Navigating an age of divergence

Global Economic Outlook 2026–2028: 1H 2026

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The short-term economic outlook continues to reflect mounting complexities, fueled by heightened geopolitical risk, persistent economic policy uncertainty, and growing divergence in a K-shaped global economy.

Foreword

This 1H 2026 Global Economic Outlook explores a world defined by a series of compounding challenges placing the economic system under ever greater strain. Heightened geopolitical risk, persistent policy uncertainty, rapid technological change, and mounting fiscal constraints continue to generate an operating environment best described as one of permanent uncertainty. Recent escalations of conflict across the Middle East are among several forces driving historically elevated uncertainty, raising baseline volatility across trade, investment, and capital flows.

Against this backdrop, the global growth outlook will remain below pre-pandemic levels. Global output will average 2.9 percent through 2028, compared with 3.2 percent growth in the decade prior to the pandemic. This growth is being supported by continued investment in artificial intelligence, adaptive supply chain strategies, and supportive fiscal policy, despite mounting geopolitical and structural headwinds.

This growth masks widening divergences. The global economy is increasingly K-shaped, with growth, inflation, and consumption outcomes varying sharply across regions, sectors, and income groups. Asia and Australasia will continue to be the fastest-growing region through the forecast period, led by the strong performance of India, the world's fastest-growing large economy. By contrast, Europe and Eurasia faces persistently weak growth prospects, weighed down by competitiveness challenges, demographic pressures, and geopolitical risk. Similar divergence is evident within economies, as higher-income households and technology-enabled sectors pull further ahead while lower-income consumers and traditional industries contend with inflation volatility and rising costs of capital in a polarized growth environment.

Policy choices are playing a central role in shaping these outcomes. Governments are intervening more directly in markets under the banner of economic security, accelerating the use of industrial policy, tariffs, subsidy supports, and investment controls. While these measures have delivered pockets of resilience and industrial gains, they have also introduced new and longer-term policy risks, weakened multilateral norms, and raised the cost of doing business across borders. At the same time, rising public debt levels are significantly constraining governments' ability to respond to future shocks, underscoring the limits of debt-financed growth.

For business leaders, there is no longer a single "average" economic trajectory against which to plan. Success in this environment will favor organizations that can both demonstrate agility and navigate divergence. This will require everything from redesigning supply chains to building constantly shifting geopolitical and policy risk into strategies. It will also require aligning investment with long-term structural changes such as AI adoption, demographic change, and climate risk. Firms that expand their strategic aperture, embrace longer-term resilience over short-term efficiencies, and position themselves as credible partners across a fragmented global landscape will be best placed to compete.

The assessment that follows examines how an environment defined by elevated geopolitical risk and wide-ranging uncertainty is translating into structural constraints, K-shaped economic outcomes, and a more interventionist policy environment—and how firms are adapting in response.

As always, we welcome your views on our analysis.

Erik R. Peterson
Partner and managing director
Global Business Policy Council
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What does the baseline outlook for the global economy suggest?

The global growth outlook is being shaped by the convergence of increased geopolitical risk, greater policy uncertainty, higher levels of technological disruption, and sharply rising debt, resulting in elevated volatility and headwinds to growth. Economic policy uncertainty spiked in April 2025 following the US tariff announcements, causing growth projections to decline. Economic policy uncertainty rose sharply again in March 2026 to roughly the same level as during the COVID-19 pandemic, following US–Israeli strikes in Iran and escalating conflict across the Middle East. These spikes reflect the degree to which economic policy uncertainty remains significantly elevated, even relative to past periods of turbulence in recent decade. Rather than dissipating, this uncertainty has become a persistent feature in the global economic environment, complicating the growth outlook. Indeed, our growth projections have moved considerably over the past year, reflecting this persistent uncertainty amid exogenous shocks and economic policy swings (see figure 1 on page 3).

Global growth is projected to average around 2.9 percent through 2028.

Amid this volatility, growth is projected to average around 2.9 percent through 2028. While this suggests slower growth than the 10-year pre-pandemic average of 3.2 percent, it is not as low as previous forecasts may have suggested. Offsetting tailwinds such as the surge in AI investment as well as broadly supportive fiscal policy in key global economies are propping up growth in the short term. For example, Germany plans to expand its budget deficit to 4.75 percent of GDP in 2026, the largest since 1975.[1] And Canada's 2025 Federal Budget proposes C$280 billion of increased spending over five years with a focus on infrastructure, housing, and the military. Further, baseline projections suggest that the United States and China, the world's two largest economies, will experience steady, albeit modest, average growth through 2028, helping anchor global output even as risks remain elevated. Both markets are expected to take steps to bolster growth in 2026, with the United States likely cutting interest rates and leaning on investment in AI and China deploying fiscal stimulus and targeted measures to lift domestic consumption and stabilize the property sector. However, the recent hostilities in the Middle East and subsequent disruptions to oil and gas markets represent a significant wildcard that could further disrupt the growth trajectories of both economies.

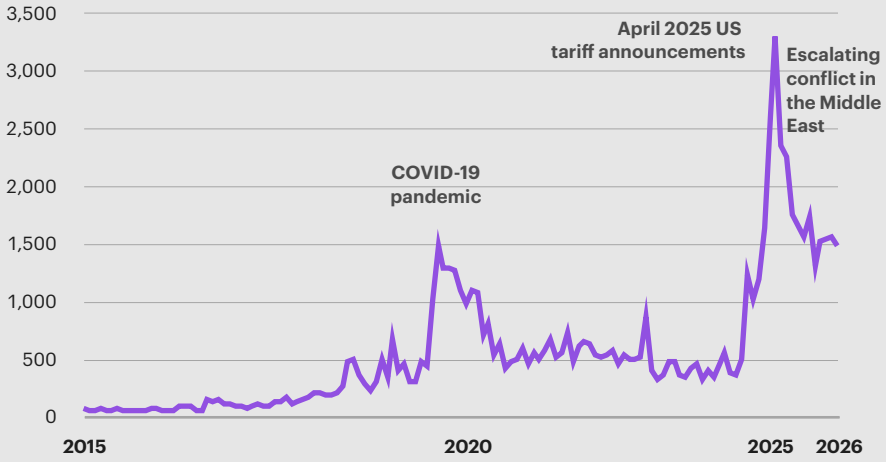
Business and consumer adaptation may also reduce some of the headwinds to growth. Companies from Unilever to Amazon are optimizing their supply chains to reduce the impact of external volatility in disrupting their bottom lines. Unilever, for example, has developed a digital replica of its entire supply chain that allows it to connect customer point-of-sale data and stock information to the company's supply system, using AI to assess and update plans in real time. General Motors is using technology-powered news scanning and data mapping to anticipate supplier disruptions. And Amazon managed to achieve record delivery speeds in the United States in 2025 by locating inventory closer to its end consumers. Taken together, these offsets are helping to stabilize growth or mitigate greater declines in growth, but they are not sufficient to overcome the structural and cyclical constraints that continue to limit upside dynamism.

