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Four signals to track as geopolitical risk rises



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Geopolitical shocks rarely disrupt markets for long – unless they spill into the real economy. In today’s environment, investors should closely monitor four signals that determine whether geopolitical tension becomes meaningful market stress.

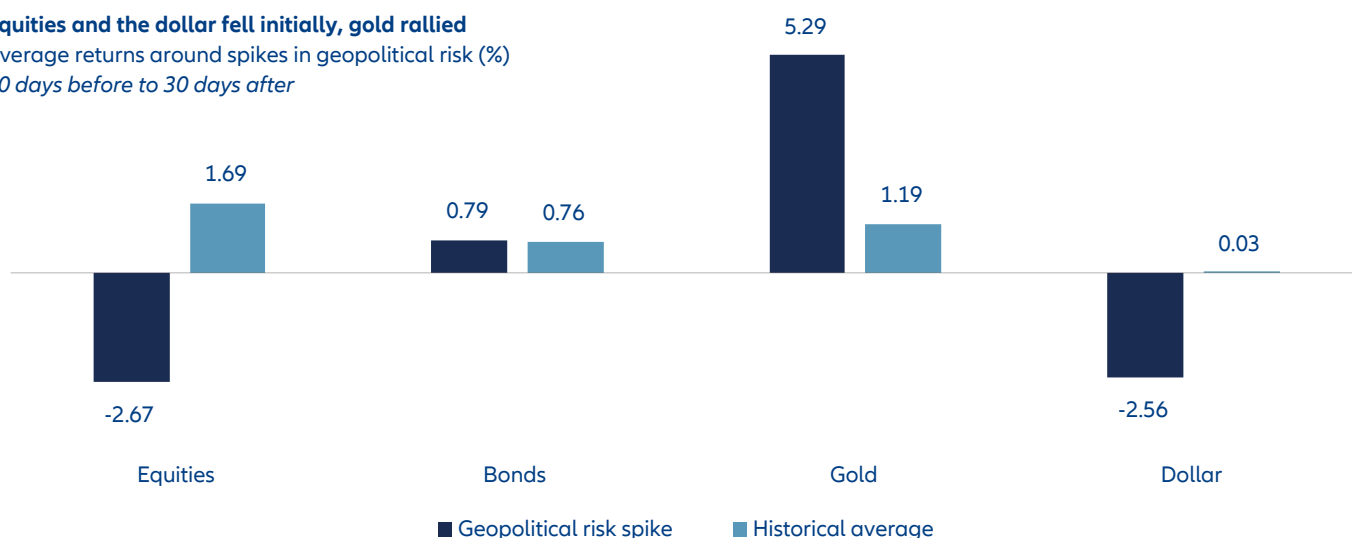
Geopolitical upheavals have become a defining feature of the global landscape, from regional conflicts to terrorist attacks and abrupt leadership crises. The latest Middle East war has again thrust geopolitical risk to the forefront of investors’ minds (see Exhibit 1, overleaf). But how much do these shocks really matter for markets – and how can investors recognise the moments when geopolitics start to matter for portfolios?

Key takeaways

- Our research based on seven decades of market history indicates that most geopolitical shocks are short-lived, but markets react more sharply when spillovers raise recession risk through energy, supply chains, sentiment or financial conditions.
- Oil spikes, tightening financial conditions and weakened confidence have historically been the clearest triggers of deeper and more persistent market corrections.
- Investors should focus less on geopolitical headlines and more on the real-economy signals that determine whether volatility becomes something more lasting.

Exhibit 2: Markets typically recover quickly following geopolitical shocks**Equities and the dollar fell initially, gold rallied**

Average returns around spikes in geopolitical risk (%)
30 days before to 30 days after



Note: Based on 10 episodes since 1990 in which the Geopolitical Risk Index (Caldara/Iacoviello) exceeded 1.5 standard deviations above its long-term mean. Equities = S&P500 total return, Bonds = US Treasuries (ICE BofA GOQ0), Gold (GFC XAU D), Dollar (DXY US dollar index).

