

Why the economy in 2026 will be more resilient than many think

BMO  Private Wealth



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After a year of seemingly constant market and economic uncertainty, investors might assume we'll see more of the same this year. But the past 12 months actually showed something different: the global economy is far more resilient than many give it credit for and that should give investors reason for optimism in the year ahead.

That was the message from the BMO Private Wealth 2026 Year Ahead Outlook panel featuring:

Douglas Porter, CFA, Managing Director and Chief Economist, BMO Financial Group

Jennifer Lee, Managing Director and Senior Economist, BMO Capital Markets

Brent Joyce, Chief Investment Strategist, BMO Private Wealth

Tom Powell, Vice President & Market Leader, BMO Private Wealth (Moderator)

The panel explored the most pressing economic issues, including the growth outlook for the Canadian and U.S. economies, what's next for global trade in a post-globalization world and what it all means for markets. Here's a breakdown:

Tariffs take less of a toll

It's almost a year ago that Canada's trade relationship with the U.S. began to shift, with our largest trading partner threatening a 25% tariff, then a 35% tariff, on everything flowing south of the 49th parallel. In hindsight, the tariffs proved much narrower than many expected, Douglas Porter explained. "There are only a few certain industries that are being affected by tariffs," he said. "They are important industries, but it's only a few that are really being targeted."

Most goods are tariff-free because they qualify under the CUSMA exemption. When you look at it in the context of the automotive sector, a typical vehicle crossing the Ambassador Bridge is paying a tariff of roughly 12% to 13%, he explained. While Porter said that's still "really serious business," the overall tariff is still lower than what the U.S. has applied to other trading partners.

There is a lot of anticipation for the pending U.S. Supreme Court ruling on whether the U.S.'s so-called emergency tariffs are legal, but Porter downplayed the significance of the decision. He noted that tariffs on steel or aluminum are separate from the ones before the court, meaning they will continue to put pressure on Ontario and Quebec. And while the decision could constrain the U.S. president, Porter believes the administration has many alternative options ready to put something similar in place.

Still, the North American economy dealt with the tariff headwinds fairly well. Porter noted that it was a challenging year, with the Canadian economy growing slightly below average, yet we avoided a recession. The U.S., meanwhile, had slightly above-average growth last year.

One reason for the difference in growth rates is the limited impact of the tariffs on U.S. consumption. While the U.S. has argued that foreign exporters are footing the bill for the tariffs, retailers and American consumers also bear some of the cost. For their part, foreign suppliers are lowering prices to keep their goods flowing into the States.

Global economy remains resilient

It wasn't just the North American economies that came through the past year relatively unscathed; the global economy was also quite resilient, said Jennifer Lee, for several reasons. For starters, amid the uncertainty, many countries started looking for ways to diversify their economies, she said.

While Europe acted swiftly to sign a new trade deal in principle with the U.S., leaders in the region now recognize they can't rely on America to further diversify their trade. The EU has since signed two new deals, one with India and another with the Mercosur bloc. Europe is also taking steps to wean itself off Russian natural gas by 2027.

The decision by both the U.S. and China to tone down their rhetoric was another factor. Specifically, Lee pointed to May 12 last year when the two nations reversed their extreme tariff proposals. On that day, the U.S. walked back its plans to impose a 145% tariff to 30%, while China responded by lowering its tariff on the U.S. from 125% back to 10%.

"Those are good tailwinds for 2025 and going into 2026, assuming that a lot of this stuff holds of course," she said.

Inflation and interest rates to stand pat

Normally, in a market outlook, Porter said inflation would be at the top of his presentation. Although inflation has been the big story in recent years, now that it's almost back to normal, he said it's less of a headline story. That theme will influence interest rate policy for 2026.

The Bank of Canada expects inflation to be close to its 2% target. While Porter said BMO expects it could be closer to 2.5% – driven largely by higher food costs – he believes the central bank will hold rates through the rest of the year. "That's not at all unusual," he said. "In fact, at one point in the last decade, they didn't change rates for a five-year period of time. So, it's entirely believable that the bank will just sit out this year."

As for the U.S., BMO expects the Federal Reserve will cut rates three times this year, narrowing the interest rate gap with Canada. Those rate cuts are expected to contribute to a weaker U.S. dollar against most global currencies this year.

Market to continue improving

The resilience in the economy helps explain the continuation of the bull market in North America. As Brent Joyce explained, investment in AI has been the headline story for much of the past year. Still, in 2026, there may be scope to explore opportunities outside of the technology sector, especially the so-called Magnificent Seven.

Not to diminish the potential of the big tech stocks, which continue to have an attractive profile with little debt, Joyce says the other 493 companies on the S&P 500 are trading at more reasonable prices. "We want to have exposure to some of these phenomenal large corporations, but we don't want to get over exposed to them," said Joyce. "Going forward, we think there are opportunities beyond the largest names and look to have exposure down the market capitalization spectrum, including small and mid-cap companies."

For the U.S. market, Joyce expects the S&P 500 to reach 7,400 this year (as of January 30, the major American index was around 6,950). For Canada, he sees the market returning about 9% this year.

But after a three-year bull market, does the market really have legs? Joyce is convinced it does. "Everything here is suggesting that this is a normal garden variety bull market that is only middle-aged and certainly has plenty of further room to run," he said.

"We need to control our emotions and our time horizons and our risk tolerance to navigate through them, because the bull markets, like the one that we're currently in, create vastly more wealth and last longer than the bear markets that are very painful and cause some scars, but are less frequent and much shorter."

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