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Hillary Clinton Vs. Donald Trump Vs. Investors

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Donald Trump has a few ideas and Hillary Clinton has a slew of them about how investing should change.

They have one thing in common: Both make investors nervous.

Clinton wants to overhaul the rules on a scope that no other major party nominee in recent decades has conceived of. Trading could get a lot more complicated and expensive. She wants six capital gains tax rates with much-longer holding periods for the lowest levy. And she proposes a tax for high-frequency trading firms that may end up hurting ordinary investors.

Trump's proposals to cut personal and corporate income taxes are standard fare for a GOP nominee. Yet some pro-growth Republicans are unconvinced he will make them happen. They fear his anti-trade and other policies, and have doubts about the fiscal feasibility of tax cuts given his unwillingness to take on entitlements.

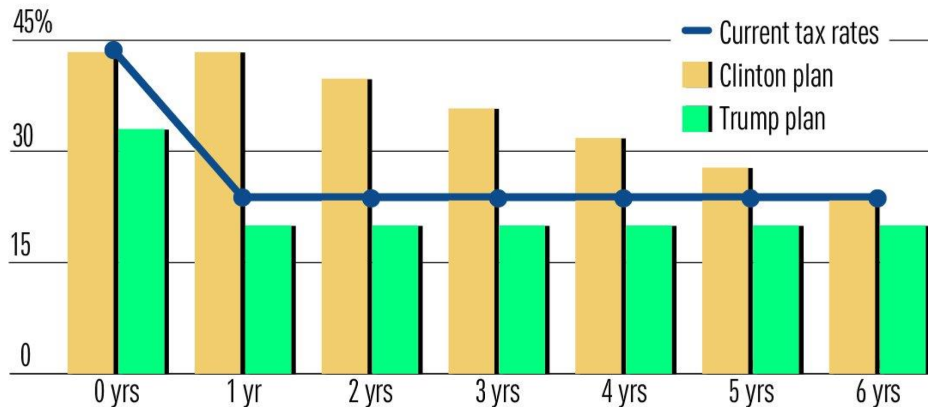
"Trump's plan -- if you believe it -- would be good for investment and financial markets," said Daniel Mitchell, tax policy specialist at the small-government-oriented Cato Institute.

But "I have my doubts," Mitchell acknowledged, noting that Trump hasn't proposed anything substantive that would rein in spending growth and make his tax cuts feasible.

Hillary Clinton's Six Capital Gains Tax Rates

Clinton has crafted policies that reflect her overriding critique that Wall Street is too focused on short-termism or "quarterly capitalism" -- meeting or beating quarterly earnings goals.

The "tyranny of today's earnings report," she says, has led business to operate in ways "that are not helping the long-term profitability of American corporations or the success of our economy."



Whether or not she's right about that -- and there's an active debate -- the clearest rationale of Clinton's program seems to be raising more tax revenue to help pay for new spending programs. The left-of-center Tax Policy Center says that her plan to hike capital gains taxes on investments held for fewer than six years, ostensibly to encourage long-term holdings, would raise $84 billion over a decade. That assumes little change in investing patterns, however. The conservative Tax Foundation, using dynamic scoring, expects Clinton's plans to reduce tax revenue by pushing investors to hold stocks longer.

Trump's ideas could shift incentives for investors in the opposite direction. By lowering the top income-tax rate to 33%, he would reduce the cost of selling profitable stock positions held less than one year, which are taxed as regular income. And killing ObamaCare, as Trump intends, would end its 3.8% tax on nonwage income, effectively lowering both the short- and long-term capital gains rates.

How would Clinton's tax plan work? Right now, capital gains are taxed as regular income or, if shares are held for at least a year, at the much lower long-term capital gains rate. Clinton wants to have six different rates, with the lowest only for equities held at least six years.

For taxpayers in the top bracket ($466,650 for couples in 2016), investments held less than two years would face the maximum tax rate of 43.4% (the 39.6% ordinary income rate plus ObamaCare's 3.8% investment tax). Beyond that, the rate would gradually fall to 39.8% for securities held for two years, 35.8% for three years, and so on, with the lowest 23.8% rate applying only after six years.

Even the Tax Policy Center fails to see the upside of discouraging stock sales. If investors pull funds from one company's stock, "the redeployed cash will create jobs elsewhere," wrote Leonard Burman, director of the Tax Policy Center, after Clinton revealed her plan last year.

"Overall, the economy gains because the extracted cash is invested in more productive activities."

What the proposal really does is reduce the rewards for intermediate-term investments (from one to five years), Burman wrote. The likely impact would be slightly "less capital investment for all sorts of purposes."

Clinton's capital gains tax proposal could have significant implications for the mutual fund industry. It would reinforce a trend toward investing in ETFs or passively managed funds, rather than actively managed mutual funds, "which tend to have a 2- to 3-year time horizon in mind" when they accumulate a position, said Todd Rosenbluth, director of ETF and mutual fund research at S&P Capital Intelligence.

Rosenbluth notes that Clinton's plan would raise the risk that investors could be hit by unexpected capital gains taxes if mutual funds are forced to sell assets to fund redemptions.

