

NORDKINN

— ASSET MANAGEMENT —

Market Review & Outlook

September 2025

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Market overview

Global review

After a turbulent August—marked by tariff fears, concerns over fiscal debt, and political interference in monetary policy—investors rotated into duration in early September. Lower U.S. policy rates, coupled with temporary relief regarding tariffs and reassurance over Fed independence, fuelled a bond rally during the first half of the month. However, stronger macroeconomic data in the second half of September erased most of these gains.

On September 17th, the Federal Reserve cut the Fed Funds rate by 25 bps to 4.00–4.25%. While the decision was unanimous, the newly appointed Fed Governor Stephen Miran, chosen by President Trump, dissented in favour of a larger 50 bps cut. The Committee justified its decision by noting rising downside risks to employment. Non-Farm Payrolls increased by only 22k in August, pulling the three-month average down to 29k—below the level most economists view as necessary to keep unemployment stable. The unemployment rate rose to 4.3% from 4.2%.

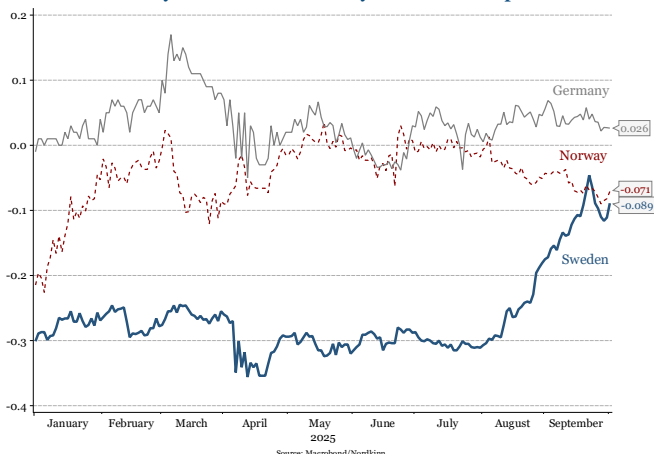
Elsewhere, the ECB, Bank of England and Bank of Japan all left their key policy rates unchanged at 2.00%, 4.00% and 0.50%, respectively.

While the Fed stressed that future adjustments will be data dependent, the updated dot plot indicated another 50 bps of easing this year, with Miran standing out as the only member advocating for substantially more. Market reaction was muted, as short-end rates had already declined following Chair Powell’s Jackson Hole speech the previous month, combined with the weak August labour market report. Ahead of the meeting, some market participants had speculated that a larger share of the Committee might lean more dovish, but Miran ultimately remained an isolated voice.

With reduced immediate concerns about Fed’s independence and greater clarity on the near-term policy path, pension funds and insurance companies took advantage of the August sell-off to add duration. Long-dated government bonds benefited disproportionately, as the front end was already anchored by priced-in rate cuts, leading to curve flattening in September.

On a net basis, the general flattening of yield curves weighed on our global themes in September, such as our European theme *“Rebuilding Europe.”* The at-least-for-now easing of geopolitical and tariff-related uncertainties made us close down *“Geopolitical tensions impacting growth”*, having limited effect on performance. In the build-up of our new global theme *“Sovereign risk premia,”* aimed at capturing anticipated repricing of fiscal risks, its return impact was marginal.

10-year Government bond yields versus swaps



Nordic review

In Sweden, the Riksbank cut its policy rate by 25 bps to 1.75% on September 23rd to provide additional support to the economy. While acknowledging the summer uptick in inflation to around 3.0%, the central bank assessed it as temporary and placed greater emphasis on supporting weak economic growth and a soft labour market. The accompanying policy-rate projection was hawkish as it signalled that the key rate would remain unchanged at 1.75% at least through Q3 2026, with the next full 25 bps hike not anticipated until 2028. Exposure towards short dated Swedish rates in and around the Riksbank announcement benefited our *“Tactical risk reward trading”*.

Just days earlier, the Swedish government presented a record expansionary budget bill for 2026, including SEK 127 bln (1.9% of GDP) in unfunded reforms. Measures such as 50% reductions in food VAT and lower electricity taxes will dramatically lower inflation in hopes to support household consumption. However, the budget will significantly increase the government’s borrowing requirement next year, putting substantial further pressure on government bond prices.

