The War in Ukraine, Commodity Prices and Inflation
What do Investors Do?

At the time of writing, the brutal and tragic invasion of Ukraine by Putin's Russian military has now continued for close to four weeks. The awful loss life, both Ukrainians, and of probably naive Russian conscripts, is truly horrific.

Most economists insist that sooner or later, sanctions will cripple Russia's economy.

However, these same bans on trading with Russia are sending convulsions through the rest of the global economy, and one thing seems certain; this year's higher inflation, driven by the recovery from the Covid-19 pandemic, is being exacerbated by the rapid price increases in oil and gas. The prices of other commodities that Russia and Ukraine export, such as wheat and corn, have increased as well.

In the week following the start of the war, the global prices of oil and natural gas rose sharply, especially gas in Europe.

In addition, the prices of key mineral and food commodities increased, including nickel, palladium, neon, wheat, and corn.

It is probably fair to say that these increases reflected fear and risk, rather than actual sanctioning or disruption of trade.

Investors also worry that there could be new events that would disrupt trade in commodities, including European reductions in purchases of Russian oil and gas, or possibly a Russian decision to limit or stop exports of key commodities.

Higher global commodity prices, if sustained or exacerbated, are likely to cause accelerated and prolonged high inflation in many countries, especially in Europe, with its reliance on oil, gas, and grains from Russia and Ukraine.

Higher commodity prices can also weaken economic growth.

Prior to the invasion, some of the world's leading central banks were already on a course toward tighter monetary policy, a reaction to the sharp increase in inflation in many countries.

However, while the war could exacerbate inflation, it could also weaken growth, which will pose a dilemma for the central bank policy-makers in the months to come.

U.S. inflation is now at a nearly 40-year-high. This is leading many investors to wonder how to protect themselves against inflation.

In general, many experts recommend investing smartly to hedge against inflation.

Suze Orman recently wrote on her site that you should;

'Keep investing in stocks' to hedge against rising costs, and Ramit Sethi noted;

'Investing is the single most effective way to get rich. Inflation can be bad for individuals when you just keep your money sitting in a bank account and do nothing else with it.'

But what kinds of companies should you be investing in? Here's what Warren Buffett has said over the decades.

2015

‘The best businesses during inflation are the businesses that you buy once and then you don’t have to keep making capital investments subsequently, while you should avoid any business with heavy capital investment.’

2009

‘If you’re the best teacher, if you’re the best surgeon, if you’re the best lawyer, you will get your share of the national economic pie regardless of the value of whatever the currency may be’ he said. After that, he says, ‘the second best protection is a wonderful business,’ which means a company in which the products are in demand even if the company does have to raise prices.

There have been thousands of these pearls of wisdom from Warren Buffet over the years, but perhaps the best thing many individual investors can take from Buffet’s comments is that rather than trying to pick individual stocks, whether we’re in an inflationary period or not, you should go with the tried-and-tested index funds, to have and to hold.

In 2021, at a shareholder meeting, Buffett declared that ‘I do not think the average person can pick stocks,’ and noted that he recommends the S&P 500 index fund to ‘have for a long, long time’.

Even Elon Musk tweeted earlier this week ‘As a general principle, for those looking for advice from this thread, it is generally better to own things or stock in companies you think make good products, than dollars when inflation is high’.

Essentially, they are all saying the same thing. The safe feeling of holding on to cash in the bank will doom investors to losses.

To ride the storm of war, worry and inflation, staying invested in quality assets for the duration is actually the safest approach in the longer term.