

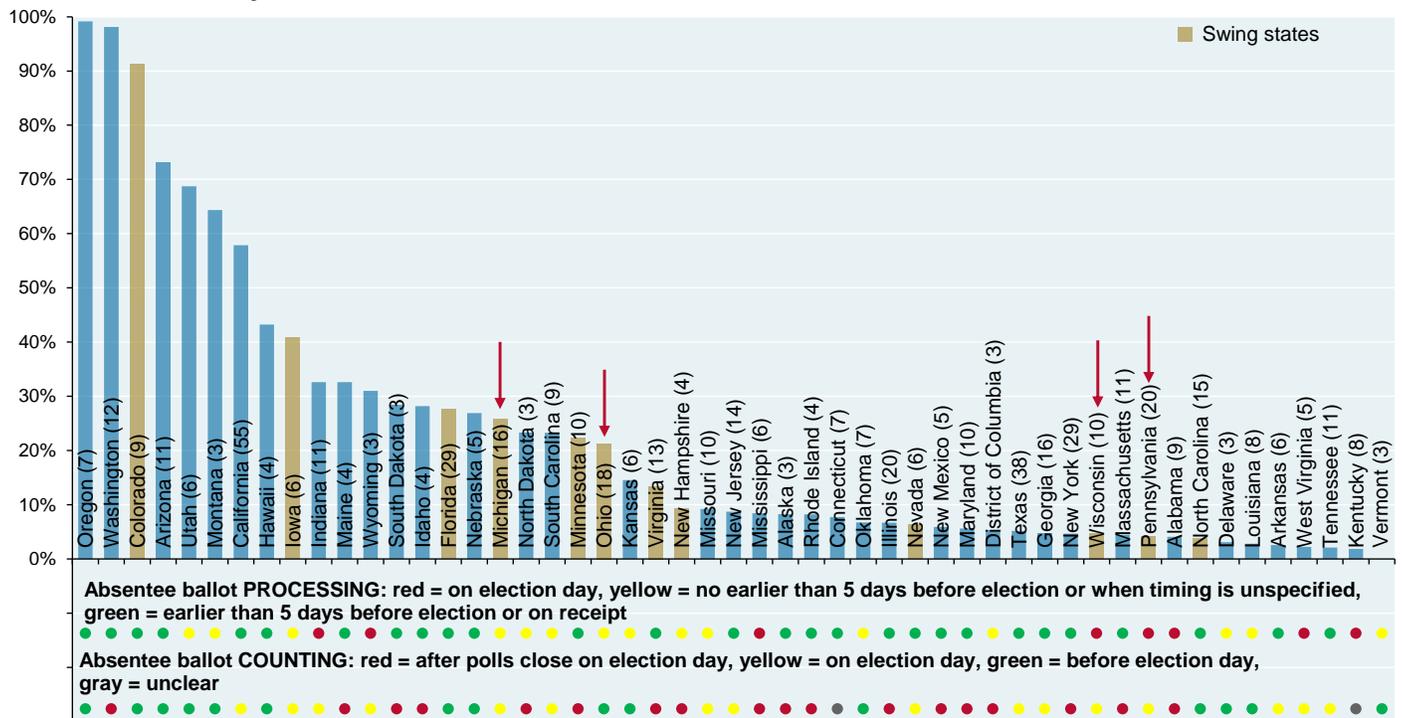


Buckle Up: States that do not allow pre-election processing of absentee ballots; COVID Rorschach test; Trump and Biden deficit explosions and equity market impacts; Vaccine timing & the economy

If Biden were to win Florida and Texas, a winner could be announced on election night. But if Trump wins these states and it comes down to Midwestern swing states, it could be a while before a winner is known. The reason: **Pennsylvania and Wisconsin share the unholy trinity** of (a) inexperience with large amounts of absentee ballots; (b) no pre-election processing of absentee ballots; and (c) being swing states with a large number of electoral votes at stake. The chart incorporates all of these factors, with potential problem states marked with red arrows. It’s worth noting that many states *changed* election rules this year to allow for earlier pre-election processing¹; to date, over 5.6 million absentee ballots have been submitted nationally, compared to just 75,000 by this point in 2016. However, Republican-controlled legislatures in Wisconsin and Pennsylvania opted not to change the rules. Also: while Michigan changed its rules last week, the state now allows absentee ballot processing to only begin on the day before the election, which feels like window-dressing to me.

