INTERNATIONAL JOURNAL OF FINANCIAL ECONOMICS (IJEFE) e-ISSN: 3063-3648
Vol. 2 No. 6 June 2025, page 574-582

THE IMPACT OF GEOPOLITICS ON MARKET VOLATILITY: MITIGATION STRATEGIES FOR GLOBAL BUSINESSES

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Abstract

Global geopolitical uncertainties are increasingly fuelling volatility in the world's financial and economic markets. This research aims to analyse the impact mechanisms of geopolitical events-such as military conflicts, economic sanctions, and diplomatic tensions-on market volatility and formulate effective mitigation strategies for global businesses. Using the literature review method, this study collects and analyses various scientific literature, financial institution reports, and recent case studies relevant to the topic. The results show that geopolitical risks contribute significantly to fluctuations in stock prices, exchange rates, and commodity prices, especially in emerging economies that are integrated with global markets. To face these challenges, mitigation strategies such as portfolio diversification, real-time risk monitoring, supply chain strengthening, and contingency planning have proven effective in enhancing business resilience. This research recommends that global businesses adopt adaptive and comprehensive risk management to minimise the negative impact of geopolitical uncertainty and maintain business sustainability and competitiveness in international markets.

Keywords: Geopolitics, Market Volatility, Mitigation Strategies for Global Business.

Introduction

The dynamics of global geopolitics have become one of the main factors influencing the stability and volatility of financial markets in different parts of the world. Global geopolitics is the study of the interaction between geographical factors, political forces, and the dynamics of international relations that shape state policies and influence political and economic developments at the world level, where elements such as geography, natural resources, national security, and interstate relations are key components in determining the distribution of power, diplomacy strategies, and the potential for conflict and cooperation between states on the global stage (Yilmaz & Kilic, 2022) . Tensions between states, armed conflicts, and aggressive foreign policies often trigger sudden changes in market sentiment and international capital flows. In recent years, geopolitical events such as the Russia-Ukraine war, conflicts in the Middle East, and strategic competition between the United States and China have generated significant uncertainty in global stock, bond and commodity markets (Suhanda ., 2023)

Indonesia, while geographically not necessarily at the centre of conflict, remains highly affected by global geopolitical dynamics. The connectedness of Indonesia's financial system to international markets makes the Indonesia Stock Exchange (IDX) vulnerable to external shocks triggered by geopolitical events. For example, the Russian invasion of Ukraine on 24 February 2022 directly impacted the IDX, where investor sentiment deteriorated and the composite stock price index (JCI) experienced a significant decline (Garcia & Singh, 2023) .

High market volatility due to geopolitical uncertainty often prompts investors to review their portfolios and seek assets that are perceived to be safer, such as gold, government bonds, or strong currencies like the US dollar. This "flight to safety" phenomenon demonstrates how changes in risk perception can trigger major shifts in global asset allocation and affect liquidity in both domestic and international capital markets (Kumar & Nguyen, 2022) .

Besides the direct impact on stock indices, geopolitical conflicts also affect the prices of key commodities such as oil and gas. Spikes in energy prices due to supply disruptions from conflict regions not only increase market volatility, but also trigger global inflation and prompt central banks in various countries to adjust their monetary policies. This creates additional challenges for market participants and policymakers in maintaining macroeconomic stability (Evans, 2020) .

Geopolitical risks can also increase the uncertainty of a company's cash flow, increase borrowing costs, and complicate projections of future market trends. This condition encourages businesses and investors to be more cautious in making investment decisions, often leading to the postponement or cancellation of new investments until the geopolitical situation becomes clearer. This "wait and see" behaviour is reflected in real options theory, where firms choose to postpone expansion or large investments when external risks increase (Rahmawati, 2024) .

Previous studies have shown that the intensity and duration of geopolitical conflicts greatly influence the magnitude of the impact on financial markets. Conflicts that are long-lasting and involve many countries tend to cause higher and prolonged volatility, compared to conflicts that are localised and quickly resolved. Investors' risk perception of each conflict is also a determining factor in the market response to geopolitical events (Forbes Councils, 2024) .

