Global
Investment
Research
Market Maps

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QUARTERLY REPORT | **JULY 2025**

Global Wealth Research

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Greater role for Fixed Income, Alternatives, International and Emerging Markets. More diversification opportunities and impact of currency decisions.

Top investment themes

1. High uncertainty and divergence increase volatility and dispersion
2. Greater role for Fixed Income and Alternatives
3. Greater role for non-US markets
4. Potential of Emerging Markets
5. Increased importance of currency hedging and currency returns
6. More diversification opportunities

Macroeconomic Backdrop

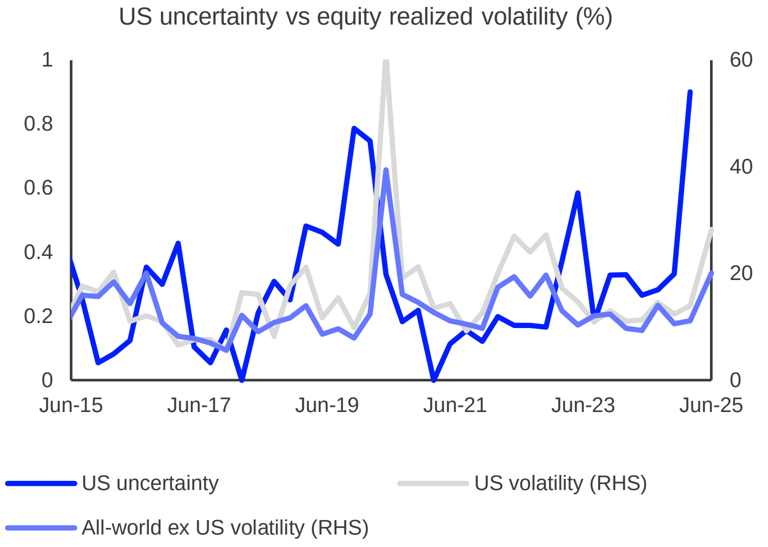
a. Macro divergence and high uncertainty lays the ground for higher dispersion and volatility

- The IMF downgraded 2025 growth forecasts across all major markets in April due to elevated uncertainty and tariff impacts. Inflation vs growth concerns differ between the US and other DMs, leading to divergent central bank paths. Net exports were a major negative contributor to US GDP growth in Q1 but a major positive contributor to other markets.
- Short term inflation expectations have unwound in Q2 globally, helped by lower oil prices, after the Q1 spike due to expectation of higher tariffs.
- Policy uncertainty and the resultant downside risks remain high, creating a backdrop that is conducive to high volatility. US equity 3M rolling volatility spiked as the market reacted to tariff updates – seeing sharp declines first, then followed by the "relief rally".
- Neither the US dollar nor the Treasuries exhibited their usual safe-haven status in the stress period following wide-ranging US policy uncertainty since the start of 2025. The recent US credit rating downgrade was another headwind for the US dollar.

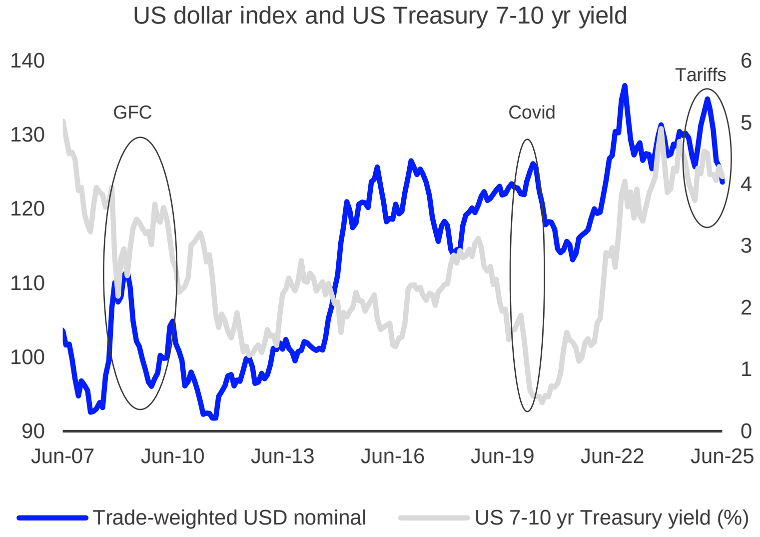
b. Steepening yield curves are now mostly a global phenomenon

- Major G7 20s/2s curves steepened on yield increases in longs (except Germany) and yield declines in shorts (except Canada).
- Higher risk from deteriorating fiscal positions and uncertainty-led increases in term premium are getting priced into DM sovereigns, particularly in the US. Rate cuts are also generally priced in.
- Curve steepening in Japan was driven more by the ultra-long JGB yields, which increased on shocks from both demand (central bank tapering & lower demand from Japanese life insurers) and supply (issuance trim).

