

Magellan – In The Know: Episode 20

War in Europe: In conversation with Former US Deputy Assistant Secretary of Defence for Russia, Ukraine and Eurasia Evelyn Farkas and former Deputy Director of the CIA Michael Morell



Announcement ([00:00](#)):

The information contained in this podcast is for general information purposes and does not constitute investment advice. You should seek investment advice tailored to your circumstances before making an investment decision.

Host ([00:14](#)):

This is In The Know, a monthly investment podcast brought to you by Magellan Asset Management, experts in global investing. We bring you timely, unique and thought-provoking insights to help you make sense of today's investment landscape.

Michael Morell ([00:29](#)):

He miscalculated the Western response. He miscalculated the military dimension of this, right? Both the strength of his own forces and the strength of his adversary. And he miscalculated the response in Russia. He miscalculated in a very significant way across three dimensions. And I don't think this is an overstatement, I think this is the biggest strategic blunder by a great power since Hitler invaded the Soviet Union in the Second World War.

Host ([00:58](#)):

That's Michael Morell, a former deputy director of the CIA giving a very Frank assessment of where Russia stands in its invasion of Ukraine. Welcome to Magellan, In The Know. In this edition of our podcast, recorded on 25th of March, Michael is joined by Evelyn Farkas, former US Deputy Assistant Secretary of Defense for Russia, Ukraine and Eurasia, to discuss the geopolitical and economic implications of war in Europe and what it may mean for food security, energy prices and the aspirations of China, as well as its impact on global investment markets.

Host ([01:41](#)):

They're hosted by Magellan's head of macro and portfolio manager, Arvid Streimann, for a fascinating discussion on everything from the military strategy to President Putin's aspirations. But first, here's a warm welcome from Arvid.

Arvid Streimann ([01:57](#)):

Welcome everyone to episode 20 of Magellan's podcast, In The Know. My name is Arvid Streimann and I'm a global portfolio manager here at Magellan, as well as our head of macro. This episode, we'll be

talking about the conflict in Ukraine, and we want to explore how the conflict may play out rather than why it's happened. And I think that looking forward is much more relevant for investors.

Arvid Streimann ([02:18](#)):

And while we will be focusing on the geopolitical economic and investment matters, I think it's important to remember that the conflict is having a very large human cost. Today, we're very fortunate to have two leading experts on the Ukraine conflict and how it may impact the rest of the world. We talk to them regularly, and I'm sure that you'll enjoy hearing from them as well. Joining us is Dr. Evelyn Farkas. Evelyn's CV is so long, it'll take half an episode to go through it. But I'll tell you that Evelyn is a-

Evelyn Farkas ([02:43](#)):

It's only because I'm old.

Arvid Streimann ([02:45](#)):

... Right. So right now she's got her own consulting company. Between 2012 and 2015, she was at the Pentagon. She was the Deputy Assistant Secretary of Defense for Russia, Ukraine and Eurasia. And I believe Evelyn, when you were in that role, that's when Russia first moved into Eastern Ukraine and Crimea.

Evelyn Farkas ([03:03](#)):

That's right, unfortunately.

Arvid Streimann ([03:05](#)):

And before that, she was a senior advisor to one of NATO's most senior leaders, the Supreme Allied Commander Europe. And in short, she's a long time expert on the region. Really looking forward to chatting to her again today, so welcome Evelyn.

Evelyn Farkas ([03:20](#)):

Thank you.

Arvid Streimann ([03:21](#)):

Now, we've also got Michael Morell. Michael Morell was Deputy Director of the Central Intelligence Agency in the US twice, its acting director. He was there for over 30 years and was in charge of delivering the presidential daily brief when 9/11 happened, and was also intimately involved in the planning on the raid on Bin Laden's compound. So welcome back, Michael.

Michael Morell ([03:40](#)):

It's great to be with you, Arvid, and great to be with Evelyn. She's the real expert here by the way.

Arvid Streimann ([03:44](#)):

Right.

Evelyn Farkas ([03:44](#)):

Well, but the man with the experience as you heard is the former director.

Arvid Streimann (03:50):

Well, I think it's going to be a good chat nonetheless. And so let's maybe kick it off here, Evelyn, with a question for you. Let's think about how this invasion has played out so far. I think of it being completed very quickly as the Russians had expected. Probably wouldn't be creating as much uncertainty as it is right now in the global economy and global markets. Clearly it's taken longer than what the Russian government would've hoped. What is it that surprised you most about the invasion so far?

Evelyn Farkas (04:17):

Well, I think you said it, Arvid. This invasion was supposed to be quick. We knew that the Ukrainians would put up a good fight, but I don't think we quite expected them to be this agile, I would say. And of course we've trained them to be this agile and we gave them the equipment to do this, but that included, or in addition to the fact that the Russians have been so shockingly disorganized, lacking in logistics, lacking in the ability to communicate, to coordinate among the branches of the military has really made the Ukrainians much more effective than maybe they would've been otherwise. As you said, now the fighting has gone on and the Russians do not have the advantage, frankly speaking.

Arvid Streimann (05:00):

Yeah, it's interesting because you say they do not have the advantage. And I guess a surprise is one of the main advantages in a conflict and it almost seemed as though they didn't have that element of surprise as well.

