

## ADVANCED ECONOMIES

2025



“ THE COMBINATION OF HEADWINDS (US TARIFFS, UNCERTAINTY) AND TAILWINDS (LOW OIL PRICES, FED RATE CUTS, EUROPEAN MEASURES) EXPLAINS THE GRADUAL NATURE OF THE SLOWDOWN (IN THE US) AND THE RECOVERY (IN THE EUROZONE). ”

ECONOMIC RESEARCH



**BNP PARIBAS**

The bank  
for a changing  
world

# TABLE OF CONTENT

2

## EDITORIAL

**3** Walking on a fine line, advanced economies continue to show resilience

## FOCUS

**6** International Trade:  
It's not all about the  
United States

## UNITED STATES

**10** Slowdown Underway

## EUROZONE

**12** Growth set to strengthen

## GERMANY

**14** A recovery in the making

## FRANCE

**16** Towards a sustained rebound  
in growth

## ITALY

**18** Growth slows;  
Public Finances improve

## SPAIN

**20** Job creation continues  
to underpin growth

## BELGIUM

**22** Smooth sailing for now,  
but where to next?

## UNITED KINGDOM

**24** A fragile rebound

## JAPAN

**26** Stuck In The Middle  
of Inflation and Tariffs

## MAIN INDICATORS

**28**

## FORECASTS

**29**



## EDITORIAL

3

## WALKING ON A FINE LINE, ADVANCED ECONOMIES CONTINUE TO SHOW RESILIENCE

Advanced economies are continuing to show resilience in the face of the US trade war. Despite significant fluctuations in trade in the first half of 2025, global trade has been broadly unaffected so far. As trade links with the United States weaken, trade is shifting towards the rest of the world. The combination of headwinds (US tariffs, uncertainty) and tailwinds (low oil prices, Fed rate cuts, European measures) explains the gradual nature of the slowdown (in the US) and the recovery (in the Eurozone). According to our forecasts, the 25 bp cut decided by the Fed in September 2025 would mark the start of a series of five cuts. The Fed would thus swap positions with the ECB, which can now opt for the *status quo*. The growth gap between the United States and the Eurozone would narrow from +2 percentage points in 2024 to +0.1 in 2026. With growth expected to rise and inflation under control, the Eurozone is escaping the stagflationary scenario seen in the United States, the United Kingdom and Japan. The euro is becoming more attractive and strengthening against the dollar (with parity expected at 1.22 by the end of 2026). The fiscal and monetary policy mix remains difficult to reconcile in the United States, the United Kingdom and Japan, while the Eurozone is in a more comfortable position.

## TRADE WAR: AFTER THE SHOCK, TIME TO ADAPT

After the major upheaval of 'Liberation Day' in early April and the multiple reversals and successive announcements on the calibration of US tariff increases, the dust has settled somewhat since late July/early August. The agreement between the United States and the European Union, in particular, followed by the disclosure of the new US tariff list, provide a clearer picture of where customs duties will land and the conditions associated with them. This restores some visibility, but significant and numerous uncertainties remain<sup>1</sup>.

The initial impact of this tariff shock on global trade has been both significant and limited. It has been significant in terms of the sharp ups and downs in exports and imports in the first half of 2025, in anticipation of the tariff increases and then in the aftermath. It has also been significant in terms of the rapid adjustment of trade flows to the new tariff situation, as highlighted in our Focus on this topic in this issue. This Focus also shows that the overall impact on global trade is limited, if not non-existent for the time being: its growth rate has not slowed and remains close to the 2024 trend. While trade links with the United States are weakening, they are redeploying and tending to strengthen in the rest of the world.

In terms of the impact on growth and inflation, the full effects of the tariff shock are yet to be felt. Not all countries are in the same boat, but contrary to the prevailing negative discourse, Europe is clearly doing relatively well<sup>2</sup> and the shock, in its current form, appears to be entirely manageable.

## THE SAME CONSTRAINTS AND SUPPORTS ARE STILL AT WORK

One of the characteristics of the economic developments observed and expected in our central scenario is their gradual nature. The slow pace of adjustments contrasts with the feeling of a world that is changing ever more rapidly. The risk of non-linear effects and a more sudden deterioration in the economic situation, particularly in the US, has certainly increased. The scale of the uncertainties contributes to the feeling that the economic trajectory is on a knife edge. But for now, signs of a slowdown and signs of improvement remain contained, due to the opposing forces that continue to affect the global economy.

## Multiple headwinds

Among the factors holding back economic activity, US tariffs and the continuing high level of uncertainty surrounding their future level and scope remain at the top of the list. We must also keep an eye on tensions surrounding long-term interest rates. These tensions remain latent and, when they do manifest themselves, they are still isolated bouts of nervousness for the time being. Bond markets are showing increased but selective vigilance with regard to fiscal risks. In addition, US long-term rates have recently eased, fuelled by expectations of Fed rate cuts. However, given the scale of financing needs and bond auctions by a number of countries, many of which have deteriorated fiscal positions, a more sustained, pronounced, and/or widespread rise in long-term rates poses a significant risk due to its potential implications.

Higher long-term rates are already complicating the fiscal situation at a time when significant consolidation efforts are needed in many countries, while at the same time there is a need to create room for manoeuvre to increase certain items of public spending (defence, environment, dependency). Fiscal consolidation, where it is taking place, even if it is being done smoothly, is another drag on growth. Added to this are the threats to the Fed's independence. In the short term, it is the additional uncertainty and concern that is detrimental; in the longer term, it is the economic and financial stability risks that this poses, in the United States and elsewhere in the world.

To conclude this list of headwinds to growth, we should mention China's vulnerabilities. The Chinese economy held up fairly well in the first half of 2025, but it seems to be running out of steam and remains mired in internal structural problems<sup>3</sup>. This is doubly negative for global growth: exports to China are suffering and imports from China remain strong, as the country is still dependent on external exports as a growth engine to offset its internal difficulties.

## And just as many tailwinds

Faced with these numerous and relatively powerful headwinds, there is also a long list of tailwinds. To begin with, there are the relatively low oil prices, which are providing significant support for GDP growth in advanced economies. In the US, this is certainly complicating life for oil producers, but it is making life easier for consumers and the Fed.

<sup>1</sup> See [EU-US Trade Deal: A Damage Limitation Success](#) (27 July 2025) and [US tariffs in emerging countries: is the picture clearer now?](#) (27 August 2025).

<sup>2</sup> See [Increase in US tariffs: Europe fares best](#), 17 September 2025.

<sup>3</sup> In China, economic growth remains resilient but the fight against deflation is far from won, 8 September 2025



BNP PARIBAS

The bank  
for a changing  
world

The Fed's resumption of rate cuts (as part of general easing trend around the world), after nine months of monetary status quo, is also a supporting factor. According to our forecasts, the 25 bp cut announced at the FOMC meeting on 16-17 September would be the first in a series of five (25 bp each). It would ease the degree of restriction in US monetary policy at a time when the US labour market is showing more significant and worrying signs of slowing down. However, this is not without risk, as it could further fuel the ongoing rise in US inflation, driven by higher tariffs on US imports, at a time when it has not yet returned to the 2% target.

The US stock market's initial reaction to the Fed's rate cut was mixed, torn between the underlying negative signal (deterioration in the labour market) and the positive signal of support provided by monetary easing). As the US stock markets approached their opening the day after the FOMC meeting, they seemed more inclined to view the cut in a positive light. This ability to see the glass as half full since the beginning of the year, despite the uncertainties and concerns surrounding the Trump administration's trade and immigration policies (the post-Liberation Day warning shot fizzled out), is a significant factor supporting growth, whose overall resilience in turn fuels market optimism. Growth and markets are also being buoyed by the tech-AI wave. However, this support is also tinged with concern due to the air of irrational exuberance surrounding it.

In the Eurozone, the favourable credit dynamics are also a positive factor. Last but not least, Germany's massive investment plan, European rearmament efforts, and the associated knock-on effects are also expected to provide support. The first effects are already visible in the business climate in Germany. They still need to be confirmed, especially as the challenges involved in materialising this support as quickly as possible remain significant. There is an awareness of the need and urgency for a European revival, and the will to tackle it, but concrete and rapid action is still awaited. This is demonstrated by Mario Draghi's renewed warning, in a speech marking the first anniversary of the presentation of his roadmap report to restore European competitiveness<sup>4</sup>. The list of achievements is not empty<sup>5</sup>, but it is not enough, for the time being, to make a difference. However, the direction taken is the right one, and our central scenario anticipates a gradual increase in momentum.

### A desynchronized rebalancing of forces

These headwinds and tailwinds do not necessarily always balance each other out, given the different and difficult-to-grasp transmission lags. The effects of uncertainty are quickly apparent, while those directly linked to the increase in customs duties emerge more slowly and to an extent that is still uncertain. High long-term interest rates and fiscal consolidation also have a long-term impact on economic activity but can quickly weigh on confidence surveys. The slowdown in China is having a more immediate effect, as are credit dynamics and the wave of investment in AI on the supportive side. Low oil prices are reflected almost instantly in prices at the pump, but their support for growth is slower to spread. Wealth effects are already at work, but in theory they take time to feed through, as do cuts in key interest rates.

The support for European growth provided by increased military spending and the German investment plan will take the longest to be felt (given the time needed to implement and adapt production capacities), but the existence and prospect of this support may already be having a positive impact on the business climate. To illustrate our point more concretely, in our Eurozone scenario, we anticipate that growth will be somewhat hampered in the short term by the deleterious effects of the US trade war before the positive effects of European measures take hold in the medium term.

## EUR/USD AT THE CONFLUENCE OF INFLUENCES

### A good indicator of the economic situation

The EUR/USD exchange rate is a good indicator of current economic developments. For the time being, the depreciation of the greenback is orderly and broadly beneficial: for the US, as long as it remains favourable to growth and inflation does not play too much of a spoiler; for the rest of the world, and the Eurozone in particular, as long as it has a moderating effect on inflation, facilitating rate cuts, and growth is not too badly affected.

### A positive signal for the Eurozone

The appreciation of the EUR/USD exchange rate is partly due to the improvement in growth prospects on this side of the Atlantic compared with their deterioration on the other side. It is not so much that the dollar is weakening as that the euro is strengthening. This positive signal in terms of attractiveness helps to put the negative impact on the Eurozone's competitiveness into perspective. The monetary policy differential (return to rate cuts on the Fed side, halt on the ECB side) is also contributing to the greenback's decline against the single currency. But, in the same vein, it is a good sign for the Eurozone that the ECB has (most likely) ended its cycle of rate cuts. The risk of more destabilising movements in the US dollar cannot be ruled out, as the greenback is not immune to a more pronounced wave of mistrust. But this risk appears to be less significant than that weighing on other markets (equities, credit, bonds). Given its strong past appreciation (nearly +50% between July 2011 and January 2025 in real effective exchange rates, nearly +30% against the euro), the US dollar has considerable room to fall before it can be considered weak (it has lost 6% since January 2025 in REER and just over 10% against the euro).

Our forecasts are for a EUR/USD exchange rate of 1.20 by the end of 2025 and 1.22 by the end of 2026, and for a further 3% depreciation in the US dollar's nominal effective exchange rate by the end of 2025 compared with its August average, and 4% between the end of 2025 and the end of 2026.

## GROWTH FORECASTS: FEW CHANGES DESPITE THE CHANGES

Since our previous issue of EcoPerspectives in April<sup>6</sup>, the major trends anticipated at that time have not changed significantly. Even if a lot has happened, including the upheaval surrounding US tariff policy, economic indicators from advanced countries have generally been in line with our growth forecasts.

<sup>4</sup> [https://commission.europa.eu/document/download/0951a4ff-cd1a-4ea3-bc1d-f603decc1ed9\\_en?filename=Draghi\\_Speech\\_High\\_Level\\_Conference\\_One\\_Year\\_After.pdf&pre-flang=fr](https://commission.europa.eu/document/download/0951a4ff-cd1a-4ea3-bc1d-f603decc1ed9_en?filename=Draghi_Speech_High_Level_Conference_One_Year_After.pdf&pre-flang=fr), 16 September 2025.

<sup>5</sup> See Draghi report, one year later: Europe strengthens its competitiveness and The Draghi report: one year on.

<sup>6</sup> EcoPerspectives — Advanced Economies | 2nd Quarter 2025 — Economic Research — BNP Paribas, 18 April 2025



Our adjustments are relatively minor and, above all, upward in most cases. While the pace of US growth is expected to remain higher than that of the euro area, the outlook remains for a slowdown across the Atlantic (-1.3 percentage points between 2024 and 2026) and a strengthening in the euro area (+0.6 pp). The growth gap is expected to narrow significantly: from +2 pp in favour of the United States in 2024, it would fall to +0.4 pp in 2025 and +0.1 pp in 2026<sup>7</sup>. Growth in the United Kingdom and Japan is also expected to improve in 2025, before slowing in 2026. Our growth forecasts for the United States for 2025 are in line with the consensus (1.7%) and slightly below for 2026 (1.5%, -0.2 pp). However, we are more optimistic than the consensus for the Eurozone in 2025 (1.3%, +0.1 pp) and 2026 (1.4%, +0.3 pp). Our forecasts for the United Kingdom and Japan are close to the consensus. Finally, we believe that the balance of risks surrounding our scenario is fairly even.

## STAGFLATIONARY CONFIGURATION, WITH THE NOTABLE EXCEPTION OF THE EUROZONE

If we combine the growth situation and outlook with those of inflation, the United States, the United Kingdom and Japan are facing a stagflationary situation, combining slowing growth (United States) or low growth (United Kingdom, Japan) with high inflation (United Kingdom, Japan) and rising inflation (United States). The Eurozone is a notable exception to this unfavourable scenario: growth is picking up and inflation is back on target, expected to fall in headline terms and remain broadly stable for the core measure.

The Eurozone continues to be characterised by the mixed performance of its four largest economies. Spain continues to significantly outperform its partners, even though a slowdown is expected. Having a bigger industry share, Germany and Italy are more affected by the increase in US tariffs, but the growth outlook is improving, albeit fragile, between 2024 and 2025 and again between 2025 and 2026. French growth is also expected to improve in 2026 compared to 2025, but after performing poorly in 2025 (with growth down compared to 2024 and below the Eurozone average). It is penalised by factors specific to it (notably particularly low consumer confidence) which mask important strengths (aeronautics, services, entrepreneurial dynamism). France nevertheless benefited from a growth carry-over of +0.6% in Q2, compared with +0.2% for Germany, +0.5% for Italy and +2.3% for Spain, which is in a class of its own.

## A RATHER COMPLICATED POLICY MIX IN THE UNITED STATES, THE UNITED KINGDOM AND JAPAN, LESS SO IN THE EUROZONE

### Monetary and fiscal policies that are difficult to reconcile

Monetary and fiscal policy in the various advanced economies we cover here are each treading carefully, moving in uncoordinated and difficult-to-reconcile directions. In the case of the United States, fiscal support for growth via the OBBBA is offset by the negative effects of the tariff shock and the tightening of immigration policy<sup>8</sup>.

We anticipate a moderately restrictive fiscal impulse, which the resumption of monetary easing may help to cushion. However, the US budget deficit remaining at a very high level is a potential factor (rather invisible for the time being<sup>9</sup>) pushing up long-term rates (added to which are the effects of threats to the Fed's independence via an increase in the term premium). This could hinder the full transmission of the Fed's monetary easing. Furthermore, this cannot be taken for granted, as it remains dependent on data developments and the balance of risks.

In the UK, persistent inflation is limiting the BoE's room for manoeuvre to continue easing monetary policy, while fragile growth is complicating the calibration of fiscal consolidation, all under the watchful eye and pressure of bond markets, which further complicates the situation. In Japan, the policy mix is the opposite but no easier to implement. Monetary policy is in a tightening phase (from a very accommodative level) to contain inflation, while the expansionary bias of fiscal policy is likely to persist and fuel inflationary pressures, with the economy at full employment. The challenge for the BoJ is to avoid falling "behind the curve" by raising rates too little and/or too late, while fiscal issues are also putting upward pressure on Japanese long-term rates.

### The ECB is in a more comfortable position

In the Eurozone, there is a one-size fits all monetary policy, while fiscal policies are national. At least the European Central Bank is in a more comfortable position than its peers. It has brought its monetary policy back to a broadly neutral stance, with inflation in line with its target. Moreover, in the short term, if it were to take further action, it would be in the direction of easing, given the fragility of the recovery. In terms of fiscal policy, the situation also looks good for the Eurozone as a whole: the fiscal impulse would be moderately expansionary in 2026, with the (controlled) increase in the German budget deficit being partially offset by an improvement in the primary balances of France, Spain and Italy.

*Article completed on 19 September 2025*

**Hélène Baudchon**

<sup>7</sup> Find all our forecasts at the end of the publication and in each country fact sheet in graph format.

<sup>8</sup> As highlighted in the latest CBO analysis: *CBO's Current View of the Economy From 2025 to 2028*, September 2025.

<sup>9</sup> Since the beginning of the year, US long-term rates have experienced some moments of tension (particularly around Liberation Day). But the relative deterioration in the macroeconomic outlook, fuelling expectations of Fed rate cuts, has pushed them down quite sharply, to the point where, on 18 September, they were nearly 70 basis points lower than in mid-January, at the peak of the "Trump trade", once again closer to 4% than 5% as at the beginning of the year. However, even at close to 4%, they are at their highest level since 2007.



**BNP PARIBAS**

The bank  
for a changing  
world



## INTERNATIONAL TRADE: IT'S NOT ALL ABOUT THE UNITED STATES

US tariffs rose sharply in two stages: first in April, then following the signing of multiple trade agreements this summer. The impact of the first stage of this tariff increase is well known: trade flows to the United States were severely disrupted. However, global trade remains dynamic, particularly in Asia (a structural phenomenon) and Europe (which should benefit from internal momentum with the rebound of the German economy). The restructuring of trade flows (already underway with the rise of China) could accelerate as different countries seek elsewhere the opportunities lost in the United States.

### US TARIFFS: A NEW WORLD

Since Donald Trump's return to the White House in January 2025, the US administration has increased its customs duties in two main phases. The first was a hike in sectoral tariffs (to 25% for cars and 50% for steel and aluminium) and the introduction of 'reciprocal' tariffs. The latter were temporarily reduced to 10% for most countries on 9 April, pending the outcome of negotiations with trading partners. This first salvo brought the average effective tariff on US imports of goods to nearly 10% in July 2025, compared with an average of 2.3% in 2024.

