

NORDKINN

— ASSET MANAGEMENT —

Market Review & Outlook

July 2025

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Market overview

Global review

Global bond yields rose in July, driven by hawkish central bank messaging, resilient macroeconomic data, and easing concerns over Trump's trade war aspirations.

The Federal Reserve left interest rates unchanged at 4.25–4.50% at its July 30th meeting. Chair Powell gave no indication of a potential rate cut in September, instead maintaining and reaffirming a cautious, data-dependent stance. Although FOMC members Waller and Bowman dissented in favour of a cut, the market interpreted the overall message as hawkish, pricing out rate cuts for the remainder of the year. Supporting this outlook were stronger-than-expected Q2 GDP figures, a rebound in consumer confidence, and signs of upward pressure in corporate pricing intentions.

However, this narrative shifted sharply on August 1st, following not only the release of weaker-than-expected U.S. Non-Farm Payroll data for July but the substantial downward revisions to May and June NFP data, reducing job growth by a combined 258,000. This has raised fresh concerns about the strength of the labour market and reignited expectations of Fed easing.

The European Central Bank also held rates steady at 2.00% at its announcement on July 24th, following seven consecutive cuts at its previous meetings. President Lagarde highlighted persistent uncertainty, especially related to trade tensions, but noted that the Euro Area economy has so far remained broadly resilient. She stated that the ECB is in a "good place" and well positioned to adopt a wait-and-see approach. The markets responded by trimming expectations for a September rate cut.

A U.S.–EU trade agreement came into effect on July 27th, reducing tariffs on most EU goods to 15% and including commitments for USD 750 bln in EU purchases of U.S. energy and military equipment. Meanwhile, the 90-day tariff pause with China was extended, helping to support market sentiment late in the month.

Our global theme *"Geopolitical tensions impacting growth"* detracted from performance, mainly due to a flatter U.S. yield curve and rising short-term EUR rates. In addition, the *"Rebuilding Europe"* theme also weighed on performance, as a weaker euro and flatter European yield curves proved challenging for positioning.

Nordic review

In Sweden, CPIF excluding energy rose to 3.3% year-on-year in June (see chart), sharply exceeding both market expectations and the Riksbank's forecast of 2.9%. The upside surprise was mainly driven by sharp increases in prices for package holidays, transport services, and car rentals, all components infamous for their volatility. Corporate price plans eased according to surveys. Nevertheless, inflation remains uncomfortably high. As a result, interest rates rose as markets reduced expectations for further Riksbank rate cuts, and the SEK appreciated.

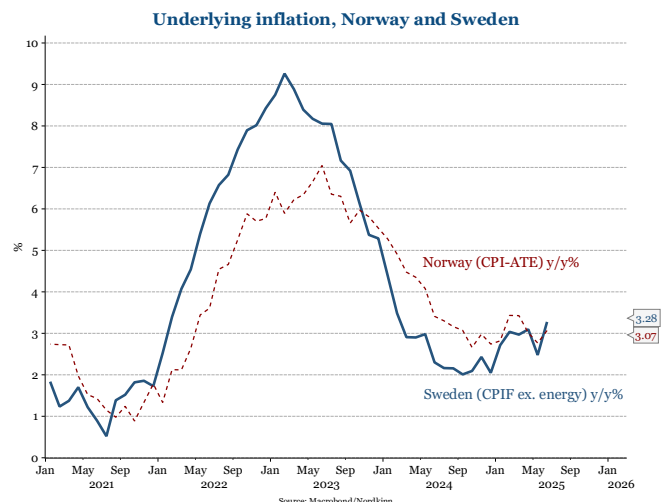
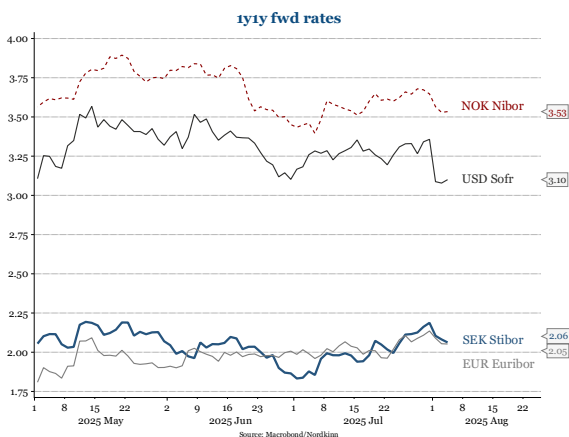
By contrast, economic activity remained subdued. According to the Q2 flash estimate, GDP expanded by just 0.1%, well below expectations, suggesting a stagnating growth picture in the first half of 2025, with household consumption continuing to lag. Unemployment remains high.

