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U.S. ‘EM-ification’ Provides Structural Support for Gold, Emerging Market Assets

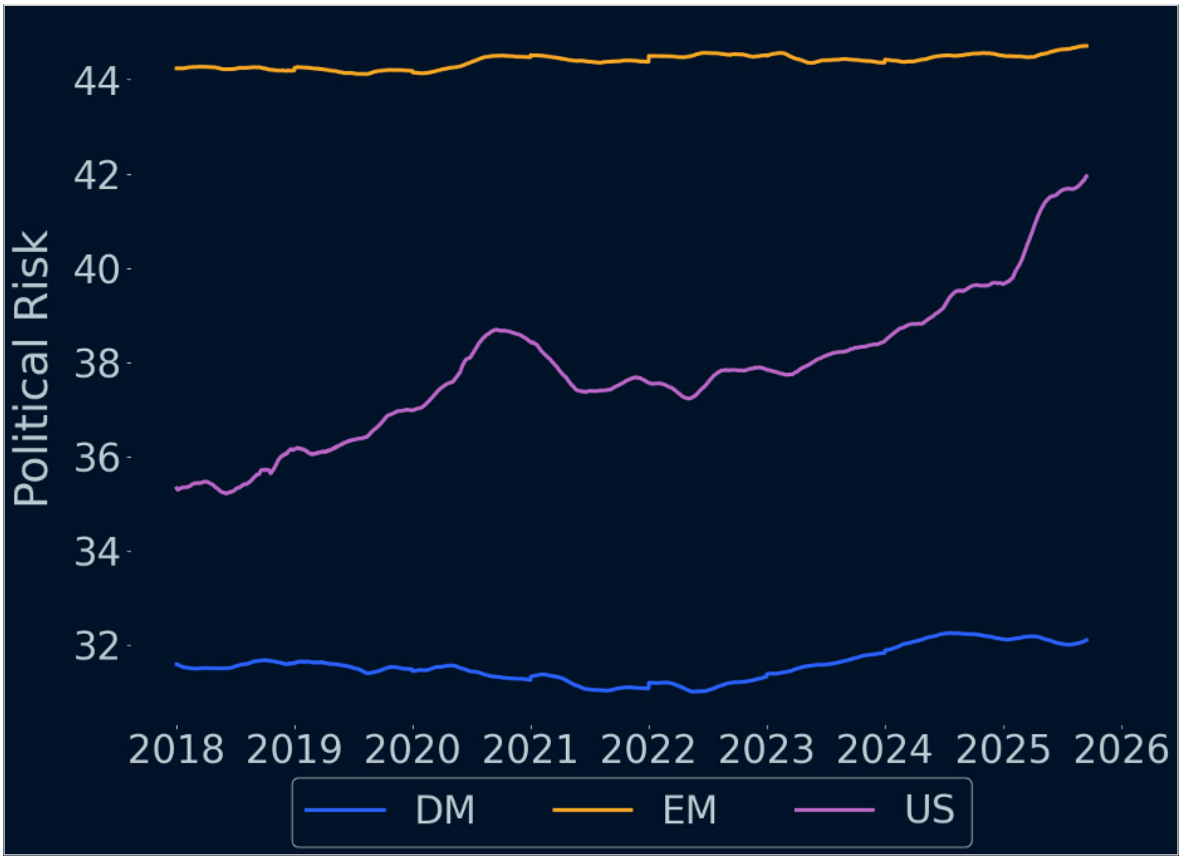
Spotlight

Spotlight: U.S. "EM-ification" Provides Structural Support for Gold, Emerging Market Assets:

- U.S. Political Risk looks more like that of an emerging market (EM), reducing the spread between U.S. and average EM Political Risk.
- The rise in topline U.S. Political Risk is very strongly and positively correlated with a surge in gold price since 1 Jan 2018.
- Relatedly, the associated decline in the Political Risk spread between EMs and the U.S. correlates strongly and positively with the declining premium on EM versus U.S. sovereign bonds since 1 Jan 2021.
- After 2 April 2025, this relationship is driven primarily a weaker U.S. dollar – itself driven by higher U.S. Political Risk.
- At the same time, the S&P 500 continues to increase alongside higher U.S. Political Risk, reinforcing conventional wisdom that There is No Alternative (TINA) to U.S. markets.

