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FIRST ANALYSIS

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Paul Christopher, CFA
Head of Global Investment Strategy

Jennifer Timmerman
Investment Strategy Analyst

Rounding third base in Campaign 2024

Key takeaways

- In our view, a close and fluid U.S. presidential race leaves potential outcomes prone to abrupt change as debates and interest-rate policy unfold while the economy slows.
- Whether or not a single party leads in Congress and the White House next year, strong inter- and intra-party divisions should persist, making it risky to guess the 2025 legislative and presidential priorities.

What it may mean for investors

- The two presidential candidates overlap on some policy proposals, but the obstacles the eventual winner will likely face (including strong partisanship in Congress) discourage us from speculating about election results.
- We believe our outlook for an economic pivot from a slowdown to a sustained improvement in growth is a more reliable basis for portfolio-allocation decisions today.

Democratic deficits in most of the key swing states have reversed since Vice President Kamala Harris replaced President Joe Biden at the top of the Democratic ticket on July 21.[1] However, the presidential race still depends on several swing states.[2] Among the battleground states, we expect Harris' electoral arithmetic to depend on winning Michigan, Pennsylvania, and Wisconsin. Meanwhile, Donald Trump's likely path to victory is through some combination of wins in Arizona, Georgia, North Carolina, and Nevada.

Polling remains fluid and is susceptible to shifts from political factors (for example, debate performance and third-party candidates) as well as the ongoing economic slowdown that we expect to continue until there is a pivot to stronger, more sustained growth after the elections. We have outlined the rationale for this economic pivot in our recent reports.[3]

1. Dan Clifton, "Harris starting to take the lead in the swing states," Strategas, August 19, 2024.
2. Based on the poll average from RealClearPolitics, as of August 23, 2024.
3. Please see our reports: "2024 Midyear Outlook: Approaching the economy's pivot point," June 2024; "Institute Alert: Rebalancing portfolio allocations," August 6, 2024; and "Institute Alert: Adjusting targets as the economy's pivot approaches," August 14, 2024.

Congressional races should deliver more gridlock

Congressional elections also matter, and we view split government as the likeliest outcome despite a potential coattail effect[4] in some congressional races. Democrats or independents caucusing with Democrats are up for re-election this year in 23 of the 34 contested Senate seats (including three in states won by Trump in 2020), increasing the odds of a slim Republican majority.[5] The math is more challenging for Republicans in the House — of the 218 Republicans up for election, 18 are in districts won by Biden in 2020. However, since 1988 the party majority in the House has followed the presidential outcome in all but two presidential elections (1996 and 2012).[6]

Party majorities in both houses of Congress have turned over more frequently in recent decades, but there never has been an election in which voters simultaneously flipped majorities in both chambers of Congress. The change could affect legislative outcomes because of differences in Senate and House rules and responsibilities. For example, the Senate's exclusive authority to approve presidential nominations could lead to policy gridlock and key vacancies if a majority opposition blocks approval. And without the 60-seat, filibuster-proof Senate majority, partisanship may water down, delay, or even derail legislation.[7]

In fact, the number of new pieces of legislation enacted so far this century is roughly only 60% of its average during the prior 14 two-year sessions of Congress, back to 1973 (Table 1). The table also shows that the number of new laws enacted has trended lower across the past 12 congressional sessions. Bills in recent years have tended to be much longer than in earlier years, but we see fewer bills being passed as a sign of the growing gridlock. The presence of gridlock blocks compromise, and it obliges small majorities in Congress to wait for voters to award large enough majorities to push through a smorgasbord of legislative ideas that gridlock had blocked in earlier sessions. Our base case remains for gridlock, with either divided government or small majorities unable to pass large, catch-all bills.

