

2025 investment outlook: After the landing

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Key takeaways



Base case

We expect significant monetary policy easing to foster an attractive environment for risk assets as central banks achieve a “soft landing” of lowering inflation without a recession.

Downside scenario

There’s the risk of a policy mistake that causes global growth to undershoot. But we would anticipate central banks to enact more rate cuts to counteract it.

Upside scenario

There’s the potential for global growth to be stronger than we expected. Falling inflation and rate cuts could help drive a “Goldilocks” environment across most economies.

It’s time for our 2025 investment outlook, the product of much thought and analysis by some of the key investment professionals and thought leaders at Invesco. This is always a very collaborative effort, with a healthy amount of disagreement and discourse. At Invesco, we value diversity of views, and believe it ultimately strengthens our outcomes.

Our outlook provides a macro “base case” scenario that we believe is most likely. We also provide two alternate scenarios that clients might anticipate — an upside and a downside — as well as some of the “swing factors” that could also alter our expectations. And we provide asset implications for all three scenarios.

Our base case for markets and economies in 2025

Investment implications

Alternate scenarios

Swing factors

Our base case for markets and economies in 2025

After a steep climb to restrictive rates to curtail rapidly rising prices, most central banks all but declared victory over inflation in 2024. Yet many of the world’s major economies have been showing signs of slowing, with pockets of weakness such as slipping Eurozone Purchasing Managers’ Indexes, rising unemployment rates, and faltering consumer confidence pushing central banks to cut interest rates in the latter half of the year.

Looking into 2025, the key question remains whether central banks can steer the world’s major economies toward moderate growth while keeping inflation in check. New and old challenges, including geopolitical tensions and a new administration in the US, introduce uncertainties in the path ahead. We expect significant monetary policy easing to push global growth back to potential rates in 2025, fostering an attractive environment for risk assets as central banks achieve a “soft landing” of lowering inflation without a recession.

United States: We anticipate higher growth than other developed economies

Since mid-2024, views about the trajectory of US economic growth have been rotating between pessimism and optimism in fits and starts. Despite patches of weakness, we’ve continued to see resilient growth in the US.

Going into 2025, we expect the US economy will continue to grow near its potential rate. While leading indicators offer a mixed picture, we suspect that areas of weakness, especially from the manufacturing sector, offer limited insight due to post-pandemic swings in demand between goods and services. We believe a modest slowdown in growth to potential rates will continue in the US in the near term, given the restrictive monetary policy environment that has persisted for several quarters and continues to this day, despite recent policy changes. However, we believe the resilient labor market and strong overall household balance sheets should help spending and the broader economy continue to grow, and that continued

easing in financial conditions and continued real wage growth should help the US economy re-accelerate in 2025.

We believe the Federal Reserve (Fed) will lower its policy rate toward neutral in 2025, reducing the downward pressure of higher interest rates on growth. If growth shows signs of deceleration, the Fed has additional room for further policy easing, laying a positive backdrop for economic momentum through 2025.

We continue to expect the US to deliver higher growth than other developed economies, largely due to the combination of its favorable demographics and immigration, its business dynamism, and its healthy rate of productivity growth.

Eurozone: Rate cuts should help reverse the growth slowdown

After staging a rebound from its late-2023 slowdown in activity, the eurozone's recovery appears to have stalled. Key economies like France and Germany appear to have lost momentum, particularly in the manufacturing sector. The eurozone continues to be weighed down by structural challenges and demographic issues, which suggests continued economic divergence from the US.

Indeed, the eurozone economic model is challenged, especially Germany's export-driven growth model, given rising trade tensions with China and the threat of renewed tensions with the US given the return of a Trump administration. However, we note that any boost to the Chinese economy is likely to have positive spillovers for the eurozone. Though energy prices have come down from the surge triggered by Russia's invasion of Ukraine, they remain significantly higher than in the US or than the past. Fiscal consolidation in France, Germany, and Italy, as well as smaller eurozone economies, may also exert downward pressure on growth, investment, and consumption. Confidence may also suffer if trade relations with the US deteriorate.

