

# Guide to the 2020 Elections

Potential impacts on policy and portfolios

September 2020

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# Keep your perspective

We expect economic and investment implications from the elections. However, the track of the pandemic and the economic recovery from the 2020 global recession still loom as possibly the larger influences on political and private decisions alike.

We see other reasons for keeping perspective amid rising campaign rhetoric.

1

## **Both presidential candidates are still positioned for a win**

Polls and other data suggest a substantial advantage for former Vice President Biden, but President Trump could still turn the advantage to himself.

2

## **Congressional control is likely to go to the party that wins the White House**

We think it is likely that the Senate will go the way of the presidency. If Biden holds his lead, single-party government is likely to return in 2021.

3

## **Unified government can coincide with a favorable investment environment**

Investors may worry about one party sweeping in to control the White House and Congress, but half of the presidential elections since 1945 have delivered single-party government, including three of the past four.<sup>1</sup> What's more, unified government has historically coincided with S&P 500 Index price returns comparable with or slightly above the 1945–2019 average annual price gain.<sup>2</sup>

4

## **Even if the elections produce single-party government, the impact of politics on markets is likely to be more complex**

The deepening political polarization in the U.S., reflected in Congress, is a trend that has limited what even single-party control of government may expect to accomplish. Thus, we believe the most controversial issues are unlikely to become law.

### Two broad questions we consider about the elections and investment decisions in this report

- What are the main election scenarios for markets, and which is more likely?
- What are the main issues we expect to dominate policy in 2021, and what potential opportunities may arise from them?

1. "Party Control of the Presidency and Congress, 1933–2010", Russell D. Renka, Southeast Missouri State University, January 2010, and Wells Fargo Investment Institute, September 1, 2020.

2. S&P 500 Index is a market capitalization-weighted index composed of 500 widely held common stocks that is generally considered representative of the U.S. stock market. An index is unmanaged and not available for direct investment. **Past performance is no guarantee of future results.**

# Potential outcomes and what to watch

## Presidential and Congressional elections.....page 4

- Biden widened his national poll lead during the summer, but the final 90 days are what will matter as voters make their final decision.
- We anticipate that Democrats will continue to lead in the House of Representatives.
- We believe the Senate will go the way of the presidential election.

## Policy implications .....page 7

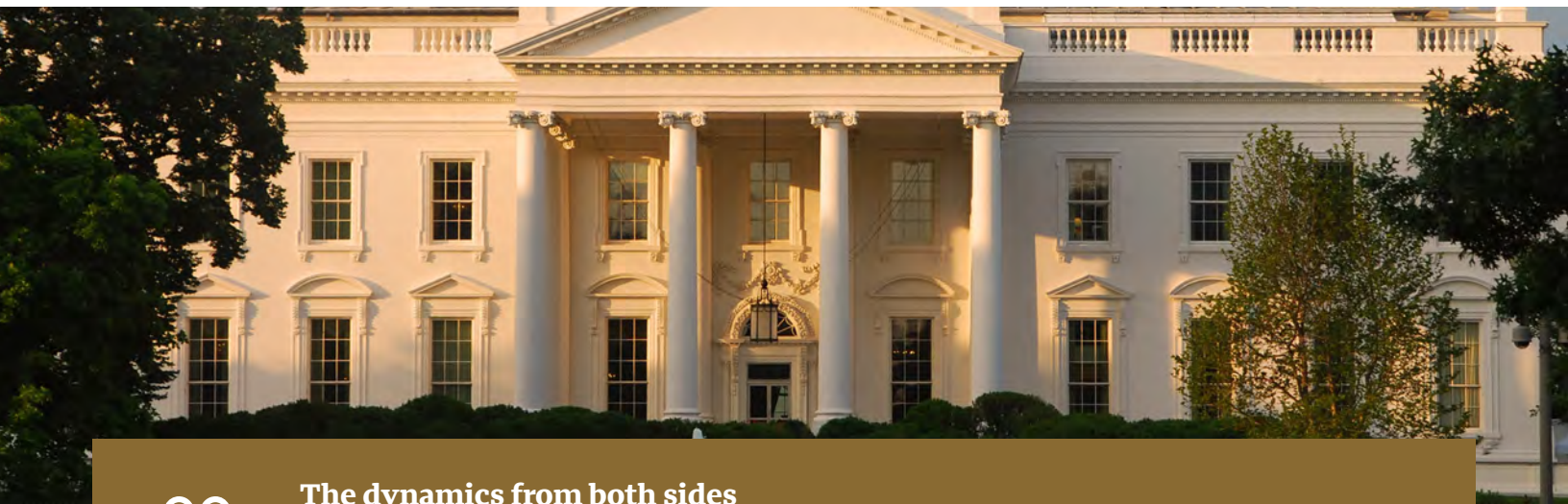
- We see five main policy categories: tax and regulatory, fiscal and monetary, foreign economic, health care, and energy/climate.

## Investment implications .....page 11

- The pandemic and slow global economic recovery are likely to dominate any election result. We prefer to align portfolios ahead of the election with our favored asset classes and sectors, which we believe are consistent with those themes.
- Considering the risk of changes in income and estate tax provisions, we favor examining potential income and estate planning consequences before year-end.
- We favor weighing the election implications for portfolios after January 1, 2021. Even if one could know the election outcomes in advance, many factors to be determined in 2021 are still important for how the elections may affect financial markets.







**The dynamics from both sides**

## Presidential and Congressional elections

**Biden opened up a sizable summer lead in the polls, but Trump is still capable of closing the gap by November. Because we expect control of the Senate to follow the results of the presidential race, we anticipate two scenarios for financial markets—single-party control by the Democrats, or re-election for Trump and split control of Congress.**

### Polls show Biden with a lead

Polls show Biden with a sizable, but not insurmountable, lead of 7 percentage points between August 23 and August 28 in an average of polls compiled by RealClearPolitics.<sup>3</sup> The quality of Biden's lead appears better than Hillary Clinton's four years ago because of its greater stability throughout the campaign as well as a stronger balance of favorable versus unfavorable ratings as of midsummer.

