Market Event Update

23 October 2023

Israel-Hamas Conflict

On 8 October 2023, Israel declared war against Hamas after the Gaza-based militant group launched a surprise attack on Israel.

As expected in periods of uncertainty, the initial response from markets had a risk-off tone, with investors turning to 'safe-haven' assets like government bonds, gold and the United States (US) dollar. The oil price also jumped due to the region's relevance to global production, while share markets fell slightly. However, this response was relatively short-lived, with markets somewhat muted ever since and most of these initial moves reversing except for the oil price, which has remained elevated.

Despite the unquestionable human tragedy, other forces have been more relevant to markets since the conflict began. As they have been all year, investors have been focused on the likelihood of further central bank interest rate rises, how persistent inflation will be, and how resilient economic growth will remain.

If the conflict remains contained, these other factors will continue to drive markets. If the conflict were to escalate and spread into a broader regional problem, this could result in the oil price increasing further and potentially trigger more meaningful 'risk off' market moves. Authorities worldwide, including the US Government, are making a concerted effort to prevent this from happening.

Although we continue to monitor the situation closely, we do not believe the Israel-Hamas conflict warrants any change to our long-term investment strategy.

Instead, we remain focused on three possible scenarios for the global economy that are most relevant to markets over the short-to-medium-term (while acknowledging an escalation in the conflict could play into these scenarios):

1. Soft landing — Higher interest rates get inflation under control without causing a recession.

2. Hard landing — Higher interest rates cause a deep recession and collapse in demand.

3. Persistent inflation — Inflation is more persistent than expected, and central banks have to move interest rates higher for longer.

In an environment of heightened uncertainty, such as the current one, we want to build portfolios that can remain resilient in a range of scenarios. With this in mind, we maintain a quality bias within equity exposures and continue to add to high-quality government bonds, which should be defensive in a risk-off environment.

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