BEHIND THE
HEADLINES

with **Ronald Temple**, Chief Market Strategist

9 MAY 2025

The Week at a Glance

- The United States and United Kingdom announced the outlines of a trade deal, but the agreement appears largely symbolic with minimal tariff reductions. Despite lower US tariffs on UK cars and potential steel tariff cuts, tariffs on UK exports will remain materially higher than in 2024.
- The US Federal Open Market Committee (FOMC) kept interest rates steady, highlighting expectations for increasing tension between its mandates to maintain price stability and maximize employment. I expect no rate cuts in 2025 while futures markets suggest 70 basis points (bps) of easing.
- China's April exports and imports outperformed expectations, but exports to the United States fell 21% while imports from the United States declined by 14%. Trade with other countries rose sharply.
- The Bank of England (BoE) cut rates by 25 bps amid a divided vote, and markets now expect less easing ahead.
- Looking forward, US inflation is expected to reach a short-term low in April before potentially reaccelerating, US retail sales growth is likely to slow, and University of Michigan Sentiment may stabilize at low levels. Japan's GDP is projected to contract slightly, while the UK's Q1 GDP is expected to show temporary strength due to one-off factors, with underlying growth remaining weak.

The Week Behind

Region	Indicator	Date	Period	Comp	Consensus	Actual	Prior Reading
United States	FOMC Target Rate Range	7 May			4.25% –4.50%	4.25% – 4.50%	4.25% – 4.50%
China	Exports	8 May	April	y-o-y	2.0%		12.4%
	Imports	8 May	April	y-o-y	-5.9%		-4.3%
United Kingdom	BoE Target Rate	8 May			4.25%	4.25%	4.50%

The Week Ahead

Region	Indicator	Date	Period	Comp	Consensus	Actual	Prior Reading
United States	CPI	13 May	April	m-o-m	0.3%		-0.1%
	CPI	13 May	April	y-o-y	2.4%		2.4%
	Core CPI	13 May	April	m-o-m	0.3%		0.1%
	Core CPI	13 May	April	y-o-y	2.8%		2.8%
	Retail Sales Control Group	15 May	April	m-o-m	0.3%		0.4%
	University of Michigan Sentiment	16 May	May		53.0		52.2
China	CPI	9 May	April	y-o-y	-0.1%		-0.1%
	PPI	9 May	April	y-o-y	-2.8%		-2.5%
Japan	GDP	15 May	Q1-25	SA q-o-q	-0.1%		0.6%
United Kingdom	GDP	15 May	Q1-25	q-o-q	0.6%		0.1%

The Week Behind

1. **The United States and United Kingdom announced the outlines of a trade agreement.**

   The outlook: On Thursday 8 May, the United States and United Kingdom announced the broad outlines of a trade agreement. This agreement is likely the first of many, but one takeaway is that the agreements are likely to be light on details and more conceptual in nature, as trade negotiations often take years to complete. Given that the tariff rate across all UK exports to the United States does not appear to have declined materially in this deal, it could also be seen as a negative signal for other countries with less close relations with the United States.

   The details: The full terms of the US-UK trade deal were not released, but key highlights included a 10% baseline tariff on most imports into the United States from the United Kingdom. Tariffs on auto imports into the United States were reduced from 27.5% to 10% on 100,000 UK cars, a level almost equal to UK auto exports to the United States in 2024. The United Kingdom announced that tariffs on steel exports would fall to zero, but the United States has not confirmed that agreement yet. Other details include reciprocal access for beef exports with UK farmers gaining 13,000 metric tons of duty-free exports to the United States but with no changes to UK standards on food imports. The United Kingdom also committed to buy $10 billion of Boeing airplanes as part of the deal. All said, the agreement appears to not materially change the trade relationship versus what was in place after 2 April which means that tariffs on UK exports to the United States remain materially higher than the levels in place in 2024.

