Investment Committee Podcast: The Election Day Effect

Cärin Viertel:

I'm Cärin Viertel, the Director of Client Services at JNBA Financial Advisors here in Minneapolis, Minnesota. We're recording this discussion on Tuesday, October 22nd, 2024. I'm with my two colleagues and members of our Investment Committee, Mark Rosenkranz, an Investment Strategist, and Michael Bilotta, a Senior Advisor and Investment Strategist. Mark and Mike, thanks for being here. We'll dive right in. In talking with our colleagues, we've heard from clients there are probably three primary topics on people's minds right now as it pertains to the markets, one being the upcoming elections, another the Fed and interest rates, and the third, the stock market keeps continuing to hit all time highs. So let's start with the elections, since, believe it or not, they're only two weeks away. Mark, what should investors keep in mind as it pertains to the elections?

Mark Rosenkranz:

Yeah, that's a question we've been getting pretty much all summer long and even in the winter last year. It's been a topic that's been on a lot of people's minds for a long time now. And as you said, we're two weeks away. The thing we've been talking about a lot throughout the year as we head up to the elections, there's two areas that we've been focusing on. The first is that generally in any typical election year you typically see a little bit more volatility heading up to that election day. And fortunately this year that so far has not been the case. Now, there's still two weeks ago, but so far markets have trended gradually upward. There hasn't been too much volatility, which has been a pleasant surprise. It doesn't mean that we're out of the woods yet, and obviously things can happen post-election, but so far so good in terms of how markets have responded to the ebbs and flows of the news cycle.

The other area that we've been focusing on throughout the year is that we are focused on the long-term. And what we say by that is we are not making any investment decisions based on who we think could or could not win, which party will be represented in the House, Senate, Presidency. There really isn't just a lot of convincing data one way or the other of which party is better or worse for markets, and even down to a granular level of which sectors or individual stock could perform better or worse under a certain Presidency or certain House leadership or Senate. There really just isn't a lot of convicting data out there. So we tend to focus on the long-term and that's where we rely on to the topics we'll discussing later of inflation, unemployment, corporate earnings, things that can obviously be impacted by policy. And as we get a resolution post-election day, there will be some tangible policy enacted one way or the other, and that's where we go back to how that impacts the broader economy.

Cärin Viertel:

Oh, great. Thank you for that perspective. Mike, do you have any additional comments or things that we should think about pertaining to the markets?

Michael Bilotta:

Sure. Yes, those are all good points. I think, amazingly, we haven't had the volatility that you typically would see in an election year, especially with the emotionally charged nature of the race that we have going on right now. So it clearly shows that the market, stock and bond market, are positioned more for the Fed and lower interest rates and so on than they are for the election. Now, the old adage is don't invest with your political views because that typically doesn't work.

If you look back over time, there's only one President in the last, let's say, seven administrations that has a negative stock market return, and that's poor George W. Bush who got saddled with 9/11 and the Iraqi war after that, and then also the housing crisis in '07, '08, and '09. And so other than that, Biden, Trump, Clinton, Bush, Reagan, Carter, Ford, you'd have to go back to Richard Nixon to have a negative administrative year as far as the stock market is concerned.

So I mean, if that doesn't show you right there that you shouldn't be investing simply based on who's in the seat of President, I don't know what does. What I do think would create a bit of a anxiety moment would be if one party swept President, the Presidential Seat, the House, and the Senate, because then what we would need to do is to look past just the outcome itself and say, "Okay, what are the policies now that are going to be pushed through with little opposition? What sectors are going to be helped? What sectors are going to be hurt?" But other than that, it's back to the Fed, the economy, earnings, interest rates, all the stuff that you usually invest in and not necessarily the election.

Cärin Viertel:

Yeah. Let's transition to the Fed and interest rates. Last month, the Fed cut interest rates for the first time in four years. Mike, what is the Fed paying attention to in order to help them guide their next decision with interest rates?

