COOLABAH CAPITAL INVESTMENTS™
THE INTELLECTUAL EDGE: MAKING EVERY BASIS POINT COUNT

Fund: **Smarter Money Long-Short Credit Fund - USD Investor Class**
Strategy: **Alternatives/Unconstrained Fixed-Income**
Return (since Sep. 2017): **7.67% pa gross (5.91% pa net)**
Net return volatility (since Sep. 2017): **2.60% pa**

October 2026

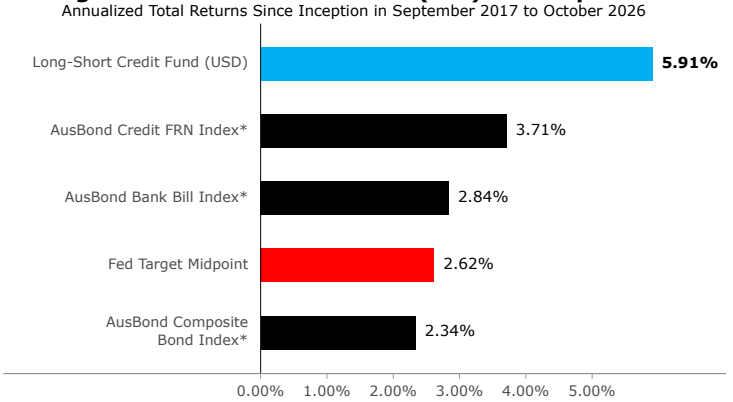
Objective: The Fund targets generating absolute returns of 4% to 6% p.a. above the midpoint of the US Federal Funds Target Range after management fees and performance fees with less than 5% p.a. volatility over rolling 3 year periods, and low to no correlation with equities, fixed-rate bonds, and property markets.

Strategy: The Fund provides exposure to an actively managed, absolute return fixed-income strategy focused on exploiting long and short mispricings in global credit markets. The Fund has exposure to an Underlying Pool which invests primarily in debt securities, hybrids and derivatives. The Underlying Pool employs an "active" fixed-income investment strategy, seeking to take 'long' and/or 'short' positions in relation to debt and hybrid securities which are considered mispriced. The goal is to generate 'alpha', or risk-adjusted excess returns, through identifying and exploiting mispricings in the underlying assets and/or derivatives related to them.

The Underlying Pool is permitted to invest in Australian and global bonds, such as government and semi-government bonds, bank and corporate bonds, hybrid and asset-backed securities, including residential-mortgage-backed securities, issued in Australian Dollars or hedged to Australian Dollars, as well as cash, cash equivalents and related derivatives. It can borrow, use derivatives and short-sell, meaning it may be geared (or leveraged). Leverage can amplify gains and also amplify losses.

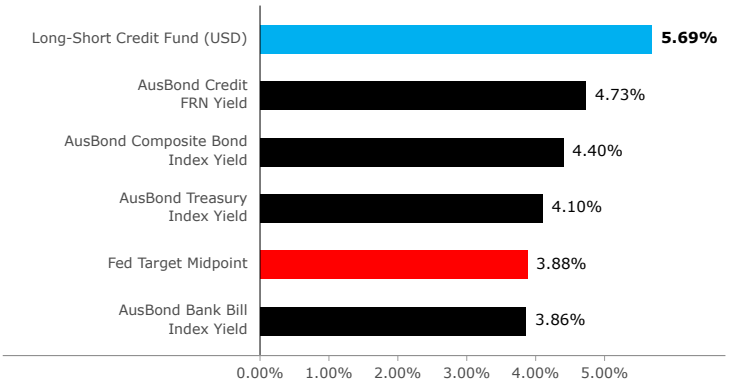
Period Ending 2026-10-31	Gross Return (USD)	Net Return (USD)†	US Fed Fund Target Midpoint	Gross Excess Return (USD)‡	Net Excess Return (USD)†‡
1 month	-0.06%	-0.12%	0.31%	-0.37%	-0.43%
3 months	0.50%	0.35%	0.92%	-0.42%	-0.57%
6 months	2.28%	1.80%	1.83%	0.45%	-0.03%
1 year	5.47%	4.39%	3.67%	1.80%	0.72%
3 years pa	**9.89%**	**8.10%**	**4.46%**	**5.43%**	**3.64%**
5 years pa	8.21%	6.52%	3.85%	4.36%	2.67%
Inception pa Sep. 2017	**7.67%**	**5.91%**	**2.62%**	**5.05%**	**3.29%**

Long Short Credit Fund Returns (Net) vs Comparisons
Annualized Total Returns Since Inception in September 2017 to October 2026



Data Source: RBA, Bloomberg, Apex Fund Services, Coolabah Capital Investments

Annual Running Yield*
31 October 2026



Data Source: RBA, Bloomberg, Coolabah Capital Investments

† Net returns are calculated from the historic gross returns using the current fee structure as displayed in the Product Disclosure Statement. *USD gross returns are estimated from AUD gross returns using 1 month forward contracts. ‡ The Excess Return columns represent the gross and net return above the midpoint of the US Federal Funds Target Range.

* The yield displayed for the Fund is the annual running yield before fees. A fund's running yield is a forward-looking measure of the income expected to be generated by the portfolio based on the coupons payable on the bonds held by the fund as at that date, before management fees, performance fees and fund expenses. The yield can change daily depending on factors, such as the fund's investment activity and market movements, and may be different on the day you invest. All investments carry risks, including that the value of investments may vary, future returns may differ from past returns, and that your capital is not guaranteed. The Fund has a different risk profile to the other comparisons, including, amongst other things, that it uses leverage, which means that both gains and losses may be amplified. To understand the Fund's risks better, please refer to the Product Disclosure Statement.

Disclaimer: Past performance does not assure future returns. Returns and yields are shown net of management fees and costs unless otherwise stated. All investments carry risks, including that the value of investments may vary, future returns may differ from past returns, and that your capital is not guaranteed. To understand Fund's risks better, please refer to the Product Disclosure Statement available at Coolabah Capital Investments' website.

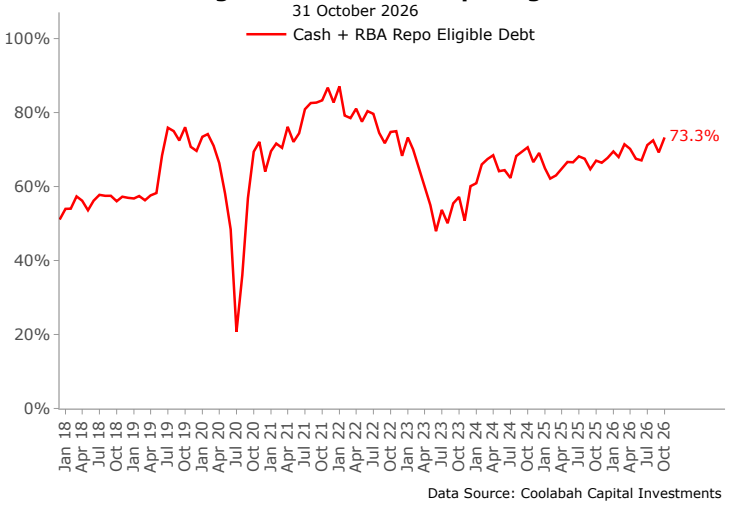
Note: all portfolio statistics other than yields and duration are reported on gross asset value

