THE MONTHLY LETTER

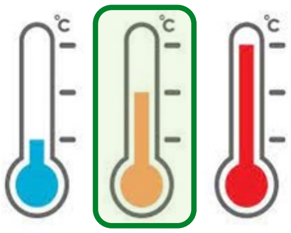
Tactical update

MAY 2025

In truth…

Global landscape

Inflation in Next 6m



Stance: above central banks targets (ex-China)
Trend: one-off ST shock first

Economic growth in Next 6m

Stance: below LT potential
Trend: weak

The long-term macroeconomic regime is characterized by irregular and volatile economic cycles

The following factors will negatively impact potential growth: Weakness in the main structural factors (demographics, excessive debt and productivity), Asymmetric risks of deflation or inflation, The uncertain pace of adoption of AI - Issues of deficit financing and debt reduction

Cyclical outlook. Global reflation under attack

Trade war has become a real threat. The ultimate shape of US economic policies will establish the framework for a more uncertain S2. EU and China are expected to enter a new regime of fiscal dominance

Geopolitics. The die has been cast

The new US administration is making bold changes. The likelihood of unexpected events has increased. There is a higher chance of de-escalation in the Ukraine/Middle East conflicts, but implications are unclear

Global liquidity momentum will gradually wane

Liquidity deceleration is underway. Watch for an ultimate - preventive - central banks' last hurrah

Negative equity-bond correlation still in place, for now

It is anticipated that US CPI volatility will resume as tariffs are passed on to consumers, potentially reaching the key 3% threshold. Japan remains a unique and sensitive case that requires close monitoring.

Highly volatile investors' sentiment and capital flows

Poor investors' sentiment is paving the way for a bottoming process for risky assets.

Global view

In the aftermath of big splashes

At the beginning of the first quarter, the sequence of new policy implementation by the Trump 2.0 administration was unclear. In a favourable and complacent scenario, debt reduction and deregulation would be aligned with, or even precede, more dangerous initiatives, particularly those relating to trade. The reality has proven to be a stark contrast to this optimistic outlook. The implementation of the economically challenging measures has commenced...

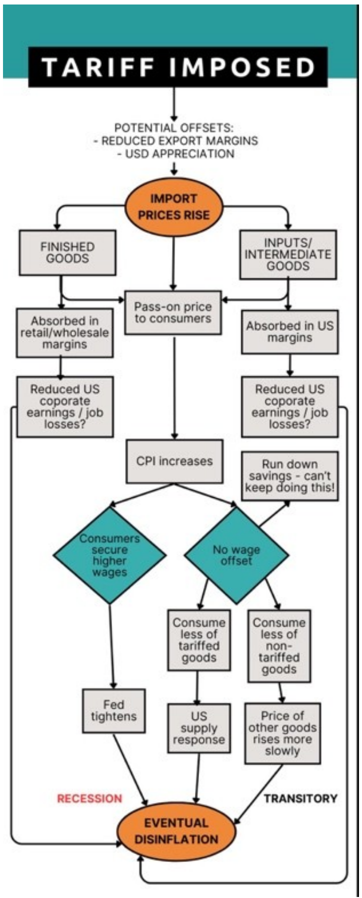
Despite the intention behind Donald Trump's 2025 customs policy being to protect US industry and rebalance trade, it has resulted in several issues, including price increases, economic uncertainty, international tensions, market volatility and the risk of a global slowdown. While some of the negotiating objectives appear to have been achieved, the economic and social cost of this strategy remains very high, both for the United States and for the rest of the world.

Trust in the US is damaged, erasing the perception of the United States exceptionalism

Recession and resurging inflation fears now dominate

The US Treasury Secretary is working hard to stabilise the capital markets and address early signs of capital flight

Ultimately, tariffs are disinflationary / deflationary



Global funding tensions are beginning to emerge

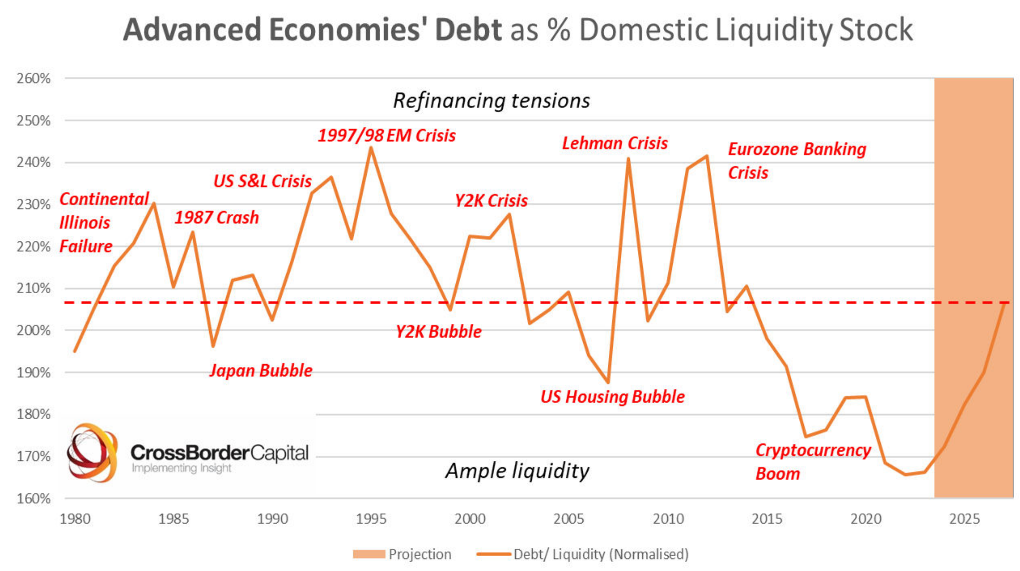
The emergence of Trump 2.0 and the EU renewed appetite for fiscal spending coincide with a specific phase of the long credit cycle. The post-covid termination of financial repression is marking the commencement of a new cycle for public and private debt. With the retreat of over-influential or omnipresent central banks, investors must relearn how to navigate the financial landscape. Interest rates are reverting to normal, the price of risk is regaining its value and debt, once commonplace, is once again a criterion for selection and judgement.

