# CIO VIEW SPECIAL

**U.S. elections 2020**

# EVERYTHING WILL BE OBVIOUS, ONCE YOU KNOW THE ANSWERS

//DWS

# U.S. elections 2020: Everything will be obvious, once you know the answers

## The upcoming U.S. elections could be remembered as the most important since 1980.

_ In our base case scenario, we see a 60% probability of Biden winning the Presidency and a 42% chance for Democrats winning the Presidency and both Houses of Congress. That leaves a divided government the most likely overall outcome.

_ We also explore some of the many long shadows that former President Ronald Reagan's victory in 1980 continues to cast.

_ Can the United States still govern itself? On this, we remain cautiously optimistic, in this unusual election year.

Johannes Müller
Head of Macro Research

Peter Doralt
Political Analyst,
Macro Group

### IMAGINE THE SCENE

Inside the Oval Office in the West Wing of the White House, the President and his closest advisers are huddled together. There is only a year to go until the President's re-election bid. The polling picture is mixed at best. Then again, they have come from behind before. Their win last time around? It took everyone inside the Washington beltway by surprise. First the primaries, then, the general election! Not just the pundits. The party's establishment too. Such an unusual and conservative candidate, the whisper campaign amongst party elites went. Anybody but him, became the battle cry of his last remaining opponents in the primaries. The establishment figures did what they could to stop him. But it was already too late. The ordinary voters had spoken. Not that it seemed to matter to some very influential people, within his own party!

Heck, throughout the President's first term in office, some of the old guard never stopped grumbling. No matter what the Administration did. Sure, there had been hiccups. Bureaucrats, who resisted. But that was to be expected. The President, after all, had run as an outsider. He **was** inexperienced in the ways of Washington. The President and his new Chief of Staff (and erstwhile campaign mastermind) would be the first to admit that. That, however, seemed to be exactly what voters had liked about him. A reformer untainted by Washington political scandals.

With one more year to go, the President and his team feel quietly confident they can do it again. Which is when a crisis of epic and previously almost unimaginable proportions hits. Changing everything. From then onwards, the President later tells his Chief of Staff, "it was one crisis after another."

Well, in fact, you do not have to imagine it. The year in question is history – ancient history, in fact, for those approaching middle age in 2020. And fortunately, the President's key advisor, strategist and White House Chief of Staff at that time, Hamilton Jordan has left us with a vivid account of how that year unfolded, largely based on contemporaneous notes. Written in an age before such memoirs became popular, Jordan's "Crisis: The last year of the Carter presidency"[1] is nevertheless a page turner. It is the first of several book recommendations we will share in this CIO Special and ends (spoiler alert) when Ronald Reagan and his team arrive at the White House on January 20, 1981. Jordan is aboard Air Force One at the time, still very much involved in the Iranian hostage crisis that followed the Islamic revolution in Iran and the fall of the Shah. (The second major crisis that year was the Soviet invasion of Afghanistan.) During a call, he suddenly realizes that Carter is no longer president, a new team is now in charge and Jordan is out of a job.[2]

The elections of 2020 may be unusual in many ways. And yet, our working assumption in putting together this CIO Special is that it will be followed by just another presidential inauguration, in the long line of office-holders dating all the way back to George Washington on April 30, 1789. The current incumbent will either be re-elected or there will be a peaceful transfer of power.

Given the Covid-19 pandemic, it might take a little longer than usual to get the election results, but as we will see, the very idea of knowing who has won on election night is a surprisingly recent development. If the race for control of the Senate is tight, it may take until after January 5, 2021, until there is a clear idea how the new, or the old, administration will govern. All of this should normally go without saying. This will hopefully be the last time we have to issue such a disclaimer when covering an election in the United States.

Finally, a few words on what else this CIO Special will and will not try to cover. Back in 2016, we put together a similar document. It covered how the U.S. political system works, demographic trends and why investors should not put too much stock into campaign promises, especially when it comes to the implications for specific sectors. New administrations tend to take a while to get up and running. Policy priorities change as events intervene. And, as far as legislation or budgets are concerned, nothing much can happen without Congressional action. Our 2016 CIO Special[3] also explained in some detail how U.S. politics evolved since the 1980s and why gridlock had become such a constant complaint. None of these longer-term, structural features has changed all that much. So, rather than cover the same ground once again, we will repeatedly refer to it, when highlighting things we have learned since.

Similarly, we put together an early roadmap to U.S. politics in 2020 and beyond back in January of this year.[4] Among other issues, it analyzes the 2016 results, explains why you can (and should) trust U.S. pollsters and highlights some of our favorite sources of information and indicators worth monitoring. For the present document, we will occasionally quote from it at length, to illustrate how our thinking has evolved.

To conclude this introduction, we should note that this CIO Special only marks the starting point for our campaign coverage of this year's U.S. elections. We are also planning to comment on events on a weekly or biweekly basis from now on, leading up to the elections. As a result, the rest of this CIO Special will largely stay clear of individual Congressional races we are watching. Instead, it is an early attempt to put this year's elections in a historical context. 2020, we think, will probably be remembered as the most important election year since... well, 1980.

---

[1] Jordan, H., 1982, Crisis: The last year of the Carter presidency, G.P. Putnam's Sons
[2] Due to Covid-19, the main author has been cut off from some of the sources mentioned since the start of March and is quoting from memory. Apologies if we got any details wrong.
[3] https://www.dws.com/insights/cio-view/emea-en/our-us-election-watch-2016-09/
[4] https://www.dws.com/insights/cio-view/macro/an-early-roadmap-to-us-politics-in-2020-and-beyond/

## 1. 2020 AS A YEAR OF **NO** SURPRISES (YES, YOU READ THIS CORRECTLY)

Looking back at the political year so far, perhaps the most surprising thing is how little surprises you can see when you look at our forecast for the U.S. presidential election. At the start of the year, it gave President Trump a 40% probability of being re-elected, his Democratic challenger 50% and another Republican or third-party candidate 10%. The current numbers, not including any lasting convention bounce for either ticket, are President Trump 35%, former Vice President Biden 60% and "Other" including third party 5%.

