# Risk aversion comes back despite positive fundamentals

- **Military escalation in our region and competitive developments in AI from China put markets under pressure**
- **Meanwhile, economic data and the start of the earnings season were objectively supportive**
- **Geopolitics are top of mind as could hurt sentiment far beyond just speculative assets**

Last week was extremely rich and to some extent, important. Today marks the 10th day of intense exchanges of fire between Iran and the US, and while most targets are military and linked to the control over the Strait of Hormuz, seeing strikes on infrastructure is a risk of material escalation. Brent crude prices were the first to react, up 15%. We continue to hope that an all-out war will not happen, with many rational reasons for both parties involved. But let's face it: there is no ceasefire anymore, and visibility has seriously worsened.

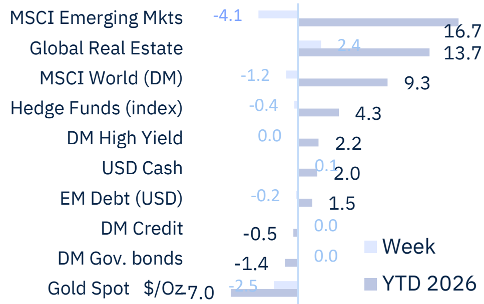
Risk-assets were logically next in line to react, that happened on concerns about AI sustainability combined with geopolitical tensions. Amidst the massive capex plans of hyperscalers, the competitive breakthroughs from China, and clear signs of reckless speculation in some segments (as we have regularly highlighted), it was no surprise that Korea, semiconductors, and the US tech universe suffered last week.

It is however important to note that fundamental data releases were nothing short of positive. The US combines robust growth, confirmed by steady industrial production and resilient retail sales, with a lower-than-expected inflation in June as per the CPI report. China disappointed on the first estimate of their Q2 growth, but not on trade nor on consumption in June. Finally, the Q2 earnings season started in a very positive way with spectacular results overall for US large banks.

As we wrote in this very publication last week, "all it would take for fundamentals to drive markets again is an improvement of the geopolitical situation". And, unfortunately, reciprocally. There is no way to tactically "play" such a situation, especially with a high level of unpredictability from the leaders involved. We thus haven't changed our positioning which has so far this year delivered clearly positive returns.

Have a great week.

Asset Classes USD % total. Return, week and YTD 2026

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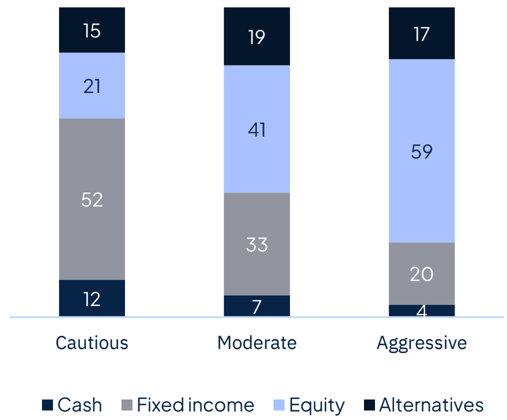
## Cross-asset Update

It was a very important week. Critical developments occurred in the Gulf crisis, that represented a turn for the worse. We got answers on the state of the US economy, currently in Goldilocks mode, an ideal condition. Fed chair Kevin Warsh reiterated his convictions during the Congress testimony, against inflation and pro-AI. Earnings for Q2 impressed, though markets failed to respond positively. China showed new progress in the AI race, and US investors panicked. Markets reacted negatively in the end, and it was more of an AI story, than anything else, as mid and small caps suffered only modest losses. Chip giants ASML and TSMC reported stellar fundamentals that failed to impress, as investors more and more weighed aggressive IT capital spending against the massive future profits required to make those outlays good. Concerns about the sustainability of AI capital expenditures were reinforced by further progress of Chinese models that work as effectively on much less compute power. To top it all, AI capex spending is expected to grow an outsize 75% this year, yet to slow down to 25% in 2027 and 6% in 2028 according to consensus estimates. Investors will be demanding consistent positive surprises to continue to be in love with the AI theme, that will be predicated on the demand side not stalling, ever.

Financial conditions tightened during the week, that added to the geopolitical flare ups. Treasuries recorded modest gains despite benign CPI and PPI prints on Tuesday and Wednesday. At the same time, inflation expectations fell significantly as Kevin Warsh maintained hawkish tones during his Congress testimony. The end result was that real yields, the difference between nominals and those expectations, hugged the highs of the year, even as Brent crude rallied strongly on growing supply concerns. Gold held a key support level, looking through the Fed chair's rhetoric helped by the softer inflation data. A spike in crude prices that proves to be sustained would be weighing on equities, bonds, and even gold, the latter most likely outperforming in relative terms.

