



By Daniel Ortwerth, CFA

July 28, 2025

Implications of the Israel-Iran Conflict

During the night of June 13, an already unsettled Middle East was shocked to a new level of unrest when bombs from an Israeli airstrike rained down on Iran's key nuclear and military facilities. In what proved to be the opening salvo of a 12-Day War, which included the first use of "bunker-buster" bombs by the United States, [Israel asserted that the barrage was necessary before its adversary could get any closer to building an atomic weapon](#). In an already tense and conflict-ridden region, questions abound as to how this conflict will affect the Middle East's balance of power and the region's relations with the rest of the world. With Iran's nuclear program at the center of the conflict and the future of its government in question, a heightened sense of risk and uncertainty looms large over the deliberations of global leaders.

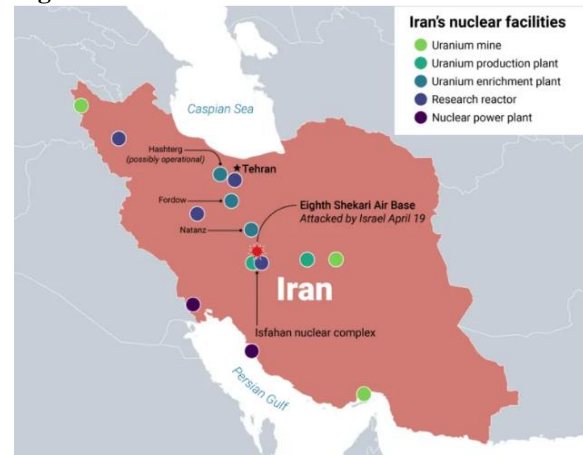
This report provides an overview of the war and discusses where things stand now (at least as of our publication date). The report also addresses the conflict's likely impact on the Middle Eastern balance of power and examines its possible long-term regional effects. As always, we conclude with investment implications.

The "12-Day War"

Although conditions in the Middle East remain fluid, a brief synopsis of the war's chief events provides a helpful context.

From the first night, the [Israeli Air Force \(IAF\) flew more than 1,000 sorties against Iranian targets](#), focusing on its nuclear sites (see Figure 1), air defense system, ballistic missile force, and key leadership figures.

Figure 1



(Source: thebulletin.org)

Having achieved uncontested air superiority over Iran, the IAF lost no aircraft or personnel; however, Iran retaliated with waves of missile and drone attacks against Israel, targeting both civilian and military sites. [An estimated 16% of Iran's missiles and one drone penetrated Israeli air defenses, reaching five military sites](#) as well as several civilian areas.

The conflict reached a crescendo on Saturday, June 21, when [US B-2 bombers dropped 14 GBU-57 Massive Ordnance Penetrators](#) (aka bunker busters) on Iran's most hardened underground nuclear facilities at Fordo and Natanz. Submarine-launched Tomahawk cruise missiles also struck the nuclear facilities at Isfahan. In response, Iran launched a pre-announced

attack of 14 missiles on the US Air Force's Al Udeid Air Base in Qatar, causing minimal damage and no casualties. After a few more relatively minor attacks from each side, a fragile ceasefire began on June 24.

Post-Conflict Questions

In our view, two immediate questions arise in the wake of the conflict: To what extent has Iran's nuclear program been damaged, and will a stable, negotiated resolution now materialize?

State of the Nuclear Program. An accurate assessment of the damage to Iran's nuclear facilities would probably require first-hand, onsite inspection. Satellite imagery and other forms of remote battle damage assessment provide only limited information, especially with underground sites, and we doubt that Tehran will allow onsite inspection or volunteer the truth to the rest of the world. On the high end of estimates, [the Trump administration claims the US strikes obliterated the facilities, and the Israeli Atomic Energy Commission asserts that the strikes will set back the Iranian nuclear program by "many years."](#)

According to a preliminary classified US intelligence report, however, [the US strike only delayed Iran's nuclear program by less than six months](#). As the weeks pass, we expect additional information to emerge, potentially from [Israeli intelligence, which is believed to have extensively penetrated the Iranian security apparatus](#). Israeli intelligence might eventually be able to provide an eyewitness damage assessment. Meanwhile, questions abound as to Iran's surviving resources, such as the location of the country's stockpile of partially enriched uranium.