Net Monthly Returns > Fed Target Midpoint	75%	Modified Interest Rate Duration	< 0.1 years
Av. Portfolio Credit Rating	AA-	Gearing Permitted?	Yes
Portfolio MSCI ESG Rating	AA	1 Year Av. Gross Portfolio Weight to Cash	3.6%
No. Cash Accounts	33	Gross Portfolio Weight to AT1 Hybrids	0.0%
No. Notes and Bonds	299	Gross Cash Accounts + RBA Repo-Eligible Debt	73.3%
Av. Interest Rate (Gross Running Yield)	5.69%	Net Annual Volatility (since incep.)	2.60%

Signatory of: PRI Principles for Responsible Investment

MSCI ESG RATINGS AA
CCC B BB BBB A AA AAA
Asset weighted average rating

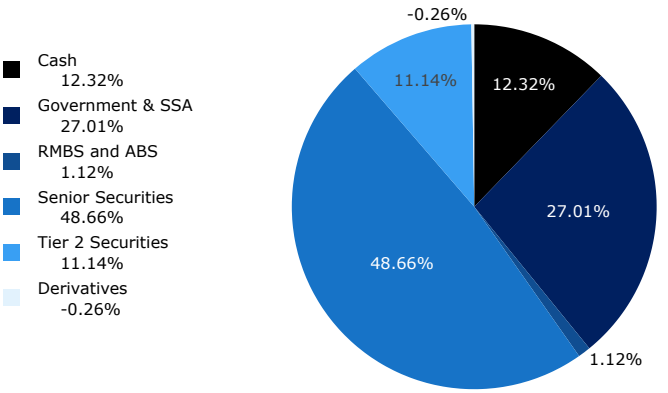
Portfolio Weights: Cash + RBA Repo Eligible Debt



Data Source: Coolabah Capital Investments

Long Short Credit Fund Portfolio Composition (GAV)

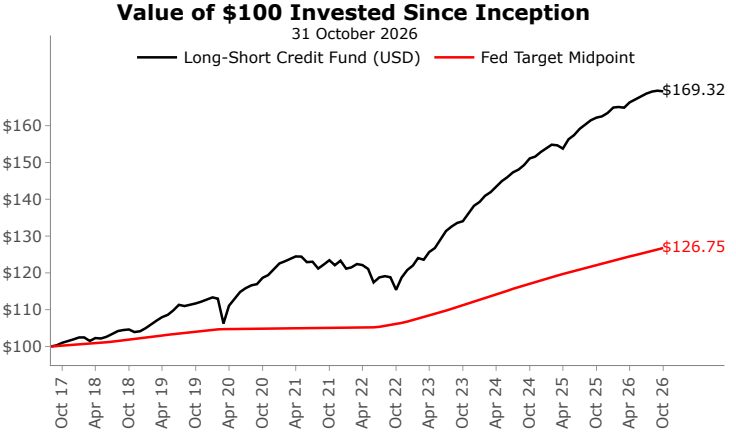
(Gross Levered Statistics) - 31 October 2026



Data Source: Coolabah Capital Investments



Value of $100 Invested Since Inception



Data Source: Bloomberg, Coolabah Capital Investments

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The since inception gross (net) return of 7.67% pa gross (5.91% pa net) is the total annual return earned by the fund since Sep. 2017, including interest income and movements in the price of the bond portfolio after all fund fees (assuming net returns are calculated from the historic gross returns using the current fee structure as displayed in the Product Disclosure Statement). The net return quoted applies to the Smarter Money Long-Short Credit Fund - USD Investor Class, with quarterly distributions reinvested. Investment return will vary depending upon investment date and any additional investments and withdrawals made. **The annualised volatility estimate of 2.60% pa** is based on the standard deviation of net daily returns since inception, which are then annualised, attributable to the Smarter Money Long-Short Credit Fund - USD Investor Class.

Portfolio Managers	Christopher Joye, Ashley Kabel, Roger Douglas, Fionn O'Leary (Coolabah Capital Investments)		
APIR Code	ETL7843AU	Fund Inception	31-Aug-17
ISIN	AU60ETL78432	Distributions	Quarterly
ARSN	617 838 543	Unit Pricing	Daily (earnings accrue daily)
Asset-Class	Alternatives/Hedge Funds	Min. Investment	US$1,000
Target Return	4.0%-6.0% pa over Fed Funds Target Mid Point	Withdrawals	Daily Requests (funds normally in 5 days)
Investment Manager	Coolabah Capital Investments (Retail)	Buy/Sell Spread	0.00%/0.05%
Responsible Entity	Equity Trustees	Mgt. & Admin Fee	0.75% pa
Custodian	Citigroup	Perf. Fee	20.5% of returns over Fed Funds Target Midpoint + 0.75% pa

Signatory of:
PRI Principles for Responsible Investment

MSCI ESG RATINGS AA
CCC B BB BBB A AA AAA
Asset weighted average rating

*In the commentary below, returns indicated with * are estimated returns in USD based on AUD returns hedged to USD with 1m forward contracts. All other returns are USD Denominated where unit classes in USD exist, and estimated from AUD returns hedged to USD using 1m forward contracts before the inception of the USD unit class. Strategy commentary is for the AUD Market.*

Portfolio commentary: In October, the zero-duration daily liquidity Long-Short Credit Fund (LSCF) returned -0.06% gross (-0.12% net), compared to the Fed Target Midpoint (0.31%), the AusBond Credit FRN Index* (0.33%), and the AusBond Bank Bill Index* (0.33%). Over the previous 3 years, LSCF returned 9.89% pa gross (8.10% pa net), outperforming the Fed Target Midpoint (4.46% pa), the AusBond Bank Bill Index* (4.66% pa), and the AusBond Credit FRN Index* (5.68% pa). LSCF ended October with a running yield of 5.69% pa, a weighted-average credit rating of AA-, and a portfolio weighted average MSCI ESG rating of AA.

Since the inception of LSCF 9.2 years ago in September 2017, it has returned 7.67% pa gross (5.91% pa net), outperforming the Fed Target Midpoint (2.62% pa), the AusBond Bank Bill Index* (2.84% pa), and the AusBond Credit FRN Index* (3.71% pa). Since inception, LSCF's Sharpe Ratio, which measures risk-adjusted returns, has been 1.85x gross (1.27x net). While LSCF's return volatility since inception has been low at around 2.60% pa (measured using daily returns), as a daily liquidity product with assets that are marked-to-market using executable prices, volatility does exist. This contrasts with illiquid credit (eg, loans and high yield bonds) wherein assets that have very high risk can appear to have remarkably low volatility, which is, in fact, just a mirage explained by the inability to properly value these assets using executable prices.

Strategy commentary: October delivered a swift reversal of September's bond sell-off. An AI-led rout in technology stocks, renewed US-Iran escalation and France's deepening political crisis drove a flight to quality that pulled sovereign yields lower across most advanced economies, even as Brent crude surged to a six-month high and the Fed, the ECB and the Bank of Japan held rates with a hawkish tone. France was the exception, with the OAT/Bund spread reaching its widest since the European sovereign debt crisis. Credit spreads widened and most equity markets fell, led by the Nasdaq 100.

