



By the Confluence Macroeconomic Team

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## Geopolitical Outlook for 2026

In mid-December, we publish our geopolitical outlook for the upcoming year, as is our custom. This report is less a series of predictions as it is a list of potential new geopolitical issues that we believe will dominate the international landscape in the coming year. It should also be noted that some of these issues may be important only in 2026, while others will extend beyond. The report is not designed to be an exhaustive list. Instead, it focuses on the big-picture conditions that we believe will affect policy and markets going forward. The issues are listed in order of importance.

### Issue #1: Stablecoins to Support Use of the US Dollar Abroad

Stablecoins are cryptocurrencies designed to hold a stable value relative to a fiat currency. That makes them different from other cryptocurrencies, such as Bitcoin and Ethereum, whose values can fluctuate wildly. Stablecoins were initially used to offer holders of traditional cryptocurrencies an “off-ramp” from their cryptocurrency holdings. If a cryptocurrency holder liquidated his or her position and returned to the traditional financial system, that holder would be exposed to the regulation of that particular financial system. In other words, if a cryptocurrency position, which is pseudonymous, is liquidated and the proceeds end up in a bank account, that transaction would no longer be anonymous and thus would likely be subject to tax. By moving into stablecoins, the position would remain pseudonymous, avoid regulation, and

not be subject to the volatility of traditional cryptocurrencies.

This doesn’t mean that stablecoins are without risk. The [collapse of TerraLuna](#), a stablecoin that was backed by a derivative scheme, raised concerns about the stability of stablecoins. Currently, the two largest stablecoins — Tether’s USDT and Circle’s USDC — mostly back their issuance with short-term United States dollar assets, such as bank deposits or Treasury bills (T-bills). However, there is no regulator for these stablecoins, and in the past, concerns have been raised about the actual backing of these coins. Tether, for example, has [refused to perform an audit](#) of its holdings.

After years of skepticism about cryptocurrencies, in general, and stablecoins, in particular, the US government reversed course in July 2025 and embraced the technology by signing the [GENIUS Act](#) into [law](#). The act creates a regulatory framework that should reduce the risk of holding stablecoins. Under the law, only banks, approved non-banks, or entities qualified by a state can issue stablecoins. An approved issuer can choose either federal or state oversight, but those using the latter are subject to a \$10 billion cap. The law also requires issuers to maintain a 1:1 backing of issued stablecoins with US currency, bank reserves, short-term Treasuries, or similar liquid assets. Finally, the law requires [stablecoin issuers to conduct monthly examinations of reserves, which are to be analyzed by a registered public accounting firm, and provide an annual audit of financial statements for issuers with more than \\$50 billion of outstanding stablecoins](#).

Importantly, the law also states that stablecoins can't pay interest.

In our view, the primary economic and geopolitical issues arising from the emergence of stablecoins are as follows:

- Stablecoins are expected to increase the demand for Treasuries.*** The Brookings Institute has created a table<sup>1</sup> that projects T-bill demand based on the annual growth rate of dollars held abroad and the stablecoin penetration rate. US dollar holdings abroad are currently growing by about 7% per year, while stablecoin penetration is about 2%. If nothing changes, this suggests that T-bill demand from stablecoins will rise to \$421 billion by 2030. However, if the 7% growth rate remains stable but stablecoin penetration rises to 20%, then demand for T-bills would rise to about \$4.2 trillion. Stablecoins therefore have the potential to be a significant new source of demand for Treasuries, replacing the foreign central bank demand lost due to Washington's aggressive use of financial sanctions. The [BIS reports](#) that stablecoins were the third largest buyer of T-bills in 2024. This source suggests that stablecoin flows led to a 5-bps decline in T-bill yields over a 25-day period from issuance.
- The US dollar is the most common denomination for stablecoins, by far.*** The [BIS reports](#) that over 68% of stablecoins are USD denominated. Taking into account market capitalization, that figure is nearly 99%.
- Most of the demand for stablecoins is coming from countries with unstable financial situations.*** A [study from 2022](#) found that cryptocurrency use increases with corruption and capital controls. Countries such as Argentina and [Venezuela](#), both dealing with currency instability, high inflation, and political instability, are increasingly using various forms of cryptocurrencies in order to protect purchasing power.
- Another factor is the use of stablecoins in foreign remittances.*** It is common for immigrants to send money home to help their families. The World Bank estimates that global remittances represent [just over \\$900 billion in flows](#). Until the advent of stablecoins, remittances either went through the banking system or transfer agents, e.g., Western Union. The banking system requires banking relationships (deposit accounts, wire transfers), which are not attractive to many migrants, either because they are undocumented and can't open such accounts or the fees are prohibitive. Transfer agents can generally handle smaller transfers and can be semi-anonymous, but they often come with [high fees](#). Stablecoins, on the other hand, require only a smartphone and access to a crypto exchange.
- Foreign governments are concerned that stablecoins denominated in US dollars could undermine their monetary sovereignty.*** As noted in the third bullet point above, dollarization in nations with unstable financial conditions can be facilitated by stablecoins. However, even developed-economy [financial authorities are expressing concern](#). To understand why, consider that when the eurozone was facing financial stress in 2011, Switzerland saw inflows that disrupted its financial system. At the time, there

