

Fisher Funds IMA Model Portfolios

Quarterly Report September 2025



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Artificial Intelligence stocks lead markets to all-time highs – is a bubble brewing?

Ashley Gardyne, Chief Investment Officer

In Q3 of 2025, equity markets surged to successive all-time highs, powered by unrelenting enthusiasm for artificial intelligence (AI) and reinforced by central banks pivoting towards easier policy. The rebound since President Trump's initial tariff announcements has been one of the fastest on record. Yet behind the euphoria, questions remain: are the dizzying gains of AI-linked companies and the promise of policy support enough to justify the pace of the rally, or are investors at risk of inflating another bubble like we saw in the dot-com era?

Markets continue to set new all-time highs

Global equities powered higher in Q3, staging one of its fastest rebounds ever as the second-quarter's volatility faded quickly into the rearview mirror. Since the April lows, global stocks have climbed 33%. September provided the standout moment: all four major US indices – the S&P 500, Nasdaq-100, Dow Jones and Russell 2000 – closed at record highs on the same day. It was the first time this has happened since 2021, and only the 25th occurrence this century. The strength was not limited to the US (+7.8% in Q3), with European markets up 2.8% and NZ stocks climbing 4.5% over the quarter.

Although leadership remained anchored in AI-linked companies, the rally showed welcome signs of broadening. US small-cap stocks (+12.0%) advanced alongside the mega-cap Magnificent 7 (+17.6%), supported by resilient economic data and the US Federal Reserve's first rate cut since December – a move that also signalled more easing could follow.

Fundamentals are hanging in better than expected

Economic fundamentals held up better than many anticipated. US GDP grew at a healthy annualised pace of 3.8%, while key inflation measures eased modestly, giving the US Federal Reserve (Fed) some breathing room as labour market momentum cooled. Concerns of a renewed tariff shock also failed to materialise, with markets now largely desensitised to policy announcements

like those that caused sharp swings earlier in the year. Corporate earnings comfortably exceeded expectations, with large-cap technology once again leading the way. Alphabet surged 38% in Q3, Oracle gained 29%, and Nvidia advanced 18% – underscoring how central the sector remains to market momentum.

The main wrinkle came from employment. The US labour market clearly showed signs of slowing throughout the quarter. Paradoxically, investors took this as good news: softer jobs data became the catalyst for the Fed's policy pivot. At its September meeting, the US central bank cut rates for the first time since December, emphasising the move was 'non-recessionary' – designed to sustain growth rather than counter a downturn.

The picture in NZ was starkly different. GDP contracted by 0.9%, well below expectations – and far weaker than the growth seen across major economies. The Reserve Bank of New Zealand (RBNZ) cut the Official Cash Rate (OCR) twice during the quarter. Also, with the GDP report misaligned to earlier forecasts, markets are now pricing in the prospect of much more easing ahead. As in the US, the promise of looser policy outweighed weak fundamentals and helped lift NZ equities, even as the domestic economy continued to lag global peers.

We have refreshed our portfolios

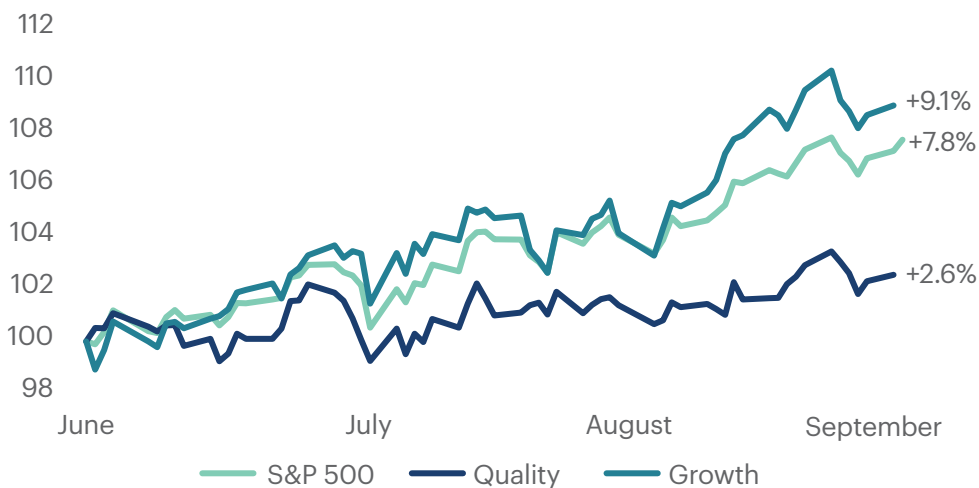
Against a backdrop of exuberant markets, our premium equity portfolios underperformed in Q3. Some of this reflected stock specific factors, as covered in the individual fund updates below. More broadly, our cautious stance on AI valuations limited participation in the sharp rally, particularly in chipmakers – an area that has historically proven highly cyclical and volatile. Our focus on high-quality companies, instead of chasing those with the strongest share price momentum, can result in underperformance during periods of 'animal spirits' in markets, as we have seen recently.

Our overweight to healthcare – sector that has long been a good hunting ground for us – was another headwind. Healthcare has been the weakest performing sector this year, pressured partly by policy uncertainty in the US, but also as a result of

investors exiting more defensive stocks to chase hotter parts of the market. Quality-oriented stocks, which are a hallmark of our investment style, also lagged more speculative parts of the market. By 'quality', we mean companies with strong balance

sheets, durable competitive positions, and reliable profits – characteristics captured by the S&P 500 Index below. As the chart illustrates, quality has trailed growth materially in recent months, weighing on the relative performance of our portfolios.

Quality Underperformed Growth In Q3



Source: Bloomberg

Importantly, we have not stood still. Throughout the quarter, we made a range of portfolio adjustments – adding new positions, rebalancing exposures, and exiting selected companies. We believe that these changes, combined with our disciplined approach,

leave us well positioned as we look ahead. While quality may be out of favour in the current risk-seeking environment, history shows that it has won over the long run, ultimately delivering higher and less volatile returns.

Quality Companies Win In The Long Run



Source: Bloomberg

Is an AI bubble brewing?

We are spending considerable time assessing how much of the recent strength in AI beneficiaries is fundamentally justified, and how much may reflect overexuberance and a growing bubble. Examples of such beneficiaries are semiconductor stocks (for example, both Nvidia and Broadcom), software players like Palantir, datacentre players like Oracle, and independent power producers that have rallied due to surging electricity needs.