Per **previous analysis**, the level of U.S. Political Risk is now closer to the emerging market (EM) average than the developed market (DM) average. While the trend has accelerated since 2025 after President Donald Trump returned to power, it has been true since 2H/2021 and a clear trend since at least 2018 (Figure1).

Figure 1: Average DM, EM, and U.S. Political Risk

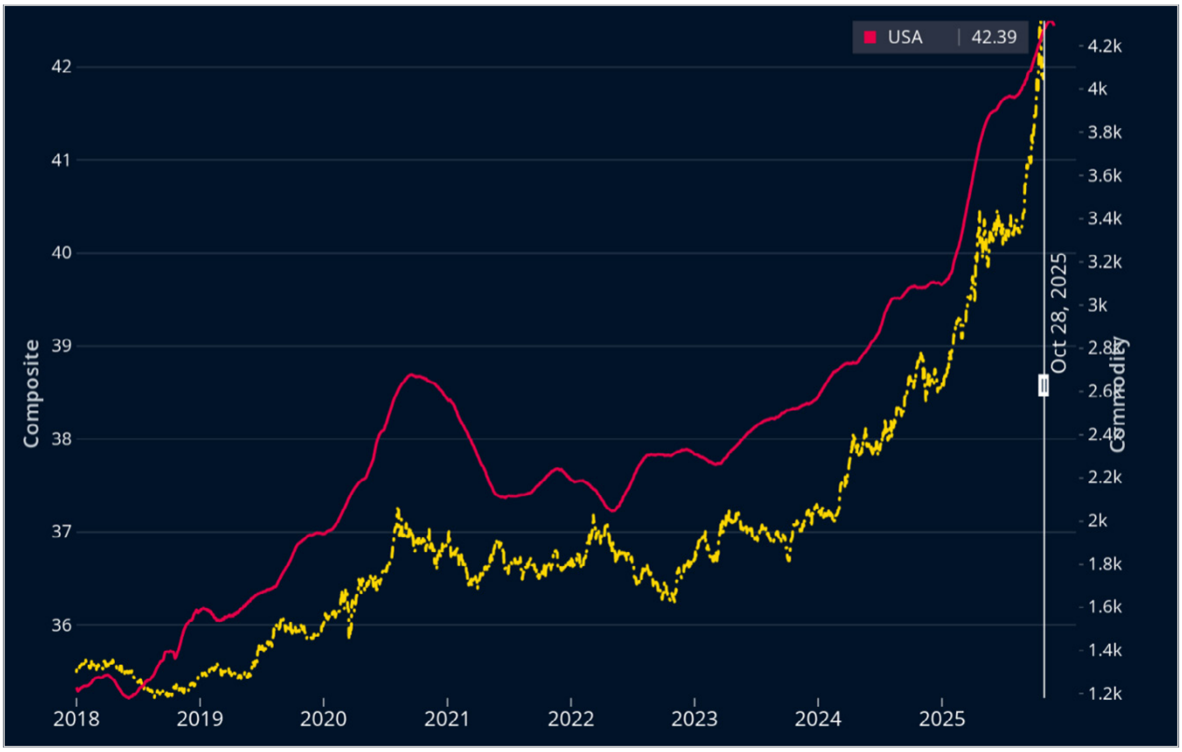


Source: GeoQuant

We **previously unpacked** the myriad drivers and implications for U.S.-dominated financial markets. In short, EM-like levels of U.S. Political Risk are (1) systematically driving up the price of gold; (2) keeping U.S. Treasury yields higher than macroeconomic conditions suggest; and (3) eroding the haven status of the U.S. dollar, which has become negatively correlated with Political Risk in 2025; and (4) seemingly irrelevant to U.S. equity markets.

Per Figure 2, the extremely strong, positive relationship between U.S. Political Risk and gold price – which survives controls for interest rates, inflation and the U.S. dollar exchange rate – speaks for itself. While broader demand for gold under Trump 2.0 has strengthened the relationship, it builds on a structural trend whereby higher U.S. political risk has driven central banks to increase gold reserves, such that **now own more gold** than U.S. Treasuries. As such, both the recent froth and even more **recent downturn** in gold prices don't have much impact on the broader, structural relationship.

