Can Policymakers Stay Ahead of Global Risks?

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Sara Murray: Welcome to C-Suite Perspectives, a signature series by The Conference Board (TCB). I'm Sara Murray, Managing Director International, and the guest host of today's episode. Today we'll examine the latest developments surrounding the war in Iran and what they mean for the global economy. As policymakers and business leaders respond to a rapidly evolving environment, we'll also explore the broader geopolitical tensions, policy decisions, and economic trends shaping growth, investment, and corporate decision-making around the world.

Joining me is Alejandro Fiorito, Economist at the Economy, Strategy & Finance Center in Europe at The Conference Board. Welcome, Alejandro.

?Alejandro Fiorito: Thanks, Sarah.

Sara Murray:Let's first take stock about the geopolitical and geoeconomic situation globally. How is the war in Iran evolving?

?Alejandro Fiorito: I don't think this will be a surprise for anyone but the situation remains quite fluid. There are diminishing returns, looking at the numbers and updates day by day or even hour by hour, unless you're in markets or press. But now we can take stock, look at the big picture, and emphasize what's clear now after four months of conflict.

First, I should say we are in an environment where there is an agreement, a memorandum of understanding. But I would take any announcement on the agreement and any development as such, as a developing framework. I recently heard a journalist, Carlos Lozada, say that in wars, the off-ramps are rarely well marked or well paved. that's a key message, that we don't really know exactly where we're going to go and it might be a bumpy road.

This is because there are still differences on crucial topics, from the impact of the conflict in Lebanon and what role the situation in Lebanon plays in this agreement to how Iran's going to manage its nuclear program. None of these issues or differences have any easy fixes. Any equilibrium we might reach or we may think we're reaching is a fragile one.

The next thing I would like to emphasize is that for markets going back to normal and particularly for oil markets, it's not going to be straightforward either. Even if at the time of this recording, oil markets have come down a lot and future pricesreflect lower levels, we are still above pre-conflict levels and we're likely to remain there for a little bit.

Sara Murray: How are all these developments affecting growth forecasts and firms' decisions?

?Alejandro Fiorito: If we look at the growth forecast we publish every month, I would say they're well-anchored. If you look the last few months, we haven't deviated that much from the revisions we did originally in March and April.

This is in part because reality has not deviated that much from a base case scenario but also because our colleagues have not gotten carried away with big news or headlines. The main message for the global economy, and this is important for our members since most are multinational companies, is that the global economy has not fallen off a cliff.

It's shown significant resilience. But of course, the forecasts have weakened and have become more uneven, so sharper revisions in some areas than in others. At the start of the year, we at The Conference Board always do this exercise, long-term projections, and we had global GDP at 2.9% for 2026.

That number is now 2.7%, so that revision is not that significant. It's two-tenths of a percentage point and actually what I think it's where we are a little more optimistic is 2027 we haven't revised down. We still have it at 3%.

As I was saying, there are significant differences about where this resilience is coming from. We'verevised down growth for the US from 2.1% to 1.8% for 2026, which is 0.3 percentage points. It's the same revision as in the Euro Area but in the Euro Area it's from a lower base. In the Euro Area, where we've moved down from 1.3% to 1% growth for this year, which means that 0.3 percentage point decrease in Europe is much more significant than in the US-- and particularly countries like Germany and France have seen sharper reductions.

As you might imagine, the largest revisions are in the Middle East and North Africa, where growth has fallen from around 3%, 4% depending on the country and the sub-region, to closer to 1%.

In contrast, in the big Asian economies, China and India are the ones that have shown resilience and we have not changed our growth forecast, which are 4.5% for China in 2026 and 6% for India. And this explains to a large extent why our global growth has not

decreased so much.

Elsewhere in Asia is where we have, again, a mixed picture. Thailand has proven to be a little more resilient than expected and the Philippines, for instance, we've been lowering and adjusting our growth forecast in recent times. While we remain optimistic, I think the key message for companies is that risks have intensified.

