MH & ASSOCIATES • SECURITIES MANAGEMENT CORPORATION

INVESTMENT VIEWS

FEBRUARY 28, 2022

CRISIS 2022: Russia Invades Ukraine

Everyone understands that the past few years have been tumultuous and volatile, not just in the stock market but for life in general. Tragically, the world now finds its attention focused on Ukraine, as Russia has invaded the country and nations grapple with how to respond and what this could mean for peace in the world. Below, we offer some thoughts in regard to the impact for investors, actual market reactions to geopolitical events and even some opportunities the situation may present. While the focus of this newsletter is on investments, our thoughts and prayers are also with the people affected by these tragic events.

VOLATILITY REALIZED

In previous newsletters we have warned investors to brace for financial market volatility. While our reasons for expecting this volatility were different than what is actually causing it now, the fact is that market volatility is focused on the events surrounding the Russian invasion of Ukraine. While certainly many sectors of the equity market has been negatively impacted, there are some sectors that have fared well so far, including energy, industrial metals, precious metals and alternative energy sectors. Some of this is based on fear, while others are based on the growing realization that the western world needs to be materials and energy independent.

We are fortunate that our portfolios have significant exposure those areas mentioned above which has helped reduce the impact of general market volatility.

GEOPOLITICS AND THE STOCK MARKET

With the invasion of Ukraine by Russia we reviewed past geopolitical crises and stock market reactions for hints as to what investors might expect. On average, stocks were higher 1, 3, 6, and 12 months after the geopolitical shock. In fact, the odds of stocks being higher increases with the passage of time. Since World War II there have been 29 geopolitical crises. Of those, 5 of them generated a negative return one year later whereas the other 24 events produced an average positive return of just over 12%.

Investors should be prepared for additional volatility, but history seems to suggest that declines associated with geopolitical fears are generally temporary setbacks and present an opportunity to buy stocks at a discount.

OPPORTUNITIES AHEAD

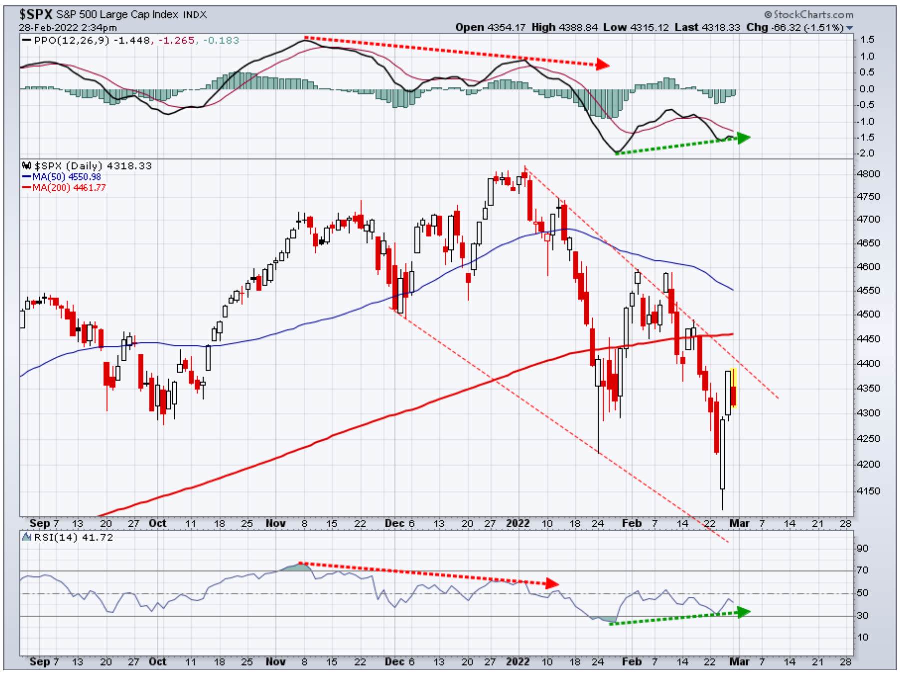
In a crisis it is helpful to stay positive and look ahead to changes that are likely to occur once the crisis ends. Our dependency on various other nations for many things such as energy, industrial metals and certain manufactured goods has revealed themselves to be serious liabilities. No where is this more apparent than European dependency of Russian natural gas. Even as of this writing Europe is taking delivery of Russian gas while it bombards Kiev with missiles...because it has no choice!

We believe that once this crisis is resolved, the United States and other allied nations will embark on a serious effort to attain self-reliance in the areas mentioned above, as well as other critical items such as medicine. This will not happen overnight obviously, but will likely span at least a decade. We welcome this shift, as we have observed this threat for many years and only regret that it took a crisis for it to be recognized.

Technically *Speaking*

The morning after the Russian invasion of Ukraine we were certainly prepared for the worse, especially after the futures markets were down significantly overnight. What happened that day was shocking and after hitting a new low, the S&P 500 recovered sharply to close up on the day and above the prior day's low. As positive as this was, the issue remains that the market is in a short term downtrend, that can only be negated by a close above the February highs. At the very least we want to see consecutive closes above the downsloping dotted red line.

There are some positives in our favor such as bullish divergences within derivatives of price and momentum. The bottom window displays the relative strength (RSI) of price and the dotted green arrow shows that when price hit a lower low on February 24th, then indicator did not confirm this with a lower low. This is a minor divergence to be fair and will need to see the absolute reading on the RSI to move above 50 to indicate momentum might be changing. Even should this occur, we expect the solid red line of the 200 day moving average to provide ample resistance. Further caution comes from the fact that we are still not registering sentiment levels that would indicate we have bottomed and there is simply too much uncertainty in the market at the moment to believe that volatility will move lower. In the meantime, until volatility subsides and the S&P can move above February highs, our bias has to remain on the bearish side.



CAUTION IN THE INTERMEDIATE TERM

In addition to our bearish short term view, our intermediate term view has taken a turn for the more cautious as well. A weekly sentiment indicator we discussed in our August newsletter that measures market breadth (advancing stocks versus declining stocks) is reaching levels it has not seen in many years. In fact, it is well below levels hit during the COVID lows and still trending down solidly. Should it cross the zero level, it would be the first time since a minor drop below in 2016 and the harsh penetration of the zero level during the 2008 credit crisis. We believe this caution is warranted, but still believe we are in a secular bull market.

GOLDS ADVANTAGES SHINE DURING A CRISIS

Gold and other precious metals have begun what appears to be a significant rally as geopolitical fears overtake the world. To be sure, this is not the only catalyst that is causing the shiny yellow metal to rise, however it is the latest. Investors seek out gold for protection from risk as it is a physical form of wealth storage with over 5000 years of history behind it and it is universally accepted. Gold should also do well for inflationary reasons, as again it does have a history of preserving purchasing power over time. Some investors distain gold as a relic of the past. During periods of crisis, precious metals continue to play an important role in helping to reduce portfolio volatility and protect purchasing power against inflation.

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