



February 28, 2022

Statement re: Russia-Ukraine Conflict

Dear Investor,

With a full-scale invasion of Ukraine now underway, we want to share some thoughts about this conflict's impact on our investment portfolios and the developments we are monitoring.

As of this writing, we have no direct exposure to Russia in our International or Global portfolios and 1% in our Emerging Markets portfolio via an investment in gold miner Polymetal (privately-owned, London-listed, and Cyprus-incorporated gold miner with about 80% of its production assets in Eastern Russia). Indirect exposure is minimal, residing primarily in global consumer and energy/resource franchises. Nestle and Danone each generate less than 5% of sales from Russia. Kinross Gold, TotalEnergies, and BP generate 12%, 9%, and 4% of cash flows, respectively, from Russia.

We have reviewed our previously-established assumptions and models to see if any adjustments were warranted, but as long-term investors, we are not making any meaningful portfolio changes at this time. We will seek to capitalize on opportunities that arise amidst the macro uncertainty.

The February 24th invasion of Ukraine is one of the most significant geopolitical developments in recent decades. From a broad perspective, there will be downward pressure on already slowing global economic growth and upward pressure on inflation. The odds of stagflation have increased. The situation is fast-moving and implications for investors are far-reaching, but some important considerations include:

- **Energy prices** are a central risk, most acutely in Europe, as the region receives nearly 40% of its natural gas and 25% of its oil from Russia. Both consumers and energy-intensive industries will feel pressure. European gas futures have already climbed from 16€ per megawatt-hour (MWH) to 142€ last week before settling at 103€ this morning. For cross-border perspective on this, 103€ MWH equates to \$33.90 per mmbtu. By comparison, US gas today is “only” \$4.44 per mmbtu.
- Beyond oil and natural gas, Russia is a major exporter of palladium (40% of global supply), titanium (22%), and nickel (11%). Coupled with Ukraine, they also produce 33% of global wheat exports and 80% of sunflower oil production. The impact of a sustained increase in **commodity prices** on emerging markets will vary, but we believe the pressure will be felt primarily by importers (India, Thailand, much of Asia, Turkey), while exporters (Malaysia, LatAm) could benefit.
- The momentum behind **climate change initiatives** could slow as policymakers focus on energy security and near-term economic pressures.
- **Supply chain disruptions** will increase, particularly in commodity-sensitive industries and those exposed to the expanding list of sanctions. The prevailing system of globalized supply chains will evolve, and new economic blocs could emerge.
- Expect an increase in **defense spending**. According to Bank of America, very few of the larger NATO countries historically spent the agreed-upon 2% of GDP on defense. US defense spending as a percentage of GDP has fallen since the Cold War era when it stood at 7% of GDP (versus 2.8% today). Just this weekend, Germany announced a commitment to spend at least 2% going forward.



- **Cybercrime and cyberwarfare** will continue to escalate. This will have broad impacts on all companies and industries given the need to increase skills and spending to combat the substantial threat. The FT and McKinsey “Business Book of the Year 2021” – *This Is How They Tell Me the World Ends* by Nicole Perlroth – is a must-read.
- The **risk of central bank policy errors** has increased as policymakers attempt to manage fragile economic conditions and rising inflationary pressures.
- Beijing has not denounced Russia’s actions and is watching how the US and its allies respond to Russian aggression in Ukraine as part of their calculations around **Taiwan**.
- A significant long-term **geopolitical shift** is underway as Russia tilts east and establishes greater engagement with China in an attempt to reduce its vulnerability and dependence on the West.

Nobody knows how this geopolitical conflict will play out, as Putin continues to be a coy actor. Our assumption is that his efforts will be swift and direct with a puppet government installed. However, it is important to remind ourselves that unexpected things happen all the time – in both life and investing.

We would be happy to discuss any of these topics in greater detail. Please do not hesitate to reach out with questions.

Sincerely,

John D. Hock

IMPORTANT CONSIDERATIONS & ASSUMPTIONS

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