



## THE MIDDLE EAST PLUNGES INTO THE UNKNOWN

**By Michaël Nizard, Head of Multi-Asset & Overlay, and Nabil Milali, Multi-Asset & Overlay Portfolio Manager at Edmond de Rothschild Asset Management (France)**

**As we feared at the end of last week, Donald Trump acknowledged the inability to reach an agreement on his own terms on the nuclear issue and decided to launch a large-scale military operation against Iran.** The elimination in the early hours of the conflict of Supreme Leader Ali Khamenei, along with 48 other political and military leaders, confirmed that the objective of the United States and Israel was indeed regime change and not just the destruction of Tehran's nuclear and ballistic capabilities. While the world has seen many phases of tension between the two sides since 1979, **this is an unprecedented escalation whose consequences will be profound and lasting for the entire region and undoubtedly for the global geopolitical balance, as it appears that this intervention is also a message sent to China, of which Iran was a partner, as Venezuela was before it.**

Faced with what is now an existential threat, the Iranian regime has decided to regionalise the conflict by attacking many neighbouring countries, such as the United Arab Emirates, Bahrain, Saudi Arabia and even Oman, despite the latter having served as an intermediary in negotiations with the United States. At this stage, these states are exercising restraint and are content to intercept Iranian missiles, but as their defensive capabilities approach their limits and human and material damage increases, the risk of retaliation on Iranian territory can no longer be ruled out. France, the United Kingdom and Germany have also adopted a defensive strategy at this stage, deploying military forces in the region to protect their interests, but greater involvement on their part in strikes against Tehran cannot be ruled out, particularly after the attack on a British military base in Cyprus. Finally, Hezbollah's entry into the war opens up a new and particularly dangerous front for Israel, but one that is likely to reinforce B. Netanyahu's strategy of definitively eliminating any Iranian threat, including its proxies.

While risk aversion is palpable on the financial markets this morning, with a further decline in stock indices, a rise in the dollar, widening credit spreads and a rise in the price of gold, **the movements are still relatively limited given the seriousness of the events. The explanation undoubtedly lies in the fact that Brent crude continues to trade at levels that are sustainable for the global economy, around \$79/bbl, even after soaring by nearly 30% since the beginning of the year.** Crude oil prices are likely to continue to incorporate a higher geopolitical risk premium, as the Strait of Hormuz, through which nearly 20% of the world's oil and more than a third of the supply transported by sea passes, is severely disrupted by the conflict. **It is not so much the attacks on tankers that are causing this disruption, but rather the surge in insurance premiums and even the total refusal to insure ships that would risk crossing the strait. In addition, several sources indicate that GPS signals are being jammed in the area, making navigation extremely difficult. If this situation were to continue, it would amount to a de facto closure of the shipping lane, but only temporarily.** The worst-case scenario would be Tehran mining the area, but at this stage there is no reason to believe that this strategy will be employed, given that the Iranian regime also depends on the Strait to export its oil to China, one of the few financial resources it still has.

A few years ago, the mere mention of the risk of closure of the Strait of Hormuz would have been enough to push Brent above \$100/bbl, but the oil market has changed structurally since then. On the one hand, global production remains abundant thanks to American shale,



the growth in non-OPEC production and the increase in the cartel's own production, as announced this weekend. On the other hand, Gulf countries now have alternative routes for exporting some of their oil, bypassing the Strait of Hormuz, such as the EWP pipeline in Saudi Arabia, whose capacity has been increased to 7 Mb/d, and the ADCOP pipeline in the UAE, which has a capacity of 1.5 Mb/d. All of these factors are likely to limit the risk of an oil shock similar to that of the 1970s and keep Brent below the \$100/b threshold. Nevertheless, it should be noted that these alternatives cannot fully compensate for the flows passing through Hormuz and that the risk of strikes against oil facilities remains high, which justifies maintaining a geopolitical risk premium in prices.

The situation is similar for gas prices, to which Europe is particularly sensitive. Gas prices rose by more than 30% this morning, but the surge could have been even greater if LNG production were not so abundant worldwide. **It will be particularly important to monitor Qatari flows, which account for nearly 20% of global supply, and in this respect Qatarenergy's announcement that it is halting its LNG production is a very bad sign.** However, the fact that Doha is one of Tehran's allies gives hope that its exports may be relatively unaffected.

