Truist Advisory Services, Inc.

Market Perspective from the Investment Advisory Group

Market implications of rising Russia-Ukraine tensions

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What happened

Markets have been trading in erratic fashion over recent days on the heels of rising Russia-Ukraine tensions. Indeed, U.S. stocks sold off late Friday and European markets, such as Germany and France, are down more than 2% this morning. We've also seen some signs of a flight to safety with gold prices at a multi-month high and oil prices at the highest level since 2014.

Our take

The Russo-Ukrainian crisis was one of the major geopolitical risks we discussed in our outlook coming into the year. This uncertainty, combined with ongoing investor angst surrounding the Federal Reserve (Fed) policy transition, is set to keep market volatility elevated relative to the serene environment seen over the past year.

That said, while it is typical to see geopolitical events lead to short-term market weakness, historically, these types of events tend not to have a lasting impact unless they lead to recession.

For example, when looking at a sample of major historical geopolitical/military events, the S&P 500 was higher 12 months later in nine of the 12 events we reviewed (see table on next page). The three instances where stocks were down a year later coincided with a recession. Our view remains that U.S. recession risks remain low. Indeed, given the peak in omicron, we expect economic growth to rebound headed into the second quarter. Pent-up demand for services remains high, cash levels of consumers and businesses remain robust, and the job market remains strong.

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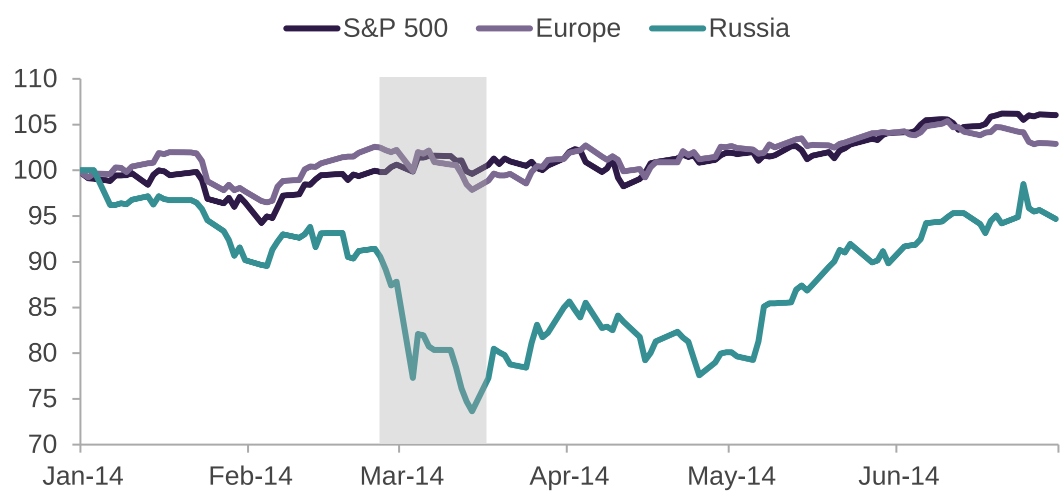
S&P 500 performance around select geopolitical/military events

Date	Select geopolitical/ military events	1-month later	3-months later	6-months later	12-months later
12/7/1941	Pearl Harbor	-3.4%	-12.7%	-9.1%	0.4%
10/31/1956	Suez Canal crisis	-2.8%	-3.8%	-0.1%	-11.5%
10/20/1962	Cuban missile crisis	8.7%	17.7%	25.1%	32.0%
10/17/1973	Arab oil embargo	-7.0%	-13.2%	-14.4%	-36.2%
11/3/1979	Iranian hostage crisis	4.2%	11.6%	3.8%	24.3%
12/25/1979	U.S.S.R. in Afghanistan	5.6%	-7.9%	6.9%	25.7%
8/3/1990	Iraq invades Kuwait	-8.2%	-13.5%	-2.1%	10.1%
1/17/1991	Gulf War	15.2%	23.5%	20.6%	33.1%
8/17/1991	Gorbachev coup	0.0%	3.0%	7.0%	8.9%
2/26/1993	World Trade Center bombing	1.2%	2.5%	4.0%	6.4%
9/11/2001	9/11	-0.2%	2.5%	6.7%	-18.4%
3/20/2003	Iraq War	2.2%	15.6%	17.4%	28.4%
	Average	**1.3%**	**2.1%**	**5.5%**	**8.6%**
	% Positive	**50%**	**58%**	**67%**	**75%**

Data Source: Truist IAG, FactSet. Grey shading represents down markets where the economy was in recession at some point during the measurement period. Past performance does not guarantee future results

Although the previous study focused on major events over recent years, there have been several lesser geopolitical events that caused investor angst such as when U.S. forces killed an Iranian military leader in January of 2020 or the North Korean missile crisis in 2017. Perhaps the most similar was in early 2014 when Russia invaded and annexed Crimea from Ukraine. While European markets were down less than 5% and the Russian market was down double digits surrounding this event, U.S markets were down less than 1% and the underlying uptrend remained in place.

A look back at early 2014 - Russia seizes Crimea



Data Source: Truist IAG, FactSet. Indexed to 100 at 1/1/2014. Past performance does not guarantee future results.

Portfolio positioning

We maintain our long-standing U.S. equity overweight relative to international markets given its higher quality and the U.S.' more insular economy. European markets are more at risk due to the interconnectedness of those economies with the Russian energy and commodity complex. Since Russia is a constituent, emerging market (EM) equities and bonds would likely also be negatively affected. Therefore, we maintain our underweight positioning to EM. Although we remain underweight fixed income, as we discussed more recently with the sharp rise in yields, high-quality bonds have become incrementally more attractive. The latest geopolitical tensions reinforce the diversification benefits of maintaining some exposure to these bonds, despite their recent underperformance.

Bottom line

The Russia-Ukraine border crisis complicates the near-term market outlook. That said, history suggests these types of events, which can be devastating from a humanitarian standpoint, tend to have a fleeting market impact unless they lead to a recession. Our work suggests recession risk in the U.S. remains low. Rising geopolitical risks, alongside the upcoming Fed transition, argue for continued choppier waters in the markets near term. Nevertheless, our base case remains that what we have been seeing this year is a corrective period within the context of an ongoing bull market.

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S&P 500 Index is comprised of 500 widely-held securities considered to be representative of the stock market in general.

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