EDMOND DE ROTHSCHILD

EDMOND DE ROTHSCHILD ASSET MANAGEMENT

MARKET FLASH: DONALD TRUMP RESUMES HIS TARIFF CAMPAIGN, UNDERPINNING A WAIT-AND-SEE STANCE AMONG CENTRAL BANKS

- **Donald Trump's recent decisions have rekindled uncertainty, particularly with the increase in H-1B work visa fees to $100,000 and the announcement of a new set of tariffs.**
- **Despite the economic slowdown and tame inflation, central banks in China and Switzerland chose to leave rates unchanged.**
- **Market expectations of Fed rate cuts have faded, and US and European government bonds have risen significantly.**

Russia's increasing drone and plane incursions within Europe's airspace further reduces the chances of resolving the Ukraine crisis and reducing energy prices.

Despite the economic slowdown and tame inflation, central banks in China and Switzerland chose to leave rates unchanged. Chinese exports rose 4.4%, or the lowest rate since February as US import expectations declined, but the PBoC wants to wait for improved visibility on trade with the US. Switzerland is also waiting to see what impact US tariffs of 39% will have and is setting the bar high for any return to negative rates.

In the US, statements from Fed governors showcased the steep divide between those worried about jobs and others focused on inflation risks. Donald Trump's latest decisions are likely to fuel the debate: H-1N work visa costs have been raised to $100,000 and import tariffs have been set at 25% for heavy goods vehicles, 100% for drugs and 50% for furniture. These measures will essentially hit US allies and not China. Over the medium term, these additional costs should feed thought to inflation and they could also reduce activity and jobs. So far, the rise in the jobless rate has mainly been caused by the anti-immigration policy shrinking labour supply.

For the moment, the latest economic data suggest the Fed was right to adopt a wait-and-see policy. Composite PMI is at a resilient 53.6 while second-quarter new orders, GDP and consumption were up 0.4%, 3.8% and 2.5%, respectively. And weekly jobless claims fell to 218,000 when they were seen remaining at the previous reading of 233,000. What's more, the latest GDP price index was 2.1%, or higher than expected and up on the precious 2%.

European data were more mixed: September's manufacturing PMI returned to negative territory at 49.5, down from 50.7, but services surprised by rebounding to 51.4 vs. 50.5 (except in France). This left the composite index at 51.2 compared to 51 previously. Activity in the UK continued to slow down in August (51 vs. 53.5) and there is a possibility of more tax rises to meet a new £30bn black hole in the budget.

These developments led to market rate-cut expectations falling and sharp rises in both US and European government bond yields. We think current levels are tactically attractive so we have raised our scores on US and European government bonds. We remain upbeat on emerging country debt and investment grade carry and are still cautious on the dollar and US equities.

EUROPEAN EQUITIES

As mentioned before, Eurozone manufacturing PMI came in at 49.5 in September or below the 50.7 expected while services beat expectations by rising to 51.4 when analysts were going for 50.4. In the US, and ahead of the PCE price index announcement, the final second quarter GDP growth reading was raised to 3.8%, or higher than the 3.3% pencilled in by analysts. The US economy looks more resilient than previously assumed. Treasury yields logically rose along with the dollar while expectations for Fed rate cuts edged lower.

European car sales rose 5.3% compared to the same month in 2024 and for the first time in a year, sales at **Stellantis** increased (source: the European Automobile Manufacturers' Association). Elsewhere, defence stocks like **Hensoldt, Saab, Leonardo** and **Rheinmetall** gained ground amid even more tension between Ukraine and Russia. **ASM International** cut its sales target for the second half of 2025, citing weak demand. The decision suggested caution in Europe's tech sector which is less exposed to AI momentum than companies in the US. DIY giant **Kingfisher** raised guidance after posting better-than-expected quarterly figures, a token of resilient consumer spending, especially in the UK. In the pharmaceutical sector, **Roche** rose to start the week thanks to upbeat results for Giredestrant, its treatment for advanced breast cancer. Sentiment was also boosted by the new management's remarkable progress in revamping R&D. Transport multinational **Alstom** trended higher thanks to a strong new order flow in the second quarter, particularly in the US. As a result, we can expect robust cash flow in the second half. Management is expected to reaffirm its annual objectives.

US EQUITIES

Unlike previous weeks, Wall Street ended lower. The S&P 500 fell 0.89% and the Nasdaq 100 0.93%. The decline was in part due to unexpectedly strong economic data which affected monetary policy expectations. Second-quarter GDP growth, for example, was revised up to an annualised 3.8% and weekly jobless claims fell from 232,000 to 218,000. The probability of two 25bp rate cuts by the end of this year then fell to 60%. Elsewhere, Donald Trump signed a decree to make the sale of **TikTok**'s US business to a consortium of investors official. There is a risk of a shutdown in the coming weeks and budget paralysis if democrats and republicans in Congress fail to reach an agreement.