We anticipate that the European Central Bank's (ECB) interest rate-cutting cycle will begin to reverse the growth slowdown. As we move through 2025, further rate cuts should help push economic growth up toward potential rates, supported by moderate real wage growth. The ECB currently seems to favor a gradual rate-cutting cycle, which, though positive for the economic picture, may delay the growth improvement. Upside surprises elsewhere in the world, such as in China, would likely boost eurozone growth as a surplus economy.

United Kingdom: We expect decent growth, but challenges remain

After years of slow growth, the UK economy has shown surprising resilience in recent quarters, and we're cautiously optimistic. The UK has faced some of the same setbacks as the eurozone — the energy price shock unleashed by the Russia-Ukraine war still weighs on spending — along with the idiosyncratic challenge of Brexit. Other factors have been weak investment and productivity growth since the Global Financial Crisis, worsened by Brexit-related trade/investment barriers with the European Union (EU) and an increase in economic inactivity since COVID (in contrast to the US). A lack of investment in the fabric of the economy (infrastructure, health care, and education) may have damaged performance, but the UK is not alone in this.

However, the UK could still surprise to the upside. The recently elected Labour government's Autumn Budget has the potential to boost growth,

as forecast by the Bank of England (although it expects a bump in inflation as well). Post-Brexit trading relations with the EU may also improve, which could facilitate the speed of trade and regulatory constraints on both goods and services.

We expect the UK to continue to deliver decent growth as inflation continues to trend lower (and real wages rise). However, challenges remain: The UK's fiscal overhang remains a hurdle, and its relatively more stubborn inflation outlook suggests the Bank of England will need to keep rates relatively high. Nevertheless, rate cuts should help the UK consume and help lift housing market activity.

Canada: Rate cuts should help economic re-acceleration

The Canadian economy has also faced headwinds and has not fared as well as the US economy. However, now that the Bank of Canada has begun easing, it appears the Canadian economy is likely to follow in the footsteps of other major developed economies and re-accelerate next year. We expect the economy to be helped by improving real wages, with a further boost if an accelerating global economy leads to higher commodity prices.

Japan: We expect wage growth to boost consumption, helping the economy

With inflation and wage growth seeing a revival in Japan, the country appears to have broken out of its long-running low-inflation regime. In contrast with many central banks, the Bank of Japan moved into a tightening stance in 2024 as inflation accelerated. However, its recent policy tightening has meant significant currency volatility, complicating Japanese export-focused business. Yet Japanese equity valuations have remained attractive relative to some markets such as the US.

We suspect Japan will reaccelerate in 2025 as wage growth helps push up consumption. As the Bank of Japan continues its very modest tightening cycle and other central banks ease, we suspect the yen may strengthen.

China: Policy support may lead to a positive surprise for growth

For much of 2024, China has contended with a slowdown in consumption and challenging sentiment in its property sector. We expect the property sector will likely continue to somewhat constrain strength in China's consumption and investment activities in 2025.

The high growth of exports strongly supported overall economic growth in 2024, but continued trade frictions could cause a slight deceleration in that growth. Capacity build-up in the manufacturing sector, which supported growth over recent years, is likely to also slow marginally.

However, policymakers have incrementally injected policy support into the Chinese economy, including measures to support the housing market, consumption, and monetary stimulus. More recent announcements beginning in late September (including initiatives that would support the equity market) are constructive and have helped boost market confidence. We believe policy stimulus measures could mitigate downward pressures, with economic growth likely to decelerate modestly in 2025. Stimulative policy measures may lead to growth surprising higher.

