

September 2025

Interest rates & bonds

Rate cut by the Fed in September likely

	10-year government bond yield			Investment-grade credit spread		
	Current	Aug. 2025*	Year-to-date*	Current	Aug. 2025*	Year-to-date*
US	4.2%	-16 bps	-35 bps	77 bps	1 bps	-3 bps
Eurozone	2.7%	-1 bps	32 bps	84 bps	5 bps	-18 bps
UK	4.7%	13 bps	14 bps	92 bps	-1 bps	-4 bps
CH	0.2%	-9 bps	-3 bps	72 bps	0 bps	3 bps

10-year government bond yield eurozone = DE, bps = basis points.

* Change as at 28 August. Source: Bloomberg

USA

- USD credit spreads in investment grade (IG) and high yield (HY) tightened in August. After US government bond yields increased across the curve in July, they saw a renewed decrease in August.
- After Fed Chair Powell's speech in Jackson Hole, a policy rate cut in September is likely. The political pressure on the Fed is also evident. We continue to expect three rate cuts for the remainder of 2025.

Eurozone

- After the tightening in July, IG and HY spreads widened in August. 10-year Bund yields increased and the risk premium on 10-year French government bonds rose due to negative political headlines.
- As the ECB has signalled no willingness to cut its policy rate, we have removed our expectation for a September rate cut and now expect the ECB to remain on hold for the remainder of 2025.

UK

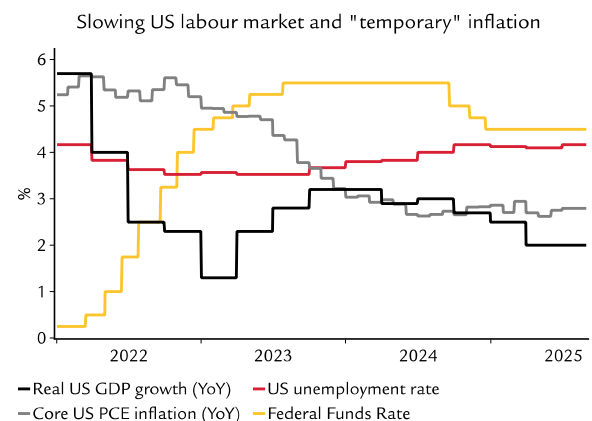
- IG credit spreads in the UK tightened slightly and rates continued to increase last month.
- After a hawkish policy rate cut in August, coupled with near-term inflation concerns, we now expect only one additional rate cut by year-end, down from two previously.

Switzerland

- IG spreads remained stable and 10-year Swiss government bond yield declined slightly in August.
- At this juncture, we believe the SNB has no need to act further and will likely maintain its current policy rate of 0% for the rest of the year.

Next rate cut by the Fed expected on 17 September

In August 2024, the so-called “Sahm Rule” signalled the start of a US recession as unemployment had risen significantly. This was followed by the Fed delivering 100 bps in pre-emptive “insurance” rate cuts. We note that, compared to a year ago, (1) US tariffs have led to higher market inflation expectations (e.g., the 10-year USD inflation swap trades at around 2.6%), and (2) there has been a slowdown in GDP growth and a gradual deterioration in the labour market. Fed Chair Powell's comments at the Jackson Hole symposium on 22 August have opened the door to a potential rate cut on 17 September. Powell considers the “reasonable base case” to be that tariff-related inflation is transitory. He acknowledged uncertainty around the timing and magnitude but also said that it will take time for inflation to return to target from the tariff shock. This suggests that the Fed might be forgiving regarding near-term inflation overshoots. The weaker economic and labour market momentum that we forecast should thus push the Fed to a series of policy rate cuts. We therefore also expect lower US government bond yields in September but remain neutral for eurozone rates. For Switzerland, our view is neutral for 2-year rates and lower for 10-year rates. Regarding credit, we expect a weaker technical picture in September due to the reopening of primary markets amid very tight credit spreads. Therefore, we anticipate wider spreads in both IG and HY and both in EUR and USD.



