January 2025

Swedbank Economic Outlook

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Recording date of price data: 2025-01-24.

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Divergence in growth, in rates and in the fight against climate change

Divergence is here to stay. While the US economy is booming, economic headwinds in the euro area, not least in France and Germany, seem to be stubborn. In China, despite various stimulus measures, consumer confidence remains subdued, and the economic outlook appears weak. A major contributing factor is that US tariffs are expected to target China to a larger extent than other markets.

Economic growth in the US is being supported by loose financial conditions as Federal Reserve tightening has been offset by strong developments in the stock market and tight credit spreads. These loose conditions could change rapidly, however. Higher long-term yields or a stock market correction could pave the way for the Fed to make more rate cuts than currently expected, leading to weaker economic development.

Central bank easing will continue. Inflation is continuing down towards monetary policy targets, and lower policy rates will be delivered in the coming year. The pace and speed will differ among central banks, but the outlook seems favourable.

The fight against climate change is another area where divergence is becoming more apparent. Global efforts to address climate change were dealt a serious blow when US President Donald Trump again pulled the country out of the Paris Agreement. Also, many US banks, financial institutions and asset managers are leaving the Glasgow Financial Alliance for Net Zero, a United Nations-affiliated group promoting emission reductions.

Europe, on the other hand, stands firm in fighting climate change – at least for now. Recently, the European Bank Authority announced stricter ESG guidelines, while the Fed is withdrawing from the Network of Central Banks and Supervisors for Greening the Financial System, a global coalition of central banks that was launched in 2017 and is engaged in the study of climate risk. It is worth noting that 2024 was the planet’s hottest year on record. We need to do more, not less.

Mattias Persson
Group Chief Economist, Swedbank

0.2%

GDP growth in 2025 in Germany

0

No rate cuts from the Fed until September

4.8%

US government bond yield, June 2025

1.50%

ECB deposit rate in January 2026

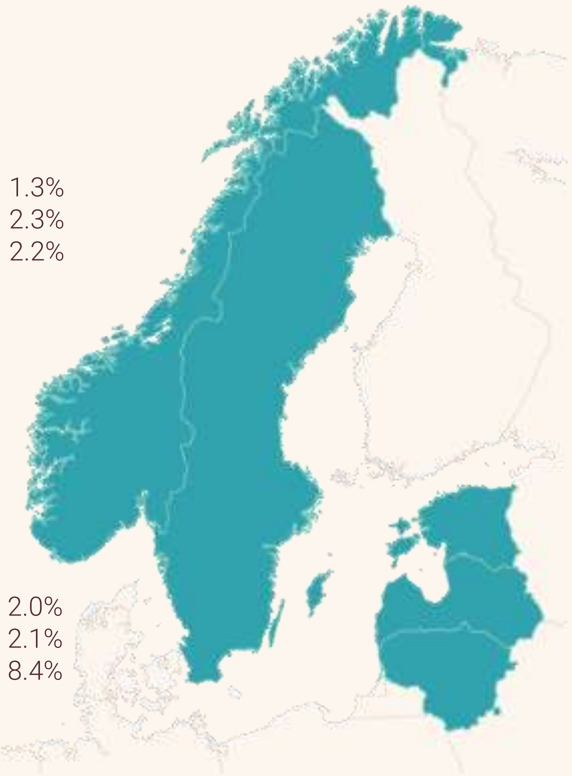
REE

Rare earth elements have gained critical importance for geopolitics, p. 35

1.03

EUR/USD, June 2025

Outlook for 2025



Norway

GDP:	1.3%
Core inflation:	2.3%
Unemployment (NAV):	2.2%

Sweden

GDP:	2.0%
Inflation (CPIF):	2.1%
Unemployment:	8.4%

Estonia

GDP:	1.5%
Inflation:	4.0%
Unemployment:	7.2%

Latvia

GDP:	2.2%
Inflation:	2.6%
Unemployment:	6.5%

Lithuania

GDP:	3.0%
Inflation:	3.0%
Unemployment:	7.5%

Global outlook

US dominance

Although GDP growth in the US will moderate somewhat ahead, it will nevertheless be markedly higher than in the euro area in both 2025 and 2026. China is struggling with both short- and long-term challenges, and its growth will be lower in the years ahead.

Return to normal inflation

In the US and most European countries, inflation is trending down despite recent stickiness. We expect inflation to fully normalise in the euro area this year, but to stay above 2% through year-end in the US. Deflationary pressures from China will help bring inflation down.

Greater protectionism

We assume that the US will impose tariffs, starting selectively and then expanding gradually. The tariffs are expected to weigh on global trade and GDP growth as from later this year, but the macro-effects are assumed to be limited during the forecast horizon.

Financial markets

Rate cuts at different paces

The US economy has remained strong, leaving the Fed in no hurry to lower the policy rate. We forecast two rate cuts this year, starting in September. The euro area economy, on the other hand, remains weak, and the ECB is expected to cut its policy rate more aggressively, so that the deposit rate reaches 1.50% in February 2026.

Higher bond yields in near term

Global bond yields have risen markedly since September 2024, driven mainly by US developments. We expect this trend to continue in the near term so that bond yields rise slightly further still. Later this year, as the US economy slows down and the Fed cuts the policy rate, we expect bond yields to edge somewhat lower.

A strong US dollar

The US dollar will gain somewhat more ground vis-à-vis the euro, supported by growth and interest-rate differentials. Uncertainty regarding Trump's policies should also support the USD. The NOK and SEK are expected to remain weak until the summer and then gradually regain some lost ground versus the euro.

Sweden

A long-awaited recovery

The Riksbank cuts the policy rate to 2% in the spring, and Sweden's economic recovery will begin this summer. GDP is expected to grow by 2% this year and 3% next year, contributing to a labour market recovery beginning in the second half of 2025.

Four reasons for optimism

Risks are on the downside, but there are four main reasons to be optimistic about Swedish growth: rate-sensitive households, growing public investments, stimulative fiscal policy, and high business investments.

Housing market rebound

Lower interest rates and eased mortgage rules will boost housing prices, while residential investment will only rise moderately, as slower population growth will reduce demand for new housing.

Baltics

Continued divergence, but more signs of recovery

Divergences remained evident across the Baltic countries – Lithuania's growth accelerated, while the Estonian and Latvian economies shrank slightly last year. Manufacturing production is already growing in all three countries, but an export recovery is unlikely to be swift.

Household consumption will drive growth

Falling interest rates, high employment rates and increasing real wages will support household purchasing power and consumption. The situation remains the most challenging in Estonia, where elevated inflation and increasing personal income tax mean that real net wages will not increase this year.

Wage growth is easing, but not everywhere

Wage growth has started easing in Latvia and Estonia, but remains very rapid in Lithuania – mainly due to hefty increases in minimum wage and public-sector wages. Although this has not yet dented Lithuania's exports, rapidly increasing unit labour costs will continue to pose medium-term challenges.

Sailing around Cape Trump

The US economy will continue on a comparatively strong growth path in 2025 and 2026, while GDP growth in both the euro area and China will be limited by structural challenges. Inflation in the western economies is not too far from the target and interest rates are on the way down, albeit the pace of decline will vary. Donald Trump's return as US president brings greater policy uncertainty and volatility. Rising protectionism and waning efforts in the fight against climate change will ultimately hurt the world economy, but the impact in 2025 and 2026 will be limited.

From a short-lived calm to stormy seas

Between election day in the United States and the beginning of Trump's second term as president, global economic data indicated that previous tendencies continued. The US economy grew strongly during this period, while most parts of Europe remained stuck in the mud. Meanwhile, incoming signals from the Chinese economy continued to be weak, despite GDP having hit the growth target of 5% in 2024.

Disruptive policies and little clarity ahead

Trump announced major policy changes as he began his second term. The most notable of these deal with immigration curbs, energy production and backtracking on the climate agenda. More disruptive policies are yet to come. There is no shortage of ideas and potential policy proposals in the Trump administration. What is lacking is clarity. Therefore, a baseline scenario with meticulously crafted assumptions will certainly turn out to be wrong. Instead, we assume a general direction of travel. (See our trade policy assumptions in on page 3.) We expect actual US policies in the next four years to be less radical than indicated by Trump's election promises. This will largely be thanks to the "voice of reason" on the part of the financial markets. However, navigating the waters around President Trump – like sailing around Cape Horn – will prove a great challenge to the world economy.

Swedbank’s GDP forecast

Annual % change, calendar-adjusted	2023	2024F		2025F		2026F	
US	2.9	2.8	(2.8)	2.4	(2.3)	1.8	(2.0)
China	5.2	5.0	(4.8)	4.3	(4.3)	4.1	(4.1)
Euro area	0.5	0.8	(0.8)	1.0	(1.3)	1.1	(1.2)
Germany	-0.3	-0.2	(-0.1)	0.2	(0.7)	0.9	(1.0)
France	1.1	1.1	(1.2)	0.5	(1.0)	0.7	(1.1)
Italy	1.0	0.5	(0.7)	0.7	(0.9)	0.8	(0.9)
Spain	2.7	3.1	(3.1)	2.3	(2.2)	1.8	(1.5)
Estonia	-3.0	-0.8	(-0.8)	1.5	(1.5)	2.5	(2.5)
Latvia	1.7	-0.2	(-0.3)	2.2	(2.4)	2.8	(2.8)
Lithuania	0.3	2.4	(2.4)	3.0	(3.0)	2.5	(2.5)
Sweden	0.0	0.6	(0.6)	2.0	(2.3)	3.0	(2.8)
Norway	1.0	0.9	(0.7)	1.3	(1.4)	1.4	(1.4)
United Kingdom	0.4	0.8	(0.9)	1.4	(1.5)	1.3	(1.5)

Previous forecast in parentheses.

Source: Swedbank Research

The net outcome of Trump 2.0 in the US will be larger tariffs, somewhat lower taxes, less immigration, higher government debt, and a risk of higher inflation. The US economy is like a container ship traveling at high speed – growth in the coming years is expected to be driven largely by the previous momentum. Our forecast for 2025 and 2026 suggests that US GDP growth will slow down but remain robust, supported by an ongoing fiscal boost.

US trade policies will reverberate around the world. China will likely enact targeted retaliatory tariffs on the US and announce an additional stimulus to its economy. It might allow the depreciation of the yuan and potentially flood Europe with goods that were previously imported by the US. China’s GDP growth will slow down to slightly above the 4% mark in the coming years, given the challenges the country faces both externally and internally.

US trade partners will retaliate in a targeted manner

Targeted protectionist retaliatory moves are also likely in Europe. Countries will be pushed towards larger debt burdens, not least due to an even greater need for increased defence spending. Our euro area GDP growth forecast indicates some cyclical recovery, but has been adjusted lower, suggesting only a slight acceleration in 2025 and 2026 as compared to 2024. The picture in Europe is far from uniform. Core economies (Germany and France) will remain weak and barely grow this year. Relative outperformance will continue in southern countries such as Spain, where Recovery and Resilience Facility funds will provide a boost. The Nordic and Baltic economies will outperform peers in terms of GDP growth, as these economies benefit more from a lower interest-rate environment than their larger European counterparts.

In Europe, core economies will underperform the north and the south

US trade policies – assumptions and consequences

We assume larger tariffs will be imposed, starting with selected sectors, products and countries, and then expanded stepwise. On his first day in office, President Trump did not announce any tariffs, but clearly signalled that they were to come. For example, he intends to hit Mexico and Canada with 25% levies by 1 February. Trump also announced tariffs on Colombia just to pull the threat after reaching a deal on deported migrants, confirming once again that tariffs will be used as a tool for negotiations. The new trade policies are expected to weigh somewhat on global trade and growth as from the second half of this year and in 2026. Their macro-effects outside China are assumed to be limited, although the consequences may harm specific firms and sectors more markedly. Moreover, the uncertainty regarding tariffs, as well as industrial policy in general, may dampen growth as firms become more cautious to invest. Risks are on the downside. Should the US tariffs and the expected retaliations in the form of counter-tariffs escalate into an outright trade war, severe global economic repercussions are likely.

Global central banks – same direction, different pace

Prices of oil and natural gas are up as compared to November last year. The price of oil has increased due to new sanctions aimed at the Russian energy sector, while the price of natural gas in Europe is up on the back of cold weather, lower gas reserves and the termination of Russian gas flows via Ukraine at the start of 2025. Key indicators still pointing to lower inflation around the world are China's falling export prices and the fact that prices for non-energy commodities are generally contained.

Despite somewhat higher energy prices, we forecast that inflation in the euro area will continue down. European Central Bank (ECB) policy rates will therefore be on a clear downward path. Persistent economic weakness will force the ECB to cut the deposit rate to 1.5% in February 2026.

1.5%

ECB deposit rate in February 2026

A somewhat different picture is forming in the US. Even though the latest CPI print showed easing underlying price pressures, inflation in the US seems to be sticky. Furthermore, there are risks of higher inflation stemming from Trump's policies. Overall, the Fed is expected to stay put for most of the year and deliver only two cuts – in September and December – followed by another two in 2026.

Bond yield drama – how far can the bond market be pushed?

Bond yields in the UK and US have risen markedly since September 2024 as term premium seems to be on the rise. Starting in December, the bond sell-off was widespread, with the US and the UK as well as Germany, France and Sweden all experiencing similar moves.

