CAIM | CROWN AGENTS INVESTMENT MANAGEMENT

APRIL 2025

CAPITAL MARKETS MONTHLY

FIXED INCOME

CHARLES THOMSON

HEAD OF PORTFOLIO MANAGEMENT

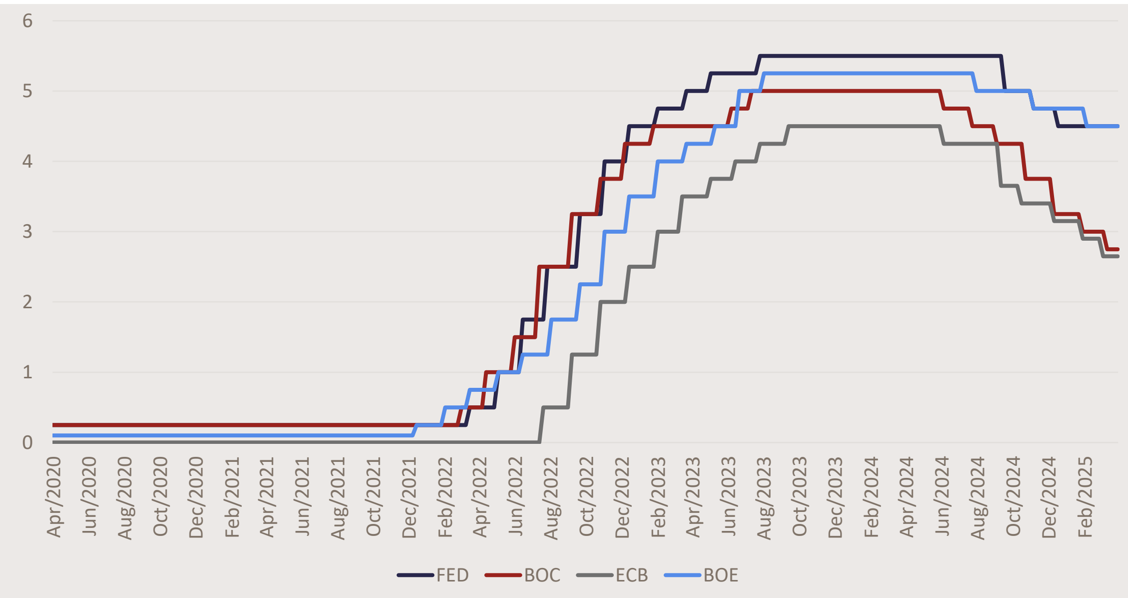
Yield volatility remains elevated as geopolitical uncertainties persist

The Federal Reserve maintained unchanged interest rates at the March FOMC meeting. The upper band of the Funds rate therefore remained at 4.5 percent. The FOMC statement highlighted the increased uncertainty around the economic outlook as the impact of tariffs may reduce GDP growth while impacting prices adversely. From April, the Fed announced a deceleration in quantitative tightening by reducing the monthly redemption cap on Treasury securities from USD 25 billion to USD 5 billion. The dot plot showed the longer-run rate unchanged at 3.00%, while the projected level of the Funds rate at the end of 2025 was 3.875%, equivalent to two 25bp cuts. This is line with market expectations. Voting against this action was Christopher J. Waller, who supported no change for the federal funds target range but preferred to continue the current pace of decline in securities holdings.

There remains significant downward pressure on short term interest rates globally. Both the Bank of Canada and the European Central Bank cut rates in March. The BoC has now reduced the overnight lending rate from 5.00% to 2.75% over while the ECB has lowered the deposit rate from 4.00% to 2.55% over the same period. A deteriorating economic outlook with below-trend GDP growth is the main driver of further monetary policy easing. Over the near term, the negative impact of US tariffs, scheduled to start in early April, is likely to push equity valuations and bond yields lower. Therefore, we expect fixed income markets to perform strongly in coming weeks.

The chart below shows the path of G7 short term interest rates (excluding Japan).

