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> "WILL 2025 FULFIL ALL THE GOOD WISHES BEING EXCHANGED ACROSS THE GLOBE AS THESE LINES ARE BEING WRITTEN? PROBABLY NOT, SADLY. BUT NARROWING IT DOWN TO THE FIELD OF GLOBAL ECONOMICS, FIVE CRITICAL QUESTIONS SHOULD DETERMINE HOW GOOD 2025 WILL TURN OUT."

ECONOMIC RESEARCH

BNP PARIBAS

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world

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HAPPY NEW YEAR?

Will 2025 fulfil all the good wishes being exchanged across the globe as these lines are being written? Probably not, sadly. But narrowing it down to the field of global economics, I see five critical questions that will determine how good 2025 will turn out.

1. WILL THE US SET OFF A GLOBAL TARIFFS WAR?

On tariffs like on other issues, nobody knows what President Trump will do. But this is the policy area on which he has been the most consistent in words and deeds. Therefore, it is likely that tariffs on some US trading partners will go up meaningfully. The question is, by how much and what will these trading partners do in response? Under the previous Trump administration, global trade flows were rerouted but not fundamentally weakened. And, of course, the US trade deficit didn't decline. This is precisely why tariffs need to be higher and more comprehensive this time around say Trump's pro-tariff advisors. Markets and most firms could probably digest without much hiccup some additional tariffs, provided 3 conditions are met: that there is still a way around them via re-shoring; that the impact on US inflation is perceived as limited; and that trading partners keep their own economies largely open, or better still try to deepen free trade among themselves. If not, costs will be high. A generalized trade war would be stagflationary for the world and the biggest risk to its prosperity.

2. WILL CHINA FINALLY STIMULATE DOMESTIC CONSUMPTION IN A STRUCTURAL WAY?

Chinese exports surged in 2024, growing by 12% in volume even as global trade was growing at a mere 3. Meanwhile, import growth collapsed. This means China relied ever more on external demand to reach its GDP growth target of "around 5%" growth despite strong domestic headwinds (from the slow deflation of its debt-fuelled property bubble, and generally depressed economic sentiment). With US tariffs leading to a marked decline in China's share of US imports, China's rising share of global trade has happened largely at the EU's expense. Since last October, the Chinese authorities have multiplied stimulus announcements. However, these have been vague, limited in size, and focused more on helping the stock market, local governments and the real estate sector, than on boosting consumption. Yet, at 39% of GDP, Chinese households' consumption ranks 137^{th} in the world (out of 146 countries covered by World Bank data) and stands 14 percentage points below the global average. This may be about to change: recent policy pronouncements by Chinese authorities have more consistently referred to consumption as a growth driver, and President Xi himself has just started mentioning social safety net policies. Remedying their near complete absence would remove a key driver of China's sky-high savings rate. Long-awaited, such a policy turn would be good for both Chinese people and the world.

3. WILL FISCAL POLICY BE A DERAILER?

All over the world, fiscal deficits and public debts have grown significantly since 2020, and adjustment is needed. In most countries, this can happen gradually and need not be a concern. Indeed, it will help monetary policy to normalise (i.e., ease). But in a few cases, including countries that still don't have a 2025 budget, fiscal policy could be a real spoiler. In the case of the US, the negative consequences would be global. One concern has to do with governance, notably the recurring political dramas around the debt ceiling (expected to be reached in the next couple of weeks and start biting within a few months) and government shutdowns if Congress doesn't pass a funding bill in time (the most recent one, voted in extremis on 21 December 2024, expires on 14 March, 2025). These issues eventually get resolved but can cause lasting uncertainty and market volatility.

The second and deeper concern has to do with the magnitude of the government's borrowing needs. Again, the US is not the only offender, but it is the largest. The budget deficit of the Federal Government is already running at USD2Trillion per year, and the policy proposals of the Trump campaign would worsen the public debt by anywhere between USD1.7 and USD15.5 Trillion, with a central scenario of UDS7.5Trillion by 2035 according to the apolitical Committee for a Responsible Federal budget. These are enormous amounts of debt issuance for the market to swallow, not least at a time when some of the largest Treasury holders are actively looking to diversify away from them for geopolitical reasons. Further upward pressure on US Treasury yields is likely, and this will pull up rates everywhere else in the world. Like with tariffs, a moderate upward drift would be a manageable headwind. A persistent large upward move could be far more damaging. If history is any guide, it could even trigger sovereign debt crises around the world given today's wide prevalence of historically large debt burdens.

