APRIL 2025

Fixed Income Focus

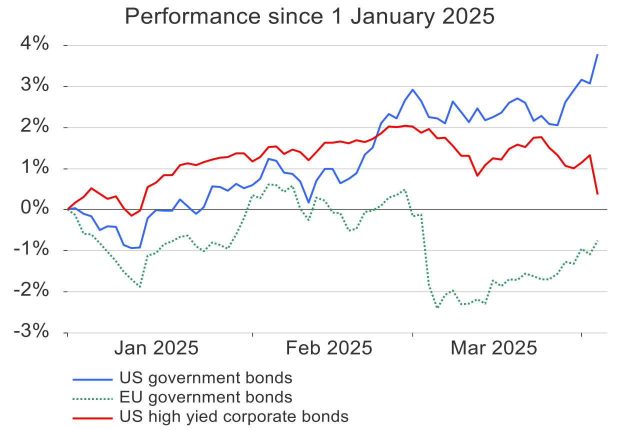
Summary

1. **Fed holds, ECB moves:** The Fed is likely to remain patient on rate cuts, while the ECB may act faster due to economic headwinds. We still expect two rate cuts this year for both the Fed and the ECB, with cuts in June and December in the US, and in April and June in the eurozone.
2. **Seeking safe-haven:** Trump's new tariffs have heightened uncertainty, raising the risk of a trade war or prolonged negotiations. Investors are likely to seek safe-haven assets, keeping US yields under pressure. In response, we have turned tactically Positive on US Treasuries, revising our 3-month US 10-year yield target to 4%. We also maintain a Positive stance on core eurozone government bonds, with a 12-month German 10-year yield target of 2.50%.
3. **Topic in focus: Keep calm and buy gilts:** UK gilts have been acting as a safe-haven since the US announcement of massive tariffs. We believe gilts can continue to outperform, supported by cooling inflation, fiscal restraint, expected policy rate cuts and a favourable shift in gilt issuance. We anticipate strong returns over a 12-month horizon and little change in the currency against the euro or dollar.
4. **Opportunities in Fixed Income:** In addition to US, core eurozone and UK government bonds, we are Positive on US Agency Mortgage-Backed Securities, US TIPS, and eurozone and UK investment grade corporate bonds.

. Drafting completed on 4 April

Contents

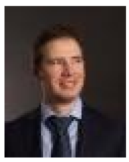
CHART OF THE MONTH: THE GOOD, THE BAD AND THE TARIFFS. SAFE-HAVEN ASSETS, SUCH AS GOVERNMENT BONDS, OUTPERFORM, WHILE RISK ASSETS, LIKE US HIGH YIELD BONDS, COLLAPSE



Source: LSEG Datastream, 03/04/2025

Edouard Desbonnets

Senior Investment Advisor, Fixed Income
BNP Paribas Wealth Management



BNP PARIBAS WEALTH MANAGEMENT

The bank for a changing world

Central banks

Fed holds, ECB moves

European Central Bank (ECB)

Market recalibration: Traders priced in fewer rate cuts after Germany's fiscal stimulus, but then priced in more cuts as a result of Trump's tariffs and higher recession risk. They now expect 2.6 rate cuts of 25bp this year and a terminal rate of 1.8%.

Policy stance: The disinflation process remains on track. Monetary policy is becoming much less restrictive, suggesting only a few more cuts in the future.

Our expectations: We still expect two rate cuts this year, but the higher downside risk to growth from Trump's massive tariffs may prompt the ECB to act sooner rather than later, i.e. in April and June rather than June and September. In our view, the German fiscal plan should prevent the ECB from cutting rates too aggressively as it raises the medium-term outlook for economic growth and inflation. The ECB could consider raising rates in the second half of 2026 as the economic effects start to feed through.