State of Negotiations. The US and Iran had conducted a series of five negotiating

sessions, moderated by Oman, prior to the 12-Day War. A sixth session was scheduled to occur June 15, only two days after Israel's surprise attack. Now that hostilities have ceased, both the US and Iran have expressed an interest in restarting the negotiations, but both camps have made conflicting statements about the timing and scope.

[Informed sources in Tehran said the Iranian government has confirmed its attendance at a new round of negotiations in Oslo during July](#), alleging that the Trump administration has also said that it will attend. Later, at a dinner with Israeli Prime Minister Netanyahu, President Trump said that Iran requested the resumption of negotiations. Contradicting this, [the Iranian Foreign Ministry stated that, "No request for a meeting has been made on our side to the American side."](#) While the talks are likely to resume, these and other examples of vague or contradictory statements suggest the two parties will approach the table with differing agendas for what is to be negotiated, to say nothing of actual positions or demands. Ultimately, we expect this to drag out for months.

Tilting Balance of Power

Once the dust settles on the immediate issues, the Israel-Iran conflict will likely have a lasting impact on the regional balance of power, as discussed below.

The Big Four. As we showed in our [report on the Middle East and its many fault lines](#), there are four major powers that are the most influential in the region and three of them — Turkey, Saudi Arabia, and Iran — have been dominant for centuries. The fourth, Israel, has joined this group since just after World War II. Among the 15 countries of the region, the Middle East's "Big Four" have historically had the largest economies, although the United Arab Emirates'

economy has surpassed that of Iran over the last decade (see Figure 2).

Figure 2

GDP, 2024 Middle East		
Source: International Monetary Fund		
Country	GDP (Bil.)	% of Region
Turkey	\$1,322	26%
Saudi Arabia	\$1,085	21%
Israel	\$540	10%
UAE	\$537	10%
Iran	\$401	8%
Egypt	\$383	7%
Iraq	\$277	5%
Qatar	\$221	4%
Kuwait	\$159	3%
The Rest	\$255	5%

[The Middle East's Big Four countries have also historically had the largest defense budgets in the region](#) (see Figure 3). The choice of exchange rate significantly impacts the dollar value of Iran's defense spending, with the country's official fixed rates showing higher figures than international rates. Although we use the most widely recognized source for our figures, the \$8 billion estimate shown here may significantly underestimate Iran's military expenditure and capabilities.

Figure 3

Defense Spending, 2024 Middle East		
Source: SIPRI		
Country	USD (Bil.)	% of Region
Saudi Arabia	\$80	43%
Israel	\$47	25%
Turkey	\$25	13%
Iran	\$8	4%
Kuwait	\$8	4%
Iraq	\$6	3%
Oman	\$6	3%
Jordan	\$3	1%
Egypt	\$2	1%
The Rest	\$2	2%

Iran's Losses. Iran's losses in the 12-Day War form just a part of the broader losses it has suffered in the cycle of violence that began with the outbreak of the Gaza conflict in October 2023. Iran's broader losses since then center on its "Axis of Resistance," i.e., the [loose, informal network of militant groups and state-controlled armed forces that Iran and its Islamic Revolutionary Guard Corps \(IRGC\)](#) have long supported throughout the Middle East. In addition to the IRGC, the axis has comprised Hezbollah in Lebanon, Hamas and the Palestinian Islamic Jihad (PIJ) in the Gaza Strip and the West Bank, certain militias in Iraq, and Houthi forces in Yemen (see Figure 4). Until December 2024, when the government of Bashar al-Assad was toppled, the Syrian armed forces had been a key component of the axis and allowed unfettered access between Iran and the Mediterranean Sea.

Figure 4



(Source: United States Institute of Peace)

The Axis of Resistance has long shaped the politics, societies, and security environment of the Middle East, giving Iran the ability to exercise influence beyond its borders; however, the recent [cycle of conflict has severely weakened the Axis and Iran's ability to support it](#). Hamas has been decimated. Hezbollah has been badly degraded to the point where there have been public reports about its wariness of getting drawn into this conflict between Israel and Iran. Bashar al-Assad's regime in Syria is gone. The Houthis have suffered considerable losses from US and Israeli strikes. Iran's proxy and partner network is now a shell of its former self, as is the Islamic Republic's ability to project its influence throughout the region.

