What will be important in 2026

We highlight the issues that are likely to shape 2026 and what this could mean for the markets. Among other things, we examine whether an AI bubble could burst, whether the Fed will remain independent, whether Germany will experience an economic downturn, whether there is a threat of a sovereign debt crisis in the eurozone, and what could happen in the event of a ceasefire in Ukraine.

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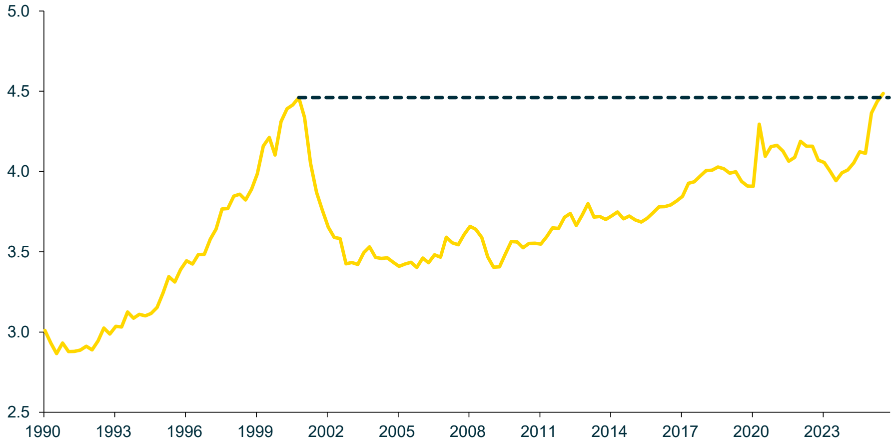
Is an AI bubble about to burst?

Many investors are fascinated by artificial intelligence (AI) and have driven up the share prices of the main players (the "Magnificent Seven") in particular. Now, more and more investors are asking whether this is a bubble and when it will burst.

There are indeed serious warning signs. This applies above all to the increasing interdependence and interconnection of companies. The fear is that companies are inflating their sales through mutual supply contracts. Cross-shareholdings increase systemic risk because they link the futures of many companies to one another. In addition, IT investments by US companies have now risen to 4.5% of gross domestic product, which is as high as they were at the peak of the New Economy bubble in 2000 (Chart 1).

We are less critical of the high valuations of AI stocks, however. Although the price-earnings ratio of the Magnificent Seven is 34, which is at the upper end of the range of 26 to 36 over the last five years, it is still far from the valuation excesses of the New Economy bubble. At the end of the 1990s, the P/E ratio of the ten largest US companies was 47, and that of the Nasdaq 100 was 90. In addition, the main beneficiaries of the AI boom are currently companies with healthy balance sheets and highly profitable business models. The Magnificent Seven have been able to rapidly increase their profits until recently. The markets are also likely to benefit in 2026 from the fact that the Federal Reserve is likely to cut interest rates significantly. This argues against a slump this year.

Chart 1 - High-tech investment reached New Economy peak
Private investment in information processing equipment and software in % of GDP, quarterly data. Dashed line: New Economy peak reached in Q4.2000



Source: BEA, S&P Global, Commerzbank Research

Will the Fed remain independent?

With his attempt to remove Fed Governor Lisa Cook from office last year, President Trump launched an unprecedented attack on the independence of the Federal Reserve. He believes he has the right to replace the leadership of any federal institution without needing a good reason, such as a breach of official duties by the person concerned. If he succeeds in imposing this view, he could fill the Fed's central governing body (the Board) with his followers and significantly influence the Fed's course. A central bank that is so politically dependent could put price stability on the back burner and give priority to supporting economic policy. This increases the risk that inflation expectations will become unanchored and long-term interest rates will rise sharply, contrary to Trump's intentions. Confidence in the dollar would dwindle.

Probably also in view of the fundamental significance of this case, the Supreme Court has prohibited Cook's dismissal for the time being. An oral hearing on this matter is scheduled for January 21. The justices' position should then become clear.

Most observers expect the Supreme Court to ultimately rule against Trump. At least that is what a passage in the order preventing Cook's immediate dismissal suggests. According to this passage, the Fed is a "uniquely structured, quasi-private institution." The justices, who had granted Trump the right to replace senior staff at other independent federal agencies, are likely to apply a different standard to the Fed.

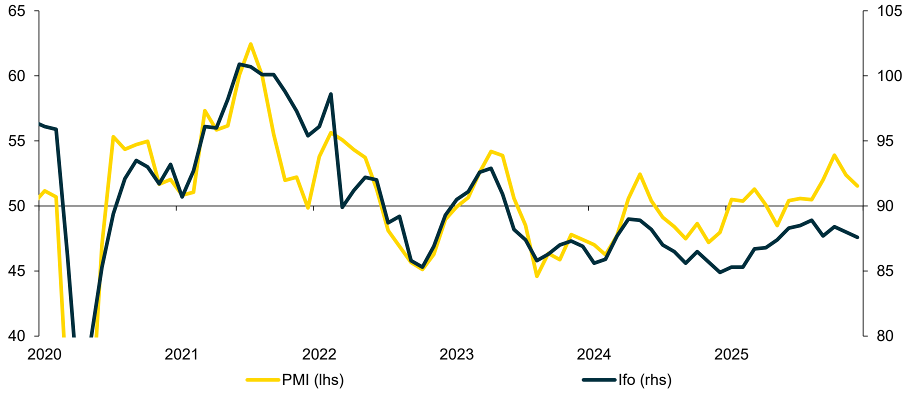
This means that Trump can probably only bring the Fed under his control by replacing Jerome Powell, whose term as chairman of the Federal Reserve Board ends in May, with a compliant monetary policymaker. Many see Kevin Hassett as the favorite to succeed Powell. Trump's economic advisor in the White House is considered a close and loyal confidant of the president.

