

SCÉNARIOÉCO

Société Générale Economic & Sector Studies

Excessive imbalances

- **US policies have increased uncertainty and fragmentation**, driving a reorganisation of value chains. Geopolitical risks remain elevated. We make the working assumption of no geographical expansion of current conflicts.
- **This continues to weigh on households and business confidence**. As a result, our scenario remains dominated by weak growth in the coming two years. We expect inflation to remain within central banks' targets allowing very gradual monetary easing.
- **We see further Fed rate cuts and one last cut for the ECB**. The Fed focus is shifting from price stability to employment. ECB monetary stance is expected to remain neutral pursuing the QT into 2026 (and possibly beyond).
- **Worries on fiscal trajectories and threats to central bank independence and will weigh on term premia**. The combination of persistent high long-term rates and slow world growth increases the risks of markets correction and financial instability.
- **The outlook for France reflects uncertainty regarding its budgetary trajectory** and the rise in public debt. The appointment of the new Prime Minister has not yet restored a clear dynamic, with the risk of delaying the path of budgetary consolidation.
- **China will continue to suffer from overcapacity and sluggish consumption, feeding deflationary pressures**. Authorities are wary of excess supply, which weighs on investment. China's excess export capacity is likely to lead to protectionist measures from importer countries.

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EDITORIAL

SLUGGISH GROWTH TO LAST

Global growth remains sluggish. The first half of the year was supported by front loading effects related to uncertainties over US tariffs. In most countries domestic demand is weak and the lift to the first half of the year on international trade and inventories build are likely to wane in the coming quarters. The headwinds come from uncertainty, tariffs and demographics, and the policy mix is not supportive. Despite rate cuts the monetary stance is not yet expansionary and fiscal constraints will continue to weigh in various countries. As such, we continue to expect growth to decelerate in 2026 in all major economies.

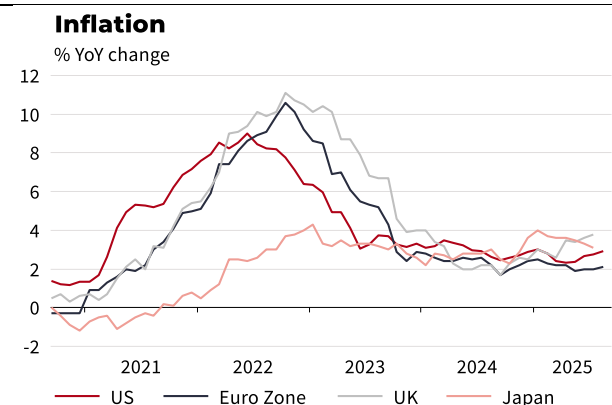
In the US, tariffs have begun to stabilize at a level 13% higher on average than 2024, but uncertainty remains elevated. Recent employment data suggest that the US is reaching an inflection point where significant layoffs may now follow. Our concern remains that a more substantial slowdown is about to unfold. It is worth note, moreover, that weaker labour supply due not least to weaker immigration, has helped keep the unemployment rate low even as job creation has slowed. Here too we see an inflection point and expect US unemployment to move higher over the coming quarters, opening to more Fed rate cuts. In this context, we remain below consensus on US growth with a marked slowdown in 2026 and 2027.

In the euro area, consumer and business confidence remains weak, resulting in sluggish credit growth. Intra-region dynamics are different as France and Italy lag, Germany is expected to benefit from public investment in the coming years, while Spain is benefiting from positive demographic dynamics related to migrant population contributing to domestic demand.

Growth on one leg: services



Inflation to get back to range



Sources: LSEG, SG Economic and Sector Studies

In China, the activity is moderating. Economic growth should reach 4.7% in 2025 and slow to 4.2% in 2026. Exports should start to be curbed by the tariffs with the US. The policy mix will remain accommodative and incremental but is not expected to

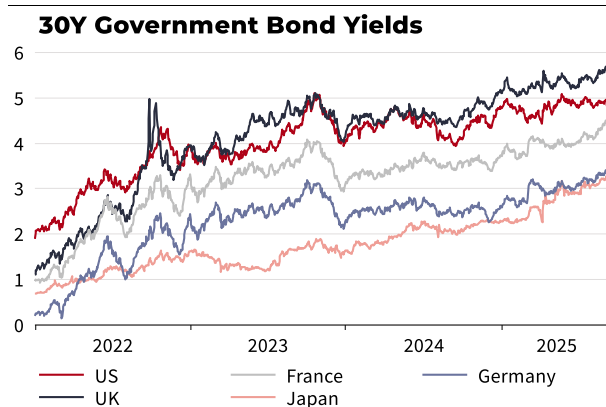
provide a structural solution to current overcapacities. The real estate correction continues. Despite strong growth on international markets the automobile sector is suffering from overcapacities and price war domestically.

RIISING TERM PREMIA REFLECT MARKETS NERVOUSNESS ON PUBLIC FINANCES

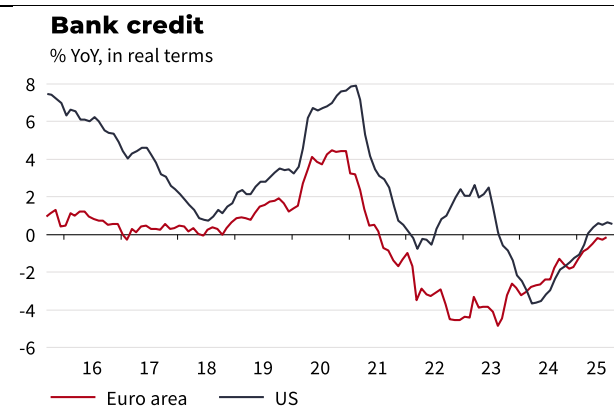
Markets are showing growing nervousness about fiscal trajectories across the board putting pressure on long term interest rates. In a context of relatively well anchored inflation expectations as witnessed by markets pricing, still high long-term interest rates are reflecting higher term premia that seem to be related to indebtedness trajectories of many countries and elevated uncertainties. Threats to central bank independence (via fiscal dominance) could also weigh on term premia. In the US, the perceived erosion of Fed independence is an additional challenge. This is leading markets to test the long end of yield curves with 30 years maturities reaching record highs (highest on more than 25 years for UK and Japan, and highest in more than 15 years for Germany and France).

Medium term challenges (ageing population, transition, defence, digital transformation) will weigh on fiscal accounts and maintain structurally higher term premia. This could contribute to slow and make more difficult the transmission mechanism of the monetary policy, not least as the quantitative tightening is ongoing.

Higher costs of funding...



...damage monetary policy transmission



Sources: LSEG, SG Economic and Sector Studies

The combination of lacklustre growth and the persistence of high interest rates is increasing the risks on potential financial markets correction. In this context, several risks worth being closely watched.

- Doubts on the efficiency of massive AI investment and valuations in the tech sector are rising and could hurt US asset prices and growth
- Institutional worries on in the US not least related to the Fed's independence could trigger financial stability issues related to the erosion of the pivot role of the dollar.

- Uncertainties on France's fiscal trajectory have increased, and further market tensions cannot be ruled out.

We assume no further geographic expansion on ongoing conflicts even though geopolitical risks remain high with Russia-Ukraine, Israel-Gaza ongoing wars, Chinese sea tensions, episodic clashes (India-Pakistan, Thailand-Cambodia), US operations on Venezuela coasts, record refugee crisis.

ECONOMIC FORECASTS

GDP, % YoY	2025f	2026f	2027f	2028f
Developed Markets	1.6	1.2	1.2	1.5
United States	1.7	1.4	1.0	1.8
Japan	1.0	0.7	0.7	0.6
United Kingdom	1.3	1.0	1.2	1.2
Euro area	0.9	0.8	1.0	1.3
Germany	0.3	1.1	1.3	1.6
France	0.6	0.6	0.9	1.3
Italy	0.6	0.5	0.5	0.8
Spain	2.6	1.8	1.6	1.6
Emerging Markets	4.0	3.6	3.6	3.6
Asia	4.9	4.3	4.3	4.3
China	4.7	4.2	4.0	3.8
India	6.5	6.1	6.4	6.5
Central and Eastern Europe	1.8	1.5	1.5	1.5
Latin America	2.3	2.0	2.1	2.2
Brazil	2.3	1.1	1.7	2.3
Middle East and Central Asia	3.5	3.5	3.1	3.1
Africa	3.5	3.8	3.8	3.8
World (PPP weighted)	3.1	2.7	2.7	2.8

CPI, % YoY, avg	2025f	2026f	2027f	2028f
Developed Markets	2.9	2.4	2.2	2.0
United States	3.2	2.9	2.6	2.6
Japan	3.4	1.8	1.5	1.5
United Kingdom	3.5	2.6	2.1	2.1
Euro area	2.1	2.0	1.7	1.9
Germany	2.0	2.0	1.9	1.9
France	1.3	1.6	1.7	1.9
Italy	2.0	1.8	1.7	1.9
Spain	2.5	2.2	1.8	2.0
Emerging Markets	5.5	4.9	4.4	4.3
China	0.3	1.0	1.2	1.5
India	4.3	4.5	4.5	4.5
Brazil	5.1	3.9	3.3	3.5

FINANCIAL FORECASTS

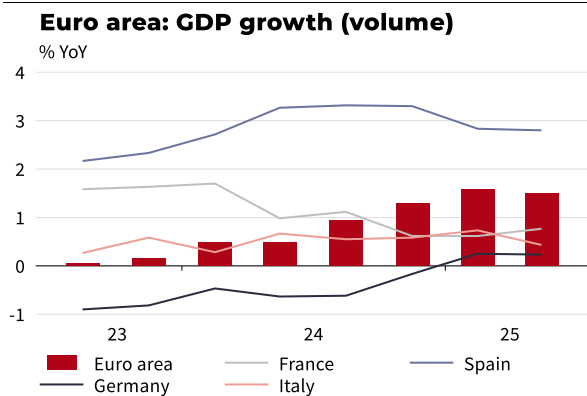
%, EoP (unless otherwise indicated)	Latest 17/09	2025f	2026f	2027f	2028f
Fed Funds target (high)	4.50	4.00	3.25	2.75	3.00
Gov 10Y, US	4.03	4.35	4.00	4.25	4.25
ECB Deposit facility rate	2.00	1.75	1.75	1.75	2.25
Gov 10Y, Germany	2.69	2.85	2.50	2.75	2.75
Gov 10Y, France	3.49	3.65	3.30	3.45	3.35
Gov 10Y, Italy	3.51	3.75	3.40	3.65	3.65
Gov 10Y, Spain	3.25	3.50	3.15	3.40	3.35
BoE, Bank rate	4.00	4.00	3.75	3.50	3.75
Gov 10Y, United Kingdom	4.64	4.90	4.50	4.50	4.50
BoJ, Bank rate	0.50	0.75	1.00	1.00	0.80
Gov 10Y, Japan	1.60	1.65	1.50	1.50	1.45
EUR / USD	1.19	1.20	1.20	1.20	1.15
EUR / GBP	0.87	0.86	0.87	0.87	0.87
USD / JPY	147	145	140	135	140
USD / CNY	7.1	7.2	7.4	7.3	7.1
Oil Brent (USD/b)	69	65	65	70	70
European Natural Gas (TTF, EUR/MgW/h)	32	35	40	40	40
EU ETS carbon (EUR/Metric ton)	77	80	100	110	120

EURO AREA

- Despite better performance in early 2025, growth is only expected to pick up speed after 2027
- After one more expected rate cut in 2025, we anticipate the ECB to pause over the next two years
- The EU-US trade agreement reduces uncertainty in the short term, but trade frictions will remain a drag on the economic outlook

The euro area is entering 2H25 with a mix of resilience and fragility. While headline indicators suggest stability, underlying dynamics reveal a region grappling with uneven performance between countries, subdued confidence, and policy recalibration. Growth is expected to remain modest in 2025-26, constrained by muted manufacturing and consumer sentiment, persistent trade frictions with the US, and the ongoing impact of quantitative tightening. We expect Spain and the periphery to continue to outperform, while France, Germany, and Italy face persistent softness. As Germany's fiscal expansion takes effect and political stability returns to France, we anticipate a gradual acceleration in euro area growth over the medium term, reaching 1.0% in 2027 and 1.3% in 2028, with a more balance contribution across member states.

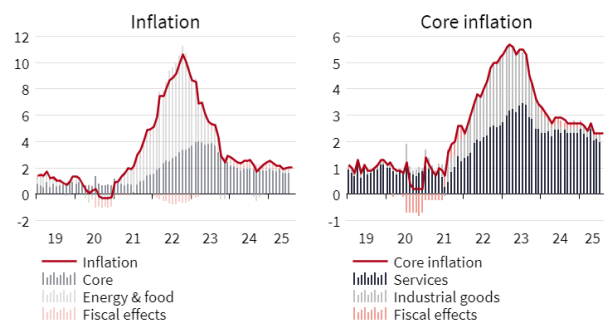
Spain continues to significantly outperform the rest of the euro area



Inflation stabilized due to energy prices, but core inflation remains sticky

Euro area: inflation breakdown

As of % and pp. contributions



Source: Eurostat, INSEE, Destatis, INE, Istat, SG Economic and Sector Studies

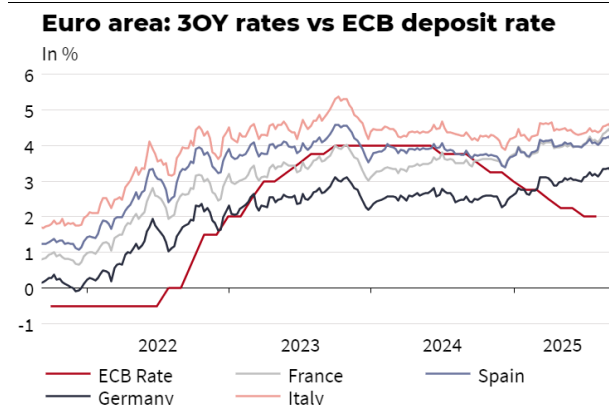
Inflation is expected to remain around target throughout late 2025 and 2026.

The convergence to the 2%-target will continue to find support from further wage growth moderation. The ECB's wage tracker suggests a continued slowdown in wage growth from 4.4% in 1Q25 of this year to 2.6% in 1Q26. We expect further disinflation pressure coming from a strong EUR, while energy and food prices finalize their normalization. In the absence of further shocks, inflation is expected to remain slightly below target in the medium term.

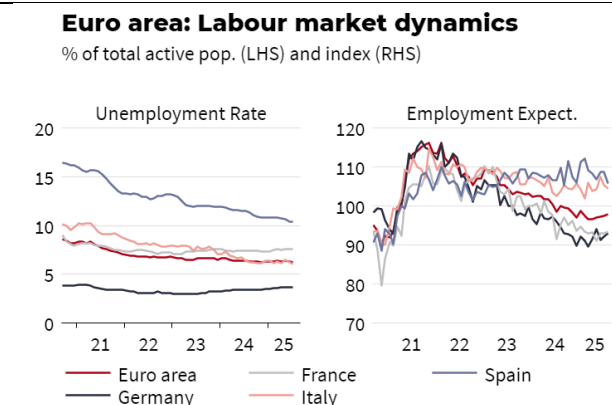
We anticipate the ECB will implement a final rate cut in 2025 in response to downside risks to economic activity. This would mark the fifth rate reduction that year, bringing the euro area's deposit facility rate down to 1.75%. In our central scenario, this cut is expected to conclude the current easing cycle. However, the easing of financial conditions will be limited by upward pressure on long-term yields, driven by quantitative tightening's impact on liquidity and market skepticism regarding the fiscal frameworks of several major economies.

Intra-bloc divergences are expected to exert a negative impact on the previously resilient labour market. In July, euro area unemployment reached the historic low of 6.2%. While the labour market remaining virtually unchanged throughout the first half of 2025 suggests overall robustness, the strong performances of Italy and Spain mask the struggles faced by France and Germany. The split is also not expected to disappear as hiring intentions between the four economies continue to bifurcate. Over the short term, we expect an uptick in unemployment in France and Germany and a stable outlook in Spain and Italy.

Long-term yields are defying the easing cycle and are raising borrowing costs



The Euro area labour market is stable, but the outlook of core countries gives rise to concern



Source: LSEG, ECB, Eurostat, DG ECFIN, SG Economic and Sector Studies

The EU-US trade agreement will provide some certainty, once signed. Tariffs on EU exports to the US are reduced to 15% on most goods, including cars, pharmaceuticals, or spirits and wine. However, steel and aluminium sectors will continue to face levies of 50%. In return for the revision of tariffs, the EU offered to reduce its own tariffs, including on US seafood and agricultural products, favourable terms in cooperation on digital services trade, along with large-scale investments in the US. The latter includes additional USD 600bn across strategic sectors in the US and the import of US fossil and nuclear energy products worth USD 750bn. The trade agreement still requires adoption in the EU Parliament, to be voted on in October 2025 at the earliest, and then in national parliaments. The approval process might be subject to potential amendments, leaving residual uncertainty.

