

2 The International Economy

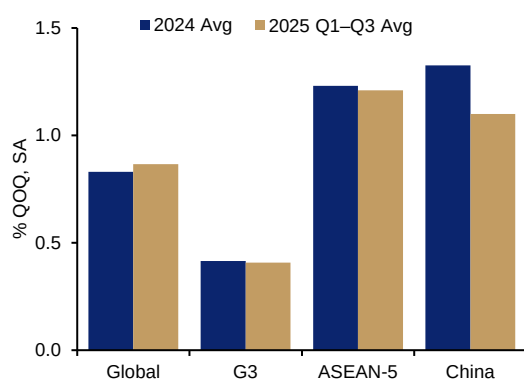
2.1 Global Macroeconomic Developments

Global growth held up at a solid pace in 2025 even as price pressures were largely contained

The global economy displayed a remarkable degree of resilience in 2025 (Chart 2.1). Despite heightened trade frictions and uncertainty, growth momentum averaged 0.9% in the first three quarters of the year, marginally faster than the pace in 2024. For 2025 as a whole, the global economy is estimated to have expanded by 3.4%, slightly higher than 3.3% in 2024. The robust growth outturn was underpinned by three key supports: agile supply chains, the AI-driven investment boom, and accommodative monetary and financial conditions.

Global supply chains have been adept in adjusting to tariff hikes. Firms responded through a combination of deft re-routing and accelerated production diversification, particularly across Asia where exports have remained firm (Chart 2.2). In particular, Chinese exporters have pivoted towards other markets such as Europe, Asia, and the Middle East, more than offsetting the decline in shipments to the US. Meanwhile, ASEAN has benefited from the re-orientation of supply chains, with exports to the US rising significantly. The tariff impact was further muted by implementation delays and phased rollouts, which spread cost pressures over time and allowed firms to more gradually adjust pricing, sourcing, and inventory strategies.

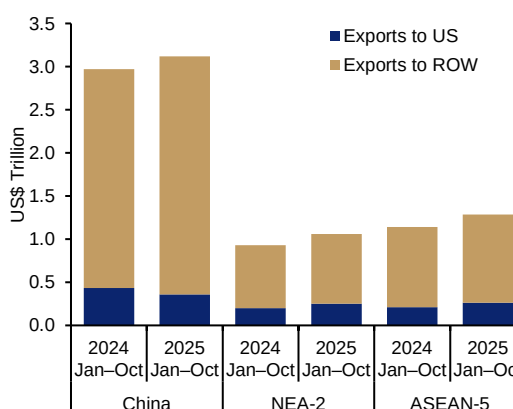
Chart 2.1: GDP Growth



Source: Haver Analytics and EPG, MAS estimates

Note: ASEAN-5 economies comprise Indonesia, Malaysia, Philippines, Thailand and Vietnam.

Chart 2.2: Asia Exports

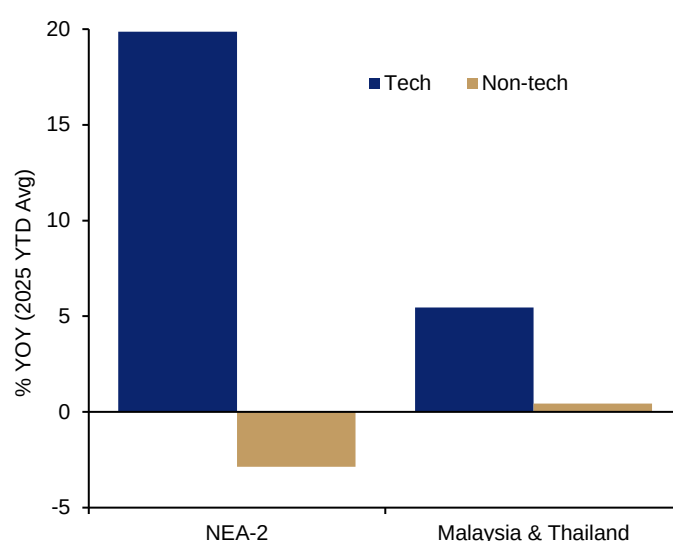


Source: Haver Analytics and EPG, MAS estimates

Note: NEA-2 economies comprise South Korea and Taiwan.