Global markets

October opened at the extremes of the recent sell-off, with 10-year Bunds touching 3.65%, 10-year Treasuries 5.34%, a 24-year high, and the 30-year UK Gilt yield reaching 6% for the first time since 1998. German yields reversed lower from those highs on the very first day, led by a bid for the front end as French risk flared, and that set the tone for the month. That bid for safety was reinforced from mid-October as risk assets sold off on doubts about the returns on AI investment, and persisted despite surging oil prices.

France was the dominant story in Europe. The OAT/Bund spread started the month at 127bps, approached 178bps intraday on 22 October amid budget gridlock, protests and weak data, its widest level since the European sovereign debt crisis in late 2011, and closed at 165bps, 38bps wider. In mid-October the 10-year OAT yield pushed above 5% for the first time since 2002. Abrupt tightening episodes were repeatedly retraced, liquidity was thin, and talk of the ECB's Transmission Protection Instrument resurfaced for the first time in years, although officials played down the need for intervention. Belgium and Italy followed, with the BTP/Bund spread widening a more restrained 16bps to 119bps, and the stress spilled into European bank shares on contagion fears.

The Fed, the ECB and the Bank of Japan all held rates in the final week of the month, although the tone remained hawkish. The Fed left the federal funds target range at 3.75%-4.00% in a 10-2 vote, with governor Lisa Cook and Cleveland Fed president Beth Hammack dissenting in favour of a hike, and Chair Kevin Warsh insisting that politics played "no role" with the mid-term elections six days away. The data gave the dissenters plenty of ammunition: September core CPI rose a firmer-than-expected 0.3%, third-quarter GDP expanded at a 3.4% annualised pace, core PCE inflation accelerated to 3.1% and unemployment sat at 4.2%. By month-end a December hike was around 80% priced.

The ECB left its deposit rate at 2.50%, prompting a mildly dovish reaction. ECB sources first questioned whether a December hike was needed, then floated one followed by a pause, citing the drag from higher yields. A December move nonetheless remained more than 80% priced into month-end. President Lagarde confirmed she will leave on 7 February, with her successor to be chosen by EU heads of state in December. The Bank of Japan also stayed on hold.

Strategy commentary cont'd: Government bond yields finished well below their September closes. The 10-year US Treasury yield fell 36bps to 4.93%, although it remains 85bps above its level a year earlier. German 10-year Bund yields dropped 26bps to 3.32%, 10-year UK Gilt yields 14bps to 5.28%, Italian 10-year BTP yields 10bps to 4.51% and Japanese 10-year government bond yields 28bps to 2.77%. French OATs were the lone exception: 10-year yields rose 12bps to 4.97% and are 155bps higher over the year.

The Middle East remained the key driver of energy markets. Brent crude rose 13.6% to US$117.64 a barrel, a six-month high, as investors increasingly expected the US to resume strikes on Iran, leaving Brent 81% higher than a year earlier, while WTI gained 15.2% to US$104.12. European natural gas rose more steeply still, climbing 43.7% to €103.94 a megawatt hour, its highest level since the 2022 energy crisis. Gold fell 6.8% to US$3,875 an ounce despite the flight to quality and is 3.2% lower over the year, while Bitcoin dropped 8.2% to US$76,782, leaving it 29.8% below its level a year earlier.

The US dollar strengthened against the euro, with EUR/USD falling 1.5% to 1.116. USD/JPY was little changed, edging 0.1% higher to 157.56.

Technology stocks came under heavy pressure amid mounting doubts over whether AI investment will generate sufficient returns. The Nasdaq 100 fell 6.65% in price terms, or 6.63% including dividends, including a 3.5% drop on the final trading day of the month, its largest daily decline since early June, after Alphabet and Amazon reported free cash flow deficits on outsized capex. The broader US market proved more resilient: the S&P 500 fell 0.93% (-0.87% total return) while its equal-weighted counterpart gained 5.0%. Elsewhere, the Euro Stoxx 50 fell 2.20% (-2.06% total return), the Euro Stoxx Banks Index slumped 11.75% (-11.36%) and the Nikkei 225 lost 5.19% on both measures. The FTSE 100 was the standout, rising 1.17%, or 1.29% including dividends.

Global credit and primary issuance

Credit spreads widened as the risk-off tone extended beyond equities. US CDX IG widened 2bps to 62bps and CDX HY 15bps to 356bps. In Europe, iTraxx Main widened 3bps to 66bps, Xover 26bps to 326bps and senior financials 5bps to 75bps. Over the year, Xover remains 6bps tighter and CDX IG 1bp tighter, while CDX HY is 3bps wider.

Cash credit also weakened. Euro aggregate corporate spreads widened 14bps to 104bps, while sterling corporate spreads widened 10bps to 101bps and US investment-grade corporate spreads 10bps to 89bps. The rally in government bonds nonetheless dominated corporate bond returns: the Global Aggregate Corporate Index hedged to US dollars gained 1.65% in October, while its duration-hedged counterpart lost 0.19% as wider spreads more than offset carry. Over the year, these indices returned 0.07% and 4.22% respectively.

US primary market activity was solid, with US$130bn of US dollar investment-grade supply in October taking year-to-date issuance to US$1.88 trillion, according to Bank of America. Corporates accounted for 52% of supply. In financials, the US banks returned following their third-quarter results, raising almost US$25bn of senior debt between them. The standout was JPMorgan's US$7bn three-tranche holding-company deal, which was well over three times covered and tightened 1-2bps on the break. In corporates, Microsoft printed US$25bn across ten tranches on peak books of around US$115bn.

In Europe, €45bn of investment-grade supply priced in October, of which €16bn came from financials, according to Barclays. With banks exiting blackout later in the month, financials issuance was back-ended and new-issue concessions averaged 7bps. As in September, secondary curves repriced wider towards new-issue levels, and higher-quality issuers fared best. Svenska Handelsbanken printed €750m of four-year senior preferred bonds with 6bps of concession, rallying 2bps on the break, and SEB followed a week later with €750m of 4.5-year senior non-preferred bonds on books 2.3 times covered, offering 9bps of concession and tightening 3bps on the day.

Strategy commentary cont'd: Australian primary markets were subdued. Approximately A$3.1bn of investment-grade credit was issued in October, 66% less than the A$9.2bn printed in October 2025, although year-to-date supply of A$157.7bn remains well ahead of the A$129.6bn recorded at the same point last year. The quiet calendar gave smaller institutions room to raise funding. Bank of Queensland resumed supply with a three-year senior floating-rate note, raising A$800m against more than A$1.2bn of demand, and Bank Australia followed with a three-year senior floating-rate deal of A$300m against A$450m of orders. Challenger Life continued its annuity-backed issuance with five-year senior fixed- and floating-rate tranches totalling A$300m against A$370m of demand, while Boral issued a seven-year senior bond raising A$300m against A$650m of orders.

October also saw a marked increase in non-ADI RMBS issuance, and ADI supply resumed through the second instalment of AMP's 2026 Progress RMBS programme, which printed A$1bn in line with demand. Earlier in the month, Japanese banks MUFG and SMBC tapped the Kangaroo market. MUFG issued A$500m of Additional Tier 1 perpetual notes, non-callable for 5.25 years, against more than A$1.3bn of demand, while SMBC issued A$900m of five-year senior floating-rate bonds against A$1.6bn of orders. Semi-government syndicated issuance added A$8.0bn through NSWTC, TCV, SAFA, NTTC and AUSCAP.

