

# The upside and downside risks to our global outlook

Everything we think could go right or wrong for the global economy over the coming months



As the dust settles on the US election result, we think the focus is going to quickly recentre on the macro story

## The upside risks: Higher growth, higher rates

Expectations for US growth in 2025 are already pretty high following Donald Trump's victory in the presidential election. Extended and expanded tax cuts, combined with the certainty of a clean and clear election result, have bolstered our 2025 GDP numbers. Profit margins and corporate balance sheets look healthy, too.

But the outlook for 2026 is more uncertain and clouded by the threat of tariffs. If those tariffs are watered down – either because they're applied more narrowly across sectors, or because they're used as a bargaining chip to achieve other foreign policy objectives – then that would boost growth in the longer term.

US growth would benefit from the reduced hit to consumers. But softer tariff rises would be a much bigger boon for Europe. Investors ramped up European Central Bank rate cut bets after Trump's victory on the basis that the continent would be hit hard by American trade policy.

Europe also stands to benefit if China manages to restore private sector and household sentiment

with a large-scale, effective stimulus package which leads to a recovery in asset prices. This would see the housing turn a corner with prices stabilising and inventories falling at a faster pace after fiscal measures accelerate SOE purchases of unsold homes. Consumption might also receive a kick-start from fiscal policy support, triggering a virtuous cycle.

Finally, our global outlook receives a boost if tensions in the Middle East subside and/or if the war in Ukraine peacefully ends earlier than many expect.

All of this would see less divergence between the Federal Reserve and European Central Bank over the coming years, driven mainly by the latter. The Federal Reserve, in the absence of tariffs and the resulting inflation hit, might end up taking rates a little lower than it otherwise might. The ECB, faced with a stronger growth outlook, would keep rates closer to 2.5% in the medium term. Depending on how far rates fall initially, that could even entail some very modest rate hikes in the first half of 2026.

## The downside risks: Recession fears reignited, regardless of the election

As the dust settles on the US election result, the focus is going to quickly recentre on the macro story. Until we get further progress on tax cuts, and at least over the next couple of meetings, the Fed's focus is going to stay resolutely on the jobs market, where the downside risks have certainly not gone away. October's jobs report was distorted by hurricanes, but sizeable backward revisions were a reminder that the hiring trend is slowing. Further surprise weakness in the next few payrolls reports could revive fears that the Fed is behind the curve on rate cuts.

Fiscal sustainability concerns and the threat of tariff-induced inflation have already led to US government bond yields rising sharply. They could rise much further and pull mortgage rates and corporate borrowing costs higher too. Combined with dollar strength, this tightening of monetary conditions could weigh heavily on US growth.

The second risk is that China's stimulus falls short in scale or is directed to ineffective areas, and confidence once again collapses. Property prices continue to decline at a concerning pace and the latest round of measures remains insufficient, continuing to suppress sentiment through a negative wealth effect. Consumption and private investment remain weak as a result, and public-led investment is insufficient to offset this drag. External demand falls off sharply due to tariffs and/or slowing global economic growth, which causes China's current primary growth driver of industrial production to sputter.

Oil remains a clear "known unknown". As Warren discusses separately, the risk is that OPEC+ decides to continue rolling over additional voluntary supply cuts into 2025. A revival in Iran-Israel tensions, which for the first time prompted a direct hit to oil supply, could also take prices materially higher. The tail risk, as always, is that we see a blockade in the Strait of Hormuz. That could take prices above \$150 USD/bbl.

Central banks face a dilemma – look through the rise in oil prices and support demand, or keep rates elevated in order to balance second-round effects.

Experience from the past couple of years suggests policymakers might opt for the latter. Rates fall back to neutral more quickly but don't go materially "accommodative". But weaker global growth could easily see a rethink at the major central banks as unemployment rises.

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