

Global Macro Insights

Summary

January overview: There was some modest positive news on growth across a number of economies, though there are still areas of concern. Most central banks left interest rates on hold in January, amid signs that the global easing cycle is nearing its end. Inflation is diverging somewhat among developed economies but remains fairly contained among a variety of emerging markets (EM). The US dollar (USD) was weaker again in January, depreciating against a range of currencies. Developed market bond yields were generally modestly higher during the month, although a relatively sharp rise was seen in Japan, while some euro area (EA) yields fell. Yields were mostly higher in emerging Asia but generally lower among other EM. US President Donald Trump nominated Kevin Warsh as the next chair of the US Federal Reserve (Fed). Geopolitics remained a source of uncertainty: US troops captured President Nicolás Maduro and his wife in Venezuela and brought him back to the United States to stand trial, the Trump administration vocalized its desire to bring Greenland under US control, and in the Middle East, protests in Iran were notable.

Outlook: Uncertainty remains a pervasive issue globally. Whereas it had seemed like some tariff-related uncertainty was lessening with the conclusion of various trade agreements, more recent events have thrown some of these into doubt. In addition to trade policy, geopolitical events have resurfaced as a source of potential instability. A number of sources of potential economic policy concern in major economies have also surfaced. Financial markets also still await the Supreme Court ruling on the legality of tariffs imposed by the president rather than Congress; the ruling may take some months yet. While uncertainty remains on a number of fronts, in general we see global growth as being quite resilient. The global monetary policy easing cycle is in its late stages and pauses or increases in rates seem the most likely outcome across a range of countries. Our core themes of improving EM fundamentals, USD weakening and global rewiring (such as geopolitically induced shifts in global supply chains) remain intact. Although data has been fairly resilient to date, risks remain from US tariff and trade policy. In addition to this, domestic political developments are of potential concern in some countries, particularly with respect to fiscal policy outcomes, while elections are also due in a number of countries this year, including a snap election called in Japan during January for February.

General market and economic overview

In the **United States**, third quarter (Q3) 2025 gross domestic product (GDP) growth was revised slightly higher to 4.4% quarter-over-quarter (q/q) seasonally adjusted and annualized, from a prior estimate of 4.3% q/q. Various manufacturing indicators were more positive during the month, and the University of Michigan Consumer Confidence Index rose. However, the Conference Board's Consumer Confidence Index (measured later in the month) fell to an 11-year low. Jobs grew but were below expectations, and revisions sizably reduced the prior reported jobs growth data. On the policy front, Trump nominated Kevin Warsh to be the next Fed chair. Warsh, who served on the Fed's Board of Governors from 2006 to 2011, would succeed Jerome Powell when his term ends in May.

EA fourth quarter (Q4) 2025 GDP growth increased 0.3% q/q (1.3% year-over-year [y/y]) compared to 0.3% q/q (1.4% y/y) in Q3, bringing full-year growth for 2025 to 1.5% y/y. Spain was notable here, growing 0.8% q/q and 2.6% y/y in Q4. Consumer confidence remains soft but has shown signs of improvement. While purchasing managers index data was somewhat mixed, German industrial and manufacturing production data notably increased well above expectations in November. Bulgaria became the 21st member of the EA, introducing the euro on January 1, 2026.

In **Japan**, Prime Minister Sanae Takaichi called a snap election for February, and stated her intention to increase fiscal accommodation. Japanese bond yields—which have already risen significantly over the past year—reacted sharply to concerns over fiscal outcomes in the wake of the announcement.

Q4 growth in **South Korea** declined by 0.3% q/q, though we believe this largely reflects payback after a surge in the prior quarter rather than underlying weakness. Early January data indicate continued strong export growth, particularly in semiconductors.

Geopolitical developments and trade deals continued to capture headlines in January.

