Principal Hong Kong
2Q 2025 Market Outlook

Key themes for 2Q 2025

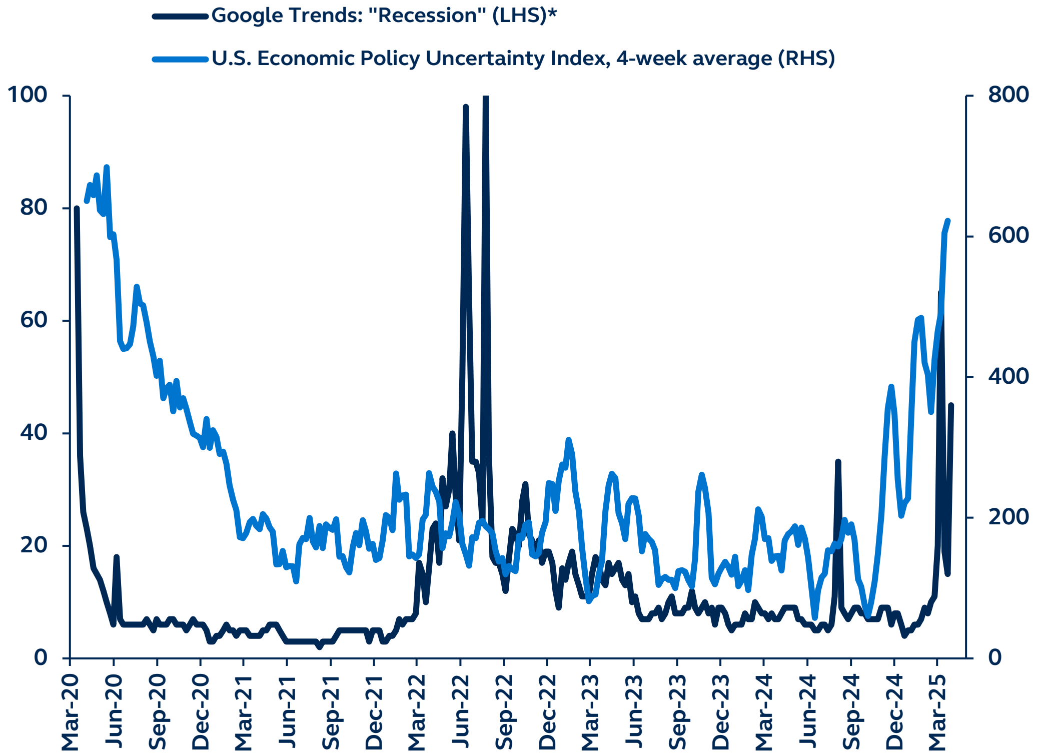
- **The global economy confronts upheaval as the U.S. looks to restructure international trade.**
  U.S. import tariffs have weakened the U.S. economy, while global economies sought to shore up their foundations to withstand the crosscurrents. Uncertainty is extraordinarily elevated and unlikely to clear immediately.
- **U.S. recession odds have spiked. Growth boosting policy measures are required to avoid recession.**
  The economy is being hit from multiple directions as consumers and businesses confront rising price pressures from import tariffs and labor market cracks. Deregulation and tax cuts will have to play a crucial role to offset the sharp rise in effective tariff rates if the U.S. is to skirt recession.
- **The Federal Reserve is biased to easy policy, but inflation fears will constrain the number of cuts.**
  Once the Fed has policy clarity, it will be able to focus on labor market concerns and resume rate cutting. Yet, inflation fears imply a shallow cutting cycle, providing only a limited stimulus injection into the U.S. economy.
- **U.S. equity markets to remain particularly challenged in the face of recession fears and tech woes.**
  U.S. economic growth is imperative if other sectors are to offset tech weakness. For now, the risk-off mood is likely to persist. International has outperformed as governments strengthen their economic foundations.
- **Fixed income is helping to weather the economic slowdown and market pullback.**
  Treasury yields may remain below 4% as recession fears persist. Credit spreads have widened but high-quality credit is performing its traditional role as ballast in investment portfolios.
- **The uncertain backdrop is challenging but prompts some important investor considerations.**
  Flows to money market funds have increased as investors defend against pullbacks and uncertainty. Global and cross-asset diversification remain crucial for capturing opportunities.

A global growth shock materializes

The U.S. economy is facing a significant policy-driven shock. Forceful policy actions in Europe and China would reduce the risks to global growth.

U.S. recession trends

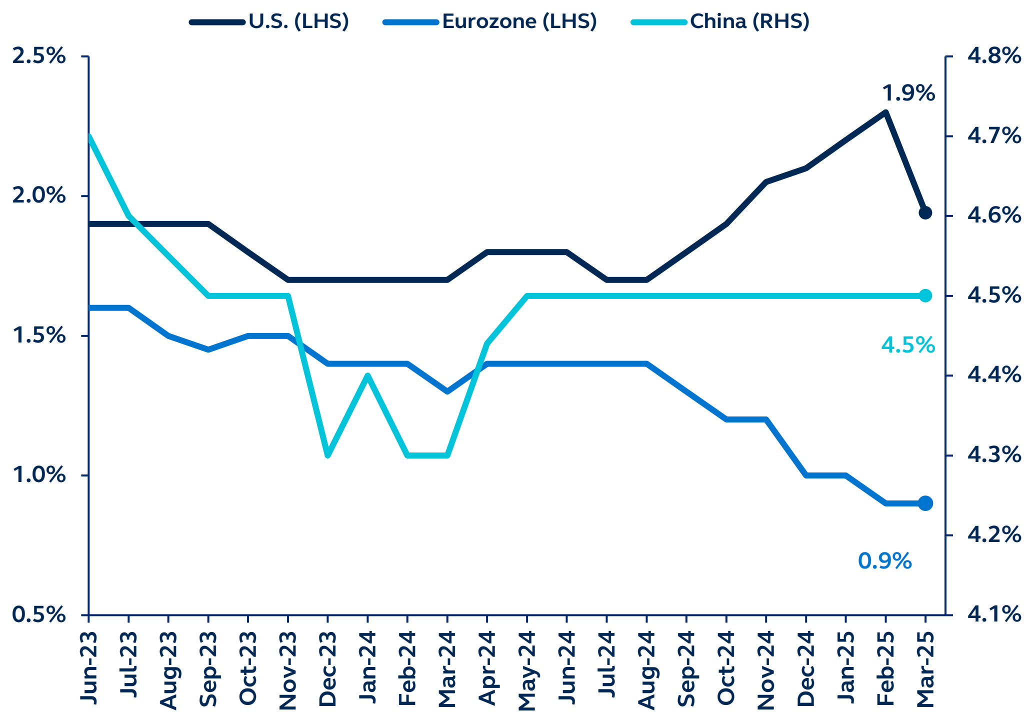
Google trends popularity level and Uncertainty Index level



Source: Bloomberg, Principal Asset Management. Data as of March 31, 2025. *Represents search interest relative to the highest point on the chart for the given region and time. A value of 100 is the peak popularity for the term. 50 means the term is half as popular.

