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FUSCO FINANCIAL ASSOCIATES

Market Commentary

To Our Valued Clients,

As much as I would like to present you with a different topic of discussion for this week's market commentary, when there's an elephant in the room, you can't just ignore it and discuss the ants. Over the past few weeks, we have seen the Taliban regain control over many provincial capitals throughout Afghanistan before finally taking control of the national capital of Kabul this past Sunday. The swift resurgence of power comes amidst the ongoing withdrawal of U.S. and NATO Military forces which started back in May of this year.

Events such as this give rise to a question that investors commonly face; what is the impact of major geopolitical developments on financial markets? As you can imagine the answer is anything but simple. Conventional wisdom might say that an increase in geopolitical risks would heighten returns from perceived safe-haven assets while dragging down stock prices. While this may sometimes be true, there are numerous instances throughout history that lend themselves to the contrary. For example, from August of 1990 through February of 1991, the S&P 500 gained 3.25%[1] while facing both the threat and occurrence of the Gulf War. During this same period yields for U.S 10-year treasury bonds remained largely unchanged. More recently, from June through September of 2016 while tensions between the United States and North Korea were rising, the S&P gained 3.30%[2] and U.S 10-year treasury yields rose. We can even take this past Monday as an example, on the day immediately following the Taliban takeover of Kabul, the S&P 500 and Dow Jones both closed at all-time highs. Simply put, markets don't always respond the way one may think. Additionally, some theoretical arguments state that financial markets react more strongly to geopolitical rumors or threats than actual events. This lends credence to the idea that investors loath uncertainty and that actual events can provide clarity. Once again there are instances of this having played true, but empirical evidence also displays examples of markets reacting more strongly to actual events versus rumors. In short, it can often be difficult to find any strong correlation between geopolitical events and asset returns.

[1] Federal Reserve Bank of St. Louis
[2] Federal Reserve Bank of St. Louis

Major geopolitical events like the one we are currently seeing in Afghanistan are unique and each event offers its own set of particular circumstances and complexities. As such, from the context of financial markets, these events cannot be viewed in a vacuum and market reactions depend largely on the context surrounding each situation. While for some it may seem tempting to act on shifts in the geopolitical landscape, it is important for long-term investors not to overreact. Patience is essential.

With My Best Regards,

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