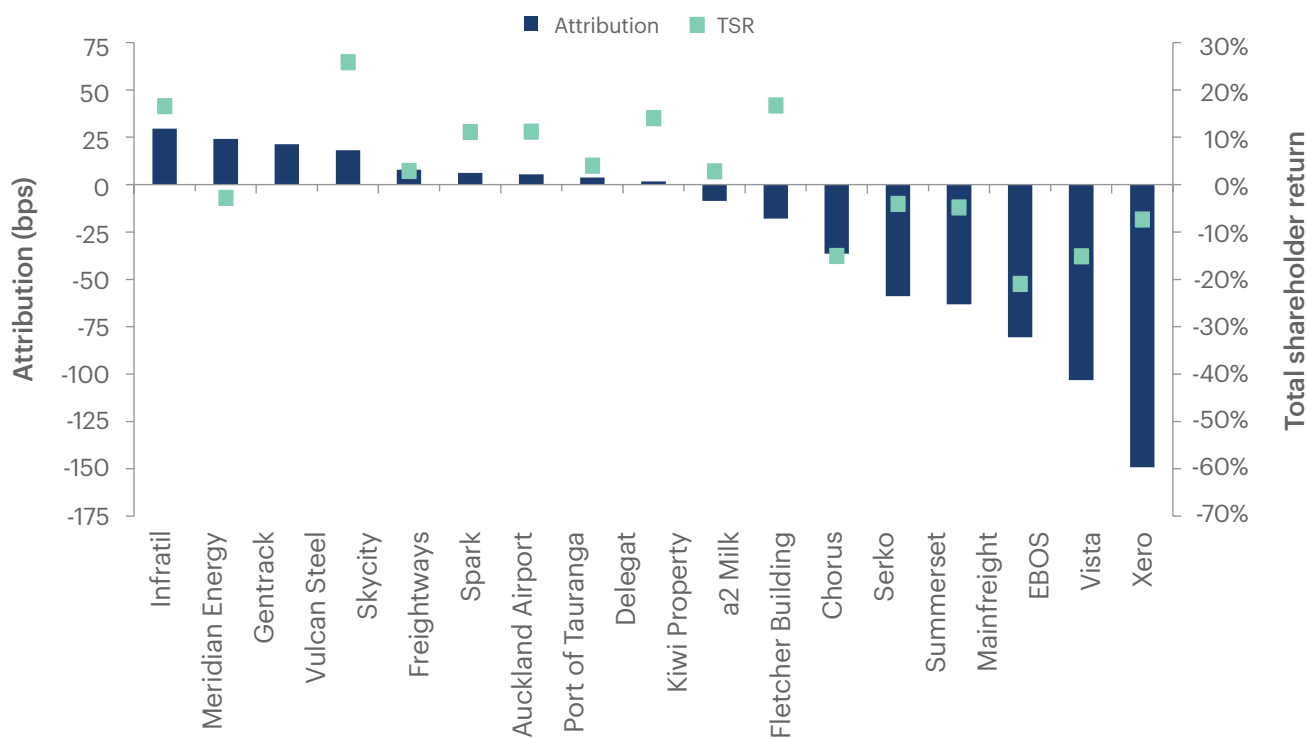
There is no question that generative AI is a game changer for some businesses, and that it is likely to become more ingrained in our everyday lives. But, as with the build-out of fibreoptic networks in the late 1990s, there are legitimate questions about how much of the datacentre and AI capacity being built will ultimately be needed, the return on the capital being deployed, and whether the high-growth assumptions embedded in many of the 'AI beneficiary' companies are sustainable.

As the dot-com era demonstrated, the promise of a transformative technology does not automatically translate into strong investment outcomes. Not every AI-related company will prove to be a winner.

In today's environment, selectivity is key. Investors need to be careful about which parts of the market they invest in – distinguishing between companies with durable, monetisable advantages and those whose valuations may be driven more by hype than by fundamentals.

Breadth returns to NZ stocks while the economy finds a floor

Matt Peek, Portfolio Manager, New Zealand Equities



Source: Bloomberg

The benchmark saw 75% of companies deliver positive returns, and 22 of the S&P/NZX 50 deliver returns of around +10% or greater in the quarter. This marked a sharp reversal from the previous two years to June, where the portfolio companies delivered a +26% return on average versus the benchmark of only +8% (based on current weightings).

Market Backdrop

The benchmark performance included a quarter of strong returns from some sectors we don't have exposure to, such as commercial property (+15% in the quarter) and regulated utilities, as we think future returns will be modest over the long term. This was after the RBNZ showed appetite to cut interest rates more than anticipated given weak local economic conditions, which makes those sectors a more favourable proposition for retail

investors hunting yield compared to term deposits.

The benchmark's rally came despite most companies continuing to exhibit weak fundamentals, as expectations of company earnings across most sectors were further reduced during the quarter. New Zealand is showing some signs of economic activity finally plateauing at low levels, although the jury is still out about the strength of any recovery.

Portfolio Commentary

EBOS and Vista were sold off after reporting results, with near-term investment constraining profits

When global markets are rocked by international Healthcare and pet product distributor **EBOS** (-21% in the quarter) delivered a slightly softer fully year result than expected, and guided for a core operating profit (EBITDA) growth of +7% in the

new financial year. Yet, when combined with the additional lease impost of the expanded facilities (not been previously flagged), this result translates to a year of unexpected flat profits before growth is expected to resume as use of the excess capacity picks up. EBOS has been a predictable grower in recent years. So, the combination of multiple unexpected disappointments saw the share price fall sharply. It was unfortunate that delivery of the disappointing message was left to the incoming CEO, and we expect credibility will return over time.

Cinema software company **Vista's** (-15%) result showed solid year-on-year growth in most metrics, but a key surprise was the company announcing it will increase costs over the short term, to accelerate migration of customers to its new cloud product suite in response to demand. This migration will suck up cashflow over the next few years, just at the point the company is poised to generate strong growth after a prolonged investment phase.

The upside of this situation is that the company should have a higher proportion of existing customers on its higher-value products earlier. The company also provided details of its plans to launch embedded payment functionality, which will be of particular benefit to its smaller customers. The company can do this in an efficient way that outsources much of the payment processing to specialist providers, and means low-cost yet recurring revenues will likely grow to over \$15m at very high additional profit margin.

Several of our domestic economy recovery exposures performed well

Three of the better performers in the portfolio were Vulcan Steel (+32%), Freightways (+26%) and Port of Tauranga (+11%).

Steel distributor Vulcan Steel delivered a trading update and full year result similar to expectations, with daily volumes stabilising towards the end of the financial year and signs of improvement in some sectors. Vulcan also announced the acquisition of Roofing Industries, a privately owned business with a leading position in the New Zealand steel roofing and cladding market.

Roofing Industries has a similar culture and business model to Vulcan, with strong focus on customer service, low cost base, and strong focus on efficiency enabled by technology. The acquisition price is attractive relative to its earnings, and the fit of the business means Vulcan should be able to derive some benefits from procurement in greater scale and, in some instances, bundling the product offerings to joint customers to gain greater share of wallet. We participated in the share issue to fund the acquisition.

Local express logistics operator Freightways has defied the softer economy until now. The company has been able to pick up market share and benefited

from some price increases, including its ongoing 'pricing for effort' programme. Faint green shoots do seem to be appearing, with same-customer network courier volumes in New Zealand improving in the last six months to June (+0.6% growth) versus the previous six months (-0.2% decline). As to the economic backdrop, CEO Mark Troughear has commented, 'I think we are through the worst of it. It's been a slow and steady grind upwards'.

As noted earlier, these positive returns were offset by weakness in the Mainfreight (-5%) and Summerset (-4%) share prices, despite our expectation that both companies will benefit from a cyclical recovery in New Zealand.

In July, Mainfreight provided a trading update that showed an unexpectedly large fall in Profit Before Tax. The company referenced the shorter trading weeks in April and May and tariff uncertainty during the period, and alluded to trading improving into June and July, although the company provided no figures to quantify this. More recently, in late September, CEO Don Braid commented, 'we are seeing better performance than we did three months ago'.

