
# The Evolving Geo-political Landscape

**Russia's invasion of Ukraine has taken a huge toll already. First and foremost, it is a humanitarian crisis through significant loss of life and human suffering. Europe is now facing yet another refugee influx.**

The economic toll is also high as trade flows are further disrupted on top of existing supply chain and logistical challenges. Commodity prices, particularly for oil and grain, have surged into an environment of already high and problematic inflation.

While central banks can technically "look through" the impact of higher commodity prices on inflation persistently higher commodity prices will ultimately feed through into core inflation, inflation expectations and wage demands.

We expect central banks need to remain focussed on inflation with the European Central Bank last week delivering a more hawkish than expected statement and the US Federal Reserve expected to deliver the first of 6 or 7 hikes this year later this week.

Open to more conjecture and debate are the long-term political implications as slow-playing geo-political tensions that typically bubble away below the surface have "bubbled up" and taken a significant step-change.

We only need to go back to the Global Financial Crisis to help put these latest developments into some context.

The GFC was the great economic leveller. It was the time at which the embracing of unfettered capitalism by western liberal democracies was its most challenged.

With the resulting loss of economic prowess by the West came a levelling of political influence between developed and developing economies. At the multi-lateral level the G20 became the more important grouping of countries.

This has inevitably brought tension given the multi-faceted political and economic arrangements in each of those countries.

Tensions have been greatest between the United States and China as the world's two largest economies vie for economic supremacy and political influence, both regionally and globally. America's "Pivot to Asia" has not gone unnoticed in Beijing and the West constantly frets about China's growing global influence through Belt and Road initiatives.

The most visible manifestation of this tension is with respect to technology. Both need technology supremacy to propel growth and living standards as US productivity stagnates and China faces into old world problems (aging population, slowing population growth, slowing productivity) before it has become rich. Hence the new focus on "Common Prosperity" by the Chinese leadership. The pandemic has only served to intensify that tension.

Western liberal democracies have had their own issues to deal with as the fall-out from the GFC focussed attention on inequality and a lack of economic progress for the average citizen.

Globalisation took much of the blame for the GFC, which was misplaced. Globalisation has led to a significant reduction in inequality and can only be partly blamed for rising inequality within countries.

But with the rise of populism, particularly in Europe in the aftermath of Eurozone debt crisis, the popular belief that globalisation is bad has prevailed. It's through this period we also witnessed "Brexit" and the US Presidency of Donald Trump, which saw new tariffs imposed and barriers erected to trade and migration.

From a diplomacy perspective, the Trump presidency saw the tearing up of the book of rules-based democratic processes and the distancing of the US from the multilateral institutions that governed them. This damage is not easily repaired.

The pandemic has also led to many businesses reassessing the security of global supply chains. Some are actively reassessing the sources of final goods and inputs into production and thinking about bringing these product stages closer to home, even if it's not at the cheapest price. Security of supply carries a cost.

It is into this background and recent history that we have now witnessed Vladimir Putin's desire to stymie the eastward advance of NATO into Ukraine.

We imagine Putin has been surprised by two things in the last two weeks: the fierce resistance of the Ukrainian people and the severity and co-ordination of the sanctions imposed by western countries.

By far the most dramatic of those so far has been the removal of SWIFT access for some Russian banks and, in an in unprecedented move, the sanctioning of Russia's central bank. The Ruble has crashed, delivering a massive inflationary shock and dramatic decline in Russian living standards. We are witnessing the weaponisation of international finance .

The path of the conflict remains uncertain. A diplomatic solution is possible, but so too is a protracted and costly war.

More fundamentally, the global political economic and political fabric that has survived since World War II has gone from being frayed at the edges to torn apart.

It is not inconceivable to imagine a return to cold-war style fragmentation and factionalism. Over the last two weeks the West has discovered a new-found sense of unity, though that may come at the price of the end of the peace dividend which has been enjoyed in the 77 years since 1945. Germany has already announced an increase in defence spending and even Switzerland has jumped off its neutral fence.

China has not yet shown its full hand by neither supporting nor condemning Russia's actions. However, earlier this week China's foreign minister reiterated Russia's importance as a strategic partner. Given China's already-global economic reach, it potentially has more to lose by a further retreat from globalisation. Much of China's wealth-generation engine relies on its integration within complex international supply chains of value-adding manufacturing.

But Putin has sent a clear message to the world that Russia is important too, and what the country lacks in economic heft, it is more than willing to make up for with aggression. At least under its present leader, Russia retains the capacity to spring surprises on an international order that was already reaching the limits of goodwill, following the two years of pandemic restrictions and associated ructions.

The long-term implications are far from certain, but they will have far-reaching implications on trade, growth, inflation, and asset returns, well beyond the immediate impact on commodity prices.