



# Global Outlook on Advanced and Emerging Economies

Macro Research Division

April 2026

## Introduction

The global economy in 2026 remains shaped by a sequence of overlapping shocks that have redefined macroeconomic conditions across regions. The legacy of the COVID 19 pandemic, the energy crisis triggered by the Russia Ukraine war, renewed conflict in the Middle East and a new wave of protectionist trade policies have increased inflation volatility, disrupted supply chains and intensified geopolitical fragmentation. In this environment, economic performance can no longer be understood through domestic fundamentals alone. Growth, inflation, fiscal sustainability and external balances are increasingly influenced by energy security, trade realignment political stability and strategic exposure to global shocks. This report examines how a diverse set of economies is responding to these pressures through monetary, fiscal and trade policy while also assessing the political and structural factors that shape resilience.

Rather than focusing exclusively on emerging markets, this report adopts a broader comparative perspective. It brings together major emerging economies such as Brazil, Indonesia, South Africa and Turkey alongside advanced economies and strategic cases such as Japan and Taiwan as well as a regional special feature on the Middle East. This wider scope reflects the reality that the key drivers of macroeconomic risk in 2026 cut across traditional development categories. Advanced economies are confronting many of the same external pressures as emerging ones while certain regions play an outsized role in shaping global inflation, energy markets, trade flows and investor sentiment. By comparing countries with different institutional structures, income levels and geopolitical positions, the report aims to provide a more complete picture of the global macroeconomic landscape and the main risks and opportunities likely to define the period ahead.

### Head of Macro Research

Alessandro Pagan: [alessandro.pagan@studbocconi.it](mailto:alessandro.pagan@studbocconi.it)

### Co-Head of Macro Research

Cao-Khai Mai: [khai.mai@studbocconi.it](mailto:khai.mai@studbocconi.it)

### Group leader:

Jovana Mrdalj: [jovana.mrdalj@studbocconi.it](mailto:jovana.mrdalj@studbocconi.it)

### Macro Research Analysts

Giandomenico Vumbaca: [giandomenico.vumbaca@studbocconi.it](mailto:giandomenico.vumbaca@studbocconi.it)

Maria Liova: [maria.liova@studbocconi.it](mailto:maria.liova@studbocconi.it)

Matthew Walzer: [matthew.walzer@studbocconi.it](mailto:matthew.walzer@studbocconi.it)

Pramit Priyam Saha: [pramit.saha@studbocconi.it](mailto:pramit.saha@studbocconi.it)

Ralph Hermans: [ralph.hermans@studbocconi.it](mailto:ralph.hermans@studbocconi.it)

Vittorio Cravanzola: [vittorio.cravanzola@studbocconi.it](mailto:vittorio.cravanzola@studbocconi.it)

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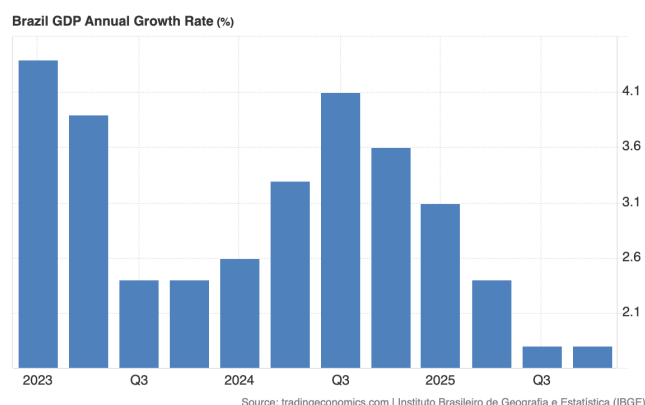
## SPECIAL FEATURE

### Middle East

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This expansion has transformed Brazil into a net exporter of oil, a characteristic that assumes particular significance in the context of the global energy crisis of 2026.

After a performance superior compared to the expectations in 2024, the growth decelerated to 2.3% in 2025, falling below 3% for the first time since covid time. The slowdown was led by the sector that is more exposed to tight monetary policy: private consumption and fixed investment have weakened significantly. GDP remained substantially stagnant on a quarter-on-quarter basis in the second half of 2025, with Q4 recording only 0.1% sequential growth (Trading Economics, March 2026). Agriculture and exports partially offset these negative factors, with the agricultural sector benefiting from an exceptional harvest in 2025 and exports growing by 3.7% in Q4.



For 2026, the forecasted growth has been cut from 2% to 1.6% by the principal institutions (World Bank and IMF) due to the conflicts in the Middle-East and the tight monetary policy. As of today the growth is still 1.9%, but is good to expect a decrease by the end of the year. The World Bank ranks Brazil 22th out of the 29 economies in Latin America and Caribbean for growth in 2026. The OCSE predicts a partial recovery at 2.2% in 2027, contingent upon the easing of monetary conditions and fiscal consolidation (OECD, December 2025). Key structural constraints include budget rigidities, low productivity growth, and an underdeveloped infrastructure base that limits private investment.

## Brazil

### Economic and Political Context

Brazil is the eleventh-largest economy in the world and the largest economy in Latin America, with a nominal GDP of 2.26 trillion of dollars (Investopedia, 2026). The economy is broadly diversified. The country is competitive in the agricultural sector, as it's the global leader in the export of soy, beef, coffee, sugar, and poultry. It also plays an important role in the export of some minerals: iron and crude oil. In recent years, the expansion in the production of offshore oil companies in the pre-sale has further increased the industrial share of GDP.

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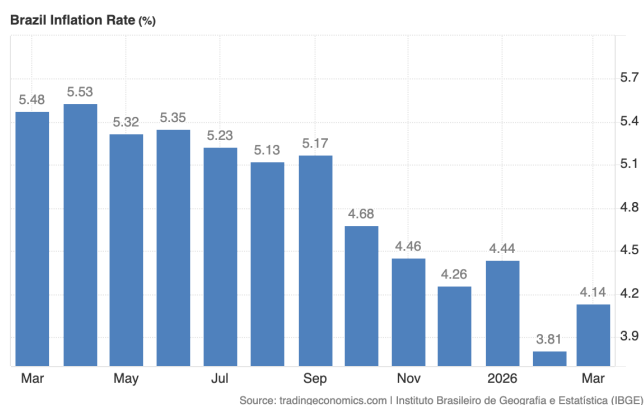


On the political side, the president Luiz Inácio Lula da Silva declared that he's running for a fourth term in the general elections scheduled for October 4, 2026. His agenda is focused on social protection, progressive tax reform, and climate investment. Lula's approval rating fell to 44% against 51% disapproval in the latest Genial/Quaest Survey, conducted March 6-9. The beneficiary is Senator Flavio Bolsonaro, who was designated by his imprisoned father as the right-wing opposition. Numerically Lula is ahead in a possible runoff scenario (46% vs 45%), even though within the margin of error (Rio Times, April 2026). The race seems to be one of the most competitive in recent Brazilian history. The pre-election pressures will most likely make the significant fiscal consolidation that Brazil needs difficult.

On the institutional side, Brazil continues to show signs of fragility. The Corruption Index stands at 35 points (December 2025), with Brazil ranking 107th in the global corruption ranking, unchanged from the previous year (Trading Economics, 2025). The country's Credit Rating stands at 46 as of April 2026, signaling a still elevated risk profile for international investors. The Gini index stands at 0.52, among the highest globally, reflecting persistent structural inequality (Statista, 2024).

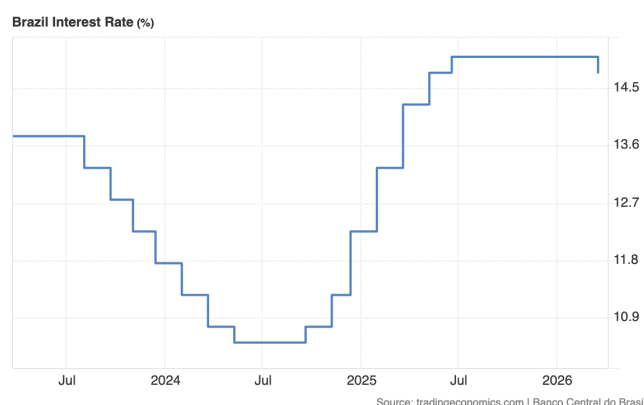
## Inflation and Monetary Policy

Inflation is still the principal macroeconomic challenge for Brazil. After closing the 2024 at 4.83%, the IPCA showed progressive moderation in 2025, settling at 4.26%. This is the lowest level since 2018 and, for the first time, within the Central Bank's tolerance range (1.5%–4.5%) (IBGE, 2025).



