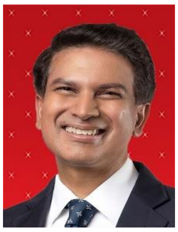
Macro Insights Weekly

Middle East tensions and global implications

Group Research | **June 16, 2025**



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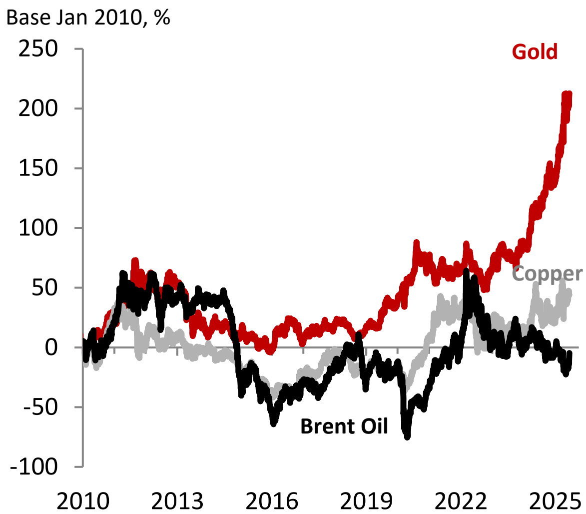
- *Israel-Iran conflict is a gravely worrisome development. Over a spectrum of adverse to extremely adverse outcomes, the market is so far inclined to coalesce around the less dire possibilities.*
- *Middle Eastern wars in the 1980s and 90s did not lead to prolonged oil shocks.*
- *Presently, global demand weakness is a bigger worry over supply constraints.*
- *Nonetheless, energy supply through the Straits of Hormuz could be potentially disrupted.*
- *The US could also be dragged into the conflict.*
- *Under such scenarios, energy prices will be much higher than what's priced in presently.*

Chart of the Week: War and commodities

The developments out of the Middle East over the past few days threaten regional stability gravely. Risks notwithstanding, global market response has been measured, with the jump in oil or selloff in equities suggesting only a modest degree of risk aversion. Gold at all-time high and bitcoin also near record territory reflect broader geoeconomic risk perceptions, in our view. The long-simmering Israel-Iran conflict reaching a major chapter should add to market stress, but so far, the view is global spillover risks are manageable.

Brent Oil vs Copper vs Gold

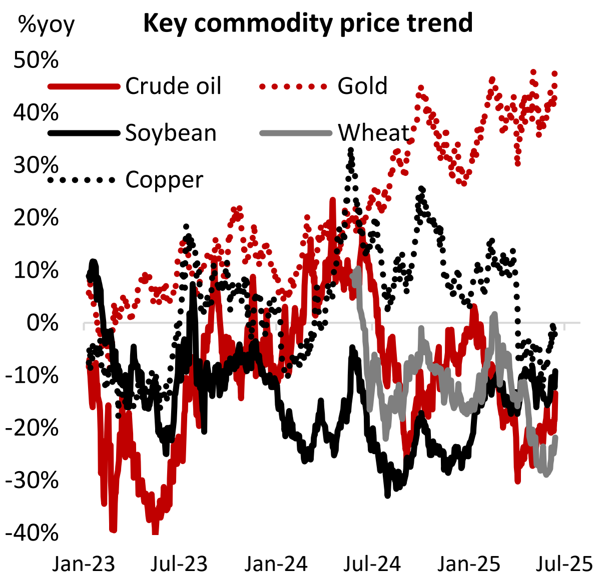


Source: Bloomberg, DBS

Commentary: Middle East tensions and global implications

The uncertainty around the Israel-Iran conflict is considerable and many scenarios are plausible in the coming days, but hardly any of them is positive. Over a spectrum of adverse to extremely adverse outcomes, we note that the market is so far inclined to coalesce around the less dire possibilities.

Looking at the movement of risk assets so far, we find the market's response centred around expectations of a short-duration conflagration, ending with a weakened Iran and an emboldened Israel, with some sort of settlement facilitated by the US. The fact that the Iraq-Iran war during the 1980s and associated disruptions to oil/gas supply/production did not cause 1970s -style oil shock may well be informing the market's composure. Even the 1990/91 Iraqi invasion of Kuwait and subsequent oil field fires did not amount to a prolonged period of high oil prices. Coming at a time when global demand softness is a greater source of worry than supply tightness, the bar for a major oil rally is high.



Source: Bloomberg, DBS

While hoping the market's view is the right one, which is that no oil shock is about to transpire, **it is important to recognise the criticality of the conflict-afflicted region at stake**. Iran sits at a global chokepoint of energy supply, disrupting which remains in its arsenal of options in the middle of an armed conflagration.

Gas and oil, crude and refined, are shipped from the ports of Persian Gulf through the narrow Straits of Hormuz from a number of countries, including Bahrain, Iran, Iraq, Kuwait, Qatar, Saudi Arabia (East coast), and the United Arab Emirates. About a fifth of the world's oil consumption passes through the Straits. All of Qatar's LNG exports go through it as well. **Most the energy flowing from this region is bound for Asia.**

Iran's ability to restrict energy shipment through the Straits is substantial but constrained nonetheless, given the substantial US Navy presence, based out of Bahrain, in those waters. US also maintains a major air force base in Qatar.

