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Last Week's S&P 500 Index: +0.2%

Immediate gratification

Key takeaways

- The stock market doesn't appear to be concerned about the potential for higher taxes and more regulation should former Vice President Biden win the election.
- Investors appear to be more focused on the near term possibility that a large stimulus package will get through Congress no matter who is elected President.

The S&P 500 has largely been on an upward trend in recent months, notching new record highs in early September, with only a few pullbacks along the way. With the election less than two weeks away and former Vice President Joe Biden ahead in most of the polls, many investors are wondering how this equity uptrend can still be intact given the proposed tax and regulation changes his potential administration would attempt to enact. Increased taxes for corporations and upper-income individuals as well as more regulation for certain industries like energy are part of this candidate's stated plans should he win the presidency and be able to get Congress to agree and pass legislation. Many pundits would argue that higher taxes and more regulation are negatives for the economy and stock market. So what gives?

We have argued for quite some time the equity market was assuming that additional positive medical news (vaccines and treatments) were likely in the nearer term, the Federal Reserve (Fed) would keep interest rates very low for an extended period of time, and Congress would provide large amounts of fiscal stimulus to the economy. So far, so good as promising medical news continues and Fed Chair Jay Powell has reinforced the message that low rates are here to stay for the foreseeable future. Congress has also provided a large amount of fiscal stimulus. We continue to believe that positive medical developments will continue and Congress will approve additional stimulus, but the ultimate timing of either is uncertain.

As far as additional stimulus is concerned, the administration has so far proposed dollar amounts that have been well below that sought by House Democrats (\$1.8 trillion vs. \$3+ trillion).¹ In either case, the amounts discussed and proposed are huge. Equity markets are coming to grips with the prospects that the magnitude of stimulus is likely going to be significant whether we continue with divided government or we have a new president and a single-party sweep. That is a major key to understanding why the stock market has continued to hover largely within a few percentage points of record levels despite the fact that Vice President Biden is leading in the polls even though he is proposing to hike taxes and increase regulation.

At least for the time being, the stock market is seeking immediate gratification in the form of a very large stimulus package and not paying much attention to how higher taxes and more regulation might impact the economy or longer-term issues like rising government debt. That will likely continue to be the case in the nearer term.

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¹ Bloomberg, October 20, 2020.

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