WINTHROP WEALTH

MARCH 2022 CLIENT QUESTION OF THE MONTH:
Market Reaction to Geopolitical Events

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The major news event in the month of February was the Russian invasion of Ukraine. At the time of this writing, the war has been ongoing for five days, with most analysts highlighting that the conflict has lasted longer than expected as Ukraine has put up a fierce resistance. Peace talks between the two sides on February 28th ended without a ceasefire but an agreement to meet again within a few days. We also want to acknowledge the humanitarian tragedy taking place in Ukraine. The events are both shocking and heartbreaking, and we hope for a quick resolution.

The United States, United Kingdom, and European Union all announced sanctions on Russian banks, financial institutions, and certain individuals with close ties to Vladimir Putin. The sanctions removed some Russian banks from the Swift payments system. The Society for Worldwide Interbank Financial Telecommunication (SWIFT) is a global system for financial transactions that connects more than 11,000 banks in more than 200 countries. The United States and other countries also announced sanctions on Russia's central bank, which are designed to prevent the selling of foreign assets for local currency to prop up Russian banks. According to the Treasury Department, the measures will "effectively immobilize" any Russian central bank assets held in the United States. The Russian Ruble is down over-20% against the US dollar over the last month. The Russian central bank also raised its key interest rate to 20%, while S&P downgraded the country's credit rating to junk.

The sanctions were also designed to be less disruptive to Russian oil and natural gas. By keeping some Russian banks on the Swift system, the European Union kept open payment channels for the purchase of natural gas. The US also created exceptions for oil purchases. The White House specified that they would try and prevent oil prices from spiking by releasing more emergency reserves

Bespoke Investment group identified fourteen major geopolitical events since 1940 and the impact on the S&P 500 after 1-week, 6-months, and 12-months. Historically, the market was down about -3.6% 1-week after the event. However, the market tended to recover relatively quickly as the S&P 500 was higher by +6.0% and +7.1% after 6- and 12-months respectively.

Impact of Geopolitical Events on the S&P 500

Event	Event Date	One Week Later	Six Months Later	Twelve Months Later
Germany invades France	5/10/1940	-15.4%	-4.5%	-18.7%
Pearl Harbor	12/7/1941	-6.3%	-9.1%	0.4%
Korean War	6/25/1950	-7.6%	4.1%	11.7%
Suez Crisis	10/29/1956	2.6%	0.0%	-11.6%
Cuban Missile Crisis	10/16/1962	-6.3%	20.7%	27.8%
Gulf of Tonkin	8/2/1964	-1.6%	5.3%	2.7%
USSR Invades Afghanistan	12/24/1979	-1.8%	6.9%	25.7%
Iran-Iraq War	9/22/1980	-5.3%	3.3%	-10.5%
Iraq Invades Kuwait	8/2/1990	-3.3%	-2.1%	10.1%
Gulf War I	1/17/1991	2.1%	17.5%	27.5%
Gorbachev Coup	8/19/1991	4.6%	8.2%	11.8%
9/11 Attacks	9/11/2001	-11.6%	6.7%	-18.4%
Gulf War II	3/20/2003	-0.8%	18.7%	26.7%
Russia Invades Crimea	2/20/2014	0.8%	8.0%	14.7%
Average		-3.6%	6.0%	7.1%

The situation in Ukraine remains very fluid, and no one can predict exactly how it will play out (unless you could get inside Vladimir Putin's head). During these periods of extreme market volatility, we follow the same playbook and convey the same messages. At Winthrop Wealth, we believe the right mindset paired with a comprehensive financial plan and a thorough investment process can provide a sense of comfort and confidence in meeting your long-term financial goals, especially during times of heightened market volatility.

The Right Mindset – Take a long-term viewpoint and avoid the impulse to market time

"Don't try to buy at the bottom and sell at the top. It can't be done - except by liars." - Bernard Baruch

Market volatility is stressful and controlling your emotions during these periods is critical. Market timing decisions are often emotional rather than rational and data based. Making sudden large adjustments to portfolios is value destructive over time and a major reason for poor investor performance. Our investment philosophy is, never time the market. Please see our Client Question titled **Market Timing Does Not Work**, where we demonstrate that: the stock market goes up over time despite frequent drawdowns, the average investor underperforms due to market timing mistakes, and the benefit of a diversified portfolio and a long time horizon.

Financial Plan

"The Best way to measure your investing success is not by whether you're beating the market but by whether you've put in place a financial plan and behavioral discipline that are likely to get you where you want to go." -Benjamin Graham

Financial planning drives the investment strategy and provides a roadmap to each client's unique goals and objectives. The comprehensive financial plan defines cash flow needs, optimizes account structures, considers tax minimization strategies, and continuously evaluates financial risks as circumstances and/or goals change.

We also stress test the financial plan for many different environments including extreme volatility and market declines. The financial plan does not assume perpetually strong markets and linear returns. Rather it assumes that your portfolio will go through periods of weakness throughout your investment time horizon. We often update financial plans during and after volatility to quantify the impact that the market decline had on the probability that the client will reach their long-term goals and objectives. Since we account for market volatility and declines, the financial plan is less likely to be damaged when these periods inevitably occur.

Investment Process

"Good times teach only bad lessons: that investing is easy, that you know its secrets, and that you needn't worry about risk. The most valuable lessons are learned in tough times." - Howard Marks

Our investment management process is designed to provide well-diversified portfolios constructed with a methodology based on prudent risk management, asset allocation, and security selection. We help our clients navigate challenging markets by ensuring their short-term cash flow needs are met while managing the rest of their investments in a globally diversified portfolio.

Market volatility can be used to our advantage by tax-loss harvesting or reallocating to more attractive securities:

- **Tax-loss Harvesting**: Tax-loss harvesting is achieved by selling an investment with a loss and immediately purchasing a different security with similar (but not identical) exposure. The loss on the sold security can be used to offset taxable gains. Since we simultaneously sell a security to capture a loss and purchase a different holding with similar exposure, the client is never out of the market. We can capture losses during declines, and as the market recovers the new position also recovers PLUS the client has a tax-loss to offset future gains. Please see our **Client Question on Tax Loss Harvesting**.

- **Repositioning Portfolios**: Repositioning portfolios means that we can increase the overall equity allocation and/or we can reallocate among various asset classes. During a market selloff, portfolio equity allocations often fall below their target levels. For example, assume a portfolio is invested to its target allocation of 60% equities and then the stock market declines-10%. The new allocation would be about 54% or-6% below the target level. We can use the market decline as an opportunity to buy stocks at lower prices to bring the allocation back to the 60% target level. Furthermore, we can rotate to the equity asset classes that have become more attractive (for equities, we allocate across regions, countries, market caps, factors, styles, sectors, and industries). Keep in mind, some of the best buying opportunities occur during periods of market turmoil.

DISCLOSURES:

Content in this material is for general information only and not intended to provide specific advice or recommendations for any individual.

The economic forecasts set forth in this material may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

All indexes mentioned are unmanaged indexes which cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment. Past performance is no guarantee of future results.

The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Financial planning is a tool intended to review your current financial situation, investment objectives and goals, and suggest potential planning ideas and concepts that may be of benefit. There is no guarantee that financial planning will help you reach your goals.

Rebalancing a portfolio may cause you to incur tax liabilities and/or transaction costs and does not assure a profit or protect against a loss.

Likewise, it is important to remember that no investment strategy assures success or protects against loss. Asset allocation does not ensure a profit or protect against loss. There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not protect against market risk. All investing involves risk which you should be prepared to bear.