

The U.S Election: An Early Take On What's at Stake for Investors

Episode #2 | December 11, 2019

Speaker Key:

DP David Pett
 KM Kevin McCreadie
 GV Greg Valliere

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00:00:00	DP	The US election is still is months away, but its potential impact on global markets is already taking shape. On this episode of the podcast, Kevin McCreadie, AGF's CEO and Chief Investment Officer, welcomes Greg Valliere, AGF's Chief U.S. Policy Strategist, to discuss the race for the White House and what's at stake for investors in the coming months.
00:00:28		I'm your host, David Pett. Let's get into it. So you guys have known each other for a few years, I'm guessing?
	KM	I bet you I first ran across Greg, I don't know, 20...
	GV	20-something, yes.
	KM	20-some-odd years, yes.
	GV	Yes.
	DP	Do you remember the first time you met or encountered each other?
	GV	I'm sure it was in Baltimore, but I don't really remember.
	KM	Yes, we had an old colleague in common, an old friend of mine.
00:01:01	GV	A dear friend who passed away.
	KM	He was the... That's how I got to know Greg on a business level but also on a personal level.
	MO	And were you following the political side of things at that stage, Greg?
	GV	I've done this since the Woodrow Wilson administration. Yes, I've

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	done it for quite a while.
KM	Everybody is joking, I think, when he says that.
MO	What's changed over the years from that standpoint?
GV	Oh, where do you start? I mean, I think the big change this year, maybe we'll get into this at some length in this conversation, is a move by the U.S. to go isolationist.
00:01:36	I mean, Donald Trump wants out. He doesn't want to get involved in any more Mid-East conflicts. He's tired of casualties in Afghanistan, and he's been quite blunt about not getting involved in foreign wars. That's a big change. A critic would say it's an abdication. Others would say he's just recognizing a turn in public opinion.
00:01:59	KM I look at that, and I always worry because that pivot, if that's what it is, the next time... And there will be crises around the world. Again, the world is still a dangerous place, and I always worry who is going to be taking the side and back of the Americans the next time they need help with this kind of a move?
	GV We've alienated a lot of allies. And I think Trump's view is that since we're now spending close to \$750 billion a year on defense that he's got a backstop. He's got all the most expensive toys in the world if we need them.
00:02:36	But in terms of alliances, whether it's the Trans-Pacific Partnership or NATO, you name it, things are pretty rocky right now.
	DP And then the impact that that has on investors and markets seems to be a lot more heightened today than it may have been ten years ago.
	KM Yes, I think the media has changed too.
00:02:58	We didn't have the tweets of the moment or the daily use of that medium as a bully pulpit in some ways. And some of it is exacerbated and felt in the markets because it's a statement, and markets interpret it immediately. And so whether it be company-specific like Amazon and The Washington Post issues that were linked earlier last year, or two years ago, I think you see some of, again, the emotion that comes out of those tweets that starts to impact markets.
00:03:35	But also the policy statements and other things, I think, have been definitely very different from 20-odd years ago, for sure.

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	GV	I would add, Kevin, there's a great, great suspicion toward the media, toward the information that people get. People think its fake news. I mean, there are things that I think you can rely on as an investor.
00:04:00		But a lot of the news accounts are now suspect, maybe too much so. But it does make people wonder if what they're hearing is exactly correct.
	KM	And I think beyond just this idea... Is it real? Do I believe it? Who is it coming from? Some of the substance has actually been impactful on the economy and, therefore, the markets. This trade issue is real. It's not just slinging quotes around.
00:04:30		It's been a real impact on business confidence, I think. You see it not just in the U.S. but in data around the world. So it's not just a headline. It's the substance of it too.
	GV	You could argue that the economy in the U.S. would be much stronger right now if it were not for, A, the trade war, and, B, a very tight labor market wherein, say Seattle or Charlotte, North Carolina, they've run out of skilled workers. And that, I think, is a headwind for the economy as well
00:05:01	KM	Yes, I know. It's an interesting data point where people forget that when you're not bringing new workers into the workforce, they're not buying clothes, jeans, etc. So to an extent, you can't find workers. There's this spending that doesn't happen. And you've got a quarter of the States in the U.S. that have, actually, unemployment rates lower than the national average. So to your point, it gets really tight in certain places.
00:05:27	DP	So let's talk about the U.S. election. It's still early days, but the campaign trail is already fairly hot. Greg, what's the political climate like in Washington at the moment?
	GV	It's bitterly partisan. It's very angry on both sides. It's frankly disheartening to see. Because when I was a young man starting in this business, political leaders would at least meet in the evening, have a drink, and talk about things in a friendly manner. The classic example is Ronald Reagan and Tip O'Neill, the Speaker of the House, who'd tell jokes in the evening.
00:06:00		Now it's nothing like that. It's extremely hostile. And you have a president who's a provocateur, obviously. And despite all of his problems... Impeachment, he's going to wiggle out of. I think he gets acquitted by the Senate. The economy, looking pretty good,

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not great, but looking pretty good.

And maybe most significantly for Trump is a pretty weak group of opponents. The challengers lining up to face him... I don't think strike fear in the hearts of the Republicans.

