momentum
global investment management

April 2024

Israel Retaliates

implications for investors

As clearly signalled, and against the wishes of its key allies, Israel has retaliated against Iran's attack of April 13th, and worryingly has chosen the more aggressive approach of a direct attack on Iran rather than on its proxies. While details are currently sketchy, we provide some perspective on the implications for investors:

1. The fears of a broadening conflict, drawing in not just Middle Eastern countries but also the great powers, have been raised.

2. While not a zero risk, we do not believe the doomsayers are correct in predicting a much broader conflict and WWIII.

3. It is plainly in no-one's interests to escalate war. Other than rogue states, the Iranian regime has few friends in the Middle East or beyond and is woefully prepared with a dated and poor air defence system that is years behind that of Israel, a message highlighted on April 13th. Unlike Israel it does not yet possess the ultimate deterrent of nuclear arms.

4. Israel, on the other hand, has its hands full with the unfinished war in Gaza and the fight against Iran's proxies. The West is doing its best to calm matters and prevent further escalation, and the response to Iran's attack on Israel was a clear demonstration of a) the clear and continuing dominance of the US militarily and its ability to apply that anywhere of its choosing; and b) when the chips are down, Israel has the full support of the US, UK, France and other key allies in the West.

5. The early response by Iran to the attack appears to support our view that the latest developments are unlikely to result in a broader conflict. The leadership appears to be playing down the impact of the strikes, and the damage inflicted seems to be modest – Israel could clearly have chosen to be much more aggressive, that it has not provides some reassurance about its intent.

6. If our assessment is correct, the main implication for investors of the instability in the Middle East will be its impact on energy prices. This remains a risk, with potentially reduced supplies from Iran if Western sanctions are intensified, and further disruption to shipping in the Gulf. This comes at a time when the improving economic picture and tight supplies from the OPEC+ group of producers are leading to a deficit in oil this year, and this could complicate the task of central banks in their battle to return inflation to targets. However, we see this as a containable risk, mitigated substantially by the record levels of production of oil in the US and the steady reduction globally of dependence on oil.

7. Whatever the outcome of the conflict in the Middle East, it is rarely, if ever, wise to build an investment strategy around geopolitical risks. Aside from their inherent unpredictability, history shows that they are rarely long-lasting, a solution is eventually found.

8. We do not ignore these risks, and we carry tail risk insurance against them in the form of gold, which has proven to be very effective this year, but we continue to build our portfolios on the basis of valuations and long term expectations.

9. The reaction of markets to date understandably reflects nervousness, but it is notable that after an initial spike, the oil price is broadly unchanged and while equity markets are weak, it needs to be remembered that by the end of March they had moved up by 25% from their October 2023 lows and in our view had run ahead of the fundamentals; a period of consolidation was overdue. The key to performance will be the factors which have dominated this cycle so far – inflation, growth and the Fed's policy moves.

10. Our approach is therefore not to react to the heightened risks in the Middle East, but to maintain a broadly diversified approach to asset allocation, including safe-haven assets alongside those offering real growth potential, and take opportunities of weakness in markets triggered by events such as these today, to add to risk assets on weakness.

Important Notes - This document is only intended for use by the original recipient, either a Momentum Global Investment Management Limited (MGIM) client or prospective client, and does not constitute investment advice or an offer or solicitation to buy or sell. This document is not intended for use or distribution by any person in any jurisdiction in which it is not authorised or permitted, or to anyone who would be an unlawful recipient. The original recipient is solely responsible for any actions in further distributing this document, and in doing so should be satisfied that there is no breach of local legislation or regulation. This document should not be reproduced or distributed except via original recipients acting as professional intermediaries. This document is not for distribution in the United States. Any opinions expressed herein are those at the date this document is issued. Data, models and other statistics are sourced from our own records, unless otherwise stated. We believe that the information contained is from reliable sources, but we do not guarantee the relevance, accuracy or completeness thereof.

Unless otherwise provided under UK law, MGIM does not accept liability for irrelevant, inaccurate or incomplete information contained, or for the correctness of opinions expressed. The value of investments in discretionary accounts, and the income derived, may fluctuate and it is possible that an investor may incur losses, including a loss of the principal invested. Past performance is not indicative of future performance. Investors whose reference currency differs from that in which the underlying assets are invested may be subject to exchange rate movements that alter the value of their investments. MGIM (Company Registration No. 3733094) has its registered office at The Rex Building, 62 QueenStreet, London EC4R 1EB. MGIM is authorised and regulated by the Financial Conduct Authority in the United Kingdom (registration no.232357)and is exempt from the requirements of section 7(1) of the Financial Advisory and Intermediary Services Act 37 of 2002 (FAIS) in South Africa, in terms of the FSCA FAIS Notice 141 of 2021 (published 15 December 2021). For complaints relating to MGIM's financial services, please contact distributionservices@momentum.co.uk.© MGIM 2024.