Economic Research View:
Global Investment Environment Outlook 2025

Nomura Asset Management Co., Ltd. Published January 7, 2025

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Global growth was solid in 2024 despite cumulative monetary tightening. Looking forward, the global economy is expected to slow down but remain resilient in 2025. The policies of the new Trump administration, which will take office in January, will create volatility and regional divergence.

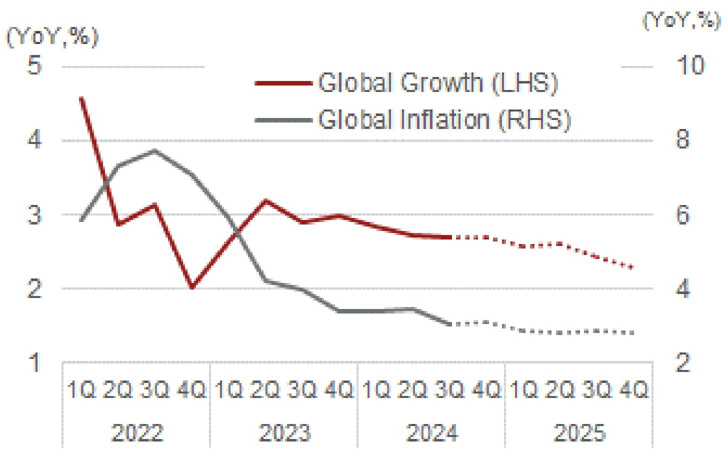
In the bond market, long-term yield in the United States and Europe is projected to decline moderately as central banks cut policy rates. In Japan, long-term yields are expected to remain range-bound as the Bank of Japan raises policy rates further. In the foreign exchange market, the US dollar will likely remain strong.

In the stock market, the price return is expected to be generally in line with the growth of corporate earnings. By country and region, US stocks will likely outperform. Although the yen's moderate appreciation will be a headwind to corporate earnings, Japanese stocks will likely outperform other regions in US dollar terms on the back of improving real income conditions and ongoing governance reforms.

Global Economic Environment Outlook

- In 2024, the global economy remained robust despite cumulative monetary tightening. While avoiding a noticeable slowdown, labor market conditions eased and inflation slowed. After reassessing the balance between inflation and labor market stability, major central banks began to cut policy rates toward neutral levels in order to adjust the degree of monetary tightening. The European Central Bank (ECB) and the US Federal Reserve (the Fed) started rate cuts in June and September, respectively.
- In 2025, the global economy will slow down but remain resilient. The US economy will keep high growth rates supported by a solid real income environment despite “high for longer” policy rate. The Euro region economy is expected to accelerate moderately as the effects of the rate cuts gradually materialize. The Japanese economy is likely to be supported by an improvement in real income conditions due to wage hikes and capex to deal with labor shortages and DX. The Chinese economy will remain weak, but the stimulus measures is expected to contribute to avoiding serious deceleration.
- The policies of the new Trump administration inaugurated in January will create volatility and regional divergence in the economic activities. Although highly uncertain, we assume that the US will raise tariff rates on China, Europe, Japan, and other Asian countries by around 10% from the second half of 2025. In the first half in 2025, the global economy will be supported by “frontloading of exports” in preparation for the tariff hikes, but economic activity will slow in the second half of 2025 when the tariff rates are actually raised. Countries subject to higher tariffs will face a decline in exports to the United States and a drag on capex due to increased uncertainty. In the US, the reacceleration of inflation and deterioration in sentiment caused by the tariffs will also depress economic activity. However, the negative impact of the tariffs on the economy may be offset in 2026 by possible fiscal expansions such as the extension of the personal income tax cut. In the Euro area, on the other hand, fiscal rules will require the government to maintain a stance of austerity, and the hurdles for fiscal expansion like those in the United States are high. Given the asymmetry of the effects of tariffs and the scope for fiscal expansion, the policies of the new Trump administration are likely to give the US economy a relative advantage.

