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It’s a mad world

I recently took out an old classic from my record collection: “Mad World” by Tears for Fears. Is there a better description of the current state of the global economy?

A breathtaking pace

The world is still trying to keep up with the new old US president, Donald Trump. Regardless of where you stand on the substance of the announced policy measures, the pace at which the US administration has come off the starting blocks is breathtaking. Interestingly, not every initiative or announcement has made it into actual policy measures (yet), and only time will tell whether sprinting into a marathon is a winning strategy. However, the series of potential trade measures, from outright tariffs to reciprocal tariffs or even targeting the VAT of trading partners, has kept politicians and analysts around the world very busy.

The actions of the Department of Government Efficiency are impressive for those who always wanted transparent disruption and scary for those with an interest in 20th-century history like me. For everyone interested in what is still to come, I can only recommend reading the Project2025 plans, a source of valuable information many Europeans must have overlooked. Otherwise, they wouldn’t be so surprised by everything that is currently happening.

Europe appears paralysed by fear

Interestingly, the domestic economic policy agenda of tax cuts and increased energy production has not taken off yet. Instead, consumer confidence has started to weaken, while big corporates recently announced significant investments in the US, investments Europe would also have liked to receive. However, instead of strengthening its domestic economy, Europe still looks petrified, terrified by the looming tariff threat and even more scared by the quickly changing geopolitical reality.

With the US and Russia negotiating a possible end to the war in Ukraine, with barely any involvement of Ukraine or Europe, and a looming withdrawal of US military, Europe urgently needs to step up its game. That's on security, defence, and strategic autonomy. The risk I see is that Europe falls into the same trap as it did after the euro crisis: producing many reports with excellent analysis and policy recommendations but being too easily satisfied with baby step progress and accentuating problems rather than thinking boldly.

Here's a little quiz: How many European presidents’ reports on strengthening the monetary union have been released since 2014?

Answer: Way too many.

After the euro crisis, it was Jean-Claude Juncker who said that all European government leaders knew what to do (i.e., eventually, nothing else than a fully-fledged fiscal and political union as well as a capital markets union). But they didn't know how to get re-elected if they did what had to be done. To paraphrase Mr Juncker, right now, most European government leaders also know what to do (i.e., increasing defence spending substantially), but they don’t know how to pay for it.

If Europe really wants to defend itself, it needs to increase military spending fast, from the current 2% of GDP to around 4% of GDP. The problem is that not every country has a domestic defence industry that would benefit from higher spending. This is why a European approach would make more sense. However, Europe is likely to follow a national approach first, allowing some flexibility in the fiscal rules but definitely putting more pressure on debt sustainability.

It makes me want to shout

How much European policy discussions are dominated by public finance concerns can hardly be better seen than in Germany, where initial hopes for imminent fiscal stimulus have already given way to political horse-trading only a few days after the elections. A special fund for more defence spending seems likely. A special fund for infrastructure investments still seems a distant dream.

And there's the rub. After five years of economic stagnation, an investment gap of some 600 billion euros, and a long list of structural challenges, how many wake-up calls does Europe need? In "Mad World," Tears for Fears sings about people running in circles. Did they have Europe in mind? Sometimes, I wish for a bit more "promises made, promises kept" in Europe. Or to say it again with Tears for Fears: “Shout, shout, let it all out, these are the things I can do without, come on, I’m talking to you, come on.”

Watch: Three key areas we’ll be watching closely in March

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Our main calls

Trade tensions are set to increase with upcoming US tariffs on EU and China. We see only little room or willingness for significant deals.

Geopolitical uncertainty has increased, despite or maybe even due to the US-Russia talks on Ukraine. We see increased defence spending in Europe over the coming years but continued uncertainty and disagreement on how to pay for additional spending.

Near-term strength in the **US economy** is likely to persist, but higher Treasury yields and the consumer being hit from tariffs is likely to usher in cooler economic growth. We expect the Federal Reserve to cut rates twice this year.

In the **eurozone**, signs of a bottoming out have increased but with looming tariffs and continued geopolitical uncertainty, we stick to our call of sluggish growth in the first half of the year. Despite inflation remaining too high, we expect the European Central Bank to continue cutting rates to at least 2% by the summer.

In **Germany**, we expect complicated and cumbersome coalition talks. Eventually, the next government will deliver some tax cuts and investments as well as higher defence spending but outright changes to the debt brake are unlikely. We see the economy regaining momentum in second half of the year but competitiveness concerns will remain.

We expect **China** to stick with its “around 5%” growth target again in 2025, a show of confidence that external headwinds might not derail growth. We continue seeing stronger Chinese retaliation to US tariffs than many expect.

We've taken a cold look at our 5.5% call for the **US 10yr** and have on balance decided to trim it to 5%. A combination of Doge, Treasury Secretary Scott Bessent and talk of SLR adjustment(s) have managed to tame the prior de-rating of Treasuries versus the risk free rate.

The **dollar** has come under some pressure on the back of the rerating of the US growth outlook and expectations that the Russia-Ukraine conflict is nearing an end. However, we expect US tariffs to regain centrality and drive the dollar sustainably higher.

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ING global forecasts

	2024					2025F					2026F				
	1Q24	2Q24	3Q24	4Q24F	2024F	1Q25F	2Q25F	3Q25F	4Q25F	2025F	1Q26F	2Q26F	3Q26F	4Q26F	2026F
United States															
GDP (% QoQ, ann)	1.6	3.0	3.1	2.3	2.8	2.7	2.2	1.6	1.4	2.4	1.6	1.7	1.8	1.8	1.6
CPI headline (% YoY, aop)	3.2	3.2	2.6	2.7	3.0	2.8	2.8	2.9	3.4	3.0	3.0	3.0	2.6	2.3	2.7
Federal funds (%, eop)	5.50	5.50	5.00	4.50	4.50	4.50	4.50	4.25	4.00	4.00	3.75	3.75	3.75	3.75	3.75
3-month SOFR rate (%, eop)	5.40	5.40	5.00	4.40	4.40	4.50	4.30	4.00	4.00	4.00	3.75	3.75	3.75	3.75	3.75
10-year interest rate (%, eop)	4.25	4.40	3.80	4.60	4.60	4.50	4.75	5.00	5.00	5.00	5.00	5.00	5.00	5.00	5.00
Fiscal balance (% of GDP)					-6.9					-6.7					-6.4
Gross public debt / GDP					99.6					100.9					103.1
Eurozone															
GDP (% QoQ, ann)	1.2	0.7	1.5	0.2	0.7	0.5	0.8	1.0	1.1	0.7	1.4	1.6	1.7	1.7	1.3
CPI headline (% YoY, aop)	2.6	2.5	2.2	2.3	2.4	2.5	2.4	2.3	2.3	2.4	2.2	2.2	2.2	2.2	2.2
ECB Deposit Rate (%, eop)	4.00	3.75	3.50	3.00	3.00	2.50	2.00	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75
3-month interest rate (%, eop)	3.90	3.70	3.25	2.85	2.85	2.40	1.90	1.75	1.80	1.80	1.80	1.80	1.90	1.90	1.90
10-year interest rate (%, eop)	2.30	2.60	2.10	2.36	2.36	2.50	2.60	2.70	2.80	2.80	2.80	2.80	2.80	2.90	2.90
Fiscal balance (% of GDP)					-3.3					-3.3					-3.2
Gross public debt/GDP					90.9					89.8					89.6
Japan															
GDP (% QoQ, ann)	-1.9	3.0	1.7	2.7	0.1	0.4	1.2	1.2	0.8	1.4	1.2	1.2	1.2	1.2	1.1
CPI headline (% YoY, aop)	2.5	2.7	2.8	2.9	2.7	3.7	3.3	2.7	2.0	2.9	1.6	1.6	1.9	2.0	1.8
Target rate	0.10	0.10	0.25	0.25	0.25	0.50	0.75	0.75	1.00	1.00	1.00	1.25	1.25	1.25	1.25
3-month interest rate (%, eop)	0.26	0.30	0.43	0.62	0.62	0.80	1.00	1.10	1.20	1.20	1.20	1.40	1.45	1.45	1.45
10-year interest rate (%, eop)	0.73	1.06	0.86	1.10	1.10	1.40	1.40	1.50	1.50	1.50	1.75	2.00	2.00	2.00	2.00
Fiscal balance (% of GDP)					-7					-7					-7
Gross public debt/GDP					257					260					263
China															
GDP (% YoY)	5.3	4.7	4.6	5.4	5.0	4.4	4.8	4.8	4.5	4.6	4.5	4.6	4.0	3.9	4.2
CPI headline (% YoY, aop)	0.0	0.3	0.5	0.2	0.2	0.4	0.7	0.8	1.2	0.8	1.1	0.7	1.0	2.0	1.2
7-day Reverse Repo Rate (% eop)	1.80	1.80	1.50	1.50	1.50	1.40	1.40	1.30	1.20	1.20	1.20	1.10	1.00	1.00	1.00
3M SHIBOR (% eop)	2.16	1.92	1.84	1.85	1.85	1.70	1.65	1.60	1.50	1.50	1.50	1.45	1.45	1.45	1.45
10-year T-bond yield (%, eop)	2.30	2.21	2.20	2.00	2.00	1.70	1.65	1.55	1.60	1.60	1.60	1.70	1.80	1.85	1.85
Fiscal balance (% of GDP)					-5.0					-5.50					-5.5
Public debt (% of GDP), incl. local govt					121					135					145
United Kingdom															
GDP (% QoQ, ann)	3.4	1.8	-0.1	0.4	0.9	2.1	1.8	1.2	0.9	1.2	0.8	0.8	1.0	1.0	1.0
CPI headline (% YoY, aop)	3.5	2.1	2.0	2.5	2.5	2.8	2.9	3.3	3.2	3.1	2.8	2.3	2.3	2.3	2.4
BoE official bank rate (%, eop)	5.25	5.25	5.00	4.75	4.75	4.50	4.25	4.00	3.75	3.75	3.50	3.25	3.25	3.25	3.25
3-month interest rate (%, eop)	5.25	5.05	4.80	4.55	4.55	4.45	4.20	3.95	3.70	3.70	3.45	3.20	3.20	3.20	3.20
10-year interest rate (%, eop)	3.95	4.20	4.00	4.25	4.25	4.50	4.50	4.60	4.60	4.60	4.50	4.50	4.50	4.50	4.50
Fiscal balance (% of GDP)					4.5					3.6					3.4
Public sector net debt (FY, %)					100.1					99.7					100.1
EUR/USD (eop)	**1.08**	**1.08**	**1.12**	**1.05**	**1.05**	**1.02**	**1.00**	**1.00**	**1.02**	**1.02**	**1.02**	**1.02**	**1.03**	**1.05**	**1.05**
USD/JPY (eop)	**151**	**160**	**143**	**155**	**155**	**150**	**152**	**155**	**155**	**155**	**155**	**153**	**150**	**150**	**150**
USD/CNY (eop)	**7.22**	**7.26**	**7.01**	**7.25**	**7.25**	**7.28**	**7.32**	**7.35**	**7.40**	**7.40**	**7.50**	**7.45**	**7.40**	**7.35**	**7.35**
EUR/GBP (eop)	**0.86**	**0.87**	**0.84**	**0.83**	**0.83**	**0.83**	**0.83**	**0.84**	**0.84**	**0.84**	**0.84**	**0.85**	**0.85**	**0.85**	**0.85**
ICE Brent - US$/bbl (average)	**82**	**85**	**79**	**74**	**80**	**76**	**74**	**75**	**71**	**74**	**67**	**69**	**73**	**70**	**70**
Dutch TTF - EUR/MWh (average)	**28**	**32**	**36**	**43**	**35**	**50**	**45**	**42**	**44**	**45**	**37**	**30**	**30**	**34**	**33**

Source: ING forecasts

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The latest upside and downside risks to our global outlook

All of the latest from our team on what could go right or wrong for the global economy over the coming months

Five upside risks

1. Eurozone embarks on major fiscal expansion

After complicated coalition talks, the new German government eventually decides on a special fund to boost infrastructure investment. This fund comes on top of earlier agreed special funds for defence spending. At the European level, there is an agreement on a European Defence Fund.

