

Wealth Talk

The multiple impacts of the conflict in Ukraine

March 16, 2022

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Block #1



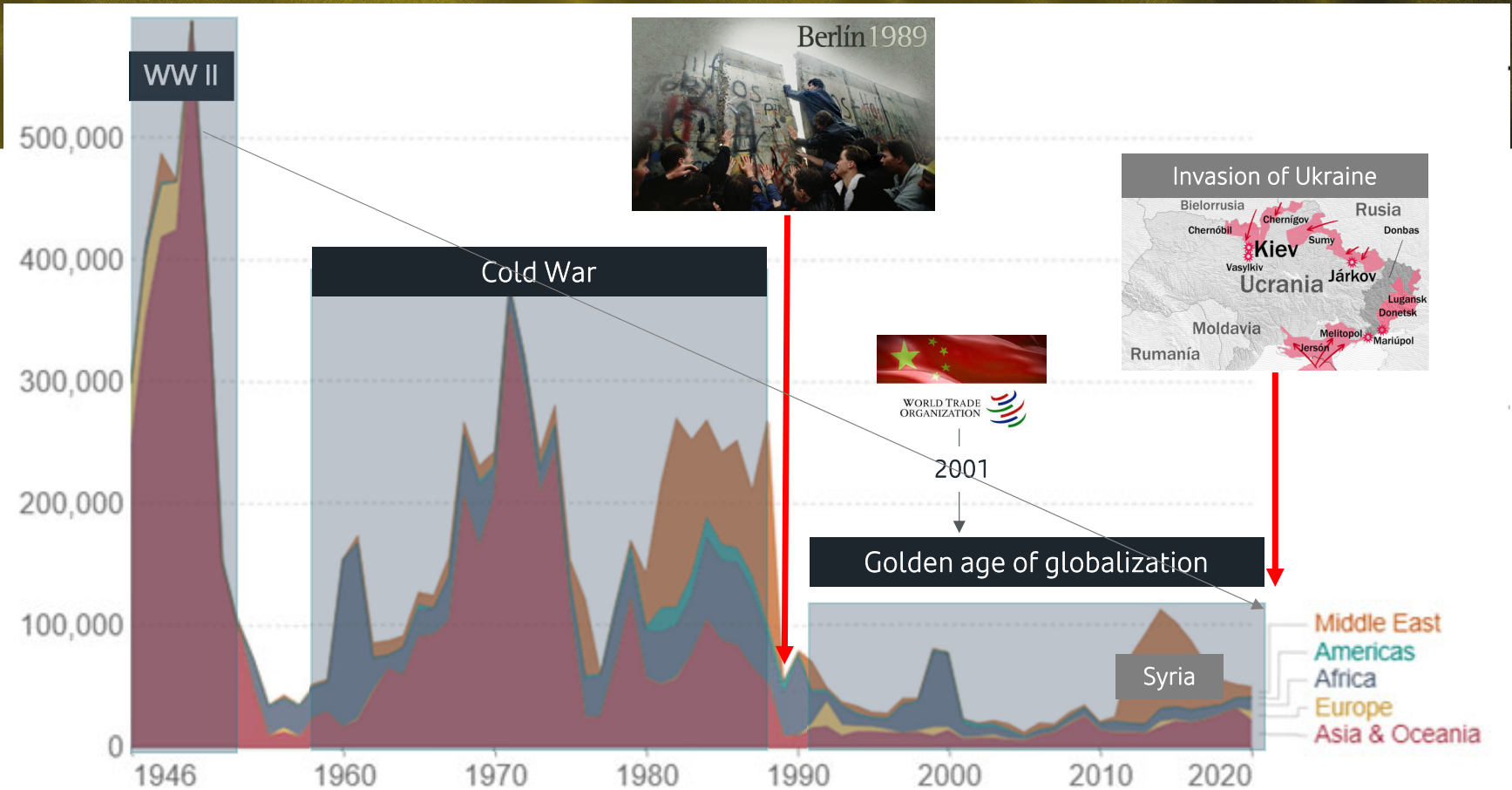
Geopolitical Risk



A historical overview of geopolitical risk events

Number of violent casualties in armed conflicts between States

Source: Our World in Data (based on UCDP)



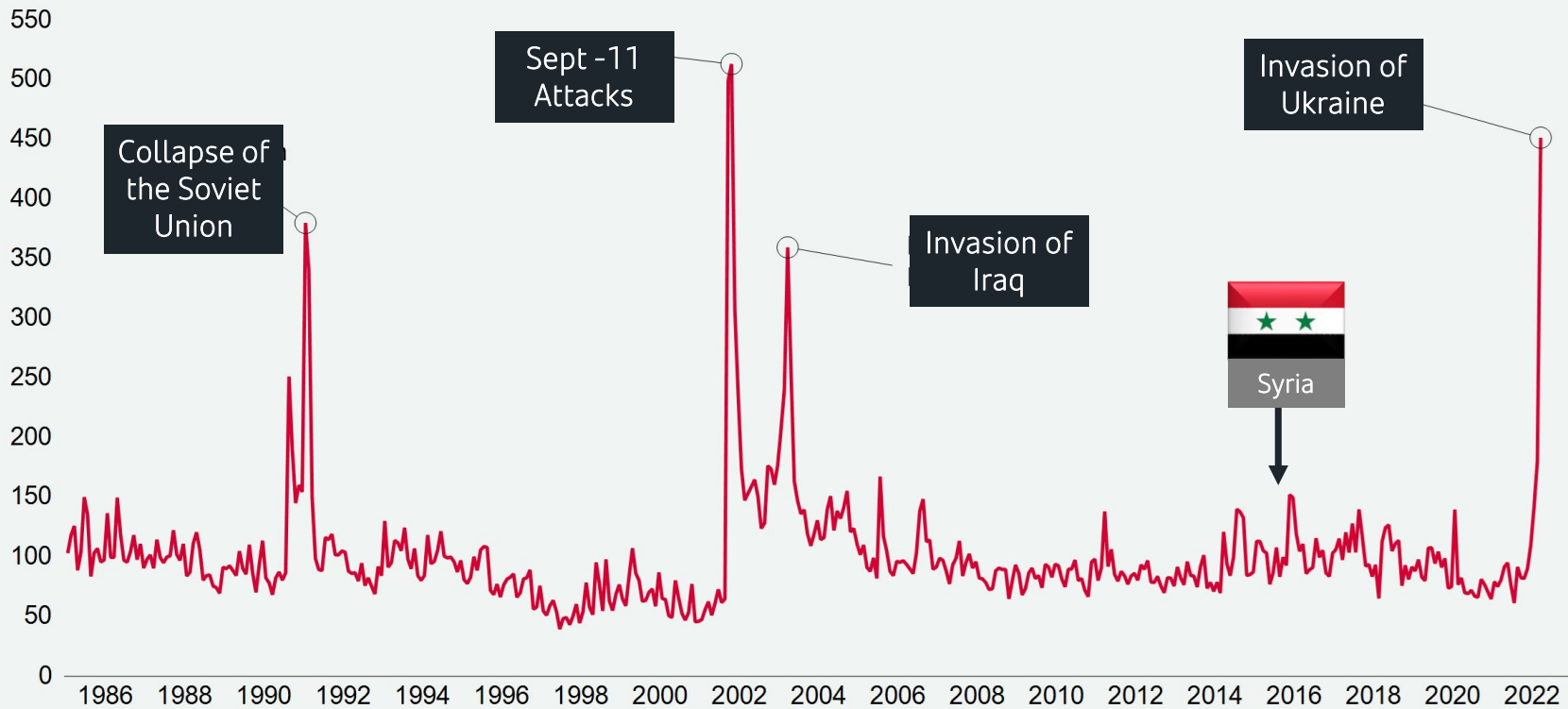


Level of geopolitical severity of the conflict in Ukraine

Source: www.iacoviello.com.

Extraordinary spike in global geopolitical risk

— World, Economic Policy Uncertainty, Geopolitical Risks (GPR), Geopolitical Risk Index, Total, Index



Caldara and Iacoviello's GPR index

reflects the results of automated text searches in the electronic archives of 10 newspapers: Chicago Tribune, Daily Telegraph, Financial Times, The Globe and Mail, The Guardian, Los Angeles Times, The New York Times, USA Today, The Wall Street Journal and The Washington Post.



The impact of geopolitical risks on the markets

Source: Own elaboration

Pearl Harbor	Korean War	Suez Canal crisis	Missile crisis in Cuba	Vietnam War	Oil Embargo	Crisis Iran	War from Gulf	9/11 Attacks	Iraq War	11M Madrid	Syria / N. Korea	Average impact
1941	1950	1956	1962	1968	1973	1979	1990	2001	2003	2004	2017	

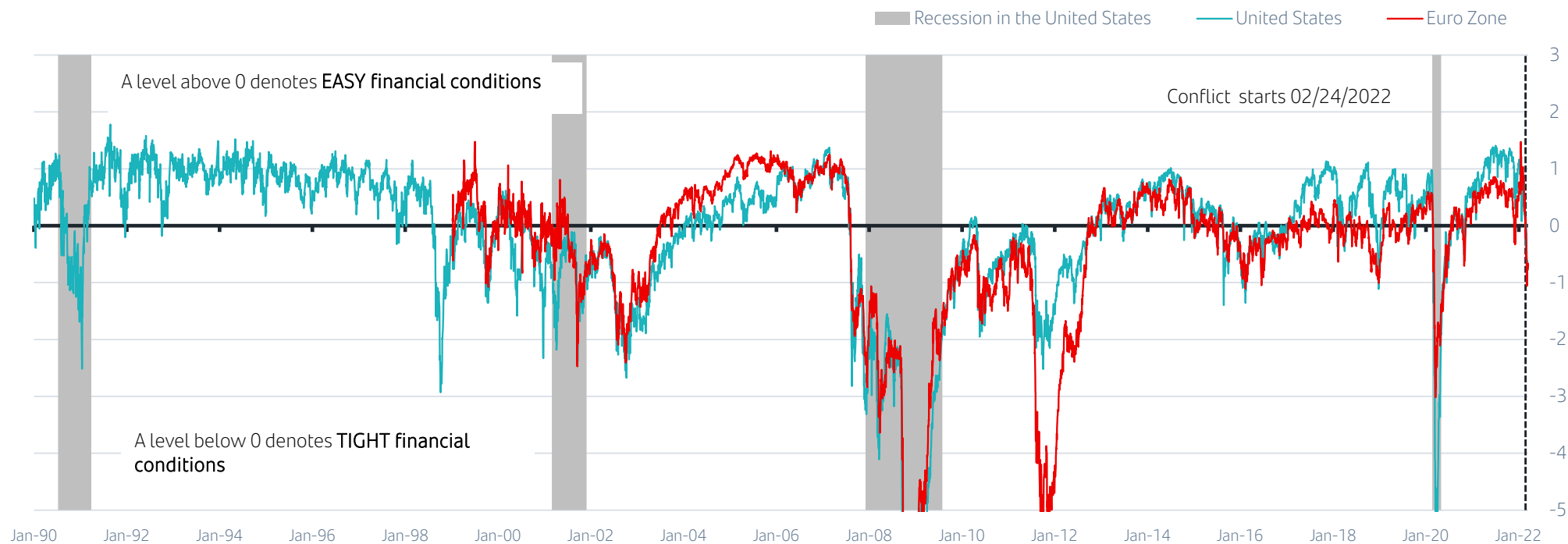
Market impact (S&P500)	Initial drawdown (maximum DD)	-18%	-8%	-21%	-4%	-7%	-44%	-17%	-14%	-32%	-5%	-8%	-10%	-16%
	Subsequent impact (revaluation 1 year later)	-0%	11%	-10%	30%	10%	-35%	26%	28%	-17%	27%	8%	14%	8%
	GDP decline (year-on-year change)			-5%			-6%			-3%				
				Energy Crisis			Energy Crisis			Dot-com crisis				



