Ostrum ASSET MANAGEMENT

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Market views and strategy

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• Topic of the week: Emerging Markets: What to Except After the Resilience and Surprises of "Liberation Day"?

by Zouhoure Bousbih

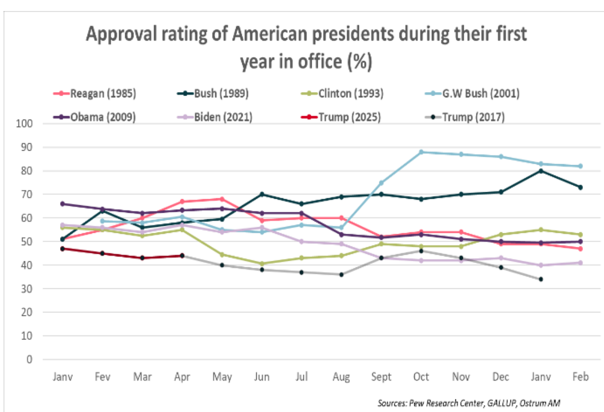
- Despite high political and economic uncertainty caused by tariffs and trade tensions, emerging markets have been resilient during the sell-off;
- The unexpected weakness of the dollar has been their main advantage, although overall resilience masks disparities between countries;
- The deterioration of global economic outlooks is likely to put highly indebted countries under pressure: the spread differential between "High Yield" and "Investment Grade" has widened;
- The significant uncertainty caused by tariffs risks keeping financial market volatility high, leading to a revaluation of risk premiums for emerging markets;
- A sustained drop in oil (and commodity) prices poses a risk to producers with high oil fiscal breakeven prices and significant financing needs.

• Market review: It's all tariff-on, tariff-off…

by Axel Botte

- Trump hints at a reduction in tariffs and suggests that Powell will serve out his term;
- Rates: Rhetorical easing allows the T-note yields to dip below 4.25%;
- Markets rebound following Trump's shift in policy;
- The Nasdaq surged 6.7% last week ahead of the earnings reports from major U.S. companies.

• Chart of the week



Donald Trump's approval rating, at 40% in April according to Gallup, is lower than that of previous American presidents since Ronald Reagan at this point in their terms.

The current occupant of the White House is performing worse than Bill Clinton did in 1993, as Clinton did not secure majority approval during his first 100 days in office.

Trump's policies are viewed negatively by most Americans, particularly his tariff policy and cost-cutting measures within the federal government. His transgressions of federal laws are also being criticized.

• Figure of the week

3521

The U.S administration is preparing to impose a 3521% tariff on solar panel imports from Southeast Asian countries such as Cambodia, Thailand, Malaysia, and Vietnam.
Source: Bloomberg

Topic of the week

Emerging Markets: What to Except After the Resilience and Surprises of "Liberation Day"?

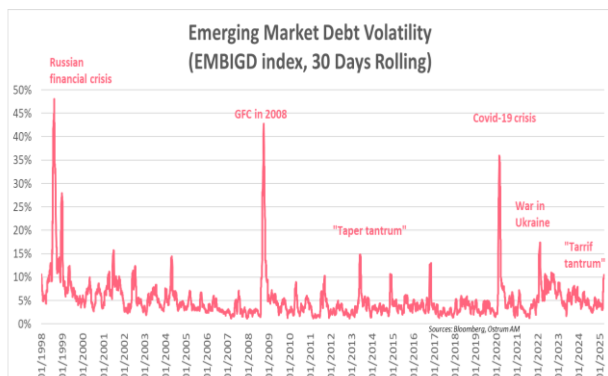
Despite significant uncertainty caused by reciprocal tariffs and trade tensions, emerging markets have surprised with their resilience. Indeed, volatility has been relatively limited in sovereign debt markets, and equity markets have also delivered surprising performances. This is mainly due to the unexpected weakness of the dollar, reflecting investors' concerns about the impact of these new tariffs on U.S. economic outlook. Despite the positive rhetoric from the American president regarding tariffs, trade negotiations between the United States and China remain at a standstill and seem unlikely to be resolved in the short term. Political uncertainty will remain high, increasing downside risks to global growth and the fundamentals of emerging markets. Falling commodity prices and tightening financial conditions also pose additional risks.

