

# Quarterly economic outlook: A shocking decade.



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Roy Sullivan, “The Human Lightning Rod,” is listed in *Guinness World Records* for being struck by lightning seven times between 1942 and 1977, more than any other person in recorded history. In more recent years, like Sullivan, the global economy has been subjected to multiple shocks: COVID-19 in 2020, Russia’s invasion of Ukraine in 2022, the Trump administration’s “Liberation Day” tariffs in 2025, and the current open military conflict in the Middle East that is causing severe shortages of crude oil and natural gas, as well as their byproducts and derivatives, along with a broad range of key commodities that feed into industrial and agricultural processes. Faced with the fourth severe economic shock of the last six years, present-day businesses, consumers, governments, investors, and policymakers could be forgiven for chalking up this string of stressors to the type of bad luck that afflicted Sullivan. That’s especially true for central bankers and investors who, for the second time since 2022, face a heightened risk of stagflation (that is, slower-to-negative economic growth combined with higher inflation); prior to 2022, they hadn’t had to deal with this situation since the 1970s.

# Squinting into the fog of war

Before the current conflict began at the end of February, Citigroup's Economic Surprise Indexes indicated that economic data was starting to look more solid in emerging markets, particularly China, as well as the U.S. The indexes painted more concerning pictures for Canada, Europe, Japan, and the U.K. at the time, but recessions for these countries didn't seem imminent. Most observers expected global economic growth to slow slightly during 2026, with inflation continuing to improve despite remaining stubbornly above most central banks' desired levels.

Private-credit worries were dragging on the outlook to some extent—but earnings-growth estimates were still well into positive territory, and AI-related companies' massive investment plans were expected to provide meaningful support to economic activity. Government fiscal expenditures were also expected to contribute. With the exception of the Bank of Japan, which has been marching to the beat of its own growth-and-inflation drummer for several decades now, advanced-economy central banks appeared to be at or near the end of their recent rate-cutting cycles, with the long-and-variable lags of monetary policy likely to bring additional benefits. The fog of war has now pushed some of these considerations into the background and called others into question.

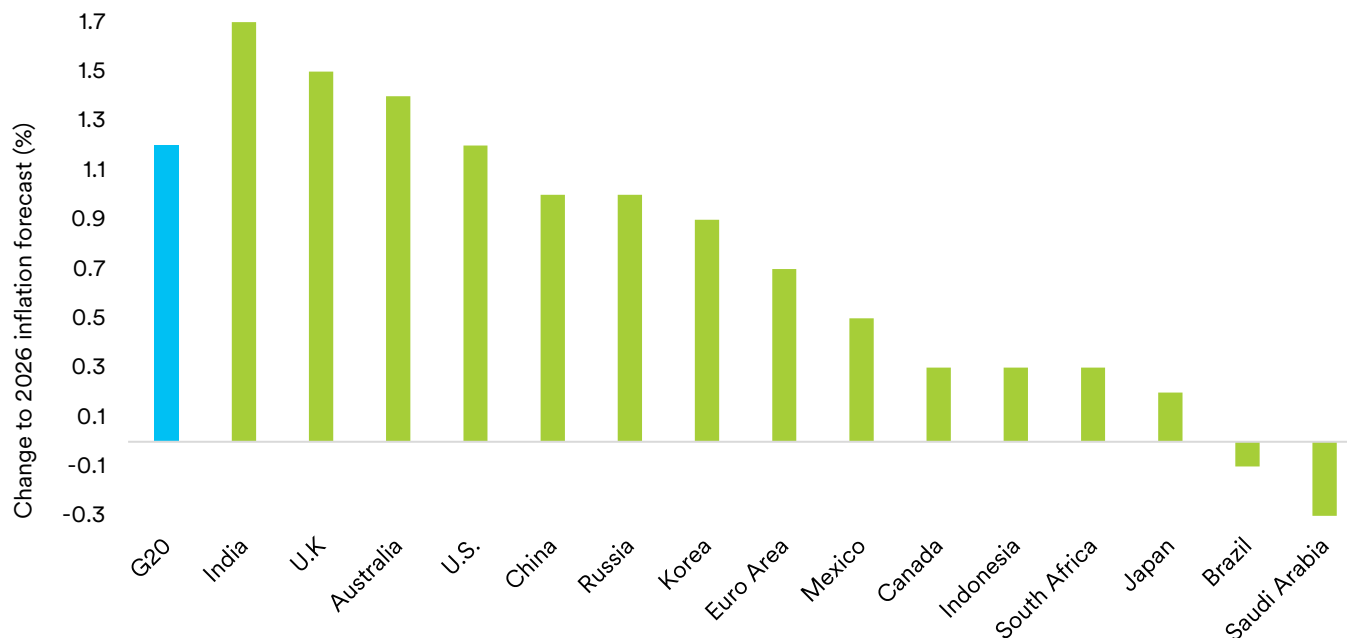
While private-credit worries remain in play, we do not expect them to create risks to banks, their depositors, or the payments system, unlike the Global Financial Crisis of 2008-2009. For the most part, equity analysts have not tempered expectations for corporate earnings and cash flows, and March's market selloffs have made valuations more attractive. But higher commodity prices and lower supplies will likely hamper economic activity in the near term; the normally favorable effects of fiscal impulses are now at risk of being dampened or overwhelmed by those higher costs, and markets are now expecting a number of central banks to raise interest rates in 2026.

