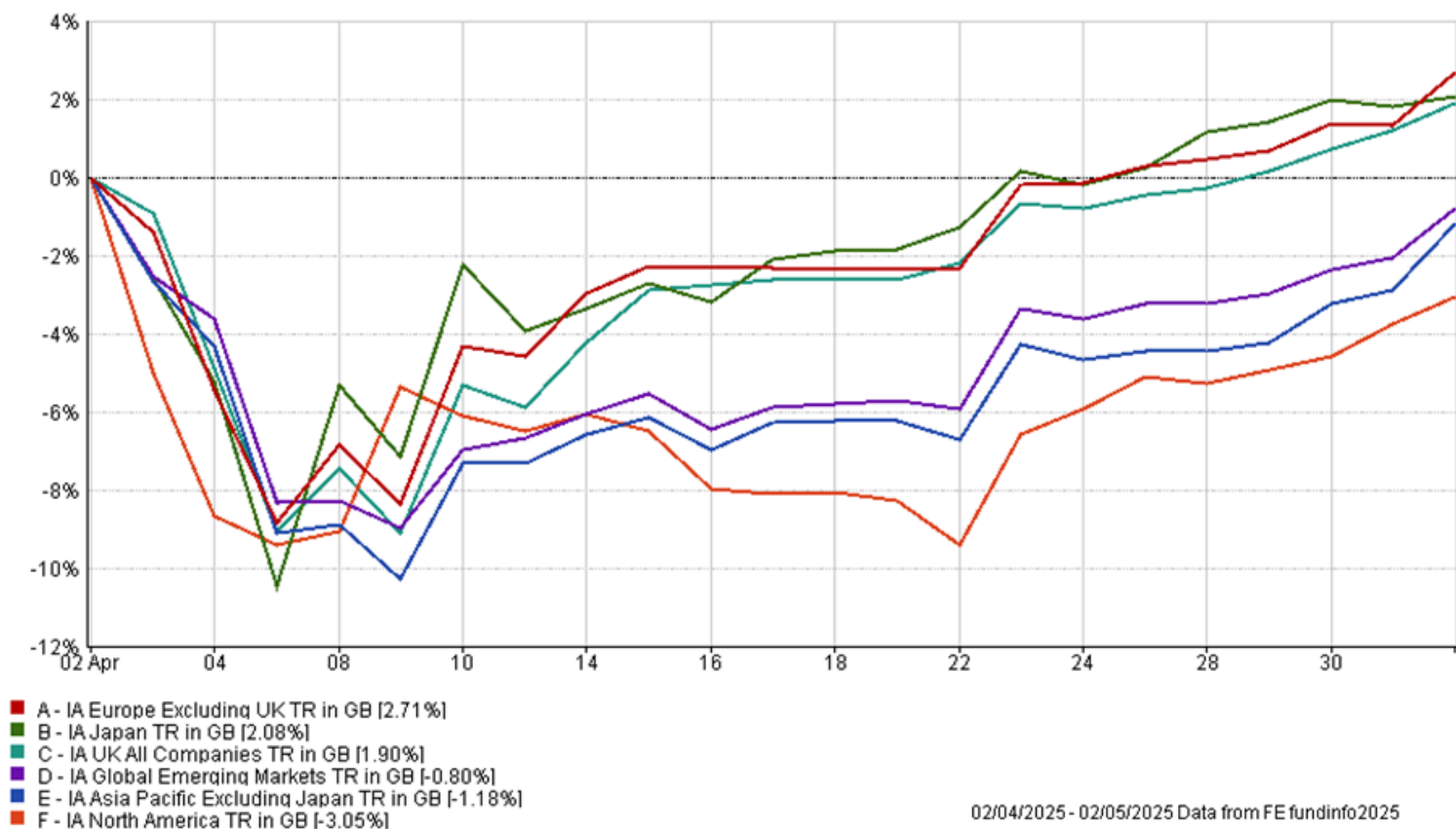


Market Matters - with Tom McGrath

Relief Rally or False Dawn? Markets Search for Direction

Markets staged a solid rebound this week, but beneath the surface, the big question remains: Is this the start of a lasting recovery, or just a pause before the next storm? With earnings propping up sentiment and central banks holding steady, investors are left weighing resilience against rising risks. One month after Liberation Day, many IA sectors are now showing gains, with only North America still showing notable losses.



