A Weekend at Vladimir's

Xponance Quick Take on the Recent Events in Russia

June 2023

Author

Adam Choppin, CFA, APFI
Assistant Portfolio Manager | Multi Manager Strategies

Unless you've been on an island without cell phone coverage for the past several days (in which case, good for you!) you are certain to have heard of the non-coup, coup attempt in Russia over the weekend.

More detailed summaries abound, and the situation will evolve quickly beyond our capacity to update it, but we offer the critical salient summary here. The Russian mercenary company, the Wagner Group, and their convict-turned soldier of fortune Yevgeny Prigozhin, on Friday, June 23 withdrew thousands of fighters from Ukraine and turned them towards Russia in a "march for justice." The mercenaries captured Rostov-on-Don, a city in southern Russia that has served as a critical logistics hub supporting Russia's ongoing war in Ukraine and were continuing to advance on Moscow until Belarusian President Alexander Lukashenko announced a deal on Saturday, June 24 for Prigozhin to call off the coup and take refuge in Belarus in exchange for an annulment of treason charges by Putin. As of this writing (Sunday evening on June 25), various news outlets are reporting that Wagner Group mercenaries are returning to their barracks (though importantly it is unclear if that means to the front lines in Ukraine) and Prigozhin is heading for Belarus.

This story appears far from over, but some early investment implications already seem apparent. Obviously, disarray in the Russian military is good for all things Ukraine, though it is still unclear how good. Counter-offensive gains through the spring and summer so far have been paltry, but small cracks in the Russian front and especially a further deterioration of (already low) Russian troop morale could yield quick and large gains for Ukraine's highly motivated military. One Ukrainian spoof news site seemed to capture the initial reaction to the coup attempt aptly with the headline: "BREAKING: Ukraine runs out of popcorn."

In the near-term, we expect some price volatility in oil and other Russian-dominated commodities such as palladium, platinum, wheat, and nickel. Beyond threats or perceived threats to Russian originated supply, the Wagner Group also controls the security for major oil producing facilities in contested areas in Libya and Sudan, in addition to diamond and gold production elsewhere in the African Sahel.

Despite the fragility in the Russian state exposed by this episode, we believe that the base case remains that Vladimir Putin will remain in power in Russia. However, the possibility of regime change has increased, as has the potential for Russian warlordism even if Putin is able to hang on to power. Either of these directions in Russia should raise or at least maintain the risk premium for those aforementioned commodities, but also for markets in general as price instability casts a longer shadow over the fight against inflation.

One potential winner we see is paradoxically for Chinese and Taiwanese risk assets. Any acceleration of the war in Ukraine in Ukraine's favor lowers the geopolitical tension over China's lukewarm support for Russia…support that surely has chilled over the past few days amid the revelations that Putin's command and control may be weaker at home than originally thought. Diverting geopolitical media attention back to Russia is also positive for depressed Chinese equities in particular. We also see non-aligned countries, like India and South Africa, which have not yet been penalized for their neutrality, as likely being able to permanently evade any potential further political scrutiny as the concern over a Russian victory in Ukraine fades.