

CIO Perspectives

23 October 2024

DBS Chief Investment Office

ASSET ALLOCATION

US Presidential Election: Macro & Cross-Assets Implications

Key Points

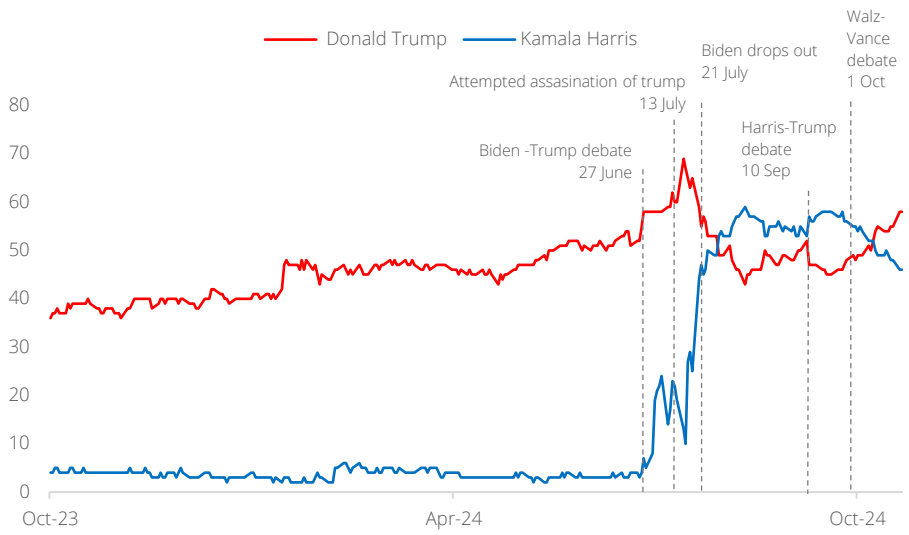
- Equites: A Republican sweep would offer short-term gains ford tax-sensitive sectors through tax cuts, deregulation, and tariffs, benefiting industries like energy and manufacturing, although these gains may be offset by trade retaliation. A Democratic sweep would see an expansion of Biden's policies, supporting sectors such as healthcare, semiconductors, and clean energy.
- Credit: A Republican sweep could boost corporate credit as business-friendly policies drive higher yields, offering opportunity in the 7-10Y duration. A Democratic sweep is expected to have neutral impact on credit, with corporate tax increases moderately affecting profits but not significantly impacting interest expense priorities.
- Rates: A Republican sweep would likely steepen the yield curve, driven by fiscal looseness, inflationary concerns from tariffs, and pressure on the Fed to cut rates. A Democratic sweep would see yield curve relatively flatter and yields relatively lower as inflationary risk will be more contained.
- FX: USD recovery expected to fade out after the US elections as Trump's policy bias will undermine the dollar's reserve status while Harris's support for Fed's independency will support ongoing rate cuts.
- Gold: A Republican sweep would boost gold given Trump's adversarial stance on geopolitics and looser fiscal stance, while a Democratic sweep would also see gold benefitting as Harris' fiscal expansionary policy will grow, albeit to a lesser extent.
- Commodities: A Republican sweep would lead to looser policy and protectionist measures, creating upside pressure on commodities' prices, while a Democratic sweep should see a relatively tighter fiscal stance and fewer protectionist policies, maintaining the status quo for commodities prices.



2024 US Presidential Election – Down to the wire. The 2024 US Presidential race begun with Trump leading the polls, fuelled by strong support and a campaign centered on economic nationalism. However, the race took a significant turn when President Joe Biden stepped down from seeking re-election, allowing Vice President Kamala Harris to secure the Democratic nomination. Since then, Harris had gained significant momentum, with early polls showing her taking the lead over Trump.

