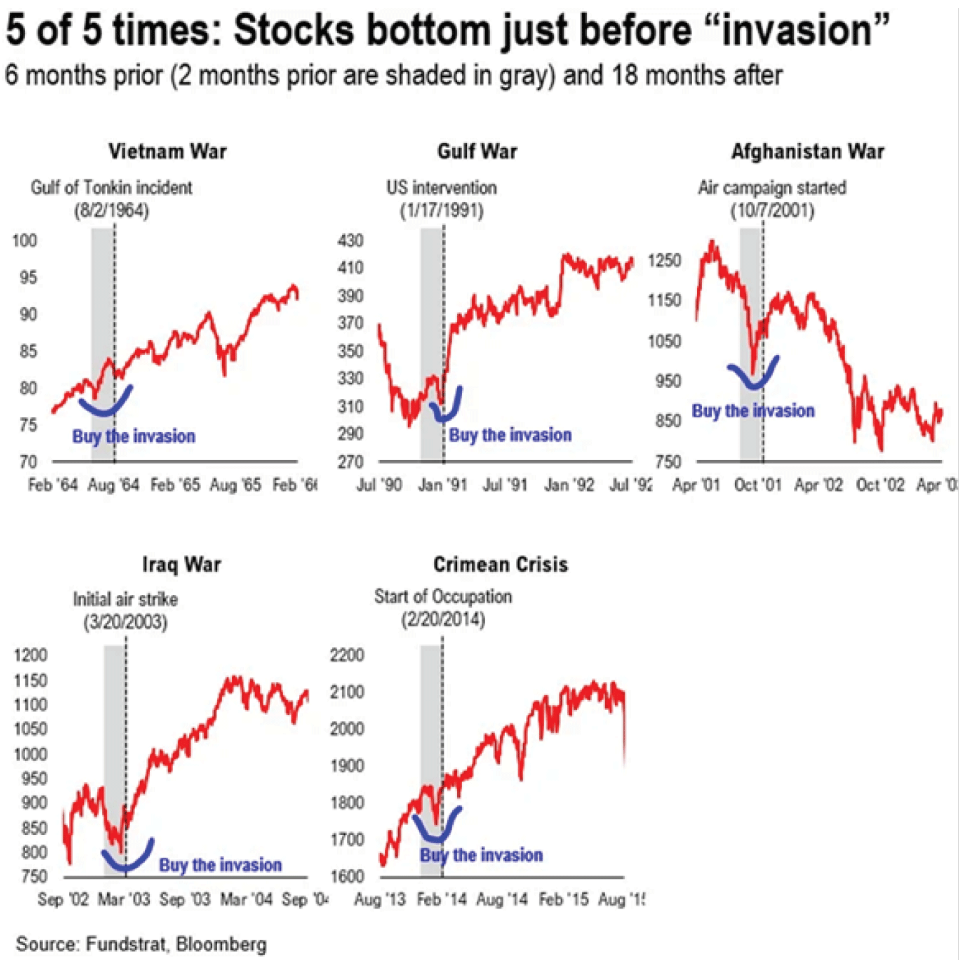
FLASH COMMENTARY
February 22, 2022

Too Early to Be 'Russian' for the Exits?

As of this writing, the likelihood of some form of Russian invasion or incursion into Ukraine has increased significantly, or may have actually already occurred. Russia's President Vladimir Putin signed a decree yesterday officially recognizing two eastern Ukranian territories in the Donbas region, the so-called Donetsk and Luhansk People's Republics as independent states. Putin has pledged "peacekeeping forces" to guarantee the security of these regions as Russia's Federation Council has formally granted Putin the power to deploy forces outside the country's borders. Pro-Russian separatists in these regions declared independence from Ukraine in 2014.

In an effort to contextualize how markets anticipate and react to geo-political tension, Fundstrat has analyzed five separate events below. The vertical lines represent the commencement of hostilities, with the 6-months preceding invasions to the left of the vertical dashed line and the 18 months after the invasion represented to the right of the line. Clearly, the angst felt leading up to the events generally over-exaggerate worst-case scenarios and represented potential buying opportunities.



When the economy is already in or entering a recession, geo-political shocks can exacerbate problems; however, if recessionary conditions are not present, the table below suggests that market declines tend to be short-lived and relatively shallow.

