

# Global Fixed Income Views

## Themes and implications from the Global Fixed Income, Currency & Commodities *Investment Quarterly*

### Author



**Bob Michele**  
Global Head of Fixed Income, Currency & Commodities and Co-Head of the Asset Management Investment Committee

### In brief

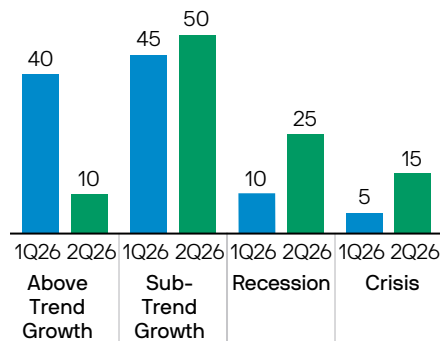
- Against the backdrop of a geopolitical and energy market shock, we significantly reduce the probability of economic expansion and increase the likelihood of contraction. The probability of Above Trend Growth falls from 40% to 10% and Sub Trend Growth rises by 5% to 50%, leaving expansion at a total of 60%, and still marginally our base case.
- How long will the Strait of Hormuz remain effectively closed? That is a key question for investors. We see only marginal capacity for the economy to absorb a prolonged period of higher energy prices before consumer demand is destroyed and recession ensues. We raise the probability of Recession to 25% from 10% and Crisis to 15% from 5%. Oil shocks resulting in stagflation are the most difficult scenarios for central banks to deal with.
- We expect the 10-year U.S. Treasury to hover around 3.75%–4.25%, as long as the Federal Reserve (Fed) is on hold, with better risk-reward at the front end of the curve. We see opportunity to go up in credit quality as spreads generally remain narrow compared with history. Securitized credit remains a top focus.
- In an era of economic and market volatility, our bias is to remain active and capitalize on recent market movements.

Our March *Investment Quarterly (IQ)* was held amid the backdrop of a three-week-old conflict in the Middle East, concerns over private credit, fears of job displacement by artificial intelligence (AI), and uncertainty about tariff policy. This administration certainly makes it hard to experience a calm quarter or two. While parts of the bond markets had already gone through a moderate repricing, much was dependent on the outcome of the conflict and the price trajectory of oil. The uncomfortable truth is that the market is in limbo between what could be vastly different outcomes.

Where markets settle over the next few weeks and months seems unlikely to be where markets are priced today. Either the U.S. administration finds a palatable off-ramp from the conflict, with oil settling down toward \$70, leading markets to rally, or events escalate with oil running up toward \$150, causing more meaningful derisking across markets.

Reflecting the uncertainty that results from an orthogonal geopolitical shock, the group was challenged to reach a consensus on the ultimate economic and market implications of such a shock. The tendency was either to ignore it as a temporal disruption or to worry about a series of dominoes toppling toward systemic risk. As always, examining current data and historical precedents helped guide us to a set of reasonable expectations and a path forward for our investments.

Scenario probabilities (%)



Source: J.P. Morgan Asset Management. Views are as of March 19, 2026.

## Macro backdrop

With Brent crude at current levels of ~\$100–110, oil and the entire energy complex serve as a tax on businesses and households. Unlike the inflation shock of 2021–2022 (which was more a function of demand-led inflation despite the compounding energy disruption from the Russia-Ukraine conflict), the current shock was driven purely by geopolitics at a time when the global economy was on a steady path. Businesses were digesting tariffs and reimagining their workforce with the advent of agentic AI.

The group felt there was only marginal capacity for the economy to absorb a prolonged period of higher prices before consumer demand would be destroyed, corporate earnings inflected negatively, and recession ensued. If over the next few weeks the relevant parties agree to a resolution that ameliorates the energy supply crunch, the group felt stability would return to markets with limited economic damage.

However, if the Strait of Hormuz remains closed for several months, the largest energy supply disruption in history would imply oil around \$150, consistent with demand destruction. We would then expect the market to price recession as its base case.

