



EDMOND DE ROTHSCHILD ASSET MANAGEMENT

MARKET FLASH - THE SIEGE OF TROY: TAKING THE LONG VIEW, A BLIND SPOT FOR MARKETS

- **US equity markets are once again banking on a scenario of sufficient growth and contained inflation, favouring technology and semiconductors, while defensive sectors are being shunned.**
- **The record fall in crude oil stocks and the possibility of a prolonged blockade of the Strait of Hormuz show that the US is using up its safety margin without addressing the structural risk of a lasting energy shock.**
- **In the eurozone, core inflation is falling but consumer confidence has dropped to its lowest level since the Covid crisis**

US equity markets are desperate to reconnect with the reassuring Goldilocks scenario, i.e. enough growth to underpin earnings, inflation that looks to be under control and an environment which is just stable enough to warrant a return of momentum, especially in technology and AI. Semiconductors and hardware are back in favour while defensives like consumer staples and some services are being snubbed, rather as if the risk of a protracted shock had disappeared.

Some data back up this view. In the US, activity is holding up with no apparent excess. Housing starts rebounded in March after several soft months even if building permits are only returning to normal after bad weather at the beginning of 2026. Residential property, however, is still under pressure: long bond rates have risen because of the Iran conflict and the number of mortgages remains very low.

Energy is a good reflection of the gap between short-term comfort and long-term risks. Crude oil inventories fell by more than 13 million barrels in a week, the biggest decline since July 2023. If we include all distillates, the drop is more than 20 million barrels, a clear indication that the global energy supply deficit is starting to appear in inventory readings. Strategic reserves have been called on the most while commercial inventories are still above pre-conflict levels. Meanwhile, US press reports said Donald Trump was considering a prolonged blockade of the Strait of Hormuz. The news sent Brent crude to its highest level since the conflict began. More recently, we have seen that the longest-dated maturities are being affected by supply tensions.

In other words, the US is eating up its safety margin to cushion the shock but not dealing with the root of the problem: the double blockade of the Strait of Hormuz is going to be more complicated and riskier for some time.

The situation in the eurozone is mixed but worrying over the longer term. Inflation in Germany and Spain came in below expectations and underlying inflation was down, falling to 2.3% in Germany and 2.8% in Spain. These figures might seem to reduce pressure on the ECB but not if we look at household inflation expectations. Strong bank lending provides us with another mixed picture. In March, households borrowed €18bn and companies €27bn. However, the European Commission's confidence survey fell to a post-Covid low with

consumer confidence down sharply. Access to loans is improving but households have reduced visibility.

Meanwhile, equity markets continue to focus on a small kernel of winners. Earnings revisions are accelerating sharply in energy, semiconductors and some commodity industries but segments with direct exposure to end demand, like consumer discretionary, transport and parts of the telecoms sector, are still under pressure. The tech derating took relative valuations to almost a nine-year low, but the segment has enjoyed a vigorous rally, largely due to AI themes while software has been left trailing. Investors are focusing on what is working today. They hope that these growth pockets will be enough to offset the gradual decline of the rest of the economy.

In economics, just as in geopolitics, the status quo is never neutral: it can eat at margins, delay investment and undermine confidence. Markets have so far chosen to look only at today's winners and relatively tame inflation. But they could find out later that the long view, which they tend to treat as a secondary variable, is in fact the heart of the problem. From the end of March, we sought to capitalise on the equity and bond market rebound but it is now time to tactically protect our portfolios with increased hedging while remaining invested.

EUROPEAN EQUITIES

An avalanche of results swept over Europe this week in an earnings season that has generally been upbeat. There have been fewer disappointments than the uncertain economic environment might have led us to expect.

In chemicals, **BASF**'s solid figures were partly lifted by a non-recurring item following a legal dispute. All divisions showed signs of accelerating so the fact that the group simply maintained guidance appeared rather cautious. **IMCD** had a results beat on strong momentum in Asia. What's more, prices are expected to be hiked significantly from this current quarter.

In industrials, most divisions at **Air Liquide** posted disappointing figures even if sales of semiconductor gas remained strong. **Epiroc** swept past expectations thanks to orders for equipment and services. But at **Assa Abloy**, a recovery in volumes has once again been put back so downward revisions could be coming. Revenues at **KION** were in line but the group won significantly more orders than expected, perhaps because clients were anticipating price rises in coming quarters.

In energy infrastructure for networks and components, results at **Schneider Electric** were in line thanks to the Energy Management division. But, sales in Industrial Automation were disappointing and the market had hoped guidance would be raised. **Prismian**'s first quarter fell short as weakness in the high voltage segment weighed on margins. **Technip Energies** revised guidance lower due to its Middle East exposure and the suspension of some projects in the region.