Stocks Usually Take Geopolitical Events In Stride

S&P 500 Index And Geopolitical Events

		S&P 500 Returns		Days	
Market Shock Events	Event Date	One Day	Total Drawdown	Bottom	Recovery
U.S. Pulls Out of Afghanistan	8/30/2021	0.4%	-0.1%	1	3
Iranian General Killed In Airstrike	1/3/2020	-0.7%	-0.7%	1	5
Saudi Aramco Drone Strike	9/14/2019	-0.3%	-4.0%	19	41
North Korea Missile Crisis	7/28/2017	-0.1%	-1.5%	14	36
Bombing of Syria	4/7/2017	-0.1%	-1.2%	7	18
Boston Marathon Bombing	4/15/2013	-2.3%	-3.0%	4	15
London Subway Bombing	7/5/2005	0.9%	0.0%	1	4
Madrid Bombing	3/11/2004	-1.5%	-2.9%	14	20
U.S. Terrorist Attacks	9/11/2001	-4.9%	-11.6%	11	31
Iraq's Invasion of Kuwait	8/2/1990	-1.1%	-16.9%	71	189
Reagan Shooting	3/30/1981	-0.3%	-0.3%	1	2
Yom Kippur War	10/6/1973	0.3%	-0.6%	5	6
Munich Olympics	9/5/1972	-0.3%	-4.3%	42	57
Tet Offensive	1/30/1968	-0.5%	-6.0%	36	65
Six-Day War	6/5/1967	-1.5%	-1.5%	1	2
Gulf of Tonkin Incident	8/2/1964	-0.2%	-2.2%	25	41
Kennedy Assassination	11/22/1963	-2.8%	-2.8%	1	1
Cuban Missile Crisis	10/16/1962	-0.3%	-6.6%	8	18
Suez Crisis	10/29/1956	0.3%	-1.5%	3	4
Hungarian Uprising	10/23/1956	-0.2%	-0.8%	3	4
N. Korean Invades S. Korea	6/25/1950	-5.4%	-12.9%	23	82
Pearl Harbor Attack	12/7/1941	-3.8%	-19.8%	143	307
Average		**-1.1%**	**-4.6%**	**19.7**	**43.2**

Source: LPL Research, S&P Dow Jones Indices, CFRA, 01/24/2021

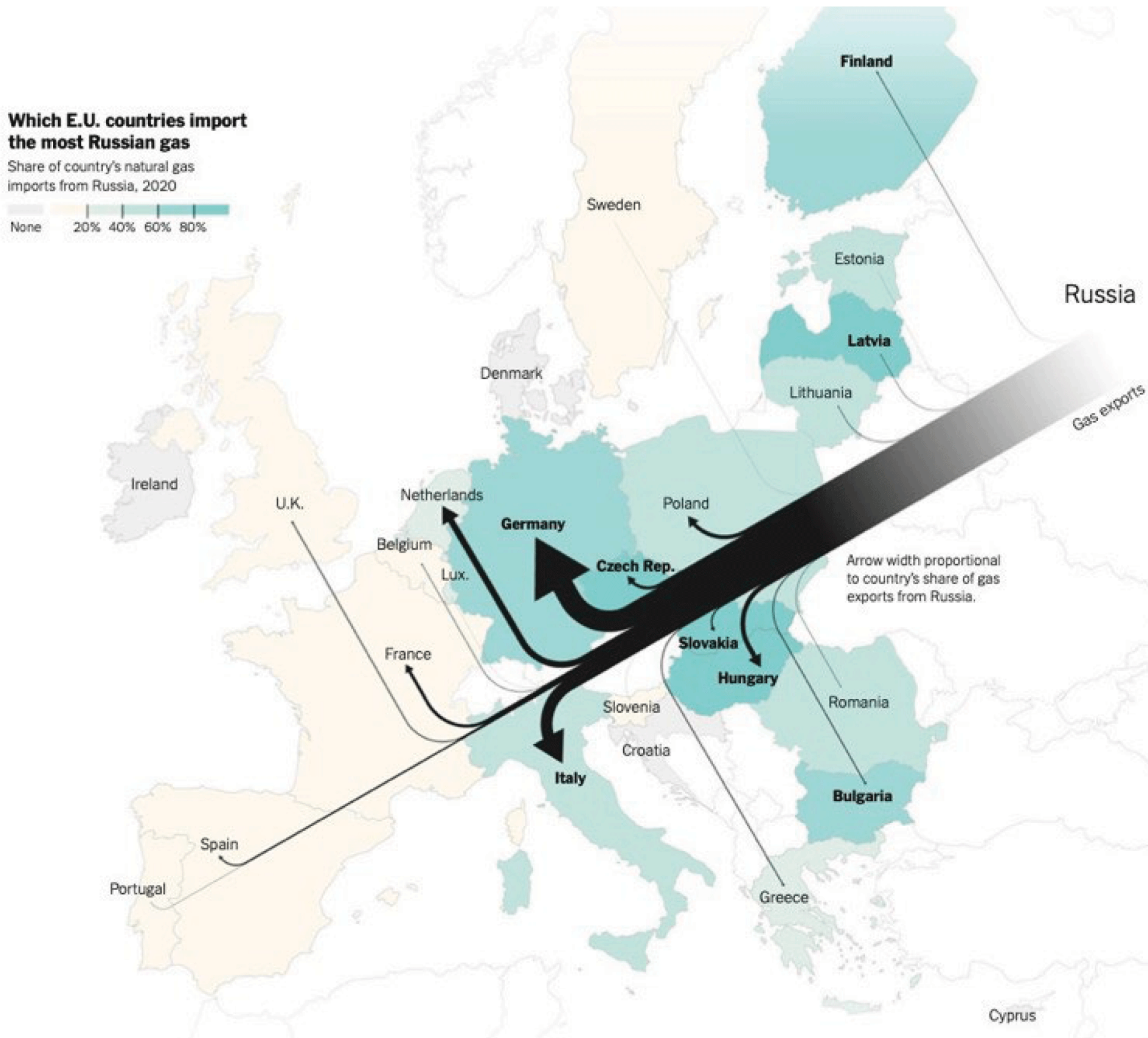
All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.

