Macro Monthly

Economic insights and asset class views

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For global professional / qualified / institutional clients and investors

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Moment of clarity

- Risk assets rallied in July as trade uncertainty eased, despite a continued rise in the effective tariff rate.
- With policy uncertainty fading, market attention is shifting to economic data. Friday's employment report underscores that the economic consequences of recent policy shifts are only now becoming visible.
- Accelerated Fed easing is likely, which should help cushion the economy and markets. The Fed does not look 'behind the curve,' examining a broad set of macro indicators.
- Still, downside growth risks have increased, reinforcing the case for pairing risk assets with exposure to high-quality duration within a diversified portfolio.

There's a well-worn investing cliché that "markets hate uncertainty." While often repeated, it's somewhat tautological – uncertainty is intrinsic to investing, and a wider distribution of outcomes naturally demands higher risk premia. What's less mentioned, however, is the inverse: markets love a reduction in uncertainty, **even when the resolution of that uncertainty is not ideal.**

Nowhere is this more evident than in recent market reactions to US tariff policy. Whether deals with individual countries have been struck or not, tariffs have only moved in one direction – up. Yet, as the range of potential outcomes has narrowed and worst-case scenarios have been avoided, policy uncertainty has declined. A 15% tariff on European imports feels manageable when 50% was on the table just weeks ago. Risk assets have responded more to this reduction in uncertainty than to the tariffs themselves, as the left tail of the distribution has effectively been truncated.

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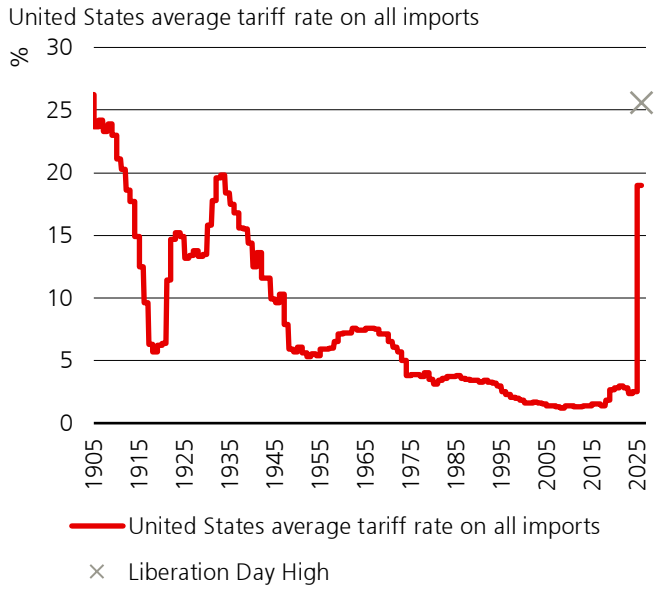
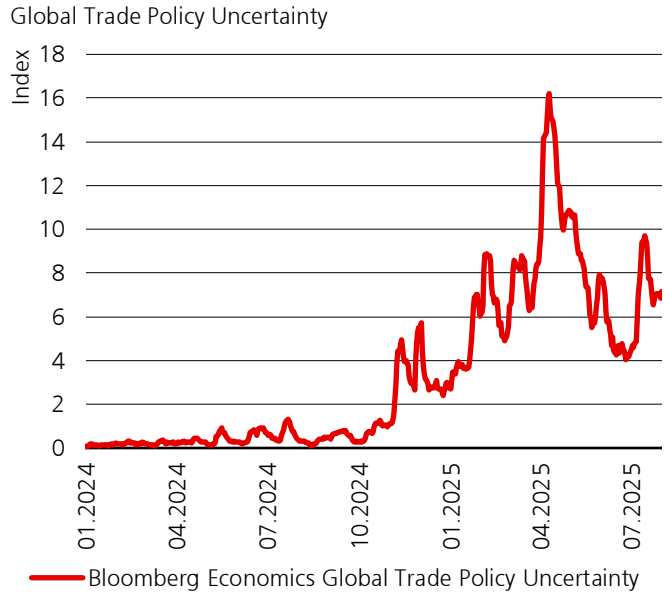
Exhibit 1: The effective tariff rate has been rising



Source: Tax Foundation, Macrobond, UBS Asset Management. Data as of August 2025.

