The Assessment of the Asymmetric Financial Effect of Strait of Hormuz Geopolitical Conflicts on International Stock Markets: A Conceptual Framework

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ABSTRACT

The Strait of Hormuz is one of the world's most important maritime routes, carrying a significant portion of global oil exports. As a strategic chokepoint, geopolitical conflicts in this region can create uncertainty in global financial markets by disrupting energy supply and affecting investor confidence. This study aims to examine the impact of conflicts in the Strait of Hormuz on international stock market performance by analyzing whether such events generate significant abnormal returns. The study applies to the Event Study Method, supported by the Efficient Market Hypothesis (EMH), to measure investor reactions before and after a selected conflict event involving attacks on oil tankers. Major international stock market indices, including the S&P 500, FTSE 100, DAX, Nikkei 225 and Malaysia's KLCI, are selected to represent different economies. Cumulative Abnormal Returns (CAR) are used to evaluate market reactions, while oil dependency level is incorporated as a moderating variable to explain differences across countries. The findings of this study are expected to contribute to a better understanding of how geopolitical risks influence international financial markets and provide useful insights for investors, policymakers and financial institutions in managing market uncertainty and investment risks.

Keywords: Strait of Hormuz, geopolitical conflict, international stock markets, event study, abnormal returns, investor behavior, oil prices and market volatility.

INTRODUCTION

The Strait of Hormuz is an important sea route located between Iran and Oman. It connects the Persian Gulf to the Arabian Sea. Many countries use this route to transport oil and gas to other parts of the world. A large amount of the world's oil passes through the Strait of Hormuz every day. Because of this, the Strait of Hormuz plays an important role in the global economy and international trade.

However, the Strait of Hormuz is also known as a sensitive area because many political and military tensions happen there which leads to geopolitical conflicts which refers to political or military tensions between countries that may affect economic stability, trade activities and financial markets. Over the years, there have been several conflicts involving Iran, the United States and nearby Gulf countries. These conflicts include military threats, attacks on oil tankers, drone incidents and economic sanctions which lead to uncertainty in global markets because countries are concerned about possible disruptions to oil supply and international trade activities.

One of the expected effects of the Strait of Hormuz crisis is the **increase in global oil prices** that will subsequently raise production and transportation costs for firms, which can squeeze profit margins and weaken the expected returns that investors rely on when allocating capital (Dong et al., 2024). Since the Strait of Hormuz is a major route for oil exports, any threat to the safety of this route can reduce confidence in global oil supply. Investors and oil traders may expect shortages in oil supply, which can cause oil prices to rise sharply. These cost pressures may weaken corporate earnings and reduce the expected cash flows that support equity valuations (Behera et al., 2024, 2026). Previous research demonstrates that oil-price shocks and volatility influence industry

stock returns, although the magnitude and direction of the effects vary across industries (Elyasiani et al., 2011; Narayan & Sharma, 2011).

Moreover, **changes in oil prices** may also affect company performance and economic activities in many countries. Investors might be worried about disruptions in oil supply and higher energy prices could negatively affect company performance and future economic growth. As a result, investors may become more cautious and reduce their investments in the stock market. Thus, stock markets in many countries may experience sudden changes and higher volatility. This situation can negatively affect companies, investors and overall market confidence thus affecting the global trade and energy supply and greater financial pressure when conflicts occur in this region.

Furthermore, conflicts in the Strait of Hormuz may also influence **investor behavior** and investment decision making. It forces investors to shift toward secured assets and to demand greater compensation for holding equities. They may change their investment strategies to reduce possible losses in respond to market instability (Ngô & Kumar, 2026). This situation can cause stock prices to fall making the stock market more volatile. Some more, according to Khatawkar (2026), the decline in the stock market is not merely a short-term reaction to news, since investors who anticipate prolonged disruption to energy supplies may revise their expectations on return and macroeconomic growth across the region.

Besides, investor's reaction to the stock markets may cause investment to lose its value thus, experience a financial loss (Caldara & Iacoviello, 2022). Such losses are not limited to individual firms, since a geopolitical risk can reduce investor risk appetite and trigger capital reallocation across countries and asset classes. For example, empirical evidence from firm-level studies suggests that these effects influence decision making since elevated uncertainty raises the cost of capital and encourages managers to postpone or cancel irreversible investments (Tan et al., 2022).

