

# Bombs and barrels are driving market volatility higher



Source: AI generated

### Executive summary

Markets are navigating a convergence of a geopolitical shock and a macroeconomic inflection point. The Iran-Israel conflict has effectively closed the Strait of Hormuz to normal traffic, triggering a +35% spike in WTI crude oil prices. Yet equities, credit, and inflation expectations have remained remarkably composed — at least for now. Separately, rising fuel costs across gasoline, diesel, and jet fuel are starting to weigh on the real economy, prompting investors to ask: what has genuinely changed, and what is simply noise?

**While we remain medium-term positive on risk assets, we are slightly reducing our exposure to equities by trimming our overweight exposure to Emerging Markets and Asia, the region which is the most impacted by rising energy costs. We expect to reinvest our cash buffer once the conflict starts to de-escalate.**

## 1. Geopolitics: the Iran war

### Where do we stand?

The conflict has evolved rapidly since the initial military operations. Last week, the United States and Israel carried out coordinated strikes on several targets inside Iran, resulting in the death of Supreme Leader Ayatollah Ali Khamenei—who had led the country for nearly four decades—along with other senior regime figures. Iranian authorities responded with missile and drone attacks directed at Israel, US-associated assets, and regional infrastructure. The scale of both strikes and the retaliation have been the most significant direct escalation between the parties in years, raising concerns about wider regional involvement and potential disruptions to energy infrastructure and shipping routes.

The escalation has shifted market focus toward two key uncertainties: how long the conflict may persist and the risk of disruptions to oil flows, particularly through the Strait of Hormuz. Approximately one-fifth of global oil consumption and a substantial share of global liquefied natural gas (LNG) trade pass through this narrow waterway, making it a critical choke point for energy markets. Even without a full closure, heightened tensions can raise shipping and insurance costs and add a geopolitical risk premium to energy prices.

### The storage capacity countdown

With exports severely constrained, Gulf oil exporters face a hard physical limit: storage capacity. If crude cannot leave the Gulf and onshore tanks fill up, producers will have no choice but to halt production at some of the largest oilfields on earth. Countries most exposed include Iraq, Kuwait, the UAE, Qatar, and Saudi Arabia.

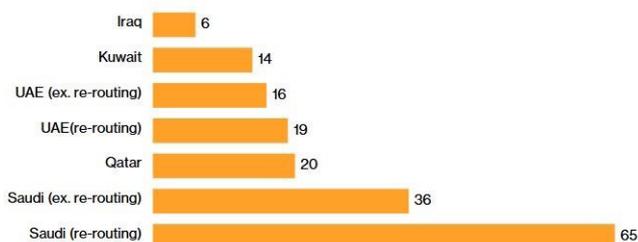
The operational detail most often overlooked: storage tanks are rarely filled beyond ~80% capacity for safety and operational reasons. This means the real countdown to forced production cuts may be considerably shorter than published figures suggest. UAE and Kuwait have already begun reducing output.

Should production shutdowns broaden, markets would not merely price in a supply disruption — they would price in structural scarcity. The economic survival of Saudi Arabia and Iraq, the first and second largest OPEC producers, would come under threat. At that point, the pressure for the war to expand becomes almost inevitable. That, in essence, is Iran's strategic calculus.

### Mideast Oil Producers Against the Clock

Hormuz halt may exhaust oil and fuel storage in weeks or days

■ Days from start of conflict until shut-in



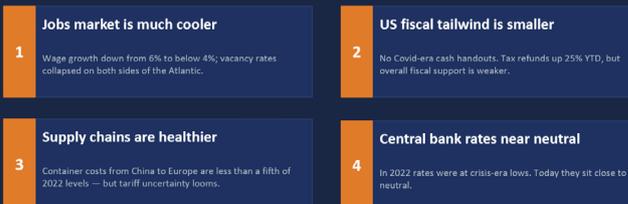
Source: JPMorgan  
Note: Re-routing denotes where Saudi Arabia and UAE have alternative options to partially by-pass Strait of Hormuz

## Is this 2022 again?

The parallel to 2022 is frequently drawn, but we believe the current macro and market context is meaningfully different. In 2022, monetary policy was in tightening mode across the board and bond yields were rising from near-zero levels. Today, the starting point for rates, valuations, and consumer balance sheets is different, and the policy response toolkit is broader — though not unlimited.

