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Portfolio Perspectives

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Key Messages for Investors

- US corporates have so far shouldered most of the costs associated with tariffs.
- While earnings have come down, the Q2 earnings season impressed, with results better than many feared.
- Companies have so far avoided the worst impact of tariffs, helped by three main factors: adoption of a range of mitigation strategies, Artificial Intelligence (AI) activity and a softer US Dollar (USD).
- It's likely that the US consumer will start to pick up a larger share of tariff costs over the coming quarters, but they too, are starting on a solid footing.
- US consumers have been resilient to-date, and with real disposable incomes starting to rise and further rate cuts likely, they should be able to weather the impact so long as they remain employed.
- Policy cross currents continue to complicate the outlook and valuations remain stretched.
- Risks remain broadly balanced from here, with risks to both the upside and downside. Remain close to benchmark.

Who's bearing the cost of US tariffs?

Recent analysis by Goldman Sachs has found that US businesses have so far borne the brunt of the higher costs associated with the Trump administration's tariffs (64%) while US consumers paid 22% and foreign suppliers 14%. While President Trump was furious with the analysis, calling for the resignation of Goldman Sachs' Chief Economist, this view is supported in the data we are seeing in US Consumer Price Index (CPI) numbers as well as import prices for manufactured goods.

US CPI remains sticky (mostly on the services side) but has not materially increased in recent months as a result of tariffs. While it is still early days, with some suggestion that firms are selling down inventories and delaying price increase until later, so far, US consumers do not appear to be paying significantly more for imported goods (aside from a few selected goods such as toys and appliances).

Nor do foreign firms appear to be paying for the cost of tariffs. The change in US import prices for manufactured goods has seen no

material change in recent months, suggesting foreign firms are holding firm on pricing. If foreign firms were bearing the cost, we would expect to see material cuts in import prices for manufactured goods.

If consumers and foreign firms aren't absorbing tariff costs, the burden falls on domestic companies – a pressure that should show up in earnings results.

Resilience in US corporates

With the US earnings season now wrapped up, results came in far stronger than many expected. While earnings have come down in Q2 as US corporates absorb the costs of tariffs, they remain at healthy levels.

Over 80% of S&P 500 companies beat analysts' forecasts, delivering 11% year-on-year earnings growth – an impressive outcome given the tariff headwinds, negative news headlines and softer macro data observed this year. Companies have, so far at least, avoided the worst impact of tariffs, helped by three main factors: companies

have employed a diverse range of mitigation strategies, AI activity and a softer USD.

Companies that have been most directly impacted by tariffs, have adopted several mitigation strategies, including tighter cost controls, inventory build-ups, supply chain diversification and selective price increases. The breadth and width of these approaches has helped shield margins and, so-far, contained broader economic spillovers.

The Mag 7 once again provided outsized support. The Mag 7 comprises 38% of the S&P 500's market capitalisation and continues to post robust earnings growth, close to 26% year-on-year (YoY). AI-driven demand has been a key driver, while tariff impacts on tech have been softened by exemptions (e.g., iPhones, laptops) and production shifts. Companies like Microsoft, with revenue concentrated in software and cloud, remain structurally less exposed.

A weaker USD also gave multinationals a decent tailwind. With the USD down 10% since the start of the year, companies generating significant offshore revenue saw earnings boosted in Q2. Historically, every 1% fall in the dollar lifts S&P 500 EPS growth by about 0.6%, according to LSEG data. With nearly 40% of S&P 500 revenue derived internationally, currency moves were a meaningful cushion.

Importantly, earnings strength appears to broaden beyond mega-cap tech. The "ex-Mag 7" cohort is expected to increase its share of total earnings growth suggesting that the gap is narrowing and recovery is spreading across sectors – albeit unevenly. Materials, industrials, and consumer companies remain sluggish.

The market reaction to these results has been positive, with equities rallying and corporate activity picking up.

While corporates have so far borne the brunt of the tariff impact, we expect that over time, that burden will shift towards the consumer in coming quarters as tariffs embed themselves further in supply chains and pricing structures.

US consumers have also been resilient

Consumer spending data in the US remains healthy and confirms the resilient consumer thematic. The Johnson Redbook Retail Sales Index provides weekly data on 9,000 stores, or 80% of the equivalent official retail sales series collected by the US department of Commerce. The index has not shown any material sign of weakening since tariffs were implemented, if anything, slight improvements have been observed in recent weeks.

US real disposable income has steadied and is now rising, up to 2% YoY in July. Wages and salaries rose 0.6% month-on-month in July while savings rates have also steadied. Add to that the potential for further rate cuts, and consumers have significantly more money in their pockets to support consumption than they did this time last year.