Healthcare was the week's worst performer due to the risks of additional tariffs on imported medical devices and drugs. New tariffs on heavy goods vehicles and furniture are also in the offing. In consumer discretionary, **CarMax** plunged 22% on a drop in sales and mounting risks of loan payment delinquencies. Tech stocks also weighed on indices. **Oracle** fell 5.6% and **Micron Technology** 3.6% on profit taking. In sharp contrast, **Intel** gained another 14.9% on the possibility **Apple** might buy a stake. **Nvidia** is to invest up to $100bn in OpenAI. The news fuelled the debate on fund flow circularity insofar as Nvidia's cash injections could end up helping to buy its own chips, thereby increasing the risk of an AI bubble.

Elsewhere, **Boeing** rose after **Turkish Airlines** ordered 75 B7878 planes and **General Dynamics** was lifted by a $1.5bn IT contract.

Healthcare giant **Pfizer** is to buy **Metsara**, a weight loss start-up. **GE Healthcare** fell 4.6% after the US Commerce Department launched an investigation into medical equipment and device imports. The gold ounce continued to advance, hitting record all-time highs and consolidating around $3,750.

EMERGING MARKETS

The MSCI EM index had edged 0.24% higher in USD as of Thursday. Taiwan and Korea outperformed other markets, advancing by 1.63% and 1.17%, respectively. Mexico and China gained 0.75% and 0.56% while India fell the most, down 2.69%, followed by Brazil (-0.88%).

In **China**, the central bank kept the Loan Prime Rate (LPR) unchanged in September as expected. Donald Trump signed an executive order to approve the **TikTok** deal and keep the app operating in the US via a majority (>80%) US-owned JV. The proposed $14bn price tag is much lower than the previous $40bn valuation. Xi Jinping and Donald Trump are scheduled to meet at the APEC summit in Korea at the end of October. At the UN Climate Summit, President Xi pledged to expand wind and solar capacity 6 times from 2020 over 10 years. MOFCOM plans to expand supply for digital consumption and support livestreaming businesses. **Alibaba**'s CEO announced plans to boost AI investment beyond $50bn over the next 3 years. **Berkshire Hathaway** confirmed that it had sold all its **BYD** investment.

Taiwan is holding off on chip export controls placed on South Africa, a sign that it is uncomfortable with using the key tech export as a weapon in diplomatic disputes.

In **Korea**, **Samsung** is reportedly planning to hike contract prices for memory chips by 5-30% in the fourth quarter of this year. **Naver**'s fintech arm is in talks with **Dumanu**, operator of South Korea's largest crypto exchange **Upbit**, over a potential merger.

In **India**, the IT service sector remained under pressure as the Trump administration proposed to scrap the H1B visa lottery system and introduce wage based selection. **Accenture**'s weaker organic growth guidance weighed on Indian IT services stocks. The government is said to be considering increasing the foreign investment ceiling in PSU Banks from its current 20%. President Trump announced that he would be imposing a 100% tariff on branded or patented pharma products, starting October 1st, unless a company invests in the US. This suggests that non-patented drugs (generics) are exempted. The **Airbus** board will meet in New Delhi, an indication of India's rise in aviation. The meeting highlights India's strategic role for Airbus.

In **Indonesia**, the deadly mud rush at the Grasberg mine will reduce near-term copper and gold output, with a possible return to pre-incident operations earliest in 2027.

In **Poland**, August retail sales fell from 4.8% in July to 3% on lower food prices.

In **Mexico**, **Citibank** sold its 25% **Banamex** stake to local businessman Fernando Chico Prado. Banxico trimmed reduced rates by 25bp to 7.50%, signalling more cuts ahead. Data center provider **CloudHQ** will invest $4.8bn in an AI data center in the Mexican state of Queretaro.

In **Brazil**, Lula is expected to hold discussions with Donald Trump next week. According to Bloomberg news, one of the main topics will be critical minerals.

The US offered broad support for **Argentina**. The World Bank sped up support for Milei's government, pledging to deploy $4bn of a pre-existing $12bn aid package in the coming months.

CORPORATE DEBT

The final reading of second-quarter US growth was revised up from 3.3% to 3.8% and weekly jobless claims improved. Markets should have benefited from the news but instead a fresh wave of customs duties levelled at a large range of US imports, notably drugs, rekindled uncertainty. As a result, credit markets were relatively stable over the week, despite higher government bond yields. Euro IG was down 0.1%, Euro HY was flat, Euro Hybrids edged 0.1% higher and Euro CoCos were level.

Even so, new issuance continued apace as order books filled up amid persistently strong appetite for credit. European high yield had one of its busiest periods with around 15 deals for a total of €7.2bn in seven days. **Kiloutou** raised €200m to fund acquisitions and petrochemical group **Ineos** €800m at 7.25% due 2031. In financials, **Generali** raised €500m with an RT1 at 4.75%. The order book took in €6.5bn with an initial issue yield of 5.375%. USD corporate hybrids saw large perpetual deals from **American Electric Power** and **Alliant Energy**. Demand in the sector is still strong. **Alliander**, for example, sold a perpetual bond at 4.125% when its initial issue yield was 80bp higher.

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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EDMOND DE ROTHSCHILD ASSET MANAGEMENT (FRANCE)

47, rue du Faubourg Saint-Honoré 75401 Paris Cedex 08

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332.652.536 R.C.S. Paris