Others' Gains (Especially Turkey).

Arguably the largest loss to Iran over the last two years has been the fall of the Assad regime in Syria, and Turkey seems poised to gain the most from it. [As our report on that regime's fall explains](#), the rebel group that overthrew the regime and replaced it as the new Syrian government is effectively a proxy of Turkey. Before the overthrow,

Turkey provided it with critical funding, equipment, training, and logistics support. Now that this group is the new government of Syria, [it has deepened its relationship with the Turkish government](#), along with breaking its former ties to Iran. Whereas Syria formerly served as the prime conduit for militants and supplies between Iran and the Mediterranean, during the 12-Day War [it functioned as a transit corridor for Israeli jets refueling over its eastern skies without resistance en route to deep strikes inside Iran](#). Meanwhile, [Turkish President Erdoğan has elucidated a vision for Syria in which Turkey exercises exclusive control over a virtual protectorate state](#).

This scenario has likewise benefited other countries. Israel has moved to extend its security buffer in its northeastern region along the Syrian frontier, and [the Gulf States, led by Saudi Arabia and the United Arab Emirates, are showering the new regime with funding to buy influence](#).

Long-Term Effects

Beyond these relatively near-term impacts to the regional balance of power, we expect long-term impacts as well. The fluid situation makes prediction difficult, but we can posit the following likely changes.

Iranian Regime Change. Regime change can take more than one form. There can be an outright change, in which the government falls and gets replaced by a new one. It can also take a stealthier form, in which the government structure remains in place, but key members are replaced and radical policy changes (previously considered out of the question) are implemented. In any case, the future of the Iranian regime has become a central topic of speculation, due to [attribution of the country's failures to the regime's sclerotic decision-making and emerging signs of infighting within its](#)

[ranks](#). Unstable and opaque situations such as this can turn in surprising directions. The classic example is the [collapse of the Soviet Union](#). At the time, virtually no Western experts, Soviet or foreign officials, or even Soviet reformers foresaw the impending collapse of the system of one-party dictatorship, state ownership of the economy, and the Kremlin's control over its domestic and Eastern European empires. Something similar could happen in Iran with little notice to the outside world; however, considering the resilience of regimes such as this, we assess it is [more likely that the regime and its political system will endure, but with transformational internal changes](#). These changes could potentially alter how the regime conducts its foreign policy.

Small-Country Realignments. In any geopolitical system, the strongest countries dominate, while smaller countries align themselves with the larger powers that best serve their interests. If the balance of power among the dominant players shifts, then the smaller nations might find themselves in a position where a strategic realignment better serves their interests than the old loyalties. With this weakening of Iranian power, we may witness any number of smaller Middle Eastern countries shifting their positions.

The case of Lebanon illustrates this idea. [The Shi'ite Muslim political party and militant group Hezbollah have dominated Lebanon since its emergence during the country's 1975-90 civil war](#). Hezbollah has been one of Iran's most powerful and loyal allies; it has dominated Lebanese politics and society, and this has held Lebanon tightly under Iranian influence. The last two years have fundamentally altered this state of affairs. Israel has waged a devastating campaign against the organization, most prominently through the [Pager Caper](#), when it used compromised hand-held devices to

kill dozens of Hezbollah's top figures. Together with the losses Iran has directly sustained and the loss of Syria as a conduit for supply, Hezbollah's (and hence Iran's) influence over Lebanon has been crippled.

With the door open to a potential realignment, we note that Lebanon enjoyed a very different reality and reputation before its civil war and era of Iranian domination. Once known as the "[Switzerland of the Middle East](#)," pre-revolutionary Lebanon was economically prosperous and known for its flourishing banking sector and pluralistic society. Its mountainous terrain was once dotted with ski resorts and its lush Mediterranean coastline attracted wealthy tourists. With this kind of demonstrated potential, Lebanon could enjoy a rebirth for itself and become a key member of a different regional alliance in the future.

