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UOB Investment Insights

Thinking Ahead

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Key takeaways

- US policies may be less predictable over the next four years after Donald Trump and the Republican party won the election.
- Market volatility will likely subside post-election, and investors will turn their focus back onto economic fundamentals and interest rates.
- The outlook for stock markets remains positive given resilient economic growth, robust corporate earnings, and expectations of gradual rate cuts. It is however important to be nimble and proactive, and to build a diversified portfolio given the prospect of unpredictable policy shifts.

What does Trump and Republican victory mean for markets?

- Donald Trump will be US President for a second time while the Republican party wrestled back control of the Senate. Control of the House of Representatives is yet to be confirmed but the prospect of full Republican control is possible.
- The immediate reaction was a rally in US stocks, the US dollar, US Treasury yields and cryptocurrencies. Chinese stock markets were weighed down by concerns of impending tariffs.
- The key ahead lies in whether President-elect Donald Trump implements all his proposed policies, as that will determine global trade, inflation, interest rates and economic growth.
- Trump2.0 policies may mirror his first presidential term. Tax cuts and deregulation will boost US economic growth and corporate profits, supporting the stock market. The targets of trade protectionism and tariffs will be negatively affected, while inflation may rise.
- Another similarity will be the unpredictability of policy shifts, and this may result in intermittent bouts of market volatility.
- The key difference is that Trump1.0 policies came during the middle of the economic cycle when pro-growth policies tend to have had a bigger corporate impact. With the economy now in the late stages of the cycle while inflation concerns have not been eliminated, the economic impact may differ slightly.

US economy and stocks to benefit from "America First" approach and Trump priorities

- Assuming Donald Trump follows through on his proposed policies, the US economy is likely to stay resilient and outperform global peers. This is due to the prospect of lower corporate taxes, extension of individual tax cuts, and deregulation of certain industries.
- This will be positive for US stocks although certain sectors will be impacted differently.
  - The financials sector will benefit from deregulation and economic resilience. Industrials and manufacturing will likely benefit from companies shifting production back onshore to the US. The energy sector will benefit as more drilling of oil rigs is likely.

    - The renewable energy sector may struggle however if there is a partial repeal of the Inflation Reduction Act (IRA).

Higher inflation may impact the US Federal Reserve's (Fed) interest rate path

- Trump has threatened to impose universal 10% tariffs on global trade partners and 60% on Chinese goods. If he does so, it will lead to higher inflation.
- Tougher immigration policy is another of his key priority, and lower labour supply will weigh on labour intensive companies while higher wage growth will further increase inflationary pressures.
- In this scenario, the Fed may not be able to cut interest rates aggressively.

Bonds affected by outlook for fiscal deficit and interest rates

- Bonds may see more short-term selling as the combination of tax cuts and higher government spending runs the risk of a ballooning US fiscal deficit. This may lead to the US Treasury issuing more bonds. In addition, the risk of higher inflation could lead to less Fed rate cuts.
- Nonetheless, interest rates are still expected to be cut ahead which will limit the downside for bonds. Investment grade bonds with higher yields will still be attractive sources of income.

China may react with more forceful stimulus

- China's growth will be greatly affected if Trump imposes 60% tariffs on Chinese goods. To offset this and the structural slowdown of the Chinese economy, the government may have to react by announcing a larger stimulus package to support the economy.
- Chinese companies that are domestically oriented will likely do relatively better.

What you can do

- Market volatility will likely subside post-election, and investors will turn their focus back onto economic fundamentals and interest rates.
- The outlook for stock markets remains positive given resilient economic growth, robust corporate earnings, and expectations of gradual rate cuts.
- It is however important to be nimble and proactive, and to build a diversified portfolio given the prospect of unpredictable policy shifts.
- If you are able and willing to take risk, consider assets that may benefit from the rate-cutting cycle
    - Investment grade bonds offer consistent income and potential capital gains when central banks cut interest rates and can serve as portfolio stabilisers amid political uncertainties.
    - Asia ex-Japan and ASEAN stocks offer attractive valuation and dividend yield. While US-China trade tension may rise under Trump's presidency, this could potentially lead to further supply chain relocation into ASEAN.
    - Global small cap stocks will benefit from lower borrowing costs and resilient economic growth.
- Speak to a UOB Advisor to learn more.

Right By You

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