

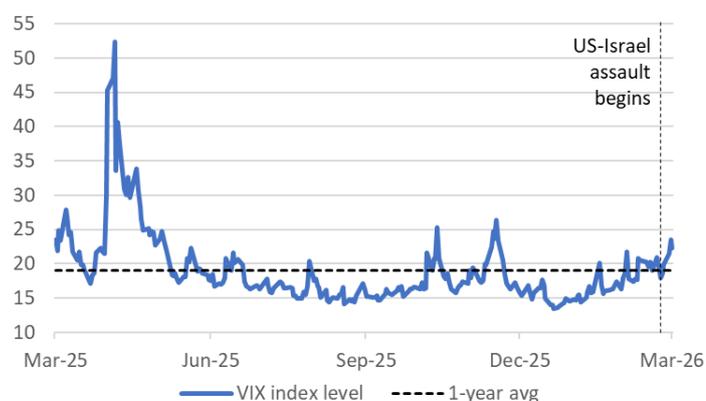
Volatility returns

5 March 2026

The surface calm of markets has been disrupted by an escalation of conflict in the Middle East. Oil prices and overall volatility have spiked, but we remain confident in the long-term prospects for well-diversified portfolios.

I began writing before the US-Israel assault on Iran. It's tempting to rip everything up and to make it all about the consequences of this escalating conflict, but that would be a mistake. Numerous forces act on markets like unseen tides. They might not be visible today, but they shouldn't be ignored. There are also many unknowns about the current conflict, not least how long it might last, and it's fast-moving in nature.

Figure 1: Volatility rises to the surface



Source: Factset, VIX market volatility as of 4 Mar 2026

Quick take:

- Oil prices, overall market volatility have spiked on Middle East conflict.
- We note other continuing influences including AI-disruption, tariff fears.
- And we remain confident that well-diversified portfolios will go up over a longer-term investment horizon.

The Iran war

Even so, we have to start by addressing the key risks for investors from these developments. While sensitive to the humanitarian costs of war, we have a responsibility to make judgements about economic and financial effects.

As we noted in the latest update of our report on major geopolitical risks, [Peace of Mind in a Dangerous World](#), the focus will be almost exclusively on oil and gas prices, as is the case whenever hostilities break out in the region.

There are two strands to analyse: production and transportation. Iran itself produces around 4.5% of global crude oil. If that supply was taken off the market other Opec countries would have

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sufficient spare capacity to make up the shortfall. So far, at least, Iran has not been successful in disrupting other countries' production capabilities either. At the time of writing, there is enough oil coming out of the ground to satisfy demand.

The bigger potential problem is getting it to consumers. In this regard the Strait of Hormuz, a narrow channel between Iran and Oman, is a crucial transportation bottleneck. Around a fifth of global oil and (liquified natural) gas supplies are shifted through it daily, so any closure would be extremely disruptive.

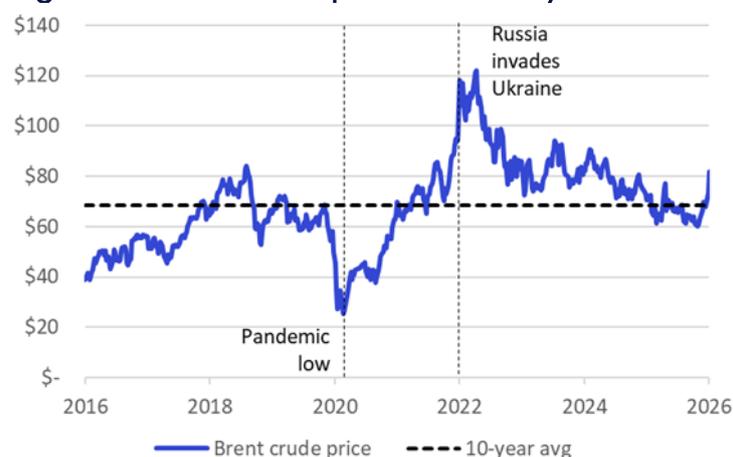
The price of a barrel of Brent crude oil had been rising steadily since January in anticipation of war in the region. From \$60 at the beginning of January, it had reached \$70 before any missiles had been fired and now trades at \$83. If \$60 was the 'undisturbed' price, then traders are effectively paying a \$23 'risk premium' today. To put that in context, the average of the past ten years is \$73.75, ranging from an intra-day low of \$19 during the pandemic and high of \$128 immediately after Russia invaded Ukraine (figure 1).