However, investors may react differently during uncertain situations depending on the seriousness of the conflict and market conditions. Some investors may respond to uncertainty by reallocating capital toward secured assets or demanding for higher risk premium, which can amplify price swings even in markets with limited direct exposure to the region (Ahmed et al., 2022; and Ngô & Kumar, 2026). While some investors may choose to withdraw their investment from the stock market and move to safer assets such as gold, government bonds or foreign currencies. Others may delay investment decisions until the political situation becomes more stable. These reactions may however create panic selling, market instability and changes in investment patterns.

Although many studies have discussed geopolitical risk and financial markets, there is still limited understanding of how conflicts in the recent Strait of Hormuz conflict specifically affect stock markets and investor reactions. Most previous studies focus on oil prices or political issues without fully examining the relationship between geopolitical conflicts, investor sentiment and stock market performance. Thus, more research is needed to better understand how conflicts in this important region influence investor confidence and financial market stability across different countries.

LITERATURE REVIEW

Effect of Geopolitical Crisis on Stock Market Performance

Geopolitical crises refer to political tensions, military conflicts, wars, diplomatic disputes or security issues between countries that may influence economic activities and financial markets. Geopolitical events often create uncertainty because they may affect trade activities, global supply chains, oil prices and investor confidence. According to Caldara & Iacoviello (2022), financial markets usually react quickly to geopolitical developments because investors closely monitor events that may affect economic conditions.

Furthermore, political conflicts and military tensions can adversely affect stock market performance by increasing geopolitical uncertainty and financial risks. During geopolitical crises, investors may become more risk-averse, leading to portfolio adjustments, capital outflows and changes in stock market returns (Catalán et al., 2023; Gala et al., 2023). These effects may vary across countries depending on their economic exposure and

vulnerability to geopolitical shocks. As a result, stock prices may decline, market volatility may increase and investment activities may slow down. Financial markets often experience stronger reactions when geopolitical crises involve important economic sectors such as energy and international trade.

Performance of stocks market reflects the economic conditions and investor expectations. These markets respond quickly to changes in economic conditions, oil prices and geopolitical events due to increasing financial market integration. This integration implies that portfolios, particularly those heavily weighted toward equities, are often subjected to abrupt, non-diversifiable risk spikes during periods of heightened tension (Apergis et al., 2017). Consequently, the manifestation of such volatility is not limited to localized equity declines but often precipitates a broader reallocation of capital away from equities toward safe-haven assets, such as government bonds and gold, to mitigate potential losses during international crises (Omar et al., 2016 and Salisu et al., 2022).

Previous studies have shown that geopolitical uncertainty negatively affects stock market performance such as Caldara and Iacoviello (2022) found that higher geopolitical risk reduces stock returns and increases market volatility. Geopolitical conflicts can increase uncertainty and contribute to volatility spillovers across international stock markets, although the magnitude of these spillovers may vary depending on market conditions and the nature of the shock (Bouri & Harb, 2022).

Investor Reactions to Stock Market Performance

Investor reactions refer to changes in investment decisions and behavior based on market information, economic conditions and external events. Investors' decisions are influenced by stock market conditions, investor sentiment, and changing perceptions of market risk, which can affect stock prices and expected returns (Shiller, 2000). Thus, investor behavior plays an important role in determining stock performance because buying and selling activities influence stock prices and market trends. During periods of uncertainty, investors may react differently depending on market conditions and perceived risks. Some investors may continue investing despite uncertainty, while others may reduce their investment to avoid potential losses. Political conflicts and geopolitical tensions often increase uncertainty, causing investors to become more cautious in financial decision-making (Baker et al., 2016).

Furthermore, geopolitical conflicts may also encourage investors to shift investment from risky assets to safer investment alternatives. During periods of financial market turmoil, investors may seek safe-haven assets to reduce portfolio risk. Gold has been found to act as a hedge against stocks on average and as a haven during extreme stock market conditions, although this safe-haven effect may be short-lived (Baur & Lucey, 2010). These reactions may influence stock prices, increase market volatility and affect overall market performance.