Retirement operator Summerset continues to see growth in unit sales volumes. The company also shared forecasts for over \$12.30 of future net tangible assets a share from current developments, versus the 30 June figure of \$13.18, and a quarter-end share price of \$10.68. This fluctuation reinforces our thesis that the current share price does not adequately reflect the strong value uplift expected from current development, despite Summerset's strong track record.

Xero and Infratil showcased strong fundamental outlooks at investor events

Xero (-7%) has seen its share price fall given no significant news during the quarter. Early in September, we attended the sold-out XeroCon in Brisbane. XeroCon is Xero's annual flagship technology and innovation conference for accountants, bookkeepers, and small businesses using its cloud accounting software. Hot on the heels of releasing over 300 product features in the past 12 months, Chief Product Officer Diya Jolly stole the spotlight, unveiling an additional 30 new launches targeted for the ANZ audience. With a bold vision to 'reimagine accounting through AI', these features aim to automate workflows, deliver actionable insights, and reflect extensive feedback from accountants and small business customers.

Over time, Xero aspires to automate 90% of manual accounting tasks while reinforcing its role as a trusted partner. As part of the event, Xero also hosted the investor community for a series of fireside chats with its executive leadership team,

including the CEO of Melio, the US payments platform Xero is acquiring. We came away reassured by the energy and cadence of product development, which we believe will continue to drive value for accountants and small businesses and, in turn, expand Xero's revenue opportunities. We were also again impressed by the depth and quality of the executive team across the Board. Management also stood by its near- and medium-term targets.

Infratil (+17%) hosted an investor day in Sydney, which showcased its portfolio of growth infrastructure investments. Its datacentre business CDC closed out the day with an upbeat presentation, foreshadowing major contract wins of which 100MW was announced just the following week. The announcement came as welcome relief after customer delays meant CDC had missed its

contracting targets in 2024. CDC has now secured 95% of the revenue it needs to deliver its target of doubling 2025 earnings by 2027.

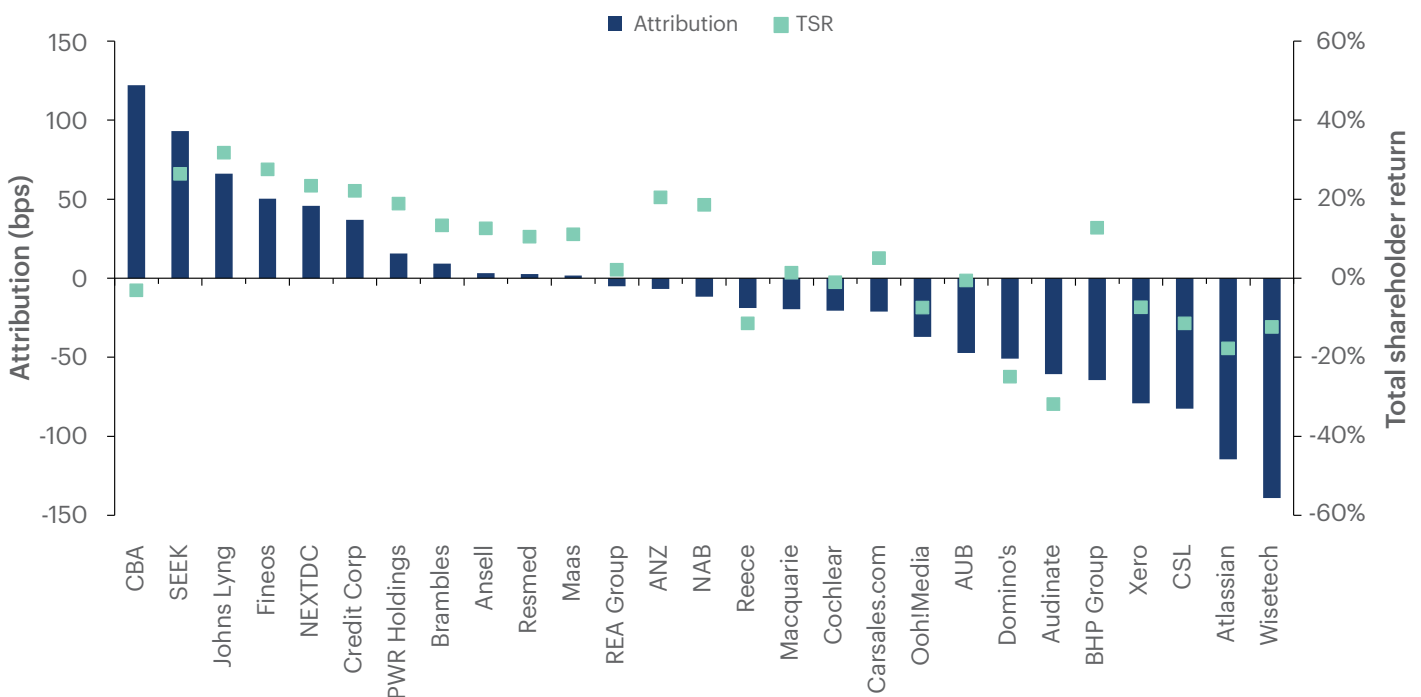
Longroad Energy, Infratil's developer of US renewable electricity projects, also provided a positive outlook. Despite changes to tax subsidies, Longroad is confident in its strong development pipeline, and its equity needs are similar to those expected before the changes.

Infratil's Asian renewable development platform Gurin, which is at a much earlier stage of development, also expressed confidence in its large pipeline of opportunities.

Infratil reiterated targets for selling off further assets which can't reach meaningful scale for its portfolio, which may include Australian diagnostic imaging business Qscan.

Patience vs. decisiveness: lessons from a volatile Australian earnings season

Robbie Urquhart, Senior Portfolio Manager, Australian Equities



Source: Bloomberg

Balancing when to be patient and when to be decisive – here are reflections from a volatile Q3. The Australian Premium Fund rose +1.3% in Q3, lagging the ASX200 benchmark index which rose +6.4%.

Portfolio Commentary

The semi-annual financial reporting season for ASX companies in August drove a wide dispersion of returns across ASX listed companies in Q3. This was one of the most volatile reporting seasons we can

remember in a long while. Notably, this volatility was also prevalent in share price moves of large, blue-chip listed companies, including portfolio holdings Brambles, CSL and SEEK (see below).

Management communication rather than the actual financial 'numbers' also amplified how the market reacted to earnings announcements. Poor communication from the likes of CSL, although painful in the short term, provide investors focused on the long term with opportunity as well.

Consequently, we have spent a lot of our work around the results season having many meetings with management teams after the results, parsing where the market has overreacted, and where the market has been justified in its reaction.

This work has informed the changes we made to our positions during Q3.

The virtue of being patient as an investor – when management teams are executing well

SEEK (+20% in Q3 in A\$) and Brambles (+7%) both delivered financial results in-line, and modestly ahead of expectation. Yet their share prices rocketed on the announcements, rising over 10% each on the day of the result. Positioning by institutional investors explains some of this move.

