



Iran Risk Rises Sharply, Fed Sees Stronger Growth, Markets Fear Oil

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Monday morning, Trump has announced a 5-day postponement in strikes on Iran's infrastructure and indicated the "productive talks took place over the weekend." This sparked a huge rally in equities, and a drop in oil and treasury yields. This announcement is significant as it marks the first ever de-escalation in the war. The situation, of course, remains very fluid and is subject to sharp swings. Iran events will dominate the movements in markets this week.

As for other events, the markets spent the week obsessing over the wrong thing. The Fed meeting was not hawkish. The Federal Reserve left the funds rate at 3.50% to 3.75%, kept its median year-end rate projection at 3.4%, and still sees 3.1% next year. That still amounts to roughly one 25-basis-point cut this year and another next year.

At the same time, the Fed raised its 2026 real GDP forecast to 2.4% from 2.3%, lifted 2027 to 2.3% from 2.0%, 2028 to 2.1% from 1.9%, and, most important, moved its longer-run growth estimate up to 2.0% from 1.8%. Markets sold off anyway because oil, not the dot plot, became the dominant variable.

That higher longer-run growth number is the real story. Central banks do not casually move trend growth higher. A 20-basis-point increase in the longer-run GDP estimate is the Fed acknowledging that productivity is improving, and I believe AI is a meaningful part of that story. That matters much more than most investors appreciate.

Faster productivity growth lifts earnings, improves the long-run fiscal arithmetic, and allows the economy to run stronger without recreating the inflation regime of 2022. Historically, markets are slow to recognize when the supply side of the economy has improved. This time should be no different. The productivity story is more durable than this week's Iran developments, which is dominate trading over the near term.

Yes, the Fed also raised its inflation forecast. But the composition matters. Powell said much of the current pressure is tied to goods inflation from tariffs and not to higher energy prices, and he made clear that these projections are unusually uncertain. That is not the same as saying the economy is slipping into a new wage-price spiral.

Real-time housing data continues to point the other way. Apartment List says national rents are down 1.5% from a year ago and vacancy has risen to a record for its index, while Zillow says asking-rent growth slowed to 1.9% in February and that 39.2% of listings offered concessions. Shelter inflation will follow these more timely indicators. Meanwhile, M2 growth is well-behaved, with AI-driven efficiency gains, and the medium-term inflation trend still looks lower, not higher.

My base case is straightforward. The Fed does nothing at the next meeting. After that, the path of rates depends much more on oil than on anything in the current dot plot. If crude stabilizes and tariff effects begin to roll off in the middle of the year, the Fed still has room to cut later in 2026. If the energy shock intensifies and inflation expectations move materially higher, those cuts will be delayed. That is one reason why the long bond has been under pressure. The market is demanding a higher term premium because geopolitical risk and more defense spending, fiscal anxiety, and energy inflation are all hitting at once. The important point is that yields are responding to oil and uncertainty, not to a materially more hawkish Federal Reserve.

For investors, that distinction is crucial. An oil shock can absolutely produce a correction, and it will hit cyclicals and disposable-income-sensitive groups first. But a correction is not a collapse. If the Middle East risk premium eases, this market can turn very quickly back to earnings and productivity, and from the March 20 close near 6,508 I would expect the S&P 500 to work back toward 6,900 to 7,000 before year-end.

I would not chase the energy spike. I would continue to favor high-quality equities over long-duration bonds and use volatility to add to productivity beneficiaries, select technology, and dividend growers. International markets have been interrupted more than invalidated; a stronger dollar and higher oil are temporary headwinds, and a de-escalation would reopen the valuation case in Europe, Japan, and emerging markets, while the global defense-tech cycle remains a longer-run tailwind for innovative new technologies outside the U.S.

The bottom line is simple. This was a constructive Fed meeting disguised by an ugly geopolitical tape. The Committee acknowledged stronger trend growth, kept its basic easing bias alive, and implicitly recognized that the U.S. economy is more productive than it thought three months ago. The near-term problem is oil. The longer-term story is productivity. I am not dismissing the risk of a correction, but I remain optimistic because growth, earnings, and AI-driven efficiency are more durable forces than a temporary shock in energy markets.

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