Rising concerns, quiet markets

- **Last week saw questions on debt sustainability and another breaking announcement on tariffs**
- **The dollar and gold took note, though there was no massive reaction from other asset classes**
- **The summer ahead could be hot, between expiring tariff deadlines and potential macro headwinds**

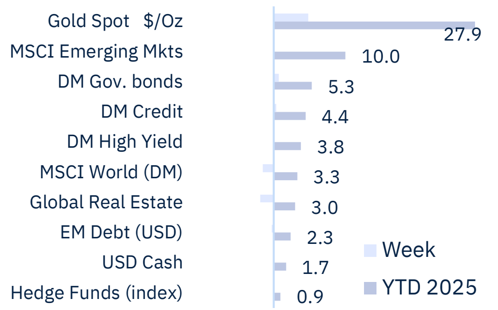
Global markets failed to deliver a third positive week for risk assets, though there was no particular drama either. Growing concerns on US debt sustainability fuelled by political uncertainty took a toll on the dollar and triggered a rebound in gold. This was all but amplified by President Trump's threat of a 50% tariff rate on imports from the European Union on Friday, which also added to caution on risk assets. Still, looking at weekly numbers, there was no sign of panic with global stocks retreating only modestly.

The week also revealed May flash PMIs for most regions. The big picture is consistently tepid for Europe and Japan, still doing ok for China, but was better than expected for the US for both manufacturing and services, lifting the composite index to a very healthy 52.1, much better than the median consensus forecast of 50.3. This wasn't enough to support US stocks and the dollar, but it continued to pressure implied expectations for monetary policy, with futures pricing in only 2 cuts in 2025.

As we write, the White House announced an extension of the deadline to negotiate with the EU to July 9th, in another typical "Art of the Deal" fashion. This is good news of course, but it also confirms that the coming summer will be eventful. First, suspension of most of the "reciprocal" tariffs will expire, and seeing them replaced with stable trade agreements is not a given. Second, while the first two quarters should be reasonably good for global activity, the second half is riskier. Consumers may be less buoyant, businesses have moderated their investments and hirings, and the "frontloaded" boost to US imports will unwind. Our view is that we could see a slowdown in activity before inflation rises, which suggests that the Fed will start cutting.

Our three profiles are up around 5% so far in 2025 and our positioning remains modestly defensive. The new week starts with a holiday in the US and some European countries and should be quiet in terms of data apart from the US PCE report.

Asset Classes USD % total. Return, Week and YTD 2025



MAURICE GRAVIER
CGroup Chief Investment Officer
MauriceG@EmiratesNBD.com

GIORGIO BORELLI
Head of Asset Allocation
GiorgioB@EmitatesNBD.com

SATYAJIT SINGH, CFA
Head of Fixed Income Strategy
SatyajitSI@EmiratesNBD.com

NAWAF ALNAQBI
Head of Equity Strategy
NawafALNA@EmiratesNBD.com

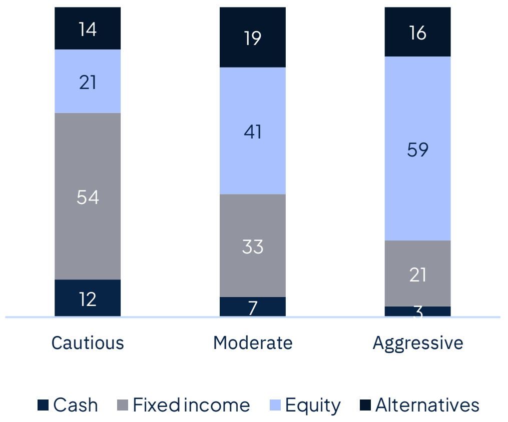
Cross-asset Update

Fiscal issues were at the forefront of investor's minds last week, and rightly so. A mix of negative factors pushed sovereign yields higher across the developed markets, putting rising inflationary risks in the spotlight. In its own right the downgrade of the US debt by Moody's the previous Friday was not a major event, yet it constituted a warning that heightened focus on the House approval of Trump's tax cut bill that followed on Thursday. The "big beautiful bill" should see its final approval by Congress in Summer further adding to the US debt burden. The disorderly rise in global yields was 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.

As for DM-country debt sustainability, there is a long-term outlook, that is very much different from the shorter-term one. 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, on top of the weakening of the currency. Commodities in general, currently being led by gold, would in the end be in a great bull market, with equities 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. This would be further enhancing 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 sensing despite the outlook for tariffs that are there to stay.

The US dollar is the primary victim of the Treasury's growing debt burden. It has been sliding year-to-date despite the prospect for delayed rate cuts and improving economic surprises. And Trump's stop-and-go approach to tariffs further erodes the trust in the dollar system itself, that after all plays to the Washington's administration advantage by making US goods more competitive. Ultimately, it will not play out well for the US dollar, nor for US assets in general in a stagflationary scenario. But for now, it is still a bull run tariffs notwithstanding.

