STATE STREET GLOBAL ADVISORS

US 2020: The COVID Election — Part III

IMPORTANT NOTIFICAITON

The following material is provided by a third-party strategist unaffiliated with AssetMark. The strategist is solely responsible for its content. Please read the risks and disclosures section for additional important information. AssetMark has not verified the accuracy of the information contained in this material.

For financial advisor use with advisory clients.

C20-16585 | 09/20120 | EXP 09/30/2021

Insights
Multi-Asset Solutions

August 11, 2020

US 2020: The COVID Election — Part III

Elliot Hentov
Head of Policy and Research

Rebecca Chesworth
Senior Equity ETF Strategist, SPDR ETFs

This is Part III of a mini-series that looks at the US Presidential Elections. Parts I and II examined the macroeconomic and broad asset class choices in the context of the elections. In early September, we will publish a comprehensive and in-depth report on equity market performances in relation to past elections as well as expected moves this cycle.

This is the third installment of our mini-series on the US elections. The first part took into account market risks that may arise from a disputed US election, while the second part reviewed competing policy platforms and their implications for asset allocation. Although we concluded that equity investing would overall become more challenging under a Biden administration, we also suggested that there would be some winners from his public investment plans. In this third part, we would like to provide an overview of equity sectors that would lend themselves better to the policies of a Democratic government.

Key Policy Drivers

First, it is important to note that most tax plans are broadly negative. Above all, plans to increase the statutory corporate tax rate, raise the tax on foreign earnings (Global Intangible Low-Taxed Income) and set a minimum corporate tax rate are all headwinds to earnings. On top of that, plans to raise personal tax income on the wealthiest Americans (higher capital gains taxes on million-dollar plus capital income and raising payroll tax threshold on households earning over US$400,000) could further drain capital out of financial markets.

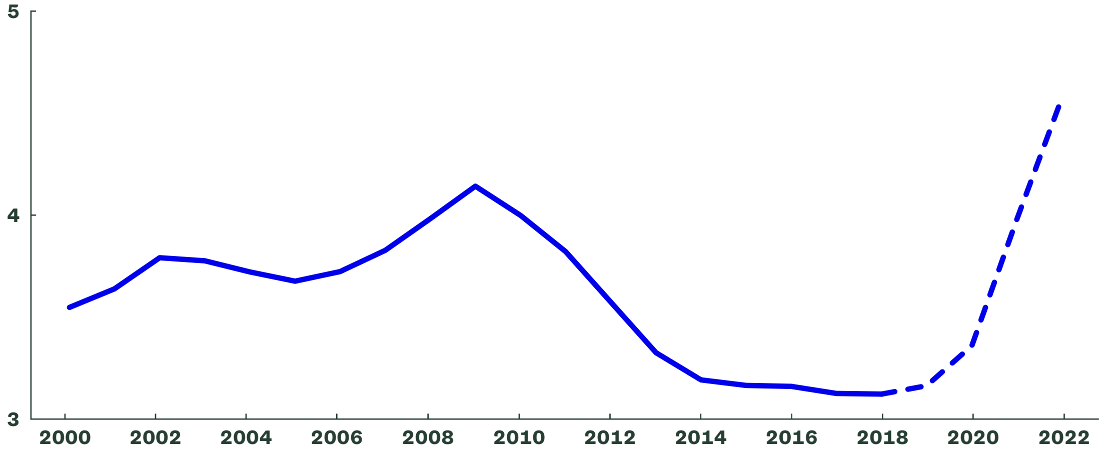
Second, there is likely to be a determination to boost earnings and bargaining power of labour. The most glaring area is the expectation of an increased federal minimum wage, but there would be other measures that could prove to be costly to labour-dependent industries as well.

Third, the degree of margin erosion that a rollback of the policies of Trump administration can cause is less quantified. There could be broad disruption from new regulatory appointees, changes in fiduciary powers, new consumer protection powers and an overarching push to promote climate change mitigation. Add in the aim to reduce income and racial inequalities, and it is clear that the regulatory landscape will be uneven. Individual companies and industries could be affected in varying magnitudes, resulting in some interesting investment opportunities.