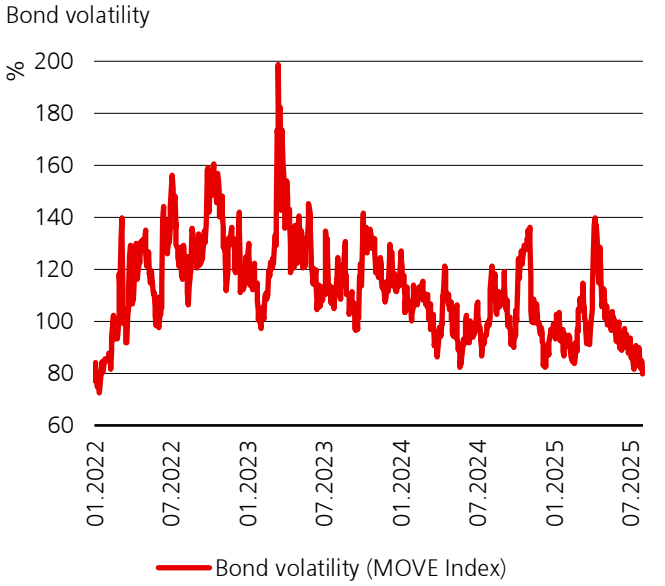
Exhibit 2: While trade policy uncertainty has drifted lower



Source: Bloomberg, UBS Asset Management. Data as of August 2025.

The passage of the One Big Beautiful Bill Act (OBBBA) has similarly brought clarity. Earlier this year, 10-year Treasury yields surged to 4.80% in part due to fears of unchecked fiscal expansion to fund Trump's extended tax cuts. But those elevated yields forced lawmakers to scale back their plans for fiscal expansion, which together with increased tariff revenues helped temper concerns about runaway deficits. While deficits remain high – 6%–7% of GDP for the foreseeable future – the market now has greater confidence that deficit expansion won't worsen. It's a far-from-ideal outcome, but one that has helped stabilize bond market volatility, which recently neared a cycle low.

Exhibit 3: Bond volatility near cycle lows



Source: Bloomberg, UBS Asset Management. Data as of August 2025.

This reduction in uncertainty matters not just for investors, but for companies as well. Greater clarity on tariffs enables even the most exposed importers to plan pricing strategies and adjust supply chains. The OBBBA also clarified tax treatment for capex and R&D, improving visibility for investment and cash management decisions. The ability to 'move on' can be a nice tailwind.

From policy uncertainty to economic reality

While some policy questions remain – sector-specific tariffs on semiconductors and pharmaceuticals, or potential secondary sanctions on Russian oil – the scope for major macro policy surprises from 'known unknowns' has narrowed. As a result, market focus is shifting to the economic data.

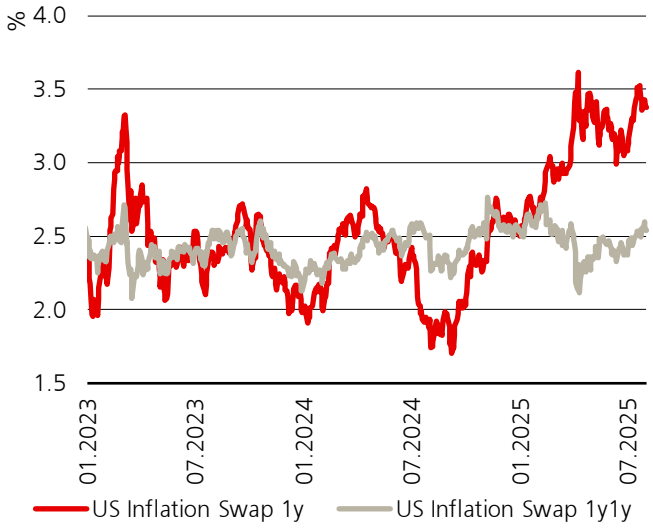
In the previous Macro Monthly, we asked whether markets could look through a weakening economy if policy shocks were already known and understood. Our answer was yes – providing the labor market held up.

