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November 4, 2020

Developments moving faster than ink can dry

Key takeaways

- With the Presidential election and some Congressional elections still undecided, both equities and bonds rose the day after polls closed.
- We retain our optimistic and glass half-full perspective for diversified portfolio returns.
- The news cycle will likely remain intense, but we encourage clients to stick with their plan and update their investment professional with questions or changes to their unique circumstances.

Irrespective of one's political views, Tuesday's election results can be characterized as dynamic, and some results may remain so for days or longer. As we write, the Presidential and several Congressional elections have yet to be called, leaving investors to ponder when we may have as close to definitive results as possible given this year's unique voting circumstances. Despite some uncertainties, we have gained at least some clarity on outcomes, and that has led to pronounced moves in specific asset classes and sectors. The dominant political theme, at least for now, is a greater split within Congress, with Democrats losing a few seats in the House and the Senate remaining under Republican control. While the Presidential election has not been determined, the potential for a former Vice President Biden win amid these Congressional shifts opens the possibility of a divided government relative to pre-election expectations. In this communication, we summarize our current views based on what we know as of 4:00 p.m. CT on November 4, 2020. As always, we will update you on any changes to those views.

Heading into the election season, we cautioned investors that this could be a very close election, closer than what polls predicted in the weeks and months beforehand. We published our election outlook piece on September 30, giving former Vice President Biden a slight edge over President Trump. We also viewed the U.S. Senate as a toss-up and predicted that Democrats would retain the U.S. House of Representatives. Through the Presidential and Vice Presidential debates, congressional and gubernatorial campaigns and the final pre-election push, we maintained our view that this election had the potential to be tight and that a contested result was a realistic probability.

Regardless of whether these views prove prescient, the most important point we made in that piece and a follow-up paper published a week ago today is that medical progress remains the most important market driver. As always, discussing COVID-19's financial impact feels insensitive relative to the more important human impact. Our thoughts remain with those affected, both directly and indirectly, as the virus continues to spike around the world. While election results are clearly today's primary focus, global economic reopening based on an anti-viral treatment has a larger and more durable capital market impact than what we think we know today and will learn more about in coming days about election results.

Our overall view remains that the glass is half-full for future return prospects for traditionally riskier asset classes like equities and real assets. While we do not recommend investors abandon bond portfolios, given current low interest rates, bond or fixed income forward return prospects look less attractive relative to equities. Three reasons buttress our optimistic viewpoint:

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1. Economic data, at the margin, is improving. Through our proprietary Global Health Check, we monitor over 1,000 unique data points that provide us with insights across geographies and industries. We are cautious about trends, since medical experts suggest we may be entering an acute COVID-19 spread phase and places like Europe enter targeted shut downs intended to thwart further spread. However, both domestic and emerging market regions appear to be migrating out of a recessionary phase and into a recovery phase. This recovery's depth and durability remain central questions as the data fluctuates, but we are seeing encouraging signs amid challenges.
2. Medical progress is becoming more tangible. As noted above, we could be entering a challenging virus phase, but the medical community's knowledge of prevention and care continues to grow. Critically, several leading pharmaceutical and biotechnology companies are entering or moving through regulatory trials to determine efficacy. Predictions on when a distributable vaccine will arrive as well as uptake likelihood across the global population vary, but we get closer each day. In the circular relationship of businesses unable to sustain growth in the current environment and consumer activity stifled by mobility and remote work obstacles, a broad economic reopening is unlikely to occur until we attain a medical solution.
3. Ongoing government support, with the potential for incremental additions, can help bridge the gap between present day corporate and consumer risks. Again, irrespective of political views, the CARES Act (the federal government's stimulus bill) coupled with the U.S. Federal Reserve's actions provided needed liquidity to markets, companies and consumers, mitigating the pandemic's early effects. Additional pre-election stimulus proved elusive, but Senate Majority Leader Mitch McConnell noted at an event today in Kentucky that, "We need to sit down and talk to each other like we did back in March and April and address the problem and I'm confident we will no matter who ends up running the government."¹ Global central banks continue to adopt pro-growth policies via asset purchase programs, with the European Central Bank (ECB) hinting a week ago that it would step up efforts in December in response to recently imposed country restrictions and curfews designed to halt recent COVID-19 spread.²

Today's outcomes, those that are known, contested and still to-be-determined, do not alter our glass half-full view. We continue to prefer domestic equities over international equities but note the underlying fundamental strength of Asia relative to Europe. At the equity sector level, we continue to favor secular growth sectors that can thrive in the uncertainty ahead with resilient business models. Information Technology, Consumer Discretionary and Communication Services are favored sectors, and Healthcare may get a boost from perceived lower regulatory scrutiny in a divided government. Meanwhile, earnings visibility within Financials, Energy, Industrials and Materials sectors appears less clear. Within bonds, we continue to like higher-quality corporate bonds and municipal bonds, and we continue to evaluate real asset opportunities should inflationary prospects increase.

Even though today marks the day after the elections, the news surrounding the elections and its implication for markets and the economy will continue at a rapid pace. Our team actively monitors developments as they unfold, and our goal is to update you with our viewpoints without unnecessarily adding to the cacophony. As always, the most important step you can take is to engage with your financial professional and establish or confirm a financial plan tailored to your unique circumstances. Please do not hesitate if you have specific questions we can answer and thank you for your trust.

¹ <https://www.businessinsider.com/mcconnell-stimulus-package-republicans-passed-by-end-of-2020-2020-11> Accessed 4 November 2020.

² <https://www.reuters.com/article/us-ecb-policy-decision/ecb-keeps-stimulus-unchanged-but-hints-at-dec-action-idUSKBN27E269> Accessed 4 November 2020.

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