Perpetual Private | Quarterly Market Update

“Go with the flow”

Navigating a market that is running hot

December 2025

Trust is earned.

Perpetual

Contents

Executive summary

2025 saw yet another year of strong returns for risk-assets as markets were able to shrug off tumultuous geopolitics, valuation concerns and continued elevated levels of conflict around the globe.

If it wasn't already clear, we are in a changed and changing environment, with international norms of the past 80 years, rapidly being upended. Additionally, whilst central banks have largely been moving in lock-step since the early days of the pandemic in 2020, inflation conditions and therefore interest rate outlooks are diverging across geographies.

Against this backdrop, we've seen precious metals reach and exceed all-time highs, as concerns regarding high government debt levels globally and US attacks on institutions (domestic and international), drive investors to seek 'safe haven' assets.

Pleasingly however, equity markets continue to retain a healthy degree of optimism, largely spurred on by the promise of the artificial intelligence (AI) revolution. Indeed, the current bull market has now been in place for over three years, and whilst AI linked stocks have started to slow their ascendancy, the trend is broadening into other segments, either likely to benefit from this new technology or actively supporting it.

As we press into 2026, it seems likely that current trends will continue. Although our sense is that we're closer to the end of the cycle than the beginning, the degree of momentum currently in markets is likely to remain resilient to all but the largest of shocks. As such, we see the environment as one that comes with higher levels of risk, alongside higher levels of return.

In this report, our Special Article **"Literally but not seriously"** delves into the significant changes occurring in international relations and the established world order, before our Economic Outlook **"Don't fight the current"** reflects on investment markets over 2025 and what we'll be monitoring in the year ahead. Should you wish to delve into any one asset class more deeply, page 19 onwards explores each one in greater detail.

Asset class snapshot

Australian equities

Australian equities weakened into year end, with the S&P/ASX 300 declining -0.9%[1] over the December quarter but still delivering a solid 10.7% return for 2025. Investor sentiment weighed on performance, largely due to the Reserve Bank of Australia (RBA) adopting a more 'hawkish' stance towards monetary policy and emphasising its need to return inflation to its target band. Value stocks materially outperformed Growth, returning 3.1%[2] over the quarter compared with a decline of -6.5%[3]. This relative strength held over the full year, with Value up 17.9%, while Growth fell -4.3%, as investors favoured commodity linked stocks and rotated out of Technology and Healthcare names. Large caps fell -1.2%[4] for the quarter, while smaller companies rose 1.8%[5], extending their standout run to deliver a 25.0% gain for the year. Positive sector performance was narrow with Materials being the clear leader, up 13.0%[6] and ending the year up 37.5%. Industrials and Energy delivered modest gains, up 0.6%[7] and 0.9%[8] respectively. Information Technology was the weakest sector, falling -23.7%[9] over the period and -19.1% over the year. Healthcare was similar, dropping -9.5%[10] over the period and nearly -24% for the year. Financial ex-REITs (-1.9%[11]) and Consumer Discretionary (-11.5%[12]) also lagged over the period but remained positive over the course of the year.

International equities

International shares delivered solid gains to close out 2025, returning 2.7%[13] for the December quarter and 13.6% for the full year. The quarter saw persistent trade tensions, alongside a 43-day US government shutdown, ongoing debates about the sustainability of AI-driven valuations and additional rate cuts by the US Federal Reserve. Value stocks (+2.7%[14]) outperformed Growth (+2.1%[15]) during the quarter as concerns regarding AI-linked companies grew, leading to a rotation of capital out of some of the most expensive pockets of the market. Health Care was the strongest performer rising 9.2%[16] as investors repositioned into defensive assets with attractive valuations. Materials rose 5.8%[17] as certain commodities rallied, and Financials (+4.3%[18]) benefited from lower rates. Information Technology and Communication Services posted positive returns of 2.3%[19] and 2.7%[20], respectively, but were notably softer than in previous quarters. Regionally, multiple international markets outperformed US Equities. Performance was led by the UK and Japan, with the FTSE 100 increasing 6.1%[21] and the Nikkei 225 rising 5.0%[22], compared with the S&P 500 and Nasdaq Composite Index posting 1.9%[23] and 2.1%[24], respectively. Despite strong performance earlier in the year, the Hang Seng index declined -4.8%[25] over the quarter.

Real estate

Australian Real Estate Investment Trusts (A-REITs) ended 2026 with mixed results, declining 1.2%[26] over the final quarter but rebounding 2.0% in December. For the year, A-REITs delivered a solid 9.7% return as the property sector continued to normalise post-COVID. The Office sector, however, continues to lag but with many indicators suggesting an improving demand/supply balance, expectations are growing that the worst is now behind it, particularly with many companies pushing employees to reduce the number of days they work from home.

Globally, Global Real Estate Investment Trusts (G-REITs) underperformed, falling 1.3%[27] in AUD terms over the quarter. Germany was the weakest, losing 9.4%[28] in the three-month period and averaging a 10.1% annualised decline for the past five years, pressured by trade disruptions and energy shortages. The US and Eurozone slipped 2.5%[29] and 3.0%[30] respectively, though annual results diverged, with the US falling 5.8%, and the Eurozone gaining 11.9%. Asia led performance, with Singapore up 3.2%[31] for the quarter and 19.1% annually, and Japan posted +2.0%[32] for the quarter and an impressive 29.0% for the year.

Refer to footnotes description on page 33

Fixed income

Global Fixed Income markets navigated a complex environment in Q4 2025, marked by diverging inflation trends and central bank policies across regions. The asset class posted a modest 0.7%[33] quarterly gain as expectations for early 2026 US Federal Reserve rate cuts faded. For the year, returns were largely income-driven (4.4%), supported by growing optimism for a looser monetary policy as the US Fed shifted its primary focus from tackling sticky inflation to supporting a softening US labour market. Conversely, Australia faced persistent price pressures. At the time of writing, markets were assigning roughly a one-in-four chance of a February rate hike by the Reserve Bank of Australia. This hawkish shift ultimately weighed on local bonds, which fell 1.2%[34] in Q4 and delivered just 3.2% for the year. Credit markets outperformed globally, buoyed by tight spreads and minimal defaults. US corporate bonds returned 0.7%[35] for Q4 and 6.5% annually, while Australian credit delivered 1.0%[36] and 5.0% respectively. High-yield securities were standout performers, gaining 2.2%[37] in Q4 and an impressive 9.6% for 2025, reflecting strong investor appetite for risk amid stable credit conditions.

Australian Cash Rate

The RBA held the official cash rate steady at 3.60% throughout the December quarter with a renewed lift in inflation halting the quarterly cut cadence of 2025. The October monthly CPI surprised sharply to the upside, rising to 3.8%[38] year-on-year. This was largely attributed to surging energy prices as state and federal energy rebates ended, combined with a handful of other ongoing housing relating costs. November's monthly CPI was lower at 3.4% but still eluded the RBA's 2-3% target band. Unemployment continued to remain steady at 4.3% in November but is potentially masking other softer underlying dynamics of the jobs market. At the December meeting, the RBA expressed a more hawkish tone than earlier in the year, as the recent data has split views on whether conditions are still mildly tight or close to neutral. Market expectations adjusted accordingly over the quarter, with further rate cuts pushed out and the possibility of rate hikes in 2026 re-entering pricing.

Australian dollar

The Australian Dollar (AUD) appreciated 0.9% against the US dollar (USD) over the December quarter, finishing the year near US$0.67. Trading remained range-bound between US$0.64 and US$0.67, reflecting a lack of conviction to push the currency meaningfully higher or lower, without a clearer macro catalyst. Factors stemming from the US were still the primary driver of currency fluctuations as US fiscal sustainability, trade uncertainty and geopolitical risks weighed on the greenback, although these pressures were partly offset by resilient US growth and improved relative US equity performance later in the year. Domestically, the AUD found support from shifting interest rate differentials. Sticky inflation and a resilient labour market reinforced the RBA's decision to hold rates over the quarter and led markets to price the risk of further tightening in 2026, in contrast to expectations for additional easing by the US Federal Reserve. Commodity prices also provided a stabilising influence, with iron ore holding up better than expected and strength in precious metals, particularly gold, supporting Australia's terms of trade.

Refer to footnotes description on page 33

Special article: Literally but not seriously

Under the black of night and shrouded by clouds, they swept in; the darkness enhanced by a failure of the city's power grid. Scores of aircraft spread across the sky, targeting air defences in precision strikes, creating safe corridors for the slower moving helicopters that would deliver key teams of Special Forces operators into their respective battle positions.

The populace was stunned. They should have been. This operation was highly secretive and highly covert. The success of the mission required it. Fortunately though, intelligence reports had proven reliable and operatives had found a receptive audience of collaborators, many of whom had suffered at the hands of the President's harsh and often vindictive punishments.

Tonight though, the towering strong-man's vulnerability was laid bare. His location leaked, with insiders clearing a path, allowing Delta Force directly into the inner sanctum. Just over two hours after the first explosions lit up the city's skyline, the mission had been accomplished. The team's quarry and his wife had been bundled into awaiting helicopters and were now making quick-time back to waiting naval support vessels.

The passage above sounds like something straight out of a spy book, the likes of which may be penned by John Le Carre or Ian Flemming (of the James Bond fame). It does, however, describe the January 3rd US operation to apprehend Nicolas Maduro, Venezuela's autocratic President.

Despite serious questions regarding the legality of the mission under international law, the operation, whilst audacious, was also effective and brilliant.

In his press conference to announce Maduro's capture, President Trump could barely contain his excitement, breathlessly exclaiming *"if you had've seen what I saw last night, you'd be very impressed"*.

While it is not common, this action is not actually unprecedented as some media organisations might have you believe. Indeed, on the exact same day (January 3rd) 36 years ago, the former CIA informant and shadow leader of Panama, Manuel Noriega was captured and taken to the US to face drug charges (another similarity). Many of Trump's supporters point to this as an example of how Venezuela might ultimately play out.

The Panama case is special. In just a short period of time following Noriega's confinement, Panama transformed into a vibrant democracy, notably one of the most stable in the region. In fact, it is one of the few examples of a democratic state successfully emerging out of the ashes of an authoritarian one.

Closer examination though shows that the only meaningful similarities between the two situations is the capture of a head of state, on drug charges, on January 3rd. Outside of that, Panama is a very different country to Venezuela. Most notable is scale; with Panama only having 3m people compared to Venezuela's 30m. Of course, the level of complexity in transitioning a population of 3m is significantly different to that of a country with 10 times that many.

Our focus here isn't Venezuela. In a meaningful sense, despite the Noriega example, this action taken by the US administration is a signal (not the first) that the paradigm under which we have all operated and existed since the end of WW2, is no more. For good or for bad. For right or for wrong. We are in a time of change.

The don-roe doctrine

It is not the first time we have discussed the changing world order on these pages. What is now clear however, is that our departure from an equilibrium that has seen the planet through an extended period of peace after a devastating beginning to the 20th century that saw two world wars in close succession, leaving tens of millions of people either dead or wounded, is certain.

This isn't to suggest that the new equilibrium point, the new 'normal' so-to-say, will be bad. Nor are we claiming that we will necessarily see an elevated level of conflict (though it is worth noting that the level of conflict is already at post-WW2 highs).

What is now abundantly clear is that the US, at-least under this President, has little interest in a rules-based international order. Indeed, as with tariffs, Trump is positioning the US with a world view that harks back to a time many assumed would remain firmly in the past.

The Monroe doctrine was first articulated during President Monroe's seventh State of the Union address to Congress in December 1823. Set against the backdrop of a European withdrawal from colonies across South America, the approach sought to establish the Americas (or "the western hemisphere" to Monroe's description) as the exclusive domain of the US.

