CITY NATIONAL ROCHDALE

How Will the Election Results Impact Markets?

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On the Radar

FAQS ON THE MARKETS AND ECONOMY

How will the election results impact markets?

CNR has been largely agnostic from a financial perspective on the election, seeing positive opportunities for investors regardless of the outcome (see our Post Election Special Bulletin).

History has taught us that markets have done well under all combinations of political power, and we suspect that will continue. Although elections bring uncertainty, as that uncertainty fades, stocks reconnect to fundamentals that are influenced — but not determined — by governmental policies.

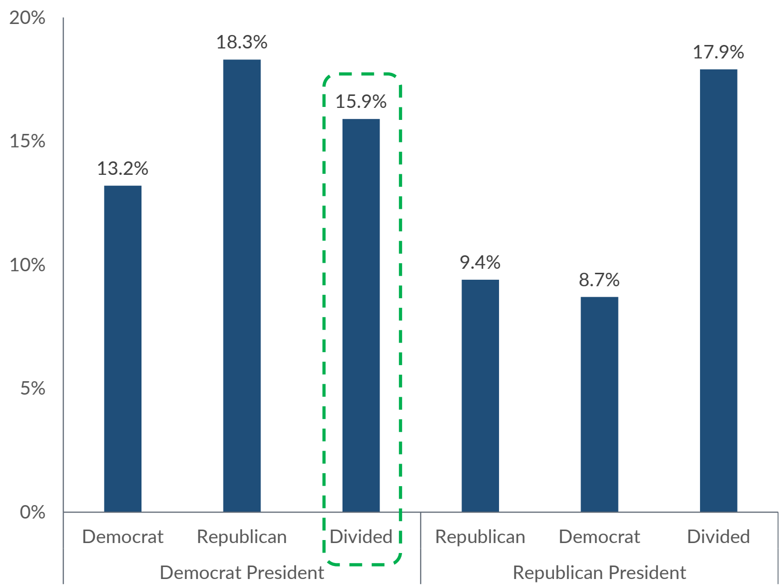
Given the likelihood of a Biden presidency and divided control of Congress, we do not expect significant shifts in policy that would have a material impact on the current trajectory of the economy or equity markets.

Indeed, early indications are that investors have welcomed prospects of a divided government all but eliminating the likelihood of substantial tax increases and sweeping regulatory reform, but not removing the potential for an agreement among lawmakers on another round of COVID-19 relief.

In sectors and industries where policy changes could have positive or negative impacts, rigorous company analysis and active management will be key.

However, in the regard to the broader outlook, we expect fiscal and monetary policy to remain exceptionally supportive regardless of the election results, and the economic recovery from the pandemic, along with improving prospects for an effective vaccine, to be the main driving force for markets over the coming year.

Stock Performance Under Different Congressional Control
(S&P 500 Annual Returns 1950 – 2019)



Source: S&P 500.

KEY QUESTIONS

What is the impact on the economy from the recent weakness in the U.S. dollar?

What did the Fed decide at their monetary policy meeting last week?

Is the labor market still strong?

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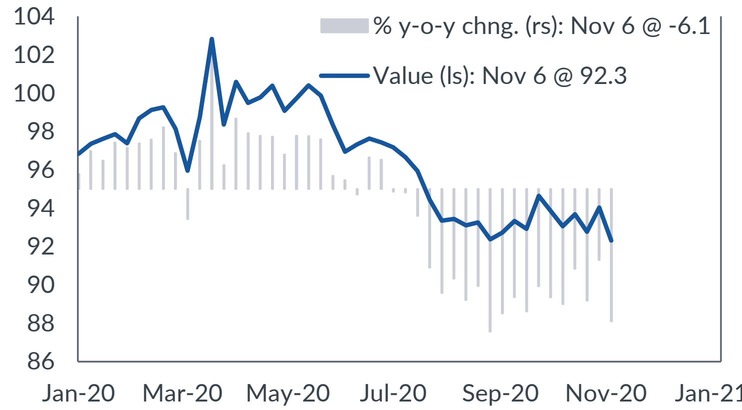
The dollar began weakening in the late-spring as the probability of a phase four fiscal stimulus plan began to fade (see chart). Then, during the early-summer, as the number of COVID-19 cases began to rise, it fell further.

Since late-summer, the USD has traded in a narrow channel, reflecting global pressures of reduced stimulus and concerns of another wave of COVID-19 as we enter the winter months.

