Macro Strategies Outlook for 2025: Growth divergence and policy uncertainty

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In brief

- 2024 unfolded largely as anticipated with US outperformance, global disinflation, central bank easing and ongoing geopolitical tensions. The year was very positive for equities, though not without a couple of hiccups, while it was mediocre for bonds.
- 2025 looks set to be another good year for the US, but not so good for Europe and China. We expect US growth to remain strong, helped by the pro-America policies of the incoming administration. By contrast, European growth remains weak and the political landscape is more unstable, while China has yet to deliver stimulus with the potential to push growth higher.
- We are comfortable taking modest long directional equity risk, within which we are most exposed to the US. However, we expect to adjust our net equity exposure dynamically, in order to manage through potential volatility amid uncertainty about policy and the inflation trajectory. We retain high conviction in US exceptionalism, which influences our fixed income and currency strategies.
- Technology adoption, healthcare innovation, emerging market consumption and climate change remain the key mega forces behind our secular themes. In 2025, we believe the biggest influencer on opportunity in this part of our portfolio will be artificial intelligence (AI).
- There is excitement in secular stories outside of AI, most noteworthy of which are areas related to healthcare innovation. We continue to monitor new drug development, including obesity drugs, and think US de-regulation under Trump will be helpful to accelerate activity.

Introduction

2025 looks set to be a good year for the US and not so good for Europe and China. 2024 saw a continuation of the divergence story that has held since the Global Financial Crisis. We expect this narrative to persist, helped by the 'America First' policy agenda of the incoming US administration. By contrast, European growth remains weak and the political landscape is more unstable, while China has yet to deliver the stimulus measures needed to push growth meaningfully higher. Another story that will continue into 2025 is AI, where we expect increased enterprise and consumer adoption.

Looking back on 2024

2024 unfolded largely as anticipated with US outperformance, global disinflation, central bank easing and ongoing geopolitical tensions. The year was positive for equities and bonds but not without a couple of hiccups as central banks did not ease as much as markets had priced, while US growth data faltered mid-year.

The biggest uncertainty of the year that played out in markets was the race for the White House. When President Biden initially handed the Democratic Party baton to Harris, a Democratic victory looked possible. What was expected to be a close race fast became an outright Republican victory, triggering a reshuffle in markets towards the anticipated Trump 2.0 playbook.

AI developments continued, pushing the narrative from a potential bubble to an evident broadening out. This development not only impacted the tech sector but also supported other secular trends, such as biologics, where AI is quickening progress and leading to new discoveries. The biologics sector was also supported by rising hopes for the impact of obesity medication.