Evelyn Farkas (05:10):

Yes, and I think momentum. At this point now, the momentum feels like it's with the Ukrainians. Of course that could shift. The Russians could bring more forces to the battlefield. We see they're trying to resupply through one of the ports that they seize, but then the Ukrainians bombed the resupply ship.

Evelyn Farkas (05:27):

Again, right now, based on the coverage that we have, which we have to acknowledge is limited. I mean, it's where us journalists can get in and report and where eyewitnesses can report. But it really does look like the Russians have been unable to mount a resupply, and the initiative is still with the Ukrainians.

Michael Morell (05:44):

Yeah, I was going to go even further, right? I was going to say that we've been through phase one of the war, right? Phase one of the war was the attempt by the Russians to do their blitzkrieg, to take over the cities, to replace the government, right, with a puppet government and then keep some smaller force behind to support that government and then pull out. And Ukrainians won phase one.

Michael Morell (06:10):

They fought the Russians to a standstill for the reasons that Evelyn cited. And were now in phase two, which is where the Russians have decided to stop moving forward, to fortify their positions. They're actually laying down mines, which is a defensive move. They're building these fortifications where the Ukrainians can't get at them.

Michael Morell (06:31):

And they are firing mortars, they're firing rockets, they're firing missiles indiscriminately at Ukrainian cities I think in the hope that they can either break through or they can convince Zelenskyy that he needs to come to the negotiating table and see things more Putin's way than Zelenskyy does at the moment.

Michael Morell (06:50):

I think things have changed dramatically since the early days. And there's really some startling statistics, Arvid. The Russians have about 260,000 ground forces. They've deployed about 190,000 of those into Ukraine, so that's a significant chunk of their force. And they've lost 40,000 people to either death or injury or capture or surrender.

Michael Morell (07:19):

And they're actually taking support troops, right? People who do things like logistics and putting them into combat roles. They're raising the conscription age from 55 to 65. They're going from high school to high school trying to recruit younger folks to join the fight. So they're in a difficult place. They're in a very difficult place at the moment.

Arvid Streimann (07:40):

Well, it's interesting you talk about phases there, Michael. I might start the next question with Evelyn and then you can add in your two cents. But if we're moving into the second phase, I don't know how many phases there are going to be in total, but I guess this is a million dollar question which I'm asking right now is, how do you think that this conflict is going to pan out? And when I'm asking that question, I guess I'm thinking about two separate sub-questions. The first is, where do you think the endpoint is? And secondly, what do you think the path along to that endpoint looks like?

Evelyn Farkas (08:08):

Yeah. I mean, this is obviously a very difficult question that you're asking here. I don't foresee this war lasting years. I see it as more in terms of weeks and months, simply because I don't think the Russians can hold out indefinitely. And as Michael just said, they have a finite amount of forces they can throw at the equation. And the Ukrainians themselves, we can continue to resupply them, but I think there are limits also to how long they will hold out.

Evelyn Farkas (08:37):

I actually think the Ukrainians stand a good chance of winning this. The Russians, for sure, are not going to win in any way, shape or form. The most likely outcome I think that most people would safely agree on would be a compromise whereby Ukraine would essentially say, "Look, we've taken so many losses. We can't fight anymore."

Evelyn Farkas (08:58):

And the people would rally behind the president actually compromising by that point because they would be so exhausted and decimated, and they would say, "As long as we can maintain our independence and maintain most of our territory, we might be willing to give away the Donbas and

maybe even some of the territory that the Russians just seized in the last month. And we would say we won't join NATO."

Evelyn Farkas ([09:23](#)):

But that's about the maximum that I could see this government, this democratically-elected government going. That's as far as I could see them going. And that's the compromise, the most likely compromise. And that, by the way, if Vladimir Putin is still at the helm in the Kremlin, that's not even really a I mean, it's not a lasting compromise, that's a ceasefire, more or less, because he's not going to change his vision of what he wants, which is utter control over Ukraine.

Evelyn Farkas ([09:51](#)):

It will just be a signal and it will be troubling problems, because we'll have to continue then helping Ukraine shore up its sovereignty. The better scenario would be if Ukraine actually prevails and that they wear down the Russians. With every week of this war, they get stronger because we're providing them with more equipment.

Evelyn Farkas ([10:11](#)):

Somehow we find a way to provide humanitarian assistance. And the equipment does help the civilians to protect the civilians. That's the outcome that I hope for. I have a hard time imagining the Russians regaining the momentum, getting their troops and people behind them. I mean, they've lost so much also in terms of morale.

Evelyn Farkas ([10:30](#)):

They sent these troops in on a fiction telling them that they were conducting an exercise, and then they told Russian people that fiction has stuck a little more, what they told the Russian people, which is they're going to replace a Nazi government and liberate the Ukrainians from this Nazi government, which of course is led by a Jewish president and Jewish prime minister.

Evelyn Farkas ([10:51](#)):

I somehow have a hard time now imagining the Russians regaining, again, their foot. I mean, they've lost their balance and they've seeded the momentum to the Ukrainians. Internally what we see coming out today is also more tension inside of Russia. We see one of the reformist economists, Anatoly Chubais, essentially resigning. He was the equivalent of John Kerry, the kind of climate czar.

