Global Market Outlook 2025

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Growth and resilience amid political challenges

This is marketing material

Introduction

The global economy is poised for a dynamic year in 2025, shaped by a confluence of critical factors. Inflation and interest rates are again at the forefront, as central banks carefully adjust their policies to sustain growth while keeping inflation in check. Political developments, particularly Donald Trump's return to the White House, are likely to influence global trade and economic strategies. Rising US debt levels add another layer of complexity – potentially affecting both fiscal stability and investor sentiment.

Corporate profits and earnings growth are projected to remain robust, driven by technological advancements and strategic investments in sectors like artificial intelligence (AI) and renewable energy. Amid geopolitical flare-ups and tensions in trade policy, economists expect steady global GDP growth with notable contributions from emerging markets. Equities should continue on a positive trajectory, supported by strong corporate earnings and favourable economic conditions. Bonds, meanwhile, present opportunities despite potential risks from fiscal policies and inflationary pressures.

How should investors navigate this complex environment? In this article, we offer a comprehensive outlook on the market dynamics for 2025.

The economy in 2025: prices, politics, profits

We believe three critical factors will shape the global economy and markets in 2025 – prices, politics and profits.

The global economy demonstrated resilience in 2024. Equity markets showed remarkable strength, with the S&P 500 rising more than 25% in the 12 months to the end of December. This robust performance was driven by a combination of favourable economic conditions and investor optimism. In 2025, we expect inflation, trade policies and tariffs, and geopolitical factors (including the ongoing conflicts in Ukraine and the Middle East) to all play a significant role. Nevertheless, global growth is projected at 3% for 2025.

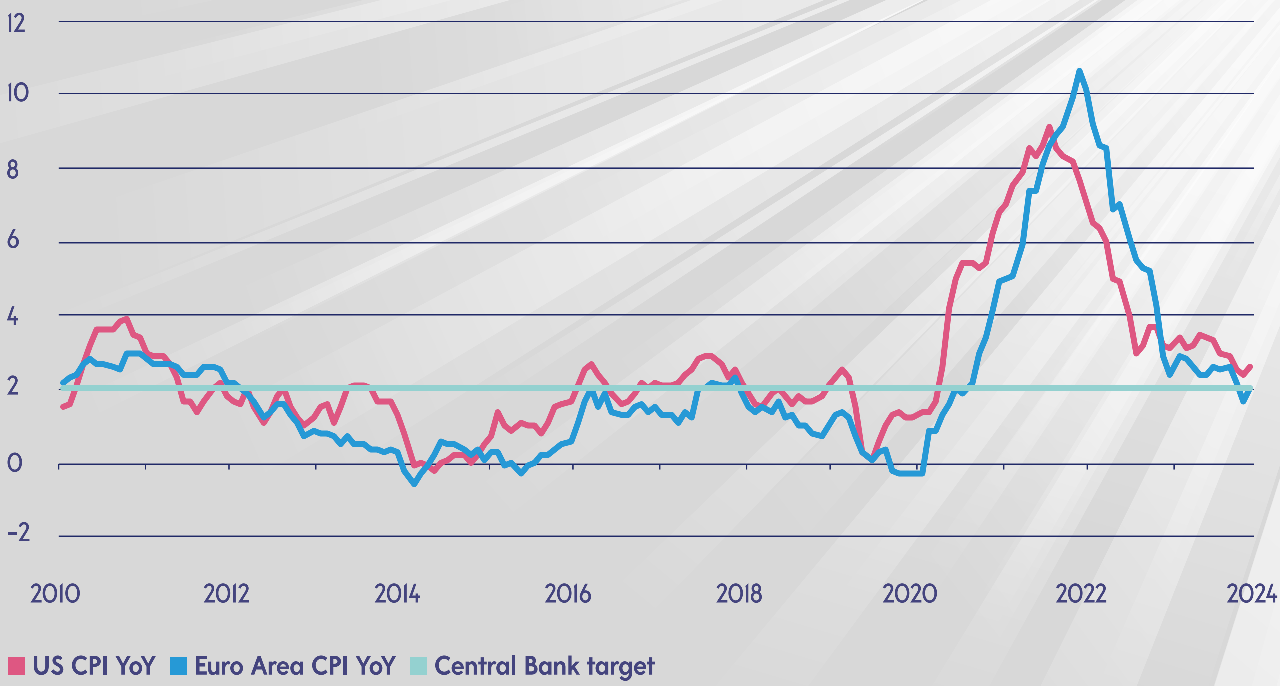
What direction for inflation and interest rates?