2025 GDP forecast

Consensus 2025 real GDP growth forecasts for U.S., Eurozone and China



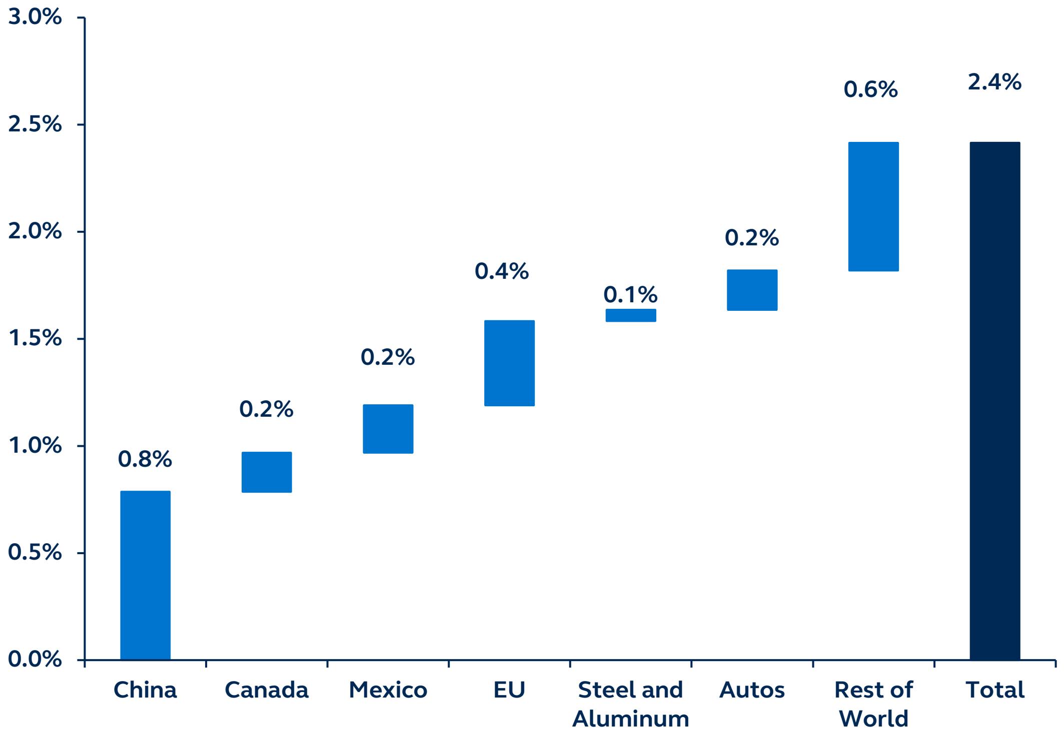
Source: Bloomberg, Principal Asset Management. Data as of March 31, 2025.

Principal® 信安

Tariffs—potentially a U.S. own goal

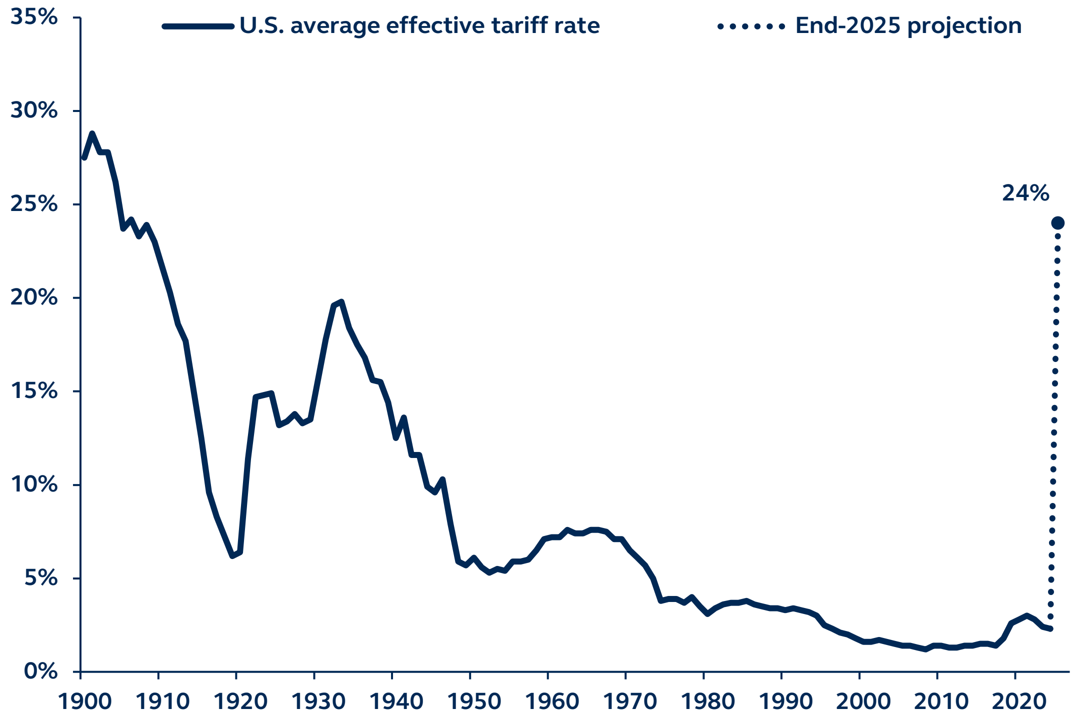
U.S. import tariffs, if maintained at current levels, are likely to lower GDP growth by 2.5%—raising the odds of recession.

Impact of tariff increases on U.S. GDP



Source: International Monetary Fund, World Trade Organization, Census Bureau, Bloomberg, Principal Asset Management. Data as of April 3, 2025.

U.S. average effective tariff rate



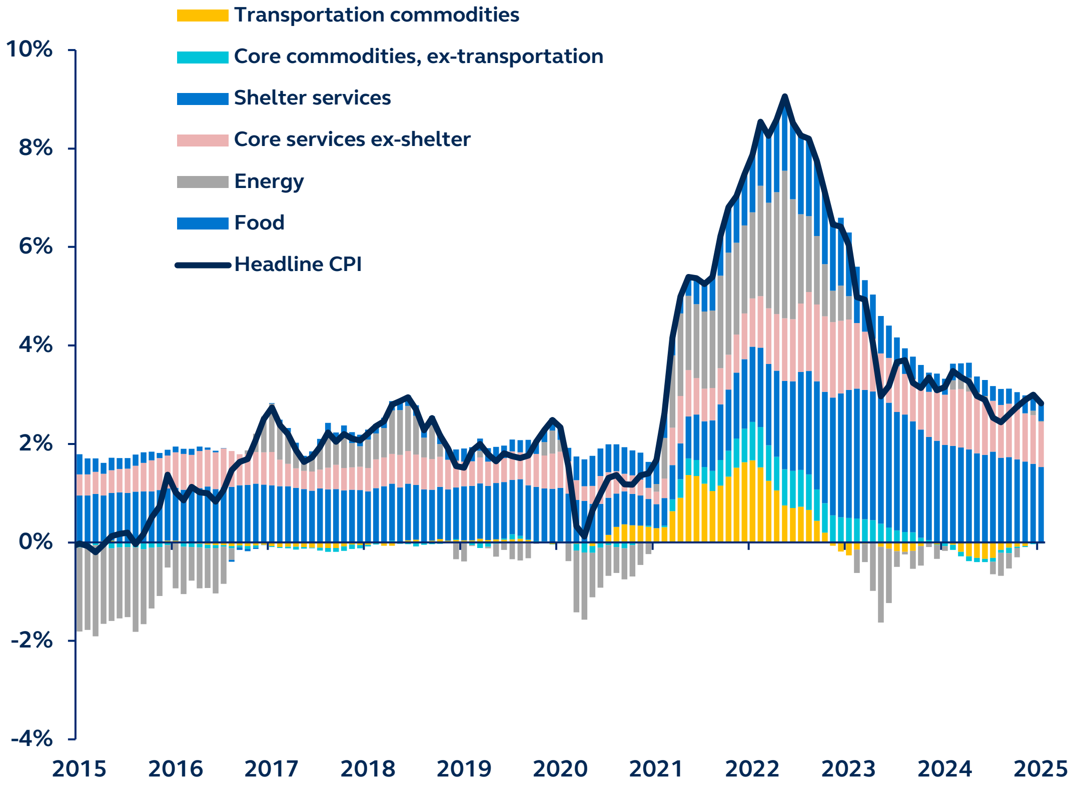
Source: United States International Trade Commission, Bloomberg, Principal Asset Management. Data as of April 3, 2025.