Australasia

Australian government bonds rallied with the global market, although the 10-year yield fell less than its US counterpart. The 10-year Commonwealth government bond yield declined 23bps to 5.12%, leaving it 82bps higher than a year earlier. Domestic credit spreads widened: five-year major-bank senior spreads rose 3bps to 70bps and subordinated spreads 7bps to 137bps, while hybrid spreads tightened a further 8bps to 151bps and were 37bps tighter over the year. The Australian iTraxx Index widened 5bps to 78bps.

Lower yields lifted domestic fixed-rate benchmarks. The AusBond Composite Index returned 1.16% and the AusBond Credit Index 0.83%, while the AusBond Credit FRN Index gained 0.37%. The Australian dollar rose 1.2% against the US dollar to US$0.7032 and is 7.4% higher over the year. Australian equities bucked the global trend, with the ASX200 gaining 1.35% in price terms and 1.38% including dividends.

New Zealand markets were quieter. The New Zealand dollar was essentially flat against the US dollar at US$0.5631, while the NZX50 price and total-return indices slipped 0.3% apiece. Late in the month the Reserve Bank of New Zealand left its cash rate at 2.75% in a 4-3 split that stunned markets, which had all but fully priced a hike, despite a renewed pick-up in core inflation to around 3%.

The RBA did not meet in October, but the data kept the cash rate debate live. The September-quarter CPI confirmed that Australia remains mired in an entrenched inflation cycle, with the trimmed mean rising at a 4% annualised pace over the quarter and 3.7% over the year, even as the unemployment rate climbed to a five-year high of 4.7% in September and NAB business confidence sank to minus 13. Deputy governor Andrew Hauser conceded that the inflation outlook was "materially worse" than the bank had forecast in August, and bond markets ended the month pricing only one further increase. On 3 November the Board delivered it, raising the cash rate by 25bps to 4.85%, its highest level since 2008, in a 6-3 vote with three members preferring to hold, taking policy into the 4.75%-5.00% range implied by our Taylor Rule modelling.

Portfolio performance

October rewarded duration. The decline in government bond yields delivered strong gains across our fixed-rate strategies. The daily liquidity and AAA rated Coolabah Active Sovereign Bond Fund's Long Duration Class returned 1.07% gross (1.02% net of fees), the Active Global Bond Fund (GFXD) returned 1.70% gross (1.65% net), and the Active Composite Bond Fund (FIXD) returned 1.10% gross (1.08% net). With the 10-year Commonwealth yield falling 23bps and core global yields 26bps to 36bps, the month offered a small preview of the capital gains available to patient fixed-rate investors as the cycle matures.

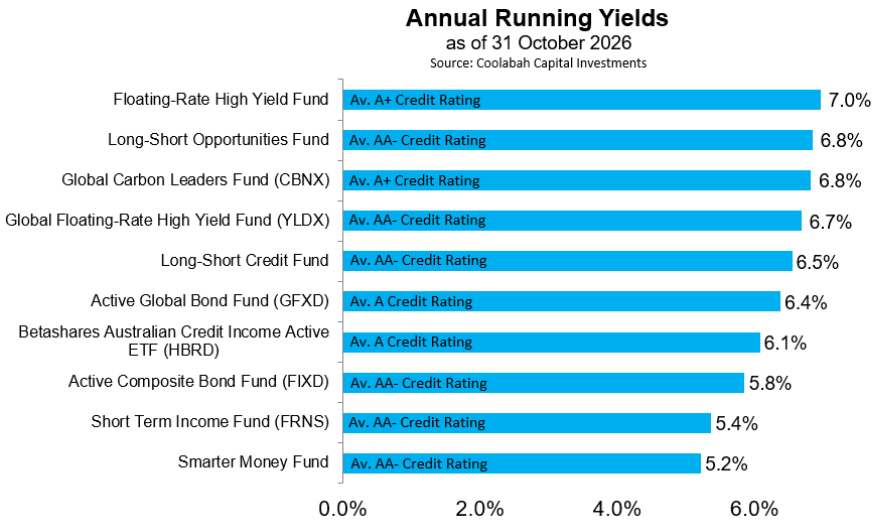
Strategy commentary cont'd: Among the floating-rate strategies, the Floating-Rate High Yield Fund, with an average A+ portfolio credit rating and zero interest-rate duration, returned 0.32% gross (0.26% net of fees) for its Institutional Class. The Short-Term Income Fund returned 0.28% gross (0.25% net) and the Smarter Money Fund 0.25% gross (0.21% net), with the widening in Australian credit spreads taxing returns in exchange for higher future yields.

The opportunity set remains. The RBA cash rate of 4.85% following the November hike and the 10-year Aussie government bond yield of 5.12% are both sitting way above long-term historical levels. We continue to favour averaging into fixed-rate exposure rather than trying to identify the precise peak in yields. If tight monetary policy and the housing correction eventually tip Australia into recession, the RBA could cut well below neutral, and high-quality fixed-rate government bonds could be major beneficiaries.

The return arithmetic remains attractive. Consider an illustrative 10-year government bond bought at par with a 5.12% annual coupon, paid semi-annually, and a 5.12% yield. Its modified duration is approximately 7.8 years. After 12 months, when the bond has nine years remaining, a rise in its yield to 6.12% would produce a capital loss of about 6.8%. Adding the year's 5.12% coupon income gives a total return of approximately -1.7%. If the yield instead fell to 4.12%, the capital gain would be about 7.5%, producing a total return of approximately 12.6%.

Under these assumptions, the bond's yield would need to rise approximately 74bps over the year before the investment lost money. These are illustrative absolute returns, before fees and tax and without coupon reinvestment, rather than forecasts or returns relative to cash. The income cushion does most of the work, while convexity adds a further benefit: an equal-sized fall in yields produces a larger capital gain than the loss caused by a rise. Persistent inflation and higher term premia remain risks, but we believe the combination of starting income and potential capital gains supports progressively building fixed-rate exposure.

At 31 October, the Floating-Rate High Yield Fund offered a gross running yield of 7.0% a year. The Long Short Opportunities Fund and Global Carbon Leaders Fund (CBNX) each had a yield of 6.8% per annum; the Global Floating-Rate High Yield Fund (YLDX) was at 6.7%; the Long Short Credit Fund 6.5%; and the Active Global Bond Fund (GFXD) 6.4%. Running yields are not forecasts of total returns, which also reflect changes in asset prices, hedging and fees.



Please note that past performance is not a reliable indicator of future performance. Investors should read the relevant Product Disclosure Statement and Target Market Determination before making any investment decision and consider obtaining advice from an independent financial adviser to determine whether an investment is appropriate for their objectives, financial situation and needs.