Source: Allianz Global Investors Global Economics & Strategy, Bloomberg, Global Financial Database (GFD), Bank of America, Dario Caldara and Matteo Iacoviello (<https://matteoiacoviello.com/gpr.htm>), data as of 17 March 2026. Past performance is not an indicator of future results.

First, the good news: most shocks shake markets, but rarely break them

Geopolitical shocks tend to trigger abrupt but short-lived market reactions. On average over the past 35 years, spikes in the Geopolitical Risk Index led to a brief risk-off move, with equities falling, while government bonds – especially US Treasuries – and gold typically rise (see Exhibit 2).

These moves usually fade quickly. Historical evidence shows that equities have tended to recoup losses within two months, the US dollar partly recovers, and bonds and gold hold modest gains. Importantly, cross-asset correlations remain broadly stable, meaning that traditional diversification continues to work even during periods of acute geopolitical tension.

In short, while geopolitical news flow can spark bouts of volatility, markets usually look through them unless deeper economic forces take hold.

When geopolitics *does* matter: oil shocks and recessions

Although most of the 49 geopolitical episodes left only a faint and temporary mark, some had far more significant consequences. Two factors stand out over the past seven decades as defining the difference between short-term turbulence and more persistent market stress:

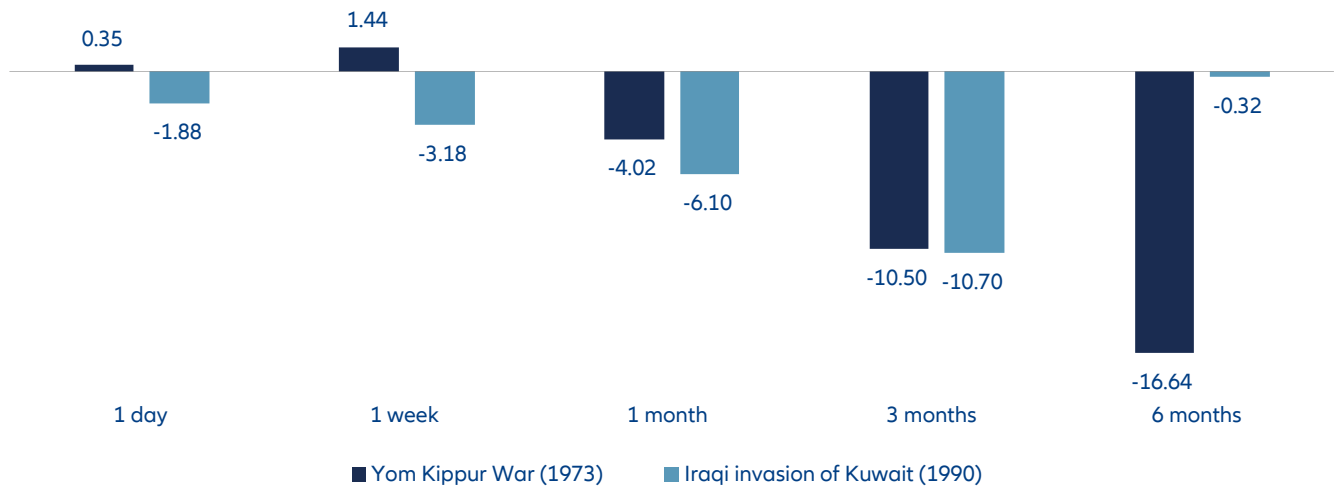
1. Sharp oil price spikes

Some of the most damaging episodes – such as the Yom Kippur War in 1973 and Iraq's invasion of Kuwait in 1990 – were accompanied by sharp increases in oil prices, often 50% or more within months. These supply shocks pushed inflation higher, squeezed consumers and businesses, and contributed to economic downturns.

