Episode 110

Election 2024—Congress matters

[00:00:00] **Jason Cole:** I'd love this to be the headline for the podcast, because I feel very strongly about this. And that is Congress matters.

[00:00:07] **Lara Rhame:** Yeah.

[00:00:07] **Jason Cole:** And that's from a person that spent 12 years in the United States House of Representatives. And so I've got a little bit of bias in this, but Congress matters in this process.

[00:00:17] **Lara Rhame:** Welcome back to FireSide, a podcast from FS Investments. I'm Lara Rhame, Chief U.S. Economist, and I'm joined by Jason Cole, our Head of Public Policy and Corporate Social Responsibility. And there's nobody who is more relevant to markets, to the policy outlook and to how investors are navigating the upcoming election than Jason. Jason has two-and-a-half decades of experience on and off Capitol Hill, and we always get so much out of our conversations with you there. I think these are some of our most watched and most popular podcasts; so excited for today's conversation. Welcome.

[00:01:08] **Jason Cole:** Thanks, Lara. It's great to be back.

[00:01:09] **Lara Rhame:** All right, I'm going to time-stamp today. September 27, 2024.

[00:01:16] **Jason Cole:** 39 days.

[00:01:18] **Lara Rhame:** Okay, good. In case anybody was counting. Thirty-nine days until the election. Jason, as we were talking before we prepared for the podcast, you were saying that pretty much the only question you get asked, and I'm happy that I'll be able to ask you much more than this is: Who is going to win? How do you answer that? Because I know the answer is more than just one name.

[00:01:41] **Jason Cole:** Yeah, the answer is much more complicated than that and the short answer is as it always has been since we've been started doing these a few months ago. I don't know right now, I mean this is a razor thin race at the presidential level and there's also congressional races that we can talk about and we know that are happening.

But at the presidential level—right now if you look at the national polling, the Vice President is running around a two- to three-point national polling lead. She had a small but very perceptible gain in the last two weeks post-debate. And if you were to line graph this, you could clearly see that. She's leading in the national polling by around two to three points. And we can talk a little bit about polling later if you want. As everybody knows, and as we talk about a lot on here, we don't elect our presidents through a national plebiscite. We have 50 state elections where we're going for, where the candidates are going to rack up electoral votes.

[00:02:45] **Lara Rhame:** And people are voting for their senator, their House of Representative.

[00:02:48] **Jason Cole:** Right. But at the presidential level, they're voting for electors.

[00:02:52] **Lara Rhame:** Right.

[00:02:52] **Jason Cole:** There's 538 of them. A candidate needs 270 to win, and we've really effectively sorted ourselves into Republican and Democrat enclaves to a point where we sort of know how 44, 45, 46 states are going to vote.

And Harris starts with 226 electoral votes. Donald Trump starts with around 219 electoral votes, and then we're really down to seven battleground states: Arizona, Nevada. Wisconsin, Michigan, Georgia and where we're sitting—ground zero—you're seeing all the ads here in Pennsylvania.

[00:03:30] **Lara Rhame:** We are really getting inundated with ads.

[00:03:32] **Jason Cole:** Yeah, I'm sorry about that. I'm grateful I only come in here a couple of times a month. The clearest path to victory for Donald Trump is to win North Carolina like he did in 2020, win Georgia and win Pennsylvania. That's 270 electoral votes right on the button.

For the Vice President, she needs to win Wisconsin, Michigan and Pennsylvania, and that's 270 electoral votes on the button. The common denominator in those two scenarios is Pennsylvania. It's the most important state on the map. It's 19 electoral votes, and whoever wins the Keystone State is likely going to be the next President of the United States, which is why you're getting inundated with ads. And that's where it stands.

[00:04:17] **Lara Rhame:** I didn't even realize that we were in the crosshairs to that degree.

[00:04:21] **Jason Cole:** In my opinion, it is the most important state on the map and that whoever wins it, we won't know on November 5. I don't think all the votes will be counted here yet, but whoever wins Pennsylvania is likely the next President.

