ARGUS®

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Washington and the Stock Market

The 45th President of the United States has now taken office, while continuing the strident and at times contradictory style that solidified his enthusiastic base and infuriated opponents. The new president comes to office with his party in control of both the House and Senate. He was elected, however, on campaign pledges that contradict long-standing GOP positions on trade, infrastructure investment, and entitlement spending. This is creating consternation among house members and senators who are also worried about potential disruption in the healthcare economy.

At Argus, we attempt to assess the political landscape only insofar as it influences the investment landscape. Regardless of how any unanimity or animosity within Republican ranks will affect policy, dispassionate analysis of the numbers shows that the stock market has historically outperformed when one party controls the White House, Senate and House of Representatives.

A GRADUAL AND COUNTER-INTUITIVE SHIFT IN THE DOMINANT PARTY

Dominance of Presidency, Senate and House by one party matters a great deal in terms of ability to set legislative agenda while avoiding the Presidential veto. Although Democrats have experienced this dominance for just two years since the mid-1990s, President Obama used that brief period of dominance (2009-2010) to push through the Affordable Care Act.

The popular Wall Street wisdom is that the best outcome in Washington is gridlock, whereby neither party controls all three chambers. Our analysis of S&P 500 performance in the post-WWII era does not substantiate that widely held perception, however. Since 1945, the stock market has relatively outperformed in years in which one party enjoyed hegemony. While talk of a Washington-Wall Street link is widespread, market drivers in any year have more to do with the economy and earnings than with who rules Washington.

Even amid demographic changes that would seem to favor Democrats, the Republican Party has generally gained more power in recent decades. The FDR years, with their sweeping social programs, followed by the successful conclusion of World War II, ushered in what is seen as a golden era in the U.S. Beginning in 1945, our enemies (also our chief economic competitors) were prostrate; the government provided for the indigent for the first time in history; and the massive suburban migration fueled an enormous housing and infrastructure boom.

Regionally, the South had not yet repudiated the Democratic Party; and the White Ethnic working class of the Northeast was also solidly Democratic. As a result, for most of the period between 1945 and 1980, the Democratic Party either controlled the Presidency, the House and the Senate, or controlled at least two of the three.

The Reagan years heralded the abandonment of the Democratic Party by its historical bedrock voters in the Northeast and South. The Reagan years also coincided with the expansion of the Treasury market and the demise of the traditional defined benefit pension plan, two events with major consequences for investing patterns.

Since 1980, the GOP has enjoyed several periods in which it had a 2-to-1 lead over the Democrats in terms of controlling the Presidency, House and Senate; it even enjoyed one brief period during the George W. Bush administration in which it controlled all three. As the Trump years begin, the GOP is again in a position of hegemony.

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WASHINGTON & WALL STREET BY THE NUMBERS

Please note that as a starting point to our analysis, we analyze market performance by the years in which the President and Congress actually served, not the election year. From 1945 to 2015, the S&P 500 averaged a simple arithmetic change of 8.2%. This tally does not include dividends; including dividends, the average annual change in the S&P 500 since 1945 change is closer to 9.5%.

From 1945 to 1980, the S&P 500 averaged an annual change of 7.1%, before dividends. From 1981 through 2015, the S&P 500 averaged an annual change of 9.3%, before dividends.

Over the 1945-2015 span, encompassing 71 years, our analysis shows 27 years in which one party controlled the Presidency, the House and the Senate. For these 27 years, the average change in the S&P 500 (excluding dividends) was 10.0%. We also count 44 years in which either the Democrats or Republicans controlled two of the three. For these 44 years, the average change in the S&P 500 (excluding dividends) was 7.1%. Given the 290-basis points outperformance in years in which one party enjoyed hegemony, party dominance has not stood in the way of the stock market. As a corollary, gridlock may actually hinder investment performance.

How does the market perform in years in which each of the two parties is dominant (3-0)? Since 1945, the Democrats have enjoyed 23 years in which they controlled the Presidency, House and Senate; on average, the S&P 500 appreciated 9.5% in those years. Prior to the current situation, the Republicans had experienced only four years in which they controlled the Presidency, House and Senate; on average, the S&P 500 appreciated 13.0% in those years. Those George W. Bush years of 2003 through 2007 represent the heart of the brief bull market book-ended by the Technology implosion on one side and the housing collapse and great recession on the other.

How does the market perform in years in which each of the two parties has an advantage (2-1) but neither is dominant? There were 44 “two out of three” years since 1945; for those years, the average change in the S&P 500 was 7.1%, excluding dividends.

For the 26 of those 44 years in which Democrats had a 2-to-1 advantage, the average change in the S&P 500 was 6.1%, excluding dividends. And for the 18 of those 44 years in which Republicans had a 2-to-1 advantage, the average change in the S&P 500 was 8.4%, excluding dividends.

CONCLUSION

In summary, since 1945 the stock market appears to do better when the GOP is “in charge” compared to when the Democrats are in charge. Since 1945, and excluding dividends, the S&P 500 has averaged gains of 9.5% when Democrats controlled Presidency, House, and Senate; and 6.1% when Democrats controlled two of the three. Over that span, the S&P 500 has averaged gains of 13.0% when Republicans controlled Presidency, House, and Senate; and 8.4% when Republicans controlled two of the three.

Conversely, the market does better under Democratic presidents than it has historically done when a Republican was in the White House. For the 72 years between 1945 and 2016, Democrats held the White House for 36 years. For years in which Democrats have held the White House, the S&P 500 has averaged appreciation of 10.2%, excluding dividends. For the 36 years between 1945 and 2016 in which Republicans held the White House, the S&P 500 averaged appreciation of 6.2%, excluding dividends.

Every period and every presidency is different. Ultimately, the economy, earnings, and other factors may have much more to do with stock performance than with who controls Washington. President Trump has promised landmark changes in economic agendas spanning infrastructure, trade, immigration, and taxes, among other things. He will have to do battle with determined Democrats – and potentially with elements within his own party.

Still, as President Trump begins his tenure with Congress on his side, the stock market has a past history of hegemony in its favor.

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Investors