EDMOND DE ROTHSCHILD

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MARKET FLASH: MARKETS HOLD FIRM AMID MIDDLE EAST TENSIONS AND US SLOWDOWN

- **Despite escalating tensions in the Middle East and recent statements from Donald Trump, investors remain broadly confident as long as the conflict does not spread and the Strait of Hormuz remains operational.**
- **The One Big Beautiful Bill Act continues to face hurdles in Congress. Meanwhile, May's economic indicators disappointed, with a decline in industrial production and weaker retail sales.**
- **Neither the Fed, the Bank of England, nor the Bank of Japan altered their monetary policy. All three adopted a cautious tone, suggesting that any potential rate cuts will depend on the evolution of trade and geopolitical tensions.**

The crisis in the Middle East worsened at the beginning of the week. However, as long as (i) the conflict does not spread, (ii) oil production is unaffected,(iii) the Strait of Hormuz remains open and (iv) the US stays out of the conflict, investor reactions tend to be muted. Markets are confident the conflict will remain circumscribed and they trust talks will begin. Even so, geopolitical tensions were the main driving force behind trading this week and shifts mirrored Donald Trump's statements. By suddenly leaving the G7 summit in Canada and calling on Tehran's population to evacuate, he sent both oil prices and equity market risk aversion higher.

In other news, talks continued in the US on the One Big Beautiful Bill Act. The Senate's finance commission suggested an amended version but with big changes that are not likely to get agreement. If the debates continue, the text might not be voted on before July 4. Elsewhere, retail sales slowed in May after several good months due to consumers anticipating tariffs. May industrial production also fell 0.2% when analysts were expecting a flat reading. The property market is also struggling: the NAHB Housing Market index fell more than expected while housing starts and permits tumbled 9.8% and 2%, respectively.

Several central banks held monetary policy meetings during the week. The Bank of Japan left rates unchanged and adopted a cautious tone. The most recent data revealed a slowdown in exports to the US. And there has still been no trade agreement between the two countries. The Bank of England also left its rates unchanged but raised hopes that the rate-cutting cycle might continue. And, as expected, the Fed stayed put. Jerome Powell said the FOMC would be patient in cutting rates and wanted to see what impact tariffs might have before moving.

Risk asset volatility edged higher over the week but remained limited. The dollar failed to act as a safe haven and traded within a narrow range. Only oil made real gains, returning to year highs. Government bond yields fell back a little. Traders are caught between a slowing economy and potential inflation from higher oil prices.

We are still cautious on equities given today's economic and geopolitical uncertainty, especially as valuations are once again demanding. In fixed income, we are neutral on duration and continue to prefer carry strategies.

EUROPEAN EQUITIES

Brent crude prices rose on Middle East tensions but market worries abated after Donald Trump mentioned possible talks with Tehran. Nevertheless, the possibility that the US might intervene militarily continued to weigh on oil prices. European equity indices edged higher at the end of the week on continued investor optimism over the US negotiating a solution to the Israel-Iran conflict. In addition, wage growth slowed in the eurozone, reducing labour market inflationary pressure and possibly weakening the price-wage loop. If so, inflation could stay close to the ECB's target.

In company news, **GTT** is to supply Samho Heavy Industries with a new LNG tanker but new order momentum has so far been limited this year. Despite less favourable trading, GTT is equipped to weather several quarters of lacklustre orders. **Airbus** raised its shareholder return objectives in line with its strategy and financial outlook. The group reaffirmed guidance on profitable growth over the next five years and reiterated its targets for this year. **Roche** is showing strong resilience faced with US tariffs thanks to local production and no risk of patent losses up to 2029. The group has boosted promising pipelines for Alzheimer, Parkinson's and obesity and also expects significant launches in the diagnostics field. **Kering** confirmed press reports that Renault CEO Luca de Meo had been appointed as its new CEO. This is a decisive move for Kering and reflects François Pinault's determination to accelerate change. The news initially lifted Kering's share price. **Pernod Ricard**'s concerns about momentum in the spirits market have led it to announce a restructuring to give the group more flexibility in tackling commercial challenges.

In M&A, **Saint-Gobain** has acquired Maturix, a Danish company which specialises in concrete temperature and strength monitoring. The deal will reinforce the French group's construction digital platform and allow clients to optimise operations and traceability.

US EQUITIES

In a holiday-shortened week for Juneteenth, the S&P fell 1%, the Nasdaq 0.6% and the Russell 2000 1.2%.

The dollar gained 1% against the euro. The Fed left its rates unchanged, recommending caution due to prevailing uncertainty over tariffs and conflicts.

Only energy (+1.8%) ended the period higher due to persistent tensions between Israel and Iran. But the rise was relatively tame compared to the 10% jump in Brent Crude to $77 a move that benefited oil majors **Exxon Mobil** (+3.2%) and **Chevron** (+2.2%).

Tech continued to ride on very heavy demand for AI applications. Open AI CEO Sam Altman said **Meta** (+0.4%) was offering up to $100m in signing bonuses to lure AI engineers. However, this tech investment race is affecting company costs. For example, **Microsoft** (+0.3%) is to make several thousand people redundant in the coming weeks. **Amazon** (-0.3%) is on the same trajectory as part of its AI integration drive and semiconductor giant **Intel** (+3.5%) is planning to lay off more than 10,000 people. Despite these massive redundancies, the outlook for tech stocks is still largely bullish due to growing demand.