Evelyn Farkas ([11:17](#)):

He resigned and left the country, because if you resign under Vladimir Putin, you probably have to go somewhere safer than Russia. And then there was this storyline about the defense minister being "missing" meaning nobody had seen him in media, in the public. And then of course the house arrest of the intelligence officers who were responsible for the assessments that preceded the invasion, the intelligence assessments that gave Vladimir Putin the idea that this would be a quick, easy operation.

Evelyn Farkas ([11:46](#)):

I think either we're going to end up with that compromise or Ukraine will prevail. I have a hard time mentally shifting. And it may be of course my prejudice, what I would like affecting me, but I have a hard time imagining the Russians prevailing.

Arvid Streimann ([12:00](#)):

And just on the part of that outcome, we talk about the retaliation, which is going back and forth between the two sides. And I wonder whether it's an escalatory or deescalatory form of retaliation which is occurring. There was some news a couple weeks ago about the Russian nuclear forces being put in on a higher state of readiness, I believe. How do you think we get to that outcome that you talked about?

Evelyn Farkas ([12:24](#)):

Well, the high state of nuclear readiness, we're not really sure what that was. It seemed like a lot of theater. But they do have a lower threshold for nuclear use at any level. Whether it's tactical or strategic, meaning intercontinental, they can use nuclear weapons if they believe the existence of the state is threatened. And of course, Vladimir Putin will decide whether the existence of the state is threatened.

Evelyn Farkas ([12:47](#)):

But more alarmingly at the tactical level, the military has a doctrine of escalating to deescalate, which is a fancy way of saying of escalating to scare your enemy from the fight. So they could use cyber, but they could also use a tactical nuclear weapon. They could explode the nuclear weapon somewhere in Siberia and say, "Next time that's going to be on Ukrainian soil or in the United States if you Americans don't get out of this fight and leave it to us to do deal with Ukraine."

Arvid Streimann ([13:15](#)):

Yeah. And Michael, what are your thoughts on that outlook?

Michael Morell ([13:18](#)):

Yeah. I agree with everything that Evelyn said, so maybe I'll sort of summarize my views. Right now I'd say there's an 80% chance that the fighting continues and a 20% chance that we get a negotiated settlement in now, right, in the next few weeks. I do think that as the pain increases on both sides, that, that probability for a negotiated settlement will go up.

Michael Morell ([13:45](#)):

But it will take the pain, right, on both sides for that to happen. Right now, Zelenskyy, he's winning the war. He doesn't have to give up very much, right, to end this, at least in his mind. I think right now he would be willing to renounce NATO membership. As Evelyn said, I think he would want a referendum in the disputed regions rather than just giving them away. But I think from Putin's perspective, that's far, far from an enough, right? Because what Putin really wants is Ukraine to be in Russia's orbit. And what Ukraine wants is to be with the west.

Michael Morell ([14:24](#)):

And even an outcome where Zelenskyy renounces NATO membership and has a referendum where he loses the disputed regions, NATO's still going to align itself with the west going forward. And they have even more reason to do that now than they did before this invasion, right? Putin's not at the end of the day going to get what he wants, right? He's not going to get what he wants on the battlefield and he's not going to get what he wants even from a negotiated settlement, because Ukraine's going to go its own way.

Michael Morell ([14:55](#)):

In the scenario in which fighting continues, I agree 100% with Evelyn. I think the chances of the Russians breaking through and getting to their goal of taking the cities has an extraordinarily low probability. Stalemate is a significant chance as the fighting goes on. It's kind of where we're at now.

Michael Morell ([15:15](#)):

And it's possible, as Evelyn said, with all the weapons, pretty sophisticated weapons flowing into Ukraine literally by the hour across the Polish border, that the Ukrainians will be able to push the Russians back, and Putin actually loses militarily, which would be a significant embarrassment for him.

Arvid Streimann ([15:35](#)):

Yeah, it's interesting when you talk about Putin and his goals, and maybe he's not going to achieve those. Some people have talked about one way of ending the conflict is that maybe Putin is overthrown as Russian leader. Now, maybe that's not a high probability, maybe it's a low probability, maybe we'll ask that quite. But as well as how likely do you think that is, maybe we'll start with you, Evelyn, can you talk about who might be the most likely group of people to try that?

Arvid Streimann ([16:01](#)):

And I think most importantly, if they were to succeed, how different would they be from Vladimir Putin? Because if there is a, let's call it a changing government, there's always going to be some short-term uncertainty. There's always short term volatility and uncertainty when governments change. But maybe in the long term, it's even a more uncertain world because this new government may be even more unpredictable.

Evelyn Farkas ([16:22](#)):

Well, I think the most likely scenario with the compromise, as I said before, if Vladimir Putin is still at the helm of the government in the Kremlin, then it's really just as cease fire. At some point he'll attack again, he'll try to get his way using military means. If however it's a more durable peace agreement, then I think the prerequisite for that has to be Vladimir Putin leaving the scene, because I do believe from everything I've read and understand that this is his fixation, this revanchist crusade to recreate this Neo Russian Imperial entity.

Evelyn Farkas ([16:58](#)):

And so that the people around him, the siloviki, these other people who have grown up in the security services with him who are really the only people as far as we can tell who have access to him. And to a large extent, they think like him, but I think they would be willing to compromise and would be less fixated on this vision, because unlike him, they haven't been sitting in office for 20 years.