Going back to the US and Europe, we see that in the sources of growth, in the US, we know that private consumption is a huge engine of growth and we know the private consumption dynamics are deteriorating. And that private investment, and our colleagues in the US have written about this, is now the main driver of growth. But there are questions about how sustainable the current cycle is, how persistent it might be, particularly if the Federal Reserve is forced to raise interest rates due to inflation.

For Europe, again, talking about the composition of growth, what we expected to be a positive cycle of growth rebounding, in part led by public expenditure related to defense, has now just become more costly and more difficult due to this increase in energy costs. Sowe're in an environment where we need to look not only at the headline numbers but at how the composition of this growth and the differences across regions and countries.

Sara Murray: It sounds then the knock-on effect is that business is more cautious, so there might not be dramatic shifts overnight but maybe reassessment of investment decisions. Managing the risk a bit more actively and just preparing for this more uncertain environment.

?Alejandro Fiorito: Absolutely.

Sara Murray:What's been the policy response from the public sector? Can we start with the fiscal side and then we can get onto the monetary front, especially in Europe?

?Alejandro Fiorito:I'll focus more in Europe but also make mention about international developments. What we have in Europe are relatively small policy responses on the fiscal side so far. In a way that's a good sign because fiscal policies to address an energy shock are costly and generally when you need to take measures, that signals that the damage that the economy is facing is substantial. So the fact that the responses have not been too large is a good sign.

The IMF actually has a very nice tracker of the policies and shows very interesting differences between advanced economies and emerging economies. For advanced economies, most measures have been subsidies to energy producers and distributors and also cut of excise taxes that aim to contain the retail price of energy.

In Europe in particular, we know that has been the case, and they've leaned very heavily on this fiscal support for households and also for firms. Again, this is in part because the shock has been manageable. If the shock had been larger, cutting taxes and this blanket support is not sustainable.

In other regions more directly affected, like Middle East or Central Asia, policy coordination has been needed and monetary and financial interventions have also been required. In other parts of Asia, where we've seen very the high levels of dependency on fossil fuel and particularly on imported fossil fuel, they have to respond with demand management or energy conservation, even rationing in some cases, which are much more extreme policy measures.

Fortunately, that'snot been the case for Europe so far. The key issue here is that if you want to take more fiscally sustainable measures-- and that basically means allowing prices to rise, to put it quite bluntly-- you need very strong safety nets and not all countries have safety nets. Or you need other interventions like promoting public transportation, which are costly and not that easy to implement in the short term.

So in Europe, as I was saying, most interventions have been related to fiscal spending or reducing revenue through tax cuts. And this has been much larger than in other regions but, again, much more contained in the size. If we look at it, Spain and Greece have been the countries that have spent the most, and it's about 0.3% of GDP, which is relatively small. If we take for comparison 2022, countries spent around 10 times that. It was over a longer period of time but still, we're not there in terms of the measures that are needed to be implemented.

What we see in Spain and Greece are some small differences on how they implemented. Spain has focused more on, to give you a couple examples, removing taxes and supporting specific industries, while Greece has offer more direct support to consumers and also focus on farmers.

But fortunately, as I was saying, while imperfect, these measures, because they're broadly untargeted, they have not been large and only cost a few billion dollars, I would say.

Sara Murray: Then the monetary front?

?Alejandro Fiorito:That'swhat's been driving the news recently because we had a very consequential meeting by the European Central Bank (ECB) in early June. I say it's consequential because it resulted in the first hike since late 2023. For more than two years, the central bank had been reducing or maintaining interest rates. We were at 2%, so relatively low, and now they've increased interest rates by 25 basis points to 2.25%.

Beyond the decision itself, the debate for the central bank and for monetary policy in Europe but also elsewhere is how do you address supply shock with monetary policy? We'vediscussed about this in the past. And here, the ECB, I have to say, has taken a textbook approach. They were cautious in communications when the conflict started because there were a lot of unknowns but signal at the same time a readiness to act.

