CUMBERLAND

ELECTION CHEAT SHEET

With the upcoming U.S. election next week, we thought a cheat sheet would provide a summary of our thoughts and the potential investment implications. This note includes the following points:

1. Six potential outcomes
2. Brief summary of each candidate's victory
3. Our strategy

Six Potential Outcomes

	President	Congress
1.	Clinton	Republican Congress (Fiscal paralysis – more of the same)
2.	Clinton	Split Congress (Bipartisan compromises likely – Clinton Lite)
3.	Clinton	Democrat Congress (Full blown social agenda)
4.	Trump	Republican Congress (Lacks support for his plan)
5.	Trump	Split Congress (Lacks support for his plan)
6.	Trump	Revises plan (Majority of Republicans opposed to financing tax cuts with debt)

The likely pattern for the economy, interest rates and the market will be influenced by the outcome of both the Presidency and the composition of Congress.

Implications of Different Victories

Trump victory:

- A more isolated US economy with potential decline in cross-border trade, immigration and foreign investment
- Reduction in tax rate for the wealthy and corporations
- Eliminate the inheritance tax
- Substantially increase public debt
- Interest rates – expect a drop in the short term as his election would put the Federal Reserve on hold. If the plan is executed, the deficit spending would eventually cause an abrupt rise in both short and long term rates, threatening a recession. Moody's estimates his plan would raise 10 year interest rates by 200 bps in the first year and 460 bps in the second year
- A sharp increase in duties on China and Mexico would increase inflation

Clinton victory:

- Foreign trade policy would look very much like Obama's
- Plans to increase taxes on the wealthiest
- Would cut corporate taxes on small business but raise taxes on large corporations that relocate
- Raise the inheritance tax
- Neutral on public funding
- Would increase government spending on infrastructure and low-income households to boost the economy. Moody's estimates Clinton's plan would help the economy by 1.7% by 2020

Summary

A Trump victory would most certainly result in greater uncertainty and a sharp, Brexit type market reaction. Realistically, he would likely get selective tax cuts for the middle class and be able to win approval of only some infrastructure spending (i.e. Trump Lite). With Trump Lite, the country would avoid a recession and an interest rate hike would likely be postponed until sometime in 2017 rather than in December of this year. Long term rates would continue slightly higher and the US dollar would show some appreciation, especially against the Mexican peso and Canadian dollar. European markets would also weaken on global growth fears.

Should Trump's plan not be compromised, it is likely the US faces a recession by 2018. The deficit would expand by $5.3 trillion, global trade would be damaged, inflation would accelerate and monetary policy would have to again consider easing with a possible QE 4 to offset the economy and broadly higher interest rates due to the deficit and inflation. Global markets would decline on protectionist fears and the prospects of lower growth.

The Healthcare sector would recover and infrastructure and defense spending companies would do well. However, purely domestic companies would probably fare better than global companies.

A Clinton victory is more of the same. She would likely get some tax cuts for the middle class and pass an infrastructure spending bill. She might also push through an increase in the minimum wage. Overall, it would result in a re-acceleration of GDP growth in 2018 and allow the Federal Reserve to continue with their rate normalization policy.

If the Democrats win control of both Chambers of Congress, it will accelerate both the economic growth rate and require higher interest rates.

However, with a more balanced budget the impact on treasury rates would be less than in Trump's plan. We'd expect a modestly positive market reaction to a Clinton victory especially if there is a divided Congress as there would be greater grounds for compromise. Should Congress swing Democratic, there could be a modest negative market reaction but the markets would likely return to a view of "business as usual".

Notes

1. The President's power on budget matters is very limited as it is a Congressional issue.
2. Any combination of Congress is unlikely to approve a substantial increase in public debt.
3. Clinton's minimum wage proposal would raise hourly rates to $12/hour versus $7.25 at the federal level. She proposes paternity leave and facilitated sick leave to be funded by tax revenues. She also endorses free tuition for low-income and middle class students in public colleges.
4. Trump proposes tariffs of 35% on Mexico, 45% on China and 10% on the rest of the world which would increase prices on imported merchandise by about 15%.
5. Clinton wants to reduce regulations on immigration while Trump would expel 11.3 million undocumented immigrants which account for 3.5% of the US population and 5.1% of the active population.

Our Strategy

From our perspective, it is difficult to hedge our investments against the various potential outcomes.

We could use portfolio insurance but that would not be cheap. Otherwise the only option that is reasonable is to raise more cash.

However, the market has been selling off given the election uncertainty and various sectors that would be hurt by either candidates' victory have been under pressure. So, it appears the market has "priced in" some of the worst case, irrespective of the candidate.

We have reviewed all of our investments in regards to their specific risk to the election and we're comfortable with their fundamentals.

Given the most likely case of a Clinton victory, we believe there are some attractive groups such as Healthcare that are discounting the worst case scenario of potential policies.

In the event of a Trump win, the best defense would be a higher weighting in cash. But as we've just suggested, such an outcome would likely result in a sharp but short negative market reaction. There would then likely be a period of uncertainly until the inauguration during which Trump will roll out his First 100 Day Plan. During this period we will have a better opportunity to adjust our portfolios and get a better measure of what is possible versus his campaign promises.

Regardless of who wins the election, uncertainty will be lifted and investors can focus on one candidate's plan and the likelihood of its success. And having one less unknown variable will be positive for the market.

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