U.S. inflation: The start of a new problem?

If inflation expectations remain anchored, the Fed can focus on growth concerns, but there's no space for complacency.

Contribution to headline U.S. inflation

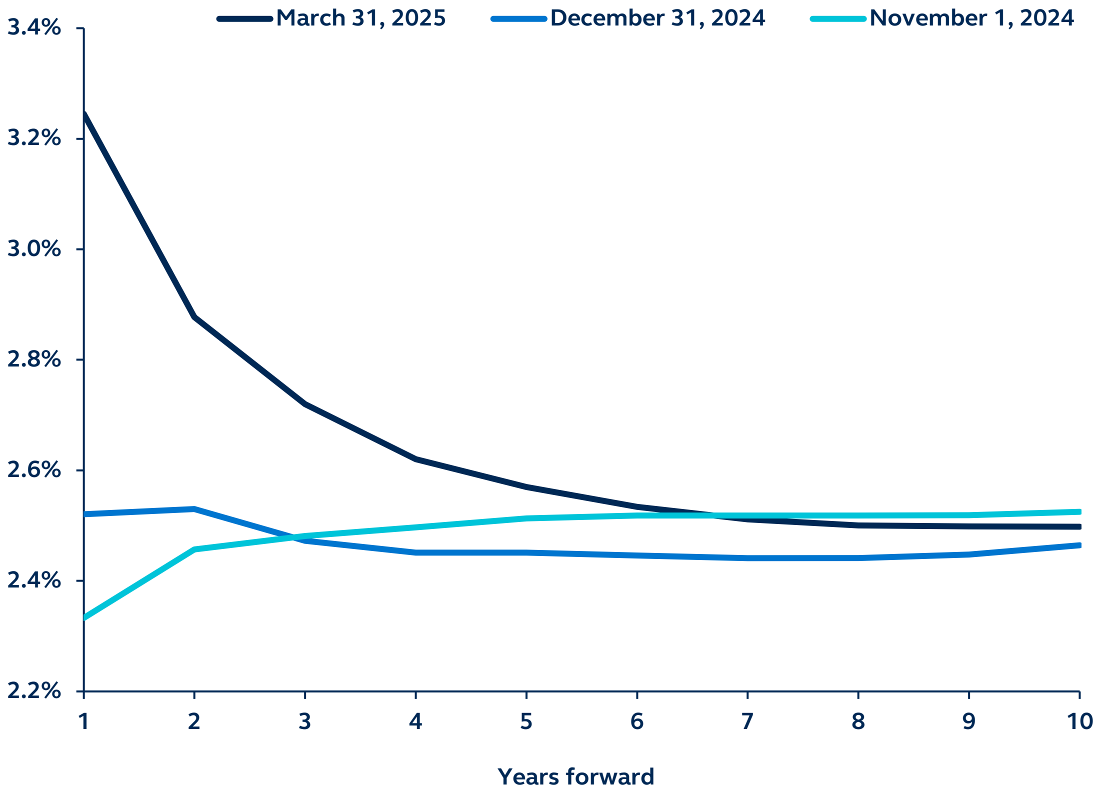
Year-over-year, January 2015–present



Source: Bureau of Labor Statistics, Principal Asset Management. Data as of March 31, 2025.

Change in market inflation expectations

Zero coupon inflation swap curve, by number of years forward



Source: Bloomberg, Principal Asset Management. Data as of March 31, 2025.

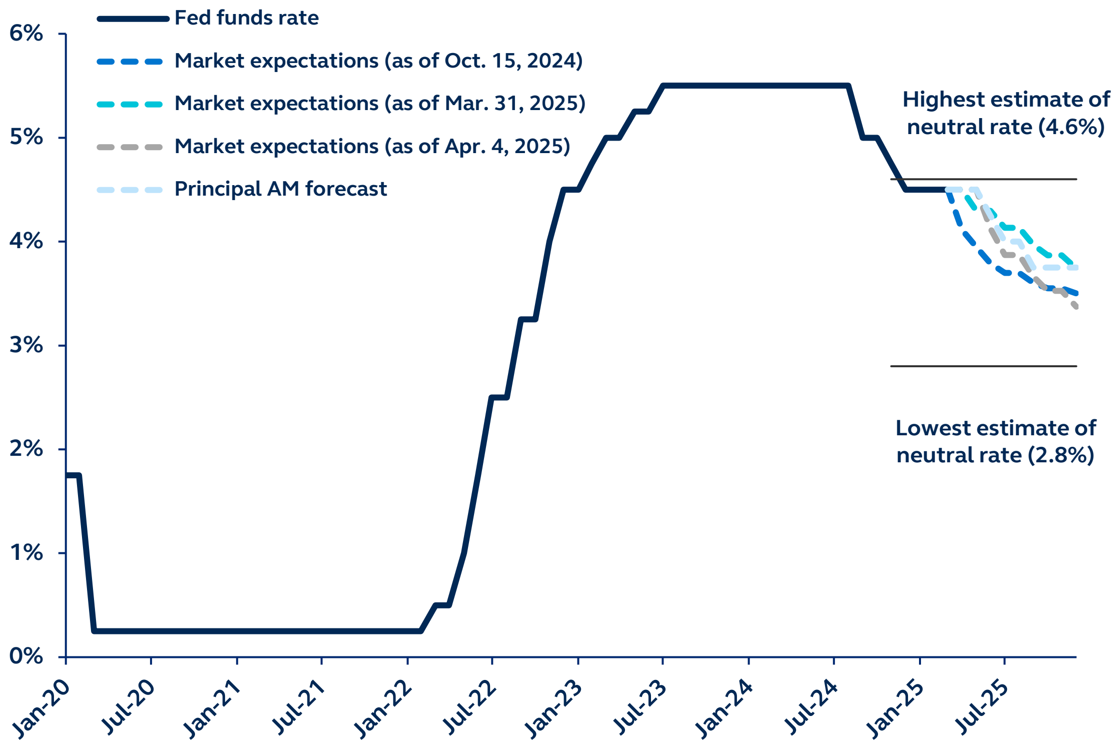
Principal® 信安

The Fed: Caught between inflation and a growth hit

Rising inflation complicates the Fed's policy decision-making. Provided inflation expectations remain anchored, policy easing is still plausible. We expect three to four rate cuts this year.