And now they'veacted and I think they've explained very well the decision. I would call it a

preemptive hike, interest rate. The reason why I call it preemptive is because we're not yet seeing reasons for a hawkish turn, for a sort of a sustained or the start of a hiking cycle.

This is because we are not yet seeing what we call second-round effects, which would be wage pressures, so wage growing substantially, or price increases that are seen as persistent because inflation fears are entrenched in expectations.

President Christine Lagarde explained that we are seeing a broadening of inflation. This means more goods and more services, categories showing growth rates above 2% year on year, which is above target.Soit's not just energy. That is a cause for concern and a cause for a hike. At the same time, she mentioned that we're not in an environment where growth is absent or under significant threat.

So growth is very low, as we just discussed, for the Euro Area. It's weak but it's not disappearing. We're not in recession territory. Taken together, all this information does not give you a clear signal of what you should do, particularly because even though uncertainty has come down a little bit, we're still managing a lot of uncertainty.

How the ECB arrived to the decision, I think, is very interesting. They ran several scenarios and they included a mild scenario, an optimistic one so to say. At the time when I first saw it, I thought that was almost wishful thinking. But it was actually very useful for them to analyze what a hike would mean if that mild scenario materializes. And by that a swift resolution of the conflict, which will lower inflation and raise growth. In that scenario, they basically pose the question, even in that scenario, is a hike consistent? Is a hike robust? The word that was used a lot was robust. When we try to measure robustness, it'sbasically testing whether this hike is warranted under different scenarios, particularly this benign one, but also more severe ones.

And the conclusion they reach-- and again I think they explained this pretty well-- is that the hike was warranted even in this milder scenario. If the conflict is resolved swiftly, it waswarranted because we are seeing that broadening of inflation and a small hike could temper that broadening.

If not, and we get a severe or a bare scenario, it is the right choice to start a potential hiking cycle. And hopefully that won't be the case. But I thought it was a very good example of central bank communicating clearly how they're thinking about monetary policy at a time of very high uncertainty.

Sara Murray: It does sound like policymakers are facing quite a delicate balancing act, as you said, they've gotta support the growth, but they've gotta maintain stability while tackling inflation, preserving fiscal discipline. It'sa very complex kind of policy environment, more so than we've seen in recent years.

?Alejandro Fiorito:Yeah, and it's one where you need to face trade-offs. You need to acknowledgeyou're not going to get a perfect answer. You're going to have to win some,

lose some. And I think communicating that clearly to the public is what policymakers need to do now.

Sara Murray: Would you say that these responses are incorporating past lessons learned, particularly from 2022?

?Alejandro Fiorito: Yes. Particularly in the monetary, as you can probably tell, I'm more positive on the monetary policy response. This discussion of scenario robustness has been very appropriate. On the fiscal front, some of I would call preemptive measures-- in terms of reducing dependencies from fossil fuels in some countries, shifting providers, diversifying providers-- have been good.

But the reaction to the shock, the measures we've been discussing, have been mostly untargeted, which is not good. I'm not very positive about the design of these policies. Back in April, we talked about that the key characteristic for an appropriate fiscal policy response is where the three Ts: targeted, tailored, and temporary.

I've recently seen a fourth T: timely. So now we have four parameters to measure responses. And the concerning thing is that for Europe, only France's, the response that the French government, took satisfies the four Ts. In part because they rely more on nuclear energy and they have pretty diversified energy sources, the impact has been smaller, which has allowed them to be perhaps more precise with their measures at the expense of a broader impact. But also we need to acknowledge they have limited fiscal space and political constraints that have forced the government to be pragmatic and take this narrow approach.

As I was saying, the concerning part for me is that no other country even achieves three of the four Ts. Most measures are temporary and timely, which is good, but very few are tailored or targeted. This is the broad blanket measures that we're seeing. They're not very precisely designed. Because they're not very large, as I said before, the distortions they could generate by not being tailored or targeted are also not very large, which is the good news.

But on the fiscal front, the policy response has been suboptimal. This does not suggest we learned a lot, to answer your question about 2022.

