

Geopolitical Conflict and Financial Market Responses: Evidence from the 2025 Iran-Israel Conflict

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Abstract

Geopolitical conflict can disturb equity markets through uncertainty, commodity-price movements, exchange-rate pressure and shifts in investor preference. This paper examines the short-term response of five equity indices - the Nifty 50, S&P 500, FTSE 100, Nikkei 225 and TASI - around the 2025 Iran-Israel conflict. Daily secondary data covering May to July 2025 were examined through an event-study framework, augmented Dickey-Fuller tests, correlation analysis, pre- and post-event mean comparisons and multiple regression. Price series were non-stationary at level but became stationary after first differencing, supporting the use of transformed series in subsequent analysis. The reported mean comparisons indicate significant differences between the pre- and post-event periods for the selected financial variables. Regression results, however, show that the direct war dummy is statistically insignificant across the five market models. Gold and the exchange rate significantly explain movements in the S&P 500 model, while the exchange rate is the only significant predictor in the Nifty 50 model. The models for the FTSE 100, Nikkei 225 and TASI have weak explanatory power. The evidence therefore suggests that the conflict affected markets mainly through indirect financial channels rather than through a uniform direct war effect. Market responses differed across countries, which highlights the importance of domestic market structure, exposure to imported energy, currency conditions and investor risk perception.

Keywords: Geopolitical Risk, Iran-Israel Conflict, Stock Market Returns, Gold Prices, Exchange Rate, Event Study

1. Introduction

Financial markets no longer operate in isolation. Cross-border investment, integrated supply chains, commodity dependence and rapid information flows transmit an economic or political shock from one region to many others. The Indian equity market, represented by benchmarks such as the Nifty 50, is particularly responsive to changes in foreign portfolio flows, crude-oil prices, the United States dollar and risk sentiment. A geopolitical conflict can therefore influence Indian securities even when the military confrontation occurs outside India.

The 2025 Iran-Israel conflict created a useful setting for examining this transmission. Escalation in the Middle East raised concern about energy supplies, inflation and regional stability. Investors could respond by reducing equity exposure, purchasing gold or United States dollar assets, or demanding a higher risk premium. These responses need not be identical across countries. An oil-importing economy may face

inflation and currency pressure, while an oil-producing market may react differently. A deep and diversified market may also absorb a shock more quickly than a smaller or regionally concentrated market. This study compares five markets: India, the United States, the United Kingdom, Japan and Saudi Arabia. It examines abnormal market behaviour around the selected event period and evaluates crude oil, gold and the USD/INR exchange rate as possible transmission channels. The study contributes a cross-market comparison to a literature that has largely concentrated on the COVID-19 shock and on single-country evidence.

2. Review of Literature

Earlier research establishes that unexpected global shocks can change returns, volatility and market efficiency. Alam et al. (2020) used an event-study approach and observed different abnormal-return patterns around the Indian lockdown announcement [1]. Mishra et al. (2020) reported severe disruption in Indian financial markets during the COVID-19 outbreak [2]. Bora and Basistha (2021) found that the pandemic increased volatility in the BSE Sensex and Nifty [3], while Sahoo (2021) documented the sharp fall and subsequent recovery of Indian equity indices [4]. These studies demonstrate that event timing and the choice of pre-event and post-event windows materially affect empirical conclusions.

Research also shows that market response is not uniform. Okorie and Lin (2021) linked the pandemic with time-varying market efficiency across countries [5]. Mittal and Sharma (2021) found sector-specific abnormal returns, including comparatively favourable responses in healthcare and pharmaceutical stocks [6]. Sharma et al. (2024) reported that firms with stronger environmental, social and governance performance experienced smaller negative cumulative abnormal returns during the pandemic [7]. Such evidence supports a comparative design because country structure, industry composition and investor behaviour may moderate the effect of a common shock.

Commodity and currency channels are also important. Bhama (2022) examined crude oil, exchange rates and pandemic variables in relation to Nifty 100 returns and reported a meaningful role for the exchange rate [8]. Gold is commonly treated as a defensive asset during periods of heightened uncertainty; a rise in gold alongside equity weakness can represent a flight to safety. The present study extends this reasoning to the 2025 conflict and jointly evaluates war conditions, gold and the exchange rate across five markets. The reviewed literature is dominated by pandemic-related evidence. Comparatively fewer studies examine a recent geopolitical shock by combining event-window analysis with stationarity tests, mean comparisons and market-specific regressions. The research gap addressed here is the absence of a unified comparison of Indian and selected global indices during the 2025 Iran-Israel conflict, with explicit attention to oil, gold and currency movements.

3. Research Methodology

3.1 Research Problem

The nature and strength of the effect of a geopolitical conflict on the Indian and global equity markets are not always clear. The problem examined is whether the 2025 Iran-Israel conflict produced a measurable short-term change in the selected markets and whether oil, gold and the exchange rate help explain the observed movements.

3.2 Objectives

To examine short-term abnormal returns around the conflict event window.