The healthcare sector is suffering from tariffs and lower drug prices for US consumers. The sector lost another 2.6% over the week. Pharma giant **Eli Lilly** shed 3.3% despite acquiring **Verve Therapeutics**, a specialist in cardiovascular diseases, for $1bn. Uncertainty is accentuating the downtrend in the sector. **Johnson & Johnson** lost 3.8% and **Pfizer** 3.9%.

Construction sector consolidation in the US is fuelling M&A deals. Building materials distributor **Home Depot** (-4.4%) reportedly counterbid for **GMS** (building material stores) shortly after building equipment specialist **QXO** (+12%) offered $5bn.

Losing sectors were led by consumer staples,(-1.9%), utilities (-1.6%) and materials (-1.7%).

EMERGING MARKETS

The MSCI EM index was down 1.02% in USD this week as of Thursday. China, India, and Taiwan saw decreases, whereas Brazil increased.

In **China**, May retail sales rose 6.4% YoY, beating the forecast of 4.9% on an earlier 618 shopping festival pull-forward effect. Industrial production in May rose 5.8% YoY vs. estimates of 6% and fixed asset investment was up 3.7% YoY, or less than the 4% expected. Donald Trump extended the timeline for the third time for the sale of **TikTok**. The Lujiazui Forum concluded with the announcement of eight major financial opening-up measures, such as increases in the QDII cap, development of free trade offshore bonds and promotion of RMB FX futures. **JD.com** announced its expansion into the hospitality and tourism sector, and entry into the stablecoin race. **WuxiBiologic** announced a $280m placement. **Xiaomi** is set to unveil the price of its new YU7 later this month, with sales expected to start in July.

In **Taiwan,** May export orders jumped 18.5% YoY on robust AI demand, or slightly below expectations of 19.4%.

In **South Korea**, the export price index fell 2.4% YoY in May, while the import price index decreased by 5%. Korean internet names shone this week on policy tailwinds across AI, stablecoin, and digital content. President Jae-Myung Lee appointed Jung-Woo Ha, head of Naver AI, as senior secretary for AI and future strategy. Under the Digital Asset Basic Act, non-financial firms may issue won-based stablecoins backed by Korean treasury bonds. Inspired by the US precedents, the policy aims to expand sovereign bond demand and elevate the won's role in digital asset markets. **Alibaba Cloud** will launch a new AI data centre in Korea. **Hynix** secured Nvidia and Microsoft for its customized HBM chips. **Samsung** had its HBM3E chip qualified by Broadcom.

In **Thailand**, the second-largest party quit the ruling coalition, piling further pressure on the Prime Minister.

In **India**, the RBI issued its final guidelines on project financing, a relief on provision requirements **Reliance** is set to invest up to ₹8,000 crore to expand its beverage brands like **Campa Cola**, challenging Coca-Cola and PepsiCo. **Dassault Aviation** and Reliance Aerostructure will manufacture Falcon 2000 business jets in India, the first-ever assembly line for Falcon business executive jets outside France. **Whirlpool** is divesting a 31% stake in its Indian arm. **MakeMyTrip** is seeking to raise over $2bn through concurrent sales of shares and convertible bonds to buy back a stake held by **Trip.com**.

In **Brazil,** the central bank hiked the Selic rate by 25bp to 15%, when no rise was expected, and guided the end of the hiking cycle. Economic activity for the month of April rose 2.46% YoY vs. 2.35% expected. The government scrapped a long-standing tax exemption on cryptocurrency gains, imposing a 17.5% tax on all crypto profits for individuals.

In **Mexico**, Fiemex, the federal government's new Fibra E investment trust, raised $4.5bn in its debut on the Mexican Stock Exchange. **Amazon Mexico**, **INVEX** and **Mastercard** launched a No-Fee Digital Account.

CORPORATE DEBT

CREDIT

Credit markets stayed resilient during another week of geopolitical uncertainty in the Middle East. Investment grade edged 0.04% higher, widening by only 1bp, and high yield slipped 0.11%. Strong fund inflows continued to underpin the market as technical factors remained solid. The Xover widened by 15bp over the week, most of it (13bp) on Thursday amid rumours of a US intervention in Iran. The Main widened by 4bp.

In financials, **Sabadell** is mulling the sale of its British bank **TSB**. Several banks, including **Barclays** and **Santander UK**, are interested. **BBVA** said any sale of TSB would not affect the bank's bid on Sabadell. New issuance continued apace with thin issue premiums. **Bankinter**, for example, raised €500m with an AT1 at 6%. The order book hit €3.9bn. The CoCo index returned 0.09% in EUR over the week.

The high yield new issues market remained busy. Since the beginning of June, €13bn has been raised and new bond offerings have been easily absorbed, thanks mainly to strong inflows. Germany's **Benteler** (car parts, BB-) raised €600m at 7.25% due 2031. Italy's **Fibercop** (telecom infrastructure) raised €2.8bn in three tranches.

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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