Southern Capital Perspective

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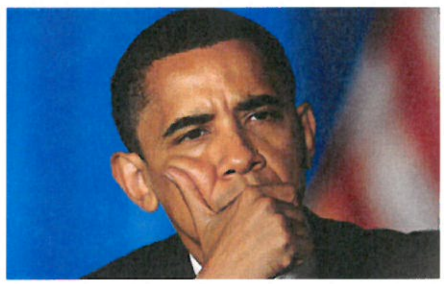
Is the USA at War?

There seems to be a great deal of confusion as to the answer to this question. The Administration has reluctantly begun calling the current military action against ISIS or ISIL, a war instead of their preferred term "counterterrorism campaign." Congress, on the other hand, has not said anything officially because they are on their election break until November. Individual Representatives and Senators have commented, but no official action from the Congress has been taken.

So … is it a war or not? The American people understand the old expression: "If it looks like a duck, swims like a duck, and quacks like a duck, then it probably is a duck." Therefore, if Americans are dying (two beheaded American journalists) and U.S. Navy and Air Force fighter jets and bombers are conducting airstrikes, then it is a pretty safe assumption that we are at war, although unofficially.

How can we be unofficially at war? Actually, the last time the U.S. was officially at war was WWII when Congress declared war in accord with the Constitution under Article 1, Section 8. All of the conflicts, from Korea 1950-1953 through Libya in 2011 and now Iraq and Syria in 2014, have taken place outside the authority that comes from our governing document, the U.S. Constitution. This situation has arisen because the Executive Branch of the Government is always seeking to expand its power by interpreting the law to allow the President to do whatever he wants to do.



Congress has gone along with many of the President's wishes in because it has relieved Congress from having to take a vote and an official stand on an issue as important as war. If a war is not going well (as most wars do not at some point), then a Representative or Senator who did not have to vote for a declaration of war can easily come out against the war after the fact.

Executive Branch *(the White House)* assertiveness in conjunction with Legislative Branch *(the House and Senate)* inaction has led to division, strife, and disunity in our nation, especially when it comes to fighting wars. If Congress was required to vote on a declaration of war before military action could be taken, then the nation would be forced to decide whether we fight or not and thus live with that decision.

Wouldn't it be refreshing to see our Representatives and Senators, in accordance with the Constitution, have the courage to come back to Washington, debate the pros and cons of going to war, then decline or declare war, pass it in both houses, and put it on the President's desk? The President would then have the responsibility to prosecute the war with the full authorization of Congress as the representatives of the people.

Following the Constitution made America the greatest nation on earth. Hopefully we can get back on that path.

HOW DOES THE STOCK MARKET RESPOND TO WAR?

Conventional wisdom would say that war is bad for the economy because vast amounts of money and resources are poured into weapons and war machines that do not produce goods and services. In fact, those very weapons and war machines are destroyed in the process. The reality seems to suggest that the events leading up to war are bad for the stock market, but once war begins, the market generally begins to rise. The fact that no war since the Civil War has been fought on our soil is a very important consideration determining the market's behavior.

To examine the effects of war on the U.S. stock market, we will look at market history going back to World War II.

See Chart on Next Page

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STOCK MARKET HISTORY THROUGH WARTIMES

The three years leading up to the US entering WW II:

Year	Market return
1939	- 4.10%
1940	- 9.78%
1941	- 11.59%

The WW II war years:

1942	+ 20.34%
1943	+ 25.90%
1944	+ 19.75%
1945	+ 36.44%

The two years leading up to the U.S. entering the Korean War:

1948	+ 5.50%
1949	+ 18.79%

The Korean War years:

1950	+ 31.71%
1951	+ 24.02%
1952	+ 18.37%
1953	- .10%

The two years leading up to the U.S. entering the Viet Nam War:

1962	- 8.73%
1963	+ 22.80%

The Viet Nam War years:

1964	+ 16.48%
1965	+ 12.45%
1966	- 10.06%
1967	+ 23.98%
1968	+ 11.06%
1969	- 8.50%
1970	+ 4.01%
1971	+ 14.31%
1972	+ 18.98%
1973	- 14.66%
1974	- 26.47%
1975	+ 37.20%

The year leading up to the First Gulf War:

1990	- 3.17%

The First Gulf War year:

1991	+ 30.55%

The two years leading up to the Afghanistan War:

2000	- 9.10%
2001	- 11.89%

The two years leading up to the Second Iraq War:

2001	- 11.89%
2002	- 22.10%

The concurrent Afghanistan and Iraq Wars Years:

2003	+ 28.68%
2004	+ 10.88%
2005	+ 4.91%
2006	+ 15.79%
2007	+ 5.49%
2008	- 37.00%
2009	+ 26.46%
2010	+ 15.06%
2011	+ 2.11%

The Iraq War ends but the Afghanistan War continues:

2012	+ 16.00%
2013	+ 32.39%

The general conclusion that can be drawn from the historical market performance is, in most but not all cases, the years leading up to war are generally weak, but when the wars actually begin, the markets are stronger. However, it is important to remember that our homeland has for the most part been spared the ravages of war since the Civil War – with the two exceptions of Pearl Harbor and the "9/11" attack. The economic impact on a nation where the war is actually fought is very severe and very negative.

Although war is a scourge to mankind, it is also an event that causes governments to spend a lot of money and buy a lot of war materials which stimulates the economy even though it adds a lot of burdensome debt to the government.

Outlook

It seems that we are heading into another war in the Mideast. This time is very different from the other two Iraq wars because ISIS has said that they are coming after us. It is not, therefore, arbitrary on our part. Also, this war is being waged in a bizarre manner (at least at this point) because there are no "boots on the ground" — ours or anyone else's. So far, the market has not shown a great deal of concern and is only a few percentage points off of its all-time highs.

The U.S. economy is in the best shape compared to the other global players: Europe, China, Japan and Russia are all having political and/or economic challenges. We are continuing to grow slowly and our rate of growth may even be slowing down, but it is still positive.

There is an abundance of cash on the sidelines (future market fuel) and stocks are the asset class that makes the most sense even though equity prices are not selling at bargain prices. They are not over-valued either, especially when you consider how low interest rates are. Therefore, we are maintaining our present investment mix of assets with the ever-present awareness that a correction could be at hand, but aside from a major geo-political event, we do not foresee a "bear market" on the horizon.