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International Economy: Did Someone Say "Resilience"?

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Editorial

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Did Someone Say "Resilience"?

Shock after shock, the global economy continues to surprise observers with its "resilience," particularly when assessed through the lens of GDP growth. Indeed, the same term was already used in this editorial last January.

If the ongoing discussions between the United States and Iran regarding the Strait of Hormuz crisis reach a successful conclusion (within the 60-day period starting on June 17) and result in a lasting agreement, the International Energy Agency (IEA) once again forecasts an oil supply surplus as early as 2027. Inflation expectations could then rapidly become reanchored at levels more consistent with central banks' targets. Under such a scenario, and although a return to normal operations for the Gulf's oil and gas infrastructure would still require several months, monetary policy could gradually ease again as confidence in the disinflation process strengthens.

In this regard, the IMF's latest forecasts (April 2026) outline a baseline scenario in which global growth reaches 3.1% in 2026 and 3.2% in 2027, while growth in emerging market and developing economies (EMDEs) would be only marginally affected (3.9% in 2026 instead of the 4.0% projected last October, and 4.1% in 2027). Even under its most severe scenario, the IMF does not foresee global growth falling below 2% in 2026—supported in particular by strong carryover effects from the second half of 2025—and projects growth of around 2.2% in 2027. Admittedly, these would represent historically low levels over two consecutive years, yet the global economy would avoid recession, unlike in 2009 or 2020.

So, under this baseline scenario—which still appears somewhat optimistic at the time of publication—would the shock amount to little more than a temporary warning before a return to normal conditions? Probably not, for at least three reasons.

First, the global growth rate conceals substantial regional disparities. The economies of the United States, China, and India now account for between 45% and 50% of global GDP. As a result, the resilience of global growth depends heavily on the United States among advanced economies (the euro area's growth rate is roughly half as high, at 1.1%) and on the two Asian demographic giants among emerging economies. While Sub-Saharan Africa continues to perform relatively well (with projected growth of 4.3% in 2026), the Middle East (1.9%) and Latin America (2.3%) are less dynamic. Asia has been unevenly affected by the inflationary shock and supply-chain disruptions. Although national growth rates remain high across the region, some countries—including Cambodia, Vietnam, and even India—are likely to lose approximately one percentage point of growth this year. Global growth is therefore resilient overall, but the impact of the shock remains highly uneven across countries and regions.

Second, sovereign bond yields appear to have increased on a lasting basis, particularly the risk-free component[1] and the long end of the yield curve, irrespective of monetary policy decisions in the months ahead. Consequently, both public and private actors must now contend with significantly higher borrowing costs to finance future investment and fiscal deficits. This is, moreover, one of the distinctive features of the current shock: it has had a more pronounced impact on financing rates in advanced economies than on the risk premia paid by emerging economies. Are we witnessing the early

[1] Between February 27 and June 9, U.S. 10-year government bond yields increased by 56 basis points, reaching 4.53%, while German 10-year yields rose by 41 basis points to 3.05% (source: EIU).

stages of a more structural convergence in interest rates between advanced and emerging economies? In any case, economic growth is likely to be affected by higher long-term interest rates, should this trend persist.

Finally, after a year in 2025 that had already significantly undermined the principles of multilateralism, the rules of international law, and certain long-standing alliances, the attacks on Iran have paved the way for geopolitical postures that would have been almost unimaginable just two years ago. And while the G7 summit that concluded in Évian on June 17 surprised observers by demonstrating the participants’ ability to agree on the objective of addressing global imbalances and renewing support for Ukraine, questions remain regarding the actual impact these conclusions will have on the key third parties concerned—namely China and Russia. In a context of persistently heightened geopolitical uncertainty, where the G7 alone can no longer resolve global crises, how will economic growth evolve over the long term?

Perhaps, then, more than the resilience of economic growth, the central question today is becoming that of the resilience of global governance itself.

International Economy

Withstanding the Perma-Shock, from the Mar-a-Lago Golf Course to the Persian Gulf

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The notion of a crisis is often used indiscriminately and/or conflated with that of a shock.[2] To date, the global economy has proven remarkably resilient in the face of the succession of shocks since 2020, including in 2025 amid the "universal" trade war launched by the second Trump administration (see Table 1). To such an extent that the current situation could be described as one of economic "perma-shock", rather than "perma-crisis".[3] At the same time, however, the global economic and institutional order is experiencing a profound model crisis, undermined by the strategic rivalry between the United States and China, further fueled by Russia's ambitions. This has weakened multilateralism and disrupted segments of global value chains.

In the face of the energy shock resulting from the closure of the Strait of Hormuz, emerging markets have once again remained resilient, with sovereign risk premia declining since the outbreak of the United States–Israel–Iran conflict on February 28, 2026, following a modest uptick in March. Investors appear to view both the conflict and its economic repercussions as manageable from a macro-financial perspective, with inflationary pressures expected to remain less severe than those experienced in 2022. Emerging market and developing economies (EMDEs) generally maintain relatively strong external positions, particularly in terms of foreign exchange reserves, enabling them to absorb pressure on their currencies. The hydrocarbon-importing countries most exposed to supply disruptions through the Strait of Hormuz are located in Asia, which also includes the region's most macroeconomically resilient economies. This broad assessment does not, however, apply uniformly across all countries, particularly the most fragile economies.

Overall, the factors likely to destabilize the global economy and heighten macro-financial risks have become even more pronounced over the short and medium term than they were in 2025:

- **Failure to implement the United States–Iran agreement following the 60-day negotiation period established under the Memorandum of Understanding (MoU) signed on June 17, resulting in the closure of the Strait of Hormuz beyond the summer and increasing the risk of global stagflation:** a sustained rise in oil prices as global shortages emerge following the depletion of inventories; similar developments affecting natural gas, fertilizers, and other products exported by Gulf countries (aluminum, helium, bromine), all of which are critical inputs for a number of industrial value chains.
- **Adverse macroeconomic, socio-economic, and potentially political consequences of this new global shock for EMDEs, compounded by the effects of a new El Niño episode in 2026-2027:** pressure on balance-of-payments positions (current account balances, capital flows, foreign exchange reserves, and exchange rates) and public finances (subsidies and social spending); monetary tightening (in response to inflation and exchange rate pressures); food insecurity and social unrest, **against a backdrop of declining official development assistance (ODA).**
- **Heightened geopolitical tensions:** continuation of the United States power-based approach (including intervention in Cuba and elsewhere, in line with developments in Venezuela) and a further escalation of Chinese pressure on Taiwan (control over the Taiwan Strait and disruption of semiconductor exports); increased risk of open military confrontation (United States–China in the South China Sea, Russia–European Union, and other regional conflicts).
- **Declining effectiveness of multilateral institutions** in resolving economic, political, and humanitarian crises.
- **Continuation of the trade war, particularly between China and the United States:** the Trump administration circumventing court rulings invalidating tariffs by invoking alternative legislative provisions and expanding the use of non-tariff barriers, following practices already employed by China (export licensing controls, bans, quotas); a more assertive

[2] A shock is a sudden event or disruption affecting a system. A crisis is a persistent state of dysfunction resulting either from a shock that has not been adequately absorbed or from pre-existing vulnerabilities. The shock is the immediate cause, whereas the crisis is the systemic consequence.

[3] The term "permacrisis" refers to a situation in which crises are no longer perceived as exceptional and temporary episodes, but rather as a permanent state of crisis. The expression was selected as the Collins Dictionary Word of the Year in 2022. A permacrisis differs from a polycrisis, which refers to a situation in which several distinct crises overlap and reinforce one another.

European Union response through retaliatory measures targeting U.S. technology and digital services, while simultaneously protecting its industries against Chinese competition, which is accelerating deindustrialization (Anti-Coercion Instrument, quotas, regulatory standards, the Carbon Border Adjustment Mechanism, and the Deforestation Regulation triggering retaliatory measures).

- **A slowdown in the Chinese economy,** a central player in Asian—and global—manufacturing value chains as well as in global commodity markets.
- **The risk that Donald Trump could challenge the outcome of the November midterm elections should the results prove unfavorable, while also undermining the independence, credibility, or even the monetary sovereignty of the Federal Reserve (Fed),** now chaired by Kevin Warsh, as it confronts a monetary policy dilemma in a context of fiscal dominance. Such a dilemma could also extend to other advanced and emerging economies given the scale of public deficits and government debt.
- **A correction in financial markets—or even the bursting of the AI-driven technology bubble—and/or a U.S. bond market crash triggered by a crisis affecting non-bank financial institutions (NBFIs),** which are subject to lighter regulation than the banking sector, or stablecoins backed by U.S. Treasury securities.
- **Consequences for the global decarbonization trajectory stemming from the United States' withdrawal from the Paris Agreement.**

Table 1 – Overview of the successive shocks since 2020

2020	COVID-19 pandemic, global lockdowns, collapse of trade and transportation
2021	Supply chain disruptions, shortages, surge in freight costs
2022	Russia's invasion of Ukraine, energy and food shock
2023	Global inflation, monetary tightening (plus the regional banking crisis in the United States)
2024	No major global shock
2025	"Universal" trade war, rising geopolitical tensions
2026	U.S. interventionist policy (Venezuela, Cuba), war in the Middle East, and energy shock (closure of the Strait of Hormuz and destruction of energy infrastructure)

Source: AFD.

Table 2 – IMF economic growth projections (%, baseline scenario)

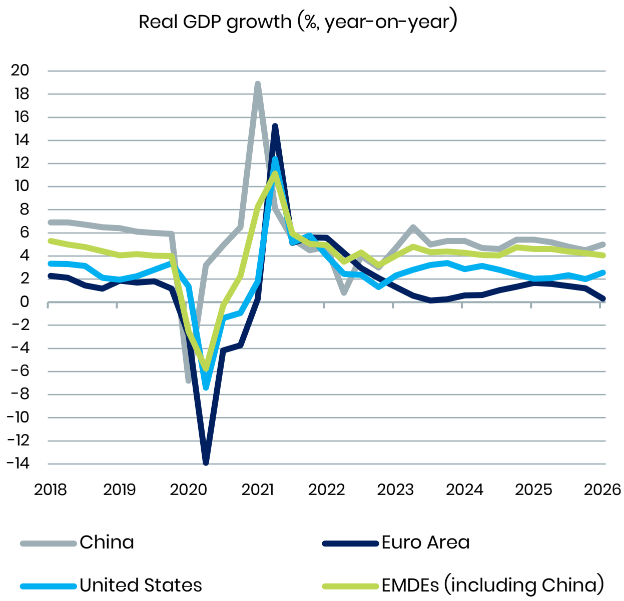
Region/Country	2025 (Oct. 2025)	2025 (Apr. 2026)	2026 (Oct. 2025)	2026 (Apr. 2026)	2027 (Apr. 2026)
World	3.2	3.4	3.1	3.1	3.2
Advanced Economies	1.0	1.9	1.6	1.8	1.7
United States	2.0	2.1	2.1	2.3	2.1
Euro Area	1.2	1.4	1.1	1.1	1.2
Emerging Market and Developing Economies	4.2	4.4	4.0	3.9	4.2
Asia	5.2	5.5	4.7	4.9	4.8
China	4.8	5.0	4.2	4.4	4.0
India	6.6	7.6	6.2	6.5	6.5
Latin America	2.4	2.4	2.3	2.3	2.7
Brazil	2.4	2.3	1.9	1.9	2.0
Mexico	1.0	0.6	1.5	1.6	2.2
Colombia	2.5	2.6	2.3	2.3	2.5
Middle East, North Africa, and Central Asia.	3.5	3.6	3.8	1.9	4.6
Türkiye	3.5	3.6	3.7	3.4	3.5
Morocco	4.4	4.9	4.2	4.9	4.5
Egypt	4.3	4.4	4.5	4.2	4.8
Sub-Saharan Africa	4.1	4.5	4.4	4.3	4.4
Nigeria	3.9	4.0	4.2	4.1	4.3
South Africa	1.1	1.1	1.2	1.0	1.3
Kenya	4.8	4.9	4.9	4.5	4.7

Source: IMF (World Economic Outlook).

Successive shocks since 2020

The COVID-19 pandemic and the wars in Ukraine and the Middle East have each generated major supply shocks for the global economy. However, only the pandemic period can be characterized as a global economic crisis, marked by a deep recession resulting from the combination of a demand shock and a supply shock (see Figure 1). It is worth recalling that these recent shocks followed three financial shocks since the beginning of the century (including the bursting of the dot-com bubble in 2000), two of which evolved into full-fledged economic and financial crises. The first was the global and systemic crisis triggered by the collapse of the U.S. subprime mortgage bubble in 2007–08. The second, more localized and stemming from the first, materialized as the European sovereign debt crisis between 2010 and 2013. Subsequently, the global economy experienced an oil price collapse beginning in mid-2014, marking the end of the commodity supercycle that had started in 2003. The sharp decline in oil prices, driven by a global supply glut (the expansion of U.S. shale oil production and OPEC's decision not to cut output), coincided with a slowdown in global demand, associated in particular with the onset of China's structural economic slowdown.

Figure 1 – Global growth has remained resilient despite successive shocks

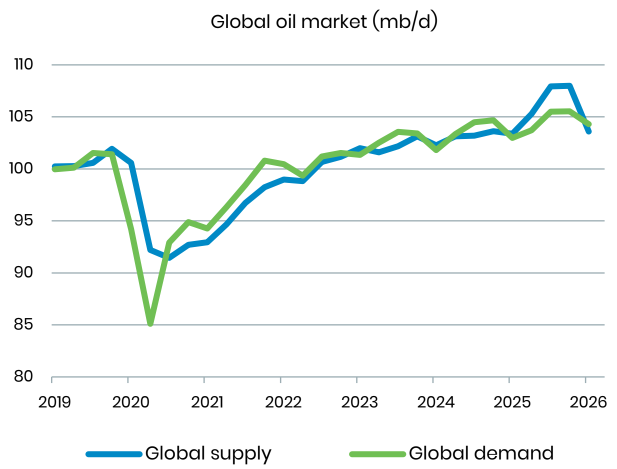


Source: IMF, Oxford Economics, AFD calculations.

A huge energy shock in 2026, in a structurally oversupplied market

Since 2024, the International Energy Agency (IEA)[4] has considered the global oil market to have entered a phase of structural excess capacity, although geopolitical tensions may still trigger temporary price spikes. Between 2024 and 2030, global oil production is projected to increase by 5.1 million barrels per day (mb/d), while demand is expected to rise by only 2.5 mb/d. Before the outbreak of the conflict, the global energy market was characterized by bearish fundamentals: high inventories, moderate demand growth, and abundant supply, supported by the Trump administration's "drill, baby, drill" strategy, the recovery of Venezuelan oil production following the U.S. intervention in January, rising production in Brazil and several African producers, and OPEC+'s decision—announced in June 2026—to increase production quotas in order to regain market share. The average Brent price of USD 74 per barrel in 2024–25 appeared to represent a near-equilibrium level balancing the interests of both exporters and importers. Shipping markets had already begun pricing in rising geopolitical risks and the possibility of escalation between the United States and Iran in early 2026, but markets only fully reassessed these risks following the effective closure of the Strait of Hormuz on February 28, 2026 (see Figure 2).

Figure 2 – A global oil market now structurally oversupplied



Source: OECD.

