consilium WEALTH ADVISORY

Cliff Notes
Weekly Capital Market Update

Cliff Notes – Kanye for President

Source: YouTube.com

Last week saw more epic stock gains, on low interest rate policies from the US Fed and strong tech earnings. The S&P500 is now up 10% year to date.

Activity has started to normalize around the globe, albeit with renewed localized lockdowns to contain virus clusters. The unprecedented policy response has boosted risk assets. Europe has agreed on a historic recovery fund, but U.S. stimulus is now at risk of fading. Talks over the size and makeup of a new U.S. fiscal package have stalled as some key benefits expired and states face budget shortfalls. Our base case calls for a $2 trillion fiscal package that extends some federal stimulus measures through late-2020, but there is a risk no deal will materialize.

Another oft-mentioned risk is the US Presidential election. With both conventions now behind us the race has tightened according to RealClear polling, between Donald Trump and Joe Biden. Which got us wondering what happened to Kayne West's much ballyhooed Presidential bid? At least the music on AirForce One would be better if he were elected – but would the tweets? Hmmm.

Read our full CliffNotes for market insights, charts, and views – along with commentary about US Presidential Elections and the market.

Weekly Index Returns & Commentary (ending 08.31.2020)

WEEK ENDING AUGUST 28, 2020 (CUMULATIVE TOTAL RETURNS)

Equities[1]	Close		Week		YTD		1-Year
S&P 500	3,508	▲	3.29%	▲	10.0%	▲	23.9%
DJIA	28,654	▲	2.64%	▲	2.0%	▲	12.7%
NASDAQ	11,696	▲	3.40%	▲	31.2%	▲	50.3%
Foreign Stocks		▲	1.69%	▼	-4.3%	▲	7.9%
Emerging Markets		▲	2.76%	▲	2.5%	▲	19.3%

Top Three S&P 500 Equity Sectors[1]		YTD
Information Technology	▲	35.5%
Consumer Discretionary	▲	27.8%
Communication Services	▲	16.6%

Bottom Three S&P 500 Equity Sectors[1]		YTD
Energy	▼	-37.9%
Financials	▼	-16.3%
Utilities	▼	-7.0%

Bonds[2]		Week		YTD		1-Year	Yield
10-Yr. Treasury[3]	▼	-0.76%	▲	10.0%	▲	6.8%	0.74%
US Bonds	▼	-0.51%	▲	6.6%	▲	6.1%	1.18%
Global Bonds	▲	0.06%	▲	5.9%	▲	5.0%	0.91%
Munis[4]	▼	-0.33%	▲	3.3%	▲	3.1%	1.31%

Market Indicators[5]		As of
Fed Funds Target	0.25%	08/28/20
Inflation (Core CPI)	1.6%	07/31/20
Unemployment	10.2%	07/31/20
GDP	-31.7%	06/30/20

Weekly Major Asset Class Commentary

Global Equities

The S&P 500 gained for the fourth consecutive week, boosted early in the week by a fall in US coronavirus cases and the FDA announcement of emergency-use authorization for convalescent plasma in COVID-19 treatment. The index closed the week up 3.29%, further supported by the Federal Reserve (Fed)’s signals of increased flexibility around its inflation target. European equities lagged the US slightly.

Commodities

Oil prices rose slightly last week after US producers in the Gulf of Mexico shut down in preparation for Hurricane Laura, although the hurricane ended up passing through without causing major damage to refineries. Pandemic-related headwinds to global demand kept prices contained, as WTI and Brent crude oil prices ended the week up 1.49% and 1.58%, respectively.

Bonds

Sovereign yields jumped last week amid risk-on sentiment, generally supportive economic data, and monetary policy developments. In the US, rates responded to the Fed’s announcement differently across the curve, which ultimately steepened as some market participants may have been disappointed by the noncommittal (versus formulaic) version of flexible average inflation targeting.

FX

The US dollar weakened against most major currencies last week with the US dollar index down -1.09%. The Japanese yen rose 0.37% against the US dollar after news of Prime Minister Abe’s resignation made investors cautious on the potential shift away from “Abenomics” expansionary policy.

(Source: GS Weekly).

Market Commentary: Trends Matter More than Headlines

With the stage set for the presidential election in November, some investors may be concerned about the impact of politics on the stock market and economy. After all, the 2016 presidential election resulted in large market swings and the political climate is even more polarized today. On a short-term basis, election headlines have the power to move markets and create stock market volatility. How should investors react to what may be a bitter campaign? Should investors fear either party winning the White House? Is it best to sit on the sidelines until the dust settles?

As citizens, taxpayers and voters, elections are extremely important. This is true regardless of which side of the aisle you're on and which candidate you support. Your vote helps to determine the principles that will be upheld by the country in the years to come.

However, it's important to separate these personal and political feelings from financial plans and investments. When it comes down to it, long-term investors should be wary of claims that one candidate or another will "kill the market" or "ruin the economy." It's likely that this has been said about every president in modern times across 14 presidencies since 1933 (7 from each party).

