



**R&R Weekly Column**  
**By Brunello Rosa**



### Russian Invasion of Ukraine Nears, With Cyberwarfare Being A Possibility As Well

Tensions at the border between Russia and Ukraine have reached a point of almost no return during the past few days. As we discussed in [an in-depth analysis by John Hulsman](#), Russia has amassed at least 125,000 troops in the areas neighbouring Ukraine. Last week, Russia and Belarus [began a 10-day joint combat training exercise](#), which reinforces the impression that Russia is ganging up with its satellite states to prepare an internationally coordinated invasion of Ukraine. A large swathe of countries, including the US, have ordered their own diplomatic forces and citizens to leave Ukraine.

Most importantly, diplomatic efforts have intensified in the last few days in an attempt to dissuade Russian President Putin from invading Ukraine. French President Emmanuel Macron [flew to Moscow](#) and agreed with Putin that they “share security concerns” in Eastern Europe. US President Biden has recently spoken to Putin and warned that the US will react forcefully to a possible Russian invasion of Ukraine, a concept that will be repeated tomorrow by German Chancellor Scholz, when he [will travel to Kyiv and Moscow](#).

Tensions between Russia and Ukraine are not new of course. Recently they reached a peak in 2014, [when Russia annexed Crimea](#), following months of destabilisation of the Russian-speaking regions in east Ukraine (Donbass in particular). Eventually, the Minsk Protocol and the Minsk II agreement (consisting of 12 points, including an immediate ceasefire) emerged to at least freeze the situation and re-establish diplomatic relations. But progress has been modest. Even the election of Volodymyr Zelensk'kyj to the Ukrainian presidency in 2019 has not helped.


The issue on the table remains the same: Russia does not want Ukraine to become part of the various European communities [beyond the existing association agreement](#), let alone a member of NATO. The ideal solution would be Ukraine following the Finnish example, of remaining a neutral country (i.e. not becoming NATO member), even as Finland has become over time a member of the EU and even the Eurozone. But Russia does not trust the word of the West since 2004, when the Baltic republics, once part of the Soviet Union, joined NATO, leaving the Russian border directly exposed to NATO member countries in spite of all the reassurances provided to Russia that this would never happen. Since then, Russia has tried to re-gain the “geopolitical” depth that has always allowed Russia to prevent a foreign invasion.

The possibility of avoiding an open conflict still exists, but it is diminishing by the hour. The West is trying to use both sticks and carrots with Putin to change his calculus and lessen the attractiveness of an invasion, given the potential consequences that such an invasion might entail. But there is something the West would be ill-prepared for: the possibility of an asymmetric or covert act of war, such a domestic putsch in Ukraine or a large-scale cyber attack on key infrastructure.

How would the West respond to attacks that only supposedly can be attributed to Russia, attacks that could be covered by the usual “plausible deniability” disclaimer? Ukraine [is reportedly shoring up its cyber defences against a possible attack of this kind, given that Russia](#) is the leading country in the world in terms of cyberwarfare capabilities. After all, one of the most famous cyber attacks in recent history, the infamous Petya/NotPetya malware, which paralysed large multinational companies such as the shipping and logistic giant Maersk, originated from Russian attempts to destabilise the Ukrainian cyberspace.

One way or another, tensions between Russia and Ukraine are unlikely to settle soon. Policymakers, market participants and populations at large would be better to prepare for the worst to happen.

#### Our Recent Publications

 [Flash Review: The Riksbank Narrowly Keeps Its Policy Stance Unchanged in February](#), by Brunello Rosa and Nato Balavadze, 10 February 2022



 [GEOPOLITICAL CORNER: A Political Risk Guide to the Crisis in Ukraine](#), by John C. Hulsman, 8 February 2022

Looking Ahead

**The Week Ahead: EZ Q4 GDP Growth To Slow Down; Annual Inflation To Stay Unchanged In The UK, While Rising In China**

**In the EZ**, in Q4 the economy is expected to: i) expand at 0.3% q-o-q, slowing sharply from 2.2% in Q3 and ii) rise by 4.6% y-o-y, accelerating from 3.9% in Q3. Industrial production in December is likely to shrink less by -0.8% (p: -1.5%).