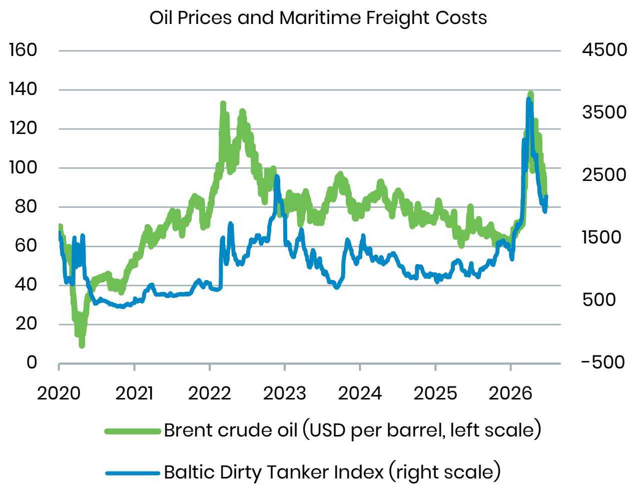
As early as March 2026, the IEA described the consequences of the Middle East conflict as the largest supply disruption in the history of the global oil market. Brent crude

[4] See: International Energy Agency (IEA). 2025. *Oil 2025. Analysis and forecast to 2030*. Paris: IEA. https://www.iea.org/reports/oil-2025.

prices rose from USD 71 to USD 138 per barrel within a month before retreating following the ceasefire announced on April 8. Prices nevertheless remained volatile before stabilizing below USD 100 per barrel in late May and early June. They subsequently fell back to pre-conflict levels, below USD 80 per barrel, following the announcement of the U.S.–Iran agreement on June 14 and the prospect of the reopening of the Strait of Hormuz (see Figure 3). Maritime freight costs also eased (-45%, following an 84% increase between late February and early April), although war-risk insurance premiums increased ten- to twentyfold on certain shipping routes. According to the IEA's latest report, published in May,[5] global oil supply had declined by 12.8 mb/d since February, with production from the Gulf countries (Saudi Arabia, Iraq, Iran, the United Arab Emirates, Kuwait, and Qatar) standing 14.4 mb/d below its pre-war level (25 mb/d, representing nearly one-quarter of global production). According to OPEC data, production by the twelve-member cartel (including the UAE) fell by 34% between late February and the end of May 2026 (see Figure 4). Global supply was partially preserved through: (i) increased exports from other producing countries (+3.5 mb/d), mainly the United States, Canada, Brazil, Kazakhstan, Russia (following a temporary exemption from U.S. sanctions), and Venezuela; (ii) the rerouting by Saudi Arabia and the United Arab Emirates (which withdrew from OPEC on May 1, 2026) of part of their exports; (iii) the coordinated release, on March 11, of an unprecedented 400 million barrels from the strategic petroleum reserves of the IEA's 32 member countries; and (iv) the continued transit through the Strait of Hormuz of tankers belonging to the Iranian and Russian "shadow fleets."

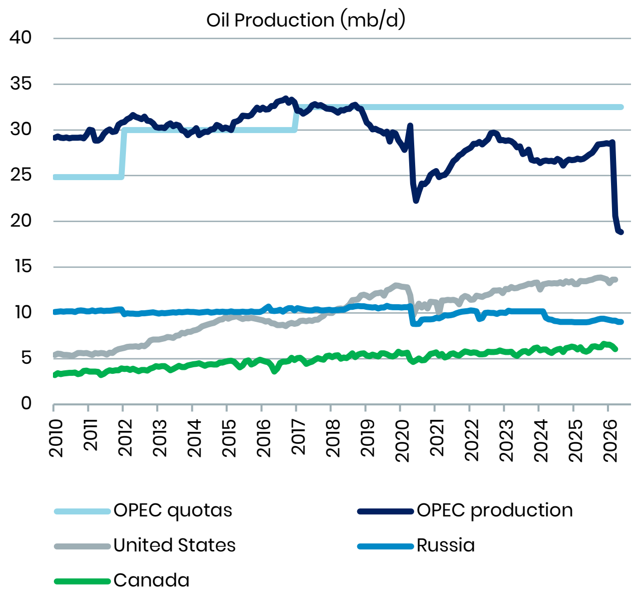
At the same time, several countries significantly reduced their oil imports, notably China (which had accumulated large inventories in previous months), Japan, South Korea, and India. Member states of the Association of Southeast Asian Nations (ASEAN) rapidly diversified their import sources by turning to alternative suppliers such as Brunei, Libya, the United States, Angola, Argentina, and Côte d'Ivoire. Although the United States has become a net exporter of hydrocarbons thanks to the rapid expansion of liquefied natural gas (LNG) exports, particularly to Europe, it remains a net importer of crude oil, importing 2.2 mb/d in 2025 according to the IEA. The "drill, baby, drill" strategy has boosted U.S. light crude production but also raises questions regarding the adequacy of domestic refining capacity that are better suited to processing heavy crude oil.

Figure 3 – Sharp spike and rapid easing in oil prices and maritime freight costs



Source: Energy Information Administration, Baltic Exchange.

Figure 4 – Sharp decline in OPEC production since March 2026



Source: JODI, OPEC (data through May 2026).

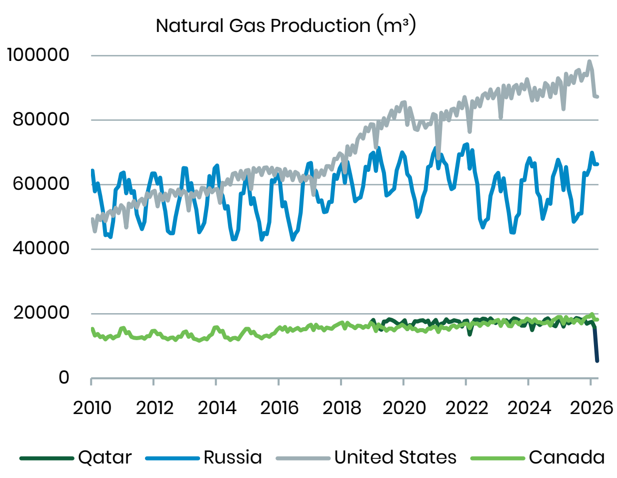
[5] IEA. 2026. *Oil Market Report - May 2026*. Paris: IEA. https://www.iea.org/reports/oil-market-report-may-2026.

According to the IEA, assuming a gradual resumption of oil flows from June onward, global oil supply is expected to decline by an average of 3.9 mb/d in 2026, reaching 102.2 mb/d, while global demand is projected to contract by 420,000 barrels per day in 2026 relative to 2025, to 104 mb/d—1.3 mb/d below its pre-conflict level. Even the reopening of the Strait of Hormuz would not be sufficient to restore normal conditions in the global oil market for several months, given the extensive destruction of oil and gas infrastructure. Refinery throughput could therefore decline by 4.5 mb/d in the second quarter of 2026, to 78.7 mb/d, and by 1.6 mb/d over 2026 as a whole, averaging 82.3 mb/d.

The implications of reopening the Strait of Hormuz extend well beyond oil. Before the conflict, the Gulf countries accounted for 31% of global LNG supply, 34% of global urea and sulfur production used in fertilizer manufacturing, 33% of helium production, twice the global production of bromine—both essential inputs for semiconductor and electronic chip manufacturing—and 8% of global aluminum production. The region also serves as a major logistics hub, handling approximately 15% of global air freight and passenger traffic. In the natural gas market, the closure of the Strait of Hormuz temporarily removed nearly 20% of global LNG trade from the market, despite the emergence of semi-clandestine maritime shipping routes. **According to the IEA, however, the main issue is the likely loss of around 15% of the additional LNG volumes expected over the 2026–30 period**, owing to damage sustained by Qatari facilities that has durably reduced liquefaction capacity. This shortfall is unlikely to be offset in the near term by the structural expansion of LNG projects in the United States and Canada (see Figure 5).

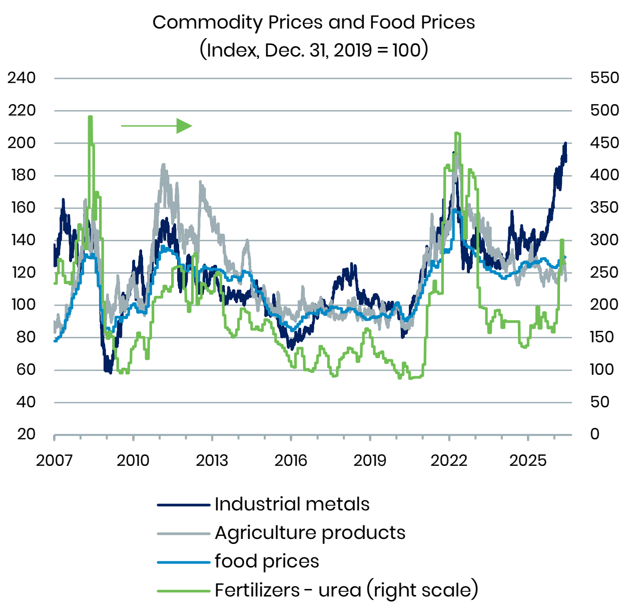
Nevertheless, the IEA's baseline scenario[6] remains one of progressively improving market conditions from late 2026 and throughout 2027. This outlook reflects growing demand from Europe, driven by declining pipeline gas imports and heightened energy security needs, as well as increasing demand from Asia, particularly China. Urea prices—urea being a nitrogen fertilizer produced from ammonia, itself manufactured primarily using natural gas—rose by 55% within a few weeks before easing by 12% in May, although they remained well below the peaks reached during the previous food price shocks of 2008 and 2022 (see Figure 6). Urea is often the main transmission channel through which higher energy prices feed into food prices, with potentially significant effects on the 2026–27 harvests.

Figure 5 – ...and in natural gas, particularly in Qatar



Source: JODI (data through March 2026).

Figure 6 – Broad-based increase in commodity prices



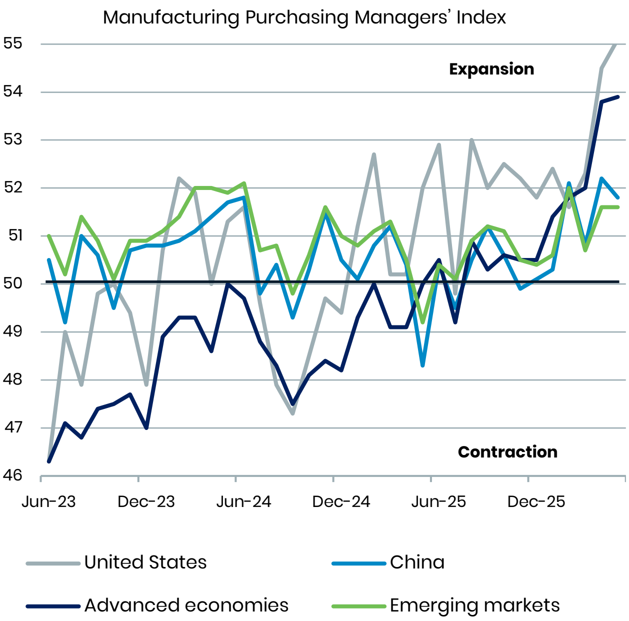
Source: S&P, FAO, IMF, AFD calculations.

[6] IEA. 2026. *Gas Market Report, Q2-2026*. Paris: IEA. https://www.iea.org/reports/gas-market-report-q2-2026.

The global economy remains resilient

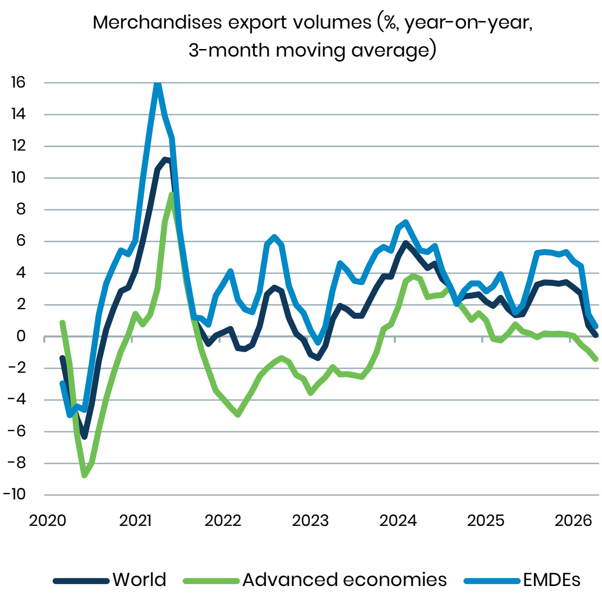
In 2025, in anticipation of the tariff shock, exporting and importing firms brought forward their activity during the first half of the year. In 2026, in response to the conflict in the Middle East and the closure of the Strait of Hormuz, firms similarly accelerated purchases during April and May, particularly in advanced economies (see Figure 7). The rebound in the Purchasing Managers' Index (PMI) was partly artificial, as firms frontloaded purchases to hedge against risks affecting energy supplies and transportation. By contrast, the contraction continued in several major emerging economies—notably Brazil, Mexico, and Türkiye—in line with the decline in their manufacturing output. At the global level, manufacturing output expanded broadly in line with economic growth in 2025, increasing by 3.1% year-on-year (y/y), including 1.2% in advanced economies and 4.4% in EMDEs. This momentum continued in the first quarter of 2026 (+3.2% y/y), despite the weak performance of the European Union (-1.6%), largely driven by Germany. Partial data available for April point to continued resilience in the United States (+1.3% y/y) and a slowdown in China to 4.0% y/y, despite the sustained dynamism of high-technology industries. At the same time, global merchandise exports in volume terms remained broadly flat over the preceding three months (y/y comparison), with advanced economies recording a 1.4% contraction in April (see Figure 8). Against the backdrop of the closure of the Strait of Hormuz, the global export price index rose by 6.5% y/y in March 2026, approaching the peak reached in June 2022. **In nominal terms, exports therefore increased significantly during the first quarter of 2026, particularly in the United States (+12% y/y), where crude oil exports reached record levels in April (reflecting both price and volume effects), and in China (+14.7%, mainly driven by volume effects), while exports contracted sharply in the euro area (-6.4%).**

Figure 7 – Firms have accelerated purchases since the closure of the Strait of Hormuz



Source: S&P Global.

Figure 8 – Decline in merchandise export volumes

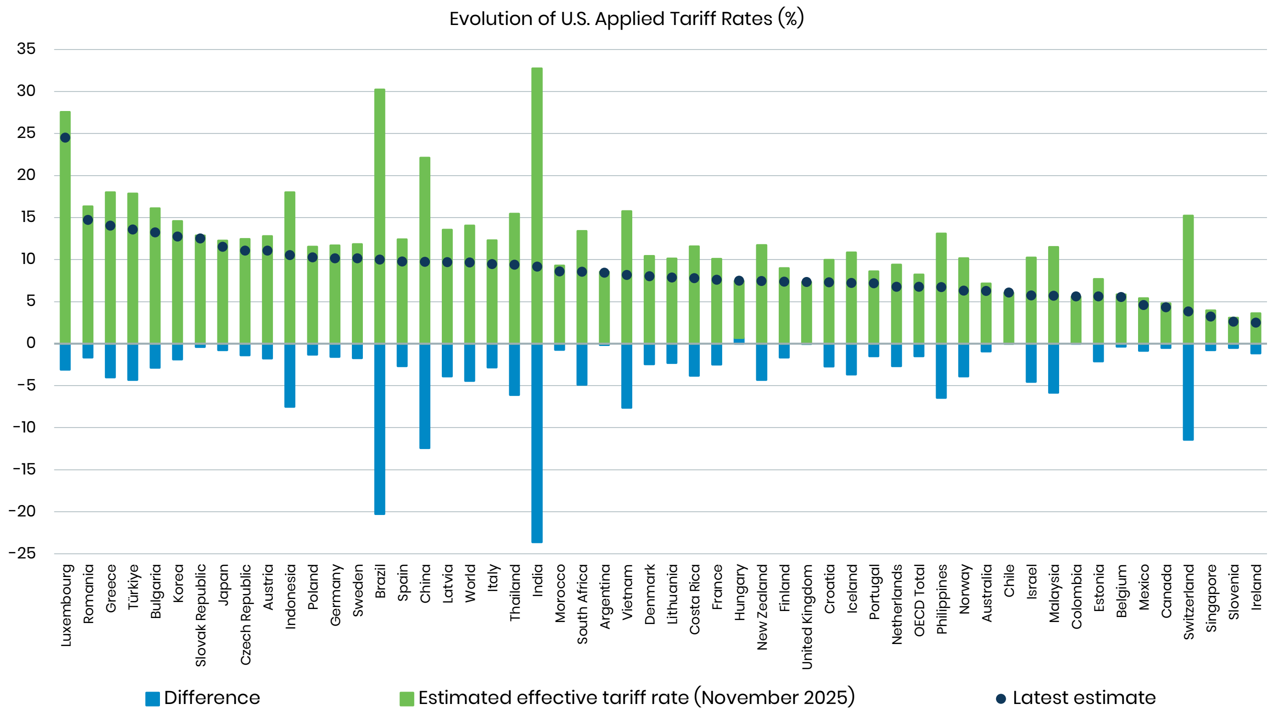


Source: IMF, AFD calculations.

