

Atchíson

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Tactical Asset Allocation Outlook

Q4 2025

Illuminating
the way forward





Tactical Asset Allocation

Tactical asset allocation (TAA) is an investment style in which three primary asset classes (shares, bonds, and cash) are actively balanced and adjusted based on market performance to meet stated risk tolerance and investment objectives.

The focus is on asset classes rather than specific assets themselves. The strategy blends and augments passive buy-and-hold methods with medium term views on market dislocations and valuation opportunities.

This report should be read in conjunction with our most recent Investment Outlook, incorporating updated capital market assumptions (CMA) which project the returns of asset classes over a ten-year horizon. These serve as key inputs into our strategic asset allocation (SAA) model and can also be termed as neutral asset allocation positions.

Refer to Table 1 for Summary TAA positions - Q4 2025. The recommendations shown in the summary are Atchison's conviction away from an SAA, therefore should not be interpreted as a recommended percentage change.

Introduction

Overall, the global economy continues to exhibit considerable resilience amid heightened policy and geopolitical uncertainty. The resilience is underpinned by supportive financial conditions, relatively healthy household and corporate balance sheets, the promise of an AI-driven productivity boost, and low energy prices, among other factors.

However, it should be noted that even though equities continue to outperform fixed income, and credit markets continue to outperform government bonds, the pace of outperformance has declined meaningfully compared to calendar year 2023 and 2024.

The high tariffs and lingering trade uncertainty will likely continue to weigh on the global economy over Q4. It is considered that Southeast Asia will be hardest hit and that the US-EU trade deal is less disadvantageous for the EU than initially perceived. With 60% of US imports now covered by trade deals or existing arrangements like the US-Mexico-Canada Agreement, the peak of trade uncertainty appears to have passed. Therefore, the view is the current slowdown is viewed as a temporary dip rather than the beginning of a sustained downturn.

We continue to be relatively optimistic for global markets as monetary and fiscal policy are stimulative and trade uncertainty continues to recede (except for the occasional blip). We see little risk of recession and favour equities over bonds heading into Q4. As we assess the market today and look across various assets, we see a few areas of dislocation.

What to watch out for?

- **Geopolitical instability** – As we consider the economic environment ahead, we must acknowledge that the current tariff policy will have some impact on curtailing the pace of economic growth. To date, tariffs have had a limited influence on growth. Escalating global tensions or trade disruptions could fuel volatility and challenge risk asset performance.
- **Earnings breadth and quality** – Continued broadening across other sectors and smaller market caps beyond the concentrated US technology names.
- **Central bank policy shifts** – A slower-than-expected pace of interest rate cuts or renewed hawkishness could impact both equity valuations and bond yields.
- **China's growth trajectory** – Remains under pressure, with elevated US tariffs continuing to pose a threat. Economic momentum remains sluggish.

Summary of our Q4 2025 TAA:

- 01. Maintain overweight exposure to International Equities ex Australia** due to projected soft landing for the US economy, improving investment conditions in Europe and attractive comparable valuations from Emerging Markets (EMs).
 - 02. Maintain Australian Equities exposure at neutral** on the back of anticipated rate cuts, and a slight uptick in forward earnings expectations.
 - 03. Reduce overweight to US Equities to neutral:** Trade policy raises concerns about US economic growth while the S&P 500's record valuations and increasing concentration in AI-related stocks show downside risk.
 - 04. Increase modest overweight to European Equities:** The region presents a compelling entry point, supported by the European Central Bank's (ECB) easing cycle, renewed interest from foreign investors, and diversification away from US tech dominance.
 - 05. Move from underweight to moderately overweight to Japanese Equities:** Supported by projected growth for the Japanese economy and a modest uplift in domestic corporate revenues.
 - 06. Move to marginal overweight position to EM's:** US dollar retreat is making is easing debt servicing pressures, while rising commodity prices and the fading impact of earlier tariffs provide a more supportive backdrop for EM equities and bonds.
 - 07. Maintain underweight Real Assets exposure:** Cautious on listed infrastructure amid moderating inflation.
 - 08. Maintain overweight Alternatives:** Uncorrelated return drivers through hedge funds, gold, listed private equity.
 - 09. Increase exposure to Duration** to capitalise on anticipated rate cuts in most developed markets.
 - 10. Maintain neutral Floating Rate exposure,** balancing the rise in credit risk against a declining interest rate environment.
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Australian Equities



We continue to maintain a **neutral allocation** to Australian equities over Q4 following mixed reporting season, opposite to the positive earnings outlook from the US market. The aggregate Earnings Per Share (EPS) for the S&P/ASX 200 Index has been revised down by around 1% for CY25 and 2% for CY26. The index-level 12-month forward EPS currently sits approximately 14% below where it peaked in October 2022. And yet, the Price/Earnings (P/E) multiple expansion has driven strong equity market returns over the last three years. The 12-month forward P/E of the S&P/ASX 200 Index is just below 20x, a touch below the previous high of 20.6x seen in late-2020.

