

Episode 67

FS Thrive x Jason Cole: What's happening in Washington?

Ginevra Czech (00:03):

Welcome back to FS Thrive, a podcast by FS Investments. I'm your host, Ginevra Czech, Director of Client Value Add Programs. Today we are talking with Jason Cole, executive Director of Public Policy and Corporate Social Responsibility here at FS. Jason and I have recently had some great calls with advisors and other financial professionals discussing what he calls the three C's: confrontation, competition, and Uneasy Cooperation. We'll explore these themes and discuss what's happening in Washington that could impact markets and your portfolios.

Well, Jason, it's great to be back here with you today. I know that we've connected in the past, and I've had you on a couple of different advisor calls. So today I was, I was hoping that we could just rehash some of the topics that we've been discussing with advisors, whether it's public policy, political risks, things that are important that are affecting your day-to-day, that could affect our advisors, their portfolios, and their, their clients' bottom lines. You know, we can just jump right in. I know that when we've had you on calls, you've really started with the political backdrop. So I, you know, I'm curious just to hear from you what, what's been going on and what you're paying attention to.

Jason Cole (01:26):

Yeah, I think, I think it's important to have context and political context for what's going on in Washington DC right now. And I think the best way to tee that up is to take a look at what happened last November in the 2022 midterm elections where Republicans took control of the House ever so narrowly. And it was, it, importantly, it was the 10th time in the 12 elections since 2000 that control of the White House, Senate, or House has changed. And so you've had this sequence of a number of change elections over the last 22 years, that, that have serious implications for policy. By, by contrast, in the, in the 50 years prior to 2000, there were just nine so-called change elections. And so the, the frequency in which we're seeing change of control in the House, white House or Senate, has some policy implications.

And the, and the biggest one is that either party thinks that they can take control of the House, Senate, or White House in any given election. And so what happens is decisions begin being filtered through this political lens of how will Decision X affect my, my prospects or my opponent's prospects at the ballot box next year? And so that's gonna make everything a lot more contentious in Washington dc. And so that's an important political backdrop to have. The other thing that happened in November was the Republicans took control, like again, I said ever so narrowly, they took a five seat, they have a five seat margin in the House of Representatives. And that close margin, is also really important in understanding what's going on, particularly in the house, but certainly in Congress, because the, that narrow control allows for factions to emerge within the majority party that can have, it can really affect outcomes. And we've seen this in a number of cases this year, whether it's over the debt limit, we're seeing it now as, as Congress tries to pass its annual funding bills and it's, it's there, there's some factions that are emerging in the house that are setting up a lot of confrontations, for members of Congress and particularly the Speaker of the House.

Ginevra Czech (03:45):

Right. Yeah. And I know that we, we talk about those three Cs when we've met with advisors. So you've touched on a couple of them. Can you just define those three C's for us and, and how we've seen them play out a little bit?

Jason Cole (03:59):

Yeah. So I think, I think that there are three C's: confrontation, competition and unsteady cooperation that are really defining, what's happening in DC right now. Confrontation, you certainly see, because we have divided government, you have Republicans controlling the House of Representatives, Democrats controlling the Senate and the White House. And so there's natural confrontation between the two parties as they fight out over their policy agendas in in the House, Senate and White House. There's also confrontation that has emerged within the Republican party, and this isn't unusual. Um, it's, it's typical where, particularly with that narrow majority where parties will, particularly majority parties, will begin seeing factions emerge as, as people jockey for position. And it, it's particularly true when you have a narrow five seat margin. We saw this last Congress when Speaker Pelosi also had a five seat majority, where members, you know, more left-leaning members of the Democratic caucus thwarted of, of big pieces of the, of, of President Biden's agenda. You're seeing that now where you've got members of the Republican caucus thwarting some of the speaker's agenda. Remember the speaker was elected after 15 rounds of voting in November or in January,

Ginevra Czech (05:22):

And that's not common.

Jason Cole (05:23):

And, and that's, that hasn't happened since the 18 hundreds. And so it, it's not, it's certainly not common. And it, and it reflect, it's reflective of the fact that there is a minority of his conference that don't necessarily want him to be speaker, or certainly want to want to extract concessions from the speaker as he moves policy agendas forward. And we're, we're, we're seeing that in, in big ways right now, the other issue that's going on is that you've got, you've got 18 members there, so there were 20 members who voted against McCarthy 14 times. Yep. You have 18 Republican members who are representing districts that President Biden won. Hmm. So you've got sort of 38 members on totally opposite ends of the political spectrum, vying for primacy within the Republican conferences. They try to get policy done, and only what the five seat majority. So the math ultimately doesn't work, and a lot of concessions and compromises have to be made.