Tracking potential electoral delays by state

Absentee and mail-in voting % of total voter turnout in 2016, with the number of state electoral votes



Source: US Election Assistance Commission, National Conference of State Legislatures, JPMAM. October 2020.

Why is processing of absentee ballots so time-consuming? Steps involved may include: ensuring that ballot ward numbers match polling places they were delivered to; ensuring no envelope tampering; checking for voter and witness signatures and addresses; ensuring voters are not on the ineligible list; ensuring that the voter is in the “poll book”, has not voted yet and in a fashion that can be heard aloud by observers (who can then file challenges); matching voter signatures; checking for Clerk initials placed on absentee ballots before they’re mailed out; checking for random markings, the wrong colored pens, over- or under-voting and other irregularities which are then placed in a separate pile to be evaluated, with the possibility of a replacement ballot filled out by election officials if the voter’s intention is clear; and feeding the ballot into a tabulator to double-check some or all of the above. Obviously, absentee ballot processing can vary greatly by state.

¹ 11 state legislatures changed rules to allow processing of absentee ballots before election day, or to allow even earlier ballot processing: AL, CT, IA, ME, MD, MI, MN, NH, NY, RI and SC.



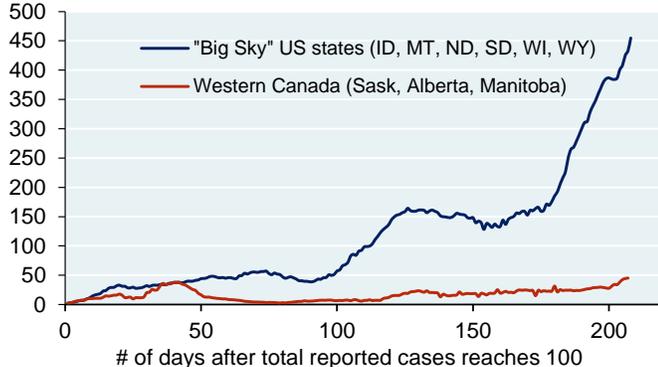
Big Sky Country: a COVID Rorschach test

The first chart below shows COVID infection rates for US “Big Sky” states compared to infection rates for the three Western Canadian provinces directly adjacent to them. Big Sky state and Canadian province population densities are similar, generally ranging from 2.5-5.0 people per square kilometer, and both are testing at roughly the same rate. In the right setting, it’s an interesting exercise to ask people to complete this sentence...

“I believe this is happening because _____”.

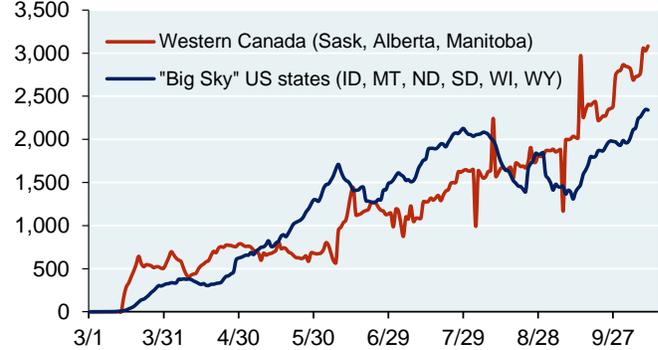
...and compare/discuss the results. Just be prepared to hear some things you might not agree with.

