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# How U.S. Bank Stock Prices Respond to Geopolitical Risk

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Geopolitical risk has emerged as a central driver of global financial markets, with episodes such as Russia's invasion of Ukraine and recent conflicts in the Middle East triggering sharp movements in asset prices and increases in market volatility. But not all industries are exposed to such shocks in the same way (Caldara and Iacoviello 2022; Culver, Niepmann, and Shen 2025). This brief zooms in on the banking sector, examining how geopolitical risk affects U.S. bank valuations and which institutions are most vulnerable.

Banks, through cross-border lending, foreign subsidiaries, and trading activities, face multifaceted exposure to geopolitical risk that can affect their profitability via credit losses, disrupted funding markets, and altered fee income. Banks' valuations, in turn, influence their funding costs and capital-raising capacity, ultimately affecting credit supply to the real economy.<sup>1</sup> And if geopolitical risk affects some banks more than others, it may create uneven vulnerabilities within the financial system, which would have implications for financial stability.

We examine how U.S. bank valuations—that is, their stock prices—respond to geopolitical risk and identify the institutional characteristics that drive variation across banks. While bank equity indexes broadly track the wider equity market, we document substantial differences between the responses of individual banks' stock prices. In particular, we find that banks with weaker earnings, smaller liquidity buffers, and larger operations in geopolitically stressed regions experience significantly larger equity declines from global geopolitical shocks.

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## Key Takeaways



U.S. bank stock prices, on average, move in line with the broader equity market during geopolitical shocks.



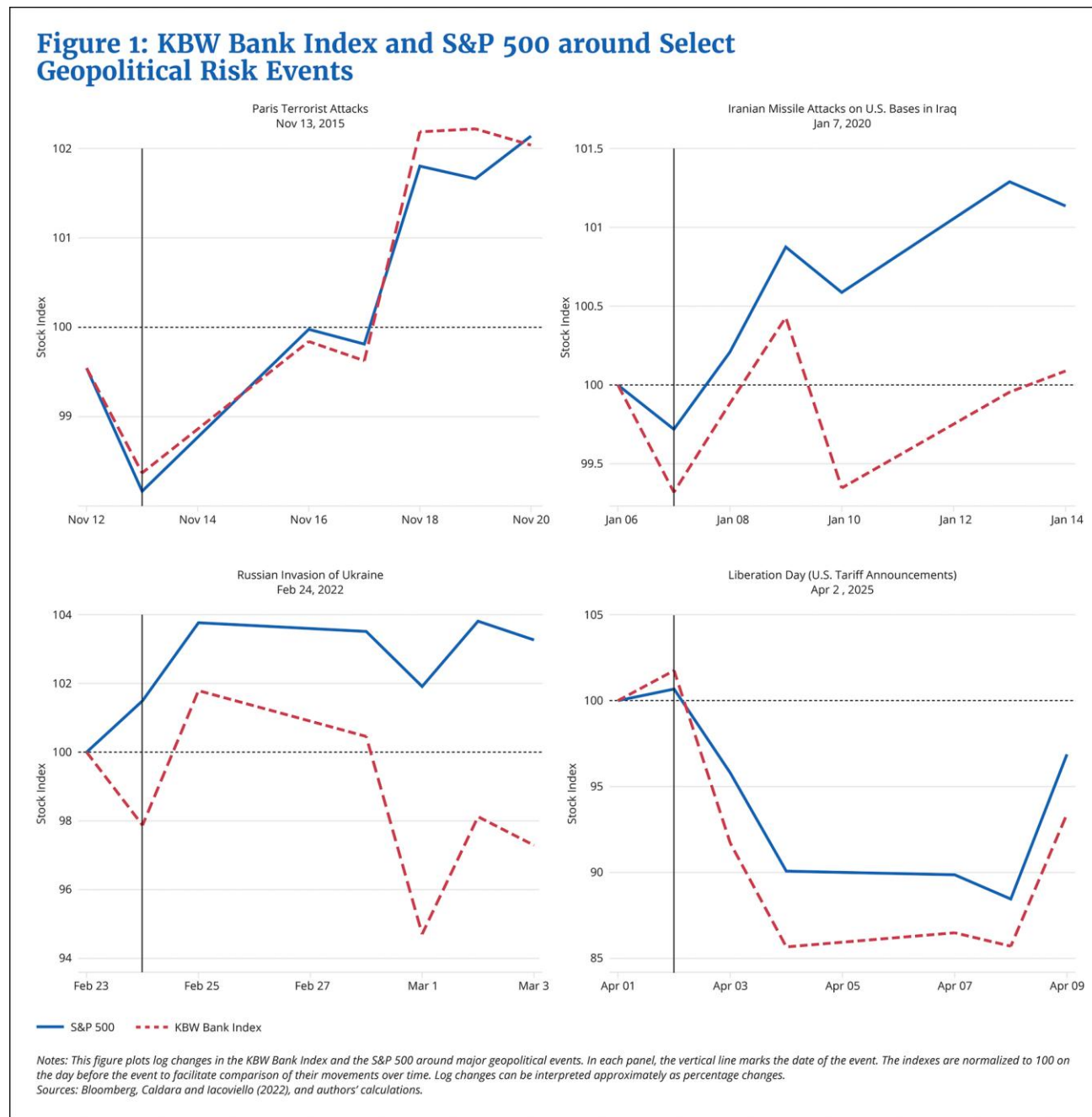
However, there is substantial variation in stock price sensitivity to geopolitical risk across individual banks.