There has been a bit more movement in our Congressional forecast. Notably, the likelihood of what we called a "Trump Triumph," in which Republicans win both Houses of Congress, has gone down from 20% to 8% now. Meanwhile, the chances of a similar Democratic sweep – winning the Presidency and both Houses of Congress – now stands at 42%, compared to 15% in February. Politically, the biggest surprise so far has been Biden – an also-ran in the first three Democratic primary contests – winning the nomination.

The race so far remains consistent with our base case, which we described back in January as the "Mushy Middle," limiting the implications for individual sectors.[5]

You can find an overview of our current thinking on the various possible outcomes below.

**ELECTION-OUTCOME PROBABILITIES (DWS EXPECTATIONS)**



| | BIDEN 60% | | | | TRUMP 35% | |
|---|---|---|---|---|---|---|
| **Probability** | **House of Representatives** | **Senate** | | **Probability** | **House of Representatives** | **Senate** |
| **42%** | **DEM** | **DEM** | | **24%** | **DEM** | **REP** |
| **15%** | **DEM** | **REP** | | **8%** | **REP** | **REP** |
| **3%** | **REP** | **REP** | | **3%** | **DEM** | **DEM** |
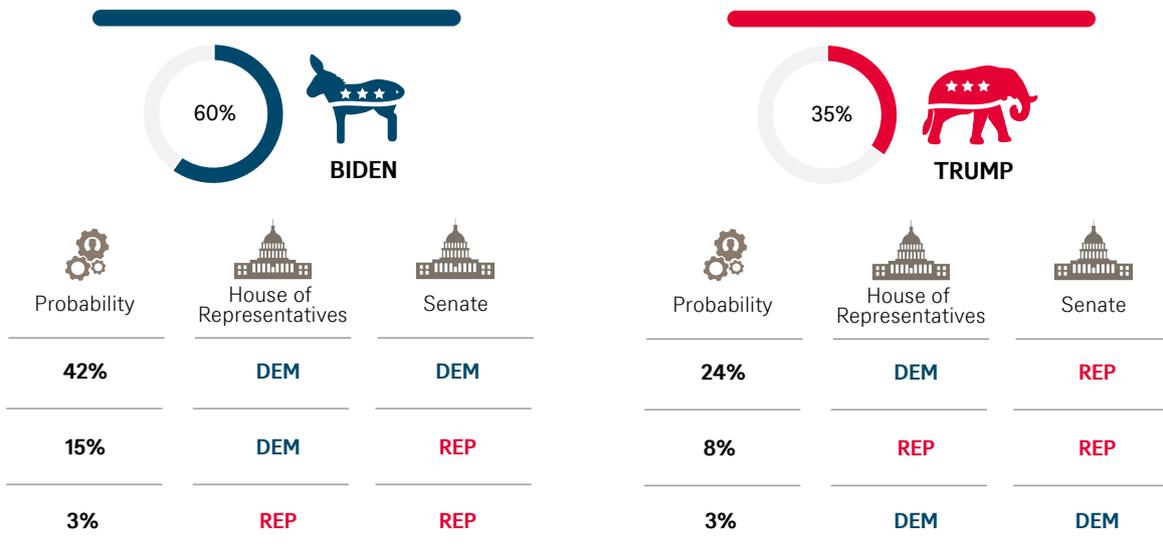
Probabilities for Biden and Trump add up to 95%, the remaining 5% mainly account for the small chance that one of the candidates becomes sick.
Source: DWS Investment GmbH as of 9/1/20

The numbers should be taken as indicative only. A lot can still change. Indeed, as we pointed out back in January, "a good, initial approach – at least until Labor Day 2020 – might well be not to get carried away by political headlines."[6]

Still, if you had told us back in December 2019 about the news events ahead – or simply shown us a chart of either the U.S. stock market or consensus forecasts for U.S. economic growth in 2020 – we would certainly have expected more volatility in both our forecast and in U.S. polling.

---

[5] Though, as we noted back in January, "For political aficionados and fracking businesses alike, there is obviously a world of difference between the current status quo of a Republican president facing a Democratic House of Representatives, and, say, the prospect of a newly elected President Joe Biden rolling back Trump-era deregulation measures." See: https://www.dws.com/insights/cio-view/macro/an-early-roadmap-to-us-politics-in-2020-and-beyond/

[6] https://www.dws.com/insights/cio-view/macro/an-early-roadmap-to-us-politics-in-2020-and-beyond/

Back then, we did not know much about corona viruses, epidemiology, or how a contagious disease eventually dubbed Covid-19 was going to upend the lives of pretty much everyone on the planet. We did know, though, that with almost a year yet to go until Election Day 2020, our forecast should leave scope for the unexpected to happen. We also knew from experience what indicators to watch out for, notably presidential approval ratings and the generic Congressional ballot. And, we knew or at least had some idea in advance what, if any, changes in our forecasts might result from events impacting the polling data.[7] That is very useful, because it can mitigate against over- or underreacting to events.

As it turned out, 2020 thus far has offered plenty of surprises in terms of news events, but very little in the actual polling data. If you compare polling during this current election year to previous ones, the most surprising and remarkable thing is how unsurprising it looks in the polling. An unpopular incumbent is steadily losing ground against the other party's candidate between the primary contests and Labor Day. On the FiveThirtyEight weighted polling average, Joe Biden was leading Trump by 3.8% in late February. Bar a small tightening to 3.4% in the middle of April, Biden's lead has slowly but very steadily been growing, and is now, 5 days after the Republican convention, at 6.9%.[8]

**NATIONAL POLLING AVERAGES TRUMP VS. BIDEN**



Lead (right axis)   Biden   Trump

Source: FiveThirtyEight, DWS Investment GmbH as of 8/31/20

Finally, a few words on how our forecasting methodology compares to other, more complicated models you might come across ahead of the 2020 U.S. elections. For this presidential election The Economist has developed an especially interesting one, with a few bold methodological choices.[9] Their model currently has Biden at 86% and Trump at 13% (compared to 60% for Biden and 35% for Trump in our forecast). So, who is "right" and who is "wrong?" Well, when one thinks about it, this is actually quite a difficult question. If the election was held next week and Trump were to win, that would certainly look "bad" for The Economist. But one would need to run the election many, many times, to know whether a forecast was actually "wrong" in any statistically meaningful sense. The more interesting question, would be why they got it "wrong."[10]

Another issue is that different forecasts of the same event can serve different purposes. Our initial goal and task has been to forecast electoral events around the world up to twelve months ahead of time for our quarterly investment-strategy process. As a result, we ideally do not want big movements in our forecasts and also need to use our resources sparingly. Therefore, our forecasting methodology is mostly driven by relatively simple and stable measures such as the generic Congressional ballot discussed above and a handful of other indicators, mostly based on polling and past electoral events.[11] Polling on head-to-head matchups between the two nominees only gains greater weight as Election Day approaches. It is thus partly by design that forecasts have been less volatile.