Figure 1. Global Growth and Inflation

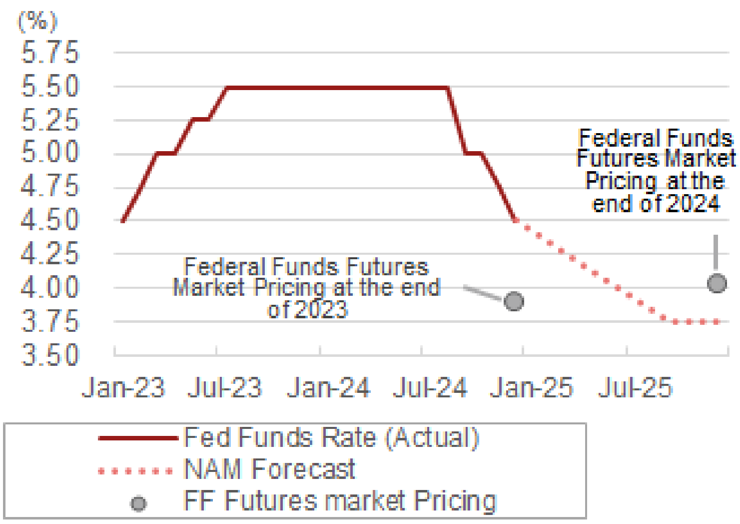


Note: Dotted line show NAM house view as of December 16, 2024. The actual values for growth rates and inflation rates are based on data available as of the preceding date.
Source Nomura Asset Management based on the data from Oxford economics

Bond Market Outlook

- In 2024, although the Fed started to cut policy rates, the scale of rate cuts was more modest than was priced at the end of the previous year, which resulted in a rise in long-term yield (see Figure 3). In 2025, long-term yields are expected to decline moderately, while monitoring the terminal rate.
- In the US, rate cuts are likely to continue toward the neutral rate, but President-elect Trump's policies of tariff hikes, immigration restrictions, and fiscal expansions will all increase inflationary pressure. As the economy remains resilient, the Fed, wary of inflation risks, is likely to slow the pace of rate cuts and pause in the second half of 2025 at a level slightly above what is expected to be the neutral rate. In this situation, the extent of decline in long-term yields is expected to be limited.
- In Euro area, wage growth is expected to slow rapidly as labor market conditions ease, and inflation is expected to fall below the 2% target in the second half of 2025. The ECB is expected to cut policy rates faster than the Fed, and the policy rate is expected to fall to an accommodative level in the second half of 2025. Reflecting such divergence in monetary policy, the gap between long-term yields between the US and Germany is likely to remain wide.
- In Japan, on the other hand, an additional rate hike is expected in early 2025, which will exert upward pressure on JGB yields. However, the Bank of Japan will keep the policy rate unchanged thereafter, citing uncertainties in overseas economies and policy developments, and the next rate hike is likely to be after 2026. Given that the market is already pricing in some additional rate hikes and that global interest rates are expected to move downward, long-term yield in Japan are likely to remain range-bound rather than continuing to rise.

Figure 2. US Policy Rate and Market Pricing

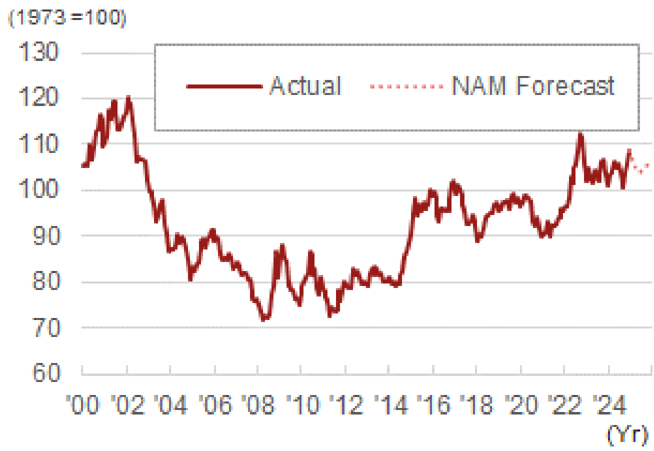


Note: NAM forecast as of December 16, 2024. FF rates are shown as upper limit of the target range
Source: Nomura Asset Management based on the data from Bloomberg.