For public debt, the end of interest rate floors reveals the true burden of accumulated debt. Governments, long lulled by the illusion of free financing, are rediscovering budgetary constraints. Debt servicing is once again a major budget item, forcing painful trade-offs at a time when investment needs remain immense.

Private debt is proving to be a robust alternative to the reluctance of traditional banks and the volatility of listed markets. However, the meteoric rise of this market, which has tripled in the space of a decade, calls for humility and vigilance. It is an irrefutable fact that unbridled deregulation always leads to excess and breakdown.

Leveraging has been a highly successful strategy, leading to a significant increase in private equity until central banks began to raise rates in 2022. The challenges faced by major US universities in selling significant portions of their portfolios indicate a PE cycle peak and a growing demand for liquidity among prominent institutions.

Global refinancing cycle at the crossroads

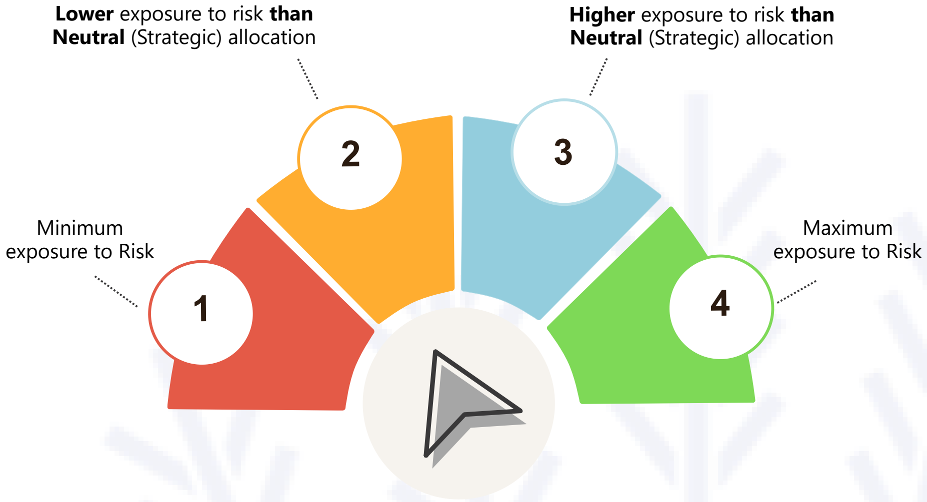


Upcoming macro volatility will coincide and reinforce that of the capital markets

Asset allocation recommendation

Hectic market adjustments were made in response to a decline in speculative behaviour. The initial shock and panic of over-indulgent investors is now being replaced, logically, by calculated prudence. It is now incumbent on central banks to assess macroeconomic and liquidity developments in the short term to adapt accordingly.

Global allocation - Risk budget



We are committed to maintaining the recently downgraded – to slightly cautious – approach to asset allocation and are actively repositioning sectors and countries.

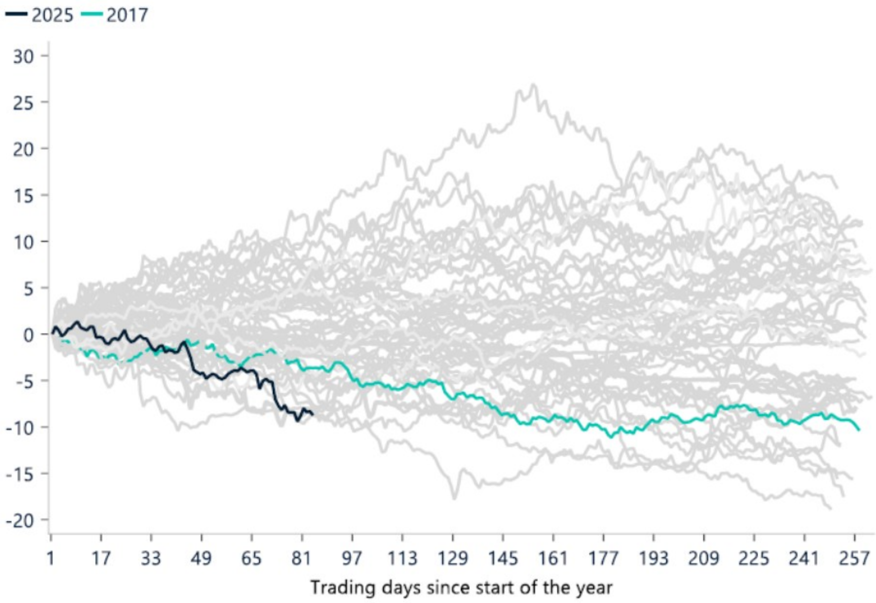
Devises

The concept of US exceptionalism is waning

The initial 100 days of the Trump administration have proven to be a turbulent period. April proved to be a month of significant change, with numerous U-turns and revisions to trade policy. It appears that the most unfavourable possible outcome regarding tariffs has been averted. Despite the 90-day reprieve, tariffs have returned to levels not witnessed since the early 1930s. Trump's desire for a weaker USD has been realised, but at a significant cost to the economy and markets.