2. **The FOMC held interest rates constant, as expected.**

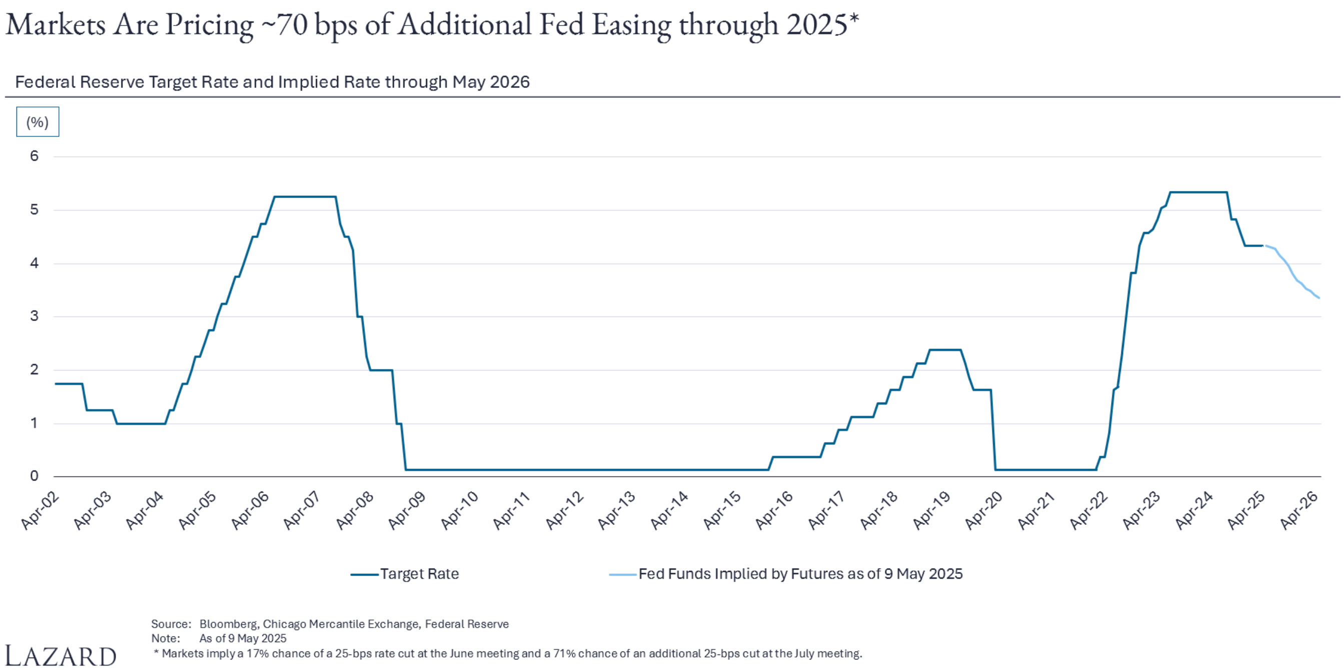
   The outlook: I expect no Fed rate cuts in 2025. The May FOMC meeting did not include an update to the Summary of Economic Projections that typically guides expectations for future meetings, and Fed Chair Jay Powell avoided any forward guidance in his press conference comments.

   Markets generally interpreted Powell's comments as being more hawkish than previously expected with fed funds futures pricing only 70 bps of easing by year end after the FOMC meeting versus 81 bps the day before the meeting.

   The details: The fed funds target rate remained at 4.25% to 4.50% with Powell asserting that policy is well positioned to react to changes in the economy that might warrant easing.

   Powell made clear that US tariff increases have been materially higher than expected and will increase inflation pressure. Powell also noted that unemployment is also likely to trend higher given pressure on companies to reduce costs to mitigate the pressure from higher tariffs.

   Powell indicated that if there is tension between the Fed's two mandates, it would decide which to prioritize based in part on how far each metric is from its target, e.g., how high inflation is versus unemployment. Given the Fed's own prioritization of inflation over employment for the last four years, I expect it to prioritize reaching the inflation target over reducing unemployment. The risk in my view is that since the pandemic, unemployment was at or below current levels while inflation was well above the Fed's 2% target. In a situation in which inflation approximates 4% and unemployment approaches 6%, this prioritization could change.



3. **China's exports and imports were stronger than expected in April.**

   The outlook: China's exports to the United States are likely to fall materially as tariffs cut into customer demand. While it is encouraging that the United States and China are beginning to talk in the days ahead about reducing trade frictions, the process will likely take time as neither side in the negotiations has high confidence in the other's willingness to comply with the terms of a trade deal.

