Report:

Monthly Commentary

June 2025

Paradice Australian Equities Fund

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Market Review

Despite a turbulent start, the S&P 500 (in USD) and the S&P/ASX 200 (in AUD) Total Return Index staged an impressive rally, up by 10.9% and 9.5% respectively during the quarter. The market climbed a wall of worries, including elevated tariff uncertainty, geopolitical instability with Israel launching an attack on Iran, and simmering concerns over the ballooning US fiscal debt.

The S&P/ASX 200 was led by Information Technology, which rose by 28% as the market swung back towards AI. Financials were +15% led by CBA which rose to an all-time high. Materials (0.7%) and Utilities (+2.0%) and other low beta names lagged.

The Bloomberg Commodities index declined 3.1% (in USD). Gold leapt 5.8% (in USD) as a safety trade against economic uncertainty and on central bank demand, and Copper and Aluminium followed, rising by 3.8% and 3.3% respectively (both in USD). Despite heighted volatility due to the Middle East conflict, the Brent closed the quarter -9.5% (in USD).

The USD continues to edge lower, down –7.0% for the quarter. As previously discussed, investors may be concerned about 1) Fiscal concerns around US debt which is exacerbated as foreign investors reduce holdings of Treasury bond, forcing issuances at possibly higher rates. 2) Weakening investor confidence due to political instability and trade uncertainty; and 3) Rising share of alternatives to the USD.

We had been expecting stagflation: a combination of higher price pressures and weaker growth. Those expectations have not manifested in hard data. The CPI has remained steady, while US non-farm payrolls[1] surprised to the high side. This could still be pending; most countries have enjoyed a tariff reprieve until the Trump administration's July 9 deadline.

Performance

The Fund returned 7.16% for the June quarter, underperforming the benchmark of 9.50% by 2.34%.

[1] Source: US Bureau of Labour Statistics

Contributors/Detractors

Positives

- **Santos (STO) – Overweight:** Rose on higher oil prices and takeover offer from an Abu Dhabi led consortium.
- **Catapult (CAT) – Overweight:** Rose on a solid result and tech rally
- **Newmont (NEM) – Overweight:** Rose on higher gold prices
- **Woodside (WDS) – Underweight:** Underperformed the broader rally. The portfolio closed the underweight during the quarter as Middle East conflict triggered a spike in oil prices.
- **Rio Tinto (RIO) – Underweight:** Iron ore prices underperformed and the CEO announced his pending departure.

Negatives

- **Commonwealth Bank (CBA) – Underweight:** CBA continued to rally on minimal earnings changes.
- **Treasury Wine (TWE) – Overweight:** US wine demand continues to be soft. The impact Trump's tariffs may have on consumer spending also weighed on sentiment.
- **Ansell (ANN) – Overweight:** Declined on tariff impact and anticipated industrial slowdown
- **Block (XYZ) – Overweight:** Declined on lowered 2Q25 guidance, portfolio weight was trimmed.
- **Alcoa (AAI) – Overweight:** Tariff impacted and expectations of lower aluminium demand due to slower growth

Portfolio Changes

Purchases

- **National Australia Bank (NAB**): Increased to manage overall Financials position and risk
- **Commonwealth Bank (CBA):** Increased to manage overall Financials position and risk
- **Xero (XRO):** Increased on increased confidence around subscriber and Average Revenue Per User (ARPU) growth
- **Santos (STO):** Increased on higher oil price expectations in light of Middle East conflict
- **Cleanaway (CWY):** New position, on confidence around improved earnings trajectory

Sales

- **Newmont (NEM):** Trimmed on outperformance and some signs of tariff uncertainty unwinding.
- **CSL (CSL):** Reduced on weakening flu vaccine backdrop and impact of potential tariffs on plasma
- **QBE (QBE):** Reduced on moderating global premium environment
- **BHP (BHP):** Reduced on lower iron ore prices
- **Block (XYZ):** Reduced on lowered 2Q25 gross profit outlook

Outlook and Positioning

Markets have rallied strongly over the last quarter as they increasingly discount USA tariff related negotiations as more rhetoric than long lasting policy. Whilst this may be true over the long term, in the short term there are still plenty of deals to be concluded, many of which will inevitably settle at higher tariffs than those in effect prior to Trump 2.0. These tariffs should have a negative effect on economic activity in the USA and abroad given they are a transfer of wealth from private to public (USA government) with the ultimate effect depending on the size of the tariffs.

Any tariff related impacts could, however, be offset by a faster pace of interest rate cuts from the US Federal Reserve (Fed) if they chose to look through any tariff induced inflation as short-term noise. In any case an expectation of decelerating economic growth in the 2nd half of 2025 will require the Fed to cut rates especially if relatively expensive equity markets are to be supported at current or higher levels. If the Fed cuts 3 times in 2025, as the rates market currently expects, then equity markets may look through any short-term economic slowdown and keep charging into 2026. Historically though, buying the S&P500 on greater than the current 22x PE has not yielded good long-term returns for investors so some caution is likely warranted for now.

In Australia, a pending RBA rate cutting cycle should support domestic cyclicals and potentially see the private sector do some of the heavy lifting which for the last couple of years has been the sole domain of the government sector. With the market trading at 19x forward earnings, cheaper money-courtesy of RBA rate cuts may be exactly what’s needed to sustain elevated earnings multiples over the next 12 months.

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