

CORE Comments

ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

February 24, 2022

Russia

The dread, but long-predicted disaster is underway; Mr. Putin has commenced his full-scale invasion of Ukraine. I write to discuss briefly the investment and economic situations now before us. Prior to Putin's 'recognition' of the independence of the two eastern provinces in Ukraine early this week and the invasion, stock markets were already weak. Yesterday, prior to the invasion, US stocks closed below the late-January lows, opening the pathway to a bigger decline. Without any Russian problems, stocks were very precarious because of incipient tightening of monetary conditions by the Federal Reserve and because of very inflated stock prices, of which I have written extensively.

The invasion caused an immediate flight to safe assets, including gold and long-term Treasuries. This process had been underway with gold over the last several weeks; gold prices have risen. As discussed in my recent letter, long-term Treasuries have not enjoyed the same success, largely based on calculations of the Fed's planned actions. Both gold and long-term Treasuries, in which Core has large investments, were up substantially in overnight and early morning trading on the invasion news. By contrast, stock markets around the world suffered intense selling. As the US trading day continued, American stock markets recovered and (amazingly) ended higher on the day. The S&P 500 rose by an astonishing 4.2% from its opening level to the close! (As I write, the futures markets foretell weakness in American stock prices tomorrow.)

I think it likely that the coming period will feature both the flight-to-safety trade and the extreme volatility in asset prices that we have witnessed in the last twenty four hours. In this context, please note that Core's clients' accounts have very small investments in stocks, large investments in the flight-to-safety assets and substantial holdings in cash. Prices may move sharply and selling of stocks will make headlines. Your assets, under Core's supervision, will not be wracked by this upheaval.

It is quite clear that the United States and other NATO members will not go to war with Russia over the Ukraine invasion. Indeed, given Mr. Putin's irrational behavior, a direct military conflict involving the United States and Russia would be very dangerous indeed. The sanctions already imposed by Western countries and those on their way will inflict serious harm on Russia and its people, but will also have adverse economic effects in the US and Europe. Russia is a very significant supplier of oil and natural gas to the world and of important industrial metals, including nickel, aluminum, palladium and others. Together, Russia and Ukraine are huge producers and suppliers of many agricultural products. Oil and natural gas prices have risen sharply in the context of Russian actions. We may also expect rising prices for food.

By

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These rising prices, which the world had been experiencing before Russia's misadventures, act as a kind of tax on individuals. Paying more to put food on the table, to put gasoline into car engines, and to put heating oil into furnaces, reduces peoples' available funds for other activity. The result will be slowing demand and economic weakness. Likely to flow from this is a re-assessment by the Fed about its plans to tighten monetary policy.

The uncertainties presented by Russia's dangerous actions are many. At our end, we shall continue the careful and risk-averse approach to investing in this fraught environment. Preserving investment capital is will be very important in the coming months while we await a more favorable investment environment.

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