Table 1. Number of bills enacted into legislation by the U.S. Congress (January 1973 – August 2024)

Congress	Time period covered	Legislation enacted
118	January 2023 – present	78
117	January 2021 – January 2023	365
116	January 2019 – January 2021	344
115	January 2017 – January 2019	443
114	January 2015 – January 2017	329
113	January 2013 – January 2015	296
112	January 2011 – January 2013	284
111	January 2009 – December 2010	385
110	January 2007 – January 2009	460
109	January 2005 – December 2006	483
108	January 2003 – December 2004	504
107	January 2001 – November 2002	383
	Average, 2001 – present	**389**
	Average for each Congress, 1973 – 2000	**628**

Sources: Govtrack.us and Wells Fargo Investment Institute. Data as of September 6, 2024. Includes enacted bills that were either signed by the president or enacted through a veto override or the 10-day rule (including joint resolutions, which can also be enacted as law).

4. This refers to either presidential candidate attracting votes for same-party House or Senate candidates.
5. Amy Walter, The Cook Political Report, May 17, 2024.
6. Charles Apple, "In Control," The Spokesman-Review.
7. The exception to this is for bills that are brought up under budget reconciliation, which can only be used once a year, and only for tax and spending issues.

Executive orders have not picked up the slack, falling to an average of 42 per year since the start of the Reagan administration in 1981. In contrast, there were 64 per year between the early 1950s and the late 1970s and an average of 200 in the first 32 years of the past century (up to Franklin Roosevelt's presidency, which began in 1933).[8]

Political tensions from the past decade also remind us that division within parties can add to gridlock. Even when congressional leaders enjoy a large majority, factions within their party can block legislative initiatives that party leaders had promised during the preceding election campaign. Examples include the GOP's failure in 2017 to repeal the Affordable Care Act and the Democrats' frustration at the defeat of their Build Back Better bill in 2022.[9] To complicate matters for 2025, the debt-ceiling suspension ends after 2024, and both parties will likely expend time and energy to arrive at a new one no matter who wins the White House.

Issues more likely to impact investors through 2025

Both presidential candidates have offered policy ideas in their public remarks, including speeches and interviews, and these have been widely cited throughout the press. However, their campaign websites offer little proposed policy detail currently. We still want investors to be aware of potential policy proposals, even at a general level, and that is what the next two sections consider, with the caveat that we believe policy proposals in any campaign typically develop more substance and detail only after the new government comes to power and sets its priorities.

Table 2 illustrates that foreign-trade policy, fiscal policy, and small-business support top our list of the most significant issues for our 2024 – 2025 outlook and investment guidance on which the candidates' positions are similar, either in intentions or outcomes.

Table 2. Campaign issues with significant overlap and most potential market impact through 2025

	Harris	Common ground	Trump
Fiscal policy	Expanded child tax credits, subsidies, and other spending exceed revenue from tax hikes	Risk of aggravating unsustainable fiscal deficits	Extend 2017 tax cuts — both individual and some corporate provisions
Foreign-trade policy	More strategic tariffs in support of U.S. labor and focused on U.S. adversaries	Additional tariffs, protectionist trade policy favoring domestic manufacturers	Generalized tariffs of 10% – 20% on most imports, 60% or more on imports from China
Small-business provisions	Increased deduction for startup costs, licensing reform, greater funding, reduced regulation	Potential compromise on small-business 20% income tax deduction	Looser regulations and potential tax relief

Source: Wells Fargo Investment Institute. Current as of September 6, 2024.

The two candidates differ starkly on **fiscal policy**. Some of the provisions of the 2017 Tax Cut and Jobs Act (TCJA) expire at the end of 2025. Trump has favored TCJA extension along with additional tax cuts, including on Social Security benefits. Failure by Congress and the new administration to extend Trump-era tax cuts would likely leave individuals exposed to higher tax rates and other increases beginning in 2026. For example, the top personal tax rate would revert to 39.6% from the current 37%.[10] Estate taxes would revert to a top 40% rate from the current 32%, and the exclusion would be more than halved, to $5.5 million per individual from the current $13.6 million.

8. "Executive Orders," The American Presidency Project, August 20, 2024.

9. The Build Back Better legislation eventually became law under the Inflation Reduction Act, but with much reduced cost.

10. "Reference table: Expiring provisions in the "Tax Cuts and Jobs Act" (TCJA, P.L. 115-97)," Congressional Research Service, November 21, 2023.