Federal Reserve policy rate path

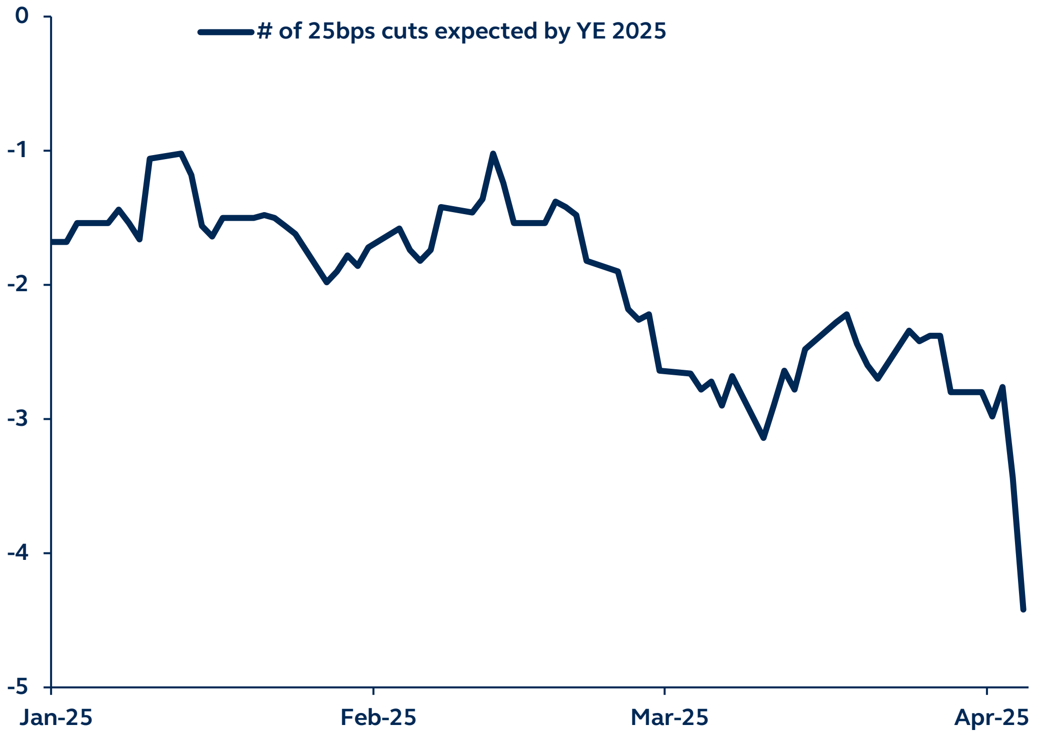
Fed funds rate and projections, 2020–present



Source: Federal Reserve, Bloomberg, Principal Asset Management. Highest and lowest neutral rate estimate levels are derived from a wide range of Wall Street analysts and models. Data as April 4, 2025.

Market Fed funds expectations

Number of 25bps moves expected by year-end December 2025, negative number = cut

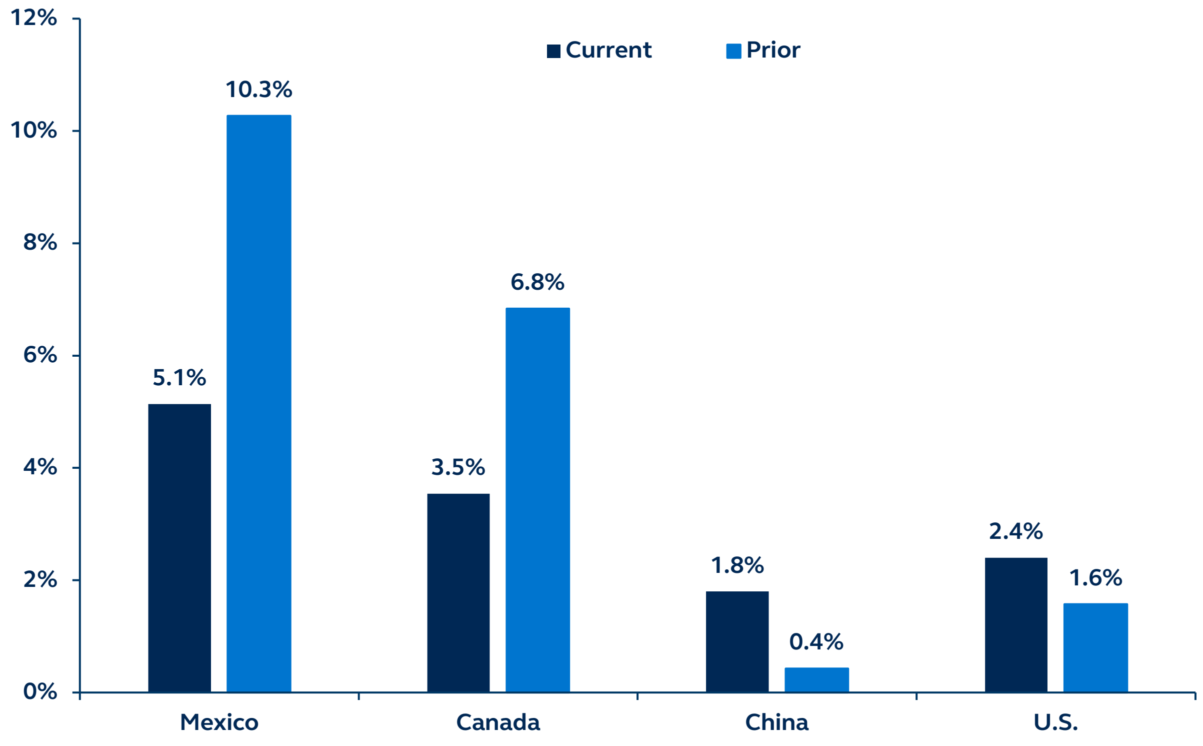


Source: Federal Reserve, Bloomberg, Principal Asset Management. Data as April 4, 2025.

Global economies brace for tariff impact

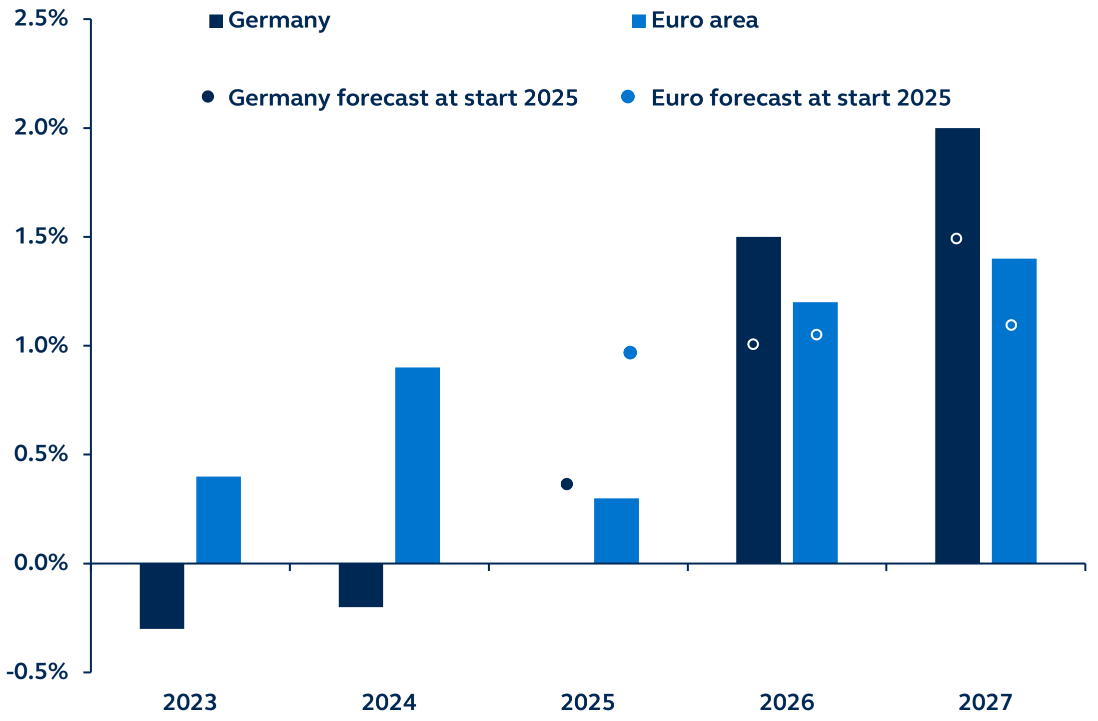
The impact of U.S. tariffs will be wide-reaching, prompting some economies to create their own insurance policies.

Potential tariff increase impact on GDP



Note: Prior estimates as of February 2, 2025 assumed a 25% tariff on Mexico and Canada, 10% tariff on China, and a 10% universal tariff on other trading partners. Current estimates now assume a 25% tariff on Mexico and Canada but with exclusions to USMCA goods and energy exemptions for Canada, a 54% tariff on China, a 20% universal tariff on other trading partners, and a 25% tariff on aluminum and steel. Source: International Monetary Fund, World Trade Organization, Census Bureau, Bloomberg, Principal Asset Management. Data as of April 2, 2025.

