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Six Minute Strategy

The invasion of Ukraine will change the world

March 2022



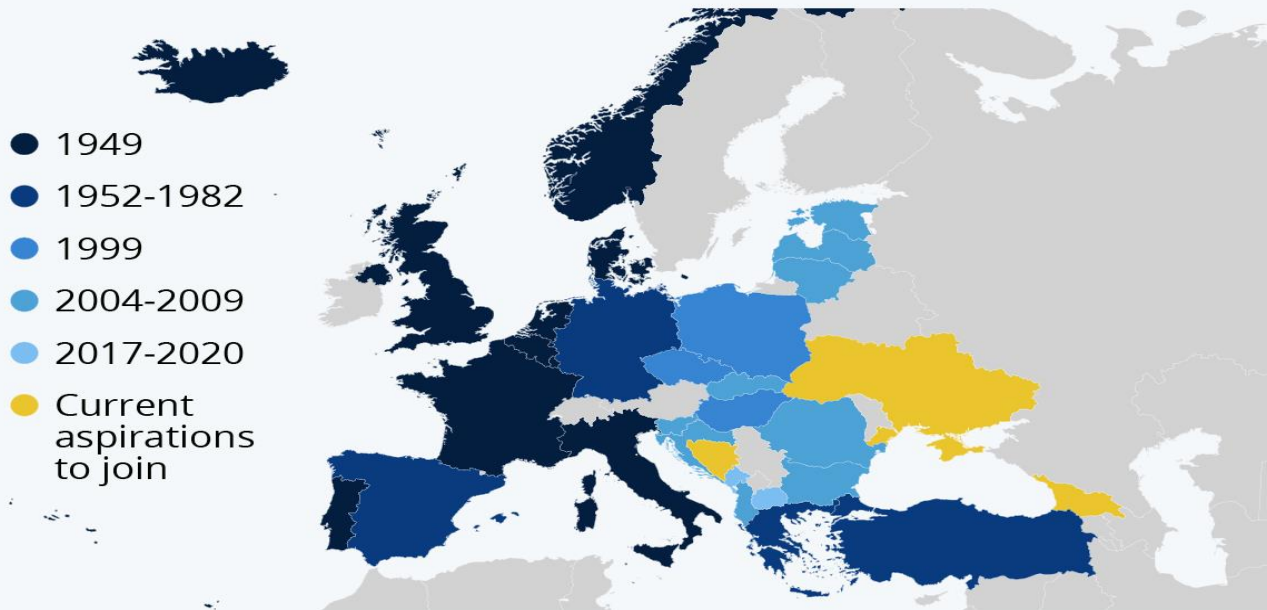
NATO became the flash point for Russia & Ukraine

Russia watched with mounting resentment as the transatlantic alliance has nearly doubled its membership since the end of the Cold War – *More Russian border threats likely*