Ginevra Czech (06:22):

So I know, uh, you, you typically, we, we talk about competition next, but it does sound like uneasy cooperation is another one of the Cs that we've, we've talked about. So I think you're, you're touching that on that a little bit. If there are gonna be these factions within parties and such slim majorities, we also have an election coming up, what is that, that cooperation or that bipartisanship gonna have to look like?

Jason Cole (06:46):

Well, first there's gotta be cooperation within the governing parties. So cooperation among Republicans, particularly in the House cooperation among Democrats in the Senate and the, and ultimately with the White House, those two entities seem to be pretty aligned on,

on moving things forward. But to get anything done, you need majorities in both the House and the Senate. And so there's gotta be cooperation between the parties, particularly on some must pass items. We saw this back in early June when the two parties came together, and particularly Speaker McCarthy and President Biden came together to cut a deal to extend the debt limit. Um, it went down to the wire. Um, it was really messy. Um, there were some market jitters along the way as there always are when there's that, that debt limit discussions get prolonged. Um, but ultimately there was a compromise between President Biden and Speaker McCarthy to get a debt limit deal done.

Back to confrontation. You had a number of members of Speaker McCarthy's party object to that debt limit deal, and it ultimately took a bunch of Democrats to help pass it and get it over the finish line. And so you're seeing this dynamic, this similar dynamic play out where there's these must pass bills- debt limit, the National Defense Authorization Act, which Congress is debating right now, the funding, the 12 annual appropriations or funding bills that Congress has to do. The FAA is up for reauthorization this year needs to be reauthorized by September 30th. So there's, there are, there are certain must pass bills where cooperation's going to have to happen in order to get these things across the finish line.

Ginevra Czech (08:28):

I, I hate to, to bring up old news, but the, the debt ceiling, I, I do think that's a perfect example and probably the one that most of us are familiar with that had a direct impact on markets, on portfolios. I think, when we last spoke, when we last had you on, you know, the spoiler alert was that we knew it would get resolved. It did get resolved, but is that going to continue to be a problem? And I know we're talking about some of these other must pass bills. I mean, how, how, how much do we need to be worried that that's gonna continue to have an impact on, on markets or investors or even headlines?

Jason Cole (09:05):

So the, the debt limit in the deal was extended until January 1st, 2025. What that obviously means is that you have another cliff on January 1st, 2025, and a deadline, a drop dead when, when the debt limit's going to expire in Congress and the president are gonna need to act. It's an interesting date, right. It comes after the 2024 elections, but before the new Congress and the new president are sworn in. And so it will, it will have to happen in a lame duck session, which may provide some political room and political space for the two parties to come together because the election just happened. And there, that political pressure is relieved a little bit. And so at least that's what I'm hoping for is that 20, you know, January 1st, 2025 will be a lot easier than June 5th, 2022 or 2023, excuse me. But that's a, that's a cliff that's hanging out there, and the next time the debt limit's gonna be in play and, and it's gonna happen at an interesting time, which could, you know, you, you could also make an argument that it, that, that it could negatively affect the dynamics that, that a Republican house, for example, if, if President Biden's reelected doesn't want to give him a win in the lame dock.

Right. And you can see that happening again. So, you know, to be seen or to, you know, but, but that's something the Congress and the President are gonna have to deal with again early in 2025.

Ginevra Czech (10:38):

I do think that that brings us to another one of the C's, which is competition. So we do have an election coming up, and I know that we've gotten a lot of questions from advisors around our thoughts around, you know, Republican primaries, possible outcomes of the

election. So I would just be curious, some of your thoughts around how you anticipate the 2024 election might unfold.

Jason Cole (11:03):

Yeah. So competition is inherent in a two party system. You have elections every two years for the House of Representatives every four years for president and, and every two years for a portion of the Senate. And so you have that natural competition between Democrats and and Republicans for control of those chambers. Probably the most significant piece in 2024 is we have a presidential election. As you point out President Biden is going to be the nominee for the Democrats. That's a foregone conclusion, unless there's some health issues that are unforeseen. Um, but there's, there's a lot of competition going on in the Republican party for who, for who will become the nominee to face off against President Biden. Right now, former President Trump is the clear favorite to win the nomination he's polling to as of today. Um, I saw a poll this morning at 59% in the Republican primary, which is a pretty massive lead.

