MARKET UPDATE

US-Israel War with Iran Rattles Markets

March 2, 2026

What Happened?

Israel and the US launched large-scale air strikes on Iran on February 28 with the stated goal of regime change. The first wave on the weekend targeted Iran's senior leadership and killed Ayatollah Ali Khamenei, Iran's supreme leader for more than three decades. Iran's nuclear facilities and ballistic missile infrastructure were also targeted. The Islamic Republic struck back with waves of missile and drone strikes on Israel and on US forces in the region, as well as against Saudia Arabia and Gulf countries. The war is a major escalation in the Middle East that could have unforeseen geopolitical and macroeconomic consequences.

Market Reaction: Oil and Gas

While strategic and geopolitical forces are in play, the market's primary interest is on the energy market and the world's access to oil and gas. Similar conflicts in the past have often triggered a short-term spike in energy prices, and as such, had a limited economic impact. However, since it's too soon to say how long this conflict will continue, we acknowledge the case for sustained higher energy price levels and a more negative impact on economic activity.

On Monday, oil and gas markets reacted sharply to the escalation. Brent crude prices surged by as much as 14% on Monday morning in Europe, taking oil prices up by about 29% since the start of the year. Natural gas prices in Europe and Asia soared more than 30% as Qatar shut down liquefied natural gas production following attacks by Iran, according to the Financial Times.

Energy markets are reacting to reduction of supply through the Strait of Hormuz, through which about a fifth of the world's oil and natural gas flows. The shipping lane through the strait, which runs between Iran on one side and the UAE and Oman on the other, is effectively closed. In addition, the other side of Saudi Arabia, along with the rest of the Red Sea, may be isolated if the Iran-backed Houthis in Yemen threaten the Bab el-Mandeb, the strait between the Arabian peninsula and the coast of Africa.

Mitigating that to some degree, OPEC+ countries have agreed to a small production increase of 206,000 barrels/day (compared to their 31 million barrels/day production and the globe's consumption of over 100 million barrels per day). However, this increase will only begin in April. If the Middle East conflict persists, larger increases would be needed to offset the reduction of supply. And most spare OPEC+ capacity comes from Saudi Arabia and the UAE, which could be compromised by the war.

Shift Toward a Risk Off Environment

The direct macroeconomic impact of an oil shock would be to increase inflation and weigh on economic growth for many countries. Much depends on how long the conflict persists and whether global commodity markets can offset the supply shock.

Beyond energy, we believe the war will push financial markets more broadly into risk-off mode. Global markets are already showing signs of a flight to safety. Equity markets in Asia and Europe fell by more than 1.5% on Monday. In regional markets, trading in the UAE is suspended on March 2 and 3. Shares on the Tel Aviv Stock Exchange rose on local optimism that the war could lead to a long-term reduction in regional risks. In the US, S&P futures fell by about 1.1% as of 06:20a EST. While stock markets are likely to be volatile in the short-term, our research suggests that most military conflicts have a limited long-term impact on equity returns, including the first and second US wars in Iraq in 1990 and 2003, respectively, which were more significant conflicts from the start that saw the US commit ground forces to achieve its military objectives.

Global bond-market reactions have so far been muted. 10-Year US Treasury yields had been falling ahead of the weekend, from around 4.3% in early February toward 3.9% as of Friday. The initial response to the outbreak of hostilities was a modest yield uptick; however, if risk-off conditions persist the next yield move could be down. Similarly, credit spreads have so far shown little change; if the global economy were to start feeling stress, the likely move would be a widening of spreads.

Our portfolio teams across asset classes are closely monitoring the situation in the Middle East and its potential impact on macroeconomic trends, sector and industry dynamics and company fundamentals. The impact of events transpiring in and around Iran will be weighed against the general economic backdrop for the US and other major economies, as well as the continued rapid technological revolution from AI, the combined impacts of government policies overall and the changing balance of investor sentiment.

INVESTMENT RISKS TO CONSIDER

The value of an investment can go down as well as up and investors may not get back the full amount they invested. Capital is at risk. Past performance does not guarantee future results.

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