Episode 38: Party Affiliations and Stock Market Returns - Who has your vote?

Bob French 00:00
The purpose of Retire with Style is to help you discover the retirement income plan that is right for you. The first step is to discover your retirement income personality. Start by going to risaprofile.com/style and sign up to take the industry's first financial personality tool for retirement planning. Looking for insightful policy analysis? Um, can we offer historical stock market data instead? Or a nice discussion on how to use statistics in your portfolio?

Alex Murguia 00:51
Hey, everybody, we're back on retire with style here with my trusted companion and my trusted companion companion. may have been a better way to introduce trust you as much as we'd been, let's be honest, but you know, I caught myself in a in a web of intrigue. Yeah, why don't you explain that for me and introduce yourself?

Bob French 01:20
Yeah, this is Bob. I'm just here to make sure Alex digs the holes as deep as he possibly can for himself.

Wade Pfau 01:29
And I'm Wade and Alex didn't introduce himself either in that little

Alex Murguia 01:36
Alex Marijana Murguia.

Wade Pfau 01:39
All right. And this is Retire with Style.

Alex Murguia 01:49
All right, Wade. You've been on the road lately? What's been happening, man?

Wade Pfau 01:55
Yeah, I'm back on the road doing in person speaking events. And I was at an event in California where five or six different people came up to me specifically to say they've been listening to the podcast. And so Hi, everyone. And Alex did have some fans, they mentioned one person specific. That may be a surprise. But one person specifically said we want more Bob French. That's gotta give the people what they wants. Right? We've got Bob French today as our guest.

Alex Murguia 02:26
So yeah, well, I know I'm not as many people don't know, people don't know that we play a little drinking game. Whenever Nemo comes in, we all take a swig

Bob French 02:36
or a little drinking game. So

Alex Murguia 02:40
Bob loves to send me all emails. Let's just say my spam filter is full

Wade Pfau 02:48
feedback on Alex's performance tests.

Alex Murguia 02:53
Well, what else has been going on? Wade, I know like and folks don't realize. I mean, we batch a lot of these recordings. So it's been a I don't know, what is it four or five weeks since we've last? had one of these? You've been traveling a lot?

Wade Pfau 03:05
Yes. Yeah, we finished that variable spending arc. And indeed, yeah, October now that October has just finished up. It felt like a pre pandemic month for me, I had a trip most every week, and maybe even more than one trip a week. So it's, it's good to be back on the road. And it's different now of being on the road with the podcast out and actually getting that feedback of people listening to it. Because up until that point, just been doing everything from home, don't really see how the world changed in that regard.

Alex Murguia 03:33
Yeah, right. And even with the podcast, man, we've been just as upset. We our numbers have been going through the roof like week after week after week. So it's, it's pretty, it's pretty good to hear and, you know, on many fronts, so you know, thank you for your your support on that a lot. Bob, what what you've been a stranger, what's been what's been happening

Bob French 03:54
Been keeping pretty busy on the Retirement Researcher. So we've actually got a retirement income challenge coming up in two weeks. If you're

Alex Murguia 04:04
late as Bob pitching, is Bob actually pitching right? At the beginning,

Bob French 04:11
so if you're on the Retirement Researcher list, you should have gotten an invitation. But we'll definitely put the link in the show notes as well. So definitely would encourage you to sign up for that. That should be a good one with with all three of us. This time round. So

Wade Pfau 04:28
yeah, yeah. And that's not the topic today. But with interest rates coming up, I'm in the process of updating the retirement planning guide book and with the funded ratio tool that we'll use and that challenge the Retirement Income Challenge. Higher interest rates are making retirement cheaper these days. People are dealing with losses, of course, but if you can spend more from a declining portfolio value, you're not necessarily in that much worse shape. And so it's really interesting some of the things going on right now. Yep. But I guess that does lead somewhat into the the topic for today. Not directly Leave, but we can make it work. Indeed we are. We're about a week away from the midterm elections. And so there's always a lot of interest. And this is an area that Bob has done quite a bit of reading research and writing about just financial market returns and their relationship to political parties. Not that this, this will not be a political podcast, just looking at the empirical data and how, how things look in election years, midterm years, when different political parties are in power, and so forth. And that's really the theme for today's episode.

Alex Murguia 05:37
Yeah, I, I think one of the one of the, one of the inspirations from this is also the holiday seasons are upon us, and this is great cocktail party conversation on information. Do you have a noisy Uncle, you know, somebody that that just, you know, loves to spout, you know, politics with regards to the markets? Well, Bob's got chock full of information.