Figure 1 – an early cartoon reflecting the Monroe Doctrine

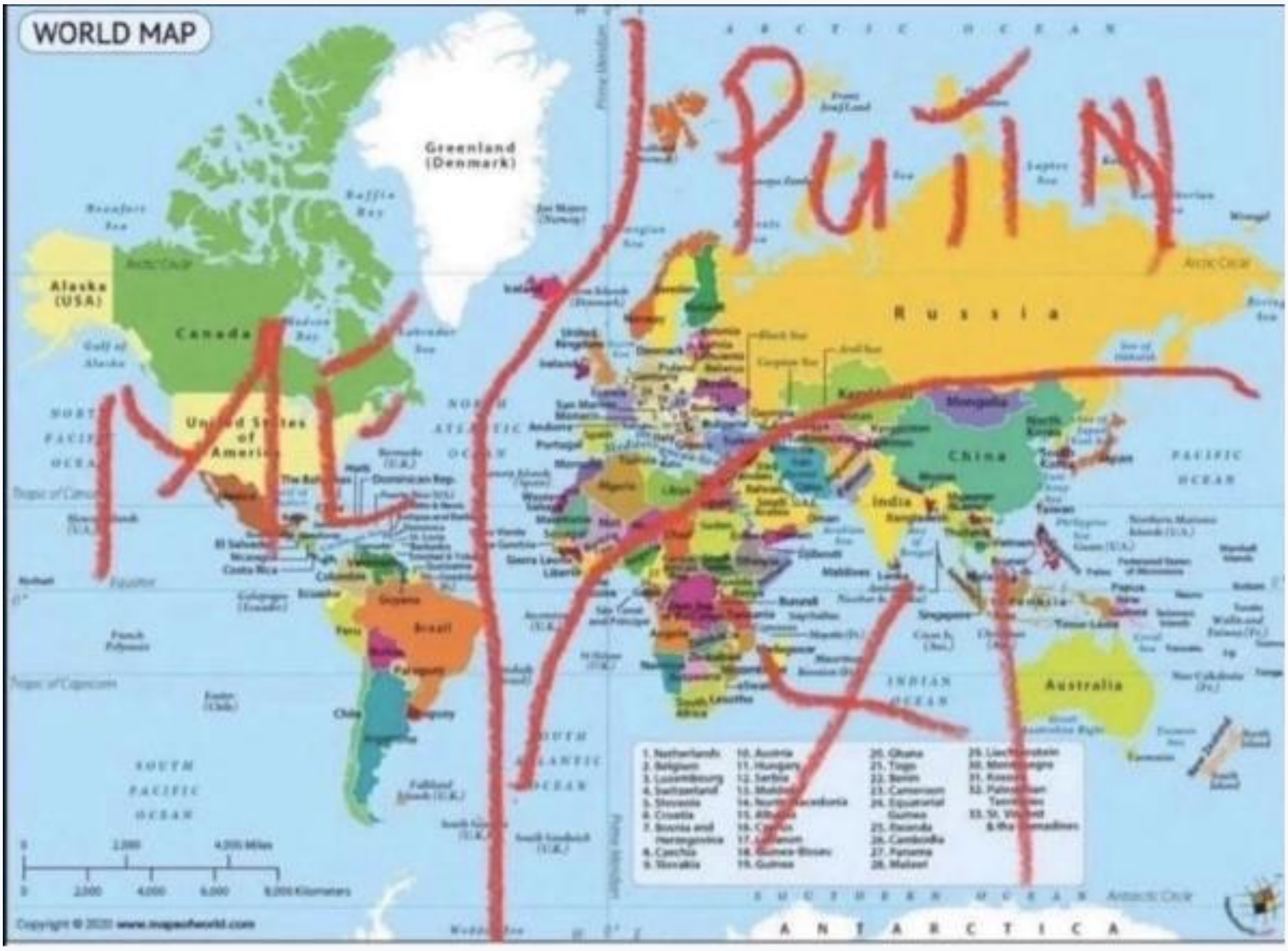
U.S. Department of State, Public Domain; Wikimedia Commons, image ID 179287267

Although the US didn't have the strength to actually enforce this at the time, the concept has persisted as a reoccurring theme in US politics since. Indeed, given the motivations for the foundation of the United States, it's not entirely surprising that the country may have an isolationistic bent. That said, this particular flavour of the doctrine, which has been somewhat reinterpreted over the years, considers the world as being broken into spheres of influence. In each of those spheres, a 'great power' dominates, essentially on a might-is-right basis. Put in simple terms; if you have the biggest, most powerful military – your sphere is yours to rule as you see fit. In the words of key Trump adviser Stephen Miller *"We live in a world in which you can talk all you want about international niceties and everything else, but we live in a world, in the real world… that is governed by strength, that is governed by force, that is governed by power… These are the iron laws of the world since the beginning of time."*

That the US might wish to stay closer to home following the past three decades of disastrous adventurism; most notably in Afghanistan and Iraq, is understandable. That the withdrawal and refocus has been so brash and so bruising, with attacks (mostly verbal) on allies and foes alike, is simply this President's personal hallmark, applied to this 200-year-old concept.

What is more problematic, particularly for investors and traditional allies, is that this approach significantly departs from existing power structures. It leaves Europe needing to race to increase its military strength, with the backing of the US no longer assured and Russia nibbling at its Eastern flank. For smaller countries like Australia, we have gone from being a respected, if junior partner, to a distraction whose Prime Minister was only afforded a meeting with the US president, some 10-months into his term.

Figure 2 – an unattributed spoof of Trump's worldview that has been widely circulated across social media



G-zero

Unmoored from norms of the past 80 years, the world now faces a future where dynamics between the 'great powers' of the world will shape the global security landscape as well as trade. This impacts us as Australians, much as it does as investors. The geopolitical stage has become less safe and ultimately less predictable.

Again; different isn't necessarily bad. As we addressed in a prior Special Article ("MEGA – Making Europe Great Again"), some of Trump's actions appear to have motivated Eurozone countries to stop bickering over farming subsidies and the authorised shapes of columns and focus on defence and cooperation. Polish Prime Minister and recent EU President, Donald Tusk made this point starkly clear when he noted only three days after Donald Trump's inauguration *"Ask not of America what it can do for our security. Ask yourselves what we can do for our own security."*

To this point, the UK having become drunk on memories of past glory, committed an act of great self-harm when it voted for Brexit in 2016. Now with the benefit of hindsight, the idea that standing alone would lead to a more vibrant and entrepreneurial economy has simply not come to pass, nor was it likely to. Indeed, the lack of a deeply logical argument for Brexit is likely the reason that Prime Minister Cameron agreed to holding a referendum on the matter – he never thought it would succeed.

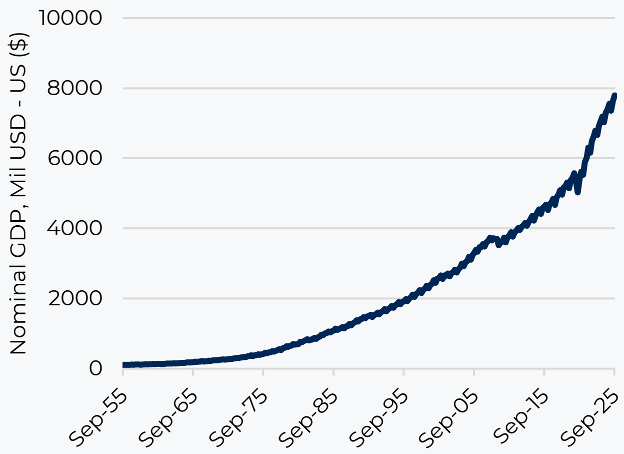
In a seeming acknowledgement that it now recognises it no longer projects the military or economic power it once did, current UK Prime Minister Kier Starmer, is now looking to reengage Europe through what he is describing as a 'reset'.

With Trump's determined erosion of the foundations of, and withdrawal from multilateral institutions that formed in the years after WW2, alliances, cooperation and coordination can no longer be taken for granted. As such, we expect a period ahead where countries that aren't superpowers, particularly those in the traditional 'West' seek to enhance and embrace their alliances with each other, with a view to building power through strength in numbers.

Too long since the last war

"Too long since the last war" is a horrible saying; but it is pertinent to the environment we find ourselves in. It's worth bearing in mind that global economic growth and stability has been impressively strong since 1946. The world has become meaningfully richer, and the amount of conflict has been low against historic standards. The US has enjoyed its own ascendancy to being the sole remaining superpower (at least before China caught up in the past decade), with the only true global reserve currency, along with the most important tech industry and deepest capital markets. That President Trump's "MAGA" movement, so driven by bitterness and envy, in a world where his supporters felt left behind as a result of globalisation, fails to recognise that the country was indeed already "great". Though it would be easy to say that this discontent is misplaced and those supporters didn't really appreciate how good they have it, in fairness to them, much of the growth and therefore benefit of the US' recent boom, did not accrue to them; but instead to the wealthiest members of society. To this point, the Gini coefficient (a measure of the gap between rich and poor) for the US is the highest (worst) for any developed country, in the World Bank's data set.

Figure 3 – US GDP post WW2



Source: FactSet. Data as of 31 December 2025.

This feature though, is not exclusive to the US. With the easy money (low interest rate) period that persisted following the Global Financial Crisis of 2008 driving asset inflation to dizzying heights and acutely expanding the gap in the fortunes of socio-economic groups, a split between the economic outcomes of the "haves" and "have-nots" has led to much anger within populations in much of the developed world. It is this driver that we believe has driven the surge in populism and more extreme flavours of politics around the world with examples in the UK, via Nigel Farage, Germany with the AfD, France with Le Penn and Japan with PM Sanae Takaichi.

The peace dividend will no-longer be paid

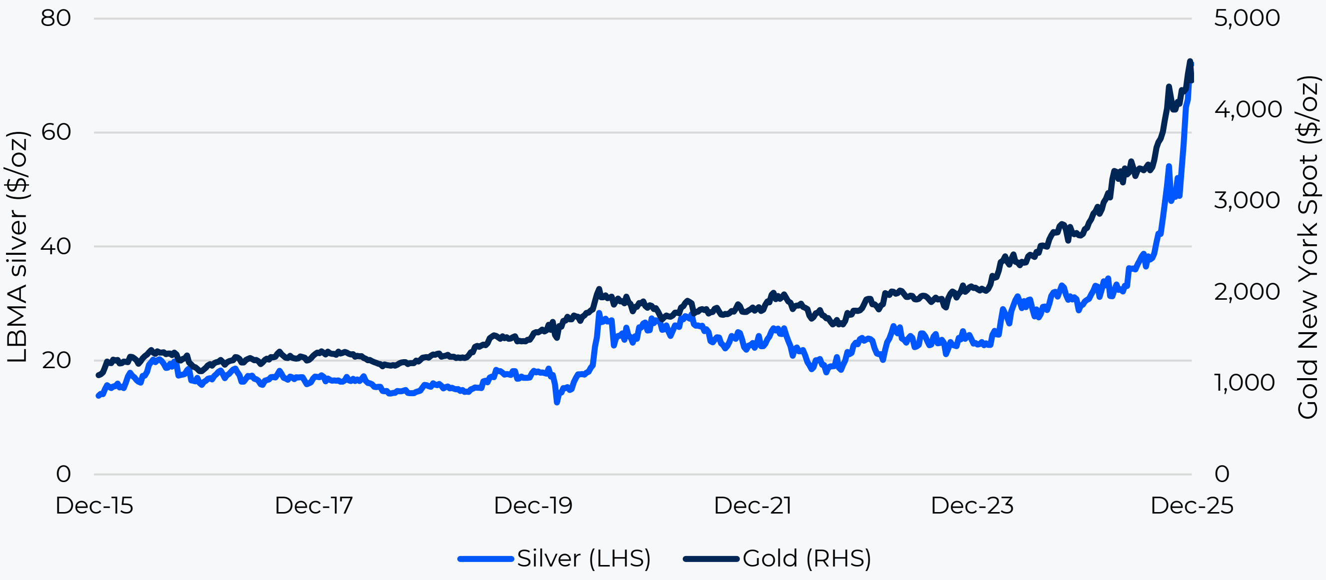
The "peace dividend" is a term used by US President George H. W. Bush and UK Prime Minister Margaret Thatcher to describe the potential for meaningful reallocation of resources away from the military and back into domestic affairs after the dissolution of the Soviet Union. Since, it has come to reflect the idea that a lack of conflict releases resources for more positive and constructive uses. It's fair to say that this is over and as societies, we will again need to maintain higher levels of military readiness.

Not much can be gained by fear. Donald Trump will continue to dominate headlines because that is his nature. Instead of reacting, such as moving investment away from US assets or avoiding investment more generally; simply acknowledging that we are now investing amongst a different set of characteristics is an act of strength.

For investors there are 3 key areas of focus that we think will be key in adapting to these new conditions.

- Rule of law: This is a tough one but it is probably the most obvious. The 'rule of law' has been diminished under this President in favour of the law of the jungle. Where investing in or with any exposure to the US, consider whether that company or strategy is politically aligned with the administration. Those who fall afoul of Trump's ire, will invariably face higher risks and impediments to business, than those who 'kiss the ring'. Investing in traditional Western economies outside the US can further balance this risk, with many areas showing significant valuation discounts to their US peers.
- Currency effects: Prior to 2025, the US dollar was the undisputed heavyweight currency of the world. "If in doubt, just hold it in USD" was often the phrase touted by investors. With the ongoing and escalating attacks on the Federal Reserve and the ever-growing levels of US debt, USD no longer bares the shine it once had (see chart on the following page – this has been a strong driver of demand for gold, and more recently, silver). USD like much with the US these days, can no longer be relied upon. Instead, currency should receive far more consideration within investment strategies, particularly with US equities, which are becoming increasingly attractive on a hedged basis.

