



Global Macro Research

7 November 2024

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US Election: It's Trump. What's next?

Markets are focusing on the reflationary aspects of Trump's agenda. This has meant a stronger dollar, higher yields, US equities up, and oil lower. But these moves may evolve as different aspects of Trump's economic agenda shift in and out of focus. Higher nominal GDP growth and higher-than-otherwise interest rates are the macro implications we are most confident about for now.

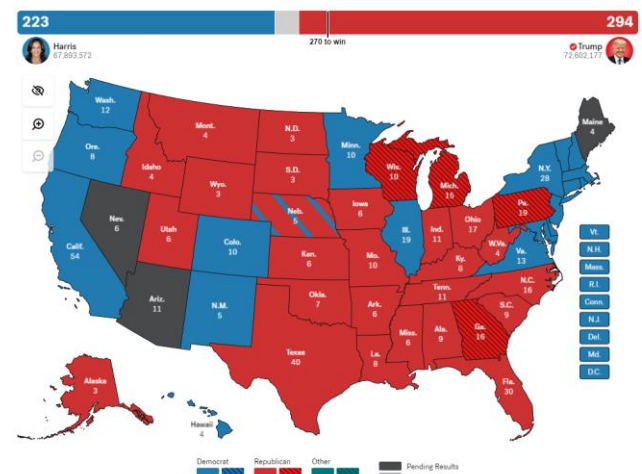
Key Takeaways

- Donald Trump will be the next president of the United States, with his broad-based gains in the popular vote translating to a strong Electoral College victory.
- Republicans have flipped the Senate, with the eventual majority likely to be between two and five seats.
- The Republicans look extremely likely to also win the House, granting the party unified control of government.
- In this red wave outcome, the scenarios we have previously called "Trump delivers for markets" and "Full fat Trump" will come to the fore, as congressional control would give Trump latitude to pursue tax cuts and deregulation.
- But if Trump finds it more difficult to push a large increase in the deficit through Congress, then the focus could be more on tariff policy, with a "Trump trade war 2.0" scenario more likely. Trump has significant executive authority to set tariffs without the need for congressional approval.
- On balance, Trump's agenda is likely to lead to higher nominal GDP growth. Tax cuts could boost aggregate demand, but as the economy is at full employment, this may not boost real growth over the medium term.
- This will likely see the Fed cut rates more slowly than it otherwise would have done, which, combined with higher debt issuance and inflation, risks putting further upward pressure on US and global yields.

Trump wins the presidency

Donald Trump will return to the White House as president of the United States, having won the Electoral College, including all seven swing states, and appearing on track to win the popular vote (see Figure 1).

Figure 1: A strong performance for Trump in the popular vote and Electoral College



Source: ABC news, 0900 GMT 7 November 2024

The polling miss, which unlike in 2016 and 2020, was within the margin of error, was nonetheless big enough for a decisive Electoral College victory.

In financial markets, the dollar is stronger, treasury yields are higher, US equity prices are up, and oil is lower.

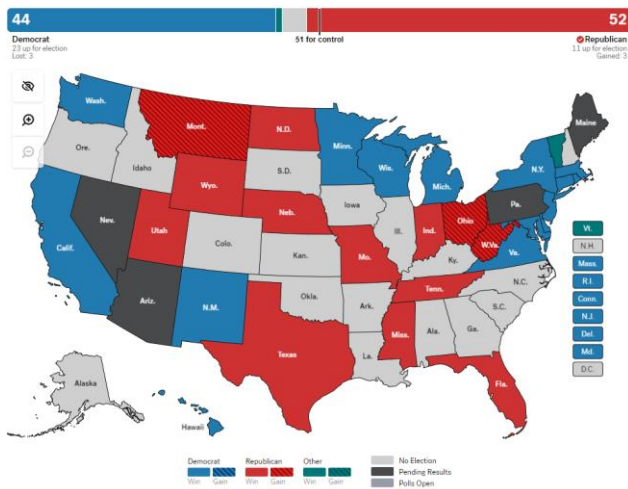


This implies the market is focusing on the reflationary aspects of Trump's policies, with the prospect of tax cuts boosting risk sentiment but weighing on bonds.

Republicans flip the Senate, but margin unclear

As anticipated, Republicans have performed well in Senate races and will take control of the chamber. The majority remains uncertain, with counting still underway in several Democratic-held seats that are vulnerable to Republican gains. The eventual Republican Senate majority will be somewhere within 52 and 56 (see Figure 2).

Figure 2: As expected, Republicans have flipped the Senate



Source: ABC news, 0900 GMT 7 November 2024

Holding the Senate is of strategic importance to the president. It makes easy confirmation of Trump's cabinet nominees more likely and gives Republicans the ability to nominate Supreme Court justices.