Evelyn Farkas ([17:23](#)):

And then during COVID apparently thinking about how they want to solidify their place in history, in Russian history. I would imagine that it would be someone in his inner circle that's says, "Okay, now, you go move to the dacha. We'll make sure nobody kills you, and you have enough money, and you can live the nice life and one of us will take over." That's the most likely scenario in terms of turnover of leadership.

Evelyn Farkas (17:47):

But this is Russia, so you never know. People can go to the streets on mass and suddenly you have a more liberal-minded, still nationalist Russian leader. Because someone like Navalny, he's still a nationalist. He's going to look out for the Russian Federation first and foremost. But he's not going to have this adversarial relationship with the west. But we don't know. We won't have much warning if that's going to happen.

Arvid Streimann (18:10):

Yeah. And where does the military sit in all of this? Are they a powerful force? Could they do this as well, or have they been sidelined?

Evelyn Farkas (18:17):

Well, I think that the military has been co-opted. Largely they are acting. Especially the minister of defense, he's been very close for years now with Vladimir Putin, and he doesn't actually have a military background himself. For about 20 years, he was head of the Emergencies Ministry, which is basically like a FEMA on steroids. And he dealt with forest fires and things like that.

Evelyn Farkas (18:40):

Vladimir Putin trusted him because he was not seen as a threat because he's not 100% ethnic Russian, et cetera, so he couldn't necessarily take over. The military is interesting because we've seen, of course, retired military officers, one in particular came out even before Putin invaded saying this would be foley, and laying out all the reasons which turned out to be accurate. I think the military leadership would be another place to look for opposition, and they could certainly force a change as well.

Arvid Streimann (19:11):

Okay. Michael, did you have any thoughts on that?

Michael Morell (19:14):

Yeah, I think it's probably unlikely. Here, Evelyn and I are going to differ a little bit. I think it's unlikely that, that inner circle, those 15 guys, and they are guys, right? Those 15 guys who were all former KGB, have been with him since the St. Petersburg days, that those guys will turn against him. And the reason I say that is because they're as guilty as Vladimir Putin of all of his sins.

Michael Morell (19:42):

And I think because of that, they see their future as his future. They would fear that if he went away, it wouldn't be long before they went away. I think the most likely actor in forcing Putin to step down would be the military. And I think what the military cares about at the end of the day is the health of the military. All militaries feel that way. But they also care about the perception of the military by the

Russian people. And killing women and children in Ukraine doesn't sell well on the streets and in the apartment complexes of Moscow.

Michael Morell ([20:18](#)):

They have to worry about their reputation. There's one scenario where, in my mind, there's a scenario where Putin orders something horrific in Ukraine and the military says, "No. And it's time that you go away." I don't think at the very top, I think at the next level down. Because the very top, they're in is inner circle.

Michael Morell ([20:35](#)):

I think another scenario is the one that Evelyn said, which is you get enough people in the streets of Moscow saying, "This needs to end. And you need to go away, Vladimir Putin," and Putin orders the National Guard to shoot and the military says, "No. And you need to go away." I think that's very low probability of Putin leaving, but I think he's facing the biggest risk that he has ever faced to his rule.

Arvid Streimann ([21:02](#)):

It certainly is very interesting times. Let's change gears slightly here and talk about something that's very important in the global economics at the moment, which is supply chains. We know that Russia's a major supplier of many commodities, not just energy commodities to Western Europe, but also mineral commodities around the world. We've also seen Western governments impose sanctions on China.

Arvid Streimann ([21:25](#)):

How likely, I'll start with you here, Evelyn, how likely do you think it is that Russia retaliates by restricting the export of some of those commodities that the west relies on, that would obviously make inflation worse around the world, would cause some economic damage on the Western economies? And when you're answering that question, maybe you can also talk about what commodities do you think are most important when they're perhaps undertaking that act.

Evelyn Farkas ([21:48](#)):

I mean, I think that the Russians, we've seen that they do like to strike back to show that they can hurt us as well. But on the other hand, they need access to foreign currency. They need revenue. I would think that they're not likely to make that move anytime soon. And that those kind of oligarchs in charge of those industries, or those members of the inner circle, if you will, wouldn't advocate for that.

Evelyn Farkas ([22:16](#)):

And if anything, maybe Russia would seek to sell the minerals to China, first and foremost, and of course then Chinese would try to make a good deal for themselves as they did in 2014 on oil and gas, and oil in particular. But I don't see Russia doing that right at the get-go. They do like to show their unhappiness with us, but that's what I would imagine.

Michael Morell ([22:39](#)):

And I agree 100%, Arvid. This is the only thing, right? The export of oil and gas, and the export of these commodities are the only thing that's keeping the Russian economy afloat.

Arvid Streimann (22:50):

Yeah. So if it did happen, then things are really bad, I guess, is what you're saying?

Michael Morell (22:55):

Yeah. I mean, things are bad now, right? I mean, things are bad. And now I hear from people in Moscow that the shelves are empty, long lines, people saying this feels like the 1980s. Somebody told me the IKEA store is empty in Moscow. I mean, one person told me that Moscow feels like North Korea, and this is somebody who had been to North Korea. Things are bad now, and so I think that any loss of that income would only make things worse.