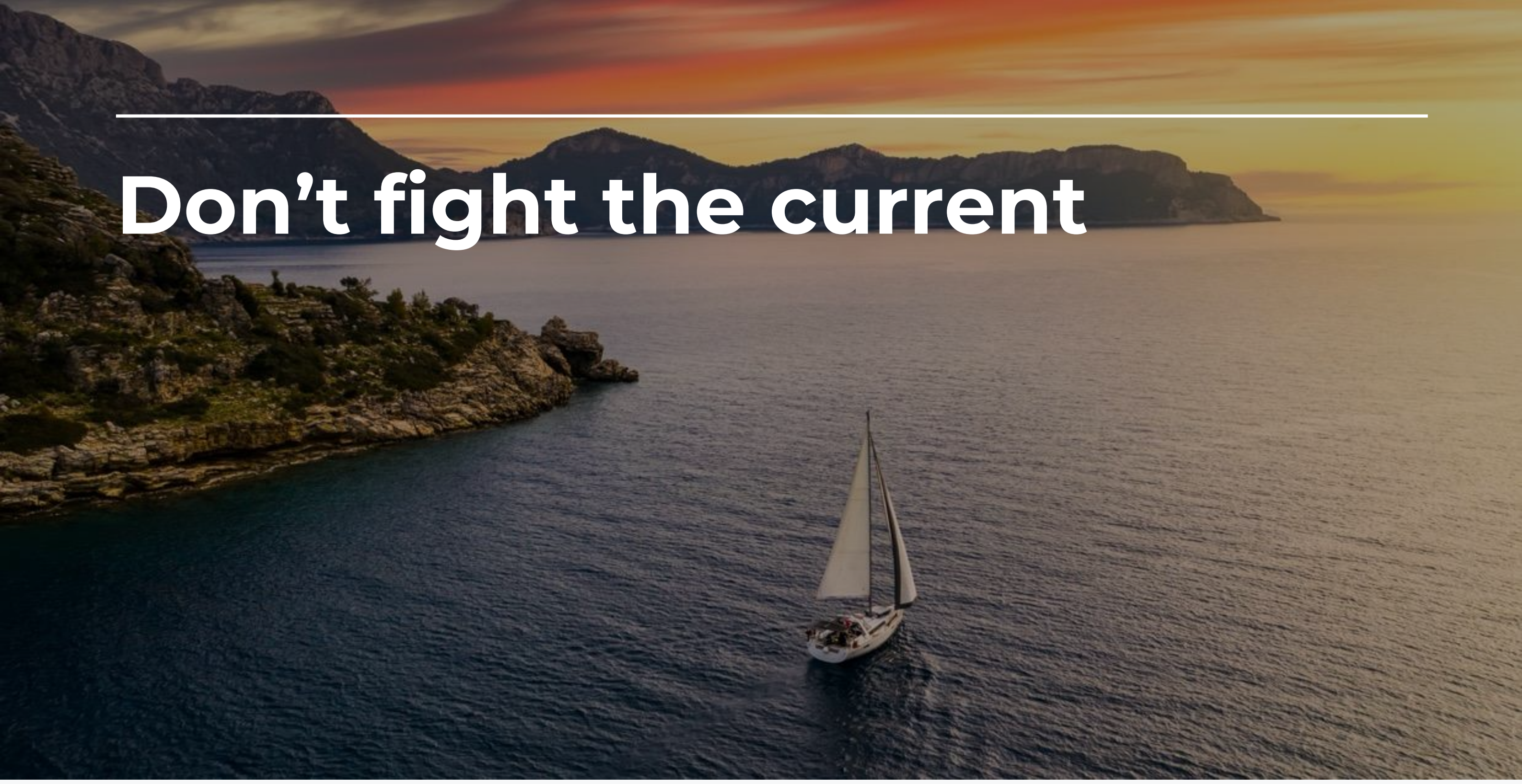
Figure 4: Gold and silver (USD) – 31 December 2025



Source: FactSet. As of 31 December 2025. Past performance is not indicative of future performance.

- Avoid concentration: Markets, particularly as a result of the US tech sector, have become extremely concentrated on just a few stocks. Though we expect it likely for them to continue in the short term, it is sensible to balance this with diversification into other sectors and regions. As we have less idea of where the next shock might appear and how it might play out, it is prudent to ensure the impact will be minimised by spreading risk widely.

In closing, the world has changed. This is neither a good thing nor a bad thing – it should simply be acknowledged and the appropriate adjustments made. As active investors, we see opportunity in such change and are doubling our efforts to position for the best possible outcomes in the years ahead. It might not be a smooth ride but we expect that hard work and dedicated diligence will be strongly rewarded in the short to medium term.



Don’t fight the current

Navigating a market that keeps running hot

As 2025 drew to a close, the equity bull market quietly marked its third full calendar year. The much-anticipated Santa Claus rally failed to materialise, but its absence did little to alter the broader picture. For a third consecutive year, both Australian and global equities delivered double digit returns, comfortably above long-term averages, even if 2025 proved to be the weakest of the three.

Heading into 2026, it is clear that markets have continued to reward optimism over caution. Volatility has been subdued, consistent with the period following “Liberation Day”, and financial conditions are broadly supportive. Impressively, risk assets have absorbed a steady stream of geopolitical and policy uncertainty with limited disruption. Global economic growth has slowed but not stalled, corporate earnings remain resilient and have begun to broaden beyond a narrow group of market leaders, and monetary policy across most major economies now appears accommodative rather than restrictive. Valuations remain elevated, particularly across parts of the AI ecosystem, yet the conditions that typically bring bull markets to an end are not clearly in place. There is an old saying that bull markets do not die of old age; they must be killed (by a catalyst). To date, no such catalyst has emerged to decisively halt the market’s advance.

The past three years have rewarded investors who aligned with the prevailing trend, as the market's defining characteristic has been its willingness to look through risks. Those positioned for an imminent reversal have been repeatedly forced to reassess as upward momentum remains firmly intact. This doesn't suggest risks are absent, but rather that fighting the current has been a costly strategy.

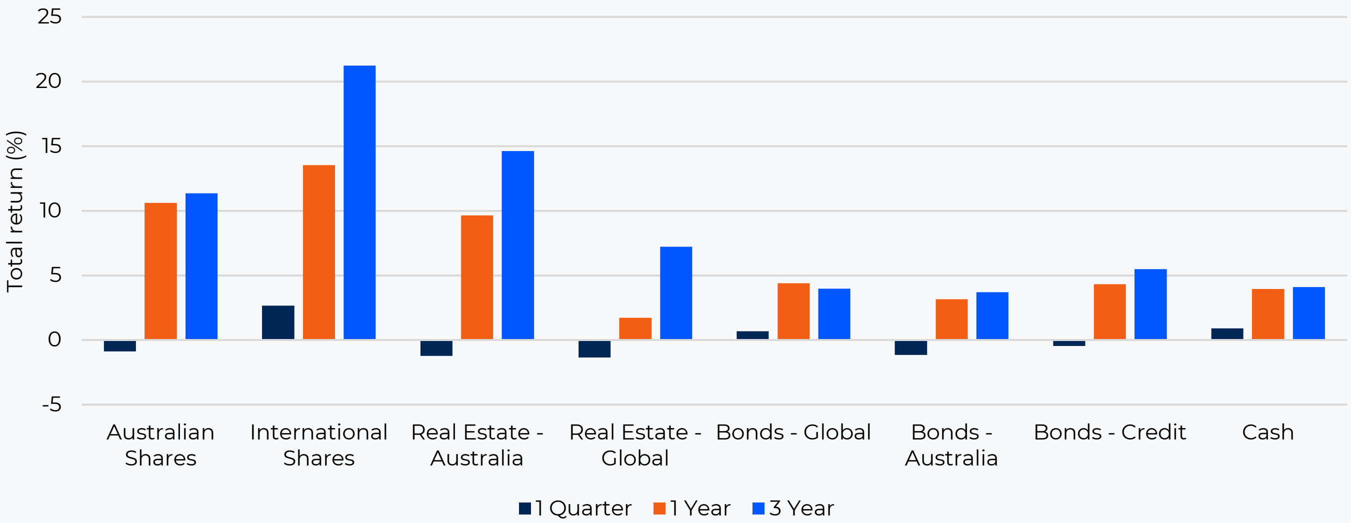
In this Quarterly Market Update, we review the key drivers of the final quarter of 2025 and the year more broadly, assess why the expansion may continue into 2026, and examine the risks that could ultimately change the direction of travel.

2025 recap

If the early years of this bull market were defined by a narrow advance led by a small group of US technology stocks, 2025 marked a clear shift in leadership. Returns once again exceeded long-term expectations, but the composition of those returns changed meaningfully. Market dispersion increased, diversification mattered more, and performance was no longer dominated by a single theme or region.

Figure 5 highlights the breadth of asset class returns in AUD terms. Equities remained the primary driver of performance, but bonds, credit and real assets also contributed in a material way. This occurred against a backdrop of slowing but resilient growth, easing monetary policy and broadly supportive financial conditions.

Figure 5: Annualised asset class returns (AUD) – 31 December 2025



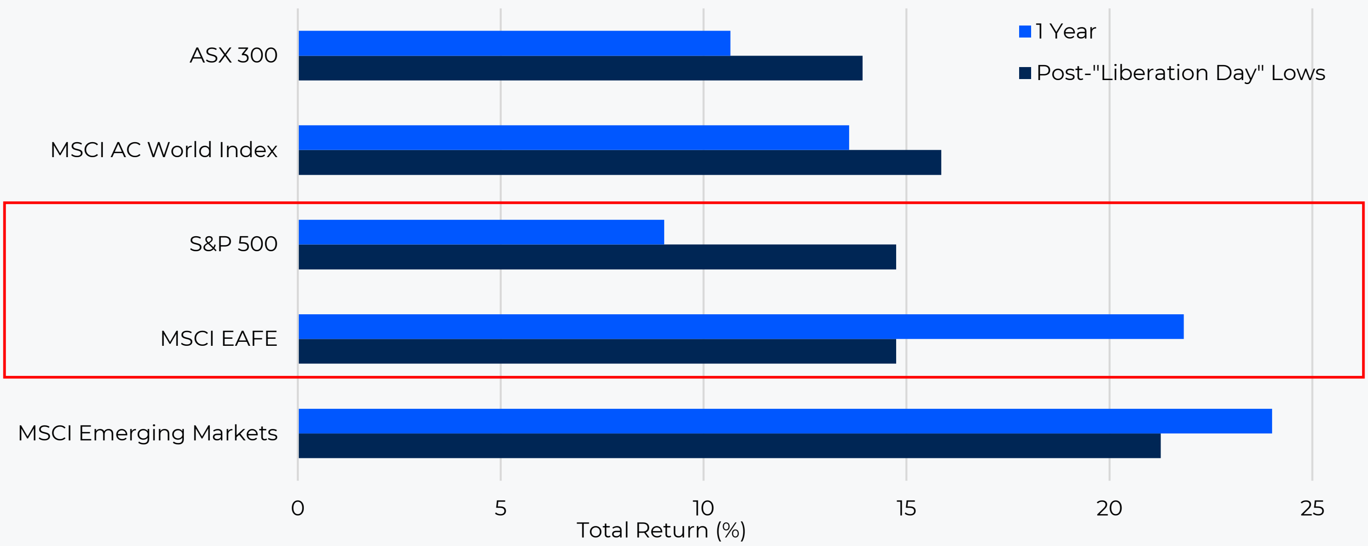
Source: FactSet, Returns are in AUD. As of 31 December 2025. All returns are in AUD. Past performance is not indicative of future performance. Indices: Australian Equities: ASX 300; International Equities: MSCI ACWI (unhedged); Real Estate – Australia: ASX 300 / A-REIT, Real Estate – Global: FTSE EPRA Nareit Global, Bonds – Global: Bloomberg Global Aggregate, Bonds - Global Credit: Bloomberg Global High Yield, Bonds – Australia: Bloomberg AusBond Composite (0+Y), Bonds - Australian Credit: Bloomberg AusBond Credit (0+Y), Cash: Bloomberg AusBond Bank Bill

A shift in regional leadership

For the first time since 2017, International equities outperformed the US market. Developed markets ex-US & Canada (as measured by MSCI EAFE) and Emerging markets both delivered stronger returns, driven by valuation re-rating in cheaper markets, improved earnings momentum and a weaker US dollar.

However, this outperformance was heavily front-loaded with much of the outperformance occurring in the first quarter, prior to the April "Liberation Day" tariff announcements. From the post-tariff lows, regional performance converged, with markets largely moving in sync. US mega-cap technology stocks, particularly those linked to AI, led the recovery and reasserted their influence on global indices through the remainder of the year.

Figure 6: Equity market returns (AUD) – 31 December 2025

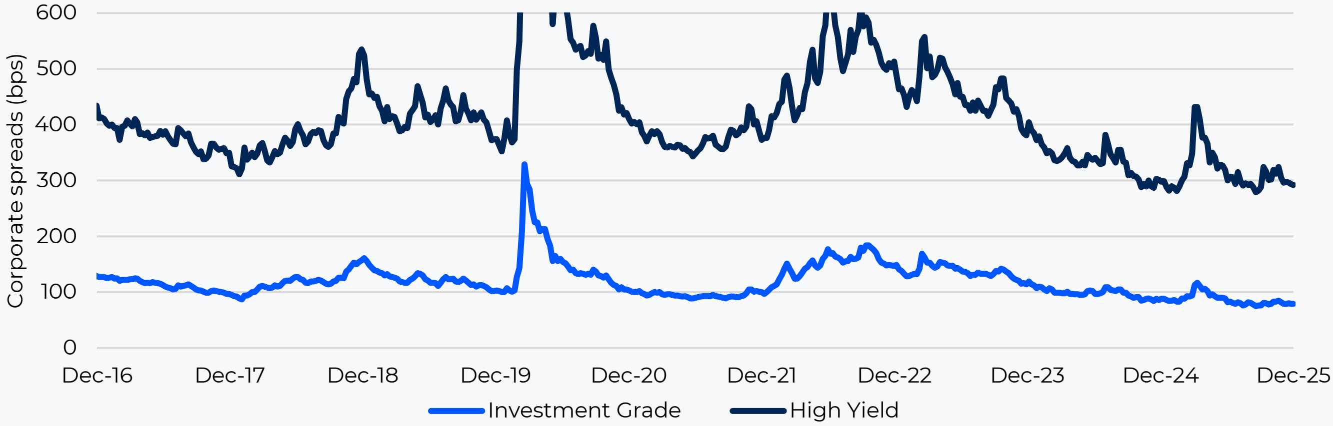


Source: FactSet, Returns are in AUD (unhedged). As of 31 December 2025.Past performance is not indicative of future performance.

