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Major Country Risk Developments
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Overview

U.S. long-term borrowing costs surged to their highest level in nearly two decades, as a jump in oil prices and the latest evidence of stubbornly high inflation reignited a global bond sell-off. The 30-year U.S. bond yield rose to 5.36%, its highest level since 2007, after the U.S. Treasury's $6 billion buyback plan received a frosty reception from investors.

Bonds are facing a double hit—oil prices are creeping higher, while U.S. buybacks and growing credibility risks are pushing long-term premiums higher. A $22 billion auction of 30-year Treasuries is being closely watched for signs of investors appetite for U.S. government debt. Yields also climbed sharply in Europe as a slump in Saudi crude production added fresh impetus to a rally in oil prices, confirming that the escalating conflict in the Middle East continues to disrupt global energy supplies and stoke inflationary pressures.

In the U.K., borrowing costs also hit their highest levels since 2007, with the 10-year yield rising 0.07 percentage points to 5.34%. German 10-year yields climbed 0.04 percentage points to 3.48%. The bond sell-off came as the European Central Bank (ECB) raised its deposit facility rates to 2.5%, warning that inflation in the Eurozone is expected to remain well above the 2% target for an extended period, as the war keeps energy prices high. The price of Brent crude, the international oil benchmark,

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rose as high as $109 a barrel. West Texas Intermediate, the U.S. benchmark, climbed to $100 a barrel for the first time since May. Underlining the price pressures in the U.S., the latest data showed wholesale inflation ticked higher in August as resurgent fuel costs made it more expensive to ship goods across the country.

The U.S. Bureau of Labor Statistics' Producer Price Index rose to a year-on-year rate of 5.4%, from 4.7% a month earlier, a larger increase than anticipated. The government conceded that oil prices will stay elevated for the rest of 2026, as crude prices surged past $100 a barrel following the latest escalation of hostilities in the Middle East.

Analysts are ratcheting up forecasts for oil prices over 2026-2027 amid few signs the U.S. and Iran are prepared to agree on a peace deal. S&P Global Energy concluded that oil markets were settling into a new normal of higher prices as the prospects for a definitive resolution to the Iran conflict dimmed and Brent crude prices topped $100. For the first time since the US-Iran war started, S&P said it did not project Middle Eastern crude oil production to return to prewar levels by the end of 2027. "The market is not returning to calm; it is adjusting to the new normal defined by unresolved conflict and persistent maritime risk — one where oil flows stay below prewar levels and the path forward remains uneven," it concluded.

Renewed Middle East hostilities come as traders and analysts warn of a renewed supply crunch in oil markets as countries draw down strategic reserves.

Meanwhile, governments around the world have created a $2 trillion monster — a debt-servicing burden that consumes greater tax revenues and has the power to overwhelm elected leaders. More money is now spent on servicing the national debt than on defense in the U.S., the U.K., and France. This is true for more than a dozen states in the 38-member OECD.

Their problem is that borrowing costs have climbed to the highest level in two decades just as governments are taking on record debt. The total owed by the U.S. government reached a record $40 trillion in August 2026.

OECD countries are expected to borrow $18 trillion between them in 2026, another all-time high. In 2025, the OECD total debt-servicing bill exceeded $2 trillion, or 3% of GDP. That number is set to rise in the coming years because of the bond sell-off that has pushed up yields since the Covid-19 crisis, increasing the cost of debt for governments across the world. These massive sovereign debts must be refinanced at ever-increasing rates.

The current rout in global bond markets has only intensified the post-Covid surge in yields triggered by inflation shocks, increased government borrowing and the end of central banks' "quantitative easing" bond-buying programs. The average benchmark 10-year bond yield for G7 countries has exceeded 4% for the first time since 2008, amid concerns about the inflationary impact of the Iran war and the sheer amount of debt being sought by both the public and private sectors — particularly tech groups.

While governments are still finding buyers for their debt, investors are demanding a higher price for their money. New bond sales in recent months for the U.S., the U.K., and others have locked in the highest yields in almost two decades for longer-dated debt. This shift has been accelerated by changes to pension schemes in some countries. Pension reforms in some countries have pushed traditional long-term buyers to step back, replaced by fast-money hedge funds quick to demand higher yields

The nature of government debt markets, where governments fund themselves with debt repaid over a wide range of maturities - some coming due decades into the future - means that higher borrowing costs feed into higher interest costs occurs gradually over time. The U.S. Congressional Budget Office estimates that U.S. debt costs will double over the next decade and, on the current trajectory, exceed Social Security spending after 2047.

The burden for other countries — which typically find it harder than the U.S. to convince investors to buy their bonds on favorable terms — is likely to be higher still. The causes of the problems with public finances are deep-rooted and long-running.

Global public debt hit 94% of global GDP last year, up more than 10 percentage points since the year before the pandemic. The International Monetary Fund now believes it will reach 100% by the end of this decade. This summer's bond sell-off has aggravated the problem. Inflationary pressures stoked by the Iran war, initially in energy prices, have forced central banks to pivot towards rate increases. The ECB raised rates in June for the first time since 2023, and did so again in September, while the Federal Reserve ("the Fed") has begun signaling likely rate increase this fall.

