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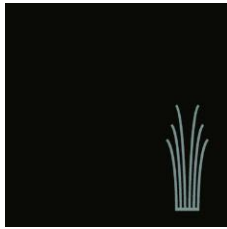
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# The Good, The Bad & The Ugly of Election Results on the Economy

Presented by:

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## U.S. Economic & Financial Market Outlook

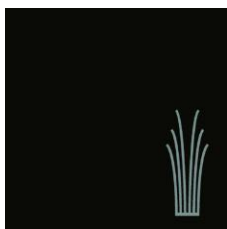
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### Positives

- 15% tax rate on dividends and capital gains remain low through 2012.
- S&P 500 reported profits are finally back to normal levels.
- Reported CPI inflation has slowed to roughly 1.5-2% annual rate.
- Passage of trade agreements with South Korea, Columbia & Panama beneficial to net exports and U.S. jobs.
- Balance sheets of U.S. corporations are very strong.

### Negatives

- Europe has fallen into recession and still faces sovereign debt dilemma in pursuing austerity rather than growth agendas.
- U.S. budget negotiations may remain in gridlock, facing “fiscal cliff” of draconian cuts in federal defense and health care expenses.
- Potential tax increases and regulatory burdens put headwinds on economic recovery beyond 2012 and create potential stagflation.
- Negative real interest rates are unsustainable over the long term, and T-bond yields should rise from current levels, even without a re-acceleration in the inflation rate .
- Post election government policies pose unusually large consequences for future economic growth.



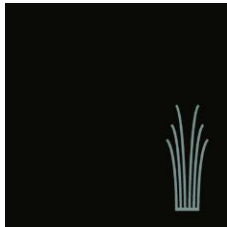
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## Intrade Prediction Markets

### Probability of President Obama Winning Re-Election



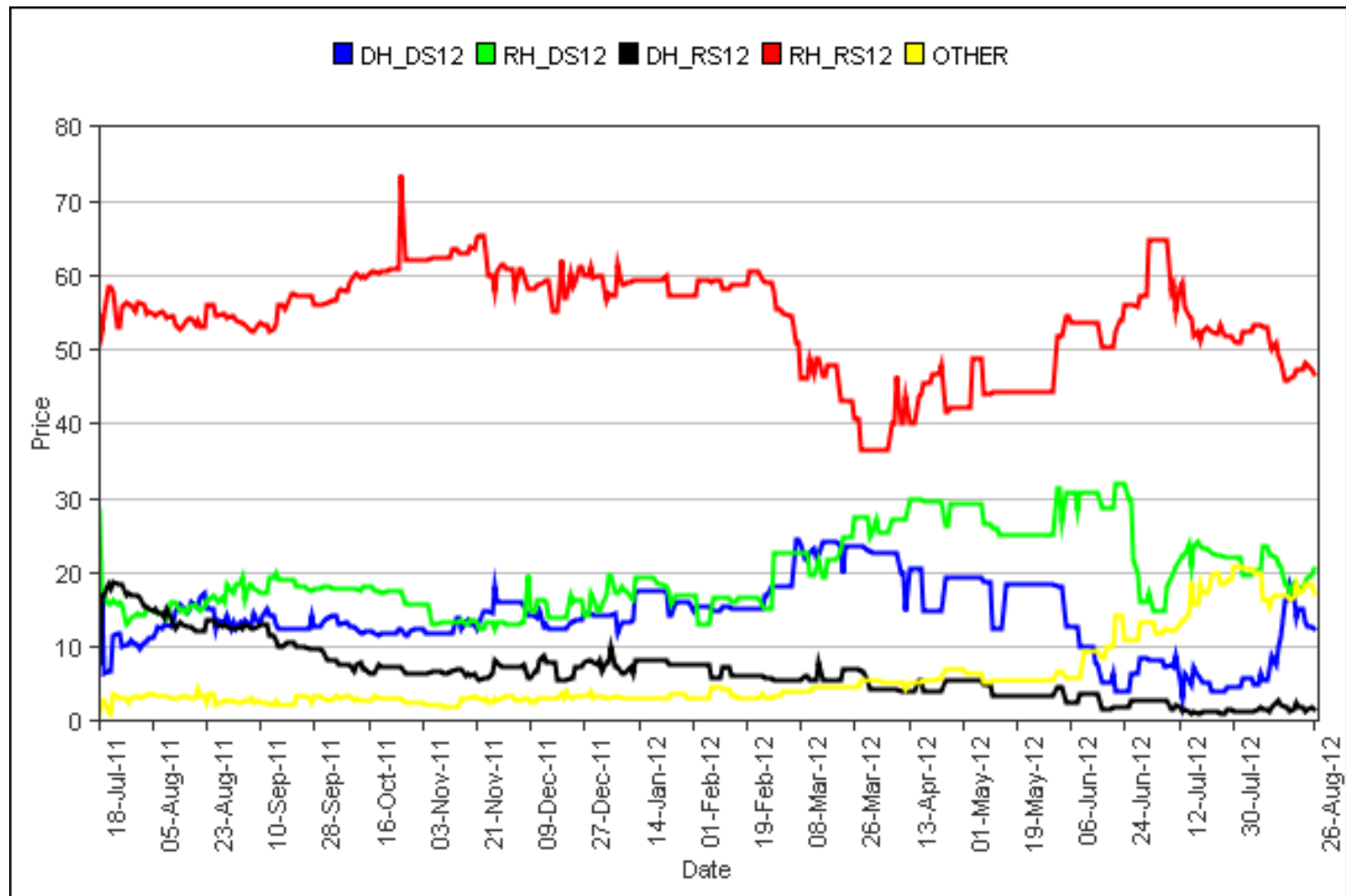
Source: [www.intrade.com](http://www.intrade.com)