Germany and Euro area GDP growth forecast revisions



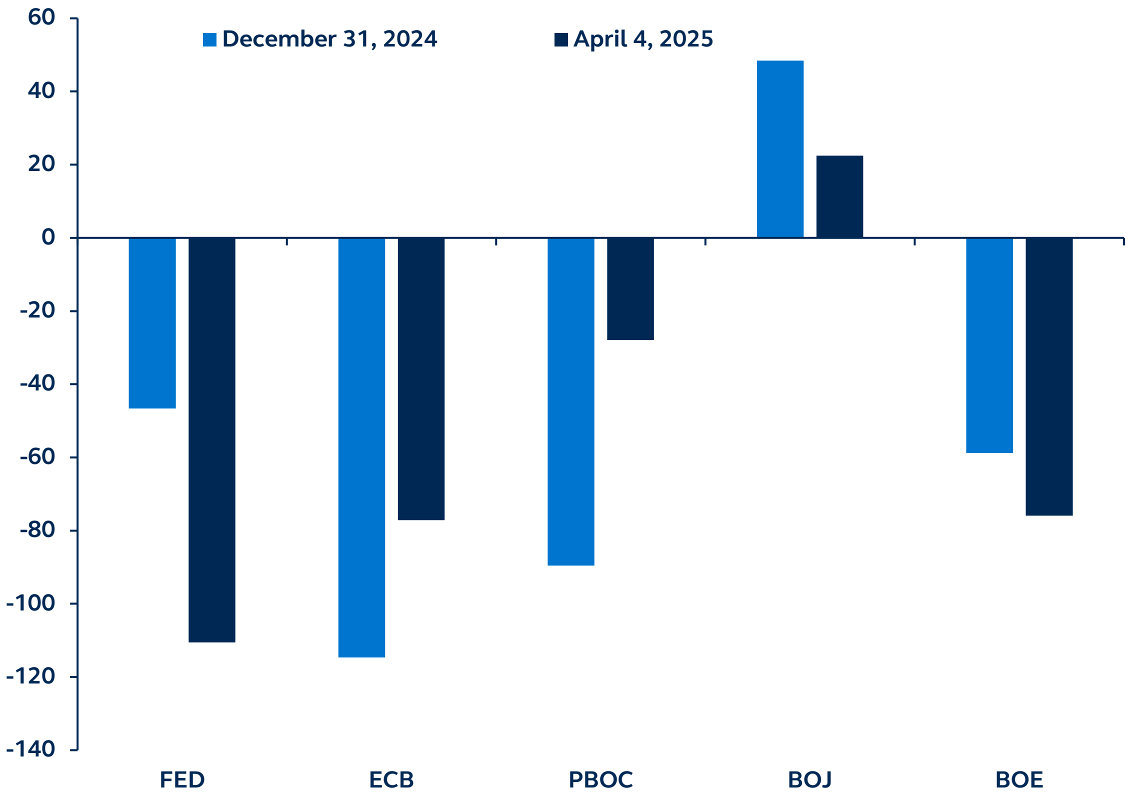
Source: Bloomberg, Principal Asset Management. Data as of April 4, 2025.

The U.S. dollar—facing a global backlash

U.S. dollar weakness will likely persist unless recession concerns fade back, or negative global sentiment towards the U.S. begins to lift.

Market priced rate action in one year

Expected policy rate move in next 12m for major central banks, basis points



Source: Bloomberg, Principal Asset Allocation. Data as of April 4, 2025.

U.S. dollar Spot Index

Source: Bloomberg, Principal Asset Management. Data as of April 4, 2025.

Principal® 信安

Investment Perspectives

Defense and diversification in a disrupted cycle

With policy shocks roiling markets and global growth expectations, investors should pivot toward caution and quality

Equities *Lean into quality and global breadth as volatility rises*

- Emphasize fundamentally sound companies with strong free cash flows less prone to economic headwinds
- Explore opportunities beyond the Mag 7, including tactical exposure to small- and mid-cap stocks
- Narrowing valuation differentials suggest a broadening global opportunity set

Fixed income *High-quality credit to serve as ballast amid widening spreads and weak sentiment*

- Increase allocation to investment-grade (IG) credit with strong balance sheets
- Extend duration selectively—attractive hedge in a slowing growth environment
- Maintain flexibility for potential spread compression entry points
- Consider deploying cash assets in higher-yielding income options, minimizing reinvestment risks

Alternatives *Pursue less correlated exposures*

- Prioritize real return strategies in a stagflationary risk scenario
- REITs and infrastructure remain compelling amid falling yields and defensive rotation

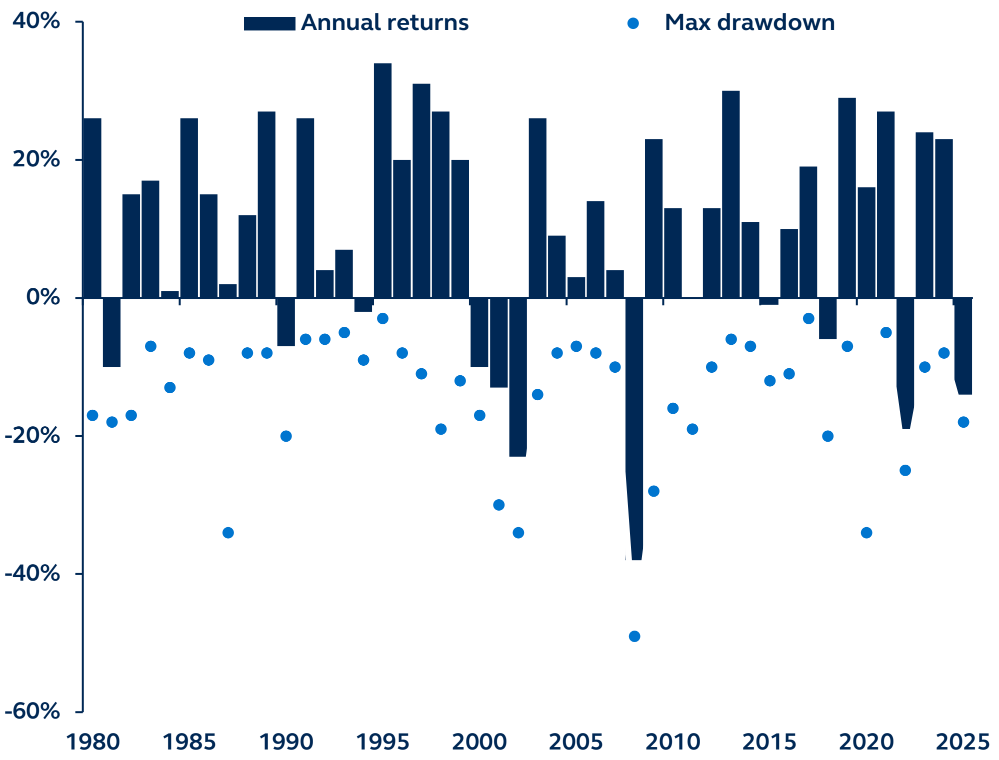
Equities

U.S. equities: Searching for the flow

U.S. markets are likely to remain in a risk-off mode until economic fears dissipate. Global markets, supported by policy stimulus, are looking relatively stronger.

