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Iran Update

Dear Investors,

We have become increasingly concerned about the situation in Iran. This interim research report sets out why we believe the likelihood of escalation may be as high as, or higher than, the probability of de-escalation.

Despite claims from Donald Trump that the war will be short, we remain sceptical that its duration can be unilaterally determined. Notably, he has acknowledged that timelines may shift as conditions evolve.

There are two major, interlinked challenges that make a short-term resolution to the conflict unlikely.

Problem 1

The first stems from the reality that, if the current Iranian regime remains in place, it cannot credibly rely on Israel or the United States to refrain from future attacks. Circumstances evolve, and recent history suggests that alliances can shift when strategic interests change. As a result, the regime requires a durable and credible security guarantee to ensure its long-term survival. The question, therefore, is how such a guarantee could be established.

In our view, the most effective form of deterrence available to Iran is control over the Strait of Hormuz. This represents its strongest, and potentially only, credible leverage. It is unlikely that Iran would place sufficient trust in external guarantors such as Russia or China, nor would it be willing to cede control by allowing foreign naval forces to operate along its coastline. Retaining control of the Strait provides Iran with the ability to escalate if threatened, reinforcing its deterrence posture. Consistent with this, messaging across Iranian political factions has remained aligned: the Strait cannot revert to its pre-war status.

The United States may, in time, find such an arrangement reluctantly acceptable, allowing traffic through the Strait of Hormuz to return to normal. Under such a scenario, the US would arguably not be in a materially worse position than prior to the conflict.

However, in the current context, sustained Iranian control of the Strait is unlikely to be tolerated. First, negotiations regarding a potential resolution are ongoing, and Iran is incentivised to push oil prices higher to maximise its bargaining power. Second, regional actors such as Saudi Arabia and the United Arab Emirates are unlikely to accept a scenario in which Iran can effectively hold their oil exports hostage. Given the extent of the conflict to date, and Iran's perceived military weakening, these countries may be incentivised to prolong the conflict, or potentially become more directly involved, to remove this risk.

It is difficult to see how Saudi Arabia and the UAE could be assured against this form of coercion without either a credible commitment to demilitarisation or a change in regime. The current Iranian leadership is unlikely to accept demilitarisation for two reasons. First, it would materially weaken its defensive capability at a time of heightened vulnerability. Second, the historical precedent of Gulf War and its aftermath reinforces the perception that disarmament can precede regime destabilisation, as seen in the case of Iraq.

We are therefore left with a structural impasse. On one hand, the Gulf States and the US cannot accept a scenario in which Iran retains control over the Strait of Hormuz. On the other, Iran views such control as its only credible security guarantee.



The absence of a mutually acceptable security framework may prove to be the central factor prolonging the conflict, much as it has in the Russo-Ukrainian War. In that case, the inability to establish credible and enforceable security guarantees has remained a key obstacle to resolution, with negotiations repeatedly stalling on this issue.

Problem 2

Iran appears to believe that time is on its side. As oil, energy and fertiliser prices rise globally, pressure on Western political systems is likely to increase, thereby enhancing Iran's leverage. At the same time, the US is unlikely to fully eliminate the threat to the Strait of Hormuz, given the difficulty of neutralising Iran's entire drone and missile capability. Iran requires only a residual level of capacity to maintain a credible threat. As such, if it cannot secure improved terms today, a prolonged conflict may strengthen its negotiating position over time.

When one side believes time is working in its favour, and neither side can deliver a decisive outcome despite asymmetries in resources, conflicts can become protracted. This dynamic has been evident in the Russo-Ukrainian War, where Russia has relied on its relative manpower advantage, and in the disruption to Red Sea shipping in the past driven by the Houthis, which persisted for an extended period despite sustained opposition.

The internal dynamics of the Iranian leadership also point toward continued resistance. Ali Khamenei is reportedly operating under heightened security constraints, communicating through a limited and trusted inner circle. In this context, statements from Abbas Araghchi may carry particular weight, given his longstanding proximity to the leadership. To date, his messaging has been consistent in rejecting a ceasefire and emphasising the need to continue applying pressure on adversaries.

From Iran's perspective, regime survival requires securing terms that are at least as favourable as, and likely more favourable than, those discussed prior to the conflict. This is viewed as necessary to establish a credible deterrent against future attacks. At a minimum, this implies retaining core military capabilities, including its ballistic missile program. However, such concessions are politically difficult for the US to accept. The result is a structural stalemate, with the conflict likely to persist until one side is able to materially shift the balance.

Other Considerations

A key question is whether the US could step back and leave regional and global powers, including China, Japan, South Korea, India, Australia, the United Kingdom and Europe, to manage stability in the Strait of Hormuz. While it is difficult to rule out entirely, we believe a full US disengagement would be challenging. Iran, alongside China and Russia, would likely retain strong incentives to push oil prices higher and to amplify anti-war sentiment in Western economies, both of which could influence domestic political dynamics and, potentially, the trajectory of the Russo-Ukrainian War.

There remains an alternative scenario that could avoid further escalation. Donald Trump could pursue a negotiated outcome, with limited public disclosure of its terms. However, this path is complicated by his stated objective of preventing Iran from obtaining nuclear weapons. Public remarks indicating that Iran retains a significant stockpile of enriched uranium, potentially sufficient for multiple weapons, create a credibility challenge. Absent clear and verifiable evidence of disarmament, it would be difficult to reconcile such a position with a de-escalation outcome. Moreover, a withdrawal without resolution could increase Iran's incentive to accelerate its nuclear capabilities.

Time appears to be working in Iran's favour. As a result, the US faces increasing pressure to act. Any such response is likely to involve further escalation, potentially through targeting critical infrastructure or attempting to seize Kharg Island. Either course of action would represent a material escalation, with uncertain scope for de-escalation thereafter.

We remain open-minded. It is possible that Iran ultimately chooses to reach an agreement to preserve the longevity of its current leadership. However, we view this as less likely given the opacity surrounding the leadership structure and decision-making process. More broadly, we acknowledge that there are factors at play which may not yet be fully visible.



At present, however, we assess there to be a meaningful risk that Donald Trump escalates the situation further. Should this occur, we would expect a corresponding deterioration in equity and broader risk markets. The risk-reward profile for equities appears unfavourable. In a downside scenario, markets could plausibly decline by a further 15–20%, comparable to the drawdown observed during the tariff-related sell-off in early 2025. In contrast, a near-term resolution may result in a more modest rebound, potentially in the order of 5%. On balance, we view the probability of escalation, as a means of forcing de-escalation, as higher than that of a negotiated compromise.

We continue to monitor developments closely and remain prepared to adjust our investment posture as conditions evolve.

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