Strategy commentary cont'd: The Fed is on track to hike in December given strong inflation

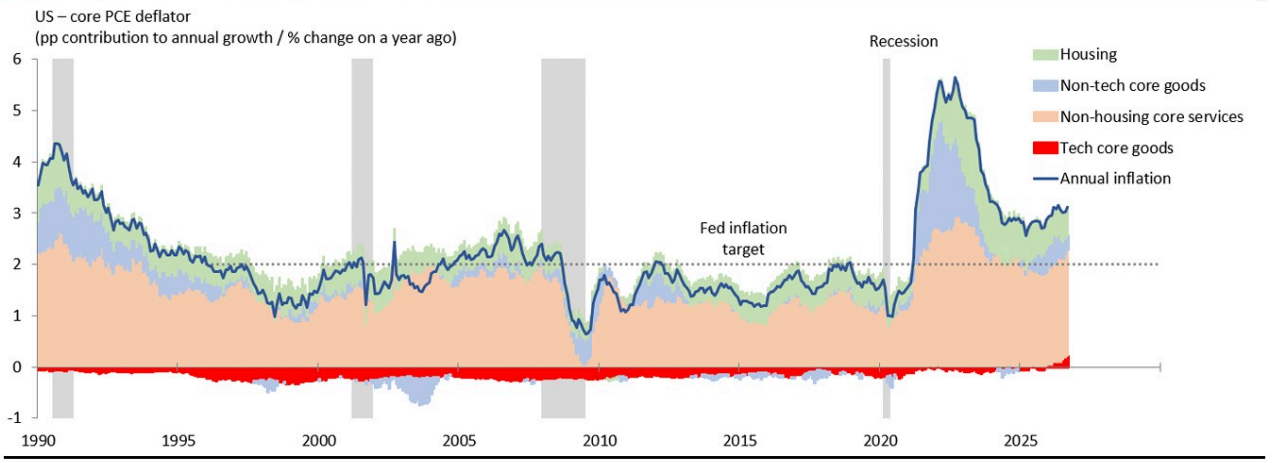
Still-high core inflation points to the Fed resuming raising rates in December.

After holding steady ahead of next week's mid-term elections, the Fed should resume raising rates in December given still-high core inflation, upside inflation risks, and no estimated slack in the labour market. A strong gain in the monthly core PCE deflator in September – which is the Fed's preferred measure of core inflation – supports this view.

The core PCE deflator matched market expectations, up another 0.3% in September (the monthly gain in August initially rounded down to 0.2% and now rounds up to 0.3%). Annual inflation was 3.1% and has ranged between 2.9% and 3.1% since December. An alternative indicator of core inflation belonging to the class of measures previously favoured by Fed Chair Warsh, namely the trimmed mean PCE deflator, rose by 0.2% for the third month in a row and is up 2.3% over the past year.

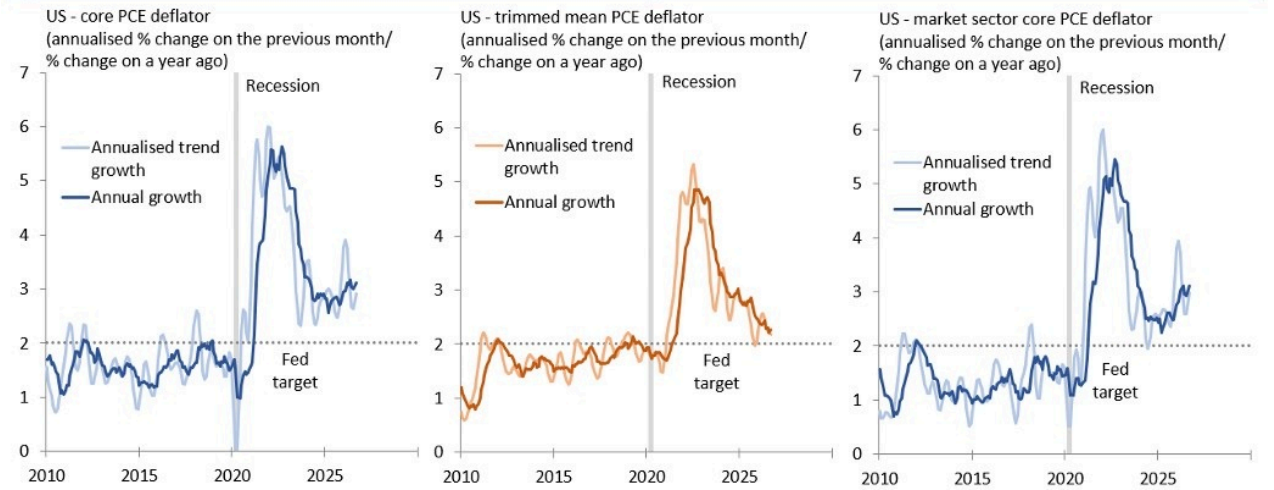
- Core goods prices rose by 0.2% and are 2.0% higher than a year ago. Tariff effects on goods prices are fading, but there is a boost from the AI boom and likely some impact from both high and volatile energy prices and global supply chain disruptions.
- Core services prices increased by 0.4% in September (also 0.4% excluding housing) and are 3.5% higher than a year ago (3.6% excluding housing).
- On CCI's estimation, tech prices are up 6% over the past year, adding 0.3pp to annual core inflation, contrasting with the pre-COVID experience when falling tech prices would usually subtract about 0.2pp from annual inflation.