Variables to watch: volatility and financial conditions

Bloomberg Financial Conditions Index

Source: Bloomberg and own elaboration. Data as of March 15, 2022



Block #2

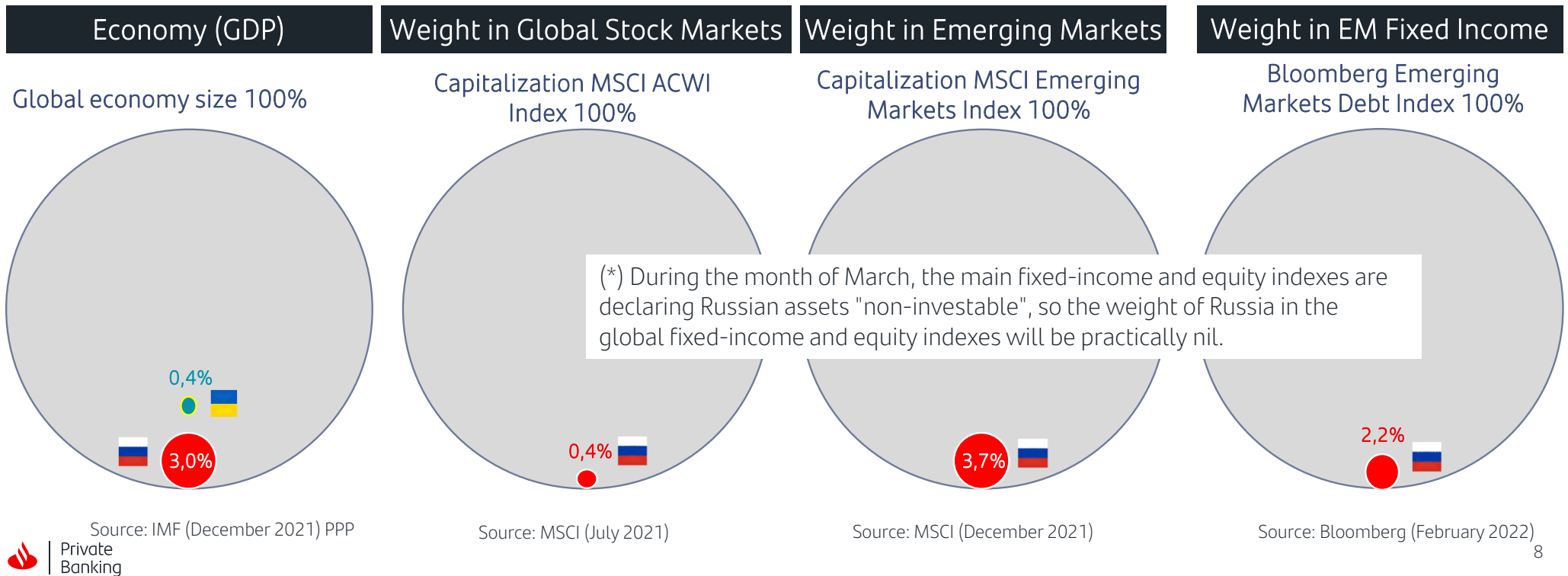


Energy Risk



Importance of Russia and Ukraine in economy and markets

Russia and Ukraine have a relatively small weight in the world economy and markets.

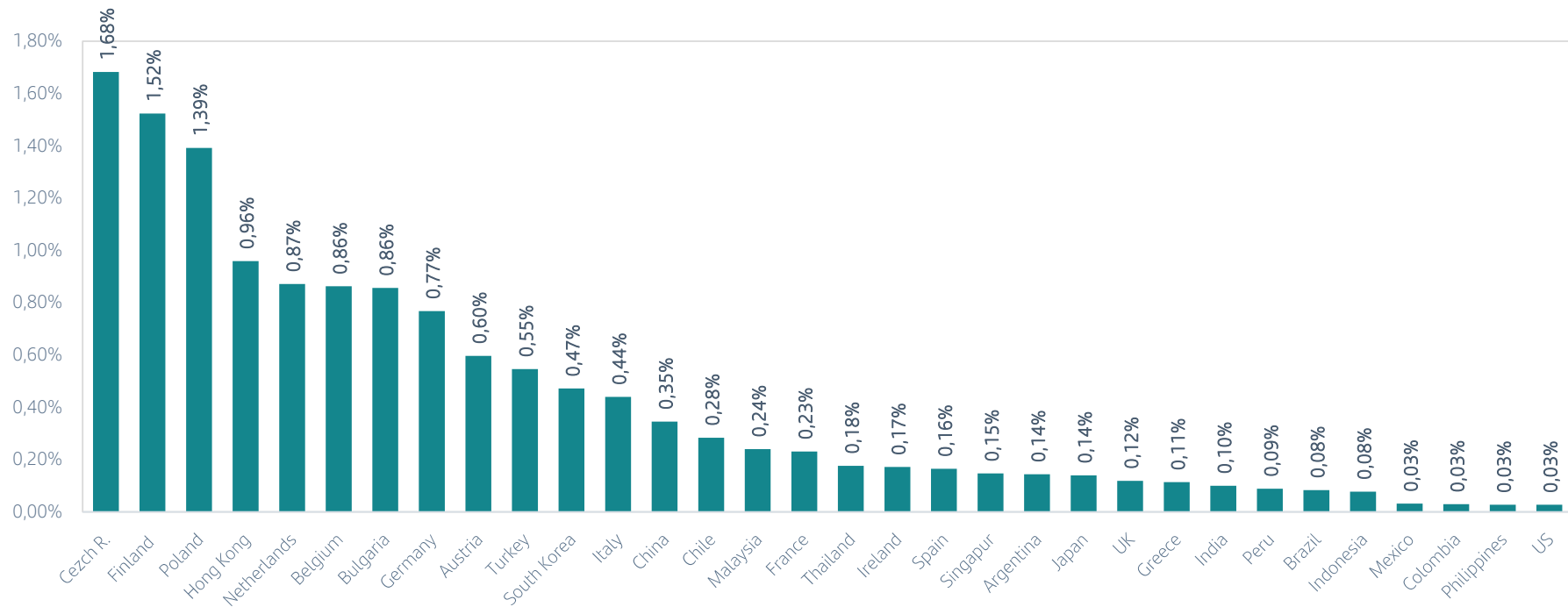




Russia's impact on international trade

Source: International Monetary Fund (IMF) and own elaboration.

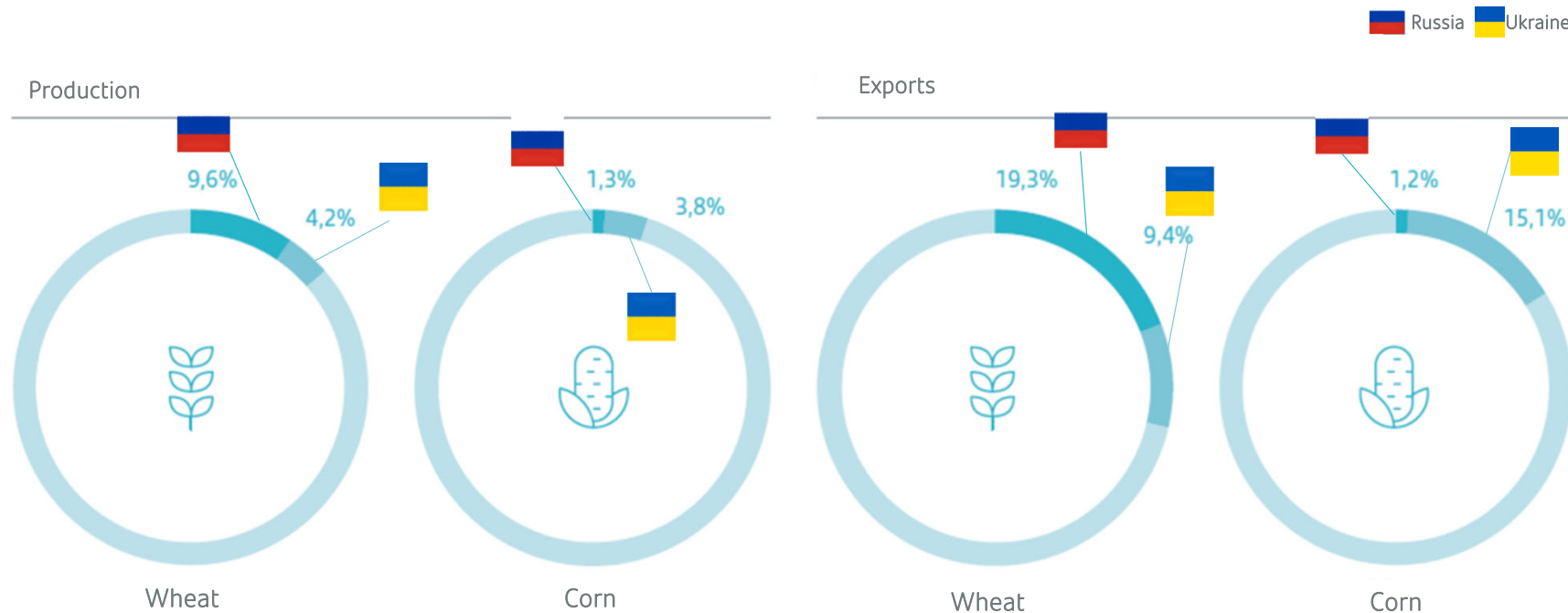
Weight of exports to Russia as % of GDP





Importance of Russia and Ukraine in agricultural production

Russia and Ukraine are the world's leading grain exporters



Source: United States Department of Agriculture (USDA)

