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The new normal is volatile, unpredictable, but not necessarily adverse

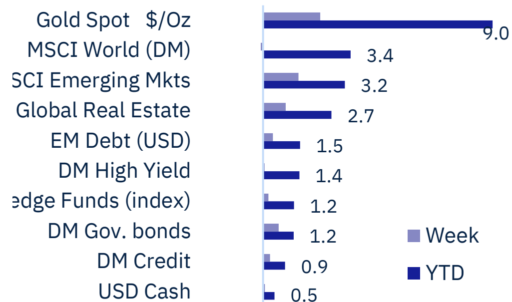
- **Last week was volatile but positive for all major asset classes except for DM stocks**
- **January PMIs show a still resilient global picture, while US labor market remains strong**
- **The perspective of tariffs continues to shake markets as well as US consumers' sentiment**

The first week of February was rich, volatile, but overall positive for all major asset classes except stocks from developed markets, down a modest -0.1%. The dollar ended a tumultuous week -0.3% weaker, despite a +10bps increase in short dated 1 and 2-year Treasury yields. The 10-year was overall stable at 4.5%. Gold jumped to another all-time high of $2,861, and the price of Brent crude oil fell $2 to $74.7.

Final PMIs for January came in and confirmed a gentle global slowdown in services, and no significant rebound in manufacturing except for the US. The global composite PMI dropped -0.8 to 51.8, though the most forward-looking components, new orders and employment, remain solid. The UAE printed a strong 55. The January US jobs report indicated only 143K job creations, below forecast, but previous months were revised higher. The labour market stays impressive, with unemployment down to 4% and hourly earnings up +0.5%. This looks like good news for consumption. However, the Michigan consumer sentiment index unexpectedly slumped to 67.8, a 7-month low. Households are concerned about future inflation, due to the perspective of tariffs, and it shouldn't improve as President Trump announced imminent "reciprocal tariffs" that will affect "everyone". This explains Friday's rise in short-dated yields and the reversal in risk appetite, despite a still supportive earnings season. President Trump added last night an announcement on tariffs on aluminium and steel.

Similarly to last week's Mexico and Canada saga, we won't take all announcements at face value but wait for details. We are fully invested, which so far works. Our monthly investment committee this Tuesday will consider all options. Our 2025 Global Investment Outlook publication is ready, and we can't wait to meet you in our upcoming roadshows. The week ahead will provide inflation data, central bankers' speeches, more earnings and maybe more surprises from Washington DC.

ASSET CLASSES USD % TOT.RETURN, LAST WEEK AND YTD 2025



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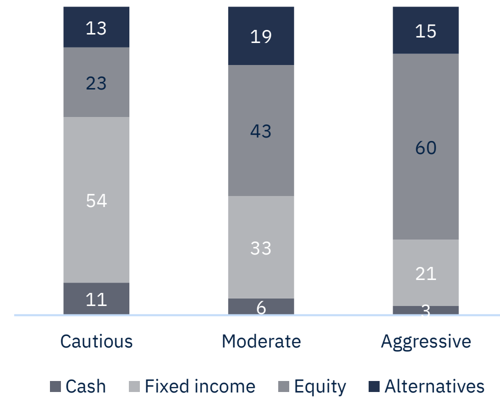
Cross-asset Update

Treasury Secretary Bessent made important statements about yields and the dollar. He said the administration is focused on policy that affects longer-dated yields, rather than short-term rates, and that a "strong dollar policy is completely intact" under President Donald Trump. A cursory reading tells us that investors will be reassured by Bessent's calming words. The impression was that at some point President Trump might want to have more than just a say on monetary policy and actively affect it. The independence of the Fed would be challenged, causing uncertainty and market volatility. Also, the president had complained that the United States has "a currency problem" undermining the competitiveness of the industry. Persistent dollar weakness would be an issue as well, with rising imported inflation, and less appeal for US financial assets. But we must scratch below the surface to get to the real implications of the Treasury Secretary's statements.