On aggregate, the fiscal outlook points towards consolidation, despite political uncertainty, higher interest payments, and defence spending. In France, the outlook depends on newly appointed PM Lecornu's ability to build minimum consensus on

the 2026 budget. Italy and Spain are expected to consolidate with a higher degree of certainty. Germany is projected to counteract this trend given large defence and infrastructure spending. Given these country-specific developments, paired with higher defence spending and rising borrowing costs across the EU, we expect consolidation to only take effect by 2027. The euro area fiscal deficit is then anticipated to shrink to 3.3% down from 3.6% in 2025 and 2026.

Domestic challenges and trade frictions tilt the risk balance of this scenario to the downside. Challenges within the bloc's two largest economies, France and Germany, risk becoming a drag on the EU's growth outlook if not addressed comprehensively. The absence of political agreement in France could trigger gridlock ahead of the 2027 presidential elections, while weak stimulus implementation in Germany may undermine economic transmission and public trust. On the international front, trade frictions and a sudden depreciation of the currently strong EUR could pose additional inflationary risks.

Euro area	2025f	2026f	2027f	2028f
Real GDP, % YoY	0.9	0.8	1.0	1.3
Household consumption	0.9	0.6	0.7	1.2
Public consumption	0.8	0.6	0.8	1.0
Investment	1.1	1.7	2.0	2.2
Exports of goods & services	0.2	1.5	2.2	2.3
Imports of goods & services	1.7	2.1	2.4	2.6
Inflation, % annual average	2.1	2.0	1.7	1.9
Core inflation, % annual average	2.3	1.8	1.7	1.9
Real gross disposable income (GDI), % YoY	0.4	0.6	0.7	1.0
Households saving rate, % of GDI	15.0	15.0	15.0	14.9
Unemployment, % of labour force	6.5	6.6	6.6	6.5
Fiscal balance, % of GDP	-3.6	-3.6	-3.3	-3.1
Public debt, % of GDP	91	93	94	94
Current account balance, % of GDP	1.7	1.4	1.4	1.2

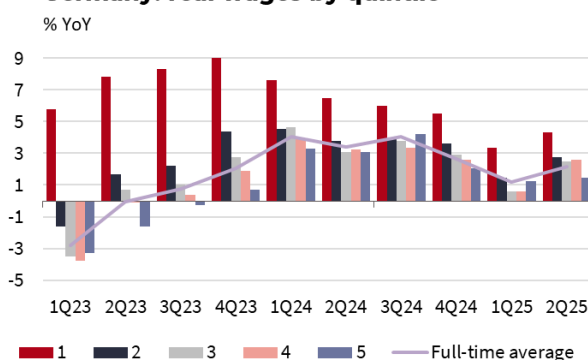
GERMANY

- **Recovery hinges on the rebound of domestic demand driven by rallying household revenue and investment**
- **Significant external rebalancing is expected as export drag persists under the weight of a strong EUR, weak productivity growth, US tariffs and shifts in the competitive landscape, not least with China**
- **The implementation of the fiscal package will be progressive, with consolidation efforts expected in the last years of the decade**

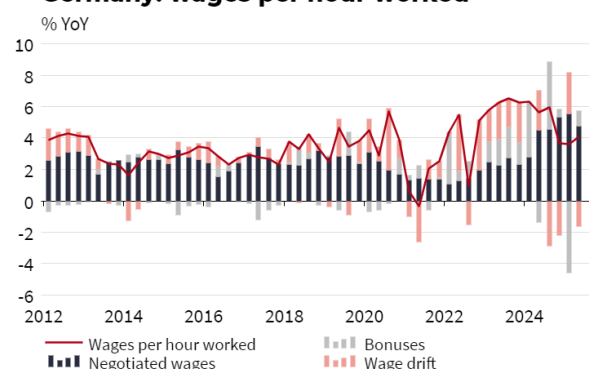
Recovery is nascent but fragile (0.3% in 2025) as structural headwinds and a challenging international environment persist. The manufacturing recession continues but leading indicators hint that the sector having bottomed in 2025. It is expected to sustain a smaller part of the economy moving forward. Industry continues to face meagre productivity gains, rising costs and heightened competition from international producers, aggravated by a strong EUR, reduced demand from China and the materialisation of US tariffs. The trade agreement between the US and the EU eases some of the uncertainty on the economy, lifting latency in the short term. However, it is set to durably reshape addressable markets as the average US tariff rate has increased from around 2 to 17%. Few sectors are subject to exceptions (e.g. pharmaceuticals, automobiles) that cap at 15% the tariff when higher tariffs would otherwise apply to certain products. Importantly, steel and aluminium remain subject to the 50% rate, including in transformed goods containing those elements, as most capital goods do. Uncertainty from US policy is set to persist (c.f. US section).

Gains in wages have been concentrated in lower income quintiles... ... and driven by hikes in the minimum wage set to increase an additional 13.5% by 2027

Germany: real wages by quintile



Germany: wages per hour worked



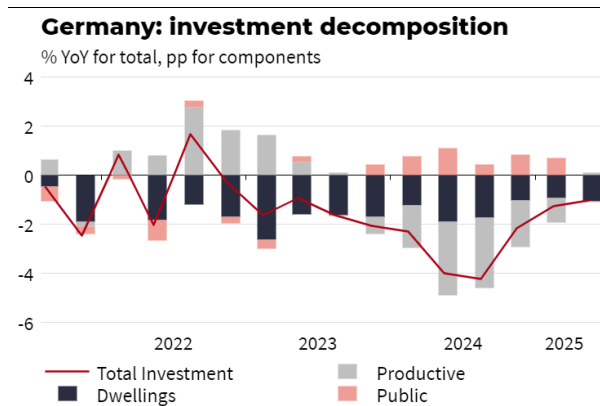
Source: Destatis, SG Economic and Sector Studies

Source: Eurostat, SG Economic and Sector Studies

The recovery of household purchasing power will bring a rare tailwind, lifting consumption. Wages are expected to maintain a dynamic trend, following the trajectory of negotiated wages. This will contribute to the stickiness of core inflation and support the acceleration of consumption. The latter is particularly salient as the

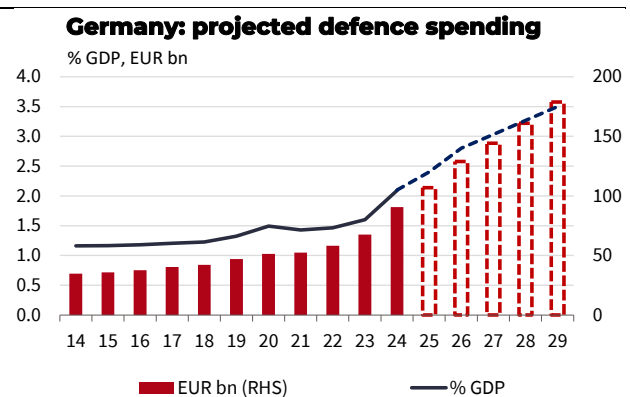
lower income quintiles -those with the highest propensity to consume- are the households that have seen the sharpest increases in real wages. The announced increases in the minimum wage to EUR 14.6 per hour by 2027 (+13.5%), will continue to support this trend even as the labour market softens. Unemployment is expected to peak over the next six months and will persistently face labour shortages especially in skilled segments as demographics continue to deteriorate, further supporting wage growth. Downward pressures on inflation will persist given the strength of the EUR and the rapid normalization of energy and food prices which will improve purchasing power and reduce precautionary consumer behaviour. This supports the pick-up in consumption and a gradual normalization of saving rates over the rest of the decade contributing to the rebalancing of the economy in favour of domestic demand.

The fiscal package is reliant on the pick-up of both public and private investment



Source: Destatis, OECD, SG Economic and Sector Studies

Flexible national and EU fiscal rules allow defence spending to reach 3.5% of GDP in 2029



Source: NATO, BMF, SG Economic and Sector Studies

Fiscal policy will remain expansionary driven by the rollout of the investment package and increased military expenditure. However the implementation will face supply-side frictions and bureaucratic hurdles. Announced hikes in military expenditure, set to nearly double by 2029 to reach 3.5% of GDP, are supported across the political spectre and are enabled by flexibility in national and European rules to avoid crowding out other spending. Investment is at the centre of the fiscal boost as 60% of the EUR 500bn Special Fund for Infrastructure and Climate Neutrality (SVIK) is earmarked for national infrastructure while EUR 100bn will fund state-level projects and the Climate Transformation Fund (KTF) respectively. These funds, excluded from debt brake, will contribute to the acceleration of investment in the second half of the decade. A recovery in private investment rate is also expected (+1pp of GDP between 2024 and 2028) as sentiment improves as growth returns, monetary easing strengthens the credit impulse, and policies are implemented to make investing more attractive (e.g. temporary changes to depreciation rules for plants and equipment, and the gradual announced reduction of corporate tax rate by 5pp by 2032). Moreover, the turnaround in construction investment -a persistent drag for the component since the pandemic- will take place at an even lower point following significant revisions in the data. The pickup is expected over the next year,

as residential prices continue to slowly recover, input prices drop, and construction is incentivized by public policy cutting red tape and accelerating civil engineering projects.

The balance of risks remains mixed. On the upside, dynamic domestic demand could outperform expectations if household and corporate spending continue to strengthen on the back of recovering sentiment. Efficient deployment of public funds under the fiscal package would amplify the growth impulse, while political alignment may enable long-overdue structural reforms, particularly those aimed at increasing labour supply from underutilised segments such as women and older workers. Emerging trade partnerships (e.g. Mercosur, Mexico, Central Asia) could also support export diversification, even if the aggregate impact remains modest. On the downside, poor implementation of the fiscal package would not only weaken its transmission but also heighten public mistrust. Concerns around fiscal dominance could reintroduce inflationary pressures, prompting precautionary behaviour and tightening financial conditions. This would raise the government's interest burden and weigh on long-term lending rates, e.g. mortgages threatening the recovery in construction. External risks including persistent trade tensions and subdued global demand further cloud the outlook.

Germany	2025f	2026f	2027f	2028f
Real GDP, % YoY	0.3	1.1	1.3	1.6
Household consumption	1.1	1.2	1.2	1.4
Public consumption	2.2	1.9	1.5	1.2
Investment	-0.5	3.1	3.4	3.7
Exports of goods & services	-0.5	1.1	1.3	1.9
Imports of goods & services	2.8	2.2	2.2	2.5
Inflation, % annual average	2.0	2.0	1.9	1.9
Core inflation, % annual average	2.5	2.0	1.9	1.9
Real gross disposable income (GDI), % YoY	0.9	1.0	1.1	1.2
Households saving rate, % of GDI	19.9	19.7	19.6	19.3
Unemployment, % of labour force	6.4	6.4	6.3	6.1
Fiscal balance, % of GDP	-3.0	-3.2	-3.2	-3.4
Public debt, % of GDP	65	67	68	70
Current account balance, % of GDP	4.9	4.5	4.3	4.1

FRANCE

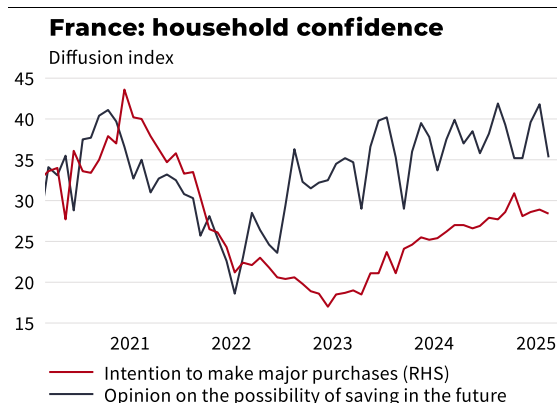
- **Economic momentum remains subdued, with fragile domestic demand and heightened political uncertainty**
 - **Labour market conditions are deteriorating amid corporate restructuring and the withdrawal of support measures**
 - **Political divisions and social tensions as well as the rising debt servicing costs complicate the path toward fiscal consolidation**
-

France is entering a phase marked by heightened political uncertainty, a slowdown in economic momentum, and persistent structural imbalances. The fall of the government underscores the volatility of the current political landscape, even if institutional continuity has so far been preserved. While a full-blown budgetary crisis has not materialized, the ability to deliver coherent fiscal policy is increasingly constrained by fragmentation and polarization.

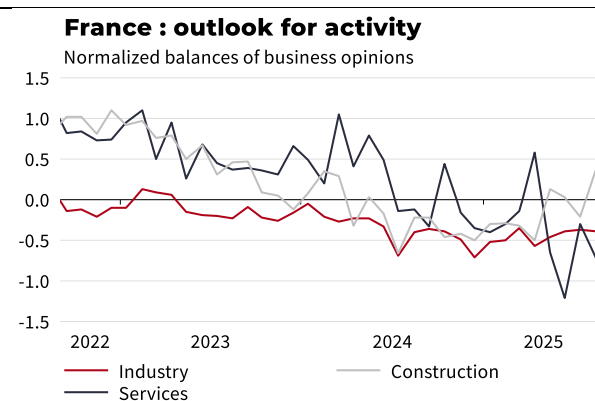
Political tensions escalated following the loss of the confidence vote on September 8, which led to the resignation of Prime Minister François Bayrou. The appointment of Sébastien Lecornu on September 9, 2025, opens a new chapter, but does not dispel uncertainty about the government's ability to pass a budget within the required timeframe. While our baseline scenario had anticipated a difficult path toward the 2026 budget, the timeline has now accelerated. A draft budget is expected to be presented to the Council of Ministers in October, then submitted to the National Assembly. The constitutional constraint remains: the Assembly must have 70 days to examine the text, which requires submission no later than mid-October. Beyond technical challenges, the budget preparation is unfolding amid elevated social tensions. The government's ability to secure a parliamentary majority remains uncertain. It may be forced to resort to a special law, similar to the one passed end 2024 to ensure continuity of revenue and expenditure.

This political instability, combined with parliamentary fragmentation and growing social mobilization, weighs on economic sentiment. Households and businesses are responding to this climate of uncertainty with greater caution, which is dampening consumption, delaying investment decisions, and fuelling a slowdown dynamic. As uncertainty persists and policy inertia limits the scope for stimulus. The unemployment rate is expected to approach 8%, weighing on household morale. Despite inflation falling below the 2% threshold, purchasing power will remain constrained due to weak real wages and a high level of precautionary savings. A gradual recovery is anticipated in 2027, contingent on improved political clarity and external conditions.

Household demand will remain subdued with elevated precautionary savings



Business sentiment remains fragile, reflecting persistent uncertainty



Source: Refinitiv, DGEFCFIN, Economic and Sector Studies

Domestic demand is expected to remain weak, reflecting subdued household consumption, delayed investment recovery, and rising unemployment. Private consumption will be constrained by modest real income gains, labour market slack, and heightened political uncertainty. Household investment should slightly rebound, supported by easing financial conditions and targeted housing incentives in the 2025 Finance Bill. Business investment will strengthen only from 2027 onward, as firms respond to improving sentiment, and a gradual rollout of regulatory reforms. These include measures from the 2025 Finance Bill such as adjustments to the R&D tax credit, and a postponed repeal of the Business Contribution on Added Value (BCAV) — as well as sectoral initiatives announced at the Choose France summit, which targeted industrial decarbonization and digital infrastructure investment. Public investment will remain constrained by fiscal rules and rising interest costs, though selective support from EU-level funding and green transition priorities offers some support.

The labour market is expected to deteriorate further, with unemployment rising to around 8% in 2026–27. Job creation is slowing, particularly due to the expiration of apprenticeship subsidies that had supported youth employment in recent years. Additionally, businesses facing uncertain demand are prioritizing productivity optimisation, further limiting employment growth. Concerns about unemployment remain high, driving greater household caution and sustaining a high savings rate.

Foreign trade faces structural headwinds from global trade tensions, regulatory divergence, and geopolitical instability. A significant constraint on export performance stems from escalating tariffs imposed by the US. Under a renewed protectionist stance, the US has introduced broad-based duties on EU goods of 15%, with French exports—particularly in high-value sectors such as aerospace, wine, and luxury goods—bearing the brunt. These tariffs will erode price competitiveness, disrupt supply chains, and dampen demand from one of France's largest non-EU trading partners. As a result, the external sector's contribution to growth will remain subdued, with limited upside in the medium term. The current account balance will

thus deteriorate moderately, limiting France's ability to build buffers against future shocks.

Our forecast budget trajectory is insufficient to reverse key imbalances. Public debt will remain on a rising trend, and the general government deficit will narrow only gradually. While short-term sovereign risk could be mitigated by favourable financing conditions and ECB support mechanisms, long-term fiscal sustainability risks intensify due to structural spending pressures and limited growth acceleration. Without meaningful reform, it will be difficult to correct the fiscal trajectory.

Risks to the growth outlook remain tilted to the downside. Domestically, mounting political tensions could lead to legislative gridlock, undermining investor confidence and delaying key fiscal decisions. This uncertainty may reinforce wait-and-see behaviour among businesses and households, dampening consumption and investment. Externally, renewed trade frictions—particularly protectionist measures from President Trump—pose a serious threat to French exports. If these pressures intensify or expand to additional sectors, France could face a dual shock: weakening external demand and constrained domestic policy space, heightening the risk of prolonged economic stagnation.