Short-Term Corporate Thinking?

Clinton's notion seems to be that if more investors are committed to standing by a company for the long haul, shareholders will back management moves to create long-term value, even if they won't help the company hit short-term targets. She argues that companies would invest more in employees and raise wages, as opposed to buying back shares, if short-term targets were less of a priority.

Clinton isn't alone in bemoaning shortsighted corporate behavior. Larry Fink, CEO of **BlackRock**(BLK), the world's biggest asset manager, has made the same case to S&P 500 company executives in recent years. "Today's culture of quarterly earnings hysteria is totally contrary to the long-term approach we need," Fink wrote early in 2016.

He continued: "To be clear, we do believe companies should still report quarterly results -- 'long-termism' should not be a substitute for transparency -- but CEOs should be more focused in these reports on demonstrating progress against their strategic plans than a one-penny deviation from their EPS targets or analyst consensus estimates."

Fink is on board with the idea of stretching out the holding period for the lowest capital gains rate. He went as far as to propose a 10-year holding period. Yet, whereas Clinton is talking about unidentified changes to corporate law to keep CEOs focused on the long term, Fink's missive to S&P 500 CEOs proposes a much more straightforward idea that doesn't require the intervention of politicians.

"We are asking that every CEO lay out for shareholders each year a strategic framework for long-term value creation. Additionally, because boards have a critical role to play in strategic planning, we believe CEOs should explicitly affirm that their boards have reviewed those plans."

As evidence of short-termism, Fink cited a six-year high in dividends as a share of profits and a 27% increase in buybacks in 2015. Yet by another measure, long-termism seems to be in vogue, wrote Mark Zandi, chief economist at Moody's Analytics.

R&D investment "has never been greater relative to the size of the economy," Zandi wrote after Clinton's initial speech on quarterly capitalism last year. "These investments are as risky as they get, and if they pay off it is generally long into the future."

The real problem with the economy, Zandi offered, isn't shortsighted behavior by American companies, but a broken tax code. "Our corporations pay too high a tax rate to be globally competitive," he said.

Candidates' Wall Street Ties

Both Clinton and Trump have a history with Wall Street that makes their respective parties uncomfortable.

Clinton was on the **Wal-Mart** (WMT) board of directors when Bill Clinton served as Arkansas governor. After leaving her post as secretary of state, Clinton famously earned big money giving speeches to **Goldman Sachs** (GS) and other securities industry audiences.

Wall Street has generally warm feelings to the Clintons. In 1997, President Bill Clinton signed off on a capital gains tax cut (from 28% to 20%). Hillary Clinton served as New York senator.

That history suggests that Wall Street doesn't have cause to fear Clinton. Her policy ideas may not be music to the ears of investors, but they lack the hard edge of Bernie Sanders' plan to make college free by slapping a financial tax on Wall Street transactions, at a cost of $75 billion a year. His plan would have cost investors $5 for every $1,000 worth of stocks traded, which would mean a big reduction in trading volume, likely more financial market volatility and possible stock-market declines.

Compared to that, Clinton's tax on high frequency trading may seem inconsequential, though it could be bad news for regular investors. Her idea, as currently conceived, is to charge a fee for canceled orders with the goal of discouraging trading firms from seeking to manipulate the market. Roughly 97% of all orders submitted are eventually canceled.

Some policy analysts have suggested that traders could simply modify orders and largely skirt the fee. But when Canada's securities regulator began charging a fee based on the number of market messages (trades, orders, cancellations, modifications), the number of messages dropped by 30%. Did markets work better? Not according to a study that concluded retail traders saw decreased returns, particularly on limit orders, even as institutional traders saw higher returns.

Trump's Economic Ideas

Trump's history with Wall Street is highlighted by the highflying 1995 initial public offering of Trump Hotels & Casino Resorts and its ensuing swan dive. After a corporate bankruptcy in

2004, those IPO investors had lost more than 90% of their investment dollars. Trump himself made out just fine.

So what are investors to make of his "can't miss" plan now?

Trump says he'll get trillions of dollars flowing to America by cutting corporate tax rates from 35% to 15% and getting companies to bring home profits stored overseas.

Apple (AAPL) CEO Tim Cook recently told the Washington Post that the tech titan would not repatriate its massive overseas cash holdings -- over $200 billion -- until there is a "fair" tax rate.

A lower corporate rate would be good news for investors, says Doug Holtz-Eakin, president of the right-leaning American Action Forum think tank. For dividend-paying firms, a lower rate would yield "greater after-tax profits to distribute," he said.

As important as tax policy is to investors, the long bull market under President Obama has shown that tax policy isn't everything. Other economic factors, such as low interest rates and future earnings expectations, have been the drivers, Holtz-Eakin says.

On those other fronts, Holtz-Eakin, an economic advisor to John McCain in his 2008 presidential bid, finds both candidates worrisome.

"Some of his stuff makes sense," like cutting back on regulations, he said of Trump. But when it comes to proposals like his anti-trade ideas, "Some of it is clearly bad."