## Financial markets: Complacent or composed?

Given that outlook, it's reasonable to ask why financial markets have nevertheless held up reasonably well. In the first weeks of the conflict, some observers asserted that markets were being too complacent with the dizzying array of risks posed to the global economy by Iran's effective closure of the Strait of Hormuz. We would push back on that narrative a bit. The strait has long been seen as a critical commodity-and-shipping chokepoint for the global economy. To hear energy and military analysts tell it, it was always a worst-case hypothetical scenario rather than one that anyone thought was likely to occur. From that standpoint, the attack on Iran has brought the global economy across the Rubicon, so to speak, so assertions of investor and market complacency are not entirely out of bounds. However, markets are complex, future-discounting systems that normally contemplate countless potential future states of the world. And, as long as there was a possibility of hostilities winding to a close sooner rather than later, some of those future states of the world were relatively benign. At the same time, if the conflict intensified (with broader damage to Persian Gulf energy infrastructure, for example) or persisted long enough to disrupt global supply chains even further, there were some future states of the world that could undermine global economic activity and create heightened uncertainty with regard to inflation and interest rates. In a war-induced fog as thick as this one, it's impossible to put accurate probabilities on possible outcomes; this, arguably, means that relatively well-behaved markets were doing a reasonable job of pricing in a wide range of possible outcomes. Markets started to price in a more negative outcome later in March. This was interrupted briefly by an enthusiastic reaction to President Trump's public musings about the war possibly drawing to a close soon, but market reactions to his speech on April 1st have been broadly negative thus far. Given the Strait of Hormuz appears to be firmly under the Iranian government's control for now, it seems reasonable that markets have priced out some of the most benign outcomes. Nonetheless, it seems that the U.S. intends to withdraw from the conflict soon, and at least one Iranian official has acknowledged direct talks (while denying they constituted negotiations). As investors, we can only hope these announcements and recent attack escalations are part of a larger bargaining process.

Many forecasters have made negative revisions to their economic outlooks in response to the conflict, calling for higher headline inflation and slower growth. For example, the Organisation for Economic Co-operation and Development's (OECD) most recent update lowered its December 2025 estimates for 2026 growth by 0.4% or more for the euro area, Korea and the U.K., while inflation estimates increased meaningfully for most members of the G20, as shown in Exhibit 1. Core inflation estimates remained benign, but we think these could also be subject to upward revisions if supply chain snarls persist for a meaningful period—as long as economic activity does not slow sharply.

## Exhibit 1: Higher headline inflation in the pipeline for most countries



Source: OECD Interim Economic Outlook 119 database; and OECD Economic Outlook 118 database. Blue bar indicates G20 as a group, green bars represent individual G20 member countries. Difference from December 2025 OECD Economic Outlook in percentage points, based on rounded figures. The G20 aggregate uses moving nominal GDP weights at purchasing power parities (PPPs). Revisions to PPP estimates affect the difference in the aggregate. Based on data available up to March 23, 2026. India is based on fiscal year starting in April.