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KM

One of the things you said, Greg, earlier about the climate, it plays into this. If you think about it, if one party does not control all three pieces of the government, it's going to be hard to see anything really getting done because there is this lack of trust. There is a fair amount of disdain. And then within these parties, there are factions now.

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And so you look at the Democratic Party, and you almost say, can Nancy Pelosi even control her own given that she probably doesn't want to take the impeachment path, but she's being forced to push that agenda?

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GV

So you've got a big schism within the Democrats: The moderates like Joe Biden and the far left, this young woman from the Bronx in New York City, and people like Elizabeth Warren who hasn't done very well lately, and Bernie Sanders.

And then among Republicans, in private you have moderates who are quite critical of Trump, but in public they look at his job approval numbers and they have to line up behind him.

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So you actually have a more unified Republican Party right now than the Democrats.

DP

And is that divisiveness that we're seeing in Washington also evident across the electorate? It seems like in this age of populism that the people are equally divided.

GV

I think it transcends issues. We can talk all day about health care and climate change and tax policy, things like that.

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But I think there's a deep divide over what the right-wing would call the deep state that's trying to undo Trump's electoral victory. The cable news, whether it's Fox on one side or MSNBC on the other side, it just feeds these passions. And again, it transcends issues. It just goes to who's controlling the country. And on that front, having a unified party like Trump does is a real asset for him.

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KM

And I think that that's absolutely a big difference today versus many years ago when you started doing this and I started following it. But I also come back to, for many people they forget that the true majority in the U.S. are the independents.

And they are going to determine the outcome of this ultimately.

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	Because you know that the Republican Party is going to vote for that candidate, and there are 30-odd percent of them.
00:08:58	The Democratic Party is going to vote for their candidate, 30-odd percent of them. How do you move the middle, the independents, to one of those two? And the views become polarized. They are very different at the extremes right now then I have ever seen.
GV	And people still want to relitigate what's happened since the Great Recession where the banks bailed out. Are we getting treated poorly? And now we finally get a chance, as Kevin said, to see just how centrist we are.
00:09:27	<p>Because there is a genuine centrist who happens to be worth \$55 billion who is running for president, and that, of course, is Michael Bloomberg, the former mayor of New York City. So I think that his agenda on everything except guns is quite centrist. And we'll see. The poles need to pick up a lot.</p> <p>But interestingly, he's not going to contest to Iowa or New Hampshire or South Carolina. He's going to wait until March 3rd. That's called Super Tuesday. Many big states, headed by California, will vote.</p>
00:10:00	And Bloomberg is betting that hundreds of millions of dollars spent on TV ads could get him a very favorable result on March 3rd. I would be reckless to predict he'll be the nominee, but he has a chance.
KM	Not that it's an exact parallel, but when he ran for mayor of New York, he took probably every opportunity, every air spot. You would have thought he was running for president or governor. And he went from really no chance to winning.
00:10:31	So to the extent that this media blitz is done the right way and the right message... He's positioning himself not against the other Democrats. He's positioning himself as an alternative to Donald Trump in this media blitz. And so maybe that gives him the momentum when he's got some time and spent.
GV	And I'm told, Kevin, that he gamed this out in November, and basically said to his aides Biden has lost his step. I think many people would agree.
00:11:01	Elizabeth Warren is too polarizing. So is Bernie Sanders, who's 78 years old and has had a heart attack. This very impressive young man Pete Buttigieg is only 37 without a lot of experience, the

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mayor of a small city.

When you look at the lineup that the Democrats have, there is an opening for Mike Bloomberg. And again, \$55 billion goes a long way. Even if he only spends a fraction of that, he can make a real splash.

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KM

And I think it says a lot, why he entered the race, though. It looks like he doesn't believe that any of these candidates can beat Trump.

GV

Exactly. And I think there's a lot of truth to that. Now, Bloomberg is going to turn 78 at the end of the winter. He is well to the right of most Democrats. He's a Wall Street billionaire, and they're not real popular right now among the Democrats. So it's still a very fluid situation. And until it's resolved, I think you have to conclude that Trump, maybe by default, is the shaky frontrunner.

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KM

And I think right now no one is taking Bloomberg seriously. And maybe we sit here six weeks from now or eight weeks from now and he's spent a fair amount of money and he hasn't moved much in the polls, then it probably falls away. I think it's too early to say if he can be serious about this. But I think the fact is certain that these policies won't appeal to the independents that a guy like Mike Bloomberg will.

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GV

There's no other savior from the outside for the Democrats. We're not going to get Hillary Clinton. We're not going to get Michelle Obama. I think what you see is what you're going to get. Because in many states, the filing deadlines have come and gone.

DP

What are some of the bigger issues that investors need to keep an eye on over the next 11 months?

KM

I think we're going to relitigate the tax cuts. And I feel very strongly that this White House will propose more tax cuts. That's like catnip in an election.

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The voters get very seduced by the idea of a big new tax reduction. So, I think we'll talk about that. We always talk about health care every four years. We re-debate that. And there will be some other things like climate change, U.S. foreign policy.