The Reserve Bank of Australia (RBA) signalling remains pivotal. Unemployment has increased to 4.5% in September 2025, the highest since November 2021, which has brought forward market expectations for an interest rate cut. At the same time, the RBA sees signs of loosening financial conditions after earlier cuts (rates at 3.60%) but continues to stress uncertainty around inflation and credit cost drivers. Slowing labour/employment momentum strengthens the case for easing, which is equity-positive in general. However, deteriorating sentiment and weakening consumer indicators suggest corporate earnings risk is rising.

Should inflation re-accelerate, or global trade/commodity pressures worsen, the domestic equity market may underperform global equities or see increased drawdowns. This reinforces the importance of active asset-class allocation and perhaps tilting to global equities and more defensive exposures.

A neutral stance permits the margin of safety while still staying invested and avoiding overstretching the risk budget.



International Equities

We believe recent macro data and policy efforts support staying marginally overweight global equities. A soft landing for the US economy and significant policy support outside the US remain key assumptions behind expectations for continued corporate earnings growth. Global equities provide access to sectors such as technology, healthcare, global consumer and emerging markets.

United States (US) equities

We prefer to **dial back our modest overweight position to US equities to neutral**. We expect US economic growth to slow below its 1.8% year-on-year long-term trend in the coming year, as the highest import tariffs in almost a century and policy uncertainty weigh on consumer and business confidence, job creation and real wages. However, the economy is likely to avoid a downturn as the impact of tax cuts and corporate investment incentives (from the One Big Beautiful Bill), and the resumption of US Fed (Fed) interest rate cuts kick in from late 2025. With trade tensions largely contained, the focus should turn to deregulation of banking, energy and other sectors, which, along with fiscal stimulus, a weak USD and lower borrowing costs, should lift consumer and business spending.

The Atlanta Fed's GDP model shows US growth is accelerating above a 3% annualised rate in Q3, even as job creation has decisively slowed. This dichotomy can be explained either by an acceleration in productivity growth or that the job market is about to catch up with the growth acceleration. The former would be positive, as it would ease inflation concerns, allowing the Fed to keep cutting rates. The latter explanation, against the backdrop of immigration curbs, could be inflationary, slowing rate cuts.

However, the immediate risks are a prolonged government shutdown and the impact of tariffs on growth and inflation. US job creation has slowed to a near-stall speed, with non-healthcare sector jobs contracting.

Whilst the macro environment remains supportive, the S&P 500 has doubled in five years to trade at record highs, led by AI stocks such as Nvidia, which has soared almost 14-fold to become the world's most valuable public company with a \$4.3 trillion market capitalisation. The current trailing P/E of ~30.9x versus a historical norm of ~16x, valuation risk in US equities is elevated. This overvaluation is largely concentrated in a narrow set of growth style companies. From a portfolio construction perspective this reinforces a cautious stance for the US large cap equity bucket in favour of tilting to value stocks, mid-caps and emerging market equities.

European equities

Increase current modest overweight position of European equities. The Euro Stoxx 50 is becoming even more attractive after several months of underperformance. The Euro Stoxx 50 has trailed the S&P 500 by nearly 18% since its strong first-quarter rally, this underperformance can be viewed as a buying opportunity.

Europe is beginning to tackle its structural issues, possibly paving the way for substantial and hopefully lasting change. The introduction of new fiscal measures, with the EU aiming to boost defence spending and Germany spending more on infrastructure, should provide some support to the economy even as US tariffs act as a headwind.

The MSCI EMU (Economic and Monetary Union) Index, also deemed a proxy for European equities, trades at a P/E valuation of 15.4x 12-months forward consensus earnings forecast, aligning closely with its long-term average. Importantly, it also trades at a discount to US equities even on a sector-adjusted basis (adjustment to sectors to avoid unintended biases when comparing indexes). Sectors likely to benefit from the fiscal stimulus, include select industrials, particularly defence, and materials. Additionally, it is expected that banks should benefit from the region's improved medium-term growth outlook and a steeper yield curve, while continuing to offer attractive shareholder returns via dividends and share buybacks. However, we remain mindful that sectors subject to tariffs such as automobiles, industrial equipment and pharmaceuticals as well as those exposed to a strong currency are less likely to outperform.

