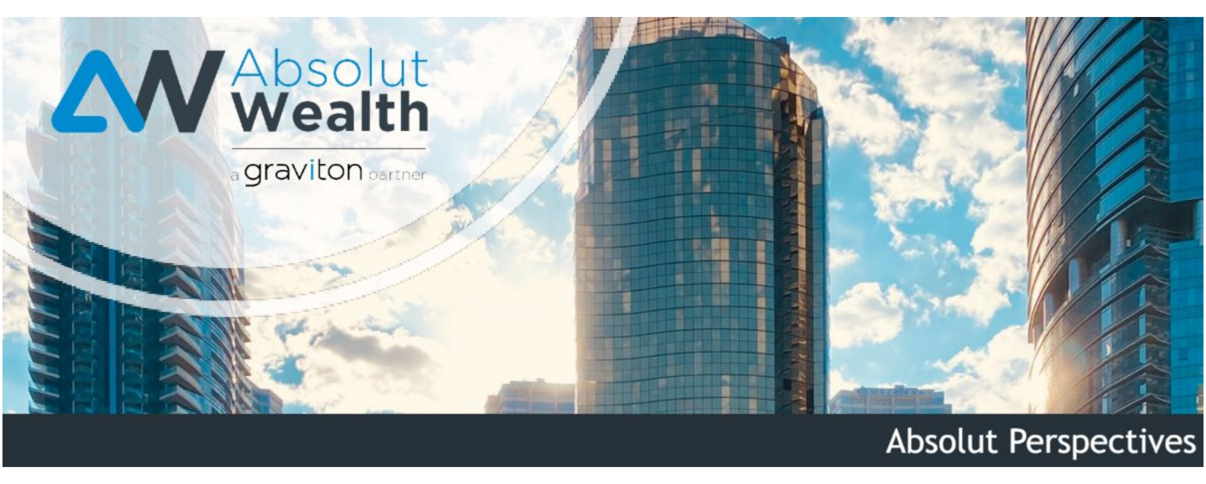


The Art of War

Richard Harris | Feb 2022

On the morning of the 24th February, we awoke to the announcement that Putin's Russia had launched a large-scale military invasion on Ukraine. Several officials and analysts have called the invasion the largest conventional military attack in Europe since WW2.

To most, this came as a surprise, as they assumed that Putin would never act on the threats he had been voicing for quite some time. However, if we take a look at some of the signs over the past few months, it is less unbelievable that the world now finds itself in this new conundrum (just as we are seeing signs of the COVID pandemic abating).

It was widely reported that Russia had amassed almost 200,000 troops in the build-up to the 24th, as Russian President, Vladimir Putin, repeated his distaste toward Ukraine's intentional allegiance to NATO, especially given his aggression to the demise of the USSR and belief that Russia still has claim to former Soviet Republics.

NATO (the **N**orth **A**tlantic **T**reaty **O**rganisation) is a military alliance between 28 European and 2 North American countries dedicated to preserving peace and security in the North Atlantic Sea. Russia, in general, considers NATO's expansion as a major concern and a threat to their national security, especially when allegiances are being created with former Soviet countries, like Ukraine, that border Russia.

What we are witnessing now is a full-blown war to the North with daily headlines giving further insights into the intricacies, as the world sits and watches, praying that the word "nuclear" stays far away from any headlines. Russia has the largest nuclear arsenal globally, seconded by the US.

Since the invasion, global leaders of political parties, businesses, and rating agencies have been clear on their views. Sanctions have been imposed on Russia, businesses have cut ties and many other measures have been taken to try and cripple Russia as a whole and put an end to this without a physical / weaponry war that could lead to more severe global outcomes. Even the assets of Russia Oligarchs have been confiscated or frozen in an attempt to push other Russian powers to find a peaceful resolution.

Despite many headlines over the past 10 days, no-one can confidently say they know the outcome to what is happening in Russia or Ukraine. News stations have often reported before fact-checking themselves and it is important to verify information as it is received. Based on the nature of Vladimir Putin and his beliefs, we can be assured that he will fight tooth and nail to get his views across (no matter how senseless they may be) and that we are likely in for a bumpy next few weeks and months, as this situation unfolds.

The Response from Global Markets

Russian Exchanges halved on the news of the invasion, as investors fled uncertainty and took a stand against this crime against humanity. They were halted last week in an attempt to stop the selling and have yet to re-open. On the other hand, the price of already-inflated commodities skyrocketed, especially those in which Russia and Ukraine are abundant.

To best analyse this, let's take a look at some of the inner fundamentals of Russia and Ukraine, and the global effects with these 2 nations at war:

RUSSIA

o Estimated to have over 30% of the world's natural resources.
o Has widely been described as an energy superpower.

- Largest global natural gas reserves (provides Europe with 30% of its natural gas)
- Second largest coal reserves
- Second largest oil exporter and producer

o Is the largest global exporter of wheat.
o Russian Foreign Exchange reserves are the 5th largest in the world.
o World's second largest exporter of arms.
o Has the 5th largest number of Billionaires.

UKRAINE

o Possesses the world's largest reserves of commercial iron ore (c.1/5th of the global total).
o Ranks second in terms of known natural gas reserves in Europe.
o Is a massive global agricultural player due to the quality of its soil and flat geography.

