Helaba

Markets and Trends 2025
Global Economy on the Catwalk

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The Editorial for 2025: Global Economy on the Catwalk

Every year, our Economic and Capital Market Outlook is based on a **theme** that acts as a metaphor for the year ahead. This time, we have chosen the world of fashion. Just like the fashion industry, both the economy and capital markets are characterised by cycles and trends, which will be parading on the global economy catwalk in 2025. But what will be in vogue in 2025? Are aspects such as trade tariffs set to remain in fashion, or will they soon be "out" again?

One name set to make a big comeback on the catwalk is Donald Trump, who made his priorities clear during his first term in office and in his most recent re-election campaign. Yet again, voters were won over by his "America First" slogan. The big question is whether the 2025 collection will largely resemble that from Trump’s first term. In respect of economic policy, this would mainly mean trade tariffs and tax cuts, which would lead to higher public debt.

The German collection is perhaps even more eagerly anticipated. What will it look like? The end of the traffic-light coalition means each couturier has to completely rethink their designs. The German public has become more discerning – hardly surprising given that the last three years' patterns all proved disappointing in the end.

> *“You can never be overdressed or overeducated.”*
> *Oscar Wilde*

With our outlook titled "**Global Economy on the Catwalk**", we explore the various concepts and ideas that the numerous designers have to offer. A successful catwalk show depends on many factors, with zeitgeist, sentiment and even pure luck playing a major role. We have put together three collections for our 2025 Economic and Capital Market Outlook that we present under the labels of "Workwear", "Haute Couture" and "The Emperor's New Clothes". Among the highly diverse range, it is not just items of clothing that make a winning outfit; the accessories are also important.

Yet, some of these accessories turn out to be badly suited. Rather than making global trade more attractive, the much-vaunted fashion jewellery of "**protectionism**" will damage global labour productivity. Despite this, it is likely that the US will impose new tariffs on Chinese goods. It is to be hoped that the general tariffs that Trump has threatened are simply a bargaining chip to encourage America's partners to make political concessions, even on issues not directly related to trade.

Baseline scenario: Workwear

The basic collection, "**Workwear**", is going to make a big splash in 2025. While protecting against a multitude of risks, at the same time it is the perfect attire for really tackling the job at hand. Ideally, workwear should fit well and the belt should neither be too tight nor too loose. The major **central banks** began loosening the **belt** in 2024, having gradually tightened it in over the previous two years. In some countries, the belt has left pressure marks behind. So, have central banks finally managed to find the best-fitting hole on the belt?

In our baseline scenario, to which we have assigned a 65 % probability, central banks succeed in finding the right belt width to contain inflation without strangling economic growth. The challenges that lie ahead in 2025 can be met with some extra accessories such as helmets, safety goggles and gloves.

Negative scenario: The Emperor's New Clothes

In our gloomy scenario, entitled "**The Emperor's New Clothes**", there is widespread disenchantment. This eagerly awaited collection was announced with the promise of magnificent robes. In the fairy tale by Hans Christian Andersen, only clever people can allegedly see the clothes, so neither the ruler nor his court reveal the deception. Blind faith in authority and a form of collective self-delusion maintain the illusion until it is abruptly shattered. The global economy, too, is not entirely immune to designs like these. We assign a probability of 25 % to this negative scenario.

Probabilities for economic and capital market scenarios

Source: Helaba Research & Advisory

Positive scenario: Haute Couture

In this scenario, a boom is in full swing. Everything runs smoothly, tensions in the global economy dissipate and world premieres captivate the public. But even **Haute Couture** requires hard work, especially backstage, and luck. Many factors would have to align for 2025 to shape new and sustainable trends in the global economy for the coming years – but it is not inconceivable. The safety goggles become a VR headset and the toolbox with its public funds is no longer needed to solve every problem, as the state focuses on establishing the overall conditions for business to flourish. Rather than an unwieldy suitcase, only a lightweight clutch bag is needed. Global trade thrives, international collaboration is frictionless and geopolitical tensions are resolved. Delicate and ornamental jewellery replaces cumbersome chains. At 10 %, our positive scenario has a lower probability than our negative scenario.

Take a seat and enjoy the Helaba Fashion Show with our 2025 Economic and Capital Market Outlook. I hope you find your favourite outfit among this year's range and that your investment decisions will cut a good figure in it.

Yours,

Dr. Gertrud R. Traud
Chief Economist/Managing Director

Baseline scenario: Workwear (65 %)

When it comes to work, external factors mainly dictate the choice of clothes, with individual preferences playing a lesser role. The nature of the task determines what to wear. In 2025, the global economy is going to need sturdy, flexible and practical workwear with enough pockets for any tools that may become necessary. Hopefully, it will also be easy care as a few stains along the way are likely.

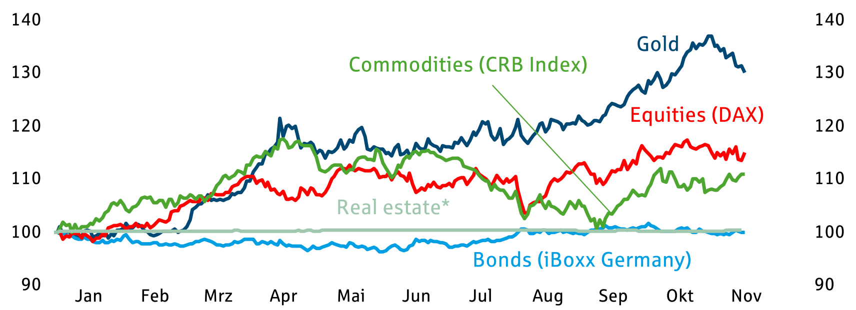
Ideally, workwear should fit well and the **belt should be neither too tight nor too loose**. After 2022, the major central banks – led by the Fed and the ECB – drastically tightened **monetary policy** before, as expected, pivoting to an easing course in 2024. For some countries, the search for the right belt width meant that, economically, things got uncomfortably restrictive. Have central banks now managed to find the best-fitting hole on the belt?

At the moment, it looks as if monetary policymakers are reining in high inflation rates **without triggering a deep recession**. For countries such as Germany or China, the economic problems they have been grappling with for some time are hardly mainly due to excessively high interest rates. In fact, the underlying causes are a property crisis in China that remains yet to be adequately addressed and Germany's competitiveness that has been deteriorating for years.

In the United States, much points to the first "soft landing" for the economy since 1995. So far, there has only been a modest softening of **labour markets** in the large industrialised countries and they remain historically tight today – partly due to shifting demographics. In addition, inflation expectations have not risen as sharply as they did in the 1970s. This achievement by central banks was anything but a foregone conclusion. Having previously been distracted by issues such as climate change and economic inequality, policymakers reacted too late to the spike in inflation.

The great outperformer: Gold

Indexed, 31.12.2023 = 100, total return in Euro



Sources: LSEG, Helaba Research & Advisory

Meanwhile, it would appear that even **China's** central bank received its instructions from the government to adopt an unambiguous path of monetary stimulus. It is likely to continue down this road in 2025. Only **Japan** has tailored a different fit for its workwear: The Bank of Japan recently hiked its key interest rate and is set to raise it a bit further by the end of 2025.

Both the **ECB** and the **Fed** are expected to **scale back the degree of monetary tightness substantially** in 2025 without venturing deep into expansionary territory, as they did in previous easing cycles. As things currently stand, this will not become necessary.

Fiscal policy: A more prudent use of the toolkit is (mostly) called for

The "monetary belt" has thus been adjusted to enable a successful “let’s get the job done!” in 2025. However, this is **just one of many factors** that will ultimately determine whether 2025 is going to be good or bad economically.

Lately, the dominant approach to **fiscal policy** in many countries has been a liberal deployment of the public spending toolkit for every conceivable problem. Based on figures from the IMF, the cyclically adjusted or **structural deficit** in industrialised countries has risen to an average of around 5 % of GDP – roughly **twice as high as before COVID-19**. Since then, however, an increasing number of governments have been forced to apply smaller wrenches, either because fiscal policy has veered along an unsustainable trajectory (as in France and Italy) or because it bumps up against legally imposed limits (the debt brake in Germany).

Here, too, it is the exception that proves the rule as **China** has been digging deep into the fiscal policy toolbox since the second half of 2024. Although the **US** is unlikely to raise the deficit in 2025, President-elect Donald Trump has promised sweeping **tax cuts**. They are likely to only come into effect at the end of next year, but their impact would be felt in advance in terms of better sentiment and a greater propensity to spend.

Long considered "out": Retro look in geopolitics and trade policy makes a comeback

Despite **some proficient tailoring**, the world's workwear in 2025 will pinch and itch in places. We do not expect any let-up in **geopolitical tensions**. On the contrary: It would likely be an achievement if the multiple conflicts do not escalate further or widen geographically in the new year. Solutions that actually deserve that name are not on the horizon, neither in Ukraine nor in the Middle East. The relationship between the West and **China** is poised to deteriorate further. All manner of market intervention remains politically fashionable.

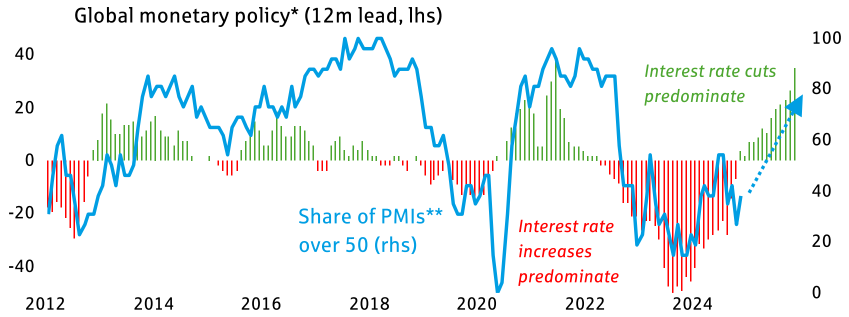
A number of accessories are likely to prove counterproductive. The costume jewellery of "**protectionism**", which many are advocating for, is hanging like a millstone around the neck of international trade and damaging global labour productivity. It is also restricting the world's mobility. New US tariffs against China are on the cards. It is to be hoped that the general tariffs that Trump has threatened to impose are simply a bargaining chip to encourage America's partners to make political concessions, including on issues that do not directly relate to trade.

Dressed for the occasion – recovery in industrial economy finally arrives!