In response to the inflation surprise, our new theme *"Sweden: Revival of the inflation hedge"* contributed positively to performance, primarily through gains in Swedish Break-Even Inflation positions. Meanwhile, the theme *"Sweden: Bond supply set to expand"* detracted from performance due to rising interest rates and a flatter yield curve. Although this theme is largely expressed via relative positioning, we had deliberately tilted our bond exposure slightly long during July, which proved costly.

In Norway, core inflation rose to 3.1% year-on-year in June, up from 2.8% in May, see chart. The outcome matched Norges Bank's projection but came in slightly above market consensus. As in Sweden, volatile transportation prices were the main contributor to the monthly increase.

The labour market is showing signs of softening. According to the labour force survey, the unemployment rate has risen sharply so far in 2025. Registered unemployment has also increased, but far less dramatically. However, recent methodological changes have made the registered unemployment data harder to interpret.

Norwegian interest rates moved higher in July, in line with global trends, while the yield curve flattened modestly. Despite this, our theme *"Lags in yield and curve dynamics"* contributed positively to performance. We entered the month with a short position in short-dated rates as a hedge against our curve steepeners, which proved beneficial. Additionally, our long positions in Norwegian government bonds outperformed both versus peers and swaps. Our second Norway-focused theme, *"Path to looser policy"*, was broadly flat on the month.



Outlook

Global outlook

The market's initial hawkish interpretation of the July FOMC press conference on July 30th quickly reversed after the release of the July U.S. jobs report on August 1st. The weaker-than-expected labour market data bolstered expectations for interest rate cuts, and sooner.

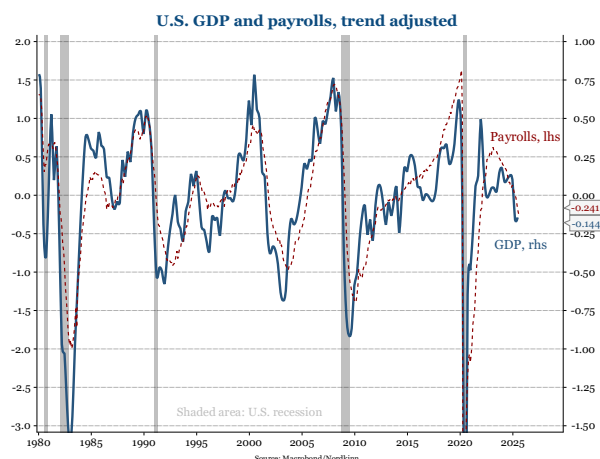
While the market reaction in U.S. rates on August 1st appeared dramatic, we do not believe it was an overreaction, for two reasons. First, the move came just two days after Chair Powell's press conference had eroded confidence in the rate-cutting path, meaning starting yields were elevated. Second, the downside surprise in the jobs report justifies at least two rate cuts in 2025, aligning with the Fed's June dot plot. At the time of writing, markets are pricing in approximately 60 basis points of cuts by end-2025.

Meanwhile, July's tariff announcements lifted the effective tariff rate slightly higher than anticipated. In addition, corporate pricing intentions ticked higher, according to several surveys, pointing to potential upside risks for inflation. However, the pass-through to consumer prices and market-based inflation expectations remain limited for now.

Taken together, we maintain a cautious view on the U.S. rate outlook. While our conviction on the precise level of future interest rates is limited, we clearly see the balance of risks as skewed to the downside. A deterioration in hard data will open the door to faster rate cuts and lower yields.