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<sup>1</sup> [https://www.brookings.edu/wp-content/uploads/2025/10/The\\_Rise\\_of\\_Stablecoins\\_and\\_Implications\\_for\\_Treasury\\_Markets\\_Davidovic\\_Ghani\\_Moszoro.pdf](https://www.brookings.edu/wp-content/uploads/2025/10/The_Rise_of_Stablecoins_and_Implications_for_Treasury_Markets_Davidovic_Ghani_Moszoro.pdf), page 12.

were concerns that some of the southern European nations might not be able to remain in the eurozone, and investors sought safety in Switzerland. USD stablecoins could be an alternative to such flows that would be simple to implement.

- ***The US and China are likely to establish a binary global currency order, with the US system based on USD stablecoins and China operating a gold-settled payment system.*** Over the past couple of years, China has been aggressively accumulating gold. It has also established a gold exchange in Shanghai. China does not appear to have any interest in creating a fiat-based reserve system to rival that of the US. This is likely because (a) it intends to maintain capital controls, and (b) it has concluded that such systems lead to deindustrialization, using the example of the United States. The primary benefit to the USD stablecoin regime is flexibility; the US can create dollars to expand with global trade. Since the expansion will mostly be funded with short-dated Treasury debt, the stablecoin would also give the US fiscal flexibility. The evolving Chinese system would have the benefit of the stability that gold offers, but the problem is that gold supply isn't infinite. However, China could offset this issue by allowing gold to steadily appreciate, thus increasing the purchasing power of gold holdings.

So far, foreign nations are responding by accelerating the process toward the issuance of central bank digital currencies. This decision does give holders the efficiency of the blockchain, but it doesn't address the currency stability issue. In other words, when a nation faces currency instability (e.g., Argentina, Venezuela), households and businesses would find little solace in holding

the digital currency issued by their respective central banks compared to holding dollars. Short of capital controls, which cryptocurrencies can often evade, it will be difficult to prevent dollarization.

The primary market ramification is that stablecoins have the potential to represent a new source of dollar demand, which could boost the dollar's exchange rate. Dollar appreciation will probably not be an issue in 2026 since the stablecoin infrastructure won't likely be fully established in that time frame. But longer term, a stronger dollar is a factor that will need to be addressed.

— BOG

## **Issue #2: China's New Aircraft Carrier and Spheres of Influence**

China recently commissioned its third aircraft carrier, the *Fujian*, which displaces 80,000 tons. This represents a major improvement over its first two, smaller carriers, which displaced 60,000 and 70,000 tons, respectively. That difference may seem insignificant, but it suggests that the *Fujian* will be able to carry twice as many aircraft (around 75) compared to the two earlier carriers. Also, the previous carriers relied on "ski-jump" decks to launch aircraft, which is a primitive technology that limited the ordnance that planes could carry.

The earlier vessels could only deploy the J-15, a relatively small, less capable fighter jet. Even worse, without catapults, the J-15 could not take off with full fuel and weapons capacity, limiting its range and strike capacity. Constrained by the lack of a catapult, the J-15 could not actually defend the carrier. In contrast, the *Fujian* sports state-of-the-art electromagnetic catapults that can launch heavier aircraft. Because of this, China's 5<sup>th</sup>-generation J-35 fighter jet can deploy from the carrier with a full complement of fuel and weapons.

The ski-jump layout of China's earlier carriers is also much less efficient. Generally speaking, those ships can only launch about 40 sorties per day. That's far less than the *USS Gerald Ford*, the US's latest, state-of-the-art carrier with electromagnetic catapults, which can facilitate at least 100 sorties per day. It is expected that the *Fujian* will be much closer to the performance of the Ford-class carrier.

