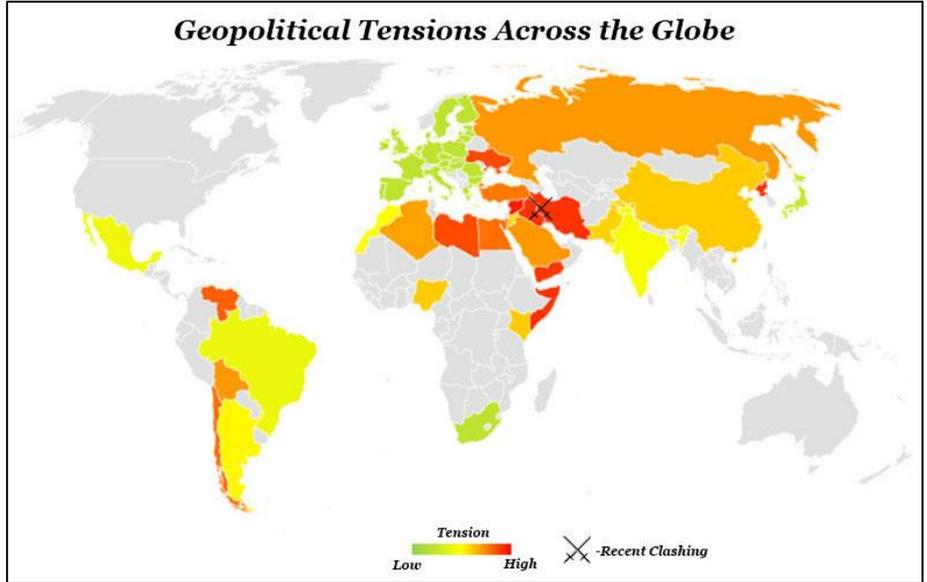


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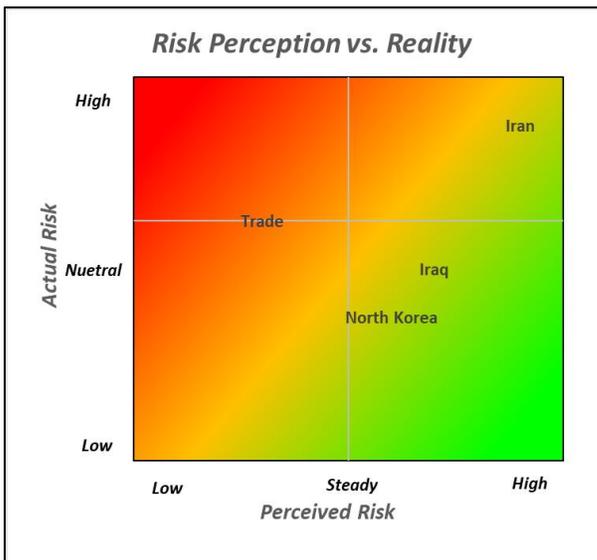
Geopolitics has been one of the biggest drivers of global markets in the first few weeks of 2020

• Academy has been doing its best to keep you updated on what to expect out of Iran and Iraq. We've issued timely [SITREP's](#), [Podcasts](#) and [T-Reports](#). Rarely has access to our Geopolitical Intelligence Group ("[GIG](#)") been so valuable to our clients as we've helped navigate these dangerous and volatile geopolitical and market events. We explore this issue in our Front and Center section, but Academy's current view can be best summarized as:

- The region will be safer in a couple of months than it was a couple of months ago.
- The cost and risk associated with that positive outcome will be low.
- We anticipate a continued asymmetric response from Iran.



That view is why we highlight both Iran, Iraq, and even North Korea as potential positive surprises in our "**Perception vs Reality**" chart. This chart tries to identify situations where the consensus view is very different than our view. The market is pricing in too much risk on the economic front. That has translated into too much hedging in the markets (many investors and traders have been buying treasuries as a hedge against renewed escalation in the region). The view that we are headed towards better and more sustainable relationships in the region (and with North Korea) isn't without its risks, and may be difficult to agree with, given the amount of negativity on the region being disseminated, but that is precisely why we see it as an opportunity for positive surprises.



