



Zanetti Monday Missive 2022.08.29 Ukraine - War and Money

Hello Everyone,

In last week's missive, we laid out the premise that all is NOT well in China.

We suggested that China's economic woes could explain the Chinese Communist Party's (CCP's) military escalation against Taiwan.

Well, that missive prompted all kinds of comments from faithful readers about war, markets, politics, technology, and so on.

It's nice to have an informed client base. :>)

Your insights and comments sparked more thinking on my part.

Therefore, rather than letting the “war” subject just drop, let’s pursue the “politics-war-money” theme further. And, as always, let’s do this with an eye toward, “What does it mean to you and your retirement?”

Let’s turn our attention, however, from the Asian Theatre to the European Theatre; and let’s examine the events taking place in Russia and Ukraine---- and the trickle effects on both Europe and the US.

So, let’s get to it.

“War is politics by other means.”

~ Prussian General Carl von Clausewitz

“If trade stops, war starts.”

~ Jack Ma (Chairman of Alibaba, and Chinese business titan)

Most of us think of war in terms of tanks, submarines, and jets. But as Clausewitz and Ma so aptly have stated, politics, money, and war are inextricably linked.

In short, not all wars are kinetic. In other words, not all wars are shooting wars.

I believe there are five types of war currently being prosecuted:

- **Trade War**—think sanctions.
- **Tech War**—think communications, data, satellites, cyber-war.
- **Geopolitical Influence War**—think alliances.
- **Capital War**—think currencies, banking, markets.

- **Military**—think shooting war.

The common denominator that links all five is money.

And in terms of money, the first four (Trade, Tech, Geopolitical, Capital) have been “hot” wars for several years. And while winners and losers in the political, diplomatic, and financial space can affect your wallet, they don’t normally affect your existence. That is why kinetic war is the dominant subject of most history books.

And while the threat of war over Taiwan is evident (we covered this last week), it has not yet become a “hot war.”

The situation is very different in the European theater, where real bullets and missiles are flying daily in Ukraine. A lot is at stake, yet we hear little of it on the nightly news. That is a mistake.

The Ukraine War (errr, Special Military Operation) is now seven months old and the “long slog” we predicted back in the spring is playing out.

From our point of view, the US and NATO are involved in a proxy war helping Ukraine fight Russia. From Russia’s point of view, we are combatants fighting side-by-side with Ukraine.

And all five categories listed above are in play.

And to the victor goes the spoils.

So what would define victory for Russia?

I'd say the following:

1. Putin stays in power.

- It's no secret, NATO wants "regime change" in Russia.

2. Almost everything east of 1400 mile-long Dnieper River would be subsumed by the Russian Federation. (See map—the river connecting Kiev to Odesa is the Dnieper.)

- o The vast majority of the population east of the Dnieper speaks Russian)
- o This area (about the size of Iowa) would be a large "buffer" between NATO and Russia.
- o Russia would control the strategic Black Sea ports.



3. The “nub” of Ukraine that remains would declare itself “neutral,” thereby providing Russia an even bigger buffer vs. NATO.

4. Europe would start to de-Americanize and “Eurussia” would emerge.

What would define victory for the US/ NATO?

1. Russian retreats back to 2021 borders.
2. Ukraine remains united.
3. Ukraine joins NATO.
4. Putin is deposed.

Currently, the odds are in Putin's favor.

Russian's "artillery war" may be slow, but it limits Russian casualties, favors Russia's shorter supply lines, bankrupts Ukraine, and pressures Europe to abandon the eastward expansion of NATO.

But what if the war becomes a stalemate?

In this scenario, logistics trump tactics. Battlefield victories will not matter as much as finance and economics.

Who can bankrupt whom becomes the goal.

But don't confuse stalemate with stagnant. Like arm-wrestlers locked up at the beginning of a match, nothing seems to be happening except a bunch of groaning. But the arm wrestlers themselves know that one of them is gaining the advantage---even though the crowd can't see it.

I believe Russia is "winning" the current stalemate. US/NATO sanctions are not working. Russia's wealth has increased since the war started. Europe's economy is imploding.

Winter is coming and energy is short across the European Union.

The question is, "How long will Europe suffer for the Ukrainian people?" My guess is not long.

And without European support, Ukraine can't go on.

With that said, war is an unpredictable thing. Regardless of outcome, are there some economic constants of war that play out no matter who wins?

Yes...

- War is inflationary.
- War means trade routes are destroyed/damaged. **In modern terms, it means the reversal of globalization.**
 - No country will provide you resources to make bombs that will be used to bomb themselves.
 - Thus, instead of off-shoring production, we will see on-shoring and near-shoring.
 - Wages will rise as low-cost foreign labor will be replaced with higher cost domestic labor.
- War means government will “crowd out” ever more of the private sector.
 - Government spending and debt loads will explode.
 - Private enterprises will be co-opted by government to provide wartime products.
 - Taxation and regulation will expand in the name of national security.
- Commodity demand will increase.
- Capital intensive investments (think manufacturing) will fare better than financial investments (think banking).

I could go on, but that is probably enough to absorb for one day. Let's pick up on our war theme again next week. There is a lot more to cover.

Signed, Your Maybe-We-Should-Send-The-87,000-New-IRS-Agents-To-Ukraine-To-Terrorize-The-Russians Financial Advisor,

Greg

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