The surge in US 10-year treasury yields was to some extent due to rising inflation expectations, but most of the increase was in real yields. The root cause is not straightforward to establish. Markets could now be expecting higher potential growth for longer, which could lift yields. Very likely, however, the key concern is on the fiscal sustainability side – namely, the steep pick-up in the US debt trajectory expected under Trump and the marked increase in bond issuance going forward.

A potential risk that the ECB may need to step in again

Central banks are reducing their balance sheets, and the ECB has stopped purchasing government bonds altogether, which takes a big buyer off the market. In Europe, where debt and deficit concerns abound (think France) this could prove to be an even greater challenge than elsewhere. Even if governments successfully cut budget deficits, their bond issuance might not go down enough to offset the impact of the ECB leaving the market. Another aspect of Europe's bond yield drama is the rising spreads between France and Germany. Should the yields continue up markedly, the ECB might need to step in once again and save the day by potentially activating its Transmission Protection Instrument (see euro area chapter, page 14).

Recently, incoming data on inflation in the US and the UK has calmed the bond markets somewhat – but for how long? Trump 2.0 and higher government debt across the world could imply increased volatility, an uncertainty premium and perhaps more "drama" ahead. We expect bond yields to edge somewhat higher during the first half of the year, driven by the US. European yields will follow, although to a lesser extent due to economic underperformance and expected rate cuts from central banks.

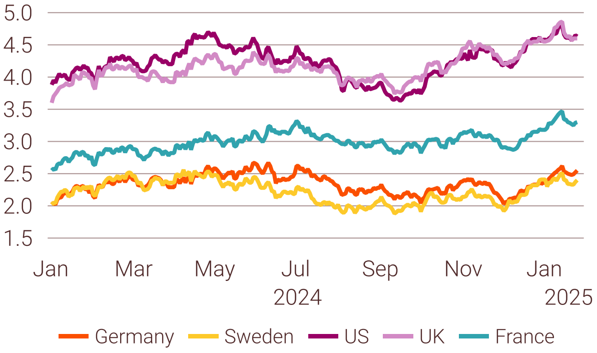
USD outperformance in the first half of 2025

The US dollar started this year as a clear outperformer, fuelled by the strength of the US economy, rate differentials as well as higher global uncertainty. It is expected to strengthen further in the short term, for these same reasons. The greenback will likely weaken somewhat starting in the second half of 2025 as the Fed starts cutting rates.

The Norwegian krone and the Swedish krona are expected to gain some lost ground. A likely prerequisite for stronger Scandies is that the dollar weakens as the US growth advantage fades and the Fed cuts rates. Sweden's GDP growth is expected to exceed that of both the US and the euro area as from the second half of 2025, which should support the SEK.

Bond yields: Up we go?

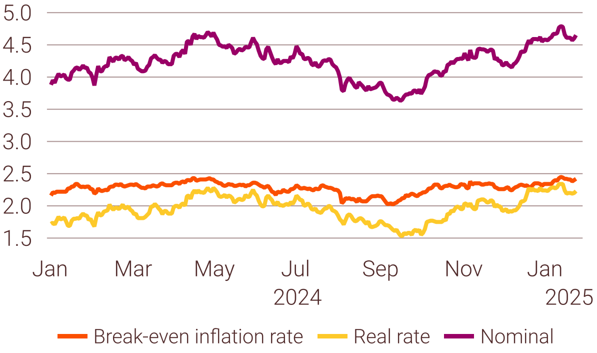
%, 10-year government yields



Sources: Swedbank Research & Macrobond

Driving force of US bond-yield rise: real rates

%, 10y Treasury yield



Sources: Swedbank Research & Macrobond

USA – outperforming peers

The United States' economy has outperformed other advanced economies following the pandemic. Although GDP growth will slow down somewhat, the economy is still expected to grow robustly in both 2025 and 2026. The Fed is expected to wait until September before cutting interest rates again.

Despite elevated inflation, real disposable incomes grew at a solid pace last year on the back of high nominal wage growth and a low unemployment rate. This will continue to support robust household consumption growth in 2025, albeit fading as inflation remains sticky, the pace of jobs growth slows further, and monetary policy restrictiveness will only slowly be dialled back. Additionally, newly elected President Donald Trump is expected to raise tariffs. This will lead to some additional upward pressure on prices and therefore dampen consumption in 2026, especially for low-income households, although the development will partly be counteracted by tax cuts for households. We expect GDP growth to be 2.4% in 2025 and 1.8% in 2026.

Trump is determined to raise tariffs; his thinking is that this will reduce the trade deficit, make companies relocate to the US, and bring in revenue to pay for tax cuts. He has proposed raising tariffs between 10% to 20% on all goods entering the US, with tariffs of 60% on goods imports from China specifically. While such high tariff rates may ultimately be realised, we believe Trump will not start off on such a high note. The range of possible tariff outcomes is large: from their size to which goods and countries will be affected and whether they will be phased in and increased later on. The president has a lot of freedom on tariff policy without approval from Congress, and Trump now comes prepared, given that he successfully raised tariffs during his previous term. All in all, tariffs are most likely to be increased above current levels, perhaps increased gradually, with the changes effective from the middle of this year at the earliest.

Tariffs will be raised, but their size, timing and the affected countries and goods are uncertain

Trump's election promises also included extensive tax cuts, but these could be hard to deliver fully, given that the government budget deficit is already large. Furthermore, estimates show that revenues raised by tariffs will not be enough to fully offset tax cuts, and it remains to be seen how much government spending Elon Musk, heading the newly created "Department of Government Efficiency", will be able to cut. Combined with the fact that Republicans have only a slim majority in Congress, we do not think Trump will have enough congressional support to pass sweeping tax cuts. Our forecast is that the Tax Cuts and Jobs Act will be extended and that it will also be amended to include some additional tax cuts for households, coming into effect in the beginning of 2026.

Businesses' fixed investments are also forecasted to grow at a slower, albeit still solid pace, weighed down by high borrowing costs. Uncertainty about Trump's trade policies may also deter or delay some firms' capex plans, as well as lead to a build-up in inventory ahead of tariff implementations. However, growth in investments in non-residential structures was government support from the CHIPS and Science Act as well as the Inflation Reduction Act. As factory constructions are completed, they are now also providing momentum for other types of business investments, such as those in equipment. Additionally, investments in equipment and intellectual property will also benefit from continued advancements in and adoption of AI.

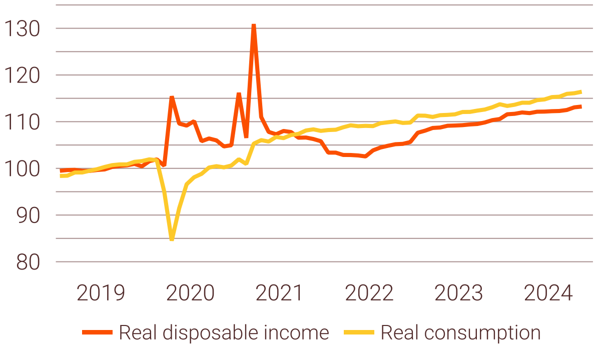
Disinflation turned from a slow crawl to a standstill at the end of last year. We assume that inflation will resume declining as consumers become more price-sensitive and as wage growth slows further. We do not expect Trump to conduct large-scale deportations of unauthorised immigrants, which would create labour shortages and upward pressures on wages, although tougher controls on immigration seem likely. Still, progress will continue to be slow, and inflation is forecasted to remain above 2% through year-end. Meanwhile, the labour market is holding up better than expected even as it continues to weaken. The Fed cut the federal funds rate by 100 basis points last autumn to an interval of 4.25–4.50%, initially due to weaker signs from the labour market and subsequently to bring rates to a more neutral stance. But with few signs that the economy and labour market are buckling, and given the uncertainty about trade and fiscal policy, the Fed is expected to move cautiously as it stamps out the last stretch of stubborn inflation. We forecast that the Fed will remain on hold for the better part of the year, delivering rate cuts in September and December, followed by two more in 2026.

2

Rate cuts by the Fed in 2025

Robust income and consumption growth

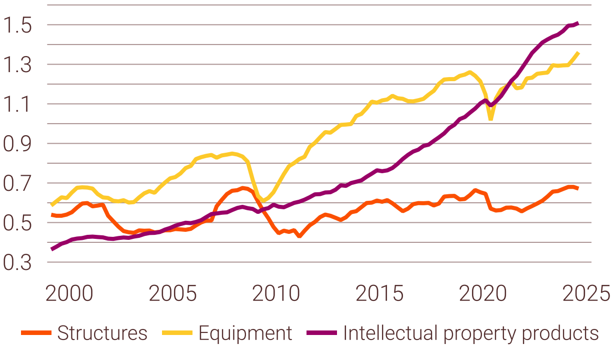
Index (2019=100)



Sources: Swedbank Research & Macrobond

Booming investments

USD trn 2017 chnd, saar, real non-residential investments



Sources: Swedbank Research & Macrobond

China – deflationary pressures

China's GDP grew by 5.0% in 2024, in line with the growth target set by Beijing. Developments were uneven, however. Net exports grew strongly, while consumption remained muted. Looking ahead, it will be difficult for China to rely on exports given the expected Trump tariffs, and policymakers will therefore have to turn towards supporting the domestic economy even more.

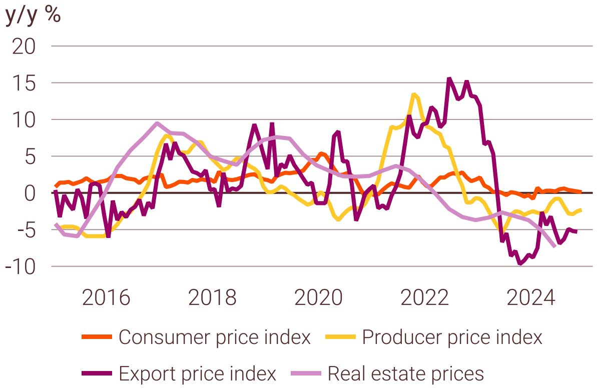
Chinese consumption is still being held back by morose consumer confidence. The labour market was disrupted by strict pandemic restrictions, and falling housing prices have led to massive negative wealth effects, resulting in uncertainty about household employment and income. Last year, China expanded its trade-in and equipment upgrade policy, which allows consumers to receive subsidies to purchase newer and more advanced consumer goods such as cars and home appliances, if they trade in their old ones. Recently, authorities also announced that they will expand the list of products that will be included in this trade-in scheme and will offer subsidies for additional digital goods this year. While these measures have boosted consumption somewhat, they likely represent only a short-term fix that will come at the expense of future consumption. Otherwise, consumption is expected to remain weak; no meaningful recovery for the real estate market is seen in the near term, which will hinder a recovery in confidence. Consumption is also being held back by important structural issues for which there are no quick fixes; an example is the country's weak social safety net.

In a sign of economic weakness, inflationary pressures have been muted. Consumer prices have barely grown in recent years due to weak household demand, while both producer and export prices have been falling due to overcapacity in manufacturing. Falling asset prices are further exacerbating this issue, especially housing prices given that around 70% of household wealth is stored in property and that real estate prices are down around 15% from their 2021 peak. One of the biggest risks facing the economy this year is that of a deflationary spiral. When cautious consumers cut back on spending, businesses reduce production and employment, which results in lower prices and wages – a phenomenon that becomes self-reinforcing. This also has global spillover effects given China's role in the world economy; notably, lower prices on Chinese exports lead to disinflationary pressures in other countries.

The economy faces the risk of a deflationary spiral

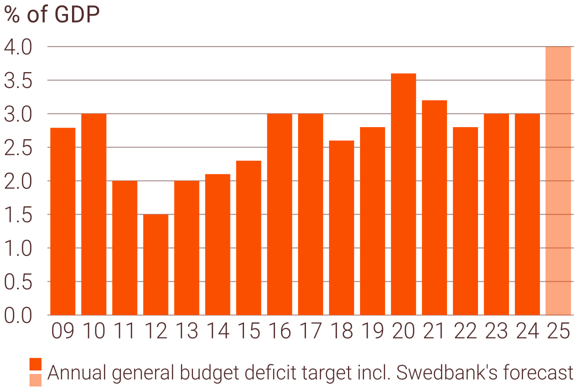
The government has delivered a barrage of monetary and fiscal policy measures in recent months, and has announced that it is ready to ramp up policy to support growth. We expect further interest rate cuts this year; however, the effectiveness of monetary easing will remain constrained, as households still prefer saving over consumption. Government spending will be ramped up to revive domestic demand; the fiscal deficit target is

Deflationary pressures



Sources: Swedbank Research & Macrobond

Record-high budget deficit in 2025



Sources: Swedbank Research & Macrobond

rumoured to be 4% in 2025, higher than the 3% China targeted last year and the country's highest deficit target on record.

China's official annual GDP growth target will be unveiled in March, and is rumoured to once again be 5%. If true, this would lead to growth exceeding our forecast of 4.3%. However, stimulus is unlikely to fully offset the cyclical and structural challenges facing the economy, and the global trade environment following Trump's accession as US president is expected to worsen, especially for China. We therefore continue to expect a gradual slowdown in growth to slightly above the 4% mark in the coming years.

