

Should You Invest in Defense Contractors as War in Korea Looms?

Defense stocks have outperformed the broader market by 15% to 10% since Trump was elected. These companies are in the news after the USA attacked a Syrian air base with cruise missiles and dropped the MOAB (Massive Ordinance Air Blast) bomb on an ISIS mountain tunnel complex in Afghanistan. Many believe that the weapons were used to send a message to North Korea regarding its nuclear and missile programs. The end result has been a huge elevation of tensions on the Korean peninsula while the US sends an aircraft carrier group to cruise off of Korea. Meanwhile Trump wants to increase military spending by 10%. *Market Watch* discusses why **defense stocks outperform** the rest of the market.

With U.S. military strikes top and center in the news, readers have been introduced to some of the most advanced and powerful weaponry built by aerospace and defense companies.

Because of the complexity of government procurement processes, the use of certain missiles doesn't necessarily mean the makers of those weapons will benefit from near-term increases in sales. But it's helpful for investors to know which contractors have been most successful recently, and which are most favored by analysts.

Tomahawk cruise missiles, manufactured by Raytheon Co. RTN, +0.64% were used against a Syrian airfield on April 6. The Massive Ordinance Air Blast (MOAB), or "mother of all bombs," is made by Boeing Co. BA, +1.43% and was used against Islamic State terrorists in Afghanistan last week. Raytheon is the fourth-largest U.S. defense contractor, with a market capitalization of \$44.5 billion, while Boeing is the biggest player, with a market cap of \$106.8 billion.

There are twenty-eight defense and aerospace companies in the S&P 1500 composite index. The five largest are Boeing, Lockheed Martin, General Dynamic, Raytheon and Northrop Grumman. These stocks have an EPS range based on projected 2017 earnings of 17.1 for Boeing to 19.1 for Lockheed Martin. These stocks have been bid up on the expectation of more defense spending and the possibility of increased armed conflict, especially in Korea.

Which Should You Buy?

24/7 Wall Street lists **aerospace stocks to buy** before first quarter earnings are announced.

In a new Deutsche Bank research report, outstanding analyst Myles Walton makes the case that Wall Street in general remains more positive on the defense stocks, and

overall more neutral on commercial aerospace companies. The analyst likes three top stock picks from both areas into the first-quarter earnings, and all are rated Buy at Deutsche Bank.

Their picks only include one of the top 5, Lockheed Martin. The other two are Rockwell Collins which does *design, production, integration and support of communications and aviation electronics for military and commercial customers worldwide*. The other is Transdigm which is a *holding company for businesses that offer a diverse array of products including ignition systems, pumps, valves, motors, actuators, controls, water faucets and systems, quick disconnects and couplings, batteries, chargers and power conditioning, cockpit security systems, composites and elastomers, audio systems and lighting and displays*. This later stock is a recovery play on top of being something you might invest in as tensions mount across the globe.

The point of investing in defense contractors is not that their profits will go up greatly from the use of a handful of cruise missiles or from dropping one really big bomb. Rather the logic is that when the nation is worried about war it funds defense spending on projects that take years and provide a cash stream to the recipients along way and this cash stream translates into higher stock prices and dividends for you the investor.

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