What a difference a border makes
New daily infections per mm people, 7 day avg



Source: Johns Hopkins University, IMF, JPMAM. October 11, 2020

Testing: Western Canada vs "Big Sky" US states
New daily tests per mm people, 7 day avg



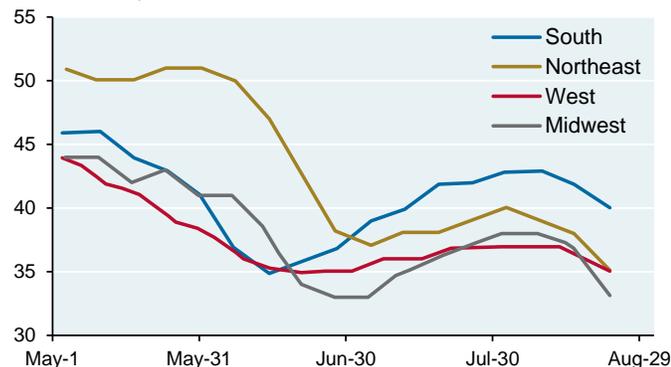
Source: JHU, Census Bureau, Statistics Canada, Esri Canada, JPMAM. October 11, 2020.

As a reminder, we’re still maintaining our COVID web portal (link above), which contains daily/weekly tracking of economic activity and the virus itself. The portal includes an extensive compilation of charts on infection, mortality, hospitalization, testing rates and hospital utilization rates. Some charts in the “What’s New” section:

- While Northeastern US (NY, NJ, MA, CT) infection rates are nowhere near March levels, it is notable that they’re roughly double the level seen over the summer
- With the exception of Italy, the spike in infections in Western Europe now surpasses levels experienced in the Spring; however mortality outcomes are much lower, a trend now seen in much of the Developed World
- Singapore finally has the virus under control and has minimal infections like the rest of Developed Asia
- With the exception of Argentina, Latin American infections are now rolling over from very high levels

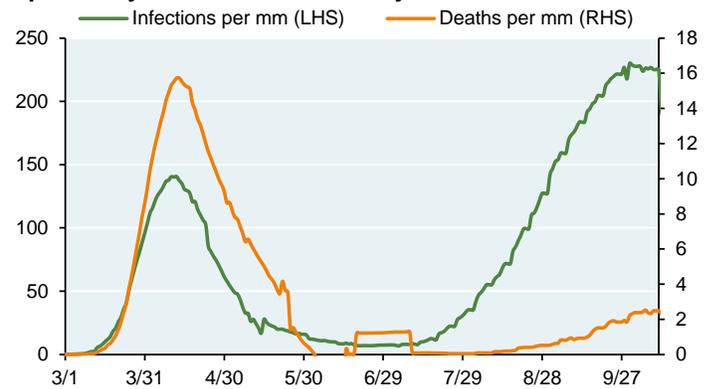
The big question: what time lags are required to assess the degree to which rising infections in young people (who make up a larger component of recent infections; see below, left) translate into rising infections and mortality in older people? In Spain, it’s already happening, albeit at a fraction of spring mortality levels.

Median age of individuals with positive SARS-CoV-2 PCR test results, Years



Source: CDC. October 2020.

Spain daily infections vs mortality



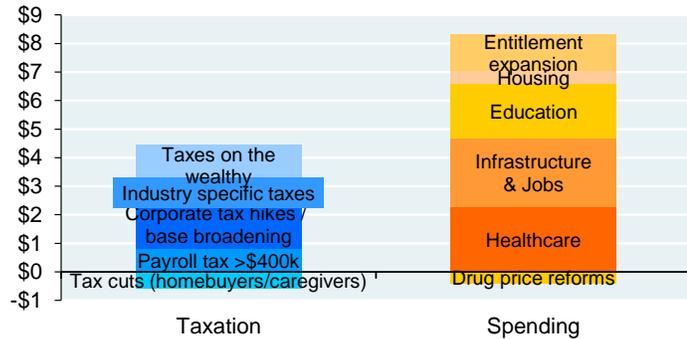
Source: JHU, JPMAM. 10/11/2020. 20 day averages.



