US presidential election
Nikko AM's views

6 November 2020

IMPORTANT NOTICE: The contents within this compilation were written on or before 6 November 2020 and are based on facts known at the time of writing. The compilation will be updated without notice upon new developments.

Introduction

In order to gain a range of perspectives on the US presidential election, Nikko Asset Management has gathered the views of the following experts and investment teams, representing many of our major asset classes and geographical regions.

- John Vail, Chief Global Strategist
- Rob Samson, Deputy Head of Global Multi-Asset (multi-asset)
- Asian fixed income team (Asian fixed income)
- Ashwin Sanketh, Senior Portfolio Manager (Asian equities)
- John Sorrell, Head of Credit, Australia (Australian credit and rates)

We hope that this range of views will provide a useful reference to readers as they navigate the global financial markets.

John Vail, Chief Global Strategist

So far, it seems the odds are favouring our prediction since June that Joe Biden would win the Presidency but the Republicans would control the Senate. The conclusion, however, is far from assured and will likely take two months to confirm. In the meantime, both equity and bond markets are revelling in our scenario of a toned-down Democratic stimulus plan, but there is a significant chance that roadblocks to such will occur. Although Biden, even without control of Congress, would have the ability to cancel all of Donald Trump's executive orders, his ability to issue his own orders may be blocked by regional judges. Even certain regulatory changes may be blocked in the same way that Trump's were often blocked. One thing seems nearly certain, the media business will continue to thrive as all of this uncertainty proceeds and that the US will likely become an even more divided country.

Many businesses can thrive in such a stalemated situation as long as there is continued fiscal and monetary stimulus, but no major civil unrest. In that regard, US 3Q earnings have been extremely good as costs continued to be pared and pricing power seemed very strong in many industries. Advertising costs and product discounting seemed particularly cut in many industries. Tech hardware and software demand surged particularly impressively, although some of that for components was pre-sanction demand from a major Chinese manufacturer. Auto companies reported much better profits than expected due to demand for high priced models and curtailed costs. So far in the 4Q, there seems little reason to expect earnings to disappoint, and in the end, corporate profits and their future outlook are the main determinants of equity performance. One area of concern is the lack of market attention to the fact that many recent mega-mergers, particularly in the tech sector, may be blocked on anti-competitive grounds.

Japanese equities should not deviate too strongly from the US trend, as both presidential candidates wished to maintain stable relations, and global economic trends are now highly favouring Japanese companies.

Rob Samson, Deputy Head of Global Multi-Asset (multi-asset)

The so-called "Blue Wave", with Democrats taking both the White House and the Senate looks like it will fail to materialize, as it appears the GOP is fairly safe in maintaining its majority in the Senate. In positioning terms, the Blue Wave has been closely associated with the "reflation trade" suggesting higher bond yields and a rotation from growth to value. As markets readjust to a different reality, growth stocks are predictably outperforming value on the back of compressing yields.

While the Blue Wave is unlikely to materialise, Joe Biden does appear to be leading, suggesting a divided government. This would lead to "gridlock", all but ending the Blue Wave plan for a major fiscal spend which was the key driver lifting bond yields and a rotation from growth to value. Even if Donald Trump does manage to win, the outcome is much the same – more limited stimulus. We expect positioning to continue with its current adjustment. Over the near-term, growth should outperform value and US Treasury yields will likely stabilize at lower levels. Emerging markets may give back some of their recent outperformance. China would clearly benefit from a Biden administration as few see the same degree of aggression as Trump in fighting the trade/tech war.

Is the reflation trade over? We don't think so. While a Blue Wave promised a larger and faster fiscal spend, stimulus is still on the horizon, whether from a Biden or Trump administration. And, importantly, monetary policy still remains very supportive. Monetary policy, as well as fiscal policy, in the rest of the world remains supportive, while demand—particularly from China—also continues to improve. COVID-19 headwinds remain, including recent lockdowns in Europe. But we still believe the world is learning to live with the virus, allowing demand to normalize. This will accelerate next year when a vaccine becomes available. Over the longer term, we believe these reflationary conditions still support a weaker dollar, higher yields and some degree of rotation from growth to value.

Asian fixed income team (Asian fixed income)

The outcome of the 2020 US presidential elections will undeniably be of greater importance to Asia compared to previous ones in recent history. As markets continue to await the final results and the possibility of a contested result, we may see risk-off sentiment dominating, with bonds yields at steady to lower range.

Running up to 3 November, financial markets warmed up to the idea of an economic bounce in the event of a Biden win. This notwithstanding, we believe the key factor to sustain the positive risk tone post-elections is the outcome of the Senate races, as this would heavily weigh on what the next US president may or may not be able to accomplish in office. In the event that the Republicans maintain control of the Senate, markets could see some short-term weakness. In the medium-term, however, we expect improvement in overall risk sentiment on the assumption that Joe Biden will be more predictable in his approach to both trade and foreign policies.

With regard to monetary policy, we see it unchanged in the near-term, as the Federal Reserve remains independent, acting within their mandate of employment and inflation. The Fed has avowed and adopted an average inflation targeting policy. Hence, we do not expect an interest rate hike to be announced until full employment is achieved. Notably, this could be seen sooner under a Biden presidency, on the back of more fiscal stimulus, than in another Trump administration.

Strained US-China relations have been a key overhang for Asian credits in past years. We see rhetoric on China remaining generally unchanged regardless of election results, as the challenge to US world leadership persists. Nevertheless, a Biden presidency is likely to engage China through proper diplomatic channels, which will have the effect of reducing volatility and uncertainties in bilateral relations. This will in turn somewhat reduce risk premium in credits, particularly those in the technology and export oriented sectors.