Sources: Bloomberg, Macrobond, Swiss Life Asset Managers. Last data point: 28/08/2025

Equities

Strong earnings, mixed outlook

Regional equity markets	Aug. 2025*	Year-to-date*
USA	2.2%	10.9%
Eurozone	1.1%	15.2%
UK	2.2%	16.4%
Switzerland	3.0%	7.9%
Emerging markets	2.1%	20.0%

MSCI net total return indices in local currency.
* Performance as at 28 August. Source: Bloomberg

USA

- After a weak start to the month and a brief correction mid-month, the US market delivered another strong performance in August.
- Key positives were the earnings season (see text on the right-hand side) and Fed Chair Powell's speech in Jackson Hole, which indicated that rate cuts may be forthcoming and that the Fed will place greater emphasis on the labour market going forward.
- The US market is very expensive; in particular, technology stocks are, on average, overvalued. Current and expected future AI investments are extremely high, and some prominent observers have warned about excessive optimism regarding AI. At present, it is estimated that 95% of users do not generate profits from their AI projects.

Eurozone

- European stocks underperformed in August due to several weak days towards the end of the month. The earnings season was better than expected.
- Valuations in the European market have increased and now exceed historical averages.

UK

- The UK market outperformed the eurozone markets slightly, as it still benefits from a low valuation.

Switzerland

- After several weak months, the Swiss market outperformed in August. Several large companies such as Nestlé, Novartis and UBS achieved returns of 5% or more.
- Swiss stock valuations are higher than in Europe, but lower than in the US.

Emerging markets

- Emerging markets have been strong and are now up more than 18% in USD terms year-to-date. The Chinese stock market has reached a ten-year high, while India continues to underperform.
- The market as a whole is fairly valued.

Earnings season wrap up and market view

The earnings season for Q2/2025 ended with strong results. In the US, earnings growth relative to Q2/2024 was 11%, 8% above expectations. Sales grew by 6%, 2% above expectations (see table). More than 80% of the companies exceeded expectations. In Europe, earnings and sales growth was much lower, but still ahead of expectations. In emerging markets, sales growth was very strong and exceeded earnings growth. These results are quite remarkable given the high uncertainty and the effects from US tariffs. How is this possible? The answer is that expectations were significantly lowered prior to the earnings season. For the current reporting period, US estimates in the 220 days preceding the earnings season were reduced by around 10%, which closely matches the observed earnings beat.

Summary of the earnings season

Region	Earnings Growth	Sales Growth	Earnings Surprise	Sales Surprise
USA	11.0%	5.9%	8.2%	2.2%
Eurozone	3.7%	-2.0%	5.7%	-1.5%
Switzerland	6.3%	-1.4%	6.3%	-1.4%
Emerging markets	5.8%	7.6%		2.5%

Change as at 28. August. Sales surprises for EM is not reliable.
Sources: Swiss Life Asset Managers, Bloomberg.

The question is what comes next and what could lead to further gains for the remainder of the year, or what could derail markets? On the positive side, markets currently expect the Fed to deliver a series of rate cuts. The current market-implied probability for a cut in September is around 85%. The start of an easing cycle is generally positive for markets, especially if not accompanied by a recession. We attach a fairly low probability to a recession scenario. Another positive could be the Q3 earnings season, starting in October. There are, however, also a number of negative factors. First, the market may overprice the extent of monetary policy easing, as US inflation is rising and above the Fed's target level and the tariff effects will only kick in fully in the coming months. Second, key economic indicators such as labour market developments indicate a slowing economy. US stocks are very expensive, and the market recovery since April has been driven again mainly by the big tech stocks. In addition, unprofitable tech stocks and all AI-related stocks saw an enormous rally and the valuations of these stocks resemble the situation in 2000. We believe that negative forces are becoming stronger and we are thus becoming more cautious on equities for the upcoming month.

