How elections move markets in 5 charts

How much do elections impact the stock market and portfolio returns? Should elections even matter to long-term investors in the first place? These are the questions investors and financial professionals are facing as we approach November 5.

To provide answers, we've analyzed more than 90 years of market and election data and identified five ways that elections influence stock returns and investor behavior.

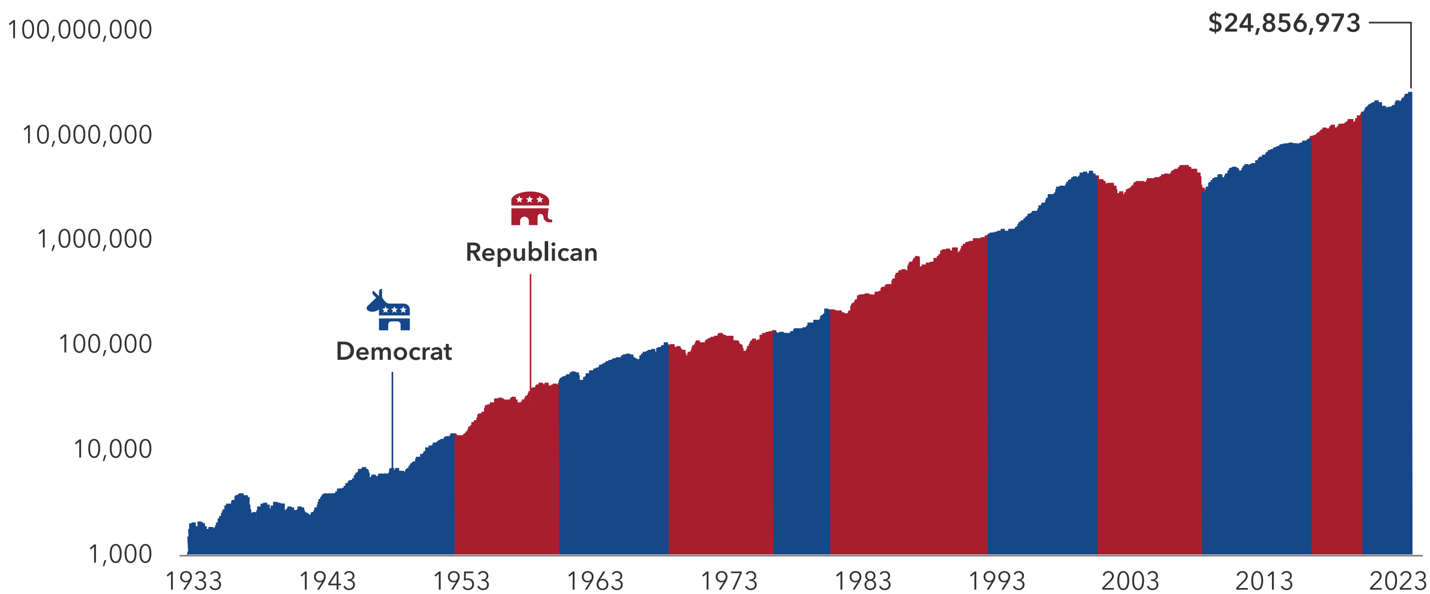
1. Markets have trended higher regardless of which party wins the election

Politics can bring out strong emotions and biases, but investors would be wise to tune out the noise and focus on the long term. That's because elections have, historically speaking, made almost no difference when it comes to long-term investment returns.

Which party is in power hasn't made a meaningful difference to stocks either. Since 1933, there have been eight Democratic and seven Republican presidents, and the general direction of the market has always been up. What should matter more to investors than election results is staying invested.

What does this mean for 2024?
Some may feel that the 2024 election is the most important in recent memory. But that has been said about previous elections and will likely be repeated about future elections. While this year has been unique in countless ways, a look at past election cycles shows that controversy and uncertainty have surrounded many elections. And in each case the market continued to be resilient. By maintaining a long-term focus, investors can position themselves for a brighter future regardless of the outcome.