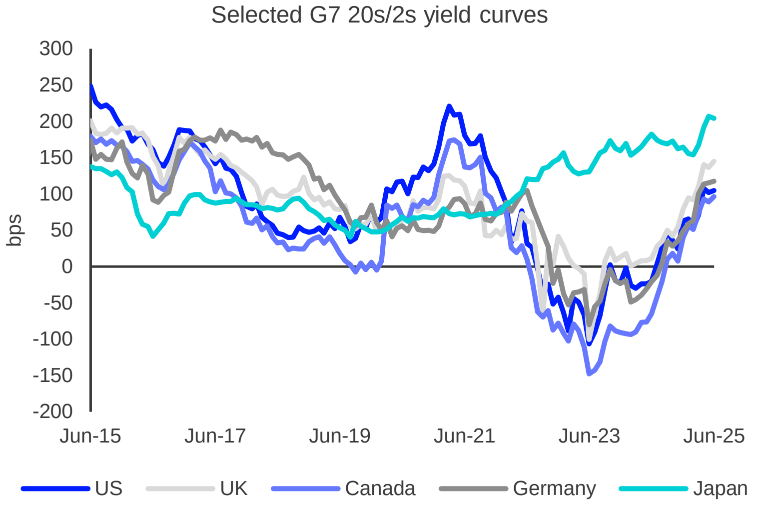
US uncertainty surged to a decade high, in response to changing goods tariffs. Rolling equity volatility picked up more in the US than the rest of the world, but spillover effects are obvious as trade policies matter to partners.



Neither the (weakened) US dollar nor (bearish) Treasuries have proved reliable safe havens on the tariff shock, unlike during GFC or Covid. The double whammy of US debt downgrade and tariffs may have led to this unusual case.



Major G7 20s/2s curves bear steepened over 3M, largely driven by yield increases in longs. JGB curve remains the steepest, despite the outlook of lower supply preventing yields from surging higher.



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A greater role of non-equity assets (Fixed Income & Alternatives) in multi-asset portfolios, implied by improving total return and return/risk ratio

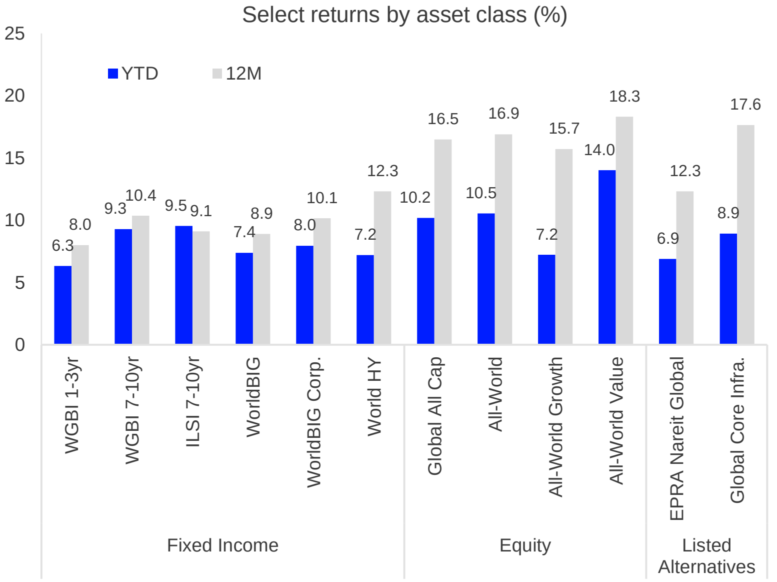
– YTD, fixed income delivered returns comparable to other asset classes. Conventional government bonds (WGBI) posted returns of 7.3%; IG corporate gained 8%, while HY corporate returned 7.2%. Alternatives delivered returns of 6.9-8.9%. These returns were not far behind those of Equities (up 10.5%). The return gap between Fixed Income and Equity narrowed YTD 2025 vs 12M, reinforcing their comparative advantage over equities.

– Fixed Income consistently provided relatively high income yield, which is demanded by asset-liability management and income investors.

– Infrastructure delivered higher returns than Equity in 1Y (17.6% vs 16.9%), while offering high income yield (3.4%) close to FI (3.8%).

– Gold, Fixed Income High Yield Bonds and Infrastructure delivered risk-adjusted returns higher than (or comparable to) equities over 1Y. Within the top 10 performers; Infrastructure, World BIG Corporate and US Inflation-linked (both fixed income) were new to the list over 1Y vs 3Y, while Russell 1000 and FTSE 250 fell out of the list. FTSE 100/ Japan/ Emerging/ Developed Europe ex UK stayed in the top 10. Gold outperformance (total return of 42% over 12M) benefitted from cyclical demand, due to uncertainty and structural demand from central bank buying.