The outlook for consumption does ultimately hinge on the labour market, which has shown some early signs of softening. However, as we have written in prior perspectives, from a starting point of extremely low levels of unemployment, there would need to be a rapid and significant deterioration in the labour market for this to become alarming.

Policy cross-currents & valuations

Tempering our more positive view on micro and macro settings, are a number of tail risks with wide and varied potential consequences. From threats to US central bank independence (which could push long-end yields higher) or the recent Court of Appeals for the Federal Circuit's finding that

the Trump administration overstepped its authority when it implemented tariffs, policy uncertainty remains elevated and prone to sharp reversal in sentiment.

Valuations too, remain stretched, suggesting at best, modest forward-looking returns for the US.

Mixed results in Australia

A final note on the domestic reporting season which has also drawn to a close. While our equity team will have more to say on the matter in our next update, at a headline level, performance was mixed across sectors. Companies leveraged to an improving domestic backdrop and recent rate cuts – particularly retailers and property groups – generally outperformed. In contrast, firms with significant exposure to the US housing market, along with CSL Ltd., struggled, posting disappointing results that triggered sharp share price declines.

Outlook and Positioning

US economic growth is holding up reasonably well at 2.1% YoY albeit, slightly below trend. We expect tariff impacts to be a larger headwind for economic growth in the second half, likely late in the September or December quarter and into next year. And it is also likely that the brunt of those costs will shift from US corporates and onto US consumers in the form of higher inflation.

However, with further rate cuts on the horizon and both US corporates and US consumers starting on solid footing, they should be well positioned to manage the interim period while the macro-outlook starts to normalise.

We remain close to benchmark as we see risks as finely balanced. We see potential for both upside and downside surprises against a backdrop of extended valuations and still elevated policy uncertainty.

Growth Assets	Underweight			N	Overweight		
Australian Equities - Large Cap				●			
Australia Equities - Small Caps			●				
Developed Market Equities - Large Caps				●			
Developed Market Equities - Small Caps				●			
Emerging Market Equities				●			
Global Listed Property					●		
Global Listed Infrastructure				●			
Growth Alternatives				●			

Defensive Assets	Underweight			N	Overweight		
Australian Bonds					●		
Global Bonds			●				
Diversified Income				●			
Defensive Alternatives				●			
Cash				●			

Current Position ● Previous Position ●

Growth Assets

Asset Class	Position	Rationale
Australian Equities - Large Caps	Neutral	Australian equity valuations remain stretched and require a re-rating in bank and resource earnings. Earnings season was mixed at best. Inflation is receding, paving the way for Reserve Bank of Australia (RBA) cuts.
Australian Equities - Small Caps	Slight Underweight	China continues to underwhelm economically as hopes for a rapid, stimulus led recovery have faded. This should disproportionately impact junior miners who make up a large portion of the Small Caps sector vs Large Caps.
Developed Market Equities - Large Caps	Neutral	The Trump Administration's tariff policies are a headwind for growth, but the impacts will be manageable. Economic indicators have moderated year to date, but fears of a severe growth scare are diminishing.
Developed Market Equities - Small Caps	Neutral	Valuations remain somewhat attractive. With US companies forming 63% of the small cap index, tariff policy uncertainty should fade as a headwind.
Emerging Market Equities	Neutral	Emerging market equities are dominated by China, where a policy shift to support consumption and an economy that has recalibrated to be less dependent on the US since 2018 are supported by compelling valuations. However, absent a catalyst, we remain Neutral.
Global Listed Property	Slight Overweight	Attractive subsector valuations warrant an active approach to this sector. Office sector remaining structurally challenged but rental growth and healthy fundamentals are appearing in other areas of the sector (age care, data management, supply chains).
Global Listed Infrastructure	Neutral	With key policy rates lower than this time last year, a key headwind to the sector is gone. Valuations are attractive versus long term averages.
Growth Alternatives	Neutral	Some improvement in the exit environment for private equity. Private credit is offering attractive yields, but spreads remain tight. Global multi-strategy hedge funds that are liquid and can respond to rapid changes in macro conditions and sentiment.

Defensive Assets

Asset Class	Position	Rationale
Australian Bonds	Slight Overweight	Australian bond yields offer good value and provide safety from overseas volatility. Positive supply/demand dynamics further supported by a budget deficit likely to be less than government forecasts.
Global Bonds	Slight Underweight	US fiscal and monetary policy uncertainty is distorting the defensive qualities of Global Bonds. Japan is still in hiking mode.
Diversified Income	Neutral	Floating rate public credit still offers relatively attractive yields.
Conservative Alternatives	Neutral	Gold acts as a risk-diversifier against a further deterioration in economic conditions or escalation in geopolitical tensions.
Cash	Neutral	Cash provides optionality during this volatile period.

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