2. Trade war delayed – tariffs largely avoided

Given the significance of the US sales market, countries facing potential US tariff action make significant concessions. This dynamic ultimately results in improved global trade relations, as countries reduce their tariff rates in line with the Most Favoured Nation (MFN) principle. Consequently, the favourable tariff reductions extended to the US are also applied to all other trading partners. This process not only fosters a more open and competitive global market but also encourages international cooperation and economic stability.

3. European consumer renaissance

In contrast to the United States, the European savings ratio is some three percentage points above its long-term average. Admittedly there's some debate about how much of that is in liquid bank deposits. But with the jobs market strong and real wage growth still positive, the deployment of that savings buffer and a return to the pre-Covid average could lift growth by more than a percentage point. The issue currently is that consumer confidence is weak – but if that changes, the European consumer is a major source of potential upside.

4. Trump unshackles America

Optimism that US President Donald Trump's tax cuts and deregulation plans can deliver meaningful growth encourages businesses to resume hiring and investment while immigration controls constrain labour supply, keeping wage growth robust. Tariff threats succeed in opening up foreign markets to US companies while also prompting announcements of foreign companies investing in US production facilities. Tariffs are subsequently watered down and look less troubling for inflation and growth. Bond markets give Trump the benefit of the doubt on fiscal sustainability, limiting the upside for Treasury yields. In turn, they present less of a headwind to growth than under our base case.

5. Chinese policymakers deliver at Two Sessions

Markets are expecting stronger policy support this year to help boost domestic demand to offset what will likely be a weaker external environment, but what this policy could look like is still unclear at this point. The Two Sessions will give policymakers a chance to communicate this year's policy focus – the growth target will be the primary focus, but more details on what form fiscal stimulus could take will also be watched closely. Clear and actionable policy direction could go a long way in bolstering market confidence.

Five downside risks

1. The US jobs market capitulates

Fears of a jobs market recession have all but faded since last summer's surprise pickup in the unemployment rate. But roughly 90% of job creation over the past two years have been in just three sectors: private health and education, leisure and hospitality and government. That suggests the underlying story in the jobs market is less healthy than the headline numbers indicate. Until now, the US consumer has been unrelentingly strong, helped by higher income households. A surprise rise in redundancies could quickly change that.

2. President Trump returns to 60% tariffs on China and 20% on everyone else

Based on the US having imported $3.3tr goods in 2024, such aggressive tariffs raise over $800bn in revenue. Despite assurances that "foreigners will pay", importers and retailers experience higher costs and this is passed onto consumers. In a worst-case scenario of zero substitution for American made products and full cost pass through to the consumer this averages nearly $2500 for every American and severely erodes household spending power. Even in a less extreme scenario, with some switching to American products and some profit margin compression, consumer spending cools due to the pressure on household finances. At the same time, reciprocal tariffs from foreign trading nations hurt the competitiveness of US exporters.

3. Oil prices spike on sanctions risk

Stricter enforcement of sanctions against Iran – and if Biden's departing sanctions against Russia turn out to be effective – will not only erase the surplus we expect for this year but push the market into a fairly large deficit, with as much as 1.7m b/f of supply at risk. The market is then left relying on OPEC+ to fill the gap, but with its fiscal breakeven levels above current prices, it will be in no rush to bring supply back quickly.

4. Broken transatlantic relationship weighs on Europe

US tariffs on European goods, particularly automotives, further dent the very fragile recovery and add to Europe's industrial worries, leading to a faster turning of the labour market. At the same time, a deal on Ukraine between the US and Russia, with subsequent withdrawal of US troops from Europe, brings new geopolitical uncertainty. In turn, consumption and investments are held back.

5. China-US negotiations fall through

While there have been reports of regular dialogue between working level officials of the two nations, so far it has been a little surprising that Chinese leader Xi Jinping and Trump have yet to have a formal high-level discussion. Early restraint from both sides on tariffs gives room for de-escalation, but this is far from a given. The clock is ticking to find a new trade deal or framework ahead of early April, when an investigation on China's Phase One Trade Agreement purchases will be published and Trump's moratorium on the TikTok ban will expire. An additional point of concern is reports that the US is now asking Mexico to also add tariffs on China. If this sort of coordinated attack on China is expanded, there are risks for an even more damaging global trade war.

Europe to face first major 'America First' trade policy test

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European leaders are facing a major test later this month regarding how to deal with the renewed 'America First' trade policy. They may be better acquainted with how President Trump does business this time around, but speed and power struggles are just two things to worry about

EC President Ursula von der Leyen, with the Danish, Icelandic and Spanish Prime Ministers in Kyiv

EU faces first major challenge as steel and aluminium tariffs return

12 March marks the first test for the European Union in tackling the renewed US "America First" trade policy. On this date, tariffs of 25% on steel and aluminium will once again come into force, with US President Donald Trump citing a surge in imports and a decrease in US capacity utilisation as his reasoning. During his first term as president, Trump announced tariffs of 10% on aluminium and 25% on steel imports, effective 23 March 2018, under Section 232, citing national security concerns. Back then, multiple deals eventually ended tariffs for many countries.

While steel and aluminium exports from the EU to the US account for only approximately 1% of total goods exports to the US, the European Commission stated that such measures would not go unanswered and would be met with "firm and proportionate countermeasures".

The EU's 2018 response to US section 232 tariffs

Back in 2018, the EU responded to the US Section 232 tariffs on steel and aluminium with immediate retaliatory countermeasures ranging from 10-25% on motorcycles, agricultural products, bourbon, clothes, and steel, among others. Additional countermeasures were to be imposed after three years if no settlement was reached.

On 31 October 2021, the US and the EU announced a multifaceted agreement to address the tariffs imposed during the Trump administration, replacing tariffs with a tariff rate quota (TRQ) system. This system allows a certain volume of EU steel and aluminium to enter the US market duty-free, with any imports above these quotas subject to the original tariffs. The EU also agreed to suspend its retaliatory tariffs on various US exports, including American whiskey and motorcycles, until 31 March 2025, while the US prolonged the TRQs on EU products until 31 December 2025. If the EU is hit

by additional tariffs from March, it could simply reinstate its retaliatory tariffs on US exports at the end of March.

Lessons in strengthening EU trade enforcements learned from Trump's first presidency

And answering to US section 232 tariffs is easier today for the EU than it was back then. Learning from the first Trump presidency, the EU has sharpened its Trade Enforcement Regulation, enabling the EU to suspend or withdraw concessions or other obligations under international trade agreements when third countries breach these agreements and affect the EU's commercial interests, allowing the EU to take countermeasures.

The EU Commission also acts on behalf of its members in this case, without requiring a subsidiarity check by national parliaments first. However, the scope of striking back remains narrow, as dispute settlement or resolution mechanisms need to prove ineffective, or trading partners need to be non-cooperative or fail to offer compensation. In turn, only the US safeguards resulted in immediate rebalancing measures under the terms of the Enforcement Regulation, and it remains unclear whether Trump's other tariff threats would provide a legal basis for using this instrument for striking back.

The EU's trade playbook: countermeasures, negotiations, and economic fortification

But given the in-depth reviews of US trade policy, tariffs on steel and aluminium will not mark the end of the tariff saga. They are only the beginning. So, what other options does the EU have at its disposal?

Negotiation strategies

As in 2018, the EU could consider increasing LNG purchases from the US, boosting EU defence spending, and purchasing more US military products. Additionally, it could offer to reduce import tariffs on US automotives to achieve a level playing field. However, the US is already a key supplier of LNG and military equipment to the EU. It's important to note that while the European Commission holds sole responsibility for trade policy negotiations, it cannot force member states to purchase goods from specific suppliers, meaning some purchases may still fall through. Moreover, this time around, Trump might not be as easily persuaded into making such a deal.

The trade bazooka: ACI

At the end of 2023, the EU put a trade bazooka in place, the so-called EU Anti-Coercion Instrument (ACI). It could be invoked if Trump attempts to impose duties on a specific member state, provided it gets the green light from a “qualified majority” of 15 out of the 27 member states, representing at least 65% of the bloc’s population. However, any reaction under the ACI would take some eight weeks, and it can't be triggered if Trump’s tariffs are not punitive, or their adoption is made conditional on policy changes performed by the EU and its member states. The EU’s first problem, then, is speed.

Retaliatory measures

Next to retaliatory tariffs on products from US swing states (e.g., soybeans, bourbon), Europe could impose export tariffs on goods that are of strategic importance to the US, such as chemically and pharmaceutically important goods. But this is not without risk, as the US could answer in a similar way, curbing chemical exports to Europe. The ultimate retaliation would be a digital services tax.

Strengthening the domestic economy

Ultimately, Europe should finally strengthen its domestic economy and should focus on implementing as many proposals from the Draghi report as possible. Reducing dependency on the US by investing in domestic military industries, deregulating the tech sector, and stepping up significant investments in infrastructure and innovation will

enhance the EU's resilience and competitiveness on the global stage – the ultimate retaliation.

Europe is better prepared, but speed and power struggles remain a problem

The EU is better prepared to tackle Trump 2.0, but it still faces a complex challenge in countering potential US tariffs. While the bloc has several options at its disposal – including retaliatory tariffs on key US exports and the implementation of a digital services tax – the effectiveness of these measures will depend on its ability to act swiftly and cohesively, with a reliance on widespread member state support.