By contrast, news outlets have very different incentives. We all want to be "right" on election night, to be sure. But news outlets also want readers to regularly return to the site. As a result, their forecasts tend to be sensitive to incoming polling data. There will probably be even more volatility this time around. That is one of the great joys of thinking about U.S.

politics in the 2010s. Over the past 15 years, a vibrant community of data-driven analysts, scholars and commentators interested in electoral forecasting has emerged. Every time, we learn new things, some of them very helpful in improving our forecasting efforts subsequently in other countries, too.[12] The model Nate Silver has developed and continues to improve with every election cycle for FiveThirtyEight is probably the best example for the continuous development of electoral forecasting.[13] As we previously pointed out, their modelling and commentary has a solid track record over different cycles and races and is well worth checking on a regular basis.[14]

---

[9] For details, see https://www.economist.com/united-states/2020/06/11/meet-our-us-2020-election-forecasting-model

[10] Perhaps, they relied too heavily on past statistical correlations between economic fundamentals in general and voting behavior, which turned out to be less stable this time around? Or maybe they should have used different economic indicators, but instead relied too heavily on particular ones that just happened to fit the past data well? That can be a big problem in forecasting U.S. elections, because there are not all that many relevant electoral data points, but a lot of indicators you can potentially fit them to. Every single time, there are also (sometimes fast, sometimes slow) changing electoral coalitions, different candidates, campaign strategies, and potentially relevant news events and potentially co-dependent variables, such as stock-market expectations of electoral outcomes, in turn driving stock prices ahead of Election Day (see Section 4. below).

[11] For further details on our forecasting approach for U.S. elections see
https://www.dws.com/insights/cio-view/macro/an-early-roadmap-to-us-politics-in-2020-and-beyond/

[12] For example, partisan non-response biases in polling are a big issue in other countries (probably a bigger problem than in the U.S.), so it is of interest to us how U.S. modelers try to deal with them.

[13] For details, see https://fivethirtyeight.com/features/how-fivethirtyeights-2020-presidential-forecast-works-and-whats-different-because-of-covid-19/

[14] We admit that when it came out (9 months after we started sharing our forecast internally), we were somewhat relieved to find ourselves in the roughly same neighborhood.

## 2. THE PITFALLS OF COMMENTING ON HISTORY, AS IT HAPPENS

When it comes to electoral forecasting, one of the most important insights is that the human mind is subject to all sorts of cognitive illusions. Notably, it "makes up narratives about the past" and has the strong "tendency to revise the history of one's beliefs in the light of what actually happened," as Daniel Kahneman (2011)[15] puts it.

"Everything is obvious, once you know the answer," the sociologist and data scientist Duncan Watts (2003)[16] warns in his book of the same title: "common sense and history conspire to generate the illusion of cause and effect where none exists (...) history obligingly discards most of the evidence, leaving only a single thread of events to explain. Common sense explanations therefore seem to tell us **why** something happened when in fact all they're doing is describing **what** happened." This is why "history cannot be told while it's happening."

Which is a bit of a problem if, as in the present publication, you are trying to write about events that are still unfolding, without knowing all of the answers yet, obvious as it might seem with the benefit of hindsight. However, there are some mental habits that can help. The most important one is to become aware what is happening inside your mind, while you are thinking. "You build the best possible story from the information available to you, and if it is a good story, you believe it. Paradoxically, it is easier to construct a coherent story when you know little, when there are fewer pieces to fit into the puzzle. Our comforting conviction that the world makes sense rests on a secure foundation: our almost unlimited ability to ignore our ignorance."[15]

So, when faced with a tricky forecasting task, it is generally a good idea to be modest and cautious in how confident you should be in your ability to get it right. Statistical base rates can be an especially powerful tool to avoid overconfidence. Base rates indicate probability based on the absence of other information. In the context of U.S. presidential elections, the base rate of either one of the two major party nominees winning

has historically been about 50% (with only minor variations, depending on what time horizon is being considered). That makes sense because in a two-party system, you would expect both parties to nominate candidates and tailor their platform to have a decent shot at winning. Of course, that is no guarantee they will succeed in any given year. Events, from scandals to foreign crises, might intervene. But if asked to make a prediction well ahead of time – a year out, say – it is generally a better idea to stay close to historical base rates and have a healthy skepticism of narratives you find convincing.

Next, you should find out more about the specific case you are trying to forecast and look for similar past events. There may not have been a global pandemic to impact the polling data, but what about floods, hurricanes, nuclear disasters, wars or hostage situations? Ask yourself not just what past events might be similar, but also why past events impacted the polling and ultimately the electoral prospects of an incumbent party or candidate the way they did. Does it make a difference, for example, if voters already disapprove of an incumbent despite the economy doing well and few, if any, natural disasters or large international crises having happened under his or her watch? How sensitive should the electoral forecast be to events turning out better (or worse) in the weeks or months leading up to Election Day than the current situation, as already reflected in the polling data? Maybe there are things that can be learned from opposite instances in the past, too. An incumbent, say, who was personally popular and considered trustworthy, but still had high disapproval numbers in the polling, because voters doubted he was doing a good job on the economy.

