Eye on the Market
Update on US Presidential Election

Volume 16, Issue 6 9 November 2016

Donald Trump is US President-elect

Outcome: Trump presidency and the Republican Congress

- The 58th United States (US) presidential election was held on 8 November 2016.
- As of 3 a.m. ET, Trump won 279 electoral college votes to Clinton's 218. A minimum of 270 votes is needed to win. He was victorious in key swing states of Florida, North Carolina, Ohio and Pennsylvania.
- A clean sweep for the Republicans as they keep control of both the House and the Senate. The Republicans held 51 seats in the Senate against 47 for the Democrats. They also held 235 seats in the House vs Democrat's 191, clearing the 218 needed for victory.

Market Responses

- After a sharp knee jerk reaction, financial markets rebounded partially after Trump delivered a surprisingly conciliatory acceptance speech.
- S&P futures fell to a low of more than -5%, before inching back up to a 1.9% drop.
- Over in Asia Pacific, the Japanese Nikkei fell 5.36% to 16,251.54, while Hong Kong's Hang Seng is down 2.16% to 22,415.19.
- The Mexican peso plunged to a record 20.78 per dollar before recovering to 20.02 per dollar and was the worst performer among currencies worldwide. Japanese yen gained 1.6% as investors seek safe havens.
- Gold jumped more than 4.1% to US$1,327 an ounce before falling back to around the US$1,300 level while US WTI crude futures fell to a session low of $43.07 per barrel, before paring losses to trade 1.04% lower.
- Sovereign bonds rallied, pushing yields on 10-year US Treasury notes down as much as 12 basis points to 1.75%, the largest drop since Brexit, though they too pared back slightly to stand at 1.85%.

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What's next?

- Single party mandates can ease some legislative processes, but can also lead to reduced party and fiscal discipline. That said, even within the Republican party, there are also widely reported policy differences especially on matters of trade and defense. This could temper Trump's agenda and prevent highly disruptive policies.
- Historically, voters have been quick to punish failing mandate administrations, and single-party majority Congresses. This could lead to a desire for the Republican party to deliver better than expected economic and market outcomes.

Trump's policies

- Donald Trump's economic policies center on tax cuts for households and firms, expanded infrastructure spending, and unspecified offsets in other public spending.
- He advocates reduced regulation, but more Congressional accountability and oversight of the Fed.
- Trump could further restrict immigration. He may also try to renegotiate many existing trade agreements, and especially challenge China on trade and currency policies.

Market Impacts and Investment Implications

- **Growth**: Trump win risks slower growth or recession if trade is restricted and fiscal expansion plans curtailed. Uncertainty alone could hit the economy. Global growth will also be impacted if uncertainty rises, US growth is hit and US financial conditions tighten.
- **USD:** Increased uncertainty about the US outlook might trigger some capital flight, but a risk off environment traditionally helps the US$. A Trump victory would boost the traditional safe-havens (JPY, CHF) and hit EM currencies.
- **Rates:** In the near term, higher risk aversion could cause Treasury yields to fall. If the Trump administration succeeds in expanding fiscal policy aggressively, this may lead to significantly stronger growth in the US in the short term and higher inflation, which may require more aggressive rate hikes by the Fed.
- **Credit:** Overall risk aversion could drive credit spreads wider and outflows.
- **Equity sectors:** Infrastructure and Defense are likely to benefit from expectations of increased

spending although the actual earnings impact may take longer to materialise. Proposed tax cuts can boost the take home pay of Americans and benefit the consumer discretionary sector. Stricter immigration rules may negatively affect industries that reportedly have high shares of unauthorised immigrants. This would include the construction as well as the leisure & hospitality sectors. At the same time, the increase in infrastructure spending can have a positive impact on the construction sector and provide some offset. Citi analysts are positive the technology sector which has historically shown that it can perform well regardless which party wins the Presidential election. However, the tech sector could come under some pressure if the program which grants temporary visas to skilled workers is also wound down on the back of stricter immigration rules.

- **Emerging Market (EM):** If there is greater RMB volatility or significantly slower China growth as a result of increased trade protectionism led by the US, that would have a negative spillover effect on the EM economy and assets. Within EM, Asia looks most vulnerable to a reduction in trade or a rise in tariffs, in particular China, Korea and Taiwan. This is because EMEA and Latam are primarily exporters of raw materials while Asia exports more consumer or intermediate goods. On the other hand, a stronger dollar may cause current account deficit fears to resurface. On this front, Latam would be most vulnerable. If the dollar strengthens and leads to capital outflows from EM, this could tighten financial conditions in EM. Historically, a stronger USD is negative for EM.

Investment Strategy

- Much is uncertain, but the election results and policies that follow could well change the fundamental outlook for the US and world economy. Like the period following Brexit, Citi analysts are carefully reassessing our views rather than reacting abruptly in disorderly market conditions. We will be paying careful attention to statements from Donald Trump on his immediate priorities now that he is President-elect.
- While we expect market volatility in the near term, historically, the post-election 1-day return of markets has been poor predictors of market performance over the next 12-months. Fundamentals such as earnings growth ultimately drive markets over the longer term.
- Citi analysts continue to advocate the benefits of having a multi-asset, diversified portfolio to investors. This can potentially limit the downside in volatile markets and help investors stay invested over the long term.

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Other Sources: Citi Research, Datastream, MSCI, Bloomberg, 9 November 2016

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