The response of the major central banks has been more nuanced. The Fed has indicated that it will keep monetary policy on hold until it has more information about the impact of the conflict on price stability and full employment. At the most recent post Federal Open Market Committee (FOMC) press conference, Fed Chair Jay Powell noted that the vast majority of the FOMC do not see a rate hike as the base case for the next move in policy rates.

In contrast, both the Bank of England (BoE) and European Central Bank (ECB) are focused on their single mandate of price stability; they have indicated that their next move could be to hike policy rates, as soon as next month. While the Fed is concerned about the impact of higher prices on aggregate final demand, the ECB and BoE worry about inadvertently accelerating higher prices through affordable funding.

At least for now, the lessons from 2008 and 2011, when central bank rate hikes only worsened the crisis, seem subordinate to the fear of a repeat of 2022, when a slow response to higher inflation led to a dovish policy mistake. Our thinking is more aligned with the 2008 experience—a supply-led oil shock will ultimately cripple final demand and lead to recession, necessitating cuts in policy rates.

With the Fed funds rate stuck at 3.625%, we expect the 10-year U.S. Treasury to remain in and around the 3.75%–4.25% range. Greater opportunities exist in the front end of government bond markets that have repriced 60 bps–100 bps higher on concerns over tighter central bank policy. The front end of yield curves also serves as a good hedge to a broader derisking move.

Despite concerns about geopolitical risks, AI-driven job displacement, evolving tariff policy and central bank independence, the group was mindful not to become too bearish. Balance sheets for both businesses and households remain strong and the tailwinds from the One Big Beautiful Bill Act (OBBBA), as well as tech and defense-related capex, are real. It's a complicated macroeconomic environment, but a palatable one assuming a reasonable resolution to the Middle East conflict.

## Scenario expectations

The group had little choice but to significantly reduce the probability of economic expansion and increase the likelihood of contraction. The pass-through of higher energy prices to lower aggregate demand is currently greater than the pass-through to higher finished goods and services prices and wage demands. We lower the probability of **Above Trend Growth** from 40% to 10% and raise **Sub Trend Growth** by 5% to 50%, leaving expansion at a total of 60%, and still marginally our base case.

The group believed that White House rhetoric has indicated that the administration should prioritize finding an off-ramp and ending the “pain at the pump” as soon as possible. While some damage to consumption and corporate earnings will occur, the offsetting impact of the OBBBA and continued capex demand for the tech and defense build-outs could allow the U.S. to avoid recession.

Damage to the U.K. and Europe could be more severe, but there is capacity for both central banks to lower rates to help cushion the impact. The risk, however, is that monetary support could come too late if the ECB and BoE focus exclusively on the immediate inflation risks.

We raise the probability of **Recession** to 25% from 10% and **Crisis** to 15% from 5%. Oil shocks resulting in stagflation are the most difficult scenarios for central banks to deal with. The Volcker playbook<sup>1</sup> (which worked): Make the pain of financing higher energy prices unbearable by raising rates aggressively despite weaker demand. As businesses and households pay the implied tax of higher energy, the funds available for consumption elsewhere dwindle.

While not our base case, the probability of contraction rises to 40%. In a crisis scenario, a prolonged conflict and extended oil price shock spills over into the broader economy, especially to the highly leveraged, lower-quality borrowers. A pullback in credit extension within the nonbank financial system could result in tighter credit conditions and a period of more painful deleveraging.

## Risks

The greatest risk is that the economy proves more resilient than we realize and easily absorbs the oil shock. And/or: Sovereigns run even larger fiscal deficits to support consumers and offset higher gas/petrol prices. If policymakers were to underestimate organic aggregate demand, central banks would become very aggressive in hiking rates to prevent inflation expectations from becoming wholly unanchored. Then asset prices would meaningfully deflate and contraction would become our base case.

<sup>1</sup> **The Volcker playbook** refers to the monetary policy approach of Federal Reserve Chairman Paul Volcker (1979–1987). Faced with stagflation — a combination of high inflation, stagnant economic growth, and rising unemployment — Volcker dramatically raised the federal funds rate, which peaked at around 20% in June 1981. The strategy was to crush inflation expectations by tightening monetary policy so aggressively that it induced a severe recession, but ultimately succeeded in bringing inflation down from double digits to around 3%–4% by the mid-1980s.

