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# Everything Investors Need to Know— and Should Ignore—About the Upcoming Election



## A Major Event

- The quadrennial U.S. presidential election is arguably the world's most important political event with implications for global peace, security and prosperity.
- As citizens, voters or interested bystanders, most of us will approach November 2016 more or less enthusiastically, with firm beliefs about which candidate best suits our personal interests, beliefs and principles.
- As investors, we will also be trying to evaluate how different electoral outcomes may affect different elements of our portfolios.



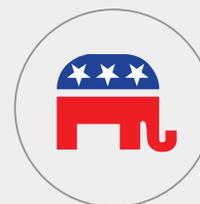
## A Series of Insights

- Corrects a common misperception about presidential politics (**page 2**).
- Offers a few predictions (**page 4**).
- Examines some truths about the impact the parties have on the financial markets (**pages 6–9**).
- Looks at areas that will be directly influenced by the election's outcome (**pages 10 and 11**).

## A Proper Perspective

- Experience has taught us it's probably best if we keep our voting and investing decisions separate.
- From an investor's perspective, there is probably one key fact to bear in mind about this election:

Well-positioned, well-led companies  
will create investment value regardless  
of who sits in the White House.



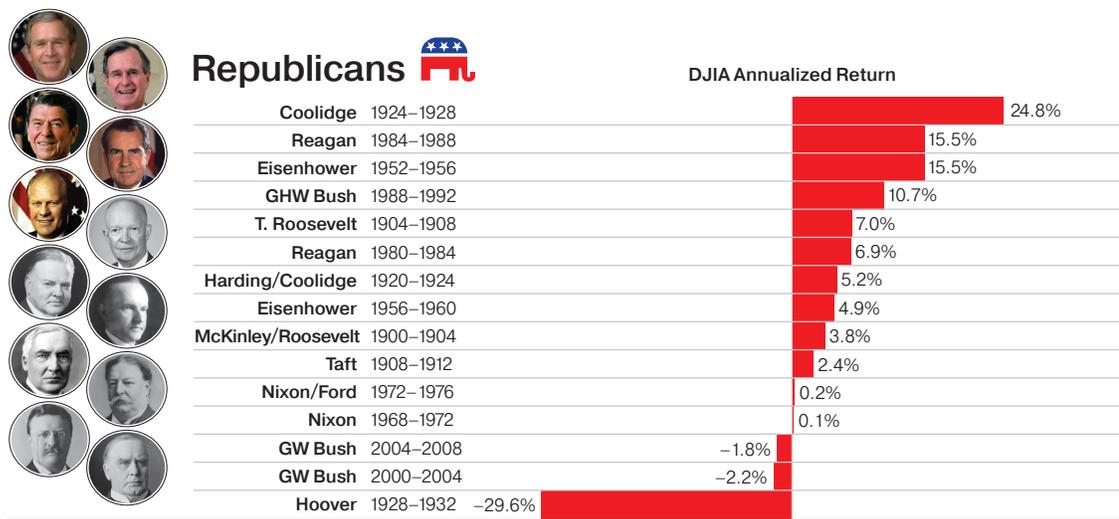
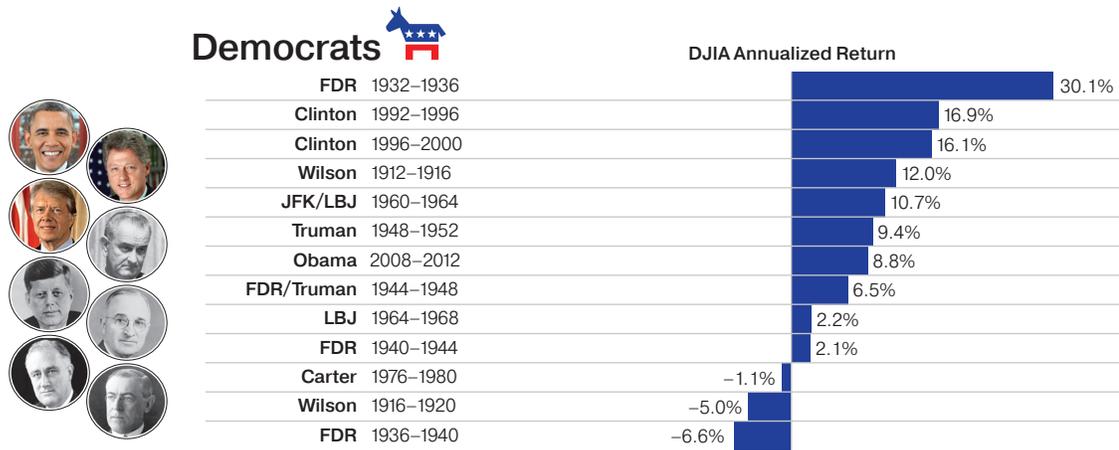
# Clearing a Common Misperception Off the Table