[1] With the exception of the technical one-off deficit of 9.4 percent of GDP in 1995

Figure 1

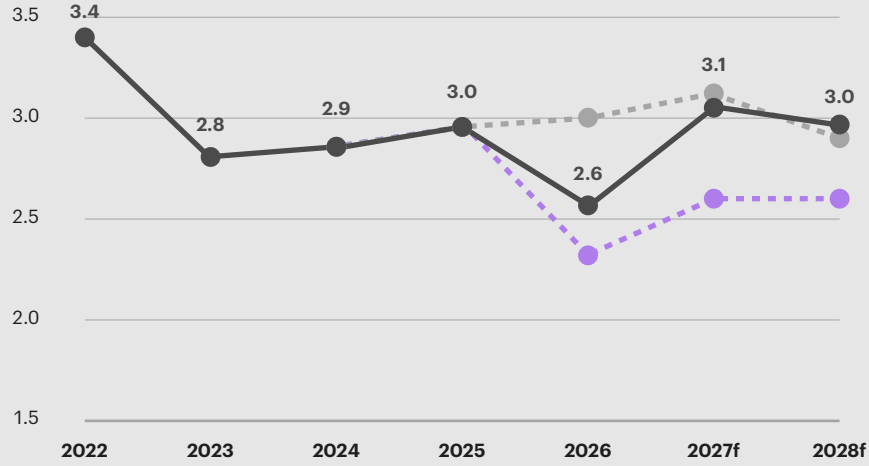
Heightened economic and trade policy uncertainty is fueling volatility in economic growth projections

Trade policy uncertainty index (Index, GDP-weighted average of national EPU indices, seven-day moving average)



Global economic output

(year-over-year percentage growth)



March 2026 forecast

January 2025 forecast

April 2025 forecast

GDP growth	2026f	2027f	2028f	Average 2026–2028f
January 2025	3.0	3.1	2.9	**3.0**
April 2025	2.3	2.6	2.6	**2.5**
March 2026	2.6	3.1	3.0	**2.9**

Note: January 2025 and April 2025 data is based on previous Global Economic Outlook forecasts.

Source: Kearney analysis

What is constraining growth? Cyclical pressures versus structural limits

The forces shaping the growth outlook differ markedly in duration and intensity. Some constraints are cyclical and may ease over time; others are structural and likely to persist, limiting upside and raising volatility.

Beyond inflation (see next section), wage growth is a cyclical constraint anticipated to impact the global economic outlook, especially in key advanced economies. For example, the Bank of England may not be able to drop interest rates this year as much as initially anticipated due to strong wage growth, up an estimated 3.5 percent in 2026, according to employer surveys. And in Germany, shortages of qualified labor in the near term could push wage growth to well above 3 percent this year. Though cuts to household energy taxes could offset the impact to inflation this year, CPI could rise to around 2.5 percent over the next three years.[2] Taken together, these near-term wage pressures are unfolding alongside deeper structural transformations in labor markets that could have longer-lasting implications for growth and productivity.

AI is at the center of such structural changes to labor markets. The IMF estimates that in the coming years, 60 percent of jobs in advanced economies and 40 percent globally will be enhanced, eliminated, or transformed by AI. And aging populations only add to these shifting labor dynamics. For example, a National Bureau of Economic Research study found that a 10 percent increase in the fraction of the population aged 60 and over in the United States decreased per capita GDP by 5.5 percent between 1980 and 2010 owing to slower labor productivity and employment growth. Absent offsetting gains from higher participation, immigration, or productivity-enhancing technologies, these demographic dynamics pose a sustained drag on growth across advanced and emerging economies alike, especially in those markets with significant aging populations such as Japan, Italy, South Korea, and China.

Geopolitical uncertainty is shifting from a cyclical constraint to more of a structural feature defining the economic outlook. The United States–Israel military offensive against Iran and its regional fallout, the United States' military operation in Venezuela, the ongoing war in Ukraine, and the unpredictability of foreign policy decision-making more broadly are all contributing to a persistently elevated risk environment that is reshaping trade, investment, and strategic decision-making across regions. For example, escalating conflict in the Middle East and disruption in the Strait of Hormuz is currently impacting roughly 20 percent of global oil trade, with the potential to drive up energy prices and inflation for a prolonged period worldwide. Indeed, a FitchRatings study in late 2023 found that a disrupted oil supply in the Middle East could shave off 0.4 percent from global GDP in the first year.

Climate change, long-term changes in the labor market, and demographic issues such as aging populations represent other structural challenges to the economic outlook. The World Meteorological Organization's latest estimates project that global temperatures will continue at or near record levels through the end of the decade, with an 80 percent chance that at least one of the years through 2029 will exceed 2024 as the warmest on record. This is especially significant, given that a 1°C hotter year could result in a 2 percent decline in overall economic activity as heat fatigue slows worker productivity. Climate change is already driving more frequent and intense extreme weather events that disrupt infrastructure, agriculture, and labor productivity, imposing rising costs on economies worldwide. At the same time, aging populations are reducing the growth of the labor force and increasing dependency ratios, which can slow GDP growth and pressure public finances in many advanced economies unless offset by higher labor participation or productivity.

[2] *Germany: Weak foreign demand poses risk to industrial recovery,* Oxford Economics, January 2026

Inflation dynamics and implications for cost of capital

Inflation pressures are easing on average, but the inflation environment remains volatile and increasingly divergent across countries and income groups. Overall, global headline inflation is projected to rise from 3.4 percent in 2025 to 4.1 percent in 2026 but will fall to 3.1 percent in 2027 and 2.9 percent in 2028 (see figure 2 on page 6). Inflation in key advanced economies will likely stay close enough to target to allow further modest policy rate cuts but remains threatened by volatility. For example, inflation in Germany and the United Kingdom is moving back to 2 percent levels, but a 2023 analysis by the European Central Bank suggests that inflation in Europe could rise by 0.8 percent if just one-third of oil and gas supplies passing through the strait of Hormuz were disrupted, suggesting greater inflationary pressures ahead. And the United States is also experiencing declines, though risks remain. The Peterson Institute for International Economics posits that US inflation could exceed 4 percent by the end of 2026 as delayed tariff effects, the fiscal deficit, and a tighter labor market, among other issues, converge.

Other markets are seeing much higher levels of inflation. Venezuela, Argentina, Iran, and Turkey could experience inflation levels well above 15 percent owing to chronic structural and institutional challenges, as well as geopolitical turbulence. Iran, for example, is now expected to see inflation of 66.8 percent this year. These disparities reinforce the K-shaped nature of the international inflation environment, with some economies regaining price stability while others remain trapped in high-inflation equilibria. Over the medium to longer term, the inflation outlook is expected to be more volatile than the pre-pandemic period as supply shocks, including those related to climate change, rising geopolitical instability, and policy uncertainty, continue to disrupt production and trade.[3]

