

U.S. Economy: A Puzzle Without a Picture

The economy today looks less like a finely tuned machine and more like a thousand-piece jigsaw scattered across the floor. In theory, the rules are simple: keep inflation anchored at 2–3% and growth should balance itself. If inflation runs hot, raise interest rates — borrowing slows, profits get squeezed, jobs are cut, unemployment rises, and prices cool. Ideally, the pieces click together into a soft landing. In practice, they don't. Inflation, growth, labour markets, tariffs, and politics all carry jagged edges, and forcing them together leaves gaps no model can smooth over.

Labour Market: A Precarious Balance

The U.S. economy has shown resilience despite policy volatility, but the labour market is clearly weakening. Headline unemployment remains near 4.2%, yet the underlying momentum has faded. Much of the earlier payroll strength came from government hiring; strip that out, and the picture deteriorates quickly. On top of that, payroll figures have been revised significantly lower, with job creation over the past three months averaging just 35,000 per month — down from 168,000 previously.

Immigration policy shifts under President Trump are compounding the slowdown, squeezing both supply and demand. Labour force participation is edging lower, and with labour force growth now flat to negative, potential output is capped. The demographic backdrop adds further pressure: an ageing population and a shrinking inflow of migrants are keeping conditions tight even as activity cools.

Corporate restructuring and cuts tied to the Department of Government Efficiency (DOGE) have yet to fully show up in the data, suggesting further weakness could emerge suddenly. For now, the labour market still looks balanced, but the balance feels precarious, one shock away from tipping unemployment sharply higher.

Inflation: The Distorted Piece

Inflation is the puzzle piece that never quite sits flat. At the height of the pandemic, it barely ticked up 0.1% a month while rates plunged to 0.25%. Two years later, the piece flipped: inflation surged to 9.1% and rates climbed to 5.5%. Today, inflation looks closer to target but still out of line. July data show total PCE prices up 2.6% year-on-year, with core at 2.9%. Goods prices rose 1.1% after years of decline, housing services are easing, but non-housing services remain stubbornly high.

Trump 2.0's tariffs have warped the picture further. Responses vary: some firms absorbed the costs, others delayed them, but many passed them straight through. Durable goods prices are rising for the first time in nearly three years, while services absorb the spillover — dentists, for example, hiking fees not for wages, but because imported equipment now costs more. The pressures are neither linear nor predictable, emerging from corners of the economy few expected. Even before tariffs, core inflation was running 30–40bps above target. With tariffs in play, the Fed faces something closer to a “tariff inflation regime.”

The key question is duration. Tariff effects are expected to peak in August and September, but pass-through lags could extend into Q4 or even early 2026. If businesses and households come to see higher prices as permanent, inflation expectations could reset, leaving the Fed with a puzzle that no longer matches the box lid.

Growth: The Missing Corner

Growth is where the puzzle shows its missing corner. Tariffs have become the common thread across data releases, distorting behaviour even in sectors far removed from global supply chains. GDP growth has slowed to 1.4%, roughly half last year's pace, as tariff uncertainty weighs on activity. The composition is uneven: consumer spending was

revised higher, government spending lower, and imports continued to rise. The first quarter of 2025 even recorded a 0.5% contraction.

Taken together, the picture is fragmented. Inflation is cooling in some areas and reigniting in others, growth has lost momentum, and the labour market remains balanced, although the balance is increasingly fragile.

Policy & Politics: The Wild Card

Fiscal policy, Fed independence, and global spillovers complete the frame, but each makes the puzzle harder to solve. Politics is now front and centre. President Trump and his team have been pressuring the Fed to cut rates more aggressively than the data support. Of the twelve FOMC voting members, three lean toward White House demands, a third remain hawkish, and Powell still skews dovish, at least as interpreted after Jackson Hole.

The bigger flashpoint is the Fed's independence. Trump recently dismissed Fed Governor Lisa Cook, a Biden appointee whose term runs to 2038. As one of seven governors, Cook holds a direct vote on monetary policy. By law, governors are nominated by the president, confirmed by the Senate, and can only be removed "for cause." Cook has launched a Supreme Court challenge, which will test not just her tenure but the institutional independence of the Fed itself.

If Trump succeeds in reshaping the FOMC with loyalists, the consequences are unknowable. It could mean faster, politically driven rate cuts, fuelling rallies in risk assets in the short term, but undermining credibility and stability in the long term. What once looked like a fifty-piece puzzle increasingly resembles a thousand-piece one, scattered and missing edges.