+46%YTD



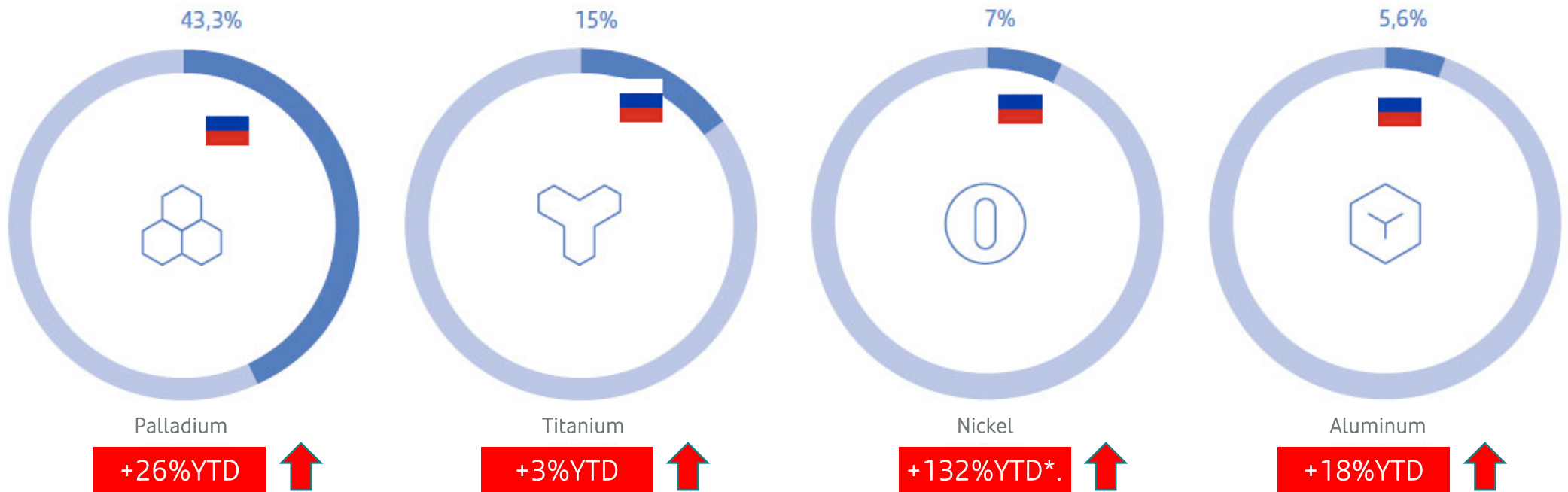
+24%YTD





Importance of Russia in metal production

Russia is one of the world's leading metal producers



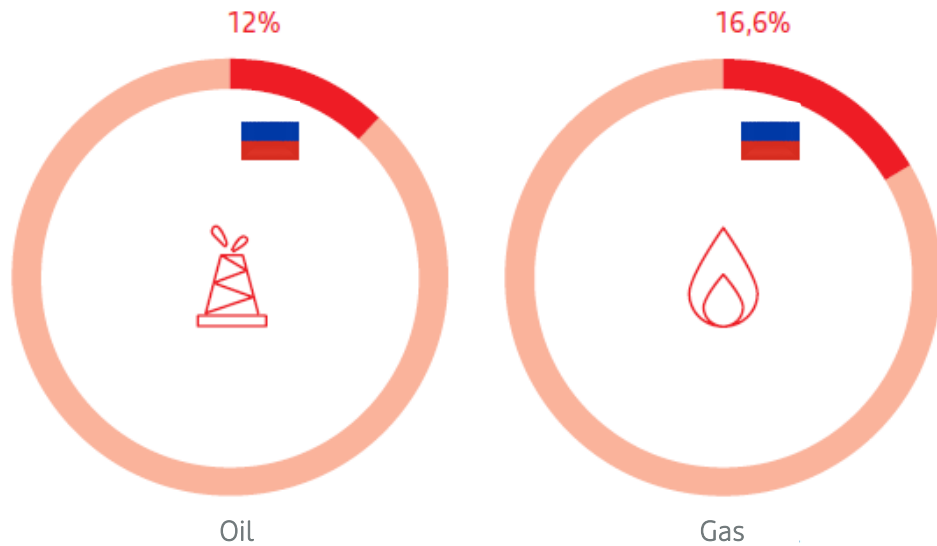
Source: Statista, mineriaenlinea.com.



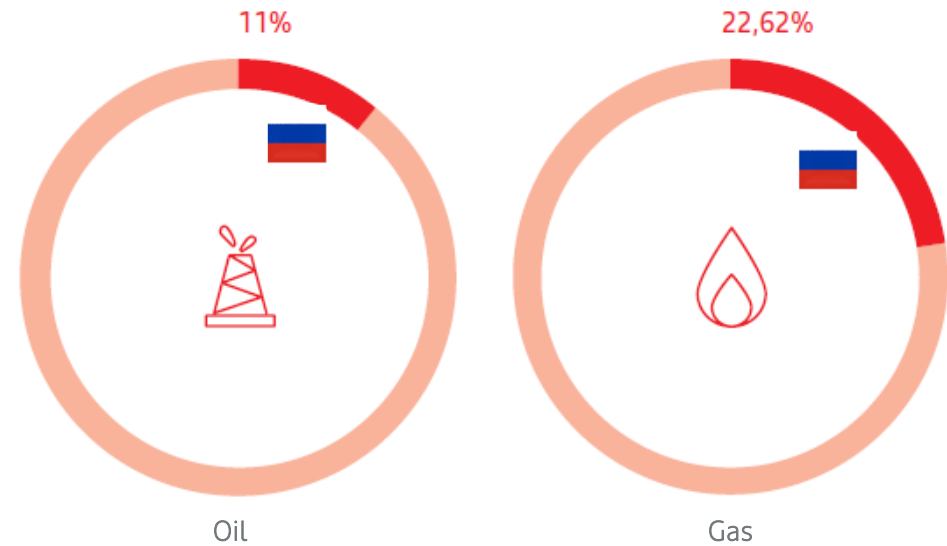
Importance of Russia in energy production

Russia is the world's largest exporter of energy (oil and gas).

Production



Exports



Source: International Energy Agency and BP



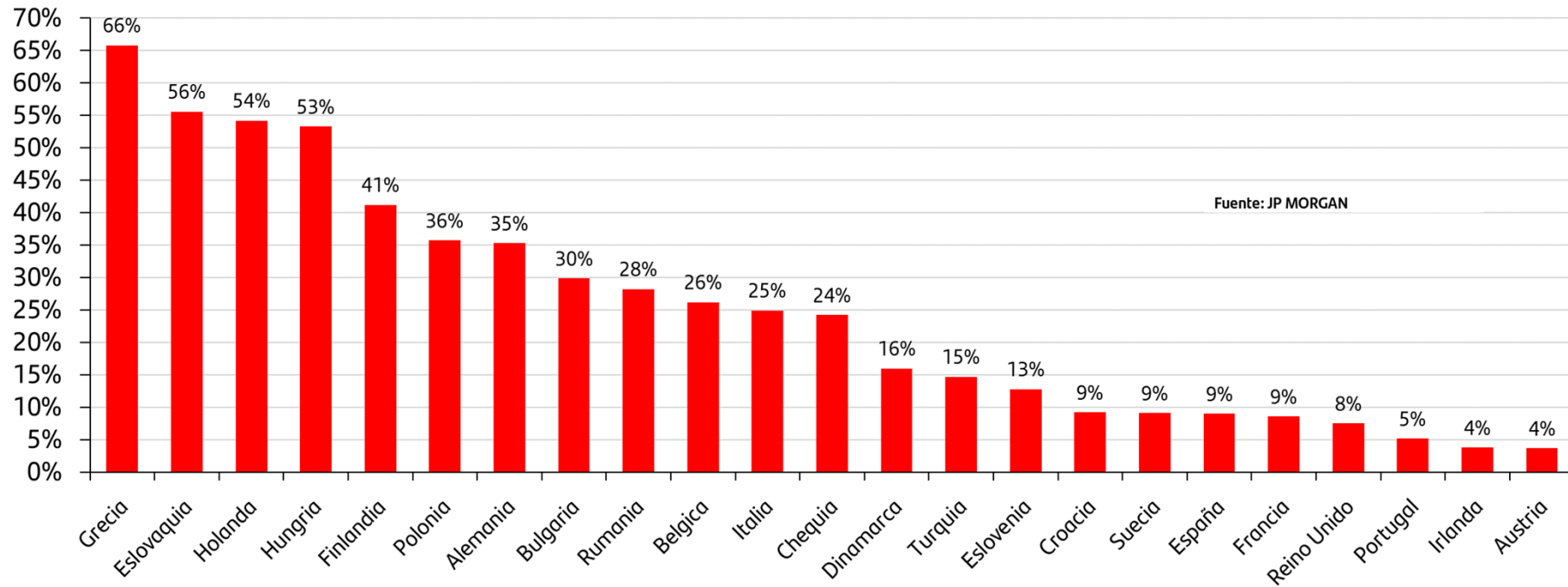
*YTD: Revaluation for the year-to-date 2022. Source: Factset. European benchmark TTF gas, American benchmark Henry Hub NYMEX. Data as of March 15, 2022.





