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5 Questions on the US Elections

The US Presidential elections on November 3rd are fast approaching. As they do, they are commanding more headline space as the combative rhetoric between the Republicans and the Democrats intensifies. In this article, we cover five key questions regarding the elections.

1. WHO ARE THE CANDIDATES AND WHAT ARE THEIR POLICIES?

The two candidates are Joe Biden and Donald Trump. Each will bring a unique set of pros and cons for various asset classes and sectors of the economy. With both the Democratic and Republican conventions having taken place, we now have a clearer view on each candidate's policies. We present a bird's eye view of these below, concentrating on what political commentators have identified as the four leading issues at play: the economy, China, the

handling of the pandemic and race relations.

Republican Candidate - President Trump

According to opinion polls, Trump seems to be favoured from an economic standpoint. He supports deregulation (beneficial for banks and financial companies) and protectionism. "Trumponomics" are generally supportive for stock markets and he has presided over an equity market that skipped from new high to new high (in August, despite the pandemic, stocks again embarked on a record-breaking streak) and a 50-year low in the unemployment rate. If he wins a second term, he is likely to usher in further tax cuts (probably through an extension of his Tax cuts and Jobs Act). We could also see further infrastructure spending. Trump has been generous to the agricultural sector, with direct federal payments to farmers forecast to hit $37.2bn in 2020 (an all-time high), according to the US Department of Agriculture. This could help win hearts and minds in agricultural states such as Ohio, Wisconsin and Iowa, which helped secure his place in the Oval Office in 2016. Trump prides himself on unleashing oil and gas production in the US and energy names are likely to benefit from a Republican win.

Trump's handling of the pandemic has been questionable and the US now accounts for around one-quarter of global infections (over 6 million confirmed cases). Until ballot day, developments on the epidemiological front could be instrumental in swaying voter sentiment. Positive developments on the vaccine front could help Trump.

Regardless of which side wins, the trade spat with China looks set to be a mainstay (opinion polls have shown that both Republican and Democratic voters support a tougher stance on China). However, a Trump win could mean another four years of shock-and-awe trade policies and would be decidedly more hawkish as he continues to push his "America First" agenda. A lot of work is still to be done if he is to fulfil his 2016 pledge to reduce the goods trade deficit with China (it has actually

only closed narrowly from $347bn for
2016 to $345bn for 2019).

Trump is campaigning on law
and order and has taken a hard-line approach when it comes to protests and social unrest.

Democratic Candidate - Joe Biden

Joe Biden
served as Barack Obama's Vice President from 2009 to January 2017. He supports higher taxes and higher public spending. The consensus view is that a Democrat victory in November will be negative for both equity and bond markets, as well as for the US dollar, but this is quite simplistic.

Biden could
in fact prove to be more market friendly, as he is likely to adopt a less bellicose rhetoric, especially on trade. In 2019, the US-China trade war was a major headwind for global growth and before the coronavirus pandemic stole the show, markets were held hostage to US trade policy (often communicated bluntly via the Trump Twitter feed), resulting in elevated volatility. With Biden installed in the White House, frictions with China – especially with regard to technology and intellectual property – are unlikely to go away. Biden pledges to "take aggressive trade enforcement actions against China or any other country seeking to undercut American manufacturing through unfair practices". However, it is expected that Biden will adopt a more dovish communication policy, leveraging the support of traditional US allies.

With regard to the economy, Biden's campaign features a Build Back Better economic recovery plan which seeks to “Mobilize American manufacturing and innovation” and “ensure that the future is made in America”. While Biden’s plans to increase the minimum wage could initially be viewed as an additional cost for firms, on the other side of the coin, it could result in higher spending, coaxing demand upwards. Infrastructure spending could also be expected, with Biden seeking to build a modern America with emphasis on decarbonization. He desires to achieve a pollution-free power sector by 2035 and to make dramatic investments in energy efficiency in building as well as sustainable agriculture. This should open a whole array of new business opportunities.

With regard to Covid-19, Biden has been critical of Trump’s approach and has outlined a seven point plan to tackle the pandemic should he be elected. This involves more testing, the equitable distribution of treatments and more reliance on science. With regard to healthcare at large, Biden wants to build on the Affordable Care Act (better known as Obamacare), giving Americans more choice, reducing health care costs, and making the health care system less complex to navigate. This may be bad news for certain healthcare stocks and pharmaceuticals.

Biden’s running candidate, Senator Kamala Harris has been a vocal supporter of the Black Lives Matter protests that are currently running through America.