**In the UK**, in January, inflation is expected to remain at 5.4% y-o-y (p: 5.4%) and core inflation to rise slightly to 4.3% y-o-y (p: 4.2%), while monthly inflation is seen decreasing to -0.2% (p: -0.5%). The unemployment rate in December is likely to stay at 4.1% (p: 4.1%).

**In China**, annual inflation is seen falling to 1.0% (p: 1.5%), while monthly inflation in January is expected to rise to 0.5% (p: -0.4%).

**The Quarter Ahead: COVID Curbs Are Lifted; Government Officials Meet To Discuss The Ukraine Crisis; BoE Governor Criticized**

**A number of countries announced plans to relax COVID curbs and reopen to travellers.** Sweden, Denmark and Norway lifted all COVID restrictions, as the governments consider COVID as a disease that is “not a danger to society or a threat to public health”. Boris Johnson signaled an early end to COVID isolation rules. On the other hand, the WHO urges governments to “protect their people using every tool in the toolkit- not vaccines alone”.

**Biden met with Chancellor Olaf Scholz of Germany**, as Biden insists on halting the controversial pipeline Nord Stream 2 in the event of possible military action from Russia in Ukraine. During his first visit to Washington, Scholz reiterated that the response to Russia will be “untied and decisive” while avoiding mentioning the project explicitly.

**Macron visited Zelensky in Kyiv on Tuesday, a day after he met with Putin in Moscow.** Macron said Putin promised that he will not escalate the situation, while the official Kremlin denies the de-escalation deal over the Ukraine crisis. Biden tells U.S. citizens to leave Ukraine immediately, as the tension intensifies.

**The governor of the Bank of England came under attack following his comments that Britons should not ask for a pay rise** this year amid soaring inflation. Increasing wages could further boost inflation, leading to a vicious circle known as the “wage-price spiral” already experienced in the U.K. in the 1970s.

**Facebook and Instagram may be shut down in Europe**, due to European data regulations that prevent parent company, Meta, from transferring, storing and processing Europeans’ data on US-based servers. Importantly, the European Court of Justice ruled that the data-sharing pact between the EU and the U.S. over the data surveillance does not meet the EU’s protection standards.

Last Week’s Review

**Real Economy: Inflation Increased In The US; Q4 GDP And Business Activity Accelerate In The UK**

**In the US**, in January: i) inflation rose to 7.5% y-o-y (c: 7.3%; p: 7.0%); ii) core inflation increased to 6.0% y-o-y (c: 5.9%; p: 5.5%); iii) monthly inflation stood unchanged at 0.6% (c: 0.5%; p: 0.6%); and iv) unemployment rate increased slightly to 4.0% (c: 3.9%; p: 3.9%).

**In the UK**, preliminary estimates for Q4 GDP showed that the economy grew by: i) 1.0% q-o-q (c: 1.1%; p: 1.0%); and ii) 6.5% y-o-y (c: 6.4%; p: 7.0%). In January, the IHS Markit/CIPS UK Composite PMI was up to 54.2 (c: 53.4; p: 53.6), as i) Manufacturing PMI rose to 57.3 (c: 56.9; p: 57.9); and ii) Services PMI rose to 54.1 (c: 53.3 p: 53.6).

**In Sweden**, the Riksbank left its repo rate unchanged at 0.0% as expected.

**Financial Markets: S&P 500 Unchanged Amid Surging Inflation; UST Yields Reach 2.0%; Potential Fed Hikes Weigh On Equities**

**Market drivers:** Last week’s main market movers that strengthened investors’ sentiment were: i) strong U.S. labour data; and ii) improved earnings performance with Alphabet and Amazon reporting big gains. Yields climbed as inflation surprised to the upside.

**Global Equities** rose w-o-w (MSCI ACWI, 1.1%, to 726). The US S&P 500 Index were virtually unchanged (+0.0% w-o-w, to 4,504) which reflects that investors have digested US inflation reports as well as expected aggressive Fed rate hikes. In the EZ, shares also increased due to stronger earnings compared to last week (Eurostoxx 50, +1.9% w-o-w, to 4,164), despite US rising inflation data. In EMs, equities rose (MSCI EMs, +2.4%, to 1,251). Volatility rose to 24.1 (VIX S&P 500, 52w avg.: 21.0; 10y avg.: 18.4).