At the beginning of 2026 the situation became more complicated. The annual rate fell to 3.81% in February, before rising back to 4.14% in March 2026, with a monthly increase of 0.88%, that is the highest in over a year (IBGE; Trading Economics, March 2026). The main drivers were transport and food, reflecting the pass-through of oil price increases linked to the closure of the Strait of Hormuz. The core inflation is at 4.72% noting persistent structural pressures in the services sector (Trading Economics, November 2025).

On the monetary side, The Copom kept the Selic at 15% for five consecutive meetings. The Selic is Brazil's benchmark overnight interest rate, set by the Copom (the Central Bank's monetary policy committee) and used as the main tool to control inflation. On March 18 2026, the Copom started the easing cycle with a cautious 25 basis points cut, bringing the Selic at 14.75%, a smaller cut compared to the market expectations. The Focus survey's year-end Selic consensus stands at 12.25%. However, Goldman Sachs has pushed its forecast for the next cut to September, suggesting the easing cycle may pause entirely for a few months (Rio Times, 2026).



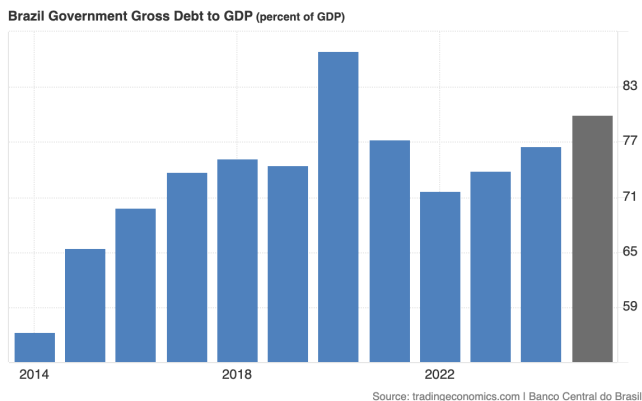
## Fiscal Policy and Public Finances

Brazil's public finance situation in 2026 is still critical. The nominal deficit of the consolidated public sector stood at 8.34% of GDP in 2025, while gross debt reached 79.2% of GDP in February 2026.



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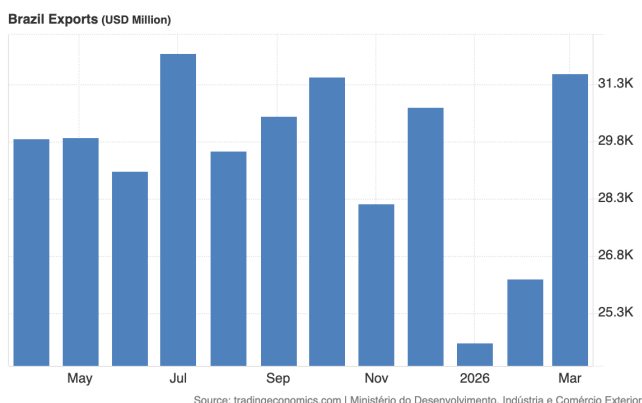
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General government debt is expected to rise to 95% in 2026 (Deloitte, 2026). The Brazilian government aims to return its primary balance to a surplus of 0.25% of GDP in 2026. Although, achieving this objective appears difficult in an election year, given the growing pressures for expansionary spending. The cost of debt remains high, with interest on public debt equal to \$16.9B, reflecting the impact of the Selic on public accounts. Post-election fiscal consolidation will be decisive for debt sustainability in the medium term (BBVA Research, March 2026).

## External Sector and Geopolitical Exposure

Brazil maintains a structurally strong trade position, with exports concentrated in agriculture and mineral commodities. China is the main commercial partner since 2009, this bond has become more important after the U.S. Tariffs.



In February 2026 exports to the United States fell 20.3%, while exports to China surged 38.7% in the same month.

The EU increased its imports from Brazil by 34.7% (Defense.info, March 2026). Although, Brazil was able to close the year 2025 with record exports, up US\$11.6 billion from 2024. This was possible thanks to the diversification towards China, India, and the European markets, facilitated also by the progress in the EU-Mercosur agreement.

On the geopolitical side, U.S. tariffs peaked 50% in 2025 before being reduced to 10% by the U.S. Supreme Court ruling in February 2026 (Atlantic Council, February 2026). As a crude oil exporter, Brazil partially benefits from the rise in energy prices linked to the conflict in the Middle East. However, a prolonged escalation would pose a risk through reduced global demand and increased prices for imported fertilizers (BBVA Research, March 2026).

## Key Risks and Upcoming Events

- General elections on October 4, 2026: the race is shaping up as a neck-and-neck contest between Lula and Flávio Bolsonaro
- Risk of pre-electoral fiscal expansion undermining budget targets
- Copom meeting on April 28-29, 2026: uncertain outcome between a pause and a cut
- Risk of de-anchoring of inflation expectations
- Public debt trajectory heading towards 95% of GDP in 2026 without credible consolidation
- Upward pressure on long-term interest rates if the market loses confidence in fiscal sustainability
- Evolution of the Middle East conflict and its impact on energy prices and domestic inflation
- Trajectory of Chinese demand for Brazilian commodities, in particular soybeans and iron ore
- Brazilian real volatility linked to pre-electoral uncertainty and the Selic easing cycle



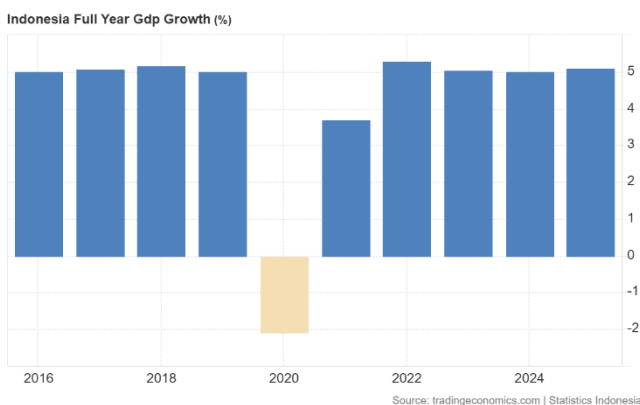
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## Indonesia

### Economic and Political Context

Indonesia is one of South East Asia's most robust emerging economies. Indonesia, has experienced economic growth of approximately 5.11% (statistic Indonesia), continuing the trend of strong economic performance post covid. The World Bank estimates that growth will continue at around the same rate in 2026 and 2027. Indonesia's growth is underpinned by high levels of house-hold consumption, strong investment, expansionary fiscal and monetary policies, and a positive net exports. Easing financial conditions and stable inflation provide support for Indonesia's ability to achieve continued growth in the near future. Indonesia has a relatively balanced GDP composition with the service sector being dominant (45.7%) supporting domestic demand whilst also maintaining a strong manufacturing sector (41.1%) and a small agricultural sector (13.2%) (Asian Development Bank).



Economic policy under President Prabowo Subianto's term so far is generally characterised by continuation rather than radical changes to the previous administration's policy. One reason for this is that the country's governance is still currently built around a broad governing coalition including the major parties that governed under the previous president. The governing coalition has experienced strong executive consolidation under Prabowo. This is argued to allow for reduced risks of political deadlock allowing policies to take effect faster. However, many fear opposition to the coalition is weak, limiting checks and balances and opening the pathway to democratic backsliding.

Additionally, though Prabowo promised continuation, nationalist and centralisation driven policies have taken effect. Prabowo has strived for greater control over domestic resources and industrial development in downstream industries and has implemented protectionist policies to achieve this. Concerns have risen regarding relations with trade partners and the shift away from market liberalisation. Moreover, Prabowo has made efforts to strengthen the role of the central government in line with his aims of building a state-led economy which he claims would improve welfare. At the core of the state-led policy framework is subsidies, incentives as well as other forms of regulation and investment to allocate capital to industries and directly influence economic outcomes. State-led enterprises also play a key role in the model as it gives the government control over key sectors.

In spite of the stable economic environment Indonesia is currently enjoying, the country's labor market continues to face challenges with weak wage growth and the informal economy remaining prevalent. One reason for this is the high hiring costs for employers which dissuades them from hiring permanent workers (DTDA). Instead, it prompts companies to favor outsourcing and temporary contracts. Moreover, labor law reforms from the beginning of the decade directed at reducing rigidities within the labor market have created unsatisfactory working conditions. According to the Global rights index, Indonesia is positioned as one of the worst countries for laborers. Jobs are however in fact being created for many in the labor force but these jobs are generally in low-skilled industries and are incapable of paying the standard middle-class wage. Though more jobs may be available to the lower classes and education is increasing, lower-class workers find themselves locked in a cycle of low-paying insecure jobs. Technological, demographic and other changes in the labor market have exacerbated income inequalities within the economy with less skilled-workers unable to adapt.