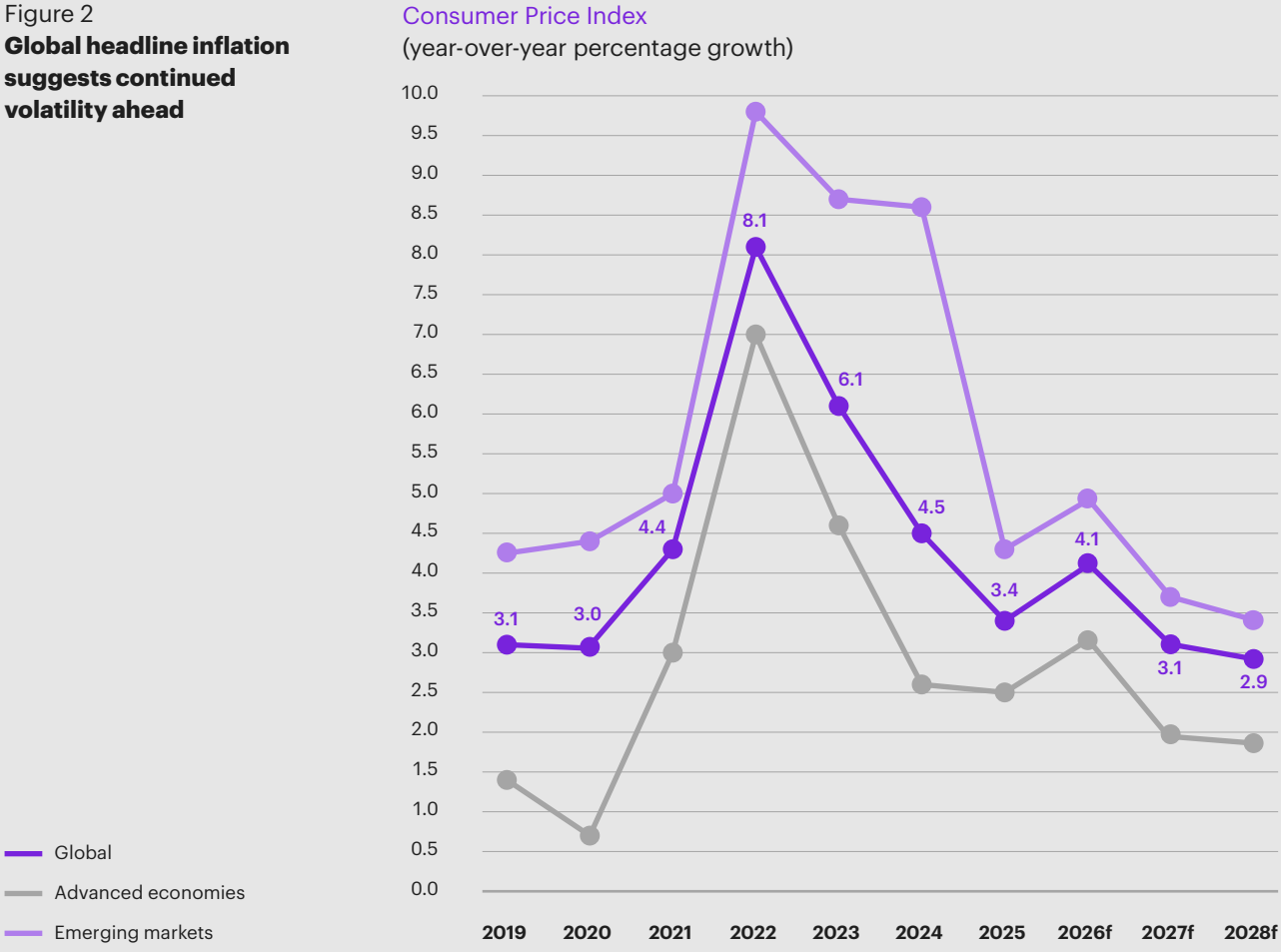
Responding to inflation volatility in advanced and emerging markets alike is becoming a challenge for governments and businesses, especially given inflation's impact on capital costs. As central banks raise rates, the cost of capital fluctuates. As such, some corporate treasury teams are shifting from floating-rate to fixed-rate debt to lock in interest rates. More broadly, firms are moving beyond purely financial hedging toward strategic responses that embed inflation risk into portfolio, pricing, and operating decisions.

Businesses are also implementing innovative strategies to account for inflation-induced cost of capital volatility. For example, Procter & Gamble has embarked on a "premiumization" campaign focused on shifting its portfolio toward higher-value, performance-driven products. With this strategy, the company aims to protect margins while simultaneously managing cost inflation. Similarly, Nestlé's Fuel for Growth program seeks to offset inflation by simplifying operations in Europe and investing in premium segments such as PetCare and Nespresso. In an environment of persistent inflation volatility, firms that combine financial discipline with strategic repositioning are better able to protect returns.

[3] *Global: Geopolitics unlikely to derail solid growth outlook,* Oxford Economics, January 2026

Figure 2

Global headline inflation suggests continued volatility ahead



Inflation in 10 largest economies

	GDP value 2026f	CPI, % change 2026–2028 average
United States	23,775,120.0	2.4
China	20,131,730.0	1.6
Japan	4,771,631.0	2.3
Germany	3,702,735.0	2.4
India	3,656,799.0	4.5
United Kingdom	3,377,250.0	2.6
France	2,767,362.0	1.9
Brazil	2,105,436.0	3.6
Italy	2,050,700.0	2.1
South Korea	1,971,464.0	2.0

10 highest inflation rates

	GDP value 2026f	CPI, % change 2026–2028 average
Venezuela, RB	64,276.8	156.0
Iran, Islamic Republic	457,419.7	34.9
Argentina	673,185.6	25.9
Türkiye	1,397,682.0	20.3
Nigeria	843,500.6	13.2
Angola	145,253.8	12.0
Egypt	564,220.9	9.2
Kazakhstan	261,498.6	10.7
Ghana	82,677.1	9.4
Zambia	31,378.9	8.0

Note: GDP is in constant prices and exchange rate, US dollars, million: 2015 prices

Sources: Oxford Economics; Kearney analysis

Fiscal constraints and limits of debt-financed growth

Even as inflation pressures ease in some economies, the room to maneuver for fiscal policy is narrowing. Rising public debt levels are constraining the scope, durability, and effectiveness of fiscal intervention. Looser fiscal policy in major world economies such as the United States and Europe is helping to cushion global GDP growth figures this year. For instance, the World Bank estimates that tax cut extensions in the United States and increases in public investment in some large euro area economies will partially offset trade-related challenges. However, this near-term support is coming at the cost of further stretching already-elevated sovereign balance sheets.

Astonishingly, global government debt is expected to surpass 100 percent by 2029. Approximately one-third of countries, accounting for 80 percent of global GDP, are driving up the value and pace of debt growth. The United States alone is already projected to exceed a 130 percent government debt-to-GDP ratio this year, with Japan expecting a striking 203 percent debt level (see figure 3 on page 8). These trajectories reflect structural shifts rather than temporary post-crisis deviations.

Although emerging markets have less debt than their advanced economy counterparts, debt in these markets is also rising. The World Bank estimates that the world's poorest countries paid a record $1.4 trillion in debt service obligations in 2023, with interest costs reaching an all-time high of 34.6 billion, four times the amount of a decade ago. Servicing the debt can be extremely challenging for these countries as high borrowing costs constrain their fiscal options. As a result, many governments face difficult trade-offs between debt servicing, social spending, and investment in growth-enhancing infrastructure.

As debt levels continue to grow through the end of the decade, governments throughout the world will have less ability to respond to future shocks, whether stemming from conflict, climate events, or financial instability. For the private sector, rising sovereign debt levels also pose indirect risks, including upward pressure on borrowing costs, crowding out of private investment, and greater constraints on the public spending for critical infrastructure and workforce development. Together, these dynamics underscore the growing limits of debt-financed growth as a tool for sustaining economic resilience in an environment of permanent uncertainty.

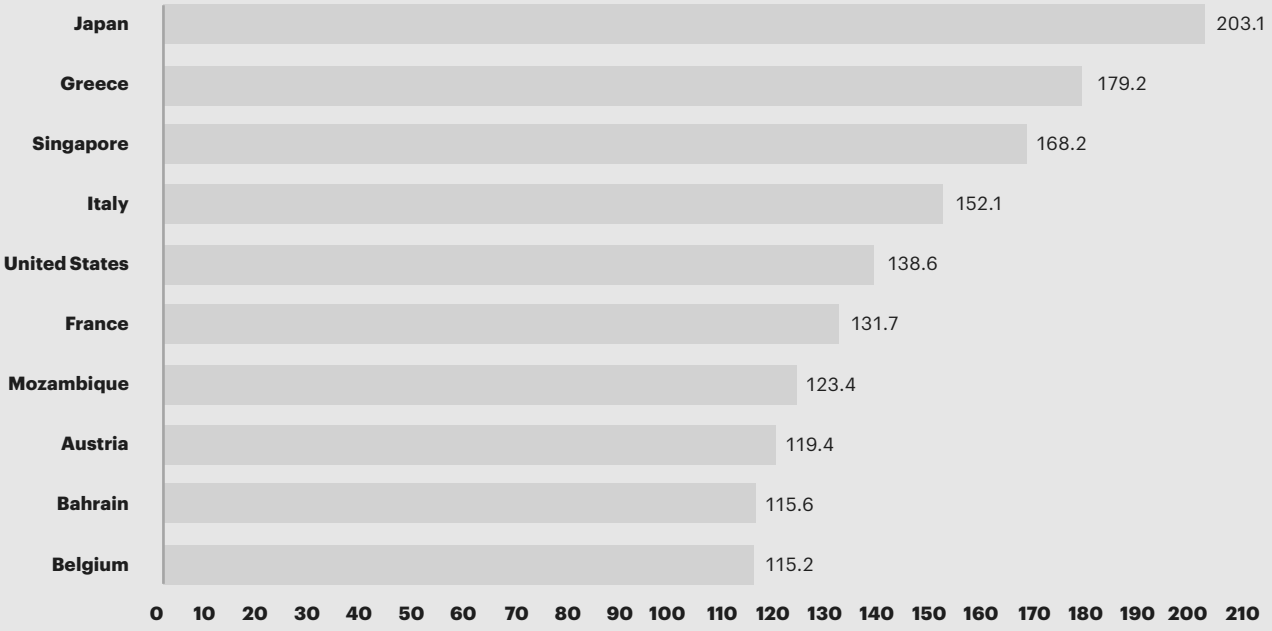
Rising public debt levels are constraining the scope, durability, and effectiveness of fiscal intervention.

