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Wake Me When November Ends

If I offered you a pill (with zero side effects) that would allow you to avoid any reference to the 2024 elections until two days after Election Day, would you take it? Based on recent conversations, many of you would. And for those e-mailing about where to obtain this pill, sadly, it does not exist. Please consult a medical professional for any further questions. But all kidding aside, the quest for such a remedy is unsurprising, as this year is shaping up to be an exhausting and stressful face-off.

As Election Day nears, both candidates will frame the stakes as increasingly dire when drawing a contrast to their opponent. My role as Bernstein's Chief Investment Officer is not to weigh in on the validity of such claims or try to sway your vote. There are plenty of people who will bend your ear on that front—and the decision rests solely with you. Our job at Bernstein is to protect and grow your assets. Yet to responsibly steward your portfolio, we must consider both candidacies, along with the potential Congressional alignment, and what those scenarios would mean for the policies enacted.

What then does that spell for the global economy and for the markets? Before we dive in, let's have a quick look at what's happened so far in 2024, where the markets stand, and what we've learned about the fundamentals.

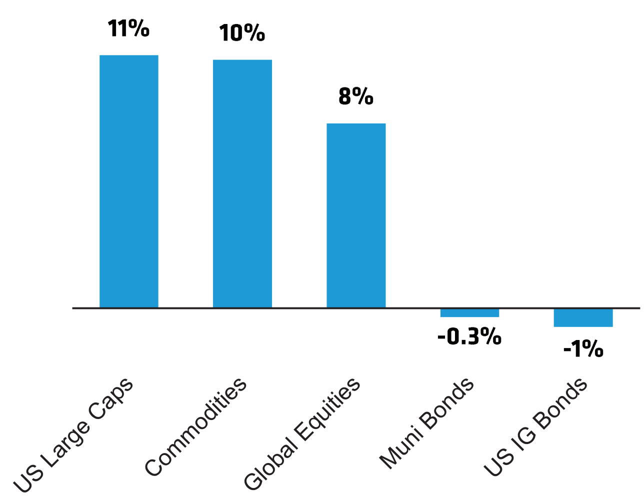
Taking Stock

The markets have largely started off the year on a strong note. Global stocks are up 8%, with US large caps leading the way, delivering an 11% total return to date. Commodities have also been robust performers, up 10% so far this year, with gold notching record highs. The yellow metal's strength is intriguing because there's frankly no good explanation for it. The best two rationales include an expectation of falling real yields as the Fed cuts rates and growing concerns over geopolitical risks. It's certainly not inflation—those expectations have remained firmly anchored while gold has rallied in 2024. That disconnect remains historically consistent. Despite its reputation, gold hasn't typically been tightly correlated with inflation expectations.

Meanwhile, it's been a slower start for fixed income, with municipal bonds flat and taxable investment grade bonds down slightly in the first three months of the year. And, despite many clamoring for a weakening dollar, it's risen by 3% year to date.

YEAR-TO-DATE RETURNS OF MAJOR ASSET CLASSES

(Percent)



As of March 31, 2024.

Past performance does not guarantee future results.

Source: Bloomberg and Bernstein analysis

What's more, we haven't seen many surprises this year. Economic data has come in largely as expected, though it's been slightly stronger than anticipated. That's led economists to raise their consensus GDP estimates for the year, further reducing the risk of recession. On balance, the Fed has done what we expected: nothing. From a market perspective, the two most meaningful moves have been the aforementioned stock surge and a significant change in the market's pricing of rate cuts from the Federal Reserve. The market is now expecting roughly 0.75 percentage points of cuts in 2024 after having entered the year with around 1.5 percentage points priced in.

The labor market continues to hold up, assuaging some of our concerns. Yet we still have our eye on the employment numbers, as the key driver of the US economy's consumer engine. Inflation continues to follow a gradual downward trajectory, though the path isn't linear and has flattened in recent months. The Goldilocks soft landing (our base case) remains intact. But we recognize the relatively high odds of both downside and upside surprises.

According to Bank of America's regular Fund Manager Survey, inflation and hawkish central banks are the biggest tail risk on investors' minds. However, if history is any guide, we could see the US election overtake these concerns in the coming months, as it did in both 2016 and 2020.

