

# U.S. Presidential Elections and Implied Volatility: The Role of Political Uncertainty

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## Abstract

This paper focuses on the effects of political uncertainty on implied stock market volatility during U.S. presidential election cycles. Using monthly Iowa Electronic Markets data over five elections, we document that stock market uncertainty, as measured by the VIX volatility index, increases as the probable winner of the presidential election becomes less uncertain. The association between implied volatility and the election probability of the eventual winner is positive even after controlling for changes in overall election uncertainty. These findings indicate that the presidential election process engenders market anxiety as investors form and revise their expectations regarding future macroeconomic policy.

*JEL classification:* E60, E65, G10, G13, G14, G18

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In brief, our empirical findings indicate that political uncertainty around U.S. presidential elections affects option-implied stock market volatility. Using monthly data on the IEM presidential contracts over five elections from 1992 through 2008, we document that the implied volatility of the S&P 500 index increases as the probable winner of the presidential election becomes less uncertain. The association between monthly changes in implied volatility and the election probability of the eventual winner is positive even after controlling for changes in overall election uncertainty. Hence, our results indicate that the presidential election process engenders market anxiety as investors form expectations

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examines the relationship between opinion polls and implied volatility around the British parliamentary election of 1987, while Bialkowski et al. (2008) conduct a robustness check of their findings using implied volatilities from 11 OECD countries. Vahamaa and Aijo (2011) document that monetary policy decisions of the Federal Reserve affect implied volatility.