Building Wealth_ Your Money & The 4 Year Election Cycle

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SPEAKERS

Keith

K Keith 00:00

We are pleased to provide this text from our podcast. As you know, the spoken word is often less formal and sometimes less precise than a written piece that may be carefully edited. I have also been known to sometimes jumble my words beyond recognition! Please let us know if you have any questions or concerns -- and thank you for supporting the show! â€“ Keith DeGreen

K Keith 00:07

Welcome to this third installment in our building wealth series. I'm Keith DeGreen. And this is As I SEA It, hey, and be sure to catch all our great as I sea it podcasts and special features at DeGreen.com. Now, here's an important question. What should you as an investor expect in each year of our country's four year election cycle? This question seems especially appropriate as the political season heats up heading into 2024. Obviously, that's a presidential election year. Did you know that each of the four years in the US election cycle present very distinct market characteristics? Now, politics alone does not drive markets not by a longshot. In fact, political outcomes are rarely the primary factor impacting markets. On any given day, month or year. There are just too many other elements of play, such as reported profits, changes in management, consumer behavior, mergers and acquisitions, new technology to just name a few. But yes, political seasonality throughout each of the four years in our election cycle does provide the backdrop against which more direct market factors occur. And that backdrop can impact how investors perceive and respond to those other factors. So there are certain helpful historical trends. Now, as always, I must issue a disclaimer. As you know, future performance is never guaranteed and past performance does not assure future results. And yes, the year to year performance variations that comprise the averages we're going to be discussing can be pretty extreme. You know, as we discussed in episode two of our building wealth series, long term investors who allocate into properly diversified portfolios suitable to their public their personal objectives, are far more likely to experience success than short term stock traders.

Historical Performance averages based on external factors such as politics can help you set expectations, but should not be the primary drivers of your investment decisions. Now, today, I'm going to borrow heavily from three sources. First, my own decades of experience as an investment advisor. Second, from a great research piece published recently by the people at Argus research, and third, from a website called slick charts, very convenient place to look up market numbers. Here's something to think about in a presidential election year. There are really only three possible political outcomes in a presidential election year. First, there can be a sweep of the House, the Senate and the presidency by one party, call that a clean sweep. Or second, we have a president of one party, while both chambers of Congress are controlled by the other party. That's a formula for legislative gridlock. Or third, we wind up with a president whose party controls one chamber of Congress, a two out of three when, if you will. Now, of course, geopolitics and domestic issues vary widely from one cycle to the next, I give you just two examples of how things can change. You might remember this in the 2012 presidential debates, President Obama ridiculed Mitt Romney for saying that Russia posed a threat to peace. It's not so funny now. Meanwhile, this would be the first year since the 1973 Roe v. Wade decision that abortion has again become a political question. And as Congressman Jack Kemp said years ago, it's the economy stupid. Indeed, the economy is always a major, if not the major issue, especially in presidential election years. But regardless of the hot button issues in any year markets, markets and certain sectors do tend to respond in certain ways, depending on which of these three outcomes occur. Now, again, with the caveat that the numbers can deviate significantly in any given year, that the numbers we are using are backward looking. And that past performance is never a guarantee of future results. Let's take a look down at the historical trends. Now. Obviously, we have a four year political cycle, right. So right now in the fall of 2023, we are ending year three of our four year cycle, we count inauguration Your as your one. The midterm election year is your to the year after midterms is your three. That's what we're in now. And the presidential election year is your for. Now please keep in mind so that you don't get confused. When I start throwing numbers at you what these dates are. Now we'll use the s&p 500 stock index as our Bellwether measuring stick, we'll examine its average historical total return by election cycle year, going back to 1988. Now it should be 1980, including 1980 and 2023. That's 44 years, each year over that four year cycle has occurred 11 times since 1980. Again, with 2023 being an incomplete year so far. Also, we'll count how many positive or negative years have occurred over that 43 year period or 44 year period in each year of the election cycle. We'll use total return for our numbers. Now total return includes capital appreciation or loss plus dividends. Okay, you're ready. Here we go. First, let's look at year one, are our next year one will be 2025 as a newly elected or reelected president takes office. Now year one is often a honeymoon year when citizens and businesses begin with optimism that the new administration can improve the economic environment. I'm not so sure that's going to be the case in 2025 If Mr. Biden wins, but nevertheless, historically, that's been the case since 1980. These year one honeymoon years have produced an average annual 18.6% total return. That's a lot. Only two of the 11 years have been negative and nine have posted positive total returns. Now year one might be a honeymoon year but political agendas rarely pan out as expected. And by year two voters tend to express their disappointment in midterm elections that punish the president's party. Our next year or two will be 2026. Now since 1980, midterm years have only produced an average total return of 6.1%. Less than a third of first years in the cycle. There have been four negative and seven positive year twos since 1980. Now, in the third year of the presidential cycle, what we're in right now 2023 Things do get interesting. The White House in Congress are frequently at odds, agenda stall and bills do not get passed. While this makes for frustrating politics and vendors love gridlock. Therefore, year three, the gridlock years like honeymoon years have produced excellent average returns. Specifically, the average year three annual total return since 1980 has been 18.5%. And guess what? Year threes have never posted a negative s&p Return since 1980.