Inflation concerns have dominated financial markets since the pandemic. Inflation has eased over the past 12 months, and, in response, central banks have begun to cut interest rates. This has helped alleviate pressure on consumers and pushed financial markets higher.

Looking ahead, we expect inflation to stay under control. If inflation continues to fall, central banks should stick to their rate-cutting cycles. However, new policies from the Trump administration – specifically regarding trade tariffs – could have significant consequences on the rest of the world and may cause global inflation to spike again.

Figure 1: Inflation continues to ease down to central bank targets

US and Euro Area Consumer Price Inflation (CPI) YoY %, 2010-2024



Source: Bloomberg Monthly data 31/12/2010 – 31/10/2024

Keep an eye on the ‘three Ps’

We believe the three Ps (prices, politics and profits) will be critical in shaping the economic and market landscape in 2025.

1. Prices

Annual consumer price inflation (CPI) on both sides of the Atlantic is currently running between 2% and 3%, which is very close to the target rate of 2% set by both the European Central Bank (ECB) and the US Federal Reserve (Fed).

Why is this so important? Because, at these levels, we can expect more interest rate cuts to follow in the year ahead, which should alleviate some pressure on households and businesses.

Economists anticipate the Fed will make two more cuts during 2025, with up to six from the ECB as it addresses Europe’s sluggish economy. This is good news, as lower interest rates and prices should ease consumer pressure and support economic growth, benefiting both bond and equity investors. Divergent interest rates could lead to a weaker euro, but this will ultimately support the eurozone, making it more competitive in export markets. The main risk to a more benign inflation outlook is the possibility of a trade war between China, Europe and the US, as this could push inflation higher again.

Figure 2: More interest-rate cuts are priced in

Fed and ECB target rates in % with market expectations

Source: Bloomberg. Monthly data 31/12/2020 – 31/12/2025E

2. Politics

US: Donald Trump returns
Donald Trump's re-election, along with the Republicans' 'red sweep' of both houses of Congress, is expected to bring higher trade tariffs on China and Europe.

The market is watching Trump's policy measures closely, especially the tariffs he sets on imports, which could affect European and Chinese exports. His previous term saw large fiscal stimulus and similar policies could lead to more inflation this time around.

With the Republicans regaining control of the Senate, it could be easier for Trump to push through larger fiscal stimulus and trade tariffs. The US is already running large debt levels, so this is an area worth monitoring closely. As Figure 3 illustrates, US debt is strained, with high deficits and total debt above 100% of GDP, and this is expected to continue to deteriorate over the next few years. Trump's agenda of lowering taxes and increasing spending could exacerbate this.

Bond investors will also be watching Trump's policies with increased interest; if Trump's policies lead to higher inflation, the Fed may adjust its rate-cutting cycle. In Europe, a key question is to what extent will Trump impose tariffs on European imports. Import tariffs could significantly impact European exporters, especially automakers.

Europe: change at the top?
As events in France demonstrated at the end of 2024 – with a no-confidence vote in Prime Minister Michel Barnier and the collapse of the French government – politics in Europe will also play a role. The political landscape in 2025 will be marked by significant changes and challenges. Both France and Germany are experiencing political instability; in France, President Emmanuel Macron's government is struggling to pass budgets through a divided Parliament while Germany faces new federal elections in February 2025 after a vote of no confidence.