Trump vs Biden spending and deficit comparisons, and the impact on equity markets

The Biden Agenda

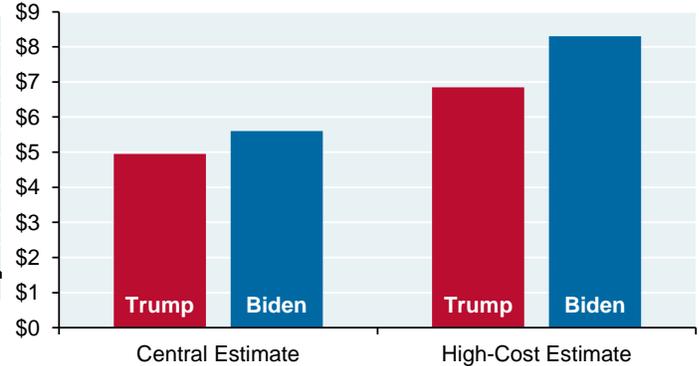
\$, trillions over 10 years



Source: Cornerstone, Tax Policy Center, Tax Foundation, University of Pennsylvania, JPMAM. October 2020.

Deficit impact of Trump and Biden agendas

\$, trillions over 10 years



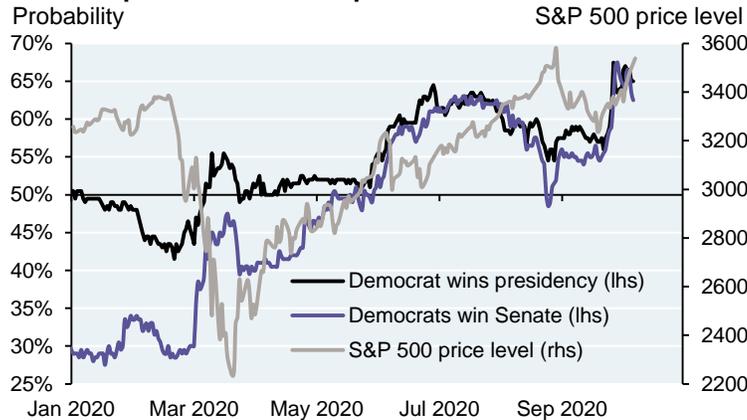
Source: Committee for a Responsible Federal Budget. October 2020.

In recent *Eye on the Market* notes, we have included the chart above (left) showing Biden’s taxation and spending agenda, and how these proposals would result in a large gap between the two. The implication is that Biden’s agenda would involve a *lot* of stimulus for the US economy, and also add a *lot* more to the US Federal debt by the end of the decade. Given rising market-implied probabilities of a Democratic Sweep, this is where we have been focusing.

However, estimates we’ve seen of another Trump term involve similar amounts of net spending and debt increase². Look at the second chart: the deficit impacts of both candidate plans are not that different. The Trump administration plan calls for lowering taxes, strengthening the military, increased infrastructure spending, more spending on veterans and space travel, lower drug prices, more school and health care choice and reducing spending on immigrants. Given the perceived likelihood of Democrats retaining the House, it’s not clear how much of a second term Trump agenda would ever get passed. But on paper, both candidates appear committed to keeping the fiscal stimulus tap flowing, irrespective of long term impacts on growth, taxes and interest rates. **For now, this has been well received by equity markets given limited near-term risks of inflation, and the perceived willingness of the Federal Reserve to keep a lid on rates if debt markets revolt.**

Rising Democratic Sweep odds have not derailed the S&P 500 rise; if anything, a brief *decline* in such Sweep odds in early September actually coincided with a minor setback in the equity market’s advance.

Election prediction market probabilities vs S&P 500



Source: PredictIt, Bloomberg, JPMAM. October 11, 2020.