### 4 WAYS THE ECONOMY HAS CHANGED SINCE 2022

The 2022 energy crisis landed on an economy ripe for inflation. That's far less true today.



## 2. A muted market reaction — for now

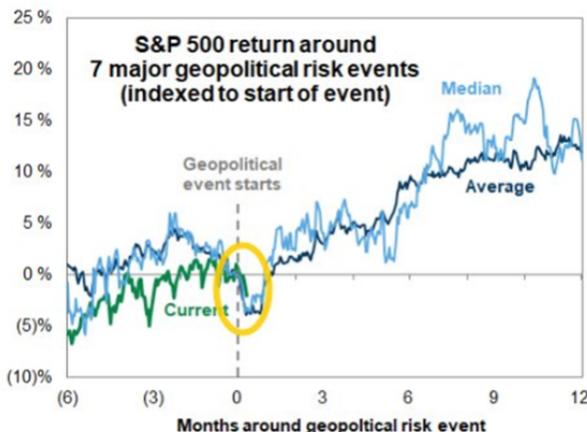
### What the data shows

The initial market response to a +35% weekly move in WTI crude has been notably subdued across most asset classes:

- › US 10-year Treasury yields: the move in crude did not drag 10-year yields higher in the fashion many expected. On a weekly regression basis, the correlation was far weaker than historical precedent.
- › Expected inflation indices (breakevens): barely moved in the first week.
- › Credit markets: spreads remained quiet, with no meaningful widening in investment-grade or high-yield.
- › S&P 500: sold off by approximately 2% following the launch of military operations — in line with historical geopolitical shock patterns. The index remains roughly 6% off its highs as of this morning.

### Context

Goldman Sachs notes that during seven spikes in the Geopolitical Risk Index since 1950, the S&P 500 fell by an average of 4% in the first week, before recovering to pre-shock levels within roughly one month. The range of outcomes, however, has been wide.



Source: Goldman Sachs Global Investment Research

## Why resilience has its limits

The market's calm should not be mistaken for immunity. Gasoline prices have risen by nearly \$0.50 per gallon over the past week, diesel by more than \$0.80, and jet fuel by over \$1.50 per gallon. These increases represent clear transmission channels to the real economy, but they typically operate with a lag. Their full impact on consumer spending, transportation costs, and corporate margins is therefore likely to take several weeks before becoming visible in hard economic data.

Meanwhile, rising short-term breakeven inflation measures are beginning to complicate the outlook for the bond market, where accommodative financial conditions remain essential to sustaining economic momentum. At the same time, expectations for Federal Reserve rate cuts in 2026 have diminished to roughly one cut, while 10-year Treasury yields have risen by about 30 basis points—although they remain within the range observed over the past eight months.

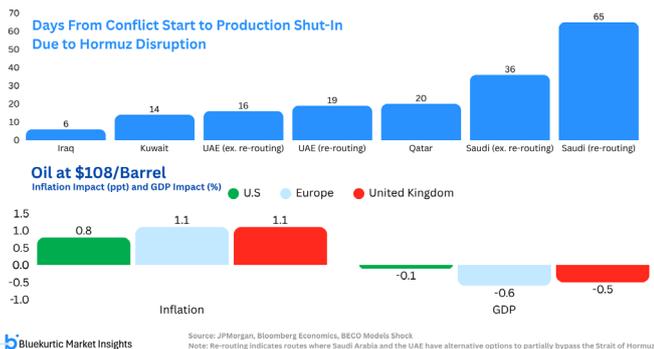
## 3. What has changed

### Energy costs & inflationary pressure

The most significant development over the past week has been the sharp rise in energy costs. Higher prices for gasoline, diesel, and jet fuel effectively act as a tax on both consumers and businesses. All else equal, this dynamic points to a slower growth trajectory and the risk of pressure on corporate margins, particularly in energy-intensive sectors such as transportation, logistics, and travel.

