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TRENDMACRO LIVE!

On the April Jobs Report, and Our 2020 Election Model

Friday, May 8, 2020

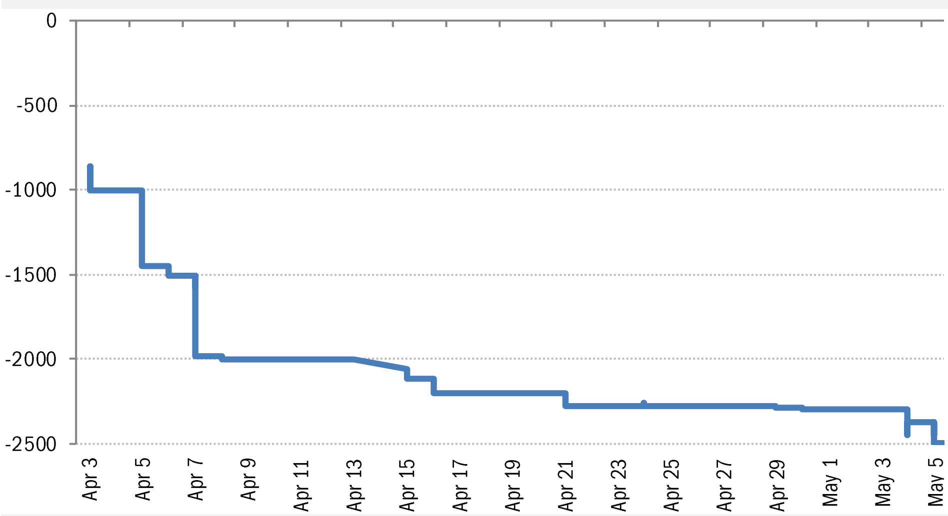
Donald Luskin

The payroll shock turns the model's bet from Trump to Biden. Or is it just broken?

Well, we got the jobs report from hell. It could have been worse, actually. This morning's April Employment Situation report with 20.5 million net lost payrolls was actually an *upside* surprise versus the consensus for 21.885 million, and Bloomberg's "whisper number" at 25 million, which has relentlessly worsened all month (please see the chart below). The surprise is explained in part by downward revisions of 214,000 payrolls for the prior two months (see "Data Insights: Jobs" May 8, 2020).

- The unemployment rate of 14.7%, up from 4.4% last month, as horrific as it seems, also beat the consensus estimate for 16%. It would have been worse, but 6.4 million dropped out of the measured labor force, reducing the denominator in the calculation.
- Average hourly wages soared by 4.7% (*not annualized!*), but this is due to the disproportionate job losses in the low-wage leisure sector. This and other anomalies are explained in a helpful document from the Bureau of Labor Statistics.
- <u>*All this – along with the other breathtaking history-making numbers coming out of the Covid-19 crisis – have effectively "broken" our presidential election model*</u> (see "Inside Our 2020 Presidential Election Prediction Model" March 18, 2019). Taking it at face

Bloomberg "whisper number" for non-farm payrolls from last report (thousands)



Source: Bloomberg, TrendMacro calculations

Update to strategic view

US MACRO, US ELECTION MODEL: This morning's jobs report was a slight upside surprise versus consensus, as was the unemployment rate. The low-wage leisure sector was again the hardest hit, perversely raising average hourly earnings. This moves our presidential election model from strongly favoring Trump to favoring his Democratic rival, presumably Biden. But the model was not calibrated for shocks like this, and this is more an "emergency" than a recession, so the effects on voter sentiment are hard to predict. In the Covid-2019 crisis, Trump's approval has risen to the highest in his presidency, while Biden's has crashed. As the virus crisis recedes in importance, the election – and whether Trump's pro-growth pro-business policies will be continued, especially the low corporate tax rate – will be a major factor for asset markets.

