Report:

Monthly Commentary

May 2025

Paradice Australian Equities Fund

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Market Review

The S&P/ASX 300 Total Return Index rebounded 4.2% over May 2025, supported by easing trade tensions. The S&P500 Total Return Index meanwhile rose 6.3% (in USD) during the month.

Global trade relationships and tariffs remain a moving target as the USA attempts to reset trade relations with all major trading partners simultaneously. The USD failed to recover and was flat over the month, as concerns mounted that Trump's erratic policy decisions may have damaged the U.S. dollar's reserve status. Gold was also flat over the month as investors sought safe-haven assets.

Across the ASX200, Information Technology was the best performing sector +19.8%, underpinned by stocks such as Life 360, Technology One and Xero. Utilities, Consumer Staples and Health Care were laggards.

In Australia the RBA cut rates by 25bps to 3.85% noting that inflation is within the target range whilst citing weaker global growth as a potential risk. Three more rate cuts are anticipated before the end of 2025 by the bond market. The 2025 Australian federal election reaffirmed the Australian Labour Party in a landslide victory. Overall government policies are modestly stimulatory and reflect Labour's continued push towards lowering cost of living (e.g. extending energy rebates, bulk billing expansion). The Fair Work Commission also announced a 3.5% increase in the national minimum wage effective 1 July 2025. This covers approximately 20% of the Australian work force and importantly ensures real wage growth above inflation.

Performance

The Paradice Australian Equities Fund was down 39ps net of fees vs the benchmark[1] for the month of May 2025. Top 3 contributors were Catapult, Seek and Qantas (all overweight position). Top 3 detractors were Treasury Wine Estate, Newmont and Block (all overweight).

[1] Benchmark is the S&P/ASX 200 Total Return Index

Noteworthy industry / macro developments

#1 USD under pressure, safe haven status challenged

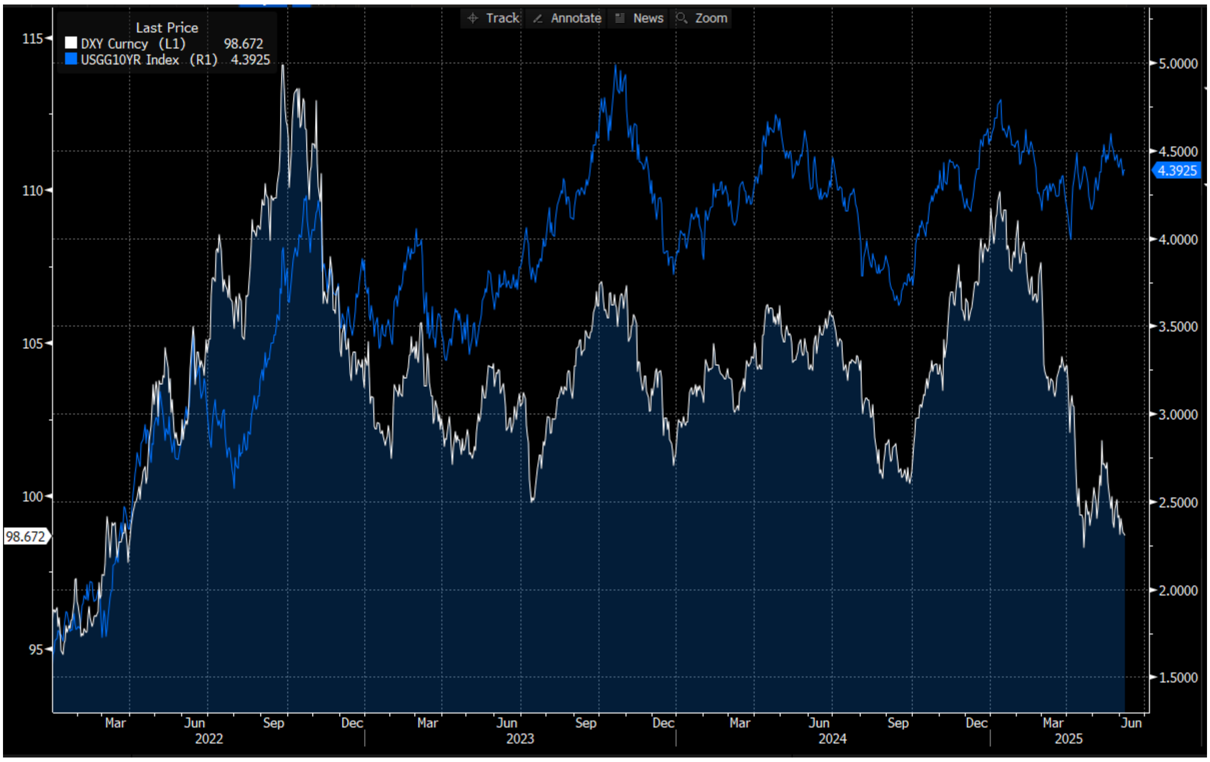
Despite a sharp rebound in global equities, with the S&P500 rising to within 3% of all-time high (reached in Feb-25), the USD has persistently faced downward pressure.

