

A Case Study in Politics and Investments

Usually politics grabs the news headlines but does not have much effect on investments. Profit margin cycles and the direction of interest rates evolve gradually over decades and are the real long term drivers of investment returns, unless you experience a dramatic and sustained political interference. So while US politics dominates our news cycle and we would argue that the current US election would have some negative consequences from either candidate, it is important to look beyond this noise and fully grasp how intrusive and stifling domestic politics has become.

We use these case studies to discuss investment concepts and what we believe to be basic principles of investing. So, not to get bogged down in a discussion of the US election, let's just use what we know of Donald Trump's proposed policies to illustrate our argument. Some of his economic ideas are not well thought out. Tearing up trade agreements is bad for business and will make international borders more impenetrable for trade and people. Nations specialize in what they choose to produce and then trade to their mutual advantage; it is really the one pure economic concept that we can definitively prove to be true. Also, if the world works together it tends to be a safer place.

On the other hand, if Donald Trump, working with a Republican congress, had any success at tax reform, this could have positive investment ramifications for decades. It is ironic that the real economic time bomb in the US is entitlement spending and the topic has hardly been addressed by either candidate.

So instead of shaking our Canadian finger at how crazy the US electoral process has become, we think a little self-criticism is in order. In Canada, a majority government does not face the same checks and balances that, for the most part, would put limits on Donald Trump. So let's look at Ontario and what the Provincial Liberal government has been able to achieve after 13 years in power.

In Ontario, the main provincial policy to promote growth has been a determined effort to build infrastructure; if you build it, business will come and economic prosperity will ensue. In reality very little new infrastructure is being built since most of the billions are being spent on repair that should have been part of the budget already. Repair does not have the same multiplier effect on growth.

So what if you were thinking of moving to or increasing the size of your business in Ontario. How would you analyze Ontario versus other locations? In the past 13 years the price of power has gone up 200%. It is now the highest in North America and it is scheduled to go higher still. In this same time period, the minimum wage has risen from \$7.25 to \$11.25 and it is about to go up again. Having a minimum wage is decent social policy but raising it at this speed it what makes it hard for small and medium size businesses adjust. Also Canadian Pension Plan contributions are to be increased. This affects all Canadian and higher contributions act as an effective increased cost on business.

Every year in Ontario more rules are added for businesses, regulation is increased and permitting restrictions are greater and more time consuming. Now, Ontario plans to price carbon using a cap and trade system. Cap and trade is the worst way of limiting carbon. It is very arbitrary,

cumbersome, bureaucratic and open to manipulation and fraud. In comparison, BC uses a simple to calculate, revenue neutral carbon tax.

In Ontario, the highest personal tax rate has risen from 46% to 54%, for anyone successful enough to earn over \$220,000. And now the Liberal government is in the process of drafting the most union friendly labour legislation in North America. Collective bargaining is a well-established cornerstone of our economy with clear processes in place. However, the nature of the new rules of association will have the effect of gluing up the flexibility needed to evolve in a rapidly changing global economy.

Ontario does need repaired roads and new transit. However, all of the above government interference dwarfs any benefit from infrastructure spending. This list is so long and complicated that the collective pressure on the economy gets lost on the average voter. So if we bring it back to the question of would you expect businesses to actively grow in Ontario? The answer is no. There is no manufacturing boom coming, even though the Canadian dollar is favourable versus the US dollar. Ontario is a great place to live but we expect the economy to bump along at the status quo.