GW&K
INVESTMENT MANAGEMENT

GLOBAL PERSPECTIVES

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KEEPING YOUR PORTFOLIO ABOVE THE POLITICAL FRAY

HIGHLIGHTS

- It has not been uncommon to see US equity market volatility rise around the time of presidential elections, but investors are well advised to look beyond short-term fluctuations.
- Historical data shows markets have performed well under both Democratic and Republican administrations, challenging the notion that one party is inherently better for investors.
- Attempts to time the market based on political outcomes or make sector-specific bets often backfire, as demonstrated by several recent examples that defied conventional wisdom.

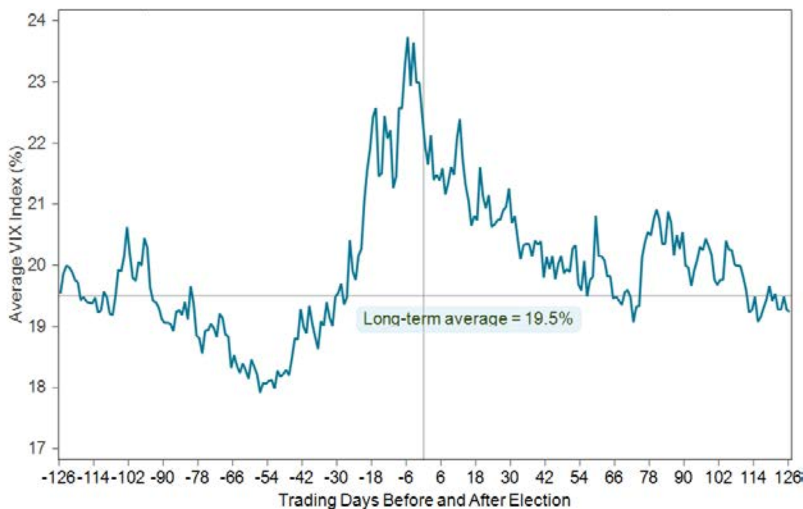
THE VOLATILITY SPIKE: A COMMON PATTERN

As the 2024 US presidential election looms, investors find themselves caught in a familiar tug-of-war between political convictions and financial prudence. The siren song of partisan prognostication grows louder, tempting many to realign their portfolios based on anticipated electoral outcomes. However, a closer examination of historical data and recent market behavior suggests that such moves may be ill-advised.

It's an established trend: market jitters often intensify around elections. The CBOE Volatility Index (VIX), often dubbed "the fear gauge," has tended to spike in the weeks surrounding US presidential elections (**Figure 1**). This year appears to be no exception, with the VIX already having shown signs of pre-election nervousness.

FIGURE 1

Volatility (VIX) 6 Months Before and After Election Day (1992–2020 US Presidential Elections)



Source: GW&K Investment Management and Macrobond

> The VIX Index of US equity volatility — also known as "the fear index" — has historically risen to above-average levels for a few weeks ahead of and following US presidential elections.

But savvy investors would do well to look beyond these short-term fluctuations. Despite the quadrennial uptick in volatility, a broader perspective reveals a more reassuring picture.