Today, the current Middle East war has again put energy markets at the centre of investor attention. While oil prices have risen meaningfully, history suggests the key

Exhibit 3: Equity drawdowns are deeper during oil-price spikes and recessions

Average returns following events with oil price shock and recession (%)



Source: Allianz Global Investors Global Economics & Strategy, Bloomberg. US equity returns based on S&P 500 total return index (S&P 500 price return index until 1/1988). A significant oil price rise (WTI) is defined as an increase by at least 50% within six months.

question is whether price pressures continue to escalate enough to threaten global growth. This is the pattern that has distinguished short-lived volatility from more persistent market corrections in past episodes – and it remains a critical signal for investors to monitor now.

2. Real-economy spillovers leading to recession

When geopolitical shocks feed through into wider economic stress – through weaker confidence, tighter financial conditions, or supply-chain disruptions to energy or other key commodities – equities tend to underperform for much longer (see Exhibit 3). Historical analysis shows that whether a recession begins within six or 12 months, equity markets have struggled in these environments.

These two factors – energy supply shocks and rising recession risk – proved to be the real tipping points. Without them, most geopolitical events faded from market pricing relatively swiftly.

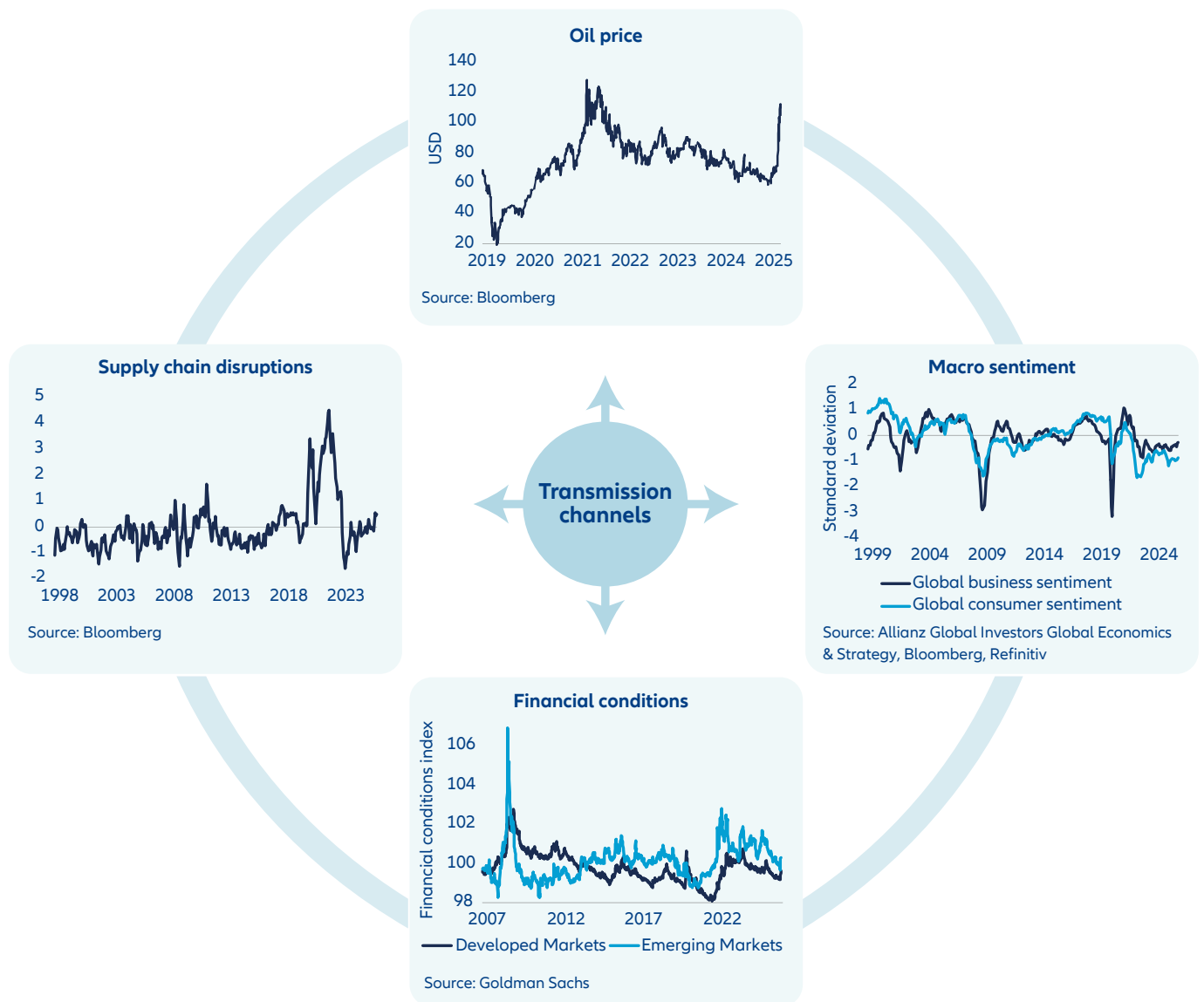
Safe havens behave differently depending on the depth of the shock