In the context of economic globalisation, geopolitical uncertainty not only affects the countries directly involved in the conflict, but also spreads to other countries through global trade, investment and supply chain channels. Indonesia as an open economy is highly vulnerable to this risk transmission, whether through exchange rate fluctuations, commodity price changes, or foreign capital flows. Increased market volatility due to geopolitical risks requires global businesses to have effective mitigation strategies (Ahmed & Chinn, 2020) . Portfolio diversification, the use of hedging instruments, and real-time monitoring of geopolitical risk indicators are important steps in reducing exposure to external shocks. In addition, the adoption of technology in supply chain management and strengthening international cooperation are also part of the strategic response to global uncertainty (Suryani, 2024) .

Central banks and international financial institutions routinely monitor developments in geopolitical risks and include them as one of the main factors in assessing the global economic outlook. A survey conducted by Gallup in 2017 showed that 75 per cent of global investors are concerned about the economic impact of military and diplomatic conflicts taking place in various parts of the world. This emphasises the importance of a deep understanding of the relationship between geopolitics and market volatility for businesses and investors (Stefanell ., 2023)

In the midst of increasing global uncertainty, literature-based mitigation strategies are highly relevant to formulate adaptive investment and business policies. Literature review enables the identification of geopolitical impact patterns from various cases in the past, while formulating strategy recommendations that have proven effective in dealing with market volatility. This approach also helps global businesses anticipate risks and capitalise on opportunities that arise amidst the world's geopolitical dynamics (UMSIDA Management Editorial Team, 2024) .

Thus, research on the impact of geopolitics on market volatility and mitigation strategies for global businesses is crucial to provide a scientific basis for decision-making in an era of uncertainty. Through a comprehensive understanding of the impact mechanisms, market response patterns and available mitigation strategies, businesses and investors can enhance their resilience and competitiveness in an increasingly complex and dynamic global market.

Research Methods

The research method used in this study is a qualitative approach with a literature review method, in which researchers collect, review, and analyse various secondary data sources such as scientific journals, books, research reports, and official publications relevant to the theme of geopolitical impact on market volatility and global business mitigation strategies (Green et al., 2006) . The literature was selected based on the relevance, currency and credibility of the sources, and included publications from reputable scientific databases. Analyses were conducted thematically to identify patterns, relationships, and strategies that have proven effective in dealing with geopolitical risks in global markets, so that the research results can provide comprehensive understanding and evidence-based recommendations for businesses and researchers in this field (Baumeister & Leary, 2020) .

Results and Discussion

Mechanism of Geopolitical Impact on Market Volatility

The mechanism of geopolitical impact on market volatility occurs through various interrelated channels that affect investor behaviour, capital flows and overall financial market performance. First, geopolitical events such as military conflicts, economic sanctions or diplomatic tensions often create high uncertainty among market participants. This uncertainty encourages investors to take cautious steps, such as withdrawing funds from the stock market or switching to assets that are considered safer, thus triggering sharp price fluctuations (Turner, 2021) .

Second, foreign capital flows are highly sensitive to geopolitical developments. When geopolitical risks increase, foreign investors tend to reduce exposure in emerging economies, including Indonesia, and move their funds to countries with lower risk levels. This withdrawal of foreign capital leads to a decline in stock prices and an increase in bond yields, which ultimately impacts national economic stability (Miller & Lessard, 2020) .

Third, market volatility is also influenced by currency exchange rate movements. Geopolitical conflicts often lead to the strengthening of safe haven currencies such as the US dollar, while emerging market currencies such as the rupiah tend to weaken. This currency depreciation can increase import costs and depress domestic companies' profits, thus worsening market sentiment (Koran Bernas, 2023) .