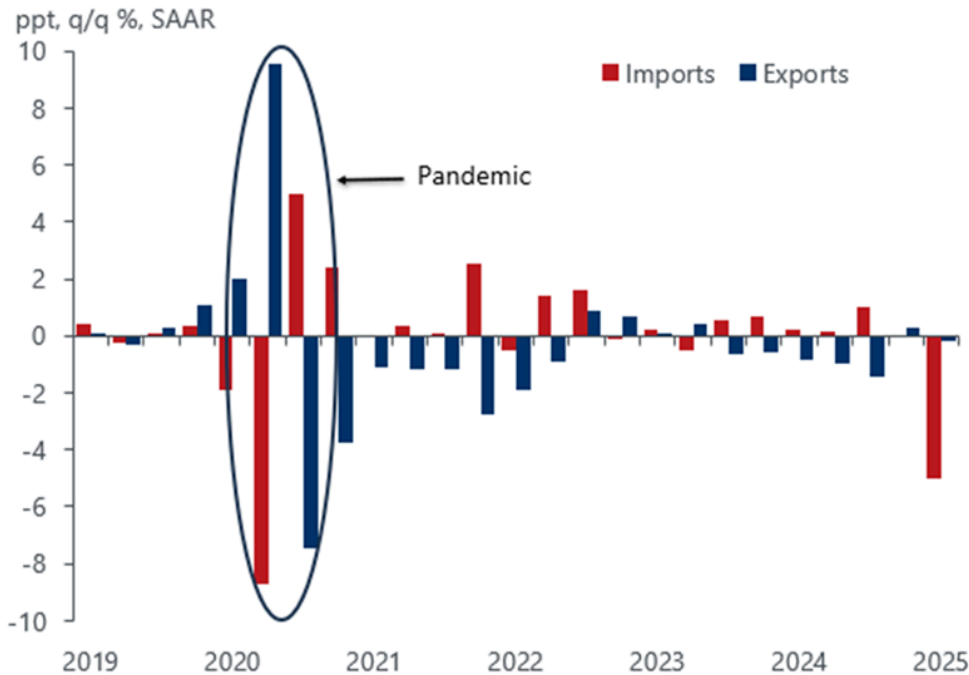
What a difference a bit of quiet can make. Global markets managed a decent week, even as US GDP disappointed and tech earnings were mixed. Investors seem relieved that the White House has toned down the chaos – for now – and hope that Trump’s administration might shift back toward growth-friendly policies rather than more trade disruption. It’s early days, but markets have taken heart from the more measured tone coming out of Washington, helped by the rising influence of Treasury Secretary Scott Bessent, who’s quickly become the market’s favourite ‘grown-up’ in the room.

US economic growth: hit a speed bump in the first quarter, with real GDP slipping by 0.3% on an annualised basis. While a quarterly contraction during an expansion isn’t common, it’s not unprecedented – and crucially, it doesn’t mean the economy has tipped into recession. Interestingly, the GDP figure came in slightly better than feared, largely because of a last-minute adjustment to inventories. That said, the data composition was troubling, with imports acting as a significant drag and effectively tilting the balance of risks to the downside for Q2 growth, where estimates are now edging closer to 2% annualised.

It’s worth remembering that GDP is a backward-looking measure, and there were some encouraging signs under the surface. Real final sales to private domestic purchasers – essentially the core engine of the economy – showed a decent gain, suggesting domestic demand hasn’t rolled over. However, that resilience is being tested in real-time, as the economy now faces a string of shocks: tariffs, supply chain strains, tighter financial conditions, and a steady drumbeat of policy uncertainty. Still, high-frequency data suggests that the economic engine hasn’t stalled heading into Q2.

Looking further, recession risks remain uncomfortably elevated between now and early next year. Some offsets are on the horizon, including deregulation efforts and a fresh round of fiscal stimulus expected later this year, both of which should help cushion growth in 2026. But the dominant risk remains the corrosive effect of uncertainty—the longer it lingers, the more likely it is to trigger a slowdown in business investment, a softening in hiring, and potentially a pick-up in layoffs.

US: Contribution to real GDP

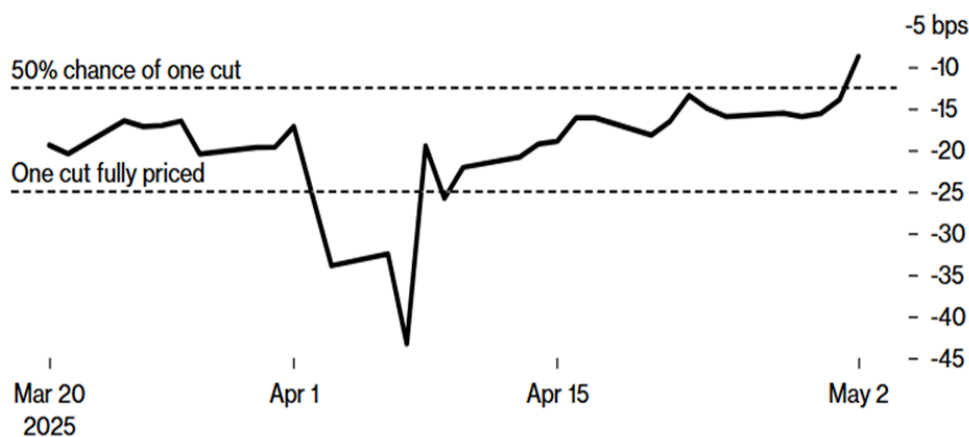


Source Graph: Oxford Economics

The Federal Reserve heads into next week's meeting with markets pulling back on expectations for near-term rate cuts after stronger-than-expected US jobs data. April's nonfarm payrolls rose by 177,000, surprising to the upside and prompting traders to shift bets on the first Fed cut from June to July.