Bob French 06:03
Depending on which side is being annoying, we got, we got stuff to get them to quiet down. But, you know, that's actually a pretty important point, before we started on this conversation, you know, this is not, I want to be very emphatic. This is not about which party is better, which party is even better for the markets or not, you know, the election goes far, far beyond the markets, you know, farming on the economy. And, you know, just again, as we've always been saying, the markets are not the economy, you know, they rhyme in the long term, they match up reasonably well, in the long term, but it ain't the same thing. But, you know, that being said, you know, with I think we put enough provisos on there on the front end, you know, we can kind of take a look at, you know, some of the the big picture stuff that we have seen historically, and towards the end and get to some really, actually, I think, interesting things that, you know, pop out of some of these numbers, that can help us think through kind of the bigger picture things about, you know, just how we put our portfolios together, how we think about what's going on within the context of our plan. So, again, you know, the financial markets, they're just different from the economy as a whole, they are a subset of the economy as a whole, and they're the forward looking subset. So that's going to have a really big impact. But just kind of starting, like I said, the kind of the high level, you know, one of the big questions always is, you know, who's better for the markets, you know, who will go which party in power, you know, leads to better market returns, then we can kind of, we can obviously cut and slice and dice this numbers, any which way we want, you know, starting at the big picture, Democratic presidents have had better market returns than Republican presidents historically, at least, judging by the s&p 500. You know, just put some numbers around, it is pretty

Alex Murguia 08:07
Bob, Wade just walked out of the podcast, he just literally left, I gotta go get him.

Bob French 08:13
Yeah. I'll try and keep the numbers brief, because I really do want to get into that bigger discussion, you know, towards the end, but I want to kind of lay the groundwork here. So there is a big premium for Democratic presidents the premiums, just shy of 6%, per

Alex Murguia 08:31
when you say premium. What does that mean? Yeah. So

Bob French 08:33
what that means is the difference between the average turn of a Democrat or have the market during periods where Democrats have been in the White House, versus the average return of the market when Republicans have been in the White House. So when Democrats been in the White House, you know, it's been an average return to the s&p, you know, from 1926, through 2021, of, you know, 15 and a quarter 15.22% versus nine and a third for Republican so 9.32%. And this is just, please Go ahead Wade

Wade Pfau 09:08
I'm sorry. What I mean, to be clear on the methodology, and just to look at recent history, so like you'd say, 1993 through 2000, those would be Democrat years. Yep. 2001 To 2008 Republican years 2009 through 2016 Democrat years, that that's kind of the idea. And then you're taking Okay, let's put all the democratic years over here are the Republican years over here, and look at the average return exactly to those categories.

Bob French 09:35
Yeah. If we were to select a random year when a Democrat was the president and a random year, when the Republican was the president, you know, this is what we would expect to get. We're probably not going to but

Alex Murguia 09:48
so So Bob, I'm in thanksgiving, I'm in whatever, let's say Thanksgiving, right? And I'm having my pumpkin pie. And someone throws the stat at me and says You know, it's 15% versus 9%, you know, something like that. Democrats versus Republicans. So there, you should have voted for a Democrat. And then, you know, somebody says, listens to that and says, well, not so fast. That's really, the Republicans are paying for the sins of the Democratic Party, you know, when they were in power. And then when the Republicans have turned around, then the Democrats, you know, right, that tailwind, or vice versa, I couldn't use the different parties, I would answer that, because that's that, you know, you when you say that, you can't win an argument, right?

Bob French 10:36
No, that's, that's a big one. You know, a few years back actually ran that those numbers looking at, you know, with a one year lag, you know, what were the

Alex Murguia 10:45

what does that mean, just to make sure,

Bob French 10:47
basically, it's, we shift it one year. So, you know, the Democrats start getting credit one year after they take office when they take office, and they get credit for the first year of the Republicans in office. So, you know, in trying to think through and when people took office, so Obama took office in most of 2008.

Wade Pfau 11:10
So he won the election and 2008

Bob French 11:12
won the election.

Alex Murguia 11:13
Don't mess with Wade, Bob. Don't mess with Wade, Bob.

Bob French 11:20
So in that case, so Obama took office in 2009. So the Democrats wouldn't get credit until 2010. Whereas the Republicans would get credit for 2009. And what we saw in that is that the premium does go down a little bit. But it still exists. Even with that lag in the data, there still is a statistically significant premium for a Democratic president. But it's important to recognize that you don't want to read necessarily too much into that for a couple reasons, you know, and a good example of this is if just looking at presidential hype, that actually supposedly, according to the numbers is a better predictor has a bigger premium than presidential party.

Alex Murguia 12:13
So okay, so Bob, so if you and I were president, so I'm clearly significantly better job than I would.

Bob French 12:20
Oh, Alex is very short. Wade and I are not.

Alex Murguia 12:26
Bobs like six, five, I'm five, five, and weighs about 6 feet.

Bob French 12:33
Yeah, so presidents who are six feet or over have much better market returns since 1926. Then presidents who are shorter than six feet.

Alex Murguia 12:47
I am left handed, I am left handed.

Bob French 12:49
That is the other one that I put into the notes that that comes in. I am right handed,

Alex Murguia 12:54
I decided that I highlighted that. Yeah.

Bob French 12:56
So I'm not sure which way that cuts. But left handed presidents Also, according to the markets, did better than right handed presidents.