The lack of clarity surrounding US trade policy has the effect of making the US economy less appealing as an investment destination. The USD index experienced a 5% decline in April, dipping below the 100 thresholds for the first time since 2022. It has experienced a decline of over 8% this year, marking its third worst start in history. The years with the lowest growth were 1986, following the Plaza Accord, and 1973, after the collapse of the Bretton Woods system. We are currently experiencing a paradigm shift in the USD. The market is becoming increasingly focused on de-dollarization, with reduced reserves and disinvestment from heavily weighted US assets.
Recent market turbulence has led to questions regarding the conventional role of the USD as a reliable investment haven. Our view on the USD is more structural in nature

The 3rd worst start on record for the USD



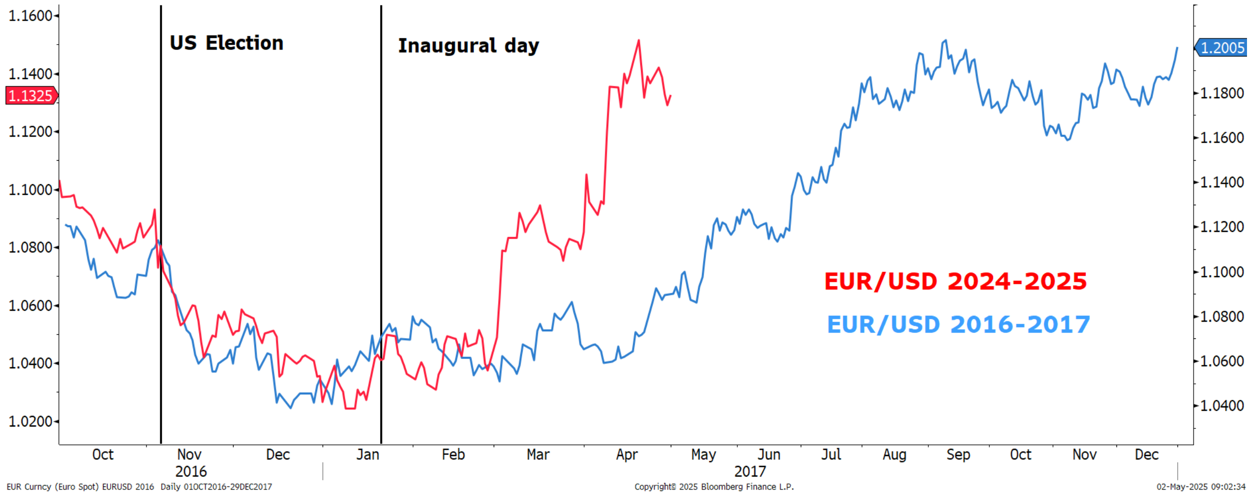
The USD has recently shown signs of stabilisation, largely due to President Trump's re-evaluation of key policy issues, including the independence of the Fed and trade matters. The fundamental issue remains unresolved. The challenges faced by the USD are primarily due to the loss of its status as a safe-haven asset, but not only. A key concern is the imminent risk of a significant economic slowdown in the US. Persistent pressure from dovish policymakers at the Fed is also a contributing factor. When the USD began to decline in January, positioning was significantly extended. The market began to capitulate in early March, and its subsequent decline has been accompanied by a sharp reduction in longs. This significant change makes the move highly significant, with the market now short USD for the first time since November.

A trading range and a consolidation around these levels will prevail until a clearer picture of the damage being done to the US economy emerges

Getting a bit ahead of itself

The EUR has performed well this year, given its status as the 2nd most traded currency. In April, it benefited from the USD weakness, despite the ECB rate cuts and warnings of economic risks. The EUR has outperformed its peers, except for the CHF. After reaching a high in April at 1.16, it has consolidated. The April move appears more fragile, based on the EUR deviation from yields spread and market concerns about US economic policy. These concerns may already be changing, as the US government suggests it could water down some tariff plans and Trump has indicated he has no plans to fire Fed Chair Powell.

The EUR/USD has rallied faster than it did



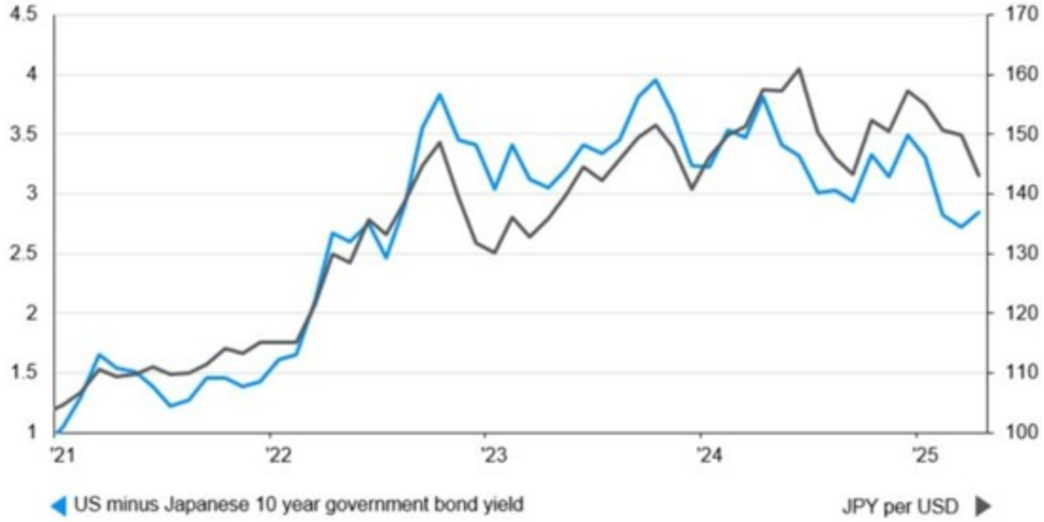
The EUR has rallied faster than expected. The present circumstances are more conducive to the EUR attracting safe-haven flows, particularly if a ceasefire occurs between Russia and Ukraine. The eurozone has a substantial current account surplus of over €400 billion over 12 months, or 2.5% of GDP. Germany's sovereign bond market is set to expand significantly more than previously expected following the announcement of a €1 trillion expansion in fiscal spending on infrastructure and defence.

