US Election: Initial Reaction

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Donald Trump returns to the White House, after a hotly contested election. There was some delay in acknowledging the result in 2020 but the winning margin is so significant on this occasion, the result is certain. Trump becomes the first Republican candidate to win the popular vote since 2004 and will become the 47th President of the United States.

In addition, the Republican party has retaken control of the Senate. The race for control of the House of Representatives is still ongoing and for now, too close to call. On balance, due to the scale of the winning margin of the popular vote, we would expect that the House of Representatives will go to the Republicans as well. However, this is very much uncertain at this stage. In any event, Republican majorities in Congress would likely be slim, and the passing of fiscal legislation will take time and may be vulnerable to different policy priorities within the party.

We expect the playbook of 2017 to be revisited and, as per Trump's comments on the campaign trail, tariffs to be an early priority, which can be passed by executive order. Such tariffs would likely pressure the manufacturing sector and will push up imported inflation. All things being equal, the latter point will likely see the Federal Reserve (US central bank) deliver a shallower interest rate cutting regime than was expected by markets previously. Additionally, Europe is likely to be a more of a target for tariffs in this term, which is a negative for growth in the region. The European Commission may respond in a tit-for-tat manner which could weigh more heavily on economic growth potential.

There are of course, potential implications for the conflict in the Middle East and Ukraine with outcomes uncertain. Immigration policy initiatives will also be early on the agenda.

Directionally, markets have responded as one would expect. US equities are higher, particularly smaller and mid size company shares which are more US economy focussed. European equities are modestly higher but underperforming the US. Short-dated bonds yields are lower (prices higher) in Europe as the market expects the European Central Bank to react more forcefully by reducing interest rates quicker to combat any potential negative growth shock. Chinese equities are holding up despite the risk of tariffs however many of company revenues in China are sourced locally rather than offshore. The US Dollar is higher and bond yields are higher (prices lower) due to the market expecting less interest rate cuts from the Federal Reserve than previously expected. Furthermore, Emerging market currencies have underperformed, particularly Mexico which may be in the tariff firing line.

Looking ahead, there is an Federal Reserve meeting this week and we'll be looking to see how they view recent economic data releases and early implications of the election results. The usual approach from the central bank is to wait until policy initiatives are brought into law and this time should be no different, so we expect interest rate cuts to continue for now. There is also inflation data released next week which the market may react more forcefully to, should there be an upside surprise.

Omnis Investment Team
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