Wade Pfau 13:06
So then let's test you on how well you remember your data. Do you recall who the left handed presidents were? Is that one of the one

Bob French 13:15
that completely left - Immediately

Alex Murguia 13:17
off the top of my head? I'm pretty sure Clinton was left handed. So was Obama. So was the Bush the second Bush,

Bob French 13:24
I just pick the Presidents with good returns, and they were probably left handed.

Alex Murguia 13:29
So another way. So if I'm left handed, you're about six, five, Wade is right handed and six, and maybe he's six feet. You're right on the cusp, you and I put together are like Wade. Is that kind of what would happen?

Bob French 13:48
So you know, I think there's there's probably a little bit of a problem with two people the president. But other than that, there's no problems with that analogy at all. I

Alex Murguia 13:58
would be as effective as Wade.

Bob French 14:00
There is that. So but it kind of goes to the point that you got to always take this stuff with a grain of salt. Yeah. Stories, but I mean anything.

Alex Murguia 14:13
It's kind of the the Mark Twain thing, right. There lies damned lies and statistics.

Bob French 14:18
Yep. Let's take a moment to let the audience know that this show is sponsored by retirement researcher. You can learn more about retirement researcher at retirement researcher.com And subscribe to our newsletter, where You'll receive weekly actionable information for your retirement

planning benefit. Retirement researcher is an online community devoted to helping you create the retirement income plan geared towards your goals.

Wade Pfau 14:44
And sample too because there isn't that many presidents since 1926? Yep.

Alex Murguia 14:50
Kind of like the returns and sustainable withdrawal rates.

Wade Pfau 14:54
Yeah, going back to that theme where you you stuck a dagger into the heart Have the 4%

Alex Murguia 15:04
I think it isn't that it's more like euthanasia. And that, like you painted such a negative picture. But but something that I think bears interest to you, because I know we're just fooling around here. And and it's, you know, this is what we're about to a large extent, but

Wade Pfau 15:22
Speak for yourself.

Alex Murguia 15:23
That's our mission statement. Speak for you know, but I'm going back to the point of what do you think about voting based on what you think the economy will react to it? I'm gonna vote for this person, because it's better for the markets, I'm going to vote for that person, because it's better for the markets, that kind of thing. What's your comment on that?

Bob French 15:45
I would say that, if you take it one step back and say it's better for the economy, that's a much more useful statement. You know, because there obviously, are some pretty significant differences in, you know, how the Democrats and the Republicans want to manage the economy at this point, there's always differences. I would say that in terms of trying to do that at the, the financial market level, I don't think that has much value. You know, for a big chunk of that is that all of this information, it's already in prices. Now, the market already knows, you know, Republicans have, you know, been worse on the stock market, supposedly, or at least have had lower returns, when there has been a Republican president that's baked into the prices. And remember that prices move based on how that new information, what happens next squares with what the market expected. The other thing you got to be thinking about is, are these numbers meaningful going forward? You know, is, you know, how a Republican president in 1920 or 1932, does that tell you anything about what a Republican or a Democratic president will look like? Now? I don't know. I don't think so. I think it's kind of some interesting numbers to play with. But I don't think trying to vote based on this information is all that particularly useful.

Wade Pfau 17:23
That sounded like a diss on I was Native Son, Herbert Hoover.

Alex Murguia 17:28
I was native.

Bob French 17:32
I don't think I need to be doing that much on that. I think that that one speaks for itself.

Alex Murguia 17:39
And for those of you Wade, hails from Iowa, and he's a big fan of visiting every presidential library before his last breath on this earth, how far are you into that Wade?

Wade Pfau 17:49
I haven't been making much progress in recent years. But so I'm, I'm well over halfway, but I don't know exactly. I still got some places to visit.

Alex Murguia 18:00
You see, when you don't know it, but you're unintentionally mission statement is levity. Bob, what what do you mean by price, then? Because that's kind of a smartass answer that people say, as well.

Wade Pfau 18:17
Like the related question, while you're getting on that theme, when what if, when there is uncertainty, like with the midterm elections, it's still not entirely clear which direction that's gonna go? Yeah, that's the conclusion of that lead to greater certainty in a way that might help markets? But that's one big question.

Bob French 18:35
So start with that first part about, you know, what is priced in meat, you know, it gets to the fact that prices, you know, they're discrete things, basically discrete things, you know, you, at least in the paper, there's a specific number, I can go and buy or sell Apple, or pick a stock, you know, there is a price for these things. But how those prices are arrived at is probabilistic. Everyone's got these models of what they think the world will look like, what they think the economy will look like. And, you know, those encompass, you know, a lot of uncertainty. You know, so as new things happen, those models are constantly being updated. Those models are constantly incorporating that new piece of information. And when something happens, that will either be better or worse than what that model happened to be predicting. So it will drive the price up or down.