Previous studies have suggested that investor sentiment and market confidence are important factors influencing stock market movements. According to Tetlock (2007), media pessimism is associated with downward pressure on stock market prices and increased trading activity, suggesting that investor sentiment can influence market behaviour. In the context of this study, conflicts in the Strait of Hormuz may increase geopolitical uncertainty and affect investor sentiment, potentially influencing investment decisions and international stock market performance.

Abnormal Return

Cumulative Abnormal Return (CAR) measures the difference between actual stock returns and expected returns during a specific event period. It is commonly used in event studies to evaluate investors' reactions to unexpected events such as geopolitical conflicts or economic crises (MacKinlay, 1997).

Many studies have used CAR to examine market responses to external shocks. Corrado (2011) explained that abnormal returns reflect how quickly markets incorporate new information. Likewise, Ramelli and Wagner (2022) found significant cumulative abnormal returns during the COVID-19 pandemic, indicating that investors reacted rapidly to unexpected events.

In geopolitical studies, CAR serves as a useful indicator of market reaction. Changani and Dudhagra (2026) reported significant abnormal returns following major Middle East conflicts, showing that geopolitical events can influence investor behaviour. Therefore, CAR is an appropriate mediating variable linking conflict in the Strait of Hormuz to international stock market performance.

Oil Dependency Level

Oil dependency refers to the extent to which a country relies on oil imports or exports for its economy. Countries with high oil import dependence are more vulnerable to rising oil prices, while oil exporting countries may benefit from increased energy revenues during supply disruptions Previous research suggests that oil dependency changes the impact of oil price shocks on stock markets. Ready (2018) found that oil importing countries experience larger negative stock market returns when oil prices increase compared to oil exporting countries. Furthermore, the sensitivity of stock markets to geopolitical conflicts may vary according to countries' dependence on oil. Kumar et al. (2021) found that stock markets in oil-exporting countries exhibit stronger and more persistent responses to oil shocks than those in oil-importing countries, particularly when geopolitical risk is considered. This suggests that oil dependency may moderate the relationship between Strait of Hormuz conflicts and international stock market reactions.

Recent studies highlight that economies heavily dependent on Middle Eastern oil are more sensitive to disruptions in the Strait of Hormuz. Countries with greater dependence on oil and imported energy may be more vulnerable to geopolitical conflicts and oil supply disruptions because rising energy prices can increase production costs, fuel inflation, and weaken economic activity (Kilian et al., 2026; Miyamoto et al., 2026). Therefore, oil dependency may moderate the relationship between Strait of Hormuz conflicts and international stock market performance, as the magnitude of market reactions may differ according to countries' levels of energy dependence.

In short, geopolitical risks may influence stock market returns and investor confidence. Market uncertainty caused by political instability may encourage investors to become more conservative in making investment decisions. Therefore, geopolitical crises play an important role in influencing financial market stability and investment behavior across different countries.

CONCEPTUAL FRAMEWORK

The Strait of Hormuz represents a strategically important geopolitical chokepoint through which a substantial proportion of global petroleum trade is transported. Consequently, military conflicts that threaten the security of maritime navigation through this strait may generate significant disruptions to global oil supply, intensify energy-market uncertainty and trigger fluctuations in international crude oil prices. These developments can influence investor sentiment, alter expectations regarding corporate earnings and increase the risk premiums demanded by investors. The transmission of geopolitical shocks to financial markets is particularly relevant because countries differ in their exposure to international energy markets, oil supply disruptions and energy-related production costs. Previous empirical studies have established that geopolitical risks are associated with movements in oil prices and stock-market returns, with evidence of volatility spillovers between oil and equity markets (Caldara & Iacoviello, 2022; Wang et al., 2013). Furthermore, disruptions to maritime traffic through the Strait of Hormuz can generate wider macroeconomic and financial consequences, including higher energy prices, weaker economic activity and tighter financial conditions (Kharroubi, 2026)

Cumulative abnormal return (CAR) is conceptualized as a mediating variable to capture the financial-market transmission mechanism through which geopolitical conflict affects international stock-market performance. Following the event-study framework, abnormal returns represent the difference between actual stock returns and the returns expected under normal market conditions, while CAR measures the accumulated abnormal performance over a specified event window (MacKinlay, 1997). In the context of the Strait of Hormuz conflict, geopolitical developments may initially trigger unexpected stock-price adjustments as investors reassess geopolitical uncertainty, potential oil supply disruptions and their implications for future corporate profitability. These abnormal price movements provide an observable indication of how financial markets incorporate conflict-related information into asset valuations. Accordingly, CAR can serve as an intermediate financial-

market response through which the effects of geopolitical conflict are transmitted to broader international stock-market performance. This interpretation is consistent with research documenting the relationship between geopolitical risk, oil-market movements and equity-market responses (Nygaard & Sørensen, 2024, and Wang et al., 2013).

