

Some comments on the 2016 U.S. election

The electoral vote vs the popular vote

The presidency is decided based upon electoral votes. There are 538 total electoral votes and 270 are needed to win.

The electoral votes are distributed over all states; the larger the state population the more electoral votes that state is worth. The candidate that wins the most votes in a state gets *all* the electoral votes of that state. A 51% majority in a state gets as many electoral votes as a 90% majority. No extra points for winning big and no points for second place.

The popular vote simply counts all the votes over the whole country one for one. The popular vote does not matter in terms of deciding the presidency.

While one can make the argument that it is clearly undemocratic that a candidate that wins the popular vote can still lose the election, the electoral vote is all that matters under the current system.

The new President-elect Donald Trump, always the entertainer, had this to say on the subject:

Nov 6, 2012

"The electoral college is a disaster for a democracy."

Nov 15, 2016

"The Electoral College is actually genius in that it brings all states, including the smaller ones, into play. Campaigning is much different!"

While Mr. Trump clearly is very flexible in his opinions, I think he has a good point in that if the presidency had been decided upon popular votes instead of electoral votes both campaigns would have had different strategies before the election and the outcome of the popular vote might have been different as a result.

Election results

First of all, 46.9% of eligible voters didn't vote. 25.6% voted for Hillary Clinton, 25.5% voted for Donald Trump and 2% voted for Gary Johnson and Jill Stein. If "didn't vote" had been a candidate, it would have won by a landslide. For some reference, in the 2014 Swedish election only 14.2% of eligible voters did not vote.

Trump won the electoral vote 306 – 232 as he won most of the swing states such as Florida, Pennsylvania and Michigan.

Clinton won the popular vote 62 million to 61 million by the latest count. The main reason for this was a 3 million vote advantage in California.

At first glance, it certainly looks like Trump won the electoral vote by a large margin but let's take a closer look at some of the key states.

Pennsylvania: Trump won by 68 000 votes (Total votes 5.95 million – Electoral votes 20)

Michigan: Trump won by 12 000 votes (Total votes 4.77 million – Electoral votes 16)

Wisconsin: Trump won by 27 000 votes (Total votes 2.93 million – Electoral votes 10)

As you can see, **107 000 votes in these three states made up the difference in this election.**

Had Clinton gotten 54 000 of those (less than 0.4% of the total votes in these three states), she would have reached 278 electoral votes and been the next president. An observation from professional sports seems very fitting to describe the situation: The higher the stakes, the smaller the margins between success and failure.

Remarkably, in Michigan, there were 88 000 people that took the time on a Tuesday to go to a voting facility, vote for other offices on the ballot but then left the presidency vote blank (in 2012 the same number was 50 000 voters). While most of them probably knew that their vote would be very important they still could not muster to vote for either candidate.

This illustrates well the theme of this election regarding the candidates; many people did not like either one. After the election only 32% said they were "proud" about the outcome – in 2008 when President Obama was elected for his first term the same number was 67%.

As mentioned above, there were also two other candidates besides Trump and Clinton in the presidential race – Gary Johnson for the Libertarian Party and Jill Stein for the Green Party. Combined, they got the following number of votes in the crucial states:

Pennsylvania 192 000 votes

Michigan 224 000 votes

Wisconsin 137 000 votes

I don't know where these votes would have ended up had the names of Johnson and Stein not been on the ballot but it's clear that in the three key states they would have had the power to make a big difference.

Predicting the future is hard

I think three things were true regarding the election and the stock market:

- 1) Most people did not think Trump would win.
- 2) In the case he would win, most people did not think the stock market would do well.
- 3) Most people were wrong on both accounts.

My working hypothesis was that it would be much closer than the media predicted due to two primary reasons. First, the fact that many voters didn't want to admit to polls that they were going to vote for the more controversial candidate Trump (this has been the case in every recent election and/or referendum that I have followed). Second, I believed there was a "Clinton bias" in the media as many large newspapers openly endorsed her.

