Market Commentary

OCTOBER 1, 2024

RJL Investment Strategy (Canada) | RJLInvestment.StrategyCanada@raymondjames.ca
Neil Linsdell, CFA, Head of Investment Strategy | 438.843.0150 | Neil.Linsdell@raymondjames.ca

Do U.S. Elections Affect Canadian Markets?

With interest rate easing cycles underway in both Canada and the U.S., focus is shifting to economic growth, employment, and the U.S. election in November. This month, we wanted to gauge the potential impact of the U.S. election on the Canadian stock market. Do Canadian stocks react differently over the 12 months following the election, based on which party is in the White House? Does the composition of Congress and the Senate play into the landscape? We look back at previous U.S. elections to gain insights into what Canadian investors might be able to expect this time.

Key Takeaways:

- **An uptick in volatility ahead of the election is normal** - The 2024 U.S. presidential election is currently a toss up. With uncertainty comes volatility, which would be expected to persist right up to election day, and perhaps beyond if there is a drawn out conclusion, such as with the Florida recount in 2000, or if we have challenges of certain results. Once the outcome is determined, volatility typically declines.
- **Strong post-election performance for S&P 500 and S&P/TSX Composite** - Regardless of who wins the election, both Canadian and U.S. key stock market indices typically perform above their long-term averages in the following 12 months.
- **Main focus should be on policy changes** - We found no clear indications that having a Republican or Democrat winning the presidential election has any immediate impact on the Canadian stock market. What is more important however is specific economic or trade policies, but these can be adjusted considerably from original campaign promises. Key policies like tariffs and fiscal measures take time to play out and have a prolonged impact on market performance.

The bottom line is that investors should stick with well established investment plans and avoid making decisions based solely on short-term noise such as election outcomes.

Anticipating Higher Volatility Leading up to Election Day

The outcome of the 2024 U.S. presidential election remains highly uncertain, and uncertainty generally leads to volatility in the stock market. The good news is that once the outcome of the election becomes clear, regardless of who wins, we can generally expect volatility to decrease and markets to appreciate over the following 12 months.

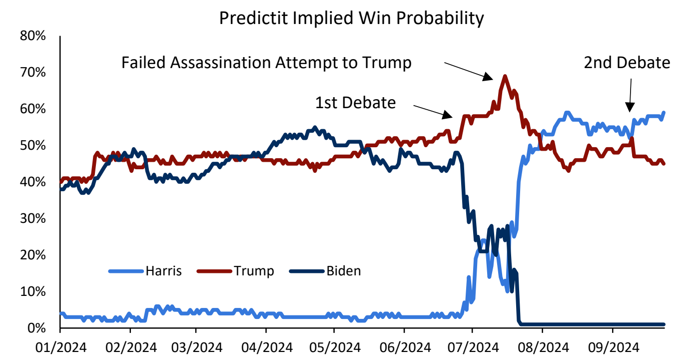
This election has been somewhat unprecedented, and based on recent experience there’s also the possibility that the outcome might not even be certain on election night, with the likelihood of results being contested or legal challenges being launched, extending that period of uncertainty.

After President Biden's poor performance in the first debate in late June and the first failed assassination attempt on former President Trump on July 13, Trump's chances surged in betting markets, peaking at nearly 70% by mid-July (Chart 1). However, since Vice President Kamala Harris replaced Biden as the Democratic nominee, she has closed the gap in recent polls, particularly after the second debate on September 10. Raymond James Research’s Washington Policy Analyst, Ed Mills, and his team recently updated their election forecast, now putting the odds at 50/50 for the presidency. Democrats are slightly favoured to win the House (55% vs. 45% Republicans), while Republicans are expected to take control of the Senate (70% vs. 30% Democrats).

Market volatility has also increased compared to the first half of this year, which is typical as elections approach (Chart 2). The good news is that once the election results are known, both the S&P 500 and S&P/TSX Composite tend to outperform their long-term averages over the following 12 months, regardless of which party wins.