Credit and fixed income resurgence

Fixed income and credit also played a constructive role in portfolios. Investment grade and high yield spreads tightened through the year, signalling limited concern about systemic financial stress. Despite most major central banks across the globe loosening monetary policy, including the US Federal Reserve, who cut the Fed Funds rate to 3.50–3.75 per cent by year-end, all-in yields remained attractive relative to the post-GFC era. For investors, 2025 reinforced the role of bonds as both a source of differentiated return as well as being a diversifier against equity market beta.

Figure 7: Corporate Yield Spreads – 31 December 2025



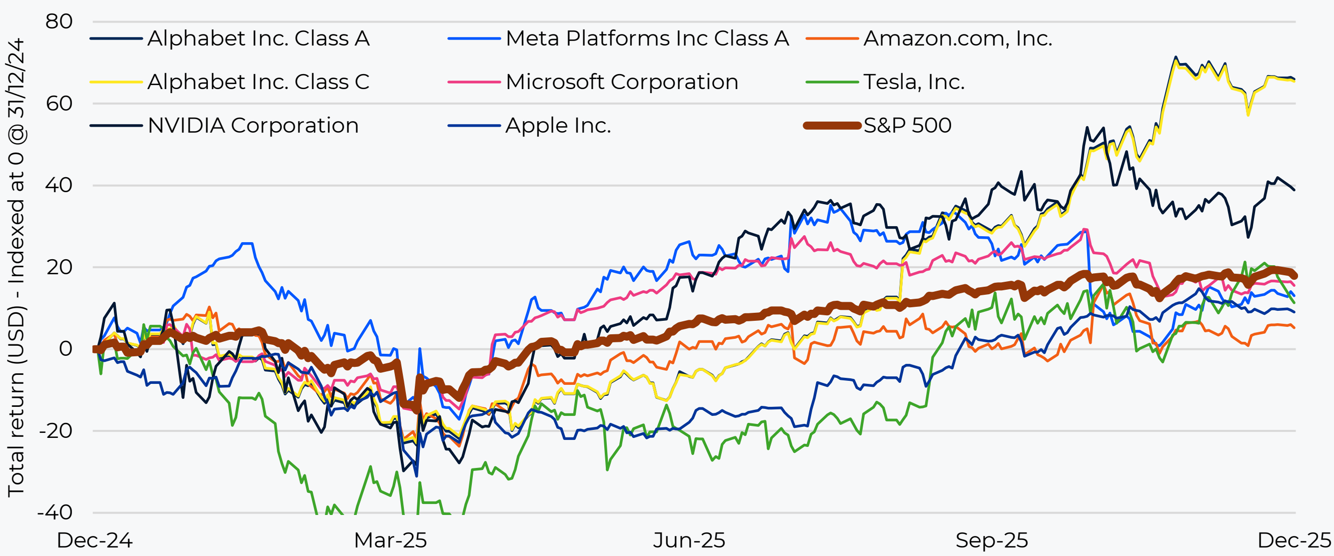
Source: FactSet, Investment Grade: ICE BofA Global Corporate Index, High Yield: ICE BofA Global High Yield Index. Data as of 31 December 2025.

Magnificent seven dispersion

Another defining feature of 2025 was the growing dispersion within the Magnificent Seven. After years of lockstep outperformance, returns within the group diverged sharply. Nvidia, widely seen as the standard bearer for the AI theme, ranked only 75th among S&P 500 constituents for the year. While its size meant it remained the largest contributor to index returns, its share price consolidated through much of the fourth quarter as investors questioned the returns on massive AI infrastructure spending.

Only two of the seven stocks outperformed the S&P 500 in 2025, down from six in 2024 and all seven in 2023. This marked a clear shift away from the one-way trade that had defined earlier years and underscored the growing importance of stock selection within AI-linked exposures.

Figure 8: Magnificent seven vs S&P 500 total return (USD) – 31 December 2025



Source: FactSet, Returns are in USD. As of 31 December 2025. Past performance is not indicative of future performance.

Robust economic conditions

Asset class returns were strong across the board largely because, despite all the geopolitical noise, macroeconomic conditions remained supportive. The global economy extended its soft-landing phase, with growth moderating but remaining resilient. Earlier rate hikes continued to show limited transmission into the real economy, and with most central banks having now cut rates several times, monetary policy is largely seen as being accommodative at their current levels. Consumer spending held up, labour markets remained relatively robust and tight compared to long-term historical trends despite some softening, and earnings growth proved stronger than expected.

A key contributor to this resilience was the AI-driven capital expenditure cycle. According to J.P. Morgan's Eye on the Market, technology sector investment accounted for 40–45 per cent of US GDP growth over the final three quarters of 2025, up from less than 5 per cent just two years earlier. To put some numbers behind it, spending by the four largest hyperscalers (Microsoft, Alphabet, Amazon and Meta) is estimated to have exceeded US$1.3 trillion since late 2022, creating a meaningful floor under growth even as other sectors have shown signs of slowing.

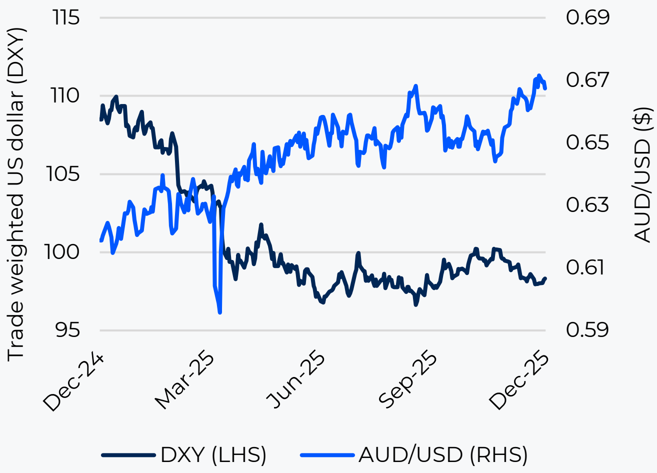
Heightened geopolitical risk

As explored in more detail in this Quarterly Market Update's special article, titled "Literally but not Seriously", geopolitical risks were an ever-present backdrop to 2025. Investors navigated prolonged policy uncertainty, including the longest US government shutdown on record (43 days) and "Liberation Day" tariff announcements. However, these shocks failed to dent enthusiasm. As financial journalist Liz Hoffman observed, *"markets kept climbing like a teenager with noise-cancelling headphones, oblivious to the chaos around them."*

These heightened risks, combined with a weaker US dollar and cuts to the Fed Funds rate, supported strong gains in precious metals, with gold and silver being the clear winners, benefitting from both safe-haven demand and central bank diversification.

Notably, the dollar declined by around 9 per cent on a trade-weighted basis (DXY) over the full 12 months, marking its fourth-worst annual performance in 30 years. Most of this decline was concentrated in the first half of the year when the currency failed to perform its traditional safe-haven role during the "Liberation Day" sell-off. While shifting interest rate differentials also played a part, relative equity and bond performance was also a key driver, with the US dollar falling sharply as US equities and US bonds underperformed early in the year, but stabilising as US relative performance improved in the second half.

Figure 9: Trade weighted dollar (DXY) vs AUD/USD – 31 December 2025



Source: FactSet. As of 31 December 2025. Past performance is not indicative of future performance.

2026 outlook

As markets enter 2026, the debate is no longer whether risks exist, but whether they are finally sufficient to change the market's direction of travel. In our view, the starting point for the year ahead is one of continued, though likely more volatile, support for risk assets. Growth is slowing but not stalling, financial conditions remain broadly accommodative, and earnings are proving more resilient and are expected to broaden out to other sectors and regions over the coming year. Against this backdrop, it does raise the threshold required to derail the 'melt up'.

Tailwinds

Momentum and economic resilience

Despite trade policy uncertainty and political disruption in the US, core indicators across consumer spending, services activity, business investment and employment remains robust against long-term trends. Bloomberg consensus forecasts global real GDP growth of 2.9 per cent in 2026, modestly below the ten-year average of 3.1 per cent, but consistent with continued expansion rather than recession.

A key concern is that the US labour market has softened, with unemployment around 1.1 per cent above its cycle low, a level that has historically always resulted in a recession. Importantly though, the recent uptick has been driven largely by an increase in labour supply rather than fall in demand. At the same time, real wage growth continues to support consumption, particularly among lower-income cohorts, while business investment remains underpinned by the AI-led capital expenditure cycle.

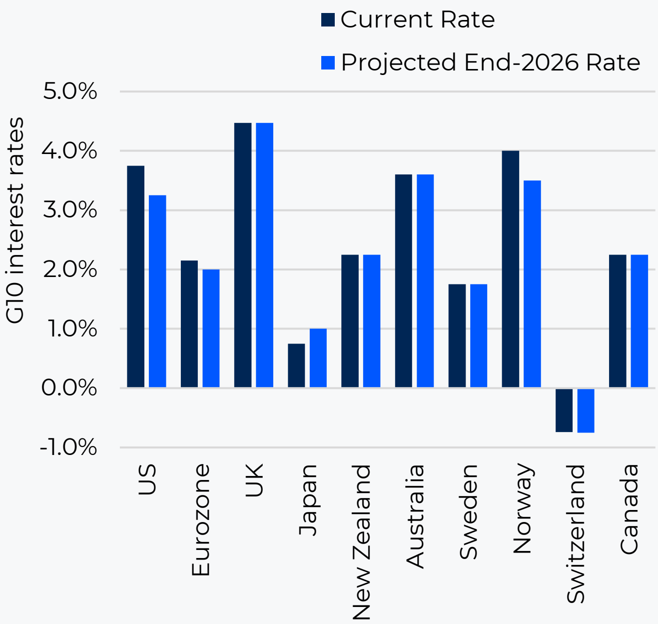
Monetary policy: Still accommodative, increasingly uneven

Against this positive backdrop, global monetary policy continues to lean dovish. The US Federal Reserve has already delivered substantial easing, and markets are pricing around 50 basis points of additional cuts in 2026, an outcome that may prove optimistic if inflation remains sticky. Even so, policy settings are arguably still accommodative at their current levels, and history suggests that fighting the Fed has rarely been a smart strategy for investors.

As shown in Figure 10, outside the US, future policy paths are looking increasingly uneven. The European Central Bank appears close to the end of its easing cycle, while the Bank of England sits near neutral. The Reserve Bank of Australia stands apart, with inflation re-accelerating and domestic demand holding firm, leaving the RBA widely expected to resume tightening in 2026. Japan is another outlier, where modest rate increases are likely to be offset by an expansionary fiscal agenda.

For investors, this divergence reinforces the case for geographic diversification, but it also raises the likelihood of currency volatility and shifting capital flows.

Figure 10: Current G10 interest rates and year-end projections

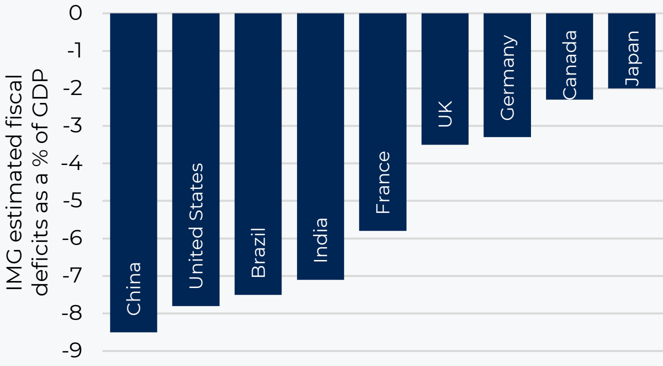


Source: FactSet. Projected End-2026 Rate is FactSet Economic – Median Broker Estimate. Data as of 31 December 2025.

Loose fiscal policy

Fiscal policy will likely add another layer of support, particularly early in the year. In the US, the One Big Beautiful Bill Act (OBBBA) is expected to lift GDP by close to a full percentage point through spring tax refunds and incentives for business investment and R&D. Concerns around fiscal discipline have faded, with bond vigilantes conspicuously absent despite widening deficits. Beyond the US, Germany's decision to deploy stimulus equivalent to 1.5 to 2.0 per cent of GDP marks a significant shift in Europe's policy stance, while Japan is pursuing a similar path (note the chart on the following page does not include the recent Takaichi administration ¥21.3 trillion (~3.5% of GDP) fiscal stimulus package). Across the G20, roughly half of major economies are expected to be stimulating simultaneously, and almost all will be running large fiscal deficits, a rare alignment that should help bolster global growth.

Figure 11: Estimate 2026 fiscal deficits



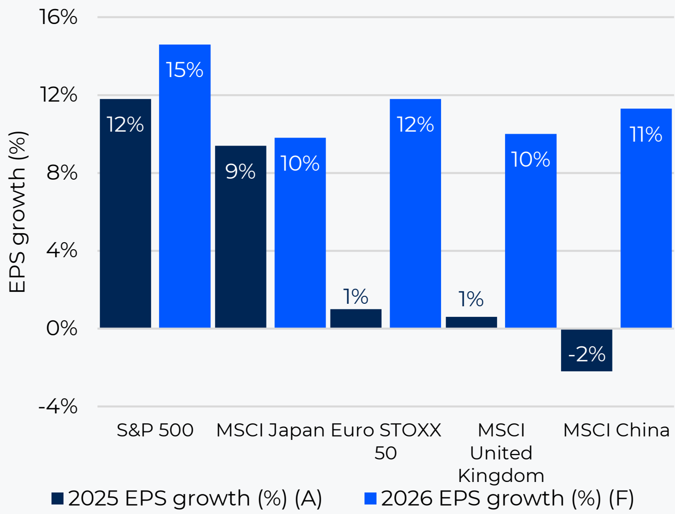
Source: IMF. October 2025 World Economic Outlook. Note: Japan's expected fiscal deficit estimate prior to the election of Sanae Takaichi as PM. Japan's fiscal deficit has become more stimulative post the publication of the report

Earnings and AI: broader, but more selective

Earnings, as always, and AI remain central to the outlook, though the market appears to have entered a more selective phase. Major US technology firms are expected to maintain elevated investment through 2026, with capital expenditure among the largest hyperscalers projected to remain near record levels as the AI infrastructure build-out continues. Importantly, this spending is no longer confined to the technology sector. Demand is flowing through to power generation, utilities, industrial automation and data infrastructure, extending the earnings support across a broader part of the economy.