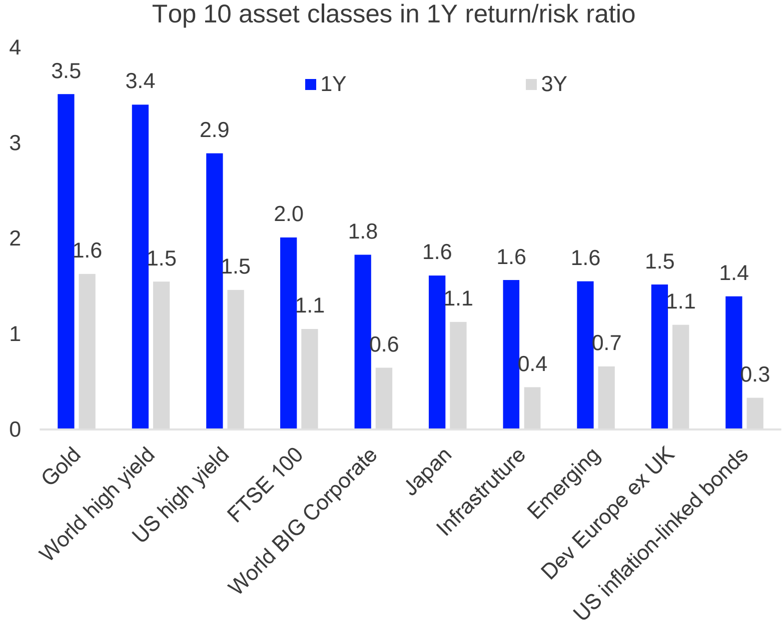
YTD, Fixed Income (both government and corporate bonds) and Alternatives (particularly Infrastructure) posted healthy returns that were comparable to Equity returns.



Over 1Y, Infrastructure (17.6%) delivered remarkable total returns that are higher than the broad Equity (16.9%); Real estate (12.3%) also caught up quickly over 1Y. This is in stark contrast to Equity's strong leadership over 3Y.

1Y Annualised	Income Yield %	Return/Risk	Risk	Total Return %
Equity	19	17	9.8	16.9
Fixed Income	3.8	14	6.3	8.9
Commodities	--	0.7	10.6	7.2
Real Estate	4.0	10	12.8	12.3
Infrastructure	3.4	16	11.3	17.6
3Y Annualised	**Income Yield %**	**Return/Risk**	**Risk**	**Total Return %**
Equity	2.1	12	14.4	17.8
Fixed Income	3.9	0.3	8.6	2.9
Commodities	--	0.5	10.9	5.5
Real Estate	4.2	0.2	17.9	4.2
Infrastructure	3.4	0.4	14.8	6.6

Gold, World HY and US HY registered the top three risk-adjusted returns over both 1Y and 3Y. Infrastructure was one of the top 10 over 1Y vs the bottom over 3Y, as was US inflation-linked. Russell 1000 dropped out of the list.



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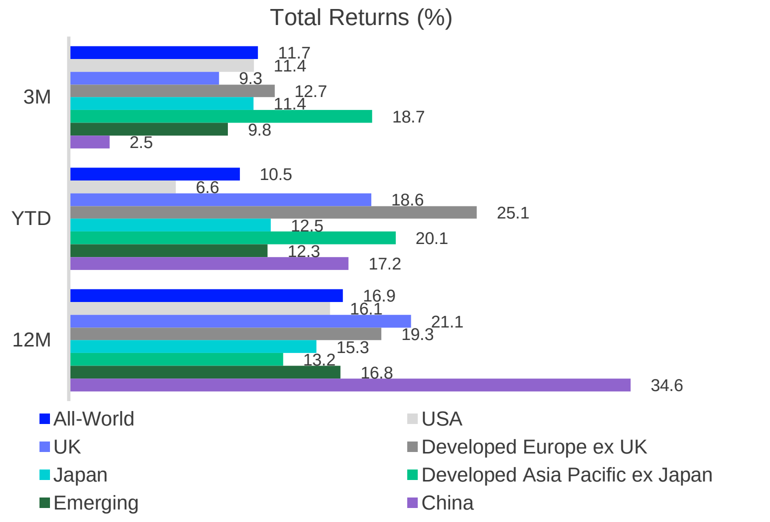
Greater attraction of international markets across Equities and Fixed Income

a. Higher Non-US returns in both equity and fixed income

- YTD, Developed Europe (25.1%), Developed APAC ex Japan (20.1%), and the UK (18.6%) were the top equity performers. The US (6.6%) has underperformed, reflecting a tariff-driven retreat. This is a significant reversal of its role as the best performing equity market during the GFC-2024 era.
- Earnings growth forecast has stayed higher in other DMs than the US since 23/Q4, adding downside risk to US equity.
- US underperformance was seen in FI, too. US IG gained 4.1% YTD, underperforming Euro IG 15.5%. US HY was up by 4.5% vs Euro HY 16.3%. EM credit returns matched the US.