Focus on longer-dated yields has nothing to do with avoiding conflicts with the Fed, it rather has the purpose of keeping the debt burden in check. It is in the best government's interest to extend the maturity of its obligations to diversify risk, so it becomes very important that long rates are maintained as low as possible. To this end, keeping inflation in check would be the main goal, and this is actually the mandate Donald Trump has from his electorate. But ultimately tariffs, a strong US economy, lower policy rates, or a mix of that could lead to resurfacing inflationary pressures.

Under those circumstances, the only socially acceptable option to keep a lid on yields would be to suppress them via some form of yield curve control. That would cause a weakening of the dollar and would represent a blue-sky scenario for gold. Gold is the best hedge against currency debasement, and artificially low yields depressing the reserve currency would be a boon for the yellow metal. In the end, yields and the dollar are linked. Low yields can coexist with a strong currency as long as inflation is not an issue. We suspect that at some point it will be, benefitting gold at the expense of the dollar. The Treasury Secretary may not be able to achieve both of the administration's goals at the same time.

TACTICAL ASSET ALLOCATION: SIMPLIFIED POSITIONING

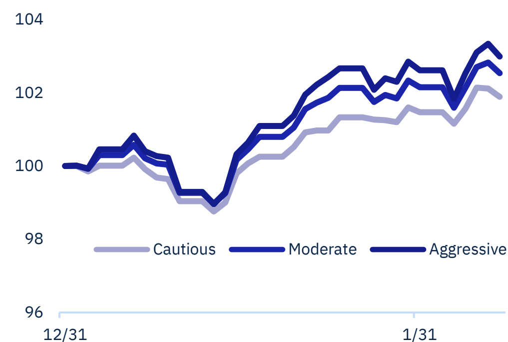


TAA – RELATIVE POSITIONING – MODERATE PROFILE

UW/N/OW: Underweight/Neutral/Overweight

	UW	N	OW
Cash			>
DM Gov.			>>
DM Credit		=	
DM H. Yield		=	
EM Debt		=	
DM Equity			>
EM Equity		=	
Gold		=	
Hedge Funds	<<		
Real Estate		=	

TAA – 2025 INDICATIVE PERFORMANCE



Source: Bloomberg. CIO Office calculation based on TAA applied to market indices, net total return in USD.

Fixed Income Update

The yield curve has twist-flattened with the front-end up by 5 to 10 bps and the long-end down between 3 to 8 bps last week. There were a lot of volatility as macro data and policy announcements continued to roil markets. The potential for the trade war to broaden looms. The long-end has been kept in check due to Secretary Bessent's comments that President Trump wants the long-end yields to stay down rather than focusing on the policy rates and Treasury's refunding announcement which kept the auction sizes unchanged as well as saying that the Treasury is well-funded till the third quarter allying any fears about increasing bond sales in near future. These comments helped ease concerns surrounding the Fed's independence and the potential for near-term changes to issuance plans. This week markets will be focused on the January CPI report. Economists anticipate the core to increase to 0.3%.

Last week's Jobs Data had a little bit for everybody but was bearish for bonds. The December JOLTS report indicated job openings fell 7% to 7.6mn, driving down the vacancy/unemployed ratio from 1.15 to 1.10 which is consistent with stable labor market conditions as indicated by recent initial claims readings. Nonfarm payrolls printed slightly weaker than expected at 143k last month, but the rest of the report was firm with December jobs revised upwards to 307k, the January unemployment rate declining back down to 4.011%, the lowest since May. The 10-year yields jumped 4 bps to hit 4.52% before settling around the 4.5% figure. This data should signal the Fed to be on pause for the moment. Markets now predict only a 7% chance of rate cut in March and a total of 35 bps of rate cuts in 2025.

