Election Economics

As 2024 forges onward, we must not digress from the overarching themes that we are continuing to navigate. There has been a welcomed shift into the New Year with the October 2023 lows demonstrating a substantial turnaround in both Canadian and US financial markets. As we turn the page, the current President of the United States, Joe Biden, most recently celebrated new record highs on the S&P 500 as the index surpassed the coveted 5000 level. This felt like an insurmountable feat in 2022, but investors are being rewarded for showing patience and resilience. After a tumultuous 2 years, and a 2020 prediction by former President Donald Trump of a full market collapse under Biden's oversight, we are now in expansive terrain for equity markets.

The jury is still out on timing of rate cuts and a forthcoming accommodative stance from our central bankers. The markets are once again showing signs to be remarkably durable and can be looked at from two angles. One angle permeates a soft-landing narrative, which would ultimately avoid a recession. This could lead to the less sought-after angle of inflation being reignited if rates are cut too soon. The perennial optimist in me speculates that a soft landing in the economy can set the table for stronger corporate earnings. This outcome is invariably reflected in positive stock prices as we embark on yet another presidential election.

A Refresher on American Politics

Americans will head to the polls in November 2024 to elect the next US President. The person situated in the White House's Oval office is widely regarded as one of the most powerful and influential individuals on the planet. Their deliberations and execution of fiscal decisions impact global functionalities as this unilateral economy holds presence internationally. It is integral in this contemporary society we live in to have integrity at the top of the house. The US Political system, although complex, can be simplified to a two party democracy since the Republicans subsumed members of earlier parties in 1860[1]. The Democrats would be considered the liberal political party, traditionally holding a political agenda that exemplifies civil rights, comprehensive social security and at the forefront, climate change mitigation and adaption [2]. The Republican party (also known as the Grand Old Party), has held a heavy stance on lowering taxes and an unwavering belief that the free market is a more efficient way to solve societal problems than through government intervention. From a pure economic lens, both parties can provide equitable or capitalistic upside. In 2020, data from the US Census Bureau showed that 60% of eligible Americans voted in the presidential election, the highest level in three decades[3]. That equates to ~155M Americans[4]. A strong turnout is expected to be mirrored this year.

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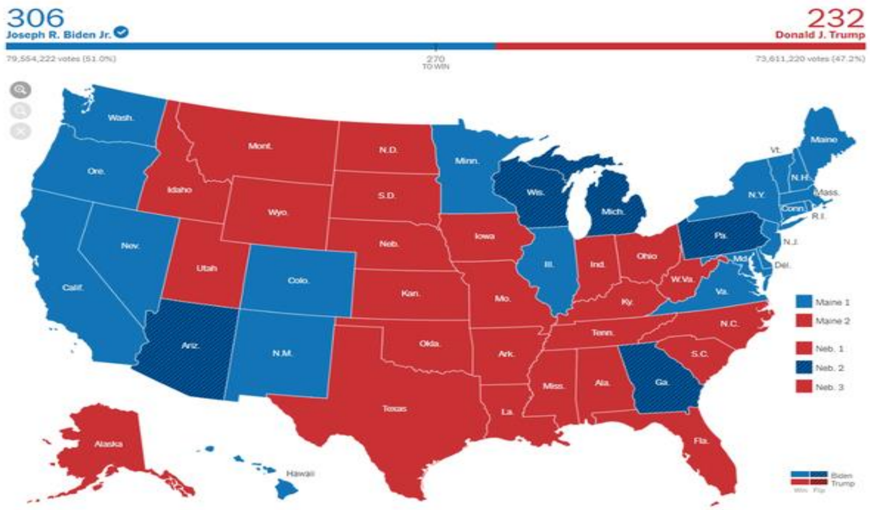

[5]

The frontrunner for each party is nominated in through an extensive series of primaries or caucuses. March 5th is a notable date, as over a dozen states hold their primary contests same day [6]. As of right now, President Biden and President Trump are the leading frontrunners for their respective party nominees. Following the electoral college voting review (a conversation for another day), the Presidency is awarded. American citizens will also be choosing new members of Congress. Having majority control of the House and Senate allows President's to administer their political agendas and a slate of amended legislation less susceptible to pushback.

As an example, investors will start to price potential changes in taxes, tariffs, and technology as they gain more clarity on the outcome. A Trump centric investor would price in corporate upside from tax cut extensions and/or appreciation in domestic focused goods and services companies with less foreign exposure. This can also spur anti-trust concerns and highly scrutinized trade policies, which almost always develops more downside risks as well [7].

How do Elections Historically Impact the Markets

Our BMO Economics team provided a condensed numerical map of S&P 500 cycle performance leading up to and following the much-anticipated presidential elections.