France	2025f	2026f	2027f	2028f
Real GDP, % YoY	0.6	0.6	0.9	1.3
Household consumption	0.7	0.7	0.9	1.2
Public consumption	0.9	0.1	0.6	1.0
Investment	0.1	1.2	1.4	2.0
Exports of goods & services	0.7	1.6	2.6	2.7
Imports of goods & services	1.7	2.7	2.7	2.9
Inflation, % annual average	1.3	1.6	1.7	1.9
Core inflation, % annual average	1.8	1.8	1.8	2.0
Real gross disposable income (GDI), % YoY	0.7	0.5	0.4	0.6
Households saving rate, % of GDI	18.2	17.9	17.5	16.9
Unemployment, % of labour force	7.8	8.1	8.0	7.8
Fiscal balance, % of GDP	-5.7	-5.2	-4.8	-4.3
Public debt, % of GDP	116	119	120	121
Current account balance, % of GDP	-0.3	-0.5	-0.4	-0.4

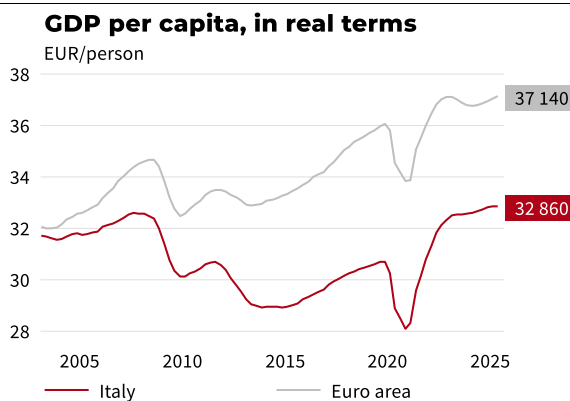
ITALY

- **GDP per capita has surpassed its 2007 peak level, but the catch-up process has stalled, and economy is set to grow more slowly**
- **Italy is one of the most vulnerable countries in Europe to the US tariffs given its close trade relations with the US**
- **Higher than expected tax revenues are supporting the primary fiscal surplus, just enough to stabilise public debt at 140% of GDP**

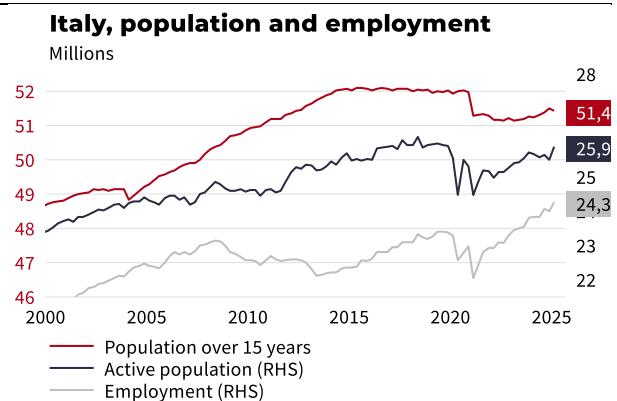
The economy is set to grow more slowly in 2025-26 given US tariffs and some delays in recovery-plan investments. Still, reforms and continuing EU-fund deployment should support medium-term growth after 2026. The economy has proved relatively resilient since the end of the Covid pandemic, benefitting from its large and diversified industrial base and export sector. GDP per capita is now back to its 2007 peak level, and 7% above pre-Covid crisis (versus 3% for the euro area).

However, Italy is one of the most vulnerable countries in Europe to the potential consequences of a trade war given its close trade relations with the US. The growing importance of the US as an export market for Italian manufacturers over the past five years has led to a substantial bilateral goods trade surplus, estimated at around EUR 39bn. Only Germany and Ireland have bigger goods surpluses with the US among euro area countries.

Growth has stalled after a rapid post-Covid recovery, but employment is still buoyant



Source: Eurostat, LSEG, SG Economic and Sector Studies



Source: Istat, LSEG, SG Economic and Sector Studies

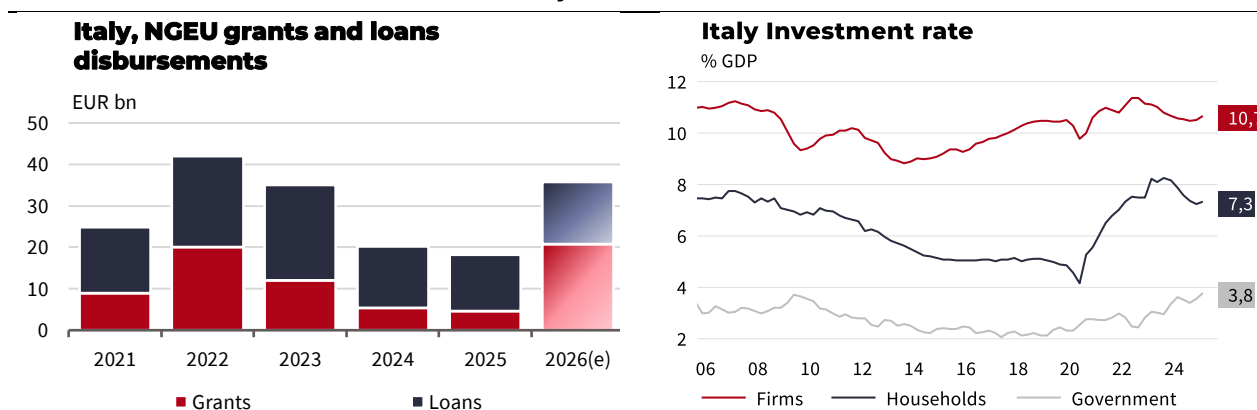
Despite weak demographic trends, employment is still leading the recovery at the expense of productivity. The unemployment rate has reached a record low since 2007 at 6% of active population, driven by strong job creation (+283,000 persons over one year) in services (trade, accommodation and catering, & professional, scientific and technical services). On the other side, productivity by hour worked has declined by 4% since pre-Covid levels, weighing on profit margins. Unemployment is set to increase slightly in the coming years, as the economy decelerates, and firms reconstitute their margins.

External demand is weighing on growth as investments are rich in imports.

Given global trade tensions, Italy's efficient deployment of EU recovery funds becomes even more important for sustaining domestic economic growth. Of the EUR 194bn allocated to Italy under the facility, the country has so far received EUR 140bn, equivalent to 72% of the total resources. Most resources to date have been allocated for tax credits, railway and school infrastructure projects. However, spending such a substantial sum has proved challenging, with estimated expenditure standing at only 30% of the total allocation according to Confindustria.

Lower-than-expected annual spending of allocated funds has also reduced the potential stimulus for the economy.

In 2021 the government projected a cumulative impact of 2.4pp of additional real GDP growth for 2021-2024, which was revised to 1pp in 2024. Most of the economic stimulus is now expected in 2025-26, with an estimated cumulative impact of 2.7pp of additional real GDP growth. However, this implies exceptionally high expenditure of EUR 37bn in 2025 and EUR 49bn in 2026, which is unlikely. Moreover, by the end of 2026, most of the EUR 194bn will be allocated to projects that are then implemented in subsequent years. The recovery plan's capacity to stimulate Italian GDP growth will be spread over a longer period than initially projected.

EUR 35bn worth of funds to be disbursed by end 2026

Source: European Commission, RRF scoreboard, SG Economic and Sector Studies

Source: Istat, LSEG, SG Economic and Sector Studies

"Italy is making very serious budgetary efforts and will probably exit from the EU excessive deficit procedure, getting soon to a deficit of 3%", said **Christine Lagarde** in Paris on 1st September 2025. In April, the government pledged to cut the deficit to 3.3% of GDP this year from 3.4% in 2024, and to 2.8% in 2026. But Italy could bring its deficit below 3% of GDP as early as 2025, paving the way for exiting the EU procedure in 2026, one year ahead of schedule.

Efforts to curb tax evasion are beginning to bear fruit. In 2024, public revenues exceeded the October 2023 forecasts by EUR 43bn. Early indications for 2025 suggest that tax and social security revenue might exceed forecasts again this year by EUR 26bn compared to the figures in the Public Finance Document released in April. Both better tax collection and a solid labour market are possible explanations.

However, if the primary balance has turned positive at 0.4% of GDP in 2024, it is still far from reaching a 2% surplus, a necessary condition for the downward trend in public debt. The budget deficit is expected to decrease very gradually from 3.5% in 2024 to 3.0% in 2028 thanks to moderate primary spending and broadly stable interest expenditure.

Public debt is set to resume an upward trajectory in 2026 and 2027. Past interest rate hikes and weak growth will weigh on public debt dynamics over the medium term. In addition, the public debt ratio is impacted in 2025 and 2026 by exceptional items related to the time profile of the use of tax credits for housing renovation. Public debt is already three points above its pre-COVID level and is expected to resume an upward trajectory to reach 140% of GDP in 2027.

Finally, Italy's growth potential over the medium term should be supported by the implementation of structural reforms planned by 2026 related to the judicial system, competition law, public administration and procurement reforms, among others. These reforms and their impact on Italy's growth potential are critical to sustain Italy's high public debt burden.

Italy	2025f	2026f	2027f	2028f
Real GDP, % YoY	0.6	0.5	0.5	0.8
Household consumption	0.6	0.3	0.5	0.7
Public consumption	0.4	0.4	0.4	0.4
Investment	2.3	1.2	0.7	1.4
Exports of goods & services	0.0	0.9	2.3	2.8
Imports of goods & services	2.0	1.7	2.5	2.9
Inflation, % annual average	2.0	1.8	1.7	1.9
Core inflation, % annual average	2.0	1.8	1.7	2.0
Real gross disposable income (GDI), % YoY	1.2	0.6	0.4	0.5
Households saving rate, % of GDI	12.4	12.8	12.7	12.5
Unemployment, % of labour force	6.3	6.3	6.6	6.6
Fiscal balance, % of GDP	-3.4	-3.1	-3.1	-3.0
Public debt, % of GDP	138	139	140	139
Current account balance, % of GDP	0.4	0.5	0.5	0.4

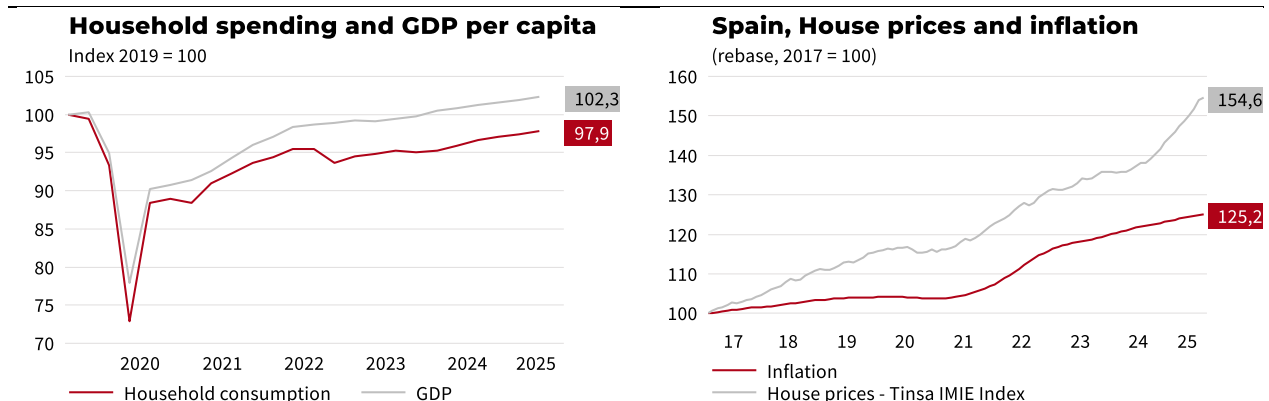
SPAIN

- **Growth will continue to outperform, supported by the influx of foreign labour, but the economy is changing gears**
- **The economy is set to decelerate as of 2027 as the support from NGEU funds will be withdrawn**
- **Climate change may end up taking a toll on tourist arrivals**

Growth continues to surprise on the upside, and Spain keeps overperforming the euro area despite inner political tensions, a unprecedented heatwave and global uncertainties. The tourist season recorded a new all-time high in terms of visitors, and receipts went up 7% in the first seven months of the year. Manufacturing activity also peaked with a strong PMI reading in August, driven by domestic demand: manufacturers are expanding their workforce to keep pace with rising workloads, while stocks of finished goods continue to decline due to stronger sales.

However, the massive wildfires and the record heatwave endured in August are likely to dent tourist arrivals in the coming years. Spain endured the worst wildfire season in over 30 years with over 380,000 hectares burned—nearly five times the annual average. Fires are the consequence of extreme weather conditions, with a temperature anomaly of 4.6 degrees (the most severe heatwave in the country's history since records began) and strong wind. Heat-related fatalities reached 2,177 in August. Overtourism is also having negative consequences for Spanish residents, in terms of housing prices, urban overcrowding (Barcelona) and environmental strain (especially in the Balearic and Canary Islands). Street protests are mounting, with protesters calling for regulation of short-term rentals, tourist taxes to fund local infrastructure, and limits on cruise ships and large-scale tourism projects.

Tourism is inflating house prices and has not benefitted household's spending



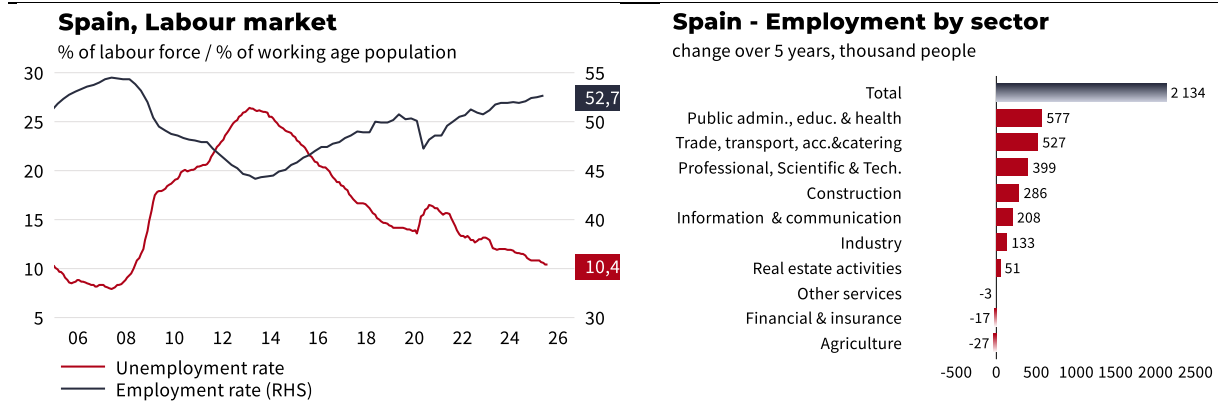
Source: European Commission, RRF scoreboard, SG Economic and Sector Studies

Source: INE, LSEG, SG Economic and Sector Studies

The labour market remains buoyant, with job creation reaching 700,000 over a year and more than two million over five years. The foreign workforce (inward migration mainly from South America) contributed to more than 80% of the increase.

Most jobs were created in professional services (computer programming, consultancy, ...), human health activities and accommodation services. The unemployment rate continues to decline but wage pressures remain muted.

Labour market shows no sign of softening and job creation is broad-based

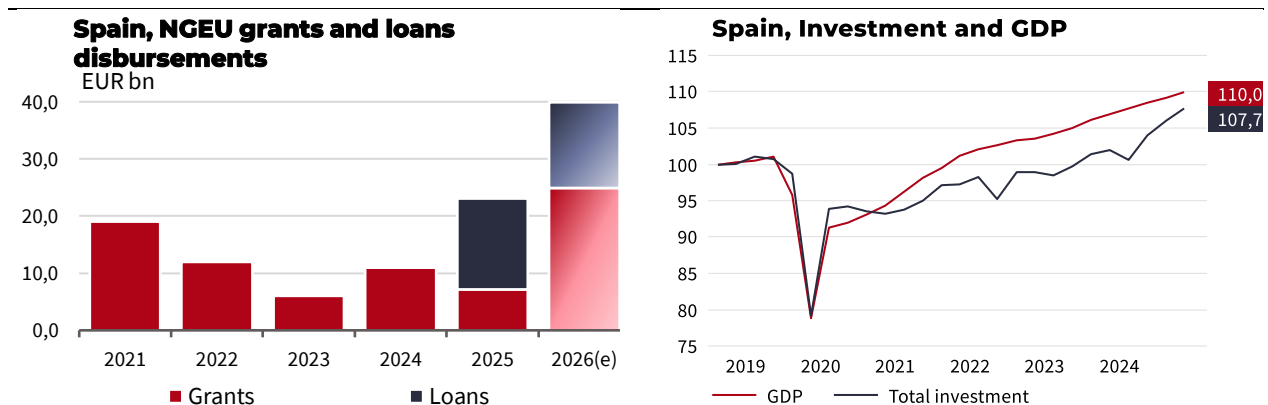


Source: INE, LSEG, SG Economic and Sector Studies

Source: Eurostat, LSEG, SG Economic and Sector Studies

The Spanish economy is entering a new and more moderate phase of expansion in which the engines of recent growth are losing steam. Public consumption and foreign tourism drove the recovery, exceeding pre-pandemic levels by 18% and 43%, respectively. Growth is now supported more by household consumption and investment, which are both welcome. The trend is likely to continue given sound household balance sheets, lower inflation, employment and wage gains, as well as the expected fall in interest rates as of 2026. Investment is driven by residential construction (benefiting from lower interest rates) and public investment thanks to the resources allocated to help the victims of the floods in Valencia and the NGEU funds.