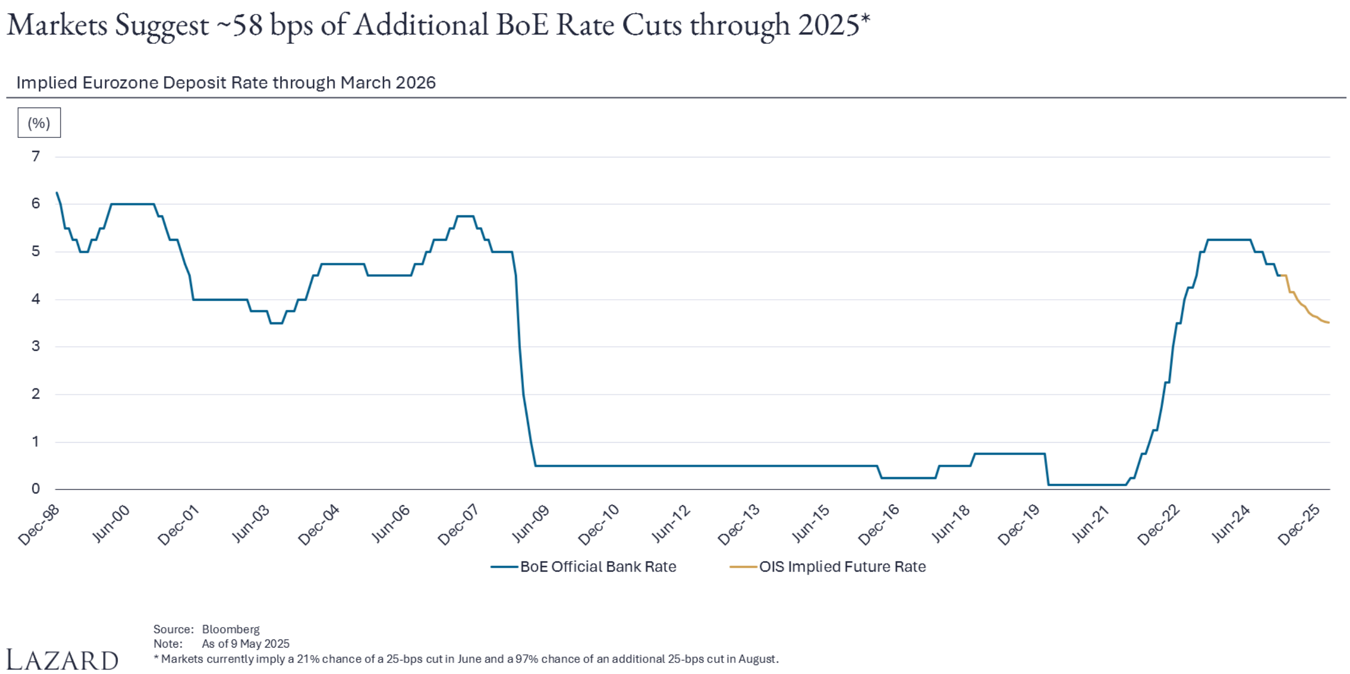
   The details: In April, total exports in US dollars rose 8.1% versus a consensus expectation for an increase of only 2.0%. Imports fell 0.2% versus expectations for a decline of 6.0%. Shipments to the United States fell 21% while imports from the United States fell 14%. Shipments to India and the ten countries in ASEAN rose by 21% while shipments to the European Union increased by 8.2%. The data this month will likely add to fears of trade either being transshipped via third-party countries to avoid US tariffs or being dumped into other countries due to lack of US demand.

4. **The BoE cut rates by 25 bps, but the three-way split in the vote was a surprise.**

   The outlook: Markets reduced the expected amount of easing after the BoE's meeting. Before the BoE policy announcement, the overnight index swap market implied 95 bps of easing by year end. After the announcement of the 25-bps rate reduction, markets were expecting only an additional 56 bps of easing, a 14-bps reduction in assumed easing.

   The details: The BoE Monetary Policy Committee (MPC) voted 5-4 to reduce rates by 25 bps to 4.25%, as expected. Two members voted to hold rates steady at 4.50% while two others voted to reduce rates by 50 bps. The remaining five members voted for the 25-bps rate reduction.

   The BoE's statement noted, "Based on the Committee's evolving view of the medium-term outlook for inflation, a gradual and careful approach to the further withdrawal of monetary policy restraint remains appropriate. The Committee will continue to monitor closely the risks of inflation persistence and what the evidence may reveal about the balance between aggregate supply and demand in the economy. Monetary policy will need to continue to remain restrictive for sufficiently long until the risks to inflation returning sustainably to the 2% target in the medium term have dissipated further. The Committee will decide the appropriate degree of monetary policy restrictiveness at each meeting."



