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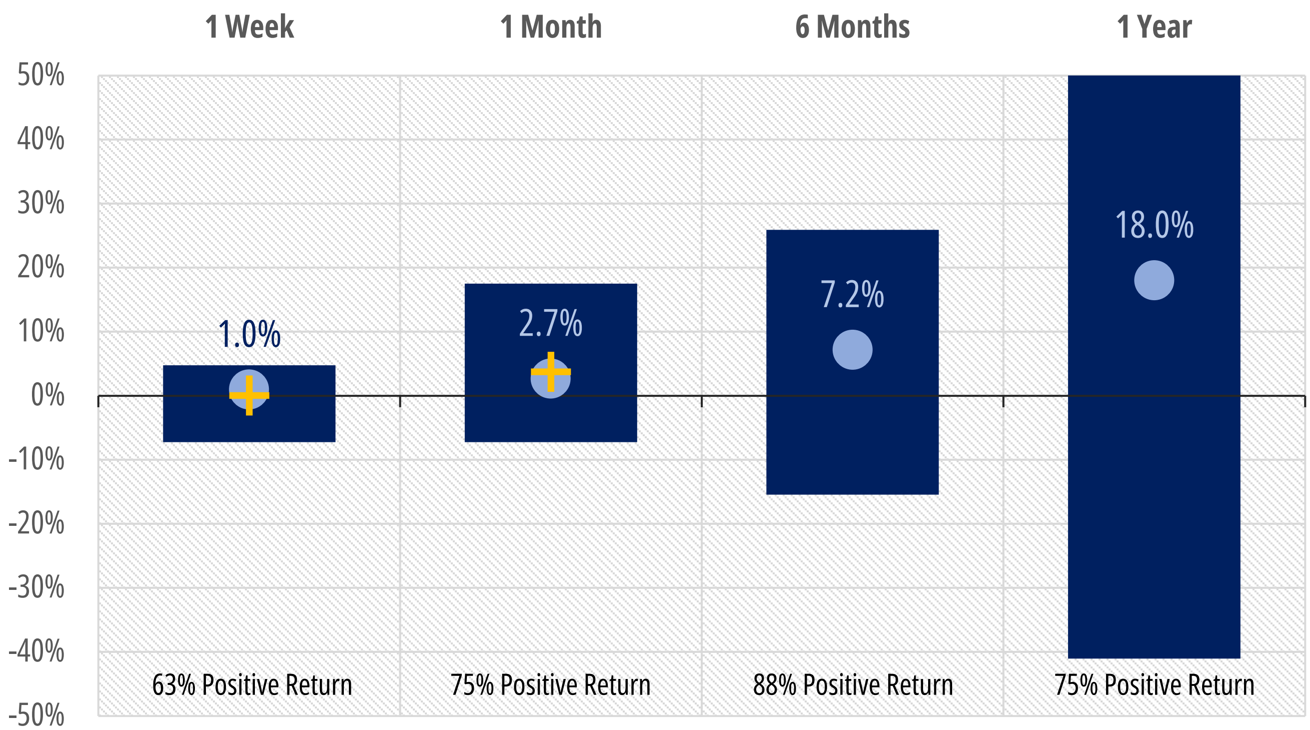
War and Markets

Volume 50 | March 2022

Armed conflicts are highly charged events that by their very nature generate legitimate and strong emotional responses. While there are many questions and implications around armed conflicts, as long-term investors, an important question is what we should do from an investment perspective? For guidance, we look at how the US stock market has reacted to 16 armed conflicts since the end of World War II.

SUBSEQUENT US STOCK MARKET RETURNS FOLLOWING ARMED CONFLICT SINCE WWII (1950 – PRESENT)



Source: List of armed conflicts from Encyclopaedia Britannica (https://www.britannica.com/topic/list-of-wars-2031197), returns are the Fama-French Market Return Series

The chart above (full data is provided on the last page) shows that median returns were positive following the onset of hostilities, even in the very short-term. The blue bars show the range of returns for each period and the blue dots represent the median results. The yellow + highlights the current Russia-Ukraine conflict. Finally, the note under each bar indicates the percentage of events resulting in a positive market return. The longer the timeframe, the higher the median return, which ranges from a 1% return one week later up to an 18% return one year later. So far, the current conflict is tracking in line with the median results.

