CAIM | CROWN AGENTS INVESTMENT MANAGEMENT

MAY 2025

CAPITAL MARKETS MONTHLY

FIXED INCOME

CHARLES THOMSON

HEAD OF PORTFOLIO MANAGEMENT

Rate cut expectations solidify - pushing short-dated yields lower

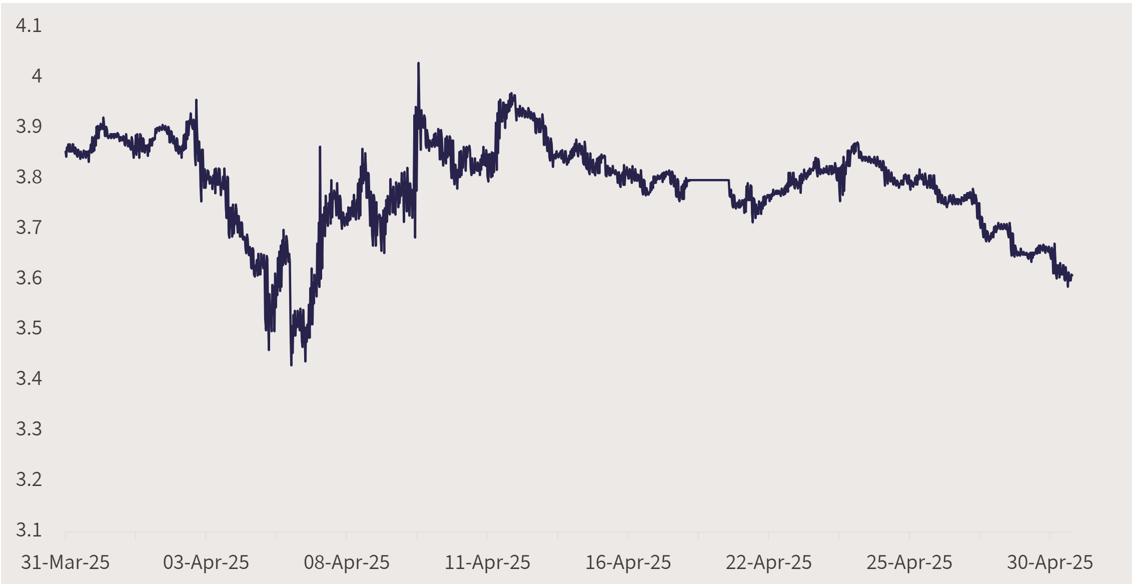
In the first week of April, short-dated US treasuries rallied strongly as yields declined sharply. The benchmark 2-year note yield fell by more than fifty basis points, from 3.96% to 3.43% between the second and fourth of April as recessionary fears escalated. This occurred despite solid US employment data showing an acceleration in non-farm payroll growth to +228,000 versus a consensus forecast of +140,000. It is, however, noteworthy that the overall unemployment rate did increase marginally, from 4.1% to 4.2% due to a rise in the labour force participation rate. Forward looking projections of US economic growth were revised downwards due to mounting concerns over the negative impact of tariffs and the significant decline in US equity indices.

The minutes of the March Federal Open Markets Committee meeting were released on 9-April. These minutes indicated that Governor Waller preferred to continue the pace of decline in securities holdings in place at the time of the vote (USD 25 billion per month). This view was based on reserve balances being over USD 3 trillion as well as there being no evidence from money market indicators that the banking system is getting close to an ample level of reserves. Additionally, rather than changing the pace of balance sheet reduction, Waller suggested that the Federal Reserve should rely on existing tools and develop a plan for how to respond to short-run strains if they emerge. There was no indication that a rate cut at the May FOMC was realistically likely, leading to significant upward pressure on yields of short-dated treasuries.

Further macroeconomic data release throughout the second half of April painted a clear picture of deteriorating economic outlook. This translated to a rally in short-dated bonds which caused the yield curve to steepen. Interest rate futures now imply over five 25bp rate cuts by the Federal Reserve over the next twelve months.

The chart below showing the path of the US Treasury 2-Year Note yield throughout April 2025.

US Treasury benchmark 2-Year Note yield over April 2025



Source: Bloomberg Finance L.P., 30 April 2025.