His next, his next closest opponent, Ron DeSantis, governor of Florida, is polling at 22%. That's a massive gap that has to be overcome. Um, it certainly can be done. The, the first votes don't happen until January with the Iowa caucuses. Um, but what's gonna need to happen if there's a competition that's going to emerge, or a serious competition that's gonna emerge is that the field that is the DeSantis, is the Tim Scotts, the Nikki Haley's, the, and the list goes on and on of about a dozen people who, uh, not named Donald Trump, who are running for the presidential nomination, is gonna have to consolidate very quickly in order for there to be a race for the republican nomination. Otherwise, I think Donald Trump and President Biden will face off again, just like they did in 2020.

Ginevra Czech (12:48):

We've talked about this with some of our advisors as well. There's pretty obvious left and right. You know, we, we pretty much know who's on the Republican and the, uh, the Democratic side in terms of identifying with party in terms of the voter base, but there is the independent and working class voters that are a little bit more of the swing voters. So how do you think that might impact the, the election and what are some of the strategies that we've seen from,

Jason Cole (13:15):

I think independents are in the general election, the voters that, that, let's again say that President Biden and former President Trump have to go after in a general election. Everybody else is pretty much stuck in their camp. Um, and there's a sliver of about 10% of the electorate, and it may be even smaller than that, of independent voters that are gonna be up for grabs. And only in a handful of states, probably about eight states that, that this is gonna be targeted because the way we run presidential elections in this country, it's not a national vote. It's really 50 state by state elections. And so these independent voters are going to be key. They're going to tip the balance. Um, they did so in 2020 to the tune of about 77,000 votes, decided the election across three states, Wisconsin, Arizona, and Georgia.

Um, and so you can, you can see the campaigns beginning to focus there. Biden in particular, is beginning to already tack to the center, I think, in an appeal to these independent voters. You saw this recently when, you know, he, back in March or April approved or didn't veto an effort to overturn a pro, uh, a, a statute in Washington, dc the dealing with crime. Mm-hmm. Um, and, and, and by lessening criminal penalties for certain offenses, Biden uh, approved that effort. Um, clearly sensing that crime and safety are

going to be issues and are issues for independent voters as they probably are for all voters, but in particular independent voters. You saw him approve, uh, the Willow Project for Conoco Phillips to drill in portions of Alaska. Um, and that's, that's not something a Democrat would normally do, but I think it's a clear indication that energy policy, yep, is likely to be on the ballot in November 2024, and that he's trying to talk to the Center on Energy policy. There are rumors that he's going to reinstate family detention policy on the border. Again, immigration is going to be a top issue in the 2024 election. And I think reinstating a policy that President Trump himself instated is, is a signal to those independent voters who are concerned about the border that, that he's trying to do something there. And so you're already seeing Biden in particular, attack to the center on some of these issues. Um, former President Trump hasn't done that yet. Um, I expect that he will once he clears a Republican primary. Yep. Um, but, but those independent voters are gonna be absolutely critical to the outcome of, of the presidential race in particular, but also down ballot races, races for the Senate and the House. They'll, they'll be key as well.

Ginevra Czech (16:05):

So I know you definitely just highlighted a couple of specific policy decisions. You think that, that are gonna impact the election, immigration, energy, any, I know pivoting a little bit we've obviously had some issues with the banking sector, and I know there's been some recent, recent legislation that's come out in that space. Probably not gonna be an issue that is as important to mass voters, but certainly to our listeners. I'm curious what you've been hearing on the, that sector, the banking sector, the finance sector, and some of the legislation that has been getting pushed in that area.

Jason Cole (16:40):

There's been a number of bills passed outta the House of Representatives both in the House of Financial Services Committee, but also off the house floor to incentivize capital formation, particularly among medium and, and, and small businesses. Um, and in, in particular interests, maybe to our listeners is that there have been three bills in various forms and fashion that would update the accredited investor definition and to, to make it more expansive, to allow more people to be deemed as accredited investors. Three of those bills passed the House of Representatives on near unanimous votes, and so they await action in the Senate. But, but those are some issues in the, in the financial services sector. Um, the, the Hospital Financial Services committee is about, in fact, tomorrow we'll be voting on stable coin legislation and broader crypto market structure legislation. Stable Coins has a real shot of getting across the finished line, the broader market structure, probably not.

