



Thanksgiving¹ Eye on the Market (updated November 20 for Wayne County news)

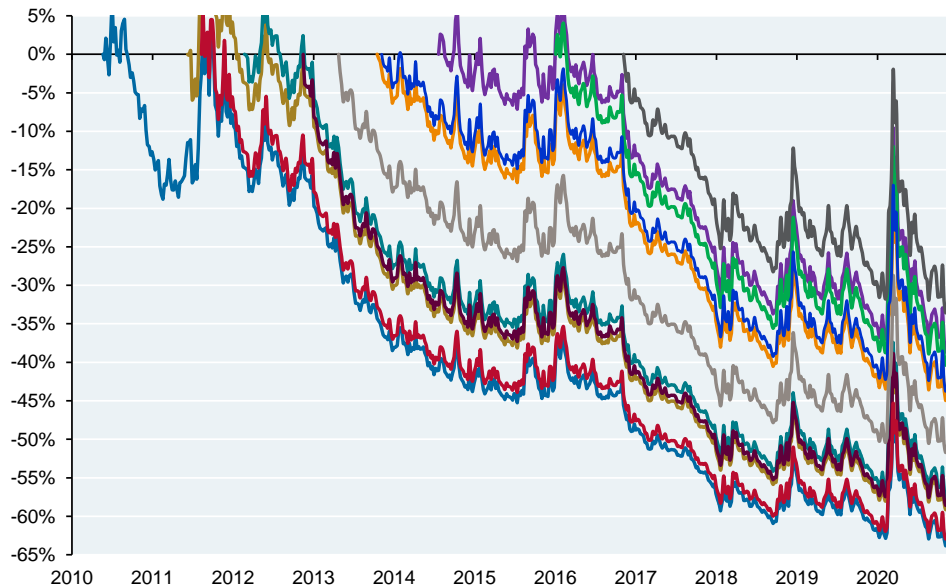
The Armageddonists were not rescued from underperformance purgatory by COVID, and markets are at all-time highs again with prospects for further gains in 2021. However, I can think of something that *could* rescue them, at least temporarily: the risk of electoral illegitimacy and Constitutional mayhem on January 6th. See pages 4-6 for a review of all the rules and procedures in play, including an update from Wayne County, MI

A year ago, I wrote about the “Armageddonists”: the market-watchers, forecasters and money managers whose apocalyptic comments spread like wildfire in print and online financial news. As we wrote last year, anyone who was underinvested since they listened to the Armageddonists suffered large opportunity losses from 2009 to 2019 given how well equity markets performed. You can read the original piece [here](#).

So, did COVID rescue the Armageddonists by finally causing the market collapse they had been anticipating? Not really. Even if we give them credit for including pandemics in their panoply of disaster scenarios, the March selloff did not erase the underperformance linked to their views. Furthermore, the 2020 equity market selloff was so quickly reversed that it would have taken an almost immediate rebalancing into riskier assets to partially recover prior losses. So no, COVID did not rescue the Armageddonists from underperformance purgatory, and now markets are at all-time highs again.

COVID did not rescue the Armageddonists from underperformance purgatory

Performance impact of shifting \$1 from the S&P 500 to the Barclay’s Aggregate Bond Index, measured from the week of the Armageddonist comment to November 13, 2020



How was the chart created?
We measured the impact on an investor that shifted \$1 from equities to gov’t, mortgage-backed and corporate bonds at the time of the Armageddonist comment. See original piece page 4, linked above, for comment archive.

- Simon Johnson & Paul Krugman
- David Levy
- Carl Icahn, John Hussman & George Soros
- Bob Janjuah
- Peter Schiff & Tom DeMark
- David Stockman & Albert Edwards
- Marc Faber & Laksham Achuthan
- Robert Wiedemer
- David Rosenberg
- Jeff Gundlach
- Nouriel Roubini

Source: JPMAM, Bloomberg. November 13, 2020. Using weekly S&P 500 and Barclay’s Aggregate data.

¹ There’s a hyperlink you may need if you are celebrating Thanksgiving this year with your relatives, either in person or remotely. See box on page 6.

