Quarterly Macro Report – 2nd Quarter 2025

The first few months of 2025 have been marked by disappointing economic data and US President Trump's aggressive trade policies, which have significantly increased global uncertainty. Amid these challenges, expectations are turning to monetary and fiscal policy to stabilise the economic outlook.

From an economic perspective, the beginning of 2025 has been disappointing, particularly in the United States. After several years of growth exceeding the long-term trend, the US economy slowed noticeably in the first months of the new year.

The slowdown has largely been attributed to President Trump's erratic economic policies. Contrary to the expectations of many observers, Trump has not prioritised the pro-growth policies of his election campaign, such as deregulation or tax cuts. Instead, he has adopted a highly protectionist, tariff-driven trade policy characterised by unpredictability and frequent reversals.

As a result, US consumers are becoming increasingly unsettled. Consumer sentiment has deteriorated sharply since the beginning of the year and inflation expectations have risen significantly. Households now expect inflation to be around 5% over the next year, some two percentage points higher than current levels.

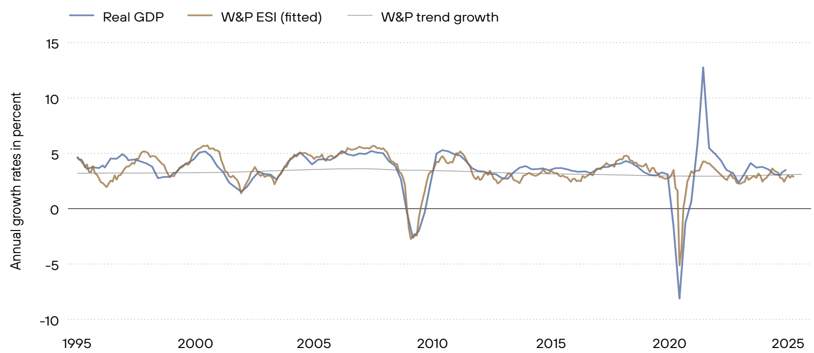
This deterioration in consumer sentiment comes at a difficult time for households, as income has long lagged expenditure growth, while pandemic-era savings appear to have been largely depleted. As a result, consumer spending - previously the key driver of US economic strength - has weakened considerably, rekindling fears of an impending recession.

Stagnation in Europe and China

Disappointing economic data is, however, not limited to the US. Europe is facing similar challenges too. In the eurozone, the expected economic recovery remains a challenge, with business and consumer sentiment stagnating and industrial activity remaining sluggish. Germany and France, the region's two largest economies, are particularly

Fig. 1: Sentiment indicates potential slowdown of economic growth

Real GDP world and sentiment proxy



So far, global economic growth has been supported by the US and select emerging markets, such as India. However, sentiment indicators are now pointing toward a potential slowdown in economic momentum.

Source: LSEG, Wellershoff & Partners

affected. In the UK, the economic upturn observed in mid-2024 has proved to be short-lived, with growth slowing significantly since then. While Switzerland remains comparatively stable, growing uncertainty over US trade policy casts doubt on its future growth trajectory.

> "The uncertainty surrounding the aggressive trade policy of the US administration is leaving its mark globally."

In China, the picture is mixed. Although business sentiment improved slightly towards the end of the first quarter and consumer spending picked up, import activity remains weak and inflation has slipped back into negative territory. A sustained recovery that would bring China closer to its 5% growth target is therefore still some way off.

Fiscal and monetary policy to the rescue?

Given the challenging global economic environment, hopes are increasingly pinned on monetary and fiscal policy interventions. In the US, market participants expect the Federal Reserve to cut interest rates substantially if economic conditions deteriorate further. Germany plans to overcome its economic stagnation with a significant fiscal stimulus package, involving new borrowing of up to one trillion euros. Similarly, the EU has relaxed its fiscal rules, freeing up an additional €800bn, mainly for defence investment. China has also recently stepped up its fiscal support measures.

However, it remains uncertain whether these measures will live up to their expectations. In the US, elevated inflation expectations have done little to improve the inflation outlook, and the Fed may even view a moderate economic slowdown as a positive. In Europe, the immediate impact of fiscal stimulus may be limited due to long investment cycles, particularly in defence and infrastructure. China's current measures have had only modest results so far, raising questions about the effectiveness of its approach.

