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Investment Strategy Insights

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Elections Ahead – Noise or Substance?

- The Election Reaction Function
    - Markets may be near-term sensitive to the election, but the recovery from the pandemic should remain most important
- To V or Not to V…
    - The rebound has been V-like, but the remaining recovery will likely move slower until a vaccine becomes available
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The Election Reaction Function

- **Near-term Political, Long-Term Apolitical.** Market volatility around the election is possible and already built into investor expectations. The market typically exhibits sensitivity to elections in the short term, as the potential for policy change weighs on investors' minds. Currently, VIX futures for November 15th are several points above their mark in September. However, over a longer window, historical data shows that there is no clear relationship between equity returns and election results.

- **Potential for Policy Change** With Biden given a 60% chance to win the election, according to PredictIt, investors are preparing for a policy shift. A Democratic White House would likely bring with it greater regulation and potentially higher taxes, but would also endorse a larger, more comprehensive stimulus bill. While the approaches espoused by Biden and Trump seem quite different, the total impact of either is likely neutral-to-net-positive for the economy. The more differential impact is the share of the economy – whether the split will favor workers or their employers (corporations).

- **A History of Less-than-Expected Follow-Through.** In the past, a recurring theme post-election is the lack of policy implementation. Candidates often have a long list of reforms that don't get completed during the presidency. The likelihood that Trump or Biden can fully enforce their agenda will depend on various political factors such as the makeup of Congress. The most important factor for investors will likely remain the economic recovery from COVID-19, as opposed to any political aspect.

Markets may be near-term sensitive to the election, but the recovery from the pandemic should remain most important

Chart of the Week:

A Range of Three Economic & Market Bottom Lines

	Scenario 1: Democrat Sweep	Scenario 2: Biden Win / No Sweep	Scenario 3: Trump Win / No Sweep
Policy Environment	Democrat Control / Potential Larger Policy Shifts	Gridlock / Modest Policy Shifts	Gridlock / Status Quo
Fiscal Stimulus / Infrastructure	Larger Package Likely	Larger Package Possible	Smaller Package Possible
Tax Reform	Corporate & Personal Tax Increases More Likely	New Legislation Less Likely, Some Tax Cuts Expire	Possible Tax Cut Extension and/or More Cuts
Minimum Wage	Federal Mandate Possible	Less Likely	Not Likely
Corporate Regulation	More Regulation	More Regulation	Less Regulation
Trade Policy / Int'l Relations	More Predictable Coordination with Allies	More Predictable Coordination with Allies	Less Predictable
Bottom Line	**Net Positive for Economy / Less Beneficial to Companies**	**Net Positive for Economy & Companies**	**Most Beneficial to Companies / Less Positive for Economy**

Source: Glenmede
The table shows key potential economic policy shifts that are likely to result under various potential outcomes from the 2020 presidential and congressional elections.

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To V or Not to V…

- **More Natural Disaster than Typical Recession.** The COVID-19 'recession' has behaved differently from a traditional recession, exhibiting the potential for a faster snapback as historically seen following the economic impact of natural disasters. U.S. initial jobless claims, which reached almost 7million in late March, have already declined to 787,000 and those remaining have classified themselves mostly as temporarily unemployed. Economists' consensus estimates show a 3rd quarter rebound in real GDP of 29.3%, which would be one of the steepest in history.

- **China's Full V.** China's recovery appears to be following a full V-rebound trajectory. After its initial decline earlier this year, China's economy has rebounded quickly back to previous levels and appears likely to deliver 2.2% growth in 2020. China's government instituted economic shutdowns, contact tracing and medical responses to the outbreak quickly, and its population has been effective in mitigating risk (e.g. wearing masks, social distancing). Stamping out reinfection early has permitted China the flexibly to reopen its economy more quickly without as much risk of contagion.

- **US.. Reopening Was V-like…** Glenmede's Reopening Index exhibited a quick rebound to over 60% U.S. economic activity regained, but its climb to the recent near-80% level has been much slower. It appears that a fast recovery beyond this point requires re-engaging in economic activity that requires more in-person interaction. Caution and a gradual reopening from this point forward appears warranted prior to the wide distribution and availability of one or more approved vaccines.

The rebound has been V-like, but the remaining recovery will likely move slower until a vaccine becomes available

Earnings…Better than Before

- **Earnings Results Appear Encouraging.** Roughly one-fourth of companies in the S&P 500 have reported their Q3 earnings, drawing quite the contrast against the downside surprises and downward revisions that dominated the first half of the year. Of the companies that have already reported, 83% of companies have delivered both EPS and revenue results ahead of expectations. In aggregate, earnings results have surpassed expectations by 18% on average, higher than the typical earnings season.

- **Clawing Back to Normal.** Earnings estimates for this quarter are currently at $32.95 per share for the S&P 500, a significant jump higher than Q2 which finished at $28.22, but still well below their previous high. Consensus estimates, however, now point to earnings reaching their previous high by the third quarter of 2021. The gradual climb back to normal reflects the ongoing reopening as well as attempts by businesses to control costs during the pandemic.

- **Disparate, but Improving Results.** The healthcare and consumer staples sectors are the only sectors in the S&P 500 expected to deliver positive EPS growth on a year-over-year basis, at rates of 3.5% and 1.1%, respectively. The energy and industrials sectors are expected to be absorb the hardest blows to profitability, with blended EPS growth figures of -124.6% and -59.1%, respectively. That said, results appear to be improving, since energy and industrials posted -164.0% and -83.8% earnings losses on a year-over-year basis just last quarter.

The strong Q3 earnings season draws a strong contrast to the weak Q2 earnings season

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