Where do we stand right now? Out of the seven battlegrounds, Trump's currently winning in three. Arizona, Georgia, North Carolina. So he's got North Carolina, he's got Georgia, he needs Pennsylvania. Unfortunately for him, Harris is winning Pennsylvania narrowly, less than two percentage points, and she's winning the other two so-called blue wall states, Michigan and Wisconsin. She also adds Nevada right now, in the polling.

And if the election were held today, and if you believe all the polls, she would win with 276 electoral votes, six more than she needs, to win the White House. Now, the polls have been wrong in the past, and these things are so narrow, there's not a single state that's above two percentage points. So that's the margin of error we're talking about, and this really could go in either direction.

[00:05:23] **Lara Rhame:** Okay. So, let's take it a level further because I think for all of the policy questions that relate to the outcome of the election, there's the next layer down of who else we're electing when we go to the polls and we encourage everyone to go to the polls.

You've often said your highest conviction call around this election is the Senate is going to swing from being Democratically controlled today to Republican control. The House, I think you had an interesting observation the other day. You told me the House, which is currently in a razor thin Republican majority...

[00:06:00] **Jason Cole:** ...four seats ...

[00:06:01] **Lara Rhame:** Yeah. And, and you've said to me whoever wins the White House is probably going to win the House. Would that also still be by a razor thin majority?

[00:06:12] **Jason Cole:** Yeah, so we'll start with the House and then we'll talk about the Senate. So the House right now, Republicans have a four-vote majority, and so Democrats would need four seats to take control. Now, again, we've sorted ourselves out really well here. There's 435 House seats. If the election were held today, Republicans probably win 210 of them. Democrats probably win around 203. That implies there's only about 20, 22 house seats actually in play.

Now, Republican Congress [House members], there's 17 of them that are sitting in districts that Biden won in 2020; there's five Democrats sitting in districts that Trump won in 2020. That's your sort of 22. There's a handful of other races. There's a couple of open seats in Michigan, that could go either direction, Michigan being a battleground. But at the end of the day, if all of

the Democrat seats broke Democrat and all the Republican seats broke Republican, Democrats would have a narrow majority 220 to 215. Now, it's not going to break that way. We don't have time here today to go to race by race.

But I would also point out that a preponderance of the battleground states are in, or seats, are in California and New York, which aren't battleground states for the presidential race. And so it's going to be interesting to watch, but there's about a dozen of those seats in California and New York. It's going to be interesting to watch since there won't be that top of the ticket poll on those down ballot races. Whether or not, for example, Republicans can hold on—they're predominantly Republican held seats in those two states that are in play, whether they can hold on if there's not a lot of top of ticket polling going on.

And so, I think my gut tells me that whoever wins the White House also probably then wins the House of Representatives. Those two entities, the White House—the presidency—and the House of Representatives haven't gone opposite directions since 1952.

[00:08:10] Lara Rhame: So…razor thin chance, again, only because we're talking about the top of the ticket election being razor thin. Razor thin chance that Democrats get the White House and House, but Republicans get the Senate. And then razor thin chance that Republicans get all three chambers.

[00:08:35] Jason Cole: And not razor thin. I mean, if we're assigning probabilities, which I hate doing, particularly in stuff like this, but you know, a trifecta, right. Coin flip, a coin flip on the presidential race.
If the presidential, or the House goes the way the president does, then you get a Trump presidency, a Republican House. And I do believe the Senate's going to be Republican. So let's call that 50-50. That's a coin flip.

[00:08:58] Lara Rhame: Yeah.

[00:08:59] Jason Cole: But 50-50, the other way, where it's a Harris White House. Again, my gut tells me then it's a Democrat House of Representatives, but the Senate still flips and it's Republican. So you have a 50-50 Republican sweep or divided government with a Democrat House, Democrat White House.

[00:09:17] Jason Cole: Again, bad, bad math, and I hate probabilities, but that's, sort of, the way I'm looking at it.

