Mackenzie insights on 2020 US election

What it means for investors

We recently hosted our **US Election Recap** event, as part of our Performance Event Series. Conventional wisdom holds that markets dislike uncertainty, and while there was no shortage of that on the morning after the US presidential election, the markets didn't seem to mind.

Mackenzie Investments Chief Economist Todd Mattina, Chief Fixed Income Strategist Dustin Reid weighed in on what the eventual results could mean for investors.

Event highlights

Historically, elections have a limited effect on the markets over the long-term, and whatever impact they have is difficult to predict.

This year stood out, however, given very different economic and social policies espoused by the candidates and their parties and the resulting high voter turnout.

Three key points

1. **Polls were wrong.** Pre-election polls were calling for a "Blue Wave" of wins by Democrats, giving them not only the White House but also control of the Senate. The presidency remains up in the air, but it appears the Republicans will hold onto their Senate majority at this stage
2. **Market don't mind.** Ahead of the election, the market appeared to price in a Blue Wave scenario. This morning's gains suggest a positive view of a divided government, potentially with a Democratic White House constrained by a Republican Senate
3. **The Fed matters more.** With limits expected on the size of a fiscal policy stimulus, the Federal Reserve is expected to continue its aggressive pursuit of lowering unemployment and normalizing inflation

Potential outcomes

While the votes are still being counted, there are three possible results.

Scenario 1

We believe that the most likely outcome is that Joe Biden will win the presidency, but that Republicans will maintain their Senate majority. This "divided" government may be the most market-friendly of the three outcomes, for the following reasons:

- Biden would likely be far more collaborative and less chaotic than Donald Trump has been as president.
- We would expect more bipartisanship to get legislation passed
- A Republican Senate majority would rein in proposed increases to corporate and personal taxes, as well as tougher regulation

On the downside:

- We would expect more modest pandemic-related stimulus than if the Blue Wave had succeeded, which could result in a slower economic recovery

Scenario 2

At the time of our webinar, there remains a potential path for a Democratic Sweep to materialize, putting Democrats in control of both houses of Congress as well as the White House. We believe this result would be less market-friendly but with a mixed impact:

- Based on some estimates, the most realistic components of the Biden policy program could have added $1.5 trillion in additional federal budget deficits over the next 10 years, on top of a larger pandemic-related stimulus of about $2 trillion in 2021-22
- We believe this large fiscal expansion could have added up to 1.2 percentage points to the expected real GDP growth rate next year

Scenario 3

We believe the least likely outcome would be a win by Donald Trump, backed by a Republican Senate majority. This would likely result in the status quo for economic policies:

- Continued downward pressure on interest rates
- More modest fiscal stimulus
- Tax cuts more likely than increases

Both scenario 1 and 2 present a period of instability, we believe. As a "lame duck" president, Trump would be unlikely to provide economic stimulus, which is much needed in the face of a US pandemic resurgence. Any aid could be targeted at specific sectors that Republicans favour, with little chance of aid for beleaguered state and local governments.

Trade implications

A Biden win would likely be much better for global trade. He has a long history as a multilateralist so he is less likely to use executive orders to restrain trade. We would expect to see a thawing of the trade conflict with traditional US allies that resulted from Trump's sometimes incoherent views on how trade policy affects the macroeconomy.

A return to trade liberalization would be bullish for global trade and growth, particularly among smaller, more-open economies like Canada.

We believe there could be exceptions to this potential trade thaw, however. One of the few areas of bipartisan agreement over the past four years has been the desire to confront China as a new strategic and economic rival. We would also expect less friendliness toward Russia, given Biden's long career in Washington and his strong views on this long-standing strategic rival.

The Federal Reserve

As has been the case for several years, the Federal Reserve is likely to play a bigger role in the markets than the federal government. The Fed has signalled that it is extremely interested in keeping credit ample and cheap across the curve, for both consumers and businesses.

Among its stimulative options, the Fed may:

- Extending its fixed income purchases toward the 10-year maturity, which would assure the market that rates would remain low across the yield curve for a long time to come
- Increase the notional amount of its purchases
- Tweak its many programs to make them more effective

Current Fed Chairman Jerome Powell, a Trump appointee, would likely remain in place under Biden. He is seen as a steady hand and his continued leadership would reassure the market.

Strategy

We remain committed to tuning out the noise and focusing on the long-term. To that end, we are maintaining or adopting the following strategies:

1. **Stay diversified**. Maintain broad exposure to various asset classes, geographies and currencies.
2. **Don't abandon low yielding bonds**. Government debt remains an important holding in a well-balanced portfolio, as long bonds can provide exposure to unpredictable economic outcomes in the future.

It is always difficult to capitalize on political risk events; not only do you need to get election results right; you also need to be right about the market response. We believe a better approach is to look for outsized risk exposures and manage those accordingly.

For more information about topics discussed in this webinar, or to learn about specific solutions that may benefit your clients and their retirement income plans, please contact your Mackenzie Sales Team.