AEI PREMIUM

Political Reality
What We Are Thinking About (WWATA) memo 009, October 28, 2020.
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Next Tuesday, the final ballots will be cast, and the counting will begin. Even after the winners are known and the celebratory balloons fall, lingering questions and uncertainty will remain. No matter the outcome, you can count on articles and talk about how the future looks bright from one side and gloomy from the other.

The purpose of this memo is to outline a few thoughts that we believe will help sort through the political uncertainties of the next administration - regardless of who is in office.

The Four Questions

After the 2016 elections, investor Howard Marks penned a memo that outlined the three questions he used to navigate the incoming Trump administration ([memo here](#)). We've adapted those questions and added a fourth:

1. How much of what the candidate said while campaigning did they mean?
2. How much of what they actually meant will they try to implement?
3. How much of what they try to implement will they be able to effect?
4. How much of what they effect will be from the issues that "land" on their desk?

These four questions are so critical because they help sort through all the noise. At the end of the day, only a subset of things campaigned about will ever see the light of political day (questions 1-3). And on the other hand, there will be challenges, situations, and events that cause the President and Congress to devote their attention to things unknowable today.

Political decision-makers are like everyone else and must allocate the time, resources, and capital at their disposal to accomplish their goals. Furthermore, urgent things that must be dealt with come up. Unlike us, they wake-up with a shot-clock telling them the number of days until they term-out or face the electorate.

In short, there is only so much time to implement their ideas. Each initiative, goal, or piece of legislation pursued is competing for the bandwidth of time, budget, and public attention. The ideas they want to implement will also be limited by the challenges that arise. For 2021, the economy and pandemic will be at the forefront, but it is hard to tell what unforeseen events will dominate the latter part of the term.

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The Economy and Deficit

While there are many unknowns and uncertainties, we know the economy and deficit will be political realities that must be faced over the next 5 – 10 years. The deficit, [measured as a share of GPD](), started trending unfavorably in 2016. Now, with the massive stimulus efforts of 2020 – and perhaps into 2021, attention starts to focus on growing the economy and dealing with a massive federal deficit.

Taxes and government spending will all go under the microscope. Don't get drawn into the debate about which side is better for the economy; the political reality is 1) the U.S. economy needed a stimulus, 2) those efforts altered the federal budget outlook, and 3) it will take years to dig-out. The federal government only has a few options for controlling the deficit and government debt situation: higher taxes, lower spending, and time (inflation).

Since we've broken the seal on taxes, don't lose sight of the reality of the current income tax environment providing the lowest *effective* tax rates most of us have ever seen. Taxes paid are, of course, a function of the tax bracket rates and the taxable income (income less deductions and allowances). Current career-low effective tax rates are unlikely to remain for the next twenty years. This is especially true in light of the pandemic stimulus efforts. Again, don't let this future debate and challenge draw you into the 'us versus them' arguments.

Farm Policy

Another certainty is that direct farm payments won't exceed $40 billion indefinitely. We can debate how or when the adjustment lower might occur, but a reversion to the mean is inevitable. Don't let the election outcome affect how you think about this for business planning. None of us should be planning on the unprecedented level of ad hoc program funds to continue into 2021 and beyond. On the other hand, don't overlook the support provided by traditional farm bill programs.

The relevant question is: what are the farm policy programs – or types of programs - Congress and the White House will be looking to craft into the next Farm Bill (the 2018 Farm Bill expires in 2023)? The follow-up is: how can producers position their operations for success in light of the farm economy outlook and the types of programs eligible to pursue?

How Does Your Outlook Change?

During a recent web broadcast, we were asked about the effects of the election outcomes. This helped us to focus on things that matter to us. Our response was to consider the uncertainties in probabilistic terms. For example:

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- What's the probability of the December '21 corn futures contract exceeding $4.25 between Oct. 15, 2020, and Aug. 1, 2021?
- What's the probability of direct payment to farmers in 2021 exceeding $20 billion?
- What's the probability of your farm reaching its financial goals in 2021?

Now, consider your forecasts today and how you'd change them based on the election outcomes. Will these change if Trump wins? Biden? A Republican versus Democratic majority in the Senate? If you're like us, your responses to these are unlikely to significantly change a week from now based solely on the election outcome. This isn't to say politics doesn't matter, but to challenge your thinking about the context of how politics – and policies - affect you and your operation.

Frame the Questions Appropriately

This brings us to our last point. Throughout the summer, we've been challenging AFN users with questions about the election outcome. Too often, the question surrounding politics are focused on support versus oppose. While these results make for an entertaining conclusion, they don't help the decision-maker. For example, consider the following three questions:

- Do you support or oppose President Trump's policies toward agriculture?
- Do you plan to vote for Trump or Biden?
- What is the probability of President Trump winning the election?

On the surface, these seem like similar questions. However, they couldn't be more different. Confounding these can have harmful consequences to our decision making as you often have to untangle these, especially from the last one. Regardless of the election – be it 2020 or 2044 – you have to carefully navigate these questions and the implications of each answer.

There is a saying in data science: "junk (data) in, junk out." The same can be said about the questions we ask ourselves. If we get too caught up in the reasons we voted a particular way, we can fool ourselves about the implications of the election outcomes.

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