Patti: Hi, everybody. Welcome to The Patti Brennan Show. This actually is Patti Brennan this time. This is part two of our series talking about the election and what markets tend to do during the election.

Joining me today is none other than Michael Brennan. Today is going to be the battle of the Brennan's. I'm not going to say the old school and the new school because I'm not old, right, Michael?

Michael: That's right.

Patti: Am I going to be Mom today or am I going to be Patti?

Michael: Mom let's do it.

Patti: Let's do it. We had this investment committee meeting. You guys came in and you were assigned this task of what happens during election years. What questions should we be prepared to answer? If you haven't listened to part one, you must go back and listen to part one. It was a blast and very revealing. In part one, we talked about this game that Michael, Rory, and Matt came up with to spice things up. They certainly have a way of spicing things up.

Michael: Michael, why don't you explain how you came up with this idea of the game and the question that you were seeking to answer.

Michael: Thank you for that. I must be fully honest here, full transparency. The game came before...

Patti: The question?

Michael: Before the question. I had an end in mind, I had a goal in mind, but I wasn't sure how we were going to get there. The goal in mind was that I wanted to find a way to play pin the tail on the donkey and pin the trunk on the elephant.

I had this vision of a big poster of an elephant and a donkey. I wanted to see if our team would have the ability to match a presidents rate of return under his term with their respective picture on the elephant or on the donkey.

That was the goal in mind. I really wanted to look at what markets did during each year of each president's term.

Patti: That's interesting because you know as well as I know, there's this big thing out there called presidential cycle theory. Everybody talks about it.

Michael: Yeah.

Patti: Historically, in year one, the theory is that the market's going to be weak. In your research, which basically goes from January 20th when they get into office through the term, what did you find and why?

Michael: The reason that markets performed the weakest, again, according to this theory, is that the chief executive tends to work on the most deeply held policies and

proposals to indulge the special interest of those that got him elected. That makes sense.

Patti: Let's just give it to them real. It's been a terrible, weak year. What did your research find?

Michael: My research found anything but that.

Patti: Interesting.

Michael: Yes. From Biden all the way down to George HW, on average, the first year that each one of those presidents was in office, the market performed 18%.

Patti: Wow.

Michael: Again, this is why it's theory versus fact, the theory states that the first year should be the weakest.

Patti: That's pretty darn good.

Michael: 18% is pretty darn good.

Patti: That's what's wild, the theory says, "Oh, you just wait. We're going to kill it in year two."

Michael: Of course. Markets are going to recover. Guess what? There's no order to recover from 18%. It's tough to come back from that. I will say, there's going to be an exception. George W had a rough first year.

He stepped into office on January 20th, 2001. There were some things going on back then that would certainly be hard for anybody to step in the office at that time. This is where theory meets fact.

My research did reveal that there is a sophomore year slump. Year two has been tough for all presidents.

Patti: Let's go into year three, then. What happens in year three?

Michael: Year three is where the theory and fact do really align. The theory states that the market should be peaking in that third year. It's suggesting that market performance is going to perform best in the second half of a presidential term when the sitting president is really trying to boost the economy to get reelected.

Let's be honest, that is what happens.

Patti: In year four, the theory says, "Before falling in the fourth and final year, after which the point in the cycle begins again with the next presidential election."

Michael: Before falling, it's already coming down from 23% to 7.24%, which is on average what has happened in the last year of the president's term. The model suggests that the president's going to be focusing on shoring up the economy to get reelected, and the major stock market indexes are more likely to gain in value.

Patti: It's very interesting. I think we should play the game.

Michael: That's the information that set the table leading into this game. I had the idea of the game before I decided what we were going to do to get there. This right here was a gold mine for me to look at.

I found what happened was not the case. Two things are not right with the theory. It does pretty much get the sophomore slump on point, that is a theme. It also gets the fact that the third year, for whatever reason, tends to be the best. Armed with this information, I was curious if our brilliant team at Key Financial would have the ability to match the rates of return to the president that the rate of return is associated with.