The short-end yields spread indicates the euro is slightly overvalued. This supports our view that the euro will consolidate over the coming months.

A Bank of Japan in distress

The Bank of Japan (BoJ) maintained unchanged its policy rates at 0.5%, while simultaneously issuing a commentary that acknowledged the disinflationary impact of tariffs on countries like Japan, which are subject to such trade restrictions. Tariffs are likely to exert a direct inflationary pressure on US prices, but it is more challenging to forecast the net effect in Japan. If the BoJ were to focus solely on inflation, it would likely result in a more pronounced and accelerated easing of its monetary policy compared to the Fed. However, given that key rates stand at 0.5%, versus 4.5% in the US, the Fed has significantly more scope to cut rates than the BoJ. Should the Fed cut by more than the BoJ, then the yield differential would narrow, and the JPY would strengthen.

If the Fed cuts more than the BoJ, the JPY could strengthen



Source: LSEG Datastream, Data as of 30 April 2025.

The BoJ has revised its core CPI targets, setting a 2.2% target for 2025 and a 1.7% target for 2026, while acknowledging the potential for downside inflation risks. It also cut its 2025 GDP growth forecast to 0.5% from 1.1%, and its 2026 forecast to 0.7% from 1%, with economic risks also skewed to the downside. The yen weakened subsequent to the meeting. Despite Ueda's indication that rate hikes remain a possibility, the market has expressed a lack of confidence in him.

The JPY's primary risk is its current positioning, which appears to be highly concentrated. According to the CBOT, the speculative net long JPY/USD position is at a record high, suggesting limited scope for long JPY bets to be easily added to, with the JPY vulnerable to an unwinding of this position.
We turn neutral on the JPY, but we are closely monitoring its movement. If it decisively breaks the 140-support level, we will adjust our strategy accordingly

Bonds

An unclear framework

The upcoming FOMC meeting will see its Chair, Powell, take centre stage. The Fed is expected to maintain its key rate unchanged. This decision is likely to be met with criticism from President Trump, who has reiterated his call for Powell to cut rates. Previously, Trump stated that he would not be dismissing Powell, which has since restored calm to the US bond market. Any further remarks from Trump could lead to a resurgence of market volatility.

While public perception of tariffs is unfavourable, there is little in the hard data to suggest a significant economic slowdown. However, financial conditions have become marginally more restrictive as investors' sentiment towards USD-denominated assets weakens and uncertainty levels rise. The current market easing expectations (75bps for this year) reflect a lack of conviction regarding the policy path. Investors are uncertain whether the Fed will need to cut rates aggressively in response to a meaningful economic slowdown, or whether it will maintain current policy as inflation persists due to tariffs. In the eurozone, inflation data was slightly higher than expected, with a rise in core inflation from 2.4% to 2.7%. Notwithstanding, the increase was attributable to higher service inflation in relation to Easte. The issue should not be of significant concern. The ECB's wage tracker indicates a distinct downward trend in wage growth, which suggests the possibility of further ECB cuts.
We continue to favour European sovereign bond market over the US one

Supply/demand imbalances will shortly resurface

Recent market turbulence has brought to light a challenging reality. Uncertainty surrounding trade policy has led to questions regarding the extent of foreign demand for US Treasuries. Investors based outside the US hold a 30% of all outstanding Treasuries, though this figure has declined in recent years. Foreign investors are owning 45% of 7-10 year notes. One strategy to manage debt is to extend the maturity. A 100-year term provides a significant timeframe for repayment. However, Japan has refused such a swap, and if a close ally declines, it is likely that others will do the same. Investors are understandably reluctant to hold long-term illiquid bonds. Furthermore, Finance Minister Kato stated on TV that Japan, the largest foreign creditor to the US, could utilise Treasuries as a bargaining chip with Washington, if tariffs are imposed.

In 2023, around the debt ceiling increase, long-end yields increased

The more challenging period will be after the debt ceiling agreement. The US Treasury borrowing will resume. The US yields will suffer upward pressure