There's issues, I think, with that bill in the Senate. Um, but, but there's become focus on how do we deal with cryptocurrency and the House of Representatives, which is of course a new emerging market for in, in the financial services sector. Um, you've seen some banking reforms pass in the Senate namely to deal with executive compensation and do clawbacks for executives of failed banks on, on compensation. I I think that Bill has a chance, probably not in its current form, but probably has a chance at some point in the house, or at least as part of a broader deal. Um, and so, so those are some of the things in the banking and financial services sector that are going on right now.

Ginevra Czech (18:30):

That's interesting. And, and you know, another thing that, I mean, crypto is definitely something we're talking about a lot in the industry. Um, I think probably during the pandemic it was a very topical, you know, you had all of the, the Reddit trades and, and whatnot. Something that we've been seeing a lot of chatter about is AI and how AI and

technology are gonna continue to impact investment opportunities. So I'm, I'm curious has that been a, a topic of conversation? It's in the news all the time, but are we actually seeing any sort of action from the government to try and regulate or, or understand?

Jason Cole (19:09):

There's been no legislative action? There is a, there is a ton of energy going into educating members of Congress, and it's a bipartisan, which is really hardening to hear Republicans and Democrats are coming together to get up to speed on AI and, and what the technology potentially means for a whole host of issues which is good that they're trying to educate themselves before jumping in and trying to regulate the space. But Senate a majority leader, Schumer's, been host hosting almost weekly dialogues with academics and other experts in, in, in artificial intelligence on a bipartisan basis with, and, and, and I'm told that those sessions with, with Republican and democratic senators are, are well attended and there's a lot of interest in the topic. I wouldn't expect legislation this year. Um, but I think, I think something in the new, in the next Congress likely could come together.

Ginevra Czech (20:06):

And I do wanna pull on that thread a little bit. The, the idea that there are some issues where there is bipartisanship and, and where, uh, we have members from different parties working together. We've, we've talked about this with advisors as well. What are some of the other issues where you think there is consensus or there is a, a more unified approach?

Jason Cole (20:27):

I think, I think the biggest area of bipartisan compromise is going to be around the issue of China policy and, and what to do about China. I think things you can see coming together, there are restrictions on data flows. Um, I think you can see export controls. I think you can see inbound investment restrictions that, that emerge. Um, and so there, I think there are a number of areas that potentially and importantly could touch investors, particularly when you look at investment controls that could come about as a result of this bipartisan interest in, in, in dealing with the, an emerging China.

Ginevra Czech (21:27):

Um, so I know we've, we've definitely talked about a lot of different things, A lot of, uh, the political side of things, some specific policy. I am hearing a couple of things that I believe are gonna be important to our advisors and our listener base. Obviously, what happens in the, in the global space is important and that will impact the type of investment decisions you make. Um, being able to understand future regulation in certain areas like technology or understanding how the government's thinking about cryptocurrency and then even just understanding the headline risk that is inevitable, that's gonna impact markets. What else should we be paying attention to?

Jason Cole (22:07):

I, I think there's an opportunity for, in addition to China policy and artificial intelligence to look at technology policy broadly. Um, in particular would be this bipartisan consensus that is emerging around the need to deal with data privacy. Um, the two parties are coming at that a little differently but it, but it's born out of, for Republicans the, a concern over large technology platforms doing maybe potentially censoring data. Um, and Democrats have large technology platforms potentially mining data for inappropriate uses. And so there's, there's the remnants of a deal there that I see on, on data privacy that that could emerge. I think you also have to look at, when we talked about this earlier, these must pass bills that, you know, could ultimately affect investors. I mean, we're looking at a National Defense

Authorization Act that's going to boost military spending that's likely will signal some action on Ukraine or additional action on Ukraine.

Um, you're gonna see an FFA policy that, you know, may or may not impact investors, but you're also gonna see the, uh, uh, a, a difficult negotiation session around the 12 annual appropriations bills. Remember the fiscal year ends on September 30th, and in theory, all 12 of those bills have to be passed in order to keep funding the government. Typically Congress hasn't met that deadline in decades, but, and then typically what they do is they pass this thing called a continuing resolution, or in Washington parlance a cr. And I think a CR could be a very difficult thing to get past this year because what CRs typically do are fund the government at current levels. And as we discussed, there's a contingency of the, of, of the house majority of Republicans that don't want to fund the government at current levels and could ultimately stall out a continuing resolution late September, early October, which could drop us into a, into a government shutdown. And we've all seen what happens there. Um, that could be a prolonged effort. Um, it could be very short, but ultimately all 12 of these bills have to get done this year as part of the debt limit deal, or you see a 1% across the board cut in federal spending. Um, that's not an insignificant number. Um, that's getting sucked out of aggregate demand.