Europe's energy dependence on Russia

Energy dependence on gas, coal and oil from Russia



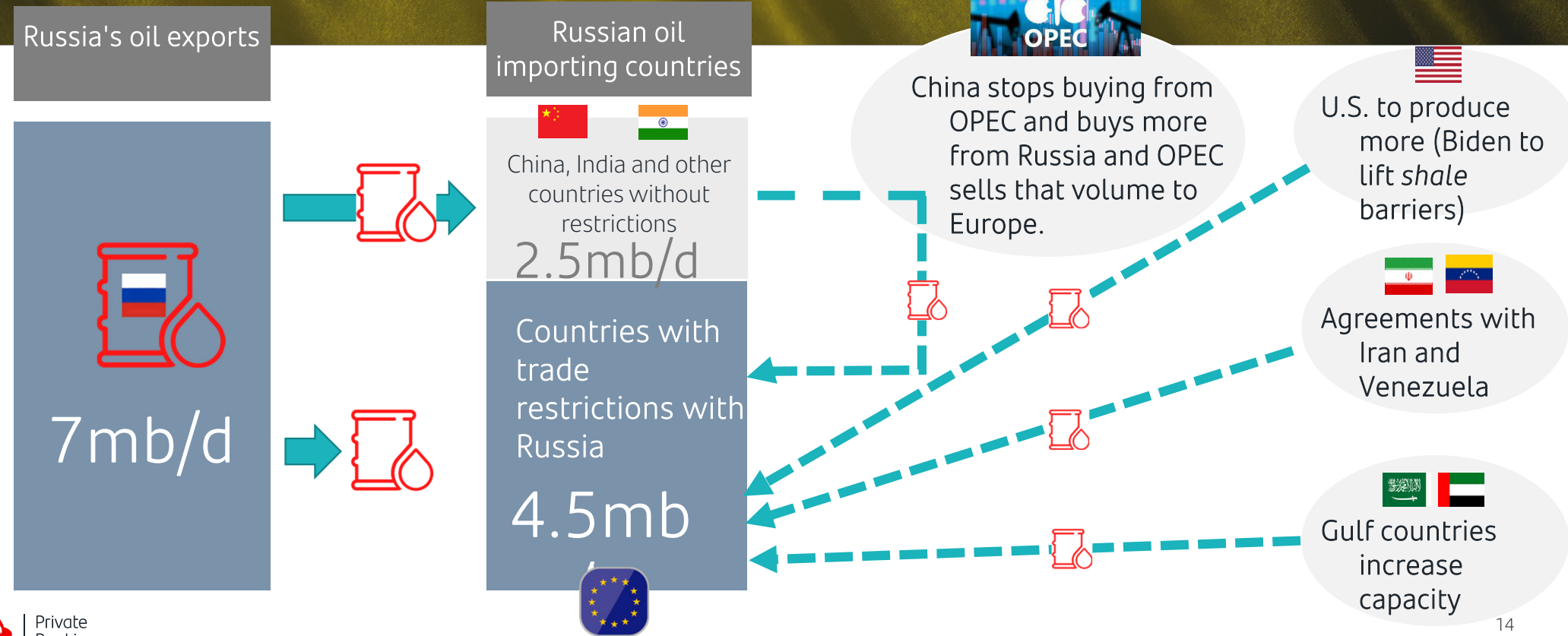


Russian oil substitution: options for Europe

Source: Own elaboration

Redirection

Increase in production

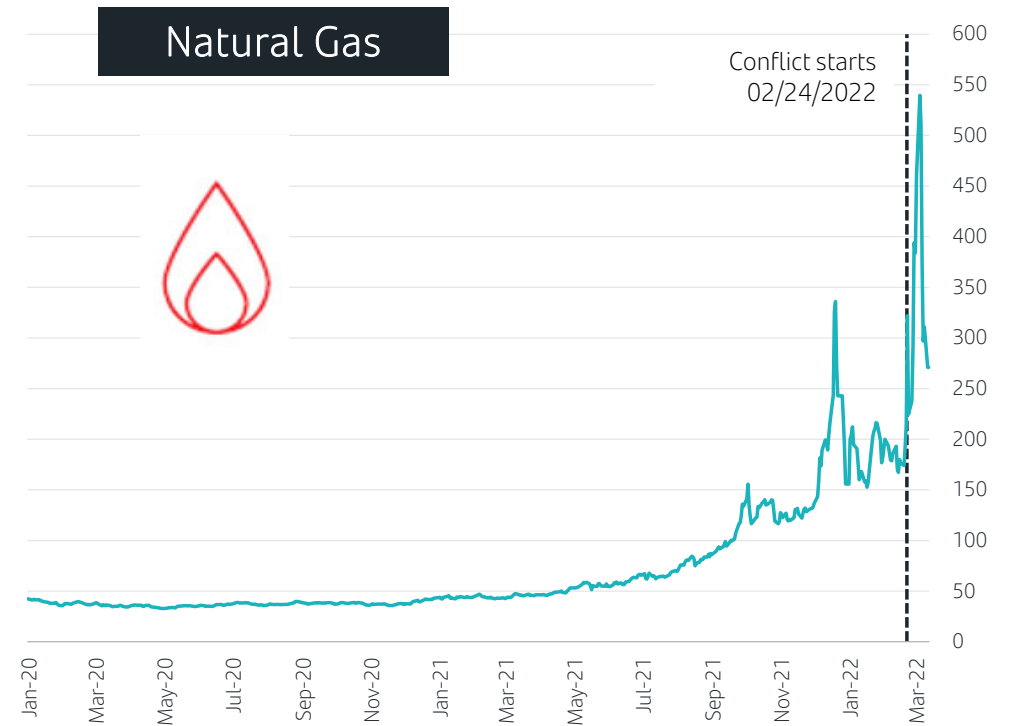
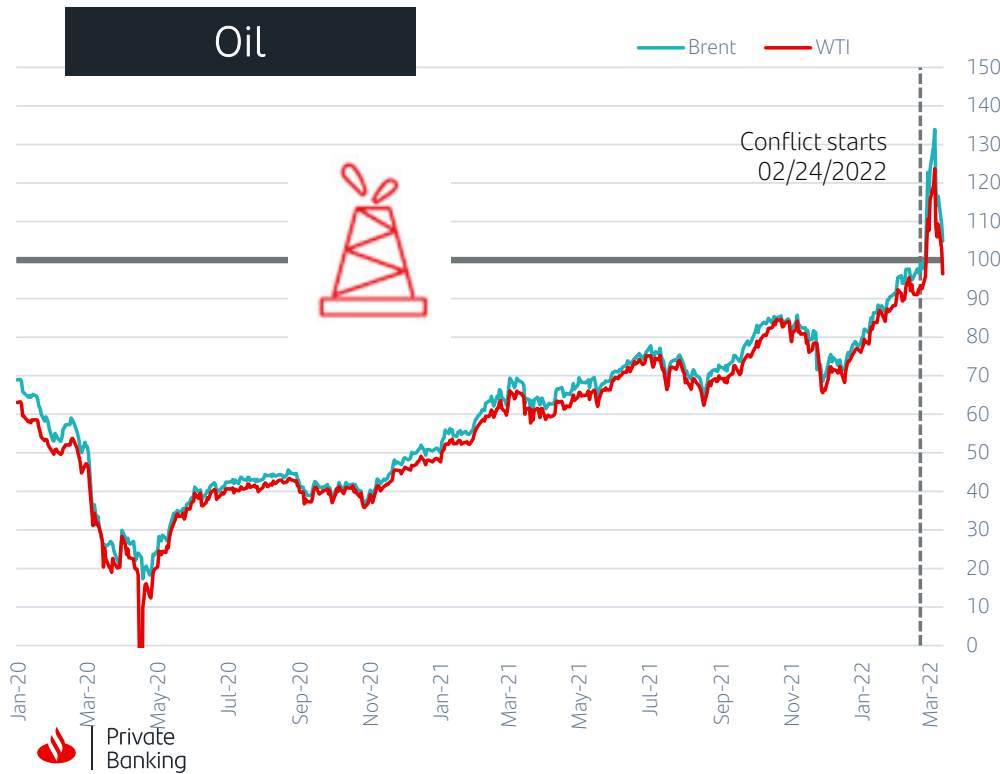




Variables to watch: gas and oil prices

Oil and natural gas prices in dollars

Source: Bloomberg and own elaboration. Data as of March 15, 2022

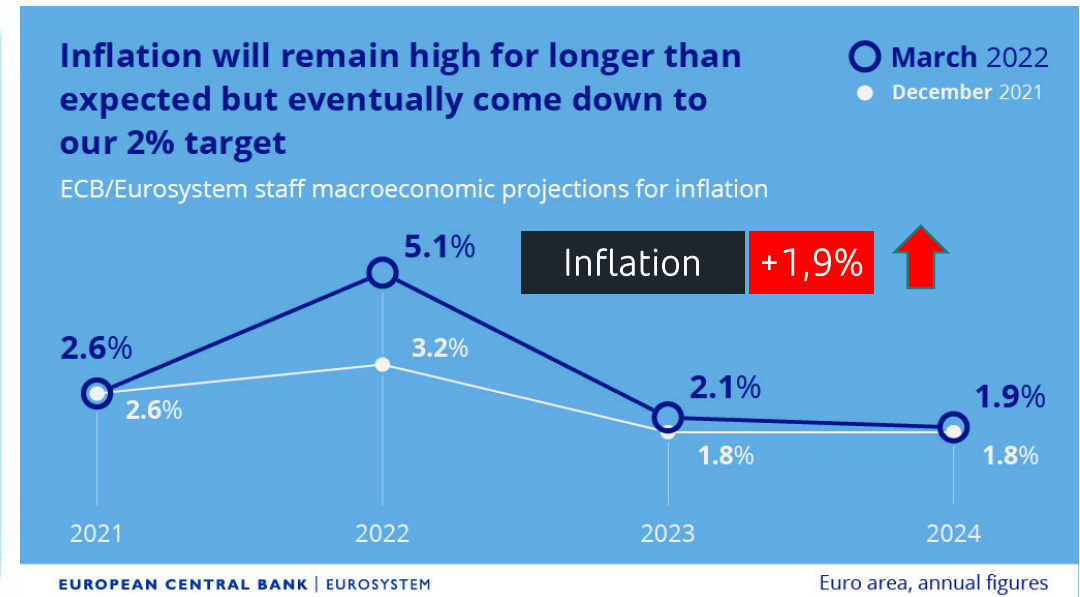
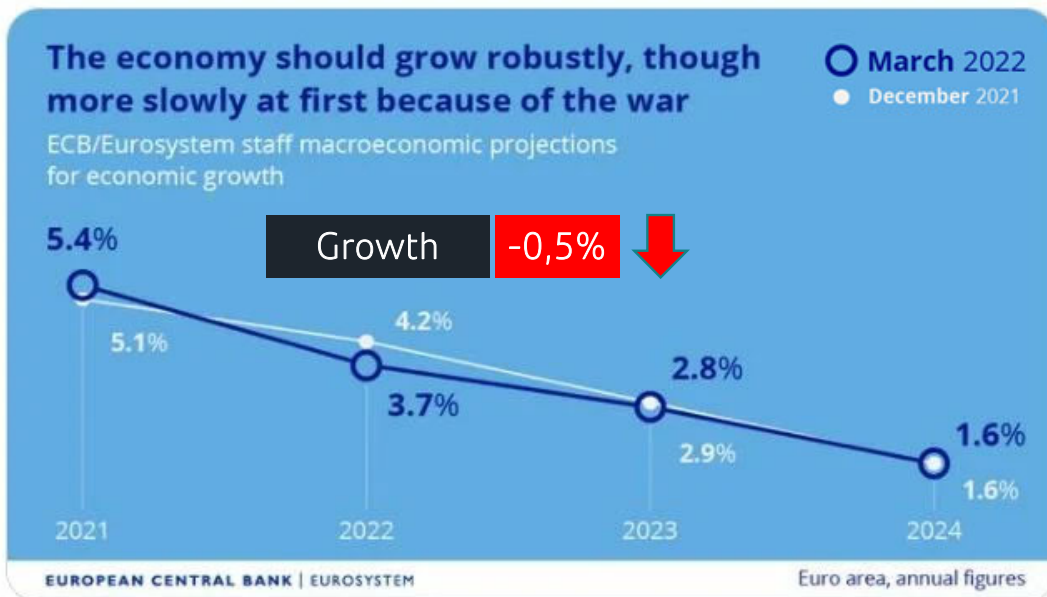