Both companies have long polarised investors for a variety of reasons. SEEK has had this effect partly because its relentless investment in initiatives (including a multi-year large technology overhaul) that will deliver growth in the longer term has led to an anaemic after-profit growth in recent years. In the case of Brambles, the market has questioned at times whether its business model is ripe for disruption (by plastic pallets for example). More generally, investors have questioned whether shareholders would see a decent return on money that Brambles has spent on productivity initiatives and technology enhancements.

To their credit, both companies have been clear and steadfast in their growth strategies, emphasising long-term value creation over the optics of delivering earnings or free cashflow growth in the short term. The financial results in August backed up their contention that shareholders will eventually reap the rewards of these growth strategies.

Despite a lethargic employment market, SEEK guided itself to FY26 revenue growth, exceeding cost growth (that is, profit growth is rising faster than revenue). Brambles has been steadily rewarded over the last few financial reporting seasons for consistency of delivery against clear management objectives. Importantly, in this result, Brambles noted that investments made in 'serialisation' trials (where pallets are uniquely identified) is yielding positive results. Serialisation may be rolled out across their larger markets, providing benefits to customers and Brambles alike. This action would

expand what is already a wide economic moat around the business.

On the other side of the performance ledger, Atlassian (-22%), Wisetech (-17%) and CSL (-16%), each of which is a large position in the portfolio, weighed meaningfully on our portfolio performance in Q3. In each case, we think these companies are focused on long-term shareholder value creation. Each company's financial results, although polarising for the market, demonstrated progress in driving towards long-term earnings growth and value creation.

We think these management teams are generally doing the right things (as SEEK and Brambles have done over the last few years). We think we will likewise be rewarded in time as shareholders for this. We have consequently taken advantage of the share price falls and added to our positions.

Atlassian's software helps teams across businesses to manage, track and improve the efficiency of their workflows. The market is concerned that its software will be disrupted by artificial intelligence (AI). This is the key reason for the share price weakness. We don't share this view, primarily because the software helps people in organisations work better together. It accelerates productivity. To the extent AI increases the rate of software development, Atlassian is a key enabler of this trend. The company's results were modestly ahead of expectations, and the company has guided for strong growth continuing into FY26.

Wisetech's core software revenue growth guidance for FY26 was solid at 14% to 21%, but lower than the market's expectation. Part of this relates to timing. Wisetech is rolling out new products that will only begin translating into meaningful revenue at the back end of the financial year. It is also changing the way it prices its software products. Longer term, we think this will be helpful in accelerating adoption of its products by customers.

CSL's result was modestly disappointing. In particular, although its profit margin continues to tick higher over time, the pace of improvement is lower than the market expected. The company is also re-organising its business structure and consolidating its research and development (R&D) functions. This likely delivers cost savings. Some of these savings may be reinvested in acquiring products in blood patient management that are already in development and showing promise. The idea is to then commercialise these products using CSL's global network (leveraging CSL's scale).

This approach makes sense to us and likely accelerates new product development compared to only undertaking research in-house. However, management muddled these messages with poor communication that accompanied the result. This left investors unclear on the growth strategy and longer-term growth prospects. Management has spent the last few weeks ironing out its messaging,

but a communication credibility gap remains. Importantly for us, CSL is confident it can grow revenue in the mid-to-high single digits (in %) each year over the medium term. The investment thesis remains intact.

The virtue of acting decisively – when a management team is not executing well

In contrast to these examples, we have also drawn a different key reflection from Q3. Through our shareholding in Domino's, we have seen the benefit of being more decisive in acting on a position (reducing or exiting) when management's performance wanes.

This is easier said than done.

Our investment process is centred on evaluating a range of factors in companies, management credibility and performance being a key factor. However, investment decision-making is complicated by a range of things. One complication is that we are long-term investors. As such, we do not want to 'duck' at shadows and at market overreaction to short-term headwinds in a company (reference the discussion about SEEK and Brambles above).

Another complication is that the market is forward looking. Missteps by management can be priced quickly by the market (that is, the share price falls). As long-term investors with a patient outlook, this quick pricing can prove to be a buying opportunity if confident that the missteps are an aberration, not a trend.

In a case like Domino's, a challenge we faced was that the poor performance was largely isolated to a few geographies (in their case, the pizza stores they had in Japan and France). A number of other core geographies have been performing well for them (such as Australia, Germany and the Benelux region).

In addition, by focusing on the valuation (another investment factor we consider), Domino's has screened cheaply. Biding our time while management 'righted the ship' in these problematic geographies seemed like the most sensible course of action.

Indeed, lack of progress in improving its performance in Japan and France saw the Domino's Board (led by chair and Domino's largest shareholder, Jack Cowin) take action – which we liked. They replaced the CEO in late 2024 with Mark van Dyck, who was tasked with overhauling the management team and improving operational efficiency across the company. He also took the hard decision in Japan to shrink the network by closing down uneconomic stores. This reversed the rapid expansion of the Domino's store network that took place during the COVID pandemic years which, in retrospect, was a poor decision.

Mark van Dyck began implementing these steps,

albeit not seemingly at the pace and scale that the Board was happy with. He resigned as CEO in Q3 and, on top of that, we noticed a continuation of lacklustre performance in the financial results delivered in August. We have been reducing our weighting in Domino's over time given these headwinds (as we wrote about in the Q2 investment update). However, the leadership team continues to be in flux and a new CEO needs to be found. Japan and France continue to struggle.

The remedies required for Domino's to return to durable earnings growth are, in our view, likely to take a long time.

So, in Q3 we took the decision to exit our small position in Domino's.

Quality, large-scale diversified miner (BHP) was added to the portfolio in Q3

BHP (+8%), the largest listed miner on the ASX, was removed from our investment exclusion list after consideration by the Environmental, Social and Governance (ESG) committee in June. It had been excluded because of its involvement in a tragic collapse of a tailings dam in 2015 at Samarco in Brazil where it mines iron ore in a joint venture with Brazilian miner Vale. The committee was satisfied that, 10 years on, BHP has taken sufficient steps (including substantial environmental and community remediation) to no longer be excluded from investment.

