



## EDMOND DE ROTHSCHILD ASSET MANAGEMENT

### MARKET FLASH: THE PATH TOWARDS REOPENING THE STRAIT OF HORMUZ IS GETTING NARROWER AND NARROWER

- **Mojtaba Khomeini's appointment as Iran's supreme leader marked another notch higher in Middle East tensions.**
- **Last Monday, Donald Trump claimed US operations in Iran had already made significant progress and that they could end soon.**
- **China, meanwhile, is still in remarkable export health.**

**Mojtaba Khomeini's appointment as Iran's supreme leader marked another notch higher in Middle East tensions. Missiles have targeted oil infrastructure both in Iran and in some neighbouring countries. Traffic through the Strait of Hormuz, a strategic passage for global oil supplies, has slowed and some observers claim it has practically stopped. 20 million barrels use this passage every day, around a fifth of global consumption estimated at 100 million b/d. Several regional producers have tightened the noose even further: Iraq reduced oil production and Kuwait and the UAE quickly followed suit. Unsurprisingly, Brent crude prices soared, initially hitting \$120 before falling back to around \$100 as fears of a new oil shock returned. The IEA said 400 million strategic oil barrels would be released to ease supply tensions.**

**Washington has not yet re-deployed systematic escorts for tankers in the Strait of Hormuz but is actively seeking to prevent Iran from laying mines in the zone. Last Monday, Donald Trump claimed US operations in Iran had already made significant progress and that they could end soon. The US is considering using strategic oil reserves and easing some Russian oil sanctions to create a temporary energy firewall. This week's US Energy Information Administration report said inventories had risen further to 3.8 million barrels. The oil shock comes at a tricky moment for the US economy. January retail sales slipped 0.2% in value and by 0.3% in volume due to bad weather and persistent weakness in car sales. And the Fed is increasingly exposed to stagflation risk as inflation might start to trend higher while the labour market looks to be slowing.**

**China, meanwhile, is still in remarkable export health. The trade surplus for February hit \$213bn. Dollar exports jumped 40% over a year while imports were up 14%. Beijing, however, decided to suspend exports of refined oil products, a move which only exacerbated tensions on a market already reeling from Middle East events.**

**For Europe, higher energy prices risk fuelling inflation and reducing growth. ECB chair Christine Lagarde was keen to say today's situation is not like 2022 and that patience was in order. The ECB is holding off before mulling a new rate hike cycle. And yet markets are now expecting rates to rise twice before the end of 2026. The Bank of England could pause its rate cuts to keep some leeway as uncertainty returns in force.**

**In Japan, wage discussions are starting to have an effect. In January, in companies employing more than 30 people, they rose by an annualised 3.2%, the largest increase in a year. This development reinforces the case for the Bank of Japan to increase rates again. As in the eurozone, markets are factoring in two rate rises this year to 1.25%, a move that will defend the yen.**

**In today's environment, safe haven currencies are once again in favour. The US dollar is up both because of this status and because the Fed is seen as having to stay restrictive for longer. The Swiss franc has also gained ground as it is a traditional safe haven.**

**What with the Strait of Hormuz practically blocked, oil supplies constrained, an explosive geopolitical situation and central banks once again hesitant, the chance of a quick resolution to the conflict with only limited consequences looks increasingly low. We have maintained the hedging strategies we adopted before the war began. We are sticking with our dollar exposure, a position we have reinforced since the end of 2025. We remain cautious on duration and prefer investment grade credit to high yield and government bonds.**

## EUROPEAN EQUITIES

Escalating Middle East tensions rekindled energy worries in Europe. Close to 57% of the European Union's energy requirements are imported and Italy, Spain and Germany are even more dependent. Bond market tension rose as traders anticipated rate hikes. ECB chair Christine Lagarde said the bank would not let inflation take off again as in the 2022-23 energy shock. Her comments suggested rates could rise if the crisis were to persist. At the same time, markets started to worry about mounting tensions in the private credit segment. Several large funds run by firms like BlackRock, Morgan Stanley and Cliffwater were forced to limit redemptions. Deutsche Bank's share tumbled, and investor worries over liquidity risk rose after the bank's annual report revealed that it had €26bn in direct exposure to private credit.