 NATO's Post-Cold War expansion – 15 new members since the end of the Cold War

How NATO Expanded Eastwards

European countries by year they joined NATO



Map excludes NATO members the United States and Canada

Source: Nato



statista 

NATO

 Post-Cold War expansion

1990 Germany*

1999 Czech Republic
Hungary
Poland

2004 Bulgaria
Estonia
Latvia
Lithuania
Romania
Slovakia
Slovenia

2009 Albania
Croatia

2017 Montenegro

2020 North Macedonia

Source: Statista/Council on Foreign Relations Feb 2022

1: Energy - Russia supplies 40-50% of European gas and 25% of oil imports

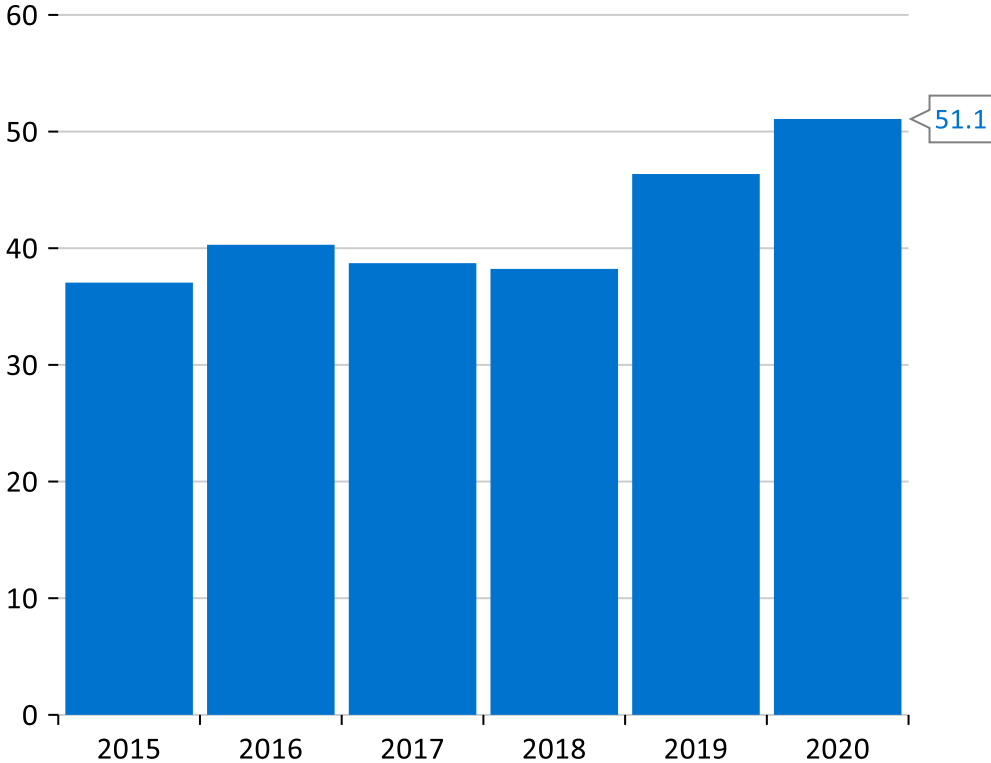


European reliance on Russian gas has been rising



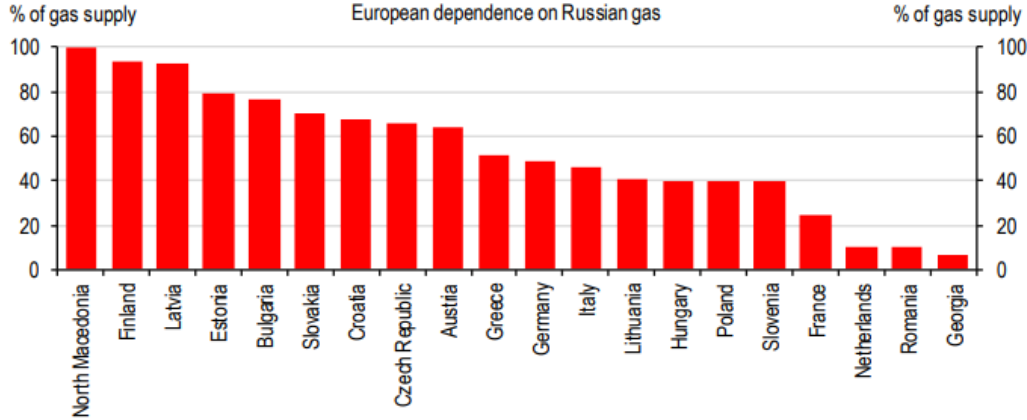
Dependence on Russian gas in Europe is very high

EU - Share of natural gas imports from Russia



Source: Macrobond, 03.03.22

1. Germany and Italy import almost half their gas from Russia



Source: EU Agency for the Cooperation of Energy Regulators. Note: Latest available data, 2019 or 2020.

“If the EU is forced or willing to bear the cost, it should be possible to replace Russian gas already for next winter without economic activity being devastated, people freezing, or electricity supply being disrupted. But on the ground, dozens of regulations will have to be revised...a lot of money quickly spent and hard decisions taken.”