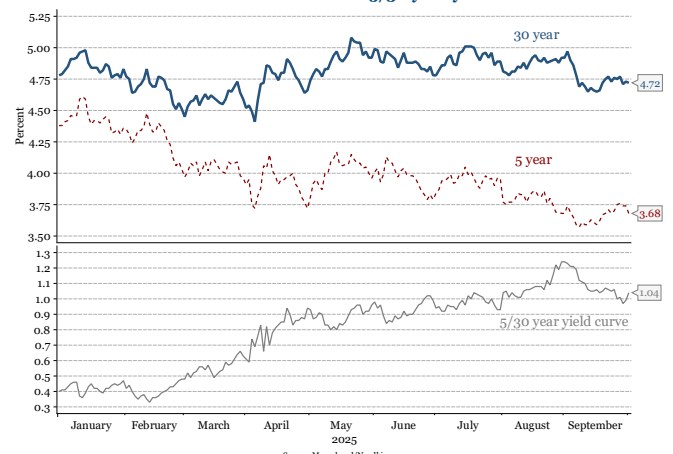
Amid expectations of heavier issuance and larger net supply ahead, longer-dated Swedish government bonds (SGBs) sold off sharply in September. The pronounced underperformance of SGBs relative to swaps, covered bonds, and cross-market peers contributed positively to our Swedish theme *“Bond supply set to expand.”*

Turning to Norway, Norges Bank lowered its policy rate by 25 bps to 4.00%, stating it did not want to restrain the economy more than necessary. However, stronger-than-expected GDP growth and underlying inflation prompted an upward revision of the rate path by up to 35 bps—much more than markets had anticipated. The new projection signals a prolonged period of unchanged rates at least through Q1 2026, with the first full 25 bps cut only expected in the second half of next year.

While our Norwegian theme *“Path to looser policy”* benefited from the rate cut itself, the gains were offset by the larger-than-expected upward revision to the rate path and its impact on market expectations for future policy rates.

Given the strong global spillovers to the long-end of the Norwegian yield curve, our theme *“Lags in yield and curve dynamics”* was in aggregate negatively affected by the broad flattening of global yield curves in September, which was further reinforced by Norges Bank’s more hawkish outlook. Gains from the relative performance of Norwegian government bonds versus Swedish and U.S. peers were insufficient to fully offset these losses.

U.S. Government bond 5/30 year yields



Outlook

Global outlook

Following the first Fed rate cut of 2025, Chair Jerome Powell described the current monetary stance as “still modestly restrictive.” The updated dot plot revealed an unusually wide dispersion of views within the FOMC regarding the appropriate policy path. While some members favour keeping rates on hold, others support a sharp reduction. The median projection points to two additional rate cuts this year. It would likely take an unexpected recovery in the labour market for the Fed to deliver less easing this year. However, Powell faces a difficult task in building consensus, and we would not be surprised to see more dissents.

Looking further ahead, the situation becomes more fluid. Potential tariff-induced inflation increases the likelihood that resistance to further rate cuts will grow next year.

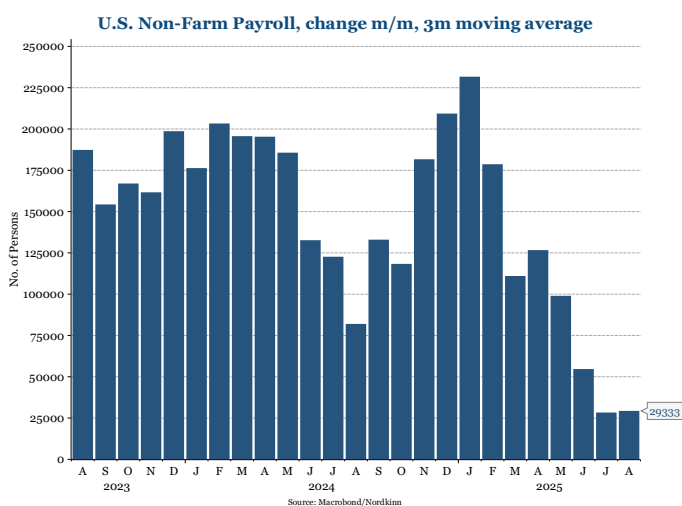
The reversal of immigration flows complicates estimates of the “payrolls breakeven rate,” but the recent rise in the unemployment rate, combined with household reports that jobs are becoming harder to find, point to a weakening of the labour market. At the same time, high-frequency indicators such as layoffs and jobless claims have yet to show any meaningful deterioration. The Fed’s characterisation of the labour market as “still decent but softening” appears accurate, and the risk of renewed wage-driven inflation pressures seems limited.