Fourth, a Biden administration would be more determined to promote public investment. US infrastructure remains starkly underfunded and the post-COVID-19 economic shock should facilitate the political case for government spending to boost the economy's recovery. In his pre-COVID-19 platform, Joe Biden had already foreseen an annual boost of roughly US$500 bn, focusing on healthcare, transport, housing and education (especially early education and childcare).

Mr. Biden has now added a substantial front-loaded proposal to enhance government spending on R&D (half of which is to be directed toward clean energy) as well as US-focused procurement of products, materials and services. In this approach, only the defense industry would be a net loser of government spending.

Figure 1
Government Investment As Percentage of GDP — 2000–2022



Note: Estimates from 2019 onward by State Street Global Advisors.
Source: Organisation for Economic Co-operarion and Development, State Street Global Advisors.

As Figure 1 shows, assuming Mr. Biden can channel one third of those plans into the first two years, it would materially lift government investments compared with that of the previous decade.

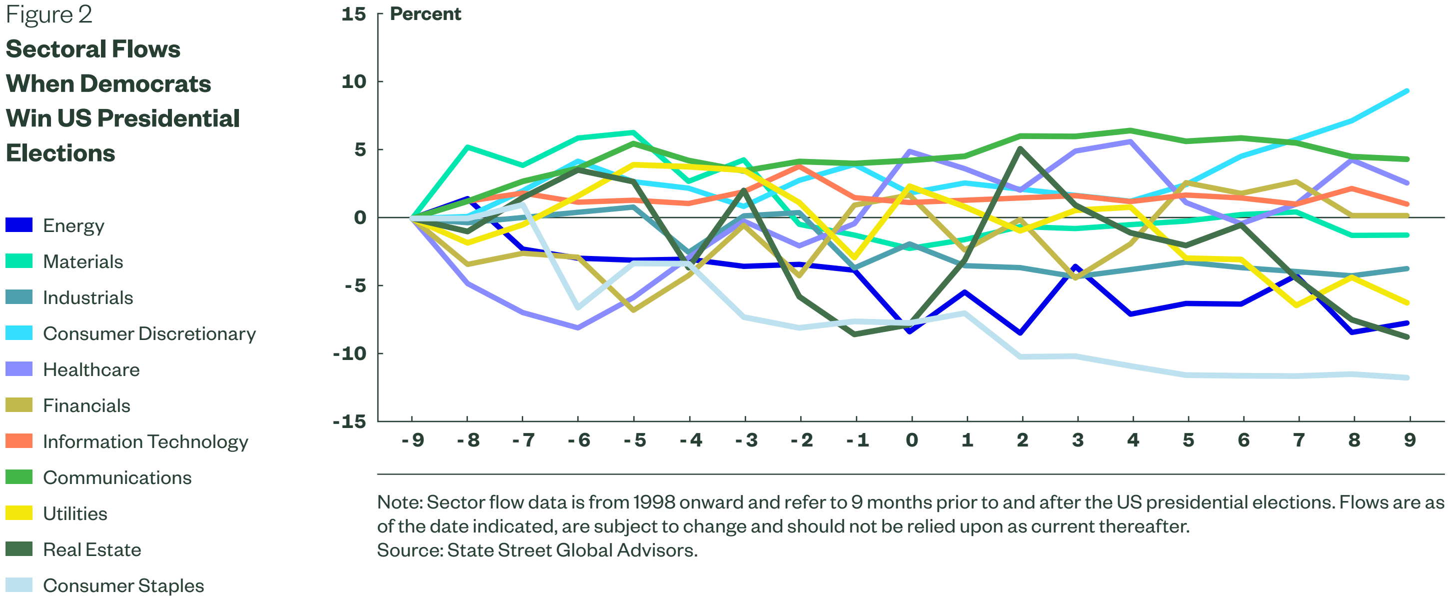
Sector Overview

Tax changes would negatively impact corporate earnings across the market, reversing some of the benefits to earnings per share seen since 2016. Furthermore, without the incentive to repatriate cash, companies could keep cash earnt outside the United States (US) abroad with a knock-on impact on the rate of dividends and share buybacks (the sectors that saw the highest increases in buyback activity in 2018 after the Tax Cuts and Jobs Act were Materials, Utilities and Technology). However, public spending and climate-friendly policies could be beneficial offsetting factors to tax increases.

