Monday 11 September 2023

focus

Ballots and bulls – Do elections impact financial markets?

Every three years New Zealand engages in the dance of the politicians, known as our General Election. Elections are often regarded as significant events, with the potential to shape the direction of a nation's policies and priorities. Given the attention and suspense they generate, the actual impact of elections on local financial markets is worth examining. A closer analysis reveals that while elections and changes in government introduce a level of uncertainty, their influence on financial market returns and economic performance is generally more limited than most surmise.

FORSYTH BARR

...common intuition might suggest that changes in government could be disruptive...

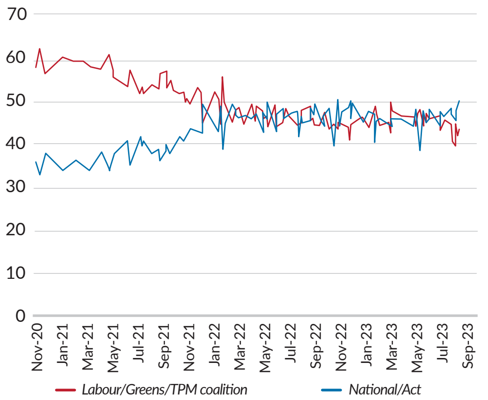
This article is up to date as of 4 September 2023

To the left or the right — does it matter?

As we enter the final countdown to Election Day, a change of government looks the most likely outcome based on recent polls. Although we acknowledge that a lot can happen even in a week in politics! A National-Act coalition appears poised to take over after two terms of Labour-led governments. While common intuition might suggest that changes in government could be disruptive, historical data shows that there is minimal difference in economic growth under left-wing or right-wing administrations. New Zealand share market returns have been notably higher under National-led governments, however, we believe that is more due to other factors than government policies.

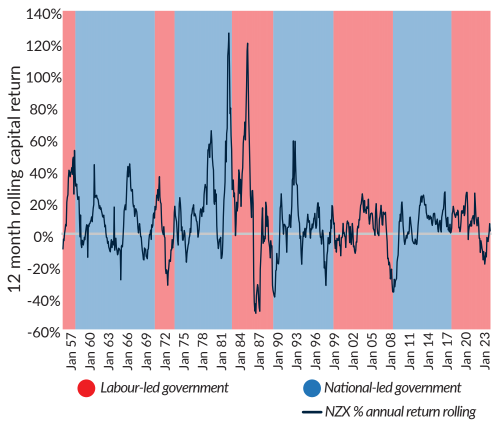
The approach of an election often casts a shadow of uncertainty for businesses. As parties present various policies, and potential shifts in governance loom, apprehension naturally prevails. While the unknown is often the scariest part, there is a general trend for business confidence to be higher under a National-led government (chart below). This aligns with the perception that right-wing policies tend to be more pro-business while left-wing policies support a higher role of the state in the economy.

NEW POLITICAL POLLS: SUGGEST A CHANGE IN GOVERNMENT IS LIKELY



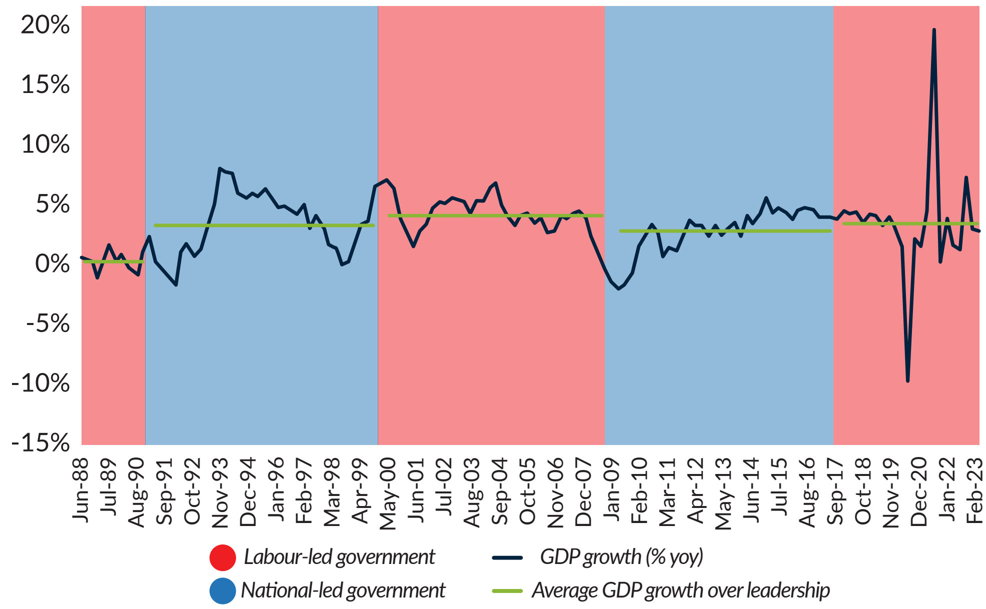
Source: Forsyth Barr analysis

ANZ BUSINESS CONFIDENCE SURVEY: BUSINESSES PREFER NATIONAL; POLITICAL BIAS?



