Elections & Markets Report

Presidential elections are one of the grandest stages for political theatre. In the coming weeks, much will be written, and many predictions will be made, about who will win the upcoming election and the likely implications for markets.

For investors, it is important to keep these periods of heightened political focus in proper perspective to avoid the potential pitfalls of short-term, emotionally-driven decisions that could prove destructive to long-term financial planning. With over a century of stock market data across dozens of presidential elections cycles, history offers valuable perspective for investors to consider in seeking to effectively navigate these periods of heightened uncertainty.

Do Elections Impact Markets?

Historically, there has been a link between elections and market returns often referred to as the Presidential Cycle. It recognizes that stock market returns have tended to be below average in the first two years of a presidential term and above average in the last two years. The economic rationale behind the Presidential Cycle contends that during the last two years of a presidential term, the party in power focuses on re-election and therefore is more inclined to increase spending and/or cut taxes in an effort to appease voters and stimulate the economy. This phenomenon has not been associated with presidents from a particular political party but has been especially pronounced with first-term presidents.

Which Political Party is Better for Markets?

Conventional thinking holds that Republicans are generally better for business (and markets) as they tend to favor policies of lower taxes and less regulation to support economic growth and corporate profits. However, history shows that average stock market returns have been higher during Democratic presidencies.

Dow Jones Industrial Average Performance		
When U.S. Government Has A:	**% Gain / Annum**	**% of Time**
Democratic President	7.8	46.8
Republican President	3.3	53.2

Based on daily data 3/4/1901-7/13/2020

Why the apparent disconnect between conventional thinking and history? Put simply, there is more to the story:

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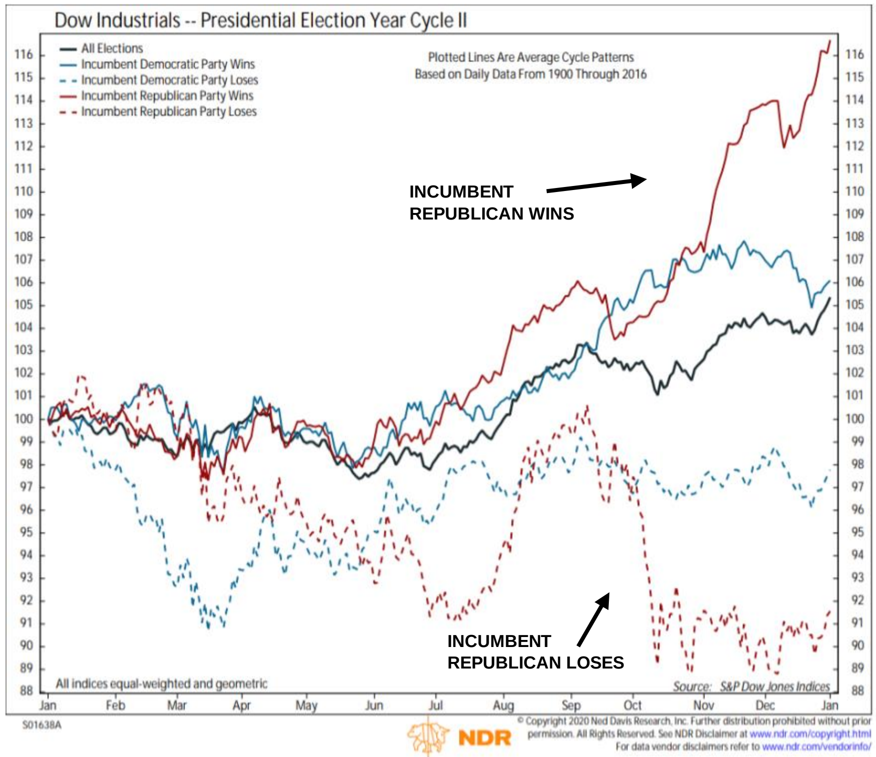
Markets Prefer Incumbents



Market returns during presidential election years have been impacted by whether an incumbent president's party wins re-election. Historically, stock market returns have been above average when an incumbent president's party wins re-election but below average when an incumbent president's party is defeated. This effect has been consistent across party lines but has been more pronounced with Republican presidents over time.