Patti: For the entire four years?

Michael: For their entire four years.

Patti: That was interesting. We broke up into teams and it was a contest. Let's do it for the folks listening today. Let's start out with our first president, George HW. He was coming in right after Reagan. He did a few things internationally.

We invaded Panama and that was scary. I'm not an old guard, but I was alive during that period. He did sign some treaties with Russia to reduce nuclear arms and that was a plus. People were feeling safer, warm and fuzzy.

He said one thing, no new taxes. Now, let me qualify that. When he was running to be elected, Reagan was president, and he was the vice president. While he was running, his campaign speech was no new taxes. He got into office and raised taxes.

Michael: Why don't you look at the board and try and pick. Of all these rates of returns, how do you think he did while he was in office?

Michael: If I'm hearing you correctly, he ran on one thing when he got into office and then he did another thing.

Patti: He did a bait and switch.

Michael: People don't like that, not one bit. I am probably going to look for one of the lower rates of return.

Patti: For the record, we've got rates of returns for four years of minus 25% to 83%. We've got one up here that's 66%. Another one, 82%. 101% for four years? Not bad. What do you think he did for his four years in the S&P 500?

Michael: This is where it gets hard, Patti. Armed with the information that you just shared with me; I know year one was probably a dog for him. People were not thrilled, and he went against his word. Year three is a perfect example of this third-year bump.

The markets were up almost 30% in his third year. He had a negative rate of return his first year. Then he had a 1% the next year. The third year was up 29%. I really think that third year brought him back up. He's not minus six, he has to be positive. I'm looking for the lowest positive number to give HW.

Patti: People are waiting. Just pick it.

Patti: Isn't it 39%?

Michael: Yeah.

Patti: 39%.

Patti: OK, because of that third-year bump, he did 39%. I'm guessing 39%. Ding, ding, ding, you did it. That's the way we do this.

Michael: Sorry. We just had a two here. Maybe that was for the team, too?

Patti: Yes, that's exactly right.

Michael: That's what confused me. Sorry.

Patti: Cool. OK, Michael. Let's start with George, the first George Bush.

Michael: HW.

Patti: HW. How do you think the market did during his four years?

Michael: In the first half of his presidential term, the market stunk. The second half, especially the third year, most notably, I know that he really swung things around. I'm going to go with either -- man, this is tough -- either 40%, 41% or 39%. Just because of his first year being a negative return, I'm going with 39%.

Patti: Ding, ding, ding, you did it.

Michael: Wonderful.

Patti: Next up, President Clinton. Clinton invaded Yugoslavia. You were five years old when he was elected, but during his term, you were 10. He had that impeachment trial.

Michael: That's right.

Patti: He had a little thing going on the side that wasn't good for our country. He was being impeached. As it turned out, he was not impeached, but he did lose his law license for five years in Arkansas.

Given all that uncertainty and the fact that America's morals were on trial, how do you think the market responded?

Michael: The stock market doesn't care exactly what's going on in the world. The stock market is a beast and it's going to do its own thing regardless of what all the noise is. I know that Clinton, in the end, crushed it. I have two terms to pick from here, this is pretty darn high.

I'm between 98% for his first term and 82% for his second term. When did his little side project occur?

Patti: That was in his second term.

Michael: If that's the case, I'm going 98% for his first term and then 82% for his second term.

Patti: That's right. You nailed it. Who was next? After Clinton, who do we have?

Michael: We have W.

Patti: W was elected in January 2001.

Michael: Tough time.

Patti: Yep. Then he got reelected for a second term. How do you think he did?

Michael: The first term...

Patti: I'm just going to set you up here. When 9/11 occurred, there was a lot of uncertainty, everybody was scared. We were invaded on our own turf. The feeling of patriotism…we were really united as a nation like we had never been before.

With that warm and fuzzy feeling that we were all having, how do you think the stock market did?