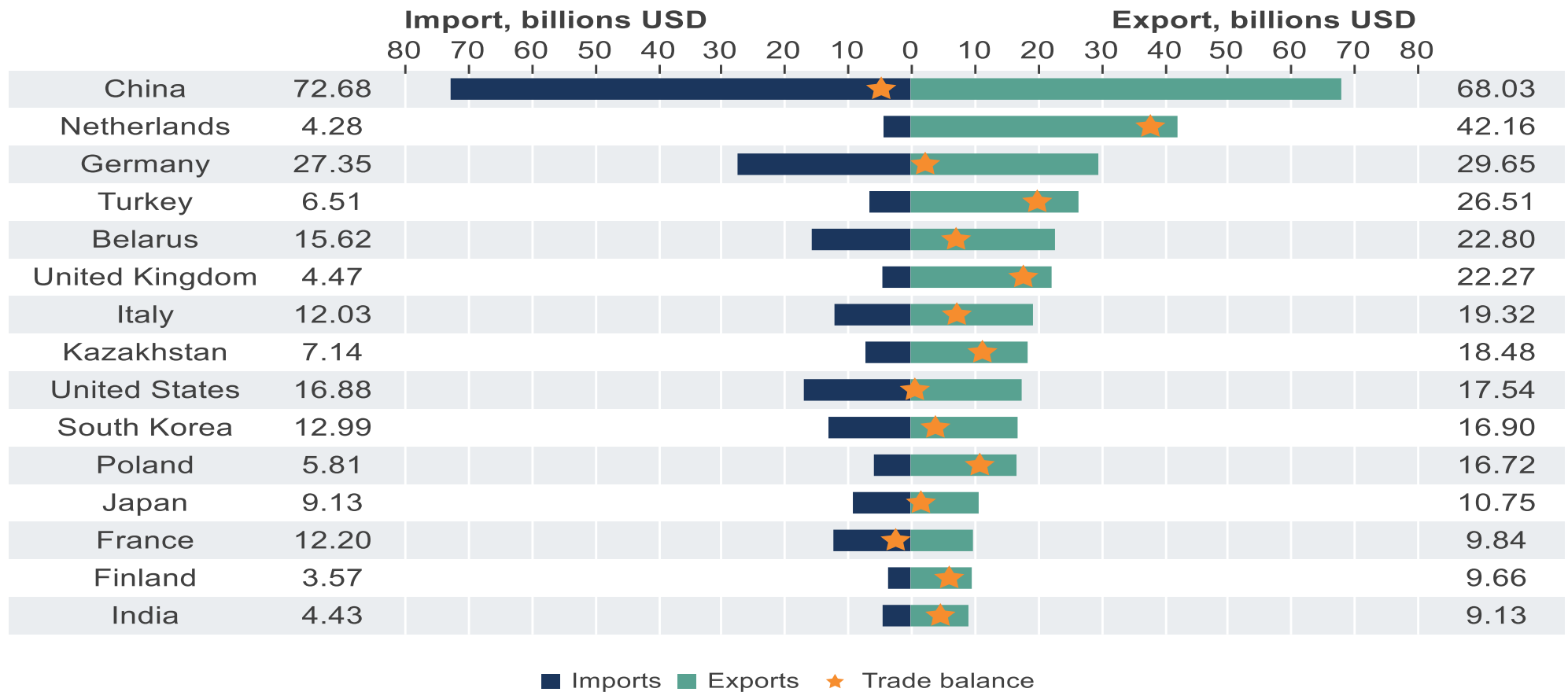
Bruegel Feb 2022

Source: Macrobond/Bruegel Brussels 2022

2. Trade: Russia as a share of global GDP is less than 2% - main transmission channel to global economy will be energy

Russia: Top trade partners

12-months rolling sum