Estimated impact on growth and inflation in the Euro Zone



Downward revision of growth and upward revision of inflation by ECB



Source: European Central Bank (ECB)

Block #3



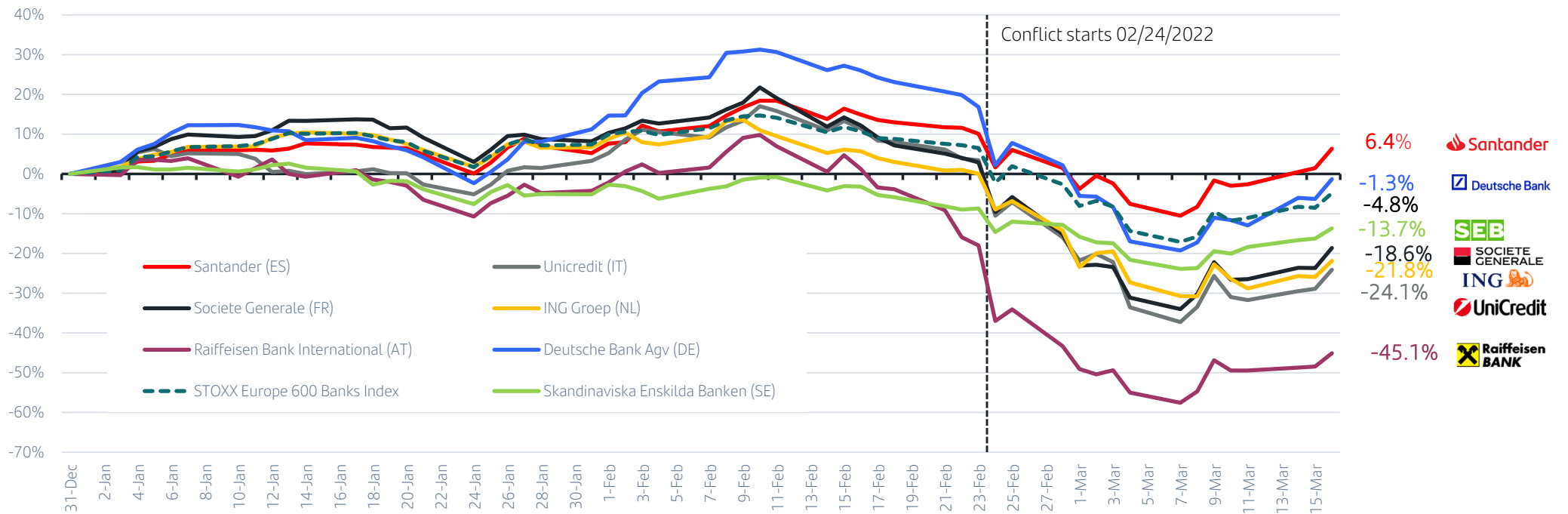
Financial System



Impact of the conflict in Ukraine on European banks

Variation (%) European Banks' share prices Year 2022

Source: Bloomberg and own elaboration. Data as of March 16, 2022

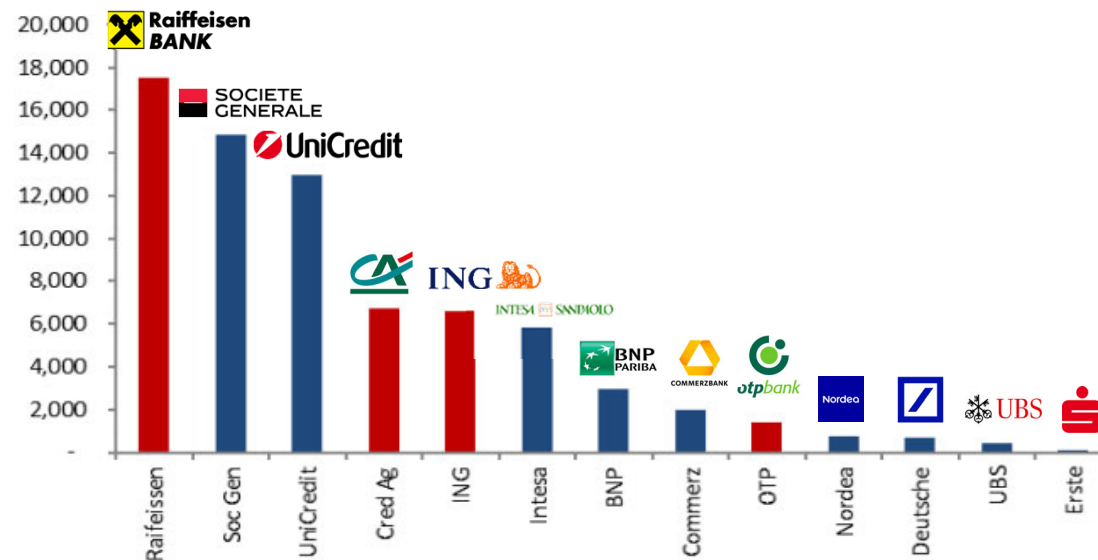




European banking exposure to Russia and Ukraine

Exposure via European bank loans to Russia and Ukraine (Mn€)

Selected banks' loan exposures to Russia and Ukraine (€mns)





The level of capitalization of European banks is very solid

Current levels of European bank capital strength are much higher than in previous crises.



Higher capital levels of European banks per risk unit



Variables to be monitored: Risk premium financial institutions

Perception of risk (CDS) of European financial institutions

Source: Bloomberg and own elaboration. Data as of March 15, 2022



Block #4



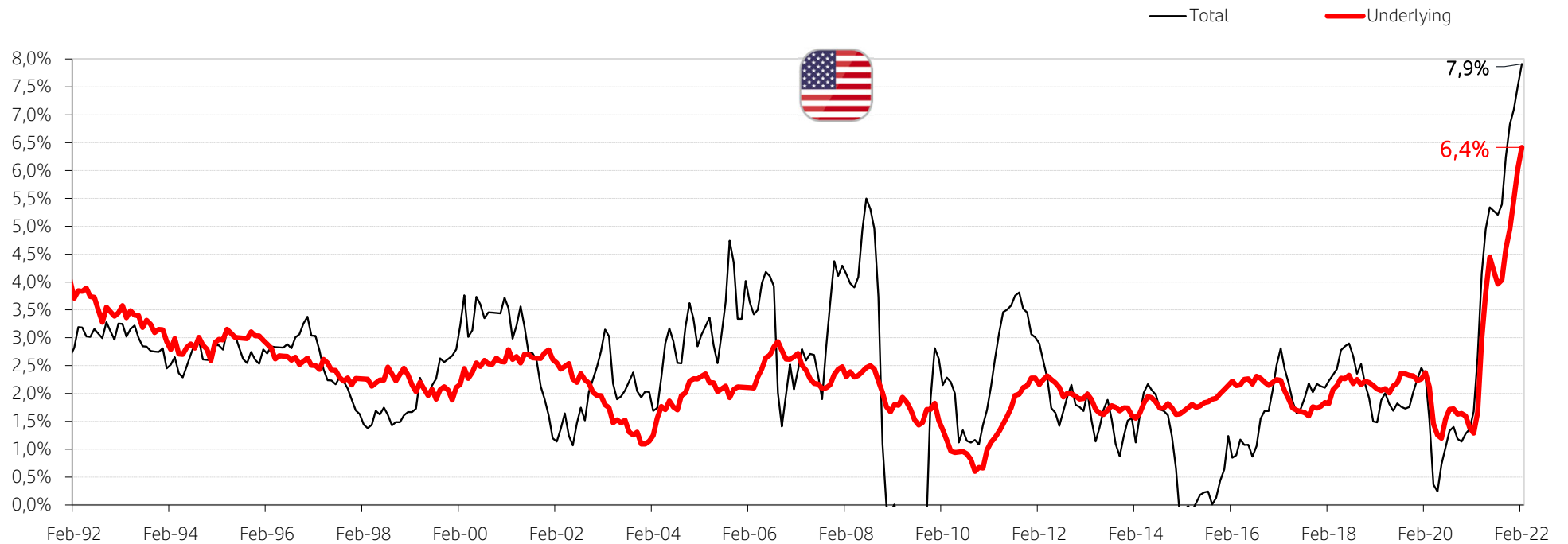
Inflation Risk



Higher and more persistent inflation than expected

Inflation levels have reached levels not seen since the 1980s.

