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Will the U.S. elections throw equity markets off course?

A candid look at what history tells us about election years

To say we are living in unprecedented times would be putting it mildly. Six months into a public health crisis that completely blindsided the world, markets are now grappling with yet another unknown – the uncertainty surrounding the U.S. presidential election.

While heading to the polls will surely be front and center in 2020, this year is a little different. With the U.S. presidential race sharing the limelight with COVID-19, what impact will this year's elections have on markets?

The impact of COVID-19 on the presidential election

A recession within two years before the election usually reduces their odds of a sitting president being re-elected. With that said, the outcome of the election will depend largely on whether the U.S. is in recession territory when voters cast their ballots in November.

Still, if voters believe the COVID-19 induced economic downturn is as an external disruptor and the U.S. president's "America first" agenda outweighs his administration's perceived handling of the pandemic, there is a glimmer of hope for the Republicans.

What history has shown in election years

History has shown that equity markets have been rather resilient in election years. On average, the U.S. stock market stalled in the 3 months preceding the last 10 presidential elections, but gains were generally observed over the following 12 months (see table).

S&P 500 total return around U.S. presidential elections

Election year	3 months before	3 months after	6 months after	12 months after
2016	-1.30%	7.80%	13.30%	23.70%
2012	3.00%	6.50%	14.50%	26.80%
2008	-19.00%	-16.60%	-8.40%	6.90%
2004	2.60%	6.00%	3.70%	9.40%
2000	-2.90%	-6.10%	-11.20%	-21.00%
1996	8.80%	9.50%	17.40%	34.50%
1992	-0.40%	7.20%	6.80%	13.40%
1988	2.90%	9.50%	13.20%	27.20%
1984	5.80%	7.50%	7.30%	16.70%
1980	5.50%	1.40%	5.70%	3.30%
Average	0.50%	3.30%	6.20%	14.10%
Positive/ Total	60%	80%	80%	90%

Source: National Bank Investments, CIO Office (data via Refinitiv).

What could we expect?

2020 is anything but an "average" year, and the run-up to the election is likely to raise investor nervousness. But is this really enough to derail the ongoing economic recovery? Perhaps not.

A closer look at history shows that what explains the divergence in market behavior around presidential elections is not the political affiliation of the new president, senate, or house of representatives but rather, the health of the economy.

To conclude

Governments have shown they are willing to support the economy and markets at all costs throughout the pandemic. Furthermore, an emerging vaccine or game changing therapeutic is plenty of reason to be optimistic about COVID-19, which is an outlier this election year.

If Democrats win the election (they are currently ahead in the polls) they will more than likely increase the corporate tax rate. However, this would be offset by increased spending, which would probably not be too unsettling for markets.

NATIONAL BANK INVESTMENTS

Avoiding the whims of panic selling and investing for the long-term

The NBI Global Equity Fund and NBI U.S. Equity Fund, both of which have exposure to U.S. companies, are portfolios composed of high-quality businesses that are held for the long-term.

Key characteristics of the funds

1. **Low average turnover:** The portfolios are composed of best-of-breed companies that are industry leaders have a sustainable competitive advantage and meet strict selection criteria. As such, the average portfolio turnover is low.

2. **Long-term focus:** Short-term macro movements such as the outcome of the U.S. elections are not part of the portfolio manager's sell discipline, since portfolios are usually constructed from the bottom-up and held for long periods of time.

Whatever challenges markets face in the coming months, it is always important to keep calm, maintain a well-diversified portfolio and look to the long-term when investing. Staying invested and avoiding the whims of panic selling will always be crucial. Whether the U.S. elections will disrupt markets or not in the short-term shouldn't change the long-term outlook south of the border.

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1-877-463-7627

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