Figure 1: The drivers of high US core inflation

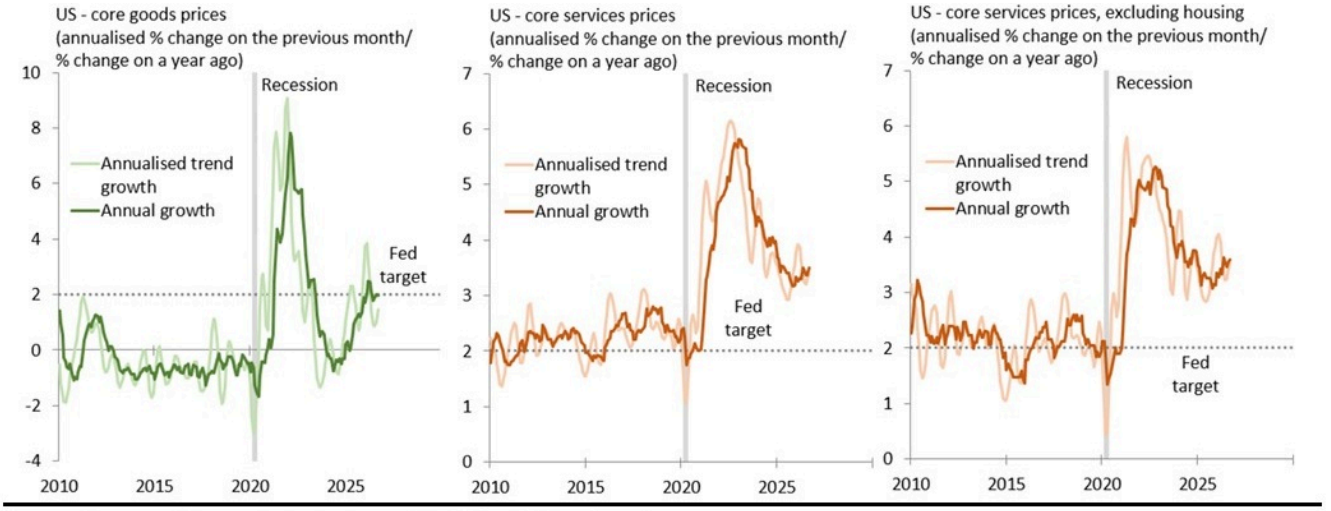


Source: Bureau of Economic Analysis, Coolabah Capital Investments

Figure 2: US core inflation remains well above the 2% target

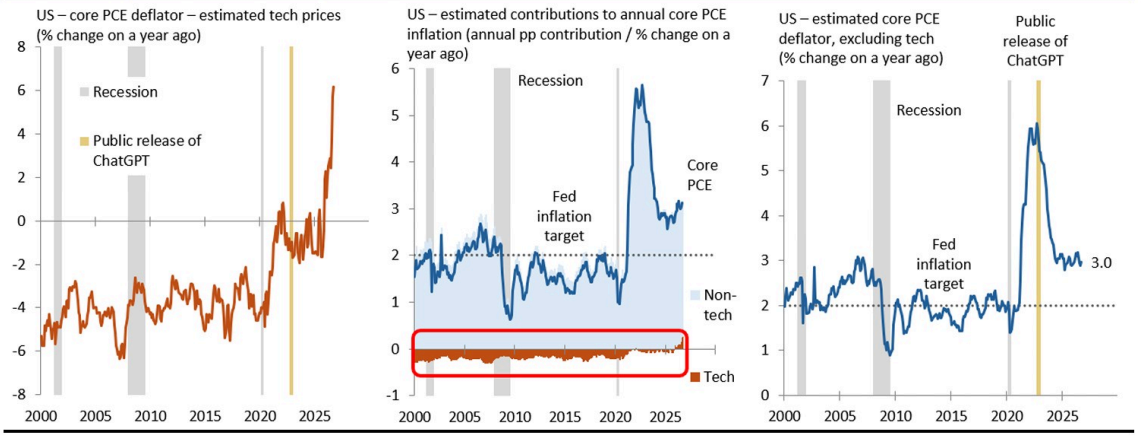


Strategy commentary cont'd:



Source: Bureau of Economic Analysis, Coolabah Capital Investments

Figure 3: Strongly-rising tech prices are adding to core inflation, contrasting with the pre-COVID experience when falling prices consistently subtracted from inflation



Source: Bureau of Economic Analysis, Coolabah Capital Investments

The risk of a US stock market correction viewed from the bond market

US equities would have to fall about 25% to return the risk premium over bond yields to more normal levels.

US equities have been very expensive for a long time when judged using simple measures of long-term valuation.

In valuing equities against bonds, US equities have historically paid a large risk premium above the risk-free rate, but this premium is currently at a historically low level, albeit not at the extremes of the dot-com bubble.

Defining the equity risk premium as the difference between the forward earnings yield and the real government bond yield*, the premium for the S&P 500 has averaged 4.6pp over the almost forty years for which data are available (the premium for the Nasdaq has averaged 3.6pp over the past twenty-five years for which there are data).

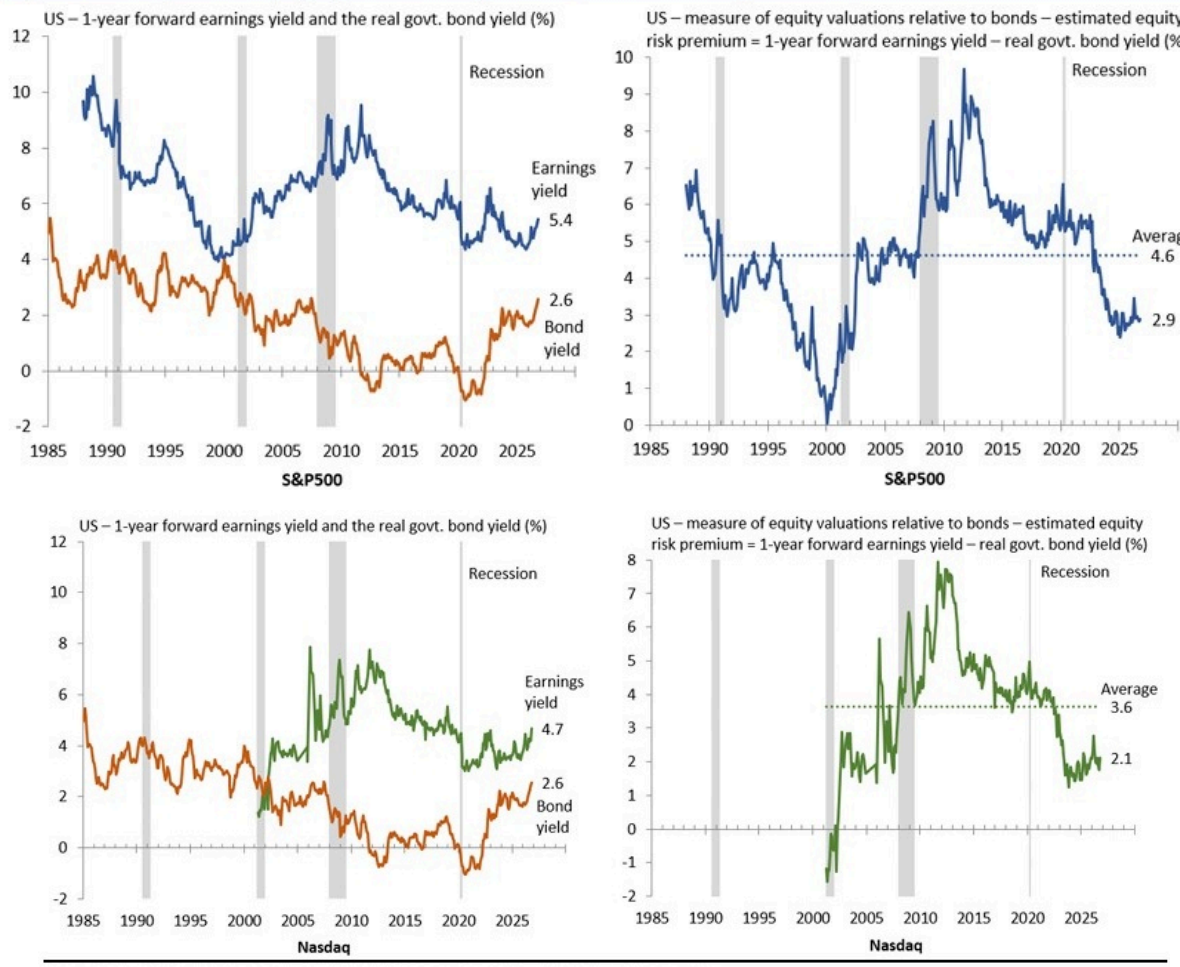
The equity risk premium for the S&P in October was well below this average at 2.9pp (or 2.1pp for the Nasdaq), although it has been around this low level for a couple of years now (or a few years in the case of tech stocks).

By design, these long-term metrics are not meant to provide a timing signal for the market, although, to provide an insight into what a sustained stock market correction could look like, the S&P 500 would have to fall by about a quarter to return the equity risk premium to its average level assuming broadly no change in earnings (about the same for the Nasdaq).

Strategy commentary cont'd: Realistically, though, in a scenario of a sustained stock market correction, a return to a more normal equity risk premium would also involve lower bond yields.

Note: * the 10-year real bond yield is the median of a number of estimates.

Figure 1: US equities are paying a historically low risk premium over government bonds



Note: The real 10-year government bond yield is the median of a range of estimates.

Source: Bloomberg, Board of Governors of the Federal Reserve System, Federal Reserve Bank of San Francisco, Federal Reserve Bank of New York, Federal Reserve Bank of Philadelphia, Coolabah Capital Investments

The BoE hikes rates and signals more to come

The BoE raised rates for the first time since 2023 and Governor Bailey signalled a further rate rise.

After recently warning about the risk of higher rates, the Bank of England raised the policy rate by 25bps from 3.75% to 4% because of high inflation and upside risks to inflation from high energy prices ("the duration and scale of the energy price increase had generated sufficient inflationary pressures in the pipeline to warrant an increase in Bank Rate").