Figure 3

Elevated debt levels present profound risks to the economic outlook

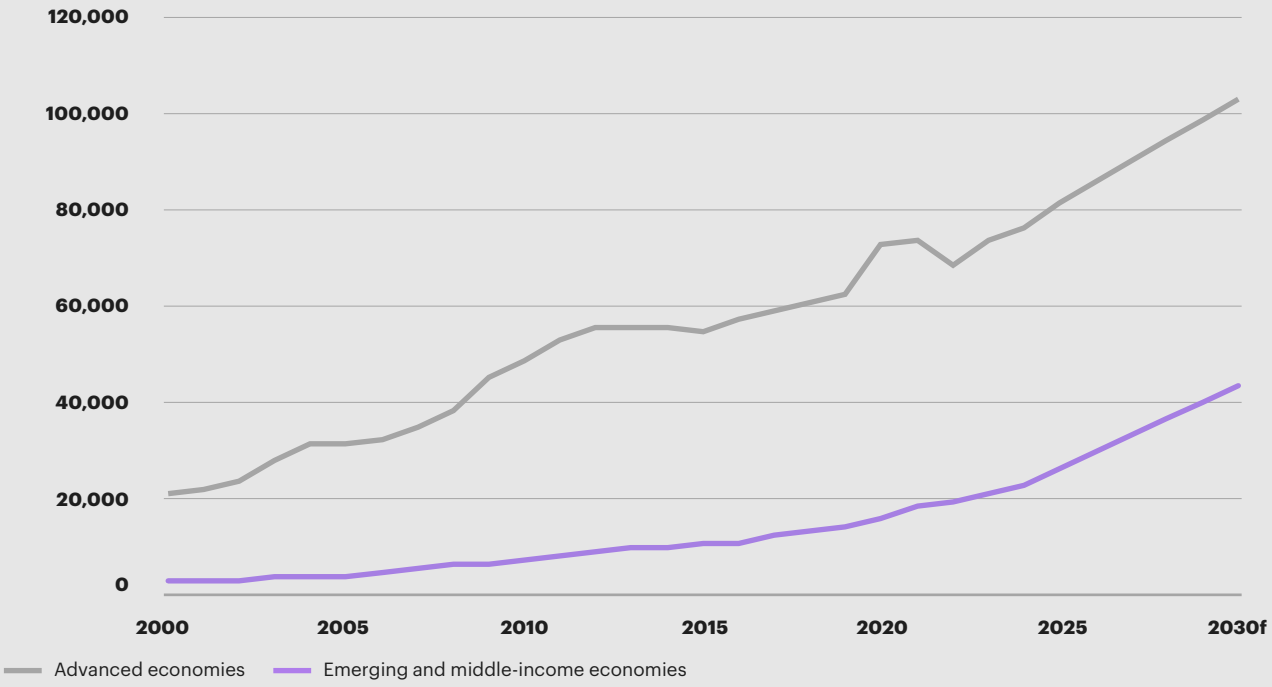
Countries with highest public debt, 2026f

(gross government debt, % of GDP)



Public debt is forecast to rise through 2030

(government debt, gross, LCU, $ billion)



Note: LCU is local currency unit.

Sources: International Monetary Fund, CNBC, Brookings, Euronews, Bloomberg, Reuters, World Bank International Debt Report 2024, Oxford Economics; Kearney analysis

What impact will the K-shaped economy have on markets?

Headline economic averages are obscuring the divergent realities shaping growth across regions, sectors, and income groups. The K-shaped economy describes an economic recovery where different geographies, sectors, and/or income groups experience highly divergent outcomes. The defining feature is the coexistence of growth and stagnation (or decline) across these segments, rather than a broad-based recovery. It differs from a V-shaped recovery, which is defined by a sharp and broad rebound, and a U-shaped recovery, which is characterized by a slower but widespread general growth path.

K-shaped divergence across regions

The K-shaped nature of global growth is clearly visible at the regional and country levels, with markedly different trajectories emerging across major economies (see figure 4 on page 10 and figure 5 on page 11). Asia and Australasia is anticipated to be the world's fastest-growing region through 2028, averaging 3.9 percent growth. One of the region's key growth engines is India, which is projected to grow at a striking 6.6 percent over the forecast period on the back of robust domestic demand and private consumption, tax reforms, and higher real household earnings in rural areas. Further, services exports in the country are resilient. China will achieve below-target growth of 4.4 percent over the forecast period and is experiencing its own K-shaped growth pattern. Supply-side factors such as robust industrial production (11.5 percent higher than 2023 levels) form the upper arm, while the lower arm is characterized by low domestic demand. Across Southeast Asia, economies such as Indonesia and the Philippines are adding to regional dynamism, with anticipated growth rates of 5.1 and 5.9 percent over the forecast period, respectively. Growth in Indonesia is expected to be attained by fiscal stimulus and state-led investment, and planned structural reforms in the Philippines aim to boost investment and productivity. The extent to which Asian economies are affected by Middle East conflict depends largely on their reliance on imported oil, the size of their strategic reserves, and their exposure to global energy markets and shipping routes.

Average growth projections for the Middle East and Africa fall just below those of Asia and Australasia, forecast at 3.6 percent between 2026 and 2028. The GCC states will fall on the lower arm of the K in the Middle East as the conflict surges, with an expected contraction of 0.2 percent in 2026. And growth prospects could be impacted by more than just straight energy price shocks. Indeed, around 10 percent of the region's activity is directly or indirectly related to travel and tourism, especially in places such as Dubai, where attacks on tourist destinations could cause inbound traveler losses of up to 27 percent this year.[4] Conversely, oil exporting African countries like Nigeria, Angola, and Ghana could benefit from conflict-induced oil price hikes in the form of higher export earnings, fiscal revenues, and foreign exchange reserves.

The Americas will see 2.4 percent average growth over the forecast period, but this headline figure masks a distinctly K-shaped regional pattern. On the upper arm, the United States is projected to grow at 2.5 percent between 2026 and 2028, the strongest performance in the G7. Although US growth slowed to 2.2 percent in 2025, with growth falling to just 0.7 percent in Q4, a modest rebound is expected in 2026, supported by AI-driven investment, resilient consumption among higher-income households, and strong capital inflows. While the United States is relatively insulated from energy oil price shocks given that it is a net energy producer, increased gas prices are likely to create drags on consumer spending, clouding the 2026 economic outlook. On the lower arm, parts of Latin America remain more exposed to commodity volatility, policy uncertainty, and geopolitical spillovers. Argentina is expected to fare relatively well, posting 2.4 percent average growth as US support helps stabilize financial conditions and the April 2025 shift to an exchange rate band improves flexibility. However, regional spillovers from US military operations in Venezuela are a wildcard, fueling uncertainty and the potential to reinforce divergence across the region over the next three years.

