Russia/Ukraine FAQ: Market Status

March 10, 2022

This FAQ is designed to help provide perspective on the current Russia/Ukraine crisis.

Q. What is the general trading status of Russian securities?

A. In line with the practices of major index providers and other data providers, SEI is defining Russian-related securities as:

i) a security listed on an exchange domiciled in Russia, Ukraine or Belarus;
ii) a security listed on an exchange outside of these countries but that derives an extensive portion of its business from Russian, Ukrainian or Belorussian operations;
iii) debt issued by Russian, Ukrainian or Belorussian public or private entities.

As of March 8, 2022:

- Russian markets are closed. Russian securities are illiquid.
- Ukraine's state stock is effectively closed.
- Leading into the Russia/Ukraine conflict, SEI's portfolios generally had small allocations to Russian securities. Mark-to-market valuations since then have made them smaller.
- In the context of a client's total portfolio (assuming a well-diversified strategy), the exposures to Russian securities are not significant.
- Trading on Russian companies with overseas listings have also been halted on the Deutsche Boerse, New York Stock Exchange, and NASDAQ.

Q. What is the status of Russian securities in benchmark indexes?

A. Index providers are removing Russian securities from benchmarks. This will result in downward pressure on pricing if/when trading resumes.

- FTSE Russell removed Russian stocks from its indexes effective March 7.
- Russian securities will be withdrawn from the MSCI emerging-market indexes on March 9.
- Stoxx plans to drop Russian companies from its indexes on March 18.
- S&P is also considering eliminating Russian equities from its equity benchmarks.
- Russian debt will be removed from all of the JP Morgan fixed-income bond indexes, effective March 31. Russia made up around 6% of the J.P. Morgan local-currency emerging-market bond index as of February 28.
- Inclusion of Ukrainian local-currency government bonds in the JP Morgan government bond index-emerging markets index, which was due to happen on March 31, will be on hold during the market disruption.

Q. Does SEI still have exposure to Russian securities?

A. Yes. Any investment manager that held Russian securities when Russia closed its markets still holds them. The most significant exposures to Russian securities within a diversified portfolio are within the emerging-market debt and equity asset classes. The exposure within each of these asset classes is small. With Russian stock and bond markets closed and sanctions in place, Russia securities are now priced using estimated values (known as mark-to-market pricing). In a volatile market, the range of what would potentially be a reasonable estimate is necessarily far broader than in a stable market. Most securities are not trading, and direct exposure is being dropped from the benchmarks. Our holdings are being written down to reflect the lack of liquidity (and in some cases solvency). Given valuation losses since the invasion, and the allocation to these asset classes within a diversified portfolio also being small, overall exposure at the total-portfolio level is quite small.

Equity-specific example

- London has long been an offshore trading hub of choice for Russian oligarchs and businesses.
- The London Stock Exchange has suspended trading in 27 Russian-linked companies, including its largest lender Sberbank and energy giant Gazprom.
- Sberbank was down 99.72% year-to-date to trade for around a single penny on Wednesday, while Gazprom was down 93.71%, Lukoil 99.2%, Polyus 95.58%, Rosneft 92.52% and EN+ 20.51%.Other companies blocked from trading in London include Lukoil, Polyus and EN+, while the subsidiary of VTB, Russia's second-largest bank, was suspended last Friday.

Bond-specific example

- The U.S. barred investors from buying Russian government bonds sold after March 1 in the primary market or the secondary market, where they trade after their initial sale. The European Union's sanctions also block new loans or credit to sanctioned entities.
- Sanctions that target Russian central-bank reserves and banks accessing the SWIFT payments system present further risks. Russia responded by banning Russian residents from transferring foreign currency abroad for new loans, although the central bank said the rule doesn't apply to payments on existing debt.
- The Russian state will likely fail to pay foreign bondholders a coupon due on a bond for the first time since 1998. Fitch Ratings recently warned of an imminent default and downgraded its rating on the country's sovereign debt.

  Our portfolio management and compliance teams continue to actively monitor the situation. A more detailed FAQ on this topic is under development.

Q. What are the implications of sanctions?

A. Sanctions impose a variety of restrictions on trading:

- The U.S. and other jurisdictions have imposed various restrictions on transacting in certain securities of Russian issuers, including prohibiting (i) the purchase of newly issued Russian government bonds, (ii) the purchase of newly issued equity or debt of certain Russian companies, or (iii) the purchase or sale of new and existing equity or debt of other Russian companies.
- The Russian central bank has banned overseas institutions from selling local securities on the Moscow Exchange.

Asset managers have been down this road before. In 2017, the Trump administration imposed sanctions on Venezuela, barring the trading of new debt issued by that government and its state oil company in U.S. markets. Those bonds were among the most-traded securities in emerging markets.

Q. Is SEI complying with the sanctions against Russia?

A. Yes, SEI has taken steps to comply with all applicable sanctions.

Q. Has there been any impact to SEI's business and operations?

A. We have not experienced any degradation in our operational integrity. Based on the current government threat guidance and recommended actions, we believe that our current technology infrastructure and contingency plans will enable us to maintain the integrity of our operations and services consistent with our service-level commitments.

Additionally, our standard procedures involve screening against sanctions lists and compliance with those financial tools employed by governmental agencies, so even though the volume of newly sanctioned persons and entities is higher than usual, we continue to operate in a "business as usual" manner with respect to those activities.

Q. What is SEI's current investment outlook in light of Russia's Invasion of Ukraine?

A. We take a high degree of comfort from the fact that direct exposure to Russian assets was already quite low across capital markets before the invasion-induced selloff. Still, Russia and Ukraine account for a significant share of critical commodity production. It's important to consider second- and third-order consequences, including those resulting from sanctions and other associated actions, which could reverberate through markets for the foreseeable future.

We believe the primary impact on economic growth will be transmitted via commodity markets, with Europe sustaining the greatest impact, although GDP growth will likely slow in the U.S. as well. While the monetary and fiscal response will likely be limited, the odds of an aggressive tightening of monetary policy this year are now considerably lower. There's a gap between the market-implied terminal Fed funds rate and the Fed's own projections, and we suspect the Fed's higher terminal rate is more likely to prevail. Even so, milder tightening could mean that the Federal Reserve remains behind the curve on taming inflation. We still think market expectations for a return toward more normal inflation conditions over the next couple years will need to be revised upward.

We are humble enough to know that skilled forecasting—even where it exists—does not warrant wholesale changes to portfolio allocations based on tactical views. This is particularly important to understand in the context of fast-moving geopolitical events.

Efficient strategic portfolio construction through broad-based diversification helps to prepare our portfolios for adverse events before they happen. It's much cheaper to buy insurance before the flood. By acknowledging both risk and uncertainty, we seek to construct resilient portfolios designed to achieve success across a wide range of economic and market outcomes, not just benign environments where we can rely on strong growth and well-behaved inflation.

Today, we generally remain positioned for continued economic growth and a reflationary backdrop that can be expected to benefit companies exhibiting earnings momentum, attractive valuations and strong financial characteristics.

Q. What should investors do?

A. Geopolitical events are just one example of the many risks that call for sound portfolio diversification. A well-diversified portfolio will include assets that can help to offset the downside risks posed by unexpected market stress, including geopolitical events like the crisis unfolding now in Ukraine.
We believe the most important thing investors can do to ensure peace of mind is to confirm that their strategic portfolio is aligned with their investment objectives and tolerance for risk

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