Figure 2: U.S. Political Risk vs Gold Price since 1 Jan 2018 (r = 0.96 d/d)



Source: GeoQuant

Like gold, the U.S. dollar had historically been positively associated with U.S. political risk, with the world's reserve currency providing a haven even from U.S.-generated risks. But this correlation has turned negative since "Liberation Day," with higher risk pushing the dollar lower even as 10-year Treasury yields stay elevated. Higher U.S. Political Risk is **clearly steepening** the Treasury yield curve, with rising 30-year yields reflecting greater sovereign risk and lower shorter-term yields showing (**politically-driven**) concerns about growth. Foreign demand for U.S. Treasuries overall **is weakening**, while the spread between US and investment-grade EM bonds **are near a 18-year low**. Although this trend is driven primarily by U.S. Political Risk before "Liberation Day", it is mostly a function of political-risk weakened U.S. dollar thereafter.

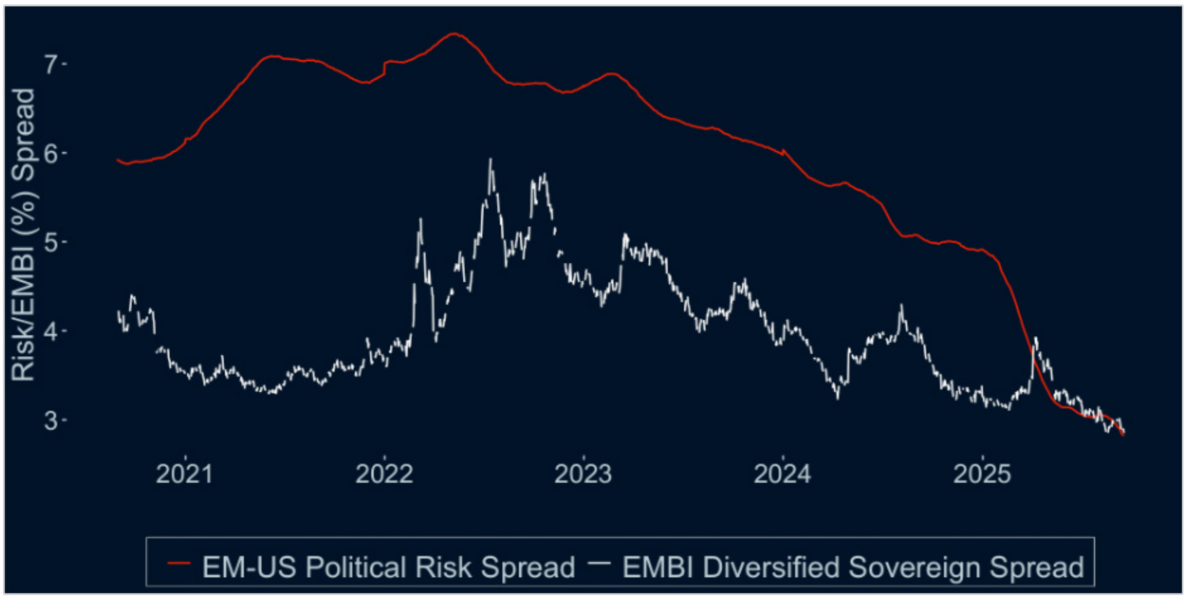
Yes, there is still no alternative to the U.S. dollar and U.S. Treasuries. But that reality is no longer a useful hedge; instead, it must increasingly be hedged against.

Tracking Political Premia in EM Debt

The J.P. Morgan **Emerging Market Bond Index (EMBI)** Diversified Sovereign Spread is a weighted average measure of emerging market bond spreads over U.S. Treasuries. This measure tracks how attractive EM debt is compared to safe-haven U.S. Treasuries. If the spread is rising, investors demand more premium for holding EM debt. If the spread is falling, EM debt is relatively more attractive.

GeoQuant data demonstrates how the accelerating increase in U.S. Political Risk in 2025 is making EM debt more attractive to investors in recent years. Figure 2 plots the EM-U.S. Political Risk Spread – which subtracts the (GDP-weighted) average level of Political Risk across 31 EMs from the level of daily U.S. Political Risk – versus the EMBI Diversified Sovereign Spread. Since 2021, they move in tandem. After Covid, stagflationary pressures in EMs widened the Political Risk spread while the U.S. stabilized after a period of social unrest and a tumultuous turnover of power. Since mid-2022, both spreads are declining, with EM's getting inflation under greater control, relative to trends, and the U.S. entering another period of social and institutional instability. Since 2025 and the second Trump administration, they are both falling rapidly.