[00:09:22] Lara Rhame: Well, we've got to summarize it somehow because there are so many moving parts. So we've got to focus the conversation somewhere. Let's talk about polling. Can we trust them? Do you have a favorite? I feel like part of being inundated with the ads is also being inundated with the polls. And again, the best way to have impact is to actually go to the polls and vote. How are we to think about all the polling data that we're getting?

[00:09:52] Jason Cole: There's a ton of polling data and we're being inundated by it. It's difficult to sift through. I do a lot of these events on the roads for our clients and advisors and whatnot. And what I do is I take averages of averages. And so what I mean by that, there's a bunch of polling aggregators—Nate Silver, 538—there's a whole bundle of them, and they all have different methodologies, but they don't just take straight averages. I think the only one that takes a straight average is real clear politics. They'll say we don't like this pollster, so we throw them out. This pollster has been really good historically so we'll weight them more. They fiddle with things and so you've got a national polling basis right now, a spread of anywhere between two points real clear politics and four points, all in favor of Harris, at the national polling level. That's a two-point spread. It's still margin of error. But that averages out.

[00:10:49] Lara Rhame: That's millions of people.

[00:10:50] **Jason Cole:** Yeah, that's millions of people. And that averages out to around 3%. Now, there's polling misses, right. In 2016, Hillary Clinton won the national popular vote by 2.1 percentage points and lost the election in the Electoral College. Joe Biden won by 4.4% in the national election and won the Electoral College by 43,000 votes in three states. So that implies a couple of things. One, that Harris is sitting right at that midpoint right now. If you think the polling misses will be where they were in 2016 or 2020, she's sitting right in that median at around 2.83%. One. Two, it also tells us that Donald Trump, historically, in the two elections that he's already run, outperforms his polling. And so when you start digging into battleground states and you see a half a point margin Harris win or even a-point-and-a-half Harris win, that may not be on the money.

And if you go into battleground states and look at polling misses, the median polling miss across battleground states was anywhere from a-point-and-a-half in Pennsylvania to almost six points in Wisconsin. And if you take that median polling miss and where the polling is today, she would lose every single battleground state.

[00:12:12] **Lara Rhame:** Okay.

[00:12:13] **Jason Cole:** At the median. Now, again, overly simplistic. We don't know that there's going to be the same polling errors. There's been a lot of work done by the pollsters to try to correct from 2016 and 2020. And we won't know where that miss is. We won't know what that looks like until November 6 or a few days after when we dig into it.

That's the cautionary tale on why I think this is a coin-flip race is because we've seen some historic polling misses and (we, financial services) past performances in the case of where we're going to be. But if there is a polling miss again, they could be off in his favor and that's why I think this is a coin flip.

[00:12:55] **Lara Rhame:** Yeah. I think that's really helpful context because a lot of people, and I'm pointing at myself here, are thinking ahead to 2025. We're looking at the economic outlook. Investors are trying to navigate not only the outcome uncertainty, but what it means for regulation, for M&A activity, for geopolitics, for the deficit.

And that's why I want to shine the light on…and this is where you're going to be the flashlight here. Because, you know, what I'm seeing from both candidates is going to be impacted by the down ballot races and how much control they actually have over the economy, which I think is something you and I've talked about.

I think for all of the campaign rhetoric, the reality is, similar to the Fed, there are some things that you can control and a lot of stuff you can't control when you're in the White House. I'm adding up my GDP forecast for next year already. And as many listeners may know, I am actually still fairly positive on the economy.

I think the U.S. economy continues to have a lot of resilience. I think we're going to experience an incremental slowdown from an incredibly fast pace of growth: 2.5% for the first three quarters of 2024. Probably more like 2% in the fourth quarter and next year may look more like 2% or so, 2% in the first half of the year, maybe one-and-three-quarters in the second half. That is an absolutely healthy, sustainable pace of growth. I would argue that is a soft landing, kind of what we all are looking for.

And one of the reasons is because I think we're going to continue to get some fiscal tailwind in the next year. And when I listen to both candidates, it seems like both of them are espousing pro-growth policies. And let's face it, no politician wants a bad economy. You always say that. So Harris just came out with the framework for her economic plan, a little more granularity, again. Huge disclaimer, like campaign rhetoric is not policy. I think we should all really remember that. Both good and bad. Am I wrong? What are you looking at for guidance for what we can expect out of fiscal spending next year?

