HOW DO STOCK MARKETS PERFORM
DURING A PRESIDENTIAL ELECTION YEAR?

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WHITE PAPERS

WT WEALTHMANAGEMENT

It's already been a difficult ending to 2015 and a tumultuous start to 2016 for most stock-market investors. The Santa Claus rally never materialized, and the January effect was an additional gut-punch that resulted in a 10% decline by January 20, 2016.

Since then, the S&P 500 has battled back from the mid-February 2016 capitulation point of 1,829, which represented a nearly 15% drop from the 2,134 achieved in May 2015, and again in June.

The "net/net" of this wild ride is an S&P 500 is flat for 2016, (as of 3/21/2016) which isn't all that bad. However, the rocky start in January has all but the savviest investor somewhat spooked. If history is any indication, it's not going to get a heck of a lot better. Why? Because markets tend to lag in historical averages—or even fall—in the last year of a U.S. president's second term.

Since 1900, the S&P 500 has, on average, fallen by 1.2% in the eighth year of a president's term in office, with the market rising only 44% of the time. The worst drop was in George W. Bush's last term, in 2008, when the market fell by about 40%.

While there are plenty of reasons why equities may struggle this year, such as falling oil prices and slowing global growth, election-related uncertainty isn't helping. Here at WT Wealth Management, we believe that it's a large but immeasurable part of the overall angst.

Come November, America will have a new president—but who that will be is still very much up in the air. This general lack of clarity is not good for the financial markets. In general, investors don't like the upheaval and uncertainty of an open-ended race with such diverse candidates.

HOW DO STOCK MARKETS PERFORM CONTINUED ON P2

HOW DO STOCK MARKETS PERFORM CONTINUED

Also, presidents in the final year of a second term are often less predictable than they were in previous years, which adds to the general uncertainty. Clearly, they are “lame duck” presidents with little political capital left, so they push through policy initiatives by executive orders and other creative means.

The final year of a two-term president stands in stark contrast to the final year of a president’s first term. Since incumbents are generally reelected, markets don’t suffer from the same uncertainty. Since 1900, the S&P 500 has gained an average of 11.5% and has risen 83% of the time in the fourth year of a president’s first term.

PAY ATTENTION IN AUGUST

There is a chance that the year won’t end up as badly as many feel it could, but it depends on who investors think will win the election. We could have the benefit of mid-year and year-end rallies—another reason why financial markets should not be timed. It is therefore important for you to invest within your risk-tolerance levels and become an interested observer.

In general, if stocks rise between July 31 and October 31, then people are generally of the mindset that the incumbent party will win. If equities fall, then the thinking is that a new party will take over. Again, it relates to uncertainty—as the saying goes, “Better the devil you know than the devil you don’t know.” That is, given a choice between a familiar but rocky situation and an unpredictable one, it is better to choose the former, because the latter could be worse. All the more reason to invest within one’s risk-tolerance levels rather than gamble on the incalculable.

PAY ATTENTION IN AUGUST CONTINUED ON P3

PAY ATTENTION IN AUGUST CONTINUED

The results of this late-summer-to-early-fall time period actually play out in the November elections. In 82% of the times stock markets have climbed from August through October, the incumbent party has won. In 86% of the times the market has been down, the replacement party has been the victor.

Individual sectors of the S&P 500 could also experience more ups and downs in the run-up to the election. Once candidates are chosen and party platforms are revealed, investors will have a better sense as to what industries might either benefit or suffer, depending on who's elected.

While those platforms are still to be determined, little things can make a big difference. For instance, an industry such as coal, which recorded a near 80% price decline in 2015, could see a rebound if investors think that the Republicans, which tend to favor less stringent air-quality regulations, will take the White House.

On the other hand, U.S-based pharmaceutical companies could see prices fall if Democrats, which have said that they want to cap drug pricing, remain in office. In our opinion, the stock markets will give a bit of clarity to the eventual outcome of the fall election.

2017, YEAR ONE, TERM ONE

In our opinion, after examining historical trends (see chart below), 2017 should be better than 2016 as the uncertainty is removed. Investors won't have to guess who will be in power, since a president's first year often yields a positive S&P 500, according to Presidential Election Cycle Theory. In fact, it's positive 61% of the time.

Since 1944, the S&P 500 has achieved, on average, a 6.2% gain in a president's first year in office, in term one, which isn't all that bad.

S&P 500 Price Changes During the Presidential Cycle

		S&P 500 1900-2015		S&P 500 1944-2015	
Year	**Term**	% Change	Up?	% Change	Up?
Year 1	**All Years**	**5.2%**	**59%**	**7.6%**	**59%**
	>First Term	8.2%	61%	6.2%	61%
	>Second Term	2.0%	60%	9.8%	60%
Year 2	**All Years**	**4.4%**	**61%**	**5.3%**	**61%**
	>First Term	-1.2%	44%	0.5%	44%
	>Second Term	14.3%	90%	13.8%	90%
Year 3	**All Years**	**10.9%**	**75%**	**16.1%**	**75%**
	>First Term	12.6%	72%	17.5%	72%
	>Second Term	5.6%	70%	11.5%	70%
Year 4	**All Years**	**7.5%**	**71%**	**6.1%**	**71%**
	>First Term	11.5%	83%	10.2%	83%
	>Second Term	-1.2%	44%	-1.4%	44%
Year 15	**All Years**	**7.0%**	**66%**	**8.7%**	**66%**
	>First Term	7.8%	65%	8.6%	65%
	>Second Term	5.3%	67%	8.8%	67%