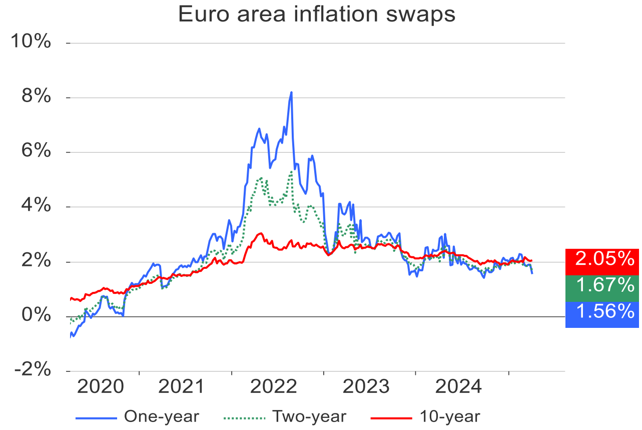
US Federal Reserve (Fed)

No rush to cut rates: The March FOMC meeting made a subtle shift towards accommodative liquidity conditions by slowing quantitative tightening, with the result that the Fed will become a net buyer of Treasuries from April. On the interest rate side, there is no urgency to cut rates despite tariff risks. Hard data has not weakened, contrary to surveys, leading the committee to overlook these less reliable signals.

Policy outlook: All members expect higher inflation this year only, with forecasts for 2026-27 unchanged, supporting Powell's view that tariff inflation could be transitory.

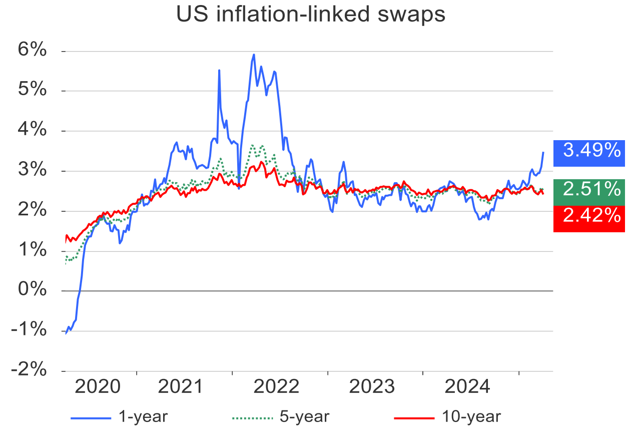
Our expectations: The Fed is likely to remain on hold for now, given recession concerns and the risk of long-term inflation expectations drifting above 2%. We expect the Fed to cut rates twice this year (in June and December) in response to the expected deterioration in economic growth and the labour market, and to end the cycle with a policy rate of 4%.

VIRTUALLY NO SIGNS OF ACCELERATING INFLATION PRICED IN FOR EURO AREA



Source: LSEG Datastream, 04/04/2025

INFLATION SWAPS SUGGEST NEAR-TERM TARIFF IMPACT



Source: LSEG Datastream, 03/04/2025

INVESTMENT CONCLUSION

Both the Fed and the ECB remain cautious amid economic uncertainty, largely driven by US tariffs. The Fed is likely to remain on hold for now amid higher inflation risks, while the ECB could cut sooner given the downside risks to growth. We still expect two Fed rate cuts this year (June and December) and two from the ECB (April and June, instead of June and September).

