The Linara Lens

Our perspective and insight

Markets in October: brought renewed market volatility as U.S.–China trade tensions escalated, the Federal Reserve struck a more hawkish tone, and reports of rising U.S. credit stress unsettled investors. Japan's equities rallied sharply following Sanae Takaichi's surprise election as LDP leader, while sentiment globally improved toward month-end on resilient earnings and continued enthusiasm for artificial intelligence (AI).

Global equities advanced, with the MSCI World Index up 2.0% and Emerging Markets up 4.2%. Technology outperformed, with the MSCI World IT sector gaining 6.5% and the NASDAQ 100 up 4.8%. Growth sectors led, while Defensives and Energy lagged. Japan's Nikkei 225 surged 16.7% on yen weakness, contrasting with China's Hang Seng, down 3.5% on renewed policy uncertainty. In Australia, the S&P/ASX 200 rose just 0.4% as stronger inflation data reduced RBA easing expectations. Materials and Resources outperformed, while Health Care and Consumer sectors declined. Gold broke above USD 4,000/oz on safe-haven demand, while oil prices softened on oversupply concerns.

Megacap Leadership: The "Magnificent Seven" - Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia, and Tesla - once again dominated U.S. equity performance, accounting for most of the S&P 500's October gains. Their combined weight now represents roughly one-third of the index, the highest in decades. Robust earnings and continued AI optimism supported valuations, but narrow leadership underscores market fragility. For investors, diversification away from this concentrated core remains prudent as the cycle matures.

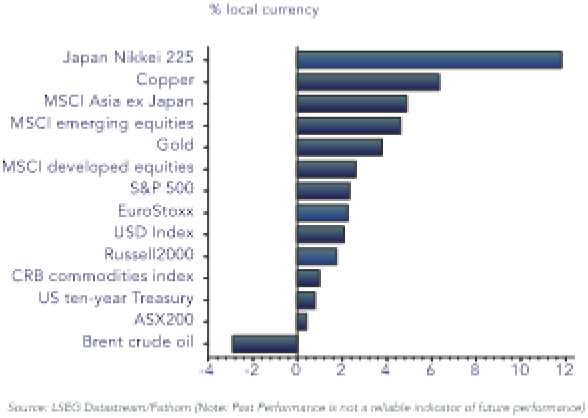
Outlook: Technology and AI remain central to market performance, underpinned by investment in semiconductors, cloud infrastructure, and generative AI. However, valuations among U.S. megacaps leave little room for earnings disappointment. Beyond the U.S., opportunities are broadening across Asia, where semiconductor demand and AI supply-chain growth support a more diversified technology story. Japan's policy optimism contrasts with China's weaker growth, highlighting increasing regional divergence. A softer USD and lower global rates should continue to favour Asian and emerging markets.

How to Position: Policy divergence remains key. The Fed's uncertain easing path and RBA's hawkish stance will drive volatility and sector dispersion. In Australia, value-add property and active credit strategies remain preferred. Investment-grade credit offers relative safety, while caution is warranted in private credit following ASIC's push for greater transparency. We continue to favour selective exposure to technology and infrastructure linked to AI, small and mid-cap Australian equities, and growth alternatives such as hedge funds and private equity, while maintaining hedges against a rising AUD.

Markets in October

October was marked by a series of unexpected developments: escalating U.S. & China trade tensions, a hawkish turn from the U.S. Federal Reserve (Fed), headlines about rising credit stress and auto dealer bankruptcies in the U.S., and Sanae Takaichi's surprise election win as leader of Japan's Liberal Democratic Party (LDP). These events contributed to a choppy month for markets, though sentiment improved toward month-end.