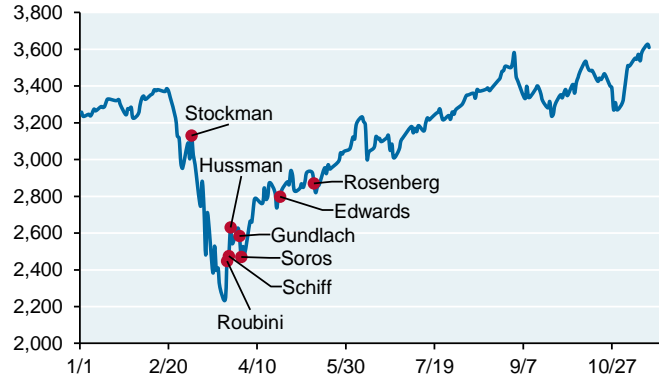


Unsurprisingly, the Armageddonists were at it again once COVID hit. The chart and table below show a selection of their very bearish quotes from earlier this year.



Timing is everything

S&P 500 index, Jan 1 2020 to present with date of latest comment



Source: Bloomberg, JPMAM. 11/17/2020. See quote table for full sources.

Date	Armageddonist	Quote
March 4, 2020	David Stockman	"The stock market is heading not only for another 50% correction (1600 on the S&P 500), but also a long L-shaped bottom rather than a quick V-shaped rebound which occurred after 2009." - <i>Published note on PeakProsperity</i>
March 24, 2020	Nouriel Roubini	"With the COVID-19 pandemic still spiraling out of control, the best economic outcome that anyone can hope for is a recession deeper than that following the 2008 financial crisis... The risk of a new Great Depression, worse than the original — a Greater Depression — is rising by the day." - <i>Published note on Project Syndicate</i>
March 25, 2020	Peter Schiff	"What the Fed is doing is extremely bearish for the U.S. economy... It ensures that this recession, depression that we're entering is going to be extremely brutal in the inflation that is going to ravage the economy, particularly investors and retirees." - <i>FOX Business</i>
March 26, 2020	John Hussman	"I continue to expect the S&P 500 to lose about two-thirds of its value over the coming years." - <i>Hussman Funds</i>
March 31, 2020	Jeff Gundlach	"The low we hit in the middle of March ... I would bet that low will get taken out... The market has really made it back to a resistance zone and the market continues to act somewhat dysfunctionally in my opinion... Take out the low of March and then we'll get a more enduring low." - <i>CNBC</i>
April 1, 2020	George Soros	"We're going to have the worst bear market in my lifetime." - <i>Business Insider</i>
April 23, 2020	Albert Edwards	"Many equity bulls think it is inevitable that massive central bank liquidity will boost equity prices. This strikes me as ludicrous... The collapse in profits is highly likely to fatally undermine the argument that equities can look through the valley. I expect instead ample liquidity to flow into government bonds." - <i>Business Insider</i>
May 12, 2020	David Rosenberg	"So even as the stock market is telling you that it is all figured out, I can assure you, what we face at this very moment is a highly uncertain economic future, and unfortunately, most of the longer-term risks are to the downside, not the upside. We are in a depression, not a recession. It's a depression. I didn't say the Great Depression; it's a depression," Rosenberg stressed. "And I think the dynamics of a depression are different than they are in a recession, because depressions invoke a secular change in behavior. Classic business cycle recessions are forgotten about within a year after they end. At a minimum, depressions entail a prolonged period of weak economic growth, widespread excess capacity, deflationary pressure and a wave of bankruptcies." - <i>Advisor Perspectives</i>





Why did Armageddonist-driven portfolios underperform?