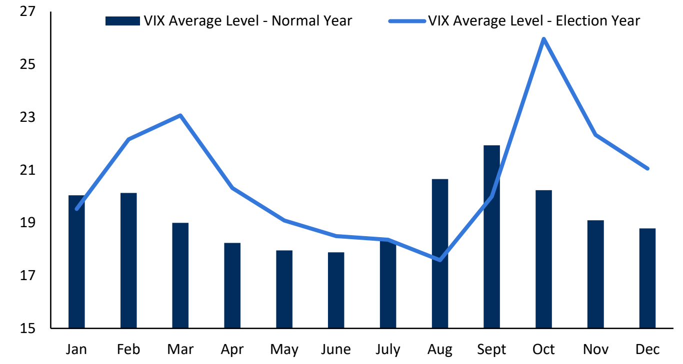
RAYMOND JAMES LTD. | 100 YONGE STREET, SUITE 1400, TORONTO, ON M5C 2W1

Chart 1 - Markets Suggest Election Is a Toss-Up



Source: Predictit; Data as of September 23, 2024.

Chart 2 - Market Volatility Tends to Peak Before the Election



Source: FactSet; Raymond James Ltd.; Data as of August 31, 2024.

Strong Post-Election Performance for the S&P 500 and S&P/TSX Composite

There is no denying the fact that there are significant economic ties between the U.S. and Canada. About 78% of Canada's merchandise exports go to the U.S., and nearly half of its merchandise imports come from there. The U.S. is also the largest source of foreign direct investment (FDI) in Canada and the top destination for Canadian investment abroad. There's also a strong 80% correlation between the S&P 500 and the S&P/TSX Composite, the leading equity indices for each country. Furthermore, around 30% of the revenue generated by companies in the S&P/TSX Composite comes from the U.S. Given these close ties, it's worth analyzing how both markets perform in the 12 months following U.S. elections.

Historically, market optimism tends to rise once election uncertainty clears. Since 1980, the S&P 500's total return in the 12 months following a U.S. election has exceeded its 40-year average of 12.1% in 7 out of 11 periods. Similarly, the S&P/TSX Composite has outperformed its long-term average of 7.8% in 9 out of 11 periods. Years where returns fell short were usually tied to major economic disruptions, such as the early 1980s recession, the dot-com crash in 2001, and the slow post-2008 recovery (although the S&P/TSX had a stronger rebound during that time due to Canada's milder recession). The only other exception was the S&P 500 performance after the 2004 U.S. election, but even then, returns were still solid at around 9.4%. Given the expectation of a soft landing for both the U.S. and Canadian economies, historical trends suggest that reducing political uncertainty in the U.S. typically has a positive effect on both equity markets. So, it's important to stick to your long-term plan and avoid reacting to short-term market volatility.

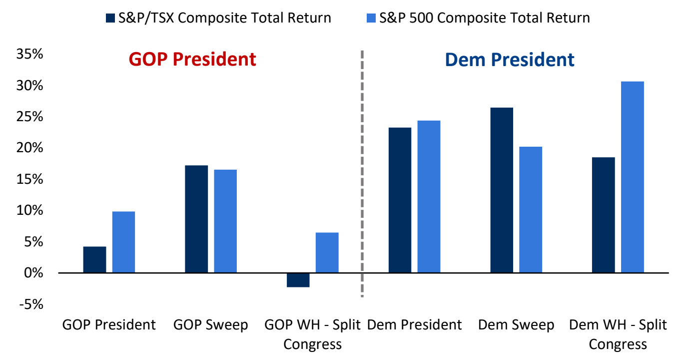
Does the Winning Party Matter?

This is a natural question to consider. At first glance, when comparing 12-month market returns after different election outcomes, it appears that returns following a Republican win, especially when paired with a split Congress, are notably weaker than under Democratic leadership (Chart 3). However, a closer look reveals that two major market downturns occurred during Republican presidencies with a split Congress: the early 1980s recession and the 2001 dot-com bubble.

Neither of these downturns can be directly linked to the party in power at the time they occurred. In the early 1980s, the recession was triggered by an oil shock from the Iranian revolution, which led to surging energy prices and inflation. Central banks responded with aggressive interest rate hikes, causing the recession. The dot-com bubble had been inflating for over a decade and burst in 2001, with little the newly elected party could do to prevent it.

