*"During an election campaign the air is full of speeches and vice versa."*

- Henry Adams

One of the lasting lessons from the 2016 Presidential election is that polls and pundits can be wrong. While early, the 2020 election appears to be tilting in favor of the Democratic party – though, again, that would be relying on fallible polls and pundits. Regardless of the election outcome, we believe the current recession and pandemic response will lead to an expansion of government's role in society, as it has with past major crises.

From an investment perspective, we are interested in exploring potential fundamental changes in policies, programs, and budgets that might accompany the election of one of the presidential candidates. In this piece we will look at three areas that may impact the investment landscape – taxes, trade, and government spending.

### *Tax Policy*

Republican/Trump: In December 2017 President Trump signed the Tax Cuts and Jobs Act (TCJA) lowering tax rates for individuals, eliminating/capping many itemized deductions, and reducing corporate tax rates from 35% to 21%. If re-elected, expect the administration to push for provisions of the TJCA to become permanent (they expire in 2026) and possibly lower corporate and individual rates further. Reduction of capital gains rates, indexing of capital gains for inflation, and greater deductibility of corporate investments are also being discussed.

Democratic/Biden: Current proposals would repeal much of the TCJA starting with reverting to prior individual tax rates (39.6% from 37%) for anyone making over $400,000 per year. In addition, earnings over $400,000 would be subject to a new 12.4% Social Security tax – split between employer and employee. Long-term capital gains and dividends would be taxed at 39.6% for those making over $1 million. The step-up basis at death for capital gains is eliminated. Corporate tax rates would rise to 28% from the TCJA 21% rate, but lower than the pre-TCJA rate of 35%.

*Comment*: At this point neither party has specifically addressed the growing deficit and ultimate cost of the COVID-19 fiscal response. With a Democratic victory in November, we could see a wealth tax seriously considered to pay for these programs.

### *Trade*

Republican/Trump: Under President Trump, trade, trade wars, and the implementation of his "America First" policies have taken center stage. Trade agreements have been renegotiated with Mexico, Canada, and South Korea in the interest of fairness, balance, and creation of US jobs. The US has withdrawn from the TPP and been highly critical of the WTO. Tariffs have been used as the "stick" to level/tilt the playing field and have led to escalating trade wars - with China being the primary focus. If re-elected, the transactional, bilateral, and unpredictable nature of current trade policy is expected to continue.

Democratic/Biden: The COVID-19 recession may have altered the Democratic/Biden position. The "Build Back Better" and "Buy American" approach appears to favor the rebuilding of US markets and supporting working families before addressing trade on a global level. We would expect a new administration to reengage with the TPP and the WTO to increase foreign investment in the US. China, the world's second largest economy, presents a challenge as unfair trade practices (acknowledged by both parties) have persisted. The current administration has taken an aggressive approach to resolution with unknown long-term results. A new administration will inherit this confrontation and need to address this struggle for global economic leadership.

*Comment*: While there is clearly a difference in approach and rhetoric to trade issues, we find the actual positions to be fairly similar. America First has been the Republican mantra under this administration and the Democrat position now appears to be less focused on globalization, perhaps as a result of the pandemic and related recession. Trade agreements differ slightly with Republicans moving toward bilateral agreements and the Democrats favoring multinational arrangements. The parties share a "tough on China" economic attitude, although this relationship is more complicated when adding in national security and human rights issues.

***Pandemic Response/Government Spending***

Republican/Trump: The arrival of COVID-19 pushed the global economy into recession and the administration along with the Federal Reserve, Treasury and Congress responded with unprecedented stimulus. To date bills totaling $3 trillion have passed. Republicans have eyed a $1 trillion "Phase Four" relief package, while Trump has indicated $2 trillion is his preference (perhaps knowing that it would be popular among voters but unlikely to have party support). An infrastructure bill, a measure supported by both parties, is on the Trump agenda with a $1 trillion price tag. However, many Republicans are unwilling to support a bill that large.

Democratic/Biden: The Democrat controlled House passed an additional $3 trillion "Phase Four" stimulus bill in May that never made it through the Senate, and recently a $1.5 trillion infrastructure bill – both confirming the party's desire to go big on future spending. Biden recently unveiled a "Buy America" program with a $700 billion price tag and an infrastructure/climate change program for $2 trillion.

*Comment*: Regardless of the election outcome, it's clear that trillion-dollar programs are central to each party's economic recovery plans. The traditional Republican stance on government spending has moved more closely to the Democratic position of fiscal stimulus being a fundamental part of restoring US economic success.

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Lastly, we have been asked about the possibility of a Democratic sweep this fall. As we said in the first paragraph, polls and pundits are unreliable. However, we did look back at results from one-party control over the last 50 years to assess the market's reaction:

| *Party* | **Democratic** | **Democratic** | **Republican** | **Democratic** | **Republican** |
|---|---|---|---|---|---|
| *President* | **Carter** | **Clinton** | **Bush 2** | **Obama** | **Trump** |
| *Election* | 11/3/1976 | 11/4/1992 | 11/5/2002 | 11/5/2008 | 11/9/2016 |
| *Majority* | 4 Years | 2 Years | 4 Years | 2 Years | 2 Years |
| **S&P 500 Return** | **% Return from Election Date** (annualized over 1-year) | | | | |
| 1 Month | -0.4% | 3.4% | 5.9% | -7.2% | 3.7% |
| 3 Months | 0.2% | 5.6% | -3.0% | -14.1% | 7.8% |
| 1 Year | -3.1% | 13.9% | 21.9% | 16.4% | 27.4% |
| 2 Year | 6.3% | 15.9% | 13.8% | 11.0% | 15.8% |
| 3 Year | 9.6% | | 12.7% | | |
| 4 Year | 14.6% | | 6.9% | | |

Economic conditions varied greatly in each of these periods. Despite that, in each of these instances, the stock market was higher over the period of one-party control – and, with one exception, returns were in line with or slightly higher than the 11% average annual return of the stock market over the last 50 years.