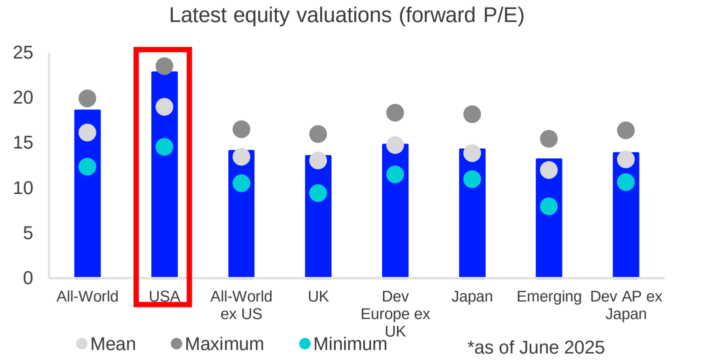
YTD, US equity has underperformed the FTSE All-World, while Developed Europe, the UK, Dev APAC, and China have outperformed.

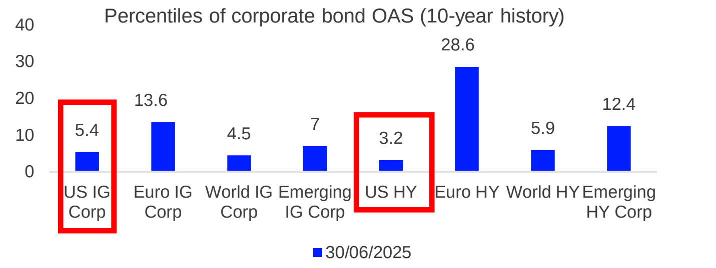


b. Lower valuations in non-US markets

- Although US valuations expanded the least YTD, they remain the most stretched and are near 10-year highs, while other developed markets, including Japan, Europe and the UK, are only slightly above their 10-year means.
- Similarly in credit, US corporate bond valuations are higher than Euro and EM bonds, for both IG and HY, indicated by option-adjusted spreads being at a lower percentile.
- Valuations in both equity and fixed income indicate downside risk is higher in the US than elsewhere.

Although stretched valuations are seen globally in both FI and Equity, they are more significant for the US than peers.

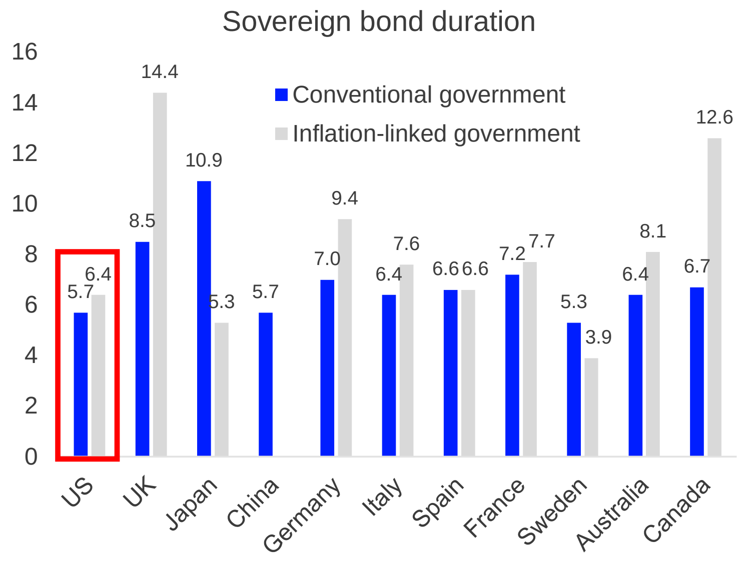




c. Non-US markets have a duration tailwind

- The US Fed is in no rush to cut further, given its inflation and growth tradeoff. As a result, the Fed has lagged the ECB and other major central banks in easing.
- Even when the Fed eases, US Treasuries have lower durations than other sovereign bonds generally, for both conventional and inflation-linked bonds.
- In a falling interest rate cycle, higher duration could provide more tailwind for non-US sovereign bonds than for the US.

US Treasuries have a shorter modified duration than most other major sovereigns, implying less sensitivity to interest rate moves.



