
The Idle Speculator™

A publication of Symmetry Capital Management, LLC

November 5, 2008

Reading the Political Winds

Senator Obama has won the Presidency resoundingly, and a Democrat super majority in the Senate may hang in the balance. In this note, we look backward and forward to assess the significance and potential impact of an Obama presidency for asset values, financial markets, economic performance, and politics.

The Significance of an Obama Presidency

The historical significance of Obama's election, and the social capital it will generate at home and abroad, should not be underestimated. This really is a big deal. It undermines the more cynical views of race and power in the U.S., and it reaffirms the ability of our political system to (eventually) overcome seemingly intractable social conflicts.

Interestingly, it also portends a kind of change that has not been discussed in this campaign, or anywhere else as far as I know – power and access create new realities and impose burdens that will inevitably undermine some important and longstanding myths of racial solidarity. These myths, presumably at an apex with Obama's ascendancy, are inevitably going to recede in the wake of this election. One need only consider, for example, whether unity of the Irish Catholic voting bloc increased or decreased in the wake of JFK's election.

It also shows that an outsider – in this case, a reformed slacker and radical from a broken and unconventional family – will be given a chance to lead, if the American people believe they're the best person for the job. No one would have expected this of Obama twenty five or thirty years ago. He wasn't bred from a pedigreed political class for the job. And yet there he is, ready to move his family into the White House. It's an incredible moment, with a long and twisted road behind it.

As for the candidate himself, we've been impressed overall. His leadership qualities, intelligence, and sobriety are apparent. His campaign was daring, innovative, and remarkably effective. Will he be able to lead a presidential administration and a country as effectively? More importantly, what direction will he lead us in? And where's that likely to get him?

Drawing Comparisons

The 20th century saw the election of six Democrats to the Presidency, and we see some interesting parallels between Obama and several of them.

Woodrow Wilson expended a good deal of political capital on progressive ideals, with mixed results. He lost Congress to the Republicans in 1918, and was succeeded by three Republican administrations.

FDR was a strong wartime leader, but also a maelstrom of political change, some good, some bad. His ability to change the office of the President so radically was enabled to a significant degree by severe Republican bungling in the face of a deep economic downturn, and their inability to offer a compelling alternative to FDR may well have prolonged the Great Depression, according to some studies.

JFK exuded a youthful and optimistic charisma, and after two difficult years, showed himself to be an intelligent and adaptable pragmatist. He unveiled a very good economic recovery plan in 1962, one based on reducing the tax burden on corporations, with the explicit understanding that employment and tax revenues would benefit as a result (you can watch it here: <http://www.youtube.com/watch?v=aEdXrfIMdiU>).

Jimmy Carter was swept into office by a widespread desire to break with the Nixon years, and promises of middle class tax cuts. I personally recall the optimism he inspired, as well as the malaise that his policies eventually caused. He helped inspire a national tax revolt, and by 1978 had lost the upper hand in tax reform to Congressional Republicans (primarily Jack Kemp and Bill Roth).

Bill Clinton inspired similar emotions to JFK and Carter, and he jumped head first into a progressive agenda, charging Hillary with developing a comprehensive plan for national health care. His party was turned out by the electorate in 1994, and Clinton, proving himself to be as flexible and pragmatic as his idol JFK, moved emphatically to the center on several key issues. The robust economy and financial markets that followed were no accident. That episode also affirmed the ingenuity of our political system, which should provide some comfort today – we can expect that if Democrats do not wield their power wisely, they're likely to be punished in two years (perhaps four if the GOP is unable to get its act together by then).

Obama's First Years

Policies in the coming months and years look certain to move to the left, but most of the specifics are still uncertain.

At the moment, it looks like there could be an additional economic 'stimulus' package passed before the current Congress retires. There will also be action on textile tariffs that expire in early January, which should provide a good indication of the new Congress' stance on trade.

Once Obama takes office, it's expected that he'll push for an expansion of SCHIP, financing it with higher cigarette taxes; this is a faint echo of Clinton's early years, but much safer politically. Where he goes from there remains to be seen. Certainly he will raise top tax rates and dividend and capital gains rates, but he could accomplish much of that by simply letting the 2003 cuts expire in 2010. He could pursue some of his less controversial tax measures, like making R&D credits permanent, enacting tuition tax credits, eliminating income taxes on many seniors, eliminating capital gains taxes on small businesses and start-ups, and simplifying tax filing.

