



Middle East Conflict 2026

Economic Transmission Channels and
Implications for Sri Lanka

Senfin Research

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SECURITIES

Escalation, energy risk & Sri Lanka's economic exposure...

- The Middle East conflict has shifted from “**regional instability**” to “**global energy & shipping risk**” due to the Iran-focused escalation and threats/disruption around the **Strait of Hormuz**, a critical chokepoint for oil and LNG flows.

- Sri Lanka's highest vulnerabilities are:

1. **Energy import bill & inflation pass-through (oil, freight, insurance).**
2. **Worker safety + remittance continuity (over 1.0 mn Sri Lankans in the region).**
3. **Supply chain/shipping disruptions affecting costs and lead times (Hormuz + potential spillover risks toward Red Sea).**



- Market impact for Sri Lanka is likely to be risk-off in the short term, with sector rotations: pressure on **tourism/transport**, **margin pressure for manufacturing**, and **relative defensiveness in banks/quality exporters (depending on FX and rates)**.

Strait of Hormuz

Connects oil and LNG production in the Middle East to global markets via the Arabian Sea and the Indian Ocean

Volume transported through the strait in 2024
(daily average)

Oil and petroleum products

20.3 MILLION barrels

LNG

290 MILLION cubic meters

Shipments through the Strait of Hormuz

30%

of global seaborne oil trade

20%

of global LNG trade

Saudi Arabia is the largest exporter of oil through the strait, while Qatar leads in LNG exports

Strait of Hormuz

80% of LNG passing through the strait goes to Asia, 20% to Europe

to Europe

to Asia

Joint U.S.-Israeli military strikes on Iran...

- On 28 February 2026, the USA and Israel launched coordinated airstrikes on Iran, targeting senior leadership and key military infrastructure, significantly escalating regional conflict.
- Israeli officials reported that Iran's Supreme Leader Ayatollah Ali Khamenei was killed in the operation, a development with major geopolitical implications.
- Israel described this as a pre-emptive attack aimed at neutralizing perceived existential threats from Iran's nuclear and missile program.

These strikes have transformed long-standing tensions into a broader conflict, raising uncertainty across global energy and financial markets.

Disruption to regional airspace and transport links...

- Following the initial strikes, Israel declared it launched additional waves of attacks against Iran, with U.S. support expected to intensify response capabilities further. U.S. leadership warned of strong retaliation if Iran hits back, underscoring the potential for sustained military engagement.

Persistent escalation increases the risk premium on commodities (especially oil), insurance, and shipping, and deters investment and travel within and beyond the region.

- Several countries, including Iran, Israel, Iraq, Kuwait, Qatar, and the UAE, closed or restricted airspace due to military operations, causing mass flight cancellations, rerouting, and cargo delays. Russia, for safety reasons, also suspended flights to and from Iran and Israel, rerouting aircraft around the conflict zone.

Airspace closures add to global transport costs, reduce tourism flows, and disrupt time-sensitive trade reinforcing inflation pressures and weakening passenger confidence.

Market reactions and commodity price pressures...

- Oil markets have already priced in heightened risk. Brent crude and other benchmarks rose amid the conflict, with analysts warning prices could climb sharply if disruptions continue. Some majors have suspended shipments via the Strait of Hormuz, and freight rate spikes reflect growing concern over safe navigation in the Gulf.

The Middle East accounts for ~20% of global oil trade via the Strait of Hormuz; supply uncertainty could lift global fuel and input costs, affecting inflation globally and for oil-importing countries like Sri Lanka.

88.154

44.186

46.681

Mixed global political reactions heighten uncertainty...