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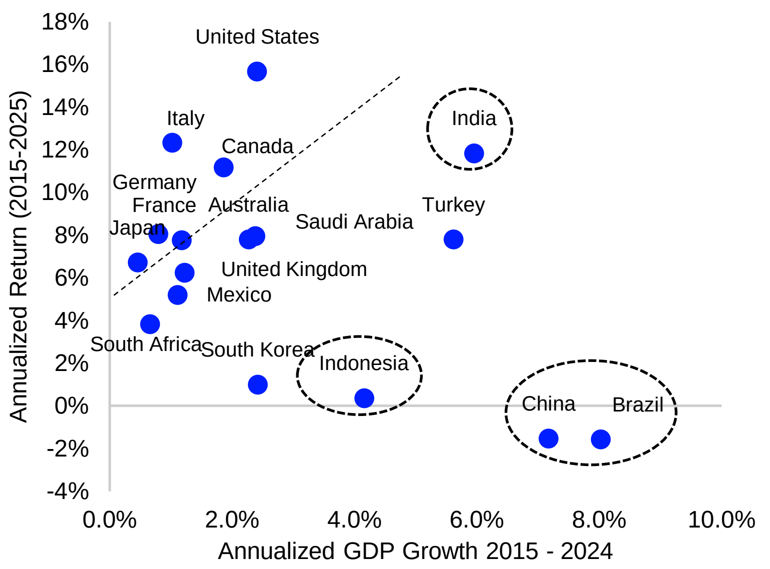
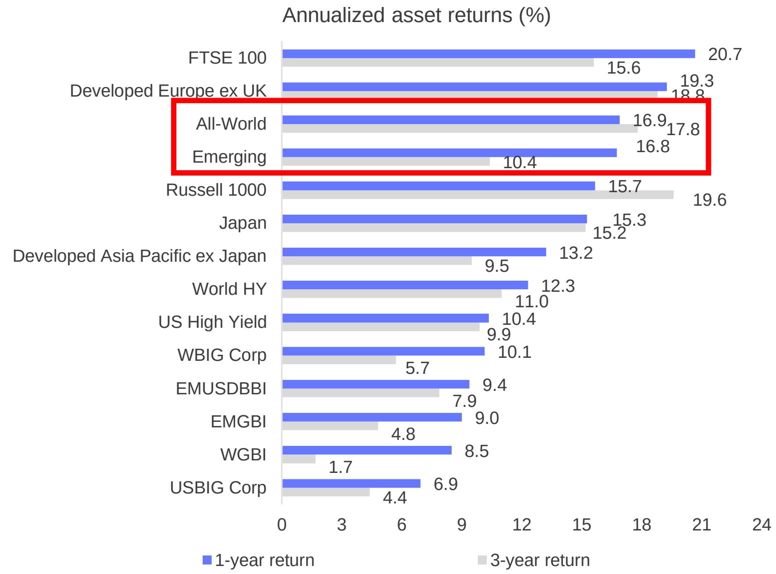
Potential of Emerging Markets – EM equity may be undervalued relative to growth, while sovereign spreads signal lower and well-priced country risk

- Correlations between GDP growth and equity returns show EM equities undervalued relative to the economic growth. Given that IMF forecasts show EMs are expected to outgrow DMs at an increasing rate post-2026, EM equities have a potential for up-rating.
- EM 7-10-year government bond spreads vs the US have been on a downward trend since the spike at the height of the Covid easing in early 2020. Spread tightening were helped by Fed's rate hikes since 2022, and are now near multi-year low, a sign that financial markets acknowledge greater resilience in EM sovereigns.
- The positive correlation between EM government bond yield and exchange change volatility may indicate that FX volatility risk premium is now generally priced in EM government bond yields .
- EM equities recently have become better diversifiers to portfolio, as their correlations with major equity and fixed income sleeves dropped by 0.2 - 0.5 over 1Y vs 3Y. EM equities 1Y correlations to Russell 1000 and All-World fell to 0.22 (from 0.52 over 3Y) and 0.42 (from 0.68 over 3Y), respectively. EM equities 1Y correlations to US IG corporate and US Treasuries 7-10-year fell to 0.43 and 0.33.

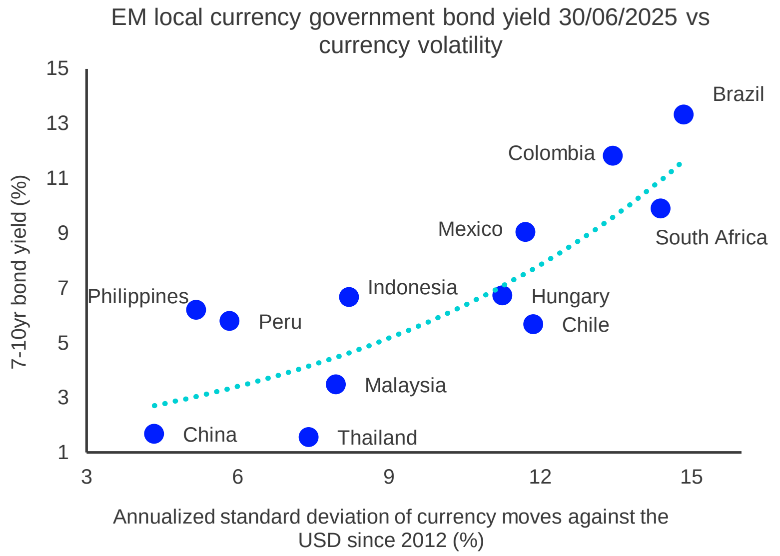
Over 10Y, equity returns have aligned with GDP growth in DMs but not in EMs. Combined with IMF forecasts that EMs outgrow DMs at an increasing rate post-2026, both suggest structural tailwinds to EM equities.



EM equity shows up among the top performers over 1Y (16.8%), majorly driven by China, on par with global equities. This contrasts EM equity performance lagging behind global equities over 3Y (EM 10.4% vs All-world 17.8%).



EM local currency government bond yields as of end-June show a positive correlation with exchange rate volatility, indicating EM LCY yields price in the risk of currency volatility.