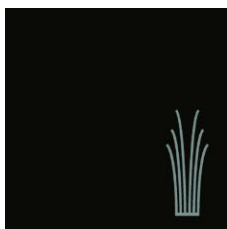
## Iowa Election Markets

### Probability of Republicans and Democrats Winning House and Senate

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Source: University of Iowa Election Markets



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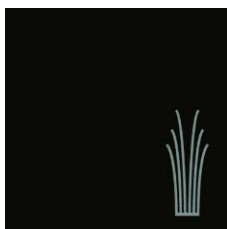
## SKBA's U.S. Economic Scenarios

*As of 6/30/12*

### 2-Year Horizon

	Estimated Return Outlook			
	Real GDP	Inflation	Stocks	T-Bonds
<b>Boom</b>	4.5	4.5	Happy Days Are Here Again	<i>Really Ugly</i>
<b>Stagflation</b>	1.5	3.5	Not So Happy	Just Ugly
<b>Historical Norm</b>	2.5	2.5	<b>Surprisingly Super</b>	Ugly
<b>Perfection</b>	4.0	1.5	<i>Boom Time Again</i>	No Better
<b>Recession</b>	-1.0	0.5	Pretty Unhappy	<b><i>Bond Heaven</i></b>

*Outlook and returns are subject to change and should not be viewed as a promise of future performance.*



