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SUMMARY

- Riverfront believes the results of this election will have less long-term stock market impact than commonly believed.
- Under US 'Economic Exceptionalism,' economic and earnings growth tends to shine through, regardless of political regime.
- We believe markets dislike the unknown...but tend to recover quickly after political uncertainty clears up.

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'Profit Over Politics'

Why US 'Economic Exceptionalism' Works Under Either Party

From now until November 5 — and perhaps for some time after — good luck having a conversation about any topic other than the US Presidential election. By most admissions, the race is too close to call. As of publication time, Real Clear Politics pre-election polling puts the lead for former President Donald Trump in swing states at well under the 3.4% threshold that CNN estimates as polling error 'noise.' Congressional races — which generally have fewer polls from which to draw conclusions — appear just as close and thus next to impossible to call. The good news is Riverfront believes the results of this election will have less long-term market impact than the news would lead you to believe.

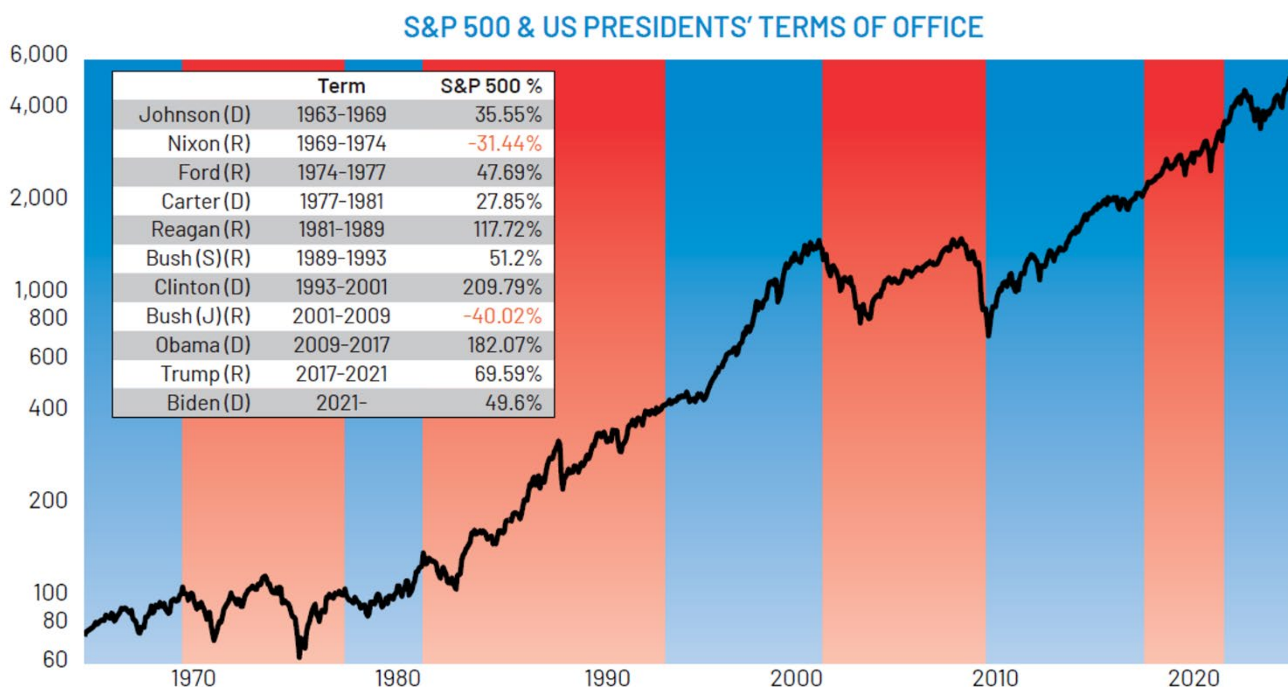
US 'Economic Exceptionalism' Matters More Than Politics

Elections tend to bring out the strongest of emotions in citizens...particularly in an uncertain and politically polarized environment. While this is understandable, we urge investors to check their personal emotions concerning politics at the door when it comes to making portfolio decisions. In our opinion, Presidential politics rarely has the effect on stock market outcomes that many expect. Instead, in our view, corporate earnings trends and interest rate direction predominantly drive intermediate-term stock prices. US corporations have a history of successfully adapting to changing environments.

While new administration policies can be disruptive at first, US companies typically figure them out. This is at the heart of US 'Economic Exceptionalism' — Corporate America's unique, world-class combination of innovation, dynamism, and flexibility that we have written about here.

