Allianz Global Investors

05/2025

Market Snapshot

Equity Snapshot

United States

It was a stellar month for US equities, with stocks recouping previous losses on a consensus-beating first-quarter corporate earnings season and optimism around easing trade tensions. Markets were briefly buffeted after President Trump threatened the European Union with 50% tariffs and on the announcement of his 'big, beautiful' bill, which extends many tax cuts made during the president's first term in office and is expected to increase the US debt burden by over USD 3 trillion of US debt in the next decade. Sentiment was further dampened after credit rating agency Moody's consequently stripped the US sovereign of its AAA rating, citing the growing fiscal deficit. However, the risk-on mood prevailed for most of the month and growth stocks outperformed their value equivalents.

Recessionary fears eased, with the Federal Reserve Bank of Atlanta's GDPNow running estimate signalling growth of 2.2% for the current quarter. The flash S&P Global US composite purchasing managers' index rose from a final reading of 50.6 in April to 52.1 in May, reflecting improvements in both services and manufacturing activity. The Federal Reserve kept benchmark lending rates on hold at 4.25% to 4.5%, with officials citing continued economic uncertainty inflationary risks.

In other data releases, headline inflation in the US unexpectedly fell to 2.3% in April, while core inflation (excluding volatile food and energy costs) remained unchanged at 2.8%. US retail sales grew by a lacklustre 0.1% in April, compared with an upwardly revised 1.7% gain in March. Non-farm payrolls rose by a seasonally adjusted 177,000 in April, slightly below the downwardly revised 185,000 in March, but well ahead of consensus estimates. Similarly, the unemployment rate remained at 4.2%, as expected, indicating that the US labour market is relatively stable, while wage growth was slightly less than forecast.

Europe

European equities moved higher in May, with defence names leading the way amid faltering hopes of a ceasefire in Ukraine. Having sold off sharply mid-month after President Donald Trump threatened to slap 50% tariffs on all of the bloc's exports to the US from 1 June, European markets rebounded on news that Trump had delayed implementation until 9 July to allow more time for negotiations. At a sector level, information technology and industrials stocks were the strongest performers amid a slew of positive earnings releases. Health care stocks brought up the rear, but still managed a modest positive return during the month.

In its Spring Forecast, the European Commission slashed its GDP growth outlook for the euro zone on the back of heightened macro uncertainty and trade tensions. The bloc's economy is now expected to grow by 0.9% this year and 1.4% in 2026, down from previous forecasts of 1.3% and 1.6% respectively. Data for May demonstrated that the euro zone is falling back into stagnation, with the flash estimate of the HCOB euro-zone composite purchasing managers' index (PMI) unexpectedly dipping into contractionary territory, falling to 49.5 from 50.4 in April (above 50 signifies growth). This was largely due to a slowdown in services activity, which has long been the bloc's main growth driver. Inflation in the euro zone held steady at 2.2% in April, defying consensus expectations of a slowdown.

Asia

Asia ex Japan equities delivered strong returns in May, with many Asian currencies appreciating significantly against the US dollar over the month. The tech-heavy markets of Taiwan and Korea led the way, buoyed both by a recovery in global tech sentiment as well as currency gains. China equities also gained initially following indications of a tariff truce with the US, before giving way to profit taking in the second half of the month. ASEAN equities also rallied, with Indonesia leading the way in a strong month for net foreign inflows. Indian equities finished the month moderately higher. Investor sentiment was boosted by a number of positive developments that included a 'landmark' free trade agreement with the UK, a strong GDP growth print of 7.4% year on year in Q1 2025 (up from 6.4% in the previous quarter), continued foreign investor inflows, and easing inflation data.

Bond

Global bonds had a volatile month in May, driven by uncertainty around tariff policies and their impact on growth. 10-year US Treasury yields peaked at 4.6% before easing to 4.4% at the end of the month, ending 24 bps higher compared to April. Yields spiked initially as Moody's downgraded US's sovereign rating to Aa1 from Aaa, reflecting the increase in government debt which raised fiscal concerns. The 10-year Treasury yields then ended lower from softer than expected inflation data which gave hope to Federal Reserve rate cut bets down the road in 2H 2025. Corporate bonds performed better as credit spreads tightened, with high yield experiencing more compression in comparison to investment grade.

In Europe, bonds also declined, where 10-year bond yields peaked at 2.7% before ending the month higher at 2.5% by 6 bps on the back of President Trump's threat of a 50% tariff on the European Union. Yields came down at the later end of the month after the US President delayed the deadline for implementing his tariff to July 9 from June 1. Similarly, Japanese treasuries fell sharply, where 10-year yields rose by 18 bps to 1.5% after an auction of long-dated Japanese government bonds drew the weakest demand in nearly a year. The poor investor demand is part of a broader trend that reflects concern over fiscal deficits in major economies such as the US and Japan. In China, bonds also sold off, with 10-year yields rising by 8 bps to 1.7% on the back of draining liquidity in the money market as the People's Bank of China sought to stabilize its currency.

Outlook

Equity markets gained ground in May as sentiment improved and volatility eased, supported by a broad-based earnings season that concluded better than expected across most regions. In Europe, nearly all companies have now reported, with earnings surprising to the upside and sales growth tracking well above consensus, even in formerly challenged sectors such as Medtech and Industrials. Importantly, Growth stocks outperformed Value, marking a possible turning point for the style, helped by a more risk-on environment and early signs of a more accommodative stance from central banks.

Globally, investor attention remained focused on tariff dynamics and the implications of a "China for China" manufacturing strategy, but the mood was far less reactive than in April. Companies across our portfolios are actively adjusting supply chains, refining sourcing strategies, and in many cases, finding opportunities to reinforce their competitive positioning.

In semiconductors, we are seeing early signs of inventory normalisation and a reacceleration of end-market demand, particularly helpful in analog semiconductors where we have exposure via Microchip. This area of the market has significantly lagged their leading-edge peers. Artificial Intelligence (AI) infrastructure remains an important area of investment where our companies including Nvidia, ASML Holding and Amphenol are well positioned. Meanwhile, many US

Industrials (or European with US exposure) continue to benefit from structural tailwinds in data centres, automation, and energy efficiency.

At a time when style and geopolitical factors remain volatile, we continue to favour companies with high returns on capital, recurring revenues, pricing power, and strong balance sheets. These traits have proved decisive again this month, as operational resilience helped insulate many of our holdings from cyclical pressure. Valuations across Quality Growth remain supportive, with a number of our holdings still trading below historical averages, particularly in Europe.

Many listed companies are now more subdued about their business outlooks, and analysts have been revising their earnings estimates downwards. As the macro backdrop stabilises and tariff concerns begin to fade into the background, we believe the stage is set for high-quality global equities to continue compounding through market noise and deliver attractive long-term returns. In this environment, we may see our relatively more resilient companies shine with Q2 earnings season ahead being a valid first test.

Source: Allianz Global Investors, as of 31 May 2025 unless otherwise stated.

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