Ginevra Czech (24:46):

It's really interesting to get to talk to you about this because I think I have a general sense of, of how the government functions, but it is interesting, perhaps frustrating to hear how much leverage the government has over, you know, our, the, our day to day or, or what can happen just over a bill getting passed that needs to get passed, that every year gets passed. Um, but maybe this year there's, you know, groups of people who've decided they, they don't wanna pass for, for whatever reason. So

Jason Cole (25:20):

Yeah, I mean, that's absolutely right. Must pass bills, provide opportunities for leverage for in the senate, any one member to advance or defeat his or her pet project. Um, and in the house, you know, a group of members, and we've seen this already probably four or five times this year to advance or defeat things that they don't like.

Ginevra Czech (25:48):

Um, pivoting a little bit, this is just something I'm, I'm kind of curious about. There's been a lot of news recently, uh, about mergers with large corporations that have been getting approved or denied. Um, and so I'm just curious that obviously from an investor perspective has a big impact on the, the type of companies that we invest in. You know, what are you hearing about that? What are your thoughts on that?

Jason Cole (26:14):

That? Um, there's a huge effort on the part of the Biden administration around this notion that big is bad and, and, you know, the president is framed it under, you know, fair competition and whatnot, but at its core, it's big, is bad and, and the agency, and you don't hear much about the agency, the Federal Trade Commission is, is the entity that's really driving this anti-merger fervor they were recently defeated, of course in Microsoft and the Activision acquisition. But I, I envision the FTC continuing to be very active in, in trying to prevent mergers of, of large corporations. And, and it's important to know that just the threat of that can have chilling effect on M&A activity. Um, you know, the, the, the street and the lawyers that do these deals know that, that that threat exists and it's a very real threat between the FTC and the Department of Justice right now that these large merger deals will be blocked. And so I think that's something for investors to keep in mind.

Ginevra Czech (27:28):

Well, I think, uh, we've definitely talked about a lot of different things. Um, there's obvious confrontation that we're seeing on a day-to-day basis with some of these must pass pills. I think it'll be interesting to see how that confrontation leads to possible uneasy cooperation, hopefully. We know we have seen that, and I know the spoiler alert is probably that we will have some type of cooperation, but it's, you know, it's gonna come down to what, what one side has to give up to the other

Jason Cole (27:59):

Maybe. Right? I, this is normally I would say yes, normally I would say, you know, people, you know, members will, will do what they do to the very end and, and then a, a compromise emerges. I'm, I'm, I'm not sure not so sure that's the case this year. I think that will happen on the National Defense bill. I think that will happen on the Federal Aviation reauthorization bill. I think that will happen on reauthorization of the Farm Bill. Maybe. Um, it's the 12 appropriations bills where I, I'm not sure I, I, I don't see a path to getting a deal done on those. And, and if you, if I were a betting person right now, I would bank on A) a government shutdown for at least some period of time in the fall and B) a likely 1% across the board cut. We may come back in the fall and I have a different opinion on that, but right now, that's how I see the stars aligning and, and not necessarily a compromise emerging on federal spending.

Ginevra Czech (29:00):

Well I'll, I think that's a great place to close, I'll say that. We'll, I appreciate all of the, the comments and insights. Um, we'll have you back in the fall to give us an update on, on whether or not you still think that that's where, where the challenge is gonna be. Um, I will say the last time we had a government shutdown, I was in the airport, uh, with TSA getting approved for global entry, and I think there were five minutes until the government shutdown <laugh>. So I know there's already a lot of passport delays right now. So hopefully you get your global entry approvals, <laugh>, you get your, your passports before we, we may or not see something like that happen. Jason, anything else you you want us to know before we, we close out?

Jason Cole (29:45):

No, I think I'm good. This is, I, I appreciate being with you. It's always fun to, uh, sit down with you, Ginevra, and, uh, chat about these issues. So thank you.

Ginevra Czech (29:57):

I hope you've enjoyed the conversation. And if you're interested in connecting more with FS Thrive and Jason, find us at FSthrive.com. FS Thrive was produced by Ginevra Czech with help from Aaron Sherman. It was edited and engineered by Aaron Sherman. Special thanks to show advisor Kim Pollock. If you enjoyed this episode, be sure to like and subscribe to the FS Fireside Podcast wherever you stream. Thanks for listening.