All in all, the independence of the Federal Reserve is likely to decline significantly. The Fed will probably ease monetary policy more than economic data justify. We expect it to lower its key interest rate to just 2.5% by the end of the year, which is significantly lower than the markets are currently pricing in. This points to a weaker dollar and higher bond yields.

Will Germany's economic recovery fail to materialize?

In the spring, the new federal government's financial package raised hopes in many quarters for a significant economic boost in Germany. However, as we feared, the necessary broad-based restart of economic policy did not materialize. This disappointment may explain why the Ifo business climate index fell for the second month in a row in December and why the purchasing managers' index for the manufacturing and service sectors also disappointed recently (Chart 2). Investors are now increasingly wondering whether the economic upturn in Germany will fail to materialize altogether.

Chart 2 - Leading indicators experience setback
Ifo business climate and composite PMI for Germany, seasonally adjusted monthly figures



Source: Ifo, S&P Global, Commerzbank Research

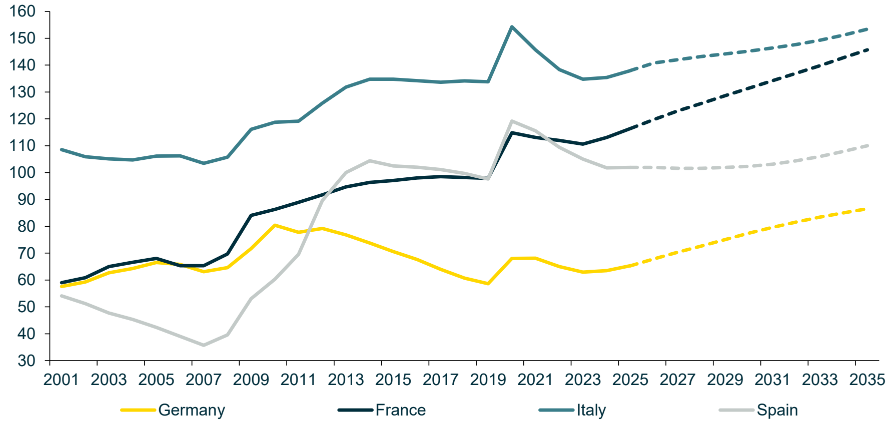
This view is certainly too pessimistic. After all, fiscal policy will relieve the private sector in 2026 by an amount estimated at 0.8% of gross domestic product. When a government spends that much money, some of it will stick with the economy. But the effect of the high fiscal stimulus also depends on business sentiment. In a recent **empirical study**, the RWI Institute showed that the fiscal multiplier, by which the above-mentioned fiscal stimulus (0.8%) is to be multiplied, is less than 1 when the future prospects of companies are clouded by disagreement among the governing parties. All in all, the growth forecasts of most economists (consensus: 1.1%) and of us (1.2%) are subject to downside risks.

Is there a threat of a sovereign debt crisis in the eurozone?

In the large eurozone countries, government debt is rising significantly faster than GDP (Chart 3). The budgets of many eurozone countries are being burdened by higher financing costs, rising defense spending, and unfavorable demographics. The government debt ratio in France is likely to rise particularly sharply because the political camps cannot agree on a significant reduction in the budget deficit, which was far too high in 2025 at a good 5% of GDP. In ten years, the country's government debt ratio could be almost as high as Italy's. In this respect, investors are repeatedly asking whether another sovereign debt crisis could break out in 2026.

No one can completely rule out such a crisis. However, it is unlikely because the EU and the ECB are likely to help highly indebted countries muddle through with numerous measures. For example, they are shifting new debt, such as that incurred to support Ukraine, to the EU level. The ECB is attempting to limit the rise in bond yields with a loose monetary policy. This is also served by its intention to hold large quantities of government bonds on a permanent basis. In addition, if push comes to shove, the ECB would buy government bonds from a member state in distress on a large scale as part of the so-called TPI program.

Chart 3 - Debt-to-GDP ratios are set to increase in the euro area
Government debt in % of GDP. As of 2025: Commerzbank forecast



Source: Bloomberg, Ameco, Commerzbank Research

What will happen if there is a ceasefire in Ukraine?

In 2025, Russia has conquered just another 0.8% of Ukrainian territory at the cost of heavy losses. Politically, however, things have gone better, as the US has largely withdrawn its support for Ukraine and is putting pressure on the country to accept at least some of Russia's demands. The chances of a ceasefire therefore seem higher than a year ago.

