



EDMOND DE ROTHSCHILD ASSET MANAGEMENT

MARKET FLASH: IS JEROME POWELL IN THE HOT SEAT?

- Donald Trump and the candidates to succeed Jerome Powell are arguing for an urgent rate cut by the Fed in response to the slowdown in activity and inflation.
- Powell's camp is urging the Fed to keep its current rates, as tariffs are expected to push inflation above 3% by the end of the year.
- In France, prime minister François Bayrou unveiled his proposed budget cuts. He hopes to reduce the government deficit to €43.5bn in 2026, but political consensus remains uncertain.

Rumours over a possible sacking of Jerome Powell disrupted markets this week. Looking beyond the pretext of poor management of the bank's renovation plans, the episode illustrated two radically opposed views on US inflation and growth. In the "rear-view mirror" camp, we find Donald Trump and candidates to succeed Jerome Powell as Fed chair. With inflation trending down towards 2%, they argue for an urgent rate cut to stop the economy slowing and the labour market worsening. The "windscreen" camp, including Powell-supporter Adriana Kugler who sits on the Fed's Board of Governors, encourages the bank to keep rates where they are as tariffs should push inflation above 3% by the end of 2025. The Fed was hoping for the trade war to have only a fleeting effect on inflation but Donald Trump's recent declarations -pushing back 200% tariffs on pharmaceuticals to 2026- could prolong the impact and cause long-term inflation expectations to de-anchor.

This week's data seem to suggest the Jerome Powell camp is right: weekly jobless claims, excluding seasonal effects, suggest the economy is at a cyclical high but proving resilient. Consumer spending is holding up: retail sales have rebounded strongly after a disappointing start to the year. The latest CPI reading revealed a significant rise in goods inflation, in particular in areas which are tariff sensitive like electronic products, even if overall inflation still looks to be under control thanks to shelter trends. Donald Trump was hoping that higher tariffs would be borne by exporters to the US but the fact that import prices have only fallen a little suggests that US companies are bearing most of the increases.

In France, prime minister François Bayrou unveiled his proposed budget cuts. He hopes to reduce the government deficit to €43.5bn in 2026 by (i) cutting government, social security and local authority spending, (ii) temporary measures like freezing tax scales and benefits or simply maintaining last year's budget, (iii) increasing the number of working days and (iv) structural reforms. Were this plan to be voted through, France could respect the budget trajectory agreed with Brussels to get the deficit down to less than 3% by 2029 while continuing to increase spending on defence, the only area not concerned by government retrenchment. The problem is that the political situation is even thornier than the budgetary equation so France's credit spreads with Germany have moved back up to 80bp.

We remain underweight equities, especially in the US. The earnings season may have got off to an encouraging start but we feel valuations are too complacent given the risk that trade talks might become more complicated. We are still neutral on fixed income but with a preference for corporate rather than government debt. We continue to be negative on the US dollar.

EUROPEAN EQUITIES

France's prime minister, François Bayrou, presented a deficit-cutting 2026 budget but the government's lack of a majority makes its adoption complicated. Tensions over Jerome Powell and the Fed's monetary stance weighed on equity markets. But they rebounded at the end of the period after Donald Trump denied he was planning to sack the Fed chair. The mood was also lifted by solid second-quarter results, especially among US banks, and the likelihood that Europe and India could reach a trade agreement with the US.

In company news, **AstraZeneca's** acquisition of **CINCOR** in 2023 looks like a winning bet after the group reported positive Phase III trials for Baxdrostat in hypertension. **Novartis** had a solid second quarter with an acceleration in growth drivers, and notably Kisqali. The group announced a new share buyback programme and also upped guidance on core operating profit growth so consensus expectations should be raised slightly. In autos, **Renault** issued a profit warning. Adjusted EBIT will be 13% lower than expected after a poor June due to Europe's depressed retail market and also tougher competition. The group revised its margin guidance for this year and cut industrial FCF forecasts. **Richemont** reported solid figures with strong jewellery sales offsetting slightly lower watch sales. Losses in China were counterbalanced by rising sales in South Korea and Australia while unexpected momentum in the US provided a contrast with lower sales in Japan. **ASML** had an excellent quarter but the stock sold off when the group said the macroeconomic picture meant its growth forecasts for 2026 were now uncertain. **Publicis** beat second quarter and like-for-like growth expectations, a big improvement on the first quarter, especially in North America. Investors, however, were not convinced and the stock fell sharply. **Virbac** had a robust first half with strong growth in Europe and Latin America but challenges in the Asia-Pacific zone. The company reaffirmed guidance on growth and its EBITDA margin despite difficult trading in Australia. The industrial sector jumped this week with **Legrand** and **ABB** leading gains on better-than-expected quarterly results. Strong new orders reflected sustained demand, especially for data centres.

In M&A, **Veolia** bought Ictec to boost its energy services division in North America. Ictec's software will help 40 clients optimise 200 MW in consumption. The acquisition was part of Veolia's plan to double sales in the US and Canada by 2030.

US EQUITIES

Wall Street edged higher overall this week with the S&P 500 up 0.3%; the Nasdaq 1.2% higher while the Russell 2000 slipped 0.4%. Uncertainty over a possible eviction of the Fed chair sent the dollar 0.8% lower.

Tech continued to rise, underpinned by **Nvidia**, which jumped 5.4% after the group received US approval to resume selling its H20 chips to China. The news also propelled **Advanced Micro Devices** (+11.3%) and **TSMC** (+5%).

