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US presidential election: how it will impact US economy and financial markets

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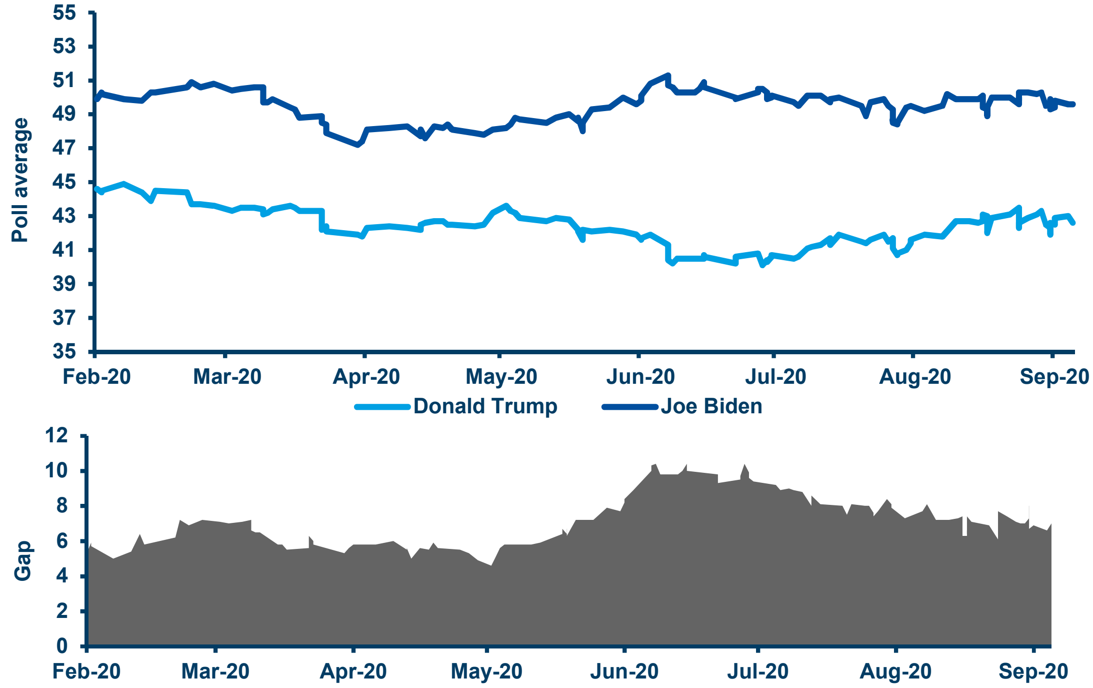
- ***US presidential election outcome:*** *Joe Biden has enjoyed a remarkably stable lead in the national polls this year. Currrently, he is leading President Trump by 7.6%, according to our poll of polls, down from a peak of 10.4% in June. However, we believe the race is much closer, at around 50/50, with a small Biden edge.* ***The outcome remains uncertain for different reasons****. Firstly, while Biden's lead in the national polls is significant, his lead in the swing states is only 3.9%, and in many states, his lead is within the margin of error. We expect the election to be determined by a handful of swing states, including Arizona, Florida, Georgia, Michigan, North Carolina, Pennsylvania and Wisconsin. In addition, turnout will be critical. We are anticipating record turnout, with the highest number on record voting by mail. Overall,* ***the public has a net negative approval rating for Trump of -9.6%,*** *according to our poll of polls. However, Trump enjoys a positive net approval rating of 4.0% on his handling of the economy, which could help him gain more popular support if the economy gains momentum.*
- ***Key themes for the candidates:*** *There are three main themes in Trump's campaign: law and order, China, and Biden's fitness for office. Biden is campaigning on economic policy ("Build Back Better"), healthcare, racial justice and morality. Biden is planning another fiscal stimulus package to address immediate economic issues tied to the pandemic. Also, he has plans for a major infrastructure investment and supports a modified version of the Green New Deal. Biden plans to boost Obamacare and prescription drug reform. Both candidates will have to deal with the long-term issue of rising inequality.*
- ***Investment implications****:* ***The dollar should stay weak in the medium term****, due to the re-emergence of twin deficits and an escalating debt/GDP ratio, together with the Fed's long-term commitment to near-zero rates.* ***If the prospects of a Trump re-election increase, we could see the dollar appreciate temporarily*** *based on concerns regarding the prospects of heightened trade tensions and broader geopolitical uncertainty. In any case, we expect to see near-term market volatility around election time. The greatest risk to short-term market dynamics is an undecided race.* ***Depending on the winner, certain market sectors may respond differently.*** *Big tech, defense, financials and carbon energy sectors are likely to perform better under Trump while renewable energy and infrastructure-related sectors will be winners under Biden.* ***Under both scenarios****, we believe that* ***ESG investing will gain increasing traction*** *globally, with rising investor pressure for increased disclosure and enhanced ESG practices, supported by accelerating ESG equity flows, including in the United States and despite Trump's backtracking. Should Trump be re-elected, the theme will continue to gain traction, albeit not at the same level should there be a Democratic sweep.*
- ***International relations****:* ***US-China relations are likely to prove difficult****. In addition to the ongoing tech war, capital war on foreign holdings, and re-shoring of the global supply chain, the current situation in Hong Kong introduces the risk of US sanctions on Chinese banks and an exclusion from the dollar system. Hence, the* ***phase-one trade deal appears on hold for now****, with little hope for a phase-two deal. Accidental confrontations in the South China Sea or in the Taiwan Strait might push the situation to a point of no return.* ***US-EU relations*** *have deteriorated significantly under Trump. Some improvement is likely under a potential Biden presidency while further trade barriers may be decided on if Trump is re-elected.*