Source: Bloomberg and own elaboration



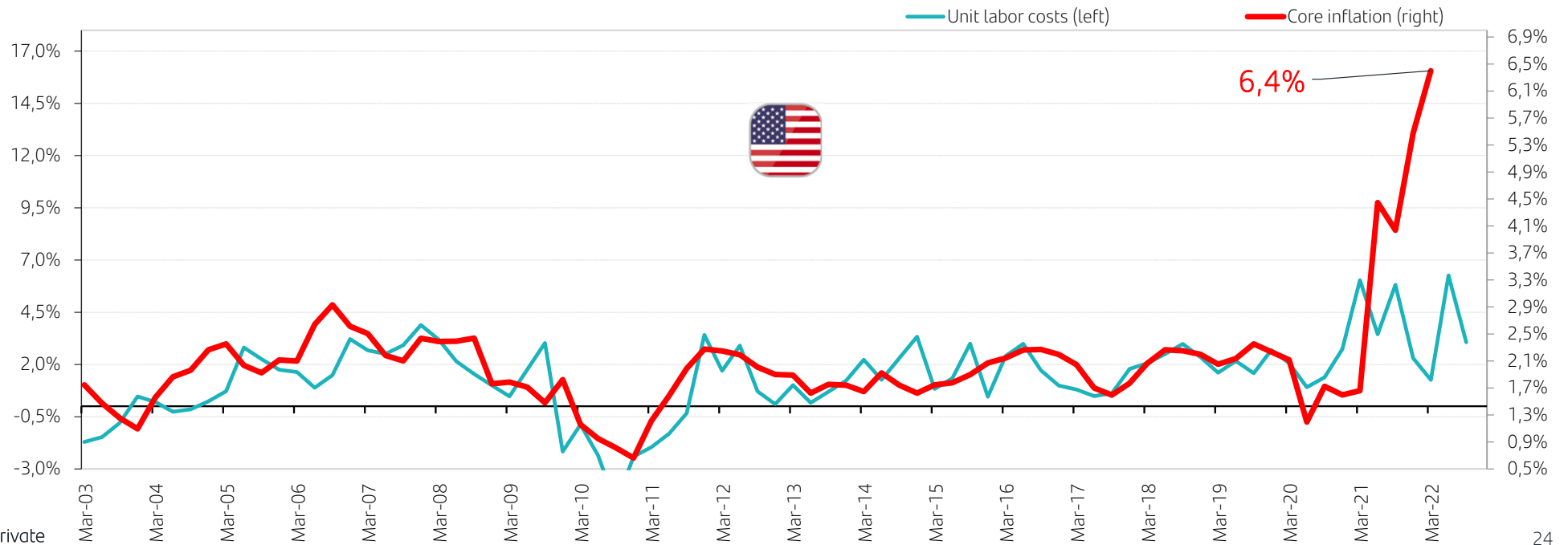


Higher inflation but no second wave effect

Labor costs are not rebounding at the same rate as inflation

Source: Bloomberg and own elaboration

Unit labor costs and core inflation. YoY



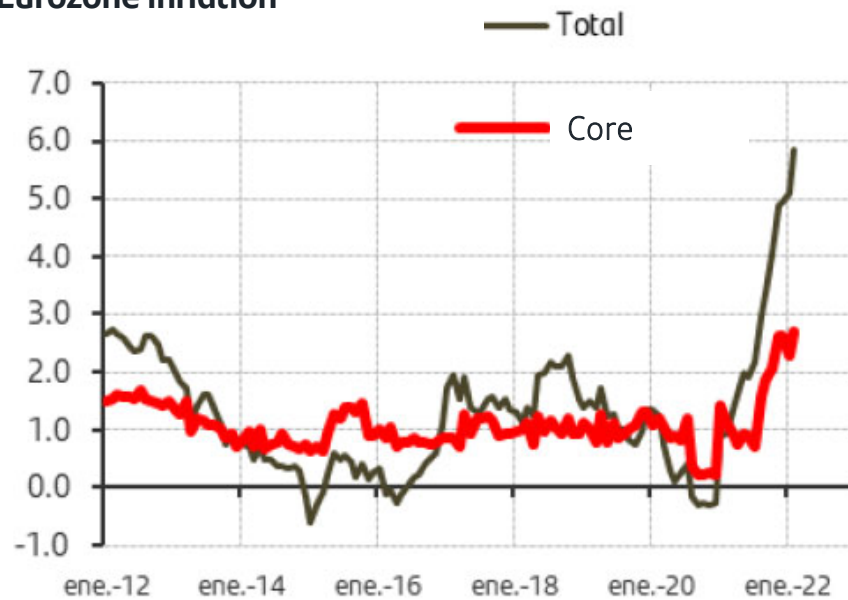


Higher and more persistent inflation than expected

The upturn in inflation in the Eurozone has several fronts

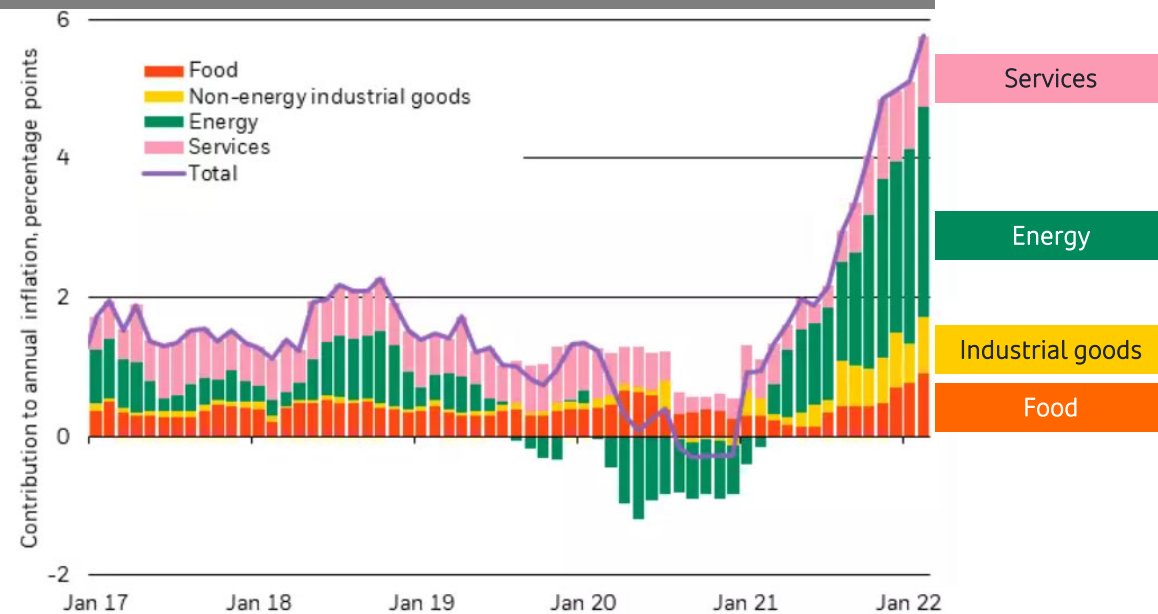
Source: Refinitiv and Blackrock Investment Institute

Eurozone inflation



Fuente: Refinitiv

Breakdown of inflation in the Eurozone by contributors



Source

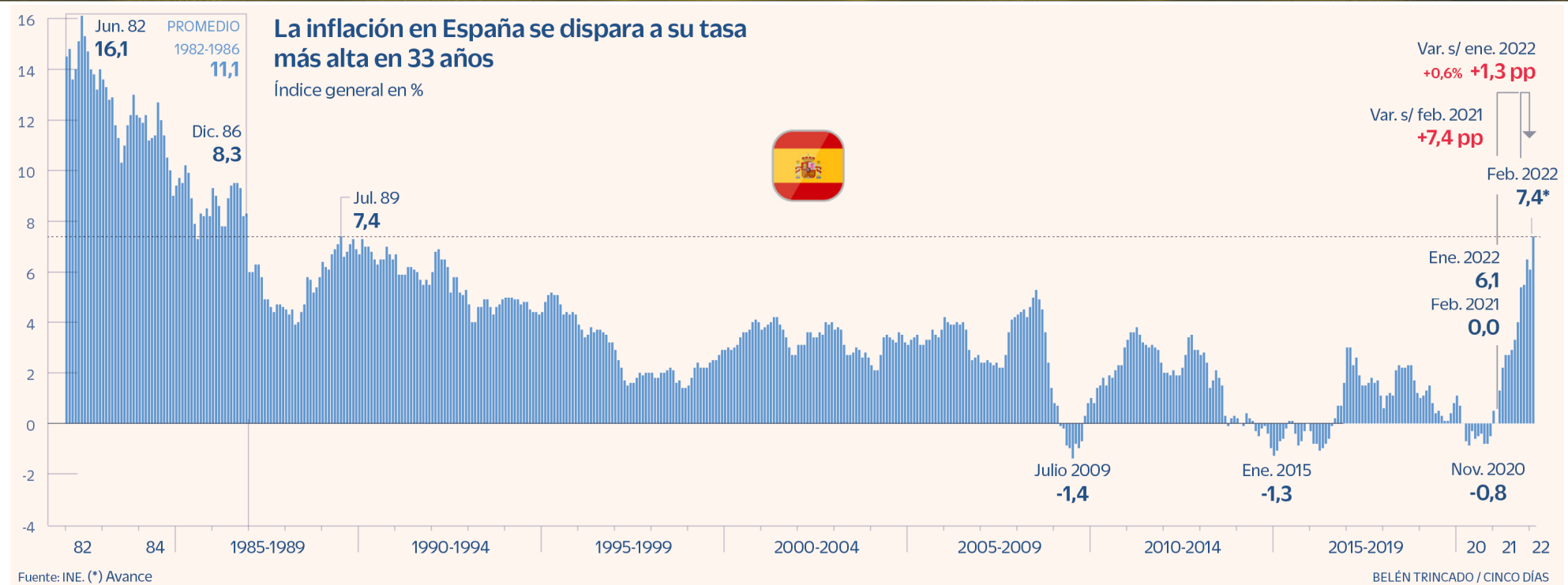
Sources: BlackRock Investment Institute, with data from Haver Analytics, March 2022. Notes: the chart shows the contribution of different goods and services to headline inflation in the euro area. The bars denote percentage point contributions to headline inflation.



Higher and more persistent inflation than expected

Inflation levels have reached levels not seen since the 1980s.

Source: National Institute of Statistics and Cinco Días

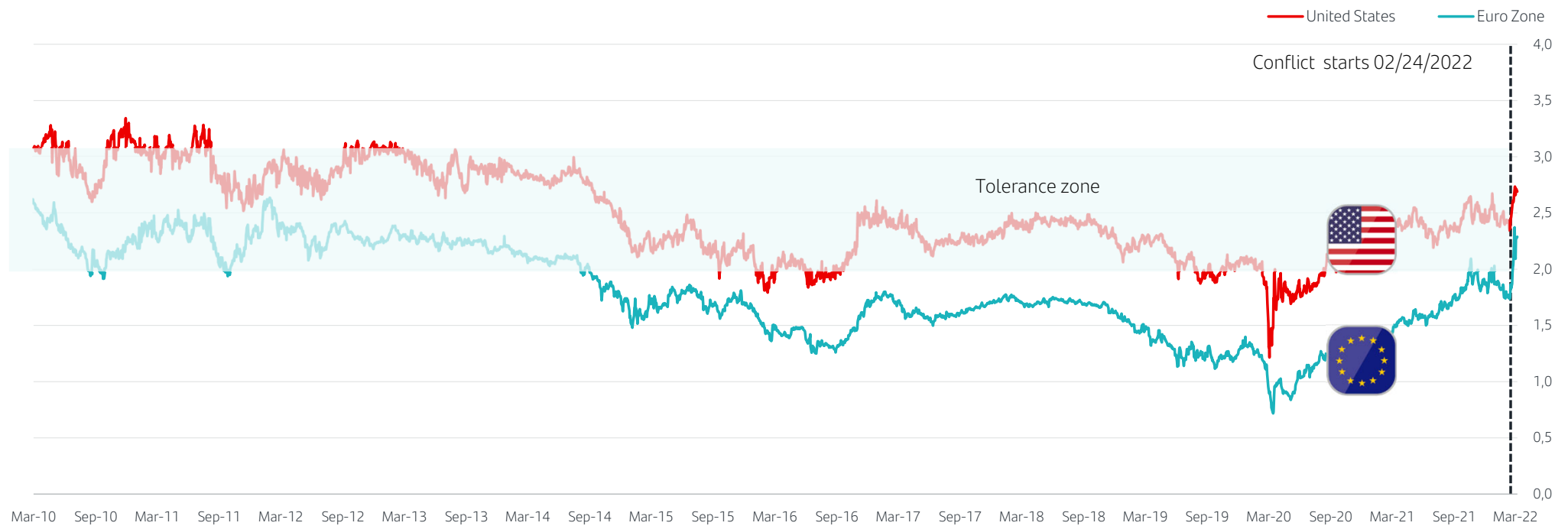




Variables to watch: inflation expectations

Long-term inflation expectations

Source: (5 years within 5 years) Bloomberg and own elaboration. Data as of March 15, 2022