That's incredible. Now, for example, as I mentioned, 2023 is a gridlock year, and through September sixth, we've seen the s&p 500 index produced a total return of about 17.6%. Now, incidentally, August and September tend to be the weakest month in our markets. So if history holds 2023 has a real shot at finishing above the historical average as we head into the fourth quarter. However, I should also point out that interest rates remain high that the Fed might raise those rates further before the end of the year. And that valuations across the s&p are somewhat above historical norms. So in 2023, we might wind up like the optimist who fell off the top of a tall building on the way down, you could hear him shout, I'm okay so far. Well, we'll see what happens in q4. Now, I

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Keith 09:27

would make one other point about 2023. It is definitely a recovery or catch up here, because the s&p lost 22% of its value in 2022. Even now in early September, the s&p has still not recovered. It's January 2022. Highs. Hmm, well finally the fourth year, which includes the actual presidential election, is the second weakest market year in the cycle, finishing just ahead of those midterm year two Lose we discussed year for s&p total returns have averaged 8.8%. However, not horrible, and they've produced only two negative years out of 11. But I have a prediction here. I think the Fed might not begin to lower rates until around mid 2024, just in time to spark a market rally going into the November election. Yes, I know. I'm cynical. And here is one more interesting tidbit. In the 44 years from 1980, into the fall of 2023, the s&p has produced an annual loss only a times only 18% of the time. In other words, throughout the political cycle from 1980 s&p 500 investors made money 82% of the time. Now that I mentioned the value of being a long term investor, I think these numbers do prove my point. But wait, there's more. Do you remember those three possible election outcomes, either a clean sweep that's three for three, the House, the Senate and the presidency for one party, or two out of three a two out of three Victory, with one park party capturing the presidency and one chamber of commerce and finally, the lonely President scenario where one party party occupies the White House while the other party controls Congress. Now let's take a look at what happens based on those three presidential election year outcomes. When the GOP sweeps the market does best in a perceived business friendly environment. Based on election since 1980. The average annualized gain following a GOP sweep is 11.9%. When the Democrats sweep, the annualized return is 8%. The gridlock scenarios are different, though, but they still favor the GOP. When Republicans win control of two of the three positions. That's the presidency or the House and Senate. The subsequent annualized return is 10.7%. When Democrats win two of the three, the annualized return is much lower at 6.1%. But here's something you might not expect. When a Republican is elected president in either a suite or a divided election, the annualized return is 7.5%. But when a Democrat is elected president under either scenario, the annualized return is a better 9.9%. Go figure. Now 2024 will be an election year, obviously, the fourth year of the political cycle, again, s&p year for average annual returns from 19 ad had been 8.8%, with only two down years since then. Now the modest 8.8% average year for return is a great example of how just one really bad or really good year can really skew results. If you subtract out 2008. And it's 37% loss, you wind up with an average year for s&p Total Return since 1980 of 13.4%. The 2008 financial crisis was a multigenerational event, the worst since the Great Depression. Now, while politicians have a nearly infinite capacity to screw things up, I think it's reasonable to believe that we will not see another such quiet crisis for quite some time. I say this, even as I worry about our national debt. And in that regard, you might want to catch my two part series on what I call the financial responsibility amendments at the green.com. Now, you can find it right here, as I say at the green.com along with a whole bunch of other cool stuff. So what can we take from all this information about election cycles? Well, for the longer term investor, the trend investor, the trend really is your friend, based on history, with the future never guaranteed, of course, you have an 82% historical chance of making money in the s&p in any given year. But you ask, what are my historical odds in each of the four election cycle years? Hmm, well, I'm glad you asked based solely on history, and certainly with no guarantee of performance, and remembering that we are focused entirely on the performance of just the s&p 500 index because there's a lot more, a lot of other more volatile indices out there. Here your odds based on history of you We're making money in the first year of the election cycle 82% with an historical return of 18.6%. That's your odds of making money in the first year, in the second year of the election cycle, you have a 64% possibility of with an average of making money with as historically speaking, with the average historical return of 6.1%. In the third year of the election cycle, guess what your chances of making money based on history 100%, they've never had a down year in the third year, with an average historical return of 18.5%. And the fourth year of the election cycle, also 82% with an average historical return of 8.8%. Now one final note on your strategy based on these long term averages, you might be tempted to say go to cash in the second year of a presidential cycle, where your chances of success have only been about 64%. And where the average total return in the s&p has been only 6.1%. Now, for a variety of reasons, and I say this as a reformed investment advisor and as a certified financial planner. I don't recommend this, but if you do go to cash, be sure to carefully consider the tax consequences of such a move. That negative tax consequence of selling might easily outweigh the risk of sticking things out. Now, different industries or sectors may be impacted in different ways depending on election results. So let's briefly look forward rather than back at four important sectors, financials, healthcare, energy and information technology. Let's go first to Financials. If the GOP wins outright, or commands a two to one majority over the presidency, the House and the Senate, more relaxed financial regulations might be expected. I'm not sure that's true. If they don't win the presidency. They gotta take the presidency and one other house. Now that may not be a slam dunk, but a Republican majority usually bodes well for bank and financial stocks. Also a pro business Washington under Republican control could create a positive backdrop for financial services consolidation. There are more than 4800 banks and about 3400 broker dealers in the United States. Many are ripe for a merger or acquisition. Now in the banking sector in particular, I like access to regional banks through a couple of ETFs. I'm not recommending them necessarily, but I find them useful. ticker Kre. Or I at that's KR e r i a team for regional banks. Now finally, while the Republicans have certainly not distinguished themselves lately, with respect to financial responsibility, a clear win for the GOP could have implications for US debt levels, and policy regarding deficit spending. Now the deficits spike due to pandemic stimulus spending, with presumably no more pandemic stimulus stimulus on the horizon. And of course, we've got the IRA Act, which is the green boondoggle that I talked about in a