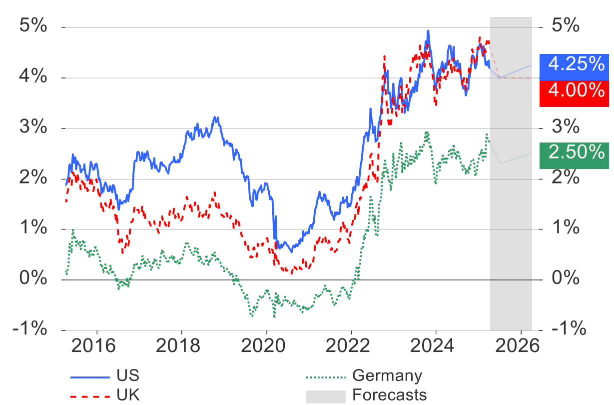
Bond yields

The great slide

We changed our stance on US Treasuries from Positive to Neutral last month, as we believed that bond yields had already fallen significantly. However, Trump's decision in early April to impose sweeping new tariffs on several US trading partners has introduced a new layer of uncertainty, potentially setting the stage for a prolonged trade war or protracted negotiations. Against this backdrop, we expect market uncertainty to persist in the near term, prompting investors to seek refuge in safe-haven assets. This dynamic should continue to put downward pressure on US yields. In response, **we have turned tactically Positive on US Treasuries** and revised our 3-month target for the US 10-year yield to 4%, while maintaining our 12-month target at 4.25%.

We expect a similar flight-to-quality effect in Europe, benefiting German bunds and other core eurozone government bonds. We are therefore maintaining our **Positive stance on core euro government bonds**, with a 12-month target for the German 10-year yield of 2.50%.

10-YEAR RATES



Source: LSEG Datastream, 04/04/2025

	Maturity (years)	03/04/ 2024	3-month target	12-month target
USA	Policy rate	4.50	4.25	4.00
	2	3.70	3.75	4.25
	5	3.74	3.75	4.25
	10	4.05	4.00	4.25
	30	4.49	4.25	4.50
Germany	Policy rate	2.50	2.25	2.00
	2	1.93	2.00	2.00
	5	2.22	2.15	2.15
	10	2.64	2.30	2.50
	30	3.03	2.55	2.75
UK	Policy rate	4.50	4.25	3.50
	2	4.02	4.00	3.60
	5	4.10	4.00	3.75
	10	4.52	4.00	4.00
	30	5.19	4.50	4.45

Source: Refinitiv Datastream, BNP Paribas WM

Investment Conclusion

Trump's new tariffs have heightened uncertainty, raising the risk of a trade war or prolonged negotiations. Investors are likely to seek safe-haven assets, keeping US yields under pressure. In response, we have turned tactically Positive on US Treasuries, revising our 3-month US 10-year yield target to 4%. We also maintain a Positive stance on core eurozone government bonds, with a 12-month German 10-year yield target of 2.50%.

Topic in Focus

Keep calm and buy gilts

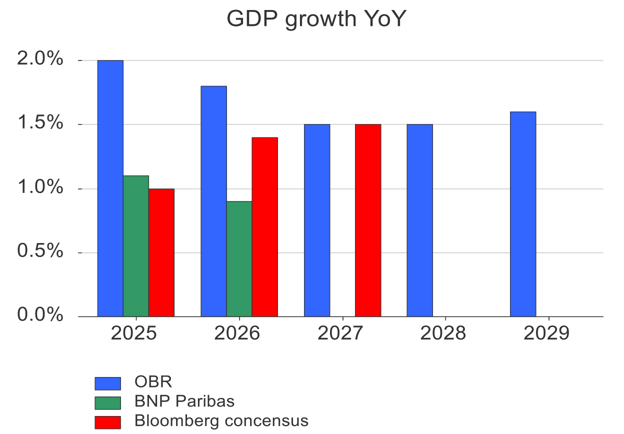
Gilt issuance strategy shifts: The UK Debt Management Office (DMO) has made a significant adjustment in its bond issuance strategy for the 2025/26 fiscal year. It plans to reduce the issuance of long-dated conventional gilts from 19.9% to 13.4%, while increasing the issuance of short-dated gilts from 35.9% to 37.1%. This shift reflects the government's strategy to adapt to higher borrowing costs and maintain flexibility in a volatile market. The decision was well-received, with long-term gilt yields declining in response.