### Inflation and Monetary Policy

In the last few months of 2025, Inflation stayed at around 2.5-3% comfortably within Bank Indonesia 2.5%±1% target range (Statistics Indonesia). This is in contrast to earlier months in the year when the inflation rate was unusually low (but still in target range).



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However, the shift is policy driven rather than a result of changes in aggregate demand within the year. Government interventions such as subsidies on electricity and price controls had temporarily subdued inflation in both 2024 and 2025. However, as the government began to remove these policies, inflation had moved back to a more normalised level. In 2026, inflation picked up more strongly moving to 3.55%, 4.76% and 3.48% in the first 3 months as a result of even more removals of subsidies and price controls and to some extent, due to seasonal holiday demand and heightened depreciation (Statistics Indonesia). Core inflation in Indonesia remained stable at around 2-2.5% (Bank Indonesia) throughout the past year in spite of changes in headline inflation reinforcing the idea that movements in headline inflation were more policy driven.

Prior to the late end of 2025 with inflation being secure and at the lower end of the target band in early 2025, Bank Indonesia had been cutting rates. However, since the last cut in September 2025 Bank Indonesia has kept interest rates fixed at 4.75% (Bank Indonesia). In addition to inflation being higher thus reducing the room for monetary loosening, this is to maintain the stability of the Rupiah in a time of global economic uncertainty and increased interest rates worldwide. The Rupiah has depreciated from 15 500 IDR/\$ to almost 17000 IDR/\$ between mid-2025 and February 2026 marking reflecting pressure on the currency (Bank Indonesia).

Looking ahead, IMF 2026 forecasts suggest that inflation would be positioned around 2.9% in 2026 but early year data (which the IMF would not have had at the time of forecasting) indicates inflation could be higher and even exceed the target range.

## Fiscal Policy and Public Finances

Under the administration of president Prabowo Subianto, Indonesia has adopted a policy centered around prioritising economic growth above taxation but aiming to increase taxes in the medium run. More specifically, the finance minister has made assurances to the public that the government will not raise taxes until GDP hits 6% with the GDP sitting around 5-5.3% post-pandemic (Bloomberg).

The strategy is to strengthen the existing tax base through pushing growth and improving tax revenue later on. This is critical as Indonesia has one of the lowest tax-to-GDP ratios in the world due to issues in collection. However, the government is adamant on improvements and under the 2025-2029 Mid-term development plan, they are targeting a range of 11.52% to 15.0% (Ministry of National Development Planning Indonesia). The 2025 goal was a ratio 10.3% (Ministry of Finance Indonesia) with the country pursuing fiscal consolidation and economic recovery projects. Although data from q3 of 2025 suggests a ratio of roughly 9.82% (Antara), the finance Minister has emphasized the government's continued dedication towards increasing fiscal space for the purpose of improved public welfare. In spite of no major tax increases in 2026, tax revenue in 2026 stands at IDR 394.8 trillion IDR 20.7% higher than the same period last year. The largest contribution is from Value added tax and Sales Tax on Luxury goods totaling 155.6, a staggering 57.7% increase year on year due to consumption increases. Income tax is also up by 15.8% reaching 61.3 trillion (MUC consulting). In addition to increased economic activity, this reflects improved tax collection largely due to reforms targeting compliance. However, Indonesia still has a long way to go with regards to compliance with constraints like the informal economy remaining prevalent.

On the spending side of things, Indonesia's government spending increased slightly from 3350 trillion IDR to 3451 trillion IDR though note that the government had permission to spend 3621.3 trillion IDR (Ministry of Finance Indonesia). Indonesia's fiscal framework is marked by decentralisation as 25% of the budget is given to regional governments leaving 2663 trillion for the central government to spend. The largest expenses within central government spending are general public services at around Rp 730 trillion, economic affairs at Rp 707 trillion, education at Rp 310 trillion, social protection at Rp 273 trillion and defence at Rp 245 trillion (Statistics Indonesia). Administrative functions and economic development are evidently the focus of the government but spending on social sectors like education, health and social protection are still noteworthy. One major factor as to why the Economic affair section is so high is spending being put towards the construction of a new capital city Indonesia.

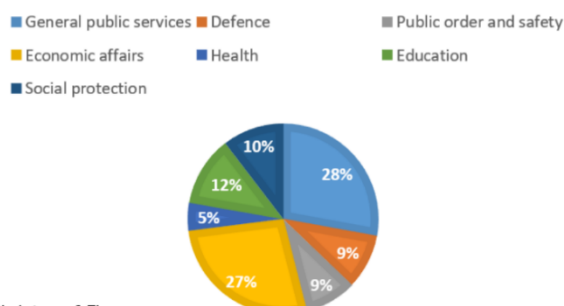


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Though the budget composition between 2024 and 2025 are broadly similar, one noticeable change is the reprioritisation of funds towards social and food programs such as large scale free-meal programs.

#### CENTRAL GOVERNMENT SPENDING COMPOSITION 2025



BPS, Ministry of Finance

Indonesia's budget deficit in 2025 had widened slightly to 2.3% of GDP up from 2% in 2024 implying controlled fiscal expansion (Ministry of Finance Indonesia). It reflects the government's dedication towards social programs whilst trying to stay under their 3% fiscal ceiling allowing them to maintain fiscal flexibility. 2025's budget deficit pushes the debt from 38-39% of GDP to 40% of GDP meaning that it remains relatively low below the legal ceiling of 60% of GDP (IMF).

### External Sector and Geopolitical Exposure

Indonesia's economy can be described as moderately open with Trade as a percentage of GDP sitting at 42.57% (World Bank), a significantly lower percentage than many of its fellow ASEAN countries. In 2025, Indonesia's exports amounted to approximately 282.9 billion with imports at approximately 241.9 billion giving a significant trade surplus of 41 billion approximately. Moreover, the non-oil and gas surplus comes out to approximately 60.75 billion as Indonesia has a large deficit in this particular industry (Trading Economics). Relative to 2024, exports grew by 6.1% whilst imports only grew by 2.8% widening the surplus (Statistic Indonesia).

According data from 2024, Indonesia's biggest exports are Coal and similar fuels (\$34.4B), Palm Oil (\$21.2B), Nickel and Ferroalloys (\$13.8B), Petroleum Gas (\$8.56B), and Copper Ore (\$8.39B) (OEC). This showcases how commodity driven the country's exports are.

On the other hand, Indonesia's biggest imports are Refined Petroleum (\$21.3B), Crude Petroleum (\$9.95B), Telephones (\$6.7B), Gold (\$4.36B), and Petroleum Gas (\$3.71B)(OEC). China is Indonesia's biggest importer, being accountable for approximately 23.8% of Indonesia's exports followed by the U.S. at 11.0% and India at 6.5%.and Japan at 6.3%. China is also the biggest exporter to Indonesia, accounting for approximately 36.2% of Indonesia's imports followed by Singapore at 7.9%, Japan at 6% and the US at 5.3% (OEC).

Under President Prabowo, Indonesia's focus has been on resource nationalism as briefly mentioned earlier. Restrictions on export commodities such as nickel and bauxite have been key to force investment in domestic industries and increase value added exports. Moreover, local content requirements, non-tariff barriers and other regulations and incentives are designed to support key industries. As Prabowo intended, these policies have played a key role in development with manufacturing growing by approximately 5% in early 2025 (Asian Development Bank) however critics point out the potential for inefficiencies and exposure to WTO and increased reliance on foreign countries such as China.

As shown earlier, China is Indonesia's biggest trading pattern with Indonesia generally exporting commodities to China whilst importing manufactured/intermediary goods. In addition to strong trade relations, China also invests heavily in key growth sectors such as nickel processing and smelting as well as EV batteries. Additionally, China has engaged in heavy investment in infrastructure and tech focused areas of the Indonesian economy as part of their Belt and Road Initiative. While the capital and technology provided by China is crucial to Indonesia's downstream strategy, Chinese firms controlling the technology and the supply chains mean less value added. Moreover, there is a tension with Prabowo's economic nationalist intentions as creating national strength in downstream industries with China's help forces Indonesia to also build foreign dependence.

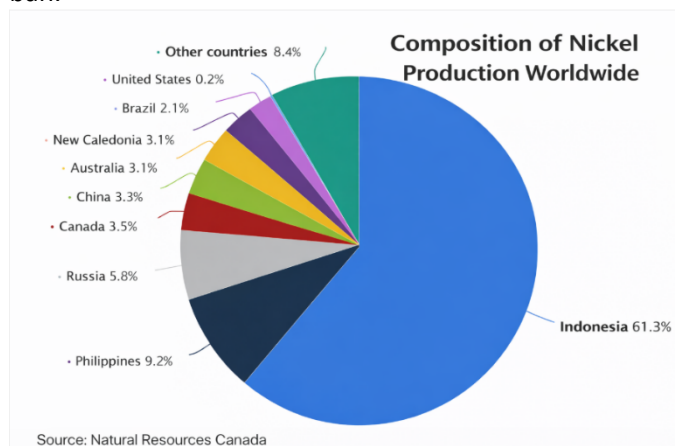
Indonesia's most recent developments with regards to trade include both risks and opportunities. New Agreements with the US and the EU focused on critical minerals and energy co-operation offer an opportunity to reduce reliance on China.



