



May 2026 Market Pulse

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FED TRANSITION, IRAN AND AI IN FOCUS IN MAY



Market conditions remained complex in May, with investors evaluating a still-resilient economic backdrop, AI-related gains and ongoing inflationary pressures from the Iran war. Negotiations between the US and Iran continued, but appeared to produce little concrete progress. Kevin Warsh took over as chair of the US Federal Reserve, replacing Jerome Powell; while Warsh is seen as more dovish on rates than his predecessor, higher inflation led investors to reduce rate-cut expectations.

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Global themes

The Iran conflict and associated inflation pressures remained in focus during May. A solid Q1 reporting season supported market sentiment, with continued enthusiasm for the AI theme. Investors increasingly priced in more restrictive monetary policy from major central banks, as economic readings were resilient and Iran-related price impacts mounted.

US

A significant US development of the month was the transition at the Federal Reserve. Jerome Powell stepped down as chair, with Kevin Warsh taking the helm. Unusually, however, Powell has decided to remain on as a Fed governor to protect the Fed's credibility and independence against perceived attacks by the Trump administration. While Warsh is thought to be in favour of rate cuts, traders moved to price in a rate hike of 25bps by December 2026. This was a sharp reversal from earlier expectations of cuts, given increasing inflation pressures linked to the Iran war and higher oil prices, as well as the resilient economic backdrop despite the uncertainty caused by the conflict.

Negotiations between Washington and Tehran remained centre stage in May, with mediators in Qatar and Pakistan shuttling between the sides. The diplomatic picture remained fragile throughout. The US and Iran traded draft ceasefire proposals over the Memorial Day weekend in late May, but both sides sought changes and little concrete progress was made. Public messaging from the US administration oscillated between stressing rapid progress and warning that talks were "not satisfactory yet", whilst President Trump repeatedly insisted that no single nation would control the Strait of Hormuz and that sanctions relief would depend on Iran's conduct.

US economic data in May pointed to an economy that remains resilient despite losing some momentum under the weight of higher prices. Nonfarm payrolls rose by 115k in April, almost double the roughly 62k expected, while March's already strong increase was revised up to 185k from 178k. The headline unemployment rate stayed at 4.3%, as forecast. Retail sales remained firm, rising 0.5% m/m, while Bank of America credit card data showed spending up 5.7% y/y and 4.5% y/y excluding gasoline sales. Sentiment surveys such as the ISM's were robust, with manufacturing and service readings at 52.7 and 53.4 respectively. The Federal Reserve's preferred inflation gauge, the PCE deflator, rose 3.8% year on year in April, with core PCE up 3.3% year on year and monthly price gains still running at 0.4%. Real disposable personal income fell 0.5% on the month and was 1.1% lower than a year earlier, marking a third consecutive monthly decline in real income, even as real consumer spending rose 0.1% on the month and 2.1% year on year. Earlier releases also showed that US Q1 GDP grew at an annualised 1.6% in the first quarter, underlining that while overall activity remains positive, higher energy costs and persistent core inflation are eroding household purchasing power.

Europe

Europe remained at the epicentre of the global energy shock in May, with oil and gas prices feeding back into inflation and real income pressures. Headline eurozone CPI accelerated to 3.2% year on year in the May flash estimate, up from 3.0% in April, while core inflation rose to 2.5% and services inflation to 3.5%, underscoring that underlying price pressures are broadening beyond energy.

The ECB's policy trajectory underwent a decisive shift in May, as the combination of stickier inflation and weakening sentiment got increasingly uncomfortable. Senior ECB officials indicated that the "benign" scenario of a short-lived energy shock is now less likely, with Chief Economist Philip Lane and others signalling that multiple rate increases may be required over the coming year to prevent higher inflation from becoming entrenched in wage- and price-setting behaviour. Furthermore, multiple Governing Council members signalled that a June rate hike was "all but inevitable", citing the Iran war's persistent inflationary impact on energy and supply chains. Markets moved to price in a June rate rise and additional tightening thereafter as the European Commission also discussed allowing member states more fiscal flexibility to cushion the impact of higher energy costs.