The Elephant (or the Donkey) in the Room

Commenting on politics is especially fraught these days, so I want to acknowledge that up front and will proceed as cautiously as possible in these pages. History tells us that it's usually a bad idea to dramatically tilt your portfolio based on elections. First, you can only have so much conviction in the results. More importantly, even if you were armed with advance knowledge of who would win, it's quite possible to position your portfolio diametrically opposite to the market's ultimate reaction. In what I'm sure will not be the last time you hear this example, think back to 2016. Hillary Clinton was generally seen as positive for risk assets like stocks and Donald Trump was seen as a headwind for them. In fact, the market traded that way for months leading up to the election, rising in lockstep with Clinton's odds of winning and falling with Trump's. After the election, those heralded forecasters were once again proven wrong: the market surged and never looked back, for the last 8 years.

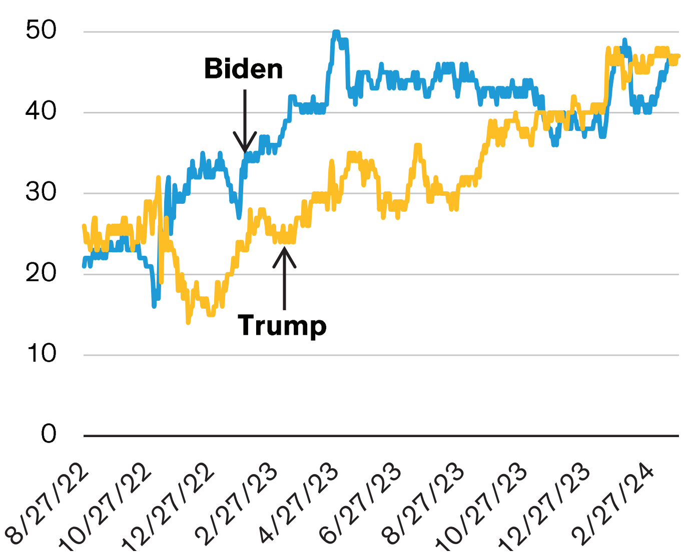
That's one extremely compelling reason we don't allow political views to influence our portfolios. With that said, we can start to think about the ultimate policy impact each candidate might have. This can be somewhat difficult because campaigns are the art of the promise while governing is the art of the politically possible. At this point, it's harder still because the candidates' platforms haven't been finalized. We're left to judge what each has said in the past, what they have or haven't implemented, and what they've highlighted out on the stump.

Let's start with taxes, since we have the greatest clarity both in terms of policy differences and consequences in that area. Biden has proposed raising corporate taxes part of the way back to their 2017 levels; Trump would implicitly leave them at the 21% level set in his 2017 Tax Cuts and Jobs Act (TCJA). When it comes to individual taxpayers, Biden's proposed wish list would disproportionately impact the rich, including a higher top marginal tax rate, a reversion in the exemption to the estate tax, a higher capital gains tax on those earning over $1 million, applying the ordinary income tax rate to carried interest, and a wealth tax on those worth over $100 million. Trump, on the other hand, would largely leave taxes on the wealthy as is and try to make the higher estate tax exemption from the TCJA permanent.

On trade, Trump focused on aggressive tariffs, mainly targeting China, but including many US allies as well. Biden has maintained these tariffs in many cases while imposing additional national security restrictions on China. In a second Trump term, we'd expect more tariff activity across the board as well as other forceful measures to weaken China. From Biden, we foresee ongoing trade restrictions (again aimed at China), along with greater efforts to build coalitions bolstering allies' economies and weakening China's geopolitical position.

PREDICTION MARKETS ARE PUTTING NEAR-EVEN ODDS ON THE ELECTION

Implied Probability



Source: PredictIt and Bernstein analysis

Along similar lines, Biden has implemented policies to onshore or reshore manufacturing in strategically chosen industries such as semiconductors and electric vehicle components. Trump would likely take an even more isolationist approach, though how he would do so remains to be seen.

Infrastructure and industrial policy has been one of the most vivid divides between the candidates—and we'd expect it to remain so. Biden has signed some of the most ambitious industrial policy in decades, with hallmark legislation like the CHIPS Act and Inflation Reduction Act. Trump's infrastructure plans never made it much further than the discussion phase. We could see a Trump infrastructure plan involving fewer direct government subsidies and incentives for industrial expansion in favor of more focus on highways and communications, delivered via public-private partnerships. The price tag that had been tossed around in the past was on the order of $1 to 2 trillion.

The candidates would also have meaningful differences on defense, immigration, healthcare, and energy policy—with potentially significant ramifications—along with differing approaches to Big Tech. These are in the early days of policy formation, but since the election is a frequent topic of client conversations, we wanted to present our latest thoughts.

