A PERPETUAL VIEW OF THE US ELECTION

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For a view of the US election result and the effect on the stock markets and the economies of the US and Australia, we're talking with:

- *Kyle Lidbury, Head of Investments Research, Perpetual Private*
- *Amanda MacDonald, Investment Specialist, Perpetual Private*
- *James Holt, Senior Investment Specialist, Perpetual Investments*

With no result yet, what does a disputed election mean for the stock market?

Amanda: The biggest risk to markets is a contested result. The likelihood of increased volatility is really dependent on that scenario happening.

James: Agreed. Markets like certainty. People want a decisive result – either a blue wave or red wave. If it's a contested result, the big fear is that it will be a [year] 2000 type result which came down to one state – Florida – and went on for weeks and eventually came down to hanging chads and only a handful of votes.

Amanda: And coupled with all the other risks in the US at the moment, social unrest, the pandemic – these will all add up along with a contested result as increasing the likelihood of more volatility and bad news for the stock market at least in the short term.

James: One flip side for volatility, a positive, there may be more opportunities for active investors.

When the market has a big rally like we've had and there is an expected clear result with Trump and taxes stay low, or an expected clear result with Biden and he spends up – either way is a good scenario but if they don't know which it's going to go is negative. It's also worth remembering there are two elections that are important today – there's also the senate.

Kyle: With a split vote between the Presidency and the Senate could also increase uncertainty as legislation is stalled in the senate.

Would a Democrat or Republican victory be better for the stock market in 2021?

Kyle: One thing to remember is that the US stock markets is pretty divergent to all markets, including the Australian market, at the moment – and largely to do with technology. That is one of impacts of the COVID-19 crisis, which have made real winners and losers from the crisis. Certainty around earnings for tech stocks on the US market is driving their valuations up and up, while other sectors – without that certainty of earnings – have not performed well.

One thing that is really affecting us [Australia] from a 'future prospects' perspective is the current state of the Australia-China relationship, which is poor. You've seen several industries come up against fairly hefty barriers, including copper, barley and now even lobsters. Education and tourism are also affected – both top 5 exports for our country. Our strength is iron ore, which so far has not been affected.

Together with these other industries, there's no doubt this helped us through the GFC and why we avoided a recession. The risk of lack of Chinese support, that's more of a headwind for us that the US election.

As a result of the US election, I don't see there will be much change from the US perspective. The China trade war – the hemming in of China has bipartisan support and won't really change as a result of who gets in.

James: Over the long term it doesn't matter who is the President. For over 200 years, the country has thrived under different presidencies. In the short term, Biden might give the economy a net boost – if there's a clear result one way or the other, the markets will move on pretty quickly.

Kyle: One thing to note is that the tech stocks have dimmer prospects under Biden. There are elements of the Democratic party that want to break up those companies.

Amanda: Generally, with less pressure from regulation [than] under a Biden presidency Tech stocks will likely continue their divergence from the rest of the market.

James: Tech stocks are pretty richly priced anyway, even before COVID; and they've come out of COVID-19 pretty even more so from that perspective it's worth noting that once you get these elections out of the way things return to basic fundamental, they're probably ripe for rotation.

Do politics really matter when it comes to stock market performance after an election?

Amanda: The year after an election the incumbent president tends to show a more positive return.

Kyle: Historically, evidence points to returns being better under a Democrat presidency – but with a split congress.

James: True - we saw that in the late 90s when Bill Clinton was President. Republicans were in control of congress and cut spending and kept tax low and Clinton was the President acting as centrist between the left-wing Democrats and the right wing Republicans. Funnily enough if the Democrats win the Presidency and the senate stays Republican that might be the best result as businesses can take more confidence that there will be fewer changes in the law and be more confident to invest and get on with business.

Democrats and Republicans will take the US economy in different directions. What should we look for and what market sectors will benefit from a Democrat or Republican victory?

Kyle: There's a lot that will be similar, but there are some differences. Both candidates have stated a desire to spend on infrastructure for example. However, Biden has said it will be around green initiatives such as renewables and environmental. Some stocks have rallied quite strongly on that prospect.

In terms of trade, there won't be a significant amount of difference as we've talked about that.

Trump has talked a lot about bringing jobs back to America, but he's been less successful on that than he might like to think despite the tariffs and other things. There's a lot of data that says there was economic stimulus but it was largely through the tax cuts that were passed, but what that did was hide a contraction that you saw from the reduction in trade as a result of the trade war.

Even thought the economy grew – it could have grown much more strongly if there was more harmonious trade.

James: The funny thing with the Democrats is that they've jumped on the trade bandwagon as well so we shouldn't expect much difference under the Democrats – even if the Democrats are more diplomatic about it.

How will ESG investments be affected by either President?

Amanda: Biden has laid out quite a clear plan for his clean energy revolution with a net zero emissions target by 2050. As Kyle mentioned previously Biden has indicated to put $2tr into green infrastructure over four years. Trump doesn't focus on climate change and has made no clear plan towards a greener future for the US.

From an ESG perspective, companies that have exposure to renewable energy sources and innovations will probably perform better under a Biden win. And Biden has also stated his intent to re-join the Paris climate agreement.

What advice do you have for investors and their investment portfolios regardless of the election result?

James: Keep your long-term plan in place. Don't make any rash decisions in the short term – remember elections come and go and economy moves on and you should base your investment decisions on that.

Kyle: Yeah, trying to position your portfolio for the outcome of an election is folly, particularly when it's close or contentious. At the end of the day it doesn't have much of an effect on markets as people would think.

The other side of things, is that, looking back to 2016 and Trump's victory – what was widely expected to be a negative for markets turned out to be quite positive. Even if you get the result right, it may not have the effect you expect. When you can't make high conviction bets, it's just important to be broadly diversified in a portfolio that is positioned for a variety of different outcomes and you don't have all your eggs in one basket.

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