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Macro Insights Weekly
US elections and markets

Group Research

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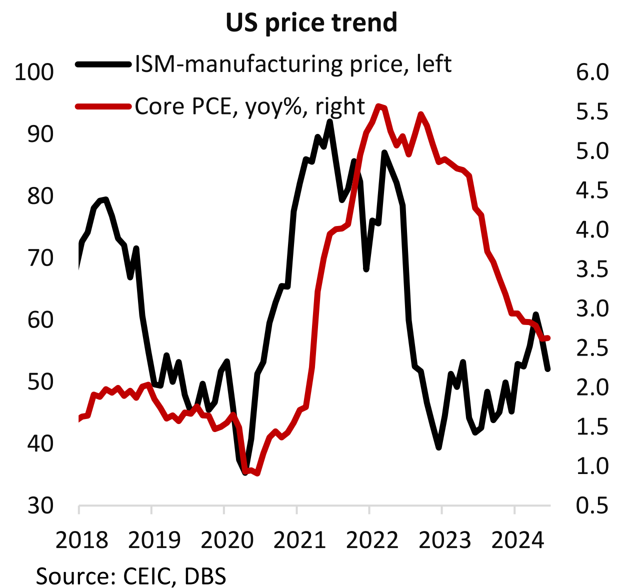
- *Using 50+ years of data, we analyse the relationship between election outcomes and asset returns. Regardless of the winner, elections tend to help equities, while largely neutral for USD and bonds.*
- *The DXY appreciates mildly before the elections and tends to be flat thereafter.*
- *The most robust finding of the study is related to the S&P500, which does well during elections.*
- *It does better in the lead-up to a Republican win, while doing very well after a Democratic win.*
- *The bond market sells off a tad before a Republic win and rallies a tad before a Democratic win.*
- *Given latest data, we have revised up marginally our US GDP growth projection for 2024 (2.3%).*

Chart of the Week: Conditions for the Fed to ease

US inflation markers are back to a downtrend that began more than a year ago. Key measures of inflation like the core PCE and trimmed-mean PCE, both on a yoy and mom, seasonally adjusted, annualised basis, have eased to the 2.6%-2.8% range. We think a path toward 2.5% inflation is sufficient for a couple of rate cuts (Sept and Dec). Fed's justification won't stem from a declaration of victory toward a 2% goal, rather that 5.5% Fed funds rate is too high when inflation and growth are well below 3%.



Source: CEIC, DBS

Commentary: US elections and markets

US presidential elections tend to be consequential for geopolitics and the global economy. But how do markets deal with election-related developments? It is well understood that markets react to the day-to-day news cycle; but what about over a period of one year; do elections leave a lasting impact on assets like the US dollar, the stock market, or bonds? Are their discernible movements before and after the elections?

Using 50+ years of data, covering elections from 1968 to 2020, we analyse the relationship between election outcomes and asset returns. One thing that immediately comes across is that elections spanning major global financial market events are characterised by substantial price swings. In the 12 months after the Nov 2020 elections, the US stock market delivered an astonishing 40% return, but how much of that was related to Joe Biden taking office and passing fiscal support measures, and how much was a function of the post-pandemic re-opening of the economy? Such caveats are key considerations in event studies of this nature.

With Donald Trump expressing a preference for a weak dollar, we find it worthwhile to start the study by tracking the USD. We find that on average, the dollar appreciates mildly before the elections (regardless of a Democratic or Republic win) and tends to be flat thereafter.

DXY and US presidential election

Winner	Returns 12 months prior	Returns 12 months after
Republican	2.5%	0.3%
Democratic	3.3%	0.5%

Source: Bloomberg, DBS, based on US election cycles from 1968 to 2020

In the 12 months after Trump's 2016 win, the DXY index weakened as per his goal, but only by 4%, not material for restoring US manufacturing competitiveness. Trade and tariff war in 2018/19 pushed up the USD, contrary to Trump's objective.

The stock market does well during elections, doing better in the lead-up to a Republican win (+9.9%), while doing very well after a Democratic win (+17.2%).

S&P500 and US presidential election

Winner	Returns 12 months prior	Returns 12 months after
Republican	9.9%	5.1%
Democratic	4.4%	17.2%

Source: Bloomberg, DBS, based on US election cycles from 1968 to 2020

What about the US bond yield, source of much concern given soaring debt and interest payment obligations? Turns out the bond market sells off a tad before a Republic win and rallies a tad before Democratic win, while rallying after a Republic win. But the Republican-win related outturns are disproportionately impacted by 1980s Reagan/Bush era. Since then, other than the GFC-adjacent 2008 election, bond markets have largely shrugged off US elections. Bottomline, election cycles seem to be significant for stocks; for bonds and the dollar, not quite so much.

