Russia and the USD

- Gulf of Oman not the only place tensions are rising
- USD has typically been a beneficiary of Russian military activity, while European currencies have suffered
- Both gold and oil have typically suffered in aftermath

While events in the Gulf of Oman are capturing the market's attention at present (oil prices are higher this morning despite the Fed related price moves seen elsewhere overnight), it’s worth noting that this is not the only place geopolitical pressures are increasing.

In particular, tensions between Russia and Georgia have risen sharply over the past week. Although there is no suggestion of a repeat of the events of 2008, it’s still interesting to consider how the FX markets have responded to Russian military activity in the past.

1: The Russia-Georgia War of August 2008

Following an announcement on August 5 by a Russian spokesman that it would defend Russian citizens in South Ossetia if they were attacked, Georgia launched a large-scale military offensive in an attempt to reclaim the territory.

By August 8, Russia had reacted by deploying troops and calling in airstrikes. After heavy fighting over the next four days a preliminary ceasefire agreement was reached on...
August 12.

In the currency markets the EUR began to slide sharply from August 8, as did the RUB, while the JPY reached the end of a five-month weakening trend (in contrast, the CHF continued to weaken until December).

Although the crisis in Russia was soon overshadowed by events in US markets, this was the point at which many of the biggest moves of the financial crisis (including gold) first began to emerge. Realized volatility in the USD index also began to rise from August 5 onward.

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2: The Russian Invasion of Afghanistan on December 24, 1979

A not dissimilar pattern to 2008 emerged in the dying days of 1979, with the USD commencing a five-year rally against European currencies just over one week later (as soon as the Christmas and New Year celebrations had ended) while gold peaked out by mid-January, commencing a 21-year downtrend.

While the JPY did not strengthen immediately, it did finally begin to appreciate in April 1980 - albeit thanks to the failed mission to rescue US hostages in Tehran.

3: The Annexation of Crimea and Activity in Eastern Ukraine (February 2014 onward)

On the face of it the events of 2014 might appear to have bucked the pattern set in 1980 and 2008.

Nevertheless, it should be noted that the 2014 turning point for the USD against the EUR coincided exactly with the controversial referendum in Crimea that resulted in it joining the Russian Federation. It also proved the peak for the gold price until this month.
A Brief Conclusion

If US military engagement with Iran (at least initially) has been a negative for the USD, then it also makes sense that Russian military entanglements have typically been associated with USD strength. It also seems logical that it has been European currencies that have typically suffered.

While less relevant in the current environment, it’s also interesting to note that the three great price peaks in oil over the past 40 years (particularly when looked at in inflation-adjusted terms) came in December 1979, the summer of 2008 and Q2 2014.

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