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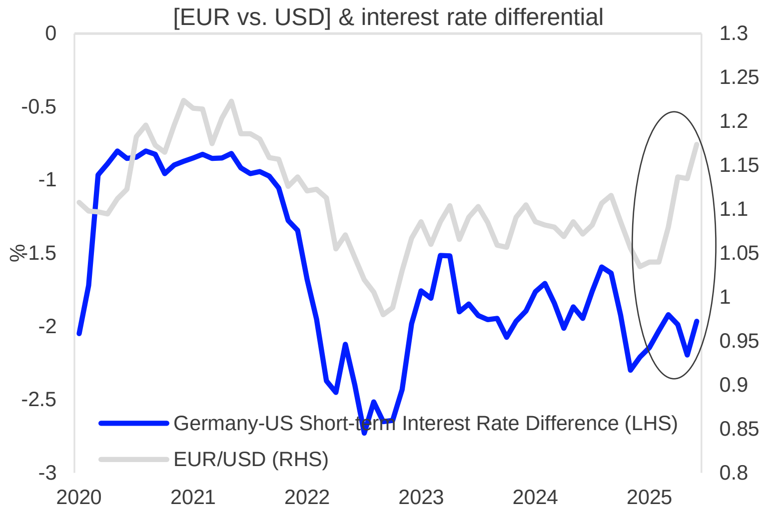
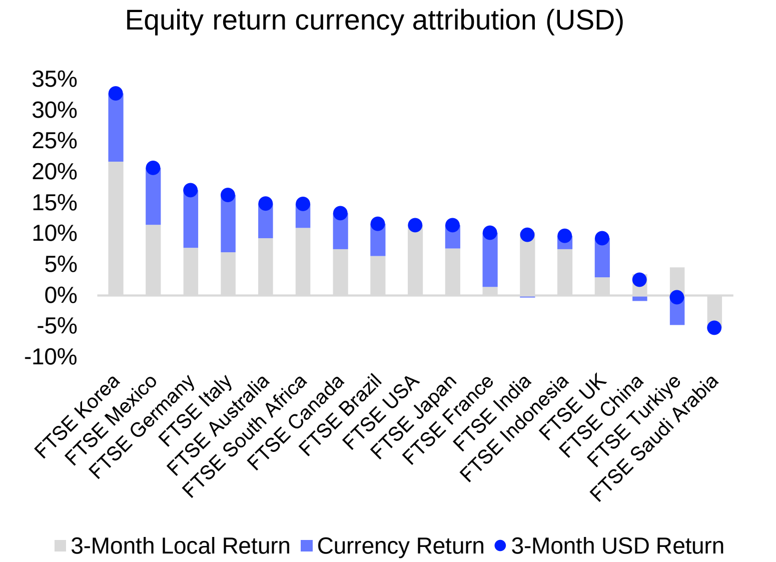
Currency moves much greater than rate differentials would suggest, and unusual US dollar performance increases the importance of currency hedging

- US debt downgrade and tariff shock helped fuel US dollar weakness. The USD failed to serve as a safe-haven currency during recent high uncertainty and volatility.
- Over 3M and YTD, many currencies strengthened vs the US dollar more than implied by rate differentials, for both DM currencies like the Euro and sterling, and EM currencies like the Mexican peso.
- But in Japan, interest rate differential maintains a positive correlation with the JPY/USD, as diverging monetary policies remain a key driver of the Japan-US spread.
- 3M currency movements account for a large share of total returns in US dollar, for both equity and major corporate bond markets.
- A relatively high weight of currency return raises the importance of portfolio hedging decisions.

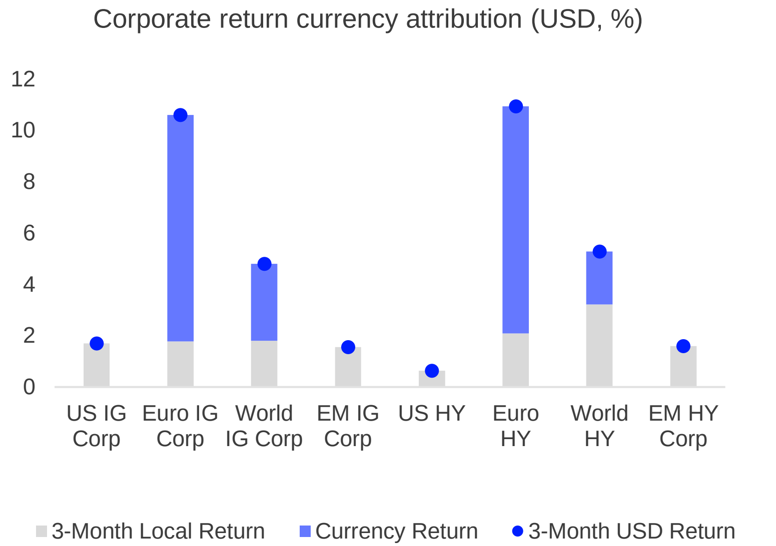
The Euro gained 13.4% vs USD YTD, only behind SEK/CHF and more than the rate differentials would imply. The recent rally has been driven more by factors such as safe-haven demand, the economic outlook and government debt plans.