Arvid Streimann (23:20):

Yeah, got it. Now, Evelyn, one thing that surprised me in all of this invasion and the conflict more generally is the strength of this Western response. And it's not just the governments, it's the corporates as well. I want to ask you, why do you think that, that response from both parties, the corporates and the governments have been so strong? And then I guess the obvious follow up to that is, how long do you think that those sanctions are going to last?

Arvid Streimann (23:43):

When I speak to people in the case of government sanctions, I always hear that these sanctions are easy to go on, but harder to come off. Is that true? And in the case of company actions, it's really interesting because obviously it's reducing these company profits voluntarily, or maybe involuntarily. Interested in your thoughts on both those Western responses.

Evelyn Farkas (24:02):

I want to answer the question, Arvid, but I also do want to kind of put a pin on the other commodity that Russia exports, which is wheat. Because there's going to be huge trouble the longer this conflict goes on in Africa, in particular Egypt. They rely on Russia and Ukraine for a disproportionate amount of their wheat. Just go to the economist, they did a great couple of articles on this, so I just want to put a pin on that.

Evelyn Farkas (24:26):

Because the dislocation economically that could result, the rise in cost of commodities is not just restricted to oil, gas and minerals. I'm actually much more worried now over the longer term, the longer this goes on about the agricultural impact, because of how that feeds into existing tensions in societies. Okay. To your question about sanctions, I think many of us were frankly surprised that the private sector sprung into action the way that it did. And we were also surprised by the Trans-Atlantic response.

Evelyn Farkas (24:58):

But the reality is there was no subterfuge, as you yourself said. There was no surprise the Russians, or maybe Michael said the Russians invaded in light of day, blatantly. And this was the third time. They had invaded Georgia in 2008 and the Europeans made up a bunch of excuses and blamed the victim. And then in 2014, well, we managed it so that it wasn't an ongoing, huge problem in terms of refugees and conflict. Again, manageable.

Evelyn Farkas (25:24):

But now he was taking on this large scale invasion in front of our eyes, and I think it was too much. And a couple of things came together. I mean, you had President Biden whom Putin had assessed as weak, but actually President Biden had already taken the measure of the man, had a strong sense of how we needed to respond to Vladimir Putin, which is with firmness and with harsh sanctions already, but Putin hadn't taken him seriously.

Evelyn Farkas (25:49):

And then the German government, I think Putin thought that ... I don't know what he thought of Angela Merkel, but he respected her. And he saw this coalition government, it looked messy to him. He didn't understand the green party is one of the firmest parties in Europe when it comes to, again, having the same attitude as President Putin vis-a-vis Russia, which is you deal with them with firmness.

Evelyn Farkas (26:10):

And the social democrat leader was a different leader. He wasn't beholden to Gerhard Schröder anymore, right, who's the former leader of the social democratic party who basically does Putin's bidding as a board member of both of his large energy commodity companies. The political leadership was different, the shock was ... I mean, there was no way to avoid what was happening, the reality of it.

Evelyn Farkas (26:33):

And then I think corporations really ... There's been a bit of a change over time, not just in relation to this crisis, but in general, in the United States with our business councils and the shift towards looking at business as a part of an environment. Business has responsibility to communities and to workers. That kind of that shift has occurred in our culture, in our business culture a little bit over the last, let's say eight years.

Evelyn Farkas (27:02):

And I think that also had something to do with what happened here. And then just seeing this underdog, smaller country being invaded like that and the reaction in the American public. And let's not forget, there are a lot of Eastern European Americans like myself-

Arvid Streimann (27:18):

And me.

Evelyn Farkas (27:18):

... a lot of Ukrainian Americans.

Arvid Streimann (27:19):

Both of us.

Evelyn Farkas (27:20):

Exactly, like my Hungarian distinct cousin here. This kind of resonates with us because we can relate to those parts of the world. Also, the Ukrainian Americans and Eastern European Americans tend to be concentrated in congressional districts and states where they have a lot of power. And so corporations also have to listen to that. I think it was just a kind of confluence of events.

Evelyn Farkas (27:46):

I will say, to answer your last question, it is true that once you put sanctions on, especially if Congress codifies them, it is harder to remove them. Because the sanctions that the president will put on using executive order, the next president, or that president can come in and change them. But once Congress springs into action, as we know with Jackson–Vanik, which was the 1980s era sanctions on the Soviet Union for its treatment of Soviet Jews, we took so long to take those sanctions off because Congress found every excuse and tried to use the leverage and didn't let successive administrations remove that legislation.

Evelyn Farkas (28:22):

So you're right, it can take a while. And business will be more cautious going back. I do commend those companies like McDonald's who have said, "We don't want to punish the Russian people. We'll continue paying salaries." Again, hopefully this war doesn't last very long because that could become costly.

Arvid Streimann (28:37):

Yeah. And Michael, what are your thoughts on that question?

Michael Morell (28:40):

I'll just do two things, Arvid. One, as Evelyn was talking, I was reflecting on all of the miscalculations here by Putin, right? He miscalculated the Western response. He miscalculated the military dimension of this, both the strength of his own forces and the strength of his adversary. And he miscalculated the response in Russia. He miscalculated in a very significant way across three dimensions.

Michael Morell (29:07):

And I don't think this is an overstatement. I think this is the biggest strategic blunder by a great power since Hitler invaded the Soviet Union in the Second World War. I don't think that's an overstatement. The other specific issue I wanted to say on sanctions is if we do get a negotiated settle, the Russians will want sanctions relief as part of that negotiated settlement.

