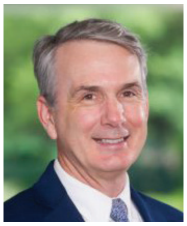
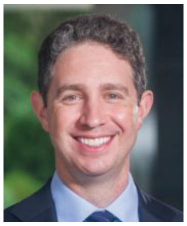
WHITE PAPER

2020 Election

While COVID-19 has dominated the headlines for the first half of the year, Election 2020 has become the focal point of the news cycle and will dominate most people's attention between now and November. Even with so little time until the elections, there are still a number of unknowns related to candidate platforms and their priorities in the next administration. With this in mind, let's take a look at the issues most material to investment markets and try to handicap the impact of the various outcomes.



SAM FRAUNDORF, CPA, CFA
PRINCIPAL &
CHIEF INVESTMENT OFFICER



JASON P. LIOON, CFA
PRINCIPAL & DEPUTY
CHIEF INVESTMENT OFFICER

Fiscal Stimulus and Economic Support

Even with an optimistic view of a highly effective vaccine becoming widely available in the first half of 2021, the economic impact from the virus will still be felt after the election is decided. There are the issues of vaccine distribution, continued healthcare system support, commerce impacts, schools and unemployment to address in 2021. Congress is continuing to debate a fifth bill to aid the economy in 2020, so the extent of additional programs is uncertain. More direct support for businesses would tend to be more favorable for equities, while more direct support at the household level might have longer-term impacts. We would expect different approaches to the government's role in addressing the economic effects of the pandemic within Congress, and certainly between President Trump and former Vice President Biden.

Tax Policy

Perhaps the greatest difference between Trump and Biden is tax policy. The Trump administration made substantial tax cuts for both individuals and corporations during its first term. While this led to an increase in the budget deficit, it helped to improve household income and corporate earnings and helped fuel 20%+ returns for stocks in 2017.

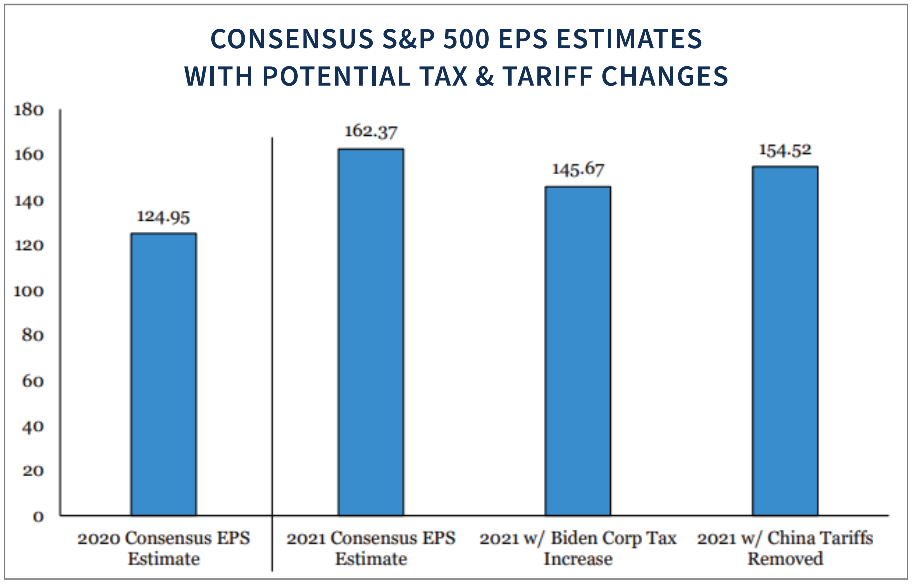
The President has not laid out any significant changes to his tax policy if he were to win a second term. It is fair to assume that he would likely continue with the status quo, potentially adding some temporary tax relief associated with COVID stimulus.