Chart 1: October Asset Class Performance

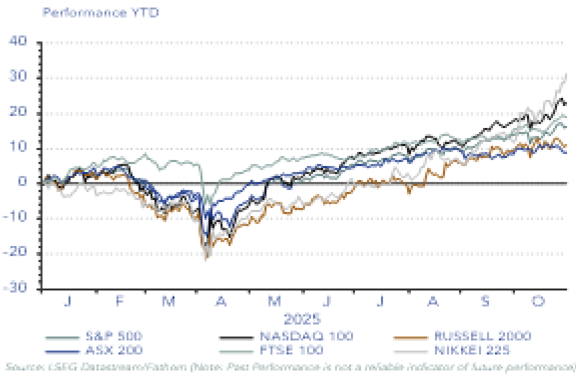


Global equities posted solid gains in October, with the MSCI World Index up 2.0% and the MSCI Emerging Markets Index rising 4.2%. Performance was supported by strong earnings and continued enthusiasm for AI and technology investment, though market leadership remains increasingly concentrated in megacap tech names.

Technology was again the standout globally, with the MSCI World IT sector surging 6.5%, while the NASDAQ 100 gained 4.8%. Growth sectors outperformed, with the S&P 500 Growth Index up 3.4%, compared to just 1.1% for Value. Defensive sectors such as Consumer Staples (-2.3%) and Real Estate (-2.6%) lagged, while Energy (-1.1%) also underperformed amid weaker oil prices.

Japan's Nikkei 225 delivered a remarkable 16.7% gain, supported by policy optimism and a weaker yen. In contrast, China's Hang Seng fell 3.5% as renewed trade tensions and policy uncertainty weighed on sentiment. European markets posted moderate gains, with the FTSE 100 up 4.1% and the STOXX Europe 600 up 2.6%.

Chart 2: Selected Equity Markets Relative Performance (0 = 1 Jan 2025)



Australian equities were more muted, with the S&P/ASX 200 up just 0.4% as hotter-than-expected inflation data dampened hopes for near-term RBA easing. Sector performance was mixed: Materials (+4.3%) and Resources (+4.0%) led gains, buoyed by critical minerals optimism. Health Care (-4.8%) underperformed sharply. Consumer sectors were weak, with Consumer Discretionary down 6.8% and Consumer Services down 7.1%. Small caps delivered strong gains, with ASX Small Resources up 3.1%, and Small Industrials rose 1.4%, both outperforming large-cap peers.

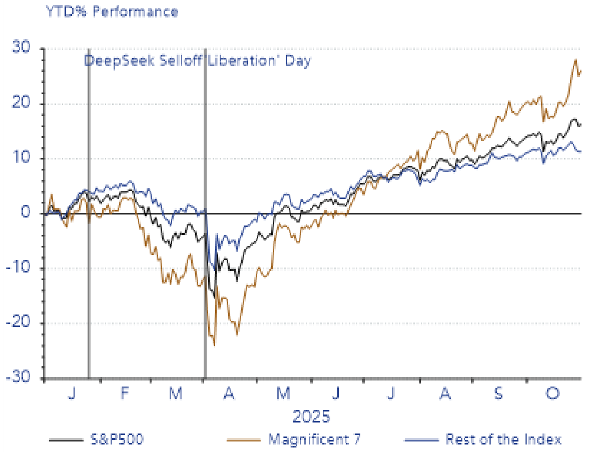
Commodities rose with gold breaking above USD 4,000/oz on safe-haven demand and central bank buying. Oil prices fell (WTI -4%, Brent -2%) on oversupply concerns before stabilising on new sanctions and improved trade sentiment.

Key Themes

Megacaps dominant again

The "Magnificent Seven" (Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia, and Tesla) extended their dominance in October, driving much of the S&P 500's monthly gain. Strong quarterly results and continued enthusiasm for artificial intelligence and cloud infrastructure pushed several of these stocks to new highs, reinforcing their leadership within global equity markets. Collectively, the group now accounts for roughly one-third of the S&P 500's total market capitalisation — a concentration level not seen in more than five decades.

