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How the 2016 Election Outcome Affects Market Sectors

2016

A LEADER IN VALUES-BASED INVESTING

November 2016 Update

In early October, we published a high-level equity market sector outlook under both a Trump and Clinton presidency. With the 2016 U.S. election now behind us, we have been regularly assessing how our outlook is measuring up, thus far, to the near term market reaction of a surprise Republican sweep of both the White House and Congress (House + Senate).

In general, our thoughts are generally unchanged and our near-term outlook under a Trump victory has been, for the most part, consistent with where the equity market sectors have trended since the morning of November 9th. To briefly summarize our previous note, we believed that two industries with the most binary potential outcomes would likely be Fossil vs. Renewable energy and Healthcare Facilities / Medicaid Managed Care. Additionally, we saw infrastructure companies, gun manufacturers, and Aerospace & Defense likely benefitting the most regardless of the election outcome.

With the Republicans taking control of the White House and Congress on election night, fossil fuel stocks have since outperformed the S&P 500 (even before the bullish OPEC production cut announced Nov. 30th); renewables & Yieldcos have underperformed; and Health Care Facilities & Medicaid levered Managed Care have also underperformed – generally in line with our views under a Trump White House. Additionally, infrastructure stocks and Aerospace & Defense stocks have outperformed, also in line with our original views. Further, we also surmised that gun manufacturers would be short-term winners under Clinton, but longer term sustainability of the industry would benefit under Trump. While the near-term double digit underperformance of Smith & Wesson and Ruger stocks confirms this view, the market reaction seems a bit overdone – we find it difficult to envision likely scenarios where Trump supporters and other Americans drastically reduce gun ownership over the longer term.

Over the next few months as President-Elect Trump and his Republican cohorts unveil more detailed policy plans and cabinet positions, we will continue to assess the implications of this election on the various market sectors with the intention of publishing an in depth outlook by market sector in early 2017.

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The U.S. economy appears unlikely to break out of what many consider a ‘new normal’ of ‘secular stagnation, where economic growth is unimpressive but steady – something we doubt either candidate can fix. While the range of likely stock market outcomes seems wider under a Trump presidency, neither candidate is immune to systemic shocks, nor the natural fluctuations of the business cycle or credit cycle. But all else constant, the next president will inherit a U.S. demographic environment that appears positive for stock market inflows. Approximately 75 million U.S. Millennial’s still need to invest for retirement 30-40 years from now while approximately 74 million retiring Baby Boomers continue a riskier reach for yield via defensive dividend paying equities in the wake of unprecedented low interest rates.

While the feasibility of each candidate’s plan hinges on which party wins a majority in the U.S. House and Senate races, the following sectors have the most at stake during this presidential election:

- *Renewables vs. Coal* – The next presidentially appointed Supreme Court justice could be the swing vote determining the survival of the EPA's Clean Power Plan (CPP), which was stayed by the Supreme Court in February (with the late Justice Scalia included in the majority 5-4 vote). Clinton seems focused on enhancing Obama's pro-renewables policy, while Trump plans to rollback anti-Coal regulations. A Clinton Supreme Court pick would benefit Alternative Energy and Renewable Power, as well as Regulated Utilities with CPP ratebase growth. A Trump victory would benefit Coal producers and coal power generators.

- *Healthcare* – A Clinton victory likely ensures the survivability of ObamaCare, benefitting Healthcare Facilities and Managed Healthcare Medicaid HMO's. However, while Trump has promised to repeal ObamaCare, it is less certain what his alternative is.

Regardless of the election outcome this November, potential sector beneficiaries, in our opinion, include the following:

- *Construction Equipment and E&C Industrials* – Both candidates tout large fiscal spending plans (Trump vows to double Clinton's proposed 5-year, $275 billion infrastructure plan)

- *Gun Manufacturers and Sporting Goods Retailers* – Federal tax receipts from pistol & revolver sales rose 90% year over year in 4Q 2008 after Obama was first elected (we expect a similar 'Obama Effect' should Clinton win, but gun sales have longer term sustainability under pro-NRA Trump)

- *Aerospace & Defense* – Trump is more hawkish than Clinton and Clinton is more hawkish than Obama, but even if the U.S. reduces its global role, other countries will need to fill the U.S. defense spending gap due to continued geopolitical instability (either way, defense spending should rise globally, boosting the sector).

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