The Phase I Trade Deal was signed this week. We still view this deal as more of a **Trade Truce** than a Trade Deal. We are shifting our view on trade, from a potential positive surprise to a potentially negative one as can be seen in our "**perception vs reality**" chart. Markets may now be pricing in too much good news on the trade front globally and would be better served by preparing for disappointment.

Regarding trade with China, we have seen that the President often felt the need to confront China and even threaten them during the Phase I negotiations. There is no reason to believe that he won't revert to that strategy (since he clearly believes it worked) and that could disrupt markets over time. Again, let's not forget for a minute that this administration has labelled China as a "[Strategic Competitor](#)" and will act accordingly. While we are currently playing nicely in the global sandbox with our other trading partners, that may be less stable than markets are pricing in.

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Front and Center - The Global Impact of the Events in Iraq/Iran

In our most recent [Around the World](#) report before the holidays, our GIG’s consensus was that as sanctions put pressure on the Iranian economy, the regime would continue to lash out via proxy forces to engage with the U.S. militarily in the attempt to extract global sympathy and have sanctions lifted. To say this plan backfired on the regime is an understatement. What we are seeing in the streets of Tehran today is a far cry from what Supreme Leader Ayatollah Ali Khamenei anticipated when his most important General, Qassem Soleimani, executed the proxy campaign against the U.S. at the end of December. As we reported in our December 30 [SITREP](#), Iran crossed a line when an attack against a joint U.S./Iraqi military facility resulted in the death of an American contractor.



The U.S. responded with airstrikes against Iranian backed militia, but that action alone did not get to the root of the problem. On January 2, we reported in our SITREP entitled [A Game Changer with Iran](#), that the U.S. drone strike against Qassem Soleimani, the leader of Iran’s Islamic Revolutionary Guard Corps, was intended to “cut the head off of the snake” and eliminate the individual responsible for not only hundreds of U.S. casualties in Iraq, but also the IRGC-Quds force sponsored proxy campaign across the Middle East.

On January 7, Iran responded by firing over a dozen ballistic missiles at two US-Iraqi military bases. No casualties were reported, and Iran appeared to immediately deescalate the situation saying that “Iran took & concluded proportionate measures in self-defense under Article 51 of UN Charter.” However, with tensions seemingly cooling, what happened next further complicated things for the Iranian regime.

In an apparent case of tragic human error, an Iranian air defense battery shot down a Ukrainian commercial airliner killing all 176 people on board. After initially denying it was responsible, Iran admitted over the weekend that it did mistakenly down the aircraft. Almost instantaneously, the outpouring of grief in the streets of Tehran as a result of the killing of Soleimani turned to anger towards the regime. The protests that have occurred have been forcefully interrupted by Basij paramilitary units using live ammunition. As the Iranian people shout “death to the dictator” amid tear gas and gunfire, one must conclude that it is time for Iran to look inward to address the discontent.

Will these events provide the U.S. an opportunity to reengage with Iraq and stop the spread of Iranian influence in Baghdad and beyond? The recent vote to expel U.S. forces likely included many lawmakers who were strong armed into voting by the PMF (Popular Mobilization Force), an Iranian backed proxy militia in Iraq. However, the U.S. is unlikely to leave Iraq anytime soon, a fact that many Iraqis privately support. Risks of a resurgent ISIS and Iranian backed Shia militia further entrenching itself in the local governments are too great. Rather, General Marks believes that this is OUR time to fix the relationship with Iraq and rebuild it to help counter Iranian influence in the region.

The question remains - how will other isolated dictators (in Syria, Russia, North Korea, and Venezuela) view the events of the past two weeks and will U.S. action bring them back to the negotiating table or will they consolidate power and look to other countries for support?

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How Will Other Dictators React to U.S. Action?

