STATE STREET GLOBAL ADVISORS

May 16, 2025
Commentary

Weekly Economic Perspectives

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Weekly Highlights

Big relief on China tariffs ignites risk-on market moves.

US CPI Inflation (Apr, YoY)

2.3%

Lowest since February 2021.

US Core CPI Inflation (Apr, YoY)

2.8%

Twin-lowest since March 2021.

US Retail Sales (Apr, m/m)

0.1%

Softening after prior surge.

UK Unemployment Rate (April, 3 months)

4.5%

In line with expectations.

UK GDP (Q1, q/q, prelim)

0.7%

Above expectations.

UK Industrial Production (Mar, m/m)

-0.7%

.Worse than expected.

JP: Capex (Q1,YoY)

3.6%

Highest since Q3 2019!

JP: Domestic Demand Contribution (Q1, pp)

+0.7

As good as it gets

AU: Employment (Apr, thous.)

89.0

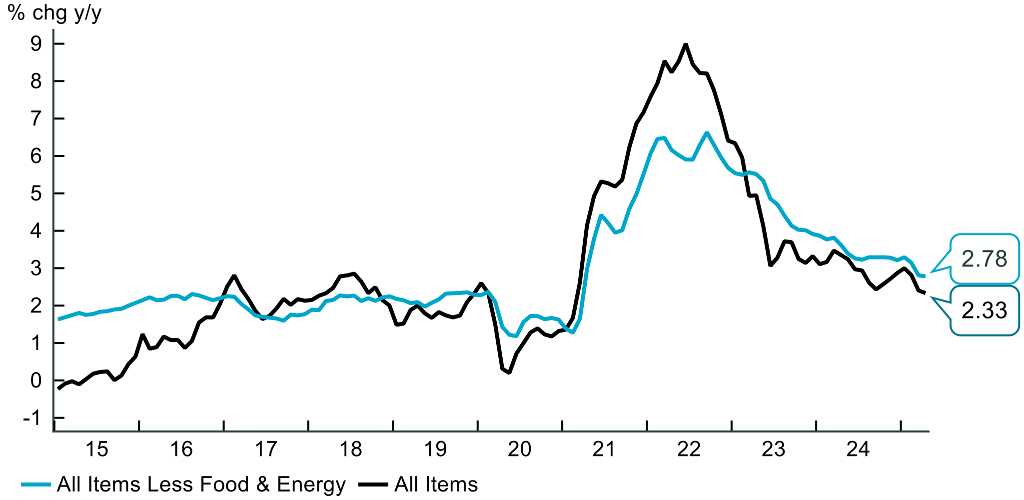
Queensland floods + strong demand.

US: OK Inflation, More Tariff Relief

Last week we said that the **April inflation** data could be a slight dovish surprise; the data this week confirmed that expectation. Both overall and core (ex food and energy) consumer prices rose 0.2% m/m, allowing the headline inflation rate to ease a tenth to 2.3% y/y and keeping the core inflation rate unchanged at 2.8% y/y. For headline, this was the lowest print since February 2021; for core, the twin-lowest since March 2021. That being said, these numbers are almost guaranteed to mark local bottoms for each of these series due to difficult base effects and tariffs impact over the next several months. Nevertheless, with the labor market already in balance, tariff risks greatly diminished amid ongoing negotiations, and the Fed Funds rate still in moderately restrictive territory, we very much continue to believe that the Fed should calibrate rates lower.

The details were perhaps less dovish than the headline. Goods prices were flat and service prices rose 0.4%, double the March rate. In addition to energy services, medical care services were a big driver, with prices jumping 0.5% m/m. Shelter prices increased 0.3% m/m, with OER up 0.4% m/m. Other, more discretionary areas of services were better behaved, with recreation flat and airline fares down 2.8% m/m. Food prices were bifurcated: Food at home prices declined 0.2% m/m, reflecting—among others—a big drop in egg prices (we think there is room for further reductions) while food away from home prices rose another 0.4% m/m. Energy prices increased 0.7%, largely on the back of a sizable increase in piped gas services. This was somewhat at odds with gas price behavior but may reflect delayed passthrough of prior cost increases.