U.S. banks with weaker earnings, smaller liquidity buffers, and larger operations in geopolitically stressed regions experience significantly larger equity declines from global geopolitical shocks.

## How Bank Stock Prices Respond Relative to Other Industries

Industries differ substantially in their exposure to geopolitical risk. A natural way to measure such exposure is through the sensitivity of stock prices to changes in geopolitical risk, as changes in stock prices capture investors' expectations about how heightened risk will affect future profitability. As Culver, Niepmann, and Shen (2025) document, international conflicts can hurt some industries (for example, travel and transportation) and benefit others (for example, pharmaceuticals and defense).



We assess the effect of geopolitical risk on the banking sector by estimating the sensitivity of U.S. bank stocks, specifically the KBW Bank Index, to changes in the Caldara and Iacoviello (2022) daily global geopolitical risk (GPR) index. The KBW Bank Index tracks the performance of 24 major U.S. banking stocks and serves as a benchmark for the banking sector. Caldara and Iacoviello's GPR index is based on the

content of newspaper articles and how frequently they include references to adverse geopolitical events and associated risks. The appendix accompanying this brief describes our regression analysis associating daily changes in the KBW Bank Index to the GPR index.

The results from our analysis reveal three important patterns. First, bank stock indexes exhibit significant negative responses to GPR index increases when we don't account for the S&P 500 return, which reflects the status of the broader equity market. We estimate that a one-standard-deviation increase in the GPR index is associated with an approximately 0.1 percentage point decrease in the price of bank stocks. Second, bank stock prices are more sensitive to geopolitical risk during crisis episodes. Our analysis capturing the Global Financial Crisis, the European Sovereign Debt Crisis, and the COVID-19 pandemic suggests that a rise in geopolitical risk weighed on bank stock prices in particular during these episodes. This is consistent with the idea that markets are more sensitive to adverse geopolitical news when financial conditions are already strained. Third, when we control for the S&P 500 return, the effect of a change in the GPR index becomes small and statistically insignificant. This suggests that bank stock prices, on average, move in line with the broader equity market during geopolitical shocks.

Figure 1 (preceding page) shows changes in the S&P 500 index (solid line) and the KBW Bank Index (dashed line) around major geopolitical risk events. Specifically, we show movements around the terrorist attacks in Paris in 2015, Iranian missile attacks on U.S. bases in Iraq in 2020, Russia's invasion of Ukraine in 2022, and Liberation Day in 2025, when the United States introduced reciprocal tariffs on its imports. While there was some divergence around specific events, such as the outbreak of the Russia–Ukraine war, overall both indexes moved largely in parallel as the events unfolded.