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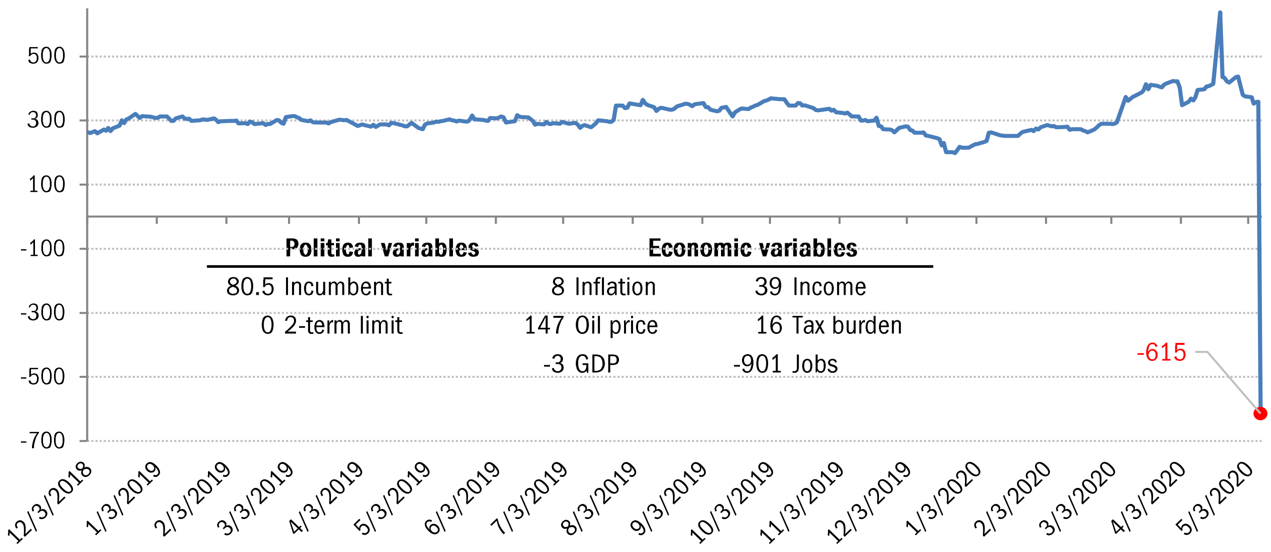
value, ***today's payroll report flips the model's prediction from a 359 electoral college vote landslide win for incumbent president Donald J. Trump, just yesterday, to a 615 electoral college vote landslide loss, today – a loss by more electoral college votes than there even are*** (please see the chart below).

TrendMacro 2020 presidential election prediction model: margin in electoral college votes for incumbent party



Source: BLS, BEA, Bloomberg, TrendMacro calculations

- But then again… on Monday last week, the oil price – one of the model's six macroeconomic inputs, along with payrolls – briefly traded at negative $40 per barrel and closed at negative $38. ***Our model that day – which treats low oil prices as a reason for consumers (and voters) to favor the incumbent president – showed Trump winning by a wider – and more impossible – electoral college vote margin than by that by which it shows him losing today*** (again, please see the chart above).
- We said that negative oil prices wouldn't last after the front-month futures expired, and they didn't (see "On the WTI Crash" April 20, 2020). ***But even with our expectations for a V-shaped economic recovery out of a mid-year recession trough*** (see "After the Crisis, the Work Begins" May 4, 2020), ***today's payroll losses will still be with us on election day to some extent, possibly a large extent. All else equal, if half the jobs lost in April are restored by October, our model will still have Trump losing by 139 electoral college votes.***
- This is not just a matter of civic interest. If our clients and friends will forgive us once again if it seems we are venturing political preferences, we will offer our sincere judgment as strategic forecasters of how markets would react to President Trump not getting re-elected. It is our view, as we have said many times going into 2020, that ***whatever one may think of Trump's personality, in general his pro-business pro-growth economic stance has been very good for asset markets, and those markets will lose value if a subsequent Democratic president reverses that stance*** (see "2020 Outlook: After a Near-Miss Recession, It's the

Election" January 2, 2020).