Uncertainty over inflation is feeding into higher long-term rates, with the market demanding more to lend to governments over the long term. Others think that the higher yields are more a reflection of worries over growing debt supply, both from governments but increasingly from the corporate sector. The stock of combined government and corporate debt globally is approaching $300 trillion, according to the Institute of International Finance.

U.S.A.

The U.S. economy grew just 1.5% in the second quarter, a marked slowdown from the 2.1% pace in the first quarter. Full-year 2026 GDP growth is projected at 2.1%.
Inflation is still running at 3.4% year over year, up from 2.7% during the same period last year, according to the Bureau of Labor Statistics. Still, inflation is far below the 9.1% peak in 2022, but high enough to hurt confidence and affect the outcome of the upcoming midterm elections. Over the past year, hourly wage growth fell by 0.2%, and average weekly earnings rose by just 0.1%, meaning wages lagged significantly behind inflation.

According to the Conference Board, U.S. consumer confidence is significantly down from the same period last year and indexed at 89.4, its lowest level in seven months. On the positive side, consumer spending has been solid. Furthermore, U.S. job growth bounced back in August. The economy added 162,000 jobs, and July numbers were revised upward by 21,000. The unemployment rate has remained unchanged at 4.1% since last year.

U.S. manufacturing is showing signs of a revival. Following six months of expansion, factory activity surged to its strongest in more than four years in July. So far in 2026, production has edged higher, around 30,000 new jobs have been created and in August companies unveiled hefty investment plans.

The U.S. manufacturing resurgence has continued despite tariffs, powered by strong demand in two sectors that underpin the expansion of industrial output. The first sector is electronic products, which include chips and servers feeding the ongoing AI drive, and the second is aerospace, where aircraft backlogs-most notably Boeing-are being filled and global conflict is swelling defense order books.

Demand for other components used to build data centers, such as transformers, generators, cooling equipment and cement, helps to prop up broader U.S. industrial output. Crucially, AI and aerospace inputs have benefited from significant carve-outs from the various U.S. tariff schemes. By contrast, sectors facing some of the highest duties-including textiles, furniture and wood-have contributed little to output, or have shrunk according to the Cato Institute.

The manufacturing revival has dovetailed with a notable pick-up in imports. The strength in U.S. capital goods imports since January 2025 has been driven by demand for components linked to AI. The jump in production this year has coincided with a drop in the effective tariff rate and the easing of trade uncertainty following the U.S. Supreme Court's decision in February to strike down the bulk of the 'Liberation Day" tariffs.

Some manufacturers report that it is getting harder to find inputs they need. Metal fabricators who make machines for tractors and trucks say they are experiencing disruption in their ability to secure raw materials. Steel for example is posing noticeable issues.

The AI boom has made securing goods increasingly challenging. Due to frenzied demand for specialized parts for memory chips and processors, suppliers are struggling to keep pace.

Shortages are being felt globally. In an August survey conducted by the Global Electronics Association, two-thirds of electronics manufacturers worldwide reported limited component availability or extended lead times. These strains will only get resolved when production increases everywhere across the supply chain.

Manufacturers are paying sharply more for raw materials, energy and freight, with some input costs rising by double-digit rates, according to executives and industry data, forcing some to raise prices and threatening further pressure on consumer inflation.

Saudi Arabia

Saudi Arabia's GDP contracted by 4.7% from a year earlier in the second quarter, as the disruption to oil exports hammered activity. The kingdom's budget deficit, at the equivalent of $42.7 billion in the first half, is already running close to the shortfall it had budgeted for the entire year.

According to the International Energy Agency ("IEA"), Saudi crude-oil production has been falling, hitting its lowest level in more than three decades last month. Crude supply fell by 2.3 million barrels a day, to 6 million barrels a day in August, the IEA confirmed. Saudi Arabia produced around 9.4 million barrels a day on average last year.

On September 11, the Saudis were forced to shut down their East-West pipeline after it was damaged by multiple drone attacks launched from Iraq. This meant closing a crucial pipeline that allowed Saudi Arabia to continue exporting crude oil since the closure of the Strait of Hormuz. The crucial East-West pipeline can carry up to 7 million barrels of crude a day 750 miles from Saudi Arabia's oil-producing heartland on the Persian Gulf to the port of Yanbu on the Red Sea. From there, the Saudis were able to ship millions of barrels of oil to customers around the world.

The armed conflict between Saudi Arabia and Iran-backed Houthi rebels in Yemen has escalated to near-

full-scale war around the Bab el-Mandeb Strait, the critical chokepoint at the entrance to the Red Sea. As the Strait of Hormuz remains effectively blockaded amid the U.S.-Iran war, clashes in the Bab el-Mandeb Strait, a lifeline for Saudi oil exports, have intensified. According to estimates, over 500 people have been killed and approximately 20,000 displaced.

The Saudis confirmed several drones attacked causing injuries and damage to the pipeline that the kingdom is repairing. The drones were fired from Iraq, where local authorities have struggled to control Iran-backed militias that have targeted Saudi infrastructure. Saudi Arabia, with the U.S., carried out rare airstrikes earlier this year against Iraqi militias, but this time, the Saudis refrained from retaliating.

The pipeline hit comes as Iran-backed Houthi militants in Yemen took hold of the Bab al-Mandeb Strait. The Houthis took control of Perim Island, and the Yemeni town of Dhubab, which sits directly on the strait, capping a series of swift Houthi gains.