The US economy showed the best of both worlds, on the growth and the inflation side, a so-called Goldilocks backdrop, for now. The NFIB survey, that measures the health of the smaller companies, pointed to optimism, and the Beige Book, a nationwide Fed survey, to steady growth. June retail sales were roughly in line with consensus, with the report highlighting resilient spending. At the same time, global growth ex-US has been slowing, as highlighted by the global share of countries showing positive growth in leading indicators dipping below 50%. Given recent market euphoria, and resurfacing geopolitical risks, we see the current backdrop as too finely balanced to be comfortable taking additional market risk. We are actually happy with our slightly defensive asset allocation, skewed towards cash and modestly underweight risk assets.

### 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 | | = | |

**Fixed Income Update**

The week was shaped by geopolitical tensions and softer inflation data. Escalating US-Iran tensions, including US strikes on Iran and Iranian attacks on Kuwaiti infrastructure, drove Brent crude higher, with oil futures up over 11% on the week. This revived inflation concerns and kept central banks and bond markets on edge. The key macro release was June US CPI, which came in softer than expected as consumer prices fell month-on-month for the first time in six years. Treasuries were volatile: 10-year yields began near 4.62% as oil surged and rate-hike bets rose, before soft CPI triggered bull steepening and front-end yields fell 8–10 basis points. By Friday, renewed oil-driven inflation fears pushed two-year yields higher while intermediate and long-end yields fell, flattening the 2s10s and 5s30s curves. The probability of a July Fed rate hike dropped from around 40% to below 17%. June PPI also missed expectations, reinforcing the disinflationary signal.

Fed Chair Kevin Warsh testified before Congress, repeating his inflation concerns, though markets continued to discount his views. He moved away from the Dallas Fed's trimmed mean as his preferred inflation measure, currently at 2.41%, and said AI-led price increases are not necessarily inflationary, signalling patience on temporary price pressures. The ECB is expected to hold on 23 July, while markets price an 85% chance of a September hike.

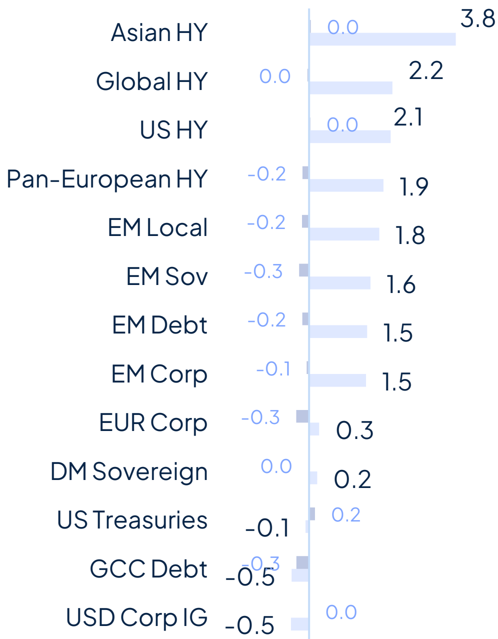
May TIC data showed foreign investors bought a net $56.6bn of long-term Treasuries, the highest since November 2025. Demand was led by private investors, who added $55.3bn, their strongest monthly buying since August 2025, while foreign official accounts bought only $3.0bn. By region, buying was concentrated in Canada, Hong Kong, and the UK. Foreign official demand is likely to stay muted, given attractive local government bond yields, notably JGBs, while US official demand should also remain low due to the Fed's hawkish bias.

The Bloomberg US IG index returned +0.07%, while new issuance fell 6% to $50.3bn across 17 issuers. Hyperscaler bonds from Meta, Alphabet, and peers, used to fund AI infrastructure, weighed on global fixed income indices, with negative total returns and wider spreads across the US, Europe, and Asia. In US HY, OAS widened 5 basis points, while the Bloomberg US Corporate HY index returned +0.03%. S&P Global affirmed Indonesia's long-term foreign-currency rating at BBB with a stable outlook, contrasting with Moody's and Fitch, which had moved their outlooks to negative earlier in the year. Despite escalating regional events, GCC IG spreads remain anchored and remain in the 80s vs US treasuries. High beta issuers from the region remain more exposed to risk premiums and have shown some recent weakness without significant widening of spreads.

Fixed Income Key Convictions

| |
|---|
| **DEVELOPED MARKETS** |
| Overall neutral DM FI |
| Cautious on duration… |
| … But opportunistic |
| **EMERGING MARKETS** |
| Neutral EM Debt |
| Favor quality and selectivity |
| Including in GCC |

Fixed Income Sub Asset Class Returns
(US$ TR, week, YTD 2026)