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Guns N' Money: Europe's reaction to the new geopolitical reality

Reduced US military support means that Europe must step up defence spending. But the question is, who will pay for it? Countries will be allowed to run higher deficits to finance the extra spending but this approach risks amplifying fiscal pressures

The start of negotiations between the US and Russia over Ukraine without involving Ukraine and Europe should have been the final wake-up call for Europe to up its game on defence security. This is a trend that started under Donald Trump's first presidency, persisted with the Russian invasion of Ukraine and now appears to be continuing in Trump's second presidency with minimal US military support in Europe.

The end of the so-called peace dividend – using cuts in defence spending as a vehicle to keep fiscal budgets in shape and leaning too long on the US – is now forcing Europe to increase defence spending and invest in its own domestic military industry. There are many economic aspects to this broad topic but we will only focus on two for now: the economic dimension and funding. Or Guns N' Money.

The economics of Europe's defence spending

With the fall of the Berlin Wall and the Iron Curtain, Europe entered a prolonged period of disarmament. This era saw the end of compulsory military service, a reduction in defence, and a subsequent decline in spending on military equipment. According to Bruegel estimates, government spending on military equipment in the European Union amounted to an average of some 0.3% of GDP between 2008 and 2020. The share of total defence spending in the EU dropped from 2.3% of GDP in 1990 to 1.3% of GDP in 2014. Of the larger EU economies, Germany, in particular, lagged behind. To some extent, it looks as if (reduced) defence spending was another important lever to achieve a balanced budget goal. Returning to the EU, total defence spending increased from 1.3% in 2017 to 2% of GDP in 2024. However, the EU number masks that seven EU NATO member countries still do not meet the NATO target of 2% of GDP.

NATO has already indicated that maintaining the alliance's targeted military capabilities could require increasing spending targets from the current 2% of GDP to around 3.6%. With last week's events, further increases can no longer be excluded.

Spending some 4% of GDP should have a significant impact on the total economy. Up to now, the European military industry has remained relatively small and overshadowed by the broader economy. And since the Russian invasion of Ukraine, roughly 80% of the EU's defence procurement has gone to non-EU firms. One reason for this is the limited production capacity. The European market for military equipment is also fragmented, lacking unified European standards and procurements, relying instead on national ones. Europe currently lacks economies of scale to cater to the sharp increase in demand.

We will explore the potential benefits that the defence industry could offer to the European economy at a later stage. Currently, the industry has a turnover of around €70bn and employs some 500,000 people. It's clear that investing about 4% of GDP in the domestic industry could have a substantial impact. Last year, a cartoon circulated showing the German automotive industry's future as producing electric tanks. Maybe that's a bit exaggerated but it's no longer a complete fiction.

How to pay for it

The heat is on and discussions in Europe are gaining momentum. The focus has shifted from 'if' to 'how' to increase defence spending. Various figures are still being debated. While the countries bordering Russia have called for €100bn of immediate spending, European Commission President Ursula von der Leyen has mentioned €500bn over the next decade. NATO has indicated an increase from 2% of GDP to around 3.6% of GDP. To be clear, an increase in the EU's annual defence spending from 2% of GDP to 4% of GDP would equal some €340bn, per year.

As so often in Europe, the question arises of how to pay for it. Taking the 2024 spending levels as a starting point, the countries that have the most catching up to do are Southern European countries Spain, Italy and Portugal, as well as Belgium. The need for all European countries to go above the 2% of GDP level will amplify fiscal pressures here. Financing higher defence expenditures with austerity measures elsewhere in national budgets looks like a dangerous social experiment. Financing higher defence expenditures with higher deficits could become a new experiment for financial solidarity and stability in Europe.

Remember that during the pandemic, the fear that different fiscal capacities across member states could trigger a new sovereign debt crisis eventually led to NextGenEU, with the Recovery and Resilience Fund as its centrepiece.

As Europe is likely to move towards closer EU procurement and more harmonised standards in the defence industry, steps towards pan-European funding could be the next logical step. This raises the question of what a common funding approach might entail. Current proposals revisit long-standing pan-European funding models.

- There have already been efforts to expand the **European Investment Bank's (EIB)** mandate to provide investment funding in the defence sector, or even issue "European Investment Bank's (EIB) defence bonds". The EIB though is mindful of maintaining its credit quality and reputation and will likely be reluctant to expand into the sector if this push into military financing does not involve a wider acceptance from commercial lenders.
- Using the existing **European Stability Mechanism (ESM)** is another avenue that has seen some consideration. Some €427bn out of the €500bn in lending capacity remains. However, it would very likely require changing the treaty as the conditions

of when it is deployed are narrowly defined around providing financial assistance when countries are threatened by severe financing problems.

- That leaves the option of creating an entirely **new issuer**, like a European Defence Fund, but depending on the setup, it could require a new treaty and of course, new paid-in capital. Considering the large financing volumes, the question remains to what degree the subscribed capital could be leveraged while also maintaining a funding cost advantage over individual countries' debt issuance. Much would depend on the eventual guarantee structure (e.g. jointly versus severally guaranteed debt). A new issuer would not be limited to providing financing to just EU or eurozone members but could include e.g. the UK as well.
- The **EU as an issuer** has proven its ability to quickly ramp up funding. In the wake of the pandemic, it first launched the €100bn SURE programme and the NextGenEU with a capacity of up to €800bn. But it would again be limited to providing financing to EU member countries. And it is likely that governments will have to agree on additional ways to bolster the EU's own resources to maintain its strong credit in the long run.

First national, then European?

The issue of defence spending is complicated by the unequal benefits to countries from the defence industry and employment, and by the fact that a common approach faces another issue: coordinated action cannot be achieved through finances alone. However, at least for now, financial markets seem to be more convinced of an imminent common European approach, reflected in a tightening of eurozone sovereign spreads.

We think that a 'first nation, then European' approach is the most likely way forward. The European Commission's announcement to once again trigger the escape clause of the Stability and Growth Pact suggests that indeed Europe's first line of defence will be to allow European countries to run higher deficits to finance additional defence spending. This would probably also mask differing views and differing levels of complacency. However, such an approach runs the risk of new sovereign debt tensions with potentially widening bond yield spreads. Consequently, and we know the script, it would then be the European Central Bank's job to step in with new asset purchases or targeted liquidity for banks, followed by an eventual European funding solution. Making such a path clear from the onset would help to stifle market turmoil.

Peace deal hopes and tariff risks drive commodities

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Energy prices have fallen over the last month amid hopes of a Russia-Ukraine peace deal. But sanction risks abound, while US tariffs rattle metal markets

Oil falls despite lingering sanction risk

Oil prices came under pressure in February as trade war uncertainty overshadowed sanctions-related supply risks. For now, the oil market is heading toward a surplus this year, justifying the weakness in prices. Things could change rapidly if we see big shifts in the enforcement of sanctions against Iran and Russia. Current price levels also increase the potential for OPEC+ to delay the unwinding of supply cuts. The group is set to gradually reverse these cuts from April. But there's growing speculation that OPEC+ may delay action, despite US President Trump calling for increased output.

The strength in natural gas prices is supporting oil demand through the Northern Hemisphere winter. Global oil demand growth estimates for 2025 have been edging higher. The International Energy Agency (IEA) expects global demand to grow by 1.1m b/d this year, compared to a previous estimate of just under 1m b/d issued in November.

Trade war uncertainty poses downside risks to oil prices, along with the potential for weaker demand. In early February, an escalation in trade tensions boosted oil prices, particularly WTI. The threat of US tariffs on Canadian and Mexican oil briefly pushed WTI prices higher, boosting Brent, too. This was before the US came to a last-minute deal with its two largest crude suppliers. Yet risks abound that these tariffs will return.

European gas storage plummets

European gas prices had a volatile month with TTF trading shy of EUR60/MWh at one point. This was the highest level since February 2023. While prices have come off since then, they remain at elevated levels.

The strength reflects EU gas storage rates falling at an accelerated pace in February. A combination of supply disruptions, stronger domestic demand and reverse flows to Ukraine tightened the market faster than expected. EU gas storage is now around 40% full, not far from where we expected storage to end the 2024/25 heating season.

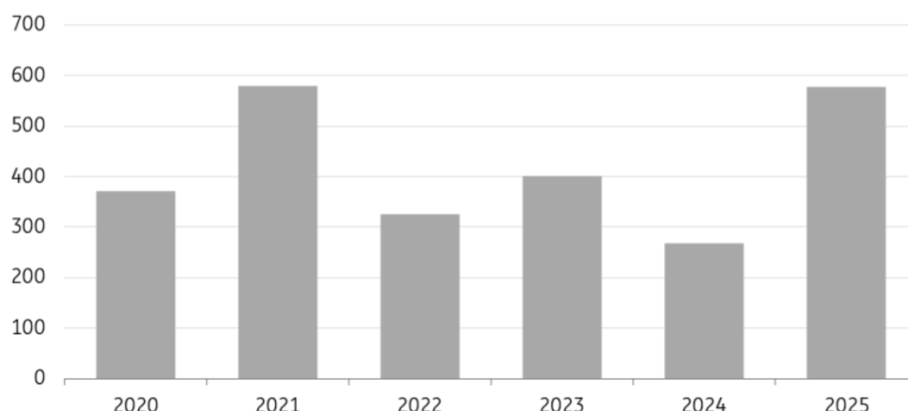
Stronger draws mean storage is likely to finish this winter at less than 35% full. The rate of withdrawals from European storage during the first 24 days of February was the fastest for any February since 2021.

This leaves Europe with an even bigger task of refilling storage ahead of the 2025/26 winter, a job complicated by the shape of the forward curve. There are suggestions that the European Commission might ease storage targets. This seems likely only from next year. It means the pressure is still on to hit the 90% storage target by 1 November 2025. However, German utilities are pushing for storage targets to be eased to 80% ahead of next winter.

Lower storage levels and the job of refilling storage means European gas prices are likely to remain well-supported through the year. We have increased our annual average forecast to EUR45/MWh.

The downside risk to this view is the Commission moving to ease storage targets for next winter. A peace deal that includes Europe agreeing to increase import volumes of pipeline Russian gas could be an even bigger downside risk.

Daily average EU natural gas storage draw for February (mcm)



The daily average covers the first 24 days of February
Source: GIE, ING Research

Metals caught up in trade tensions

Industrial metals had a volatile start to 2025 thanks to Trump's tariff policies. In early February, the US president imposed 25% tariffs on all US imports of steel and aluminium, effective March 12.

The impact will be greater for aluminium than steel because the US imports significant volumes of aluminium. Tariffs would boost aluminium prices, representing a significant upside risk to the US Midwest premium forwards. By contrast, the effects on LME prices will be minimal.