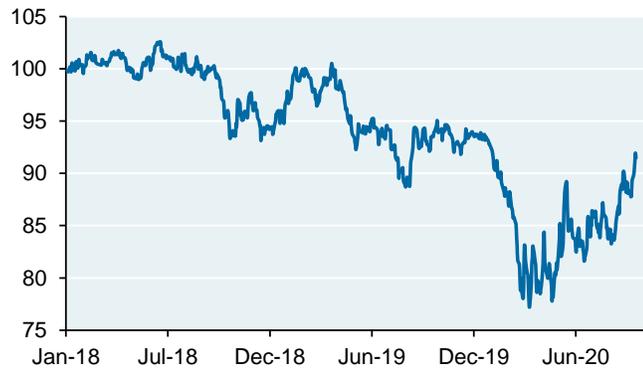
² “The Cost of the Trump and Biden Campaign Plans”, Committee for a Responsible Federal Budget. 10/7/2020



A few more election-related equity market observations:

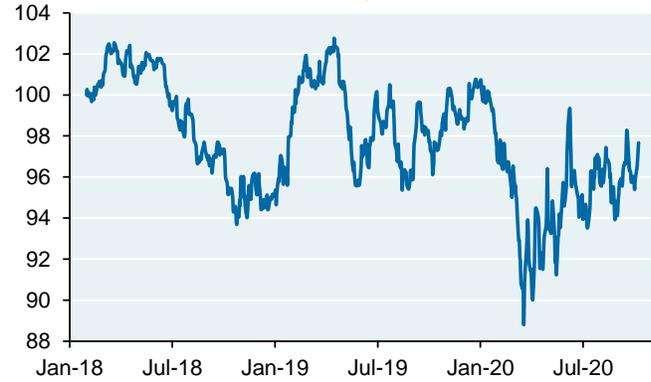
- As Biden’s election prospects and Democratic Sweep projections rise, markets appear to be pricing in a **faster resumption in global trade and lower trade tensions with China**, benefitting stocks with exposure to both factors (first two charts)
- Markets are also pricing in **some headwinds for mega-cap tech and social media stocks** relative to the rest of the market. One way to see this: the market cap-weighted S&P 500 has finally stopped outperforming the equal-weighted S&P 500 (third chart). Reasons could include greater antitrust scrutiny from a Biden administration, as well as the beneficial impact of Biden’s spending plans on the broad economy
- For those concerned that higher capital gains tax rates could result in a market selloff as investors take advantage of existing lower rates, there is **little evidence of this occurring** in 1986 or 2012 (fourth chart)

Relative performance of companies with high exposure to US-China trade war vs S&P 500, Jan 2018 = 100



Source: Barclays Research, Bloomberg, JPMAM. October 09, 2020.

Relative performance of companies with high exposure to international sales vs S&P 500, Jan 2018 = 100



Source: Barclays Research, Bloomberg, JPMAM. October 09, 2020.

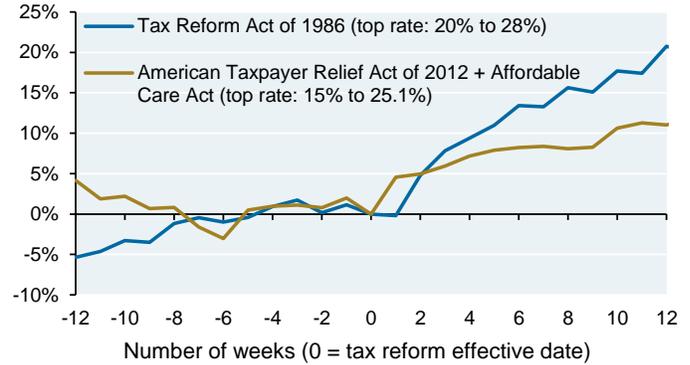
S&P 500 megacap outperformance

Outperformance of market cap vs equal weighted S&P 500, %



Source: Bloomberg. October 12, 2020.