Even trade disputes will not prevent a recovery in the **industrial cycle**, which has been sputtering for some time. Partly due to the disruptive effects of trade and industrial policy described above, we anticipate a gradual upturn rather than a fully-fledged boom in this segment. Nevertheless, it will be precisely those countries that previously suffered the most from the industrial downturn that will benefit disproportionately from its recovery. These include **Germany**, where 2025 is likely to see a **long period of stagnation** and negative sentiment **come to an end**. At the same time, a host of structural factors, such as demographics, a lack of investment in next-generation technology or overregulation, will remain. A major shift like decarbonisation also does not come cheaply.

Monetary easing to help manufacturing

Share of central banks cutting interest rates minus those raising interest rates, 3M average, % points %



*changes to key interest rates by 19 leading central banks ** manufacturing in 26 countries
Sources: Macrobond, Helaba Research & Advisory

A year ago, we underestimated the growth prospects for the US in 2024 and overestimated those for Germany. **On a global scale, however, these mistakes have cancelled each other out**. As we forecast last year, the world economy as a whole neither significantly picked up nor lost momentum in 2024. With the appropriate workwear, it should also be successful in 2025, with Germany finally contributing to growth again.

Overview of forecasts in the baseline scenario

We expect the annual average of global economic **growth** in 2025 to remain roughly the same as in 2024. Following two years of stagnation, Germany is set to expand again with growth of 0.7 % – a rate that will continue to underperform the average in the euro zone (1.2 %). China and the United States should both post somewhat weaker growth on average than in 2024, although this masks a cyclical recovery that will gather steam during 2025.

It is unlikely that **inflation** will be a dominant factor in 2025; instead, it will probably act as more of a limiting condition in determining the scope for monetary policy easing. Even with oil prices going up, consumer price inflation will be lower on average over the year than in 2024. We anticipate that inflation in both Germany and the euro zone as a whole, at 2.1 % and 2.2 % respectively, will be close to the ECB's own inflation target in 2025. Across the pond, the Fed should also broadly achieve its definition of price stability.

Selected forecasts for 2025

Euro area

GDP growth, %	1.2			
Inflation, %	2.2			
Q1 - Q4				
Deposit rate, %	2.50	2.00	2.00	2.00
USD / Euro	1.05	1.05	1.10	1.10
EURO STOXX 50, index value	4,900	4,950	5,000	5,050

Germany

GDP growth, %	0.7			
Inflation, %	2.1			
Q1 - Q4				
3M Euribor, %	2.30	2.00	2.00	2.00
10y Bunds, %	2.20	2.20	2.30	2.50
DAX, index value	19,750	20,000	20,250	20,500

USA

GDP growth, %	2.2			
Inflation, %	2.5			
Q1 - Q4				
Federal Funds Rate (mid-point), %	3.88	3.63	3.63	3.63
10y Treasuries, %	4.30	4.30	4.40	4.50
S&P 500, index value	6,250	6,300	6,350	6,400

Source: Helaba Research & Advisory

Consequently, we look for **central banks** to stick to the same path that they embarked on in 2024. In the US, the Federal Funds Rate will most probably fall to around 3.5 % while the Fed is likely to terminate its passive balance sheet run-off at some point during the year. Similarly, in the euro zone the ECB will presumably lower the deposit rate to 2 % and continue winding down its balance sheet.

Theoretically, the rate-cutting cycle should provide a relatively positive environment for **bonds**. However, fiscal policy and other political issues will emerge as particularly critical factors for sovereigns. The best that can be expected are temporary yields of up to 2 % for German Bunds and 4 % for 10-year US Treasuries. By the end of 2025, benchmark issues are likely to be trading at 2.5 % and 4.5 %, respectively.

While it would appear that many positive developments have already been priced in, **equities remain en vogue**. Consequently, any further cuts to key interest rates will create additional scope for higher valuations. An improving global growth and earnings outlook also bodes well for a modest increase in prices in 2025. However, given that valuations on US benchmark indexes are already high and that structural challenges are holding back the DAX, this increase will "only" be average. The DAX is forecast to reach 20,500 points by the end of 2025.

> *“Always wanting to keep up with fashion has one disadvantage: You will always be behind it.”*
> *Ernst Ferstl*

In 2025, the German **real estate market** should see a modest rise in house prices with a continued high level of demand and shortage of supply. At the same time, there is likely to be a further decline in new construction. Prices for commercial real estate should stabilise and transaction activity is set to climb again.

Gold will continue to reap the rewards of a turnaround in monetary policy and ongoing geopolitical tension. For this reason, we expect this asset class to shatter even more records in 2025, even if not at the same pace as this year. At year-end, gold should be trading at just over 2,800 US dollars per troy ounce as the precious metal remains in fashion as a safe alternative during times of uncertainty.

The political environment will be the dominant factor for the **US dollar**. Little impetus can be expected from monetary policy, the Fed and the ECB will reduce their key interest rates by a similar magnitude. However, US President Trump is likely to fuel volatility on the markets, particularly with his trade policies, and a stronger dollar is unlikely to be his objective. The euro-dollar exchange rate should settle at around 1.10 by the end of 2025.

Patrick Franke

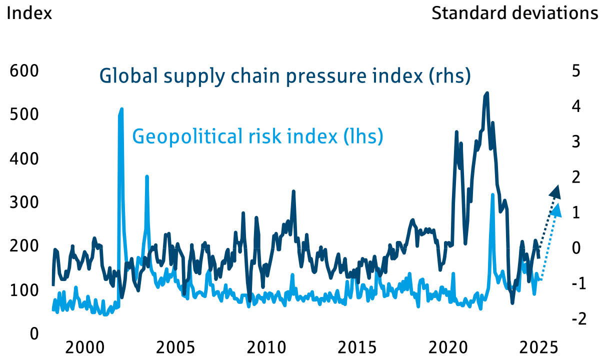
Negative scenario: The Emperor's New Clothes (25 %)

In the fairy tale by Hans Christian Andersen, fraudsters trick the vain Emperor into believing that they are tailoring magnificent robes for him. As only clever people can allegedly see the clothes, neither the ruler nor his court reveal the deception. Blind faith in authority and a form of collective self-delusion maintain the illusion until it is abruptly shattered. The global economy may be about to experience a similar moment of truth.

In our negative scenario, the macroeconomic policies that governments and central banks so often pride themselves on turn out to be a mirage. Just like the child's voice in the fairy tale, even a mild shock could disrupt the world's **collective self-delusion** and make companies, consumers and financial markets realise that their actions and plans are based on unsustainable and overly positive assumptions. The result: abrupt adjustments.

But what could provide such a **wake-up call**? For all the recent complacency that some central bankers have been flaunting, it is far from a foregone conclusion that previous **monetary tightening** has not overshot the mark after all and is acting as a bigger drag on the economy than anticipated. While policymakers changed course as early as 2024, most key interest rates are still clearly in restrictive territory. It may well be that monetary policy is just as effective in this cycle as it always has been but is simply working more slowly. The withdrawal of liquidity from the economy could expose underlying vulnerabilities.

Geopolitical tensions disrupt supply chains



Sources: Wells/Yang/Yu/Iacoviello, Bloomberg, Helaba Research & Advisory

However, a more likely spark is an **escalation in geopolitical tension** leading to a marked increase in uncertainty and disrupting global supply chains. The list of potential triggers is long and ranges from a regional spillover of conflicts in Ukraine or the Middle East all the way to possible new flashpoints in Asia (Korea, Taiwan, the South China Sea).

> *"Only when the tide goes out do you discover who is swimming naked."*
> *Warren Buffett*

It does not even have to necessarily involve conflicts developing along the usual fronts. **Transatlantic relations** could also sour very quickly, with differences of opinion over the pace of decarbonisation – consider here the EU's Carbon Border Adjustment Mechanism coming into force at the start of 2026 – and protectionism emerging as contentious issues. The likelihood that these kinds of disagreements could get out of hand is large when an erratic figure such as Donald Trump is involved. In our negative scenario, the Unites States and the EU engage in a tit-for-tat trade war, imposing considerably higher tariffs on each other.

Governments are part of the problem, not the solution

In many places, **imbalances in the private sector** are currently smaller than in previous recessions, with the exception of housing prices in some countries. However, a number of governments are running unsustainably high fiscal deficits and the average **debt-to-GDP ratio** in industrialised countries has reached almost 110 %, despite the recent surge in inflation dressing up the figures. The pandemic appears to have been the second economic shock with a ratchet effect after the financial crisis that has led to debt becoming entrenched at a higher level. Meanwhile, even the generous use of public funds no longer serves as a magic bullet for every type of crisis.

There are no indications of urgently needed economic policy reforms. While **overregulation** of the economy is acknowledged as a problem, nothing is being done to address it effectively. In many cases, people even continue to heap praise on the splendid colours of the Emperor's new clothes: In President Biden's last year in office, for instance, the number of new regulations “with an economic impact" has shot to an all-time high. Rules have recently come into effect in Europe that not only force companies to monitor possible human rights violations in their supply chains but also the historical use of agricultural land by their business partners – with the threat of financial penalties if they do not. Despite new protagonists taking the reins the United States and Germany, very little progress is made here in this scenario.

Overview of forecasts in the negative scenario

The global economy plunges into a **recession**. With a growth model largely dependent on exports, Germany is disproportionately impacted by protectionism and disruption to supply chains. This leads to a contraction in German GDP of around 2 % in 2025. The United States, less dependent on manufacturing and trade, is not as badly affected. There is a significant rise in unemployment rates.

Inflation falls due to tumbling oil prices and companies' dwindling pricing power. Those who had always regarded inflation as a "transitory" phenomenon gain the upper hand. Inflation in Germany slips below 1 % and the rate of price increases eases back across the whole euro area, too. Higher import tariffs in the United States prevent a sharper drop in inflation, which is mainly driven down by significantly **lower oil prices**.

> “*Clothes make the man. Naked people have little or no influence on society.”*
> *Mark Twain*

In this environment, **central banks** respond by pursuing an even more accommodative monetary policy than in the baseline scenario. The ECB accelerates the interest-rate cutting cycle, lowers the deposit rate into expansionary territory towards 1 % by the end of 2025 and stops quantitative tightening. The Fed cuts the Fed Funds Rate to below 2 %.

There are sharp price gains on the **bond market**. In the wake of a steep decline in key interest rates and decreasing inflation expectations, the yield on 10-year US Treasuries falls to 2 % while that on 10-year German Bunds approaches the 1 % mark.

Mounting geopolitical tension results in major disruption to supply chains, with conflicts over trade exacerbating the problem. Consequently, corporate earnings plummet. Investors become more risk averse, causing valuations to shrink. **Equities** enter a bear market and the DAX plunges to 12,500 points.