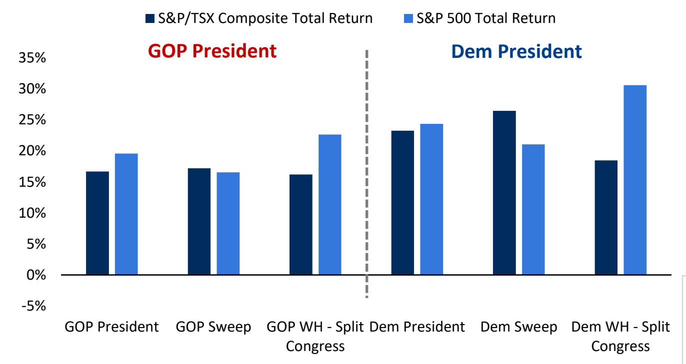
When excluding these two periods, the returns under different election outcomes are much more balanced (Chart 4). Furthermore, given the small sample size (e.g., only two instances of a Democratic White House with a split Congress), there isn't a strong case for significant differences in how the U.S. and Canadian equity markets perform under different political scenarios. Additionally, if we divide each 4-year presidential term into two congressional terms (due to potential changes in the House or Senate at midterms) and conduct the similar analysis over the following 24-month period (Charts 5 and 6), the results across both indices become more evenly distributed.

Chart 3 - Index Average Total Returns 12 Months After General Election Day Since 1980



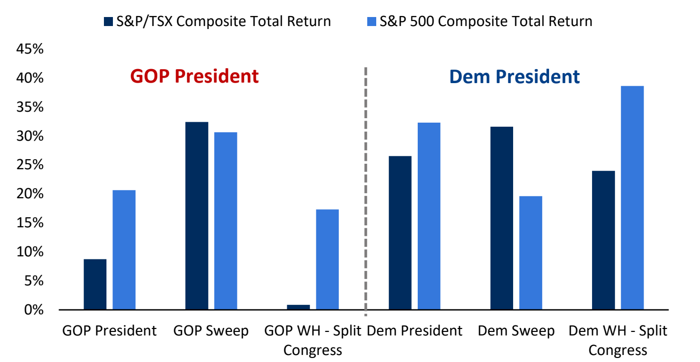
Source: FactSet; Raymond James Ltd.; Data as of September 20, 2024. Total returns in local currency.

Chart 4 - Index Average Total Returns 12 Months After General Election Day Since 1980, Excluding Major Market Corrections*



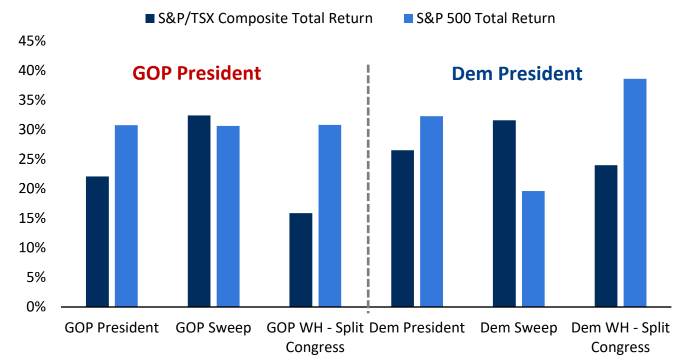
Source: FactSet; Raymond James Ltd.; Data as of September 20, 2024. Total returns in local currency. *Major Market Corrections: 1981, 2001.

Chart 5 - Index Average Total Returns 24 Months After General/ Mid-term Election Day Since 1980



Source: FactSet; Raymond James Ltd.; Data as of September 20, 2024. Unannualized total returns in local currency.

Chart 6 - Index Average Total Returns 24 Months After General/ Mid-term Election Day Since 1980, Excluding Major Market Corrections*



Source: FactSet; Raymond James Ltd.; Data as of September 20, 2024. Unannualized total returns in local currency. *Major Market Corrections (Canada): 1981, 1989, 2001, 2007; Major Market Corrections (U.S.): 2001, 2007.

Long-Term Market Impact Hinges on Policies, Not Election Results

Perhaps a better way to approach the market is to focus on policy changes and their long-term effects rather than just the election results. Some policy changes only fully materialize years after a president leaves office. In Chart 7 on the next page, the S&P/TSX Composite performance is overlaid with the political landscape since 1980, highlighting the primary causes of major market corrections. It reveals that major market corrections are rarely tied directly to election outcomes, with index performance typically impacted by broader factors such as domestic and global economic conditions, commodity prices, and external disruptions, which build up over time and are definitely less predictable than election dates.

