

Jumping the Blue Wall?

The U.S. presidential election campaign will end on Tuesday, November 8th. We will not try to call the results of the election, but we think it is important to review the hurdles that Mr. Trump would have to overcome. The election of the president and vice president is more complicated than a simple majority. It is the Electoral College and its electors who select these two positions. The number of electors representing each state is based on population. More people equals more electoral votes. All of a state's electoral votes go to the winner of the popular vote in that region. As an example, if Ms. Clinton receives more of the popular vote in California than Mr. Trump, then all 55 of the electoral votes representing California will be voted in favour of Ms. Clinton. To become president, the candidate must receive a majority, or 270, of the electoral votes.

The "Blue Wall" is a description of the states that have voted for a Democratic candidate over the last six elections. The key states that make up the Blue Wall are California and New York, which have 84 electoral votes combined. The other Blue Wall states have close to 240 Electoral College votes. The only large state that has voted Republican for the past six elections is Texas, which has 38 electoral votes. The battleground states are the ones that are close in terms of their popular vote. When these states are analyzed, a Trump presidency is possible, but he would have to win a majority in those states. While definitely possible, it will be difficult to jump clear of the Blue Wall.

The clear message to us is that volatility will persist. Volatility in the capital markets has picked up since the FBI reported a new angle on "Emailgate". The question remains, what actions will take place after a Clinton victory versus a Trump victory? Will Trump rip up NAFTA, which he claims is the worst trade deal the U.S. has ever signed? Will Clinton spend wildly on infrastructure, while keeping her promise to not raise taxes for the "middle class"? We think the main point worth considering is that the president cannot unilaterally implement policy changes at will. President Obama has had difficulty moving bills through the House of Representatives due

to the Republican majority. It will be unlikely that one party will control both chambers of Congress, according to projections. This will ensure that campaign proposals will have some sober second thought before they are carried out. Volatility makes markets nervous, but this volatility can create opportunities. We will use any market declines to add to current positions or to introduce new companies from our watch list. Long-term investors can use this volatility to their advantage.

"Magna Surges on Demand Spike"¹

...but the stock was down 2.2% on the day. In reading the above headline, most would have guessed the stock was up maybe 10% or more. Isn't that what "surges" means? This is what makes quarterly earnings season difficult to interpret. If you happen to glance through the newspapers, reading headlines like the one above may give the wrong impression. Highly regarded analysts set their earnings estimates each quarter based on their model projections and commentary from management. When a company reports earnings, it is indicated whether the company "beat" or "missed" analyst consensus estimates. Let us give an example. Let's say a company earned \$3.50 per share last year. This year, management suggested earnings would grow to between \$4.60 and \$5.00 per share. The reported earnings came out and they earned \$4.55 per share. Some analyst reports would sound negative in that the earnings "missed" expectations and the company's stock price might sell down as a result. We might still be happy with the "miss" because the company increased its earnings over last year and its competitive position remains intact. This is a simplified example, as each company has many moving parts that need to be analysed. However, this short-term behaviour provides volatility and therefore opportunity for the long-term investor to purchase at lower prices. Just like in an election year, we use the volatility around earnings season to adjust our exposure in businesses we want to own for the long run.

¹ The Globe & Mail