The similarity between the responses of bank stock prices and the overall equity market to geopolitical risk likely reflects offsetting effects. On the one hand, banks often benefit from volatility through higher trading volume, which boosts their fee income. Additionally, geopolitical risk can trigger a rise in inflation and potentially higher interest rates, which banks can benefit from through higher net interest income (see endnote 1). On the other hand, geopolitical risk can dampen economic activity (Caldara and Iacoviello 2022), reduce loan demand, and increase credit risk. For globally active banks, geopolitical shocks can have a direct effect through their foreign operations, as shown in Niepmann and Shen (2025).

## Substantial Heterogeneity in Stock-price Sensitivity across Banks

While the banking sector as a whole responds to geopolitical risk similarly to the broader equity market, we find substantial variation across individual institutions. We measure bank-specific sensitivity to geopolitical risk by estimating bank-specific *GPR betas*.

A bank's GPR beta measures how its stock price tends to respond to changes in geopolitical risk. We estimate this relationship using daily stock returns (the log change in stock prices) and daily changes in the GPR index over the period from January 2000 to June 2025. Specifically, we relate stock returns to next-day changes in the GPR index. (We use *next-day* changes in the GPR index because, as noted, the index is constructed from newspaper coverage, which tends to reflect geopolitical developments with a short delay relative to financial markets.) This estimated sensitivity coefficient captures how strongly a bank's stock price reacts, on average, to changes in geopolitical risk. A more negative value indicates that the bank's stock price tends to decline more sharply when geopolitical risk increases.

We focus on 38 large U.S. banks with at least 12 years of stock price data since 2000. This sample includes major universal banks, large regional institutions, and specialized banks, providing a diverse cross section of business models and geographic footprints.

