NORTHERN TRUST

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GLOBAL ECONOMIC OUTLOOK

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- **Believe It or Not**

Ripley's is an American franchise that features strange events, unusual objects, and unbelievable stories. It's tagline is "Believe it or not." The U.S. administration has also initiated some unusual actions that defy belief, and which could permanently alter the international trade landscape.

The first few months of 2025 promised to be bumpy, but not many expected the world to be on the brink of a full-blown trade war. More tariff announcements are in sight. Whatever shape they take, they will be a significant expansion of trade restrictions.

We expect average duties on goods arriving in the United States from most parts of the world to reach 10%, with Chinese imports subject to significantly higher rates. This substantial shift (from an average rate of just over 2% in 2024) will put a significant dent in economic growth in many places. Central banks will have to navigate carefully, as tariffs tend raise inflation and slow growth.

Following are our thoughts on how top areas are faring.

United States

- High uncertainty is cooling both business investment and consumer confidence. A downshift from above-potential to slower growth is our base case. Our forecast assumes actual average tariffs do not reach their maximum threatened level and that many of them will eventually be rescinded (at least partially). But the higher the levies go and the longer they remain in place, the stronger the probability of a downturn.
- At its March meeting, the Federal Open Market Committee held rates steady. Their decision came with cautious guidance of slower growth and higher inflation through 2026. Chair Powell acknowledged uncertainty across several policy domains (trade, immigration, fiscal policy and regulation), supporting a patient stance. Sticky inflation and a resilient labor market will keep the Federal Reserve sidelined for the time being. We anticipate one cut later this year, followed by two more in 2026.

Canada

- Coming into 2025, the Canadian economy was on the mend. But a path of sustained improvement is no longer in sight, amid the looming trade war with the United States. High tariff levels are likely to remain in place until the renegotiation of the United States-Mexico-Canada Agreement in 2026. Reciprocal tariffs along with the potential industry-specific duties on April 2 will amplify the pain. Given the Canadian economy's high dependence on the United States and trade, the economy faces elevated risk of recession. But that is not our base case.
- The Bank of Canada (BoC) has lowered interest rates to 2.75%, the mid-point of its neutral range. Though the central bank cut its policy rate by 25 basis points at the March meeting to hedge against downside risk, it also warned of the risk of tariff-fueled

higher inflation. We expect the BoC to cut again in June and stay on the sidelines thereafter.

Eurozone

- The prospect of higher government spending on defense and infrastructure in countries like Germany has created some exuberance around the eurozone's growth prospects. That said, the lift to activity from fiscal stimulus may take time to materialize. There is also a risk that any near-term positives will be more than offset by a further escalation in trade tensions. The U.S. administration is likely to apply reciprocal tariffs on imports from Europe, in addition to the new 25% duty on autos. This would exert downward pressure on growth in 2025, especially on countries like Germany and Italy.
- The European Central Bank (ECB) cut its key policy rates by 25 basis points at its March meeting. But the central bank is starting to sound more cautious on further rate cuts with President Lagarde suggesting that the direction for rates was "no longer as straightforward." Given the potential positive spillovers from the fiscal boost in 2026 and the risk of higher prices from tariffs in the near term, we think the ECB will conclude its easing cycle after another 50 basis points of cuts this year.

United Kingdom

- The U.K. economy entered 2025 on a weak footing, with GDP contracting in January. Business surveys have been softer, owing to uncertainty around trade and the upcoming increase in employers' national insurance contributions. Fiscal headroom has tightened, which will force the government to cut spending. Though the U.K. is not in the direct firing line of the Trump administration, knock on effects of a global trade war will have a bearing on growth.
- The Bank of England's Monetary Policy Committee (MPC) voted by a majority of 8-1 to keep its interest rate at 4.5% at the March meeting. The MPC reiterated its "gradual and careful approach" to policy easing amid rising global trade uncertainty. Wage growth in Britain remains stubbornly high, well above the rate consistent with 2% inflation. Inflation expectations have been rising, further complicating the backdrop for the central bank. But given the subdued growth outlook and fiscal tightening, we share Governor Bailley's view that "interest rates are on a gradually declining path."

Japan

- America's reciprocal duties are going to have a minimal direct impact on most Japanese industries, given it has only a moderate tariff differential with the U.S. That said, 25% levies on metals and automobiles will prove to be painful for Japan's exports. President Trump's recent criticism of the weaker yen may be a prelude for duties on Japanese products. We expect Japan's economy to be supported by gradual improvements in consumption on the back of a recovery in real wages, but the external backdrop is set to become unfavorable.
- Initial agreements from Shunto wage negotiations are pointing toward another year of strong wage gains. Even though wages and price conditions are on track with the Bank of Japan's (BoJ) outlook, the central bank is in no rush to raise rates. The BoJ remained on hold at this month's meeting, with Governor Ueda conveying caution over the potential impact from U.S. trade policy. We expect gradual normalization of monetary policy with a hike every six months; rates are set to reach a neutral rate of 1.0% in early 2026.