Uncertainty is likely to persist for some time, however, as Donald Trump himself has suggested that the conflict could last for nearly four weeks. In terms of our strategy, at this stage, **we prefer to establish a framework based on key criteria and an investment plan rather than rely on a political outcome, because this geopolitical environment reminds us how much we are on complex and major tectonic plates in terms of medium-term impact. We see three possible scenarios emerging:**

- **The most feared scenario is one of chaos (20%), similar to the situation in Libya after the fall of Muammar Gaddafi.** Even if the current regime falls, the alternatives are not obvious and the institutional vacuum could lead to civil war between the different factions of Iranian society. In this case, instability could last for many years, with significant consequences given Iran's strategic importance in the region. If militias were to form, they would have considerable capacity to cause disruption by permanently disrupting maritime traffic through the Strait of Hormuz or by regularly targeting oil facilities in the region, while being very difficult to eliminate, as illustrated by the case of the Houthi rebels. In this scenario, the geopolitical risk premium would remain very high and persistent in crude oil prices, **with a significant risk of a new inflationary spiral, justifying a slightly more prolonged caution on risky assets and long-term government bonds.** Second-round effects on US private debt linked to higher capital costs would then be a concern, and questions could also arise regarding debt issuance by AI players, which is set to increase significantly over the next two years to finance their CAPEX.
- The second scenario is that of **a war of attrition (50%) lasting several months before a de-escalation initiated by Donald Trump.** The Iranian regime is likely to prove more resilient than anticipated by the United States and Israel. History shows that it is extremely difficult to overthrow a regime without ground intervention, which Trump categorically rules out due to the high risk of human casualties. In addition, press reports indicate that the Iranian command is no longer centralised and that different units are acting more or less independently, which further complicates the destruction of the regime. If the conflict becomes bogged down, even if the regime's structure remains in place, Trump will be tempted to end hostilities by declaring victory regardless, highlighting the elimination of the Supreme Leader and the destruction of Iran's military capabilities. Indeed, the US president will not want to risk a further surge in petrol prices in the run-up to the mid-term elections and will



favour a return to the status quo with a continuation of the standoff with Iran, but at a lower intensity. In this scenario, **crude oil prices would fall back without returning to pre-crisis levels, which would nevertheless be enough to fuel a renewed appetite for risk** in the financial markets.

- Finally, **the scenario hoped for by the United States and Israel would be regime change (30%)**, whether towards a democratic transition or another authoritarian regime that is more conciliatory towards Washington. At this stage, it is impossible to imagine what form this might take, but if Washington achieves its goals, it would mark a major turning point in the history of the region, ending a cycle of more than 40 years that began with the Islamic revolution of 1979. The US would have won an important victory, having succeeded in isolating Iran from the rest of the Persian Gulf countries and further consolidating the Abraham Accords, with the project of a pan-Arab arc conducive to direct investment. Beyond the expected sharp decline in Brent crude prices and renewed risk appetite in the financial markets, this would represent a major boost to the region's attractiveness for foreign investment. **In this scenario, we could continue to consider that we are in an inflationary boom driven by monetary and fiscal policies that remain as accommodative as ever**, across all major regions (US, Europe, China, Japan, UK). This scenario would favour the search for opportunities in equities and credit, with a continued preference for international rotation in favour of Japan and EMs.

**With regard to our asset allocation**, given the lack of visibility on the outcome of this crisis, it is appropriate to weight each of these scenarios, which leads us to **maintain for the time being the optional hedges and credit CDSs that we added to our portfolios before this weekend's escalation. We had already taken profits on our dollar underweight position, which is now regaining its safe-haven characteristics.** We had also reduced our exposure to equity markets, favouring the oil sector as we expect Brent crude to rise further without breaking through the symbolic threshold of \$100/bbl. Energy prices should therefore remain at sustainable levels for the global economy, limiting the risk of a growth slowdown. **Given the multitude of risk factors, we remain overweight in resilience-related themes (defence, energy security, strategic autonomy).**

On the other hand, rising energy prices should translate into a further positive contribution to inflation, which will pose a new challenge for central banks. In particular, **the US Federal Reserve is entering 2026 in an uncomfortable position.**

**Although it maintains a slightly accommodative stance in its rhetoric, with the prospect of lowering rates during the year**, the reality of the figures makes any decision increasingly delicate. Inflation remains more stubborn than hoped for, the labour market remains surprisingly robust despite signs of a slowdown, and technological and geopolitical shocks further complicate the economic outlook. At the same time, the Fed is monitoring tensions in private credit and risks related to the Middle East, but does not currently see any reason for a radical change of course. The rise in credit spreads remains contained at this stage, far from crisis levels, but has been on an upward trend for several weeks. **At this stage, we believe that Kevin Warsh should favour lowering key interest rates despite high oil prices, as a prolonged oil shock would act as a potential drain on household consumption and weigh on growth, which, from the Fed's point of view, would justify increased monetary support to offset this drag on activity.**

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EDMOND DE ROTHSCHILD ASSET MANAGEMENT (FRANCE)

47, rue du Faubourg Saint-Honoré 75401 Paris Cedex 08

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332.652.536 R.C.S. Paris