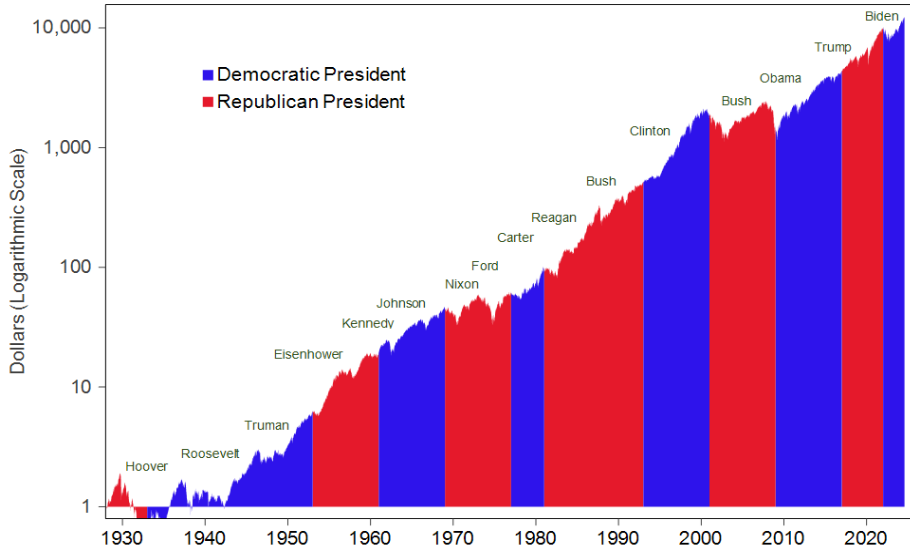
RISING TIDES LIFT ALL PARTIES

Contrary to popular belief, markets have demonstrated a remarkable ability to climb higher regardless of which party occupies the White House. Over the past century, both Democratic and Republican administrations have presided over periods of robust stock market performance. This bipartisan bull run challenges the notion that one party is inherently "better for business" than the other (**Figure 2**).

FIGURE 2

Growth of a Dollar Invested in the S&P 500

January 4, 1928 – July 31, 2024



Sources: GW&K Investment Management, Standard & Poors, and Macrobond

Notwithstanding periods of elevated volatility around presidential elections, the US equity market has rewarded long-term investors under both Democratic and Republican presidents.

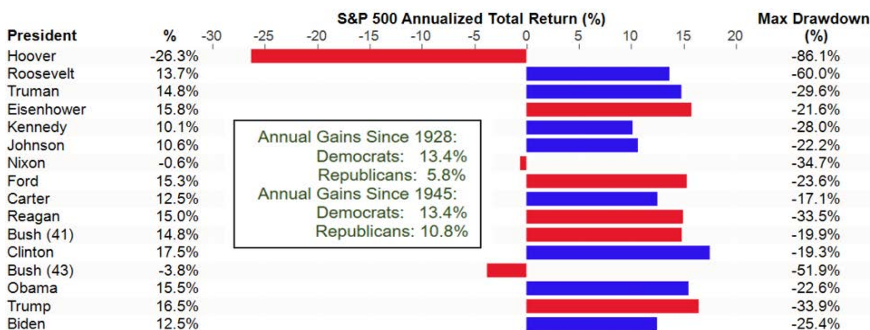
RECESSION FEARS: MORE BARK THAN BITE?

Recent survey data from Nationwide's annual Advisor Authority report paints a stark picture of partisan economic pessimism.[1] Nearly one in three investors believe a recession is imminent if their less-favored party gains power in 2024. Yet, historical evidence suggests such fears are often overblown.

An analysis of presidential terms and corresponding market performance reveals a more nuanced reality. While it's true that most administrations have seen significant market drawdowns — with only three presidents escaping "bear market" territory of 20% or more — the overall trajectory has remained positive across party lines (**Figure 3**).

FIGURE 3

Stock Market Performance Under US Presidents Since 1928



Note: Data from 3/4/1929 through 7/31/2024
Sources: GW&K Investment Management, Standards & Poors, and Macrobond

Regardless of party affiliation, most US presidents have presided over robust stock market performance. That said, all have also seen double-digit drawdowns occur on their watch, with only three escaping "bear market" drawdowns exceeding minus 20%.