The completion of numerous bilateral agreements in July and August<sup>1</sup> and the application of higher tariffs for non-signatory countries marked the second stage, which takes the average tariff to 17.6% according to our estimates (see Chart 1). Products from China would continue to make the largest contribution (of the 17.6 percentage points, nearly 5.5 are linked to tariffs levied on Chinese products). However, among the main partners, it is the European Union and the USMCA countries that are seeing the biggest increase in their contribution to this tariff (notably due to the weight of trade between these two areas and the United States).

This sequence has caused significant volatility in the volume of goods imports into the United States. After rising by +11.0% q/q in Q1 2025, they fell by -10.1% in Q2. However, year-on-year, imports rose for the fourth consecutive half-year in H1 2025, up +4.7% from one half-year to the next (+11.8% y/y). This shows that the decline in Q2 (Chart 2) has not yet fully offset the sharp increase in Q1. The stability of the capital goods category – which accounted for 31% of imports in 2024 – in Q2 after the jump in Q1 (+10.5% q/q) explains this growth. Unsurprisingly (with customs duties raised to 25%), the automotive sector suffered a sharp decline in H1 2025 (-3.8% compared to the previous half-year) after a sharp decline in H2 2024 (-4.9%). Imports are also penalised by subsidies granted to manufacturers of cars produced in the United States, support from which imported vehicles do not benefit. As the trade agreements negotiated this summer come into force, trade flows to the United States could decline more sharply for the sectors concerned.

### WHILE THE UNITED STATES IS IMPORTING LESS, OTHER REGIONS CONTINUE TO IMPORT MORE

The US tariff shock highlighted the adaptability of global trade flows. While imports declined in the US in Q2, they rose in other regions of the world (see Chart 2). This was particularly noticeable in the Eurozone, where imports rose by 2.5% q/q, a similar pace to Q1. Europe is one of China's most important substitution markets, as the structure of the European market is similar to that of the United States. Imports also increased in Latin America and Japan (up 3.8% q/q in Q2). In China, im-

<sup>1</sup> Notably with the European Union (15% tariffs), Japan (15%), South Korea (15%), Taiwan and ASEAN countries (19%-20%), the United States' main partners, while the 'truce' with China has been extended.

EVOLUTION OF THE EFFECTIVE TARIFF RATE ON IMPORTS OF GOODS IN THE US (TOTAL IN %, NATIONAL CONTRIBUTIONS IN PP)

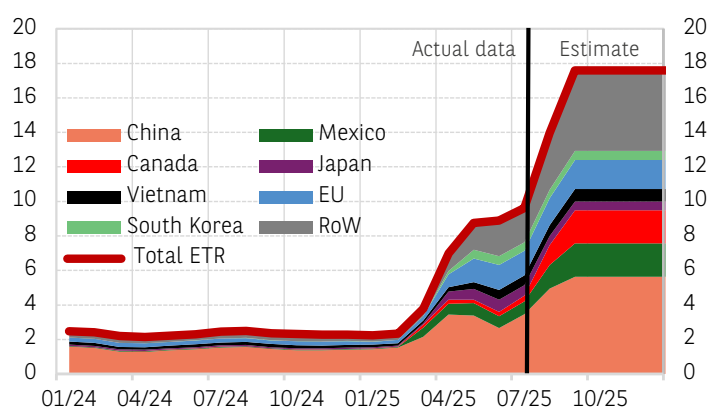


CHART 1

SOURCE: US CENSUS BUREAU, BNP PARIBAS CALCULATIONS

EVOLUTION IN IMPORTS SINCE DECEMBER 2024 (IN VOLUME, %)

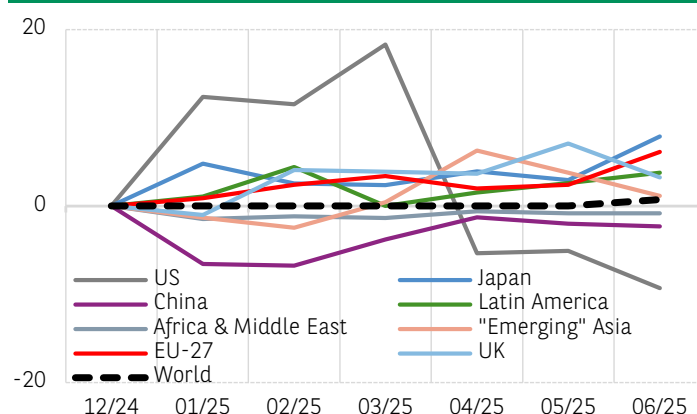


CHART 2

SOURCE: CPB, EUROSTAT, ONS, BNP PARIBAS

ports initially declined as the country retaliated by raising tariffs on the United States, but much of this decline was subsequently reversed.



BNP PARIBAS

The bank  
for a changing  
world

The United States continues to account for a significant share of global imports (around 14%), but Asia's share has continued to grow, supported by sustained high economic growth and effective regional trade partnerships. Emerging Asia<sup>2</sup>, which accounts for 10% of global imports (an all-time high), has taken over from China. The latter has embarked on a policy of substituting imports with local production.

## GLOBAL EXPORTS ARE HOLDING UP WELL DESPITE THE UNCERTAINTY SURROUNDING THE AMERICAN OUTLET

As such, the US tariff offensive only affects a minority of global trade (see Chart 3). Aggregate data from the Dutch Central Plan Bureau (CPB), which serves as a benchmark in this area, clearly shows that the upward trend in global trade has not been affected (see Chart 4). After rising sharply in Q1, exports declined moderately in Q2. Ultimately, global trade is currently continuing to grow at a rate close to that of 2024, i.e. +0.8% q/q. However, US tariffs have been detrimental to countries for which the United States is an important market and which have few alternatives. This is the case for Canada, whose exports declined throughout the first half of the year.

In Europe, developments differed greatly across sectors. In nominal terms, the surge in pharmaceutical exports (and other chemical products) in Q1 was not entirely offset in Q2. Compared with 2024, the growth in these exports in H1 2025 (+31%, or nearly EUR 55 billion) more than offset the decline in automotive exports (-6.9%, or EUR 9.7 billion). This evolution obviously leads to redistributive effects between countries (clearly positive for Ireland and Switzerland, less so for Germany). However, at the EU level, these effects are broadly offset.

This resilience in global trade can also be explained by the acceleration in the trade of electronic equipment around the world. Demand for these products, which are crucial for massive investment projects in artificial intelligence (AI), originates mainly in China and, more broadly, in Asia, where they are also largely produced. This underpins much of the strength of Asian countries' exports and, above all, the steep rise in exports from South Korea and Taiwan, two key countries in the manufacture of AI equipment. As semiconductors are not currently subject to US tariffs, trade continues to grow strongly driven by large-scale investments in this area, including in the United States. In addition, the United States and China remain dependent on each other in highly strategic sectors (rare metals exported by China, semiconductors exported by the United States). This gives cause for hope that customs barriers will not hinder this fast-paced development, as is the case in the aerospace industry, which benefits from zero customs duties under the US-EU agreement given the strong interdependence between the two major industrial players in the sector.

## US TARIFFS: A MANAGEABLE SHOCK PROVIDED THEY STOP EVOLVING

There is still no data available to measure the impact of the trade agreements signed by the United States this summer. Furthermore, it is not guaranteed that US tariffs will not change again. Investigations are currently being conducted in the United States in sectors targeted for their significance (notably the pharmaceutical and semiconductor sectors, which are currently exempt from additional tariffs) under Section 232 of the Trade Expansion Act. The outcome of this investigation could lead to an increase in sectoral tariffs (the most vulnerable country for

<sup>2</sup> IMF terminology, covering 18 Asian countries (excluding China, Japan and South Korea).

US TARIFF OFFENSIVE IN RELATION TO TOTAL INTERNATIONAL TRADE (USD BN, 2024)



CHART 3

SOURCE: IMF, US CENSUS BUREAU, WHITE HOUSE, BNP PARIBAS

EVOLUTION IN WORLD EXPORTS (JAN. 2024=100)

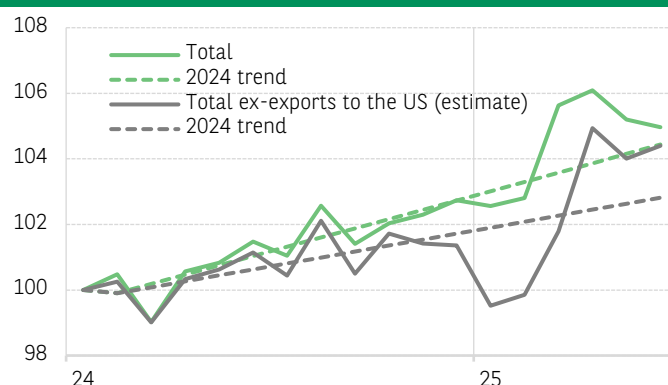


CHART 4

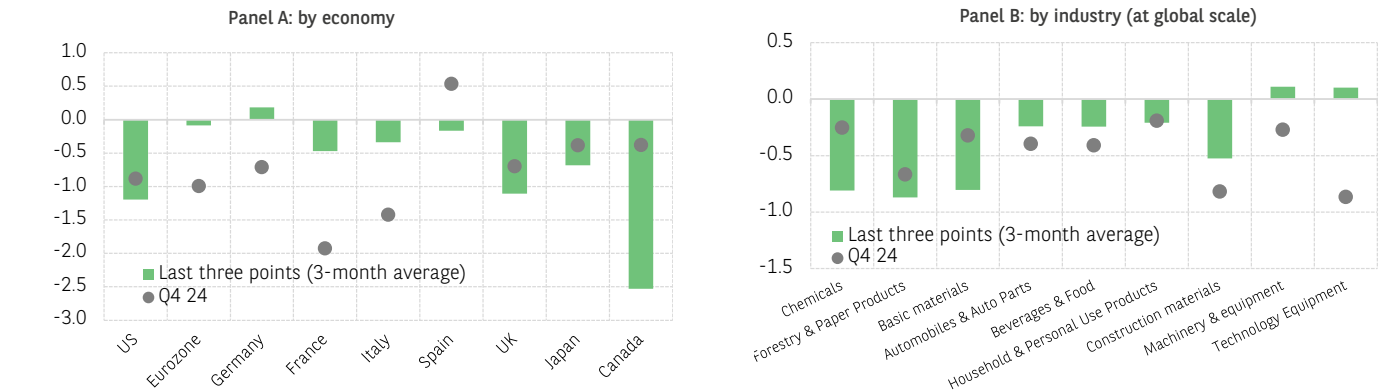
SOURCE: CPB, BNP PARIBAS CALCULATIONS

each sector considered is shown in Table 1). Furthermore, the review of the legality of the procedure used to implement 'reciprocal' tariffs has not yet reached a final verdict (the Supreme Court is expected to rule in November). A ruling against these tariffs could pave the way for an increase in sectoral tariffs. Furthermore, discussions between Washington and Beijing led to a provisional agreement on 12 May to reduce the level of bilateral tariffs from the high level reached in April. This provisional agreement has since been renewed and remains in force in the absence of a final agreement for the time being.

However, according to business climate survey data, most of the uncertainty shock created by the US administration in April has subsided, particularly in Europe. The PMI index for new export orders has recovered in most countries (see Chart 5): where figures are available for July (France), exports to Germany are rebounding; this phenomenon is expected to strengthen in the second half of 2025.



MANUFACTURING PMI NEW EXPORT ORDERS (Z-SCORE)



Z-score based on the 15-year average (August 2010–August 2025)  
Sectoral PMIs cover more than 40 countries.

SOURCES : MARKIT, BNP PARIBAS CALCULATIONS

GRAPHIQUE 5

The customs duties imposed on US imports from the EU have been raised to 15%, but this includes pre-existing customs duties. The appreciation of the euro is a second brake on competitiveness (nearly 10%). The overall shock is similar to that experienced by companies in 2007-08 (linked solely at the time to the sharp depreciation of the dollar). While this remained manageable in terms of volumes (which were relatively resilient), it had a greater impact on companies' prices and margins. This time, Europe is not the only region to suffer from increased customs duties (whereas the shock of the strong euro was specific to it in 2007-08), which could once again limit the ultimate impact on trade volumes.

The countries closest to the United States, which cannot rely on finding alternative markets for their trade, will be hardest hit by the tariff increases. The trend in Canada's new export orders index is particularly striking in this regard.

From an industrial sector perspective, according to PMI surveys, the outlook is good for capital goods (technology, machinery and equipment) and is improving for the automotive sector, which is now less heavily taxed. This is not the case for the chemical industry, where basic materials (including metals) are both more heavily taxed and increasingly subject to competition, particularly from China.

WHAT REMAINS UNKNOWN BUT WILL BE DECISIVE: WILL THERE BE AN ACCELERATION IN THE RESTRUCTURING OF TRADE FLOWS?

Trade flows were already changing before the increase in US tariffs. Will this restructuring accelerate due to the relative loss of the US market? It is possible, but not certain:

- In Asia, China now appears to be a paradoxical winner, as its close neighbours in ASEAN are also experiencing a tariff shock (the effective tariff applied to US imports of Chinese goods rose from 10.7% at the end of 2024 to 41.4% at the end of August, and the average tariff for ASEAN-5 from 2.5% at the end of 2024 to 17% at the end of August). In addition, the 40% tax on Chinese goods transiting through third countries (envi-

VULNERABILITY OF COUNTRIES TO POTENTIAL NEW SECTORAL TARIFFS ON SEMICONDUCTORS AND PHARMACEUTICAL GOODS

Rank	Semiconductors	Pharmaceutical
1	Taiwan	Singapore
2	Malaisie	Suisse
3	Israël	Israël
4	Thailand	India
5	South Korea	Canada
6	Mexico	EU
7	Vietnam	UK
8	Japan	South Korea
9	Singapore	Japan
10	Indonesia	Australia

Ranking of countries according to their vulnerability to new sectoral tariffs on semiconductors and pharmaceutical goods. Countries are ranked in accordance with the importance of the considered sector in their respective GDP. The colour code illustrates each country's respective share in aggregate imports of semiconductors and pharmaceuticals into the United States.  
The European Union is over-represented in US imports of pharmaceutical goods (60% of the total in 2024), but Ireland accounts for a significant share and vulnerability is significantly lower for most other European countries.

TABLE 1

SOURCE: US CENSUS BUREAU, NATIONAL SOURCES, BNP PARIBAS

saged by the Trump administration, but which will be difficult to implement) could reduce its ability to use these "connector" countries to circumvent US tariffs, as it has done until now.





- With regard to Europe, growing competition is not something that began with the introduction of US tariffs. This is particularly true with regard to trade between Germany and China, with the latter gradually (and particularly since the Covid-19 pandemic) shifting from being an outlet to a competitor. This appetite is likely to grow and spread to other sectors, with more exports and more investment in the EU in order to circumvent barriers to entry. This phenomenon could increase with the decline of the American market, given that China, with its structural overproduction, has no choice but to find new markets, while its domestic market is not sufficiently taking over (see Ecoweek's editorial on this subject).

Furthermore, the world will not stop rotating. The acceleration of negotiations between states, with the aim of concluding or strengthening trade agreements, shows that free trade retains solid foundations, despite being under attack from the American protectionist strategy. And Europe will not stop moving forward either. While reform of the internal market is taking time, the implementation of a common defence effort should help to create new momentum. More broadly, the revival of investment in Germany should quickly have an impact on intra-zone trade. Finally, even if it is futile to hope to replace lost market share in the United States or China, this should encourage the European Union to redouble its efforts to win new markets (EU-Mercosur agreement).

*Article completed on 16 September 2025*

**Stéphane Colliac, Guillaume Derrien, Anis Bensaidani**

With the help of Benjamin Puiseux for the charts, intern.

[stephane.colliac@bnpparibas.com](mailto:stephane.colliac@bnpparibas.com)

[guillaume.a.derrien@bnpparibas.com](mailto:guillaume.a.derrien@bnpparibas.com)

[anis.bensaidani@bnpparibas.com](mailto:anis.bensaidani@bnpparibas.com)



**BNP PARIBAS**

The bank  
for a changing  
world

# UNITED STATES

10

## SLOWDOWN UNDERWAY

Growth in the United States has slowed significantly compared with 2024 and is expected to remain moderate in the coming months, while maintaining some dynamism. Inflation is gradually rising again, mainly due to higher tariffs, while the labour market is already showing clear signs of weakening. These developments are resulting in a rebalancing of risks around the Federal Reserve's (Fed) dual mandate: downside risks to employment are increasing relative to upside risks to inflation. In our view, this should prompt the Fed to make two further cuts to its policy rate between now and the end of 2025, following the September cut. At the same time, fiscal policy is unlikely to stem the rise in the public debt ratio.

### SLOWER GROWTH

GDP growth slowed significantly due to uncertainty and inflation fears arising from economic policy decisions, particularly trade policy. Measured as an average over H1 2025 to neutralise the volatility caused by the sharp rise in imports in Q1 (and their decline in Q2), it fell to +0.3% q/q (+0.7% on average in H2 2024). Final sales to private domestic purchasers also slowed (+0.5%, compared with +0.8% previously). At an average of +0.3%, consumption eased sharply (vs. +0.9% in H2 2024). Residential investment contracted during the last two quarters and stood 12% below H2 2021 at the same time. Conversely, business investment picked up, with average growth of +1.9% (+0.1% in H2 2024).

Available data for Q3 are generally encouraging. Retail sales were robust in July and August. At the same time, the two-sided trend in investment continues, with difficulties in housing starts (-8.4% m/m in August) and building permits (monthly contraction in July and August), but core durable goods orders rising in July. According to our forecasts, the average annual growth rate should reach 1.7% in 2025 (+2.8% in 2024), largely helped by the carry-over effect from the previous year (1.0 pp), then 1.5% in 2026.

### FOREIGN TRADE: BEYOND THE SPRING PEAK, A LASTING UNCERTAINTY SHOCK

The United States has been subject to very few tariff retaliations, apart from China, and foreign trade contributed very slightly to growth in H1. In July, exports of goods fell to the same level as in H2 2024, as the boost seen at the end of Q1 2025 gradually faded. Previously, trade tensions had caused volatility in the trade balance for goods, while the balance for services, spared by them, remained stable (+1.0 – +1.1% of GDP). Trade policy uncertainty has receded as a result of the clarification resulting from the trade agreements announced in the summer (covering 60% of imports in 2024), but remains high (Chart 2). Finally, major issues remain unresolved, namely the investigations under Section 232 of the Trade Expansion Act, which could lead to sectoral tariffs on pharmaceuticals, chips and semiconductors, and the appeal on the legality of reciprocal tariffs before the Supreme Court (early November).

