

Hard Labour?

The forthcoming local elections have focused media attention on the potential for a Labour government led by Jeremy Corbyn. Mouhammed Choukheir, Chief Investment Officer of Kleinwort Hambros, analyses the historical record to see what such a government might mean for both economic growth and the performance of equity markets. Some of his findings may be surprising.

Local elections in the UK – coming in May – will be the clearest litmus test of the country's mood since last year's snap election. Conclusions will be drawn about the state of the parties nationally, notably the potential for a Labour government at the next parliamentary elections. If the headlines are to be believed, the Conservative party is heading for a rout; and this has raised what for some is the spectre of a Jeremy Corbyn-led Labour government raising tax rates sharply, and perhaps even placing controls on capital.

When it comes to elections, we have learnt to be sceptical about headlines. Before the 2015 general election, no party was expected to win outright. In fact, David Cameron led the Tories to a clear majority. In the subsequent Brexit referendum, his advisers and most pundits predicted a remain vote. When Cameron's successor, Theresa May, bowed to favourable opinion polls and opted to call a snap general election to bolster her party's lead and win a mandate in her own name, the Conservatives lost their majority and she lost face.

Such miscalculations occur often and everywhere. Like financial markets, politics is dependent on human behaviour, which is complex and unpredictable, and near certainties can turn out to be anything but.

With that in mind, we explore the question of a change in government in the UK in the same way we attempt to unravel the uncertainty of financial markets – by looking at historical data.

Breathe again

While this election carries new and unexplored questions for the UK, we have looked back at 118 years to see what history can teach us. In that time, Conservative governments have delivered average

annual GDP growth of 2.6%, appreciably better than their Labour counterparts (2.1%). However, Labour governments' record has been far from disastrous. In fact, the economy expanded during the tenure of every single Labour prime minister barring Gordon Brown. Removing the three Brown years – which spanned the pre-financial-crisis peak to the post-crisis trough – there is even less difference between the two parties.

Moreover, whether the government is Conservative or Labour has made little difference to equity market performance. In the 37 years since 1900 that began with Labour running the government, UK equities were up 7.7% per year on average in real terms (adjusting for inflation). For the 65 years when the Conservative party held sway, UK equities were up 7.9% annually on average. Indeed, Labour arguably has the better record: only one of its six prime ministers, Clement Attlee, presided over negative equity returns. By contrast, no fewer than four of the 14 Tory PMs – Sir Alec Douglas Home, Anthony Eden, Edward Heath and Neville Chamberlain – saw total returns from equities fall in their tenure.

Interestingly, when the now defunct Liberal party – a very different entity from today's Liberal Democrats – was in charge for 16 years in the early 20th century, GDP growth and equity returns were abysmal, with annual averages of 0.1% and –0.7%, respectively. If anything, one should hope for a continuation of the two-party system of successive Conservative and Labour governments – the only other party that has run the show had terrible results.

Another observation was teased out from the underlying data: political change appears to have an impact on equity performance. In years when there is no change in Prime Minister, equity performance averages about 4.8%. However, in years when the Prime Minister changes, equity performance is 13.0% in real terms. One likely explanation is that, before an election or in periods of political turmoil, investors are obsessed with all the things that might go wrong. We may be in such a period now. Inevitably, when that election or choppy period has passed, investors realise that the UK's powerful national institutions remain strong, and a sense of relief may well cause markets to rally.

We can draw an important inference about the value and depth of the UK's institutions. No matter who is in power, or what the pre-election rhetoric has been, a strong system of checks and balances exists. This helps temper any leftward or rightward lurch of policy, nudging it back towards the moderate centre.

Moreover, no government should take too much credit for growth or investors' returns: economies and markets are affected by far more than just prevailing domestic politics and policies. In the end, both major parties recognise the foundational role of global market forces in the UK's prosperity, and both uphold that the provision of a welfare state is a basic principle of government. When it comes to continuing growth and conditions conducive to favourable investment returns, although each period is always different, the detail tends to matter little over the long arc of history.

- 1 Total return calculated by taking the cumulative return/loss from capital appreciation and income (dividends, coupons, etc.) using Barclays Equity Gilt Study Data.
- 2 PM at beginning of year given credit for entire year.
- 3 Real GDP data taken from a Bank of England continuous time series that runs from 1700: 1870-1913 Solomou and Weale (1991) balanced measure of GDP at constant 1900 factor cost; 1913-20 Feinstein's Compromise index of GDP at factor cost available in Mitchell; 1920-48 Sefton and Weale (1995) balanced measure of GDP; 1948-2009 ONS GDP at factor cost, chained-volume measure, 2006 reference year prices.

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UK Prime Ministers since 1900	Years in Office	Total Real Return on UK Equities (%)	Average GDP Growth
Conservative	65	7.9	2.6
Alec Douglas Home (1964)	1	-9.3	5.6
Andrew Bonnar Law (1922 - 1923)	2	20.6	4.2
Anthony Eden (1956 - 1957)	2	-8.0	1.8
Arthur James Balfour (1903 - 1905)	3	5.8	1.2
David Cameron (2011 - 2016)	6	5.1	2.1
Edward Heath (1971 - 1974)	4	-11.3	2.9
Harold Macmillan (1958 - 1963)	6	18.2	3.4
John Major (1991 - 1997)	7	13.9	1.9
Margaret Thatcher (1980 - 1990)	11	12.3	2.5
Marquess of Salisbury (1900 - 1902)	3	3.7	1.3
Neville Chamberlain (1938 - 1940)	3	-9.9	5.1
Stanley Baldwin (1925 - 1929; 1936 - 1937)	7	5.7	2.9
Theresa May (2017)	1	9.1	1.8
Winston Churchill (1941 - 1945; 1952 - 1955)	9	14.0	2.1
Labour	37	7.7	2.1
Clement Attlee (1946 - 1951)	6	-0.2	1.7
Gordon Brown (2008 - 2010)	3	1.6	-0.9
Harold Wilson (1965 - 1970; 1975 - 1976)	8	15.7	2.3
James Callaghan (1977 - 1979)	3	8.5	3.4
Ramsay MacDonald (1924; 1930 - 1935)	7	13.0	1.8
Tony Blair (1998 - 2007)	10	4.2	2.9
Liberal	16	-0.7	0.1
David Lloyd George (1917 - 1921)	5	0.7	-4.4
Henry Campbell-Bannerman (1906 - 1908)	3	3.9	0.4
HH Asquith (1909 - 1916)	8	-3.3	2.9
Grand Total	118	6.7	2.1

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