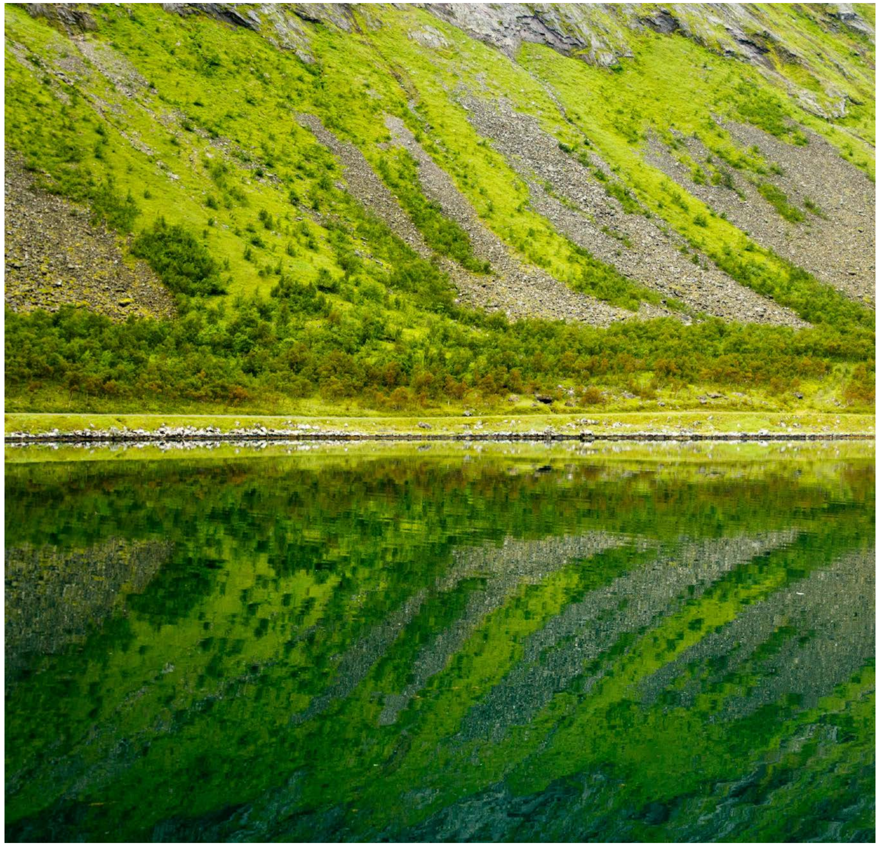
Q1 2025
Market commentary

Global governments, markets and investors experienced an economically and politically turbulent first quarter as Donald Trump regained the Oval Office. Headline hunters were bombarded with a flurry of executive orders and policy revisions, sweeping federal department cuts and promises to resolve complex geopolitical crises at a stroke.

The president's opening actions were also influenced by a longstanding personal grievance that the US has enjoyed less return value and fewer resources for all it's invested in global trade deals and security. Even before his second term, Trump signalled that "America first" would herald a new and uncompromising era of reciprocal tariffs to reverse decades of perceived unfair treatment and disrespect from global trading partners. The announcement of those tariffs on 2 April – "Liberation Day" – raised questions about their long-term impacts and calculation metrics but left no doubt they represented a significant shock to global trade and economics. Consequently, the Global Economic Policy Uncertainty (GEPU) Index ended the quarter at its highest level since the beginning of the Covid crisis.

However, Trump's powerplay for American enterprise did little to raise domestic growth expectations during Q1. The launch of China's DeepSeek generative AI model significantly undercut existing market leaders and hit the hitherto booming technology sector hard. Investors rotated into sectors not dominated by the tech giants as questions were asked about the long-term sustainability of returns from huge upfront investments in AI infrastructure. The wider effects of evolving US economic policy also impacted investor sentiment. The potential economic and inflationary consequences of trade tariffs are still largely unknown, as are the swingeing cuts made to federal department spending and employment by Elon Musk's Department of Government Efficiency (DOGE), especially as DOGE's remit to reduce the fiscal deficit in the long-term comes with shorter-term job losses and contract cancellations. These cuts are already having a significant impact on the US's ability to address climate change and are weakening environmental protection. There have already been aggressive cuts to the Environment Protection Agency and the National Oceanic and Atmospheric Administration has been disbanded, which plays a key role



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in climate science and weather prediction and operates a vast infrastructure of satellites, ocean buoys and forecasting stations globally. Tariff-related uncertainty was reflected in volatile US equity markets reacting to shifting expectations regarding the severity of pending announcements and pre-emptive tariff charges placed on infrastructure commodities and automobiles. In this environment, the Federal Reserve took no action on interest rates during the quarter, though Fed Chair Jerome Powell indicated in March that a rate cut would be considered if domestic growth slowed and unemployment rose.

Trump's combative stance had a galvanising effect on European policymakers. With the president and US defence secretary Pete Hegseth decrying the country's "imbalanced relationship" with its Nato allies, the European Commission announced a significant increase in spending to boost the region's defensive capabilities. The €800 billion spending target comprises €150 billion of new initial borrowing and an additional €650 billion raised by allowing member states more fiscal latitude for defence spending within the Commission's rules. A less cautious approach to fiscal deficits was most evident in Germany where the Christian Democratic Union party pushed through parliamentary consent to lift the deficit cap on the country's defence spending and fund a €500 billion domestic infrastructure development programme. Investor response saw Germany's DAX Index enjoy its strongest Q1 since 2023. When reciprocal trade tariffs were initially threatened by the US, a vocal minority in the EU suggested that the region should loosen its regulatory frameworks to encourage increased investment. This position gained more traction among member states as the quarter progressed and the European Central Bank welcomed the change in approach and the prospect of further fiscal stimulus. It also cut the region's base rate twice during the quarter with more cuts expected during the year.