To study the relationship between crude-oil prices and stock-market performance during the conflict.

To study the relationship between gold prices and stock-market performance during the conflict.

To compare selected financial variables between the pre-event and post-event periods.

To assess the influence of gold prices, the USD/INR exchange rate and the war dummy on the selected stock markets.

3.3 Hypotheses

H01: Each price series contains a unit root at level.

H02: The conflict has no significant direct effect on the selected equity indices.

H03: Crude-oil prices have no significant relationship with the selected equity indices.

H04: Gold prices have no significant relationship with the selected equity indices.

H05: Mean values do not differ between the pre-event and post-event periods.

3.4 Data and Research Design

A quantitative, deductive and analytical design was adopted. Daily secondary data for May-July 2025 were drawn from the financial-data sources identified in the original project, including Yahoo Finance, Investing.com and the Multi Commodity Exchange. The purposively selected indices were the Nifty 50, S&P 500, FTSE 100, Nikkei 225 and TASI. Crude-oil prices, gold prices and the USD/INR exchange rate were included as financial transmission variables. The observation period was divided into a pre-event window, an event window and a post-event window. Microsoft Excel was used for data organization, while EViews or SPSS was used for econometric analysis.

3.5 Analytical Procedure

Stationarity was tested with the augmented Dickey-Fuller test. First differences were used after the level series failed to reject the unit-root null. Correlation analysis was applied to examine pairwise association. Pre-event and post-event means were compared through the reported t, Welch and analysis-of-variance tests. For each index, the following market-specific model was estimated:

$$\text{Stock Market} = \beta_0 + \beta_1 (\text{War}) + \beta_2 (\text{Gold}) + \beta_3 (\text{USD/INR}) + \epsilon$$

The war variable is a dummy for the designated conflict period. Statistical significance was assessed primarily at the 5 percent level. The event-study calculations in the project used market-model expected returns and abnormal returns, defined as the difference between actual and expected returns.

4. Results and Discussion

4.1 Stationarity

Table 1: Augmented Dickey-Fuller Test Results

Variable	Level statistic	Level p-value	First-difference statistic	First-difference p-value
S&P 500	-1.842	0.356	-5.842	0.000
Nifty 50	-2.112	0.238	-4.921	0.000
FTSE 100	-1.765	0.398	-5.112	0.000
Nikkei 225	-1.923	0.312	-4.876	0.000
TASI	-2.045	0.268	-5.004	0.000
Crude oil	-3.412	0.062	-6.112	0.000
Gold	-2.876	0.051	-5.334	0.000
USD/INR	-1.998	0.287	-4.998	0.000

All level-series p-values exceed 0.05; consequently, the unit-root null cannot be rejected at level. After first differencing, every reported p-value is 0.000. The transformed series are therefore treated as stationary. This result supports the use of changes or returns in the subsequent analysis and reduces the risk of spurious inference from trending price levels.

4.2 Pre- and Post-Event Comparisons

Table 2: Reported Pre- and Post-Event Mean Comparisons

Variable	Pre-event mean	Post-event mean	Difference	Reported p-value
Crude oil	69.90	64.62	-5.28	0.0000 (sig.)
FTSE 100	8,692.68	8,926.00	+233.32	0.0000(sig.)
Gold	95,054.04	97,379.66	+2,325.62	0.0000(sig.)
Nifty 50	24,686.10	25,213.89	+527.79	0.0000(sig.)
Nikkei 225	37,532.02	40,004.16	+2,472.14	0.0000(sig.)
S&P 500	5840.23	6,256.00	+415.77	0.0000(sig.)
TASI	11,251.63	11,047.02	-204.61	0.0017(sig.)
USD/INR	85.31	86.07	+0.76	0.0000(sig.)

The reported tests reject equality of pre-event and post-event means for all eight variables. Gold and USD/INR increased, which is consistent with defensive positioning and depreciation of the Indian rupee. Nifty 50, FTSE 100 and Nikkei 225 also recorded higher post-event means, indicating that the response was not a uniform global decline. The TASI and the reported S&P 500 series declined. These comparisons describe a change between periods but do not, by themselves, establish that the conflict caused the entire change because other contemporaneous factors are not controlled.

4.3 Regression Results

Table 3: Market-Specific Regression Results

Market	War coefficient (p)	USD/INR coefficient (p)	Gold coefficient (p)	R squared	Model p-value	Durbin-Watson
S&P 500	-6.40 (0.5573)	-38.10 (0.0300)	-0.0162 (0.0068)	0.242	0.0038	2.06
FTSE 100	4.60 (0.6759)	34.35 (0.0539)	-0.101 (0.0896)	0.112	0.119	2.12
Nikkei 225	37.86 (0.7089)	254.31 (0.1187)	-0.0163 (0.7629)	0.050	0.464	1.44
Nifty 50	-16.48 (0.7396)	303.87 (0.0003)	-0.0251 (0.3453)	0.241	0.0034	2.30
TASI	-5.04 (0.9932)	-340.06 (0.7186)	-0.39 (0.2223)	0.036	0.610	3.03

The direct war coefficient is statistically insignificant in every model. H02 is therefore not rejected. This does not imply that the conflict was irrelevant; rather, the specified dummy does not explain index

variation after the included financial variables are considered. The result is consistent with indirect transmission through currency and safe-haven channels and with differences in the speed at which national markets incorporate geopolitical information.

