

September turned out to be a positive month for both stocks and bonds as the markets digested a larger than expected 50 basis point cut from the Federal Reserve and economic data that supported the soft-landing narrative. For the month, all the major stock and bond indices we track for you in these updates increased with the biggest winner being the emerging markets:

S&P 500, 2.1 percent

Dow Jones Industrial Average, 2.0 percent

Russell Mid Cap, 2.2 percent

Russell 2000 (Small Caps) 0.7 percent

MSCI All Cap World Ex-US, 2.7 percent

MSCI EAFE, 1.0 percent

MSCI Emerging Markets, 6.7 percent

Barclays Aggregate Bond Index, [1.3 percent](#)

Our team was surprised at the 50-basis point cut and had expected a more modest 25 basis points. We worried that a too-aggressive cut might signal the markets the Fed believed a recession was more likely than did the markets. Fortunately, the economic data in September and so far in October, has assuaged that concern to some degree. In fact, Morgan Stanley just cut its calendar 2025 recession odds from 35 percent to 25 percent based on the economic indicators and the Fed's policy shift. [Lisa Shallett](#), our Chief Investment Officer, summed it up this way in her note from September 30th, "The commencement of Fed easing with a 50-basis-point rate cut has increased soft-landing prospects in our base case from 50% to 65%, with recession odds receding to roughly 25%. While the implication for US equities has been improving breadth and a shift in market narrative toward realization of ambitious earnings forecasts, the upshot for bonds has included a rapid steepening of the bellwether two-year/10-year US Treasury yield curve in the third quarter."

Our team continues to anticipate further market broadening in a bull cycle with other sectors and capitalizations playing catch-up to the Magnificent 7 and S&P500 – as opposed to valuations reaching more equilibrium from a decline in the last 18-months winners. In fact, the magnificent 7 actually peaked back in July, though the overall indices are higher – nascent evidence our advice is coming to fruition. As Morgan Stanley noted in this month's [On the Markets](#), "not only did the Nasdaq Composite Index and the "Magnificent Seven" peak on July 10, as Fed cuts finally came into view on improving inflation, but since then, market breadth has been excellent, with nearly three-fourths of all stocks beating the capitalization-weighted S&P 500, driving outperformance of the equal-weighted version."

It would not shock us at all to see a prolonged period of outperformance of small and mid-cap stocks, value stocks, international stocks, and emerging market stocks as the dollar weakens and interest costs decline during this Fed-cutting cycle.

On a totally different and election related note, you likely know already that we don't place a lot of stock in making market predictions based on election outcomes. However, our disinterest does not, at least on average, seem to lessen client's enthusiasm and certainty that a bad election outcome from their perspective spells certain financial doom. We are not saying that this election is not important. We are

also not saying that elections generally are not important. What we are saying is that they are both very difficult to predict and that stock markets have typically fared quite well under both Democratic and Republican regimes.

Richard Bernstein at RBA Advisor wrote an excellent piece on September 17th entitled "[Fade the Election.](#)" His point was much the same as ours. I quote directly:

"The market doesn't crash when the other side wins. The losing side in every Presidential election seems to predict the financial markets will be doomed. Yet, history shows that investors reaped double-digit annualized returns under every President except one in the last 45 years.

Table 1 shows S&P 500® annualized returns by Presidential time in office for each of the last eight Presidents. The S&P 500® had a negative compounded return only during Bush 43's time in office, which was called the "Lost Decade in Equities".

The S&P 500® tended to have meaningful positive returns regardless of a President's political party."

TABLE 1:
S&P 500® Annualized Total Return by Presidential Term*

President	Return
Carter	12.0%
Reagan	15.1%
Bush 1	14.6%
Clinton	17.5%
Bush 2	-4.5%
Obama	16.3%
Trump	16.3%
Biden**	12.9%

Source: Richard Bernstein Advisors LLC, Bloomberg Finance L.P.

*Presidential Term measured by Inauguration dates.

**Biden returns are calculated through 8/31/2024.

That said, if we had to bet on the outcome right now, we would bet on a split decision –meaning neither party sweeps the house, senate and the presidency. Thus, we do not think the market is likely to move dramatically this time on the morning of November 6th.

In Morgan Stanley's view and ours, the presidential election is simply too close to call in the electoral college, though Harris has enjoyed a slight but persistent lead in the national polling. That said, the polling errors the last several cycles have been extraordinarily high so we would not be shocked to see a

decisive presidential election in either direction. Betting markets currently [say](#) the race is essentially a tossup, with Harris at 51% chance to win and Trump at 49%. We like betting markets better than polls as a data point because they account both for intensity of support and popularity – something polls can miss.

The Senate on the other hand seems more likely than not to shift to the Republicans. Betting markets place that outcome at about a 70 to 75 percent probability. As Morgan Stanley notes in its [“US Policy Pulse: 2024 General Election Series,”](#) the Cook Political Report, “recently moved Montana Sen. Jon Tester’s race to Lean Republican from Toss-Up after polling showed a five-point average lead for Republican Tim Sheehy. The development in the Montana Senate race and the overall breakdown inherently puts the Democrats’ majority at risk. The retirement of Sen. Joe Manchin (D-WV) opens a seat in a state where Trump won 69% of the vote in 2020.” In a nutshell, picking up an almost certain victory in West Virginia and a likely victory in Montana puts Republicans in a strong position to take over the Senate. Betting markets have adjusted accordingly.

The House is a different matter altogether. We think the Democrats are more likely than not to take control of the house with a very slim majority. Morgan Stanley’s research folks sum it up this [way](#), “For example, CPR (Cook Political Report) rates 174 seats as Solid Democrat (not considered competitive) and 29 as Likely Democrat or Lean Democrat. Meanwhile, it rates 192 seats as Solid Republican and 16 as Likely Republican or Lean Republican (see Exhibit 1). If all seats are awarded to their projected parties, Republicans would control 208 seats to the Democrats’ 203, and (Republicans) would need to win just 10 of the 24 remaining races to which CPR assigns a Toss Up rating (most competitive). However, we note that enthusiasm for Harris, if continued, could translate to positive results for Democrats running in down-ballot elections.” Essentially, betting markets currently have the Democrats at about a 62 percent change to win the House because Harris’s polling advantage likely translates down the ballot in house races even if Trump ultimately prevails in the Electoral College.

Mathematically, taking all that together, it puts the odds of Republican sweep at around 15 percent, a Democratic sweep at around 10 percent, and a split decision at around the remaining 75 percent. In reality, the odds of a sweep are likely much higher as elections have a tendency to shift all in one direction at the end. But, in our opinion, even taking that effect into account, a sweep in either direction is still much less likely than a split decision. That’s all the more reason not to overact to the emotional impulse or trade a portfolio on the possibility of your side losing this election. It does mean however, that we think there is a good chance the individual Trump-era tax cuts might sunset in January of 2026 to some degree. We will write more about that in our November update once we see the election results.

As always, if you have any questions or concerns, please don’t hesitate to give any member of the team a call.

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