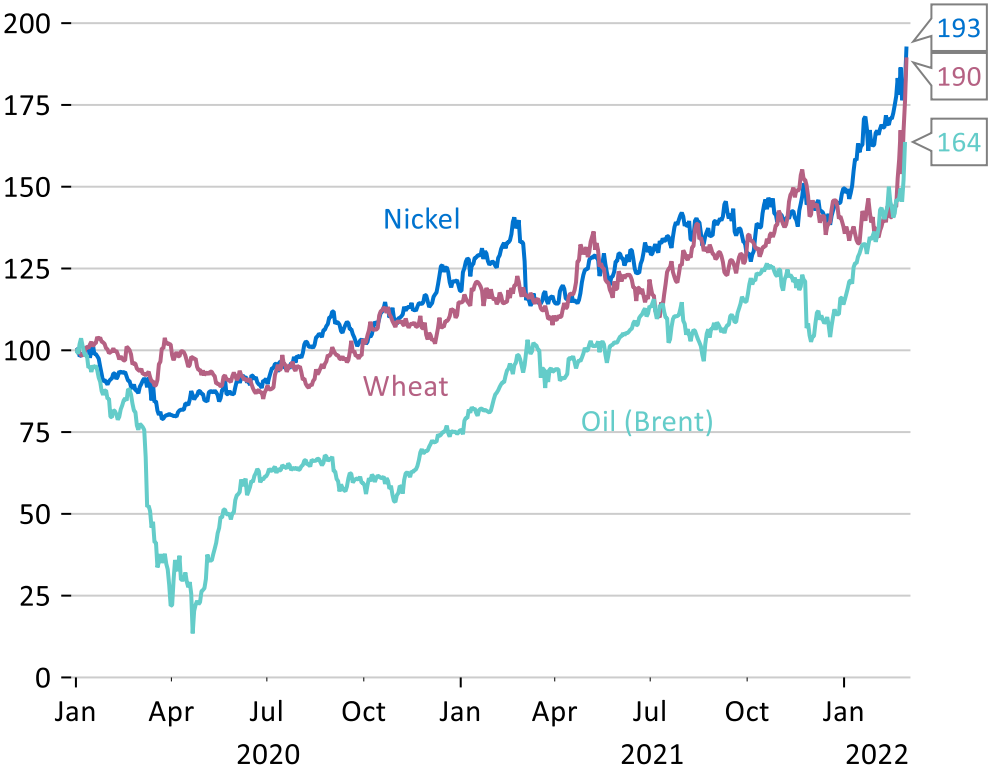
Source: Macrobond

3: Ukraine crisis is adding to global inflation fears

Base effects still mean pricing pressures ease over time

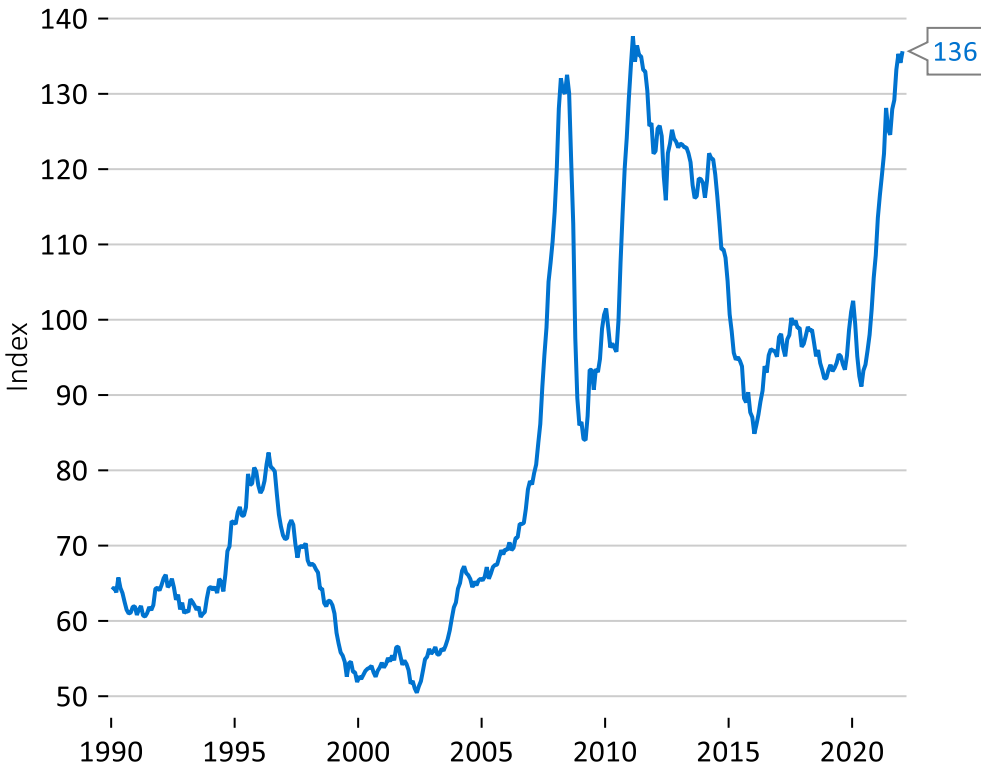
Key Russian commodity prices soar

Russian Key Export Commodity Prices (Rebased end 2019)