Figure 3: US debt levels continue to rise

US gross government debt as a % of GDP, in %, 2001-2028e

Source: IMF, 31/12/2001-29/12/2028E

3. Profits

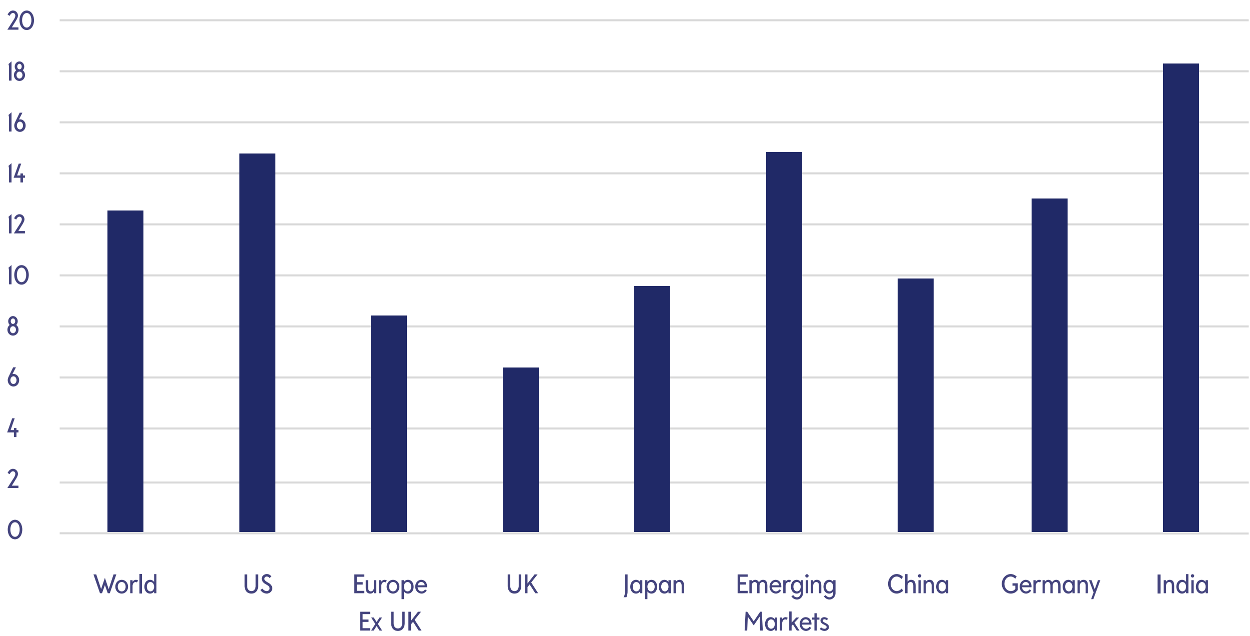
Equity markets continue to thrive, driven by trends like AI and the energy transition, which have boosted corporate profits. These trends are expected to be long term.

Amid a growing global economy, corporate profits are projected to remain robust. Analysts predict 12.5% global earnings growth over the next 12 months. However, the strongest growth is likely to be in the US, with forecasts of 15% growth compared with just 8.5% in Europe. China's earnings growth is expected to be 10%, while in fast-growing India, companies are expected to grow profits by 18%.

With inflation under control and interest rates lower, consumer confidence should remain high. This should support continued spending and economic growth, which in turn benefits equity markets. Spending on AI, the energy transition and diversifying supply chains are significant tailwinds for the market, and look set to continue into 2025.

Figure 4: Earnings growth to remain strong in 2025

2025E earnings growth % by country/region



Source: IBES, 2025E

The economic picture – a regional view

US: Since the pandemic, the world's largest economy has gone from strength to strength. Secular trends like AI and favourable tax policies by the Biden administration have helped cement the country's dominance and importance on the world stage. The US economy continues to fare well, driven by expansionary fiscal policy and a robust consumer base. AI and other long-term trends have boosted the profits of US companies, driving the S&P 500 Index to all-time highs. This, in turn, is leading to a substantial wealth effect across the US. Total US household wealth is now at a staggering US$170 trillion.

We expect a similar picture to emerge in 2025. Growth is projected to be lower, but steady, at around 1.9%, and policies from the Trump administration are likely to be aimed at boosting growth further. However, these policies may come at the expense of other trading partners. Significant policy changes from Trump's return to power and the Republican sweep of Congress could cast a fog on the economic outlook. While the specifics and timing of potential policy shifts remain unclear, we expect to see tax cuts, higher tariffs, reduced immigration and deregulation of various sectors.

Europe: Europe has struggled to gain momentum since the pandemic, and the outlook for 2025 is no different. Economic growth in the eurozone is forecast to stay below the US at 1.2%. In part, this is due to the structural nature of the slower EU economy, with core nations like Germany and France struggling.