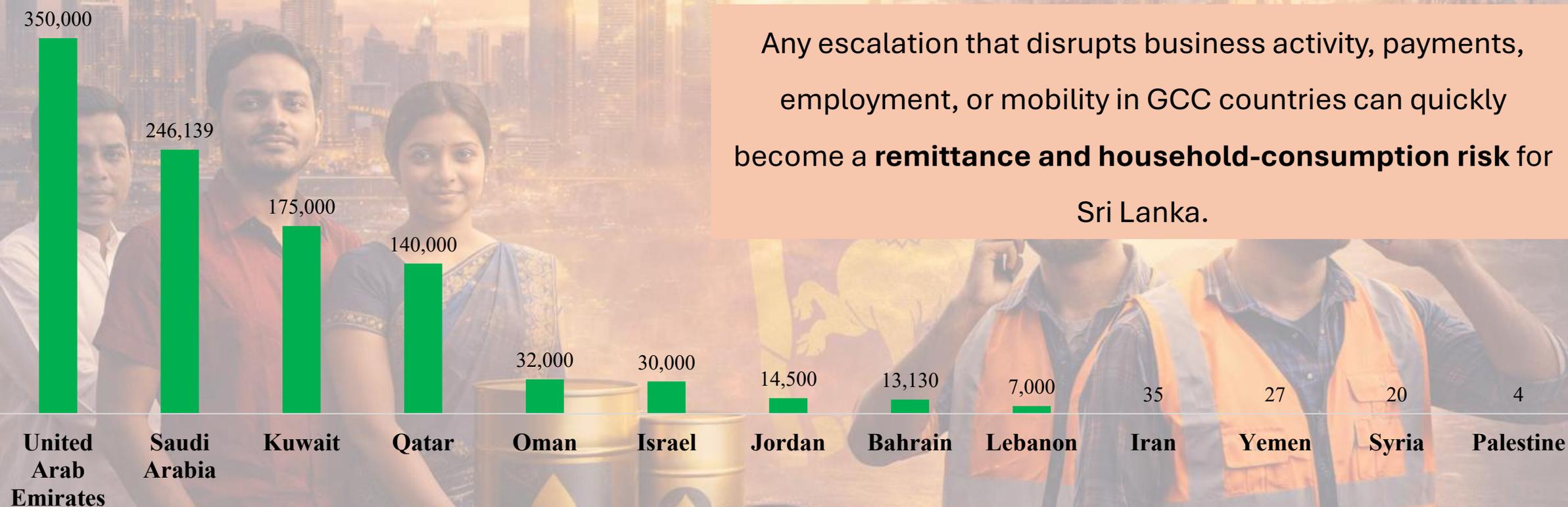
- International responses have been divided. The UN called for cessation of hostilities, while some nations condemned the strikes as destabilizing. Pressure is mounting on diplomatic channels even as military actions continue, creating policy unpredictability in economic decision-making.

Divergent global political stances complicate market expectations, potentially leading to increased volatility in currencies, risk assets, and investment flows.

Sri Lankan presence in the Middle East...

- Government-linked figures (as of 28 Feb 2026) indicate 1,007,855 Sri Lankan nationals across 14 Middle Eastern countries.

Estimated Sri Lankans in Middle Eastern Countries



Any escalation that disrupts business activity, payments, employment, or mobility in GCC countries can quickly become a **remittance and household-consumption risk** for Sri Lanka.

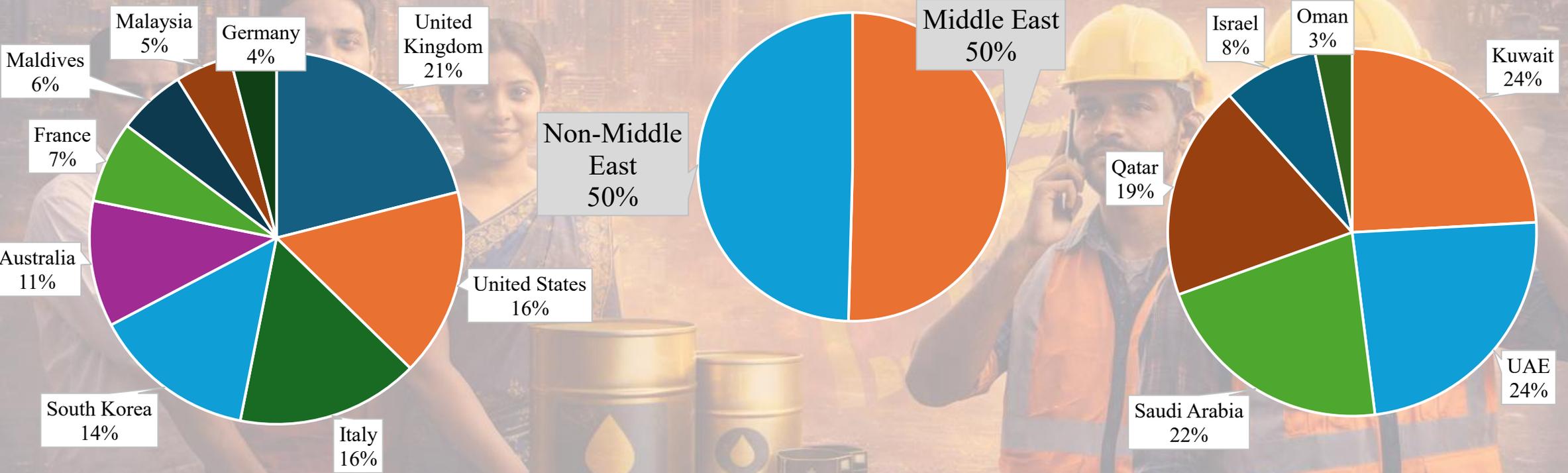
Woker remittances from Middles East...