It seems logical that dramatic and horrifying events should have an equally dramatic impact on global markets. But in practice, major geo-political events and their downstream effects are extremely hard to anticipate and evaluate. Over time, markets tend to gradually process and absorb short-term shocks and other factors begin to outweigh the single event. While we have no way of knowing the eventual outcome of the current war and its implications, for long-term investors, staying the course is often the best course of action.

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From the Behavioral Viewpoint

What is going on?

1. War triggers our **fight or flight instincts**. We are on the lookout for danger and prepared to flee. Our **two for one loss aversion** encourages us to act to avoid potential loss

2. Geo-political events and the constant chatter create a negative **availability cascade**, in which the never-ending stream of dramatic events have the potential to ruin everything.

3. We **overestimate** our ability to evaluate events and their implications and **underestimate** the randomness of world events. This **overconfidence bias** can result in emotional decisions which lead to costly behavioral mistakes.

What can we do?

1. Individual events are rarely a reliable basis for making investment decisions. Tune out the media when it comes to investments. Use a consistent approach to monitor the markets and the economy in order to keep emotions in check.

2. Use needs-based planning to separate short and long-term investments and to insulate your investments from short-term noise. Follow a well-developed investment process that delivers critical discipline.

3. Work with an experienced behavioral financial advisor. They can provide valuable perspective and coaching to help stay on track and remain focused on long-term plans and goals.

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Table of Armed Conflicts and Returns

No.	Armed Conflict	1 Week	1 Month	6 Months	1 Year
1	Korean War (1950–53)	-7.2%	-7.2%	10.6%	20.0%
2	Algerian War (1954–62)	1.3%	5.0%	21.1%	50.4%
3	Vietnam War (1954–75)	0.7%	2.4%	15.5%	38.4%
4	Six-Day War (1967)	2.1%	2.8%	8.3%	18.7%
5	War of Attrition (1969–70)	0.2%	3.0%	-3.1%	-7.0%
6	Yom Kippur War (1973)	1.3%	-4.5%	-15.4%	-41.0%
7	Dirty War (1976–83)	-0.5%	-0.5%	5.4%	2.9%
8	Afghan War (1978–92)	-3.5%	-5.5%	5.9%	8.7%
9	Iran-Iraq War (1980–88)	-2.3%	2.5%	6.5%	-4.2%
10	Falkland Islands War (1982)	2.2%	3.2%	9.1%	44.8%
11	Persian Gulf War (1990–91)	4.8%	17.5%	25.9%	44.5%
12	Bosnian conflict (1992–95)	-0.1%	2.1%	0.9%	12.6%
13	Kosovo conflict (1998–99)	3.2%	8.3%	5.5%	30.7%
14	Afghanistan War (2001–14)	2.2%	3.5%	7.9%	-23.6%
15	Iraq War (2003–11)	-0.3%	2.5%	21.7%	34.8%
16	Syrian Civil War (2012–)	2.8%	4.5%	4.2%	17.3%
Summary	Minimum	-7.2%	-7.2%	-15.4%	-41.0%
	Average	0.4%	2.5%	8.1%	15.5%
	Median	**1.0%**	**2.7%**	**7.2%**	**18.0%**
	Maximum	4.8%	17.5%	25.9%	50.4%
	Positive Outcome %	**62.5%**	**75.0%**	**87.5%**	**75.0%**
	Negative Outcome %	37.5%	25.0%	12.5%	25.0%
17	Russia-Ukraine conflict	0.1%	3.8%		

Source: List of armed conflicts from Encyclopaedia Britannica (https://www.britannica.com/topic/list-of-wars-2031197), returns are the Fama-French Market Return Series