Other emerging markets: India remains a stand-out

US rate cuts, global monetary easing, China's stimulus, and moderate US dollar softening should all be broadly supportive of emerging market growth and performance. Commodity prices should trend somewhat

higher — especially if China stimulus gains traction. Fed rate cuts should pave the way for emerging market rate cuts, especially where rates are still very high and inflation is coming down (potentially parts of Latin America, Central Europe, Asia, and South Africa).

That said, we believe domestic dynamics are likely to have a larger impact on emerging market economies.

- **India** still stands out among emerging economies. Growth in investment and consumption is running strong with inflation under control. The major challenge continues to be the difficulty of raising manufacturing investment, employment, and exports — all constrained by the political difficulty of loosening up the labor market and the land market.
- **Latin America** will probably continue to offer both opportunities and risks. Mexico should gain from a US soft landing and reacceleration in due course. However, the advent of Claudia Sheinbaum as president may keep markets a bit tense, given her populist and potentially leftist tilt. Brazil has high real rates with inflation seemingly well under control. Yet concerns about fiscal policy and a lack of economic reforms may well keep risk premiums high.
- **Central Europe** has continued to bring down rates with successful disinflation, and further ECB easing should point to further rate cuts. However, Central Europe is arguably more exposed to US political and foreign policy choices than at any time since the Soviet collapse. The potential for a major reduction in US support for Ukraine would probably need to be offset by increased European NATO spending, which could add to fiscal pressure.

Investment implications

Markets appear to have priced in a relatively optimistic macro scenario already. Given the positive macro backdrop, we favor an overweight to risky assets but are cognizant of high valuations for some assets.

Equities

We favor cyclicals and smaller caps given lower valuations and greater sensitivity to the economic cycle. We also prefer developed ex-US stocks — especially UK and domestic-focused Japanese companies — and emerging markets equities for those same reasons.

Bonds

With bond yields sitting at relatively high levels, we believe bonds also offer attractive opportunities despite tight spreads, especially for longer holdings periods. Strong fundamentals underpin many fixed income assets, helping to explain extremely tight credit spreads in both investment grade and high yield credit.

- To take advantage of the resilient and improving growth backdrop, we favor some credit risk such as higher quality high yield to take advantage of this environment.
- We also like the diversification properties of bank loans, which tend to have similar volatility to investment grade credit but today offer greater return potential (in our opinion) due to the high current yield. With near-zero duration, loans have also been relatively immune to recent

near-zero duration, loans have also been relatively immune to recent interest rate volatility compared to other fixed income asset classes.

- We also anticipate strong performance from emerging markets local currency bonds.

Alternatives

We're also finding more opportunities in real estate, where we believe there's meaningful upside potential as the environment improves and rates ease. In terms of commodities, we favor industrial metals given their sensitivity to the economic cycle. In terms of currencies, we anticipate the US dollar will begin to weaken in 2025 against some currencies as the Fed continues to cut rates, and we would favor currencies such as the Japanese yen and the British pound.

Alternate scenarios

There's the potential that our base case is not realized, so we need to contemplate alternate scenarios.

Downside scenario

There's the risk of a policy mistake that causes global growth to undershoot. For example, we've seen weak patches in recent data, which could presage a sustained growth deceleration in key economies, including the US. However, if activity does falter, we would anticipate central banks to enact more rate cuts to counteract a growth slowdown, resulting in below-trend performance in the first half of the year, followed by a pick-up towards trend in the latter half of the year.

In this environment, we would favor a more defensive positioning, including US stocks and longer duration Treasuries. Within commodities, a favored pick would be gold, given it has often had a lower correlation to equities and has typically benefited from lower yields. In terms of currencies, we would prefer "safe haven" currencies such as the US dollar and the Japanese yen.

Upside scenario

There's the potential for global growth to be stronger than we expected. Falling inflation and rate cuts could help drive a "Goldilocks" environment across most economies: greater regional participation versus our base case, a period of growth above potential across most major economies, and inflation near target rates. China could also surprise to the upside, helping to lift emerging markets as a whole.