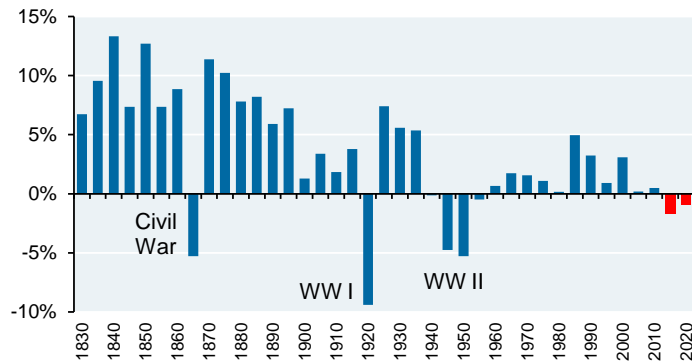
Fiscal and monetary stimulus explain a lot. The last decade has seen the longest period of negative real policy rates in recorded US history, other than during the Civil War, WWI and WWII. More recently, COVID stimulus was 2x the levels provided during the Financial Crisis, and was delivered 4x faster. Other factors that partially explain the speed with which bear markets are reversed: the technical shortage in US publicly traded equities, since M&A activity and buybacks outweighed primary and secondary issuance (third chart).

While stimulus helped, profits have been more resilient to COVID than Armageddonists may have expected. In Q3 2020, earnings beat expectations (-8% vs consensus -25%), with airlines, other travel-related businesses and energy accounting for almost all of the earnings contraction in the quarter. Free cash flow for the core of the market (excl. financials, REITs and energy) was actually *up* in Q1, Q2 and Q3 of 2020. At the current pace of improvement, S&P 500 EPS should exceed pre-pandemic levels by the end of 2021.

Despite the latest surge in infections² and mortality in the Developed World, **we anticipate a further recovery** in consumption, inventory demand, capital spending and corporate profits in 2021, fueled by central banks purchasing *another* \$3-\$4 trillion in assets and by the eventual impact of vaccines³ on labor force participation and mobility. If so, portfolios would continue to benefit from normal allocations to risky assets.

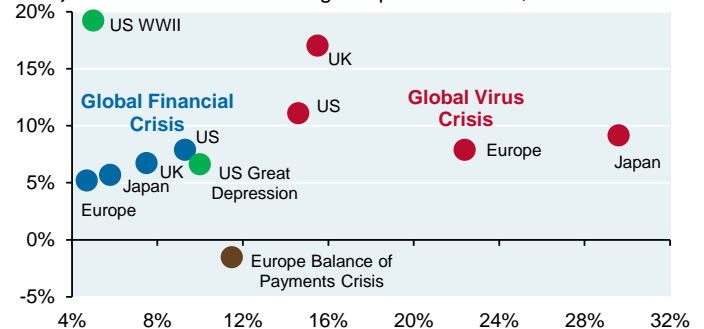
However...I can think of one thing that *could* rescue the Armageddonists, at least temporarily: an unorthodox US transition of power that is seen as unlawful by the markets. That’s what we discuss next.

Lowest real yields on cash since 1830, other than during wartime, T-bill/Funds rate less inflation, 5-year average



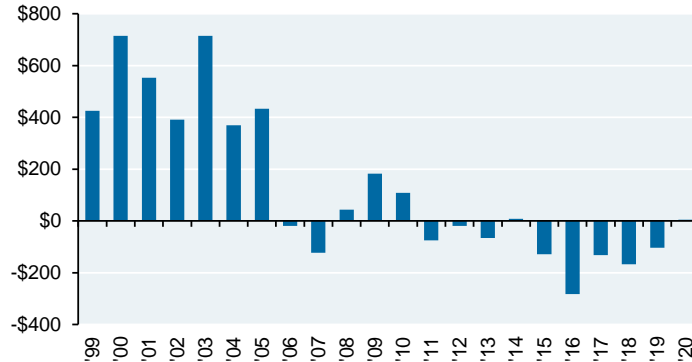
Source: FRB, Robert Shiller, GFD, BLS, JPMAM. October 2020.