#### Favorability rating midsummer 2016 vs. 2020

	Favorable	Unfavorable
<b>Biden</b>	44.5%	46.0%
<b>Clinton</b>	38.3%	55.3%

Sources: RealClearPolitics and Wells Fargo Investment Institute, July 27, 2020. Biden favorability ratings are based on the average of 11 polls between May 7, 2020, and June 16, 2020. Clinton favorability ratings are based on the average of 7 polls between July 9, 2016, and July 24, 2016.

3. "Latest 2020 Presidential General Election Polls," RealClearPolitics, September 1, 2020

4. "It's Way Too Soon to Count Trump Out," Nate Silver, FiveThirtyEight, August 12, 2020

### ... but Trump can narrow the gap

We believe it's too early to count President Trump out, for a number of reasons:

1. Presidential elections in 1988, 2000, and 2016 show that big leads evaporated in the weeks before an election.<sup>4</sup>
2. Biden's narrow leads in several of the key battleground state polls (including Arizona, Michigan, Pennsylvania, and Wisconsin) and right-of-center Texas, Georgia, and others add to Biden's vulnerability.
3. Trump's assertive campaign style has yet to test the Biden campaign.
4. The severe recession may give an overly pessimistic view of the president's popularity if new fiscal policy support or good news on a COVID-19 vaccine or the economy appear.
5. Biden's critical—but delicate—shift to a more progressive Democratic platform may alienate moderates inside and outside the party.

## Mapping Biden's tilt to the left

Biden's shift to a more progressive platform since the presidential primaries seems designed to engage younger voters but has the potential to alienate moderates. Biden's move left also seems designed to co-opt highly motivated, progressive voters capable of energizing the nominee's campaign by voting and by getting out the vote through social media and other nontraditional venues. Included in that group are so-called Gen Z voters (born after 1996), the only age group with an increased share of eligible voters in 2020, as shown in Chart 1.

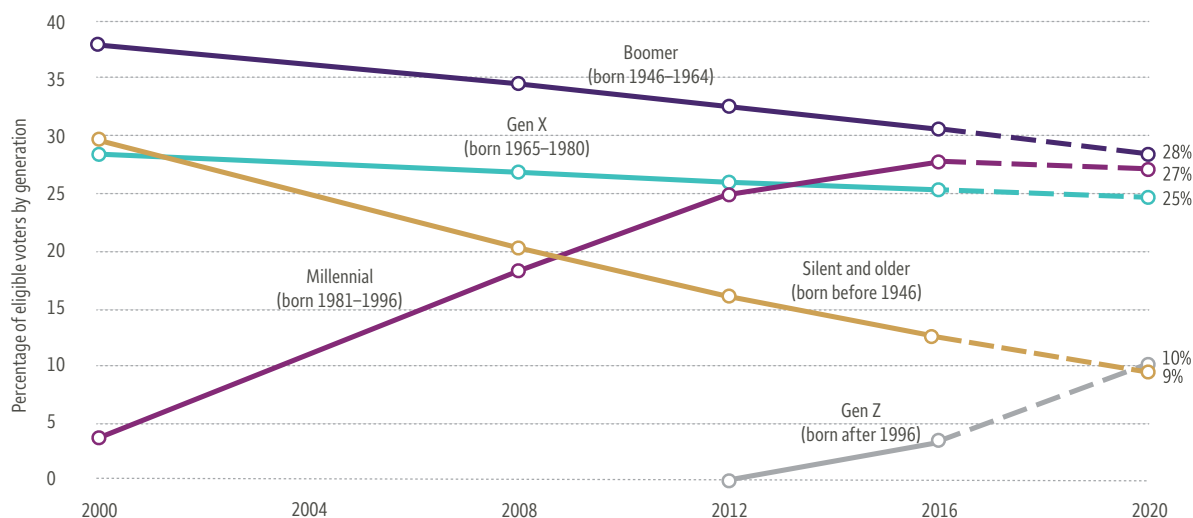
## Key proposed policy points announced by Joe Biden in March and August 2020

	March 2020	August 2020
<b>Taxes</b>	<ul style="list-style-type: none"> <li>Revamp and increase labor protections</li> <li>Increase Federal minimum wage to \$15/hour</li> </ul>	<ul style="list-style-type: none"> <li>Restore the top individual income tax rate to 39.6%</li> <li>Raise the corporate tax rate to 28.0%</li> <li>Added Social Security taxes at 12.4% split between workers and employers for all wages above \$400k</li> </ul>
<b>Fiscal policy</b>	<ul style="list-style-type: none"> <li>Greater reliance on public transportation using "green" energy</li> </ul>	<ul style="list-style-type: none"> <li>Manufacturing tax credits and subsidies for capital investment, process upgrades deploying low-carbon technologies</li> <li>A \$1.3 trillion government-funded program</li> </ul>
<b>Energy</b>	<ul style="list-style-type: none"> <li>Ban fracking on federal land</li> <li>Eliminate fossil fuel subsidies</li> </ul>	<ul style="list-style-type: none"> <li>A \$1.7 trillion federal investment toward a 100% clean-energy, net-zero emissions economy by 2050</li> <li>A carbon tax on fossil fuels</li> </ul>
<b>Health care</b>	<ul style="list-style-type: none"> <li>Allow Medicare to negotiate drug prices</li> </ul>	<ul style="list-style-type: none"> <li>A Medicare-like public health insurance option available to all.</li> <li>Allow Medicare to negotiate drug prices</li> <li>Protect and expand the Affordable Care Act (ACA)</li> </ul>
<b>Foreign economic policy</b>	<ul style="list-style-type: none"> <li>Take multilateral approach with allies to compete with China</li> <li>Resume multilateral trade negotiations, instead of bilateral talks and tariff threats</li> </ul>	<ul style="list-style-type: none"> <li>Foreign policy to extend U.S. values, for example, policy as a tool to fight international corruption</li> <li>Seek international agreements to regulate technology firms</li> </ul>

Source: Wells Fargo Investment Institute, September 1, 2020

## Chart 1: Gen Z rising

In 2020, 1 in 10 eligible voters will be members of Generation Z, making it the only age group with an increased share of eligible voters in 2020.