In theory, the *Fujian* should give China power-projection capabilities beyond the first island chain. In practice, however, the *Fujian* probably can't operate much past the second island chain. Unlike US carriers that are nuclear powered, the *Fujian* is diesel powered, which limits its range. China is investing in "[oilers](#)" to address this factor. Another issue is that in wartime conditions, which involve higher speeds and evasive maneuvering, the fuel constraint could prevent the *Fujian* from giving China a true "blue water" capacity.

Perhaps the larger question is to what end is China investing in aircraft carriers? China has written the playbook on access denial. It has developed land-based anti-ship missiles, the DF-21D and the DF-26. The former is a medium-range missile with a range of 330 miles, while the latter has a range of 2,400 miles. It has also developed the YJ-21, a hypersonic anti-ship ballistic missile that can be launched from either sea or air. If China has created weapons designed to reduce the effectiveness of aircraft carriers, it seems illogical then to spend the money to build them as part of its own blue water navy. Aircraft carriers are not only expensive, but they also don't travel alone — an array of support and protection vessels accompany these ships.

Furthermore, history shows that naval arms races are destabilizing. The naval buildup of

the US, Japan, and Germany against the incumbent UK at the turn of the last century was a factor in two world wars.

We see two ways in which this investment in carriers could potentially make sense. First, given China's massive industrial capacity, Beijing may simply believe it can outbuild the US in a major naval war. Given the [degraded state of US shipbuilding](#), this might be a reasonable assessment. However, the US has a much longer history of being a major naval power, and China could find itself fighting a competitor that can inflict damage at a rate even China can't recover from.

But there is a second, perhaps more logical reason. If the US and China are facilitating a "sphere of influence" world, where China dominates the Far East, then it would be a rational course of action to expand its fleet to ensure carrier availability for enforcing its regional will and maintaining open sea lanes (something the US would no longer do in such a world). In other words, aircraft carriers may no longer be an effective weapon against another superpower but are still quite effective against lesser powers.

Although it is clearly too early to tell which path the US and China will take, a potential naval arms race clearly supports heavy industry and the defense sector.

— BOG

### Issue #3: The US Adopts a Modern Monroe Doctrine

In 1823, the United States issued the Monroe Doctrine, which warned European powers that the Western Hemisphere was closed to future colonization. Any interference in the newly independent states of the Americas would be treated as a hostile act. Although the doctrine was conceived as a defensive measure, it quickly became a

foundation for US regional dominance. While Washington has not formally revived the doctrine this year, the current administration has markedly expanded its diplomatic and economic engagement with Latin America in an effort to counter growing Chinese influence, therefore reviving the doctrine in spirit.

Latin America's proximity makes it a priority for US national security planners, who view Chinese activity in the region as a strategic risk. Beijing has steadily deepened its ties with Latin American countries — especially those with left-leaning governments — through investment, trade, and political outreach. In response, the Trump administration has leaned toward cultivating relationships with right-leaning parties, viewing them as more aligned with US economic and geopolitical interests.

This strategy has been most visible in US economic support for friendly governments. [Argentina, under Javier Milei, received a dollar swap line and a reserve-depletion guarantee](#) intended to bolster its stabilization program. The administration has also advanced preferential trade arrangements with [Argentina, El Salvador, and Ecuador](#), offering relief from inflationary pressures while reinforcing their alignment with Washington.

In contrast, the US has taken a tougher stance toward governments perceived as “less aligned.” Venezuela is the most prominent example as several of its vessels have been [targeted for suspected narcotics activity](#), and the administration has repeatedly signaled the possibility of stronger measures. These actions have drawn concern [from neighboring Colombia](#). Brazil has also faced higher trade tariffs amid US allegations that it [acted against the interests of former President Jair Bolsonaro](#),

a close ideological ally of the current administration.

The key difference between the original Monroe Doctrine and the current approach is that Washington has not explicitly demanded that China reduce its presence in South America. Instead, US efforts aim to shift the incentives facing regional governments by pressuring them, directly or indirectly, to limit strategic reliance on Beijing. While left-leaning governments may seek constructive ties with the US, as [demonstrated by the relaxing of tariffs on Brazilian beef and coffee](#), any such relationship is now likely to encounter heightened scrutiny.