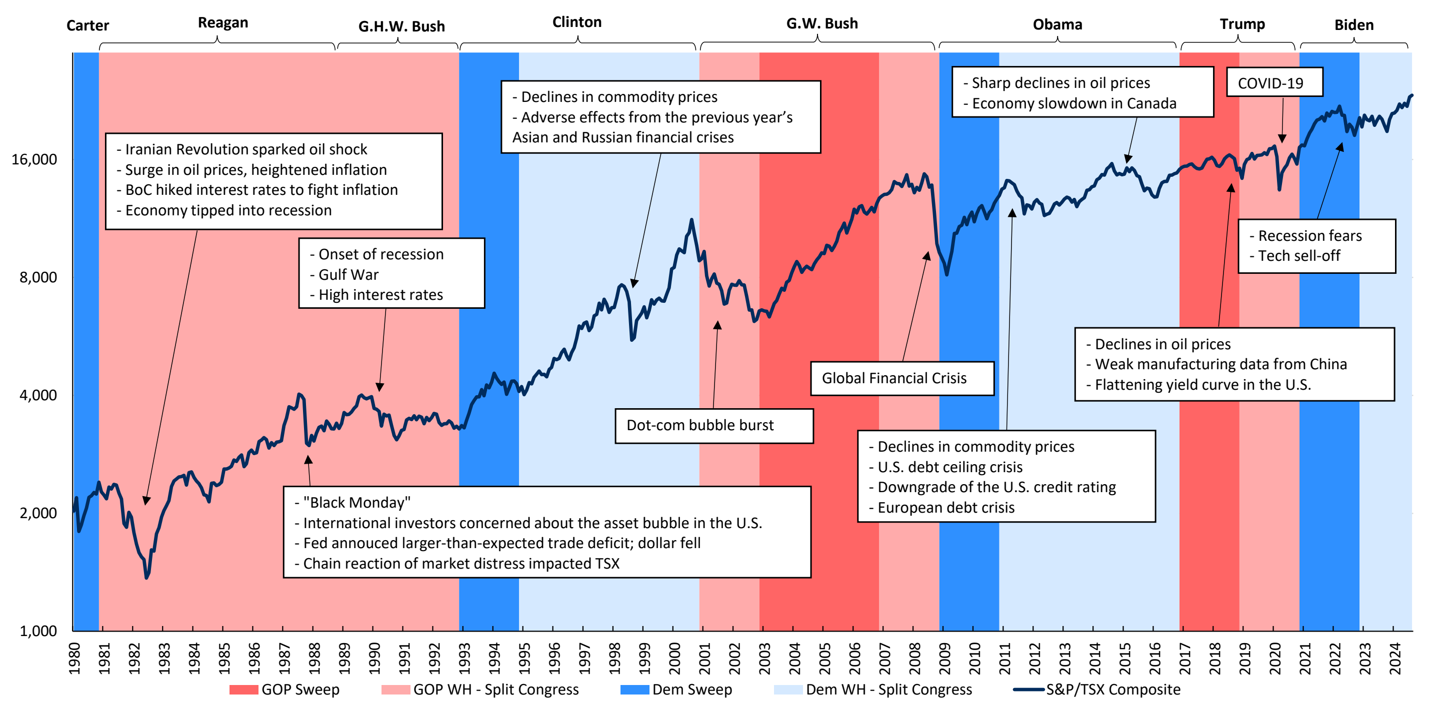
Given the U.S.'s dominant role in global markets and its position as Canada's top trading partner, its policies inevitably influence Canada's economy from multiple angles. For example, systemic shocks originating in the U.S., like Black Monday, the dot-com crash, and the 2008 global financial crisis, affect Canadian markets significantly. U.S. economic health impacts Canadian exports, especially in energy. While U.S. trade agreements, tariffs, and dollar strength can directly influence Canadian businesses, U.S. fiscal policies indirectly affect Canada as well. Additionally, U.S. diplomatic policies, particularly in an increasingly fragmented world, play a role in shaping Canada's trade relations with other countries. All of these factors can influence the valuations and/or earnings of Canadian companies.

Areas that most relevant to Canadian markets are U.S. trade policy, fiscal policy (debt ceilings, tax hikes/cuts), policies around clean and traditional energy. However, it's important to remember that new policies take time to be fully implemented, and many initial proposals are often watered down. Therefore, while closely monitoring developments is essential, it's wise not to overreact to the anticipated election results, especially given the increasingly polarized policy proposals from both parties.

Note of upcoming webinar:

October 23, 2024 (1-2pm ET) - Join Raymond James' Neil Linsdell, Head of Investment Strategy, Ed Mills, Managing Director, Washington Policy, Eugenio Aleman, Chief Economist, and Tavis McCourt, Institutional Equity Strategist, for a quarterly update on financial markets and insights into what to expect with the upcoming U.S. presidential election. For a Client Insights Webinar invitation, please reach out to your financial advisor at Raymond James Ltd.