The recession and increasing global uncertainty weigh on **real estate**. In this weak economic environment, the correction in commercial real estate gathers pace again. Although prices in the residential segment remain stable, the trend of rising house prices that had recently emerged grinds to a halt.

In times of uncertainty, **gold** lives up to its timeless reputation. The precious metal benefits both fundamentally and politically as a safe haven investment and soars to 3,800 US dollar per troy ounce.

In the midst of geopolitical volatility, the **US dollar** is once again in strong demand as a safe haven currency – even with Donald Trump in the White House. Additionally, Europe suffers more than the US from escalating trade wars. The euro-dollar exchange rate falls to 0.90.

Patrick Franke

Positive scenario: Haute Couture (10 %)

“Haute couture” is associated with supermodels, Karl Lagerfeld's fan and legendary icons of style such as Giorgio Armani. However, designing a winning collection requires a passion for innovation, hard work – particularly backstage – and luck. Many factors would have to align in the global economy in 2025 to shape new and sustainable trends for the coming years – but it is not inconceivable.

Regrettably, the number of **necessary conditions** for our positive scenario to materialise is considerably higher than for the negative scenario's "illusion". These include a greater willingness to collaborate on the international stage that would ease geopolitical tensions, create a more predictable environment and, ideally, promote technological progress. Having posted **record earnings in** recent years, large US companies are in a particularly strong position to invest. As unrealistic a prospect as it might seem, shifting away from a widening schism in the global economy between a US-dominated bloc and one led by China would clearly benefit transnational research, specialisation and, in turn, **worldwide productivity**.

This is a crucial factor because no reforms, however successful they may be, will provide any short-term boost to the **supply of labour** in the largest economies. In addition, there is no prospect of significantly longer working weeks or lives in most countries, and it is unrealistic to expect any drastic rise in the labour force participation rate. Consequently, raising productivity is the only way to achieve higher growth and this will require **smarter or fewer regulations** that stimulate research and development and, as a result, investment. In many areas, long-overdue structural reforms would have a similar effect. Deploying more (broadly defined) capital such as **artificial intelligence** could lift output per worker.

> *“Throwing money out the window brings money back in through the front door.”*
>
> Karl Lagerfeld

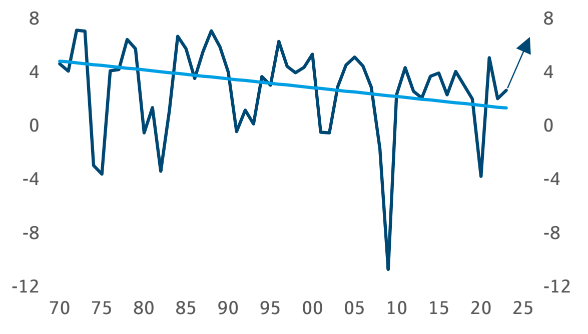
On the demand side, **private consumption** in many countries, including Germany and China, has significant upside potential. Demand for **housing** is rising faster than the rate of construction in many places, so there is scope for further growth here as well. The key driver, though, would be **business investment** and, on this front, there is ample room for improvement in the euro zone and the United States.

Governments and central banks playing their part

The state can also contribute directly to the "2025 collection" if governments, which have increasingly reined in **public investment** in favour of transfer payments and public consumption, finally reverse their course. A **better fiscal position** in the positive scenario would similarly raise investment in infrastructure.

Technological progress fuels investment boom

Real fixed capital formation in OECD countries and trend line, % yoy



Sources: Macrobond, Helaba Research & Advisory

Key interest rates would be higher in this kind of scenario. Yet as positive supply-side effects would let stronger economic growth raise capacity utilisation by less than usual, inflationary pressures (excluding higher prices for oil and other commodities) would be dampened. Moreover, in this environment, there would also be a higher **neutral interest rate**, i.e. the rate at which central banks neither restrict nor stimulate the economy. As a consequence, the restrictive effect of monetary policy would only be marginally larger than in our baseline scenario.

Overview of forecasts in the positive scenario

Economic growth picks up sharply and, instead of a mere recovery of the industrial cycle in the baseline scenario, there is a **boom**. Less regulation and greater international collaboration address some of Germany's structural problems, which enable the country's economy to grow by 2 % in 2025. In the United States, a rollback of red tape and surging innovation rapidly yield results. The US economy grows strongly in 2025.

The oil price is the main factor driving **inflation**. By contrast, a productivity spurt has a dampening effect on core inflation so that, while consumer prices rise by more than in the baseline scenario, there is no repeat of the spike in prices that occurred from 2021 to 2023. The average inflation rate in Germany reaches 3.5 %. The oil price feeds through to consumer prices, particularly in the United States, where prices also rise more quickly than in 2024.

Even though **central banks** tighten monetary policy, this only prevents the economy from overheating. The ECB lifts key interest rates back into restrictive territory towards the 4 % mark and steps up quantitative tightening. In the United States, the Fed also performs another pivot on monetary policy and raises the Fed Funds Rate back to around 5.5 %.

Prices on the **bond market** fall dramatically. As a result of rising key interest rates and higher inflation expectations, the yield on 10-year US Treasuries breaches the 5 % mark while that on 10-year German Bunds climbs as high as 4 %.

An ideal environment of deregulation, investment and innovation helps companies substantially boost their revenue. As margins remain simultaneously high, there is a double-digit growth in corporate profits. Risk appetite rebounds strongly and investors believe **equities** are significantly undervalued. The DAX exceeds 23,000 points by the end of the year.

In our positive scenario, the **gold** price plummets. On the one hand, it is dragged down by higher real interest rates; on the other hand, it is no longer in demand as a safe haven investment. The price of a troy ounce drops to USD 1,800.

Real estate benefits from buoyant growth in the wider economy and a lower level of uncertainty. Greater purchasing power and robust consumer spending support retail property, while a more rapid rise in employment drives up demand for office space. The strong growth in residential property prices seen in the years prior to the correction returns.

As geopolitical tensions subside, the euro gains ground while demand for the **US dollar** as a safe haven currency softens. Furthermore, growth surprises on the upside, especially in the euro area. This reduces the dollar's yield advantage over the single currency and the euro-dollar exchange rate rises to as much as 1.25.

Patrick Franke

Monetary policy: Loosening the belt

Central banks have their sights set on cutting key interest rates in 2025, again. Given lower inflation expectations, however, it will likely be an easier task for the ECB than for the Fed.

To date, the interest rate cutting cycle in the euro area has largely unfolded as expected. Looking to 2025, the key questions that investors are now asking are: how quickly will the **ECB** act and what level will it reduce the deposit rate to? The former will mainly have a bearing on investors' tactical behaviour, while the **key rate target** is of major strategic importance as it determines the level of capital market rates and the yield curve.

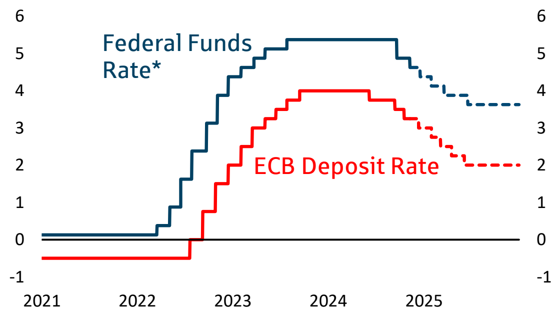
Although central bankers have already lowered interest rates, monetary policy has still had a restrictive effect in 2024. Their goal for next year is to stabilise rates at a **neutral level**, that is to say a level that neither restricts nor stimulates economic growth in the euro area. We expect further monetary easing to be accompanied by moderate inflation data. The doves in the ECB's Governing Council will likely point to sluggish growth in Germany to justify pushing for rapid interest rate cuts and a deposit rate of under **2 %**, which would be tantamount to accommodative monetary policy. However, given that the economic outlook is likely to improve again in the course of the year, it is doubtful whether they will prevail.

> *“The pace of rate cuts will depend on the data. The same can be said for how far interest rates can be cut overall.”*
> *Isabel Schnabel in the Frankfurter Allgemeine Zeitung, 22 July 2024*

Persistent **structural inflation risks** are another argument against any further loosening of monetary policy. It is true that inflation expectations have been trending lower for the past year, which is reflected in forward market rates. However, the ECB must tread cautiously in this cycle to avoid gambling away the **confidence** that it has only recently won back. If nothing else, this should be reason enough to press ahead with shrinking the balance sheet.

Central banks: Further monetary easing

Key interest rates, % (forecasts from November 2024)



* midpoint of target corridor
Sources: Macrobond, Helaba Research & Advisory

Fed: Towards neutrality

Following a zickzacking communication by the **US central bank** over 2024 it began easing a bit later than the ECB. However, the Fed then started with a 50 basis point move in September. This was followed in November by an interest rate cut of 25 basis points, which was accompanied by a meanwhile standard reference to the "**data dependency**" of future decisions.

We expect the data to prompt the Fed to lower the Federal Funds Rate by a further 25 basis points at each of the forthcoming meetings. The current cycle should then terminate in the summer of 2025 with a target range of **3.50 % to 3.75 %** which, in our view, would mark the upper end of a "**neutral zone**" in which monetary policy neither stimulates nor restricts economic growth in the medium term. At that point, the Federal Funds Rate will have fallen by 175 basis points from its previous peak.

At the same time, the Fed is set to continue with **passive quantitative tightening** despite interest rate cuts. It has announced its intention to shrink the balance sheet until, in its view, excess liquidity in the banking system has fallen to an appropriate level. This point is likely to come in the course of 2025.

%	Q1/25	Q2/25	Q3/25	Q4/25
3M Euribor	2.30	2.00	2.00	2.00
ECB Deposit Rate	2.50	2.00	2.00	2.00
Fed Funds Target Rate	3.88	3.63	3.63	3.63

Source: Helaba Research & Advisory

Ulf Krauss, Patrick Franke

Government bonds: Political developments a source of risk

Theoretically, the rate-cutting cycle should provide a relatively positive environment for bonds. However, fiscal policy and other political issues will emerge as critical factors.

Even though inflation has subsided and interest rates are falling again, the performance of German government bonds has been somewhat patchy in 2024. The fact that losses in the first half of the year were largely recouped in the last six months provided some consolation. Overall, short maturities fared significantly better than longer-dated issues. Yields on 10-year Bunds ranged from 2.0 % to 2.7 % versus around one percentage point in the previous year and as much as two and half percent points in the crisis-hit year of 2022.