MARKET ROUND-UP

Equities

Global equities performed well despite the complex macro backdrop, returning 5.4% (5.8% in euro terms), with the AI trade the dominant driver of sentiment, along with strong first-quarter earnings. In the US, Q1 earnings beat forecasts by 6%; in Europe by 4%; and in Japan by 9%. Leadership remained firmly with growth and AI-exposed sectors, as US and European technology, semiconductors and other cyclicals such as industrials, travel & leisure and basic resources outperformed.

The MSCI USA rose 5.3% in local terms (5.8% in euros), driven mainly by large-cap growth and AI-related names against a backdrop of solid earnings and contained macro worries. Emerging markets outperformed, with the MSCI Emerging Markets (EM) gaining 9.7% (10.3% in euros), with Korea and Taiwan rising 37.5% (35.6% in euros) and 15.2% (16.9% in euros) respectively, driven by AI and semiconductor-linked names. European equity markets navigated the ECB pivot with relative resilience, with the MSCI Europe ex UK up 4.1% (4.3% in euros), benefiting from the global AI tailwind and energy sector dynamics, though the prospect of higher borrowing costs and weaker growth capped upside.

Equities also benefited from the 19.3% fall in Brent crude oil during the month. Brent was down as ceasefire talks advanced towards month end, while the loss of the 20 million barrels per day from the closure of the Strait of Hormuz was partly offset from alternative sources.

Bonds

The US 10-year Treasury yield ended May at 4.44%, up 5 bps over the month, as sticky inflation data and resilient growth kept markets positioned for a possible rate hike rather than cuts. In the euro area, the ICE BofA 5+ Year Euro Government bond index delivered a strong 1.5% return, helped by a rally in longer-dated bonds, with the 10 year German Bund yield edging down 7 bps to 2.96% as oil prices retreated and growth sentiment readings weakened, leading some ECB Council members to urge a measured pace of rate hikes.



CHARTS OF THE MONTH

Global equities



Source: ILIM, FactSet. Data is accurate as at 31 May 2026.

Bonds – German 10-year yield



Source: ILIM, FactSet. Data is accurate as at 31 May 2026.

MARKET SNAPSHOT

Market returns (EUR)

Equity Markets (EUR)	MTD Return (%)	YTD Return (%)	2024 Return (%)
MSCI Ireland	4.8	1.3	39.9
MSCI United Kingdom	0.2	7.7	19.1
MSCI Europe ex UK	4.3	8.1	20.4
MSCI North America	5.6	11.7	4.5
MSCI Japan	5.5	17.1	10.3
MSCI EM (Emerging Markets)	10.3	26.5	18.5
MSCI AC World	5.8	13.1	8.3
10-Year Yields	Yield last month	2025 Yield (%)	2024 Yield (%)
US	4.44	4.17	4.57
Germany	2.96	2.86	2.37
UK	4.83	4.48	4.57
Japan	2.66	2.07	1.10
Ireland	3.10	3.01	2.64
Italy	3.67	3.55	3.52
Greece	3.60	3.44	3.22
Portugal	3.28	3.15	2.85
Spain	3.37	3.29	3.06
FX Rates	End last month	2025 Rates	2024 Rates
U.S. Dollar per Euro	1.17	1.17	1.03
British Pounds per Euro	0.87	0.87	0.83
U.S. Dollar per British Pounds	1.35	1.35	1.25
Commodities (USD)	MTD Return (%)	YTD Return (%)	2025 Return (%)
Oil (Brent)	-19.3	51.3	-18.5
Gold (Oz)	-1.2	5.4	64.7
S&P Goldman Sachs Commodity Index	-7.6	37.7	7.1

Source: ILIM, Bloomberg. Data is accurate as at 1 June 2026.

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THE ILM VIEW – LOOKING AHEAD

Prior to the outbreak of the war in Iran, the fundamental backdrop was positive and improving and contributed to the strong start to the year for global equities.

This backdrop was threatened by the outbreak of the conflict and risk of persistently high oil prices, which could give rise to a stagflationary environment with slower growth and higher inflation.

Despite the uncertainty and stagflation fears which contributed to an initial correction in March, equities have rallied to new all-time highs on the back of continued strong earnings, renewed strength in the AI theme and resilient economic data, particularly in the US.

The future path for markets will be determined by a combination of how long the Strait of Hormuz remains closed, its impact on energy prices and the resilience of growth and earnings amid an uncertain backdrop.