Michael Morell (29:31):

Zelenskyy, right, will come to the US and come to the EU, and he'll say, "I have a deal with Russia to end this war, and it includes you removing sanctions." Right? That will be a demand of Putin. And Zelenskyy, if he agrees to it is going to come and ask us for that. And we're going to have to figure out how to respond. And I think I know how we'll respond. I think we'll say yes, right, to end the bloodshed. But there will be voices in the United States that some of those sanctions should remain for a long period of time.

Evelyn Farkas (30:04):

And even beyond that, there are some voices now talking about reparations, that the Russians should pay reparations to Ukraine. And that sounds very World War I-ish. Having said that, I think if the Russians do have a real regime change, if you will, and show real repentant at the highest levels, then we should consider, not just kind of a Marshall plan for Ukraine because frankly of course the Russians destroyed it, but also some assistance to the Russians to stand their economy back up. But that would be predicated on a real change of government and perspective in Moscow.

Michael Morell (30:43):

The other thing that occurs to me is no matter what the outcome, no matter what the outcome here, whether Putin wins militarily, gets defeated militarily, or there's a negotiated settlement, Vladimir Putin and Russia, for as long as Vladimir Putin is running it, is going to be a pariah state internationally. Right? And the deep irony here is that Vladimir Putin wanted to go down in history as a great Russian leader, right? As a leader who rebuilt Russia's greatness, and actually just the opposite is going to happen. He's going to go down in history as somebody who destroyed his country.

Arvid Streimann (31:20):

Yeah, it's not the best situation to be in when you've catch it like that. Now, when we're thinking about these sanctions, what do you think have been the most effective sanctions? There's obvious been a unified response. There's been some new ones and powerful ones, particular with the financial system and the access to foreign reserves. So maybe Evelyn I'll start with you.

Arvid Streimann (31:39):

What do you think has been the most effective sanction or response here? And the reason why I asked this is because I suspect that they're the ones which are going to continue the longest in some sense, and those sanctions or responses, which have been less effective, and maybe they did have a large economic cost, maybe those ones don't last quite as long.

Evelyn Farkas (31:56):

I think the sanctions that had the greatest impact and were most surprising were the sanctions on the Russian Central Bank, because it suddenly eliminated the ability of the Russians to access those foreign reserves that they had kept, frankly, in New York on a data line for the most part.

Evelyn Farkas (32:15):

And so in order to keep on fighting this fight, they have to spend money on their troops on material. And so I think those were the biggest sanctions and those are the ones that prompted, I believe, the private sector to also then take the actions they took, because it was very hard for them to imagine how they could continue to do business, get paid in Russia without having to resort to being paid in the useless rubles.

Evelyn Farkas (32:38):

To my mind, that was the most important. I think as this goes on, potentially as important are the export control sanctions on computer, and semiconductors and other kind of tech components that the Russians need for their missiles and things of that nature that they can't get from China. But that's not an issue yet, I don't think.

Arvid Streimann (32:59):

Yeah.

Michael Morell (33:00):

I agree 100% with that. Nothing to add. Evelyn has always nailed it.

Evelyn Farkas (33:03):

Thank you. Thank you, cousin Michael.

Arvid Streimann (33:07):

Well, Michael, maybe then I'll ask you a slightly different question. Maybe we'll zoom out a bit here. Because a lot of people are saying we're in a new cold war here with Russia. And I think when you think back to the cold war of the Soviet Union and NATO, what was really interesting was that there was this ever present nuclear threat.

Arvid Streimann (33:23):

And right now I think that there's maybe three superpowers in the world rather than two, however you want to measure superpowers of course, whether it's military or economic. What are your thoughts on this so-called cold war? And if it does exist, what does it actually mean for governments and businesses, and I guess most importantly, people like us or consumers?

Michael Morell (33:43):

Yeah. I don't think we're in a cold war. I think we're actually in a hot war at the moment with Russia. We happen to be fighting it from a proxy perspective. We happen to be fighting it directly, so we're in a hot war. Let me step back and say something and actually get Evelyn's response to it. What's happening in Ukraine is horrific. It's absolutely horrific, and we can't forget that.

Michael Morell (34:05):

But as Evelyn said earlier, there's no way that Putin wins this, right? He's already lost militarily. He's not going to win militarily. He's not going to win diplomatically, even if he gets an agreement, because he's not going to get what he ultimately wants, is Ukraine in his hands or Ukraine as a vassal state, right? He's not going to get that. So you have that piece. And the second piece you have is that we're in a very dangerous time.

Michael Morell (34:29):

This war could widen, right? President Biden, I think, is working very hard to make sure that we don't escalate to direct conflict with the Russians. And I think that's exactly the right thing to do. I don't think Putin wants that either. I don't think either leader wants World War III here. But the probability is not zero of that happening. I mean, there are Western arms flowing in. I said this earlier, right? Flowing into Ukraine on an hourly basis. What if the Russians decide to take those out?

Michael Morell (34:58):

And they don't shoot on the Ukrainian side of the border, they shoot on the Polish side of the border, what do we do? There are ships in the Black Sea from multiple countries operating in very close proximity, right. There could be a miscalculation. There's a very dangerous time here. I mean, he could use chemical or biological weapons or even a tactical nuclear weapon, and then how would we respond to that? Right?