S&P 500 Election Cycle Performance*

	Avg. return (%)	% positive
Year before election	17.2	89%
Election year	7.3	83%
Year after election	7.9	61%
2 years after election	3.7	56%

Period 1952 to 2023

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For 70 years since 1952, the S&P 500 averaged a solid ~7% gain on the presidential election year (albeit, lagging average returns). In contrast, leading up to the election year, the index returned ~17%. Returns are far more pronounced as conventional wisdom has shown us that the markets are often anticipatory leading up to a known event. There is a litany of data points in between, but it appears that there is some uniformity as positive returns were reflected under both circumstances over 80% of the time.

While there are no shortages of events impacting global relations, one discernable influence is the outcome of a presidential election. These cycles can have differing effects on tax schemes, climate focus, and trade relations, which are all directly correlated with corporate America. It is understandable that voters and investors akin continue to explore the dichotomy of two competing political schedules and make inferences on the direction of the capital markets**. Past performance during election years can be variable, through macro economic turbulence, or structural economic regime changes.** The below illustration sourced from Morningstar on past presidential term cycles showcases two fundamental points. The first being time is one's greatest strength when investing. The second (and more relevant to this piece) is that the most diversified market on the globe does not gyrate through extended periods of Democratic or Republican representation**. Regardless of who is in the chair, the barometer for the US economy continues to march upward.**

SOURCES: Morningstar, Standard & Poor's. As of 12/31/19. Dates of party control are based on inauguration dates. Values are based on total returns in USD. Shown on a logarithmic scale. [9]

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When shown in a longer-term graph, the subsequent illustration can be generalized from a rosy lens. There were years subject to economic calamity which resulted in negative returns over extended periods. For example, President Bush faced the dot-com bubble burst and President Obama was plagued with a full scale housing market crash. Both of which were out of their control.

Historical U.S. Presidential Election Results		
Election Year	President Elected	S&P 500 Index Total Returns
2016	Trump	12.0%
2012	Obama	16.0%
2008	Obama	-37.0%
2004	Bush W.	10.9%
2000	Bush W.	-9.1%

[10]

What does this mean from an investors lens?

In my opinion, to state that the outcome of an election is the overiding factor to market returns in a twelve month span is as illusory as it is precise. **I pay little credence when Presidents take full ownership for prosperous years in the financial markets, while in contrast, opponents blame incumbents for poor results.** There is a culmination of other factors (growth of labor force, increases in human capital, technological improvements etc.) that contribute to an economic engine and further, the capital markets. At the end of the day, we need a person in office that can either be the "alchemist" of broad-based fortune, or the scapegoat for inevitable market troughs. The main lesson here is that we will face these redundant headlines every four years. From a financial planning lens, Congress positioning, tax policies and health care amendments can impact the cash flows of domestic citizens. But from a pure long-term investor lens, try to avoid the noise and lip service paid by "experts". Throughout all economic modalities, diversification and remaining steadfast will eclipse the inevitable volatility in the short-term. **The reality of the American economic engine is that it will always prevail over the tyranny of the present.**

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Continued ...

1) The Multiparty System: History | Democracy Web
2) Democrat vs Republican: Major Differences between US parties (bestdiplomats.org)
3) How many Americans voted in 2020? (usafacts.org)
4) Census Bureau Releases 2020 Presidential Election Voting Report
5) What's Going On in This Graph? | 2020 Presidential Election Maps - The New York Times (nytimes.com)
6) Which States Vote on Super Tuesday? (usnews.com)
7) US corporations push to roll back Trump-era tax policies they once endorsed | US taxation | The Guardian
8) News & Commentary | BMO Economics
9) Stock Market Performance by President (in Charts) (darrowwealthmanagement.com)
10)https://www.bing.com/ck/a?!&&p=f4d641596396dc54JmltdHM9MTcwOTA3ODQwMCZpZ3VpZD0wZTRkOTdiMC1kMGJhLTZmY2QtMmQ5MS04MzgyZDE5MDZlMTQmaW5zaWQ9NTI5MA&ptn=3&ver=2&hsh=3&fclid=0e4d97b0-d0ba-6fcd-2d91-8382d1906e14&psq=s%26p+500+performance+from+roosevelt+to+trump&u=a1aHR0cHM6Ly9hZHZpc29yLm1vcmdhbnN0YW5sZXkuY29tL3RoZS1lcm5pZS1nYXJjaWEtZ3JvdXAvZG9jdW1lbnRzL2ZpZWxkL2UvZXIvZXJuaWUtZ2FyY2lhLWdyb3VwL1MlMjZQJTIwNTAwJTIwaW4lMjBQcmVzaWRlbnRpYWwlMjBFbGVjdGlvbiUyMHllYXJzLnBkZg&ntb=1

Colin Marinelli, MFin, CFA, CFP
Investment Counsellor & Portfolio Manager
colin.marinelli@bmo.com
902-421-6212

BMO Private Wealth
1675 Grafton Street, 14th Floor
Halifax, NS, B3J 0E9