**Fixed Income:** w-o-w, UST yields increased to 2.0% (+8.5 bps) for the first time since 2019 following the inflation data release. German 10-year bonds were up too (+4.5 bps, to 0.25%) as investors watch closely a key inflation gauge rising and anticipate ECB to raise rates.

**FX:** w-o-w, the US Dollar Index rose (DXY, +0.3%, to 95.78; EUR/USD -0.5%, to 1.139), lifted by hawkish messages from the Fed. In EMs, currencies increased against the USD compared to last week. (MSCI EM Currency Index, +0.4% w-o-w, to 1,747).

**Commodities:** w-o-w, oil prices were slightly down (Brent, +1.1% to 92.2 USD/b). However, oil prices climbed above \$90 per barrel – the highest level in nearly eight years as IEA reported oil markets were tight. W-o-w, Gold prices rose (+1.0% to 1,826 USD/Oz) boosted by rising inflation worries.



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## Abbreviations, Acronyms and Definitions

a	Actual	LN	Northern League, Italy
AKP	Justice and Development Party, Turkey	MSS	Five Star Movement, Italy
ann.	annualized	m-o-m	Month-on-month
ARS	Argentinian Peso	mb	Million barrels
avg.	Average	mb/d	Million barrels per day
bn	Billion	MENA	Middle East and North Africa
BoC	Bank of Canada	MHP	Nationalist Movement Party, Turkey
BoE	Bank of England	mn	Million
BoJ	Bank of Japan	MPC	Monetary Policy Committee
bpd	Barrels per day	NAFTA	North-American Free Trade Agreement
bps	Basis points	NATO	North Atlantic Treaty Organization
BS	Balance sheet	OECD	Organization for Economic Cooperation and Development
c	Consensus	Opec	Organization of Petroleum Exporting Countries
C/A	Current account	p	Previous
CB	Central bank	P2P	Peer-to-peer
CBB	Central Bank of Bahrain	PBoC	People's Bank of China
CBK	Central Bank of Kuwait	PCE	Personal Consumption Expenditures
CBT	Central Bank of Turkey	PE	Price to earnings ratio
CDU	Christian Democratic Union, Germany	PM	Prime minister
CNY	Chinese Yuan	PMI	Purchasing managers' index
CPI	Consumer Price Index	pps	Percentage points
DJIA	Dow Jones Industrial Average Index	pw	Previous week
DJEM	Dow Jones Emerging Markets Index	QCB	Qatar Central Bank
d-o-d	Day-on-day	QAR	Qatari Riyal
DXY	US Dollar Index	QE	Quantitative easing
EC	European Commission	q-o-q	Quarter-on-quarter
ECB	European Central Bank	RE	Real estate
ECJ	European Court of Justice	RBA	Reserve Bank of Australia
EIA	US Energy Information Agency	RRR	Reserve Requirement Ratio
EM	Emerging Markets	RUB	Russian Rouble
EP	European Parliament	SWF	Sovereign Wealth Fund
EPS	Earnings per share	tn	Trillion
EU	European Union	TRY	Turkish Lira
EUR	Euro	UAE	United Arab Emirates
EZ	Eurozone	UK	United Kingdom
Fed	US Federal Reserve	US	United States
FOMC	US Federal Open Market Committee	USD	United States Dollar
FRB	US Federal Reserve Board	USD/b	USD per barrel
FX	Foreign exchange	UST	US Treasury bills/bonds
FY	Fiscal Year	VAT	Value added tax
GCC	Gulf Cooperation Council	VIX	Chicago Board Options Exchange Volatility Index
GBP	British pound	WTI	West Texas Intermediate
GDP	Gross domestic product	WTO	World Trade Organisation
IMF	International Monetary Fund	w	Week
INR	Indian Rupee	w-o-w	Week-on-week
IPO	Initial public offering	y	Year
IRR	Iranian Rial	y-o-y	Year-on-year
JPY	Japanese yen	y-t-d	Year-to-date
k	thousand	ZAR	South African Rand
KSA	Kingdom of Saudi Arabia	2y; 10y	2-year; 10-year



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