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Great-West Capital Management, LLC (GWCM) Research Note

Don't let the presidential election alter your long-term investment strategy

As we approach the three-year mark of President Barack Obama's second term in office, it is again time for the nation to focus its attention on who will occupy the Oval Office next. Democratic and Republican primary debates are already underway in anticipation of the primary elections that are scheduled to begin in early 2016. News coverage ahead of the 2016 presidential election is already heavy, and amidst all of the hype, investors may be wondering what the election could mean for their portfolios. To address this investor curiosity, we examined the U.S. stock market's behavior through various lenses as it relates to presidential elections and political parties in office. While the data produces some interesting outcomes, we remind investors that correlation does not always imply causation, and we believe that investors should continue to stick to their long-term investment strategy through the upcoming election.

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Stock market performance during election years

Annual Returns of U.S. Large-cap Stocks

ELECTION YEARS		POST-ELECTION YEARS		MIDTERM YEARS		PRE-ELECTION YEARS	
2012	16%	2013	32%	2014	14%	2015	1%
2008	-37%	2009	26%	2010	15%	2011	2%
2004	11%	2005	5%	2006	16%	2007	5%
2000	-9%	2001	-12%	2002	-22%	2003	29%
1996	23%	1997	33%	1998	29%	1999	21%
1992	8%	1993	10%	1994	1%	1995	38%
1988	17%	1989	32%	1990	-3%	1991	30%
1984	6%	1985	32%	1986	19%	1987	5%
1980	33%	1981	-5%	1982	22%	1983	23%
1976	24%	1977	-7%	1978	7%	1979	19%
1972	19%	1973	-15%	1974	-26%	1975	37%
1968	11%	1969	-9%	1970	4%	1971	14%
1964	16%	1965	12%	1966	-10%	1967	24%
1960	0%	1961	27%	1962	-9%	1963	23%
1956	7%	1957	-11%	1958	43%	1959	12%
1952	18%	1953	-1%	1954	53%	1955	32%
1948	6%	1949	19%	1950	32%	1951	24%
1944	20%	1945	36%	1946	-8%	1947	6%
1940	-10%	1941	-12%	1942	20%	1943	26%
1936	34%	1937	-35%	1938	31%	1939	0%
1932	-8%	1933	54%	1934	-1%	1935	48%
1928	44%	1929	-8%	1930	-25%	1931	-43%
Average Return	11%	Average Return	9%	Average Return	9%	Average Return	17%
# of Down Years	4	# of Down Years	10	# of Down Years	8	# of Down Years	2

Source: Morningstar® Direct℠; GWCM analysis. Returns are shown for the IA SBBI US Large Stock Ext Index. *Past performance is no guarantee of future results.*