Taken together, while markets scaled back expectations for deeper cuts in the second half of September, we believe that meaningfully lower bond yields from here will require a significant deterioration in labour market data, potentially triggering recession concerns.

Turning to longer-dated government bonds, we expect pricing and volatility to remain highly sensitive to fiscal developments. Although lower policy rates ease debt-service burdens in the near term, persistently large fiscal deficits and rising debt-to-GDP ratios leave sovereign risk premia vulnerable over the medium term.

Following the September bond rally, during which long-term bonds outperformed and yield curves flattened, we introduced a new global investment theme: “Sovereign risk premia.” This theme is designed to capture the risk that investors will increasingly demand higher compensation for fiscal uncertainty, particularly at the long end of yield curves.

At the same time, with some temporary easing of geopolitical uncertainties—such as tariff tensions and their near-term growth and inflation effects—we decided to terminate our global theme “Geopolitical tensions impacting growth.”



Nordic outlook

In Sweden, the Riksbank’s projections are consistent with a stable policy rate of 1.75% for an extended period. Unlike previous trajectories that signalled a bias toward further cuts to support the economy, the current rate path shows no inclination to move in either direction. This suggests that the Riksbank sees the current stance as appropriate and that the hurdle for near-term policy changes is relatively high.

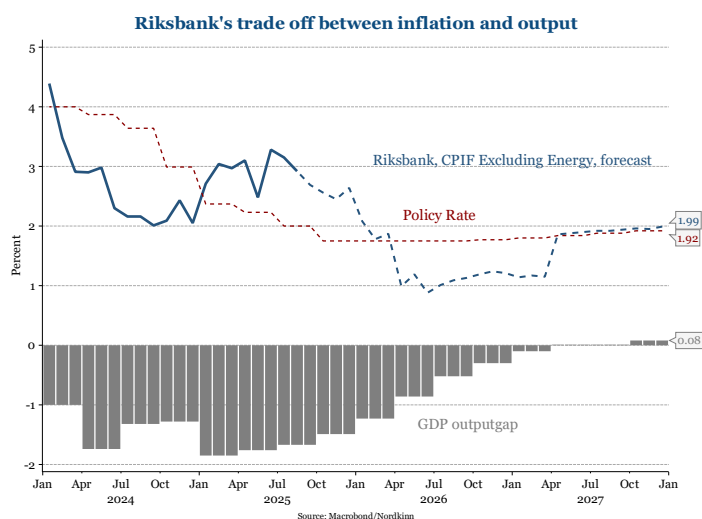
The Riksbank appears notably confident in its forecast that underlying inflation will fall below target next year, from around 3.0% currently. The main upside risk is that inflation proves stickier than expected. Conversely, there is a risk that the Riksbank’s upgraded GDP forecast for next year—from 2.2% to 2.5%—is too optimistic, as it will take time for the 2026 Budget Bill to filter through the economy. On balance, we expect the Riksbank to keep rates on hold at least through next year and will fade any expectations of earlier hikes.

At the long end of the curve, dynamics differ. Swedish government bond supply is set to remain elevated through the autumn and at historically high levels in the coming years, exerting constant pressure on bond prices. While Swedish government bonds have already cheapened significantly versus swaps, we believe there is scope for further cheapening on a cross-market basis, including relative to Norway.

In Norway, by contrast, the supply backdrop is considerably more favourable. The Debt Office plans to issue only NOK 12–15 bln for the remainder of the year, implying average auction sizes of just NOK 2–2.5 bln until year-end. For 2026, issuance is expected to rise only modestly, in sharp contrast to developments in most other countries, as Norway does not rely on borrowing to finance its budget. With Norwegian government bonds still trading cheap relative to swaps and peers, we view the supply outlook as constructive for NGB performance.

On shorter-dated NOK rates, we expect Norges Bank to keep the policy rate unchanged at 4.00% through Q1 2026, in line with its own projections. Our proprietary inflation modelling points to a somewhat lower inflation trajectory in the first half of next year compared with Norges Bank’s forecast, mainly reflecting lagged effects from lower commodity price growth on food prices.

With markets having trimmed rate-cut expectations significantly during September, we see the balance of risks skewed to the downside. The probability of a hike from 4.00% is low. By contrast, several plausible scenarios could prompt earlier or faster easing than currently projected, including a quicker return of inflation to target, a stronger NOK, or a negative external demand shock.



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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