CHASE INVESTMENT COUNSEL CORPORATION

PRESERVING & GROWING WEALTH
Since 1957

February 2022
REVIEW & COMMENTARY

PETER W. TUZ, CFA, CFP®
PRESIDENT & PORTFOLIO MANAGER

March 2, 2022

Game Changer

Peter W. Tuz, CFA, CFP®
President & Portfolio Manager

"The January-February drop in the markets have, at least initially, made them more attractive. "

Like a lot of phrases in investing, "game changer," is overused. Not this time. The invasion of Ukraine by Russia is a game changer, a tragic event unlike anything investors have seen in decades. We are possibly seeing the end of Ukraine as an independent country and a new iron curtain falling over Europe, or the end of Putin as Russia's president. Time will tell.

The other overused Wall Street phrase "markets hate uncertainty," proved true in February. Equity markets, both in the United States and around the world, continued the downward trend started in January. In the U.S., the S&P 500 Index ("S&P 500") fell 2.99% and the Dow Jones Industrial Average fell 3.29%. Globally, the S&P International 700 Index fell 2.09%. At February's end, the S&P 500 was down 8.01% for the year, again approaching "correction" territory. Surprisingly, smaller stocks fared better than larger stocks in the month, with the S&P Mid Cap 400 and Small Cap 600 Indices up 1.11% and 1.40% respectively. Investors unlucky enough to hold the VanEck Vectors Russia ETF (RSX), suffered a 55% loss in February. Volatility has spiked as have oil and gas prices while "safe havens" like U.S. Treasury bonds and gold have risen.

As with January, the pain was felt among almost all of the 11 S&P sectors. Only the energy sector, up 7.3%, rose. The weakest performance was in communications services, down 6.98%, real estate, down 4.91%, and information technology, down 4.90%. Due to the growing "risk off" mentality, bonds were modestly stronger in the month, with the S&P U.S. Aggregate Bond index up 2.38%.

The question "What happens now?" is almost impossible to answer, at least in the short-term. In the long-term markets always recover. But now, in addition to global turmoil, we still have the concerns about rising inflation, rising interest rates and their effects on markets that caused a down January.

According to J.P. Morgan, the last 12 major geopolitical events, ranging from the Arab Israeli war and oil embargo in 1973 to the Intervention in Syria and the first Ukraine-Russia conflict in 2014, caused, on average, a two week sell-off followed by a four-month recovery. The size of the sell-off averaged a modest 6.5% but ranged from a 17% drop to only a 2% drop (ironically when Russia seized part of Ukraine in 2014). The longest recovery period occurred after the 1973 Arab Israeli war and first oil embargo when it took the S&P 500 four years to reach prior highs.

The January-February drop in the markets have, at least initially, made them more attractive. According to FactSet, the S&P 500 now sells at its 5-year average p/e ratio of about 18.6x earnings. At the beginning of 2022, it sold for 21x the $228.85 earnings estimate for 2022. The five-year average p/e ratio remains well-above the 10-year average of 16.7x. There is also a high likelihood that $228.85 estimate will fall. Inflation, already running at levels not seen in 20 years, will be exacerbated by higher energy prices. Unless you are an energy company or defense contractor, it is difficult to believe the current conflict and the current inflation won't cause your earnings estimates for 2022 to fall. (over)

“The current environment is complicated and confusing and points out the need to watch your assets more closely than ever.”

The current environment is complicated and confusing and points out the need to watch your assets more closely than ever. Should peace happen, especially if accompanied by Putin’s leaving, there could be the mother of all rallies. Or we could see the mother of all bear markets should China decide it’s time to take over Taiwan. In any case, the current turmoil points out the ever-present role that diversification and asset allocation serve in mitigating market risk. As always, we are here help you with any questions about investment matters.