Note: Eligible voters are U.S. citizens ages 18 and older.

Source: Data from 2000 to 2016 from Pew Research Center analysis of 2000 decennial census and 2008, 2012, and 2016 American Community Survey (IPUMS). Data for 2020 from Pew Research Center projections of the electorate based on U.S. Census Bureau 2017 population projections.

## Other factors—congressional races, vote-by-mail, and turnout

We view the congressional contests as nearly as important in shaping the Washington power balance as the vote for the top post. The House of Representatives seems safely Democratic. The required net gain of 18 seats for a GOP majority appears out of reach.<sup>5</sup>

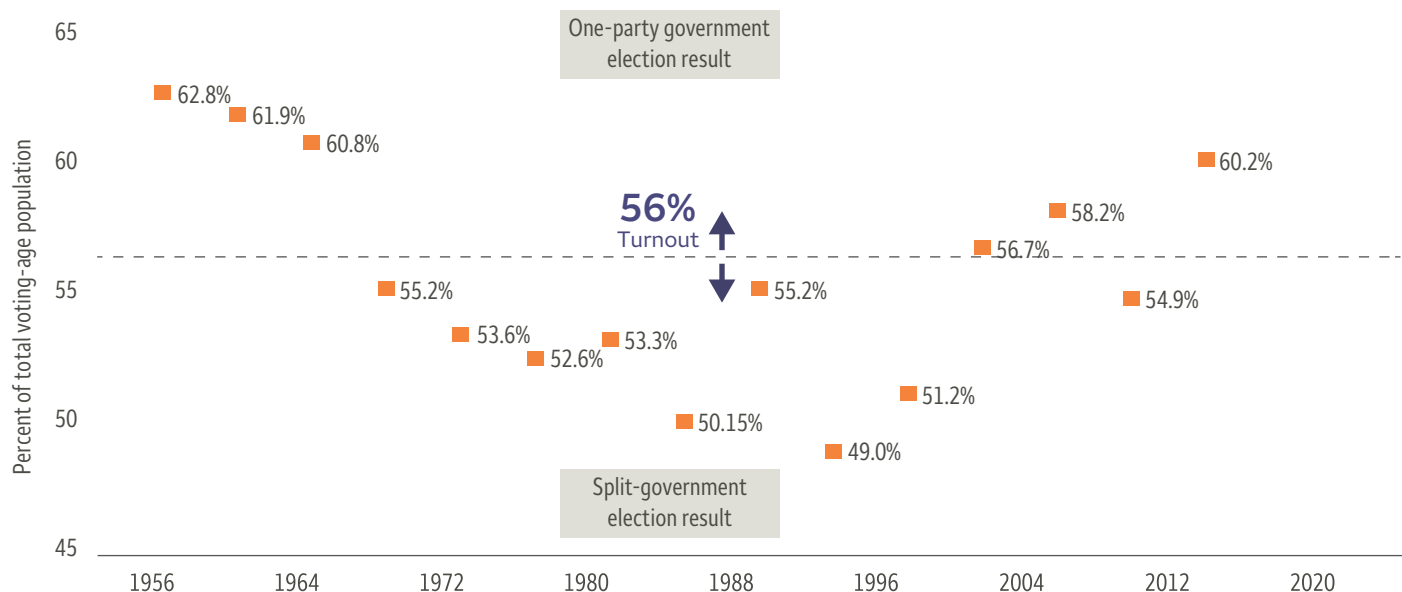
However, increasingly rare split tickets culminated in a clean sweep of all 34 Senate races by the winning party in the presidential election of 2016.<sup>6</sup> A similar correlation is shaping up again for 2020. Presidential polls have moved toward Biden, and a recent Cook Report estimates that 1) 6 of the 23 Republican seats up for election are toss-ups and 1 leans toward the Democrats; and 2) no Democratic seats are toss-ups and just one of the 12 exposed Democratic seats leans Republican.<sup>7</sup> These numbers could shift if President Trump regains the upper hand.

We expect only a muted market reaction to any delays in reporting due to voting by mail, much like the market's limited reaction to post-election limbo in November and December 2000.<sup>8</sup> Turnout remains tough to predict. Since 1960, a turnout of 56% or more of the eligible voters has coincided with one-party government (see Chart 2 below). Biden must balance his outreach to progressives during the final weeks of the campaign, to energize his campaign and to boost voter turnout, against alienating moderates inside and outside his party.

One factor to watch in 2021 will be whether the Senate votes to end the filibuster, a 60-vote procedural hurdle. We acknowledge the risk that the Senate may abolish the filibuster but still expect divisions between moderates and progressives within the Democratic Party to prevent policy swings to ideological extremes. Consequently, the most divisive proposals from the campaign trail seem unlikely to become laws.

### Chart 2: High turnout correlates with one-party government

Historically, higher voter turnout has tended to result in one party taking the White House, the Senate, and the House.