Table 1: Macroeconomic estimates (in %)

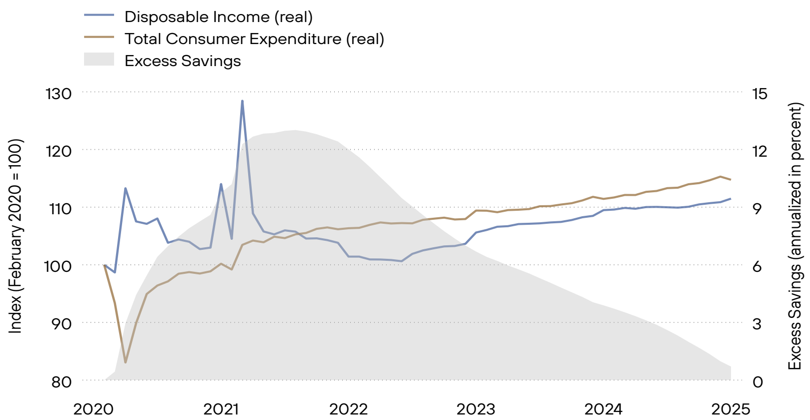
	GDP Growth			Inflation		Interest Rates	Money Growth M1
	Trend	**2024**	**2025*E***	**2024**	**2025*E***	**Q2 2025**	**y/y 03/2025**
USA	1.6	2.8	2.4	3.0	2.5	4.50	3.0
Eurozone	1.1	0.8	1.0	2.4	2.5	2.50	3.8
UK	1.8	0.9	1.2	2.5	2.4	4.50	2.2
Switzerland	1.3	1.3	1.5	1.1	0.8	0.25	5.7
Japan	1.1	0.1	1.1	2.7	1.5	0.50	0.8
China	4.5	5.0	4.5	0.0	1.0	4.35	64.3[1]
Brazil	1.7	3.4	1.5	4.4	3.2	14.25	4.7
India	5.0	6.7	5.5	4.9	4.2	6.25	6.1
Russia	1.0	4.1	1.0	8.5	4.5	21.00	4.5
World	3.1	3.2	3.1	5.8	3.8	–	–

Source: LSEG, Wellershoff & Partners

1 China has expanded the statistical scope of M1 as of January 2025.

Fig. 2: Disposable income lags behind expenditures

US household's disposable income, expenditures and excess savings since 2020

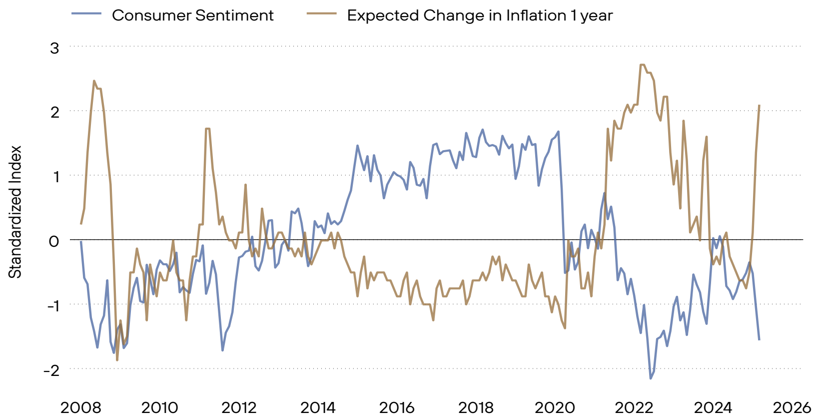


Source: LSEG, Wellershoff & Partners

Household expenditure has risen faster than income, reflecting growing financial pressure. In addition, the excess savings accumulated during the COVID-19 pandemic have been largely depleted, leaving less cushion for future spending and increasing the risk of reduced consumer demand.

Fig. 3: Drop in consumer sentiment and rising inflation expectation

US consumer sentiment index and one-year inflation expectation

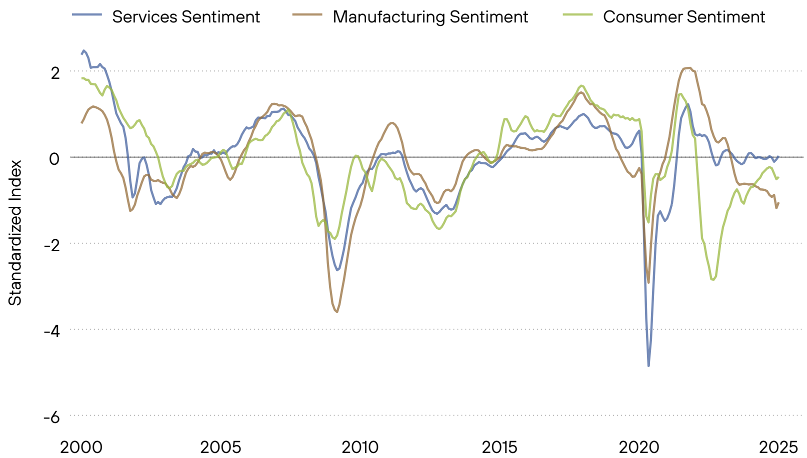


Source: University of Michigan, Wellershoff & Partners

US consumer sentiment has declined, reflecting growing economic concerns. At the same time, one-year inflation expectations shot up, signalling that consumers are bracing for sustained price pressures in the near future.

