FLASH UPDATE

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NORTH CAPITAL

The US Turns Red

What is the result?

The US just experienced an election campaign and result that will likely live long in the history books. We discussed the potential impact of this in our US Election Spotlight from July, and now after months of debate we have a new US President. Polls immediately before the election yesterday were extremely close but while some votes are yet to be counted, Donald Trump has been declared the winner, marking his return as president of the United States. In addition, the Republicans have officially won the Senate, and they appear highly likely to continue their control of the House of Representatives, although there is not a confirmed majority yet, and so it seems likely, that the Republicans have achieved a "clean sweep". For bills to become law, they need to be passed through both the House and the Senate; control of both should mean a very powerful mandate.

So far today, we have seen a strong reaction in markets. Yields on US government debt have increased driven by the expectation that Trump's policies will lead to higher inflation; the dollar has strengthened, and stock markets have risen. Smaller, more domestically focused companies have led this morning's rally.

What should investors now consider?

When Donald Trump won the US election in 2016, the result generated uncertainty as polls had indicated a Democrat win but this time around is quite different – recent polls have been much tighter and, as it is his second time around, there may be less fear of the unknown. This clarity has provided a supportive backdrop for stock markets today. Key policy areas for investors are likely to centre around: taxes, trade, and immigration. Trump has stated the intention to reduce taxes, including lower corporation tax as well exempting overtime and tips from income tax, which was in contrast with Harris' tax policies. US stock markets are likely to welcome this stance as it supports consumer's take-home pay as well as the direct impact on businesses of lower corporation tax. Higher tariffs, on the other hand, are likely to push up inflation by increasing the price of imported goods. This inflationary effect, combined with the recent strength of the US economy, is likely to lead to increased interest rates in the longer term, weighing on bonds but supporting the USD. This mirrors the narrative that has played out in markets so far today. Furthermore, Trump's immigration policy will likely mean a reduced supply of workers, potentially pushing up wages and inflation.

The outlook for equities is uncertain but we do believe US stocks can continue to outperform other regions against the backdrop of Trump's business friendly rhetoric. Furthermore, as long-term investors we would point out that the US stock market is home to a large share of the world's most innovative companies. This could be especially true when considering that European and emerging markets exporters could be adversely impacted by higher tariffs. It is also possible that these tariffs trigger a general deterioration in global trade, slowing global growth and hurting businesses in the US as well as elsewhere. This risk should be monitored closely, and alongside the potential for more inflationary pressure, supports an allocation to gold within multi-asset portfolios. Turning to sectors, Trump favours a more relaxed regulatory environment which should benefit smaller companies and financials, again this appears to be playing out so far. Higher bond yields may, however, offset some of this benefit to smaller companies. Meanwhile, plans to raise tariffs will make imported goods more expensive and may prove very challenging for the consumer discretionary sector. While Harris is an advocate for clean energy and addressing climate change, Trump is a known climate sceptic and has expressed the intention to drill more oil. It seems likely that traditional energy stocks can outperform in this environment.

Bottom line

As described above, there are risks to businesses and asset prices resulting from tariffs as well as higher inflation and bond yields. However, the powerful mandate that has been achieved makes it likely that lower taxes will be enacted, benefitting both businesses and consumers, while government spending is expected to expand further. There are a lot of moving parts for investors to consider, highlighting the benefits of an actively managed multi-asset portfolio.