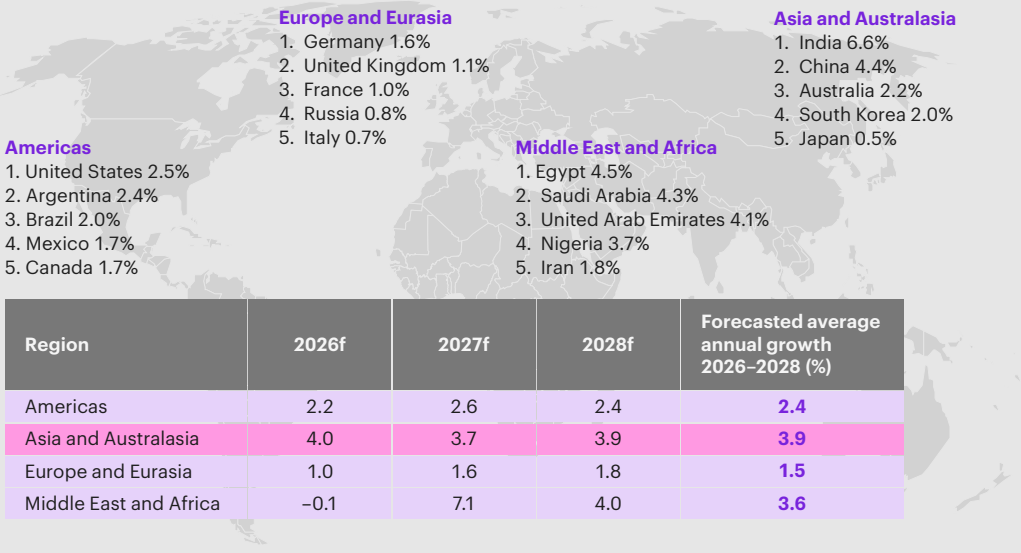
[4] *World Economic Prospects Monthly,* Oxford Economics, March 2026

Figure 4

Asia and Australasia is the world's fastest-growing region, led by India, the world's fastest-growing large economy

Regions driving economic output

(average annual GDP growth of largest regional economies)



Region	2026f	2027f	2028f	Forecasted average annual growth 2026–2028 (%)
Americas	2.2	2.6	2.4	**2.4**
Asia and Australasia	4.0	3.7	3.9	**3.9**
Europe and Eurasia	1.0	1.6	1.8	**1.5**
Middle East and Africa	–0.1	7.1	4.0	**3.6**

Note: Countries are ranked in order of fastest average forecasted growth for 2026–2028.

Sources: Oxford Economics; Kearney analysis

Despite being one of the world's largest economic blocs, Europe and Eurasia has the weakest regional growth prospects, with anticipated average growth of just 1.5 percent through 2028. Tariff hangovers add to the region's sluggish growth, along with geopolitical instability in the region and beyond. And Europe is slated to be hit especially hard by the Middle East conflict, given its dependence on LNG. Europe's productivity and competitiveness challenges are mounting on the back of stringent regulations and high debt levels are weighing on the lower arm of the K, particularly among countries and sectors with limited exposure to technology-led investment. Between 2010 and 2019, labor productivity in Europe grew by just 0.7 percent and subsequently fell by 0.7 percent in 2023. This is substantially lower than a 2.0 percent long-run average in the United States, for example.

Continued increases in defense spending could help to mitigate downside risks in Europe, however. For instance, Germany plans to hike defense spending to almost 3.5 percent of GDP by 2029, up from 2.1 percent in 2024. This spending could boost the 2029 level of German GDP by around 0.8 percent according to Goldman Sachs. Indeed, this fiscal stimulus in Germany is improving its growth prospects through 2028, with average growth of 1.6 percent. The United Kingdom and France, in contrast, face comparatively lower growth prospects of 1.1 and 1.0 percent, respectively. Europe's outlook is increasingly defined by K-shaped divergence between countries and sectors able to mobilize fiscal and strategic investment and those constrained by productivity stagnation and policy rigidity.

Figure 5

Growth patterns are diverging amid the broader growth slowdown

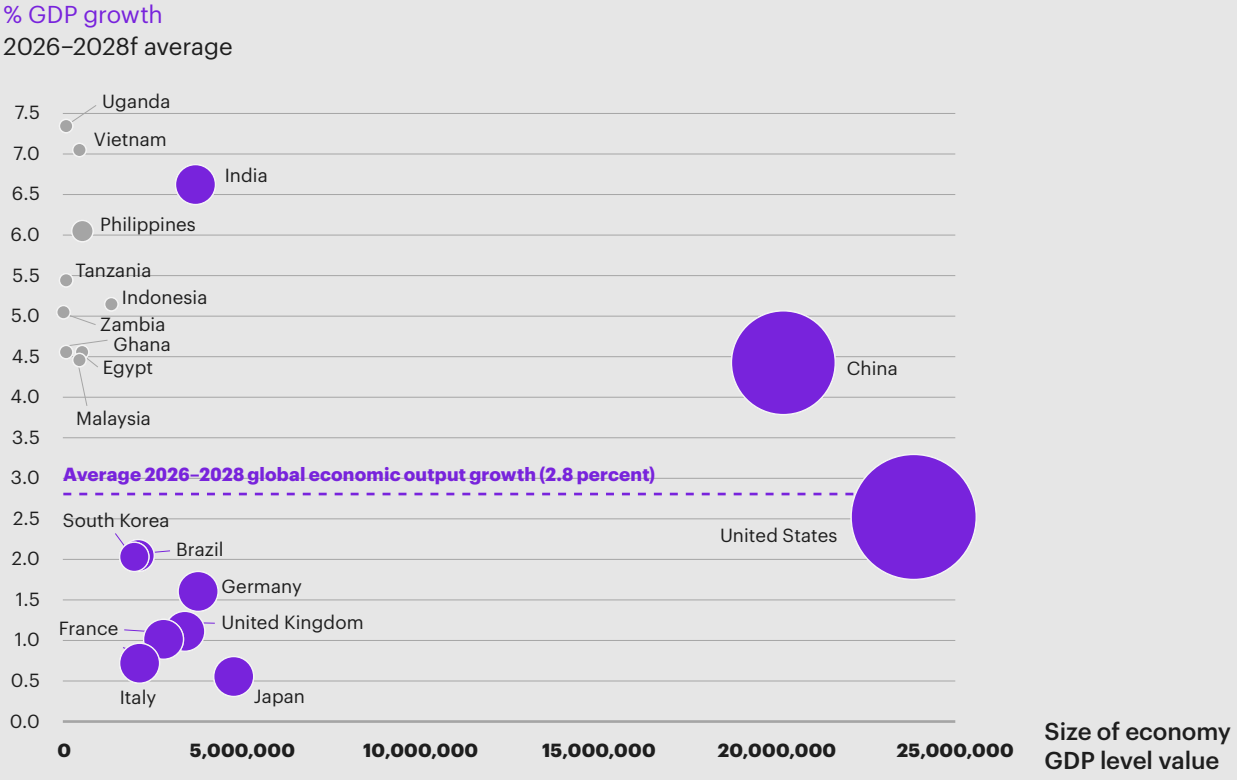
K-shaped growth trajectories shape the outlook within and between countries, as major economies face markedly different trajectories.

Top 10 economies by size

	GDP value (2026f)	GDP % growth 2026–2028f
United States	23,775,120.0	2.5
China	20,131,730.0	4.4
Japan	4,771,631.0	0.5
Germany	3,702,735.0	1.6
India	3,656,799.0	6.6
United Kingdom	3,377,250.0	1.1
France	2,767,362.0	1.0
Brazil	2,105,436.0	2.0
Italy	2,050,700.0	0.7
South Korea	1,971,464.0	2.0

10 fastest growing economies

	GDP value (2026f)	GDP % growth 2026-2028f
Uganda	51,052.0	7.3
Vietnam	464,503.8	7.0
India	3,656,799.0	6.6
Philippines	498,034.6	6.0
Tanzania	88,572.7	5.4
Indonesia	1,368,908.0	5.1
Zambia	31,378.9	5.0
Ghana	82,677.1	4.5
Egypt	564,220.9	4.5
Malaysia	464,930.5	4.4



Note: GDP is in constant prices and exchange rate, $ million: 2015 prices. GDP value is level, millions, 2025 prices, based on 2025 values. GDP growth by % change, average.