The US presidential election is expected to be one of the key market drivers in Q4: what are current market expectations and what is your view?

Joe Biden has enjoyed a remarkably stable lead in the national polls since the beginning of the year. According to our poll of polls, Biden leads President Donald Trump by 7.3% as of 15 September 2020, little changed from before the Democratic and Republican conventions which took place this summer, when Biden's lead was 7.5% on 5 August 2020. However, Biden's margin has shrunk from a peak of 10.4% reached on 23 June 2020.

Biden has led Trump since beginning 2020, US general election poll average



Source: Amundi based on polls of polls as of 22 September 2020.

"The trajectory of the race remains fluid and potentially volatile as we head into the final stretch of the campaign".

The political betting sites also have Biden as the favourite. Predictit — one of the leading betting sites — recently forecast the odds of a Biden victory at 60% while Iowa Electronic Markets showed a smaller edge, at 52% as of 13 September 2020. However, despite the stability in the national polls and the betting site expectations, we **believe the race is much closer**, at around 50/50, with a small Biden edge. **The outcome remains uncertain**. **The trajectory of the race remains fluid and potentially volatile as we head into the final stretch of the campaign** for different reasons:

- Firstly, as former Democratic presidential candidates Al Gore and Hillary Clinton learned the hard way, it is not the popular vote that elects a president in the United States in the end, but who wins the electoral college. While Biden's lead in the national polls is significant, his lead in the swing states is only 3.9%, and in many states, his lead is within the margin of error. **We expect the election to be determined by a handful of swing states and we are focusing on Arizona, Florida, Georgia, Michigan, North Carolina, Pennsylvania and Wisconsin.** Biden's lead in Florida and North Carolina is within the margin of error; his lead in the other states remains nominally above it.
- Secondly, **turnout will be critical**. **We are anticipating an all-time record turnout**, with the highest number on record voting by mail. This could potentially account for one-third of all votes cast. We estimate that among Biden supporters, only 25% of voters expect to vote on election day compared with 67% of Trump voters. This begs the question of whether there are adequate resources in place around the country to handle the number of votes by mail. Mail-in ballots can represent a fraught issue, with the challenges of counting of split ballots (with votes for candidates of different parties in different races) and the accuracy of filling out the ballot. Regarding Trump, he is likely to bring more voters to the polls who do not normally vote in elections. This was his path to victory in 2016. David Wasserman from the Cook Political report estimates that among those who did not

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vote in the 2016 election, some 60-65% were the likely Trump voters (non-college educated white voters) in the swing states of Pennsylvania, Michigan and Wisconsin.