The AI investment boom in the US has also delivered a powerful impulse to growth in Asia. Capex was heavily concentrated in data centres, advanced semiconductors, power grids and networking equipment, lifting high-tech industrial production and exports in Asia. However, given the capital-intensive nature of the boost, there were limited spillovers to employment and traditional manufacturing segments (Chart 2.3).

Chart 2.3: Asia Industrial Production



Source: CEIC and EPG, MAS estimates

Note: Aggregates are calculated as simple averages across economies. Among the ASEAN-5 economies, only Malaysia and Thailand have readily available data breakdowns.

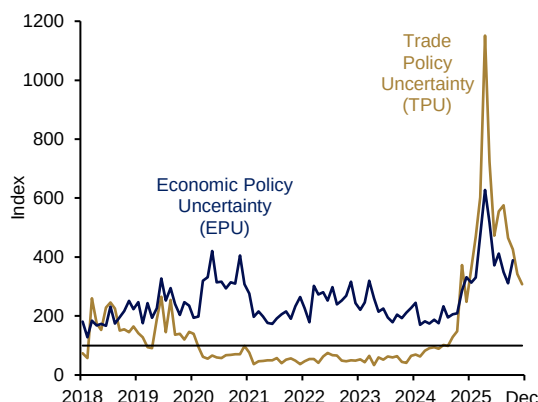
Global headline inflation continued to ease in 2025, supported by a confluence of cyclical and structural factors. Goods inflation across countries reflected the asymmetric impact of tariffs, which posed an adverse supply shock to the US while weighing on demand elsewhere. Disinflationary impulses emanating from well-balanced global commodity markets as well as subdued export prices among key external economies also capped price pressures. For the year as a whole, global inflation is estimated to have moderated to 1.8% in 2025, from 2.1% in 2024.

2.2 Outlook

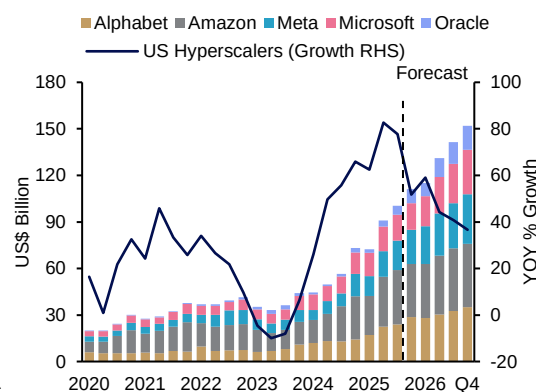
The firm growth momentum is likely to continue into 2026

Looking ahead, the pace of global economic expansion should remain intact in the near term. Trade policy uncertainty has broadly eased with the de-escalation in US-China tensions and finalisation of US tariff levels for most of the Asian economies (**Chart 2.4**). Meanwhile, the AI-driven capex upcycle appears to have further momentum, which will continue to benefit the US as well as Asian economies with significant exposure to the technology and semiconductor sectors (**Chart 2.5**). This is most clearly reflected in the sustained surge in US imports of AI-related products from Asia, with the NEA-2 economies, Vietnam, and Thailand accounting for the largest shares in recent months.

Macroeconomic policy settings are also expected to remain broadly supportive. Most central banks will likely ease monetary policy modestly in the quarters ahead, or remain on an extended hold, given the generally benign outlook for inflation. Meanwhile, fiscal policy is expected to be accommodative across the G3 economies. In the US, the One Big, Beautiful Bill Act, which includes household tax refunds and more generous corporate depreciation allowances, should provide additional near-term support to consumption and investment. Germany's gradual pivot to increased public spending and Japan's expansionary fiscal stance will support domestic demand. In Asia, China, Indonesia, and Malaysia are implementing various fiscal and quasi-fiscal measures, which should help to support domestic demand and cushion external headwinds.

Chart 2.4: Economic Policy and Trade Policy Uncertainty

Source: PolicyUncertainty.com

Chart 2.5: Hyperscalers' Capex

Source: Bloomberg

Note: Forecast refers to the Bloomberg consensus forecast.