Sources: Oxford Economics; Kearney analysis

Which sectors will win and lose in a K-shaped economy?

The K-shaped economy is also impacting business and brands as technological innovation reaches new heights and spending patterns evolve. Oxford Economics industry data suggests that certain sectors are benefitting globally from economic asymmetries, while others are losing ground.[5] For example, the high-tech goods and information and communications services sectors are expected to see 9.9 percent and 5.2 percent growth, respectively, in 2026 (see figure 6 on page 13). This is in no small part on the back of massive AI-related spending on a global scale, estimated to surpass $500 billion this year. However, motor vehicles and parts are anticipated to post 1.1 percent growth as trade protectionism, slowing EV sales, and weak consumer confidence create headwinds.

Over the next three years and beyond, the tech sector will continue to be at the top of the K as AI investment expands. Wealthy consumers are projected to concentrate their spending among the luxury goods and services, financial services, and healthcare innovation industries. These industries are poised to benefit directly and indirectly from the AI boom. However, there is some nuance here. The top arm of the "K" is most exposed to a potential stock market correction. In the United States, for example, around 30 percent of the net worth of American households is tied up in stock ownership. This is concentrated among those in the upper income brackets, whose spending is powering of growth. Conversely, the bottom of the K is less exposed to stock market fluctuations, barring retirement account movements, and could be comparatively more sheltered.

Traditional industries targeting lower-income consumers could face challenges. These include established retail, hospitality services, and manufacturing sub-industries that are impacted by automation and at higher risk of job displacement. And even traditionally higher-earning consumers, like software engineers, could see generative AI-related job losses. Sector performance is thus increasingly determined by technology exposure and customer income profiles rather than geography alone.

K-shaped impacts on inflation and consumption

These K-shaped growth dynamics are translating directly into uneven inflation and consumption outcomes. The Federal Reserve Bank of Cleveland has found that since the onset of COVID-19, especially after inflation peaked in June 2022, US households in the bottom 40 percent of the income distribution experienced consistently higher inflation than headline CPI, with the gap persisting through mid-2024 at roughly 0.25 to 0.50 percentage points. In contrast, households in the top 20 percent generally faced lower inflation than average, with a negative gap of 0.25 percentage points early in the post-pandemic period that narrowed as inflation cooled in 2023–2024.

This data reveals that headline inflation masks meaningful distributional differences and asymmetries. Indeed, lower income households tend to spend a larger share of their budgets on goods and services, such as food and housing, whose prices rose faster than average during and after the post-pandemic inflation peak. This reflects the degree to which inflation shocks are not experienced equally, with important implications for real purchasing power, inequality, and how monetary and fiscal policy outcomes should be judged.

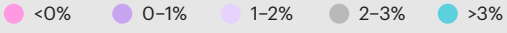
These dynamics are affecting consumption patterns as well. US consumer spending has become increasingly concentrated at the top during the pandemic recovery, with the Dallas Federal Reserve estimating that the highest-earning 20 percent accounted for 57 percent of total spending between 2020 and mid-2025, up from 53 percent in the 1990s. This increase is driven by gains in asset prices that disproportionately benefit wealthier households. In contrast, middle-income spending has stagnated since 2023, while lower-income consumers face striking rises in credit-card debt.

[5] *Global Sector Outlook: Global Industry Forecasts,* Oxford Economics, December 2025

Figure 6
Sector heat map

Global industry performance projections
(production, value-added output, real $, % change year over year)

Key sector	% of GDP (2024)	2024	2025	2026f	2027f	2028f
GDP	**100.0**	2.9	2.9	2.6	3.1	3.0
Agriculture	**4.1**	2.9	3.0	2.4	1.9	2.2
Extraction	**2.3**	0.2	1.7	-0.4	3.9	0.4
Manufacturing	**17.6**	2.8	4.1	2.9	3.4	3.4
Food and beverages	2.2	3.3	2.4	2.6	3.1	3.3
Industry and building materials	0.0	1.0	0.8	-0.2	2.9	2.6
Chemicals	1.5	4.5	3.3	1.0	3.0	3.6
Pharmaceuticals	0.9	5.2	10.3	2.1	3.3	3.9
Basic metals	1.2	4.2	5.1	2.3	3.3	3.0
High-tech goods	1.9	8.3	10.0	9.9	7.5	6.3
Engineering and metal goods	3.4	0.3	3.6	3.7	3.6	3.5
Motor vehicles and parts	1.2	-0.3	2.9	1.1	0.3	1.5
Aerospace	0.3	5.2	10.4	4.5	3.3	4.1
Utilities	**2.2**	3.7	0.8	3.0	3.7	3.3
Construction	**5.2**	2.2	1.4	2.0	3.6	3.0
Services	**68.6**	3.0	3.0	2.5	3.0	2.9
Retail and wholesale distribution	11.5	3.6	2.4	2.4	2.9	3.0
Transport and storage	4.5	3.9	3.3	2.4	3.7	3.6
Accommodation and catering	2.3	2.8	1.6	2.9	3.1	3.4
Information and communication services	6.2	5.5	7.0	5.2	4.8	4
Financial services	6.3	2.6	3.9	3.5	3.5	3.3
Business services	19.7	2.0	2.5	2.3	2.7	2.6
Government and community services	18.1	2.7	2.4	1.6	2.4	2.2



Sources: Oxford Economics; Kearney analysis

These developments are also evident globally. A pan-European Sapienza University of Rome study shows that lower-income households devote a much larger share of income to basic goods, especially food. Across the five countries studied—Spain, France, Italy, Poland, and Sweden—the share of income spent on food declines steeply with income, reaching over 40 percent for the bottom quintile in Poland versus below 30 percent in Sweden, making poorer households structurally more exposed to price shocks. And in China, consumption is showing an urban/rural divide, with housing demand and related consumption rebounding mainly in tier 1 cities, while lower-tier and more rural-linked cities remain weak. For example, housing inventory in tier 3 cities requires a destocking period of 34 months, a striking 14 months longer than in tier 1 cities and 20 months above the 2017–2020 average. Together, these trends underscore how the K-shaped economy is reinforcing inequality and reshaping inflation and consumption dynamics across advanced and emerging markets alike.

Finally, the conflict in the Middle East could have outsized economic impact on the K-shaped economy and consumption patterns. Energy shocks do not hit all households equally. Lower- and middle-income consumers allocate a larger share of their budgets to gasoline, utilities, and transportation, so higher energy prices compress their real disposable income more quickly. In contrast, higher-income households are less exposed to energy costs as a share of spending but far more sensitive to asset prices. Deutsche Bank projects that each 1-cent increase in gasoline prices costs consumers between $1.0–$1.4 billion, disproportionately impacting lower-income households first. However, if the shock also triggers a persistent 10 -15 percent decline in equity markets, the wealth effect can meaningfully reduce discretionary spending among higher-income consumers, particularly on big-ticket items such as vehicles, furniture, and electronics.[6]

To what extent will governments continue to intervene in economic decisions?

As fiscal space narrows and geopolitical competition intensifies, governments are intervening more directly in economic decision-making under the banner of economic security. What began as targeted efforts by G7 members, including Canada, France, Germany, Italy, the United Kingdom, and the United States, to counter China's unfair trade practices broadened during the COVID-19 pandemic. More than 75 countries, from EU countries to India, imposed export restrictions on critical pharmaceutical products, fueling a spike in subsidies. Russia's invasion of Ukraine then triggered a rise in investment and export restrictions. More recently, rapid advancements in new technologies compelled an expansion of export and investment controls on the materials underpinning these technologies as major powers, notably the United States and China, looked to protect their strategic competitiveness. With few guardrails on these measures, governments are likely to continue intervening in economic decisions, citing economic security and the need to protect strategic industries.

