



(UBS)

Politically driven pessimism can often be a costly mistake

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In recent election cycles, we've seen a consistent pattern in the confidence measures such as the University of Michigan Consumer Sentiment Index: opposition party investors are more pessimistic than incumbent party investors, and this sentiment shifts significantly when political power changes hands.

When your political party is in power, it not only improves your optimism about the economy—it also seems to have an impact on how you evaluate your current financial circumstances.

For example, on the cusp of the 2016 election, Republican consumer sentiment was 27% lower than Democrat sentiment. By the time President Trump was inaugurated, Democrat sentiment fell 24% and Republican sentiment rallied 56%, more than reversing the sentiment gap. The same thing happened in 2020, when Republican sentiment went from 35% higher than Democrat sentiment to 31% lower after the election.

Before the 2024 election, Democrats scored about 70% higher on the University of Michigan Consumer Sentiment Index. If the pattern holds, many Democrats are likely to become significantly more pessimistic in the months ahead, viewing President-elect Trump's victory as a risk to markets and the economy.

There is a risk that many Democrat investors will take this pessimism to heart and reduce their stock allocations. This would be a mistake, in our view, because such politically driven pessimism has often been a costly mistake for investors in past elections.

To demonstrate this, we looked at the impact of this partisan consumer sentiment from 2006 to 2024 in a [recent ElectionWatch report](#). To the extent that investors reduced portfolio risk to reflect their newfound pessimism about the

economy after losing past elections, they likely missed out on significant market gains in the early days of the incoming administrations.

For example, Democrats would have missed out on about 8% of potential growth during President Trump, while Republicans would have earned about 15% less under President Obama and 13% less under President Biden. In all, we estimate that trading based on the opposition party's consumer sentiment index readings would have underperformed a buy-and-hold investor by about 0.9% per year, or about 61% from September 2006 to October 2024.

For more, see [Don't just do something, stand there!](#), published 6 November, 2024.

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