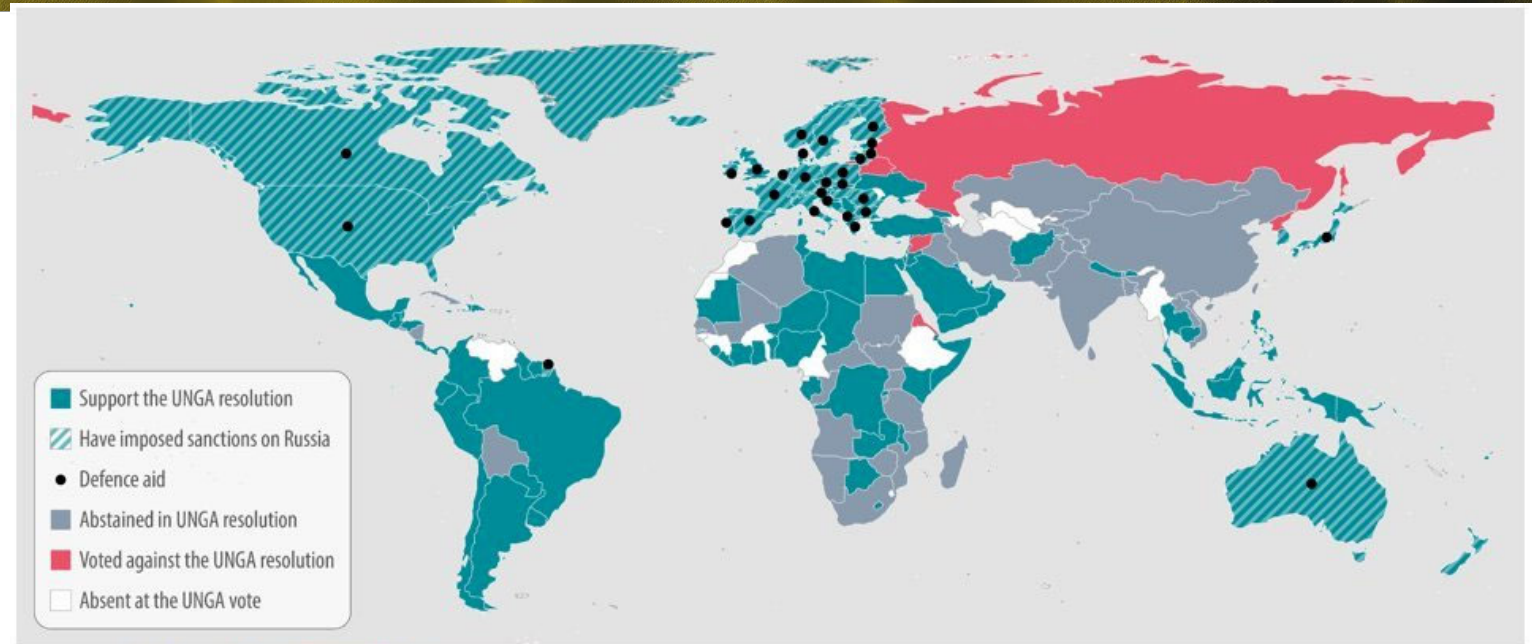
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Fiscal Policy Response



Europe has been united in the diplomatic response



Data source: [UNGA resolution A/RES/ES-11/1 vote summary](#), government statements for sanctions and commitments of defence aid as reported by the press.

Defence aid includes various items, lethal and non-lethal, such as fuel, helmets and other protective equipment, medical items and medical care for injured Ukrainian soldiers in third countries, as well as lethal weapons, from rifles and ammunition to air defence rockets and anti-tank systems.

UNGA: United Nations General Assembly



European Union Response - Energy Policy



REPOWEREU TO CUT OUR DEPENDENCE ON RUSSIAN GAS



More rooftop solar panels, heat pumps and energy savings to reduce our dependence on fossil fuels, making our homes and buildings more energy efficient.



Decarbonising Industry by accelerating the switch to electrification and renewable hydrogen and enhancing our low-carbon manufacturing capabilities.



Speeding up renewables permitting to minimise the time for roll-out of renewable projects and grid infrastructure improvements.



2030 Doubling the EU ambition for biomethane to produce 35 bcm per year by 2030, in particular from agricultural waste and residues.



Diversifying gas supplies and working with international partners to move away from Russian gas, and investing in the necessary infrastructure.



A Hydrogen Accelerator to develop infrastructure, storage facilities and ports, and replace demand for Russian gas with additional 10 mt of imported renewable hydrogen from diverse sources and additional 5 mt of domestic renewable hydrogen.





European Union Response - Defense Spending

Germany to set up €100bn fund to boost its military strength

Chancellor Olaf Scholz says urgency of Ukraine crisis has forced decision to increase defence spending

● **Russia-Ukraine war latest news: follow live updates**



■ Scholz announces €100bn rise in German defence spending after Russia's Ukraine invasion - video

In a historic announcement to parliament, the German chancellor, **Olaf Scholz**, has said a fund of €100bn (£85bn) will be set up immediately to boost the strength of the country's armed forces, as he also announced a sustained increase in defence spending over the coming years.

Source: <https://www.theguardian.com/world/2022/feb/27/germany-set-up-fund-boost-military-strength-ukraine-putin>

High support from German citizens for change in defense and energy policy

Level of support for German government measures in response to the invasion of Ukraine by Russia



Source: infratest dimap/ARD-DeutschlandTrend for ARD Tagesthemen | Values up to 100%: 'I don't know'/'No response' | March 3, 2022 | * June 2014

Source: <https://www.dw.com/en/germans-approve-of-government-u-turn-on-ukraine/a-61011528>



Variables to watch: risk premium on peripheral bonds

Risk premium of government bonds vs. 10-year German bonds

Source: Bloomberg and own elaboration. Data as of March 15, 2022



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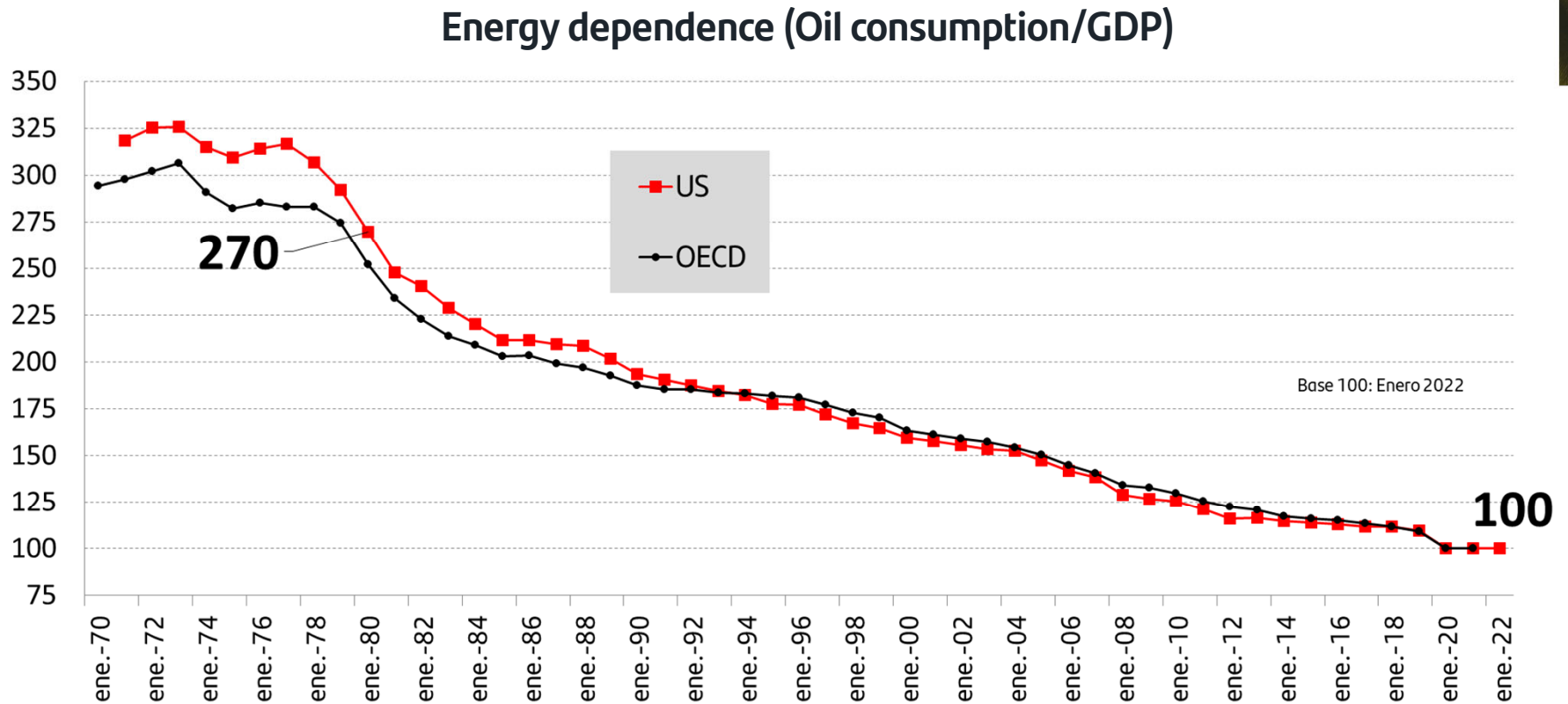


