

Investing In The Blue Wave

Stock markets have rallied even as a group of pro-Trump insurgents rampaged through the U.S. Capitol and the number of COVID-19 infections and deaths continue to rise. Investors are focused on the increased likelihood of additional relief spending due to the new Democratic administration's control of Congress *and* the Federal Reserve's commitment to ultra-low interest rates.

As a result of the Georgia Senate elections, the Democrats hold sway over both the House of Representatives and the Senate. That power means they will be able to push through fiscal stimulus in areas like infrastructure, healthcare, education and aid to the states. This spending will complement the huge monetary tailwind coming from the U.S. Federal Reserve. The outcome in Georgia strengthens the Biden mandate to remake the economy and "build back better". Barring any new COVID-19 surprises, the economy is expected to grow sharply in 2021.

This is a stock market determined to march higher. Investors need to keep their eyes forward and look ahead to what should occur under a Biden presidency: more predictable domestic policies, improved trade relations and most importantly, additional efforts to revive the economy. At the same time, investors must be aware that not all Biden policies will have a positive impact on stocks. The President-elect has a to-do list for tax changes, including a higher tax on investment income, a return to the top individual rate of 39.6%, and an increase in the corporate rate from 21% to 28%, all of which would be a detriment to a rising market.

The leader board in U.S. stocks has switched since the Georgia denouement. Long favored tech stocks like Apple and Microsoft have lagged behind the broader market. The tech sector had outperformed since the outbreak of COVID-19 as rock-bottom interest rates bolstered the appeal of businesses whose valuations are dependent on profits in the distant future. Investors have rotated away from tech into economically sensitive sectors such as small cap and value. Small businesses are more domestically driven than their large counterparts, so the rollout of vaccines and a return to normalcy by American consumers should lift small cap and value - those sectors hardest hit by the pandemic – higher than the tech names.

There will be bumps in the road. A geopolitical crisis can suddenly arise at any time. Expectations for the pandemic to recede rapidly are already baked into corporate profit estimates. The ambitious social and economic policies will drive deficit spending and fuel inflationary pressure, which would undermine stock prices. A temporary decline in the market due to rising interest rates, however, is not a bad thing, as it signals that the fortunes of our country in general are finally on the rise.

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