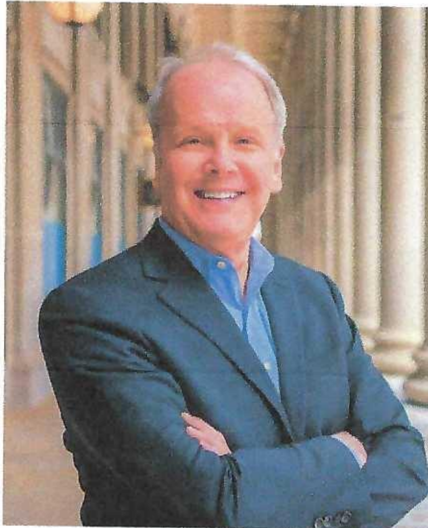

Do Political Parties Really Power the Stock Market?

Conventional wisdom has it that one political party is better than the other when it comes to stock market returns, but a look at historical trends proves otherwise.

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This year, for the first time since 2009, there is a Democratic president, a majority Democratic House of Representatives, and a majority Democratic Senate (not technically but practically, as the two independent senators vote with the Democratic caucus and Vice President Kamala Harris will be called in to cast any tie-breaking votes). Will the changes in power in Washington, D.C. be a positive or a negative for the stock market? In this column, I'll consider the so-called "popular" view, and then see if it holds up to the facts, looking back to our recent and not-so-recent history for clues.

THE POPULAR VIEWPOINT

It's a common exercise to speculate on the influence political parties will have on the stock market. Of course, the popular view—the one that plays to familiar stereotypes—is that Democrats are bad for the market, as they will raise taxes on corporations and individuals then redistribute that revenue to the masses who are not entitled to that money. In this view, Republicans are good for the stock market, as they reduce taxes and cut regulation, providing a better environment for businesses and allowing more money to remain in the hands of those who earned it.

In keeping with this view, it follows that unified government—where the president and both houses of Congress are the majority party—is bad for the stock market when Democrats are in power and is good for the market when Republicans are in power. When government is divided, the impact on the stock market is less predictable. There is another, perhaps more cynical, view that says that the best outcome for the stock market is divided government, as the checks and balances provided by the Constitution will keep one party from doing too much economic harm to the country.

Reality, as one might expect, is more nuanced than that. Let's look to history for actual examples of how administrations have affected the stock market.

ADDING UP THE NUMBERS

From 1929 to 2019, there have been 45 years when one party controlled the presidency and both houses of Congress. According to the Wall Street Journal, the average annual return of the S&P 500 in those years was 7.45 percent. The Democrats were the controlling party in 34 of those 45 years. Under those administrations, the S&P 500 rose 24 times and fell 10 times, for an average annual return of 9.4 percent. Meanwhile, in the 11 years when the Republicans were the controlling party, the S&P 500 rose six times and fell five times, for an average annual return of 1.5 percent.

From 1929 to 2019, there were 46 years when the presidency and Congress were split, one controlled by the Republicans and one controlled by the Democrats. The Wall Street Journal reports that the average annual return of the S&P 500 in those years was 7.26 percent. In 10 of those years, the Democrats controlled the White House and the Republicans controlled both houses of Congress. During that time, the S&P 500 rose six times, fell three times and was unchanged once, for an average annual return of 13.0 percent. In 22 of those years, the Republicans controlled the White House and the Democrats controlled both houses of Congress. The S&P 500 rose 14 times and fell eight times for an average annual return of 4.9 percent. The remaining 14 years featured a split Congress, and the S&P 500 rose in nine of those cycles and fell in five, for a weighted average annual return of 6.9 percent.

WHAT THE NUMBERS SAY

These statistics run counter to the popular viewpoint that has influenced American voters for generations. There is only a modest percent difference in average annual S&P 500 returns during periods of unified government (7.45 percent) and divided government (7.26 percent). The stock market basically shrugs off the impact of an "all red" or an "all blue" government.

When the Democrats oversee a unified government (37 percent of the time since 1929), average annual S&P 500 returns have risen 9.4 percent. When the Republicans oversee a unified government (12 percent of the time since 1929), average annual S&P 500 returns have risen 1.5 percent. When the government is divided (51 percent of the time), as stated previously, average annual S&P 500 returns have risen 7.26 percent.

I believe these statistics are telling us that the determination of investment returns is independent of the power structure in Washington. The simplistic idea that Republicans are good for the market and that Democrats are bad for the market, and the cynical viewpoint that divided government is good for the market, fall apart under closer scrutiny.

So then, who affects the market? I believe the statistics show that the real mover and shaker is the American worker. I see a testament to the American capitalist system, the ingenuity of the American entrepreneur, and the drive of the American workforce, regardless of which political party is in power.

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