Alex Murguia 19:42
So is it fair to say, like in like, like in Vegas, right, their odds, it's really the odds, right? You don't just bet on the football team, you have to bet on the spread. So is it fair to say and within the context of Wade's question as well. The markets today are reflecting the probability As of the elections already, it may not end up like that, because the spreads change over time with new information that's unpredictable. But the markets already reflecting this. And so to some extent, to assume markets are going to tank the day of the election, barring some hugely unexpected information that comes in 24 hours before the election, there is nothing to see here, kind of kind of context.

Bob French 20:28
So they incorporate both the probability of the event and also the expected value of the event, basically, you know, how big of an effect is this going to have weighted against? How likely is this thing going to be? So you know, if there, if there's one party out there, who the market just decides is absolutely horrible, if there's one event that the market decides is the worst thing in the world, but there's a very low probability of that happening, it won't move the market all that much, it won't move prices all that much, because it's just probably not going to happen. Whereas if there's a higher probability event that isn't so bad, but that's going to probably, obviously, depending on how the numbers fall out, but that would probably move the market more. And also, these things are already happening, these things are already impacting the future prices.

Alex Murguia 21:30
Now, Bob, in addition to Iowa's favorite son, Herbert Hoover, there is another call to fame that I will have Wade. It's the electronic markets where they actually do bet on on elections, you know, that

Wade Pfau 21:46
my alma mater,

Alex Murguia 21:48
the University of Iowa, their University of Iowa, did you have you ever been on it? By the way?

Wade Pfau 21:53
No,

Alex Murguia 21:54
no. Firm? Nope. I was like, oh. Remind me to follow his browsing. Do you want to your and a lot of folks don't know, Bob is actually it was you're very much into politics, at least you were you know, I don't know if that's sort of swiveled up. But how accurate are these Iowa markets? Because this is we're telling you these things are priced in, but there are live markets that you can actually see that will effectively show you the probabilities.

Bob French 22:29
Yeah, I don't know, I don't have any numbers off the top of my head. You know, it's one of those things where, you know, I always liked seeing markets. You know, but there's some pretty significant limitations on those Iowa markets in terms of the amount of money that you can basically put up there,

Alex Murguia 22:48
it's not five to 500, something like that.

Bob French 22:50
Yeah, it's something something relatively small and crucially small enough that someone who will two things one, you know, a lot of people are perfectly happy to throw away 500, or whatever the top number is, I can't remember it is off top, my head, perfectly happy to throw that money away to try and

move those types of numbers move the market. Because that could potentially have an impact manipulated the actual events, which crucially, one of the important parts of the actual financial markets is, you know, no one's big enough to actually move the markets in any meaningful way across a broad swath of stuff.

Alex Murguia 23:32
So you're contributing to a political campaign. And if turning around and taking those contributions, and betting on themselves in the market that move the market?

Bob French 23:41
I wonder if they have any rules around, you know, for like the smaller end of those races?

Alex Murguia 23:48
These guys are trying I don't know.

Bob French 23:52
I've never looked into that. Now. I'm kind of curious. Right. But yeah.

Wade Pfau 24:03
A two page outline. Sort of the way through the first page.

Alex Murguia 24:10
That's the danger of putting Well, I guess I naturally do that. But if you put three of us together.

Wade Pfau 24:16
Well, I guess to get us back on track here, you look at more than just like the president in power. And I think a while since we were following the outline here. I think we did also talk about No, we did not touched on it. Yeah. House of Congress. That's

Bob French 24:30
so yeah, kind of get back since you know, we're talking about a midterm rather than a presidential. It's one of the key things here is that if looking at them in isolation, looking at, you know, the Senate or the House in isolation, you know, there's no substantive difference between the returns when one party controls one or the other party controls it. You know, it's about the same. And, you know, that's partially because, you know, it's one and how or is one half of one branch of office? Or one branch of the government? Excuse me? And there's also just some structural reasons why, you know, it's not as effective in moving things through as the presidency. But when we start kind of, I'm sorry, Wade, go ahead

Wade Pfau 25:20
luck. Just yeah, I mean, in that regard with it's the, there's a possibility that you have a divided government. And that is another issue you've looked at.

Bob French 25:27

Exactly. So when we start kind of picking it apart, what we see is that unified government, so, you know, the Republicans or the the president, House and Senate, all from the same party are all controlled by the same party actually have about the same returns between the two parties, you know,

Alex Murguia 25:48
roughly 14 and a half and change, yeah, 14 to 15.

