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Family Office Digest

The Big Picture

As our table and charts below suggest, markets often "look through" violent geopolitical events after an initial— sometimes sharp—sell-off. Subsequent returns have tended to reflect deeper, underlying economic forces. Losses from a seismic event such as the attack on Pearl Harbor were erased well within a year, whereas the more contained geopolitical shock of the 1973 Arab-Israeli War was followed by a 40% down year for the S&P 500 Index due to a fallout that included an oil embargo, a series of stock market crashes and policy mistakes, and grinding stagflation. These were pre-existing problems exacerbated by the war.

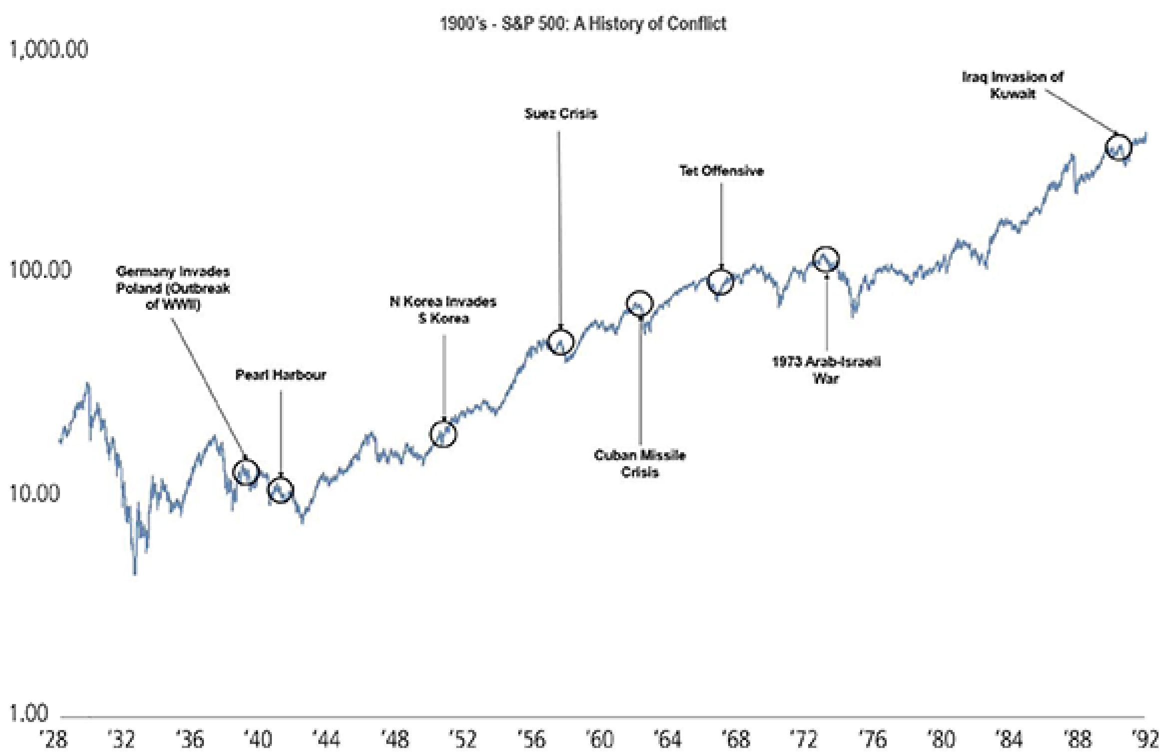
We think the current situation looks very similar. There are signs that markets are refocusing away from the immediate risks from Russia's invasion of Ukraine, back onto their pre-war concerns about inflation and rising rates—not least because that's what the European Central Bank (ECB) and the Federal Reserve (Fed) appear to be doing, too. But investors will find those pre-war inflation concerns exacerbated by the conflict. Grain and fertilizer shortages could become an issue later this year, but energy prices remain the major immediate transmission mechanism to the broader economy of this crisis.

European Union (EU) countries get 20% of their total oil imports from Russia, according to the International Energy Agency (IEA), but they now have a target to be independent of Russian fossil fuels by 2027. The U.K. has committed to phasing out Russian oil imports by the end of this year and is exploring options to end gas imports. Longstanding shareholder demands for capex discipline, among other factors, is likely to hold back supply from elsewhere. That adds urgency to the transition to a net-zero emissions economy—but Russia is also an important supplier of the metals that are essential to that transition. Add in a likely increase in defense spending and Cold War-like tensions raising incentives to localize and deglobalize value chains, and we think we get a recipe for higher inflation and growth headwinds. As Hakan Kaya and Joe McDonnell discuss in one of our recent podcasts, this only strengthens the case for reintroducing commodities to the asset allocation mix. .