Meanwhile, **oil dependency level (ODL)** is proposed as a moderating variable because the sensitivity of national stock markets to geopolitical disruptions may vary according to their dependence on imported petroleum and the relative importance of oil in their economic structures. Countries with high levels of oil-import dependence may be more vulnerable to supply disruptions, rising energy costs, inflationary pressures and deterioration in their trade balances. These developments may subsequently affect corporate profitability, economic growth expectations and investor confidence. Conversely, oil-exporting countries or economies with relatively diversified energy sources may experience different, and potentially less adverse, financial-market responses. Empirical evidence supports this country-level heterogeneity. Wang et al. (2013) demonstrate that the magnitude, duration and direction of stock-market responses to oil-price shocks depend on whether a country is a net oil importer or exporter and on the underlying source of the oil-price shock. Similarly, Aloui et al. (2012) identify differences in stock-market sensitivity to oil-price fluctuations across emerging economies with different levels of oil dependence. More recent evidence also highlights differences in the exposure of stock-market sectors in petroleum-importing and petroleum-exporting economies to oil-price shocks (Bagirov & Mateus, 2025). Therefore, ODL is expected to moderate the relationship between Strait of Hormuz geopolitical conflict and international stock-market performance, such that the magnitude and direction of the market response depend on the degree of a country's exposure to oil-related supply risks.

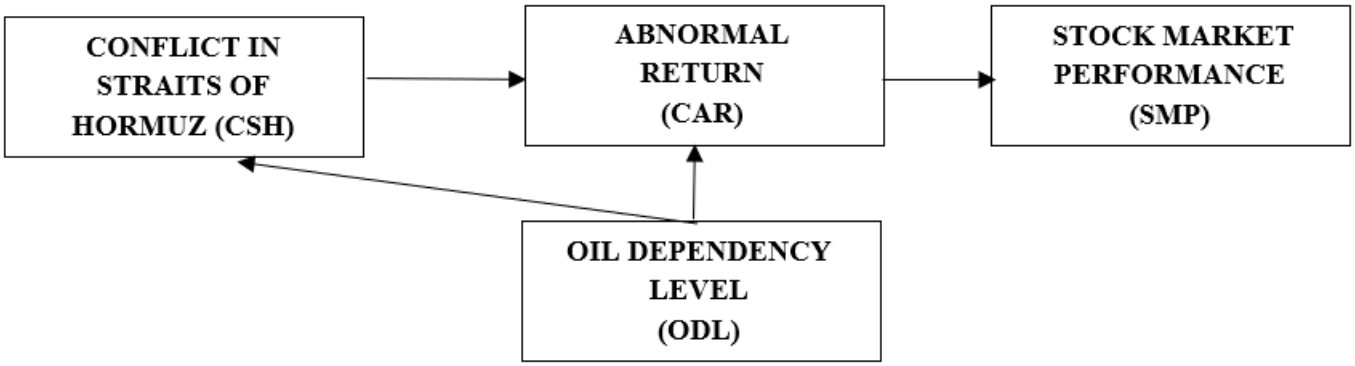

Figure 1: Conceptual Framework for The Effect of Straits of Hormuz Conflict towards International Stock Market

Figure 1 depicts the conceptual framework for analyzing the impact of conflict in the Strait of Hormuz, mapping the flow from the geopolitical shock through abnormal market returns to international indices indicated by the stock market performance, with oil dependency level as the moderating variable. The current study expects that the geopolitical conflicts have significant effects on international stock markets through increased uncertainty, volatility and changes in investor behavior.

