Flash Economics

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In reality, nothing is investable for a European in the United States

In the United States, we can expect

- Further depreciation of the U.S. Dollar against the Euro, as short-term interest rates fall in the United States ;
- A downward correction in equity markets, particularly in the Information Technology sector, due to the slowdown in growth and disappointment over the profitability of investments in Artificial Intelligence;
- A rise in long-term interest rates, due to the size of the public deficit and the rapid increase in the public debt ratio.

This means that a European investor must anticipate losses on all the American assets he holds (short-term securities with the depreciation of the U.S. Dollar, equities with the fall in stock market indices and the depreciation of the U.S. Dollar, bonds with the rise in interest rates and the depreciation of the U.S. Dollar). Hedging the currency risk reduces the return on short-term securities and bonds, leaving the effects of falling stock market indices and rising long-term interest rates intact.

Patrick Artus
Senior Economic Advisor
patrick.artus-ext@ossiam.com
@PatrickArtus
Patrick Artus

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Three forthcoming developments on US financial markets

1- Further depreciation of the U.S. Dollar against the Euro

The U.S. Dollar's exchange rate against the Euro should continue to depreciate (**Chart 1**), **due to the forthcoming cut in US short-term interest rates**, particularly following Jerome Powell's departure from the Federal Reserve, which is anticipated by financial markets (Chart 2A) but has not yet translated into a cut in 2-year interest rates (Chart 2B).

Chart 1
Euro/dollar exchange rate (EUR 1 = USD...)

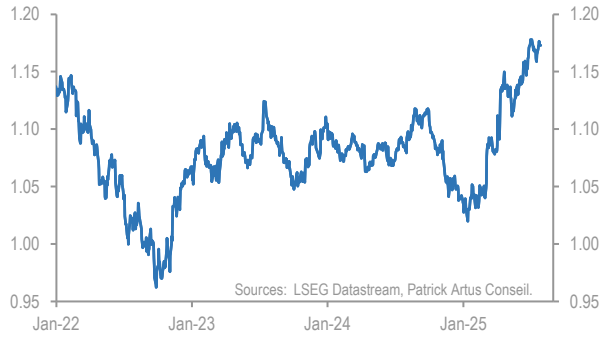
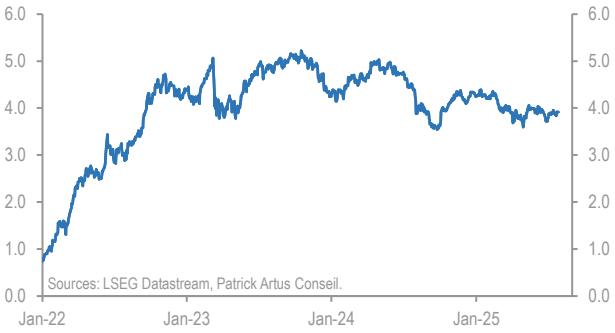


Chart 2A
United States: Eurodollar contracts (3-month)



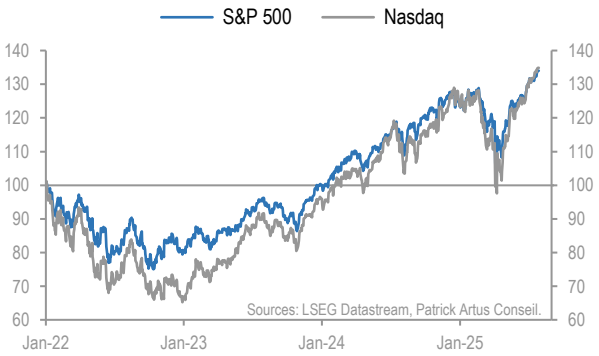
Chart 2B
United States: Interest rate on 2-year government bonds (as %)



2- Downward correction in the US equity market

The US equity market has resumed its upward march, following the decline in April 2025 (**Chart 3**).

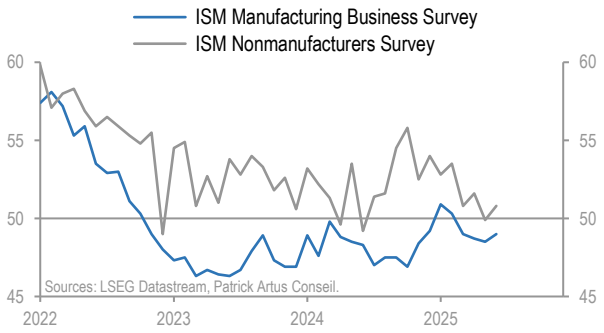
Chart 3
United States: Stock market indices (01.01.2022 = 100)



It is almost certain that **this market will undergo a downward correction as a result of**:

- **the slowdown in growth in the United States** (**Chart 4**), linked to the rise in inflation caused by tariffs;

Chart 4
United States: Manufacturing and Nonmanufacturers PMI (indices)



- **The high valuation** of US equities (**Chart 5**);

