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Equity Strategy Insights

Perspectives on Market Volatility Amid Ongoing Geopolitical Risk

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Executive Summary

- March's 9% S&P 500 drawdown amid geopolitical risk and rate volatility fits within historical norms and thus far mirrors past conflict-related pullbacks that ultimately proved temporary.
- History shows stocks often recover quickly during military conflicts, especially when economies are resilient, oil price spikes moderate, and earnings fundamentals remain strong, as in the Iraq War beginning in 2003, though past performance does not guarantee future results.
- Improved valuations, resilient earnings expectations, and normal levels of volatility suggest a favorable risk-reward backdrop, even as geopolitical uncertainty persists and near-term market swings remain likely.

Oil Price Spike and Ongoing Geopolitical Uncertainty Hurt Stocks in March

In March, the S&P 500 endured one of its biggest drawdowns of the past year, falling 9% peak-to-trough at the recent lows. Putting last year's tariff scare aside that almost sent the S&P 500 into a bear market, it was the biggest drop in the S&P 500 since October 2023 when stocks struggled with rising interest rates and the Israel-Hamas war. On a monthly basis, last month's 5% decline was just the second drop of more than 5% in any month since the end of 2022. In this month's *Equity Strategy Insights*, we offer some more perspective on how stocks have performed historically during wars and other military conflicts. In addition, we highlight some positive fundamental factors that point to attractive potential gains post-conflict after volatility subsides.

Historical Perspective: History Doesn't Repeat But Often Rhymes

Our investment process begins with the data. While earnings growth, valuations, interest rates, and inflation are always key elements of LPL Research's investment decisions, finding periods in history that share similarities with the current environment is another important piece of the equation. To that end, we go back to March 2003, the start of the Iraq War. While we do not expect a major ground invasion or a multi-year war in Iran, the better economic environment in 2003 is what makes the period comparable to the current backdrop. The first Gulf War in 1990 was soon followed by recession, not the environment we're in today or expect to be in this year.

When the Iraq War began in 2003, the economy had already healed from the dotcom bust and the 2001–2002 corporate accounting scandals. Profits were rebounding, monetary policy was supportive, and valuations were reasonable. As the fundamental outlook improved, markets refocused on the firmer backdrop soon after hostilities began and embarked on a five-year bull market run through October 2007. The maximum S&P 500 drawdown in 2003 was 14%, while the index gained 26.4% for the year. The next 10% correction didn't come until 2008.

Another reason stocks performed well after the Iraq War began was because of the moderate impact on oil prices. Crude rose from $31.85 in early January 2003 to a peak of $37.83 in mid-March, approximately 19%, before falling sharply by late March as markets anticipated a modest economic impact.

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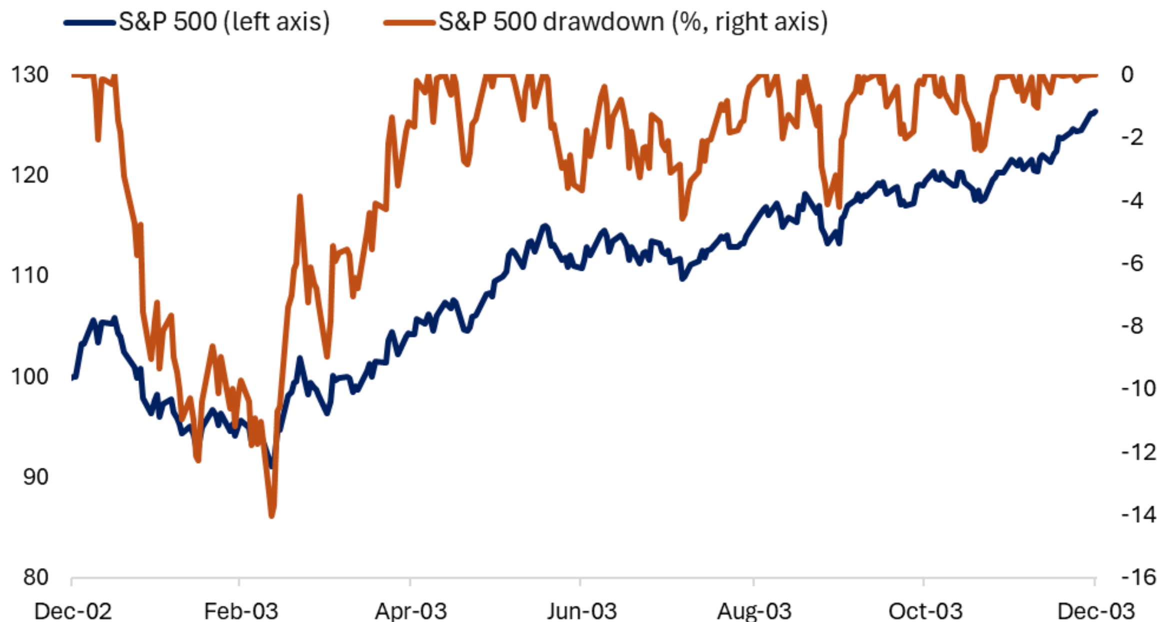
Healed Economy Helped Drive Strong Stock Rebound after Start of Iraq War in March 2003