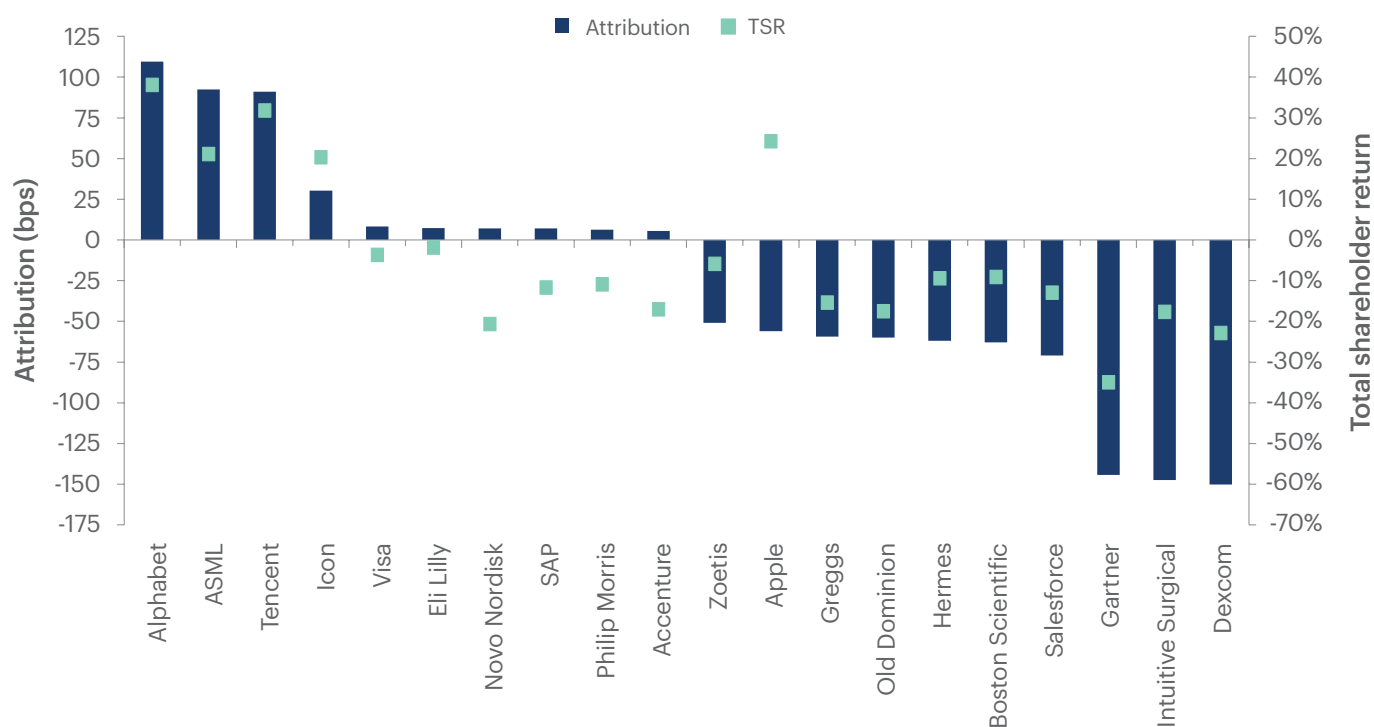
BHP is one of the highest-quality diversified miners in the world, with a focus on three key commodities: iron ore (essential for steel production), copper, and potash (a fertiliser for crops). While BHP's iron ore assets are mature, the other two commodities are both growth commodities. Potash benefits from structurally rising demand driven by population growth and rising standards of living. Long-term demand for copper is underpinned by the increased electrification and transition (decarbonisation) of the world economy.

BHP's moat is based on having some of the highest-quality assets globally in each of these categories. This coupled with BHP's scale enables it to operate at the low end of the global cost curve in each of these commodities – a great position to be in.

In terms of people, BHP has performed well during current CEO Mike Henry's tenure, and we note the recent appointment of Ross McEwan to BHP's Board as Chair. We think highly of Ross, based on our experience of being invested in NAB when he was CEO. We think he will ensure BHP remains disciplined in how it allocates its capital in the coming years.

AI build-out and easier policy drive Q3—healthcare overhang tests conviction

Sam Dickie, Senior Portfolio Manager, Global Equities



Source: Bloomberg

Global share markets had a solid quarter (+7%), driven by easing trade tensions, robust corporate earnings, optimism around artificial intelligence (AI), and expectations of monetary policy easing.

Market Backdrop

The best example of this enthusiasm towards AI was the 30% rise in one day in the Oracle share price during the quarter – OpenAI signed a \$300 billion (\$60 billion a year) contract with Oracle to house the accelerated computer chips to train OpenAI’s AI models. For context, OpenAI’s total revenue today is \$15 billion. And remember, the \$60 billion annual operating cost OpenAI committed to is only one of its many costs!

Portfolio performance lagged the benchmark significantly, primarily due to our exposure to the healthcare sector. It is rare to see sentiment so beaten down in a sector – healthcare has not been cheaper versus the broader market in 25 years. This manifested in the last few days, with our largest

healthcare weighting, Danaher, bouncing almost 20% in three days on the back of some ‘less bad’ news for its pharmaceutical customers on US drug pricing. We discuss the healthcare sector in detail below.

Portfolio Commentary

Our overweight position in healthcare was a drag again in Q3, with several of our large healthcare positions, including **Intuitive Surgical**, **Dexcom** and **Boston Scientific**, being among our worst performers.

Healthcare has been a strong performing sector over the long term, driven by an ageing population and technological advances in how we treat disease. Companies like Boston Scientific, which manufactures a range of innovative medical devices, has nearly tripled since we added it to the portfolio in 2020. However, with government budgets stretched post COVID, governments like those of the US are looking to put some pressure on rising healthcare costs. This has been most acutely felt in the pharmaceutical sector, which has negatively

impacted portfolio companies like Danaher and Icon that both provide products and services to these pharmaceutical companies.

In hindsight, we have underappreciated how long some of these headwinds would take to resolve and the severity of some of the proposed changes; and that has hurt portfolio performance over the last 12 months. While we anticipate that the eventual impact of these changes will be manageable, companies do not like uncertainty. Boards are unlikely to approve billion-dollar drug plants or trials without clear visibility about drug pricing and tariffs. And this reticence had led to consistent underperformance from companies like Danaher and Icon. Recently, we have seen some signs that end-customer demand is improving. When sentiment shifts, stock prices can move fast: we saw this with Icon, which was up 40% over the course of 3 days during July.

While we have reduced our total exposure to healthcare, we are maintaining an overweight position. Sentiment on the sector is near the lowest in decades on what we think are manageable headwinds.

Our healthcare portfolio companies are generally market leaders in innovative and fast-growing markets, that are also playing a role in managing overall healthcare costs, which at least partially shields them from Government spending cuts. For example, Dexcom's continuous glucose monitors for diabetics have been proven to reduce total costs to healthcare systems, such as reducing emergency department visits by 30%; and Robert F Kennedy Jr, who is effectively the Minister for Health in the US, believes widespread use of devices like CGMs will help make Americans healthier.

Our top three performers for the quarter were all AI related. **Alphabet** continues to prove the critics of its AI capabilities wrong, winning AI cloud deals with Meta and OpenAI, and is in discussions with Apple to integrate Google Gemini into a revamped Siri. The continued demand for AI computing requires increased investment in semiconductor manufacturing capacity, in turn driving demand for **ASML's** advanced lithography tools used to develop these advanced chips. **Tencent** is using AI to drive performance in its advertising and gaming businesses. AI algorithms are improving the return on advertising spend for advertisers on Tencent's short-video product, driving 50% revenue growth from short-video advertising in the quarter.

Google and **ASML** have both dragged on portfolio performance over the last 6–12 months. We took the opportunity to add significant weight to each of these names during this period, and have benefited from the subsequent outperformance. While these recoveries in share prices can take time to play out, they highlight the benefit of also playing offence when sentiment is negative, provided our investment thesis has not changed.

On the opposite side of the fence was **Gartner**, a company deemed an AI loser by the market. Gartner's negative earnings resulted in elevated fears in August that AI is disrupting the research and consulting industry, despite management's commentary that it was more macro-driven. We had reduced a third of our position coming into results as we felt the AI risks had heightened. We now hold it at a very small weight after the sell-off. While we acknowledge the AI risks, we think Gartner's proprietary data and independence provide some defence, and the business is not standing still: Gartner recently launched its own AI search product, called AskGartner.