Bob French 25:51
So, you know, historically, when Democrats have controlled all three branches, or all three, the presidency in the two houses, they got 14.9, Republicans, it was 14.5. So that's the same number in these types of things. But when we start looking at divided government, we start seeing some really interesting stuff, or we start at least seeing some differences. So first off, the average is a lot lower the average annual return, again, for the s&p 500, when we have divided government, so when at least one is different from the other two, was only 9.8% per year. So significantly lower. And, you know, there's a big, big difference, you know, in terms of, you know, how that's arrived at, because in terms of, you know, if the Democrats controlled two of the three sections of government, if you will, they were up at like, 15.9% per year. That was a much smaller number of years, then when Republicans were in control of a divided government. But that was down again, and 9.8, right, around 9.8% per year. But when we start getting into this, it really starts being important to look at the time periods we're talking about, we're looking at 14 years, where Democrats were in control of, or at least had two of the three sections of government that we're looking at, to kind of break that down six of those years, were the late 90s, when Clinton was President, which means they got the good part of the tech boom. You know, the next six years or another six years was kind of the heart of the post, oh, eight bull market from 2011 to 2016. And then the other two were right after World War Two, what was it 47 and 48. So they have some really, really good years, that, you know, just happen to coincide with them having, you know, that type of, you know, government setup. So they had some really, really good years. I don't think anyone's going to be arguing that, you know, the late 90s tech boom was because Clinton was the president.

Alex Murguia 28:22
Well, Gore did invent the internet.

Bob French 28:24
That is true. That is true. So that lockbox, so but, yeah, I mean, so we got to think about that. On the other hand, you know, Republicans did have 34 years of that deferred divided government. And, you know, there were some some bad periods in there as well. I mean, they that included 1931 which was when the market crashed. That was the great crash. You also had, you know, oh 102 which was the crash part of the tech boom as well.

Alex Murguia 29:00
Not only that, Bob, I don't know what it was from Oh, eight but it took a while from Oh, one after the because it wasn't just the tech crash. Remember, there was 911 which then call it was brought to light that that bounce back but there was remember the Enron there was a whole bunch of corporate malfeasance that for good, we're

Bob French 29:21
double checking this this statement as I'm making. I'm pulling out my spreadsheet, but yeah, from Oh, three through Oh, six. That was unified republican government. Yeah. And

Alex Murguia 29:33
that's it. Bad luck. I mean, they were no one trusted corporate balance sheets for a good year. It was one of these where people didn't know how to price assets. Yeah. And that, you know, it just so happened, you know, good news, Republicans are in power, but

Bob French 29:48
Athens happens, you know, a year or two earlier, we can be talented, at least a slightly different story. Yeah, it just how all of this stuff falls out and you know, the unknown Line point is that the President and Congress, you know, don't necessarily have control of the markets.

Alex Murguia 30:09
But Bob, what about, you know, these general policies where I'm broad brushing here and you know, a personal political affiliation, I really am straight down the middle, frankly, I kind of apolitical to a large extent. But what happens if someone says, How could this be Bob, it's clear that the Republicans are so pro business and, you know, low tech, you know, that kind of stuff, like the general high level things? Yeah. How could that be? You know, how could you have such a disparity between a Republican president and a Democratic president, I get the whole lag, I get the whole this or that, but it should be a blowout, why isn't it

Bob French 30:49
Its expectations? It's, you know, everyone? Well, at least the market knows, you know, Republicans are supposed to be better for the economy than Democrats. You know, they know that Democrats are supposed to raise taxes or, you know, whatever it might be, you know, whether those are actually true statements or not, you know, that's kind of what the

Alex Murguia 31:09
caveat when we're talking like this to make the examples.

Bob French 31:13
Exactly. But, you know, it's that's already priced in, that's already in everyone's models of what's going to happen. If, you know, the Republicans win the election, or if the Democrats win the election, that's kind of already baked into what everyone thinks the world will look like, in these two different scenarios.

Alex Murguia 31:38
But Bobby already did a lag shouldn't that then change the lag score?

Bob French 31:42
It did to a certain degree? Absolutely. We saw that premium come down, relatively significantly, didn't get rid of it. You know, what I would say is that, you know, in a perfect world, you know, we wouldn't see any difference between the parties. You know, I don't think there's, you know, a, I can't come up

with a good, substantive, risk based reason for Democrats to have higher returns, meaning that there's a higher level of risk for a Democratic president. But we're dealing with really random numbers, there's going to be a difference in almost every situation. You know, I think that's to a large degree, what's happening here. Same reason we're seeing for tall presidents or left handed presidents.

Alex Murguia 32:38
Do you remember offhand what how much the premium shrinks to it went from five to 3 to 2?

Bob French 32:44
Let me pull that up. Also, real quick. where

Alex Murguia 32:47
I'm going with this is okay, that that reduces it that can that snap to controls is too strong a word, but it's somewhat controls for the lag, the sort of the expectation piece that you're talking about. And then the other, the other, whatever, whatever is leftover is just pure noise because of the economic cycle that they happen to be elected in?

Bob French 33:05
Yep, absolutely. I don't remember what the what the lag dropped to or what the premium dropped to with the lag. But it was definitely reduced, but it was still statistically significant. So purely by chance, it's unlikely we would have gotten those numbers. But that's not necessarily impossible. That was by chance. But your point, there is very well taken that there's a lot happening here.

Alex Murguia 33:37
A lot more of the variables that play in here. Yep.