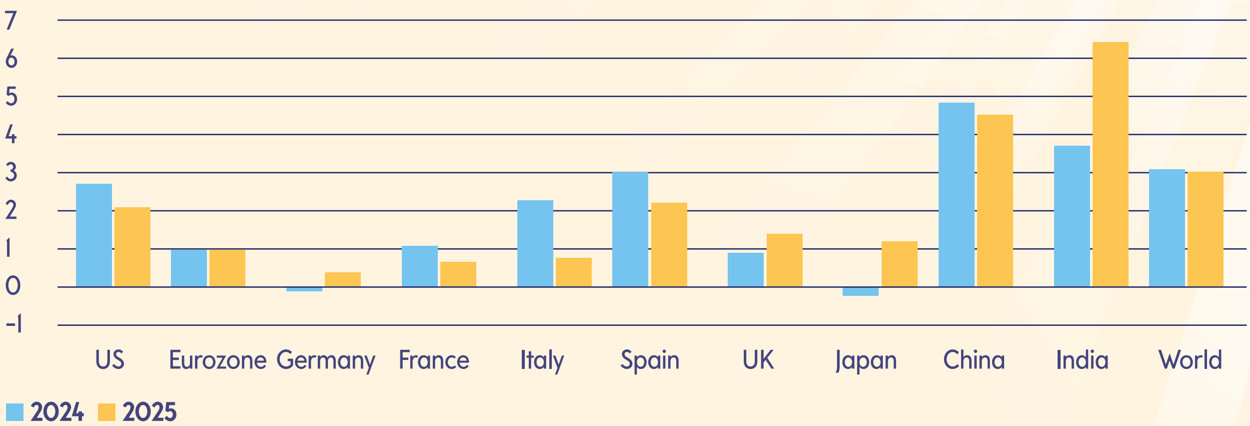
One risk we see is that protectionist policies might also strain transatlantic trade relations. In a worst-case scenario, the ECB may need to speed up its interest-rate cuts to counteract these economic pressures, and, up to six more interest-rate reductions are expected from the ECB to support growth. European bonds should be boosted by more aggressive rate cuts.

China and emerging markets: Trump's trade policies could mean headwinds for emerging markets, particularly tariffs on Chinese goods. These tariffs could exacerbate China's economic malaise, affecting other emerging economies tied to China's supply chain.

Despite these challenges, there are growth opportunities. China is expected to grow by 5% while India's economy is expected to grow by around 6.5% in 2025, driven by strong domestic demand and supportive policies. Indian bonds are set to perform well due to anticipated central bank rate cuts and strong inflows from foreign investors, making them an attractive investment option. Overall, India remains poised for growth across various sectors despite some challenges.

Figure 5: The global economy is expected to grow by 3% in 2025

Real global GDP growth by country, in %, 2024 & 2025E



Source: Bloomberg Economics, 2024 & 2025E

Equities in 2025: will the bull market continue?

Equity markets have shown remarkable resilience and growth over the past two years, driven by easing inflation, supportive fiscal policies and technological advancements such as AI.

As we expect these trends to continue in 2025, we think four key factors will shape the equity market:

- **Positive outlook:** While investors need to be vigilant to geopolitical developments and economic indicators, the overall environment appears conducive to continued market gains for both equities and bonds.
- **Inflation and interest rates:** With inflation under control and interest rates low, consumer confidence is expected to remain high. This should support continued spending and economic growth, which in turn benefits equity markets.
- **A broader recovery:** Market gains in 2024 were primarily driven by valuation expansion from large-cap technology stocks. As inflation, wage growth and supply-chain issues that plagued profitability continue to abate post-COVID, margin recovery should broaden to other parts of the market.
- **Trump returns:** Donald Trump's re-election and his proposed tariffs on imports, particularly those from China and Europe, could create market volatility. However, strong economic fundamentals should mitigate any negative impact.

Robust profits to drive markets

Due to strong market returns in recent years, equities are not cheap. Global equities are trading at around 19x forward earnings – above historical averages. Investors cannot count on the same level of returns in recent years, as a lot of good news is already priced in.

With valuations at the upper end of historical ranges, further equity market gains will need to be driven by stronger corporate profits. The positive news is that analysts are forecasting another 12.5% earnings growth over the next 12 months. The technology sector is once again expected to have the highest level of growth at 22%, followed by the healthcare sector, which is expected to grow by 19.5%.

Spending on AI will spread to other sectors

Spending on AI, the energy transition and diversifying supply chains are significant tailwinds for the market. Companies are accelerating capital expenditures to upwards of US$200 billion in 2024, and 2025 is set to be another year of substantial investment.

This spending will benefit areas such as data centres, real estate, engineering and construction, nuclear and renewable power, energy transmission, gas-powered electricity, cooling technologies and the electrical components connecting these systems. This broadening of market leadership, resilient economic fundamentals, policy tailwinds and secular trends should support a more inclusive rally in the year ahead.

The regional view

US: beyond the Magnificent Seven

The US has enjoyed a strong bull market for the past two years, with US equities rallying around 60% in the last 24 months. In fact, US dominance has been so strong that US companies now account for over 70% of total global market capitalisation. These strong gains were initially concentrated on the 'Magnificent Seven' (the tech giants Nvidia, Apple, Microsoft, Amazon, Meta Platforms, Tesla and Alphabet), but broader market leadership is expected in 2025.