In consumer goods, **Unilever** slightly beat expectations thanks to volume growth which suggests growth will accelerate over the rest of 2026. Figures at **Remy Cointreau** fell short due to a slower-than-expected rebound in cognac sales. In autos, **Stellantis** reported free cash flow that was more negative than expected as well as persistently soft margins. **Michelin**'s results were generally in line with growth owing more to volumes than pricing.

Capgemini posted excellent results with growth accelerating sequentially. AI-linked orders now count for 11% of the total. **DSV** posted a disappointing drop in volumes in its Air & Sea divisions. The next catalyst for the share will be the group's Capital Markets Day on May 12. **AstraZeneca** beat expectations. **Kone** had a very good quarter with improving revenues and new orders; guidance was adjusted towards the top of the spread. The group said it had informed **TK Elevator** it was bidding for it. But will the acquisition get regulatory approval?

US EQUITIES

Against the backdrop of the ongoing energy crisis and a divided Fed, the S&P 500 edged 0.4% lower and the Nasdaq shed 0.66%. The Russell 2000 ended the period 1.7% lower.

The Fed left its rates unchanged after what was Jerome Powell's last meeting as chair. His mandate ends on May 15 but he said he would remain on the board to defend the bank against political pressure. Voting at the meeting revealed the Fed was very divided. Four governors voted against the decision, the largest dissenting number since 1992. Three members said the communique was overly accommodating while another argued for an immediate 25bp cut. Jerome Powell warned the meeting that inflation had not yet peaked and that the energy shock could result in another flare up. Markets have in any case largely abandoned the idea of a rate cut this year and are now starting to factor in the possibility of some tightening further out.

After Wednesday's close, four of the Magnificent Seven reported results. **Alphabet's** sales rose by an impressive 22% over a year to \$109.9bn, driven by a 63% surge in Google Cloud's revenues. **Meta** beat expectations but the share was down pre-market due to the group massively raising investments. **Microsoft** slipped after the bell. Investors viewed Azure's growth as missing expectations. **Amazon** increased spending on its cloud activity, a decision which has made trading in the share particularly volatile. Capex is still at the core of the AI theme. Spending is clearly on the rise but there is reduced visibility beyond 2026. **Microsoft** wants to boost investments by around \$36bn this year, **Meta** by around \$10bn and **Google** around \$5bn. **Amazon** has so far not said it will spend more. In all, these four groups could spend close to \$725bn in 2026, with \$1 trillion earmarked for 2027, or around 38% more than current levels.

In this week's sector returns, Energy (+3.78%) led gains: **Permian Resources** gained 2.7% over the period, a reflection of the higher-for-longer price scenario. Financials (+0.88%) advanced slightly but with significant dispersion. Payment services and data stood out: **Visa** (+8.1%), **Verisk Analytics** (+7.6%), **Mastercard** (+3.7%) and **FactSet** (+3.1%).

IT slipped 0.66% but with marked dispersion. **Qualcomm** jumped 17% in extended trading on good news about a hyperscaler client and signs China was recovering. **Nvidia** shed 1.8% and **Teradyne** plunged 19.4%, the biggest drop in the index. **Viavi Solutions** surged 24% before the market opening on indications sales would beat expectations. **Healthcare** (-0.99%) was affected by medical device and equipment plays like **GE HealthCare** (-15.6%), down on cost inflation and tariffs. **Insulet** plunged 15% on an FDA warning over insulin pump incidents. **Baxter International** tumbled 8.6% ahead of its quarterly results. In contrast, **Biogen** gained 6% on upbeat figures from its Alzheimer drug, Leqembi. **Centene** (+24.1%) jumped on better-than-expected quarterly results, raised earnings guidance for 2026 and a medical costs indicator which proved more favourable than expected. Consumer discretionary (-1.34%) was hit by fears inflation would stay elevated with "higher for longer" interest rates. **Starbucks**, however, posted upbeat figures and **O'Reilly**

Automotive gained 4% on better operating margins. **Ford** fell after the bell despite better-than-expected EPS and improved guidance. **MGM Resorts** lost ground after EPS missed expectations.

Materials (-2.67%) led losers due to fears energy costs would stay high and financial conditions more restrictive, weighing on industrial demand and margin expectations. Mining companies were the worst hit. **Newmont** lost 7.3% and **Freeport-McMoRan** 6%. Specialist chemicals were also down with **Sherwin-Williams** 5.4% lower and **PPG Industries** off 5.1%. But some steel makers and basic chemicals groups proved more resilient. **Dow Inc.**, for example, gained 3.8%.