Chart 4: 'Mag Seven' v S&P 500 v bottom 493



Source: LSEG Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

This concentration reflects both genuine earnings strength and investor confidence in the long-term growth potential of these companies. However, it also highlights a growing imbalance in market dynamics. Index performance is increasingly dependent on the outlook for a small number of technology-driven firms, leaving the broader market vulnerable to any shifts in sentiment or slowdown in their earnings momentum.

While the Magnificent Seven continue to set the pace for equity markets, their dominance raises important questions about market breadth and diversification. For investors, understanding how much portfolio performance is tied to this narrow leadership will be key as markets navigate the next phase of the economic and interest-rate cycle

Chart 4: 'Mag Seven' market cap share of S&P 500

Source: LSEG Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Outlook

Looking ahead, technology and AI are likely to remain key drivers of global equity markets, supported by ongoing investment in cloud infrastructure, semiconductors, and generative AI. However, the market's heavy reliance on US mega-cap tech stocks introduces fragility. Valuations remain demanding, and earnings expectations leave little room for disappointment, suggesting investors should consider where future growth leadership may broaden out.

Opportunities in technology are not confined to the US. Asian markets are benefiting from strong semiconductor demand, advanced manufacturing, and the build-out of AI-related supply chains. In October, several of these markets delivered solid performance, even as China continued to lag on weaker growth and policy uncertainty.

This growing regional divergence highlights the importance of diversification within the technology theme. We believe that clients should look to complement US mega-cap exposure with selective positions in Asia's technology and industrial leaders, which combine structural growth potential with more attractive valuations. A broader geographic and sectoral approach can help balance concentration risk while maintaining exposure to the powerful long-term trends driving global innovation.

More broadly, we believe conditions remain largely supportive of Asian and emerging markets exposures with a weaker USD and lower interest rates providing solid tail winds.

How to Position

Defensive

Central bank policy divergence remains a defining feature of the global macro landscape. The Federal Reserve's split FOMC and debate over the pace of future easing will keep U.S. monetary policy in flux, heightening volatility and the risk of abrupt market repricing. Any shift in consensus or signs of political interference could have outsized effects on risk assets and currencies.

In Australia, the RBA's hawkish tone and stubborn inflation have reduced the likelihood of near-term rate cuts. This has important implications for rate-sensitive sectors and **property** markets: cap rate compression is not a given, and actively managed, value-add strategies remain the most compelling approach, in our view. Sector dispersion is likely to be high, reinforcing the need for selectivity.

Credit spreads remain tight versus historical levels, and while recent defaults in the U.S. auto industry and knock-on impacts on banks appear isolated, they highlight latent risks in leveraged segments. We continue to prefer investment-grade, high-quality credit exposures implemented through managed strategies, while remaining cautious on private credit where ASIC has released its findings into the industry, calling for better transparency and more consistency. Regulatory scrutiny in this space is welcome and overdue.

Growth

Developed equity markets continue to grind higher, but leadership is increasingly concentrated in megacap technology and AI-related names. This reliance on sustained AI investment is a significant assumption, profitability and margin expansion have yet to materialise, leaving equities vulnerable to a pullback if spending slows.

Emerging markets remain attractive, particularly in Asia's technology and industrial sectors, though China faces structural headwinds and weaker growth. Regional and sectoral differentiation is becoming more important; broad global beta exposure may no longer suffice. In **Australia, we favour small and mid-cap strategies** over expensive large caps with lower earnings growth.

Growth **alternatives** such as hedge funds are finding more supportive conditions as single-stock volatility and dispersion create opportunities for long/short strategies. **Listed property and infrastructure** remain of interest, especially assets tied to AI-driven demand such as data centres and U.S. utilities supporting compute power expansion.

We see any U.S. dollar strength as fleeting and continue to hedge against a rising AUD. Conditions for private equity across venture, growth, and buyout remain solid, particularly for new capital, with valuations less demanding than public markets.

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