In sum, Washington's new focus on stronger engagement and influence in Latin America is consistent with the theory that it wants a US sphere of influence in the Americas. Looking ahead to 2026, Latin America may offer compelling opportunities for investors seeking international exposure. If the US continues to support right-leaning, market-oriented governments in the region, these countries could become increasingly attractive. Many favor deregulation, fiscal discipline, and private sector-led growth, which are policies that may be further reinforced by preferential trade terms or financial backing from Washington.

— TW

#### **Issue #4: The US Makes Its Move in Central Asia**

In August, [President Trump announced](#) he had brokered a peace deal between Armenia and Azerbaijan. These two former Soviet states had been in some level of conflict since 1988. A critical conflict point was [Nagorno-Karabakh](#), a region claimed by both sides. After several years of conflict, Armenia took control of the region and held it until 2020, when Azerbaijani troops

reestablished control. Azerbaijan then expanded its control to regions surrounding Nagorno-Karabakh during the next couple of years.

Armenia had petitioned Russia, its ally, for protection. However, Russia was preoccupied with Ukraine and took only modest steps to support Armenia. In that vacuum, President Trump intervened with a peace proposal that was accepted by both sides. As part of the deal, a new transit route, called the Trump Route for International Peace and Prosperity, was established, with the US getting development rights for the next 99 years. The route is expected to facilitate the development of oil and gas pipelines, fiber optic lines, rail lines, and perhaps electricity transmission.

Then in early November, President Trump met with the [five leaders of the Central Asian nations](#) (“the ‘stans”) to develop economic and security relations. Pictures of these leaders meeting at the White House were clearly unwelcome news in Moscow, Tehran, and Beijing. These regions have generally been considered to be in the orbit of Russia and China, with some influence from Iran as well. This isn’t to say that the area hasn’t been disputed historically. In the 19<sup>th</sup> century, the [British and Russian empires](#) attempted to gain influence over this region. Russia’s invasion of Georgia in 2008 was mostly due to fears in Moscow that NATO was considering accepting that nation into its defense treaty.

Overall, we doubt the US will be able to expand its influence significantly in the region, but it is a point of leverage for Washington. With Russia preoccupied with Ukraine, China worried about Taiwan and the first island chain, and Iran reeling from direct attacks by Israel and the US, the bandwidths of these nations are currently a

bit narrowed. And so, the US is giving these nations “something to think about” and perhaps earning some leverage in ongoing talks.

From a market perspective, if the US is able to develop commercial relationships with these Central Asian nations, it could increase supplies of valuable raw materials. Although we doubt the US can maintain control over the long run, it could ease supply constraints in the near term. — *BOG*

### **Issue #5: Deregulation in Europe**

As the US and China work to build their spheres of influence along their own idiosyncratic visions, and as Russia continues its aggression against Ukraine, European leaders will likely feel increasingly isolated and vulnerable in 2026. Therefore, they probably won’t be content to just focus on rebuilding their military capabilities. We think they will also focus on rejuvenating their economic growth to help generate the resources needed for defense and ensure political stability. Since recent high-level analyses have focused on the need for more investment and liberalized business activity, European officials have started to deregulate the region’s economy, and we expect that effort will deepen in the new year.

Nascent signs of deregulation are already evident in Europe. [In November 2025, for example, the European Commission said it would ease its onerous rules on artificial intelligence and other technologies to spur innovation.](#) In May 2025, Brussels said it would further delay new rules on banks’ trading businesses to ensure the institutions can compete with newly deregulated US banks. Most telling, the Commission and the European Parliament have taken steps to roll back or slow EU regulations related to

climate change and environmental protection.

Importantly, there is a new political dynamic behind this deregulatory effort, especially in the European Parliament. Until recently, the parliament's centrist political groups (akin to parties in a national legislature) had committed to a *cordon sanitaire* policy of not cooperating with the far-right groups, even as those factions grew in electoral power and gained more seats. In 2025, the dominant center-right party, the European People's Party, abandoned this policy and refused to cooperate several times with the main center-left party, instead relying on far-right groups to pass laws watering down the EU's energy and environmental laws.