Fiscal policy uncertainty: While the UK government avoided immediate fiscal tightening in its Spring Statement, the optimistic economic forecasts from the Office for Budget Responsibility (OBR) raise concerns (see chart). Growth expectations seem excessive, and the proposed consolidation measures -mainly welfare reforms and departmental spending cuts- may face political resistance. With further adjustments likely in the Autumn Budget, uncertainty over public finances remains high, creating a complex backdrop for gilts.

Bank of England's expected moves: We anticipate that the Bank of England will cut interest rates by 75 basis points this year and by a further 25 basis points early next year, leading to an end-of-cycle rate of 3.50% in 12 months' time. This is significantly more than the 70 basis points currently priced in over the next 12 months. Given that monetary policy is a key driver of gilt yields, these rate cuts should provide support for bonds.

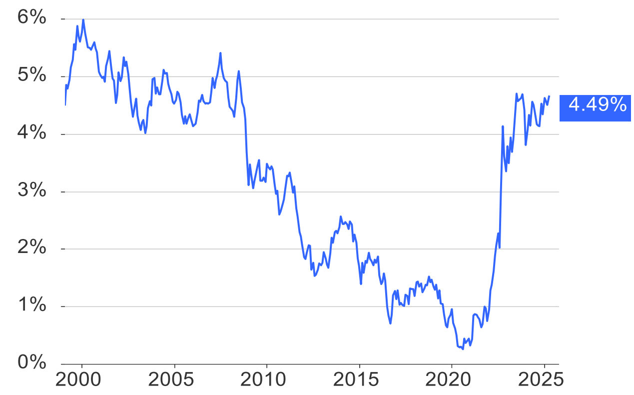
Strong return potential: UK government bonds offer an average yield of 4.5% (see chart) with a duration of 8.4 years. We expect bond yields to decline – for example, we think that the 10-year yield will drop from the current 4.4% to 4.0% in 12 months. This drop in bond yields would translate to an expected total return of close to 7% over one year for UK government bonds, making gilts an appealing choice for global investors (we do not anticipate major changes in EUR/GBP or USD/GBP over the next 12 months).

GROWTH FORECASTS FROM THE OFFICE FOR BUDGET RESPONSIBILITY SEEM EXCESSIVE



Source: LSEG Datastream, 03/04/2025

UK GOVERNMENT BONDS OFFER AN AVERAGE YIELD OF 4.5%



Source: LSEG Datastream, 03/04/2025

Investment Conclusion

UK gilts have been acting as a safe-haven since the US announcement of massive tariffs. We believe gilts can continue to outperform, supported by cooling inflation, fiscal restraint, expected policy rate cuts and a favourable shift in gilt issuance. We anticipate strong returns over a 12-month horizon and little change in the currency against the euro or dollar.

Our Investment Recommendations

Asset class	Zone	Our opinion	
Government bonds	Germany	+	Positive on German sovereign bonds. Prefer 5-10 years maturities.
	Peripheral countries	=	Neutral on peripheral debt (Portugal, Italy, Spain, Greece).
	United Kingdom	+	Positive on UK government bonds.
	United States	+	We have turned tactically Positive from Neutral on US government bonds. Positive on TIPS.
Corporate bonds Investment Grade (IG)	Eurozone United Kingdom United States	+	• Positive on eurozone and UK IG corporate bonds, and Neutral on US corporate bonds. • Prefer short maturities in the US (up to 5 years) and up to 10 years in the eurozone. • Positive on convertible bonds in the eurozone.
Corporate bonds High Yield (HY)	Eurozone and United States	=	• Neutral on HY bonds. • Positive on *fallen angels* and *rising stars.*
Emerging bonds	In hard currency	=	Neutral on EM hard currency bonds (sovereign and corporate).
	In local currency	=	Neutral on EM local currency government bonds.