The prospect of deregulation and corporate tax cuts by the Trump administration may finally give investors the confidence to invest in previously unloved areas of the market, such as value and mid/small-cap stocks, which are also benefiting from earnings recovery and attractive valuations.

Over the past two years, the industrial, energy and materials sectors have faced challenges due to weak manufacturing activity. However, as the cost of capital declines with falling interest rates, both consumers and companies are expected to resume capital-intensive expenditures. Durable goods industries, particularly those tied to housing, should also see a boost.

The financial sector stands to benefit from increased loan and insurance demand; a more favourable yield curve; normalising mergers and acquisitions (M&A) and initial public offering (IPO) activity; and prospects for deregulation. Falling rates also enhance the relative value of bond proxy sectors like utilities and real estate.

Emerging markets: long-term positives

Looking ahead to 2025, we are optimistic about emerging market equities due to strong economic growth, improving inflation and easing interest rates. In China, despite coordinated stimulus efforts leading to a 30% tactical rebound in Chinese equities in the third quarter of 2024, China remains mired in its cyclical downturn.

Looking ahead, policies are likely to remain accommodative until economic momentum stabilises, but policymakers do not seem intent on generating robust growth. Should President-elect Trump fully implement his tariff campaign promises, Chinese policymakers might respond with more aggressive economic stimulation. Nonetheless, opportunities exist in China, as it is one of the cheapest markets globally.

India plays a significant role in AI innovation and there are opportunities across the various stages of AI development. India is expected to drive returns through structural growth while supportive policies should continue to benefit Indian equities.

Overall, despite individual performance variations, the long-term outlook for emerging markets remains positive.

Europe: confidence is slow to emerge

Europe is also grappling with its own cyclical challenges. A shift in sentiment and earnings for European equities will largely depend on a rebound in China, a manufacturing upturn or stronger consumer spending – all of which we believe will be difficult to achieve in 2025.

Additional easing by the ECB should eventually provide some support, especially for businesses that rely more on bank lending. However, confidence and consumer spending have been slow to improve. Furthermore, the eurozone may face tariffs next year. Despite these challenges, we believe sector-level discounts combined with healthy buybacks and dividend yields present compelling opportunities in select European companies.

Fixed income in 2025: Lower rates to drive returns

The bond market in 2025 is likely to be influenced by a combination of easing inflation, central bank policies and benign global economic conditions. With lower rates expected and still attractive yields available in the bond market today, investors may be wise to allocate part of their portfolio to bonds.

Could central bank policies support longer duration?

With inflation easing, the ECB and the Fed, alongside other central banks, have begun cutting interest rates. This trend is likely to continue, keeping borrowing costs low and supporting bond prices. Annual inflation is expected to remain between 2% and 3%, which should help maintain the purchasing power of bond interest payments. This environment is favourable for fixed income investors seeking predictable returns.

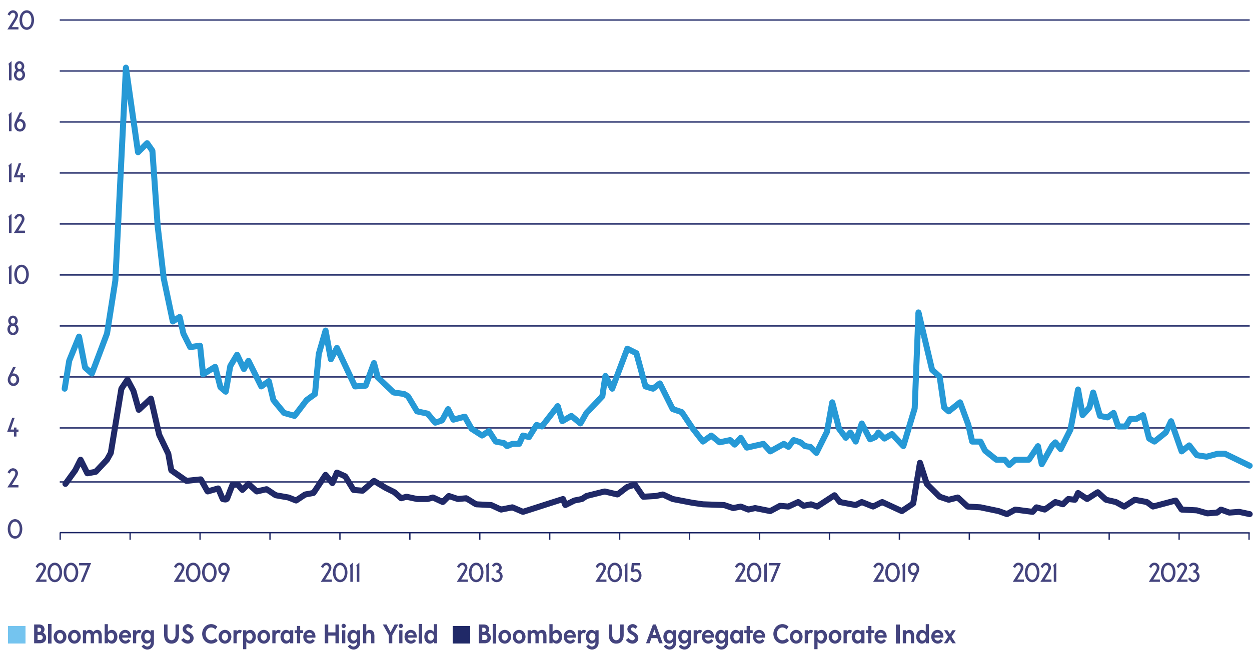
Lower interest rates should lead to lower yields on bonds, pushing bond prices higher. As interest rates are cut, longer-maturity bonds tend to do better as they are more sensitive to central bank interest rates, and investors can generate good returns in longer-duration bonds. Because of the softer macroeconomic backdrop, we expect European and emerging market fixed income assets to outperform their US counterparts.