4. WILL EUROPE HEED THE WAKE-UP CALLS IT RECEIVED IN 2024?

The reports delivered by Enrico Letta and Mario Draghi, and the election of Donald Trump to a 2nd term all signalled with urgency that business-as-usual will lead Europe down a *cul-de-sac*. There are early indications that European policymakers took notice, but it remains too soon to predict with any confidence that action will follow. Leaders disagree on some key elements of policy response, notably on trade and common borrowing. France and Germany, traditionally leading the debate, can be expected to remain focused on domestic politics for a few quarters.

Still, there are areas where the EU Commission could impel meaningful progress by identifying a few early deliverables, and thereby create a good catalyst for a turnaround in investor sentiment. Some good places to start? Pausing new regulatory requirements while reviewing existing red tape, and setting an agenda for breaking the most economically costly internal market barriers.

5. CAN THE UK SHAKE OFF THE DOOM AND GLOOM OF 2024?

The UK economy has been mired in stagflation for at least a semester, as we analysed in *Ecobrief* : Bank of England: no change, but more fears about economic activity. Economic sentiment from both households and businesses is low. While our (and consensus) forecast expects a pickup in growth to around 1.4% in 2025, this hinges on the effects of the mild fiscal stimulus voted in Autumn and continued very gradual rate cuts by the Bank of England to lift the mood of economic agents. A more compelling growth narrative from the government, supported by productivity-boosting reforms, could be another helpful catalyst to improve the odds of the base case scenario.

While the answer to these questions will be key to 2025 economic outturns, their relevance extends well beyond the coming year. Indeed, they will weigh on the next decade or even quarter century. Let's not forget that the latter half of the roaring [19]20's carried the seeds of the great depression and all the misery that ensued. Now like then, democratic politics are challenged and looking weak across the world, and international relations—whether economic or otherwise—lack strong and widely accepted underpinnings. Prosperity shared by a greater number is imperative. Or else, our collective ability to tackle the truly existential challenges of our era: climate change and AI, will be at stake.

Isabelle Mateos y Lago

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ECONEWS

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UNITED STATES

The ISM Manufacturing index ends 2024 as it began: in contraction territory. Only once in the last 26 months has this index indicated growth in activity. However, the result of 49.3, the highest since March, is an improvement on the previous month (48.4). A number of FOMC members have recently expressed concern about the persistent inflation: Mary Daly, President of the San Francisco Fed; Tom Barkin, President of the Richmond Fed; and Adriana Kugler, member of the Board of Governors. US long-term interest rates have risen sharply in recent days, amid fears of "longer rates for longer" and a widening government deficit. On 6 January 2025, 10-year yields were over +4.6%, while 30-year yields were over +4.8%, the highest since April.

EUROZONE

Business sentiment continues to deteriorate in the largest economies, with the exception of Spain, where it is improving further in both industry and services. The PMI indices for December showed better momentum in services (+2.1 points to 51.6). Nevertheless, the trend in the manufacturing index remains worrying (-0.1 points to 45.1), while the new orders indicator ended 2024 at its lowest level of the year (43.0). Household confidence fell for the second month in a row in December (-0.8 points to 14.5), according to the European Commission's flash estimate. The services input price index is rising, but this is not posing a threat to the new phase of disinflation expected in 2025 at this current time. On the banking supervision side, the 2024 Supervisory Review and Evaluation Process (SREP), led by the eurozone's single supervisor, has not resulted in any major changes to Pillar 2 capital requirements for 2025. On average, the overall CET1 capital requirements and guidelines of the 113 banks supervised by the ECB increased only very slightly on 1 January 2025, from 11.2% to 11.3%.

UNITED KINGDOM

The PMI index for employment in services plunged in December (-3.9 points to 45.4), raising fears of a sharper downturn in the labour market in early 2025. This monthly fall was the second largest since 1996, excluding the COVID period. It reflects the effects of the economic environment and rising wage costs. The PMI index for services nonetheless posted a slight increase (+0.3 to 51.1), while the manufacturing index fell further into contraction territory (-1 point to 47.0). Household consumption remains sluggish. New car registrations were down 1.9% year-on-year in November, despite a 58% increase in electric vehicles. House prices ended 2024 with a strong rise of 2.0% (after -2.3% in 2023).

JAPAN

The latest JibunBank surveys from 2024 point to positive developments in December. Admittedly, the Manufacturing PMI is still in contraction territory for the sixth month in a row, but the headline figure rose to 49.6. In addition, the Services PMI again suggests growth in activity, standing at 50.9 (compared with 50.5 in November). As a result, the Composite PMI improved to 50.5 (+0.4 pp).