During the last week before the election I had the odds at a slight advantage for Trump. This was not based on any analysis done on my part but primarily on analysis done by Marcus Oscarsson that covered the elections on TV4. Not only has he loved politics since he was a kid; he is also very smart, hardworking and has shown an uncanny ability of being right in his analysis and predictions during the whole election season. What he manages better than most is to be emotionally detached and remain completely unbiased – I think it's fair to say that this election was especially difficult in this regard for many people.

Keeping your emotions at bay might not be desirable in life in general but it's very helpful when you're analyzing difficult multi-dimensional problems. I highly recommend Marcus to anyone interested in politics.

So, did we adjust our portfolio based on my belief that Trump had a higher than expected chance of winning?

No, besides making some extra liquidity available going into November, I did not make any changes. Why not?

As I discussed in the last half year letter regarding Brexit; that is not what we do. Even though my viewpoints were that Trump had a higher than expected chance of winning *and* that his economic plan was a net *positive* for US businesses (more on that below), I didn't know what the market's reaction to him being elected would be. Predicting such things is incredibly complex and acting on them is even harder. As you know, I don't even try.

What about now that Trump has won?

Trump's economic plan that was released in September is designed to grow the US economy by 4% per year over the next decade compared to the average 3% growth rate over the past 60 years and the current 1% to 2% growth rate. In it he outlined plans for:

- large infrastructure investments
- reduced regulation
- lowering the US corporate tax rate from 35% to 15%.

While you may not believe that his 4% growth goal over the next decade is possible, these three initiatives are clearly positives for US corporate profits.

On the negative side, he has said that he will make it harder for US companies to outsource manufacturing jobs to other countries and that he will keep America out of the Trans-Pacific Partnership (TPP) and renegotiate or leave the NAFTA agreement.

Surely, if the positives outweigh the negatives and lead to stronger economic growth, the Fed is more likely to raise interest rates faster which would drive down asset prices over time.

Now, we don't know how much of what Trump said during the campaign that will be acted upon and how much was just campaign talk. Furthermore, whether he will actually be able to implement his ideas remains to be seen.

As far as not keeping one's word; I personally believe it is one of the worst things you can do to another human being, and even worse – to millions of voters. When it comes to politicians, however, this seems to be the rule rather than the exception. That is by no means unique to any particular politician. As tragic as that is, and as wrong as you and I think that is, it is our reality. If I'd have to guess, I would say that more of what he has said will not get done than will. This is usually the case with all new governments and not necessarily because there is a lack of will.

In summary, in terms of US corporate profits, I believe there are more positives than negatives in his plan. There is nothing major there (yet) that has changed the overall fundamental outlook for any of our companies. There might well be in the future though. We currently own shares in three companies that are either US based or do the majority of their business in the US so I will be attentive to new policies that might, negatively or positively, affect those businesses.

Summary

None of this is to say that the stock market is going to go up now. I have no idea about that. Investor sentiment can change for a number of reasons, sometimes predictable but most often not predictable. This is true whether we have just had a historical election or not.

I do think that this early after a very dramatic election it's easy to be over-worried about all the uncertainty. Such worry will pass sooner or later and as investors, one of our jobs is to distinguish worry and uncertainty from true risk. We invest in companies based on their value, i.e. their net assets plus their future free cash flow. As an example, the demand for Fortnox products or its future earnings power is not likely to be materially affected by Trumps policies over the long term under almost any scenario.

It's also good to remember what Peter Lynch said:

“I've always said that I don't know which way the next 1000 to 2000 points in the market will go, but I believe that the next 10000, 20000, and 30000 points will be up.”

Either way, whatever the market chooses to do, we are investing based on what we view as knowable fundamentals; we are not trying to predict macro events or other people's feelings. I'm very happy that we can leave that game to others.

Nov 17, 2016

Daniel Glaser

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