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**Equity update**

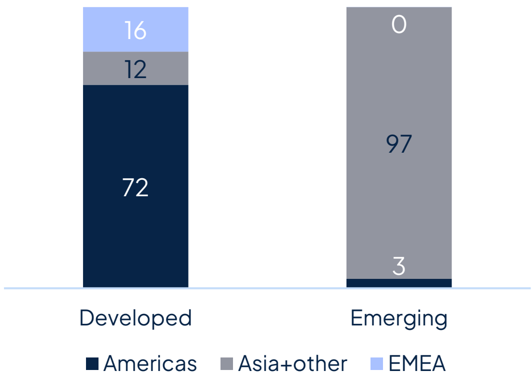
Global equities turned lower through tech last week as the US-Iran conflict deepened and China delivered another AI shock, Moonshot's Friday release of its Kimi K3 model reignited doubts over the payback on AI capex. The S&P 500 fell 1.5%, trimming its year-to-date gain to around 9.4%, and the Nasdaq lost 4.1%. Europe was the resilient side this time, the Stoxx 600 flat and the UK up 1.3% on its lighter tech weighting, while Asia bore the brunt: Japan fell 4.1%, India 0.9% and Taiwan dropped 6.5% on Friday alone. From the sector perspective, the rotation extended, Real Estate and Energy leading, the latter's year-to-date run now above 26% as Brent surged roughly 16% from $76 to around $88 with Iran declaring the Strait of Hormuz closed, while Tech (-4.7%) and Communications (-2.2%) sat at the bottom.

Underneath, the semis again did the damage. The SOX fell 10%, marking its worst week since April 2025, now in a bear market. IBM crashed 24% on a revenue pre-announcement, and, more telling, ASML and TSMC delivered blowout beats, but were sold anyway (-2.8% and -8.3%) as investors set aggressive capex against Chinese models running on a fraction of the compute. The hyperscaler-semis inversion flagged last week has moved to the centre of the debate, making this week's hyperscaler prints a test of that dislocation rather than of the quarter's numbers themselves.

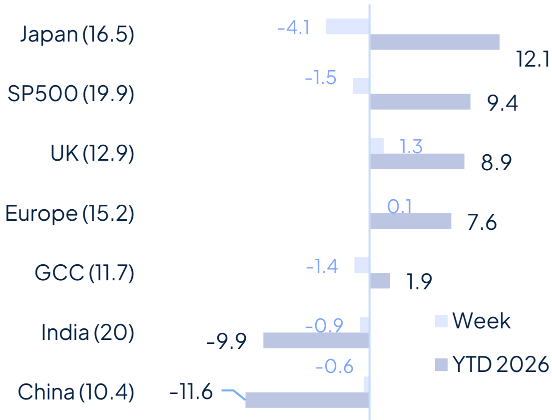
Elsewhere, the Hang Seng rose 1.6% on state fund purchases and record June exports, extending the rotation out of Korean chipmakers; Korea (shut Friday) was left down 9%, causing the EM index to slip into correction. Banks delivered on their raised estimates, beats outpacing misses 11-0 and JPMorgan's $6.0bn of equities trading revenue crushing the $4.0bn consensus, leaving Financials among the few sectors in the green. The 'Goldilocks' macro setup was simply ignored: June CPI fell 0.4% on the month, the first decline in six years, with core flat, yet inflation expectations dropped so sharply that real rates ended at highs for the year. The VIX rose 25% to 18.8 on the back of regional developments.

The escalation has again followed into Monday: Brent rose as much as 3.8% to $91.42, the Kospi caught down 3.7% with Samsung and SK Hynix off 5% early, while US futures steadied and Alibaba added 5.6% on its Qwen3.8 Max preview. Wednesday night will be important, with Alphabet and Tesla earnings headlining the heaviest week of the season; Texas Instruments Tuesday and Intel Thursday completing the chip read. TSMC has already confirmed the demand, but was sold for its spend, so assume the same asymmetry applies: capex commentary will matter more than the print, and for a market still priced for near-record results, misses will be punished harder than beats are rewarded, again. The macro calendar is light; the ECB should hold Thursday with a hike priced in by oil later in the year, flash PMIs land Friday, and the Fed is in blackout into its late-July meeting with roughly two hikes priced by early 2027. The Middle East remains the swing factor, where a shift in either direction overrides everything else.

Equity Recommended Regional Positioning

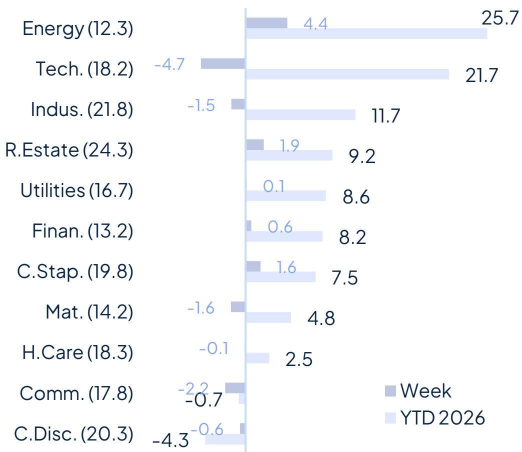



Major Indices Performance (TR, US$), P/E in brackets




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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