KOVITZ INSIGHTS

Racing Towards November

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As the 2020 presidential election campaign heats up and polls show Joe Biden holding a lead of 7.5 points (49.2% to 41.7%) over President Trump, while the betting odds suggest a tighter spread, we must caution that the race is far from over. Indeed, pollsters and oddsmakers are hardly infallible as just four years ago, Hillary Clinton led Donald Trump in the presidential race by four or five percentage points one month before Americans cast their ballots. Market historians, and perhaps everyone, should be thrilled to see the page turn to 2021, even as the winner of the Oval Office will still be dealing with COVID-19, as well as political and economic uncertainties.

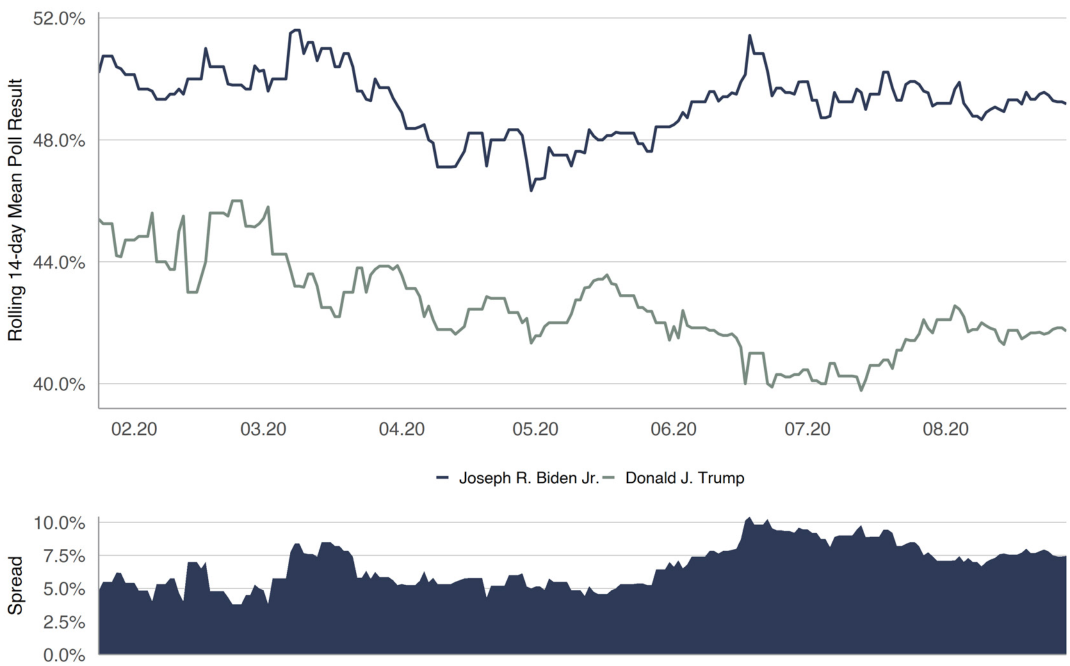


Figure 1: Presidential Polling
From 01.11.2020 through 08.31.2020. Rolling 14-day average poll result. Source: Kovitz using data from RealClearPolitics.

No doubt, COVID-19 and more than 175,000 U.S. deaths now attributed to the disease, not to mention the economic fallout from the Great Lockdown and efforts to control the pandemic, have not helped President Trump. While there has yet to be a presidential debate, there will be plenty of news on health and wealth between now and Election Day. We realize that some investors are concerned that a Biden victory could hit them in the pocketbook, but Figure 2 shows that Value stocks have performed very well with Democratic control of the White House and Capitol Hill, although it is hard to draw grand conclusions from relatively few data points.

THE STOCK MARKET DOES NOT HAVE A PARTY

Of course, others are worried that a win for the incumbent could also spell trouble for U.S. equities. President Trump has proven to be even more unconventional than initially thought. For example, many businesses benefited from a significant corporate tax cut and reduced regulation, even though shifting views on trade and tariff skirmishes have made it difficult for companies to make long-term planning decisions. We do not mean to suggest that a President Hillary Clinton would have proved better for equity markets, nor do we give much credence to today's assertions that a President Biden would take a more aggressive COVID-19 stance, whatever that means, that would somehow ensure more favorable medium-to-long term domestic growth at the expense of shorter-term prospects.

