



June 13, 2016

Trump v. Clinton

Do Canada and the S&P/TSX care who wins?

All values in Canadian dollars unless otherwise noted.

Priced as of prior trading day's market close, ET (unless otherwise stated).

Key Points

- **Our View:** U.S. Presidents probably get too much credit or too much blame for what goes right or wrong during their time in office. **That said, the S&P/TSX has shown a predilection for blue-coloured presidents over the past 100 years, which we do not chalk up purely to chance.**
- **The S&P/TSX has returned an average of 9.3% during the years in which a Democrat has occupied the White House vs. 1.3% on average when a Republican has had the keys.**
- **There has been an enormous differential in first-year returns under Democratic vs. Republican leadership for the S&P/TSX.** While the data set here is somewhat limited, we do believe that some of this outperformance is potentially the result of higher spending under Democratic administrations filtering through to the economy and the U.S.'s export partners.
- We believe the platforms of both candidates have more puts (negatives) than takes (positives) as it pertains to Canada. However, the likelihood of a divided balance of power makes any overreactions to suggested platforms a buying opportunity in our view.

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Do Canada and the S&P/TSX care who wins the U.S. Presidential election?

Key Points

- Over the past 96 years, there have been 48 years of Republican presidents and 48 years of Democratic presidents. The S&P/TSX has returned 1.3% on average (excluding dividends) during Republican years and 9.3% on average during Democratic years.
- The first-year returns have shown an enormous differential, with an average return of ~25% in first-year Democratic years and a loss of ~10% in first-year Republican years.
- We believe there are three key issues in the platforms of Mr. Trump and Mrs. Clinton that have the potential to impact Canada and the S&P/TSX. These issues are immigration, which we somewhat ironically think would become a net positive for Canada should Mr. Trump win and build his wall, free trade, and the environment.
- There will potentially be two opposing forces at work this November—challenging electoral math for Republicans vs. the tendency for the electorate to eschew “third terms” over the past 50 years.
- Thirty-three years ago, the final episode of *Mash* established the record as the highest-rated television program of all time. We expect this record, which still stands, to be broken in October when Mr. Trump and Mr. Clinton debate for the first time.

With the candidates for this November’s U.S. Presidential election now settled (although someone may need to inform “the Bern” of such), we thought it would be a good time to weigh in on the potential impact this may have on Canada and the S&P/TSX. We admit before we get started that some of this is more art than science, as there is a lot of fancy data we can and will cite; however, we believe that some (and perhaps a large amount) of how the economy and by extension the stock market performs is the result of what took place before the new White House tenant gained access to the big chair.

For example, while it has been popular to assign blame to George W. Bush for much of what plagued the U.S. from 2000 to 2008, he took over for an economy that had generated 23 million jobs in the prior eight years (an unheard of amount) and a stock market that was trading at a very rich price-to-earnings multiple. Was it his fault these things turned sour? Perhaps, but we have our doubts that blame can be solely assigned to one individual, no matter how powerful that individual may be.

Regardless, we do believe the data has an interesting story to tell as far as the S&P/TSX is concerned, and we do not believe all of it is mere coincidence. We will endeavour to explore the upcoming election in three parts: 1) Does it matter from a market perspective who wins? 2) Based on the data, who is more likely to win? 3) What are some of the key issue platforms that may impact Canada and the S&P/TSX?

Does it matter who wins?

If we go back to 1922, we get a nice synergy, as there have been 48 years of Republican presidents and 48 years of Democratic presidents. Let's first look at some data for these years and then comment:

Exhibit 1: Over the past 96 years, there have been an equal number of Democratic and Republican years; however, results have been far from equal

Performance of the S&P/TSX: 1922 to 2016

	Democrat	Republican
Avg TSX Performance	9.3%	1.3%
# of years	48	48
# of positive years	33	26
# of presidents	7	9
Avg. first year performance	25.4%	-10.2%

Note: Returns exclude dividends

Source: Wikipedia, Bloomberg, RBC CM Canadian Equity Strategy

There has been a decided difference in the performance of the S&P/TSX under each party, with Democratic years delivering about 8% more on average than Republican years. Further, positive years have occurred about two-thirds of the time under Democratic presidents and only about half of the time under Republican presidents. In addition, the propensity for outsized losses (10% or more) has been more than twice as common under Republican presidents (11 vs. 5). Lastly, first-year market gains have been significantly larger under Democrats than under Republicans. This last data point is based on only 16 observations, so hardly a robust set; however, we would posit that a Democratic president's propensity for more spending (or at least the perception of such) could be a catalyst of a sort for stocks.