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The country's increased dominance in nickel production resulting from a successful downstream mining policy has contributed to a global oversupply of nickel. This indicates growth to a point where they can influence market outcomes and become partial price makers. However, this also reflects how heavily concentrated the export model is on commodities making it quite fragile. Another risk is that tensions with the WTO continue for Indonesia due to measures such as their nickel exports ban.



## Key risks and Upcoming Events

- Expansion of mineral export restrictions: After the nickel ban policymakers are considering extending restrictions to other commodities which could escalate tensions with the WTO.
- Nusantara capital project: The new capital city project faces significant financing challenges and depends on securing foreign and private investment.
- Digital Rupiah: Bank Indonesia is developing a digital currency initially for interbank use with pilot programs underway to assess financial system implications.

## South Africa

### Economic and Political Context

South Africa is a diversified emerging market economy, with key sectors including mining, manufacturing, financial services, and agriculture.

The country is one of Africa's largest exporters, with platinum group metals, gold, and coal accounting for a significant share of export revenues (World Bank, 2024).

However, growth remains constrained by structural challenges, including persistent electricity shortages, high unemployment (32.1% in 2023), and infrastructure bottlenecks (World Bank, 2024).

Economic growth has been weak, with GDP expanding by 0.6% in 2023 and projected to remain below 1.5% in the medium term due to low investment and supply-side constraints (IMF, 2024). While the economy is relatively diversified compared to peers, it remains sensitive to commodity price cycles and external demand.

South Africa is a constitutional democracy historically dominated by the African National Congress (ANC), though its electoral support has declined below 50% in recent polls, increasing the likelihood of coalition governments and political uncertainty (Reuters, 2024). Governance challenges, including corruption and inefficiencies in state-owned enterprises, have weakened policy implementation, although institutions such as the judiciary and the South African Reserve Bank remain relatively strong (IMF, 2024).

### Inflation and Monetary Policy

Inflation in South Africa is driven primarily by food prices, energy costs, and exchange rate movements. As a net oil importer, the country is highly exposed to global energy price fluctuations. Headline inflation averaged 6.0% in 2023, slightly above the central bank's target midpoint (IMF, 2024).

The South African Reserve Bank (SARB) operates an inflation-targeting regime with a 3–6% target band and has maintained strong credibility and independence. In response to elevated inflation, the SARB raised its policy rate to 8.25% by 2023, reflecting a tightening cycle aimed at anchoring expectations (SARB, 2024).

Although inflation has begun to moderate, it remains vulnerable to external shocks, particularly exchange rate depreciation and commodity price volatility. The central bank has therefore maintained a cautious stance, balancing inflation control with weak domestic growth.



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## Fiscal Policy and Public Finances

South Africa's fiscal position is characterized by elevated public debt and limited fiscal space. Government debt reached approximately 74% of GDP in 2023, up from around 56% in 2019, driven by persistent deficits and support for state-owned enterprises such as Eskom (IMF, 2024).

The fiscal deficit stood at roughly 4.9% of GDP, reflecting ongoing expenditure pressures, including a large public wage bill and social spending commitments (National Treasury, 2024). While the government has pursued moderate fiscal consolidation through improved revenue collection and spending controls, progress remains gradual.

Debt sustainability remains a concern, particularly given rising interest costs, which now account for over 20% of government revenue (National Treasury, 2024). Although most debt is denominated in local currency, reducing exchange rate risk, borrowing costs remain sensitive to global financial conditions and domestic risk perceptions.

## External Sector and Geopolitical Exposure

South Africa's external sector is heavily dependent on commodity exports, with China, the European Union, and the United States as key trading partners. Minerals and metals account for over 50% of total exports, increasing vulnerability to global commodity price cycles (World Bank, 2024).

The country maintains relatively open capital markets, attracting foreign investment but also exposing it to capital flow volatility. Periods of global monetary tightening have led to currency depreciation, with the South African rand among the more volatile emerging market currencies (IMF, 2024).

Geopolitically, South Africa follows a non-aligned approach, participating in BRICS while maintaining trade relations with Western economies. This positioning provides flexibility but may create exposure to geopolitical tensions and shifting global trade dynamics.

Additionally, the economy remains sensitive to global energy prices and supply chain disruptions due to its reliance on imported refined fuels and capital goods.

## Key risks and Upcoming Events

- Upcoming elections and potential coalition government dynamics
- Ongoing electricity crisis and Eskom reform progress
- Monetary policy changes amid global interest rate uncertainty
- Fiscal consolidation challenges and rising debt servicing costs
- Commodity price volatility affecting export revenues
- Exchange rate instability and capital outflow risks

## Turkey

### Economic and Political Context

Turkey is the 17th largest economy globally, with a nominal GDP of \$1.57 trillion as of 2025, and is currently undergoing a challenging stabilization phase, characterized by moderate growth and significant disinflation. During the last decade its real GDP has been growing in a strong but volatile manner, averaging 5.4%. After an intentional slight slowdown in 2025 (3.6%), the forecasts now project a 3.9% for 2026 aiming for a stabilization in the following years. (Newsroom, 2026)

The main drivers of output, services (58%), manufacturing and industry (25.5%) and construction (5.8%), all faced a growth during the last year, while the agricultural sector contracted by 8.8%, reaching the same share of construction. Still, the economy faces structural constraints that are high energy imports, especially considering the current situation, and the skills gap in high-tech manufacturing in the labor market. (isbank, 2025)

The government system is a presidential republic and the president is Recep Tayyip Erdoğan. While the national government is actually controlled by the Justice and Development Party (AKP or AK Party), the Republican People's Party (CHP) obtained a victory in the March 2024 local elections taking control of most major cities, including Istanbul and Ankara.



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After winning the elections in May 2023, Erdoğan's government started a process of normalizing macroeconomic policies to pull Türkiye's economy back onto a sustainable path. This led to the independence of the Central Bank (CBRT), which brought restrictive policies that contributed to the slowdown in 2024 but anchors inflation expectations and makes Turkey more attractive for global investors.

### Inflation and Monetary Policy

2025 was a year of successful transition for Turkey, with inflation that fell to 31% in December 2025, with respect to the 44% registered in the previous year. Still, it was 6.9 percentage points above the interim target of 24%. (TCMB, 2026)

While inflation is slowly falling, it remains high, particularly for services: services inflation, especially rents, has exceeded that of goods, raising the share of services in headline CPI inflation from 30% to 55% since 2021 (TurkStat, 2026). This was mainly driven by TurkStat's updates of the CPI basket in order to align with Eurostat criteria and by the stickiness of prices in this sector. Due to the geopolitical tensions and the trend of global protectionism, the rise in commodity prices caused imports to be more expensive, and, since Turkey is a major importer of energy and raw materials, pushed costs up. In addition, extreme weather events, drought and frost, have an impact on food prices inflation both through supply and expectation channels. Finally, the last two factors are the output gap, the economy hasn't cooled down as expected, and the prices regulated by the government, which were higher than CBRT's predictions. (isbank, 2025)

The Central Bank recently adjusted its forecasts for 2026 and 2027, with inflation to be between 21% and 15% for the end of this year and between 12% and 6% for the end of the next, targeting respectively 16% and 8%. Next, the hope is for a stabilization at 8% also for 2028 to reach the interim target of 5% in the medium term. To accomplish this, the CBRT is maintaining a restrictive monetary stance, holding the policy rate at 37%, with the overnight lending rate and the overnight borrowing rate at 40% and 35.5%, respectively. Even if the rate was slightly decreased from the 45% in late 2025, policymakers decided to hold it in response to regional conflicts and rising energy costs.