- Roughly half of Sri Lanka's remittance inflows from these major corridors originate from the Middle East. The Gulf alone (Kuwait, UAE, Saudi, Qatar) accounts for over USD 3.07 billion, highlighting structural dependence.

Remittance Income from Non Middle East :
USD 3,421.7 Mn in 2025

Middle East vs Non-Middle East

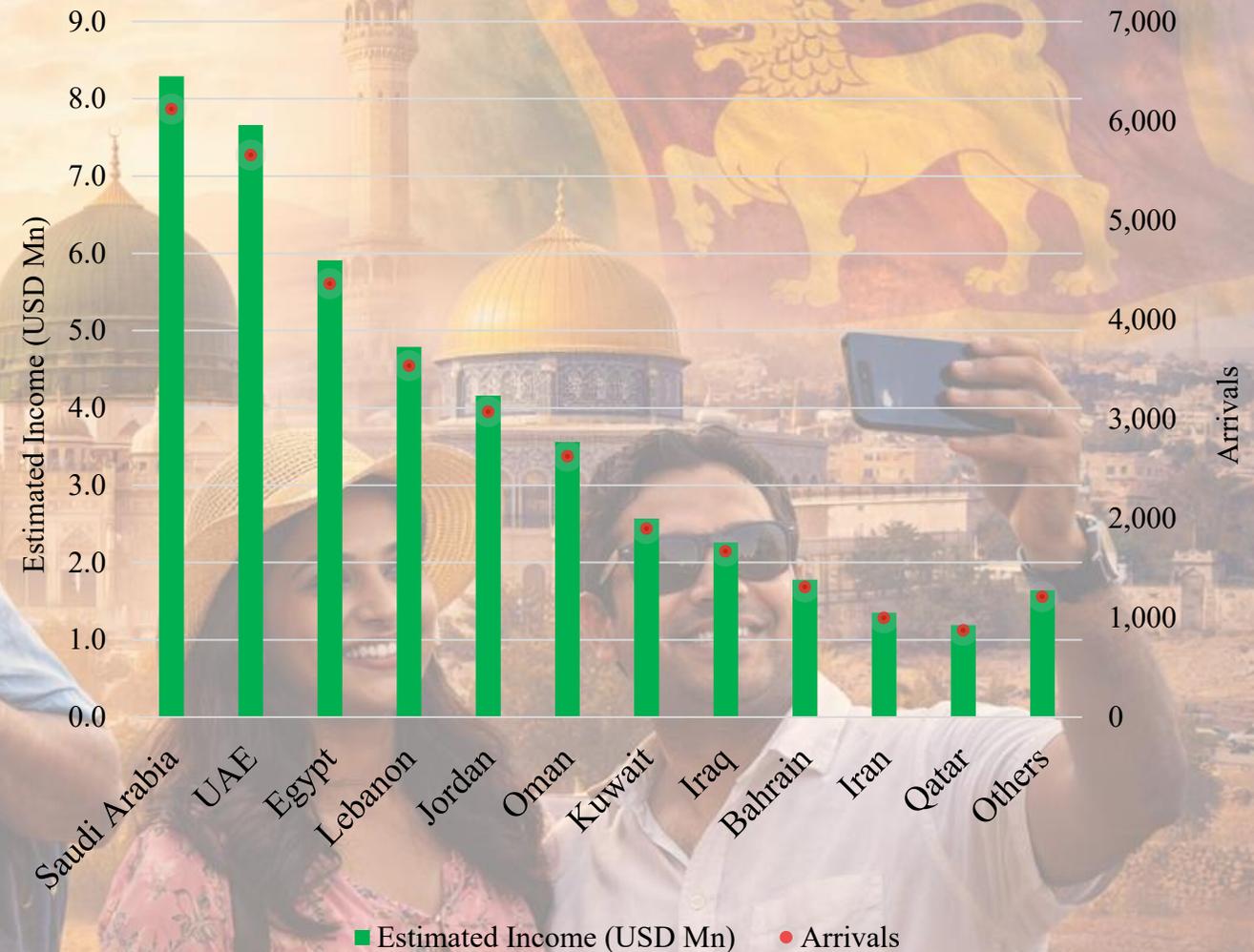
Remittance Income from Middle East :
USD 3,480.4 Mn in 2025