Harris appears to align with Biden in terms of higher taxes on households with annual incomes above $400,000 and levies on household wealth, including unrealized capital gains, though specifics of such a measure remain unaddressed. Harris also favors a new tax on unrealized capital gains for a subset of wealthy individuals. The plan applies only to individuals with at least $100 million in assets, with an effective tax rate of less than 25% of their income and with 80% of that wealth in tradeable assets.[11] That threshold would exclude private startups and real estate, though there would be a deferred tax capped at 10% for unrealized gains when they are liquidated.

The candidates' fiscal plans come from different directions, but we see overlap in that both would widen federal deficits significantly, no matter who sits in the Oval Office. Geopolitical strains also risk expanding the deficit as defense outlays rise. Beyond any discretionary deficit widening, we anticipate that financial markets will weigh the potential for inflation and higher interest rates from the ever-widening structural deficits driven by entitlement programs, mainly Social Security and Medicare. These programs have inflation indexing that automatically boosts spending, even as indexing of tax brackets restrains federal revenue growth.

Practically speaking, however, such changes should require larger majorities than we envision, even under single-party government. For example, negotiations over the fiscal-year 2024 budget stalled at times last year because of differences within the GOP over the size and distribution of government spending sketched out in a debt-ceiling deal. Nevertheless, investors may want to consult with legal and tax experts to help manage that potential risk.

Policy overlap extends to more restrictive **foreign economic policies**, which are focused on tariffs and reflect a bipartisan trend toward more fragmented, protectionist measures that can be implemented through executive orders. International trade and investment restrictions would likely reinforce a slower U.S. economy early in 2025 if the levies are implemented, and they could work their way into higher price inflation as firms pass along tariffs to consumers.

Yet, a couple of factors may mitigate these negative effects. First, the inflationary impact may be lessened to the degree that the U.S. expands its already sizable purchases from countries other than China, such as Mexico and those in Southeast Asia. Second, from a legal perspective, Trump's proposal for a 60% tariff on Chinese goods and a blanket 10% – 20% tariff on other trading partners may fall afoul of the June 28, 2024 Supreme Court decision that eliminated the so-called Chevron doctrine, by which judges gave the executive branch wide latitude to interpret laws for regulatory purposes.[12] To reiterate, a president's power to unilaterally implement his or her campaign promises is not necessarily predictable before the election and may not be until a court decision comes much later.

We also see bipartisan support for extending key **small-business provisions** in the expiring TCJA, notably the 20% tax deduction on qualified business income. However, the Democrats' push for expanded child-care tax credits as a quid pro quo for small-business tax relief could complicate negotiations as part of a broader tax debate in 2025.

Issues less likely to impact investors through 2025

Table 3 lists issues where we see less overlap between the candidates and, therefore, less room to compromise. The extent and timing of their potential market impact should depend on the priorities and leadership skills in the

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11. The effective tax rate shows the portion of income actually paid (after deductions, write-offs, etc.), not simply the tax rates applied before those adjustments are made. The tax payer would be subject to levies on unrealized gains and other wealth, if actual payments were below that 25% threshold. Presumably, the effective rate would rise from 25% after the added levies were applied.

12. The president's tariff authority rests on statutes that allow the executive to protect U.S. industries against foreign government tactics that block U.S. exports or where dependence on foreign goods threatens U.S. security. Under the new high court ruling, formally *Loper Bright Enterprises v. Raimondo*, U.S. courts might rule on whether blanket tariffs on allies or raising the current retaliatory tariff on China (from 25% to 60%) extrapolate too far from the statutes. For more on how the post-Chevron legal environment may apply to tariff policy, please see Alan Wm. Wolff, "Would Trump's threats of new tariffs survive legal challenge in the Supreme Court?" Peterson Institute for International Economics, February 16, 2024.

White House and on Capitol Hill. We think these issues are worthy of investor attention, but they currently appear too fractured by partisan disagreement to affect our current investment outlook through 2025.