### LABOUR MARKET: STILL TIGHT, DESPITE A SHARP DROP IN JOB GROWTH

The labour market has been softening since 2024, but this trend is intensifying. This is fuelling fears of a steeper rise in the unemployment rate (4.3% in August, +0.1pp y/y). Nonfarm payrolls fell from +175k in January

<sup>1</sup> The exact scale of this reduction is a matter of debate (due to difficulties in counting and possible carry-over effects in the native population statistics). Nevertheless, it highlights the risk that deportations pose to the US labour market.  
<sup>2</sup> The 'break-even' unemployment rate corresponds to the number of jobs needed to keep it stable in relation to changes in the labour force. We currently estimate this to be 35k–50k, compared with 70k–100k previously.

#### GROWTH AND INFLATION (YEARLY AVERAGE)

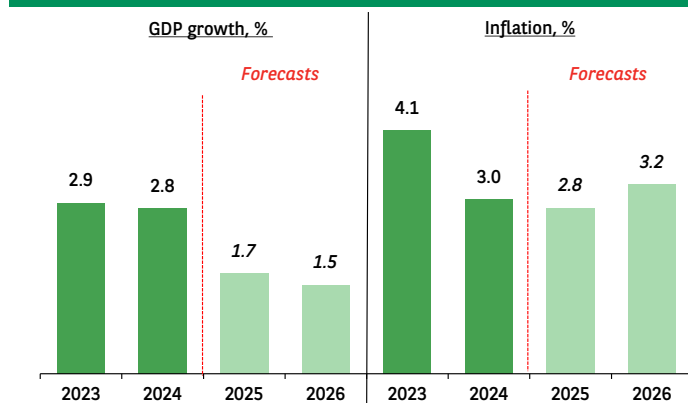


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

to +64k in August (6-month moving average). The government sector (+1k monthly average since January) echoed the associated policy, while the leisure and hospitality sector slowed (+8k, +20k annual average in 2024). Manufacturing employment declined (-5k). The weakening was reflected in the BLS's latest annual revision of salaried employment between April 2024 and March 2025, which reached -911k in the preliminary estimate (an all-time high). The labour supply is being penalised by the new and particularly restrictive migration policy, which coincides with a reduction of 1.5 million non-native workers between March and August 2025<sup>1</sup>. At the same time, the labour force participation rate fell by 0.2 pp to 62.3%.

For the time being, the unemployment rate is still within the 4.0% to 4.3% band, in line with or slightly below full employment. Our baseline scenario anticipates stabilisation in the short term, as growth in the available labour force and the pace of payroll growth<sup>2</sup> are slowing simultaneously. The 'curious kind of balance' outlined by Jerome. Powell is reflected in underlying measures of labour market stress. The lack of movement among hires, resignations and dismissals suggests a widespread wait-and-see attitude, while the ratio of job vacancies to unemployed individuals is close to 1 (compared with 2.1 before the start of monetary tightening and an average of 0.6 between 2001 and 2019).


**BNP PARIBAS**

The bank  
for a changing  
world

## INFLATION: NO SECOND-ROUND EFFECTS?

The pass-through of higher tariffs to inflation is becoming more evident. CPI inflation rose in Q3 (+2.9% y/y vs. +2.4% in Q2), driven by core goods (+1.5% y/y in August, vs. an annual average of -1.1% in 2024). This trend is likely to continue. Trends on the prices paid sub-component of the ISM survey, a leading indicator of core inflation, have unprecedented since 2022 (Chart 3). Non-energy services, housing and non-housing, are slowing overall, but remain well above 2%, at +3.3% and +3.6%, respectively. Therefore, we are forecasting inflation to rise to a peak of +3.5% y/y in Q2 2026.

The main risk lies in the likelihood of second-round effects from this tariff-induced inflation, which are unlikely at this stage as long as the economic slowdown continues. Market inflation expectations remain well anchored, although the deterioration in household expectations is a warning to be monitored. Jerome Powell adopted the view of the doves on his board. He felt that wage inflation was 'not [...] likely' due to 'increasing downside risks' in the labour market, and therefore considered a 'one-time shift in the price level' to be a 'reasonable base case'.

## FOMC, THE DOVE'S CALL

While tensions intensify on both sides of the Fed's dual mandate, developments and downside risks in the labour market are resulting in a reallocation of risks towards the 'maximum employment' component. Therefore, the Fed cut its target rate by 25 bps in September, to +4.0% - +4.25%, in a 'risk management' effort. According to our forecasts, this is initiating a cycle of monetary easing that will continue until the terminal rate of 3.0% (upper limit) at the end of H1 2026, including two further 25-bp cuts by end-2025. In 2026, the materialisation of inflationary risks and the resilience of the economy should not justify more than two additional rate cuts. However, the further emphasis on employment means that the risks associated with this baseline scenario point to further rate cuts should things worsen. At the same time, the question of the Fed's independence is drawing considerable attention. This is a major issue that carries material risks (increased inflation premium, bond pressures and/or weaker national currency).

## DEFICIT STABILISING AT A DANGEROUS LEVEL

The administration's fiscal policy is not expected to get the public accounts in order<sup>3</sup>. The One, Big, Beautiful Act (OBBA) budget reconciliation bill, enacted on 4 July, is expected to have an adverse impact on the federal deficit, which the Congressional Budget Office (CBO) estimates at between USD 4.113 trillion and USD 4.971 trillion over the 2025-2034 period. The CBO also estimates that tariff revenues will reduce the deficit by USD 4 trillion over the same period, which, all other things being equal, would offset most of the impact of the OBBA and limit the increase in the deficit. Under these conditions, we estimate that the federal deficit will stand at -5.5% in 2025, corresponding to a negative fiscal impulse, and between -5.5% and -6.0% of GDP over the 2026-2029 (-6.4% in 2024) period. These would be particularly high levels, contributing to an increase in the public debt-to-GDP ratio (97.8% in 2024, rising to 99.9% in 2025 and 101.7% in 2026).

In the meantime, relative bond pressure is emerging: the US 30-year yield approached 5.0% in August (compared with an average of 4.7% in H1 2025), before falling back following disappointing economic data.

<sup>3</sup> See our Ecolnsight: [The US Treasuries Market: An Idol with Feet of Clay](#), [US Federal Debt: The Risks of Abundance](#)

### UNITED STATES: TRADE POLICY UNCERTAINTY (30-D MMA)

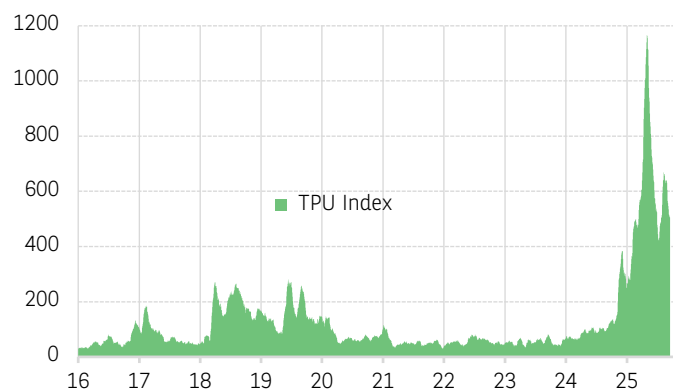


CHART 2

SOURCE: MACROBOND, BNP PARIBAS

### UNITED STATES: PRICES PAID AND CORE CPI

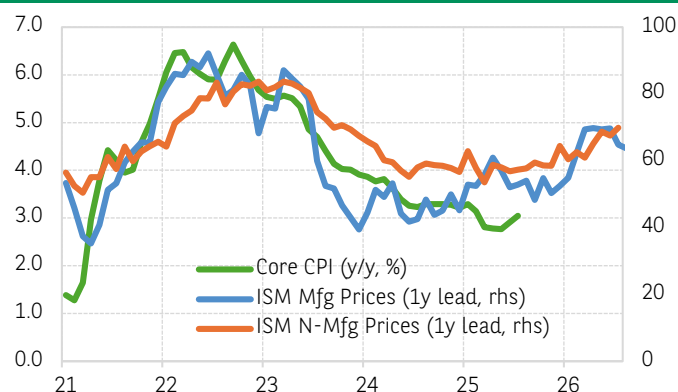


CHART 3

SOURCE: BLS, ISM, BNP PARIBAS

At the same time, the Treasury is stepping up its securities buyback programmes. It has acquired USD 135 billion in securities since 20 January 2025 in order to reduce the interest burden by shortening the average maturity of the debt. However, this practice increases the liquidity risk on short maturities that are in high demand.

Article completed on 18 September 2025

**Anis Bensaidani**

[anis.bensaidani@bnpparibas.com](mailto:anis.bensaidani@bnpparibas.com)



**BNP PARIBAS**

The bank  
for a changing  
world

# EUROZONE

12

## GROWTH SET TO STRENGTHEN

Growth in the Eurozone has so far proved fairly resilient to shocks (accompanied in particular by an acceleration in new lending against a backdrop of falling interest rates) and should gradually accelerate. Exports will continue to be weakened by Chinese competition and US protectionism. However, the foreseeable rebound in German growth will benefit economic activity in the Eurozone as a whole. Moreover, the buoyant labour market is supporting household purchasing power, without generating inflationary pressures, giving the ECB visibility and room for manoeuvre if necessary.

### GROWTH: RESILIENCE IN 2025, ACCELERATION THEREAFTER

Growth was uneven in H1 2025, due in particular to the sharp increase in exports to the United States in Q1 (Germany, Ireland), followed by a contraction in Q2. Even so, activity remained relatively sustained (0.3% q/q on average over the first half of the year), despite the increase in US customs tariffs. Growth should be similar in H2 2025 (+0.2% in Q3, +0.3% in Q4), before strengthening in 2026 (+0.5% on average per quarter). Increased military spending in Europe and plans to support public and private investment in Germany should add 0.3 and 0.5 points of growth in 2025 and 2026 respectively. In particular, a buoyant labour market and moderate inflation should support household consumption. The industrial recession should come to an end (the manufacturing PMI rose back above 50 in August for the first time in three years), enabling [Germany](#) and [Italy](#) to gradually return to growth. The need to step up spending linked to the energy and ecological transition, combined with the past cut in ECB rates and the resulting rise in the volume of credit, will also support business investment.

### MOMENTUM IN NEW LENDING COULD BE MODERATED

New NFC investment loans remained sustained in July 2025 (year-to-date, +15.2% y/y) while interest rates have been relatively stable since February (around 3.6% for those with an initial rate fixation period >5 years). The rate on new treasury loans (variable rate and initial rate fixation period <3 months) continued to fall in July 2025 (-5 bp m/m to 3.31%), but should stabilise. New treasury loans cumulated over one year accelerated in July 2025 to 9.0% y/y, which could reflect cash flow difficulties for some businesses or an increase in inventories.

As far as households are concerned, the stability in the average rate of new loans for house purchases across all maturities in H1 2025 (3.3% between February and July) could broadly continue in H2. The pricing of fixed-rate loans (around 75% of new home loans in the Eurozone) is largely based on the 10-year/3-month swap rate (plus a liquidity premium), whose fall since 2024 contrasts with the rise in sovereign rates. As a result, the cost of new fixed-rate loans (over 10 years) remained stable at 3.12% between April and July 2025. This is likely to remain the case as the ECB is no longer expected to cut rates in our scenario. As a result, new home loans will lose the main factor underpinning their recent dynamism (year-to-date, +28.7% y/y in July 2025). What is more, some households taking a wait-and-see approach could be encouraged to buy if they no longer anticipate a further fall in interest rates. With banks and households expecting demand for consumer credit to remain relatively stable, consumer credit should continue to grow at a rate close to that currently seen (year-to-date, +1.3% y/y in July 2025), while the rate remains historically high (7.5% in July 2025 compared with an average of 5.5% between 2018 and 2022).

### GROWTH AND INFLATION (YEARLY AVERAGE)

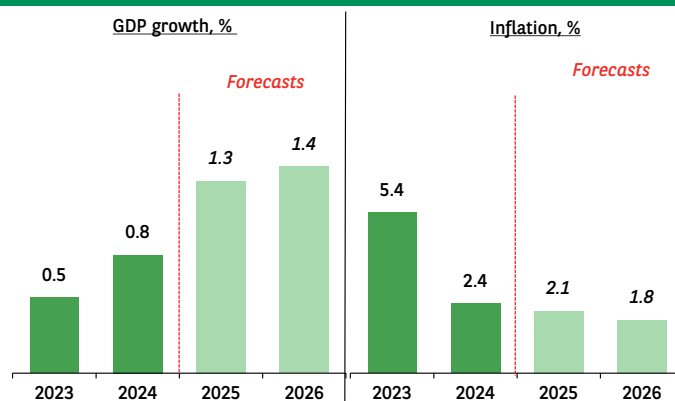


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

### TENSIONS ON THE LABOUR MARKET MAY INCREASE

At 6.2% in July, the unemployment rate in the Eurozone was comparable to its historic low and should continue to fall. Heterogeneity between countries is narrowing. The rise in unemployment seen in France and Germany over the past year has been limited (+0.2 points and +0.3 points over one year). This is largely offset by the improvements seen in southern Europe, which are set to continue. With the European Commission estimating that the minimum unemployment rate required to prevent inflation from accelerating (NAIRU) in the Eurozone is 6.5%, the labour market is already under pressure. A further fall in the jobless rate could be accompanied by greater wage pressures. At the same time, the rebound in productivity gains is insufficient to lower unit labour costs (+3.1% y/y in Q2), which are the most relevant indicator of production costs. Nevertheless, in the short term (to the end of 2025), wage rises should ease, helping to bring down inflation in services (see [chart 2](#)).

### INFLATION: LITTLE DEVIATION FROM TARGET

Inflation should remain stable at around the 2% target, and the risks balanced: while internal dynamics (tighter labour market, wage growth outstripping productivity gains) are likely to fuel price rises, particularly in services, exogenous factors should moderate them: the EUR/USD should continue to appreciate moderately (to 1.22 at the end of 2026, according to our forecasts), the stabilisation of hydrocarbon prices should ease the energy component, while freight costs have continued to normalise after the tensions of 2024. In addition, the rise in imports


**BNP PARIBAS**

The bank  
for a changing  
world

from China has been amplified by the fall in the yuan, and this trend could continue. From this perspective, this imported disinflation would limit the risk of a reacceleration in inflation in the Eurozone.

### THE ECB IN A GOOD POSITION

Given the inflation outlook, the ECB is in a comfortable position. At the current 2% on the deposit facility rate, the cycle of interest rate cuts is over, in our view, as activity is expected to strengthen. Faced with a more frequent risk of a shock to prices and activity, the ECB will tolerate even prolonged deviations from the target, as long as they are not too large and do not jeopardise the anchoring of inflation expectations - an objective that has been achieved so far (according to the ECB, the median long-term inflation expectations of households (5 years) were stable at 2.1% in July). This tolerance is reflected in the ECB's latest autumn macroeconomic projections (September 11), with inflation forecast to be below the 2% target in 2026 (1.7%) and 2027 (1.9%). Nevertheless, in the event of a negative shock implying a persistent downside risk to inflation forecasts, the ECB has left the door open to further cuts in its key rates. At the same time, the process of quantitative tightening should continue with a policy of passive sales, leading to a further reduction in the ECB's balance sheet in 2026.

### THE INCREASE IN THE BUDGET DEFICIT SHOULD REMAIN UNDER CONTROL

European fiscal policy will be moderately expansive in 2026. The public deficit in the Eurozone is set to increase in 2025-26, but will remain close to the 3% of GDP target. The increase in Germany's deficit would be offset by an improvement in the primary balance in France, Italy and Spain. The rise in bond yields would have a relatively limited short-term effect on debt servicing, due to the lengthening of the average maturity of sovereign debt (8.3 years on average in the Eurozone) but would gradually increase the fiscal consolidation effort in the least well-positioned countries, France in particular. The launch of the European defence lending facility (SAFE, with European countries having to submit their requests to the Commission by 30 November) and the escape clause (allowing national governments to increase their defence investment by up to 1.5% of GDP for 4 years, without this being taken into account in the calculation of the public deficit) will nonetheless facilitate part of the consolidation effort at national level.

### EXPORTS ARE FACING INCREASING HEADWINDS

Tariff shock in the US, appreciation of the euro, China's move up the value chains: the obstacles to European exports are adding up in 2025. While the evolution of US trade policy remains uncertain, the agreement with the United States (taxing the majority of European exports at 15%) is more favourable than for most countries (notably because, in the case of the EU, this 15% includes pre-existing and, in principle, future tariffs). Competition from China, which is a major structural brake on European exports, has become tougher since Covid and the depreciation of the yuan, which began in 2022: Eurozone export volumes to China have fallen by 33% (Dec. 2019-June 2025, see chart 3) and by 27% to ASEAN over the same period. The structural decline in activity in intermediate sectors (chemicals, plastics, iron & steel), against a backdrop of economic decarbonisation, will be particularly difficult to reverse. At the same time, European imports from China have soared by 41%. Faced with the risk to demand from the US and China, the EU is seeking greater diversification (Mercosur, India, Philippines, Indonesia), but first and foremost it will have to boost its internal trade.

#### EUROZONE: EVOLUTION OF WAGES AND INFLATION

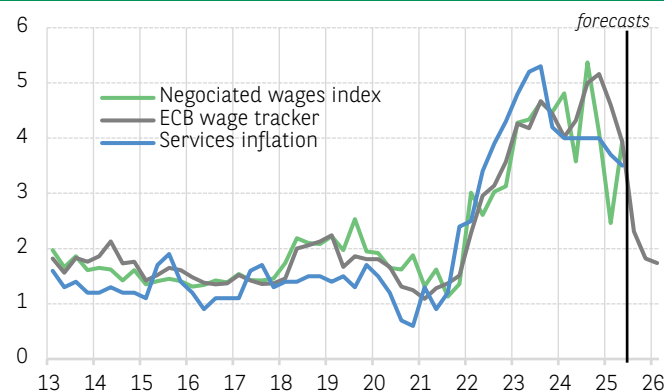


CHART 2

SOURCE: ECB, EUROSTAT, BNP PARIBAS

#### EUROZONE: BILATERAL TRADE WITH CHINA

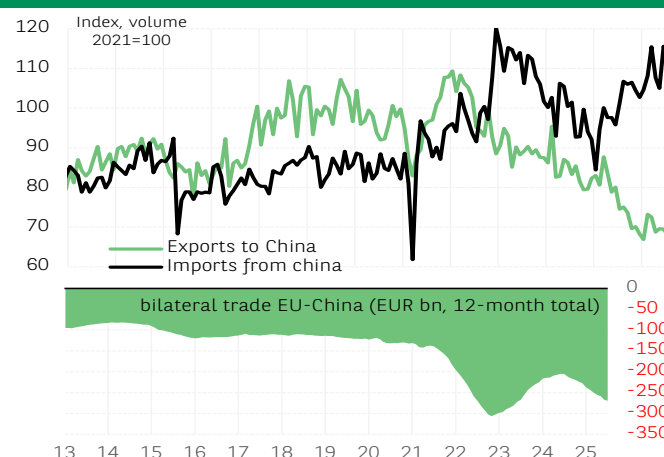


CHART 3

SOURCE: ECB, EUROSTAT, BNP PARIBAS

Intra-Eurozone exports have in fact fallen by 2% since the end of 2019 (see our [focus](#) in this issue for a more global overview of the latest developments in international trade).