The U.S. economy is not unravelling, but the pieces refuse to lock together. Labour is softening but constrained, inflation is cooling yet distorted, growth is losing momentum, and politics is pressing hard against central bank independence. A soft landing is still possible, but only if the puzzle cooperates, and right now, it does not.

Australia: A Puzzle with Shifting Edges

Australia's puzzle initially looked straightforward, with inflation easing from 2.5% in January to 1.9% in June, unemployment steady at 4.3%, and growth remaining subdued. The RBA's August rate cut, which brought cumulative easing this cycle to 0.75%, reflected this outlook. However, the picture shifted once the 'cut' was in place. July inflation surprised to the upside at 2.8%, with the trimmed mean at 2.7%, while unemployment ticked slightly lower. The RBA's forecasts showed residential investment lifting even as consumption, business investment, and government spending were revised lower. Despite weaker demand, the Bank maintained its inflation projection at 2.6% and emphasised that policy would remain data dependent. The RBA will meet at the end of September to make its next monetary policy decision, and with markets divided after the mixed data, the outcome will be closely watched. For now, the edges of the puzzle remain unclear.

Reporting Season: Precision Over Promise

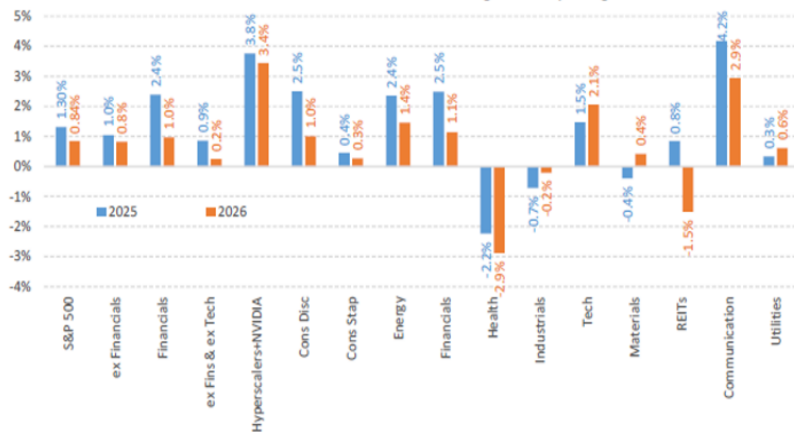
Both the U.S. and Australia have recently concluded their reporting seasons, reinforcing a clear theme: when valuations are elevated, consistent delivery is critical. The market offers little benefit of the doubt; any miss is punished, and only precision keeps companies in favour.

U.S. Reporting Season

The U.S. reporting season drew close attention following new tariffs and corporate tax changes under the One Big Beautiful Bill. Overall, it was broadly strong, with almost all sectors registering positive earnings revisions and guidance. Of the eleven sectors, only three had either negative full-year guidance or downward earnings revisions. Hyperscalers and NVIDIA remained the key contributors, and given their elevated valuations, anything less than expected from them would not be well received.

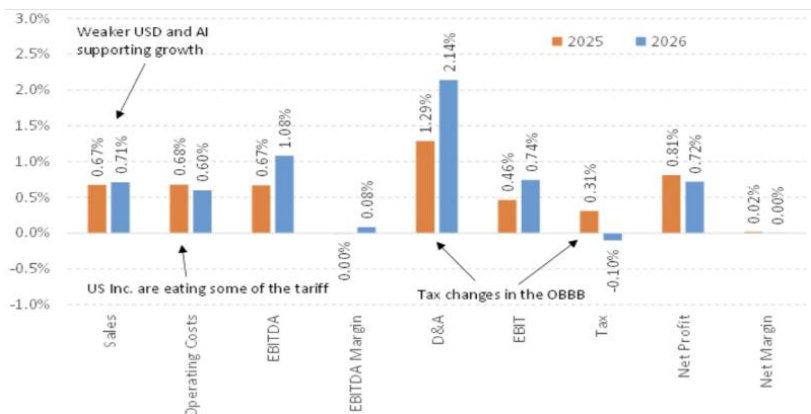
S&P 500 profits for 2025 were revised up 1.2%, with 2026 forecasts up 0.8%, largely driven by AI investment and a weaker U.S. dollar.

S&P 500 EPS revisions for calendar 2025 and calendar 2026 during 2Q25 reporting season



The DXY index, which measures the dollar against a basket of major currencies, is down roughly 10% year-to-date, providing a tailwind for multinational companies. At the same time, cost pressures remain elevated, but tax changes are boosting the bottom line and driving EPS upgrades despite a challenging macro environment.