Euro area – growth will remain below trend; the ECB will provide more stimulus

We have lowered our GDP growth forecast for the euro area for 2025 and 2026, mainly due to the ongoing manufacturing weakness and the likely headwinds from US trade policy. The good news is that purchasing power is growing and household consumption is recovering. All the region's large economies, especially France, are trying to consolidate their public finances, which will create a negative fiscal impulse, but investments in southern European countries will continue to rise thanks to Recovery and Resilience Facility funds.

GDP in the euro area grew by an estimated 0.8% in 2024, but the year was marked by large differences across countries and sectors. The German economy shrank by 0.2% for the second year in a row, while Spain's GDP growth accelerated to 3.1%. Manufacturing continued to decline in France, Italy and, especially, Germany last year. The weaker euro will provide some tailwinds for manufacturers, but at the same time it will make imported energy and other commodities more expensive. Euro area manufacturers continue to suffer from sluggish productivity growth, intense competition (especially from China) and expensive energy. On top of this, the US is very likely to introduce new or increase existing import tariffs on at least some goods, further dampening recovery prospects. Thus, even with some improvement in global demand for goods, European exports and manufacturing output are unlikely to recover swiftly during our forecast horizon.

1.0%

GDP growth this year

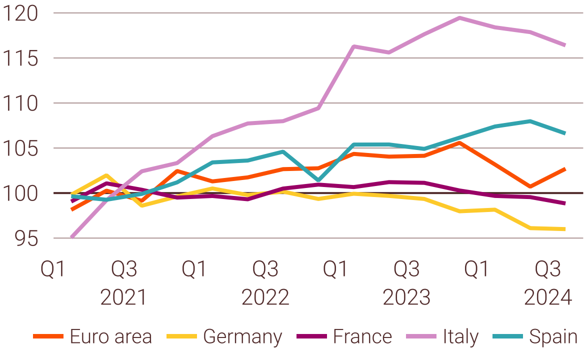
The prospects for domestic demand, however, are brightening. The employment rate increased to record highs (70.8%), and real wage growth accelerated to 2% in the euro area last year. This is already helping the recovery of household consumption – growth in retail trade volumes accelerated in the second half of 2024. Wages in advertised positions suggest that nominal wage growth will ease slightly to 3% this year, but household purchasing power will continue growing rapidly, as inflation is likely to decline further. Natural gas and crude oil prices have spiked in recent months and may keep headline inflation slightly elevated for now, but we forecast that it will fall to 2% already in the second quarter of this year. The risks to inflation are balanced – services inflation may prove to be stickier than we are currently forecasting, but higher-than-expected US import tariffs could lead to even more deflationary export-dumping from China to Europe. We are maintaining our forecast for the ECB policy rate;

we expect the ECB to continue cutting policy rates at each of its meetings until the summer. We expect the deposit interest rate to be cut to 1.75% in September and, after a brief pause, to 1.5% in February 2026. Lower interest rates and improving lending standards have also helped to turn the tide in credit growth. Credit impulse turned positive last year and will likely continue improving further this year.

Two risks loom large this year and the next. First, Trump's administration may impose larger-than-expected import tariffs on European manufactured goods, which could further dampen export growth prospects. The EU could retaliate, further dampening cross-Atlantic trade. Furthermore, even larger import taxes on imports from China (and elsewhere in Asia) could mean a rise in cheap imports to the EU and more intense local competition. Second, at the beginning of this year, the ECB stopped buying bonds, and the amount of its bond holdings will drop by some EUR 150 billion per quarter. This quantitative tightening is testing markets' confidence, as is the French political crisis – particularly France's inability to find consensus on how to reduce its budget deficit, which was close to 6% of GDP in 2024. The spread between French and German 10-year government bond yields is close to 1pp and is at the highest level since 2012. Although a rerun of the euro area sovereign debt crisis is unlikely, it cannot be ruled out that the ECB will need to step in, perhaps by activating its new Transmission Protection Instrument (TPI).[1] The outcome of Germany's elections could cause the country to abandon its debt brake and boost short-term investments in defence and energy infrastructure. The political uncertainty resulting from the lack of clear political leadership and resolve in the euro area's two largest economies will weigh down on confidence and growth. We forecast that, in 2025, the German and French economies will grow by a meagre 0.2% and 0.5%, respectively.

Investments

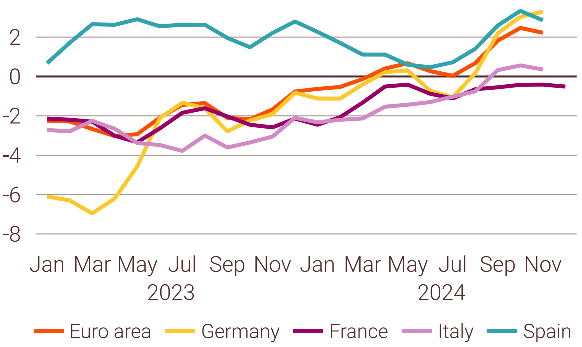
Index (2021=100), constant prices



Sources: Swedbank Research & Macrobond

Retail trade: first signs of recovery

y/y %, 3mma



Sources: Swedbank Research & Macrobond

[1] The TPI is part of the ECB's toolkit, and can be activated to counter unwarranted, disorderly market dynamics that pose a serious threat to the transmission of monetary policy across the euro area. The instrument allows the ECB to buy bonds from specific countries to support the transmission of monetary policy.

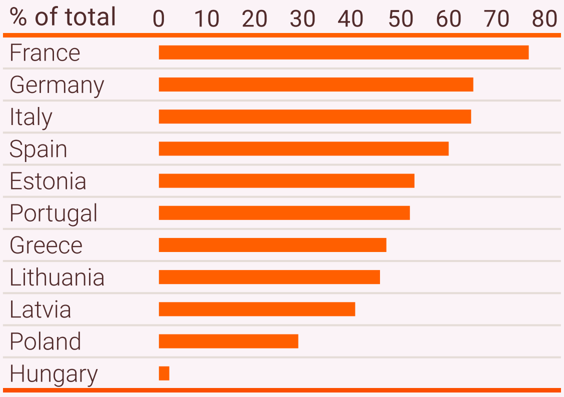
The role of European Recovery and Resilience Facility funds and fiscal consolidation

All of the euro area's large economies are trying to reduce their budget deficits. The EU Commission estimates that this will create a **negative fiscal impulse** worth 0.1-0.4 pp of euro area GDP (and close to 1pp in France) this year. The continued disbursement of Recovery and Resilience Facility (RRF) funds will, however, provide an ongoing boost to investments in both 2025 and 2026. Only around 50-60% of RRF grants had been disbursed by the end of 2024 in Italy, Spain, Portugal and Greece. These four countries have been allocated 78% of RRF funds (even though they make up less than 30% of the euro area economy).

Admittedly, the effects of these RRF funds differ from country to country; they will not necessarily have a lasting effect and boost long-term growth. Italy, for example, is renewing its railway networks, but is spending even more on housing renovation subsidies, which will do little to improve competitiveness and productivity. Spain, on the other hand, is investing a lot in renewable energy – a strategy which has already pushed down electricity prices and attracted private-sector investment in data centres. The strings attached to the RRF funds – requirements to implement **structural reforms**, improve fiscal balances and market functioning – may be an even more important long-term success factor. For example, to unlock these funds, Italy is undertaking major reforms of its public administration and judicial systems. If done right, these reforms could boost countries' efficiency and long-term competitiveness.

The ongoing flows from RRF funds are one reason why southern economies in the region will continue to **outperform** their northern peers, who barely benefit from the funds. Furthermore, falling interest rates and a positive credit impulse will have more and faster positive impact on peripheral euro area economies. Finally, these southern economies are more reliant on services exports (especially tourism, but more recently also on various higher value-added business services) and are thus somewhat less vulnerable than manufacturers to a likely increase in US import tariffs.

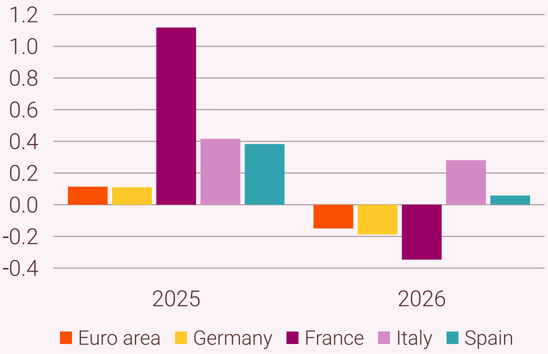
RRF grant disbursement*



* as of 31 December 2024
Sources: European Commission, Swedbank Research & Macrobond

Tighter fiscal policy in 2025

Change in structural balance, % of GDP (EC forecast)



Sources: European Commission, Swedbank Research & Macrobond

German industry malaise

Germany, once the economic powerhouse of Europe, is facing many economic challenges. Its industrial sector is at the heart of the decline, with production in manufacturing having stagnated during the past 15 years. Yet, the manufacturing sector still accounts for more than 19% of Germany's GDP and employs 14% of the country's labour force. Key challenges are higher energy costs, as well as increased competition and lower demand – particularly from China.

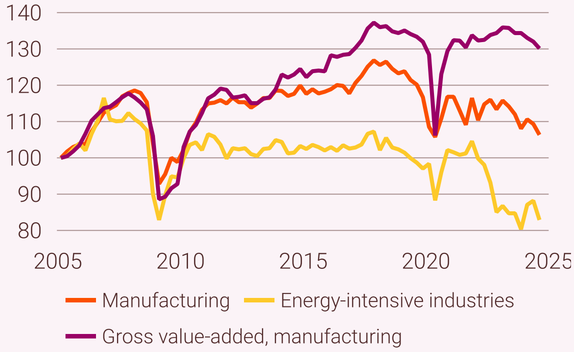
The shutdown of Russian gas supplies in 2022 marked the start of Germany's **energy crisis**, causing a 17% drop in production in energy-intensive industries such as chemicals, metals and paper. Rising energy costs have led the government to promote renewables and reduce gas consumption, but its target of a 100% renewable electricity supply by 2050 seems out of reach. According to The Economist, Germany would need to build 15-20,000 onshore windmills in the next decade to meet the target. If Germany continues to construct windmills at its current pace, only around 7,500 will be built during this period. While firms are exploring alternative energy sources, energy uncertainty is hampering growth.

Exports are also under strain because of weak global demand and **intensifying competition**. The automotive industry, contributing 5% to GDP, faces intense competition from electric vehicle manufacturers such as Tesla and BYD. The stagnation of car exports to China and rising imports of components have hit the industry severely. On top of this, US trade **policies**, including potential tariffs, could disproportionately harm German industries.

The International Monetary Fund's list of German structural **challenges** is long, and includes an aging population, underinvestment, bureaucracy, slow approval processes and a strict fiscal framework. Political challenges, with new elections coming up on 23 February, are further complicating the economic recovery. Despite these challenges, opportunities exist in sectors such as climate technologies, industrial automation and healthcare. Germany needs to prioritise investments in energy and digitalisation, while addressing structural barriers such as excessive bureaucracy to boost competitiveness and productivity.

Germany: industrial production

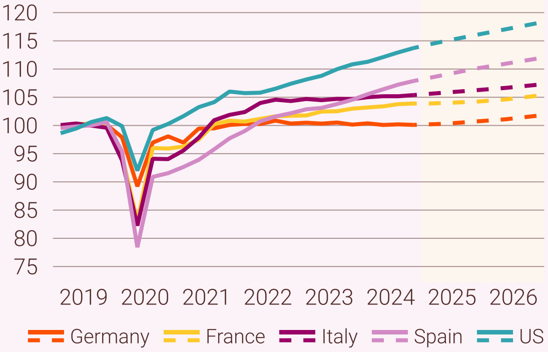
Index (2005Q1=100), sa, constant prices



Sources: Swedbank Research & Macrobond

Germany lags behind

GDP incl. Swedbank's forecasts, index (2019=100)



Sources: Swedbank Research & Macrobond

United Kingdom – gradual rate cuts from the Bank of England

Higher inflation and elevated wage growth together with a cooling labour market and low growth prospects are complicating the Bank of England's decision-making process. We nevertheless expect a gradually lower policy rate during our forecast horizon.

UK economic activity decelerated substantially during the second half of 2024, implying a stagnation in the third quarter and the beginning of the fourth quarter. Although GDP growth was weak, household consumption, business investments and government consumption all boosted growth.

Going forward, we expect household consumption to continue to increase as purchasing power strengthens. Unemployment remains low by historical standards, although the labour market is cooling a bit. Also, increased government spending and investments are expected to contribute to the 1.3–1.4% GDP growth that we expect to see this year and next. There is a great deal of uncertainty, stemming from factors such as the tariffs that the US may potentially impose on UK exports. However, the fact that services account for most of the UK-US trade means that the impact of these potential tariffs would be manageable.