10-yr bond yield and US presidential election

Winner	Returns 12 months prior	Returns 12 months after
Republican	0.22	-0.48
Democratic	-0.40	-0.01

Source: Bloomberg, DBS, based on US election cycles from 1968 to 2020

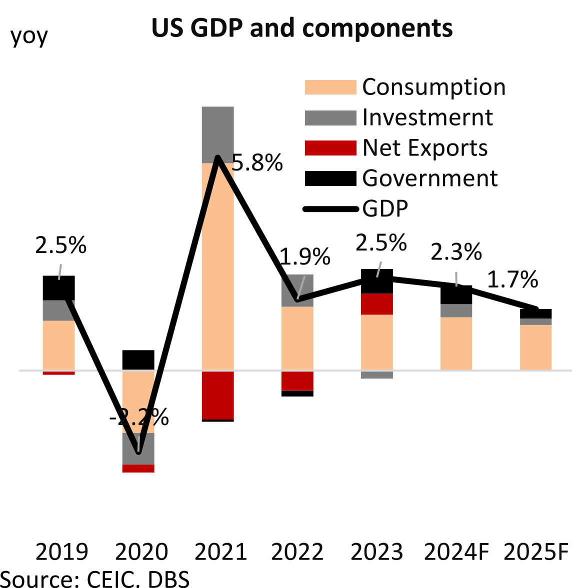
Policy positions of Trump and Harris

Harris	Trump
Inflation	
Supports targeted relief for households most affected by high cost of living. In favour of tax credits for those with spend at least 30% of their income on rent and utilities. Will push for paid family leave and affordable child care.	*Supply side and tariff measures are expected to boost domestic production, in turn lowering inflation. But planned tax cuts, tariff measures, and immigration restrictions could be inflationary.*
Tax and fiscal policy	
Supports Biden's tax agenda to make corporations and high-income households pay more while keeping taxes flat or cutting them for households making under USD400k/year. Has been in favour of low wage earners to be supported through tax credits.	*Would cut corporate income tax to 15% from the existing 21%. Would extend the 2017 Tax Cuts and Jobs Act, given that many of its tax cuts expire at the end of 2025.*
Income support	
Supports raising teachers' salaries substantially. Has advocated for measures to support minority entrepreneurship.	*Proposed exempting tipped wages from taxes.*
Trade	
Opposed TPP and USMCA on the ground that climate related provisions were inadequate. Unlikely to provide relief from prevailing tariffs or ease tech access restrictions.	*Wants to construct a "ring" around the economy, through tariffs of at least 10% on any imported goods. Has threatened to impose a 100% tariff on made-in-Mexico EVs by Chinese firms. Has proposed raising import duties on made-in-China products to as high as 60%.*
USD	
Has expressed no intent to change the status quo on USD or Fed independence.	*Has stressed that a strong USD burdens US manufacturers. May lean on the Fed for lower rates and take punitive FX measures.*
Crypto	
Wants a reset with the Crypto industry. Wants to build a constructive relationship that would set a smart regulatory framework that would help the growth of the entire asset class.	*"If crypto is going to define the future, I want it to be mined, minted and made in the USA." Intends to create a "strategic national bitcoin stockpile" where the government would keep the tokens it holds or acquires. Will fire SEC head Gensler, who has pursued strict crypto regulation.*
Climate	
Strong proponent of Green New Deal and Inflation Reduction Act. Has opposed fracking. Wants to wean the US economy off fossil fuels, while overhauling the nation's energy and transmission infrastructure.	*Considering eliminating EV subsidies. May roll back funding for manufacturing of clean energy technologies and gut provisions like hydrogen and carbon capture tax credits.*

Adjusting our GDP and inflation forecasts

The equity markets may be undergoing some angst over earnings disappointments and elevated valuations, but the US economy continues to deliver strong growth numbers. 2Q24 national accounts release was characterised by better-than-expected numbers. Real gross GDP increased at an annual rate of 2.8%, double that of the 1Q24 outturn of 1.4%. The increase in the second quarter primarily reflected increases in consumer spending, inventory investment, and business investment. Imports increased as well, reflecting rising domestic demand. We are compelled to raise the 2024 forecast based on this data, forecasting a real GDP growth of 2.3% (2% earlier).

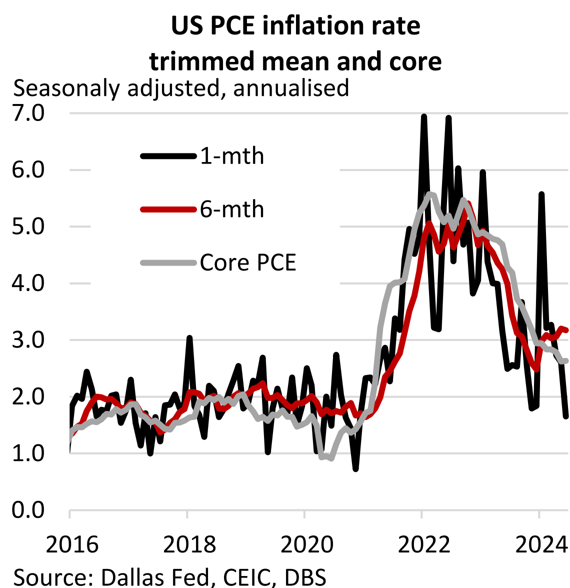
The dataflow is a bit mixed. We see easing PCE inflation, investment-led 2Q growth, soft retail sales, and a marginally cool job market. 2Q24 may well be the high-water mark for growth this year, but we don't see a major correction in demand, short of some financial stability issues.



