Investors often worry about poor stock returns during election years, and that's not surprising, given the idea that markets dislike uncertainty. But while election years are often volatile, the truth is that over the years has tended to be good.

Between 1937 and 2022, for example, the S&P 500 index has posted an average annual return of 9.9% during presidential election years. You can rest assured that emotions will be in full swing as the November election approaches. But where your investment portfolio is concerned, it's important to be calm and rational, to minimize your risk and be ready to seize opportunities.

In presidential election years, the market volatility tends to be front-loaded into the first half of the year. That's when candidates, campaigning in the primaries, tend to make extreme policy proposals. It doesn't matter that they'd likely never become law: The point is to appeal to voters on the far ends of the political spectrum who play an outsized role in selecting presidential candidates.

By the time the general-election campaign is in swing, the rhetoric has typically calmed down a bit, and markets start to gain some traction. Opportunities to invest will present themselves throughout the year.

But first, it's important to evaluate the risk in your portfolio. That's because the large-cap stocks that carried 2023's big returns, including the big rally at the end of the year, will likely cool off.

If you've owned any of the "Magnificent 7" stocks over the past year or two—Apple, Microsoft, Alphabet, Amazon, NVIDIA, Tesla and Meta Platforms—those stocks could be seriously overweighted in your portfolio right now. And given their inflated prices, they could do a nosedive during the periods of volatility and set you back significantly.

In my view, small- and mid-cap stocks are poised to have a strong year. They were largely overlooked last year, and broadly speaking they're priced attractively. Furthermore, smaller-cap stocks tend to benefit strongly from falling interest rates, and it's widely believed that the Federal Reserve is done raising rates and will start cutting them in 2024.

As for new investments, there's plenty of opportunity, and many companies could become more efficient and profitable thanks to the widening adoption of artificial intelligence. I believe AI could spur the next growth wave of corporate profits. As always, we want to wait for an attractive price before buying any stock. In the meantime, you might want to park your cash in three-months Treasury bills, which are currently yielding an attractive 5.45%.

Don't hesitate to reach out to us if you'd like to review the risk level of your investment portfolio and identify the stocks that could power your portfolio for the coming year.