Michael Bilotta:

Yeah, the Fed really has one goal with two different mandates. The goal is to promote economic stability, and the two mandates are watching prices and price stability, inflation, and unemployment. And as we all know, for most of the last couple of years, it's all been about inflation. We had 8%, 9%, 10% inflation. The fed raised rates from basically zero to almost 5.5%, caused a lot of dislocations in the market and so on, a stock market sell-off a bond market sell-off, but at the end of the day, they were successful eventually in getting inflation down. And I think now we're in a little bit of a sweet spot, to be honest. Inflation has gotten down into that 2% to 3% range, which the Fed keeps saying 2%, but I think two to three is close enough. And then the other thing that they're watching is the unemployment rate and jobless claims and so on.

Not necessarily what the reading is itself, but is the trend going in one direction or another? So we did see the unemployment rates spike up a little bit here in the last month or two. A lot of that's being attributed probably to dislocations from the tropical storms and so on down in the southeast. And so I think now it depends on, what is the trend going forward as to whether or not they feel like they can proceed slowly to try to get ahead of any economic slowdown, or if they have to go more and more quickly because of too much of a slowdown or a recessionary environment. That would not be a good situation to lower interest rates in. We would obviously much prefer the first one, slow, measured, trying to keep the economy greased, if you will, rather than the quick and large amounts that we've seen before on the upside. Really caused some dislocations and that sort of thing.

Cärin Viertel:

Do you have anything that you wanted to share in regard to economic growth that Mike has already laid out?

Mark Rosenkranz:

Yeah, I think Mike touched on a lot of good points. And the main catalyst for the rate cut that we saw last month was really around the unemployment picture. And right now the underlying data is pointing towards not a lot of firings and not a lot of hiring. So it really is in a unique balance at the moment. And that's where we touch on how these things are all interconnected. That goes back to corporate earnings. And we're sitting here right in mid-October, right in the heart of earnings season and a lot of hiring or firing decisions will be based on corporate profitability. And so we'll get a lot of data over the next couple of weeks, but overall this year, earnings have held in there largely intact. And so you're not seeing big broad-based decisions from various companies on how they're hiring and firing. So it is a wait and see approach, but right now it's at a very balanced equation right now.

Cärin Viertel:

These things seem to be propping up the stock market. Mark, how likely are we going to continue to see these highs in the markets, and what should we be prepared for?

Mark Rosenkranz:

Yeah, I mean, after '22, I think it was a good expectation that things could get a little worse. Things are a little challenging and we saw a really strong performance in 2023, and that would've been a natural time to say, okay, we got everything recovered back. We could be a little dicier in '24. So far this year we're, again, all at record highs. And we get the question a lot of, when's the right time to get into the market and how worried should I be about how things are at all time highs? When's the right time? You take a look back at the company fundamentals, and there's been a lot of concern, especially in this more recent run. Around the Magnificent Seven, the largest seven companies that are driving a lot of the market performance. Valuations are elevated, not historically so, but they're definitely above average.

But it's important to note that these seven companies are also growing the fastest. You look at their earnings growth over the last four quarters, anywhere from 20% to 50% for these top seven names compared to the market down to up 10%. In terms of profitability, the Magnificent Seven, over the last four quarters, their profit margins are sitting around 20%, whereas the rest of the market's up 8%. So these Magnificent Seven companies aren't getting bid up for no reason. It's not necessarily hysteria. They are delivering earnings to back that kind of support, but over the long-term, it's just hard to imagine the law of large numbers not playing some role where they can't keep growing at an elevated rate for a long time. And that's where you really want to see broader market participation from the remaining, not only S&P 500, but mid-caps, small caps, internationally emerging markets.

The other area that is always interesting is I've seen a lot of charts over the years and one that particularly jumped out is, over the last 30 and 40 years, you can take a look and say, "What would be the best time to buy into the market?" And you can have the choice of either any random day or only one of the days when the market's at all time highs. And over any forward period, whether it's six months, three years, five years, 10 years, buying at all time highs is actually more productive than buying at any random day. We're at all time highs fairly constantly. Markets are generally trending upwards. So a lot of investors that are around at all time highs waiting for a better entry point, sometimes never find that better entry point. And that goes back to the old adage of time in the market is more productive for long-term performance than timing the market.