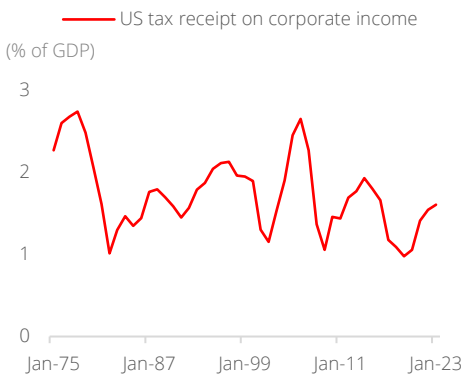
However, in recent weeks, the political landscape took a dramatic shift as Trump regained momentum and now finds himself in the lead once again. With less than two weeks until the election, much can still change, adding to market volatility as investors weigh the implications of different outcomes. In this CIO Perspective, we highlight the macro and cross assets implications in the event of either a Democratic or Republican sweep.

Figure 1: Market poll on who will win the 2024 US Presidential Elections



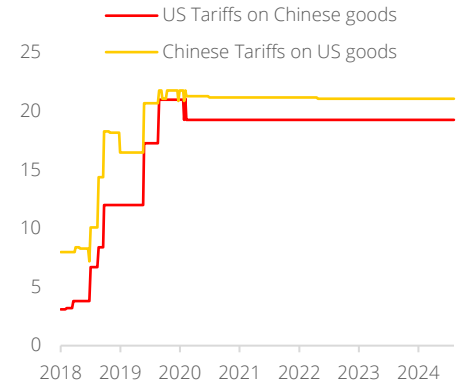
Source: PredictIt, Bloomberg, DBS

Republican sweep may lower it, while a democratic sweep could raise it



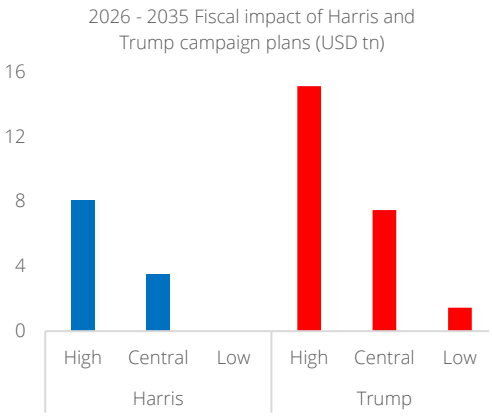
Source: Federal Reserve Bank of St. Louis, DBS