Despite President Trump's colorful governing style, it remains challenging to attribute rising or falling markets to individual presidents, their parties, or the makeup of Congress given the multitude of factors that drive performance. Historical evidence suggests that performance is very much a mixed bag, with investment success as dependent on the equity category as a political party. Despite trials and tribulations along the way, Figure 3 shows that the U.S. stock market has been better off at the end of eleven of thirteen presidencies since World War II, Richard Nixon and George W. Bush the exceptions.

Figure 2: Parties in Power & Annualized Returns

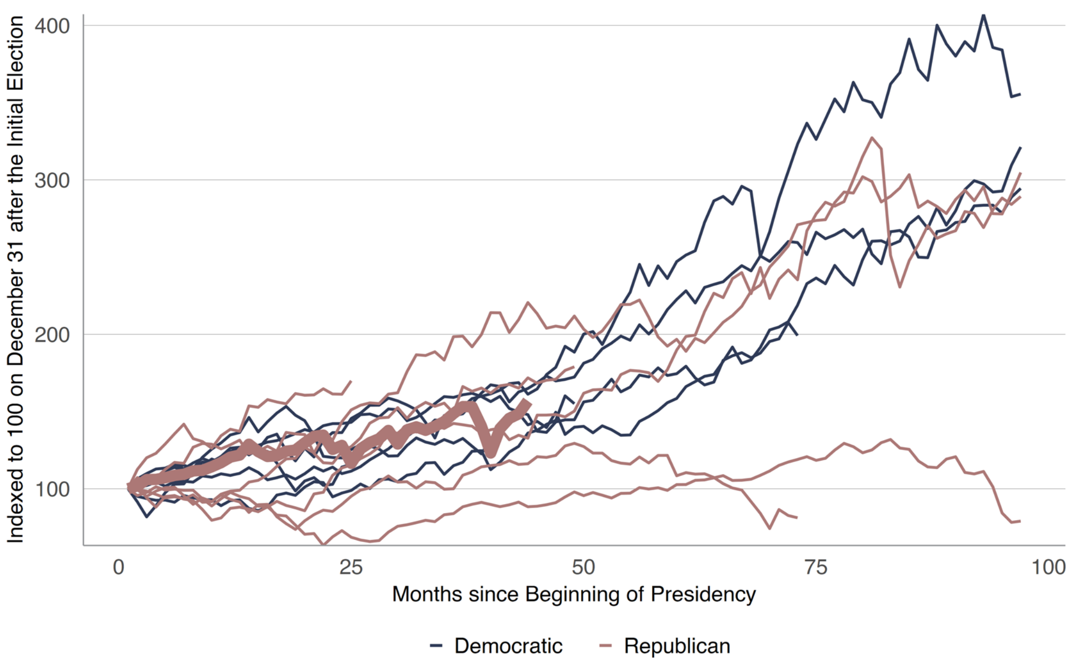
From 12.31.1928 through 12.31.2018. Annualized total return. Performance segregated by presidential and congressional party. SOURCE: Kovitz using data from the U.S. House of Representatives, Morningstar and Professors Eugene F. Fama and Kenneth R. French

Presidential Performance

Presidential Party	Congress Party	Fama-French Value Stocks	Fama-French Growth Stocks	Large Company Stocks	Small Company Stocks
Democratic	Democratic	20.6%	16.5%	12.9%	24.0%
Democratic	Republican	15.6%	9.9%	15.0%	10.4%
Democratic	Split	14.5%	14.9%	15.6%	14.3%
Republican	Democratic	10.7%	6.7%	9.5%	6.4%
Republican	Republican	-2.4%	-4.2%	-2.0%	-4.9%
Republican	Split	10.7%	1.9%	5.8%	5.4%
Democratic President		**19.0%**	**14.9%**	**13.5%**	**20.3%**
Republican President		**6.1%**	**2.0%**	**4.8%**	**2.3%**

Figure 3: S&P 500 Index Performance by President

From 12.31.1944 through 07.31.2020. Total return. President Trump's return is indicated by a thicker line. SOURCE: Kovitz using data from Morningstar, Professors Eugene F. Fama and Kenneth R. French



EQUITY MARKET'S "PRESIDENTIAL CYCLES"