- Moreover, the **debates are likely to have a large impact and may sway the small number of undecided voters**. The focus will be Biden's performance in the debates, as the pandemic has limited his exposure to voters on the campaign trail.
- Finally, the unfortunate death of Supreme Court Justice Ruth Bader Ginsburg gives Trump an opportunity to galvanise his most loyal core base evangelical voters since conservative court appointments is the single most important issue for these voters. At the same time, Biden will remind voters of the about turn in the GOP politicians for not holding the same standards of allowing the next president to choose the next justice (no hearing for Obama's selection of Merrick Garland in 2016). He will campaign that a conservative-dominated court risks the over-turning of previous decisions including abortion, gay rights and Obamacare.

What are the most important issues facing the United States in this election? What are the key distinguishing points of the Trump vs the Biden campaign?

Americans believe the most important issues facing the United States are **the economy and jobs**, at 29%. Behind that, 15% cite **healthcare and Covid-19**, with morality picking up 9% and 8% choosing crime, according to an Ipsos poll taken over 3-8 September 2020. **Trump is facing tremendous pressure to shift the narrative in this election from a referendum on his first term** — which is typical for a president running for re-election — **to a binary choice between him and Biden**. The events of the past six months are driving this change, since Trump has a negative net approval rating on his handling of Covid-19 and race relations. His net approval rating remains -14.1%, based on a RealClearPolitics poll of polls. His current net unfavourable ratings have improved since 2016, when they stood at -21%, possibly putting him in a stronger position as a winning underdog. On his handling of race relations, he received a net negative approval rating of -17%, according to a Fox poll taken over 7-10 September 2020. Overall, **the public has a net negative approval rating for Trump of -9.6%,** according to our poll of polls. However, Trump enjoys a positive net approval rating of 4.0% on his handling of the economy, which could help him gain more popular support if the economy gains momentum in the next six weeks.

Historical approval ratings during presidential re-election campaigns

Year	President	Net approval	Re-elected?
June 1972	Richard M Nixon	23	Yes
June 1976	Gerald R Ford	5	No
September 1980	**Jimmy E Carter**	**-18**	**No**
October 1984	Ronald W Reagan	25	Yes
October 1992	**George HW Bush**	**-22**	**No**
October 1996	Bill J Clinton	18	Yes
October 2004	George W Bush	1	Yes
October 2012	Barack H Obama	5	Yes
September 2020	**Donald J Trump**	**-14**	**?**

Source: Amundi, American Presidency Project, RealClearPolitics for 2020 election. Data as of 21 September 2020

"There are three main themes in Trump's campaign: law and order, China and Biden's fitness for the office. Biden is campaigning on economic policy, healthcare, racial justice and morality".

There are three main themes in Trump's campaign: **law and order**, **China and Biden's fitness for the office.** In order to respond to negative poll numbers on the social/racial protests, Trump has accused Biden of supporting the defunding of police departments, a move that does not have popular support among Americans.

Biden has denied any move to defund the police. **On China**, **Trump's campaign has focused on a tough-on-China message**, and his success negotiating the phase-one trade agreement. Such a deal should help boost exports and create jobs in the United States. Finally, a recurring theme for Trump has been questioning Biden's mental and physical fitness for the office, though there is no evidence that Biden is not capable of governing. Trump hopes this tactic will help change the narrative from a referendum on his presidency to a binary choice. **We would expect that the Trump administration's approach regarding deregulation and taxes will persist**.

"Biden is planning another fiscal stimulus package to address immediate economic issues tied to the pandemic. Also, he has plans for major infrastructure spending and supports a modified version of the Green New Deal".

On the other hand, Biden is campaigning on economic policy ("Build Back Better"), **healthcare, racial justice and morality**. Biden has been focusing on promoting his economic plan, which begins by attacking the economy's largest hurdle, namely the effects of the Covid-19 pandemic. Such a plan would see the implementation of broader testing, an increase in the availability of medical supplies, and would ensure the safe opening of schools, even though the latter could be shut down depending on scientific advice. **Biden is planning another fiscal stimulus package to address immediate economic issues tied to the pandemic. Also, he has plans for major infrastructure spending and supports a modified version of the Green New Deal. Biden's healthcare plan is to boost Obamacare and prescription drug reform**. Finally, Biden frequently talks about "restoring decency" to the office. **Biden is hoping to woo voters that have cited morality as an important issue facing the United States. Funding for proposed initiatives is likely to come from higher corporate and individual taxes.**

Milestones on the way to the November election

Source: Amundi as of 23 September 2020.