It's worth noting that the OECD's downside case projections (which assume price shocks of \$135 per-barrel crude oil and €77 per-megawatt natural gas) are much starker, with growth falling most significantly among Asian OECD members for at least two years, followed by Europe, and then by the Americas. Inflation was also projected to be highest among Asian OECD and non-OECD countries, followed by OECD members in the Americas and Europe, respectively. The actual inflation experience would likely vary considerably across Europe given OECD Europe is composed of countries in eastern, northern, and southern Europe, Scandinavian nations (including energy-rich Norway), and Turkey.

## Looking at history to update the roadmap

Geopolitical shocks are always an educational experience for market strategists, be it geography, political history, cultural peculiarities, industry dynamics and jargon, or any number of other things. This war has been no exception, with strategists busily dusting up on a variety of subjects, including the region's geographic features, the commodity-production facilities and transit routes around the Persian Gulf and Red Sea, the current political alignments within the Middle East and beyond, and the existing energy byproducts and derivatives (and their many downstream uses)—not to mention terms like *force majeure* (an event or effect that cannot be reasonably anticipated or controlled), *shut-ins*, *feedstocks*, *bunker fuels*, *bromine*, *urea*, *NAPHTHA* (a flammable liquid made from distilling petroleum), and *days cover* (the amount of a commodity or currency that a country holds measured in days). Economic, financial, and political analysts engaged in this crash course since the start of the conflict would almost certainly agree with what markets seem to have been saying—that the world is faced with an unusually complex situation that presents a range of possible outcomes (not only within the energy sector but also in shipping, agriculture, industry, tourism, and medicine) with as-yet-unknown probabilities that are heavily conditional on the direction and duration of the war. Updating an investor roadmap for 2026 and beyond is currently a challenging endeavor, to say the least.

In these kinds of situations, it can be reassuring to look at similar historical episodes. So far, oil, commodity, equity, and equity-options markets have followed paths that, for the most part, resemble those of prior energy-supply shocks arising from geopolitical conflicts. Of course, we're still in the early days of the war, and there are no guarantees. As we monitor the conflict and its ongoing impacts on global economic and market conditions, there continues to be at least one key takeaway: this is the "mother-of-all" supply shocks. Many countries and industries will likely face serious shortages in the coming weeks

and months that could, in the case of energy-infrastructure damage, reportedly take years to repair, according to the International Energy Agency, the government of Qatar, and others. If the warring parties were to find an exit opportunity sooner than later, any residual turbulence within global supply chains should prove temporary and without much economic scarring. If the combatants fail to find an off-ramp soon, the global economy could be in for some rough and somewhat unprecedented sledding.

## Impacts will be uneven

From a 30,000-foot level, the conflict is going to reallocate revenues, costs, income, and earnings across sectors, industries, income brackets, and geographies to as-yet-unknown extents and durations—with those shifts heavily dependent on the ultimate degree of intensity and persistence of the war. Several Asian countries are particularly exposed to Gulf region commodities and downstream goods. A number of countries will lose meaningful amounts of remittance income from migrant labor in Persian Gulf countries, and almost all countries will experience pressure on agricultural sectors due to the unavailability of key inputs. Following geopolitical shocks of recent decades, we’ve seen social and political unrest in some of the countries that were most negatively impacted, and that seems likely to recur in the wake of this conflict should it persist much longer. Looking at variables such as the percentages of energy, fertilizer, and food that are imported, foreign exchange reserves, and political-stability scores, we sought to identify the countries that might be most exposed to future instability. The results are shown in Exhibit 2, and it’s worth noting that there have already been rationing measures and initial unrest in a number of these countries, even those in the moderate-risk category. While these rankings are not something on which one should base their investment strategy, they can serve as a useful component of the investing roadmap that we’re trying to update.