EMERGING MARKETS

The MSCI EM index was 0.53% in USD as of this Thursday's close. Korea, Taiwan and India were up by 2.99%, 0.54% and 0.47%. Mexico, Brazil and China were down by 3.34%, 2.68% and 0.18%

In **China**, industrial profits jumped 15.8% YOY in March, taking Q1 2026 profits up 15.5% – the biggest pickup for the period in five years. April composite PMI came in at 50.1, suggesting China's economy remained resilient despite the Iran conflict. The NDRC ordered **Meta** to unwind its already completed \$2bn acquisition of AI startup **Manus**. China EV exports rose 42% YoY in March, and solar exports doubled in a month to record highs as countries responded to energy shocks. First-quarter results at consumer companies were broadly in line 1Q, with early signs of recovery. Industrial companies with higher export exposure suffered an unfavorable FX impact, while margin resilience was better than feared amid the current raw material price rises. **BYD's** Q1 profit tumbled to its lowest in over three years, signalling strain from the EV price war, while exports remained solid. China's Big Three airlines (**Air China, China Eastern, China Southern**) all swung back to profit in the first quarter thanks to a passenger demand surge offsetting jet fuel costs.

In **South Korea**, **Samsung** said that higher oil prices raise shipping-cost risks; Korea and Australia agreed to work on stable energy supplies (including liquid fuel and LNG). **SK Hynix** is reportedly raising as much as \$10bn in its planned US listing. **Hanwha Aerospace's** first quarter operating income jumped 20.6% on robust arms exports. **Samsung Electronics** chip profit soared 48-fold due to the AI-fuelled memory shortage. **LG Electronics** returned to profit in the first quarter after a Q4 loss, signalling resilience despite tariff and Mideast headwinds.

In **Taiwan**, Q1 GDP grew 13.69% YoY (est. +11.30%) – the fastest since 1987 – driven by AI-related demand. **TSMC** is ramping 2nm production by 70% to power the AI future and exited its position in Arm. **OpenAI** is working with **MediaTek** and **Qualcomm** to develop smartphone processors targeting mass production in 2028. **Chroma** reported a beat driven by a surge in ATS sales

In **India**, the RBI tightened provisioning rules for future loan and credit losses. Bandhan Bank reported a beat on improving asset quality. **Axis Bank** had a mixed result with net income beating estimates but NII missed; **Maruti Suzuki** reported a beat on the topline and in line margin with an upbeat outlook on growth but cautious commentary on margins. **Varun Beverages** beat first-quarter expectations on stronger volume growth and better input cost management. **Hindustan Unilever** profits beat on tax-cut-enabled price reductions but said Iran-war-driven volatility presented fresh cost and supply risks. **Eternal** posted good results, amid high competition.

In **Mexico**, March export revenue surged 27.7%. President Sheinbaum confirmed an agreement to set diesel at MXN27/litre after a meeting with **Pemex** and the gas station sector. **Walmex**

reported weaker results due to higher expenses. Management expects better results ahead, driven by operational results.

In **Brazil**, the BCB cut the Selic by 25bp to 14.5% (its second straight cut) but dropped forward guidance — signalling a cautious stance. President Lula plans to roll out a R\$100bn (~\$20bn) household debt renegotiation programme ahead of October's election. **Santander Brasil** missed on first-quarter results; private credit is <1% of total credit and the book is fully hedged with no material risk. **WEG**'s first quarter was a soft print on FX headwinds and weaker start-of-year seasonality.

CORPORATE DEBT

European credit markets turned more restrictive. Financial conditions tightened after government bond yields rose due to geopolitical tension and rising energy prices. The ECB is therefore likely to stay cautious over the short term but is moving towards a more restrictive bias that could mean a 25bp rate hike in June. Note that markets have already largely factored in this rise but they are also expecting another three similar moves higher this year.

Since last Friday, Brent crude has jumped 15% to return to around \$120, a year high. The Euro Stoxx lost 1.2% (-0.6% YTD°, Investment grade 0.4% (-0.3%) and High Yield 0.2% (+0.2%). There were big moves on credit markets. The Schatz and the Bund widened by 16 and 11bp to 2.71% and 3.11%. But cash spreads did not budge.

The credit market's technical situation is still very healthy. Investors are generally moving from equities and private credit to public markets. The new issues market is still busy and investor appetite is strong. Dispersion has risen but the distress ratio is still low with default expectations anchored below long term averages.

The European scorecard for yields is 2% for money markets, 3.2% for short-dated IG, 3.6% for IG, 4.6% for BB-rated issues and 6.7% for B rated companies.

The latest high yield issue was from Belgium's **Befimmo** (property management) which is owned by Brookfield. Befimmo refinanced with a new 2031 B+ maturity at 6.875%. An average 40% of investor bids were served and the bond then traded above its issue price.

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.

- CTA: quantitative strategy which uses futures to invest in a wide range of financial assets, including equity indices, short-term and long-term interest rates, currencies, and commodities.
- 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.
- RT1s: perpetual bond issues with early redemption possible after 10 years. Coupon payments are discretionary and non-cumulative.

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