Arda Viraz (the wise) with the divinities Sraosha, Mithra and Rashnu on the Chinvat Bridge.
Manuscript of the Zoroastrian Arda Viraz, 1789. John Rylands Library, Manchester.

HOUSE VIEW

HORMUZ AND THE CHINVAT BRIDGE

BancaMarch

HORMUZ AND THE CHINVAT BRIDGE

According to Persian mythology, after death, all souls must cross the Chinvat Bridge. A place where a divine tribunal presided over by Rashnu, guardian of justice, weighs the totality of the deceased's good and bad deeds on a golden set of scales. For the righteous, the bridge widens, becoming a path to paradise. For the wicked, however, the bridge narrows until it becomes as thin as the edge of a sword, making it impossible to cross before the souls fall into the abyss of hell.

Over the past few days, Iran has become angry and intends to turn Hormuz into its own Chinvat Bridge, determining who is righteous and who is wicked. The ayatollahs are resisting the fact that a significant proportion of shipping through the strait is now travelling through Omani waters in order to avoid being "identified". The shipowners' intention is clear: to circumvent the new "Gulf Strait Authority" created by Iran — in the manner of Rashnu — so that there is no administrative basis on which transit fees and charges could be levied in the future.

Iranian authorities have therefore selectively attacked some vessels linked to Western interests while allowing Chinese oil tankers to pass. Despite the alarmist headlines, and although the dispute may appear to be escalating following Trump's responses, everything points to these being skirmishes designed to exert pressure. In our view, a new phase truly began on 17 June. At the risk of sounding flippant, both sides continue to "test the waters" without seeking to bring the gradual reopening of the strait to an end. However many ups and downs there may be, the path towards normalisation is difficult to reverse, and this is reflected in crude oil prices. At $72 a barrel, Brent has not only fallen 39% from its peak, but the futures curve has also flattened completely. The spot price is trading at the same level as the six-month contract, pointing to less pressure on inventories. This price is in line with the average of the past two years and is excellent news for many companies that, such as airlines, commit to their purchases six months in advance.

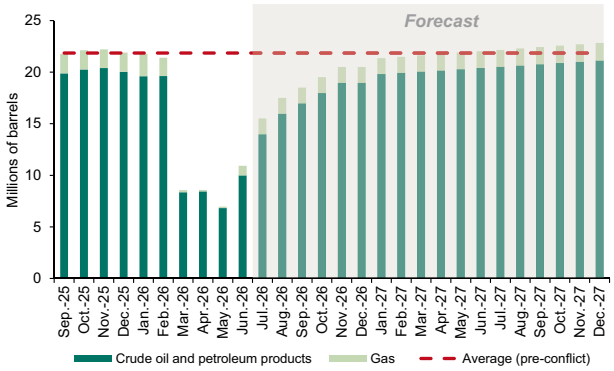
From our perspective, exports through the Strait of Hormuz will recover gradually: we estimate that within one month they will have reached 70% of pre-war levels and, by the end of the year, 95%.

Within this veritable Chinvat Bridge, it is particularly paradoxical that, while energy prices are entering a period of easing, we are simultaneously seeing expectations of interest-rate hikes by the Federal Reserve become more pronounced. The curve points to a first hike in October and, possibly, a second in March of next year.

This is undoubtedly the result of the rhetoric of Kevin Warsh, the newly appointed Federal Reserve chair, as well as the publication of the institution's dot plot, which raised the median estimated rate from 3.4% to 3.8%.

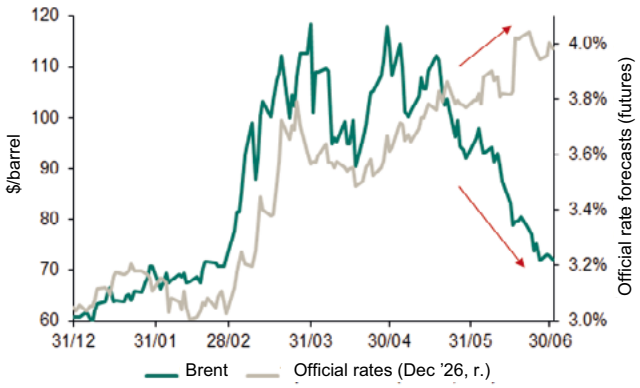
1. ESTIMATED RECOVERY IN EXPORTS THROUGH THE STRAIT OF HORMUZ

Sources: Bloomberg and Banca March



2. OIL PRICE PERFORMANCE VS. US OFFICIAL INTEREST-RATE EXPECTATIONS

Sources: Bloomberg and Banca March



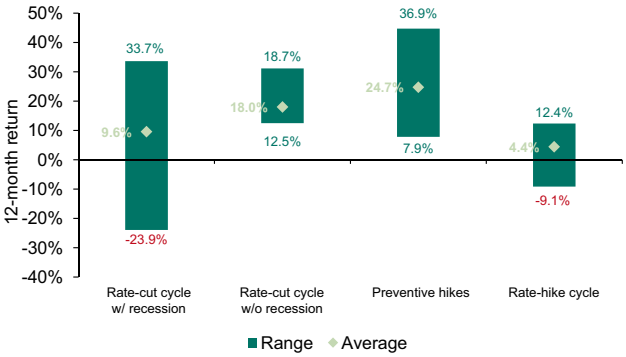
In any event, although we believe the market's current view of Fed rates is too hawkish — as it would be consistent with a scenario in which the Strait of Hormuz remained blocked and Gulf oil exports were unable to pass through — it is worth bearing in mind that stock markets rise more when the Federal Reserve raises interest rates than when it cuts them. This is because, historically, recessions have generally been accompanied by rate cuts, since by the time the monetary authorities realised that the cycle was turning, it was already too late.

Likewise, when rate hikes are preventive — and do not mark the beginning of a structural upward trend — equity market performance is particularly strong, because they confirm that the economic cycle is continuing and that companies are still generating profits. This was the case in 1984 and again in 1997, when the US economy achieved a soft landing and the S&P 500 posted average gains of more than 20% over the following 12 months.

Although at Banca March we believe that Kevin Warsh will not raise rates this year, if history is any guide, we should not be concerned about equities even if the hikes currently priced into the curve were to materialise. With Trump in the mix, our Chinvat Bridge will probably not be a gentle path to paradise accompanied by Daena, the beautiful sacred maiden, but in our view, there is still room for the market to continue rising.

3. S&P500: PERFORMANCE ACCORDING TO THE FED RATE REGIME (*)

Sources: Bloomberg and Banca March



(*) Preventive rate hikes: official interest-rate hikes that are not followed by further hikes over the next 12 months.

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