US Economic Exceptionalism is 'bipartisan,' in the sense that economic and earnings growth tends to shine through, regardless of political regime. This is borne out in the historical record. Since the start of the S&P 500 in the mid-1950s, only two Presidents have presided over negative index returns (see Chart 1, below). In both instances, external factors (the Arab oil crisis, tech's collapse and a historic financial crisis) played a significant role. More recently, stocks fared exceptionally well under both the Trump and Biden/Harris presidencies, confounding critics of both political regimes. Given our positive current views of both the US economy and corporate earnings trends, we expect this recent uptrend in US markets to continue — regardless of what happens on November 5.

Chart 1: S&P 500 Has Performed Well Under Either Party



	Term	S&P 500 %
Johnson (D)	1963-1969	35.55%
Nixon (R)	1969-1974	-31.44%
Ford (R)	1974-1977	47.69%
Carter (D)	1977-1981	27.85%
Reagan (R)	1981-1989	117.72%
Bush (S)(R)	1989-1993	51.2%
Clinton (D)	1993-2001	209.79%
Bush (J)(R)	2001-2009	-40.02%
Obama (D)	2009-2017	182.07%
Trump (R)	2017-2021	69.59%
Biden (D)	2021-	49.6%

Source: LSEG Datastream, RiverFront. Data daily as of September 30, 2024. Note: Price Return shown only. Chart shown for illustrative purposes only. Past performance is no indication of future results.

Why Political Gridlock is Usually Good for Stock Markets

We have the US Constitution to thank for limiting the power of any individual or political party through our three-branch government system and Presidential term limits. This is not to say that politics does not matter… political policy that meaningfully impacts economic policy can affect markets. However, a President rarely has the mandate from Congress to enact the full extent of their intended policies, even with a legislative majority. Regardless of the composition of the government, the market's exceptional earnings engine tends to take center stage — 'profits over politics,' we might say. But since a full sweep by either party cannot be ruled out, we think a fair, non-partisan method of handicapping the potential market impact might be to highlight the most likely effects of such a sweep.

Under a 'Red Wave' Scenario…Focus on Inflation and Interest Rates

As we wrote about in our 'Trumponomics' series earlier this year, our best guess is that Trump's economic policies, if enacted in full, would likely cause both US nominal GDP growth and inflation to rise, along with the value of the US dollar and long-term interest rates, in our view. At this time, we do not see a repeat of 1970s-style inflation as a result, as the current Fed is more vigilant and US energy supply is in a much stronger position than in the seventies. Thus, we think a GOP sweep scenario can support positive gains in stock markets, particularly in the U.S.

- **What We Would Worry About Most in a Red Wave:** Broad use of tariffs could create higher inflation and uncertainty…potentially harming valuation multiples. We will also watch Presidential rhetoric surrounding the Fed; we believe the Fed's assumed political independence is an important component of the US market's premium valuation.

- **Possible thematic beneficiaries:** Small-capitalization US companies which disproportionately benefit from corporate tax cuts, financials, US energy, US-centric companies, gold, value sectors.
- **Sectors that may be disadvantaged:** International stocks, China assets, multinationals reliant on offshoring and/or with large international revenue exposure, US longer-maturity government bonds.

Under a 'Blue Wave' Scenario…Focus on Taxes and Business Sentiment

Under a Vice-President Kamala Harris win, along with Democrats gaining control of both houses of Congress, the biggest changes we would expect to see relative to President Biden's current platform would revolve around increases to taxes for corporations, wealthy individuals, and investors. All else equal, we feel increases to corporate taxes tend to have a direct, negative effect on earnings. However, with an easy monetary and fiscal backdrop to support business investment and consumer spending, we expect US stocks would continue their winning ways over the next few years under Harris.

- **What We Would Worry About Most in a Blue Wave:** Increased regulation and higher corporate tax regimes could damage corporate earnings and business sentiment; investment-related taxes could hurt after-tax returns and wealth transfer.
- **Possible thematic beneficiaries:** Infrastructure spend beneficiaries, renewables, and green energy.
- **Sectors that may be disadvantaged:** Highly taxed utilities and consumer stocks which benefited disproportionately from the 2017 tax cuts, US oil and gas, pharma due to potential regulation.

What Happens if We Don't Know the Election Outcome for a While?

With a race this close, we should expect that we may not know the results as soon as we would like. There could be a challenge to the results by the losing party in either political scenario. Congressional results may take an especially long time to tally — for instance, even in a 'normal' election, we may not know the House of Representatives' results for weeks.

In general, we believe markets dislike uncertainty, but also tend to recover quickly after political uncertainty is cleared up, regardless of who wins. But what about the potential for social unrest to follow a contested election? It is worth noting that during and after the 2020 election, the S&P 500 rose fairly consistently from Election Day to Inauguration Day the following January, despite significant political turmoil surrounding election results.