## Strategy implications

The group felt the best opportunity was to take advantage of the repricing of the front end of most government yield curves. The number of rate hikes now embedded into market expectations seems overdone and there appears to be a deleveraging event occurring as investors exit yield curve steepening positions. From current elevated levels, front end government bond yields can fall either because the conflict with Iran de-escalates, or it escalates further, creating demand for safe havens as focus shifts from upside inflation risks to downside growth risks.

The group also saw an opportunity to go up in credit quality at a time when spreads generally remain narrow compared with history, especially across the European banking capital structure. Securitized credit remains a top focus. The inherent credit enhancement of the securitization structure and the resilience of the U.S. consumer are comforting during times of market stress.

## Closing thoughts

We are in an era of economic and market volatility emanating from the U.S. administration's current policy. Despite the strain, we should embrace the value creation resulting from market repricing as it occurs and take advantage of it in our portfolios. For now, the administration is attempting to balance its policy initiatives with economic and market stability. Rather than completely derisk, our bias is to remain active and capitalize on recent market movements.

	Expansion		Contraction	
	<b>Above Trend</b> Global GDP growth >3.5% Inflation >2%	<b>Sub Trend</b> Global GDP growth 2%–3.5% Inflation ~2%	<b>Recession</b> Global GDP growth <2%	<b>Crisis</b> A disorderly movement in markets causes systemic impact
<b>Probability</b>	10%	50%	25%	15%
<b>Change from last quarter</b>	-30%	+5%	+15%	+10%
<b>Drivers</b>	Labor markets are resilient amid supportive fiscal policy and productivity gains  Conflict in the Middle East de-escalates, allowing for the resumption of normal energy supply  Capital expenditure, led by AI and defense investment, causes growth to reaccelerate	The U.S. labor market remains in a low-hire, low-fire equilibrium, keeping wages and cyclical price pressures benign  Conflict in the Middle East de-escalates, but resumption of normal energy supply is slow  Higher energy prices dampen consumer spending, offsetting the impact of tax refunds  Strong private sector balance sheets help companies manage higher input costs	Prolonged conflict in the Middle East disrupts energy supply, driving oil prices higher for an extended period and materially impacting consumers and businesses  The unemployment rate moves meaningfully higher. Layoffs lead to weak income growth and a decline in consumption. Businesses scale back capital investment plans	The combination of multiple financial and economic shocks, including energy supply disruptions, AI displacement, and a pullback in capital extension within the nonbank financial system, results in tighter credit conditions and a period of deleveraging
<b>Monetary and fiscal environment</b>	Central banks introduce more two-way risks around policy rates and monitor the extent to which wages and inflation accelerate  Fiscal policy across the globe promotes growth	The resolution of the energy shock allows central banks to gradually ease toward neutral  Fiscal impulse offsets higher energy costs and the lingering impact of tariffs	Despite higher energy prices, central banks are forced to respond with rate cuts to offset weaker growth and worsening labor markets  Automatic stabilizers from counter-cyclical programs help manage growth	Neither central bank easing nor fiscal policy is sufficient to forestall systemic impact
<b>Market and positioning</b>	Risk assets, especially public and private high yield, lower-rated investment grade credit and lower-quality emerging market debt outperform	High-quality corporates and securitized credit outperform  The front end of the yield curve outperforms as markets price out central banks' hawkish response to higher energy prices	Core government bonds and agency mortgage-backed securities outperform  Intermediate duration serves as an effective positive carry hedge	Cash and alternative reserve currencies outperform as right-way correlations break down

Source: GFICC Investment Quarterly; as of March 19, 2026. Forecasts, projections and other forward-looking statements are based upon current beliefs and expectations. They are for illustrative purposes only and serve as an indication of what may occur. Given the inherent uncertainties and risks associated with forecasts, projections and other forward statements, actual events, results or performance may differ materially from those reflected or contemplated. MBS: mortgage-backed securities.

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