Nevertheless, growth in 2026 could be uneven across countries and sectors. Economies with a stronger nexus to the AI ecosystem are likely to outperform relative to trend through three main channels: exports, investment, and to a lesser extent, consumption. For Asia, the export channel will be particularly important, given the region's role as the global manufacturing hub for AI hardware and related components.

Within the US, growth supports will remain bifurcated. Beyond the AI-driven investment cycle, the K-shaped consumption profile across income groups could become more entrenched. Higher-income households stand to gain disproportionately from AI exuberance-fuelled stock market gains as equities make up a significant share of their balance sheets (**Chart 2.6**). In contrast, lower- and middle-income households continue to face weak real income growth amid tariff-related cost pressures and a cooling labour market. Employment gains have fallen sharply to an average of just 49,000 jobs per month in 2025 from 168,000 in 2024, the weakest annual payroll gains (outside of recession episodes) since 2003. Other indicators such as rising unemployment and underemployment, as well as greater reported difficulty in securing jobs, further underscore the limited spillovers from AI-led growth to the broader workforce (**Chart 2.7**). This is occurring at a time when household buffers have thinned considerably, with the US personal saving rate dipping to 4.0% as at September 2025.¹

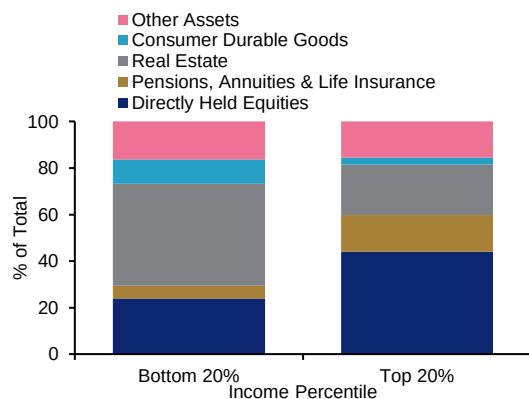
Against a backdrop of narrow and uneven growth, the effects of sustained higher tariffs are set to become more pronounced. The drag from higher effective tariffs is expected to become increasingly evident as effective rates converge towards those announced.² For example, activity in major US ports has slowed considerably in recent months (**Chart 2.8**). Non-technology exports are also likely to remain a key source of weakness, weighed down by subdued final demand. The latest Asian trade data already point to a widening divergence between technology and non-technology shipments, with the latter struggling to gain traction

¹ This is the lowest since 2008, excluding the post-COVID-19 period in 2022 when households drew down previously accumulated savings. The rate averaged 5.5% in 2023–24.

² The effective tariff rate based on federal customs revenues collected was estimated to be around 11% in October 2025. In comparison, the effective announced tariff rate was estimated to be significantly higher at 17% as at December 2025.

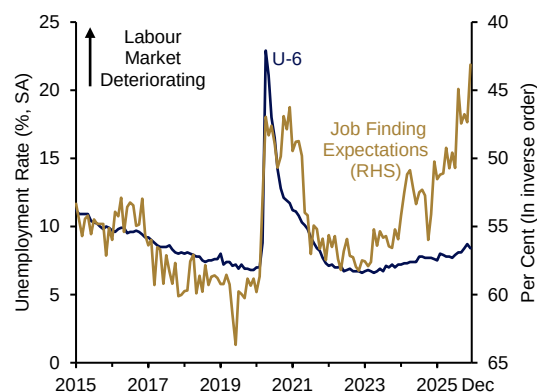
as the full impact of US tariffs progressively filters through (**Chart 2.9**). All in, global growth is projected to ease to 3.1% in 2026 from the estimated 3.4% in 2025.