This strategy ensures a positive real interest rate, which is central to anchoring inflation expectations and maintaining the stability of the Lira. (BIS, 2026)

### Fiscal Policy and Public Finances

Right now, Turkey is maintaining a restrictive fiscal stance to complement the central bank's tight monetary policy fighting inflation. Central government budget data for 2025 indicate that the budget deficit narrowed to 2.9% of GDP in 2025, outperforming the official target of 3.6%. This performance was largely driven by revenues increasing more strongly than anticipated in 2025. While a primary deficit had been projected for the year, the budget instead recorded a primary surplus. According to forecasts, the central government budget deficit-to-GDP ratio is expected to stand at 3.5% in 2026. (Garanti BBVA Securities, 2026) Turkey features a solid debt profile, which gives it a structural advantage among emerging markets. The public debt-to-GDP ratio stood at 23.8% in December 2025, significantly lower than the global average of approximately 94.7%. For 2026, it is expected to increase to around 25%, because of the government's interest expenditures, which rose by 61.7% compared to the previous year. However, this should not compromise overall sustainability, thanks to the strategy adopted by the government, which has increased the share of TRY-denominated debt to a projected 91% in 2026, reducing vulnerability to exchange rate shocks. Consequently, we have that the main key driver of deficit are interest expenditures, which will be around TL 2.7 trillion in 2026 and account for the 14-16% of total budget expenditures. Another major expenditure rigidity is the earthquake reconstruction, with a budget of TL 653 billion for housing and infrastructure in 2026. To be considered is also the personnel expenditure and current transfers, which amounts to TL 1,015.9 billion out of TL 1,184.8 billion of total no-interest expenditure just for January 2026. Currently, Turkey's strategy to manage debt is the lira-ization, which consist in holding an high level of Domestic borrowing, planned at TL 5.3 trillion, and reducing the share of external borrowing, planned around TL 947.8 Billion. (Republic of Turkey Ministry of Treasury and Finance, 2026)



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## External Sector and Geopolitical Exposure

Turkey achieved the largest export performance in its history in 2025, with total goods, services exports estimated at \$396 billion, with goods exports that rose 4.5% from the previous year to reach \$273.4 billion, the automotive sector continues to lead exports (\$41.5 billion), followed by chemicals (\$31.9 billion) and electrical-electronics (\$17.7 billion). Another growth manifested in defense exports, with shipments that reached \$9.87 billion in 2025. The target for 2026 is \$282 billion in goods exports and \$128 billion in services. (Daily Sabah, 2026) Moreover, Turkey became the European Union's fifth-largest trading partner, with bilateral trade reaching \$232.7 billion and its main partners are Germany, United States, Iraq and the United Kingdom. Its position is both an advantage and a risk: thanks to the Zangezur and Middle Corridors to bypass traditional Russian routes, Turkey is indispensable to storage, manage and transport gas to Europe, giving it leverage in negotiations with the EU, but for the same reasons it is highly vulnerable to external shocks in the Middle East. As a net energy importer, the country is highly sensitive to the increase in oil prices, which significantly weigh on the account deficit. Furthermore, the risk of a prolonged conflict in that regions could lead to big losses in tourism revenues. According to the CBRT the foreign direct investments (FDI) increased by 12.2% in 2025, despite the global fell of 2% in FDI to developing nations, with a strategic focus on technology and manufacturing thanks to the HIT-30, an incentive program for investors in semiconductors, EVs, and green energy. In January 2026, the country saw record portfolio inflows of \$8.4 billion, due to attractive real interest rates, but capital flows still remain sensitive to regional geopolitical tensions. (Daily Sabah, 2026)

## Key risks and Upcoming Events

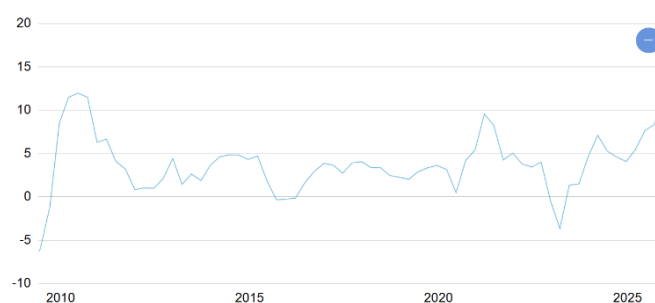
- Policy Continuity and Political Stability: The primary internal risk is a reduction of the CBRT independence. Investors will closely watch for any political pressure on the CBRT to cut interest rates prematurely or any fiscal deviation ahead of future electoral cycles that could compromise the 3.5% deficit target.

- Monetary & Inflation Anchoring: Success depends on keeping the real interest rate positive. If this margin is narrowed, through rising inflation or aggressive rate cuts, it could destabilize the Lira.
- External Energy Shocks: Turkey's greatest vulnerability is its dependence on energy import. Continued regional conflict in the Middle East could push oil prices up, which would widen the current account deficit.
- Geopolitical and Corridor Risks: While the Zangezur and Middle Corridors provide strategic leverage and trade diversification, they are located in volatile regions. Any disruption to these routes or a significant drop in tourism revenues due to regional wars would directly impact the country's external financing needs.

## Taiwan

### Economic and Political Context

Taiwan delivered its strongest GDP performance in 15 years in 2025, growing 8.68% for the full year, beating an already-upgraded Q3 forecast of 7.37%. Q4 2025 alone surged 12.65% year-on-year, the highest quarterly reading since Q3 1987, driven overwhelmingly by an AI-and-semiconductor export boom in which real exports of goods and services expanded 38.81% (DGBAS, February 2026; Taipei Times, January 2026).



YoY GDP

GDP per capita reached USD 39,477, surpassing both Japan (USD 34,713) and South Korea (USD 35,962) for the first time in over two decades (Focus Taiwan/CNA, January 2026).



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On the back of this performance and a landmark US-Taiwan trade deal, DGBAS revised its 2026 GDP growth forecast to 7.71% in February 2026, with GDP forecast to surpass USD 1 trillion and GDP per capita projected at USD 44,181 (DGBAS, February 2026; Focus Taiwan/CNA, February 2026). ING Think (January 2026) independently forecast 6.8% for 2026, while the IMF's April 2026 World Economic Outlook projects 5.2%, reflecting more cautious assumptions around Middle East risks and global trade slowdown (IMF, April 2026; Worldometer, April 2026).

The economy is structurally concentrated in technology manufacturing. Electronics, information and communication products account for over 70% of goods exports. TSMC alone represents more than 44% of the Taix and approximately 10% of total electricity consumption. Services represent roughly 60% of GDP, manufacturing and industry approximately 35%, and agriculture around 2%. Private investment is expected to grow 4.24% in 2026, with continued semiconductor fab expansion as the primary driver (DGBAS, February 2026). Taiwan's long-run average growth of approximately 3.9% in the 2000s and 3.6% in the 2010s underscores that 2025's outperformance reflects a technology-cycle-driven surge rather than structural acceleration (ING Think, January 2026).

On the political side, President Lai Ching-te (Democratic Progressive Party, DPP) took office in May 2024. The January 2024 legislative elections produced a divided legislature: KMT holds 52 seats, DPP 51, and TPP 8, with 57 required for a majority (Taipei Times, January 2024; CSIS, January 2024). The KMT-TPP opposition coalition exercised this majority in January 2025 to pass unprecedented NT\$207.5 billion (approx. USD 6.3 billion) in budget cuts -6.63% of total central government expenditures, far exceeding the historical norm of below 2% annually. Cuts included targeted reductions to the Ministry of National Defence, the Ministry of Digital Affairs and the Ministry of Foreign Affairs, alongside reductions in energy subsidies to Taiwan Power Company (Liao, Taiwan Insight, March 2025; Lai & Chiang, Taiwan Insight, March 2025).

A key political event on the 2026 calendar is the nine-in-one local elections, confirmed by the Central Election Commission for November 28, 2026.

These elections will choose mayors and city councillors across all six special municipalities (Taipei, New Taipei, Taoyuan, Taichung, Tainan, Kaohsiung) and officials in all 16 counties and county-level cities (Focus Taiwan/CNA, October 2025; Taipei Times, November 2025). KMT and TPP formally agreed on March 14, 2026 to coordinate candidate nominations, with the two parties nominating the strongest candidates based on opinion polls across key races including New Taipei, Chiayi City and Yilan (Focus Taiwan/CNA, March 2026; Wikipedia, 2026 Taiwanese Local Elections). Results will shape the balance of power ahead of the 2028 presidential cycle and directly affect Lai's ability to pass defence and digital budgets.

Governance indicators are a structural positive. Taiwan ranks 6th in the IMD World Competitiveness Yearbook 2025 and 4th on the Heritage Foundation's Index of Economic Freedom. S&P Global affirmed Taiwan's long-term issuer rating at AA+ with a stable outlook in April 2025; Fitch Ratings affirmed AA with a stable outlook in August 2025; Moody's affirmed Aa3 in April 2024. All three agencies cited Taiwan's low debt ratio, fiscal discipline and economic resilience (Ministry of Finance, R.O.C., 2025).