For instance, this was certainly said about both Presidents Trump and Obama. In 2016, markets plummeted overnight when Candidate Trump became President-elect Trump, only to then reach all-time highs by the end of the year and rally until the COVID-19 crisis. During the 2012 midterm elections, political pundits focused on the Affordable Care Act ("Obamacare") and how it would burden the economy. An investor who bought on election day in 2012 and held until election day 2016 would have experienced a 63% total return, or roughly a 16% average annual return. Throughout these examples and more, investors who over-reacted to politics rather than the underlying economic facts would have missed out on significant portfolio growth.

To be clear, this doesn't guarantee that either candidate has sound economic plans or suggest that their policy proposals and values don't matter. Government policy can certainly have an impact on economic growth, e.g. through corporate taxes and trade, and can also affect specific stocks, bonds, and sectors. However, for most long-term investors, it makes more sense to focus on economic and market fundamentals rather than day-to-day election coverage.

This is because the relationship between politics and the stock market is not a simple and obvious one. While there may be conventional wisdom about how each political party may affect the economy, these views actually have a poor record when it comes to predicting stock market returns. Not only is economic policy difficult to evaluate, implementing and enforcing such policies take time. And even when investor predictions are correct, the market tends to price in these facts well ahead of time.

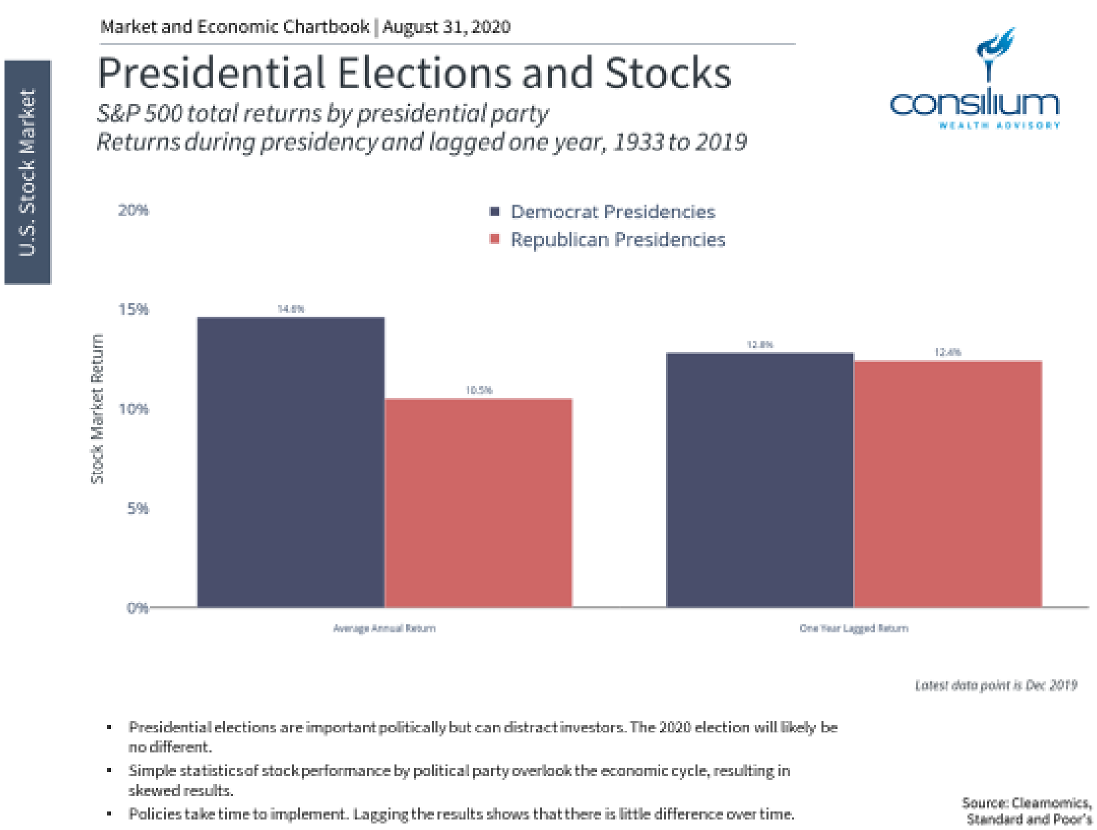
For instance, one reason for a significant surge in the stock market after 2016 was a recovery from the corporate "earnings recession" of 2015-2016. Similarly, one reason the market performed so well after 2008 and 2012 was that it bounced back from the global financial crisis, Eurozone crisis, and other problems along the way. It's not a stretch to argue that these macro trends would have driven markets irrespective of which party controlled the White House.

This is perhaps best illustrated by the 1990s and early 2000s: the Clinton era happened to coincide with the tech boom while the dot-com bust coincided with the start of the George W. Bush presidency. It would be a stretch to argue that their presidencies caused the boom and bust, respectively.

More importantly, even if there is a large difference in stock market performance, it's clear that returns are positive under both parties. History also tells us that market returns are positive on average during election and non-election years alike. Jumping out of the market due to the outcome of an election, or simply because an election is occurring, is not a decision supported by history.

