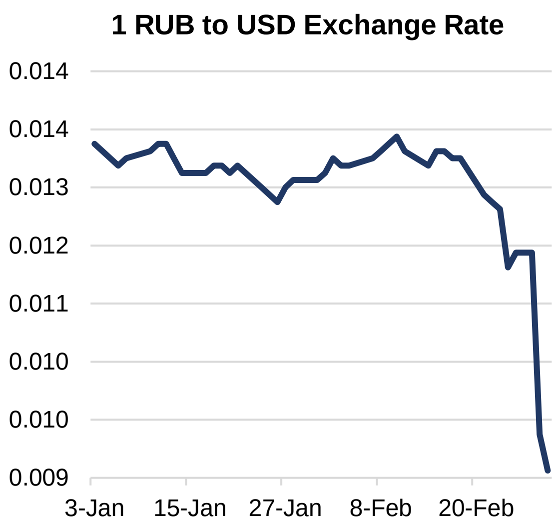
MARKET UPDATE

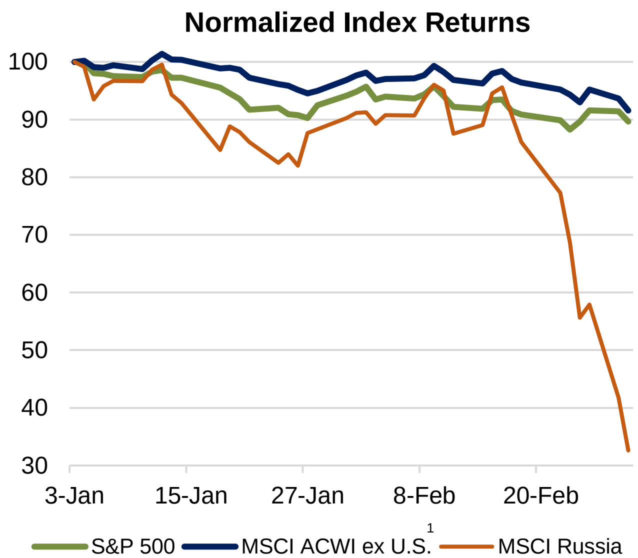
March 2, 2022

THE CONFLICT IN UKRAINE

Current Situation

- Russian forces struck the central square of Kharkiv, Ukraine's second largest city, on Tuesday. Moscow's frustrations with the prolonged initial conflict have propelled them to target civilian areas in an attempt to demoralize Ukrainian resistance.
- Ukrainian President Volodymyr Zelenskyy has officially signed an application for Ukraine's membership in the European Union in an effort to garner more support from the bloc.
- Cease-fire talks have failed to produce results so far. Russia and Ukraine have agreed to further talks; however, Moscow is expected to increase the tempo of its assaults on major Ukrainian cities and is pouring manpower and equipment into the country.
- The European Union is set to instruct the SWIFT financial network to delist seven Russian banks, including VTB bank. Sberbank of Russia isn't among the banks to be delisted at this point, representing an EU compromise as some countries like Germany have argued it is important to ensure some banks remain on SWIFT to help Europe pay for energy imports from Russia.
- Russia's financial markets remain largely closed since Monday as they grapple with the financial fallout from a barrage of international sanctions.





[1]MSCI ACWI ex U.S. represents developed and emerging markets outside of the United States

What is Driving Volatility?