Michael: With all of that going on, I do recall that in his first two years, he was crushed. Again, in keeping in line with this third-year bump, I don't think it's as bad. It's going to be negative, it's not good. I don't know how deep of a negative his first term would be, but let me try to find the highest negative, negative 6% for his first year.

Patti: For his first term? That's right.

Michael: For his first term. Excuse me.

Patti: Second term?

Michael: That was the bad one. The second term was fun, 2005 to 2009.

Patti: That was the financial crisis.

Michael: That's the financial crisis. I'm going to find the lowest possible rate of return on this list, which is going to be minus 25% for Bush's second term. Geez.

Patti: George W got smoked in both terms and the market did, while he was the sitting president.

Michael: This is interesting. If we were to look at both of his terms together, the market was down 31% across an eight-year period. I guess that's why they call it the lost decade.

Patti: Yep. You got it.

Michael: The market was down 31% during those eight years. My goodness.

Patti: Now, let's go to Obama. Obama gets in in 2008. We are in the middle of this worldwide economic crisis like we had not seen since the Depression. He gets into office and people are scared to death. I'm not kidding you. In 2008, the market lost 39% for the year.

Then he basically gets into office in 2009 and it kept going down. I'm telling you; I feel like it was yesterday. From January to March 9th, the market continued to go down another 15% on top of that.

Michael: Good Lord.

Patti: Then on March 9th, it turned on a dime just like that. By the end of the year, the market did what?

Michael: 44.75%.

Patti: Crazy. Keep in mind, we were still scared. It was a banking crisis, it was a financial crisis, and it was an economic crisis on a worldwide basis.

Michael: Here's a question for you. That first year he did 45%. Is that because it was at such a low bottom?

Patti: There's no question about it, it helped. He came in and he was calm. We have had an economic and financial crisis whether a Democrat or Republican was leading, something that we had not seen since the Depression. Everybody thought we were heading towards another one. That's when leadership really matters. It could be a Republican or a Democrat, it's the person. The person must be strong and confident.

Michael: Was it really the president or could it have been the Federal Reserve? I will tell you, we all here at Key Financial believe wholeheartedly that Ben Bernanke really was the hero.

He was the man who probably single-handedly saved the world economy because of the work that he had done, earning his PhD from Princeton. His PhD was regarding The Great Depression. He did some unusual things that no Fed Reserve chairman had ever done before. He flushed the economy with cash, and we had a recovery.

It wasn't nearly as strong an economic recovery. The big thing back then was the new normal. We're going into a new normal. I'm telling you all, I never believed a word of it. We had an economic new normal, but the economy and the stock market are two different things. It didn't mean that the stock market was going to get what everybody predicted back then as very low single-digit returns.

I'm not kidding you, it's like I could hear it all over again. I'm not going to tell you all the people that were saying it, but the pundits that everybody listened to were saying, "Oh, forget it. We're going to have below average returns." Back to the case in point.

Michael: I probably remember more than anything else all the darn Cash for Clunkers. I still have the jingle stuck in my head.

Patti: K-A-R-S, Kars4Kids.

Michael: That was more recent.

Patti: Oh, my goodness.

Michael: The Cash for Clunkers, in the end, it ended up working.

Patti: It just goes to show you, that was fiscal policy. That's the government making those decisions, then you have the Federal Reserve. We need them both.

Michael: Yes, we do. Back to Obama's first term, he crushed it the first year. I know that it kept up, but not nearly at that pace. While every other year was a positive rate of return in Obama's first term, it didn't keep up with that first year.

For Obama's first term, I want to see the highest rates of return because I think he's up there. Again, Clinton crushed it. '98, I already put under it that Clinton won. Wow, President Obama, you're getting 101% during your term.

Patti: Here's the question. Was it sustainable? Everybody says, "Oh, it's already done its thing. It's not sustainable." What happened during his second term?