Elsewhere, company results were mixed depending on sectors. In the retail space, **Zalando's** operating profits beat expectations and the group unveiled a €300m share buyback programme. **Inditex** once again posted solid annual figures, and momentum since the beginning of the year continued with 9% growth. But in autos, **BMW** and **Volkswagen** both reported disappointing results and guidance fell short of expectations. Due to costs from the move into electric cars as well as customs tariffs, **Porsche** now expects margins of 5.5-7.5%, or below analysts' estimates. **ID Logistics** announced robust results with 27 new contracts signed in 2025, or more than expected. But investments are expected to continue weighing on margins over the short term. In services, **Elis** surprised the market with a €500m share buyback programme representing 9% of its market cap. In industry, **Alstom** signed a €1.03bn contract with Portugal's railway operator to provide 153 trains and build a new factory in the country. In other headline news, recently listed **CSG** reportedly failed to inform investors that its Spanish subsidiary had been suspended from NATO procurement because of irregularities in ammunition contracts. **Novo Nordisk** settled its legal dispute with **Hims & Hers** by agreeing to a distribution agreement for its weight loss treatments. **Scout24** said generative AI's immediate impact on its business was relatively small as less than 1% of its traffic used language models.

## US EQUITIES

Wall Street had another choppy week with traders torn between hopes Middle East tensions would abate and signs that the oil shock was likely to last longer. Markets initially rebounded sharply after Donald Trump suggested the war with Iran was practically over but then retreated over the rest of the week. The S&P 500 ended the period around 1% lower. As small caps are more sensitive to the cost of capital and the domestic economy, the Russell 2000 (-1.44%) continued to underperform. Implicit volatility stayed high as energy prices saw wide swings. Government bond yields rose across the board with US 10-year Treasuries moving above 4.2% and the 2-year bond close to 3.7-3.8%. Investors repositioned for a “higher for longer” scenario. The euro slipped to around 1.15-16 against the dollar.

The week was naturally dominated by the ongoing conflict between the US and Israel against Iran with a focus on energy price shifts. Initial optimism over the US President’s comments suggesting the war would be short, and the Strait of Hormuz secured, was dashed by fresh tensions. Iran laid mines, launched drones and missiles, threatened to completely block oil exports and repeatedly said it could shut down the strait for some time. Washington and G7 allies suggested various offsetting measures like releasing 400 million barrels of strategic oil reserves, temporarily waiving the Jones Act and possibly deploying military escorts for tankers. However, price tensions continued. Oil first jumped significantly above \$100 before brutally reversing course but then rapidly moved higher to around \$95-100. Brent crude ended up moving back above \$100. Monetary policy anticipations tightened due to this mix of a persistently resilient economy combined with a supply shock. At the beginning of the month, markets had been banking on more than 50bp in cuts in 2026 but are now expecting only a marginal fall by the end of the year. And yet February’s CPI was in line, weekly jobless claims are still stable, housing starts have improved and the trade deficit has narrowed. The problem is that the data are seen as lagging energy market developments. Future inflation reports are likely to reflect recent oil price surges more accurately.

Sector moves were more marked as the oil shock ramped up and financial conditions tightened. Unsurprisingly, energy led gains as WTI rose and short-term visibility on North American producers improved. Tech also managed to end the period higher. Despite profit taking on some mega caps to start the week, the AI theme remained solidly centre stage. Software and cloud earnings reports came in strong, especially for Oracle, and there were a number of AI infrastructure investment announcements. Financials led losers as interest rates rose and concerns over private credit increased. Several funds restricted redemptions and major banks were more cautious over detailing exposure. Industrials and consumer discretionary were also weak. Both are sensitive to the cycle and higher funding costs and any lasting rises to oil prices would hit transport, tourism, autos and some discretionary spending segments. Defensives like utilities, materials, healthcare and communication were also down but held up better than cyclical plays. Listed property stocks logically lost ground due to rising long bond yields and an increase in the cost of capital.

## EMERGING MARKETS

The MSCI EM index was down by 0.46% in USD as of Thursday. Brazil and China were up by 1.01% and 0.97%. India, Mexico, Taiwan and Korea fell 3.24%, 2.14%, 0.34% and 0.28%, on higher energy cost concerns.

In **China**, February CPI surged to 1.3% YoY, exceeding expectations of 0.9%. This marked the highest level in nearly three years and was driven by Lunar New Year holiday spending. PPI came in at -0.9% YoY, or better than the estimated 1.1% decline. Trade data for January-February showed exports surging 21.8% YoY, or well above consensus expectations of around 7%. The National People's Congress trimmed its GDP growth target to 4.5-5.0% for 2026, while keeping the fiscal deficit-to-GDP ratio flat at about 4%. Tencent joined other Chinese tech companies and launched its own Openclaw AI agent. CATL delivered strong fourth-quarter results reflecting its global leadership in batteries for EVs and energy storage systems.

