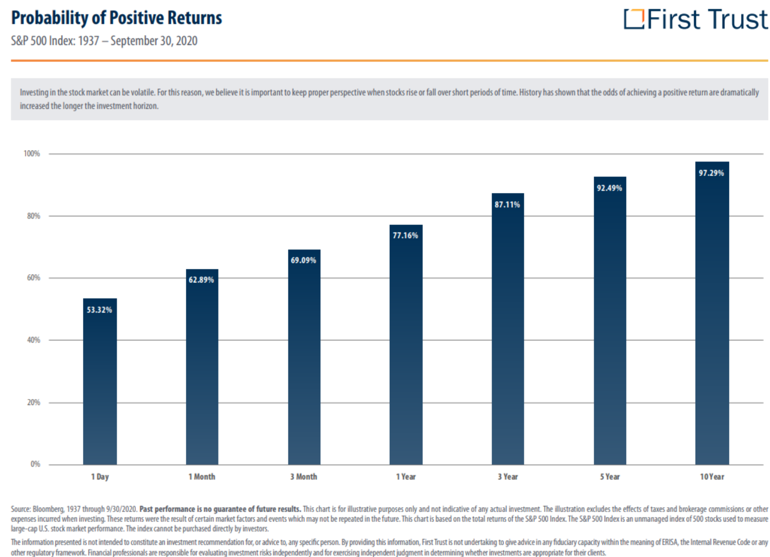
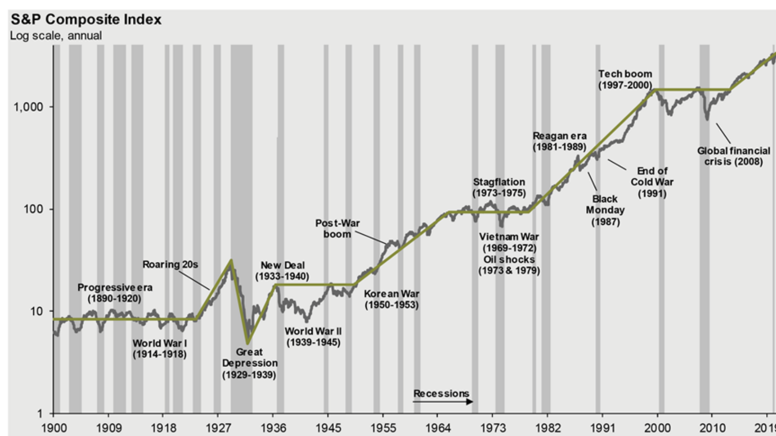
ELECTIONS HAVE CONSEQUENCES...MAYBE

Rule number one of investing: the stock market goes up over time. This is an indisputable fact. And any basic finance class teaches the critical concept of the time value of money. Simply put, the longer your time frame, the greater the potential value of an investment. This can be applied to most asset classes. Conversely, the shorter an investor's time frame, the higher risk of negative returns. Holding period matters greatly, as illustrated in this chart:



Apart from the worst economic period in our country's history, the market has consistently trended up.



Source: FactSet, NBER, Robert Shiller, J.P. Morgan Asset Management.
Data shown in log scale to best illustrate long-term index patterns. Past performance is not indicative of future returns. Chart is for illustrative purposes only.
Guide to the Markets – U.S. Data are as of September 30, 2020.