Source: LPL Research, Bloomberg, 03/31/26 (normalized to 100 on 12/31/02)
Disclosures: All indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results.

The first Gulf War, which began in August 1990, is another interesting analog but with a much weaker economic backdrop. That war caused oil prices to spike from around $22.89 in January 1990 to $40.42 in October 1990 — a 77% increase. The invasion of Kuwait by Iraq and subsequent military response created significant supply concerns, though prices retreated relatively quickly once the conflict's outcome became clear. The U.S. was much more dependent on imported oil back then, increasing the risk of damage to the U.S. economy, which was already slipping into recession in July 1990. Corporate profits were flattening, inflation remained elevated, and consumer confidence was fragile. With little fundamental support in place, markets initially struggled before recovering on anticipated stabilization. Importantly, equities began recovering well before the conflict formally ended — a reason for optimism during the current conflict as markets tend to look through these events if they are expected to be short-lived.

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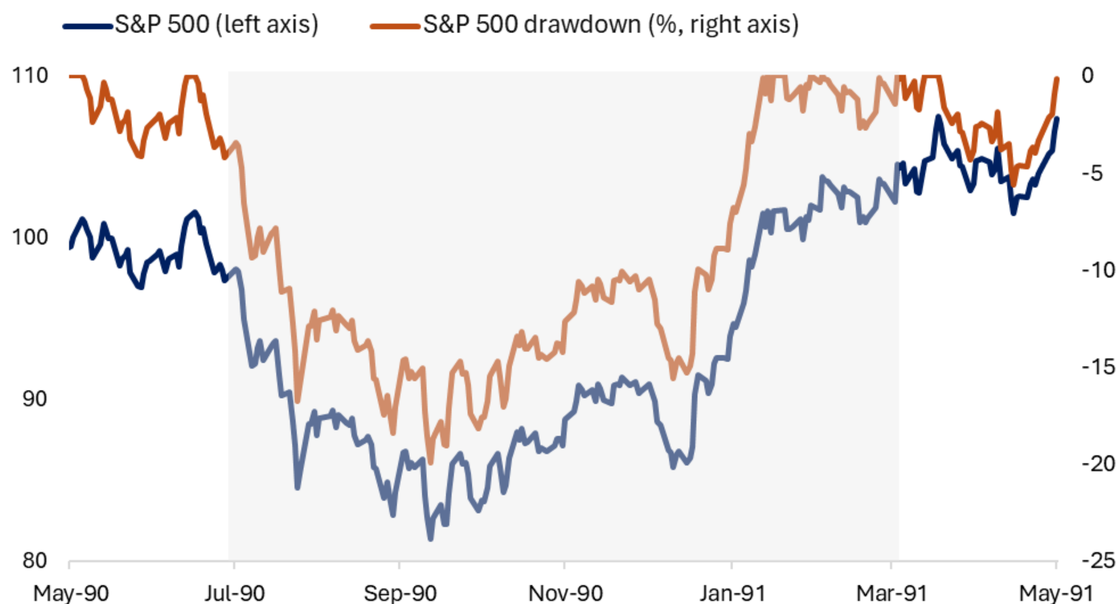
Bear Market Narrowly Avoided During First Gulf War, Which Was Accompanied by Recession



Source: LPL Research, Bloomberg, 03/31/26
Disclosures: All indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results. Shading represents recession.