Japan equities

We have **moved from underweight Japanese equities to modestly overweight** as Japan's economy is tracking better than anticipated at the beginning of 2025. The International Monetary Fund (IMF) has revised up its 2025 growth forecast for Japan to 1.1% (from 0.7% in July) and estimates growth of about 0.6% in 2026. This suggests the economy is showing more resilience than the earlier low single-digit outlook.

However, the recovery is uneven, heavily reliant on domestic demand rather than export strength, with structural headwinds. That said, corporate results suggest pockets of strength; for example, Fast Retailing (Uniqlo) reported record profits, driven by strong domestic consumption and international expansion. The stabilising labour market and rising wages (as surveys suggest) could help underpin domestic demand if sustained.

Favourable corporate governance reforms and restructuring continue to provide a tailwind, combined with a relatively high dividend yield, translates to a high cash return to shareholders.

Emerging market equities

Move to a slight overweight to EM equities on the back of improving earnings. While EM exposure comes with heightened volatility and risks - including a range of economic, political, regulatory, and currency factors - the asset class offers compelling upside through attractive relative valuations and the potential for a stronger-than-expected policy response from China.

The US dollar's loss of momentum this year has provided a relief for many key emerging markets. Interest rate differentials, fiscal dynamics, and trust in institutional quality assets are all shifting in response to recent US policies. Lower valuations for EM equities compared with developed markets makes them attractive while in fixed income, higher-than-average yields favour EM hard currency bonds.

Despite the anticipated tariff-triggered economic slowdown in the final quarter of 2025, trade policy uncertainties are fading. Most emerging markets have also refrained from retaliating against the US measures, limiting the fallout from tariffs on their consumers and industries from price shocks.

Real Assets



Maintain an underweight to Real Assets by a modest amount relative to a neutral benchmark. The structural tailwinds, improved entry valuations in certain segments and diversification benefits still make the investment case compelling. However, because of heightened macro uncertainty, and interest-rate risk, the allocation size should be measured, selective, and executed with governance and liquidity controls in mind.

Recommended focus on segments that are deemed attractive within real assets. In infrastructure, this includes core regulated assets and thematics such as digital infrastructure, power and grid, and data centres. rather than speculative greenfield developments. In property, preference lies with industrial/logistics, and multifamily/residential (or other strong sub-sectors) as opposed to office or retail, where structural risks remain.

Alternatives

We **maintain overweight allocation to alternatives** as this is an important driver of uncorrelated returns, in a world of frothy valuations and sentiment driven growth.

Hedge funds offer the ability to generate returns from movement in rates, currencies and commodities - even when traditional assets like stocks and bonds are highly correlated. Many hedge fund strategies, such as long/short equity, global macro, currency, and event-driven, are designed to be uncorrelated and aim to deliver consistent returns with lower volatility. Our preference is to deploy uncorrelated hedge funds to provide a more diversified stance and react in an uncorrelated fashion versus equities.

Gold has been one of the year's strongest-performing assets, reaching record highs above US \$4,000 per ounce. In contrast, Bitcoin often described as "digital gold" has underperformed, rising only about 11% year to date. While gold cannot be valued using traditional cash flow metrics, its price is strongly influenced by macro factors, particularly real yields, US dollar strength, and volatility. Looking ahead, gold's appeal remains supported by persistent geopolitical risks, and ongoing central-bank demand - particularly from China, India, and Japan.



Duration



We are **marginally increasing our modest overweight** to duration, as indicators suggest we are entering a phase where yields are elevated, and central banks are gradually shifting towards interest rate cuts. However, the timing, magnitude, and market expectations differ significantly across regions. Economic growth appears to be weakening in Australia while remaining relatively resilient in other major economies, such as the United States. Consequently, there is a case to tilt allocations towards longer-dated government bonds to benefit from a potential decline in yields. Since the start of 2025, the Australian 10-year government bond yield has risen back above 4%.

Should economic conditions soften evidenced by a higher unemployment rate - long-dated government yields could fall. One way to capture this opportunity is to lengthen portfolio duration through increased exposure to longer-maturity bonds. Globally, the fixed income outlook for long-duration sovereign bonds has also improved. Many developed-market yields remain near historically elevated levels. Interestingly, the Bank for International Settlements' Quarterly Review (September 2025) noted that during Q2 2025, flows into sovereign bond funds targeting euro-area and other advanced economies surpassed those directed towards the US. The data also showed particularly strong inflows into Asian emerging-market sovereign bond funds during June and July.

Floating Rate

Neutral exposure to floating rate instruments, particularly global high yield credit given very tight spreads. Year-to-date equities continue to outperform fixed income, and credit markets continue to outperform government bonds, but the pace of outperformance has declined meaningfully compared to calendar year 2023 and 2024.