The trade confrontation continues at lower intensity

The trade war has been overshadowed by the conflict in the Middle East. Since late 2025, the signature of several bilateral agreements between the United States and its trading "partners", notably China, appears to have initiated a degree of de-escalation. Nevertheless, the threat of renewed tariff and non-tariff hostilities remains very real. After the U.S. Supreme Court ruled on February 24, 2026, that the Trump administration had improperly relied on emergency powers under the *International Emergency Economic Powers Act* (IEEPA)[7] to impose the generalized tariffs announced on April 2, 2025, the administration has nevertheless continued to pursue its trade agenda (see Figure 9). Since February 24, it has imposed an additional tariff of between 10% and 15% under Section 122 of the *Trade Act* of 1974, which provides for temporary measures to address balance-of-payments difficulties. In early June, the administration also announced two new tariff proposals under Section 301 of the *Trade Act* of 1974, targeting what it considers unfair foreign trade practices. These include a proposed 25% tariff on imports from Brazil and additional duties of 10% or 12.5% on imports from around sixty countries—including the European Union and China—partly justified on the grounds of forced labor. According to *Global Trade Alert*,[8] approximately 43% of U.S. imports would remain exempt from these measures. For its part, the Peterson Institute for International Economics (PIIE)[9] argues that this use of Section 301 is highly likely to be struck down by the courts.

Figure 9 – Downward adjustment of U.S. Tariff rates following the supreme court ruling



Source: OECD (June 2026).

[7] This federal law authorizes the President to regulate trade during a national emergency in response to a foreign threat.

[8] See: https://globaltradealert.org/.

[9] See: https://www.piie.com/blogs/realtime-economics/2026/us-reciprocal-trade-deals-built-push-americas-trade-partners-away?utm_source=update-newsletter&utm_medium=email&utm_campaign=piie-insider.

According to the PIIE, by early June nine countries had signed bilateral Agreements on Reciprocal Trade (ARTs) with the United States: Argentina, Bangladesh, Cambodia, Ecuador, El Salvador, Guatemala, Indonesia, Malaysia, and Taiwan. These agreements represent a hybrid arrangement combining elements of preferential trade agreements with economic security partnerships, against the broader backdrop of U.S. efforts to reduce China's economic influence. Mexico and Canada have officially proposed extending the United States–Mexico–Canada Agreement (USMCA)[10] through 2042. Although the North American trade agreement is currently set to remain in force until 2036, it is subject to a mandatory joint review in July 2026. The Trump administration is seeking to renegotiate several provisions of the agreement, notably rules of origin, trade imbalances, and selected issues relating to investment and supply chains.

China: a cold sun

China's centrality in the global economy does not necessarily translate into attractiveness. Beijing continues to pursue its strategy of influence without interference through economic partnerships that stop short of formal alliances—including with Russia and Iran—allowing it to maintain a posture of apparent neutrality and remain largely in the background of the conflicts in Ukraine and the Middle East. China has thus positioned itself as a defender of free trade, multilateralism, and EMDEs. At the same time, however, its actions in the South China Sea and its increasing pressure on Taiwan continue to pose significant risks to regional—and potentially global—stability. On May 2, 2026, the Chinese authorities issued an order prohibiting compliance with U.S. sanctions targeting five Chinese oil refining companies, in response to measures related to their oil transactions with Iran. On May 8, China officially eliminated tariffs on imports from 53 African countries through April 30, 2028 (Eswatini being the only exception because of its diplomatic relations with Taiwan). The U.S.–China summit held on May 14–15 may best be described as one of cautious détente, or a "cold peace." Both powers sought to prevent any further deterioration in their economic relationship, yet the underlying disagreements remain unchanged with respect to trade, technology, security, and geopolitical rivalry, particularly over Taiwan.

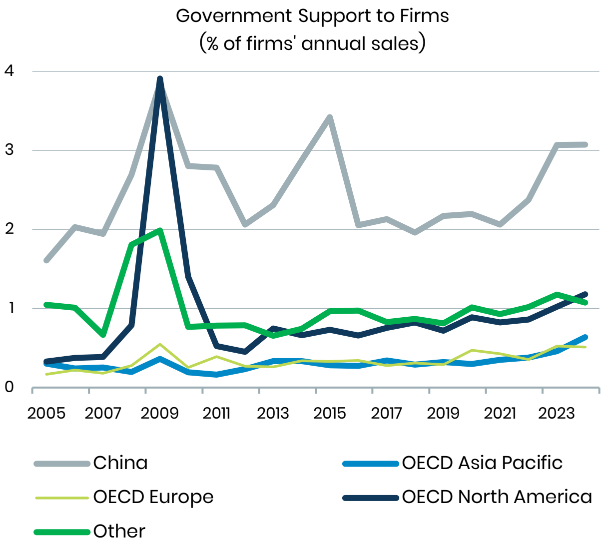
According to a recent OECD study,[11] Chinese firms received, on average, between three and eight times more public support than firms in OECD countries over the 2005–24 period (see Figure 10). The OECD estimates that approximately 22% of the global market share gains achieved by the firms included in the study can be attributed to public subsidies; for Chinese firms, this figure rises to 60%. Public support—including direct subsidies, tax incentives, preferential access to land, concessional lending, and other forms of state assistance—has enabled Chinese firms to expand their global market shares without generating commensurate improvements in productivity or profitability. The sectors receiving the highest levels of support include photovoltaics, semiconductors, steel, aluminum, shipbuilding, batteries, and other heavy industries. In a communication issued on May 29, 2026,[12] the European Commission stated that the current state of trade and investment relations between the European Union and China is no longer sustainable and that a firmer and more coherent policy response will be required, while maintaining an approach based on de-risking rather than decoupling. The EU's coordinated response continues to be constrained by divisions among member states, with a clear fault line separating those advocating a tougher stance—notably France—from those, led by Germany, concerned about the economic consequences of a more confrontational relationship with Beijing.

[10] The United States–Mexico–Canada Agreement (USMCA), known in Mexico as the *Tratado entre México, Estados Unidos y Canadá* (T-MEC), entered into force on July 1, 2020, replacing the North American Free Trade Agreement (NAFTA), which had been in effect since January 1, 1994.

[11] OECD. 2026. *OECD MAGIC Database of Industrial Subsidies*. Paris: OECD Publishing. https://doi.org/10.1787/ce94f33b-en.

[12] European Commission. 2026. "European Commission considers current state of economic relations with China 'untenable', promising rebalancing". Europe Daily Bulletin no 13877, 29 May 2026. https://agenceurope.eu/en/bulletin/article/13877/15/european-commission-considers-current-state-of-economic-relations-with-china-untenable-promising-rebalancing.

Figure 10 – China: the world's leading provider of corporate subsidies



Source: OECD.

The risk of a global recession remains contained for the time being

Even under their most adverse scenarios, neither the IMF nor the OECD anticipates a contraction in global economic activity in 2026–27. Oxford Economics (OE), however, presents a scenario involving a global technical recession beginning in mid-2026, assuming a further escalation of the conflict in the Middle East. The global growth outlook remains highly dependent on several factors: the pace at which maritime traffic through the Strait of Hormuz resumes; the extent of damage to oil and gas infrastructure across the Gulf countries; and, consequently, the evolution of commodity prices, supply chain disruptions, the pass-through of higher production costs to final prices, and the adjustment of demand in response to national monetary and fiscal policy measures. Between its October 2025 and April 2026 projections, the IMF left its forecast for global growth in 2026 unchanged at 3.1% (following 3.4% in 2025), reflecting a stronger-than-expected carry-over effect from late 2025, some easing of the tariff war, and improved prospects for the United States, China, and India (see Table 2). The North Africa and Middle East region is, unsurprisingly, expected to be hard hit, with growth projected to be halved to 1.9% in 2026, whereas other regions are expected to perform broadly in line with the projections released in the autumn.

In its April 2026 World Economic Outlook,[13] the IMF presents two alternative scenarios. Under the more adverse scenario, global growth would slow to around 2% in both 2026 and 2027, with average oil prices reaching USD 110 per barrel in 2026[14] and USD 125 in 2027 (see Table 3). In its June 2026 Economic Outlook,[15] the OECD projects global growth of 2.8% in 2026, followed by a rebound to 3.1% in 2027. This baseline scenario assumes that disruptions remain temporary, with average oil prices of USD 92 per barrel in 2026 and USD 80 in 2027. It also assumes that global activity will recover during the second half of 2026 after a marked slowdown in the second quarter (see Figure 11). Under a scenario in which disruptions persist beyond 2026, hydrocarbon prices would remain around 50% above the baseline scenario through the third quarter of 2027. The adjustment of global demand to a stronger inflationary shock, combined with constrained supplies of energy products and other key industrial and agricultural inputs, would limit global growth to 2.1% in 2026 (0.7 percentage point below the baseline scenario) and 1.8% in 2027 (1.3 percentage points below the baseline). Oxford Economics, for its part, models a scenario involving a further escalation of the conflict, in which oil prices rise to USD 160 per barrel in the third quarter of 2026. This would trigger a global technical recession, reducing average annual global growth to 1.9% in 2026 and 1.3% in 2027. **Under this scenario—which Oxford Economics assigns a probability of around 10%—the cumulative loss in real GDP relative to the baseline over the 2026–27 period would amount to approximately 4.5% for the Gulf countries, more than 2.5% for the United States and Japan, around 2% for the euro area and Asia-Pacific, more than 1.5% for China, and around 1% for both Africa and Latin America.**

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[13] IMF. 2026. *World Economic Outlook. Global Economy in the Shadow of War.* Washington, D.C.: IMF. https://www.imf.org/en/publications/weo/issues/2026/04/14/world-economic-outlook-april-2026.

[14] As of June 16, 2026, the average daily Brent crude oil price since January 1 stood at approximately USD 90 per barrel.

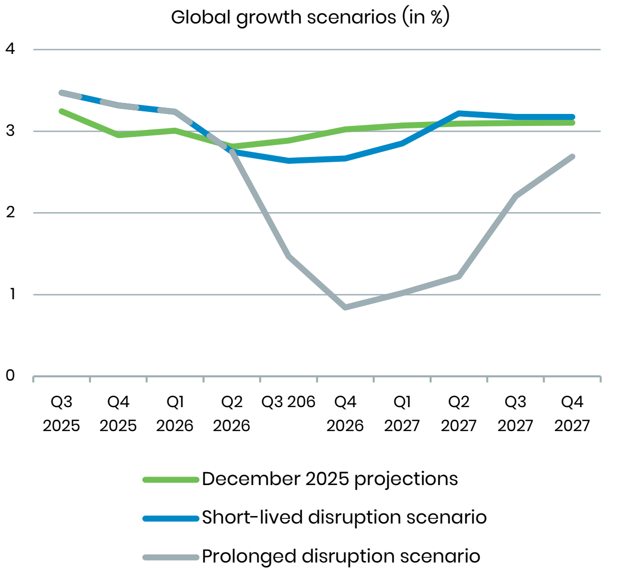
[15] OECD. 2026. "Under Pressure". *OECD Economic Outlook* 2026 (1). Paris: OECD Publishing. https://doi.org/10.1787/2d1956f0-en.

Table 3 – IMF alternative scenarios

SCENARIOS	BASELINE	ADVERSE	SEVERE
Global growth 2026	3.1%	2.5%	2.0%
Global growth2027	3.2%	3.0%	2.2%
Global inflation2026	4.4%	5.4%	5.8%
Global inflation 2027	3.7%	3.9%	6.1%
Oil price 2026 (USD/b)	82	100	110
Oil price 2027 (USD/b)	76	75	125

Source: IMF (World Economic Outlook).

Figure 11 – Whoever controls the seas (and the straits) controls the economy

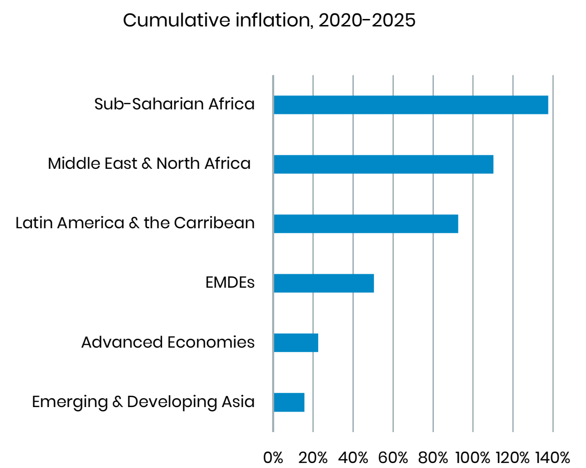


Source: OECD (June 2026).

A sustained increase in the cost of living

In 2026–27, the global inflationary shock is expected to be less severe than that experienced in 2022–23, except under a scenario involving a prolonged closure of the Strait of Hormuz and/or a further escalation of the conflict, in which case the increase in inflation would be broadly comparable to that observed in 2022–23 (around 2–2.5 percentage points). Even then, however, the inflation peak would be less pronounced, mainly owing to a more favorable base effect. Since the pandemic, the increase in the cost of living has been particularly marked in EMDEs, especially in Sub-Saharan Africa (see Figure 12). According to the International Labour Organization (ILO),[16] real wage growth has been robust in emerging Asia, whereas advanced economies and Latin America have only gradually recovered the purchasing power lost during the 2022–23 inflationary episode. In 2022, inflation was already elevated before Russia's invasion of Ukraine (6.3% at end-2021, compared with 4.0% at end-2025). The subsequent energy shock further accelerated price increases, driven by the strong post-pandemic recovery, shortages of intermediate goods, global logistics bottlenecks, and expansionary fiscal and monetary policies. Under the most adverse scenario, global inflation would peak at around 6.0% in 2026–27 according to the IMF and 6.8% according to Oxford Economics, compared with 8.9% in 2022.

Figure 12 – Sharp cumulative inflation since the pandemic



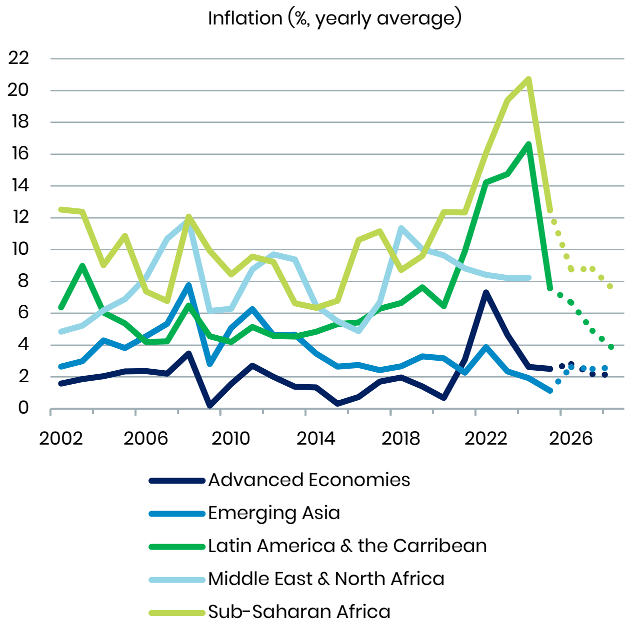
Source: IMF (World Economic Outlook), AFD calculations.