Up to EUR 40bn worth of funds to be disbursed by end 2026



Source: European Commission, RRF scoreboard, SG Economic and Sector Studies

Source: INE, LSEG, SG Economic and Sector Studies

In August, the European Commission disbursed EUR 23.1bn to Spain, which will support measures to boost renewable energy, cut red tape, and improve justice efficiency. The funds will also be invested in short-distance rail travel and strengthen cybersecurity resilience. This is twice the amount received in 2024 (EUR 11bn), and

there is still up to EUR 40bn worth of NGEU funds to be disbursed by end 2026, out of a total envelope of EUR 163bn (13% of GDP).

Despite the current political deadlock, PM Sanchez is unlikely to resign before 2027. The intense wildfire this summer and corruption cases linked to the PM inner circle have led to a political crisis in Spain. The government is accused of “inefficient and slow” response to the fires. Despite mounting pressure, Sánchez reiterated that neither resignation nor early elections are under consideration, as he seeks to keep his fragile coalition afloat until the 2027 elections.

Spain has not passed a budget since 2022, and this year will be no exception. As a consequence, the fiscal stance is set to be broadly neutral. Less expenses will come from the post-Valencia floods reconstruction and a bit more are expected from an increase in defence spending. The government would have to nearly double its defence budget, to EUR 33.7bn from EUR 17.5bn last year, to reach the 2% of GDP target. This will be challenging given the ongoing lack of parliamentary support. The government is however securing support from its regional coalition partners by making plans to absorb EUR 83bn in debt held by regional administrations. The move does not affect Spain's overall public debt, as regions' liabilities are already included in the calculation. The move is seen as credit positive and could lead to some positive rating actions on regional debt.

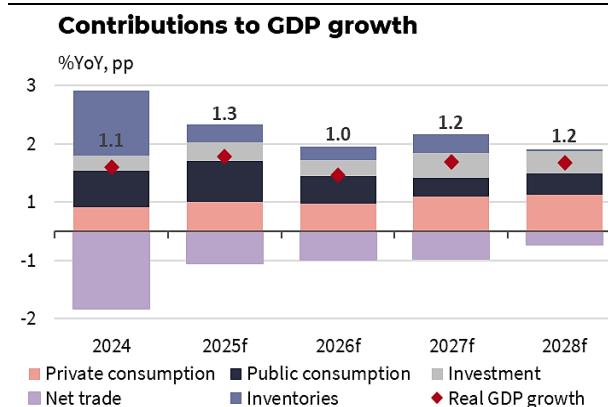
Spain	2025f	2026f	2027f	2028f
Real GDP, % YoY	2.6	1.8	1.6	1.6
Household consumption	3.0	2.1	1.8	1.8
Public consumption	1.5	1.7	1.0	0.8
Investment	5.3	2.5	1.9	1.7
Exports of goods & services	3.2	2.2	2.6	2.7
Imports of goods & services	4.5	2.8	2.7	2.7
Inflation, % annual average	2.5	2.2	1.8	2.0
Core inflation, % annual average	2.4	2.1	1.8	2.0
Real gross disposable income (GDI), % YoY	2.2	1.6	1.6	1.4
Households saving rate, % of GDI	12.9	12.5	12.4	12.0
Unemployment, % of labour force	10.9	10.9	11.1	11.3
Fiscal balance, % of GDP	-2.8	-2.6	-2.5	-2.5
Public debt, % of GDP	100	100	100	99
Current account balance, % of GDP	2.0	1.9	1.9	1.8

UNITED KINGDOM

- The UK is demonstrating resilience, with growth expected to outperform European peers in 2025, before slowing in 2026
- Public spending is set to sustain growth through 2026, but tax rises are expected in November to address fiscal pressures
- UK inflation, now the highest in the G7, will stay above the BoE's 2% target until 2027, preventing further rate cuts this year

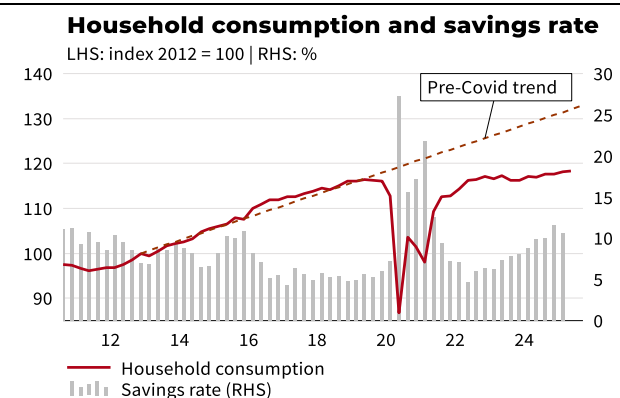
The UK recorded the strongest growth amongst the G7 countries in 1H25 (2.2% annualised). Growth was supported by government spending and a surge in private investment in 1Q25. However, elevated uncertainty has continued to weigh on exports and household spending. High-frequency indicators — including the PMI Composite and the OECD Composite Leading Indicator— suggest that the UK will outperform its European peers this year. We forecast real GDP growth of 1.3% in 2025 but expect momentum to slow to 1% in 2026 as fiscal support tapers and subdued private demand exposes underlying economic fragility.

GDP forecast: resilient growth



Source: SG Economic and Sector Studies

High savings constrain household consumption



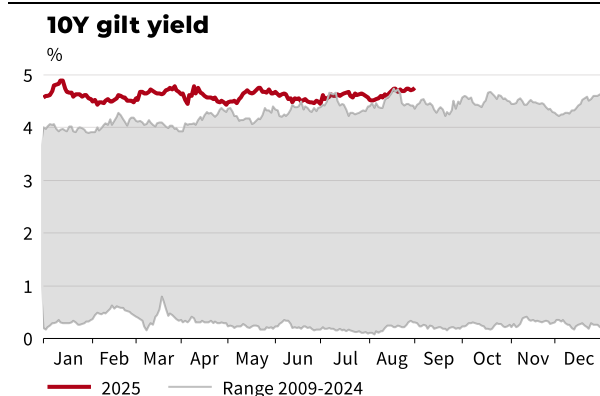
Source: ONS, Refinitiv, SG Economic and Sector Studies

Household consumption is expected to remain subdued in 2025-26, before seeing some moderate improvement in 2027-28. Elevated precautionary savings persist, reflecting ongoing global uncertainty, a weakening labour market, and high gilt yields, which are limiting declines in mortgage rates despite the BoE's continued rate-cutting cycle. As a result, private consumption remains around 11% below the level implied by pre-Covid trend growth. Medium term, we expect private consumption to recover gradually, supported by monetary policy easing, positive wealth effects from rising asset prices, and continued real income growth. While the household savings rate will fall in the coming years, it is set to remain above its long-term average, as the effects of successive economic shocks — including Brexit, the war in Ukraine, the energy price crisis, and persistent trade tensions — continue to shape household behaviour.

Public spending set to sustain growth through 2026... Since taking office, the Labour government has committed an additional GBP 360 bn to current expenditure and public investment — equivalent to 14% of 2025 GDP. Most of it is for the NHS, defence, and infrastructure. The spending profile is front-loaded: departmental budgets will grow by an average 3.4%/year until FY2025-26, before slowing to an average of 1.5%/year through FY 2028-29.

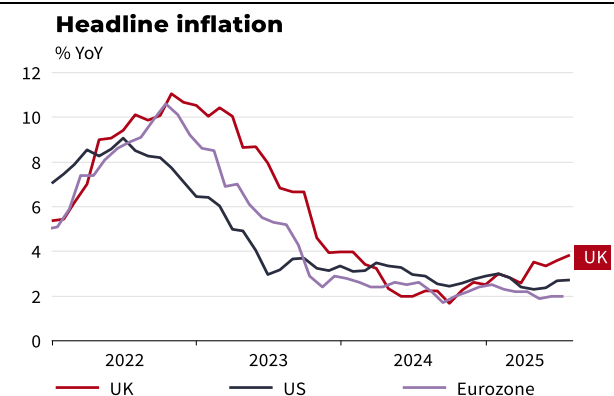
...but tax increases are expected in November as public finances are under strain. Over the past year public sector borrowing has overshoot forecasts, and the 10-year gilt yield is now the highest in the G7. This reflects elevated inflation expectations, the BoE's active bond sales under its QT programme, and a higher risk premium as investors focus on the UK's structural twin deficits. Against this backdrop, we expect the government to announce tax increases in the November Autumn Budget to rebuild fiscal headroom and comply with fiscal rules. Over the longer term, supply-side measures — including reforms to planning rules to accelerate infrastructure delivery and housebuilding — are expected to lift potential output and ease fiscal pressures.

The highest 10Y gilt yield since 2009



Source: ONS, Refinitiv, SG Economic and Sector Studies

UK inflation outpacing peers



Source: ONS, Refinitiv, SG Economic and Sector Studies

Inflation is expected to remain elevated through 2025–26 before gradually converging to the BoE's 2% target in 2027. Headline inflation reached 3.8% YoY in July — the highest in 18 months — leaving the UK with the highest inflation in the G7, almost double that of the Eurozone. Domestic price pressures are persistent, particularly in services, where inflation has risen to 5%. This is driven by strong wage growth, alongside the Government's decision to raise vehicle excise duties, water charges, employer social contributions, and the national minimum wage. We expect these factors to keep inflation elevated, averaging 3.5% YoY in 2025. However, the labour market is cooling as firms adjust employment and wages to offset rising labour costs and protect profit margins. Unemployment has risen to 4.7% — the highest since May 2021 — while the vacancy-to-unemployment ratio has returned to its pre-pandemic average. Recruitment difficulties reported by businesses have fallen to their lowest point in four years. As labour market weakens and spare capacity

emerges, we expect disinflationary momentum to build from 2026, paving the way for inflation to return to the BoE's 2% target in 2027.

We do not anticipate further BoE rate cuts in 2025. With inflation running at almost twice the 2% target, economic growth close to potential, and long-term inflation expectations among businesses and consumers remaining elevated, the BoE must proceed cautiously to ensure the current inflation spike proves temporary and to avoid a wage-price spiral that could entrench higher inflation. Following its 7 August decision to reduce the Bank Rate by 25bp to 4%, we expect the BoE to hold rates steady for the remainder of the year. It should resume its monetary easing cycle again in 2026, as softer growth and lower inflation create scope for further rate cuts.

Risks to the outlook remain tilted to the downside, primarily due to international tensions. A geopolitical escalation could trigger a rise in energy prices, derailing the anticipated disinflationary path in 2026 and keeping gilt yields elevated. Further downside risks stem from mounting trade frictions and uncertainty linked to a potential expansion of US tariffs which — even if not directly aimed at the UK — would undermine business confidence and weigh on external demand.

United Kingdom	2025f	2026f	2027f	2028f
Real GDP, % YoY	1.3	1.0	1.2	1.2
Household consumption	0.8	0.8	1.0	1.0
Public consumption	3.3	2.1	1.5	1.6
Investment	1.8	1.5	2.3	2.2
Exports of goods & services	3.2	1.0	1.4	2.0
Imports of goods & services	4.5	2.3	2.5	2.4
Inflation, % annual average	3.5	2.6	2.1	2.1
Core inflation, % annual average	3.6	2.7	2.0	2.0
Real gross disposable income (GDI), % YoY	0.5	0.7	0.7	0.7
Households saving rate, % of GDI	9.8	9.7	9.4	9.1
Unemployment, % of labour force	4.7	4.8	4.9	4.9
Fiscal balance, % of GDP	-5.4	-5.5	-5.3	-5.0
Public debt, % of GDP	99	101	102	103
Current account balance, % of GDP	-3.4	-3.5	-3.6	-3.6

UNITED STATES

- **Tariffs are now 13pp higher on average than 2024, but uncertainty remains elevated**
- **Concerns over Fed independence and burgeoning federal debt is expected to contribute to rising risk premia, particularly at the long end of the Treasury curve**
- **Stalling employment growth in cyclical sectors signals extent of labour market deterioration, prompting the Fed to increase weight on employment mandate, accelerating rate cuts despite inflation remaining above target and risks to the upside**

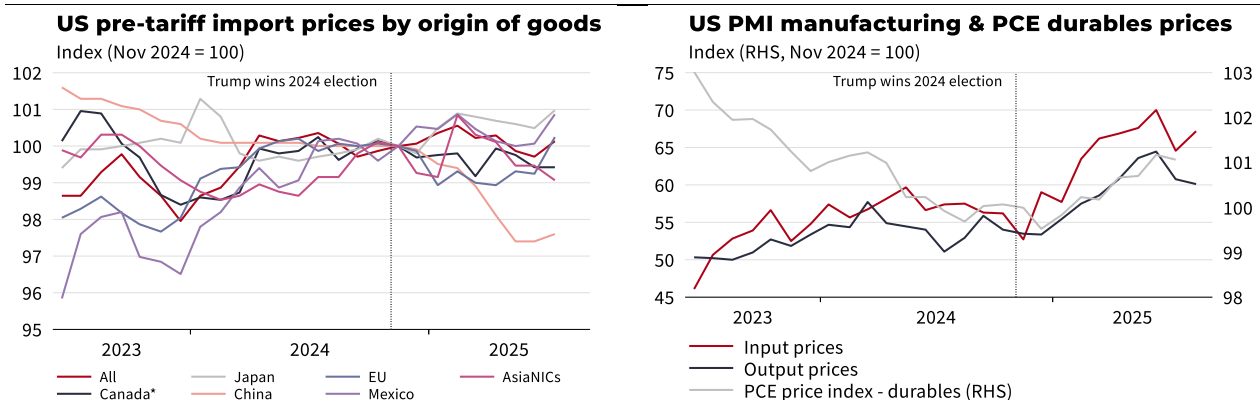
Following a slew of trade deals covering approximately 45% of US imports, the weighted average tariff rate (pre-substitution effects) is around 13pp higher than last year. Official retaliation has been limited so far; however, we do not expect a broad boost to US exports. US exports are likely to face intensified competition on global markets, as trading partners seek to diversify and reduce exposure to policy volatility.

The Trump administration has secured a number of trade deals, featuring protectionist tariffs on US imports on the one hand and reduced barriers to entry for US exports on the other. Counterparts have also signed up to unrealistic foreign investment and import commitments, the largest of which is the EU's promise to buy USD 750bn of LNG, oil and nuclear energy products through 2028. This sum would represent an annual increase of over 150% above current imports levels in these sectors. Certain sectors prioritised for export growth by the US in trade negotiations, notably LNG and civil aviation, face strong supply constraints in the near term meaning the US would be unlikely to be able to meet extra new orders before 2030 should they materialise. Another headwind on export growth comes from the administration's 50% tariffs on steel and aluminium and "derivative" goods, which will raise input costs and constrain American manufacturers production expansion.

Trade uncertainty has fallen from its post- "Liberation Day" peak but remains significantly higher than recent years. Section 232 investigations are ongoing into sectors including semiconductors, pharmaceuticals and lumber, meaning new tariffs could be on the way on goods which are currently tariff exempt. If the administration perceives trade partners' investment and import promises to be unfulfilled, tensions could flare up again. A signed deal should not be mistaken for a lasting resolution, as the trade tensions with the US's neighbours illustrates despite the USMCA agreed during Trump's first term. Furthermore, the legal basis for certain tariff increases remains in doubt after the Court for Appeals for the Federal Circuit upheld the decision of the Court of International Trade, which found the tariffs

imposed under the International Emergency Economic Powers Act (IEEPA) to be unlawful. The administration has appealed the decision, keeping tariffs in place until the Supreme Court reviews the case. A range of outcomes is possible, including the cancellation of all “reciprocal” tariffs brought in under IEEPA and an order to refund duties collected. The Section 232 tariffs are more legally secure under Presidential authority under the Trade Expansion Act of 1962 and are therefore more likely to remain in place and could even be expanded should IEEPA tariffs be annulled. The continuing uncertainty could delay investment and hiring decisions, putting a dampener on growth.