Figure 1: April To Mark Temporary Bottom For US Inflation



Sources: Macrobond, SSGA Economics, BLS
Updated as of 5/14/2025

Much more important than the April inflation data was the announcement of tariff de-escalation with China. In the April 14 Weekly Economic Perspective we write the following: "The further increase in US tariffs on China (to 145%) and retaliatory Chinese tariffs on the US (125%) is no "joke"; it is very serious business, but not good business. We argued that the April 2 tariffs were unsustainable, and we argue the same here. There are many valid grievances that the US has vis-à-vis China's trade practices. However, imposing tariffs of this magnitude goes far beyond making the point; it actually diminishes it. And so, we look forward to a near-term de-escalation so that meaningful negotiations can unfold. At the end of the day, the world needs the US, the US needs the world, and we all need trade." The announcement this week of a 90-day delay in reciprocal and retaliatory tariffs between US and China bring back a sense of normality to global trade. It may be a fragile equilibrium, but the 90-day negotiation window is not just a holding place – its purpose is to turn it into something more robust. We remain watchful, but we are doing the watching with much less oppressive anxiety.

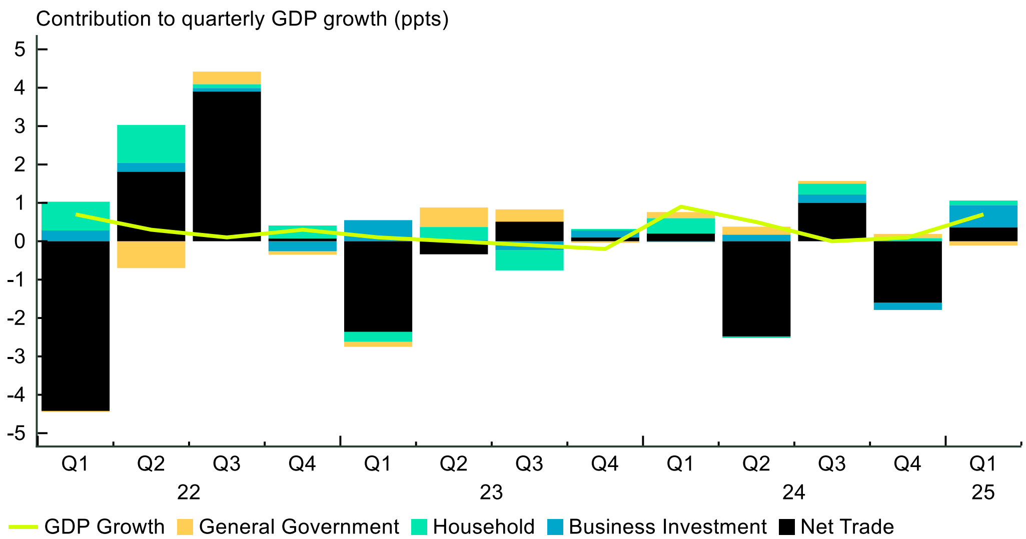
UK: Firm Growth, But on the Surface

On the surface, the economy is expanding robustly with stronger-than-expected Q1 print. But the details were mixed.

The UK Q1 2025 print this week came in stronger than expected. Growth was 0.7% q/q, a sharp increase from the 0.1% q/q previous quarter and above market expectation of 0.6% q/q. Importantly, most of the strength in this quarter came from gross fixed capital formation (GFCF), and particularly business investment. Trade also outperformed with both exports and imports beating expectations. In contrast, household and government consumption performance was disappointed.

Nevertheless, the details raise questions about the sustainability of Q1 strength. Higher investment was mainly driven by large increases in transport equipment which is the major export to the US. Admitted, not all of these will be exported to the US, but it does suggest some element of Trump effect and is linked to front-loading. Exports to the US rose by £2.4bn in Q1 (to £17.5bn) while imports were up £1.3bn (to £15.4bn). That said, we would expect this growth to fade in the coming months. The modest increase 0.2% q/q in household consumption reflects higher spending on household goods and services and housing. This is contrast to recent retail sales figures, which have been surprisingly strong. However, GDP data does lag retail sales and so there are chances that these measures could converge over the coming months. Meanwhile, the decline in government spending (-0.5% q/q) was due to lower healthcare and education spending. Here, it suggests that the fiscal stimulus has faded faster than we expected.