US-China bilateral tariffs



Source: Bloomberg, DBS

Fiscal impact of a Harris or Trump Presidency

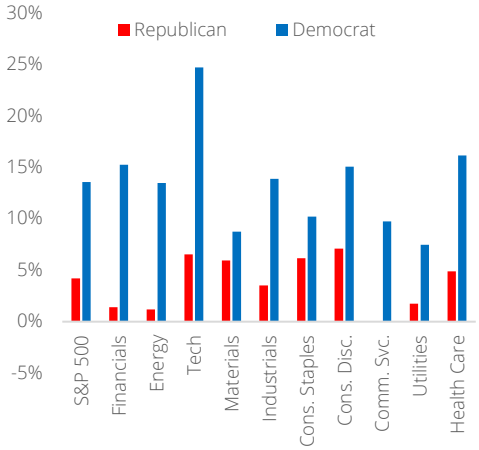


Source: Committee for a responsible Federal Budget, DBS

Macro Implications

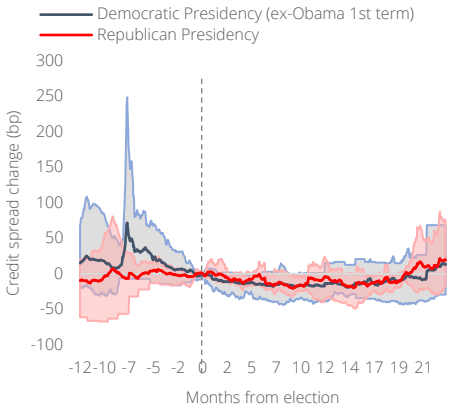
	Republican Sweep	Democratic Sweep
Taxes	▪ In the attempt to revitalise domestic manufacturing and job creation, Republicans to lower corporate tax rates from 21% to 15% for US-based companies. ▪ Extension of the Tax Cuts and Jobs Act (TCJA) across all income levels, further reducing the overall tax burden. While these policies are designed to promote economic growth, they come with the risk of increasing the national debt, especially if the resulting economic growth does not generate enough additional revenue to balance the fiscal impact.	▪ Democrats to raise taxes on corporations and high-income earners to fund social programs. Key proposals include increasing the corporate tax rate from 21% to 28%, alongside raising the top individual income tax rate from 37% to 39.6%. ▪ Extension of the TCJA tax cuts for individuals earning less than USD400k while expanding the Child Tax Credit and Earned Income Tax Credit to provide further relief for low- and middle-income families.
Tariffs	▪ Trump's protectionist stance to be revived, focusing on tariffs to reduce trade deficits and protect domestic industries. This may encompass the imposition of a blanket 10% tariff on most imports, along with significantly higher tariffs of up to 60% on Chinese goods. ▪ The imposition of tariffs, along with renegotiations of trade deals like the USMCA, would aim to revitalise US manufacturing, but also carry the risk of escalating trade tensions.	▪ Harris's policies would likely align with Biden's approach, which has retained many of Trump's tariffs, especially on Chinese imports. ▪ While there is relatively more openness to international trade, the administration is expected to maintain a cautious stance, preserving existing tariffs to protect domestic industries and workers.
Fiscal Impact	▪ Republicans to focus on fiscal policies aimed at extending the Tax Cuts and Jobs Act (TCJA) beyond its 2025 expiration, which could add approximately USD 7.5tn to the national debt. ▪ Republicans to propose significant cuts to entitlement programs like Medicare and Medicaid to help offset revenue losses from tax reductions. ▪ Proposed spending cuts may not be enough to fully cover the costs, and this can potentially exacerbate the budget deficit and raise concerns about long-term fiscal sustainability.	▪ Democrats to focus on increased social benefits, potentially adding USD 3.5tn to the national debt. ▪ Significant investments in childcare, education, and healthcare would be at the centre of their fiscal policy, aiming to boost labour force participation, particularly among parents. ▪ These policies are designed to drive long-term economic growth, although they may contribute to moderate inflation in the short term. ▪ The tax increases that will be introduced may not fully cover the costs of expanded social programs, leading to growing deficits over time.

Average performance of Democratic vs Republican Presidencies on S&P 500 sectors since 1989 (excluding Real Estate)



Source: Bloomberg, DBS

Credit spreads behave well post-elections regardless of presidency



Source: Bloomberg, DBS

Cross-Assets Implications

	Republican Sweep	Democratic Sweep
Equities	▪ A Republican sweep would create short-term opportunities for tax-sensitive sectors, with expected corporate tax rate cuts of 15%, deregulation across various industries, and increased tariffs on imports, particularly from China. Sectors like energy, transportation, and financial services stand to benefit from lower taxes and reduced regulatory burdens. ▪ Additional tariffs could boost US manufacturing especially in the pharmaceutical, semiconductor, and renewable energy sectors through competitive advantages and tax cuts. However, these gains may be short-lived due to the retaliatory nature of global trade, which can increase costs and disrupt production for companies reliant on global supply chains.	▪ Harris has positioned herself as a leader who aims to blend continuity with Biden's policies while also injecting her own distinct vision for the future. ▪ Significant deviations from current policies are unlikely, expect enhancements for existing initiatives. Key policies such as the Affordable Care Act, the Inflation Reduction Act, the CHIPS Act, and the Infrastructure Investment and Jobs Act will continue to benefit crucial industries like healthcare, semiconductors, and clean energy.
Credit	▪ The predominant assumptions of a prospective Trump presidency revolve around runaway federal debt (stemming from unfunded corporate tax cuts), and hence higher 10Y UST yields. ▪ Our quantitative examination of past Republican presidencies, however, reveals that the prevailing narrative warrants investigation. Empirically, UST yield curves tend to flatten under past Republican presidencies, with 10Y UST yields inhabiting lower ranges under Republican presidencies vis-a-vis Democratic presidencies, an observation which also echoed near the end of Trump's first presidential term. ▪ Drastic unfunded tax cuts under a second Trump term could amplify deficits and introduce further risk premiums to US Treasuries, which suggests that investors should continue to avoid ultra-long duration trades like 30Y bonds. We also see a likelihood for Trump to revive tariffs which, in 2018, had in fact sent 10Y UST yields tumbling following aggravated trade tensions. Note also that Trump's business-friendly inclinations had been	▪ A Democratic victory would be the voters' bid for stability. As markets are already well-acquainted with the incumbent's policies and views, we believe the market impact of a Democratic victory would be credit neutral. ▪ Although Kamala Harris' proposals to raise corporate taxes could hit the bottom line of US companies, we note that interest expenses are ultimately paid from pre-tax earnings which would impact credit more moderately due to its seniority in the capital structure. ▪ The Fed will likely stay on an undisturbed course towards its 2% inflation target and move ahead with the rate-cut cycle. Our empirical assessment shows gradual steepening of the UST yield curves 1 year after election under past Democratic presidencies. Taken together, a post-election bull steepening may gradually manifest, which favours the front end at the margin.