A pinch of salt: Political scientist Anthony Downs once noted that “politicians don’t get elected to formulate policy; they formulate policy to get elected.” Investors should avoid conflating policy positions with their future policy path. The extent to which these policies come to fruition will largely depend on the composition of Congress and the trajectory of the pandemic (a recovery plan will probably push policy intentions onto the backburner).

2. WHO WILL BE THE NEXT PRESIDENT?

Historically, incumbent presidents have been re-elected unless there was a recession during their term. However, the polling failure of 2016 shows that nothing can be taken for granted, and this is especially true in the current, highly polarized context. Initially, due to the handling of the pandemic, Joe Biden was shown to have a comfortable lead. Now, as November 3rd draws nearer, an assortment of polls and betting markets show that President Trump is closing in on Biden's lead.

Nothing can be taken at face value because of the Electoral College[1], a system which means that the President is not elected based on overall popularity. Indeed, in 2016, Hilary Clinton tallied 3 million more votes than President Trump, but the dispersion of these votes across states, meant that she did not take the White House. A lot will depend on a few, key swing states such as Arizona, Georgia, Florida, Michigan, North Carolina, Pennsylvania and Wisconsin.

3. THE PRESIDENT IS JUST ONE BRANCH OF GOVERNMENT – WHAT ABOUT THE OTHER 2?

As mentioned previously, the composition of Congress will also influence how the next administration will function. A divided government in the US occurs when one party controls the executive branch while another party controls one or both houses of the legislative branch. The degree to which the President of the United States has control of Congress often determines his political strength – such as the ability to pass sponsored legislation, ratify treaties, and have Cabinet members and judges approved.

All 435 voting seats in the United States House of Representatives will be up for election; 218 seats are necessary for a majority. Democrats have held a majority in the House since 2018 and are likely to hold onto this. At least 35 of the 100 seats in the Senate will be up for election. Republicans have held control of the Senate since 2014. They currently hold 53 Senate seats, while Democrats hold 45 seats, and independents hold two seats. Barring further vacancies or party switching, 23 Republican-held seats, along with 12 Democratic-held seats, will be up for election. Whether the Republicans can

hold onto their Senate majority is pivotal for the party – it will allow them to obstruct certain elements of the Democratic Presidential agenda in the event that the White House is lost.

Some political commentators argue that a divided government is positive as "it encourages more policing of those in power by the opposition, as well as limiting spending and the expansion of undesirable laws", while other commentators just claim the opposite, arguing that "divided governments become lethargic, leading to many gridlocks." The latter is perfectly illustrated at the moment by the ongoing bickering over the size and shape of a second fiscal recovery package.

4. WHEN WILL WE KNOW THE RESULTS?

In capital markets, the sooner the elections done and dusted, the better, in order to remove this significant hunk of event risk from portfolios, allowing investors to position themselves accordingly. However, with the global pandemic shaking up the traditional way of voting, results may not be cut and dried as quickly as one would expect.

Democracy
in the time of corona could potentially be a slower process: election day could well transpire into election week and potentially even election month, with postal voting potentially delaying the final result. The US is still in the thick of its first wave of the pandemic. In order to uphold social distancing and prevent further contagion, many states are opting for postal voting. As a result, it could take significantly more time for the results to be counted and verified. As states roll out the results one by one, confusion could arise with one candidate appearing to have won, only for the tables to subsequently turn.

President Trump is vehemently against postal voting, claiming that it paves the way for electoral fraud. He has gone as far as to tell voters in North Carolina to vote twice, once by mail and once at polling stations, saying: " if the system is as good as they say it is then obviously they won't be able to vote (in person)." Fears are arising that Trump could contest the election if Joe Biden takes victory. With social tensions already nearing boiling point, there are worries that a full-blown constitutional crisis could ensue. The VIX index – a barometer of expected volatility on the S&P 500 equity index – shows that volatility through October and November is expected to be higher than usual for this particular set of elections. Moreover, this volatility is expected to remain elevated after the election date – implying that results may not be clean.

5. WHAT DOES IT MEAN FOR MY PORTFOLIO?

This set of elections could be messy on markets and nothing is written on the wall, especially with the pandemic still at large. However, investors should remember that no matter who is President, saving the economy will come first and foremost and policy will be fine-tuned in order to achieve this. In short, both candidates seem to be destined to take a journey with the same destination: budgetary expansion. Quality names with sound financials and a future-proof business model that encompasses key societal trends such as digitalisation or sustainability should thrive, regardless of who sits in the Oval Office. Ultimately, no matter who is President of the United States the golden rules still apply: spend less than you earn, grow your savings and investments, diversify and take a long-term approach. We advise against directional bets with uncertainty set to be the dish of the day for the foreseeable future.

[1] The Electoral College consists of 538 electors, and an absolute majority of at least 270 electoral votes is required to win the election.

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