[00:15:36] Jason Cole: Yeah. There's a lot to unpack there. I'd love this to be the headline for the podcast, because I feel very strongly about this. And that is Congress matters.

[00:15:48] Jason Cole: And that's from a person that spent 12 years in the United States House of Representatives. And so I've got a little bit of bias in this, but Congress matters in this process. With the exception of maybe trading, tariffs and that sort of thing.
But when we get into other fiscal policy and taxes, and by the way, taxes as everybody on this listening I'm sure knows, there's going to be a big tax debate in 2025 with the expiration of the TCJA or Trump tax cuts.

[00:16:16] Lara Rhame: Yeah, the Tax Cut and Jobs Act.

[00:16:18] Jason Cole: Tax Cut and Jobs Act. You know, those all expire on December 31, 2025. That creates a fiscal cliff for Congress, for whomever is the new president, that they're going to have to address over the coming year. And to your point, there have been a lot of things bandied about on the campaign trail by both candidates. The candy store is wide open and has been.

[00:16:46] Lara Rhame: That doesn't sound like a good thing.

[00:16:47] Jason Cole: No tax on tips. Outbidding each other on the child tax credit. [Former] President Trump reversed course on the state and local income tax deduction in Long Island last week. Harris, as you've pointed out, has a bundle of plans for home ownership tax credits for small business startup tax credits. I mean, the candy store is open.

[00:17:12] Jason Cole: But Congress has to be involved in that process when it's all said and done and supply the votes to move that policy. And so the makeup of Congress is going to be extraordinarily important in how that fiscal policy is going to shake itself out in 2025. There will be a tax debate.
The question is in our 50-50 probability world, Republican sweep, probably the path of least resistance is a lot of hand-wringing, a lot of debate, and maybe some nips and tucks, but ultimately at the end of the day, some form of extension of existing law. And again, some nips and tucks and whatnot.

I mean, I've had a lot of conversations with members of Congress around the tax on tips in particular. And there's a lot of head-scratching among members who actually have to write that policy on, how do you do that? And what's it look like? Where do you put guardrails? And so on and so forth. And so it's not evident to me that, even in a Republican sweep, that's something that could come to fruition. I think there'll be an effort to try to do it, but it's not evident to me there's a vote because there is bipartisan support for it.

And some of these other things, there's a growing populism in the Republican party. And so what we thought to be true in the past, lower taxes on corporations, for example, may not be true any longer because there is a growing sense on Capitol Hill, at least, certainly not on the campaign trail with the presidential candidates. But on Capitol Hill, at least there is a growing concern around the rising deficits and debt that could come to a head in 2025, as we begin having these fiscal policy discussions.

In a divided government, 50-50 probability, there will also be a debate around tax policy, but it will nibble a lot more at the edges of the TCJA, but I think it will preserve things like middle income tax rates. The upper rate goes back up 37–39.6. That's certainly more at risk than in an all Republican scenario. Corporate rate, I think, becomes more at risk in a divided government scenario. But there's going to be a debate and something that you and I are going to be able to talk about well into next year on these podcasts.

[00:19:34] Lara Rhame: The best thing you said was that there's growing concern from both parties about the size of the deficit. And, while I hate paying taxes, what I hear when I hear tax cuts is bigger deficits.

So, I think something I am very quick to point out when I have a lot of conversations about the election and the election outcome is that our deficit and debt dynamics have really hit a tipping point. The growing deficit is everybody's fault. It's everybody's problem. And I don't think either candidate...both parties have, over the last eight years, been responsible for just blowout deficits that have continued to grow.
That's something I'm hoping is on the radar.

I think another part of my forecast for next year is interest rates are...we've all heard the phrase hire for longer. I think the Fed wants to cut rates. They're going to be cutting rates, but in that long-term part of the yield curve, I think, we've probably seen the bulk of the long duration trade play out, and in a scenario where the economy does fine, we're going to get interest rates that are kind of at current levels or higher.
And I think the massive and soaring debt that needs to be refinanced and then increased deficits—given everything you're saying about policy proposals—to me is a higher-for-longer environment.