All else being even, a weaker dollar makes exports more attractive (helping domestic exporters) and imports more expensive, which will help increase inflationary pressures (the Fed would like to see). That said, the movement in the value of the dollar over the past year is not enough to have a measurable impact on either of those events.

U.S. Dollar

$, trade weighted value



Source: Bloomberg as of November 6, 2020.

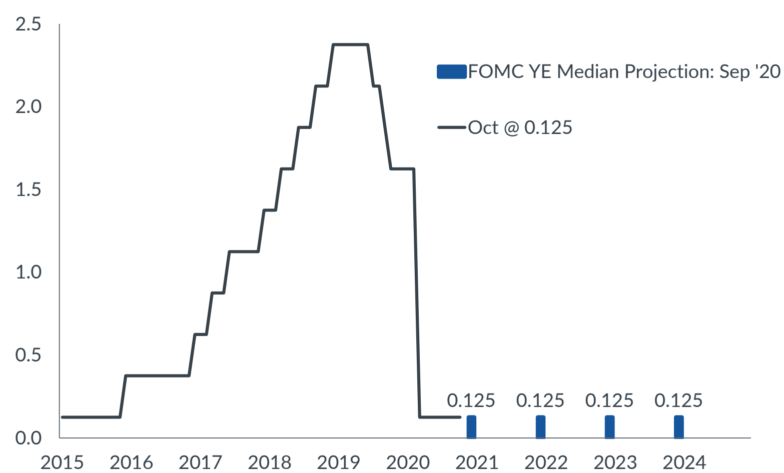
What did the Fed decide at their monetary policy meeting last week?

The Fed is holding pat. They unanimously decided to keep the federal funds rate unchanged at 0.125% (see chart) and will keep the pace of asset purchases unchanged (treasuries at $80 per month, mortgages at $40 per month). All of this was consistent with market expectations.

The Fed acknowledged the recovery is underway, but the path of the economy hinges on the course of the coronavirus. The recovery depends on the public getting back to their way of life and spending habits they had before the pandemic set in.

They also believe more fiscal aid from the federal government is needed. This is especially true for industries that have been significantly impacted by the virus, like hospitality, airlines, and state and local government workers. The greater the fiscal support, the stronger the recovery.

Federal Funds Rate & FOMC Projections (%)



Source: Federal Reserve Bank as of October 2020.

Is the labor market still strong?

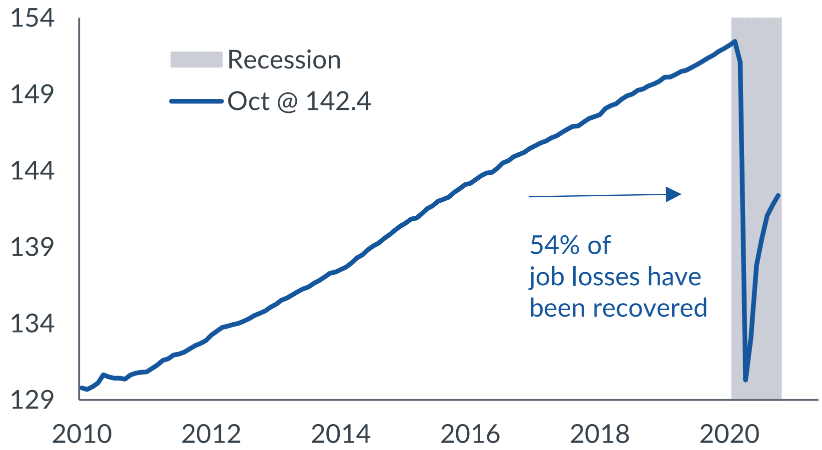
The October labor report was unquestionably strong. The unemployment rate plunged from 7.9% to 6.9%, which places it 0.7 ppts below the Fed's median year-end forecast of 7.6%.

Nonfarm payrolls increased 638,000. It is a strong number in normal times but represents a declining trend of four months, since peaking in June at 4.8 million. That said, the details were more encouraging. The gain represents the private sector increasing 906,000 (larger than September's gain of 892,000) and government jobs declining 268,000. The decline in government jobs can be primarily attributed to Census-related layoffs of 147,000 (there are still 99,000 remaining Census workers).

Overall, the economy has regained roughly 12 million of the 22 million jobs lost due to the pandemic, representing a 54% recovery (see chart).

The troubling part is that the number of people on permanent layoffs (3.7 million) now exceeds those on temporary layoff (3.2 million). This is normally a sign of slowing job growth in the future.

Nonfarm Payrolls
millions, seasonally adjusted



Source: Bureau of Labor Statistics as of October 2020.

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