The S&P 500 model is significant overall and explains 24.2 percent of the reported variation. USD/INR and gold have significant negative coefficients. The negative gold coefficient is consistent with movement away from equity and towards a defensive asset. The Nifty 50 model is also significant overall and explains 24.1 percent of variation; USD/INR is its only significant predictor. The positive sign should be interpreted cautiously because the dependent variable specification and the use of a common USD/INR measure across international models may affect economic meaning.

The FTSE 100, Nikkei 225 and TASI models are not significant overall. Their low R-squared values indicate that the included variables explain little of the observed market variation. The Durbin-Watson statistic of 1.44 for the Nikkei 225 suggests possible positive residual autocorrelation, while 3.03 for the Tadawul model suggests possible negative autocorrelation. Robustness checks with alternative specifications and market-specific exchange rates would strengthen inference.

4.4 Event-Window Interpretation

The original event-window analysis reports increased abnormal-return volatility during the conflict and gradual stabilization afterward. The comparative pattern is more important than a claim of identical negative returns across all markets. Nifty 50 and the Tadawul index generally display smaller day-to-day abnormal movements than the most extreme values reported for the developed-market comparisons. Because several raw rows contain apparent cross-series transcription errors, extreme abnormal-return observations are not treated as reliable point estimates in this paper. The consistent econometric outputs indicate heterogeneous reactions rather than a single global effect.

5. Findings

The findings reveal that the 2025 Iran–Israel conflict was associated with heightened short-term volatility and changes in abnormal returns across the selected stock markets; however, the direction and intensity of the response varied considerably across countries. The event-window results therefore indicate a heterogeneous market reaction rather than a uniform decline. Crude-oil price movements exhibited weak or statistically insignificant relationships with most of the selected indices, suggesting that oil-price changes alone were insufficient to explain equity-market performance during the study period. Gold prices displayed a generally inverse association with equity performance, particularly in the S&P 500 model, supporting the role of gold as a safe-haven asset during periods of geopolitical uncertainty. The simultaneous increase in gold prices and the USD/INR exchange rate further reflects greater risk aversion, defensive asset allocation and pressure on the Indian rupee. The regression analysis nevertheless found that the war dummy was statistically insignificant across all five market-specific models, indicating that the conflict did not produce an independently measurable and uniform direct effect on stock-market performance. Instead, the significant influence of gold and USD/INR in the S&P 500 model and of USD/INR in the Nifty 50 model suggests that geopolitical risk was transmitted primarily through safe-haven demand and currency movements. The relatively weak explanatory power of the FTSE 100, Nikkei 225 and Tadawul All Share Index models also indicates that market reactions were shaped by additional domestic, macroeconomic and institutional factors. Overall, the findings demonstrate that geopolitical shocks affect financial markets through multiple and market-specific transmission channels, with their ultimate impact depending on each economy's energy exposure, currency conditions, market structure and

investor response.

For policymakers, the findings underline the relevance of imported-energy exposure, currency stability and clear communication during international shocks. Reducing excessive dependence on imported crude oil, strengthening energy alternatives and maintaining adequate foreign-exchange resilience may reduce the transmission of external stress. Researchers should extend the analysis with longer estimation windows, market-specific exchange rates, volatility models, sectoral indices and controls for monetary-policy and macroeconomic announcements.

6. Limitations

The study uses secondary data and a short observation window. Only five equity indices and three financial channels were examined. A single war dummy may not capture changes in conflict intensity or the timing of information arrival. The pre- and post-event mean tests may be influenced by other developments occurring during May-July 2025. The original raw tables also contain apparent transcription inconsistencies in several index rows; accordingly, the extreme abnormal-return values require verification against the source data before they are used for further inference. The regression models do not include all domestic, sectoral or global factors that could influence returns.

7. Conclusion

The 2025 Iran-Israel conflict coincided with meaningful changes in the selected financial series, but its effect was neither direct nor uniform across markets. Stationarity testing supports the use of first-differenced data. Reported mean comparisons show statistically significant shifts between the pre-event and post-event periods, including higher gold prices and a weaker Indian rupee. In the regression analysis, however, the war dummy is insignificant for every index. Currency and gold variables provide more explanatory power in the S&P 500 and Nifty 50 models, while the remaining market models are weak. The principal conclusion is therefore that geopolitical risk is transmitted through several financial channels and interacts with market-specific conditions. Investors and policymakers should monitor commodities, currency movements and domestic resilience together rather than relying on the occurrence of conflict alone.

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