Companies are guiding to even stronger capital expenditure. 2025 capex has been upgraded by 2.5% (\$29 billion), entirely from hyperscalers including Amazon, Alphabet, Microsoft, Meta, and Oracle, while the 2026 increase of 6% (\$76 billion) is 80% attributable to the same group. Permanent 100% expensing of capex and R&D encourages companies to bring forward investment, although future administrations could alter the rules. Rising capex drives higher depreciation, which limits near-term net margins, but tax changes suggest margins will improve over time. This surge in investment also has broader market implications, as one company's capex becomes another's revenue, supporting market-wide sales. The 2025 capex increase equals roughly 1% of U.S. GDP, rising to 2.6% in 2026.



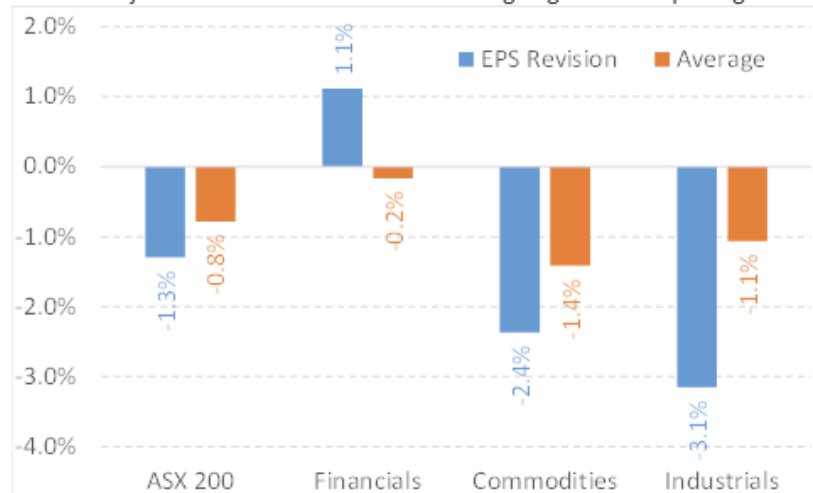
Housing and construction remain weak, reflecting the broader slowdown in economic activity and the influence of interest rates. Financials contributed positively, supported by tax provisions. Overall, the combination of tax-driven EPS boosts, AI investment, and a weaker dollar has temporarily decoupled earnings from the macro backdrop in a way not seen in 30 years, while tariffs and ongoing cost pressures remain a headwind.

Australia Reporting Season

Australia's reporting season resembled a complex puzzle with little room for mistakes. The ASX 200 trading at 19x P/E, well above its historical average, which left valuations stretched. Earnings revisions were harsher than usual, with a 130bps downgrade compared to the typical 80bps, as operational leverage magnified revenue shortfalls. At the same time, a record 18 buyback announcements highlighted management's determination to support shareholder returns.

Looking into some of the results, Life360 was a standout, delivering strong Q2 growth in Monthly Active Users and paying circles, alongside its ninth consecutive quarter of positive operating cash flow. Recent advertising

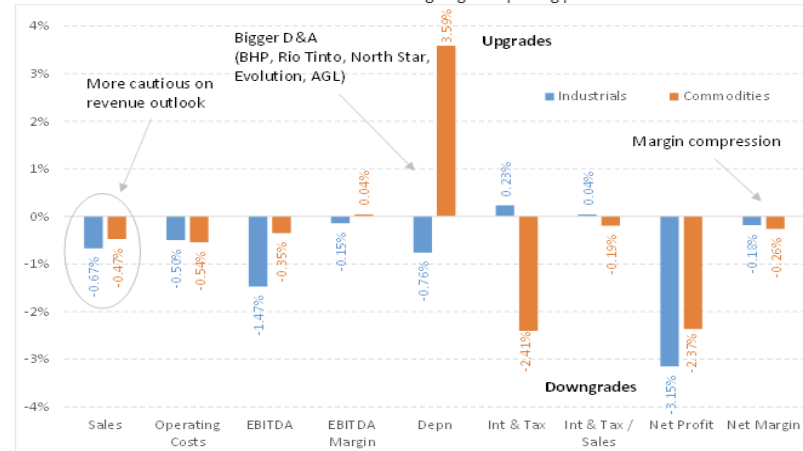
ASX 200 major sector June 26 EPS revisions during August 2025 reporting season



product launches, Place Ads and Uplift, underscored its monetisation potential and pushed the share price about 8% higher on announcement day.