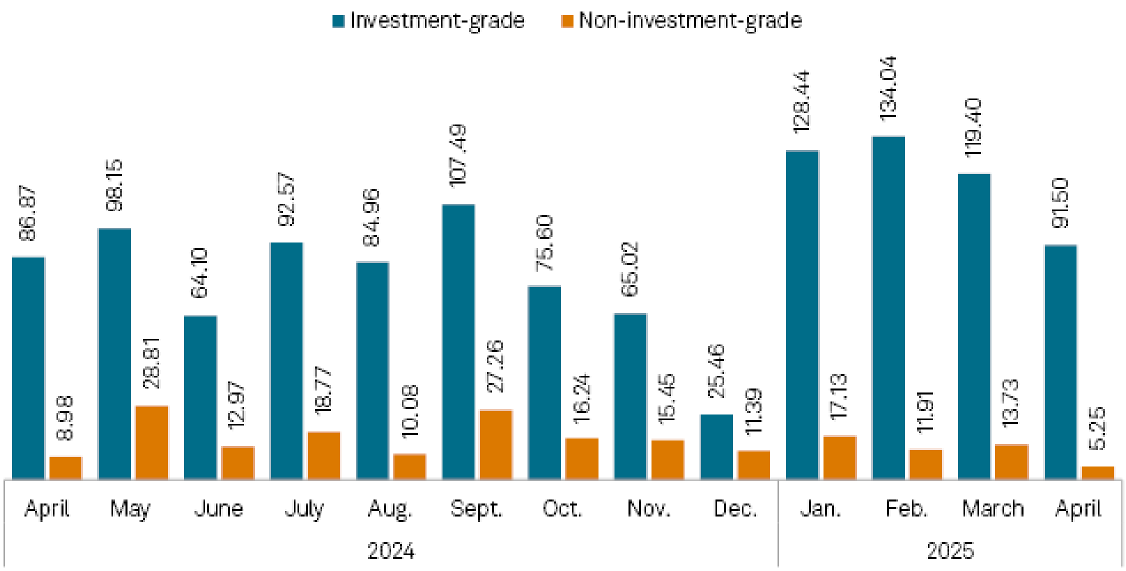
The US Treasury's announcement regarding its May refunding was anticipated. The US Treasury will primarily utilise its TGA until the debt ceiling limit is addressed by Congress. The net US issuance volume is expected to decline until July. Furthermore, the Fed is no longer reducing its US Treasury portfolio. This is positive news for bonds in the short term. Once the debt ceiling will be lifted and the US Treasury will resume borrowing, a more challenging period will ensure.
The US Treasury and US yields will face further challenges during summer period

Higher credit premium requested

Investors are requesting higher returns when it comes to investing in US IG corporate debt. As with equities, debt markets were rocked by President Trump's April 2nd announcement of global tariffs and subsequent decision April 9th to delay the tariffs' implementation by 90 days. The US IG spread climbed to a 17-month high at 102bps on April 7th from 82bps on April 2nd. The spread retreated since its recent high but it remains elevated compared to levels from earlier this year.

Recent years have seen strong demand for US IG bonds, as investors have been drawn to their elevated yields in the higher-for-longer interest rate environment. The recent spread widening appears to be a reflecting of investor desire for greater risk premiums rather than a bond selloff driven by weakening demand. The US IG companies in April have issued $91.5bn in bonds. While this volume is down from each of the last 3 months, when issuance surged and collectively reached a quarterly record, April's bond issuance has surpassed the monthly activity seen in 6 of the last 12 months and is up from April 2024. Of greater concern is the lack of appetite from investors for the HY segment. With $5.2bn, the US HY has experienced is lowest issuance volume in more than 3 years. This underscores the investor preference for quality over return.

US corporate debt issuances have significantly slowed



Since the early April spike, the US IG spread has decreased, settling at 89 bps in April as market panic subsided due to indications that the US has been pursuing international trade deals, and that Trump would not attempt to remove Powell yet. It is improbable that the spread will return to the historical lows of 65bps experienced in late 2024/early 2025, as concerns regarding tariffs are likely to persist. The 2 major macro-related risks, inflation and growth, have resulted in a shift in the range of spreads.

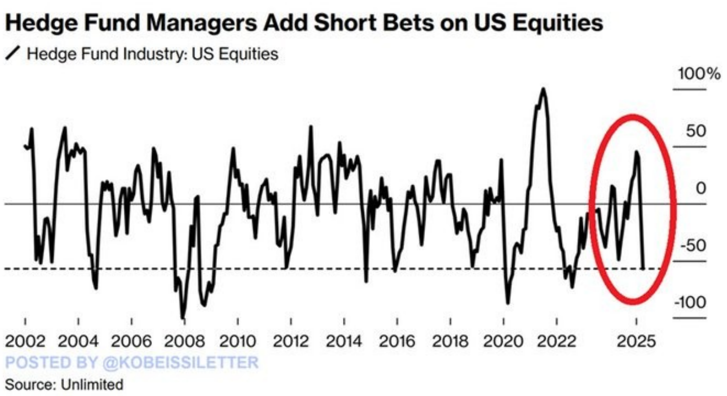
In the absence of greater clarity on Trump's policy agenda, the risk will persist in the financial system. It is also worth noting that institutional investors have already accumulated a significant amount of cash. The objective is to reinvest at a wider spread level. In addition, the sustained high yield of government bonds continues to underpin the elevated corporate bond yields that have contributed to the sustained demand for corporate bonds.
The balance of risks has partially rebalanced. We still favour IG over HY

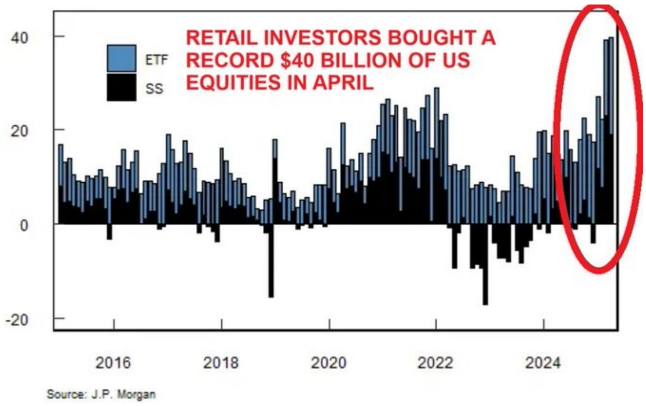
Equities

Technical, cyclical, or no recession? The first scenario would not call the bull market into question, the second would lead to a bear market, and the third would be "business as usual."

