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Party control in Washington has offered little clue to bond and stock performance

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Boston - A hardy perennial of pre-election financial reporting is comparing how stocks have fared under past presidential and congressional terms. In that spirit, Eaton Vance widened the scope of study beyond stocks to include major fixed income sectors.

The study includes every two-year period, broken down by "first two years" of presidential terms and "second two years," back to November 1, 1988, the month of President George H.W. Bush's election. We averaged the performance during the six kinds of "like" partisan control for 16 two-year periods: Democrat president / Democrat Congress, Democrat president / Republican Congress, Democrat president / Split Congress, Republican president / Democrat Congress, Republican president / Republican Congress, and Republican president / Split Congress.[1]

Democrats had two periods in which they occupied the White House and both branches of Congress, reflecting first two years of presidents Bill Clinton and Barack Obama. These periods are notable in the data because risk assets like high-yield debt, investment-grade bonds and small-cap equities did substantially better than the average of the other two-year periods.

How markets have fared over two-year periods of Democratic and Republican control
Annualized, 2-year total returns

			First Two Years							
Count	President	Congress	US Treasury	US Agg	Municipal	Investment Grade Corp	High Yield	Broad Equity Market	Large Cap Equity	Small Cap Equity
2	Democrat	Democrat	5.46%	7.34%	7.55%	12.86%	21.04%	12.11%	11.83%	15.48%
1	Democrat	Republican	9.96%	9.11%	8.25%	8.86%	6.88%	23.82%	25.63%	6.78%
1	Democrat	Split	0.67%	1.49%	2.94%	2.63%	7.33%	22.36%	22.45%	21.36%
1	Republican	Democrat	8.94%	9.07%	7.76%	8.44%	-2.03%	5.77%	6.78%	-8.31%
3	Republican	Republican	4.04%	4.23%	4.37%	4.42%	2.90%	2.82%	2.57%	5.98%
0	Republican	Split	-	-	-	-	-	-	-	-
	Average		5.82%	6.25%	6.18%	7.44%	7.22%	13.37%	13.85%	8.26%

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			Second Two Years							
Count	President	Congress	US Treasury	US Agg	Municipal	Investment Grade Corp	High Yield	Broad Equity Market	Large Cap Equity	Small Cap Equity
0	Democrat	Democrat	-	-	-	-	-	-	-	-
3	Democrat	Republican	5.42%	5.89%	5.63%	6.30%	6.68%	15.17%	15.51%	11.94%
1	Democrat	Split	4.21%	5.13%	6.37%	8.00%	8.92%	11.27%	11.44%	9.36%
2	Republican	Democrat	9.39%	7.80%	5.01%	4.66%	8.15%	4.31%	4.09%	8.31%
1	Republican	Republican	3.86%	5.22%	5.57%	9.04%	22.20%	16.38%	15.64%	26.56%
1	Republican	Split	9.86%	9.47%	6.92%	11.59%	5.38%	13.64%	14.52%	1.35%
16	Average		6.55%	6.70%	5.90%	7.92%	10.27%	12.15%	12.24%	11.50%

The Democrat / Democrat periods are two interesting data points, but they also highlight the limits on what we can expect to achieve with this kind of analysis. Here are a few examples:

Limited dataset. To be inclusive of the major fixed income sectors, the analysis includes the newest one: the ICE/BofAML High Yield Index, which started in 1986. A small dataset like this means that "one-off" events like the 2008 global financial crisis will skew the data to a greater extent than with a larger dataset. For example, the above-average Democrat/Democrat performance noted above is pushed upward in all sectors by the powerful market rebound in 2009 and 2010 following the crisis. Obviously, other events like wars and pandemics also skew the data. While there can be debate over the extent to which administration policies influence the impact of such events, larger datasets allow for averaging that would mitigate the skew introduced by any single one.

Unproven causation. The correlation of performance in any given period with presidencies and congressional control doesn't necessarily indicate causation. The policies and market trends of prior periods often play a significant role. To take one example outside the range of our study, former US Federal Reserve Chairman Paul Volcker is widely credited with monetary policies that broke the back of 1970s inflation, helping launch the subsequent decades-long bull market in stocks and bonds. Volcker was appointed by President Jimmy Carter in 1979 and reappointed by President Ronald Reagan in 1983. Both parties can claim some credit, but Reagan's tenure was the first to reflect the positive market impact.

Secular skew. The above example also illustrates how long-term secular trends can strongly influence performance, regardless of party control in Washington. The standouts in our dataset were the two periods of Democrat / Democrat control. But during the prior two periods of Democrat / Democrat control — the Carter years of 1977 to 1980 — US Treasurys had a total return of just 0.87% per year, based on the ICE/BofAML 7-10 year

Treasury Index.

Bottom line: Studying the correlation between partisan control in Washington and financial performance can be informative, but our analysis wasn't designed to guide investment decision making. Clearly, elections have consequences for the economy and markets. But to paraphrase a common caveat, past political alignments are no guarantee of future results.

[1] The 16 two-year periods had no instances of Democrat / Democrat control in the second two years, nor Republican / Split control in the first two years.

Investing involves risk including the risk of loss. An imbalance in supply and demand in the income market may result in valuation uncertainties and greater volatility, less liquidity, widening credit spreads and a lack of price transparency in the market. Investments in income securities may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. As interest rates rise, the value of certain income investments is likely to decline.

The value of investments may increase or decrease in response to economic, and financial events (whether real, expected or perceived) in the US and global markets. The value of equity securities is sensitive to stock market volatility. Smaller companies are generally subject to greater price fluctuations, limited liquidity, higher transaction costs and higher investment risk than larger, more established companies.

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