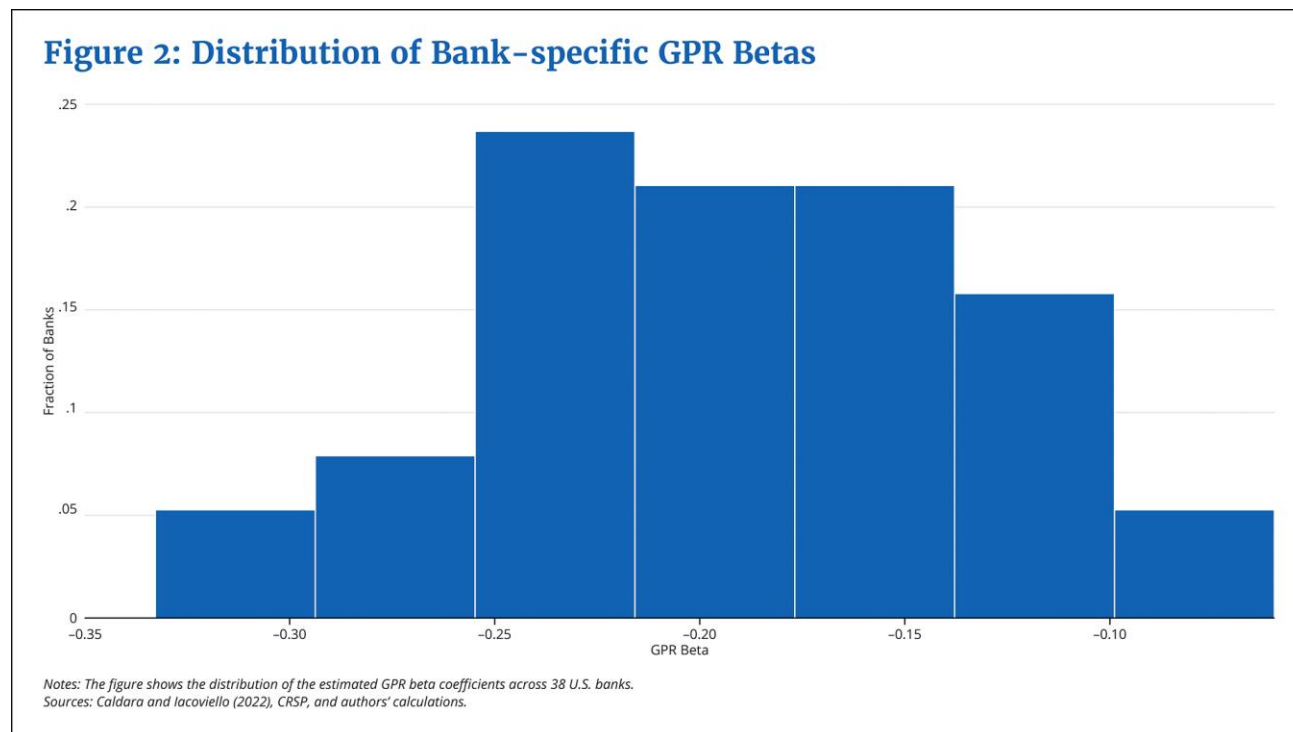


Figure 2 charts the distribution of the estimated GPR betas for the 38 banks. While most banks experience negative stock price responses to geopolitical risk increases, the magnitude of this response varies considerably across institutions. GPR betas range from approximately  $-0.33$  to  $-0.06$ , with a median of approximately  $-0.19$ . The median beta implies that a one-standard-deviation increase in the GPR index reduces bank stock prices by about 0.1 percentage point, which is consistent with our findings concerning the response of the KBW Bank Index to changes in the GPR index. This heterogeneity raises a natural question: Which bank characteristics explain the variation in geopolitical risk sensitivity?