Figure 2. GDP Overshot But Domestic Demand Is Weakening



Sources: Macrobond, SSGA Economics, ONS
Updated as of 16/05/2025

Overall, the implications of this print are still unclear. On one hand, the GDP overshot on the back of a decline in government spending does suggest an underlying strength that has not been captured in recent data. On the other hand, it's now looking that supply has not been constrained as much as previously thought while demand weakening continues. That will help to limit the upside risks to the inflation.

Japan: GDP Disappoints, but Domestic Demand Is Firm

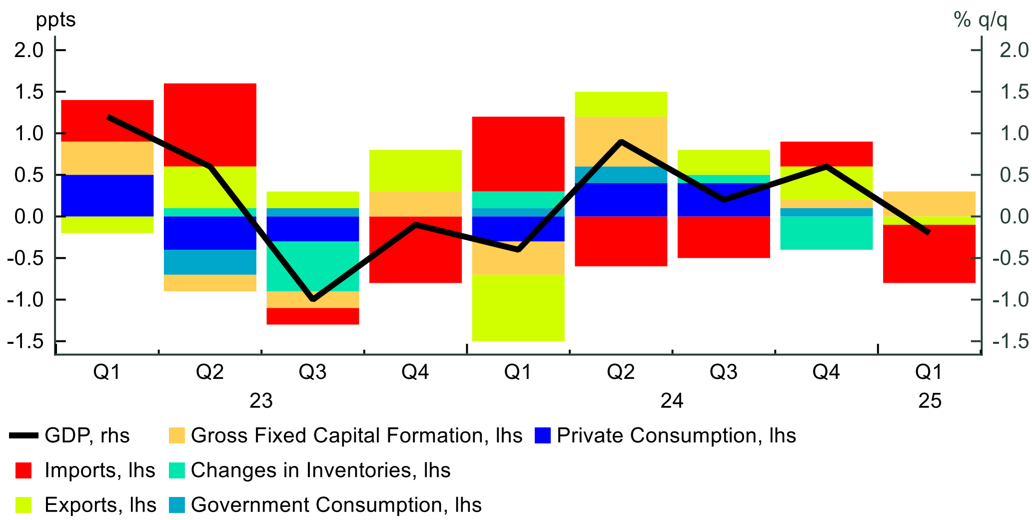
The preliminary estimate of Q1 GDP showed that it contracted -0.2% q/q (-0.7% annualized), missing our +0.3% pick by a big margin. The key difference came from external demand, which turned negative for the first time in four quarters. Exports were in line with expectations at 3.8% y/y, although services exports (tourism) eased as usual in the first quarter owing to seasonality. However, very interestingly, imports overshot expectations at 6.5% and within that, services imports were even stronger with a sequential rise of 4.5% q/q, highest since Q3 2023. All this meant that net exports detracted a massive 0.8 pp off of growth.

On the contrary, domestic demand was very resilient as expected and added 0.7 pp to growth. Private consumption rose 1.6% y/y, the strongest showing since Q1 2023. Durable goods consumption shot up 13.6%, highest since Q2 2021. All other categories also performed better with expectations.

The most significant positive surprise however was capital expenditures, which rose 3.6% y/y, the highest since Q3 2019! This is all the more surprising as we expected capex to have stalled on heightened uncertainty; notwithstanding it, the rise came on the back of labor shortages as well as a strong corporate intent on investments. Private housing investments also rose sharply by 3.0%.

Figure 3: Imports Drag Japan's GDP Amid Strong Domestic Demand

Contribution To GDP Growth



Sources: SSGA Economics, CAO, Macrobond
Updated as of 5/18/2025

So, on the surface, GDP missed our expectations by a lot, but details imply more of an upside surprise. Hence, we view the data as very encouraging, especially as consumption was strong while capital expenditures remained resilient.