As oil markets rise, with Brent crude trading above $104 a barrel, traders are focused on whether strikes on pipelines, ports and tankers will further reduce the amount of Gulf oil reaching the global market. That, in turn, is hitting the bond market, raising borrowing costs including mortgage rates.

Oil traders project that Houthi advances and damage to the East-West pipeline could boost oil prices toward $120 a barrel, though the fallout will depend on the extent of damage. If the conflict persists, the risks to energy supplies and prices persist. The pipeline strike tightens the squeeze Saudi Arabia faces on both of its main export corridors. The Iran conflict has constrained shipments through Hormuz, while the Houthis have intensified attacks on energy infrastructure and Saudi Red Sea shipping.

It is not the first time the East-West pipeline has been pulled into the conflict that began when the U.S. and Israel attacked Iran in February. Attacks earlier this year damaged a pumping station and reduced the line's capacity by about 700,000 barrels a day. The country restored the pipeline to its full capacity within days. The latest attacks targeted several pumping stations. Saudi Arabia will likely repair damages relatively quickly but there is the risk of repeat attacks. So, while this does not end the East-West bypass, it adds additional strain, compounded by the threat to shipping in the Red Sea.

The disruptions are adding pressure to the Saudi economy and complicating Crown Prince Mohammed bin Salman's Vision 2030 plans, which rely on sustained state spending to diversify the economy and finance large-scale infrastructure projects.

The attacks also struck Saudi Air Force bases and key Aramco oil refining and power facilities. Saudi authorities stated that at least 73 people, including women and children, were injured. This marks the largest-scale attack on Saudi territory since the U.S.-Iran war erupted in February.

The Saudi economy is the largest in the Middle East. Despite growing financing constraints, the crown prince and de facto ruler, Mohammed bin Salman al-Saud, is pressing ahead with a far-reaching plan (Vision 2030) to modernize and diversify the economy while embracing social change. However, political reforms will remain largely off limits.

Saudi policymakers have long recognized the importance that investors place on a stable political environment as they seek to sustain support for their ambitious economic diversification plans. However, the Iran conflict has reinforced Saudi Arabia's concerns about its exposure to regional instability.

The limitations of relying predominantly on the U.S. security umbrella became increasingly apparent during the ongoing war, although this is unlikely to lead fundamental changes in the kingdom's strategic partnership with the U.S. Instead, Saudi Arabia will seek to cultivate other global alliances as a way of providing an extra layer of protection. This process was already under way before the Iran war, illustrated by the Strategic Mutual Defense Agreement that the kingdom signed with Pakistan in September 2025. The security arrangement has now been expanded to include Turkey.

The country's economic diversification strategy could open investment opportunities for local and foreign firms alike over the next decade. However, some of the more grandiose official plans are being scaled back because of financial constraints. The operating environment for businesses should be enhanced by reforms, including changes to the commercial court system and a new foreign investment law, but the effectiveness of these reforms will become evident only over the medium term.

The Iran war has caused a hiatus in the rolling-back of the constraints on oil production that Saudi Arabia together with its OPEC+ partners, pursued in 2025. However, the kingdom will be eager to restore its previous oil output levels and take advantage of its large spare capacity as soon as possible. This should spur economic growth once regional stability is restored, and additional support would come from a rapid expansion of natural gas production.

Growth over the next four years will also be driven by a rising contribution from non-hydrocarbons sectors, such as manufacturing, mining, renewable energy and artificial intelligence. The setbacks to tourism caused by the Iran war will dissipate slowly, but we expect a recovery in the sector to strengthen in 2027 and onward. The riyal is pegged to the U.S. dollar, at SR3.75:US$1—a rate that has been in place since 1986. The peg will likely remain unchallenged. Backed by its large financial assets, and continued demand for hydrocarbons, Saudi Arabia has historically demonstrated a capacity to weather serious global headwinds.

South Korea

South Korea's economy is in a state of recovery momentum, though with uneven underlying dynamics. Growth is accelerating as the country capitalizes on the global memory chip investment cycle. The latest forecast projects GDP growth of 3.3% in 2026, a notable step up from 1.1% in 2025, before moderating to 1.5% in 2027. This acceleration reflects strong semiconductor demand,

with Samsung Electronics and SK Hynix capturing a commanding position in the global memory chip market where overseas demand still outpaces local production capacity.

Export strength is the economy's primary growth engine, with ongoing business investment in equipment and facilities supporting the expansion. However, this export-led dynamic hides growing weakness in domestic demand. Consumer spending is constrained by elevated inflation, which is driven by rising energy costs and deteriorating labor market conditions, as manufacturers scale back payroll amid uncertainty over overseas demand.

The near-term risks to growth are material. South Korea's vulnerability to energy supply disruptions is pronounced: over 70% of crude oil and 20% of liquefied natural gas ("LNG") imports pass through the Strait of Hormuz.

Beyond energy, the chipmaking sector depends heavily on helium imported from the Middle East, adding another layer of supply-chain exposure. A prolonged conflict in that region would have cascading effects across both input costs and production capacity.

Meanwhile, U.S. pressure on South Korea to contribute to Middle East security continues to mount. The U.S. scaled back joint military drills with South Korea in August as it pushed its ally to consider becoming involved in securing free shipping through the Strait of Hormuz. As the world's third-largest buyer of LNG, South Korea's reliance on energy imports makes it extremely vulnerable to tensions in the Middle East.