RESEARCH METHODOLOGY

In the manner of Jardak & Belghith (2026), this study adopts the **event-study methodology** developed by MacKinlay (1997) to examine the effect of the conflicts in the Strait of Hormuz. The methodology evaluates whether specific events influence stock prices by measuring abnormal returns around the event dates. According to MacKinlay (1997), event studies rely on the premise that the effects of new information are reflected in security prices, allowing the economic impact of an event to be assessed over a relatively short period. Other studies that have applied this approach to analyze the effects of terrorism and geopolitical events on stock markets. For example, Markoulis and Katsikides (2020) found that major terrorist attacks generated negative abnormal returns and international market spillovers, while Tahir et al. (2020) and Osuala et al. (2015) examined stock market reactions to terrorist incidents in Pakistan and Nigeria, respectively. Their findings provide evidence that terrorist events can generate abnormal stock returns, although the magnitude and statistical

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significance of the market reaction may vary depending on the event. These studies suggest that unexpected geopolitical events can influence investor behavior and stock market performance, supporting the application of event study methodology to examine conflicts in the Strait of Hormuz.

The current study is grounded on the underpinning **Efficient Market Hypothesis (EMH),** which suggests that stock prices quickly incorporate new information. The theory assumes that markets instantly process the geopolitical risks of the conflict, reflecting the new reality via immediate Abnormal Returns. According to this theory, when new information becomes available, such as geopolitical conflicts, political instability or disruptions to global trade, investors immediately adjust their expectations and investment decisions.

Research Design

The analysis will involve the following steps:

Step 1: The "event" would be the military attacks on oil tankers occurred on: 15 June 2025

This date becomes the: Event Date (t = 0)

Step 2: Sample identification

The selected indices across five countries namely:

- S&P 500 (United States)
- FTSE 100 (United Kingdom)
- DAX (Germany)
- Nikkei 225 (Japan)
- KLCI (Malaysia)

Step 3: Estimation Window.

The estimation window of -250 days to -30 days is used to estimate the stock's "normal" return behavior before the event. During this period, no event effect is assumed.

Step 4: Event Window.

The event window captures investor reactions before and after the event. This study will be using a long window which is five days before and five days after the event as follow:

Day -5 - 4 -3 -2 -1 0 +1 +2 +3 +4 +5

↑

Event Date

Step 5: Calculation of Actual Returns.

Daily stock returns are calculated as:

$$Rit = \frac{Pt - Pt-1}{Pt-1}$$

Where:

Rit= actual return

Pt= today's price

Pt-1= previous day's price

Step 6: Estimation of Expected Returns

Expected returns represent what investors would normally expect if no conflict occurred.

The formula is as follows:

$$ERi = \alpha i + \beta i + Rm$$

Where:

α = intercept

β = systematic risk coefficient

Rm = market return

Step 7: Calculation of Abnormal Returns (AR)

Abnormal return is the difference between actual return and expected return.

$$ARit = Rit = E(Rit)$$

Interpretation:

Negative AR

Investors reacted negatively indicated by Actual Return = -4%

Positive AR

Investors reacted positively indicated by Actual Return =3%, Expected Return =1%, and AR=2%

Step 8: Calculate Cumulative Abnormal Returns (CAR). To measure the overall impact across several days:

$$CAR = \sum_{t=t1}^{t2} Art$$

Day	AR
-1	-1.2%
0	-2.8%
+1	-1.0%

If CAR = -5.0%

Interpretation: Investors lost approximately 5% relative to expected returns over the event period.

Step 9: Test Statistical Significance

t-test

If CAR = 0, or CAR ≠ 0

If significant:

- Investors reacted to the event.
- The conflict affected stock prices.

If insignificant:

- Markets may have already anticipated the event.
- The event may have had limited economic impact.