Surprising Resilience of Emerging Markets Despite Increasing Global Risks…

Relatively Limited Volatility in Emerging Markets' External Sovereign Debt Markets

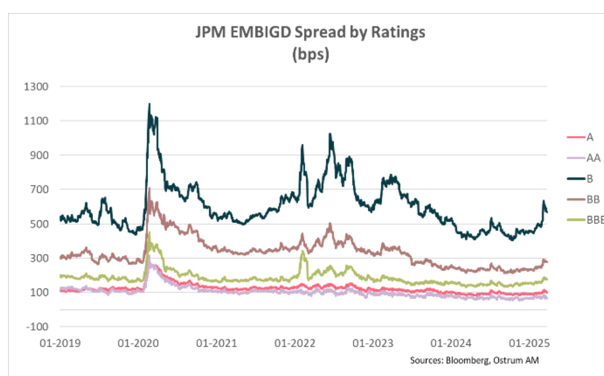
The volatility of emerging external debt has been extremely limited compared to previous episodes of financial market stress.

The volatility induced by global trade tensions in emerging markets' external sovereign debt markets has been relatively limited compared to previous episodes of financial market stress, as shown in the accompanying chart.



Relatively Stable Risk Premiums

Risk premiums (JPM EMBIGD spread) for "Investment Grade" rated countries have remained relatively stable, as depicted in the chart above. However, spreads for "High Yield" rated countries have widened, though still limited, especially for those rated "B" and "CCC." Ultimately, the JPM EMBIGD index spread widened by 7 basis points to 350 basis points after the White House announced a 90-day pause on reciprocal tariffs.

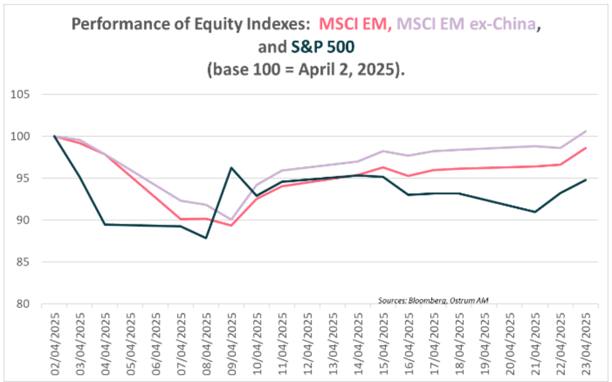


Unexpected Performances in Emerging Market Equities

Against all expectations, emerging market equities have better withstood rising volatility

Emerging market equities have delivered surprising performances, even as they are primarily targeted by reciprocal tariffs!

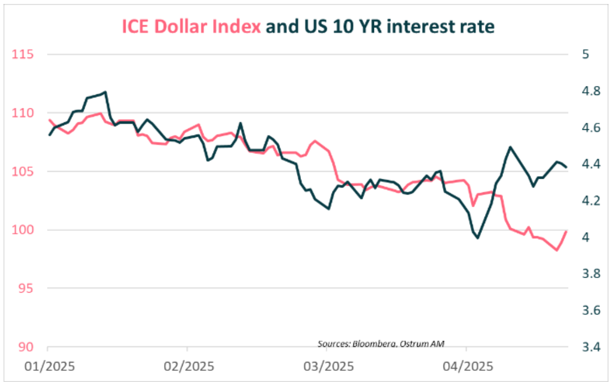
compared to U.S. stock indices, as illustrated by the accompanying chart. The MSCI EM ex-China index outperformed the U.S. S&P 500 index during the study period. This observation is particularly surprising given that the reciprocal tariffs predominantly affect emerging markets. Notably, since the beginning of the year, the MSCI EM index has outperformed the other two equity indices due to the rebound in the Chinese stock market early in the year, driven by a consumption plan. As a result, the MSCI EM index showed a performance of 0.3%, -2.3% for the MSCI EM ex-China index, and -9.9% for the S&P 500.



... Thanks to the Unexpected Drop in the Dollar!

The unexpected weakness of the dollar was a boon for emerging markets.

The relative resilience of emerging markets is primarily attributed to the weakness of the dollar. The greenback behaved unusually compared to the 2018 trade war. Instead of appreciating, the dollar weakened even as long-term interest rates rose and U.S. stocks plunged, as shown in the accompanying chart.



This reflects concerns about the outlook for the U.S. economy, which is expected to be more adversely affected by these new reciprocal tariffs than other regions of the world, explaining the more severe sell-off in American financial assets.

However, the simultaneous rise in U.S. long-term rates, alongside the dollar's decline and the yuan's weakness, could also be attributed to emerging market central banks selling Treasuries to defend their currencies. This would explain the relative resilience of debt markets, particularly the catch-up in local debt and the outperformance of emerging market equities compared to G10 markets.