From hereon though, the outlook depends entirely on how, when, and whether Japan signs a trade deal with the US, on which there has been little progress. Media reports suggest that Japan is negotiating hard on auto tariffs, which account for over three-fourths of its deficit with the US and also a key focus for President Trump.

Prime Minister Ishiba is positioning himself for the upper house elections in July, which is a very hard given his weaning popularity and tough choices on trade. He reportedly is not willing to let US agricultural imports into Japan too, failing which could weaken the prospects for his Liberal Democratic Party, considering the sector's powerful lobby. The hard-bargain strategy could backfire not only on PM Ishiba, but also on the Japanese economy and we worry if the Bank of Japan (BoJ) will have to eventually take a longer pause than expected. In the face of this raging uncertainty we maintain our macro outlook, that Japan's GDP may rise between 0.7%-1.0% in 2025 and that the BoJ might hike only once, likely in Q4.

The focus for the next week will squarely be on the third round of negotiations with the US in Washington. We look forward to some positive developments.

Week in Review

Our summary of the key global data releases from the past week.

Country	Release (Date, format)	Consensus	Actual	Last	Comments
Monday, May 12					
No major data release.					
Tuesday, May 13					
US	CPI (Apr, y/y)	2.4%	2.3%	2.4%	Good report, but will move up from there.
UK	ILO Unemployment Rate (Mar, 3mths)	4.5%	4.5%	4.4%	Softening.
GE	ZEW Survey Expectations (May)	11.3	25.2	-14	Clear momentum.
AU	Westpac Consumer Conf (May, m/m sa)	n/a	2.2%	-6.0%	Consumers are still not confident enough.
Wednesday, May 14					
GE	CPI (Apr, y/y, final)	2.1%	2.1%	2.2%	No big surprises.
JN	PPI (Apr, y/y)	4.0%	4.0%	4.3% (↑)	Inflationary pressures in the pipeline.
Thursday, May 15					
US	Empire Manufacturing (May)	-8.0	-9.2	-8.1	Soft but appears to be stabilizing/
US	Retail Sales Advance (Apr, m/m)	0.0%	0.1%	1.7% (↑)	Pull back after surge.
US	PPI Final Demand (Apr, m/m)	0.2%	-0.5%	0.0% (↑)	Welcome but outweighed by tariffs.
US	Initial Jobless Claims (May 10, thous)	228	229	229	Steady.
US	Industrial Production (Apr, m/m)	0.1%	0.0%	-0.3%	Nothing spectacular.
CA	Existing Homes Sales (Apr, m/m)	1.0%	-0.1%	-4.8%	Disappointing.
UK	GDP (Q1, q/q, prelim)	0.6%	0.7%	0.1%	Domestic demand clearly weakened,
UK	Industrial Production (Mar, m/m)	-0.5%	-0.7%	1.7% (↑)	Worse than expected.
FR	CPI (Apr, y/y, final)	0.8%	0.8%	0.8%	Soft.
AU	Unemployment Rate (Apr)	4.1%	4.1%	4.1%	14^{th} month between 3.9%-4.3%
Friday, May 16					
JN	GDP (Q1, q/q sa, prelim)	-0.1%	-0.2%	0.6%	Good details but bad headline.
JN	Industrial Production (Mar, m/m, final)	n/a	0.2%	-1.1%	Stress is clear.
US	Housing Starts (Apr, thous)	1,364	1,361	1,339 (↑)	Soft.
US	Building Permits (Apr, prelim, thous)	1,450	1,412	1,481 (↑)	Soft.
US	U.of Mich. Sentiment (May. Prelim)	53.4	50.8	52.2	Bleak!

Source: for data, Bloomberg®; for commentary, SSGA Economics.

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* Pensions & Investments Research Center, as of December 31, 2023

† This figure is presented as of June 30, 2024 and includes ETF AUM of $1,393.92 billion USD of which approximately $69.35 billion USD is in gold assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated. Please note all AUM is unaudited.

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