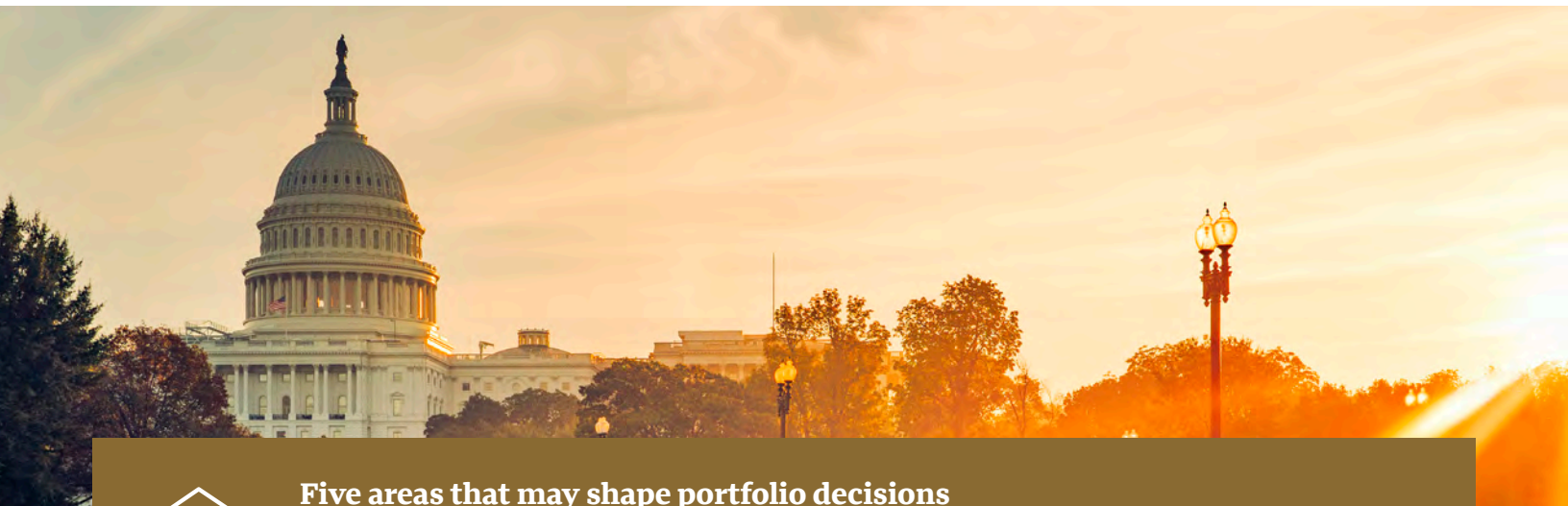
Source: Dr. Michael McDonald, University of Florida, United States Election Project

5. The Cook Political Report, "House Race Ratings, as of August 21, 2020", September 1, 2020

6. "There Were No Purple States on Tuesday," Harry Enten, FiveThirtyEight, November 10, 2016

7. The Cook Political Report, "Senate Race Ratings, as of August 17, 2020", September 1, 2020

8. Outcomes are not affected materially, either, judging from a recent county-by-county study of three states with universal vote-by-mail showing only modest increase in voter turnout with little effect on the election results between 1996 and 2018. See Daniel M. Thompson, Jennifer A. Wu, Jesse Yoder, and Andrew B. Hall, "Universal vote-by-mail has no impact on partisan turnout or vote share," May 6, 2020



Five areas that may shape portfolio decisions

## Policy implications

Election 2020 is coalescing around five priority policy categories. The table on page 8 contrasts the candidates' proposals within the five categories. However, we also highlight the candidates' common points that are forming because of trends already in place. Whoever wins the election will face several overarching economic themes, including a slow economic expansion, the ongoing risk of another wave of COVID-19 infections in the autumn, demand for an expanded health care system, persistently low interest rates, and national security concerns about U.S.-China competition and the offshoring of U.S. manufacturing.



Tax and  
regulatory



Fiscal and  
monetary



Foreign  
economic  
policy



Health  
Care and  
immigration



Energy

## Side-by-side comparison of our expectations for potential Biden and Trump policy positions

Policies likely to be implemented	Biden <i>Likely under a Democratic sweep</i>	Trump <i>Likely under a split government headed by Trump</i>
<b>Tax and regulatory</b>	<ul style="list-style-type: none"> <li>Raise the corporate tax rate from 21% to 28%</li> <li>Create a 15% rate on minimum book value for firms with net income of \$100 million or more and double the rate on foreign income to 21%</li> <li>Top individual rate to pre-2018 level, new payroll taxes, higher estate taxes</li> <li>Return regulations to Obama-era levels</li> </ul>	<ul style="list-style-type: none"> <li>Cuts to the payroll tax and capital gains tax</li> <li>Make expiring 2017 tax cuts permanent</li> <li>Continue to roll back regulation</li> </ul>
<b>Fiscal and monetary</b>	<ul style="list-style-type: none"> <li>A four-year, \$700-billion "Made in All of America" plan for federal procurement of U.S. manufactured goods</li> <li>Increased spending on infrastructure and health care</li> <li>Government transfers to narrow income inequalities</li> <li>Low Federal Reserve policy interest rates</li> <li>Annual budget deficits probably over \$1 trillion</li> </ul>	<ul style="list-style-type: none"> <li>Support domestic manufacturing via tariffs, other trade restrictions</li> <li>Increased infrastructure and health care spending</li> <li>Limited direct income payments to reduce income inequality</li> <li>Low Federal Reserve policy interest rates</li> <li>Annual budget deficits probably over \$1 trillion</li> </ul>
<b>Foreign economic policy</b>	<ul style="list-style-type: none"> <li>Multilateral pressure on China</li> <li>Reduce tariffs on allied countries</li> <li>Revive U.S. participation in multilateral and nongovernmental organizations (for example, Trans-Pacific Partnership for trade, United Nations agencies)</li> <li>"Made in All of America" plan to encourage overseas manufacturing to return to the U.S.</li> </ul>	<ul style="list-style-type: none"> <li>Continue pressure on China via tariffs and trade, visa, licensing restrictions</li> <li>Continue efforts to re-shore manufacturing jobs, using bilateral negotiations with tariffs for leverage</li> <li>Remain critical of multilateral agreements and nongovernmental organizations</li> </ul>
<b>Health Care and immigration</b>	<ul style="list-style-type: none"> <li>Public option for Affordable Care Act (ACA)</li> <li>Designate Medicare to negotiate lower drug prices</li> <li>Expand Medicare and Medicaid access</li> <li>Control drug price inflation, especially for specialty drugs</li> <li>Expand immigration and ease the citizenship process</li> </ul>	<ul style="list-style-type: none"> <li>Encourage private-sector measures to expand health care</li> <li>Base some Medicare drug prices on comparable foreign costs</li> <li>Tighter immigration policies</li> </ul>
<b>Energy</b>	<ul style="list-style-type: none"> <li>Rejoin the Paris Climate Agreement</li> <li>Endorse policies to target net-zero carbon emissions in power generation</li> <li>Support for renewable energy generation, electric vehicles, and other clean-energy spending</li> </ul>	<ul style="list-style-type: none"> <li>Maintain a favorable regulatory environment for fracking, pipelines, energy exports, and, more generally, fossil fuel generation</li> </ul>
Policies that may or may not be implemented	Biden <i>Likely under a Democratic sweep</i>	Trump <i>Likely under a split government headed by Trump</i>
	<ul style="list-style-type: none"> <li>Tax on unrealized capital gains at death</li> </ul>	<ul style="list-style-type: none"> <li>Further Tax Cuts and Jobs Act tax cuts</li> </ul>
	<ul style="list-style-type: none"> <li>Tax on digital transactions</li> </ul>	<ul style="list-style-type: none"> <li>ACA repeal through an executive mandate</li> <li>Work requirements and other limitations on Medicaid eligibility</li> <li>Convert Medicaid spending to block grants to help cap spending growth rates</li> </ul>
	<ul style="list-style-type: none"> <li>Monetary policy implicitly focusing on racial gaps in jobs, wages, and wealth</li> </ul>	<ul style="list-style-type: none"> <li>Reduce regulations on air and water pollution</li> </ul>
Policies unlikely to become law	Biden <i>Likely under a Democratic sweep</i>	Trump <i>Likely under a split government headed by Trump</i>
	<ul style="list-style-type: none"> <li>Medicare for All</li> <li>Green New Deal</li> </ul>	<ul style="list-style-type: none"> <li>Repeal the ACA</li> </ul>