According to an estimate presented by the EU and UN in early 2025, the war has caused Ukraine direct damage amounting to $180 billion (about 100% of Ukraine's GDP, but only 1% of the eurozone's GDP). The total cost of reconstruction and economic/social support is estimated at around $524 billion over the next ten years, or just over $50 billion per year. Ukraine will be able to bear part of these costs itself. International support will come mainly from the EU; the US is unlikely to contribute any significant amounts.

Part of the demand could benefit European construction companies and exporters. However, in relation to the economic output of the eurozone ($19 trillion per year), this is unlikely to have any significant macroeconomic impact. But any ceasefire will probably have to be secured by European military forces. This, together with the continuing threat from Russia, also argues for high EU defense spending in the longer term. The scale of this spending will be significantly higher than the economic support provided to Ukraine.

A rapid resumption of trade with Russia is unlikely, especially as Europeans will not want to return to dependence on Russian raw material supplies.

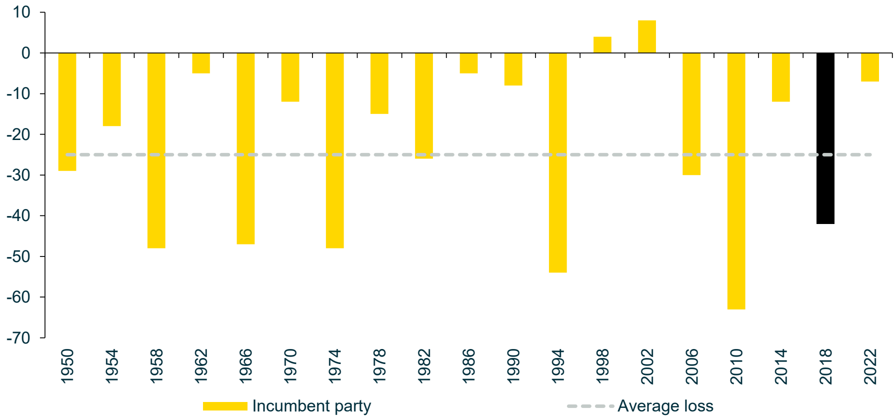
A ceasefire in Ukraine is likely to have only a limited impact on oil prices. The US could lift sanctions against Russia's two largest oil companies, but this would hardly bring significantly more oil onto the market, as Russia is bound by OPEC+ production targets and is already producing close to capacity. Furthermore, it is unlikely that the EU will ease sanctions and resume purchases of Russian oil.

Will the midterm elections lead to a change in policy in the US?

On November 3, midterm elections for Congress will be held in the US ("midterm" because they take place between the congressional and presidential elections in 2024 and 2028). All 435 members of the House of Representatives will be re-elected, as will about one-third of the 100 senators, who serve six-year terms.

The president's party usually loses seats in the House of Representatives in midterm elections (Chart 4). During Trump's first term, the Republicans lost 42 seats there. Currently, the Republican Party has only a razor-thin majority with 218 members. There is a high probability that the Democrats will be able to regain the majority they lost in the 2022 elections.

Chart 4 - President's party usually loses mid-term elections
House of Representatives, incumbent party, losses (-) or gains (+) of seats in the mid-term elections. Black column: midterms in President Trump's first term



Source: Office of the Clerk of the US House of Representatives, Commerzbank Research
A shift in the Senate majority in favor of the Democrats would be much more difficult. They would need to win a net total of four seats. Of the 35 senators up for election, 22 are Republicans. Most of them are in states that consistently vote Republican. This means that the Senate is likely to remain under Republican control.

It would become more difficult for Donald Trump to govern if the Democrats win one of the two chambers. After all, he also needs the approval of the House of Representatives for legislation. He could then rely even more heavily on executive orders. In general, the discussion about Trump's successor among Republicans will begin after the elections. The favorites at the moment are Vice President Vance and Secretary of State Rubio. Trump's predecessors had become "lame ducks" at this point in their terms, and no major policy decisions were made. All of this increases the risk that President Trump will focus on foreign policy, where he has a lot of leeway.

What foreign policy crises are looming?

Foreign policy crises have had a significant impact on government spending and the economy in general in recent years. There are no signs of a rapid calm in this area in the new year. In addition to the unresolved situation in Ukraine, there are other potential flashpoints:

- The US appears keen to swiftly implement the National Security Strategy published in November 2025. The arrest of the Venezuelan president at the beginning of the year is the first application of President Trump's expanded Monroe Doctrine, which aims to prevent foreign influence in the Western Hemisphere and ensure American dominance in this region. Greenland is obviously also part of this hemisphere. If the US were to take action here, NATO would be finished. In any case, the US wants to massively reduce its defense burdens in Europe, and Europe has been further downgraded in the US priority scale.
- China has once again stepped up its military maneuvers around Taiwan and increased political pressure on the island. Both China and the US, as Taiwan's protective power, should have a strong interest in avoiding escalation – and this is also emphasized in the aforementioned updated US security strategy. However, the situation is complicated by the fact that important regional powers such as Japan feel increasingly threatened by China's actions. Confrontations cannot be ruled out.

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