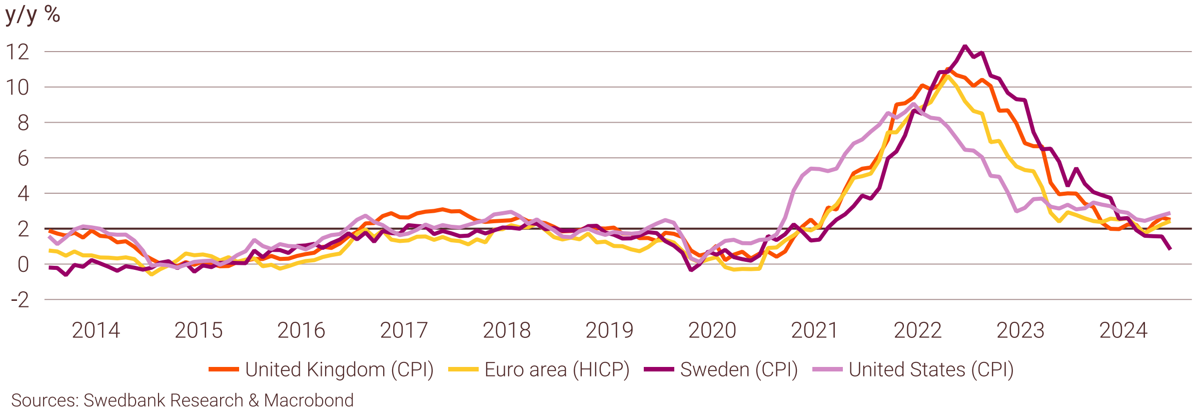
Inflation has recently increased to about 2.5% after having reached the Bank of England's inflation target of 2% during the summer. Services inflation, one of the central bank's key metrics, remains elevated and is expected to decline only slowly as wage growth remains high. We also see a risk that measures in the autumn budget, such as the increase in the national insurance contribution, will be passed on from the corporate sector to consumers; higher prices would make it harder for the UK to reach its inflation target again. The Bank of England is therefore expected to cut the policy rate only gradually at a quarterly pace, reaching 3.75% by the end of this year and then making one more cut in 2026, to 3.50%.

Bank of England stops cutting policy rate at

3.50%

Government bond yields have surged in recent months. Although the increase is mainly being driven by US developments, there are a few factors that make the situation less favourable in the UK than elsewhere.

Inflation above Bank of England's target

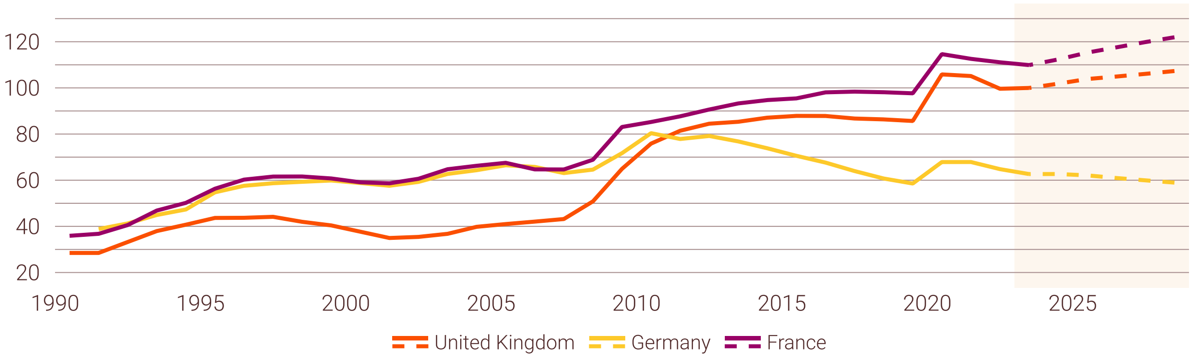


Sources: Swedbank Research & Macrobond

For example, the fiscal situation is poor in both the US and the UK, but growth prospects are gloomier in the UK. Also, the forthcoming change in debt metrics[2] to free up scope for additional borrowing to finance public investments may be contributing to investors' unease.

Debt on the rise in the UK

Maastricht debt, % of GDP



Sources: IMF Fiscal Monitor, Swedbank Research & Macrobond

[2] At the release of the autumn budget on 30 October 2024, Chancellor Reeves announced changes to the fiscal target, relating to the way debt is measured. The previous debt measure was "public-sector net debt excluding public-sector banks and excluding the Bank of England". Going forward, the UK will instead target "public-sector net financial liabilities excluding public-sector banks", which is a wider balance-sheet measure. The aim is to free up scope to borrow more money to finance public investments. The new debt measure will take effect once the House of Commons has approved the change; a vote is likely in early 2025.

Sweden

Dawning optimism

The Riksbank will cut the policy rate to 2% in the spring, and Sweden's economic recovery will begin this summer. GDP is expected to grow by 2% this year and 3% next year, supporting a labour market recovery in the second half of 2025. Housing prices will be boosted by lower rates and eased mortgage rules.

Four reasons to be optimistic about Swedish growth

The economy has bottomed out, but the recovery will not gain speed until the second half of the year. There are several reasons to be optimistic about the Swedish economy in the coming years. First, Sweden has an interest rate-sensitive economy, especially the household sector, which means that the past year's interest rate cuts should provide a boost to growth going forward. Second, public investment is expected to grow rapidly during our forecast period. In contrast to several other European countries, such as France, Italy and Spain, fiscal policy is also supporting the recovery, including tax cuts for households. In addition, business investment as a share of GDP has risen to its highest level in decades, indicating that corporates are in a good position to increase output once demand picks up.

However, the global situation remains uncertain, with geopolitical tensions, trade uncertainties, and political instability in Germany and France. We also see risks related to the domestic economy, particularly concerning labour market recovery. If employment declines more than expected, demand and growth will weaken beyond our current forecast. Meanwhile, it remains uncertain whether Swedish households will prioritise spending or saving, and the recovery could be either faster or slower than forecasted.

Sweden (%)	2024	2025	2026
Real GDP	0.6	2.0	3.0
CPIF inflation	1.9	2.1	2.0
Unemployment	8.4	8.4	8.0
Policy rate (EOP)	2.50	2.00	2.00

Growth will pick up in the second half of 2025

Given the slowdown in global trade, Swedish export growth has been resilient, although it slowed to 2% last year. Since 2019, the United States has become an increasingly important market, and in 2024 Sweden's surplus in trade in goods with the US was equivalent to 2% of GDP. Germany is still Sweden's most important trading partner (exports and imports of goods with Germany amounted to around 8.5% of GDP last year), but the robust growth of the US economy is benefiting Swedish foreign trade. Looking ahead, however, US tariffs could weigh on exports to the United States, and uncertainty about trade policy could also lead to a lower rate of investment in Sweden.

2% of GDP

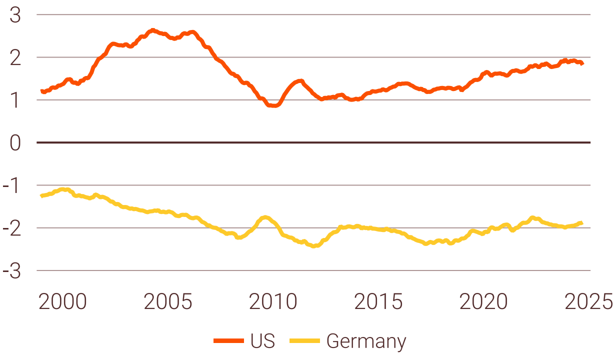
Trade surplus with the US in 2024

Business investments have fallen from high levels. However, the decline is expected to be relatively limited, and firms will gradually increase investments over the course of the year. Public investment, on the other hand, has risen sharply during the past two years and is expected to continue to grow faster than normal during our forecast period. This is true not only for the defence sector, but also for research and transport infrastructure. Housing investments are heading towards brighter times after a few difficult years. Housing starts picked up slowly last year, and residential investment is gradually increasing as lower interest rates contribute to higher demand. However, the increase is expected to be moderate, partly because slower population growth is reducing the need for new housing. We expect housing starts to reach 32,000 this year and 37,000 in 2026, slightly above our recent estimate of an annual need for 30,000 new homes in the coming decade.

Households are optimistic about their future economic situation but remain cautious. Consumption has slowly begun to increase, but growth has not gained momentum. One reason is that interest expenses have remained largely unchanged since the beginning of 2024, and it is only this year that the Riksbank's rate cuts will start to have more of an impact on household finances. Additionally, real wage growth and tax cuts will contribute to strengthening purchasing power this year, and we expect household consumption to grow significantly faster than trend in the second half of the year as the labour market also begins to strengthen.

Sweden's trade surplus with the US

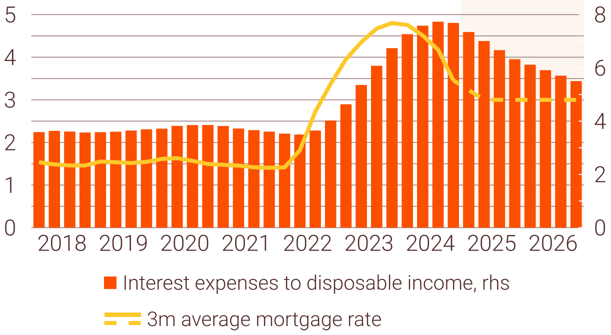
% of GDP, goods



Sources: Swedbank Research & Macrobond

Delayed impact of rate cuts

% (lhs), % of disposable income (rhs)



Note: Average mortgage rates, new & renegotiated agreements
Sources: Swedbank Research & Macrobond

All in all, we expect domestic demand to drive growth during our forecast period, with the recovery starting in the summer. GDP is projected to increase by 2% this year and accelerate to a 3% growth rate in 2026.

Initially sluggish labour-market recovery

The labour market has been weakening for more than two years, with the number of people employed falling by around 30,000 in 2024. Compared with a year earlier, employment fell particularly in sectors such as construction, IT services, trade and education. However, most indicators, such as hiring plans and the trend for temporary employment, suggest that most of the decline has already taken place and that the labour market situation will stabilise.

We expect the labour market to strengthen gradually in the second half of this year, as GDP growth will be above average. However, the recovery in the labour market will be slow, and unemployment is anticipated to remain high at 8.3% by the end of 2025. There is a risk of a worsening trend, especially in the short term. If employment continues to fall in 2025, household sentiment and consumer spending could be dampened again.

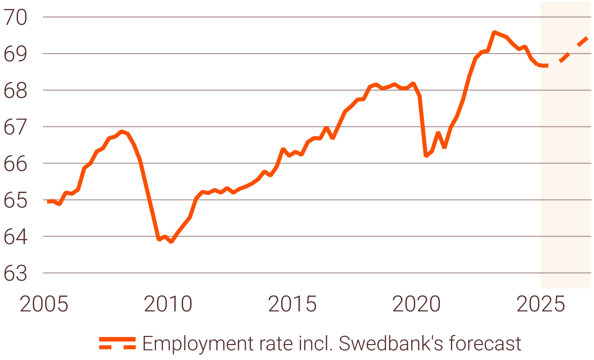
Wage growth was 4% last year, implying real wage growth of 1% (based on CPI). The current collective agreement expires in March 2025, and a new agreement is to be negotiated before then. We expect the parties to agree on a two-year deal and that total wage growth in the economy will be 3.6% in both 2025 and 2026. The relatively high wage growth combined with low inflation means that real wages will rise by 3% this year and 2% next year, which, together with the turnaround in the labour market, will help to strengthen household purchasing power in the coming years.

3%

Real wage growth in 2025 (based on CPI)

Slow recovery in the labour market this year

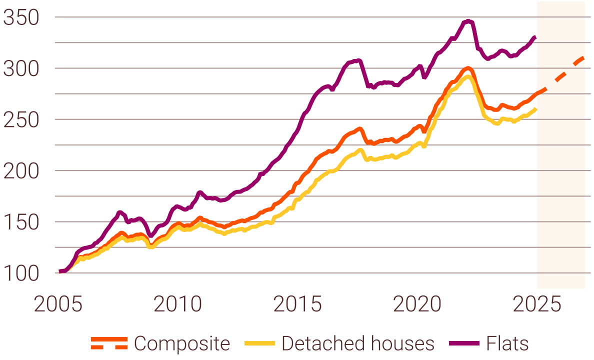
% of population 15-74 years



Sources: Swedbank Research & Macrobond

Housing prices will rise in 2025 and 2026

Index (2005=100), sa



Sources: Valueguard & Swedbank Research

Housing prices will be boosted by easing mortgage rules

The housing market has started to recover, with a significant increase in home sales and rising prices. In December 2024, housing prices were 5% higher compared to a year earlier. We expect further strengthening as purchasing power improves due to lower mortgage rates and rising incomes, while mortgage rules are eased. However, the high supply of homes for sale will dampen price increases for a while longer. Overall, we expect housing prices to rise by around 5% this year and 7% in 2026.

7%

Increase in housing prices in 2026

In part, price growth is seen to accelerate in 2026 because the government is expected to ease macroprudential tools by raising the mortgage ceiling and easing repayment requirements. It is unclear when these changes will be introduced and what form they will take, but we expect them to be phased in from autumn 2025. All else being equal, the easing will mean that homebuyers can afford to take out a larger loan and thus buy a more expensive home. We expect prices for smaller homes in major cities to be most affected, as buyers of these homes are more constrained by current mortgage rules.