Monetary policy easing continues in Europe and North America



Source: Bloomberg Finance L.P., April 2025.

During March 2025 there were eighteen Sovereign, Supranational and Agency issues in USD with amount outstanding of at least USD 500m, credit rating at least A- and maturity between 1 and 10 years. The UAE emirate of Ras Al Khaimah issued an inaugural USD 1bn 10-year transaction at an attractive spread of UST + 80bp. This traded significantly tighter in secondary markets, making it one of the best performing new issues last month. The Danish local authority lender Kommunekredit also performed well as the spread versus treasuries tightened from 17.5bp to 13bp. However, some transactions were clearly priced too aggressively and performed poorly. The inaugural New Zealand Local Government Funding Agency deal was arguably priced too expensively at UST +22bp. Despite a strong order book, these bonds widened in subsequent trading.

Issuer	Maturity	Issue Spread	Rating
Emirate of Ras Al Khaimah	12/03/2035	80	A
Kommunekredit	28/02/2030	18	AAA
Kreditanstalt fuer Wiederaufbau	15/05/2028	8	AAA
New Zealand Local Government Funding	20/03/2028	23	AA+
African Development Bank	18/03/2030	14	AAA
Canada Government	18/03/2030	11	AAA
European Investment Bank	15/06/2028	11	AAA
Islamic Development Bank	18/03/2030	25	AAA
International Bank for Reconstruction & Development	20/03/2030	15	AAA
OMERS Finance Trust	20/03/2030	38	AAA
Kommuninvest	21/04/2027	10	AAA
Asian Development Bank	22/03/2035	17	AAA
Inter-American Investment Corporation	01/04/2030	21	AA+
Japan Finance Organization for Municipalities	02/04/2030	36	A+
Kuntarahoitus	01/04/2030	18	AA+
New Development Bank	31/03/2028	38	AA+
Development Bank of Japan	08/04/2030	29	A+

Source: Bloomberg Finance L.P., March 2025.

FOREIGN EXCHANGE

SLAWOMIR SOROCZYNSKI

HEAD OF FIXED INCOME

The tariff wars present headwinds to the US Dollar.

March proved to be an eventful month for global financial markets. The long-awaited Federal Reserve meeting was well-received, with the key takeaway being that the Fed views inflation as transitory. The Fed's primary focus has now shifted to the economy and its growth trajectory. The market responded positively to this message, with risk volatility remaining contained. However, attention gradually shifted towards geopolitics, particularly regarding the US.

The tariffs deadline set for the beginning of April became a key factor affecting valuations in the foreign exchange market. The US Dollar Index (DXY) experienced one of its worst trading months since November 2022, dropping by 3.16%. Given this performance, it's no surprise that the US Dollar emerged as the worst-performing currency in the G10.

The main forex pair, EUR/USD, moved by 4.21%, marking one of the best months for the eurozone currency since 2022. The euro turned out to be the third-best-performing currency in the G10, with the top two spots taken by the Scandinavian currencies. The Swedish Krona advanced by 7.26%, while the Norwegian Krone gained 7.03%. For both currencies, this marked their best performance in a decade! We believe the solid fundamentals of both economies, along with their smaller exposure to tariff risks, made them an attractive investment for financial flows seeking diversification.