Annual returns and pullbacks

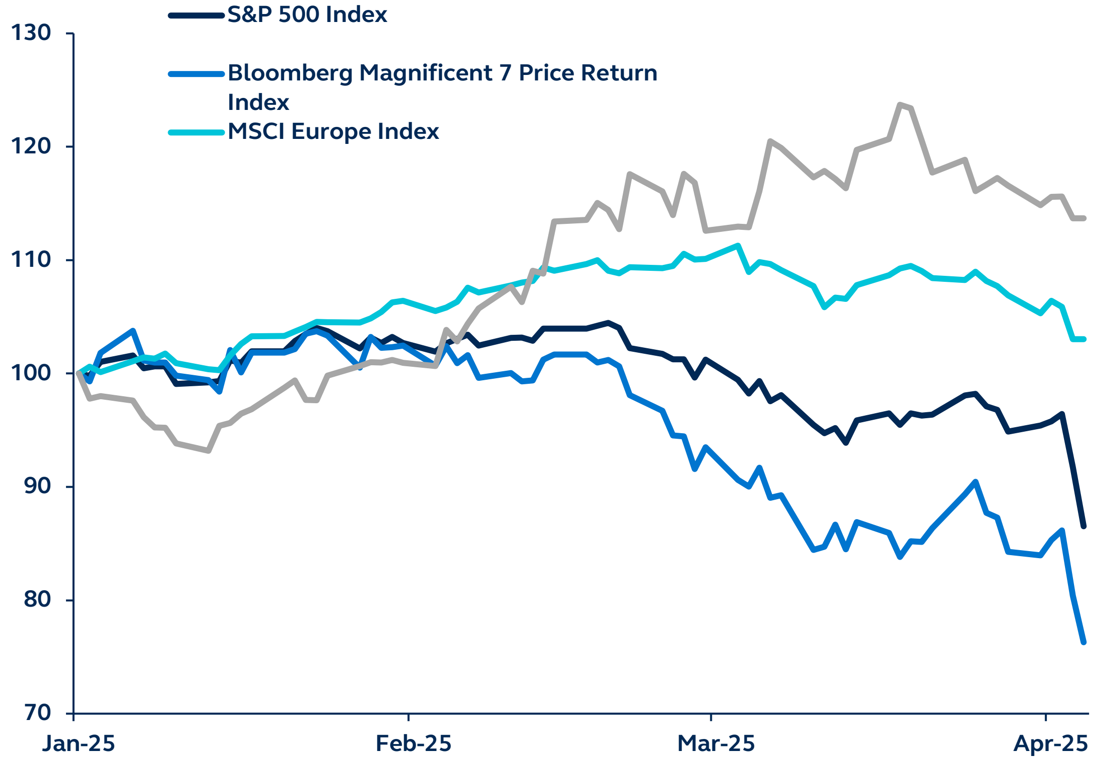
S&P 500 Index price return, max drawdowns represents the biggest intra-year decline



Source: Clearnomics, Standard & Poor's, Bloomberg, Principal Asset Management.
Data as of April 7, 2025

Magnificent 7 performance vs. major indices YTD

Index price return, rebased to 100 at January 1, 2025



Source: Bloomberg, Principal Asset Management. Data as of April 4, 2025.

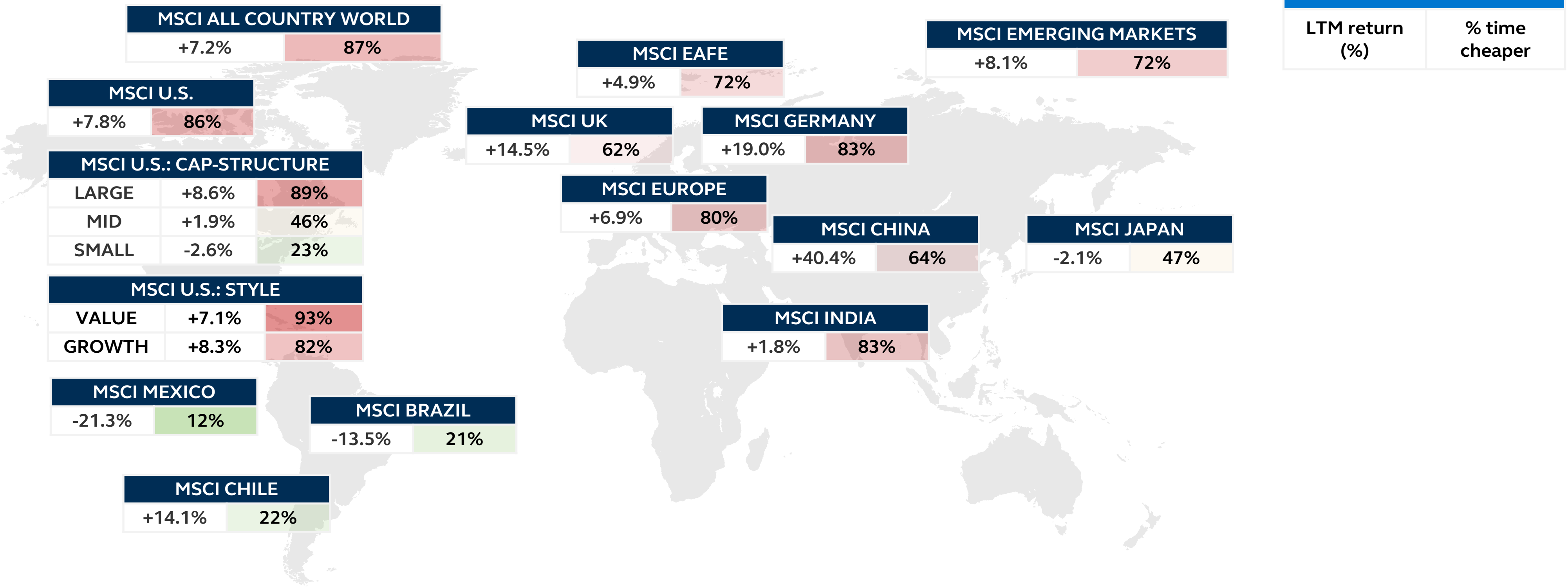
Principal® 信安

Global valuations: Investors finally take notice

Valuation differentials have narrowed as global diversification proves its worth. The global opportunity set has broadened.

Global equity returns and valuations

Last twelve months returns and % of the times the Index been cheaper relative to its history since 2003, MSCI indices



Source: FactSet, Bloomberg, MSCI, Principal Asset Allocation. LTM (last twelve months) returns are total return and in USD terms. % Time Cheaper is relative to PAA Equity Composite Valuation history. PAA Equity Composite Valuation is a calculated measure, comprised of 60% price-to-earnings, 20% price-to-book and 20% to dividend yield. Composite started in 2003. EAFE is Europe, Australasia, Far East. See disclosures for index descriptions. Data as of March 31, 2025.