- Largest exporter of seed oils like sunflower and rapeseed
- 5th largest exporter of wheat

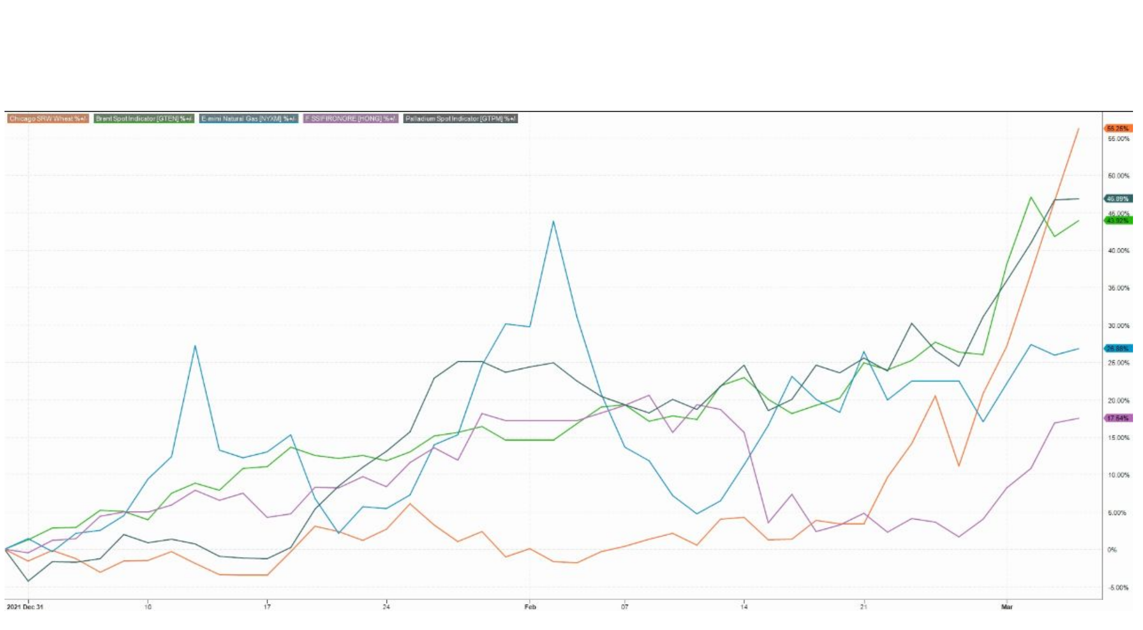
o Chemicals, coal, aircraft, and ship building are also important sectors of the Ukrainian economy.

After reading the above, it should be of no surprise that the War being fought above will have significant impacts on the global economy and prices of both soft and hard commodities. The longer it continues, the more supply chains will be affected and the greater the effect on prices globally, especially Oil, which is the common pricing commodity to all others, as it is a major input cost to almost all production.

Something else that cannot be neglected is that Russia is a large importer of many consumable goods. For example, Russia is the 4th largest importer of citrus. The knock-on effects of this reduction in demand could have serious effects on many agricultural industries that now need to find new demand for their products (that have a shelf life).

All we can hope for is that a peaceful resolution takes place and that damage to Ukraine and its citizens is limited as best possible.

The Chart below shows the prices of 5 commodities year-to-date: **(1) Wheat +56%**; **(2) Palladium +47%**; **(3) Brent Oil +44%**; **(4) Natural Gas +27%**; and **(5) Iron Ore +18%**



Market Review

We continue to see volatility in stock markets across the Globe as investors adjust their portfolios in preparation for the abovementioned headwinds. Continued tensions with Russia and their invasion of Ukraine have also added to market woes and is something that should be watched closely in the months ahead.

The largest gainers of the month were Gold, Energy, and commodities, up between 6 and 8%, and on the other end of the stick, Automotives, Technology, and Consumer Discretionary lost 8%, 5%, and 4%, respectively.

On the commodity front, Oil remained strong as geopolitical tensions and supply shortages remained a hot topic. Base metals also held strong with Palladium, Silver, and Aluminium all up between 9% and 11%.

The South African Rand and other Emerging Market currencies remained resilient as global funds shifted from expensive Developed Markets to better-valued Emerging Markets. The South African Rand also benefitted from continued strength of commodity prices, as mentioned above, but weakened in the last few days due to geopolitical tensions and investors fleeing to the US Dollar as a safe haven.

Despite recent moves, our market outlook, both locally and offshore, remains cautious as we continue to monitor ongoing global developments and commentary from Central Banks. We are defensively positioned with maximum offshore exposure and relatively high levels of cash and defensive allocations among our portfolios, which we look to deploy into higher return (alpha) generating investments that offer adequate risk-adjusted returns at favourable entry points in the near future.

Chart of the Month:

The Chart below shows the iShares MSCI Russia Exchange Traded Fund (ETF), which broadly tracks the Russian Stock Market. Following the announcement of its invasion of Ukraine, the Index sold off more than 50% in a matter of days as the world imposed sanctions and financial restrictions.

Trading on major Russian Exchanges was halted last week as a result, in order to limit further losses as investors fled.

"I know not with what weapons World War III will be fought, but World War IV will be fought with sticks and stones." - Albert Einstein