During April 2025 there were only three 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. Tokyo Metropolitan Government issued a USD 500m 5-year bond at a price of SOFR mid swaps plus 77bp equivalent to a US treasury spread of 41bp. These bonds remained at the issue spread in secondary trading. The German state of NRW issued a USD 1.5bn 3-year note at UST + 16bp (SOFR + 44bp). Again, these securities failed to perform versus UST in secondary despite the help of widening asset swap spreads. The AAA rated Norwegian KBN issued a 4-year floating rate note at SOFR + 41bp. These bonds widened and were bid at around SOFR + 43bp at the end of the month.

Issuer	Maturity	Issue Spread	Rating
Tokyo Metropolitan Government	07/05/2030	UST + 41bp	A+
North Rhine-Westphalia Germany	25/04/2028	UST + 16bp	AA
Kommunalbanken	09/04/2029	SOFR + 41bp	AAA

Source: Bloomberg Finance L.P., 30 April 2025.

FOREIGN EXCHANGE

SLAWOMIR SOROCZYNSKI

HEAD OF FIXED INCOME

US Dollar decline continues as gold prices reach new all-time highs

Tariffs have severely impacted markets. High uncertainty and poor liquidity have caused equity prices to drop sharply and credit spreads to widen. As usual, investors sought refuge in traditional safe havens. Gold prices surged to $3,500 per troy ounce, while government bond yields fell to their lowest levels of the year. This environment was fully reflected in the foreign exchange market. The search for safety pushed the USDCHF cross to levels not seen since 2015. The Swiss Franc (CHF) emerged as the best-performing G10 currency, appreciating over 7% against the US Dollar. Meanwhile, the Japanese Yen, another safe-haven currency, gained 4.8%, with the USDJPY briefly testing the key support area located at 140.00.

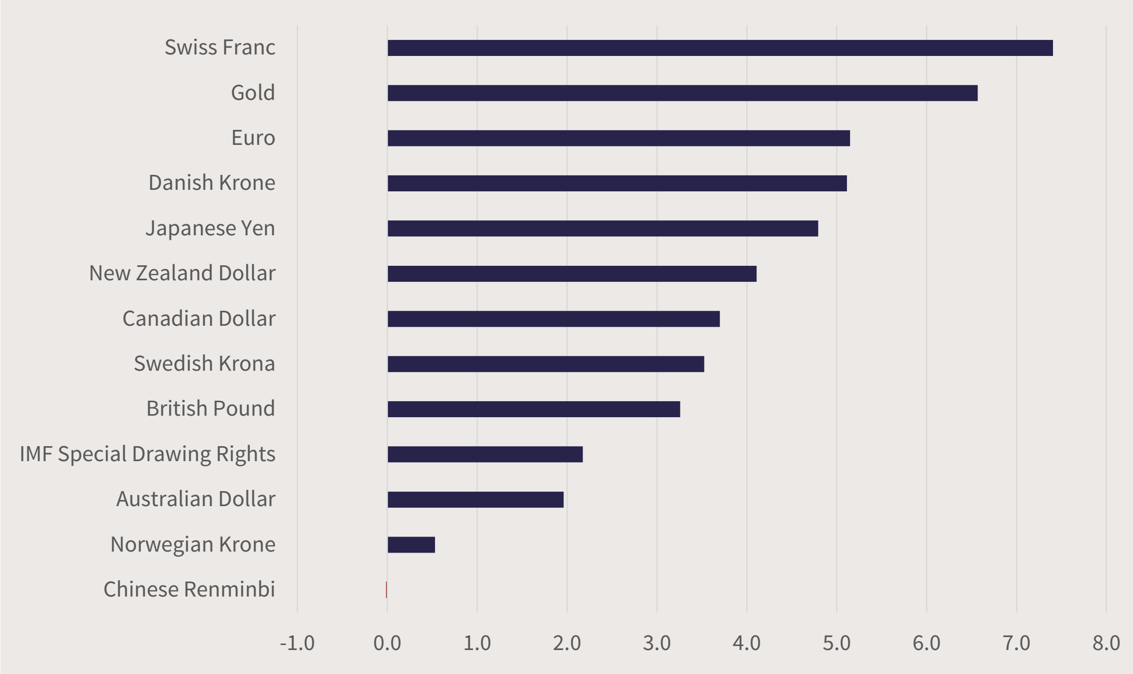
It's worth noting that, among the G10 currencies, (see the table overleaf), the EUR was the second-best performer. This supports another key investment theme observed in April: the search for a liquid alternative to the US Dollar. Going forward, we expect these two themes—diversification away from the US Dollar and a search for alternatives—will dominate the market landscape in the near term.