What to except for Emerging Markets Post-"Liberation Day"?

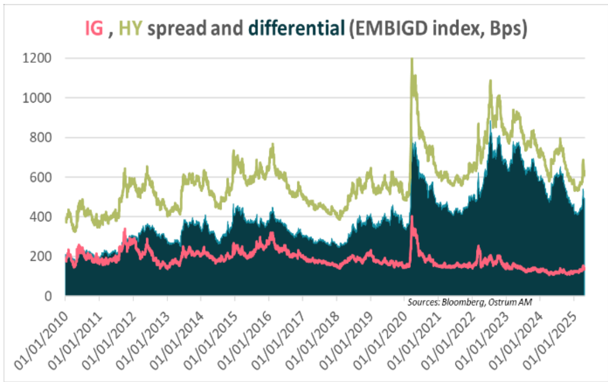
The surprising performances of emerging markets mask disparities between countries.

These surprising performances, however, mask disparities between countries. Bond and equity performances vary from one country to another depending on tariff rates, the vulnerability of countries to the slowdown in global trade, and their intrinsic fundamentals. The deterioration of global economic prospects is expected to put pressure on heavily indebted countries and lead to a decline in commodity prices. The significant uncertainty induced by tariffs risks keeping financial market volatility high, leading to a revaluation of risk premiums.

The deterioration of global growth prospects threatens highly indebted emerging countries.

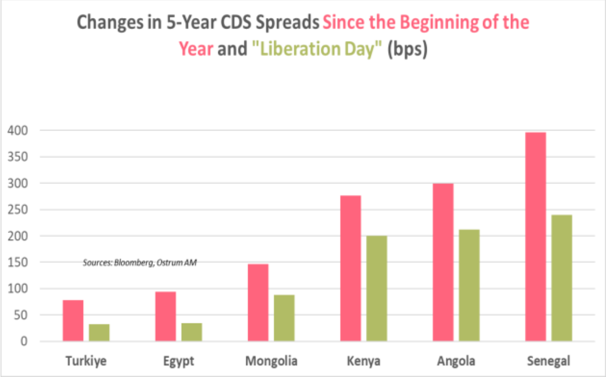
Widening of the spread between "High Yield" and "Investment Grade" post-Liberation Day...

While external sovereign debt has been relatively resilient to the "Liberation Day" turmoil, the spread differential between High Yield and Investment Grade widened during the recent sell-off, as shown in the accompanying chart on the left. The persistent uncertainty related to tariffs is expected to weigh on the growth of emerging countries by reducing their fiscal revenues.



... Reflecting fiscal risk for countries that are already heavily indebted, such as Senegal, Angola, and Kenya.

Countries such as Senegal, Angola, and Kenya, which are already heavily indebted, risk widening budget deficits and increasing public debt. The 5-year CDS spreads for these countries have significantly widened since April 2, as illustrated in the accompanying chart.



These countries benefit from financial support from multilateral organizations like the International Monetary Fund (IMF) and the World Bank, but this support could be challenged by the new American administration, which has suggested the possibility of withdrawing from these international institutions.

For example, 55% of Kenya's external debt is held by multilateral organizations and 22% by China. Despite a slight decrease in its public debt to 70% of GDP, Kenya is experiencing a sharp increase in borrowing costs, and high debt servicing (80% of its budget revenues) limits its fiscal leeway. The government is trying to reduce pressure by altering its debt instruments but faces internal opposition and deteriorating confidence from international investors. In March, Kenya applied for a new program with the IMF.

A sustained drop in crude oil (and commodity) prices could pressure emerging producer and exporter countries.

Despite the tariff de-escalation, Brent is still recording a negative performance of -11% since the beginning of the year...

Another indirect effect of reciprocal tariffs is the enduring decline in commodity prices, particularly oil.

Despite reduced risk aversion, Brent crude still shows a negative performance of more than -11% since the start of the year. This reflects risks to global oil demand. Several OPEC+ member countries, such as Kazakhstan (accounting for 5% of global crude production), seek to increase their production to boost their oil revenues, exerting downward pressure on prices. If this decline continues, producer countries with high fiscal breakeven oil prices and significant financing needs could quickly come under pressure.

The table below, from the IMF's Regional Economic Outlook: Middle East and Central Asia, shows the fiscal breakeven oil prices for many producer countries in the Middle East and

Central Asia. This is the oil price at which the fiscal balance is zero.