That is how back in late 2019, we first started to think that 1980 might provide some interesting comparisons. Among his predecessors since modern polling began, Donald Trump is very unusual in having very stable approval and disapproval ratings. More specifically, he is the only one who, since the middle of February 2017 (a mere three weeks into his term) has consistently had disapproval ratings above 50%, bar two brief blips (one in March 2017 and one in April 2020).[17] Even if you just consider the last two years of Trump's term, there is only one predecessor with disapproval ratings almost as dismal: Jimmy

[15] Kahneman, D., 2011. Thinking, fast and slow. Farrar, Straus and Giroux; 1st Edition, pp. 202
[16] Watts, D.J., 2011. Everything is obvious: Once you know the answer. Crown, p. 122, italics in the original
[17] https://projects.fivethirtyeight.com/trump-approval-ratings/?cid=rrpromo
    which helpfully lets you compare presidential approval, disapproval and the net between the two since Harry Truman at this point in the Trump presidency.
[18] On the role of third party candidates in both 2016 and 2020, also see:
    https://centerforpolitics.org/crystalball/articles/why-2020s-third-party-share-should-be-lower-than-2016/
[19] All historical data is based on the information released by the Federal Election Commission, available at:
    https://www.fec.gov/introduction-campaign-finance/election-and-voting-information/

Carter in 1980. George H. W. Bush only comes close towards the end of his term (before losing to Bill Clinton in 1992). Barack Obama, George W. Bush and Bill Clinton, by contrast, while occasionally quite unpopular, kept their disapproval ratings below 50%, bar the occasional blip. To us, that looked like a big warning sign for team Trump.

After all, as described in the roadmap, his 2016 success was partly due to third-party candidates: "15 contests went to a "winner" of less than 50% of votes within those states or districts. Those contests accounted for 157 electoral votes out of 538, i.e. easily enough for an Electoral-College "landslide" of either Clinton or Trump. In those 14 states, as well as Nebraska's second Congressional district, both Trump and Clinton were so unpopular that enough voters decided to instead vote for independent or third-party candidates to deprive them both of a 50% win."[18]

That meant that unlike most of his predecessors, Trump did not have majority support in many of the states that propelled him to victory in the Electoral College. "Statistically speaking, Trump can be classified very much as an accidental president. In Michigan, Pennsylvania and Wisconsin, the three states that propelled him to victory in the Electoral College, he was ahead by a mere combined 78,000 votes (or 0.56%) out of 14m votes cast in those states."[19]

Of course, a similar claim can be made about George W. Bush's victory over John Kerry in 2004. Kerry "got into spitting distance of winning the presidency, despite lagging Bush by more than 2% in the popular vote."[20] Indeed, as one alert reader reminded us after the piece was published, a mere 50,000-vote swing in Ohio would have been enough for John Kerry to win the White House.

These specific cases underscore four things. First, winning re-election has been far harder for President Trump's immediate predecessors than we tend to think with the comforting benefit of hindsight. Second, it would be foolish to discount the role of luck. Since 2007, a series of papers have explored the impact of weather patterns, for example, in the U.S. and a number of other countries.[21] Third, campaigns appear to make a big difference in helping even an unpopular (but not too unpopular) incumbent like George W. Bush or Barack Obama win, perhaps by defining their opponent early on.[22] Fourth, though, there might be a point of presidential disapproval at which re-election is really hard, and exploring Carter's ultimately doomed 1980 re-election bid might help us identify it, or at least what to watch out for.

[20] https://www.dws.com/insights/cio-view/macro/an-early-roadmap-to-us-politics-in-2020-and-beyond/
[21] Gomez, B.T., Hansford, T.G. and Krause, G.A., 2007. The Republicans should pray for rain: Weather, turnout, and voting in US presidential elections. The Journal of Politics, 69(3), pp.649-663.
[22] See: Issenberg, S., 2013. The victory lab: The secret science of winning campaigns. Broadway Books on how the Obama campaigns pioneered the use of data analytics.

## 3. HOW REAGAN WON IN 1980 AND WHY IT MATTERS FOR 2020

Based on what has historically tended to happen in the final months of a campaign, we would expect the 2020 polls to at least tighten somewhat. With the benefit of hindsight, pundits might blame any such tightening, perhaps followed by a widening, directly on the effects of Covid-19, the economic downturn or the ongoing protests since the death of George Floyd. However, we think there might be another important mechanism to keep in mind in 2020: what rolling crises do to the capacity of an incumbent president to run an effective re-election campaign.

One of the reasons – more of a hunch really – why, as the year 2019 ended, we increasingly found ourselves thinking of 1980 was that it was the last time a new administration had encountered a series of crises late in its term. Michael Lewis, American author and journalist, had just written another book, this time about the Trump Administration's botched presidential transition and how critical government infrastructure was falling into disarray and dysfunction. According to him, the Trump Administration appeared dreadfully unprepared, with many critical agencies being run by political appointees without experience in the field. Or, they were not being run at all, because nobody had been appointed yet. If some disaster were to strike requiring quick and thoughtful government action – stopping a virus, say, from causing an epidemic – the results could prove catastrophic, Lewis warned.[23]

But how sure can we be that the same might not have been said about at least some previous, inexperienced new administrations as well during their first term in office, had there been the same level of scrutiny? Similarly, there is now a small library of books alleging chaos inside the Trump White House, as well as plenty of personal accounts exploring the President's behavior and psychology.[24] Rereading Hamilton Jordan's book, however, left us wondering whether there might be quite a bit more to the story. When it comes to the potential effects crises have on the electoral prospects of an incumbent, you would ideally want to identify some causal mechanisms that do not purely rely on the personal idiosyncrasies of the individuals concerned.

Jordan became White House Chief of Staff in July 1979, after 3 years of chaos convinced President Carter that such a role was needed after all. When the events of that final year before the 1980 election unfolded he was 35. Within a few years, he went from masterminding Carter's election campaigns to dealing with some of the most complicated policy problems of the time. What is most striking is the amount of micro-managing he was doing. One day, he was directly negotiating in secret with Iranian diplomats about the American hostages. The next, helping Carter decide whether and, if so, to grant the ailing shah of Iran 'medical sanctuary'. Alongside all of this, he was also planning and running the re-election campaign. The challenge from Sen. Edward M. Kennedy had hurt Carter badly in the Democratic primaries. Carter needed Kennedy to campaign for him in his re-election bid. So, when Kennedy demanded that the Carter campaign help pay off the Senator's debt from his primary challenge, it was again up to Jordan to negotiate a deal. Whether or not all these claims are accurate, Jordan's book is, among other things, an unwittingly quite damning account of organizational dysfunction during a time of crisis.[25] Key decision makers, both individually and collectively, suffer from cognitive overload.