Chart 5
P/E ratio

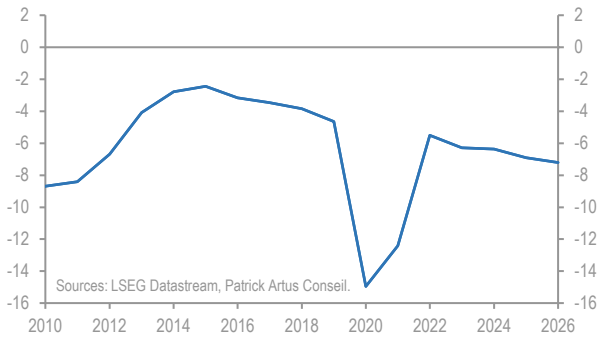


- **Future disappointment over the profitability of investments in Artificial Intelligence (AI)**, which are enormous (more than $400 billion in 2025 for Meta, Alphabet, Apple, Amazon and Microsoft), while AI is open source and the major US technology companies are competing to develop their AI models by over-investing.

3- Rising long-term interest rates in the United States

The tax cuts passed by Congress (in the Big Beautiful Bill) are far from being offset by the rise in customs duties and the fall in health spending. The result will be a sharp rise in the public deficit (around $400 billion a year), taking **the public deficit above 7% of GDP** from fiscal year 2025-2026 (**Chart 6**).

Chart 6
United States: Budget deficit (as % of nominal GDP)



As a result, there will be an oversupply of government securities, **leading to a rise in long-term interest rates** (**Chart 7**).

Chart 7
United States: Interest rate on 10-year government bonds (as %)

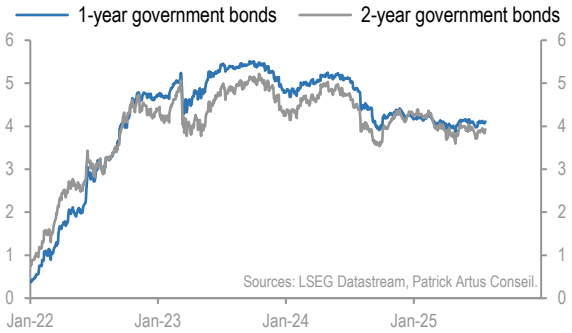


Consequently, a European investor should refrain from investing in all asset classes in the United States

A European investor:

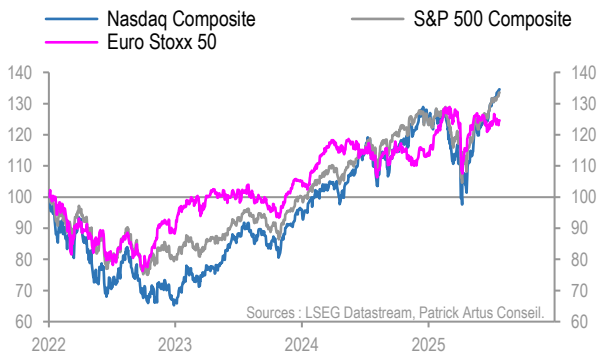
- **If he takes currency risk into account, is not attracted by a short-term dollar investment** (**Chart 8**);

Chart 8
United States: Interest rate on 1-year and 2-year government bonds (as %)



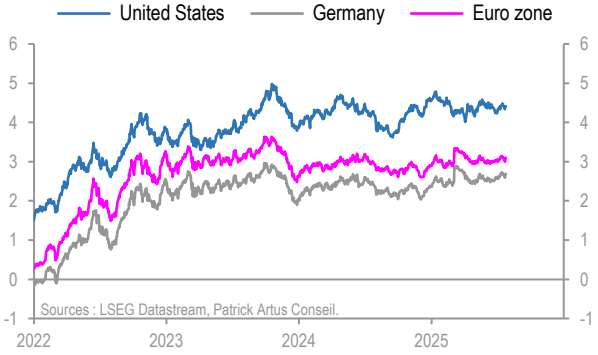
- Considering the exchange rate risk and the risk of a downward correction in the US equity market, **is not attracted to investing in equities in the United States, even if this investment has so far been profitable** (**Chart 9**) ;

Chart 9
Stock market indices (01.01.2010 = 100)



- Considering the exchange rate risk and the risk of a rise in long-term interest rates, **should not be attracted by an investment in US bonds**, even if long-term interest rates are higher in the United States than in the eurozone (**Chart 10**).

Chart 10
Interest rate on 10-year government bonds (as %)



If this European investor hedges the currency risk:

- He obtains a low return on short-term US securities ;
- He is still exposed to the risk of a stock market correction in the United States;
- He is still exposed to the risk of rising long-term interest rates.

Summary: Towards difficulty in financing the US external deficit

If a European investor is effectively discouraged from investing in short-term securities, US equities or bonds, since Europeans account for around 1/3 of the financing of the US current account deficit (which reaches $1185 billion in 2024, $450 billion in the 1st quarter of 2025), **there will be difficulty in financing the US external deficit, with the risk of a balance of payments crisis**. If such a crisis were to occur, there would inevitably be a recession and a rise in US interest rates

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