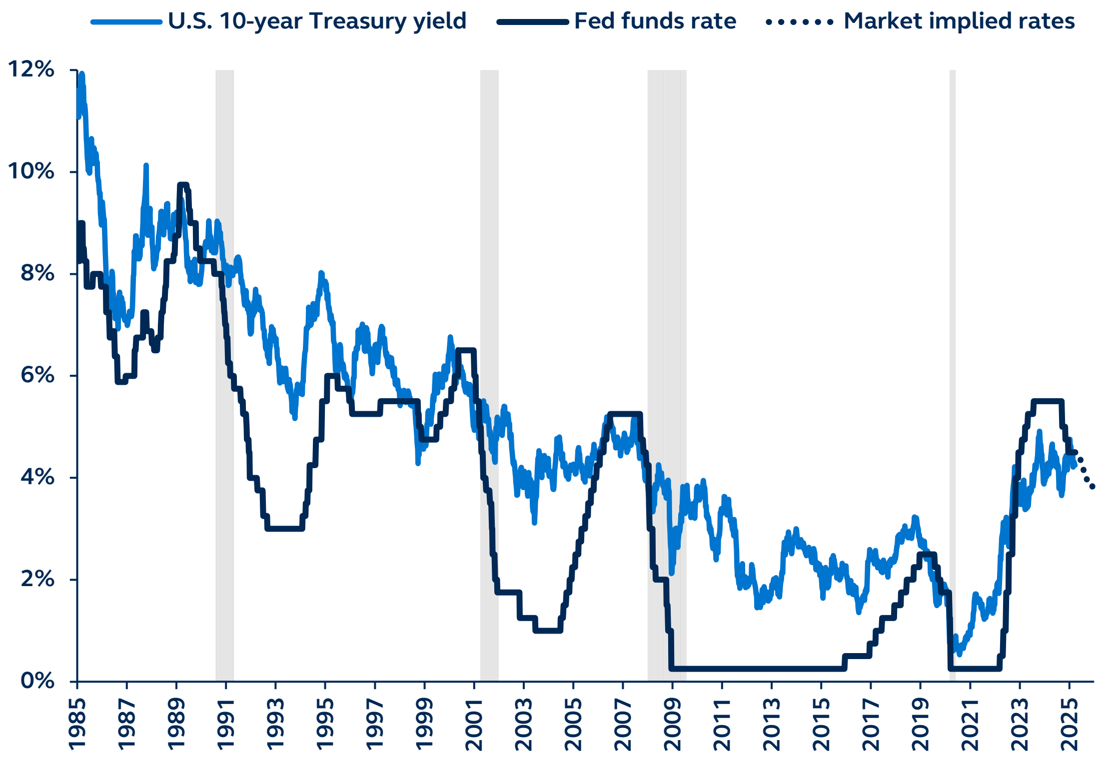
Fixed Income

U.S. bonds caught in the growth/inflation crosshairs

U.S. bond yields may trend lower as growth weakens, although rising inflation may cap the rally. European yields have likely hit their ceiling as tariff effects are realized.

Fed funds rate and U.S. 10y Treasury bond yield

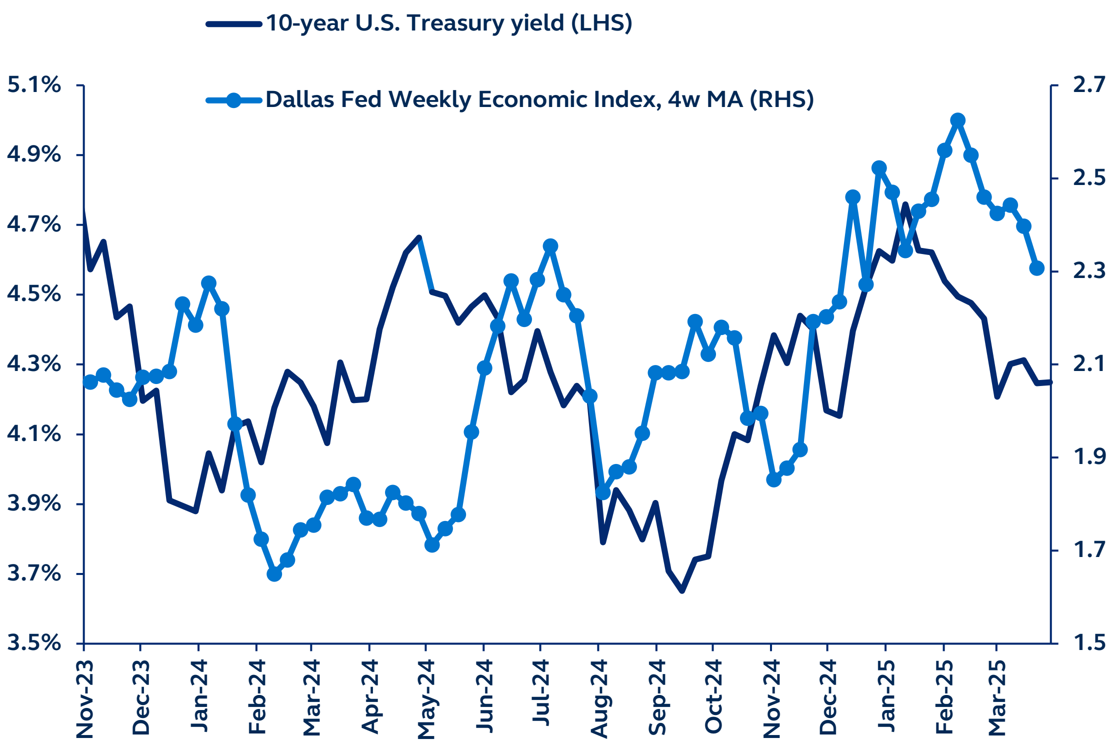
Recessions are shaded, 1985–present



Source: Federal Reserve, Bloomberg, Principal Asset Allocation. Data as of March 31, 2025.

10-year Treasury yield and economic activity

November 2023–present



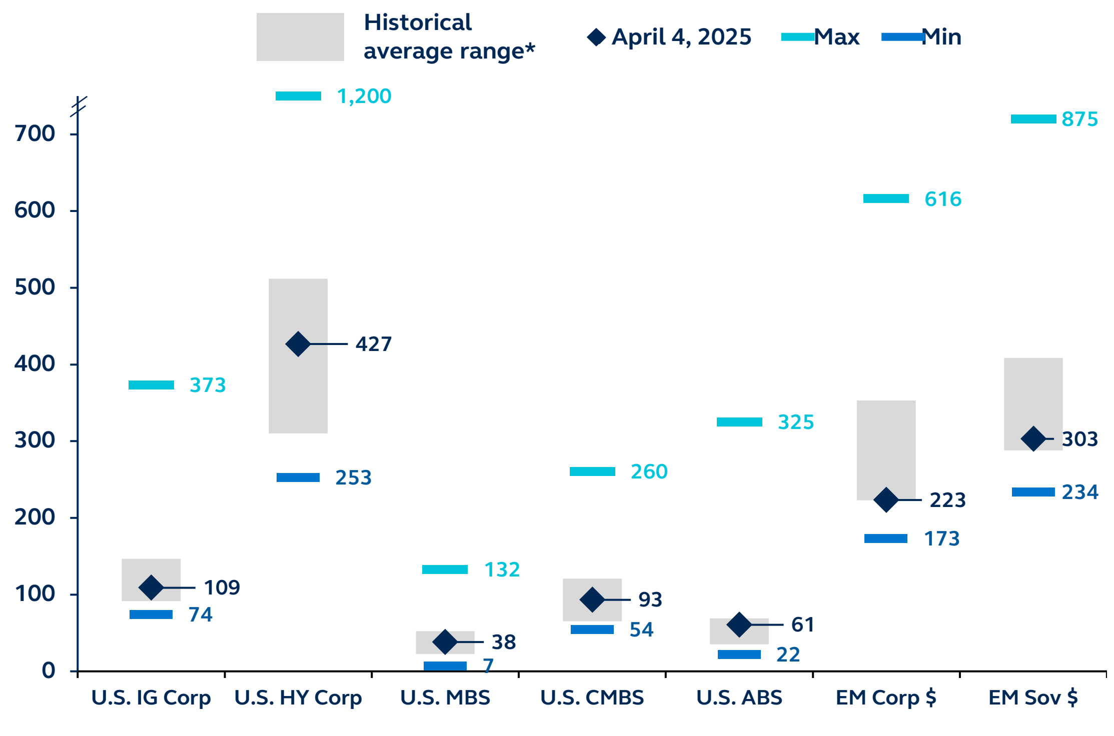
Source: Bloomberg, Principal Asset Management. Data as of March 31, 2025.

Recession fears call for focus on high-quality credit

Credit spreads have widened sharply and could widen further as economic pressures persist. Given recession risks, focusing on high quality credit will enable fixed income to perform its ballast role.