Americans set to pay the bulk of the tariffs, not foreigners



Source: Bureau of Labor Statistics, Refinitiv, SG Economic and Sector Studies

Source: S&P Global, Bureau of Economic Analysis, Refinitiv, SG Economic and Sector Studies

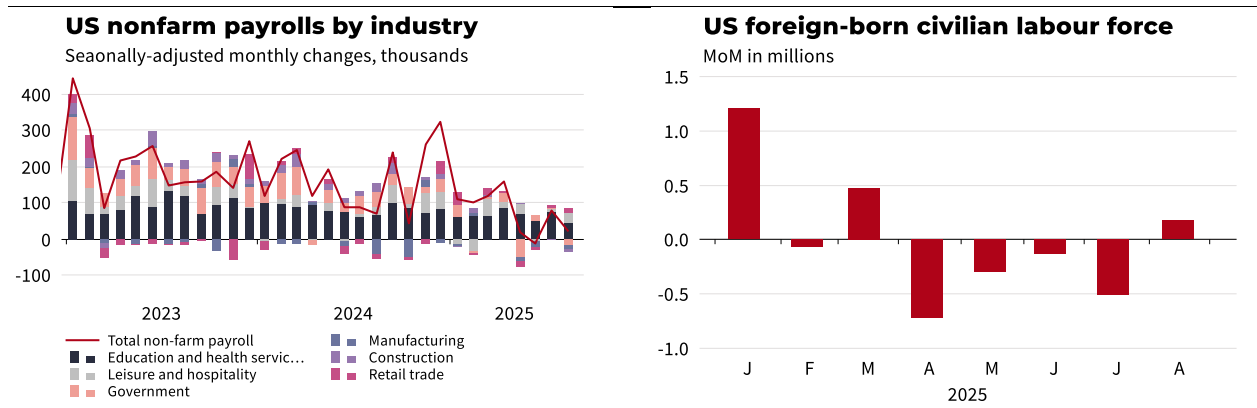
*Manufactured goods from Canada

Contrary to the administration’s hopes, most of the tariff hikes are not being paid by exporters, as shown by relatively stable pre-tariff import price indices in 1H25, save for a modest 2.5% drop on prices of imports from China so far this year. As anticipated, the tariffs are instead driving up input costs in sectors most dependent on imports such as durable goods, previously a disinflationary sector. The full extent of the impact on consumer prices will take time to feed through as inventories are depleted. We continue to expect inflation to peak around 4% around the turn of the year. The risk remains that higher import prices will spillover to less directly affected sectors, including services (where inflation remains stubbornly high at 3.6%). More broadly, higher inflation will erode real incomes and weigh on consumption, thus stifling growth. If the Supreme Court tariffs remain in place after’s decision, they would entrench protection for less efficient domestic producers, reducing competitive pressure and dragging on productivity growth for years to come.

Political pressure on the Fed has escalated significantly, putting the institution in its most perilous position since Nixon. From September, three governors will be Trump appointees. The President has dismissed Governor Lisa Cook based on allegations of mortgage fraud, pending judicial review. Chair Jerome Powell’s term ends in May 2026, although it remains unclear whether he will complete his term as governor, which runs until 2028. The influence the growing cadre of administration-

appointed governors can exert over the rest of the Board and the regional presidents remains to be seen, however, the politicisation of monetary policy risks undermining the Fed's credibility in maintaining price stability. This could heighten inflation risks, especially amid rising economic frictions. Further institutional erosion is evident in the dismissal of Bureau of Labor Statistics head. Markets appear complacent about these developments, particularly the increasing concentration of executive power at the expense of Congressional oversight. This gradual erosion of institutional predictability, credibility, and trust is likely to contribute to continued dollar depreciation and a steepening yield curve. Term premia on 10-year Treasuries are expected to rise toward 1%, increasing borrowing costs across the real economy.

Hiring drastically slowing as foreign workers are expelled, keeping the unemployment rate from climbing faster



Sources: Bureau of Labor Statistics, U.S. Department of Labor, Refinitiv, SG Economic and Sector Studies

Sources: Bureau of Labor Statistics, U.S. Department of Labor, Refinitiv, SG Economic and Sector Studies

Hiring deteriorated significantly in 2Q25, with average monthly payroll gains of just 27,000 from April to August - well below breakeven employment growth, even accounting for a suspected rise in the NAIRU. The slowdown may have begun earlier than previously thought. In its preliminary benchmark revision, the BLS indicated that payroll growth for the 12 months through March 2024 may have been overstated by 911,000 jobs, halving monthly average gains from 147,000 to 71,000. The economy is undergoing simultaneous shifts. Tariffs introduced in 2025 and a crackdown on immigration are increasing frictions in the labour market. Since April, an estimated 1.5 million foreign-born workers have exited the labour force, likely lowering the breakeven threshold for non-farm payrolls. Over the past year, hiring has remained robust in healthcare and social assistance – sectors largely shielded from cyclical dynamics by social security and government transfer programmes. In contrast, construction, manufacturing, and retail – typically bellwethers of private demand – are showing signs of strain. During slowdowns, these sectors typically correlate strongly with deterioration in the broader labour market. We expect layoffs to accelerate, reinforcing our forecast of a year-end unemployment rate of 4.7%. Against this backdrop, the Fed faces a shifting policy calculus and is expected to tilt more toward the employment side of its mandate despite inflation remaining above target. Powell signalled at Jackson Hole that the balance of risks is shifting in favour

of labour market deterioration. The Chair sees the risk that tariff-related price rises lead to a wage-price spiral as remote, a view consistent with the Board's dovish wing. We therefore expect the FOMC to accelerate rate cuts - looking through an anticipated tariff-driven surge in inflation - bringing the target rate down to 4.0%-3.75% by year-end, followed by a 25bp cut in 1Q26. The Fed's reweighting away from inflation risks will likely increase uncertainty around the long-term inflation outlook, contributing to increasing term premia.

Risks to the outlook remain skewed to the downside. While investment is projected to be supported in the coming years by the artificial intelligence (AI) boom, it remains difficult to evaluate the extent of profitability gains the technology can deliver. A recent MIT study¹ found that 95% of AI-related investments failed to yield measurable profitability gains, raising concerns about the sustainability of current valuations. Market leadership is highly concentrated: four companies—Nvidia, Meta, Microsoft, and Broadcom—account for roughly 60% of the S&P 500's year-to-date gains. Price-to-earnings ratios remain elevated compared to historic averages. A correction toward mean valuations could erase trillions of dollars in household wealth, amplifying the negative wealth effect on consumption from tariffs and deepening the downside risks to growth beyond our central scenario.

United States	2025f	2026f	2027f	2028f
Real GDP, % YoY	1.7	1.4	1.0	1.8
Household consumption	1.7	1.5	1.2	1.8
Public consumption	1.0	1.4	1.1	1.4
Investment	1.9	2.2	2.1	2.4
Exports of goods & services	1.9	1.4	1.0	2.4
Imports of goods & services	2.4	2.1	2.5	3.4
Inflation, % annual average	3.2	2.9	2.6	2.6
Core inflation, % annual average	3.4	2.8	2.6	2.7
Real gross disposable income (GDI), % YoY	1.5	1.9	1.2	1.7
Households saving rate, % of GDI	4.3	4.7	4.7	4.9
Unemployment, % of labour force	4.4	4.9	5.2	5.1
Fiscal balance, % of GDP	-5.7	-6.7	-6.8	-7.0
Public debt, % of GDP	100	104	108	111
Current account balance, % of GDP	-3.6	-3.8	-3.8	-3.9

¹ MIT NANDA (2025) *The GenAI Divide: State of AI in Business 2025*
https://mlq.ai/media/quarterly_decks/v0.1_State_of_AI_in_Business_2025_Report.pdf

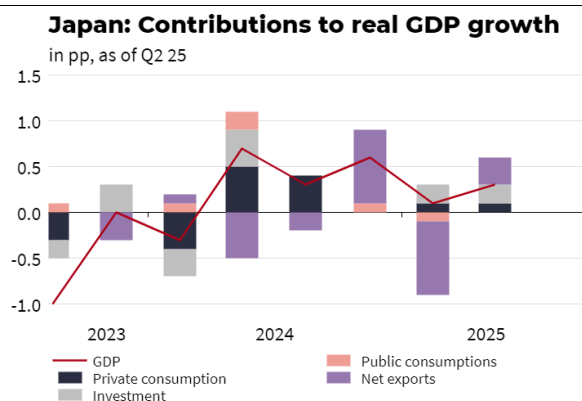
JAPAN

- **Real GDP is set to slow to 0.6% in 2026 after 1% in 2025, as a result of global trade frictions and the impact of inflation on consumption**
- **The normalisation of monetary policy is expected to continue very gradually**
- **After the resignation of the prime minister, Japan enters a new period of political uncertainties**

After strong momentum in 1H25, the economy is losing momentum. The economy should grow by 1% in 2025, due to resilient private consumption and recovering business investment in the first half of the year, as well as a boost from front-loaded trade. However, private consumption is bound to decelerate as household finances are hit by sticky inflation, while more moderate nominal wage growth is likely ahead. Meanwhile, elevated political and policy uncertainty, due to the weakness of the minority government and the trade uncertainties, will weigh on business sentiment.

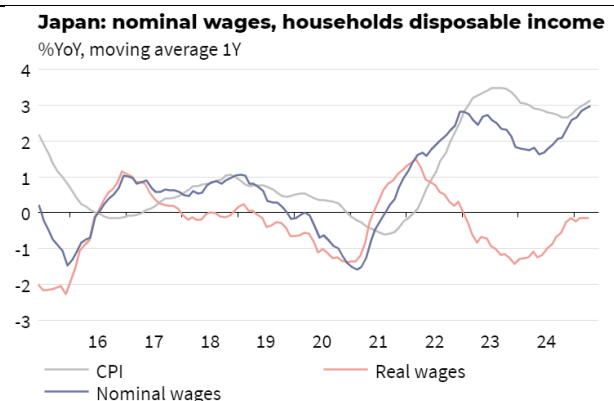
Export momentum is weakened by global trade frictions. Japan's trade agreement with the US includes relatively moderate levels of US reciprocal tariffs and levies on Japanese cars, both at 15%. For a leading exporter of vehicles, machinery and robotics this remains negative for growth. The US is Japan's main export destination at 20% of total goods exports in 2024.

Growth will be weakened by tariffs



Sources: SG Economic and Sector Studies, LSEG

Inflation suspends real wage growth

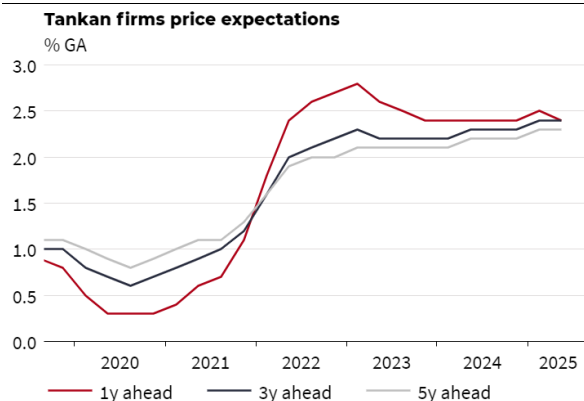


Sources: SG Economic and Sector Studies, LSEG

Corporate investment should continue to sustain growth. Corporate profits are firm, especially in sectors such as services, which have benefited from strong domestic sales thanks to tourism and higher prices. The increase in profits supports their investments. They are expected to continue to rise, albeit at a slower pace, supported by government subsidies, especially for green and digital investments. The structural need to increase productivity in the face of labour constraints should also boost corporate investment in the medium term.

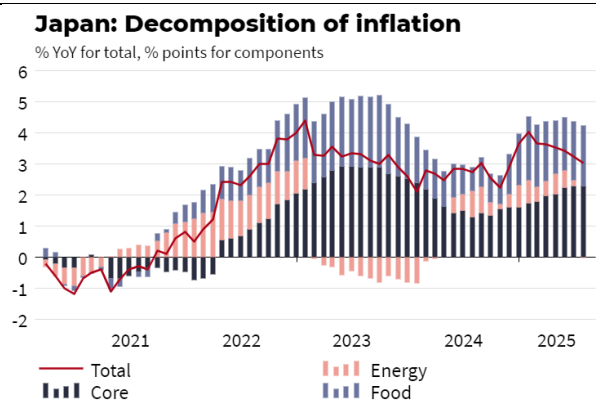
Inflation should ease but Japan will stay clear of deflation. Heightened geopolitical tensions and adverse weather conditions have kept energy and food prices high. These factors are now expected to dissipate. Real wage growth should take over and support inflation in the coming years. In the medium term, labour shortages and an ageing population could keep pressure on wages and prices. However, past performance calls for caution. Even if expectations are now much more anchored, the inflation trajectory could still disappoint if real wages adjust to lower than anticipated GDP growth.

Price expectations are stabilizing



Sources: SG Economic and Sector Studies, LSEG

Core inflation is still rising



Sources: SG Economic and Sector Studies, LSEG

The Bank of Japan is expected to gradually normalize monetary policy over the next two years and raise its policy rate to around 1% by the end of 2026. The central bank will remain cautious throughout this period to ensure that policy normalization does not cause an economic slowdown or jeopardize its success in the recovery. The pace of further rate hikes will depend on inflation data and real wage growth. We expect the BoJ to continue its quantitative tightening. The central bank has scaled back its purchase of ten-year government bonds and exchange-traded funds, which is reducing the size of its balance sheet. The BoJ would slow this tapering only if the bond's market volatility is considered too high. Due to its history of deflation, we expect the BoJ to err on the side of caution.

The fiscal deficit is expected to narrow slightly over the forecast horizon, but fiscal policy will remain supportive of activity. The deficit is expected to widen in 2025 given the stimulus plan implemented at the end of 2024, with the resumption of subsidies to ease inflationary pressures on households. In the medium term, ageing-related spending, particularly in the health sector, will continue to put pressure on the fiscal deficit. The planned increase in defence spending by 2027 is significant, to align with a new benchmark of 2% of GDP. Debt servicing costs are also going to rise. We expect the fiscal deficit to average close to 3% of GDP over the forecast horizon.

Japanese PM Ishiba announced his resignation early September, in the wake of presiding over the party after a second setback in national elections in the July

Upper House election. Ishiba's decision comes ahead of an LDP vote that could have forced his departure. Concern now is to see a new PM with less commitment to fiscal discipline.

Risks are tilted to the downside. Uncertainties over global trade could continue to exert pressure on Japanese exports (20% of GDP) and growth and delay the pace of monetary policy normalisation. A large appreciation of the yen could reduce corporate profits and weigh on wage increases. Interest rates on long-dated Japanese government bonds are rising and a loss of confidence in Japan's fiscal sustainability could increase the sovereign risk premium.

Japan	2025f	2026f	2027f	2028f
Real GDP, % YoY	1.0	0.7	0.7	0.6
Household consumption	1.1	0.8	0.8	0.6
Public consumption	0.3	0.8	0.4	0.4
Investment	2.1	0.8	0.7	0.6
Exports of goods & services	3.1	1.5	1.7	2.0
Imports of goods & services	4.1	2.6	2.0	1.8
Inflation, % annual average	3.4	1.8	1.5	1.5
Core inflation, % annual average	2.8	1.6	1.2	1.2
Real gross disposable income (GDI), % YoY	0.8	0.7	0.7	0.6
Households saving rate, % of GDI	3.9	3.8	3.7	3.7
Unemployment, % of labour force	2.5	2.2	2.1	2.3
Fiscal balance, % of GDP	-3.3	-3.2	-3.1	-3.1
Public debt, % of GDP	238	240	240	242
Current account balance, % of GDP	4.2	4.0	4.2	4.2

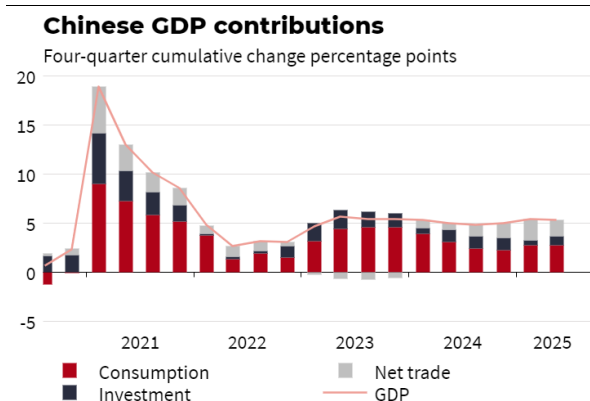
CHINA

- **Activity is moderating. Economic growth should reach 4.7% in 2025 and slow to 4.2% in 2026**
- **Exports should start to be curbed by the tariffs with the US. The real estate correction continues**
- **The policy mix will remain accommodative and incremental but is not expected to provide a structural solution**

The growth outlook is deteriorating due to persistent low consumer confidence and the lasting effects of the slowdown in housing market, and the hurdles faced by the additional tariffs on exports. Rebalancing growth towards consumption could increase China's growth potential, but consumption-related measures remain too incremental for the time being. Without a recovery in the real estate sector and structural measures (improvement in social protection, etc.), household confidence will remain structurally weak and will dampen consumption.

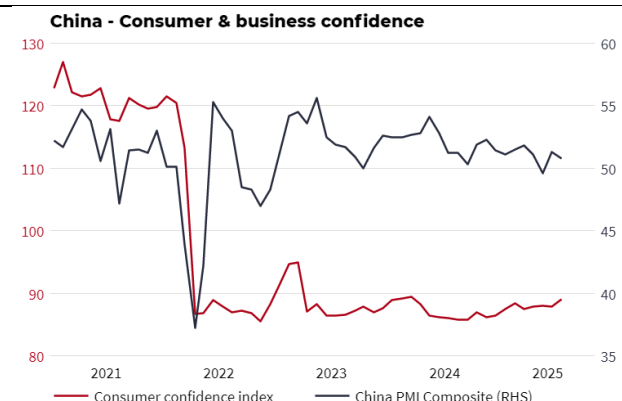
Exports have remained resilient so far in but now face higher tariffs on shipments to the US. China's exports even surprised to the upside, accelerating from 5.9% in June to 7.2% in July in USD terms. The frontloading ahead of the July deadlines for many countries, supported export strength. By destination, exports to the US fell by more than 20%, but this was more than offset by rising shipments to the EU and to ASEAN countries. In August the US and China agreed to pause tariff hikes for an additional 90 days. Tariffs on Chinese goods were previously set to rise to 54% but are now back to 30% until a trade deal is reached, while transshipments continue to face a 40% tariff. China exporters, given the domestic deflation and weak demand, are likely to offer increasingly competitive export prices.