**Exhibit 2: Political resilience could be tested**

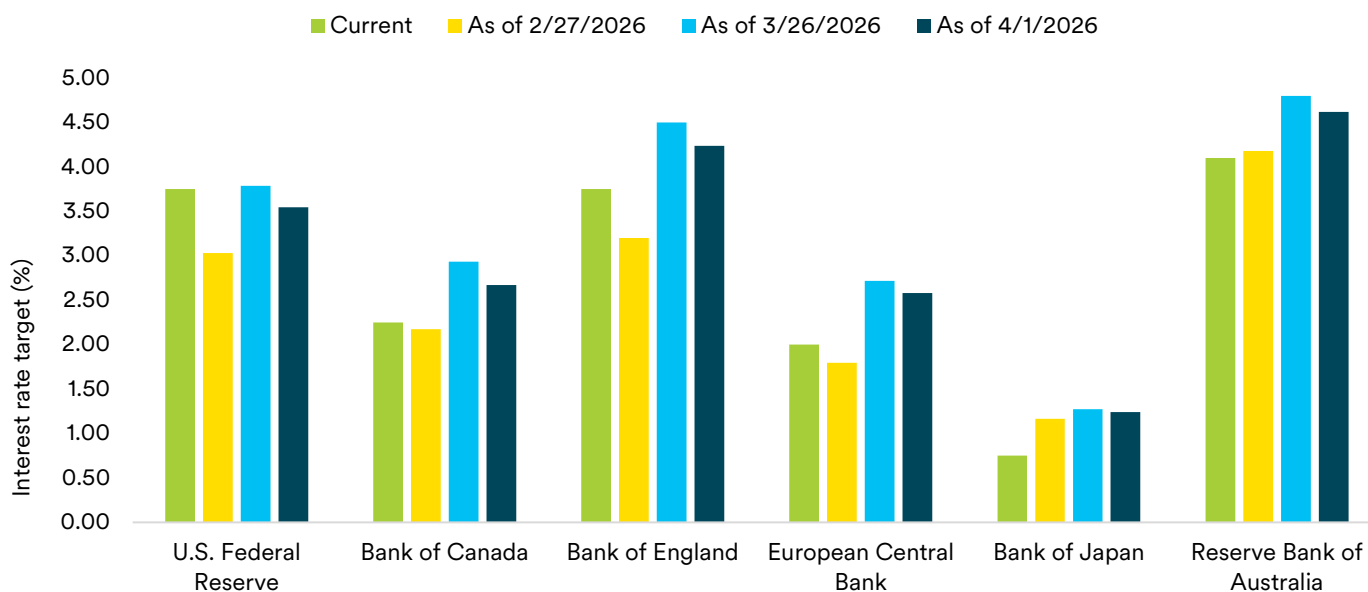
VERY HIGH RISK	HIGH RISK	MODERATE RISK	LOW RISK	VERY LOW RISK
Yemen Afghanistan Sudan Haiti	Myanmar Ethiopia Pakistan Nigeria Lebanon Bangladesh Kenya	Sri Lanka Egypt Turkey Philippines India Zambia Morocco Colombia Tanzania Thailand Tunisia Peru South Africa Ghana Bahrain Mexico Indonesia Brazil Ukraine Vietnam	Israel Saudi Arabia Kuwait Argentina Chile Russia Malaysia China Oman Poland Singapore	France U.K. U.S. Australia UAE Qatar Germany Netherlands South Korea Norway Canada Japan

Source: Food and Agriculture Organization, Fund for Peace, IMF, Raj Patel, Visual Capitalist, World Bank, SEI. Figures are estimates only and data is incomplete for some countries. Days cover calculated as estimated stockpiles divided by average daily consumption. Data as of March 24, 2026.

# What's a central banker to do?

Among the more interesting economic and market developments to this point are shifts in inflation and interest-rate expectations. As illustrated in Exhibit 3, there has been a sharp turn in expectations for the directions of global central banks' interest-rate policies. Before the Middle East conflict started, most advanced-economy monetary policymakers were expected to ease a bit further or remain unchanged in 2026. In late March, those rate cuts had been completely priced out of market expectations, and most central banks were expected to *raise* interest rates. After the recent relief rally, markets once again expect the U.S. Federal Reserve (Fed) to cut rates slightly, but other central banks are still expected to hike in the face of higher inflation risks.