J.P.Morgan
Asset Management

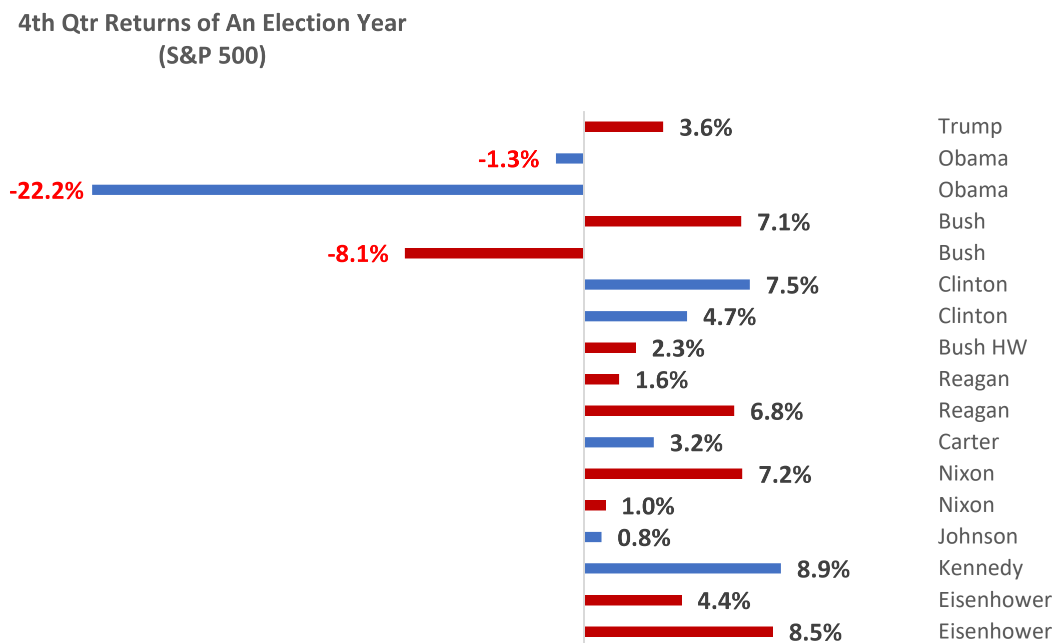
Now we are on the doorstep of an election, one that many believe may have the greatest consequence in the post-World War II period. The most common question we get is "what does the election mean for the market?" or "what happens to the market if (Trump/Biden) wins?" The underlying fear is that the market will correct, or even crash. Is there any real basis for such concern?

PERFORMANCE DURING AN ELECTION YEAR

Our team looked at a variety of data going back to when Dwight D. Eisenhower was elected president in 1952. We deliberately wanted to look at the post-Depression era.

First, in examining the quarter when a presidential election is held, we found that the weakest market returns in that time period came in 2008, when the S&P 500 lost more than 22% of its value between October and December. The best performing 4th quarter in an election year was in 1960, when John F. Kennedy was elected. What's more important, though, is that stock performance has been positive 82% of the time in the fourth quarter of an election year.

(red bar = R, blue bar = D)



Of the 14 quarters when stocks rallied, nine occurred when a Republican won office, with an average gain of 4.7%. The remaining 5 periods of positive gains occurred during a Democratic win and gained an average of 5%. Here is some additional pertinent data related to returns:

- Since the 1952 election, in the months of October to December, the range of returns was -22% to +9%
- The average market return during positive periods was +4.8%
- The average market return during negative periods was -10.5%

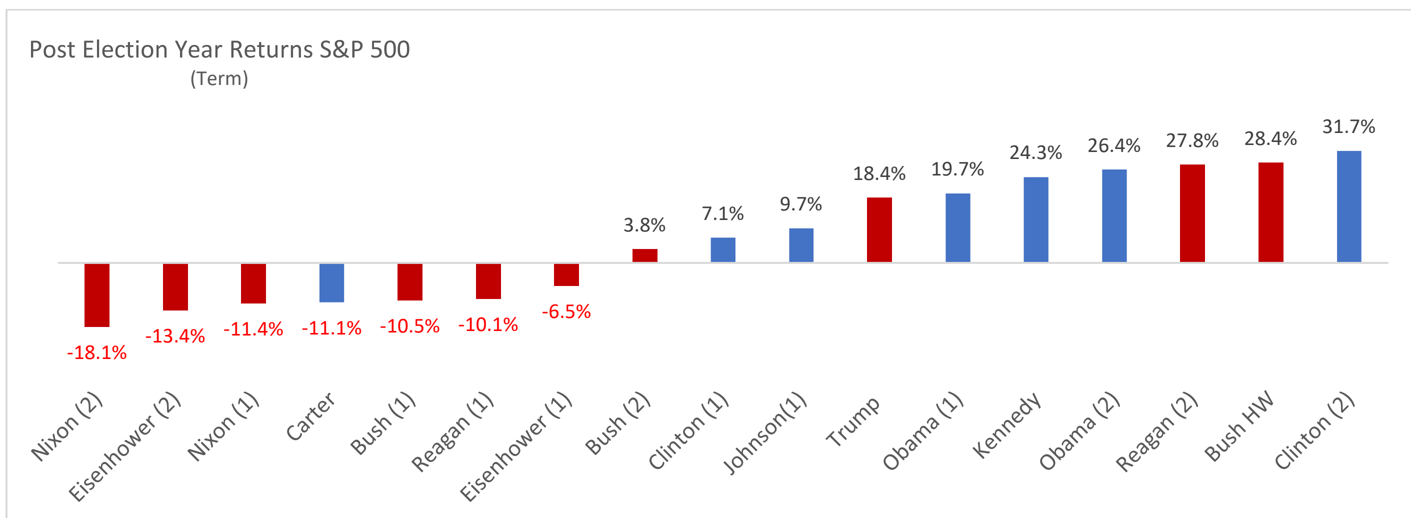
- Both the best and worst performing 4th quarter in an election year occurred when a Democrat won the presidential election (Kennedy, Obama respectively), and both times the Democrat succeeded a Republican