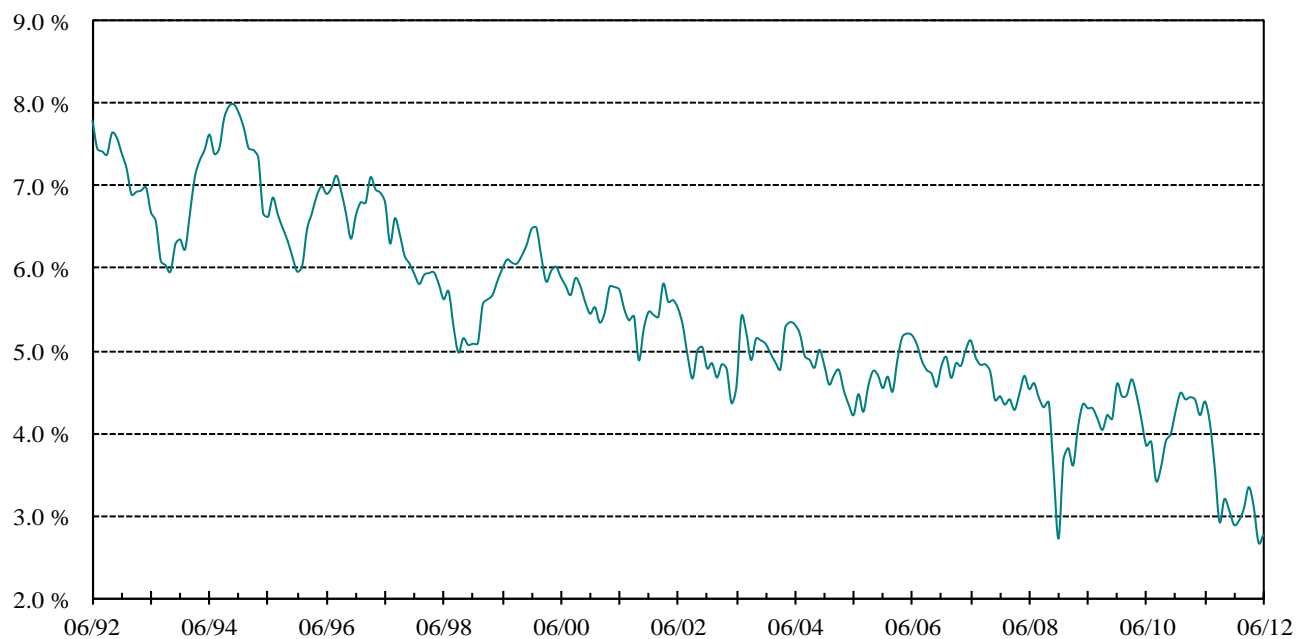
# U.S. Treasury 30 Year

*As of 6/30/12*

## 30 Yr US Treasury Yield

*Monthly, Last 20 Years*

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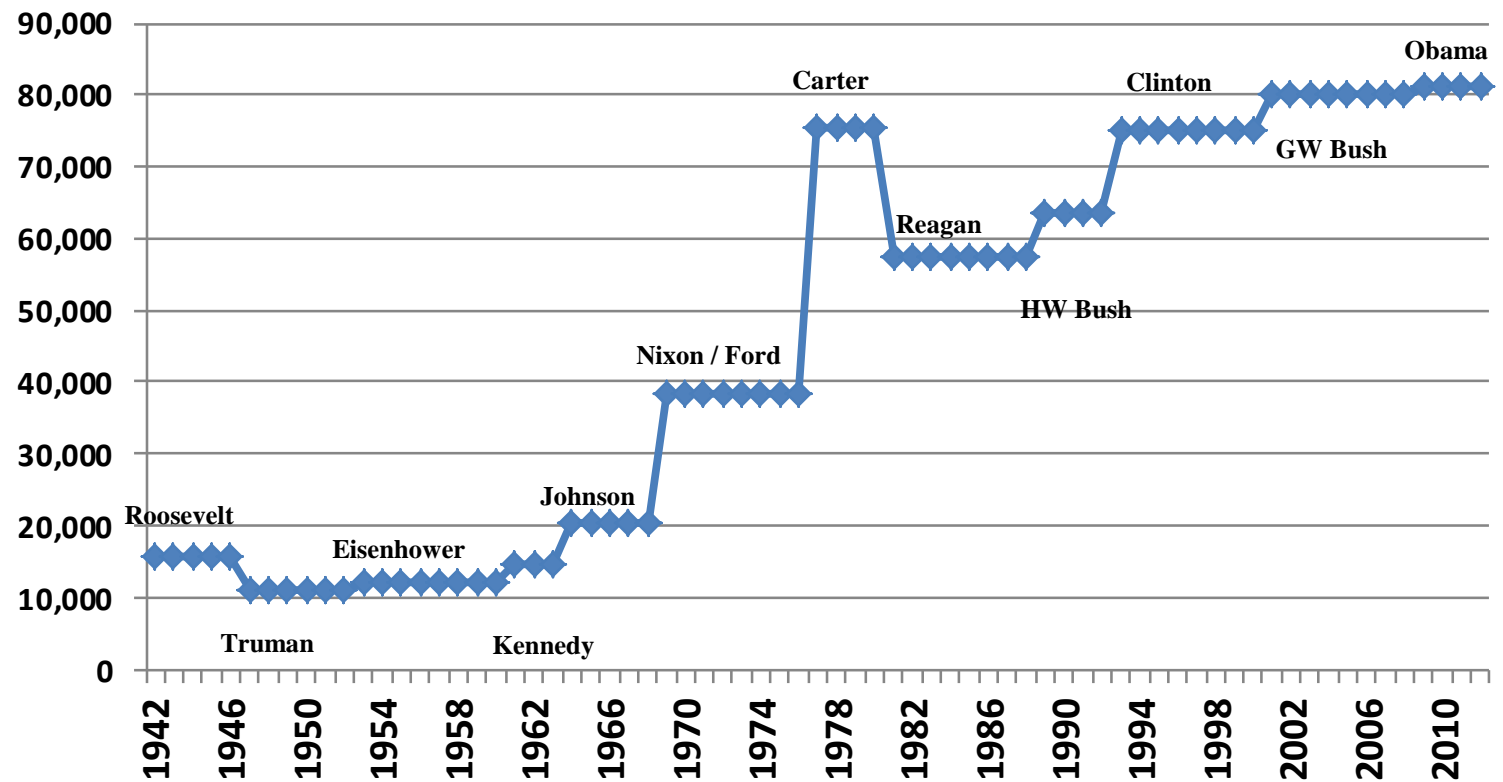
*Source: FactSet/Compustat*