With the taboo of working with the far-right now broken, and with the far-right continuing to gain voters who oppose many regulations, we suspect the "rightist" alliance will keep working toward dismantling EU business rules. Along with the EU's increasing embrace of fiscal and monetary stimulus, this deregulation trend has the potential to help spur faster economic growth in the region and give a further boost to European stocks. If this trend advances as we think it will, it could be especially beneficial for European industrial stocks. — PFH

#### **Issue #6: Data Centers Going Global**

As artificial intelligence (AI) becomes mainstream, the US and China are locked in a global contest for technological dominance. This rivalry is increasingly expressed through the construction and financing of data centers and related AI infrastructure abroad as both powers work to entrench their proprietary technologies and standards. This strategy — often described as technological colonialism — has become a defining tool of modern power projection.

The rapid spread of AI is inseparable from the explosive growth of data centers, the essential engines that supply AI's massive computational needs. These facilities underpin cloud computing and process the enormous datasets that make modern AI possible. Yet their heavy consumption of energy, water, and land has created major logistical and environmental strains. In response, leading nations are pursuing a dual strategy: scaling up domestic capacity while aggressively expanding overseas to secure the resources and geopolitical leverage necessary to maintain a competitive edge.

China has anchored its domestic build-out in the ["East Data, West Computing" initiative, launched in 2022](#). By shifting data centers to the country's more resource-rich western regions, Beijing aims to tap cheaper energy and ease congestion in the industrialized east. China is also experimenting with underwater data centers as a next-generation solution to their cooling demands.

Across the sea, the US is undertaking its own sweeping expansion. Through various [initiatives, such as "Stargate," the White House is partnering with leading technology firms](#) — including OpenAI and other major industry players — to accelerate data center development across the country. The administration is also supporting complementary projects aimed at expanding low-cost energy supply and limiting regulatory burdens for fast-growing AI companies, mining firms, and energy providers.

This competition has now spilled far beyond domestic borders. Washington has explored data center development in key allied nations such as [Canada](#), the [UAE](#), the [UK](#), and [the EU](#). Meanwhile, Chinese tech giants — including [Huawei](#), [Tencent](#), and [Alibaba](#) — are extending their footprint into Mexico,

Brazil, Southeast Asia, and the Middle East. Each new facility deepens geopolitical ties, embedding host nations more firmly within either the US or Chinese technological ecosystem.

The global race to build data centers is poised to shape the future of geopolitical influence. As more countries become nodes in this expanding infrastructure map, they will face increasing pressure to align with one of the two superpowers. Ultimately, the decisive factor may not be which nation leads in technical capability, but which can forge the strongest, most dependable web of international partnerships.

Looking ahead to 2026, momentum points toward even broader global expansion. Investment will flow into two primary arenas: strategic allies, where the US seeks to solidify its technological sphere of influence, and resource-rich emerging markets, whose abundant energy supplies are vital for powering the next generation of AI-driven infrastructure. — TW

### **Odds & Ends**

Now that its punitive 2025 tariffs are in place, the US will likely focus on finalizing new bilateral trade agreements with a range of major commercial partners in 2026. With *fewer surprise tariff hikes from the US*, policy uncertainty will ease, and countries and companies will be able to settle into new trading patterns. That's likely to prompt a rebound in global trade flows, capital flows, and investment.

As the US and China continue working to build their spheres of influence and begin to better appreciate that their comprehensive power is now essentially equal, the two nations could reach a *“grand bargain”* in which they recognize each other's interests, pledge non-interference in their respective

spheres, and find a way to live together with much less rivalry. The resulting decline in global geopolitical tensions would likely be bullish for US and Chinese stocks, as well as the emerging markets, but could be short-term bearish for assets such as precious metals.

Finally, *Russia and Ukraine* are likely to continue fighting for at least much of the year, but they will still inch toward a peace agreement under further pressure from the US. As part of its pressure campaign, the US is likely to continue its disregard of many European interests, further weakening the traditional US-European alliance.

### **Investment Implications**

Many of the investment implications discussed above are consistent with what we've been arguing for the last few years. Although stablecoins could eventually boost dollar demand and strengthen the greenback, the currency looks set for a period of weakness in the immediate term, which should give an advantage to foreign stocks versus US stocks. A potential naval arms race involving the US and China would buoy defense firms and broader industrials, but the better defense and industrial opportunities will probably be in Asia and Europe. Meanwhile, US-China tensions and global fracturing will likely support key commodities, such as gold and critical minerals, and those firms that produce them.

In sum, as global fracturing takes root, we continue to see multiple ways in which the global investment environment is changing compared to how it looked in the three decades of globalization after the Cold War.

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