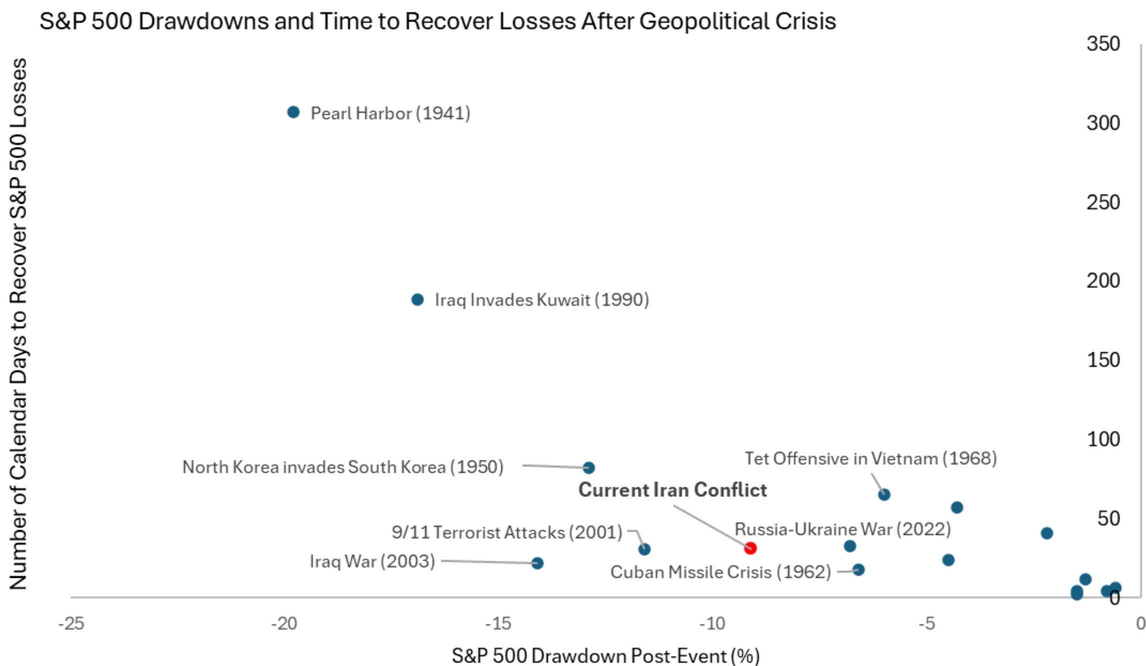
Stocks Have Historically Been Resilient During Wars and Other Military Conflicts

As we wrote about in our March 9 *Weekly Market Commentary*, stocks have historically been resilient to geopolitical shocks. In the "Stocks Have Historically Been Resilient to Military Conflicts" chart, we focus just on wars and significant military operations to get a more comparable set of events than the broader list we published last month. As the accompanying chart illustrates, even in the face of these more serious and longer-lasting events, the stock market has demonstrated impressive resilience — on average, the S&P 500 draws down 7% and recovers losses within an average of 55 days, or less than two months.

While the latest headlines and commentary from the White House suggest the conflict will be over within the next few weeks, which has helped drive stocks higher this week, disruptions to oil tankers and other shipments through the Strait of Hormuz cannot be ruled out, nor can the risk of further damage to energy facilities or other infrastructure in neighboring Gulf countries. In the event of a ceasefire that opens the Strait of Hormuz, we would expect oil prices to come down, but the floor is likely higher than in February and how long a possible détente might last is an open question.

Bottom line, we believe history suggests that the 9% drawdown in the S&P 500 may be all we get during the current conflict, while market-watchers may not have to wait too long for stocks to recover year-to-date losses. At the same time, geopolitical uncertainty remains high enough to warrant patience and leave us comfortable recommending portfolio risk at or slightly below benchmarks currently.