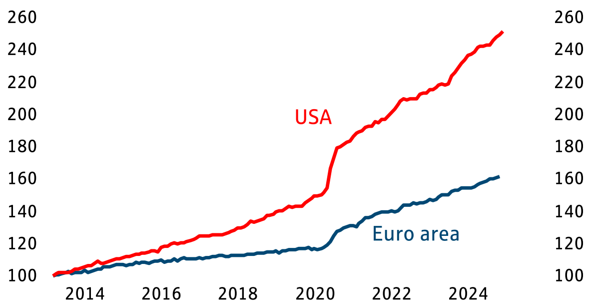
Growing political dependence – opportunities and risks close together

Are yields set the decline in 2025, leading to higher returns? The odds are actually quite good, at least in the first half of the year. Experience shows that a rate-cutting cycle tends to create a **favourable environment** for bonds. Bund yields **in the region of 2 %** are definitely within the realms of possibility – **conditions in the United States** permitting. The main caveat here is an **uncertain inflation outlook** under the new administration.

A higher **national debt**, the risk of increasing trade tariffs and politicians calling the Fed's **monetary policy independence** into question all have the potential to drive up risk premiums, especially on longer maturities. In an environment such as this, the yield on 10-year **US Treasuries** is more likely to be above than below the **4 % mark** as the year unfolds. This means that we can expect to see periods of sharp volatility in yields, particularly in the United States.

Bonds looking for buyers

Volume of outstanding government bonds, 1 January 2013 = 100



Sources: LSEG, Helaba Research & Advisory

Government spending in the **euro area** had also risen significantly during the pandemic and has not been curbed since then. While Germany's deficit stands out positively from the crowd due to its "**debt brake**", even here political developments could shift expectations towards **higher government debt** and, in turn, greater issuance. Given the recent inflation spike, it may be unwise to rely on the **ECB** to step in. Euro area central banks have scaled back their share of all outstanding euro government bonds from 42 % to 33 % since mid-2022; from the end of 2024, they will stop reinvesting any principal payments from the pandemic emergency purchase programme (**PEPP**).

%	Q1/25	Q2/25	Q3/25	Q4/25
10y Bunds	2.20	2.20	2.30	2.50
10y Treasuries	4.30	4.30	4.40	4.50

Source: Helaba Research & Advisory

Normalisation in yield curves

The inversion of the **yield curve** largely disappeared in autumn. Almost simultaneously, the 10-2 spread (yield on 10-year minus 2-year bonds) returned to a **normal,** positive range on both sides of the Atlantic. The 10-2 spread on German Bunds has been positive in around 40 of the past 50 years. Over the course of the year, support is also likely to come from a **rosier economic outlook** in Germany.

In our baseline scenario, the yield on **10-year German Bunds** is forecast to reach **2.5 %** by the end of 2025. In the first six months, yields are likely to s undershoot this level due, among other things, to still weak economic indicators and mounting hopes over further interest rate cuts. The US bond market should provide temporary, supportive conditions. The yield on 10-year **US Treasuries** is expected to close out the year **significantly above the 4 % mark.**

Ulf Krauss

Equities: Far from out of fashion

Despite the myriad challenges 2024 has thrown up, equity investors have enjoyed above-average returns. With a lot of positive news already priced in, how much upside potential remains?

In all likelihood, this past year is shaping up to be the second in a row with higher-than-average gains for equities. The US benchmarks the Nasdaq Composite and S&P 500 posted the steepest gains among the most closely watched indexes. Chinese equities, which had been languishing in the doldrums for much of the year, staged an impressive rally in the autumn, leaving indexes such as the Nikkei 225 and the DAX behind them. Globally, the tech sector was the best performer and was driven by the **megatrend of artificial intelligence** in 2024. Financial stocks follow at a considerable distance. Energy and raw materials bring up the rear.

Central banks provide equities with renewed appeal

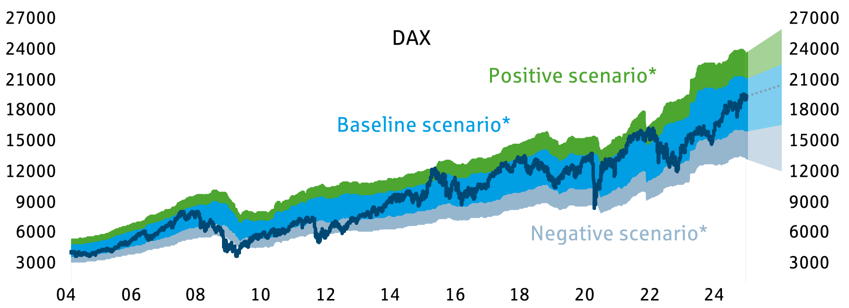
With economic indicators around the world alternating between positive and negative surprises in 2024, prompting repeated **concerns over growth or even fears of a recession**, inflation rates in most countries were, on balance, lower than expected. This constellation provided many central banks with the necessary scope to **cut interest rates**. In 2025, monetary policy easing will be sustained and will be a key factor supporting equities. However, as the year unfolds, rising equity prices will also need to be reinforced by stronger growth in corporate earnings.

DAX and Germany performing on different stages

In Germany, **perceived uncertainty** has been, and remains, especially pronounced. The war in Ukraine, challenges arising from a climate-related structural transformation and a government seen to be lacking resolve in recent months have all **weighed on sentiment** in both the population and the business community. Having initially ticked up in the spring, the ifo business climate index deteriorated again. However, early elections following the collapse the traffic-light coalition may soon usher in fresh prospects.

DAX offers attractive risk/return profile

Index, weekly prices



*bands: fair value based on profit, dividends, cash flow and book value
Sources: LSEG, Helaba Research & Advisory

However, the **German economy** plays a minor role for DAX companies as they only generate an average of around a quarter of their total revenue here. As a consequence, corporate profits remain strong despite the downturn in Germany. In this respect, German companies' **vast global footprint** acts as an advantage. On the flipside, in light of ongoing geopolitical tensions and the **punitive import tariffs** that Donald Trump has threatened to impose, this can quickly turn into a disadvantage, particularly as German companies are already struggling with the costs of the transition to sustainability and its associated structural transformation.

So far, though, equities have been **driven more by the prospect of further interest rate cuts** than by the outlook for economic growth. The historical performance of the DAX since 1965 during periods of falling interest rates underpins this view. The only years in which the DAX lost value, in some cases significantly, despite interest rate cuts were 2001/2003 and 2008/2009. Overall, the annualised return during rate-cutting cycles averaged 13 %.

Admittedly, many factors have already been priced into the DAX. On the positive side, however, the leading German index still exhibits a **moderate valuation**. Notwithstanding further gains, the DAX remains comfortably within its fair valuation range of currently between 15,800 and 21,100 points. Any further interest rate cuts would create

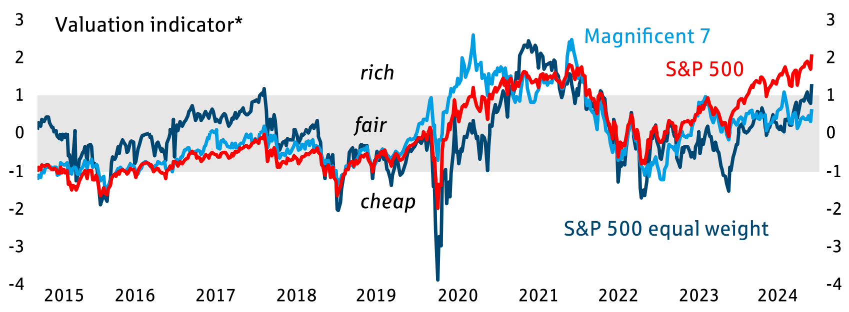
> *"Fashion fades, only style remains the same."*
> *Coco Chanel*

scope for additional valuation opportunities. Furthermore, better **prospects for global growth and corporate earnings** point to modest share price gains in 2025 - although these are likely to be "only" average. With this in mind, our **Helaba BEST indicator** suggests adopting a hold position. We expect the DAX to close 2025 at around 20,500 points.

US equities in premium price segment

It is especially true of the US market that falling key interest rates alone are insufficient to justify a sustained growth in equity prices. The valuation of US equities rose even when the Fed was still hiking rates, an unusual phenomenon for this phase. As such, even at the beginning of the rate-cutting cycle, the S&P 500 appears very expensive at first glance. However, this **high valuation is put into perspective** when considering the fact that it is primarily attributable to the multiples of the so-called "Magnificent 7" stocks, which are heavily weighted in the S&P 500. Relative to their historical performance, though, these stocks are trading within a normal range. Recently, the S&P 500 Equal Weight Index slightly exceeded the upper edge of its normal range. That does not mean US equities are a bargain. Even if dreams of an AI-powered future that are priced into the Magnificent 7, in particular, will have to pass a reality check first, the current situation is very different from that of 2021/2022. Back then, US equities were considerably overpriced – both across the board and at the top.

US equities less expensive than they appear at first glance
Standard deviations



*consisting of price/earnings ratio, price/cash flow ratio, price/book ratio and price/dividend ratio
Sources: Bloomberg, Helaba Research & Advisory

Only time will tell whether Trump, in his second term as President, manages to boost equity markets yet again with a combination of **tax cuts and deregulation**. The question of **punitive import tariffs** also poses not inconsiderable risks for US companies heavily dependent on sourcing parts from China. During Trump's first term, his "America First" slogan left an unmistakable mark on global equity markets: the S&P 500 performed significantly better than the indexes of the United States' most important trading partners. At that time, however, valuations on the US market were substantially lower than they are today. In view of this, even if Trump pursues pro-business policies, a repeat of that **outperformance is unlikely**. The S&P 500 should climb to around 6,400 points by the end of 2025.

Index value	Q1/25	Q2/25	Q3/25	Q4/25
DAX	19,750	20,000	20,250	20,500
Euro Stoxx 50	4,900	4,950	5,000	5,050
S&P 500	6,250	6,300	6,350	6,400

Source: Helaba Research & Advisory

Equities more than just an accessory

Having recorded two years of above-average performance, in 2025 **equity prices are only expected to see moderate gains**. When it comes to fashionable themes such as artificial intelligence, in particular, trying to catch up with a trend on which you have missed the boat would be unwise. For equities as an asset class, however, it appears too early in our view to be rushing for the exit given falling key interest rates and an anticipated recovery in the industrial economy in 2025.

Markus Reinwand, CFA

Gold: The Roaring Twenties

Gold is reaping the rewards of the ECB and Fed's monetary policy shift and a geopolitical turning point. In 2025, the precious metal will remain strongly underpinned by a shift in demand.