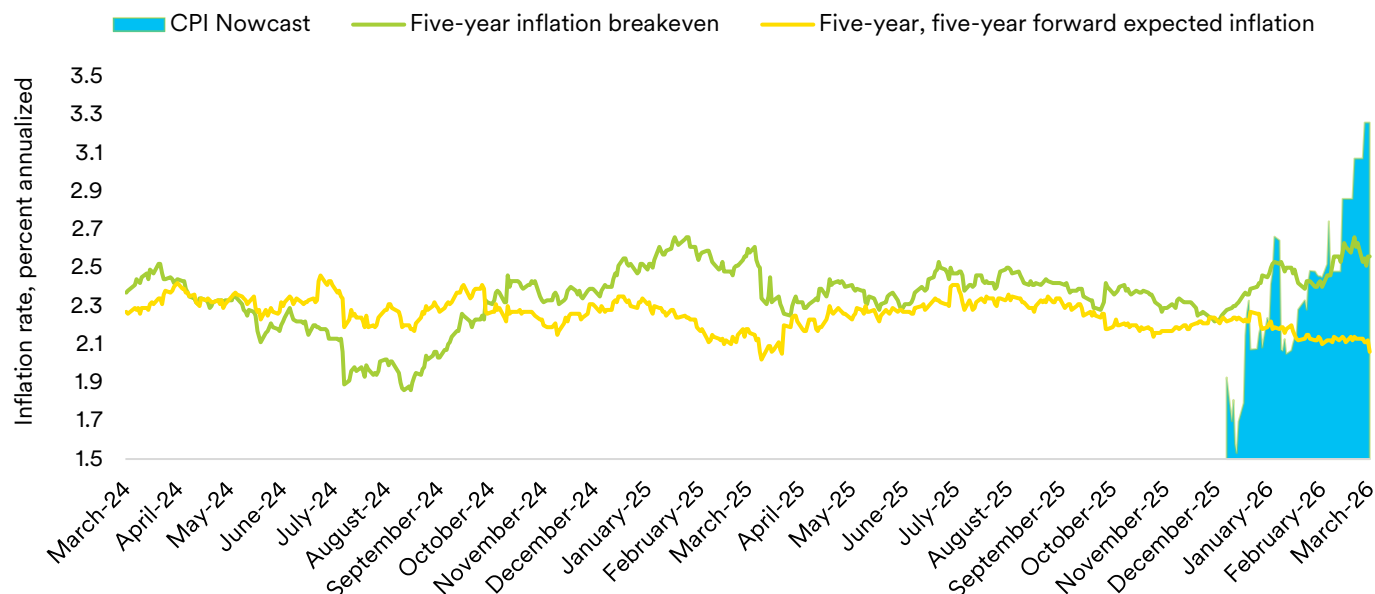
## Exhibit 3: Sharp reversal of monetary-policy expectations



Source: Bloomberg, SEI. Current interest rate targets and market-implied year-end rate targets derived from overnight index swaps as of February 27, March 26 and April 1, 2026.

There can be a robust debate about whether hiking interest rates is a prudent response to global supply shocks. The textbook approach is to look through these types of events as they lie well outside the reach of monetary policy. However, given the high inflation already experienced in this decade, it seems some central bankers are intently focused on defending their inflation-fighting credentials by doing whatever it takes to keep price-level expectations well anchored. Monetary policymakers in that camp might also argue there's a case to be made for using interest-rate policy to "shut in" business and consumer demand as long as various nodes of the global supply chain are having to shut in logistics and production. We think that argument is more tenuous than that of the textbook approach—as long as inflation expectations remain relatively stable (a point acknowledged by multiple central bank heads in recent days), and especially if markets begin to discount a global recession. As a result, we anticipate that central bankers are more likely to publicly mention the possibility of raising interest rates in order to spur markets into fearing that outcome while sitting on their hands when it comes to actual rate hikes (a behavior known as "jawboning"). If labor markets and the global economy start to sputter meaningfully, we expect that monetary policymakers would consider easing further. Nonetheless, near-term inflation expectations up to five years are sending warning signals while longer-term expectations are pricing in lower inflation (Exhibit 4). While falling long-term inflation expectations may reflect concerns about economic scarring, they could also simply be a function of lower inflation tending to follow periods of higher inflation. Central banks have committed procyclical errors in the past, so we can't rule out rate hikes entirely. Fed Chair Powell put it aptly at the press conference following the most recent Federal Open Market Committee meeting: "We just don't know."

