



## CIO OFFICE MORNING MARKET WRAP

### 26 May 2025

Markets were buffeted by rising concerns about high levels of sovereign debt that saw yields rise in concert across the developed countries, as well as by tariffs back in the spotlight at the end of the week. Equities, bonds, and the dollar all retreated despite a good business confidence print in the United States. Data in China and Europe failed to help, showing lacklustre growth in both areas. The three main US benchmarks lost at least 2.4%, led lower by Energy (-4.4%) and Information Technology (-3.5%), with all equity sectors ending in the red. DM ex-US gained over 1%, despite both Europe and Japan ending in negative territory, while the Emerging Markets closed little changed. The yield on the 10-year note rose by 3bps to close at 4.51%, retreating from a high at 4.61%, and the 30-year yield settled just above 5%. The dollar saw consistent selling to finish 0.8% lower, whereas gold surged 4.9% on global bond turmoil. Bad news started the previous Friday, with the downgrade by Moody's of the US credit rating, continued on Wednesday as a 20-year Treasury auction saw poor demand, while on Thursday the House approved Trump's sweeping tax-cut bill keeping the US debt on the wrong trajectory. Equities fell, longer-term yields pushed higher, and the 30-year yield reached its highest level since 2023. Inflation was above expectations in the UK and in Japan, that exacerbated negative sentiment and caused longer-dated JGB yields to blast through multiyear highs. On Friday Wall Street was rattled by President Trump's threats to impose 50% tariffs on the European Union starting June 1, as well as a 25% levy on Apple, that fell 3%, if it did not produce its iPhones domestically. Later the threat was broadened to Samsung and all iPhone producers. Investors were reminded that the reprieve on reciprocal tariffs expiring in June and the truce with China ending in August kept the trade war in the driver's seat. At the same time, peak volatility should be behind us as trade negotiations will be ongoing. Also, the solid monthly performance of the S&P 500 alongside the broad degree of market participation historically has meant further stock gains 12 months ahead. Economic uncertainty kept Fed speakers through the week from warming up to more rate cuts for the year. NY Fed Williams said it will take time beyond June and July for a clearer outlook, while money market traders lowered easing bets to slightly less than two cuts by year-end. On the opposite front, the April ECB minutes highlighted concerns about the disinflationary effects of tariffs on the economy pointing to an easing bias of the Governing Council.

Fiscal issues were at the forefront of investor's minds, and rightly so. It is not only about the United States, but rather a whole bunch of countries, the UK, Japan, Canada, and Australia, with similar policies that bond markets don't like. It is mostly about core inflation being above target, a loose fiscal stance, and in some cases dovish central bank forward guidance. Under these circumstances bond investors demand a higher yield for the inflation risk they are taking. There is a long-term outlook, very much different from the shorter-term one, for DM-country debt sustainability. Let's take the US case. Longer term stagflation is likely, as rising yields at some point will force central banks, the Fed, to resort to yield-curve-control, or at least massive open-market purchases to cap rising interest costs. And nominal yields below inflation indeed tend to foster price pressures. Commodities in general, currently being led by gold, would be in a great bull market, and equities would be underperforming. Shorter term, the can will be kicked further down the road. Should yields rise further, the large amount of US debt to be rolled over this year could be tackled by raising the share of T-bills over coupon-bearing bonds, that would represent a cash injection for the economy. And this would further enhance the easing effect of lower dollar and oil prices, that are already translating into positive economic surprises. And first and foremost, the Fed would be stepping in with some round of QE to cap the 10-year yield below 4.8%, providing a further boost to markets. Overall, the debt crisis represents one more reason for policymakers to add to the overall liquidity, and this is what markets in the current fast and furious rally may be looking forward to.

#### Markets this morning:

US and European equity futures climbed with Asian stocks on Monday as President Trump eased trade tensions extending a deadline on aggressive tariffs on the European Union. Levies on European goods were pushed back to July 9 from June 1 following a call with European Commission President von der Leyen. Contracts for the S&P 500 and the Nasdaq advanced about 1% and those for the Euro Stoxx 50 jumped 1.4%. The dollar fell 0.3% to its lowest level since December 2023, while oil edged higher, and gold slipped.

#### Upcoming key events/data:

US financial markets will be closed today in observance of the Memorial Day holiday. Investors will be focusing on Nvidia's 1Q results on Wednesday, with the company expected to beat 2026 consensus projections on accelerated adoption of its chips. The main macro highlights for the week are the release of the Fed's minutes on Wednesday, and the report on personal income and spending on Friday that includes PCE inflation, of extreme relevance for the direction of Treasury yields. The second print of Q1 GDP on Thursday should not see significant revisions. China industrial profits will be reported on Tuesday, and Germany inflation on Friday alongside Tokyo's CPI ex fresh food.

Best Regards,

Chief Investment Office  
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