

December 14th, 2020

2021 Themes

- It Ain't Over 'Til the Peach State Sings
 - The most likely outcome in '21 is economically tenable political gridlock, but investors shouldn't entirely write off the alternative
- COVID-19 Endgame
 - Rising cases may cause near-term disruption, but the outlook for a vaccine-induced recovery remains a distinct tailwind
- Anticipating the "Next Normal"
 - Expect larger federal debts/deficits, higher productivity and inflation fears to be the reality in a post-pandemic economy

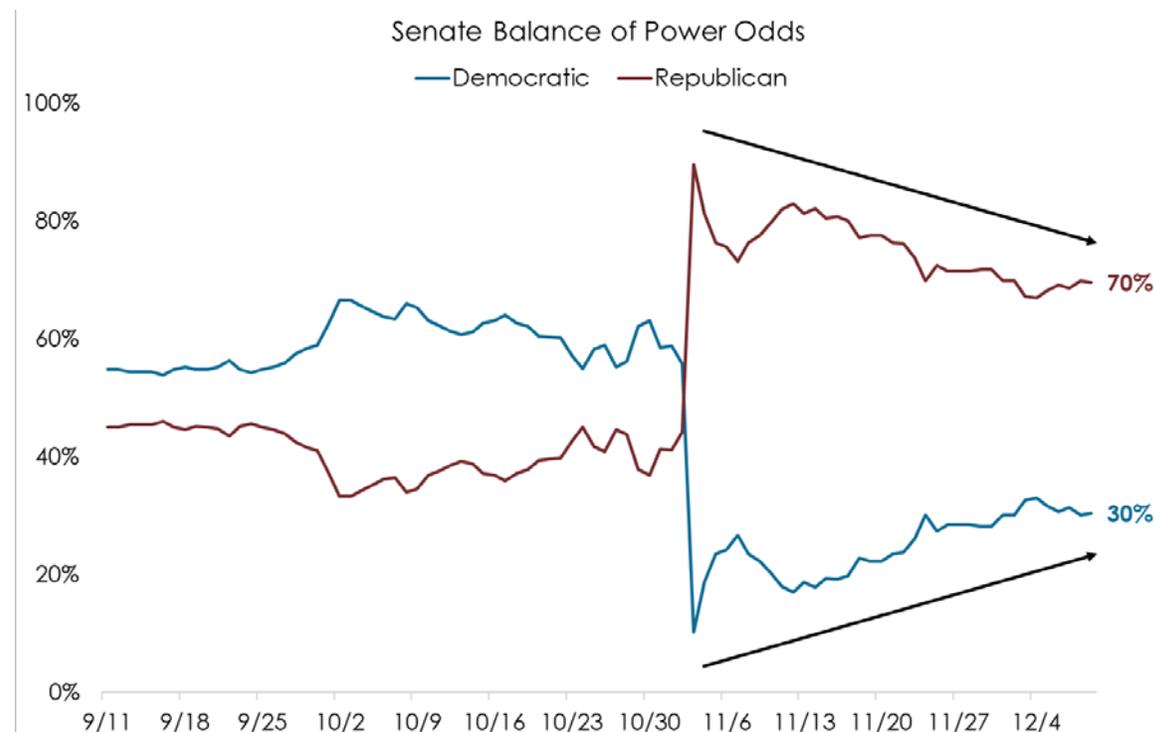
It Ain't Over 'Til the Peach State Sings

- All Eyes on Georgia.** Anticipating the policy agenda of the incoming Biden administration is a key focus for investors heading into the new year. To that end, the composition of Congress matters in determining the latitude Biden has to enact his ideas into law. As a result, many are circling January 5th on their calendars, the date of the two Georgia runoffs. If the GOP wins just one seat, they will likely stonewall some of Biden's more ambitious proposals, but a Democratic sweep of both elections might give the incoming administration free rein on their policy agenda.
- Senate Could Still Swing Either Way.** Polls for both Georgia races have tightened since early November, as Perdue/Ossoff and Loeffler/Warnock battle for the last two seats in the Senate, respectively. However, the betting markets appear to favor the GOP's chances of holding onto the Senate at 70%, noticeably lower than the 90% odds immediately following Election Day. 30% odds of a Democratic sweep is not negligible – that's roughly the probability that it rains in Philadelphia on a given day.
- Implications: Short- & Long-Term.** Over the near-term, if Congress fails to agree on a fiscal package by the end of the year, the winning party of the Georgia runoffs would gain leverage in influencing the size and scope of the stimulus. All else equal, a Democratic Senate is likely to rubberstamp a larger package that the GOP has been reluctant to agree on. Over the longer-term, investors will be focused on the prospect for corporate taxes – if Democrats sweep Washington, there is some expectation that effective corporate tax rates could return to their pre-2017 highs.