supportive of risk assets like corporate credit in his previous term.

- Higher credit yields in anticipation of a 2024 Trump victory is a buy-the-dip opportunity for investors, especially in the 7-10 year duration segment.

Steepening as Trump's odds rise

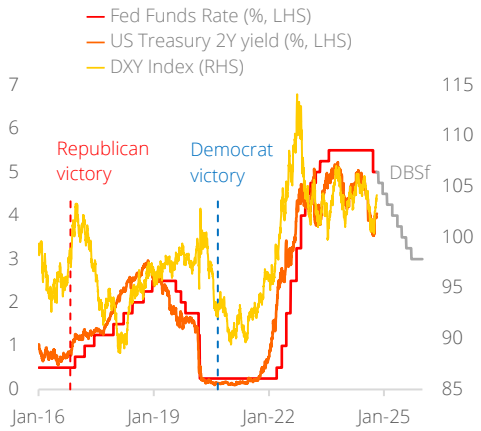


Source: Bloomberg, DBS

Rates

- Trump's victory is currently reasonably anticipated by the betting markets, which have assigned odds higher than 60% of him retaking the Presidency in November.
- Trump is widely considered to be looser on the fiscal side. Issuances worries would likely prompt the curve to be somewhat steep as investors demand a premium. Moreover, there is the added complexity that Trump would likely add more pressure on the Fed to cut rates.
- If rates get driven lower than they otherwise should be, inflationary pressures could re-emerge, compounding tariff inflation worries, leading to upward pressure on the back of the curve.
- A Democrat victory would likely be more of the status quo. Harris is the frontrunner now that Biden has dropped out, but her odds of victory is still hovering around 40%.
- A Democrat victory will temper deficit worries somewhat and fiscal deficit expectations should not differ too much from the CBO's projection of 5-6% over the coming decade.
- However, there should be less tariff worries, less worries on Fed intervention and accordingly, less worries on inflation. Curves would be relatively flatter and yields relatively lower under a Democrat victory compared to a Trump victory.

Next US presidential term will be about Fed cuts, not hikes

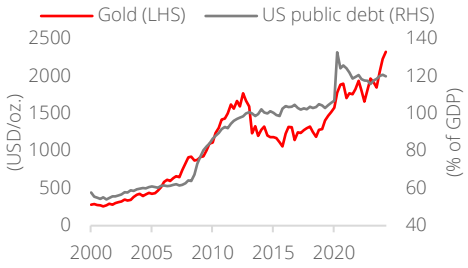


Source: Bloomberg, DBS

FX

- In the short term, USD bulls want to re-enact the greenback's year-end rally on a Trump-led Red Wave at the 2016 election. They believe higher fiscal spending and tariffs could reignite inflation and keep US interest rates relatively high.
- However, the UK mini-budget crisis illustrated how rising government bond yields could expose currency vulnerabilities, mainly if they reflect an unsustainable fiscal situation.
- A second Trump presidential term could hurt the USD's coveted reserve status if he undermines the Fed's independence and pushes for lower rates. Trump will also weaponise tariffs and step up efforts to reshore manufacturing activities and jobs to America while complaining that Japan and China seek unfair competitive advantages via weaker currencies.
- Speculators noted that a Democratic sweep in the 2020 elections led the USD lower for the rest of the year.
- However, the circumstances that led to the USD's rise in the first two years of Biden's term are missing. Biden's back-to-back fiscal boost to tackle the COVID-19 pandemic led to exceptional US growth that required aggressive Fed hike rates to rein in decades-high inflation.
- In contrast to the last two presidential terms, Harris' term will start with falling, not rising, interest rates. With Harris respecting the Fed's independence, the Fed should keep reducing interest rates towards neutral in 2025 based on its projection for a soft landing in the US economy, allowing inflation to decline towards the 2% target. In such scenario, the USD's recovery is likely to lose momentum.