The US imports roughly half of its aluminium. Canada is the biggest supplier, accounting for 58% of imports, followed by 6% from the United Arab Emirates. Imported steel accounts for roughly a quarter of US consumption needs, with Canada the top supplier at 25%, followed by Brazil and the EU at 17% apiece and Mexico at 14%.

Trump claims the duties will increase domestic production and bring jobs back to the US. However, previous tariffs didn't increase domestic production of either metal. In 2024, the US steel industry's output was 1% lower than in 2017 before Trump's first round of tariffs. The aluminium industry produced almost 10% less.

Copper imports are also at risk as Trump orders an investigation on national security grounds. This paves the way for tariffs down the road. As a result, Comex copper futures have surged.

Tariffs are bearish for industrial metals as global growth slows. Yet the prospect of a prolonged trade war raises expectations that Beijing may unveil more aggressive stimulus measures, limiting the downside for metal prices.

Concerns that tariffs might intensify inflation risks as economic growth slows are boosting demand for safe-haven assets like gold. Gold prices are already up more than 12% year-to-date, establishing a series of consecutive record highs along the way. With tariff concerns likely to linger, gold will continue to benefit from heightened uncertainty.

Meanwhile, central banks will continue to buy gold as geopolitical tensions and a difficult economic environment increase demand for safe-haven assets. The People's Bank of China (PBoC) increased gold reserves for a third consecutive month.

Trump's return is triggering something of a gold rush in the US, too. Though Trump hasn't specifically targeted gold with levies, traders worry the precious metal could be hit by any potential blanket tariffs. This US demand surge could provide a further boost for gold prices. We believe gold will hit more record highs this year, with $3,000/z now in sight.

Our latest views on the major central banks

Our take on what could be on the horizon for the Federal Reserve, European Central Bank, the Bank of England and the Bank of Japan over the coming months

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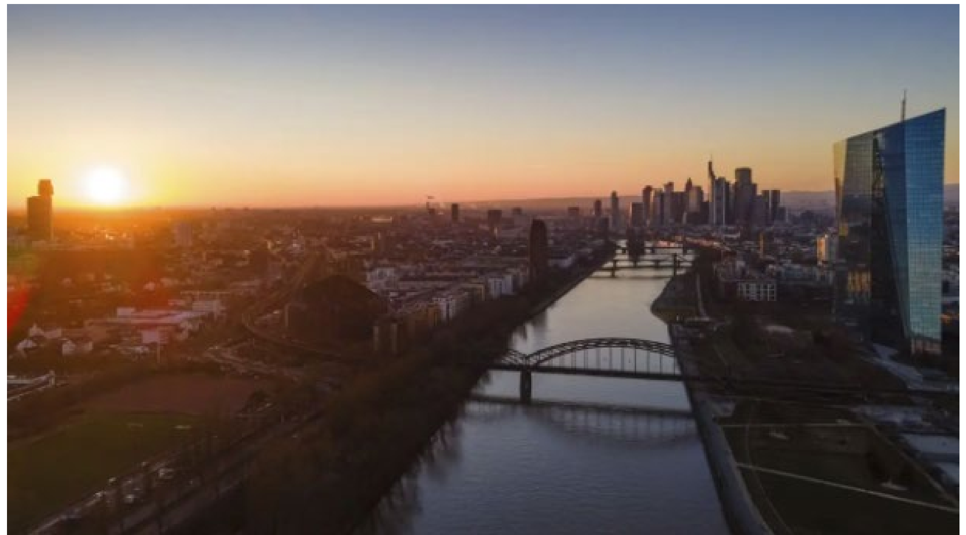

In the run up to the European Central Bank's March meeting, official statements have pointed to an increasingly heated debate about where to stop the current rate cut cycle

Federal Reserve

In the immediate aftermath of the election, it was sensed that pro-growth tax cuts and deregulation combined with potentially inflation-boosting tariffs and immigration controls would mean the Federal Reserve would have less scope to cut rates. In the wake of recent disappointing data, there has been more focus on the potential downsides of President Donald Trump's policy thrust. There are concerns that aggressive government austerity will be bad news for overall economic activity and that steep tariff increases would eat into the spending power of middle and lower income households. This has reinvigorated the belief that the Fed may need to offer more support.

Despite worries about government-related job losses, unemployment is low and inflation is still tracking too hot, so we see little prospect of a rate cut before late summer. Nonetheless, we see a good chance of rate cuts in September and December, with a third coming in March next year – particularly with housing-related inflation measures looking better behaved, which would act as an offset to some of the tariff-related inflation fears. This would leave the policy rate in the 3.5-3.75% range – still well above the 3% level the Fed has as its long-term forecast.

European Central Bank

Another cut and then what? In the run up to the European Central Bank's March meeting, official statements have pointed to an increasingly heated debate about where to stop the current rate cut cycle. While the well-known doves continue calling for a policy rate at 2% by the summer, the hawks have started to emerge again, questioning the need to cut rates below 2.5%.

Despite this debate, a 25bp rate cut at the March meeting still looks like a done deal. The policy rate would then be at the upper end of the range for the neutral interest rate. With inflation notoriously being too high but the economy remaining weak, the ECB will

have to find a fragile balance between losing control again and supporting the economy. As we think that the central bank's own growth forecasts are still too optimistic, we see the ECB cutting to at least 2% by the summer once the eurozone economy indeed turns to out to be weaker than it had expected.

Bank of England

Having cut rates in February, the path of least resistance is for the Bank of England to keep lowering rates once per quarter for the remainder of the year. While Catherine Mann – once the arch-hawk of the committee – has begun voting for more front-loaded cuts, it’s not a view shared by many others. Indeed, we detect some caution at the Bank about the recent rise in energy prices and the fact that headline inflation is set to rise above 3% this year. Still, the jobs market is under more visible pressure and we expect service sector inflation to fall back in the spring, undershooting the most recent BoE forecasts. That should make the Bank more comfortable with cutting rates much closer to 3% than markets are currently pricing.

Bank of Japan

After a rate hike in January, the Bank of Japan is likely to remain on hold at its March meeting, monitoring the impact of previous rate hikes and other developments such as inflation, wage growth and US tariff policy. Given the recent sharp moves in the FX and JGB markets, the BoJ's communication should be cautious about sending any signals on the timing of future rate hikes.

We expect the BoJ to deliver a 25bp hike as early as May while maintaining its flexibility in the JGB purchase operation in order to manage any sudden moves in the JGB markets. In our view, the spring wage negotiations are key for gauging the timing of the BoJ's next rate hike, while the main risk factor remains Trump's tariff policy and how it could affect the Japanese economy.

Optimism about Trump exceptionalism fades amid subdued start to 2025

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After a frenetic first month in office, initial optimism that President Trump will deliver ongoing US growth exceptionalism is giving way to concerns about the downside impact of some of his policies, including trade tariffs and government austerity on spending power and jobs

Despite optimism about Donald Trump's policy mix, the US economy has started the year on a soft footing

Subdued start to 2025

Despite plenty of optimism about Donald Trump's policy mix of light-touch regulation and lower taxes, the economy has started the year on a soft footing. January's drop in manufacturing output and retail sales was possibly cold weather-induced with some marginal impact from the LA fires, but the fact that we saw internet sales also drop suggests that softer consumer confidence numbers may be translating into cooler spending.

There are certainly signs of stress amongst lower-income households; the Philly Fed reported that a record 11% of credit card holders only make minimum monthly payments, and the New York Fed reported rising auto and credit card delinquencies. However, higher-income households are still spending strongly and we look for a rebound in February and March, if only to avoid the impact of potential tariffs on the prices of big-ticket items. Thereafter there is much greater uncertainty.

The jobs market continues to hold up well, but the plunge in the quits rate suggests labour market turnover is slowing rapidly, which is a strong predictor of cooling wage pressures. Household income growth looks set to slow meaningfully in the second half of the year and government spending cuts will only exacerbate this situation. Initiatives by the Department of Government Efficiency to cut at least 200,000 federal workers from the government's payroll may be the tip of the iceberg when we consider that upwards of five million private sector jobs are tied to government contracts.

Financial pressures set to build

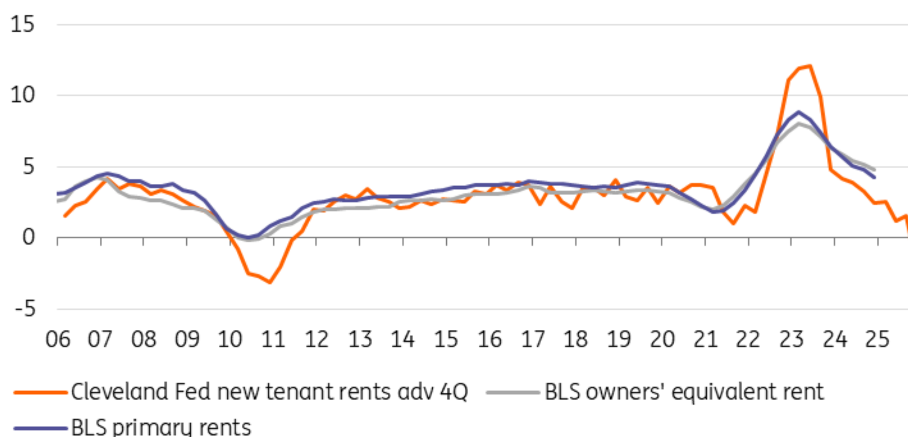
At the same time, there are likely to be increasing financial pressures from Trump's trade policies. Trade tariffs are likely to be implemented in the second quarter, and while the Administration argues that "foreigners will pay" there is an acknowledgement that

there may be some financial pain for consumers. We think this could be significant since it will be difficult to substitute American-made products for all foreign imports.

Trump has suggested lower taxes will provide a more than offsetting boost, but we are not so sure. The extension of 2017 tax cuts will almost certainly pass, but there will be no noticeable change in household after-tax income. The ending of the tax on tips is possible since there is bipartisan support. However, proposals to exempt social security and overtime pay from taxation will likely struggle to pass.

Moreover, while Trump's policies are supposed to prompt reshoring and boost activity in the US, the lack of clarity on the trading environment faced by US corporates suggests action is likely to be slow. At the same time, household and corporate borrowing costs have actually risen despite the Federal Reserve cutting the policy rate by 100bp in late 2024. We forecast GDP growth to slow from 2.4% in 2025 to 1.6% in 2026.

Some potential good news for inflation from housing rents



Source: Macrobond, ING

Inflation outlook clouded by tariffs

In terms of inflation, how the tariffs are implemented will be important for the outlook. If the tariffs are one big step change, then the Fed may choose to look through it and focus on the potential hit to spending power in the knowledge that the base effect will likely drop out next year. However, if it is incremental ratcheting up over time then that is likely to be more bearable for the economy and the Fed sees it more as a structural story that keeps it from cutting rates.