Bob French 33:40
And actually, that kind of gets to something I was talking about. In the article I just wrote, you know, on the midterm elections, one of the things that popped out was that, you know, in yours, excuse me, I'm trying to think where we are in our notes here. But, you know,

Wade Pfau 34:04
moving away from the political parties, it's just if you divide all the historical years, years with the midterm election years with a presidential election, and then the other rest than non election years. Yeah. So another set of interesting results come out of that.

Bob French 34:19
Yeah. But know where I was going with that was when the party in power switches. You know, within an election year where the party in power switches, the market had a much, much lower return than during an election year where it didn't switch. And, you know, then that obviously brings up the question of causation. You know, did the fact that, you know, the presidency went from Republican to Democrat, does that mean the market went down? Or, you know, is it really kind of this this third thing, the economy wasn't great, which meant that the stock market had a bad year. but it also meant that, you

know, the person running or the who is the president lost the election. You know, there's there's a lot of stuff that just happens, and you know, isn't necessarily what's causing the outcome.

Wade Pfau 35:18
Okay, there could be some effective throw the rascals out type of situation, we

Bob French 35:24
I'd argue that that's, you know, kind of the third effect that the market is reacting to the economy. And the election is also acting the economy. And that situation is not the election reacting to the market necessarily, though, that will obviously get dragged in.

Alex Murguia 35:41
Okay, so the takeaway from in terms of Republican Democrat, House Divided house not divided, you know, any iteration you can think of it? I'm going to try to sum it up, correct me here is Democrats seem to have the lead. But there's too much noise to really identify why that is the case. I mean, that's kind of a sense, because you make this because you can make the same statement with presidents over six feet, or left handed presidents. And so there's, there's too many potential artifacts that that can play into it, especially since the market is pricing things in the future. And so it kind of is what it is. And they're variables that have an extraordinary amount of sway. Beyond just political affiliation with regards to stock market success. Is that kind of the vibe?

Bob French 36:31
Yeah, I think that's a pretty good way of summing it up. There's a lot of stuff going into this. And what we're looking at, at least in terms of the mark, are kind of pretty gross levers.

Alex Murguia 36:43
Okay, so then I think Wade was getting to this next point, which is, Okay, forget, Democrats, Republicans or anything like that. election years versus non election years midterms or, you know, whatever, all that kind of stuff. What, what do you find? Because the you do see this, you see this on CNBC all the time that, oh, it's an election year in an election year, XYZ happens. Yeah. And, you know, I find that just idiotic, frankly, a reason but I don't know, maybe I'm the one that's an idiot. What do you find? Well, for those, please don't email me.

Bob French 37:18
They say they're gonna have to give something right, eventually, you know, but one of the things we do see when we actually start pulling apart the data is that election years, and especially midterm election years, have lower returns than non election years. You know, just put some numbers around again, just using the s&p 500. You know, since 1926, through 2021, non election years, were a little bit over 14 and a half on average per year, presidential election years, the average annual return was about 11.6. And midterm election years was all the way down at 8.6. So something seems to be happening, that, you know, the market for whatever reason, isn't doing as well. Now,

Alex Murguia 38:13

Okay, but not, but this is a midterm election year. Do you think that has anything to do with the market being done? How it is this year? I don't know. So this kind of their spurious kind of things, actually.

Bob French 38:30
And, you know, there's, I think that there's a lot of stuff that happens that we can't kind of have a good story around as much as we want that good story, just because we can run some numbers doesn't mean we can find the answer.

Alex Murguia 38:46
In fact, I would say, if you look at this is me, anecdotally. So please correct me. But if someone were to ask me, based on what I hear on the news, do the stock markets Perform Well, during an election year for the president or not? I would have said yes. Because you always hear this sort of, oh, it's an election year. So the President is going to make sure that XYZ doesn't happen. Can How are the is he's going to somehow have a secret meeting with the Fed, and they got to make sure that they don't get, you know, bamboozled in this election cycle, you know, things like that. When you actually see if I'm looking at your numbers, no election is 14 and a half, then the year of a presidential election is 11 and a half, you kind of I would have I would have guessed the other way.

Bob French 39:30
I would have, if that's what I expected as well. You know that. And then looking at volatility, which is actually something I get into my article on it that we just put out a little while ago, is that the volatility of the average annual returns of midterm election years is significantly lower than the other years. So we get into that whole conversation around. Well, how much can you actually trust these statistics does? How do you evaluate this? Does this truly make sense? But what was really interesting to me is, you know, when we start looking at these numbers, you know, what do they tell you about how you should be investing? What do they tell you about how you should be managing your portfolio? Do they tell you anything? You know, should he be setting out every other year, you know, to avoid election year, she'd be sitting out every fourth year to avoid the midterms or whatever the case might be? Well, I mean, to do that, we kind of have to look at the alternatives. You know, kind of in that spirit of the election, you got to figure out what you can actually do with the options available to you. So a quick and dirty way of checking this out is, what did the bond market do? What, just so we have long term data here, I use five year treasuries, you know, how did they perform, you know, during, you know, those three categories, midterm presidential and non election years? Well, actually kind of the reverse.