Nonetheless, as the country responds to U.S. pressure, the South Korean government is reportedly reviewing a possible military deployment to the Strait of Hormuz. South Korea announced it was considering various options including dispatching a warship to the Strait. The U.S. criticized Seoul as it announced an eleventh-hour reduction to military drills with South Korea in August, saying it had refused to support the U.S. war against Iran. South Korea reported it will conduct a review in accordance with domestic legal procedures, considering the security posture on the Korean Peninsula. It stressed that nothing has been decided, but that a review is underway.

U.S. officials also await proposals of concrete South Korean investment projects in the U.S., a year after it agreed to invest $350 billion as part of negotiations in exchange for U.S. tariff relief. South Korean officials complain that the U.S. have not applied similar pressure on Japan, but Tokyo had already made several investment commitments in the U.S.

The two allies routinely conduct joint military exercises on and around the Korean Peninsula in a longstanding effort to deter North Korea. Any deployment would be a political risk for South Korea's President Lee Jae Myung, whose approval ratings are already languishing at historic lows. A Korea Gallup poll in March, conducted days after U.S. expressed hope that South Korea and other countries would send warships to the strait, found 55% of South Koreans were opposed to doing so.

The U.S. says the South Korean snub raises questions in the Asia-Pacific. South Korea faced a similar dilemma during the first Trump term, when the U.S. raised the prospect of drawing down the ranks of the 28,500 U.S. troops stationed in South Korea and scrapping a bilateral trade agreement amid a cost-sharing dispute. In 2020, amid escalating U.S.-Iran tensions and pressure from Washington, then-president Moon Jae-in expanded the operating area of Seoul's 300-strong Cheong Hae anti-piracy naval unit, which focused on the waters around Somalia, to include the Strait of Hormuz. However, the Korean president stopped short of joining the U.S.-led maritime coalition, opting instead to operate independently to avoid angering Tehran.

According to the Korea Risk Group, if Seoul deploys military assets in the Middle East, it remains doubtful that Iran would continue to treat South Korea as a "non-hostile country." Even if South Korea were to limit its military involvement to logistics and support, the move could still carry significant diplomatic and economic costs for South Korea.

Canada

Canada faces significant macroeconomic headwinds driven primarily by US trade policy uncertainty and its deep economic integration with the U.S. Real GDP growth slowed to 1.9% in 2025, with the economy broadly stagnant in the first quarter of 2026. The forecast is for GDP growth of just 0.9% in 2026, reflecting persistent uncertainty surrounding tariffs and the United States-Mexico-Canada Agreement ("USMCA") review.

The near-term outlook remains constrained by external pressures. Although U.S. tariffs have moderated from peaks of 35% to a blanket 10% – after the U.S. Supreme Court struck down the prior IEEPA tariffs in February 2026 and the administration replaced them under Section 122 – targeted tariffs continue to weigh heavily: 25% on autos and auto parts, 50% on steel and aluminum, and 10% additional on softwood lumber. These sectoral tariffs pose risks to provinces like Ontario and Quebec, where manufacturing is central. That said, household consumption should remain comparatively resilient, supported by lower interest rates and contained inflation, whilst higher oil and commodity prices will boost export revenues.

Looking ahead, the expectation is for a gradual recovery. Growth is forecast to accelerate to an average of 2%

annually in 2028-30. However, Canada will remain vulnerable to external risks, including further protectionist U.S. trade policies and commodity price fluctuations. Domestically, political polarization is expected to intensify over years 2028-30, driven by economic disparities, housing affordability challenges and regional tensions. Canada's economic outlook reflects a transition from near-term weakness to gradual recovery, contingent on tariff dynamics and global commodity prices.

The U.S. called for a boycott of several Canadian companies and products including Bombardier, the Canadian business jet manufacturer. This follows Canada imposing retaliatory tariffs on $20 billion worth of U.S. goods - in the intensifying trade war between the countries. President Trump said there should be no more selling Bombardier in the U.S. He added that more than 50% of the company's revenue came from the U.S and insisted that Canadian companies build more of what they export to the U.S. in the U.S.

The U.S. also accused Ottawa of blocking Gulfstream Aerospace from doing business in Canada. President Trump's posts came just before new Canadian counter-tariffs on U.S. goods became effective at midnight on September 8th. Canada's "dollar-for-dollar" retaliation applies levies of up to 50% on US $20 billion worth of U.S. goods. They come after the U.S. imposed tariffs on an equal value of Canadian goods in August.

The U.S. administration has threatened additional 50% tariffs as the trade war between the neighbors shows no sign of easing. Leaders from both countries confirmed that no formal talks are planned to resolve the impasse, as each side blames the other for the collapse of trade deal negotiations.

In late January, the U.S. escalated its dispute with Canada by threatening to "decertify" Bombardier jets in the U.S. and slap a 50% tariff on all Canadian-made aircraft – ostensibly over Canada's slow certification of U.S. Gulfstream jets. The tariff fix leaves U.S. trade policy in a state of flux. The administration did not immediately clarify whether its latest move against Canada was a call for additional trade measures targeting Bombardier or for Americans to stop buying the company's products. A spokesperson for Canada's transport minister stressed that Gulfstream aircraft are and can continue to be, freely sold and operated in Canada.

