



Ad-hoc | Middle East conflict

Our Strategy Guide for the conflict in the Middle East

For the past two weeks, the war in Iran has been almost the only topic relevant to financial markets. Even the smallest news from the Persian Gulf affects equity and bond markets via the oil price. This is unlikely to change, at least in the short term. Therefore, with this publication, we want to provide a guide on how investors can position themselves for escalation or de-escalation scenarios.

De-escalation or escalation? Developments in Iran drive financial markets

Since the beginning of the war, the oil price has become the most important variable for equity and bond markets. If the situation in Iran escalates - as it did at the end of last week when US forces bombed Kharg Island - oil prices rise as stock and bond markets fall. If Trump suggests a swift end to the war, oil as well as rates fall, while equity markets recover. Even the smallest changes in Brent affect stocks and bonds markets around.

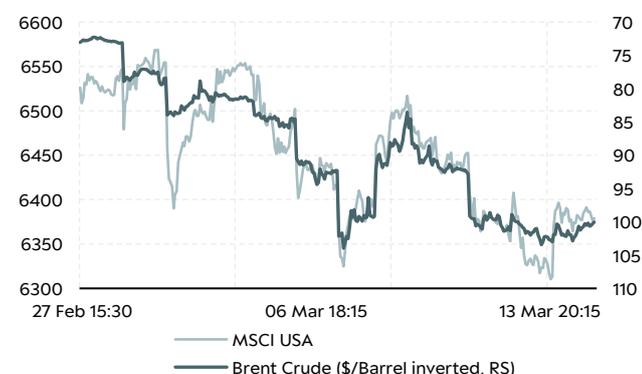
The oil price is in the drivers seat for financial markets; jobs data, inflation and other economic data indicators play only a secondary role.

Markets will continue to be dominated by whether the situation in Iran cools down or heats up even further. In the event of a further *escalation*, shipping in the Strait of Hormuz could be impaired for several months, while Iran intensifies its attacks on neighboring countries. In such a scenario, we expect oil prices to break the 2022 highs and soar well above the \$150 mark, which would further intensify the sell-off in stocks and bonds seen over the past couple of weeks.

More *positive scenarios* envision a cooling of the conflict, in which the Strait of Hormuz becomes fully passable for global shipping again in the coming weeks. A significant rise in oil prices above the \$120 mark would then be avoided. In this environment, stocks and bonds are likely to rapidly recover some of the losses from the past weeks.

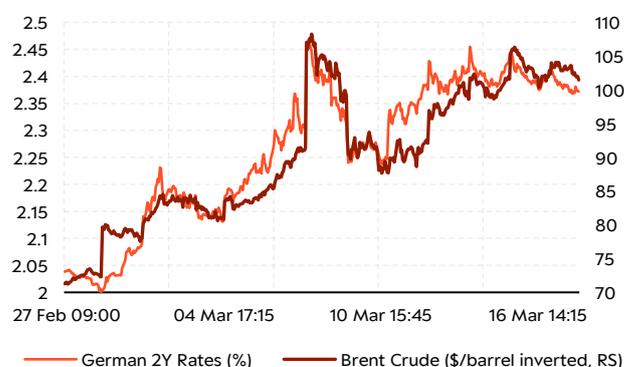
The oil price is driving both equity markets...

Intraday performance of US equities (MSCI USA) und Brent crude oil



... as well as the bond markets!

Intraday performance of 2 year German bonds and Brent crude oil



Source: Bloomberg, own calculations. Time period: 27/02/2026-17/03/2026

MSCI USA: 12-month periods over that last 5 years

17/03/25	17/03/24	17/03/23	17/03/22	17/03/21
17/03/26	17/03/25	17/03/24	17/03/23	17/03/22
11.8%	10.7%	28.6%	-8.1%	16.8%

Source: Bloomberg, own calculations. Time period: 27/02/2026-17/03/2026



De-escalation seems a bit more likely, at least from a political perspective

For the Trump administration, domestic pressure to end the war in Iran is mounting. The US military operation in Iran is relatively unpopular among the American population and is already harming the Trump administration's approval ratings. This is reflected, among other things, in the betting markets, which now expect the Democrats to win both chambers of Congress - the House of Representatives and the Senate - in the upcoming midterm elections in November. Before the conflict, the Republicans' chances of holding at least one of the two chambers looked relatively good.

Domestic pressure is mounting on the Trump administration to resolve the Iran conflict as soon as possible.

The declining popularity of the *Grand Old Party* is likely related to the rising cost of living. Diesel prices in the US have recently climbed to their highest level since 2022. But the war affects consumers not only at the pump: the increased prices for fertilizers are also likely to lead to higher food prices in the medium term.

Given the voters' frustration with the high cost of living, which was already palpable before the war broke out, President Trump thus has a strong incentive to prevent a further unwelcome price increase and to de-escalate the war in Iran quickly.