Growth of a hypothetical $1,000 investment in S&P 500 Index



Sources: Capital Group, RIMES, Standard & Poor's. Chart shows the growth of a hypothetical $1,000 investment made on March 4, 1933 (the date of Franklin D. Roosevelt's first inauguration) through June 30, 2024. Dates of party control are based on inauguration dates. Values are based on total returns in USD. Shown on a logarithmic scale. Past results are not predictive of results in future periods.

Investments are not FDIC-insured, nor are they deposits of or guaranteed by a bank or any other entity, so they may lose value.

History shows that stocks have done well regardless of the makeup of Washington.

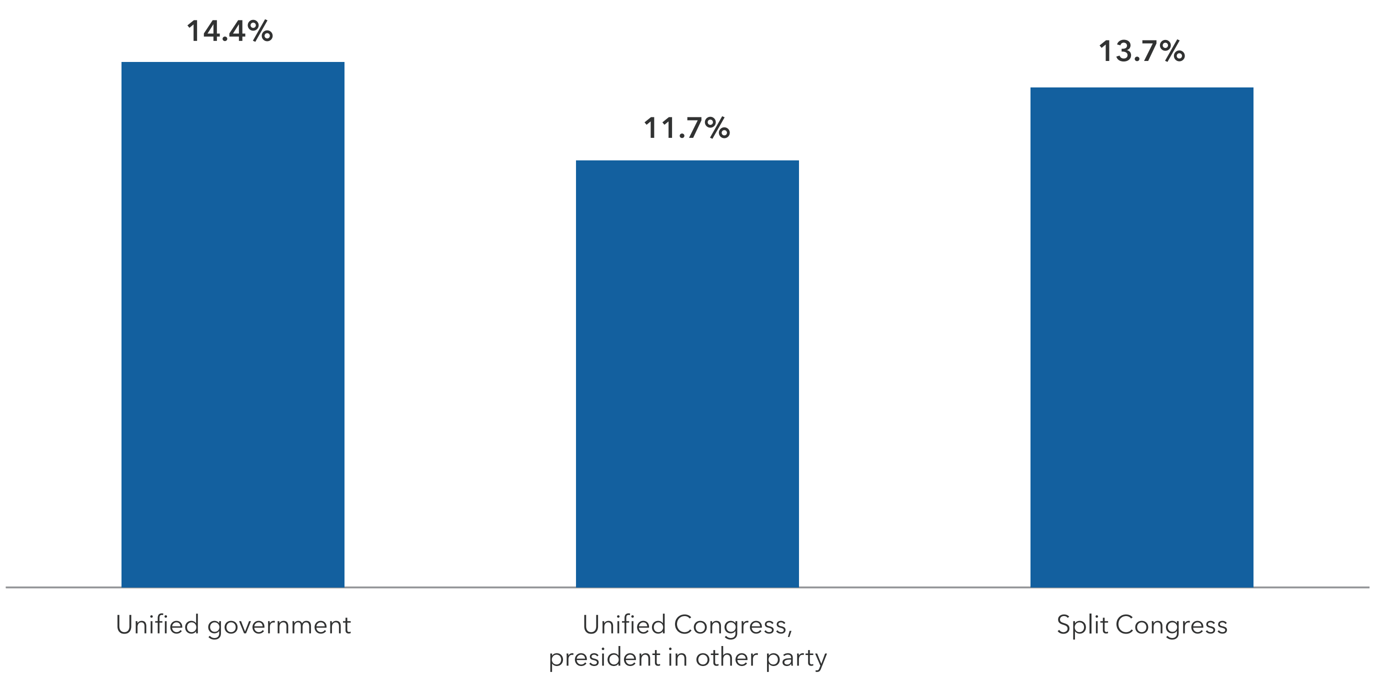
2. Gridlock or sweep? Equities have gone up either way

The presidential election isn't the only one to watch. The results of key legislative races could determine whether either party controls both chambers of Congress, making it easier to fulfill their policy agenda. Investors often fear such "red wave" or "blue wave" scenarios, but assuming such an outcome will lead to meaningfully lower stock prices oversimplifies the complexities of stock markets.