Figure 3: EM – U.S. Political Risk Spread and EMBI Diversified Sovereign Spread



Source: GeoQuant

Regression Results

We formalize these intuitions by setting up a regression of the EMBI Diversified Risk Spread on our EM-U.S. Political Risk spread alongside other relevant macro indicators, especially DXY, which generally drives much of the relative value of EM assets. While a weaker USD makes EM assets relatively more attractive, a stronger dollar makes them less attractive. We also include the U.S. Fed policy rate (higher rates, higher spread), as well as the difference between average quarterly GDP growth and monthly inflation rates in EMs relative to the U.S, intended to capture relative economic performance. We run the analysis from 1 January 2021 to present to remove the 2020 Covid shock.

Table 1 presents the regression results. We look at three different samples in three columns. The first column is the fully specified model, running from 1 January 2021 to September 2025 and including all controls. While the relationship between the EM-U.S. Political Risk spread and bond spread is positive, it is a relatively weak and not statistically significant, with DXY overpowering its impact. However, if we end the analysis in April 2025 – before the U.S. dollar began weakening more explicitly on higher U.S. Political Risk – we see that the EM-U.S. Political Risk spread has a very strong and positive relationship with the bond spread, per column two. Moreover, if we remove DXY from the analysis in the first specification, the Political Risk spread regains its power across the entire period.

These results reveal an interesting relationship between the EM-U.S. Political Risk spread and DXY. While the correlation between DXY and bond spreads is predictably positive and significant in all samples, before Liberation Day this dollar effect runs alongside a similar (if stronger) relationship between the EMBI spread and EM-U.S. Political Risk. After Liberation Day, however, the U.S. dollar comes to reflect (i.e., closely track) higher U.S. Political Risk itself, wiping off the association between the political risk and bond spreads. Political Risk no longer has an independent effect; it is now captured by the U.S. dollar which, until Liberation Day, was insulated from Political Risk.

Table 1.

Variable	Sample 2021-September 2025	Sample 2021-April 2025	Sample 2021-September 2025
E.M. - U.S. Political Risk	**4.70** **(3.07)**	**41.01 ***** **(3.10)**	**46.86 ***** **(3.00)**
U.S. Dollar Index (DXY)	9.02 *** (0.38)	9.94 *** (0.33)	(excluded)
U.S. Policy Rate	8.07 *** (1.20)	9.71 *** (1.03)	9.81 *** (1.45)
E.M. - U.S. GDP Growth	-4.29 *** (0.90)	0.72 (0.81)	-11.82 *** (1.03)
E.M. - U.S. Inflation Rate	-4.49 (3.62)	-0.44 (3.16)	-6.72 (4.38)

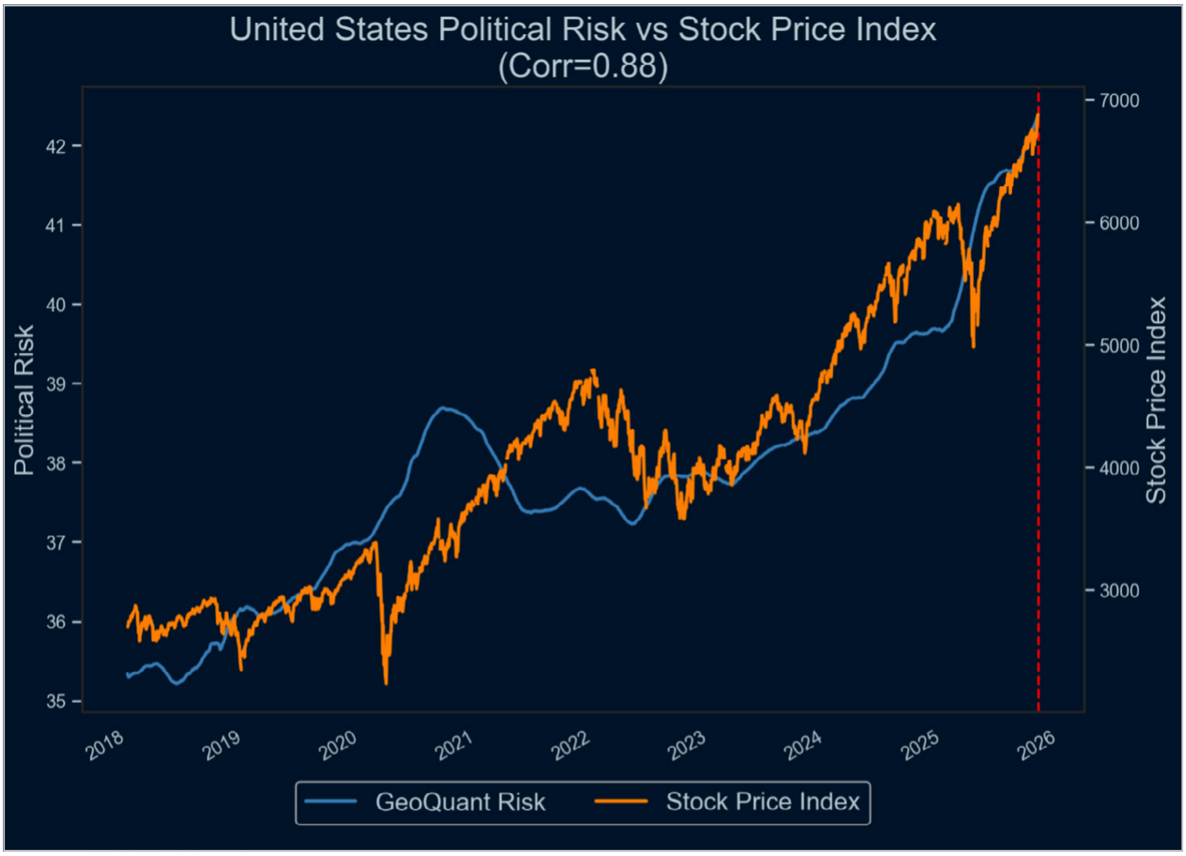
*** p<0.01, ** p<0.05 * p<0.1. Dependent variable is EMBI spread, covariates are lagged by a week, regression includes linear time trends.