Trade tensions between the EU and China have been rising steadily since autumn 2024, when European taxes on Chinese electric vehicles were introduced (China has also retaliated by imposing taxes on spirits and pork). However, the imbalance between the two zones continues to grow. Once the post-Covid normalisation effect had worn off (imports from China and the EU's bilateral deficit had surged in 2020-2021), the deficit started to rise again from 2024 onwards. Competition from Chinese goods in Europe therefore continues to grow and is likely to increase with the probable rerouting of Chinese exports to the United States to Europe.

Article completed on 12 September 2025

**Guillaume Derrien, Thomas Humblot**

[guillaume.a.derrien@bnpparibas.com](mailto:guillaume.a.derrien@bnpparibas.com)

[thomas.humblot@bnpparibas.com](mailto:thomas.humblot@bnpparibas.com)



**BNP PARIBAS**

The bank  
for a changing  
world



# GERMANY

14

## A RECOVERY IN THE MAKING

The resumption of German growth has been hampered by US tariffs. However, the outlook continues to brighten thanks to the government's strategy, which is structured around a vast programme of public investment and incentives for business investment. Beyond the anticipated economic rebound, the structural recovery of growth will depend on the country's ability to control its value chains and reposition itself in global trade amid increased competition. Inflation is expected to continue to decline. Despite unfavourable developments in industry, unemployment remains contained, and labour market tensions could quickly resurface. Public debt is expected to grow as a result of the widening budget deficit and rising interest rates (the effects of which will be felt by other Eurozone members).

### DESPITE A DIFFICULT FIRST SEMESTER, ECONOMIC RECOVERY SEEMS TO BE UNDERWAY

After a dynamic start to the year (+0.3% q/q in Q1), driven by a surge in exports in anticipation of higher US tariffs, activity declined in Q2 (-0.3% q/q). While exports are experiencing an expected backlash, their decline is moderate. The decline in investment in machinery and equipment, as well as in construction, explains the negative figure for Q2. Yet this decline could be explained by the postponement of projects that will benefit from support (for businesses) and additional funding (for infrastructure and defence, see below) from the second half of the year onwards – an analysis that is corroborated by the nine-month uninterrupted recovery in the Ifo business climate index (+4.2 points between last December and August, when it reached 89 points). At the same time, household consumption remains constrained by deteriorating sentiment. In mid-2025, real GDP will thus remain close to its end-2019 level<sup>1</sup>.

In a context where external pressures are likely to persist, the recovery will depend on the new government's economic policy. This policy aims to support a rebound in public and private investment (notably through the accelerated depreciation of investment scheme, which reduces corporate tax). The first effects are expected in the second half of the year, before accelerating in 2026 due to anticipated spillover effects. The diagnosis of a decline in investment in Q2 linked to a postponement of these expenditures reinforces the expectation of an imminent rebound. Our growth forecasts are +0.3% in 2025 and +1.4% in 2026 (after -0.5% in 2024), respectively 0.1 point below and 0.2 point above the Consensus Forecasts for September.

### EMPLOYMENT LEVELS OFF, BUT UNEMPLOYMENT RATE REMAINS LOW

Although job creation momentum has slowed due to the industrial recession, the labour market remains historically strong. After hitting a low of 3% in 2023, the unemployment rate gradually rose to 3.7% in July 2025 – still a low level, particularly compared to the Eurozone average of 6.2%.

Job losses continue in the manufacturing sector (-85,000 in H1 2025, -220,000 since 2023), in contrast to the services sector, which continues to create jobs, particularly in health and social services (+120,000 in H1 2025).

In the short term, the economic recovery should boost labour demand and support new hiring. However, in the longer term, labour supply could become a constraint: without sufficient and appropriate immigration, demographic trends are likely to lead to labour shortages, particularly for skilled workers.

<sup>1</sup> For comparison, see the 'growth' chart on the charts page at the end of this publication.

#### GROWTH AND INFLATION (YEARLY AVERAGE)

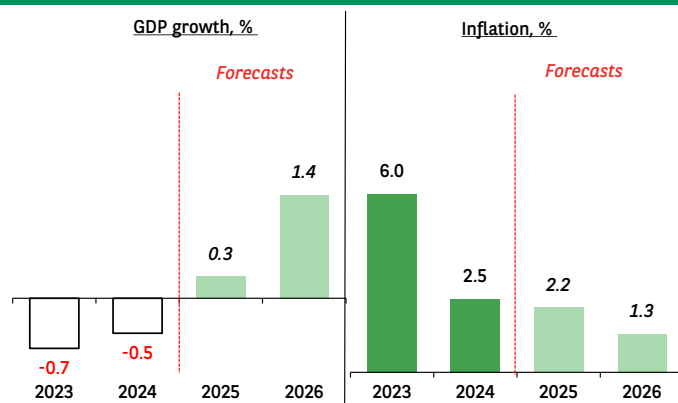


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

### DISINFLATION IS EXPECTED TO CONTINUE BEYOND THE ECB'S TARGET

Inflation has slowed significantly, and this trend is expected to continue. After averaging +2.5% in 2024, harmonised inflation is expected to settle at +2.2% in 2025 and +1.3% in 2026. Energy is expected to continue to pull the index down (particularly if the planned reduction in electricity taxes is effectively implemented) while services inflation would continue to ease as wage growth slows (labour cost index up +3.4% y/y in Q2 25, after +2.5% in Q1 but an average of +5% between 2022 and 2024).

However, several factors could hinder the continuation of disinflation, such as the planned increase in the minimum wage (EUR 13.9 in 2026, then EUR 14.6 in 2027, vs. EUR 12.82 currently) and the German investment and European rearmament plans, which are likely to revive wage pressures in the long term.

### AN AMBITIOUS FISCAL POLICY WITH CONSEQUENCES BEYOND THE COUNTRY'S BORDERS

Germany is undergoing a major shift in its economic and fiscal policy under the Merz government. A EUR 500 billion fund, spread over twelve years, is intended to modernise public infrastructure and accelerate the low-carbon transition. The defence budget is also expected to increase significantly. These measures have required a relaxation of the 'debt brake'.


**BNP PARIBAS**

The bank  
for a changing  
world

At the same time, the government is undertaking a series of reforms aimed at supporting businesses. As these reforms are not covered by the relaxation of the debt brake, their cost will have to be offset by austerity measures. A reform of social security benefits is being considered to achieve this, although no consensus has yet been reached between the various stakeholders in the ruling coalition.

This new German fiscal policy implies increased borrowing and is likely to widen the budget deficit, which, according to our estimates, would rise from -2.8% of GDP in 2024 to -3.8% in 2025 and -4.4% in 2026. At the same time, public debt would reach 66% in 2026 (compared with 62.1% of GDP in 2024). The 10-year Bund would continue to rise to 3.2% at the end of 2026 (compared with 2.66% at the beginning of September 2025) – a significant development for the Eurozone as a whole, for which German rates are the benchmark.

### ↔ GERMAN FOREIGN TRADE, A PILLAR OF ITS ECONOMY, IS WEAKENED

In 2025, exports still account for nearly 41% of German GDP and help to maintain recurring external surpluses (current account balance of +120 billion in H1 25, stable at around 5.5% of GDP). However, this traditional driver of prosperity has not been driving growth for several years.

This is due to the loss of outlets in two key markets. Exports to China, whose competitiveness has risen, have been falling for three years now (-28% in value seasonally adjusted since January 2022, latest data in July). And with the tightening of US trade policy, the last significant growth driver is now fading. German exports to the United States fell by 2.8% y/y in value seasonally adjusted in the first half of 2025, leading to a deterioration of EUR 3.9 billion (-11%) of the bilateral balance in one year.

The European Union, Germany's largest trading partner, has helped to offset some of these losses. However, given the size of the markets lost, the country has no choice but to seek further growth domestically. The reorientation of the German growth model towards investment, potentially financed by better mobilisation of domestic savings, could lead to an increase in imports and reduce the current account surplus, which would nevertheless remain comfortable.

### ↗ WHAT ARE THE LEVERS FOR GROWTH?

In the short term, renewed growth could be achieved through better mobilisation of labour and capital, which are currently under-employed (capacity utilisation in manufacturing stood at 77.2% in Q3 25, nearly 6.5 pp below the historical average). However, these adjustments would only restore potential growth to a level that is already historically low. Estimated at 2.5% in the 1970s, it stood at 1.4% between 2000 and 2019, and has been below 1% since 2020. This decline can be explained by a weaker contribution from capital – a consequence of insufficient private and public investment – by slowing productivity gains and, more recently, by rising unemployment.

#### GERMANY: CHANGES IN GDP AND ITS COMPONENTS

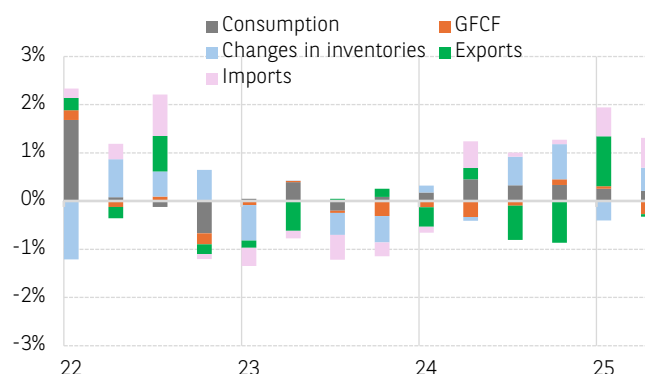


CHART 2

SOURCE: FEDERAL STATISTICAL OFFICE

#### GERMANY: NEW DEBT ISSUANCE AND PUBLIC DEBT RATIO

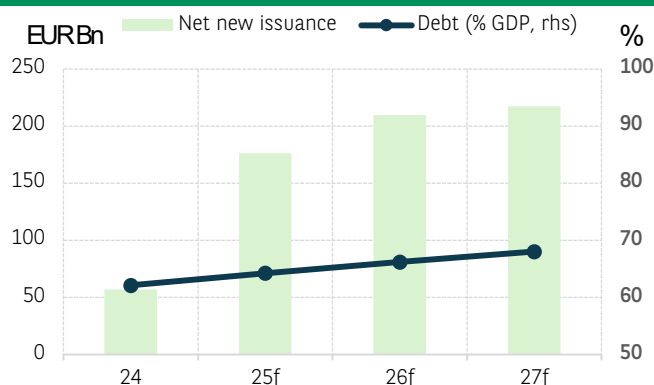


CHART 3

SOURCE: FEDERAL MINISTRY OF FINANCE, BNP PARIBAS FORECASTS

However, the coming years are set to be particularly challenging in view of demographic ageing and the fact that the energy transition – another major challenge – will have to be carried out in an economy dominated by energy-intensive industries. In the face of these challenges, the new government's economic policy is a source of optimism. By focusing on modernising and strengthening productive capital, as well as supporting innovation to boost productivity gains, it could partially offset the potential contraction in the labour factor. It remains to be seen whether these ambitions will actually and quickly translate into tangible results.

Article completed on 18 September 2025

**Marianne Mueller**

[marianne.mueller@bnpparibas.com](mailto:marianne.mueller@bnpparibas.com)



**BNP PARIBAS**

The bank  
for a changing  
world

## FRANCE

16

## TOWARDS A SUSTAINED REBOUND IN GROWTH

France recorded a rebound in growth to 0.3% q/q in Q2 2025 after a more unfavorable period marked by political uncertainty. Although this uncertainty persists, the rebound in growth should be sustained. Unlike the political situation, other aspects of the French economy have improved (agricultural and aeronautical production, interest rates in the private sector, investment) or are on track to do so (German demand). The stabilization of the labor market and the sharp increase in business creation already confirm the rebound.

### GDP GROWTH: AFTER WINTER COMES SPRING

French growth is recovering after several quarters below the Eurozone average. Beyond budgetary uncertainty, stagnant aeronautics production (supply constraints) and declining agricultural production weighed on growth until Q1 2025. Only the trend growth in services continued to support it.

Spring 2025 saw the beginning of a rebound in production thanks to a one-off effect in agriculture (return to normal wheat production) and another, more structural effect in aeronautics (new production capacity). The rebound in German growth in 2026 should add to the support provided by services, aeronautics, and housing (see below) to enable French growth to return in 2026 to the pace recorded in 2024 (1.1%).

### LOWER BORROWING COSTS AND A REBOUND IN REAL ESTATE

After falling by 60 basis points since the beginning of 2024, mortgage rates have plateaued (3%) since February 2025. Their disconnect from the rising OAT rate can be explained by the decline in the 10-year swap rate (a more relevant indicator of changes in the cost of bank resources backing fixed-rate loans). As a result, new business volumes rose sharply in H1 2025 (+46% y/y). This momentum enabled bank housing loans outstanding to return to slightly positive annual growth (+0.1% in June) for the first time since February 2024. However, this growth remains hampered by significant repayment flows linked to the abundant loans granted during the period of low interest rates.

Improved credit conditions supported real estate purchasing power and, in October 2024, halted the decline in existing home sales volumes that had been observed since 2022. In June 2025, these had reached 906,000 transactions over 12 months (+8.2% year-on-year). Existing home prices (+0.1% q/q in Q4 2024) returned to growth in Q1 2025 (+1.0% q/q). The same is true for new housing, where, after the historic low of 2024 (264,000 cumulative annual starts in October), construction figures are on the rise again (+5.9% y/y in July, after +4.4% in June). New housing prices, which had been falling since October 2022, have been rising again since Q3 2024 (+2.0% y/y in Q1 2025). However, the disappearance of support from lower mortgage rates weighed on prices in the existing home market in Q2 (-0.6% q/q), which helped keep transaction volumes high.

The ECB's key interest rates and swap rates are expected to stabilize. As a result, mortgage rates are likely to remain close to their current levels over the coming quarters (despite the moderate rise in German and French sovereign yields, which is expected to continue until the end of 2026). This trend, combined with slower growth in household income (notably due to the end of the catch-up effects on past inflation, which will still be at play in 2025), suggests that transaction volumes and prices will remain relatively stable over the coming quarters.

#### GROWTH AND INFLATION (YEARLY RATE)

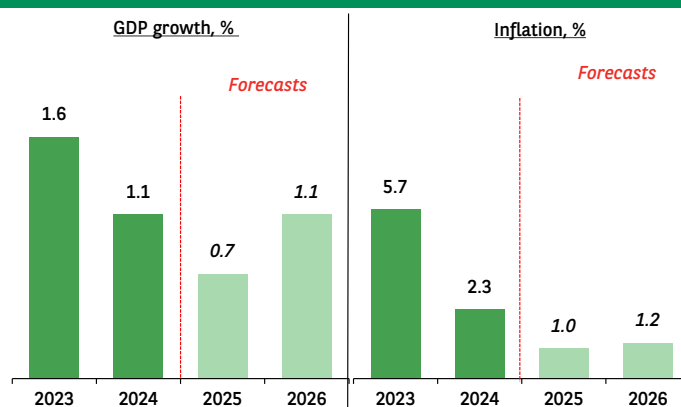


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

### FRANCE: A LAND OF INVESTMENT AND BUSINESS CREATION

The political context has led to increased uncertainty, without calling into question the main engines of the French economy. After a dip in late 2024 and early 2025, business creation has regained momentum (as has employment, see below). It reached an unprecedented level of nearly 100,000 businesses created in July 2025 (up nearly 5% on the pace recorded at the end of 2024).

Beyond the positive signs on the household investment front (+1.4% between Q3 2024 and Q2 2025), business investment has been stable for three quarters at nearly 21.5% of value added (about 2 points higher than in Germany). Its previous decline was inevitable: it had reached a historic high in Q2 2021, at 23.3% of the value added of non-financial businesses, driven by the France Relance plan. Under the effect of rising interest rates, tangible investment fell sharply until Q3 2024, and then much less so thereafter. At the same time, the groundswell of « servitization » of investment is leading to uninterrupted growth in intangible investment, which is set to continue.

### LABOR MARKET: STABILIZATION

France saw a net loss of 103,000 salaried jobs in Q4 2024 and Q1 2025. This figure has only been exceeded (excluding Covid) in 1993 and 2008, two years of recession at the end of which the unemployment rate had risen by more than 2 points. This time, it reached 7.5% in Q2 2025, marking a marginal increase (+0.2 points in one year) and is not expected to rise significantly in the coming quarters. In addition, hiring resumed in Q2, leading to an increase in salaried employment (+52,000), suggesting more of a postponement (at the height of political uncertainty) than a cancellation of hires.



BNP PARIBAS

The bank  
for a changing  
world

The rise in the retirement age since 2010 continues to support the employment rate for 55-64 year olds (+20 points in 15 years, to 61.8% in Q2 2025). In addition, the decline in real wages in 2022-23 (i.e., wages did not keep pace with inflation) contributed 2.5 points to the improvement in corporate margins. This is helping to support employment, whereas the rise in real wages in the years preceding the recessions of 1993 and 2008 had, on the contrary, penalized it.

### LOW INFLATION BUT NO INCREASE IN CONSUMPTION

Inflation has returned to its pre-COVID level (close to 1% y/y) and is expected to remain there. However, household consumption has yet to rebound. French consumers' perception in their standard of living deteriorated, which can be explained by a loss of purchasing power of wages observed in 2021-23. However, for nearly 18 months, wages have been growing faster than inflation. In addition, social benefits continue to fuel purchasing power, as do wages (both contributed equally, 0.2% each, to the 0.4% increase in purchasing power in Q2). Consumption is also growing slowly because pension increases (accounting for nearly half of the rise in social benefits in 2024 and 2025) are largely being saved (see INSEE's June 2025 economic report). Growth in household consumption is expected to remain moderate (+0.4% in 2025 and +0.9% in 2026): gains in purchasing power are real but are declining (+2.5% in 2024, +0.9% in 2025, and +0.4% in 2026 according to our forecasts). In addition, the state of public finances may weigh on household spending intentions, as households understand that most of the consolidation work remains to be done.

### FISCAL CONSOLIDATION HAS NOT YET TAKEN PLACE

An average reduction in the budget deficit of 0.5 percentage points of GDP per year is needed to bring it down to 3% of GDP by 2030 and to stabilize public debt at 120% of GDP (113.2% in 2024). This reduction actually requires a greater effort, in the order of 0.8 percentage points excluding interest charges, as interest charges are expected to increase by an average of 0.3 percentage points per year.

