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Markets under stress test: Where volatility creates opportunity

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The war in Iran increases uncertainty, but not all market reactions are fundamentally justified. The sell-off in short-term rates appears exaggerated and opens opportunities to reduce portfolio risks. As in 2022, gold has so far disappointed—and if rate hikes fail to materialize, this could present a buying opportunity. The war also reminds us that energy and supply security remain structural core themes, with corresponding opportunities for long-term investors. In addition to equities, such themes can also be represented through select infrastructure and private equity investments.

Markets responded with relief to US President Donald Trump's announcement that he is postponing the deadline for targeted strikes against Iran's energy infrastructure by five days, citing good progress toward a possible resolution of the conflict. The details of these talks remain unclear, however, with the Iranian side denying they have taken place. What is clear is that sharply rising gasoline prices are weighing on US consumers and the government's political approval. The war is thus also imposing costs on the American side, which may be influencing the president's calculations.

At the same time, memories of 2022 are resurfacing: Russia's attack on Ukraine also led to rising energy prices, inflation concerns, and fears of further rate hikes. Even if an agreement is reached soon, it will likely take longer for energy and goods exports to fully normalize due to substantial infrastructure damage. Accordingly, there has recently been a sell-off in both short- and long-term bonds—partly because markets expect various central banks to raise rates, and partly because increased spending and subsidies to ensure energy supply and security could lead to higher deficits.

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The extent of economic damage depends on the duration of the conflict. Equity markets, in particular, continue to assume this is a temporary escalation—not least because the US, Europe, and China have a strong interest in avoiding a prolonged energy shock. However, the risk is rising that the uncertain situation around the Strait of Hormuz will persist, with elevated energy prices increasingly burdening the global economy. The Iranian leadership appears to have realized that the trade blockade exerts considerable economic pressure and can improve its negotiating position in any potential ceasefire discussions.

This uncertainty is only partially priced into the markets. While widespread panic has not yet occurred, initial distortions are visible beneath the surface. These provide tactical and structural opportunities for investors:

First, short-term yields in the bond markets have spiked in anticipation of rate hikes, but we don't expect central banks to raise them. While it is conceivable that central banks may wait and see in this environment, history shows that monetary policy measures are of little help in supply shocks. This creates an opportunity for investors to tactically invest in short-term bonds to reduce risk—especially where equity allocations are currently too high. We see attractive opportunities in the euro area in particular.

Second, the market also assumes that these rate hikes will lead to higher opportunity costs, which typically weigh on the gold price. Since we do not expect rate hikes, we see attractive entry points at current levels—not only for gold, but also for commodities in general.

Third, the conflict in the Middle East reinforces long-term trends: the need for energy independence, supply security, and strategic sovereignty. We expect many countries to invest even more in the future to better prepare for upcoming crises. Infrastructure investments and select private equity investments can meaningfully complement portfolios. In the current zero and low interest rate environment, such investments can at least partially be financed by reducing bond allocations.

Against this backdrop, nuclear energy is likely to regain focus in energy policy. It offers a stable, low-CO_2, and domestic energy source—qualities that are gaining importance in the current situation. Despite the risks, political support appears to be increasing worldwide, and rising investor interest reflects this potential paradigm shift.

Conclusion: In the short term, uncertainty remains high, and the likelihood of an economic crisis increases with each week that energy and goods exports through the Strait of Hormuz remain disrupted. Further price declines—especially in equities—are therefore conceivable, making cautious, tactical risk management a priority. Especially with elevated equity allocations, investors should consider how best to hedge their portfolios.

Increased volatility, temporarily higher interest rates, and the market correction make structured strategies attractive, in our view, both for hedging portfolio risks and for generating income. However, it should also be noted that the situation could normalize relatively quickly. This creates interesting opportunities to consistently exploit the tactical and structural opportunities mentioned above, positioning the portfolio to be both more resilient and future-proof.

Appendix

Non-traditional asset classes are alternative investments that include hedge funds, private equity, private credit, real estate, and managed futures (collectively, alternative investments). Interests of alternative investment funds are sold only to qualified investors, and only by means of offering documents that include information about the risks, performance and expenses of alternative investment funds, and which clients are urged to read carefully before subscribing and retain. **An investment in an alternative investment fund is speculative and involves significant risks.**

Specifically, these investments (1) are not mutual funds and are not subject to the same regulatory requirements as mutual funds; (2) may have performance that is volatile, and investors may lose all or a substantial amount of their investment; (3) may engage in leverage and other speculative investment practices that may increase the risk of investment loss; (4) are long-term, illiquid investments, there is generally no secondary market for the interests of a fund, and none is expected to develop; (5) interests of alternative investment funds typically will be illiquid and subject to restrictions on transfer; (6) may not be required to provide periodic pricing or valuation information to investors; (7) generally involve complex tax strategies and there may be delays in distributing tax information to investors; (8) are subject to high fees, including management fees and other fees and expenses, all of which will reduce profits.

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In addition to the risks that apply to alternative investments generally, the following are additional risks related to an investment in these strategies:

- **Hedge Fund Risk:** There are risks specifically associated with investing in hedge funds, which may include risks associated with investing in short sales, options, small-cap stocks, "junk bonds," derivatives, distressed securities, non-U.S. securities and illiquid investments.
- **Managed Futures:** There are risks specifically associated with investing in managed futures programs. For example, not all managers focus on all strategies at all times, and managed futures strategies may have material directional elements.
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- **Private Equity:** There are risks specifically associated with investing in private equity. Capital calls can be made on short notice, and the failure to meet capital calls can result in significant adverse consequences including, but not limited to, a total loss of investment.
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