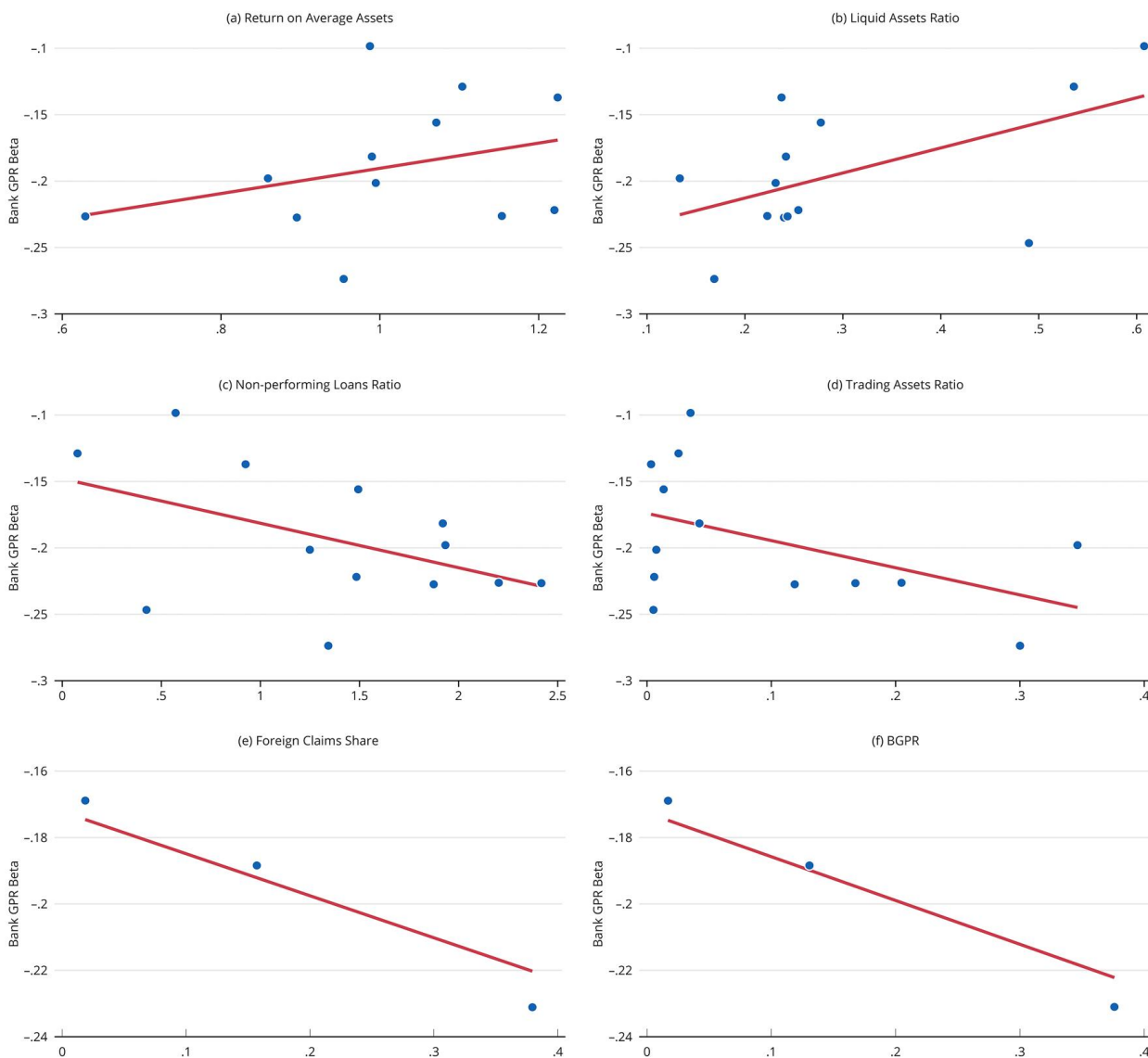
## Explaining the Heterogeneity

To understand what drives differences in banks' stock price sensitivity to geopolitical risk, we examine the explanatory power of seven bank characteristics:<sup>2</sup>

- **Tier 1 capital ratio:** Better-capitalized banks—those with a high ratio of regulatory capital to risk-weighted assets—may be more resilient to shocks, potentially exhibiting lower geopolitical risk sensitivity.
- **Return on assets:** More profitable banks—those that generate higher earnings relative to their assets—may be better positioned to deal with the effects of heightened geopolitical risk and continue distributing capital to shareholders.
- **Liquid assets ratio:** Banks with larger liquidity buffers—measured as a high ratio of cash and securities to total assets—may be better protected during periods of market stress.
- **Non-performing loans ratio:** Non-performing loans are loans on which borrowers have fallen behind on payments or stopped making payments altogether. If a large share of a bank's loans is in default or significantly overdue, the bank may be more constrained in distributing profits and therefore more vulnerable to geopolitical risk shocks.

- **Trading assets ratio:** Trading assets are securities and financial instruments held primarily for short-term resale or market-making activities. Banks with larger trading operations may benefit from volatility-induced fee income, potentially offsetting negative effects of geopolitical risk.
- **Internationalization:** Banks with larger foreign operations may face greater direct exposure to geopolitical risk events.
- **Geography of foreign operations:** Beyond the overall extent of international activity, banks with greater exposure to countries experiencing geopolitical risk may be more vulnerable to geopolitical shocks.