2024 will go down in the history books as a record-breaking year for gold. Nearly every week has seen the precious metal shatter all-time highs and, with an annual performance over 30 % at its peak, it even looks set to outshine equities. Yet, the rally that gold has enjoyed cannot solely be attributed to the monetary easing cycle ushered in by the Fed and the ECB. In fact, the combination of an interest rate frenzy among investors and a geopolitical risk premium is the principal driver that has propelled gold to such unprecedented heights.

> *"No nation in history has ever survived fiat money, money that did not have precious metal backing."*
> *Ronald Reagan, US President*

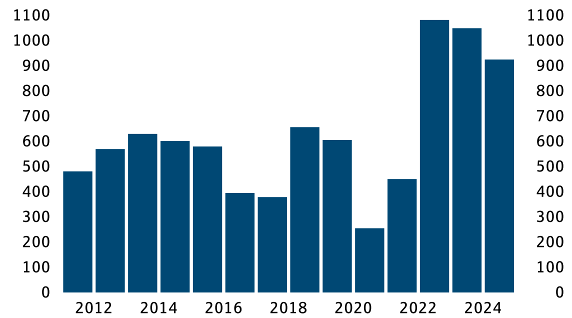
On a fundamental level, the gold price is mainly determined by investors' interest rate expectations, which is particularly the case during periods when the risk/reward perception on capital markets is balanced. As gold does not generate any income, it competes fiercely with safe government bonds. The precious metal has been capitalising on falling interest rates, i.e. declining opportunity costs, since the Fed and the ECB initiated a turnaround in monetary policy. As a consequence, gold's appeal has grown in relative terms. Having previously plummeted during the phase of rising key rates, interest from investors in Germany is now returning in the form of growing demand for gold. In 2025, though, the rationale of falling interest rates for buying gold will lose traction and no longer hold true as soon as a neutral interest rate level has been reached. Based on investors' expectations, gold is overvalued anyway. Yet, the most important factor behind its attractiveness is a geopolitical risk premium.

Geopolitical risks fuel structural shift in demand

Geopolitical risks and uncertainties reflected in the creation of new blocs among industrialised and emerging economies are fuelling a relentless demand for gold beyond the effect of monetary policy alone. Emerging markets with large reserves of US dollars most notably China, have been striving for greater autonomy since the outbreak of Russia's war of aggression against Ukraine. That is why their central banks, in particular, are increasingly buying up gold on global markets. In addition, with China grappling with economic challenges, demand from retail consumers shifting away from real estate is also growing.

Central banks increasingly buying gold

Gold in tonnes, annual amounts*



*2024 amounts up to and including Q3
Sources: Macrobond, Helaba Research & Advisory

Other significant buyers of gold include Russian and Indian consumers and the Turkish central bank. There is a long way to go before the BRICS countries are able to establish a global reserve currency to rival the US dollar. If only for this reason, they may have to rely on the conventional precious metal for the time being, ensuring that the structural shift in demand is here to stay for the foreseeable future. As a consequence, gold is set to perform quite independently of interest rates – a s a form of geopolitical risk premium.

Price / ounce	Q1/25	Q2/25	Q3/25	Q4/25
Gold in euro	2,571	2,571	2,545	2,545
Gold in US dollar	2,700	2,700	2,800	2,800

Source: Helaba Research & Advisory

Overall, we expect gold to achieve new record highs in 2025. Demand will remain high, both fundamentally and politically, as long as the rate-cutting cycle continues and elevated geopolitical risks persist. The party should gradually fizzle out as monetary easing comes to an end. Nevertheless, gold remains en vogue as a safe alternative in politically uncertain times.

Claudia Windt

Real Estate: Fallen stars

While the correction on the German real estate market has run its course, structural problems remain. More transactions will breathe new life into markets.

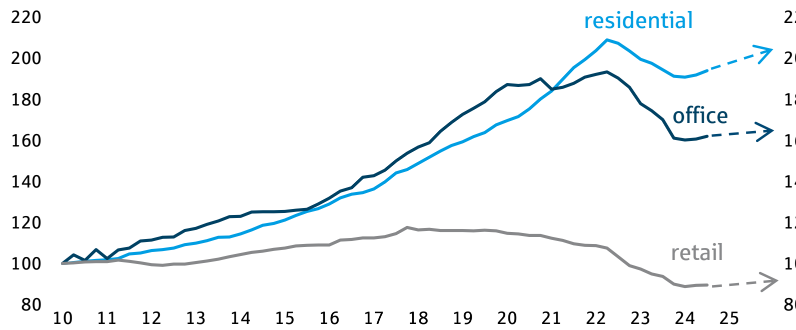
After the boom years and a subsequent correction, the German real estate market is currently in a phase of bottoming out. While the performance of each segment is driven by its specific features, a convergence in price expectations among buyers and sellers means that transactions are expected to rise across the board next year.

Lack of supply leads to higher prices on housing market

Price corrections on the German residential property market have ranged from around 9 % (vdp index) to 13 % (German Federal Statistical Office). In both cases, data series indicate a **trend reversal as early as in the course of 2024**. Corrections for properties with lower energy efficiency standards were considerably more pronounced.

Improvement in all real estate segments

vdp Property Price Index Germany, capital values, Q1 2010 = 100



Sources: vdp, Helaba Research & Advisory

The majority of previous increases in prices were **fundamentally justified** as a shortage of housing coincided with growing demand due to immigration.

The number of **completed homes** has been significantly below the German government's target of around 400,000 units per annum for many years. A sharp drop in building permits and new construction orders suggest that this figure will fall to as few as **roughly 220,000** in 2025. **Measures** such as improving options for tax relief and more flexible building standards may help to lower building costs and cut bureaucracy.

However, given further growth in Germany's population and a rapid decline in construction activity, this will be insufficient to adequately boost the supply of housing in the short term. The consequence will be a sharp rise in rents. Additionally, regulations such as **capping rent increases** serve to widen the **price gap between new and existing tenancies**. The lack of available housing also acts as a drag on overall economic growth, as it limits the **relocation** of workers to particularly attractive regions.

No improvement in affordability of home ownership in 2025

In 2024, the **affordability of home ownership** has improved. House prices bottomed out and **real wages** rose again thanks to strong wage increases and lower inflation. There was only a modest rise in **construction costs**, which had already reached a high level, while **mortgage rates** fell slightly as the ECB finally embarked on a monetary policy easing cycle.

However, **no further improvement in affordability** is anticipated in the new year. A return to the previous low interest environment is not in sight, thus financing rates are unlikely to fall significantly. Increases in real wages look set to be somewhat smaller than this year. At the same time, a number of factors suggest a modest recovery in house prices in 2025: In addition to stronger demand due to the improved affordability of homes, higher rents, a continued shortage of housing and a gradual recovery in the economy will all contribute to an expected **rise in residential property prices of around 4 %.**

Commercial real estate: Market to stabilise in new year

The correction in **office property** prices has been more pronounced than in the residential segment. However, latest indications suggest that a stabilisation is imminent. Office buildings in prime locations and of high quality remain sought after and continue to enjoy increasing rents. Despite a stable labour market, there has been a **permanent decline in demand for space** as a result of the now established working from home policy. However, this will not lead to rising vacancy rates everywhere, as the shift to more flexible working arrangements is only happening gradually and will lead to a reduction in new construction activity. The **supply of premium space in attractive locations remains limited.** As such, major differences can be observed with regard to changes in market prices, rents and vacancy rates as well as between prime properties and less attractive office space.

> *"Don't be into trends."*
> *Gianni Versace*

According to the Association of German Pfandbrief Banks (vdp), new lease agreements for **retail properties** have already risen slightly since the end of 2023. We anticipate a sideways movement on a low level in 2025 as the correction in property prices in this segment began as early as 2018 and is already well advanced.

The risk that commercial property will depreciate further has receded. At the same time, buyers that had financed purchases at the peak valuations may run into difficulties when **refinancing** due to the significantly higher interest rates. For this reason, it is likely that the insolvency rate in the sector will remain elevated. On a positive note, however, better economic prospects and an uptick in consumer spending in the new year will be instrumental in driving the recovery of the commercial real estate market.

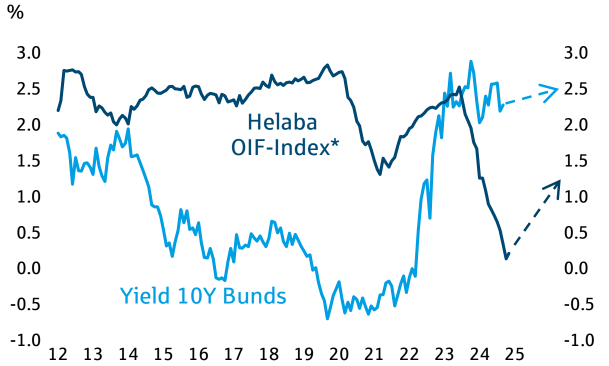
% yoy	2021	2022	2023	2024f	2025f
Open-ended fund index*	2.0	2.3	1.5	0.2	1.3
Residential real estate**	10.3	7.2	-5.0	-1.2	4.0
Commercial real estate**	-0.8	-0.4	-10.2	-5.3	1.5

* Helaba index für German open-ended funds (annual total return); **vdp price indices Germany (annual average), f=forecast; Sources: vdp, LSEG, Helaba Research & Advisory

Relative attractiveness of German open-ended property funds to remain low

The average **performance** of German open-ended real estate funds has declined sharply over the past year and, as measured by the "Helaba OIF Index", was recently hovering just above the **0 % mark**. This index tracks the average performance of nine major mutual funds from the four leading providers. Deteriorating performance as a result of depreciation in certain funds is not expected to persist into 2025, a conclusion supported among others by the latest price data from key markets, such as the UK and the United States. Over the course of next year, the average performance of open-ended funds is likely to **improve somewhat**, reaching **over 1 %** at year-end. That would be well below the long-term average of nearly 3 % and below the yield on 10-year German Bunds, which we forecast to be trading at around 2.5 % by the end of 2025.

Performance of open-ended funds set to improve



*total return, average of nine major German open-ended real estate funds
Sources: LSEG, Helaba Research & Advisory

Consequently, given the fact that they remain relatively unattractive compared to fixed-income investments, it is likely that **net outflows** from open-ended real estate funds – a trend that has persisted for over a year – is likely to **continue** in 2025. Even the key interest rate cuts by the ECB will do little to change this, as capital market rates will remain significantly higher than average fund returns. Considering that funds' **liquidity ratios** are still high and that there is a one-year **notice period** for withdrawals, we assume that they will still be able to pay out redemption requests in the new year. Additional scope for asset sales will arise from an improved market environment with higher transaction volumes.