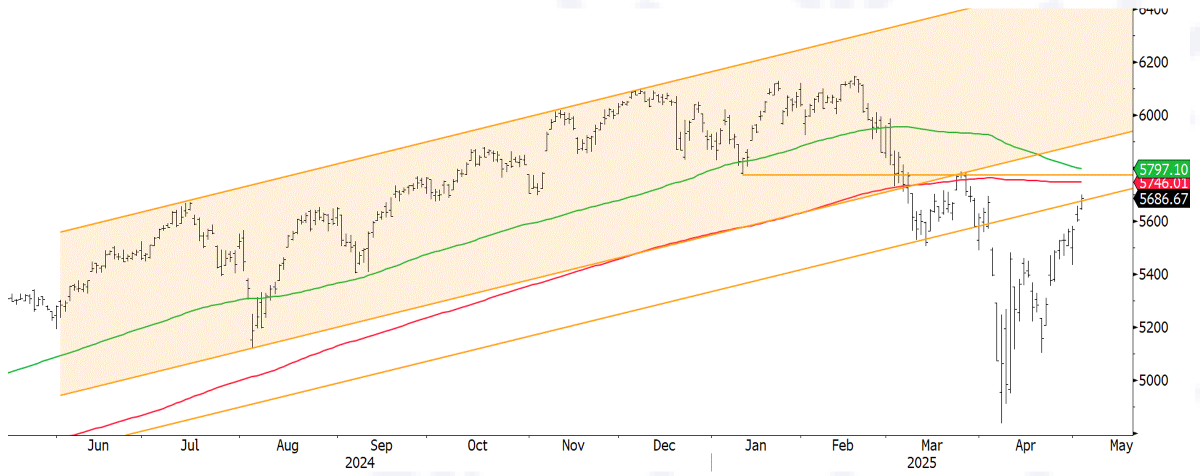
Trump's brutal trade war could push the United States and the rest of the world into a recession. The S&P 500 had signaled this risk on April 7 with a rapid (intraday) entry into a bear market. However, Donald Trump's announcement, forced by rising pressure on the US debt, of a pause in his tariff war, while maintaining 10% tariffs for the entire planet and 25% on steel, aluminum, and automobiles, as well as 145% on Chinese products, led to a powerful stock market rally, between 16% and 18% (intraday) depending on the index, and 24% for the Nasdaq and the Magnificent Seven. The stock market correction between February and March, followed by a strong rebound in April, continues to validate the upward trend. Individual investors have been the driving force behind this rally. We are in a fight between Wall Street vs. Main Street and hard data vs. soft data.

Individual investors bought a record $40 billion of US stocks in April, while hedge funds increased their bearish bets





Technically, the S&P 500 is 1.5% away from a significant resistance at 5,773, consisting of an inverted head and shoulders pattern and the 100-day (green) and 200-day (red) moving averages. The index has already reentered a minor upward trend. The reentry level into the major upward trend is around 5,950.



Polls show that a majority of Americans - financiers, economists, households, and businesses - believe in a recession in the second half of 2025. The US Chamber of Commerce (SME) is calling for a complete lifting of tariffs for them. The first 100 days are crucial for a president. Unfortunately, polls for Donald Trump are the worst in 70 years for a US president during his first 100 days in office. Especially on the economic front.

Tactically, due to more favorable technical considerations and the enthusiasm of individual investors, we have raised our stance to slightly positive. We will monitor whether the soft data, which signal an economic slowdown, will be transmitted to the hard data.

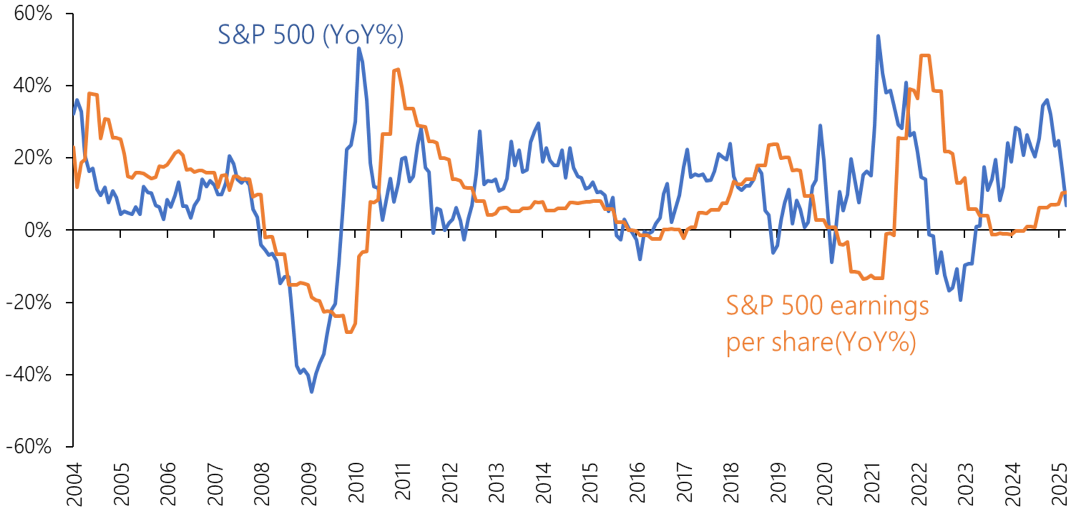
The positive points:

- The peak of the tariff war was probably reached in early April. The world has decided not to respond immediately to the Donald Trump’s attacks, unlike China, but to come and discuss to find out what the United States wants. It is clear that, of the 80 countries concerned, about fifteen are currently negotiating, including Japan, India, South Korea, and... Switzerland. China will consider the possibility of discussions with the US, meaning they are obviously already negotiating.
- S&P 500 companies' first-quarter earnings are solid, up 13% compared to the 7% estimated just a month ago.
- The United States and Ukraine signed a minerals agreement with an economic guarantee for Ukraine's reconstruction and an implicit territorial guarantee. This is a fairer agreement, but it remains binding for Ukraine, as Ukraine will have to ask the United States if they accept non-US partners (European, for example) in the minerals, oil, and gas sectors. This is not necessarily good news for Europe, and it may complicate Ukraine's entry into the European Union.
- The larger-than-expected decline in US GDP of -0.3% for Q1 25 could confirm a technical recession, but it is explained by a very sharp increase in imports in March in anticipation of the tariff increase in April. Job creation was solid in April, once again demonstrating the resilience of the economy. The Atlanta Fed's GDPNow model estimates a rebound in US GDP in Q2 25 of 2.4%.
- Deregulation and tax cuts. This week, Donald Trump will present his 2026 budget to Congress, with spending cuts and tax cuts. He will propose an increase in military spending beyond $1 trillion and a reduction in spending of more than $160 billion related to the environment, renewable energy, education, and foreign aid programs.
- The "Buffet Indicator," a ratio of market capitalization to GDP, indicates an attractive valuation for stocks.

The negatives:

- Analysts are reducing their earnings growth estimates, and many companies are suspending their forecasts in the face of uncertainty. For Q2 25, analysts reduced the S&P 500's earnings growth from +9.1% to +5.7%. Amazon and Apple warned that the negative impacts of the trade war were beginning to be felt.
- At 44, the US ISM Manufacturing Production is at its lowest level since 2020, 2008, 2000, and 1990, each of which was a recession.
- Historically, the return of the 10-year-2-year yield curve to a positive steepening precedes a recession. Considered more sensitive, the 10-year-3-month curve is very slightly inverted, which would lead us to be less concerned about an upcoming recession.

As in previous periods, the S&P 500 seems to have anticipated (in whole or in part?) weaker growth or the decline in profits



We underweight US equities in the absence of support from the Biden plans and AI, which had driven US outperformance in 2023 and 2024. With Chinese AI and the DeepSeek shock, the Magnificent Seven will no longer outperform as a group. Downward earnings revisions will be more significant in the US than in Europe and Japan.

We overweight European equities. Faced with the war in Ukraine and the loss of reliability of its historic American ally, Europe is moving in the right direction, but still at its own pace, meaning, slowly. Three ideas should boost its growth: 1) an €800 billion defense spending plan, 2) a €500 billion German plan, with the abandonment of the debt brake, dedicated to infrastructure, transport, defense, and the energy transition, and 3) administrative simplification and deregulation. Points 1 and 2 will result in the creation of a vast military industrial complex. Germany is pushing in this direction by demanding that military spending be excluded from community rules. We are truly in a new world! The Swedish SIPRI institute shows that in 2024, Europe was the main contributor to the increase in overall military spending (+9.4%) with +17%; this trend will continue in the coming years. The enthusiasm for the European defense sector has propelled valuations to high levels, but we remain very positive, as PERs are in line with growth rates over the next three years, and this reinvestment process is only just beginning. Led by Germany, the EU wants to reduce administrative burdens and ease regulation. In February, the European Commission submitted proposals to simplify rules for citizens and businesses. Great Britain also has a deregulation plan to eliminate red tape and administrative burdens for businesses. The current period presents an opportunity for Europe to accelerate its economic growth.

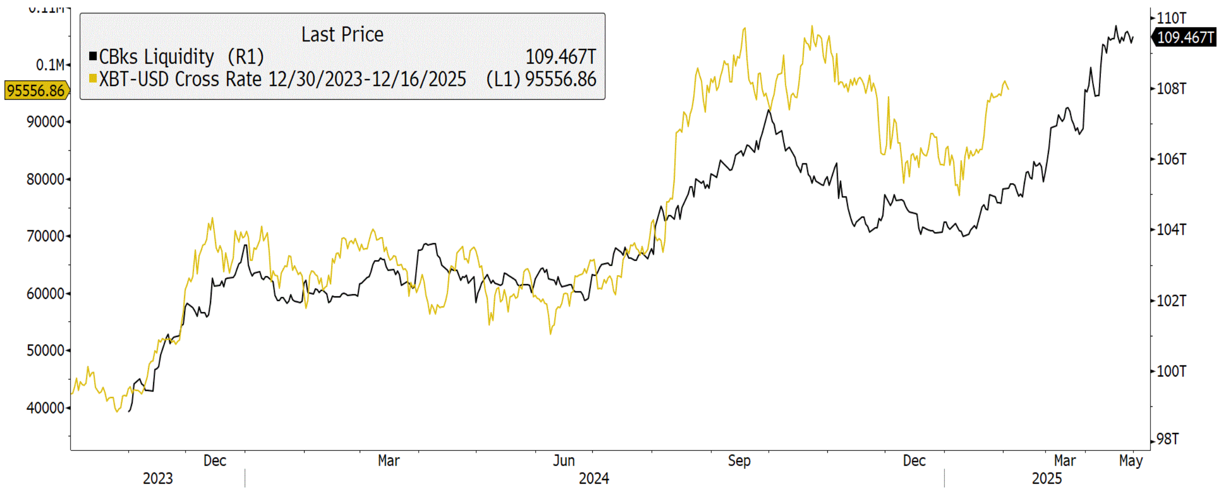
Faced with the uncertainty surrounding its exports to the United States, China will seek other, more reliable outlets for its production. In Asia, Europe, Latin America, or Africa? Donald Trump is seeking to make the United States a producer country. At the expense of consumption? Ultimately, this could be good news for emerging Asian countries in terms of domestic consumption, as well as stock market performance. In terms of sectors, we favor European financial stocks, European industry and more specifically European defense, consumer staples (a defensive sector little affected by the trade war), and electricity producers (strong growth in demand thanks to AI and the electrification of vehicles). We remain neutral on the pharmaceutical sector, as we do not yet know what Donald Trump's drug pricing policy will be; the United States is a major market for the pharmaceutical industry.