- In early January, US troops captured President Nicolás Maduro and his wife in Venezuela and brought him back to the United States to stand trial. Vice President Delcy Rodríguez has now been sworn in as president. Protests in Iran, which continued from December into January, put some pressure on oil prices; the situation seems to have abated more recently, but bears monitoring.
- Geopolitical considerations continue to be significant in the trade agreement sphere. The US administration's stance over Greenland (and threats about increased tariffs over the issue) have resulted in the European Union (EU) pausing the ratification of its trade agreement with the United States. The free-trade agreement agreed between the EU and India is expected to increase EU exports to India and for both parties to cut or eliminate tariffs on a majority of shipments. The trade agreement between the EU and Mercosur (a South American trade bloc whose full members include Argentina, Bolivia, Brazil, Paraguay and Uruguay) was approved by EU members during January. While the EU Parliament has voted to delay ratification for legal review, the agreement may be implemented on a provisional basis. China and Canada reached an agreement to slash tariffs on electric vehicles and canola. Just after month-end, the United States and India announced an agreement to cut tariffs significantly, partly linked to India agreeing to buy more goods from the United States and to cease buying oil from Russia.
- South Korean President Lee Jae Myung visited China for the first time, with the ultimate aim of a full normalization of South Korea-China relations. A package of cooperation documents, across areas such as industry, environment and intellectual property, was adopted. President Lee also visited Japan to meet Prime Minister Takaichi, with a broadly constructive tone conveyed. Meanwhile, amid heightened diplomatic tensions between China and Japan, China announced a number of export restrictions on Japan.
- The “Board of Peace” proposed by Trump was officially established during January. Around 25 countries, mostly among EM so far, have accepted invitations to join the organization.

Global inflation outcomes continue to diverge somewhat. US December consumer price index (CPI) inflation was unchanged from 2.7% y/y in November, and core CPI was also unchanged at 2.6% y/y. In the EA, December inflation dipped to 1.9% y/y in December, from 2.1% y/y in November. Inflation in Japan slowed significantly to 2.1% y/y in December from 2.9% y/y in November, but this was largely attributed to base effects from a spike in food prices a year prior as well as cuts to energy subsidies. “Core-core” inflation, which excludes fresh food and energy, eased marginally to 2.9% in December from 3.0% prior. The Bank of Japan (BoJ)'s quarterly regional assessment revealed that strong wage-hike momentum is set to continue with firms passing on higher input costs to output prices, and some noting that Japanese yen (JPY) weakness is also increasing costs. Some other developed economies have seen continued inflationary pressures, notably Australia, and most developed markets remain above their inflation target ranges. By contrast, a significant number of EMs have inflation within their target ranges and a few have inflation below their target at present. On the whole, inflation appears well-contained among EMs.

Most central banks that held policy meetings in January left policy rates unchanged; developments during the month generally supported the notion that the global easing cycle is close to an end. In the United States, the Fed left the federal funds rate target range unchanged at 3.50%–3.75%, following three consecutive 25-basis-point (bp) cuts. There were two dissents to this vote that preferred another 25 bp reduction. The European Central Bank (ECB) did not hold a January policy meeting. Norway left rates unchanged in January. The BoJ kept its policy rate unchanged at 0.75% (after an interest-rate hike in December), even as it revised inflation projections higher. Most EMs left rates unchanged in January but there were some noteworthy signals, particularly in Latin America. Although Brazil left rates unchanged, it indicated that the next move would be a cut—this is in the context of Brazil having raised rates against the global trend a few times last year. Colombia raised its policy rate by 100 bps, above consensus expectations of a 50-bp hike, to address inflation pressures and rising inflation expectations. Elsewhere in EM, central banks in South Korea, Malaysia, China, Poland and South Africa left rates unchanged. In South Korea, the central bank removed prior forward guidance suggesting a future possible rate cut.

The USD was somewhat weaker on average again during January; the US Dollar Index (DXY) index fell by 1.4% over the month.¹ Developed market currencies generally gained against the greenback, including the JPY, euro, Norwegian krone and Australian dollar. A renewed bout of JPY weakness earlier in the month was reversed on speculation that the BoJ might intervene in the market following comments from Japanese officials. Among EMs, Latin American, eastern European and African currencies were mostly stronger against the USD, while Asian currencies showed mixed performance.