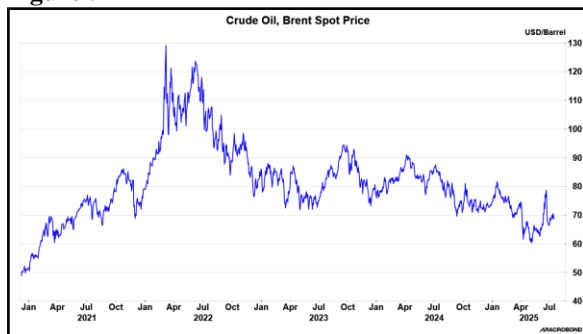
A Cautionary Tale. History is replete with examples of unexpected outcomes following major events. The Middle East is a region with a delicate balance, and changes in power can produce unintended and unforeseen consequences. For example, after removing Saddam Hussein from Iraq in 2003, a civil war ensued, and Iran emerged as a stronger power with Iraq under its sway. At present, the bombing of Iran and the weakening of its regional position appears to have improved Israel's position, but it is far too early to know with certainty what the eventual outcome will be. The range of possibilities is wide, and only time will tell.

Investment Implications

We judge that the key investment implications of the 12-Day War relate to the global oil market in the short-to-medium term and the world's overall level of geopolitical insecurity and uncertainty over the longer term, as discussed below.

Oil. The global market has shown a surprising ability in recent years to take Middle Eastern conflict in stride, with the price of oil remaining relatively stable (see Figure 5). There is always the possibility of a price spike in response to an extreme event, such as Iran’s attempt to close the [Strait of Hormuz, through which 20% of global petroleum consumption flows](#); however, *it seems increasingly likely that oil prices will ride out Middle Eastern turmoil*. Compared to previous historical periods when Middle Eastern crises shocked the oil markets, global supply has diversified, with new or growing supply coming from places such as the US and Guyana. Also, [advancing technology has enabled improved management and enhanced visibility of global transportation flows](#). When the 12-Day War began, oil market participants were able to use new tracking capabilities to determine in real time whether the number of tankers transiting the Strait of Hormuz had changed. Observing virtually no impact, traders refrained from bidding up the price.

Figure 5



(Source: Macrobond)

Rising Turmoil & Uncertainty. Israel’s bold move to bomb Iran fits an increasingly evident global pattern. Boundaries and norms that had been relatively stable elements of the global order for decades are losing their force. We view this trend as a natural consequence of the US reassessing its global commitments and willingness to serve as the global hegemon. In the wake of this retreat of the world’s stabilizing force, countries in virtually every region are increasingly asserting themselves and taking security matters into their own hands, rather than relying on the US or the international, “rules-based order” to protect them. As this pattern unfolds, *the world will become an increasingly risky place*. This makes the global investment environment riskier than what was typically the case in the post-Cold War era of globalization.

Among the consequences, we expect countries and investors alike to respond to rising risks with budgets and investment allocations tailored to this new landscape. This will include rising defense budgets, which will benefit not just the global defense sector, but also related industrial and technology sectors, especially those focused on infrastructure and cybersecurity. We expect the price of gold to continue to rise as central banks and investors turn to the yellow metal as a safe haven asset. We also expect rising interest rates and higher inflation as governments issue more debt to finance rising expenditures.

Daniel Ortwerth, CFA
July 28, 2025

This report was prepared by Daniel Ortwerth of Confluence Investment Management LLC and reflects the current opinion of the author. It is based upon sources and data believed to be accurate and reliable. Opinions and forward-looking statements are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security.

Confluence Investment Management LLC

Confluence Investment Management LLC is an independent Registered Investment Advisor located in St. Louis, Missouri. The firm provides professional portfolio management and advisory services to institutional and individual clients. Confluence’s investment philosophy is based upon independent, fundamental research that integrates the firm’s evaluation of market cycles, macroeconomics, and geopolitical analysis with a value-driven, company-specific approach. The firm’s portfolio management philosophy begins by assessing risk and follows through by positioning client portfolios to achieve stated income and growth objectives. The Confluence team is comprised of experienced investment professionals who are dedicated to an exceptional level of client service and communication.