Food prices may exceed 2011 high – risking a global crisis

FAO, Global Food Price Index



Source: Macrobond, 03.03.22

Source: Macrobond, 03.03.22

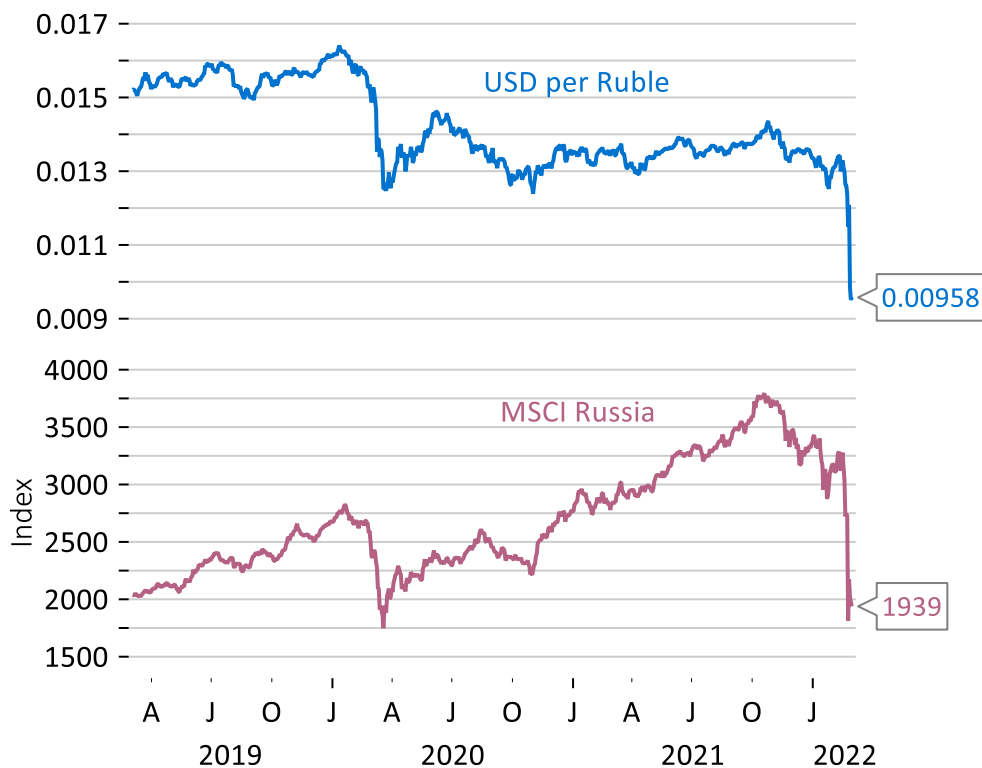
Food prices now close to 2011 levels which contributed to political uprisings in Libya and Egypt