In **Taiwan**, February exports rose 20.6% YoY, missing expectations of a 35.5% rise due to the Lunar New Year date. Sales at TSMC in February rose 22.2% YoY.

In **South Korea**, exports for the first 10 days of the month jumped 55.6% YoY. The government announced plans to restart six nuclear reactors by mid-May to stabilise power prices. Samsung announced it would cancel a total of 87 million treasury shares, including preferred shares, in the first half of 2026.

In **India**, February CPI rose 3.21% YoY, or in line with expectations. President Trump said Reliance Industries would invest \$300bn in a new oil refinery in USA. The government said that gas supplies to manufacturing and other industrial consumers, supplied through the national gas grid, would be maintained at 80% of average gas consumption in the last 6 months. ABB India announced a \$75m investment to expand manufacturing and R&D capabilities. Netflix launched Eycline Studios as its global production and innovation studio in India.

In **Mexico**, annual inflation accelerated to 4.02% in February from 3.79% in January, exceeding estimates of 3.94%. The Senate committee unanimously backed a cap on public sector "golden pensions".

In **Brazil**, the government announced the elimination of PIS/Cofins taxes on diesel, introducing a temporary subsidy along with a temporary oil export tax (from 0% to 12%). February IPCA inflation came in above expectations and markets to reduce expectations of the first interest cut by the Central Bank next week from 50bp to 25bp. MercadoLibre announced plans to invest \$3.4bn in Argentina in 2026 and add 1,900 jobs, representing a 30% increase versus the planned \$2.6bn for 2025.

## CORPORATE DEBT

Trading was highly volatile due to geopolitical uncertainty and rising oil prices. The Xover widened by 8bp over the period up to Thursday's close with wide swings between 270 and 310bp. Investment grade fell 0.51% and European high yield 0.71% due to rising rates and IG and HY spreads widening by 3bp and 16bp, respectively. The CoCo index shed 0.59%, Tier 2 subordinated debt widened by 6bp and the bank sector also suffered from private credit news.

In the US, Wednesday was one of the best ever days for issuance with deals totalling close to \$60bn. Amazon raised \$37bn in 11 tranches and Salesforce \$25bn in 8 tranches. In Europe, Amazon also raised €14.5bn in 8 tranches in its first ever euro issue. The order book ballooned to €27.9bn, the fifth largest amount in euro-denominated corporate debt.

In the hybrid segment, Stellantis seized a lull on Wednesday to raise the equivalent of €5bn, 2 euro tranches for €4bn and a sterling tranche for £825m. It was the largest deal since 2020 and it passed the liquidity test as it was oversubscribed 4 times.

**GLOSSARY**

- Investment Grade: bonds rated as high quality by rating agencies.
- High Yield: corporate bonds with a higher default risk than investment grade bonds but which pay out higher coupons.
- Senior debt benefits from specific guarantees. Its repayment takes priority over other debts, known as subordinated debt.
- Debt is considered to be subordinated when its redemption depends on the earlier payment of other creditors. To offset the higher risk, subordinated Senior debt has priority over other debt instruments.
- Tier 2 / Tier 3: subordinated debt segment.
- Duration: the average life of a bond discounted for all interest and capital flows.
- The spread is the difference between the actuarial rate of return on a bond and the rate of return on a risk-free loan with the same maturity.
- The so-called "Value" stocks are considered to be undervalued.
- EBITDA: Earnings before Interest, Taxes, Depreciation, and Amortization.
- CTA: quantitative strategy which uses futures to invest in a wide range of financial assets, including equity indices, short-term and long-term interest rates, currencies, and commodities.
- The PMI, for "Purchasing Manager's Index", is an indicator of the economic state of a sector.
- AT1s belong to a family of bank capital securities known as contingent convertibles or "Cocos". Convertible because they can be converted from bonds to shares (or depreciated entirely) and contingent because this conversion only occurs if certain conditions are met, such as the issuing bank's capital strength falling below a predetermined trigger level.
- RT1s: perpetual bond issues with early redemption possible after 10 years. Coupon payments are discretionary and non-cumulative.

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