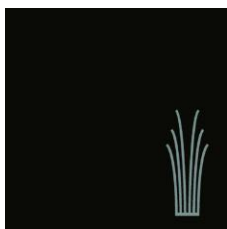
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## Proxy for the Burden of Regulation and Compliance

### Average Annual Pages Added to Federal Statutes & Federal Register By President (2012 Estimated)

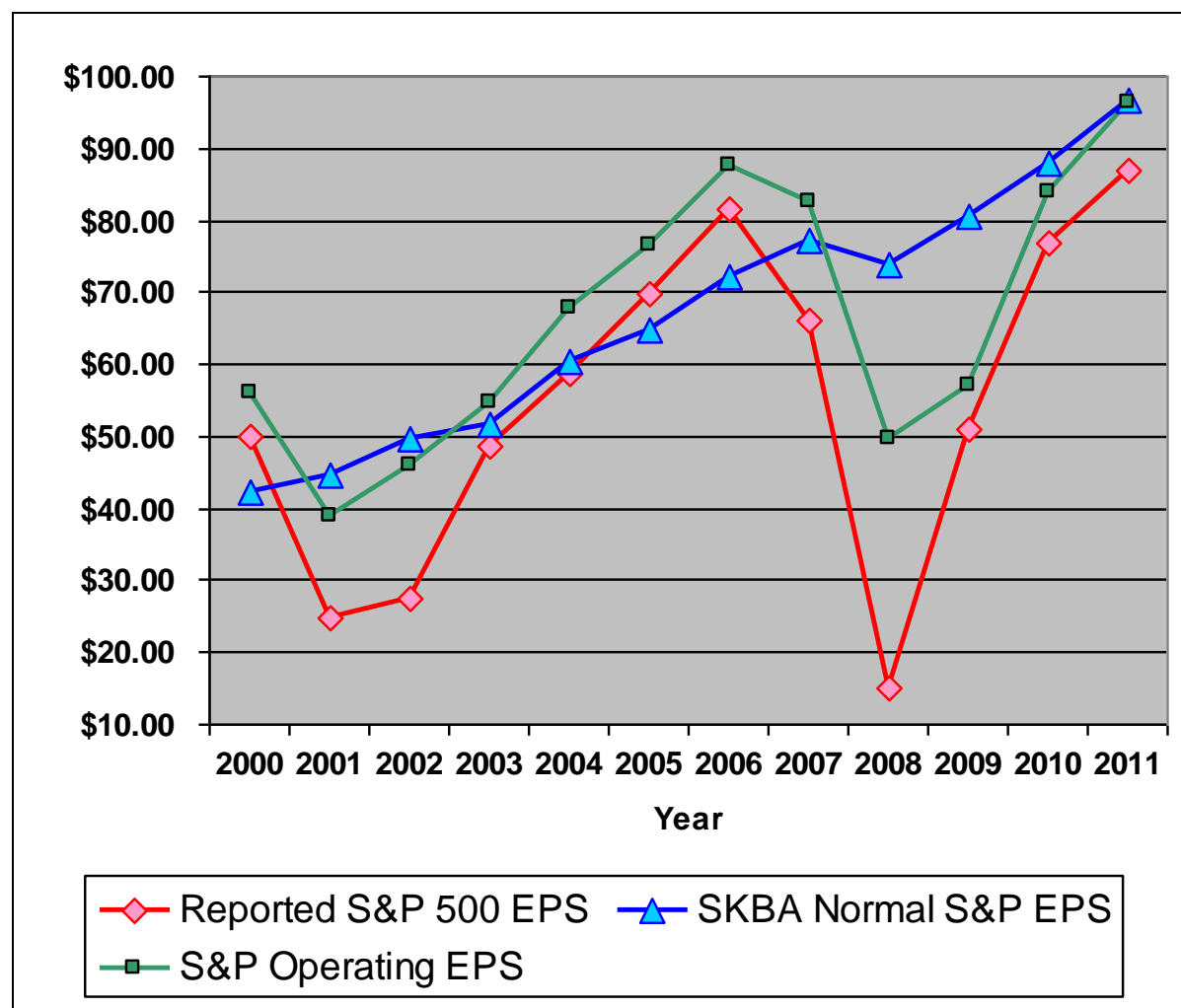


Source: Law Librarian's Society of Washington DC; Federal Register & Federal Statutes