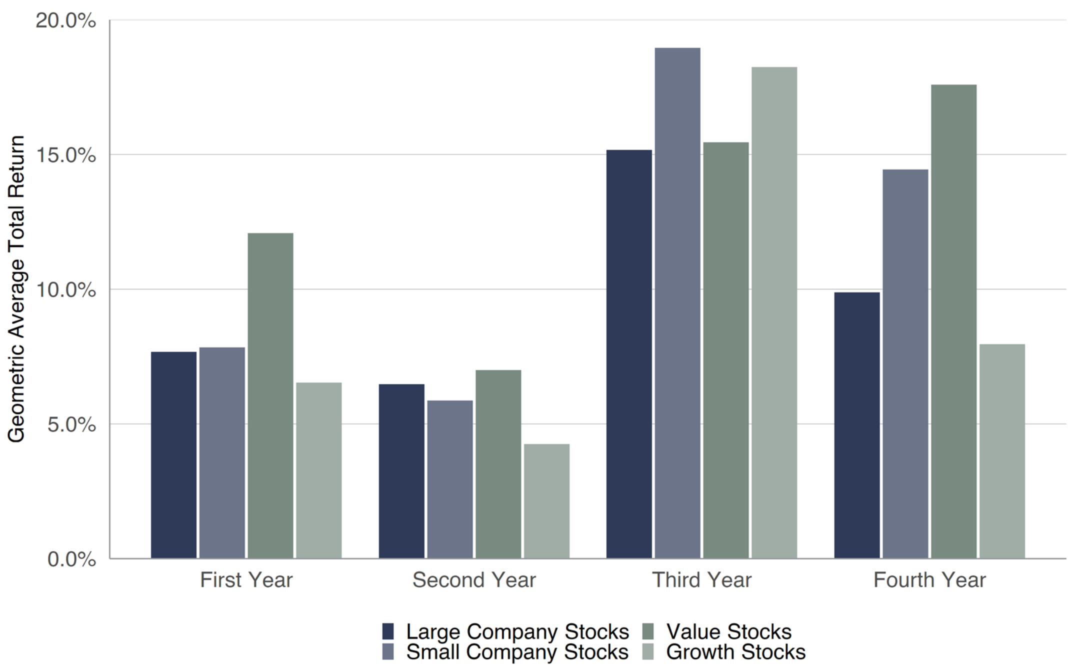
We must always be careful about drawing significant conclusions from a small number of data points, but it is interesting to look at equity market returns in each of the four years of the presidential cycle. Given that the Commander in Chief often makes tough choices early on, while doing everything possible to spur the economy late in the four years to ensure personal or party re-election, we suppose Figure 4 could be unsurprising, with equities on average having not performed as well in the first couple of years of the presidency and much better over the last two years.

The more than 60% price gain for Large Company Stocks, represented by the S&P 500, since Election Day 2016 has been terrific, especially as so many supposed market experts were predicting that a Trump victory would lead to big losses in the equity markets. We'll see what 2021 brings, but nine decades of market history show that the S&P has managed a solid average annual return of 7.7% in the last calendar year of the Presidential Cycle, though 2001's 11.9% drop is a weight on that figure. Happily, Value Stocks have beaten Growth by 5.6 percentage points in the first-year performance derby, while the S&P 500, on average, has achieved similar performance to Small Company Stocks.

We recognize that past performance is no guarantee of future performance or even profitability but market historians who favor Value strategies should be thrilled to see the page turn to 2021, even as the winner of the Oval Office will still be dealing with COVID-19, as well as political and economic uncertainties.

Figure 4:
Equity Performance by Year of Term

From 12.31.1927 through 12.31.2019. SOURCE: Kovitz using data from Morningstar, Professors Eugene F. Fama and Kenneth R. French



OUR VOTE

We believe that we are likely to encounter additional volatility on both sides of the election, as America chooses a direction for the next four years. But Washington is just one of numerous factors that drive stock market gyrations, so we would never recommend major alterations to a long-term asset allocation plan based solely on politics. Therefore, it should come as little surprise that the only endorsement we will offer is in support of a broadly diversified portfolio of undervalued stocks to be held for its long-term appreciation potential, no matter who is in power in D.C.

For more information on working with our financial professionals contact us at wealth@kovitz.com or 312.334.7300.

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The factor-based (book value-to-price) portfolio data is from Eugene F. Fama and Kenneth R. French. The dataset is broken into four groups: large value, large growth, small value and small growth. The aggregate Value and Growth porfolios are monthly averages of the two returns.

The Standard & Poors 500 index (S&P 500) is a broad stock market index based on the market capitalizations of the largest 500 companies listed in the U.S. Small company stocks, via Ibbotson Associates, are the bottom twenty percent of the New York Stock Exchange. Large company stocks, via Ibbotson Associates, are represented by the S&P 500 index.

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