The most likely outcome in '21 is economically tenable political gridlock, but investors shouldn't entirely write off the alternative

Chart of the Week:

Market Odds Favor the GOP to Win At least One Georgia Senate Seat



Source: Glenmede, PredictIt, FivethirtyEight
 Data in the top panel shows each party's probability of control in the Senate for the 117th Congress via PredictIt. PredictIt purports to be an experimental research and educational facility of Victoria University of Wellington, New Zealand, and not an investment market or gambling facility. Its website supports the operation of a "predictions market," a facility for buying and trading futures contracts linked to political or financial events or circumstances. The reference to PredictIt and use of its data herein in no way should be interpreted as an endorsement or recommendation of PredictIt by Glenmede, and none of the items predicted in the chart may actually occur.

COVID-19 Endgame

- **Virus Concerns Mounting.** Vaccine distribution has now officially begun following the FDA's emergency approval, yet the pandemic has reached concerning levels on multiple fronts. The seven day averages of case counts (214k), deaths (2.4k) and hospitalizations (109k) in the U.S. all sit at record highs. The viral resurgence has induced lockdown measures throughout the country, stunting economic reopening efforts. If the viral spread is not brought under control by year-end, it will likely be a key initiative to do so in early 2021 before a vaccine has become widely distributed.
- **Vaccine(s) To the Rescue?** Vaccine progress, the main force behind recent market strength, is well underway as the FDA has now authorized the Pfizer/BioNTech vaccine for emergency use. In addition, the FDA will meet this Thursday to consider doing the same for the Moderna vaccine. Reaching vaccine-driven herd immunity will be the logistical challenge of 2021, which will be crucial to the last legs of economic recovery needed to return to some semblance of "normal," perhaps by summer 2021.
- **The Post-Vaccine Economy.** In a post-vaccine world, the economy's deeper wounds are expected to heal. For example, Glenmede's Reopening Index estimates that 73% of all economic activity has recovered since the March/April lows. At the same time, the rising tide has not lifted all boats – low-contact economic activity (i.e., groceries/retail shopping) has recovered 82%, but high-contact (i.e., in-restaurant dining/air travel) has only regained 36% of its prior peak. This suggests that a return to "normal" stands to benefit the unloved sectors of the economy and markets most.

Rising cases may cause near-term disruption, but the outlook for a vaccine-induced recovery remains a distinct tailwind

Anticipating the "Next Normal"

- **Federal Debts & Deficits.** The massive fiscal stimulus package passed earlier this year blew out the federal balance sheet, with net U.S. federal government debt to GDP reaching 107%. However, net interest payment costs have remained relatively unchanged, due to the meaningful move lower in Treasury rates to offset. This may be a sustainable new normal, assuming expiring debts need not be refinanced at meaningfully higher interest rates than have prevailed over the last decade.
- **Fed Giving Inflation Some Elbow Room.** Inflation has been put under the microscope as a result of the recent increase in federal debt. The influx of new money into the economy via unprecedented monetary/fiscal policy has worried some investors that inflation will spike. That said, inflation and market-implied inflation expectations remain relatively tepid, well below the Fed's stated comfort range of 2.0 – 2.5%. While inflation is unlikely to rise to concerning levels in 2021, investors should keep an eye out as economic activity shifts into a higher gear through the year.
- **Virtual Productivity Lift.** The pandemic has changed the landscape for how businesses operate and many that needed to adapt to a work-from-home setting have realized substantial benefits. Time lost commuting and capital allocated for physical spaces are just a few inefficiencies that have been mitigated by working remotely. Remote work has even allowed for the first increase in productivity during a recession in recent memory. And according to a BCG* survey, 83% of firms plan to accelerate digital transformation, suggesting this trend may be here to stay.

Expect larger federal debts/deficits, higher productivity and inflation fears to be the reality in a post-pandemic economy



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