Does it really matter?

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Debra Slabber
Director: Portfolio Specialist
Morningstar South Africa

For Financial Advisors and their Clients

2024 is a big year on the election front, with democracy taking center stage. With more than half of the world's population heading to the polls, it's understandable that investors are feeling a sense of unease. Elections tend to bring up a lot of emotion, introduce uncertainty and prompt investors to brace for some market volatility. Couple this with the geopolitical tension that is already persistent.

Locally, the election is just around the corner, and it could be a significant one. Sentiment towards the ruling party has been falling and some polls predict that the election will see the ANC lose its majority. This may require the ruling party to form a coalition government for the first time since 1994. Coalitions can come with disadvantages, namely slow decision making and instability. This could prove to be a headwind for a country looking to improve its economic prospects. What will happen this time around? Will it be a regime shift, are we facing a coalition government, or will it just be more of the same? Who knows. It's incredibly difficult to predict how these political events will pan out, and even harder to predict how the market will react based on these events.

Elections do not take place in a vacuum

When it comes to markets and politics, one clear lesson from the past is that elections don't take place in a vacuum. Politics sit alongside many other variables, including macro and micro, fundamental and technical, foreign and domestic factors that can impact asset prices.

If we cast our minds back to the most recent US election for example, the pandemic was a far bigger driver of markets in 2020 than the election was. Another lesson is that initial reactions don't always persist. The small value rallies of both 2016 and 2020 eventually faded, as large-cap growth stocks resumed their dominance. Earnings and cash flows are ultimately bigger drivers of markets in the long term than politics. Therefore, we shouldn't assume that market behaviour in 2024 will resemble that of 2016 or 2020. The candidates might be the same as 2020, but the context differs. The expectations that powered the small value rally of 2016 won't be the same should Trump prevail in November, especially given the US equity market behaviour under the Trump presidency. Markets know that campaign rhetoric is one thing; what happens under an administration is quite another.

Turning back to the local front, uncertainty over election outcomes continues to drive weak appetite for risk assets and investors remain skeptic amidst economic inertia. With that being said, investors have had to endure many uncertainties over several years, including politics. A weak currency, lackluster economic growth, an unstable energy supply, deteriorating infrastructure and elevated interest rates, to name just a few. Uncertainty, volatility, and political instability is nothing new to South Africa.

A quick glance at history

It's often said that politics and investing don't mix, but that's not because political dynamics have no impact on financial markets. Taxing and spending, policy and regulation—these are all important variables that can impact stocks, bonds, currencies, and commodities. But politics is just one of the many forces that move asset prices.

The chart below shows how South African equities and bonds have fared for each calendar year, when an election took place in our country. It also shows what happened to the rand in that calendar year. It is hard to draw any concrete pattern from the data. Maybe that in itself tells you that it's maybe more noise than anything else?

Election year	All Share Index Return	All Bond Index Return	Rand
1966	21%	1%	0%
1970	-26%	-6%	0%
1974	15%	-5%	3%
1977	31%	14%	0%
1981	1%	2%	28%
1984	9%	2%	63%
1987	-5%	15%	-11%
1989	56%	22%	8%
1994	23%	-9%	4%
1999	71%	30%	5%
2004	25%	15%	-15%
2009	32%	-1%	-22%
2014	11%	10%	9%
2019	12%	10%	-3%

Source: Bloomberg: ALSI 1966 to 1994, ALBI 1966 to 1999. Morningstar: ALSI 1999 to 2019, ALBI 2004 to 2019. South African Reserve Bank: USD/ZAR 1970 to 2019.

In conclusion

Emotions intertwined with political beliefs present behavioural challenges, undermining the type of rational, coolheaded decision-making that investing demands. It's wise to acknowledge the fact that elections will most likely increase short-term volatility, but it should not affect your long-term investment strategy or financial plan. As with all uncertainties in the world of investing, diversification remains one of the most important and underrated strategies to deal with the wide range of outcomes. Recent bear markets in South Africa (and globally) have been driven far more by factors other than election outcomes.

At Morningstar, we continue to build robust portfolios for our clients that will deliver on their mandate, without taking any binary bets on macro factors or political outcomes. A well-diversified portfolio that is designed to meet your investment goals whilst remaining within your risk tolerance is a far better solution, and much more likely to result in long-term investment success than trying to predict election outcomes.

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+ t: (0)21 201 4645 + e: MIMSouthAfrica@morningstar.com + 5th Floor, 20 Vineyard Road, Claremont, 7708.