Source: Statistics New Zealand, Forsyth Barr analysis

GDP GROWTH THROUGH ELECTION CYCLES: NOT A LOT OF DIFFERENCE BETWEEN RED AND BLUE



Source: Statistics New Zealand, Forsyth Barr analysis

While businesses prefer governments on the rights, analysing GDP growth in New Zealand through political cycles reveals little significant difference in economic output from which party is in government. Other factors, such as the global economy, timing within the business cycle, and interest rates, tend to carry more weight.

This time around, whoever wins will be facing tough headwinds from the economic climate. Interest rates are at the highest level in over a decade, the economy was in a technical recession at the start of this year and we expect the economy to remain sluggish over the next six to twelve months. Regardless of the victor in October, tough decisions await on balancing spending to support the economy while managing higher interest rates and potential debt.

What about financial markets?

Looking at the performance of the NZ equity market back to 1957, on average we have seen slight positive returns of 1.5% in the three months following the election of a National-led government and a -3.3% return following a Labour-led government being elected. When looking across the whole three-year government term, annualised returns have also historically favoured a National government. The NZX capital index has averaged a compound annual return of 8.3% under National and 2.2% under Labour. However it's crucial to note that Labour drew the short-straw in this contest - they were in power through the 1987 stock market crash, the bursting of the dot-com bubble, and the first half of the global financial crisis (GFC). In addition, numerous other factors significantly impact equity market performance, often far outweighing the influence of who's in charge at the Beehive. There have been strong and weak periods of performance under both Labour and National-led governments through history, and we caution against jumping to any conclusions from the headline comparative returns.

Policy tweaks unlikely to have much impact

In some elections specific policies can influence certain sectors or companies, and potentially their market values. For example, we have recently seen both National and Labour announce that they will remove structure depreciation expense on commercial property buildings — a temporary measure that was introduced in March 2020. This is estimated to increase the tax burden for the commercial property sector and have a negative impact on real estate investment trusts (REITs), particularly those with newer assets. This has already been factored into the share prices of these companies, given it's been clearly signalled and the policy change is agnostic of the election outcome.

TABLE 1: NEW ZEALAND ELECTIONS AND EQUITY MARKET PERFORMANCE

Election dates	NZX performance 3 months pre-election	NZX performance 3 months post-election	NZX performance over government term	MSCI world index performance over government term	Winning party/ coalition
27/10/1990	-23%	-15%	16%	16%	National
6/11/1993	15%	10%	1%	12%	National
12/10/1996	7%	7%	-2%	19%	National/NZFirst
27/11/1999	0%	-5%	-4%	-15%	Labour/Alliance
27/07/2002	-7%	3%	13%	18%	Labour/Progressive
17/09/2005	6%	-6%	-11%	-6%	Labour/Progressive
8/11/2008	-18%	-2%	-1%	8%	National/Act/United Future/Maori Party
26/11/2011	-5%	3%	13%	21%	National/Act/United Future/Maori Party
20/09/2014	0%	5%	10%	7%	National/Act/United Future/Maori Party
23/09/2017	2%	7%	13%	9%	Labour/NZFirst/ Green Party
17/10/2020	7%	4%	-5%	9%	Labour/Green Party

Source: Refinitiv, Forsyth Barr analysis

Looking at other policy details, we see only minor (if any) implications for most listed companies. Sectors such as agriculture, energy, construction, and housing are areas where there are some differing policies on the table.

Some of the proposals which could have sway include:

Labour is focused on moving the country to 100% renewable electricity generation by 2030 → ***net effect for generator-retailers will depend on specifics across ETS, decarbonisation and electricity policy.***

National is looking to reintroduce full interest expense deductibility for rental properties by April 2026, and reduce the bright-line test for capital gains on non-owner occupied property back to two years → ***positive for aged care stocks if property prices rise as a result***

National would push out the timing for farm-level emissions pricing to 2030 (rather than 2025 under Labour) → ***slight positive for agri sector generally but unlikely to give much benefit to listed companies***

Some of the minority parties have tabled policies that could have a more meaningful impact on certain sectors (Greens' broader climate change policies would likely make things tougher for the agricultural sector for example), but most of these are unlikely to get adopted wholesale in any coalition negotiations. Hence, it's a stretch to bake them into the central outlook at this stage.

Tax policies are also in the limelight this election, with a clear focus on individual tax and GST, but these are unlikely to have much of an impact on individual listed companies. Both major parties have ruled out a capital gains or wealth tax.

..., markets tend to breathe a bit easier once an election is out of the way...

Back to business after the election circus

Regardless of who the governing parties turn out to be, markets tend to breathe a bit easier once an election is out of the way for another three years. For investors with a medium or long-run time horizon, elections generally pass by without much (if any) lasting impact. As discussed, it is hard to determine convincingly that political outcomes consistently impact markets in one direction or other. For investors, it is important to keep in mind the economic environment, asset allocation, and your broader investment goals and time horizons. These factors will drive market performance over the long-term far more than the Beehive merry-go-round.

Zoe Wallis, CFA
Investment Strategist

If at any time you want to discuss investment options and opportunities, your Forsyth Barr Investment Adviser is available to provide you advice and assistance.

0800 367 227

forsythbarr.co.nz