This is reflected in forward earnings expectations, where in 2026, earnings growth is forecast to broaden meaningfully, with all eleven MSCI All Country World GICS sectors expected to deliver positive growth. In addition, this broadening is not expected to remain US-centric, as shown in the figure 12 above. Earnings growth in Europe, Japan and Emerging markets is projected to accelerate and converge toward US levels, supported by fiscal stimulus, improving domestic demand and structural reforms. If realised, this shift would mark a meaningful structural change from the narrow earnings leadership that defined earlier stages of this cycle.

Figure 12: Earnings growth expected to go global in 2026



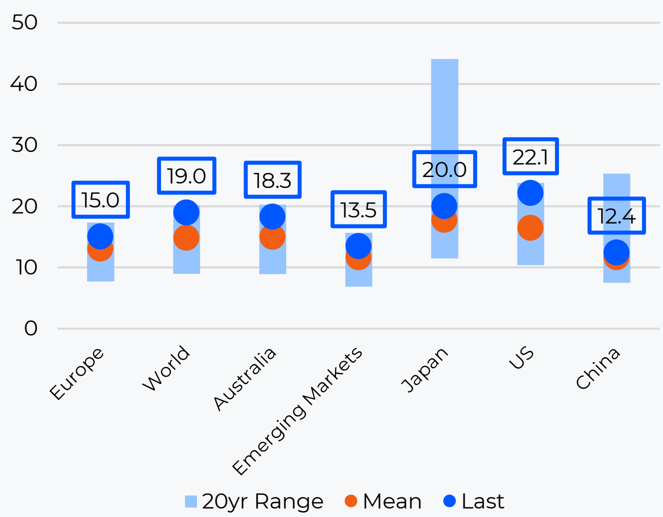
Source: FactSet. Data as of 31 December 2025. Past performance is not indicative of future performance.

Headwinds

Lofty valuations

Valuations remain one of the clearest headwinds. Equity markets, particularly in the United States and Australia, are trading well above long-term averages. Current pricing assumes continued earnings growth, broadly supportive policy settings and an orderly economic slowdown. With little margin for error, even modest disappointments risk being amplified, especially in markets where expectations are already stretched.

Figure 13: Valuations are high - Next twelve months (NTM) P/E 20yr average

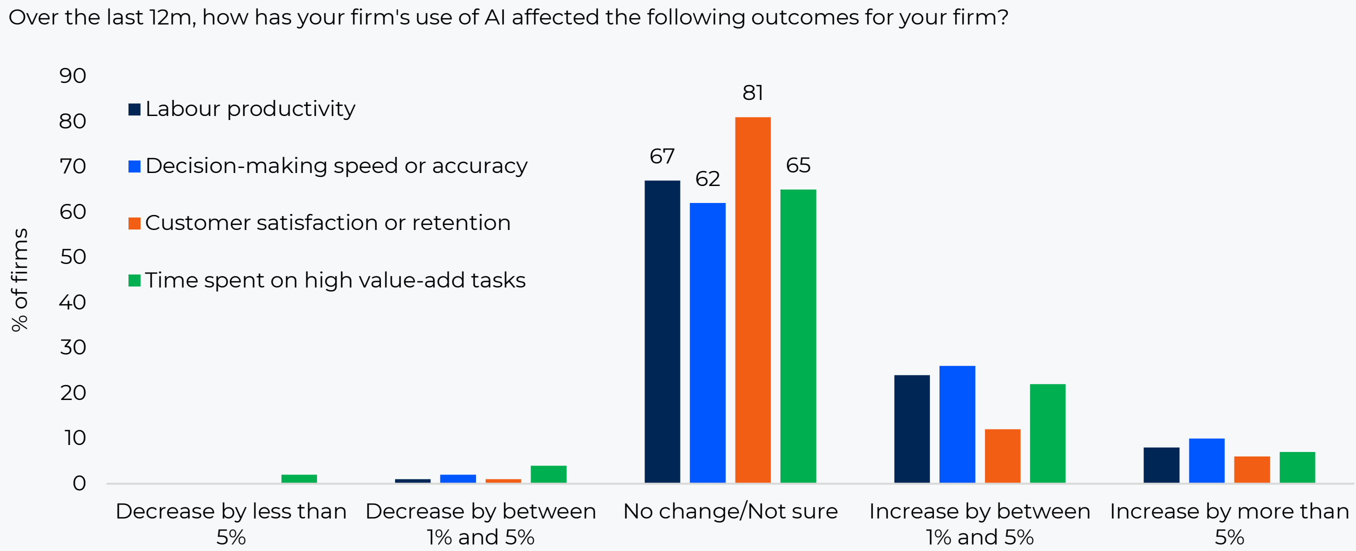


Source: FactSet. Data as of 31 December 2025. Past performance is not indicative of future performance. Indices: Australian Equities: ASX 300; Europe: MSCI Europe; World: MSCI ACWI; US: S&P 500, Emerging Markets: MSCI Emerging Markets, Japan: Nikkei 225, China: MSCI China

AI faces execution risk

The AI narrative remains compelling, and there are few serious doubts about it being a long-term transformative technology. However, execution risk is rising. Markets are increasingly treating AI as a certainty rather than a probability, despite mixed evidence of short-term productivity gains and limited proof that current levels of capital spending will generate a commensurate return. Surveys of corporate executives point to only modest improvements so far in labour productivity, decision-making efficiency and profitability. This growing gap between capital deployed and returns realised increases the risk that expectations have moved ahead of fundamentals, particularly after more than US$1.3 trillion has been invested in hyperscaler capex and R&D since 2022.

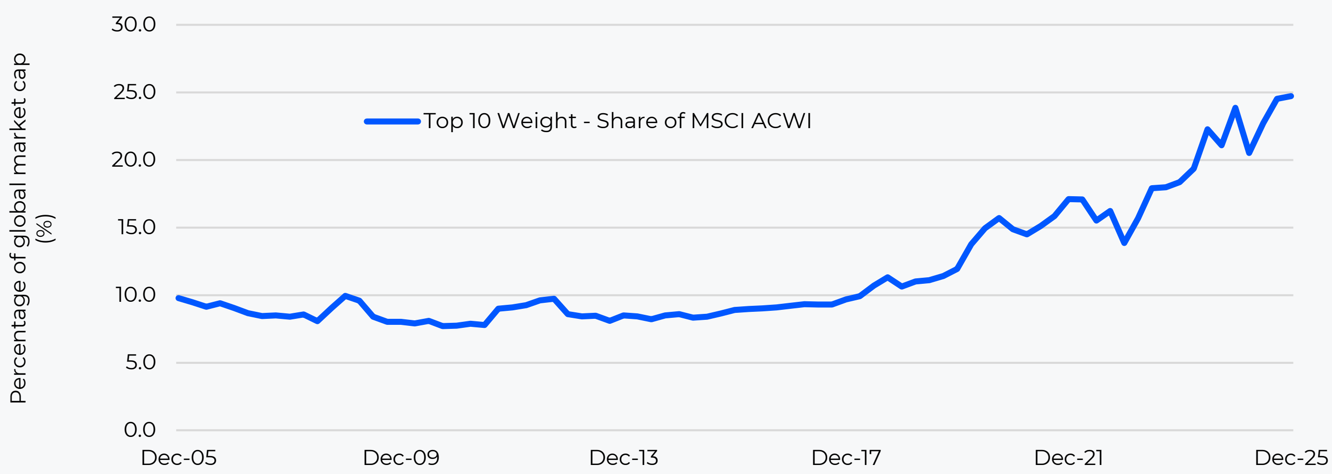
Figure 14: Survey - How has your firm's use of AI affected your firm?



Sources: CFO Survey, Federal Reserve Bank of Richmond, Federal Reserve Bank of Atlanta, Apollo Chief Economist

Market concentration compounds this risk. A relatively small group of AI-exposed companies now accounts for a disproportionate share of global equity market capitalisation and index performance. This concentration leaves markets more vulnerable to shifts in sentiment should the AI narrative be reassessed, echoing the abrupt repricing seen during the technology unwind in 2022. For investors, the implication is that diversification benefits at the index level are weaker than they appear, and despite some recent broadening out in the equity market rally, future headline outcomes will increasingly be driven by the fortunes of a narrow group of AI-linked stocks and their ability to execute on their growth plans.

Figure 15: Percentage of global market cap



Sources: FactSet. Data as of 31 December 2025.

There are also practical constraints within the AI ecosystem with power generation capacity, semiconductor supply chains and geopolitical exposure, particularly involving China and Taiwan, introducing additional uncertainty. At the same time, long-term profitability remains difficult to model. Unlike more mature industries, AI adoption, pricing power and competitive dynamics are still evolving, making forecasts inherently less reliable.

Sticky inflation

Inflation remains a lingering threat. Tariffs, fiscal expansion and tight labour markets in parts of the global economy could reignite upward pressure on prices. If inflation proves stickier than expected, central banks may find their room to respond to weaker growth more limited than markets currently assume.

Geopolitics: A less forgiving backdrop

As discussed in the Special Article ("Literally but not Seriously"), geopolitics adds another layer of risk. Markets have so far shown a remarkable ability to look through political disruption, trade tensions and conflict, but complacency carries its own dangers, particularly where conflicts intersect with supply chains, energy markets or trade policy.

Navigate the current

As we begin 2026, the defining feature of this market to-date remains its resilience. Growth has slowed, policy paths are diverging, and geopolitical risks are elevated, yet some of the underlying drivers that have supported asset prices over the past three years remain largely in place. Financial conditions are accommodative, earnings are broadening, and fiscal policy is adding support to the global economy. None of this means that the market is free of risk, but it does mean that the hurdle for a sustained reversal in the direction of travel, remains high.

For investors, these conditions argue for discipline rather than big bold binary investment decisions. Diversification remains essential, not just as a hedge against a recession, but as protection against leadership shifts. Selectivity has become increasingly important, particularly within AI, where dispersion is widening and expectations are arguably priced to perfection for certain stocks. Volatility is likely to rise as policy and earnings outcomes diverge, but volatility alone is not a reason to turn defensive. Until there is clearer evidence that liquidity, earnings or financial conditions are becoming restrictive, the more prudent approach is to respect the current, manage exposures thoughtfully and remain flexible. This bull market has been unforgiving to rigid and overly defensive views, and there is little reason to believe 2026 will be different.

Australian equities

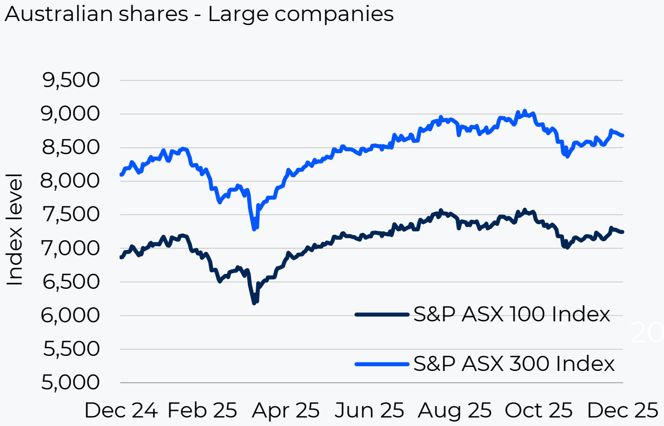
Australian equities weakened into year end, with the S&P/ASX 300 declining -0.9%[1] over the December quarter, though the market still delivered a solid 10.7% return for the full year. This marked the third consecutive calendar year of double-digit returns for Australian equities, underscoring the strength of the broader cycle despite a softer finish to 2025. Investor sentiment was weighed down by a more hawkish domestic monetary policy backdrop, as the Reserve Bank of Australia kept rates on hold in December and continued to emphasise its commitment to returning inflation to target. Persistent inflation in the monthly CPI prints led markets to reassess the likelihood of further easing, with growing expectations that the next policy move may eventually be higher rather than lower.

From a style perspective, Value stocks materially outperformed Growth, returning 3.1%[2] over the quarter compared with a decline of -6.5%[3] for Growth. This relative strength held over the full year, with Value up 17.9% while Growth fell -4.3%. The divergence reflected strong investor demand for more attractively valued sectors, particularly those linked to commodities, as well as continued weakness in high-multiple technology and healthcare names. Size also proved a key differentiator; Large caps fell -1.2%[4] for the quarter, while smaller companies rose 1.8%[5], extending their standout run to deliver a 25.0% gain for the year. Small caps benefited disproportionately from the cumulative impact of the RBA's three rate cuts delivered earlier in 2025, as well as their heavy weighting to the resources complex, where record gold prices have provided a massive tailwind for junior miners and explorers.