Conclusion: 'Profits Over Politics'…and 'Process Over Prediction'

Elections tend to bring out the strongest of emotions in citizens. What can be lost in the noise is our view that, generally speaking, the structural advantages that the US enjoys — what we have termed as US 'Economic Exceptionalism' — will likely persist regardless (and often in spite of) who holds political office. In uncertain times like these, it is also worth noting that our investment team's motto is 'Process Over Prediction.' Our process is to reassess our views as new information comes in and act accordingly, if necessary. Should our internal view of risks related to the election outcome increase significantly, our risk management process allows us to be nimble with regard to portfolio construction.

Risk Discussion: All investments in securities, including the strategies discussed above, include a risk of loss of principal (invested amount) and any profits that have not been realized. Markets fluctuate substantially over time, and have experienced increased volatility in recent years due to global and domestic economic events. Performance of any investment is not guaranteed. In a rising interest rate environment, the value of fixed-income securities generally declines. Diversification does not guarantee a profit or protect against a loss. Investments in international and emerging markets securities include exposure to risks such as currency fluctuations, foreign taxes and regulations, and the potential for illiquid markets and political instability. Please see the end of this publication for more disclosures.

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All charts shown for illustrative purposes only. Technical analysis is based on the study of historical price movements and past trend patterns. There are no assurances that movements or trends can or will be duplicated in the future.

Stocks represent partial ownership of a corporation. If the corporation does well, its value increases, and investors share in the appreciation. However, if it goes bankrupt, or performs poorly, investors can lose their entire initial investment (i.e., the stock price can go to zero). Bonds represent a loan made by an investor to a corporation or government. As such, the investor gets a guaranteed interest rate for a specific period of time and expects to get their original investment back at the end of that time period, along with the interest earned. Investment risk is repayment of the principal (amount invested). In the event of a bankruptcy or other corporate disruption, bonds are senior to stocks. Investors should be aware of these differences prior to investing.

In general, the bond market is volatile, and fixed income securities carry interest rate risk. (As interest rates rise, bond prices usually fall, and vice versa). This effect is usually more pronounced for longer-term securities). Fixed income securities also carry inflation risk, liquidity risk, call risk and credit and default risks for both issuers and counterparties. Lower-quality fixed income securities involve greater risk of default or price changes due to potential changes in the credit quality of the issuer. Foreign investments involve greater risks than U.S. investments, and can decline significantly in response to adverse issuer, political, regulatory, market, and economic risks. Any fixed-income security sold or redeemed prior to maturity may be subject to loss.

Index Definitions:

Standard & Poor's (S&P) 500 Index measures the performance of 500 large cap stocks, which together represent about 80% of the total US equities market.

A small-cap stock is a company with a market capitalization between $250 million to $2 billion. The precise figures used can vary among different brokerages, so this is a guide to their classification.

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Dividends are not guaranteed and are subject to change or elimination.

Gross Domestic Product (GDP) is the monetary value of all finished goods and services made within a country during a specific period. GDP provides an economic snapshot of a country, used to estimate the size of an economy and growth rate.

Technology and internet-related stocks, especially of smaller, less-seasoned companies, tend to be more volatile than the overall market.

Definitions:

In a rising interest rate environment, the value of fixed-income securities generally declines.

Inflation is a gradual loss of purchasing power, reflected in a broad rise in prices for goods and services over time.

Investing in foreign companies poses additional risks since political and economic events unique to a country or region may affect those markets and their issuers. In addition to such general international risks, the portfolio may also be exposed to currency fluctuation risks and emerging markets risks as described further below.

Changes in the value of foreign currencies compared to the U.S. dollar may affect (positively or negatively) the value of the portfolio's investments. Such currency movements may occur separately from, and/or in response to, events that do not otherwise affect the value of the security in the issuer's home country. Also, the value of the portfolio may be influenced by currency exchange control regulations. The currencies of emerging market countries may experience significant declines against the U.S. dollar, and devaluation may occur subsequent to investments in these currencies by the portfolio.

Foreign investments, especially investments in emerging markets, can be riskier and more volatile than investments in the U.S. and are considered speculative and subject to heightened risks in addition to the general risks of investing in non-U.S. securities. Also, inflation and rapid fluctuations in inflation rates have had, and may continue to have, negative effects on the economies and securities markets of certain emerging market countries.

Interest rate sensitivity is a measure of how much the price of a fixed-income asset will fluctuate as a result of changes in the interest rate environment. Securities that are more sensitive have greater price fluctuations than those with less sensitivity. This type of sensitivity must be taken into account when selecting a bond or other fixed-income instrument the investor may sell in the secondary market. Interest rate sensitivity affects buying as well as selling.

Unrealized capital gain refers to the increase in value of an investment or an asset that an investor holds but has not yet sold. These gains are "unrealized" because they exist only on paper; they only become "realized" once the asset is sold.

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