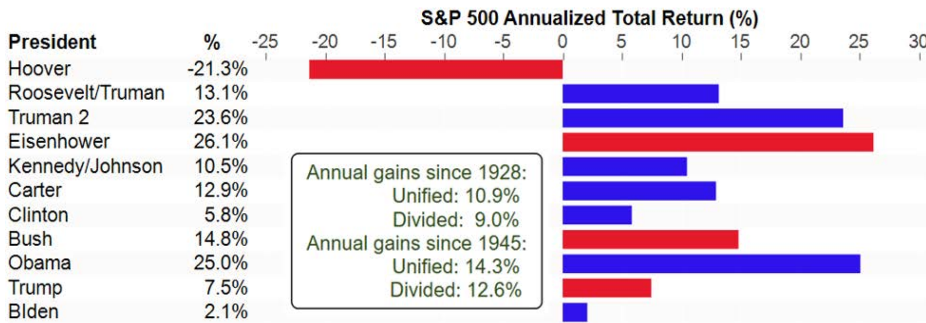
[1] Nationwide Retirement Institute, "Nearly Half of Investors Believe the 2024 Election Will Have a Bigger Impact on Portfolios Than Market Performance, *Advisor Authority Survey,* October 30, 2023.

UNITED WE STAND, DIVIDED WE… STILL GROW?

That's not to say politics are irrelevant to market performance. History indicates that periods of unified government — when one party controls the presidency and both chambers of Congress — have generally produced stronger returns compared to divided governments. However, the differential is not so dramatic as to justify drastic portfolio reallocations based on predicted election outcomes (**Figure 4**).

FIGURE 4

Stock Market Performance Under Unified Goverment Since 1928



Note: Data from 3/4/1929 through 1/2/2023; Covers only portion of the President's term when the President's political party controlled both chambers of Congress.
Sources: GW&K Investment Management, Standards & Poors, and Macrobond

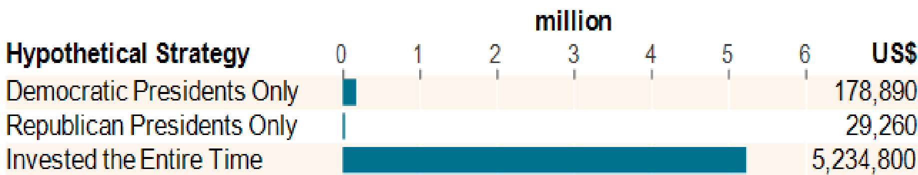
Periods of unified governments have generally produced stronger returns than periods of divided government, but the average performance difference has not been dramatic.

THE PERILS OF PARTISAN TIMING

Indeed, attempts to time the market based on political winds have proven treacherous. A hypothetical investor who only held equities during administrations of their preferred party, switching to cash otherwise, would have dramatically underperformed a simple buy-and-hold strategy over the long term. This performance gap underscores the dangers of letting political biases dictate investment decisions (**Figure 5**).

FIGURE 5

Returns Since Truman's Inauguration (1945): $1,000 Invested in the S&P 500



Note: Hypothetical returns of holding the S&P 500 Index and reinvesting dividends during administrations of a preferred party, or switching to cash otherwise.
Sources: GW&K Investment Management, Bloomberg, and Macrobond

Hypothetical strategies of only holding equities during administrations of a preferred party, switching to cash otherwise, dramatically underperformed a simple buy-and-hold strategy over the long term.

A similar conclusion comes from a National Bureau of Economic Research study on investor behavior following the 2016 US presidential election.[2] The research reveals that investors in Republican-leaning areas increased their equity exposure after the election, while those in Democratic-leaning areas reduced theirs. This divergence, persisting for months, highlights how political beliefs can cloud financial judgment and lead to potentially suboptimal investment decisions.

Perhaps most concerning is the finding that some investors made drastic changes to their portfolios, with a small but significant group altering their equity exposure by 50% or more. Such large swings, likely driven more by political sentiment than by sound financial analysis, underscore the risks of allowing partisan views to dictate investment strategy. As markets generally rose in the months following the election, those who reduced their equity exposure based on political disappointment may have missed out on substantial gains.

SECTOR SURPRISES: WHEN CONVENTIONAL WISDOM FAILS

Even those who correctly predict election results can find their company- or sector-specific bets going awry.[3] Consider three recent examples that defied conventional wisdom:

1. **Apple under Trump:** Despite escalating US-China trade tensions during the Trump administration, shares of heavily China-exposed Apple gained 351%, handily outpacing the S&P's 81% gain over the same period (**Figure 6**).