And there is another data point that we should keep in mind and we should continue monitoring and Bruegel has a tracker on this, which shows that 86% of the measures that have been taken so far as of mid-June actually increase incentives to consume fossil fuels. Only 3.5% incentivize a decrease in consumption. We need to be fair and recognize that we still live in a world where fossil fuels remain incredibly important for economic activity. But it is a concerning sign that the money that governments are spending is sometimes going to the wrong places.

Looking forward, I would emphasize again the election cycle is going to be important. It might create even more perverse or wrong incentives that might make governments take

sort of shortsighted measures. Just to summarize the discussion about the policy response, I think we talk a lot about resilience-- and I like to divide resilience in two components when thinking about how countries are resilient to a shock. One is their capacity to absorb the shock and here's where I think Europe in particular has gotten better and firms as well. We should say they have gotten better at receiving the shock, absorbing it. Particularly for countries and on fiscal side, I'm not sure they've gotten better at the second part of resilience, which is responding to the shock. That's where I think there's still work to be done.

Sara Murray: So definitely could be better.

?Alejandro Fiorito: Yes.

Sara Murray: Okay. We're going to take a short break and be right back with more of my conversation with Alejandro.

Welcome back to C-Suite Perspectives. I'm your host, Sara Murray, Managing Director international at The Conference Board. I'm joined by Alejandro Fiorito, economist in the ESF Center at The Conference Board Europe.

What do we know about the government's actions elsewhere beyond Europe?

?Alejandro Fiorito:Sowe've discussed a little bit about the fiscal and how it's been very different depending on impact. On monetary policy, I think it's where, again, the latest news and the most interesting part is happening right now.

The most meaningful development is, of course, that we have a new chair of the Federal Reserve, Kevin ,Warsh and our US colleagues had a great podcast after his first meeting in charge a few weeks back. This is perhaps or most likely the most important nomination that can happen for the global economy. I will leave the US implications to our US colleagues but I think whatever the Federal Reserve does matters for monetary policy everywhere.

We saw two key things. First, a hawkish tone. While at TCB, we still do not expect a hike of interest rates in the US this year, given high uncertainty and the fact that rates are already elevated.

I think there was an important perception that the Fed is really focused on the inflation part of its mandate. And in addition to this hawkish perception, Warsh announced five task forces to review and assess the functioning of the Federal Reserve. I think this is quite significant for the US, but again, also for the rest of the world because this might mean some operational changes or revisions to how the Fed works.

And particularly at a period of turbulence like where we are right now, we're not in normal times, coordination between countries and central banks is very important to assess financial stability risk, to assess global liquidity. And I think we can continue to expect this

coordination but it's going to be a little trickier, at least in the short term.

Markets are going to be more important in giving signals. The new Fed chair has expressed a preference for markets interpreting what the Fed is doing themselves and not so much forward guidance. And the first reading that markets are giving us is that the Fed is going to be more hawkish, as I was saying.

This is already impacting monetary policy elsewhere and exchange rate dynamics. In Europe particularly, we're already seeing very shortly after the meeting some effects. The euro has fallen vis-a-vis the dollar. So when monetary policy tightens in one central bank, that usually means its currency appreciates vis-a-vis other currencies, and that's particularly the case when it's the Federal Reserve. The euro, as I was saying, has fallen below 1.15 vis-a-vis the dollar for the first time in more than a year.

It's important to highlight where we're coming from. This has happened after the euro had strengthened quite a bit last year and we wrote about it last year. We talked about how this harmed exporters because it was also a double whammy-- it's how we call it-- from both tariffs and this appreciation that affected Europe's exports, particularly to the US.

So in a way, if the US dollar now strengthens, the euro weakens and this can help exporters gain some external competitiveness. This is a little bit artificial because it's competitiveness stemming from exchange rate movements. But it can help growth a little bit in the Euro Area.