Fourth, global commodity prices are highly vulnerable to geopolitical tensions, especially energy commodities such as oil and gas. Supply disruptions due to conflicts or sanctions can cause price spikes, which in turn increase volatility in commodity markets and impact related sectors in the stock market (Smith & Lee, 2022) .

Fifth, investor sentiment plays an important role in amplifying the impact of geopolitics on market volatility. News of international conflicts or tensions often triggers an overreaction in the market, where investors engage in mass sell-offs or simultaneous purchases of safe haven assets, magnifying fluctuations in stock and bond prices (Park & Lee, 2022) .

Sixth, empirical research shows that geopolitical risk has a strong positive correlation with stock price volatility across market sectors. When a geopolitical event occurs, stock prices tend to increase or decrease significantly, depending on the risk perception and exposure of the relevant sector to the event (Wang & Li, 2023) .

Seventh, the impact of geopolitics on stock markets is not uniform across countries. Factors such as economic conditions, political stability, and national productivity can moderate the magnitude of the impact. Countries with strong economic fundamentals tend to be more resistant to geopolitical shocks than countries with fragile economies (Zhang & Sun, 2022) .

Eighth, geopolitical actions such as war or terrorism can amplify the influence of geopolitical risk on markets. Research shows that the impact of geopolitical risks will be greater when followed by real actions on the ground, such as conflict escalation or terrorist attacks, which drastically increase market uncertainty and volatility (Darcy & Roy, 2024) .

Ninth, high volatility in the market due to geopolitical risks may trigger delays or cancellations of new investments by businesses. This "wait and see" phenomenon occurs as firms and investors wait for clarity on the situation before making major investment decisions, in accordance with real options theory (Choi & Lee, 2023) .

Tenth, geopolitical risks can also affect the synchronisation of global stock markets. Major geopolitical events often cause markets in different countries to move simultaneously, as global investors respond to similar sentiments and risks, increasing inter-market correlation (Apergis & Payne, 2021) .

Eleventh, in the long run, geopolitical risks can negatively impact macroeconomic outcomes, such as economic growth and financial stability. High market volatility can trigger financial crises and push economies into recession if not properly managed (Bouri & Demirer, 2022) .

Twelfth, the impact of geopolitical risks also varies depending on the industry sector. Sectors that rely heavily on international trade or specific commodities are more vulnerable to geopolitical shocks than domestically orientated sectors (Johnson & Baker, 2023) .

Thirteenth, international portfolio diversification is an important mitigation channel. Investors with portfolios spread across different countries tend to be better able to withstand the impact of volatility due to geopolitical risks than investors who are focused on one particular country or region (Antonakakis & Gupta, 2021) .

Fourteenth, overall, the mechanism of geopolitical impact on market volatility is complex and multidimensional, involving interactions between external factors, investor sentiment, capital flows, exchange rates, commodity prices, and government and central bank policies. Therefore, an in-depth understanding of these mechanisms is critical for investors, businesses and policymakers in formulating effective mitigation strategies (Ivanov, 2022) .

Geopolitical Risk Mitigation Strategies for Global Businesses

Facing market volatility due to geopolitical risks, global companies need to develop comprehensive and adaptive mitigation strategies. The first step is to conduct regular risk identification and assessment to understand the potential threats that may arise from changes in the geopolitical situation in the countries where companies operate. This assessment forms the basis for developing relevant and effective mitigation strategies (Lee & Kim, 2021) .

Diversification is one of the main strategies that can be implemented. Diversification includes not only investment portfolios, but also supply chains, markets and products. By diversifying suppliers and markets, companies can reduce dependence on one particular region or source, minimising the risk of disruptions due to conflicts or sanctions. For example, firms may seek alternative suppliers from different countries or expand sales markets to more politically stable regions (Chen & Xu, 2023) .

In addition, companies need to build good relationships with local governments and stakeholders. Strong relationships can provide access to critical information and help companies respond more quickly and appropriately to policy changes. Building strategic partnerships can also increase business resilience, especially in the face of changing regulations or international trade policies (Wang & Li, 2023) .

