

[Home](#) > [Insights](#)
[Blog](#)

First take: Ukraine conflict, looming bear market

A new market update from Chief Market Strategist Troy Gayeski



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1. Clearly, the Russian invasion of Ukraine has led to additional downside in risk assets, upside in commodities, particularly oil, and a short-term respite from surging bond yields.
2. Unfortunately, this has occurred at a time when markets were already unusually fragile given the run-up in valuations the past three years and a Fed about to embark on a long tightening cycle. Furthermore, the invasion will lead to more near-term inflationary pressure, which makes the Fed's job of restraining inflation even more challenging.
3. One should always be humble about making any bold predictions tied to geopolitical risks as the situation can deteriorate or even improve rapidly. That being said, if not for the upcoming tightening of monetary policy (remember, the Fed hasn't really done anything yet other than slow down the pace of its balance sheet expansion), this would look like a classic opportunity to add risk given the VIX is above 30 and equity indices are now well below their 200-day moving average. Unfortunately, as we may be in the early stages of a mild bear market, we would urge all but the most skilled investors or traders to proceed with caution. Further, always remember that dip buying works until it doesn't and then it ends in tears. Lastly, if we get a strong counter trend rally (aka bear market rally) next week, it may be a golden opportunity to cut risk for investors that incorrectly assumed the last three, five, and 13 years of exceptional market performance would continue forever.
4. The additional downside pressure on equity markets from the Russian invasion has led to a short-term decline in bond yields, which has temporarily improved the performance of vanilla fixed-income securities with high levels of duration. If you came into this year with excessive levels of duration and were feeling the pain of higher yields until recently, this may be a golden opportunity to lighten up on duration.
5. Regarding the economy, we still believe the U.S. economy should have a solid year of growth. The current geopolitical storm may modestly reduce consumption as even higher inflation takes a further bite out of consumer confidence and spending, and corporate investment growth and inventory rebuild cycles become more muted. However, the events unfolding so far are unlikely to materially alter the ongoing economic expansion.
6. In an environment where classic 60/40 asset allocation strategies continue to struggle, we continue to believe alternative strategies may offer a port in which to weather the storm: both potential downside protection as well as income and return potential in user friendly solutions that are accessible to not only large institutions, but also average investors as well. Democratizing the asset class has taken time, but fortunately in 2022, you don't need to be a sovereign wealth fund or multibillion-dollar endowment to participate.

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