Sovereign bond yields were mixed during the month with an upward bias among developed markets, but most movements were relatively modest. Japanese bond yields however rose significantly again following fiscal concerns around the election announcement, and the Japanese 10-year bond yield rose 19 bps to 2.24% over January—its highest monthly close since 1997. The yield on the 10-year US Treasury note rose seven bps to 4.24% over January. The EA benchmark German Bund yield edged down by one bp, with movements mixed among other EA countries. Among EMs, yields mostly declined in Latin America, Africa and eastern Europe but were generally higher in Asia. **EM sovereign credit overall gained modestly over January**, with the total return on the J.P. Morgan EMBI Global Index (JPM EMBIG) rising 0.6%.²

Outlook and positioning

Policy uncertainty remains relatively high on a number of fronts, even as some tariff-related uncertainty is decreasing as deals are made. The Supreme Court ruling on tariffs will be an important factor to watch; at present it is unclear when the decision might be expected. In the United States, higher uncertainty surrounds monetary policy—stemming both from a divergence of views within the Fed as mentioned earlier and the prospect of a new Fed chairman. Geopolitically, the recent events in Venezuela have raised some concerns about possible further unilateral actions around the globe. A number of countries will also hold general and/or presidential elections this year, including Japan's snap election, the second round of Portugal's presidential elections in February, and Thailand, Hungary, Colombia, Brazil, New Zealand and the mid-term United States elections later this year.

Global growth continues to look relatively resilient, if unexciting. The International Monetary Fund (IMF) released its January World Economic Outlook update, revising its global growth projections slightly higher to 3.3% in 2026 and 3.2% in 2027. The outlook noted that surging investment related to technology—including artificial intelligence (particularly in North America and Asia), fiscal and monetary support, broadly accommodative financial conditions and adaptability of the private sector—are helping to offset headwinds from shifting trade policies. The IMF noted a "reevaluation of technology expectations" (which would affect both the stock market and technology investment) and escalation of geopolitical tensions as growth risks. As has been the case for some time, the IMF expects EMs to grow faster than advanced economies. Within emerging and developing economies, emerging Asia is projected to grow fastest, with India particularly notable at 6.4% both this year and 2027; sub-Saharan Africa is also forecast to have robust growth rates.

Global inflation is likely to decline over 2026, in our view, but progress may be uneven across countries. In developed markets, the prior disinflation trend remains largely stalled, and some countries have seen unwelcome recent increases in inflation. Australia, New Zealand, Norway and the United Kingdom all currently have inflation rates above 3% (and above their inflation targets). There is mixed evidence of tariff effects so far, but we expect that where companies have absorbed costs to date they cannot do so indefinitely; tariff effects thus remain an inflation-risk factor. In the United States, we expect near-term pressures from tariffs but anticipate inflation should be trending back toward the target in the second half of 2026. In addition, we think the US fiscal situation may complicate the medium-term inflation outlook in the United States. By and large, major EMs have inflation within their target ranges.

The global monetary policy easing cycle seems close to its end. Inflation outcomes complicate the outlook for meaningful further easing in developed markets. We expect some further policy rate reduction from the Fed this year but, absent any meaningful downward surprise in EA growth, we think the ECB has reached the end of its rate-cut cycle. We believe that chances have tilted toward Australia raising rates this year. We continue to expect the BoJ to continue gradually normalizing. A significant number of EMs appear to be near or at the end of their rate reductions, other than Brazil where potential rate cuts come in context of a period of interest-rate increases last year counter to the general trend.

We continue to highlight the concerning fiscal outlook in a number of countries. Already-high debt levels in major economies are set to rise further, while some political developments also complicate efforts to consolidate fiscal expenditures. The IMF estimates G7 gross government debt at 126% of GDP in 2025 and projects an increase to 137% by 2030. In our view, such fiscal burdens raise risks for longer-dated maturities in the bond market. EM fiscal positions have also deteriorated since the pandemic. The IMF estimates average EM gross government debt-to-GDP at just under 74% in 2025 and projects it to rise further to around 84% by 2030, compared to 55% in 2019.