In this scenario, we would favor a more "risk on" positioning. Within equities, that leads to a preference for emerging markets equities, including Chinese equities. Within fixed income, that leads to a preference for high yield, emerging market debt, bank loans, and private credit. Within commodities, that leads to a preference for industrial commodities including energy, which are more sensitive to the economic cycle. Within currencies, that leads to a preference for "commodity currencies" such as the Canadian dollar and the Australian dollar.

Swing factors

There are also some additional factors that can impact our expectations, which we also need to consider.

Swing factor #1: The new US administration may cause disruptions to the global economy

With US President-Elect Donald Trump set to enter office early in 2025, policy uncertainty on tariffs and immigration has increased and there's the potential for higher market volatility. As we saw in the first Trump administration, stocks reacted negatively to the tariff wars in 2018 and 2019. And now bond markets have reacted negatively to the potential for higher inflation and larger fiscal deficits. Proposed policies for the second Trump administration, including an extension of tax cuts passed during the first administration, have the potential to place upward pressure on yields on the longer end. They also have the potential to amplify growth — and inflation — which could in turn impact the trajectory of Fed policy.

Swing factor #2: China stimulus could reinvigorate growth

Beginning in September, a raft of stimulus measures have helped reinvigorate Chinese financial markets and stoked expectations for a pick-up in growth, which could have positive spillovers to the global economy and equities. Recent cuts to mortgage rates should spur more homebuying. As policymakers deliver fiscal stimulus measures, we suspect investor sentiment will become more positive. We note that, historically, economic performance and stock market performance in China have generally not been strongly correlated. Policy tends to matter more here than elsewhere. We remain watchful for further shifts in investor sentiment sparked by recent policy momentum.

Swing factor #3: Inflation could return

Markets and policymakers in many regions have turned their attention to growth and its downside risks. While not our base case, we believe a return of inflation could spark a sea change in the current outlook and recalibrate expectations around policy easing and the resulting boost to the economy. Recent areas of concern in the US include upticks in wage growth and the ISM services prices paid sub-index. This highlights the risk that inflation could return as a market factor. Supply chain factors, such as shipping rates, could import inflation into economies. An oil supply shock would derail our base case, which would hit inflation and growth. And, as mentioned above, Trump administration policies on trade and immigration as well as pro-growth policies could also create inflationary forces.

Swing factor #4: Fiscal pressures may shift government spending trends

Recent above-potential growth in key economies was driven in part by large-scale fiscal spending. Now, despite a more normal macro environment (compared to the pandemic-era economy), the fiscal taps remain largely open. However, investors are increasingly concerned with the state of government balance sheets. Government bond yields at the longer end of the curve may suggest concern not only about inflation but rising debt levels, especially given the rise in US term premia in recent months. If governments curtail spending to rein in deeply expansionary fiscal policy, we may see growth headwinds build that limit the degree of reacceleration we expect in 2025.

Explore more

Learn more about our 2025 Annual Investment Outlook.

Important information

All investing involves risk, including the risk of loss.

Past performance does not guarantee future results.

Investments cannot be made directly in an index.

This does not constitute a recommendation of any investment strategy or product for a particular investor. Investors should consult a financial professional before making any investment decisions.

Diversification does not guarantee a profit or eliminate the risk of loss.

In general, stock values fluctuate, sometimes widely, in response to activities specific to the company as well as general market, economic and political conditions.

The risks of investing in securities of foreign issuers, including emerging market issuers, can include fluctuations in foreign currencies, political and economic instability, and foreign taxation issues.

Investments in companies located or operating in Greater China are subject to the following risks: nationalization, expropriation, or confiscation of property, difficulty in obtaining and/or enforcing judgments, alteration or discontinuation of economic reforms, military conflicts, and China's dependency on the economies of other Asian countries, many of which are developing countries.