Bombardier employs more than 3,000 people at nine U.S. facilities and sources goods from 2,800 U.S. suppliers. "Bombardier values its great partnership with American companies and its U.S. employees," the company said in a statement, adding: "Our plan is to continue to invest in our people, our customers and the communities in which we operate across the country." The jet maker's Toronto-listed shares fell more than 6% in early trading on Tuesday following the imposition of the tariffs and Trump's call for a boycott of the company.

Prime Minister Mark Carney says Canada is ready for talks with Washington but cautioned a deal was unlikely considering ongoing U.S. hostility toward Canada.

Continued U.S. taunts against Canada have not helped. The U.S. trade representative blamed Canada for turning down a very good deal, saying Ottawa had overplayed its hand and warned that the U.S. relished the trade fight. The trade official also hinted that the president would respond to Canada's tariffs with additional levies on the U.S. side.

The breakdown in talks came after 18 months of tension in which the U.S. threatened annexation through economic force, as well as tariffs on Canadian steel, aluminum, automotive and lumber sectors. Following the end of trade talks over Washington's new 50% tariff, and on August 25, Canada announced retaliatory levies of 15, 25 or 50% on $20 billion worth of U.S. imports, such as cheese, honey, appliances, cosmetics, agricultural equipment, motorcycles and video game consoles.

In late August, the U.S. threatened to double duties on Canadian cars to 50% and days later, President Trump signed an executive order renaming Lake Ontario -- which straddles the U.S. and Canada -- to "Lake America." Robert Zoellick, a former head of the World Bank and a former U.S. trade representative, called the U.S. threats against Canada self-defeating.

PM Carney will shortly host an investor summit, aimed at unlocking $1 trillion pool of global capital, in an attempt to invigorate efforts to decouple the Canadian economy from the U.S. Carney is targeting the world's richest asset managers to increase their Canada exposure in oil & gas pipelines, nuclear plants, mining, railways, ports and AI data centers totaling 167 projects.

Canada's Public Sector Pension Investment Board, which has C$320.6 billion worth of assets under management, said international investors are underweight on Canada relative to other jurisdictions. The Canadian fund is expecting to increase investments in Canada by 30%- 40% in four years. The summit is pivotal to Carney's plan to unite the world's "middle powers" as an alternative to the U.S.-centric world order, which is in transition. Canada is promoting its triple A credit ratings, a mark of outstanding fiscal credibility and near-zero default risk, as a safe bet. However, business leaders say while Carney looks abroad for foreign support, serious work at home needs to be done to lure investment. They insist that more capital will flow when Ottawa lowers taxes, shortens permitting timelines, incentivizes investment and improves the regulatory landscape. Carney needs big investors to back his pledge to turn Canada into an "energy superpower", considering its vast oil and natural gas resources, as it pivots to supplying Asian and European markets.

Turkey

The forecast is for GDP growth of 2.6% in 2026, with expectations that growth will pick up to 3.8% in 2027, aided by a degree of fiscal loosening, income support and possibly monetary policy loosening ahead of the 2028 national elections.

Turkey's GDP grew by 2.3% year-on-year in the second quarter of 2026, according to the Turkish Statistical Institute (TurkStat). External conditions and anti-inflationary policies will continue to constrain economic activity, although GDP growth is expected to pick up in 2027 as the government makes efforts to boost the economy ahead of elections in 2028. GDP growth is set to remain subdued through the remainder of 2026 before gradually accelerating in 2027 as pre-election stimulus kicks in.

GDP growth held up quite well in 2024-25, sustained by household consumption amid relatively tight, anti-inflationary policies and challenges in export markets. Revised data show that annual growth picked up from 3.5% in 2024 to 3.7% in 2025. The slowdown since then has been relatively pronounced. Year-on-year growth decelerated for the fourth successive quarter in the second quarter of 2026, reaching 2.3%, which is the lowest rate in four years.

Monetary conditions are set to ease modestly in the second half of 2026, providing some relief after a mid-year tightening shock. At the time the Iran war began, it pushed up fuel and other prices, keeping inflation above 30%, and prompted the Central Bank of Turkey ("CBT") to suspend its weekly repossession auctions, effectively raising the cost of funding from 37% to 40%, and affecting economic activity in the second quarter. On August 24th, the CBT resumed repossession auctions and could start cutting its 37% policy rate in the third or fourth quarter. That said, the economic slowdown may already have run its course. On a quarter-on-quarter basis, the economy grew by 1.1% in the second quarter, the highest rate of the past four quarters.

The composition of second-quarter growth points to an economy under pressure but not in freefall, with pockets of resilience that could support a recovery. Household consumption (about 55% of GDP) grew by just 3.5% year on year and contracted by 1.3% quarter on quarter, reflecting squeezed real incomes. Export performance improved modestly compared to imports, while industry held up better than expected, with value added rising 2.4% year on year. Agriculture surged 13.3% owing to much better weather than in 2025, but this boost could fade.

The outlook for the third and fourth quarters of 2026 is mixed. International tensions and oil prices remain high, and available indicators for July and August point to a still-sluggish Turkish economy. Meanwhile, easing monetary policy and cautious fiscal stimulus ahead of the 2028 elections should support a gradual recovery from late 2026.