The first presidential debate has the potential to change the trajectory of the race or to reinforce the current polls. If Trump is still lagging in the polls, it may be his last opportunity to change the momentum in the race. For Biden, his goal will be to instill confidence that his message is more in tune with the American mood than that of Trump.

What are the main economic and social challenges that the two candidates will have to face once the Covid-19 crisis is over?

"On a longer-term basis, it is the rise of inequality that has become the central issue over time and its potential consequences are of concern to authorities, including the Federal Reserve".

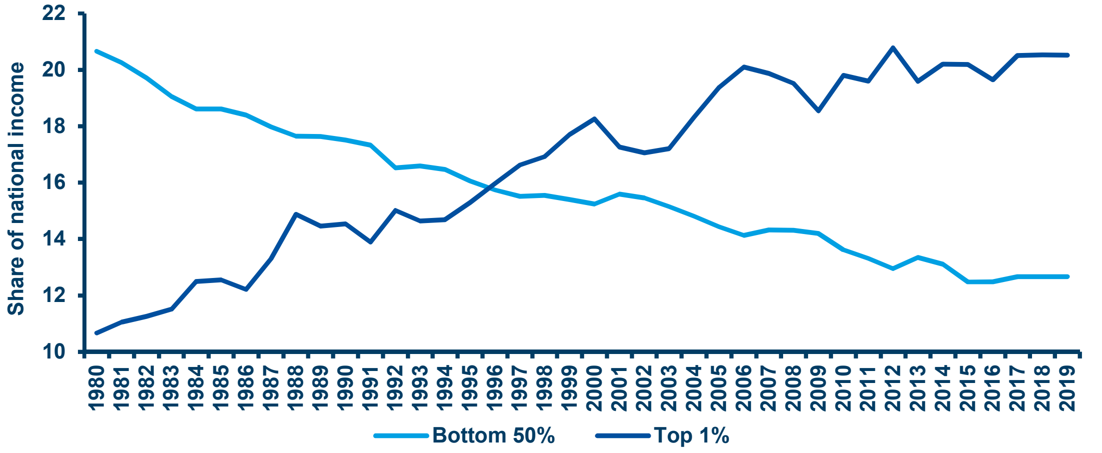
Managing the pandemic and its fallout will remain the top economic priority for the next administration in the short term. On a longer-term basis, it is the rise in inequality that has become the central issue over time and its potential consequences are of concern to authorities, including the Federal Reserve. Regarding this issue, the Covid-19 crisis has aggravated the situation, as it is the most fragile groups who have been most hard hit by the crisis-induced unemployment. In addition, these people are also the ones who do not have the means to take care of themselves when they fall ill, as they often do not have health insurance coverage. In this respect, the developments of the past 50 years are alarming:

- During this period, the share of income available to the top 20% of US households has grown steadily. Since 2018, their income has accounted for over 50% of all distributed income. The share of income of the richest 5% rose from 16% in 1968 to 23% in 2018.
- Income inequality in the United States is the highest of all G7 countries, according to OECD data. In addition, the income gap between black and white people has tended to widen, exacerbating racial tensions.
- The wealth gap between the richest and the poorest more than doubled between 1989 and 2016. The richest are also the only group whose wealth increased after the Great Financial Crisis. This is likely to be the case after the Covid-19 crisis as well.
- Middle-class income has grown less rapidly than that of upper-class income over the past 50 years.

Over 60% of US citizens believe that inequalities are too high. Unsurprisingly, opinions differ across political parties and household income levels, ultimately increasing the polarisation within US society. **Consequently, the main challenge in the United States is not to restore**

full employment, but to make growth more inclusive. This has become a prerequisite for political and social stability in the country in the coming decades. More and more Republican members of Congress understand the need to address the problem of inequality.

Share of national income earned by the top 1% vs bottom 50%, United States



Source: World Inequality Database, Amundi. Data as of 21 September 2020.

INVESTMENT IMPLICATIONS

Do you see any impact on the US dollar from the election?