What About Congress?

Although they receive the most media attention, presidential elections are not all that matter to markets, as presidents must work with Congress to enact legislation and advance their agenda.

As discussed earlier, the stock market has experienced above average gains under Democratic presidents. However, these gains have been strongest in periods where there has been a check on a Democratic president's power from a Republican or split Congress. Conversely, stock market returns have been below average under Republican presidents but have been strongest when Republican presidents have enjoyed legislative majorities in Congress.

Dow Jones Industrial Average Performance		
When U.S. Government Has A:	**% Gain / Annum**	**% of Time**
Democratic President, Republican Congress	5.2	10.1
Democratic President, Split Congress	7.9	3.3
Democratic President, Democratic Congress	2.9	33.4
Republican President, Republican Congress	7.1	25.5
Republican President, Split Congress	-5.4	11.2
Republican President, Democratic Congress	-2.1	18.4

Based on monthly data 3/30/1901-5/29/2020

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"It's the Economy Stupid"

This phrase was made famous by Bill Clinton's lead political strategist James Carville during the 1992 presidential election campaign. It expresses the widely held belief that the state of the economy, and how people feel about their personal financial situation, are the most important factors in determining election outcomes.

Historically, the incumbent president's party has lost the White House 80% of the time when the U.S. economy has been in recession or the stock market has declined by 20% or more in a presidential election year. This compares to the incumbent president's party having retained the White House nearly 70% of the time when these challenging conditions were not present in the economy and/or markets during an election year *(Ned Davis Research).*

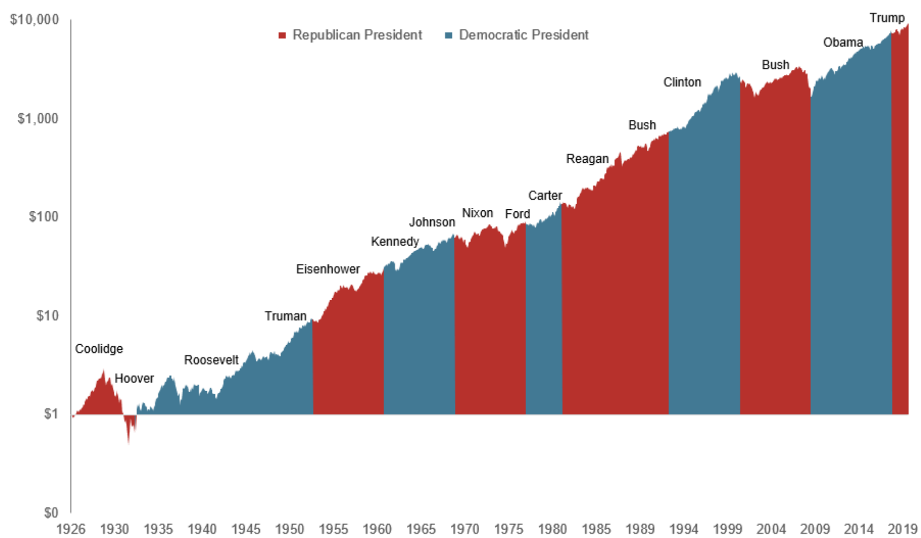
Since 1948, no incumbent president's party has retained the White House when there was either a 20% decline in the market or a recession in a presendential election year *(Ned Davis Research)*. In 2020, we have experienced both a recession and a significant decline in the stock market, which suggests history is not on the side of President Trump staying in the White House.

Implications for Investors

While it may be tempting to try to time the market around elections to gain an advantage, one should remember that past performance is not a guarantee of future results. History suggests that the markets have rewarded long-term investors regardless of which political party controls the White House. Arguably, the best course of action is to cast your vote and stay focused on your financial plan.

Markets Have Rewarded Long-Term Investors under a Variety of Presidents

Growth of a Dollar Invested in the S&P 500: January 1926–December 2019



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