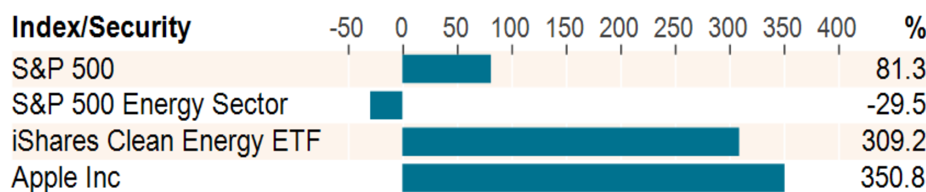
2. **Clean energy under Trump:** Despite Trump being viewed as no friend to the clean energy industry, the iShares Clean Energy ETF soared by 309% during the Trump administration, outpacing the S&P 500 while the traditional S&P 500 Energy sector lost 30%.

3. **Energy under Biden:** Contrary to fears of an anti-fossil fuel agenda, the S&P 500 Energy Sector Index has surged 148% under President Biden, outpacing the tech sector and more than doubling the broader market's 53% return (**Figure 7**). Ironically, the iShares Clean Energy ETF lost half of its value while oil and gas production rose to record highs.

These cases illustrate the perils of making sweeping and "obvious" thematic bets based on perceived political headwinds or tailwinds.

FIGURE 6

Returns Under Donald Trump Presidency
Total Return: 1/19/2017 – 1/19/2021



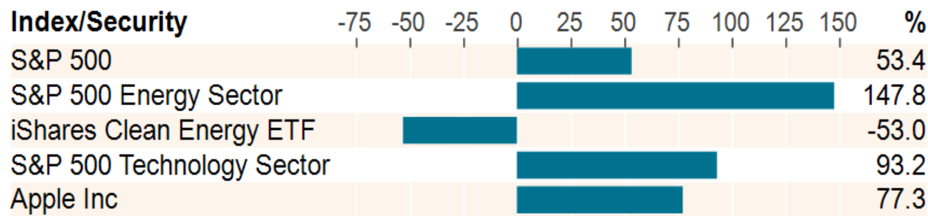
Sources: GW&K Investment Management, Bloomberg, and Macrobond

Contrary to expectations, under Donald Trump's presidency the Energy sector lagged the S&P 500 Index while clean energy stocks soared. Heavily China-exposed Apple also did very well despite rising US-China trade tensions.

[2] Maarten Meeuwis, Jonathan A. Parker, Antoinette Schoar, and Duncan I. Simester, "Belief Disagreement and Portfolio Choice," NBER Working Paper No. 25108, June 2021.
[2] Danny Noonan, "Oil and Water: How to Invest During an Election Year," Morningstar, June 20, 2024.

FIGURE 7

Returns Under Joseph Biden Presidency
Total Return: 1/19/2017 – 7/31/2024



Sources: GW&K Investment Management, Bloomberg, and Macrobond

Also contrary to expectations, under the Joe Biden presidency the Energy sector outpaced the Technology sector and more than doubled the return of the S&P 500 Index. Over the same period, clean energy stocks lost half their value.

MAINTAINING PERSPECTIVE: YOUR PORTFOLIO'S NORTH STAR

As election rhetoric intensifies and market volatility rises, investors would be wise to anchor themselves to time-tested principles rather than political projections. The data consistently shows that maintaining a well-diversified portfolio aligned with your long-term goals and risk tolerance is a far more reliable strategy than attempting to outsmart the market based on electoral outcomes.

While it's natural — and even civically important — to have strong political convictions, the voting booth and investment account serve different purposes. By keeping your investment strategy above the political fray, you position yourself to navigate market cycles and capitalize on long-term growth, regardless of which party claims victory in November.

In the grand sweep of market history, presidential terms are mere chapters in a much longer story of economic progress and innovation. Successful investors are those who remain focused on this broader narrative, resisting the temptation to rewrite their financial plans with every electoral plot twist.

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