Compared with the last presidential election, two sectors may experience less scrutiny, namely Healthcare and Financials. First, Healthcare has been at the fulcrum of political debate for years and has been exposed to changing insurance plans as well as desires to manage pricing and prescription processes. During the current election campaign, a pandemic is still raging, and therefore the country is reliant on healthcare provisions and supplies. A full economic recovery depends on an effective vaccine — not only development but also manufacturing and distribution.

Historic fears of political repercussions are reflected in the underweight positioning of institutional investors in US Healthcare and net outflows from the sector pre and post past election dates (Figure 2). However, given the sector's stable earnings growth and lower risk to business models, we believe there could be an attractive opportunity this time around.

Figure 2
Sectoral Flows When Democrats Win US Presidential Elections



Note: Sector flow data is from 1998 onward and refer to 9 months prior to and after the US presidential elections. Flows are as of the date indicated, are subject to change and should not be relied upon as current thereafter.
Source: State Street Global Advisors.

Financials benefited significantly from the Trump administration's deregulation and appointment of industry-friendly policymakers. We do not expect as much focus in this campaign: a tax rise would hit earnings and consumer-facing products may incur margin shrinkage. Substantially tighter financial regulation in the coming years, however, is unlikely given the regulatory changes post the Global Financial Crisis that remain in place.

The proposed green policies present a switch proposition. Mr. Biden's plans could benefit Utilities in terms of their transition toward cleaner electricity generation. This could mirror large European electricity providers that have enjoyed re-ratings on the back of their leadership in energy transition. By contrast, the already pressurised Energy sector could be hit by these fiscal policies even as low oil prices are offering no relief to their profit and loss accounts.

The cyclical groupings of Industrials and Materials are traditional beneficiaries of infrastructure spending. Whilst the latter will have to contend with lower defense orders for aerospace equipment, the miners and construction material companies in the Materials sector are well placed for new building projects.

Meanwhile there could be mixed results for Consumer Discretionary businesses including retailers, hoteliers and leisure companies. With a fillip to the consumer balance sheet under Mr. Biden, there may be upside from consumer spending, but many of the corporates are large employers of lowly paid workers. The outlook may not be as rosy as after the last Democratic win, when large investor inflows followed.

By contrast, Technology has a relatively low labour/capital mix and would be less affected by employee wage hikes. This sector stands out for its secular growth opportunities, but these could be tempered near term by tax changes and a more determined stance on antitrust enforcement.

Investment Implications

Overall, US and global equities could see a rise in volatility over coming months until markets can reasonably forecast an outcome. Such an uncertain environment could lend itself to taking a selective approach to investment. During the 2016 election, we witnessed a dramatic widening of dispersion of returns between sectors and a sharp rise in interest for sector exchange-traded funds as a means of positioning against various political outcomes.

While all the sectors will face mixed implications across different industries, we look favorably on Healthcare, Materials and Utilities as being well placed to navigate any political transition in the US.

In addition to the pandemic, social justice themes will be a significant feature in coming years. The priority would be criminal justice reform to lessen police abuse and reduce the disproportionate sentencing of black youth. It goes without saying that the investment implications of the Black Lives Matter movement cannot be overemphasized. Such a major societal change will inevitably drive investment decisions and corporate governance in the coming years.

Together with the increased environmental focus, this focus on social justice is likely to accelerate environmental, social and corporate governance parameters in the US to that already seen in Europe. Among sectors, Utilities are better positioned in relative terms to take advantage of this new trend.

The authors are grateful to Anthi Tsouvali and State Street Global Markets for contributing to the article.