Stocks Have Historically Been Resilient to Military Conflicts



Source: LPL Research, Bloomberg, CFRA, Strategas, 03/31/26
Disclosures: All indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results. Events not labeled include Hungarian uprising ('56), Suez crisis ('56), Gulf of Tonkin Incident ('64), Six-Day War ('67), Yom Kippur War ('73), Israel-Hamas War ('23), U.S.-Israeli Airstrikes of Iran Nuclear Sites ('25). The modern design of the S&P 500 stock index was first launched in 1957. Performance back to 1950 incorporates the performance of the predecessor index, the S&P.

Earnings Still Drive Stock Prices

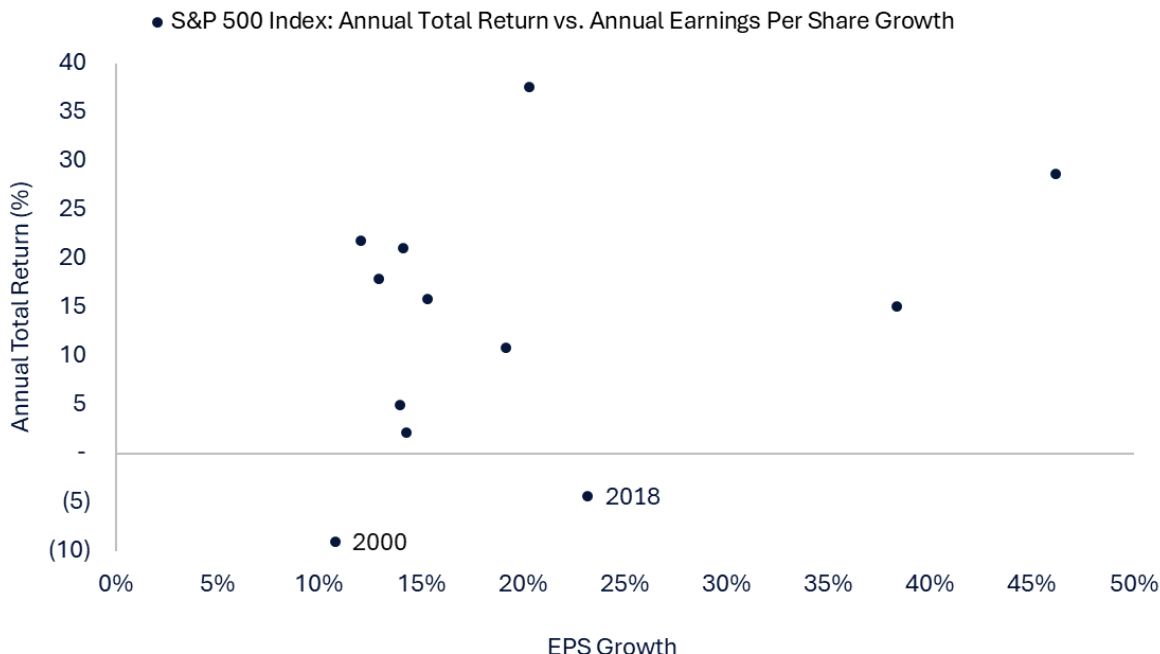
Some may be surprised by the stock market's relative resilience during the conflict. The market's expectation that the operation will be over this month is certainly part of that resilience. U.S. energy independence is part of it as well. But if there is one reason stocks have held up well so far — and hopefully they continue to do so — we would say it's the strong earnings outlook — even in the face of higher oil prices and rising interest rates.

A dampened outlook for companies that are obviously hurt by high oil prices, such as airlines and cruise ship operators, have been more than offset by improving outlooks for earnings from technology companies, largely immune to the conflict, and U.S. energy companies, of course, which benefit.

We wrote about earnings in the March 30 *Weekly Market Commentary*, so we won't go too deep into the topic here. However, we do think it's worth highlighting that stocks have a strong track record of gains when earnings grow double digits, as they may in 2026. Although companies will probably talk expectations down during first quarter earnings conference calls, we still believe fundamentals support double-digit growth in S&P 500 earnings per share (EPS) in 2026. As the accompanying figure illustrates, over a one-year time horizon, strong earnings growth may be accompanied by higher stock prices.