On that front, the July employment report released Friday was a gut check. While the headline numbers weren't alarming – 73,000 jobs added vs. 100,000 expected, and unemployment at 4.25% (slightly above the 4.2% forecast) – the real surprise was a sharp 258,000 downward revision to May and June figures. This brought the three-month average job growth down from 150,000 to just 35,000.

Markets swiftly priced in a more aggressive path of Fed rate cuts, reflecting a labor market that now appears significantly softer than previously anticipated. Part of this reflects reduced labor supply, with declining immigration weighing on the workforce. Still, this shift likely clears the way for the Fed to begin cutting rates in September, despite valid concerns about rising inflation. Encouragingly, inflation expectations remain anchored: one-year inflation swaps reflect tariff impacts, but forward-looking expectations remain stable.

Exhibit 4: 1Y inflation expectations reflect tariffs, the market-pricing of forward looking inflation expectations beyond 1y are remarkably stable

US inflation swaps

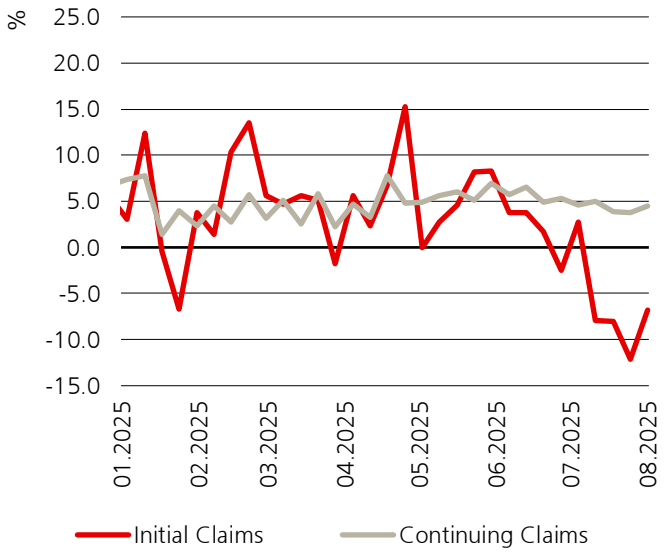


Note: US Inflation Swap 1y1y shows the swap contract starting in 1y and running for 1y.
Source: Bloomberg, UBS Asset Management. Data as of August 2025.

Is the Fed too late to prevent an unraveling of the labor market and recession? We don't think so. It's reasonable that hiring slowed in the spring amid post-Liberation Day uncertainty. But after an initial spike, jobless claims have been trending lower. The labor market remains low-churn, with limited hiring or firing. Nominal income growth remains solid. High-frequency indicators – like tax receipt growth and card spending – suggest consumers are holding up, as do corporate anecdotes.

Exhibit 5: Initial jobless claims spiked around the spring, but have dropped off in the summer

Jobless claims, % YoY



Source: Bloomberg, UBS Asset Management. Data as of August 2025.

Asset Allocation

In our view the 'muddle-through' economy should benefit from accelerated rate cuts, upcoming tax relief, and continued AI-driven capital investment.

We remain constructive on the medium-term outlook for risk assets. We believe greater policy clarity – even with lingering macro risks – is a strong tailwind. Corporate America has proven resilient through multiple shocks and continues to deliver on earnings. That said, we're entering a seasonally weaker period, and near-term data may be volatile, especially as markets are likely to have heightened focus on the Fed's reaction function. We think a market pullback would be normal – and could present a buying opportunity.

While we expect the US and global economy to cool but remain resilient, a sharper slowdown is still possible. Although there are ongoing concerns about government debt levels and persistent inflation, we remain confident that, in the event of a deeper economic slowdown, flight-to-safety flows which would support the Treasury market will take precedence over these issues. We remain short USD as the US economy and rates 'catch down' to the rest of the world. The muddle through economy is a good environment for carry, which we express in EM local currency debt. We continue to hold exposure to precious metals as a hedge against inflation expectations becoming de-anchored and any potential geopolitical shocks.

Asset class views

The chart below shows the views of our Asset Allocation team on overall asset class attractiveness as of 04 August 2025. The colored circles provide our overall signal for global equities, rates, and credit. The rest of the ratings pertain to the relative attractiveness of certain regions within the asset classes of equities, bonds, credit and currencies. Because the Asset Class Views table does not include all asset classes, the net overall signal may be somewhat negative or positive.