Table 3. Campaign issues with much less overlap and potential market impact through 2025

	Harris	Common ground	Trump
Housing affordability	Incentives to increase supply and subsidize first-time home buyers	Move toward improving housing supply	Reduce federal regulations and boost supply with federal land
Cost of living (excluding housing)	Address price gouging, cap prescription drug costs, and cancel medical debt	Mitigate high cost of living	Reduce regulatory restraints
Digital assets	Back measures to grow digital assets, tempered by safeguards	Support for digital assets	Decrease federal regulations
Immigration	Support Biden's border and immigration reform	At least some immigrant asylum restrictions likely	Close the southern border, deport millions of unauthorized residents
Regulation	Record regulatory costs on private sector	Little common ground	Hard freeze on new regulations

Source: Wells Fargo Investment Institute. Current as of September 6, 2024.

Other policy proposals (Table 3) face obstacles from likely slim majorities, intra-party divisions, and distractions like the debt-ceiling and the 2026 budget. Even both candidates' goal of a larger housing supply to improve **housing affordability** could face administrative challenges, including zoning restrictions and targeted incentives.

Other, more populist elements in both Democratic and Republican proposals may address top voter concerns like the **high cost of living**, but again, they seem unlikely to gain traction in a divided Congress or even in a unified government with slim majorities that take fundamentally different approaches to the problem. Bipartisan support for **digital-asset growth** is also notable, but partisan views about regulation suggest limited progress on this issue.

On **immigration** law reform, both presidential candidates advocate tougher asylum rules and more vigorous border policing. Harris may follow Biden's stalled bipartisan border-security deal that combines $20 billion in emergency funding for increased detention capacity, accelerated review of asylum claims, and tighter control at the southern border. Trump's immigration plan partially overlaps that bipartisan bill but also proposes mass deportation of potentially millions of unauthorized residents. We think these approaches could put upward pressure on inflation through a tighter labor supply, particularly in labor-intensive, lower-paying jobs in health care, leisure, and hospitality as well as, to some extent, higher-paying construction jobs. Limiting immigration also likely would restrain total consumer spending and the economy's potential growth.[13]

Finally, philosophical differences also shape party attitudes toward **regulation** — Republicans seek to reduce regulation in support of small and corporate businesses, for example, while Democrats seek to use regulation as an instrument of environmental, anti-trust, and other control. The ability of the president to mandate regulations

13. The non-partisan Congressional Budget Office estimated that stepped-up legal and illegal immigration through 2026 would add the bulk of the projected 5.2 million increase in the labor force over the next 10 years and boost the value of output (nominal gross domestic product) by $7 trillion from what it would have been without immigrant arrivals. Source: Congressional Budget Office, "Director's Statement on the Budget and Economic Outlook for 2024 to 2034," February 7, 2024.

through executive orders could be complicated by the previously mentioned Supreme Court ruling that reins in the freedom of the executive branch to interpret legislation.

Investment implications

We believe the economy's approaching pivot provides a stronger basis for adjusting portfolios at this time. We summarize our views below on the elections as potential market influencers:

1. Today's campaign promises often fail to survive intact tomorrow, after the elections.
2. We have greater confidence that a divided Congress will matter more for markets than who is president.
3. Even under single-party government, gridlock is probable due to inter- and intra-party divisions.
4. We will not know how the new leaders will prioritize issues until January or later.
5. The economy is much more likely to move markets than the elections.

For these reasons, we prefer not to change portfolio guidance around campaign promises but rather to orient our portfolio preferences toward our economic outlook, which we think will be more predictable and more important than the elections for moving markets. The points below summarize what we have published in the past month:

1. Instead of maintaining high balances of cash or cash equivalents (for example, money-market balances), we prefer to reallocate into equities or intermediate-term fixed income (with maturities of three to seven years).
2. The interest-rate rebound since early August lows provides a window of opportunity for this reallocation.
3. We favor not selling out of long-term fixed income with nearby maturities but would look for opportunities to add cash from maturing securities to intermediate-term fixed income.
4. Within equities, we favor the following sectors: Energy, Communication Services, Financials, Industrials, and Materials.

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