## Exhibit 4: Inflation expectations at risk?



Source: Federal Reserve Bank of Cleveland, Federal Reserve Bank of St. Louis, Bureau of Labor Statistics, Bureau of Economic Analysis, Energy Information Administration, Financial Times, and Haver Analytics. Daily data from March 27, 2024, through March 27, 2026, as of March 30, 2026. Five-year and five-year, five-year breakeven inflation estimates are derived from nominal U.S. Treasury yields and Treasury Inflation-Indexed Securities yields. Cleveland Fed inflation nowcast is produced from a small number of available data series at different frequencies, including daily oil prices, weekly gasoline prices, and monthly CPI and PCE inflation readings.

## Additional political fallout risks

Although central-bank tightening is not our base case, the pain it would cause should prove tolerable as long as unemployment doesn't start marching higher. However, like so many other things, labor-market impacts also depend heavily on the depth, breadth, and duration of the conflict. Labor-market risks also highlight that central bankers aren't the only policymakers who could find themselves in a difficult situation—fiscal, trade, and regulatory policies could all be upended by persistent and widespread supply shocks. If the knock-on effects of the war are sufficient to cause higher unemployment and recessions, fiscal policy decisions could be especially fraught given already-substantial government debt levels in many countries. We would expect automatic, countercyclical fiscal stabilizers to take effect, but it could be far more difficult to enact the kinds of supportive measures (or, “excessive” measures, some might say for certain countries from 2021 on) that we saw during the initial years of the COVID-19 pandemic.

Investors should also be aware of how the conflict could impact elections, particularly the 2026 U.S. Congressional midterms. Comparing polling by SSRS, Reuters/Ipsos, and The Washington Post to historic data<sup>1</sup>, the attack on Iran had the lowest level of public support at its outset than any other conflict of the last 43 years (except for the 2011 NATO air campaign over Libya). Of course, if we've learned anything from the last 10 to 15 years, it's that poll results should be taken with appropriate skepticism. Still, it's clear that the Trump administration has taken quite the political gamble with this intervention. The president's approval rating has fallen by 10 percentage points to 40% since his second-term inauguration in 2025, according to an aggregation of recent polls by *The New York Times*.<sup>2</sup> Political forecasters and prediction markets are putting a high probability on Democrats reclaiming the majority in the House of Representatives this autumn, with longer odds of retaking the Senate (a majority in the latter would likely be quite narrow). If that happens, 2027 would likely see multiple House investigations including subpoenas, hearings, and potentially impeachment proceedings against one or more members of the Trump administration (although impeachments would have little chance of succeeding as they would require a two-thirds Senate approval). The bottom line is that policymaking in the U.S. could take a radically different turn in the 2027-2028 period,

<sup>1</sup> “War Approval Ratings,” <https://war-approval.vercel.app>, last accessed March 28, 2026.

<sup>2</sup> “President Trump's Approval Rating: Latest Polls,” <https://www.nytimes.com/interactive/polls/donald-trump-approval-rating-polls.html>, last accessed March 28, 2026.

with high risks of gridlock, intensifying partisanship, and additional government-funding impasses, as well as a higher hurdle for passing additional fiscal support in a negative economic scenario.

## **What's an investor to do?**

Fog of any kind is a navigational challenge, and that holds true for investors trying to negotiate the uncertainties of a major military conflict with potentially massive implications for global supply chains, economic activity, and inflation. In times like these, it's important to focus on some of the key tenets of strategic investing: As long as a portfolio is tailored to an investor's objectives and designed to navigate a wide range of economic and market environments, we believe the best response to geopolitical uncertainty is to take a deep breath, fasten one's seatbelt, and repeat as needed. Economies, markets, and investors will get through the current episode of geopolitical volatility. Once we're past it, let's just hope that we encounter smoother sailing and don't edge any closer to Roy Sullivan's record of seven shocks.

## **GLOSSARY AND INDEX DEFINITIONS**

For financial term and index definitions, please see: <https://www.sei.com/ent/imu-communications-financial-glossary>

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