Contrasting with expectations that some policymakers might vote to keep rates on hold, the decision to raise rates was unanimous, although there was a split in views over the size of the rate rise, with one policymaker voting for a 50bps increase (Mann). Governor Bailey pointed to a further rate rise, with the next two policy meetings scheduled for 17 December and 4 February.

Strategy commentary cont'd:

- **The BoE signalled a further hike was likely.**

  Governor Bailey pointed to another rate hike, saying, "without news which softens the risks to inflationary pressures, I can see the argument for a further increase in rates and thereafter taking a more conditional approach, dependent on the evidence on energy prices and inflation dynamics." Simple policy rules based on the BoE's economic outlook had pointed to a period of unchanged rates, although such rules are less reliable in the UK than in other countries given the uncertainty around estimating the UK NAIRU. The BoE forecasts were conditional on a market path showing interest rates peaking at almost 5% late next year.

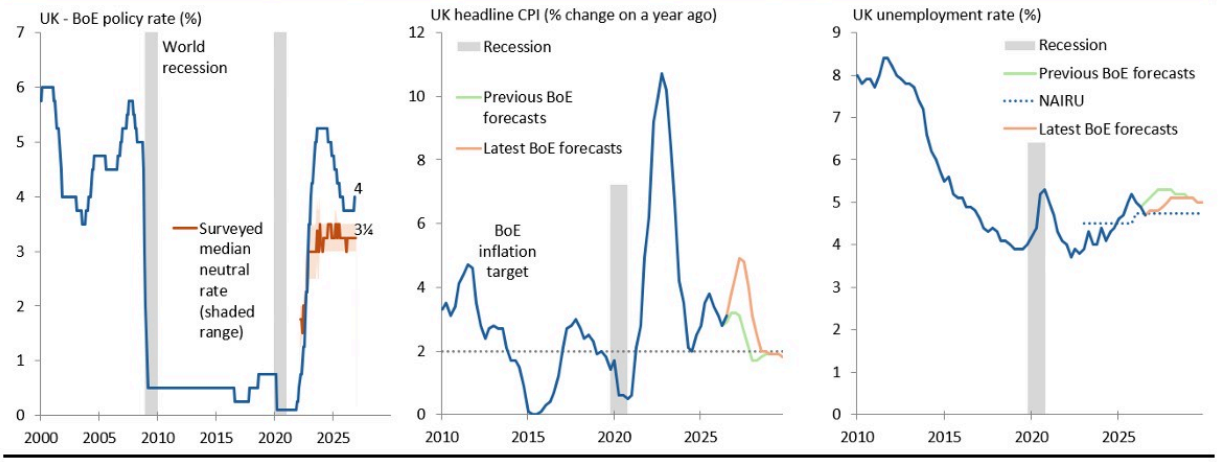
- **Upside risks to inflation from energy prices had increased.**

  There was "still limited evidence to date of second-round effects in wage and price-setting", but "second-round effects were likely to be state-dependent and the outlook for headline inflation had risen materially", such that the Monetary Policy Committee "judged that the risk of material second-round effects emerging had risen further since September and could remain a risk for some time".

- **The BoE expects slightly higher core inflation and the recent decline in unemployment to be reversed.**

  The BoE now expects a much higher peak in headline inflation of 4.9% (previously 3.2%), with inflation not returning to the 2% target until late 2028 (previously early 2028). The BoE only publishes a near-term outlook for core inflation, which is now expected to reach 3.2% by early next year (previously a peak of 2.8%). The recent decline in the unemployment rate is expected to be reversed, with unemployment holding around the 5% level over most of the forecast horizon (previously a peak of 5.3% and then holding around 5%).

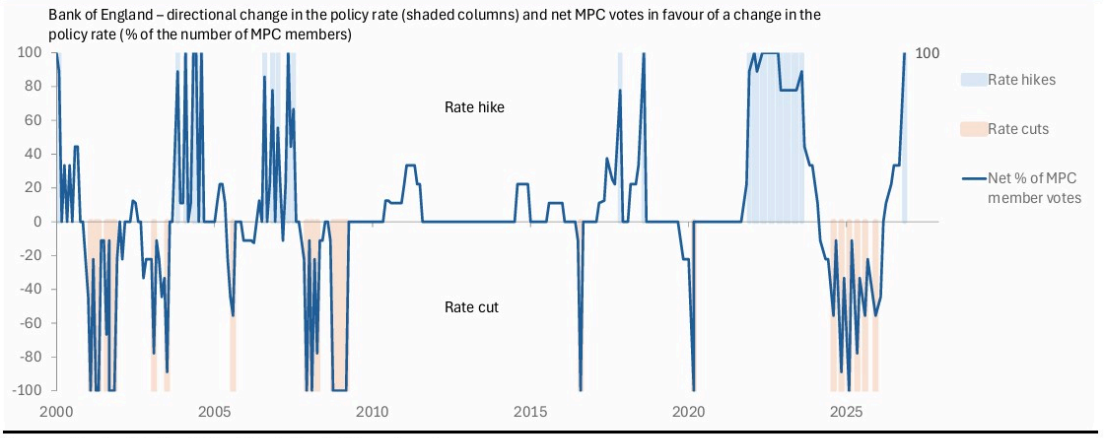
Figure 1: The Bank of England expects higher inflation and higher unemployment



Source: Bank of England, Office for National Statistics, Coolabah Capital Investments

Strategy commentary cont'd:

Figure 2: The Bank of England's decision to raise rates was unanimous, with one policymaker voting for a 50bp rate rise



Source: Bank of England, Coolabah Capital Investments

Booming US demand for AI driven by falling token prices

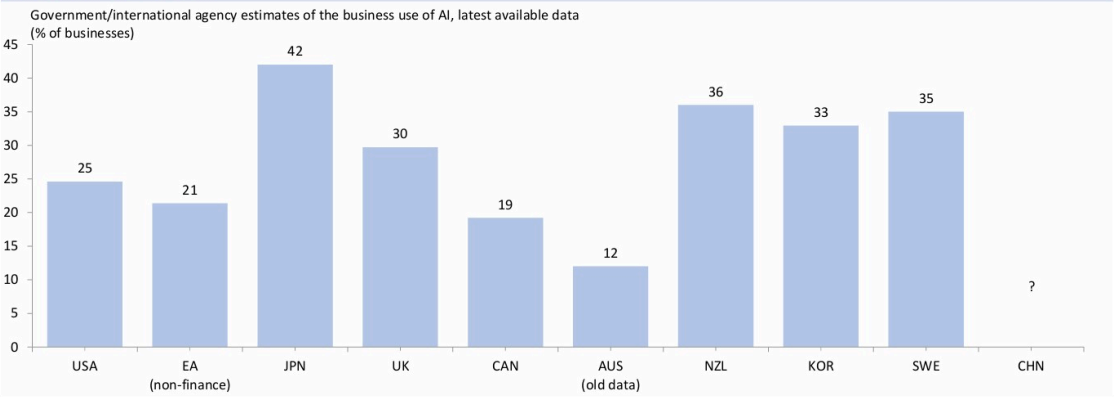
Outpacing the earlier take-up of the internet, US business adoption of AI is booming, propelled by rapidly falling token prices.