Biden, on the other hand, has laid out some substantial tax policy changes as part of his platform. These include:

1. Increasing the individual income tax rate for the top bracket
2. Imposing social security payroll tax on wage income over $400,000
3. Increasing capital gains and dividend tax rates for those earning more than $1 million
4. Eliminating the Trump corporate tax cuts, bringing the corporate tax rate to 28% from its current 21% level.

continued on next page ›

Although initially focused on corporations and the top 1% of taxpayers, these changes would all mean substantial tax increases. For investors, we believe an increased corporate tax rate would be the most significant. If the corporate rate is raised to 28%, it would immediately decrease S&P 500 earnings by more than 10%. However, it is currently believed a corporate rate increase might be somewhat mitigated by removing most Trump-era tariffs, directly benefitting firms with sales currently subject to these payments.



Source: Strategas

Health Care

Biden has made a “Public Option” for health insurance part of his platform. While this is an area for which there are a number of potential approaches – we would need a separate paper to discuss them all – it is fair to describe it as a variation on the “Medicare for All” proposals that were floated by Bernie Sanders and others. Such a fundamental change in public health insurance could potentially have a large impact on the health care sector. Insurers and drug companies would likely see their margins compress, and concern that such an option might be a bridge to a single-payer system would weigh heavily on healthcare valuations.

continued on next page ›

This policy change remains highly controversial, however, and would likely require a Democratic sweep of Congress and the White House to have a chance for implementation. It might also require circumventing the rules of order in the Senate to eliminate the chance of filibuster. If Biden were to pursue this policy, he would have to make it the centerpiece of his legislative agenda, and the ensuing political battle would likely be long and arduous with other important policies falling by the wayside in the interim. As we saw early in the Clinton administration, focusing on overhauling the healthcare system is politically risky and can hijack an entire presidential agenda.

What's Likely to Happen?

The economic impact of the virus during the first two quarters has led to the most severe contraction in the U.S. economy in history. As reflected in the chart below, recessions leading up to a presidential election have generally spelled doom for the incumbent party, as many "swing voters" simply vote their pocketbooks. If they are happy with their economic situation, they support the incumbent. If they are not, they look to change from the opposition party. Today, that happiness can be approximated by the level and severity of unemployment, the impact of the virus, and the government's actions at the individual and family level. By those metrics, the current environment points to trouble for President Trump this November and explains his current lagging position in most polls.

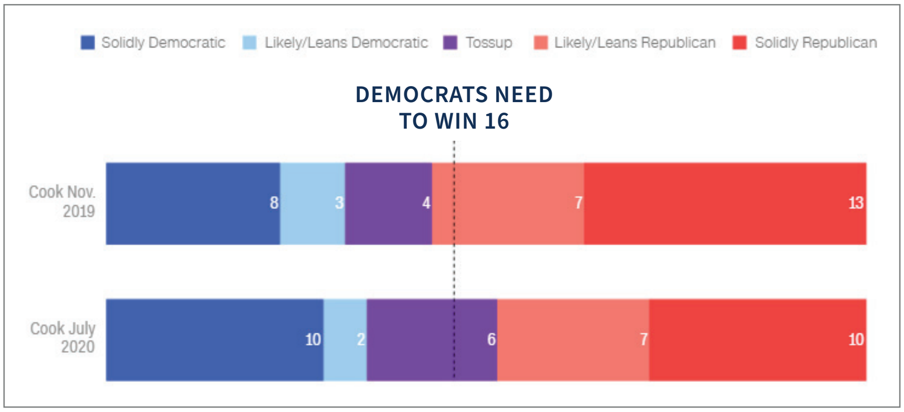
NO RECESSION TWO YEARS BEFORE ELECTION		
PRESIDENT	RECESSION?	RE-ELECTED?
Obama	No	Yes
Bush II	No	Yes
Clinton	No	Yes
Reagan	No	Yes
Nixon	No	Yes
LBJ	No	Yes
Eisenhower	No	Yes
Truman	No	Yes
FDR	No	Yes
FDR	No	Yes
FDR	No	Yes
Wilson	No	Yes