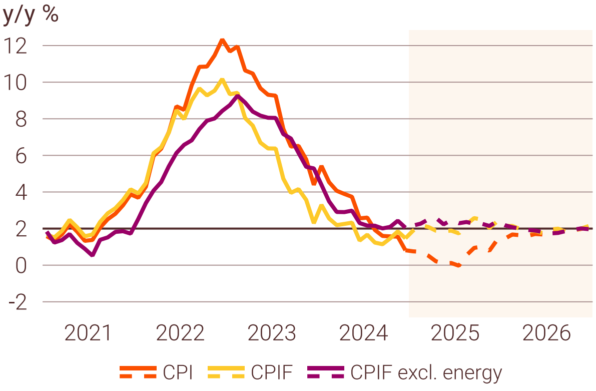
The Riksbank will hit the low point of its rate-cutting cycle this spring

Annual CPIF inflation was 1.5% in December, but is expected to rise and remain close to the 2% target during our forecast period. While services inflation will ease slightly during 2025, goods inflation will rise, albeit from low levels. This increase will be primarily driven by food prices, which are expected to rise by 3%. The risk picture is balanced during the forecast horizon, with upside risks stemming mainly from higher wage growth and faster commodity price increases, while downside risks stem from potentially higher productivity growth and price pressures from Chinese exports.

Balanced risks to the inflation outlook

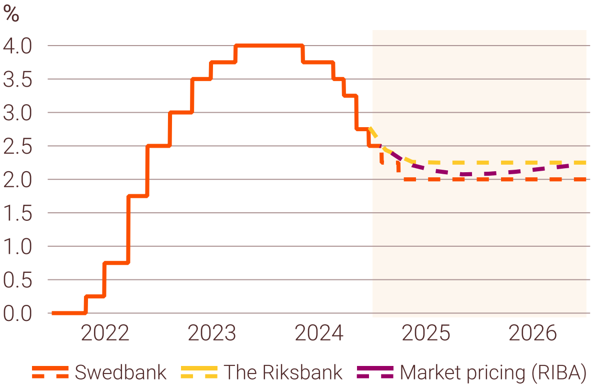
As inflation has stabilised around the inflation target, and with growth in the Swedish economy expected to remain weaker than normal for some time, we anticipate that the Riksbank will continue cutting the policy rate, reaching 2.00% in March. Thereafter, it will be evident that the recovery in the Swedish economy is underway, and we believe that the Riksbank will stop cutting, even though the still-weak labour market will justify further cuts. Fiscal policy will also support the recovery this year when, among other things, tax cuts for households take effect.

Inflation close to target for the next two years



Sources: Swedbank Research & Macrobond

Rate cuts down to 2% in the spring



Sources: Swedbank Research & Macrobond

The Riksbank has indicated that it will only cut the policy rate down to 2.25%, which is also the midpoint of its projected range for a long-term neutral policy rate. However, we anticipate that the recovery in the Swedish economy may progress more slowly than the Riksbank's December forecast. Persistently weak economic conditions, exacerbated by downside risks such as weaker export growth and cautious consumer behaviour, explain why the Riksbank will cut the policy rate a bit more in the spring than what the interest rate path suggests. Furthermore, given the dominance of these downside risks over a longer horizon, we cannot rule out the possibility that the Riksbank could lower the policy rate below 2% later this year or into 2026.

Norway

Rate cuts, at last

Norges Bank has announced that its first rate cut will come in March, and we expect an additional three cuts this year as inflation normalises and growth momentum stays weak. Even with less restrictive monetary policy, growth will be moderate during 2025 and 2026.

Lower inflation expected before the summer

Norwegian inflation slowed by almost 3 percentage points during the past year and, while remaining above the central bank target, it is now more in line with peers. Goods inflation remains somewhat higher than in comparable countries, while services inflation is equal to or lower than in the UK, US, and euro area. The past weakening of the NOK is expected to have limited impact on inflation. Food prices and housing costs will also have a limited impact going forward. On the other hand, cost pressure remains high, which suggests that inflation will remain above target for some time ahead. We expect core inflation to remain at current levels until Easter, but decline towards 2-2.5% ahead of the summer.

Turning to the real economy, growth remains meagre and varied across sectors based on their sensitivity to interest rates. As monetary policy will remain restrictive, we expect overall growth to remain below trend in the coming years, although growth drivers will change. Following two strong years, oil and gas investments are set to expand only moderately this year, while we also expect government expenditures to grow more slowly. Hence, the two main growth engines of the Norwegian economy are set to lose some steam. On the other hand, increased real disposable income growth for households should support consumption growth ahead. We expect consumption growth to remain below historical averages, however. Likewise, housing prices should be further supported by factors such as lower policy rates, decent income

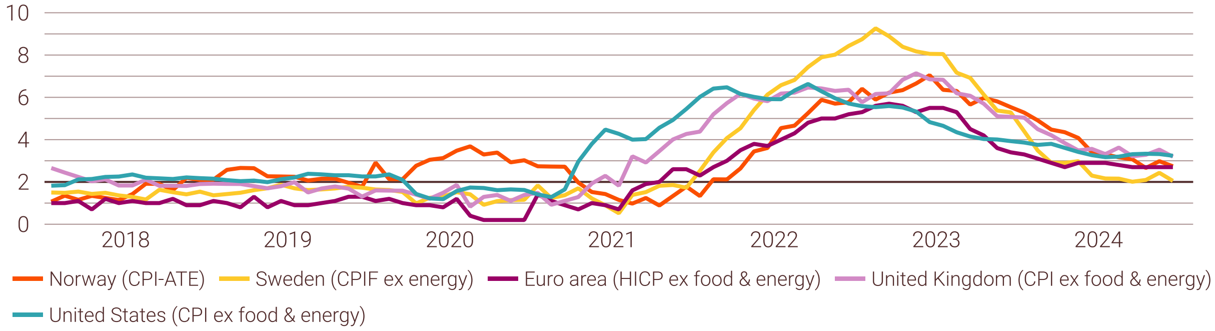
Norway (%)	2024	2025	2026
Real GDP	0.9	1.3	1.4
Core inflation	3.7	2.3	2.0
Unemployment	2.0	2.2	2.4
Policy rate	4.50	3.50	2.75

2.0%

CPI-ATE in July 2025

Peer comparison: Norway in the middle

y/y %, core inflation



Note: Definitions of core inflation vary across countries.
Sources: Swedbank Research & Macrobond

growth, the limited supply of new homes, and the easing of mortgage loan-to-value regulations. We expect housing investment to rise only slowly in the coming years, remaining well below pre-pandemic levels. Taken together, the growth rotation from interest rate-insensitive to sensitive sectors will start this year, but overall moderate growth is expected.

4

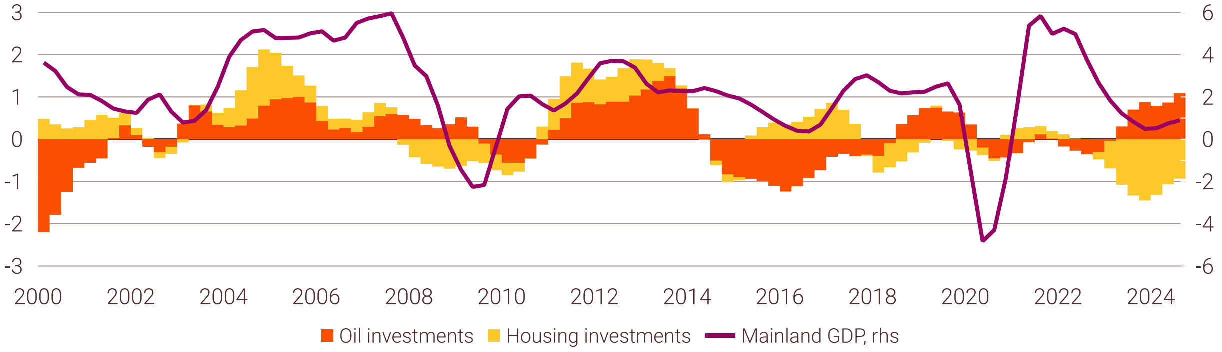
Number of rate cuts expected in 2025

The labour market has softened slowly during the past few years, but most of the slack is stemming from increased labour supply. Demand for labour is, however, also growing more slowly, which suggests a moderate increase in the unemployment rate ahead from a historically very low level; the current rate is 2.1%.

Norges Bank kept the policy rate unchanged at 4.5% in January, and indicated that it will most likely reduce the policy rate in March, kicking off a much-awaited cutting cycle. The latest policy-rate path suggests that the rate will be reduced to 3.75% by the end of the year, and that another three cuts will be delivered in the coming years. Norges Bank evidently has low tolerance for inflation being stuck above the 2% target. The central bank has seen real policy rates increase markedly during the past year as inflation and inflation expectations have fallen while it has kept policy rates unchanged. Looking ahead, however, as the interest rate-sensitive sectors must do more of the pulling in the economy, we deem the current rate path to be too high; we expect the policy rate to be reduced to 3.50% this year and further down to 2.75% next year.

Oil and housing investment contributions to GDP

pp (lhs); y/y% (rhs)



Sources: Swedbank Research & Macrobond

The tide is turning, but challenges remain

Large divergences remained apparent across the Baltic countries in 2024, although signs of a more synchronised recovery became evident towards the end of the year. Inflation is rising, mainly due to higher taxes, but lower interest rates and healthy labour markets should boost household consumption this year and next.

Manufacturing production continued to accelerate in Lithuania last year, and more recently output seems to have started to recover in Latvia and Estonia as well. Export orders have also increased somewhat, although they remain slightly below the long-term average. Employment rates remained close to record highs (and above the EU average) in all three Baltic countries. Wage growth trends, however, diverged somewhat. While it has remained elevated in Lithuania, wage growth has started easing in Latvia and Estonia. Household consumption continued to shrink in Estonia but started recovering in Latvia, and its growth accelerated in Lithuania. The situation remains the most challenging in Estonia, where average real net wages will not grow this year due to personal income tax increases and stubborn inflation. The prospects are brightening, however, and GDP growth is likely to be close to 2.5% in all three Baltic countries in 2026 (unless protectionist policies prove to be more aggressive and damaging than expected).

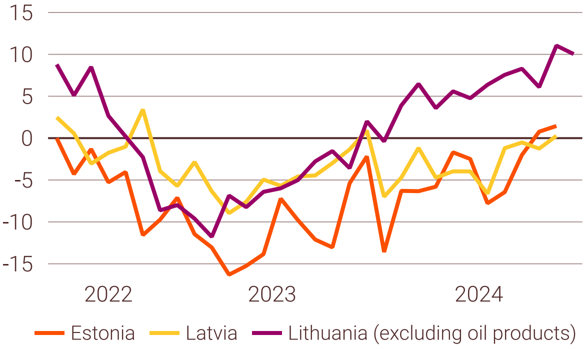
1.5-3%

GDP growth in 2025

In the longer term, the largest risk remains cost competitiveness. Wage growth has outpaced productivity increases in recent years, which has already caused trouble for some lower value-added sectors (e.g., textile manufacturers). It is not all gloom and doom, however. Export market shares are stable, and the Baltic countries have no persistent trade deficits. Furthermore, the structure of the economies is changing, with higher value-added manufacturing and services sectors making up an increasingly larger share. Going forward, higher investment growth and structural reforms should boost productivity, while lower wage growth will pull down unit labour costs. We forecast that, in 2025 and 2026, almost all GDP growth will come from productivity gains, not increases in employment.

Manufacturing output is recovering

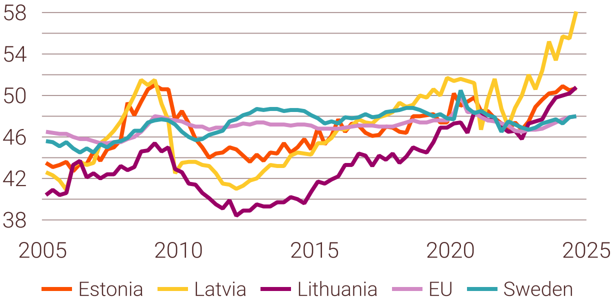
y/y %, constant prices, ca



Sources: Swedbank Research & Macrobond

Less scope for sustainable wage growth

Compensation of employees, % of GDP, swda



Note: Compensation of employees comprises wages and salaries, as well as employers' social contributions.
Sources: Swedbank Research & Macrobond

Estonia

Gradual recovery despite fiscal policy brakes

The Estonian economy contracted last year, but we forecast that it will expand in 2025 and 2026. This year, the growth will be supported primarily by larger exports and investments, while household consumption will contribute considerably less. The labour market will remain resilient, while tax hikes will keep inflation elevated.

Estonia (%)	2024	2025	2026
Real GDP	-0.8	1.5	2.5
Inflation	3.5	4.0	3.5
Unemployment	7.6	7.2	6.5
Wage growth	7.9	6.3	6.1

Current estimates indicate that Estonia's economic recession ended in the first quarter of 2024; only a modest recovery was seen in the second and third quarters. We forecast that the economic situation will continue to improve in 2025 and 2026.

On top of the moderate growth in services exports, trade in goods started to expand as of mid-2024. Although close to half of the growth has come from only two product groups – wood products and mobile equipment – exports would have increased without these goods as well. Better export opportunities have contributed to the recent increase in manufacturing production, which had been on a downward trend since the middle of 2022. Industrial sector confidence and export expectations are showing some improvement. Even though we have cut our forecast for the economic growth of Estonia's trade partners, overall foreign demand will improve, and we forecast moderate export growth in 2025 and 2026.

