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September 2024 Crescent Commentary

How will the elections impact your investments?

With elections in the U.S. less than a month away, investors want to know how the outcomes could impact their investments. Whether you own stocks, bonds, or real estate. Public or private. There's no question that economic conditions will impact your investments. But what about the elections themselves? Given the system of checks and balances in our government, how much impact can any given election have? And what impact will the current elections have? In this Commentary, we'll look at a century's worth of data to find answers to these questions.

Let's start with presidents. Since 1926, the U.S. has had nine Republican and eight Democrat presidents. And during that time, with the exception of periodic recessions that do not correlate with political control, the U.S. economy and stock market trended higher regardless of which party held the presidency. And because of the system of checks and balances in our government, even if we did have or do have an incompetent administration, there's only so much impact they can have on our country. And for this reason, we expect what has happened over the past hundred years to continue for the foreseeable future, and that is for our economy to trend upward over time regardless of which political party is in control. The way we look at it is our economy has succeeded over time despite missteps from our politicians. And because of our system of checks and balances, we expect that to continue.[(1)]

Let's get more granular now. We can use the U.S. stock market as an indicator for public and private financial markets and the economy. Which presidents have been the worst and best for the U.S. stock market? Is there any connection with political party? Morningstar ran a study of the best and worst first three years for all presidents since Eisenhower. It turns out that the two best and two worst presidents for the U.S. stock market came from both political parties. The two best presidents for the stock market were Eisenhower and Clinton. The two worst were Nixon and Carter. This set of facts brings up a crucial point regarding presidents, the economy, and financial markets. It shows that rather than political party, what has mattered for financial markets is the economic conditions already set in motion when the president took office.[(2)]

Looking at the two best presidents for the stock market, each of them took office at the beginning of an economic recovery from a recession, and each of them benefited from an enormous boom set in motion before they took office. In the case of Eisenhower, he took office after World War II, when the U.S. economy began an enormous recovery from the Great Depression. Eisenhower also benefited from the baby boom, when soldiers returned from the war. With Clinton, he took office at the beginning of the recovery from the 1991 recession, and he benefited from an economic boom (and bubble) fueled by interest rate cuts by Federal Reserve Chair Alan Greenspan.

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And you can see the exact opposite with the worst presidents for the U.S. stock market. Nixon was president from 1969 to 1974, which was a period of economic bust following an economic boom for the stock market in the 1960s.
Carter took office in 1977, in the middle of a period of double-digit inflation in the U.S. The Federal Reserve raised interest rates to nearly 20% in order to break the inflation. The Fed's inflation fight did work but also caused the U.S. to experience back-to-back recessions. These challenged economic forces were already in play before both of these presidents took office.(2)

Now that we've discussed presidents, what about control of Congress? What we know is that looking at the past 70 years beginning in 1953, U.S. stocks have gone up under all scenarios of congressional control—whether you look at one party in control or split control. This is true when looking at which party held the presidency in conjunction with congressional control. So this takes account of which party held the presidency and which party controlled Congress. The data aren't as clear cut as the president data, because there are only a few data points for some of the scenarios. But the bottom line is stocks have advanced under all scenarios of political control between the president and Congress. Ultimately, this reflects the innate prosperity of America's economic system. Rather than thriving as a result of politics, America has thrived despite its politics.(1)

Now that we've looked at the long-term data, some of you may wonder if you need to fasten your seatbelts over the short term for a bumpy ride during the election month. Well, we have also looked at how stocks have done during an election month, going back nearly a hundred years to 1926. What we've found is that the stock market does not show any consistent patterns when it comes to election months. And the winning party has not been predictive for the direction or amount of market movements during election months. It ultimately gets back to what we talked about earlier with how the economy determines how the stock market does during a presidency.(1)

Looking at a year like 2008 provides a great example. It didn't matter who got elected in 2008, they were dealing with a financial crisis on a scale our nation hadn't seen in 80 years. And it was that crisis, which was a full-blown panic, that drove stock market returns into the end of 2008 and early 2009. It would not have mattered who won the presidency or which party took control of Congress. Either party was going to have to fight a roaring fire. The economy was tanking and politics were not going to change that.

So we can see from all of this election data going back over a hundred years, it's the course that our economy is currently set on which will matter for investment markets over the next few months and next few years. The current economic conditions we would highlight are the data showing the economy has slowed over the past few months, with an increase in the unemployment rate. There are currently 20% more unemployed Americans compared to summer 2023. And the all-important question is whether this is simply a slowdown or whether it leads to a recession over the near term.(3)

Given the uncertainty about the direction our economy is headed in, we continue to recommend balanced and defensive investment allocations. It's fine to own diversified amounts of investments currently perceived as "growth" investments. But it's important to realize that at some point perceptions will change, and those investments that are currently most popular will be vulnerable to a significant correction when perceptions do change. And for that reason, we recommend that investors maintain a high allocation to stable, dividend paying stocks which have a demonstrated track record of doing well no matter what economic conditions come our way.(4)

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Forbes Best-In-State Wealth Management Team 2024

Sources:
(1) Dimensional Funds; (2) Morningstar; (3) CNBC; (4) RBC

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