An increase in oil prices to around \$108 per barrel is estimated to add roughly 0.8 percentage points to US headline inflation—a meaningful impact at a time when PCE inflation measures are already proving relatively sticky.

### Oil Output Cuts and Their Impact on Inflation and GDP



### Dollar strength & the de-dollarisation debate

A stronger US dollar and a renewed flight into USD assets have significantly dampened the recent debate around de-dollarisation and tempered some of the enthusiasm for precious metals that had built earlier in the year. Data from January on official gold holdings also indicate that central banks have reduced their purchases. This marks a notable shift from a narrative that had been steadily gaining momentum.



## Rate cut expectations & bond dynamics

Expectations for Federal Reserve rate cuts over the remainder of 2026 have narrowed to roughly one cut. The roughly 30 basis point increase in 10-year yields—while still within the range observed in recent months—suggests that markets are beginning to reprice the risk of a stagflationary mix: a negative growth shock driven by higher energy costs occurring alongside an inflationary shock from rising prices.

## 4. What has not changed

### The AI capex cycle

The artificial intelligence capital expenditure cycle is expected to remain a key driver of long-term equity returns, even as the exceptional growth rates seen in 2024 begin to moderate. However, a new and still underappreciated risk is emerging. Countries that rely heavily on imported LNG for power generation could face supply shortages because of disruptions in the Strait of Hormuz. Such shortages could constrain electricity availability and potentially reduce semiconductor manufacturing output, creating broader ripple effects across the global technology supply chain.

### Private credit pressures

Concerns surrounding private credit have not disappeared. One of the key structural questions in today's market is the extent to which private equity and private credit funds have become intertwined through their shared exposure to the same portfolio companies. If signs of stress in private credit persist—as has periodically been the case over the past year—it would likely imply that private equity valuations also need to adjust downward. Such adjustments tend to occur gradually and often in a slow, opaque, and potentially disorderly manner.



## The labour market remains intact — for now

Initial jobless claims remained relatively low last week, and corporate earnings estimates have so far proven resilient. One week of data is not sufficient to trigger meaningful revisions to earnings forecasts, although adjustments could begin to emerge in the coming weeks. The latest payroll report does point to some early signs of softening, but not yet to the degree that would shift the macro consensus toward a recessionary outlook.

## 5. What comes next: key variables to watch

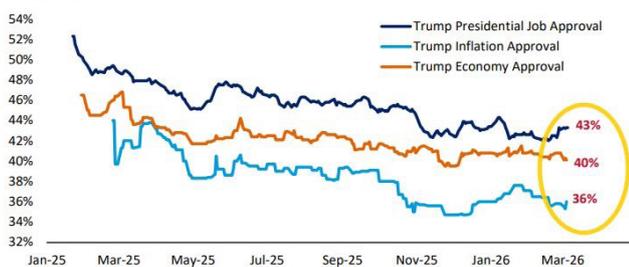
### Energy supply continuity

If oil and LNG exports resume without significant physical disruption, the recent surge in prices may gradually ease as the geopolitical risk premium fades. However, if infrastructure damage or shipping disruptions prove sustained—particularly if Gulf producers are forced into production halts—energy prices could remain structurally elevated, reinforcing global inflationary pressures beyond the near term.

### Duration of the conflict

A brief and contained episode could mirror previous regional flare-ups, where volatility subsided once immediate risks faded. A prolonged confrontation—especially one involving additional regional actors or broader disruption to Hormuz shipping lanes—would increase the probability of more persistent inflationary pressure and extended market volatility. The political dynamics around Trump's approval ratings—40% on the economy and 36% on inflation, both near their lows—suggest that gasoline prices at the pump may ultimately be the forcing function that brings the US administration toward a ceasefire position.