Michael Morell (35:18):

There'd be intense pressure on the west to provide a more direct support to Ukraine, I think. It's a very dangerous time. But once we're through this war in Ukraine, and once we're through this dangerous time, I think the world's a better place. I really do think the world is a better place because of how the west came together and said, "This is a line that you cannot cross." And that sends a very powerful message to every other country in the world who might think about violating an international norm.

Michael Morell (35:48):

And I think that's why at the end of the day, we're not going to be in a cold war with Russia because it is going to be a defeated nation. And we'll see if we end up in a cold war with China or not. I don't think we're in one yet. I hope we can manage that relationship so that it doesn't happen. But I think the west standing up also sends a very powerful signal to China that there's certain things you can do and certain things you can't do. And we might be able to get to a better place with China going forward because of this. Boy, that's the only optimistic thing I've ever said.

Evelyn Farkas (36:18):

And I agree 100%. I couldn't have ... Yeah, perfect.

Arvid Streimann (36:22):

Okay. Well, maybe let's turn to China, and a question for you, Evelyn. In February, there was that famous meeting between presidents of China and Russia, and there was this declaration that the friendship between the two nations has no limits. What do you think no limits actually means? And of course, that declaration was made prior to the invasion. Do you think that, that declaration still stands to the same extent that it did before?

Evelyn Farkas (36:45):

Well, I'm sure when they said it had no limits, both men had their fingers crossed behind their backs, which in American culture means you are saying something, but you don't really mean it. Because clearly there are limits. I mean, there are huge limits. If you look at it historically, Russia is descending, China is ascending power. Even before this war, the Chinese are growing their nuclear arsenal, so at some point it can rival Russia's.

Evelyn Farkas (37:14):

Russia will not know what to do at that point in time. The Chinese have been buying real estate and Siberia for years now. If you know scratch a Russian general, they will eventually admit that they are worried about China down the line, so there were always limits to this. But President Xi was very clever. All along he's treated Vladimir Putin like an equal, even when Russia was not the equal of China.

Evelyn Farkas (37:35):

I think there were always limits. What we saw in 2014 was similar, interestingly to what we're seeing now, which is somewhat surprising given that declaration that they made at the Olympics. The Chinese response in 2014 was curiosity. In fact, I was at a meeting with a state department colleague or then assistant secretary for Europe, and the Chinese came asking for a meeting because they were trying to understand what was happening.

Evelyn Farkas (38:02):

Of course they wanted to understand it to see how they could use the lessons learned and apply it probably to Taiwan. Fast forward now, we've had Xi in power this whole time, and he has been very assertive and clearly was looking to see what the Russians could get away with again. But also is quite happy to have Russia create problems for the west to weaken the democracies, to distract us from dealing with the Indo-Pacific area.

Evelyn Farkas (38:30):

And so for China, that component of this looked good, but the downside now is clearly that Russia is threatening the economic order and the international order writ large, and that is something that China is not prepared for. While the international order is something that also restricts them, at the moment they have not come to the conclusion that they need to tear it apart, rather they want to co-opt it.

Evelyn Farkas (38:54):

And economically, certainly this economic system is working for them. And so they don't want to see a complete collapse that could happen as we already discussed if this war continues. The Chinese now are still on that tight rope that they were on in 2014, which is showing allegiance and support to Russia, but not in any real, tangible way, sufficient to upset the west.

Evelyn Farkas (39:19):

And I think that's what's going to continue now. They will provide some support to Russia, provided they can do it quietly, and it's not going to provoke or cause us to really pay attention and call them out. And certainly they want to avoid any kind of secondary sanctions.

Arvid Streimann (39:34):

Yeah. It's interesting, Evelyn. When you were talking about the border between China and Russia and how maybe the generals are looking at each other, despite what the leaders are saying to each other, I kind of think about it this way. And so if you've got three people in a room and they're all quite powerful, then two will gang up on one. And right now we can see that the two together are Russia and China, and let's call the other one the west.

Arvid Streimann (39:58):

Let's fast forward into the longer term. Do you think that, that's the natural order of things in terms of who are the natural groupings here? Because I kind of look at it and say, "Well, Russia, Moscow is kind of towards the west of the country. It's closer to western Europe than it is the China." Do you think that, that relationship that's very strong under the presidents of both of those countries, do you think that, that's actually the, let's call it the natural equilibrium?

Evelyn Farkas (40:22):

Well, it's interesting because you're using terms that I think the Russians would understand, because the Russians culturally, they do not consider themselves in Moscow to be an Asian country, even though as you rightly point out, much of their geography is Asian. But they associate themselves culturally with Europe, which is why I also think in the longer run, Russia will seek a closer relationship with Europe and with the west as they always have.

Evelyn Farkas (40:50):

And it remains to be seen what kind of relationship, I agree with Michael, that we will have in the future with China. It's not a foregone conclusion that it needs to be adversarial. I do think that this particular Chinese president is a bit problematic in his foreign policy. And I don't know, we haven't seen any signs that he's learning from, or the people around him are learning from this Putin experience.