Thus, the best course of action for long-term investors, regardless of political preference, is to stay invested and maintain the discipline to keep our political and financial lives separate. Below are three charts that put this important topic in perspective.

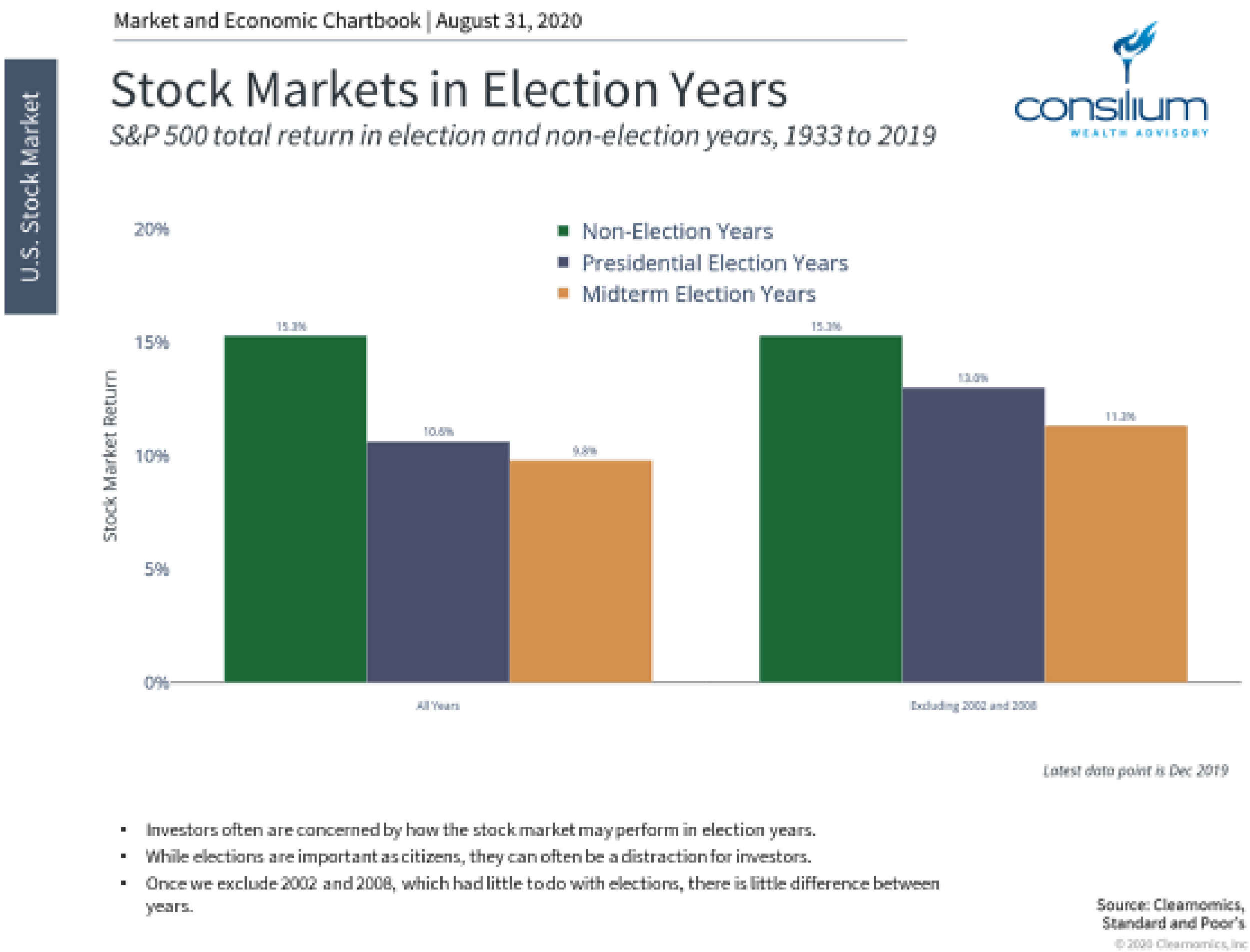
1. The stock market has performed well under both parties



A simple average of stock market returns under Democrats and Republicans shows a clear advantage for Democrats. However, not only are there outliers including the dot-com bust and the 2008 financial crisis that happened to fall under Republican years (and arguably had nothing to do with which party was in office), but it can take years to fully see the effect of economic policies.

Incorporating a lag into the data shows that there's hardly any difference in stock returns between the two parties. More importantly - stock returns are positive on average regardless of presidential party. Thus, making portfolio decisions on the basis of political preference can often backfire.

2. Market returns are historically positive in all years



While it does appear that non-election years tend to have higher returns on average than election years, this difference is small after excluding 2002 and 2008. Additionally, the fact that all years are positive means that avoiding election years is generally not supported by history.

3. In the long run, economic trends matter more than politics

Over the past 90 years, the stock market has trended upward due to innovation and economic growth. This has been the case despite global conflicts, financial crises, recessions and a pandemic while different parties have controlled the White House and Congress.

The bottom line? In the long run, it's economic growth that matters. There is no simple way to predict stock market returns based on presidential elections. Long-term investors should stay focused and not over-react to day-to-day election coverage.