Although Floating Rate Notes (FRNs) have less interest rate (duration) risk than fixed-rate bonds, they still carry credit risk. If the underlying issuers face pressure (e.g., in a weaker growth environment), FRNs may suffer via spread widening. In addition, with the expectation that short-term interest rates will continue to decline, the coupon reset mechanism becomes less attractive.

Bank hybrids, despite their yield premium, face growing scrutiny around capital structure complexity and regulatory headwinds, making them less attractive on a risk-adjusted basis.



Currency



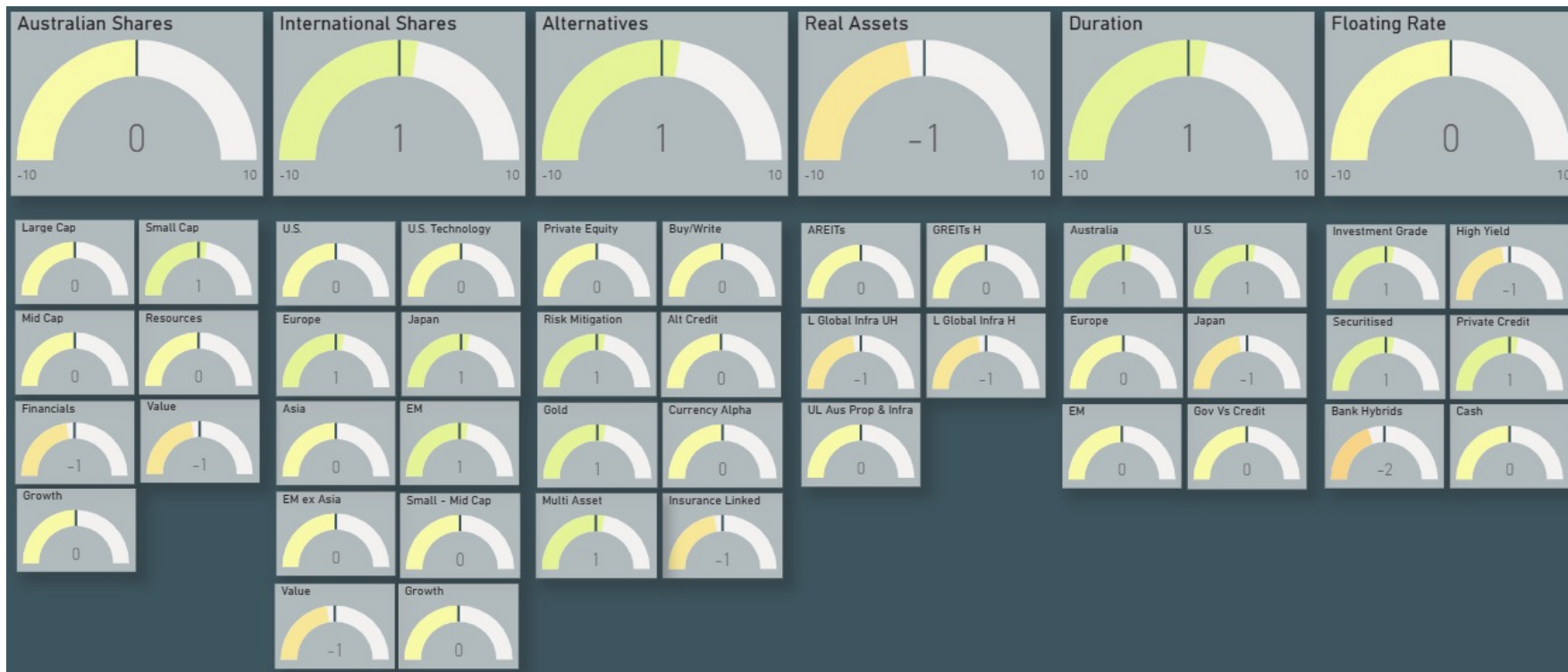
Increase hedging position from neutral to marginally overweight on currency, based on a measured view of relative growth, interest rate differentials, and risk sentiment across major economies.

When the Australian dollar (AUD) rallies versus the USD, unhedged overseas investments (which are USD-denominated) can lose value in AUD terms. A unique feature of investing in Australia is how our dollar responds to global economic conditions. When global markets struggle, the AUD usually weakens. This happens because the Australian economy is closely tied to commodity prices, which tend to fall during tough market conditions. The AUD is currently relatively low versus long-term averages, which suggests some potential for appreciation (making hedging more attractive).

Table 1:

Summary TAA positions – Q4 2025

12 Month Relative Value Summary - Q4 2025



12 Month Relative Summary (Q4 2025). Refer to **Table 1 for Summary TAA positions - Q4 2025**. The recommendations shown in the summary are Atchison's conviction away from the SAA, therefore should not be interpreted as a recommended percentage change.

Important information

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