Source: Wells Fargo Investment Institute, September 1, 2020



# A deeper look at policy issues

## Tax and regulatory policy

- Large ideological differences persist between the two candidates. Biden has called for a variety of higher income, payroll, capital gains, higher estate and caps on deductions; a 28% corporate tax rate (up from 21% today); and a \$15/hour federal minimum wage. Trump wants to make permanent the 2017 tax changes, opposes raising the capital gains rate, and prefers that the states set minimum wage rates.<sup>9</sup>
- Even if the Democrats exercise single-party leadership, tax reform is difficult to negotiate across different power centers in the majority party. The process of compromise may delay and dilute the final version of tax changes, as Republican lawmakers discovered in 2017.
- On regulation, Trump has taken steps to reduce regulations across a number of industries. Biden likely will reinstate greater regulation similar to Obama-era priorities, particularly on climate change, the financial sector, prescription drug prices, and technology companies.

## Fiscal and monetary policy

- Both candidates seem willing to expand federal spending, to encourage economic growth and broaden the U.S. manufacturing base, but their spending preferences differ. The centerpiece of Biden's "Build Back Better" plan is a four-year, \$700 billion "Made in All of America" plan for federal procurement of U.S. manufactured goods. Other Biden plans include a multi-trillion-dollar infrastructure proposal, plus extended income transfers to narrow income inequality. Trump also favors infrastructure spending and support of U.S. manufacturing. However, Senate Republicans have resisted funding a large infrastructure program, while Trump prefers tariff policy to encourage U.S. manufacturing. His income transfer programs probably would be more modest than Biden's.
- The challenge of reaching congressional majorities among progressives, moderate Democrats, and Republicans should preclude highly controversial bills, such as Medicare for All, the Green New Deal, and the repeal of the ACA.



9. WFIJ summary interpretation of policies, based on news analyses that appeared in *The Washington Post*, *The Wall Street Journal*, *Barron's*, *The New York Times*, and [www.JoeBiden.com](http://www.JoeBiden.com) between January 2020 and August 2020

## Foreign economic policy

- Both candidates have taken a tough stance on China. Trump prefers bilateral trade negotiations and tariffs for negotiating leverage, and has not hesitated to implement trade restrictions with U.S. allies. Biden's approach rejects tariffs and has a more traditional, multilateral approach to trade.
- Each of the two tactical approaches have different pros and cons. Trump's tariffs directly penalize Beijing's policy of forced technology transfers, but cycles of reciprocal punitive measures create uncertainty for financial markets and increase U.S. consumer and business costs. Biden's multilateral negotiations likely will move more slowly and should be more familiar for markets. Yet Europe and Japan depend more on trade with China than the U.S. does, and the differences may dilute the enforcement measures of an eventual multilateral deal.

## Health care and immigration

- Biden's plan to revitalize the ACA and Trump's support for more of a private-sector solution seeks to use different tactics to expand health care amid the pandemic. Moreover, both sides support restraining drug-price inflation. However, Biden proposes using Medicare's market clout in drug-company negotiations. Trump proposes to link domestic prices to lower prescription drug prices in overseas markets.
- On immigration, Biden calls for immigration reform that includes a "roadmap to citizenship" for undocumented immigrants, and expanded immigration for workers in sectors from agriculture to technology. Trump is expected to continue executive action to tighten policies on deportation, asylum, and visa policy.

## Energy

- Biden's \$2 trillion proposed spending program to achieve 100% clean energy by 2035 contrasts starkly with Trump's focus on deregulating the production, transportation, and export of fossil fuels.
- The balance of power in Congress likely will not support the most controversial policies. Presidential candidates among the Democrats have pushed Medicare for All and multi-trillion-dollar plans to fuel power generation and transportation by renewable energy. Even under single-party control, we view these multiyear plans as so complex in their technical details, and far-reaching in their impacts, that their passage is unlikely without significant compromises. We have seen that ideology has often adapted to the existing trends.<sup>10</sup>

