

October 21, 2016

Dear clients and colleagues,

In 1980, a few weeks before his failed bid for a second term as president, Jimmy Carter was leading in election polls by 8% when, surprisingly, Ronald Reagan won the debate and the ensuing election by over 10%. Following the final debate of the 2016 US election, the Democrats hold a 5% lead in the polls, but as history shows, large swings can happen quickly, so we shouldn't count our chickens before they hatch.

When there's a change of political party in the White House, history indicates there will be increased volatility in the markets just prior to and post the election period. However, history also shows that the S&P 500 has risen an average of 6.5% in the first year of a presidential term, regardless of whether the new president is a Democrat or Republican. During the election year itself, highly regulated industries such as financials and utilities seem to perform best. This is not surprising since during an election year the sitting government is unable to pass many new regulations. In the year after an election year, consumer discretionary, IT, industrials, energy and health care tend to perform well as the market recovers from the uncertainty of which party will be in power. Sector performance in the years immediately following a US election is noted in the table below.

Sector performance in election cycle

	ELECTION YEAR	ELECTION YEAR + 1	ELECTION YEAR + 2	ELECTION YEAR + 3
Financials	8.8%	15.7%	4.5%	8.1%
Utilities	6.2%	3.7%	0.3%	12.8%
Consumer staples	6.1%	8.5%	8.3%	10.2%
Energy	4.6%	13.9%	2.4%	19.9%
Health care	4.5%	13.1%	10.4%	14.3%
Industrials	3.5%	14.9%	3.2%	18.5%
Consumer discretionary	1.1%	19.9%	9.4%	13.7%
Materials	-3.5%	14.7%	4.7%	16.7%
Information technology	-4.3%	18.3%	15.7%	36.1%
Telecommunications	-6.0%	5.7%	7.9%	13.5%

Source: Strategas Research Partners under S&P 500 data from 1/1/1992 through 12/31/2014. Past performance is no guarantee of future results.

Sector performance: Clinton v. Trump win

	CLINTON WIN	TRUMP WIN
Financials		✓
Utilities		✓
Consumer staples	✓	
Energy	—	—
Health care		✓
Industrials	✓	
Consumer discretionary	✓	
Materials	—	—
Information technology	✓	
Telecommunications	✓	

As for the impact, the two candidates will have on the various market sectors, health care and financials should benefit under Trump as these are generally regarded as the most regulated industries. Consumer discretionary, staples, industrials and information technologies should benefit under Clinton as she is more progressive on international trade and employment. Both parties plan aggressive infrastructure spending.

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Energy and health care are the sectors where the candidates differ greatly and where their policies are likely to have an impact.

In terms of energy, Donald Trump favours more traditional energy sources and advocates a rescinding of the Climate Action Plan and the Waters of the US rule, which would effectively allow drilling for oil and other fossil fuels in currently protected areas. He has also promised to invest heavily in the coal industry. In contrast, Clinton has pledged to expand investment in renewable energy, proposing that over half a billion solar panels be installed by the end of her first term, a nearly 700% increase in solar capacity by 2020.

For health care, Clinton is proposing to increase the Affordable Care Act (ACA), also known colloquially as Obamacare, promising to reduce out-of-pocket cost (deductibles) for citizens. Trump, however, has promised to repeal the ACA, proposing state-level Medicaid for citizens instead. Both parties agree that the rising cost of drugs is an issue and have promised to fight to keep drug costs down. Clinton will legislate to keep drug cost down while Trump says he will negotiate aggressively with drug companies and remove barriers to entry for generic, non-patent alternative products.

Global Alpha portfolios should benefit from a Clinton victory. Two important growth strategies we look for in companies are product innovation and geographical expansion. These strategies benefit from free market economies and limited protectionism between countries. Examples such as Tomra, which sells material collection and sorting solutions through 43 sites and 60 distributors globally, and Gentherm, an automotive specialty company with 11 production sites across the globe.

As discussed, Democrats are more inclined to favour renewable energy sources, and the environment figures as one of Global Alpha's five key secular themes. We hold Ormat Technologies, a global leader in geothermal energy; Atlantic Tele-Network, a diversified operator of telecomm and renewable energy assets; and Solaredge, a leading technology provider to the solar industry.

Tighter regulations also drive another important Global Alpha theme: outsourcing. Companies benefitting from outsourcing trends include ACI Worldwide, which delivers electronic banking and payment solutions to more than 5,000 financial institutions, and Nice Systems, an enterprise software company focused on operational risks that has 150 offices worldwide.

In the event of a Trump victory, we will certainly follow any policy that could cause structural changes to markets in which our portfolio companies operate. We should have sufficient time to react, because as we all know, there is a long time lag between campaign promises and political execution.

Have a good weekend.

The Global Alpha Team

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