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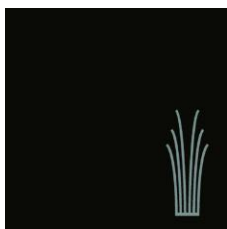
## Reported Versus SKBA Normalized S&P 500 Earnings Per Share



*Forecasts are subject to change and should not be viewed as a promise of future performance*

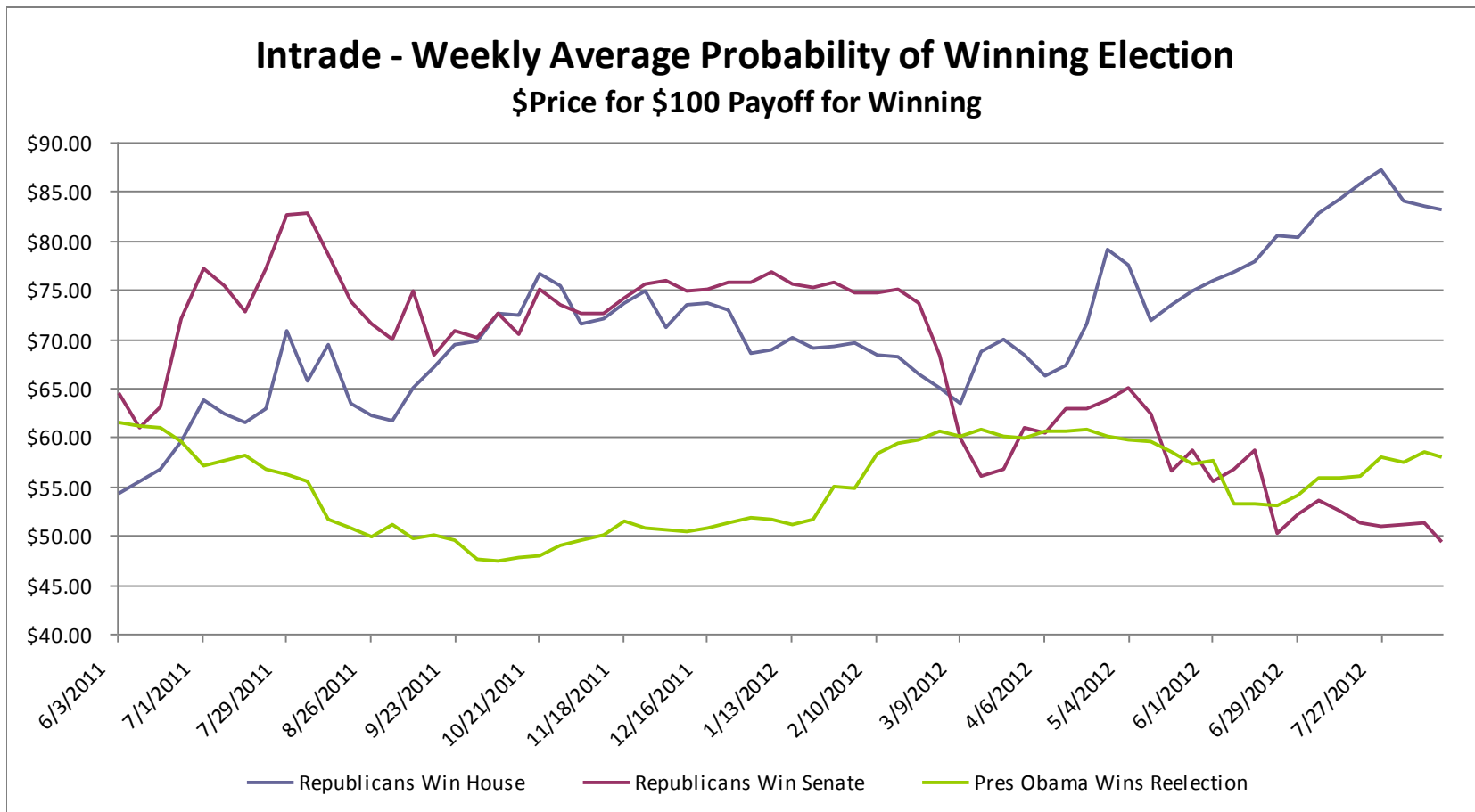
*Source: FactSet/S&P, Compustat, and SKBA Estimates*