And that's what we try and stress with clients as to how we're positioned today. We've been fairly overweight equities, we've been that way since right at the end of '23, and that's been beneficial to us and those same models and internal discussions are indicating a fairly positive outlook. We're very long-term focused on, just because we're at all time highs doesn't mean we can wait it out or there's doom on the horizon, so to speak.

Cärin Viertel:

Yeah, no, good advice. Mike, do you have anything to comment as far as the Investment Committee and other things that you're paying attention to?

Michael Bilotta:

This is always the question, isn't it, is okay, we've hit in fact right now as of going into this week, the S&P 500 has hit 47 different record highs this year alone, which really is only in the top 10 of all instances. There have been nine other years when it's but 47 record highs. The old adage that we know trees don't grow to the sky. So we do know at some point that given fair valuations to slightly overvalued, some areas are really overvalued, but is that at some point the growth in the earnings are going to have to show up and have to deliver to justify the prices that a lot of these companies are trading at. If they do, great, we can continue on. If they don't, then it might be a sector, it might be certain companies, it might be a geographic region, whatever it is, are going to feel the gravitational pull down if those growth rates don't deliver.

Mark mentioned a little bit about the Magnificent Seven. One of the things that we were looking for going into the summer was the rally to broaden out into the rest of the market and it has and that has helped propel the stock market. But I just looked as of, again, the end of last week. The Magnificent Seven still accounts for nearly 65% of the entire return of the S&P 500 year to date, and it was down at about 55 a couple of months ago. So it's crept back up a little bit. To Mark's point, the earnings are there and they've been delivering, but again, it's the, can they keep jumping over the high bar to get there?

I mean, I look at it and a way to sum it up is, the average investor often focuses on the rear-view mirror. The traders and very short term market timers will focus on only what they can see directly in the windshield, and long-term asset allocators, wealth managers, retirement planners like us appreciate both of those because those dictate some of the shorter term moves in the market. But we turn on the GPS and we try to figure out where we're going beyond just the windshield. And right now, that certainly has some questions, but the conditions as we sit here today are conducive to good stock market performance and bonds can continue to clip in their 3% to 4% to 5% returns. And I mean, we are, again, just in that sweet spot. How long that will continue, we'll see. But right now, it's smooth sailing for the most part.

Cärin Viertel:

Well, it's a great analogy. Thanks, Mike, thanks, Mark for sharing these insights and the perspective of our investment committee with our listeners. And thank you, listeners, for joining us today. We hope you'll visit jnba.com and tune into our other podcasts and videos where we cover both investment and financial life planning topics. Thank you for your continued trust in JNBA, not just as your financial advisor, but also as your advocate. Please reach out if you need anything at all. You can find our contact information at jnba.com.

DISCLAIMER:

The previous presentation by JNBA Financial Advisors, LLC ("JNBA") was intended for general information purposes only. No portion of the presentation serves as the receipt of, or as a substitute for, personalized investment advice from JNBA or any other investment professional of your choosing. Different types of investments involve varying degrees of risk, and it should not be assumed that future performance of any specific investment or investment strategy, or any non-investment related or planning services, discussion or content, will be profitable, be suitable for your portfolio or individual situation, or prove successful. Neither JNBA's investment adviser registration status, nor any amount of prior experience or success, should be construed that a certain level of results or satisfaction will be achieved if JNBA is engaged, or continues to be engaged, to provide investment advisory services. JNBA is neither a law firm nor accounting firm, and no portion of its services should be construed as legal or accounting advice. No portion of the video content should be construed by a client or prospective client as a guarantee that he/she will experience a certain level of results if JNBA is engaged, or continues to be engaged, to provide investment advisory services. A copy of JNBA's current written disclosure Brochure discussing our advisory services and fees is available upon request or at jnba.com.