Substantial presence and interest in the region also add to the risk of the US being drawn into the conflict. The desire to keep oil prices from spiking and keeping US allies secure may lead to a much broader conflict, with American troops being deployed in numbers not seen since the war against Iraq. Donald Trump only recently gave a speech about his desire to keep US military involvement out of the Middle East; he may have to reverse his position.

Taimur Baig

Base and bear case oil price scenarios

Scenario 1: Base Case

What may transpire: Limited strike scenario, Iran response is calibrated but flare up does not extend beyond a few days, US-Iran tensions do not blow up, trade routes remain largely unaffected.

Assumption: Higher level of geopolitical risks than the levels prevailing since end-2024, some uncertainty will continue to prevail in oil markets in near term leading to volatility. Spikes above USD75/bbl possible, but not sustained in our view, given the OPEC+ production cut reversals and trade war related demand fears.

Oil price trading range: USD65-75/bbl

Scenario 2: Escalation

What may transpire: Heavier than expected retaliation from Iran, either directly or through proxy players, but full-scale regional conflict prevented by global diplomatic efforts

Assumption: Tighter sanctions on Iran oil exports as Iran gets directly involved, or Iran oil infra could get hit, which could reduce global oil supplies by up to 1.5mmbpd and raise fears of market disruption. Saudi will likely not intervene in the market unless oil prices are well above USD100/bbl.

Oil price trading range: USD75-100+/bbl

Scenario 3: Prolonged Conflict

What may transpire: Full-scale prolonged conflict between Israel and Iran envelops other countries in the region, drawing response from the US and other western powers if US assets in region are targeted.

Assumption: Conflict could damage oil infrastructure in the region and lead to blockages of key chokepoints in the Gulf of Persia like the Strait of Hormuz. Spikes of above USD150/bbl possible in the worst-case scenario.

Oil price trading range: USD100-150+/bbl

Suvro Sarkar

FX: Short-term USD respite on Mideast risks

The USD, which remains weak in the medium term, should get some respite on the escalating Israel-Iran conflict. The base case remains a case of continued hostility without full-scale war, though the risk of miscalculation is high. G7 leaders are gathering for a summit in Canada. However, the lack of a joint G7 communique underscored divisions between the EU's desire for a unified front to push for a ceasefire vs. a unilateral pro-Israel US stance that did not favour US military intervention. Outside the G7, Russia and China backed Iran, condemned Israel's strikes on Iran, and viewed the fractured West as incapable of providing collective leadership to maintain global order. The Red Seas, Straits of Hormuz, and Gulf oil infrastructure remained key chokepoints that could lift global oil prices.

Canada extended invitations to several key non-G7 countries – India, Australia, Brazil, Mexico, South Africa, and South Korea – to facilitate bilateral talks with the US to lay the foundation of future trade deals after the summit. However, the Mideast conflict will likely become a distraction that risks politicising trade, raising oil prices that hurt emerging markets with high energy import bills, highlighting the lack of US global leadership, and fuelling questions about aligning with the US-led trade framework. Brent crude oil prices rose another 2% to above USD75.80 per barrel this morning after last Friday's 7% spike.

The FOMC meeting on 18 June will remain important. Although we see the Fed keeping rates unchanged at 4.50% for the fourth consecutive meeting, the futures market is hopeful of the Fed lowering rates in September. According to the New York Fed's survey, inflation expectations declined across the 1-year, 3Y, and 5Y horizons. Tariffs did not lift US CPI inflation higher. Core inflation slowed to 0.1% MoM in May vs. the consensus for an increase of 0.3% from 0.2% in April. US President Donald Trump could inject volatility and hurt the USD by pressing the Fed to lower rates aggressively and making good on his threat to announce a dovish successor to Fed Chair Jerome Powell, whose term expires in May 2026. The DXY Index is caught between staying subdued in a 97.5-98.5 range on the Fed or returning into this month's earlier 98.4-99.4 range on higher oil prices.

GBP/USD has a soft bias within its three-week range of 1.3450-1.3630 after failing to break decisively above 1.36. We expect the Bank of England to keep the bank rate unchanged at 4.50% at its June 19 meeting. But the monetary policy committee could signal another rate cut at the August meeting. On June 19, UK CPI inflation should ease to 3.5% YoY in May from 3.5% YoY in April, to 3.5% from 3.8% for core inflation, and to 4.8% from 4.8% for services inflation.

JPY and CHF to become less of a haven amid the Mideast crisis. On June 17, The Bank of Japan should affirm expectations for a delayed rate hike to 4Q25. On June 19, The Swiss National Bank should seize the opportunity to discourage the CHF's haven appeal by cutting rates to 0% while leaving the door open for negative rates in 2H25. Against rising commodity prices, the AUD, NZD, and CAD could find support but find it hard to shake off global growth fears from a possible oil shock.

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