KAPUSTA FINANCIAL GROUP

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The Stock Market in an Election Year

Believe it or not historical statistics going back to the 1930s tell us that there is an overwhelming probability that the stock market's performance in this election year will be flat to positive. Those percentages bear out regardless if the incumbent president is running for reelection, is a lame duck, is a Republican or Democrat. Will this year's market performance be in line with the overall historical positive returns?

Many economic factors suggest that it may. While manufacturing remains at recessionary levels, consumer spending and the job market continues to buoy our economy – defying a slow down across the globe. For all of last year economic growth (GDP) grew at a moderate 2.3% level – respectable - but the weakest since President Trump's election in 2016. The ongoing trade dispute with China has also become less menacing to our economy over the last few months. The Federal Reserve interest rate cuts of last summer and fall continue to provide a temporary stimulus to the aging economic expansion.

Stock prices closed out last year with double digit gains and have charged into the beginning of this year with virtually nothing but upside momentum. That's all well and good, but we can't ignore a few warning signs. The stock market is now priced to "perfection". The five largest stocks in the S&P 500 (Google, Apple, Microsoft, Amazon and Facebook) have a combined valuation of greater than the next 282 stocks in the index. Even as it continues to melt up in performance it is important to understand that any disruption in corporate earnings or consumer spending can and will have an immediate and negative impact on stock valuations. Despite last year's stock market performance of double-digit returns, 2019 also contained the largest stock fund outflows in over a decade. How much lower can the Federal Reserve decrease interest rates? They are simply running out of room to reduce borrowing costs in an effort to stimulate the economy.

Most economists see a slow down this year but not necessarily a recession. We tend to agree. A real wild card event sometimes called a black swan event that has yet to play out is the Coronavirus. To date Wall Street has pretty much ignored what the economic impact of this disease may bring upon China's economy and the rest of the world's economy. It's hard to believe that we won't see reduced first quarter

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corporate earnings in this country due to the virus when those earnings are reported in early-mid April.

To reiterate what we said in last fall's newsletter, stocks will probably oscillate between rallies and sell-offs along the way up until the election in the fall. Defensive sectors such as government bonds, utilities, consumer staples, real estate and gold will continue to provide defensive protection while paying good income and appreciating in value.

As always, we at Kapusta Financial Group would like to thank you for the trust and confidence you place in our team.