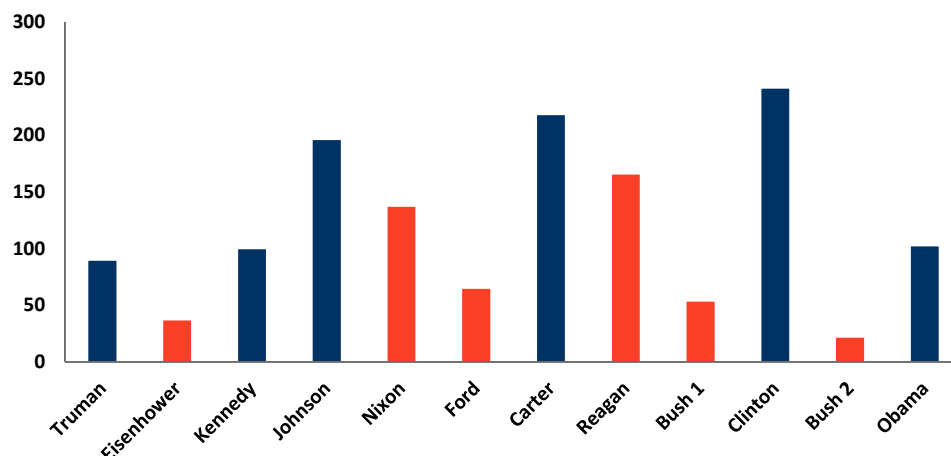
We note that hand-offs matter, and starting with a market that has been on a tear for the better part of 18 years as George W. Bush did in 2001 is a tougher gig than being handed a market that has been going nowhere for 12 years as Ronald Reagan was in 1981. That said, while it would be folly to assign the majority of the credit or blame for a stock market to the sitting president, we note that the average starting S&P 500 price-to-earnings multiple for Democratic presidents has actually been about a multiple point higher than the average starting point for Republican presidents, so the above results (which are similar directionally for the S&P 500) are not solely due to cheap markets being handed to Democrats and expensive ones being handed to Republicans.

Some other interesting data tidbits

Before moving on, we point to a couple of other interesting tidbits that we discovered in our travels through the data. First, while again we acknowledge that hand-offs matter, we thought it would be interesting to look at jobs created by presidency to determine whether or not one party was consistently responsible for more job growth than the other.

Exhibit 2: Job growth has generally been more robust under Democratic presidents

Average jobs created per month based on non-farm payroll data (in 000's)



Blue bars denote Democratic presidents, Red bars denote Republican presidents

Source: Bloomberg, RBC CM Canadian Equity Strategy

Going back to World War II, the average number of jobs created per month under both parties has been 118,000. Under Democratic presidents, this figure rises to 158,000, whereas under Republican presidents, this figure has been 80,000. Similarly, when we look at real GDP growth, there has been an approximately 0.6% difference in growth, with Democratic administrations again coming out ahead.

Exhibit 3: GDP growth has also been higher under Democratic presidents

President	Term	Months in Office	Jobs Created (in 000's)	Jobs/Month (in 000's)	Average Real GDP Growth	President	Term	Months in Office	Jobs Created (in 000's)	Jobs/Month (in 000's)	Average Real GDP Growth
Truman	1945-1952	93	8,368	90	1.4%	Eisenhower	1953-1960	96	3,580	37	3.0%
Kennedy	1961-1963	35	3,511	100	4.4%	Nixon	1969-1974	68	9,373	138	2.8%
Johnson	1963-1968	61	11,991	197	5.3%	Ford	1974-1976	28	1,829	65	2.6%
Carter	1977-1980	48	10,495	219	3.3%	Reagan	1981-1988	96	15,963	166	3.5%
Clinton	1993-2000	96	23,235	242	3.9%	Bush 1	1989-1992	48	2,589	54	2.3%
Obama	2009-2016	88	9,050	103	1.4%	Bush 2	2001-2008	96	2,113	22	2.1%
Average Dems		70	11,108	158	3.3%	Average Reps		72	5,908	80	2.7%

Source: Haver Analytics, Bloomberg, RBC CM Canadian Equity Strategy

Who's more likely to win?

We are not political pundits and thus we will endeavour to answer the question of who's going to win purely through the math of it. While it has been well publicized, we do believe that there is a compelling argument to be made that the math of the U.S. Presidential election has come to favour the Democratic candidate in recent years.

If we go back through the last six elections (1992 to 2012), the Democratic candidate has managed to win the same 18 states plus the District of Columbia in all six instances. These six states, which have been referred to as "the blue wall", account for 242 electoral votes. Considering that only 270 votes are needed to win the White House, cracking this blue wall is nearly a necessary condition for a Republican to win the White House, as they would have to come close to running the electoral table otherwise.