One of the main tasks of Turkey's Medium-Term Economic Program (2027-2030) is the fight against inflation. The authorities confirmed that inflation reached 75.5% in May 2024, and thanks to policies implemented, as of August 2026, inflation stood at 31.5%. Inflation is expected to end 2026 at 28.4%.

The government highlighted the program's main goals as follows: (1) reduce inflation to single digits in the long-term; (2) create 2.1 million new jobs, reducing unemployment below 8%, (3) expand Turkey's GDP above $2.2 trillion; (4) increase exports of goods and services to $450 billion; and (5) increase in GDP per capita to $25,000.

Around $104 billion will be allocated for the recovery of regions affected by earthquakes, and by the end of 2027, expenses will exceed $116 billion. Construction of 455,000 housing units for right-holders has already been completed. Special attention will be given to economic security and resilience: reducing dependence on imports of energy and critical resources, strengthening food security, developing the defense industry, healthcare, semiconductors and artificial intelligence, as well as increasing the resilience of cities to natural disasters.
The framework of medium-term program forecasts defense spending increasing by 229%, housing spending by 150%, and investments in railway projects by 49%. Also envisaged are increases in investment in irrigation by 42%, drinking water by 71%, organized agricultural zones by 103% and investments in the mining sector by 139%.

Meanwhile, a Turkish court ruled in favor of the removal of the leadership of Turkey's biggest opposition party; in a landmark decision that could tighten President Recep

Tayyip Erdoğan's hold on power and spark market turmoil. The court nullified the results of a 2023 congress of the Republican People's Party (CHP), a move that voids the election of Özgür Özel as its chair and could hobble Turkey's main opposition force. Turkish stocks fell more than 6% after the ruling. The lira dipped sharply but quickly bounced back to trade broadly unchanged at 45.6 against the dollar.

The decision opens the way for the return of former CHP leader Kemal Kılıçdaroğlu, an unpopular figure who could potentially upset party unity in the run-up to the next presidential election in 2028. İmamoğlu's arrest sparked mass riots and a financial panic that led the central bank to spend $50 billion to support the lira. Since then, dozens of other CHP officials have been detained, further increasing concerns about democratic backsliding and worrying investors. The CHP, which is running even with the ruling party in opinion polls, has faced an unprecedented judicial crackdown since the arrest last year on corruption charges of Istanbul mayor, Ekrem İmamoğlu, widely seen as Erdoğan's main rival.

Foreign exchange reserves suffered a record $43 billion decline in March 2026, and the current account deficit has widened, exposing a potential financing gap. In addition, Turkey's economy and financial markets are strained because of the energy market fallout from the Iran war, which particularly affects Turkey's imports of almost three-quarters of its energy needs.

Separately, Turkey and Israel have traded accusations after the Israeli bombing of a Syrian air base 70 kilometers from the Turkish border intensified a growing power contest between two of the Middle East's strongest militaries. Turkey objected to Israeli strikes on the Abu al-Duhur base, which drew rare criticism from U.S. envoy, Tom Barrack, who described the strike as an "unnecessary escalation."

Israel accused Syria of being on the verge of breaching an agreed security status quo by allowing Turkish troops to deploy at the base. Israel warned Syria that such a deployment would threaten its security. This highlights increasingly incompatible Turkish and Israeli visions for Syria, as well as the wider region. Turkey is one of the principal backers of the government of Syrian President, Ahmed al Sharaa -- a former militant Islamist who, under the nom de guerre Abu Mohammaed al-Julani, led the rebel offensive that ousted strongman Bashar al-Assad in December 2024.

Turkey has provided military training, equipment, and logistical support to Syria to rebuild state institutions shattered by Syria's nearly 14-year civil war. Israel sees Syria's government, which is dominated by al Sharaa's Islamist faction, as a threat. Israel has conducted repeated strikes in the country since the overthrow of Assad, destroying much of the former regime's military infrastructure and occupying positions in southern Syria. Israel has also objected to Turkey — which maintains thousands of troops across northern Syria following successive interventions during the civil war — establishing military infrastructure that could restrict Israel's freedom of action, particularly in Syrian airspace.

Turkey says it will continue to co-operate with the Syrian government for the establishment of peace, stability and prosperity in Syria. The Institute for National Security Studies in Tel Aviv, said Israeli concerns about Turkey stemmed from Ankara's increasingly hostile rhetoric and its expanding regional military ambitions and capabilities.

President Erdogan and his ministers describe NATO as a cornerstone of Turkey's security. Public support for the alliance has risen since the 2010s, though it remains lower than in most member states. The U.S. war with Iran and Russia's invasion of Ukraine have brought NATO's value home. In early March, NATO air defenses intercepted Iranian ballistic missiles bound for Turkey. Turkey hosts two NATO bases and a radar station, and the alliance's presence is set to grow. Germany deployed a new Patriot air-defense system, accompanied by 150 troops, to southern Turkey in late June. NATO is also setting up a new multinational corps headquarters in the region. Nervous about U.S. waning commitment to NATO, other alliance members are eager to keep Turkey onside. Europe is indulging Mr. Erdogan even as he continues to snuff out Turkey's democracy. Other than Germany, no NATO government has addressed -- let alone condemned -- President Erdogan's mounting attacks against his political opponents.