## **The Market Does NOT Perform Any Better When the “Pro-Business” Party Is in the White House.**

A common belief holds that the stock market will fare better when a Republican is in the White House because the Grand Old Party tends to be more pro-business. The related expectation is that Democrats—with their purported preference toward higher taxes and increased regulation—hinder economic and market growth. The historical evidence doesn't support either notion.

- The markets have done very well, and had bouts of difficulty, during the terms of presidents from both parties. **Exhibit 1** ▶
- In fact, if you look at the returns of the Dow Jones Industrial Average since its invention in 1897, it's clear the stock market does not favor either party. **Exhibit 2** ▶
- Investors who stay the course are likely to fare much better than those who invest only when one of the two major political parties controls the White House.

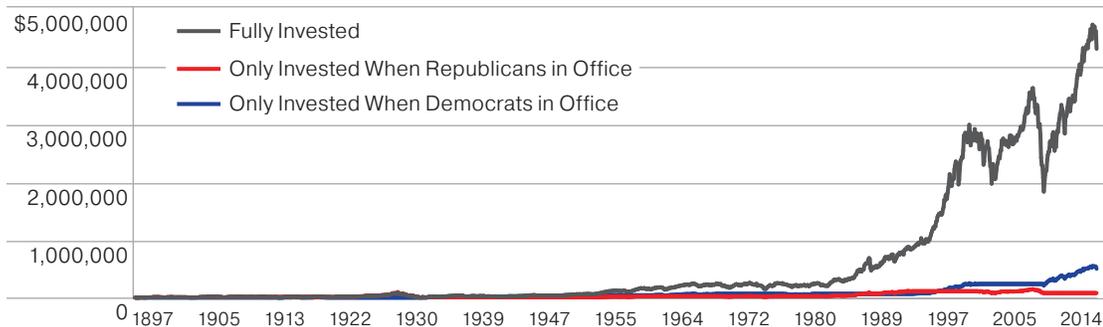
**Exhibit 1: Neither Party Can Lay a Claim to Delivering Better Market Performance**



Source: *The New York Times*. As of 10/26/12. DJIA is an acronym for the Dow Jones Industrial Average. **Past performance does not guarantee future results.**

**Exhibit 2: Investors Who Ignore the President’s Party Fare Best**

Growth of \$10,000 since 1897 in the Dow



Sources: Bloomberg, OppenheimerFunds. As of 12/31/14. **Past performance does not guarantee future results.**

# One Caveat and Two Predictions

## The Caveat:

### Forecasting Is Not an Exact Science.

With all the surges, gaffes and collapses yet to transpire, and with all the domestic and international events yet to shake our perception of the world's risks (think of the rolling financial crises in the month before the 2008 election), it would be easier to forecast next November's weather than predict the presidential election outcome. That being said, it still seems possible to have reasonable expectations about how the two other major centers of Washington power will likely sort themselves out, though voter turnout for each party will certainly have a big influence on which party ultimately prevails.

## Prediction 1:

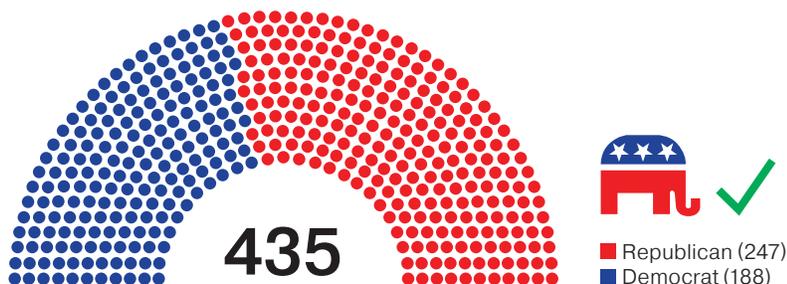
### The Republican Party Will Likely Retain Control of the House of Representatives.