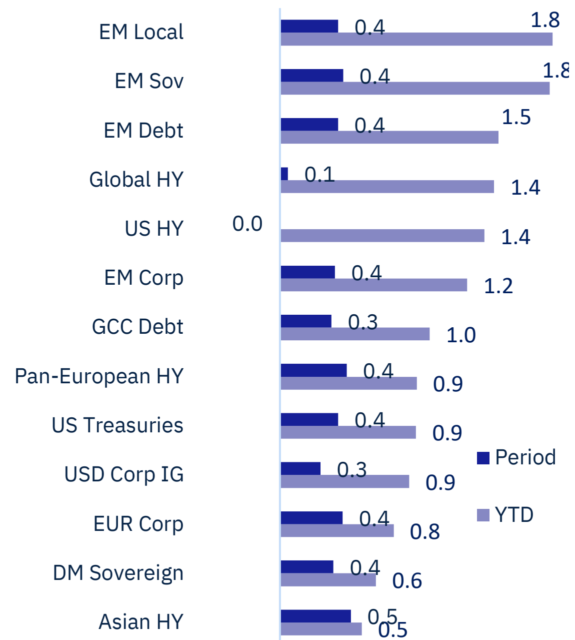
Credit spreads continue to be range bound as technical and fundamentals both support the credit markets. HY and EM Debt YTD returns have crossed 1.4%. Valuations remain quite expensive in light of all the uncertainties. IG maturity is set to surge as a record $790bn were issued between March and May 2020. According to JPM estimates, there will be $325bn of maturing IG bonds during March to May of this year reducing the Net issuance by double digits and keeping a firm ceiling on the spreads. The tariff impact on spreads would be minimal unless we see significant EU tariffs or a surge in inflation that changes Fed's current stance towards more hawkish.

The Emerging Markets continue to be volatile with tariff threats impacting currencies. MXN has already had eight moves greater than 2% in either direction this year. Chinese tariffs have come into effect along with retribution. However, as of now tariffs are seen more as a rhetoric than an actual risk. Thus, EM Debt returns have been steady. GCC credit has returned 1% with issuance tracking last January and KSA leading the bandwagon. The planned 25% tariff on aluminum and steel does not impact the GCC issuers which have outstanding bonds.

FIXED INCOME KEY CONVICTIONS (2024)

DEVELOPED MARKETS
Overall overweight DM FI
OW Government Bonds
Neutral corporate (IG & HY)
EMERGING MARKETS
Neutral EM Debt
Favor quality and selectivity
Including in GCC

FIXED INCOME SUB ASSET CLASS RETURNS (YTD, LAST WEEK)



Source: Bloomberg

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Equity Update

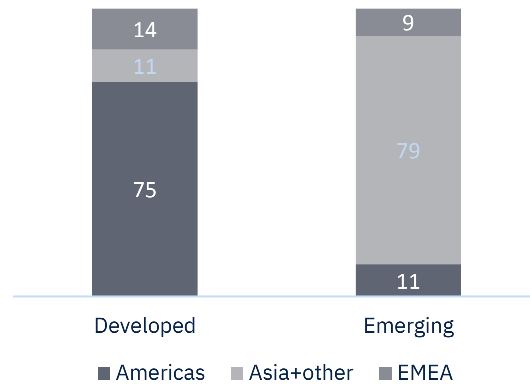
Global equities climbed for most of the week, though momentum collapsed on Friday after President Trump announced plans for new reciprocal tariffs. The MSCI ACWI finished flat, just slightly positive, for the week up, with emerging markets outperforming, rising 1.4%, while developed markets edged lower by 0.1%. The S&P 500 declined 0.2%, with selling pressure picking up on Friday after the Dow fell 444 points. Markets had already been grappling with weak consumer sentiment and stubborn inflation data, but the latest trade threats pushed markets lower. Meanwhile, cracks started to appear in the AI rally. Nvidia did rebound from the previous week's losses, but AMD struggled after failing to provide a clear outlook on future AI chip demand. Tesla faced its worst week since October, losing ground to Chinese rival BYD, which surged ahead on excitement around its latest self-driving technology. The sudden reversal left markets at a crossroads, with strong earnings on one side and renewed inflation and trade risks on the other.