The other side of this is that it will make imports more expensive, and this matters particularly beyond Europe for emerging markets, including particularly Asia, and countries that import a lot of energy. Energy's usually paid in dollars, so that energy's going to become a little more expensive if the dollar continues to strengthen.

So while we're seeing prices come down, exchange rates might have a little bit of a negative impact on costs and on inflation. Countries like Philippines, as I mentioned before, that have suffered high burden from this crisis, might need to adjust their monetary policy more strongly to ensure that a currency depreciation does not result in further inflation or significant fiscal cost.

The key thing internationally now is see how countries react to the Federal Reserve entering a new era and we will need to keep tracking this.

Sara Murray:It'salmost like governments around the world, they'll respond in different ways depending on the economic priorities and exposure but the common theme is how to strengthen the resilience while limiting the kind of economic fallout.

?Alejandro Fiorito: Yes.

Sara Murray: What do these policies or the policy responses mean for companies, consumers, and the broader outlook?

?Alejandro Fiorito: So particularly for Europe, we have some data points. We have the consumer confidence on the Euro Area. The headline is that it has fallen to its lowest level since late 2023, so consumer confidence is quite low.

The cumulative drop since February is one of the largest that has been recorded, even if there's been some recovery from the lows we reached in April. But I think it's interesting and this is the nice thing about the measure, that it has several components.

Four to be precise. The two that are deteriorating the most are economic expectations, what consumers think is going to happen with the broader economy and the future financial situation But when we ask-- or when the European Commission, because this is their data that we just analyzed-- we ask about the current financial situation and expectations, consumers tell us they're feeling a little bit better about those.

I interpret this difference between pessimism on the outlook. It's still negative, but less pessimism about current financial situation and spending expectations as consumers are very concerned by the external environment but not perceiving a direct impact yet. The data we have from labor markets supports this narrative.

Unemployment has not meaningfully increased in the Euro Area; remains around six, 6.5%, which is near historic lows. There are some nuances here. A lot of the positive comes from countries like Spain and Greece, we mentioned before. Their unemployment has come down quite a bit from historic highs.

But overall, the labor market seems fairly strong. While wage growth has cooled a bit and therefore purchasing power is deteriorating because of inflation, consumers show some resilience. And of course, fiscal policy here plays a role. The fact that it has been expansionary even if imperfect, as I mentioned, it has supported consumers.

And monetary policy --which has been more restrictive and will eventually affect consumers and companies through borrowing costs-- has not tightened significantly. So borrowing financial conditions are still relatively benign in the Euro Area. And for companies, we see something similar, whereasthey'revery concerned about the economic outlook but there's pockets of resilience.

We talked about an indicator we had at The Conference Board, the CEO Confidence for Europe, which we released in June. And we have in this measure a mixed picture, right? The results are not good but there is this sort of mild optimism, I would call it, in sales prospects from companies.

And also when we ask about expectations for their industry, they're near neutral. So not negative nor positive. This is something we also hear from members: businesses are also becoming better at dealing with a complex and even negative external environment.

It's not good that we have all these shocks and that we're needing to react to this, and that policy has been so proactive the public sector has had to intervene so much. But seems

to me that companies are also learning how to absorb and deal with these shocks. And the policy responses, as I was saying, they're imperfect but so farthey've been fairly supportive of consumers and companies.

I would say that governments in Europe particularly may be accepting lower efficiency and potentially higher inflation in the medium term to ensure that consumers and firms and growth more broadly issomewhat protected in the near term.

Sara Murray: It sounds to me like while policy can or is helping to cushion some of the immediate impacts, it doesn't totally eliminate the uncertainty. But that said, businesses and consumers seem to be better at adapting to what continues to be quite a fluid environment.

?Alejandro Fiorito:Yeah. And that's where once uncertainty starts hopefully dissipating, it's going to be very interesting to see how they react, how quick-

Sara Murray: How the confidence changes.

?Alejandro Fiorito: Exactly. How hopefully quickly it recovers. I think that's the question.

Sara Murray: What can we expect for the rest of the year then, in terms of key dates and policy decisions?

