上海商業銀行
SHANGHAI COMMERCIAL BANK
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Instant Thoughts

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Trump's Doom Loop

- **Making use of an econometric model developed by the Fed, a US$10, US$30, US$50 oil price shock would take 0.02, 0.08 and 0.14 percentage point off U.S. growth over a year, respectively. Meaningful, but it isn't as inexorable as many fear.**
- **The same can be said for inflation. Initially, headline PCE inflation moves 33bps, 100bps, and 167bps higher, respectively, with the impulses moderating to 9bps, 27bps, and 44bps a year later.**
- **Still, the AI-enabled productivity boom looks increasingly flimsy, and the oil shock is very real. Focusing on tangible outcome, while not seismic, could be self-reinforcing.**
- **One might consider hedging tail risk via payers amidst an event-rich year.**

The curse of Trump's order-shaping obsession has struck again: the assassination of the Iranian Supreme Leader brings war to the Gulf doorstep.

Much depends on how long the standoff lasts and how intense the exchange of fire becomes. Trump might admire military adventurism, but he isn't known to play three-dimensional chess. The commander-in-chief, however morally unshackled, has already leaped out and called for a blitz that is expected to last only four to five weeks.

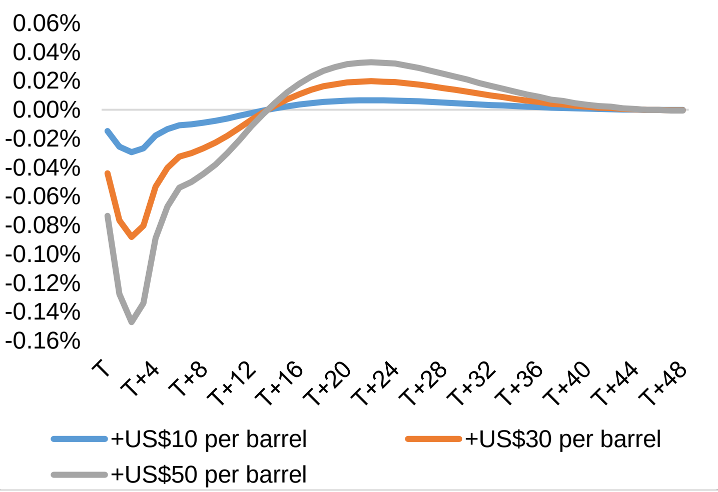
But could things get worse than traders expect? Not a very tall order. Peace, now often forgotten, isn't a law of nature. "War made the state and the state made war." Battling is how modern states built their capacity, as political scientist Charles Tilly wisely summarized.

Over years, though, traders have built the muscle memory to sell geopolitical risk premium when combat start. That's exactly why another panic wave could be set off if containment fails.

What happens next? Speculate no more. We make use of an econometric model developed by the Fed to assess the impact of the blockade of the Hormuz Strait. With a broad brush, the peak effect occurs one year ahead (Exhibit 1). A US$10, US$30, and US$50 oil price shock would take 0.02, 0.08, and 0.14 percentage points off U.S. growth over a year, respectively. Meaningful, but it isn't as inexorable as many fear.

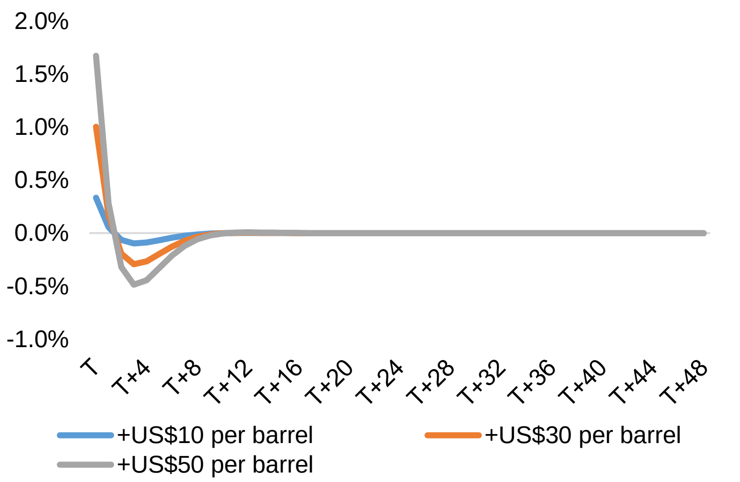
The same can be said for inflation. Initially, headline PCE inflation moves 33bps, 100bps, and 167bps higher, respectively, with the impulses moderating to 9bps, 27bps, and 44bps a year later. These result feel true to life, as the world's largest economy can lean on its shale gas industry.

Exhibit 1: Impact of Oil Shock on U.S. GDP



Source: FRB/US Model, Shanghai Commercial Bank

Exhibit 2: Impact of Oil Shock on PCE



Source: FRB/US Model, Shanghai Commercial Bank

Life won't be lift if things were as neat as model predicted. The AI-enabled productivity boom looks increasingly flimsy, and the oil shock is very real. Focusing on tangible outcomes could be self-reinforcing. So far, the market is trading this war as a terms of trade episode much more than a flight to safety, as evidenced by the rally of AUDCHF. One might consider hedging the tail risk via payers amidst an event-rich year.

Exhibit 3: AUDCHF

Source: Bloomberg, Shanghai Commercial Bank

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