Personally, I think the big issue may not be something specific like tax policy. The big issue is Donald Trump himself. And the polls show that he gets horrible grades on likability, trustworthiness, things like that.

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00:13:29 And I think the Democrats will go right after Trump the man rather than the issues.

KM And for me, I think it's actually not going to be as much the issues that people campaign on. I think it could turn on the economy. Have we done too much damage with this uncertainty around trade to the manufacturing sector? The three key states that are going to be really important for Trump to hold that he won last time that are really centric to manufacturing.

Some of the agricultural issues, to the extent that we have done some damage. I think the economy is going to play a big factor into some of this, certainly in terms of the electoral college potentially.

00:14:04 GV And Kevin refers to the three states that Trump narrowly won: Pennsylvania, Michigan, Wisconsin. If the nominee for the Democrats, probably Biden or Bloomberg, if they can flip those three states, there's a path to the White House. Even if Trump wins Texas, Florida, Ohio, there still is a path to the White House if they can flip those three states.

00:14:30 KM So I think it comes back to my mind, if the economy reignites here, and if the Fed, basically, is right to stay on hold, and there's enough momentum here either through a trade deal in confidence that you get back, that probably is a bigger determinate in some way than some of the specific issues, I think.

GV Well, we know we're going to get enormous fiscal stimulus. We are spending in Washington like drunken Keynesians. You name it; we're throwing money at it.

00:14:56 What to me is fascinating... And maybe if I could ask Kevin a question? What about the Fed? Does the Fed still come back into the picture with another rate cut if the economy looks soggy during the winter?

KM Yes. I mean, the Fed has been pretty divided, as you know, Greg. More divided than I've seen it in a long time. There have been stops and starts. One would argue that if you had settled this trade issue back in the Spring, would the Fed have even cut rates to begin with? Now you're at the... We've cut three times. Now you've made a bold statement that they're on hold.

00:15:31 But I think if you get into the early couple of months of next year and things start to soften because there is a tail effect to when the impacts are felt from some of this, that they probably come back and cut again.

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But right now, they've been bold out there in saying they're done. I don't see them raising rates. But it could be if things weaken, they'll have to come back around and take a couple more cracks at it.

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DP

Given there's so much focus on the U.S. election at the moment and all the noise that that brings, how do investors decipher between what's important and what's not important?

KM

I think markets have ground their way to new highs on the back of basically the promise that you are going to get trade results, and the promise that the Fed had been at your back and is willing to bail it out, and the fact that the Fed has stepped aside makes people say maybe they know more than we do about the health of the economy. The economy is growing at about 2%. Not terrible. Not great. And so maybe they're right to stand back.

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But I think if you're an investor with markets at these levels and interest rates at still pretty accommodating low levels, I think you've got to be a little bit more cautious as you move into next year. I don't see a recession in the near term.

But, again, we're going to see the lag effect of this trade uncertainty play out over the next few months. That's probably the key thing for markets. If you see economic weakness start to show up, it's probably going to be more of a risk-off world for a bit until you can see some stabilization.

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Now, the bright side of that is, I think if you avoid a hard Brexit, and I think that you see some of the data in Germany, for instance, start to flatten and then maybe improve, you probably can take some further risk off of the global economy which should help the U.S. as well.

DP

Is there something about the U.S. election that isn't being priced in at the moment that should be?

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GV

Well, you always worry about the fact that when there's unanimity of one position that sometimes a contrarian view is overlooked. And I would argue that everyone expects Trump to get acquitted, but there is the potential for more disclosures. Could, for example, John Bolton testify about his meetings with the President?

Could there be tape recordings? Could there be new disclosures in the press? So while I think that we will get through impeachment and political unrest, it is worth noting that, in private, an awful lot of the Republicans who I talked to are tired of this guy.

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00:18:04 They are tired of defending him. And I do think that if there are big new disclosures, maybe he'll survive as president but this could really soften him up for the fall election. And if the fall election is a clear victory by the Democrats, the markets may have to worry.

Could the Senate be the firewall and stop this legislation? Or could the outlook get a little more cloudy for the financial markets if the Democrats do well?

00:18:32 KM I think that that's a risk that's absolutely not being priced in. You see it priced in a little bit by sectors. When Elizabeth Warren took the lead in the polls, health care really took it on the chin. Financials a little bit, which would not be good for the financial sector in the U.S. if she were the candidate.

But I do think this Trump fatigue idea is real. I think, if you look at it... Again, the Republican's view of impeachment and the Democrat's, no surprise, they're polar opposites.

00:18:58 But the independents, since this thing has started, their appetite for it has seemed to start to wean. And so if you get into the spring and people really feel fatigued, does this open up the potential for, again, people really turning away from the Trump piece of this and moving more toward the Democrats?

And, again, what does that mean for the Senate? And I think that would be a potential down card that's not being priced into the market.

00:19:26 A Senate sweep over the Democrats and a Democratic president would have a pretty dramatic impact for certain policies that would impact certain sectors of the market.

DP And with that, I'd like to thank Greg for being with us. And Kevin. Until next time when John Christofilos, AGF's Chief Trading Officer, joins the podcast to talk about market structure and how it continues to evolve for better or worse.

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