June Fed Rate-Cut Expectations Vanish After Jobs Data

✓ Bets on June Fed rate cut



Source: Bloomberg

Markets are now pricing in around 79 basis points of easing this year, down from roughly 90 earlier in the week. Bond markets reacted swiftly, with two- and five-year Treasury yields posting their biggest two-day jump since October. Resilient jobs and manufacturing data have forced investors to rethink just how quickly the Fed might move, even as confidence surveys signal more caution.

For the Fed, the near-term picture is one of patience — the labour market has yet to show meaningful cracks, and the full economic impact of tariffs and tightening financial conditions is still playing out. With global trade negotiations still in flux and markets pricing in only three cuts by year-end, the Fed's approach remains measured. For now, policymakers are waiting for clearer signals before making their next move — and markets are left adjusting to a slower, more data-dependent path.

Europe & UK: Elsewhere, Europe quietly notched a win. The euro has strengthened even as the ECB moved to cut rates, a sign that capital is rotating out of the US as investors tire of policy gridlock. European equities saw rare outperformance in April, buoyed by hopes of fiscal stimulus and optimism over a possible trade deal with Washington. Germany's push for infrastructure and defence spending has added to the sense of a pro-growth shift across the continent. European bond markets, meanwhile, are reflecting confidence that inflation pressures can be contained without choking off growth, giving the ECB room to keep supporting demand.

The UK is preparing for a widely expected 25 basis point cut this week, bringing Bank Rate to 4.25%. This continues the Bank of England's pattern of easing at alternate meetings, though some on the committee, including Swati Dhingra, may push for a larger move. The real focus is on how the Bank interprets the economic shock from new US tariffs and what that means for the growth and inflation outlook.



Source Graph: Oxford Economics

The Bank is expected to revise near-term growth and inflation forecasts, reflecting the drag from weaker global trade, softer export demand and the squeeze on already subdued business investment. Financial markets have turned decisively more dovish, pricing in additional cuts over the year, giving the Bank scope to hint at a more flexible, possibly faster easing path. The main challenge for policymakers is balancing the negative demand shock from tariffs against stubborn domestic wage pressures. While the Bank has long worried about structural inflation risks, recent signals from Governor Bailey and others suggest the focus is shifting toward downside growth risks. The upcoming meeting will be closely watched not just for the cut itself but for any change in language on the pace of future moves.

While the UK gears up for a rate cut and Europe leans on stimulus hopes, China finds itself grappling with the sharp edge of escalating tariffs. With effective levies now around 145%, Chinese equities have stumbled despite a strong domestic tech rally. Beijing continues to project resilience, but the export engine is under real strain. Most investors expect some easing in tariffs once negotiations progress, though signs of compromise remain scarce.

US Earnings Update: April also marked one of the most jittery periods for US tech stocks since the financial crisis. Markets swung wildly as investors tried to recalibrate around new growth and policy expectations, and the dollar (usually a haven in turbulent times) buckled under the weight of capital outflows – raising uncomfortable questions about its global reserve status. That said, the dollar remains expensive by historical standards, so there may be more room to fall...

Earnings season, meanwhile, has thrown markets a timely lifeline. Around 72% of S&P 500 companies have now reported, with 76% beating EPS estimates – a touch below the five-year average but still enough to keep market nerves in check. Earnings growth has climbed to 12.8%, delivering the second consecutive quarter of double-digit gains, even if revenues have been more subdued at 4.8%. Healthcare, communication services, and tech have done much of the heavy lifting, while energy and industrials have trailed behind. Big tech has largely delivered: Amazon beat on sales but offered cautious guidance, Apple's services revenue hit new highs, though China iPhone sales lagged, Microsoft again leaned on its cloud strength, and Alphabet impressed with AI-fueled cloud gains. For now, earnings have helped steady the ship – but with guidance turning more cautious and analysts already marking down expectations for the rest of the year, the real test is still to come.

The mood remains cautious but not panicked. Investors are hoping that the White House's softer tone sticks, that central banks stay dovish, and that some sort of trade sanity returns before real economic damage sets in. It's a fragile equilibrium, but for now, a relatively quiet Trump has been the best news the markets could ask for.



TOM MCGRATH

Chief Investment Officer & Portfolio Manager