We forecast moderate export growth, as foreign demand is expected to improve

The protracted annual decline in retail sales subsided towards the end of last year, while sales of vehicles increased robustly before the new tax on vehicles came into force at the beginning of this year. Consumer confidence remains downbeat, however.

Swedbank card payments data suggests that household consumption remains weak despite real wage growth in both 2023 and 2024. A growth slowdown relating to the number of employed people and to average wages has caused the growth of the total wage bill to decelerate. Along with the decline in consumption and investments, household savings have increased. However, bank deposits are distributed unevenly. Swedbank private customers' average deposits amounted to around EUR 9,200 at the end of 2024, while the median was only EUR 1,100 (71% of average net wages in 2024).

Household consumption is expected to pick up only modestly in 2025. We forecast some decline in employment, while tax increases (e.g. VAT, excises, vehicle tax, personal income tax) will reduce net wages in real terms. At the same time, lower interest rates will have an increasingly larger positive impact on purchasing power for households with loans and leasing obligations. We expect that household confidence will show some improvement as well.

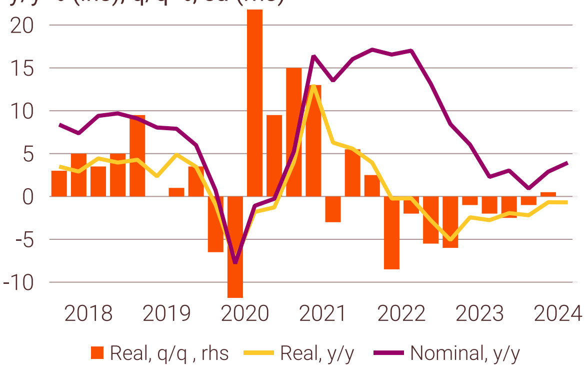
Tax hikes and elevated inflation will reduce real net wages in 2025

Inflation in Estonia has reached some of the highest levels recently recorded in the euro area, largely due to tax hikes in 2024. We have cut our inflation forecast for 2025, but tax hikes will keep it elevated. Households' inflation expectations rose again in the second half of last year. We forecast that the largest contribution to inflation in 2025 will come from the increasing food and transportation prices.

The labour market has been resilient to the long-term economic recession. We forecast that the gradual economic recovery will reduce the number of unemployed people in 2025. Registered unemployment increased seasonally at the beginning of this year, but it was lower than during the corresponding periods in 2023 and 2024. Although we forecast that the number of employed people will drop slightly this year, Estonia's employment rate will remain among the highest in Europe (more than 69%). High employment will help the business sector to respond faster to the expected increase in demand. At the same time, it could tighten Estonia's labour market and maintain pressure on wage growth.

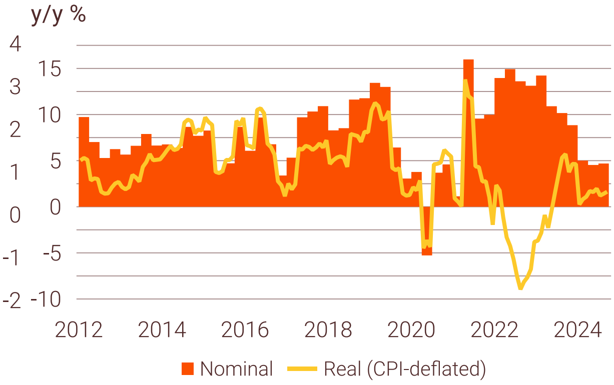
Employment rate will remain among the highest in Europe

Estonia's economic recession has ended



Sources: Swedbank Research & Macrobond

Growth in total wage bill has slowed



Sources: Swedbank Research & Macrobond

Latvia

Signs of recovery, but choppy waters ahead

Signs of stronger activity are already being observed in several areas of the Latvian economy. In 2025, consumption and exports will pick up, and government investment should see markedly stronger growth. GDP will rise by 2.2% in 2025 and 2.8% in 2026. Inflation has picked up as expected and will remain within the 2-3% range in the coming years.

Latvia (%)	2024	2025	2026
Real GDP	-0.2	2.2	2.8
Inflation	1.3	2.6	2.5
Unemployment	6.9	6.5	6.0
Wage growth	9.5	6.5	7.0

It is likely that the Latvian economy stagnated overall in 2024, even though the year seems to have ended on a rather positive note in a range of sectors. The available data for Q4 2024 indicates that retail growth picked up and that manufacturing continued to grow compared with the preceding quarter. Exports of services were up, likely fuelled by business services and the ICT sector. In the final two months of 2024, the number of passengers using Riga Airport increased robustly, finally exceeding the pre-pandemic levels seen in 2019. After a seven-quarter fall, port cargoes also climbed substantially. Economic sentiment in Q4 remained slightly below the long-term average but very close to it, marking the highest level since the start of 2022.

European Commission survey indicators point to a gradual improvement in demand and export orders in manufacturing in the coming months. However, economic growth expectations for 2025 have been lowered in key trading-partner economies, e.g. the euro area (notably Germany) and Sweden, limiting Latvia's export prospects. As a result, we have revised our GDP growth forecast slightly down this year. We now expect GDP growth to pick up to 2.2% in 2025 and 2.8% in 2026. This is still an acceleration in economic activity after more than two years of stagnation.

Growth will return after a prolonged period of stagnation

The Latvian labour market is resilient. The unemployment rate was on the way down in the second half of 2024. Employment expectations are up – businesses plan to increase employee headcount slightly in the coming months. Wage growth surprised on the upside in the third quarter of 2024. We still maintain that gross wage growth in 2025 will decelerate somewhat, due to the lower profitability of businesses during the last two years and because of the 2.6% cap on public-sector wage bill growth.

2.6%

Inflation in 2025 will pick up

Inflation increased at the end of 2024 as expected. With economic activity picking up, wage growth resilient, and energy prices on the rise, inflation will stand at around 2.6% this year. Net wage growth in 2025 is expected to reach 8.5% – around 2 percentage points above gross wage growth due to the introduction of a fixed non-taxable minimum. Therefore, workers' purchasing power will continue to rise. Furthermore, consumer optimism is trending up. All of this will support consumption growth going forward.

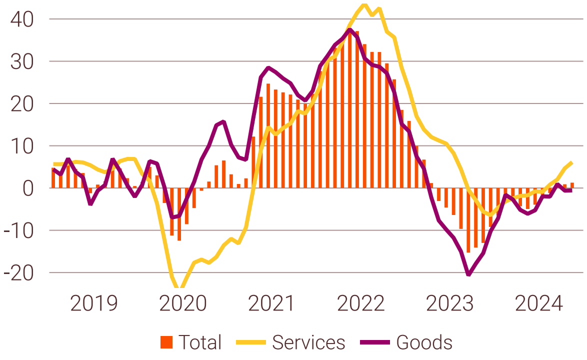
Notable increase in government investment expected

Investment was the weakest link in the Latvian economy in 2024. Cyclical factors as well as public-sector investment delays were to blame. Projects funded by the EU Recovery and Resilience Facility (RRF) need to be implemented by mid-2026. Contracts have been concluded for nearly 90% of total allocated funds, but as of the start of 2025, outgoing payments for projects only amounted to around 20% of the allocated funds. If Latvia is to absorb the RRF funds, the pace of investment needs to increase materially in 2025 and 2026.

Lending struggled in the high rates environment but saw a strong pick-up towards the end of 2024 as rates declined. Latvia's household loan portfolio grew at its fastest pace in 15 years. The pace of lending to corporates also picked up. Fundamental economic factors suggest that stronger credit growth should continue. However, the recently introduced tax on banks' net interest income could distort the generally improving outlook. The tax disincentivises new corporate lending unless overall lending portfolio growth is in double-digit figures. Latvia needs greater financial deepening, and poorly designed taxes risk delaying rather than helping the achievement of this objective.

Services exports up, goods still struggling

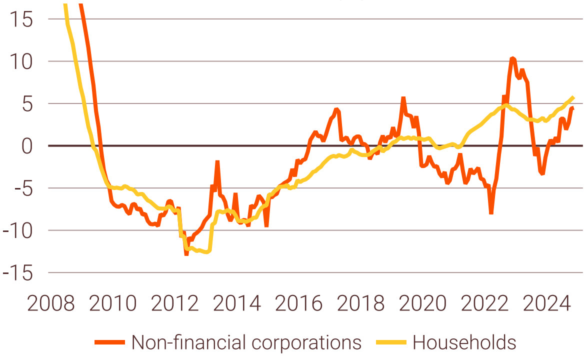
Annual growth of exports, % 3mma



Sources: Swedbank Research & Macrobond

Household lending growth – fastest in 15 years

Changes in bank loan portfolio, y/y %



Sources: Swedbank Research & Macrobond

Lithuania

Goldilocks economics and looming tax reform

Manufacturing and retail trade growth accelerated at the end of last year while wage growth remained close to 10%, and employment as well as consumer confidence increased to record highs. Ambitious plans to increase defence expenditures will likely be financed by a tax reform, but neither its success nor its benefits are guaranteed.

Lithuania (%)	2024	2025	2026
Real GDP	2.4	3.0	2.5
Inflation	0.7	3.0	2.7
Unemployment	7.2	7.5	7.5
Wage growth	10.2	9.4	7.7

Lithuanian manufacturing and retail trade growth accelerated at the end of 2024. Our estimates show that GDP grew more than 3% year-on-year in the final quarter of last year. Export orders have improved somewhat, but remain below the long-term average. As demand in export markets improves, we forecast that export growth will pick up further, but it will not be the main driver of GDP growth this year or next. Wage growth is no longer easing; Swedbank client data suggests that in the final quarter of 2024, annual growth was close to 10%, mainly due to faster wage growth in the public sector. Inflation increased to 2.1% at the end of last year and is likely to approach 3% before this summer (mainly because of higher excise taxes and as wages are still increasing rapidly).

Further increase in public spending on defence

At the start of this year, the Lithuanian State Defence Council (which includes e.g. the President, Prime Minister, Speaker of the Parliament and Minister of Defence) announced a bold and ambitious target – to increase defence spending to 5-6% of GDP, starting already in 2026 and at least until the end of this decade. This decision is not binding, and the ruling coalition members are not confident that it can or should be achieved. Nevertheless, it is likely that the government will try to increase defence spending to at least 4% of GDP next year (up from 3% in 2025). As this year's budget deficit is expected to be close to 3% of GDP, there is little room to fund additional expenditures solely with larger debt.

Government debt

43%

of GDP

Many sources of potential funding have been floated – such as usage of the country's foreign exchange reserves or social security fund reserves, and lowering the VAT gap. However, this ambitious aim is unlikely to be achieved without tax increases. A tax reform was on the cards even before this decision, as Lithuania has made commitments to find more sustainable tax revenues so that it can receive remaining grants from the EU's Recovery and Resilience Facility. Lithuania's previous government attempted to eliminate some personal income tax exemptions and loopholes, to increase the tax on residential real estate and to increase pollution taxes (more or less in line with European Commission recommendations), but did not find sufficient support in parliament to pass these laws. The new government seems to be willing to move in a similar direction. We think that most of these proposals are sound, and the government should keep Lithuania's attractiveness to foreign investors in mind and abstain from excessive corporate taxation. The process is unlikely to be smooth, however, and consensus within government will be hard to find.

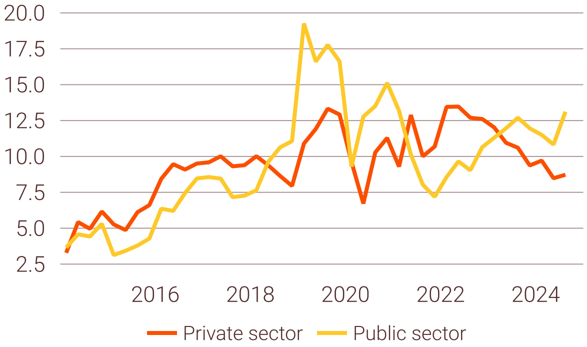
Another emerging challenge, which is more pronounced in Lithuania than in Estonia or Latvia, is a very rapid wage growth. So far, this development has proven beneficial with limited negative side effects – household purchasing power has improved significantly, while exports of most goods and services have continued growing and export market shares have increased. Wage growth in the private sector eased to 8% at the end of last year, while it accelerated to 13% in the public sector. The problem here is that the minimum wage in the private sector is indexed to the national average wage, creating a dangerous loop. In other words, rising minimum wage and public sector wages automatically requires further increases in the minimum wage in the following year, even if the private sector has problems with cost competitiveness. This is one of the reasons why we are forecasting that the unemployment rate will stay elevated. We think that this minimum-wage indexation rule should have some sort of circuit-breaker (for example, indexation pauses if unemployment increases by 2 percentage points) or at least be changed so that it covers only private-sector wage growth. For now, the economy remains in a Goldilocks scenario and growth is expected to increase to 3% this year, before easing slightly in 2026.