Growth in 1H was driven by exports



Source: SG Economic and Sector Studies, LSEG

Households' confidence struggles to improve

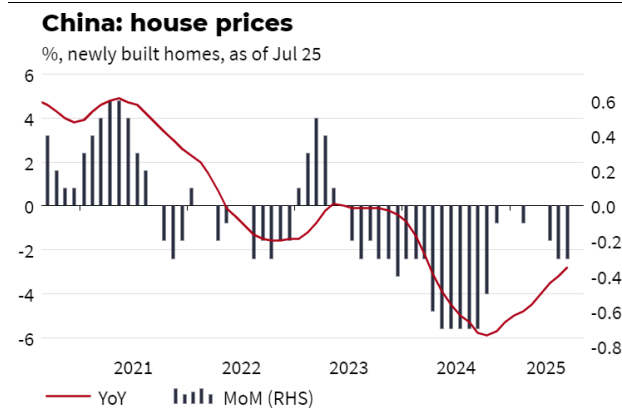


Source: SG Economic and Sector Studies, LSEG

The real estate sector continues to contract in a relatively controlled manner, thanks to support measures, but structural problems, such as fragile buyers' confidence and overcapacity, persist. House prices have continued to fall, the

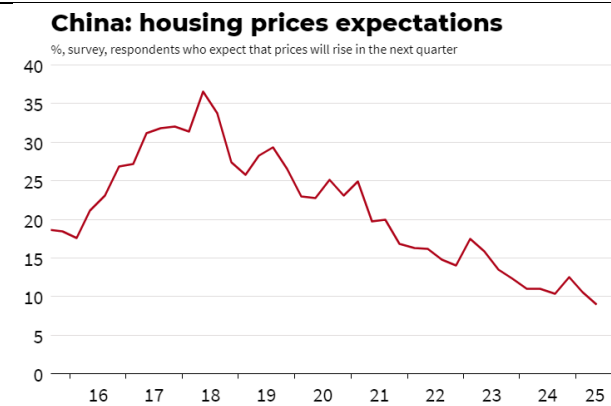
decline in first-tier cities has even intensified. Further relaxations in purchase restrictions have been announced. This is in addition to support measures in May with the reduction of the prime borrowing rate (LPR) by 10bp, to 3% and 3.5% for the 1-year and 5-year LPR, respectively and the reduction in pre-selling of homes by real estate developers.

Further contraction in housing prices



Source: SG Economic and Sector Studies, LSEG

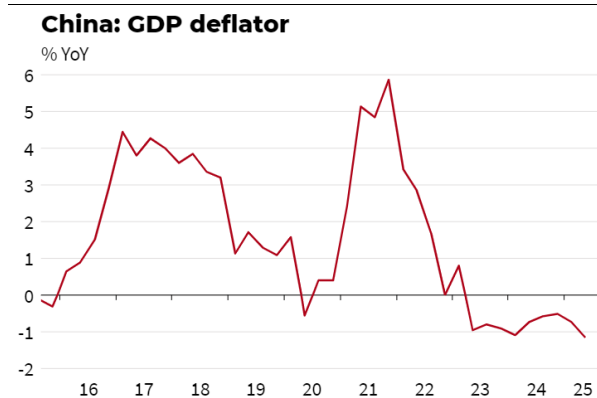
Price expectations are not recovering



Source: SG Economic and Sector Studies, LSEG

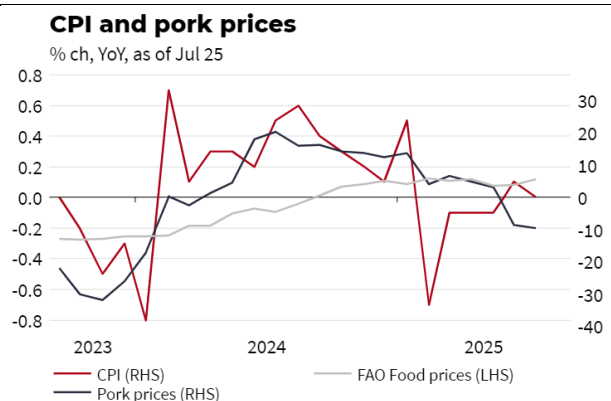
Inflation will remain close to zero in 2025, despite a decline in disinflationary pressures. Lower global commodity prices and negative food prices have contributed to disinflationary pressures. Inflation is close to zero and the contraction of the GDP deflator over the past year reflects the weakness of domestic demand. The price of pork has contracted given stable domestic consumption and a supply that continues to increase this year.

The deflator remains in contraction



Source: SG Economic and Sector Studies, LSEG

Food prices weaken CPI



Source: SG Economic and Sector Studies, LSEG

The policy mix will remain accommodative and incremental but is not expected to provide a structural solution. The National Party Congress in March put consumption as a top priority to support growth this year. As a result, the budget of the *Trade-in* programme in place since July has been doubled, from CNY 150bn to CNY 300bn financed by the issuance of special Treasury bonds. As a reminder, this program, which consists of replacing more energy-efficient appliances (especially

household appliances), contributed to the acceleration of consumption by one percentage point in 2024. It has now been extended to cars and electronic devices (smartphones, tablets, etc.). While the scope has been extended, the impact is expected to be less significant in 2025 and only temporary. The budget deficit target has also been raised from 1pp to 4% in 2025, the highest in history but is expected to partially compensate for export losses.

Geopolitical tensions will remain present and could intensify with the risks of overcapacity. Geopolitically, relations with the United States and national security rationale will continue to weigh on and shape China's role in global value chains. The Taiwan issues also remain a source of risk. China's rhetoric has hardened towards the island, leading to an increase in coercive military activities. As a result, the risks of errors related to Chinese military exercises cannot be excluded.

China	2025f	2026f	2027f	2028f
Real GDP, % YoY	4.7	4.2	4.0	3.8
Household consumption	5.5	4.5	4.2	3.8
Public consumption	6.1	4.9	4.8	4.5
Investment	4.0	4.0	3.9	3.5
Exports of goods & services	3.0	1.8	2.1	2.5
Imports of goods & services	4.0	2.8	2.2	2.0
Inflation, % annual average	0.3	1.0	1.2	1.5
Fiscal balance, % of GDP	-8.0	-7.8	-7.6	-7.6
Public debt, % of GDP	94	97	99	101
Current account balance, % of GDP	1.5	1.0	1.0	0.9

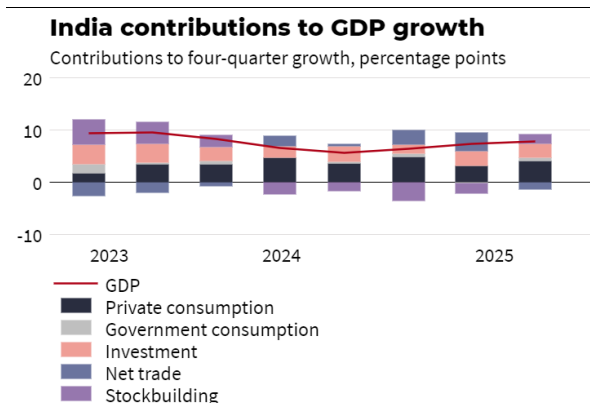
INDIA

- **GDP Growth will remain elevated, even if the trade conflict with the US will moderate the momentum**
- **The financial system has become more resilient, allowing support for the domestic investment dynamic**

GDP growth will be affected by the new US tariffs which are significantly above Asian peers. In August the US have imposed an additional 25% tariff on Indian exports, as a penalty for buying military equipment and oil from Russia, taking the total tariff on most Indian exports from 25% to 50%. If they remain in place, it will reduce GDP growth by around 0.3 percent point. This has pushed us to revise our forecast to 6.1% in 2026. The US accounts for 20% of India's good exports, or about 2% of India's GDP). The goods affected by the new tariffs (USD 45 bn, or 1% of GDP), are mainly in labour-intensive sectors such as textiles, gems and jewellery, leather, and shrimps. The impact should be partially dampened by the ability to redirect part of these exports. Meanwhile, rising interest in India's large domestic market and multinational efforts to diversify beyond China have recently encouraged global firms to form export-driven partnerships with local manufacturers. This should sustain sectors which remain up to now exempt from the new levies such as pharmaceuticals, finished electronic goods and refined petroleum products.

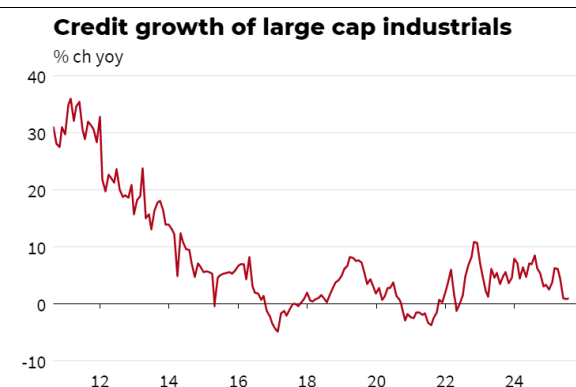
The country benefited from years of public investment helped also by the recovery of the banking sector. We expect a gradual pickup in private investment as soon as this fiscal year, supported by rate cuts and infrastructure improvements following the massive public investment campaign. The planned reform of simplification of the GST tax is also expected to sustain consumption. This should enable growth to remain around 6.5% YoY in the medium term.

Growth rebounded in 2025



Source: CSO, SG Economics and Sector Studies, LSEG

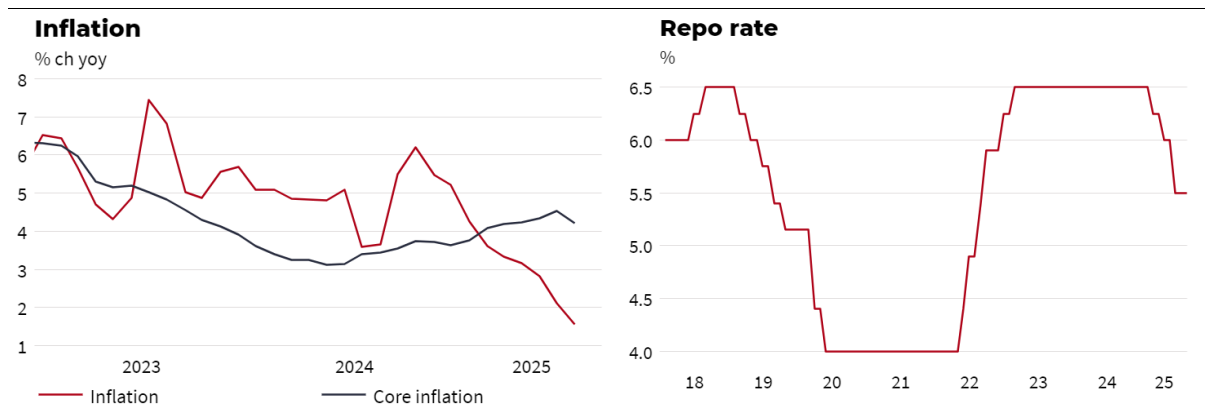
Private capex should pick up



Source: RBI, SG Economics and Sector Studies, LSEG

Inflation is slowing but expected to stabilize around 4%, enabling further rate cuts that should support private consumption. Inflation has sharply decelerated to below 2% YoY in July due to easing vegetables prices pushed down by a favourable monsoon, but core inflation remains above 4% after an acceleration due to the gold prices. The RBI has cut the policy rate from 6.5% to 5.5% since the start of 2025. This cycle should continue and support private consumption. However, we expect that the RBI will struggle to reach its 4% target. The economy is still characterized by durable supply constraints linked to still insufficient infrastructure and production capacity. Domestic demand is expected to remain vigorous linked to demographics and urbanisation. As a result, inflationary pressures are likely to persist.

Inflation is stabilising at levels in line with the RBI's 4% target... ...which has started its cutting cycle



Source: RBI, Refinitiv and SG Economics and Sector Studies, LSEG

Source: RBI, Refinitiv and SG Economics and Sector Studies, LSEG

Fiscal consolidation has begun, and the budget balance will improve over the medium term. The downside of India's growth since 2020 has been rising public debt, which now stands at 80% of GDP (a high ratio compared with other emerging countries). Consolidation is therefore a major goal for the Modi administration. Already, for the fiscal year 2024-2025, the central government has posted a deficit of 4.9% of GDP, compared with 5.8% in 2023. This dynamic will continue over the medium term, with public debt falling as a percentage of GDP and public consumption slowing.

India's financial services sector has recovered well in recent years from a domestic bad-loans crisis the late 2010's and from the global turmoil caused by COVID-19. The banking sector has recorded several years of higher profits as the tightening of monetary policy has improved interest margins for lenders. Since 2017, partly thanks to recapitalizations of public sector banks, the capital adequacy ratio of the banking system has gained nearly 300bp to reach over 17% and nonperforming loans declined from over 9% of total loans to below 4%. In its February 2025 financial stability assessment, the IMF has recognized this improvement, flagging only some concerns about the Non-Banking Financial Companies, due to their concentrated exposures, especially to the power and infrastructure sectors

Risks to this scenario are balanced. On one hand, domestic demand dynamics could positively surprise in a context of easing monetary policy and inflation stabilisation which could boost investment and consumption. On the other hand, downside risks come from the country's exposure to climate uncertainties given the size of the agricultural sector and its impact on food prices. Geopolitical risks remain elevated following tensions with Pakistan.

India (fiscal year from April to March)	2025f	2026f	2027f	2028f
Real GDP, % YoY	6.5	6.1	6.4	6.5
Household consumption	6.7	6.3	6.4	6.6
Public consumption	5.6	5.2	5.0	4.8
Investment	6.0	6.3	6.5	6.7
Exports of goods & services	5.5	4.0	5.5	6.0
Imports of goods & services	5.8	5.0	6.0	6.5
Inflation, % annual average	4.3	4.5	4.5	4.5
Fiscal balance, % of GDP	-7.3	-7.3	-7.1	-6.9
Public debt, % of GDP	82	80	78	76
Current account balance, % of GDP	-1.7	-1.4	-1.7	-1.8

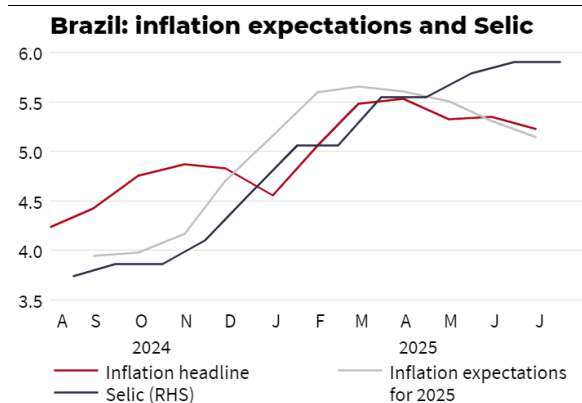
BRAZIL

- **A tight labour market and strong agricultural production in 1H25 will result in resilient growth prospects in 2025**
- **Sustained high interest rates weigh on public finances, inflating the debt and further restricting fiscal space**
- **As monetary policy transmission strengthens, the cyclical downturn will be accentuated**

Growth will remain resilient in 2025 (2.3%) on the back of a still tight labour market and record agricultural production amidst increasing downward risks.

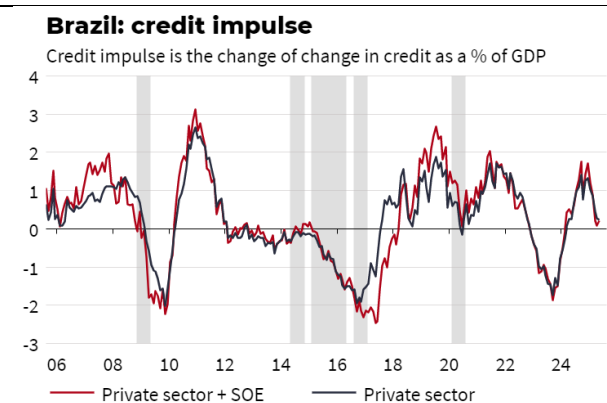
Consumer expenditure will remain elevated as the unemployment rate remains at its lowest levels in over a decade, informality stabilizes, and wages continue rising. Private investment will stay robust this year, mainly driven by machinery and equipment which have a significant import content as firms anticipate increased demand in a strained international environment. The dynamism of investment is part of a recovery of investment rates that plummeted in the 2014-2020 period. Coupled with favourable agricultural production (notably for soy, rice and corn), it lifts the growth prospects for this year even if a cyclical downturn continues to be expected from the latter part of the year into 2026.