That said, there is some good news potentially coming through on inflation. The Cleveland Fed's new tenant rents series has turned steeply negative and there is also a noticeable slowing in the continuing rents series. They suggest the possibility of the housing components within CPI "normalising" late this year or early next. This can go a long way to offsetting the effect of tariffs given that housing components are 42% of the core CPI basket and keep the door open to Fed interest rate cuts.

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Geopolitics take centre stage for the eurozone

Geopolitics have shifted into the spotlight, with European politicians struggling to get involved in a Ukraine peace deal while at the same time trying to prevent higher US import tariffs on European goods. Calls for higher defence spending are gaining traction. With the economy bottoming out, the ECB thinks the trough in interest rates is approaching

US President Donald Trump meets with French President Emmanuel Macron in Washington DC

Europe less than prepared for geopolitical shifts

The early weeks of US President Donald Trump's second term in office have already caused significant upheaval in the European Union. It now appears likely that, starting from the second quarter, the US will use reciprocity as a justification to increase import tariffs on European goods in sectors where European tariffs are higher than those in the US. The Trump administration also views VAT as an additional import tariff in Europe, which could increase the scope for US tariff increases.

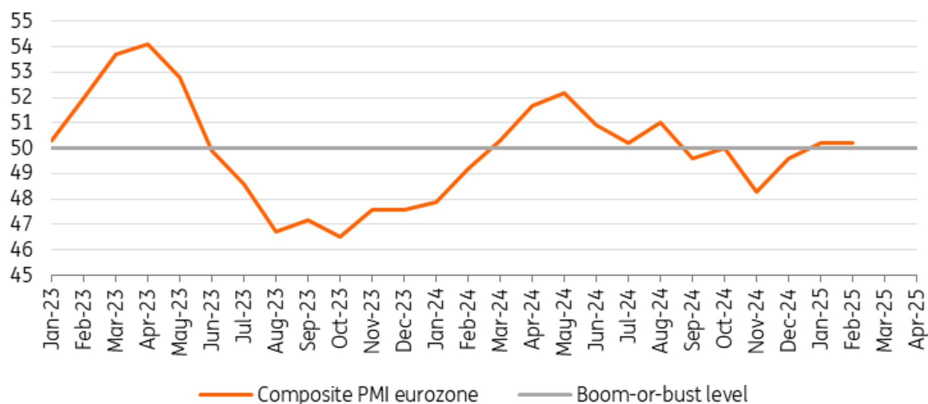
Simultaneously, Trump has been advocating for a ceasefire in Ukraine, largely sidelining Europe and Ukraine as potential partners in the negotiations. While peace in Ukraine would be beneficial for business and consumer sentiment and could potentially lower energy prices, a deal is not yet guaranteed – especially if Russia is treated too favourably. Meanwhile, the US has made it clear that Europe must enhance its own defence efforts, as the US is less willing to continue guaranteeing Europe's security. This has led to confusion and indignation in European capitals, but no clear common response has emerged so far.

More defence spending

On a positive note, the German elections have resulted in only one viable coalition: a "grand coalition" between the CDU/CSU and the SPD. Unfortunately, scrambling together the two-thirds majority needed to amend the debt brake seems challenging. However, we remain confident that the new chancellor, Friedrich Merz, will find a way – such as declaring a state of fiscal emergency – to increase government spending, particularly for defence. Germany still has some budgetary room for fiscal expansion.

Other countries that also need to increase defence spending (Europe should probably move from about 2% to 3.5% of GDP over the next five years), but have less fiscal space, will need to find savings elsewhere. On top of that, when taking the long lags and high import content of military spending into consideration, GDP stimulus for this year and next year seems limited. Nonetheless, we have already added 0.1 percentage points to our 2026 growth forecast, and the boost for 2027 could be slightly higher. The likelihood of the extra military spending being financed by a European defence fund with borrowing capacity remains small for now.

Eurozone economy bottoming out, but growth outlook remains subdued



Source: LSEG Datastream

Economic situation not as bad as markets feared

Since December, European economic indicators have surprised positively, mainly because they weren't quite as bad as the market expected. The best description for the state of the eurozone economy seems to be “bottoming out.” The composite PMI stabilised at 50.2 in February, just above the boom-or-bust level. However, the new orders component remained weak and employment fell, especially in manufacturing. Consumption has been disappointing due to a less positive assessment of the labour market, leading to a higher savings rate. While there is potential for stronger consumption growth, geopolitical uncertainty is not helping boost consumer confidence. We've therefore maintained our growth forecast of 0.7% for this year, while raising it to 1.3% for 2026, driven by additional military spending.

The ECB is approaching the neutral rate

Inflation is likely to remain above the European Central Bank's projections in the first quarter, and higher input prices in both manufacturing and services have increased selling price expectations. At the same time, the ECB’s wage tracker continues to indicate a deceleration in wage growth in the second half. In February, the ECB published estimates of the neutral interest rate, which ranges between 1.75% and 2.25% based on recent model updates, and between 1.75% and 3.0% based on all available models.

It’s therefore no surprise that ECB director Isabel Schnabel stated that the central bank is approaching the point where it might need to pause or halt rate cuts. We still believe that 2% will be reached by the summer, and 1.75% is feasible if the upturn remains very subdued. However, the consensus within the central bank seems to be that any recovery might quickly encounter supply constraints, making it risky to adopt an overly expansionary monetary policy.

German elections: Wirtschaftswunder 3.0 still far out

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Germany is heading towards another revival of the grand coalition as its political landscape grows increasingly fragmented

Signing of the parliamentary group of the CDU and CSU by Friedrich Merz and Markus Söder, Berlin

The results of the elections are well-known by now: the CDU/CSU led by Friedrich Merz came in as largest party, followed by the far-right AfD, SPD, Greens and Linke. The FDP and BSW didn't make it into parliament.

Besides the results themselves, there are a few important observations: the 84% voter turnout was the highest since reunification, and the three parties of the collapsed government coalition lost some 18 percentage points of their 2021 votes, with the SPD and the FDP suffering severe losses. At the same time, far-right and far-left parties gained almost 20ppt compared with 2021, reaching almost 30% of the total votes. And there is more – despite winning the elections, Merz's CDU had the second weakest result ever, and the SPD had its worst result ever.

Towards a revival of the grand coalition

Given that the CDU/CSU strictly ruled out a coalition with the AfD, the only possible government coalition is a revival of the grand coalition between the CDU/CSU and SPD. Still, coalition talks won't be straightforward. After its worst election result ever, the SPD will not easily move into a government coalition as junior partner to the CDU/CSU. The party is likely to now enter a new era of political leadership and another existential crisis. Also, any coalition agreement will probably have to pass a grassroots vote, with members who are traditionally more left-wing than their party leaders.

Still, we think that eventually the SPD will budge, as a grand coalition is the only feasible option for the CDU/CSU to form a government and the SPD has proven often enough not to shy away from the responsibility to join a government. The only other option would be a coalition with AfD; a scenario Friedrich Merz had strictly ruled out.

In the first days after the elections, Friedrich Merz already learned that being the leader of an opposition party is something different than becoming the next chancellor.

Promises made in an election campaign are not that easily implemented in a government coalition.

After complicated coalition talks, a revival of the grand coalition could bring some tax cuts for households and corporates without cuts in social expenditures, as well as some deregulation. The coalition will probably also agree on investments in infrastructure and defence, either via a special purpose vehicle or changes to the debt brake. Germany might support increased European efforts to fund defence and infrastructure spending. However, significant reforms, such as changes to the pension system, seem highly unlikely. Additionally, achieving lower and more stable energy prices should not be taken for granted.

How to pay for it?

The biggest challenge will be financing any new plans. During the campaign, the CDU/CSU presented plans with a significant funding gap. Joining a coalition with the SPD will make this funding gap even larger as cuts on social expenditures are less likely to happen. However, it was always suspected that the CDU/CSU would shift its stance on the debt brake after the elections. Whether this is really happening is a different story. Suggestions made by Friedrich Merz after the elections for possible changes to the debt brake were corrected a few hours later.

With the Left and the Greens, there is now a two-thirds majority in parliament for outright changes to the debt brake, although the Left would not support such a debate for increased defence spending. There is a narrow window to reform the debt brake by using the next 30 days – during which the current parliament is still in place – to secure the votes of the SPD, Greens, and CDU.

The CDU, however, has now ruled out these outright changes. Still, a special funds for additional defence spending might still be announced with the help of the ‘old’ parliament. What's more is that the CDU/CSU has manoeuvred itself into a difficult position. While probably open for more substantial changes to the debt brake for infrastructure investments, the tough talk during the election campaign will keep the CDU/CSU from pushing too hard for these changes. It doesn’t want to suffer reputational damages. Promises made, promises kept.

Some cyclical improvement without Wirtschaftswunder 3.0

German voters will get what they want the most: soft and gentle change but no disruption. Some cyclical recovery without getting close to any Wirtschaftswunder 3.0. In fact, the biggest risk next to simply delaying overdue reforms is a further strengthening of the far-right and far-left (as we saw previously whenever the CDU/CSU and the SPD were in a coalition). Therefore, a lot of the success of the next government will depend on the willingness of individual parties and leading politicians to leave personal and party interests behind and focus on getting the economy out of its structural stagnation. This would also require leaving some political holy cows behind.

UK: don't overdo the gloom just yet

The mood music around the UK jobs market is becoming increasingly sour. But with big injections of government spending coming, 2025 growth still looks set to be reasonable

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The UK Chancellor, Rachel Reeves, will give her 'Spring Statement' in March

'Non-linear' falls in employment? We're not there yet

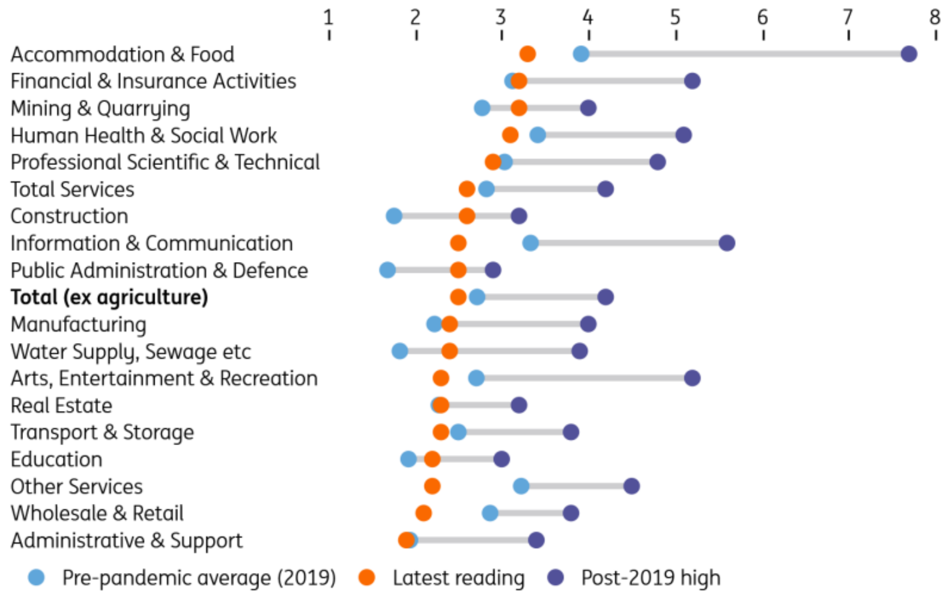
Is the UK headed for recession? It's a question that's coming up more regularly following fourth quarter growth which, though fractionally positive, was a lot weaker than many had expected just a couple of months ago. And with a sizeable tax hike on employers looming in April, the mood music on the jobs market is turning increasingly sour. Bank of England rate-setter Catherine Mann – until recently an arch-hawk – surprised everyone with a vote for a 50bp rate cut on the basis that we could see "non-linear" falls in employment.