## Intrade Election Prediction Markets For Presidential, House & Senate Races

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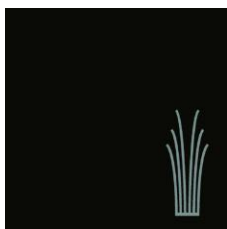


Source: [www.intrade.com](http://www.intrade.com)

## What Are Possible Economic Consequences of Election Results?

<b>Intrade Prediction Markets Probabilities</b>						
		<b>Estimated Probability</b>			<b>Likely Resulting</b>	<b>Possible 2013-14</b>
		<b>As of: 16-Aug-12</b>	<b>If Independent</b>		<b>US Political</b>	<b>US Economic</b>
<b>Election For:</b>	<b>Probability of Winning</b>	<b>Resulting Govt</b>	<b>Events Result:</b>		<b>Outcome*</b>	<b>Outcome*</b>
<b>House</b>	<b>Republican</b>	87.0%	All Three Republican	19.5%	Growth Agenda	Economic Boom
	<b>Democrat</b>	13.0%	All Three Democrat	3.6%	US Falls Off Cliff	Recession
<b>Senate</b>			Reps Win House Only	23.9%	Bad Compromise	Recession
	<b>Republican</b>	50.6%	Dems Win House Only	2.9%	OK Compromise	Historic Norm
	<b>Democrat or Tie</b>	49.4%	Reps Win Senate Only	3.7%	Muddle Through	Stagflation
			Dems Win Senate Only	19.1%	Compromise	Stagflation
<b>President</b>	<b>Romney</b>	44.4%	Reps Win Pres Only	2.9%	Gridlock	Recession
	<b>Obama</b>	55.6%	Dems Win Pres Only	24.5%	Clinton Compromise	Historic Norm
				100%		

\*These SKBA hypothetical outcomes may be changed without notice and are for illustration only, not a promise of future performance



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## 2 Year Multi-Scenario Outcomes & Estimated Returns

### June 2012 Outlook

*As of: 06/30/12*

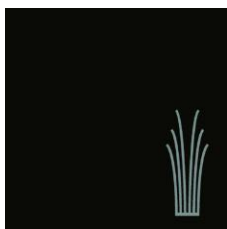
*2 Years to: 06/30/14*

Scenario Forecasts	Boom	Stag- flation	Historic Norm	Perfection	Recession	
<b>SKBA Probabilities</b>	0%	20%	45%	5%	30%	100.0%

