EDMOND DE ROTHSCHILD

EDMOND DE ROTHSCHILD ASSET MANAGEMENT MARKET FLASH: THE MARKETS ARE FLYING BLIND

- **Despite contradictory announcements from the Trump administration, markets reacted positively to the temporary tariff exemptions on Chinese technology imports and progress in trade talks with Japan.**
- **The Fed is taking a wait-and-see approach to avoid inflation expectations becoming unhinged, as the economic outlook worsens, despite solid US retail sales due to pre-tariff advance purchases.**
- **The ECB is benefiting from the euro's appreciation, which gives it room for manoeuvre to ease monetary policy without worrying about the Fed's immobility.**

Investors battled with contradictory announcements from the Trump administration but still chose to focus on positive signals from Washington on the trade war front. Donald Trump announced that Chinese tech product imports would be temporarily exempt from 145% tariffs and be taxed at 20% in the meantime. He also said progress was being made in trade talks with Japan, raising hopes that any initial agreement would then lead to compromises with other trading partners.

Equity markets rallied on this more conciliatory tone and recovered almost half of the ground lost since April 2. The mood was enhanced after Treasury Secretary Scott Bessent said the tariffs announced on April 2 were maximum levels which successful trade talks with countries could bring down. He added that he was confident the Trump administration could reassure markets and avoid a recession. Even so, Washington is insisting on very demanding concessions. Europe, for example, is being asked to abandon its agricultural standards, increase drug prices and reduce VAT. And as part of Washington's strategy to isolate China, Asian countries are being encouraged to waive any economic partnerships with Beijing.

As he waits for better visibility on the actual policies Donald Trump will roll out, Jerome Powell reaffirmed the Fed's wait-and-see approach. The bank is apparently focused on stopping inflation expectations de-anchoring. The latest survey from the New York Fed once again highlighted this risk. The data showed that Americans' expectations for near-term inflation had risen significantly while the economic outlook was revised down sharply. However, US retail sales sent a more reassuring message although the figures were driven by anticipatory buying by households before tariffs came into force. Clearly, the impact from the trade war will take time to show up in economic data. Uncertainty is, however, already weighing on companies. Visibility has fallen sharply and order books are starting to thin out as figures from ASML showed. And some companies are on the trade war's front line: Nvidia is to book $5.5bn in asset writedowns as a result of the ban on exports of its H20 chips to China.

The risk for the Fed is evenly balanced between inflation and growth. The ECB, however, is confronted with deteriorating economic prospects which is why it decided to cut rates by 25bp to 2.25%. The move was facilitated by the euro's 4% rise over the last month to $1.137, so the ECB did not have to worry over much about the Fed staying put. As a result, European interest rates continued to stabilise after wiping out almost all of the surge in yields following Berlin's decision to go for a stimulus programme.

Elsewhere, the first estimate of China's GDP growth came in at 5.4%, or better than the 5.2% expected. The rise was underpinned by an increase in exports before tariffs came into effect but also by government stimulus programmes. Retail sales, for example, rose 5.9% after a 4% increase in the preceding month.

However, current Chinese resilience essentially reflects the past. China's economy is likely to be hit by the trade war with the US, especially as Beijing is Donald Trump's main target. This is why we took profits last week and turned neutral on China. We are also cautious overall on risk assets and government bonds. We prefer investment grade credit.

EUROPEAN EQUITIES

Markets rallied after reassuring macroeconomic news. Investors were encouraged by additional US import tariffs on tech products being suspended. They were also glad to see the Fed suggesting it could provide support. US and European markets recovered but the dollar remained under pressure against the euro. President Trump seemed to take a more conciliatory approach and said he was considering delaying tariffs on autos to give companies time to reshore production in the US.

The first quarter earnings season was in focus over the week. Luxury giant **LVMH** sold off after a sharp drop in sales, especially in the US, as economic uncertainty dampened consumer sentiment. Figures at **Hermès** reflected robust growth but slightly less than expected with weaker-than-expected contributions from the beauty and perfumes divisions. In contrast, **Brunello Cucinelli** showed resilience with a well-balanced 10% rise in first half sales. Elsewhere, **Waga Energy**'s 2024 results beat estimates. **Publicis** once again had a reassuringly strong first quarter and guidance for the first year was underpinned by strong sales momentum. First-quarter results at **BioMérieux** also beat expectations thanks to a sharp increase in revenues and strong growth in its molecular systems. But orders at **ASML** were below expectations and the news doused views on the tech sector.

