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Geopolitics, policy and earnings

Strong US earnings upgrades are likely to overcome renewed tensions in the Middle East.

US election constraints may eventually limit escalation in the Middle East conflict. Central banks are likely to hold rates this month as they assess the inflation outlook. Strong earnings upgrades are likely to drive equity market outperformance.

Middle East conflict limited by US election constraints

The re-escalation of Middle East tensions, with Yemen's Houthis joining the conflict, has driven European gas prices back to March peaks, but US gasoline prices remain well below the latest peaks. Notably, Iran has avoided attacking Saudi Arabia and UAE in the latest escalation, signalling restraint. While there is a window for further near-term escalation, any rebound in US gasoline prices back to May's peaks in the run-up to November's mid-term elections is likely to put pressure on President Trump to resume negotiations. Thus, it is expected that the US crude oil (WTI) to trade largely in the USD 70-90/bbl range in the next few months, limiting the economic impact.

Fed, central banks to hold rates this month.

Central banks to hold rates this month as they assess the inflationary impact of the latest escalation in the Middle East. The softer-than-expected US inflation report for June confirmed inflation peaked in Q2. Fed is expected to stay on hold for the rest of the year as long as long as gasoline prices remain subdued, given slowing wage growth and cooling shelter and services inflation.

ECB, BoJ under rising pressure to hike

The ECB, being an inflation-targeting central bank, is under growing pressure to hike rates in the coming months to counter any energy-price driven inflation if European natural gas prices stay elevated. The BoE is likely to be constrained from hiking rates, though, due to weakening domestic growth outlook. Meanwhile, the BoJ remains behind the curve as a weaker currency pours fuel on domestic wage-driven inflation. There is rising chance the BoJ hikes twice this year, if only to support the JPY.

US earnings to drive equity outperformance

US big tech might deliver solid earnings and clearer signs of AI monetisation. The tech sector has driven over half of S&P 500 EPS upgrades since end-February 2026, with Q2 sector earnings expected to rise around 66% y/y on cloud growth and AI demand. US Census Bureau data show AI adoption has reached 20-25% across US industries. While lower-cost Chinese models raise commoditisation concerns, efficiency gains should lift total usage. The US technology and communication services sectors are favourable to rising AI demand.

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