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This veteran Wall Street investor thinks pundits are overestimating the chances of a Biden victory

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Michael Arone believes that President Trump stands a much better chance of winning reelection than the polls are showing or that the big investors he regularly talks to believe. A surprise Trump win, says the chief investment strategist for State Street Global Advisors, the world's third-largest investment manager overseeing \$2.7 trillion in assets, would be a boon for the likes of tech and health care stocks that could suffer under a Biden administration and keep thriving under Trump, while industrials that benefit from global trade would fare better under the former VP.

In a conversation with *Fortune*, Arone recalled his surprise in 2016 when betting sites put a high probability on a Clinton win at the same time swing state polls stood within the margin of error. "We're exactly in the same spot now, including with investors," he cautions. He adds that the polls have narrowed since June and are close enough in many swing states that the vote could go either way. "Investors have short memories," he adds, "but you wonder if they have amnesia, too."

Arone cites a recent Cato Institute study from the end of July suggesting that two-thirds of Americans are reluctant to share their beliefs about the candidates in this stormy political climate for fear of offending others. "That contributes to the tendency of the polls' becoming less reliable," he says. "Just look at the two most consequential votes of 2016. The polls indicated that Brexit would fail and Trump would lose." For Arone, the election is too close to call—and investors are wagering too heavily on a Biden win.

For Arone, it's the COVID-19 trajectory that explains the shifting fortunes of the two candidates. "The 2016 election is unique; it's a unicorn," he explains. "That's because it's the COVID-19 election." Biden's lead expands when, for example, the pandemic spreads, and contracts when infections decline, states reopen successfully, and tests for new vaccines show promising results. "It's clear people don't think Trump's done a great job with the pandemic," he says. "But when the hotspots in the Sunbelt got better and fatalities trended lower, the polls narrowed," he says. "Biden's lead expanded with the new outbreaks in the U.K. and in parts of the U.S. in the last couple of weeks." Arone believes that whether the COVID outlook worsens or improves in the next few weeks will determine the outcome on Nov. 3.

If the pandemic's grip relaxes in the next few weeks, he says, voters and investors will start viewing the election less as a referendum on Trump's management of the crisis and more of a choice between two sharply contrasting platforms.

For Arone, watching the types of stocks that are thriving and languishing suggests where investors are placing their bets. "The rise in the basket of stocks that would benefit from a Biden win signals to me that the markets assume he'll win in November," says Arone. "Investors may be setting themselves up for a surprise." He notes that industrial and materials shares have been doing well in the past couple of weeks, a sign markets anticipate a Biden win. "Biden is the candidate more closely aligned with globalization," he says. "He has a softer approach on trade than Trump in favoring accords like the Trans-Pacific Partnership. More open trade under Biden would tend to help exports for America's industrial companies and increase global growth, expanding the markets for those products."

On the other hand, he believes a Biden win would be a negative for health care and energy, among other sectors. "Biden would be tougher on drug pricing and favor more universal health care coverage under Obamacare. HMOs and other private providers would suffer as the government coverage and price controls expand." Biden, he adds, would also pursue a climate-friendly agenda that would hurt oil companies.

Tech, he says, is something of a wild card. "Both Trump and Biden have talked about hitting tech companies with more regulation," he says. "But a Biden administration is also likely to impose much tougher antitrust regulations," given the widespread view among Democrats that Big Tech enjoys excessive monopoly power.

Biden also pledges to raise the corporate tax rate from 21% to 28%, a move that in Arone's view would be an overall negative for stocks. "The corporate income tax has been a race to the bottom," he says. "It's only been increased twice in 80 years."

In general, Arone believes that the markets fear a blue wave would mean higher taxes and stiffer regulation, a bad combination for equities. By contrast, a Trump victory would benefit energy, health care, and tech stocks, because "investors would be relieved that tighter regulation and antitrust enforcement won't happen."

At these high valuations, says Arone, the markets have already "paid in advance for next year's earnings growth." He believes that a Biden win would lower both future earnings and price/earnings multiples. On the other hand, stock prices are now so high that they don't have much room to rise even if Trump wins. "We might see a rally," he says, "because some of the fears would be relieved." But he thinks the gains would probably be mild and short-lived.

Arone adds that his observations aren't political opinions but express his view of how the polls, oddsmakers, and investors are handicapping the election. They all got it wrong in 2016. This doesn't mean another big surprise is at hand—but if this is really the toss-up that Arone thinks it is, the chances of another shock are a lot higher than investors are anticipating.