With this in mind, a first step would be to achieve the government's target of reducing the public deficit to 5.4% of GDP in 2025 (vs. 5.8% in 2024). However, this could be achieved by increasing revenues (including the exceptional contribution to corporate tax). France differs from other European countries mainly in terms of higher social spending. This has even increased faster than inflation, reaching 26.6% of GDP in 2024 (vs. 25.6% in 2019). This increase is unfunded (and the main cause of the rise in the public deficit), as contributions have grown at a rate close to that of wages (below inflation). As wages are now rising faster than inflation, benefits could now be under-indexed. This would reduce their share of GDP without risking a decline in the purchasing power of households' gross disposable income: a challenge for 2026 and beyond.

### FOREIGN TRADE EXPECTED TO RECOVER

While foreign trade supported growth in 2024, this was due more to a decline in imports than to an increase in exports, which were penalized by the industrial recession in Germany and Italy. The first half of 2025 saw this trend continue, particularly in the automotive sector and its inputs, which were affected by the increase in US customs duties.

However, there are reasons for hope: on the one hand, since the implementation of US customs duties, there has been no decline in French

#### FRANCE: AERONAUTICS OUTPUT (VOLUME, SA)

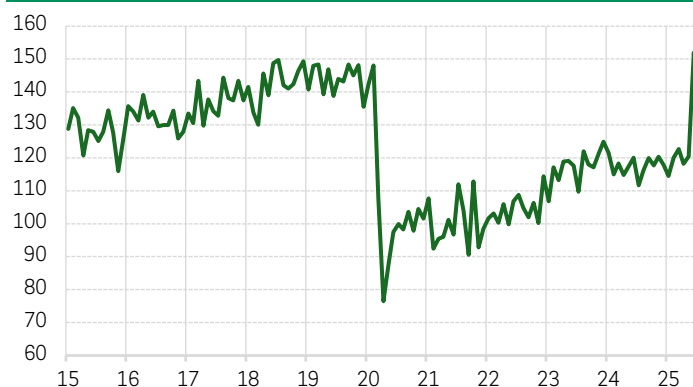


CHART 2

SOURCE: INSEE, BNP PARIBAS

#### FRANCE: MONTHLY BUSINESS CREATIONS (SA)

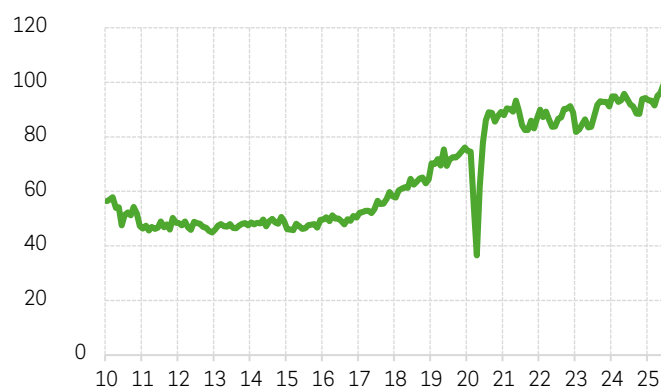


CHART 3

SOURCE: INSEE, BNP PARIBAS

exports across the Atlantic, but rather stagnation; on the other hand, the rebound in exports, already noticeable in the aeronautics and food sectors, should strengthen. Similarly, exports to Germany are growing again (after two years of decline), a trend that should be sustained by the implementation of significant investment support in Germany.

Article completed on 14 September 2025

**Stéphane Colliac, Laurent Quignon**

[stephane.colliac@bnpparibas.com](mailto:stephane.colliac@bnpparibas.com)

[laurent.quignon@bnpparibas.com](mailto:laurent.quignon@bnpparibas.com)



**BNP PARIBAS**

The bank  
for a changing  
world

## ITALY

18

## GROWTH SLOWS; PUBLIC FINANCES IMPROVE

In Q2 2025, Italy's real GDP fell by -0.1% q/q. This decline marks the end of seven consecutive quarters of growth. Investment rose (+1% q/q) but could not compensate for the fall in net exports, while industrial production slipped 1.1% y/y. Despite the challenges, the latest turnover data and qualitative indicators show an increase in activity and new orders, as well as improved business confidence. The labour market remains robust: employment held steady at 24.2 million and the unemployment rate kept falling. Inflation stayed low at 1.7%, enabling purchasing power to rebound (+0.9% q/q). Public finances have improved - the deficit has halved and a primary surplus has been recorded - but future spending pressures will increase as the working age population is projected to shrink by around 5 million people by 2040.

### IN Q2, INVESTMENT GROWTH WAS UNABLE TO OFFSET THE NEGATIVE CONTRIBUTION FROM NET EXPORTS

In Q2 2025, Italy's real GDP fell by -0.1% q/q. On the supply side, this can be explained by a decline in value added in agriculture and industry and a stagnation in services. On the demand side, growth in domestic components did not offset the decline in net exports. Final domestic consumption remained stable while gross fixed capital formation increased by 1% q/q (with investment in machinery, equipment and armaments rising by +2.1% and investment in transport equipment rising by +2.5%).

Affected by weaker foreign demand, Italian industrial production continues to decline. In the first half of the year, it fell by 1.1% y/y (vs. -1.7% in Germany, -0.3% in France, and +0.3% in Spain). Of the main sectors, only the food industry recorded positive growth.

Despite these apparent difficulties, manufacturing companies surveyed in the Bank of Italy's inflation and growth forecast survey appear slightly more optimistic about operating conditions compared to previous months. The latest data on turnover and qualitative indicators, such as the PMI indices and Istat surveys, show an increase in activity and new orders, as well as an improvement in business confidence, particularly in transport and storage services. The increase in tourist spending also reflects a modest recovery in this sector.

The Bank of Italy<sup>1</sup> has also pointed out that, despite the challenges, Italian industry has undergone a significant restructuring process in recent years. The share of employees in medium-sized and large companies has increased, as has the rollout and use of advanced technologies. The profitability and financial soundness of companies have also improved.

### LABOUR MARKET CONDITIONS REMAIN STRONG

The outlook for the labour market remains favourable. After rising in Q1 2025 (+0.5% q/q), the number of people in employment remained unchanged in Q2 (24,169 million people). The increase in self-employed workers (+74,000, +1.4% q/q) was offset by the decrease in the number of permanent employees (-21,000, -0.1% q/q) and fixed-term employees (-45,000, -1.7% q/q). The employment rate, unemployment rate and inactivity rate also remained stable compared to Q1 2025, standing at 62.7%, 6.3% and 33.0% respectively. Compared to the pre-pandemic period (Q4 2019), Italy has 1.12 million more people in employment (vs. +0.6 million in Germany, +1.8 million in France, and +2.4 million in Spain). However, the employment rate remains low compared to the EU-27 average (71.2% in Q1).

In this scenario, employment growth (measured using full-time employment figures) in 2025 and 2026 would exceed GDP growth. The

<sup>1</sup> Bank of Italy, Annual Report, The Governor's Concluding Remark, May 2025

#### GROWTH AND INFLATION (YEARLY AVERAGE)

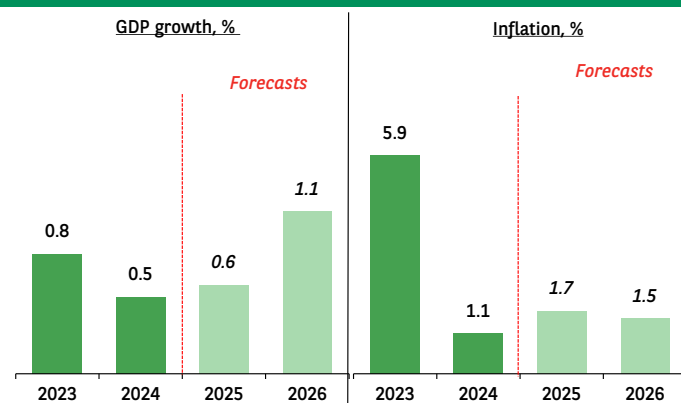


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

unemployment rate is expected to keep falling in 2025, a trend that would continue in 2026.

### CONTAINED INFLATION FUELS REBOUND IN PURCHASING POWER

In August, the Harmonised Index of Consumer Prices (HICP) recorded an increase of +1.7% y/y (unchanged from July, and lower than the Euro area average). Energy prices deflation increased, from -3.5% in July to -4.4% in August. On the other hand, food prices rose slightly (from 3.8% in July to 3.9% in August), mainly due to higher prices for unprocessed food (from 5.9% in July to 6.4% in August). Core inflation has remained stable at 2.0% since June.

With the exception of March 2025, inflation in Italy has remained below 2% since October 2023. This trend has led to a slight increase in household purchasing power, which recovered in Q1 2025 (latest data available), rising by 0.9% q/q after falling in the previous quarter.

Over the coming months, moderate inflation is expected, supported by lower energy prices and weaker demand. Private consumption is expected to grow at a moderate but stable rate (below 1% in both 2025 and 2026), supported on the one hand by wage and employment growth, and held back on the other by the climate of uncertainty, with a likely increase in the propensity to save. Indeed, in Q1 2025 (latest data available), the personal savings rate is estimated at 9.3% (+0.6 p.p. q/q).

### PUBLIC FINANCES ARE GRADUALLY IMPROVING

Italy's public finances have strengthened markedly over the last fifteen



BNP PARIBAS

The bank  
for a changing  
world



years, supported by improved macroeconomic fundamentals. In 2024, the general government deficit-to-GDP ratio halved compared to 2023 (-3.4% vs. -7.2%), and the country returned to a primary surplus (0.4% of GDP) for the first time since 2019. The Government debt-to-GDP ratio increased only moderately (135.3%).

The IMF recently highlighted Italy's better than expected fiscal results, mainly due to lower than expected expenditure and public revenues supported by a resilient labour market. The 2025 Public Finance Document, published last April, confirms the fiscal roadmap agreed by the European Commission, forecasting a deficit-to-GDP ratio of 3.3% in 2025 and 2.8% in 2026 (thus respecting the 3% ceiling set by the EU Stability and Growth Pact).

Although Italy's public debt exceeded EUR 3 trillion in June 2025, thanks to improved fiscal metrics and political stability, the spread between Italian and German government bonds has continued to narrow (83 bp vs 135 on average in 2024). In April 2025, S&P raised Italy's sovereign rating for the first time since October 2017 (from BBB to BBB+), while maintaining a stable outlook. Shortly afterwards (in May 2025), Moody's left the rating unchanged (at Baa3) but revised Italy's outlook rating from stable to positive.

## POPULATION DECLINE THREATENS LONG-TERM GROWTH POTENTIAL

Over the next few years, public spending will come under increasing pressure, mainly due to population ageing, the green and digital transitions, and the need to increase spending to strengthen defence capabilities. Medium- and long-term debt sustainability will depend mainly on the implementation of structural reforms<sup>2</sup> and the efficient use of available resources. Economic growth and fiscal sustainability are mutually reinforcing: confidence in public finances promotes investment, while stronger growth facilitates fiscal consolidation.

Population ageing and low birth rates are expected to have a profound impact on the growth potential of the Italian economy. According to Istat, the working-age population will decline by around 5 million people by 2040. Furthermore, 700,000 Italians have emigrated in the last ten years, a fifth of whom are young graduates. Legal immigration could help, but among the major EU countries, Italy has the lowest proportion of immigrants with university degrees.

## EXPORTS SUSTAINED BY INTRA-EU TRADE AND TRADE WITH THE US

In the first six months of 2025, Italy's trade balance was largely positive, amounting to EUR 22.82 billion. Exports increased (+2.1% y/y), mainly driven by intra-EU trade, particularly with Spain (+11.8% between January and June; 5.5% of total Italian exports) and Germany (+2.6%; 11.4% of Italian exports and Italy's main destination market). Outside the EU, exports declined almost everywhere, with the exception of the United States, where they increased by 7.8% in the first half of the year (mainly due to a +10.4% y/y increase in June). This increase was driven by the pharmaceutical sector (+77% y/y in June and +77.9% in the first half of 2025) and the chemicals sector (+10.9% y/y in June).

The dynamics of Italian exports to the United States are very different from those observed in the rest of the EU: according to Eurostat, EU-27 exports to the United States fell by 10.3% y/y in June. It is likely, therefore, that Italy has continued to benefit from stockpiling by its US counterparts, who have attempted to anticipate the impact of the

<sup>2</sup> The IMF recently pointed out how Italy should focus on boosting productivity and innovation and improving labour participation, while advancing the transition to renewable energy and a resilient energy infrastructure.

<sup>3</sup> Istat, Rapporto sulla competitività dei settori produttivi - Edizione 2025, March 2025.

ITALY: EMPLOYMENT BY AGE GROUP (THOUSANDS, JULY 2025, S.A)

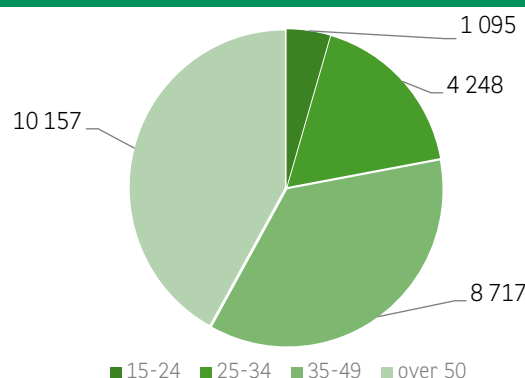


CHART 2

SOURCE: ISTAT, BNP PARIBAS

ITALY: INFLATION IN ITALY AND THE EURO AREA (HPCI, % CH A/A)

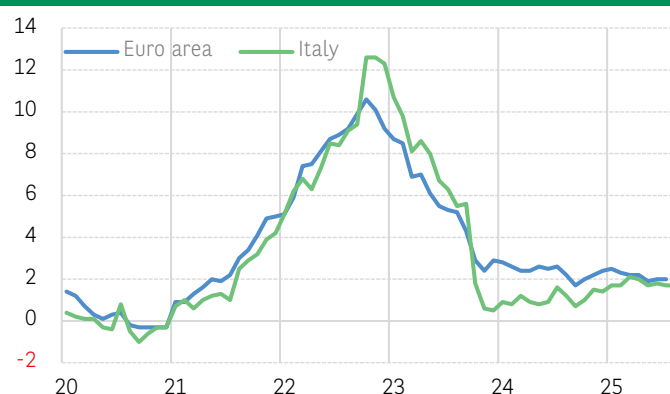


CHART 3

SOURCE: EUROSTAT, BNP PARIBAS

tariffs. This phenomenon should therefore come to an end with the implementation of the new measures, which came into force in August. In recent months, a survey conducted by Istat<sup>3</sup> has shown that just over 23,000 companies (0.5% of the total) are vulnerable to exports (due to excessive concentration of products and geographical areas). Of these vulnerable companies, 3,300 have the United States as their main destination market, while around 2,800 have Germany as their main market.

All in all, although the ongoing trade tensions are expected to ease gradually in the second half of 2025, they might have a negative impact on the economic cycle in Italy, with more pronounced effects on investments and foreign trade and, to a lesser extent, on household consumption, by negatively affecting their confidence.

Article completed on 3<sup>rd</sup> September 2025

**Simona Costagli, Paola Verduci**

[simona.costagli@bnpparibas.com](mailto:simona.costagli@bnpparibas.com)

[paola.verduci@bnpparibas.com](mailto:paola.verduci@bnpparibas.com)



**BNP PARIBAS**

The bank  
for a changing  
world

## SPAIN

20

## JOB CREATION CONTINUES TO UNDERPIN GROWTH

After a strong first half of the year, Spanish growth should remain higher than that of its European neighbours in 2025 and 2026. Domestic demand is likely to remain the main driver, primarily supported by job creation, while the contribution of foreign trade is expected to become slightly negative. The budget deficit and the debt-to-GDP ratio should continue to benefit from significant nominal growth, which is nevertheless expected to slow gradually. Weak productivity could, however, hold back potential growth in the longer term, particularly as the available labour force begins to shrink.

### ECONOMIC ACTIVITY: DOMESTIC DEMAND, THE MAIN DRIVER OF GROWTH

Spanish growth averaged +0.7% q/q in H1 2025, driven mainly by private consumption and a rebound in investment in machinery and equipment. It should remain robust in the second half of the year (+0.6% on average), bringing the annual average to +2.7% in 2025.

Next year, economic activity is expected to slow slightly, with GDP growth at +2.3%. The contribution of foreign trade is likely to become negative. On the one hand, geopolitical and trade uncertainty, caused by the rise in US tariffs and its impact on Spain's main European trading partners, should push exports down (more details below). On the other hand, imports will be further stimulated by strong growth in domestic demand.

Household consumption should remain the main driver of growth. Retail sales volumes continue to rise steadily (+1.9% q/q in Q2), household confidence is high by historical standards (47.8 versus 42.3 on average over 2015-2019 according to the Ipsos survey), and the savings rate is gradually declining (12.8% of disposable income in Q1 2025, versus 14% in Q1 2024). Investment, meanwhile, should continue to rebound. Although the recovery has been particularly slow since Covid, investment in machinery and equipment has recently shown signs of recovery. Since Q4 2024, it has returned to its pre-Covid level, supported by aid for flood victims in the Valencia region and by investment associated with the disbursement of funds from the recovery and resilience plan.

In addition, like other eurozone countries, Spain should benefit from the positive effects of the roll-out of the German infrastructure plan (leading to an increase in German demand) and the rise in defence spending over the next two years (generating more industrial opportunities at European level).

### LABOUR MARKET: FURTHER STRENGTHENING

In terms of production factors, Spanish growth is driven by the availability of abundant, skilled and inexpensive labour. The strong contribution to growth from household consumption stems from the income generated by this large workforce, which is then spent. This performance of the labour market is reflected in the latest figures: the unemployment rate has fallen to its lowest level since May 2008 (10.4% in July) and employment, measured by the number of people registered with the social security system, has reached a historic high (21.6 million in July). Slight tensions persist, however. According to the Bank of Spain, the proportion of companies reporting labour availability problems decreased in Q2 compared with Q1 (-3pp) but remains at a high level (42.9% compared with an average of 30.2% in the same quarter over the last four years). These issues are particularly marked in agriculture, hospitality and construction. Nevertheless, it is in tourism-related sectors that employment continues to grow the most (services up 2.4% y/y in July).