Paul Richter

Currencies: Trump dollar without common thread

The US dollar may be exposed to greater political influence. Although that could lead to an increase in market volatility, on balance the euro-dollar rate is unlikely to change significantly.

2024 has seen no new fads emerging on currency markets: The euro-dollar exchange rate moved within a **sideways range around the 1.10 mark**, with stronger demand alternating between the US and European currencies. Yet, the macroeconomic environment has been mixed on both sides of the Atlantic, with resilient US growth standing in contrast to the absence of a recovery in the euro area. However, as both the Fed and ECB have cut their key rates to a similar extent, for a long time there was hardly any shift in the yield spreads – and the exchange rate.

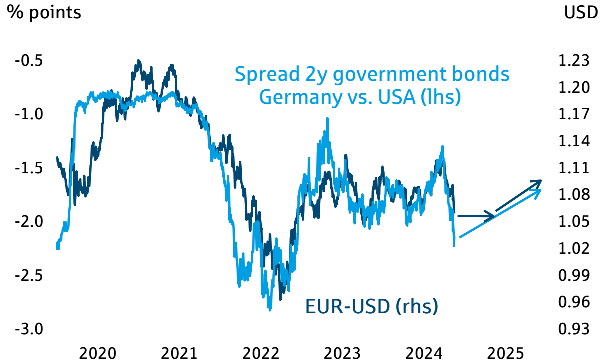
Trump and the US dollar

President Donald Trump could be about to shake things up. In theory, the **punitive import tariffs** he has threatened to impose should prompt a reaction by currency markets – i.e., currencies of countries affected would depreciate, while the US dollar would appreciate. That said, there is considerable uncertainty as to whether and when Trump's tariffs would be imposed, how high they would be and which countries they would hit. It is also important to consider that, in the second quarter of 2024 for instance, the gap between the euro area's current account surplus and the deficit in the US had reached its largest level ever – **without having any noticeable impact on the euro-dollar rate**. However, should higher inflation resulting from US trade policy and other actions substantially restrict the Fed's room for manoeuvre on interest rates, that would support the dollar – at least temporarily.

Monetary policy a crucial factor

Any speculation about a persistent growth disparity, with the associated monetary policy divergence, could temporarily lift the US currency. However, one argument **against any greater monetary easing in the euro area** is the prospect of an economic recovery. Broadly speaking, the Fed and the ECB will maintain their respective strategies to a similar extent in 2025. In the autumn, the expectation on futures markets was of fewer rate cuts from the Fed. Should this prove to be inaccurate, the US yield advantage would likely diminish, leading to a slightly higher euro-dollar rate.

US yield advantage will decline slightly



Sources: Macrobond, Helaba Research & Advisory

While announcing his desire to preserve the dollar's dominant status, Donald Trump simultaneously bemoans its strength. In terms of purchasing power parity or real effective exchange rate indices, the **dollar** is indeed trading **at a very high level**. This reflects the US trade deficit excluding petroleum products. It is debatable whether trade tariffs would do much to change this. Any appreciation of the dollar would be counterproductive as far as Trump's goals are concerned and would hardly sit well with him. Intervention on foreign exchange markets is unlikely to be particularly successful for a US administration in weakening its own currency. The Fed can indeed exert influence, but it is independent. However, the President nominates members of the Board of Governors, although they require confirmation by the Senate. As such, the Fed does not entirely operate in a political vacuum. Fundamentally, **US debt policy** (the "twin deficits") also poses risks to the dollar; so far, though, it seems to have remained immune to them. During Trump's first term in office, the greenback did not trend stronger overall.

> *"So we have a big currency problem because the depth of the currency now in terms of strong dollar/weak yen, weak yuan, is massive."*
> *Donald Trump*

Different forces are set to affect the dollar in 2025. It is possible that outliers will be more pronounced and that the US currency will see periods of temporary appreciation. Ultimately, if monetary policy on both sides of the Atlantic does not diverge significantly, the euro-dollar rate should be trading **slightly higher at around 1.10** at year-end.

Pound sterling to lose sexy edge

In 2024, the Pound sterling's performance was among the strongest of all major currencies, largely driven by a nascent economic recovery. Irrespective of declining inflation rates, the Bank of England has so far taken a more cautious approach than the Fed or ECB and this has supported the British currency. The **new Labour government**'s policies of higher taxes and public spending with a rise in the budget deficit are unlikely to have any material impact on currency markets. On the flipside, this will do nothing to make the UK currency any more attractive.

The economic recovery looks set to remain reasonably strong in 2025, although growth of 1.2 % will not pick up significantly. Inflation will not benefit from falling energy prices in 2025 with the result that the headline rate will barely decline. However, given a slowdown in wage growth, core inflation will come down, especially in the service sector. This should make the **Bank of England more receptive to further interest rate cuts**. As this is only partly priced in, unlike in other currency areas, the UK's yield advantage against the euro will presumably shrink and this should weigh on the pound. The euro-pound rate is likely to rise slightly to 0.85 by the end of 2025. Against the US dollar, the British currency will be trading at just under 1.30.

Swiss franc never completely out of fashion

On balance, 2024 saw little movement in the Swiss franc, which was able to **recoup** temporary, sharp **losses** against the euro. The Swiss National Bank (SNB) launched its interest-rate cutting cycle earlier than other central banks. Meanwhile, though, the ECB has followed suit and this accounts for shifts in the exchange rate.

vs. Euro	Q1/25	Q2/25	Q3/25	Q4/25
US dollar	1.05	1.05	1.10	1.10
Japanese Yen	158	155	158	158
British Pound	0.83	0.83	0.84	0.85
Swiss franc	0.93	0.94	0.95	0.96

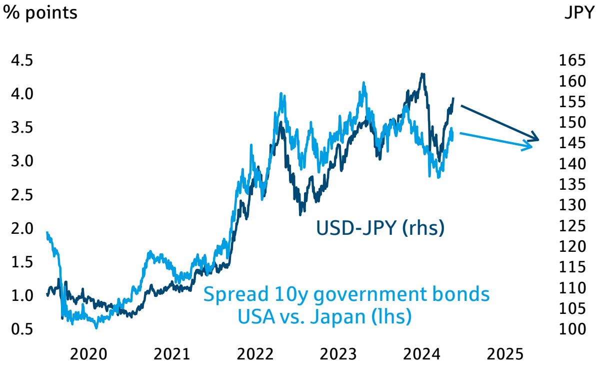
Source: Helaba Research & Advisory

With growth of around 1 %, the Swiss economy promises to deliver a solid performance in 2025 even if, unlike this year, it will not outperform the euro area. However, at just under 1 %, inflation should come in lower. As a result, the **SNB** will reduce its key rate of currently 1 % even further but remain in positive territory. The Swiss key interest rate disadvantage relative to the euro area is likely to narrow. As capital markets have largely priced this in, the franc will probably not benefit much from it. In fact, the **Swiss yield disadvantage could even widen again** towards the end of 2025. Furthermore, the SNB will intervene in currency markets to limit the potential for franc appreciation. Provided demand for the Swiss currency does not rise significantly, as a result of its safe-haven status, the euro-franc rate is likely to rise slightly by the end of 2025 but **remain below parity**.

Will the Japanese yen finally catch on?

The Japanese yen experienced a **rollercoaster ride in 2024**, which is likely to end on a negative note. Changes in **international capital market yields**, and in turn interest rate spreads, in combination with carry trades, will continue to impact yen exchange rates.

Yen's interest rate disadvantage fades



Sources: Macrobond, Helaba Research & Advisory

After a disappointing 2024, Japanese economic growth will pick up sharply next year. Inflation is likely to fall slightly to 2.0 % – a far cry from past deflationary levels. The **Bank of Japan will** therefore be able to **normalise its monetary policy** and continue making cautious interest rate hikes. As the Fed and ECB have adopted the reverse stance, the Japanese interest rate disadvantage will recede. To some extent, this should be reflected in capital market yields and **support the yen** – especially as this is already indicated by current spreads. The dollar-yen rate is likely to be trading at 144 and the euro-yen rate at 158 at the end of 2025. A stronger yen would presumably make Donald Trump happy, too.

Christian Apelt, CFA

Germany: Recovery finally arrives

Higher purchasing power will boost consumer spending in 2025. Additionally, growing international demand supports the industrial sector. Structural problems will continue to be a burden.

After two years of stagnation, a **German economic upswing** is on the cards in 2025 – albeit a belated one. The main driver will be increasing consumer spending. While consumers have set aside a larger share of wages rises in 2024 to top up their savings, they are likely to spend more again in the new year. This catalyst for growth will be complemented by global manufacturing industry, which is on track to recover in 2025 – largely attributable to less restrictive, partly even expansionary monetary policy. However, with a growth rate of 0.7 %, Germany is **still likely to underperform the euro area**.

	2024e	2025f	2026f
GDP real, % yoy	-0.1	0.6	1.5
GDP real, % yoy, working day adjusted	-0.1	0.7	1.2
Private consumption, % yoy	0.5	1.0	1.0
Government spending, % yoy	2.0	1.0	1.0
Gross fixed capital formation, % yoy	-3.0	-0.5	1.5
Investment in equipment, % yoy	-6.5	-1.5	1.5
Construction, % yoy	-3.0	-1.0	1.5
Exports, % yoy	0.5	2.5	2.0
Imports, % yoy	-1.0	2.5	2.0
Consumer prices, % yoy	2.3	2.1	2.1
Unemployment rate, %	6.0	5.8	5.2
Unemployed, thousands	2,750	2,650	2,400
Budget balance, % of GDP	-2.0	-1.5	-2.0
Current account balance, % of GDP	6.5	6.4	6.7

Sources: Macobond, Helaba Research & Advisory

Germany's persistent **structural problems** are the reason for its weaker momentum. Furthermore, **prices for electricity and natural gas** remain above their pre-crisis levels. Given that manufacturing industry in Germany accounts for a significantly higher proportion of gross value added than the average for the euro area, the German economy has suffered to a disproportionate extent from high energy prices. Additionally, export industry has been adversely affected by a rising tide of protectionism, geopolitical tensions and the associated disruption to supply chains. These factors are also putting excessive strain on Germany's export-driven economy. So, it would appear that the German economic model has fallen somewhat out of fashion. To make matter worse, **burdensome taxes and bureaucracy** have long been an impediment to economic growth in all sectors.