In Europe, the ECB has poured cold water on the prospect of 2025 rate cuts, despite downside growth risks from trade tensions. We believe the front end has now repriced sufficiently, and the case for curve steepening is becoming more compelling. Two factors support this view: anticipated fiscal stimulus from Germany could push 10-year Bund yields higher, while weaker near-term growth or faster disinflation (not our baseline scenario) could trigger a renewed rally in front-end rates.

While our EUR/USD positioning was on the wrong side of the July move, we continue to see upside potential for the cross. This is underpinned by a more constructive outlook for Eurozone growth relative to the U.S., and the divergence in central bank trajectories—with the ECB near the end of its easing cycle and the Fed likely to ease further ahead. Additionally, U.S. trade policy developments and Trump's increasing attacks on institutional independence fuels the potential for a more structural weakening of the USD ahead.



Nordic outlook

Swedish interest rates rose sharply in July, driven by a stronger-than-expected inflation print and spillover from a more hawkish-than-anticipated ECB communication. Markets are now pricing in around 20 basis points of cumulative cuts over the coming meetings. While this appears broadly consistent with the Riksbank's guidance, implying a roughly 50/50 probability of another cut from the current 2.00% policy rate, we view the balance of risks as tilted to the downside.

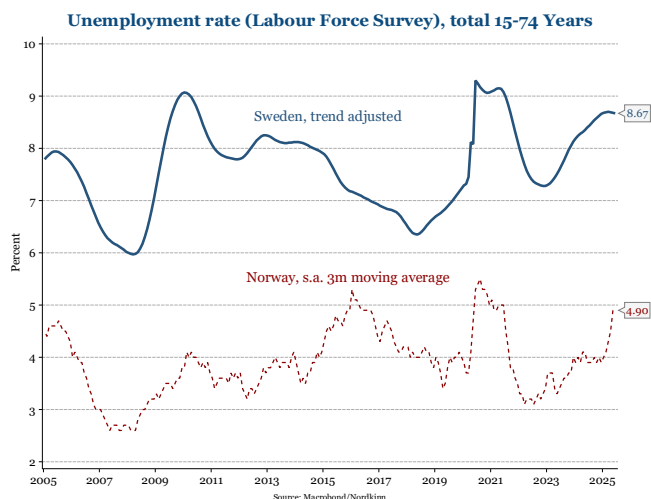
Economic activity continues to recover only slowly, as highlighted by a modest 0.1% expansion in Q2 GDP. Although consumer and business sentiment indicators improved meaningfully in July, surveys still point to subdued growth. We believe the upside surprise in June CPI inflation was largely driven by temporary factors as indicated also by corporate price plans, expecting inflation to moderate ahead. As a result, we shifted from short to long exposure in Swedish short-term rates during July.

In Norway, market pricing now reflects slightly less than one rate cut per quarter over the next year, with a terminal policy rate of 3.25%. We believe this path is justified by the prospect of continued disinflation toward the 2.0% target in the coming months and quarters.

While our baseline rate view has remained broadly unchanged over the summer, we now see three developments nudging the balance of risks to the downside, from a previously neutral stance: 1) The increased likelihood of a more aggressive U.S. easing cycle could influence Norges Bank's policy outlook; 2) Despite heightened uncertainty in Norwegian labour market statistics (due to ongoing data revisions), the recent uptick in unemployment, evident in both survey-based and registered measures, warrants close monitoring; 3) Our proprietary food price tracker model points to a decline in July inflation, with CPI data due on August 11th.

We currently prefer to express our view through curve steepeners and tighter cross-market spreads, but we keep standing ready to tactically add directional exposure once the opportunities present themselves.

Furthermore, Norwegian government bonds are well-positioned to benefit from upcoming rate cuts. These assets are becoming increasingly attractive to foreign investors hedging FX risk, and the government borrowing outlook remains contained. Any potential increase in fiscal spending is likely to be financed via higher petroleum revenue spending, rather than through increased bond issuance.



About Nordkinn

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Our focus is to generate stable absolute returns that exhibit low correlation to other assets. Our Nordkinn Fixed Income Macro Fund was launched in 2013.

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