We're not convinced we're at that point yet, but the jobs data is undoubtedly cooling. With a handful of predominantly government-related exceptions, vacancy rates are below pre-Covid levels – and quite considerably across consumer services and retail. Private sector hiring, though more stable in the most recent month, did fall by close to 1% in 2024.

That said, there's no sign of a pick-up in redundancies. Employers are required to notify the government when they are proposing more than 20 job losses, and those notifications haven't risen. That will almost certainly change as we get closer to the April tax hike.

That all means that wage growth – currently stuck up at 6% - should, in theory, come lower this year, though we and others have been saying that for a while. The near-7% rise in the National Living Wage in April will maintain some pressure. But business surveys point to pay growth of more like 4% in the months ahead.

UK vacancy rates are generally below pre-Covid levels



Source: Macrobond, ING calculations

Tough spending decisions are coming in March

Barring a surprise collapse in the jobs market, UK growth should still be reasonable this year. We're already less optimistic on the fourth quarter than the likes of the Bank of England and Office for Budget Responsibility and we're keeping our previous 1.2% forecast for 2025 as a whole. A spike in activity in December gives the first quarter a decent tailwind. And remember that we're looking at hefty increases in government spending this year.

That fact is unlikely to change dramatically at the Spring Statement on 26 March. The Chancellor has run out of fiscal headroom, or money left over, once the fiscal rule requiring a balanced current budget in 2028/29 is met. Higher market rates and lower 2025 growth forecasts mean the Chancellor will need to make modest changes to spending in March. Whether this is done upfront or via changes to spending plans in future years will have a heavy bearing on how markets react. Backloaded spending cuts risks further gilt underperformance next month.

Ultimately, we think any changes the Chancellor makes will only delay the inevitable decisions on further tax hikes until later in the year.

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China's Two Sessions will set the economic stage as China-US trade talks loom

After a fairly quiet February, policymaking is about to heat up as Beijing unveils its 2025 growth target and priorities as trade war headwinds intensify

Thousands of delegates will take part in the 'Two Sessions' gathering in Beijing

China's growth target likely to be set at "around 5%" again this year

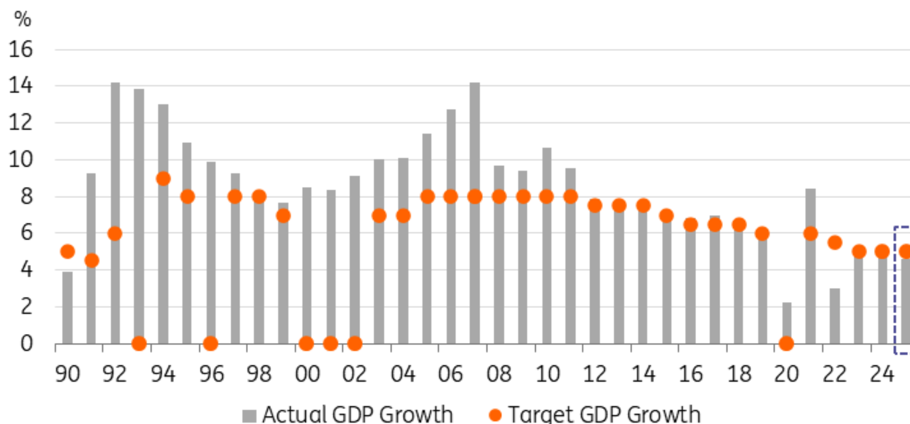
We expect China to stick with its "around 5%" growth target again in 2025, a show of confidence that external headwinds might not derail growth in Asia's biggest economy.

The setting of China's annual growth target at the "Two Sessions" tends to be one of the premier economic events of the year, signalling the direction of policy. Since 1990, China's growth has only fallen notably short of the GDP goal twice -- in 1990, the first year Beijing announced a target, and in 2022 amid pandemic lockdowns.

At times last year, China's initial "around 5%" target seemed to be on shaky ground amid weak domestic demand. However, a big stimulus push beginning in September catalysed a strong rebound in the fourth quarter, putting growth back on track.

Another "around 5%" target, to be announced on 4 March, would suggest a renewed determination to maintain rapid growth. An "above 4.5%" target would be on the softer side but still show a commitment to keep growth from weakening significantly. However, such a downshift would likely be poorly received by markets. It would be read as a sign that growth will come under greater pressure this year.

China historically almost always meets annual growth targets



Source: CEIC, ING

Two Sessions to shed light on monetary and fiscal policy direction

China's official monetary policy tone was altered at December's Central Economic Work Conference to "moderately loose" from "prudent," the first change in language since 2010. This new posture will likely be validated at the Two Sessions. While these descriptive terms aren't binding, they're likely to signal that monetary easing will continue. We currently forecast 30bp of rate cuts and 100bp of reserve requirement ratio (RRR) cuts this year.

Policies from the People's Bank of China over the last year have generally been well-received by market participants. But fiscal policy is likely to be under greater scrutiny in 2025. While troubled local government finances limited the rollout of policy support last year, there's hope that last November's RMB 10tr fiscal package will ease downward pressure. We expect the Two Sessions will prioritise increased fiscal spending, a higher debt ceiling (set at RMB 35.5tn in 2024), higher levels of special government bond issuance, and telegraphing Beijing's strategy to support domestic demand.

Early signs are that fiscal policy will focus on expanding the trade-in policies to support consumption and broadening the government's equipment renewal scheme. Markets will watch the Two Sessions closely for any hints of directional shifts in fiscal stimulus. Possible areas to watch: expanded consumption voucher programmes and tax relief for low-income households.

China-US talks expected ahead of key deadlines in April

China was the first country hit with new tariffs in President Trump's second term. An additional 10% levy took effect in February. China's initial retaliation moves have been mild so far -- 10-15% tariffs on just 10% of US imports. This early restraint from both sides has fuelled some optimism, but few expect this to be the end of the US-China trade clash.

Early April features two key dates from the US side. First, an investigation into China's purchases under the "Phase One" trade agreement to be completed by April 1. It will find that China fell short of purchases, though the pandemic and policy shifts under Joe Biden's administration could offer some justification. Second, Trump's decision to keep TikTok operating in the US expires on 5 April. While neither variable represents a hard deadline, an escalation in tensions seems likely without high-level talks in March.

Striking another trade deal and heading off a tariff arms race could be a win-win for both nations. This, however, could be challenging given the US prioritising increased export controls on high-tech exports in the Trump 2.0 era.

Economic recovery gaining momentum in Central and Eastern Europe

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Economic growth in the CEE region is picking up pace, but recent data shows some inflationary challenges. Additionally, geopolitical factors are once again impacting CEE countries, creating uncertainties that further complicate the continuation of central bank rate-cutting cycles

We project GDP growth of 3.2% in Poland in 2025. This time, domestic demand will be the primary driver

Poland: Back on recovery track with growth outlook above 3% in 2025

January's monthly data aligns with our baseline scenario for economic and price developments in 2025. Construction output has rebounded after 12 consecutive months of annual declines, indicating the anticipated resurgence of public investment has begun. We predict that Recovery and Resilience Fund projects, along with European Union Cohesion Funds, will drive a 9.5% increase in investments this year. We expect public investment to stimulate private spending through multiplier effects. Polish corporates are among the most deleveraged in the EU, so we see space for a private investment recovery possibly at the turn of 2025-26, subject to better business confidence and lower interest rates.

At the same time, industrial production indicates continued stagnation in domestic manufacturing, mirroring trends in Germany and the Czech Republic. With external demand remaining weak due to Germany's prolonged recession, Poland's main trading partner, we anticipate further declines in net exports. Consequently, the current economic recovery will differ from previous cycles, where net exports positively contributed to the recovery. This time, domestic demand will be the primary driver. We project GDP growth of 3.2% in 2025.

CPI inflation rose more than anticipated in January, reaching 5.4% year-on-year from 4.7% in December, mirroring trends in other CEE countries. However, wage growth slowed to a single-digit rate at the turn of 2024 and 2025, which is expected to reduce cost pressures on businesses. Consequently, the outlook for service prices and core inflation is improving, potentially allowing the National Bank of Poland to implement rate cuts in the second half of 2025.

Zloty appreciation (EUR/PLN is at the lowest level in more than seven years) is also making the inflation outlook brighter. We expect CPI inflation to peak in March at around

6% YoY, ease slightly in the second quarter and head southwards in the second half of the year. Our baseline scenario assumes the NBP cuts rates by 50bp in September, followed by two more 25bp rate cuts in October and November, reducing the main policy rate to 4.75% at the end of this year.

Czech Republic: Expansion gains traction while the terminal rate approaches

The economic recovery is about to gain pace in the Czech Republic, further driven by solid real wage growth and consumption expenditure. That said, we see some risks to aggregate spending appetite should the situation in manufacturing remain bleak, as households could restrain expenses due to the economic and labour market situation looking less rosy ahead.

Still, the Czech economy is set to outperform the eurozone, as the real growth differential turned positive in the middle of last year after flying in the sub-zero range for three years. The convergence process for the Czech economy appears to be back on track, even in real terms. Although the economy is still growing below its potential, the output gap is expected to close by year-end, shifting the broader economic stance towards a more inflationary position than before.

We expect both headline and core inflation to remain above target, while the headline rate will be supported by increasing food prices and rents. Cost pressures have accumulated in the agricultural sector, and the property market is likely to heat up in the spring season. With the demand for residential properties hideously exceeding the supply side, the risks to core inflation are non-negligible. Steady price growth persistence of services may also contribute to elevated inflation, while the disinflation in the service sector is expected to continue gradually. However, this all comes down to whether the labour market tightness will recede somewhat to soften the buoyant wage growth. The construction sector lift-off will at least partially outweigh recent layoffs in manufacturing.