Syria

On January 7, President Putin met with President Assad before making a stop in Turkey to open the TurkStream pipeline, a joint project to deliver natural gas to Turkey and Europe. In Putin's first visit to Damascus, he declared "...enormous progress has been made in the Syrian conflict to restore the country's territorial integrity." As we predicted in our most recent Around the World, Russia will make the Middle East, particularly Syria, a more permanent stronghold moving forward. The historical relationship, strategic location, and access to the port of Tartus ensures a Russian presence for years to come. Recent weapon sales to Egypt and Turkey further underscore this point. To remain in power, Assad will stay close to Putin and is likely to side with Russia in discouraging Iranian proxy activity against U.S. personnel in Syria. Putin does not want to further complicate matters in the region which could result in a larger U.S. presence.

Russia

On Wednesday, President Putin announced sweeping constitutional reforms that would ensure his continued influence and power even after the end of his term. As a result, Prime Minister Dmitry Medvedev and his entire cabinet resigned abruptly following the announcement.

*"Fair to say our GIG has been predicting the "limitless" consolidation of Putin's power for years. Absolutely no surprise. Medvedev's resignation was inevitable...no appearance of resistance and acknowledgement that he's irrelevant. It sure beats a poison dart to the throat." **General Marks***

North Korea

The U.S. strike against Soleimani further demonstrated to Kim Jong-un that the U.S. is willing to act. Kim believes the only thing standing between him and a U.S. Reaper drone is his nuclear capability. The world never received the "Christmas gift" Kim promised before the holidays, which many expected would be a long-range ballistic missile test. While U.S. action will likely make Kim think twice before doing something rash, he will be in no hurry to give up his nuclear program. This may also result in North Korea looking to China and Russia for help with sanctions relief.

*"Kim will keep a low profile as a war will bring an end to Kim and his regime." **General Chinn***

Venezuela

Juan Guaido has been calling for more protests in Venezuela since being blocked from entering the National Assembly before the election of new leadership. Maduro further consolidated his power by taking control of the Assembly and now Venezuela has two competing leaders for the presidency and head of the nation's legislative body. Recent U.S. action may be factoring into Maduro's desire to consolidate power.

"I don't see any changes in Venezuela unless a U.S. citizen is killed there, and I am sure President Maduro and his team are doing all they can to safeguard U.S. citizens. The stalemate continues in Venezuela as Maduro remains in power and Guaido cannot get enough popular/military support to lead the country as the interim President, ensuring free and fair elections.

*Towards the end of last year, Maduro welcomed dollarization to combat hyperinflation/financial collapse, meaning there will be two currencies in Venezuela, the bolivar and U.S. dollar. Cuba, Ecuador, Panama, and El Salvador are other countries in the region that operate under dollarization Like Cuba, Venezuelans are currently getting support from relatives who have left and are sending money back to Venezuela - keeping the economy afloat. Dollarization helps with stability in Venezuela and will help Maduro maintain power." **General Chinn***

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Markets at a Glance – Equities, Asian Currencies Surge Across the Globe, Bonds do Little