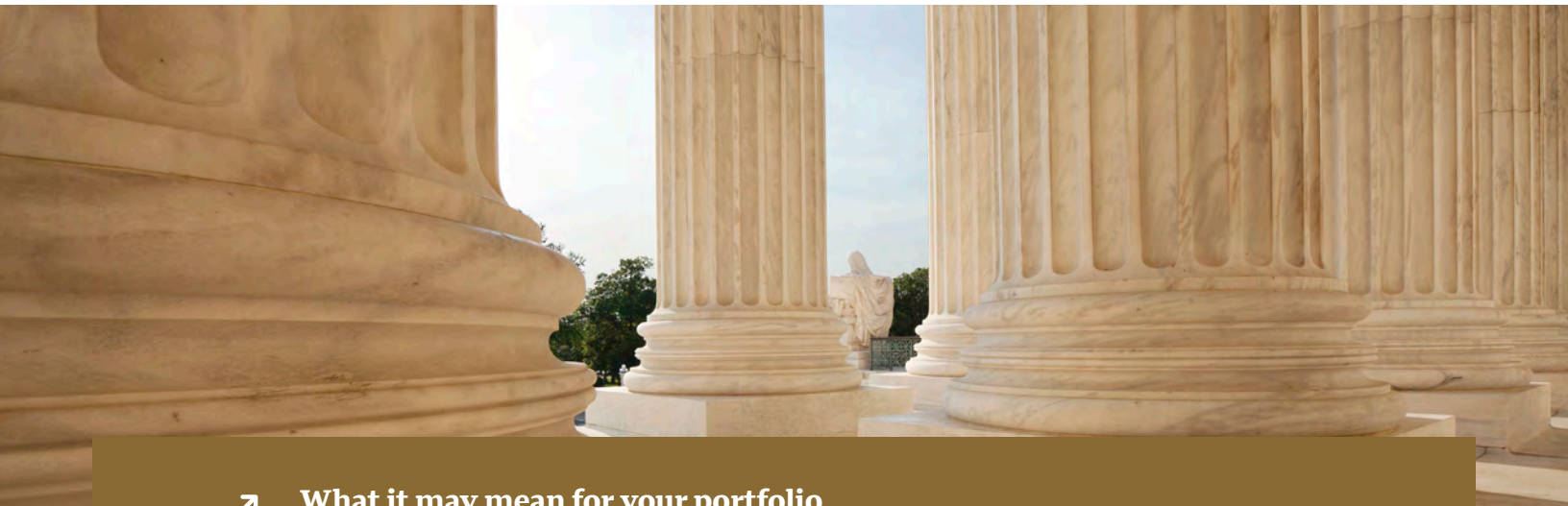
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*From the other side, it seems unlikely that the Republicans can overturn the Affordable Care Act.*



10. We wrote in August 2020 on the technical and practical difficulties facing plans to legislate the U.S. economy from fossil fuel to renewable energy over a fixed time horizon. Our research found a gradual conversion to renewables already in progress but technical constraints that likely limit the pace of a broader changeover. See Policy, Politics, and Portfolios, “‘Green’ gold? Biden’s plan for a green America”, August 25, 2020, at [wellsfargo.com/elections2020](https://wellsfargo.com/elections2020)





What it may mean for your portfolio

## Investment implications

### Global trends and polarization constrain policies

Political differences certainly matter, but we anticipate two factors should temper or redirect the ideological impulses or tactics behind many policy proposals.

First, the global economic themes already in motion should constrain policy agendas. We believe that this is why the two candidates have some similar goals around prominent policy questions—particularly for competing with China, renewing U.S. manufacturing, increasing government spending (for example, on infrastructure), and expanding access to health care.

Put another way, the domestic and international economic backdrop should bend or redirect many ideological impulses. But we believe the candidates' differences on tactics should create investment opportunities. As an illustration, we consider that there is bipartisan support to broaden health care coverage by expanding the insurance system currently available. This should generally favor managed care. By contrast, bipartisan support for restraining drug prices (albeit to different degrees) should be broadly negative for pharmaceuticals. Meanwhile, biotech may face crosscurrents, including possible regulation, but also enhanced spending on research and development.

Our current investment preferences acknowledge several economic and geopolitical themes that appear set to dominate the investment environment during this presidential election cycle.<sup>11</sup> Our most prominent preferences include the following:

1. U.S. financial markets over international markets, because the U.S. has more and better resources for confronting the pandemic and its negative economic consequences.
2. U.S. large- and mid-cap equities, because of their efficiency and greater focus than U.S. small caps and most international equity markets in digital technology and health care, two themes we believe are accelerating in importance. Thus, our preferred equity sectors include the Health Care and technology-oriented sectors (Information Technology, Communication Services, and Consumer Discretionary).
3. High-yield and investment-grade corporates, and preferred securities, which should see positive returns if the gradual economic recovery continues as we expect and Federal Reserve (Fed) policies extend low interest rates into the coming years.

11. For more on these themes and how our guidance aligns with them, please see our “Five Ways the Pandemic Changes the Investment Landscape” report, July 9, 2020, <https://www.wellsfargo.com/investment-institute/id-pandemic-and-investment-landscape>

As a second constraint, there may be limits to what even single-party control of government may expect to accomplish in this age of increasing political polarization. At the end of 2017, some media reports noted the few bills passed into law by the single-party government.<sup>12</sup> Widely accepted metrics used in academic research confirm anecdotal evidence, such as in the preceding health care policy example, suggesting that ideological extremes in Congress create balkanization that works against compromise.<sup>13</sup> Another way to observe this phenomenon is in the declining percentage of presidential campaign promises kept during the first term. From President Woodrow Wilson to President Jimmy Carter, presidents signed legislation equating to an average of 75% of their

campaign promises.<sup>14</sup> The pattern has changed in the past 20 years, however. Presidents George W. Bush and Barack Obama averaged only 47% in their first terms, while Trump had only 24%.<sup>15</sup>

Investors worry about one party sweeping in to control the White House and Congress, but single-party governments occur more frequently than many may realize. Half of the presidential elections since 1945 have delivered single-party government, including three of the past four.<sup>16</sup> Moreover, unified government historically has coincided with S&P 500 Index price returns comparable to or slightly above the 1945–2019 average annual price gain.

## S&P 500 Index return under partisan scenarios, 1945–2019\*

Despite the focus on elections, there is often little return difference attributable strictly to Republican or Democratic leadership. The decisions of millions of private households and businesses also have an impact on the market, and policy is but one influence on these decisions.