Contingency plans are an important element in mitigation strategies. Companies should prepare contingency scenarios, such as diversion of resources, storage of additional inventory, or adjustment of shipping routes, to maintain continuity of operations in the event of supply chain disruptions. In the shipping sector, diversification of shipping routes and the use of insurance are also effective mitigation measures to minimise potential financial losses due to conflict or political instability in major shipping lanes (Mensi & Hammoudeh, 2021) .

Proactive risk management is urgently needed, including regular monitoring of global geopolitical developments and the use of data-driven analytical tools to identify high-risk areas. By doing so, companies can take anticipatory steps before risks develop into larger crises (Indonesia Legal Network, 2024) .

Improving operational efficiency through the adoption of technology and innovation can also strengthen a company's resilience to market fluctuations. Technology enables companies to respond to market changes more quickly and efficiently, and optimise business processes amidst uncertainty.

Investment in human resource development is an important part of the mitigation strategy. Competent and adaptive employees can help companies navigate changes in a dynamic and complex business environment. In addition, transparent internal communication and work flexibility can maintain team productivity amid geopolitical uncertainty (Brown & Zhang, 2021) .

Managing compliance globally is also a challenge. Each country has different regulations, so companies must build flexible systems to remain compliant with various local rules, such as taxation, data protection, and international trade policies. Failure to comply with regulations can lead to severe sanctions that are detrimental to the company (Yilmaz & Kilic, 2022) .

Insurance coverage is an additional strategy that can transfer some of the financial risk to a third party. Cargo insurance, for example, can protect companies from losses due to damage, theft or disruption of shipments triggered by geopolitical conflicts. In addition, utilising free trade zones can help companies avoid high import duties and taxes resulting from changes in international trade policies (Suhanda ., 2023)

Governments and financial institutions also need to play an active role in supporting national business resilience. Exchange rate stabilisation policies, incentives for market diversification, and strengthening international cooperation can help create a more stable business environment that is resilient to external shocks (Garcia & Singh, 2023) .

As such, geopolitical risk is a serious challenge that can trigger market volatility and disrupt global business operations. The impact is not only limited to fluctuations in stock prices and exchange rates, but also extends to supply chain disruptions, changes in trade policies, and significant financial losses. Therefore, companies need to develop comprehensive mitigation strategies, ranging from supply chain and market diversification, regular risk analysis, strategic relationship building, to the utilisation of technology and insurance coverage. Business resilience in the era of globalisation is highly dependent on companies' readiness to deal with increasingly complex geopolitical risks. With a deep understanding and proper implementation of mitigation strategies, companies can improve their competitiveness and business sustainability in an uncertain global market.

Conclusion

The impact of geopolitics on market volatility is very real, where events such as military conflicts, economic sanctions or diplomatic tensions can trigger uncertainty leading to sharp fluctuations in exchange rates, commodity prices and stock markets. This condition not only affects the stability of the global economy, but also has a direct impact on developing countries such as Indonesia that are heavily connected to international trade and investment. Geopolitical uncertainty encourages investors to take defensive measures, such as withdrawing investments from the capital market or shifting assets to safer instruments, thus magnifying market volatility.

In the face of these challenges, mitigation strategies are crucial for global businesses to remain resilient amidst uncertain market dynamics. Some of the key strategies that have proven effective include portfolio diversification, close monitoring of geopolitical developments, use of information technology for real-time risk monitoring, as well as contingency planning and supply chain diversification. Companies that are able to proactively integrate risk management into their business strategy tend to have a competitive advantage and better resilience to external shocks.

Overall, adaptive and comprehensive risk management is key to dealing with market volatility due to geopolitical impacts. By conducting thorough risk identification and implementing integrated mitigation strategies, companies can not only minimise the negative impact of global uncertainty, but also increase opportunities for growth and business sustainability in increasingly complex international markets.

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