#### Expected Values & Annualized Returns by Scenario\*

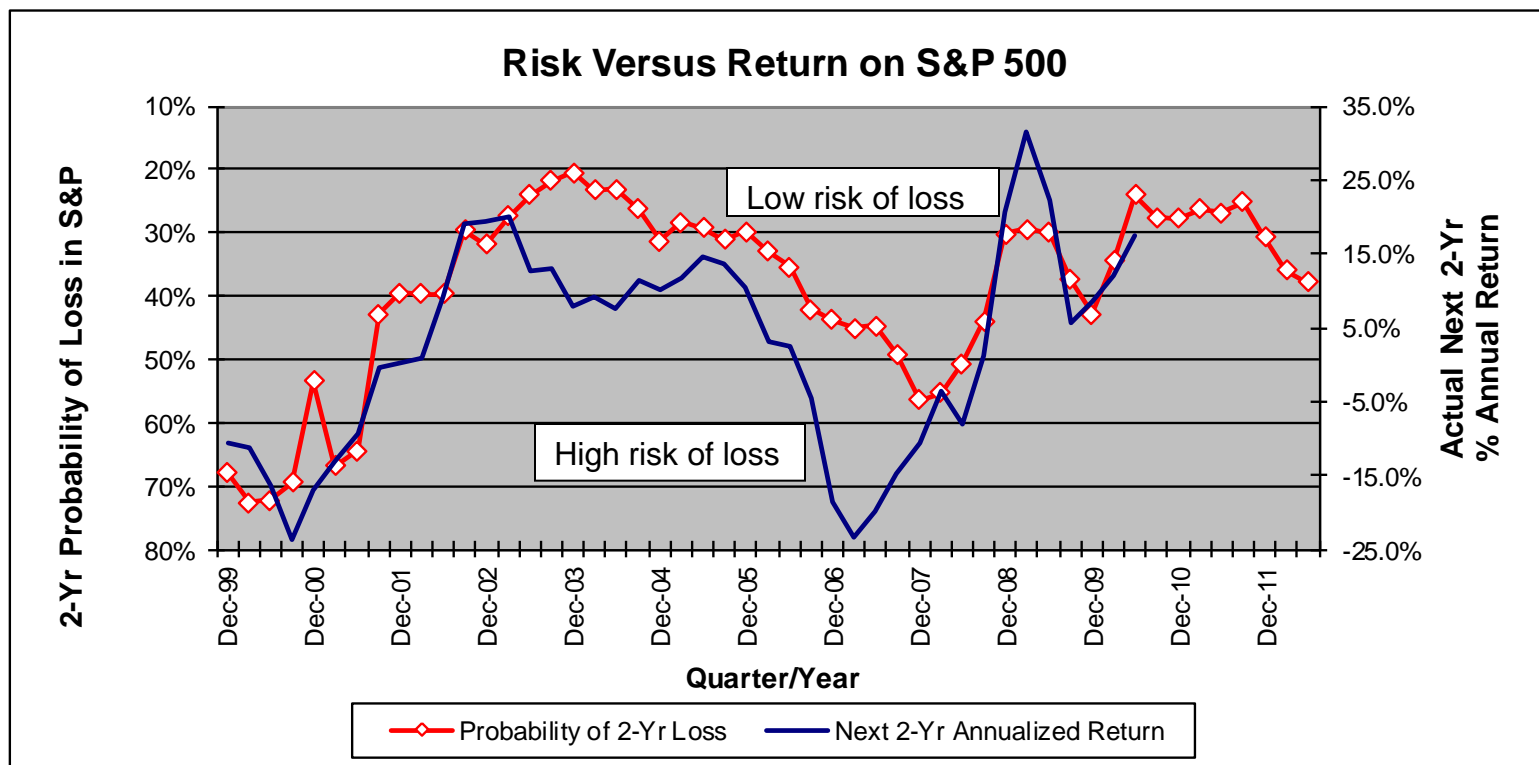
	Today's Values 06/30/12	Estimated Future Values						Estimated Returns*
<b>S&amp;P 500</b>	\$1,362	\$1,529	13.5%	-3.7%	20.7%	45.6%	-12.6%	<b>7.0%</b>
<b>30-Yr T-Bond</b>	2.75%	3.5%	-20.0%	-9.9%	-8.1%	-12.3%	11.9%	<b>-2.7%</b>
<b>6 Month T'Bill</b>	0.15%	1.2%	3.2%	1.2%	0.8%	1.3%	0.1%	<b>0.7%</b>

\* Estimated Returns are subject to change and should not be viewed as a promise of future performance.