Meanwhile, the challenger, Ronald Reagan, was running a highly disciplined, and, as it turned out effective campaign. At least in part, that was probably due to him and his team being able to focus on that task. On November 4, 1980, Reagan defeated Jimmy Carter by 10 percentage points in the popular vote. It was an Electoral-College landslide, with 489 electoral votes for Reagan compared to Carter's 49. In 1984, Reagan's winning margin was even larger: a whopping 525 electoral votes, compared to 13 for Walter Mondale, the former vice president under Carter, who only won his home state of Minnesota and the District of Columbia.[26]

For comparison, Trump received 304 electoral votes in 2016, compared to Hillary Clinton's 227.[27] In February 2017, shortly after his inauguration, Trump claimed: "I guess it was the biggest Electoral-College win since Ronald Reagan."[28] As reporters were quick to point out, Trump received fewer electoral votes not just than Reagan, Bill Clinton and Barack Obama in each of their runs for the White House, but also far fewer than Bush senior in 1988.

[23] Lewis, M., 2018. The fifth risk: undoing democracy. W. W. Norton & Company; 1st Edition

[24] The most revealing one so far is probably the account by Mary Trump, the President's niece and a clinical psychologist. See: Trump, M.L., 2020, Too Much and Never Enough: how My Family Created the World's Most Dangerous Man. Simon + Schuster UK; 1st Edition

[25] https://www.upi.com/Archives/1982/09/20/Hamilton-Jordan-says-Carters-last-year-was-pure-hell/4201044230454/

[26] https://ballotpedia.org/Ronald_Reagan#cite_note-biobio-2

[27] https://ballotpedia.org/Donald_Trump

[28] https://thehill.com/business-a-lobbying/donald-trump-falsely-claims-biggest-electoral-win-since-reagan

This also inadvertently drew an unflattering contrast with Reagan for those old enough to recall the former President in his daily dealings with the press. Reagan is widely remembered as a very gifted communicator, but not one keen to blow his own trumpet. "Government's view of the economy could be summed up in a few short phrases: If it moves, tax it. If it keeps moving, regulate it. And if it stops moving, subsidize it."[29] As President, Reagan became perhaps the world's most influential advocate of tax cutting, deregulation and entrepreneurship, triggering lasting policy changes well beyond U.S. shores. "Mr. Gorbachev, tear down this wall!"[30]

By the time he left office, Reagan had plenty to brag about. He rarely did. In part, that probably reflected his life experiences. Specifically, perhaps that his road to the White House had been so long and twisted. After a somewhat mediocre acting career, Reagan spent years travelling the country as a motivational speaker before being elected governor of California in 1966. He campaigned unsuccessfully for the Republican nomination for the U.S. presidency in 1968 and again in 1976, before finally winning first the Republican nomination and then the White House in 1980. Jimmy Carter and his team spent the summer hammering away at Reagan's supposed weaknesses: his age, mental acuity and, most of all, Reagan's supposed extremism, much as Team Trump has been trying to hammer Joe Bidden. For the Carter campaign, that turned out to be a big mistake, but it took until the very last week of the campaign for that to become clear.

Carter genuinely believed that by being so fervently anti-communist, Reagan might stumble into a nuclear war with the Soviet Union. For a while, that line of attack appeared to be working. According to polling, voters still personally liked and trusted Carter, despite growing doubts whether he was up to the job.[31] When the Iranian hostage crisis struck, his approval ratings initially received a big bounce. That was thanks to what has become known as the "rally-round–the-flag" effect. In times of crisis, voters frequently turn to the incumbent president or party – indeed, that's what we saw in many other countries during the early stages of the Covid-19 crisis and was probably also behind the slight fading of Joe Biden's polling lead in April.

However, Carter's standing in the polls was badly hurt after an attempt to rescue the hostages in April of 1980 failed. His team felt that the only way to win was to make the alternative candidates seem unacceptable to the majority of voters. To do so, their first priority was to squeeze the vote of third-party candidates, notably outgoing Republican Congressman, John Anderson. In what was probably a political misjudgment, Carter refused to participate in any debates that included Anderson. So, Anderson and Reagan held their first debate without Carter on September 21, 1980. To the dismay of Carter's team, they spent most of their time attacking the incumbent president, instead of each other. Pressure continued to grow for Carter to accept at least one debate. The President finally did, and the two debated on October 28, with only a week to go until Election Day.

According to Gallup, Governor Reagan had been trailing Carter by 8 points among registered voters (and by 3 points among likely voters[32]) right before their debate.[33] In the debate, Carter continued his well-rehearsed attack lines to depict Reagan as an anti-government, free-market extremist opposed to Medicare. Reagan audibly sighed, looked genial and replied: "There you go again." The result was a late-breaking surge in the polls, many observers attributed to the presidential debate and the "There you go again" exchange in particular. It seemed to move voter preferences in Reagan's direction, giving him a 3-point lead among likely voters immediately afterwards, again according to Gallup.

Reagan had mastered the art of deflected charges during his previous runs, without sounding inauthentic. When caught out with some falsehood (as happens to most politicians at some point), he would deflect the charge with a self-depreciating bit of humor.[34]

[29] Shiller, R.J., 2019. Narrative economics: How stories go viral and drive major economic events. Princeton University Press, p. 51 points out that this quip originally dates back to a Chicago Tribune newspaper columnist, Walter Trohan. In his 1986 speech, Reagan improved it slightly. Combined with Reagan's celebrity status, that helped it go viral. Shiller uses it as an example how contagious ideas can trigger lasting changes in economic policy and performance.

[30] https://www.youtube.com/watch?v=lguMXrgfrg8

[31] To get an idea of how the 1980 campaign played out and ended, it is well worth checking the election night coverage of the U.S. news networks. The NBC broadcast mentioned below can be found here: https://www.youtube.com/watch?v=OMuWVsPQbwM

[32] Likely voters are those registered voters a pollster thinks will probably cast a ballot, for example because they have expressed the intention to go vote or frequently voted in previous elections.

[33] https://news.gallup.com/poll/111451/late-upsets-rare-happened.aspx.

