverted below their long-term average.

Historically low credit spreads drive our preference for liquid, IG-oriented bonds and portfolios and the need for our managers in

Long-dated UST yields have risen again

US and AUD 10-year government bond yields



our core and yield fixed income models to remain flexible and dynamic in their portfolio management.

Meanwhile, the latest published data from the RBA confirmed the challenge facing TD holders with six-month retail TD rates now down to 3.05%. While high net worth investors are usually able to source higher deposit rates, wholesale TD rates are materially below the 5%-plus rates previously available. Given this, and with the elevated fixed income portfolio yields on offer, we see merit in moving from short-term cash products into fixed income investments that are moderately higher yielding, but liquid and IG-based, as noted above.

The challenge for fixed income investors does not end there, with APRA reconfirming its decision to phase out riskier bank hybrid capital last month. In practice, this means banks are now further incentivised by APRA to redeem their outstanding hybrids, at or before, the first call date with hybrid investors needing to re-deploy this capital into alternative income-based investments that meet their risk/return profile. This topic was discussed in our [special report](#) dated 16 July 2025.

Real Assets:

Real Assets build on solid foundations

- Real Assets such as Property and Infrastructure can provide long-term investment stability.
- It can also provide a hedge against the inflationary-based erosion of asset value.

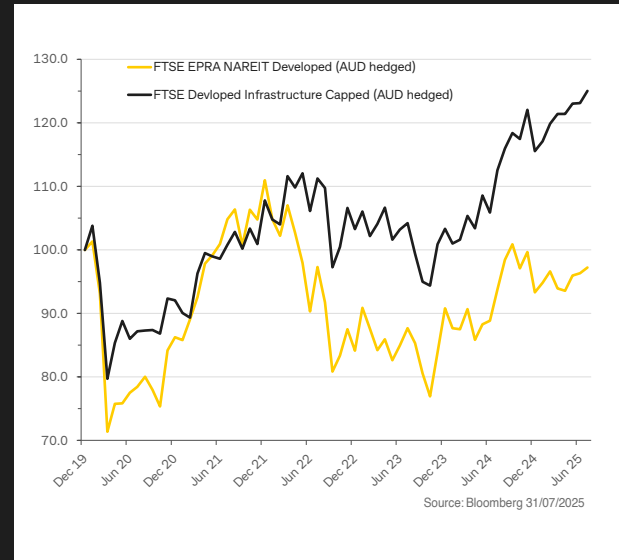
In Australia, investors continue to monitor the commercial property market for confirmation that capital values have stabilised and are returning to capital growth. While the Industrial and Retail sectors have already seen consecutive quarters of growth, capital returns from the Office sector are yet to achieve that milestone.

One factor that continues to hold back valuations in this sector is the supply-demand balance. Over the past few years, fund managers and institutional investors have looked to sell assets to rebalance their portfolios, reduce gearing levels, or to satisfy redemption requests. At the same time, investors have been cautious in deploying new capital, and have sought to buy at significant discounts to book values. Rather than accept such opportunistic bids, some owners held back from selling properties until demand, and valuations, increased again. While a significant amount of this overhang has now been resolved, it has not been exhausted. However, we are cautiously optimistic that fresh capital is returning to the sector, and that this will support valuation levels over the next 12-months.

From a fundamental perspective within the Office sector, CBD locations in Brisbane and Sydney have generally been better supported than Melbourne. This is underpinned by differing drivers per city, with the Brisbane market showing the lowest vacancy rate as well as achieving the highest net effective rental growth. Conversely, the Melbourne Office market continues to have a high vacancy rate despite the significant rental incentives on

Real Asset investment returns

AUD Hedged (Indexed to 100 at 31/12/2019)



offer. Within these markets, modern buildings that provide a high level of tenant amenity are continuing to be well sought after by tenants. With limited supply of such Prime quality buildings expected over the next few years, tenants have been taking advantage of rental incentives and upgrading their leases from older buildings, thereby driving ongoing differentiation between Prime and Secondary quality assets.

Overall, our outlook for direct commercial real estate investing remains positive, driven by current valuation levels, expectations of increased capital inflows, and consensus expectations that the cost of debt finance will decrease as key central banks reduce their target cash rates.

Similarly, we maintain our positive outlook for Infrastructure in 2025. This asset class continues to evolve, bringing new opportunities to market in sectors such as energy transition, digital infrastructure, and waste recycling. It also encompasses the necessary refreshment and upgrade to electricity infrastructure (such as electricity grids and energy storage), which will provide a base for infrastructure investment and returns in the decade to come.

Alternatives:

Long-term return drivers remain intact

- Hedge Funds aim to provide absolute returns with low correlation to traditional asset classes.
- Alternative Credit offers enhanced yields.
- Private Equity offers access to value-added opportunities and participation in developing businesses and technologies.

In July 2025, credit spreads of more-liquid high-yield and lower investment grade alternative credit instruments continued to tighten from their early-April 2025 peak levels, as shown in the chart to the right. This has, in general, assisted these strategies to recover from the mark-to-market performance impact of spreads widening across March and April.

This tightening primarily reflects the abatement of concerns regarding the economic impact of US tariff imposition, particularly in the US, and economic forecasts that are centred around a continued US easing cycle. It's also supported by the ongoing robust demand from investors for portfolio yield enhancement which is of increased importance as central bank cash rates are expected to continue to decline over the remainder of 2025.

Despite this tightening, our near-term outlook for alternative credit assets is stable, and absent any material shocks to the system, we expect credit spreads for high-yield strategies to be sustained around their current levels. Further, we note that market spreads for illiquid direct private loans have not been subject to the tightening described above for more-liquid strategies, and therefore continue to provide a greater measure of yield enhancement.

Overall, we maintain our preference for experienced specialist credit managers which: (a) actively manage a diversified portfolio of investments across multiple credit strategies (such as high yield bonds, corporate loans, and structured credit), and (b) have a strong focus on risk assessment and can demonstrate ongoing below-system asset downgrades and default

High-Yield spreads and discount margins


Basis points



rates. In the current market context this includes preferencing companies that have high-quality stable cashflows, and consideration of the additional risks posed by sectors that are more exposed to changing economic and policy drivers.

We remain cautious regarding private lending to real estate development projects in Australia, as builders and developers continue to digest elevated construction and interest costs, which presents elevated risks to lenders. While this risk has diminished for new transactions which have been underwritten in the current cost-environment, legacy transactions, particularly development projects, have provided challenges for some lenders.

Meanwhile, we continue to see healthy levels of Private Equity transactions. As well as the deployment of fresh capital into primary transactions, there has also been a refreshed interest in PE secondary market transactions. These transactions serve multiple objectives, including allowing institutional investors to lock-in profit on historical transactions and rebalance their portfolios, as well as provide other investors the opportunity to deploy capital into proven businesses – often at a significant discount to their assessed valuation levels.



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