**Figure 3: Bank Characteristics and GPR Stock Price Betas**

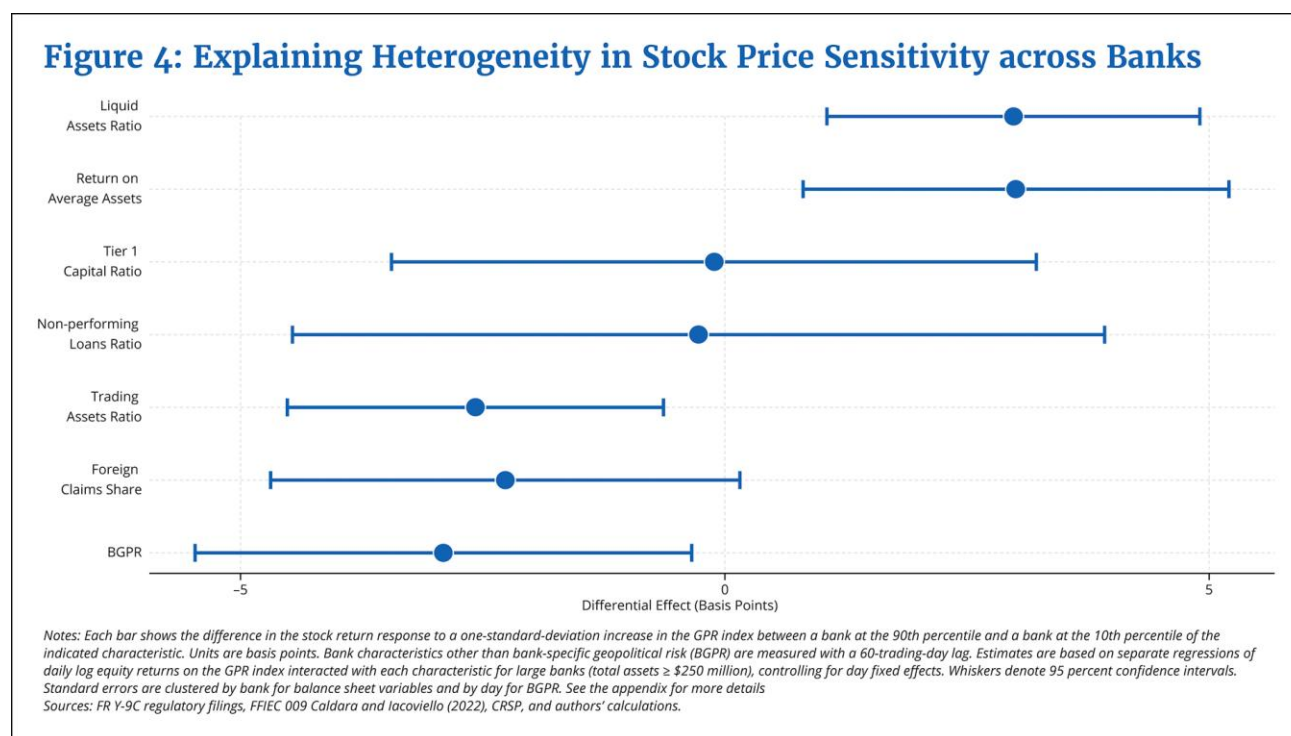


Notes: The panels in the figure plot the relationship between different bank characteristics and estimated GPR betas, showing bin scatter plots in panels (e) and (f) to preserve the confidentiality of the data. Each point represents the (average) estimated GPR beta and the corresponding bank characteristic. Bank-specific geopolitical risk (BGPR) is computed following Niepmann and Shen (2025) by weighting country-level GPR indexes by each bank's geographic exposure shares and is summed over the sample period of stock returns used to estimate the GPR beta of each bank. The line shows the fitted relationship from a linear regression. See the appendix for more details.  
Sources: FR Y-9C regulatory filings, FFIEC 009, Caldara and Iacoviello (2022), CRSP, and authors' calculations.

We measure whether the geography of banks' foreign operations matters by following Niepmann and Shen (2025) and constructing bank-specific geopolitical risk (BGPR). BGPR captures not just whether a bank is internationally active, but where it operates and whether those foreign countries are experiencing geopolitical risk. The accompanying appendix includes details on how we construct BGPR and on our regression analysis involving bank stock prices, the GPR index, and bank characteristics.

In our analysis, we examine heterogeneity in stock price responses among smaller and larger banks separately. The relationships are substantially stronger for the larger banks—those with more than \$200 billion in average total assets. These institutions are generally more internationally active and more integrated into global financial markets and therefore more exposed to the cross-border channels through which geopolitical risk is likely to operate. This is consistent with the broader literature on global banks and international shock transmission (for example, Peek and Rosengren 1999 and Fillat, Garetto, and Corea-Smith 2023). Several of the factors we propose significantly explain differences in stock price responses within this group of banks. By contrast, we find fewer robust relationships between bank characteristics and geopolitical risk sensitivity among smaller, more domestically oriented banks.<sup>3</sup>

Figures 3 (preceding page) and 4 show the results based on our analysis of the 13 largest banks. Figure 3 plots the relationship between each bank characteristic and estimated GPR betas. Figure 4 quantifies these relationships based on formal regression analysis: Each bar shows, in basis points, the differential excess stock return response to a one-standard-deviation increase in the GPR index between banks at the 90th and 10th percentiles of each characteristic based on the regressions reported in Table A2 in the appendix.