4. Russia: Sanctions, SWIFT exclusion, and frozen central bank reserves may trigger domestic economic collapse



CBR increases policy rates to 20% to defend currency

Russia Currency & Equities

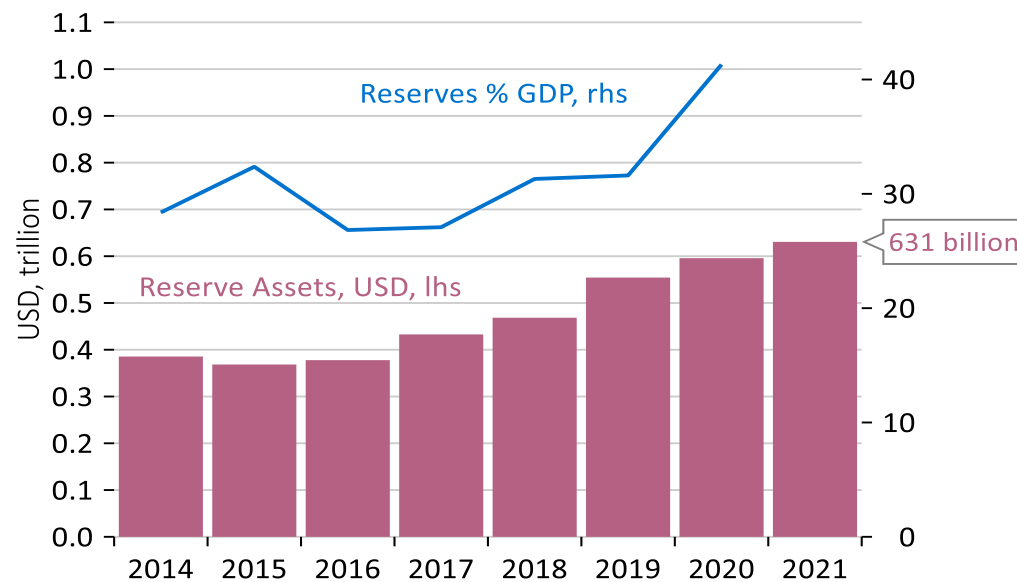


Source: Macrobond, 03.03.22



Russian Central bank reserves (50-70% likely frozen)

