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It's a New Year! Is it a New Day?

Global Markets and Regions

	4th QTR	2016 YTD
US	4.27%	11.60%
Developed Europe	-0.40%	0.20%
Asia	-3.50%	4.30%
Emerging Markets	-5.84%	11.60%

US Markets

	4th QTR	2016 YTD
Dow 30	8.70%	16.5%
Large Cap Cos.	6.65%	12.10%
Mid. Cap Cos.	6.84%	20.66%
Small Cap Cos.	10.15%	26.70%
Bonds	-2.93%	2.44%

Does a presidential election really make a difference to long term investment prospects? According to research done by Vanguard Funds, presidential elections have no long term effect on market performance. This conclusion is based on data going back to 1853. It is sound investment policy that you should invest with a long term time horizon and not make major changes based on short term changes in circumstances as markets deliver their returns over time. Returns over short time horizons can vary greatly. One hundred and sixty years is quite a long time horizon. The election was barely two months ago and markets and investment prospects appear to have changed rather dramatically. Since most investor's investment goals need to be realized in less than 160 years, I guess it depends on what your time horizon is.

Donald Trump winning the presidential election was a surprise and definitely the least expected outcome. Analysts had for the most part forecast a Hillary Clinton win, and with that had forecast a continuation of the essentially "benign" investment and market status quo. Fiscal policies would be little changed. A Trump win, on the other hand, was expected by many to result in a major market decline as it would disrupt the status quo. Trump campaigned on fiscal policies that are dramatically different and are anything but the status quo.

As it became apparent on November 8th that Trump was going to win, markets did react quite negatively for a very brief moment. That was at least the case outside the US and in pre-market futures trading. But markets reversed solidly higher when actual US based trading began the next day. That strength has continued. Was this just another event in what has been an event sensitive market or does this represent something new? Time will tell.

Recent market trading has been characterized by bouts of modest optimism followed by intense negativism as significant events unfolded. Last year at this time the Federal Reserve had just raised the Fed Funds interest rate a quarter point. Their rationale was that they needed to begin to "normalize" rates in advance of the next recession and the economy was strong enough at the time to start the process. The economy was barely growing at a 2%, corporate earnings were in the midst of a slow decline and the rest of the world's economies were in much less robust circumstances. Over the next two and half months, markets reacted negatively retreating about 10-15%. When the economy didn't tank as a result, markets recovered. The Fed was quiet the rest of the year.

By early summer, the vote on the British exit from the European Union roiled the markets once again as the action was perceived to be a serious threat to a fragile economy. Markets declined about 6-8% before recovering again when Armageddon didn't develop. In the background, the impending US election was setting up the next market discontent. What was little noted was that prices in general had not moved higher than levels reached in late 2014. Markets have delivered little to no returns for the past two years, certainly well below their long term averages. The market has periodically stumbled and then recovered and then repeats the process. Economic fundamentals have not been robust enough to completely overcome the negative events.

Since the election, we've seen a significant change in market characteristics. Prices have risen and optimism and general market sentiment have gone decidedly positive. It's all good so far. The negative perception of Trump winning the election has turned out to be the opposite. Is this justified or is this just another event for the market to digest before returning to its prior malaise?

The case for optimism has been bolstered by modestly improving fundamental economic statistics. Markets have been responding positively to better jobs and wage data, better housing and retail data and generally better manufacturing and service economy data. Markets are beginning to anticipate the effects of lower tax rates and decreased regulation rather than continued monetary stimulus as a driver of economic growth and are expecting those polices to support that growth. Already analysts are responding by raising earnings estimates and raising growth targets for 2017.

The problems facing the global economy have not suddenly gone away, even as Trump has made the US domestic economy one of his main priorities. Europe is still a daily crisis with seemingly insolvable debt, demographic and political issues. China is as enigmatic as ever. Their economy is a key global component. The same can be said of India, Latin America and the other emerging market economies. Russia and the Middle East are not getting any quieter. So the parade of potentially market disrupting events marches on. We'll see if we are better able to deal with it.