Michael: Again, keeping in line with this trend of year one, he did pretty darn good. I'm looking at 2013 here, he did 26%.

Patti: It was a momentum market.

Michael: It was. Here's an anomaly in talking about the third-year bump. Believe it or not, Obama's third year, he was negative. He was down 6%.

Patti: What was going on then? Didn't he pass Obamacare right around there? That was a controversial piece of legislation. I'm not saying that that was the reason. I must go look at the timing of things because I could be completely wrong. People were thinking, "I don't know if this is such a good idea."

Michael: Then it turned back around again for his fourth year.

Patti: He's a good sales guy and a great orator. He did a good job and had Biden as his vice president. People were thinking at the time that Biden was going to run. He needed to get the country together to support Biden.

Biden didn't end up running right away because his son had just passed away. He took time off and guess who got elected? We had Hillary Clinton going against Donald Trump and Trump won. What happened during Trump's term?

Michael: Before I get into Trump's term, I just want to finish off Obama's second term. I think that he was still significantly up again. His first year and his fourth year of his second term were both 25, 26%. I'm going to go with 66% for President Obama second term.

Patti: Not bad for four years.

Michael: Not bad at all. My goodness. If you look at President Obama's entire term in office, for those eight years, he was up 235%.

Patti: Wow, drum roll! So, we have this election. It's Hillary Clinton and Donald Trump. I will tell you, people thought Hillary Clinton was going to win because we're coming off a Democrat and it was a great couple of terms. Rough times, but the market was amazing. Hillary's probably going to win, and I remember staying up all night watching that.

Michael: Of course. As did I.

Patti: When it looked like Donald Trump won the election, the market at one point was down 900 points on the Dow. Then I got a couple of hours of sleep, woke up, and the futures market was going absolutely nuts.

Donald Trump, how did he do in the first term? We must remember what happened during his term. To his defense, we had the pandemic. That was a scary time. How did the stock market do during Donald Trump's term?

Michael: I know the day after Donald Trump was elected, the market was up. I believe that it continued that way for the rest of that first year for him. He took a hit in the second year, which is in line with our presidential cycle theory. This is a case where the theory has certain merit. He was down 3% in his second year.

Patti: Sophomore slump all over again.

Michael: Sophomore slump, you got it. In keeping in line, this is where the theory does sometimes have merit, he was back up year three. Year four wasn't too shabby either. I have a couple of high numbers here, although some have been taken. I'm going to say, Donald Trump, 83% for his four-year in office.

Patti: He runs again, doesn't get elected. It's all the election stuff and January 6th occurs. We now have President Biden. We are just coming to the end of President Biden's term. How's he doing?

Michael: His first year was great, but the second year, not so much (sophomore slump). He had a great bump in the third year, his junior year, that crushed it again.

Patti: Michael, if there's one thing consistent that I'm hearing from you and that we sort of know, is that the third year tends to be good.

Michael: It's incredible. The third year is what drove this little activity here. Me looking at the actual raw data, finding a trend, and thinking "There's no way that I'm the only person that has found this trend." Sure enough, I did some digging and that leads me into this whole presidential cycle theory. It was fun, frankly. Not everybody would call it fun.

Patti: Here's the question of the day. Now that you know those numbers, let's finish with Biden. How did Biden do and how's he doing? We only have one left, it's 40%.

Michael: 40%.

Patti: He's 40%. Not bad for three-plus years.

Michael: The way that I started to determine the end of the term, he will have...

Patti: The rest of this year.

Michael: Theoretically, through the rest of this year up until January.

Patti: Which tends to be decent.

Michael: As we found.

Patti: Excellent. You've seen the theory, you've read the theory, and you've seen actual history. What do we do about it? You manage portfolios and we take care of $2.2 billion. That is a ton of money.

Michael: I get goosebumps every time I hear it, and I hear it every single day.

Patti: We are supposedly considered one of the top 100 firms in the entire country. We do our work, and we do our research. We have discovered something or validated some information, a theory. What do we do with that information?