Exhibit 4: The last six elections have established some well-entrenched trends

States won by Democratic candidate (Blue Wall) and Republican candidate (Red Wall) since 1992 election

Blue Wall		Red Wall	
State	Electoral Votes	State	Electoral Votes
California	55	Texas	38
New York	29	Alabama	9
Illinois	20	South Carolina	9
Pennsylvania	20	Oklahoma	7
Michigan	16	Kansas	6
New Jersey	14	Mississippi	6
Washington	12	Utah	6
Massachusetts	11	Nebraska	5
Maryland	10	Idaho	4
Minnesota	10	Alaska	3
Wisconsin	10	North Dakota	3
Connecticut	7	South Dakota	3
Oregon	7	Wyoming	3
Hawaii	4		
Maine	4		
Rhode Island	4		
D.C.	3		
Delaware	3		
Vermont	3		
Total	242		102
% of total needed	90%		38%

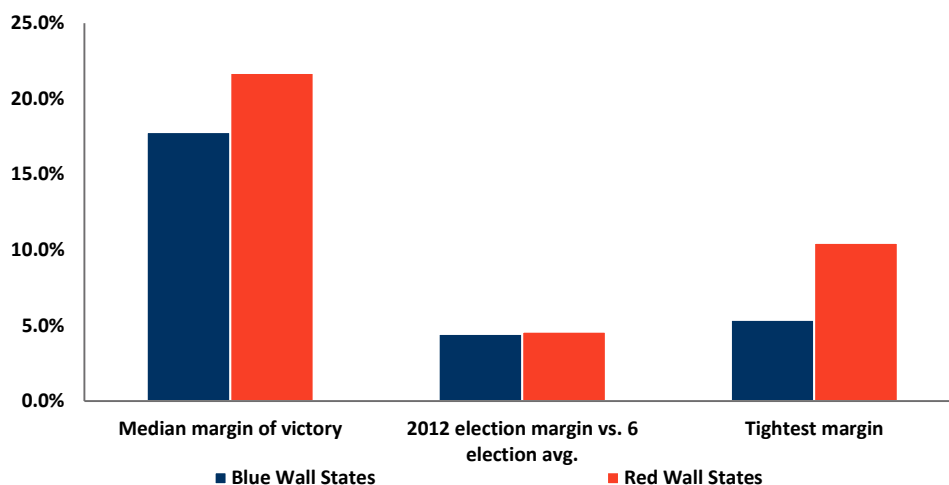
Percentage of total needed based on 270 electoral votes needed to win election

Source: Wikipedia, RBC CM Canadian Equity Strategy

Adding to the challenge is the general trend of the last six elections. Not only have the above states been trending more toward the winning camp (i.e., the margins of victory have been widening), but also none of the above states saw a margin of victory within five percentage points in the most recent election.

Exhibit 5: The margins have been widening and none of the states is particularly close

Results in the 19 Blue Wall states and 13 Red Wall States



Source: Wikipedia, RBC CM Canadian Equity Strategy

Of course, it is not impossible for a Republican to wrest control of the election, as George W. Bush proved in 2000 and 2004; however, our point would be that it's a fairly daunting task based on the math. We note that other trends are not as daunting, with Gallup recently reporting that the percentage of people identifying themselves as either Republican or Republican-leaning exceeded the percentage that answered the same on the Democratic side (47% vs. 46%).

Before we move on, we note that there is a countervailing force to the above—since World War II, there has been reluctance on the part of the U.S. electorate to hand a “third term” to one party or the other. In the roughly 70 years since Franklin Roosevelt and then Harry Truman won five consecutive elections for Democrats, there has been only one instance (i.e., Ronald Reagan/George H.W. Bush) in which one party has been able to string together three consecutive elections.

The Platforms

Obviously, platforms that are presented during campaigns can differ dramatically from those that are put into action once the business of actually governing takes hold. Thus, we would begin this section by suggesting that what we eventually get may be significantly different from what we are presented with now. Further, there is a fair bit in Mr. Trump's and Mrs. Clinton's platforms that is not particularly relevant to Canada, so we will focus on the couple of issues that are relevant. Lastly, we note that anything accomplished would have to be done with some agreement from Congress, which may be challenging in some (or many) instances.