Alex Murguia 41:03
Bhandari just said real quick, what's the size discrepancy between the bond market and the stock market? Because I think

Bob French 41:11
all the way through. Right now, it's about the bond market is about twice as big as the stock market in terms of market capitalization. And if I had to guess, that just got, or the stock market has gotten bigger relative to the bond market through time. So I'd imagine the multiple back in 1926, was even bigger than it is right now. But, you know, the bond market, again, five year treasuries, just as a quick and dirty proxy with really good data history, during midterms, was almost six and a half per year, are averaged

almost six and a half per year 6.46. The presidential election was five and a half. And the no election years, was down at a little bit more than four and a third. You know, so one of the things we're seeing is that basically, the equity premium in midterm elections is really small, or during years with midterm elections that

Alex Murguia 42:15
mean equity period premium,

Bob French 42:18
basically how much the market is paying you to hold stocks over how much it pays you to hold bonds. So

Alex Murguia 42:25
So as an example, in this example, the midterm was 8.6. The first stocks, the midterm for bonds was 4.4 was 6.4. Let's say 6.5. Right? So 8.5 minus 6.5. To make it easy, is to read it's a 2% percent.

Bob French 42:43
You're right. Yeah, so you got paid by, there's a little bit more to it than that, since we're looking at five year treasuries, but call it you got paid 2% To hold stocks, rather than bonds. Whereas if we're looking at the no election years, when, you know, the stock market was returning on average call it four and a half. The bond market was up sorry, 14 and a half, excuse me, the bond market was returning call it 4.4. Well, now we're talking about a premium of a little bit more than 10%. You know, that's the premium. That's how much the market is paying you for holding stocks rather than bonds. You know, so what do you do with that? You know, how do you think about how that should impact your portfolio? Are you getting close to or are you in retirement? Well, investing during retirement is a little bit different than during your working years. Your investments are there to help you pay for retirement, and now is when they need to earn their keep to make sure you're on the right track, download retirement researchers eight tips to becoming a retirement income investor by heading over to retirement researcher.com/eight tips, again, get retirement researchers eight tips becoming a retirement income investor by going to retirement researcher.com/eight tips. That's the number eight tips. And, you know, that's a really tough question to answer because there's really getting to how do you value risk within your portfolio and something obviously, we talk a lot about the broader kind of how do you value risk within your plan that we're talking about within your portfolio, which is part of your plan. But what I would argue is that, I don't know that it has that much of an effect. I don't know that for most people. It should really be moving the needle and how you allocate your portfolio. You know, certainly I wouldn't advocate you know, jumping in and out of stocks every other year. Are every four years? Yeah, there's tons of volatility in there.

Alex Murguia 45:04
I would say it. The good news is it's still a positive premium. Yes. So it's like, you know, I mean, it is what it, you know, capture your role as an investor is not to guess but to capture the returns?

Bob French 45:19

Yep, absolutely. So, yeah, there's, like I said, there's tons of volatility, you know, there's been, you know, a bunch of really, really good midterm years, there's been some pretty bad midterm years in terms of the market. But to Alex's point, yeah, it's still a positive expected return, you're still getting paid, you know, to a less less amount than in non election years, but you're still getting paid to hold stocks. And, you know, one of the big things I always think about is, again, what's the alternative? You know, if we were to adjust our portfolio, would we actually be better off? And for some people who are thinking very, very, very carefully, about you know, how to allocate that risk budget? Maybe there might be, you know, some advantage and kind of tamping down your equity exposure in those particular years? I don't think any of us, you know, Wade, maybe, maybe you do, I don't, at least I do not. Think about it in those fine of terms, I don't think we're capable of dealing with risk. At that level, there's just too much randomness, it's too much noise in the equation.

Wade Pfau 46:35
Right. And looking forward, I wouldn't really ever want to assume a 10% risk premium on forward looking expectations. So it's, there's not much actionable content there. The only thing looking at these numbers to it, and Alex had brought up this point, which is just with the lowest returns on bonds and the non election years, that might imply that it's not election years where we raise interest rates, and that actually stocks and bonds and in maybe during election years, whether midterm or presidential, there's not a tendency to raise rates, maybe even a tendency to decrease rates, although certainly not this year. And that may not work that way. So yeah, this year is not the data. So this year is gonna hurt that midterm number, because its going to be an outlier

Alex Murguia 47:28
but But it's good from the standpoint of, you know, I think I can safely say, what's happening this year in the markets has, it doesn't seem to me, you know, anecdote is not evidence, but it doesn't seem to me that it has to do with a midterm cycle, as opposed to just, you know, what we've experienced in the last three, four years or so I call me crazy. That's my hunch.

Bob French 47:55
Right, would increase inflation, you know, increased inflation. So yeah, no, and I think that's probably true. If we were to go back and look at, you know, every midterm every presidential shoot, any year with a bad return, whatever its election status was, you know, we can point to specific things that, you know, likely influenced what those returns look like. But a crucial thing is we couldn't have said what those things were likely to be beforehand, we couldn't have predicted what that would have been, look, what next year will look like, at any point in time.