## Inflation and Monetary Policy

Taiwan's inflation remains among the most contained in the region. Full-year 2025 CPI came in at approximately 1.67% and core CPI at 1.65%, both below the CBC's 2% alert threshold for the eighth consecutive month by year-end. For 2026, DGBAS projects headline CPI at 1.68% which is still firmly anchored below the alert level (DGBAS, February 2026). Monthly readings show CPI fell to a five-year low of 0.69% in January 2026 before rebounding to 1.75% in February 2026. The February rise was attributed by DGBAS to seasonal factors in the service sector during Lunar New Year holidays, alongside persistent dining-out cost increases; core CPI rose to 2.6% year-on-year in February (Focus Taiwan/CNA, March 2026).

Inflationary risks in 2026 are predominantly supply-side and energy-driven. The ongoing Middle East conflict has pushed global crude oil above USD 100 per barrel at points, and the CBC Governor stated in March 2026 that CPI could reach 1.9% for the full year if oil averages USD 100 per barrel, against a base case of 1.8% assuming USD 85 per barrel.



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The government has deployed price stabilisation mechanisms including fuel subsidies and a 50% commodity tax cut on diesel and gasoline imports to contain pass-through (Focus Taiwan/CNA, March 2026; Taipei Times, March 2026). Structural disinflationary forces include NTD appreciation and moderation in global goods prices.

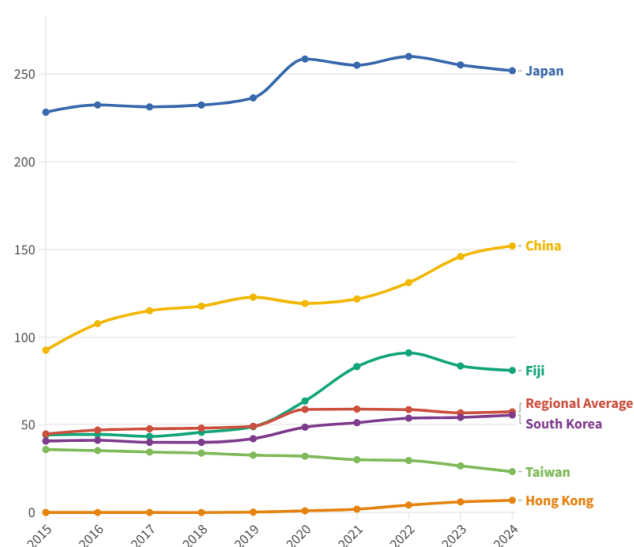
The Central Bank of the Republic of China (CBC) held its discount rate unchanged at 2.00% at its December 2025 meeting - a seventh consecutive hold since a final +12.5bps hike in March 2024. The decision was unanimous. The CBC noted that the domestic inflation outlook was projected to be mild, with the rate staying below 2%, and that a rate hold would best support sound economic and financial development amid global uncertainties (CBC, December 2025). At its March 19, 2026 meeting, the CBC held rates for an eighth consecutive quarter, raising its 2026 GDP forecast sharply from 3.67% to 7.28% and lifting the CPI forecast from 1.63% to 1.80%, citing strong exports and private investment along with government energy-price stabilisation measures (Focus Taiwan/CNA, March 19, 2026c).

Capital Economics (December 2025) forecasts rates on hold throughout 2026–27 given strong growth and contained inflation. The primary risk to the current stance is a potential Fed chair appointment under Trump willing to weaken the USD, which could narrow the US-Taiwan rate differential and generate NTD appreciation pressure, squeezing traditional industry exporters as occurred in May 2025 (Focus Taiwan/CNA, December 2025).

## Fiscal Policy and Public Finances

Taiwan's public finances are a structural strength. Central government gross debt-to-GDP stands at approximately 24% -below the statutory ceiling of 40.6% of average GDP stipulated in the Public Debt Act, and far below the emerging market average (Ministry of Finance, R.O.C., 2025; Allianz Trade, January 2025).

The fiscal balance has been in sustained surplus: the 2024 overall budget posted a surplus of NT\$99.1 billion, followed by a 2025 general budget surplus of NT\$239.8 billion. After accounting for special budget deficits, the 2025 overall surplus stood at NT\$40.2 billion.



Debt-to-GDP

S&P, Fitch and Moody's each affirmed Taiwan's AA-equivalent sovereign ratings in 2024-25, citing fiscal discipline and the low debt trajectory (Ministry of Finance, R.O.C., 2025).

The fiscal stance is neutral to mildly contractionary in 2025-26. The opposition-imposed NT\$207.5 billion budget cut of January 2025 reduced government expenditure by 6.63% relative to the executive's proposal. Cuts targeted the Ministry of National Defence (freezing NT\$89.9 billion and cutting NT\$8.4 billion from the proposed NT\$647 billion defence budget, affecting 20.7% of the proposed defence allocation) alongside digital affairs, foreign affairs, and Taiwan Power Company energy subsidies (Liao, Taiwan Insight, March 2025; Lai & Chiang, Taiwan Insight, March 2025). This creates a structural contradiction: Lai's administration seeks expanded defence investment as cross-strait tensions escalate, while the KMT-TPP majority constrains the fiscal envelope. Rising emergency energy procurement costs from the Iran war represent an additional unbudgeted fiscal pressure in 2026 not reflected in the approved budget.

Debt composition is almost entirely domestic and NTD-denominated, minimising foreign currency and rollover risk.



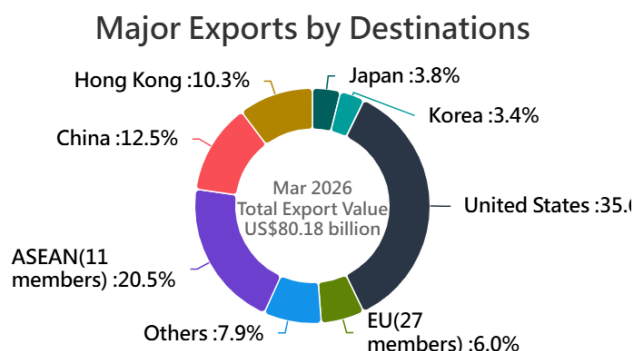
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Taiwan's current account surplus is estimated at approximately 15% of GDP, underpinned by persistent technology trade surpluses and underpinning the island's strong external balance sheet (Allianz Trade, January 2025).

## External Sector and Geopolitical Exposure

Taiwan is one of the world's most trade-exposed economies. Exports surged 34.9% in 2025 to a record USD 640.75 billion, with the US overtaking China as the largest market for the first time in 26 years, accounting for 30.9% of total exports (US\$198.27 billion) (Focus Taiwan/CNA, January 9, 2026a).



DGBAS projects exports to grow a further 12.68% in 2026 (DGBAS, February 2026). A landmark US–Taiwan trade deal signed on January 15, 2026 reduced reciprocal tariffs to 15%, exempted from stacking with MFN tariffs, and granted preferential Section 232 treatment for semiconductors within quota limits (Reuters, January 2026). TSMC has committed USD 165 billion across up to 12 US fabs, though analysts warn this risks eroding the ‘Silicon Shield’ deterrence logic (CFR, February 2026). Approved inbound FDI reached USD 11.39 billion in 2025, up 44.98% year-on-year, while outbound FDI to China fell 59% to USD 1.50 billion, reflecting a structural de-risking toward India, Vietnam and the US (Focus Taiwan/CNA, January 2026; Allianz Trade, January 2025).

Taiwan imports 95-98% of its primary energy. Since the shutdown of its last nuclear reactor in May 2025, electricity has relied on LNG (~42%), coal (~39%), and renewables (~11.6%) (NucNet, May 2025). The ongoing Iran war has severely disrupted Strait of Hormuz traffic, through which 78% of Middle Eastern crude oil exports to East Asia transited in 2025;

Iranian strikes have already hit Qatar's Ras Laffan LNG complex, which supplies around one-third of Taiwan's LNG (Atlantic Council, March 2026a; Atlantic Council, March 2026b). As of March 2026, Taiwan has secured 20 of 22 near-term LNG shipments and holds approximately 150 days of oil reserves (Focus Taiwan/CNA, March 2026). The legislature enabled nuclear licence renewals in May 2025; restart feasibility for Kuosheng and Maanshan was approved in November 2025, with reactors potentially back online around 2028 (NucNet, December 2025; The Diplomat, April 2026). On the security front, wargaming exercises show a PLA ‘energy quarantine’ could halve Taiwan's electricity generation within weeks (FDD, November 2025). Beijing exploited the energy crisis in March 2026 by offering Taiwan ‘energy security under reunification,’ dismissed by the Lai administration (The Diplomat, April 2026). The US-Taiwan relationship deepens institutionally but on transactional terms, with US Commerce Secretary Lutnick tying US protection explicitly to Taiwan meeting investment commitments (CFR, February 2026; CSRI, April 2026).