Evelyn Farkas (41:10):

But if there's anything to be derived from it if you're a Chinese leader and you're not Xi, it's I don't want my leader getting all revanchist and messianic and ruining a good thing that we have going. Let's continue maybe quietly exerting our influence and maybe they could go back to some economic pressure and economic incentives when it comes to dealing with Taiwan, because they did in the past have a policy where they were going to reunite softly without force, right?

Arvid Streimann (41:43):

Well, maybe with our last question, I'll throw it over to you, Michael. And it's a question that I think is on everyone's lips at the moment. I know I certainly get asked the question a lot. What is the read through here for China and Taiwan? Obviously they're watching what's happening in Ukraine, both as the larger power and the smaller participant, maybe in a conflict. What do you think the learnings are for both China and Taiwan, and what does that actually mean for the future of that potential flashpoint?

Michael Morell (42:10):

Yeah, I'd be happy to answer that, but let me just make one point about out the overall Russia-China relationship, and I think it's fully consistent with what Evelyn said. This is not a deep strategic relationship. This is a relationship that's built really on three things. It's a relationship built on a personal bond between two leaders who I think like looking at somebody like them sitting across the table.

Michael Morell (42:37):

Number two, it's based on the fact that one's a large energy exporter and one's a large energy importer. And it's based on a desire to undermine the United States ability to exert its influence in the world. That's all it's based on. Nothing else. They have nothing else in common. And their futures from an economic perspective have nothing in common besides energy. This is not a deep relationship, and I think it's important to remember that.

Michael Morell (43:03):

With regard to Taiwan, I am not one of these folks who believe that China has a timetable for unification. I'm not one of these folks who believe that Xi believes by 2029 or whatever date he's thrown out there, that if Taiwan's not back in the fold by that date, that China will take military action. I've never believed that. I believe that China's policy remains to coerce Taiwan back into the fold, not force them back into the fold.

Michael Morell ([43:34](#)):

China would absolutely take military action if Taiwan declared independence and I think if the United States changed its One-China policy. But China's not going to be the first mover here. If there's going to be a war, it's going to start either in Taipei or in Washington. And China thinks it has all the time in the world to coerce them back into the fold. I think what you're seeing from Xi when he talks about timetables, he's playing to his domestic audience.

Michael Morell ([43:58](#)):

I mean, Taiwan is an incredibly important issue to the Chinese people, and so I think it's more domestic than it is real. And given what's happened with Ukraine, I think it reinforces that view in China. China has always known that if they had to take military action Taiwan, they would pay economically for some significant period of time, and what's happening right now must drive that point home.

Michael Morell ([44:24](#)):

Look, the other things that I would be thinking about if I were Xi, number one, "Is my military any good?" Right? "The vaunted Russian military just showed its true colors in Ukraine. And my military, right, which I've invested a tremendous amount of money in, just like Putin invested a tremendous amount of money in his forces, right, they haven't fought a war since 1979, and that was a war they actually lost to Vietnam. So how good are my forces?" Right? That has to be going through his head.

Michael Morell ([44:54](#)):

The other thing that has to be going through his head is what Evelyn said. In leadership circles, will people see this as an opportunity to chip away a little bit at Xi's power by questioning whether being aggressive in the world is the right approach or not? They have a leadership, Congress coming up, right? And I'd love to be a fly on the wall of that to see how these conversations go.

Michael Morell ([45:18](#)):

And then the last point I'll make is China studies everything, and they will study this. And they'll probably take a year to two years to study this, and they'll study every aspect of it, right, in these study groups. And they'll come to conclusions, and we'll see what those conclusions are. But they will look at this very, very closely in terms of what it means for China.

Arvid Streimann ([45:39](#)):

Yeah. And it's hard to see at least from my perspective that them saying or concluding that it's a really good idea to make a move in the short term, because there is a lot of uncertainty for the reasons that you pointed out and perhaps their troops aren't proven or battle-hardened, however you want to think about it.

Michael Morell ([45:54](#)):

I think the other thing to think about is Taiwan is not Ukraine, right? They're not connected by a border. There's a pretty significant body of water, right? And the terrain in Taiwan is completely different than the terrain in Ukraine. It would be a very difficult fight for the Chinese, and they know that going into it, whereas Putin thought it'd be a cake walk.

Evelyn Farkas (46:14):

And the other difference, of course, is that the United States has a longer, firmer security commitment to Taiwan than we ever had to Ukraine, so that has to give impasse as well.

Michael Morell (46:22):

Yeah.

Arvid Streimann (46:23):

Yeah. Okay. Well, I think we might end it there. And what a great conversation that was. I hope you enjoyed listeners listening to it as much as I enjoyed in terms of being part of it. So thank you very much, Evelyn, and thank you Michael, for being on the pod today.

Michael Morell (46:35):

You're welcome. And it was great to be with Evelyn.

Evelyn Farkas (46:38):

Oh, likewise. It was an honor to be with Michael. Thank you.

Host (46:41):

That was Magellan's head of macro and portfolio manager, Arvid Streimann, who was joined by former US Deputy Assistant Secretary of Defense for Russia, Ukraine and Eurasia, Evelyn Farkas, and former CIA Deputy Director, Michael Morell. We trust you've enjoyed this episode of Magellan, In The Know. Join us in a month's time for the next episode. For more information on upcoming episodes, visit Magellangroup.com.au/podcast, where you can also sign up to receive our regular investment insights program. Thanks for listening..

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