History shows that stocks have done well regardless of the political makeup of Washington. Since 1933, there have been 44 years when one party has controlled both the White House and Congress at the same time. During these periods, stocks averaged a robust 14.4% return, slightly higher than the average gains when Congress was split between the two parties. Historically the "least good" outcome has been when Congress is controlled by the party opposite the president, but even this scenario averaged double-digit returns.

What does this mean for 2024?
Many election watchers expect the Senate to flip to Republican control in November. But narrow margins in both chambers of Congress and shifting polls for the general election mean any outcome is still possible. Voters may have a strong preference for these results, but investors should take comfort that all of these scenarios have historically produced strong equity returns.

S&P 500 Index — Average annual total return (1933–2023)



Sources: Capital Group, Office of the Clerk — U.S. House of Representatives, Senate.gov, Standard & Poor's. "Unified government" indicates White House, House and Senate are controlled by the same political party. "Unified Congress, president in other party" indicates House and Senate are controlled by the same party, but the White House is controlled by a different party. "Split Congress" indicates House and Senate are controlled by different parties, regardless of the White House control. Data excludes 2001 due to Senator Jeffords switching parties midyear. As of December 31, 2023. Past results are not predictive of results in future periods.

A simple stock market metric has correctly predicted the winner in 20 of the last 24 presidential elections.

3. Markets have tended to predict election results

A simple stock market metric has correctly predicted the winner in 20 of the last 24 presidential elections since 1936 — a track record that might make even the top pollsters jealous. If the S&P 500 Index is up in the three months prior to Election Day, the incumbent party usually wins. If markets are down during that period, the opposing party typically claims victory.

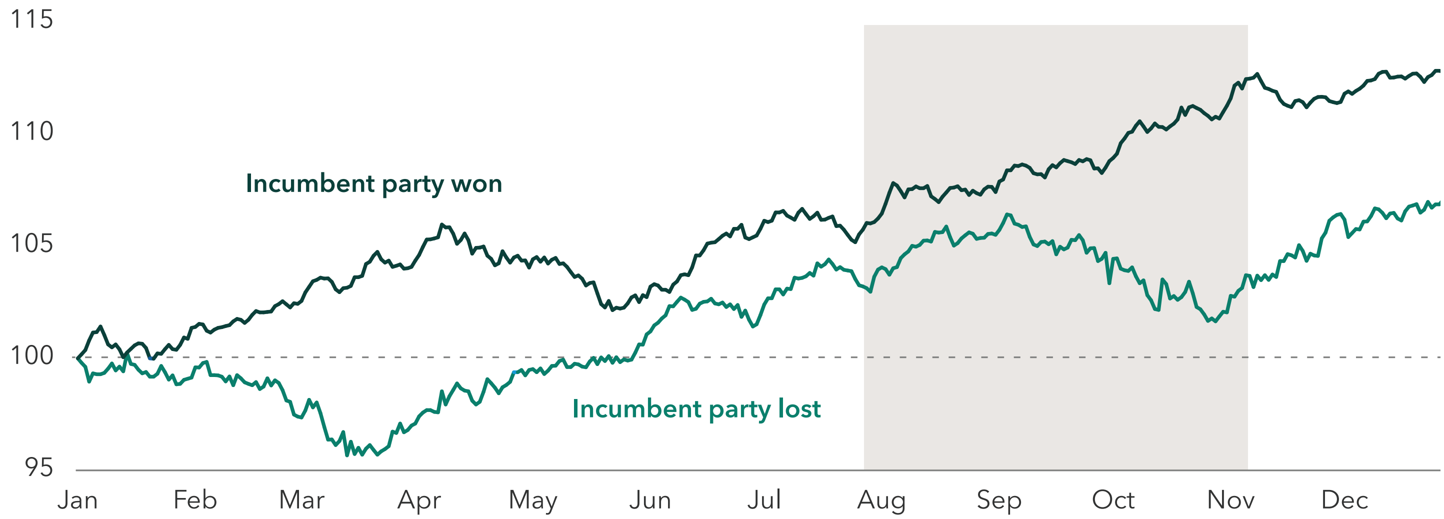
Why is this? It's because equities tend to look ahead and "price in" uncertainty — including that caused by an upcoming election.

