

## EXECUTIVE SUMMARY

Once again, the global economy is threatened with being thrown off course—this time by the outbreak of war in the Middle East at the end of February 2026. Over the past year, headwinds from higher trade barriers and elevated uncertainty have been offset by tailwinds from technology-related investment; accommodative financial conditions, including a weaker US dollar; and fiscal and monetary policy support. The Middle East conflict presents a significant counterforce to these tailwinds through its impact on commodity markets, inflation expectations, and financial conditions.

Given the difficulty of underpinning in real time a consistent set of assumptions for projections, this *World Economic Outlook* (WEO) report presents a “reference forecast”—in lieu of the traditional baseline—predicated on the assumption that the war will have limited duration, intensity, and scope, such that the disruptions will fade by mid-2026, consistent with commodity futures prices as of March 10. However, given the fluidity of the situation, the report complements the global reference forecast with scenarios in which the conflict lasts longer or expands. The likelihood of these scenarios materializing rises progressively as hostilities and associated disruptions continue.

Under the reference forecast, global growth is projected to be 3.1 percent in 2026 and 3.2 percent in 2027, slower than its recent pace of about 3.4 percent in 2024–25, and to settle at about that rate in the medium term, slower than its historical (2000–19) average of 3.7 percent. The forecast for 2026 is revised downward by 0.2 percentage point and that for 2027 is unchanged, compared with those in the January 2026 WEO *Update*. Global headline inflation is expected to increase to 4.4 percent in 2026 and decline to 3.7 percent in 2027, marking upward revisions for both years.

Absent the war, global growth would have been revised upward. Indeed, forecasts based on preconflict assumptions would have shown a slight upward revision of 2026 growth relative to that forecasted in the January WEO *Update*, by 0.1 percentage point to

3.4 percent. Hence, the downward revision for 2026 largely reflects the disruptions from the conflict in the Middle East, partly offset by carryover from recent strong data and reduced tariff rates.

Crucially, there is a high degree of cross-country dispersion in the reference forecast. While the growth and inflation revisions seem relatively modest at the global level, the toll on the conflict region and more vulnerable economies elsewhere—in particular, commodity-importing emerging market and developing economies with preexisting fragilities—is much more pronounced. The downward revision to growth in emerging market and developing economies is 0.3 percentage point for 2026, relative to that in the January WEO *Update*, while the forecast is broadly unchanged for advanced economies.

Under an adverse scenario with larger and more persistent increases in energy prices, global growth would slow further to 2.5 percent in 2026, and inflation would reach 5.4 percent. Under a more severe scenario in which there is more damage to energy infrastructure in the conflict region, the impact would be even larger: Global growth would be cut to only about 2 percent in 2026, while headline inflation would be just above 6 percent by 2027. The impact on emerging market and developing economies would be almost twice that on advanced economies.

Downside risks dominate, even after the realization of a risk event—namely, an escalation of geopolitical tensions—frequently underscored in previous WEO reports. Geopolitical tensions could worsen even more than they already have—turning the situation into the largest energy crisis in modern times—or domestic political strains could erupt. Political stress factors can get entangled with shifts in trade and other international policies. Independently of geopolitical developments, trade-related disputes could flare up. As the Commodity Special Feature highlights, the critical role of rare earth elements in global supply chains constitutes a particular point of friction. A reevaluation of profit expectations regarding artificial intelligence (AI) or lowered expectations of viable markups stemming from more intense competition—even if productivity

gains are realized—could lead to a decline in investment and trigger an abrupt correction in financial markets. Larger fiscal deficits and increasing public debt, starting from a position where fiscal buffers are already eroded, could put pressure on long-term interest rates and, in turn, on broader financial conditions. An erosion of institutions, including central bank independence and monetary policy credibility, could raise inflation expectations—especially at a time when headline inflation is increasing because of a shock in salient prices. On the upside, activity could be further lifted by AI-related investment and eventually transform into sustainable growth if faster AI adoption translates into strong productivity gains and increased business dynamism. Activity could also be supported by renewed momentum for structural reforms and by a sustained easing in trade tensions.

Navigating a profoundly changing economic and geopolitical landscape requires policies that are robust to alternative states of the world. As Chapter 2 shows, scaling up of defense spending prompted by a rise in geopolitical tensions could boost economic activity in the short term but also bring about inflationary pressures, weaken fiscal and external sustainability, and risk crowding out social spending, which could in turn ignite discontent and social unrest. As Chapter 3 demonstrates, where conflict erupts, acute macroeconomic trade-offs and scarring follow and last well beyond the immediate wartime shock.

A comprehensive policy package would combine measures that countries should take on their own and measures that countries should pragmatically work together to implement to enhance resilience and foster agility and adaptability. This first and foremost involves preserving price and financial stability, safeguarding fiscal sustainability, and implementing structural reforms without further delay. Central banks should remain vigilant and be prepared to act clearly and decisively in line with their mandates. They must

guard against prolonged supply shocks destabilizing inflation expectations. Monetary policymakers should reserve the option to look through negative supply shocks—such as the current one—as long as inflation expectations remain well anchored and the monetary policy stance is already properly calibrated. Transparent communication and strong central bank independence are critical for credibility. Where an imminent risk of excessive or disorderly exchange rate movements emerges, temporary foreign exchange intervention and capital flow management measures may be warranted, provided they support appropriate monetary and fiscal policy stances. Financial supervisors should be prepared by ensuring robust prudential oversight, conducting scenario analysis, and maintaining adequate capital, liquidity, and reserve buffers. Where fiscal support is deemed to be necessary to protect the most vulnerable against extreme external shocks, it should be targeted, timely, temporary, and funded within current budget envelopes by reprioritizing spending, and if that is not possible, with the path to restoring fiscal balances clearly communicated. To replenish buffers for future shocks, governments should—as appropriate for their country-specific circumstances—mobilize revenues, reprioritize expenditures, make spending more efficient, and manage windfalls prudently. A second priority is addressing domestic imbalances, especially when doing so also helps reduce excessive external imbalances. Actions aimed at removing domestic distortions—through fiscal, structural, and industrial policies—can simultaneously narrow external imbalances while enhancing global output. Trade restrictions play a limited role in correcting imbalances but can worsen output. Instead, countries should cooperate and take coordinated actions to restore stability in international economic relations. They should seek opportunities to enhance trade integration, supported by predictable, transparent, and well-communicated trade policy frameworks.