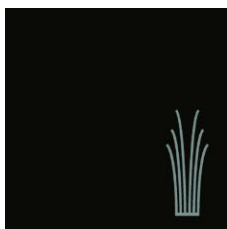


## SKBA Historical Probabilities of Rolling 2-Year Perspectives

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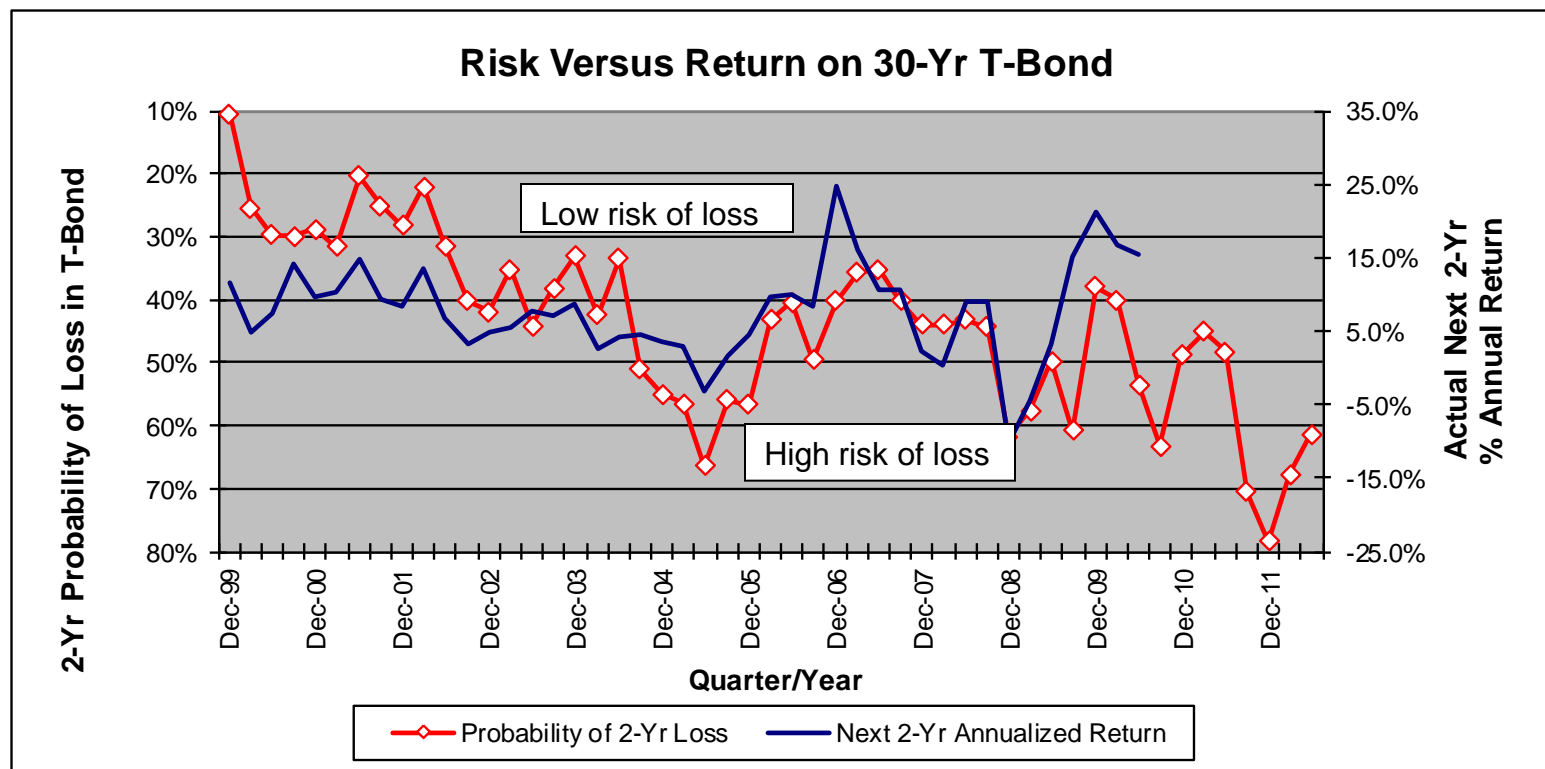


The **multi-scenario process** helps us *gauge the general direction of the markets*, and offers a *disciplined framework for considering the range of possible outcomes*.



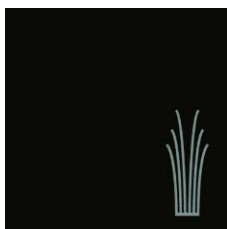
## SKBA Historical Probabilities of Rolling 2-Year Perspectives

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The **multi-scenario process** helps us gauge the general direction of the markets, and offers a disciplined framework for considering the range of possible outcomes.

\* 30-Year T-Bond returns are calculated using Merrill's 30-Year T-bond Index.



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## Conclusions - With US Election Outcome Too Close to Call, What Should You Watch Out For?

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- The world views of candidates are dramatically different - with possibly vastly different economic policy paths post election.
- The private sector wants to grow investment and employment but fears the regulatory and tax burdens that are coming.
- European malaise is a problem for U.S. exports and accounts for roughly 20% of S&P 500 company profits.
- The Federal Reserve Board still sustains artificially low interest rates that are hurting economic growth!
- **Yet even just 2.5-3.0% economic growth would be good for stocks.**