We have also added to several of our positions outside of tech and healthcare, opportunistically increasing our position size in **Zoetis**, **Hermes** and **Tradeweb**, and adding a new company called Old Dominion to the portfolio.

While the market is overly focused on near-term challenges for Zoetis's Librela pain drug for dogs, we believe these challenges will eventually be resolved, and the market is missing the multi-year growth runway for Zoetis as it continues to launch innovative new treatments for animals.

We continued to add to our Hermes position among weakness in the broader luxury market given that key brand health metrics (like resale values) remain stable, indicating the brand's MOAT is intact.

We increased our Tradeweb position. The sell-off in defensive companies, coupled with temporary concerns about low-fee competitors taking market share from Tradeweb, created the opportunity. Tradeweb remains the best positioned electronic bond trading platform, and will benefit from the ongoing structural shift to electronic trading.

Portfolio Changes

We initiated a position in Old Dominion Freight Line (ODFL), which is North America's second largest less-than-truckload (LTL) carrier, a segment where operators charge more than full-truckload peers due to multi-customer handling and sorting. ODFL is regarded as the industry benchmark, with on-time deliveries above 99%, damage claims of only 0.1%, and 15 consecutive #1 quality rankings from Mastio & Company. Its culture of 'helping the World Keep Promises' has supported market share gains and industry-leading margins. With the freight sector in its longest recession in decades as COVID over-earning continues to unwind, we began building a position.

We exited **UnitedHealth Group** during the quarter. The company was one of our worst performers in the June quarter, as earnings were cut 50%, shaking investors' confidence in this historically stable business. We had trimmed our position size significantly into the result, and again as we reviewed our investment thesis. Following an increase in share price of around 40% from the start of August, we exited our position.

Trimming tech underweights while leaning into materials, healthcare, and staples

Mark Brighthouse, Chief Investment Strategist, Core International Equity



Source: Bloomberg

The Core International Equity portfolio gained 13.20% over the September quarter, outperforming the benchmark which rallied 12.65% and bringing the calendar-year-to-date performance back above the benchmark.

Market backdrop

Geographic allocation was a slight detractor from relative returns as the US market was very strong, and the portfolio is slightly underweight in the US. Growth stocks outperformed value stocks for the second consecutive quarter, which was also a drag on the portfolio's performance. Industry tilts detracted from performance, as the information technology sector led the way and consumer staples lagged. We were pleased to see that the materials sector, the portfolio for which is quite overweight, was the second-best performing sector over the quarter.

Security selection was a major positive contributor to portfolio performance, especially in the financial, consumer discretionary and healthcare sectors. Examples include the overweight to Japanese

financials such as **Mitsubishi UFJ** (up 25%), the overweight to auto parts and electronic supplier **Sumitomo Electric Industries** (up 41%) and the overweight to drug maker **AbbiVie Inc** (up 32%). Security selection within industrials was a detractor and included industrial equipment maker **Hitachi** (down 4%).

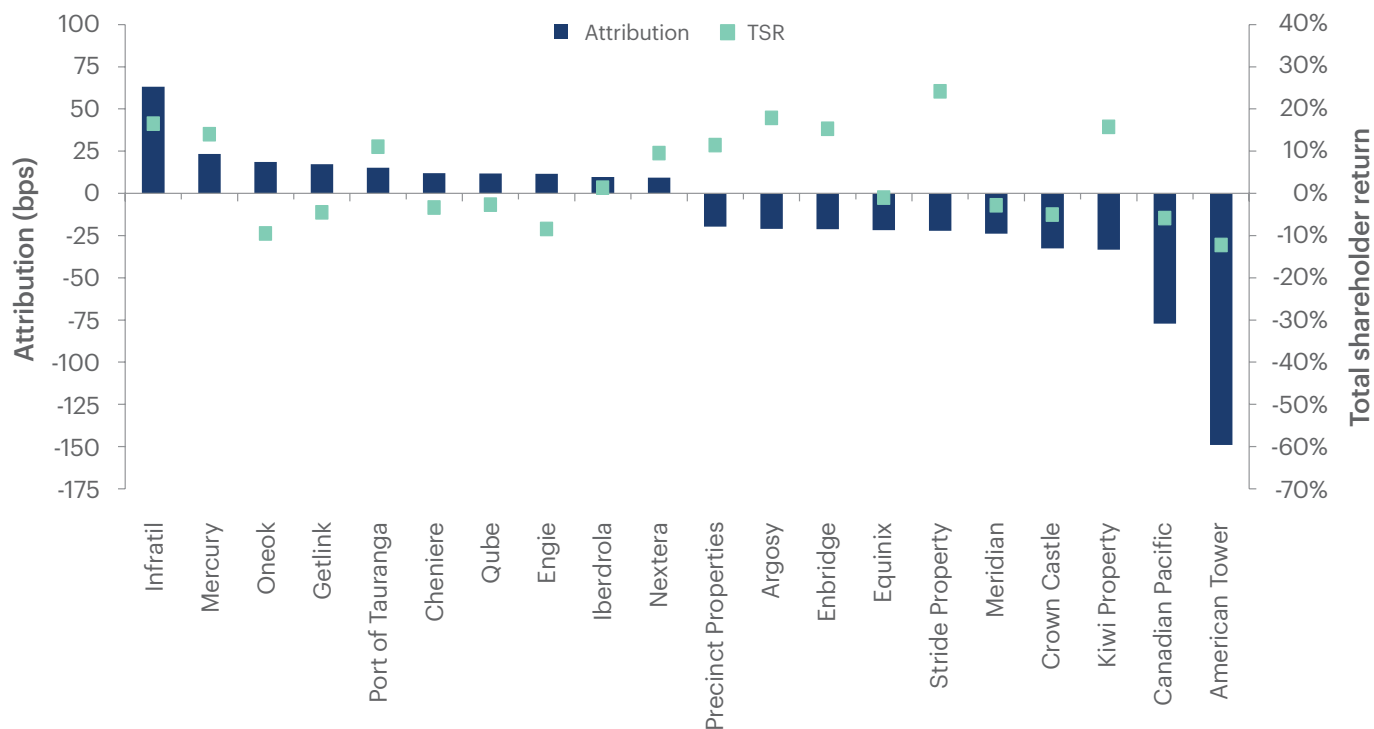
Portfolio Commentary

The strongest performing stock in the portfolio was **Warner Bros Discovery Inc** (up 78%), which benefited from potential takeover rumours, upgrades from analysts, and a superhuman box office performance from its latest cinematic releases.

During the quarter, we trimmed active risk in the portfolio by reducing some of the technology underweights. The portfolio remains overweight materials, healthcare and consumer staples sectors, and underweight energy and information technology. Geographic tilts favour Japan, Europe and the UK relative to the US.

Dovish RBNZ and softer NZ yields revive property as AI power demand lifts utilities

Michael Bacon, Senior Investment Analyst, Property & Infrastructure



Source: Bloomberg

New Zealand property stocks had a standout quarter (+15%), followed by Australian property (+5%) and global infrastructure (+4%).