Capitalization does not seem to systematically affect bank stock price responses to geopolitical shocks.<sup>4</sup> By contrast, profitability matters: A bank at the 90th percentile of return on average assets experiences a 3 basis point smaller decline in stock prices compared with a bank at the 10th percentile, which is consistent with greater profits increasing a bank's ability to distribute capital under adverse circumstances. Banks that have larger liquidity buffers exhibit lower sensitivity to geopolitical risk by the same magnitude. This is consistent with the view that liquidity provides protection during periods of elevated uncertainty and market stress when funding costs may rise.

The non-performing loan ratio shows a negative relationship with GPR betas, providing some evidence that asset quality affects geopolitical risk sensitivity, though the effect is not statistically significant. The results run counter to the hypothesis that trading banks benefit from volatility: A bank at the 90th percentile of the trading assets share experiences a 3 basis point larger decline than one at the 10th percentile, suggesting that the risks associated with holding trading positions during geopolitical turmoil outweigh the potential fee income benefits, at least from the perspective of equity investors.

Internationalization matters, in terms of both the extent to which a bank operates abroad and the geographic locations of its foreign operations. A bank at the 90th percentile of the foreign claims share experiences a 2 basis point larger decline in response to a one-standard-deviation increase in the GPR index compared with a bank at the 10th percentile, although the difference is statistically significant at only the 10 percent significance level.

The effect is slightly more pronounced for BGPR, which captures not just whether a bank is internationally active but where it operates and whether those countries face heightened geopolitical risk: The differential between the 90th and 10th percentiles is 3 basis points. This result echoes findings by Niepmann and Shen (2025), who show that banks reduce lending and tighten credit standards when BGPR increases.<sup>5</sup> The stock market response documented here suggests that investors anticipate these operational consequences and price them into bank valuations. Relative to the baseline effect of a one-standard-deviation change in the GPR index on bank stock returns of about –10 basis points, a differential effect across banks of as much as 3 basis points appears notable.

Our findings shed light on financial stability risks in an era of elevated and evolving geopolitical tensions. With mounting geopolitical conflict, pressures on banks can build indirectly through weaker economic activity and rising inflation, higher loan losses, and volatility in financial markets as well as through direct exposure to conflict. As economic fragmentation progresses and supply chains realign, banks face differentiated exposures depending on whom they lend to and where they operate. At the same time, their balance sheet vulnerabilities differ. Banks with higher profits and more liquid assets appear better positioned to weather geopolitical risk shocks. The stock market responses for the largest U.S. banks documented here suggest that investors recognize these vulnerabilities and price them into bank valuations, highlighting how geopolitical risk affects financial institutions unevenly.

## Endnotes

1. Geopolitical risk shocks tend to be inflationary and can lead to tighter monetary policy. Banks can benefit from higher inflation through higher interest rates raising net interest income (Converse and Jain 2024). Therefore, in principle, geopolitical risk, through higher inflation and higher interest rates, could have a positive effect on bank valuations. In our analysis, we tested for this channel but did not find evidence of its relevance.
2. Following Converse and Jain (2024), we also investigated whether greater securities holdings or larger short-term deposit liabilities predict a larger negative effect of geopolitical risk on a bank's excess return because banks with these characteristics tend to benefit more from inflation, which geopolitical risk can increase. However, we did not find evidence for this channel.
3. For the set of smaller banks, we find that only the non-performing loans ratio consistently affects the sensitivity of bank stock prices to geopolitical risk—when the ratio rises, stock price sensitivity increases. The coefficient on the foreign asset share tends to be positive, but other bank characteristics do not robustly predict the stock price responses of smaller banks to geopolitical risk.
4. Figure 3 omits a panel showing the relationship between the GPR beta and the Tier1 capital ratio; our analysis finds no relationship between these two variables.

5. The predictive power of BGPR for bank stock prices is supported by local projection estimates that additionally shed light on the dynamics of the effects. The results of local projections of monthly bank stock returns on monthly BGPR with one lag and a six-month horizon are shown in Figure A2 in the appendix. The figure indicates that the effects of BGPR on stock prices occur immediately during the first month of a BGPR shock, with effects largely reversed by month 3. This result is in line with the findings by Dieckelmann et al. (2025).

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