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Keith 18:27

in a recent climate crazies versus common sense podcast. Despite all that, I would hope that the GOP would want to gets serious about deficit reduction. On the other hand, with Republicans in control, we might finally be able to allocate more into national defense. Now, if the Democrats win, and particularly if they win outright, corporate tax rates could go back up. This would compress profit margins across all publicly traded companies and subdue the market. While inflating prices. You know, ultimately, corporations don't pay taxes, they collect taxes, and must pass that expense on to their customers, if they hope to earn a reasonable rate of return on their shareholders investments. Still, the Dems would try to sell this as a way of reducing the deficit. In my opinion, however, higher taxes only slow the economy, ultimately producing less tax revenue than the government could receive with a more robust economic growth rate. You know, we would also see a continuation of the stifling regulatory mandates we see today if the Democrats retain the White House, especially because they're ruling right now through executive fiat and would also keep the economy from operating at its full potential. A less robust economy reduces lending and obviously slows the financial sector in many ways. Now let's look at healthcare, the Affordable Care Act or Obamacare or the ACA, whatever you want to call it has so far survived three supreme court challenges. Still, the court has made clear that it finds legislative and regulatory overreach, unconstitutional. So we might still have some serious ACA, ACA core challenges, regardless which party dominates next year, if the Democrats when they might seek to strengthen the A E, ACA and further why Medicare availability, but this would likely require a democratic sweep on election day. Now, meanwhile, the Democrats could potentially stiffen controls on drug pricing. Let me say something about this. This provides a disk disincentive duck fixing drug prices provides a disincentive to innovate by big pharma. It's my opinion. I think it's a terrible idea. Drug companies need the ability to price their own drugs during the relatively brief time period, that they are patent protected. Now, that's how they've been able to recoup the massive costs of developing and testing not only successful drugs, but also the countless drugs that never make it to market. They simply must make a profit sufficient to provide an incentive to keep pursuing new innovations. Now, if government health care programs demand lower prices, drug companies will charge private insurance companies and consumers more, they must make up the difference somewhere if they're to stay in business. Now, in broad terms, patent Patents protect the right to establish market based pricing under a pattern, which is why almost all the major drug breakthroughs have in recent years have come from the United States. European countries use socialized medicine and fixed drug prices. So there's very little incentive for companies over there to risk billions to innovate. We've been doing it for him. Now the Biden administration says it negotiates drug prices Oh, that's ball. There is no negotiation involved because drug makers must have their drugs approved for use in Medicare and Medicaid, the largest insurance market that there is. So from the government's point of view, it is my way or the highway that is not negotiated. Now, let's examine both the energy and so called clean energy sectors. If the GOP wins, a top priority may be priority number one, would likely be to scale back or eliminate programs that subsidize boondoggle green energy programs and companies. As I mentioned a moment ago, I address just how bizarre and otherworldly this problem has become. In my recent podcast, climate crazies versus common sense. I hope you listen in@degreen.com. But beware, the green boondoggle lobby has become a powerful force in Washington. So the Republicans could cave or at least will face an uphill fight. And of course, they'll be accused of wanting to commit suicide by destroying the planet. With Republican control, we can certainly anticipate increased domestic oil, natural gas and coal production, that's a good thing. It's also likely that they would