The Impact of the Crisis in Ukraine on the Markets and Client Portfolios

(February 22, 2022)

The situation in Ukraine, which has already created volatility in the financial markets, rose to a higher level of geopolitical risk on Monday.

Russia's President, Vladimir Putin, formally recognized the separatist regions of Donetsk and Luhansk in the Donbas area of Ukraine, and stated that he is sending Russian troops to those regions. The U.S. and other countries have stated they will follow through with sanctions they have threatened to impose on Russia if it escalated the situation in Ukraine.

We obviously feel for the people of Ukraine and sympathize with the potential loss of lives. Our aim in this email is to communicate what this new escalation means to the financial markets and our client portfolios.

The initial reaction, as expected, is that global stock markets are falling on this new development and the price of Brent crude oil has climbed to a new seven-year high near $100 per barrel. In our client communication on February 14th, we discussed the investment positions being utilized to mitigate client portfolio volatility. Those same positions are important for the current market volatility. In addition, we discussed our overweight allocation to commodities and especially our overweight allocation in energy and base metals. We also discussed our large allocation to real asset funds in 401(k) portfolios where available, such as in the GM and Ford 401(k) plans.

Both Russia and Ukraine are large exporters of commodities (oil, gas, coal, metals, wheat). One impact of a broader military action and/or sanctions imposed by Europe and the U.S. on Russia is that those commodities become even more scarce in the U.S., Europe, and other countries. As an example, this is the reason crude oil spiked to its highest level in seven years on Monday. Metals, such as nickel, aluminum, palladium, and others are also setting new multi-year highs. Because of our overweight allocation of energy and commodities in our client portfolios, those portfolios actually benefit from sanctions on Russia. It is yet to be seen how severe the sanctions become and what commodities, products, financial holdings, policies, etc. may be included.

Another impact of these potential sanctions on the most abundant Russian exports of energy supplies (i.e., oil, natural gas, coal) and other commodities is the potential to drive inflation even higher. Many commodities have already been in undersupply worldwide, driving prices higher. This is the opportunistic tactical reason for our overweight in commodities and other real assets in our client portfolios. Higher commodity prices have been a driver of higher inflation in the U.S. and other regions of the world. Higher inflation has meant higher interest rates and higher bond yields. As bond prices move inversely to bond yields, bonds have suffered greatly. Hence, our reason for avoiding interest rate sensitive bonds in client portfolios, as discussed in our client communication on February 14th.

Our tactical strategy for more diversification and defense early in the year, relative to each portfolio strategy's objectives and risk profile, has proved prudent. Additionally, our overweight positions in energy and other commodities are proving even more profitable for client portfolios during this period.

It should be pointed out that no geopolitical crisis has a perpetual impact on markets. However, they do cause headline risk that results in day-to-day volatility for the markets in the short term. Ukraine’s impact on stock market volatility will eventually subside. While we have mitigated volatility in portfolios, relative to each portfolio's objectives and risk profile, just as importantly, we are analyzing the events for profitable opportunities for our client portfolios.

For now, and as always, it is important to keep your eye on your long-term goals and not get shaken by short-term volatility. Leave the work and worry to us.

I hope this report has helped you better understand how our current strategy helps mitigate volatility during the crisis in Ukraine, as well as benefit our portfolios profitably.

Please continue to keep yourself and your loved ones healthy and safe. As always, if you ever have any questions about your portfolio holdings, our investment strategy, the financial markets, your personal financial plan, or anything related to your personal finances, contact us at 810-953-5510 or toll-free at 866-444-6246.

We always look forward to talking with you.

Sincerely,

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