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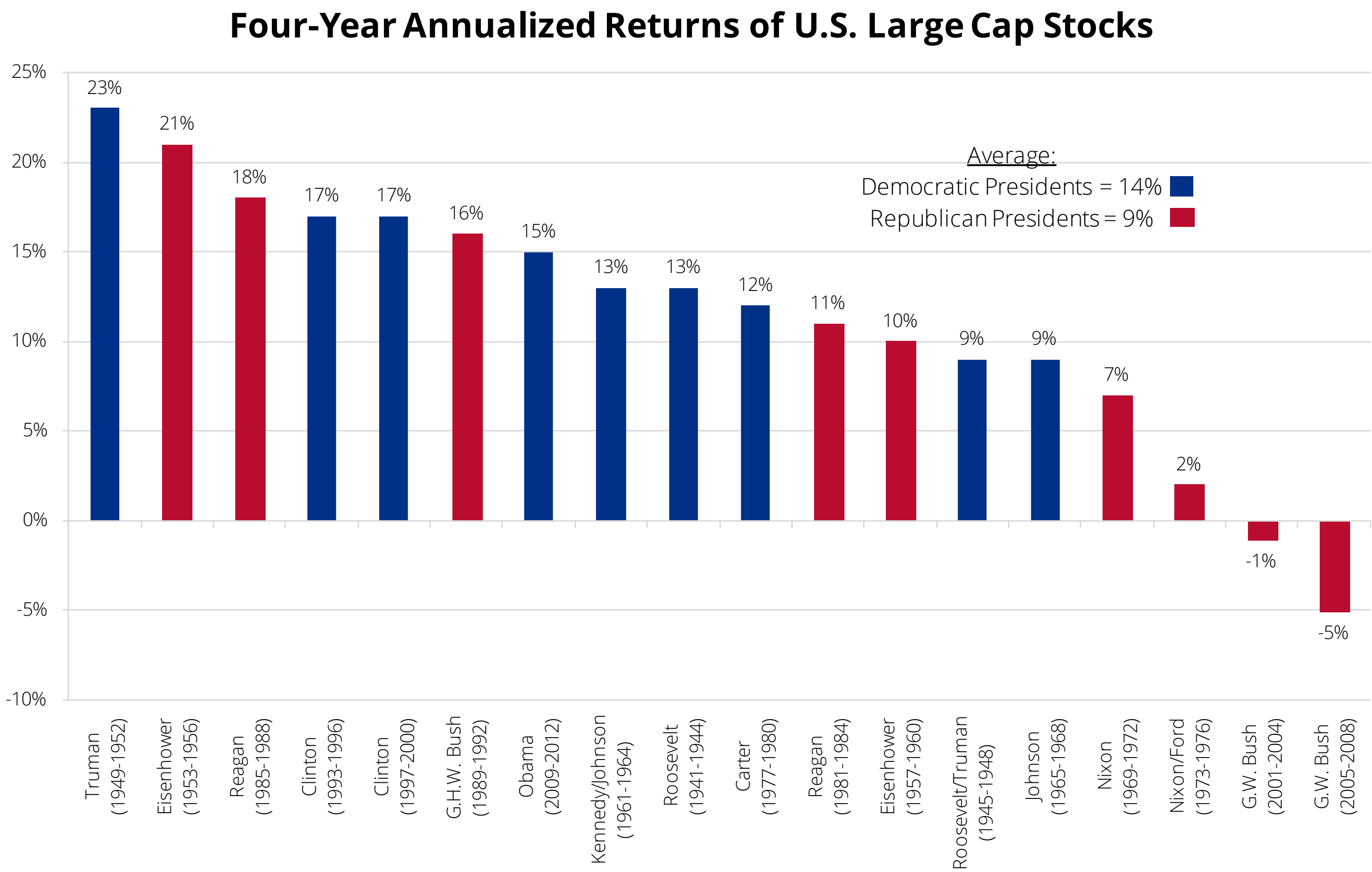
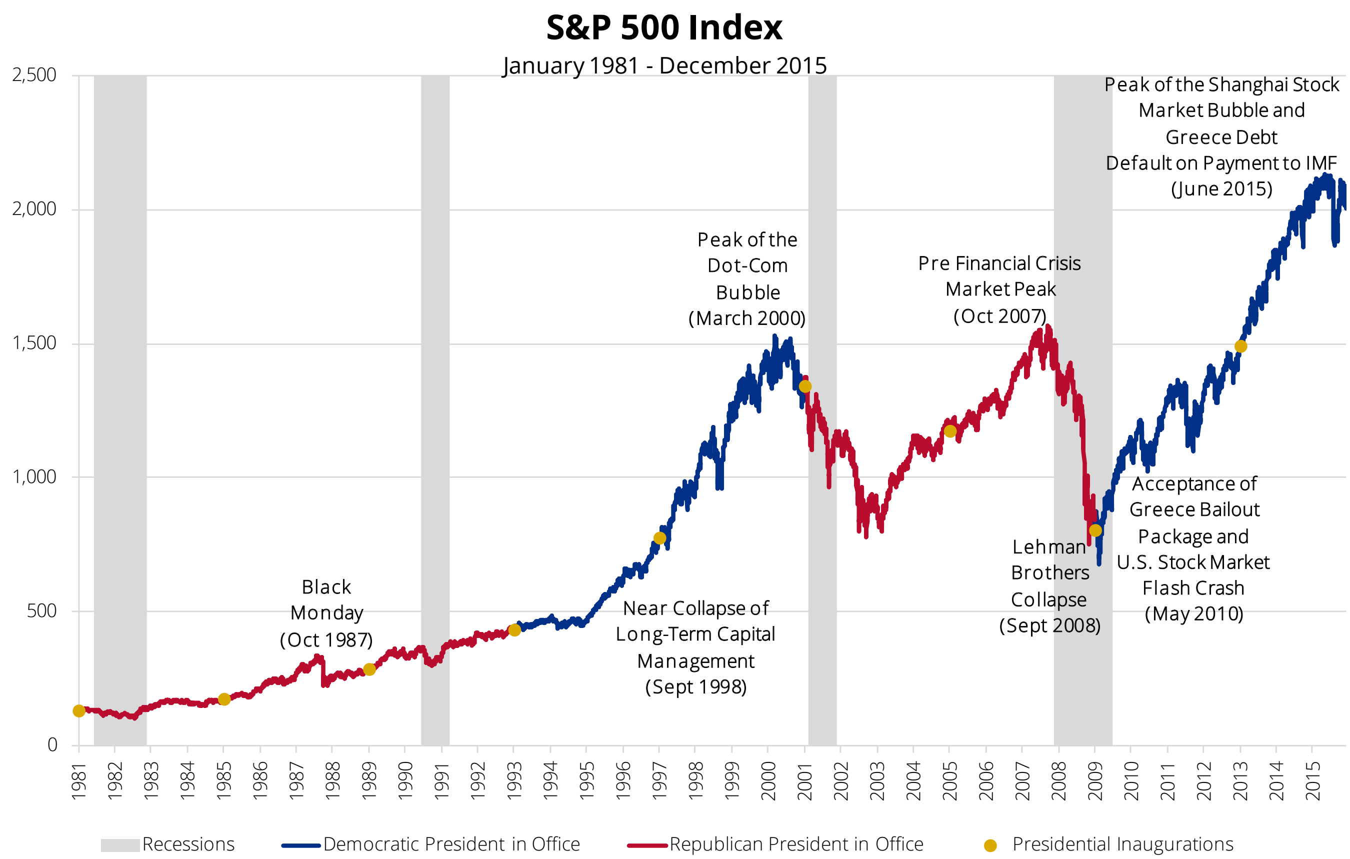
The table above shows the annual performance of U.S. large-cap stocks beginning with the election of 1928. The table separates annual returns into four categories: election years, post-election years, midterm years and pre-election years. The table shows that U.S. large-cap stocks have historically, on average, generated returns of 11% during election years. An 11% return is considered a healthy return and it ranks second behind pre-election years, which show a historical average return of 17%. Pre-election years have overwhelmingly been the most favorable years for U.S. stock market returns, producing both high average annual returns and the fewest number of negative return years. However, the historical trend has broken down in recent election cycles and there is certainly no guarantee that 2016 returns will meet the average historical return for election years. Pre-election year returns most notably have broken the trend, with returns falling to the low single digits. That strength has instead been seen in recent post-election year and midterm year returns.

