The Stock Market is Eyeing the Upcoming Presidential Election

Are you worried about how the results of the upcoming presidential election will affect your portfolio? Without doubt we are living through unprecedented uncertainty during a global pandemic and amidst unprecedented animosity between our two main political parties. Is it time to sell out of stocks and wait for calmer days? I would discourage anyone from embarking down that road without a well thought out plan and the proper guidance. Over the years I have met countless investors who did just that and either never got back into the market and have been sitting on significant piles of cash for years or, when they did eventually get back in, they did so at much higher levels then when they sold. Unless you are following a proven and reliable market timing strategy, avoid trying to time the market on your own.

Many are concerned that the stock market will react unfavorably if the right candidate is not elected. Democrats generally want higher taxes on capital gains and corporate earnings. They also tend to favor regulations like increased minimum wages which can reduce corporate profits. Conventional wisdom suggests that Republican policies of lower income and capital gains taxes lower corporate taxes, and more business-friendly laws and regulation are much better for the stock market. All those points seem logical but if we look at the numbers alone, the stock market has done better by far under the Democrats. The disparity is quite surprising. Since the end of World War II the average total return during a Democratic president's term was 53% vs. 26% for Republican presidents. However, if you go back to 1929, the total return of the S&P 500 has averaged 57.4% under Democratic presidential administrations versus just 16.6% under Republican presidents.

If your anxiety level is high, there may be some cause for optimism. Election years have generally been good for stocks. Since 1952, the Dow Jones Industrial Average has climbed 10.1% on average during election years when the incumbent runs for reelection, according to the Stock Trader's Almanac, which is used by many investors to track historical patterns of stocks and indexes. Over the same period, the index has fallen 1.6% during election years when there is an open field. In the years leading up to an election, sitting presidents tend to use all of the tools at their disposal in the form of lower taxes or favorable fiscal policy to prop up the economy and the stock market to help their chances of reelection. Amidst the current pandemic, we have never seen such an extensive and dramatic use of monetary policy, and federal stimulus to bolster the economy. This is creating a tailwind for stocks. Since 1990 the six months preceding the election year has produced positive returns 6 out of the last 7 times except for 2008 during the financial crisis. Consistent with that pattern since April, the S&P 500 is already up 33%, at least in part based on the stimulus.

Regardless of who wins, the markets will immediately react and attempt to discount the effect of the anticipated policies from the incoming administration. If the market perceives those policies to be detrimental to corporate earnings, prices of stock will typically go down in anticipation of those policies even before the president is inaugurated. For those who anticipate the market falling if the "wrong" candidate is elected, consider this. Since 1972 if you look at the period between the day the president was elected and the date the president was inaugurated, the market was up during that approximate 1o week period 11 out of the last 12 times, with an average gain of 3.85 during those years. The one notable exception was at the end of 2008 during the economic crisis. So perhaps there is no need to panic about the upcoming election, regardless of who gets elected, although with the current state of the economy and the pandemic there is certainly cause for concern.

Finally, the stock markets are certainly aware of current polling numbers and the market likely has already priced in the possibility although not the certainty of a Democratic president.

One trend to keep an eye on however is that when the stock market has risen in the three months before an election, the incumbent party generally has gone on to win the White House; when it has fallen, the incumbent party has generally lost. Voters who are happy with the economy and their personal financial statements tend to want to avoid change. Since 1928, this trend has held up 87% of the time and has not failed since 1980. While the S&P 500 has had a nice recovery, we are still dealing with a pandemic that could inflict further damage on the economy.

Finally, one should remember is the reason stocks and ETF's are used by investors is because they generally go up more than inflation over long periods of time. Over the short term they sometimes go up, but they often also go down. Therefore in theory it doesn't really matter what happens in the short term. Many investors, however, have a hard time accepting that concept.

We are committed to helping you achieve your financial goals. Please feel free to contact us with any questions, comments, or a more in-depth discussion.

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