As with the inflationary shocks of 2008, 2011 (food price spikes), and 2022, EMDEs are expected to be more severely affected than advanced economies, including the European Union, whose dependence on Gulf hydrocarbons in 2026 is lower than its dependence on Russian natural gas was in 2022. This is all the more

[16] ILO. 2024. *Global Wage Report 2024-25: Is wage inequality decreasing globally?*. Geneva: ILO. https://www.ilo.org/publications/flagship-reports/global-wage-report-2024-25-wage-inequality-decreasing-globally.

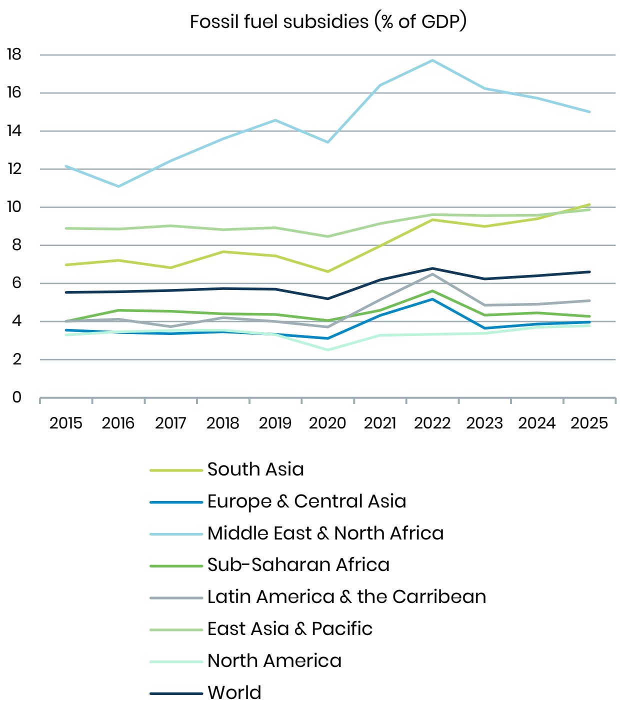
significant as a new El Niño episode is looming and could prove particularly strong, with potentially adverse effects on the 2027 agricultural season. This largely reflects the greater weight of energy and food expenditures in household consumption baskets across EMDEs. Since March, national authorities have introduced a new round of anti-inflation measures, particularly in the energy sector, as documented by the IEA.[17] These policies have sometimes reflected conflicting objectives between supporting firms and preserving household purchasing power—through energy subsidies, price caps, tax reductions, and direct transfers—and moderating demand via energy-saving incentives, restrictions on energy use and travel, mandatory teleworking, and temporary closures of public administrations and schools. Fiscal space to sustain energy subsidies—and, in some cases, subsidies for fertilizers or selected food products—remains limited in many countries, particularly in Africa (see Figures 13 and 14). Since 2022, several countries—including Nigeria, Angola, Kenya, Ethiopia, Senegal, Cameroon, and Egypt—have eliminated or substantially reduced fiscally costly fuel subsidies, in line with IMF and World Bank recommendations favoring more targeted social support. Although Asia was the region least affected by the 2022 energy shock, it is the most exposed in 2026 owing to its heavy dependence on energy imports from the Gulf. Nevertheless, most Asian economies benefit from sound macroeconomic fundamentals and relatively strong fiscal buffers. In Latin America, exposure to physical energy supply disruptions remains comparatively limited, with the exception of Central America and the Caribbean. The region nevertheless remains vulnerable to higher international energy prices, while generally having more limited fiscal room for maneuver than Asia. **It should also be noted that if the June 17 agreement is successfully implemented and sustained over time, although it would not immediately resolve supply disruptions or reduce prices, it would likely help re-anchor inflation expectations and facilitate a gradual easing of monetary policy.**

Figure 13 – Post-2022 disinflation interrupted in 2026–27



Source: IMF (World Economic Outlook).

Figure 14 – Fossil fuel subsidies remain substantial worldwide



Source: IMF, Climate Change: Fossil Fuel Subsidies, Washington, DC.

[17] https://www.iea.org/data-and-statistics/data-tools/2026-energy-crisis-policy-response-tracker?tab=Energy+conservation.

Rising risks of tighter conditions in international financial markets

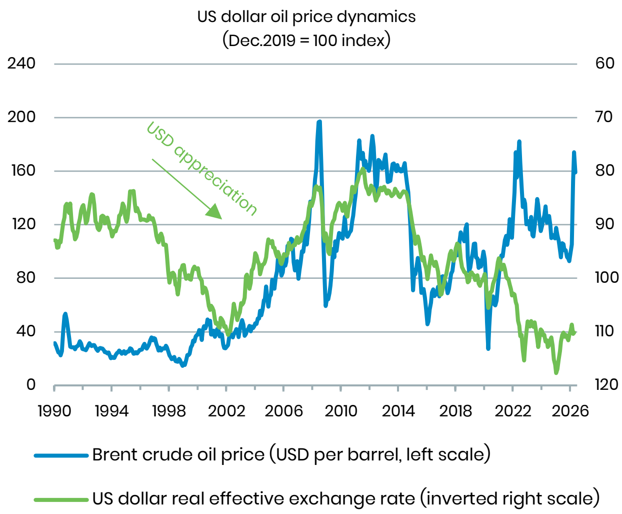
After a particularly favorable year in 2025, emerging financial markets experienced turbulence in March 2026 before recovering. The risk of tighter international financing conditions for EMDEs has increased as a result of several factors:

- **a moderate strengthening of the U.S. dollar;**
- **the interruption of monetary easing in response to the resurgence of inflation;**
- **tighter global liquidity conditions, as liquidity has been absorbed by the U.S. equity market boom driven by the technology sector—including the record-breaking initial public offering (IPO) of SpaceX, with Anthropic and OpenAI expected to follow—against a backdrop of massive investment requirements and rising leverage;**
- **increasing pressure on sovereign bond markets in advanced economies owing to substantial public financing needs (see Figures 15–20).**

Since Donald Trump's re-election, the U.S. dollar has depreciated by around 7% in real effective terms. This trend partially reversed following the outbreak of the conflict with Iran in February 2026, with the dollar appreciating by around 1%. A stronger dollar, combined with renewed pressure on exchange rates, has reinforced inflationary risks in EMDEs. Several central banks—including those of Indonesia, the Philippines, and Türkiye—have tightened monetary policy during 2026, as did the euro area on June 11, raising its policy rate by 25 basis points to 2.25%. Asian central banks, particularly those of India and Indonesia, have intervened actively in foreign exchange markets to support their currencies. Türkiye has done likewise, leading to a significant depletion of its foreign exchange reserves. The stance of U.S. monetary policy remains central to the outlook for emerging financial markets. Emphasizing its commitment to restoring price stability, the new Chair of the Federal Reserve, Kevin Warsh, has already reshaped the institution's communication strategy, moving away from the highly explicit forward guidance associated with Jerome Powell toward a much more cautious and conditional approach. At its first meeting under his leadership, held on June 16–17, the Federal Open Market Committee (FOMC) left policy rates unchanged, maintaining the Fed Funds target range at 3.50–3.75%. The accompanying statement did not signal a discretionary or accommodative bias, on the contrary, despite repeated pressure from the White House to lower interest rates.

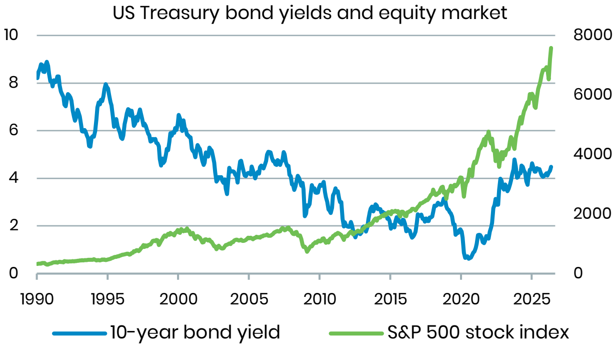
In a context of rise in 10-year "risk-free" sovereign yields (U.S. Treasuries for U.S. dollar financing and German Bunds for euro-denominated financing), EMDE sovereign risk premia remained close to historical lows after widening temporarily in March. Following net outflows during that month, portfolio investment flows to EMDEs recovered after the U.S.–Iran ceasefire agreement announced on April 8, before weakening again in May as hostilities continued and the Strait of Hormuz remained closed. **Overall, between late February and mid-June, international market financing conditions became more expensive for advanced economies (with borrowing costs increasing by 35–50 basis points in Germany, the United States, and France), for Asian economies (+36 basis points on average, bringing U.S. dollar yields to around 5.5%), and especially for the Middle East (+73 basis points, to 6.4%, albeit from historically low levels). Over the same period, Africa and Latin America experienced relative stability in the average yields on outstanding Eurobonds, at approximately 7.5% and 7.3%, respectively.**

Figure 15 – The U.S. Dollar has followed a downward trend since the second Trump administration took office



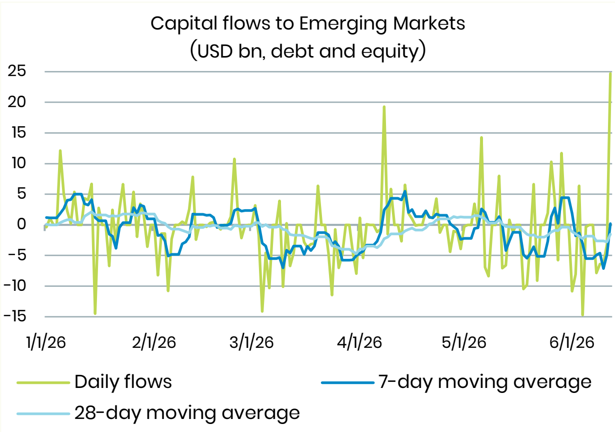
Source: IMF, EIA, ECO calculations.

Figure 16 – Equity markets at record highs, bond markets under pressure



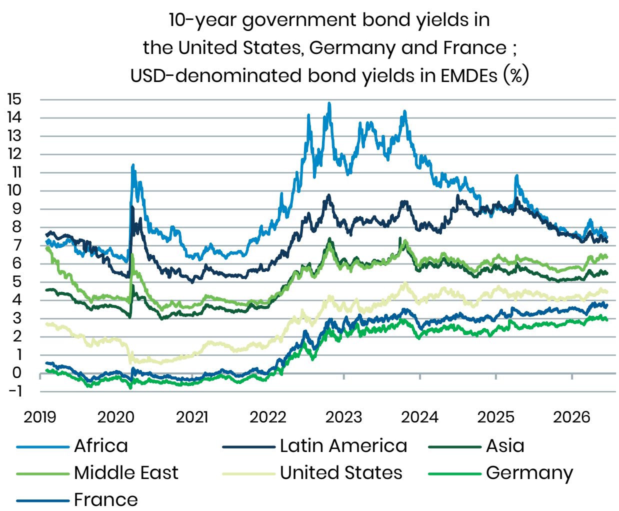
Source: U.S. Department of the Treasury, S&P Global.

Figure 17 – Volatile capital flows to emerging markets during the first half of 2026, but no large-scale capital flight



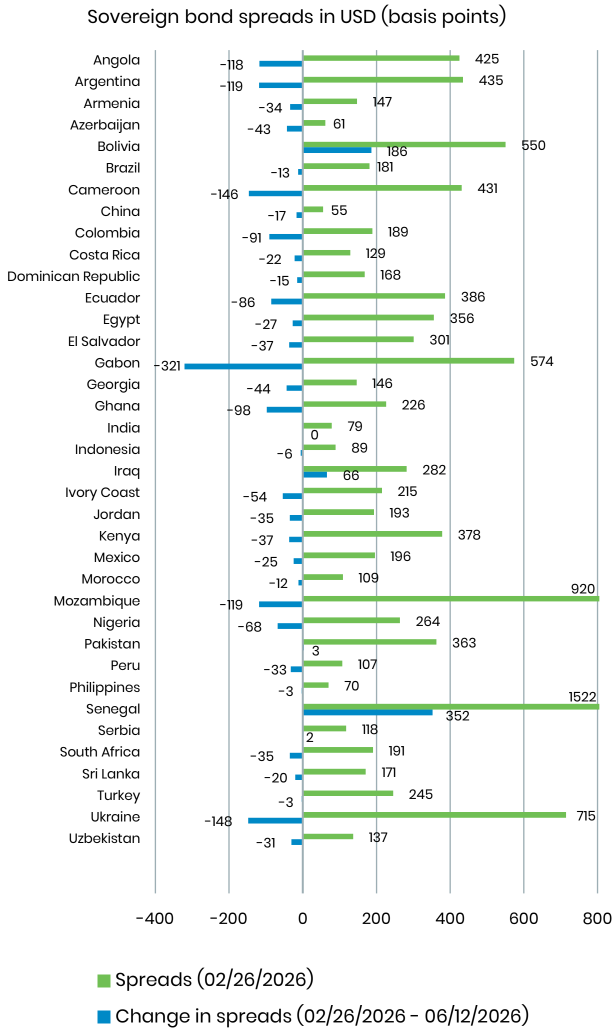
Source: Institute of International Finance (IIF).

Figure 18 – The easing of financing conditions for EMDEs is being called into question



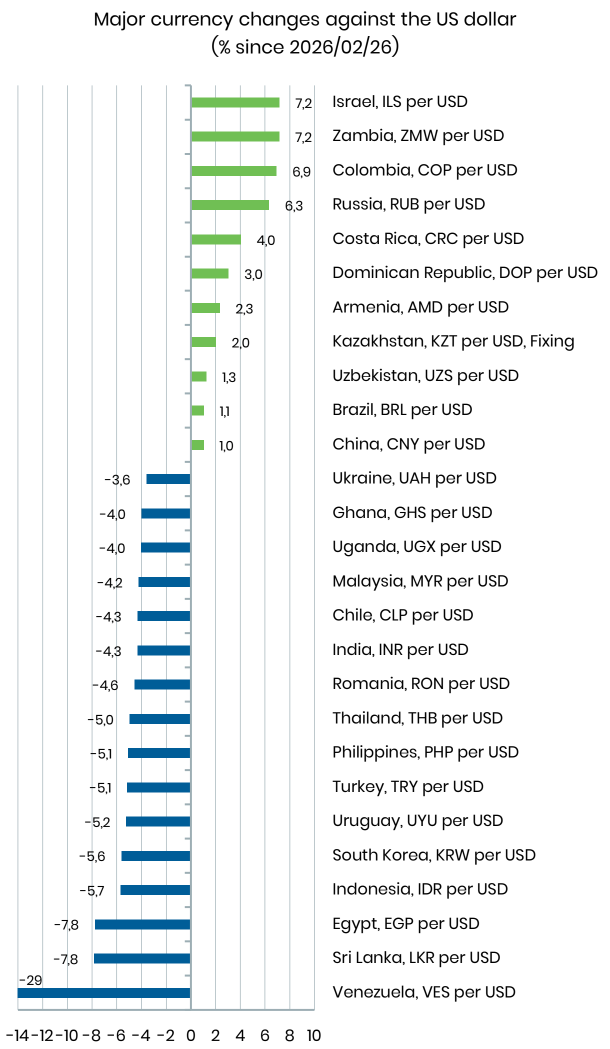
Source: J.P. Morgan.

Figure 19 – ...Despite compressed sovereign risk premia in the first half of 2026



Source: J.P. Morgan, AFD calculations.