#### GROWTH AND INFLATION (YEARLY AVERAGE)

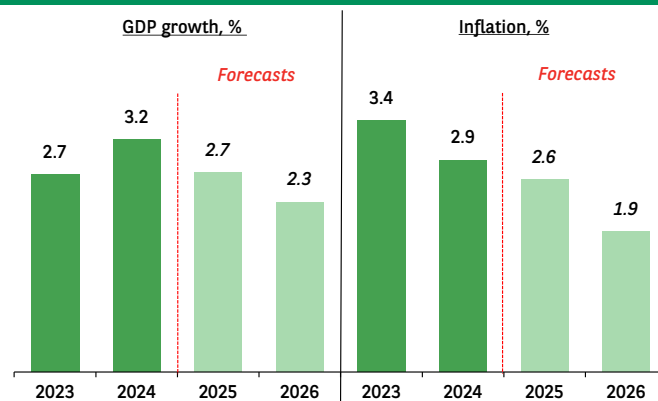


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

### INFLATION: TOWARDS A REDUCTION IN THE MEDIUM TERM

Strong tourist demand is having a positive impact on activity, but also on prices. The rise in services inflation (+3.6% y/y in July, +0.2pp m/m) reflects in particular the passing on of costs by businesses to their customers, as confirmed by the PMI services survey. This phenomenon, driven by the continued growth in nominal wages (+3.5% y/y in July), remains the main contributor to headline inflation (+2.7% y/y; +0.4pp m/m and -0.3pp compared with July 2024). Despite nominal wage growth now outstripping inflation, real wages remain around eight percentage points below their pre-inflationary crisis level.

Two forces will be at play over the coming quarters. On the one hand, energy prices should continue to fall, which will act as a brake on price rises. On the other hand, continued strong wage growth and the housing shortage will exacerbate inflationary pressures. The housing shortage is due to demand still far outstripping supply. Demand is benefiting from the improvement in financial conditions, and a construction deficit explains the low level of supply. To ease these pressures, the government has introduced measures to regulate tourist rentals. It has also rolled out a national housing plan, including increased public investment to speed up construction. However, these tensions are likely to persist, pushing up property prices and rents over the next two quarters. We therefore anticipate inflation to remain relatively high in 2025 (+2.6%), before easing to +1.9% in 2026.



BNP PARIBAS

The bank  
for a changing  
world

## PUBLIC FINANCES: FAVOURABLE TRENDS IN BUDGET RATIOS

Despite the absence of a budget for 2025, measures approved in November 2024 have increased public revenue. These include the introduction of a minimum 15% corporate income tax for multinationals, an increase in the top bracket on personal capital income, and an increase in taxes on tobacco and electronic cigarettes. These measures, combined with higher social security contributions (driven by growth in the number of workers) and the removal of VAT reductions introduced during the inflationary period, should give the government significant leeway to increase its spending, particularly on defence (from 1.3% of GDP in 2024 to 2.1% from this year<sup>1</sup>). However, this should not prevent the public debt ratio from falling, as it has done in recent years (from 109.5% in 2022 to 101.8% in 2024). Spanish nominal growth is expected to remain high (5.1% in 2025 and 4.4% in 2026) and above the apparent interest rate on the debt (2.6% of GDP and then 2.7%), which would allow for a reduction in the public debt-to-GDP ratio (see chart 2).

## FOREIGN TRADE: BETWEEN TRADE SLOWDOWN AND RENEWED ATTRACTIVENESS OF FDI FLOWS

The surplus on the balance of goods and services is set to decline over the next two years. On the one hand, the services surplus is likely to shrink, due to the marked slowdown in tourism revenue growth<sup>2</sup> (the main source of the services surplus). On the other hand, the goods deficit is set to widen, with goods exports having already begun to slow in Q2 (EUR 101.3 bn; -0.4% y/y) due to the direct and indirect impacts of higher US tariffs. Exports of goods to the United States fell sharply (-11.7% y/y), as did those to the EU (Spain's main trading partner), which fell by 1.2%. These declines were offset by a rise in exports outside the EU (+1.5%), notably to China (+4.6%).

Although foreign direct investment (FDI) flows to Spain have slowed, as in most developed economies in 2024 (-35% y/y), they remain significant for the country (EUR 31 bn). Spain remains second in Europe in terms of attracting the most investment, after France<sup>3</sup>. This inflow of FDI supports the development of Spain's productive potential and improves the country's export capacity.

## LACK OF PRODUCTIVITY REMAINS THE MAIN STRUCTURAL PROBLEM

The persistent gap in the GDP per capita ratio between Spain and the other three major countries in the Eurozone (Germany, France and Italy) is mainly due to its low productivity<sup>4</sup>. The Spanish economy is based on sectors with lower productivity (such as tourism services). This handicap can also be explained by the small size of its companies, their difficulty in expanding, and their low level of investment in research and development. In Spain, gross domestic expenditure on R&D reached 1.5% of GDP in 2023, compared with 2.2% in France. Despite GDP growth above the eurozone average, this lack of productivity could become more damaging in the medium to long term. In addition, the potential slowdown in net immigration and the burden of population ageing will weigh on human capital, the main strength of the Spanish economy.

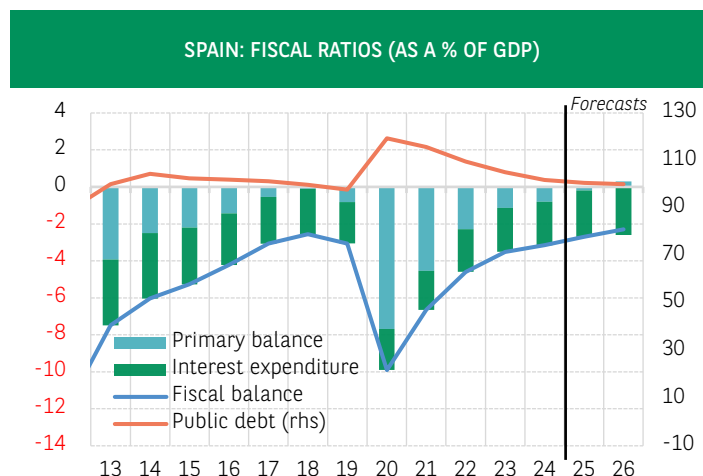


CHART 2

SOURCE: DG ECFIN AMECO, EUROSTAT, BNP PARIBAS FORECASTS

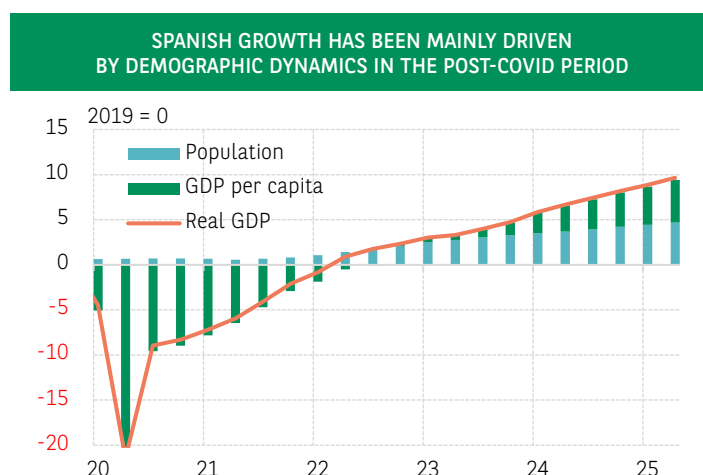


CHART 3

SOURCE: EUROSTAT, BNP PARIBAS

According to the OECD<sup>5</sup>, if productivity levels remain unchanged, Spain's real GDP per capita will grow by just 1.0% per year between now and 2040 due to population ageing (compared with an average of 1.5% between 2000 and 2024<sup>6</sup>).

Article completed on 29 August 2025

**Lucie Barette**

[lucie.barette@bnpparibas.com](mailto:lucie.barette@bnpparibas.com)

<sup>1</sup> However, Prime Minister Pedro Sanchez has announced his refusal to comply with the 5% military spending threshold required by NATO in the long term.

<sup>2</sup> Tourist arrivals rose by 1.4% y/y in June 2025, compared with +13.2% a year earlier.

<sup>3</sup> World Investment Report 2025 «World Investment Report 2025: International investment in the digital economy», UNCTAD.

<sup>4</sup> June 2025 Note «Spain's Productivity Gap Vis-à-vis Europe and the United States: Diagnosis and Remedies», IMF.

<sup>5</sup> July 2025 Note, «OECD Employment Outlook 2025: Spain», OECD.

<sup>6</sup> Excluding 2020, due to the Covid period.



**BNP PARIBAS**

The bank  
for a changing  
world

# BELGIUM

22

## SMOOTH SAILING FOR NOW, BUT WHERE TO NEXT?

Belgian growth fluctuated in the first half of this year, with a strong Q1 followed by a slowdown in Q2. Nevertheless, our nowcast for Q3 points to growth of 0.3% q/q, with renewed confidence among households and businesses. Export growth was subdued, hit by tariffs and the related uncertainty. However, the wage catch-up in neighbouring countries should improve Belgian's competitiveness (wages are now rising faster than inflation in comparable European countries). House prices continue to rise, but the low number of new homes makes them less affordable. The public debt ratio is increasing by 2 percentage points per year and increased commitments to NATO are widening the deficit. The government has no choice but to take difficult decisions to reduce it.

### RESILIENT GROWTH

Growth slowed to 0.2% q/q just before the summer, after a strong showing in Q1 (0.4%). For Q3, our nowcast of 0.3% q/q suggests resilience. Household confidence is at its highest level in a year, coinciding with an increase in consumer spending and a gradual recovery in the property market. Business confidence has continued to improve across all sectors since April, with only the services sector still lagging somewhat. Based on our monthly analysis of anonymised financial transactions from a subset of Belgian companies, we are seeing a sharp increase in activity levels.

In the longer term, we see favourable prospects abroad thanks to Germany's budgetary spending, which could be offset by stronger fiscal consolidation at national level. As a result, we forecast annual growth of 1.1% for both 2025 and 2026.

Internal geographical disparities are expected to widen, with the north (Flanders) outperforming the Brussels-Capital Region and southern Wallonia. A key driver is the large share of market services in the Flemish economy. In addition, a recent simulation by the Belgian Federal Planning Bureau points out that the number of workers from Brussels and Wallonia commuting to Flanders will increase, further cementing the latter's economic dominance.

### LABOUR MARKET: SOFT LANDING, EPISODE 241

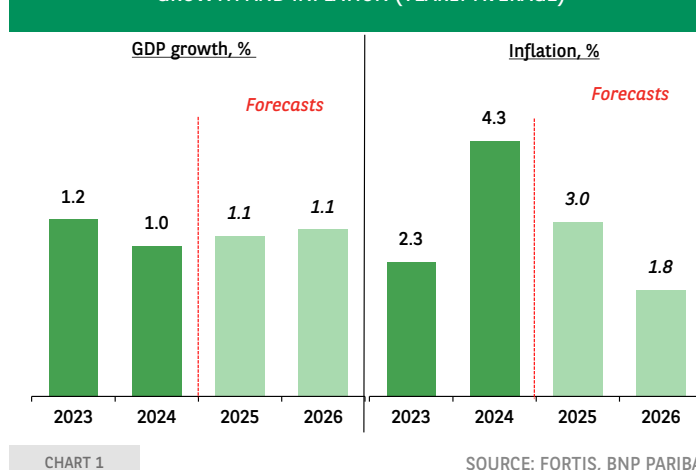
The unemployment rate has been hovering slightly above 6% since the start of the year, after reaching its lowest level during the pandemic at 5%. Leading indicators have been pointing towards a slowdown for a while now. The private sector job vacancy rate, which peaked at 6% in 2022, has now fallen back to 4.8%, although this is still high. Fear of unemployment, a sub-indicator of household sentiment, has been rising since 2024.

Recently however, this fear has subsided. In fact, total employment growth has been speeding up somewhat since the start of the year. While job creation has recently been dominated by non-market services, and fiscal consolidation efforts are expected to put an end to this trend, the significant uptick in self-employment, with a growth rate almost double its pre-pandemic average, is a welcome boost. We expect the unemployment rate to rise slightly further but then stabilise before reaching 7%. Meanwhile, policy support for the labour market could help speed up total job creation, but not as much as the current federal government hopes (see below).

### INFLATION: NORMALISATION OF CORE INFLATION

After experiencing the highest inflation in the EU (together with Romania) for most of 2024, growth in the Belgian harmonised index slowed from 4.4% y/y in January to 2.6% in August. Over the same period, core

#### GROWTH AND INFLATION (YEARLY AVERAGE)



inflation also stabilised at 2.2%, in line with a slowdown in wage growth (indexed to inflation). The latter is expected to remain at this level, as the maximum margin for growth in collectively negotiated real wages for the period 2025-2026 was recently set at zero, according to the National Bank of Belgium.

Furthermore, new measures announced by the federal government, such as a cap on social security contributions, are expected to reduce employer contributions and, in turn, labour costs. Energy inflation is expected to fall initially due to improved supply conditions and the weak US dollar, before rising again in 2027 with the introduction of the EU ETS2 system.

### FISCAL POLICY: EVERYONE HAS A PLAN...

The budget deficit stood at 4.5% of GDP in 2024. After lengthy negotiations to form a government, Prime Minister Bart De Wever reaffirmed his party's goal of reducing the deficit. However, reality quickly undermined these ambitions, as increased NATO spending commitments and higher interest expenditure – which is expected to rise by 0.3pp of GDP every year for the foreseeable future – make this goal more difficult to achieve. Furthermore, the government's strategy was based in part on higher employment in order to bolster revenues and reduce social spending. But the goal of creating more than 500,000 jobs in four years is difficult to achieve under current conditions. Consequently, the deficit is expected to increase further, with public debt rising by more than 2pp of GDP per year over the forecast period.


**BNP PARIBAS**

The bank  
for a changing  
world

The government has taken measures that should help to achieve fiscal consolidation in the longer term, including reducing civil servants' pensions, which will help to limit the increase in age-related expenditure.

## HOUSE PRICES ARE UP, IF YOU CAN AFFORD IT

The issue of housing affordability is becoming increasingly pressing, with the Belgian property market falling victim to its own success. Since mid-2022, property prices have risen faster than those in France and Germany, reaching the same level as those in the Netherlands. This has fuelled the expectation of further price increases, supported by strong fundamentals.

However, price is only one part of the story. The transaction volumes on the secondary market fell by 15% in the quarters following the first rate hikes. Although the situation appears to have improved recently, the number of new builds continues to decline. New builds are an important means of increasing the housing stock. Yet the number of new build permits continues to fall and is now 35% below its 2022 level. A New-builds are only affordable for a minority of households.

As we expect property prices to continue to rise by 2% per annum over the next few years, new initiatives to promote home ownership are urgently needed.

## NET EXPORTS WEIGHING ON THE ECONOMY

Belgium's trade surplus improved in the first half of 2025, compared with the first half of 2024. This result is largely due to anticipated exports to the US in the first months of this year. However, taking a step back, it is clear that net exports have been a drag on growth and that this situation is unlikely to change any time soon.

Looking ahead, the decline in trade flows linked to COVID-19 and the loss of competitiveness during the 2022-2023 wage indexation cycle will continue to weigh on exporters. That said, Belgium's wage disadvantage should ease as neighbouring countries catch up, creating opportunities to regain lost export market share. France, Germany and the Netherlands remain the most important trade partners, so an uptick in economic growth due to fiscal spending (Germany, most notably) could also help reverse the situation.

*Article completed on 5 September 2025*

**Arne Maes**

[arne.maes@bnpparibas.com](mailto:arne.maes@bnpparibas.com)

### BELGIUM: LABOUR MARKET: UNEMPLOYMENT RATE AND SENTIMENT



CHART 2

SOURCE: NATIONAL BANK OF BELGIUM

### BELGIUM: REAL ESTATE MARKET CONDITIONS

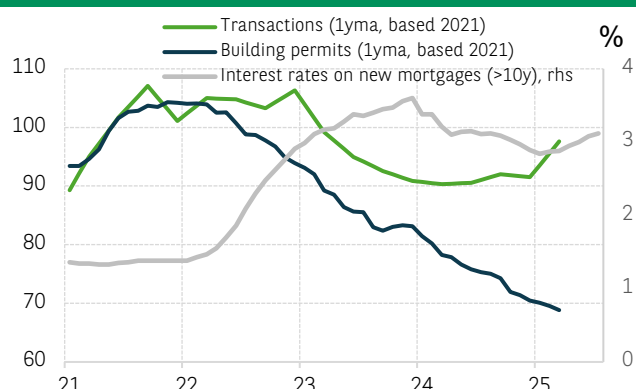


CHART 3

SOURCES : NATIONAL BANK OF BELGIUM, STATISTICS BELGIUM



**BNP PARIBAS**

The bank  
for a changing  
world



# UNITED KINGDOM

24

## A FRAGILE REBOUND

After solid growth in H1 2025, the second half of the year is expected to see a slowdown (under the weight of US trade policy and UK fiscal policy). Despite the downside risks on the labour market and industry difficulties, growth is expected to be at a higher and stable rate in 2026 (+0.3% q/q on average) thanks to monetary easing. However, the policy mix will remain moderately restrictive, constrained by high inflation and gilt market pressures. Striking a balance between fiscal consolidation and growth remains a challenge in the UK.

### ↑ A MORE CHALLENGING H2 2025, BUT A STRONGER RECOVERY IN 2026

After a good first half of the year (+0.7% q/q in Q1 and +0.3% q/q in Q2), growth is expected to be more moderate in H2 (+0.1% q/q in Q3 and 0.3% in Q4), before stabilising close to its potential rate in 2026 (+0.3% q/q per quarter). On annual average, however, growth is expected to slow between 2025 (1.3%) and 2026 (1%), with 2025 benefitting from a more favourable carryover effect. On the positive side, household consumption has been rising for the past four quarters, helped by increasing real wages, even if this growth in real wages is slowing (+1.2% y/y in June). However, the likely rise in unemployment could adversely affect consumer choices. A fall in the savings rate, currently high compared with its historical average (10.9% of disposable income in Q1 25), would help to cushion part of the shock. However, there is no guarantee that this will materialise, as the continuing high level of uncertainty is likely to keep precautionary saving high.

Overall, the strength of activity in the services sector (PMI index of 54.2 in August) should act as a buffer for an economy that is exposed to a number of vulnerabilities. Industrial activity is still depressed (PMI index down to 47.0 in August). The slowdown in growth in the United States, the UK's biggest export market after the eurozone, will have an immediate impact, while the positive effects of strengthening activity in the eurozone should materialise later (especially in early 2026). Therefore, the outlook for 2026 is still ambivalent, as there is a risk that fiscal consolidation will weigh more heavily on growth or that, in order to support growth, this consolidation will be delayed, which would add to the pressure on long-term interest rates (and would also affect growth).