ERMERGING COUNTRIES

China: stronger economic growth at the end of 2024, but financial market concerns at the beginning of 2025. PMIs for the month of December suggest a strengthening in activity in the services sector (the PMI published by NBS reached 52, vs. 50.1 in November, and the Caixin PMI reached 52.2, vs. 51.5 in November). Meanwhile, manufacturing PMIs declined slightly but remained above 50. Despite the growth acceleration expected in Q4 2024 and additional stimulus measures that have been recently announced, financial markets have been nervous in the past few days. The short-term outlook for the Chinese economy indeed remains darkened by low confidence of households and private investors and by the rise in protectionist risks. Since January 1st, 2025, the CSI 300 equity market index has lost 6%, but it is still higher than its average level in the first nine months of 2024 (it rose by 15% between the beginning and the end of 2024). Depreciation pressures on the yuan have increased and long-term bond rates have reached record lows.

Türkiye: Disinflation and first easing of monetary policy. On 26 December, the central bank lowered its main policy rate from 50% to 47.5% in response to the slowdown in inflation, which continued in December (+1.1% over one month compared with +3.1% per month on average in 2024). In yoy terms, the inflation rate fell to 28.5% from 44.2% in December 2023.

Brazil: Central bank interventions fail to stem currency slide. During the last two weeks of December, the BCB spent nearly USD 20 bn in foreign exchange reserves to curb the depreciation of the real and stem the negative market confidence spiral affecting the country since late November. In the absence of fiscal recalibration efforts deemed credible by the markets, the effectiveness of the BCB's interventions – aimed at reversing the downward trajectory of the currency and limiting its spillover into other asset classes – is expected to remain relatively limited.

COMMODITIES

The drop in stocks is pushing the price of hydrocarbons up at the beginning of the year. On the European gas market, the TTF benchmark reached EUR 50/MWH, a 15-month high. While the halt in Russian gas exports transiting through Ukraine (around 5.6% of total EU imports) was widely anticipated by the market, the accelerated decline in European gas inventories (to a two-year low), in a context of seasonal demand increases, has increased market nervousness and pushed prices up. In the short term, beyond seasonal factors, prices are expected to remain strong, with the replacement of the Russian flow via Ukraine (by pipeline) by LNG imports resulting in additional costs.

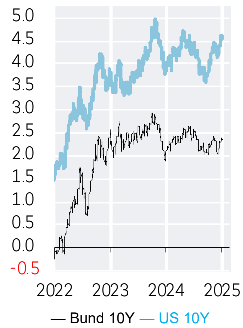
At the same time, Brent prices have recovered above USD 75/bbl, against a backdrop of a reduction in US crude oil inventories (excluding strategic stocks), which are close to their lowest level in 5 years. In this context, the support of Asian demand was welcomed by the market.

MARKETS OVERVIEW

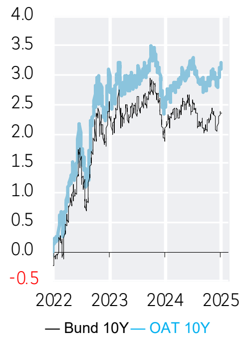
Bond Markets

Bond Markets	in %	in bps			
	03-janv.-25	1-Week	1-Month	Year to date	1-Year
Bund 2Y	2.18	+6.8	+21.0	+11.8	-51.1
Bund 5Y	2.19	+4.9	+31.0	+8.1	+26.0
Bund 10Y	2.43	+3.5	+37.2	+6.3	+41.1
OAT 10Y	3.22	+9.0	+37.1	+9.1	+73.2
BTP 10Y	3.49	+5.5	+36.5	+6.7	-4.6
BONO 10Y	3.07	+3.2	+35.6	+5.0	+12.4
Treasuries 2Y	4.28	-5.0	+6.3	+3.2	-12.0
Treasuries 5Y	4.41	-4.4	+28.3	+3.2	+52.4
Treasuries 10Y	4.60	-2.0	+36.5	+2.6	+69.7
Gilt 2Y	4.19	-5.8	+11.8	+4.2	+8.9
Treasuries 5Y	4.39	-3.0	+28.9	+4.0	+94.3
Gilt 10Y	4.59	-4.1	35.0	+2.1	+87.5

