STODGELL INVESTMENT MANAGEMENT

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FOUR MORE YEARS

Our title is not a prediction of the upcoming US Presidential election but a starting point for a discussion on whether the stock market will do better under a Democratic or Republican administration. It is widely thought that a Republican administration is more business friendly thus positive for stock prices; a Democratic administration more likely to spend more on social programs, and increase taxes which may impact stock prices negatively. This view was recently supported by President Trump who predicted that if Vice President Biden were to be elected the stock market would crash and the worst depression in US history would follow.

While there are several studies, each potentially biased, as most studies can be, it would be important to try and find a relatively objective one which is why the UK based investment bank, Liberum, given their literal and figurative distance from the USA might be a worthwhile reference. In their recent study, they conclude that traditional thinking which suggests stock prices do better under Republican leadership, is not accurate.

According to Liberum's study, since 1947, the S&P 500 has posted a total annual return of 10.8% under Democratic presidents, versus 5.6% under Republican presidents. If you go further back to the 2008-2009 Recession, which was under a Republican administration, the results still favour a Democratic administration. Even from 1947 to 2006 Democratic administrations watched the stock market provide returns of over 10% compared to just over 6% for Republicans.

Obviously, the present administration's term has not yet ended and while the stock market has done well, the point of the study is simply that Democrats are not bad for the stock market. In fact, given they tend to spend more rather than reduce taxes, the economy is generally stronger. Trump's tax break was more selective directed toward wealthier Americans and corporations and, of course, the economy has suffered due to COVID 19. While stock market index returns can be misleading, given they are often market cap weighted, another interesting study, done by CFRA Research, states that 10

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of the last 11 recessions began under Republican administrations. While COVID 19 is to blame for the most recent recession, the trend continues with the recent recession started under Republican rule.

There are exceptions to every rule. Jimmy Carter's democratic administration was in power during the one recession that started when a Republican was not in the White House. Slow growth and high inflation were inhibiting economic growth and stock prices due to extremely high oil prices. And to be fair, George Bush was in charge during 9/11 and the bursting of the dot com phenomenon. Trends are useful but not always reliable. However, it would appear that a Biden administration, along with the possibility of a Democratic led House and Senate, will be no worse for investors than a Republican presidential victory.

Of course, the economy and stock market performance in the next four years, will depend on many factors. One important influence will be fiscal and monetary policy. Possibly, a Biden Presidency might roll back some of the present tax breaks that seem to benefit the more favoured economic classes. It would appear doubtful with the economy straining to recover that either administration would increase taxes across the board. A new tax cut may favour cuts to benefit those left out of President Trump's tax cuts. Interest rates appear to be remaining close to present levels for some time though you may see more government spending under Biden leadership rather than an incumbent administration. And, of course, we have COVID 19 which seems to be rearing its lethal head again, especially to younger members of the population. While some may be related to the September long weekend and a return to school, economies either side of the border cannot afford to shut down businesses again. Admittedly, nor can they afford the pandemic getting out of control. Certainly, with the election and the fact that the US has not been able to contain their COVID cases which leads to an important question; what about a second wave in the US? It is hard to figure whether they have contained the first one.

Bifurcation continues in the markets and the separation in values continue to widen. But with the prospect of continued recovery in the economy (a democratic administration has enjoyed higher GDP growth than their counterparts) the more cyclicals have been gaining some attention. However, the market certainly continues to favour some of the big technology companies. Interesting that whispers in the US continue about the current administration challenging the hegemony of big technology. Calls to break them up in the House of Representatives have resurfaced lately. It is uncertain whether this will continue if there is a change in the White House in the upcoming U.S. election.

It is not the viability of these high-flying technology companies that is in question, it is more their valuation. At the time of writing, Shopify has a market cap of approximately 157 billion, trades at 55 times sales and has a price earnings ratio of over 445. The Royal Bank has a market cap of 138 billion, trades just over 2 times sales and has a forward price earnings ratio less than 13. Royal Bank pays a dividend. While I am sure both companies will continue to flourish, we continue to favour those more conservatively valued companies for more than the next four years.