Next, we looked at the year following an election.

The Democrats have an edge here, and by a decent margin. Of the 17 elections starting with 1952, ten have been won by the GOP, seven by the Democrats. Of those seven wins, only one was immediately followed by weak stock performance, under Jimmy Carter. Some other notable stats:

- The gold, silver, and bronze go to Clinton, Bush (HW), and Reagan respectively for calendar year stock market performance following their election wins
- The average return was 15.4% for Democrats, with positive performance 85% of the time
- The average return was 8.3% for Republicans, with positive performance 40% of the time

Here we see a ranking of stock market returns, worst to best, in the calendar year following an election:



Yes, but…!

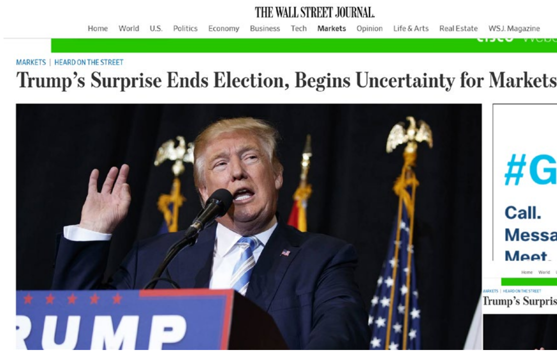
We have heard the arguments to fit a political leaning. Generally, there are two:

- A Republican administration is better for stocks because a core GOP ideal is smaller government, which loosely translated has meant fewer regulations and lower taxes; OR
- A Democratic win would return the country to institutional norms and less government disruption, which would calm a volatile stock market.

Data, and history, do not fully support either claim. In 2016 it was widely believed that a Hillary Clinton win was better for the market because Donald Trump was such a non-traditional candidate. This is not merely my opinion; look at reporting by financial news media before and after that election:

Wall Street's long-running view that [Hillary Clinton](#) would easily become the next president has been replaced by a new fear that [Donald Trump](#) could win, and it probably won't be a pretty picture for stocks if he does.

(CNBC, Nov 2, 2016)



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MARKETS | HEARD ON THE STREET