Chart 7 - Historical Performance of the S&P/TSX Composite Index (1980-Present)



Source: FactSet; Raymond James Ltd.; Data as of September 20, 2024. Y-axis in logarithmic scale. Election day typically occurs in early November of the general/mid-term election year.

Exhibit 1 - U.S. Party Division and GDP Growth (% y/y), Selective Index Total Returns Index Average Total Returns 24 Months After General/Mid-term Election Day Since 1980

Election Year (Y0)	President	President Party	Senate	House	Divided/ Unified	U.S. GDP (Y1)	U.S. GDP (Y2)	Canada GDP (Y1)	Canada GDP (Y2)	S&P 500	S&P/TSX Comp	SPGSCI Index	Comm Svc	Cons Discret	Cons Staples	Energy	Finan-cials	Health Care	Indus-trials	Info Tech	Mate-rials	Real Estate	Utilities
1980	Reagan	R	R	D	Divided	2.5%	-1.8%	3.4%	-3.2%	22.6%	-18.2%	-32.4%	--	--	--	--	--	--	--	--	--	--	--
1982	Reagan	R	R	D	Divided	4.6%	7.2%	2.6%	5.9%	29.9%	26.9%	-0.9%	--	--	--	--	--	--	--	--	--	--	--
1984	Reagan	R	R	D	Divided	4.2%	3.5%	4.7%	2.1%	56.1%	26.7%	-19.0%	--	--	--	--	--	--	--	--	--	--	--
1986	Reagan	R	D	D	Divided	3.5%	4.2%	4.1%	4.4%	19.3%	6.2%	5.1%	--	--	--	--	--	--	--	--	--	--	--
1988	G.H.W. Bush	R	D	D	Divided	3.7%	1.9%	2.3%	0.2%	19.2%	-6.3%	48.9%	4.5%	-12.9%	3.3%	21.8%	-12.0%	4.4%	-11.6%	20.3%	-13.0%	-39.3%	-1.7%
1990	G.H.W. Bush	R	D	D	Divided	-0.1%	3.5%	-2.1%	0.9%	46.1%	10.4%	-26.5%	18.2%	27.8%	22.9%	-15.9%	25.1%	20.7%	-17.3%	72.4%	0.9%	-38.9%	4.3%
1992	Clinton	D	D	D	Unified	2.8%	4.0%	2.7%	4.5%	17.9%	31.3%	-1.7%	9.4%	10.3%	-13.2%	36.4%	13.6%	42.7%	32.0%	21.4%	64.4%	11.4%	16.9%
1994	Clinton	D	R	R	Divided	2.7%	3.8%	2.7%	1.7%	60.5%	39.3%	12.6%	27.7%	22.5%	36.8%	27.8%	66.0%	100.4%	44.5%	85.7%	14.6%	5.4%	13.7%
1996	Clinton	D	R	R	Divided	4.4%	4.5%	4.3%	3.9%	64.2%	16.8%	-26.9%	61.1%	33.2%	78.0%	-4.1%	44.2%	-16.4%	15.6%	21.3%	-26.9%	12.4%	31.2%
1998	Clinton	D	R	R	Divided	4.8%	4.1%	5.1%	5.1%	28.6%	55.6%	61.9%	146.8%	27.0%	51.5%	29.8%	29.0%	59.9%	50.1%	232.1%	-15.6%	-8.9%	-11.7%
2000	G.W. Bush	R	D	R	Divided	1.0%	1.7%	1.9%	3.0%	-33.6%	-30.6%	-14.0%	-46.3%	-25.3%	40.5%	28.9%	-2.5%	-39.5%	-34.0%	-89.8%	20.6%	21.8%	28.1%
2002	G.W. Bush	R	R	R	Unified	2.8%	3.8%	1.8%	3.1%	29.7%	43.8%	67.2%	26.1%	22.6%	17.4%	67.9%	60.0%	-17.7%	9.8%	95.5%	33.4%	36.1%	23.6%
2004	G.W. Bush	R	R	R	Unified	3.5%	2.8%	3.2%	2.6%	25.5%	42.3%	24.5%	40.9%	33.5%	8.3%	70.4%	43.3%	-18.5%	45.8%	-9.7%	59.0%	47.5%	41.5%
2006	G.W. Bush	R	D	D	Divided	2.0%	0.1%	2.0%	1.0%	-26.2%	-16.3%	0.2%	8.2%	-25.5%	-10.9%	-17.0%	-20.2%	-33.1%	-9.8%	-5.1%	-19.1%	-37.9%	2.9%
2008	Obama	D	D	D	Unified	-2.6%	2.7%	-2.9%	3.1%	27.2%	35.5%	26.4%	9.1%	30.8%	23.2%	27.1%	27.2%	79.3%	27.0%	0.0%	98.0%	42.5%	30.9%
2010	Obama	D	D	R	Divided	1.6%	2.3%	3.1%	1.8%	20.6%	1.0%	6.0%	39.6%	2.4%	26.1%	-3.1%	10.6%	96.9%	19.8%	-53.3%	-17.4%	12.9%	14.8%
2012	Obama	D	D	R	Divided	2.1%	2.5%	2.3%	2.9%	48.4%	25.1%	-17.8%	26.7%	81.5%	72.5%	15.4%	46.0%	109.5%	74.9%	82.4%	-38.3%	21.3%	7.8%
2014	Obama	D	R	R	Divided	2.9%	1.8%	0.6%	1.0%	9.4%	6.0%	-33.9%	26.0%	11.4%	42.9%	-11.9%	12.4%	-75.2%	3.5%	29.3%	17.8%	5.8%	18.1%
2016	Trump	R	R	R	Unified	2.5%	3.0%	3.0%	2.7%	36.7%	11.1%	26.1%	10.5%	16.3%	4.0%	-6.1%	19.1%	62.6%	35.0%	39.3%	-8.7%	23.7%	3.2%
2018	Trump	R	R	D	Divided	2.5%	-2.2%	1.9%	-5.0%	22.6%	9.1%	-22.2%	2.7%	0.7%	22.1%	-34.1%	-2.3%	-58.1%	24.6%	137.6%	59.0%	-2.7%	48.1%
2020	Biden	D	D	D	Unified	5.8%	1.9%	5.3%	3.8%	13.8%	28.0%	85.0%	28.5%	29.3%	30.2%	145.5%	40.9%	-57.8%	25.0%	-36.2%	-11.6%	10.2%	8.1%
2022	Biden	D	D	R	Divided	2.5%	--	1.2%	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--