The U.S. Constitution determined that a census would be conducted every 10 years, and its results would determine how the House's 435 seats are apportioned among the 50 states. The most recent census was conducted in 2010, a year when Republicans enjoyed many political victories at both the federal and state level. The power they gained enabled them to draw the lines of congressional districts (commonly known as gerrymandering<sup>1</sup>) to favor Republican candidates. Democrats also tend to congregate near big cities, while Republican voters are spread across the country.<sup>2</sup>

- Given all this, the likelihood that Democrats could win the number of seats needed for a majority—218—is very small, based on current projections. Of course, anything can happen between now and election day.
- You can likely paint the House of Representatives red at least through the 2020 election.

#### House of Representatives—Existing Composition

All seats up for reelection



“Prediction is very difficult,  
especially if it’s about the future.”

—Niels Bohr, Nobel Laureate in Physics

## Prediction 2:

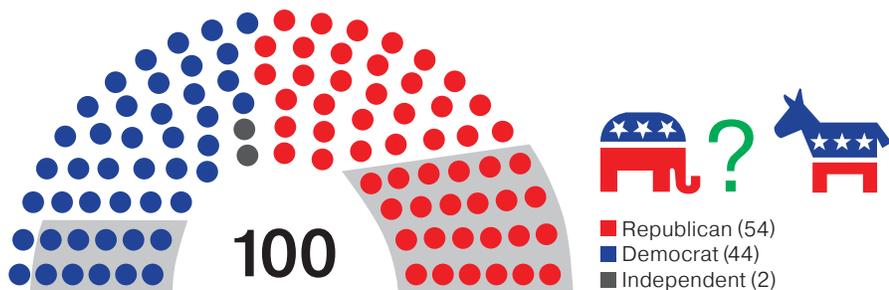
### Regardless of Who Controls the Senate, the Next President Isn’t Likely to Have a Filibuster-Proof Upper House.

The 2010 Republican sweep also saw the election of seven Republican Senators in states that President Obama then carried in his 2012 reelection. Democrats need to gain five Senate seats to retake the majority in the 100-member upper house.<sup>3</sup> We probably will be counting Senate seats well into the morning hours of November 9, and at this point the race for 51 seats seems to be a toss-up.<sup>4</sup>

**Still, 51 isn’t the magic number in the Senate; 60 is.** Without the votes to stop a debate, the filibuster—another hoary tradition (dating from the 1850s)—remains a powerful negotiating tool for any block of 41 Senators, whoever holds the Senate majority. President Obama and the Democrats held a majority in the House, and a filibuster-proof majority in the Senate from mid-2009 until February 2010, and still needed unusual parliamentary maneuvers to pass his signature Affordable Care Act. Barring a historic landslide, the next president is unlikely to have even that brief legislative advantage.

#### Senate—Existing Composition

34 total seats up for reelection—shaded in gray

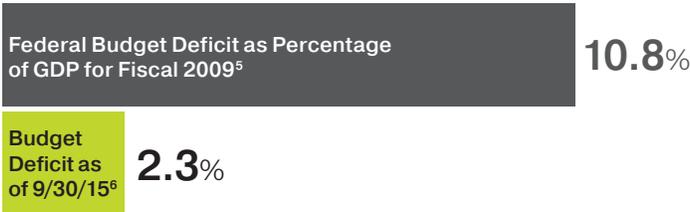


# Six Truths that Won't Be Affected by the Election's Outcome

## 1 Gridlock Doesn't Mean Nothing Gets Done.

The volume of legislation that can get passed will be lessened if the occupant of the White House doesn't have a majority in the House of Representatives and a filibuster-proof majority in the Senate. Still, gridlock doesn't mean inaction. Consider, as an example, the progress made on reducing the federal budget deficit during a period of notorious Washington gridlock.