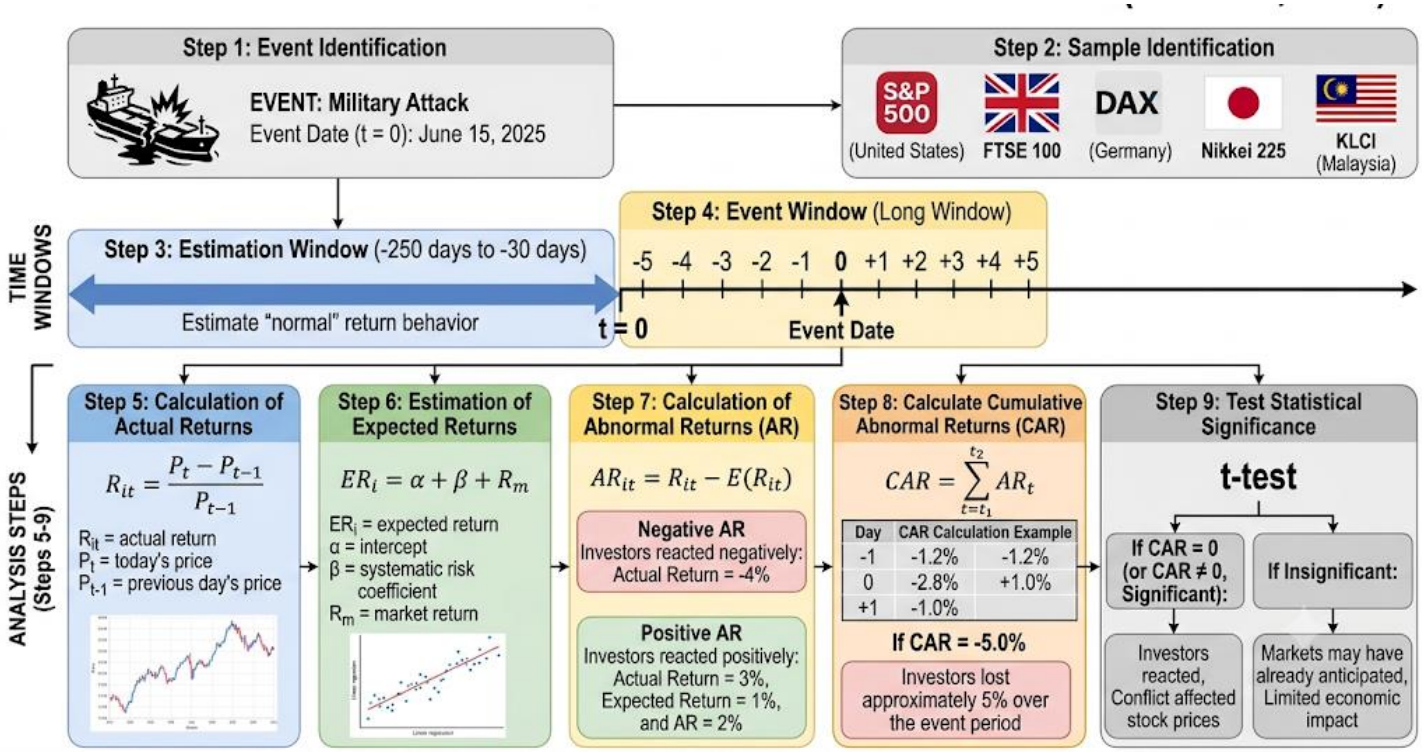

Figure 2: Event Study on Oil Tanker Attack

Overall, the event study methodology provides a systematic approach for examining the impact of conflicts in the Strait of Hormuz on international stock market performance. Supported by the Efficient Market Hypothesis (EMH), this methodology enables the study to analyze how investors respond to unexpected geopolitical events through changes in abnormal stock returns. To ensure a clear and structured analysis, the following sections describe the variables used in the study, including the independent, mediating, dependent and moderating variables, followed by the research design adopted to achieve the research objectives.

CONCLUSION

The Strait of Hormuz remains one of the most strategically important oil transportation routes in the world, making geopolitical conflicts in this region highly influential on global financial markets. This study investigates how such conflicts affect international stock market performance by examining investor reactions through the Event Study Method and measuring abnormal returns. Guided by the Efficient Market Hypothesis, the study

expects that unexpected geopolitical events are quickly reflected in stock prices, resulting in significant market reactions.

The research also highlights the importance of oil dependency as a moderating factor, suggesting that countries relying heavily on imported oil are more vulnerable to negative market effects than oil-exporting economies. The findings are expected to enhance understanding of the relationship between geopolitical risk, investor behavior and stock market performance. Furthermore, the study provides valuable implications for investors in managing portfolio risk, policymakers in strengthening financial stability and researchers seeking to expand knowledge on geopolitical risk and finance by demonstrating how conflicts in critical geopolitical regions can influence global investment decisions and market stability.

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