FINANCIAL MARKET SNAPSHOT

May 28, 2024

Decoding Market Dynamics: Unveiling the Truth Behind Presidential Politics and Market Performance

In this edition of the Market Snapshot, we take a look at past presidential election years and how markets performed under different administrations.

With the upcoming Presidential election stirring anticipation, this Market Snapshot investigates the historical relationship between U.S. presidential elections and the broader domestic equity market. In a landscape saturated with news coverage and political messaging, investors are naturally concerned about potential impacts on the economy and their portfolios. However, amidst the noise, it's essential to discern reliable insights from sensationalism.

Analyzing the performance of the S&P 500 Index since 1926, our study scrutinizes 24 U.S. presidential elections to uncover market trends under different administrations. While acknowledging the complexity of economic events influencing market behavior, the analysis sheds light on the broader patterns transcending political cycles.

Beyond politics, our investigation underscores the significance of market fundamentals and the broader business cycle in driving long-term investment success. While presidential policies may wield short-term influence, the enduring factors of economic growth, global trade dynamics, and technological innovation shape market trajectories over decades. Moreover, the role of independent institutions like the Federal Reserve and the inherent forces of supply and demand underscores the multifaceted nature of market influences.

Ultimately, our findings advocate for a disciplined investment approach grounded in comprehensive research and long-term perspective. By prioritizing fundamental analysis over political speculation, investors are better positioned to navigate market fluctuations and pursue their financial goals with prudence and foresight.

What Data did you Analyze to Determine Market Performance?

In conducting our analysis, we examined the returns of S&P 500 Index, which is often considered a good proxy for the broader market for several key reasons. First, the index includes 500 of the largest publicly traded companies in the United States, representing a wide range of industries. This diversity means that it provides insight into a broad cross-section of the American economy. Second, companies included in the S&P 500 account for about 80% of the total market capitalization of the U.S. stock market, helping to ensure that the index mirrors the performance of the overall market. Third, the S&P 500 has a long history of being a reliable indicator of market trends. Investors and analysts frequently use it to gauge the health and direction of the U.S. economy. The S&P 500 index, in its current form, was introduced in 1957, which marked the beginning of the index as a compilation of 500 large-cap U.S. stocks. However, historical data for the S&P 500 has been constructed retroactively to provide insights into the index's performance before 1957. This reconstructed data extends back to 1926, allowing for a longer-term analysis of market trends and performance.

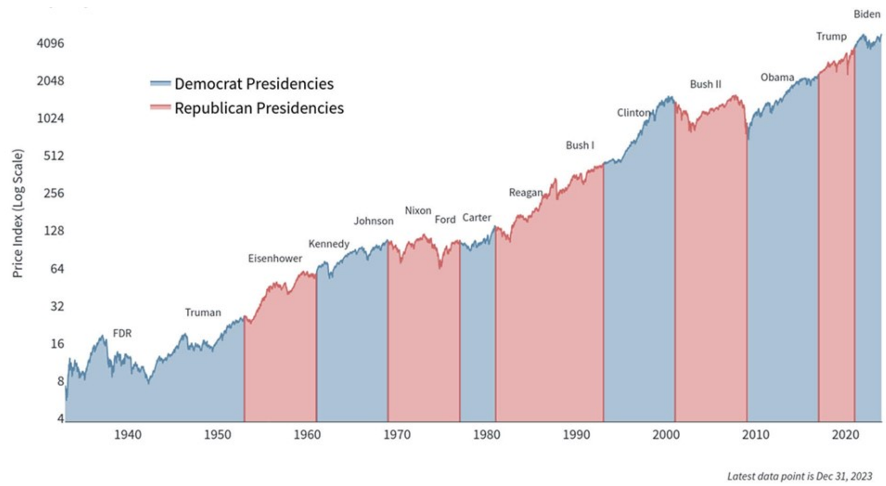
How Many Presidential Elections are Included in the Analysis?