Elsewhere, traditional high-beta currencies outperformed the US Dollar, though the scale of the outperformance varied. After a strong performance in March, the Norwegian Krone took a breather, advancing only 0.5% in April. In contrast, the New Zealand Dollar posted a solid 4.1% gain against the greenback, followed by the Canadian Dollar (+3.7%) and the Australian Dollar (+1.9%). While it's challenging to pinpoint the exact factors driving this divergence among the high-beta crosses, we believe that their importance will continue to rise in global portfolios seeking alternatives to traditional currencies.

As for the Chinese Renminbi (CNY), it held its ground against the US Dollar. However, concerns over the domestic economy and fears of potential retaliatory measures from Washington kept global diversification flows away from Beijing. That said, following the recent depreciation of the US Dollar against major G10 currencies, the CNY looks extremely attractive from a non-USD perspective.

In summary, many currency pairs hit CAIM's medium-term price targets in April. While we believe the diversification away from the US Dollar will continue, many pairs now appear to be in overbought territory. As a result, we wouldn't be surprised to see some corrective movements in the near future. Our preferred scenario is for the market to consolidate below key technical levels before resuming its search for US Dollar alternatives. Key technical levels to watch include: EUR 1.1520-1.1550, USDJPY 138.50-140.00, and GBPUSD 1.3550.

April performance vs. USD (%)



Source: CAIM, 30 April 2025.

EQUITIES

SIMON PRICE

SENIOR EQUITY FUND MANAGER

United States

US- A rollercoaster ride with more to come

During the month, US equity markets experienced significant volatility but ended with only mild losses. The announcement of reciprocal tariffs by President Trump under the International Emergency Economic Powers Act (IEEPA), declaring a national emergency over the trade deficit, initially created market turmoil. Investors quickly repriced the likelihood of a US recession, fearing retaliation from other countries. This concern was exacerbated by the reaction of long-dated treasuries, with 30-year bond yields spiking above 5% intraday. However, market turmoil turned into elation when President Trump announced a 90-day pause on reciprocal tariffs for non-retaliating countries, and US officials began negotiating deals with other nations. Risk assets faced further pressure after Fed Chair Powell's speech, which suggested that any 'Fed put' remains well out of the money, prompting calls from President Trump for Powell's replacement. Sentiment improved when President Trump stated he had "no intention" of firing Powell and signalled a desire to reach a deal with China. This series of events caused volatility to gyrate, with the Vix moving above 50, a level seen only during the height of the GFC and initial Covid-19 turmoil, before declining to its lowest level since Liberation Day, closing beneath 25 points. In terms of monetary policy, Fed Chair Powell, sounded more concerned about inflation than the recent past. He warned that the tariffs were "significantly larger than expected", and that the Fed had an "obligation" to keep long-term inflation expectations anchored.

Regarding the macro environment, it was still a mixed picture with soft data, including sentiment indices, painting a weakening picture while hard data continued to point away from a recession. US payrolls data for March was better than expected. The unemployment rate did tick up slightly so there was little change there. Inflation data for March came in softer than expected. Headline inflation saw its largest monthly decline since early Covid restrictions in spring 2020, while core inflation saw its smallest monthly rise since January 2021 with the data showing little evidence of price pressures from the early rounds of tariffs.

On the corporate earnings front, US companies are generally reporting solid results for the first quarter. Although the percentage of S&P 500 companies reporting positive earnings surprises is below recent averages, the magnitude of earnings surprises is above recent averages. The index is also reporting double-digit earnings growth for the second consecutive quarter. US Banks and Non-Bank Financials generally reported solid fundamentals and healthy profitability, with those involved in capital markets benefiting from strong activity. Outside of financials, the Mag 7 entities that have so far reported were mixed. Microsoft delivered a solid revenue, and earnings beat amid strong AI-driven cloud growth. Meta's revenue also exceeded expectations, and the company boosted its 2025 capex plans. Alphabet, Google's parent delivered a decent revenue and earnings beat, mostly driven by its search advertising business, and announced a 5% dividend increase. Tesla's Q1 results saw sizeable misses on both revenue and operating income. Nonetheless, the company's shares gained after CEO Elon Musk touted the prospects for the company's autonomous vehicle and robot businesses and said that he would "significantly" pull back from his government work and devote "far more of my time to Tesla" starting next month.

