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FOCUS NOTES

Republican candidate Donald Trump wins November 8th US Presidential election

Main agenda of the US President-elect
Market reaction to Donald Trump's victory and Republican clean sweep

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Defying the majority of recent opinion polls, Republican candidate Donald Trump was elected to become the 45th US President defeating his Democratic rival Hillary Clinton. He managed to secure more than the 270 Electoral votes required after succeeding to turn around a number of traditionally Democratic states and win the bulk of the so-called swing states including Florida and Ohio. Republicans have also retained the majority in Congress, albeit losing some seats. They managed to hold on to their majority in the 436-seat House of Representatives (the lower house), as was widely expected, and to also gain a slim majority in the 100-seat Senate (the upper house) but remains still short off securing the 60% supermajority.[1] Admittedly, Donald Trump's victory and a clean sweep for the Republic party give execution powers that will purportedly exceed those of outgoing President Barack Obama. Donald Trump's term in office will start with his Inauguration on January 20th 2017. Until then, Barack Obama will hold the presidency.

The main agenda of the US President-elect (as was presented during the election campaign)

Fiscal policy. Donald Trump has proposed an expansionary fiscal policy endorsing, among others: (i) $1trn in new spending over 10 years for infrastructure investment such as roads, airports, public buildings (to be carried out both by the public sector and in partnerships with private corporations), (ii) across the board large-scale tax cuts including a decline in the corporate tax from 35% currently to 15%, reduction in the top personal income tax bracket to 33% from 39.6% currently and elimination of the estate tax; and (iii) one-time overseas corporate tax repatriation holiday (at a discounted rate of 10% compared to 35% currently). According to preliminary and rough estimates, the Committee for a Responsible Federal Budget[2] argues that, assuming that all Donald Trump's policy proposals are implemented, net public debt would increase more sharply relative to current law projections[3]. In more detail, the Committee estimates that Trump's proposals would increase net public debt by c. $5.3trn over a decade taking net public debt to around 105%-of-GDP compared to the Committee's current law projections of 86%-of-GDP, assuming no policy changes.

[1] In the US, the passing of a bill into law requires only a simple majority in both the House of Representatives and the Senate along with the president's endorsement. However, some actions like impeaching, expelling a member of Congress, amending the Constitution, ratifying/postponing a Treaty and overriding a presidential veto, require a supermajority of more than 60% of the seats in either House.

[2] The Committee for a Responsible Federal Budget is an independent, not-profit public policy organization that addresses federal budget and fiscal issues.

[3] Current law projections estimate that, US net public debt is projected to grow from 76%-of-GDP in 2016 to around 86%-of-GDP by 2026 and about 150%-of-GDP by 2050.

Trade. Donald Trump adopted a relatively more protectionist stance compared to his rival Hillary Clinton insisting renegotiation of free trade deals. The Republican candidate argued that US jobs have been lost due to generous trade agreements with other countries such as the North American Free Trade agreement (NAFTA) and trans-Pacific partnership (TPP). If elected, he has vowed to pursue a certain trade policy plan envisioning, among others: (i) withdrawal of the US from the TPP trade agreement that was negotiated and promoted by the Obama administration and awaits ratification by Congress to enter into force[4], (ii) appointment of tough US negotiators; (iii) renegotiation of the NAFTA to secure better terms and, if not feasible, withdrawal from it; (iv) labeling of China as a currency manipulator on the grounds that China's trade practices harm US companies; and (v) consideration to withdraw the US from the World Trade Organization (WTO). In addition, he has promised imposition of large import tariffs (around 45%) of non-energy imports from both Mexico and China.

Foreign Policy. In an interview earlier this summer, Donald Trump appeared to make US military support for NATO member states conditional on whether those states have met their financial obligations to the bloc. According to Article 5 of NATO, an attack on one member is an attack on all.

Immigration. Donald Trump's policy was cited as more radical on immigration compared to that of the Democratic candidate during the election campaign. He has publicly stated that "a nation without borders is not a nation" and has proposed the building of a wall along the US-Mexican border. He has suggested a series of steps that would strength border control, limit ease of entry and create more stringent requirements for hiring from overseas. He has also mentioned deporting all unauthorized immigrants which according to the American Action Forum (AAF) would shrink the labor force by 6.4% over a 20 year horizon. Labor intensive sectors such as agriculture, construction, retail and eating and drinking would likely be the hardest hit.