Sector performance was narrow, with only three of the eleven ASX 300 sectors finishing in positive territory. Materials were the clear standout, rising 13.0%[6] and ending the year up 37.5%. Strength was led by the major miners, with index heavyweight Rio Tinto hitting a record high late in the year and gaining 20.3% over the period, while BHP rose 7.0%. Industrials also edged higher, up 0.6%[7], and Energy delivered a modest 0.9%[8] gain. At the other end of the market, Information Technology was the weakest sector, falling -23.7%[9] over the period and -19.1% over the year, as enthusiasm for technology stocks continued to fade. WiseTech Global came under significant pressure, declining -24.1% amid ongoing leadership concerns, while Xero fell -27.6%, extending a challenging year for the sector. Health Care also underperformed, dropping -9.5%[10] over the period and nearly -24% for the year. Financials ex-REITs declined -1.9%[11], reflecting some rotation away from banks toward mining stocks, although the sector still delivered a solid 12.0% return for 2025 and remains the strongest performer over the past three years. Consumer Discretionary was another notable laggard, falling -11.5%[12], as a more restrictive interest rate outlook weighed on household spending and consumer confidence.

Refer to footnotes description on page 33

Figure 16: Australian shares



Source: FactSet, Perpetual Private

Australian equities – Manager insights and outlook

Heading into the December quarter we remained cautious on the outlook for Australian Equities, which were already trading near record highs and at considerable valuation premiums versus their historical averages. Despite relatively subdued earnings growth from companies more broadly, the continued flow of capital from both institutional investors, such as the larger superannuation funds and offshore investors, and retail investors, through the now abundant choice of ASX-listed passive and active exchange traded funds, have been a key source of support for Australian Equities. Our expectations are that whilst these continued flows and positive investor sentiment might be supportive of equities over the near term, we could at some point soon expect a correction back towards more sustainable valuation levels, particularly if we see persistent inflation and softer macroeconomic conditions. Against this backdrop, our portfolio held a broadly style neutral approach with a bias towards mid and smaller sized companies, where we note stronger growth profiles and often more attractive valuations.

In reflecting on the quarter that's now past, it was a relatively weak period for Australian Equities when examined on a sector-by-sector basis. Materials (+13%) were the only materially positive for the quarter and given they represent nearly a quarter of the benchmark S&P/ASX 300 on a market-cap weighted basis, the sector was a major positive contributor to the aggregate market return. Outside of Energy and Industrials which were marginally positive, all other sectors were negative. Rhetoric from the RBA suggested a more hawkish stance on interest rates may be adopted going forwards, as inflation remained persistent and more imminent rate cut expectations diminished. It was no surprise the more richly valued growth stocks and other cyclical exposures that are more sensitive to interest rate expectations bore the brunt of the pain, such as Tech (-24%), Consumer Discretionary (-12%) and Healthcare (-9%).

Along a similar vein across our strategies, we saw a positive contribution to our performance from both Core large cap and Value managers. While separately, our continued preference for companies further down the market spectrum proved favourable – with small caps beating large caps by around 3% for the quarter.

Looking ahead, we remain slightly cautious on the outlook for the Australian Equities market and expect more modest returns over 2026. Our outlook is constructive, but mixed – in that whilst the labour market and economic growth has remained relatively resilient and the tide may continue to rise with the steady flow of capital into our local share market from a variety of both institutional, offshore and retail investors; we hold some concerns around the current elevated valuations more broadly, persistent inflation and subsequently more hawkish stance from the RBA, as well as the continued macro-economic uncertainty and geopolitical conflicts abroad. Investor sentiment has already weakened slightly on the news that there would be no rate cut in December with more stubborn inflation prints. Against this backdrop, we have maintained a portfolio that is relatively balanced by style, while having a tilt towards to the mid and small cap segment of the market where we believe more attractive opportunities remain available for skilled stock pickers.

International equities

International shares delivered solid gains to close out 2025, returning 2.7%[13] for the December quarter and 13.6% for the full year. This represents the third consecutive calendar year of double-digit returns for the MSCI All Country World Index, albeit the most muted of the three. The December quarter saw persistent trade tensions, the 43-day US government shutdown (the longest in history), and ongoing debates about the sustainability of AI-driven valuations, all of which contributed to periods of heightened volatility. However, the US Federal Reserve's rate cuts in both October and December generally supported risk assets. In addition, corporate earnings results were overall positive and economic growth remained robust. The US dollar weakened 0.6% against the Australian dollar over the three-month period, modestly dampening unhedged returns for Australian investors.

From a style perspective, market breadth improved during the quarter, with Value stocks (+2.7%[14]) outperforming Growth (+2.1%[15]). This performance differential was driven by mixed earnings in the technology sector and growing concerns regarding the elevated valuations of certain AI-linked stocks. This resulted in a rotation of capital out of some of the most expensive pockets of the market into sectors trading on more attractive multiples. On a full-year basis, however, performance was effectively tied, with Growth (+12.5%) and Value (+12.2%) delivering similar returns as early-year AI momentum was counterbalanced by the year-end rotation. Smaller companies returned 2.0%[39] for the quarter and 11.6% for the previous 12-months. While positive, small caps continue to trail their larger counterparts over the longer term.

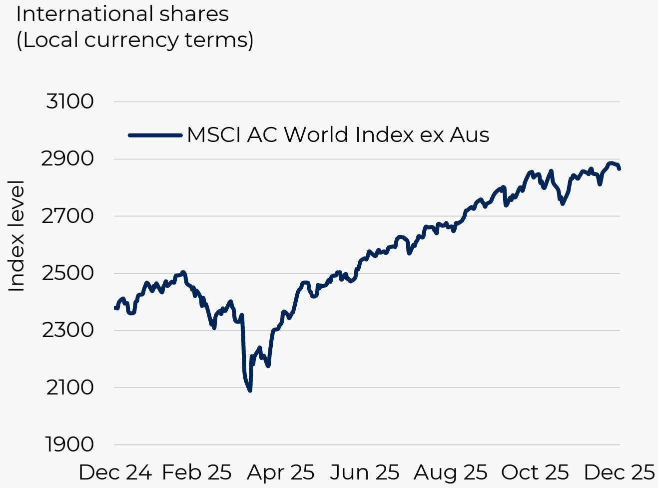
At the sector level, Health Care was the strongest performer, rising 9.2%[16]. This was attributed to investors rotating into defensive assets trading at attractive valuations, alongside relief that the government shutdown did not result in material decreases in US federal healthcare spending. Materials also gained 5.8%[17] as the prices of certain commodities rallied, while Financials rose 4.3%[18], supported by improved lending prospects in a lower-rate environment. Conversely, Information Technology and Communication Services posted a return of 2.3%[19] and 2.7%[20], respectively. A departure from the outsized gains investors have become accustomed to in these sectors. Real Estate was the weakest performer, declining -3.1%[21]. The sector faced headwinds from lingering home affordability concerns, particularly out of the US, and a rise in longer-dated bond yields.

Regionally, 2025 marked the first time in several years where international markets (excluding the US) outperformed US equities. While the bulk of this outperformance was established in the first quarter, the performance gap narrowed significantly following the "Liberation Day" market lows. Performance was led by the UK and Japan, with the FTSE 100 increasing 6.1%[22] and the Nikkei 225 rising 5.0%[23], the latter supported by the election of Prime Minister Sanae Takaichi and expectations of fiscal stimulus. US returns were more muted compared to the normal pattern that has been observed over the last several years, with S&P 500 and Nasdaq Composite Index posted 1.9%[24] and 2.1%[25], respectively.

Refer to footnotes description on page 33

Emerging Markets performed strongly, returning 4.1%[40] for the quarter, led by South Korea and Taiwan where demand for AI memory technology and semiconductors remained robust. Falling global interest rates and a generally weaker US dollar provided further support. Conversely, despite a strong run earlier in 2025, Chinese equities underperformed, with the Hang Seng index declining -4.8%[26] over the quarter, as profit-taking and domestic property market weakness weighed on investor sentiment.

Figure 17: International shares (local currency terms)



Source: FactSet, Perpetual Private

International equities – Manager insights and outlook

The new calendar year brings the opportunity to spend some time navel-gazing and thinking about what the year ahead might bring. As we consider 2026, there are several ideas percolating in our thinking.

While AI remains an exciting prospect for productivity enhancements across industries and sectors, the current hype requires a 'pause for thought' as to what the next stage might bring. Some of our current questions include:

1. Can the AI business model (which we still think is yet to be proven) sustain debt-financed capex, high aggregate debt levels, and increased interrelated-party transactions and financings, etc.?
2. Can corporates in traditional industries generate adequate return on AI-capex investment to deliver increased revenue? Or will most of the benefits come from 'corporate efficiencies' (cost out)?
3. Can AI companies sustain what are already arguably stretched valuations? To this end (and as at the time of writing), recent earnings from Nvidia were positive and impressive, but the stock price has taken a pause and retreated somewhat.

Up until recently, Emerging Market equities have lagged behind broader Developed Market equities, and most notably US equities. Recent (positive) price movements across Emerging Markets have seen these assets move towards long term average valuations, but relative to Developed Markets, they are still looking attractive. To support the case for Emerging Market equities, we'll be looking to see clear indications of sustainable EPS growth. Given China's recent weakness, to support our thesis, we need to see stabilisation in China's macroeconomic outlook, and preferably, additional fiscal stimulus.

Elsewhere in Emerging Markets, we are seeing greater emphasis on corporate reforms. For example, South Korea is implementing a Corporate Value-Up Program that is making solid progress toward changing corporate behaviour and increasing shareholder value, and looking to emulate pockets of success witnessed in Japan with similar programmes. Also, the impact of tariffs on EM growth has been less than anticipated, with those countries expecting greater impacts taking a proactive approach and implementing policy responses prioritising domestic markets and enhancing economic resilience. At the same time, lower central bank policy rates have been a significant net positive for financial conditions within emerging markets.

Earnings growth has largely been confined to US mega-cap stocks over the last three years, however recent months have seen a broadening of earnings growth both in terms of market cap, and region. With strong fiscal impetus from the Trump Administration coming into effect in 2026, we hope to see this nascent trend continue. Further afield, European nations are also engaging in fiscal stimulus (e.g. Germany) while the ECB embarked on a rate cutting programme in 2025, from which we expect to see fruits of lower interest rates as 2026 proceeds.

Real estate

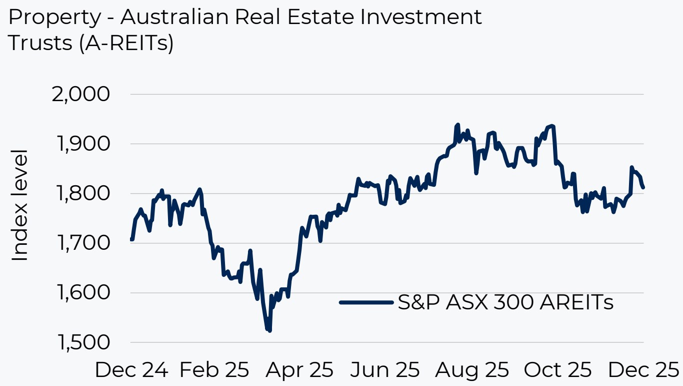
A-REITs experienced a relatively soft final quarter of 2026, slipping some 1.2%[27] over the 3-month period, albeit firming by a healthy 2.0% in December. On a 12-month basis however, the segment returned a robust 9.7% with the Australian property sector continuing to normalise from impacts brought about by the COVID pandemic. The Office sector continues to lag but with many indicators suggesting an improving demand/supply balance (such as reduced incentives and discounting), expectations are growing that the worst is now behind it, particularly with many companies pushing employees to reduce the number of days they work from home.

Globally, G-REITs did not fare as well as their Australian peers, with the relevant index receding by 1.3%[28] in AUD terms, or 0.2%[29] in USD over the quarter. Germany continues to be the laggard of the pack, losing 9.4%[30] in the quarter. Indeed, the German property market has now lost 10.1% on an annualised basis for the past 5 years (to 31st December 2025). As a highly export focused country, the German economy has been suffering from a multitude of complications, not the least of which include tariff/trade disruption and the loss of Russian gas supply. Whilst the US and Eurozone performed similarly over the quarter (-2.5%[31] and -3.0%[32], respectively), their experience over the year was widely different with the US receding 5.8% (impacted strongly by USD weakness), whilst the Eurozone gained a healthy 11.9% for the year. The best performing regions for the quarter are also amongst the best performing regions for the year, Singapore and Japan.

Refer to footnotes description on page 33

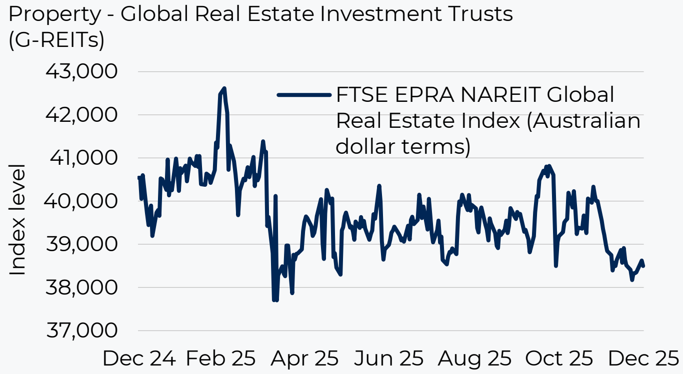
Singapore gained 3.2%[33] for the quarter and 19.1% for the year, whilst Japan had a quieter quarter (2.0%[34]) its year delivered an impressive 29.0%.