US EQUITIES

Despite persistent volatility, Wall Street was stable over the period in question. The S&P 500 edged 0.2% higher, the Nasdaq slipped 0.5% and the Russell 2000 gained 1.8%.

The tech sector was in focus after the Trump administration rolled out new rules. AI chip producer **Nvidia** (-2.9%) said it would be booking a $5.5bn charge in the first quarter because of US restrictions on H20 chip exports to China. The stock tumbled 6% on the day. **Advanced Micro Devices** (-0.5%) is steeling itself for a $800m charge for the same reasons. In addition, Europe's **ASML** said its order book was less buoyant than usual and the group warned against the impact of customs barriers.

The Magnificent 7 had a mixed week: **Apple** gained 2%, while **Microsoft** fell 2.5% and **Amazon** ended the period 3.8% lower. **Netflix** jumped 4.4% as management eyed $1 trillion in market cap amid hopes to double its revenues by 2030. Social media giant **Meta** plunged 8% due to an antitrust court case.

In banks, **Goldman Sachs** (+1.9%) reported excellent first-quarter figures driven by strong equity trading. **Bank of America** and **Citigroup** gained 3.6 % and 1.8 % after they both maintained annual guidance. Increased consumer borrowing marked a contrast with a recent drop in consumer confidence levels.

In consumer discretionary, **General Motors** (+1.1%) and **Ford** (+2.9 %) gained on expectations auto sector tariffs might be suspended. Meanwhile, Beijing added to market tensions by ordering Chinese airlines to suspend deliveries from **Boeing** (-2.3%) and banning purchases of US aerospace equipment. Results at leading transportation and logistics company **JB Hunt** (-7.2%) were disappointing and management gave cautious guidance.

Despite the uncertainty, some sectors bucked the trend: energy gained 3.5%, healthcare 1% and materials 2.7%.

EMERGING MARKETS

The MSCI EM index had advanced by 1.37% in USD as of Thursday's close. Mexico, India, Brazil, Korea and China gained 5.39%, 3.61%, 0.78%, 0.47% and 0.21% respectively. Taiwan fell 1.45%.

China's first quarter GDP rose 5.4% YoY, or ahead of 5.2% expected. Exports jumped 12.4% YoY in March, or much more than the 4.6% expected, after factories rushed out shipments in anticipation of significantly higher US tariffs. Industrial production in March also grew 7.7% YoY, or ahead of the 5.9% expected. Retail sales rose 5.9% YoY in March, or better than the 4.3% expected. President Xi Jinping travelled to Vietnam, signing 45 deals covering areas including connectivity, AI, customs inspection and agricultural trade, as part of his broader SEA trip to make closer trade partnerships in the region. As mentioned before, the US government banned **Nvidia** H20 chip sales to China "for the indefinite future". E-commerce platform **JD** and **PDD** announced favorable plans for exporters impacted by tariffs to sell in the domestic market. **CATL** delivered another solid quarter, with profits beating expectations and robust orders despite US tariff challenges.

In **Taiwan**, **TSMC** reported an overall beat for the first quarter result. Net income was NT$ 361.6bn billion, up 60% YoY vs. estimates of NT$ 346.76bn. The company kept full year guidance little changed despite ongoing trade uncertainties. **Nvidia** will start to manufacture Blackwell chips in **TSMC** facilities in the USA.

In **Korea**, BOK held the key benchmark rate stable at 2.75%. The government unveiled a 12 trillion won supplementary budget plan to support its export-reliant economy, with a third of the total earmarked for dealing with trade risks and boosting AI capabilities. **Amorepacific** is accelerating its efforts to add more manufacturing capacity in the US.