[34] https://www.youtube.com/watch?v=Pgs-LaWyUJI

On April 26, 1981, a profile worth quoting at length appeared in the New York Times, marking Reagan's first 100 days in office: "With a gift for political theater, Mr. Reagan has established his goals faster, communicated a greater sense of economic urgency and come forward with more comprehensive proposals than any new President since the first 100 days of Franklin D. Roosevelt, the hero of his youth and the man whose record of achieving social change Mr. Reagan seeks to emulate – albeit at the opposite end of the political spectrum. (…) Mr. Reagan's accomplishments seem all the more remarkable for having come from one of the most improbable figures ever to assume the Presidency – a one-time baseball announcer (…) who has had to force the Establishment to take him seriously."[35]

In contrast with the current incumbent, Reagan's style made him personally popular, even among those who disagreed with his policies.

[35]  https://www.nytimes.com/1981/04/26/magazine/reagan-s-first-100-days.html

## 4. THIS TIME **IS** DIFFERENT – AND SO IS EVERY TIME

Back in our 2016 CIO Special, we ran a chart looking at the performance of U.S. stock markets during election years. It showed that U.S. equity markets are generally slightly weaker in election years and had been suggested by a very kind colleague, who has since left the company. To be very honest, we had not given the chart enough thought at the time, but thinking about it a bit harder this time around has been extremely helpful to understand not just markets but electoral events better.

So, below it is, without further ado, this time for years in which an incumbent seeks re-election, going all the way back to 1936, the first time Franklin D. Roosevelt faced voters again.

You will notice the election-year averages are highly sensitive to when you start. If you exclude 1936, by starting in 1940, much of the difference in performance vanishes. We noted as much at the time:

"Of course, such statistical results should come with a soup spoon of salt. There are simply not enough recent election years to make any reliable inferences. The relationship between the economy and financial markets is complex and ever-changing. Worse still, there are breaks in the data when it comes to how electoral politics might impact both the economy and markets. In the statistical jargon, there are plenty of non-stationary processes involved. (To take just one example, consider how U.S. monetary policy changed from 1979 on, when the Federal Reserve Board (Fed) under Paul Volcker got tough on inflation.)"[36]

**U.S. STOCK-MARKET PERFORMANCE DURING ELECTION YEARS**
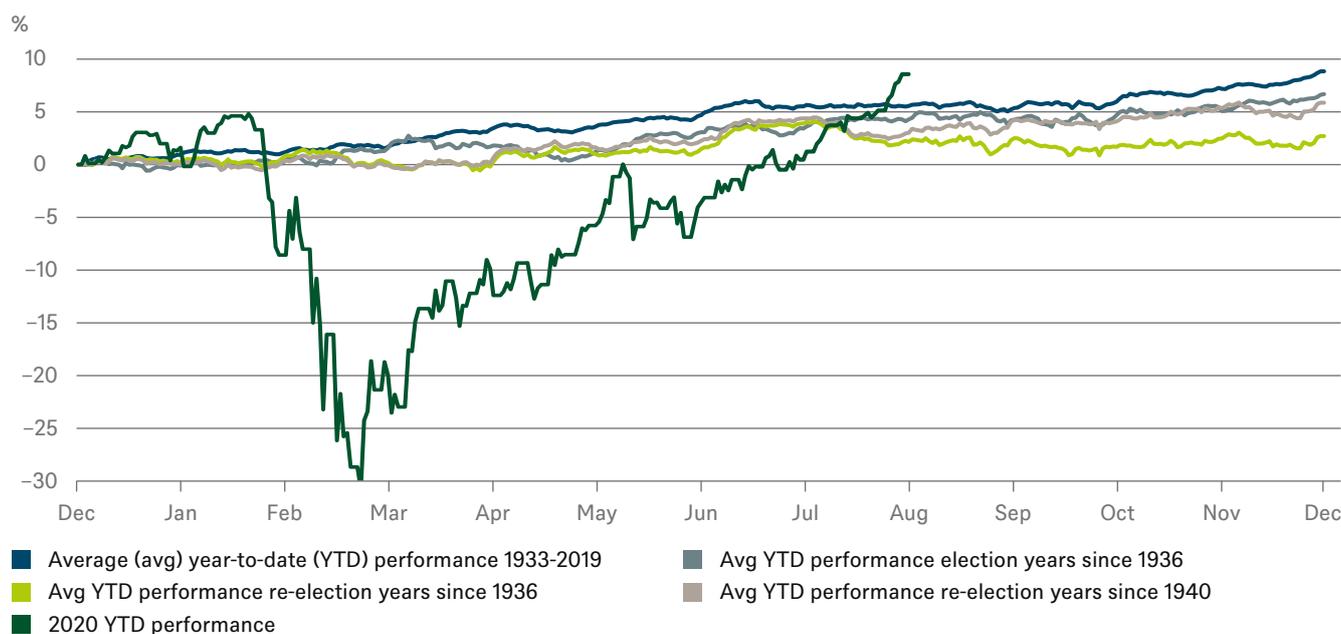


- Average (avg) year-to-date (YTD) performance 1933-2019
- Avg YTD performance re-election years since 1936
- 2020 YTD performance
- Avg YTD performance election years since 1936
- Avg YTD performance re-election years since 1940

Source: FiveThirtyEight, DWS Investment GmbH as of 8/30/20

---

[36] https://www.dws.com/insights/cio-view/macro/an-early-roadmap-to-us-politics-in-2020-and-beyond/

However, we probably did not notice perhaps the most obvious non-stationary processes: how electoral forecasting continues to evolve and inform market opinion. 1936 was famously the first year that George Gallup started opinion polling. Gallup correctly predicted a victory for Roosevelt, but that prediction was widely ignored. Instead, conventional and especially stock-market wisdom thought that Roosevelt was going to lose – which was considered a favorable outcome by many business people. This was partly informed by a large (2.4m) survey by the magazine Literary Digest, providing a textbook example of how sampling errors can distort polling results.[37] As a result, equity markets reacted very negatively when the results came in – it was a genuine surprise.

The 1980 campaign tells a similar story, only with the nature of the surprise reversed from a stock-market perspective. Until we started reading up on it again, we had not quite realized ourselves how much campaigning had changed in the last 40 years. For one thing, it was the first time that a major network, NBC, relied on exit polls to call a winner. Based on its call, Carter conceded before California even finished voting. For another thing, it was one of those occasions when pollsters got it wrong. "Humiliation for pollsters who made completely wrong call on the presidential election," veteran BBC commentator Alistair Cooke reported in his justly famous Letter from America the week after.[38] That was a touch unfair. What caught the pollsters and forecasters by surprise was that undecided voters so heavily broke for Reagan after the only debate, which in turn happened only a week before Election Day. It is a reminder that even today, polls cannot tell you what voters will do before voters themselves have made up their mind.