Stocks of small- and mid-sized companies tend to be more vulnerable to adverse developments, may be more volatile, and may be illiquid or restricted as to resale.

Businesses in the energy sector may be adversely affected by foreign, federal, or state regulations governing energy production, distribution, and sale as well as supply-and-demand for energy resources. Short-term volatility in energy prices may cause share price fluctuations.

Alternative products typically hold more non-traditional investments and employ more complex trading strategies, including hedging and leveraging through derivatives, short selling and opportunistic strategies that change with market conditions. Investors considering alternatives should be aware of their unique characteristics and additional risks from the strategies they use. Like all investments, performance will fluctuate. You can lose money.

Commodities may subject an investor to greater volatility than traditional securities such as stocks and bonds and can fluctuate significantly based on weather, political, tax, and other regulatory and market developments.

Fixed income investments are subject to credit risk of the issuer and the effects of changing interest rates. Interest rate risk refers to the risk that bond prices generally fall as interest rates rise and vice versa. An issuer may be unable to meet interest and/or principal payments, thereby causing its instruments to decrease in value and lowering the issuer's credit rating.

High yield bonds, or junk bonds, involve a greater risk of default or price changes due to changes in the issuer's credit quality. The values of junk bonds fluctuate more than those of high quality bonds and can decline significantly over short time periods.

Fluctuations in the price of gold and precious metals may affect the profitability of companies in the gold and precious metals sector. Changes in the political or economic conditions of countries where companies in the gold and precious metals sector are located may have a direct effect on the price of gold and precious metals.

Investments in real estate-related instruments may be affected by economic, legal, or environmental factors that affect property values, rents or occupancies of real estate. Real estate companies, including REITs or similar structures, tend to be small and mid-cap companies and their shares may be more volatile and less liquid.

The health care industry is subject to risks relating to government regulation, obsolescence caused by scientific advances, and technological innovations.

Correlation is the degree to which two investments have historically moved in relation to each other.

Credit risk is the risk of default on a debt that may arise from a borrower or issuer of bonds failing to make required payments.

Credit spread is the difference in yield between bonds of similar maturity but with different credit quality.

Disinflation, a slowing in the rate of price inflation, describes instances when the inflation rate has reduced marginally over the short term.

Duration is a measure of the sensitivity of the price (the value of principal) of a fixed income investment to a change in interest rates. Duration is expressed as a number of years.

Idiosyncratic developments refer to unique events that do not affect an entire market or portfolio.

Inflation is the rate at which the general price level for goods and services is increasing.

Interest rate volatility measures the extent to which interest rates change over time.

Monetary easing refers to the lowering of interest rates and deposit ratios by central banks.

A policy rate is the rate used by central banks to implement or signal their monetary policy stance.

The Prices Paid sub-index of the ISM Services PMI tracks changes in the prices paid by services industries for various raw materials and goods.

Purchasing Managers' Indexes (PMI) are based on monthly surveys of companies worldwide and gauge business conditions within the manufacturing and services sectors.

A risk asset is generally described as any financial security or instrument that carries risk and is likely to fluctuate in price.

Risk-on refers to price behavior driven by changes in investor risk tolerance; investors tend toward higher risk investments when they perceive risk as low.

A risk premium is the amount of return an asset generates above cash to compensate for the higher risk.

Spread represents the difference between two values or asset returns.

Tightening monetary policy includes actions by a central bank to curb inflation.

Brexit refers to the exit of the UK from the European Union.

Safe havens are investments that are expected to hold or increase their value in volatile markets.

The yield curve plots interest rates, at a set point in time, of bonds having equal credit quality but differing maturity dates to project future interest rate changes and economic activity.

The opinions referenced above are those of the author as of **Nov. 15, 2024**. These comments should not be construed as recommendations, but as an illustration of broader themes. Forward-looking statements are not guarantees of future results. They involve risks, uncertainties and assumptions; there can be no assurance that actual results will not differ materially from expectations.