Michael: We stick to our guns and our fundamentals. We have that data here and know what markets have done. Are markets going to always do what they have done? No. Over the long term, markets are up, what, 70% of the time?

Patti: Irrespective of who is president.

Michael: It doesn't matter who's in office.

Patti: My question for you is this. Sorry, folks, as you can probably tell, I'm pushing a little bit because this is what we do.

Michael: This is Mom.

Patti: This is how we train the next generation of great financial advisors. Now, you've done the research. Why do we do the research? Why do we bother?

Michael: Because the research leads me to a place where I can accurately and confidently state that from 1928 to 2023, the market is up 67.4% of the time.

Patti: People aren't going to live that long.

Michael: No, they're not.

Patti: I'm not going to live that long.

Michael: Let's play devil's advocate. If you're not planning to live that long, how are you, Patti Brennan, going to handle that information? I understand what you're saying, 67% of the time it's up. That also means that 33% of the time, it's down. Is that a risk that you're willing to take?

Patti: Here's the other way to look at it. If you're on an airplane and the pilot gets on and says, "OK, folks, we have a 67% chance of not crashing." What does that mean? That means that 33% of the time, you could crash. That's the way people think.

The most important thing that we must understand, Michael, is that human beings have fears. We must understand that is real for them. They're focused on the crash. They're not focused on the 67% of the time. They don't think in the long term. They're listening to the people on TV and looking at the headlines, and they're scared. Fundamentally, this is the way we roll, what matters more than anything is them.

Michael: If it happens, are they going to be, OK?

Patti: Bingo.

Michael: That's the takeaway there. I don't know if all of our listeners out there have someone looking at their portfolio the way that we are looking at it. It's very nice to be in a position when a client does experience these fears, whether they're real or not.

In the case of where they are real, I love to be able to state the fact that, "Look, if a 33% crash does occur today, you're going to be OK."

We have designed your portfolio in such a way where you have how many years of living expenses marked up in this bucket. Assets that are going to consist of money market instruments, short-term bonds. All the stuff that is relatively safer no matter what happens in the markets. We don't care if they're up 39% as it was under HW or down 25% under W, we've got you.

Patti: We're prepared. The most important thing is that every individual and every family is different. We understand not only what their risk tolerance is, but what their risk capacity is. If something happened, would they be SOL?

I want to know what's going to make this thing fail. I want to know what's going to put this family in trouble. Let's know ahead of time and make sure that we're prepared because we don't know. Nobody knows what's going to happen.

We have got to protect people and their hard-earned money. That's the most important thing. Protect it and grow it so that it lasts the rest of their lives irrespective of who was president and who got invaded.

Michael: Stuff happens and it's not fun. We never know what's going to happen, but we know what to do when it does.

Michael: Absolutely. We know.

Patti: That's the takeaway.

Michael: It doesn't matter who's in office. What matters more than that is, do we have pools of money secured?

Patti: OK, Michael. Let's wrap this up for everybody. The takeaway is what? Presidential elections, does it matter? Presidential cycle theory, does it matter?

Michael: There may be some merit to the sophomore slump and there may be some merit to the third-year bump.

Patti: Does it matter to our clients, though?

Michael: No, it doesn't.

Patti: Does it matter in terms of what we do and what we recommend for their portfolio? What matters more than that?

Michael: What do we do during those times.

Patti: Perfect. Lesson learned. All right, guys.

Michael: Did I pass?

Patti: You passed. You have witnessed a little bit of mentoring. It is the battle of the Brennans, back and forth. Hopefully, you learned a little bit about presidential cycle theory. The fact of the matter is sometimes it works, sometimes it doesn't. It doesn't matter. What matters is you.

Patti: Michael, fantastic. Lesson learned. Thank you all for tuning in to this session and learning about presidential cycle theory as well as some other things. I am Patti Brennan, Key Financial, wealth management with wisdom and care. Have a great day, everybody.