The impact of political parties on stock market performance

In addition to examining stock market returns throughout the four-year election cycle, we also examined stock market returns under Democratic and Republican presidents. The bar chart below shows the annualized four-year returns under all presidents in office since the end of the Great Depression. The data demonstrates that U.S. large-cap stocks have historically, on average, generated higher returns while Democratic presidents held office. However, the chart also demonstrates that the U.S. stock market has produced solid returns during the terms of many U.S. presidents, including Republican presidents Dwight Eisenhower, Ronald Reagan and George H.W. Bush. When examining this chart it is important for investors to keep in mind that other factors besides the political party in the White House are often at play influencing stock market returns, such as global economics and Federal Reserve monetary policy.



Source: Morningstar® DirectSM; The American Presidency Project; GWCM analysis. Returns are shown for the IA SBBI US Large Stock Ext Index. *Past performance is no guarantee of future results.*



Source: Bloomberg; National Bureau of Economic Research; GWCM analysis. *Past performance is no guarantee of future results.*

In order to further explain the relationship between the political party in the White House and the historical performance of the U.S. stock market, we have provided a line chart of the S&P 500 Index® since the beginning of Ronald Reagan's presidency in 1981. The blue line segments on the chart represent the time periods when a Democratic president was in office and the red line segments represent the time periods when a Republican president was in office. The chart provides another visual, historical representation of stock market strength under Democratic presidents, but it also reminds us of other significant events that have taken place in recent decades. Some of these events may have had little connection to the political party in the White House and they represent how the correlation of political parties and stock market returns may simply be lucky (or unlucky) timing. As an example, the tech bubble peaked near the end of the term of a Democratic president, but the brunt of the market correction occurred during the term of the new Republican president. Is it then fair to conclude that the bear market was the result of the new Republican president? Of course not. It was simply a function of the timing of market events that occurred around the change in the White House.As a second example, we look at the two most recent events shown on the chart above, the resurfacing of Greece's debt crisis and China's stock market bubble. Both of these events introduced volatility into U.S. financial markets. This is not entirely surprising because as markets become more global, we are seeing that international events can also have a significant impact on U.S. domestic markets. The important thing to note here is that events like this can occur independently of the political leanings of the U.S. president. Because other factors are expected to have an impact on market performance, we caution investors against using presidential elections and election cycles as the sole basis for investment decisions.

In conclusion, while the historical statistics around presidential elections and stock market performance have produced some interesting results, we believe that investors should continue to stick to their long-term investment strategies as the 2016 presidential election approaches.

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