Debt monetization response to GVC eclipses everything else, Govt. fiscal deficits: change vs pre-crisis level, % of GDP



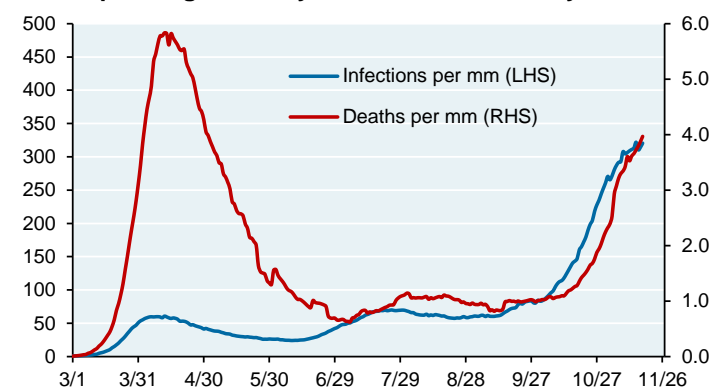
Central Bank balance sheets: change vs pre-crisis level, % of GDP
Source: Central bank sources, OMB, St Louis Fed, JPM Global Economic Research, JPMAM. November 2020. GVC = Global Virus Crisis.

Unprecedented low levels of net US equity supply
US\$ billions, based on MSCI All Country World Equity Index



Source: JPM Global Markets Strategy. October 2020.

Developed Regions daily infections vs mortality



Source: JHU, JPMAM. 11/17/2020. 7 day avg.

² Michigan now has 7x more infections than in March, and hospitalizations/mortality are rising sharply. Radiologist and Trump coronavirus expert **Scott Atlas** responded to renewed restrictions in Michigan with this medical recommendation: “The only way this stops is if people rise up. You get what you accept”. Only the best people!

³ Pfizer and Moderna have announced successful Phase III trials results; NovaVax, J&J and AstraZeneca may soon follow.



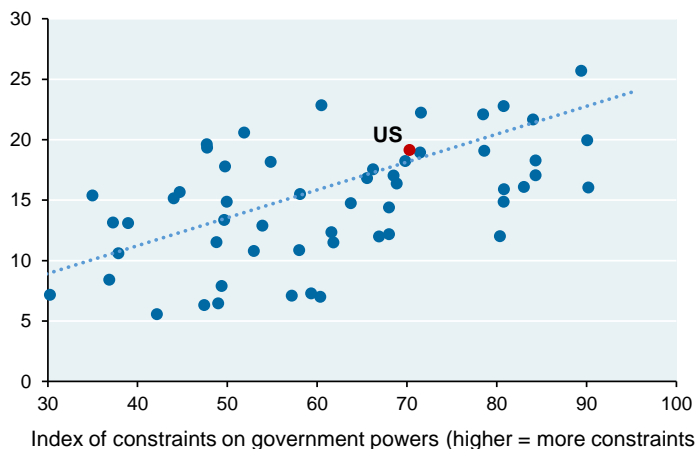


The remote risk of an American Horror Story: Constitutional mayhem on January 6th

Democracies can/should enforce the rule of law to ensure that only lawfully cast ballots are counted. However, **the devil is in the details of how this is achieved**; markets might react negatively if the US as the world’s reserve currency nation is seen as sliding down a path toward electoral illegitimacy due to post-election maneuvers by political parties. In the chart, we show equity market valuations vs constraints on government power. **A modest decline in the rule of law, if it cost 3x-4x multiple points on earnings, could result in a de-rating of US equities.**

Countries with more constraints on government power tend to trade at higher valuations

Equity market P/E ratio



Constraints on government power index:

- Government powers are limited by the legislature
- Government powers are limited by the judiciary
- Government powers are limited by independent auditing and review
- Government officials are sanctioned for misconduct
- Government powers are subject to non-governmental checks
- Transition of power is subject to the law

Source: n=67 countries. World Economic Forum, World Justice Project, MSCI, Factset, JPMAM. November 2020.

The Constitution, the Courts, the Congress, electoral fraud allegations and a hyperlink for Thanksgiving