In terms of performance, most US equity markets were in negative territory for the month but finished well off the lows. In terms of sector performance, it was a mixed picture with no clear theme. Information technology and communication services were leaders while energy and healthcare were laggards.

Europe

Macro and policy uncertainty take the lead

European equity markets faced significant challenges due to high macro/policy uncertainty, with tariffs and a rising euro posing hurdles for exporters.

The European Central Bank (ECB) cut interest rates by 25 basis points to 2.25%, marking the seventh quarter-point cut in the current easing cycle, totalling 175 basis points from the peak. The ECB's tone was mildly dovish, emphasising exceptionally high uncertainty and a heightened dependence on data.

Corporate earnings for the first quarter so far were mostly in line with expectations, but guidance has declined, leading to lower full-year projections. The sharp rise in the euro is becoming a headwind for European earnings, with relative EPS estimate revisions for Europe starting to decline in sync with the strengthening euro.

Over the past month, export/trade-sensitive sectors such as Autos, Tech ex-Software, Consumer Durables, and Healthcare have seen the steepest de-rating, indicating that some tariff risks are already priced in. Conversely, domestically oriented sectors, including retail, insurance, and utilities, have outperformed due to stronger EPS trends, in line with forward estimate revisions.

Developed Asia

Japan to potentially be a relative beneficiary of US/China tensions?

Performance was mixed across the region. Hong Kong saw declines due to larger-than-expected tariff hikes from the US on April 2 and China's unexpected retaliation.

Japan saw a rebound following the initial Liberation Day selloffs with expectations of an agreement in their tariff negotiations within 90 days as the US prioritises these negotiations. There are also expectations that Japan could be a beneficiary of capital flowing away from the US and China with the end of "US exceptionalism" and the escalation of US-China trade tensions.

Emerging markets

Emerging market equities posted modest gains in April, outperforming developed markets despite heightened trade policy uncertainty. Following initial declines due to the Liberation Day announcement and escalating tensions with China over reciprocal tariffs, markets rebounded. This recovery was driven by a 90-day reprieve on most reciprocal tariffs, excluding China and exemptions for certain electronic products.

Regionally, Latin America continued its strong performance from March, while Central and Eastern Europe, the Middle East, and Africa (CEEMEA) and EM Asia experienced more subdued gains.

AUTHORS

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

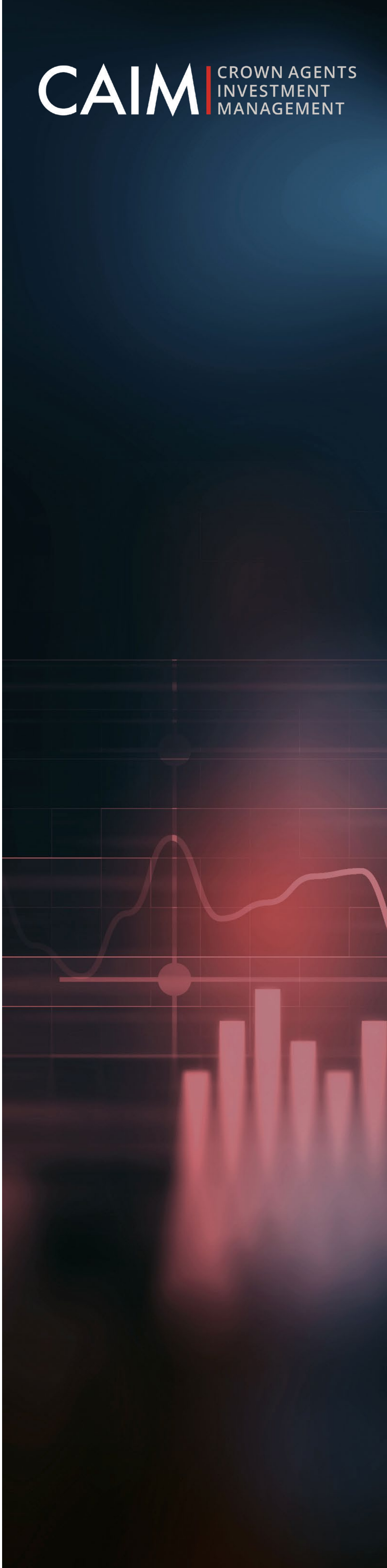
Slawomir Soroczynski
Head of Fixed Income
slawomir.soroczynski@caiml.com

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



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