3M return breakdowns for G20 equity markets show a notable impact of currency returns on total returns for USD investors. Korean won, Euro, Mexican peso, and sterling led currency gains vs the US dollar, amplifying USD returns.



Same trend in fixed income markets. Euro bonds significantly outpaced global peers in USD terms, but most returns were from gains in Euro. Local currency returns were much closer across US/ EU/ EM, or almost on par in IG.



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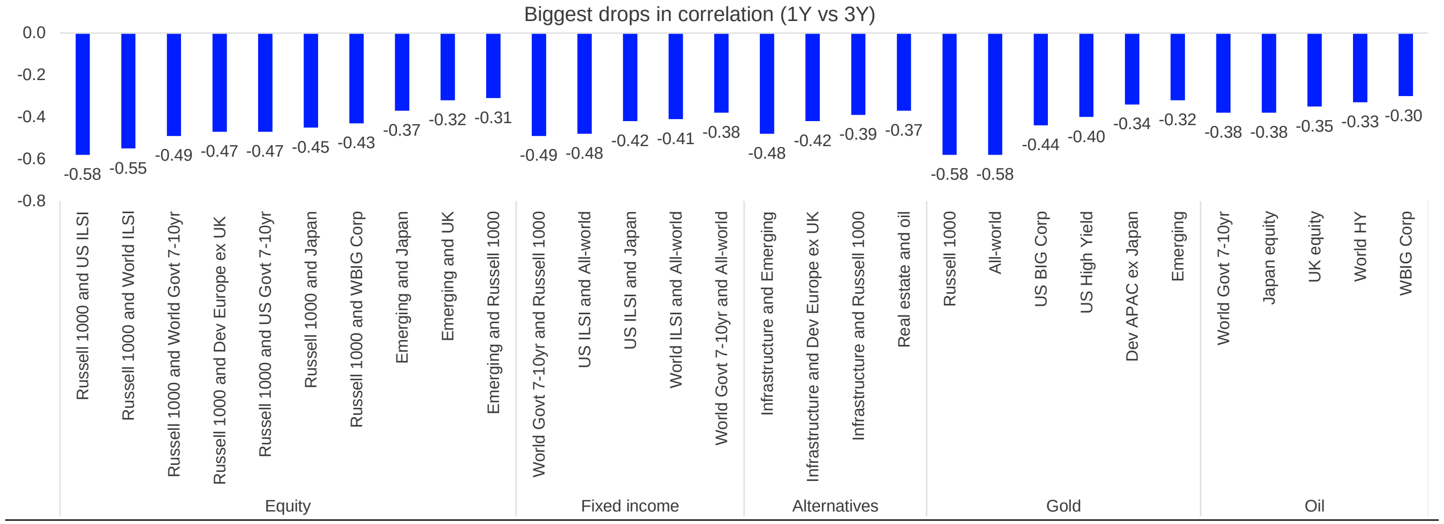
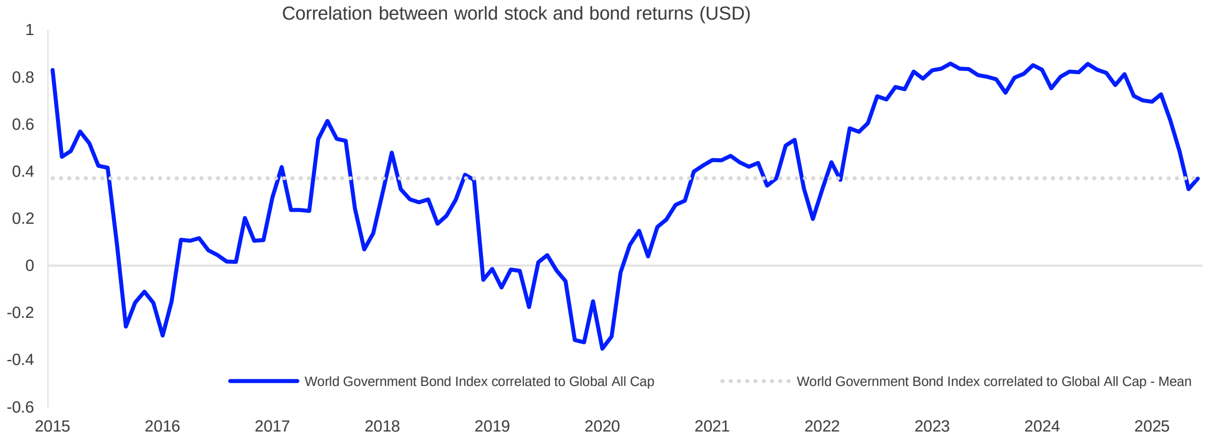
Greater diversification opportunities

Differences between 1Y and 3Y correlations show significant declines for almost all asset classes, as de-globalization picked up. US equities decoupled from international markets. Commodities correlations with stocks and bonds also dropped.



