

## Positioning Recommendations - February 25th, 2022

The tanks roll, oil rolls over, and tech roars back! This is not exactly what a rational investor would have expected in the event of a multi-front invasion of Ukraine with Kyiv already under siege.

Perhaps this odd reaction is a function of the feather-light wrist-slap the West has administered to Russia thus far. Reportedly, Italian Prime Minister Mario Draghi is pressing to exempt his country's luxury goods from prohibited exports to Russia. Belgium is allegedly trying to protect its diamond trade with Mr. Putin's thievocracy, as well. More significantly, the US has avoided placing sanctions on Russia's energy industry, as has Europe. Consequently, I think it's fair to say our current crop of leaders bears little resemblance to Winston Churchill. But it does evoke memories of Neville Chamberlain! (One exception is Germany Chancellor Olaf Scholz, who showed some spunk by revoking the approval of Russia's recently completed Nord Stream 2 pipeline. It will be interesting to see if that resolve holds up should Putin stop the gas from flowing through Nord Stream 1.)

Despite the stock market's cavalier attitude toward the tragedy in the Ukraine, it's my view that it is a substantial negative in a number of ways. The main risk is that this situation intensifies what is already a brutal energy crisis in Europe. There is the very real possibility that it causes oil and natural gas prices to rise on a global basis from already lofty levels. In turn, this makes the dreaded economic condition of stagflation a greater risk. As regular *EVA PR* readers know, I've been anticipating an inflationary boom later this year, and the war in Ukraine could work against that outcome.

On the other hand, a case could be made that the U.S. economy actually benefits from the European energy fiasco. There are already moves to restrict the Continent's heavy industry due to soaring electricity prices. Governments are attempting to prioritize household energy needs over those of the industrial sector. Accordingly, US producers may need to fill in the output gaps.

Interestingly, despite the lack of official restrictions on Russian oil, it is trading at a \$12 discount to Brent crude, the key European benchmark. Apparently, there is an aversion by buyers of nearly all Russian exports, even by China (per Goldman Sachs' ace commodity analyst, Jeff Currie.) Based on how much wheat Russia and Ukraine produce, about 25% of the planet's total, along with their enormous output of fertilizer, this could benefit the US agricultural sector.

With a massive cost advantage due to natural gas, a key petrochemical input, trading sub-\$5 in the US versus well over \$30 in Europe, the US chemical industry also looks to be in the catbird seat. A certain major player in this sector, that has half the name of the most venerable US stock index, looks interesting. It offers almost a 5% yield and trades for just eight times earnings. (It has risen sharply of late, so easing into the position is logical.)

Since yesterday morning, The Bloomberg Commodity index has moved in the opposite direction of the overall stock market. After initially popping almost 5% on the invasion news, it has fallen 6%. It continues to be my recommendation to add commodity exposure on pullbacks. Should the US experience an inflationary boom – as it reprises its critical supplier role to Europe during and after WWII — commodities, particularly energy, should be a most rewarding destination for investment dollars. If there is stagflation, commodities are likely to outperform as

they did in the 1970s. In the actual Positioning Recommendations section, I've got a new idea in that regard. Keep reading!

## Positioning Recommendations

### LIKE

A new buy suggestion involves the US oil field service (OFS) industry. Previously, I've been reluctant to recommend this energy sub-sector due to intense pressure to hold down exploration spending for a variety of reasons. But I believe the Ukraine disaster is a game-changer. It's now a very high odds proposition that the world is going to need US oil and gas even more than it has in the past. (US shipments of liquified natural gas—LNG—were preventing intensifying shortages and price spikes in Europe; note, this was before Mr. Putin's blitz began.) The Permian basin remains the most prolific production basin in the world due to its unique geology. Thus, focusing on companies with material exposure to that expansive area—it has the area of a mid-sized state—might be the superior approach. But simply buying an OFS ETF is reasonable, as well.

- Large-cap growth names at a reasonable price.
- Certain international developed markets, especially Japan
- Publicly traded pipeline partnerships, i.e., MLPs and other mid-stream energy securities.
- Gold-mining stocks
- Gold
- Silver
- Select international blue chip oil stocks
- **Oil field services companies, particularly those well exposed to the Permian Basin**
- Short-term investment grade corporate bonds
- Emerging market (EM) bonds in local currency (focusing on stronger countries, particularly in Asia)
- Large-cap value
- High-dividend equities with *safe* distributions
- Most cyclical resource-based stocks
- BB-rated corporate bonds
- Canadian REITs
- South Korean Equities
- Certain "Virus Victim" equities such as refiners, homebuilders, and select retail stocks
- Investment-grade floating rate corporate bonds
- The higher quality mortgage REITs
- Floating rate bank loans
- Copper producers
- Healthcare stocks

### NEUTRAL

REITs have been under considerable selling pressure lately. Accordingly, these look more attractive, justifying some selective buying. At this point, though, I'm reluctant to upgrade them to Like status.

- Uranium and uranium producers
- Renewable Yield Cos

- Intermediate-term investment-grade corporate bonds, yielding approximately 2.25%
- Mid-cap value
- Emerging stock markets; however, a number of Asian developing markets look undervalued
- **US-based Real Estate Investment Trusts (REITs)**
- Cash
- Canadian dollar-denominated short-term bonds
- One- to two-year Treasury notes
- Traditionally “safe” sectors such as Staples and Utilities
- Virus Victors
- Small-cap value
- European banks

## DISLIKE

The main Indian stock index is popularly referred to as the SENSEX. Frankly, based on its valuation level, I think it should be known as the “Senseless SENSEX”. Incredibly, it trades at 24 times current and forward earnings, implying no growth next year. This is about a 20% premium to a very pricey US stock market. India is also a major importer of oil. Thus, it is highly vulnerable to a crude market that appears to be getting tighter and tighter from a supply standpoint.

- **The Indian stock market**
- A wide range of high-income securities, including preferred stocks
- Intermediate-term Treasury bonds
- Small-cap growth
- Long-term treasury bonds
- Long-term investment grade corporate bonds
- Most municipal bonds
- US dollar
- Many semiconductor tech stocks
- Mid-cap growth
- Lower-rated junk bonds
- Green energy stocks
- SPACs
- Most new issues
- Despite a disastrous February, 2021, most of the popular Reddit/WallStreetBets meme stocks still have material downside.

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