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		=	

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Fixed Income Update

There was a global bond selloff last week driven by fiscal deficit concerns across the developed markets. The US, UK and Japanese government bonds were the worst affected. The sell-off gathered pace on Wednesday after a surprise in the UK CPI driven by services inflation. The Headline and Core CPI numbers came in above estimates at 3.5% and 3.8% respectively. Services inflation climbed to 5.4%. It accelerated after the tepid 20-year US notes auction. US 30-year yields, leading losses on the day, pushed higher and reached as high as 5.09%, the cheapest since October 2023. The Republican tax cut bill was passed by the House by a narrow margin on Thursday. The bill includes a $4 trillion increase in the US debt ceiling, which the Treasury Department forecasts could otherwise force a default as soon as August or September, adding urgency to the timeline.

The US manufacturing index showed expansion at 52.3, compared to the 49.9 estimate. Input prices for the composite measure rose to the highest since Nov. 2022. On the contrary, Private-sector activity in the euro area unexpectedly shrank in May as services recorded their worst performance in 16 months. The composite PMI dipped below 50 to 49.5. The market is pricing around two rate cuts for both the US and Europe. We believe ECB has more leeway to be dovish than the Fed. We continue to like long-duration exposure in the German government bonds.

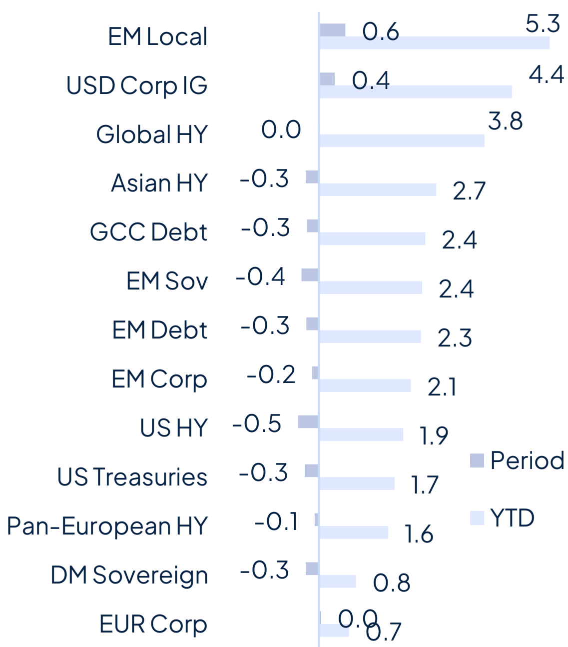
Hawkish Fedspeak continued as John Williams suggested policymakers may not be ready to cut rates before September amid a murky economic outlook. Raphael Bostic also signaled an unwillingness to ease for some time. Fed Vice Chair Philip Jefferson also emphasized a wait-and-see approach at the Atlanta Fed's 2025 Financial Markets Conference. Fed Governor Christopher Waller said the central bank could cut interest rates in the second half of 2025 if the Trump administration's tariffs on US trading partners settle around 10%. In a landmark decision, the US Supreme court ruled that the Federal Reserve is a "uniquely structured, quasi-private entity" and its decision supporting the administration to fire other independent agency chairpersons won't apply to the Fed, shielding Jerome Powell from being fired by Donald Trump.

Today, Sharjah Islamic Bank announced a mandate for a new NC 6 AT1 $ sukuk. The proceeds will be used to refinance its AT1 sukuk, with a call date in July. For comparison, DIB's perpetual sukuk is currently trading around 5.55%, while ADIB's AT1 sukuk is trading around 5.70%. SIB is rated one notch below DIB and two notches below ADIB. The government of Sharjah owns more than 37% of the bank. SIB is well capitalized with CET1 and CAR at 11.32% and 15.76%. In FY24, the bank reported total operating income of $591 Mn (+21% YoY), and NI of $285 m (+24% YoY). As of March 2025, the bank's total assets, deposits and financing amounted to $22.5 Bn (+18% YoY), $14.2 bn (+16% YoY) and $11.4 bn (+20% YoY), with 77.4% financing to deposits ratio.

