

WEEKLY ECONOMIC COMMENTARY

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The announcement of an extended ceasefire in the Middle East is welcome news. The accord, which is scheduled to be signed late this week, reduces a source of geopolitical uncertainty that has hovered over the global economy. But significant risks remain.

As of this writing, the full text of the agreement has yet to be shared. Reports suggest that the U.S. and Iran will drop their respective blockades, allowing shipping traffic in and around the Strait of Hormuz to resume. Iran will receive relief from sanctions on oil exports, and the release of some funding that has been frozen.

A 60-day cease fire will go into effect, during which time negotiations will continue over Iran’s nuclear program and the long-term security of maritime transit through the Strait. That window could easily be extended if negotiations are progressing. Few think that we will return to the kind of aggression that we witnessed in March and April.

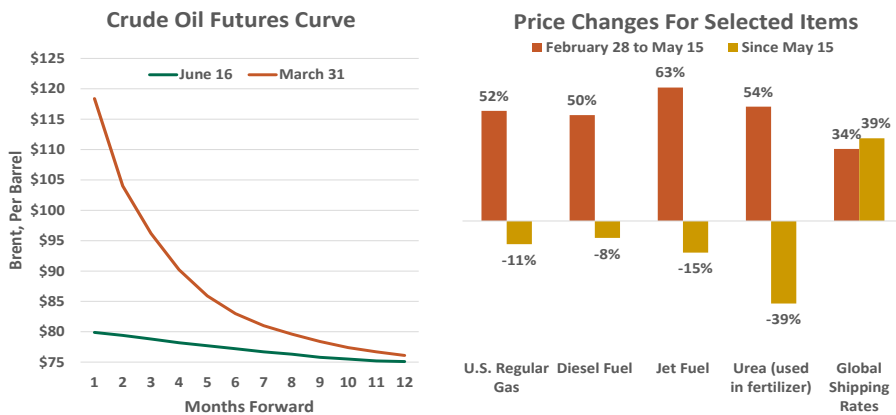
The agreement reduces global inflation risks. Oil markets are reflecting a much more benign outlook, and the prices of items disrupted by the war have begun to recede. Long-term bond yields have fallen, and the likelihood of interest rate hikes from major central banks has been reduced.

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Source: Bloomberg

All of that said, a return to normalcy may take time...and the old normal may never return. It will take a while to fully reopen the Strait; mines need to be removed, insurers need to gain comfort, and stalled oil, gas and fertilizer production needs to be restarted. According to Eurasia Group, it will take several weeks to re-establish 30%-50% of the pre-war traffic. Global shipping rates have continued to escalate, despite the truce.

Interested parties will be watching upcoming negotiations very closely. Having demonstrated an ability to close the Strait, Iran has a high asking price for conceding it. It

seems unlikely that shippers will be comfortable reestablishing prewar supply lines until there are more durable guarantees of their safety. The linkage of this topic to discussions over Iran’s nuclear program (which have proven very difficult in the past) complicates matters considerably. Israel’s patience may be tested if Iran is seen as dragging its feet to conceal its uranium.

Lingering uncertainty will lead energy consumers to have a long-term look at their sourcing. New pipelines may be built; new sources may be developed; and alternatives to fossil fuels will gain momentum. Demand for fuel from the Persian Gulf may never be the same.

Much as we might like to think that the war is over, a guarded posture is still recommended. Volatility is never far from the surface in the Middle East.