The UK was targeted with Trump's minimal 10% "baseline" tariff and domestic equities proved relatively robust prior to the chaotic events of Liberation Day. The government nevertheless took note of changing attitudes to global trade relationships and announced a cut to its foreign aid budget to finance a 2.5% increase in defence spending. The economy remained sluggish, however, and some economists argued that slow progress coupled with higher interest rates on government borrowing would limit the effects of increased defence spending on overall growth. Chancellor Rachel Reeves was also forced to make further cuts to welfare benefits departments after the Office for Budget Responsibility (OBR) concluded that reforms to the welfare system would save much less than ministers claimed. The chancellor's Spring Statement also saw the OBR halve its 2025 UK growth forecast from 2% to 1%.

Global financial institutions rethink net zero commitments after Trump's election victory

Some major global banks and asset managers caught between real-world, science-based climate risks and escalating political opposition to sustainability withdrew from financial sector climate initiatives during the quarter. Deregulation in the energy sector and the threat of government criticism created a "chilling effect" among financial institutions less certain about the future of their climate strategies.

After the Republican election victory, the Net Zero Banking Alliance (NZBA) saw US financial institutions backtrack on their net zero targets, arguing that they couldn't decarbonise any faster than the wider economy. Top European lenders also threatened to withdraw from the NZBA unless it loosened its rules. In response, the NZBA proposed a vote among its remaining members to replace its existing pledge to track the Paris Agreement's 1.5°C global climate target with a less onerous commitment to keep warming "well below 2°C".

The parallel Net Zero Asset Managers initiative (NZAM) suspended all activities to track its signatories' reporting and implementation commitments after the withdrawal of BlackRock. NZAM advised it would conduct a review to ensure it was still "fit for purpose" after policy shifts in the US and changing client expectations. Research by ShareAction found that the world's biggest asset managers were backing fewer resolutions seeking stricter climate targets, improved human rights policies and increased disclosure of corporate lobbying activities.

AI discussions focus on effective governance, secure access and risk management

Key presentations at February's landmark AI Action Summit in Paris warned against the environmental and resource impacts of generative AI, highlighted the risk potential for AI-driven productivity to create new global inequalities, and emphasised the importance of safeguarding security and sharing developmental breakthroughs. The summit's Statement on Inclusive and Sustainable Artificial Intelligence for People and the Planet outlined priorities such as promoting AI accessibility to reduce digital divides, ensuring AI is ethical and trustworthy, and reinforcing international cooperation for effective AI governance. The French government also announced the launch of a $400 million endowment for Current AI, a mechanism to democratise access to high-quality datasets, invest in open-source AI tools, and measure AI's wider societal impacts.

In March, the European Commission published the third and final draft of its General-Purpose AI (GPAI) Code of Practice. The Code details how GPAI providers and models with systemic risk can comply with their obligations under the EU AI Act, focusing on transparency and copyright-related rules, systemic risk assessment, the adoption of security frameworks, and technical and governance risk mitigation. The revised and streamlined final draft was submitted to a range of stakeholders including businesses, EU member states, civil society organisations and international observers. Once their feedback is assessed, the Commission expects the approved version of the Code to be launched in May 2025.

EU's Omnibus proposal "simplifies" the scope of regional sustainability reporting

Citing the need to increase regional competitiveness, the European Commission's Omnibus proposal presented itself as a "simplification" of due diligence and corporate sustainability reporting obligations under legislative measures like the Corporate Sustainability Reporting Directive (CSRD), the Corporate Sustainability Due Diligence Directive (CSDDD), and the Carbon Border Adjustment Mechanism (CBAM). Omnibus limits the scope of companies required to report under the EU Taxonomy, increases the number of company exemptions to relieve them of reporting burdens, and significantly reduces the number of reporting templates. MEPs voted in March to support the Commission's proposal which gave member states and the first tier of affected businesses an additional year to implement revised due diligence rules. Similar extensions will apply to second and third tier businesses which will also benefit from two extra years to incorporate CSRD requirements.

Ahead of the vote, Greenbank, alongside the wider Rathbones Group, signed onto a statement addressed to the European Union (EU) encouraging it not to reopen negotiations on its full suite of sustainability reporting directives. 165 investors, service providers and other supporting organisations supported the statement, calling on the European Commission to preserve the integrity and ambition of the EU's sustainable finance framework. Arguments made included the fact that businesses and investors require long-term consistent policy signals and access to comparable and high-quality reporting from companies to accurately inform investment decisions. Despite the large amount of investor and civil society support for the statement, the European Commission went ahead and published the package of proposals in February, marking a start of a process that could result in significant changes to EU sustainability reporting. The Commission's proposed changed will need to go through the EU's legislative process, with scrutiny and approval of the European Parliament and Council. Greenbank continue to look for opportunities to engage as the proposals make their way through the legislative process.

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