Issue/Sector	Biden	Trump
Corporate Taxes	Raise corp tax rate from 21% to 28% while increasing min tax for large corporations from 15% to 21%.	Maintain corp tax rate at 21% (per 2017 TCJA).
Individual Taxes	Increase IRS funding for improved enforcement. Top tax rate reverts to 39.6%. Estate tax exemption reverts to pre-2017 levels (~1/2 current level of $13.6 mil.). Cap gains tax at ordinary income rate on those making over $1 mil. Allow SALT deduction limit to expire at the end of 2025, so those taxes revert to being fully deductible. Potential for carried interest to be taxed as ordinary income. Potential wealth tax of 25% on those with wealth exceeding $100 mil.	Keep top tax rate at 37%. Raise SALT cap deduction limit to ~$20K from $10K rather than letting it expire. Make the estate tax exemption increase from TCJA permanent.
Trade	Maintain or reduce existing tariffs. Possibly more national security restrictions on China, especially around tech. Chinese car tariffs TBD. Potentially resurrect Trans-Pacific Partnership or similar formal coalition of Asian countries to counter China.	Higher tariffs on imports in general, especially on China, but also on allies. Aggressive tariffs and forceful measures to counter Chinese auto industry and any North American footprint they establish.
China/Taiwan	Significant support for Taiwan, only question is degree.	Questionable support for Taiwan if China invades. Considers Taiwan a rival to US and a US job taker.
Onshoring	Onshoring or reshoring of key national security, tech, and climate priorities including semiconductors and EV components.	Isolationist approach favoring onshoring/reshoring of wide range of supply chains.
Infrastructure	Expansion of active government industrial policy akin to the CHIPS Act and Inflation Reduction Act to spur private investment in factories and other production facilities.	Incentivize private investment with limited government spending. Emphasis on highways and communications.
Defense	Provide significant financial and material support to Ukrainian forces to prolong defense, deter Russia, and minimize potential lost territory. Encourage Western Europe to contribute their share to NATO. Reduce need for allies or foes to adjust military spending due to lack of confidence in US support.	Pull back US defense commitments in general. Limit or end support for Ukraine, force a deal with Russia involving loss of territory. Ensure Western Europe and other countries ramp up their military spending. Increased incentives for allies and foes to expand military budgets.
Immigration	Boost Border Patrol and ICE budgets while hiring more immigration judges to ease backlog of asylum cases. Increase legal pathways to immigration. Potentially enact policy like the DREAM Act to create path to citizenship for people born and raised in US.	Pledged biggest deportation program in history by rounding up undocumented immigrants and tightening asylum rules.
Healthcare	Negotiate with drug companies to cap prices paid by Medicare.	Potentially reverse Affordable Care Act, as attempted in first term. Recent focus on fentanyl/cartels.
Energy	US oil production likely to continue setting records for most production by any country in history. Further incentives for clean energy. More regulation of fossil fuels.	Reduce fossil fuel regulations. Reverse EV incentives and pace of deployment in the Inflation Reduction Act.
Big Tech	Continued crackdown on investment/acquisition through aggressive antitrust enforcement.	Likely DOJ investigations and Congressional hearings.

You may be wondering why a comparison of the national debt and deficit was not included under each candidate. Partly, that's because it's a net result of the policies already described. But also, there's not much difference between the two sides when it comes to the deficit—Biden, Trump, and the bulk of both parties have embraced deficit spending and few in government are currently incentivized to address the trajectory of the debt. Meanwhile, higher interest rates, the hangover from COVID stimulus program spending, and a slower economy cannot be addressed easily. Our research team is deep at work writing a long-form research piece on both topics. Be on the lookout for that as we roll from spring to summer.

To November and Beyond

It's likely to be a fierce campaign season over the next two quarters. While we might wish we could take that pill to avoid it, we cannot. We're monitoring the potential policy ramifications and not making substantial portfolio changes because of political leanings or evolving poll numbers.

As always, thank you for trusting us as stewards of your capital. We take that responsibility seriously, aiming to multiply your assets steadily over time. Now that spring is here, we hope you take the opportunity to enjoy some fresh air and sunshine. We're all going to need it.

Alex Chaloff
Chief Investment Officer

Alex Chaloff is the Chief Investment Officer and Head of Investment and Wealth Strategies at Bernstein. In this role, he leads a national team of strategists across investments and wealth planning—including asset allocation advice, investment platform oversight, model portfolio construction, new product development, manager research, tax planning and solutions, and estate planning research—while remaining continuously focused on moving our clients forward with strong after-tax risk-adjusted returns. Alex has spent his Bernstein career refining our investment platform, listening to clients, and conducting deep research into investment and wealth planning topics that are critical to achieving clients' goals.

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