

War...Maybe

Russia is on the move again. In the ongoing quest to recapture Soviet-era glory, Putin and the Russian military appear ready to invade Ukraine on several fronts. The land objective for Russian forces appears to be the Donetsk and Luhansk regions in the southeastern part of the country. Troops and artillery are massed at several points around Ukraine's borders, effectively surrounding the country. Putin also has an interesting timing mechanism. His two previous invasions in the same region, Georgia, and Crimea, came right around the Olympics.

This morning's accusations of mortar rounds being launched looks like a false-flag attempt. Creating a pretext to invade is about as old a tactic as the siege. We are reminded of the German fake attack on a German radio tower in 1939. The agents were dressed as Polish soldiers. Hitler invaded Poland the next day.

What does this mean for stocks? Events can temporarily rattle markets but rarely change the long-term trend. In general, the prelude and start of an event provides the most drama for markets. Markets like certainty and uncertain outcomes cause humans to be cautious. Markets also have an impressive track record of looking ahead six to twelve months into the future and deciding whether the trend may change.

But Wait

There's more. The market's trend before an event, whether war, natural disaster, or pandemic, tends to control the outcome more than the event. There is a human bias to think that "this time it is different" after an event starts. Pandemics are unique in this regard; they do not change trends but do accelerate them.

Back to guns. There are times when events are completely overwhelmed by the economy. 2008 is an excellent example. Russia's August 1 invasion of Georgia occurred after a 15% drop in the S&P 500 as the housing crisis was beginning to take hold. The market's primary trend continued through the 12-day war, ultimately ending in a 57% slide from its October 2007 highs. The bursting housing bubble here and abroad simply overwhelmed the war news.

History Tour

The last century's war events show how the primary trend usually controls after the event. In the 33 war related events compiled by Ned Davis Research, shown in Table 1, only five saw the Dow Jones Industrials lower six months later. The 126 days referenced in the table refer to trading days – not calendar days. Note that the first four were associated with World Wars and the fifth was the Gulf war – driven by oil supply fears.

A quick tour of the S&P 500 back to the early sixties shows similar results. Four times since 1964 the S&P 500 was lower one month after the start of a conflict. In all four cases the index was higher some six months later. The lone exception was 2001, when the economy was already in recession.

Comment

We have no idea what Putin may do in the coming days or months. Clausewitz said that “war is politics by other means.” The ongoing internet attacks on Ukrainian banks and utilities, it could be argued the war started years ago. If more tax revenue is the real issue, then the recent rise in oil prices has greatly benefited Russian government coffers, at the expense of consumers everywhere. If reminding Europe how dependent they are on Russian natural gas, surely, he has their attention.

For our portfolios, a conflict may present a buying opportunity. However, we believe that the Fed, interest rates and inflation will have greater impact on our indicators than military action.

Table 1

Event	Event Date	DJIA	Percentage	Change	S&P 500	Percentage	Change
		%Gain 22	/Loss 63	Days 126	%Gain 22	/Loss 63	Days 126
WWI - Assassination in Sarajevo	6/28/1914	-0.5	-1.1	10.2			
Austria declares war on Serbia	7/28/1914	-4.2	-6.4	7.1			
WWI - Exchange closed	12/12/1914	8.1	5.5	20.4			
WWI - U.S. declares war on Germany	4/6/1917	-2.3	1.2	-11.8			
WWI - U.S. troops arrive in France	6/26/1917	-5.1	-14.4	-24.4			
WWI - Austria Hungary Surrender	11/4/1918	-3.3	-6.1	6.8			
WWI - Germany Surrenders	11/11/1918	-5.3	-7.3	3.9			
WWII - Germany invades Poland	9/1/1939	13.9	12.3	8.1			
WWII - Germany invades France	5/10/1940	-23.6	-17.9	-9.9			
WWII - France Surrenders	6/22/1940	0.3	9.4	7.4			
WWII - Pearl Harbor	12/7/1941	-2.4	-9.6	-16			
WWII - D Day	6/6/1944	4.8	5.2	4.4			
WWII - Germany Surrenders	5/7/1945	0.8	-3	12			
WWII - Hiroshima	8/6/1945	8.3	13	24.8			
WWII - Nagasaki	8/9/1945	9.8	16.7	21.5			
WWII - Japan Surrenders	8/14/1945	8.3	15.5	21.9			
Korea - North Korea invades South Korea	6/25/1950	-8.9	1	2.2			
Korea U.S. Ground troops arrive in Korea	6/30/1950	2.5	9.3	10.5			
Korea - Cease Fire Signed	7/27/1953	-0.9	2.1	8.3			
Vietnam - Gulf of Tonkin	8/2/1964	0.3	3.7	7.4	-1.2	2.02	5.35
Vietnam - U.S. Marines sent	3/8/1965	-0.4	0.6	0.5	-0.32	0.06	1.42
Vietnam - North Vietnam overtakes Saigon	4/30/1975	3.6	2.7	4.4	8.73	15.75	5.43
Gulf - Iraq invades Kuwait	8/2/1990	-9.8	-15.6	-6.4	-7.71	-10.5	4.87
Gulf - U.S. ground troops arrive in Saudi A	8/9/1990	-4.4	-9.1	3.5	-5.12	-6.55	8.66
Gulf - U.N. authorizes force	11/29/1990	3.9	13.7	18.4	1.45	18.88	21.7
Gulf - Desert Storm begins	1/17/1991	17	19.8	18.7	11.33	17.14	16.74
Gulf - Ground assault begins	2/24/1991	0.9	0.4	4.1	2.91	2.55	7.8
Gulf - Kuwait Liberated	2/27/1991	1.7	3.3	6.1	2.03	2.65	7.81
Afghanistan - Initial Bombing	10/7/2001	5.2	11.8	11.9	4.15	6.26	5.32
Afghanistan - Fall of Kabul	11/12/2001	3	2.7	7.2	1.65	4.23	-2.73
Iraq - Use of Force Authorized	10/10/2002	17.2	20.4	12.8	11.3	15.38	9.02
Iraq - US Invasion	3/20/2003	0.8	12.4	15.5	2.05	13.59	16.33
Iraq - Fall of Baghdad	4/12/2003	5.4	11.9	17.9	8.52	14.95	18.6
Mean		1.4	3.1	7	2.8	6.9	9.0
Median		0.8	2.7	7.4	2.0	5.2	7.8
Min		-23.6	-17.9	-24.4	-7.71	-10.5	-2.73
Max		17.2	20.4	24.8	11.33	18.88	21.7
Number of observations				33			14

Days = Market Days
Performance calculated from day prior to event date

Source: Dow Jones Industrials from Ned Davis Research, Inc.
S&P 500 from S&P Capital IQ

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