

Disruptions

Geopolitical disruptions often spill over into market sentiment if not outright trends. It may be too early to assess the impact of the most recent attack by the U.S. and Israel on Iran and the counterattacks by Iran on many of its Middle East neighbors. Nevertheless, assessing the most immediate as well as intermediate may provide insight into which trends will dominate in the post-disruption period. Disruptions result in relative “winners” and “losers”. The determination thereof may come well-after the disruption events themselves. As a result, changes in investment strategy may be best deferred from some periods of disruption. On the other hand, more immediate strategy changes may be warranted if one is to fully benefit from the changes rendered. Changes from past periods of disruption may provide some insights into future investment strategy improvements.

Q PERSPECTIVE

Stock market returns following periods of geopolitical disruption are shown in [Table I](#) for the Dow Jones Industrial Average (“DJIA”). While returns were volatile, they were not consistently so. This was true for all three time periods measured. Similarly, there was no consistency of return patterns within periods, i.e., prior period returns did not set the stage for returns in subsequent periods. While the largest return after one quarter was -13% following the Iraqi invasion of Kuwait, one-quarter had the largest number of positive returns across the periods of disruption measured. Investors have been hard-pressed to find insights for equity allocation strategy from this analysis of disruption periods.

Bond market yield changes following periods of geopolitical disruption are shown in [Table II](#) for 10-Year U.S. Treasury bonds. “Flight to quality” is an investor sentiment often associated with periods of adverse market uncertainty. Reflecting this uncertainty is a perceived investor preference for higher quality investments such as Treasury bonds. The actual outcomes for the periods shown are not consistent with this anticipated relationship. Policymakers are believed to be active in periods of geopolitical disruption. Under more extreme circumstances, the Federal Reserve may become outright buyers of Treasury Bonds, putting downward pressure on yields. Again outcomes have not supported this expectation, leaving investors hard-pressed to find bond allocation strategy insights.

The periods of geopolitical disruption shown in [Table III](#) all are ones in which foreign countries are in turmoil. The U.S. is pulled into each one either directly or by proxy. Differences among currency level changes tend to reflect perceptions of relative risk and opportunity. Differences can reflect as well actions being taken by central banks. Here, central banks tend to be more active and the outstanding currency balances of foreign banks are much lower than that of the U.S. Federal Reserve. As a result, their impact can be greater but offsets from the U.S. may be larger per amount of currency expended. The relative stability of the U.S. dollar amidst periods of geopolitical uncertainty has offered little guidance for portfolio allocation strategy during such periods.

INVESTMENT IMPLICATIONS

Investors once again find themselves in a period of geopolitical disruption. While still early in this period, the search is on for investment strategy guidance including portfolio asset allocations. Reviews of trends in stock market returns, bond market yields and relative currency levels from prior periods of geopolitical disruption appear to offer limited strategy value. Nevertheless, such periods generally are ones of higher market volatility. Managing this volatility by matching individual portfolio risk tolerance with expected portfolio risk levels is more important than ever during periods of disruption.

TABLE I

DJIA RETURN FOLLOWING GEOPOLITICAL DISRUPTION				
EVENT	DATE	ONE DAY	ONE MONTH	ONE QUARTER
Cuban Missile Crisis	10/23/1962	1.8%	13.3%	19.1%
Oil Embargo	10/16/1973	-0.5%	-7.9%	4.1%
Iraq Invades Kuwait	8/2/1990	-1.9%	-7.8%	-13.0%
September 11	9/11/2001	-7.1%	-2.0%	2.9%
Iraq War Begins	3/20/2003	2.8%	0.6%	11.0%
Russia Invades Crimea	2/20/2014	-0.2%	1.2%	1.5%
Houthis Attack Saudi Arabia	9/15/2019	0.1%	-0.2%	3.9%
Russia Invades Ukraine	2/24/2022	2.5%	4.4%	-3.9%
U.S./Israel Attack Iran	2/26/2026	-0.6%	?	?

TABLE II

TREASURY BOND YIELD CHANGE FOLLOWING GEOPOLITICAL DISRUPTION				
EVENT	DATE	ONE DAY	ONE MONTH	ONE QUARTER
Cuban Missile Crisis	10/23/1962	0.0%	-0.2%	-0.6%
Oil Embargo	10/16/1973	0.1%	-0.1%	0.2%
Iraq Invades Kuwait	8/2/1990	0.2%	0.5%	0.2%
September 11	9/11/2001	-0.2%	-0.1%	0.3%
Iraq War Begins	3/20/2003	0.1%	-0.3%	0.2%
Russia Invades Crimea	2/20/2014	0.0%	0.0%	-0.2%
Houthis Attack Saudi Arabia	9/15/2019	0.0%	-0.1%	-0.3%
Russia Invades Ukraine	2/24/2022	0.0%	0.4%	0.8%
U.S./Israel Attack Iran	2/26/2026	-0.1%	?	?

TABLE III

U.S. DOLLAR CHANGE FOLLOWING GEOPOLITICAL DISRUPTION				
EVENT	DATE	ONE DAY	ONE MONTH	ONE QUARTER
September 11	9/11/2001	0.0%	0.0%	0.5%
Iraq War Begins	3/20/2003	0.0%	-0.2%	-0.5%
Russia Invades Crimea	2/20/2014	0.0%	0.0%	-1.0%
Houthis Attack Saudi Arabia	9/15/2019	0.0%	0.0%	-0.9%
Russia Invades Ukraine	2/24/2022	-0.6%	0.0%	0.2%
U.S./Israel Attack Iran	2/26/2026	0.0%	?	?