try to eliminate the so called windfall profit taxes on domestic oil and gas producers imposed by the Democrats under the paradoxically named inflation Reduction Act. GOP when might also resort resort, a result in the increased mining of critical minerals such as lithium, nickel and cobalt right here at home, which are used in electric vehicle battery production, and none too soon. We rely way too heavily on foreign sources of critical materials, especially on China and on countries in Africa that often allow child labor and horrible working conditions in their minds. Meanwhile, if the Democrats win, regulatory oversight and attacks on oil and gas producers would almost certainly increase. President it's hard to believe that because they've been so pronounced Now, President Biden rejoined the Paris climate accord that President Trump exited. Now compliance with the Accord is likely to require ever more stringent regulation of fossil fuels. So with a Democrat when oil and gas companies would almost certainly come under additional pressure, and efforts to collect more taxes from these companies could increase There could also be attempts to raise fuel efficiency to a higher standard than the 36 mile per gallon, currently targeted for 2026.

The new target is reportedly 49 miles per gallon. Finally, please, I encourage you to go to my commentary on my podcast on climate crazes versus common sense, because none of that works. None of that has helped clean up the environment, none of it. Anyway, Finally, let's look at the elections impact on information technology, the info tech industry. You know, if the GOP wins antitrust efforts could intensify particularly efforts to break up the big social media companies that so arrogantly conspire to block conservative voices. Now, regarding tech workers in 20, set between 2017 to 2020. The GOP increased restrictions on what's called H B one work visas. Now these are used to bring in often highly skilled techies from abroad. These restrictions do protect higher paid American workers, and they have not changed much under the Biden administration. So a victorious GOP is unlikely to loosen those HB one restrictions. Now, if the Democrats win, the tech sector could benefit from the expansion of the chips Act. In other words, more subsidies. And I trust activity could become a low priority, and they would probably favor increased foreign trade. Now that would include not only imports from abroad, but also more exports to other countries.

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I grew up in the Rust Belt outside of Cleveland, Ohio, I watched us factories and entire towns closed down due to so called free trade agreements. So count me skeptical about the impact on American workers. But if the Dems do expand trade, China would would likely remain the lone exception, starting in 2022. To his credit, President Biden has used a series of increasingly restricted bans to deny China what it wants most high tech stuff from cutting edge US companies, I hope they continue that. Now finally, a big Democratic win might result in efforts to treat independent gig workers. Those are often tech workers, as someone's anyone's employees, even though they're independent. This agenda includes arbitrary formulas for more overtime pay, paid maternity leave access to health care and other perks despite the choice of gig workers themselves, to remain independence, to remain able to set their own hours and to be able to establish their own goals. As you might guess, I strongly oppose this agenda. Now, again, I must emphasize that every election especially a presidential election, always involves wildcards that we just cannot reasonably anticipate. This year we already have a couple of doozies doing Biden's creeping age related incompetence and Trump's indictments. Current polls put the two dead even many voters say they wish neither of them would wrong. But unusual business is business as usual in American politics. It always has been so fasten your seat belts and if you are a candidate, wear a cup. The political season is upon us but then again, it never really ends. Thanks for joining me today. I am Keith DeGreen. And this is As I SEA It!

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Keith 28:46

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