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US PRESIDENTIAL ELECTIONS AND RECESSIONS

US Presidential

Elections and Recessions

As you know, I follow the business cycle, which describes the ebb and flow of the economy from boom to bust that drives asset prices and thus our investment choices.

Linear models in a cyclical world

Most economic models don't use the business cycle even though it clearly exists, which strongly suggests that economic linear models are wrong, yet economists sadly persist in this flawed linear analysis. This lack of acknowledgement of the business cycle is why so many economists are almost always wrong in their forecasts. Steady state analysis is proven time and time again to be junk.

Austrian economists (and a few others) do however accept the business cycle as given but they endlessly debate what causes this ebb and flow in the economy. In general, most opt for the credit cycle as the explanation without thought as to what creates the credit cycle and thus they fall into the economic model trap again.

The practical world

I live in the world of practical economics – where the investment rubber meets the economic road – so I ponder less about the detailed *why* and try to instead look at the *when* in terms of timing of the booms and busts.

Recession and Elections

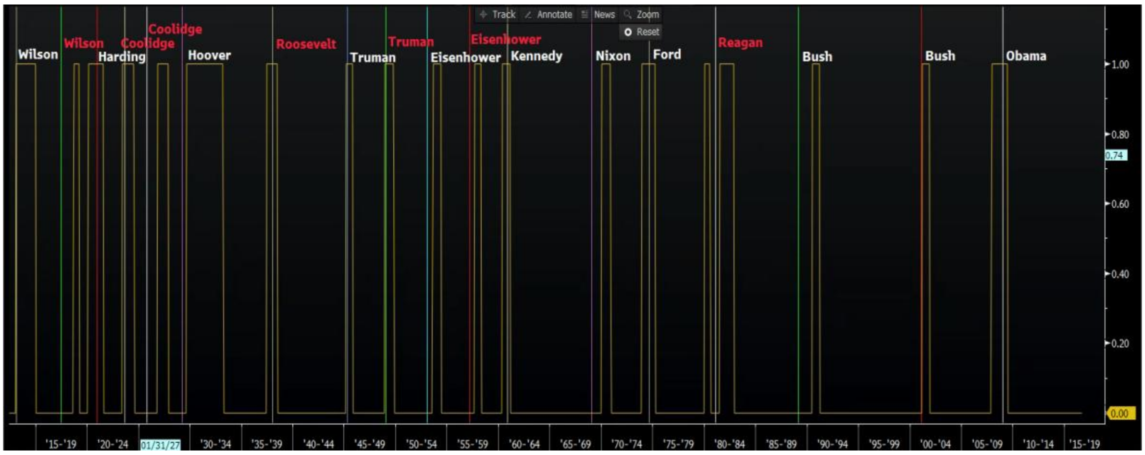
I recently noted that since 1910, the US economy is either in recession or enters a recession within twelve months *in every single instance* at the end of a two-term presidency… effecting a 100% chance of recession for the new President.

No recession without an election

I then spent some time looking at US recessions in general, and found that every single one occurred during, or just after, an election, *without exception.*

Not every single election sees a recession, only every two-term incumbent change. Some two-term Presidents saw recessions at their first-term re-elections too (Wilson and Eisenhower).

The following chart shows every NBER recession since 1910 (in yellow) with the new President after a two-term election marked in white and the new Presidents after a single-term presidency in red. Wilson and Eisenhower appear as both. Only Coolidge saw more than a year (sixteen months) from his second-term election and the onset of the subsequent recession at the end of WWI…



Just to be 100% clear, the coloured vertical lines show the election date. Every President's name written in white followed a two-term presidency. They each suffer recessions early in their presidency. And those names in red also suffered immediate recessions but after a single-term change of presidency. No recession except that of 1979 (clarified below) is not explained by its proximity to an election.

Some observers might suggest that the correlation between recession dates and election dates is spurious but I simply refuse to believe that based on the chart above. It is not a coincidence.

Why some new governments, after a change of a single-term presidency, don't see an immediate recession remains a mystery, but those instances are few: Clinton, Carter and Johnson. Of these only Johnson and Clinton did not see a recession at all. Carter got his recession at the end of his presidency, but don't forget Ford was not voted in so no election cycle occurred.

In the last 100 years, the recession of 1979 is the only recession not to occur around an election date (again, Carter came into office after Ford who did not undergo the election cycle).

Just mull that over…

Every single US recession bar one (with explainable circumstances) occurred around an election. Only two Presidents in history did not see a recession and they were inaugurated after single-term Presidents.

There are a few other things to note from this analysis:

Politics creates recessions

Firstly, *it is the political cycle that is the key driver of recessions* – governmental cycles in one way or another are an essential component. I am really not yet sure of the reason why two-term presidential cycles are so spectacularly consistent in provoking recessions but I do know that election dates are super helpful for predicting recessions and thus asset prices. The investment game is all about odds, and odds of 100% – even from a small data sample – are incredibly useful. Sure, it might not remain 100% forever but the probability is still going to be extremely high and that's all we need to make successful forecasts and investments.

[If you are not yet familiar with the relationship between the business cycle and asset prices, I'd suggest watching the video on the subject that I produced for Real Vision Television. The link is here:]

Politicians care about themselves

Secondly, it makes you question whether the governmental system in general has politicians' best interests at heart, or that of the country. It is difficult to believe it is primarily the country's economic wellbeing that the politicians care about when this cycle is so evident.

Trump will see a recession in 2017

Finally, bearing in mind the above, we have to acknowledge that there is an extremely high chance of a recession within the coming year with the imminent change of government in the US after a two-term presidency. *History would suggest that the odds are 100%.*

Should you really be betting on growth and inflation for 2017?

I very much doubt it.

I think that the current euphoria for equities and hatred for bonds is going to be exactly the wrong trade for 2017.

Raoul Pal
Global Macro Investor

Background

Raoul Pal has been publishing Global Macro Investor since January 2004 to provide original, high quality, quantifiable and easily readable research for the global macro investment community hedge funds, family offices, pension funds and sovereign wealth funds. It draws on his considerable 26 years of experience in advising hedge funds and managing a global macro hedge fund.

Global Macro Investor has one of the very best, proven track records of any newsletter in the industry, producing extremely positive returns in 8 out of the last 11 years.

Raoul Pal retired from managing client money at the age of 36 in 2004 and now lives in the tiny Caribbean island of Little Cayman in the Cayman Islands.

He is also the founder of Real Vision Television, the world's first on-demand TV channel for finance: www.realvisiontv.com

Previously he co-managed the GLG Global Macro Fund in London for GLG Partners, one of the largest hedge fund groups in the world.

Raoul moved to GLG from Goldman Sachs where he co-managed the hedge fund sales business in Equities and Equity Derivatives in Europe. In this role, Raoul established strong relationships with many of the world's pre-eminent hedge funds, learning from their styles and experiences.

Other stop-off points on the way were NatWest Markets and HSBC, although he began his career by training traders in technical analysis.

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Raoul Pal, Global Macro Investor, Little Cayman, Cayman Islands
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