The dollar has been experiencing a cyclical weakening. Over the last two years, the dollar bull market had been supported by large interest rate differential and above-trend growth relative to the rest of the world. Since the pandemic-induced recession, we have seen the removal of the twin pillars that used to support the dollar — interest rate differentials and US growth exceptionalism — replaced by the re-emergence of the twin deficits, especially the fiscal deficit. In addition, the Fed's long-term commitment to near-zero rates and an escalating debt/GDP ratio will put pressure on the currency, both now and in the medium term. **If the prospects of a Trump re-election increase, we could see the dollar temporarily appreciate on concerns about the prospects of heightened trade tensions and broader geopolitical uncertainty.**

The Fed has recently announced a change in its policy framework. What are the main risks and opportunities of such change? Do you see the possibility of a reassessment of inflation expectations, which would potentiall affect real rates and risk asset valuations?

"There is a broad consensus that it is the equilibrium rate that has fallen, together with an increase in the equilibrium valuation of risky assets. All other things being equal, this factor should encourage savers to switch to equities from bonds".

As a result of its strategic review, the Fed amended its 'reaction function'. Now, it will seek to stabilise inflation around 2% on average over an entire economic cycle, most likely over a four- to eight-year period. In practice, this will allow the Fed to avoid rate hikes at the first signs of an acceleration in inflation. This will require that the recovery is firmly anchored and that inflation remains above 2%. These two conditions will not be met before 2024, according to most FOMC members (only four out of 17 members anticipate a first rate hike in 2023, despite having recently upgraded both growth and inflation forecasts). In doing so, the Fed will anchor the short end of the yield curve. Such an approach supports expectations of an economic recovery. In a very uncertain environment, it is essential to reassure investors that monetary conditions will remain very accommodative during the recovery phase. Also, this strategy will allow to contain interest charges to be contained and the postponement of the debate on rising federal debt.

However, **the recent fall in real interest rates is not only related to monetary policy developments. There is a broad consensus that it is the equilibrium rate that has fallen. As a result, the equilibrium valuation of risky assets has increased**. All other things being equal, **this factor should encourage savers to switch to equities from bonds.** That said, rising costs related to value-chain disruptions, deglobalisation (re-onshoring), and the aspirations of a growing share of the population for wage rises are likely to push up inflation expectations at some point. Moreover, real interest rates have fallen into negative territory and are now below their equilibrium rate. In the short term, if inflation expectations rise, real rates may fall even more sharply, temporarily supporting growth stocks. However, it should be remembered that the Fed is not committed to maintaining long-term yields at their current level. In particular, **if growth and inflation pick up more sharply than expected, the Fed may want to let market forces play their role, leading to a rise in long-term Treasury yields and to a steepening of the yield curve**. This is a potential source of volatility and correction in the stock market that will need to be monitored closely.

What about other possible market implications of the 2020 presidential race?

While history has shown that party leadership in the Oval Office has had little long-term impact on market returns, **we expect to see near-term volatility around election time**. Excluding the economic boom of the 1990s under the Clinton administration, and the subsequent Dot.com bubble burst under George W Bush, market returns have been similar across party leadership. **The greatest risk to short-term market dynamics is an undecided race**. There is already expectation that results in Georgia will not be certified until well into December, as half of the state's voters do so by mail, and a recent ruling allows for a delay in the absentee deadline. Eighteen other states accept absentee ballots after Election Day**. Given the recent decline in equity market volatility, there is a risk of a sharp sell-off from current levels, especially if the election outcome is still unknown days after 3 November.** Depending on the winner, certain market sectors may respond differently. **Big tech, defense, financials and carbon energy sectors are likely to perform better under Trump** while renewable energy and infrastructure-related sectors will be winners under Biden.

"The greatest risk to short-term market dynamics is an undecided race".