The BCB tightening cycle re-anchored expectations and transmits to prices



Source: BCB, SG Economic and Sector Studies

A lagged transmission of the policy rate materialises in the credit impulse



Source: IMF, IBGE, SG Economic and Sector Studies

A hawkish BCB is set to hold the Selic at a 19-year-maximum for the rest of the year, accentuating the risks on the fiscal accounts. Inflation remains elevated and beyond the BCB tolerance interval (3% +/- 1.5pp) at 5.1% this year but it peaked earlier in the year and inflation expectations have re-anchored with corrections to the downside. Further disinflation is expected over the rest of the year backed by the normalization of food prices and a stronger than expected BRL (+13.8% YTD). Hawkish action from the BCB is to be expected in the short term, keeping the real rates elevated and contributing to the rate differentials that will help support the BRL further. High policy rates accentuate fiscal risks, as Brazil's public debt is

predominantly concentrated in the local market (nearly 90% denominated in BRL) and with a rather short average maturity of 4 years. The interest charges are then expected to gain over 2pp of GDP in 2025 from the previous year. Rising interest charges balloon the debt stock and reduce the fiscal space available for the government to face additional shock in an uncertain environment, and ahead of next year's general elections.

Transmission of monetary policy is set to be more salient in the rest of the year, weighing on consumption and investment. Pass-throughs to market-base lending rates has been complete per the IMF with relatively short lags in transmission (about 4 months). The pass-through to public banks' loans is significantly lower, but the 2017 reform to gradually reduce their subsidies, has enhanced overall transmission. The resilience of credit dynamics to the private sector (+11.4% YoY monthly average over the first 7 months of 2025) has been enabled by increased competition in the financial space, notably from fintech, and structural reforms aiming to reduce lending costs. As these effects run their course, tight monetary policy is expected to be apparent in the quantity of credit produced, turning the credit impulse negative through next year -even if some accommodation from BCB is expected- and constraining domestic demand and accentuating next year's downturn.

The international environment is more stringent towards Brazil. The US rhetoric towards the country became much more aggressive, resulting in threats of 50% tariffs on Brazilian imports. The effective tariff rate on exports to the US is only set to increase by 25pp as a significant part of the exports (notably fossil fuels, aircrafts parts, wood) benefit from exemptions to high tariffs. The effect of the tariffs were they to be perennial, the first-round effect on growth should be limited as exports represent a moderate share of the economy (and the US accounts for only 13% of total exports) and substitution effects play in. Agricultural exports should be hit the hardest but can more easily be re-routed to other markets like China. Retaliation, if implemented as announced, would be the main source of risk in this regard as it would fuel inflation via imports.

Another source of risk comes from the political context and public finances. The aftermath of trial of former President Bolsonaro, sentenced to 27 years in prison for his failed conspiracy to overturn the 2022 elections, will heighten polarization ahead that could bleed into social unrest clouding the economic environment ahead of the 2026 elections. As previously mentioned, fiscal space is highly constrained as snowball effects are elevated as interest rates largely surpass nominal growth. The capacity of the Government to respond to future shocks with fiscal policy is thus highly limited.

Risks are tilted to the downside. We expect a cyclical downturn from 2H26 that will limit growth in 2026-27 (1.1%, 1.7% respectively), as the labour market is expected to deteriorate and negative credit impulse softens domestic demand. A stronger than expected deterioration in the labour market (via an increase in unemployment

and/or via an exacerbation of informality) represents a downward risk to the outlook. Moreover, the rise of lending rates in a context of elevated real policy rates not only could lead to a sharper deterioration of the domestic demand but elevate financial stability risks notably on the household balance sheet as their debt service-to-income ratio reaches an historical high of 28%.

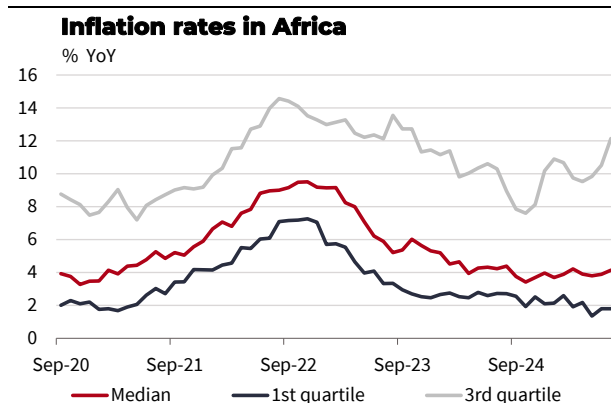
Brazil	2025f	2026f	2027f	2028f
Real GDP, % YoY	2.3	1.1	1.7	2.3
Household consumption	2.2	1.4	2.1	2.5
Public consumption	1.5	0.8	0.8	0.8
Investment	3.5	0.7	2.0	2.5
Exports of goods & services	2.1	1.3	2.1	2.3
Imports of goods & services	6.9	1.5	2.2	2.3
Inflation, % annual average	5.1	3.9	3.3	3.5
Fiscal balance, % of GDP	-8.5	-8.3	-7.0	-6.4
Public debt, % of GDP	92	97	99	100
Current account balance, % of GDP	-2.5	-2.3	-2.3	-2.3

AFRICA

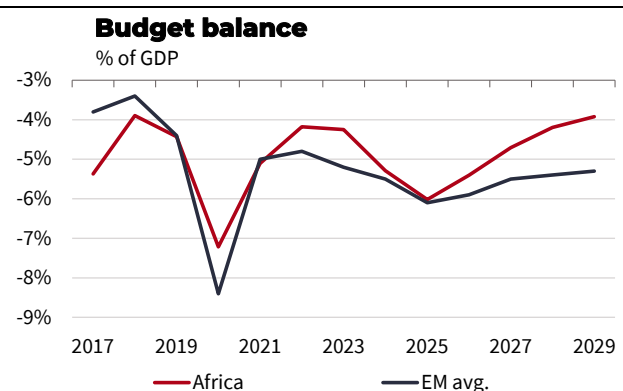
- **Regional growth is expected to accelerate slightly in 2025 and 2026, to 3.5% and 3.8% respectively**
- **This acceleration is partly linked to the region's ability to attract FDIs**
- **However, these growth rates remain too low to resolve the region's structural problems (lack of economic catch-up, debt vulnerabilities, etc.)**

Average regional growth is still expected to accelerate slightly in 2025 and 2026, to around 3.5% and 3.8% respectively (compared with 3.2% in 2024 – one of the worst performances since 2010). This acceleration will mainly be driven by stronger private demand, benefiting from the gradual normalisation of inflation rates in the region (despite significant disparities within the region). On the other hand, public demand is expected to remain constrained overall, due to ongoing fiscal consolidation efforts (particularly in Sub-Saharan Africa). These efforts are necessary in most countries due to persistent tensions in local currency financing conditions, caused, among other things, by the structural lack of depth in domestic financial markets (and the fact that “traditional buyers” are already highly exposed: public debt already accounts for around 20% of bank balance sheets in Africa). More reassuringly, foreign currency financing conditions remain resilient, with, for example, USD 7bn in Eurobonds issued in the first eight months of 2025, a level comparable to the same periods in 2024, 2021 and 2019.

Inflation rates are stabilizing, despite significant regional disparities



Ongoing budget consolidation efforts will weight on public demand

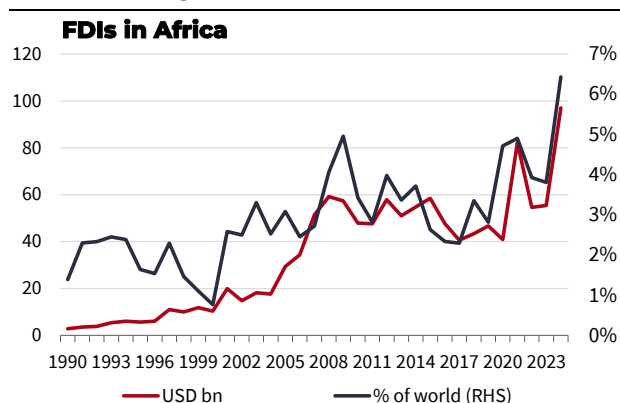


Source: Refinitiv, SG Economic and Sector Studies

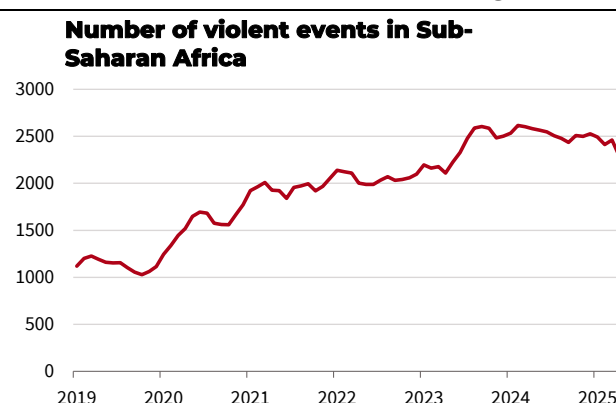
Private demand in Africa is also benefiting from strong foreign direct investment (FDIs), which has remained resilient for several years. FDIs reached USD 97bn in 2024, compared with USD 55bn in 2023. Even excluding the Ras El-Hekma megaproject in Egypt (USD 35bn invested by a Dubai-based company), FDI grew by 12% in 2024, despite declining globally (-11% to USD 1,490bn) and in all

other emerging regions. On the positive side, this resilience likely reflects the region's dynamism (second-highest average growth globally, behind emerging Asia), even though African governance levels remain low on average. On the more negative side, analysis of FDIs highlights several structural weaknesses in the region: excessive concentration in the carbon-intensive energy, extractive industries and construction sectors (which account for more than 80% of total FDI); weakness (and even decline) in intra-African FDIs and therefore ever-increasing dependence on international capital flows (a phenomenon also illustrated by the region's structural current account deficit, which has been widening again since 2021).

FDIs are rising



The number of violent events is still high



Source: Refinitiv, UNCTAD, World Bank, SG Economic and Sector Studies

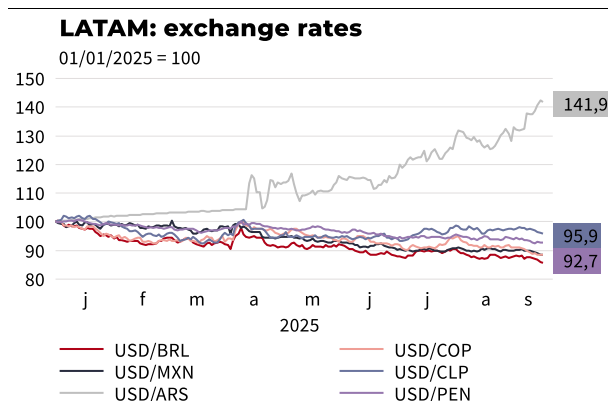
Although dynamic compared to other emerging regions, current growth forecasts remain insufficient, both in terms of ensuring sustainable development in the region (African per capita GDP levels still lag behind those of other regions) **and resolving its structural problems:** persistent questions about the sustainability of public debt (high borrowing costs, weak tax bases, etc.), growing vulnerability to increasingly frequent climatic events, etc. In addition, the region is still characterised by fragile political structures and security environments, as illustrated by a historically high level of violent events. **Finally, several significant risks continue to weigh on these forecasts:** rising levels of protectionism worldwide (although Africa appears to be relatively unaffected by recent increases in US customs duties), greater “financial autarky” on the part of the United States, which could hamper the financing capacity of international financial institutions (which are crucial to the “financing plans” of the region's states).

LATIN AMERICA

- The region is expected to slow down between 2025 and 2027. It remains sensitive to developments in relations with the US
- Persistent fiscal challenges underscore the urgency of consolidation efforts and heighten vulnerability to future shocks
- Structural issues must be addressed to safeguard long-term growth potential prospects

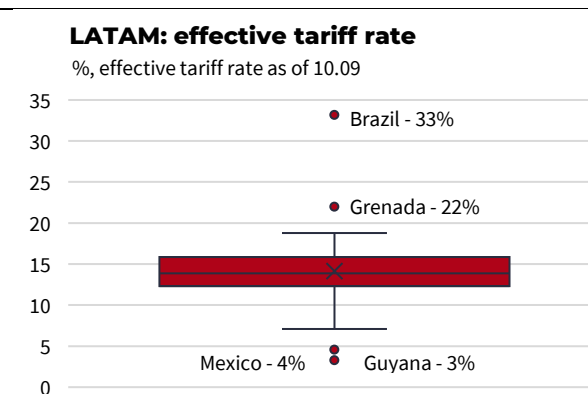
The region is expected to slow down between 2025 and 2027 (2.3%, 2.0%, 2.1% respectively) reflecting significant divergence across countries. Argentina is set for a sharp rebound in 2025 (5.5% per IMF), as its macroeconomic adjustment plan, supported by fresh liquidity from the latest IMF program, deliver results. Growth will moderate thereafter but remain dynamic as inflation normalizes. Brazil and Mexico are expected to outperform previous forecasts in 2025, though their medium-term outlooks remain subdued. Colombia should accelerate to 2.4% in 2025 per the IMF and show resilience thereafter, anticipating policy shifts following next year's elections, though inflation remains stubborn. Smaller economies continue to show upbeat prospects, albeit with heightened volatility from external risks.

Regional FX see gains YTD following significant depreciations late 2024



Source: LSEG, SG Economic and Sector Studies

US policy, including tariff policy, towards the region is shifting



Source: US Census Bureau, SG Economic and Sector Studies

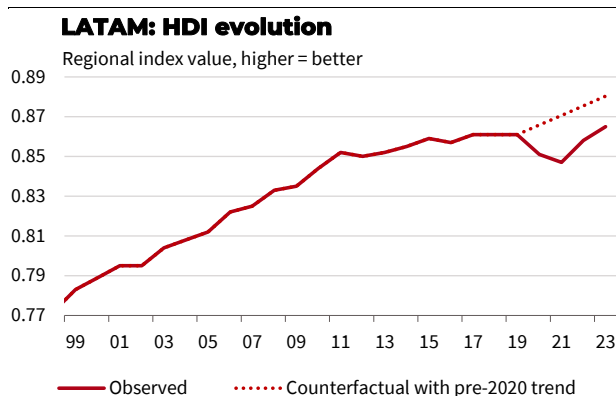
Local currencies have recovered some of the sharp losses from late 2024, as the region's international standing becomes more fragile. The Trump administration has adopted a more interventionist stance than expected, diverging from its previous term. Notably, the implementation of 50% tariffs on Brazilian imports since August, a response to the trial of former President Jair Bolsonaro, despite its domestic nature embodies this shift. The U.S. is also using stronger language regarding regional efforts to combat drug trafficking, leading to the deployment of marines in the Caribbean. This includes operations against cartels now designated as terrorist organizations, such as the recent strike on a Venezuelan vessel allegedly linked to *Tren de Aragua*.

Trade policy is also taking a different turn. Mexico currently enjoys a more favourable tariff position under USMCA, and this privileged relationship is expected to continue as renegotiations begin next year. In contrast, the rest of the region faces higher base tariffs, with significant sectoral disparities: oil and gas are largely exempt, while copper, steel, and aluminium face rates of up to 50%.

Labour markets remain resilient underpinning consumer spending, while investment is set to rebound. Some softening is expected, with the capacity of the countries to limit informality remaining highly dependent on the local context and national legislation. Investment remains subdued with the regional investment rate standing at its lowest level since 2003, and FDI flows having contracting by 12% in 2024, notably in the large economies of South America (Argentina, Chile, Colombia).

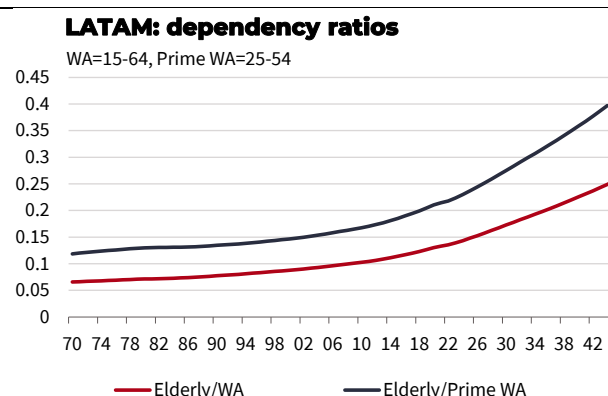
Investment is expected to rebound over the rest of the decade as the region capitalizes on investors' interest in digital economy, clean energy and mining projects. Additional tailwinds could come from changes in local environments, either from reforms that cut red tape and bureaucratic hurdles, and/or changes towards more pro-business governments.

Gaps in development following the pandemic haven't close



Source: World Bank, SG Economic and Sector Studies

Ageing population poses risks to the fiscal accounts and catch-up



Source: UN, SG Economic and Sector Studies

The region continues to face structural challenges that could hamper its long-term productivity growth. Shortcomings in education and health have not been overcome after the Covid crisis as indicated by a regional Human Development Indicator that just recovered its 2019 level. Moreover, ageing population combined with high migration and lower than expected birth rates challenges the region's potential as dependency ratios will rapidly deteriorate, before countries catch-up to advanced economies and pressuring challenged social security systems and public finances further. Institutional fragilities and security challenges are persistent in several countries (Mexico, Central America, Colombia, Venezuela) limiting economic activity.