But careful: markets face a setback should de-escalation doesn't materialise

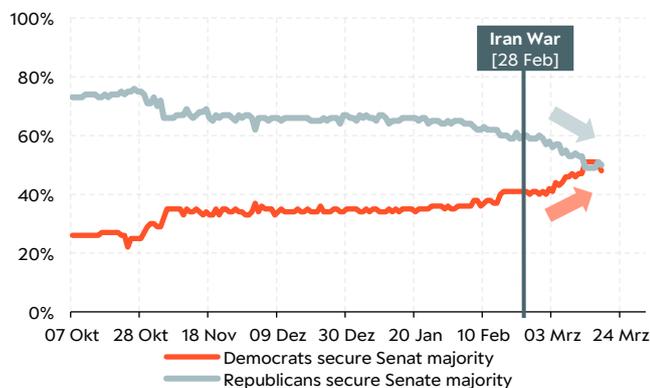
So far, markets are not pricing in a bigger economic turmoil. However, should the latter materialise, equities have more downside. The energy price shock triggered by the war in Iran and the effective closure of the Strait of Hormuz has already led to a significant setback in the stock markets. European stocks have fallen by more than 5% since the outbreak of the war, while Emerging Markets lost almost 7% since February 27. For less energy-dependent countries like the US, the loss has been more or less moderate. If the situation in Iran eases, there is potential, especially for hard-hit stocks, to price out geopolitical risks and quickly make up for some of the recent losses.

So far, the markets have not priced in any major economic upheavals. However, should such upheavals materialise, shares are likely to have even greater downside potential.

Compared to previous economic shocks, the current stock market route seems relatively slim. For example, the sell-offs after the Ukraine war or Trump's "Liberation Day" were significantly sharper. This indicates that the markets are not yet fully pricing in major economic disruptions or "worst-case scenarios". Should oil prices rise significantly again, investors should therefore brace themselves for further stock market losses.

Democrats now have a chance to secure control of the senate

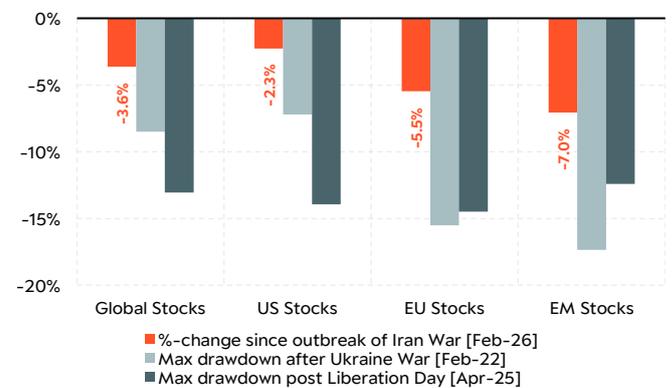
Polymarket probability of winning for the mid-term election result



Source: Bloomberg, own calculations. Time period: 06/10/2025-17/03/2026

Equities are not pricing in any major disruptions caused by Iran

Maximum drawdown in the two months following geopolitical events



Source: Bloomberg, own calculations. Time period: 01/01/2022-18/03/2026



Nevertheless, investors should not underweight equities at the moment

In the following graphic, we summarize our expectations for the two central scenarios in the Iran war. Our base scenario remains that the conflict will cool down (somewhat) in the foreseeable future and that the stock markets will reverse the sell-off of the last two weeks. To position for such a recovery rally, we would keep our equity allocation above our benchmark. Markets that have suffered particularly from the oil price shock, such as European or emerging market equities, are likely to lead such a counter-movement. Therefore, these markets remain interesting as regional overweights. At the same time, we remain overweight in oil stocks to cushion energy price spikes and balance our portfolio.

European and emerging market equities could lead a recovery rally.

However, if it becomes apparent that the Strait of Hormuz will remain closed not just for weeks but for months, portfolios would need to be positioned more defensively. On a regional level, a reallocation in favor of the US and other energy-exporting markets such as Latin America would be sensible. Bonds are likely to continue to lose value in this scenario and would still not represent a "safe haven" for investors. However, we currently see no acute need to position for such an escalation scenario.

Our strategy guide for escalation and de-escalation scenarios in the Iran war

	Scenarios for the Iran War	Market reaction over the next 1-3M		Adjustments to our Portfolio
De-escalation [Base Case]	<ul style="list-style-type: none"> Iran, Israel, and the USA jointly push for de-escalation. The Strait of Hormuz becomes passable for all tankers again by the end of March. Oil prices may rise slightly here and there but remain below \$120 per barrel. 	<p>Stocks price in de-escalation & reverse setbacks. "Losers" (=Europe) perform well.</p> <p>Bonds price in a transitory energy shock. Interest rates & USD fall.</p>	<p>Global Stocks ↑</p> <p>EU vs. US Stocks ↑</p> <p>10Y Bund Rates ↓</p> <p>Brent Crude ↓</p> <p>US-Dollar [DXY] ↓</p>	<ol style="list-style-type: none"> Maintain our slight overweight in equities; setbacks are seen as opportunities for further purchases. Regional overweights remain in Europe and Emerging Markets... also to position for a recovery rally. Energy overweight helps to cushion energy price spikes.
Escalation [Risk Case]	<ul style="list-style-type: none"> Efforts for a swift end to the war fail. Attacks on freighters and neighboring countries increase. The Strait of Hormuz remains closed into the summer. Brent crude oil rises towards \$150-\$200. 	<p>Strong equity setback. A bear market is noticeable, especially in European and parts of the Emerging Markets complex.</p> <p>Bonds price an inflation shock similar to 2022. Rates and the green back continue to rise.</p>	<p>Global Stocks ↓</p> <p>EU vs. US Stocks ↓</p> <p>10Y Bund Rates ↑</p> <p>Brent Crude ↑</p> <p>US-Dollar [DXY] ↑</p>	<ol style="list-style-type: none"> Reduction of portfolio risk and exposure toward risk assets. Shift regional overweights from Emerging Markets and Europe toward the US. LATAM markets also become interesting. Increase overweight position in energy stocks. Sectors that have already experienced a sell-off (e.g., Tech) are of interest. Increase the USD allocation.

Base Case



Publishing Information

Publisher

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