Table: Fiscal Breakeven Oil Prices ($) for Countries in the Middle East and Central Asia.

...Widening the gap with the fiscal breakeven oil price for countries like Bahrain, Iran, Kazakhstan, and Saudi Arabia, which have significant financing needs.

Country	Average 2000–20	2021	2022	2023	2024	2025
Algeria	101.1	111.4	109.8	93.8	125.7	119.4
Azerbaijan	52.6	57.5	67.3	76.4	88.2	89.3
Bahrain	85.0	131.6	131.8	138.4	125.7	127.8
Iran	92.4	118.8	131.4	105.1	121.0	123.9
Iraq	70.9	54.2	68.5	80.4	93.8	90.0
Kazakhstan	...	183.5	95.3	109.3	123.5	109.3
Kuwait	59.6	87.6	81.5	81.0	83.5	78.3
Libya	75.0	52.2	64.4	65.9	66.0	63.7
Oman	70.1	76.7	55.4	57.2	58.1	53.9
Qatar	45.3	47.7	46.3	46.5	43.1	40.4
Saudi Arabia	80.0	83.6	88.1	93.3	96.2	84.7
Turkmenistan	37.9	28.9	31.5	34.2	35.8	37.1
United Arab Emirates	50.0	53.0	46.6	51.6	56.7	54.3

Sources: IMF, Ostrum AM

Thus, countries such as Bahrain, the most indebted of the Gulf states, Iran, Kazakhstan, and Saudi Arabia are most exposed to a sharp decline in crude oil prices.

Donald Trump will visit Saudi Arabia in May to seek $1 trillion in investment. It seems complicated. The budgetary breakeven price of crude oil has been set by the Kingdom at $84.7, above its average for the period 2000-2010, to finance massive investments such as infrastructure for the 2034 FIFA World Cup. Markets anticipate a price of around $65 per barrel, widening the gap between funding needs and the fiscal breakeven price.

Conclusion

The resilience and performance of emerging markets have come as a surprise during this sell-off, driven by significant political uncertainty related to reciprocal tariffs. However, the post-"Liberation Day" world could represent a turning point for emerging markets. The indirect effects of tariffs, such as tightening financial conditions, rising borrowing costs—particularly for highly indebted emerging countries—and falling oil (and commodity) prices may reignite the specter of emerging sovereign debt. Emerging markets have diversified their financial sources, notably from China and Gulf countries. However, the role of the latter has shifted from provider to fund raiser for financing their significant infrastructure projects in a context where the gap between the price of oil and their oil fiscal breakeven price has widened significantly. A withdrawal of the United States from the International Monetary Fund or the World Bank would be catastrophic for emerging countries like Kenya, Angola, and Senegal, which primarily rely on financial support from these international financial institutions.

Zouhoure Bousbih

Market review

It’s all tariff-on, tariff-off…

The U.S. administration is compelled to reassess its strategy. The current tariff policy has become untenable, and Donald Trump must make concessions. While the easing seen thus far may be largely rhetorical, it has fostered optimism in both equity and bond markets.

It appears that Donald Trump, facing a significant decline in popularity, is finally recognizing the economic toll of rising tariffs. The noticeable drop in maritime trade to the U.S. since the beginning of the month raises concerns about potential shortages of goods. Retailers heavily reliant on Chinese imports—such as Walmart, Target, and Home Depot—have made their case to the White House. Trump has signaled that a reduction in tariffs could be on the table, which has been sufficient to soothe market fears. Additionally, pressure from Trump on Jerome Powell has lessened. Treasury Secretary Scott Bessent has also sought to reassure Wall Street, indicating that tariffs on China cannot be maintained indefinitely. His intervention has contributed to a decline in long-term rates, even as a dollar crisis looms on the horizon. In short, the U.S. administration is navigating troubled waters, as market sentiment shifts between optimism and pessimism.

From a cyclical perspective, regional surveys have shown a uniform decline in April, including in the services sector. The rise in input prices is not matched by a comparable increase in output prices, indicating emerging pressure on margins. Nonetheless, layoffs remain very low, and consumer confidence is less downbeat than anticipated, according to the final estimate from the University of Michigan survey. First-quarter growth is likely to be negative due to the external balance. However, the increase in new home sales to an annualized rate of 724k in March is a positive surprise. Alongside the solid auto sales in March, these real estate purchases may reflect concerns about rising costs in the future (lumber, immigration enforcement).

