We recognize the profound human consequences of military conflict and hope for outcomes that prioritize stability, peace, and the protection of civilians. This update is intended primarily to assess the market, policy, and investment implications of recent developments in Iran and the Middle East. It does not take a political position on these events. As fiduciaries, our responsibility is to provide objective analysis for our clients.

What happened?

- Early on Saturday, February 28, Israel and the U.S. launched joint military air strikes on Iran. Subsequent retaliation by Iran has seen the conflict impact other countries across the region. T. Rowe Price has both staff and clients in the region, and our primary concern is their safety and well-being.

- Speculation over the potential for military action had intensified in recent weeks as the U.S. built up its military presence in the region to levels not seen since the 2003 invasion of Iraq.

- Geopolitical tensions had been escalating around Iran's nuclear program, wider military arsenal, and a crackdown by the regime on civilians following protests earlier in February. The move to military action came despite attempts at negotiation on these matters over recent weeks between U.S. and Iranian representatives.

- Iran's supreme leader, Ayatollah Ali Khamenei, was killed in Saturday's air strikes, with Israel and the U.S. calling for regime change.

- Iranian retaliation involved attacks on Israel, Jordan, Iraq, as well as several Gulf Cooperation Council (GCC) countries, including Saudi Arabia, the United Arab Emirates (UAE), Qatar, and Bahrain. Iranian strikes in the past typically have been limited to Israel and U.S. bases in the region, but this round has expanded to include civilian infrastructure in neighboring countries.

- The situation remains fast-moving and highly fluid, and tensions are high. Uncertainty remains as to the potential duration of the conflict and the range of longer-term outcomes.

What are the initial market and economic implications?

- The initial market reaction was a rise in the price of oil. Crude had already been climbing in recent weeks as markets weighed the U.S. military buildup in the region and the growing risk of conflict.

- The price rises came despite an announcement by the Organization of the Petroleum Exporting Countries (OPEC), of an increase in production quotas starting in April, to help quell the extent of oil price rises.

- Gold and the U.S. dollar strengthened early Monday as investors sought traditional safe-haven assets.

- Asian and European equities came under some pressure in early trading amid rising risk aversion. Volatility is to be expected across global equity markets as investors weigh implications of the conflict.

- Regional bond markets in the Middle East were also under pressure on Monday, with yields rising across the board.

What are the developments to watch?

- As of writing, military strikes across the region were continuing. Tensions remain elevated with no signs of de-escalation. The conflict will remain an immediate source of concern for investors and likely contribute to volatility for commodity prices and global equity and bond markets.

- With the death of Supreme Leader Ayatollah Ali Khamenei, how the political situation in Iran evolves will shape the extent, duration, and outcomes of the conflict. Corresponding geopolitical tensions and the potential for local and regional unrest will add to uncertainty.

- A prolonged regional conflict that sustains the risk of disruption to the production and shipment of oil and liquefied natural gas from the region would have the biggest impact on energy prices and equities that are sensitive to them. To date, Iranian attacks have focused on U.S. military bases and civilian infrastructure—including airports, hotels, and ports—while energy infrastructure has mostly been spared.

- The Strait of Hormuz is a narrow waterway between Oman and Iran, through which roughly 20% of the world's seaborne oil travels on its way to market. Disruptions to energy production in the region and to shipments via the Strait of Hormuz will sustain upward pressure on oil prices in the near term, despite OPEC production pledges.

- Pressures may moderate over time, as higher oil prices weigh on consumption and spur spare or short-cycle oil and gas production to come onstream. The United Arab Emirates and Saudi Arabia have capabilities to circumvent the Strait for a large share of their exports. That is not the case for Iraq and Kuwait.

- Countries within the Gulf Cooperation Council generally maintain strong financial buffers that can help weather periods of stress. Many have balance sheet strength to help safeguard the foreign exchange regime, public finances, and the banking sector during times of volatility. The large sovereign wealth of Qatar, Saudi Arabia, the United Arab Emirates, and Kuwait is largely held abroad and remains at the disposal of the state.