

The Election's Impact on the Markets

Prior to the November 4 election, there had been plenty of discussion and speculation about how the election outcome would impact the economy and financial markets. For example, investors were wondering:

- *Do stocks typically rise more after a Democrat or a Republican is elected to the White House?*
- *What happens to the market when the Congress majority is – or is not – the same party as the President?*

With the 2008 election behind us, let's take a look at the election's impact on the markets. To begin, let's consider what history shows us*:

- In general, equity markets tend to do better under a Democratic administration versus a Republican administration.
 - Average annual performance is +8.9% with Democratic leadership compared to +3.8% with Republican leadership.
- Overall, stocks tend to exhibit positive performance when we have a single party (either Republican or Democrat) heading up the administration and a majority of Congress.
 - Historically, stocks tend to do better with a Republican administration and a Republican-controlled Congress (+12.4% return) than a Democratic administration with a Democratic-controlled Congress (+7.4% return).
- In the past, market performance has been better when a Republican Congress works with a Democratic president (+10%) as compared to a Democratic Congress working with a Republican president (-5%)

History is an Indicator, Not a Predictor

Although this historical view is interesting, we can always find exceptions. For example, some Democrats (both in the presidential role and as members of Congress) act more like Republicans, and vice-versa. We've seen:

- Former Republican president George H.W. Bush raised taxes.
- Former Republican president Richard Nixon instituted wage and price controls.
- Former Democratic president John F. Kennedy cut taxes.

We also have to consider *the extent* of the control of Congress. A Congress with the necessary votes to override a filibuster (60) or a veto (67) would probably have a different impact on market outcomes and the economy than a Congress without this power. Also, some Republicans may side with Democrats on controversial issues, and when that happens, 58 or 59 votes may be enough for control.

Another consideration is the state of the U.S. economy and monetary policy conditions at the time the new Administration takes office. There's typically a delay from the time programs are decided, developed, and implemented to the time when subsequent changes actually impact the economy. Likewise, the stock market tends to respond in anticipation of changes. In both scenarios, one party may get the credit, or the blame, for actions previously taken by the opposing party.

Looking Ahead

In early 2009, we expect the President, his administration and Congress to be focused primarily on fixing the slumping U.S. economy. We also expect them to begin work on a number of other initiatives that were discussed during the campaign. Here's our short list of anticipated policy initiatives, along with our view of related investment implications:

- **Stimulus Package:** If Congress does not complete a stimulus package in the 2008 "lame duck" session, we expect it to be one of the first bills passed and signed by the President in 2009. The Administration's version of a stimulus package would most likely include funding for areas strongly promoted in the campaign, such as extension of unemployment and food stamp benefits, assistance for state governments facing Medicare/Medicaid funding shortfalls, and a limited program of infrastructure spending.
- **Taxes:** Despite the campaign rhetoric, taxes under the new Administration and Congress are yet to be defined – with no major changes expected prior to 2010 (the expiration of the Bush tax cuts). In general, President-elect Obama has promised higher taxes for taxpayers making more than \$250,000 per year, but it's unlikely that these taxes will be adequate to fund the many projects discussed during the campaign. We also can't overlook the significant cost of current bailouts – and the possibility of future bailouts – which will have a great effect on future tax increases and future Treasury borrowing.
- **Government involvement in the private sector:** President-elect Obama will likely be sympathetic to the plight of the U.S. auto industry and favor some form of bailout. There is also a strong possibility that we will see greater government involvement in the mortgage industry, with the structure of Fannie Mae and Freddie Mac transformed into a government-backed structure similar to Ginnie Mae.
- **Regulatory reform in the financial sector:** There appears to be agreement between the Administration and Congressional leaders to establish tighter regulation of credit default swaps and hedge funds and crack down on predatory lending practices. Increased regulation could add another layer of expense to the financial industry and curtail a firm's ability to generate the kind of returns enjoyed in the past. However, accounting or consulting firms could benefit from increased regulation.
- **Energy:** The energy policy will likely be a high priority for the new Administration and Congress. Anticipated initiatives include renewable energy and clean technology investment incentives, expanded use of biofuels, and the creation of "green jobs". President-elect Obama has a goal for our country to generate 10% of our electricity from renewable energy sources by 2012, as compared to 2% today. Wind and solar companies would most likely benefit from these initiatives.
- **Health Care:** There are no easy answers here. If enacted, a National Health Insurance program would force drug prices down, however, offering this program to many new individuals would increase demand for drugs. At this point, because of the complex and diverse nature of the health care industry, it's just too early to predict benefactors or losers here.
- **Infrastructure:** The creation of new jobs will stimulate the economy, and it's likely that transportation (especially rebuilding and refortifying roads, bridges, etc.) will be one area of concentration. Construction and engineering companies, especially ones with a history of government business, would most likely benefit from this initiative.

*Historical data covers the periods of 1921 to present. Sources: Merrill Lynch, Credit Suisse

Products and services offered through Bremer Insurance, Bremer Trust, and INVEST Financial Corporation are not insured by FDIC, are not a deposit or other obligation of, or guaranteed by, the depository institution, and are subject to investment risks including possible loss of the principal amount invested. This report has been compiled using data and other statements of fact derived from sources which we believe to be accurate and reliable. However, such data and other statements of fact have not been verified by us, and we do not make any representations as to their accuracy or completeness. Any opinion expressed herein reflects our judgment at this date and is subject to change.