

March 7, 2022

Dear Friends,

Typically we refrain from commenting on short-term moves in financial markets. We don't like to lend credibility to bumps in the road and, frankly, Big Media is much better at the panic first, think about it later style of communication.

Furthermore we like to let time pass so the noise can settle. Now that the initial noise over the Russian invasion of Ukraine has passed (and the microchip implanted by the government via all those COVID shots has stopped broadcasting (#FoilHatClub)) we think it's time to offer a few words.

At Apollo our preference is to remain objective and dispassionate. Obtain information from credible sources, analyze and then incorporate into a larger, existing framework when appropriate.

A critical point about credible sources. They vary depending upon the situation. The CDC is a notable example of a credible source throughout the fluid COVID situation. Sources that are generally **not** credible include (but are not limited to) CBS, ABC, NBC, MSNBC, CNBC, FOX, Fox News, Fox Business News, Twitter, Facebook, Instagram, YouTube, TikTok, family, friends, coworkers, neighbors, bloggers, vloggers, people on your group text chain, people in your fantasy football league, people at Costco fighting over toilet paper, etc. None of these outlets has factual, unbiased information. None of these outlets has an interest aligned with yours. Trust at your own risk.

### **(1) THE SITUATION**

Events continue to evolve rapidly and in a most unfavorable way. Ignoring the human impact for a moment and focusing solely upon the economic/financial the world has weaponized finance by cutting off Russian access to payments systems, buyers for Russian oil, etc. The Russian stock market has collapsed with many stocks trading at little/no value due to the lack of buyers. It's an important lesson in illiquidity.

As an aside the weaponization of finance should scare the \_\_\_\_ out of every American. According to the U.S. Treasury foreign governments hold \$7.7 trillion of U.S. debt. Japan and China hold \$1.3 trillion and \$1.1 trillion respectively. Imagine if one (or both in coordination although highly unlikely) decided to dump the entirety of their holdings. The oversupply relative to demand would drive interest rates so high that it would kill the U.S. economy. Food for thought the next time Healer Joe proposes spending \$3.6 trillion and sending "stimulus" (i.e. cigarette, beer and meme-stock) checks to anyone with the ability to fog a mirror.

### **(2) THE FINANCIAL MARKET IMPACTS**

It's important to note the prices of assets such as stocks and bonds are derivatives. In the short term they reflect sentiment. In the long term they reflect the discounted value of revenue net of expenses.

The father of value investing Benjamin Graham once quipped, “In the short run the market is a voting machine but in the long run it is a weighing machine.”

The short run is rife with uncertainty. With uncertainty comes fear and the desire to act in order to delude ourselves into thinking we have control. Sell now. Down the road we can worry about what the future will look like.

Does this sound logical? Of course not. Illogical thinking leads to illogical action.

Fine. But prices (other than oil) are still going down. Someone is selling. Let’s look at who:

1. **Speculators.** Momentum players buy simply because prices are going up. Conversely they sell simply because prices are going down. The more prices go down the more they sell. Leveraged participants are forced to sell. Borrowing at cheap rates to enhance returns only works when the underlying collateral is stable or rising. When the prices of stocks and bonds on deposit as collateral for loans decline selling to raise cash is a necessity. Selling begets selling.
2. **Indexers.** They’re speculators too even though they won’t admit it. Capturing 100% of an index return on the upside means accepting 100% of the loss on the downside. To avoid losses they sell. It’s market timing and it never works. Never.
3. **Institutions.** Most money managers are compensated based upon performance relative to peers. When peers are selling it isn’t easy to have conviction and hold on during uncertain times. No one wants to look stupid – certainly not when compensation is based upon such.
4. **Newbies.** These are the folks who began putting money to work in/after 2009. They’ve seen an almost straight line up. A 16.5%/yr average ROR for the S&P 500 over the past 13 yrs. They believe not only that markets go in one direction but in leaps and bounds. They don’t understand down markets such as the 37% decline in the S&P 500 in 2008. As the saying goes, “You can’t teach experience.”
5. **Nervous Nellies.** They need no explanation. They will, however, try to disguise their emotional decisions with quasi-logical and plausible-sounding “evidence.”

The list of sellers goes on and on. Notice who isn’t included in the list. Experienced, diversified and dispassionate investors. Hmm...

### (3) UKRAINE/RUSSIA OUTCOMES

The situation is untenable and apparently a lose-lose. Russia cannot afford a lengthy conflict (estimates are \$10 billion/day) and Ukraine lacks a war machine that can match Putin. Although the range of outcomes is vast we’d like to focus on three:

1. **Settlement.** Some sort of compromise through talks and de-escalation. Putin would likely be satisfied to control eastern Ukrainian regions. He could allow most of Ukraine to remain independent – particularly if it pauses efforts for NATO admission.
2. **Overt Quagmire.** Ongoing conflict. Russia continues its efforts. Lives are lost on both sides. International sanctions harshly impact the Russian people. Putin’s support erodes.
3. **Clandestine Quagmire.** Russia captures the major Ukrainian cities and installs a puppet government that must manage a large, unsupportive populace. Cold War 2.0.

We see settlement as the most likely outcome.

#### **(4) INVESTMENT STRATEGY (in context of all-encompassing financial planning)**

Yeah, OK, but “the market” is going down and “they” say it’s going to continue. My 401(k) is down x%. Who cares about all the geopolitical mumbo jumbo? I “need” to do something.

Really? Was there a “need” to act during the dot-com bubble, the housing crash, the credit crisis, Brexit, Greek banks, Trump’s election, Trump’s impeachment, Trump’s non-impeachment – these were all supposed to sink the markets (depending upon your favorite “expert”) and yet simultaneously the buying opportunity of a lifetime (depending upon your favorite “expert”).

Our crystal ball isn’t so clear but we can say the Ukraine/Russia situation is but another blip on the radar screen. Life marches on. It always does.

The tried and true three-pronged cash/bond/stock investment approach works.

We hold cash for liquidity and times of uncertainty. In up markets it’s a drag on returns. In down markets it provides a safety net and an avoidance of panic selling to fund day-to-day expenses.

We hold bonds because they temper the volatility of portfolios and provide income. They provide higher returns than cash but lower returns than stocks. They are riskier than cash but less risky than stocks. They are a drag on returns when stock prices are rising. They support the portfolio when stock prices are falling.

We own stocks and “hard assets” because in the long run they provide the inflation-beating rate of return needed to achieve financial security. They are wonderful in up markets and lousy in down markets. They are a drag on returns when prices are down and the driver of returns when prices are up.

We never want to make light of serious situations. Innocent people on both sides of the conflict are suffering. We feel for these people.

Nonetheless we cannot allow emotion and the short-term to be a distraction as we construct our long-term financial plans. At Apollo we partner with clients to construct logical, holistic financial plans that go far beyond the most obvious component of investing. We adhere to the plans. It’s a trust we are flattered and humbled to receive. We take it incredibly seriously.

As the world watches it’s important we maintain some sense of normalcy. Personally my favorite and most effective weapons are humor and perspective. I hope to have provided a bit of both.

It can’t be said enough. On behalf of the entire Apollo team I am appreciative of the opportunity to be a prudent steward of your financial affairs. Thank you very much (or Mahalo Nui as we say in Hawai’i) for your trust and support.

*Howard*