Banks kicked off the second-quarter earnings season. **JP Morgan** (+0.6%) revised guidance higher after upbeat figures driven by trading and investment banking. Corporate defaults stabilised with a positive effect on **Citigroup** (+6.9%). **Wells Fargo** (-3.2%) also benefited but cut annual guidance on interest income. Despite US customs tariffs, banks were keen to stress that consumer indicators reflected continued strength in the economy.

In consumer discretionary, **Netflix** gained 1.9% after raising guidance and reporting robust quarterly figures. **United Airlines** (+4%) also raised annual guidance. The group stressed that demand had returned for the second half of the year as consumer confidence revived despite persistent economic instability. In consumer staples, **PepsiCo** (+6.9%) surprised markets by reporting a rise in quarterly revenues, mainly thanks to international sales. However, volumes in the US fell.

Healthcare (-2.7%) was this week's worst performer. Bucking the trend, giant **Johnson & Johnson** gained 3.4% thanks to upbeat results and lower-than-expected tariff impacts (\$200m instead of \$400m). Healthcare insurer **Elevance Health** tumbled 12.5% after slashing its annual revenue forecast. The group blamed drastic budgetary cuts due to the Affordable Care Act and Medicaid.

Other losing sectors this week included energy (-2.3%) and materials (-2.4%).

EMERGING MARKETS

The MSCI EM index was up 1.03% in USD this week as of Thursday. China, Taiwan, Brazil and Korea advanced by 2.42%, 1.17%, 0.65% and 0.13%, respectively. Mexico edged 0.24% lower. India was flat.

In **China**, the economy grew 5.2% in the second quarter as exports offset consumer spending. Retail sales growth slowed sharply to 4.8% YoY in June, missing the 5.2% expected. Industrial production rose 6.8% YoY in June vs. the 5.6% expected while exports grew by 5.8% YoY vs. expectations for 5.2%. Fixed asset investment saw the slowest growth since December 2021, rising 0.5% YoY in June. The State Council met to talk about boosting consumer demand further and pledging to reduce irrational competition in the EV industry. **Pop mart** expects revenue to increase 200% YoY and profits to increase 350% YoY. **Baidu** announced a multiyear strategic partnership with **Uber** to deploy thousands of Baidu's Apollo Go autonomous vehicles.

In **Taiwan**, technology-related exports continued to enjoy strong momentum with June exports rising 33.7% YoY vs. 27.1% expected while exports to the US rocketed 90.9%. June CPI rose 1.37% YoY, or less than the 1.60% expected. Second-quarter sales at **TSMC**, excluding currency effects, beat guidance at the high end on robust AI demand.

In **South Korea**, the central bank kept the benchmark rate stable at 2.5%. Exports for the first 10 days of July grew 9.5% YoY and imports grew 1.8% YoY. The government will start to distribute cash vouchers to all citizens. Donald Trump postponed his 25% reciprocal tariff on Korea to August 1. **Samsung Electronics'** preliminary second-quarter figures missed consensus expectations mainly due to a delayed earnings recovery in semi divisions. Deputy Prime Minister nominee Koo Yun-Cheol said he was in favour of the idea of separate taxation for dividend income. **Hyundai Motors** will launch a mass-produced version of its advanced robotics-based small mobility platform by the end of this year.

In **India**, Prime Minister Narendra Modi and Brazil's President Lula signed six agreements to expand the horizon of the cooperation between the two countries in sectors such as energy, agriculture and technology, setting the target of achieving \$20bn in bilateral trade over the next five years. The Defence Ministry is seeking to increase defence spending as a percentage of GDP from today's 1.9% to 2.5% over the next five years. India's domestic pharma market grew 11.5% YoY in June, an acceleration vs. May's 6.9%. **Titan**'s preliminary report indicated sales growth below consensus, but in line with guidance. Kotak Mahindra surprised on the upside as credit for the first quarter of FY 2026 grew 14% YoY, outperforming the system and expectations. **TCS** reported a weak quarter with headline numbers missing consensus expectations. **Hindustan Unilever** announced the appointment of a new CEO. **JSW** Group plans to raise its stake in **JSW MG Motor India**, its car manufacturing joint venture with **SAIC Motor**.

In **Brazil**, June inflation came in as expected at 5.35% YoY. May retail sales rose 2.1% YoY, or less than the 2.6% expected. The Supreme Court backed the IOF tax increase.

In **Mexico**, June CPI rose 4.32% YoY, or in line with expectations. Spanish foreign direct investment in Mexico jumped 69% to 3.3bn in 2024 compared to 2023. June output in the automotive industry rose 4.9% YoY and exports increased 14% YoY. **CIBanco**, **Intercam** and **Vector** won a temporary reprieve from US money laundering sanctions. **Walmex** reported weak results driven by lower EBITDA margins on higher expenses.

CORPORATE DEBT

CREDIT

Ahead of the Fed's key monetary policy meeting this month, and with Jerome Powell still under pressure, returns on credit markets were flat. The Xover continued on its gradual contraction, flirting with 275bp, a year low. The new issuance market remained busy before the summer break: Greece's **AlphaBank** raised €500m with a Tier 2 at 4.3% due 2036. In the high yield space, regular issuers like **Loxam** and **Levi's** sold debt. In a more notable move, ice cream maker **Froneri** raised billions with new bonds and €3bn with syndicated loans to fund a €4bn dividend for its shareholders, **Nestlé** and the **PAI Partners** private equity fund.

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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18/07/2025

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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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