A resolution to the conflict in the near term – with the Strait of Hormuz being reopened and oil returning close to pre-war levels – would result in a limited impact on growth and inflation. With positive fundamentals reasserting themselves, both bonds and equities would be expected to rise.

In a more severe scenario – with the war escalating, lasting longer than currently expected and with the Strait of Hormuz remaining closed for several months – oil could rise further, which would create increasing fears around growth and could contribute to renewed downside in both equities and bonds. In such a scenario, with growth fears beginning to dominate inflation fears, bond yields would eventually be expected to fall and provide protection within a diversified portfolio.

Our base case is that the conflict can be resolved soon, as it is ultimately in all parties' interest to do so. This would reinforce the positive fundamental backdrop which has been evident in recent months, even with the uncertainty associated with higher energy prices since the end of February.

Based on an eventual resolution and the positive fundamentals which existed pre-war reasserting themselves, we continue to believe equities will be higher on a 12-month view.

Global equities are on a P/E multiple of 18.1x compared to the long-term average of 16.3x, and the US P/E has already contracted from the October high of 23.3x to 21.5x. With a resumption of the positive fundamental backdrop, with global economic and earnings growth of around 2% and in the high teens respectively, equities can be higher on a 12-month timeframe. However, the asset class could remain volatile in the short term and sensitive to newsflow around the war.

A de-escalation or resolution of the conflict, with oil falling back to circa \$80/90 per barrel should contribute to lower bond yields as inflation fears fade and contribute to some reversal of the more hawkish expectations around central bank policy rates, both of which would support equities.

On a 12-month view, our base case is that the German and US 10-year government bond yields fall from current levels of 2.96% and 4.44% to 2.50% and 4.00%, respectively.

If a resolution to the Iranian conflict is reached, the recent rise in yields due to inflation concerns should reverse.

We believe fixed income offers a strong risk-reward profile at this stage in the cycle, with the potential to offer protection if the economy slows. The asset class is attractive from an income perspective while also providing potential for capital gains via falling yields. From current levels, we believe that the risks of materially higher bond yields have reduced, and, if the economy falters, major central banks will be able to cut rates to support growth. In that scenario we would expect bonds to outperform.



THE MONTH AHEAD

June

MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
	<p>09</p> <p>Australia Westpac consumer confidence change; NAB business confidence</p> <p>China balance of trade; exports YoY; imports YoY</p> <p>Germany balance of trade</p> <p>US existing home sales</p>	<p>10</p> <p>China inflation rate YoY</p> <p>US core inflation rate MoM, YoY; inflation rate MoM, YoY; BoC interest rate decision</p>	<p>11</p> <p>Euro Area ECB interest rate decision</p> <p>US PPI MoM</p>	<p>12</p> <p>UK GDP MoM</p> <p>US Michigan consumer sentiment (prel)</p>
	<p>16</p> <p>China industrial production YoY; retail sales YoY</p> <p>Japan BoJ interest rate decision</p> <p>Australia RBA interest rate decision</p> <p>Germany ZEW economic sentiment index</p> <p>US building permits (prel); housing starts</p>	<p>17</p> <p>Japan balance of trade</p> <p>UK inflation rate YoY</p> <p>US retail sales MoM; Fed interest rate decision; FOMC economic projections</p>	<p>18</p> <p>UK unemployment rate; BoE interest rate decision</p>	<p>19</p> <p>Japan inflation rate YoY</p> <p>UK retail sales MoM</p>
<p>22</p> <p>Canada inflation rate YoY</p>	<p>23</p> <p>Germany manufacturing PMI flash</p> <p>UK manufacturing & services PMI flashes</p>	<p>24</p> <p>Germany Ifo business climate</p>	<p>25</p> <p>Germany consumer confidence</p> <p>US core PCE price index MoM; durable goods orders MoM; GDP growth rate QoQ final; personal income MoM; personal spending MoM</p>	
	<p>30</p> <p>China manufacturing PMI</p> <p>France inflation rate YoY (prel)</p> <p>Italy inflation rate YoY (prel)</p> <p>Germany inflation rate YoY (prel)</p> <p>US JOLTS job openings</p>			

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