### 📊 RELATIVE INCREASE IN UNEMPLOYMENT

The unemployment rate continued to rise in the first half of 2025, reaching 4.7% in June (+0.6 points higher than the low point in July 2024), while the volume of job vacancies fell back to its lowest level since 2017. The rise in labour costs, exacerbated by the April Budget measures, is weighing on British businesses. Up until now, they have been squeezing their margins, but this approach is reaching its limits, with margins falling to 43.2% in Q2 2025, their lowest level in 15 years. Employment could now become the main lever for adjustment. Some surveys point in this direction (see chart 2). A sharper slowdown in the labour market would dampen wage growth. The latter has already slowed (+4.5% y/y in June, the slowest pace since the end of 2021), but it remains above inflation, which is supporting purchasing power.

### 📈 INFLATION: A MODERATE REBOUND IN 2025 AND A LIMITED SLOWDOWN IN 2026

After rising again to 4.2% y/y in July, inflation is expected to remain at a high level until May 2026. Inflation in services should remain close to

#### GROWTH AND INFLATION (YEARLY AVERAGE)

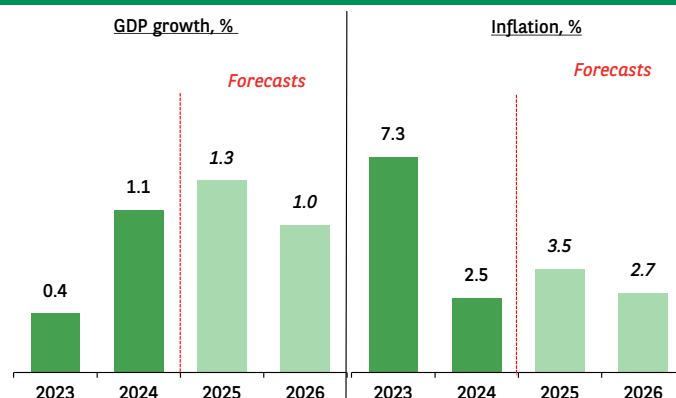


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

5% until that date, when the base effect linked to the introduction of the April 2025 tax hikes fades. The trajectory will then depend on developments in the labour market, where the anticipated deceleration should lead to a slowdown in wages and prices in services. While a return to the 2% inflation target will not occur, in our view, in 2026, inflationary pressures should be gradually less widespread. Following a 6.4% increase in Q2, the rise in the energy price cap for unregulated tariffs will slow in Q4 (+2%, according to Ofgem), which will limit energy inflation thereafter. Another positive development is that the rise in rents has slowed since the start of 2025, from a peak of 7.8% y/y in January to 4.5% in July, and could fall back below the services component (excluding rents) this autumn for the first time since the summer of 2023.

### 🏠 TWO FURTHER RATE CUTS AND LESS PRONOUNCED QUANTITATIVE TIGHTENING

After a 125-bp cut in the policy rate in one year, two further rate cuts (each of 25 bps) are expected in Q4 2025 and Q1 2026, according to our forecasts. The landing point for rates (3.5%) will be higher than in the eurozone (2% for the deposit facility rate), reflecting higher and persistent inflation. Furthermore, against a backdrop of pressure on sovereign long rates and an expected rise in UK government bond issuance in 2026, the BoE is likely to opt for more fine-tuned and regular management of its quantitative tightening (QT), both in terms of the size and structure of the central bank's balance sheet. The decision to slow the pace of reducing the BoE's balance sheet (from £100 bn (October 2024–September 2025) to £70 bn (October 2025–September 2026), at the 18 September meeting, is a first step in easing the quantitative tightening programme,


**BNP PARIBAS**

The bank  
for a changing  
world

which could continue to evolve in 2026, depending on how gilt market pressures develop. Nevertheless, the reduction in QT implies heavier losses on the BoE's gilt portfolio, losses which must be compensated by the Treasury, thereby increasing the Treasury's financing requirements.

## THE DEFICIT TARGET WILL BE DIFFICULT TO ACHIEVE

Bond-market pressures (which have caused 30-year yields to rise by around 30 bps since the start of the year) and the downturn in the labour market are complicating fiscal consolidation. On the one hand, despite sustained inflation and the April Budget measures, which increased some revenues (stamp duty and employer contributions), VAT receipts are growing at a limited rate (+3.9% year-on-year in July), which is also limiting the rise in current receipts (+5.3%). On the other hand, public sector wage increases and higher debt servicing costs are pushing up current expenditure (+7.3% year-on-year). As in 2024, the deficit target for the 2025 financial year (which runs from April to March) of 3.9% of GDP targeted by the OBR (March forecasts) will be difficult to achieve. Therefore, an upward revision of the deficit is likely this autumn (the autumn Budget will be announced on 26 November), which will further force the government to step up its fiscal consolidation measures. Nevertheless, according to our estimates, the gap between the primary balance and the balance needed to stabilise the public debt ratio is smaller than in France; the rise in the debt ratio should therefore be more moderate in the UK. Debt servicing, which stood at 2.9% of GDP in 2024, is expected to increase, but only moderately (to around 3.2% of GDP at the end of 2026). The high average residual maturity of government securities (14 years) means that refinancing phases can be spread out over time.

## EXTERNAL ACCOUNTS: FALLING EXPORTS TO ASIA

There is a high risk that the trade deficit (GBP 243 b in July, cumulative year-on-year) will continue to deteriorate in 2026. While the UK has managed to limit the tariff shock with the United States, notably by negotiating an export quota for the automotive industry, the fall in exports from the sector, one of the largest export items (over 10% of the total), is structural and stems mainly from a drop in demand from the Asian market. The decline in hydrocarbon exports, which is due to energy transition efforts, and which once accounted for 13% of the UK's exports of goods (2012), now only account for half of exports. This is also contributing to the higher trade deficit. The UK's share of global exports, which fell below 2% in 2024, continues to decline in 2025 (1.9% in May on a 12-month moving average basis, which is lower than in France (2.5%), Italy (2.7%) and *a fortiori* Germany (6.8%)). Nevertheless, the surplus in services continues to grow, offsetting a large part of the goods deficit, a trend that should continue in 2026 (see chart 3).

While Brexit will leave a lasting mark on trade between the EU and the UK, exports of goods to the EU (in volume terms) rose by 11% over the first seven months of the year, however. As a result, the share of UK exports to the EU-27 rose back above the 50% mark this summer. While it is too early to start talking about a recalibration in trade, the UK will need to strengthen its trade links with its European neighbours. This would enable the UK to take advantage of the expected rise in investment in Europe, while increasing its resilience to future shocks to global trade.

### UNITED KINGDOM: REC/KPMG SURVEY AND UNEMPLOYMENT RATE

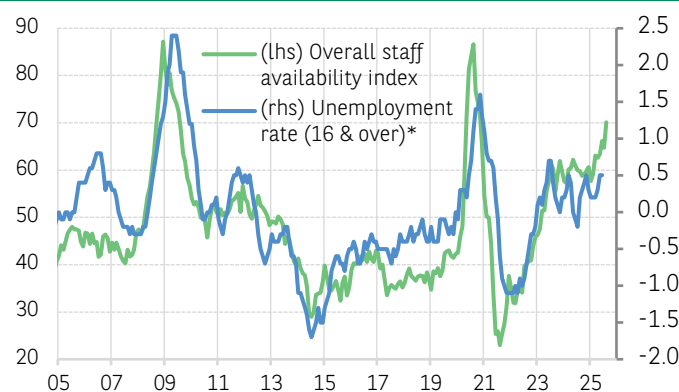


CHART 2

\* ANNUAL CHANGE, IN P.P.  
SOURCE: REC/KPMG, ONS, BNP PARIBAS

### UNITED KINGDOM: GOODS AND SERVICES BALANCES (£ BN, 12-MONTH MOVING TOTAL)

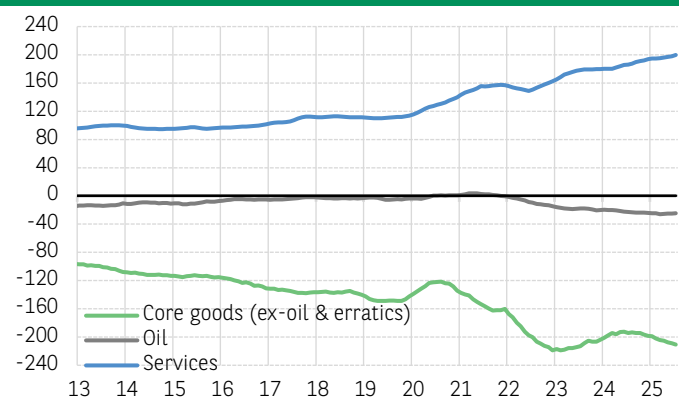


CHART 3

SOURCE: ONS, BNP PARIBAS

UK's participation in the SAFE European rearmament programme (which has not yet been formalised, but is in the final stages of negotiation), which should actually come into effect in 2026, would bring the two zones even closer together.

Article completed on 18 September 2025

**Guillaume Derrien**

[guillaume.a.derrien@bnpparibas.com](mailto:guillaume.a.derrien@bnpparibas.com)



**BNP PARIBAS**

The bank  
for a changing  
world

## JAPAN

26

## STUCK IN THE MIDDLE OF INFLATION AND TARIFFS

The Japanese economy has been showing some momentum for just over a year. However, this performance is likely to fade in the second half of the year, not least as a result of the tightening of US trade policy. The labour market remains tight, and inflation continues to exceed the 2% target. Caught between an economic situation that may signal a weakening and a sharp rise in long-term interest rates amid fiscal concerns, the Bank of Japan (BoJ) is exercising extreme caution by raising its policy rate very gradually.

## GROWTH: SURPRISING MOMENTUM THAT COULD FADE

The Japanese economy has just completed a run of five consecutive quarters of positive growth (including +0.6% q/q in Q4 2024, +0.1% and +0.5% in Q1 and Q2 2025), which has not been seen since 2017. The strong performance in Q2 2025, driven by household consumption (+0.4% q/q), was surprising in view of high inflation. Business investment contributed 40% to GDP growth in H1, compared with a negative contribution from foreign trade, with imports rebounding (+5.3% y/y over the half-year).

However, the Japanese economy's performance could subsequently falter, hampered by higher US tariffs and, crucially, by a domestic environment that could become stagflationary. Indeed, the Japanese economy seems to be operating at full capacity: according to the Cabinet Office, the output gap narrowed at the end of 2024 before turning slightly positive in 2025 (+0.1pp in Q2), against a backdrop of a tight labour market and expansionary fiscal policy. The turbulent political environment could also weigh on the economy (see below). However, the strength of the PMI indices (the composite index reached 52.0 in August, after four consecutive months of improvement) suggests that the slowdown may still be some way off and that growth could once again surprise on the upside in Q3 (compared with our forecast of 0% q/q).

## A ONE-SIDED TRADE AGREEMENT WITH THE UNITED STATES

US policy poses a downside risk to Japanese growth. The US represents the largest export market for an economy whose goods exports accounted for more than 15% of GDP in 2024. In the first half of the year, the trade balance narrowed due to a rise in imports in Q1. On 22 July 2025, the United States and Japan reached a bilateral trade agreement, which was formalised on 4 September. Additional tariffs on Japanese products entering the United States are set at 15%, compared with a 'reciprocal' tariff of 25% announced on Liberation Day and another of 10% applied since 9 April. Importantly, this tariff will also apply to the automotive sector (as in the agreement with the EU), which accounts for nearly one-third of Japanese exports to the United States and for which the standard sectoral tariff is 25%. At the same time, Japan has committed to investing USD 550 billion in the US economy by 2029, as well as increasing the openness of its domestic market to US players, particularly those in the rice sector.

Overall, according to our estimates, the average tariff applied to Japanese exports is set to reduce to 11.5% (compared with 15% between April and the agreement of 22 July). Although this tariff remains well above the average level observed in 2024 (1.5%) and the agreement is lopsided, its conclusion reduces uncertainty. However, the full effect is yet to be felt. The context is also inflationary, with production costs leaving Japanese companies little scope to reduce their export prices. The export price index has been falling year-on-year since April 2025. This movement is much more pronounced in yen (JPY) than in foreign exchange contracts.

GROWTH AND INFLATION (YEARLY AVERAGE)

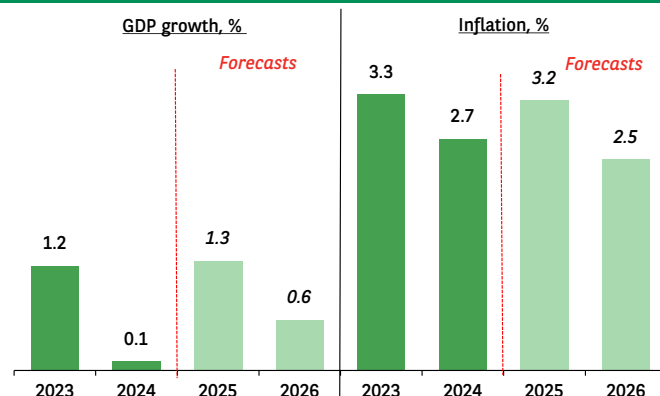


CHART 1

SOURCE: BNP PARIBAS GLOBAL MARKETS

## INFLATION PERSISTENTLY ABOVE TARGET

Inflation is expected to remain above the 2% target until the end of 2026, even if it has slowed down after reaching a 34-year high in Q1 2025 (+3.8% y/y). It remains driven upwards by the food component (+7.2% y/y on average since the start of the year, accounting for 58% of the year-on-year change in the CPI in 2025 to date). This is attributable to the major issue of rice prices (+90.7% y/y), which is set to continue according to the Bank of Japan (BoJ). Core inflation is also well above target (+3.2% y/y on average since the start of the year), with services inflation being more moderate (+1.5% y/y in June, +2.1% y/y excluding imputed rents, up very slightly since the start of the year). As for market inflation expectations, as measured by the 10-year breakeven inflation rate, they regained momentum from May 2025 onwards, after losing 30 basis points in April following Liberation Day in the United States. In August 2025, they stood at +1.5% (the historical record is 1.6%). This anticipated inflation closer to the target is a favourable sign, especially as the BoJ seeks to ensure that the country does not return to the deflationary spiral of the past once the temporary factors driving inflation have dissipated.

## DESPITE A STRONG LABOUR MARKET, REAL WAGES ARE FALLING

The rise in contractual scheduled earnings, an underlying measure of wage growth, reached 2.5% y/y in July 2025, the highest since December 2024. More broadly, nominal income growth has been gradually picking up momentum over the course of the year, after dipping slightly at the end of Q1 2025. This strength is expected to continue, driven by a tight labour market, as illustrated by an unemployment rate (+2.3%) at its



BNP PARIBAS

The bank  
for a changing  
world

lowest since the end of 2019. In addition, the final results of the Shunto (+5.25%, Chart 2), the annual wage negotiations conducted by the Rengo trade union confederation, mark an improvement on 2024 (+5.1%) and a record high since 1991. However, persistent inflation is taking its toll on real wages. These have only been positive once in 2025 (+0.5% y/y in July), which is likely to weigh on Japanese household consumption.

## THE BOJ IS EXPECTED TO RESUME MONETARY TIGHTENING AFTER A LONG PAUSE

The Bank of Japan has put rate hikes on hold for the time being. The uncollateralised overnight call rate (key interest rate) has been kept stable at +0.5% since the January 2025 hike (+25 bps). The gradual and cautious nature of monetary normalisation, linked to fragile domestic demand, has been amplified by uncertainty surrounding trade policy, the pause is continuing despite inflation remaining above target.

With trade uncertainties having eased, a rate hike is expected in December (+25 bps) in view of the inflation outlook and the central bank's communication. We then expect three further hikes (+25 bps) in 2026, one per quarter between Q2 and Q4. The BoJ's key rate would then reach 1.5%, which would correspond to a moderately accommodative monetary policy with inflation still above its target. These developments would result in an appreciation of the JPY against the USD (to 145 at the end of 2025 and 141 at the end of 2026), adding further pressure on Japanese companies.

## TOWARDS HIGHER DEFICITS

Japan is seeking a new Prime Minister less than a year after the appointment of S. Ishiba (1 October 2024), whose resignation was announced on 7 September 2025. This departure follows two major electoral setbacks: the early general elections in October 2024 (loss of absolute majority for the LDP/Komeito coalition in the lower house) and the upper house elections (decline of the LDP) in July 2025. Ishiba's departure adds to the instability, in a context of a minority assembly and the rise of populist parties. Ishiba's successor as LDP president will be appointed during the internal election on 4 October and will, in all likelihood, become Japan's new PM.

Japan's primary deficit is projected to increase slightly to -2.4% of GDP in 2025 (+0.3pp) on the back of expansionary fiscal policy, before stabilising at this level in 2026, according to the IMF. The increase in interest payments will lead to a larger overall deficit (2.9% in 2025 and 3.1% in 2026, compared with 2.5% in 2024). At the same time, public debt is on a downward trajectory (234.9% in 2025 compared with 236.7% in 2024), due to inflation and stronger nominal GDP growth.

Furthermore, the current configuration of the Diet may lead the future PM to lean towards more fiscal stimulus. This, combined with the generally unstable situation, may add to the current pressure on bonds (Chart 3). This pressure partly reflects global fiscal concerns, but also concerns specific to Japan, due to the high level of public debt and expectations of rate hikes by the BoJ.

### JAPAN: RECORD INCREMENTS IN SPRING WAGE NEGOTIATIONS (%)

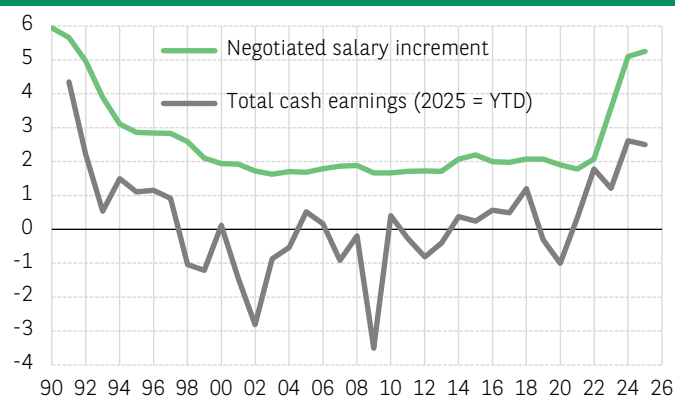


CHART 2

SOURCE: MACROBOND, BNP PARIBAS

### JAPAN: PRESSURE ON JGB'S LONG-TERM YIELDS (%)

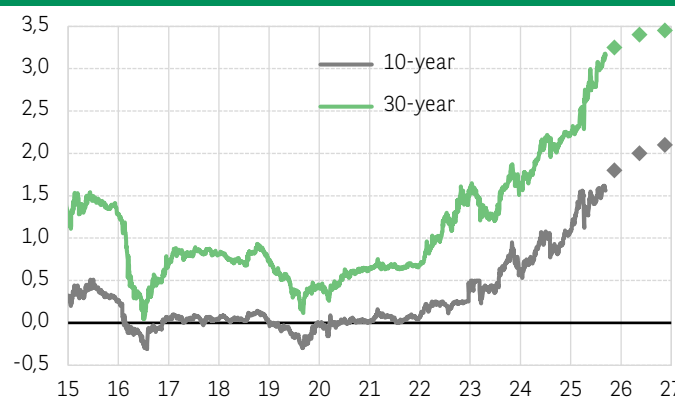


CHART 3

SOURCE: MACROBOND, BNP PARIBAS FORECASTS

Our central scenario anticipates a continued rise in bond yields, particularly long-term yields, with 10-year and 30-year rates reaching 2.0% and 3.4% respectively in mid-2026 (compared with 1.56% and 3.17% at present), before stabilising at this level over the horizon of our projections (Q4 2026).