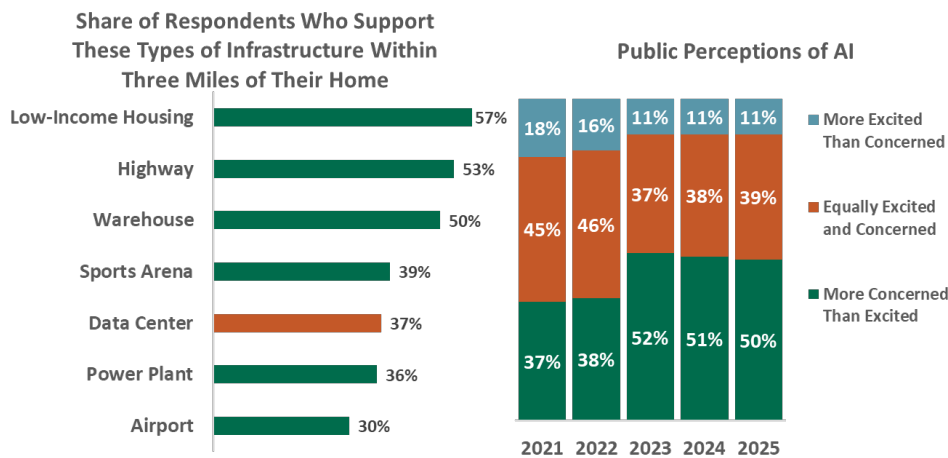
Double Secret Probation

At graduation ceremonies, audiences are often reminded to limit their audible reactions and hold applause, so that all graduates’ names can be heard. But a few viral videos this year showed a new disturbance to be managed: graduating students booing speakers if they extolled the virtues of artificial intelligence (AI).

This year has been marked by a shift in the perceptions of AI. The technology gained mainstream attention upon the public launch of ChatGPT in November 2022. For a few years thereafter, users explored the new capabilities, businesses set adoption strategies, and investors rewarded any firm with exposure to AI. But in the year to date, markets have grown nervous, security experts are on alert, communities are protesting, and students are rebelling.

New entrants to the labor force may see AI as competition, with good cause. Harvard University economists found a pronounced decline in junior-level job postings by firms who adopted AI, and for positions more exposed to AI. The trend emerged conspicuously in 2023 as ChatGPT took root.

The truce is welcome, but many issues remain unresolved.



Sources: Politico, Strategas, Pew Research Center

Macro risks around AI are on the rise. Anthropic found that its latest model, *Mythos 5*, could identify software security vulnerabilities with a speed and precision that far exceeded any human hacker. The model was previewed for only select institutions for research into its security. Last week, the company launched a scaled-back version, *Fable 5*, but it, too, was taken offline on orders from the U.S. government when it showed potential as a cyber weapon. Other AI firms are sure to launch models that can be used similarly; defending against them will be a tall order. A large-scale cyberattack could quickly undo any economic upside that AI adoption had promised.

Ethical worries are also mounting: AI-generated content lends itself to plagiarism, and AI-manipulated images have broken boundaries of consent and decency. Copyright and privacy laws were not designed to protect against the vast, indiscriminate data-gathering of AI models.

Citizens are organizing to protest new data centers, citing worries about noise, water and electricity consumption, along with limited economic benefit to communities that host these structures. Some of the sentiment may stem from seeing data centers as the embodiment of AI. Demand for AI capacity is rising, but data center limitations could become a barrier to growth.

Market enthusiasm has also found limits this year. Private credit lenders with software exposures have seen higher redemptions; publicly-traded funds have been challenged. AI dominance will require tremendous capital outlays, which is crowding out investment in other sectors.

The makers of AI models are not ignoring their disruptive potential. [OpenAI](#) and [Anthropic](#) have published policy frameworks to help governments deal with the potential economic fallout of an AI transition, especially lower employment. Their proposals include more funding for job retraining, more income relief programs, and investment in AI safety and education.

Current policy responses focus on immediate risks. President Trump signed an [executive order](#) (EO) for federal cybersecurity coordination and to encourage AI developers to share new models to evaluate their security. The EO makes participation voluntary, a change from a leaked draft that mandated pre-clearance. And as of April, [222 local governments](#)—across red and blue regions—passed laws to pause data center construction. Fourteen [statewide moratoria](#) have been proposed.

One of the best commencement speeches was delivered by a technology visionary: [Steve Jobs, at Stanford in 2005](#). In it, he reflected on his journey of embracing uncertainty: dropping out of college, getting fired, facing a health scare. The rise of AI is creating uncertainty for today's students, and they are expressing their frustration. Hopefully, Jobs' message that good things can emerge from challenging times will ring true for the class of 2026.

