Marketline September 2020

Stocks:

This month we briefly review returns, but we are going to spend more time on the effects of elections on returns and whether one party dominates in terms of economic or market performance. So here goes…

Stock returns were down slightly across the board as money moved from technology stocks to other sectors. The Dow, which is light on tech, was off 2.3%, but the S&P and the Nasdaq, where tech is dominant, were each down 4% to 5%. Overseas, returns ranged from -2% to 2%, with the strongest numbers in Mexico.

For those of you who want the *Reader's Digest* version of this presentation: of the four years in a presidential term, election years are historically the second best time frame to own stocks, and there is no bias in returns to Democrats or Republicans. Now you may skip ahead to ***Bonds***! For everyone else, here is some interesting detail:

1. Election year total returns for the S&P 500 since 1944 have averaged 9.9%. The third year of a presidential term tends to produce even better numbers, at 11.9%.
2. On the other hand, watch out for year one of a term; returns average 5.7% and almost 45% of the time, the return is negative. These numbers go back to 1833.
3. The market is unimpressed with your opinion of the president. Stocks do best when approval ratings for presidents are between 30% and 50%. Greater than 50% approval ratings tend to coincide with worse returns.
4. There is virtually no statistical difference between Democratic presidents and Republican presidents in terms of return. Both have seen good and bad returns, as well as strong and poor growth. (Our time period for measurement here is 75 years.)
5. Predictions that the market will tank if this person or that takes office are notoriously wrong and should be ignored. Investors are better off staying invested and not reacting to politics.
6. A split Congress does result in better returns. When one party dominates Congress, no matter which it is, returns tend to be lower.

The takeaway is, the most treacherous year for returns in the election cycle is ahead of us, and the likelihood of a poor outcome increases if one party dominates the administration as well as Congress. After that, however, history tells us that improvement is probable. For those with a long term outlook, best to remain invested throughout. For those with other reasons to moderate asset allocation, now might not be a bad time.

Bonds:

After lots of action last month in the longer end, this month the entire curve was quiet. There are virtually no important yield changes to report.

With the bond market near all time low yields, this is a good time to understand that that means bond prices are at **all-time highs**. The bond market gets short shrift in the media, so it's harder to understand that if you sell stocks near all time highs to buy bonds today, you are basically moving out of the frying pan into the fire. When a bond is at a yield of 1.5%, it provides very little protection against inflation or changes in interest rates. A decline in price equal to the yield – just 1.5% - would give you a 0% return on that asset. To put that into perspective, many securities move by that much every single trading day. Worse yet, because of the way bond math works, low yields mean bonds are *more volatile in reaction to economic statistics*, not less. If bonds were at 5% yields, we would have adequate protection, but that is not the case. You can understand why the bond landscape offers a lot of challenges and not much reward. Still, we are taking second looks at securities that pre-Covid we would not have been interested in. That's because their yields are now much higher as investors fret about credit concerns. To us, these lower prices in certain sectors are like catnip to a cat.

Note: Michelle was named to the Board of Directors of Lewis & Clark Bank, headquartered in Oregon City, recently. This tour of duty has been very helpful towards understanding our local economy and how the environment is affecting financial institutions.

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