Alex Murguia 48:37
And Bob, one of the one of the things as we're nearing the 45 minutes, that's our sort of cue to kind of start winding this down. One of the things, you know, we want to do with the podcast, as when you myself and Wade got together was the practical applicability. You know, we wanted to get away from, you know, just sermons and things like that, but putting things in practical application. And to me, this is one of these episodes, that it's one of those their sins of commission and sins of omission, you know, kind of thing. And this is where we don't want you to do something, simply because of you think there's going to be some outcome based on the election. Look, I have friends, that, you know, as you get older,

you get more political and see live, you know, it's almost like they've switched from following sports, to following politics, and it's become an obsession. It really has. And it's like a rite of passage when you get to a certain age, I guess. And and they're obsessed with this and how it's going to affect the market. And as much as I want to say, don't worry about it. I mean, there's it's kind of like there's many things, you know, under the stars that are jumped up and your philosophy kind of thing. It seems to me that based on this that you can't really get any true signal from any election result even though you may say to yourself Well, Republicans have this kind of economic proclivity. And Democrats have this kind of economic proclivity, if the data just doesn't bear it out, no matter how much you want to sort of see the conceptual underpinnings, that the data actually has a lot of noise, because the the economic cycle in which you're elected the President, to bring president in, carries to me a lot more weight. I don't know. I'm just so my, my kind of end game is, don't worry about it. It doesn't kind of matter. And, you know, I realized the irony of we sat here for 40 minutes, talking about numbers to then say, these numbers don't mean a damn thing. But the reality is they don't, on many levels

Bob French 50:42
I would actually phrase it the exact opposite way, coming to the same point.

Alex Murguia 50:51
Bob, you're right handed.

Bob French 50:53
That's right. But I'm taller. As long as we get that out there.

Alex Murguia 50:57
All right. But you're uglier.

Bob French 51:00
I got nothing to respond with on

Alex Murguia 51:02
that one. Wade, Wade, please, can you be an arbeiter

Wade Pfau 51:05
Arbeiter here, who is more handsome.

Alex Murguia 51:09
Sorry Bob, go on

Bob French 51:09
So these numbers mean, a lot is just what? What do they imply for how you move forward. And what they imply is that you need to stick with the plan, you need to kind of keep with that long term focus. What this is showing us is that there's a lot of stuff happening, that we have no way of predicting, there's a lot of stuff happening in the market. That, you know, is, to a certain extent, random, you know, but even with all of that randomness, we still can understand the fundamental risk and return

characteristics, we can still profit off of those relationships that we can build our portfolios around. So even with all of this stuff happening, you know, the song remains the same, you know, there's still references to hear. It gets us to the same sort of place, but in a I think, philosophically different manner. Wade, are we just leaving Stairway to Heaven?

Wade Pfau 52:26
Entered the outdoor

Alex Murguia 52:28
trying to work in When the Levee Breaks? Nothing? I had nothing.

Wade Pfau 52:33
Yeah, you've got to wrap this in through the door to not go over 15 minutes. Which is too late. But no, I think yeah, it's this is more than just a conversation at a cocktail party. But at the end of the day, it's also there's not a lot of actionable content here. Just stay the course. And yeah, there's some interesting statistics you can glean from looking at the data. And it's statistically significant, but at the same time, it's not necessarily something that would persist or is actionable, or there's not necessarily any theory behind why the results are as they are. It's left handed presidents and so forth are pretty clear examples of you can find correlations that don't always have they just happen to occur without any underlying causation. Okay, and that's ultimately a lot of where we are here.

Alex Murguia 53:36
Well, Wade, you know, it just hit me and Bob and I'll finish it with this. I swear. We've come full circle as a show. We've reached Seinfeld status podcast about nothing

Wade Pfau 53:58
no, no, that's doing great work. No.

Alex Murguia 54:05
Thank you way that Seinfeld was the show but nothing, you know. Okay, just to make sure. All right.

Wade Pfau 54:15
I get your cultural movie so much, but with not with your 1970s movies.

Alex Murguia 54:25
Then we can do the long kiss goodbye. All right. All right, everyone. Thank you so much, Bob. Take us away, man.

Bob French 54:36
Thank you guys for having me on. It's it's always fun to talk about this type of stuff. And yeah.

Wade Pfau 54:44
Okay, thank you, Bob. And we'll have you again, very soon to explore some other investment related content that will be more actionable.

Bob French 55:00
Wade and Alex are both principals in McLean Asset Management and Retirement Researcher. Both are SEC registered investment advisors located in Tyson's Virginia. The opinions expressed in this program are for general informational and educational purposes only, and are not intended to provide specific advice or recommendations for any individual or on any specific securities. To determine which investments may be appropriate for you, consult your financial advisor. All investing comes with the risk including risk of loss. Past performance does not guarantee future results.