Fixed Income Key Convictions (2025)

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)



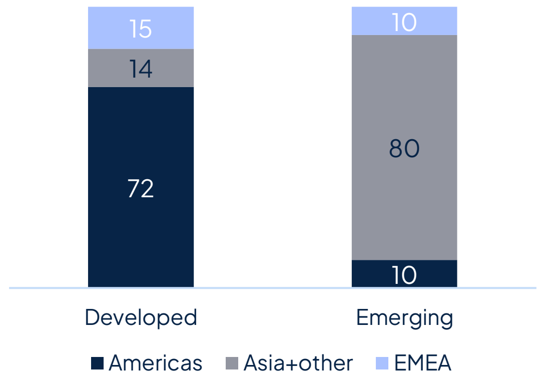
Equity Update

Global equities pulled back last week as risk appetite cooled and markets reassessed stretched valuations against a backdrop of policy uncertainty. The MSCI ACWI fell 1.4%. Developed markets declined 1.5%, weighed down by renewed trade tensions and softer earnings reactions. Emerging markets were more resilient, dipping just 0.1%, helped by strength in China. The S&P 500 led losses across major indices, dropping 2.6% for its worst week since early April. U.S. equities came under pressure as megacap tech lost steam and corporate commentary turned more cautious. Nvidia traded sideways ahead of earnings. Workday dropped 13% after providing a muted outlook, even as it met expectations. The focus has shifted from beating numbers to providing forward clarity. The tone in U.S. markets changed midweek following President Trump's renewed push for tariffs. A proposed 50% levy on EU imports and fresh pressure on Apple to localize production rattled sentiment. Apple is down more than 7% last week. While earnings season has broadly delivered, the policy pivot drove a sharp rotation away from globally exposed sectors and highlighted the fragility in sentiment. So far, 96% of S&P 500 companies have reported Q1 results, with 78% beating EPS estimates. That beat rate exceeds both five- and ten-year averages, yet markets are reacting more to guidance than to headline prints. Europe held up better by comparison. The MSCI Europe Index declined 0.5%, as solid earnings helped cushion the tariff-related pullback. First-quarter results came in ahead of expectations, with improving margins and top-line resilience across key sectors. Strategists have revised profit forecasts higher for 2025 and 2026. Automakers, semiconductors, and luxury names bore the brunt of trade fears, while domestically focused sectors proved more stable. Companies that maintained guidance were rewarded, but any sign of caution was met with repricing.

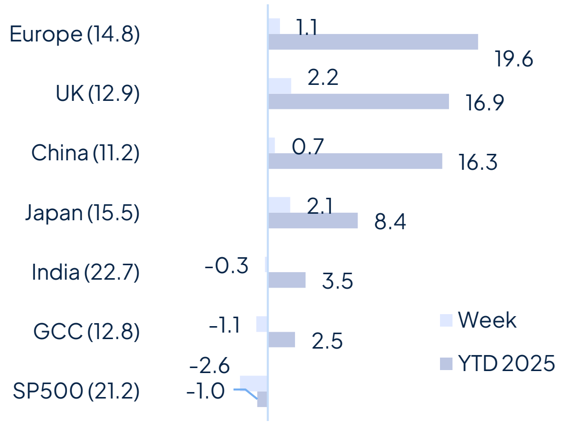
China saw modest upside. The MSCI China Index rose 0.9%, supported by the PBOC's rate cut and a revival in equity issuance. IPOs from CATL and Hengrui priced strongly in Hong Kong, narrowing the valuation gap between offshore and onshore listings. Alibaba and JD advanced early in the week on stimulus hopes, though Baidu slipped after delivering weaker ad revenue. Policy support and capital markets activity are beginning to stabilize sentiment, even as earnings remain uneven. Japan was little changed. The TOPIX edged 0.2% lower, with exporters supported by better U.S. economic data and signs of steady progress in trade discussions with Washington. Large-cap industrials and electronics saw modest gains, helping offset broader caution into the weekend. In India, the MSCI India Index dipped 0.6% as rich valuations and slowing foreign inflows triggered some consolidation after a strong run. Flows remain net positive, but the pace has moderated.

Equity markets are shifting gears. Earnings have held up, but the path forward now depends more on policy signals, sector rotation, and clarity around margins. This is not yet a retreat, but a reset. The tone is less euphoric, more selective. Momentum is no longer carrying the tape alone.

Equity Recommended Regional Positioning

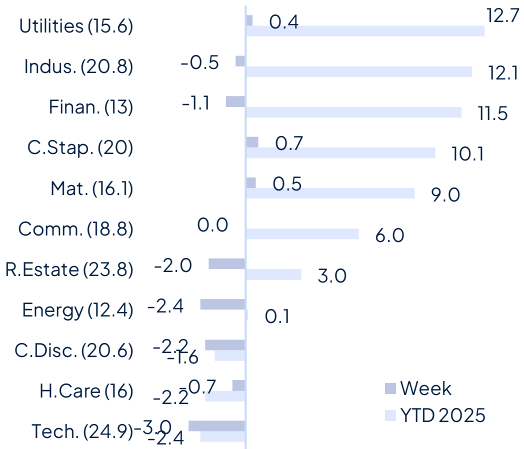


Major Indices Performance (TR, US$), P/E in brackets



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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