More controversial measures that could negatively impact most asset values include tax

and regulatory changes that would: seek to punish corporate investment abroad; mandate higher health care costs and payroll taxes for employers; expand the well intended but misdirected limits on executive compensation deductibility enacted in 1993; raise the cost of energy exploration and production, and thus the price of energy to consumers and businesses; increase the likelihood of unionization by removal of secret ballots; and impose draconian costs related to 'carbon emissions'. Of course, not all asset values would suffer, just most. Obama has promised to create both a carbon cap and trade system, and a national 'health care exchange'; it's likely that these initiatives would enrich certain parties at consumer and taxpayer expense.

The net effect of these more worrisome measures will be to lower domestic employment at the margin, which will only worsen the decline in home prices and the financial crisis. Should he pursue these measures aggressively, his early years will be much more reminiscent of Carter than Clinton. And while I believe that is where Obama's heart lies, he's a very smart guy, and is probably well aware of the risks that a sharp turn to the left would create for our economy, and ultimately, his presidency. If he is mindful of those risks, he may try to contain the left flank of his party early on; it will be interesting to see whether he can pull it off. If not, the Democrats are likely to be punished in 2010 or 2012, as they were in 1994.

[Tax Revolt II Brewing?](#)

If Democrats are dismissive of that possibility, they ought to be paying closer attention. In yet another parallel to the 1970s (and one that scant attention has been paid to), there appears to be a nascent "tax revolt" across the country. Tax related measures were on ballots in twenty three states yesterday (WebCPA, 2008), and by our count, 30% of them were aimed at protecting taxpayers' interests, either through caps on taxes or spending, or through lowering rates (Henchman, 2008). The outcome wasn't overwhelming, but if the Democrats lean too hard on the private sector, that's likely to change in future elections.

[Other Predictions](#)

Who's going to fill the GOP's leadership vacuum? There's been some intense debate, especially on the right, about Sarah Palin's political future. We felt that she and Gov. Jindal were the best strategic options for McCain's choice of VP. In hindsight, Gov. Palin, despite her star power, was not quite ready for the stage that she found herself on. We don't expect her to disappear, and if she can deepen her message and broaden its appeal in the ensuing years, she could end up following a path similar to the one Reagan followed in the 1960s and 70s. Overall, she was poorly managed by the McCain campaign. For example, she was introduced as someone who was above dirty politics, but it didn't take much investigation to show that she's a political animal like any other. Gov. Jindal seems to have avoided the national stage during the campaign, but we'd expect to see him as well. And of course, the young guns among the House Republicans will play an increasingly important and public role – and in yet another parallel to thirty years ago, one of them, Rep. Paul Ryan of Wisconsin, is a protégé of Jack Kemp.

It's clear that the economy is in for a long, tough sled. As for where economic policies are

headed, other than a few near certainties and a general shift to the left, there are a lot of crosswinds and uncertainties. The scope of possibilities is clear enough, but their respective probabilities are up in the air. President Obama is very likely to pull to the left, as did JFK, Carter, and Clinton. But like JFK and Clinton, he seems to be pragmatic enough to change course when necessary; if he can avoid Carter's brand of stubbornness when the electorate suggests he do so, then he – and we – should be OK. We'd point out that the best economic performances have come under Democratic Presidents with Republican Congresses, so a Congressional lurch to the left in the next two years, as problematic as that might be in the short term, could have bullish consequences in the longer term, if Republicans can produce a sufficient crop of compelling candidates by 2010 (which is by no means guaranteed).

There's a caveat though, at least in expecting Obama to enjoy the kind of strong economic performance that Clinton did. Clinton benefited, in part, from the fact that much of the world was in poor economic shape relative to the U.S. For example, China was recovering from a slowdown and a currency devaluation, Russia had recently undergone “shock therapy”, and the economies of Asia, Russia, and Latin America were eventually ground down by excessive leverage and a strong U.S. dollar. That meant that most of the first order benefits of U.S. tax and monetary policy accrued to the domestic economy. President Obama inherits a situation that is almost the direct inverse of that, and much closer to the situation faced by Jimmy Carter. Viewed in that light, Obama's challenge is likely to be tougher than JFK's and Clinton's. We believe he has the *potential* to meet it, but only time will tell whether he has the will. With the campaign over, he can no longer be all things to all people. That's one of the hardest things about assuming leadership.

There is at least one market prediction that we're fairly confident in – the next bubbles are likely to be in the federal budget and U.S. Treasury debt, and we wouldn't be surprised to see a return of the “bond market vigilantes” that dogged President Clinton during his time in the White House. We'd also wager that a 'bubble' of government intervention is likely to form in the coming months and years.

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