	Return**	# of years
<b>Unified government</b>	10.63%	30
Democratic president	9.79%	22
Republican president	12.95%	8
<b>Split Congress</b>	11.81%	11
Democratic president	13.60%	3
Republican president	10.91%	8
<b>Unified Congress</b>	7.97%	32
Democratic president	12.96%	10
Republican president	5.70%	22
<b>All years*</b>	<b>9.67%</b>	<b>73</b>

**Sources:** Bloomberg and Wells Fargo Investment Institute, September 1, 2020

\*The analysis excludes the years 2001–2002 because neither party had a majority in the Senate until Senator Jim Jeffords switched parties in mid-2001.

\*\*Average annual price return of the S&P 500 Index (dividends excluded) during years as defined by different combinations of party leadership in the White House and Congress.

S&P 500 Index is a market capitalization-weighted index composed of 500 widely held common stocks that is generally considered representative of the U.S. stock market.

An index is unmanaged and not available for direct investment. **Past performance is no guarantee of future results.**

Unified government: President and leaders of both congressional chambers are of the same party. Unified Congress: One party leads both chambers of Congress; president is of the other party.

Split Congress: Different parties lead the chambers of Congress.

12. “When divided government worked better than unified government does today,” Steven M. Gillon, The Washington Post, January 19, 2018

13. “The polarized Congress of today has its roots in the 1970s,” Drew DeSilver, Pew Research Center, June 12, 2014

14. “A PolitiFact Special Report: Obama’s First-Term Campaign Promises,” Angie Drobnic Holan, PolitiFact, January 17, 2013

15. [politifact.com/truth-o-meter](http://politifact.com/truth-o-meter), as of August 7, 2020

16. “Party Control of the Presidency and Congress,” Russell D. Renka, Southeast Missouri State University, 2010, <https://cstl-cla.semo.edu/rdrenka/ui320-75/presandcongress.asp>



## Our estimate of potential policy impact on broad U.S. financial markets

Our main conclusion of this report is that, ahead of the elections, we favor aligning portfolios with the dominant economic trends already in place. Our second conclusion is that differences between the two candidates will likely have more perceptibly different market impacts, once the new Congress is seated. Below are our expectations for the directional impacts (from current levels) of policy on U.S. financial markets during the coming four years.

	Biden	Trump
Equities	Neutral to lower	Neutral to higher
Long-term interest rates	Slightly lower	Slightly higher
Dollar's value	Neutral to lower	Neutral to higher

**Source:** Wells Fargo Investment Institute, August 24, 2020. Forecasts are based on certain assumptions and are subject to change.

### Equities

The proposed Biden corporate tax hikes would reduce corporate margins and earnings, and we forecast a \$7 per share reduction in the S&P 500 Index 2021 earnings per share from our 2021 forecast of \$145. Higher tax rates are a negative factor for equity prices but are not necessarily decisive for the direction of equity prices.<sup>17</sup> Both parties favor large federal spending expansions, and without sufficient spending stimulus, a new recession could endanger the election winners' prospects in the 2022 midterm elections. We believe the crucial factor for equities will be the slow but persistent economic recovery we expect through 2022, even if tax rates rise. Consequently, policy under Biden is slightly more negative; under Trump it's slightly more positive.

### Interest rates and the U.S. dollar

Both candidates favor sizable budget deficits. However, even large deficits and sizable U.S. Treasury issuance are unlikely to raise inflation and long-term interest rates. Here, again, the economic trends are more important: Slow global economic growth, rising household saving, and abundant labor supply should maintain low inflation and long-term interest rates and keep Fed policy interest rates near zero.

There is room for marginal differences in long-term rates and the dollar's value. Slower growth and more subdued inflation under a Democratic regime of higher taxes and greater regulation likely would weigh on inflation-sensitive, longer-term yields, narrowing the gap between them and

more policy-sensitive, short-term rates (that is, a flatter yield curve), which would suggest a weaker dollar. A less burdensome tax and regulatory regime under a Republican government should foster moderately stronger growth, higher interest rates, and a slightly stronger dollar.

Beyond the influence of interest rates, the dollar's value should also depend on how trade policy affects growth. Trump's higher tariffs and Biden's higher taxes both undermine U.S. economic growth, but tariffs and trade protections reduce U.S. demand for imports, which reduces U.S. overseas borrowing and supports the dollar. On balance, small changes in economic growth and inflation suggest small moves in the dollar, but slightly stronger under a Trump administration than under a Biden presidency.

*Long-term implications for interest rates and the value of the dollar:* Beyond the next four years, accelerating public debt poses a risk to the U.S. credit rating and to the dollar. Proposals to contain record deficits are noticeably absent on either side of the aisle. Moreover, there is surprisingly modest pushback from both parties against tax and spending proposals that risk adding to historically high deficits and debt relative to the economy's size.

Government financing costs suppressed by subdued inflation and an accommodative Fed have helped keep a potential budget problem at bay. Ultimately, interest rates could become vulnerable to increases, and the dollar to declines, if investor appetite for U.S. Treasury debt wanes enough to overwhelm the Fed's debt purchases.

17. For example, a 2013 budget law raised levies capital gains, dividends, and on the top individual income tax rate, but the 2013 S&P 500 Index total return in excess of 32% was the best calendar-year gain since 1997.

## Equity sectors

We believe the sectors most in line for potential policy impacts appear to be Energy, Financials, Health Care, and those influenced most directly by digital technology innovation (Information Technology and Communication Services).

*Energy:* Policy could be most significant in terms of the regulation of fossil fuels and broad new subsidies for renewable energy. Trump policy likely will offer little change to current opportunities.

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*However, under the Democrats, a larger shift is likely—more favorable on renewable energy, less favorable on fossil fuel production, transportation, and export.*

*Financials:* A rise in long-term interest rates may improve margins, while additional regulation would add costs. Of particular note would be policies regarding stock buybacks and dividends, and additional regulatory scrutiny in lending practices.

*Health Care:* Both parties favor expanding health care coverage and so does our outlook. However, the parties approach the problem differently. Expansion of the ACA would likely be positive for managed care. Prescription drug price caps would likely be negative for pharmaceuticals. Biotech companies may benefit if the federal government spends more on health care research and development or if tax policy incentivizes pharmaceutical companies to move production from China to the U.S.