S&P 500 return relative to effective date of capital gains tax hikes, % change in S&P price level from date of tax reform



Source: Bloomberg. 2020.

Past performance is no guarantee of actual results. It is not possible to invest directly in an index.



Vaccine timing and virus-sensitive businesses

A lot of clients have asked about vaccine timing. I can understand why; while large public companies have benefitted from Federal Reserve programs to lower the cost of credit and increase its availability³, small and mid-sized businesses (particularly “virus-sensitive” ones) are suffering from tighter credit conditions. The Paycheck Protection Program helped smaller companies⁴, and many built up cash buffers. However, roughly 70% of respondents to Census, Verizon and Goldman surveys indicated that they could survive 3-6 months before experiencing more severe cash flow shortfalls. Furthermore, the Fed’s Main Street Lending Program (MSLP) has seen limited participation. So, vaccine timing is of critical importance for virus-sensitive businesses given its potential for normalizing consumer behaviors to pre-COVID levels. A few comments:

- **A vaccine is not a foregone conclusion.** Many vaccine candidates rely on approaches that haven’t been approved before in developed countries. Immunogenicity results from Phase I studies (general antibody responses) were promising, but that’s different from Phase III results on efficacy and long-lasting immunity. Yesterday, J&J paused its vector vaccine trial due to an unexplained illness, just weeks after AstraZeneca did the same (resumed in the UK, still paused in the US). My view: “**superforecaster**” predictions on vaccine timing are useless and a waste of space; and the most likely vaccine candidates to be approved may be simpler ones involving production of coronavirus proteins, rather than vector vaccines or mRNA vaccines. See Section 4 on our web portal for more details.
- **Some vaccines may be approved with only 50%-60% efficacy**, without plans to determine ex-post if inoculated persons are in fact immune by checking their actual antibody responses
- **The US ranks in the bottom of the third quartile globally with respect to trust in and use of vaccines.** In addition, a USA Today poll found that only 27% of respondents would choose to get the COVID vaccine as soon as it’s available; 44% would wait a while until others take it; and the remainder wouldn’t get it at all. If you are part of the cohort upon whom the vaccine doesn’t work, your chances of getting the disease are higher if overall adoption rates are low
- Since most vaccine companies received funding from Operation Warp Speed, **the US government will own and distribute initial supplies.** Given limited supplies upfront, initial vaccine distribution will likely be determined based on the CDC’s Advisory Committee on Immunization Practices prioritization (obviously, there’s some overlap in these categories):
 1. 20 million healthcare workers
 2. 60 million essential service workers (food and & agriculture, transportation, education, energy, water/wastewater and law enforcement)
 3. 100 million individuals with “high risks” other than age (obesity, diabetes, chronic obstructive pulmonary disease (COPD), heart conditions, chronic kidney disease)
 4. 50 million people over age 65
 5. Then, the remaining general population

My best guess is that if a vaccine is approved by year-end, the US would treat healthcare and other essential service workers in Q1 2021, and that most remaining populations would be inoculated in Q3 2021. While markets are likely to price in approved vaccine benefits upfront, the *actual* benefits in terms of economic activity and consumer behavior may not occur until true herd immunity is reached (i.e., antibody prevalence resulting from both disease survivors and vaccinated individuals).

³ Examples: The Fed’s Primary and Secondary Corporate Credit Facilities. Investment grade and high yield bond issuance has surged since both programs were announced, driving credit spreads 80% - 90% of the way back to pre-COVID levels.

⁴ A study of 6,000 small businesses found that PPP loans led to a 14-30% increase in expected survival and had a positive (though imprecise) effect on employment. Source: “*The Targeting and Impact of Paycheck Protection Program Loans to Small Businesses*,” Bartik et al, National Bureau of Economic Research. July 2020.



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