The modern design of the S&P 500 Index was first launched in 1957. Performance before then incorporates the performance of its predecessor index, the S&P 90.

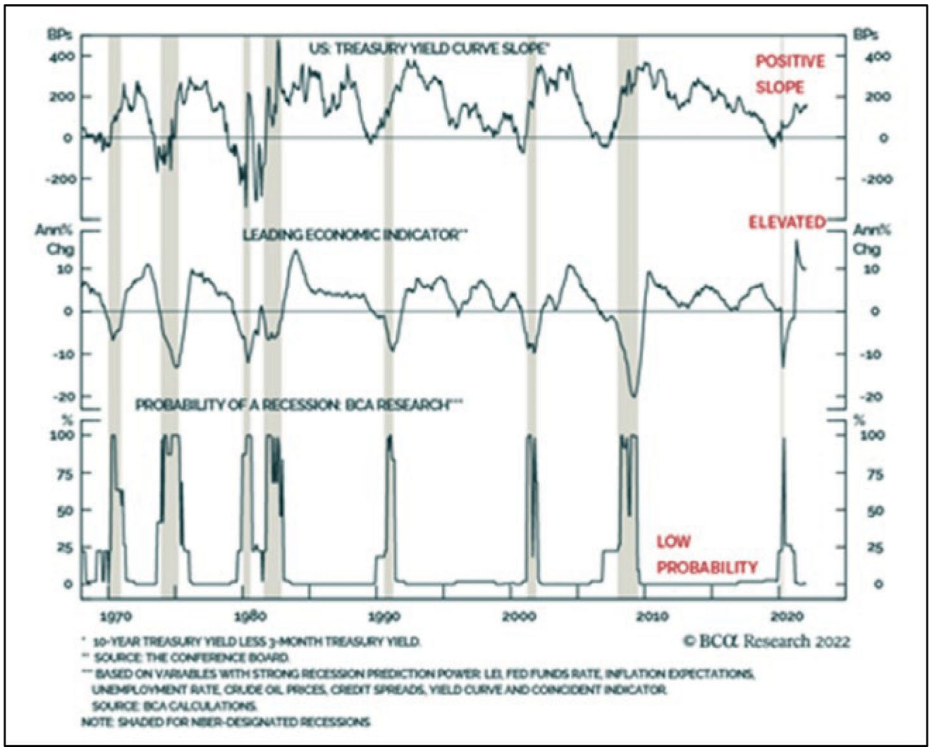
Below are some important facts that Strategas has tabulated regarding Russia's economic position:

- Russia is the world's 3rd largest producer of oil and 2nd largest producer of natural gas;
- 1/3 of European natural gas consumption and more than 1/4 of its crude oil imports are from Russia;
- Germany derives 30% of its crude oil supplies and 50%+ of its natural gas from Russia;
- Russia's major export partners:
  - EU & UK: 45.8%
  - China: 9.8%
  - Belarus: 4.9%
  - Turkey: 4.8%
- Russia's major import partners:
  - EU & UK: 38.2%
  - China: 20.9%
  - U.S.: 6.1%
  - Belarus: 5.2%