China

- Chinese exports are highly vulnerable to U.S. trade policies, owing to the massive size of the bilateral trade deficit and the strategic nature of the nations' competition. The Chinese are already facing the brunt of Trump's tariffs. Levies on Chinese imports have been increased twice by a total of 20%. Further announcements of more punitive tariffs would be no surprise.

The deteriorating external backdrop will only aggravate domestic woes for the Chinese economy. Reduced demand for Chinese goods will add to excess capacity, further intensifying deflationary pressures. Last year's plan for housing inventory destocking found weak buy-in. The job market is deteriorating as firms hold back hiring. Credit demand remains weak, with an outright contraction in loans to households and softer demand from corporates last month.

- Policymakers rolled out more easing in March's Two Sessions meeting, but missed an opportunity to be more aggressive. The Two Sessions attempted to signal that policymakers will deliver robust government support, but the scale and composition of stimulus measures will not fully offset domestic economic hardships or cope with rising external headwinds. Already-elevated debt levels will limit policymakers' capacity to intervene.

Australia

- The Australian economy ended 2024 on a relatively favorable footing. The recovery is being underpinned by a strong labor market, moderating inflation, tax cuts and cost-of-living rebates. The federal budget extended support measures ahead of the upcoming election. Given its small direct trade exposure to the U.S., reciprocal tariffs will likely have a limited impact on the Australian economy. In our view, the second-order effects of a weaker Chinese economy will prove to be more worrisome for Australian exporters.
- The labor market in Australia remains tight, with forward-looking indicators showing no signs of easing. With domestic demand improving and productivity still weak, we continue to expect the Reserve Bank of Australia (RBA) to tread cautiously. The RBA is likely to deliver only one more cut towards the end of the year.

Global Economic Forecast – March 2025

United States	2023	2024	2025F	2026F
Real GDP (Q4-Q4 % change)	3.2	2.5	1.7	1.9
Unemployment Rate, EOP (%)	3.7	4.1	4.2	4.1
Inflation (CPI, Q4-Q4, %)	3.2	2.6	3.0	2.7
Policy Rate (Top), EOP (%)	5.50	4.50	4.25	3.75
Canada	**2023**	**2024F**	**2025F**	**2026F**
Real GDP (Q4-Q4 % change)	1.2	2.4	0.2	1.5
Unemployment Rate, EOP (%)	5.8	6.7	7.0	6.9
Inflation (CPI, Q4-Q4, %)	3.2	1.9	2.6	2.2
Policy Rate (Top), EOP (%)	5.00	3.25	2.50	2.50
Eurozone	**2023**	**2024**	**2025F**	**2026F**
Real GDP (Q4-Q4 % change)	0.2	1.2	0.7	1.3
Unemployment Rate EOP (%)	6.5	6.3	6.6	6.5
Inflation (CPI, Q4-Q4, %)	2.7	2.2	2.3	2.0
Policy Rate, EOP (%)	4.50	3.15	2.15	2.15
Deposit Rate, EOP (%)	4.00	3.00	2.00	2.00
United Kingdom	**2023**	**2024**	**2025F**	**2026F**
Real GDP (Q4-Q4 % change)	-0.3	1.4	1.1	1.3
Unemployment Rate EOP (%)	4.0	4.4	4.7	4.6
Inflation (CPI, Q4-Q4, %)	4.2	2.5	3.0	2.3
Policy Rate, EOP (%)	5.25	4.75	3.75	3.50
Japan	**2023**	**2024**	**2025F**	**2026F**
Real GDP (Q4-Q4 % change)	0.9	1.2	0.8	1.0
Unemployment Rate EOP (%)	2.5	2.4	2.4	2.4
Inflation (CPI, Q4-Q4, %)	2.9	2.9	2.5	2.0
Policy Rate, EOP (%)	-0.10	0.25	0.75	1.00
China	**2023**	**2024**	**2025F**	**2026F**
Real GDP (Q4-Q4 % change)	5.3	5.4	3.5	3.1
Unemployment Rate EOP (%)	5.1	5.0	5.1	5.1
Inflation (CPI, Q4-Q4, %)	-0.3	0.2	0.5	0.5
7-day Reverse Repo, EOP (%)	1.80	1.50	1.10	0.90
Australia	**2023**	**2024F**	**2025F**	**2026F**
Real GDP (Q4-Q4 % change)	1.5	1.3	1.9	2.2
Unemployment Rate EOP (%)	4.0	4.0	4.5	4.4
Inflation (CPI, Q4-Q4, %)	4.0	2.4	3.2	2.5
Policy Rate, EOP (%)	4.35	4.35	3.85	3.35
Exchange rates (EOP)	**Jun-2025**	**Sep-2025**	**Dec-2025**	**Mar-2026**
USD/CAD	1.43	1.41	1.38	1.37
EUR/USD	1.07	1.08	1.09	1.10
GBP/USD	1.27	1.28	1.29	1.30
USD/JPY	148.0	147.0	145.0	143.0
USD/CNH	7.28	7.32	7.35	7.37
AUD/USD	0.64	0.65	0.66	0.67