Getting a Jump on U.S. Election Day 2020

Historically, the U.S. stock market seems to prefer a divided government, but that doesn't necessarily mean it welcomes a stalemate.

Featured Contributor

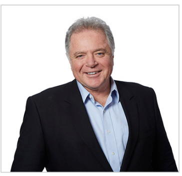

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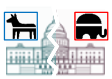
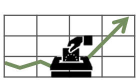
Table 1. Historical Impact of Elections on the S&P 500® Index

Real returns on the index, based on 35 post-WWII U.S. federal government elections





	Period Before Election			Period After Election			
Outcome	12-months	6-months	3-months	3-months	6-months	12-months	# of Cases
Divided Government	**6.4**	**1.1**	**2.6**	**6.3**	**9.3**	**8.7**	**20**
Change in Composition by Party	-1.3	-1.7	0.0	4.3	6.8	8.7	14
Undivided Democrat	-3.6	-3.4	-2.4	3.6	5.6	7.1	11
Undivided Republican	-1.1	-2.1	-2.4	3.2	4.3	9.3	5
Type of Election							
Off-Year Elections	1.3	-1.5	1.1	7.5	13.3	13.3	18
All Presidential Elections	3.2	0.1	-0.4	2.6	1.7	3.3	17
Change of Party Presidential	**-1.3**	**-1.7**	**-3.4**	**1.4**	**0.4**	**-0.7**	**9**
Close Presidential Elections*	2.1	-0.4	-0.6	3.2	1.6	-0.9	6
All Elections	**2.3**	**-0.7**	**0.4**	**5.0**	**7.5**	**8.3**	**35**

Average of All Periods	12-months = 5.2	6-months = 2.6	3-months = 1.3

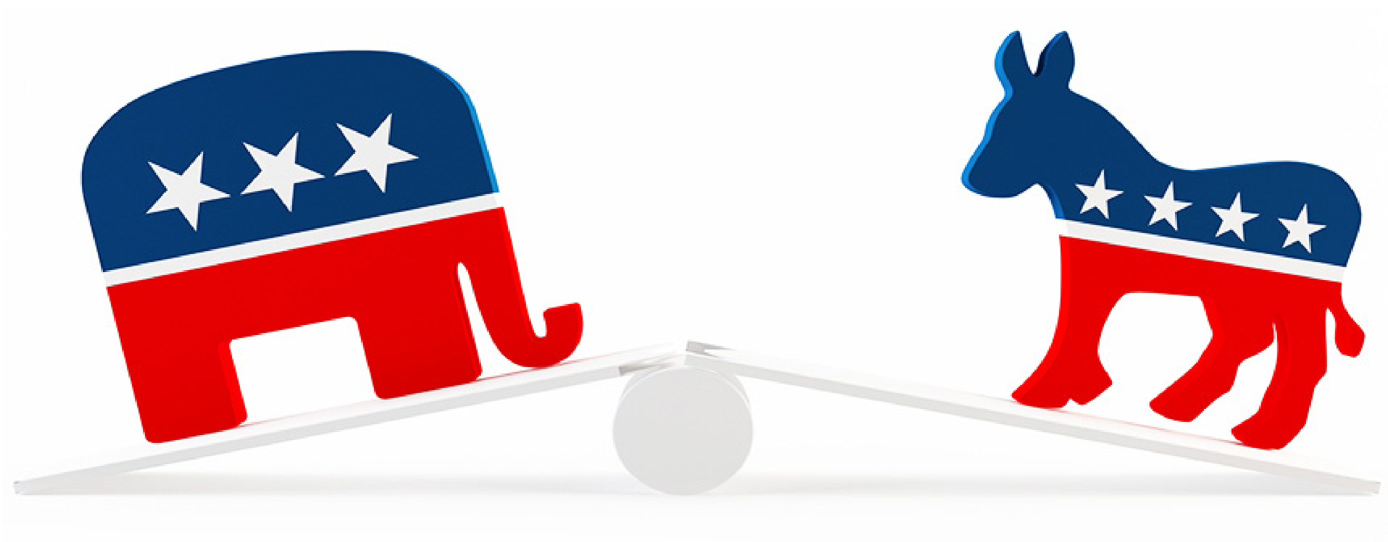
*1960, 1968, 1976, 2000, 2008, and 2016.
Source: uselectionatlas.org. and Lord Abbett. Returns are as adjusted for inflation.

■ Highest and ■ lowest returns during pre-and post-election periods.

We wish we had a crystal ball and could answer the many questions we have been receiving on the potential market impact of the U.S. presidential election on November 3, 2020. As the date draws nearer, and candidates and their positions are better known, we will, from time to time, provide perspective on the policies that are likely to affect the sectors and asset classes that are part of our investment strategies. Times of political transition typically offer both risks and opportunities in our business.

Until then, only history can be our guide (and one thing we know for certain is that past performance does not guarantee future results!) Table 1 looks at the political demographics of 35 post-World War II U.S. federal government elections and their impact on the broad U.S. stock market, as represented by the S&P 500® Index.

Although we make seven observations on the historical results, we offer an important caveat: *We would not predict anything based on this history* because none of the data control for any of the fundamentals that actually drive returns, such as earnings expectations and surprises, inflation expectations and surprises, yield changes, and other factors.



Seven Observations

1) The U.S. stock market has tended to outperform after elections. This is in comparison with both the period before the election and the long-term average.
2) This post-election outperformance followed off-year elections. Comparatively, the market has underperformed after presidential elections.
3) The underperformance after presidential elections may be due to the fact that five out of 17 (29%) cases were associated with recessions (1948, 1952, 1980, 2000, 2008). Three out of 17 presidential elections had recessions in the preceding year (1960, 1980, 2008).
4) The market has underperformed long-term average returns in periods of comparable length before elections.
5) Elections that resulted in divided government—at least one out of three of the president, Senate, and House are in the hands of one party and the other two are in the hands of the other—had the best returns both before and after.
6) Elections that resulted in a change in composition by party, undivided Republican, or undivided Democratic control tended to be preceded by underperformance.
7) Elections that resulted in undivided Republican control have tended to be followed by underperformance in the three- and six-month periods immediately afterwards but have delivered the best average returns in the subsequent 12 months.

Note that the market performed slightly less well before and after elections that resulted in undivided Democratic control (11) than before and after those that have resulted in undivided Republican control (5).

However, the number of cases is small for each outcome and there are no fundamental controls applied to the results. So, in our opinion, extrapolating from them can only be done with extremely low confidence.

It's often remarked that the market likes divided government and, based on our Table, that's been true.

But, in our opinion, we shouldn't conclude that the market has outperformed after such elections because it welcomes a stalemate (which is sometimes the result) or relative inaction on the part of our elected officials.

Divided government more often results in compromise—which can be a good thing—on issues such as taxes, federal spending, and infrastructure. As these and other problems seem to be getting larger, we believe the incentive to compromise might be stronger when both sides have a say in how they are resolved.

As we noted earlier, we will be offering periodic commentary and analysis on election-related topics as the U.S. campaign unfolds. We will be keeping a close eye on developments along the way.

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