



Global Fixed Income Outlook & Strategy

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but the US economy may not be.**



Market Recap & Outlook

US technology companies may still be exceptional, but the US economy may not be. A big downward revision to May and June payroll employment has dimmed the narrative around US economic growth. July payrolls grew 73,000, but this now follows two months of near-zero gains. The White House was not amused, and the head of the Bureau of Labor Statistics was fired. Ten-year Treasury yields rallied to 4.2%.

What is going on? Slow growth. First-half US GDP growth averaged about 1.5%, and we may get more of the same, in our view. Labor supply growth is stalling, as net migration has been curtailed. Payrolls grew by 1.5 million over the past year, for an average of 125,000 per month. If we stop creating new establishment jobs, that will be a major negative development. That leaves only productivity as a growth driver. Output per hour has been slowing for a year and was 1.3% year-on-year (YoY) in Q1 2025. We expect a slightly better Q2 result, but not much.

Inflation looks sticky, in our view: the core personal consumption expenditure price index, the Fed's preferred measure of inflation, has been stuck at about 2.8% YoY, for a year, while average hourly earnings, i.e., wage inflation, is a point higher at 3.8%. The 1% gap between these is a separate measure of effective productivity. AI may be boosting Magnificent Seven share prices, but not the US economy.

Fiscal policy probably won't speed things up much, as 17%-18% tariffs are a \$300bn sales tax hike, which we believe will likely offset any business tax cuts from the budget. We see the deficit as a share of GDP stuck at about 6.5% of GDP next year.

Our Strategy

Even though inflation looks stuck, we see future growth scares leading to policy rate cuts beginning in September. These should be enough to keep GDP running at 1.5%-2.0% for the next year, but not enough to shrink Federal deficits. The net result may be a range-bound Treasury yield, and a weaker dollar, as markets come to terms with the increasingly narrow base of US exceptionalism. We see broader grounds for optimism in Europe, Asia, and emerging markets.

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