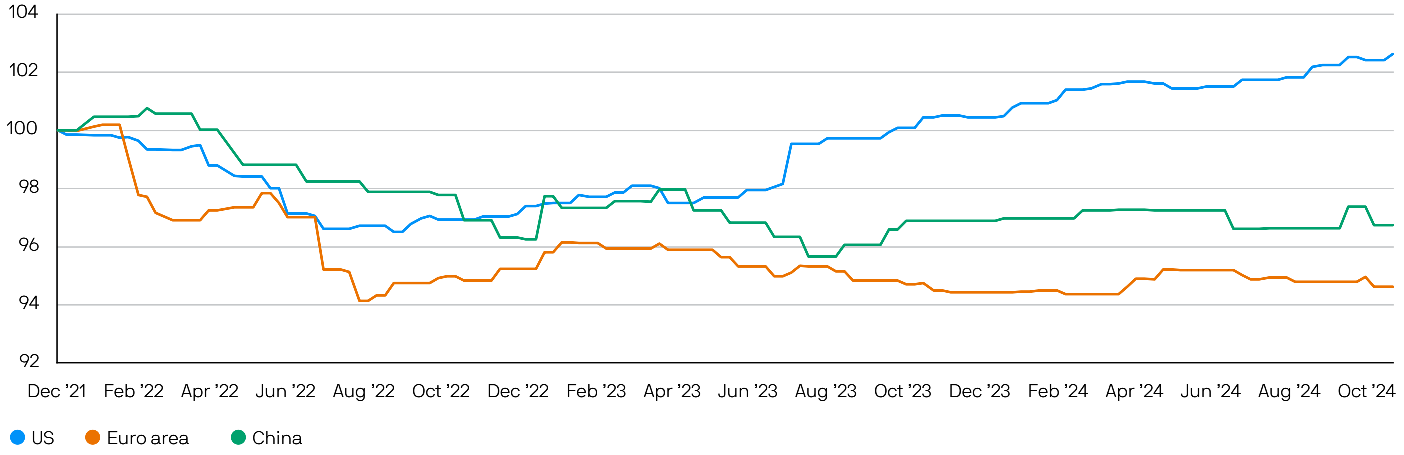
The big picture for 2025

What do we expect for this quarter century year? Unexcitingly, much the same as 2024. We believe US exceptionalism, disinflation and geopolitical tensions will continue. However, disinflation is less certain, central bank action may be more divergent and geopolitical tensions are potentially greater as Trump pursues an 'America First' policy. The latter might be counterbalanced with some form of resolution in Ukraine and de-escalation in the Middle East, which is happening as of the time of writing.

The relative strength of the US economy is central to our macro view. **Exhibit 1** shows US growth revisions marching steadily higher, while the rest of the world has plateaued.

Exhibit 1: Pronounced divergence in US, euro area and China growth revisions

JPMorgan Forecast Revisions Index



Source: Real GDP forecasts. Changes reflect %-point revision to 4-quarter rolling percent change forecast. J.P. Morgan Asset Management, Bloomberg; data as of 22 November 2024.

Around the world

US

US growth is strong and above trend versus history, supported by a strong consumer. We expect decent employment growth, decent wage growth and a strong wealth effect to result in continued consumption. The policy of the new administration should provide a further boost to growth. Against this backdrop, disinflation may continue but the risks are more balanced than last year.

Compared to 2016, the Republicans have a greater weight across the Senate and Supreme Court but a narrower margin in the House. In terms of policy, we expect President Trump to be fiscally expansionary mainly through rolling the Tax Cuts and Jobs Act and deregulating across sectors. We also expect the new President to use his executive powers on day 1 to restrain immigration and implement tariffs with a particular focus on China. This sequencing may initially penalise growth before more support is provided later in 2025. While we know the direction that Trump wants to travel, we are less certain on the magnitude.

In terms of the economic backdrop, today we are experiencing moderately high inflation, whereas in 2016 inflation did not pose any constraint to policy action. Given this backdrop, one thing that is central to our view is that inflation is going to be the master of a lot of America First policy setting, with a focus on averting higher inflation outcomes.

The Federal funds rate is also higher today than in 2016, and the corresponding costs to the government in terms of interest on its debt are significantly higher. This situation poses a budgetary constraint when we think about fiscal policy decisions towards the end of next year.

In terms of Federal Reserve (Fed) action, we expect the US central bank to continue on its modest easing path, given unemployment and inflation are close to target. However, there is uncertainty as to how far the Fed can cut, and policy decisions will be data dependent.

● Portfolio implications

A positive US growth backdrop supports taking more directional equity risk, which we have added since the election. The ‘America First’ stance held by Trump should be positive for US domestic assets, where we own select banks, homebuilders and industrials.

However, we expect to adjust our net equity exposure dynamically as policy uncertainty may fuel more volatility. Similarly, we anticipate being tactical in US duration with a focus on market positioning.

US exceptionalism versus the rest of the world and tariffs should continue to support the US dollar, particularly against Chinese-exposed currencies and the euro.

Around the world

Europe

European growth is weak with the threat of tariffs, weak consumer and business confidence, weak demand from China – a key trading partner – and low productivity. Coupled with slowing inflation, we are more convinced that we will see significant European Central Bank easing, most likely taking rates into accommodative territory.