At A Crossroads

The 2026 FIFA World Cup is a celebration of North American teamwork. The United States, Mexico and Canada are sharing the stage, dividing the schedule across 16 cities, and presenting themselves as partners in a vast continental stage.

That image of coordination is striking because, off the pitch, the region's most important partnership may enter a far less harmonious phase. Just as the three co-hosts welcome the world together, the United States-Mexico-Canada Agreement (USMCA) is heading into its first mandatory joint review on July 1. The agreement does not expire if it is not extended; instead, it sets off annual reviews, and can remain in force for up to a decade unless one country formally exits. That reduces the odds of a sudden collapse, but not the stakes surrounding the negotiations.

The review process can broadly evolve along three paths. The first is that the pact is preserved with limited changes. This would restore policy clarity and maintain broad market access. While still possible, this outcome looks less likely given the U.S. administration's stance.

The second, and the most plausible, is a status quo with no formal renewal, triggering annual reviews. In this case, the agreement stays in place, and many USMCA-compliant goods continue to move without much friction. While it would retain current terms, recurring negotiations would insert uncertainty in the system. Sector-specific issues will return to the forefront repeatedly.

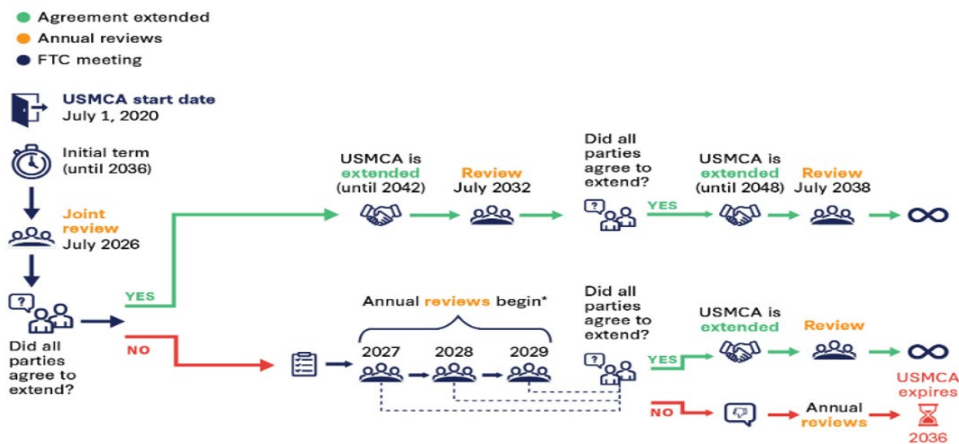
The third, worst-case scenario is a breakdown, where one or more parties ultimately step away.

Public pushback on AI may limit its potential.

That would mean a loss of exemptions, higher tariffs, and disruptions to deeply integrated supply chains built over decades. While outright termination of the USMCA during this review cycle remains unlikely, uncertainty alone could prove to be nearly as damaging as a full rupture for future business, trade and investment plans.

For the U.S., the review is about reducing trade imbalances and aligning trade policy with industrial strategy. America’s trade deficit with Mexico stood at over \$200 billion in 2025 and just above \$50 billion with Canada. Policy is increasingly also tied to strategic competition, particularly with China.

USMCA Review Timeline



Source: CSIS

Rolling annual reviews could prove as disruptive as a formal rupture.