Source: S&P Capital IQ. Past performance is no guarantee of future results

2017, YEAR ONE, TERM ONE CONTINUED ON P4

2017, YEAR ONE, TERM ONE CONTINUED

Year two of term one is where things potentially get difficult. Since 1944, the S&P 500 has achieved, on average, a mere .5% gain in a president's second year in office. During that first year, or the "honeymoon period," Americans are optimistic about their new leader. Then, by year two, policy makers begin to feel less restrained about introducing new policies and programs, which at times may be restrictive and unpopular with even voters that supported them. As these new programs—usually involving higher taxes, more spending and more regulation—are implemented, they begin to negatively impact business profits, consumers, and the financial markets.

The big numbers tend to appear in the third year of term one, after the midterm elections—and that is where, historically, the markets have really improved. Since 1944, in the third year of a president's first term, the S&P 500 has been up on average of 17.5% and has been positive 72% of the time.

What does this all mean? Do we manage money bases on these numbers? Of course not—but historical patterns, be they the weather or the financial markets, should be watched, and smart money managers are aware of them

CONCLUSION

In all reality, the world is different today. The '60s, '70s and '80s are almost like the "dark ages" compared to today's global economy. Heck, it's vastly different than just eight years ago! GDP (Gross Domestic Product) events in Europe, Japan and China impact the United States as if they were happening right here on our shores, because the U.S. financial markets do not operate and trade in the vacuum they had done for most of the 20th century. Currency and exchange rates from around the world affect the United States on a variety of fronts, and they impact commodities and financial markets daily around the world.

Since 1944, in the last year of a second term the S&P 500 has been, on average, down 1.4%, and positive only 44% of the time. But do we believe this is a reason not to invest? Absolutely not!!

Investing in the current environment is different—vastly different—than virtually any other time period in our lifetime. In January 2000, President Clinton's last year in office, the 10-year U.S. Treasury yield was 6.6%. Many investors today would happily take 6.6% and turn their back on the stock market. Today, with a 10-year Treasury yield under 2%, it's not really a wise option to invest there and forget CDs (certificates of deposits). In 1992, George H.W. Bush's last year in office, the 10-year Treasury yield was 7.03%, and in 1988, Ronald Reagan's last year, the 10-year yield was a staggering 8.6%. Future presidential uncertainty potentially drove equity investors to safer options with compelling returns while they waited to see how the presidential election played out. We believe this could have impacted equity returns to a great extent: fewer buyers in the marketplace, and stock prices will drop.

Unfortunately, we at WT Wealth Management believe that many investors are in the equity markets, not by choice, but by necessity. People are living longer, interest rates are dramatically lower, and people who retire in their late 60s still feel the need to grow their portfolios. Think about it: A $1 million portfolio invested in the 10-year Treasury yields less than $20,000, and a one-year CD yields less than $15,000. These historically low rates have driven usually conservative and risk-adverse investors into the equity markets to obtain higher returns.

CONCLUSION CONTINUED ON P5

CONCLUSION CONTINUED

At WT Wealth Management, we believe that years like 2016 are the reason why we manage every investor portfolio differently and uniquely. This is about your comfort level and your goals and objectives, not ours. So it is critically important to know your personal risk tolerance and what the potential downside of your portfolio could be.

As always, we are here to help. Please contact us if we can serve you in any way. Note, however, that the facts in this paper are mere observations about history, and truly it's anyone guess how this year will turn out.

DISCLOSURE

WT Wealth Management is a manager of Separately Managed Accounts (SMA). Past performance is no indication of future performance. With SMA's, performance can vary widely from investor to investor as each portfolio is individually constructed and allocation weightings are determined based on economic and market conditions the day the funds are invested. In a SMA you own individual ETFs and as managers we have the freedom and flexibility to tailor the portfolio to address your personal risk tolerance and investment objectives – thus making your account "separate" and distinct from all others we potentially managed.

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In addition to the normal risks associated with investing, narrowly focused investments, investments in smaller companies, sector ETF's and investments in single countries typically exhibit higher volatility. International, Emerging Market and Frontier Market ETFs investments may involve risk of capital loss from unfavorable fluctuations in currency values, from differences in generally accepted accounting principles or from economic or political instability that other nation's experience. Emerging markets involve heightened risks related to the same factors as well as increased volatility and lower trading volume. Bonds, bond funds and bond ETFs will decrease in value as interest rates rise. A portion of a municipal bond fund's income may be subject to federal or state income taxes or the alternative minimum tax. Capital gains (short and long-term), if any, are subject to capital gains tax.

Diversification and asset allocation may not protect against market risk or a loss in your investment.

At WT Wealth Management we strongly suggest having a personal financial plan in place before making any investment decisions including understanding your personal risk tolerance and having clearly outlined investment objectives.

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DISCLOSURE CONTINUED ON P6

DISCLOSURE CONTINUED

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