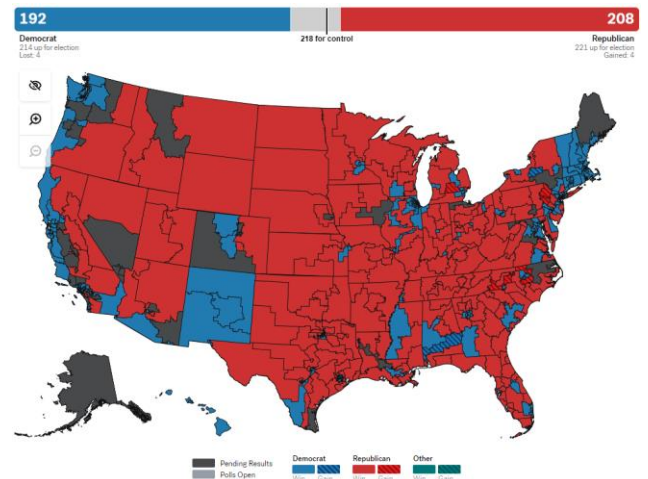
A bigger majority in the Senate would give Trump more leeway to pass legislation, negating the need for compromises on policy. It also has implications for the longevity of the Republican majority, which could last multiple electoral cycles.

We still don't know the outcome in the House, but it's very likely to see Republican control

At the time of writing, there isn't yet a majority in the House. However, Republicans are overwhelmingly likely to secure a majority as the final few districts are called (see Figure 3).

Control of the House is important for the eventual macro and market impacts of Trump's presidency. Unified control of government will give Trump latitude to pursue legislative changes, including significant tax cuts.

Figure 3: The House is very likely to be controlled by the Republicans



Source: ABC news, 0900 GMT 7 November 2024

Unified government gives Trump latitude to pursue tax cuts

A unified Republican government will almost certainly extend the expiring and expired provisions from the Tax Cuts and Jobs Act, as well as pursue further tax cuts.

However, the scale and composition of these measures is uncertain. Trump has pledged a wide range of initiatives including cutting corporation tax from 21% to 20%, with a further reduction to 15% for companies manufacturing in the US; removing tax on tips, overtime and social security benefits; and removing the \$10k cap on state and local tax deductions from federal income tax.

These and other proposals are costed at close to \$10tn and are therefore very unlikely to come even close to being fully realised due to the implications for the deficit. However, we should expect a clear loosening in fiscal policy via tax cuts, with the scale of this impetus potentially sensitive to the size of Republican majorities in the House and Senate.

Unified government would also likely see increases in defence spending, while cutting funding for other discretionary spending and regulatory agencies as part of a wider emphasis on reducing the regulatory burden on businesses. We await to see what formal role, if any, Elon Musk has in the administration, as this could be a waymark for how much funding cuts regulatory agencies may experience. Regardless, these cuts are very unlikely to offset the increase in the deficit triggered by tax cuts and spending increases.

Finally, unified government would create uncertainty around the future of the Inflation Reduction Act.

Large swathes of funding for green investment flow to red states, which should make full repeal of the legislation, or a rescinding of unspent funding, unlikely. However, there could be changes to the bill, particularly eligibility requirements for accessing grant funding.



And budget cuts to the Environmental Protection Agency may limit its ability to distribute remaining funds.

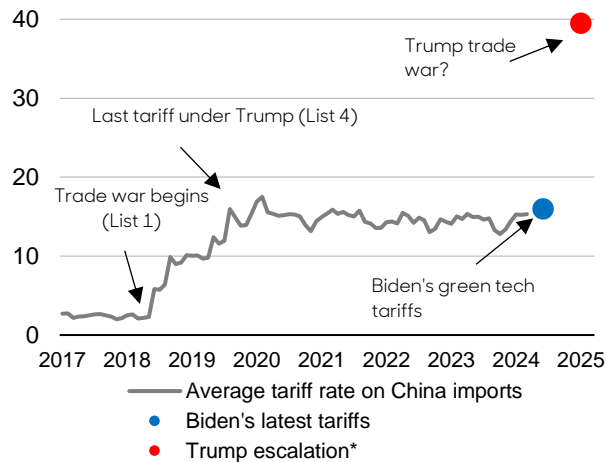
This, combined with the likely increase in oil and gas permitting, would create the perception of a material policy shift for businesses without the need for additional legislation or major amendments to the IRA. But, while uncertainty over its future persists, companies might be deterred from investing based on these tax credits.

Tariff increases likely, but their volume and permanence are uncertain

Trump has been clear on the campaign trail that he continues to consider tariffs an effective means of rectifying perceived trade imbalances and unfair trading practices. He has also said some of his pledged tax cuts would be paid for using tariff revenue. His pledged tariff increases of 60% on all trade with China, and a universal 10-20% tariff on all other US imports, would imply a significantly larger increase in effective tariff rates than implemented during his first term.

However, there remains uncertainty over how tariffs play into Trump's wider trade strategy. His first term saw tariffs threatened and applied as a means of seeking concessions from trade partners. If he pursues this approach in his second term, tariff threats would likely be used more frequently than their actual application. A key waymark will be who is chosen for Commerce Secretary and their views on whether tariffs are better used as a negotiating tool or a means to alter trade flows.