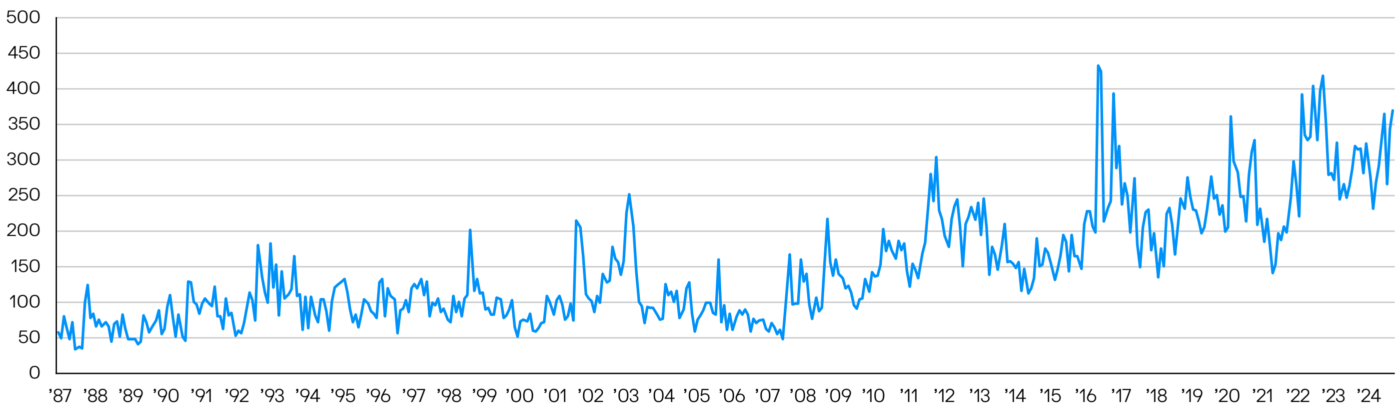
Politics also adds to European fragility, with the French and German governments collapsing and both likely to go to the polls in 2025. The weakening of political structures raises the risk of less fiscal consolidation. This backdrop is illustrated by the political uncertainty index rising (**Exhibit 2**).

The new US administration darkens the outlook for Europe as US trade and industrial policy will be unfriendly. We anticipate more fiscal spend next year as the region attempts to counterbalance this negative impulse. Some of this fiscal spend will be on defence to support Ukraine amid expectations Trump will stop US spending on the war and push for a compromise solution. Even if Europe increases its spending, this may not maintain the war and a resolution of sorts becomes more likely in 2025.

● Portfolio implications

We are long German Bunds and UK Gilts, which we believe are not fully pricing our view of weaker growth and continued disinflation. We are short the euro against the US dollar to reflect our relative growth view.
In equity, we took advantage of French political instability in the summer to add to select luxury goods and industrials names.

Exhibit 2: European political uncertainty index has moved higher



Source: J.P. Morgan Asset Management, Bloomberg; data as of 22 November 2024.

Around the world

China

The Chinese economy has been struggling since the pandemic, with growth remaining weak (**Exhibit 3**). Significant stimulus in 2024 has potentially put a floor under growth, but the focus has been on risk mitigation and stability, not the provision of meaningful stimulus to help achieve strong economic growth. The stimulus may help the property market, but it is doing so by reducing supply rather than increasing demand. Therefore, many typical beneficiaries of Chinese stimulus remain vulnerable and will likely reprice lower, with only local equities better supported.

We expect China to be the worst hit in the early days of Trump's second term. Policy action will come directly from the White House, not requiring congressional approval, with a focus on raising tariffs materially on Chinese imports. China is less exposed than in 2016 but tariffs are expected to be as high as 60%, so this will be impactful and increase geopolitical tensions.

● Portfolio implications

We are reflecting the negative China outlook in currency. However, we are long the Chinese domestic equity market via futures as we think policymakers will provide support to the stock market.

Exhibit 3: Falling yields reflect falling growth expectations

China 10-year government bond yield

Source: JP Morgan China Forecast Revisions Index. J.P. Morgan Asset Management, Bloomberg; data as of 5 December 2024.

Around the world

Asia Pacific ex China

The region is likely to suffer with tariffs and a weaker China but there are bright spots. For Taiwan and Korea, AI investment is pushing up demand for high bandwidth memory though broader tech exports have been weaker. In India, structural growth has been very strong and although there has been some recent weakening, we are not concerned and expect the economy to rebound modestly.