RECESSION TWO YEARS BEFORE RE-ELECTION		
PRESIDENT	RECESSION?	RE-ELECTED?
Bush I	Yes	No
Carter	Yes	No
Ford	Yes	No
Hoover	Yes	No
Coolidge	Yes	Yes
Taft	Yes	No

continued on next page ›

But this year may be unlike any other in the memory of the voting public. While this recession has been severe, projections are for a robust recovery in the third quarter. This could lead voters to feel better about their economic situation as we get closer to the election. While predicting an election is always difficult, the current one is particularly challenging as reflected in recent polling numbers that are similar to those from 2016 which showed Hillary Clinton ahead of Trump right up to the election.

More important than the presidency, though, is the Senate. Our system of government limits what the president can do alone, and progress can be slowed by a divided Congress and very nearly halted by an opposition Congress. While the House appears to be solidly in Democratic hands, the Senate is another story. With 35 seats up for grabs, the Democrats would need 16 in order to garner a majority. While such an outcome appeared unlikely late last year, the probability is increasing as some formerly solid Republican seats now appear to be in potential danger.



Source: The Cook Political Report / Graphic: Christopher Hickey, CNN

If Congress remains divided, either a second Trump term or a Biden win could be met with significant legislative opposition forestalling any meaningful policy changes for either side. However, a Democratic sweep is a real possibility and could lead to significant reforms.

continued on next page ›

What's the Potential Impact for Investors?

Every four years we field a number of questions about what the next presidential election will bring and how it will impact markets. The coming election has understandably attracted more attention than usual given the polarized nature of today's political environment. As we have highlighted, the two candidates would undoubtedly pursue very different policy agendas over the next four years, with a wide spectrum of potential outcomes. However, from an investment standpoint the reality is that the president actually has a fairly limited ability to influence markets.

Markets hate uncertainty. As such, the tendency has been that a resolution of an election, often leads to a stock market "relief rally," regardless of which party wins. Additionally, the actual impacts to earnings, GDP and employment tend to take a longer time to unfold, which means markets will need some time to digest not only election results, but also the probabilities and consequences of the winning party's policy agenda.

As reflected in the below chart, history shows that there is no direct correlation between equity market performance and which party holds the presidential office.

PRESIDENT	POLITICAL PARTY	YEARS IN OFFICE	S&P RETURN (%)
William J. Clinton	D	1993-2001	210
Barack H. Obama	D	2009-2017	182
Dwight D. Eisenhower	R	1953-1961	129
Ronald W. Reagan	R	1981-1989	117
Harry S. Truman	D	1945-1953	87
George H.W. Bush	R	1989-1993	51
Lyndon B. Johnson	D	1963-1969	46
Donald J. Trump	R	2017-	43
Jimmy E. Carter	D	1977-1981	28
Gerald R. Ford	R	1974-1977	26
John F. Kennedy	D	1961-1963	16
Richard M. Nixon	R	1969-1974	-20
George W. Bush	R	2001-2009	-40

continued on next page ›

Strategas Partners reviewed equity returns since 1933 and found that the best U.S. returns have come under a Democratic President and Senate and a Republican House, at 13.6% per year. Such an outcome this year would require a change in the executive branch and both legislative branches. Based upon current polls (which will probably change more than once before November!), the most likely outcome at this point is a Democratic House and Presidency, and a Republican Senate, a combination not seen since Grover Cleveland was elected in 1886.