There is still room to further ease the monetary policy stance as the terminal rate approaches. We are likely to see a base rate reduction during meetings with a new Czech National Bank forecast, accompanied by hawkish commentary, bringing the nominal rate to 3.25% in August. However, if consumer price dynamics remain strong, the real interest rate could approach the zero bound. In such a scenario, we believe a 3.5% rate would also do the job.

Hungary: Waiting for clarity

The Hungarian Central Statistical Office will release the detailed GDP data for the fourth quarter of 2024 on 4 March, which will be a really important milestone. This will give us a better idea of whether there are signs of life in investment activity and whether the positive momentum in consumption has been maintained. If we see weak domestic demand, that could be another nail in the coffin of the government's plan for a flying start to 2025. We are now looking at 2% GDP growth in 2025, but with weak momentum at the end of last year, this forecast could be even lower.

Inflation could also be a party-killer here. After the January surprise, we've updated our average inflation forecast to 5.1%, subject to further upward revision if the February print shows that the jump in repricing at the beginning of the year was not just a one-off but rather the start of a trend. Rising inflation will translate into higher inflation expectations, weakening consumer confidence, the economic outlook and ultimately business confidence.

With labour hoarding, a further deterioration in projected economic performance could lead to layoffs, particularly in the manufacturing sector. Anecdotal evidence suggests that this has already begun. The next few months of labour market data will be crucial in

measuring the expected damage and the possible impact on real wage growth as well. This kind of negative news about Hungary could raise market expectations that the government will feel some urgency and let go of this year's deficit target, reversing the recent positive market sentiment.

This sentiment has been driven more by hopes of a ceasefire and peace in Ukraine, though. With the second phase of Trump's tariffs on the horizon (from 12 March), this may also weigh on market sentiment. The bottom line is we expect uncertainty to increase in the coming months, leading to a weaker forint and possibly higher risk premiums on bond yields, and a hawkish repricing is also on the cards for the short end of the yield curve.

Romania: Fiscal and geopolitical risks continue to dominate the picture

After the fourth quarter preliminary release, Romania recorded a well-below-potential 0.9% GDP growth. The structural need for imports weighed on growth visibly last year and large improvements are rather unlikely in the short run. For 2025, we expect GDP growth to pick up towards 1.6%. Consumer demand should remain robust, and productivity improvements from the Schengen ascension and new infrastructure developments should provide some tailwinds ahead. Investments are also projected to strengthen. That said, risks are rather tilted to the downside, stemming from the potential need for an even higher tax burden down the line and the upside pressures on interest rates fuelled by geopolitical events. Lower wage growth should also prevent growth from accelerating too much.

On the monetary policy front, the National Bank of Romania left rates on hold at its February meeting. Policymakers hinted towards a cautious approach to monetary conditions until the fiscal outlook and its impact on inflation becomes clearer, and external risks moderate. For 2025, we foresee a total of 50bp of rate cuts left for the second half of this year, taking the key rate to 6.00%, with risks mildly to the upside.

Concerning the fiscal situation, we continue to expect a correction of the fiscal deficit to 7.0% in 2025, with risks tilted to the upside again, following the outsized 8.6% deficit in 2024. The government coalition elaborated an investment-driven budget for 2025, which counts on a solid EU-funds absorption. Based on the announced measures so far, achieving the desired target through increased spending efficiency and better tax collection looks like a priority for officials. Risks to the outlook stem from scenarios of weaker-than-expected consumption and more challenging financing conditions.

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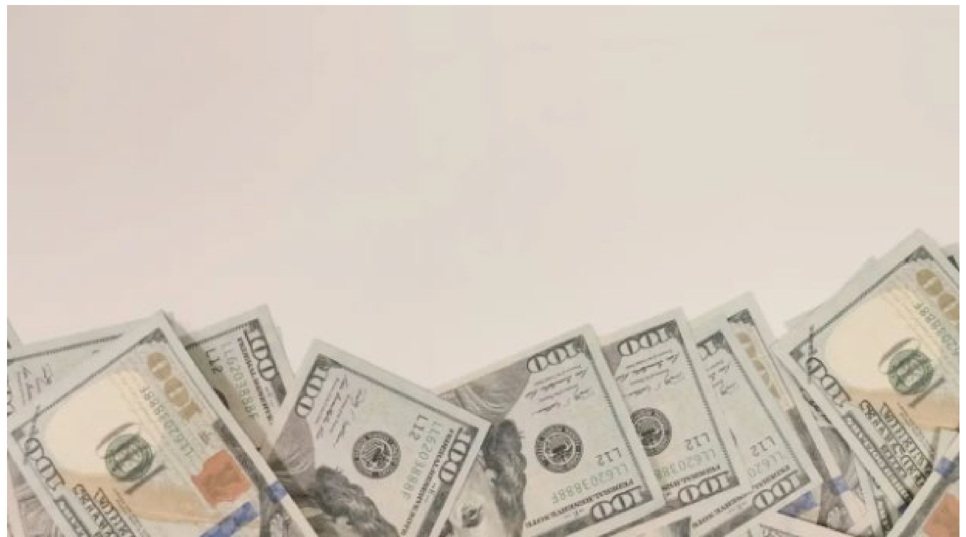
FX: Why we remain bullish on the dollar

The dollar has come under some pressure on the back of the rerating of the US growth outlook and expectations that the Russia-Ukraine conflict is nearing an end. However, we expect US tariffs to regain centrality and drive the dollar sustainably higher



Large post-US election dollar long positions were trimmed in February as markets reassessed some of the key drivers of the USD bullish trend. In this note, we discuss those drivers and why we remain bullish on the dollar.

Firstly, US tariffs. Markets have adapted to President Trump's unpredictable communication style and are treating tariff threats with a greater dose of scepticism. However, our baseline view remains that the US will go ahead with tariffs on the European Union and Asia. That could be part of a Treasury-led, longer-lasting policy measure – as opposed to the erratic, border-focus approach seen in the US-Mexico-Canada trade incident. We expect a peak protectionism risk premium in FX in the second quarter, which implies a stronger dollar and a weakening of developed European and emerging Asia currencies.

The second factor that contributed to recent dollar weakness has been souring sentiment on US activity. The consumer story has softened, but we doubt there will be enough deterioration in hard data to bring the Federal Reserve closer to a rate cut, which we currently expect only in September. As long as markets are comfortable with no more than two cuts (our call) in 2025, the pass-through to a weaker dollar will be limited, and a gradual worsening of US activity and employment should not really hinder a tariff-led dollar rally.

Finally, geopolitics. The FX market is broadly pricing in a Russia-Ukraine peace deal in the near term, and the residual downside risk for the dollar from that should not be big. Ultimately, a clear shift towards a more confrontational US-EU relationship could be the longer-term takeaway, and EU defence spending shouldn't be enough to revive the bloc's stagnant economy.

We continue to expect downside potential extending to parity for EUR/USD. Our year-end target is 1.02, but we acknowledge there are some upside risks should the tariff story or US exceptionalism deflate sooner. The European Central Bank will likely continue to cut rates to at least 2.0%, and remain a net negative for the euro.

In the rest of G10, sterling is facing substantial downside risks from fiscal turbulence and potentially larger Bank of England cuts, and we see GBP/USD heading towards the low 1.20s. Commodity currencies should suffer from revamped tariff risk, while the yen can resist a dollar reappreciation better than others.

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Rates: The glass half empty trade

The Department of Government Efficiency, Treasury Secretary Scott Bessent, and the supplementary liquidity ratio have been the drivers of lower Treasury yields, compounded by weaker consumer confidence and lowered expectations for the terminal rate. The market is now weighing potential downsides. Can this trend continue? Yes, for a while...

It remains unclear how realistic the doge spending cut goal is

US Treasuries see a glass half empty version of the Trump cocktail

We point again to some of the impulses out there that have been driving Treasury yields lower.

First, the Department of Government Efficiency (DOGE); the doge-tracker.com site has recorded US$55bn of "tax dollars saved" so far, 2.75% of the US$2tr goal. The feasibility of the DOGE spending cut goal remains uncertain. However, it cannot be ignored as a potential factor in containing the fiscal deficit and, by extension, Treasury issuance requirements. In extreme cases, it could negatively impact GDP, especially if even half of the target is achieved.

Second, while Treasury Secretary Scott Bessent cannot directly control the 10-year yield, it is clear he has an overt ambition to get it lower.

Third, potential adjustments to the supplementary liquidity ratio (SLR), particularly the exclusion of Treasuries from the measure, would free up bank balance sheets, ultimately increasing liquidity in US Treasuries. This, in turn, helps Treasury yields to trade lower than they otherwise would.

From 4.8% to 4.3% on the 10yr – a 50bp swing from all amazing to some material doubts

We believe that these three factors have already been somewhat impactful, as we see on the spread from 10yr SOFR to the 10yr Treasury yield, which has tightened from 55bp to 40bp since the turn of the year. The US 10yr Treasury yield at around 4.5% was flat to our estimate of neutrality. It has since broken down to 4.3% in the past 24 hours driven by a dip in consumer confidence, and a ratcheting down in the terminal Fed funds rate.

When the 10yr hit 4.8% in mid-January, the market distilled a net upward risk coming from the Trumpian mix of policies. The reversion back below 4.5% to now 4.3% represents the distillation of a different outcome, one where the mix of policies is net negative. It's tough to resist this move for now. The implied floor from the funds strip has shifted down to 3.5%, mostly on a whim. But that's all that's needed to make some room for the 10yr yield.

The tactical bullish impulse we identified some weeks back has turned more sinister. Still tactically bullish, or at least neutral given the size of the move. Expect the unexpected though, as this market can just as easily decide that the glass is half full again, and that's when the structural view of the 10yr getting to 5% can be latched on to. Clearly not the mood music right now though.

The eurozone remains caught in the cross hairs, with lower yields the outcome for now

Meanwhile, the concerns coming out of Europe are contributing to the same trend. The expectation that the European Central Bank will continue cutting rates in the coming months is likely to push longer-term rates lower or at least keep them contained. In the eurozone, the ECB aims to reduce deposit rates to 1.75%. That's below the 2% area that we deem to be neutral.

The rationale for the ECB landing below neutrality while the US lands above largely centres on relative fundamentals. Germany continues to act as a drag in the eurozone – and typically when Germany is not working, the eurozone is in trouble. On top of that, the US tariff bullets aimed at Europe are the last thing that the eurozone needs – partly because they would be rebuffed by counter-tariffs, so everyone loses.

But still, the contrast between the two regions is stark as US growth remains more lively, and the Trump administration has stimulus at its core even if the market is currently questioning this. On balance, there is pressure to the downside for yields. But we're not convinced this will be a structural move. Pressure for a reversion higher in longer tenor rates remains a theme that is likely to come back onto the radar screen in the months ahead.