Over the last 30 years the only exceptions were 2000, when stocks were pricing in a bursting internet bubble before earnings fell, and 2018, when concerns about a Fed policy mistake drove a sharp correction beginning in early December of that year. Those fears quickly eased in 2019 as the S&P 500 went on to gain 30% that year.

Double-Digit Earnings Growth Tends to Be Accompanied By Stock Market Gains



Source: LPL Research, Bloomberg 03/31/26

Disclosures: All indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results. 2003 was omitted as an outlier observation with annual earnings per share growth of 362.3% and an annual total return of 28.7%.

This Level of Volatility is Quite Normal

Putting the Middle East aside for a moment, we also want to reiterate that this level of volatility is completely normal. Regular readers may think we sound like a broken record, but we cannot overstate the importance of this point. As we wrote in our [March 31 LPL Research blog](), the average S&P 500 maximum annual drawdown is 14%, while the average annual gain for the S&P 500 is 10%. The drawdown of just 9% this year is well within the normal range and does not diminish our confidence that the broad market will end higher in 2026.

Of course, nothing is guaranteed. The risk of lasting disruption to energy production, transportation, or other critical assets in the region is real. Still, history suggests the risk-reward trade is favorable currently, though past performance does not guarantee future results.

Valuations Have Improved

The benefit of stock market declines is that it gives investors an opportunity to buy stocks at lower valuations, assuming earnings hold up. That's what seems to have happened, in our view. Since the conflict began on the last day of February, the S&P 500 has dropped about 6% and the consensus S&P 500 EPS estimate for 2026 has increased 2.5% (from roughly $310 to $317). We wouldn't argue stocks are cheap, but when the Middle East calms down we see an opportunity for a higher price-to-earnings ratio. Our year-end fair value target range for the S&P 500, at 7,300 to 7,400, is based on a price-to-earnings ratio of 23 and our 2027 S&P 500 EPS estimate of $320.

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Stock Market Pullback as Earnings Estimates Rose Has Lowered Valuations

Source: LPL Research, Bloomberg 03/31/26
Disclosures: All indexes are unmanaged and cannot be invested in directly. Past performance is no guarantee of future results. Estimates may not materialize as predicted and are subject to change.

Conclusion

March's volatility has been uncomfortable but not unusual. While stocks have faced a challenging mix of geopolitical risk, higher oil prices, and interest-rate volatility, history reflects market resilience, especially when economic fundamentals remain intact. The comparison with prior conflicts reinforces that distinction. The 2003 Iraq War illustrates how markets can recover swiftly when earnings are improving, policy is supportive, and oil price spikes are contained.

Earnings continue to provide support for stocks during this volatile period. Consensus expectations for double-digit S&P 500 EPS growth in 2026 have not only held firm, but they have improved despite recent market stresses, resulting in more reasonable valuations and pointing toward gains for stocks in 2026.

This does not mean risks have disappeared. Further disruption to energy infrastructure or shipping routes could prolong uncertainty and drive market volatility. However, based on historical precedent, the current risk-reward backdrop appears favorable, though past performance does not guarantee future results.

Important Disclosures

This material is for general information only and is not intended to provide specific advice or recommendations for any individual. There is no assurance that the views or strategies discussed are suitable for all investors or will yield positive outcomes. Investing involves risks including possible loss of principal. Any economic forecasts set forth may not develop as predicted and are subject to change.

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Because of their narrow focus, sector investing will be subject to greater volatility than investing more broadly across many sectors and companies.

The Standard & Poor's 500 Index (S&P500) is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The PE ratio (price-to-earnings ratio) is a measure of the price paid for a share relative to the annual net income or profit earned by the firm per share. It is a financial ratio used for valuation: a higher PE ratio means that investors are paying more for each unit of net income, so the stock is more expensive compared to one with lower PE ratio.

Earnings per share (EPS) is the portion of a company's profit allocated to each outstanding share of common stock. EPS serves as an indicator of a company's profitability. Earnings per share is generally considered to be the single most important variable in determining a share's price. It is also a major component used to calculate the price-to-earnings valuation ratio.

All index data from FactSet.

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