Relations with the U.S. appear to be improving. Earlier this year, the U.S. withdrew troops from Syria, where they fought alongside Kurdish fighters that Turkey considers terrorists. This withdrawal removed an important source of friction. President Erdogan lapped up suggestions by the U.S. ambassador that Turkey may at last receive F-35 fighter jets it ordered a decade ago. The U.S. shelved the sale in 2019 after Turkey bought an S-400 air-defense system from Russia.

In August, Turkey, Saudi Arabia and Pakistan signed a joint defense agreement - the Mecca Agreement - under which an armed attack against any of them would be deemed an attack against them all. Turkey also maintains the Qatar–Turkey Combined Joint Force Command in Doha, with an estimated 3,000 troops stationed there, and a Somali Turkish Task Force Command in Mogadishu, with more than 500 troops. Turkey and its Arab allies increasingly view Israel's military operations in the region as destabilizing. The tension between the two countries is real. Turkey, a mostly Muslim country, fumes over Israel's ill-treatment of Palestinians. Israel accuses Turkey of harboring leaders of Hamas, which attacked Israel on October 7th, 2023. Each thinks the other threatens its borders. Israel has fostered ties with the Kurds, including some that Turkey's government (ever wary of Kurdish nationalism) sees as enemies.

President Erdogan will continue to dominate Turkish politics until at least the 2028 elections, through a mix of authoritarianism, control of state resources and bureaucracy, and a largely supportive domestic media. He is likely to remain in power beyond 2028, despite being constitutionally barred from serving another term.
Turkey's foreign policy choices, including deepening ties with Russia, continue to increasingly clash with those of the U.S. and the EU. Nonetheless, Turkey is expected continue to pursue a pragmatic and transactional relationship with the U.S. and the EU.

Since August 2025, Turkey has faced U.S. 15% tariffs, (50% on steel and aluminum) on most of its exports to the U.S. Turkey's limited trade exposure to the U.S. means that the effects of tariffs will be manageable. However, some sectors, including cement, textiles and auto parts, will be more affected.

Current foreign exchange reserves are relatively stable; and with ongoing support from the IMF, multilateral institutions and international banking, the country has managed to service its foreign obligations within agreed terms in recent years, while financing both its budget and current account deficits. The expectation is that it will continue to do so without difficulty over the next four years.

The Turkish construction and engineering sector stands to benefit from rebuilding and expansion projects that will be pursued across the Middle East over several years.

India

India hosted the BRICS summit on September 12th &

13th. China's Xi Jinping attended, making his first visit since China and India fought deadly border clashes in 2020. It also marks the culmination of years of careful diplomacy to thaw relations between the world's two most populous nations. The neighboring countries have been at odds for decades, even as their growing importance to the global economy has raised the stakes for both.

Relations hit a low following the 2020 clashes in the Himalayas, when 20 Indian soldiers and an unknown number of Chinese troops were killed, and dozens more injured. Political dialogue between both countries faltered, engagement plunged and trade and investment fell.

However, since then, President Xi and PM Modi have pursued a tentative rapprochement at regional forums. Xi's attendance at the BRICS summit in New Delhi was not only be his first visit in seven years, but a showcase for attempts to set aside disagreements and project a more unifying global role, as the U.S.-Iran conflict continues. The structural differences and strategic trust deficit in their bilateral relations are significant, therefore multilateral forums such as BRICS provide a platform for managing the challenges between both countries.

Led by officials including the Chinese foreign minister and key Modi advisers including security officials, and India's foreign minister, both sides have been slowly warming to one another. This year, trade negotiators held their first bilateral meeting since 2019. Soon after, India authorized two large state-owned companies to procure critical components from China, lifting restrictions imposed in 2020. Bilateral trade between China and India last year rose 12.4% to a record $155 billion, more than double the $71.6 billion reported a decade earlier. In the first seven months of 2026, bilateral trade increased a further 23% compared with the same period a year ago.

Investment flows are also picking up. Over the past 18 months, Chinese companies in the technology and energy sectors have increasingly scoped opportunities in India, including cleantech developer Envision, Geely-backed engine supplier Horse Powertrain and battery maker Cos MX. In March, the Modi administration moved to relax screening of Chinese investments in solar energy and electronics sectors.

A tentative change in foreign investment rules means Chinese companies will gain automatic clearance for non-controlling stakes of up to 10% in Indian entities. In 2024, the two countries agreed to resume patrols of their 3,500km border, which was suspended after the clashes in 2020. They also resumed direct flights last year for the first time since 2020, and this year reopened border trade at three Himalayan crossings and jointly organized a Hindu and Buddhist pilgrimage to sacred sites in Tibet. The cautious re-engagement is bringing both countries back to a regional rivalry dressed in competition and co-operation which dates back decades. A thaw in the relationship has begun, because Prime Minister Modi has spent a lot of political capital on China.

The University of Hong Kong's Centre on Contemporary China and the World, identified clear and positive signs of détente. This coincides with the tumultuous period in U.S. foreign policy, which has frayed relations with India- which had been pursuing a closer relationship with Washington.