| Country | Currency* | 1 Week | 1 Month | 10 Yr Yield* | 1 Week | 1 Month | Stock Index | 1 Week | 1 Month |
|---------------------|-----------|---------|---------|--------------|--------|---------|-------------|--------|---------|
| United States | 97.23 | -0.07% | 0.06% | 1.78 | -0.09 | -0.04 | 3,289 | 1.11% | 3.80% |
| Asia Pacific | | | | | | | | | |
| China | 6.9 | 0.64% | 1.74% | 3.09 | -0.04 | -0.11 | 4,167 | 1.32% | 5.00% |
| Korea | 1,156 | 1.26% | 1.33% | 1.70 | 0.14 | 0.06 | 2,231 | 3.70% | 2.80% |
| India | 70.8 | 1.23% | -0.01% | 6.63 | 0.07 | -0.16 | 12,343 | 2.64% | 2.12% |
| Indonesia | 13,695 | 1.47% | 2.11% | 2.87 | -0.02 | -0.03 | 6,283 | 0.93% | 1.39% |
| Philippines | 50.7 | 0.01% | -0.22% | 2.63 | -0.01 | -0.10 | 7,664 | -0.93% | -2.71% |
| EMEA | | | | | | | | | |
| Russia | 61.4 | -0.32% | 2.30% | 2.99 | -0.05 | 0.02 | 3,133 | 0.73% | 4.56% |
| Saudi | 3.8 | 0.00% | -0.03% | 2.80 | -0.15 | -0.05 | 8,433 | 3.80% | 5.33% |
| South Africa | 14.4 | -1.61% | 0.97% | 4.77 | 0.11 | -0.25 | 58,064 | 1.29% | 2.32% |
| Turkey | 5.9 | 0.56% | -1.19% | 5.68 | -0.35 | -0.56 | 120,939 | 7.14% | 9.47% |
| Ukraine | 24.1 | -0.28% | -2.66% | 5.95 | -0.21 | -0.75 | 505 | -0.96% | -1.10% |
| Americas | | | | | | | | | |
| Argentina | 60.0 | -0.23% | -0.23% | 19.42 | -0.89 | -2.34 | | | |
| Brazil | 4.2 | -2.91% | -1.84% | 3.62 | -0.06 | -0.08 | 116,414 | 0.14% | 3.42% |
| Colombia | 3,299 | -1.60% | 2.28% | 3.03 | -0.04 | -0.06 | 1,649 | -0.49% | 1.10% |
| Mexico | 18.8 | 0.12% | 1.31% | 3.20 | -0.04 | -0.07 | 44,453 | 0.67% | 0.22% |
| Venezuela | 70,587 | -29.82% | -52.63% | | | | 1,649 | -0.49% | 1.10% |

| Commodities | | | | | | | | |
|--------------------|--------|---------|-------|--------|---------|---------|--------|---------|
| Oil | 1 Week | 1 Month | Gold | 1 Week | 1 Month | Bitcoin | 1 Week | 1 Month |
| 57.81 | -3.02% | -3.76% | 1,556 | -0.01% | 5.41% | 8,822 | 10.21% | 21.84% |

U.S. Currency is DXY. China, Korea and India are local currency bonds, the remainder are U.S. denominated bonds. Bloomberg data as of 1/16/20.

Stocks Surge Across the Globe. Despite the turmoil in the Middle East, stocks have had strong weekly and monthly performance. Emerging markets continued with our theme from the last Around the World that **it's an Emerging Market World!** Much of the surge in **Asian currencies** and global stocks can be attributed to the Trade Truce finally announced late last year, which unleashed some pent-up demand. Seasonal factors also helped markets as U.S. investors started to chase riskier assets in late December and continued to do so in early January.

Saudi Arabia deserves some special attention. Not only did their stock market do well during this period, but their bonds performed well. **We will be expanding our coverage of Middle East issued bonds** as we see opportunities there, especially if we are correct in our assessment of the risk/reward and positioning in the region.

Ukraine. While the Ukrainian currency gave up some gains (it had a great 2019) and the stock market pulled back, its bonds have done extremely well, with its 10-year yields dropping 75 bps in the past month. That is the most impressive return of any bond market we currently track.

Turkey regains some ground. Turkey was a noticeable outlier in the last report, where it hadn't done as well as many other emerging markets. That reversed course as its currency, bonds, and stocks all soared. Turkey has been an area of concern for us, and little has changed on the geopolitical front, but markets quite clearly disagreed with our nervous position on the country and its leadership.

Oil Down. Oil, which did spike at the peak of tensions, is down on the week and the month. That makes the performance of many emerging markets, especially Saudi Arabia, that much more impressive.

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Dusting off the Bitcoin “how to” guides. Bitcoin is once again gaining some traction and while the hype surrounding it is nothing like it was back when it was breaking to new highs daily and nearly broke \$20,000, there is an undeniable buzz about it again. **It is impressive that while gold was weak last week as tensions eased, Bitcoin continued to surge.** There has been discussion around the fact that half of all bitcoin has been mined and whether or not this fact caused the resurgence. There has also been some discussion that a few so-called “whales” have pushed on the market as the halving story (combined with geopolitical tensions) created a good opportunity to push it higher. Worth watching, especially as there is more work being done on **Central Bank stable coins and digital currencies** (special thanks to the digital currency team at the IMF for helping us on this).

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