GDP forecasts

Developed Markets (QoQ% annualised growth)	4Q24F	1Q25F	2Q25F	3Q25F	4Q25F	1Q26F	2Q26F	3Q26F	4Q26F	2024F	2025F	2026F
US	2.3	2.7	2.2	1.6	1.4	1.6	1.7	1.8	1.8	2.8	2.4	1.6
Japan	2.7	0.4	1.2	1.2	0.8	1.2	1.2	1.2	1.2	0.1	1.4	1.1
Germany	-0.9	-0.7	0.0	1.2	1.1	1.4	1.4	1.4	1.4	-0.2	-0.2	1.4
France	-0.3	0.4	0.8	1.2	0.8	0.8	1.2	1.2	1.2	1.1	0.7	1.0
UK	0.4	2.1	1.8	1.2	0.9	0.8	0.8	1.0	1.0	0.9	1.2	1.0
Italy	0.0	0.9	1.2	0.8	1.0	0.5	1.3	1.0	0.6	0.5	0.7	0.9
Canada	1.7	1.6	1.5	0.7	0.8	1.5	2.2	2.3	2.5	1.3	1.4	1.6
Australia	0.8	1.6	2.0	2.4	2.8	2.8	2.4	2.4	2.4	1.0	1.6	2.6
Eurozone	0.2	0.5	0.8	1.0	1.1	1.4	1.6	1.7	1.7	0.7	0.7	1.3
Austria	0.0	0.0	1.0	1.0	1.2	1.4	1.4	1.4	1.4	-1.0	0.3	1.3
Spain	3.1	2.0	2.1	2.3	2.5	2.2	1.8	2.0	2.0	3.2	2.5	2.1
Netherlands	1.6	4.7	0.2	0.2	0.5	0.6	0.8	1.2	1.5	0.9	1.8	0.8
Belgium	0.8	0.0	0.8	1.2	1.2	1.2	0.8	1.2	1.6	1.0	0.8	1.1
Greece	0.5	1.3	2.4	2.1	2.3	1.3	2.3	2.1	2.1	2.2	1.7	2.0
Portugal	6.5	2.8	2.1	2.2	2.2	2.0	2.0	2.5	2.5	1.9	2.9	2.2
Switzerland	1.2	1.2	1.6	1.6	1.2	1.2	1.6	1.6	1.6	1.3	1.5	1.4
Sweden	1.0	1.3	1.1	0.7	0.8	1.1	1.4	1.4	1.4	0.5	1.0	1.1
Norway	1.3	1.5	1.7	1.7	1.7	1.7	1.7	1.7	1.7	1.0	1.6	1.7

Emerging Markets (YoY% growth)	4Q24F	1Q25F	2Q25F	3Q25F	4Q25F	1Q26F	2Q26F	3Q26F	4Q26F	2024F	2025F	2026F
Bulgaria	2.4	2.4	2.5	2.4	2.4	2.6	2.8	2.6	2.6	2.3	2.4	2.6
Croatia	2.8	3.3	2.9	2.8	2.9	2.7	2.6	2.3	1.8	3.6	3.0	2.4
Czech Rep.	1.6	1.7	2.1	2.2	2.4	2.5	2.5	2.5	2.5	1.0	2.1	2.5
Hungary	0.4	0.4	0.6	2.7	4.2	4.8	5.1	4.3	3.3	0.5	2.0	4.4
Poland	3.2	3.0	2.4	3.7	4.0	3.8	3.1	2.9	3.8	2.9	3.2	3.4
Romania	0.3	1.1	1.4	1.8	1.7	2.0	2.3	2.6	2.8	0.7	1.6	2.5
Turkey	2.0	0.9	2.2	3.1	3.8	4.7	4.2	3.8	3.5	2.9	2.6	4.0
Serbia	3.3	3.8	4.0	4.3	4.2	4.3	4.3	4.3	3.8	3.9	4.1	4.2
Azerbaijan	3.0	2.0	2.5	3.0	3.0	3.5	3.0	2.5	2.0	4.1	2.6	2.8
Kazakhstan	3.6	5.4	5.5	5.3	5.7	4.0	3.8	5.0	5.0	4.8	5.5	4.5
Russia	3.8	3.0	2.5	2.0	1.5	1.0	0.5	0.0	-0.5	4.1	2.3	0.3
Ukraine	2.1	2.2	3.0	4.0	4.5	4.6	4.3	4.0	4.0	4.0	3.3	4.3
China	5.4	4.4	4.8	4.8	4.5	4.5	4.6	4.0	3.9	5.0	4.6	4.2
India	6.6	6.6	6.8	6.9	6.9	7.3	7.3	7.3	7.3	6.9	6.8	7.3
Indonesia	5.0	5.1	5.1	4.9	5.0	5.0	5.0	5.1	5.1	5.0	5.0	5.1
Korea	1.2	0.3	1.1	1.6	2.1	2.2	2.0	1.9	1.8	2.1	1.3	2.0
Philippines	5.2	5.5	6.6	6.3	6.0	6.1	6.1	5.9	5.7	5.7	6.1	6.0
Singapore	2.1	2.4	2.5	2.6	2.7	2.6	2.8	2.6	2.6	3.4	2.6	2.7
Taiwan	3.3	3.3	2.8	3.1	3.7	3.5	3.0	3.1	2.7	4.7	3.2	3.0

Norway: Forecasts are mainland GDP
Source: ING estimates

CPI Forecasts (pa)

YoY%	4Q24F	1Q25F	2Q25F	3Q25F	4Q25F	1Q26F	2Q26F	3Q26F	4Q26F	2024F	2025F	2026F
US	2.7	2.8	2.8	2.9	3.4	3.0	3.0	2.6	2.3	3.0	3.0	2.7
Japan	2.9	3.7	3.3	2.7	2.0	1.6	1.6	1.9	2.0	2.7	2.9	1.8
Germany	2.5	2.7	2.4	2.3	2.1	1.8	1.9	2.1	2.2	2.5	2.4	2.0
France	1.7	1.6	1.5	1.6	2.2	2.0	2.0	2.0	2.0	2.3	1.7	2.0
UK	2.5	2.8	2.9	3.3	3.2	2.8	2.3	2.3	2.3	2.5	3.1	2.4
Italy	1.3	1.7	1.6	1.8	2.0	2.0	2.1	2.2	2.2	1.1	1.8	2.1
Canada	1.9	1.9	1.5	2.1	3.0	3.3	2.7	2.0	1.7	2.4	2.1	2.4
Australia	2.5	2.2	1.9	2.3	2.8	2.8	2.7	2.5	2.4	3.2	2.3	2.6
Eurozone	2.3	2.5	2.4	2.3	2.3	2.2	2.2	2.2	2.2	2.4	2.4	2.2
Austria	1.9	2.5	2.2	2.1	2.1	2.1	2.1	2.1	2.1	2.9	2.2	2.1
Spain	2.4	2.6	2.2	2.0	2.0	2.1	2.1	2.1	2.1	2.8	2.2	2.1
Netherlands	3.7	3.1	3.3	2.9	2.6	3.1	2.6	2.1	2.2	3.2	3.0	2.5
Belgium	2.8	3.8	2.8	2.2	2.0	2.1	2.2	2.1	2.1	3.0	2.5	2.1
Greece	3.0	2.9	2.6	2.3	2.4	2.4	2.4	1.9	1.9	3.0	2.5	2.1
Portugal	2.8	2.4	2.1	2.0	2.0	2.1	2.2	2.2	2.1	2.7	2.1	2.2
Switzerland	0.9	0.7	0.8	0.9	0.8	0.9	0.9	1.0	0.9	1.1	0.8	0.9
Sweden	1.0	0.6	0.8	1.5	1.5	1.5	1.6	1.5	1.5	1.8	1.1	1.5
Norway	2.2	2.4	2.4	2.4	1.9	2.2	2.2	2.2	2.2	3.1	2.4	2.2
Bulgaria	2.1	3.6	4.4	4.6	4.7	2.9	2.8	2.9	3.0	2.4	4.3	2.9
Croatia	2.4	3.9	3.5	3.1	2.8	2.7	3.3	3.5	3.8	3.0	3.4	3.3
Czech Republic	2.9	2.7	2.6	2.6	2.9	2.6	2.5	2.4	2.4	2.4	2.7	2.5
Hungary	3.8	5.1	4.9	5.1	5.4	3.8	3.6	3.4	3.1	3.7	5.1	3.5
Poland	4.8	5.6	5.2	3.9	3.8	3.3	3.2	2.8	2.6	3.7	4.7	3.0
Romania	4.8	4.7	5.5	4.9	4.8	4.5	4.3	4.1	3.8	5.6	5.0	4.4
Turkey	44.4	39.3	34.4	28.6	27.0	21.6	19.9	19.2	18.2	58.5	33.0	20.2
Serbia	4.0	4.6	4.5	4.0	3.5	3.4	3.5	3.5	3.6	4.7	4.1	3.5
Azerbaijan	4.2	5.7	6.1	4.5	4.5	4.1	4.6	5.1	5.7	2.2	5.2	4.9
Kazakhstan	8.5	8.8	9.2	8.7	8.1	7.3	6.8	6.5	6.4	8.7	8.7	6.7
Russia	9.0	10.0	9.7	9.1	7.7	6.7	6.3	5.9	5.6	8.4	9.1	6.1
Ukraine	12.0	14.0	13.5	12.0	8.4	7.0	6.7	6.5	6.3	6.5	12.0	6.6
China	0.2	0.4	0.7	0.8	1.2	1.1	0.7	1.0	2.0	0.2	0.8	1.2
India	5.1	4.9	4.7	3.8	3.5	4.9	4.9	4.7	4.4	4.8	4.6	4.7
Indonesia	2.2	2.1	2.0	2.1	2.2	2.2	2.2	2.2	2.2	2.1	2.1	2.2
Korea	1.6	1.8	1.8	1.7	1.8	1.5	1.6	1.9	2.1	2.3	1.8	1.5
Philippines	2.7	2.4	2.5	3.0	3.2	3.5	3.5	3.5	3.5	3.4	2.8	3.5
Singapore	2.0	2.2	2.0	1.8	1.8	2.3	2.4	2.4	2.4	2.5	2.0	2.4
Taiwan	1.9	2.5	2.4	2.3	2.1	1.5	1.5	1.4	1.5	2.2	2.3	1.5

*Quarterly forecasts are quarterly average; yearly forecasts are average over the year, HICP for Eurozone economies

Source: ING estimates

Oil and natural gas price forecasts (avg)

	1Q25F	2Q25F	3Q25F	4Q25F	1Q26F	2025F	2026F
Brent **($/bbl)**	76	74	75	71	67	74	70
Dutch TTF **(EUR/MWh)**	50	45	42	44	37	45	33

Source: ING estimates

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