Recent tensions surrounding U.S. bond yields have eased. The independence of the Fed must be preserved at all costs, and Trump has had to concede that he does not intend to dismiss or force Jerome Powell to resign before the end of his term, which is due in a year. In this context, the 10-year Treasury yield has fallen back below 4.25%, nearly 30 bps below April's highs. The prevailing trend towards a steeper yield curve has subsided. In the eurozone, the stability of the Bund underscores the renewed safe-haven status of German debt, facilitating a broad-scale easing of sovereign spreads, including the OAT, which trades around 72 bps. The Italian BTP, following a rating upgrade to BBB+, has also returned to around 110 bps. Anticipated inflation is normalizing as well, with a two-year inflation swap rising by 8 bps over the week. The recent recovery in oil prices, partly attributed to the lack of progress in U.S.-Iranian negotiations, has contributed to this rebound in breakeven rates. Interestingly, the inflation concerns reflected in surveys have yet to manifest in the U.S. Consumer Price Index (CPI).

The rebound in equities has been remarkable, with the Nasdaq gaining 6.7% last week ahead of earnings reports from Microsoft, Apple, Meta, and Amazon. Advances in Chinese technology could weigh on the outlook for the Magnificent Seven. Europe has also rallied, gaining 3% and leading to a notable easing in credit spreads and equity volatility. Euro IG spreads are currently at 95 bps over swaps, while high-yield spreads stand at 354 bps.

Axel Botte

Main market indicators

G4 Government Bonds	28-Apr-25	1wk (bp)	1m (bp)	2025 (bp)
EUR Bunds 2y	1.73%	+5	-29	-35
EUR Bunds 10y	2.51%	+4	-22	+14
EUR Bunds 2s10s	77.4 bp	-1	+7	+49
USD Treasuries 2y	3.75%	-1	-16	-49
USD Treasuries 10y	4.27%	-14	+2	-30
USD Treasuries 2s10s	51.4 bp	-13	+18	+19
GBP Gilt 10y	4.51%	-6	-18	-6
JPY JGB 10y	1.32%	+3	-17	-3
€ Sovereign Spreads (10y)	**28-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
France	72 bp	-4	+1	-10
Italy	103 bp	-14	-10	-13
Spain	66 bp	-4	+2	-3
Inflation Break-evens (10y)	**28-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
EUR 10y Inflation Swap	1.92%	+6	-9	-1
USD 10y Inflation Swap	2.43%	+7	-6	-3
GBP 10y Inflation Swap	3.31%	+7	-9	-21
EUR Credit Indices	**28-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
EUR Corporate Credit OAS	108 bp	-4	+17	+6
EUR Agencies OAS	53 bp	-3	+4	-9
EUR Securitized - Covered OAS	51 bp	-2	+6	-6
EUR Pan-European High Yield OAS	367 bp	-29	+49	+49
EUR/USD CDS Indices 5y	**28-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
iTraxx IG	66 bp	-6	+3	+8
iTraxx Crossover	338 bp	-28	+16	+25
CDX IG	67 bp	-8	+6	+17
CDX High Yield	406 bp	-39	+30	+94
Emerging Markets	**28-Apr-25**	**1wk (bp)**	**1m (bp)**	**2025 (bp)**
JPM EMBI Global Div. Spread	356 bp	-12	+26	+30
Currencies	**28-Apr-25**	**1wk (%)**	**1m (%)**	**2025 (%)**
EUR/USD	$1.135	-1.407	4.849	9.6
GBP/USD	$1.334	-0.292	3.091	6.6
USD/JPY	JPY 143	-1.737	4.527	9.7
Commodity Futures	**28-Apr-25**	**-1wk ($)**	**-1m ($)**	**2025 (%)**
Crude Brent	$66.8	$0.5	-$6.0	-9.2
Gold	$3 295.4	-$128.6	$210.2	25.6
Equity Market Indices	**28-Apr-25**	**-1wk (%)**	**-1m (%)**	**2025 (%)**
S&P 500	5 525	4.59	-1.00	-6.1
EuroStoxx 50	5 187	5.09	-2.71	5.9
CAC 40	7 600	4.31	-4.00	3.0
Nikkei 225	35 840	4.55	0.62	-10.2
Shanghai Composite	3 288	-0.09	-1.88	-1.9
VIX - Implied Volatility Index	25.40	-24.90	17.32	46.4

Source: Bloomberg, Ostrum AM

Additional notes

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