Business adoption of AI is booming, rapidly outpacing the take-up of the internet in the 2000s and 2010s, such that the eventual productivity payoff from AI could be delivered sooner than widely expected. The US experience shows AI is being used in all industries, although most intensively in the IT, professional services, and finance sectors. However, Ramp transactions data show that extraordinarily strong demand for AI tokens from US tech-intensive businesses is mostly a function of average token prices falling at an even faster rate, halving over recent months. As a result, growth in the dollar spend on AI tokens by US tech-intensive firms – while still very strong – has slowed sharply, which, if sustained, would raise questions about the return on the massive investment undertaken by AI providers.

- **AI usage by US and EA businesses ramping up, although it is lagging many other advanced economies.**

  Business use of AI varies considerably across countries and is actually at the lower end of the scale in the US and the euro area, at 25% of US businesses and 21% of EA non-financial businesses. However, some of the differences between countries can reflect differences in survey questions and sampling.

Figure 1: There has been widespread adoption of AI by businesses, although the US and EA are lagging some advanced economies



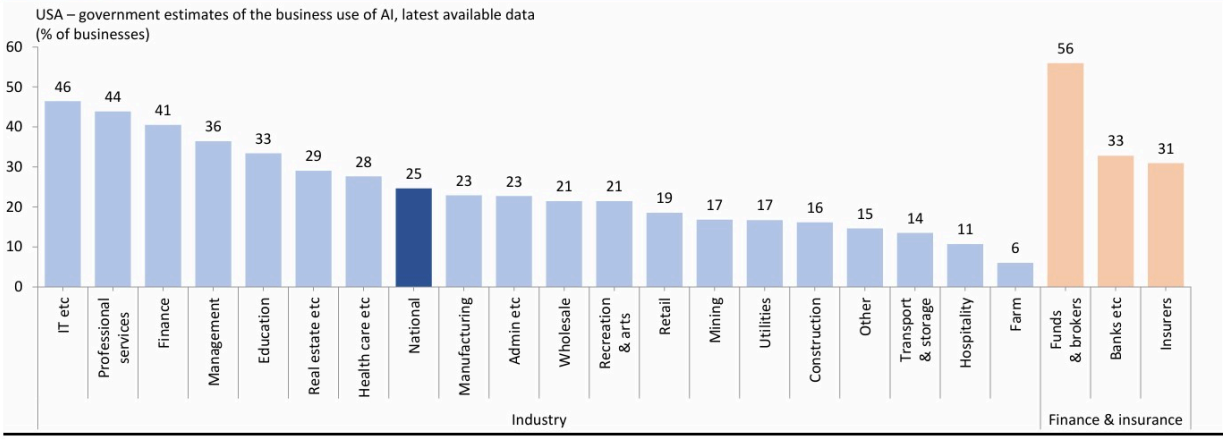
Source: Australian Bureau of Statistics, Census Bureau, Eurostat, Innovation platform agency, Ministry of Business, Innovation & Employment, Office for National Statistics, Organisation for Economic Co-operation and Development, Statistics Canada, Coolabah Capital Investments

Strategy commentary cont'd:

- **AI is being used across all industries in the US, but most extensively in the IT, professional services and finance sectors.**

  In the US, AI has made inroads across the entire economy, although there is a wide variation in industry use of AI. The heaviest users of AI are the IT, professional services, and finance sectors, which is not surprising, as they have long accounted for the bulk of investment in software. At the other end of the distribution, there is a long tail of industries with a below-average take-up of AI.

Figure 2: Every US industry is making use of AI, although the IT, professional services and finance sectors dominate

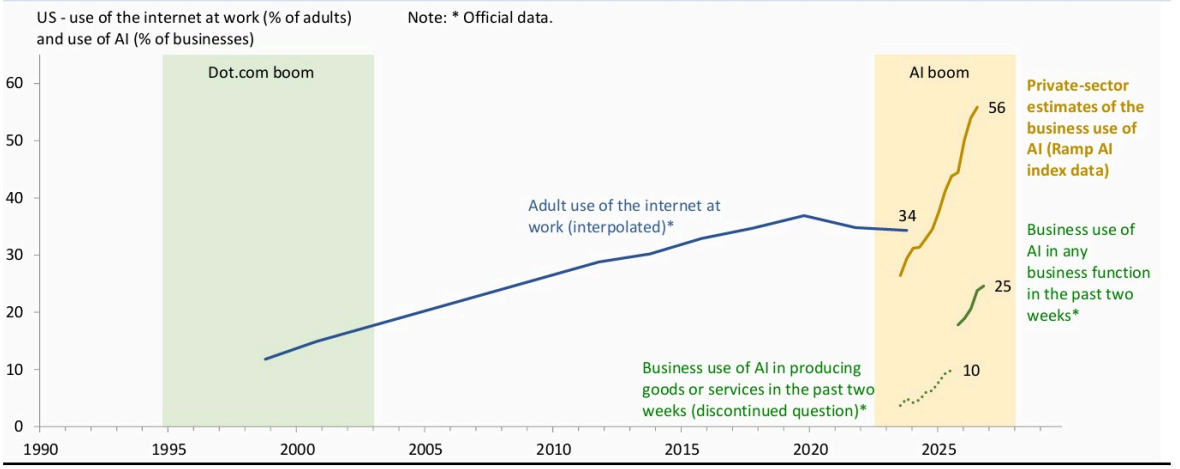


Source: Census Bureau, Coolabah Capital Investments

- **Business adoption of AI is occurring at a much more rapid rate than take-up of the internet, such that the eventual boost to productivity could emerge sooner than widely assumed.**

  The productivity payoff from AI could be delivered more quickly than the earlier payoff from the use of the internet given that US data show that business use of AI is growing at a much faster pace than take-up of the internet over the 2000s and 2010s.

Figure 3: US business adoption of AI is occurring at a much faster rate than the earlier take-up of the internet



Source: Census Bureau, Ramp Business Corporation, Coolabah Capital Investments

- **Private-sector data overstate the economy-wide use of AI in the US, but provide the right signal on the direction.**

  Private-sector estimates of business use of AI in the US – such as the transaction-based data published by Ramp that are monitored by the Fed – are heavily skewed towards companies that are more intensive users of AI, although they still provide valid insights into the rate of take-up of AI.

Strategy commentary cont'd:

- **US business use of AI is booming among heavy users of technology, but only because the price of AI tokens has halved over the past three months.**

  With that caveat, the Ramp transactions data show that business use of tokens for the top AI models continues to grow at an exceptionally rapid rate, increasing by about 70% over the past three months in log terms. However, this phenomenal growth has been supported by average token prices falling at a much faster pace, down about 50% over the past three months in log terms.

- **Falling prices mean that the dollar value of US tech-intensive business spending on AI has slowed sharply, albeit to a still strong rate, which is problematic for AI providers if sustained.**

  With exceptionally strong demand for AI tokens propped up by rapidly falling average token prices, growth in US tech-intensive businesses' dollar spending on tokens has slowed sharply, according to the Ramp data. Log growth over the past three months is still strong at about 20%, but this is the slowest growth since a brief volume-driven contraction late last year, and well below the average 60% growth over most of this year. It is too soon to know whether this slowdown will be sustained, but it raises questions about the return on investment for AI providers.

Figure 4: Ramp data show spending on AI tokens by US tech-intensive businesses has slowed to a still -strong rate, as exceptionally rapid growth in demand is driven by token prices falling at a much faster rate



Source: Ramp Business Corporation, Coolabah Capital Investments



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