?Alejandro Fiorito:I've mentioned it before, but just to reiterate, I think the election calendar is going to become more important for Europe.

There might be very significant changes in the policy front, even before the results are in, even before the elections happen, because just the fact that we're having these elections will affect policy decisions. They will most likely, unfortunately, create a little bit of uncertainty and will reset the agenda for countries and for the EU.

They're likely to make fiscal policy a little more expansionary, even in the near term. So that's where we are in the I would say almost a new cycle, politically driven cycle that, that's starting, I would say, in the second half of this year.

To be more, more specific on dates, I think something we've also touched before is that monetary policy meetings are going to become more and more important. First, because they're going to deal with this change in leadership in the Fed. Sowe're going to need to interpret the decisions to reassess how we read the most important central bank in the world.

And second, because what we've seen this year is that when monetary policy meetings happen, and usually most major central banks meet pretty closely-- and this happened in March, for instance-- markets take the time to take stock. These are a few days where everyone is thinking about what the day-to-day craziness means and what does it amount to.

And these can be breaking points for confidence. We have four meetings left in the year by both the ECB and the Federal Reserve, and they're broadly similar dates. One in late July, one in early September, one in late October, and one in mid-December. Hopefully they'll be uneventful but if past experience tells us anything, it's that they won't.

So those are key dates where markets, consumers, and companies might reassess what their priors are and what environment they'reoperating in. To conclude and summarize what I think is left for the rest of the year and for the near term is we need to continue to track a lot of key risks beyond the war in Iran.

There is an understanding that we need to monitor all them but I'll still mention because I recently heard an analyst say that he was comparing current shocks or current events to past. And it was a very interesting exercise of saying, first, the current war in Iran and the shock to oil markets has not been as destructive or damaging as the oil shock that we saw in the 1970s.

The second thing is private credit. There are some concerns about private credit in the US and elsewhere. He said it's not the same. These concerns are not as bad as the concerns we had when we were approaching the global financial crisis. Risks are now more concentrated, less systemic, and regulators-- and I agree with this-- are better equipped to deal with this.

The third thing he mentioned is that the AI bubble, or whether it is a bubble. It's different from what we saw in the early 2000s with the dot com, because now what we're seeing is large investors, thehyperscalers, are actually solid companies that have real revenue, tangible assets, right? So it was an optimistic view about all the risk.

And I would add to this. The trade tensions from last year have not resulted in trade tanking, but more of trade being reshaped and redirected. And the worst fears probably have not materialized for any of those sort of four key risks. But the key point to me is that these things are all happening at the same time and that is the exception.

We've talked about policy responses a lot in this podcast. And policy responses are complex because they're addressing all these key risks. I think we're entering an environment in which fiscal policy might remain expansionary for longer than we may wish, particularly large fiscal deficits in emerging markets but also in the US.

If that happens-- and at the same time monetary policy becomes more restrictive, tightens more-- we might have some imbalances in the policy responses and in markets that make some of these risks materialize. There's not any immediate cause for concern but there are many things we need to continue paying close attention.

Sara Murray: It sounds as though the second half of the year could be shaped by several important policy decisions given the meetings that are still to take place. But for business leaders, as you said at the start, the more informed they are and the more that they remain flexible, that's just as important as trying to predict exactly how events are going to

unfold.

For me, one of the key takeaways from the conversation today is that while geopolitical events might occur in one region, the economic effects are global. But business leaders really need to focus on resilience, agility, scenario planning. That's becoming more and more essential as a capability rather than optional capabilities.

?Alejandro Fiorito: And we're getting a better understanding of what the risks are. I would say that is even if the risks generate uncertainty, having a better understanding of them decreases uncertainty. So that's some mild good news, I would say.

Sara Murray: Yes, exactly. Exactly. That takes us to the end of today's conversation. Thank you for joining. And thanks to all of you for listening to C-Suite Perspectives. I'm Sara Murray, and this series has been brought to you by The Conference Board.

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