## Key risks and Upcoming Events

- November 28, 2026 local elections: Nine-in-one elections across six special municipalities and 16 counties.
- Middle East energy crisis: Strait of Hormuz disruptions risk Taiwan's summer 2026 electricity peak demand.
- Section 232 semiconductor tariff risk: The January 2026 deal provides quota-based zero-tariff treatment, but the Trump administration has signalled potential tariffs exceeding 100% on chips outside quota.
- Post-AI-boom demand normalisation: 2025 orders included significant pre-tariff inventory stocking by global firms. If hyperscaler capex normalises, export growth could undershoot even the upgraded 7.71% forecast
- NTD currency pressure: A dovish Trump-appointed Fed chair could narrow the US-Taiwan rate differential, generating NTD appreciation pressure and squeezing traditional exporters.
- CBC rate decisions (March, June 2026): The CBC explicitly flagged oil price risk and NTD dynamics as conditions it will monitor.



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## Japan

### Economic and Political Context

On the 21st of October 2025, Japan elected its first female prime minister, Sanae Takaichi, who went on to be officially designated on February 18th of 2026. She is known for leading from the right of the Liberal Democratic Party, being tough on immigration, conservative views and for pushing nationalist policies. "Unless Japan can defend itself, its fate will always be at the mercy of shallow US opinion," Takaichi has stated (BBC).

Historically, the Liberal Democratic Party has dominated Japanese politics since its founding in 1955. In early February, after Takaichi moved to dissolve the lower house, the election delivered a landslide LDP victory (The Interpreter), strengthening the government's mandate while also raising market attention to the credibility and funding of any pro-growth but potentially deficit-expanding agenda.

The IMF published a report on Japan that indicated Japan's significant resilience despite global shock, including robust domestic demand and low unemployment (IMF). The BoJ's assessment in March 2026 was that the economy "has recovered moderately," with exports and industrial production "more or less flat," corporate profits are high, and business fixed investments are steadily increasing (BoJ). The IMF has, however, flagged the steadily rising old-age dependency ratio in its baseline projections, reinforcing the case that continuous growth will be limited unless labour participation reforms occur (IMF).

### Inflation and Monetary Policy

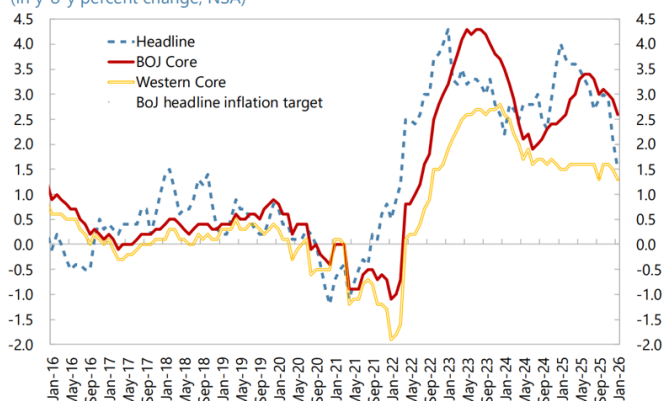
Japan's inflation regime changed meaningfully from 2024 onward, as yield curve control policies and negative interest rates came to an end. This high global and domestic inflation rates that resulted above BoJ's target of 2%, allowed for these changes to be made. However, since the gradual normalisation of monetary policy, the policy rate has increased to the current amount of 0.75% (IMF). Importantly for forward guidance, the BoJ stated that, with real interest rates still "significantly low," if the outlook baseline is realised, it

will "continue to raise the policy interest rate and adjust the degree of monetary accommodation" (BoJ).

Japanese inflation dynamics in early 2026 look less like pure "imported inflation", but instead look to be due to wage pass-through is increasingly visible in addition to food/energy shocks, all while government price-relief measures can temporarily suppress that measured inflation. In March 2026, the BoJ explicitly linked above 2% CPI readings partly to food, highlighting rice prices. They noted inflation had "recently fallen to around 2 per cent" partly due to government measures aimed at reducing the household burden of higher energy prices. The IMF similarly emphasises that nominal wages are rising at a "historic pace", but households continue to feel squeezed when inflation erodes purchasing power. The IMF's Executive Board summary projects inflation rising again in 2026 before converging to the target in 2027. (IMF)

#### Inflation

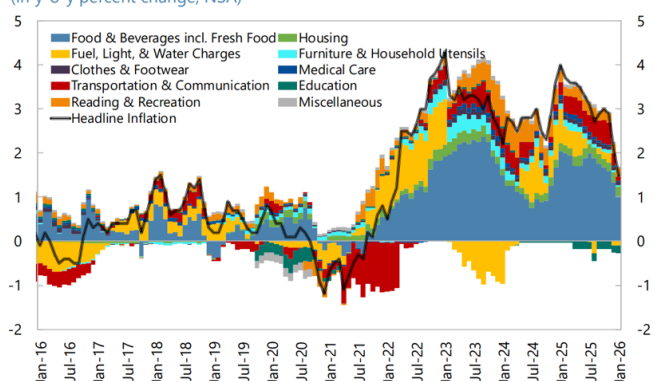
(In y-o-y percent change, NSA)



Sources: Japan Ministry of Internal Affairs and Communications; and Haver Analytics.

#### Contributions to Headline Inflation

(In y-o-y percent change, NSA)



Sources: Ministry of Internal Affairs & Communications; Haver Analytics; and IMF staff calculations.

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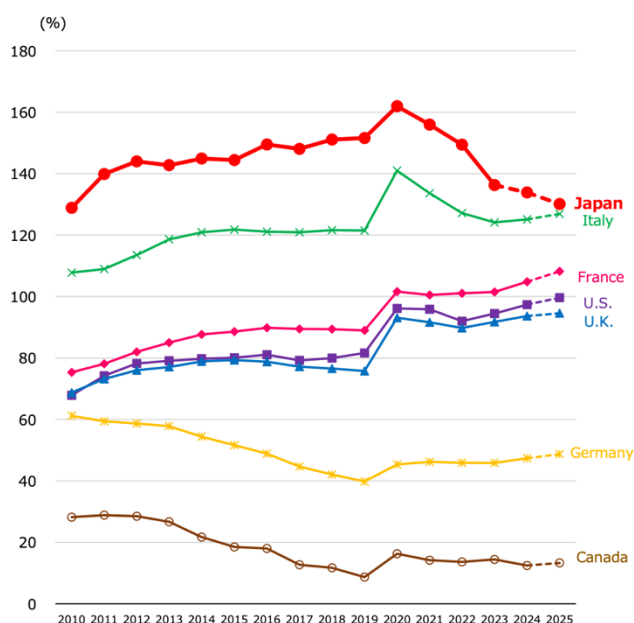


## Fiscal Policy and Public Finances

Japan is moving away from very low (even negative) interest rates towards something more standard, and as a result, the cost of debt is going to go up. Between 2025 and 2026, the amount the country has to pay to service its debts is increasing by ¥3.06 trillion, reaching ¥31.28 trillion. The government is hoping to get around ¥83.74 trillion in taxes, and intends to borrow ¥29.58 trillion by selling government bonds (according to Japan's Ministry of Finance).

How the government plans to spend its money in 2026 shows both long-term, essential needs and where it's focusing its security. The draft budget for 2026 specifically shows around ¥8.8 trillion being used to strengthen the military, multiple-year plans to help industry (including support for semiconductors), and a series of plans to improve the country's ability to withstand disasters and shortages (Japan Ministry of Finance).

The IMF believes will come down a little in the next few years (shown in graph below). However, the IMF warns that increasing interest rates and the costs of looking after an ageing population could make the deficit increase in the further future. Hence the necessity for a reliable long term plan to retain confidence from population and global investors.



The BoJ graph demonstrates the Government Net Debt as a percentage of the country's GDP.

## External Sector and Geopolitical Exposure

The IMF predicts that Japan will have a bigger surplus in its current account, around 4.8% of its GDP by 2025, up from 4.5% in 2024. This signifies possible greater stabilisation of the Yen, due to its greater global demand.

Japan's trade numbers by the customs department demonstrates two big exposure: the country relies heavily on supply chains from Asia, especially China, and is especially vulnerable to trade restrictions from the US, particularly in the auto and industry sectors. These large dependences demonstrate undiversified trade which does not result in problems currently, but would create weaknesses if the counterparty countries use this dependence to negotiate future affairs.

In February 2026, Japan's exports were worth approximately ¥9.56 trillion, which is a 4% increase from the same time last year, while imports were around ¥9.52 trillion, a 10.3% jump (Japan Customs). This left Japan with a small surplus of approximately ¥44.3 billion. When looking at trade partners, exports to China dropped by 11% and to the US by 8%, but exports to Western Europe rose by 17%. Demonstrating a shift in trading partners due to how countries and companies are adjusting to uncertain risk, cost and strategy globally.