US 2020 presidential elections: market implications

Scenarios	Trump victory (Democrats House, Republicans Senate)	Democrats sweep	Biden victory (Democrats House, Republicans Senate)
Summary	Positive equities, stable rates, strong dollar.	Negative equities, higher rates, weak dollar.	Positive equities, stable rates, weak dollar.
Equities	Equities rise from prospects of further tax reform, may include capital gains; Infrastructure, defense, energy, financials and telecom sectors win.	Potential for initial sharp sell-off as markets price in higher taxes and regulation; Possibly buy on an overreaction; Construction, transportation and resource sectors could outperform.	The prospect of a divided government will push equities higher; Infrastructure, construction, defense may outperform, while tech and energy may underperform.
Rates	Large supply and Fed QE will help keep rates stable. However, potential for tighter fiscal policy later could push rates higher.	Large supply and fiscal impulse could offset Fed's QE, leading to higher rates.	Large supply and Fed QE will help keep rates stable. However, potential for tighter fiscal policy later could push rates higher.
Dollar	Uncertainty over trade policy, large portfolio inflows into equities and home bias by US investors could lead to stronger dollar.	Fiscal impulse will boost growth prospects in US/globally; without tighter monetary policy, dollar will depreciate further.	Low interest rate support, dollar overvalued and relative growth underperformance vs G10, leading to weaker dollar.

Source: Amundi as of 23 September 2020.

What might be the impact of the two candidates with regard to ESG themes? And which investment opportunities could arise in this respect?

Under President Trump, there has been a backtracking of ESG-friendly policies, with a rollback of regulations and loosening of environmental oversight. The Trump administration has discouraged the implementation of ESG criteria in the nation's retirement plans. According to a *New York Times* analysis of the Trump administration's environmental deregulation, **Trump eliminated 68 rules that were been completed, and another 32 rules are on track to be rolled back.** Trump's completed rollbacks include a loosening of air pollution and emissions standards, allowing more drilling and extraction, and rollbacks of other regulations related to

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infrastructure, animals, water pollution, toxic substances and safety. Some examples the administration's environmental deregulation include:

- Weakening the Endangered Species Act;
- Restricting California's ability to enforce stricter auto emissions;
- Loosening and cancelling requirement of energy companies to report methane emissions; and
- Weakening the National Environmental Policy Act for quicker approval of infrastructure projects.

A Biden win would alter the course for ESG in the United States. We would expect to see the following actions implemented:

- United States would re-join the 2015 Paris climate accord;
- Reversal all of Trump's anti-ESG policies via executive order; and
- Passage of parts of the Green New Deal. This could occur quickly if both houses of Congress are controlled by Democrats, but would take longer if Republicans maintain control of the Senate.

We believe that ESG investing will gain increasing traction globally going forward, with rising investor pressure for increased disclosure and enhanced ESG practices, supported by accelerating ESG equity flows, including in the United States and despite Trump's backtracking. Should Trump be re-elected, the theme will remain under way, albeit not at the same level should there be a Democratic sweep.

INTERNATIONAL RELATIONS POST THE US ELECTION

US-China relations

On 15 August, the two countries agreed to postpone a review of their phase-one trade deal. The US election campaign and the hard rhetoric from President Trump could exacerbate tensions, with negative spillover effects. The equally hawkish tone from members of the Democratic Party brings new policy uncertainties to the bilateral relationship in a Biden-win scenario. In addition to the ongoing tech war, a capital war on foreign holdings, and re-shoring of the global supply chain, the current situation in Hong Kong introduces risks of possible US sanctions on Chinese banks and an exclusion from the dollar system. Hence, **the phase-one trade deal appears on hold for now, with little hope of a phase-two deal**. Accidental confrontations in the South China Sea or in the Taiwan Strait might push the situation to a point of no return. Under an extreme scenario, this 'cold war' might involve Europe as well.

Towards a change in transatlantic relations?

Relations between the United States and Europe will be dominated by the personality of the next president. Transatlantic relations have deteriorated significantly since the election of Donald Trump. The common values on which the two continents have built their relationship since WWII — eg, democracy, respect for human rights, free trade — are no longer promoted by the Trump administration. The current president makes no secret of his contempt for all international organisations and, generally, for all forms of multilateral negotiations. Bilateral negotiations are favoured instead. Donald Trump welcomed the United Kingdom's departure from the EU and openly criticised NATO. He has been able to impose his vision within his administration on many issues, particularly on trade topics. Conversely, a victory for Joe Biden would help normalise transatlantic relations, especially on the diplomatic front. Biden would set himself apart from his predecessor, notably by abandoning Trump's mercantilist approach and putting multilateral organisations back in the saddle:

"The phase-one trade deal appears on hold for now, with little hope for a phase-two deal".