### Progress on a Budget Deficit Reduction During a Period of Gridlock



### How Did It Happen

- Modest growth in U.S. economy
- Budget Control Act of 2011
- Budget Sequestration (across the board cuts imposed as punishment for 2011 supercommittee's failure to enact comprehensive budget reform)
- The American Taxpayer Relief Act

### What It Means

- Federal debt burden is gradually becoming more affordable.
- Progress was made even during a period when most pundits believed and reported that the degree of animosity between the two parties was leading to stalemates.

## 2 Changes in Washington Don't Typically Come All at Once But in Increments.

With few exceptions (like Obamacare or Dodd-Frank), the United States changes policy, not with one broad, sweeping effort, but rather with small steps. Consider the examples that have been debated for decades but seen few major changes: energy, transportation and immigration policy. We've made significant policy changes—for better or worse—in each of those areas, but we've done so with repeated small steps, rather than one great leap forward.

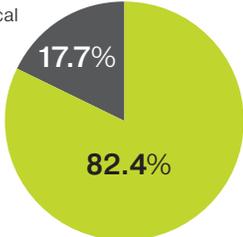


### 3 Campaign Rhetoric Doesn't Always Influence What Happens During a President's Tenure.

<b>The Promise</b> 	<b>The Reality</b> 	<b>The Reason</b> 
<p><b>In support of environmental issues, 2008 candidate Barack Obama promised to:</b></p> <ul style="list-style-type: none"> <li>• Limit carbon emissions.</li> <li>• Support development of non-petroleum fuels.</li> </ul>	<p><b>2008</b> U.S. crude oil production satisfied 25.6% of domestic consumption.</p> <p><b>2015</b> U.S. crude oil production satisfied 46.7% of domestic consumption.<sup>7</sup></p>	<p><b>Mainly affected by economic changes:</b></p> <ul style="list-style-type: none"> <li>• Advanced techniques for oil extraction drove production to a 45-year high.</li> </ul> <p>Also partly influenced by the government—in the form of favorable tax treatment.</p>
<p><b>Conclusion</b></p> <p>Any assumption a Democratic administration would have been unfriendly to the petroleum industry proved irrelevant—because of economic forces at work during the president's time in office.</p>		

### 4 Consumers and Businesses Have a Far Greater Impact on the Economy than the Government.

The overwhelming majority of what happens in the U.S. economy depends on you, me, and the businesses we work for and patronize.

<b>Share of Gross Domestic Product<sup>8</sup></b> 	<b>What This May Mean</b>
<p>Federal, state, and local government spending and investment</p> <p>17.7%</p> <p>Private consumption, private investment, foreign trade</p> <p>82.4%</p>	<ul style="list-style-type: none"> <li>• Whether the government should account for more or less than 17.7% of our economic output is obviously a subject of great debate, as is whether much of that spending is wasteful.</li> <li>• Answering these questions demands our attention, but these arguments shouldn't distract us from trying to figure out how to best participate in the other 82.4% of the economy that produces U.S. wealth—not to mention the vast global output that is produced outside the United States' borders.</li> </ul>

# 5 The State of the Economy Influences Who Is President, Not Vice Versa.

Decades of history prove that the state of the economy determines the president, not the other way around. In fact, the economy's impact on elections can be stated in a fairly simple equation: Strong economy (declining employment and inflation) = A win for the incumbent party candidate.

Exhibit 3: Presidential Elections Are Determined by the Level of the Misery Index (Unemployment and Inflation Rate)

Misery Index (Unemployment Rate + Inflation) Up in the Last Year of Term: Opposition Wins				Misery Index (Unemployment Rate + Inflation) Down in the Last Year of Term: Incumbent Wins			
	Misery Index Up or Down	Incumbent Party Candidate	Opposition Party Candidate		Misery Index Up or Down	Incumbent Party Candidate	Opposition Party Candidate
1960	↑		 ✓	1964	Unchanged	 ✓	
1968	↑		 ✓	1972	↓	 ✓	
1980	↑		 ✓	1984	↓	 ✓	
2000	↑		 ✓	1988	↓	 ✓	
2008	↑		 ✓	1996	↓	 ✓	
<b>Exceptions</b>				2004	↓	 ✓	
1976	↓		 ✓				
1992	↓		 ✓				