Market Data

	10-year rate (%)	Spread (bp)	Spread change 1 month (bp)
United States	4,18	---	
Germany	2,73	---	
France	3,44	71	-3
Italy	3,82	110	2
Spain	3,35	63	-6
Portugal	3,25	52	-2
Greece	3,53	80	-9

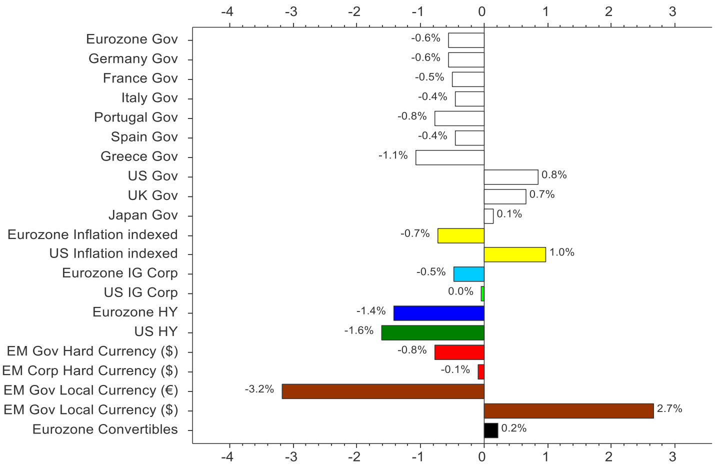
03/04/2025
Source: Refinitiv Datastream

	Yield (%)	Spread (bp)	Spread change 1 month (bp)
Global	3,60	34	1
Corporate bonds IG EUR	3,29	97	6
Corporate bonds IG USD	5,13	93	6
Corporate bonds HY EUR	5,85	322	38
Corporate bonds HY USD	7,62	334	54
Emerging government bonds in hard currency	6,87	268	15
Emerging corporate bonds in hard currency	6,44	229	15
Emerging government bonds in local currency	6,27	232	-7

03/04/2025
Source: Refinitiv Datastream, Bloomberg

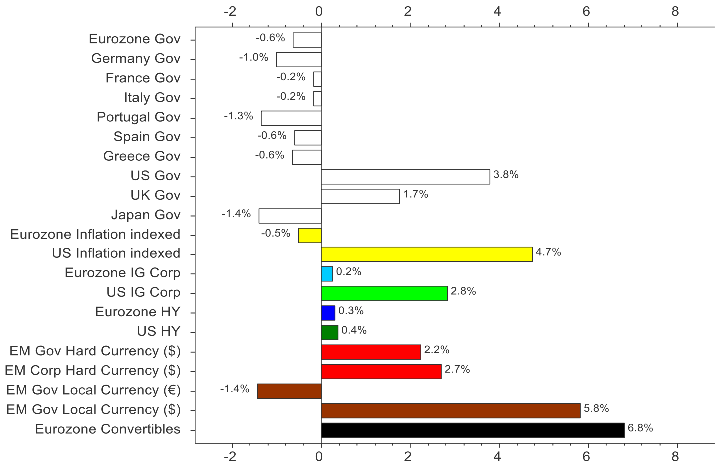
Returns

OVER ONE MONTH



Source: LSEG Datastream, 03/04/2025 Source: Bloomberg Barclays indices except EM local debt (JPM) and Convertibles (Refinitiv)

SINCE 01/01/2025



Source: LSEG Datastream, 03/04/2025 Source: Bloomberg Barclays indices except EM local debt (JPM) and Convertibles (Refinitiv)