Governments are likely to continue intervening in economic decisions under the banner of economic security.

[6] *Oxford Economics. The Economic Impact of Conflict in the Middle East*. Webinar, March 2, 2026

This expansion of economic security agendas is a key factor in the proliferation of industrial policy measures. According to Global Trade Alert, the number of new industrial policy interventions rose by 262 percent in 2025 relative to 2019, with 5,033 measures introduced in 2025 alone (see figure 7). These interventions reflect a shift from market-correcting policies toward more interventionist approaches, spanning tariffs, export controls, and taxes, alongside financial grants, state loans, and localization requirements. Recent data show that industrial subsidies and other state-backed support measures have surged to record levels globally, with more governments using fiscal incentives and state aid to attract strategic industries such as semiconductors, clean energy, and critical minerals.

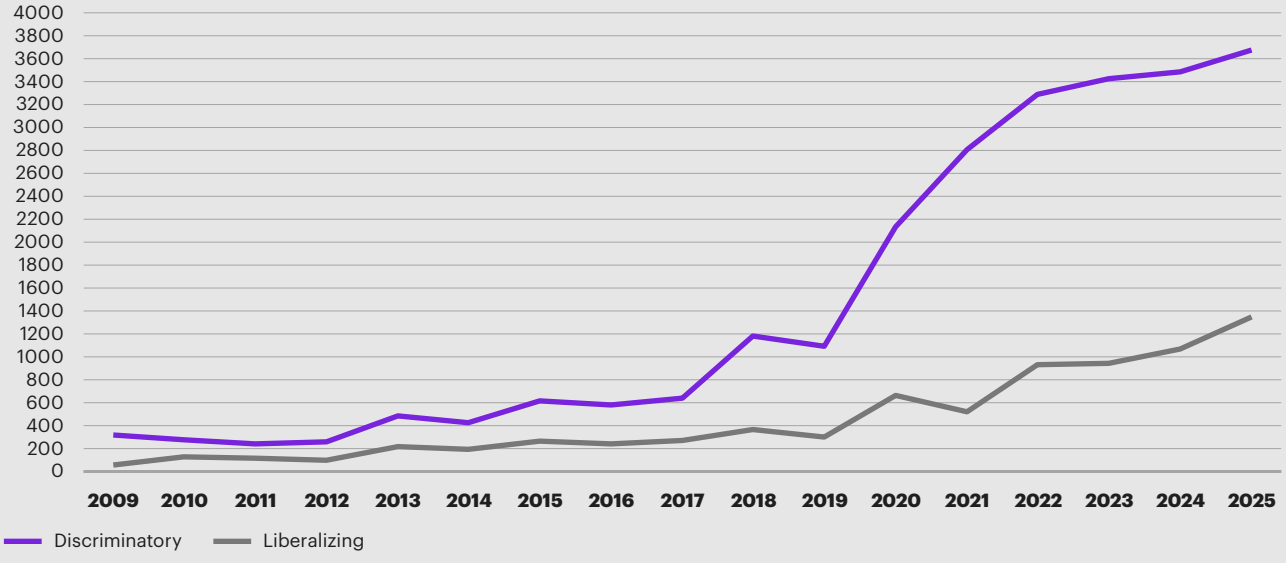
The surge in industrial policy stems from new priorities in government strategies. The United States has aggressively applied tariffs to fortify domestic industry; Europe is increasingly deploying industrial policy as part of the region's push for higher competitiveness; and China's Made in China 2.0 strategy focuses on building a technology forward industrial base, a natural extension of earlier Made in China industrial policy efforts started in 2015.

The post-COVID boom in industrial policy has been characterized by a heavy reliance on discriminatory policy measures rather than liberalizing policy measures. The former tend to discriminate against imports or foreign firms and stand to worsen treatment of foreign commercial interests. In contrast, liberalizing measures increase openness and reduce barriers to international commerce. In 2025, 73 percent of the new industrial policy interventions governments deployed were discriminatory, reflecting a more defensive government stance.

Data from the New Industrial Policy Observatory highlights the growing security rationale behind these actions. In 2024 and 2025, Western governments cited national security and geopolitical concerns as the driver of 39 percent of industrial policy actions, a striking 36 percentage point increase from 2009–2016 (see figure 8 on page 16). The rest of the world cited national security and geopolitical concerns as the driver behind 25 percent of industrial policy actions, while 54 percent of actions were motivated by strategic competitiveness. Together, these trends suggest that economic security considerations are becoming a durable feature of the policy landscape rather than a temporary response to crisis.

Figure 7
Industrial policies continue to proliferate globally

Number of new interventions related to industrial policy
(world)



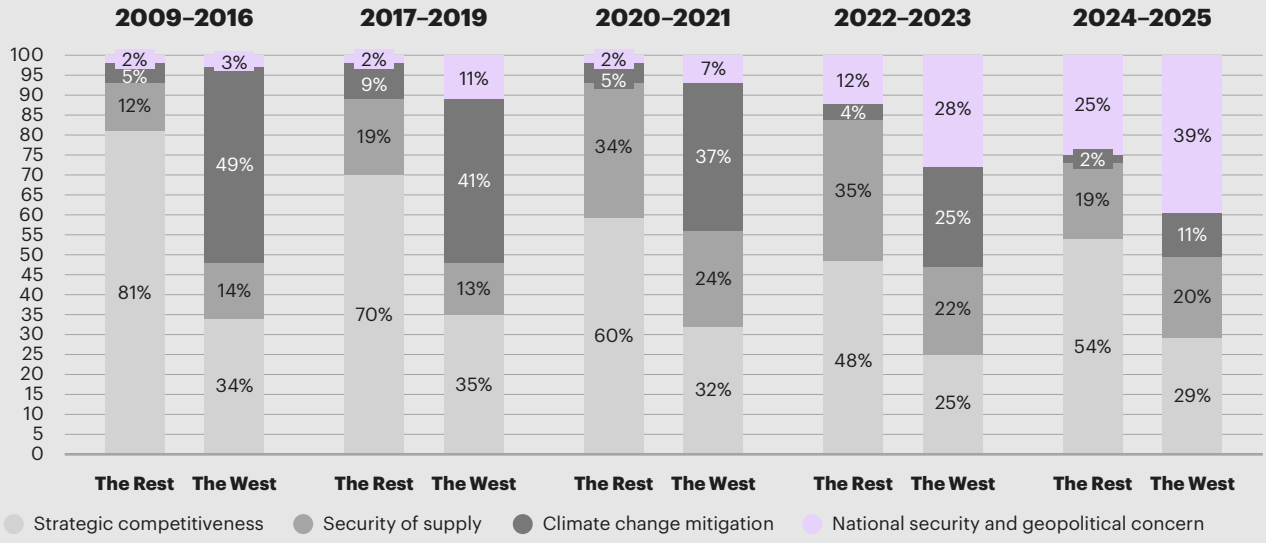
Sources: Global Trade Alert; Kearney analysis

Figure 8

The motives underpinning industrial policies are shifting, with greater emphasis on national security

Stated motives for industrial actions

(percentage of actions by group and year)



Note: West refers to Australia, EU-27, the G7, and South Korea.

Sources: NIPO by Global Trade Alert; Kearney analysis

Trade barriers, tariffs, and fragmentation risk

Trade barriers and tariffs are increasingly functioning as instruments of geopolitical strategy rather than tools of economic adjustment, with implications that extend well beyond trade flows. Governments are leveraging tariffs not only to protect domestic production, but also as a bargaining chip in wider geopolitical and commercial negotiations under the umbrella of economic security. This can trigger retaliatory measures, defensive policies from partners, and the formation of new trade alliances. However, the economic effects of US tariffs measures have been more muted than initially projected, at least in the short-term. The Peterson Institute notes that, surprisingly, there was very little reconfiguration of global trade following the Trump administration's trade tariffs by the end of 2025, with the share of total trade among 19 impacted foreign partners changing only marginally. This was owing to a combination of factors, including moves by companies to front-load exports before the tariffs came into effect and a reluctance of many trading partners to retaliate against the United States.