Tourism exposure...

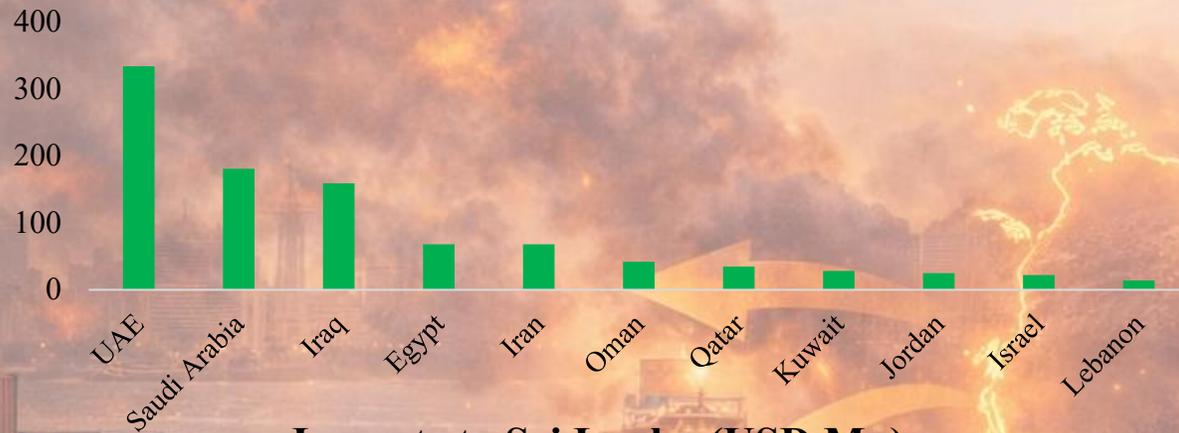
- Sri Lanka's Middle East arrivals are relatively small as a share of total arrivals, but still meaningful for diversification and transit connectivity.
 - **Total arrivals from Middle East (Jan–Dec 2025): 32,338**
 - **Total Sri Lanka tourist arrivals (Jan–Dec 2025): 2,362,521**
 - **Middle East share $\approx 1.37\%$**
- Sri Lanka's tourism generated about USD 3.2 bn in 2025. If we pro-rate earnings by arrival share (a simplifying assumption), Middle East-linked receipts are roughly: **~USD 44 mn ($\approx 1.37\% \times \text{USD } 3.2 \text{ bn}$)**
- Dubai/Doha are key hubs. Any disruption increases costs and reduces seat capacity, impacting inbound tourism and outbound travel costs.

Estimated Tourism Income from Middle East (USD Mn)



Trade exposure: imports, exports, and key dependencies...

Exports from Sri Lanka (USD Mn)



Imports to Sri Lanka (USD Mn)



UAE trade

- Exports to UAE: USD 334.63 mn
- Imports from UAE: USD 1,291.03 mn

UAE is among Sri Lanka's major import origins and an important export destination.

Iran Trade

- Sri Lanka exported goods worth USD 67.81 mn to Iran in 2024. Tea is the dominant export (~USD 62.25 million). Other export products include textile fibers, aluminum, edible fruits and machinery parts.
- Sri Lanka's imports from Iran were USD 2.44 million in 2024. Major import categories included plastics, fertilizers, pharmaceuticals, fruits, fish, and vegetables.

Saudi trade

- Sri Lanka's Foreign Ministry stated Sri Lankan exports to Saudi Arabia recorded a 19% increase in 2025 (and highlighted ongoing imports of essential commodities/energy supplies from the Kingdom).

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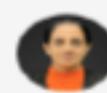


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