	Underweight			Overweight		
Global Equities						We are overweight equities on the back of solid earnings growth, a robust AI capex cycle, and expectations for upcoming Fed easing. We are monitoring the cooling in jobs growth, but with layoffs low, we think the economy is in a muddle-through phase as opposed to a sharp slowdown.
US						We expect US equities to outperform as high-quality stocks continue to drive strong earnings, and the weaker USD is a tailwind. Given recent labor market softness, continued US equity outperformance may require support from Fed rate cuts.
Europe						We are underweight European equities as earnings are weak relative to other regions, and the year-to-date EUR strength is a headwind. Within Europe, we continue to like European banks which are delivering good earnings growth.
Japan						Japan has seen better nominal GDP growth, resilient earnings and improved corporate governance, which are tailwinds. The potential for JPY strength and sharp rises in long JGB yields keep us neutral.
Emerging Markets						We are overweight EM equities as EM earnings are strong across most regions and supported by a weaker USD. The MSCI EM index is heavily weighted by North Asian tech giants which we expect to do well as the AI capex cycle pushes on.
Global Government Bonds						We are neutral duration as near-term inflation risk and increased bond supply globally should work against the slower growth profile we expect for the remainder of the year. Short-tenor bonds may offer protection against risk assets should growth weaken more materially.
US Treasuries						We are neutral on US duration as Treasuries face volatility from policy-induced changes. We believe the front end of the curve still offers good protection against a weaker labor market, as global debt supply puts upward pressure at the long end.
Bunds						We think the front of the German curve could rally on external growth risks but think fiscal spending will keep the curve steep.
Gilts						We are overweight Gilts on attractive valuations, slowing growth, and our expectation for the BoE to ease more than is priced.
JGBs						We are neutral Japanese government bonds. Although the BoJ is likely to hike more, we expect the BoJ will be slow to act as they evaluate the effects of tariffs on the economy. In the meantime, carry costs of shorting JGBs are elevated due to the low BoJ rate.
Swiss						We are neutral Swiss bonds. Valuations are historically expensive, and the market has already priced the SNB to cut rates into negative territory.
Global Credit						We think IG & HY credit spreads have marginal room for compression but still face the risk of material widening in case the economic outlook deteriorates more than expected. Regionally, we see Asia HY as offering the best risk-reward.
Investment Grade Credit						With IG spreads less than 80 bps to Treasuries, we see little room for further spread compression. Still, corporate fundamentals and all-in yields remain attractive outright.
High Yield Credit						US HY spreads have tightened back to year-to-date lows. While we expect spreads to remain tight amid improving corporate credit quality and strong investor inflows, we do not see much room for further spread compression.
EMD Hard Currency						We believe Asia HY provides the most attractive risk-adjusted carry across global credit segments. The share of Chinese issuers has dropped following a 3-year default cycle in real estate, making for a more diversified exposure.
FX						
USD						We are bearish on the USD but reduced our conviction as the USD reached oversold levels. That said, we still think the USD is in a downtrend, and weakness would accelerate if the Fed became more dovish in reaction to weakening job growth. We also see room for foreign investors to increase their FX-hedge ratios.
EUR						We think the EUR can be supported by increased FX-hedging flows and as the ECB signaled on-hold rates over coming meetings. We also like long EUR against GBP with rates likely to decline in the UK amid weakening employment data.
JPY						We are neutral on JPY as the BoJ's tightening remains gradual. That said, we think the JPY has plenty of room to strengthen against USD if the US economy weakens materially from here.
CHF						We are negative on CHF against other non-USD reserve currencies given its low yield and expensive valuation.
EM FX						We like BRL and INR, which both offer high volatility adjusted carry and a relatively low correlation to global equities.
Commodities						We are constructive on precious metals, and think silver has more room to catch up to gold. Oil risks are more balanced, as oversupply remains a headwind, while there are risks of secondary sanctions on Russian oil exports.

Source: UBS Asset Management Investment Solutions Macro Asset Allocation Strategy team as of 04 August 2025. Views are provided on the basis of a 3-12 month investment horizon, are not necessarily reflective of actual portfolio positioning and are subject to change.

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