*Information Technology and Communication Services:* Policies to encourage innovation and research and development would likely benefit the sector. Proposals to insulate new technology development from Chinese firms could encourage domestic production but may harm international business growth (as Chinese or Taiwanese firms take over in markets where U.S. firms retreat). Tax reform that raises tax liability on overseas profits would likely be negative. Regulation of technology firms remains a potential policy question but is unlikely to change our favorable view on the sector.<sup>18</sup>

18. For a variety of reasons, we do not see extensive regulation and the breakup of technology firms as imminent or inevitable. Source: Policy, Politics & Portfolios, “Regulatory clouds move toward interactive media and ‘big tech,’” Wells Fargo Investment Institute, June 25, 2019, [wellsfargo.com/elections2020](https://wellsfargo.com/elections2020)



## Investor preparation and planning are crucial as events unfold

### Some steps may be appropriate to take before the elections

Some of the tax strategies available today may cease in 2021, with some changes retroactive to January 1, 2021. We favor consulting with financial advisors and wealth planning teams, together with tax and legal counsel, for help in reviewing income or capital gains pull-forward strategies as well as potential changes to estate planning.<sup>19</sup>

The differences between candidates may dictate much of the daily news, but we foresee that the pandemic and its related trends will remain relevant for far longer. These dominant trends include slow economic growth, low inflation and interest rates, accelerated spending on e-commerce and remote access to services, and changing international relationships. Our current investment preferences, listed on page 11, align with these trends.

### But we prefer not to extrapolate campaign promises into portfolios

When it comes to planning portfolio reallocations for the election results, our planning horizon extends into 2021. The political agenda and its priorities, as well as the balance of power in Congress and important appointments, may not be clear until sometime in the first quarter of 2021.

### The congressional balance of power and the legislative agenda will remain questions into 2021

Single-party government may not eliminate ideological differences that can complicate the passage of controversial issues. It is difficult to know how power will settle among the progressive and moderate Democrats and the Republicans. Still, we expect the old adage to hold—namely, that across ideologically diverse groups, the moderates typically hold the deciding votes. So, the most controversial proposals from the campaign trail are likely to face delay and dilution.

### Market opportunities may not evolve until cabinet and other key positions are staffed

A regularity of new presidential administrations is that appointments to senior administration roles after the elections are material for translating the president's initiatives into effective regulation and legislation. Significant positions include leadership at the Fed, Federal Deposit Insurance Corporation (FDIC), Securities and Exchange Commission (SEC), Supreme Court justices; and senior White House staff, including health, education, Treasury, and other cabinet and senior staff. Without knowing who will fill these positions, the election results on November 3 will not settle the investment outlook.

### Elections are the beginning—not the end—of any policy changes

We prefer not to extrapolate today's campaign promises into next year's action. Instead, we favor using this report as a road map that may reveal investment opportunities as the political agenda finally emerges early next year. At that time, we believe the preparation undertaken now should reward the investor who can ignore the increasingly heated campaign rhetoric.

19. Wells Fargo and its affiliates are not legal or tax advisors. Be sure to consult your own legal or tax advisor before taking any action that may involve tax consequences. Tax laws or regulations are subject to change at any time and can have a substantial impact on individual situations.

# Investment expertise and advice to help you succeed financially

Wells Fargo Investment Institute is home to more than 145 investment professionals focused on investment strategy, asset allocation, portfolio management, manager reviews, and alternative investments. Its mission is to deliver timely, actionable advice that can help investors achieve their financial goals.

For assistance with your investment planning or to discuss the points in this report, please talk to your investment professional.

## Risk Considerations

Forecasts and targets are based on certain assumptions and on views of market and economic conditions which are subject to change.

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. **Foreign investing** has additional risks including those associated with currency fluctuation, political and economic instability, and different accounting standards. These risks are heightened in emerging markets. **Small- and mid-cap stocks** are generally more volatile, subject to greater risks and are less liquid than large company stocks. **Bonds** are subject to market, interest rate, price, credit/default, liquidity, inflation and other risks. Prices tend to be inversely affected by changes in interest rates. **High yield (junk) bonds** have lower credit ratings and are subject to greater risk of default and greater principal risk. Preferred securities have special risks associated with investing. Preferred securities are subject to interest rate and credit risks. **Preferred securities** are generally subordinated to bonds or other debt instruments in an issuer's capital structure, subjecting them to a greater risk of non-payment than more senior securities. In addition, the issue may be callable which may negatively impact the return of the security.

**Communication services** companies are vulnerable to their products and services becoming outdated because of technological advancement and the innovation of competitors. Companies in the communication services sector may also be affected by rapid technology changes; pricing competition, large equipment upgrades, substantial capital requirements and government regulation and approval of products and services. In addition, companies within the industry may invest heavily in research and development which is not guaranteed to lead to successful implementation of the proposed product. Risks associated with the **Consumer Discretionary** sector include, among others, apparel price deflation due to low-cost entries, high inventory levels and pressure from e-commerce players; reduction in traditional advertising dollars, increasing household debt levels that could limit consumer appetite for discretionary purchases, declining consumer acceptance of new product introductions, and geopolitical uncertainty that could affect consumer sentiment. The **Energy** sector may be adversely affected by changes in worldwide energy prices, exploration, production spending, government regulation, and changes in exchange rates, depletion of natural resources, and risks that arise from extreme weather conditions. Investing in the **Financial** services companies will subject an investment to adverse economic or regulatory occurrences affecting the sector. Some of the risks associated with investment in the **Health Care** sector include competition on branded products, sales erosion due to cheaper alternatives, research and development risk, government regulations and government approval of products anticipated to enter the market. Risks associated with the **Information Technology** sector include increased competition from domestic and international companies, unexpected changes in demand, regulatory actions, technical problems with key products, and the departure of key members of management. Technology and Internet-related stocks, especially smaller, less-seasoned companies, tend to be more volatile than the overall market.

## General Disclosures

Forecasts are not guaranteed and based on certain assumptions and on views of market and economic conditions which are subject to change.

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