EM = Emerging Markets

THE INVESTMENT STRATEGY TEAM

FRANCE

Edmund SHING
Global Chief Investment Officer

Jean-Roland DESSARD
Chief Investment Advisor

Isabelle ENOS
Investment Advisor

ITALY

Luca IANDIMARINO
Chief Investment Advisor

BELGIUM

Philippe GIJSELS
Chief Investment Advisor

Alain GERARD
Senior Investment Advisor, Equities

Patrick CASSELMAN
Senior Commodities Strategist

GERMANY

Stephan KEMPER
Chief Investment Strategist
Stefan MALY

LUXEMBOURG

Guy ERTZ
Chief Investment Advisor – Deputy Global CIO

Edouard DESBONNETS
Senior Investment Advisor, Fixed Income

ASIA

Prashant BHAYANI
Chief Investment Officer, Asia

Grace TAM
Chief Investment Advisor, Asia

CONNECT WITH US

wealthmanagement.bnpparibas

DISCLAIMER

This marketing document is communicated by the Wealth Management Métier of BNP Paribas, a French Société Anonyme, Head Office 16 boulevard des Italiens, 75009 Paris, France, registered under number 662 042 449 RCS Paris, registered in France as a bank with the French Autorité de Contrôle Prudentiel et de résolution (ACPR) and regulated by the French Autorité des Marchés Financiers (AMF). As marketing material, it has not been prepared in accordance with legal and regulatory requirements aimed at ensuring the independence of investment research and is not subject to any prohibition on dealing ahead of its dissemination. It has not been submitted to the AMF or any other market authority.

This document is confidential and intended solely for the use of BNP Paribas SA, BNP Paribas Wealth Management SA or their affiliates ("BNP Paribas") and the persons to whom this document has been delivered. It may not be distributed, published, reproduced or disclosed by any recipient to any other person, nor may it be quoted or referred to in any document, without the prior consent of BNP Paribas.

This document is provided solely for information and shall not constitute an offer or solicitation in any state or jurisdiction in which such an offer or solicitation is not authorized, or to any person to whom it is unlawful to make such offer, solicitation or sale. It is not, and under no circumstances is it to be construed as, a prospectus.

Although the information provided herein may have been obtained from published or unpublished sources considered to be reliable and while all reasonable care has been taken in the preparation of this document, BNP Paribas does not make any representation or warranty, express or implied, as to its accuracy or completeness and does not accept responsibility for any inaccuracy, error or omission. BNP Paribas gives no warranty, guarantee or representation as to the expected or projected success, profitability, return, performance, result, effect, consequence or benefit (either legal, regulatory, tax, financial, accounting or otherwise) of any product or transaction. Investors should not place undue reliance on any theoretical historical information regarding such theoretical historical performance. This document may contain or refer to past performance; past performance is no guarantee for future performance.

The information contained in this document has been drafted without prior knowledge of your personal circumstances, including your financial position, risk profile and investment objectives.

Prior to entering into a transaction each investor should fully understand the financial risks, including any market risk associated with the issuer, the merits and the suitability of investing in any product and consult with his or her own legal, tax, financial and accounting advisors before making his or her investment. Investors should be in a position to fully understand the features of the transaction and, in the absence of any provision to the contrary, be financially able to bear a loss of their investment and willing to accept such risk. Investors should always keep in mind that the value of investments and any income from them may go down as well as up and that past performance should not be seen as an indication of future performance. Any investment in a product described herein is subject to the prior reading and understanding of the legal documentation concerning the product, and in particular the one which describes in details the rights and obligations of investors as well as the risks inherent to an investment in the product. Save as otherwise expressly agreed in writing, BNP Paribas is not acting as financial adviser or fiduciary of the investor in any transaction. The information, opinions and projections expressed herein reflect the opinion of their author at the time of writing; they are not to be relied upon as authoritative or taken in substitution for the exercise of judgment by anyone, and are subject to change without notice. Neither BNP Paribas nor any BNP Paribas Group entity accepts any liability whatsoever for any consequences that may arise from the use of information, opinions or projections contained herein.

As distributor of the products described herein, BNP Paribas may receive distribution fees on which you can obtain more information upon specific request. BNP Paribas, their employees or administrators may hold positions in these products or have dealings with their issuers.

By accepting this document, you agree to be bound by the foregoing limitations.

© BNP Paribas (2025). All rights reserved.

Pictures from Getty Images.