

FINANCIAL FOCUS

Robert Smith says the stock market may benefit from Tea Party candidates prevailing in upcoming elections. **Page 5**



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Tea Party's uprising could aid economy

November elections likely to result in a reshaped Congress and perhaps a stronger stock market

So, why is the stock market rising so much and so suddenly? After all, investors just moved more money from stocks to bonds than at any time in recent memory.

Free market capitalism is back. This is the message being sent to the capital markets via recent Tea Party primary victories in Alaska, Delaware, New York and New Hampshire. As Lawrence Kudlow said recently, "The free-market power of the Tea Party political revolt is totally bullish for stocks and the economy."

The Tea Party movement is stopping Barack Obama and his radical lurch to the left with Keynesian-style big government spending and planning dead in its tracks. It is Reaganism on steroids. In short, it is transforming the Republican party and will transform Congress. The markets already know this won't be your father's Congress, so it won't be business as usual. In 2011 and 2012 it will hold back the government tide and unleash a wave of entrepreneurship and capitalism not seen since the 1980s and the



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"Reagan revolution."

This will in part be accomplished by an extension of all the Bush tax cuts through 2013. There are enough endangered Democrats running away from the president and Nancy Pelosi to make this possible. There is also a growing awareness that increasing taxes on households earning more than \$250,000 adds an unnecessary risk to the short-term recovery when it can least afford it. America's experience in 1937 and Japan's in 1997 are powerful evidence that ill-timed tax increases can tip weak economies back into recession.

Higher taxes at the top (those who create jobs) and waning fiscal stimulus and belt tightening by states, will further weaken the growth rate. Obama may not mind being the author of an American "lost decade," but his party can ill afford it. Surviving

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Democrats will begin to look beyond his presidency.

Investors believing that a remade Congress will work hard to restrain government spending will then make the stock market stronger and more rewarding. Furthermore, Ned Davis Research tells us that stocks have historically performed best when a Democrat occupies the White House and Republicans control Congress.

Financial stocks may rally. More fiscal restraint from a Republican-controlled Congress would be good for bank stocks in particular. Defense stocks may rise as Republicans have historically favored military spending more than have Democrats. Health-care insurers may also

enjoy a reprieve as this transformational breed of free-market Republicans work over time to de-fund Obama Care.

Specifically, pure plays in the defense industry are: Lockheed Martin Corp., Raytheon Co. and General Dynamics Corp., all of which are trading at 10 times earnings or less. Other, defense-related stock possibilities are: Boeing Co., United Technologies Corp. and Precision Castparts Corp. However, these are more reasonably priced.

In the banking sector, I particularly like JP Morgan Chase & Co. It is arguably the most conservatively managed money center bank. Its absorption of Bear Stearns two years ago became

part of the solution, not the problem. The stock is selling for 12 times earnings or slightly less than book value.

So, now is not the time to desert stocks. Cash flow and dividend yields suggest equities are cheap. This is largely being ignored by investors burned by the 2008 financial crisis. When this disconnect is coupled with the free-market power of the Tea Party about to wash over Washington, it may provide intrepid souls with a uniquely profitable opportunity.

The road to full recovery will still be long and difficult. However, with a more realistic, market-centric set of policies at work we will work off the recession hangover faster. Americans are accustomed to traveling great distances. It is simply a matter of making sure our political leaders understand which road we should be traveling.

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