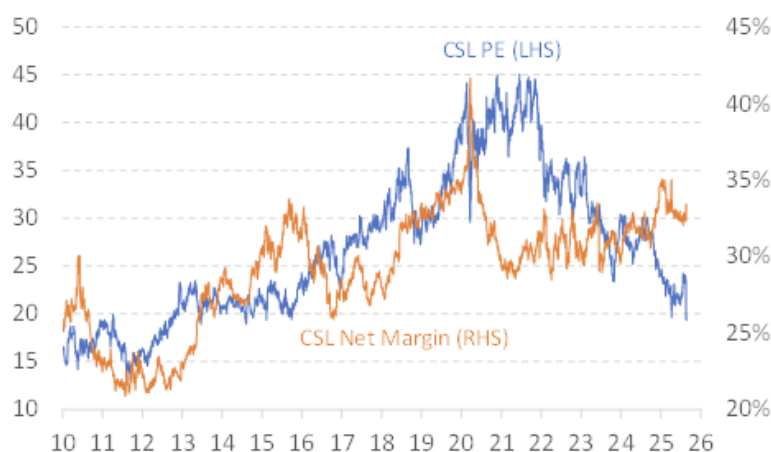
The supermarkets told a tale of two outcomes. Woolworths missed across key metrics and cut its dividend by 41%, driving a 16% share price decline, while Coles posted robust results and traded at record highs.

ASX 200 ex Financials June 2026 P&L item revisions during August reporting period



Reece and James Hardie highlighted the balance between execution and macro pressures. Reece faced rising competition and wage headwinds in both Australia and the US. James Hardie's Q1 EPS downgrade of 40%, reflecting weakness in US housing and strategic missteps, wiped a third off its share price and raised governance concerns.

CSL surprised this reporting season, though the market did not take all the news positively, likely because there was a lot to unpack and the increased competition in Behring raised an eye or two. For a company of its size, starting with a "clean slate" is rare. Its decision to demerge the vaccine business and list it separately on the ASX in 2026 is a bold step to unlock shareholder value. Seqirus, which contributes around 14% of group revenue, has long been volatile. While the pandemic generated strong vaccine demand, recent trends have been underwhelming. Regulatory changes in the U.S., such as allowing vaccines to be administered by pharmacies rather than GPs, combined with rising anti-vaccine sentiment and funding cuts for mRNA vaccines, have weighed on the outlook. Seasonal fluctuations and reliance on the Northern Hemisphere further add to volatility. Carving out Seqirus allows CSL to focus more fully on its "curing" business, sharpening its strategic focus and operational priorities.



Behring now appears more like a mature business, with heightened competition in its core markets reflected in the recent results. Nevertheless, CSL is taking decisive steps that should be seen as constructive. The closure of 22 plasma sites follows the rollout of RIKA, which is now deployed in over 220 centres and expected to be fully implemented soon. RIKA improves efficiency by increasing plasma volume per donation by 10% and reducing collection time to under 35 minutes, lowering both costs and donor burden. The company is also consolidating R&D from 11 sites to six, cutting fixed costs and focusing investment, while participating selectively in tenders to protect margins.

These initiatives are expected to streamline operations, improve cost management, and create long-term shareholder value despite one-off restructuring costs and the heightened competition. CSL is currently trading at multiples near ten-year lows relative to its historical average, suggesting the market may not yet fully reflect the potential benefits of these changes. The company remains a high-quality, globally competitive healthcare business offering defensive earnings, structural growth, and exposure to biotechnology innovation. By separating Seqirus and concentrating on its curing business, CSL positions itself for a clearer strategic path while maintaining an attractive valuation relative to its history.

Mining companies reported flat to slightly positive production, but weaker commodity prices weighed on earnings. Dividend cuts were widespread, with Fortescue down 44% year-on-year to levels not seen since 2018, BHP down 25%, and Rio Tinto down 16%. The sector rose about 9% over the past month, giving some relief, supported by CATL's temporary halt of lithium production. However, the real catalysts are yet to emerge, as China remains the major consumer of commodities and its property market is still far from recovery. Having said that, we remain constructive on the sector. Mining is well positioned to benefit from megatrends, offering a long-term growth story despite short-term volatility. Looking ahead, China's planned steel production cuts through 2026 and 2027 could pressure performance unless demand from outside China offsets the shortfall.

Conclusion

The season highlighted how short-term performance remains highly sensitive to macro shifts, operational execution, and stretched valuations, even as long-term fundamentals continue to provide support. Missteps were punished and precision was rewarded. Overall, it was not a strong reporting season, though quality businesses did deliver, and momentum continues. The broader market has generally been gaining, reinforcing the importance of staying invested in high-quality names. A quality business is one where management delivers consistently, even in a downturn, navigates risks with precision, and protects profitability. For these companies, creating shareholder value is non-negotiable, and their discipline and resilience set them apart in uncertain markets.



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