

Quarterly Outlook

How might investors manage ongoing policy uncertainty as the new normal?

June 2025



Market developments and other events

In Q2, early-April 'Liberation Day' tariffs sent equities tumbling and caused elevated volatility. Towards the end of the quarter, trade policy concerns faded fueling a rebound in capital markets supported by the 90-day tariff pause, the US-UK trade deal, and early progress on a potential US-China trade deal. The frontloading of US imports anticipating a rise in trade tariffs, resulted in a Q1 US GDP contraction, while euro area growth stayed steady yet sluggish. Current economic activity seems to hold up relatively well as reflected by coincident nowcast indicators.

Credit spreads tightened and equities ended the quarter positively, especially US and emerging markets equities showed strong local currency returns following a weak dollar. Significant geopolitical tensions, following the war between Iran and Israel, had a muted impact on markets, while gold propelled to record highs and oil drifted lower into quarter-end.

NATO's commitment to raise defense spending towards 5% of GDP offers a gradual fiscal boost for Europe, while US Senate approval of the Reconciliation Bill revives deficit concerns both putting upside risks for medium-term inflation. With headline inflation slipping below target, the ECB cut interest rates twice to 2%. The US Fed kept policy unchanged for a fourth straight meeting, preferring a wait-and-see stance to see the inflation impact of US trade tariffs.



Outlook for growth, inflation, and interest rates

Despite some tangible progress in US trade talks, uncertainty about tariffs remains elevated with most negotiations still unresolved. Moreover, trade tariffs will likely remain higher when compared to the end of 2024, pointing towards a more durable shift in global trade relations and putting some drag on global economic activity, with the added risk that duties could snap back to the 2 April schedule if talks stall.

With peak tariff tensions fading, the growth outlook improves. However, short-term growth is anticipated to remain below trend owing to headwinds from ongoing trade and policy uncertainty.

The impact of trade tariffs on inflation remains to be seen. With firms stocking up ahead of tariff deadlines potential rising costs could be passed on to consumers later in the second half of the year. In the medium term, inflation is expected to stabilize somewhat above central bank target, amongst others, owing to anticipated upward fiscal spending pressures associated with elevated geopolitical risks.

For the coming years, long rates are expected to move around their recent levels for most developed markets. This reflects higher for longer dynamics as inflation is anticipated to remain somewhat above central bank target.



Outlook for financial assets

The economic cycle outlook improves, driven by a recovery in investor confidence despite ongoing (trade) policy uncertainty. Nevertheless, the short-term US equity outlook has somewhat deteriorated after a strong rebound in the second quarter, while the short-term outlook for European equities improves partially compensating for previous underperformance.

The government bond return outlook weakens for the UK and Germany due to decreased long rates amid elevated market volatility. Following the compression on government yields, the short-term corporate credit return outlook also deteriorates for most countries. For high yield, lower spreads amid fading trade concerns also contribute to a weakening outlook.

The outlook for financial assets remains clouded by elevated volatility and downside risk due to (trade) policy uncertainty and geopolitical tensions. Tariffs imposed by major global players, particularly the US and China, heighten economic risks and may escalate into a broader trade conflict. While trade tensions have somewhat eased, the recently declared Israel–Iran ceasefire is still being tested and a quick resolution of the war in Ukraine seems unlikely.

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