**Chart 2: Bulls need a Q2 recovery in Trump approval ratings**  
Trump job approval rating and approval on inflation & economy



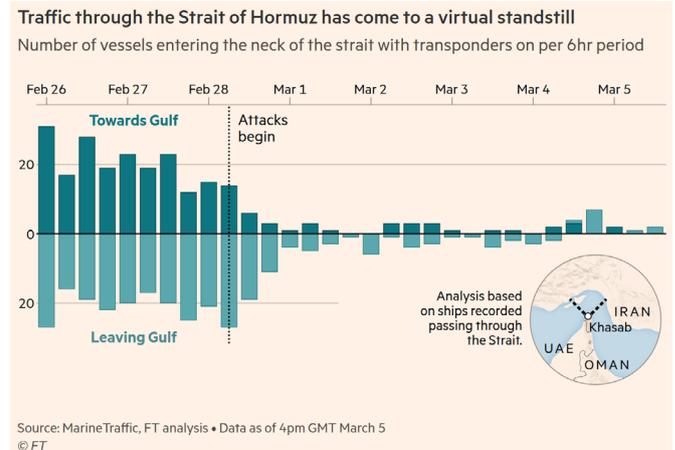
Source: BofA Global Investment Strategy, Bloomberg, Real Clear Politics

BofA GLOBAL RESEARCH

### The insurance crisis

Recent reports suggest advisers around Trump are urging the administration to prepare an exit strategy from a potential conflict with Iran, citing rising oil prices and growing political pressure tied to a prolonged war. The reasoning is straightforward: the war ends, oil prices stabilise and shipping resumes. But the mechanics of global energy

markets are more complicated. On 5 March, seven major Protection & Indemnity (P&I) insurance clubs in London withdrew war-risk coverage for ships transiting the Strait of Hormuz. The move was not driven by politics; it was driven by regulation and risk modelling.



Under the European insurance framework known as Solvency II, insurers must hold capital sufficient to cover extreme loss scenarios at a 99.5% confidence level. With missile strikes, drone attacks, and vessel incidents occurring in one of the world's most critical maritime choke-points, insurers' capital requirements surged beyond what many clubs were willing or able to sustain. Coverage was therefore withdrawn.

The key point is that insurance markets do not reopen when political leaders declare a ceasefire. Coverage typically returns only after actuarial models show that the probability of incidents has returned to normal levels. Historically, that process can take 12 to 24 months after hostilities end.

Even if a ceasefire were announced tomorrow, insurance markets could remain constrained, tanker operators might still struggle to secure coverage and as much as 20% of global seaborne crude flows could remain commercially restricted. This helps explain why oil continues to trade near \$90 per barrel, rather than returning to the roughly \$70 pre-conflict range, despite periodic signals of de-escalation.

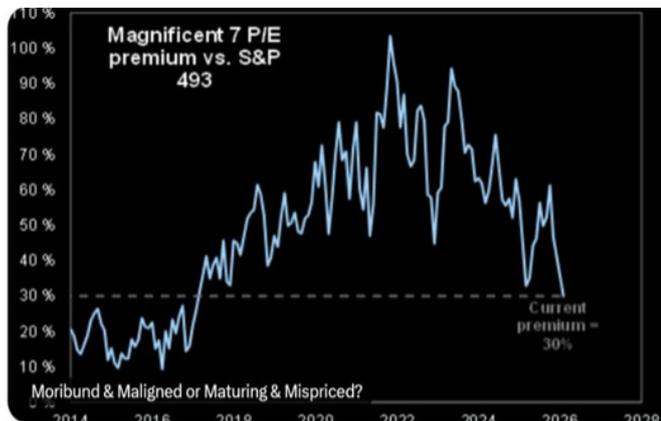
In effect, markets are not pricing the duration of the war. They are pricing the duration of the insurance disruption.