When the stock market and the economy are strong, there is usually less motivation for a change in leadership. In those years, stocks may not need to discount the uncertainty, which often allows stocks to continue rising, further bolstering the incumbent's chance of reelection.

When the political and economic climate are more challenging, there is a greater chance that the opposing party will win. The market discounts the added uncertainty of the election outcome and what policy changes may occur, which can lead to higher volatility.

What does this mean for 2024?
The S&P 500 Index has risen 18% this year (through July 11), and U.S. GDP has been positive for seven consecutive quarters. A strong economic and market environment typically benefits incumbent candidates. However, higher volatility in the months ahead may occur as voters wrestle with a contentious campaign. Although it will be interesting to watch how stocks move leading up to the election, investors shouldn't use it as a reason to try to time markets. Historically, whether the incumbent wins or loses, election volatility has usually been short-lived and quickly given way to upward moving markets.

S&P 500 Index average returns during election years (1936–2020)



Sources: Capital Group, Standard & Poor's. Returns are indexed to 100 on January 1 of each election year. Returns are in USD. The shaded region approximately shows the three-month period prior to Election Day. Past results are not predictive of results in future periods.

History has shown that elections have had a clear impact on investor behavior, but it's important that investors don't allow pessimism to steer them from their long-term investment plan.

4. Investors often become more conservative in election years

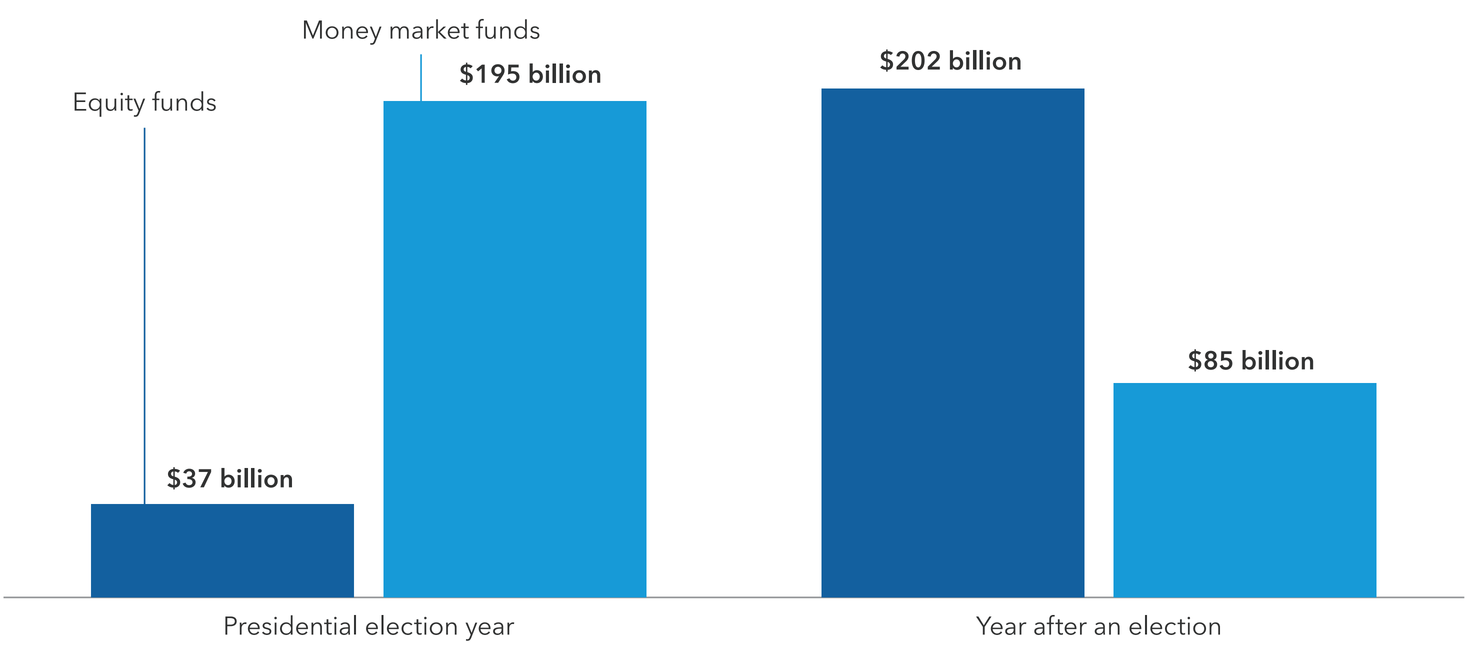
It can be tough to avoid the negative messaging around election coverage. And it's natural to allow the rhetoric of political campaigns to make us emotional. History has shown that elections have had a clear impact on investor behavior, but it's important that investors don't allow pessimism to steer them from their long-term investment plans.