Fig. 4: Sentiment indicators recover only marginally

Sentiment indicator by industry in the Euro Area



Source: LSEG, Wellershoff & Partners

In the euro area, sentiment in the services sector remains stagnant. Consumer and industrial confidence, while pointing upwards, are still well below their long-term averages, reflecting ongoing economic challenges despite fiscal stimulus efforts.

Capital Market

Concerns about rising inflation expectations and weakening consumer sentiment have created turbulence in global markets. While US equity markets briefly entered a technical correction earlier this year, the fixed income markets have shown divergent developments across regions.

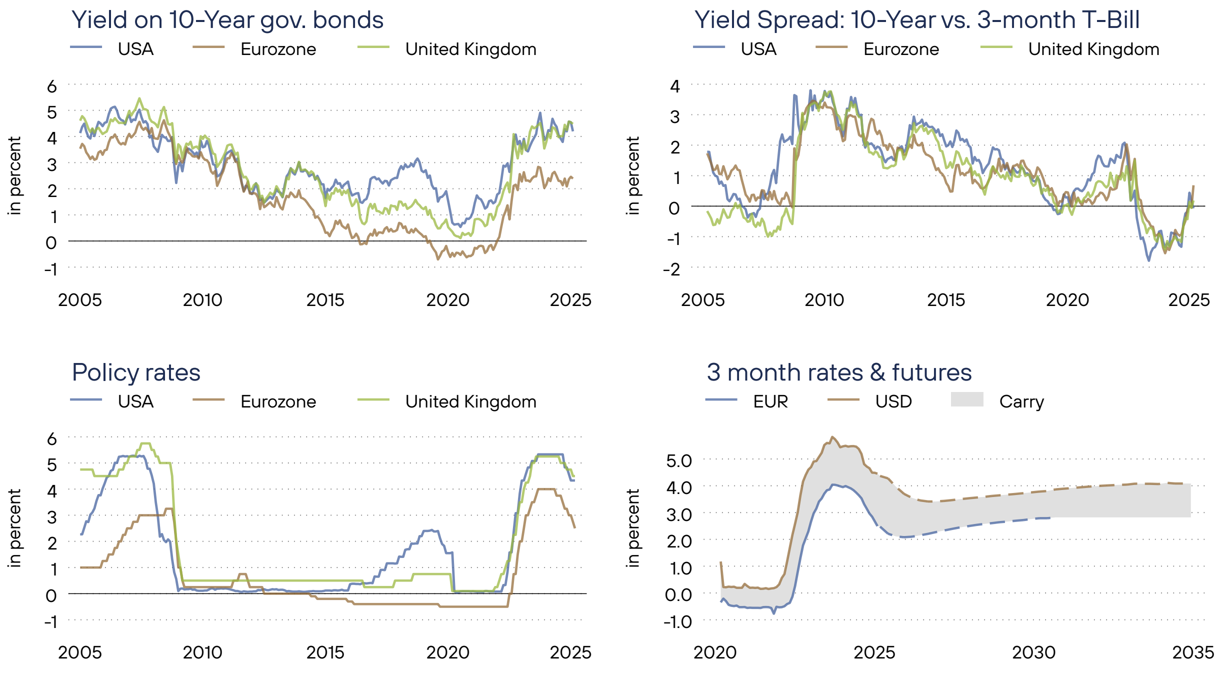
In the US, the rise in long-term bond yields, mainly driven by concerns over Donald Trump's inflationary tariff policies, observed in late 2024 did not persist. The yield on 10-year government bonds declined from 4.8% in mid-January to approximately 4.3%. However, this retreat in long-term rates has not extended to the short end of the curve. With the Federal Reserve holding its benchmark interest rate steady since December, yields on 3-month Treasury bills remained stable around 4.3%. This resulted in a flattening of the US yield curve, with short and long-term rates now at similar levels. The Federal Reserve maintained a cautious stance at their last meeting, balancing rising inflation expectations with declining consumer sentiment and rising recessionary fears. Markets anticipate 50 to 75 basis points of rate cuts by the Fed over the course of this year.

> "Capital markets hinge on a balancing act of inflation pressures and fragile economic recovery."

Conversely, in the eurozone, long-term interest rates rose during the first quarter of 2025. The yield on 10-year government bonds increased by roughly 70 basis points, driven in part by Germany's announcement of a significant fiscal stimulus package, which led to a repricing of government bonds across the region. At the short end of the curve, the European Central Bank implemented further monetary easing, cutting its reference rate by 25 basis points in both January and March. As a result, the eurozone yield curve has moved back into positive territory. Markets have priced in an additional 50 basis points of rate cuts by the ECB for the remainder of the year, reflecting a continued accommodative monetary policy stance.

The geographic divergence in interest rate trends underscores differing economic challenges and policy priorities in the US and Europe.

Fig. 5: Money market and capital market interest rates



Source: LSEG, Wellershoff & Partners

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