Wars can end through political decisions. Insurance crises end only when actuarial data confirms that risk has declined. For policymakers in Washington, that distinction matters. While the administration recently announced a \$20 billion reinsurance backstop, industry analysts say the measure does little to address the core constraint: insurers remain bound by Solvency II capital rules and elevated modelled risk in the Strait.

Until those models change, shipping—and the oil market—may remain constrained long after the fighting stops.

### The return of 'buy growth when growth is scarce'

If slower growth becomes the consensus view over the next six months, a familiar dynamic is likely to reassert itself: investors paying a premium for companies that can compound earnings regardless of the macro environment. That dynamic could quickly revive the Magnificent Seven trade, which showed early signs of reasserting itself last week. It would also refocus attention on the technology sector—one of the areas that has experienced the most notable multiple compression in 2025.



From zerohedge.com

### Recession risk — still early, but worth monitoring

It feels too early to seriously discuss recession. However, three historical instances of sharp oil price spikes preceded recessions by roughly one year: the 1973 oil embargo, the 1979 Iranian Revolution, and the 1990 Gulf War. That is not a forecast—it is a tail risk worth tracking. Vulnerabilities in global energy infrastructure could also keep oil prices structurally higher than pre-conflict levels, with broader implications for growth and inflation expectations well beyond the near term.

## 6. Investment conclusions & house view

### THE BIG PICTURE

The United States is facing simultaneous pressure on growth and inflation. Measures of inflation based on the Personal Consumption Expenditures Price Index remain stubbornly elevated, while rising energy costs are beginning to weigh on both consumer spending and corporate margins.

For now, we are not increasing our probability estimate of a US recession or stagflation in 2026, which remains at 20%.

A short-term spike in energy prices can still be absorbed by the economy, particularly if households temporarily reduce their savings rate to sustain spending.

However, the margin for adjustment is narrowing. It would not take a significant additional shock for those recession or stagflation probabilities to begin rising.

From a market perspective, the timeline is tightening: the Middle East supply situation could become critical within a matter of weeks if current pressures persist.

### VIEW

*Financial conditions have not tightened significantly yet. The S&P 500 remains approximately 17% higher over the past year and is just 3–6% below all-time highs. We recommend staying invested and well diversified.*

### Near-term positioning

With visibility around the duration of the conflict and the short-term price behaviour of oil being very limited at this stage, we decided to realign our model portfolios closer to our Strategic Asset Allocation (SAA). We are therefore reducing our exposure to Emerging Markets and Asian equities from overweight to neutral. Overall, we are now neutral on equities, underweight fixed income, overweight commodities and gold and neutral hedge funds. We also keep our neutral stance on the dollar.

### Longer-term outlook

Most indicators continue to point to healthy US and global activity. It would require a large and sustained spike in oil—not merely the initial shock—to materially derail the broader growth story. Geopolitical shocks of this scale often trigger sharp short-term repricing but do not always lead to lasting structural changes. The average performance of the S&P 500 following the start of a conflict tends to be range-bound in the immediate aftermath, before recovering.

We remain constructive on the longer-term outlook for growth and corporate profitability. At the same time, we acknowledge that the combination of factors in play—geopolitical risk, energy price sensitivity, private credit fragility, and AI capex dependency on stable energy supply—makes staying open to scenario shifts more important than it has been for some time.

## 7. THE WEIGHT OF THE EVIDENCE

Our asset allocation preferences are based on 5 indicators, including 4 macro and fundamental indicators (leading) and 1 market dynamics (coincident). The weight of the evidence suggests a constructive view on equities (positive). Below we review the main drivers for each of them.

Negative -	Neutral =	Positive +
	Macro Cycle	
	Liquidity	
		Earnings Growth
	Valuations	
	Market Factors	

- ▶ **Macro cycle (from positive to moderately positive):** Recent developments surrounding the Iran crisis have led us to slightly temper our macroeconomic outlook. Although fundamental economic data have remained broadly positive in recent weeks, the overall outlook has weakened somewhat. Coordinated strikes by the United States and Israel against Iran, followed by Iran's retaliation, have pushed global energy prices higher. The recent surge in oil prices—Brent and WTI crude both moving above \$100 per barrel—has increased the risk of a meaningful negative impact on global growth and inflation.