For Equities, TINA still reigns supreme

Investors in U.S. equities, of course, may simply say: so what? As the There is No Alternative (TINA) crowd will remind you, the U.S. also has the world's largest and most resilient economy, home to its deepest and most liquid capital markets, reserve currency, and benchmark sovereign debt, all backed by its most powerful military. While global investors may be more exposed than ever to EM-style political risks – helter skelter protectionism, expropriation, regulatory uncertainty, distorted statistics, social instability, and so on – they also have no choice but to remain so.

Indeed, and per Figure 4, U.S. Political Risk remains strongly and positively correlated with the S&P 500, a trend that has continued in 2025 as (EM-style) opportunities from fiscal stimulus, looser monetary policy, and bets on politically favored sectors like AI and crypto fuel animal spirits. The bond market stages brief revolts – and notches brief victories – but investors continue to buy back into "American exceptionalism."

Figure 4: U.S. Political Risk vs the S&P 500 since 1 Jan 2018



Source: GeoQuant

Precarious Position

Still, the impact of EM-ification on the U.S. dollar and debt markets presents a very precarious position for the instruments that grease the wheels of the global financial system. In short, the "full faith and credit" of the government behind them less secure than any time since World War I. Just as the 2008-9 crisis in the wider U.S. housing market very quickly became a global financial crisis, now a material crisis in the American political system – say a violently contested 2026 midterm election; a prolonged government shutdown or debt ceiling breach; a constitutional crisis regarding tariffs or Fed independence; clashes between federal and local law enforcement in a major U.S. city – could trigger a similar contagion. This time, however, the U.S. sovereign will not be a haven from risk, but rather the source of risk itself.

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About GeoQuant

GeoQuant is an innovative AI-driven data and technology company, acquired by Fitch and now part of BMI, that is transforming the way the world's leading organizations are quantifying, integrating, and navigating political risk.

By fusing PhD-level political and computer science, GeoQuant generates high-frequency, quantitative measures of risk that are systematic, back-testable, and predictive.

The result is real-time updates for over 40 political risk indicators in more than 140 countries, and analytics that enable you to foresee risk trends and make proactive moves.

GeoQuant data, modelling and advisory services have been used to successfully inform the asset, risk and sovereign ESG strategies of leading institutional partners.

About BMI

In an uncertain macroeconomic environment, BMI's systematic, independent and data-driven market insights, analysis and forecasts enable you to recognize and assess risks and opportunities across 200+ markets and 20+ industries. For more than 40 years, we have provided impartial and transparent analytics, data and research across themes, countries and sectors, with deep insight into emerging markets. Our detailed intelligence is frequent, consistent and systematic, enabling you to easily make comparisons and interrogate data to support your strategic plans and investment decisions.

Learn more at fitchsolutions.com/bmi/geoquant

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