- **Could one or more states submit competing slates of electors?** Only North Carolina expressly grants the legislature a role in certifying electors. Other legislatures, despite constraints in their state constitutions and statutes, might assert authority to act under Article II of the Constitution and submit a competing slate of electors. While there’s no explicit authority granted to them to submit competing slates, a Governor or Secretary of State could *also* submit one. Competing slates contrary to the popular vote could be invalid under the federal Election Day statute, and may violate voting rights the Supreme Court recognized in Bush v. Gore. **Competing slates are extremely rare:** it only happened once in the 20th century (Hawaii, 1960)
- Competing slates would be dealt with via rules spelled out in the **Electoral Count Act (ECA)** of 1887: on January 6th, the newly seated Congress would resolve them. In case of a split Congress, the prevailing view is that ECA tiebreaker rules generally require Congress to adopt whichever slate was signed by the Governor of the state in question. Governor affiliations: Democrats in MI/PA/WI/NV, Republicans in GA/AZ
- US-China historian Graham Allison wrote that **the GOP could declare the ECA unconstitutional** on the grounds that federal statutes cannot constrain the power the Constitution grants to chambers of Congress to count and determine validity of electoral votes. As the argument goes, counting must proceed under the 12th amendment, and if the House and Senate disagree on competing slates, VP Pence (as presiding officer of the joint session of Congress in which electoral votes are counted) **could cast the deciding vote**. In the nightmare scenario for markets, the ECA is jettisoned by the Senate, the GOP declares Trump as the victor by flipping 3 states, Democrats disagree and refuse to participate in the Jan 6th session, all of which sets up the prospect of dueling inaugurations, an outcome narrowly averted in 1876 and which led to the 1887 Act
- **Allison’s scenario assumes that Senate Republicans discard the ECA**, despite the fact that it was created to address competing slate outcomes. In any case, let’s do the math: due to Senate seating rules, its composition on Jan 6th will be 51-R and 48-D, since one Georgia runoff election will not be seated yet and the other will still be GOP irrespective of the outcome (since it was a special election). **So, if 2 or more GOP Senators respect the ECA when resolving competing slates, Gubernatorial tie-breakers would remain**



- **Breaking news: the risk of canvassing board rejections of the popular vote**
 - Wayne County’s Board of Canvassers was deadlocked since 2 GOP members refused to certify; then they certified; and then announced that **they rescinded prior certifications** since the Michigan Secretary of State had not pledged to conduct a full audit. Note: Biden appears to have won Wayne County by > 30%, and Wayne County GOP canvassers are refusing to certify based on reportedly minor discrepancies; if so, this would be one of the more transparently partisan acts of gov’t I can recall
 - **The State Canvassing Board can ignore the Wayne County results and still certify the state’s results.** However, if the State Canvassing Board does NOT certify or is deadlocked, an old Michigan state law appears to allow the state legislature to make the decision instead. The State and Wayne County Canvassing Boards could be required by State Courts to certify if their reluctance to do so is based on factors outside the scope of its review powers, but that would require a judgment call by the courts. Breaking news: the GOP leaders of the Michigan legislature are flying this week to meet with Trump
 - However, even if the State Board certifies willingly or from a court order, this same state law still appears to allow the legislature to assume responsibility for resolving the election if “results are contested”. The law is written in the passive voice and does not specify who is doing the contesting, but case law dating back 100 years indicates that all a losing candidate or dissenting member of the State Board of Canvassers would have to do is contest the outcome and the decision could be thrown to the legislature
 - **If it went this far, it would probably come down to a Michigan Supreme Court ruling on the old state law.** Federal courts could get involved, but outcomes would be murky given Constitutional constraints on federal courts from getting involved in election decisions by state legislatures
- Another remote risk: Attorney General Barr could in theory direct investigators to **seize or impound election records** to investigate voter fraud, which would slow down canvassing and recounts. Usual DoJ policy would hold off until after the election is settled before investigating fraud for prosecution or civil enforcement proceedings. But if this happened, it could prevent a state from meeting the Dec 14th Electoral College deadline. However, states have already begun to certify results and once results are certified, even if DoJ seizures interfere with recounts, initial certifications would likely stand as the basis for appointing electors
- On **recounts**, Georgia’s is completed with no material changes to results; Trump may now request a *second* recount conducted via high-speed scanners. Recounts might also be requested and conducted in Pennsylvania (Biden +0.8%), Wisconsin (Biden +0.7%) and Nevada (Biden +2.7%). Historically, recounts have not changed outcomes with margins this large
- **Bottom line: a LOT of very unorthodox things have to happen for Trump to remain President after January 20th. Based on the uncertified vote results, Trump would have to reverse or impede results in three states to prevent Biden from reaching 270 electoral votes (EV).** Biden unofficially has 306 EV, so Trump would need to flip three states via one of the avenues described above (see table on following page for EVs by state and other data)
- **How remote are these risks?** Ed Foley of Ohio State (the constitutional election law expert cited by Allison) wrote his *own* article last week entitled “*Relax. Biden will be sworn in on Jan. 20*”, and another expert that I have been working with agrees with him. Among their arguments: the high hurdle needed to prove sufficient levels of unlawful ballots for courts to set aside the outcome in that state
- **Even so, I’m not ruling anything out.** Trump **fired the top US election security official last night**, and his campaign lawsuits are petitioning judges to prevent state certification of results due to fraud and other improper conduct. The RNC hasn’t signed on to many of these lawsuits, and some Trump law firms are reportedly abandoning him. But anything is possible, particularly since a senior DoJ official who oversees voting investigations stepped down from his role after Attorney General Barr authorized US attorneys to probe alleged fraud. The departing DoJ official stated to colleagues that the **new DoJ policy abrogates the forty-year old Non-Interference Policy for ballot fraud investigations**



