COVID-19, the Stock Market, and Presidential Elections

In February, the stock market reached an all-time high, unemployment was at an historical all-time low, and the economy was chugging along just fine, thank you. Many financial experts foresaw a continuation of the stock market rally through 2020 and the Presidential election.

And then came the coronavirus pandemic and an unprecedented closing down of businesses across the country. The stock market and the economy reversed trends, and we were all told to stay home, put on a mask, and practice social distancing...so much for predicting the future.

We, as investors, are only human, and as such, tend to look for patterns in certain random or seemingly unconnected events. Klaus Conrad coined the word "apophenia" that has come to represent this human tendency. This inclination can be seen in gamblers who play numbers based on their birthday, their children's birthdays, their Social Security numbers, serial numbers on paper currency, or any other set of numbers they may imagine to have some meaning.

In the stock market, there are all kinds of theories arising from unrelated events. One example is jumping out of the market in May and reinvesting again in October. Another example is if an NFC team wins over the AFC team, the stock market will go up and if an AFC team wins, the market will go down. A final example is buying the "Dogs of the Dow" (a popular investing strategy that recommends buying Dow stocks with the 10 highest dividend yields in January and then selling them in December). A very compelling case can be made for each of these theories as well as many others.

But just because you see a pattern does not mean it will continue into the future. It's interesting to look at the numbers, but the patterns are probably no more reliable than a UFO sighting, the flip of a coin, finding a four-leaf clover for good luck, or worrying about what will happen to you on Friday the 13th.

As to this year's Presidential election, the country is divided, tensions run high, and speculation is rampant. That said, statistics based on historical data since 1929 indicate that the Dow Jones Industrial Average (Dow) in any year is generally positive about two-thirds of the time (66.7% to be exact). In Presidential election years, again the market has been up about two-thirds of the time (65% to be exact). These results show no real significant difference between a Presidential election year and any other year.

Regardless, whatever impact the Presidential election may have on the market will be short-lived (odds are it will go up either way). The old or new administration's ability to help the economy and promote real job growth will ultimately tell which way the market will go.

We all may suffer from apophenia to some degree, but a smart investor will stick to Sudoku and other puzzles as a prescription for this psychosis. Changing your investment mix due to some pattern you see developing can ruin your financial future.

In my opinion, investors should not change their current investment allocation hoping to profit from an event such as a Presidential election—it's just another form of market timing. The stock market may be influenced by external monetary and fiscal policy, but investment returns should not be viewed as a direct result of election cycles.

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All the posturing and politics associated with a Presidential election makes it impossible to predict the outcome. There's no way of knowing how the market will respond to election results in the short term – just as there is no way to predict the next pandemic. What we do know is:

Timing the market simply does not work. A well-diversified strategic allocation based on an investor's personal goals and risk tolerance will work best in the long run.

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