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WEALTH MANAGEMENT

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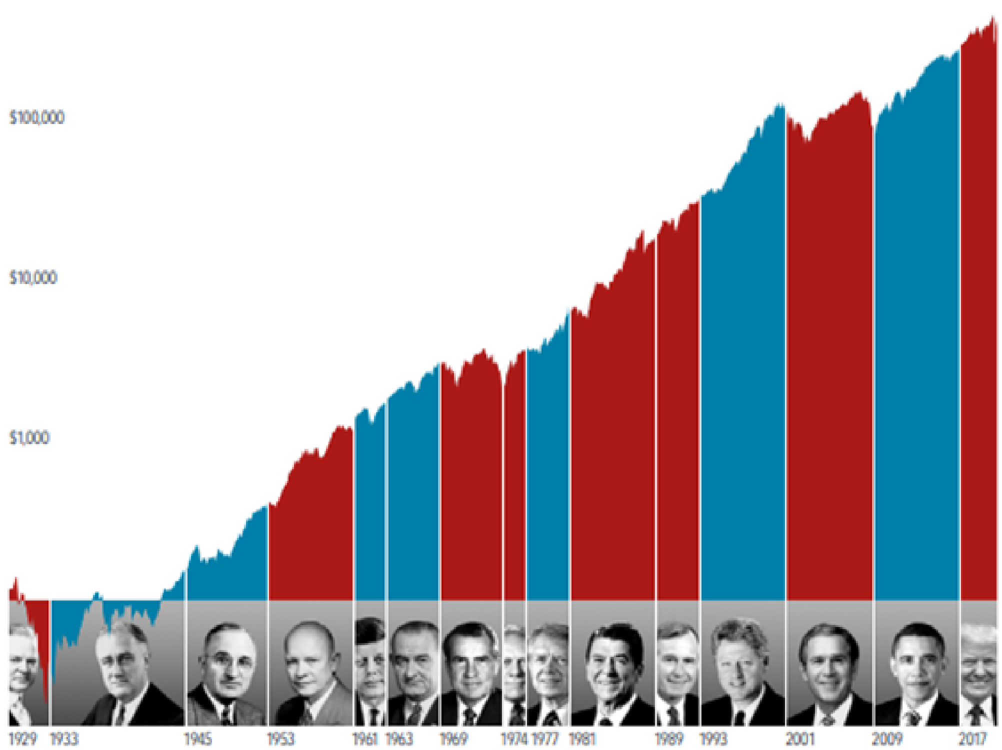
Monthly Insight

Election Years and Your Portfolio: Focusing on What Is Most Important

As these words are being written, we still don't know who the next President of the United States will be. Outcomes in several states remain too close to call, and both candidates are within striking distance of sufficient electoral votes to win the presidency. As with many events during this tumultuous year, we are in uncharted territory.

But even in this environment, there are some important facts to keep in mind as you think about your investments and how they might fare under a Democrat or a Republican presidency. Let's take a step back from the minute-by-minute coverage of the various vote counting operations in the undecided states and remember a few key principles that history teaches us.

First, the financial markets do not hate or love either party. In fact, over the past ninety years, the stock markets have trended steadily upward—with intermittent drops in pricing—during both GOP and Democrat administrations. The following chart—which I have used recently in an article on a related topic—does a very good job of illustrating the relative indifference of the stock market to whether the president is a Democrat or a Republican:



Source: Dimensional Fund Advisors, "Growth of $100: Fama/French Total US Market Research Index, March 4, 1929–June 30, 2020." Past performance is no guarantee of future results.

In fact, no matter which way it goes in the race for the White House, the stock market is likely to continue trending upward over time.

Next, we need to recall that the main thing the stock markets do hate is uncertainty. But what is interesting about our current situation with a still-undecided election is how confident the markets seem to be in the face of it. From the day before the election until today, as the votes are still being counted, the S&P 500 is up 200 points, or about 6%. It seems possible that the market perceives that, despite the unusual circumstances, the election is proceeding in an orderly way, without massive political unrest or social upheaval. Thus, even though the outcome of the election is still up in the air, our political system seems to be proceeding methodically and according to plan. At present, the markets appear to be rewarding that state of affairs.

All that said, from a historical standpoint, the markets tend to exhibit better returns when an incumbent is re-elected. The average return during all election years from 1928 to 2019 is 11.3%. During years when the incumbent was defeated, the average return was 9.3%, but in years when the incumbent was re-elected, the average return rose to 13.4%. This is likely because of what I mentioned earlier: the stock market dislikes uncertainty. The policies and leadership trajectory of an incumbent are known; those of the challenger are unknown. Nevertheless, over time, these differences tend to even out. After all, when the challengers win, they become the incumbent; the pendulum of certainty will tend to swing back in the other direction.

Third, keep in mind that the president, whoever he or she is, does not singlehandedly control the economy, taxation, or other important matters that can have a direct effect on your portfolio. In the current year, it appears likely that at least one chamber of Congress will remain largely in the control of a different party than whoever is sworn into office next January. The balance of power among the branches of our government is one of the great strengths of this nation—and it also insulates your portfolio from the whims of any single individual, even the president.

Fourth, everyone should remember to take the headlines with a grain of salt. A look back at the 2016 election is instructive. If your computer is handy, do a Google search on the phrase “2016 Trump win and stock market.” You will see predictions of an immediate plunge in stock prices, accompanied in some scenarios by the onset of a recession. But if you think back to what actually happened, such dire predictions did not come to pass. In fact, the day after President Trump’s victory, the Dow rose 257 points, nearing its record highs at the time. The fact is, equity markets are supremely complicated and affected by a myriad of factors, with the occupant of the White House being only a single data point—and one that is not strongly correlated historically with stock market performance.

Finally, and not only in an election year but all the time, investors should remember to focus on what they can control. Once you’ve exercised your right to vote for the candidate of your choice, you have no further control over the outcome of this or any other election. You have only limited control over the policies or laws that will be supported or enacted by your public officials. You have no control whatsoever over the daily price movements of the financial markets.

But you do have control over several very important factors. You can control the amount of diversification in your portfolio, which is the best protection against market volatility. You can control the rebalancing among asset classes in your portfolio, to ensure that your investments remain in the correct proportions that match your risk tolerance. And you can control your commitment to a long-term financial and investment strategy that is geared to your specific goals and stage in life. You can also control your reaction to news headlines, the claims and counterclaims of competing politicians, and predictions that may or may not come to pass.

History and financial science tell us that investors who remain patient, well diversified, and committed to a long-term strategy will do well over time, in most circumstances. Those same characteristics hold true during election years.

During uncertain times, it is also immensely helpful to have the guidance of a professional, fiduciary financial advisor. We provide reliable, evidence-based advice to our clients that helps keep them on track for reaching their most important financial goals. If you're questioning what the future might hold for your investments and are interested in a "second opinion" on your current portfolio allocation, click here to schedule a complimentary consultation.*

In the meantime...

Stay Diversified, Stay YOUR Course!

*Investable assets in excess of one million dollars.

KIMBERLY FOSS

President, CFP®, CPWA®, CFT-I™ Candidate

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