Figure 20 – Emerging market currencies have remained broadly stable despite a generally weaker U.S. Dollar

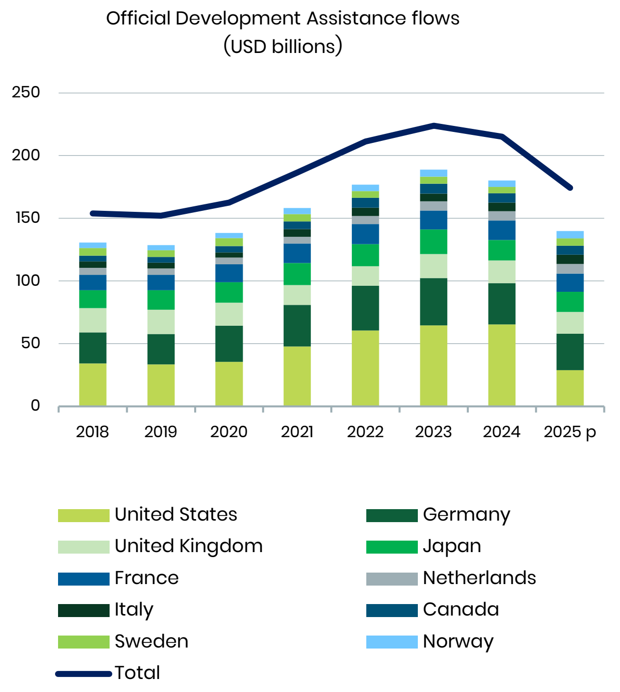


Source: Macrobond, AFD calculations.

The yields on outstanding external public debt therefore remain below the yields required on new Eurobond issuances since 2024, particularly in Africa. Over time, this raises concerns about the increasing cost of external borrowing and the resulting rise in external debt service, against a backdrop of declining official development assistance (ODA)—which fell by 23% in 2025 relative to its 2023 peak, to USD 174 billion according to the OECD—[18] and shrinking concessional financing (see Figures 21 and 22). Market financing conditions remain substantially more expensive than before the pandemic: by roughly 100 basis points in Africa, 170 basis points in Latin America, 180 basis points in Asia, and 220 basis points in the Middle East. These financing costs, which are inversely related to the regions' underlying structural risk profiles, partly reflect the short-term risks associated with the conflict in the Middle East. For African sovereign issuers, market borrowing costs generally range between 8% and 10%, including for South Africa, Egypt, Nigeria, Kenya, Côte d'Ivoire, Cameroon, Benin, and Gabon. Morocco, which retains the strongest sovereign credit profile on the continent (excluding Botswana, which does not issue Eurobonds), has not returned to international capital markets since 2023, while Tunisia has not issued international bonds since 2019 because of prohibitively high financing costs. Senegal has effectively lost market access, with sovereign spreads around 1,500 basis points following the deterioration in its public finances revealed in 2024, a situation similar to that of Mozambique. Both countries could eventually require sovereign debt restructuring. At this stage, countries that have already completed debt restructuring—including Ghana and Zambia (as well as Sri Lanka outside Africa)—have not yet returned to international capital markets, while Ethiopia is close to completing its own restructuring process. Argentina has not issued Eurobonds since 2018. By contrast, Bolivia, despite facing a protracted balance-of-payments crisis, returned to the market in 2024, while Ecuador issued a conventional Eurobond in January 2026—its first since the 2020 debt restructuring, excluding the 2023 debt-for-nature swap. In Pakistan, improved macroeconomic conditions since the 2022–2023 crisis allowed the country to return to international markets in April 2026, after its last issuance in 2021.

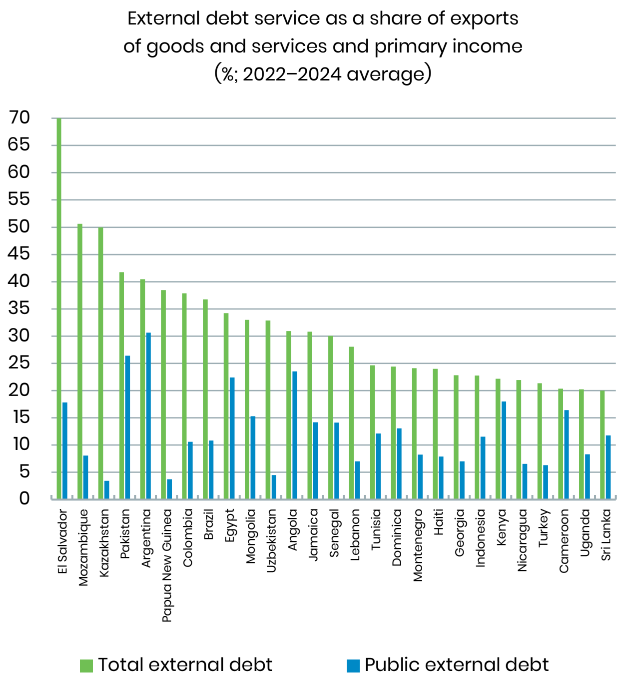
[18] OECD. 2026. "A historic decline in foreign aid: Preliminary 2025 ODA data". 9 April 2026. https://www.oecd.org/en/data/insights/data-explainers/2026/04/a-historic-decline-in-foreign-aid-preliminary-2025-oda-data.html.

Figure 21 – Official development assistance has declined since 2024



Source: OECD.

Figure 22 – Rising risks to external public debt service and total external debt service



Source: World Bank, AFD calculations.

Country focus

Egypt
Ethiopia
Nigeria
Uganda
Bangladesh
Uzbekistan
Pakistan
Serbia

Egypt: A Fragile Stabilization

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Despite a visible improvement in key macroeconomic indicators—exchange rate stabilization, declining inflation, and the gradual return of external financing—Egypt’s economy remains characterized by deep structural vulnerabilities. External imbalances remain significant, while the growth model continues to rely on capital inflows, support from Gulf partners, and the dominant role of the state. Against the backdrop of a particularly deteriorated regional environment, this recent stabilization remains fragile and vulnerable to a new external or geopolitical shock.

Recent progress in addressing macroeconomic imbalances has helped partially restore the confidence of investors and the IMF. However, these gains remain insufficient to dispel several major vulnerabilities: (i) a still fragile socio-political environment and a lag in convergence with comparable emerging economies in terms of per capita income; (ii) a very high level of public debt weighing heavily on the sustainability of public finances; and (iii) external shocks stemming from regional conflicts that could further worsen an already deficit-ridden current account and undermine the ongoing process of disinflation and interest rate reductions.

Genuine macroeconomic stabilization since 2024

Since 2024, Egypt has appeared to enter a promising phase of macroeconomic stabilization following several years of severe turbulence marked by pressure on the pound, record-high inflation, and substantial fiscal imbalances. The main achievement has been monetary stabilization. Following several successive devaluations, the adoption of a flexible exchange rate regime significantly reduced distortions in the foreign exchange market. Foreign currency shortages and the gap between official and parallel market exchange rates have virtually disappeared, reflecting renewed confidence among domestic economic agents. This has contributed to the return of foreign investor confidence and improved financial conditions. At the same time, inflation, which had exceeded 38% in 2023, slowed markedly to around 12% by early 2026. This disinflation marks a major turning point after several years of declining purchasing power. It has enabled the Central Bank to initiate a monetary easing cycle through a series of policy rate cuts, supporting credit growth, private investment, and domestic demand.

Fiscal outcomes have also become more favorable. The authorities have undertaken politically sensitive reforms, notably the gradual reduction of energy subsidies. Tax revenues have increased owing to a broader tax base, the digitalization of tax administration, and a reduction in exemptions. These improvements have allowed the government to maintain a substantial primary surplus. The public debt situation has also shown signs of improvement. After peaking at 96% of GDP in 2023, the debt-to-GDP ratio declined to around 87% in 2025, supported by fiscal consolidation, stronger growth, and a more favorable financing structure. The authorities aim to reduce public debt to 71–73% of GDP by 2028–29.

This stabilization is beginning to generate tangible effects on economic activity, with growth exceeding 4% again in 2025. The recovery has been supported by tourism, Suez Canal-related activities, manufacturing, and the gradual rebound of private investment. Significant external financing (IMF: USD 4.3 billion; World Bank: USD 7 billion; European Union: USD 8 billion; Saudi Arabia: USD 5 billion), together with private inflows—notably through the Ras El-Hekma agreement (USD 35 billion)[19]—have also strengthened short-term prospects.

[19] This agreement, signed in February 2024 between Egypt and Abu Dhabi’s Sovereign Wealth Fund (ADQ) for the development of the Ras El-Hekma Peninsula on Egypt’s northern coast, is one of the largest foreign investment projects ever undertaken in the country.

Yet major challenges remain

Behind this stabilization, progress on the most sensitive structural reforms remains slow, raising questions about the country's ability to transform this cyclical improvement into durable consolidation. The primary source of concern remains the continued dominance of the state in the economy. Reducing the state's footprint is essential to ensure a level playing field between public and private enterprises, stimulate private investment, enhance competition, and increase productivity. Yet progress under the privatization program has remained limited despite repeated commitments from the authorities. Egypt had announced the privatization of 38 state-owned enterprises under the IMF-supported program, but few significant transactions have actually materialized. The ambitions now appear to be shifting toward the rationalization and formalization of state-owned enterprises rather than genuine asset divestitures. Efforts to improve transparency and governance remain insufficient to durably transform the functioning of the economy.

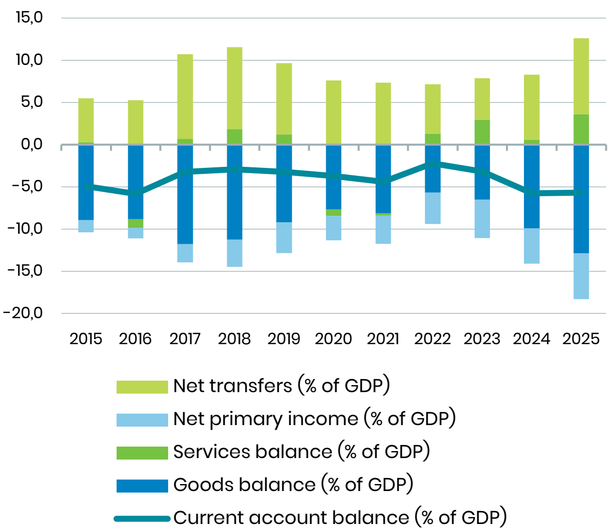
Vulnerabilities related to public debt also continue to weigh heavily on the country's outlook. Despite the recent decline in the debt ratio, the level remains very high for an emerging economy exposed to external shocks. Financing needs remain considerable, at around 40% of GDP annually, while debt-service interest payments are projected to absorb more than 80% of government revenues in 2026 (IMF), a global record. This fiscal constraint significantly reduces the government's policy space and increases dependence on external financing and IMF support. External imbalances also remain substantial, with an economy highly dependent on imports and on volatile sources of foreign exchange earnings such as tourism, remittances from expatriate workers, Suez Canal revenues, and real estate investment.

A real risk of deterioration

The recent deterioration in the regional geopolitical environment directly threatens the gains achieved since 2024. Egypt remains highly dependent on imports of wheat—the world's largest importer—as well as energy products and intermediate goods, making it particularly vulnerable to any increase in global oil and commodity prices. The rising energy import bill will simultaneously widen the current account deficit and increase the cost of public subsidies. Adjustments to administered energy prices are also likely to fuel inflationary pressures. In this context, the authorities have allowed the Egyptian pound to depreciate in order to preserve foreign exchange reserves. As a result, the currency lost nearly 10% of its value against the U.S. dollar during the spring of 2026. While exchange rate flexibility helps absorb part of the external shock, it also significantly increases import costs and may trigger a new inflationary spiral. The Central Bank could therefore be forced to maintain high interest rates at the expense of credit growth and private investment.

External accounts appear particularly exposed. The trade deficit could widen further as energy imports increase. At the same time, Egypt has experienced substantial foreign capital outflows, particularly from the sovereign bond market. Between mid-February and mid-March, these outflows amounted to nearly USD 10 billion, although the flows have since returned. Consequently, financing the external deficit continues to expose Egypt to the risk of a renewed reversal in investor sentiment. Finally, the risks of a decline in tourism, Suez Canal traffic, and remittances from Egyptian workers in the Gulf threaten several of the country's main sources of foreign exchange earnings.

Figure 23 – A marked deterioration in the current account balance (% of GDP)



Source: IMF, AFD calculations.

Ethiopia: Highly Sensitive to Shocks

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The far-reaching economic reforms implemented beginning in July 2024 have led to an improvement in macroeconomic fundamentals, marking the country’s emergence from the economic crisis it had faced for the previous five years. However, the Ethiopian economy still has only limited policy buffers and remains vulnerable to shocks, particularly those stemming from the crisis in the Middle East.

After several years marked by successive shocks—the COVID-19 pandemic, the conflict in Tigray, recurrent droughts, and declining international financing—Ethiopia’s economy has shown tangible signs of recovery since mid-2024. The government launched a broad reform agenda (*Homegrown Economic Reform 2.0*), supported by an IMF program, aimed at correcting the macroeconomic imbalances that had resulted in high inflation, foreign exchange shortages, and debt distress.

An economy on the path to recovery

The reforms quickly yielded positive results, supported by a combination of highly favorable exogenous factors, including strong agricultural harvests and higher international prices for gold and coffee. One of the most significant measures was the move toward a more flexible exchange rate regime in July 2024. This reform triggered a sharp depreciation of the birr (40% within seven days and 55% between July and December 2024) and substantially reduced the gap between the official and parallel foreign exchange markets, which had been a major source of economic distortions. At the same time, access to external financing improved following IMF approval of a USD 3.4 billion program, a substantial share of which was rapidly disbursed to support the balance of payments and restore the confidence of investors and international partners. In addition, the conclusion of a debt restructuring agreement with official bilateral creditors in July 2025 placed Ethiopia’s public debt back on a sustainable trajectory, while the financial restructuring of state-owned enterprises reduced the government’s contingent liabilities.

Foreign exchange reserves began to recover, reaching more than USD 5 billion by the second quarter of 2026—equivalent to more than two months of import coverage. Foreign currency shortages eased, and inflation started to decline, falling below 10% in December 2025 (9.7%) for the first time in seven years, supported by tighter monetary policy and a reduction in monetary financing of the fiscal deficit.

Economic growth has regained momentum, exceeding 8%. Growth is estimated at 9.2% during fiscal years 2024/25 and 2025/26, with economic activity benefiting in particular from the gradual normalization of foreign exchange availability. Prospects for FY26/27 are somewhat more nuanced and depend on developments in the Middle East conflict. The IMF projects growth of 7.8%,[20] whereas the authorities, in the draft budget presented in June 2026, anticipate growth of 10.1%.

Exposure to the Middle East crisis

The war in Iran and the tensions it has generated—particularly in global oil and fertilizer markets— tested the resilience of the Ethiopian economy at a time when its policy space remains limited.