Source: FactSet; Raymond James Ltd.; Data as of September 20, 2024.

Note: Election Day typically occurs in early November. For example, if the election year is 1980, Election Day would be in early November 1980. Y1 would correspond to 1981, and Y2 to 1982. All index total returns are unannualized, in local currency, measured over a 24-month term after Election Day. Unshaded rows indicate general election years, while light blue shaded rows represent midterm election years.

IMPORTANT INVESTOR DISCLOSURES

Complete disclosures for companies covered by Raymond James can be viewed at: Disclosures https://raymondjames.bluematrix.com/sellside/Disclosures.action

This newsletter is prepared by the Private Client Services team (PCS) of Raymond James Ltd. (RJL) for distribution to RJL's retail clients. It is not a product of the Research Department of RJL.

All opinions and recommendations reflect the judgement of the author at this date and are subject to change. The author's recommendations may be based on technical analysis and may or may not take into account information in fundamental research reports published by RJL or its affiliates. Information is from sources believed to be reliable, but accuracy cannot be guaranteed. It is for informational purposes only. It is not meant to provide legal or tax advice; as each situation is different, individuals should seek advice based on their circumstances. Nor is it an offer to sell or the solicitation of an offer to buy any securities. It is intended for distribution only in those jurisdictions where RJL is registered. RJL, its officers, directors, agents, employees and families may, from time to time, hold long or short positions in the securities mentioned herein and may engage in transactions contrary to the conclusions in this newsletter. RJL may perform investment banking or other services for, or solicit investment banking business from, any company mentioned in this newsletter. Securities offered through Raymond James Ltd., Member-Canadian Investor Protection Fund. Financial planning and insurance offered through Raymond James Financial Planning Ltd., not a Member-Canadian Investor Protection Fund.

Commissions, trailing commissions, management fees and expenses all may be associated with mutual funds. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. The results presented should not and cannot be viewed as an indicator of future performance. Individual results will vary and transaction costs relating to investing in these stocks will affect overall performance.

Securities mentioned in this publication may entail higher risk. Clients should contact their Financial Advisor to determine if the securities are compatible with their risk tolerance and investment objectives.

Information regarding High, Medium, and Low-risk securities is available from your Financial Advisor.