Immigration

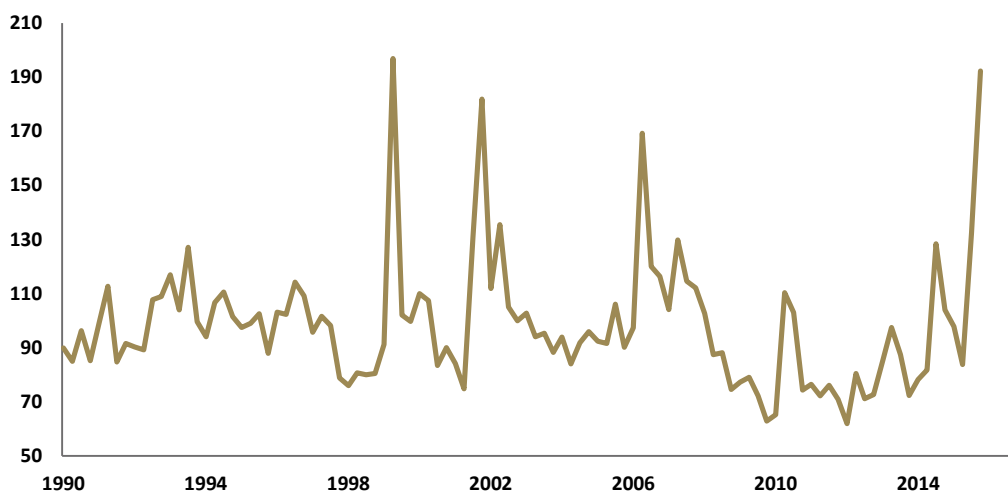
Without stepping too heavily on any third rails, we will begin with Mr. Trump's plan to build a wall and deport millions of people. The irony is that Mr. Trump's platform, were it implemented to its full extent, would potentially be a big positive for Canada. One of RBC Capital Markets U.S. Equity Strategist Jonathan Golub's core theses is that there is a group of businesses that can grow despite an overall tepid growth environment. These “secular growers” have businesses that transcend the ebbs and flows of the economy, generating profit growth, while other businesses more tied to the economy struggle. These types of businesses tend to proliferate in the Technology and Health Care sectors, two areas of the

market in which the S&P/TSX has limited representation (the combined weight of both sectors is below 5% of the index).

However, immigration provides a potential outlet, albeit longer-term, for leveling this playing field. Canada currently has net immigration per 1,000 people of 5.66, which is significantly higher than that of the U.S., which sits at 3.86 per 1,000 (Source: CIA World Factbook). Canada also has fairly rigorous immigration selection criteria that tend to push Canadian immigrants toward higher education levels than the general population, a trend that tends to be imbued in the children of immigrants, who also have higher education levels on average than the general population. In places such as Waterloo, Ontario, we have already begun to see some of the benefits of these policies, as technology giants such as Google and Apple have established significant presences. Were the “Trump plan” to be implemented, we believe Canada could stand to subsume some of the benefits.

Exhibit 6: U.S. immigration fears nearing their highest level on record

Index based on counts of newspaper articles (both print and on-line) relating to economic uncertainty and immigration



Source: Haver Analytics, PolicyUncertainty.com

Free Trade

Both candidates for president have talked to varying degrees about potentially revisiting the issue of free trade (although one candidate may have done it slightly more noisily than the other). Neither candidate has specifically mentioned Canada by name, but any barriers put up to trade (again with Congress’s consent, which may be very difficult to gain) could potentially be negative for Canada (not to mention global growth).

The Environment

The two candidates are diametrically opposed on the environment, with Mrs. Clinton looking to greatly expand the use of alternative energy and reduce the use of fossil fuels while Mr. Trump has made statements suggesting that he feels the opposite. While Mrs. Clinton does not specifically mention Canada and the oil sands in her platform, she has made statements that suggest she would stand in the way of the Keystone XL pipeline whereas Mr. Trump has indicated that he would approve XL.

Conclusion

The S&P/TSX has shown a predilection for Democratic presidents over the past 96 years, returning about 8% more per annum before dividends during years in which a Democrat has



occupied the White House. While presidents probably get too much credit or too much blame for what goes right or wrong with the economy and the stock market, we believe that the consistency of the data and the fact that starting valuations on average have been relatively similar for Democratic and Republican presidents suggest that this is not entirely due to chance.

Based on the electoral math of the last six elections, Democratic candidates would appear to have the upper hand heading into November; however, this is mitigated by the tendency of the U.S. electorate over the last approximately 70 years to eschew “third terms” for either party.

The key election platforms for Canada in our view are immigration, trade, and the environment. From an immigration perspective, a Trump presidency could potentially be a long-term positive for Canada as it continues to enrich its economy with well-educated immigrants and their families. Both candidates have indicated that they would look to restrict free trade to some degree, which could be negative not only for Canada and the S&P/TSX but also for the global economy. Lastly, the candidates appear diametrically opposed on the environment, with a Trump presidency potentially proving positive for Canadian energy and the oil sands whereas the opposite may be the case under a Clinton administration. We caution that the rhetoric of elections often gives way to the reality of governing. Further, the balance of power and the ability of Congress to stand in the way of the president’s agenda should not be underestimated, and thus what you read in the coming months or witness on television is likely to differ greatly from the reality of the next four years.



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