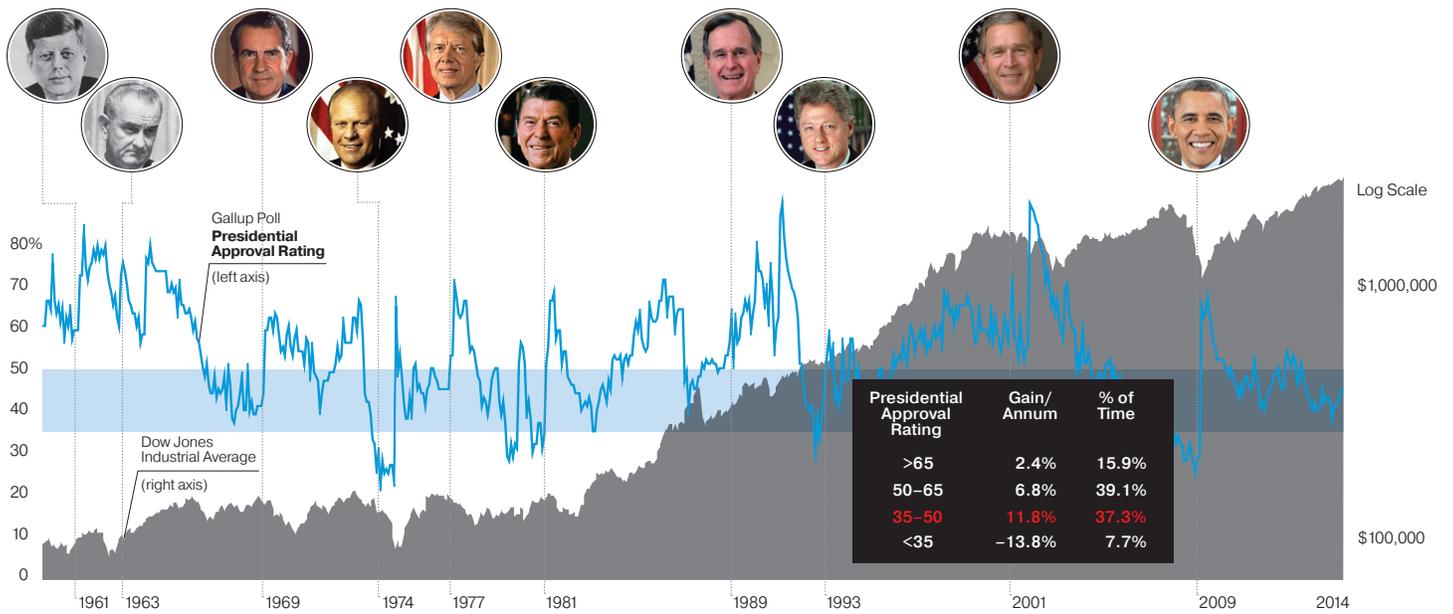
Sources: Bloomberg, OppenheimerFunds. As of 12/31/14. Past performance does not guarantee future results.

## 6 The Stock Market Doesn't Care If the Public Is Happy with Who's President.

Finally, one lingering fear investors may have is that the markets could suffer if the public elects a president who is already very unpopular or who could become unpopular while in office. Here again, though, history suggests the market is resilient and indifferent to a president's current approval rating.

**Exhibit 4: A President's Approval Ratings Does Not Matter Much to the Markets**

Gallup Poll Presidential Approval Ratings and Dow Jones Industrial Average Growth of \$100,000



Source: Gallup, 2/28/15. The Presidential Approval Ratings were introduced to gauge public support for the President of the United States during the term. For illustrative purposes only and not intended as investment advice. **Past performance does not guarantee future results.**

# Issues that Could Be Affected by the Election's Outcome

Only a true cynic—and a misinformed citizen—would conclude it doesn't matter whether a Republican or Democrat sits in the Oval Office. In fact, several major issues are likely to be affected by which party occupies the White House, though if Paul Ryan remains speaker (which seems likely at this point), we might reasonably expect more traditionally conservative viewpoints to remain influential.