The earnings season remained a key driver. 62% of S&P 500 companies having reported so far, 77% have beaten EPS estimates, and 63% have posted higher-than-expected revenue. Amazon and Microsoft both signaled higher spending on AI infrastructure, with Amazon committing to a $105 billion capital investment in 2025, up 25% from last year. Alphabet's earnings also reinforced the challenge of turning the AI hype into immediate revenue, with Google Cloud growth slowing, sending the stock down 7%. Tech stocks were the most volatile. Nvidia gained 8%, recovering some ground as fears over DeepSeek's AI model have begun to wane from the previous week. Tesla had its worst week since October, tumbling 11% as global sales weakened. The company lost market share in China, where deliveries fell 11%, just as BYD surged 21% on its latest self-driving technology.

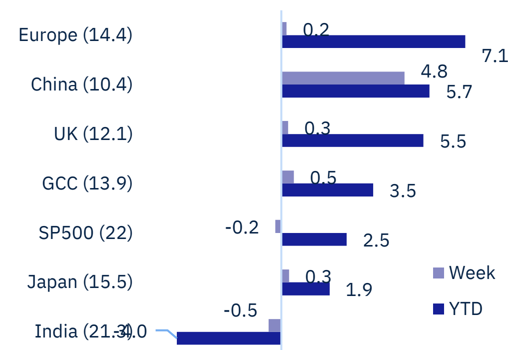
European stocks moved higher, with the MSCI Europe Index rising 0.7%. The FTSE 100 added 0.3%, continuing its run of record highs as money shifted away from US tech stocks. However, the broader European market faced pressure from Trump's tariff plans, with the Stoxx 600 declining 0.4% on Friday. L'Oreal disappointed, dragging down luxury stocks; Porsche fell 8% to a record low after lowering its profit outlook due to weak EV demand. Banks held up well and suggested they can maintain strong returns over the long term by focusing on fee income and loan growth, even as interest rates decline. Six major lenders are planning to distribute nearly €24 billion in dividends and buybacks over the next few months.

Asian equities were led by China. The Hang Seng Tech Index jumped 4.5%, its best week since October on the back of Tencent and Alibaba . DeepSeek's AI breakthrough lifted Chinese tech stocks, with the CSI 300 rising 2.0%. BYD was one of the biggest winners, soaring 21% as analysts raised expectations for its self-driving capabilities. Elsewhere in Asia, the MSCI India Index gained 0.5%, but the mood was cautious. The RBI delivered its first rate cut in five years, but a weaker growth outlook limited gains. Japan underperformed, with the TOPIX falling 1.8%. Speculation is growing that the BOJ could raise rates sooner than expected, adding strain to equities.

EQUITY RECOMMENDED REGIONAL POSITIONING

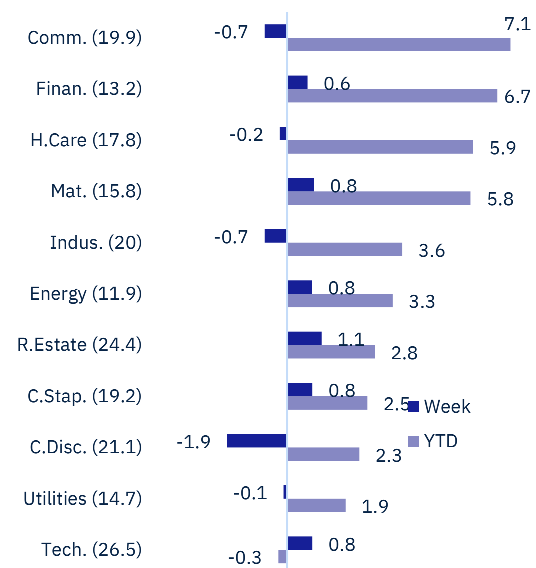


MAJOR INDICES PERFORMANCE (TR, US$), P/E in brackets



Source: Bloomberg consensus. MSCI Indices unless specified.

GLOBAL SECTOR PERFORMANCE (TR, US$), P/E in brackets



Source: Bloomberg consensus. MSCI All Country World sectors US$.

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