- *Every Democratic presidential nomination-seeker, including the presumptive nominee Joseph R. Biden, is in favor of raising the corporate income tax rate from today's low 21%, back toward (or exceeding) the highest-in-the-world 35% where it was when Trump found it* (see "Biden: Be Careful What You Wish For" For March 5, 2020). *A reversion to 35% would slice about 12% off S&P 500 earnings with the stroke of a pen. Given the trauma that markets have already suffered this year, that would be a mortal blow*.
- *And with the Covid-2019 crisis, Democrats have a whole new rationale for it. As Blackrock CEO Lawrence Fink, always eager to cater to the Left, reportedly put in a private speech Wednesday, corporate taxes are destined to rise as a means of paying for the "stimulus" spending necessitated by the lockdown of the economy.* It's not "stimulus" if you make the people you were trying to "stimulate" pay for it – but that's politics.
- *For this reason, as the Covid-2019 crisis passes and the economy begins to return to normal, we expect that investors will turn to the election as the primary thing to worry about* (not to diminish the importance of Murder Hornets, of course).
- So we wish we could have more faith in our model now, which correctly predicts every election starting in 1952 in-sample, and out-of-sample correctly predicted the 2012 election within 4 electoral college votes, and correctly predicted Trump's win in 2016 (when every other quantitative model predicted Clinton by a landslide). But a model is only as good as its inputs – and while we don't doubt the technical accuracy of the reported macroeconomic variables we use, we do doubt their meaning and significance in the hearts and minds of the electorate in this highly unusual recession.
- This is not really a recession. It is a "shock." It is not the result of the endogenous accumulation of internal imbalances, but rather an exogenous bolt from the blue, a national emergency. Recessions divide people into haves and have-nots. Emergencies bring people together, and when they are over, "animal spirits" are reinvigorated in a spirit of shared victory over shared hardship. Remember, the terrorist attacks of September 11, 2001, didn't cause a recession – they marked the end of one.
- We can't rule out that even though, by the numbers, the US economy will appear to be still in severe hardship on election day in November, we are very certain it will be on the upswing. *The question for Trump, come November, is whether voters are resentful that conditions are worse than they were a year ago, or glad that they are better than they were six months ago.* Remember, Franklin D. Roosevelt was re-elected in a landslide in 1936 even though the unemployment rate was 16.9% – because it *had* been 24.9% three years before.
- *And Trump's approval ratings have not been hurt by the Covid-2019 crisis – despite attempts by his opponents to blame him for it, the way George W. Bush was blamed for Hurricane Katrina* (see "Covid-2019 Becomes Covfefe-2020" February 28, 2020). *In fact, at 49%, they're toward the high end of what he's experienced*

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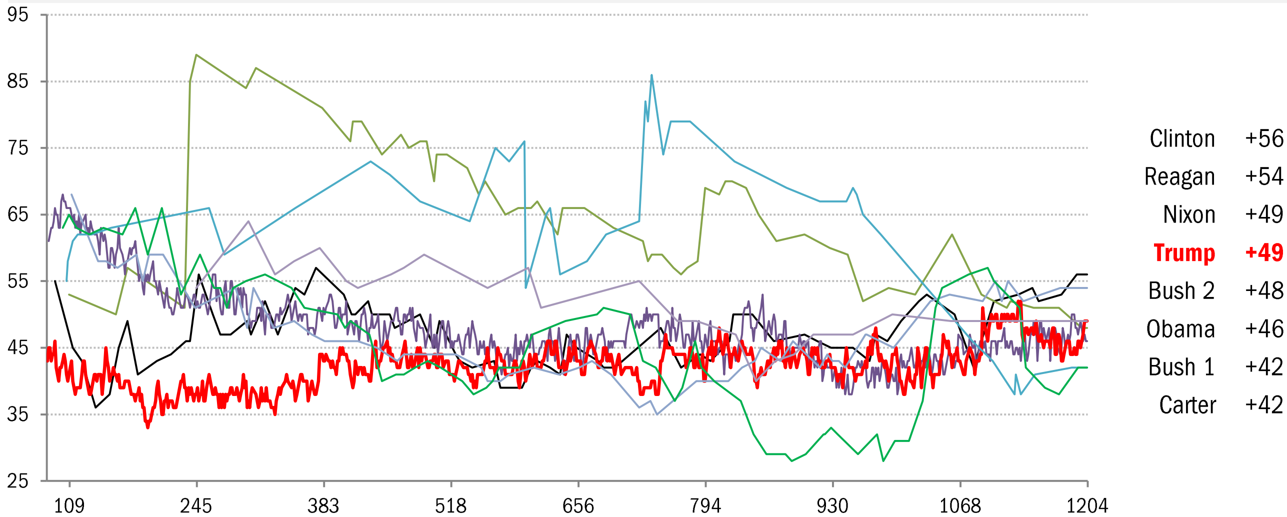
during his controversial presidency (according to Gallup, his highest ever).