Investors have poured assets into money market funds – traditionally one of the lowest risk investment vehicles – to a much greater degree in election years. By contrast, equity funds have seen the highest net inflows in the year immediately following an election.

This suggests that investors want to minimize risk during election years and wait until uncertainty subsides to revisit riskier assets like stocks. But market timing is rarely a winning investment strategy, and it can pose a major problem for portfolio returns.

What does this mean for 2024?
Net money market flows soared $971 billion last year while equity flows were relatively flat. This pushed money market fund assets to record levels – $6.1 trillion as of July 10, 2024, according to the Investment Company Institute. At these levels, many investors' portfolios have likely become misaligned with their long-term goals. Speaking with a financial professional can be helpful to ensure portfolios are well-diversified and in line with investment objectives.

Average net fund flows by year of presidential term (1992–2023)



Source: Morningstar. Values based on USD. Funds include mutual funds and ETFs. Equity funds include funds within Morningstar's International Equity and U.S. Equity categories. Money market funds include funds within Morningstar's Money Market category. As of December 31, 2023. Past results are not predictive of results in future periods.

5. Moving to cash in election years can reduce long-term portfolio returns

What has been the best way to invest in election years? It isn't by sitting on the sidelines.

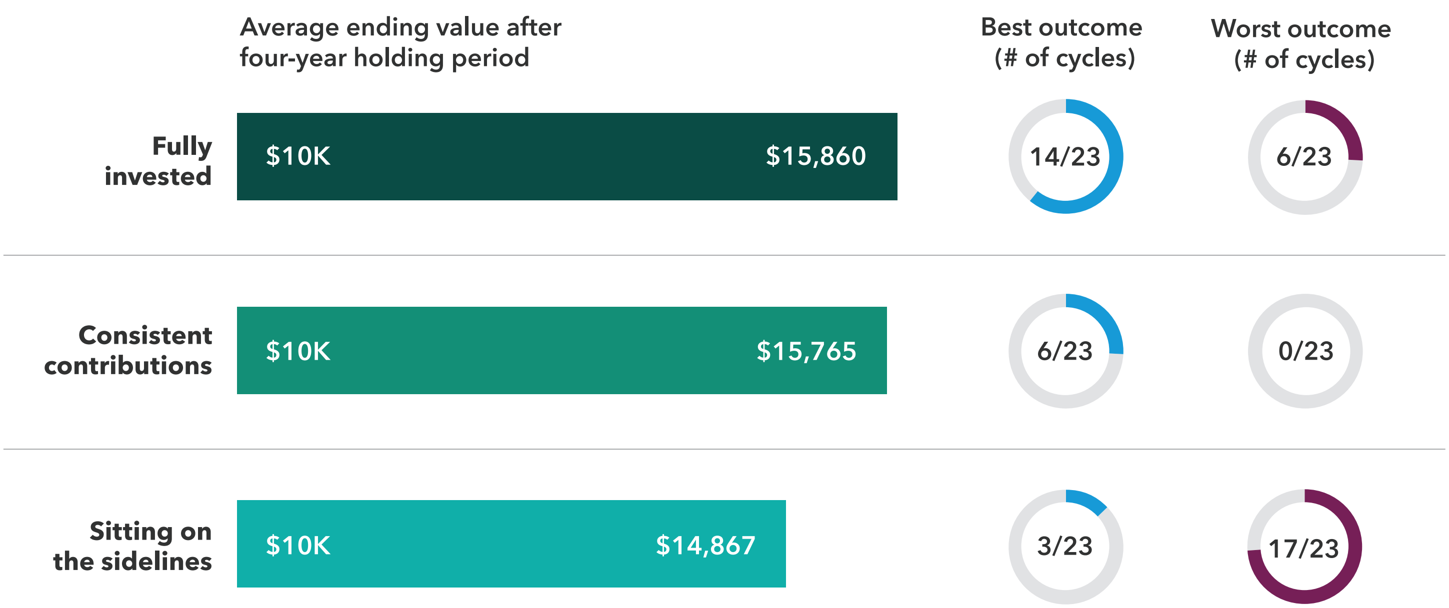
To verify this, we looked at three hypothetical investors, each with a different investment approach. We then calculated the ending value of each of their portfolios over the last 23 election cycles, assuming a four-year holding period.

The investor who stayed on the sidelines had the worst outcome 17 times and had the best outcome only three times. Meanwhile, investors who were fully invested or made monthly contributions during election years came out on top. These investors had higher average portfolio balances over the full period and more frequently outpaced the investor who stayed in cash longer. These results reflect four-year holding periods, but the divergence would be even wider if compounded over longer time frames.