Alternative investments

Gold and Bitcoin are two powerful instruments to protect against a sovereign debt crisis and a Mar-a-Lago shock

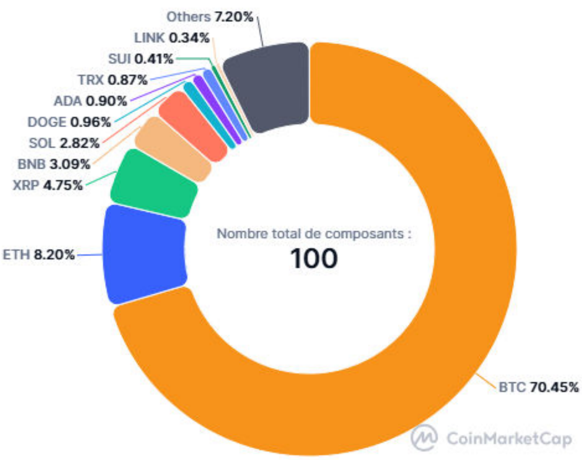
A new world order. A Mar-a-Lago Accord to restructure global financial flows, reduce US debt, and depress the dollar would be highly favorable for both gold and bitcoin. The dollar would remain a global reserve currency but would be used as an "economic weapon," while cryptocurrencies could play a role as a store of value under this potentially disruptive plan. Gold is in a structural uptrend and reached an all-time high of $3,510 on April 20. It is currently consolidating to exit an overbought zone. Profit-taking is also being observed among Chinese investors, although they have been a major contributor to inflows into ETFs invested in physical gold. Central banks and individual investors are active. Saudi Arabia was a significant buyer in 1Q25. A decline towards $3,000-3,100 cannot be ruled out, which would be a buying opportunity. The recent weaknesses in gold and BTC are due to the appreciation of the dollar, which passed from 1.1570 against the euro on April 21 to below 1.13 today.

BTC/USD und M2 global

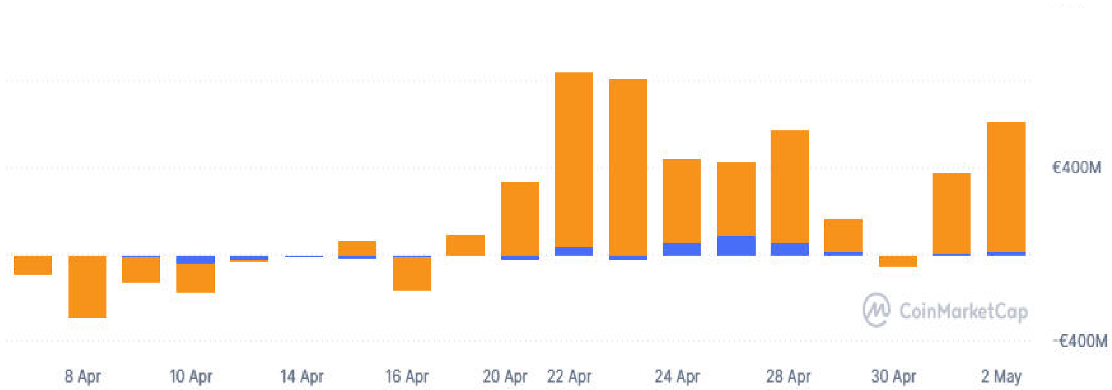


Following Donald Trump's executive order on digital assets, a draft regulation is expected to be published soon, which will shed light on the feasibility of a US strategic reserve of BTC.

Market capitalization by cryptocurrency



Crypto ETF net flows. A good April



We anticipate a return of BTC to its all-time highs of $110,000. And higher if we refer to the Stock-to-Flow model. The chart below shows a breakout of a resistance level.

Industrial metals are holding up very well. Copper is heavily influenced by Donald Trump's tariff war. Outside the United States, inventories have never been lower, particularly in China. US demand is very strong: traders are accumulating copper and other industrial metals in anticipation of higher tariffs, which is drying up supply in the rest of the world. At this rate, copper inventories in China could disappear and no longer be able to meet domestic demand. This could potentially be one of the largest tightening shocks this market has ever experienced. This situation is causing a significant price gap between London and New York. The risk of a decline in international prices is limited if US traders release their inventories, as China would be the counterparty at that time. We are neutral/positive on industrial metals, which are a key factor in the current trade and geopolitical war.

Oil prices are falling due to non-OPEC overproduction, weaker-than-expected demand, and the Trump administration's pro-fossil fuel policy. Donald Trump has announced he will ease drilling requests. Saudi Arabia is expected to increase production by 400,000 barrels/day starting in June and has signaled it can live with low prices. Its 2025 fiscal deficit is expected to be 2.3% of GDP, and likely higher if oil prices continue to fall. The ambitions of the Neom mega-city project have been significantly scaled back. Saudi Arabia needs Brent crude prices at $100 to balance its budget. A break of the $59 support would take us towards the $40-50 range. We remain cautious on the oil sector and favor companies in gas production and transportation.