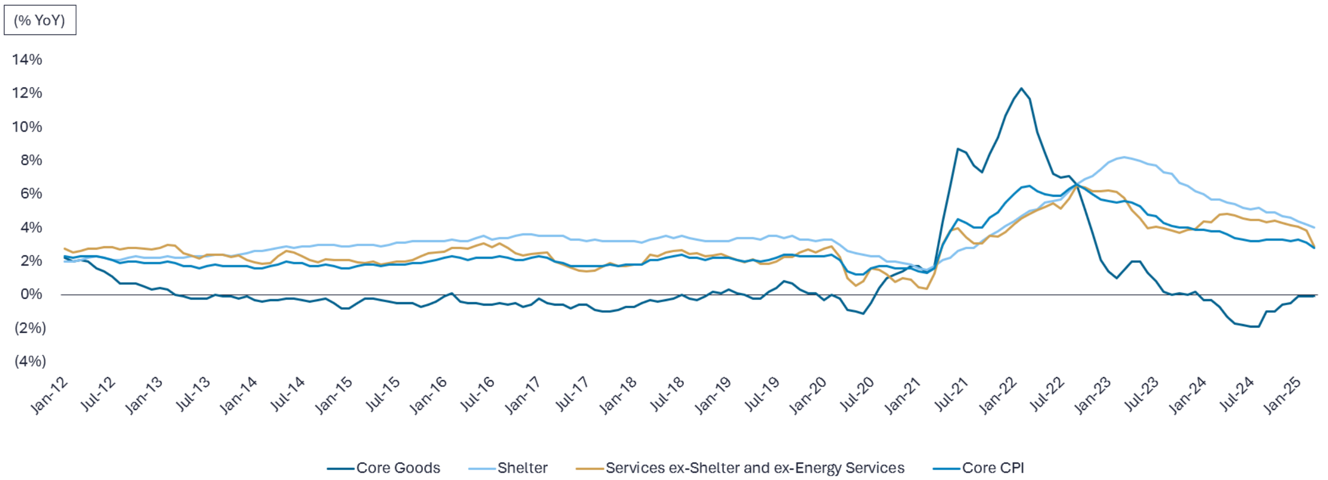
The Week Ahead

1. US Consumer Price Index (CPI) inflation is likely to reach a cyclical trough in April.

<u>The outlook:</u> Headline CPI inflation is expected to increase by 0.3% month-on-month (m-o-m) in April and 2.4% year-on-year (y-o-y). Core inflation is expected to increase by 0.3% m-o-m and 2.8% y-o-y. In March, a material deceleration in inflation for services ex-shelter helped drive core CPI inflation below expectations. However, in April, I expect to see increased inflation pressure from core goods with auto prices being a key driver of upside risk. The first chart below shows the three broad categories of prices captured in core CPI while the second graph shows the Manheim Used Car Price Index. In April, used car prices rose 2.7% m-o-m after months of relative stability. Given the impact of tariffs on new car prices, one should expect used car prices to adjust as well.

US Core CPI Inflation Is Likely to Trough in April before Reaccelerating

US Consumer Price Index Inflation for Key Categories

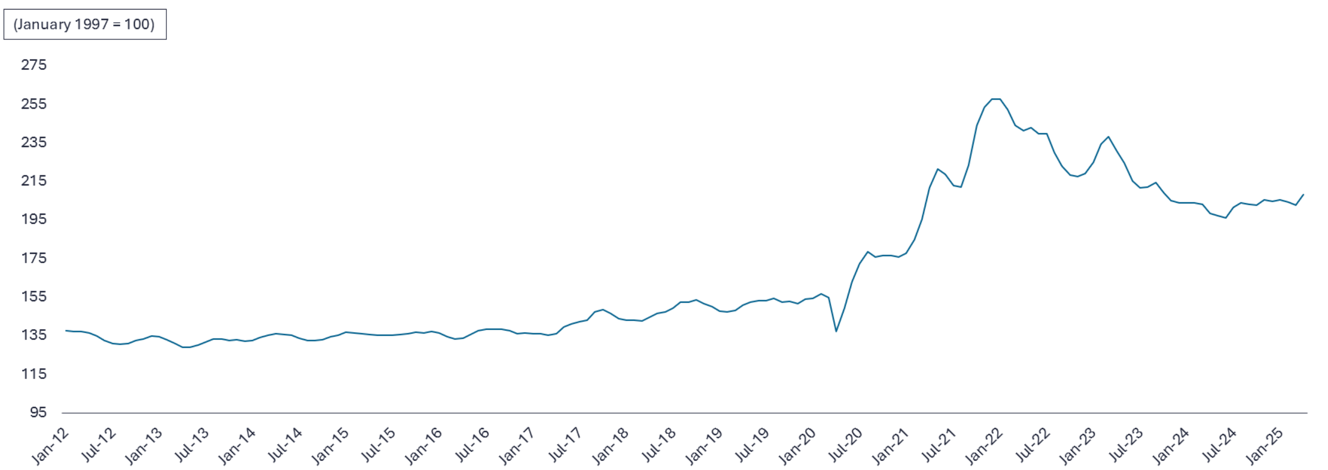


LAZARD

Source: Bureau of Labor Statistics, Haver Analytics
Note: As of March 2025
Core goods represent ~24% of core CPI, shelter represents ~44%, and other services ex-shelter and ex-energy services represent ~32%.