Beijing appears hopeful that India can be pulled further from U.S. influence while offering China's slowing economy a large potential market for its companies. China views India as being in a period of adjustment because of U.S. policies, so the outreach and measures to improve ties are geared towards pulling New Delhi closer to China. This will help shape India's strategic choices and persuade India from viewing China as a threat. That would move India away from siding with the U.S. by default because of China.

In India, there is still resistance towards Chinese participation in sensitive sectors, including IT and electronics. Meanwhile, China remains wary of India becoming an alternative for global export manufacturing as the country is not pivoting away from its efforts to strengthen domestic manufacturing to compete with China. For example, by wooing Apple to make iPhones and designing and producing semiconductors in India.

Despite Beijing having agreed to address New Delhi's requests during negotiations a year ago, Indian companies still struggled to secure Chinese licenses that allowed shipments of rare earth magnets and industrial machinery, according to diplomats.

India appears to be embracing a form of competitive coexistence with China. It is accepting China as a long-term rival, while strengthening engagement to prevent competition from hardening into perpetual confrontation.

Germany

Germany faces prolonged economic stagnation amid structural pressures that will shape the outlook for years to come. The German economy has stalled since the pandemic, with real GDP almost unchanged from end-2019 levels, making it the worst performer among G7 members over this period.

The prolonged weakness stems from high energy costs acting as a drag on its large industrial sector, substantial exposure to external demand fluctuations (with exports accounting for nearly 50% of GDP), and intensifying trade pressures. U.S. import tariffs are adding to industrial headwinds, whilst Chinese competition has become increasingly severe, particularly in the automotive sector where German carmakers struggle with price competitiveness and the sophistication of electric vehicles.

However, medium-term prospects have brightened. A landmark reform of Germany's previously restrictive debt-brake framework has expanded fiscal space, and the government is deploying new infrastructure and defense spending to revive demand. This could trigger a consumer spending rebound when confidence returns, though significant uncertainties remain about implementation given repeated delays to public investment projects.

Germany confronts deep structural challenges that constrain long-term growth. An aging population and declining working-age population will likely steadily erode headline growth and government revenues, with labor shortages becoming increasingly pressing over the next decade. The country has lagged in digitalization and supply-side reform, and its previous heavy reliance on Russian energy and Chinese trade has exposed vulnerabilities in its growth model. Chinese competition in advanced industrial sectors, particularly automotive, represents an ongoing threat to Germany's export competitiveness.

Germany has maintained a strongly centrist and consensus-based political culture, supporting relatively effective policymaking. The Christian Democratic Union's (CDU's) largest share of the vote in the 2025 parliamentary election provided conditions for effective political bargaining and coalition management.

Now, that is changing. The populist-right Alternative for Germany (AfD) party won a staggering 44% of the vote in this month's state election: its best-ever score, and better than polls predicted. The AfD was dominant among most segments of the electorate, excluding the elderly. A record-breaking turnout, projected at over 75%, fell in the party's favor; exit polls suggested that over half of the AfD's growth since the last election in 2021 came from mobilizing non-voters. There is no denying the depth of the defeat inflicted on the center-right Christian Democratic Union (CDU), which leads both the federal government and the coalition in Saxony-Anhalt. The mood among CDU leaders is decidedly subdued. The CDU's vote share halved to 17%, presumably in part because of tactical anti-AfD votes shifting to the Social Democrats and Greens to nudge them over the 5% threshold to enter parliament. Both, especially the Greens, outperformed expectations.

Germany's chancellor Friedrich Merz has had a difficult time in recent months, and his approval rating is at a record low. The state elections in September will add to the challenges he faces, and the growing speculation about a possible change of leadership. This remains unlikely this year, but the risks will persist in 2027. Mr. Merz currently has the worst approval ratings of any democratic leader of a major economy.

Of course, beneath these issues around political management and communication there are also structural underpinnings. The long awaited economic upswing is taking time to emerge, the state is struggling to spend its massive infrastructure fund effectively, and politicians are trying to agree reforms in sensitive areas such as healthcare and pensions which, although arguably necessary, are not popular.

Although Germany's traditional political parties, the CDU/CSU, together with the SPD, would in theory have sufficient votes to elect a successor, in practice, the secret ballot can result in unpredictable outcomes. Any risk that the ballot will not turn out the desired successor could result in a collapse of the government and a new election. Neither of Germany's traditional political parties will want to take that chance.

Meanwhile, German auto and steel manufacturers are eliminating thousands of jobs as part of a wide move to cut positions under extreme pressure from Chinese goods which have rendered German produced goods increasingly uncompetitive.

Automakers such as Volkswagen and Mercedes Benz are cutting the number of managers on their respective payrolls. VW's initial program was to cut 50,000 jobs in Germany in manufacturing and back-office roles across the VW and Audi brands, and its software unit Cariad. That didn't go far enough, and an internal analysis found administrative costs were 30% above the level of other auto manufacturers around the world. The difference is largely driven by the complexity of the group structure across all levels. Even if VW does ultimately cut 100,000 jobs (unlikely because of union opposition) – the group would still employ approximately 580,000 people, well above Toyota's 390,000 and the 335,000 employed by South Korea's Hyundai.

At Porsche, the latest restructuring measures come in addition to an existing plan to reduce headcount by 3,900, including 2,000 temporary workers employed in factories. Porsche says it experienced disproportionate growth in indirect areas. Management says it is now intervening and making "disproportionate reductions" in those areas.

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