

SUB-MANAGER'S COMMENTARY



Market Overview

Global equities rose in September, led by emerging markets (EMs), as the global artificial intelligence (AI) revolution supported a sustained technology rally in China. Developed markets also rose, notably in North America. US stocks were supported by a resilient macro backdrop and dovish rhetoric from the US Federal Reserve (Fed).

US markets brushed aside labour market weakness and persistent inflation to focus on strong earnings and fading recession fears. The US economy grew at an annual rate of 3.8% in the second quarter of 2025, a healthy clip that did not slow into the third quarter, according to estimates from the Atlanta Fed GDP Now model.

On a less-positive note, the annual US core Consumer Price Index rose to 3.1% in August, pressured by higher shelter costs. This figure is projected to fall to 2.4% in 2026, according to the Federal Reserve Board, but will remain above the Fed's target of 2%. A consumer confidence survey from The Conference Board found concerns over jobs and employment rose sharply in September, likely influencing the Fed's decision to prioritise labour market weakness over inflation concerns.

Against this background, US Treasury yields fell at the very short end of the curve in response to lower interest rates. However, intermediate yields were largely unchanged despite inflation concerns. Elsewhere, US corporate bonds rose as spreads narrowed on sustained risk appetite.

European equities had a tougher ride, as political volatility in France, fiscal concerns in Germany and weaker growth in peripheral economies diluted regional returns. The European Central Bank (ECB) remained cautious, with markets pricing in limited further easing amid lingering inflation. Euro area annual inflation is expected to be 2.2% in September, up from 2% in August, impacted by rising services and food costs.

In addition, Germany's extensive fiscal stimulus package exacerbated inflation concerns and contributed to upward pressure on bond yields. Business sentiment in the euro area dipped to a four-month low in September, according to S&P Global, amid waning confidence in the manufacturing sector. Weak demand from China and US tariffs combined to suppress new orders. Against this background, European equities rose in September but underperformed global indexes. The euro government yield curve flattened, as short-term German Bund yields rose amid hawkish rhetoric from the ECB. European credit added value on narrowing spreads, notably high-yield issues.

EM equities fared better than their developed market counterparts across the month, led by China. Despite persistently weak domestic demand, a strong rally in large-cap technology names led markets higher. Companies such as Tencent, Alibaba and Xiaomi were able to shrug off economic weakness and drive earnings via lucrative AI contracts and expanding client bases. Elsewhere, Taiwan and South Korea benefitted from more clarity around semiconductor tariffs. In contrast, Indian companies continued to suffer from punitive US tariffs.

The MSCI ACWI Islamic Index returned 4.75% in US dollar terms during September, while the Dow Jones Sukuk Index returned 0.81%. Gulf Cooperation Council (GCC) bonds rose in September, with the FTSE MENA Bond – GCC Index posting a 1.50% return in US dollar terms.



Performance and Positioning

The portfolio posted a net return of 2.15% (in US dollars) during September, ahead of its custom benchmark, which returned 2.11% (also in US dollars).

The equity element of the custom benchmark was changed to MSCI ACWI Islamic Index on 8th May this year, when the previous benchmark (MSCI ACWI Islamic ex-Japan Index) was decommissioned.

The fund held an underweight to fixed income relative to the benchmark, balanced by off-benchmark positions in cash and gold. This positioning was additive to relative performance. Our equity allocation was broadly neutral, including the equity element of a position in Franklin Shariah Global Multi-Asset Income Fund.

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Our EM equity holdings benefitted relative results, outperforming the global benchmark, while our US equity holdings had no significant impact on relative results. Elsewhere, our multi-asset holdings proved a slight drag.

Our defensive positioning contributed to relative returns, in aggregate, notably gold shares. Gold prices rose during September, responding to US dollar weakness, declining real yields and “safe haven” flows that were partially linked to ongoing concerns about government debt and stagflation. Sukuk holdings had no significant effect, in aggregate. Both underlying funds had an effective duration of just under five years and broadly matched the fixed income benchmark, given intermediate US Treasury yields remained relatively stable during the month.



Outlook

We adopt a positive view of risk assets ahead of the final quarter of 2025, as we weigh extended equity valuations against a generally positive macro environment, strong corporate fundamentals and monetary policy easing.

The strength of the recent equity rally has brought warnings about irrational exuberance, especially where retail investors are concerned. However, we prefer to take a more measured approach, examining the underlying macro and corporate environment for signs of weakness.

Our analysis finds a broadly positive setup for risk assets, where improving business activity and solid economic growth has provided the platform for strengthening global earnings-per-share growth forecasts. From a policy standpoint, US labour market weakness provided the Fed with a reason to cut interest rates in September, which should further bolster equity market momentum.

Fair value analysis does suggest to us that equities are expensive, with most good news priced in, but we place greater emphasis on fundamentals. In addition, measures of sentiment remain surprisingly neutral, while positioning also looks restrained—notably among discretionary investors—suggesting the rally has room to run. This strengthens our conviction in a responsibly bullish approach to risk as we move into the final quarter of 2025.

From a cross-asset perspective, we have altered our stance by rebalancing our defensive positioning. We believe market expectations for Fed easing are too lofty given resilient growth and persistent inflation pressures, while fiscal instability should put further upward pressure on long-term yields. As a result, we prefer the lower interest-rate sensitivity of cash. We also improve our view on commodities, noting that gold may act as a useful inflation hedge.

Within our sukuk portfolios, we maintain a defensive and highly selective stance, ensuring that risk is taken only where compensation is commensurate.

Consistent with our defensive posture, we are prioritising high-carry currencies to help offset volatility and provide attractive income. This strategy allows us to defend against US dollar weakness and generate portfolio income, while maintaining a prudent risk profile.

Despite rich credit valuations and our tactically defensive posture, we believe that global sukuk continue to stand out globally, supported by impressive credit fundamentals. GCC issuers, in particular, benefit from stronger sovereign balance sheets, higher ratios of reserves to gross domestic product, and lower debt burdens compared to their global EM peers.

These structural advantages translate into more efficient compensation per unit of risk, making the region particularly attractive in a world of elevated debt and compressed spreads. The relative strength of GCC fundamentals provides a buffer against potential market stress, reinforcing the case for long-term allocations to global sukuk.

Past performance is not an indicator or a guarantee of future performance.

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