Since 1928, there have been 24 U.S. presidential elections that resulted in 11 Republican and 13 Democrat wins. Over that time period, seven different Republican individuals were elected while eight different Democrats were elected. In terms of time, Republicans have held the White House for 44 years, while Democrats have held the office 52 years. So, while our data set has a fairly lengthy history, it only contains the performance data for 24 elections and 15 elected individuals, making it somewhat difficult to draw statistically significant conclusions about how those elections impacted stock market returns.

Perhaps more importantly, we note that some of the election periods in our sample occurred in years when major economic developments – not the elections themselves – had an outsized influence on equity markets. Examples include the Great Depression (1932), World War II (1940 and 1944), the technology bubble (2000), the global financial crisis (2008), and the COVID-19 pandemic (2020).

How has the S&P 500 Index Performed Under Each Presidential Party?

The chart below shows the historical level of the S&P 500 price index under every U.S. President by their political party since 1932. The blue shaded areas represent periods when the Democrats were in the White House while the red shaded areas are times when Republicans held the office. As you can see, the chart highlights that the stock market has historically performed relatively well across both political parties.



Source: Standard & Poor's

What other Factors – Beyond the Presidency – Impact Market Returns?

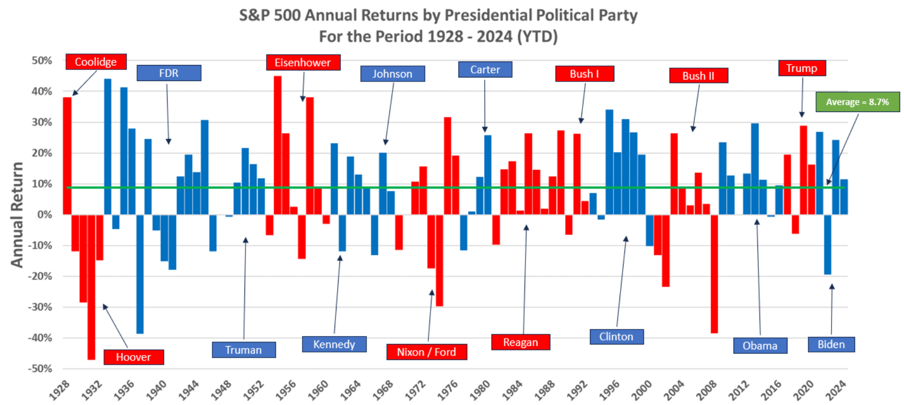
For most long-term investors, it makes more sense to focus more on fundamentals, such as those related to the business cycle, rather than day-to-day election coverage. On a short-term basis, election headlines have the power to move markets and create stock market volatility. However, these short-term moves are eclipsed by the long-term gains created by market and business cycles.

The business cycle, which refers to the fluctuations in economic activity that an economy experiences over a period of time, is considered to have a more far greater impact on the economy than the individual who occupies the White House for several reasons.

First, the business cycle is driven by fundamental economic factors such as consumer spending, business investment, government spending, and global trade. These factors tend to have a more direct and powerful impact on the economy than the policies of any single administration.

Second, economic trends often span multiple presidential terms, and the effects of policies can take years to manifest. This means that the current state of the economy is often the result of actions taken by previous administrations, not just the current one.

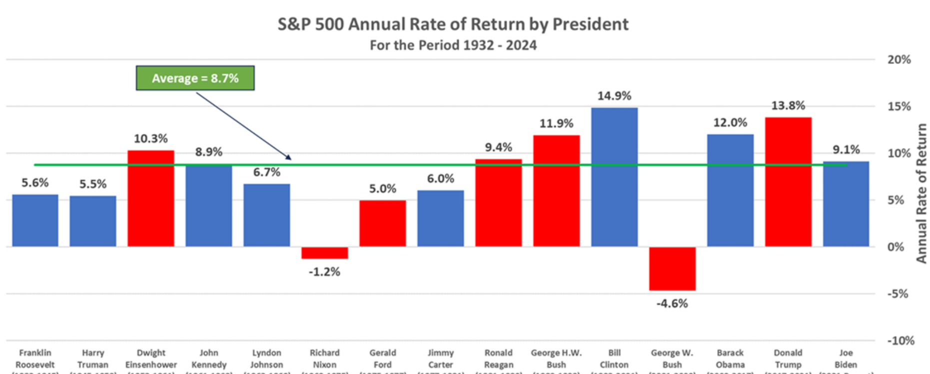
Third, the U.S. economy is deeply integrated into the global market. Geopolitical events, trade relationships, and economic conditions abroad can have a significant impact on the domestic economy, regardless of U.S. political leadership. These relationships are illustrated by the chart below which shows the annual returns of the S&P 500 Index by President and political party.



