TAM INTERNATIONAL INVESTMENT NOTE

Bulls vs the Great Bear

Is it time for the bulls to hold their nerve as the Great Bear stirs?

It is understandable that, on the face of it, headline news of Russia invading a sovereign nation on the borders of the EU may give rise to some alarm for investors, but the media has been positively revelling in the word "Invasion!" as Russian President Putin dispatched 6,000 Russian troops to key strategic Russian assets in the Crimea.

However, we believe that this is a limited strategic move by Russia to protect what it sees as its direct assets and that whilst we are not political analysts, we do not perceive this to pose a threat to the long term sovereignty of Ukraine and not something that demands a shift in investment strategy. With global stock markets already sitting with their finger on the "sell" button in face of notionally high valuations and the eternal tapering issue, a sell off might have been expected. The fact is that Ukraine's turmoil and political and economic weakness was nailed on the moment the existing regime fell last week and that markets ignored it and went on to new highs. Why? - Because they believed it was not a market moving event.

The fact is that Russian politics and business are intertwined and President Putin carefully weighed up the likely western response to the military action beforehand and concluded that there's not much to worry about from the Russian perspective. At most, some boycott of the post-Olympic G8 was to be expected. This will hurt Russia a bit but the rising cost of energy, and Russia's stranglehold over it, offsets any other reaction from the west which, so far, has been all noise and rhetoric. The champagne bill for G8 in Sochi was never going to move the needle on the $45 billion cost of building the venue in the first place.

Even President Obama seems keen to distance himself from any ugliness. His best offering was a rather weak and ambiguous statement that "Russia will count the cost if it orders military action in Ukraine". What does this mean? Not much, in our view. Maybe a few top Russian officials don't get their visas to go to Aspen or California this year. So far, it's been Obama's Secretary of State, John Kerry, that's been sent in again to do the hard talking following his tense visit to Beijing two weeks ago. Sadly, Obama's also off the Christmas card list in China too, after his meeting with the Dalai Lama. Readers may remember that he was due to visit later this year after his October trip was cancelled due to the US government shutdown.

It never rains, it just pours, in Washington these days.

Reaction from Europe, as it heads close to deflation, is similarly muted as Germany in particular, is badly exposed on its reliance on Russian gas supplies. Greece, who currently hold the EU Presidency (we're not making this up), will chair an emergency meeting in Brussels. What this is supposed to achieve, and what Putin will make of it, is anyone's guess. It's an uncomfortable reality for the EU that Yanokovich, who's ousting the EU supported was actually democratically elected, and so it's is not difficult for President Putin to argue at home that mother Russia needs to act to stop the bad guys and, according to some reports, save Ukrainians from the threat of starvation. This is all face saving, of course, but President Putin is also under considerable pressure to act. A show of strength is as much for his own people who may have smouldering thoughts of regime change themselves. The biggest issue is the naval base in Crimea's Sevastopol which is the home of Russia's Black Sea fleet and already home to between 15,000 to 25,000 Russian Navy personnel. It is a key strategic port giving Russia its only access to the southern warm water oceans (Syria was closed due to the civil war) but the military assets, and we must assume nuclear weapons, must surely be secured now that they find themselves located in a country with a political vacuum. The fact that most of the population in the region hold Russian passports is also a factor. We do not see the Russian move as a warning shot against the expansion of NATO but more internal face saving.

So while the politicians argue and exchange vague warnings in a political battle for Ukraine's soul, we do not see the current situation as one that is likely to escalate to dangerous levels. It is unthinkable that Ukrainian and Russian soldiers, literally ex-comrades in arms, would take up arms against one another and any military intervention from the west is absolutely out of the question. Even for William Hague.

As we write, the FTSE100 Index is off marginally but still around 6,700. Given the recent sell off to near 6,400, and recovery to over 6,800, some easing from the highs was already underway and to be expected. We currently see economic factors as exerting a greater influence over markets than geopolitics – however intertwined some may be. Growth in the US and UK must come in 2014 to support current valuations and persistently low inflation in the EU and Japan is cause for concern.

As we set out in our Outlook 2014 in January, we believe that it is really only equities and selected property that will deliver this year. As the market grinds higher, it is almost impossible to predict what the next catalyst for profit taking will be as there are dozens of issues around the world that keep the nervous on the sidelines in cash and bonds.

In conclusion our strategy remains the same. We are optimistic for investment returns on equities in 2014 and will buy on any unwarranted or excessive weakness. This will test the mettle of investors but, right now, we think it's time for the bulls to face down this stirring of the Great Bear.

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