- **Trade relations:** this is the first area of concern for Europeans should Trump be re-elected. Europeans are worried about his repeated threats of tariffs on cars. Criticism of the EU has remained at the level of verbal threats for now while political realism has

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prevailed. Many lobbies have opposed the establishment of tariff barriers with the EU, but the importance of lobbying would take a back seat in the event of a second term for Trump. Let us recall some figures to understand what is at stake:

- **The United States and the EU are each other's largest trade and investment partners**. Total trade in goods and services between them reached $1.3tn in 2019. In 2018, US direct investment into the EU amounted to $3,300bn vs $2,600bn of EU direct investment in the United States. The EU accounts for over 50% of total FDI in the United States and US direct investment abroad, and FDI covers a range of sectors, including manufacturing, finance and insurance.
- In 2019, the **US deficit with the EU-28 was $123bn**, with a deficit in trade of goods ($179bn) exceeding the surplus in the balance of services ($56bn). It is the imbalance on cars — especially with Germany — that has attracted the most attention from the Trump administration, which blames Europeans for imposing 10% tariffs on their car imports, whereas the US imposes only 2.5% tariffs on auto imports from Europe. The Europeans have argued that the relationship is fair and mutually beneficial given the surplus in the US balance of services and the higher profits made by US companies based in Europe. In 2017, subsidiaries of US multinationals in the EU-28 had a sales turnover of $2.5tn, $400bn more than the sales turnover of EU multinationals in the US.
- Under section 232 of the Trade Expansion Act, **the president can adjust imports** — including through the use of tariffs — if excessive foreign imports are found to be a threat to US national security. In May 2019, the section 232 investigation found that this was the case.
- Should Trump impose tariffs, **Europeans are likely to retaliate**. The fact is that value chains are intertwined and the presence of US multinational subsidiaries in Europe and vice versa would make the transatlantic relationship even more complex, with unpredictable consequences on value chains and FDI.

- **The Brexit dossier is emblematic of the different approach between Trump and Biden:** President Trump supported the United Kingdom's decision to leave the EU and expressed doubts about the future viability of the EU. He supported a free-trade agreement with the UK after its withdrawal from the EU. On the other hand, Joe Biden's team warned Boris Johnson that the Northern Ireland protocol with the EU should not be challenged, otherwise the UK-US trade treaty would be compromised. On 16 September, Joe Biden tweeted: *“We can’t allow the Good Friday Agreement that brought peace to Northern Ireland to become a casualty of Brexit. Any trade deal between the US and UK must be contingent upon respect for the Agreement and preventing the return of a hard border. Period”.*
- **Trump’s foreign policy can be summed up in two words: "America First"**. Unsurprisingly, some of its decisions counter the EU's positions, including the US decision to withdraw from the multilateral nuclear agreement with Iran and the Paris agreement on climate change. The Covid-19 crisis will exacerbate existing tensions.
- On **security and defence**, President Trump does not seem to consider the EU to be a reliable partner. He believes that the Europeans are not meeting their financial obligations (namely, the targeted 2% of GDP set by NATO) and has threatened to withdraw militarily from Europe if the Europeans do not fulfil their obligations. These attempts to withdraw from NATO or Europe would probably be thwarted by his administration, which has adopted a more balanced position. However, in case of an international crisis (eg, between Turkey and Greece), President Trump's ambiguous stance could be a concern.

Transatlantic relations will be completely different depending on who becomes the next president. **It is less US fiscal policy — which would be expansionary in any case — then international relations that are at stake for the next four years.** For both Europe and China, the results of the US presidential election will be as important as for the United States.

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Definitions

- **Curve steepening:** A steepening yield curve may be a result of long-term interest rates rising more than short-term interest rates or short-term rates dropping more than long-term rates.
- **FDI:** Foreign direct investments.
- **FX:** FX markets refer to the foreign exchange markets where participants are able to buy and sell currencies.
- **GOP:** Grand Old Party, the US Republican political Party.
- **Spread:** The difference between two prices or interest rates.
- **Volatility:** A statistical measure of the dispersion of returns for a given security or market index. Usually, the higher the volatility, the riskier the security/market.

Important Information

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