Japan is seeing inflation rise structurally due to tightness in its labour market, which we expect to lead to tightening by the Bank of Japan. At the same time, we expect more fiscal spend as the government seeks to win back favour among voters after a surprise rebuke of the ruling party in the recent general election.

● Portfolio implications

To reflect the negative tariff and China growth view, we are short China-centric currencies such as the Australian dollar. We are leaning into the positive AI backdrop with exposure to Asian semiconductor manufacturers, and into the India growth story with exposure to select private banks. Meanwhile, our Japanese view supports being short Japanese government bonds.

Macro cycle dashboard

The dashboard illustrates our current view on macro cyclical conditions by region and component part, i.e. growth, inflation, sentiment and liquidity. The phases shown reflect whether the economy is accelerating or decelerating, above or below trend. In the final row, we show the aggregate regional phase and whether it has been changed since the prior month's deep-dive discussion. As detailed already, today the dashboard highlights the divergence we see by region, particularly in US growth vs. the rest of the world. The dashboard guides our discussions on expectations by asset class, sector, factor and FX, influencing the composition of our portfolio and individual security selection.

	US	Europe	China	Asia Pacific ex-China
Growth	Expansion	Contraction	Contraction	Contraction
Inflation	Expansion	Slowdown	Contraction	Slowdown
Sentiment	Expansion	Contraction	Recovery	Slowdown
Liquidity	Recovery	Recovery	Recovery	Slowdown
Macro cycle phase	Expansion =	Contraction =	Recovery =	Contraction =

Source: J.P. Morgan Asset Management; data as of 11 December 2024. US theme includes Canada. Opinions, estimates, forecasts, projections and statements of financial market trends are based on market conditions at the date of the publication, constitute our judgment and are subject to change without notice. There can be no guarantee they will be met.

Portfolio summary

Our macro view in aggregate is mixed, with significant regional divergence. We are comfortable taking modest long directional equity risk, within which we are most exposed to the US. However, we expect to adjust our net equity exposure dynamically to manage through potential volatility amid uncertainty about policy and the inflation trajectory. We retain high conviction in US exceptionalism, which influences our fixed income and currency strategies.

Secular equity trend highlights for 2025

Technology adoption, healthcare innovation, emerging market consumption and climate change remain the key mega forces behind our secular themes. In 2025, we believe the biggest influencer on opportunity in this part of our portfolio will be AI. We do not view this as a secular theme itself, but an overarching trend shaping many secular themes and cyclical opportunities.

The AI story is broadening out from training infrastructure to enterprise usage. This broadening is beneficial for the software infrastructure layer of the AI stack, with the emergence of AI assistance in enterprise and for consumers. It also supports our focus on select investments in hyperscalers, software providers, semiconductor manufacturers and consumer technology companies. We wrote about the AI landscape and investment opportunity in detail in a dedicated paper: 'Our Approach to Investing in Artificial Intelligence'.

There is excitement in secular stories outside of AI, most noteworthy of which is the narrative related to healthcare innovation. We continue to monitor new drug development, including obesity drugs, and think likely US de-regulation under the Trump administration will be helpful to accelerate activity. Another area of keen interest is India, where we see secular opportunity as we expect the growth of the middle class to be a long-term trend. We are already invested in Indian financials and are reviewing opportunities elsewhere in the market.

Conclusion

2025 will be marked by divergence in growth and policy between the US and the rest of the world. There is also an increased risk of higher inflation in the US, and rising geopolitical tension given Trump's tariff plans. Europe faces weaker growth and political turmoil, while China will likely only do enough to reduce left-tail risks rather than supercharge growth. Divergence and policy uncertainty will contribute to dispersion in asset prices and create more opportunities for us to express our fundamental views. Meanwhile, AI will be the determinant of most secular opportunities.

For further macro updates, please subscribe to our monthly webcast and/or speak to your usual **J.P. Morgan Asset Management representative**.

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