While the United States is now better insulated from energy price shocks than during previous energy crises, rising inflation expectations reduce the likelihood of the two Federal Reserve rate cuts that financial markets had previously priced in for this year. A similar dynamic is visible in the Eurozone, but to an even greater extent: market expectations have shifted toward fully pricing in an ECB rate hike this year. Higher energy prices effectively act as a tax on consumers, transferring income to energy producers. This dynamic ultimately weighs on economic growth while adding upward pressure to inflation.

For the time being, we still believe the US administration under President Trump has strong incentives to bring the conflict with Iran to an end—sooner rather than later. Persistently elevated energy prices could erode voter support for the Republican Party and President Trump ahead of the midterm elections in November, now just eight months away. Nevertheless, uncertainty surrounding the evolution of the crisis and its potential impact on energy markets has increased significantly.

Overall, while we still expect a global environment characterised by positive growth and moderate inflation—including in major financial market economies such as the United States, the Eurozone, Japan, and the United Kingdom—the outlook has become somewhat less favourable since the escalation of the Iran crisis. As a result, we are downgrading our macro pillar assessment by one notch, from positive to moderately positive.

- ▶ **Liquidity (from positive to moderately positive):** We are downgrading our liquidity pillar to moderately positive following the latest developments. Expectations for interest rate cuts in the United States have declined, while in the Eurozone the probability of a policy pivot toward rate hikes has increased. A more “hawkish” monetary policy outlook—meaning a less expansionary or potentially more restrictive stance—tends to be less supportive for overall market liquidity.

Despite these adjustments, both pillar 1 and pillar 2 remain in positive territory, although our assessment is now somewhat less constructive than at the time of the last Investment Committee meeting a week ago.

- ▶ **Earnings growth (still positive):** Earnings remain a tailwind for equities with more sectors to show earnings growth improvement. Technology stocks will continue to benefit from the adoption of AI, while the “old economy” is set to recover from a low base.
- ▶ **Valuations (still neutral):** US large cap stocks trade significantly above their 10-year averages, while international equities trade at a discount vs. the US. However, equity risk premium remains low in both the US and Europe.
- ▶ **Market factors (from positive to moderately positive):** While US indicators remained stable in positive territory, European indicators somewhat deteriorated over the week, with half of it in negative territory. Technical indicators were downgraded, as well as market breadth. Indicators with lower frequency (trend) remained in positive territory.

As a result, the signal is less constructive than a week ago.

## Asset Allocation Grid - Tactical Asset Allocation (TAA) – 9 March 2026

The weight of the evidence lead us to cut our stance on equities from overweight to neutral.

With 3 pillars being slightly downgraded (macro, liquidity and market factors), the weight of the evidence – which is the combination of the 5 pillars – has slightly deteriorated since our last TAA meeting.

Within our asset allocation grids, we are thus aligning our equity weights closer to our Strategic Asset Allocation (SAA), leading us to reducing Emerging Markets and Asian Equities from overweight to neutral and slightly reducing our local equities exposure to neutral.

	Underweight -	Neutral =	Overweight +
<b>Asset Classes</b>		Cash	
		Equities	←
	Fixed Income		
		Alternatives	
<b>Fixed Income</b>	Govies 1-10		
	Govies 10+		
		Corporate IG (local)	
		High Yield (local / global hdg)	
		EM Debt	
<b>Equity</b>		United States	
		Eurozone	
		UK	
		Switzerland	
		Japan	
		Emerging Markets	←
		China	
		Hedge Funds	
<b>Commodities</b>			Gold Commodities
<b>Forex (vs. USD)</b>		EUR	
		CHF	
		GBP	
		JPY	
		EM Currencies	

← → Arrows show our latest TAA moves.

# Welcome to Syzerland®

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