Market backdrop

September marked a benign quarter for bond yields, with US and Australia 10-year government bond yields flat for the quarter. New Zealand yields dropped 16 basis points, reflecting a weaker economy. This development, combined with a more dovish RBNZ, boosted interest-rate sensitive stocks in New Zealand.

Portfolio Commentary

Kiwi Property Group returns to the portfolio supported by improving fundamentals

The NZ property sector (+15%) was supported by lower interest rates and increasing investor confidence in the earnings outlook. We have been

underweight in the sector for a long time, given concerns about growth, dividend sustainability, debt levels and growth opportunities compared to infrastructure and Australian property. Over the past five years, investors have experienced negative returns (-5% annualised), while global infrastructure has returned +8% and Australian property +9%. The P&I fund returned +10% annualised over the same period.

However, these concerns have increasingly been priced into the sector, as shown by the recent rally on improving fundamentals. During the quarter, we added **Kiwi Property Group** (+18%) back to the portfolio. Since we exited the company in late 2023, the stock price had stayed flat through to June this year. In the interim, management has reset the dividend, improved capital allocation and re-signed leases on key assets.

Artificial Intelligence investment has benefited power providers more than datacentres

The quarter saw ongoing headlines related to artificial intelligence (AI). Notable deals included Nvidia's plan to invest US\$100 billion in OpenAI and US\$5 billion in Intel. Oracle announced a US\$300 billion cloud computing deal with OpenAI. The Oracle–OpenAI deal will involve building 4.5 gigawatts of datacentre capacity in the US, equivalent to the power output of two Hoover Dams.

Debate continues in the market about whether all the AI investment can be monetised or whether we are in a 'bubble'. Various listed infrastructure sectors are potential AI beneficiaries, although their performance was mixed. **Kinder Morgan** (-3%) (who sells gas to power plants, among other customers) had a soft quarter, datacentre provider **Equinix** (-1%) was also weak, while US utilities rose +8% and Morgan Stanley's AI power beneficiary basket rose +18%.

While independent power producers such as Constellation are the most obvious beneficiaries, they also have the widest range of outcomes – contracts are typically short term and power prices can be volatile. We don't think there is a sufficient margin of safety to add such companies to the portfolio right now. During the quarter, we bought more shares in **CMS** (+7%) and **NextEra Energy** (+10%). These companies benefit from rising power demand in the US, yet have defensive earnings through regulated returns and long-term power contracts for their unregulated development projects.

Infratil's CDC signs 100MW of new contracts

Infratil's (17%) CDC investment is a datacentre developer capitalising on the strong demand environment. CDC closed Infratil's September investor day with an upbeat presentation, foreshadowing major contract wins that were announced the following week. For context, 100MW is larger than CDC's entire New Zealand footprint. The contracts are a welcome development after CDC earlier missed contracting targets in 2024. CDC has now secured 95% of the revenue it needs to deliver its target of doubling 2025 earnings by 2027.

Longroad Energy, a US renewable developer, also provided a positive outlook. Despite changes to tax subsidies, Longroad is confident that a growing development pipeline and its equity needs are similar to expectations before the subsidy changes. Asian renewable platform Gurin, which is at a much earlier stage of development, also expressed confidence in its large pipeline. It noted that it is facing competition on its key Singapore power project, and we think the market will need to see more execution before it gives credit for the project.

Infratil also reiterated targets for recycling assets, and subsequent press reports suggested Qscan, an Australian diagnostic imaging business, is for sale.

The Trump administration's pro-merger stance had a negative impact on rails and towers

Union Pacific (+3%) and **Norfolk Southern** (+18%, a former portfolio holding) announced a US\$250 billion merger, the largest in railroad and infrastructure history. Such a combination was typically branded 'unthinkable' before President Trump's second term due to market concentration concerns. Union Pacific expects over US\$2 billion in synergies, citing customer benefits such as two days less transport time for cargo travelling West–East across the US. The merger potentially has negative implications for portfolio holding **Canadian Pacific Kansas City** (CPKC, -6%). CPKC's network covers Canada, the Central US and Mexico. CPKC expects double-digit earnings growth from the new trade routes created from its merger. Yet some of those earnings may be threatened by the merger of Union Pacific with Norfolk Southern. That merger is seen to have President Trump's blessing, in part because he fired a Board member of the Surface Transport Board who was expected to vote against the merger.

Challenger telco DISH sold US\$23 billion in spectrum assets to AT&T and a further \$17 billion of spectrum assets to satellite operator Starlink during the quarter. Our tower investments **American Tower** (-12%) and **Crown Castle** (-5%) were negatively impacted. Investors are concerned that telco customers will need to spend less on tower leasing because of the spectrum deals. We agree that these deals will have an impact, but consider the share price reaction to be too strong. We don't think satellites will pose a meaningful threat to the traditional mobile market, and note that AT&T's plan to aggressively sell Fixed Wireless (mobile broadband) should result in more tower leasing in time. We reduced our position in American Tower during the quarter, acknowledging that near-term fundamentals have softened.

Other notable portfolio changes

We exited **Vienna Airport** (-2%). The company has been a strong contributor to fund performance (+14% annualised return over 14 years), yet it has faced challenges recently. Low-cost carrier Wizz Air exited Vienna (citing cost challenges), and a proposed new runway will require significant capital without benefiting traffic growth for many years.

We increased our position in **Port of Tauranga** (+11%) following a strong full year result and improved pricing outlook.

We also bought more **Waste Connections** (-6%) shares, as a recent sell-off provided an opportunity to build a larger position in a high-quality business.

Calm seas, tight spreads: why patience beats yield-chasing now

Quin Casey, Senior Portfolio Manager, New Zealand Cash & Fixed Interest

Fixed-income investors benefited from a quieter market backdrop during the September quarter as financial market volatility declined. Global inflation data was relatively contained, central bank guidance was skewed towards further easing, and global growth remained steady. Yet, with investors still adjusting to US tariff policy uncertainty, and economic momentum somewhat uneven across regions, downside risks remain. It pays to proceed with caution when the waters appear unusually calm and we think patience and attention to detail are required more than ever to traverse today's markets.

A bit of caution is warranted

Credit spreads – the extra yield investors receive for owning corporate bonds instead of government bonds – are a measure of expected default risk.

When credit spreads are high and volatile, fear is the dominant investor emotion and compensation for default risk is high. When spreads are low and stable, optimism reigns and investors tend to assume default risk is low. Yet history has shown that narrow credit spreads can be deceptive, and that periods of calm in the sea of credit often precede stormy waters.

Let's look at the period leading up to the Global Financial Crisis (GFC). During 2006 and into early 2007, credit spreads across global investment grade and high-yield markets compressed to very low levels. At the time, many investors convinced themselves that a new era of financial engineering, rising house prices, and broad-based growth justified a view that default risk was remote. But credit risk never sleeps. When the GFC hit, credit spreads spiked higher, bond prices collapsed, and investors who had stretched for yield faced hefty losses.

The timeless lesson is that low and stable credit spreads do not mean risk disappears. Indeed, when spreads are tight, the margin for error shrinks: even a modest rise in corporate defaults can quickly overwhelm the extra yield on offer from credit investments.