From a geopolitical risk standpoint, Japan is still very sensitive to disruptions in global energy supplies. The same trade data from February 2026 shows that Japan imported around ¥0.86 trillion worth of goods from the Middle East, which highlights the country's heavy dependence on imported oil and gas. This is a significant concern for Japan, given they were the fifth highest global consumer of oil in 2022, relying on imports to meet 97% of its demand" (U.S. Energy Information Agency). The upcoming year of 2026 is expected to bring a significant energy-security shock. Both the Bank of Japan and the International Monetary Fund have explicitly linked their outlook to the risk of conflict in the Middle East and the volatility of oil prices.



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## Key risks and Upcoming Events

- The BoJ monetary policy normalisation path: The current policy rate is already 0.75%, however, it is variable based on inflation rates that could increase due to the higher geopolitical tension that might largely decrease trade, decrease the Yen's stability and increase the cost of fuel.
- New government reforms: Under a conservative leader whose party controls more than 2/3rds of the lower house, decreasing the power of the opposition. This ultimately enables a higher chance of deficit spending due to decreased oversight.
- Increasing labour pool age: Important to pay attention to the risks an increasing labour pool will have on the future productivity of the nation.

## Special Feature: Middle East

### Introduction

This report analyzes macroeconomic conditions in the Middle East as of April 2026, covering Arabia (UAE, Saudi Arabia, Oman, Yemen, Qatar, Bahrain, Kuwait), the Levant (Israel, Palestine, Jordan, Lebanon, Syria), as well as Iraq, Egypt, and Iran. Turkey is excluded due to separate treatment.

The analysis is structured across four dimensions: economic and political context, inflation and monetary policy, fiscal dynamics, and the external sector. The central framework is that the region is undergoing a conflict-driven repricing, in which geopolitical developments dominate economic outcomes (World Bank, 2026).

### Economic and Political Context

The regional outlook has deteriorated sharply following the escalation of conflict involving the United States, Israel, and Iran.

Growth across the broader MENAAP region (excluding Iran) is projected to fall from 4.0% in 2025 to 1.8% in 2026 due to disruptions to energy infrastructure, trade routes, and investment flows (World Bank, 2026).

The Gulf economies entered 2026 with strong fiscal buffers and external surpluses, but the war has challenged the core assumption underlying their economic model: stability. Oxford Economics notes that GCC growth has been downgraded significantly due to weaker oil exports, reduced tourism, and softer domestic demand (Oxford Economics, 2026). The issue is not simply lower growth, but a shift in perceived risk.

This is most visible in the UAE. Its economic model relies heavily on attracting foreign capital and labor. Evidence of regulatory flexibility around expatriate tax residency and reported staff relocations indicates that authorities are actively managing retention risks (Financial Times, 2026). In hub economies, even temporary relocations can weaken the ecosystem that supports finance, real estate, and services.

Saudi Arabia faces a similar dynamic but at a different scale. Its continued investment push reflects both economic objectives and strategic signaling. BNP Paribas notes that diversification efforts are continuing despite fiscal pressures, highlighting the importance of maintaining long-term credibility (BNP Paribas Economic Research, 2026).

Egypt represents a different category of risk. While IMF-supported reforms have improved macroeconomic stability, the economy remains highly exposed to external shocks. Continued reliance on external financing and trade-related revenues increases vulnerability under current conditions (IMF, 2026).

Jordan faces similar pressures but retains stronger institutional stability. Iraq, meanwhile, remains vulnerable due to its dependence on oil revenues combined with weak governance structures.

Within the Levant, Israel retains institutional strength, though its economy is increasingly shaped by wartime conditions. The Bank of Israel's March 2026 forecast reflects continued growth potential but under significant uncertainty (Bank of Israel, 2026). Lebanon, Syria, and Yemen remain structurally fragile, though Syria has shown limited signs of recovery from a low base.



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Iran sits at the center of the regional system. Its economy is under pressure from sanctions, inflation, and conflict-related disruption, making it both a driver and a victim of the current crisis (World Bank, 2026).

## Inflation and Monetary Policy

Inflation across the region is driven primarily by external supply shocks. The IMF identifies energy, trade disruption, and financial conditions as the key transmission channels (IMF, 2026). Energy prices have risen due to disruptions in production and transport, particularly through the Strait of Hormuz. However, the broader inflationary impact comes from increased shipping costs, higher insurance premiums, and supply chain disruption. In the Gulf, inflation remains relatively contained at the headline level, but underlying costs are rising. Oxford Economics highlights weakening tourism and domestic demand alongside higher operating costs (Oxford Economics, 2026).

Labor dynamics are also important. Gulf economies rely heavily on expatriate workers. While there is no clear evidence of a permanent exodus, mobility and retention risks are increasing, affecting both labor supply and consumption (Financial Times, 2026). In Egypt and Jordan, inflation is more pronounced. Higher import costs feed directly into domestic prices, while monetary policy remains restrictive to maintain stability (IMF, 2026). Israel faces a more balanced inflation environment, with upward pressure from energy and fiscal expansion offset by weaker demand. Iran's inflation remains structurally high due to currency depreciation and limited access to foreign exchange (World Bank, 2026). In Lebanon, Yemen, and parts of Syria, inflation is driven primarily by structural and political factors rather than monetary policy.

## Fiscal Policy and Public Finances

Fiscal policy across the region is focused on absorbing shocks and maintaining stability. In the Gulf, higher energy prices provide revenue support, but this is offset by increased spending on defense, infrastructure protection, and economic support. Oxford Economics notes that growth and fiscal outcomes are being negatively affected by reduced exports and weaker domestic activity (Oxford Economics, 2026).

In Saudi Arabia, continued investment reflects both economic and strategic considerations. BNP Paribas highlights that diversification efforts are continuing despite fiscal pressures, suggesting that spending serves both developmental and signaling functions (BNP Paribas Economic Research, 2026). The UAE faces a related challenge, with fiscal performance tied to non-oil sectors such as real estate, tourism, and finance. Measures to support business continuity and retain expatriates reflect the importance of maintaining this ecosystem (Financial Times, 2026). Egypt's fiscal position remains constrained. IMF support provides stability, but high debt levels and external pressures limit flexibility. Continued adjustment depends on external financing and domestic tolerance (IMF, 2026). Jordan operates within a narrow fiscal space, while Iraq faces challenges due to reduced oil revenues and increased expenditure needs. Israel's fiscal position is being reshaped by wartime spending, though financing capacity remains relatively strong. Iran faces significant fiscal pressure due to reduced export revenues and increased military spending (World Bank, 2026). Lebanon, Yemen, and Syria have limited fiscal capacity, with outcomes dependent on external support.

## External Sector and Geopolitical Exposure

The external sector is the primary transmission channel of the conflict. The most critical constraint is not oil, but insurability. Marine insurers have increased war-risk premiums and withdrawn coverage in parts of the Gulf, significantly affecting shipping activity (Insurance Journal, 2026; S&P Global Commodity Insights, 2026). Traffic through the Strait of Hormuz has declined as a result of security concerns and maritime restrictions (USNI News, 2026). This creates a reliability constraint, where the movement of goods becomes uncertain regardless of price. For the Gulf, this directly challenges the hub model. These economies depend on predictable movement of goods, capital, and labor. When reliability declines, their competitive advantage weakens. The expatriate dimension reinforces this effect. While large-scale permanent departures are not confirmed, even temporary relocations affect labor supply, consumption, and investor perception (Financial Times, 2026). Egypt is particularly exposed through disruptions to trade routes and reduced Suez Canal revenues.



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IMF analysis highlights the importance of external financing and trade flows for economic stability (IMF, 2026). Iraq remains vulnerable due to reliance on oil exports, while Israel's external position is more resilient but still affected by reduced tourism and investment uncertainty. Iran faces the most direct constraints, with sanctions and conflict limiting both exports and imports (World Bank, 2026). Lebanon, Yemen, and Syria remain highly exposed due to weak financial systems and reliance on external support.

## Conclusion

The Middle East is undergoing a structural repricing driven by conflict (World Bank, 2026). The Gulf economies remain financially strong, but their vulnerability has shifted from commodity dependence to credibility. Their economic model depends on stability and predictability, both of which are now under pressure. Egypt represents a key systemic risk, with continued stability dependent on external support and the sustainability of domestic adjustment (IMF, 2026). Saudi Arabia's investment strategy reflects both economic and strategic objectives, with spending increasingly serving a signaling function (BNP Paribas Economic Research, 2026). The most critical constraint across the region is external. The conflict is impairing the insurability and reliability of trade routes, limiting the movement of goods, capital, and labor (Insurance Journal, 2026). The region is not experiencing a conventional downturn. It is being reshaped by a conflict that is redefining economic relationships and risk across all major sectors.

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