Historical spread range over the past 10 years

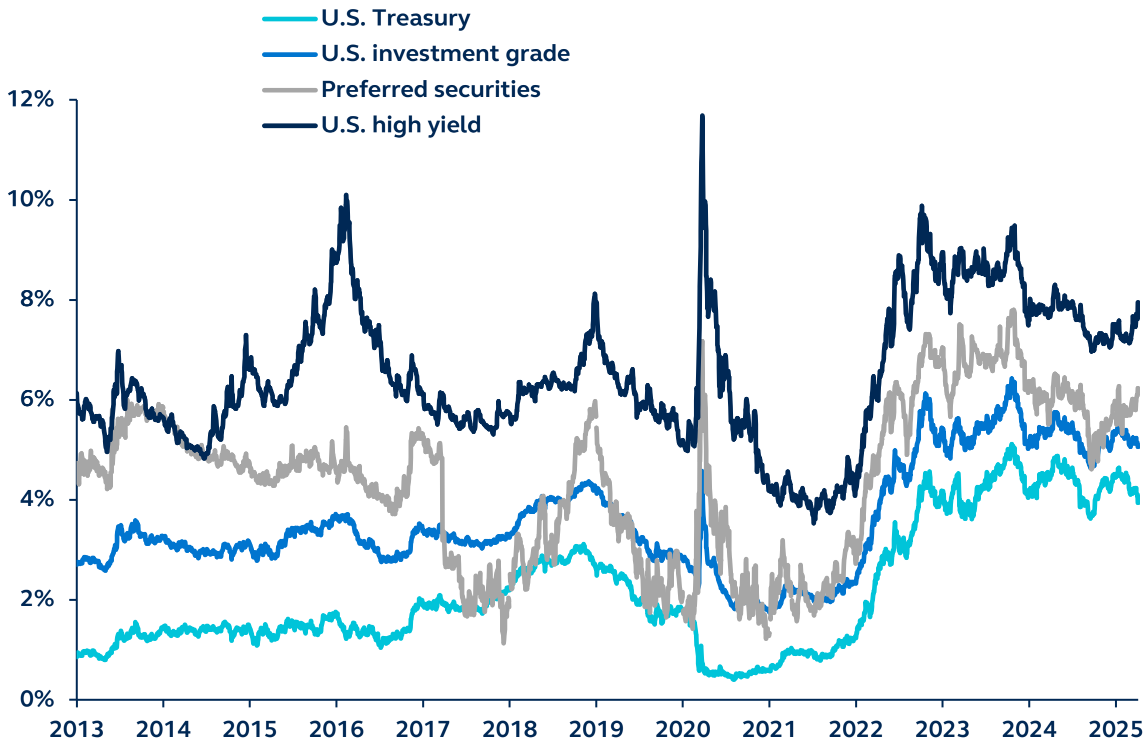
Option-adjusted-spread, basis points, 2015–present



*Bars in the chart indicate the OAS range one standard deviation above and below the historic average for each asset class. Source: Bloomberg, Principal Asset Management. Data as of April 4, 2025.

Yield comparison

Yield-to-worst, 2013–present



Source: J.P. Morgan, Principal Asset Management. Data as of April 4, 2025.

Principal® 信安

DISCLOSURES

Investment involves risks. Past performance of any particular fund or product mentioned in this document is not indicative of future performance of the relevant fund or product, and the value of the each fund or product mentioned in this document may go down as well as up. You should not invest solely in reliance on this document. There is no assurance on investment returns and you may not get back the amount originally invested.

This material may contain ‘forward looking’ information that is not purely historical in nature. Such information may include, among other things, projections and forecasts. There is no guarantee that any forecasts made will come to pass. Reliance upon information in this material is at the sole discretion of the reader.

Equity investments involve greater risk, including higher volatility, than fixed-income investments. Fixed-income investments are subject to interest rate risk; as interest rates rise their value will decline. International and global investing involves greater risks such as currency fluctuations, political/social instability and differing accounting standards. Potential investors should be aware of the risks inherent to owning and investing in real estate, including value fluctuations, capital market pricing volatility, liquidity risks, leverage, credit risk, occupancy risk and legal risk. Non-investment grade securities offer a potentially higher yield but carry a greater degree of risk. Risks of preferred securities differ from risks inherent in other investments. In particular, in a bankruptcy preferred securities are senior to common stock but subordinate to other corporate debt. Emerging market debt may be subject to heightened default and liquidity risk. Risk is magnified in emerging markets, which may lack established legal, political, business, or social structures to support securities markets. Small and mid-cap stocks may have additional risks including greater price volatility. Treasury inflation-protected securities (TIPS) are a type of Treasury security issued by the U.S. government. TIPS are indexed to inflation in order to help investors from a decline in the purchasing power of their money. As inflation rises, rather than their yield increasing, TIPS instead adjust in price (principal amount) in order to maintain their real value. Inflation and other economic cycles and conditions are difficult to predict and there Is no guarantee that any inflation mitigation/protection strategy will be successful. Contingent Capitals Securities may have substantially greater risk than other securities in times of financial stress. An issuer or regulator’s decision to write down, write off or convert a CoCo may result in complete loss on an investment. Real assets include but not limited to precious metals, commodities, real estate, land, equipment, infrastructure, and natural resources. Each real asset is subject to its own unique investment risk and should be independently evaluated before investing. As an asset class, real assets are less developed, more illiquid, and less transparent compared to traditional asset classes.

You should consider your own risk tolerance level and financial circumstances before making any investment choices. If you are in doubt as to whether a certain fund or product mentioned in this document is suitable for you (including whether it is consistent with your investment objectives), you should seek legal, financial, tax, accounting and other professional advice to ensure that any decision made is suitable with regards to that your circumstances and financial position,and choose the fund(s)/product(s) suitable for you accordingly.

The information contained in this document has been derived from sources believed to be accurate and reliable as of the date of publishing of this document, and may no longer be true, accurate or complete when viewed by you. The content is for informational purpose only and does not constitute an offer, a solicitation of an offer or invitation, advertisement, inducement, representation of any kind or form whatsoever or any advice or recommendation to enter into any transactions in respect of the funds/products referred to in this document. This document is not intended to be relied upon as a forecast, research, or investment advice regarding a particular investment or the markets in general, nor is it intended to predict or guarantee the performance of any investment. The information does not take account of any investor’s investment objectives, particular needs or financial situation. You should not consider the information as a comprehensive statement to be relied upon. All expressions of opinion and predictions in this document are subject to change without notice.

All figures shown in this document are in U.S. dollars unless otherwise noted.

Subject to any contrary provisions of applicable law, neither the companies, nor any of their affiliates, nor any of the employees or directors of the companies and their affiliates, warrants or guarantees the accuracy of the information contained in this document, nor accepts any responsibility arising out of or in connection with any errors or omissions of the contents set out in this document.

Principal Asset Management is the global investment management business for Principal Financial Group® and includes the asset management operations of the following : Principal Global Investors, LLC; Principal Real Estate Investors, LLC; Principal Real Estate Europe Limited and its affiliates; Spectrum Asset Management, Inc.; Post Advisory Group, LLC; Origin Asset Management, LLP; Claritas Investimentos; Principal Global Investors (Europe) Limited; Principal Global Investors (Singapore) Ltd.; Principal Global Investors (Australia) Ltd.; Principal Global Investors (Japan) Ltd.; Principal Asset Management Company (Asia) Ltd., and include assets where we provide model portfolios. Marketing assets under management include certain assets that are managed by Principal International and Retirement and Income Solutions (RIS) divisions of Principal.

This document has not been reviewed by the Securities and Futures Commission.

This document is issued by Principal Asset Management Company (Asia) Limited.

Reference number: 4428348

Principal® 信安