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Emerging Market Debt: 6 key lessons from the US-Iran conflict

The Middle East conflict has revealed a new, and perhaps lasting, realignment of the geopolitical order, while also offering a few surprises—like how quickly oil supply and demand responded to the energy shock.

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The question I'm getting asked most often now is: What have we learned from this year's US-Iran conflict? I think we can frame the answer around six key lessons.

1. US military power remains central to foreign policy.

The US administration has been increasingly active in using its military across multiple theaters, including Iran, Yemen, Iraq, Nigeria, Somalia, Ecuador and Venezuela. The US is willing to use force selectively and with specific objectives.

The takeaway for markets: Military escalation is now treated as a recurring feature, not an exception.

2. The US military's preference is distance.

The US has opted not to make large ground commitments or accept the high risks of significant naval exposure in the Strait of Hormuz, where reaction time collapses, defenses become less effective, ships have less room to maneuver, and unknown minefields create blind risk. Instead, the US is relying on airpower, naval assets, drones, missiles, intelligence and precision strikes.

The takeaway for markets: The US preference for engaging militarily from a distance reduces the risk of a large-scale conflict.

3. Iran's strategy is to leverage its neighbors.

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4. The US needs to continue to project power.

These three actors will continue to dominate geopolitics in the Middle East. The US needs to continue to project power. Israel remains focused on its core security threats, and Iran wants deterrence against future attacks. The key risk is that negotiations over Iran's nuclear program break down.

The takeaway for markets: Investors should assume an ongoing geopolitical risk premium for such setbacks.

5. We have been reminded how energy shocks transmit into the real economy and how governments are able to respond.

Military conflicts create disruption. Disruption moves energy markets. Higher energy prices impact inflation. Inflation impacts demand. It's a chain reaction. Countries

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responded with rationing policies and fiscal countermeasures such as reductions in the taxes on diesel and gasoline. The ability to manage these transition mechanisms is critical.

The takeaway for markets: It's clear that policy response matters and governments are now better at responding to these shocks.

6. Energy markets are far more elastic than inelastic.

On the supply side, new sources of crude have emerged from Saudi Arabia and the United Arab Emirates, and most importantly, from increases in the refined export capacity of the US. On the demand side, we saw countries such as China that were able to reduce consumption sharply when needed. Together, those adjustments show that supply and demand can respond much more quickly than investors have anticipated.

The takeaway for markets: It's clear that policy response matters and governments are now better at responding to these shocks.

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