Trump's Surprise Ends Election, Begins Uncertainty for Markets

The New York Times

DealBook/ Business & Policy

DEALBOOK

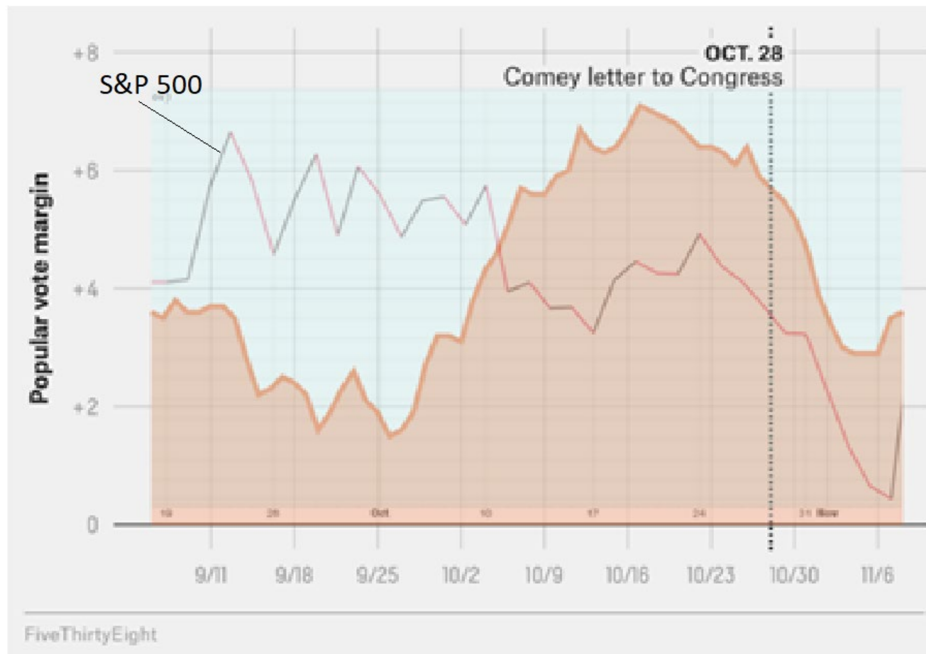
What Happens to the Markets if Donald Trump Wins?

The conventional wisdom is that, right off the bat, the stock market would fall precipitously. [Simon Johnson](#), the Massachusetts Institute of Technology economist, [posited that Mr. Trump's presidency](#) would "likely cause the stock market to crash and plunge the world into recession."

(Nov 9, 2016) (Nov 1, 2016)

On October 28th, 2016, James Comey, the Director of the FBI at the time, sent a letter to Congress announcing that the FBI had uncovered additional emails pertaining to Hillary Clinton's use of a private email server as secretary of state. Prior to that letter her poll numbers were surging; they subsequently collapsed. The stock market was up approximately 6% going into late September, when it gradually started to sell off. In the week prior to the election, stocks lost 3% of their value and bottomed the day after Donald Trump was elected.

We see below that stock prices started to trend closely with Clinton's poll numbers. The selloff began on October 23 and bottomed the day after the election.



Considering the headlines and polling data, it seems clear that markets were pricing in a Hillary Clinton victory. And markets hate surprises and uncertainty. But clearly, the Trump win was not as awful for stocks as many predicted, and maybe not even much of a surprise for financial markets. The S&P 500 gained nearly 7.5% from election day to the end of 2016.

Ascribing causation by correlating only two data points is weak analysis. There are a multitude of factors that move stocks. The three we pay closest attention to are market valuation, the attractiveness of stocks vs. other assets, (bonds, most significantly), and investor sentiment. In the autumn of 2016, none of those three data points suggested an impending correction in stocks.

DOES IT MATTER WHO WINS?

In the end, even the most careful analysis of presidential elections is only of limited utility when it comes to prognostication. Consider another factor: the overall macroeconomic conditions present during different administrations. George W. Bush inherited an economy in 2000 that had just peaked, along with a stock market bubble. Rising unemployment caused the market to contract by 10% during Bush's first year in office. On the other hand, in 2009 Barack Obama took office during the worst financial crisis in generations, close to its nadir. As a result, the only place to go was up, and the market rose nearly 20% during his first 12 months.

Today we have a reasonably valued stock market, with no decent alternative as bond yields are non-existent, and an anxious investment community. Remember, poor investor sentiment is good for stocks. These factors should help keep any decline in stock prices shallow.

A concluding thought: maybe the election for the leader of the free world doesn't have much real influence on markets! A disappointing concept, to be sure, especially if you are looking for a clear-cut answer to the question of 'what happens if ____wins the election.' Likely, you already have a strong feeling about who *should* win the election, and perhaps you've been looking for financial commentary to support that feeling. The lesson here, though, is that financial analysis is never this cut-and-dried, and even less so during a period of tremendous political uncertainty.

The best advice, as always, is to ignore the noise of the financial media, think like a contrarian, and for heaven's sake, if nothing else, remember rule number one.