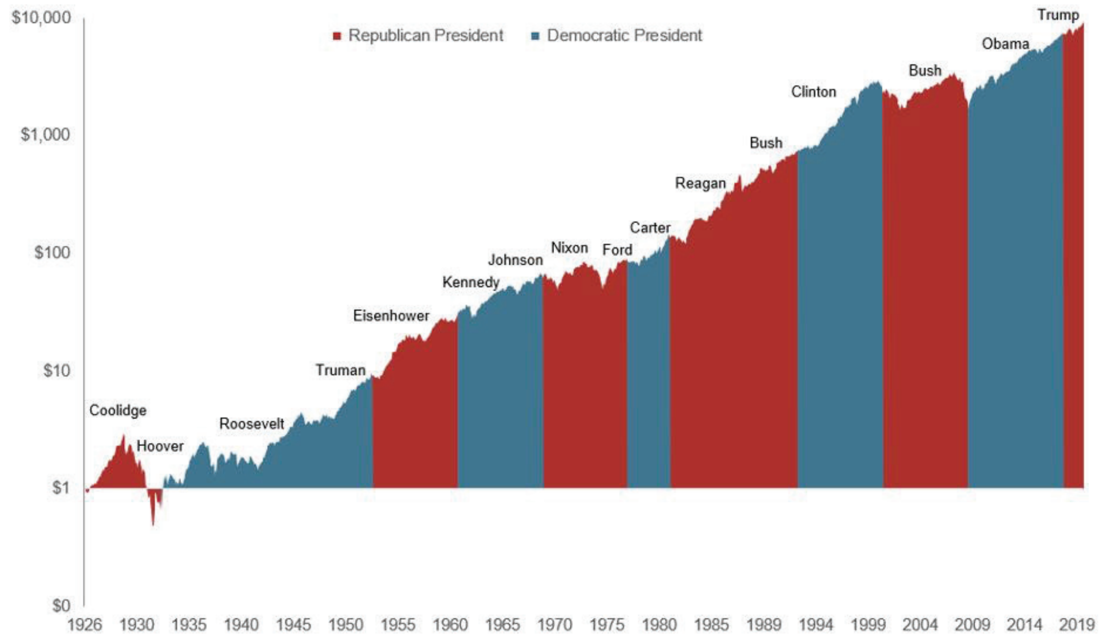
Often overlooked by election followers is the importance of Federal Reserve policy. In our increasingly partisan world, media headlines highlight the differences between political parties and often instill a level of fear in voters. But markets tend to watch the Fed much more closely than the president. As previously discussed, candidate platforms are often quite different than eventual policy implementation. Because the Fed does not have to deal with political negotiations, their policies have a much more direct impact on the economy and markets. Chairman Powell has made it clear that the Fed will remain accommodative by keeping interest rates low and providing economic backstops as needed to wade through the pandemic. These assurances have been a primary reason why equity markets have rebounded to pre-COVID levels, and why markets have not yet declined in the face of a potential Democratic sweep.

In our increasingly partisan world, media headlines highlight the differences between political parties and often instill a level of fear in voters.

continued on next page ›

From an investment perspective it is important to remember that over the last 100 years U.S. policy has changed countless times. As reflected in the graph below, changes may be bumpy in the short run, but equity markets have absorbed them and pushed higher. Consequently, we would encourage investors to remain focused on the long term and not on prospective policy changes that may or may not come to pass. The key is to take advantage of what we know, when we know it. Guessing or making changes to a well-constructed long term investment plan based on political fears is generally a bad plan.

GROWTH OF $1 INVESTED IN THE S&P 500: JANUARY 1926 - DECEMBER 2019



We do think it makes a lot of sense to consider some of the tax and estate planning opportunities that are currently available because some of the favorable tax law currently in place could change after the election. We will publish a discussion covering the planning alternatives in coming weeks.

ATLANTA
400 Galleria Parkway, Suite 1400
Atlanta, GA 30339
Phone: 770.226.5333

GREENSBORO
701 Green Valley Road, Suite 300
Greensboro, NC 27408
Phone: 336.217.0151

MEMPHIS
6075 Poplar Avenue, Suite 850
Memphis, TN 38119
Phone: 901.761.7979

NASHVILLE
3102 West End Avenue, Suite 600
Nashville, TN 37203
Phone: 615.386.7302