## 1 Public Policy



Issue	Democrat	Republican	Our Forecast
<b>Healthcare</b>	Hillary Clinton supports leaving Obamacare in place. She is also in favor of allowing the government to negotiate drug prices with pharmaceutical companies.	Donald Trump—like many fellow Republicans—has said he would repeal Obamacare, though there is no clear indication of whether or not it would be replaced.	We are likely to see changes to, but not the repeal of, Obamacare.
<b>Entitlement Programs</b>	Hillary Clinton wants to preserve and expand Social Security and may look to do so by increasing the current Social Security taxable wage base cap.	The most outspoken advocate of broad reform has been House Speaker Paul Ryan. Donald Trump has not offered any specific views other than proclaiming that he would not cut Social Security benefits.	It's doubtful that we'll see 80 years of entitlement policy reverse, but we probably can expect cost control measures for Medicare and Medicaid.
<b>Defense Spending</b>	While Hillary Clinton hasn't made specific campaign pronouncements about military spending, she has been known as one of the most hawkish Democrats, so it would be a surprise if a Clinton administration cuts defense spending.	Donald Trump is on record advocating for a stronger military, but would look to do so in conjunction with the curtailing of defense spending.	We can anticipate a debate over the best use of additional defense dollars. Given that most of us have a defense contractor in our congressional district, there will likely be a jobs argument added to the natural security case in the negotiation over whether to cut or keep each procurement item.
<b>Taxes</b>	Hilary Clinton has spoken of ending the "carried interest" loophole, imposing the "Buffet rule" to ensure that no millionaire pays a lower overall tax rate than his or her secretary, and introducing a financial transactions tax targeted at high frequency traders. She would also add a surtax for those who make more than \$5 million per year and increase the top estate tax rate to 45%. <sup>9</sup>	Donald Trump has proposed creating 4 tax brackets with rates of 0%, 10%, 20%, and 25%, eliminating the net investment income surtax, lowering the top corporate rate to 15%, and eliminating the estate tax. <sup>9</sup>	Everybody wants taxes simplified, but what looks to you like a loophole looks to someone else like an incentive to build a business. It's important to remember that all tax legislation starts in the House, where compromise may be limited. It's also worth noting that while Donald Trump has proposed significant tax cuts, we haven't heard many specifics about the budget items that will be reduced or eliminated to make those cuts possible.
<b>Dodd-Frank</b>	Democratic candidates have routinely expressed a desire to keep Dodd-Frank and go even further. Hillary Clinton has revealed nothing less, and has proposed to give regulators more discretion to break up financial firms.	Donald Trump, in line with most of his fellow Republicans in this regard, has said that he would repeal the law, viewing it as an example of big government and excessive regulation that stifles economic growth.	While many in the financial services industry may wish otherwise, this compendium of regulations put in place to prevent a recurrence of the financial crisis of 2008 is unlikely to be repealed. How aggressively rules are enforced, however, will depend on who sits in the White House.

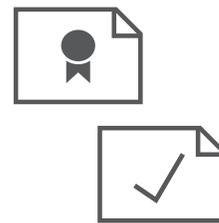
## 2 Judicial Appointments

A Barack Obama-appointed replacement for the late Justice Antonin Scalia will face a stiff battle in the Republican-controlled Senate this year. If an appointment is delayed for the remainder of President Obama's term, the next President will be able to appoint at least one justice to the court. Given that Justice Ginsburg is over 80 years old, and two more (Justices Breyer and Kennedy) will turn 80 over the next three years, there is the possibility that the next President could appoint several justices during his or her term, thereby shaping the court and its decisions for decades to come.



## 3 Regulatory Stance

The executive branch has considerable latitude to decide how existing laws will be enforced. Financial services, education, defense, healthcare, environmental protection and energy production are just a few of the areas that executive direction can influence in the absence of legislative action.



As the campaign proceeds, both Hillary Clinton and Donald Trump may begin to reveal more of their views on regulatory issues, including some areas—such as drug pricing—where the president's regulatory powers may fall short of his or her campaign rhetoric. (Hillary Clinton's tweeted pledge to end drug price gouging offers one clear example.)