Source: Bloomberg

To further illustrate this point let's consider the broader market performance during the 1990s and early 2000s. Recall that Bill Clinton's two terms in office were perfectly timed with the information technology boom while the ensuing dot -com bust coincided with the start of the George W. Bush presidency. Unfortunately, the 2008 financial crisis also occurred at the tail end of George W. Bush's second term, resulting in his presidency encompassing both market crashes. As a result, during President Clinton's time in office the S&P 500 Index generated an impressive average annual rate of return of 14.9%,while the average annual return during George W. Bush's presidency was a decline of 4.6%.

However, it would be a stretch to argue that their presidencies were the reason for these booms and busts. Instead, while policies may of had some influence on these events, market performance had much more to do with technological innovations and other financial factors. Consequently, these and other historical episodes suggest that presidents often receive too much blame and credit for economic conditions.



Source: Bloomberg
2024 YTD returns through 5/21/2024

Furthermore, the Federal Reserve, which is independent of the executive branch, plays a crucial role in managing the economy through monetary policy. Its decisions on interest rates and money supply can have immediate and significant effects on economic conditions.

Lastly, market forces such as supply and demand, technological innovation, and demographic changes are powerful drivers of economic activity that operate independently of political leadership. While political decisions can influence the economy, they often do so within the context of the broader business cycle.

What Lessons Can We Take Away from the Data?

Historical data suggest that overly focusing on the political leadership rather than on fundamentals might be imprudent for several reasons. First, the stock market is influenced by a myriad of factors – such as macroeconomic data, corporate earnings, geopolitical events, and investor sentiment. While political decisions and fiscal policies can have an impact, they are just one piece of a much larger puzzle.

Second, political administrations are transient, typically lasting four to eight years, whereas economic cycles and market trends can span decades. Consequently, we believe that disciplined, long-term investors tend to benefit more from understanding these enduring trends rather than from over reacting to shorter-term political changes.

Additionally, political actions and their impacts on the market can be unpredictable and are often already priced into the market by the time they occur. In contrast, market fundamentals – such as revenue and earnings growth, valuation levels, interest rates, unemployment rates, and inflation – are more objective measures that can be tracked and analyzed to potentially make informed investment decisions.

Also keep in mind that a well-diversified portfolio is already designed to withstand a variety of market conditions, including changes in political leadership! As such, overreliance on political speculation could lead to concentrated portfolio risks that might result in missed market opportunities.

So, while it's important to be aware of how political developments can affect the markets, we believe that maintaining a disciplined investment approach that prioritizes bottom-up, fundamental research coupled with top-down, macroeconomic analysis is likely to be a more reliable method in helping to achieve long-term financial goals.

Of course, policies on taxes, trade, industrial activity, antitrust, and more can have important impacts on specific industries which can then affect the broader economy. However, not only do policy changes tend to be incremental, but history shows that it is very difficult to predict how any particular policy might affect the economy and markets, despite conventional wisdom about each party.

When it comes down to it, we believe that successful, long-term investors should be wary of claims that one candidate or another will "kill the market" or "ruin the economy" and instead take the opportunity to vote at the ballot box and not with their hard-earned savings.

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The MSCI EAFE Index is a free float –adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S. and Canada.

The MSCI EM (Emerging Markets) Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of the emerging market countries of the Americas, Europe, the Middle East, Africa and Asia.

The S&P 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing the major sectors of the U.S. economy.

The Bloomberg Barclays U.S. Aggregate Bond Index is an index of the U.S. investment grade fixed-rate bond market, including both government and corporate bonds.

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