The primary transmission channel is energy imports. Ethiopia imports all of its refined petroleum product requirements. Under a long-term supply agreement, it sources most of its fuel

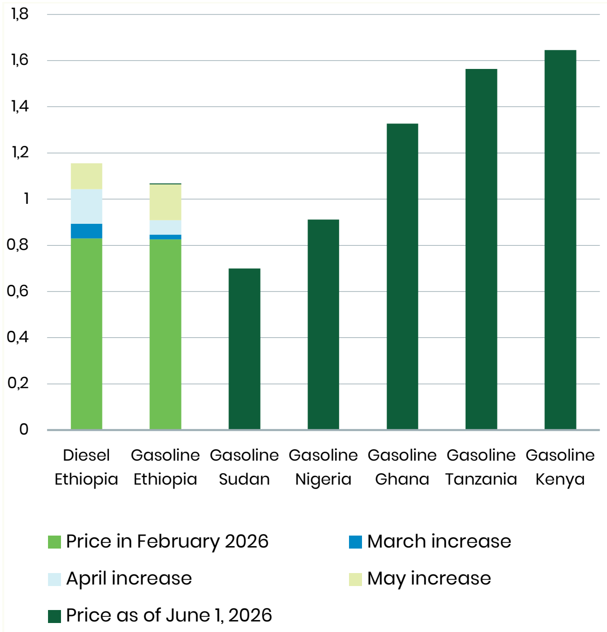
[20] IMF, Ethiopia: Fifth Review under the Extended Credit Facility, July 2026. See: https://www.imf.org/en/news/articles/2026/06/03/pr26183-ethiopia-imf-reaches-staff-level-agreement-fifth-review-extended-credit-facility.

from Kuwait (60% of its diesel imports and 100% of its kerosene imports). As disruptions to supplies from the Gulf emerged, Ethiopia was forced to identify alternative suppliers on short notice. With fuel imports exceeding USD 4 billion annually in both 2023 and 2024—equivalent to nearly 3% of GDP—an increase in oil prices directly weight on the trade balance, the current account, and foreign exchange reserves. Although the country's dependence on petroleum products remains relatively limited—these account for only 7.8% of the energy mix[21] thanks to the central role of hydropower and biomass—they remain essential for transportation and account for nearly half of energy consumption in the industrial sector.

Higher oil prices also represent an inflationary risk that could erode household purchasing power. The authorities continue to maintain a fuel subsidy system, which was reinforced during the exchange rate reform in 2024 in order to limit the inflationary impact of currency depreciation. Since 2025, however, the government has embarked on a gradual phase-out of these subsidies, with the objective of eliminating them entirely during 2026. Subsidies continue to play a role, retail fuel prices remaining significantly below the levels that would result from a full pass-through of international prices. The authorities have nonetheless implemented several increases in administered fuel prices since late 2025 and early 2026 (see Figure 24). As of June 1, 2026, the retail gasoline price stood at ETB 167 per liter (USD 1.07 per liter). Fuel prices in Ethiopia therefore remain below the global average of USD 1.44 per liter and rank among the ten lowest in Africa (see Figure 24).

The authorities faced a delicate trade-off between containing the fiscal cost of subsidies and preserving household purchasing power. For fiscal year 2025/2026, the budget allocated to fuel subsidies was initially set at ETB 100 billion, equivalent to approximately 0.6% of GDP. Tensions in international energy markets could reignite inflationary pressures. In this regard, the first months of 2026 already appear to signal a slowdown in the disinflation process observed since the exchange rate reform. In April 2026, inflation reached 11.7% y/y, once again exceeding the 10% threshold.

Figure 24 – Trends and international comparison of retail fuel prices (USD per Liter)



Source: Global Petrol Prices, AFD calculations.

A second transmission channel concerns agriculture. Ethiopia relies heavily on imported agricultural fertilizers, making it vulnerable to both rising prices and supply disruptions resulting from disturbances in the Strait of Hormuz. In 2024, Ethiopia was Africa's largest fertilizer importer by volume, importing 1.97 million metric tons. Rising fertilizer import costs weigh on the country's trade balance. Because fertilizers continue to benefit from public support mechanisms, the immediate impact on farmers is partially mitigated. However, much like the fuel subsidy system, the gradual reduction of fertilizer subsidies is increasing the economy's exposure to fluctuations in international prices. This could raise agricultural production costs and, ultimately, food prices.

[21] Energy System of Ethiopia (database), International Energy Agency (IEA), Paris, 2023. https://www.iea.org/countries/ethiopia.

Nigeria: A Net Macro Beneficiary of the Global Shock

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The direct impact of the global energy shock is expected to be positive for Nigeria's external accounts. As an exporter of oil, natural gas, refined petroleum products, and urea, the country stands to benefit from both price and volume effects. The elimination of fuel subsidies and the anticipated increase in fiscal revenues could, however, be offset by mounting pressure on public spending as the authorities seek to address the social costs and the slowdown in domestic demand resulting from a stalled disinflation process in the run-up to the general elections.

A crude oil price of USD 100 per barrel undoubtedly contributes less to Nigeria's "macro-social equilibrium"[22] than a price of USD 74 per barrel, its average level during 2024–25. Yet, at the center of the new global economic shock triggered by the war in Iran, Nigeria currently enjoys its lowest sovereign risk premium since September 2014, with spreads narrowing to 270 basis points over U.S. Treasury securities. In May, S&P upgraded the country's foreign-currency sovereign rating to B/Stable. The 2014 oil price collapse and the end of the commodity supercycle marked the beginning of a "lost decade" for Nigeria. By contrast, the current shock may serve to validate the economic policy orientation adopted by the Tinubu administration over the past three years and confirm both the rationale and durability of its reform agenda, without diminishing the significance of the country's socio-economic challenges.[23]

An oil and gas sector rebound

Although the hydrocarbon sector now accounts for only 5.5% of GDP, it remains a strategic and critical sector, generating on average 87% of exports and 36% of fiscal revenues between 2021 and 2025. According to BP, Nigeria possesses the world's eleventh-largest oil reserves and tenth-largest natural gas reserves. The recovery in oil production, which approached Nigeria's OPEC+ quota of 1.5 million barrels per day in 2025, enabled the country to regain its position as Africa's leading oil producer. This rebound was supported in particular by maintenance efforts and enhanced security around production facilities. Reforms to the legal and fiscal framework aimed at attracting and retaining domestic and foreign investors have also begun to yield results. The government's objective is to double crude oil production by 2030. Major international oil companies—including Exxon-Mobil, Shell, and TotalEnergies—are gradually divesting from onshore operations due to environmental concerns, declining profitability, and tensions with communities in the Niger Delta. At the same time, they remain active offshore, particularly in the natural gas sector.

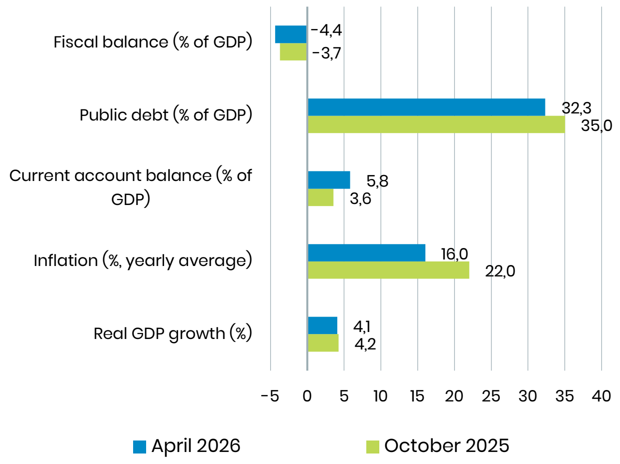
Relations also appear to be improving between the Nigerian National Petroleum Company (NNPC), the state-owned enterprise that retains a monopsony position in the upstream segment, and Dangote Group, the dominant player in the downstream sector and a near-monopoly provider of domestic refining capacity. In September 2025, the two companies renewed for an additional two years their "naira-for-crude" agreement to supply the Dangote refinery, inaugurated in 2024. Planned expansion of the refinery's capacity to 1.4 million barrels per day by 2028 would make it the largest refinery in the world. These developments represent a genuine turning point for Nigeria's energy independence and for the emergence of a regional energy hub in Africa. However, they remain heavily dependent on a private conglomerate controlled by the continent's wealthiest individual. While Dangote's strategy is officially presented as serving the national interest, the group has historically been known for

[22] Defined here as the capacity of a society to absorb economic, political, or geopolitical shocks without triggering social instability or unrest.

[23] See: Bellefontaine, Sylvain. 2026. *Nigeria: The Long Road from Stabilization to Development*. MacroDev 74. Paris: Éditions Agence française de développement.

aggressive pricing practices aimed at weakening competitors, particularly in the cement and sugar industries.

Figure 25 – Changes in macroeconomic projections for 2026



Source: IMF (World Economic Outlook).

An external beneficiary of the Middle East crisis

The return to a current account surplus in 2022 helped strengthen Nigeria's external position, notably through higher foreign exchange reserves. Combined with improvements in monetary governance, this contributed to stabilizing the naira following the adoption of a more flexible exchange rate regime and the two major devaluations implemented in 2023–24. The current account surplus is expected to strengthen further in 2026, reaching 5.8% of GDP according to the IMF. This improvement reflects higher export revenues from both crude oil and refined petroleum products—including gasoline, fuel oil, and kerosene—sold to West Africa and Europe. Europe remains Nigeria's leading trading partner, accounting for 42% of exports in 2024 and 58% of the inward FDI stock, while the United States accounts for 13% of exports and 16% of inward FDI. Nigeria has been only marginally affected by the tariff measures introduced by the Trump administration, as petroleum products were exempted. The country nonetheless remains exposed to developments in the United States through two channels: remittances from the Nigerian diaspora, which reached record levels in 2025, and official development assistance formerly provided through USAID, particularly in the areas of healthcare, epidemic response, and nutrition.

Historically, Nigeria relied on imports of urea, a key fertilizer input, primarily sourced from Iran. The country has since become a major producer thanks to investments by Dangote Group and Indorama Eleme Fertilizer & Chemicals. Following disruptions to global fertilizer markets caused by the closure of the Strait of Hormuz, Nigeria has increased fertilizer exports to neighboring countries in the sub-region.

With regard to foreign investment, inward FDI flows remain structurally limited—averaging only 0.5% of GDP over the past decade—and are heavily concentrated in the hydrocarbon sector, reflecting a difficult business environment and a domestic market whose effective purchasing power remains constrained by high poverty levels. Although Nigeria's population is expected to reach 242 million in 2026, around 70% of the population lives below the lower middle-income countries' threshold of USD 4.20 per day in purchasing power parity terms. Renewed confidence in the country's macro-financial trajectory has nevertheless translated into a strong rebound in FDI inflows, which reached a post-2014 high of USD 4 billion in 2025. Following the signing of a cooperation agreement with China—the country's largest supplier and source of 7% of the inward FDI stock—in September 2024, investment commitments totaling USD 20 billion were announced in agriculture, automotive manufacturing, energy, and mining, including lithium extraction. At the same time, net portfolio investment flows remain volatile but continue to support the domestic bond market, reaching USD 7.2 billion in 2025 after USD 13.6 billion in 2024.

An ambivalent impact on public finances

The positive effects of the oil shock on fiscal revenues could be largely offset by rising social expenditures, particularly as the January 2027 general elections approach. The authorities face increasing pressure to preserve the purchasing power of vulnerable households while maintaining economic growth at around 4%. The disinflation process, which had proceeded more rapidly than anticipated following the inflation peak of mid-2024 (34% y/y), lost momentum during the first half of 2026 amid renewed pressures on food and transportation prices. Retail fuel prices have increased by 48% since February. Nevertheless, headline inflation has remained broadly stable at around 15–16%, a level that both the IMF and Oxford Economics expect to persist on average throughout the year.

The IMF’s upward revision of its 2026 fiscal deficit projection—from 3.7% to 4.4% of GDP between October 2025 and April 2026—does not appear to jeopardize the medium-term fiscal trajectory, which continues to benefit from reforms implemented since 2023. These include the elimination of fuel subsidies, tax reform, and the end of monetary financing of fiscal deficits. The renegotiation of several oil production-sharing agreements in 2025 and the government’s reassertion of control over financial flows previously managed by NNPC in 2026 illustrate the authorities’ determination to “recentralize” resource rents without undermining investor confidence. The tax reform that entered into force at the beginning of 2026 has yet to demonstrate its effectiveness in addressing one of Nigeria’s principal structural weaknesses: extremely low tax revenue mobilization, estimated at only 5.3% of GDP in 2025. This remains the main vulnerability of public finances in a country facing massive needs in social spending, security expenditures, and infrastructure investment. Combined, these expenditures remain lower than interest payments on public debt, which absorb approximately 30% of government revenues despite a relatively moderate public debt ratio of 35% of GDP.

Uganda: Carbon-Driven Economic Momentum

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Since the end of the COVID-19 period, Uganda has experienced a gradual acceleration in economic growth. Over the last three fiscal years, growth has remained on a strong trajectory (above 6% per year) and is expected to accelerate further, albeit temporarily, with the commencement of oil production. Oil revenues will contribute to partially correcting external imbalances and, to a lesser extent, fiscal imbalances. However, their sound management requires the establishment and effective implementation of appropriate governance mechanisms. In this regard, the long-awaited resumption of an IMF-supported program would help to strengthen the macroeconomic and financial framework in the years ahead and to support the trajectory of external financing required to meet the country's investment needs.

In January 2026, President Museveni's re-election for a seventh term brought a tense pre-election period to a close and signaled continuity for a regime entering its fifth decade in power. Against a highly uncertain international backdrop shaped by the conflict in the Middle East, the Ugandan economy has demonstrated resilience, supported by the imminent start of oil production.

Robust economic growth supported by the imminent start of oil production

The 1990s and 2000s were characterized by strong economic growth, during which the Ugandan economy underwent significant structural transformation. The services sector and manufacturing industries oriented toward regional markets expanded considerably. Nevertheless, the economy remains largely informal, and employment continues to be concentrated in the agricultural sector.

The 2010s were marked by relative stagnation in terms of international integration and export diversification, as the country continued to suffer from its landlocked position and dependence on the supply corridor through Mombasa. Unlike Tanzania, Uganda has yet to break through the low-income country ceiling.

Following the slowdown associated with the COVID-19 period, economic growth gradually accelerated and has exceeded 6% per year since fiscal year 2023/24. Sectoral contributions to growth have been broadly balanced across agriculture, manufacturing and extractive industries, and services, supported by investment in the oil sector and strong agricultural export performance, particularly coffee exports.

The main new engine of growth is expected to come from oil production. The start of production at the Lake Albert oil fields, operated by TotalEnergies and China's CNOOC, has been postponed several times but is now expected by the end of 2026. Output is projected to peak at around 80 million barrels per year (220,000 barrels per day) during the 2030–2033 period before declining relatively rapidly thereafter (to approximately 25 million barrels by 2040). Over time, a growing share of production is expected to supply the domestic market through investment in the Hoima refinery. The resulting growth shock is expected to be limited to roughly 6 percentage points of GDP and concentrated over four fiscal years beginning in FY26/27.

Beyond oil, however, it remains essential to develop new drivers of growth by improving the business environment, expanding private sector access to finance, and, above all, addressing chronic underinvestment in social sectors given strong demographic growth, the youthfulness of the population, and the productivity constraints weighing on the economy.

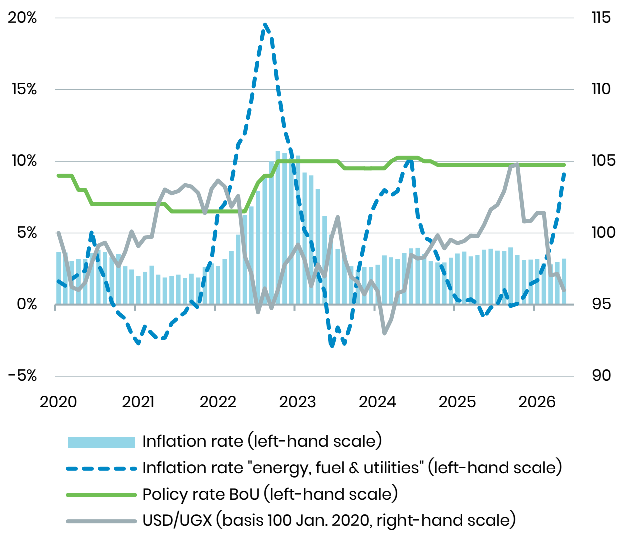
Inflation under control despite international economic tensions

The Ugandan economy is characterized by remarkable price stability within a framework of exchange rate flexibility and a 5% inflation target. Russia's invasion of Ukraine did lead to an inflation spike above 10% at the end of 2022. However, the prompt response of the central bank—the Bank of Uganda (BoU)—which raised its policy rate by 350 basis points, enabled inflation to fall below 4% y/y by mid-2023. Since then, price increases have remained contained and at the lower end of the range compared with Uganda's main partners within the East African Community (EAC).