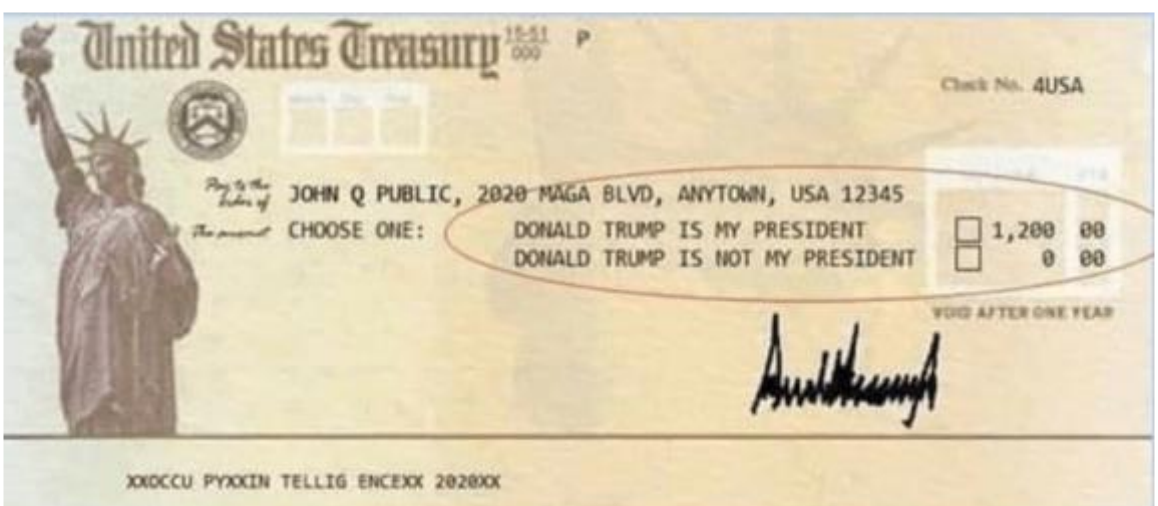
- 49% exceeds the approval ratings on this day of the respective first terms of re-election *winners* Obama (46%) and Bush 2 (48%), and ties Nixon (please see the chart below). It beats by far the two re-election *losers* in recent history, both of whom were dogged by weak economies – Carter (42%) and Bush 1 (42%).

Presidential approval-minus-disapproval, day by day in first term



Source: Gallup, Rasmussen, TrendMacro calculations

- *Meanwhile, Biden's approval ratings have crashed during the Covid-2019 crisis*. We warned in February the moderate-seeming Biden would be the most effective competitor for Trump with approval ratings consistently above 50% (see "Video: What you're not hearing about why stocks are making new highs (hint: it's the election!)" February 10, 2020). But after peaking at 54% exactly at the height of the Covid-2019 scare in the last week of March, Biden's approvals have fallen to 41%, a low Trump hasn't seen since late 2017.
- Who's to say why? Perhaps Trump's team has managed to



succeed at portraying Biden as mentally inadequate, or perhaps in a world obsessed with Covid-2019, Biden has not done enough to define himself. We think, more likely, *it's an example of the awesome power of presidential incumbency*. Whatever you may have thought about Trump's daily press conferences on the virus, he certainly managed to monopolize the nation's attention as its commander-in-chief. And it's his signature on the stimulus checks (not really, but see the image on the previous page anyway).

- *This is why our model gives any incumbent president an automatic advantage of 80 electoral college votes. For more than a century, except for very special exceptions, incumbents always win because they have the asymmetrical power of the presidency.*
- If we had to make a sealed-envelope prediction today, we'd say that Trump will be re-elected. That is contingent on the US economy achieving, by November, a visible down-payment on the V-shaped recovery we expect (see "After the Crisis, the Work Begins").
- So our outlook – starting from today's very low base – is quite optimistic. We are very respectful of the uncertainties and the risks.

Bottom line

This morning's jobs report was a slight upside surprise versus consensus, as was the unemployment rate. The low-wage leisure sector was again the hardest hit, perversely raising average hourly earnings. This moves our presidential election model from strongly favoring Trump to favoring his Democratic rival, presumably Biden. But the model was not calibrated for shocks like this, and this is more an "emergency" than a recession, so the effects on voter sentiment are hard to predict. In the Covid-2019 crisis, Trump's approval has risen to the highest in his presidency, while Biden's has crashed. As the virus crisis recedes in importance, the election – and whether Trump's pro-growth pro-business policies will be continued, especially the low corporate tax rate – will be a major factor for asset markets.