Monetary Policy Response



Differences with respect to the shock of the 1970s

Source: Bloomberg and own elaboration

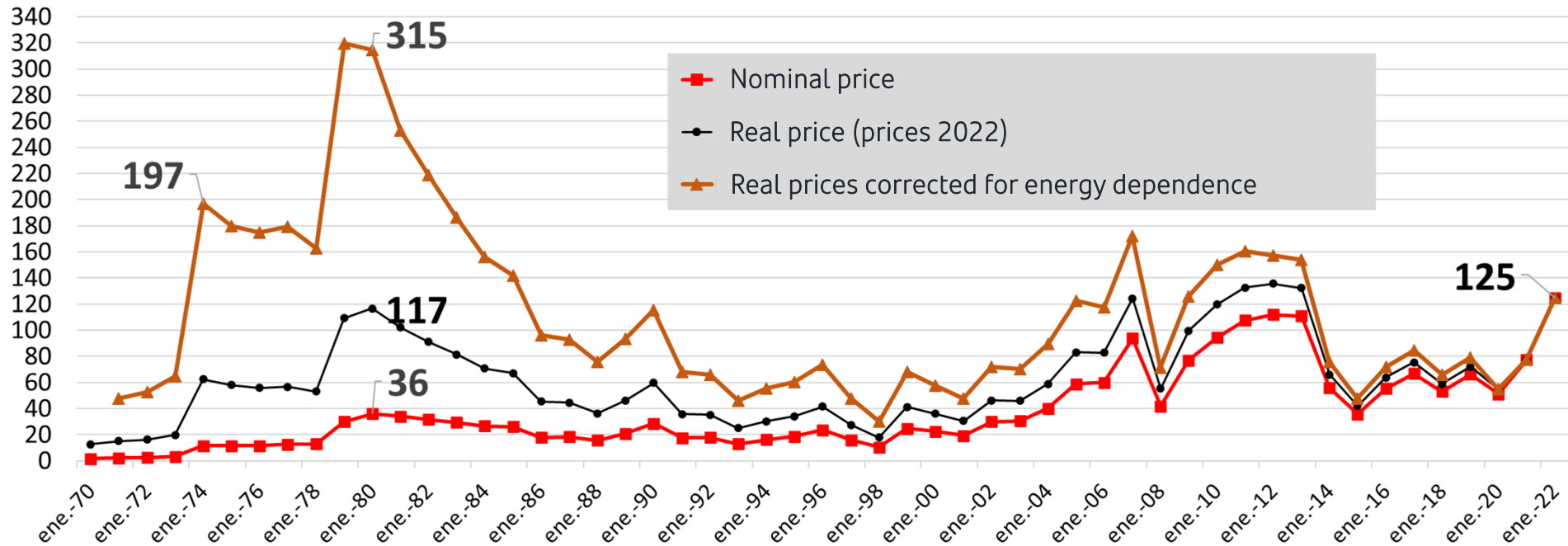




Comparable crude oil price performance

Source: Bloomberg and own elaboration

Oil prices in nominal, real and adjusted by energetic dependence

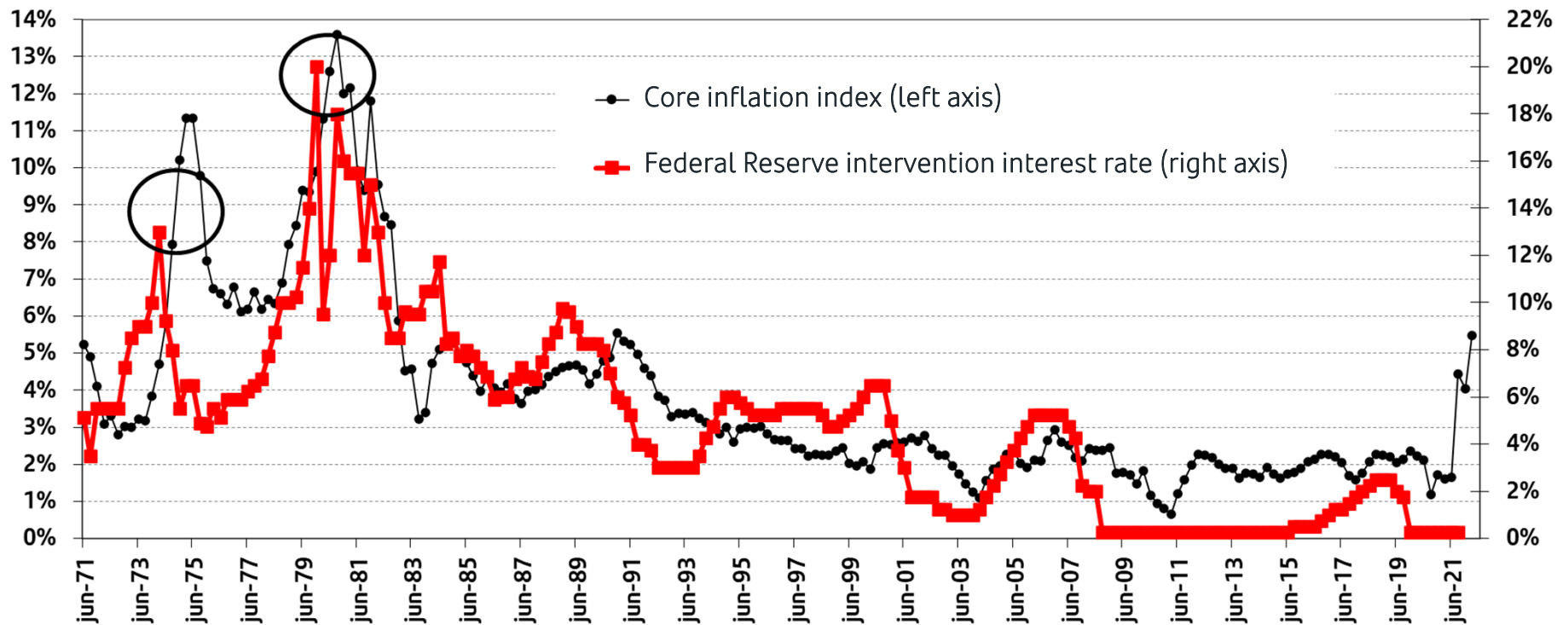




Differences with respect to the shock of the 1970s

Source: Bloomberg and own elaboration

Fed Funds rate and core inflation



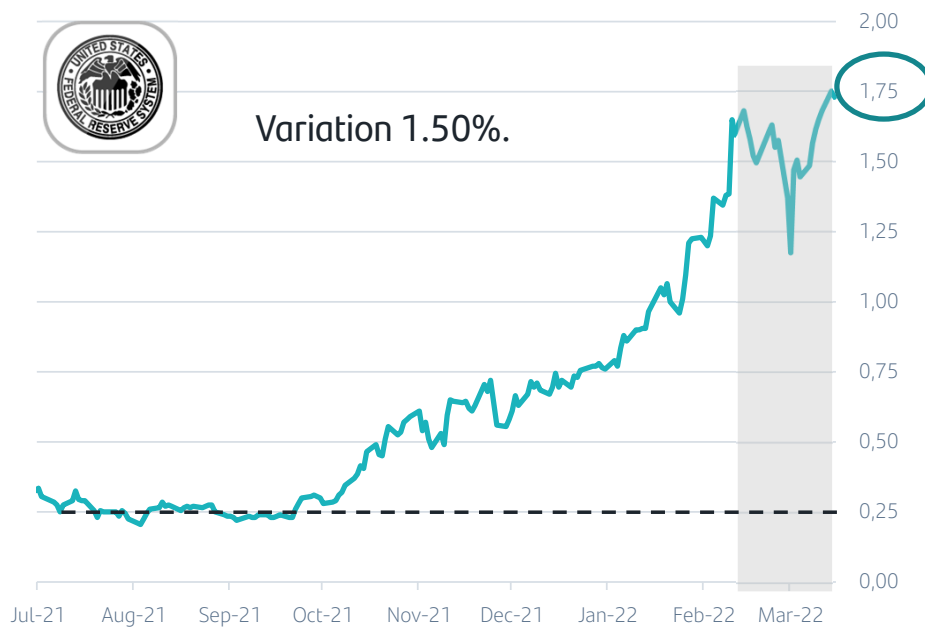


Expectations of rate hikes by the market

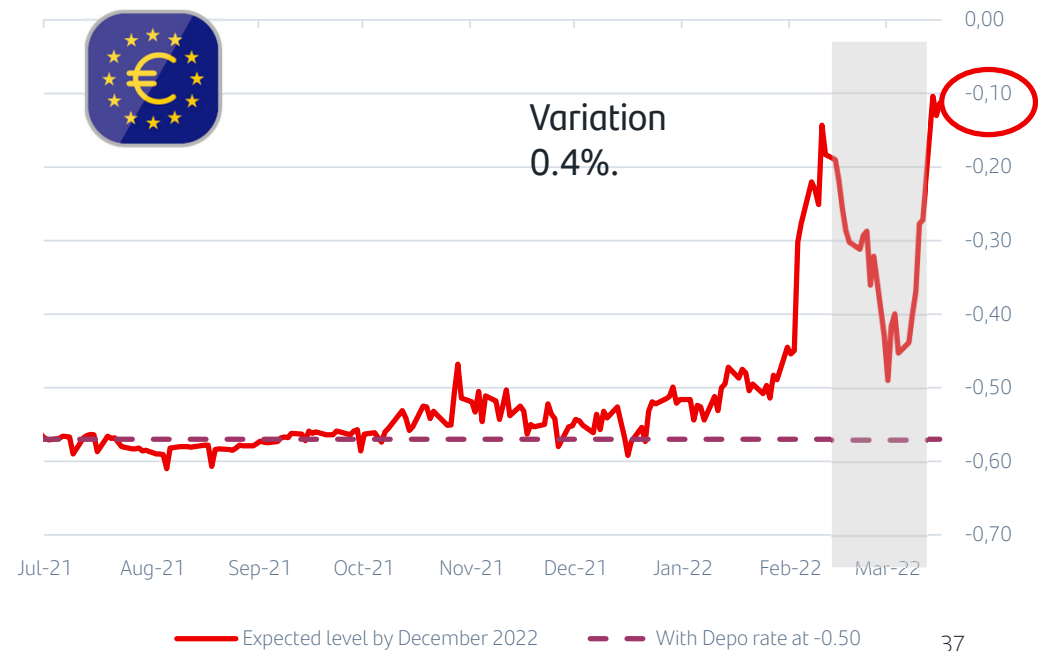
The market has reacted with volatility but expectations for increases are maintained

Source: Bloomberg and own elaboration. Data as of March 15, 2022

6 rate hikes expected by December 2022



4 rate hikes expected by December 2022





Variables to watch: Long-term interest rates

10-year government bond rates

Source: Bloomberg and own elaboration. Data as of March 15, 2022



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Thank you

grazie
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