Manulife
Investment Management

Market Note

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Recent geopolitical tensions involving Iran have renewed focus on oil prices and their potential economic and market effects. Paul Kalogirou, Head of Client Portfolio Management, Asia & Global Multi-Asset Solutions, shares latest views on it.

Economic and market implications for oil prices

What can higher oil prices mean for the economy and markets?

Geopolitical risks often cause periodic market volatility, but over time they have generally had limited long-term market implications. Oil is often at the epic-center of heightened geopolitical risk, particularly when tensions originate in the Middle East.

From an economic perspective, higher oil prices may present headwinds across much of the economy, although the magnitude of impact has diminished over time. Higher oil prices can increase costs for consumers, particularly for lower-income households where a greater share of spending is allocated to fuel. That said, we believe the economy's dependence on oil has declined significantly over the years due to technological innovation and energy-transition trends.

Another consideration is that higher oil prices may contribute to inflationary pressures, which could increase the likelihood of a tighter monetary policy stance. The disinflation observed in recent years has been partly supported by lower energy prices, and sustained increases in oil and gas prices could slow further disinflation to some extent. Overall, the direct economic implications appear relatively contained, though increased geopolitical uncertainty may weigh on sentiment. Notably, consumer sentiment is already relatively subdued, while market sentiment has remained comparatively strong, as reflected in valuations and equity market leadership.

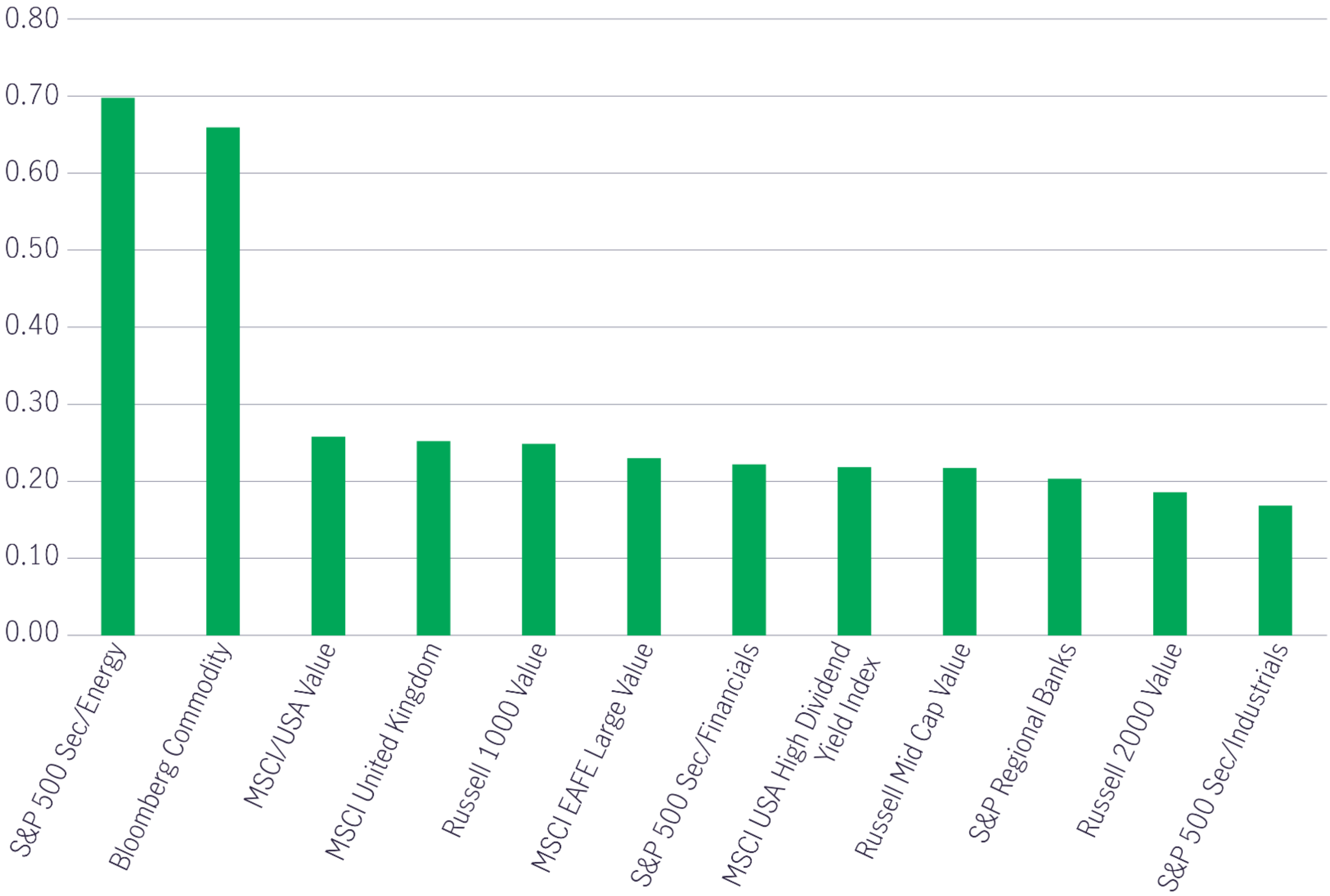
Market implications of geopolitical-driven oil price moves have historically tended to be short-lived. A review of historical correlations suggests certain asset classes have tended to perform differently during periods of rising oil prices. Unsurprisingly, the energy sector has shown the highest correlation to oil prices. Broader energy exposure is often more prevalent in value-oriented segments of the market relative to growth-oriented segments. Industrials have historically been the second most correlated sector, reflecting their role in supplying equipment to the energy industry, as well as exposure to aerospace and defence, which may perform relatively better during periods of geopolitical tension.

From a factor perspective, higher oil prices have tended to support income-oriented segments, which often carry higher exposure to energy-related businesses. Certain value-oriented equity segments, including mid- and small-capitalisation stocks, have also historically shown sensitivity to rising oil prices. Some of these dynamics may already be reflected in market pricing, given recent style and sector performance.

Currency responses are less clear-cut. The U.S. dollar has shown a modest positive correlation with oil prices in recent years, reflecting the U.S.'s increased role as an energy producer. Historically, this relationship was negative, as higher oil prices tended to benefit energy-importing regions more than the U.S.

We would not typically expect to adjust broader asset allocation views solely in response to geopolitical events. While markets may experience short-term reactions as investors attempt to price in heightened uncertainty, these moves have often proven temporary and may be less relevant for longer-term investors.

5-year monthly correlation with the Bloomberg WTI Oil Index



Source: Bloomberg, Crude Oil Futures, Manulife Investment Management, 31st January 2026.

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