The following chart shows the relationship between the US 10-year government bond yield (blue line) and the USD (white line). Whilst there has been somewhat of a loose correlation historically, there has been a clear divergence to date in 2025.

Several reasons likely drive this:

1) **Fiscal concerns around US debt:** The national debt surpassed US$35 trillion, just as cUS$9 trillion will be refinanced in 2025 against a backdrop of higher US interest rates. US interest payments are likely to rise to cUS$1 trillion in 2025, amplifying an already sizeable fiscal gap. This is exacerbated as foreign investors reduce holdings of Treasury bonds, forcing issuances at possibly higher rates.
2) **Weakening investor confidence due to political instability and trade uncertainty**: Inconsistent and unpredictable trade policies are creating market unpredictability. We note Moody's Ratings became the third and final credit rating to downgrade the U.S. government's debt from its top rating by one notch from Aaa to Aa1.
3) **Rising share of alternatives to the USD:** The dollar's share of global foreign exchange reserves has been declining from over 70% in 2000 to 58% as at the end of 2024[2], reflecting a gradual shift towards alternatives like the euro, yuan and gold. Geopolitical shifts such as sanctions on Russia, and US-China tensions have accelerated efforts by nations to diversify away from dollar dependency, undermining its dominance. A lower USD makes imports more expensive and possibly exacerbates inflationary pressures in the US.

[2] IMF Foreign Exchange Holdings in US Dollars (Not Seasonally Adjusted)



Source: US Dollar Index versus US Generic Government 10 year Index, Bloomberg, 6 June 2025

#2. Possible reallocation of capital flow away from US to Rest of the World

According to a recent report, which cited EPFR data, there have been cUS$2.5 trillion inflows to US assets (treasuries, corporate bonds), and US$1.3 trillion inflows into US stocks alone since 2020. The Fed Flow of Funds showed foreign investors owning sizeable levels of US stocks . This may mean that a small reallocation away from US stocks could have a positive impact on other global markets including Australia. Anecdotally this could be a factor driving up share prices of large, liquid Australian companies such as Commonwealth Bank and Wesfarmers.

#3. Troughing office market?

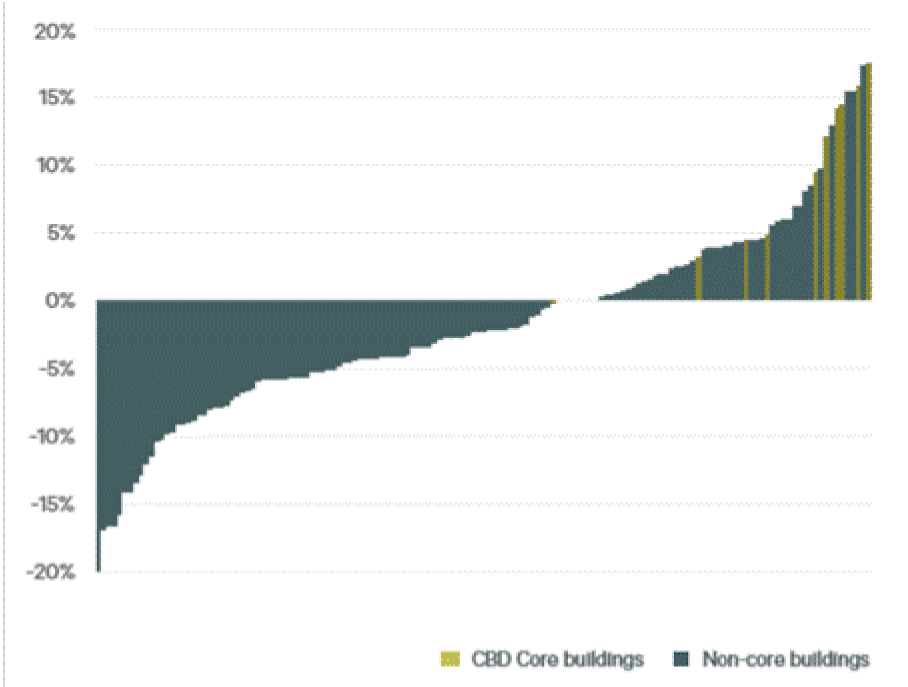
The Australian office market has been confronted with a valuation declines of up to 25% since their peak in 2022, reflecting factors such as high interest rates, low occupancy due to work from home and oversupply.

We are cautiously optimistic the office market has broadly troughed, with most listed REITs reporting an office cap rate of 6.0-6.5%, c200-250bps above the Australian 10-year government bond yield, in line with the historical premium.

However, as the following chart from CBRE shows, there is extreme bifurcation in net effective rent growth depending on whether the building is super prime (key streets of the CBD), A grade or B grade. Positively, whilst incentives and refurbishment costs remain high, the bid ask spread for office transactions have narrowed and we expect to see the return of transaction activity.

As such we remain selective in picking office REITs, with a focus on asset quality and sustainable cashflow.

Sydney Net Effective Rent Growth over 2024, by building



Source: CBRE

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