ON COURSE

Understanding Election Cycles and Their Impact on Wealth and Markets

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WINTER 2024

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Election cycles in the United States are not only pivotal moments in our nation's political history, but they can also have an impact on financial markets and the wealth of citizens. This year, the U.S. will be holding elections for President, one-third of the Senate, and all seats in the House of Representatives. The outcomes of such elections, the economic policies of incoming presidents, and the uncertainties surrounding political transitions all contribute to various implications for investors, businesses, and individuals.

Let's explore further the impact of an election cycle on wealth and financial markets and how a wealth manager can help navigate through this every-four-year event. We'll start with the most notable impacts election cycles can have on wealth and markets:

1. **Market Volatility**. One of the most immediate effects of an election cycle is increased market volatility. As elections draw near, investors tend to become more cautious, and uncertainty rises. The financial markets commonly respond with higher levels of short-term fluctuations as participants try to assess the potential implications of a new administration.
2. **Policy Changes**. Elections virtually always have some impact on the nation's economic policies. Each candidate comes with their unique policy proposals on items like taxation, trade, and financial regulation. Depending upon the election outcome, the direction of such policies may change, leading to shifts in market dynamics.
3. **Sector Rotation**. Election cycles often lead to sector rotation within the markets. As new policies are proposed and expectations change, investors may shift their focus to sectors they believe will benefit the most under the incoming administration.
4. **Fiscal and Monetary Policy**. The President's ability to influence fiscal and monetary policy is substantial. They can work with Congress to pass

budgets and tax legislation and appoint or nominate key economic officials, including the Federal Reserve Chairperson. Subsequently, the Federal Reserve can impact interest rates and inflation, and Congress and cabinet members can impact government spending.

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5. **Taxation Changes**. Taxation is central to election campaigns. Candidates may propose changes to income tax rates, capital gains taxes, and estate taxes. These policies can significantly impact an individual's wealth and financial planning strategies, as different tax proposals can have varying effects on economic growth and employment.

Who should we root for?

One concern that we hear virtually every election cycle is the market impact of the election of a particular party. Here are some insights to consider based on the impact of markets in general and based on different political party victories:

- **Stock Market Performance**. According to data published by RetirementResearcher.com, from 1926 to 2022 the S&P 500 has produced the following average annual returns: 14.52% during a unified Republican government (13 years), 14.01% for unified Democrat (36 years), 7.33% for a divided government with a Republican President (34 years), and 15.94% divided with a Democratic President (14 years). Note, these figures are historical averages and do not guarantee future performance.
- **Interest Rates**. Research by Capital Group indicates that interest rates have historically been lower during Democratic presidencies.
- **Historical Patterns**. Some studies have attempted to find correlations between party control and market performance. However, such market correlations tend to be mixed and can vary significantly based on the specific timeframe analyzed.
- **Short-Term Volatility**. As mentioned before, elections often lead to short-term market volatility due to uncertainty about potential policy changes. This volatility may not necessarily indicate a long-term trend but could affect short-term trading strategies.
- **Sector-Specific Reactions**. Certain sectors may react differently based on the perceived impact of new policies. For instance, healthcare stocks can be affected by proposed healthcare reforms, while energy stocks may react to changes in environmental policies.
- **Bond Market Reaction**. Changes in fiscal policies, government spending, and borrowing can influence bond markets. Policies suggesting increased government spending may impact bond yields and issuance.
- **Global Context**. Of all the economically developed countries, U.S. elections have the largest impact on the global stage, playing

significant roles in both the global economy and geopolitics.

- **Long-Term Trends**. While elections can prompt short-term market movements, long-term market trends are generally driven by broader economic fundamentals, technological advancements, and global economic conditions.

How your wealth manager can help

Navigating the complexities of election cycles and their impact on wealth and financial markets requires a deep understanding of financial planning, investment strategies, and economic policies. These are five key ways we help our clients navigate through election cycles, as well as non-election years:

1. **Informed Investment Decisions**. We provide clients with valuable insights into how different policy proposals may impact your investment portfolio. These insights and your response to them help us make informed decisions on asset allocation and sector-specific investments to maximize returns and manage risk.
2. **Risk Management**. In periods of increased market volatility, risk management is crucial. We can assess your risk tolerance, recommend adjustments to your portfolio, and implement strategies to mitigate potential losses.
3. **Tax Efficiency**. As tax policies may change with different administrations, we can help you plan for potential tax changes. This includes strategies for tax-efficient investing, estate planning, and asset allocation.
4. **Long-Term Financial Planning**. Elections may create short-term market disruptions, but we will guide you in focusing on your long-term financial goals. Those are the goals that will best help you develop a financial plan that considers the impact of election cycles and adjusts your strategy as needed.
5. **Staying Objective**. Emotional decision-making can lead to impulsive investment choices that may not align with your long-term financial goals. We provide an objective perspective and will help you make rational decisions.

Election cycles can have an impact on wealth and financial markets, though the impacts are typically short-term in nature. Successfully navigating these investment waters requires staying primarily focused on long-term goals and blocking out the noise that elections inherently provide.

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