In the short term, **the collapse of the governing traffic-light coalition** will result in less fiscal policy intervention. However, after fresh elections have been held, the prospect of **more extensive measures from a new government** will increase. Germany is in need of substantial reform to address its structural problems and this was not something the outgoing government could be expected to deliver any longer. While the premature demise of the traffic-light coalition may create greater short-term uncertainty, in the medium term it could turn out to be a blessing for the country's economy.

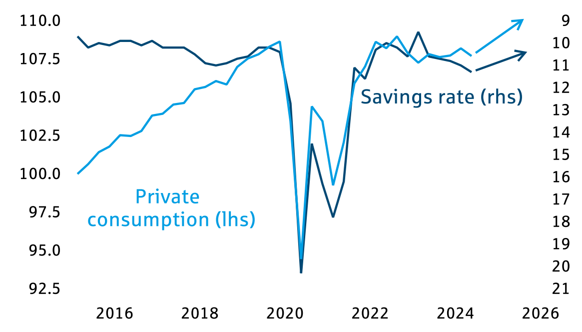
Higher consumption to stimulate growth

2023 was overshadowed by inflation, which has also been a hot topic 2024 as the turnaround in interest rates took centre stage. **In 2025, attention is likely to shift away from consumer prices** as Germany's inflation rate arrived at the target of 2.0 % in October of this year. Notwithstanding a few minor fluctuations, it should remain this way in 2025. For the year ahead, we expect an **average inflation rate of 2.1 %**.

Was inflation just a passing fad or is it here to stay?

Wage increases have already outstripped the rate of inflation in 2024 so that people have seen their real incomes grow. However, this has not yet led to any significant rise in consumer spending. Instead, consumers have used this additional income to boost their savings. Real wage growth is likely to continue in 2025 and, as the **savings rate normalizes**, this should lead to **higher levels of consumer spending**.

In addition, the number of people in work has remained on a very high level. As a result of the economic upswing, there will be a **slight decline in the unemployment rate**, such that the aggregate purchasing power will not only be fuelled by higher wages but also by a growing number of wage earners.

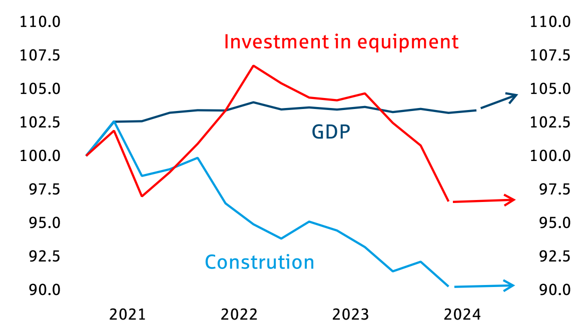


Sources: Macrobond, Helaba Research & Advisory

However, **real disposable incomes** are expected to grow at a slower pace in 2025 than in 2024. The biggest negotiated pay increases have already been implemented and there will be no additional inflation compensation bonuses. Pensions are set to rise by around 3.5 % on 1 July 2025, compared to as much as 4.6 % in 2024. Social security contributions are also scheduled to rise in the new year. In the public health insurance system, the supplementary contribution is to increase by an average of 0.8 percentage points and the long-term care insurance contribution by an expected 0.2 percentage points. Both of these increases will be split equally between employers and employees. Moreover, higher contribution assessment limits in all four social security schemes will hit higher earners. While there are plans to increase the tax-free personal allowance, for most Germans the hike in social security contributions will more than offset any reduction in income tax. As a result, while consumer sentiment should pick up, this may be **dampened** somewhat by the **increasing tax and insurance burden**. We expect consumer spending to rise by 1 % in 2025.

Gradual recovery in industrial cycle

Stronger domestic demand will not be the only factor supporting manufacturing industry. An anticipated rebound in the global industrial cycle should also help to fill the order books in the German industrial sector. On top of that, corporate funding costs have decreased compared to twelve months ago. Nevertheless, the reversal in interest rates has probably been largely priced in already such that interest rates for companies, especially for longer-term debt, are unlikely to see any significant further declines. These factors should ensure that **capital expenditure on equipment will stabilize in 2025**. Hence, while the sharp fall in equipment investments has been a drag on GDP growth in 2024, this should no longer be the case in 2025.



Sources: Macrobond, Helaba Research & Advisory

Construction sector leaves worst of crisis behind it

Capital investment in construction has been declining since 2021. However, in 2024, the **crisis in the construction sector** has probably **left its lowest point behind it**. Since peaking in November 2023, mortgage interest rates have fallen slightly and this has improved the funding situation for investors. That said, there will be no return to a low-interest environment. While capital expenditure for construction will not be a major driving force in the economy, at least it will not act as a significant drag either.

Growing international demand

Recently, real exports and imports have not generated any significant growth in the economy, but the signs are that this could change in 2025. Non-domestic demand, bolstered by a recovering global industrial economy, should increase and that would also drive a renewed expansion in German exports. Although protectionism is expected to see a resurgence under US President Trump, which could put a damper on this recovery, we assume that **cross-border trade will contribute to growth**.

Simon Azarbayjani

United States: The return of Donald Trump – more concerns than hope?

Is the US economy set to maintain its outperformance under the new administration or is it time to dress for inclement weather in 2025 – perhaps even because of the outcome of the elections?

So far, the **US economy has been humming along nicely**, with neither the surging inflation in 2021/2022 nor the drastic monetary policy tightening that followed having derailed growth. It expanded by almost 3 % in 2023 and, at 2.8 %, should post a similar performance in 2024, despite China struggling with an extended slowdown and Europe's largest economy, Germany, practically flatlining for years. None of this appears to have had any major adverse impact on the United States.

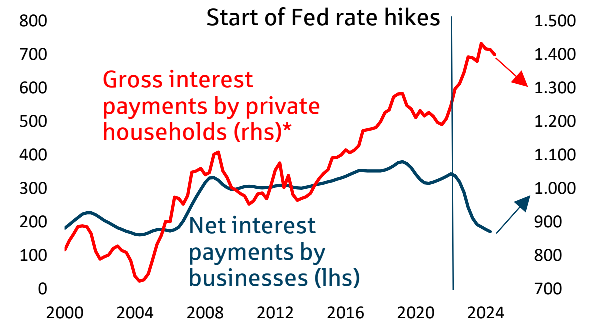
Identifying the reasons for this success story is key to understanding **whether this trend can continue in 2025.** This is a highly contentious question. Fiscal policy, having provided a substantial tailwind in 2023, stopped being a significant factor in 2024. There are no signs of a fiscal consolidation in the years ahead – quite the opposite. That said, the economic fallout of the pandemic and the political response to it are gradually subsiding. To some extent, the surprisingly strong growth in consumer spending is explained by upward revisions to household incomes and to the savings rate. By the end of 2024, it still does not look as if the "**excess savings**" that households had accumulated earlier have been exhausted.

The **housing market** has stabilised, and prices are rising again nationally. Following two years of decline, growth in real residential construction spending resumed in 2024, despite high mortgage rates compared to previous years. This is a factor supporting higher private consumption. We look for another rise in residential construction in 2025.

The **strong labour market** has also been a significant driver of consumer spending. Although the jobless rate of just over 4 % is around half a percentage point higher than the previous low in mid-2023, this uptick is not due to layoffs but to a sharp rise in immigration. Since the start of 2023, the working-age population has grown by almost 3 million. Job growth, despite gradually losing momentum, has frequently surprised to the upside. A sudden decline in 2025 seems unlikely.

Impact of monetary policy varies by sector

USD bn (annual rate)



*excluding mortgage rates. Households are net interest income recipients.
Sources: Macrobond, Helaba Research & Advisory

Impact of monetary and fiscal policy

Among other things, this is because the easing cycle that the Fed began in late summer 2024 will lift economic activity. We forecast that the US central bank will lower the key rate only to a "neutral" level in 2025 due to the limited risk of recession. However, the Federal Funds Rate is still likely to be almost 150 basis points lower on average in 2025 than in 2024. Even if it does not provide any noticeable tailwind, the **absence of a monetary policy headwind** alone will support economic growth. Given the time lag with which monetary policy affects the real economy, this will become more pronounced over the course of 2025.

However, a **counterbalance** to this is provided by a very specific combination of factors in this cycle: high levels of liquidity at many **companies**, invested short-term, combined with longer-term debt issued during the phase of low interest rates. This is likely to have delayed the negative impact of past interest rate hikes. With the majority of corporate debt having an average maturity of three to five years, this effect may partly offset the positive impact of falling key interest rates in 2025/2026.

According to the IMF, **fiscal policy** has hardly had any stimulating effect on the economy in 2024. The general government deficit was a staggering 7.6 % of GDP. On balance, though, the public sector did not act as an additional catalyst for growth. Based on current law, this is not set to change in 2025. That being said, there are indications that the **incoming administration's policies** will result in a higher deficit and, consequently, an even greater rise in the national debt. Most of Donald Trump's tax cuts from 2017, which are due to expire at the end of 2025 under current legislation, are likely to be extended. During the election campaign, Trump pledged additional relief for households and companies that would lead to even more federal borrowing. Given the lack of constraint from Congress, it is even conceivable in the medium term that the administration will test the **resilience of financial markets** – just how much fiscal profligacy can the US government get away with before it leads to significant risk premiums?

> *"To me the most beautiful word in the dictionary is tariff. It's my favourite word."*
> *Donald Trump*

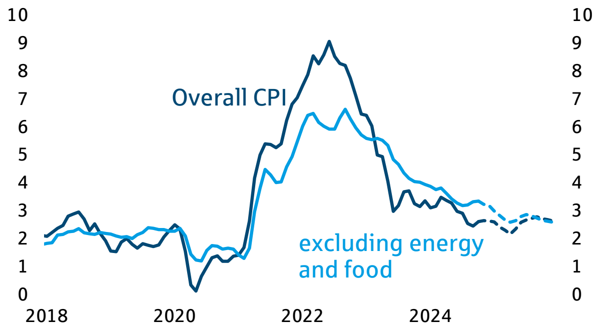
On balance, we expect real GDP to rise by 2.2 % in 2025 after an estimated 2.8 % in 2024, with quarterly **growth** initially falling **to or below the rate of trend growth** before accelerating again as the year goes on. The prospect of corporate tax cuts will support capital expenditure. However, the outlook for growth is subject to uncertainty due to geopolitical tension. We expect the latter to exert a somewhat more dampening effect on the economy, particularly in terms of investment activity.

How far will trade disputes escalate in 2025?