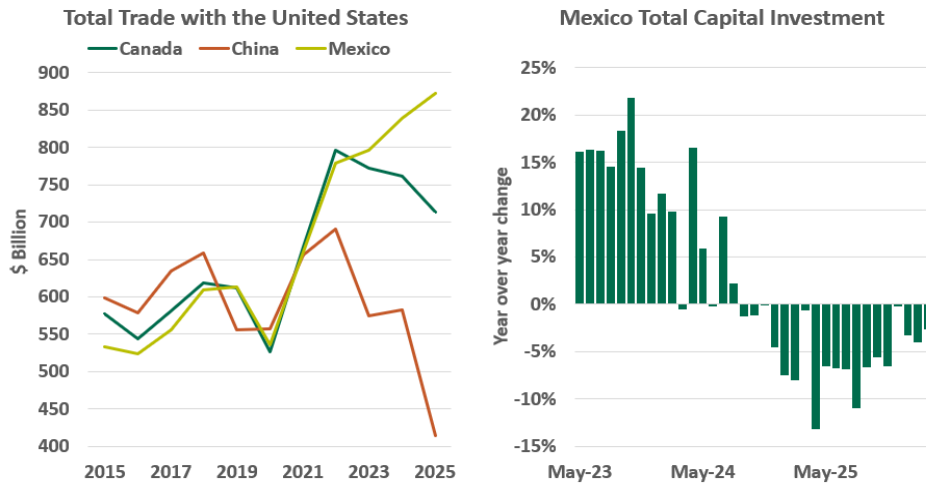
The auto sector remains at the center of discussions. The U.S. administration is pushing for new vehicles to contain at least 50% American content to qualify for tariff-free treatment, as it seeks to reshore production and jobs. Since both Canada and Mexico rely heavily on imported products, including from China, concerns about transshipment and indirect market access are likely to feature prominently in negotiations.

For Mexico, trade with its northern partners accounts for 44% of GDP, with total USMCA trade exceeding \$800 billion. The country is highly dependent on U.S. demand, which absorbs 83% of its exports. The agreement has broadly worked in Mexico’s favor, supported by lower labor costs, a deep manufacturing base and proximity to the U.S. market. Mexico has strengthened its position as a hub for assembly and integration within regional supply chains, including in technology-linked sectors. A stable USMCA framework would reinforce this momentum.

Canada’s dependence on the U.S. market remains substantial, with about 77% of its goods exports heading south of the border. While Canada still enjoys preferential access, that edge is eroding as the rules evolve. The country’s strengths lie in its resource base like energy, agriculture and critical minerals, where it remains strategically important. However, its footprint in next-generation industries is relatively limited. As U.S. demand increasingly tilts toward electronics, AI-driven supply chains and advanced manufacturing, Canada risks being underrepresented in the fastest-growing segments of commerce.

Canada and Mexico would bear the larger direct burden from any USMCA disruption given their dependence on U.S. trade. Reduced market access would hit export growth, manufacturing employment and investment flows. Mexico, already under strain, lost 300,000 auto sector jobs last year and has seen 19 straight months of negative total investment. Wary of jeopardizing the trade pact, it has raised tariffs on a wide range of Chinese imports, including steel and electric vehicles.

Trade uncertainty is already weighing on Canada. Its exports base is concentrated in sectors such as autos, metals, machinery and wood products. This leaves it exposed to targeted tariffs, tighter content rules and shifting policy discretion. Even without a breakdown of USMCA, there is risk of a gradual loss of market access. Efforts to broaden trade ties to countries like China risk adding friction to an already sensitive negotiating dynamic with America.



Sources: CATO Institute, Bloomberg, Mexico's National Statistics Agency

Without USMCA renewal, North America's competitive edge will gradually erode.

American firms will not be immune. Canada and Mexico account for roughly one-third of U.S. exports, with shipments to the two countries up 56% since USMCA took effect in 2020. U.S. producers are deeply rooted in North American supply chains, particularly in autos, machinery and agriculture. Stricter domestic content requirements in autos would likely push prices higher. New U.S. vehicles already average more than \$51,000; costs would climb further if tariff burdens were passed through more fully. A prolonged period of policy uncertainty or more complex rules would raise production costs and risk weakening export demand for U.S. firms.

Even in the baseline scenario, where the agreement persists but shifts to annual reviews, costs will accumulate. Investment decisions would be delayed or scaled back, because its durability is in question. Over time, this would weigh on productivity and weaken the region's competitive edge.

The ongoing World Cup showcases three countries working together. The USMCA review will reveal whether that cooperation extends beyond sport. A shared platform can continue to deliver strong outcomes, but only if the rules remain clear, stable and broadly accepted.

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