At the time of writing, the Strait is not 'closed' as such, but shipping has been greatly disrupted as insurers either withdraw cover or make it punitively expensive to sail through.

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Unsurprisingly, independent operators are unwilling to subject their crews to the danger. The only reported cargoes flowing through the Strait are on some national carriers and Chinese tankers.

Figure 2: Brent crude prices over 10 years



Source: Factset; weekly prices, as of 4 March 2026

China is a big net importer of oil and gas and Iran is a key supplier. Iran is highly dependent on oil-based revenues, as are its neighbours who have been targeted with Iranian missiles. And President Trump will be keenly aware that higher inflation could weigh on the performance of the Republican Party in November's mid-term elections. So the vested interests in keeping shipping lanes open suggest that any blockage should be short-lived.

Analysts at US bank Goldman Sachs calculate that \$80 oil is discounting up to six weeks of shipping disruption.

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But what happens if there's a longer closure? The price of a barrel of oil in that case could jump to more than \$100, and possibly even higher in the very short term. That has consequences for inflation, particularly for net oil and gas importers like the UK and Europe. Higher energy prices can depress economic activity by diverting expenditure from other sectors. But if already-sticky inflation starts rising again, this would make it even more difficult for central banks to cut interest rates faster.

Markets have tended to bounce back quite quickly from most event-driven sell-offs. But the exceptions are sell-offs with an extended period of higher energy prices. The worst ones were caused by supply disruptions. For example, the 1973 Arab oil embargo, the 1979 Iranian revolution (when Iran had a much bigger share of global output than today), and 2022's Russian invasion of Ukraine.

Another AI scare

Even before Iran jumped to the top of the investment agenda, there were more than enough things to keep investors on their toes. There are the perceived economic and societal threats from accelerating development of generative artificial intelligence (AI) and the tools that it can help to create (see my recent [Weekly Digest](#) that focussed on this). A blog post from an unregulated research company,

detailing a theoretical AI-related collapse in the labour market from the retrospective viewpoint of 2028, caused a big stir in February. Markets have often been resilient in the face of genuine bad news, but in this case were upset by what was literally a work of fiction.

As we also reported in the most recent [Digest](#), although volatility had not been apparent on the surface of markets, there have been some monumental shifts below the waterline. Market-watchers have coined a new acronym for companies that seen as safe from AI disruption: Halo, which stands for hard assets, low (risk of) obsolescence. Think 'stuff' rather than easy-to-copy computer code. We believe that solid research can unearth valuable opportunities from the indiscriminate selling of supposedly vulnerable companies, as they prove their resilience.

Scotus vs Potus

The US Supreme Court (Scotus) caught markets on the hop by ruling 6-3 that President Trump's (Potus') IEEPA tariffs were illegal. The full implications aren't clear yet, especially since the decision about refunding tariffs already collected (around \$175bn) has been deferred to a lower court. And this is far from the end of the tariff story. There are other ways for President Trump to impose tariffs, as we also outlined in last week's [Digest](#). He immediately went down the route of

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the 1974 Trade Act's Section 122, which allows universal tariffs of up to 15% for 150 days to address deficits in the balance of international transactions.

The fact that the Supreme Court delivered this ruling is a reason for optimism, showing it's not in hock to the White House as many feared. Two Trump appointees ruled against him, much to his displeasure. It appears the checks and balances that protect the Constitution are not in complete disrepair. Indeed, we have seen more vocal opposition to Trump's policies from within his own party recently, though the lack of pushback from corporate America remains a concern.

A strong earnings season

Despite this malaise, global equity indices ended the month (before the Iran news) very close to their all-time highs – probably a pleasant surprise to anyone following news headlines but not financial markets. Strong earnings growth has been a key support. Reporting so far for the final quarter of 2025 has shown year-on-year earnings growth at around 10% globally.

Conclusion: process and discipline

The investment horizon is a distant one, whereas markets are highly reactive. In most cases the best course of action has been to remain fully invested (and keep investing) even as prices swing violently around longer-term upward trends.

Indiscriminate selling can also provide level-headed investors with opportunity. It's not possible to predict major geopolitical risks and their impact on investments, but [we are prepared for them](#). A key part of this is constructing portfolios resilient to shocks, with some element of insurance against the worst outcomes. This means that balanced portfolios are well-diversified across asset classes. And this is the time for the 'boring' constituents to prove their worth.