Bund 10Y vs US Treas. 10Y



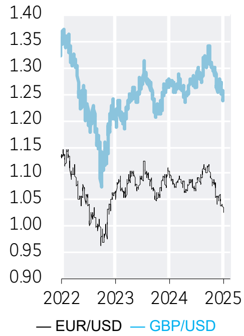
Bund 10Y vs OAT 10Y



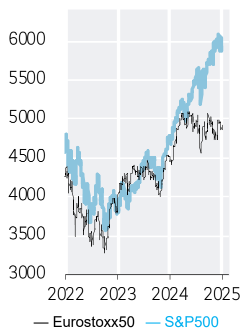
Currencies & Commodities

Currencies & Commodities	Level	Change, %			
	03-janv.-25	1-Week	1-Month	Year to date	1-Year
EUR/USD	1.03	-1.3	-2.2	-0.6	-5.7
GBP/USD	1.24	-1.4	-2.0	-1.0	-1.8
USD/JPY	157.40	-0.1	+5.5	+0.2	+9.6
DXY	111.99	+7.9	+11.5	+10.5	+6.1
EUR/GBP	0.83	+0.1	-0.2	+0.3	-3.9
EUR/CHF	0.94	-0.3	+0.6	-0.1	+0.8
EUR/JPY	161.95	-1.4	+3.2	-0.5	+3.4
Oil, Brent ($/bbl)	76.35	+3.1	+3.7	+2.2	-2.2
Gold ($/ounce)	2643	+1.0	+0.1	+0.7	+30.0

EUR/USD vs GBP/USD



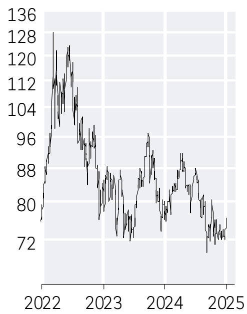
EUROSTOXX 50 vs S&P500



Equity Indicies

Equity Indicies					
World					
MSCI World ($)	3738	-0.5	-2.4	+0.8	+20.0
North America					
S&P500	5942	-0.5	-1.8	+1.0	+26.3
Dow Jones	42732	-0.6	-4.4	+0.4	+14.2
Nasdaq composite	19622	-0.5	+0.7	+1.6	+34.5
Europe					
CAC 40	7282	-1.0	+0.4	-1.3	-1.7
DAX 30	19906	-0.4	-0.6	-0.0	+20.4
EuroStoxx50	4871	-0.6	-0.1	-0.5	+9.5
FTSE100	8224	+0.9	-1.6	+0.6	+7.1
Asia					
MSCI, loc.	1435	-0.6	-0.1	+0.2	+15.5
Nikkei	39895	-1.0	+1.6	+0.0	+19.2
Emerging					
MSCI Emerging ($)	1073	-0.9	-2.2	-0.3	+7.0
China	63	-2.8	-1.2	-2.1	+15.5
India	1039	+0.9	-2.7	+1.1	+13.6
Brazil	1172	-0.2	-8.7	-0.4	-33.6

Oil, Brent ($/bbl)



Gold ($/ounce)

Performance by sector

Eurostoxx600

Year 2025 to 3-1, €

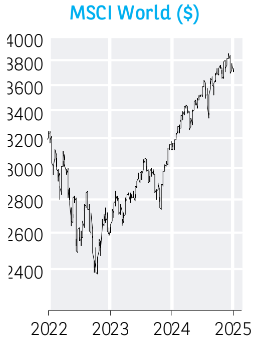
+3.6%	Oil & Gas
+1.9%	Utilities
+0.9%	Telecoms
+0.7%	Insurance
+0.4%	Health
+0.1%	Industry
+0.1%	Index
+0.0%	Technology
-0.0%	Real Estate
-0.2%	Commodities
-0.4%	Banks
-0.4%	Construction
-0.4%	Food industry
-0.7%	Retail
-0.9%	Media
-1.2%	Travel & leisure
-1.4%	Chemical
-2.3%	Automobiles
-2.7%	Consumption Goods

S&P500

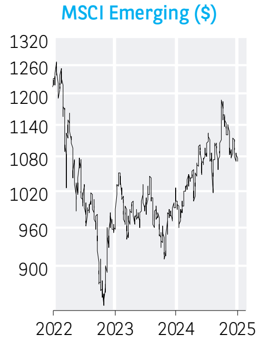
Year 2025 to 3-1, $

+5.2%	Semiconductors
+1.9%	Energy
+1.8%	Utilities
+1.6%	Media
+1.6%	Consumer Discretionary
+1.5%	Bank
+1.3%	Automobiles
+1.3%	Healthcare
+1.0%	Index
+0.8%	Pharmaceuticals
+0.8%	Capital Goods
+0.5%	Real Estate
+0.2%	Retail
+0.1%	Consumer Services
+0.1%	Commercial & Pro. Services
-0.1%	Telecoms
-0.2%	Food, Beverage & Tobacco
-0.4%	Insurance
-1.1%	Materials
-2.0%	Tech. Hardware & Equip.

MSCI World ($)



MSCI Emerging ($)



SOURCE: LSEG, BLOOMBERG, BNP PARIBAS

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