The election night of 1980 was quite interesting in another way too. To report the results, NBC put up a colored map, on which Reagan states were in blue (or "dark grey," as the commentators helpfully kept pointing out for viewers watching on "black-and-white" TV screens). The modern media convention of "Blue states" (voting for Democratic candidates) and "Red states" (opting for Republicans) only stuck after 2000, when the country was riveted for months in the electoral battle of Bush vs. Gore that ultimately ended up in the Supreme Court. Not that everyone was happy with that color scheme. In 2004, Republican operative Clark Bensen complained that

the colors were all wrong: "The cooler color blue more closely represented the rational thinker and cold-hearted and the hotter red more closely represented the passionate and hot-blooded. This would translate into blue for Republicans and red for Democrats."[39]

In the era of President Trump, it certainly seems like the two parties have swapped emotional places since 2004. Meanwhile, stock markets have been on a rollercoaster ride. Future historians and stock-market algorithms will look back at the data and perhaps draw inferences from this strange year to what typically happens when a U.S. incumbent president runs for re-election. Eventually, some of them, and the users of their analysis might not even remember that 2020 was the year of Covid. For us, that should be a reminder whenever we look at events and data from years gone by. When history happens, especially when new and unexpected events unfold, it is different every single time. But if we take time to gather enough information, there is plenty we can learn from the past, allowing us to make better forecasts for the future. Not just by remembering what happened before. But by keeping an open mind as to what could have happened, to avoid being overconfident in trying to guess what the future might hold.

[37] https://www.math.upenn.edu/~deturck/m170/wk4/lecture/case1.html
[38] https://www.bbc.co.uk/programmes/b043w54r
[39] For a history of a color scheme, including the quote, see:
https://www.smithsonianmag.com/history/when-republicans-were-blue-and-democrats-were-red-104176297/

## 5. CAN AMERICA STILL GOVERN ITSELF? YES!

Republican anger at the status quo has been a constant and growing refrain over the past 15 years. This election season, we expect to see plenty of hand-wringing from the other side too on how things could go wrong on Election Day and in the weeks and months that follow.[40] When compared to other countries, especially recently established democracies of Eastern Europe, the United States has actually dealt quite well overall with attempts of Russian meddling and other types of foreign interference. Sadly, we fear that this is another topic we may have to return to in our blogs.

But we believe the question of whether the United States can still govern itself goes far deeper. It also predates recent concerns on whether the world's oldest democracy will be able to hold an orderly election at the time of a global pandemic. Over the past 15 years, political scientists have grown increasingly concerned about how polarized legislators, and, increasingly, voters have become. This has coincided with growing inequality in wealth and income since 1980 and several interesting ideas on how the two – political polarization and inequality – might be linked.[41]

From a European perspective, these concerns appear to be a bit overdone. We plan to partially address them in our blog by constructing "counterfactual scenarios, in which small butterfly-effect tweaks caused history to unfold differently."[42] These can "form an indispensable tool for drawing thoughtful lessons from the past, above all for giving us a nuanced sense of the degree of inevitability in what happened."[43]

Along these lines, we will probably return to 1980 repeatedly, which is why the extensive account provided above is of more than just historical interest. From a U.S. perspective, we might explore the question already touched upon. Reagan benefitted from having to wait his turn, before finally winning the White House, not just in fine-tuning his campaigning skills, but also in having a full-fledged program, team and governing philosophy by the time he did. What if Reagan had won the nomination in 1976 already, instead of having to wait his turn until 1980? What if Reagan had been in charge 1979, when events like the Islamic revolution in Iran happened? Would the Soviets still have invaded Afghanistan? Would Reagan have been similarly doomed to become a one-term president? What might that have meant for the future evolution of the Republican Party? Might Carter and his team have been more effective, had they arrived four years later?

From a European perspective, an even more intriguing question is what would have happened if neither Reagan nor Carter but John Anderson had won in 1980. During that summer, that certainly seemed like a possibility, and a serious threat to the Carter campaign, partly explaining why they were so keen not to include Anderson in the debates. An Anderson win could have opened up political and institutional paths very different from what actually happened under Reagan. In terms of deregulation, privatization and lower taxes, economic policymaking of the 1980s probably would not have been all that different. All these would probably have happened anyway, sooner or later, as they began to in many other countries at around the same time. This suggests that the ideas summed up under Reaganomics might well have succeeded, even without their most talented messenger, simply because their time had come. In other areas (such as defense spending and foreign policy) policy might well have been different. But perhaps the biggest and most lasting impact of an (admittedly unlikely) Anderson win could well have been on U.S. politics. In short, we plan to speculate in one of our blogs what the U.S. in 2020 could have looked like, after an Anderson win. And, after 40 years of moderate policymakers in Washington jointly running the country in a more permanent grand coalition of the two major parties. We bet you that scholars of U.S. politics would still have plenty to complain about – and some of it, fully justified but the total opposite of what they are saying in the year 2020 we are actually in.

For now, though, we will leave you with just one final book recommendation. It's Democracy in America, by Alexis de Tocqueville.[44]

---

[40] For a recent sampling, see:
https://slate.com/news-and-politics/2020/08/election-nightmares-experts.html
https://www.nytimes.com/2020/08/27/opinion/trump-biden-2020-supreme-court.html
https://www.brennancenter.org/our-work/analysis-opinion/trumps-hidden-powers
[41] The following books provide a good overview of recent research: McCarty, N., Poole, K.T. and Rosenthal, H., 2008. Polarized America: The dance of ideology and unequal riches. University Press Group Ltd; McCarty, N., Poole, K.T. and Rosenthal, H., 2013. Political bubbles: Financial crises and the failure of American democracy. Princeton University Press; Lee, F.E. and McCarty, N. eds., 2019. Can America Govern Itself?.Cambridge University Press
[42] Gardner, D and Tetlock, P, 2015. Superforecasting: The Art and Science of Prediction. Crown p. 187
[43] Tetlock, P.E. and Parker, G., 2006. Unmaking the West: "what-if" scenarios that rewrite world history. University of Michigan Press, p. 4
[44] De Tocqueville, A., 2004. Democracy in America: A new translation by Arthur Goldhammer (Vol. 10). Library of America; 1st Edition

Among its many insights, it describes how democracy works best, when it emerges from the bottom up, rather than being imposed top down by some strong leader or foreign power. Democracy, after all does not rest on what lawmakers do in some distant capital city. Voting them in or out every few years is a start, but it is only a start. Self-government, according to Tocqueville, is about so much more. From the myriad of local bodies, school boards and private associations to professional bodies, it is about citizens autonomously creating a healthy and free civil society.