[00:21:13] **Jason Cole:** I totally agree with that. You're the economist at the table, but these policies are inflationary from both candidates.

[00:21:22] **Lara Rhame:** Right, and that's another piece of this.

[00:21:24] **Jason Cole:** And rates. That's going to put upward pressure on rates moving forward, unless there is a good dialogue about deficit and debt. There's one action-forcing event that will occur on January 1, 2025. The debt limit expires.

[00:21:44] **Lara Rhame:** Oh, so we're back to the debt limit expiring.

[00:21:46] **Jason Cole:** Under the June deal. Now, that's interesting timing, right. Because you have a president-elect, you have a Congress-elect, but neither of which are sworn in yet. And so, my thinking is that Secretary Yellen will be able to enact extraordinary measures to begin stretching things out. And the new Congress and the new president will have to deal with the debt limit in some form or fashion in 2025.

The extraordinary measures can probably take us into May. Maybe June. Depends on how receipts come in April, but there will be a conversation-forcing event in the debt limit, which we've talked about here before; the markets just love it. I say tongue fully planted in cheek, the issue will be a 50-50 probability, again, Republican sweep. I think the debt limit's a non-issue.

They extend it. Nobody wants it. They're in charge. They've got to deal with it. In a divided government situation, however, you have the opportunity where I think you see debt limit brinksmanship once again. But you also create a conversation around the need to address the deficit and debt, and perhaps you get some sort of deal. Not super optimistic about that, but I think it begins opening the dialogue.

[00:23:06] **Lara Rhame:** Well, the fact that you said that both parties are concerned, it's on the both of their radar.

[00:23:12] **Jason Cole:** So if you look at a radar as a bullseye, it's on the outer, outer, outer rings of the radar.

[00:23:19] **Lara Rhame:** Alright. Well, I think we are just about to enter October. October surprise. What's your prediction?

[00:23:27] **Jason Cole:** Well, it wouldn't be a surprise if I knew, but let me throw a few ideas out there. We continue to have problems brewing in the Middle East. It seems like we're on the brink of just ongoing escalation of the conflict, the war, whatever you want to call it there. Spreading now into Lebanon, Iranian proxies. What is it? What does that all mean? So I think that's issue one.

Two, you have Ukraine, Russia, that I'm not sure what the surprise is there other than maybe a very stern Russian incursion and offensive sometime in advance of the election that shines a spotlight on that to cast blame on the Biden administration for their handling there, could be in order.

The one that I'm watching is on Monday, September 30. I expect the whole Eastern Seaboard Longshoremen to strike.

[00:24:26] Lara Rhame: Oh, yeah. And supply chain disruptions.

[00:24:30] Jason Cole: And if that strike happens and if it's prolonged, enough that you start getting supply chain and movement in prices a week out from the election, that could be meaningful and something I may get to pay attention to. The president says he won't intervene. I'll take him at his word on that, and we will have to see how that plays out, but I think that's something to pay attention to.

And then, unfortunately, the big one is, there's a lot of foreign, state and non-state actors that want to influence our elections in one way or another.

[00:25:02] Lara Rhame: Sure, or just sow chaos.

[00:25:04] Jason Cole: Yeah, sow chaos. And that could go either direction. But it's something to be mindful of as we head into the silly season.

[00:25:13] Lara Rhame: All right. Well, let's do this in a couple of weeks when we're even closer to the big event. I think we will have a vice presidential debate by then that you and I can parse. And I think we're going to have another round of data. We'll have a Fed meeting coming up the day after the election or a Fed announcement. No shortage of new conversation topics related to this, because I think this is top of mind for every advisor that I'm meeting with. I can only imagine how busy you are, Jason.

[00:25:46] Jason Cole: Yeah. Thanks, Lara. This is great. And we'll see you soon.

[00:25:48] Lara Rhame: Thank you.

[00:25:49] Jason Cole: Yeah. Take care.