I have not mentioned **Contingent Elections**, since most scenarios I can think of entail one candidate or the other reaching 270 EVs; and/or since if any state’s EVs are not submitted by the December 14th deadline, such EVs would most likely be removed from the numerator *and* denominator of the Electoral College equation. As a result, a candidate would need to obtain a simple majority of all remaining EVs to win.

What about the Supreme Court?

- First, the Court might be able to hear appeals on **state challenges**, such as late-arriving absentee ballots in PA (too few to change the outcome); complaints on transparency of vote counting (judicial relief could entail recounting certain counties); illegal acceptance of certain votes (votes in question too small to change the results); and complaints that the voting process suffered from pervasive irregularity and fraud (most of these claims have been rejected by lower courts over the last 2 weeks). However, many election disputes are resolved by state courts and cannot be reviewed by the U.S. Supreme Court
- Second, **what if the Court heard a challenge to constitutionality of the ECA?** Such a lawsuit would probably fail: the ECA does not violate the rights of any person in particular, therefore no one has standing under Article III of the Constitution to contest it. Furthermore, since the Constitution grants sole authority to chambers of Congress to count and determine the validity of electoral votes, a federal court (including the Supreme Court) lacks jurisdiction under the Political Question Doctrine to constrain Congressional authority

I’m not going to comment on likelihood of pervasive fraud; the courts will rule on that. I will say this: in February 2020, Senate Republicans blocked bills related to election security, including election security funding and a proposal to ban voting machines from being connected to the internet. At the time, there were 10 other election security bills that McConnell was also blocking (**this election is delivering an unending stream of Schadenfreude**). Also, **my brother in-law** has been sending me videos and links to “internet news sources” asserting “proof” of widespread fraud from election hackers. I spent a few hours of my life that I will never get back responding to him with sources clearly refuting these theories, but I’m not sure it will make much of an impact on him. If you have to deal with family members like this at **Thanksgiving**, here you go: <https://www.factcheck.org/2020/11/bogus-theory-claims-supercomputer-switched-votes-in-election/>

Sources and articles cited

I’ve been working with Michael Morley (FSU), who teaches and writes in areas of election law, constitutional law, federal courts, election emergencies, post-election litigation and defendant-oriented injunctions

“Donald Trump’s Stealthy Road to Victory”, Graham Allison (Harvard) in *The National Interest*, 11/6/2020

“Relax. Biden will be sworn in on Jan. 20”, Edward B Foley (Ohio State), Washington Post, 11/11/2020

Party affiliations of key state entities

State	Governor	State Legislature	Secretary of State	Electoral Votes	Certification Deadline
AZ	R	R	D	11	Nov. 30th
GA	R	R	R	16	Nov. 20th
MI	D	R	D	16	Nov. 23rd
NV	D	D	R	6	Nov. 24th
PA	D	R	D	20	Nov. 23rd
WI	D	R	D	10	Dec. 1st

Source: NCSL, National Association of Secretaries of State, Washington Post. November 2020.



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