About State Street Global Advisors

Our clients are the world's governments, institutions and financial advisors. To help them achieve their financial goals we live our guiding principles each and every day:

- Start with rigour
- Build from breadth
- Invest as stewards
- Invent the future

For four decades, these principles have helped us be the quiet power in a tumultuous investing world. Helping millions of people secure their financial futures. This takes each of our employees in 27 offices around the world, and a f irm-wide conviction that we can always do it better. As a result, we are the world's third-largest asset manager with US $3.05 trillion* under our care.

* This figure is presented as of June 30, 2020 and includes approximately $69.52 billion of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated.

ssga.com

Marketing Communications

State Street Global Advisors Worldwide Entities

Abu Dhabi: State Street Global Advisors Limited, ADGM Branch, Al Khatem Tower, Suite 42801, Level 28, ADGM Square, Al Maryah Island, P.O Box 76404, Abu Dhabi, United Arab Emirates. Regulated by the ADGM Financial Services Regulatory Authority. T: +971 2 245 9000. **Australia:** State Street Global Advisors, Australia, Limited (ABN 42 003 914 225) is the holder of an Australian Financial Services License (AFSL Number 238276). Registered office: Level 14, 420 George Street, Sydney, NSW 2000, Australia. T: +612 9240-7600. F: +612 9240-7611. **Belgium:** State Street Global Advisors Belgium, Chaussée de La Hulpe 120, 1000 Brussels, Belgium. T: 32 2 663 2036. F: 32 2 672 2077. SSGA Belgium is a branch office of State Street Global Advisors Ireland Limited. State Street Global Advisors Ireland Limited, registered in Ireland with company number 145221, authorised and regulated by the Central Bank of Ireland, and whose registered office is at 78 Sir John Rogerson's Quay, Dublin 2. **Canada:** State Street Global Advisors, Ltd., 1981 McGill College Avenue, Suite 500 , Montreal, Qc, H3A 3A8, T: +514 282 2400 and 30 Adelaide Street East Suite 800, Toronto, Ontario M5C 3G6. T: +647 775 5900. **France:** State Street Global Advisors Ireland Limited, Paris branch is a branch of State Street Global Advisors Ireland Limited, registered in Ireland with company number 145221, authorised and regulated by the Central Bank of Ireland, and whose registered office is at 78 Sir John Rogerson's Quay, Dublin 2. State Street Global Advisors Ireland Limited, Paris Branch, is registered in France with company number RCS Nanterre 832 734 602 and whose office is at Immeuble Défense Plaza, 23-25 rue Delarivière-Lefoullon, 92064 Paris La Défense Cedex, France. T: (+33) 1 44 45 40 00. F: (+33) 1 44 45 41 92. **Germany:** State Street Global Advisors GmbH, Brienner Strasse 59, D-80333 Munich. Authorised and regulated by the Bundesanstalt für Finanzdienstleistungsaufsicht ("BaFin"). Registered with the Register of Commerce Munich HRB 121381. T: +49 (0)89-55878-400. F: +49 (0)89-55878-440. **Hong Kong:** State Street Global Advisors Asia Limited, 68/F, Two International Finance Centre, 8 Finance Street, Central, Hong Kong. T: +852 2103-0288. F: +852 2103-0200. **Ireland:** State Street Global Advisors Ireland Limited is regulated by the Central Bank of Ireland. Registered office address 78 Sir John Rogerson's Quay, Dublin 2. Registered Number: 145221. T: +353 (0)1 776 3000. F: +353 (0)1 776 3300. **Italy:** State Street Global Advisors Ireland Limited, Milan Branch (Sede Secondaria di Milano) is a branch of State Street Global Advisors Ireland Limited, registered in Ireland with company number 145221, authorised and regulated by the Central Bank of Ireland, and whose registered office is at 78 Sir John Rogerson's Quay, Dublin 2. State Street Global Advisors Ireland Limited, Milan Branch (Sede Secondaria di Milano), is registered in Italy with company number 10495250960 — R.E.A. 2535585 and VAT number 10495250960 and whose office is at Via Ferrante Aporti, 10 — 20125 Milano, Italy. T: +39 02 32066 100. F: +39 02 32066 155. **Japan:** State Street Global Advisors (Japan) Co., Ltd., Toranomon Hills Mori Tower 25F 1-23-1 Toranomon, Minato-ku, Tokyo 105-6325 Japan. T: +81-3-4530-7380. Financial Instruments Business Operator, Kanto Local Financial Bureau (Kinsho #345), Membership: Japan Investment Advisers Association, The Investment Trust Association, Japan, Japan Securities Dealers' Association. **Netherlands:** State Street Global Advisors Netherlands, Apollo Building, 7th floor Herikerbergweg 29 1101 CN Amsterdam, Netherlands. Telephone: 31 20 7181701. SSGA Netherlands is a branch office of State Street Global Advisors Ireland Limited, registered in Ireland with company number 145221, authorised and regulated by the Central Bank of Ireland, and whose registered office is at 78 Sir John Rogerson's Quay, Dublin 2. **Singapore:** State Street Global Advisors Singapore Limited, 168, Robinson Road, #33-01 Capital Tower, Singapore 068912 (Company Reg. No: 200002719D, regulated by the Monetary Authority of Singapore). T: +65 6826-7555. F: +65 6826-7501. **Switzerland:** State Street Global Advisors AG, Beethovenstr. 19, CH-8027 Zurich. Authorised and regulated by the Eidgenössische Finanzmarktaufsicht ("FINMA"). Registered with the Register of Commerce Zurich CHE-105.078.458. T: +41 (0)44 245 70 00. F: +41 (0)44 245 70 16. **United Kingdom:** State Street Global Advisors Limited. Authorised and regulated by the Financial Conduct Authority. Registered in England. Registered No. 2509928. VAT No. 5776591 81. Registered office: 20 Churchill Place, Canary Wharf, London, E14 5HJ. T: 020 3395 6000. F: 020 3395 6350. **United States:** State Street Global Advisors, One Iron Street, Boston, MA 02210-1641. T: +1 617 786 3000.