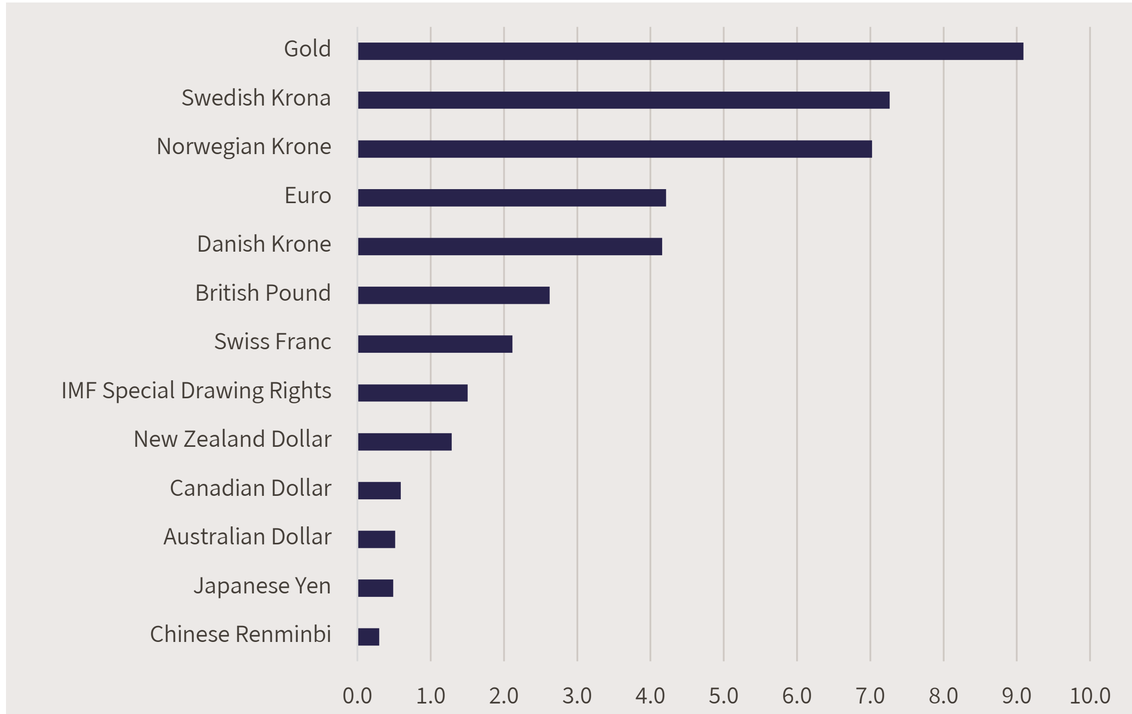
Traditional high-beta, commodity-linked currencies such as the Canadian Dollar and Australian Dollar gained substantially less against the greenback. This leads us to believe that risk reduction was not the main driver behind price moves in March. This view is supported by the relatively modest appreciation of the Japanese Yen (JPY), which has historically been used as a funding currency. The Swiss Franc, another traditional safe-haven currency, performed better than the JPY, delivering a 2.1% gain. (For a detailed performance breakdown, please see the table below).

As for the Chinese Renminbi, it had a relatively quiet month, with a modest 0.30% gain. This suggests that global diversification capital flows chose to stay away from China, which remains a potential epicentre of tariff-related risks.

Looking ahead, the market's focus will be entirely on tariff news, and any unexpected developments could trigger substantial shifts in global financial market dynamics.
The price action observed in March reinforces our view of US Dollar weakness, driven by diversification flows and repatriation flows from those who previously correctly predicted US exceptionalism.

In terms of market levels, our medium-term target for EUR/USD remains 1.1500, for GBP/USD it's 1.3500, and for USD/JPY, it's 142.00.

March performance vs. USD (%)



Source: CAIM, March 2025.

EQUITIES

SIMON PRICE

SENIOR EQUITY FUND MANAGER

United States

US- Selling pressures gain momentum as tariff and potential recession concerns increase

US equity markets experienced significant volatility, with the S&P 500 posting its largest monthly decline since 2022. This was largely driven by the President's aggressive stance on tariffs, which led to heightened recession fears and concerns about inflation. Both the President and Treasury Secretary indicated they were prepared for economic pain to reorientate the economy, further increasing these fears. Investors worried about higher inflation, which was already above target, despite the Federal Reserve's assurances that the impact of tariffs would be transitory. By the end of the month, volatility had decreased from recent highs.

