OUR TAKE ON THE IMPACT OF THE RUSSIA-UKRAINE CONFLICT

22 February 2022

The military tensions on the Russia-Ukraine border continue to take center stage, increasing market volatility. These tensions have been rising since the Russian annexation of Crimea and the breakaway of two separatist Russian-speaking enclaves from Ukraine in 2014. Russia provides almost 10% of the world's energy and supplies 35% of European natural gas consumption. Russia and Ukraine are major wheat, corn, vegetable oil, and fertilizers exporters.

Depending on the extent of the military actions and the severity of the western alliance sanctions, the impact on the energy markets may be substantial as major energy pipelines flow through the region. However, if you are looking for opportunities in other regions, oil drillers in North America could be an area to invest in during this tenuous time.

Another area of potential risk and opportunity lies in the agricultural markets. A conflict could put pressure on the supply chain and push prices higher. Once again, opportunities in the agriculture sector outside of the region could benefit from these higher commodity prices. Furthermore, any disruption in the supply of these commodities is likely to increase the already high global inflation and, consequently, central bank policies.

We have no exposure to any Russian or Ukrainian entities at this time. However, like everyone else in the market, we own some large-cap multinational companies in our portfolios that these developments may impact.

As far as the equity market is concerned, it may be helpful to take a historical perspective and look at previous geopolitical tensions and their lasting impacts. Looking at major geopolitical surprises in the last 80 years, from the Pearl Harbor attack to the Cuban missile crisis, the oil embargo, Iraq invasion of Kuwait, and the drone strike killing the Iranian Chief of staff in 2020, the S&P 500 recovered and was higher 83% of the time by a median of 14%, 12-months later. Although, past performance is no guarantee of future results.

Therefore, history shows it is risky to exit stocks altogether due to a geopolitical event as they usually result in significant knee-jerk selling, followed by a steady recovery.

As the world grapples with the uncertainties of a major war in the heart of Europe, it is essential to realize that we will be facing more volatile markets ahead. However, if history is any guide, the long-term impact on markets should be manageable.

Dr. Fall Ainina, PhD, CFA   Trent Dysert, CFA   Moustapha Mounah, CFA, ERP