We remain constructive on select EMs, despite risks from tariffs. We believe sounder policies and reforms across a range of countries have strengthened their fundamentals. The resilience of EM has been evident not only in the way they weathered the stresses of the past few years, but in external validation of the positive impact of sounder policies. One example is IMF agreements with a number of countries recognizing their progress on reform (Egypt is an example here). Another is a swath of credit rating upgrades in a broad range of countries across regions and income levels over the past year or so—countries as

varied as South Africa, Kenya, Zambia, Bolivia, Ecuador and India. Resilience is also evident in some recent internal developments—for example, late last year South Africa revised its official inflation target from 3%–6% to 3% (with a 1% tolerance band), and the central bank forecasts inflation for the next two years to be well within that range. Another example is Brazil, whose average growth of 3.2% in the 2022–2024 period outperformed IMF projections by an average of 2% a year. We expect differentiated impacts among countries from tariff changes and other shifts in US foreign policy. In general, we think the imposition of tariffs is likely to underpin the current global trend of regionalization and reshoring, a trend that we expect to benefit select countries. We continue to monitor risks around potential negative implications from US tariff and trade policy.

We maintain the view that the USD is broadly overvalued and we expect further depreciation over the medium term, though we note that the magnitude of further weakness may not be as much as was seen during 2025. Against a background where we think the Fed is likely to cut rates somewhat further while most other developed markets pause—or even raise rates, in the case of Japan and potentially Australia—we think the underlying trend will still be dollar weakening. We highlight that the expected move is largely cyclical with some structural (twin deficit) undertones. Consequently, we also look to carry³ as a source of return, which underpins our view of select opportunities in non-dollar assets in EMs in particular. We are also constructive on select developed market currencies.

Regionally, our two main focus areas currently remain the Asia-Pacific region and Latin America. In Asia, we generally focus on countries with positive fundamentals and undervalued currencies, as well as those we expect to be more insulated from tariff effects. In Japan, we continue to see evidence of a structural reflationary shift. In Latin America, we favor countries with prudent macroeconomic policies (including those where central banks have proved to be independent and proactive), relatively high yields and undervalued currencies.

Beyond these two broad regions, we also see opportunities in certain emerging and frontier markets in both local-currency and hard-currency assets. In particular, we have exposure in some portfolios in select African countries where we believe reform efforts have resulted in notable improvements in fundamentals and the economic outlook. Elsewhere in Africa, reforms are reaping rewards with improving economic conditions and growth prospects in a number of countries. South Africa and some other African countries benefited from credit ratings upgrades last year. We also have some holdings in select frontier Asian markets. These all also offer attractive opportunities for potential yield pickup, in our analysis.

In local-currency positions, we hold select countries in both developed markets and EMs. Our currency positions focus on potential upside based on our assessment of undervaluation against the USD. These countries historically have had robust balances of payments and growth fundamentals. In bonds, we hold positions in countries where we identify supportive fundamentals. These might cover a range of factors, such as inflation and interest-rate outlooks, fiscal progress and other economic reforms, and/or anticipated economic benefits from reshoring. We aim for a relatively high overall portfolio yield by holding higher-yielding, local-currency positions in specific emerging and (where relevant) frontier markets that we view as having attractive risk-adjusted yields.

In hard-currency-denominated sovereign credit positions, we favor emerging (and, where relevant) frontier markets with improving fundamentals and policy responses.

In all positions, we closely monitor idiosyncratic factors in different countries to identify relative valuation opportunities. We remain highly selective at the sovereign level, given significant variations in economic fundamentals and policy responses

For a more detailed outlook, please refer to our [Quarterly Economic Outlook, First Quarter 2026](#).

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ENDNOTES

1. Source: Bloomberg. As of January 31, 2026. The DXY is a measure of the value of the dollar against six foreign currencies: the euro, Swiss franc, Japanese yen, Canadian dollar, British pound and Swedish krona. **Past performance is not an indicator or a guarantee of future performance.** Indexes are unmanaged and one cannot invest directly in an index. Important data provider notices and terms available at www.franklintempletondatasources.com.
2. Source: Bloomberg. As of January 31, 2026. The JPM EMBIG tracks total returns for US dollar-denominated debt instruments issued by emerging market sovereign and quasi-sovereign entities. **Past performance is not an indicator or a guarantee of future performance.** Indexes are unmanaged and one cannot invest directly in an index. Important data provider notices and terms available at www.franklintempletondatasources.com.
3. Carry refers to the potential profit or loss derived from holding an investment over time.

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Currency management strategies could result in losses if currencies do not perform as expected.

Active management does not ensure gains or protect against market declines.

Diversification does not guarantee a profit or protect against a loss.

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