Fiscal deficits are expected to rise under both Trump and Harris, this will be a tailwind for gold

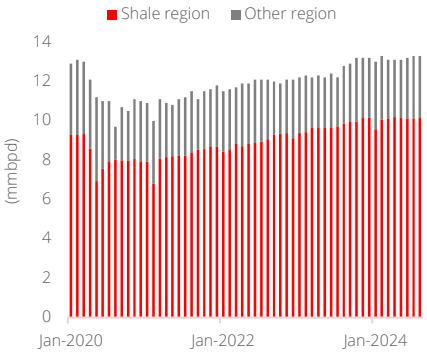


Source: Federal Reserve Bank of St. Louis, Bloomberg, DBS

Gold

- The immediate impact of a Republican victory on gold should be a positive one as Trump's adversarial stance on geopolitics will likely boost gold's safe haven appeal.
- Trump's looser fiscal stance, which is set to increase federal debt by USD7.5tn through 2035, should also be a tailwind for gold as the latter is positively correlated with US indebtedness.
- Overall, gold should be structurally well-supported under a Trump administration. The key downside risk to this scenario is that tariffs and government spending could see a resurgence in inflation and prompt the Fed to raise rates, which will in turn put downward pressure on gold prices.
- While the Democrats may practise more restraint on the fiscal front, Harris's fiscal expansionary policy proposals are still expected to grow federal debt by USD3.5t through 2035.
- Notwithstanding that this figure is smaller than the projections under a Trump presidency, there is still a substantial increase and should contribute positively to gold demand. To the extent that the (relative) fiscal discipline by the Democrats manages to keep inflation at bay, the Fed should be able to maintain its gradual rate cutting cycle, which would be positive for gold.

US crude oil production at record highs, further increases could spell oversupply



Source: Bloomberg, DBS

Commodities

- The economics of a Trump presidency will likely be inflationary; loose fiscal policy in the form of tax cuts and government spending will raise aggregate demand while protectionist policies tighten and disrupt supply.
- This suggests the impact on commodity prices will likely be to the upside, though different sub-asset classes will experience different nuances. The main exception to this is energy as Trump's pro-fossil fuel position will likely see the easing of environmental regulations and make it easier for energy producers to ramp up oil and gas production, thereby lowering energy prices.
- Conversely, his combative stance towards the energy transition may see parts of the Inflation Reduction Act (IRA) repealed, which will have a negative impact on the demand and prices of green metals.
- A Democrat victory should see a relatively tighter fiscal stance, fewer protectionist policies, and consequently a smaller impact to budget deficits and supply chains.
- In such a scenario, inflationary pressures will be lower, and commodity prices should maintain more of a status quo trajectory. Demand for green metals will likely stay supported from clean energy investments and associated tax credits under the IRA.
- Energy prices should also remain more stable under the Democrats as Harris is unlikely to dole out the same regulatory concessions that Trump would to energy producers; this should keep supply more constrained and prices on the higher side.

Look beyond short-term volatility and focus on long-term secular trends. In conclusion, predicting election outcomes and their market impact is inherently complex, as campaign promises often face challenges in execution due to shifting political, economic, and global circumstances. Therefore, it is crucial to look beyond short-term volatility and focus on long-term secular trends like the rise of AI, which can provide sustainable growth regardless of political outcomes.

DBS

Over the past several years, technology has consistently been one of the best-performing sectors under both Presidents Trump and Biden. The resilience and rapid advancements in areas like artificial intelligence, cloud computing, and cybersecurity have proven that the technology sector remains a key driver of economic growth, regardless of which party holds power.

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