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How will Russia's invasion of Ukraine impact your investments? There are a few main points we want to get across to you during this time of increased uncertainty. The first is that your investments will do just fine. The second is that the Federal Reserve's reduction of interest rate stimulus matters more for your investments than does the Ukraine invasion. The third is that we've positioned client investments for resilience through both the Ukraine invasion and reduction of Federal Reserve stimulus.

We begin with a table showing how U.S. stocks reacted to past geopolitical crises from 1941 to 2020[(1)]:

		S&P 500 Index decline		Calendar days to	
Market shock event	**Date**	**One-day**	**Total**	**Bottom**	**Recovery**
Iranian general killed in airstrike	1/3/2020	-0.7%	?	?	?
Saudi Aramco drone strike	9/14/2019	-0.3%	-4.0%	19	41
North Korea missile crisis	7/28/2017	-0.1%	-1.5%	14	36
Syria bombing	4/7/2017	-0.1%	-1.2%	7	18
Boston Marathon bombing	4/15/2013	-2.3%	-3.0%	4	15
London Tube bombing	7/5/2005	0.9%	0.0%	1	4
Madrid bombing	3/11/2004	-1.5%	-2.9%	14	20
9/11 terror attacks	9/11/2001	-4.9%	-11.6%	11	31
Iraq invasion of Kuwait	8/2/1990	-1.1%	-16.9%	71	189
Ronald Reagan shot	3/30/1981	-0.3%	-0.3%	1	2
Yom Kippur War	10/6/1973	0.3%	-0.6%	5	6
Munich Olympics	9/5/1972	-0.3%	-4.3%	42	57
Tet Offensive	1/30/1968	-0.5%	-6.0%	36	65
Six-Day War	6/5/1967	-1.5%	-1.5%	1	2
Gulf of Tonkin Incident	8/2/1964	-0.2%	-2.2%	25	41
JFK assassination	11/22/1963	-2.8%	-2.8%	1	1
Cuban Missile Crisis	10/16/1962	-0.3%	-6.6%	8	18
Suez Crisis	10/29/1956	0.3%	-1.5%	3	4
Hungarian uprising	10/23/1956	-0.2%	-0.8%	3	4
N. Korea invades S. Korea	6/25/1950	-5.4%	-12.9%	23	82
Pearl Harbor attack	12/7/1941	-3.8%	-19.8%	143	307
Average		**-1.2%**	**-5.0%**	**22**	**47**

As you'd expect, the Pearl Harbor attack had the biggest stock market impact since it preceded World War II. But even the scale of that situation only led to a 20% stock market decline, which fully recovered in eleven months. The main point of this table is that geopolitical events have all had only a short-term impact on stocks. We expect the same to be true for the Ukraine crisis. As you can see, the average geopolitical event led to a 5% decline in U.S. stocks, with full recovery in 22 days.

It's also important to note that the vast majority of the investments we have selected for you have endured through both world wars. Some of them endured through the U.S. Civil War, which killed more Americans than any war and almost destroyed our nation. In fact, we won't buy an investment that doesn't have a demonstrated long-term track record of enduring through crises. That is a cornerstone of our investment strategy. While we will experience continued short-term volatility as a result of the Ukraine invasion, we know that our investments will endure through this crisis(2).

Now getting back to the chart above, how does the average geopolitical stock market decline of 5% compare with where stocks sit at the end of February? As we mentioned last month, U.S. stocks were already in the middle of a correction that began last November as a result of the Federal Reserve announcing it would reduce interest rate stimulus in order to tame inflation. Through the end of February, U.S. stocks had fallen 15% from their November high levels. As we also mentioned last month, speculative and popular investments have done worse, with the technology-heavy NASDAQ index falling 22% into February. So at this point, U.S. stocks have already fallen far more than they have during the average historical geopolitical event. And the decline was driven more by Federal Reserve stimulus reduction than by the Ukraine invasion(3).

The biggest question the Ukraine invasion poses for financial assets is whether it adds to our inflation problem and forces the Federal Reserve to reduce interest rate stimulus even more than expected. Because Russia supplies oil and other commodities to the world, the prices of those commodities have increased substantially since the Ukraine invasion. Obviously, these commodities are used in the production and transport of almost all physical products. So at this point in time, the Ukraine invasion does have the potential to make our inflation problem worse.

If this higher inflation means the Fed must do more to reduce interest rate stimulus, we would expect the declines in popular and speculative investments experienced over the past several months to continue. In order to get an idea of what happens during time periods of elevated inflation and Fed stimulus reduction, we have to go back fifty years to the 1970s. The 1970s had some similarities to today, with high inflation, rising interest rates, and a spike in oil prices. Over the ten years 1972 to 1982, the Dow Jones stock index was flat. But investors who reinvested dividends over that time period earned a 69% return over that decade, rather than the zero percent return of the index. This illustrates the importance of investing in stable businesses that pay steady dividends in the coming years, which is another cornerstone of our Group's investment process(4).

We can look back twenty-three years to another time period when speculative and popular investments did poorly. From 1999 to 2009, the U.S. experienced events with some similarity to current economic conditions, with two periods of Fed stimulus reduction, as well as a major geopolitical event in the 9/11 attacks. This time period also witnessed the collapse first of technology stocks, and then home prices. Over those ten years, U.S. stocks as a whole declined 9%. Yet individual sectors generated gains over that period, with Consumer Staples increasing 66%, Health Care increasing 30%, and Industrials increasing 8%. This again points to the importance of owning stable businesses that pay steady dividends over time(5).

Going through corrections and crises is always uncomfortable. But it's also always a part of successful investing. Just two years ago our economy fell into dark days, with the highest unemployment rate since the Great Depression. No one knew how the covid-19 economic crisis would end, but it did end and financial markets came roaring back. We must learn from that experience. All crises begin for different reasons, but they all share something in common: they end. Our conservative investment process of owning steady businesses providing the basic necessities of life has prepared our clients to meet this moment of uncertainty. If you have any questions or concerns, please contact us.

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Sources:

(1) Kiplinger
(2) Company reports
(3) Yahoo Finance
(4) Roger Thomas
(5) Richard Bernstein Advisors