Source: CEIC, DBS

On the inflation front, the personal consumption expenditure index, the Fed's preferred measure of underlying US inflation, rose at a relatively tame pace in June, which can be seen as encouraging for FOMC officials looking for signs of cooling inflation.

June PCE was up 2.5%yoy, while core PCE was up 2.6%yoy (0.2%mom). Goods prices dropped 0.2% after falling 0.4% in May. Prices for motor vehicles and parts declined 0.6%. Furnishings and durable household equipment prices dropped for a third straight month, while gasoline and other energy goods decreased 3.5%. Clothing and footwear were cheaper for a second straight month. We see the core PCE heading toward 2.5% toward the end of this year, although further disinflation may be hard to achieve, given that services inflation is yet to be tamed decisively.



Source: Dallas Fed, CEIC, DBS

Signs of cooling in the labour market are starting to translate into less purchasing power. Wages and salaries rose 0.3% in June, half the prior month's pace. On an inflation-adjusted basis, disposable income growth slowed to 0.1%.

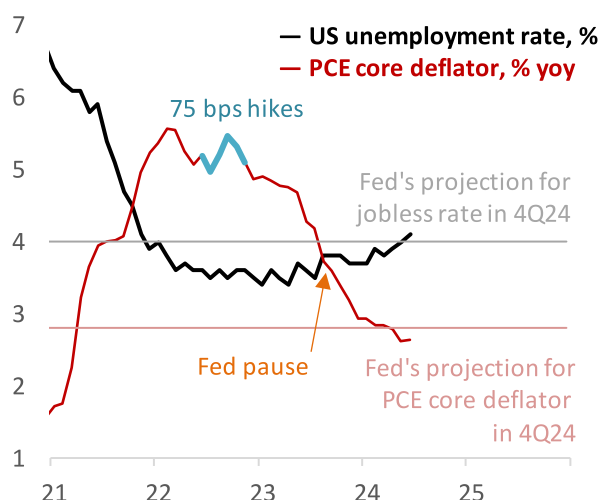
Taimur Baig

FX: Turmoil amid conflicting factors

The DXY Index was volatile last week, trading in a tight 104.1-104.6 range, due to conflicting currency market themes. Despite the futures market pricing a more than 100% chance for a Fed cut in September, the USD's outlook was obscured by the twists and turns in the US Presidential Elections and the unwinding of JPY carry trades. Additionally, the JPY and the CHF became havens amid a sell-off in tech stocks.

At its FOMC meeting on July 30-31, the **Fed should keep the door open to lower interest rates but avoid endorsing** the market's bet for **a September cut**. The guidance on the timing will likely come at the Kansas City Fed's Jackson Hole Symposium on August 24-26, following the US unemployment rate data on August 2 and the CPI data on August 14.

The Fed is getting nearer to lowering rates



Sources: DBS Research, Bloomberg data

USD/JPY plunged from 162 to 152 in the fortnight to July 25. The sell-off was triggered by the third decline in US CPI inflation fuelling bets for a Fed cut in September, suspected currency interventions from the Bank of Japan, and US Republican presidential candidate Donald Trump's decrying of the JPY's massive weakness.

Japan sees an opportunity to reverse the JPY's weak fortunes at this week's BOJ-FOMC meetings on July 31. The Liberal Democratic Party believes that the JPY's multi-decade lows sank the Kishida Cabinet's approval ratings by adding to the consumers' cost of living crisis and hurting small and midsize companies via higher raw and energy prices. Over the weekend, Japan successfully pushed for the G20 joint communique to include the commitment against excessive foreign exchange volatility. Given the potential for a dovish Fed tilt, the **BOJ will need to heed the call** by LDP Secretary-General Toshimitsu Motegi **for an unequivocal resolve to normalize monetary policy**. We see the BOJ halving its monthly JGB purchases to JPY 3 trillion but **markets want the BOJ to hike rates a second time this year**.

Following the Labour Party's big victory at the UK snap elections on July 4, GBP/USD rallied from 1.2760 to 1.3009 on July 17. However, **GBP/USD depreciated over the past fortnight by 0.9% to 1.2867 from a global unwinding of JPY carry trades.** GBP/JPY plunged for a third week by 2.7% to 197.83 on July 26, its lowest since June 4, ahead of the **25 bps rate cut expected at the Bank of England meeting on August 1**. The commodity-led currencies were hit hardest by the unwinding of JPY carry trades last week because of Canada's surprise interest rate cut and New Zealand's dovish tilt amid a weaker Chinese economy.

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