In this respect, the focus is on the relationship between the US and **China**, specifically, but not exclusively, in terms of **technology transfer** and **trade policy**. While the tariffs that Donald Trump has threatened to impose on the rest of the world may simply prove to be bargaining chips for "deals" in the end, it is likely that the administration will slap new **trade sanctions on China**. In this case, it is more a question of when and how much rather than if. Only time will tell whether tariffs on Chinese imports will really be raised to as much as 60 %. It is also uncertain as to how China will react and to what extent the trade war that was put on hold in 2020 will flare up again. Back then, China was not the only one to suffer from the conflict – it also negatively affected US companies and consumers.

Further core rate disinflation in 2025

Consumer prices, % yoy*



*forecasts from November 2024
Sources: Macrobond, Helaba Research & Advisory

Inflation: Cooling off but upside risks remain

As expected, the **pace of disinflation** has **slowed** in 2024, mainly as regards the headline rate. In 2025, we look for inflation to continue along its trend of the past twelve months. While headline inflation should **largely move sideways** around a level of 2 ½ %, the core rate of just above 3 % at the end of 2024 is likely to decline to around 2 ½ % over the course of 2025. That would **meet the criterion of price stability**, as far as the inflation indicator that the Fed focuses on, the PCE price index, is concerned.

However, there are **policy-related upside risks** to this forecast. In our baseline scenario, we have factored **lower immigration** into the US labour market, but not mass deportations. Wage pressures are likely to increase slightly. In the case of **trade tariffs**, which directly affect the consumer price index via prices for imported goods, there are more damaging alternatives than the one we have included in our baseline forecast. Modelling shows an increase of one to two percentage points in inflation should the US adopt a more aggressive tariff policy.

		2023	2024e	2025f	2026f
GDP, real change	% yoy	2.9	2.8	2.2	2.0
Inflation rate	% yoy	4.1	2.9	2.5	2.5
Unemployment rate	%	3.7	4.0	4.1	3.7
Budget balance*	% GDP	-6.5	-6.5	-6.0	-7.0

*Federal incl. Social Security
Sources: Macrobond, Helaba Research & Advisory

Patrick Franke

China: Geopolitical wrangling and domestic mending work

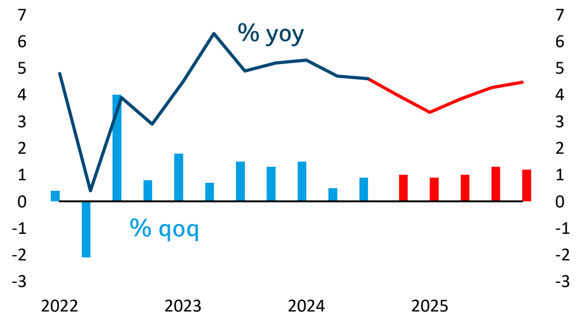
Hopes are pinned on fresh stimulus from the government after a protracted slowdown. But can Xi Jinping deliver? Will the country's dispute with the US escalate?

In the classic Chinese novel "Journey to the West", one of the characters covets the protagonist's valuable robe and attempts to steal it in violation of the law of hospitality. The episode culminates in a catastrophic fire and the death of the unsuccessful thief. This is considered an **allegory against envy, avarice and vanity**.

The debate over the extent to which China's recent pursuit of political, economic and technological hegemony represents a **legitimate historical process of catching up** with the West and to which it reflects a **nationalistic power grab** will likely continue for a long time. The days when Western countries tolerated industrial espionage and cyber-attacks, while accepting the inevitability of manufacturing industry relocating to China because of "market forces", are probably a thing of the past. As such, the only question is **how quickly and dramatically** the conflict will escalate in 2025.

Economy to find its feet in 2025

Real GDP*



*forecasts from Q4 2024

Sources: Macrobond, Helaba Research & Advisory

Donald Trump's return to the White House in January 2025 heralds **a new round** in the US-China **trade war** that has been largely dormant since the beginning of 2020. Higher US tariffs for Chinese products and retaliatory measures from China are very likely. This will have an adverse impact on export-focused industries and make finding a solution to weak domestic demand all the more urgent.

Challenging but easier to solve: Domestic economic problems

This is because, in addition to external economic conflicts, China is still struggling with a **real estate crisis** at home that is paralysing construction activity and weighing heavily on consumer spending. In our view, the odds are good that the government will succeed in containing the crisis. That does not mean, however, that the country's numerous structural and macroeconomic woes will simply vanish overnight. They will continue to hold back economic growth.

> *"The United States is the biggest threat to our country's development and security"*
> *Xi Jinping*

Ultimately, **Chinese growth should stabilise** in 2025. But the figures will send out conflicting signals. Although the average expansion in GDP of 4.0 % is likely to be lower than 2024 (4.5 %), quarterly number should clearly exceed the weak period over the spring and summer of 2024. The year-on-year growth rate is expected to initially fall before rebounding over the course of the year.

Central bank can keep its foot on the gas

Despite many references to a purported deflation in China, the more accurate term for the current situation there, at least at the consumer level, would seem to be "**price level stability**". At 1.2 %, the consumer price index should rise at a slightly faster pace in 2025 than in 2024 provided that domestic demand gradually picks up. However, for the time being, no arguments against additional monetary stimulus will come from inflation.

		2023	2024e	2025f	2026f
GDP, real change	% yoy	5.1	4.5	4.0	4.0
Inflation rate	% yoy	0.2	0.4	1.2	2.0
Unemployment rate*	%	5.2	5.2	5.0	4.9
Budget balance	% GDP	-6.9	-7.4	-7.8	-7.8

*"Surveyed". Sources: Macrobond, Helaba Research & Advisory

Patrick Franke

Gross domestic product and inflation

	Gross domestic product Real change, % yoy				Consumer prices Change, % yoy			
	2023	2024e	2025f	2026f	2023	2024e	2025f	2026f
Euro area	0.5	0.8	1.2	1.3	5.4	2.4	2.2	2.2
Germany	-0.1	-0.1	0.7	1.2	5.9	2.3	2.1	2.1
France	1.1	1.2	1.2	1.4	5.7	2.3	2.1	2.1
Italy	0.8	0.5	1.0	1.0	5.9	1.1	2.2	2.2
Spain	2.7	3.0	2.2	1.6	3.4	2.8	2.4	2.4
Netherlands	0.1	0.9	1.5	1.3	4.1	3.0	2.3	2.5
Austria	-0.8	-0.5	1.0	1.3	7.8	3.0	2.3	2.3
Sweden	-0.1	0.5	2.0	2.5	8.5	2.8	1.0	1.7
Poland	0.1	2.5	3.0	3.5	11.4	3.8	5.0	3.0
Czech Republic	0.0	1.0	2.3	2.7	10.7	2.5	2.5	2.3
Hungary	-0.8	0.5	2.3	3.3	17.6	3.7	4.0	3.5
United Kingdom	0.3	0.9	1.2	1.5	7.3	2.5	2.5	2.5
Switzerland	1.2	1.0	1.0	1.2	2.1	1.1	0.8	1.0
USA	2.9	2.8	2.2	2.0	4.1	2.9	2.5	2.5
Japan	1.7	-0.3	1.3	0.8	3.3	2.5	2.0	2.0
Asia ex Japan	4.9	4.4	4.1	4.1	2.0	1.7	2.1	2.5
China	5.1	4.5	4.0	4.0	0.2	0.4	1.2	2.0
India*	8.2	6.8	6.5	6.1	5.7	4.8	4.4	4.2
Russia	3.0	3.0	2.0	1.8	5.9	7.0	4.5	3.2
Turkey	4.5	2.4	3.7	3.5	53.9	55.0	27.0	9.0
Latin America**	2.1	1.8	2.4	2.4	18.3	25.8	8.1	5.7
Brazil	2.9	2.8	2.5	2.0	4.6	4.0	3.5	3.0
World	3.1	2.9	2.8	2.8	5.0	4.5	2.9	2.7

*India: Financial Year; ** Latin America ex Venezuela due to hyperinflation; f=forecast, e=estimate; GDP growth working-day adjusted if available
Sources: Macrobond, LSEG, Helaba Research & Advisory

Financial markets forecasts

	Change from end of year	latest*	Helaba forecast for end of period...			
			Q1/2025	Q2/2025	Q3/2025	Q4/2025
Interest rates	basis points	%				
ECB refinancing rate	-110	3.40	2.65	2.15	2.15	2.15
ECB deposit rate	-75	3.25	2.50	2.00	2.00	2.00
Overnight rate €STR	-72	3.16	2.45	2.00	2.00	2.00
3M Euribor	-89	3.02	2.30	2.00	2.00	2.00
6M Euribor	-108	2.78	2.20	2.05	2.05	2.05
2y Bunds	-24	2.17	2.00	2.00	2.10	2.10
5y Bunds	27	2.22	2.05	2.05	2.15	2.30
10y Bunds	37	2.39	2.20	2.20	2.30	2.50
2y swap rate	-53	2.27	2.10	2.10	2.20	2.20
5y swap rate	-14	2.29	2.20	2.20	2.30	2.45
10y swap rate	-14	2.35	2.30	2.30	2.40	2.60
20y swap rate	-18	2.34	2.05	2.05	2.15	2.35
30y swap rate	-23	2.11	2.05	2.05	2.15	2.35
Fed funds target rate	-75	4.63	3.88	3.63	3.63	3.63
10y Treasuries	57	4.45	4.30	4.30	4.40	4.50
Equities	in local currency, %	index				
DAX	13.4	19,003	19,750	20,000	20,250	20,500
Euro Stoxx 50	4.8	4,740	4,900	4,950	5,000	5,050
Dow Jones	16.6	43,958	45,400	45,800	46,200	46,500
S&P 500	25.5	5,985	6,250	6,300	6,350	6,400
Nikkei 225	15.7	38,722	39,900	40,300	40,700	41,000
Gold / crude oil	%					
Gold €/oz	30.3	2,436	2,571	2,571	2,545	2,545
Gold $/oz	24.7	2,573	2,700	2,700	2,800	2,800
Brent crude $/barrel	-6.2	72	80	82	82	83
Currencies	vs. euro, %	exchange rate				
US dollar	4.5	1.06	1.05	1.05	1.10	1.10
Japanese yen	-5.2	164	158	155	158	158
British pound	4.3	0.83	0.83	0.83	0.84	0.85
Swiss franc	-0.8	0.94	0.93	0.94	0.95	0.96

*13/11/2024

Sources: Bloomberg, Helaba Research & Advisory

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