

# Monthly Investment Viewpoint

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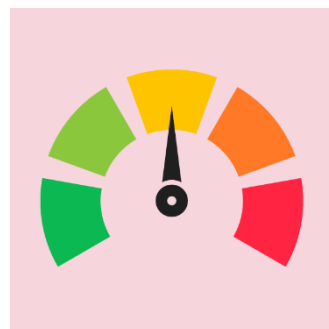
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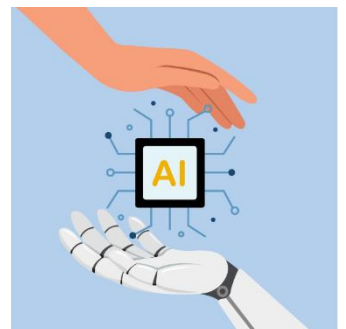
## KEY INVESTMENT THEMES



Tariffs, trade  
deficits and  
inflows



Interest rates  
and risk



China needs more  
than AI

...to read more  
from the

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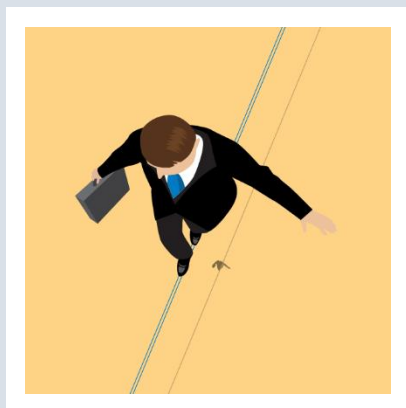
## Tariffs vs. investment returns



US President Donald Trump isn't happy with the global economic and political order. He feels the US has been badly treated. The prolonged and large US trade deficit means the rest of the world owns increased amounts of dollar assets. His tariff focus is one way of addressing this.

The US has enjoyed plentiful capital inflows - the bigger the deficit, the bigger the flows as foreign investors take comfort in the dollar's reserve currency status. But what if tariffs do cut the trade deficit? Capital inflows should ease too. Flows into US equities have been significant, and inflows boost stock returns, which in turn attract more inflows. The US has outperformed as a result. But if flows diminish, the US valuation gap versus the rest of the world could be reduced. As the old saying goes, be careful what you wish for.

## Understanding neutral rates can help investors allocate risk

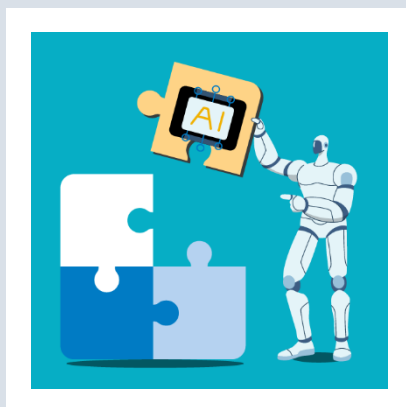


The European Central Bank (ECB) recently estimated the neutral rate - the short-term interest rate that would prevail when the bloc's economy is at full strength and inflation stable - to be between 1.75% and 3%. A simpler method looks at the sum of potential growth and the central bank's inflation target - which matches the ECB's main deposit rate of 2.75%.

In the US, models suggest the benchmark interest rate (at 4.50%) looks close to the neutral level. However, using the simpler method of assessment, the neutral rate could be lower, at around 3.50%.

Monetary policy decisions cannot be reduced to a single equation, but this is useful to investors when looking at the interest rate outlook and how they allocate risk.

## China's economy needs more than AI



The emergence of DeepSeek - a rival to the popular ChatGPT - has been a gamechanger in terms of China's position in the artificial intelligence (AI) race. It has bolstered optimism about AI's potential growth and economic benefits. But it's early days in terms of real-world applications; and the risks are vast - AI data usage, industry regulation, national security and more. However, it indicates that innovation is likely to come from a broader group of players. China's recent market rally is narrowly focused; policy support is still required to address its deflationary challenges, to drive a broader, sustainable earnings recovery. Demand-side policy support and signs of a more market-friendly policy shift towards technology companies are encouraging but much more is needed to shore up confidence in consumers and investors, as well as in the private sector.

## Asset Class Summary Views

Views expressed reflect CIO team expectations on asset class returns and risks. Traffic lights indicate expected return over a three-to-six-month period relative to long-term observed trends.

Positive	Neutral	Negative
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CIO team opinions draw on AXA IM Macro Research and AXA IM investment team views and are not intended as asset allocation advice.

<b>Rates</b>		Medium-term rate expectations are stable but subject to policy triggered volatility
<b>US Treasuries</b>		Fed on hold until more clarity on inflation and Trump policy; bonds in range
<b>Euro – Core Govt.</b>		Range trading while markets wait for any new policy initiatives on the fiscal side
<b>Euro – Govt Spreads</b>		Spreads to remain narrow; focus on what eventual new German government will do
<b>UK Gilts</b>		Investors unsure about path of inflation and fiscal policy; gilts range bound for now
<b>JGBs</b>		Markets still expect further interest rate hikes
<b>Inflation</b>		Scope for breakeven rates to move higher as inflation continues to be sticky
<b>Credit</b>		Credit remains strong with spreads stable and positive returns
<b>USD Investment Grade</b>		Strong earnings backdrop supportive for US corporate debt
<b>Euro Investment Grade</b>		Demand for fixed income remains strong; fundamentals are solid
<b>GBP Investment Grade</b>		Spreads have narrowed in 2025, but demand remains strong
<b>USD High Yield</b>		Solid economic data, strong cash-flows and technical factors continue to support high yield
<b>Euro High Yield</b>		Resilient fundamentals, technical factors and ECB cuts support total returns
<b>EM Hard Currency</b>		Spreads over US Treasuries are attractive but Trump agenda could be disruptive
<b>Equities</b>		Signs of broadening of performance away from narrow US technology sector leadership
<b>US</b>		Earnings momentum starting to flatten; valuations are still expensive
<b>Europe</b>		Modest pick-up in earnings forecasts and possible beneficiary of global move away from US
<b>UK</b>		Markets need to see how government can improve growth prospects; lower rates will help
<b>Japan</b>		Solid combination of valuations and expected earnings growth
<b>China</b>		Tech sector bolsters investor optimism, with scope to broaden out on policy support
<b>Investment Themes*</b>		Competition in AI to create more opportunities for technology beneficiaries

\*AXA Investment Managers has identified six themes, supported by megatrends, that companies are tapping into which we believe are best placed to navigate the evolving global economy: **Technology & Automation, Connected Consumer, Ageing & Lifestyle, Social Prosperity, Energy Transition, Biodiversity.**

**Data source:** Bloomberg

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