Figure 18: Australian Real Estate Trusts (A-REITs)



Source: FactSet, Perpetual Private

Figure 19: Global Real Estate Investment Trusts (G-REITs)



Source: FactSet, Perpetual Private

Real Estate – Manager insights and outlook

REITs have underperformed broader equity markets, particularly offshore, but absolute returns remain positive. This is consistent with what we see as a constructive environment for existing landlords. We believe REITs are now trading near fair value, with limited exposure to the mega-cap technology companies that have been driving global equity markets higher - though there is some secondary exposure via data centres.

We've long highlighted the divergent outcomes between industrial and office property, but these sectors now appear to be converging. Office is beginning to stabilise from its trough, while industrial is softening from peak conditions. Residential has been the more perplexing area of weakness. Higher interest rates and region-specific dynamics play a role, but given the housing shortages across Australia, the US, Canada, the UK, and Europe, fundamentals should support the sector over time. In the US, CBRE has reported rising absorption rates (the pace at which available housing stock is being leased or sold) and falling construction pipelines, yet rental growth has been modest and volatile. A reversal in net migration trends may be a factor here and is a theme we will continue to monitor.

The past quarter produced mixed results locally. Healthcare stocks rebounded, Residential weakened further, with Office and Industrial delivering modest returns. Retail has been resilient, supported by firm consumer demand and a healthy transaction environment. While employment remains solid for now, any weakening in the labour market could weigh on retailers. In industrial, rental growth is being offset by higher incentives, leading to negative effective rental growth, while vacancy rates - though still low - are trending upwards. The sector also faces tariff-related risks, particularly in Australia where Goodman Group accounts for around 40% of the index. Regionally, weakness in Europe and the UK this quarter has tempered what was otherwise strong performance earlier in the year.

In the US, cash rate increases between early 2022 and mid-2023 disrupted the sector, but two years on, markets are adjusting. Over that period, returns have exceeded 10% p.a. globally and 20% p.a. domestically. REITs remain more sensitive to rate moves than broader equities, which explains some of the relative underperformance. Looking ahead, the core fundamentals for real estate remain supportive, but the key risk lies in a slowdown in economic activity that leads to job losses or weaker consumption. While not our base case, recent signs of softer US labour market data suggest this is a risk worth watching closely.

Growth alternatives

We enter 2026 with optimism hoping to see a stable macroeconomic environment, an increase in merger and acquisition (M&A) activity, and markets placing emphasis on fundamentals. As it stands, we don't expect material changes in our asset allocation or investment pipeline.

Across private equity, we continue to hear talk of 'innovation' to support the ecosystem, however, with increasing minority sales, multiple GPs holding equity in the same assets, NAV loans, and capital solutions, etc, much of the 'innovation' seems to be more aligned to facilitating outcomes for GP's rather than LPs. That said, sentiment around corporate activity is improving, and we hope that spurs a return of deal making, and subsequently realisations across older private equity vintages.

In our view, European buy-out strategies continue to offer relative value when compared to their North American counterparts. In Europe, we see more attractive entry prices and fiscal stimulus that could further support demand. German industrials remain under pressure from high energy costs, divesting non-core assets to creating carve-out opportunities for private equity (PE). Despite the fluid backdrop, we remain disciplined in our PE approach, with a focus on valuation, financing structures, and manager operational capabilities. As we move through 2026 and later into this market cycle, we will continue to be highly selective around which managers and strategies we seek exposure to, with emphasis on high total return, high cash flow investments primarily within leveraged buyouts and growth equity, while actively managing our vintage year exposures.

In real estate markets transaction volumes remain weak relative to history, though they have increased modestly year-on-year. We believe cap rate expansion has now peaked in most sectors and markets, creating more stable conditions which should provide a confidence boost to investors. While we expected a reasonably uniform fall in global interest rates, it is increasingly possible that central banks are likely to be less coordinated that initially anticipated, meaning that regional allocation to real estate-based strategies will become increasingly critical.

Infrastructure saw an uptick in demand during the quarter after a lull in recent periods. Encouragingly, pricing remains sensible. Infrastructure remains a core holding across portfolios, valued for its stable and inflation-linked cash flows. As we move into period where fiscal policy is expansionary in most parts of the developed world, we wouldn't be surprised to see inflation tick up modestly, which should support increasingly free cash flow across inflation linked assets.

Across traded markets, dispersion in equity and credit pricing continues to reflect divergent macroeconomic and political conditions. Our existing credit exposures have delivered solid performance, but tighter spreads have reduced the appeal of new opportunities. In response, we are reallocating towards hedge fund strategies with asymmetric return profiles and relative value approaches, which offer resilience in risk-off markets. We are currently reviewing several opportunities and expect to make new allocations across into 2026

Income alternatives

Demand for private credit assets remained robust throughout the December quarter, with flows driving continued spread compression across multiple segments. Limited credit issuance in 2025 has exacerbated supply constraints, while declining base rates have encouraged a number of companies to increase balance sheet leverage without compromising debt serviceability. Broadly Syndicated Loans (BSLs) continue to exhibit similar fundamentals without material changes to spreads, delivering margins of approximately 1-2% above cash.

Deal flow in private corporate credit remains subdued in Q4 2025 in-line with the observed slow-down in M&A activity. We have seen more institutional capital move into alternative segments of private credit such as asset-based finance, bank regulatory risk transfers and NAV lending. While the risk considerations may vary materially across these segments, we are seeing an increased willingness by investors to chase yield while ignoring stretched fundamentals. Indeed, despite the corporate defaults experienced in 2025 such as First Brands and Tricolor, the appetite for these assets has not waned.

Insurance-linked assets continue to enjoy elevated spreads, providing all-in returns of circa 10% p.a. However, pricing of transactions in this space remains heavily bid with more parties relying on leverage to meet their cost of capital. Given the competitive nature of the market, we have seen more asset managers engage in organic growth strategies; increasingly integrating origination capabilities with asset management. Within catastrophe risk, we anticipate maintaining our modest allocation to catastrophe bonds. While spreads have tightened slightly, they remain attractive relative to other income-generating opportunities.

We have adopted a more cautious stance towards specialty finance and regulatory capital. While geopolitical risks in the US are not a primary concern, capital reallocation by institutional investors away from the US has created selective opportunities to acquire assets at better spreads with reduced competition. Credit assets in developed Europe remains heavily bid, while capital remains scarce for assets located in periphery Europe. Notably, there remain a persistently large dispersion in credit terms and quality. We continue to favour a nimble approach to capital allocation and expect the portfolio to benefit from a marginal pick-up in yield.

Portfolio income returns remain compelling, though further spread compression could temper future performance. We maintain a constructive outlook on income alternatives but remain selective, favouring niche or structurally complex segments such as specialty finance. The portfolio retains a defensive bias, balancing income generation with prudent liquidity management to ensure flexibility in the event of credit dislocations.

Fixed income

The final quarter of 2025 saw Fixed income markets having to contend with a dispersion of economic conditions as inflation and central bank considerations, diverged across geographies. On a global basis, the December quarter saw a positive, albeit muted return of 0.7%[35] for Fixed Income, as expectations of early 2026 interest rate cuts from the Federal Reserve ("the Fed") receded. More broadly however, global Fixed Income generated the majority of its returns (4.4%) through income received over the year, with a slight tailwind provided by growing dovish expectations for the Fed's future interest rate path.

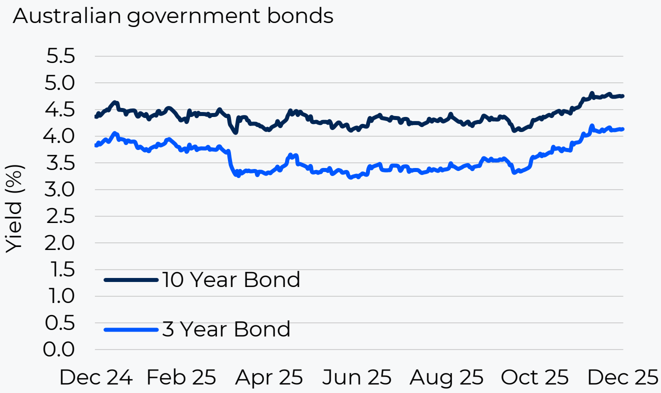
We have observed that the Fed has gone from focusing primarily on stubbornly high inflation, reducing chances on further rate cuts, to a focus on signals that the labour market might be softening (with employment conditions being the second leg of the bank's 'dual mandate'). Whether this change is at all influenced by pressure from the US president, or is simply a normal balancing of priorities, remains to be seen. What we know now, is that the Fed today has a dovish bias that it didn't have just six months ago. In Australia, almost the opposite has happened. With inflation remaining sticky, expectations of further cuts late in 2025 quickly diminished, to the point that by year-end, markets had even started to price in a rate increase at the bank's February meeting (at the time of writing, market prices within FactSet are implying a 24.6% probability of an interest rate increase).

Locally, the change in posture from the RBA, meant that bond prices fell to accommodate the potential for higher cash rates.

This ate into income for the asset class, resulting in an annual return of just 3.2%[36] for the year, after falling 1.2% in the final quarter.

Meanwhile, Credit continues to deliver handsomely for those exposed to it, with spreads remaining low and defaults scarce. The US, for instance, saw its corporate bonds deliver 0.7%[37] for the December quarter and 6.5% for the year. Similarly, if we look at the Australian market, Credit continues to perform well, particularly if we remove duration (and therefore interest rate sensitivity), resulting in returns of 1.0%[38] for the 3 months, and 5.0% for the year. Against this backdrop, it should be no surprise that the more risky "high yield" securities, continue to deliver outsized returns, gaining 2.2%[39] in the quarter and a whopping 9.6% for 2025.

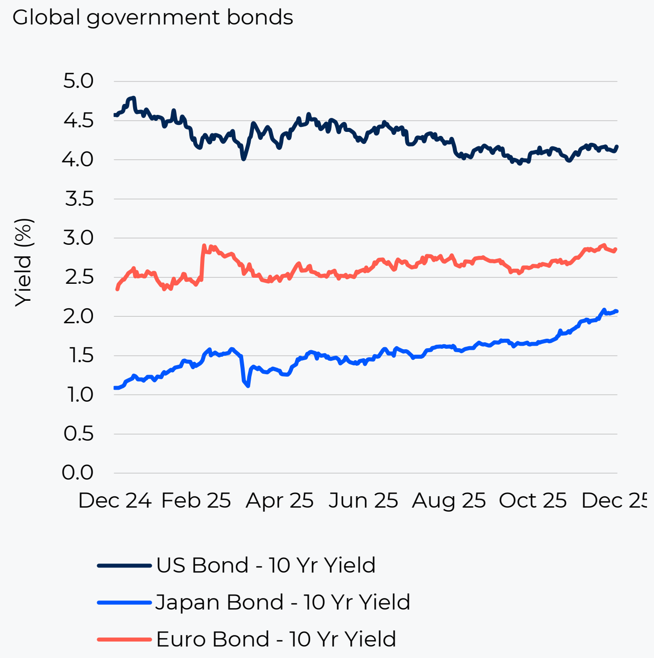
Figure 20: Australian government bond yields



Source: FactSet, Perpetual Private. Note: Bond prices are inversely correlated with bond yields.

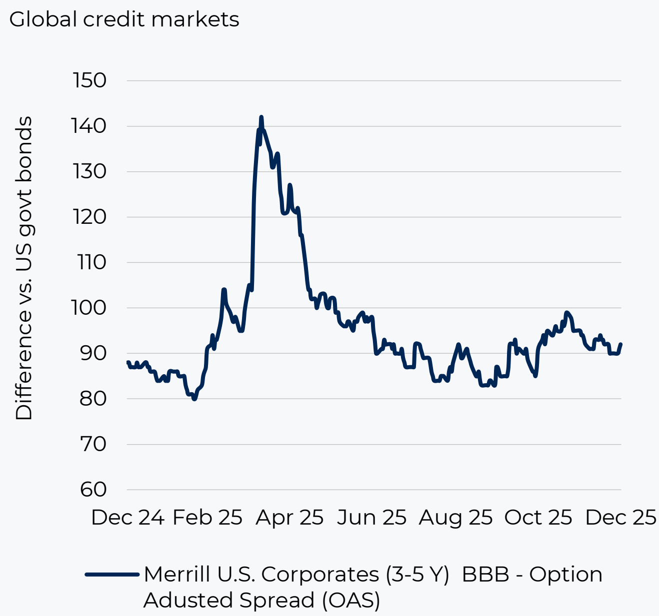
Refer to footnotes description on page 33

Figure 21: Global government bond yields



Source: FactSet, Perpetual Private

Figure 22: Global credit markets



Source: FactSet, Perpetual Private

Fixed income – Manager insights and outlook

The Reserve Bank of Australia maintained policy rates steady during the December quarter as inflation edged slightly higher. Commentary from the board indicates a more cautious stance. Government bond volatility persisted and is expected to remain elevated through 2026. Analysis of domestic inflation drivers point to housing as the largest contributor, followed by food and healthcare.

US tariffs have had minimal impact on inflation to date, though longer-term implications of trade policy remain uncertain. We anticipate diverging inflationary pressures globally, with moderate upward pressure on US inflation over the medium term. Economic growth remains positive, supported by infrastructure investment, while consumer spending, though resilient, moderated during the quarter. Monetary policy uncertainty continues to drive volatility in global sovereign bond markets. Despite this, absolute yield levels remain elevated relative to historical norms, particularly compared to the pre-2022 zero-rate environment.

