

Markets might use the risk of war as excuse for another...

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My discussion on the economics of war yesterday appears to have been timely. Everyone now seems to be addressing the issue.

Martin Wolf [had a discussion of the subject](#) in the FT yesterday. His concern was not so much with the cost of military action, or its human impact. It was instead focused upon the consequence for the price of oil.

So far markets have not reacted in any significant way to the weekend aggression by Iran. Instead, they appear to have been following the diplomatic line of waiting to see what Israel does next. But, if there was a marked escalation, Martin Wolf is worried about the impact of any increase in the price of oil on global financial stability.

It is his suggestion that the savings buffers that protected the economy in the immediate aftermath of the Covid crisis (others suggest fuelled inflation) have now dissipated. As a consequence, he thinks that the margins for the management of an oil shock are small.

We also all know that oil and other traders have an enormous propensity to hike prices at the least provocation, always presuming that the merest hint of a shortage provides them with an opportunity for excess profit taking.

The latter worries me at least as much as any cost of military action, given that the human impact cannot be directly measured in monetary terms. Saying so, do recall that the majority of the inflation that we saw in the period from late 2021 until early 2023 was not caused by shortages in supply. It was, instead, created by financial speculation. The consequences were dramatic, and are continuing because of the increase in interest rates that could never have addressed the speculation that caused the price hikes, but which central bankers now wish to be a permanent feature of the economic landscape.

Another bout of speculation of a similar sort is now possible, no doubt with the likelihood that it will be reinforced by the desire of central bankers to at least maintain

interest rates, or even increase them. The likelihood that such speculative price increases might be necessary to address any real shortage of oil is extremely remote, as was proved in 2022. But if they happen, and the need for price increases and their happening are not related events, then we know that central bankers are as irrational as market traders, and they will find any reason, justified or not to hike interest rates.

The risk that the threat of war could give rise to another round of recessionary inflationary activity is very real, but is utterly justified at present by any real events actually occurring in the world. The problem is that market speculation takes place in its own make believe world where we all become the collateral damage.