The conflict in the Middle East has renewed pressures on petroleum products, with the price index for the "energy, fuel, and utilities" basket increasing by 9.1% y/y in May 2026. However, its impact on headline inflation has so far remained limited, with overall consumer prices rising by only 3.2% y/y.[24]

The counterpart to this effective control of inflation is the very high level of real interest rates (more than 600 basis points between the BoU policy rate and year-on-year inflation), which constrains private sector access to bank credit (with the credit-to-GDP ratio standing at only 12%) and substantially increases the cost of public debt servicing, as interest payments absorb more than one-quarter of fiscal revenues.

Figure 26 – Inflation, policy rate, and exchange rate



Source: UBoS; BoU; AFD calculations.

Maintaining high real interest rates is also essential to ensuring exchange rate stability under a flexible exchange rate regime by preserving the attractiveness of the Ugandan shilling to foreign investors in domestic financial markets. Consequently, monetary policy easing appears unlikely under current conditions, particularly as the shilling has depreciated by 7% against the U.S. dollar since November 2025.

Expected reduction in external and fiscal imbalances through oil production

Uganda's growth momentum has been accompanied by significant twin deficits, with fiscal and current account deficits averaging 5.9% and 7.1% of GDP, respectively, over the last three fiscal years (FY23/24–FY25/26). Public finances continue to be affected by structurally weak fiscal revenues, notably due to extensive tax exemptions, and by the rising cost of public borrowing resulting from the authorities' reliance on domestic debt financing. The widening current account deficit is largely explained by investment associated with oil development projects.

In this regard, the start of oil production at the end of 2026 is expected to significantly reduce the current account deficit, by approximately 5 percentage points of GDP between FY25/26 and FY28/29. This new source of resource revenues would bring the current account balance close to -2% of GDP, although not into surplus, given the country's investment needs and the projected trajectory of hydrocarbon production.

The projected impact on public finances remains much more limited at this stage. While oil-related fiscal revenues are expected to exceed 2% of GDP from FY29/30 onward, current projections assume a broadly stable fiscal deficit of more than 6% of GDP over the next five fiscal years. The persistence of a large fiscal deficit reflects the expected growth in public expenditure, particularly debt interest payments. It also implies a continued upward trajectory in public debt, which is projected to reach nearly 60% of GDP by the end of the decade, compared with 55% of GDP in FY25/26.

[24] Since the outbreak of the conflict, gasoline and diesel prices have risen by 26% and 30%, respectively, remaining within the lower range observed across the region.

Bangladesh: The Slowdown of an Economic Model

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After three decades of strong growth, the Bangladeshi economy has slowed sharply over the past three years due to inflation, the banking sector crisis, and heightened political and geoeconomic uncertainty. The country's economic model, centered on the garment industry and remittance inflows from the diaspora—primarily located in the Gulf countries—is showing structural limitations. The conflict in the Middle East has exacerbated pre-existing domestic vulnerabilities and could have adverse effects on public finances, external accounts, inflation, and economic growth.

Following the national elections held on February 12, 2026, the newly elected government took office in a highly uncertain economic environment. The transmission channels of the shock stemming from the conflict in the Middle East are multiple: higher logistics costs (insurance and maritime freight), weaker global demand, a decline in remittance inflows from the diaspora, and rising global energy and fertilizer prices, combined with the possibility of exchange rate depreciation.

Economic slowdown and limited scope for countercyclical policies

The economy recorded robust expansion over the past three decades, with average annual growth reaching 6.8% during the 2010s. These thirty years of economic progress have firmly anchored Bangladesh in the lower-middle-income country category since 2015. The two main drivers of the economy—the garment industry (accounting for 80% of exports), which developed on the basis of low labor costs, and remittance inflows from the diaspora (averaging 5.5% of GDP since 2021)—have supported consumption in a large domestic market of 170 million inhabitants. However, growth has been slowing for the past three years, constrained by weaker consumption resulting from high inflation and slowing export markets (the United States and the European Union), subdued investment in a costly and uncertain environment, and persistent vulnerabilities in the banking sector. In this context, the convergence of GDP per capita toward that of upper-middle-income countries has lost momentum, inflation has eroded purchasing power, and nearly 3 million people are estimated to have fallen back into extreme poverty (using the USD 3 per day threshold), fueling social discontent. Following the outbreak of the conflict in the Middle East, the World Bank revised its growth outlook downward, now projecting growth of 3.9% for fiscal year 2026 (FY26),[25] compared with 4.6% before the onset of the conflict. Higher input costs and inflation are expected to reduce household purchasing power, weakening private consumption. Elevated energy prices and heightened macroeconomic uncertainty could also discourage private investment, particularly in the manufacturing sector.

Weak public finances limit the government's capacity to implement countercyclical stimulus measures. The tax-to-GDP ratio is among the lowest in the world and declined during fiscal year 2025 to its lowest level in fifteen years (below 7% of GDP). Nevertheless, the fiscal deficit remained contained in FY25 (-2.9% of GDP). Under-execution of capital expenditures and social spending more than offset the decline in revenues and the increase in current expenditures, keeping the primary deficit at 0.7% of GDP in FY25. An increase in energy subsidies aimed at mitigating the impact of higher prices on households could crowd out priority expenditures, undermine fiscal consolidation efforts, and increase government financing needs in a context of tighter domestic and external financing conditions. The fiscal deficit is contributing to a rising public debt burden, which is projected to exceed 45% of GDP by the end of 2028, compared with 42% at end-2025. In June 2025, the IMF downgraded Bangladesh's risk of public debt distress from low to moderate, leaving limited room to absorb future shocks.

[25] Fiscal year running from July 2025 to June 2026.

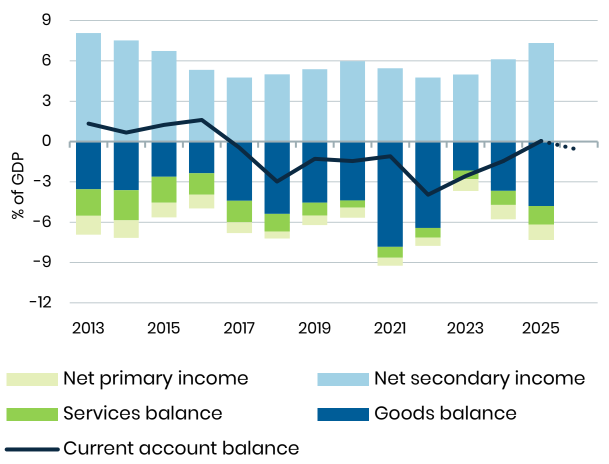
Renewed inflationary pressures in the short term

Inflation remains elevated (averaging 9.6% between 2023 and 2025), well above the Bangladesh Bank's (BB) target range of 5–6%. Between December 2023 and October 2024, the BB raised its policy rate by a cumulative 225 basis points, bringing it to 10%, where it has remained since then. However, the substantial liquidity injections provided to support fragile banks from November 2024 onward have weakened the transmission of monetary policy. The ongoing conflict in the Middle East threatens to increase import costs, particularly for energy, thereby worsening the inflation outlook. Higher energy prices directly affect production costs in both the agricultural and industrial sectors. Rising transportation costs could generate broader spillover effects across the economy. Inflation nevertheless remained relatively contained by the country's historical standards, standing at 9.0% y/y at end-April 2026 (and projected by the IMF to average 9.2% in 2026). The banking sector crisis has intensified in recent quarters, contributing to higher systemic risk. The non-performing loan ratio almost doubled in 2025, partly as a result of stricter loan classification regulations, reaching 32.3% at end-March 2026.

High exposure of the current account

The current account balance deteriorated significantly in 2021–22, notably due to the increase in the energy import bill following the war in Ukraine. After declining in FY23 and FY24, exports recovered strongly in FY25 (+7%, compared with -5% in FY24). In early 2025, the increase in U.S. tariffs to 35% (from approximately 15% previously) weighed on the garment sector, with 20% of garment exports destined for the United States. The tariff rate was subsequently reduced to 20% in July 2025 and then to 19% in February 2026. At the same time, moderate import growth contributed to an improvement in the trade balance (to -5.6% of GDP in FY25). Remittance inflows from the diaspora (45% originating from the Gulf countries and 16% from the United States) reached record levels. Increasing by more than 25% and representing 6.6% of GDP in FY25, remittances offset the trade deficit and helped maintain a balanced current account. The conflict in the Middle East could negatively impact all components of the current account. Imports could increase due to the combined effect of higher energy import costs and freight charges. Exports, meanwhile, could be affected by disruptions to global trade routes and slower demand growth in key markets. The conflict is also likely to have an adverse impact on remittance inflows as economic activity slows in host countries, reducing labor demand and wage growth. Financing any future current account deficit will require close monitoring, particularly given structurally low foreign direct investment inflows (0.4% of GDP in FY25). While foreign exchange reserves had been declining continuously since mid-2021, the adoption of a more flexible exchange rate regime in mid-2025, together with support from development partners, helped stabilize the taka and rebuild reserves, which reached the equivalent of 3.8 months of imports of goods and services at end-2025.

Figure 27 – Breakdown of the current account balance



Source: IMF, AFD calculations.

Uzbekistan: Well Positioned to Withstand the New Global Shock

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The succession of global shocks in recent years has demonstrated Uzbekistan's economic resilience. The Uzbek economy benefits from strong fundamentals and robust growth momentum. Improved macroeconomic management by the authorities, supported by substantial assistance from development partners, has limited the accumulation of imbalances and provided the country with valuable policy space. A relatively diversified and inward-oriented economy, strong energy self-sufficiency, the significant countercyclical role played by gold, and limited direct exposure to Persian Gulf countries place Uzbekistan in a favorable position to avoid the worst effects of the shock stemming from the war in Iran.

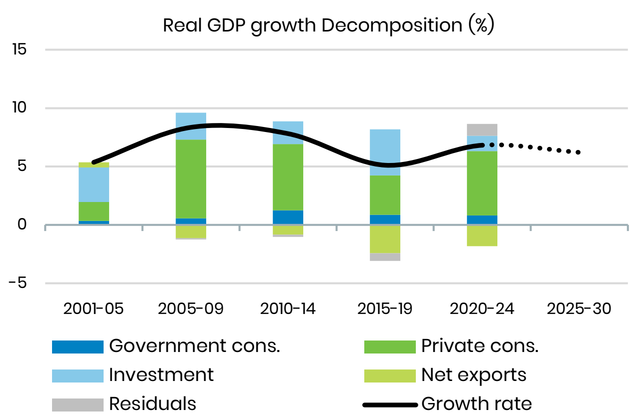
Since coming to power in 2016, President Shavkat Mirziyoyev has launched Uzbekistan into a broad program of institutional, administrative, and economic reforms. Structured around the national strategy Uzbekistan 2030, adopted in 2023 and updated in 2026, these structural reforms aim to open and liberalize the economy, improve public governance, and gradually align economic management practices with international standards. While some reforms have experienced delays, the country has seen gradual economic opening, more effective public action, and improving macroeconomic management, although significant room for further progress remains.

Strong economic momentum

Real GDP growth averaged 7.5% per year during the two decades preceding the COVID-19 crisis. The pandemic's impact proved only temporary, and by 2021 growth had returned to its pre-crisis dynamism, averaging 7% annually and reaching as high as 7.7% in 2025 despite adverse global conditions (including tariffs, conflicts in the Middle East and Europe, and widespread uncertainty). This places Uzbekistan among the world's twenty fastest-growing economies in the post-COVID period and has increased real GDP per capita by 26% since 2019.

Growth has been driven primarily by private consumption, which accounted for an average of 80% of GDP growth over the 2021–24 period. Consumption has been supported by favorable demographic trends and rising real wages, which increased by an average of 8%annually over the past five years. This has been complemented by a sharp rise in migrant remittances in recent years, reflecting both the emigration of Uzbek workers (who send funds back to their home country) and the inflow of Russian migrants since 2022 (who have transferred assets to Uzbekistan). These remittance inflows, whose sources have become increasingly diversified beyond traditional origins (such as Russia and Kazakhstan) toward other regions (including the European Union and Asia), averaged 14% of GDP between 2020 and 2024. In addition, investment is playing an increasingly important role in the economy. Its share of GDP rose from 20% in 2016 to 33% in 2025, supported by foreign direct investment inflows and rapid expansion of bank credit.

Figure 28 – Strong growth driven by private consumption



Source: World Bank; IMF; AFD calculations.

Key strengths to cushion the impact of the conflict in the Middle East

Supported by substantial financial and technical assistance from the international community, Uzbekistan has sought to align its fiscal, monetary, and economic policies with international standards. The authorities have notably strengthened public financial management and financial regulatory frameworks and initiated a transition toward a flexible exchange rate regime and inflation targeting.

The authorities’ commitment to prudent macroeconomic management is reflected in the country’s economic fundamentals. Public finances remain sound: public debt is moderate (29% of GDP in 2025), as is the interest burden (3.3% of government revenues), while the fiscal deficit remains under control (1.7% of GDP in 2025, compared with 3.8% in 2023). Supported by favorable growth prospects (projected by the IMF at an average of 5.9% over 2026–2031) and contained fiscal deficits (averaging 1.9% of GDP), public debt is expected to decline gradually to 27% of GDP by 2031, well below the ceiling established by the authorities (60% of GDP). Similarly, the current account deficit (averaging 5%of GDP over 2021–25) has generally been financed through rising foreign direct investment inflows (averaging 3% of GDP), concessional financing, and increasing portfolio investment (2% of GDP). This has enabled the country to preserve substantial foreign exchange reserves, which stood at USD 66.3 billion at end-2025, equivalent to 14 months of imports. These factors provide significant buffers against external shocks.

Compared with many developing countries, Uzbekistan appears well prepared to cope with the conflict in the Middle East. Direct exposure to the Gulf countries remains limited: they account for only 3.1% of imports (including a negligible share of energy imports) and 2.1% of exports. Consequently, the effects are likely to be primarily indirect, stemming from the anticipated slowdown in global trade, heightened inflationary pressures, strains on external and fiscal accounts, and the risk of tighter global financial conditions. The resilience factors outlined above should help mitigate the economic impact of the war in Iran. Furthermore, the continued presence of administered prices—particularly for energy—and long-term gas supply contracts should limit the pass-through of higher global fossil fuel prices to domestic inflation.

Nevertheless, considerable uncertainty remains regarding the duration and severity of the energy crisis and its economic consequences, even if the most severe phase of the conflict appears to have ended and the Strait of Hormuz is gradually reopening. Over the medium to long term, the liberalization and opening of the Uzbek economy pursued by the authorities represents a complex and lengthy process that may generate social challenges (such as pressures on purchasing power and rising inequality) as well as governance-related difficulties (including concentration of power and reform fatigue).

The authorities are navigating a complex geopolitical environment with flexibility

Located at the crossroads of Eurasia and endowed with substantial mineral resources (including gold, copper, molybdenum, selenium, lithium, cadmium, and rare earth elements), Uzbekistan occupies a strategic position. At a time of rising geopolitical tensions and a shifting global order, the country has adopted a multi-vector foreign policy aimed at expanding international partnerships while maintaining a balanced stance toward the major Eurasian powers. This multi-directional approach, while preserving pragmatic relations with both Moscow and Beijing, enables Tashkent to diversify its partnerships and strengthen its strategic autonomy.