Credit demand from asset owners remains strong, while credit creation is subdued amid weak M&A activity and a limited issuance pipeline. Spreads are tight, but we see scope for further compression. Base rates have declined over 2025, supporting corporate credit quality and improving overall debt serviceability.

Our portfolios benefited from tactical positioning across the government bond curve and sector rotation within credit. Emerging market debt contributed positively to performance at the headline portfolio level. However, with fundamentals now fully priced, we have exited the position during the quarter. We maintain a selective approach in credit, favouring shorter-dated exposures where valuations remain attractive.

Australian cash rate

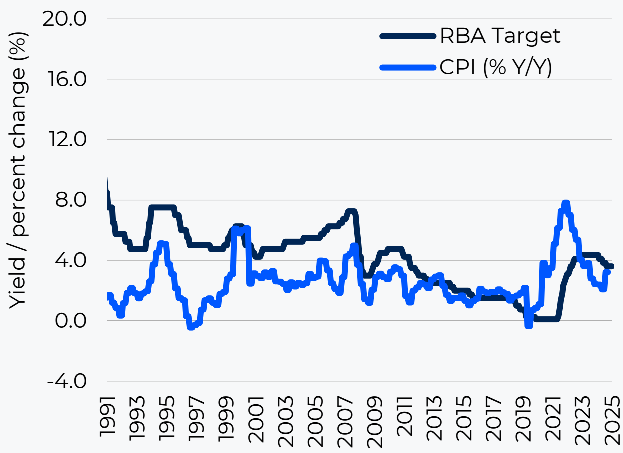
The Reserve Bank of Australia (RBA) held the official cash rate steady at 3.60% throughout the December quarter, extending the pause that began in September. While markets had entered the quarter expecting the RBA to continue its earlier cadence of a cut a quarter, a renewed lift in inflation and signs of ongoing capacity pressures prompted a clear shift in both policy tone and market expectations.

The October monthly CPI surprised sharply to the upside, rising to 3.8%[40] year-on-year. Much of the increase was driven by a surge in electricity prices, following the roll-off of state and federal energy rebates, alongside ongoing strength in housing-related costs such as rents and new dwelling construction. November's monthly CPI release moderated to 3.4% but remained above the RBA's 2–3% target band. The unemployment rate held steady at 4.3% in November, marginally below expectations. However, this stability masked softer underlying dynamics, with employment falling by 21,000 and participation declining to 66.7%. The RBA continued to assess the labour market as "a little tight," with limited spare capacity putting upward pressure on wages and prices.

At its December meeting, the RBA struck a noticeably more hawkish tone than earlier in the year. Members acknowledged that recent data had reduced confidence that monetary policy remained clearly restrictive, with views split on whether conditions were still mildly tight or closer to neutral. Importantly, the Board discussed the circumstances under which a rate increase might need to be considered in 2026, citing persistent above-target inflation and signs that excess demand in the economy may be more durable than previously expected. In response, market pricing shifted materially, moving from expectations of further easing to pricing in the possibility of rate hikes next year.

Figure 23: Long-term cash rate vs inflation

Long-term cash rate vs inflation



Source: FactSet, Perpetual Private.

Refer to footnotes description on page 33

Australian Cash Rate – Outlook

Looking ahead, the RBA finds itself at a delicate stage of the policy cycle. In its November Statement on Monetary Policy, the Bank forecast that underlying inflation would remain above the 2–3% target range until the second half of 2026 and settle above the midpoint thereafter. That assessment, reaffirmed in December, represents a meaningful extension of the timeline for returning inflation to target and underscores the difficulty of the final leg of disinflation.

While inflation has fallen substantially from its peak, the economy continues to operate with limited spare capacity. Private demand has proven stronger than expected, labour market conditions remain tight, and cost pressures in housing and services are proving sticky. These persistent pressures are increasingly testing the RBA's patience, and the case for further tightening has strengthened. Given considerable uncertainty around the new monthly CPI series and its volatility, the quarterly CPI remains the primary gauge for assessing inflation momentum, with the December quarter print due ahead of the February 2026 meeting.

The RBA has made clear that policy will need to remain restrictive for some time to ensure inflation returns sustainably to target, and the risks are now skewed towards further rate hikes rather than cuts. While market pricing has moved quickly to anticipate rate increases in 2026, the Bank appears content to remain patient for now, watching how inflation, labour market conditions and financial settings evolve before taking its next step. However, the window for tolerance is narrowing, and another rate increase looks increasingly likely if inflation proves more persistent than hoped.

Australian dollar

The Australian dollar (AUD) edged modestly higher over the December quarter, rising 0.9% against the US dollar to finish the year near US$0.67. While the move was incremental, it marked a clear improvement from the post-"Liberation Day" lows of US$0.59 seen earlier in 2025 and capped a year in which the currency finally broke a four-year losing streak against the greenback. The AUD/USD traded within a relatively narrow US$0.64–0.67 range for most of the quarter, highlighting the market's reluctance to drive the currency meaningfully higher without a clearer macro catalyst.

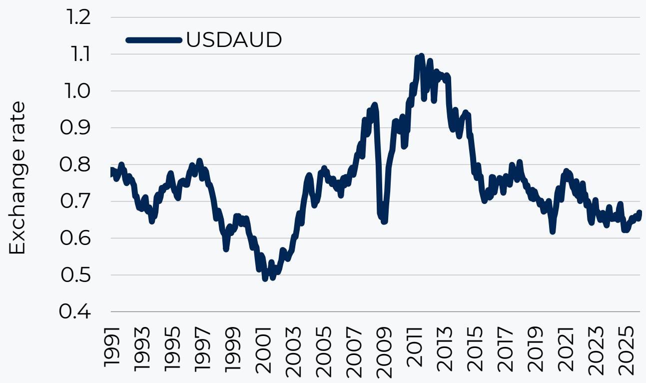
Currency moves during the quarter were driven primarily by developments in the United States rather than domestic factors. The US dollar stabilised after a sharp decline earlier in the year, with the US Dollar Index trading in a narrow 98–100 range. Ongoing concerns around US fiscal sustainability, trade uncertainty, and geopolitical risk continued to weigh on sentiment, but these were largely offset by resilient US growth data. Notably, the earlier decline in the US dollar coincided with a period of US equity underperformance, while stabilisation in the greenback aligned with an improvement in relative US equity performance later in the year.

Domestically, the AUD drew support from shifting interest rate differentials. Sticky inflation outcomes and a resilient labour market reinforced the Reserve Bank of Australia's decision to keep the cash rate on hold throughout the quarter, while markets increasingly priced the risk of further tightening from the RBA in 2026. By contrast, expectations for the US Federal Reserve continued to factor in additional rate cuts as inflation pressures eased and labour market data softened. This divergence helped underpin the AUD later in the year, although the currency remained sensitive to broader risk sentiment and developments in China.

Commodity prices also provided a stabilising influence for the AUD/USD. Iron ore prices held up better than expected, while strength in precious metals added further support. Also, gold surged over the year amid heightened geopolitical uncertainty, improving Australia's terms of trade and lending further support to the currency.

Figure 24: Australian dollar US dollar (daily) long term

USD per AUD long-term exchange rate



Source: FactSet, Perpetual Private

Australian Dollar – Outlook

Looking ahead, the Australian dollar enters 2026 with a more constructive backdrop than it has faced in recent years, although meaningful upside is likely to be gradual rather than abrupt. Interest rate differentials remain a key support, with Australian policy settings relatively restrictive compared to a Federal Reserve that is expected to continue easing. This dynamic should help limit downside pressure on the AUD and may allow for a gradual push higher should US dollar weakness re-emerge. It is also a central pillar behind the broadly constructive outlook for the AUD among major investment banks into 2026.

Valuation models continue to suggest the AUD is undervalued, with purchasing power parity estimates placing fair value closer to US$0.72. However, valuation alone is unlikely to drive a sustained breakout. Further appreciation will depend on a combination of renewed US dollar softness, a stable global growth backdrop, and confidence that China can avoid a sharper slowdown. While recent data point to resilience in Chinese trade and manufacturing, structural challenges in the property sector and subdued domestic demand continue to cap enthusiasm.

Overall, a decisive move above US$0.70 is likely to require more clarity on the outlook than markets currently have. Many of the conditions that could support a stronger AUD have been in place for some time, yet the currency has remained range bound. Until uncertainty around the broader macro backdrop begins to ease, the balance of risks points to gradual gains rather than a meaningful breakout.

1. As measured by the S&P/ASX 300 – Total Return index
2. As measured by the MSCI Australia Value – Net Return index
3. As measured by the MSCI Australia Growth – Net Return index
4. As measured by the S&P/ASX 100 – Total Return index
5. As measured by the S&P/ASX Small Ordinaries – Total Return index
6. As measured by the S&P/ASX 300 Materials (Sector) – Total Return index
7. As measured by the S&P/ASX 300 Industrials (Sector) – Total Return index
8. As measured by the S&P/ASX 300 Energy (Sector) – Total Return index
9. As measured by the S&P/ASX 300 Information Technology (Sector) – Total Return index
10. As measured by the S&P/ASX 300 Health Care (Sector) – Total Return index
11. As measured by the S&P/ASX 300 Financials ex-REITs (Sector) – Total Return index
12. As measured by the S&P/ASX 300 Consumer Discretionary (Sector) – Total Return index
13. As measured by the MSCI All Country World index in AUD (unhedged) terms
14. As measured by the MSCI World Value index in AUD (unhedged) terms
15. As measured by the MSCI World Growth index in AUD (unhedged) terms
16. As measured by the MSCI AC World – Health Care index in AUD (unhedged) terms
17. As measured by the MSCI AC World – Materials index in AUD (unhedged) terms
18. As measured by the MSCI AC World – Financials index in AUD (unhedged) terms
19. As measured by the MSCI AC World – Information Technology index in AUD (unhedged) terms
20. As measured by the MSCI AC World – Communication Services index in AUD (unhedged) terms
21. As measured by the FTSE 100 in AUD (unhedged) terms
22. As measured by the Nikkei 225 in AUD (unhedged) terms
23. As measured by the S&P 500 in AUD (unhedged) terms
24. As measured by the Nasdaq Composite index in AUD (unhedged) terms
25. As measured by the Hang Seng index in AUD (unhedged) terms
26. As measured by the S&P/ASX 300 A-REIT index
27. As measured by the FTSE EPRA Nareit Global index in AUD terms
28. As measured by the FTSE EPRA Nareit Germany index in AUD terms
29. As measured by the FTSE EPRA Nareit USA index in AUD terms
30. As measured by the FTSE EPRA Nareit Eurozone in AUD terms
31. As measured by the FTSE EPRA Nareit Singapore index in AUD terms
32. As measured by the FTSE EPRA Nareit Japan index in AUD terms
33. As measured by the Bloomberg Global Aggregate
34. As measured by the Bloomberg AusBond Composite (0+Y) index
35. As measured by the ICE BofA Global Corporate (AUD hedged) index
36. As measured by the Bloomberg AusBond Credit FRN (0+Y) index
37. As measured by the Bloomberg Global High Yield (AUD Hedged) index
38. Australian Bureau of Statistics (ABS), Labour Force Survey, and Consumer Price index
39. As measured by the MSCI AC World Small Cap index in AUD (unhedged) terms
40. As measured by MSCI Emerging Markets index in AUD (unhedged) terms

Authors

Andrew Garrett, CFA CAIA
National Investment Director, Perpetual Private

Andrew provides investment research, portfolio construction and bespoke investment advice for Perpetual Private's clients.

Andrew works closely with advisers by providing specialist investment knowledge on Perpetual's investment process and strategy implementation, focusing on delivering optimal solutions to our stakeholders and partners. This is further augmented by his provision of transparent and accessible knowledge of financial markets and asset classes both globally and locally.

Having spent 15 years in London, Andrew returned to Melbourne with a wealth of international experience to benefit Perpetual's clients and partners. Having started his career working on private equity transactions and stock market listings, he then spent time working on equity trading desks, before moving into investment management. In his role as a Portfolio Manager for Barclays Investment Solutions, Andrew managed money across multiple asset-classes on behalf of various client groups, before focusing on the charity and not-for-profit segment. With responsibility for as much as £3bn in assets, he developed a strong reputation for delivering robust investment performance linked to his comprehensive understanding of global investment markets.

Andrew is a holder of the Chartered Financial Analyst and the Chartered Alternative Investment Analyst designations.

Hugo Goode, CFA
Investment Specialist, Perpetual Private

Hugo is an Investment Specialist at Perpetual Private, where he joined the Investment Research Team in October 2023. He supports the Head of Managed Accounts and Perpetual Private Investment Directors by developing and maintaining investment content and collateral. He also helps communicate Perpetual Private's investment offerings to advisors and intermediary sales teams, representing the Multi-Manager and Direct Equities teams.

Before joining Perpetual, Hugo gained valuable international experience working as a Research Analyst for a wealth management firm in Vancouver, Canada. During his four years there, he focused on strategic and tactical asset allocation of multi-asset portfolios for the firm's high-net-worth clientelle. Prior to his time in Canada, he held roles in Sydney at BT Financial Group as a Customer Relations Consultant and TP ICAP as a Trainee Broker.

Hugo is a CFA charterholder and holds a Bachelor of Commerce degree, majoring in Finance and Accounting, from the University of New South Wales.

More Information

1800 631 381
perpetualprivate@perpetual.com.au
perpetual.com.au

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