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Regional highlights

US. Experience suggested the consensus forecast of year-on-year profit growth in the S&P 500 of around 7% for the final quarter of last year would be beaten. The question was, by how much? With around 90% of results in the bag, the final number looks as though it will come in at around 14%. There had been lingering concerns that, for example, tariff liabilities might weigh on margins, but US corporate managers have once again found the means to mitigate cost pressures. Although the technology sector has been at the epicentre of this year's market earthquakes, it's 31% earnings growth is still top of the sector tables. The next highest-growing sector was materials (26%), testament to the demand for the raw materials required to fulfil current capex plans. Industrials (14%) was another beneficiary, as the sector that provides the necessary components, services and equipment. Interestingly, two of the better performing sectors so far this year, energy and healthcare, posted the weakest earnings growth (1% and flat, respectively). Both have benefitted from the rotation towards sectors deemed less liable to AI disruption. Consensus expectations for 2026 suggest overall US earnings growth of 15% this year.

UK. Coming into the reporting season, earnings growth for 2025 was expected to be around 5%, with a stronger pound reducing the value of overseas profits when translated back to sterling.

The average exchange rate was \$1.32 in 2025 vs \$1.28 in 2024. But earnings growth is coming in above expectations, with the banking sector leading the way. Energy and basic resources companies were the other main beneficiaries of positive cyclical tailwinds. Current consensus estimates for 2026 suggest closer to 10% earnings growth. That might be subject to revision in the current environment, but the FTSE 100 does have a greater diversity of leadership (excluding the technology sector) than many other markets. That lends it some safety appeal.

Europe. With the euro having risen around 10% against the dollar last year, European company earnings were fighting a currency headwind. Although they did exceed expectations, 4% growth versus 2% estimates was not as convincing a beat as in the US. Even so, the growth gap between the US and Europe is slowly shrinking.

Among the sectors of meaningful size, financials was the big winner, posting growth of 19%. The banking sector enjoyed many of the same tailwinds as its US peer group. It's taken a few testing periods for them to prove their worth, but European banks seem finally to have shaken off the bad reputation they acquired during the global financial and eurozone crises. Looking to 2026, the consensus forecast of 12% earnings growth is expected to further narrow Europe's gap versus the US.

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Emerging markets. Granular earnings data is not as readily available, but headline growth is strong here too. Consensus forecasts for 2026 suggest more than 30%. A big chunk of that is attributable to Asian technology companies. Some of the biggest winners from the demand for data centre investment are Taiwanese and South Korean chip makers. Chinese e-commerce companies such as Alibaba are also prospering again. There were concerns that US tariffs would weigh more heavily on emerging market activity, but an increase in trade between these emerging countries has been a positive counterweight. Collectively, they weathered both the pandemic and the dramatic tightening of financial conditions in 2022 with fewer fiscal liabilities than developed markets. They then increased interest rates more quickly to head off inflation. That leaves them well placed to prosper over the longer run, with the main caveat over the shorter term being a reliance on energy imports.

Fixed Income. The Bloomberg Global Aggregate Bond Dollar Index gained 2.1% in February (1.7% for the sterling-hedged version). Yields started to fall again as investors saw some risk to economic growth from the disruptive AI threat. UK gilts were given a boost by two windfalls. Capital gains tax receipts were surprisingly high from sales of assets ahead of what was expected to be a stringent debut Labour Budget in October 2024. Lower-than-expected inflation also reduced the interest payable on index-linked

gilts. This reduced the required debt issuance this year. However, events in the Middle East threaten to lower growth (and associated taxes) and increase inflation (leading to higher payments on index-linked gilts). The potential inflationary shock from rising energy prices, as well as reduced expectations for interest-rate cuts this year, led to a sharp sell-off in government bonds at the beginning of March. This underpins our preference for minimal duration exposure, so that we benefit from still decent short-term interest rates without exposing ourselves to the greater volatility of longer-dated bonds.

The All UK Conventional Gilts index delivered a total return of 2.5% over the last three months and 5.7% over the past year. Index-linked gilts returned 4.9% and 4.3% over the same respective periods. Emerging market bonds produced a total return of 6.3% in sterling over the three months to the end of February (16.4% over 12 months). Global high yield bonds delivered 1.6% (6.4% over 12 months) in sterling terms.

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