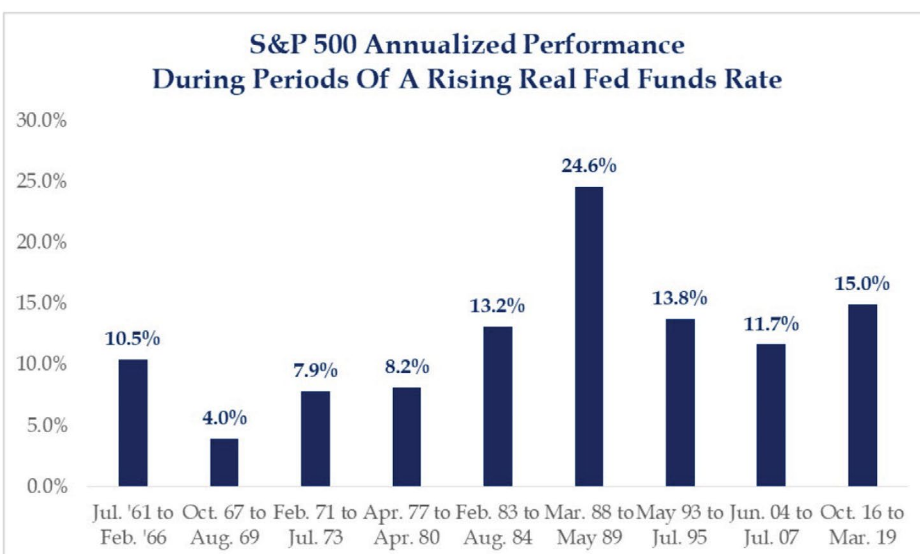
A whole-scale land war in Europe is clearly not in anyone's best economic interest. However, the scope and scale of Russian aggression remains to be seen. Russian motives could have a very short-term focus on minor territorial gains or this potentially represents the beginning of a more significant conflict. The numerous geo-political strategists that we track have varied interpretations of recent events, thus we have no particularly unique insights into how the situation will play out. The possibility does exist that Putin is not posturing and as the impact of sanctions and Western responses escalates, Putin may then feel he has a pretext to expand the Russian presence in Ukraine. German Chancellor Olaf Scholz recently said that the Nord Stream 2 pipeline intended to provide Russian oil and gas to Europe "cannot go online" with Russian troops in eastern Ukraine and that Germany is assessing other ways to secure its energy needs. As seen below, Germany has been a significant consumer of Russian gas exports historically. Its willingness to contemplate other sources of energy is not a trivial decision.



When the weight of the evidence is examined, from a fundamental perspective, the likelihood of an economic recession occurring soon is relatively low.



When it comes to headlines affecting prevailing market conditions, the actions of the Federal Reserve pertaining to both rate hikes and balance sheet management are likely to impact market sentiment and direction. The FOMC will convene in several weeks in mid-March. Regardless of how the situation unfolds in Ukraine in the interim, the Fed's stance has the potential to move markets meaningfully. With both nominal and real interest rates at historic lows, the beginning of a tightening cycle does not necessarily portend malaise for the markets. Historically, rising interest rates can coexist with positive stock market returns (rising rates are typically a reaction to healthy economic growth).



Conclusion

The situation in Russia and Ukraine remains fluid and is dominating the news cycle currently. The risks are unknown as the situation can take many potential turns. As a reminder, the public equity markets hit all-time high levels in early January. Stocks have since fallen as Fed officials have adopted a more hawkish tone as the threat of inflation looms large. After a prolonged period of loose monetary policy, the shift to a more restrictive regime raises many questions regarding the prospects for holding risk assets. While we continue to monitor developments with both Ukraine and the Federal Reserve, we advise clients not to make hasty, knee-jerk reactions with their investment programs. We will continue to remain diligent and facts-focused before meaningfully altering strategic investment allocations. When the broad economic landscape is surveyed from a perspective that considers "the forest, rather than the trees" we remain constructive on risk assets and feel that economic growth is likely to continue to provide opportunities for diversified portfolios to out-perform traditional 'safe-haven' assets that can rise abruptly on occasion when fear dominates short-term market psychology. We close this brief with a thoughtful quote from Sir John Templeton:

"The four most expensive words in the English language are 'This time it's different.'"

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