Current conditions in global credit markets bear an uncomfortable resemblance to the period before the GFC (see the chart at the end of this article). If the global economy weakens, or if inflationary pressures keep interest rates higher for longer than expected, leading to pressures on corporate earnings, credit investors may encounter choppy waters again.

Therefore, a bit of caution is warranted given credit spreads are low relative to history. But it is not simply about avoiding losses: it's about maintaining the flexibility to act when opportunities arise.

Indeed, investors who resisted the urge to overreach in 2006–2007 were far better positioned to buy attractively priced assets in 2008–2009. Conversely, investors who abandoned discipline during the boom before the GFC were often forced to sell into the downturn, locking in losses and missing the positive returns that followed.

Successful credit investing is less about chasing yield in good times and more about surviving the turn in the credit cycle. Timing a turn in financial markets is always hard, yet patience, discipline, and adherence to a time-tested investment process remain the most reliable navigating tools.

When markets eventually adjust and credit spreads widen, those investors who exercised caution will have the resources and confidence to seize the investing opportunities that follow.

We are cautious for now, but we are ready to pounce.

A bit more KIWI

During the quarter, we added to our investment in Kiwibank. Kiwibank, owned by the Crown, remains well capitalised. As such, its debt securities tend to provide predictable returns. This predictability makes those securities attractive for investors seeking security and consistency. While New Zealand's economy has had a difficult few years, there are signs of life as we head into summer. These signs should support Kiwibank's asset growth and earnings profile. In fact, the bank is actively targeting funding support for NZ businesses as other banks have stepped away from this area of the market. Supporting local makes sense to us, and we remain comfortable with our Kiwibank investment positions.

No bad blood

Following a period of strong returns, we decided to lock in profits and exit our position in Grifols SA. While Grifols maintains a strong business profile – anchored by its global leadership in plasma-derived therapies and related resilient demand for life-saving treatments – credit spreads had tightened to the point where room for further upside was limited. Taking profits will enable us to reallocate this capital to alternative credit opportunities. This decision reflects prudent portfolio management, not a lack of confidence in the Grifols business and financial profile. The reallocation doesn't mean 'bad blood' with Grifols – we may revisit their business in the future when the risk-reward balance improves.

Welcome Tina from Turners

Towards the end of the quarter, Turners Automotive Group Limited announced plans to issue fixed-income assets backed by a pool of its car loans (these types of bonds are known as 'asset backed securities'). The transaction provides investors with an opportunity to earn relatively attractive returns from New Zealand's largest integrated automotive financial services company. With strong market presence across car sales, finance, and insurance, Turners benefits from diversified revenue streams and a proven track record of profitability. The group also has a solid balance sheet and consistent

cashflow generation, making it a compelling option for fixed-income investors. By supporting Turners, investors are aligned to a trusted Kiwi brand that fuels mobility and economic growth nationwide.

Outlook and strategy

We have maintained our duration overweight over the period for several reasons. The New Zealand economy continues to struggle to generate growth despite a series of Official Cash Rate (OCR) cuts from 5.50% to 3.00% currently. In addition, 10-year government bond yields have remained elevated despite the magnitude of the OCR reductions, leaving yields in the 5–10 year segment relatively attractive. We remain focused on domestic economic data for signs of improvement, but for now are comfortable maintaining this positioning.

Our broader investment views are largely unchanged. The sharp decline in short-term interest rates over the past 12 months has delivered strong returns from our New Zealand duration position. However, we now view New Zealand bonds as trading near fair value, aside from select areas where additional yield remains attractive.

While credit spreads remain tight by historical standards, we continue to favour high-quality issuers, maintaining a defensive tilt within the portfolio.

Softer data, easier policy: NZ duration and quality credit do the heavy lifting

Benjamin Wilton, Fixed Income Analyst, Global Fixed Interest

Global Fixed Interest Fund

The Global Fixed Interest Fund returned 1.21% in the September quarter, outperforming its benchmark return of 0.88%. Global bond markets rallied as investors priced in easier monetary policy following softer economic data, particularly from the US and New Zealand. US Treasuries performed strongly, led by shorter dated maturities as markets anticipated further US Federal Reserve rate cuts after a series of weaker than expected labour market points.

Most of the Fund's outperformance came from its overweight position in New Zealand Government bonds, which benefited from the relative weakness of the domestic economy and a clear shift in the Reserve Bank of New Zealand's stance signalling more rate cuts ahead. The quarter's key development was the surprisingly weak June quarter GDP result, which fell -0.9% versus expectations of -0.3%. This prompted major bank economists to forecast three additional Official Cash Rate (OCR) cuts to around 2.25% – roughly half its level from a year earlier (5.5%). Expectations of easier monetary policy pushed short-term interest rates lower, lifting New Zealand Government bond prices.

The Fund also benefited from its overweight to short-dated Australian credit, which continued to offer attractive yields relative to comparable securities in the US and Europe.

Credit

One of our best performing credits during the quarter was the Fund's position in KIOXIA Corporation – a leading global supplier of flash memory and solid-state drives. The company benefited from a shallower than expected downturn in memory markets, as demand – partly driven by artificial intelligence (AI) applications – continued to exceed expectations. KIOXIA's bonds returned 4.9% over the quarter.

Other positions that are beneficiaries of the growing demand for AI infrastructure included Oracle and Broadcom. Oracle continues to gain from strong growth in its cloud infrastructure business, which supports AI workloads, while Broadcom manufactures key semiconductor components used

in AI datacentres.

Following a period of strong returns, we decided to lock in profits and exit our position in Grifols SA. While Grifols maintains a strong business profile – anchored by its global leadership in plasma-derived therapies and the resilient demand for life saving treatments – credit spreads had tightened to the point where the room for further upside is limited. Taking profits enables us to reallocate capital to alternative opportunities. This decision reflects prudent portfolio management rather than a lack of confidence in Grifols' business or financial profile. The reallocation doesn't mean 'bad blood' with Grifols – we may revisit their business in the future when the risk-reward balance improves.

Outlook

The Fund has been positioned with slightly more New Zealand interest rate risk (duration) relative to its benchmark, which has worked well as a trade. We have since reduced this overweight following the strong rally in rates. Looking ahead, we expect activity in the New Zealand economy to gradually improve, though the recovery is likely to be slow. The housing market remains relatively subdued and job opportunities somewhat scarce – a combination that will likely limit a rapid rebound in household spending. We will continue to actively monitor and adjust positioning as economic conditions evolve.

Credit markets have continued to perform strongly, with many measures of credit spreads (the additional yield offered on a corporate versus government bond) now close to, or at, all-time lows. In this environment, the Fund maintains an up in quality bias, favouring investment-grade issuers over high-yield names. We also took profit on selected credit positions during the quarter following strong spread performance.

Fixed-income investors benefited from a quieter market backdrop during the September quarter as volatility declined. Global inflation data remained contained, central-bank guidance tilted towards further easing, and global growth held steady. Yet with investors still adjusting to US tariff policy uncertainty and uneven momentum across regions, downside risks persist. It pays to proceed with caution when the waters appear unusually calm. More than ever, we believe patience and attention to detail are essential to managing risk in today's markets.

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