In **India**, March headline CPI inflation declined to a 5.5-year low of 3.3% YoY (vs. consensus: 3.5% YoY, February: 3.6% YoY), driven by a 1pp decline in food inflation (3.5-year low) to 2.9% YoY. Exports for March grew 0.7% YoY vs. a decline of 10.9% in February. The tech ministry said smartphone shipments surged 54% in the fiscal year through March 2025, with **Apple** exporting more than $17.4bn-worth of iPhones in order to avoid the full damage of much higher reciprocal tariffs. **HDFC Bank** cut savings deposit rates by 25bp for the first time since 2020. **IndiGo** is planning to add more direct flights to Europe and Africa to capitalise on India's travel boom. **Wipro** reported a weak quarter with revenues missing consensus expectations by 80bp; management is now expecting 1.5% to 3.5% QoQ decline in revenue in the June quarter.

In **Mexico**, industrial production in February was 1.3% lower YoY vs. the 3.5% drop expected. **Vista Energy** acquired **Petronas**' 50% stake in an oil field in Argentina for about $1.5bn.

Banorte bought 44.28% of **Rappi Card Division** for $50m. **MercadoLibre** plans to add 28,000 workers across Latin America this year, a 33% YoY increase to 112,000 by the end of 2025

In **Brazil**, IBGE inflation for March came in at 5.48% YoY, or in line with expectations. Economic activity in February rose 4.1% YoY, or ahead of the 3.6% expected. The budget secretary said Brazil would reduce social spending by 50.8 billion reais in 2025-2029. **Carrefour Brasil** posted a 3.6% YoY increase in gross sales for the first quarter. Airline **Gol** postponed the deadline for investors to analyse proposals for $1.9 billion in financing. **Nissan** opened 400 new jobs in Brazil with a focus on exports.

In **Agentina**, IMF approved a 48-month Extended Fund Facility (EFF) arrangement totalling $20bn with an immediate disbursement of $12bn, or much higher than market expectations. The peso will now be allowed to float freely within a gradually expanding band between 1,000-1,400 pesos per dollar before the election. Markets cheered the news.

CORPORATE DEBT

CREDIT

Volatility fell and tension eased after Donald Trump's about turn on customs duties.

Lower volatility meant tighter spreads on credit markets. The Xover fell from 389bp on April 11 to 365 on April 17 and the Main narrowed from 77bp to 71bp.

Between April 11-16, cash indices rallied with investment grade returning 0.4% and high yield 0.75%. Corporate hybrids gained 0.53%. CoCos outperformed with a 0.96% gain.

The lull occurred during holidays in several countries so trading volumes were relatively light. The earnings season got off to a good start for banks. US banks reported satisfactory results thanks to trading desks. **Nordea** kicked off the season in Europe with upbeat results. **BNP Paribas** is due to report next week. Following the ECB's comments, the bank will no doubt be asked how it plans to account for the **AXA IM** acquisition.

In company news, the autos sector rebounded on the possibility of US import tariffs being delayed. The new issues market was on standby.

GLOSSARY

• Investment Grade: bonds rated as high quality by rating agencies.

• High Yield: corporate bonds with a higher default risk than investment grade bonds but which pay out higher coupons.

• Senior debt benefits from specific guarantees. Its repayment takes priority over other debts, known as subordinated debt.

• Debt is considered to be subordinated when its redemption depends on the earlier payment of other creditors. To offset the higher risk, subordinated Senior debt has priority over other debt instruments.

• Tier 2 / Tier 3 : subordinated debt segment.

• Duration: the average life of a bond discounted for all interest and capital flows.

• The spread is the difference between the actuarial rate of return on a bond and the rate of return on a risk-free loan with the same maturity.

• The so-called "Value" stocks are considered to be undervalued.

• EBITDA: Earnings before Interest, Taxes, Depreciation, and Amortization.

• Quantitative easing describes unorthodox monetary policy from a central bank in exceptional economic conditions.

• Stress Test: a process which simulates extreme but possible economic and financial conditions so as to assess any impact on banks and measure their resilience to these events.

• The PMI, for "Purchasing Manager's Index", is an indicator of the economic state of a sector.

• AT1s belong to a family of bank capital securities known as contingent convertibles or "Cocos". Convertible because they can be converted from bonds to shares (or depreciated entirely) and contingent because this conversion only occurs if certain conditions are met, such as the issuing bank's capital strength falling below a predetermined trigger level.

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17/04/2025

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Société anonyme governed by an executive board and a supervisory board with capital of 11.033.769 euros

AMF Registration number GP 04000015

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