

Macro Insights Weekly

Three risks for 2026

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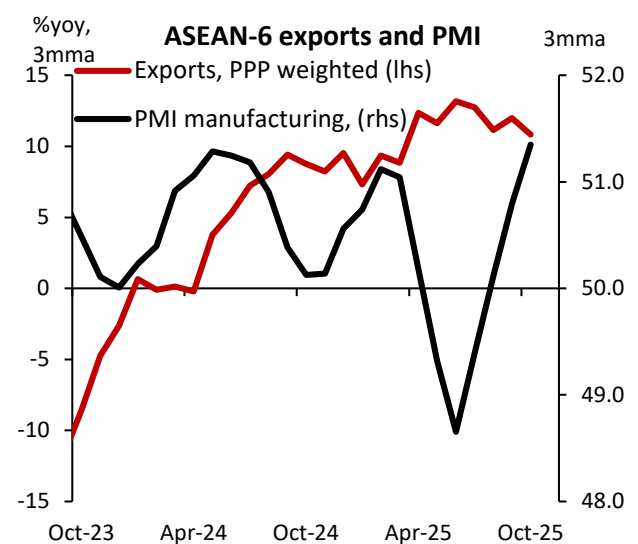
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- *The global economy is ending the year with much better outcome than expected. The 2026 outlook is broadly constructive; but we have three risks in mind that could spoil the picture.*
- *Inflation and interest rates should be constructive for most economies.*
- *Global trade is proving to be resilient.*
- *Three risks: First, a major correction in the US stock market, with global reverberations.*
- *Second, global bond market selloff.*
- *Third, an exacerbation of geoeconomic risks.*

Chart of the Week: Manufacturing optimism

Regional manufacturers and exporters are ending 2025 feeling constructive. Having experienced a crisis-like dip in their sentiments earlier this year, they have seen their exports, whether to the US or China or elsewhere, do much better than expected. This outperformance goes beyond the “front-loading” dynamic of earlier this year, when exports jumped to get ahead of US tariffs. Overall, global economy and trade have been resilient, defying the inward pivot of the US.



Source: CEIC, DBS.

Commentary: Three risks for 2026

The global economy took in a great deal of stress in 2025; but it is ending the year with much better outcome than expected. Fears that global trade and commerce will succumb to endless geoeconomic volatility unleashed by the US has thankfully proven to be wrong. All economies in South and South-East Asia are on track to have their exports rise substantially in 2025 over 2024, both to the US and the rest of the world. The key actors in the trade war, China and the US, are tracking economic growth rates much higher than forecast back in April.

The 2026 outlook is broadly constructive. Inflation is not an issue in most parts of the world, the US being an exception. Interest rates have been on an easing trend worldwide, with only Japan bucking the pattern. A major tech investment cycle is underway, and commodity supply-demand balance is favourable. Short of a few manifestations of shocks, another stable year lies ahead, in our view. But it is worth looking at a few scenarios under which this benign outlook can be upset.

First, a major correction in the US stock market. If companies that are leading the AI-tech wave begin to report a slowdown in earnings growth or the new US-developed AI models turn out to be not superior to the made-in-China models that are much cheaper, there could be a major reckoning. Hundreds of billions being deployed to AI-infrastructure could prove to be excessive, warranting a re-rating of the value of the entire AI-investment complex. Given the disproportionate valuation of tech companies in the major US stock indices, and the disproportionate size of US stocks in global equity holdings, a sharp correction of AI-

adjacent stocks will reverberate through global financial markets. It would hit the balance sheets of asset managers, sovereign and private, cast a chilling impact on investment and lending, and affect global consumer sentiment substantially. It is not clear to us if there are major systemic implications like there was during the 2008 global financial crisis, but even if the shock turns out to be of smaller magnitude than it was then, there would nonetheless be financial stability implications. Credit spreads of AI-related businesses would jump and electronics exports, especially semiconductors and servers, would likely collapse. US growth could fall to 1% or below in this scenario.

Second, global bond market selloff. Warning lights are aplenty, from record debt burdens in industrial economies to rising rates in Japan. For the US, sticky inflation, no progress toward fiscal consolidation, data issues, a propensity toward financial repression, and a steady erosion of Fed independence add up to rather worrisome mix. This could lead to short-term interest rate volatility and yield curve inversion, and like the equity market selloff scenario, have adverse ramifications for the global economy.

Third, an exacerbation of geoeconomic risks. There is no shortage of conflict flash points, ranging from Latin America to Europe to the Middle East to Asia. There is also no assurance that a flurry of late-year “deals” would pave the way for a stable trade environment next year. Like it or not, these risks will be omnipresent in 2026, in our view.

Taimur Baig

FX: Commodity currencies shine before FOMC

Markets may pay less attention to Fed Chair Jerome Powell at the December 10 FOMC meeting. The centre of gravity may already have shifted towards US President Donald Trump's impending pick for Fed Chair, a decision he may announce around the turn of the year, months before Powell's term ends in May 2026. Investors are increasingly focused on the emerging Shadow Fed rather than Powell's short-term guidance. The futures market has started to reflect this transition, with rate cuts in 2026 being driven more by expectations of a new supply-side-oriented Fed Chair, weighing on the USD.

Against this backdrop, commodity currencies – AUD, NZD, and CAD – have outperformed in the first week of December. Markets view the Fed as having more cuts ahead in 2026, while its counterparts in Australia, New Zealand, and Canada may have finished with easing and signalling a high bar for additional cuts.

AUD has the strongest policy divergence story, with the futures market pricing in a possible 2026 hike. In contrast to the Fed, the Reserve Bank of Australia is prioritising inflation over jobs in its dual mandate. Both CPI and core inflation have risen above the RBA's 2-3% target band, while the unemployment rate is slightly below the NAIRU, or the non-accelerating inflation rate of unemployment. During the Senate hearing on December 3, RBA Governor Michele Bullock said the private sector may be starting to take over from the public sector as the driver of economic growth. Bullock rejected allegations that the monetary policy was responsible for rising housing prices.

USD/CAD broke decisively below 1.40 last week to 1.3817, retracing some 50% of July-November's rise. Following stellar Canadian jobs data, no one expects the Bank of Canada to mirror the Fed's expected cut this week. In contrast to the soft US labour market, Canada's unemployment rate fell to 6.5% in November, bucking the consensus for an increase to 7% from 6.9% in October. Apart from 275 bps of rate cuts since mid-2024, the Canadian economy is also supported by a fiscally stimulative budget. Hence, the BOC is unlikely to take any chances even though inflation has been near target. Look for the BOC to signal an extended pause at this Wednesday's meeting. The OIS market is more hawkish and has started positioning for a possible BOC hike in late 2026. Look for any correction to reinstate USD/CAD shorts to September's low of 1.3725.

NZD/USD rebounded from the year's low of 0.5580 after the Reserve Bank of New Zealand cut rates and signalled a high bar for further easing at its November 26 meeting. Prospects for an extended pause lifted NZD to 0.5775 last Friday. Assuming her position on December 1, new RBNZ Governor Anna Breman was clear about restoring credibility to the monetary policy. Her appointment came after the departure of former governor Adrian Orr, who drew government criticism for losing control of inflation, prompting his resignation in March. With inflation higher at 3% in 3Q25, Breman will focus on returning it to 2% or the middle of the 1-3% target range. NZD/USD needs to break above 0.5785 (38.2% Fibonacci retracement level) to further advance to 0.5850 (50% Fibo).

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