A Century of Violent Geopolitical Shocks to the S&P500 Index

Event	Date	One Day Move	Total Drawdown	3 Month	12 Month	Days to Bottom	Days to Pre-event Recovery
Pearl Harbor	07.12.1941	-3.80%	-19.80%	-10.20%	7.30%	143	307
North Korea Invades South Korea	25.06.1950	-5.40%	-12.90%	3.90%	20.60%	23	82
Suez Crisis	29.10.1956	0.30%	-1.50%	-2.70%	-8.80%	3	4
Cuban Missile Crisis	16.10.1962	-0.30%	-6.60%	14.40%	32.10%	8	18
Kennedy Assassination	22.11.1963	-2.80%	-2.80%	12.50%	27.80%	1	1
Tet Offensive	30.01.1968	-0.50%	-6.00%	5.90%	13.90%	36	65
1973 Arab-Israeli War	06.10.1973	0.30%	-0.60%	-9.10%	-40.90%	5	6
Iraq Invasion of Kuwait	02.08.1990	-1.10%	-16.90%	-10.40%	14.00%	71	189
September 11 Attacks	11.09.2001	-4.90%	-11.60%	4.40%	-15.50%	11	31
London Subway Bombing	05.07.2005	0.90%	0.00%	-0.20%	7.50%	1	4

Source: American Association of Individual Investors, LPL Research, FactSet, reflects S&P 500 Index. For illustrative purposes only. Nothing herein constitutes a prediction or projection of future events or future market behavior. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed or any historical results. Indexes are unmanaged and are not available for direct investment. Investing entails risks, including possible loss of principal. **Past performance is not a guide to future results.**



Source: FactSet. For illustrative purposes only. Nothing herein constitutes a prediction or projection of future events or future market behavior. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed or any historical results. Indexes are unmanaged and are not available for direct investment. Investing entails risks, including possible loss of principal. Past performance is not a guide to future results.

The Close-Up

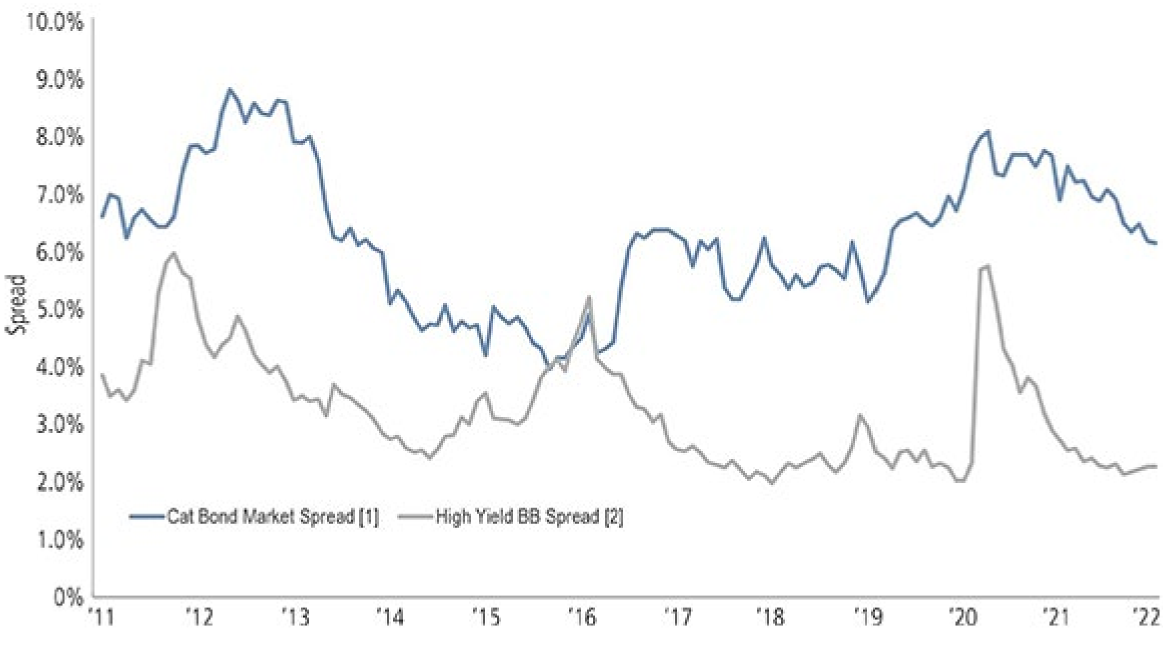
The probability that the invasion of Ukraine adds a profound and unwelcome geopolitical layer to pre-existing concerns about inflation and rising rates would explain why global fund managers came into March so pessimistic about future growth prospects. Yield-curve flattening through January and February already pointed to the risk that stubborn inflation might force central banks, markets or both to tighten financial conditions enough to tip the economy into a slowdown or even a recession. Messaging from the ECB and the Fed indicates that they remain more concerned about inflation than growth, even after the outbreak of war.

Investors Appear to be as Pessimistic About Global Growth Prospects as They Were in October 2008
BofA Global Fund Manager Survey, net percentage expecting a stronger economy

Source: Bank of America. Nothing herein constitutes a prediction or projection of future events or future market behavior. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed or any historical results. Investing entails risks, including possible loss of principal. **Past performance is no guarantee of future results**.

The Snapshot

Widespread pessimism about geopolitics impacting the economy could be a signal to come for investors to start taking on market risk. Others may wish to seek compensation for risks that are not at all exposed to geopolitical or economic catastrophe: Insurance-Linked Strategies (ILS) have tended to offer diversifying exposure to natural catastrophe risk—and they may offer attractive spreads



Source: Cat Bond spreads from Bloomberg, Lane Financial (includes USD-denominated 144A notes covering natural catastrophe risks only); ICE BofA BB U.S. High Yield Index option-adjusted spreads from Federal Reserve Bank of St. Louis (FRED). Data as of January 2022. For illustrative and discussion purposes only. Nothing herein constitutes a prediction or projection of future events or future market behavior. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed or any historical results. Indexes are unmanaged and are not available for direct investment. Investing entails risks, including possible loss of principal. **Past performance is no guarantee of future results**.

Fixed Income Amid Inflation

What does the current inflationary environment mean for multi-sector fixed income portfolios?

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