12.3%

Increase in minimum wage in 2025

Diverging net wage growth

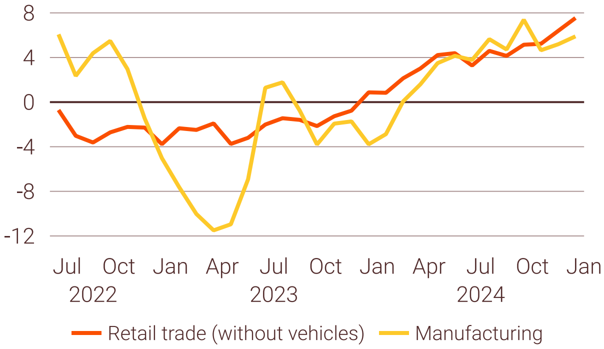
y/y %



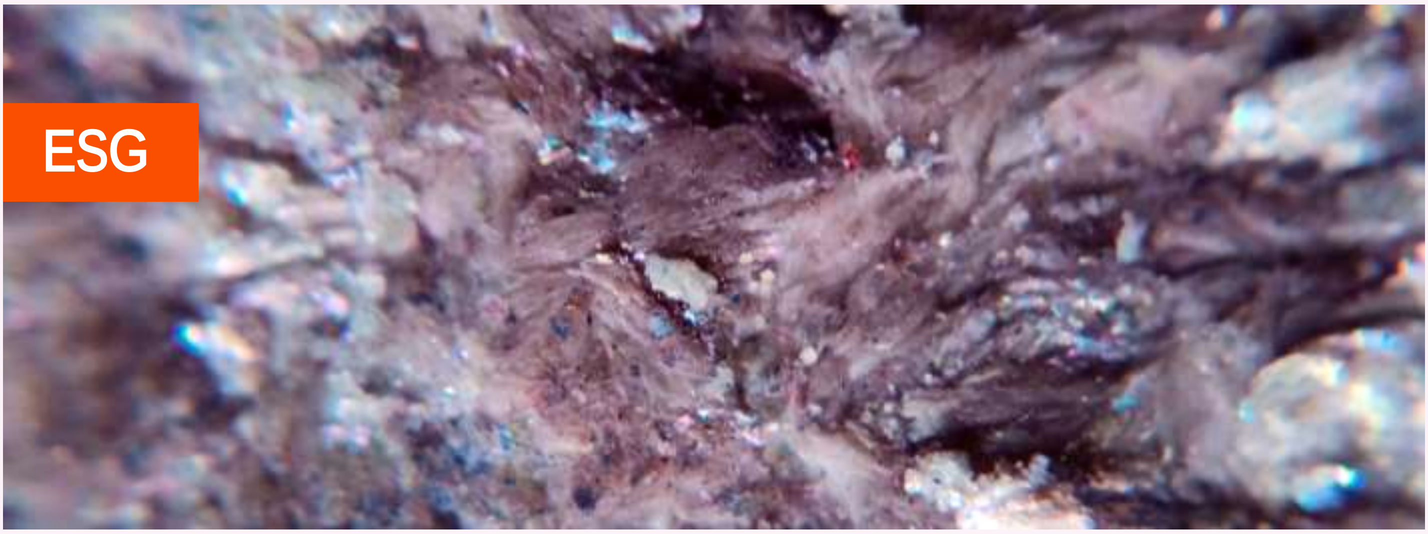
Sources: Swedbank Research & Macrobond

Surging manufacturing and retail trade

y/y %, 3mma, constant prices



Sources: Swedbank Research & Macrobond



ESG

Critical minerals, critical power

China is the dominant force in the mining and production of rare earth elements and other critical raw minerals, occupying a pivotal position in the global supply chain. As geopolitical tensions intensify, the EU and the US are seeking to secure their supply of these critical materials. The Nordic countries have a significant potential for advancing the future supply of metals and minerals and are key to diversifying EU supply.

Critical raw materials at the heart of geopolitical tensions

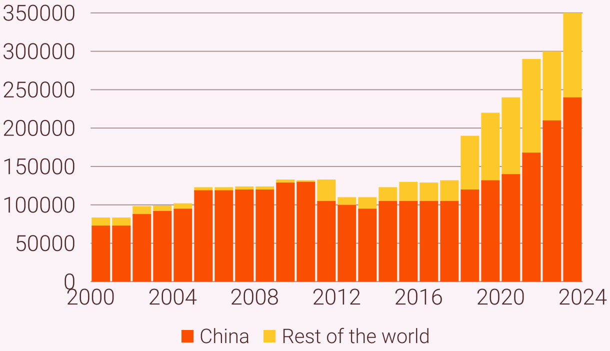
The green transition will change how countries produce, use and store energy to decarbonise their economies, and this change will be dependent on certain raw materials. Rare earth elements (REE) play a vital role in components such as magnets in electric motors and in the generators that are used in power plants and batteries. Together with 33 other raw materials, such as lithium and cobalt, REE are therefore included in what the EU classifies as "critical and strategic materials", based on their importance for the green transition of the economy but also for other areas, such as the defence industry. These materials are also regarded as critical given that they are associated with a high risk of supply disruption in any step of the value chain, from mining to processing and usage.

Nearly 40 years ago, Chinese leader Deng Xiaoping stated "The Middle East has oil, China has rare earths". China mines around 70% of the world's REE and refines nearly all of them, bolstered by government subsidies that drive prices down. Where it lacks domestic deposits, such as in nickel, China invests abroad—for example, in Indonesia. Nickel is important for battery production, and China's control over nickel prices has put pressure on other producers, such as Australia, leading to mine closures. Additionally, China dominates the world's lithium market, processing around 70% of the global supply. Hence, fears that China seeks to exert control over the industry have been circulating for some time. Nickel is currently just below the EU classification threshold for "high risk of supply disruption", but is nevertheless a "strategic" material in the Critical Raw Materials Act.

Both the EU and the US are currently dependent on imports, particularly from China, to obtain REE and other materials for green technologies. The EU produces no REE and lacks production of a substantial proportion of the other critical raw materials needed for these technologies. According to the ECB, the market supply of minerals is even more concentrated than the oil market was in 1960, when OPEC was formed. As global fragmentation and geopolitical risks have increased, these critical materials have become central to escalating trade tensions, with trade barriers for minerals and other tech components implemented in 2024 by both the US against China and China against the US. Further escalating geopolitical tensions pose, therefore, a threat to both the green transition and the prosperity of our digital societies.

Rare-earth metals, mining & quarrying

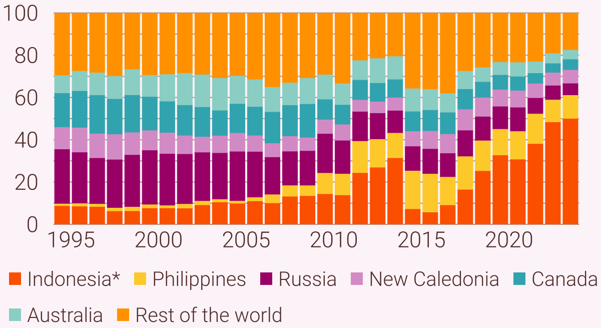
Tons



Sources: Swedbank Research & Macrobond

Nickel, mining & quarrying

% of total



*Chinese companies dominate local processing

Sources: Swedbank Research & Macrobond

Diversification could be boosted by Nordic mineral reserves

To mitigate these raw material supply-chain risks, the EU has decided to reduce its reliance on any third country by restricting imports to no more than 65% of any of the critical materials at any stage of the material lifecycle, by 2030. The EU also wants to increase its own extraction capacities to 10% of annual needs, from today's 3%. These targets are ambitious, but have so far not been followed up with a public plan or incentives specifying how they are to be met.

Europe has known reserves of critical raw materials, but the process of mining often meets resistance from environmental groups and local communities. Projects might also be unprofitable due to cheap Chinese supply, meaning that significant financial support could be needed from the EU. The problem is circular: if no action is taken, the risk of supply-chain disruptions will persist, potentially delaying the green transition. However, taking action could result in short-term and possibly long-term environmental costs at the affected locations.

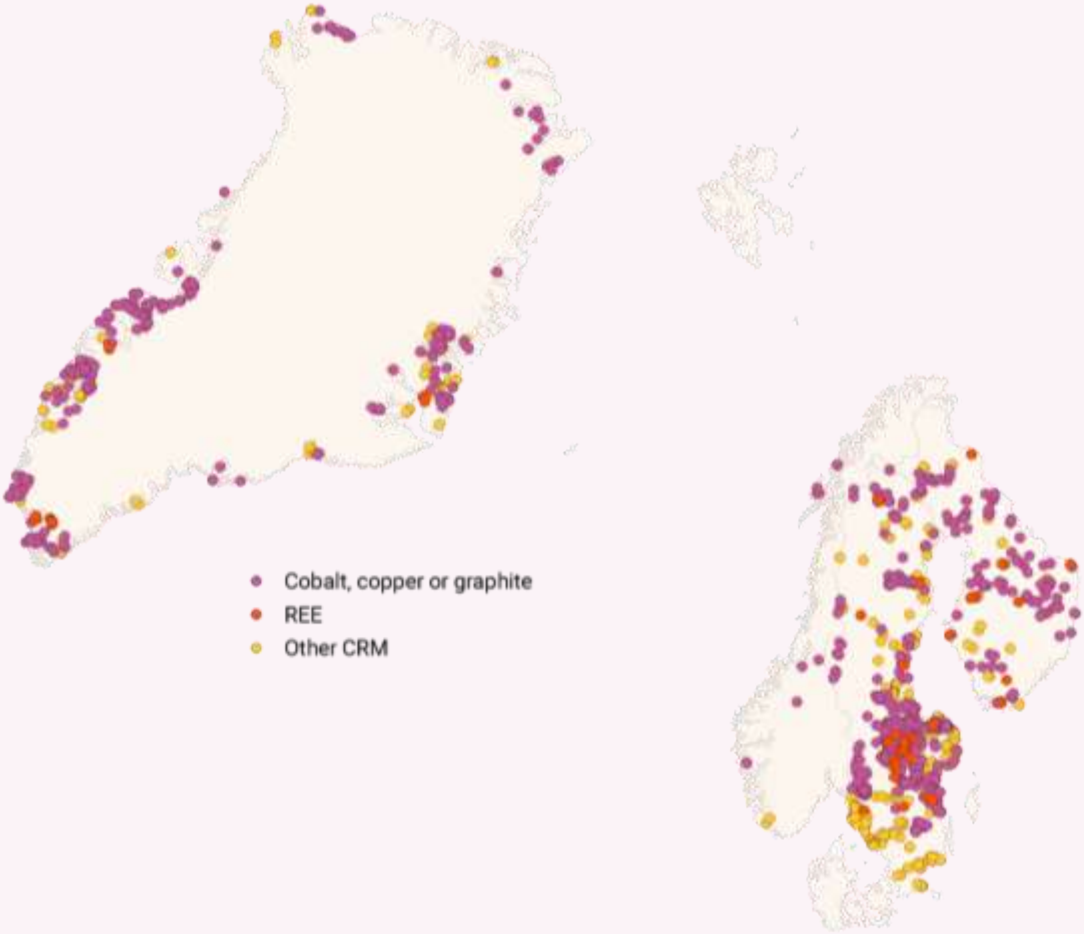
To complicate the situation further, most of the critical metals are "companion metals", meaning that they can only be produced as part of the production of another metal. Nickel and cobalt are an example; increasing the production of cobalt requires an increase in the production of nickel. This can lead to overproduction and price dumping of certain metals as the demand for their companion metals increases, potentially hindering the mining and extraction process.

However, companionability can also be seen as a positive factor. In known reserves of one metal, it is often likely that a companion metal will be found as well. This has been the case in Sweden: in Kiruna's iron ore reserves, Europe's largest known deposit of REE has been found. Moreover, Sweden and Finland already produce nickel and copper, while Norway is mining graphite. In 2023, Sweden made up 93% of EU iron production (iron is not a critical material, but its byproducts can include REE) and Norway 5% of EU graphite imports, while 34% of graphite imports came from China. Finland is the only country in Europe with primary production of cobalt and refines 10% of all cobalt in the world.

The Nordic countries, including Greenland, have a significant potential for furthering the future supply of metals and minerals, as both primary and secondary sources in processes that are already up and running today. So far, there are both known reserves and probable mineral resources of various critical raw materials in most of the Nordic countries. Greenland stands out in that it has undergone less exploration for minerals than the other Nordic countries, and its known reserves of REE are of "worldclass size", which may explain Donald Trump's recent interest in Greenland. In the Nordics, known deposits that are not currently being mined include graphite, cobalt, lithium, tungsten and REE in Sweden; gallium and REE in Norway; germanium, graphite and REE in Greenland, and lithium in Finland. Sweden is now one step closer to opening a graphite mine outside Vittangi, after long disagreements between local politicians and the government. The decision is justified as being of national interest and because of the high risk of supply disruptions. In 2024, it emerged that China for a long period of time had prevented export of graphite to Sweden, while a Chinese company had applied to open synthetic graphite production in Sweden.

The Nordic mining industry has greater access to fossil-free energy sources (such as hydropower and wind) compared to many other countries, where coal is used in energy-intense processes. Combined with its use of advanced machinery, Nordic mining is less carbon-intensive and safer for workers in the industry. If Nordic mining were extended to REE, for example, the price would probably be higher than if these elements were mined and refined in e.g. China. Yet, considering trade barriers and taxes, Nordic metals might not be significantly more expensive. However, in addition to extending mining to more materials such as REE, it is equally important to develop refining facilities and capabilities so that a supply chain for the EU can truly be secured. As more countries diversify their raw-material supply chains, Nordic metals and minerals could have strong market potential, especially with EU support.