In terms of monetary policy, The Federal Reserve maintained the fed funds rate at 4.25%-4.50% for the second consecutive meeting and announced a slowing in the pace of quantitative tightening (QT). The updated dot plot revealed that the median FOMC member still expects two rate cuts in 2025, although the distribution of responses shifted towards a more hawkish stance, with 8 of the 19 members anticipating one or no cuts this year. Projections for 2025 showed higher core inflation and lower growth, with risks leaning towards stagflation. During the press conference, Powell emphasized that policy was in a "good place" and the Fed was not in a hurry to cut rates, citing "remarkably high" uncertainty. He acknowledged that tariffs might delay progress on inflation but maintained that their impact would be transitory, with long-term inflation expectations remaining anchored.

Regarding the macro environment, the latest jobs report was largely in line with consensus, with the unemployment rate ticking up to 4.1%. February's CPI numbers surprised on the downside for both headline and core inflation. Although PPI data was slightly softer than expected, components feeding into PCE inflation were relatively stronger, raising concerns about the Fed's ability to cut rates meaningfully this year.

On the corporate earnings front, fourth-quarter earnings exceeded expectations, with technology, financials, and healthcare sectors contributing positively. Within the technology sector, Nvidia, Microsoft, and Google had narrower surprises compared to the previous quarter, and capex spend for 2025 was projected to be stronger than anticipated.

In terms of performance, most equity markets declined, with significant losses in consumer discretionary, information technology, and communication services sectors due to weakness in the MAG 7 stocks. Defensive sectors outperformed cyclicals, with utilities and energy being the only sectors to see gains during the period.

Europe

Europe – ECB commentary and global risk off tone promote profit taking

Despite the ECB delivering another 25bps cut, bringing the deposit rate to 2.50% (with a total of 150bps cuts since last June), European equity markets couldn't escape the risk-off sentiment. In Germany, the debt break reform successfully passed its final legislative hurdle in the Bundesrat, but there remains significant uncertainty regarding the scale and timing of the anticipated fiscal expansion.

The recent rate cut was accompanied by hawkish adjustments, with the policy statement indicating that the stance has become "meaningfully less restrictive." The ECB also acknowledged that a pause at the next meeting in late April is a possibility. Overall, uncertainty dominated the discourse, with Lagarde emphasizing a data-dependent, meeting-by-meeting approach.

Over the past month, European sector performance has been largely influenced by tariff exposure. Sectors heavily exposed to US goods, such as Durables/Luxury, Autos, Healthcare, and Semiconductors, have underperformed. Conversely, more domestically focused and service-oriented sectors like Banks, Insurance, Telecoms, and Utilities have outperformed.

Developed Asia

Developed Asia –Japan to be negatively impacted by tariffs?

Performance was mixed across the region. Hong Kong saw slight gains following news that China was implementing policies to boost domestic consumption. Early support came from technology stocks, driven by rotations away from US technology and Alibaba's release of a new open-source AI model that performs comparably to DeepSeek's R1 with significantly less training data. However, profit-taking occurred later in the period.

Japan saw further selling pressure due to concerns over the negative impact of tariffs, leading to downgrades in EPS growth forecasts. Additional selling pressures were fuelled by comments from the US administration about the weak yen and the potential for a US recession

Emerging markets

EM equities was marginally positive for the month, outperforming developed markets by one of the highest margins since November 2022.

Regionally, Latam bounced back from its decline in February, aided by strong commodity prices, while CEEMEA posted gains and EM Asia posted a moderate decline.

AUTHORS

Charles Thomson
Head of Portfolio Management
charles.thomson@caiml.com

Slawomir Soroczynski
Head of Fixed Income
slawomir.soroczynski@caiml.com

Simon Price
Senior Equity Fund Manager
simon.price@caiml.com

CONTACT

Crown Agents Investment Management
The Rex Building
62 Queen Street
London
EC4R 1EB
United Kingdom

www.caiml.com
CAIMInsights@caiml.com
T: +44 (0)20 7489 7223

IMPORTANT NOTES