Credit – the good news is already priced in

The economic backdrop is supportive of credit, both high yield and investment grade. Company defaults remain at relatively low levels and lower rates, particularly in Europe, should keep defaults in check. However, like equities, a lot of the positive news for credit markets is already priced in. Spreads – the additional yield an investor is compensated for holding more risky credit – are already at quite tight levels. Therefore, investors should not factor in further gains from spread compression compared with sovereign alternatives but focus on the yields available as a guide to future expected returns.

Figure 6: Credit spreads at their tightest since the global financial crisis

Bond yields % for US investment grade and US high yield



Source: Bloomberg Economics, 31/12/2007 – 29/11/2024

Potential risks from Trump's policies

One area to watch closely is how the bond market reacts to Trump's policies. His fiscal policies, including tax cuts and increased spending, could lead to higher inflation and economic growth. This might prompt the Fed to adjust its monetary policy, potentially slowing the rate-cutting cycle.

Concerns about rising national debt under Trump's administration could impact the perceived safety of US government bonds. Investors might demand higher yields to compensate for increased risk, affecting both short-term and long-term bonds.

Despite these potential risks, the bond market outlook for 2025 is generally positive. There are opportunities across the spectrum in high-quality corporate and sovereign bonds.

Summary – How should investors approach the year ahead?

Focusing on the three Ps, the year ahead presents challenges for investors. Beyond the headline forecasts for the year ahead – 3% global economic growth, inflation falling and interest rates returning to a more manageable level – investors will need to be alert to market volatility.

But for those willing to seek it, the next 12 months will present investment opportunities, spanning regions and asset classes.

The regional perspective: US or further afield?

As the US economy continues to thrive, potential policy changes under Trump are expected to favour US equity markets. The technology sector, which has shown robust earnings growth in recent years, is also expected to continue performing well. However, the dominance of technology could give way to a broader set of opportunities, which might include sectors like healthcare. Trump's policies could also provide a significant boost to small and medium-sized companies in 2025.

Elsewhere, Europe and China face greater challenges compared with the US. However, there are still opportunities, particularly in the healthcare and consumer goods sectors within Europe and emerging markets. One key area to watch in 2025 will be the extent to which Chinese authorities can reignite the domestic economy. A successful economic revival in China would benefit both emerging markets and European companies significantly.

Asset classes: Equity markets buoyant, bonds benefiting

Economic growth backed by rising consumer confidence and spending would be a positive backdrop for equity markets. Additionally, the policies implemented by the Trump administration are anticipated to be supportive of risk assets. The energy transition and AI are among the key trends expected to drive corporate profits, particularly in the US.

For bonds, the outlook is also positive. There are opportunities in sovereign bonds in both emerging and developed markets and in high-quality corporate bonds, as central banks are expected to continue cutting interest rates in 2025. The ECB is anticipated to cut rates more aggressively than the Fed, which favours European bonds over their US counterparts.

As investors consider the year ahead, there are a range of different assets and strategies that may suit their needs. Staying the course and remaining invested with a diversified portfolio can help get the best from 2025.

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