Chart 2.6: US Components of Household Wealth by Income



Source: US Federal Reserve Board and EPG, MAS estimates

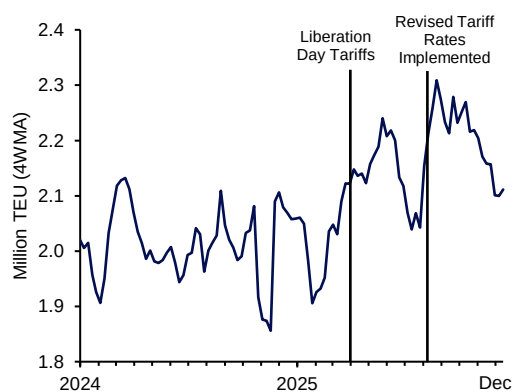
Chart 2.7: US Unemployment and Survey-based Labour Indicators



Source: Haver Analytics and the Federal Reserve Bank of New York

Note: The U-6 unemployment rate is a broader measurement of unemployment as it includes unemployed, underemployed, and discouraged workers. The job finding expectation question in the Survey of Consumer Expectations tracks respondents' pessimism about finding work, calculated as the probability of finding a job in the next three months if one loses a job today. A lower number means greater pessimism in securing employment.

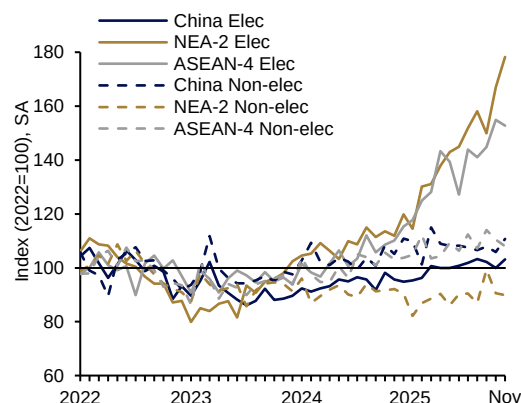
Chart 2.8: Capacity of Container Ships Calling at US Ports



Source: CEIC and EPG, MAS estimates

Note: Anticipation of tariffs and sudden changes in announced measures caused sharp volatility in shipments.

Chart 2.9: Asia Electronic and Non-Electronic Exports



Source: Haver Analytics and EPG, MAS estimates

Note: ASEAN-4 economies comprise Malaysia, Philippines, Thailand and Vietnam.

Global inflation is expected to edge higher in 2026

With global disinflation having largely run its course, inflation is likely to edge modestly higher in 2026 to 2.0%. In the US, inflation is expected to remain elevated, driven by tariffs and reduced net immigration inflows. Core goods inflation should pick up slightly, amid evidence of increasing tariff pass-through. Nevertheless, a continued moderation in core services

inflation alongside the current job-light economic expansion should anchor wage-price expectations and thus inflation. In Japan, inflation will be supported by a tight labour market, sustained wage growth, and stronger pass-through of labour costs to services fees. Meanwhile, ASEAN-5 inflation should pick up, as administrative price subsidies expire and domestic demand remains resilient. In contrast, China is expected to gradually transition from deflation to low inflation, reflecting rebalancing efforts.

The balance of risks points to stronger growth in the near term should AI capex momentum prove more robust than expected; but fragilities remain

Global growth could turn out firmer than anticipated if the AI-driven investment cycle in the US remains unrelenting, with robust AI hyperscaler-related capex providing a stronger boost to real private non-residential fixed investment. At the same time, further equity market gains driven by heightened AI optimism would increase household wealth and risk appetite, lifting consumption and crowding in non-AI investment through lower cost of capital, thereby supporting a stronger pickup in aggregate demand. Growth in the EM economies would also be underpinned by improved risk sentiment, stronger capital inflows, and easier external financing conditions. Firmer growth would push global inflation moderately higher but still remain close to targets. In response, most central banks would likely stay on hold through 2026. Financial conditions could therefore remain broadly supportive, allowing the AI-driven expansion to persist without triggering destabilising macro-financial imbalances.

However, the AI-centred economic expansion, and its attendant market buoyancy, could also present downside risks to growth in the event of a sharp repricing of market expectations about the profitability of AI ventures. This could set off broad-based de-risking, with spillovers into the real economy through negative wealth and confidence effects, and tighter financial conditions. The rapid growth of private credit in AI investment could also obscure underlying leverage positions and may amplify vulnerabilities within the broader financial system.

The probability of a systemic market correction is tied to the threat of several potential shocks materialising at once. A trigger event—including a re-escalation of tariffs, upsurge in geopolitical flashpoints and deepening fiscal sustainability concerns amid elevated and rising public debt—could cascade into a sharp loss of confidence with contagion that leads to an unravelling of the AI buildout and associated financial excesses.