Over the medium to longer term, however, the effects of trade barriers are likely to become more pronounced. The World Trade Organization now forecasts that growth in global trade in goods will slow to 0.5 percent this year, down from previous projections of 1.8 percent. By late 2025, projections already showed that US two-way trade with 19 trade partners grew slower than world trade in 2025, and *The Wall Street Journal* reported that EU goods exports to the United States were 20 percent lower in November than a year earlier. Research from the IMF finds that tariff shocks and trade-policy uncertainty have persistent negative effects on trade, investment, and output, magnifying the long-term economic cost of using tariffs as policy instruments. Further, the cost of more widespread fragmentation and international trade restrictions could reduce global economic output by as much as 7 percent over the long term.

Tariffs are also contributing to higher prices. Core goods prices were 1.9 percent above pre-2025 trends as of June 2025, and an estimated 61 to 80 percent of new 2025 tariffs were passed through to consumer core goods prices. At the same time, tariffs have delivered selective gains, with industrial output in tariff-sensitive US industries rising by 3.5 percent, returning to early-2024 levels, according to Yale's Budget Lab. These mixed outcomes underscore the trade-offs inherent in using tariffs as a policy instrument.

Policy risk as a structural feature of the global economy

Beyond their direct economic effects, protectionist policies are weakening multilateral institutions and norms. As unilateral measures proliferate, multilateral coordination struggles to keep pace, elevating the risk of sustained fragmentation. Early evidence of this erosion is visible in foreign direct investment trends. Trade volatility in early 2025 resulted in an 11 percent decline in FDI in the first half of the year compared with a year prior, although inflows rebounded as trade conditions stabilized later in the year.

Taken together, rising industrial policy, expanding trade barriers, and elevated fiscal constraints are embedding policy risk more deeply into the global economic environment. For businesses and investors, policy uncertainty is now a structural feature, influencing decisions around capital allocation, supply chains, and market entry. This shift marks a transition from a rules-based global system toward a more fragmented and discretionary policy regime, with lasting implications for growth and investment.

Policy uncertainty is influencing decisions around capital allocation, supply chains, and market entry.

How leading multinationals are redesigning footprints, supply chains, and risk

As governments intervene more actively and policy risk becomes a structural feature of the global economy, multinational firms are redesigning their strategies to preserve flexibility, access, and resilience. As increased protectionism and competing economic security measures amplify geopolitical tensions, multinational firms are walking a tightrope between needing to maintain relationships and access to competing global superpowers and managing exposure. More countries and companies are pursuing "polyalignment" among competing global powers. Firms are challenged to strike a balance between conflicting sides of geoeconomic and geopolitical competition, as projects intersect financial, infrastructural, or manufacturing investments from different geopolitical blocs.

This dynamic is clear in critical mineral markets. Argentina's lithium-rich Jujuy province, has engaged both the United States and China rather than align with any one superpower as concerns around the securitization of lithium and green extractives concerns mount. Similarly, despite evidence of decoupling between Washington and Beijing, exemplified by falling shares of trade between the two countries, many US companies are reluctant to sever ties with China. In a 2025 Chamber of Commerce Foundation survey of 200 American companies, 70 percent planned to maintain or expand ties with China, even as 83 percent identifying China as the top geography of concern.

Rather than retreating from globalization, many firms are building geostrategic logic into company strategies. Firms are positioning themselves as secure partners, cultivating relationships across superpowers to access industrial policy benefits, such as subsidies and market access, while hedging geopolitical exposure.

Tariffs, in particular, are forcing firms to rethink how they manage government interventions. "Connector countries," such as Poland, Hungary, Vietnam, Indonesia, Malaysia, and Mexico, are positioning themselves as intermediary hubs to bypass tariffs and sanctions. Companies are leveraging these connector economies as alternative entryways to avoid burdensome tariffs. Retaliatory tariffs are driving similar adjustments: Apple plans to send more iPhones to the United States from India, expanding production in India at five factories, to offset the high cost of Chinese tariffs. In tandem, the company is maintaining long-term relationships in its China-centric supply chain. Amid tariff spikes in April 2025, Taiwanese semiconductor firm TSMC announced its intent to expand investment in the United States to $165 billion to "power the future of AI," increasing investment in the region to add three new fabs, two advanced backing facilities, and a new R&D center.

Domestically, tariff actions create both winners and losers in manufacturing. Though manufacturers remain downbeat in surveys, production is slightly up. In the United States, firms such as Marlin Steel Wire Products, saw a more protected industrial environment as an opportunity to invest in expensive equipment to boost production, but others, such as DRR USA, which makes electric and gas-powered all-terrain vehicles and bought most of its batteries and other parts from Taiwan, struggle with volatility and heightened costs. Globally, US tariffs on India had a negative impact on stock prices of major pharmaceutical companies, such as Sun Pharma, Cipla, and Dr. Reddy's, which saw declines of up to 5 percent, and concerns that tariffs could negatively impact a further 30 to 47 percent of US-derived revenues. Conversely, liberalizing trade efforts in other countries, such as the UK–India free trade agreement and recent EU–India free trade agreement, are showing early signs of economic tailwinds. For example, the UK–India free trade agreement, signed in May 2025, is projected to increase trade by 2040 annually by an estimated $35 billion.

Despite the turbulent economic operating environment, the private sector has shown notable resilience in the face of trade uncertainty and aggressive government action. The IMF attributes this resilience in part to the private sector's ability to mitigate trade disruptions by frontloading, stock building and supply chain strengthening, and leveraging profits to squeeze margins to avoid raising consumer prices. Taken together, these firm-level adaptations illustrate how resilience, flexibility, and strategic optionality are becoming core sources of competitive advantage in a fragmented global economy.

Conclusion and implications for business

Relatively stable growth and surprisingly resilient firm performance are masking turmoil beneath the surface. Beneath the headline figures, deepening geopolitical divisions and expanding regional conflict, prolonged policy uncertainty, increased government interventions, rapid technological disruption, mounting debt, and widening K-shaped asymmetries continue to shape a far more complex operating environment.

By adapting to evolving trade conditions, preparing for sustained volatility, and embracing technological advances, particularly through investments in AI, firms have helped cushion shocks and smooth growth trajectories. This resilience has not been accidental. Strategic firms are already refining supply chain planning to reduce the impact of external volatility in eroding margins, deploying tactics such as frontloading, stock building inventory, and factory location diversification.

Building resilience now requires nuance, with strategies that consider asymmetries and are informed by geopolitical realities. Decisions such as how to limit tariff exposure and maximize the benefits of government interventions or how to reduce margins to avoid trade volatility cutting too deeply into consumer spending demand coordinated, cross-functional planning, informed by geopolitical and regulatory context.

Firms will also need to design for divergence, recognizing that regions, countries, and groups within countries are following disparate trajectories, experiencing growth unevenly. This will require differentiated strategies for different groups. Instead of assuming a one-market-fits-all approach, strategic firms will explore options from tailored pricing and product offerings to market-specific investment and sourcing decisions. Firms that align strategy with these uneven growth paths will be better positioned to sustain performance across cycles.

Technology is a critical enabler in these decisions. Firms that have successfully navigated recent volatility have invested in advanced supply chain tracking and analytics to tailor to this new nuance, linking point-of-sale data, inventory management, and production planning in real time. When deployed effectively, AI can boost productivity, improve risk anticipation, and ensure that large-scale technology investments translate into tangible economic gains.

In a world defined by growing geopolitical risk, persistent uncertainty, and lingering volatility, resilience is no longer just defensive. It is a source of competitive advantage. Firms that adapt fastest, plan strategically, and invest well will not only withstand volatility, but transform uncertainty into opportunity in an age of divergence.

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