The views expressed in this material are the views of Elliot Hentov and Rebecca Chesworth through 11 August 2020 and are subject to change based on market and other conditions. This document contains certain statements that may be deemed forward looking statements. Please note that any such statements are not guarantees of any future performance and actual results or developments may differ materially from those projected.

The information provided does not constitute investment advice and it should not be relied on as such. It should not be considered a solicitation to buy or an offer to sell a security. It is not known whether the sectors or securities shown will be profitable in the future. It does not take into account any investor's particular investment objectives, strategies, tax status or investment horizon. You should consult your tax and financial advisor.

All information is from State Street Global Advisors unless otherwise noted and has been obtained from sources believed to be reliable, but its accuracy is not guaranteed. There is no representation or warranty as to the current accuracy, reliability or completeness of, nor liability for, decisions based on such information and it should not be relied on as such.

Past performance is not a guarantee of future results. Investing involves risk including the risk of loss of principal.

The trademarks and service marks referenced herein are the property of their respective owners. Third party data providers make no warranties or representations of any kind relating to the accuracy, completeness or timeliness of the data and have no liability for damages of any kind relating to the use of such data.

For EMEA Distribution: The information contained in this communication is not a research recommendation or 'investment research' and is classified as a 'Marketing Communication' in accordance with the Markets in Financial Instruments Directive (2014/65/EU) or applicable Swiss regulation. This means that this marketing communication (a) has not been prepared in accordance with legal requirements designed to promote the independence of investment research (b) is not subject to any prohibition on dealing ahead of the dissemination of investment research.

Investing in foreign domiciled securities may involve risk of capital loss from unfavorable fluctuation in currency values, withholding taxes, from differences in generally accepted accounting principles or from economic or political instability in other nations.

ID275607-3197293.1.1.GBL.RTL 0820
Exp. Date: 31/08/2021