The ongoing improvement in relations with other Central Asian countries represents a major shift. Historically marked by deep tensions over economic issues, territorial disputes, and resource management, Central Asia has, under Uzbekistan’s leadership, embarked on a positive trajectory toward greater cooperation. Breaking with the approach of Islam Karimov, the Uzbek authorities have adopted a “good-neighbor” policy. One of the most significant achievements has been the signing of the Khujand Treaty in 2025 with Tajikistan and Kyrgyzstan, bringing an end to longstanding border disputes. Other forms of cooperation are also expanding, including greater intra-regional investment and trade, as well as a more unified stance on the international stage. Such cooperation is critical given that the key challenges facing these countries are inherently regional in nature, including water, energy, climate, and security issues.

Pakistan: A Fragile Geopolitical Pivot Facing a New Economic Shock

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While Pakistan had experienced a marked macroeconomic improvement since the 2022–23 crisis, the conflict in the Middle East is generating new uncertainties and raising fresh challenges. Policy space remains limited to cope with rising hydrocarbon prices, supply disruptions, the potential weakening of public finances, and a resurgence of inflation. Positioned at the center of the geopolitical storm due to its role in negotiations between the United States and Iran, Pakistan could see its economy affected by significant headwinds in 2026 and 2027.

Early 2026 marked a geopolitical turning point for Pakistan. Less than a year after the April–May 2025 clashes with India (which were halted by a fragile ceasefire), Pakistan opened a new front by entering into conflict with Afghanistan in late February 2026 and found itself at the center of negotiations between a third neighboring country, Iran, and the United States. While these developments confirm Pakistan's role as a regional geopolitical pivot, they also entail significant economic and financial risks. The country's economy, which is only recently emerging from the 2022–23 crisis, remains fragile and highly exposed to the spillover effects of the conflict in the Middle East.

Economic stabilization since 2023…

In 2022–23, the global economic repercussions of the war in Ukraine significantly weakened Pakistan's economy, which was simultaneously facing a number of idiosyncratic shocks. Alongside rising hydrocarbon prices, higher interest rates, and a sharp decline in capital inflows, Pakistan was experiencing a period of intense political instability following the removal of Imran Khan and his government in April 2022. In addition, the country was hit by catastrophic floods, the cost of which was estimated at 9% of GDP. As a result, Pakistan's macroeconomic situation deteriorated sharply: recession in 2022–2023, depreciation of the PKR/USD exchange rate, surging inflation, widening twin deficits, erosion of foreign exchange reserves, and the introduction of capital and import controls.

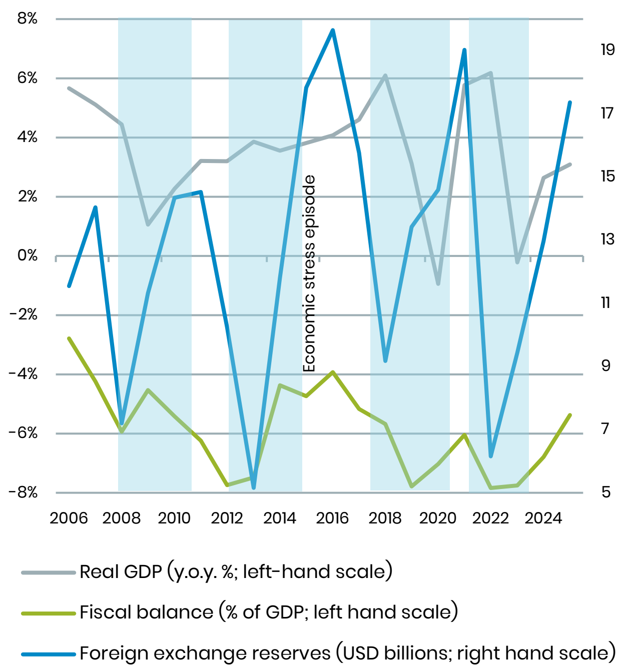
Since late 2023, however, conditions have improved, and Pakistan has entered a phase of consolidation. Supported by a new IMF program, the government of Shehbaz Sharif first succeeded in implementing a significant fiscal adjustment. The fiscal deficit was reduced from more than 7.5% of GDP to a level expected to be close to 3.2% of GDP in fiscal year 2025/26 (which ended in June 2026), allowing public debt to decline from 78% of GDP in June 2023 to 70% of GDP in June 2026. Meanwhile, lower imports and resilient workers' remittances led to a small current account surplus in 2025, which, combined with external financing, enabled a rebuilding of foreign exchange reserves from a low of USD 3 billion in January 2023 (equivalent to less than one month of goods and services imports) to USD 16.5 billion at end-2025. Finally, exchange rate and inflation dynamics stabilized, allowing the State Bank of Pakistan (SBP) to ease monetary policy by cutting its policy rate by 1,150 basis points (from 22% to 10.5%) between June 2024 and December 2025. These factors supported economic activity, with GDP growth reaching 3.1% in fiscal year 2024/25 and 3.6% in FY25/26.

…Amid the multiple risks of 2026

Pakistan is therefore confronting a new global geo-economic shock in a highly ambivalent context. Beyond the cyclical macro-fiscal adjustment, the country's economic model has undergone no major transformation that would shield it from the repercussions of the crisis in the Middle East. The 2022–23 episode was merely the latest in a long history of balance-of-payments crises (also experienced in 2008, 2013, and 2018) and recurrent boom-and-bust cycles.

This is particularly true in 2026, as the specific characteristics of the current shock could have significant consequences for the Pakistani economy through numerous transmission channels.

Figure 29 – An economy prone to recurrent economic crises



Source: IMF (WEO).

The first channel relates to higher hydrocarbon prices, as hydrocarbons account for 30% of the country's total imports, potentially exacerbating external imbalances. In 2022–23, the shock widened the trade deficit by approximately USD 6 billion between April 2022 and March 2023, contributing to the decline in reserves. Higher prices could also weigh on public finances through both direct and indirect subsidies. Since March 2026, the authorities have announced several measures aimed at limiting the impact on retail fuel prices, financed for the time being through the reallocation of other expenditures that have been frozen. Over the longer term, however, such an approach will be difficult to sustain without further increasing public indebtedness. Pakistan's public debt remains particularly costly: interest payments absorb nearly 50% of government revenues, which are themselves very limited (barely 16% of GDP in 2025). Finally, the international shock could intensify the inflationary pressures already observed since late 2025. Inflation has exceeded the SBP's target range of 5–7% since February 2026 and reached 11.7% in May 2026. In response, the SBP raised its policy rate by 100 basis points in late April 2026.

In addition, Pakistan's dependence on Gulf economies creates further vulnerabilities. Disruptions in the Strait of Hormuz are complicating oil and gas supplies, of which 80–90% originate from the Gulf region. Despite measures aimed at curbing energy and fuel consumption—and thereby reducing costs—the country has experienced shortages. These shortages are exacerbating an already difficult social environment and are likely to weigh on economic activity. Furthermore, workers' remittances from Gulf countries amount to approximately USD 20 billion per year (5% of GDP) and constitute one of Pakistan's main sources of foreign exchange, but these flows could decline as regional economic activity slows. Financial support from Gulf countries may also weaken. In early April 2026, the United Arab Emirates decided not to roll over a USD 3.5 billion deposit held at the SBP (which had been renewed annually over the previous seven years), forcing Pakistan to repay it. While continued IMF support (including a USD 1.3 billion disbursement in May 2026) and renewed access to international capital markets (Pakistan issued USD 750 million in Eurobonds in April for the first time in four years) help mitigate liquidity risks, the country has only limited buffers to absorb a reduction in external financing or a capital outflow episode. Foreign exchange reserves still cover less than three months of imports.

Pakistan is likely to continue benefiting from international support given the pivotal role it occupies in the region and its position as an intermediary in negotiations between the United States and Iran. Nevertheless, the macro-economic impact of a prolonged conflict in the Middle East could be substantial, exposing Pakistan to renewed pressures on its balance of payments, public finances, and economic growth.

Serbia: A Prolonged Period of Turbulence Amid the Middle East Crisis

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Despite structural constraints—including emigration, demographic decline, governance weaknesses, and a low value-added productive specialization—Serbia has maintained a favorable growth trajectory over the past decade, contributing significantly to the country's socioeconomic development. However, the deterioration of the rule of law, which is distancing the country from accession to the European Union, has generated social tensions that have manifested in sustained street protests since 2024. These tensions are amplifying the economic slowdown driven by a combination of domestic and external factors. Since early 2026, the impact of the crisis in the Middle East has added a further challenge through the inflation channel. Serbia nevertheless retains substantial policy space to confront these developments.

While preparations for International Expo 2027—which will bring together more than 130 countries in Belgrade next year—are progressing rapidly, clouds are gathering over the Serbian economy without calling into question the fundamentals that have underpinned its dynamism over the past decade.

Since 2016, Serbia has recorded solid economic performance, supported by its growing role in value chains as an exporter of manufactured goods to the European Union. Between 2018 and 2024, real GDP growth averaged 3.8% per year, one of the strongest performances in Europe, driven by both export growth and robust domestic demand. Private consumption benefited from rising average net wages (+13% annually since 2019), declining inflation since 2023, and falling unemployment, which reached a record low of 8.6% in 2024 (despite youth unemployment remaining elevated). Alongside Montenegro, Serbia is the Western Balkan country with the highest gross national income (GNI) per capita.

Sustained fiscal consolidation efforts, supported by a succession of IMF programs—including the current 2024–27 Policy Coordination Instrument, which does not involve financing—have enabled the country to strengthen its public finances and maintain the primary fiscal deficit within a range of 0% to 0.8% of GDP since 2023. As a result, the public debt ratio declined by 12 percentage points of GDP between 2020 and end-2025, reaching 42.4% of GDP (excluding government guarantees).

Despite a structurally large current account deficit (averaging -4.5% of GDP since 2021), Serbia rebuilt its international reserves, which more than doubled between May 2022 and early 2025, supported by export growth (+65% over four years), strong FDI inflows (averaging 6% of GDP over the past decade), and Eurobond issuances on international financial markets.

Sociopolitical disruptions amid worsened economic conditions

Since late 2024, however, the country has been facing a major sociopolitical crisis. Following the deadly collapse of the canopy at Novi Sad railway station, a movement initially led by students and now comprising a broad coalition of groups, emerged in protest against corruption and poor governance.[26] Its actions have included university occupations, road blockades, and large-scale demonstrations. Although the mobilization has weakened since the second half of 2025, it remains active, with demands now centered on the organization of early elections. Following the scale of the gathering held in Belgrade on May 23, President Vučić stated that elections could take place in the autumn.

[26] Since the Serbian Progressive Party came to power, the country has fallen 45 places in Transparency International's Corruption Perceptions Index (ranking behind only Belarus in Europe) and 25 places in the World Bank's Worldwide Governance Indicators ranking.

Among other factors, this prolonged social movement has contributed to economic disruption, reflected in the slowdown of growth from 3.9% in 2024 to 2.0% in 2025. Economic activity was also affected by adverse weather conditions (reducing wheat and fruit production), weak economic performance in Europe—the main market for Serbian exports—and lower FDI inflows across all sectors. FDI inflows were halved over the course of a year against a backdrop of global macroeconomic uncertainty, the end of the expansion cycle of Chinese investment in mining and manufacturing, and growing concerns related to the domestic sociopolitical environment.

In addition, the entry into force in October 2025 of U.S. sanctions linked to the Russian ownership structure of the oil company NIS, which is majority-owned by Gazprom, forced the closure of the country's only refinery for more than one month. At the end of January 2026, the government announced that the Hungarian company MOL had agreed to acquire all Russian-owned shares in NIS, but negotiations have yet to be concluded. They may last longer than initially anticipated and continue to pose risks to fuel supply should Washington's sanctions waivers not be renewed.

An economic recovery affected by the crisis in the Middle East

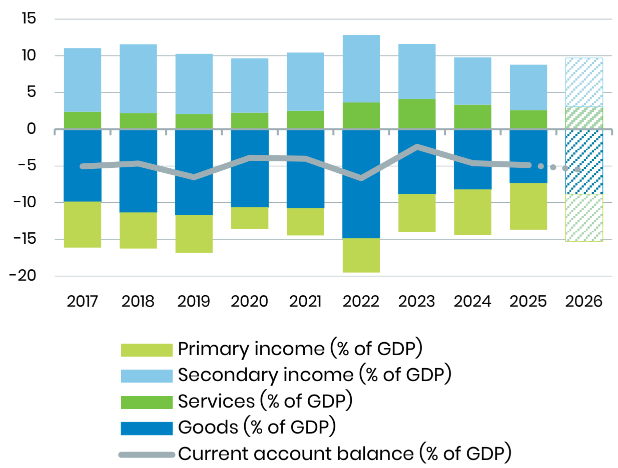
Economic performance in 2026 is expected to be affected by the spillover effects of the crisis in the Middle East. Growth, while improving relative to 2025, is projected to remain contained at 2.75%, according to the IMF's latest forecasts following the completion of the third review of the PCI program in early May. A return to more robust growth (4%) is now expected in 2027, notably supported by the economic spillovers associated with Expo 2027.

Since March 2026, inflation—which had only been contained in 2025 through controls on distributors' profit margins—has begun to edge upward again, reflecting higher fuel prices. Nevertheless, it remained within the central bank's target range (1.5%–4.5%), standing at 3.3% y/y in April, thanks to measures adopted by the government to mitigate the impact on consumers: a 20% reduction in fuel excise duties, caps on retail fuel prices, and a ban on oil exports. Under a scenario involving a prolonged disruption of traffic through the Strait of Hormuz, the central bank could be compelled to raise interest rates if inflation accelerates, while the government may need to strengthen subsidy measures.

As a result, the EUR 48 billion economic development plan unveiled on March 7—which aims to support infrastructure, defense, digitalization, and artificial intelligence through 2035—could become a fiscal adjustment variable should the situation deteriorate further. Indeed, the Serbian government is committed to maintaining the fiscal deficit below 3% of GDP. However, the deficit widened slightly in 2025 to 2.4% of GDP and is expected to increase further in 2026.

The country's economic openness could also serve as a transmission channel through which the conflict affects the balance of payments. Higher import costs will weigh on the trade balance, which had reached a historically favorable level in 2025, and on the current account deficit, which could widen to 5.7% of GDP in 2026 according to the IMF, compared with 4.9% of GDP in 2025 and 6.5% of GDP in 2022 during the previous energy shock triggered by the war in Ukraine. As in 2025, international reserves may be called upon to absorb these pressures. The exchange rate regime—de jure managed floating against the euro and de facto a stabilized arrangement—remains sustainable, supported by an adequate monetary policy framework and ample foreign exchange reserves.

Figure 30 – The deterioration of the current account deficit could intensify in 2026 as import costs rise (% of GDP)



Source: IMF, EIU, ECO calculations.

List of acronyms and abbreviations

ADQ	Abu Dhabi's Sovereign Wealth Fund
ART	Agreement on Reciprocal Trade
ASEAN	Association of Southeast Asian Nations
BB	Bangladesh Bank
BoU	Bank of Uganda
EAC	East African Community
EMDEs	Emerging market and developing economies
FDI	Foreign direct investment
Fed	Federal Reserve
FOMC	Federal Open Market Committee
GDP	Gross domestic product
GNI	Gross national income
IEA	International Energy Agency
ILO	International Labour Organization
IMF	International Monetary Fund
LNG	Liquefied natural gas
PMI	Purchasing Managers' Index
NBFI	Non-bank financial institutions
NNPC	Nigerian National Petroleum Company
ODA	Official development assistance
OE	Oxford Economics
SBP	State Bank of Pakistan
USAID	United States Agency for International Development
USMCA	United States–Mexico–Canada Agreement
y/y	year-on-year

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