Rising Used Car Prices Could Add to Inflationary Pressure from Core Goods

Manheim Used Car Price Index



LAZARD

Source: Manheim, Haver Analytics
Note: As of April 2025

2. US retail sales growth is expected to decelerate in April.

<u>The outlook:</u> After delivering relatively strong numbers in Q1-25, retail sales growth is likely to slow in April partly reflecting consumers accelerating purchases to avoid tariffs. The control group, which excludes food services, auto-related sales, building materials, and gas stations, is expected to increase by 0.3% m-o-m versus a gain of 0.4% in the prior month.

3. **The University of Michigan Sentiment Index is expected to stabilize.**

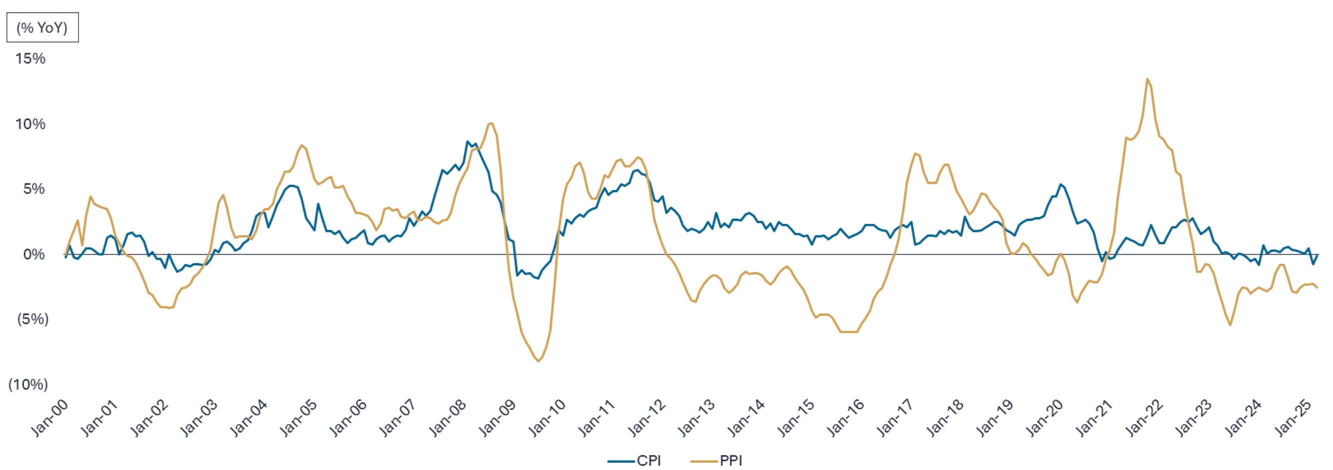
   The outlook: The University of Michigan Sentiment Index has fallen to 52.2 in April from 74.0 in December 2024, one of the steepest declines in the history of this metric. The preliminary figure for May is expected to rise slightly to 53.0. A key driver of the index level is likely to be inflation expectations which have risen sharply to 6.5% for one-year inflation expectations and 4.4% for 5- to 10-year inflation expectations.

4. **China will report CPI and Producer Price Index (PPI) inflation for the month of April.**

   The outlook: After 30 consecutive months in deflation, the PPI is likely to remain well below zero with consensus expectations at -2.8% y-o-y. CPI is expected to remain slightly in deflation at -0.1% y-o-y. China remains at risk of slipping further into deflation due to the reduced demand for exports to the United States driven by the weighted average tariff rate of 105% to 110% on goods exports.

China Inflation Is Undesirably Low with PPI Deflation for 30 Months and CPI ≤1% for 26 Months

China CPI and PPI



LAZARD

Source: Bloomberg, National Bureau of Statistics
Note: As of March 2025

5. **Japan will report preliminary GDP figures for Q1-25.**

   The outlook: Japan's Q1-25 GDP is expected to contract by 0.1% due to a significant drag from net exports. Private consumption is expected to rise 0.1% quarter-on-quarter (q-o-q) while business investment is expected to increase by 0.5% q-o-q.

6. **The United Kingdom will report preliminary GDP figures for Q1-25.**

   The outlook: UK Q1-25 GDP is expected to increase by 0.6% q-o-q and 1.2% y-o-y. The strong growth figures in the first quarter are largely attributable to one-off factors, with the BoE indicating in its monetary policy commentary this week that underlying GDP growth is likely closer to zero and is expected to decelerate to only 0.1% in Q2-25.

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