The Ukraine War and Equities: Surprising Findings on Defense, Commodities, & Tanker Stocks

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As we mark the somber first anniversary of Russia's invasion of Ukraine, I thought it would be interesting to have a look at what equities have been impacted by this brutal and very unnecessary war. My first thought was that defense or drone stocks would be slam-dunk outperformers. I also figured there would be several resource companies that may have done well if they produce key commodities where Russia was a dominant player, assuming the company in question wasn't actually operating in Russia where it likely would have had to forego its assets. What I found surprised me.

Defense and Drone Companies

I first looked at the biggest U.S. defense and drone stocks and did not find what I expected at all. Let's start with Raytheon Technologies Corporation (NYSE: RTX), and Lockheed Martin Corporation (NYSE: LMT) because not only are they two of the largest market cap defense contractors (US$145 billion and US$122 billion, respectively) but they also count as two of the biggest manufacturers of military drones. Excluding dividends, Raytheon is actually down 3.5% over the last year, while Lockheed Martin rose 10.5%. Granted a positive 10.5% return over the last year did materially outperform the S&P 500, which was down 9% over the comparable time period, I was expecting a much better return.

Given the ever-increasing use and impact of drones in Ukraine, I thought I'd look at a company that was almost exclusively focused on this sector alone to see if there was any difference in performance from the multi-faceted defense names. I choose Kratos Defense & Security Solutions Inc. (Nasdaq GS: KTOS). Not only because of the name but the Company has contract ties to the U.S. Department of Defense, and roughly 25% of Kratos' revenue comes from its "Unmanned Systems" division. This all sounds good on paper but the Kratos share price saw a dismal 40% loss over the last 12 months. Even with that pummeling, Capital IQ has the stock trading at 33.2x Forward P/E. I don't think I'll be putting this name on my list as a hedge against the war in Ukraine dragging on for a lot longer.

(Note: An Unmanned System (US) or Unmanned Vehicle (UV) can be grouped into four primary types: (1) in the air, as Unmanned Aerial Vehicle or System (UAV or UAS), commonly known as a "drone"; (2) on the ground, as Unmanned Ground Vehicle (UGV); (3) on the water surface, as Unmanned Surface Vehicles (USV); and, (4) in the water, as Unmanned Underwater Vehicles (UUV).)

Commodity Stocks

Time to change gears and start looking at commodities. Despite oil, natural gas, and refined products accounting for Russia's largest value of exports, I chose platinum as the first place to look given Russia's Norilsk Nickel (MISX: GMKN) accounts for 10-12% of the world supply, which is a higher percentage of global market share than oil or natural gas. For reference, Nornickel, as it is also known, is also the world's largest palladium and refined nickel producer, plus a top-ten producer of copper as well. The best platinum/palladium surrogate I could find was Sibanye-Stillwater (NYSE: SBSW), another of the world's largest primary producers of platinum and palladium. This stock is down an abysmal 57% over the last 52 weeks. With platinum prices down 10% year-over-year and palladium down 41%, it appears the market isn’t reeling from the impact of Russian supply disruptions in these particular metals.

Early in the conflict, natural gas was making a lot of headlines, with European prices spiking to unimaginable heights and all the subterfuge around the two Nord Stream pipelines. The leading European benchmark is Dutch TTF Gas and it is priced in Euro per megawatt hour (€/MWh). Despite this benchmark price peaking in late August 2022 at €339, it is currently trading below €50, even lower than it was trading before this whole mess began. Meanwhile, Henry Hub gas prices in the U.S. also peaked in August at US$9.71/MMbtu (Metric Million British Thermal Unit) but iscurrently transacting around US$2.70, also below year-ago levels. Thus, it will probably come as no surprise that big natural gas producer ARC Resources Ltd. (TSX: ARX) in Canada and EOG Resources, Inc. (NYSE: EOG), a leading gas producer in the U.S., are trading at pretty much the same price they were last year at this time. Or maybe it is a surprise as one might think they’d be down year over year based on the commodity price.

Oil and Refined Products Companies

The question is, did anyone’s share price benefit from this unfortunate event? There were a few that I found and they were all oil and refined products related. The most well know name of the bunch is Exxon Mobil Corp (NYSE: XOM) which returned an impressive 41% excluding dividends over the last year. We all know Exxon is a behemoth, and there could be lots of reasons other than Russian supply disruptions that could have influenced the share price but other integrated global giants like Shell PLC (formerly Royal Dutch Shell) (LSE: RDSA | NYSE: SHEL) and BP plc (LSE: BP | NYSE: BP) all had similar one-year performances.

Albeit they all had setbacks of some form in the last year due to the fact that they had to write off or choose to sell (for essentially zero) some Russian assets. Regardless, the large integrated oil companies outperformed the rest of the sector for the most part.

Tanker Stocks

But the big outperformers were the oil and refined product tanker stocks. The returns in this category were what I would have expected from the defense stocks, which as we discussed above, were relatively disappointing. There are many to choose from but I looked at two that I have traded in the past but did not have the foresight to continue holding them. The first company is Scorpio Tankers Inc. (NYSE: STNG), a Monaco-based international transporter of refined petroleum products with a fleet of 113 vessels. This stock returned a whopping 255% over the last 12 months.

The second company is Frontline Ltd. (NYSE: FRO) a Bermuda-based company providing marine transportation of crude oil and oil products with a fleet of roughly 70 tankers. Frontline returned 97% excluding dividends since the end of February 2022. This quote from Scorpio's Q4, 2022 results pretty much sums up why this sector has performed as well as it has:

> *"…the volatility brought on by the ongoing conflict in Ukraine, which has resulted in the implementation of sanctions on the export of Russian crude oil and refined petroleum products, has continued to disrupt supply chains for crude oil and refined petroleum products, changing volumes and trade routes, and thus increasing ton-mile demand for the seaborne transportation of refined petroleum products."*

Scorpio’s Q4/2022 vessel revenue increased 211% as a result and needless to say, the market paid attention even though I did not.

Today I’ve only scratched the surface of what ramifications the Russian invasion of Ukraine has had on markets and stocks around the world. What I truly hope is that I won’t be doing this again a year from now.