	Currency composition (% total)
Eur	32%
Gold	21%
USD	16%
CNY	13%



Source: Macrobond, 03.03.22

No recession risk yet but pace of global growth already slowing

IMF forecasts global growth to moderate to 4.4% in 2022

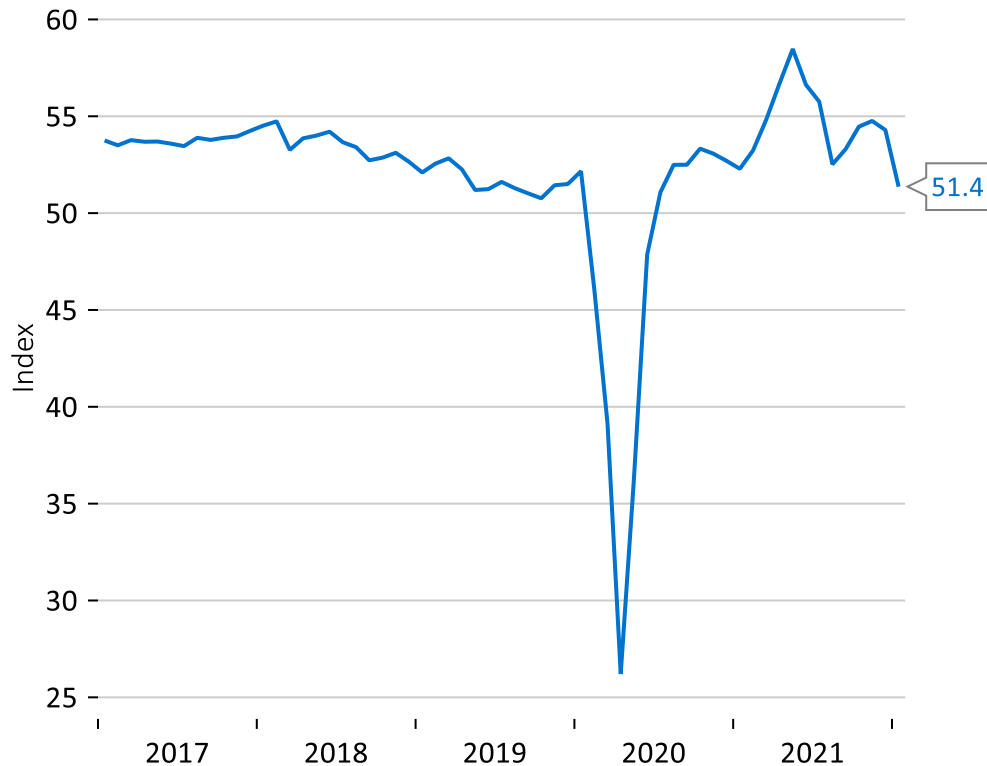


World Composite PMI suggests growth was slowing



Several PMI readings are already < 50 indicating contraction

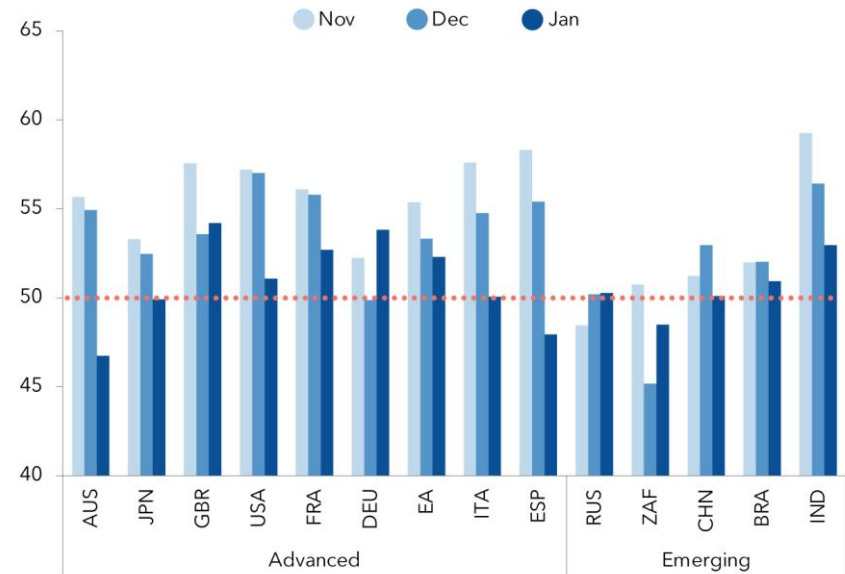
World Composite PMI (IHS)



Source: Macrobond, 03.03.22

Recent weakening

Survey-based measures of activity for some of the world's largest economies are indicating weaker momentum.
(composite purchasing managers' indexes, seasonally adjusted, index > 50=expansion)



Sources: Haver Analytics and IMF staff calculations.
Note: Reading of 50 signals no change from prior month. Readings above 50 indicate improvement, lower readings signal deterioration. ESP is a permanent invitee.

