ABR Dynamic Funds – 3Q 2024 Newsletter

Positioning a Portfolio for the U.S. Election:
Do You Really Think You Can Outsmart the Market?

A common question we receive is how portfolios should be adjusted in anticipation of the 2024 U.S. Presidential election. Here's ABR's perspective on that.

Behavioral finance expert Joe Wiggins recently published a post discussing whether investors should make portfolio adjustments based on known, upcoming events. He offers a three-step test for evaluating this, to which we've added a logical fourth step.

For long-term investors, the process is straightforward:

1. **Does the event matter for long-term investment horizons?**
   If not, there's no reason to act. If so, move on to the next step.
2. **Is the event's outcome predictable?**
   If not, there's no reason to act. If so, move on to the next step.
3. **Will the outcome have a knowable impact on markets?**
   If not, there's no reason to act. If so, move on to the next step.
4. **If the outcome and its market impact are predictable, why isn't it already priced in?**
   If an event is important, predictable, has a clear market impact, and isn't already reflected into market prices, then short-term tactical moves might make sense. <u>But that's a very high bar, rarely met in reality.</u>

Step 1: Does the Event Matter?

Far fewer events have impacted long-term portfolios than most people assume. Over time, investors have navigated every kind of market and political scenario imaginable, and diversified long-term portfolios have continued to reach new highs.

Elections have been no exception. The average monthly return for the S&P 500 has been about 0.6%, and the average quarterly return around 2.0%. In election months and quarters, these figures have been 1.1% and 2.3%, respectively. The difference is not major, and volatility during election periods is similarly unremarkable.

Step 2: Is the Outcome Predictable?

Predicting election outcomes is harder than we think, largely because hindsight biases make past results seem obvious. In the case of the 2024 election, both polls and betting markets currently show it's about a toss-up. After the election, many people will claim they "knew it all along"—but right now, no one really does.

Step 3: Will Markets React Predictably?

Even when events seem significant, predicting market reactions is tricky. Take 2023, for example: amidst bank failures, U.S. debt ceiling tensions, multiple wars, and inflation concerns, the S&P 500 still posted a remarkable 26% return—much to the surprise of many experts.

The upcoming U.S. election might follow a similar pattern. The last two presidential elections brought major political shifts, yet the S&P 500 returned 11% and 3% in those months.

Step 4: Isn't It Already Priced In?

If you're aware of the election, so are your fellow investors. If the outcome and its market impact were truly predictable, they'd likely already be priced into the markets. If that's the case, it's hard to see why any opportunity for tactical adjustment remains.

Conclusion: Focus on What You Can Control

It's human nature to want to feel in control of each event, but, in investing, it's more productive to focus on what you can actually influence: risk, time, and diversification.

- **Risk**: Risk and reward are inseparable. Embrace risk as a part of risk premiums, which have been a driver of returns, but be wary of anyone promising returns without risk.
- **Time**: Stay invested. The only way to capture the risk premium has been by staying in the market. Often, the moments that have felt the riskiest are the ones that have delivered rewards.
- **Diversification**: Spread your risks. Diversification might not work perfectly at all times, but it has historically worked better for most people than trying to time the market or concentrating bets based on predictions.

Rather than trying to outguess the market or react to the election, maintaining a disciplined, long-term approach has been a more reliable path to success.

To learn more, please reach out to us at info@abrfunds.com.

References:

Joe Wiggins, Behavioural Investment. The Noise Factory, October 8, 2024.

Disclosures:

ABR Dynamic Funds, LLC

ABR Dynamic Funds LLC
17 State Street, Suite 725
New York, NY 10004
212-918-4664
info@abrfunds.com