Currencies

USD still in a confidence crisis

	Aug. 2025*	Year-to-date*	1-month view
EUR/USD	1.9%	12.4%	↗
EUR/CHF	0.6%	-0.8%	→
GBP/USD	2.1%	7.8%	↗
USD/JPY	-2.3%	-6.3%	↘

* Performance as at 28 August. Source: Bloomberg

USA

- At the beginning of August, the USD Index appreciated sharply as the tariff deadline approached but continued its general downhill path after that. SEK and NOK appreciated the most vs the USD, while the NZD was the only currency to depreciate.
- We anticipate continued weakness in the USD as we are cautious about declaring an end to the confidence crisis. Also, we expect the Fed to turn more dovish in coming months as Powell's Jackson Hole speech signalled a shift in the Fed's focus away from inflation towards growth and labour market risks.

Eurozone

- In August, EUR reversed its July losses against the USD as the ECB communication turned more hawkish, indicating that the hurdles for further rate cuts from the ECB have become higher.
- We reiterate our positive view on EUR/USD and our neutral view on EUR/CHF.

UK

- GBP appreciated significantly vs the USD in August, as higher-than-expected inflation numbers for July led the market to price in fewer interest rate cuts by the Bank of England than previously expected. The widening in the interest rate differential supported GBP.
- We reiterate our neutral view on EUR/GBP and our positive view on GBP/USD.

Switzerland

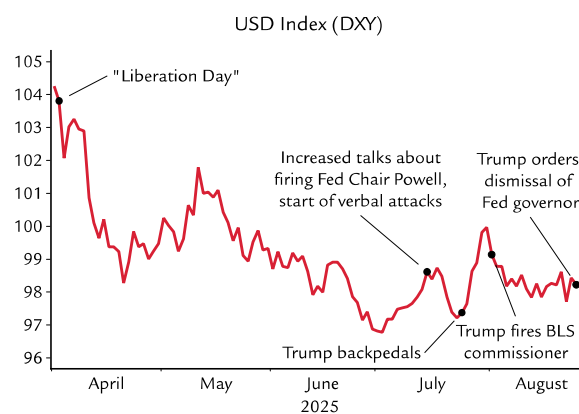
- CHF depreciated slightly against EUR in August as the Swiss growth outlook for 2026 deteriorated dramatically after the announcement of 39% US tariffs.
- We remain neutral on EUR/CHF.

Japan

- The JPY managed to reverse some of its July losses against the USD in August.
- In line with our view of a weaker USD, we expect USD/JPY to move lower in the coming weeks.

Muted USD, mounting risks

The confidence crisis surrounding the independence of US institutions escalated further in August. Tensions intensified following the dismissal of the Bureau of Labour Statistics (BLS) Commissioner after the US President had repeatedly accused the BLS without evidence of “rigging” economic data. The situation reached a new level of concern with the attempted dismissal of Federal Reserve governor Lisa Cook, reigniting doubts about the Fed's future independence. The Fed's independence and its credibility in providing an independent monetary policy is the cornerstone for trust in the USD and US Treasuries as global assets. Yet, US financial markets have responded with surprising composure to these events so far. The USD did not weaken dramatically, contrary to what might have been expected. This muted reaction could suggest that markets are becoming increasingly resilient – or desensitised – to political disruptions. Beyond personnel decisions, fiscal concerns persist. The budget deficit remains unsustainably high, adding another layer of uncertainty. While markets have remained relatively stable so far, the USD remains the most sensitive and immediate channel through which any further escalation in the confidence crisis would likely be reflected. In addition to the confidence crisis, which is likely here to stay, macroeconomic divergence further clouds the outlook for USD. The growth/inflation mix is increasingly unfavourable, and interest rate differentials are expected to tighten as the ECB is not committed to any further interest rate cuts in 2025, while the Fed looks increasingly likely to cut rates in September. Given these dynamics, we maintain our negative outlook for the USD over the next month.