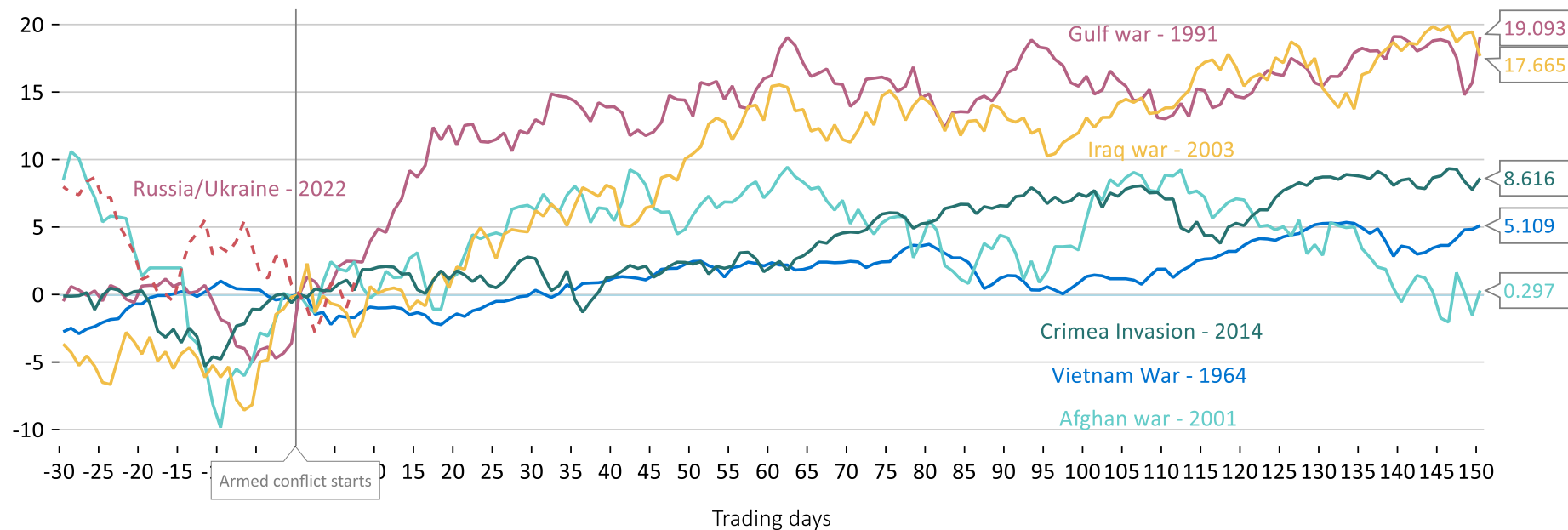


Equity markets are typically resilient at the start of armed conflict

Chart 1: Performance of the US equity market in the six months following a major conflict

S&P500: Equity performance during recent conflicts

Rebased at the start of armed conflict



Source: Macrobond, 03.03.22

Ukraine Invasion: Initial Policy Implications



Ukraine Invasion – Policy implications March 2022

Economic	<p>Inflation higher for longer - no global recession yet</p> <ul style="list-style-type: none"> • Inflation already at 40 year high – Average oil price 2022 of U\$110 means US inflation peaks close to 8% • Interest rates 2022: 4-5 rate rises US, 3 in UK , none in Euro • QT 2022: BOE begins Q2 2022, Fed Q3 and ECB stops bond purchases Q3
Geopolitical	<p>Risk of escalation high</p> <ul style="list-style-type: none"> • Terrible destruction of Ukrainian cities follows experience in Chechnya and Syria • Poland, Hungary & 5 further NATO countries share border with Russia/Ukraine/Belarus – Risk of border clash high • Outside possibility of peace talks - may be sponsored by China
Trade	<p>Deep Russian recession – global trade fragments</p> <ul style="list-style-type: none"> • Russian economy risks recession or possible financial collapse from sanctions/trade restrictions • International banks, industry and consumers reluctant to trade/use Russian assets - moral & sanctions risks • Further partitioning of technology/internet between West, China & Russia
Asset Allocation Implications	<p>Neutral equities</p> <ul style="list-style-type: none"> • Equities neutral – quality, thematic preference with dividend yield where appropriate • Strong UW bonds and credit – caution EM – zero direct exposure Russia • OW Cash - portfolio insurance where appropriate – neutral currencies • OW Alternatives – gold, renewables, infrastructure
Risks	<p>Energy: Russia ceases European gas exports Military: NATO dragged into border war – Further nuclear warnings Recession: Collapse in European consumer and business confidence on drawn out conflict Inflation: Higher for longer as energy centric shock spreads (esp. food) - Triggers wage response</p>

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