Article completed on 9 September 2025

**Anis Bensaidani**

[anis.bensaidani@bnpparibas.com](mailto:anis.bensaidani@bnpparibas.com)



**BNP PARIBAS**

The bank  
for a changing  
world

# MAIN INDICATORS

28

GDP, Q4 2019=100

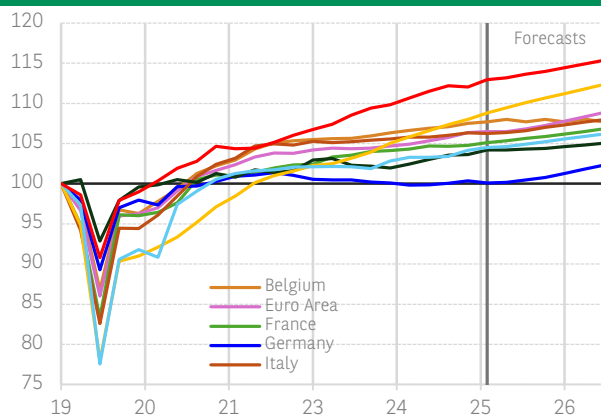


CHART 1

SOURCE: EUROSTAT, BEA, ONS, CAO, BNP PARIBAS FORECASTS

INFLATION RATE, % CH Y/Y

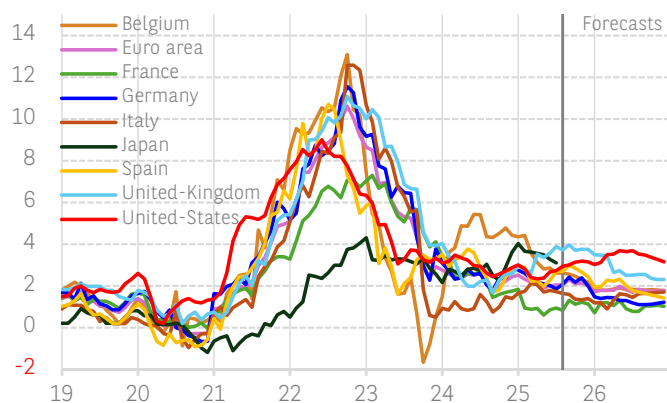


CHART 2

SOURCE: EUROSTAT, ONS, BLS, BNP PARIBAS FORECASTS

UNEMPLOYMENT RATE, %

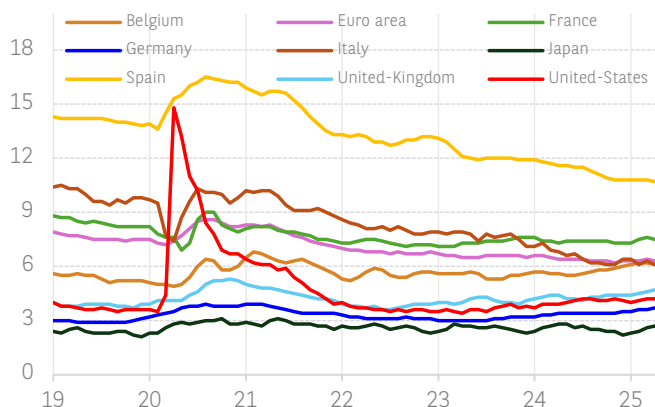


CHART 3

SOURCE: EUROSTAT, BLS, SBJ, BNP PARIBA

CURRENT ACCOUNT BALANCE, AS % OF GDP

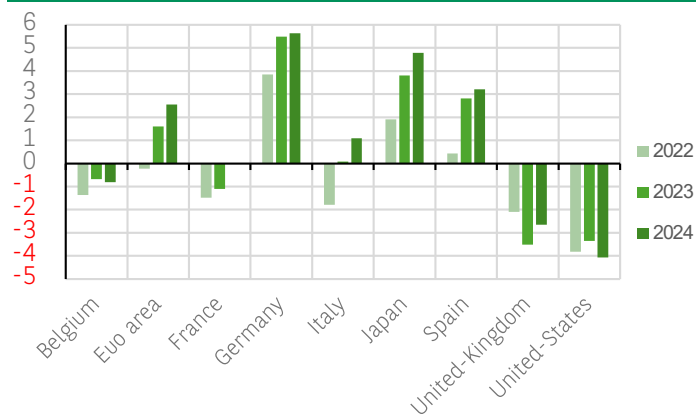


CHART 4

SOURCE: OECD, BNP PARIBAS

GOVERNMENT NET LENDING / BORROWING, % OF GDP

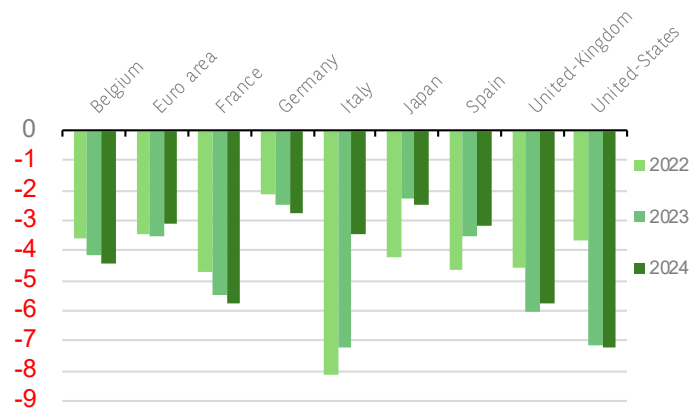


CHART 5

SOURCE: IMF, BNP PARIBAS

GENERAL GOVERNMENT DEBT, AS % OF GDP

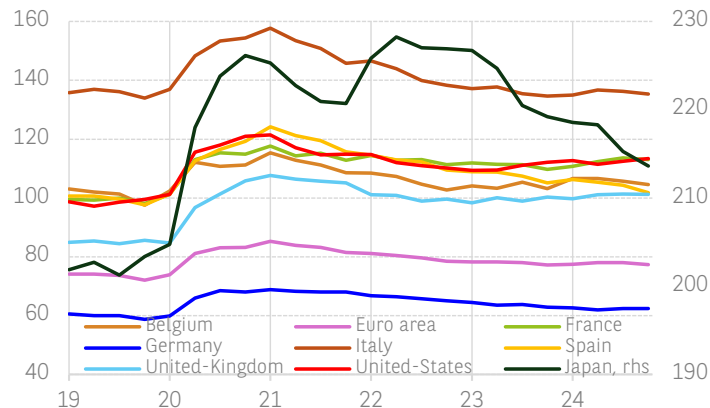


CHART 6

SOURCE: IMF, BNP PARIBAS


**BNP PARIBAS**

The bank  
for a changing  
world



# FORECASTS

29

## ECONOMIC FORECASTS

%	GDP Growth				Inflation			
	2023	2024	2025 e	2026 e	2023	2024	2025 e	2026 e
United States	2.9	2.8	1.7	1.5	4.1	2.9	2.8	3.2
Japan	1.2	0.1	1.3	0.6	3.3	2.7	3.2	2.5
United Kingdom	0.4	1.1	1.3	1.0	7.3	2.5	3.5	2.7
Euro Area	0.5	0.8	1.3	1.4	5.4	2.4	2.1	1.8
Germany	-0.7	-0.5	0.3	1.4	6.0	2.5	2.2	1.3
France	1.6	1.1	0.7	1.1	5.7	2.3	1.0	1.2
Italy	0.8	0.5	0.6	1.1	5.9	1.1	1.7	1.5
Spain	2.7	3.2	2.7	2.3	3.4	2.8	2.6	1.9
China	5.2	5.0	5.0	4.5	0.2	0.2	0.0	1.0
India*	9.2	6.5	6.2	6.4	5.4	4.7	3.2	4.4
Brazil	2.9	3.4	2.3	1.6	4.6	4.4	5.1	4.4

\* Fiscal year from 4 April of year n-1 to March 31st of year n

SOURCE: BNP PARIBAS (E: ESTIMATES &amp; FORECASTS)

## FINANCIAL FORECASTS

### Interest rates, %

End of period	Spot 19/09/2025	Q4 2025	Q2 2026	Q4 2026
US "Fed Funds (upper limit)"	4.25	3.75	3.25	3.25
T-Note 10y	4.11	4.25	4.30	4.40
Eurozone deposit rate	2.00	2.00	2.00	2.25
Bund 10y	2.71	2.90	3.05	3.20
OAT 10y	3.49	3.70	3.80	4.00
BTP 10y	3.56	3.60	3.70	3.85
BONO 10y	3.24	3.43	3.55	3.70
UK Base rate	4.00	3.75	3.50	3.50
Gilts 10y	4.72	4.60	4.50	4.40
Japan BoJ Rate	0.50	0.75	1.00	1.50
JGB 10y	1.63	1.80	2.00	2.10

### Exchange Rates

End of period	Spot 19/09/2025	Q4 2025	Q2 2026	Q4 2026
USD EUR / USD	1.18	1.20	1.21	1.22
USD / JPY	148	145	143	141
GBP / USD	1.35	1.38	1.38	1.39
EUR EUR / GBP	0.87	0.87	0.88	0.88
EUR / JPY	174	174	173	172

SOURCE : BNP PARIBAS GLOBAL MARKETS


**BNP PARIBAS**

The bank  
for a changing  
world

# GROUP ECONOMIC RESEARCH

<b>Isabelle Mateos y Lago</b> Group Chief Economist	+33 1 87 74 01 97	isabelle.mateosylago@bnpparibas.com
<b>Hélène Baudchon</b> Deputy Chief Economist, Head of Global Macroeconomic Research	+33 1 58 16 03 63	helene.baudchon@bnpparibas.com
<b>Stéphane Alby</b> Maghreb, Middle East	+33 1 42 98 02 04	stephane.alby@bnpparibas.com
<b>Lucie Barette</b> Europe, Southern Europe	+33 1 87 74 02 08	lucie.barette@bnpparibas.com
<b>Anis Bensaidani</b> United States, Japan	+33 1 87 74 01 51	anis.bensaidani@bnpparibas.com
<b>Céline Choulet</b> Banking Economics	+33 1 43 16 95 54	celine.choulet@bnpparibas.com
<b>Stéphane Colliac</b> Head of Advanced economies – France	+33 1 42 98 26 77	stephane.colliac@bnpparibas.com
<b>Guillaume Derrien</b> Europe, Eurozone, United Kingdom – World Trade	+33 1 55 77 71 89	guillaume.a.derrien@bnpparibas.com
<b>Pascal Devaux</b> Middle East, Western Balkans – Energy	+33 1 43 16 95 51	pascal.devaux@bnpparibas.com
<b>Hélène Drouot</b> Latin America	+33 1 42 98 33 00	helene.drouot@bnpparibas.com
<b>François Faure</b> Head of Country Risk – Türkiye	+33 1 42 98 79 82	francois.faure@bnpparibas.com
<b>Salim Hammad</b> Head of Data & Analytics – Brazil	+33 1 42 98 74 26	salim.hammad@bnpparibas.com
<b>Thomas Humblot</b> Banking Economics	+33 1 40 14 30 77	thomas.humblot@bnpparibas.com
<b>Cynthia Kalasopatan Antoine</b> Central Europe, Ukraine	+33 1 53 31 59 32	cynthia.kalasopatanantoine@bnpparibas.com
<b>Johanna Melka</b> Asia	+33 1 58 16 05 84	johanna.melka@bnpparibas.com
<b>Marianne Mueller</b> Europe, Germany, Netherlands	+33 1 40 14 48 11	marianne.mueller@bnpparibas.com
<b>Christine Peltier</b> Head of Emerging economies – Asia	+33 1 42 98 56 27	christine.peltier@bnpparibas.com
<b>Lucas Plé</b> Sub-saharan Africa, Colombia, Central America	+33 1 40 14 50 18	lucas.ple@bnpparibas.com
<b>Jean-Luc Proutat</b> Head of Economic Projections	+33 1 58 16 73 32	jean-luc.proutat@bnpparibas.com
<b>Laurent Quignon</b> Head of Banking Economics	+33 1 42 98 56 54	laurent.quignon@bnpparibas.com
<b>Tarik Rharrab</b> Data scientist	+33 1 43 16 95 56	tarik.rharrab@bnpparibas.com
<b>Mickaëlle Fils Marie-Luce</b> Media contact	+33 1 42 98 48 59	mickaelle.filsmarie-luce@bnpparibas.com



**BNP PARIBAS**

The bank  
for a changing  
world

# GROUP ECONOMIC RESEARCH

## ECOINSIGHT

Structural or thematic topics

## ECOPERSPECTIVES

Analyses and forecasts with a focus on developed and emerging economies.

## ECOFASH

Data releases, major economic events

## ECOWEEK

Recent economic and policy developments, data comments, economic calendar, forecasts

## ECOPULSE

Easy-to-read monthly overview of inflation dynamics

## ECOCHARTS

Monthly barometer of key economic indicators of the main OECD countries.

## ECOTV

What is the key event of the month?  
You will find the answer in our economy broadcast.

## MACROWAVES

Our economic podcast

The information and opinions contained in this document have been obtained from, or are based on, public sources believed to be reliable, but there is no guarantee of the accuracy, completeness or fitness for any particular purpose of such information and such information may not have been independently verified by BNPP or by any person. None of BNPP, any of its subsidiary undertakings or affiliates or its members, directors, officers, agents or employees accepts any responsibility or liability whatsoever or makes any representation or warranty, express or implied, as to the accuracy and completeness of the information or any opinions based thereon and contained in this document and it should not be relied upon as such. This document does not constitute research, as defined under MIFID II, or form any part of any offer to sell or issue and is not a solicitation of any offer to purchase any financial instrument, nor shall it or any part of it nor the fact of its distribution form the basis of, or be relied on, in connection with any contract or investment decision. Information and opinions contained in this document are published for the information of recipients, but are not to be relied upon as authoritative or taken in substitution for the exercise of judgment by any recipient, are subject to change without notice. In providing this document, BNPP does not offer investment, financial, legal, tax or any other type of advice to, nor has any fiduciary duties towards, recipients. Any reference to past performance is not indicative of future performance, which may be better or worse than prior results. Any hypothetical, past performance simulations are the result of estimates made by BNPP, as of a given moment, on the basis of parameters, market conditions, and historical data selected by BNPP, and should not be used as guidance, in any way, of future performance. To the fullest extent permitted by law, no BNPP group company accepts any liability whatsoever (including in negligence) for any direct or consequential loss arising from any use of or reliance on material contained in this document even when advised of the possibility of such losses. All estimates and opinions included in this document are made as of the date of this document. Unless otherwise indicated in this document there is no intention to update this document. BNPP may make a market in, or may, as principal or agent, buy or sell securities of any issuer or person mentioned in this document or derivatives thereon. Prices, yields and other similar information included in this document are included for information purposes however numerous factors will affect market pricing at any particular time, such information may be subject to rapid change and there is no certainty that transactions could be executed at any specified price. BNPP may have a financial interest in any issuer or person mentioned in this document, including a long or short position in their securities and/or options, futures or other derivative instruments based thereon, or vice versa. BNPP, including its officers and employees may serve or have served as an officer, director or in an advisory capacity for any person mentioned in this document. BNPP may, from time to time, solicit, perform or have performed investment banking, underwriting or other services (including acting as adviser, manager, underwriter or lender) within the last 12 months for any person referred to in this document. BNPP may be a party to an agreement with any person relating to the production of this document. BNPP may to the extent permitted by law, have acted upon or used the information contained herein or in the document, or the analysis on which it was based, before the document was published. BNPP may receive or intend to seek compensation for investment banking services in the next three months from or in relation to any person mentioned in this document. Any person mentioned in this document may have been provided with relevant sections of this document prior to its publication in order to verify its factual accuracy.

This document was produced by a BNPP group company. This document is for the use of intended recipients and may not be reproduced (in whole or in part) or delivered or transmitted to any other person without the prior written consent of BNPP. By accepting or accessing this document you agree to this.

BNP Paribas is a société anonyme incorporated in France, licensed and supervised as a credit institution by the European Central Bank (ECB) and as an investment services provider by the Autorité de contrôle prudentiel et de résolution (ACPR) and Autorité des marchés financiers (AMF), and having its registered office at 16, boulevard des Italiens, 75009 Paris, France.

Some or all of the information contained in this document may already have been published on

For country-specific disclaimers (United States, Canada, United Kingdom, Germany, Belgium, Ireland, Italy, Netherlands, Portugal, Spain, Switzerland, Brazil, Turkey, Israel, Bahrain, South Africa, Australia, China, Hong Kong, India, Indonesia, Japan, Malaysia, Singapore, South Korea, Taiwan, Thailand, Vietnam) please type the following URL to access the applicable legal notices:

© BNP Paribas (2025). All rights reserved.

Subscribe to our publications:

**ECONOMIC RESEARCH**



HOW TO RECEIVE OUR PUBLICATIONS

**SUBSCRIBE ON OUR WEBSITE**  
see the [Economic Research website](#)

&

**FOLLOW US ON LINKEDIN**  
see the [Economic Research linkedin page](#)

**OR TWITTER**  
see the [Economic Research Twitter page](#)



Published by BNP PARIBAS Economic Research

Head office: 16 boulevard des Italiens – 75009 Paris France / Phone: +33 (0) 1.42.98.12.34

Internet: [www.group.bnpparibas](http://www.group.bnpparibas) – [www.economic-research.bnpparibas.com](http://www.economic-research.bnpparibas.com)

Head of publication: Jean Lemierre / Chief editor: Isabelle Mateos y Lago

Copyright image: MihaCreative



**BNP PARIBAS**

The bank  
for a changing  
world