On Asian rates, we see a supportive environment as US rates rise may be slower than those priced for a Democratic "Blue Wave" win across the US executive and legislative houses. We also expect EM inflows into local markets to improve over time on declining political uncertainty. Overall, we continue to favour countries with high carry such as Indonesia, where flows have begun to return. In the medium term, we expect Asian currencies to appreciate against the US dollar, with the Chinese yuan, South Korean won, and Singapore dollar—being relatively more trade-sensitive—outperforming. The Malaysian ringgit and Thai baht may lag peers, on the back of rising political risk in their respective countries, whereas the Indonesian rupiah is likely to do comparatively better as it benefits from EM inflows.

Ashwin Sanketh, Senior Portfolio Manager (Asian equities)

There are no US citizens on Nikko AM's Singapore-based Asian Equities team. We also do not live in America, nor are under US jurisdiction. Essentially, a country in the west is electing its president. So why are we writing about it?

Because the US was, until recently, the "leader of the free world". Because the US was, until recently, the world's only superpower. Because the US is, still, the world's largest economy and defence superpower. The last four years under President Donald Trump have been eventful to say the least—he brought a "deal-making" approach to his office, withdrawing the US from multilateral agreements like the Paris Accord, pulling out from the WHO amid the worst pandemic in a century, inciting several trade wars and restricting immigration. If Trump wins a second term, one could expect more vitriolic rhetoric and policy volatility. However, if Joe Biden wins, there is scope (perhaps more hope) that some of this will be undone, and a more "politically correct" approach might be adopted. But Trump's presidency has also set in motion events that will likely outlast his presidency (even if he doesn't win a second term) particularly apropos China. And therein lies the answer to why we, and indeed, the world at large, cares who the next US president is.

But who the next US President is matters less than you might think.

Institutions, rules and processes put in place limit the powers of the US president; this is not unique to the US. And we have these to thank for the last four years not being any more chaotic. So what matters more is which party has control of the Senate and the House of Representatives, and it appears those elections are also too close to call. A betting person would go with a Republican controlled Senate and a Democratic controlled House. Thus, regardless of who sits in the Oval Office, it is unlikely to be smooth sailing. Also, he is likely to approve greater fiscal stimulus (the magnitude may differ), which the US Federal Reserve will likely monetise. A weaker US dollar is likely.

That China is aware of the bipartisan support for policies to straitjacket its technological progress is old news. That it is taking steps to mitigate the fallout is also not new. And given the country's track record in getting done things that really matter to it, give or take a couple of years and a few hundred billion renminbi, one wouldn't bet against it. So the world's second largest economy will march to its own beat.

All things considered, for investors in Asia ex-Japan markets, a weaker US dollar has positive implications. The relative stability in Asia will also stand the region in good stead, as neither trade nor politics will change meaningfully regardless of who occupies the Oval Office. Asian countries have, by and large, handled the COVID-19 pandemic better than their western counterparts and are now emerging from that nadir. Further, Trump's "America First" stance has already forced US allies—South Korea and Taiwan—to take stock of their relations with China, the largest economy in Asia, and one that is still growing faster than most economies anywhere.

It would serve us well to remember a quote attributed to famous American actor Will Rogers: "After elections and after marriage, people rarely get what they expect".

John Sorrell, Head of Credit, Australia (Australian credit and rates)

After a day of counting, it seems that polls overestimated Joe Biden's support, but what initially looked like it could be a Donald Trump victory has faded, and it now seems reasonably likely that Biden has won over half the popular vote and will scrape in sufficient Electoral College votes. Final results willdepend on the completion of counting absentee voting, which so far has heavily favoured Joe Biden. The Democrats appear to have retained the House of Representatives and may strengthen their position in the Senate, but the Republicans will likely maintain control. The lack of control of the Senate could heavily impact Biden's ability to implement his agenda, especially in light of an unsympathetic Supreme Court. Irrespective of whether Biden gets across the line, the US would appear to have a quite dysfunctional government.

Given the lack of serious policy debate and the focus on personality during the campaign, Biden's actual agenda is vague, although it might be expected to focus first on a stimulus package and a more active effort against the pandemic, followed by areas such as healthcare and the environment. For those outside the US, it may be most important to focus on the following five areas: the management of the pandemic; the US economy and its impact on the global economy; the role of the US as a global player; the approach to protectionism, and the attitude to environmental issues. The pandemic and the economy may hinge on the immediacy of the vaccine, although more focused action may help slow the spread. America's global role will be challenged by the distraction of conflict between the presidency and Congress, which will encourage a more inward-looking perspective. This lack of focus could create a favourable environment for China (and to a lesser extent Russia) to be increasingly assertive, but the Democrat's less transactional focus on the moral high ground could pressure Biden to be more outspoken on controversies such as Hong Kong or the treatment of the Uighur minority and may also limit the willingness to wind back Trump's more protectionist trading policies. As regards the environment, Biden will be more focused on re-implementing controls and on reconsidering the Paris Accord, which the US formally exited yesterday. However, ratifying any formal agreement might be challenging with a hostile Senate.

More specifically, for Australia, given US internal distractions, we might expect pressure from China to be maintained, with limited expectation for US support in any disagreement with China. A more focused US view on climate change and a reconsideration on the Paris accords may increase the pressure on Australia's current government to become more active environmentally. However, for Australian fixed income, the impact of the US election outcome is much smaller than the ability to bring the pandemic under control. An effective deployment of a successful vaccine, or a turning of the tide of infections will do more to boost Australia's economy than any other single factor. As such, whether the winner is Biden or Trump will have limited impact on the expectation for interest rates, where Australia is likely to maintain low rates (even possibly negative). As for credit spreads, economic conditions similar to today's would normally be expected to put pressure on spreads, but sovereign support for corporate borrowing and the search for yield are expected to limit spread widening except in clearly impacted sectors such as aviation.

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