## Conclusion:

### It's Probably Best Not to Let Your Reaction to Who Wins Shape Your Investment Decisions.

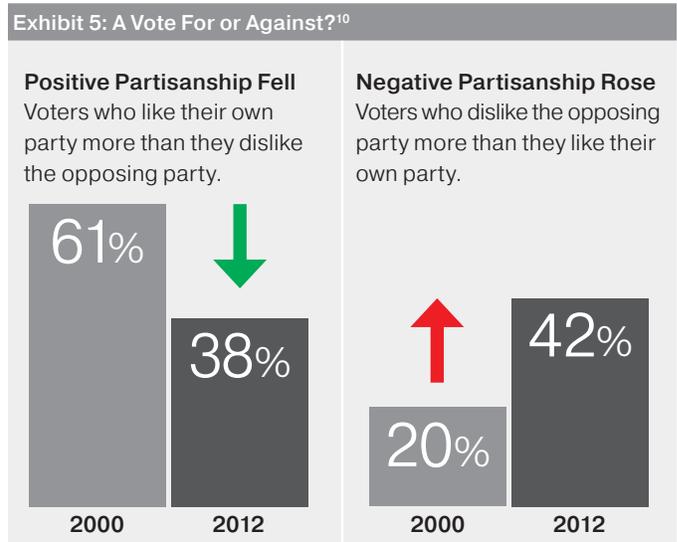
For U.S. citizens and observers in other countries, the U.S. election will, as always, give us sufficient reasons for both optimism and despair. But as investors, whether our preferred outcome materializes or not, we must keep our focus on where economic value is being created under the circumstances that actually occur, not on what would have happened had our choice been realized.

#### Most of Us Dislike the Other Party More than We Like Our Own<sup>10</sup>

I'll conclude therefore with a warning: over the past decade and a half, most of us who lean one way or the other have maintained the same skeptical but positive view of our own party, but our view of the other party has gone from mostly negative to quite bitter. That change means that many of us will be highly frustrated, even angry, at the results of the November election. **Exhibit 5** ▶

#### Stick with Your Plan Under Any Circumstances

On November 9, 2016, be prepared to slam a door or shout down the basement stairs if your candidate and party lose, but don't abandon your well-thought-out investment plan. Patiently compare it to changed circumstance but don't let electoral disappointment turn into financial disappointment as well.





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## The Right Way to Invest

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For more insights on what the 2016 U.S. Presidential Election may mean for your portfolio, visit [oppenheimerfunds.com/Election2016](http://oppenheimerfunds.com/Election2016).

1. The term dates from 1812.
2. Source: Alan I. Abramowitz and Steven Webster, "Explaining the Republican "Lock" on the House: Strong partisanship, not gerrymandering, tells much of the story," University of Virginia Center for Politics, April 23rd, 2015. <http://www.centerforpolitics.org/crystalball/articles/explaining-the-republican-lock-on-the-u-s-house-of-representatives/>.
3. Four seats plus the Democrats' nominally independent allies would give the eventual vice president tie-breaking power.
4. As of 6/30/16. According to the Cook Political Report Cook Ratings. <http://cookpolitical.com/senate/maps>
5. Source: <https://www.whitehouse.gov/omb/budget/Historicals>. Table 1.2.
6. Source: [https://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/50724-Update-OneColumn\\_0.pdf](https://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/50724-Update-OneColumn_0.pdf)
7. Source: <http://www.eia.gov/forecasts/steo/query/index.cfm?periodType=ANNUAL&startYear=2000&endYear=2015&formulas=x13x4x64x3px20xgx44x2g>.
8. Source: <http://www.bea.gov/newsreleases/national/gdp/gdpnewsrelease.htm>. See attached tables.
9. As of 6/30/16. Tax Foundation. <http://taxfoundation.org/comparing-2016-presidential-tax-reform-proposals>
10. Source: Alan I. Abramowitz and Steven Webster, "The Only Thing We Have to Fear Is the Other Party: How negative partisanship is dividing Americans and shaping the outlook for the 2016 election," University of Virginia Center for Politics, June 4th, 2015. <http://www.centerforpolitics.org/crystalball/articles/the-only-thing-we-have-to-fear-is-the-other-party/>.

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