Correlation between stock and bond returns has just fallen back to the 10-year average, after staying above the mean for more than 4 years. A relatively high correlation has been the new normal, in contrast to the below-average correlation between 2015 and 2020.



a. Decoupling among asset classes increases diversification opportunities

- The declines in correlation were more broad-based and significant in Equity than Fixed Income, as US equities decoupled the most.
- EM equity correlation dropped the most with Infrastructure (-0.48); correlation with other equities fell by ~0.1 - 0.4. Lower correlations signal higher diversification benefit of EM equities.
- Commodity correlations with both equity and fixed income decreased, including gold and oil.

b. Mean-reverting stock – bond correlation brings back 60/40 portfolio diversification benefit

- Stock and bond correlation fell sharply recently, as markets responded to higher US tariffs, after years of near 0.8 correlation. The latest correlation is near the 10-year average of 0.37, but still higher than the trough seen in previous periods of crisis, like Covid-19 and volatile global equity market in 2015-16, when correlations were negative.
- Both policy uncertainty and historical trend imply there may be room for the correlation to fall further from here. A lower correlation between stock and bond returns is welcome in a 60/40 portfolio, providing diversification opportunities.

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Appendix: List of indices used in report

Name	Mnemonic/Code	Name	Mnemonic/Code
US Treasury 1-3yr	US_TSY1-3	Russell 1000 Index	R1000
US Treasury 7-10yr	US_TSY7-10	Russell 2000 Index	R2000
US Treasury 20yr+	US_TSY20+	FTSE Global All Cap Index	GEISLMS
UK government 1-3yr	GB_TSY1-3	FTSE USA Index	WIUSA
UK government 20yr+	GB_TSY20+	FTSE UK Index	WIGBR
Canada government 1-3yr	CA_TSY1-3	FTSE Developed Europe ex UK Index	AWDEXUKS
Canada government 20yr+	CA_TSY20+	FTSE Emerging Index	AWALLE
Germany government 1-3yr	DE_TSY1-3	FTSE All-World Index	AWORLDS
Germany government 20yr+	DE_TSY20+	FTSE Global Core Infrastructure Index	FGCII
Japan government 1-3yr	JP_TSY1-3	FTSE USA All Cap Index	LMSUSA
Japan government 20yr+	JP_TSY20+	FTSE All-World ex US Index	AWXUSAS
FTSE World Government Bond Index	WGBI	FTSE/CoreCommodity CRB® Index	RJEFCRT
FTSE World Government Bond Index 1-3yr	WGBI_1-3	FTSE Australia	WIAUS
FTSE World Government Bond Index 7-10yr	WGBI_7-10	FTSE Brazil	WIBRA
FTSE World Inflation-Linked Securities Index 7-10yr	ILSI_7-10	FTSE Canada	WICAN
World Broad Investment-Grade Bond Index Corporate	WBIG_CORP	FTSE China	WICHN
US Broad Investment-Grade Bond Index Corporate	BIG_CORP	FTSE France	WIFRA
Euro Broad Investment-Grade Bond Index Corporate	EBIG_CORP	FTSE Germany	WIDEU
Emerging Markets US Dollar Broad Bond Index Corporate – Investment-Grade	EMBBI_CORP_IG	FTSE India	WIIND
Emerging Markets US Dollar Government Bond Index	ESBI	FTSE Indonesia	WIIDN
US High-Yield Market Index	HY_MKT_US	FTSE Italy	WIITA
Pan-European High-Yield Bond Index - EUR	EUROPE_HYM_EUR	FTSE Japan	WIJPN
Emerging Markets US Dollar Broad Bond Index Corporate – High-Yield	EMBBI_CORP_HY	FTSE Korea	WIKOR
US Inflation-Linked Securities Index	ILSI_US	FTSE Mexico	WIMEX
FTSE World High-Yield Bond Index	WHYM	FTSE Saudi Arabia	WISAU
US Treasury	US_TSY	FTSE South Africa	WIZAF
UK government bond	GB_TSY	FTSE Turkiye	WITUR
Japan government bond	JP_TSY	US Economic Policy Uncertainty Index	USEPUPOLR
China government bond	CN_TSY	FTSE EPRA Nareit Global	ENHG
Germany government bond	DE_TSY	US Trade Policy Uncertainty Index	USEPTRPUR
Italy government bond	IT_TSY	Gold	GOLDBLN
Spain government bond	ES_TSY	Global Economic Policy Uncertainty	WDEPUCUPR
France government bond	FR_TSY	Nominal Trade Weighted USD	USCXTW..F
Sweden government bond	SE_TSY		
Australia government bond	AU_TSY		
Canada government bond	CA_TSY		
FTSE Emerging Markets Government Bond Index	EMGBI		

For more details regarding Index Construction for these and related FTSE Russell indices, and for ETFs and Mutual Funds linked to these FTSE Russell Indices, please reach out to your FTSE Russell Sales contact.

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