Critical and Strategic minerals in Sweden, Norway, Finland and Greenland



Source: EGDI v1.6.16027 /MIN4EU 2023, Critical Raw Material. REE = Rare earth elements, CRM = Critical raw materials.
For Sweden, Norway, Finland, the dots show known mineral deposits, while Greenland also includes occurrence points for assumed resources.

Appendix

SWEDEN: Key economic indicators, 2023-2026

Annual % change unless stated otherwise	2023	2024F		2025F		2026F	
Real GDP growth (calendar-adjusted)	0.0	0.6	(0.6)	2.0	(2.3)	3.0	(2.8)
Real GDP growth per capita (calendar-adjusted)	-0.3	0.3	(0.4)	1.7	(2.1)	2.8	(2.6)
Real GDP growth	-0.2	0.6	(0.6)	1.7	(2.0)	3.3	(3.1)
Household consumption	-2.2	0.1	(0.0)	1.8	(2.5)	3.7	(3.2)
Government consumption	1.4	1.3	(1.3)	1.5	(1.3)	1.8	(1.9)
Gross fixed capital formation	-1.5	-1.4	(-2.1)	2.1	(2.0)	4.4	(4.0)
private excluding housing	3.4	-0.2	(-0.5)	1.4	(1.1)	4.0	(3.5)
public & NPISH	4.1	4.0	(2.9)	4.3	(4.0)	3.5	(4.1)
housing	-23.4	-13.3	(-15.5)	2.4	(2.8)	7.4	(6.6)
Exports, goods and services	3.2	2.0	(1.6)	2.1	(1.9)	3.2	(3.3)
Imports, goods and services	-1.1	2.0	(0.4)	1.9	(2.2)	3.4	(3.4)
Change in inventories (contribution to GDP)	-1.5	0.4	(0.1)	-0.2	(0.2)	0.1	(0.0)
Domestic demand, excl. inventories (contribution to GDP)	-1.0	0.1	(-0.2)	1.7	(1.9)	3.2	(2.9)
Net exports (contribution to GDP)	2.3	0.1	(0.7)	0.1	(0.0)	0.0	(0.1)
CPI (average)	8.6	2.9	(2.8)	0.6	(0.6)	1.8	(1.5)
CPIF (average)	6.0	1.9	(1.9)	2.1	(2.1)	2.0	(1.9)
CPIF excluding energy (average)	7.5	2.7	(2.7)	2.3	(2.2)	1.9	(2.0)
Riksbank policy rate (December)	4.00	2.50	(2.50)	2.00	(1.75)	2.00	(1.75)
Unemployment (% of labour force, 15-74)	7.7	8.4	(8.4)	8.4	(8.5)	8.0	(8.0)
Change in labour force (15-74)	1.6	0.2	(0.3)	0.1	(0.3)	0.7	(0.5)
Change in employment (15-74)	1.4	-0.6	(-0.6)	0.1	(0.2)	1.1	(1.1)
Employment rate (15-74)	69.5	69.0	(69.0)	68.8	(68.9)	69.3	(69.4)
Number of hours worked (calendar-adjusted)	1.4	-0.5	(-0.5)	0.4	(0.6)	1.2	(1.3)
Nominal hourly wage (NMO, whole economy)	3.8	4.0	(4.0)	3.6	(3.6)	3.6	(3.6)
Household real disposable income	-1.3	1.4	(1.2)	2.6	(2.4)	2.5	(2.8)
Household own savings (% of disposable income)	5.3	6.4	(7.2)	7.0	(7.1)	6.0	(6.7)
Balance of goods and services (% of GDP)	4.0	3.9	(n/a)	3.6	(n/a)	3.6	(n/a)
Current account balance (% of GDP)	6.7	6.2	(n/a)	5.8	(n/a)	5.7	(n/a)
General government budget balance (% of GDP)	-0.8	-1.6	(-1.5)	-0.9	(-1.0)	-1.0	(-0.5)
General government debt (Maastricht, % of GDP)	31.5	33.5	(33.4)	33.5	(33.2)	33.5	(33.1)

Previous forecast in parentheses
Sources: Statistics Sweden & Swedbank Research

ESTONIA: Key economic indicators, 2023-2026

Annual % change unless stated otherwise	2023	2024F		2025F		2026F	
Real GDP	-3.0	-0.8	(-0.8)	1.5	(1.5)	2.5	(2.5)
Household consumption	-1.3	-1.2	(-0.3)	0.5	(0.5)	3.5	(3.5)
Government consumption	0.9	1.0	(1.5)	-0.5	(-0.5)	0.0	(0.0)
Gross fixed capital formation	7.5	-6.0	(-4.0)	4.0	(4.0)	5.0	(5.0)
Exports of goods and services	-9.0	-1.5	(-1.0)	2.5	(2.5)	3.5	(3.5)
Imports of goods and services	-6.7	-1.0	(-0.5)	2.0	(2.0)	4.5	(4.5)
CPI (average)	9.2	3.5	(3.7)	4.0	(4.3)	3.5	(3.5)
Unemployment (% of labour force)	6.4	7.6	(7.6)	7.2	(7.2)	6.5	(6.5)
Employment	2.5	0.8	(1.0)	-0.4	(-0.4)	0.4	(0.4)
Gross monthly wage	11.4	7.9	(7.3)	6.3	(6.5)	6.1	(6.2)
Nominal GDP (billion euro)	38.2	39.4	(39.3)	41.6	(41.6)	44.1	(44.1)
Exports of goods and services (nominal)	-5.9	0.6	(0.5)	4.5	(4.5)	5.6	(5.6)
Imports of goods and services (nominal)	-8.2	-0.1	(0.0)	4.0	(4.0)	6.6	(6.6)
Balance of goods and services (% of GDP)	0.9	1.2	(1.2)	1.6	(1.5)	0.9	(0.8)
Current account balance (% of GDP)	-1.7	-0.9	(-0.7)	-0.3	(-0.3)	-0.9	(-0.8)
General government budget balance (% of GDP)	-2.8	-2.7	(-2.8)	-2.9	(-2.8)	-2.1	(-2.0)
General government debt (Maastricht, % of GDP)	20.2	22.9	(23.0)	24.8	(24.7)	25.9	(25.7)

Previous forecast in parentheses
Sources: Statistics Estonia & Swedbank Research

LATVIA: Key economic indicators, 2023-2026

Annual % change unless stated otherwise	2023	2024F		2025F		2026F	
Real GDP	1.7	-0.2	(-0.3)	2.2	(2.4)	2.8	(2.8)
Household consumption	-1.0	0.4	(0.3)	2.5	(2.8)	2.8	(2.8)
Government consumption	7.0	7.5	(7.0)	1.9	(1.3)	1.2	(1.2)
Gross fixed capital formation	9.9	-6.0	(-4.7)	5.5	(6.6)	5.1	(5.1)
Exports of goods and services	-4.7	-2.0	(-2.2)	2.0	(2.4)	3.8	(4.0)
Imports of goods and services	-2.0	-2.7	(-2.9)	3.9	(4.3)	4.0	(4.1)
CPI (average)	8.9	1.3	(1.3)	2.6	(2.6)	2.5	(2.5)
Unemployment (% of labour force)	6.5	6.9	(7.0)	6.5	(6.5)	6.0	(6.0)
Employment	-0.2	-0.7	(-0.4)	0.7	(0.5)	0.5	(0.2)
Gross monthly wage	11.9	9.5	(8.7)	6.5	(6.0)	7.0	(7.0)
Nominal GDP (billion euro)	39.1	39.9	(39.9)	41.7	(41.8)	44.1	(44.4)
Exports of goods and services (nominal)	-6.4	-1.5	(-2.2)	3.2	(3.6)	5.0	(5.2)
Imports of goods and services (nominal)	-7.1	-2.7	(-3.3)	4.9	(5.3)	4.7	(4.8)
Balance of goods and services (% of GDP)	-3.7	-2.8	(-2.8)	-3.8	(-3.9)	-3.6	(-3.6)
Current account balance (% of GDP)	-3.9	-2.3	(-3.0)	-3.2	(-3.5)	-2.9	(-3.1)
General government budget balance (% of GDP)	-2.4	-2.0	(-3.0)	-3.0	(-3.1)	-2.9	(-3.0)
General government debt (Maastricht, % of GDP)	45.0	47.9	(46.2)	47.7	(47.4)	49.9	(48.7)

Previous forecast in parentheses
Sources: Statistics Latvia & Swedbank Research

LITHUANIA: Key economic indicators, 2023-2026

Annual % change unless stated otherwise	2023	2024F		2025F		2026F	
Real GDP	0.3	2.4	(2.4)	3.0	(3.0)	2.5	(2.5)
Household consumption	0.3	3.7	(3.7)	4.4	(4.4)	4.0	(4.0)
Government consumption	-0.2	1.4	(1.2)	1.0	(1.0)	1.0	(1.0)
Gross fixed capital formation	9.3	0.2	(4.0)	6.2	(6.2)	5.5	(5.0)
Exports of goods and services	-3.4	1.8	(2.2)	4.2	(4.4)	4.0	(4.0)
Imports of goods and services	-5.3	0.2	(1.0)	5.2	(5.6)	5.0	(5.2)
CPI (average)	9.5	0.7	(0.7)	3.0	(2.7)	2.7	(2.7)
Unemployment (% of labour force)	6.8	7.2	(7.2)	7.5	(7.5)	7.5	(7.5)
Employment	1.4	1.9	(1.8)	0.3	(0.1)	0.3	(0.1)
Gross monthly wage	12.2	10.2	(9.6)	9.4	(9.2)	7.7	(7.2)
Nominal GDP (billion euro)	73.8	78.2	(76.3)	83.0	(80.7)	87.4	(85.0)
Exports of goods and services (nominal)	-3.6	1.3	(2.9)	6.0	(7.1)	5.5	(6.5)
Imports of goods and services (nominal)	-10.7	-2.0	(0.8)	7.2	(8.5)	6.5	(7.5)
Balance of goods and services (% of GDP)	3.9	6.0	(5.4)	5.2	(4.5)	4.6	(3.8)
Current account balance (% of GDP)	1.1	4.1	(3.9)	3.4	(2.9)	3.1	(2.3)
General government budget balance (% of GDP)	-0.8	-1.7	(-1.8)	-2.9	(-3.0)	-2.5	(-2.3)
General government debt (Maastricht, % of GDP)	38.3	37.2	(38.2)	43.0	(43.0)	43.3	(44.3)

Previous forecast in parentheses
Sources: Statistics Lithuania & Swedbank Research

Interest and exchange rate forecasts

	Outcome	Forecast			
	2025	2025	2025	2026	2026
	24 Jan	30 Jun	31 Dec	30 Jun	31 Dec
Policy rates (%)					
Federal Reserve, USA (upper bound)	4.50	4.50	4.00	3.75	3.50
European Central Bank (refi rate)	3.15	2.15	1.90	1.65	1.65
European Central Bank (deposit rate)	3.00	2.00	1.75	1.50	1.50
Bank of England	4.75	4.25	3.75	3.50	3.50
Riksbank	2.50	2.00	2.00	2.00	2.00
Norges Bank	4.50	4.00	3.50	3.00	2.75
Government bond rates (%)					
US 2y	4.27	4.30	4.10	4.00	3.90
US 5y	4.43	4.40	4.40	4.30	4.20
US 10y	4.63	4.80	4.70	4.50	4.40
Germany 2y	2.29	2.00	1.90	1.80	1.80
Germany 5y	2.36	2.20	2.10	2.00	2.00
Germany 10y	2.55	2.50	2.40	2.30	2.20
Exchange rates					
EUR/USD	1.05	1.03	1.06	1.08	1.10
EUR/GBP	0.84	0.85	0.84	0.84	0.83
EUR/SEK	11.46	11.30	11.10	11.00	10.90
EUR/NOK	11.75	11.50	11.35	11.30	11.20
USD/SEK	10.94	10.97	10.47	10.19	9.91
USD/CNY	7.24	7.40	7.30	7.30	7.30
USD/JPY	155.7	150.0	145.0	140.0	140.0
NOK/SEK	0.98	0.98	0.98	0.97	0.97
KIX (Trade-weighted SEK)	126.6	125.2	122.4	120.8	119.3

Sources: Swedbank Research & Macrobond

Swedish interest rate forecasts (%)

	Outcome	Forecast			
	2025	2025	2025	2026	2026
	24 Jan	30 Jun	31 Dec	30 Jun	31 Dec
STIBOR 3m	2.40	2.10	2.10	2.10	2.10
Government bond yields					
2y	2.02	2.10	2.10	2.20	2.20
5y	2.16	2.30	2.30	2.30	2.30
10y	2.40	2.50	2.50	2.50	2.50
Swap rates					
2y	2.35	2.40	2.40	2.50	2.50
5y	2.47	2.60	2.60	2.60	2.60
10y	2.68	2.80	2.80	2.80	2.80

Sources: Swedbank Research & Macrobond

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