You can feel this strangely American spirit, whenever people in other corners of the world get their first taste of freedom. More often than not, they are inspired by that shining city on the hill Reagan invoked, whether or not anyone in Washington actually knows or cares about their plight. You could see it on your TV screens, during the protests, on the Maidan, Kiev's Independence Square, and right now as citizen journalists are pulling together in improvised newsrooms in the run-down, Soviet-era apartment blocks of Minsk, Belorussia. "The political and social activity of the Maidan from December 2013 through February 2014 arose from temporary associations based upon will and skill. The essential idea was that freedom was responsibility," notes Timothy Snyder (2018)[45] , and continues quoting one of the protesters: "On the Maidan a Ukrainian civil society of incredible self-organization and solidarity is thriving. (...) We do not need your permission! We are not going to ask you for something! We are not afraid of you!"

Only, in the United States, that spirit of civic responsibility and self-organization has had 224 years to thrive. Democracy has formed deep roots. Much deeper, than when Tocqueville travelled the country and observed: "In order to destroy permanently the laws on which the republic is based, one would almost have to abolish all the laws at once. (...) the republic penetrates, if I may put it this way, into the ideas, opinions, and general habits of the Americans at the same time that it establishes itself in their laws. (...) What strikes you most upon arriving in the United States is the tumultuousness of political society. The laws change constantly, and at first sight, it seems impossible that a people so uncertain of its wishes would not soon decide to replace its present form of government with an entirely new one. Such fears are premature. When it comes to political institutions, there are two kinds of instability that must not be confused. One has to do with secondary laws, and a settled society can live with such instability for long periods. The other continually strikes at the very foundations of the constitution and the generative principles of law; it is always followed by unrest and revolution; the nation that suffers from it is in a violent and transitory state. (...) The first kind of instability is found in the United States, but not the second. Americans frequently change their laws, but the constitutional foundation is respected."[46]

[45] Snyder, T, 2019. The Road to Unfreedom: Russia, Europe, America. Tim Duggan Books; Reprint Edition
[46] De Tocqueville, A., 2004. Democracy in America: A new translation by Arthur Goldhammer (Vol. 10). Library of America; 1st Edition, p. 458-459

## 6. CONCLUSION

This CIO Special only marks the starting point of our campaign coverage. On a week-to-week basis, we will probably focus on current events, rather than the distant past and the fluid future. Either way, there are many questions still to be addressed, both big and small.

What are some of the bellwether Congressional races we are watching? (This time around, Kansas has rather caught our fancy, in terms of both of its House contests and the Senate seat. Watch our blog to find out why.) What is happening in key swing states, and what light can specific contests shed on more general questions? How much, for example, might Joe Biden benefit from having been raised in Scranton, Pennsylvania? (Probably not all that much. The evidence on family ties of a nominee to any particular state influencing voter behavior is pretty tenuous. Then again, Biden's life experiences and working-class outlook appear to be helping the Democratic ticket outperform Hillary Clinton's 2016 numbers with certain demographic groups, not just in Pennsylvania.)

In this CIO Special, though, we have taken a much longer view than in the 2016 version focusing on some of the bigger questions. Throughout it, we have drawn comparisons with 1980 and explored some of the many long shadows that Ronald Reagan's victory that year continues to cast. We explained how we approached 2020 and why, at least as far as the polling is concerned, this has been a year of no surprises. We commented on how difficult it is to understand history as it happens. And we concluded by looking at some of the challenges as the United States tries to govern itself by looking at the past to get a sense for what the future might hold.

In two months, U.S. voters will face a stark choice, which might play an outsized role not just in policymaking for the next four years, but also in how politics will operate, potentially for many years to come. "Big" election years like 1980 can to some extent change the evolution of parties and other governance institutions, taking them down a different path than the one they had been on before. We surmise that 2020 may well be such a year. In part, this is because political polarization appears to have reached such extreme levels that there appears to be a wide-spread feeling among U.S. scholars and voters alike that "something will have to change, and fairly soon," if the United States is to effectively govern itself.

That does not preclude the possibility of another "small" election year. But in our view, big changes appear increasingly likely.

GLOSSARY

The Democratic Party (Democrats) is one of the two political parties in the United States. It is generally to the left of its main rival, the Republican Party.

The Electoral College is the body which elects the President and the Vice President of the United States. It is composed of electors from each state equal to that state's representation in Congress.

Inflation is the rate at which the general level of prices for goods and services is rising and, subsequently, purchasing power is falling.

Medicare is the U.S. national health insurance program for people aged 65 and above and younger people with disabilities or kidney failure.

Monetary policy focuses on controlling the supply of money with the ulterior motive of price stability, reducing unemployment, boosting growth, etc. (depending on the central bank's mandate).

Reaganomics refers to the economic policies promoted by U.S. president Ronald Reagan during the 1980s, which called for widespread tax cuts, decreased social spending, increased military spending, and the deregulation of domestic markets.

The Republican Party (Republicans), also referred to as Grand Old Party (GOP), is one of the two major political parties in the United States. It is generally to the right of its main rival, the Democratic Party.

The Supreme Court is the highest federal court of the United States and the final interpreter of federal constitutional law. It has appellate jurisdiction over all federal courts.

The U.S. Federal Reserve, often referred to as "the Fed", is the central bank of the United States.

The United States Congress is the legislature of the federal government. It is comprised of the Senate and the House of Representatives, consisting of 435 Representatives and 100 Senators.

Volatility is the degree of variation of a trading-price series over time. It can be used as a measure of an asset's risk.