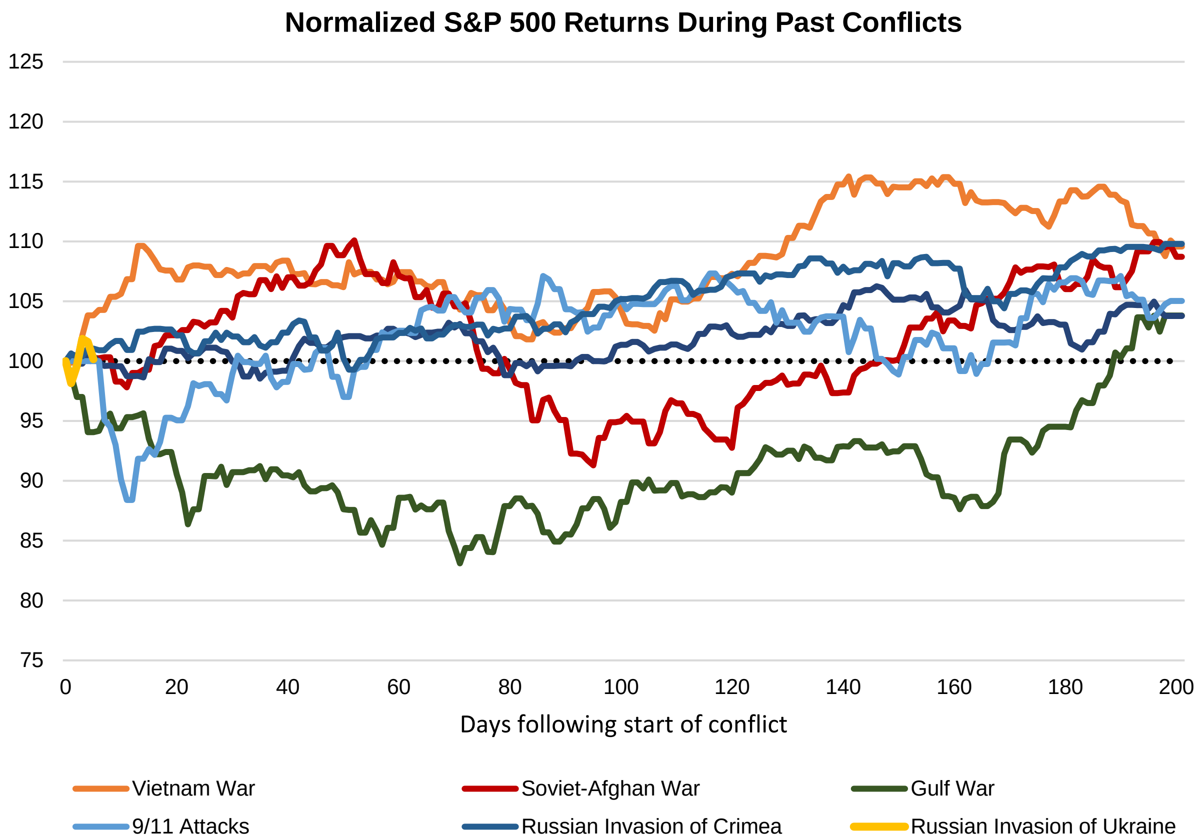
Vladimir Putin ordered an invasion of Ukraine after a months-long buildup of Russian forces along Ukrainian borders. The invasion was launched along three fronts: from the South through Crimea, from the North through Belarus, and from the East directly through Russia. There are reports of pockets of successful resistance from the Ukrainian military, but it is largely believed that the conflict will end with a Russian victory. Mr. Putin is primarily motivated by preventing the expansion of NATO into Ukraine which would place strike weapons along Russian borders. Additionally, taking over Ukraine has long been part of Mr. Putin's ambition to redeem the humiliation of the collapse of the Soviet Union. To that end, he plans to topple the current Ukrainian regime in Kiev and install a puppet government. In doing so, Mr. Putin has sacrificed all relations with the West, severely weakened Russia's future economic prospects, and taken steps to making Russia an international pariah.

The Western Response

The Western response was largely expected, focusing on sanctions that seek to cripple Russia's economic and military capabilities. The actions being taken by the U.S. are targeting large state-owned enterprises, Russian oligarchs, and exports of critical military and aerospace technology to Russia. The European Union and U.K. have announced similar sanctions aimed at stifling Russia's economy. How the Western response develops from here will be the key to how systemic this conflict becomes. While the announced sanctions are damaging, they stopped short of explicit sanctions on the Russian energy sector and removing Russia from the SWIFT global interbank payments system. These two sanctions are probably being held as cards to be played in the event of further escalation, as they are likely to provoke a Russian response. Europe has become largely dependent on Russian oil exports as they have aggressively cut domestic oil production in their quest to shift to alternative energy. By sanctioning the Russian energy sector, oil prices will increase meaningfully, and Western politicians will have to answer to constituents that have already been dealing with record-high inflation. A removal from the SWIFT system could provoke Russia to cut its own oil production numbers, sending oil prices higher and creating dissent in Western nations. The delicacy being taken in rolling out sanctions demonstrates the diplomatic dynamic of dealing with the irrational, immoral, autocratic nuclear powers of the East.

Investment Implications

In reaction to the news of the invasion global stocks tumbled, while havens and commodities surged. The flight to safety saw the 10-year U.S. Treasury yield touch 1.9% and gold hit its highest level since early 2021. The dollar jumped while the Euro retreated. In the near-term we expect more volatile markets as the situation remains in flux. The immediate impacts are on food and energy prices, which will feed into higher inflation and slower economic growth. It is more likely now that inflation will peak later in 2022 than previously expected as this conflict exacerbates global supply shocks. The combination of higher inflation and slower economic growth puts the Fed in a difficult decision with respect to rate hikes. On the one hand, current inflation levels necessitate some degree of policy normalization. However, they will be hesitant to tighten aggressively into a slowing growth dynamic. In our opinion, the Fed will hike at their March meeting but the likelihood of a 50 basis point hike is dwindling quickly. Overall, this shouldn't derail the economic expansion this year if the conflict remains contained to non-NATO countries. As markets navigate the situation, they should eventually discover a new equilibrium in this tense geopolitical environment.



Given what we know at this point, we still believe that equilibrium will favor value-oriented equities over growth equities in a slowing growth environment. We continue to remain underweight duration within core fixed income as long-term rates should move higher. Finally, we still see favorable relative valuations in international equities relative to the U.S. if the conflict remains contained and doesn't escalate to the point of NATO troop involvement.

We don't change our portfolio positioning in reaction to geopolitical shocks. Such moves would be akin to market timing and the surprising rebound on Thursday after the news was announced is a testament to how fruitless that exercise is. Investment plans account for volatility and unexpected events over the duration of the plan. Remaining invested in a diversified portfolio that accurately reflects your specific risk tolerance remains the best option in today's market environment.

We thank you for your continued trust and confidence. Please call us if you would like to discuss this further.

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