Figure 4: The US-China bilateral tariff rate could increase significantly



*Scenario assumes 60% tariffs applied to Lists 1-4

Source: abrDN, U.S. Census Bureau, USTR, WITS, September 2024

For now, we think that a reasonable base case might involve a meaningful increase in US tariffs on Chinese imports but falling short of the threatened 60% tariffs on all trade with China. We previously modelled 60% tariffs on the List 1-4 goods, which would increase the bilateral tariff rate to around 40% (see Figure 4). The 10-20% global tariff might be used more as a negotiating tool to extract concessions, such as higher defence spending by European countries. In

practice this might mean tariff increases will be more product and country specific, and implemented and removed sporadically, similar to Trump's first term.

An upside scenario might involve very little follow through on tariff threats. Meanwhile, a downside, which would become more likely in the event of divided government, could see a much greater focus on tariff policy alongside little follow through on tax cuts.

The impact of immigration restrictions is likely to fall short of Trump's pledges

A unified Republican Congress is likely to pass H.R 2, a bill passed by the House prior to the election but rejected by the then Democratic-controlled Senate. This would require employers to verify whether employees have the legal right to work in the US, as well as restricting the asylum process and allocating funding to extending the border wall with Mexico. If passed, the bill is likely to result in reductions to the undocumented workforce, as well as reduce the flow of new arrivals into the US. On top of this, Trump is likely to slow the pace of legal immigration significantly.

However, these measures stop well short of a mass deportation plan, which we think is unlikely to be politically or logistically feasible. Nonetheless, the migrant workforce is likely to be smaller under Trump than it would otherwise be, which is a negative labour market shock.

What all this might mean for macro and markets

There remains considerable uncertainty about the eventual economic implications of a Trump presidency. But on balance we think it is likely to mean higher nominal GDP growth, with the bulk of the increase through higher inflation on the back of potentially looser fiscal policy, higher tariffs and lower immigration.

This means policy interest rates will likely fall less rapidly than they otherwise would have done, and the Fed will face several difficult decisions and trade-offs.

In the short term, it will need to judge how much the shift in market interest rate expectations represents an appropriate endogenous repricing of the likely economic environment, versus an unwarranted move that needs to be resisted.

We suspect its mostly the former, meaning the Fed doesn't have to become more dovish to offset higher bond yields.

In the likely event that tariff levels are increased, the Fed will need to decide whether to look through the inflationary impact of higher taxes as it represents a one-off price-level shock, or whether inflation expectations are too weakly anchored to withstand such a large shock. The recent inflation overshoot probably means they will err on the more hawkish side.

Over the medium term, the Fed is likely to find itself under rhetorical pressure from Trump if rates and the dollar do not evolve as the administration would like.



On balance, we are sceptical that Trump can engineer a sustained weakening in the dollar either via the Fed or a broader agreement with trading partners. But we expect Trump to change some personnel at the Fed, including Powell when he gets the chance in 2026. There is a risk that heavy handed interference in the Fed prompts disquiet in markets around the central bank's independence.

For now, we continue to expect the fed funds rate to end the year at 4.375%, followed by quarterly cuts next year. But the risks are skewed toward slower and less easing.

Longer maturity yields may need to reflect both a somewhat slower pace of easing, as well as a significant increase in issuance, which pushes up on the term premium.

Given the importance of treasury yields in setting global interest rates, this is likely to put upward pressure on the global rates complex. For central banks elsewhere, this would represent an exogenous tightening in financial conditions. The likes of the European Central Bank may lean against this by becoming more dovish, although many EM central banks may have to turn more hawkish amid downward pressure on their currencies.

This could also put significant fiscal pressure on various other countries, especially as a Trump presidency may entail the need for higher defence spending.

Over the long term, it is possible that deregulation and a sustained environment of positive risk sentiment helps to boost capital formation and potential growth, which would

limit some of the inflationary effects. But it's more likely that the combination of a larger deficit and higher rates in an already full-employment economy leads to some crowding out of the private sector, which alongside Trump's immigration reforms, would weigh on potential growth.

Trump's policy agenda will be revealed over time, which means market pricing could continue to shift

As different aspects of Trump's agenda shift in and out of focus, the initial market reaction may evolve.

In what we've previously called a "Trump delivers for markets" scenario, risk-on sentiment could be sustained by Trump's tax and regulation policy, while his protectionist agenda becomes less prominent, limiting its inflationary fallout.

But in a "full fat Trump" scenario, where Trump pursues the full suite of policies discussed on the campaign trail, then risk sentiment may fade over time as the complicated policy mix leads to greater uncertainty about the path of interest rates and the robustness of institutions. Yields and the dollar would likely rise more in this scenario in the near term given the highly inflationary composition of this agenda. However, if Trump seriously attempts to reform the Fed to deliver a weaker dollar, the longer-term moves are less certain.

All told, higher nominal GDP growth, mostly via higher inflation, and a higher-than-otherwise path for policy rates, are the economic outcomes we feel most confident about at this stage.

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AA-071124-185548-16