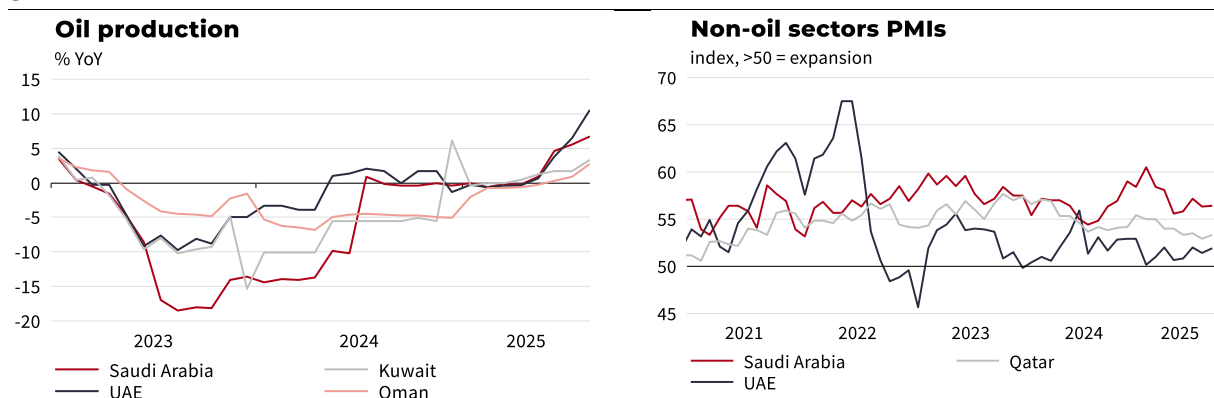
The balance of risks remains tilted to the downside. A sharper-than-expected deterioration in consumers' conditions could lead to a deeper contraction in the coming years. The region remains exposed to downward pressure on external demand and commodity prices, with a dual impact on growth and tax revenues, particularly in South America. Fiscal space remains extremely limited, heightening the risk that countries may lack the necessary tools to respond effectively to future shocks.

GULF STATES

- **Growth in the GCC will accelerate in 2025 and 2026, mainly due to the rebound in oil production**
- **This favourable economic momentum is also supported by FDIs, which has risen sharply since 2021**
- **Despite a still-difficult regional geopolitical context, the risks faced by the region are limited**

Average growth in the Gulf Cooperation Council (GCC) countries is still expected to accelerate in 2025 and 2026, to around 3.5% and then 4% (vs. less than 2% in 2024). This acceleration will be mainly explained by the rebound in oil productions, in line with the OPEC+ decision (in April 2025) to gradually cancel the reductions decided in 2023 (as a reminder: 2.2 million barrels/day – mb/d – withdrawn from the market). Since then, those who have adopted an “aggressive line” (aiming at cancelling these reductions before the end of 2025), such as Saudi Arabia and the United Arab Emirates, have recorded the most significant rebounds (these countries also have the most “easily accessible” marginal production capacities). For their part, non-oil sectors should remain dynamic, as illustrated by PMIs still firmly in the expansion zone (and despite a slight decline in recent quarters, probably due to the still delicate regional geopolitical context and still low oil prices). These sectors continue to benefit from significant investment plans (mainly public) in favour of the diversification and “greening” of their economies (while the region remains one of the most exposed to climate risks – more particularly to transition risks).

Rebounds in oil productions will support Non-oil sectors continue to show dynamism growth rates

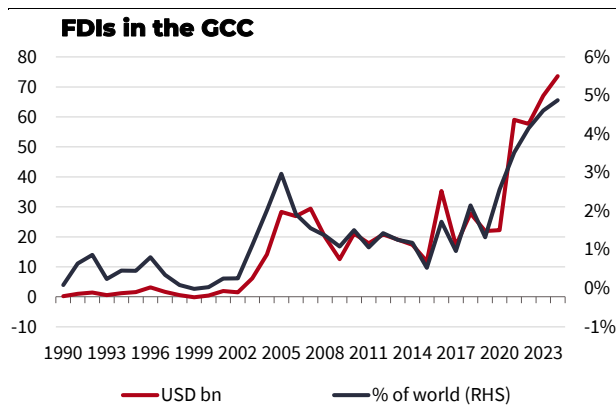


Source: Refinitiv, SG Economic and Sector Studies

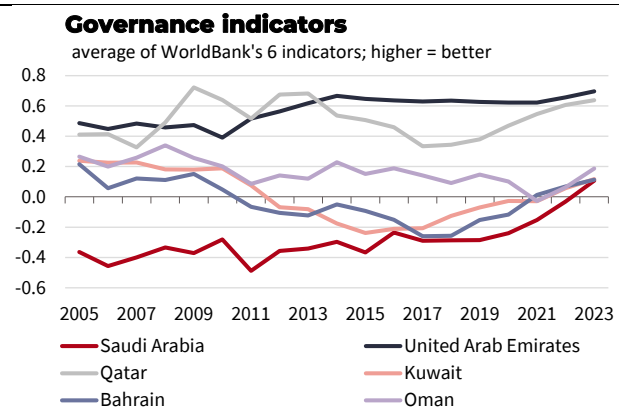
The region's economies are also benefiting from the significant increase in Foreign Direct Investment (FDIs), which exceeded USD 70bn in 2024, vs. USD 22bn in 2019. Portfolio investment has also increased, driven by international investors' appetite for GCC fixed income products (particularly debt): Eurobond issues thus exceeded USD 15bn during the first 8 months of 2025, the highest level

(over a comparable period) since 2020 (USD 18bn). Kuwait, traditionally absent from international capital markets (a single Eurobond issue in 2017), has also planned several issuances for 2025 and 2026, following the vote of a new law allowing this type of operation in April 2025. In total, total non-resident private capital inflows reached USD 175bn in 2024 and are likely to exceed USD 200bn this year (which would constitute a historic high), compared to a GCC GDP of around USD 2,300bn. The dynamism of these capital inflows reflects in particular i) the general improvement in governance environments in the GCC countries for more than 5 years, and ii) the particularly solid macroeconomic fundamentals of the region, illustrated (*inter alia*) by vast public assets abroad (estimated at around USD 4,200bn at the end of 2024, or 180% of regional GDP), stable currencies (because they are pegged to the USD) or particularly low inflation rates (around 2% forecasted for 2025 and 2026).

Rising FDIs since 2021...



... probably lifted by improving governance indicators



Source: Refinitiv, UNCTAD, SG Economic and Sector Studies

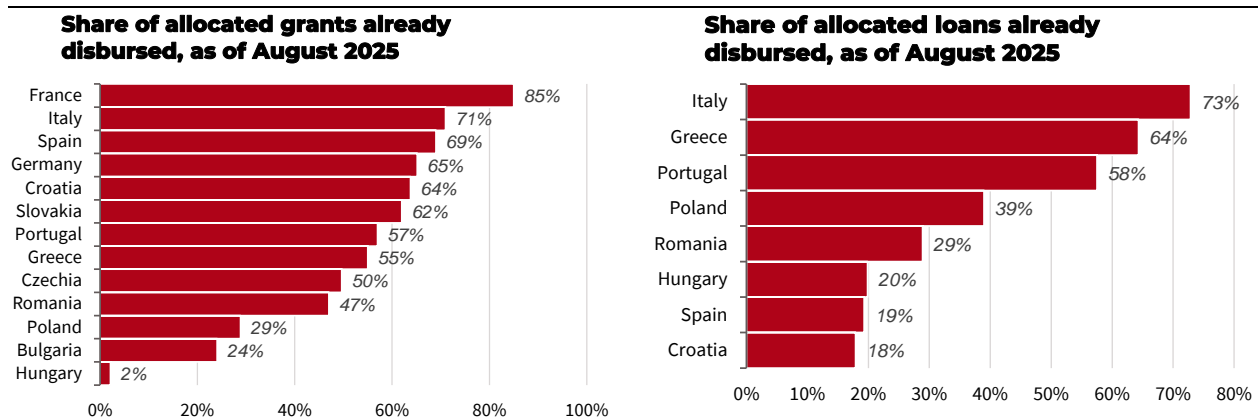
More generally, the risks to these regional forecasts remain contained, despite a still delicate regional geopolitical context. For example, the main market indicators (stock markets, spreads) have reacted very little to the Israel-Iran confrontation in June 2025, despite direct “physical consequences” for certain Gulf countries (e.g. Iran's attack on the American base at Al-Udeid in Qatar). The region also appears to be quite insensitive to possible increases in US customs duties, as raw materials are traditionally excluded from these measures. The Gulf countries obviously remain dependent on oil prices, which are expected to be relatively stable (and low) over the next few years, due to the good performance of global production and a still sluggish global demand (as illustrated by the downward revisions made – almost monthly – by the IEA).

CENTRAL AND EASTERN EUROPE

- The main growth drivers in the region will remain household consumption and investment thanks to an acceleration in the absorption of EU funds (after a slow start)
- Nevertheless, divergences in growth trajectories are appearing, with a marked slowdown in some countries implementing large-scale fiscal consolidations, such as Romania
- The impact of the 15% tariffs decided by the Trump administration should be limited and the region could benefit from the German stimulus plan focused on infrastructure and defence

Growth in the region will continue to be driven by domestic demand in 2H25 and 2026. Household consumption will benefit from real wage increases in a context of contained inflation and tight labour markets (low unemployment rates associated with labour shortages in several sectors). In this context, the services sector, and in particular retail sales, should continue to perform well. In addition, investment is expected to be driven by the increased absorption of EU funds, both *Next Generation EU funds* (available until the end of 2026) and European Structural and Investment Funds (available over the period 2021-2027). Note that the absorption of EU funds has been slow in CEE until August 2025 compared to the Euro area. While external demand has so far been sluggish, the German stimulus plan could support exports from CEE, particularly for building materials, machinery and electrical equipment.

The region is at the bottom of the league tables ... as well as NGEU loans in terms of absorption of NGEU subsidies...



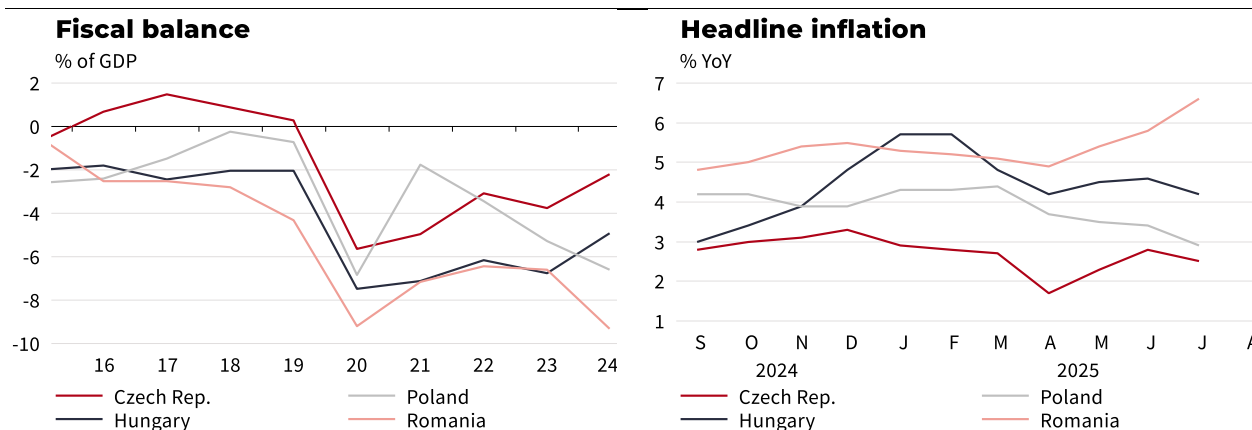
Source: European Commission, SG Economic and Sectoral Studies

Divergences in growth trajectories are emerging in the region, with dynamic growth expected in some countries (Czech Republic, Poland) and a more or less severe slowdown due to fiscal consolidations implemented in particular in Romania and Hungary. Czech Republic and Poland will post sustained growth driven by private consumption and investment supported by EU funds absorption.

Note that Poland has regained access to more than EUR 150 bn (i.e. 20% of GDP) of EU funds in 2024 following reforms favourable to the rule of law implemented by the pro-European government. In Czech Republic, activity will also benefit from the rapid growth of the construction sector and from the recovery of the manufacturing sector, which bottomed out in January 2025. Conversely, the Romanian and Hungarian economies could post a slowdown due to the fiscal consolidation plans implemented. The Romanian Prime Minister announced a fiscal consolidation package in July including measures of around 0.6% of GDP in 2025 (notably an increase in VAT and excise duties from 1 August) and 3% of GDP for 2026 (public wage and pension freeze, increase in the dividend tax, increase in the special tax on banks' gross revenues, increase in the number of contributors to the public health system, cuts in investment spending). This consolidation plan – key to ease financial tensions, maintain access to EU funds and avoid a downgrade of the Romanian sovereign – will weigh significantly on growth in the 2H25 and in 2026. In Hungary, fiscal consolidation, combined with weak investment (EUR 18 billion of EU funds out of EUR 28 billion remain blocked), are weighing on activity, despite a strong dynamic of foreign direct investment in the country (notably in the battery sector).

Romania's large-scale fiscal consolidation will have an impact on growth...

... and on inflation, due in particular to the increase in VAT implemented in August 2025.



Source: Refinitiv, SG Economic and Sector Studies

Inflation is expected to remain stable in the region (with the exception of Romania) in late 2025 and into 2026 amid moderate energy prices. Romania is expected to see a sharp rise in inflation due to the liberalisation of electricity prices in July 2025 and to the VAT hike in August 2025.

Despite this overall stability of consumer price indices in the region, monetary policies are expected to diverge in some countries. In Czech Republic and Hungary, policy rates are expected to remain stable. The Czech National Bank, which has eased its monetary policy since the end of 2023 (cutting the key rate by 350 bps over the period to 3.5% in August 2025), is not expected to make further rate cuts in a context of overheating real estate markets and rising food prices. The Hungarian central bank is also expected to keep its policy rate unchanged at 6.5% in the face of persistently high inflation expectations. In Poland, the central bank started lowering

its policy rate in April 2025 and is expected to continue its easing cycle in the 2H25 and 2026 amid stable prices. In Romania, the central bank is facing a difficult combination of temporary price shocks and a stagnant economy. For 2H25, we expect rates to remain stable while rate cuts could resume in 2026 assuming a disinflationary trend is on track.

Risks to growth are tilted to the downside amid uncertainty around the US administration's trade policy and talks around a peace agreement in Ukraine.

The trade agreement signed between the EU and the US at Turnberry at the end of July and raising tariffs to 15% on the majority of European products imported into the US is expected to have a limited impact on CEE given the marginal share of the region's exports to the US. Nevertheless, in a context of strong integration of the region into global value chains, particularly for the automotive sector, the indirect impact, through the slowdown in German exports to the US, has to be closely monitored. In addition, the region remains impacted by the lack of progress on a peace agreement in Ukraine and by the reduction in US bilateral aid. In this context, the majority of countries have planned a sharp increase in defence spending that could affect their public finances. However, the introduction by the European Commission of a safeguard clause (requested by fourteen Member States) gives the region some fiscal flexibility for the next four years.

CONTACTS

Michala MARCUSSEN

Group Chief Economist
+33 1 42 13 00 34
michala.marcussen@socgen.com

Olivier de BOYSSON

Emerging Markets Chief Economist
+33 1 42 14 41 46
olivier.de-boysson@socgen.com

Emmanuel MARTINEZ

Chief Environment Economist
+33 1 57 29 57 88
emmanuel.martinez@socgen.com

Ariel EMIRIAN

Head of macroeconomic analysis
+33 1 42 13 08 49
ariel.emirian@socgen.com

Edgardo TORIJA ZANE

Head of macro-sectoral and macro-finance
analysis
+33 1 42 14 92 87
edgardo.torija-zane@socgen.com

Foly ANANOU

Euro area, France
foly.ananou@socgen.com

Benoit ASTIER

South and Central Asia, Turkey, Climate
benoit.astier@socgen.com

Evelyne BAHN

Asia
evelyne.bahn@socgen.com

Constance BOUBLIL-GROH

Climate, Central & Eastern Europe, Russia
constance.boublil-groh@socgen.com

Natalia CARDENAS FRIAS

Germany, Latin America
natalia.cardenas-frias@socgen.com

Clément GILLET

Africa, Middle East
clement.gillet@socgen.com

Dominic LOCK

North America
dominic.lock@socgen.com

Danielle SCHWEISGUTH

Western Europe
danielle.schweisguth@socgen.com

Antonio VISANI

Climate, United Kingdom
antonio.visani@socgen.com

Stéphanie HUET

Assistant
+33 1 57 29 34 97
stephanie.huet@socgen.com

Yolande NARJOU

Assistant
+33 1 42 14 40 07
yolande.narjou@socgen.com

Société Générale | Société Générale Economic and Sector Studies | 75886 PARIS CEDEX 18

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