Fed Monetary Policy. Subject to Senate approval, the US President-elect will nominate among the sitting Governors the next Fed Chair and Fed Vice Chair when the terms of both Chair Janet Yellen and Vice Chair Stanley Fischer expire in 2018. History suggests that it is unusual for incoming Presidents to replace a sitting chair, allowing chairs and vice chairs to serve multiple terms; Democrat Barack Obama reappointed Ben Bernanke for a second term in 2009, first nominated by George W. Bush and Democrat Bill Clinton reappointed Alan Greenspan twice, while Republican Ronald Reagan reappointed Paul Volcker. However, speaking publicly during the election campaign, Donald Trump has left the door open for a possibly replacement of Fed Chair Yellen when her term expires. Whether his preference will lie to the more hawkish side, remains to be seen. In theory, looser fiscal policy in an economy with reduced slack that operates near full employment could lead to increased inflationary pressures, potentially triggering monetary policy to tighten more quickly.

Market reaction to Donald Trump's victory and Republican clean sweep

As expected, Donald Trump's victory and the clean sweep of the Republican party triggered a risk-off mode across the globe on the view that the President-elect will likely attempt to deliver on the core of his programme as soon as his term in office starts. Major Asian bourses recorded sizable losses and European equity markets lost ground in early trade on Wednesday. Hillary Clinton was perceived as the status quo candidate, while investors were reportedly concerned about the potential impact of Republican candidate Donald Turmp's proposals on global growth, foreign policy, fiscal policy, trade and immigration. However, risk sentiment somewhat improved a few hours later following the softer tone Donald

[4] Trans-Pacific Partnership (TPP) trade agreement involves 12 countries, the US and 11 other Pacific Rim nations (Japan, Malaysia, Vietnam, Singapore, Brunei, Australia, New Zealand, Canada, Mexico, Chile and Peru) that represent roughly 40% of global GDP and one-third of world trade. The trade agreement aims to "promote economic growth; support the creation and retention of jobs; enhance innovation, productivity and competitiveness; raise living standards; reduce poverty in the signatories' countries; and promote transparency, good governance, and enhanced labor and environmental protections" via, inter alia, reduced tariffs on certain goods traded between the countries, cooperation on wider issues such as employment practices and harmonization of all sorts of regulation.

Trump adopted in his victory speech compared to that throughout his election campaign. In response, the FTSEurofirst 300 index rebounded recording losses to the tune of around 0.6% at the time of writing (16:00 EET) after falling nearly 2% in early trading. In a similar fashion, US stock futures improved pointing to losses of around 2% for Dow Jones index when it reopens later in the day compared to earlier expectations for a 4% fall. Reacting to the relatively improved tone in global equity markets, long-dated US Treasuries gave back earlier gains with the 10-yr bond yield rising in late European trade to levels above 1.93% for the first time since mid-March after marking multi-week lows near 1.71% a few hours earlier. Market participants' withdrawal from certain US assets also had an impact on Bunds which retained a firm tone due to flight-to-quality though they gave up a significant part of their earlier gains. Short-dated US Treasuries outperformed the long end on the view that in an environment of elevated market volatility a Fed rate hike as soon as next month comes into question. Fed funds futures are currently assigning a probability of around 50% for a 25bps rate hike in December compared to around 85% earlier this week.

Reduced expectations for a Fed rate hike at the December 13-14 FOMC monetary policy meeting pushed the USD lower especially against low yielding currencies such as EUR, JPY and CHF with the JPY leading this rally against the US currency. On the flipside, the USD gained some ground against commodity related currencies such as AUD, NZD and especially CAD given Canada's trade links with the US. Investors need some time to digest the incoming news flow, suggesting that, at this point, it would be hard to attempt any forecast of market moves on a multi-session/week horizon. To this end, upcoming speeches by the US President-elect will be closely scrutinized by market participants, especially with respect to his policy priorities and the composition of his cabinet.

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