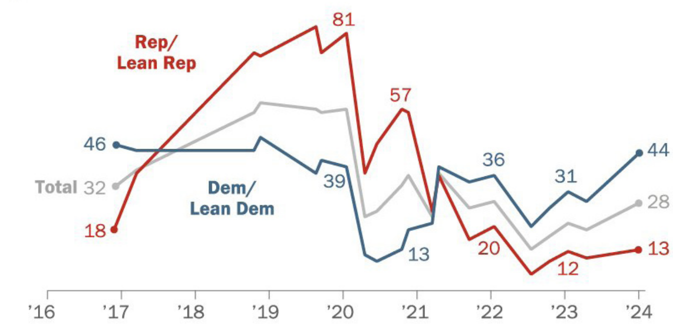
The Perils of a Partisan Portfolio

A Case Study in the High Cost of Mixing Politics and Investing

The highly contentious 2024 presidential election in a deeply divided United States is nearly upon us. Everyone is of course entitled to their political opinions, but there are some acute dangers awaiting investors should they allow those preferences to have too much sway over investment decisions. In the following case study we'll demonstrate why focusing too intently on which party is in power, and the subsequent policy ramifications, can seriously dampen an investor's long-term returns.

Positive views of the nation's economy increase, driven by Democrats

% who say economic conditions in this country today are ***excellent or good***



Source: Survey of U.S. adults conducted Jan. 16-21, 2024.

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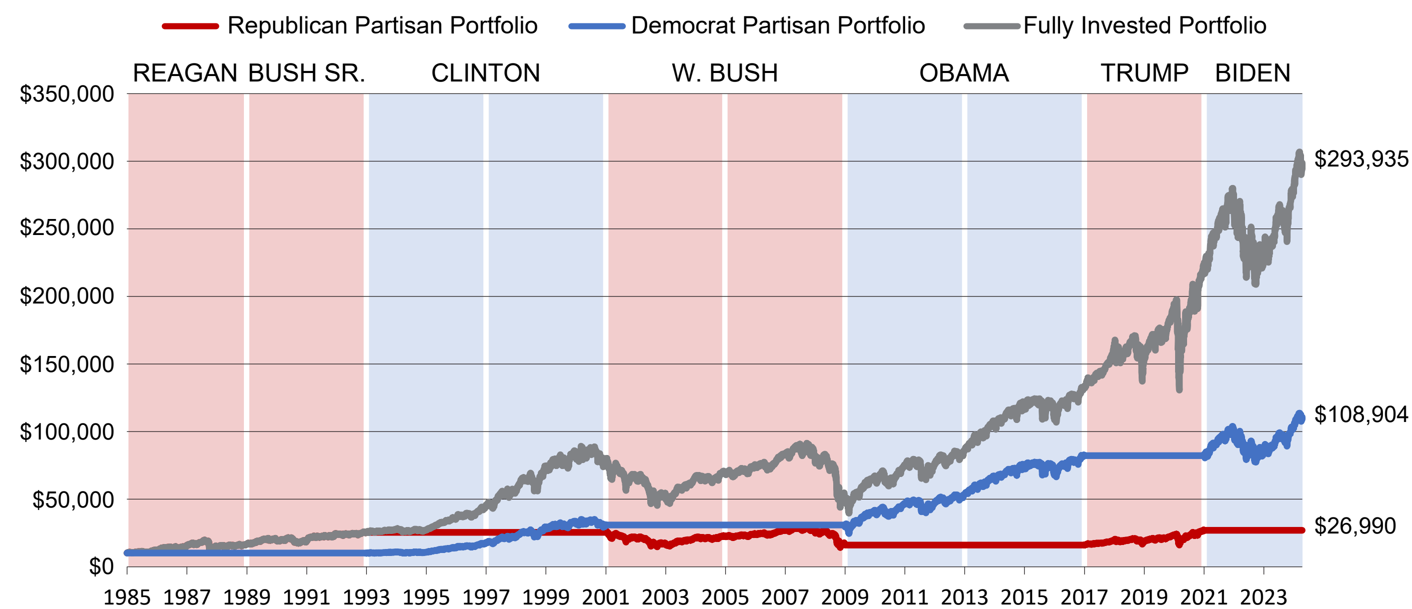
Most investors likely will take into account the economic outlook when making investment decisions. However, the party occupying the White House has dramatic effects on how individuals gauge the strength of the economy. From the Pew Research chart on the right, you can see larger numbers of Democrats reporting the economy as excellent or good as Barack Obama was finishing his second term at the beginning of 2017. Then the flip to Republican confidence during Donald Trump's term in office (Jan 2017 – Jan 2021) and then the flip back to Democrats in early 2021, not coincidentally shortly after the inauguration of Joe Biden. Partisan economic perceptions, however, may not always align with reality.

To test these perceptions, let's imagine we construct a simple investment strategy for a hypothetical partisan investor. When their preferred party occupies the White House, in theory that is positive for the economy, so we'll allocate 100% to equities. When the opposite party is in the White House, in theory that is negative for the economy, so we'll sell equities and go 100% to cash. If our partisan economic hypothesis is correct, we should expect this portfolio to outperform the broader market over a nearly 40 year period. It should capture the majority of the upside while avoiding the majority of the downside. However, the results speak for themselves. A fully invested portfolio beat both of the partisan portfolios by a country mile.

S&P 500® Index Growth of $10,000



Source: FactSet financial data and analytics.

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A few important points about these results:

- The chart covers the 10 most recent presidential terms in office: 5 Republican and 5 Democrat
- The Fully Invested Portfolio made a 9.0% annualized return
- The Democrat Partisan Portfolio made a 6.3% annualized return
- The Republican Partisan Portfolio made a 2.6% annualized return
- For simplicity's sake we ignored taxes and dividends

We would advise against reading too much into the Democrat investor's outperformance over the Republican. The Democrat benefited from some especially fortuitous timing, avoiding major drawdowns in the 2001 and 2008 recessions, and then getting back in the market right at the beginning of the longest bull market in history starting in 2009. Even with this good luck, the Democrat still vastly underperformed a fully invested portfolio.

The moral of the story is we encourage everyone to vote at the ballot box, but perhaps not with your portfolio. While we expect returns to be more muted going forward compared to the recent past, it is our view that the US economy and the US stock market will continue to perform well over the long-term, regardless of who wins in November.

> **If you mix your politics with your investment decisions you're making a big mistake.**
>
> *- Warren Buffett*

Pew Research Center: "Positive views of the nation's economy increase, driven by Democrats." Pew Research Center, Washington, D.C. (01/25/2024) https://www.pewresearch.org/politics/2024/01/25/americans-more-upbeat-on-the-economy-bidens-job-rating-remains-very-low/pp_2024-1-25_biden-economy_00-01-png/.

Warren Buffett quote: https://www.youtube.com/watch?v=56R_tMGRq0M

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