Sticking with a sound long-term investment plan based on individual investment objectives is usually the best course of action. Whether that strategy is to be fully invested throughout the year or to consistently invest through a vehicle such as a 401(k) plan, the bottom line is that investors should avoid market timing around politics. As is often the case with investing, the key is to put aside short-term noise and focus on long-term goals.

What does this mean for 2024?
Cash investors have enjoyed their highest yields in decades, but those rates have paled in comparison to stock returns. Between October 2022 and June 2024 – a period in which money market fund assets increased from $4.6 trillion to $6.1 trillion – the S&P 500 Index rose more than 55%. It's too early to know the long-term portfolio impact of this flight to cash, but it is safe to assume many investors missed at least some of this powerful equity rally and remain on the sidelines ahead of the November election.

Three hypothetical $10K investment strategies during an election cycle



Sources: Capital Group, Board of Governors of the Federal Reserve System (U.S.), RIMES, Standard & Poor's. The three hypothetical investors each have $10K to invest during an election cycle and are invested in a combination of equities and cash at all times. "Fully invested" is always fully invested in equities. "Consistent contributions" starts with $1K in equity and $9K in cash. At the start of each of the next nine months, this investor reduces cash by $1K and makes a $1K contribution to equities, after which they will have made the full $10K contribution to equities. "Sitting on the sidelines" is entirely invested in cash during the first year. At the start of the second year, this investor reduces cash by $10K and makes a $10K contribution to equities. S&P 500 Index used for equity returns and reflect the reinvestment of dividends. Three-month Treasury Bills used as a proxy for cash returns and reflects the reinvestment of interest. Returns and portfolio values are calculated monthly and in USD. Analysis starts on January 1 of each election year and reflects a four-year holding period. Past results are not predictive of results in future periods.

S&P 500 Index is a market capitalization-weighted index based on the results of approximately 500 widely held common stocks.

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