Understanding these dynamics helps explain why some assets protect portfolios better than others during heightened geopolitical stress. Our research highlights clear distinctions across safe-haven assets:

- Gold delivers the most consistent protection. It performed especially well in episodes where rising geopolitical risk coincided with recessions.
- US Treasuries tend to generate modest gains on average, but their strongest performance occurs when the US Federal Reserve cuts rates in response to underlying economic weakness.
- The US dollar often moves sideways during the initial shock but typically appreciates over a three- to six-month window during more severe downturns or elevated geopolitical stress.

These dynamics reflect investors’ search first for stability, and then for yield, in times of elevated uncertainty.

Exhibit 4: Four transmission channels to watch for potential global economic fallout



How shocks spill into the real economy

Ultimately, these are the four signals that determine whether geopolitics becomes a significant market-moving force – and they are exactly the indicators investors should be tracking now (see Exhibit 4):

- Oil and broader energy shocks** – historically, large oil price increases have been a necessary (though not sufficient) precursor to US recessions and remain a key risk factor even in a less energy-intensive global economy.
- Supply-chain disruptions** – geopolitical tensions increasingly threaten intermediate inputs such as helium, sulphur, fertiliser and aluminium, with potential global knock-on effects.

- Tightening financial conditions** – falling asset prices, central bank rate hikes, stronger safe-haven currencies and tighter lending standards can all amplify weakness and expose financial stability risks.
- Worsening macroeconomic sentiment** – persistent stress often weighs on business and consumer confidence, eventually feeding through to weaker activity and slower growth or recession.

In severe episodes, several of these channels interact simultaneously, increasing the risk of more durable downturns.

Implications for today's environment

Recent weeks have seen an unusual alignment: equities, bonds and gold have all declined, while the US dollar has strengthened. Historically, this pattern is uncommon, suggesting markets may be pricing in elements of stagflation risk or adjusting to stretched valuations.

If tensions ease, the historical record suggests that losses could unwind relatively quickly. But if the conflict

persists – especially if oil prices stay elevated and supply-chain disruptions broaden – the risk of deeper and longer-lasting corrections increases. Investors should therefore closely monitor developments across the key transmission channels.

While diversification has historically been a robust strategy in periods of geopolitical stress, a regime with persistently positive cross-asset correlations would require more active and flexible risk management.

Conclusion: history doesn't repeat, but it rhymes

Seven decades of geopolitical shocks offer a clear message: geopolitical events tend to move markets less than the headlines imply. Most shocks are absorbed quickly unless they trigger broader economic spillovers. But when those spillovers raise recession risks through energy price spikes, supply chain strains, souring macroeconomic sentiment or tighter financial conditions, markets react more forcefully.

With global uncertainty elevated, investors should remain vigilant – focusing not on the headlines themselves, but on whether geopolitical turmoil is beginning to reshape the underlying economic landscape.

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