Sources: Macrobond, Swiss Life Asset Managers. Last data point: 28/08/2025

Asset allocation

Shifting market drivers: from tariffs to the Fed

Review

- Equity markets faced headwinds in early August due to softer US labour market data. However, they resumed their upward trend later in the month, supported by strength in AI-related sectors, a rebound in megacap tech stocks and solid corporate earnings.
- Government bond yields were relatively stable throughout August. US 10-year yields dipped following weaker job market data but recovered by month-end.
- Corporate credit spreads continued to narrow and remain at historically tight levels, reflecting strong demand and solid fundamentals.
- The US dollar depreciated by 1.7% on a trade-weighted basis in August, influenced by shifting rate expectations and softer economic indicators.

Current asset allocation views

Asset class	Active weight
Global government bonds	neutral
Global investment-grade credit	underweight
Emerging market bonds	underweight
Global equities	overweight

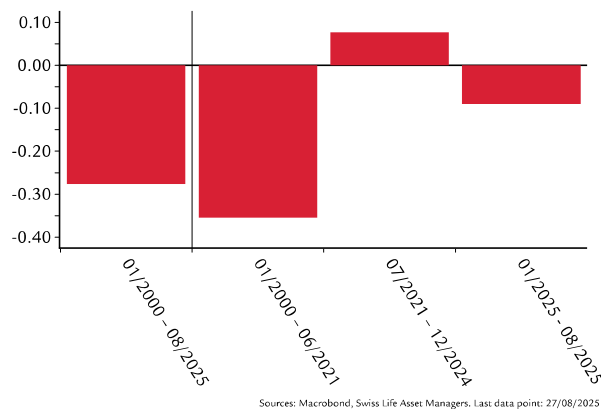
Source: Swiss Life Asset Managers

- We have trimmed our equity allocation but remain overweight relative to the benchmark, as we continue to see upside potential. This is supported by expectations of the US Fed entering an easing cycle and continued strong corporate fundamentals.
- On government bonds we remain neutral to slightly overweight in anticipation of a Fed rate cut. Within rates, we prefer US exposure over European, given more attractive yield dynamics and monetary policy.
- Credit spreads remain historically tight. While we acknowledge that all-in yields (government yield plus credit spread) are high, we continue to favour government bonds over credit. We believe the risk-return profile in credit remains asymmetric, whereas equities offer more compelling upside. As a result, we maintain an underweight in credit.
- We remain cautious on the US dollar, particularly from a Swiss franc perspective. Despite the USD's depreciation in August, we see further downside risk, primarily driven by anticipated Fed rate cuts.
- Financial markets have shown remarkable resilience despite ongoing trade tensions and uncertainty regarding inflation and labour market health in the US.

“Fed pivot” reshapes asset allocation strategy

While risks related to the trade war persist, financial markets have shifted their attention to the Federal Reserve's near-term policy direction. Chair Jerome Powell signalled a recalibration of priorities – from fighting inflation to preventing labour market weakness. At the Jackson Hole symposium, Powell acknowledged signs of a cooling labour market, suggesting the Fed may soon begin an easing cycle without reigniting inflationary pressures as potential tariff-related inflation is judged to be a temporary phenomenon. This policy pivot provides a tailwind for equities, which stand to benefit from a more accommodative monetary policy stance. However, markets remain sensitive to inflation surprises and earnings disappointments, underscoring the need for selective equity positioning. We continue to favour a globally diversified equity allocation with overweights in the US and emerging markets.

Correlation between US government bond and US equity returns



Sources: Macrobond, Swiss Life Asset Managers. Last data point: 27/08/2025

In light of the policy pivot by the Fed, we are increasingly considering government bonds as a strategic counterbalance to our equity allocation. For over two decades investors relied on the principle that bond prices typically rise when equities fall. However, since mid-2021 this relationship has reversed. Amid elevated inflation and heightened monetary policy uncertainty, the correlation between equity and bond returns turned positive, as inflation surprises began to depress both asset classes simultaneously. While the diversification benefit has not been fully restored, the Fed's monetary policy shift suggests a potential reversion to the historical norm. As inflation cools and monetary policy regains its traditional role, we expect equity-bond correlations to trend back towards negative territory, restoring their traditional hedging role within a multi-asset portfolio.

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