Currency Market Outlook

- In the foreign exchange market in 2024, the US dollar appreciated, reflecting a widening interest rate differentials between the US and other countries. In 2025, the US dollar is expected to remain at an elevated level, although the movements of each currency could differ, reflecting relative economic strength and diverging monetary policy stances (see Figure 4).
- The Euro is expected to move within a range. When the US dollar is sold as risk appetite improves, the Euro is likely to be bought as a counterparty. However, in the second half of 2025, the ECB is expected to cut policy rates to below neutral level, while the Fed is expected to pause rate cut at above neutral level. At the same time, uncertainty due to higher tariffs is likely to materialize. In such an environment, the Euro is likely to depreciate again.
- The Japanese yen is expected to move in tandem with the interest rate differentials between Japan and the US. With US yields declining moderately and JP interest rates rising or remaining flat, the interest rate differentials are likely to narrow and cause appreciation pressure on the yen. However, given that the extent of narrowing interest differential is likely to be small, and that structural deterioration of demand-supply balance caused by digital deficits and new NISA (Nippon Individual Savings Account) remain, the possibility of a significant yen appreciation is limited. There is limited speculative yen-selling positions driven by carry trades, which contributed to the yen's sharp appreciation in the summer of 2024.
- The Chinese yuan will depreciate against the US dollar if tariffs on China are raised, as Chinese authorities ease their defensive stance somewhat. A weaker yuan could cause depreciation pressure on other Asian currencies, which have strong trade ties with China

Figure 3. US dollar Index

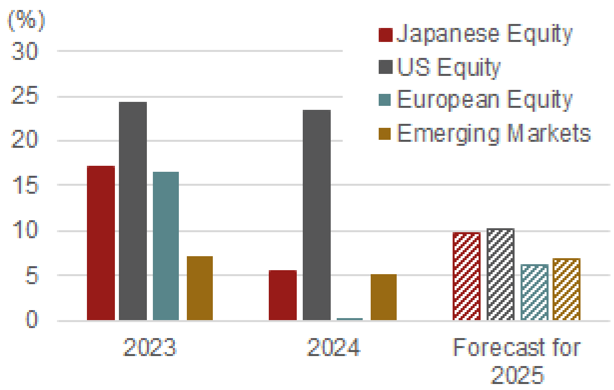


Note; NAM forecast is based on the house view for the Euro and yen as of December 16, 2024.
Currencies other than the Euro and yen are calculated based on the weight of the USD index, assuming the same rate of change as the Euro.
Source Nomura Asset Management based on the data from Bloomberg

Equity Market Outlook

- Global equities rallied for the second consecutive year in 2024, driven by economic resilience, expectations for AI-related stocks, and rate cuts. The S&P500 posted annual returns of about 23%, followed by about 24% in 2023. The big gains were driven by P/E ratios, with S&P500's P/E ratio rising to levels not seen since the IT bubble era around 2000, excluding the pandemic period. Against this backdrop, further expansion in valuations is unlikely in 2025, and equity prices are expected to rise in line with corporate earnings.
- By country, US will likely outperform. In addition to the relatively robust growth, AI-related stocks will drive earnings growth. Among President-elect Trump's policies, higher tariffs are a negative factor, but deregulation and tax cuts can bring a net positive impact on corporate activity. On the other hand, the Euro area is subject to geopolitical tensions in addition to continued downward earnings revisions. Emerging markets are likely to be hit hard by the risk of tariffs and the persistently high US dollar.
- Japan's equity market posted high returns, with the TOPIX rising about 18%. However, corporate earnings were boosted by the depreciation of the Japanese yen, and US dollar performance was not significantly different from that of major markets excluding the US (see Figure 5). Although the moderate appreciation of the yen is expected to be a headwind to corporate earnings in 2025, it is likely to be supported by improvements in real income conditions resulting from wage increases, continued corporate reforms, and relatively little overheating of valuations. Although yen-denominated returns will be lower than in 2024 due to the appreciation of the yen, US dollar returns are expected to exceed those of major markets.

Figure 4. Equity Index Return in USD terms



Note; NAM forecast is based on the house view as of December 16, 2024.
Source Nomura Asset Management based on the data from Bloomberg

Note: This commentary is based on Nomura Asset Management's house view discussed at the Investment Environment Assessment Meeting.