What You Need to Know - US Election

Outcome: Former President Trump won both the electoral college and the popular vote to win his second non-consecutive term, a feat that has only happened once before in 1893.

Congress: The Senate flipped to Republican control, but they will fall short of the critical 60-seat position that eliminates the ability for Democrats to block legislation. Republicans are likely to keep the House, on a path to have a similar narrow majority (+3 to +4 seats) as they do now. When Trump came into office in 2017, he had a more decisive 23-seat House majority.

Fiscal Spending/Tax cuts: The Supreme Court has been clear on Executive limitations. The likely narrow majority in the House and Senate could limit what Trump can get done.

Any large spending cuts will be difficult to get through the House and would be difficult to do on reconciliation (which only requires 50 votes in the Senate and can be done once a year with respect to tax policy only); everything else requires 60 votes. This means that the mooted $2 trillion cuts have little chance of passing.

However, an extension of the expiring Trump tax cuts is likely, but possibly only extended for a shorter period given the already high budget deficit of ~6.5%.

Changes at the Federal Reserve: The first Fed governor vacancy is not until January 2026, similarly, Fed Chair Powell's term expires in 2026. The President cannot fire a Fed governor without cause and Powell has said he would refuse to resign if Trump asked him to.

Executive Orders on Day 1 – What's possible?

Roll-back executive orders: including in the energy sector (e.g., LNG export ban and prohibitions of drilling on federal land).

New executive orders: including on the border, restricting migration and prioritizing criminal deportations, rather than a broad-based deportation program.

Replace single directors at some federal agencies: Potential replacements include the Consumer Financial Protection Bureau (CFPB) and the Federal Housing Finance Authority (FHFA). Additionally, a new director is needed for the Federal Trade Commission (FTC), as the current director's term has expired, and for the acting director of the Office of the Comptroller of the Currency (OCC), a key banking regulator.

Impose new/higher tariffs on China: The administration may leverage the existing Section 301 investigation (the tool used by Trump in 2018 and later by Biden to raise tariffs). However, any additional tariffs would require a lengthy investigation process that could take several months before implementation.

Market Reaction: Markets had already started to position for a Trump victory. But markets also like certainty, and this result has been definitive: taking out the tail risk of a protracted election resolution has added to the recent rally in risk assets.

Given the clear result, Gold and equity market volatility immediately dropped. While the reaction from the bond market has been quite violent, with short-dated yields up given perceived inflationary risks, long-dated yields are also up on fiscal worries.

Sectors such as energy, real estate, industrials, and financials could benefit from looser regulations and have rallied strongly post-result. We explore the implications and outlook for selected assets and sectors below.

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Asset / Sector	Implications / Outlook
Global Growth	An increase in tariffs would likely reduce global growth or at least keep it subdued for longer. To counter this, central banks outside the US could ease policy further and at a faster pace than currently expected.
US Economy	The US is surprisingly quite a closed economy, with growth not reliant on exports as one might expect. The US represents less than 10% of the global export market.
Inflation	Trump's policies might be inflationary, with factors like limiting immigration, imposing higher tariffs, and potentially nominating a more dovish Fed Chair after Powell's term ends.
Bonds	The market has arguably priced in much of the inflationary impact of a Trump victory. However, the bond market could have another role to play here, with sharply higher yields due to a deteriorating fiscal position limiting the ability of Trump to spend.
USD	The likelihood of higher rates due to inflation, as well as strong economic growth are likely to continue to support the USD in our view.
Gold	Despite temporary weakness, momentum is likely to return here in our view.
EM	A potentially challenging period. Tariffs and moderating global growth likely to be negatives. However, the risk of large foreign outflows is now more limited (capital has already left) and China may announce further stimulus.
ASX Equities	There are individual companies with higher US economic or USD exposure, but overall ASX returns tend to be a product of the economic cycle.
US Financials	Potential lighter-touch capital regulation, investment banks (due to increased M&A activity), and life companies (from a steeper yield curve).
US Utilities	Utilities might struggle with higher bond yields and could be adversely affected by any rollback on green initiatives
Crypto	It's unclear, but this sector may see further deregulation or indeed support from a Trump administration. Bitcoin has rallied strongly on a trump win.
US Energy	US energy companies could outperform their global peers under Trump due to factors like extended asset life, reduced pressure to diversify into new energy areas, and potentially toned-down ESG mandates. His stance on fossil fuels may drive more drilling activity
Renewables	The clear loser in the short-term. With the potential for the rolling back of Biden-era executive orders and focus on traditional energy sources.
Tech and Software	Software companies have minimal exposure to China, so the impact of tariffs is likely to be muted. However, controls on parts of tech are possible, especially given JD Vance’s support for antitrust policies.
Semis	The sector derives ~20% of revenues from China. Both parties aim to localize semiconductor production, potentially benefiting US-based chip manufacturers. Under Trump's policies, this process may accelerate.
Autos	Trump’s scepticism of climate change and the potential elimination of the EV mandate could extend the lifespan of internal combustion engines.
Defence	Even before the election result, European defence spending was projected to increase significantly given regional conflict and the need to be more self-sufficient. This is only likely to accelerate given Trump is likely to once again step away from international defence treaties, and funding of NATO and wants to bring the Ukraine conflict to a close.

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What You Need to Know - October

Month of October: Higher bond yields on the back of stronger economic data and markets positioning for a Trump election victory saw interest rate-sensitive asset classes underperform. After a strong September, a weak AUD helped protect investors from weak global equity markets. US equities took a breather on a mixed start to the US corporate earnings season, election concerns and continued sluggishness in Europe and China.

Policy Watch: Following the Fed's 50 basis point interest rate cut in September, the sticky core inflation reading highlighted the challenge facing US policymakers. After today's 25bp cut, a further rate cut is still possible in December, but a strong labour market and resilient inflation have seen market expectations of future rate cuts reduce and the terminal rate rise.

Inflation Watch: In the US, headline CPI rose by 0.2% and 2.4% year-over-year, marking the slowest annual increase since early 2021. However, core inflation remained elevated at 3.3%. In Australia, progress on inflation is also slow with the third quarter consumer price index report very close to expectations, and the annual rate of inflation dropped to 2.8% y/y. However, the distortions from government subsidies were very clear as the trimmed mean was 3.5% y/y.

Risk Budget: Equity market volatility spiked at the start of the end of October, but only peaking at 23.

Our Portfolio: We remained underweight equities overall in the run-up to the election, as like many we had expected a closer result with the potential for a drawn-out process. Regardless, our portfolios were well positioned with large exposure to a rising USD, unhedged exposure to Treasury yields which has been offset by a stronger USD, a position in US small caps and an overall bias to smaller and mid-cap equities.

Outlook: US inflation expectations have been rising again and are likely to rise faster post the election result. While the US Fed has been cutting rates (including this morning) they are likely to now have to refocus their attention on the risk of inflation reigniting through next year.

US equities have bounced strongly on a mix of a clear and decisive election result and on the hopes of corporate tax cuts to boost earnings in a slowing environment. However, given the state of Congress, it remains to be seen how many policies Trump version 2.0 will be able to implement. A slower global economy and higher costs from the implementation of tariffs could take the shine off the rally.

How to Position: We haven't made any changes to our portfolio settings following the election result. We expect further appreciation in the USD given the inflationary threat of a Trump Presidency and for the rotation into US small caps to gain some momentum. Despite initial weakness, we continue to believe that Gold to appreciate in this environment, while it is too early to add to government bond positions.

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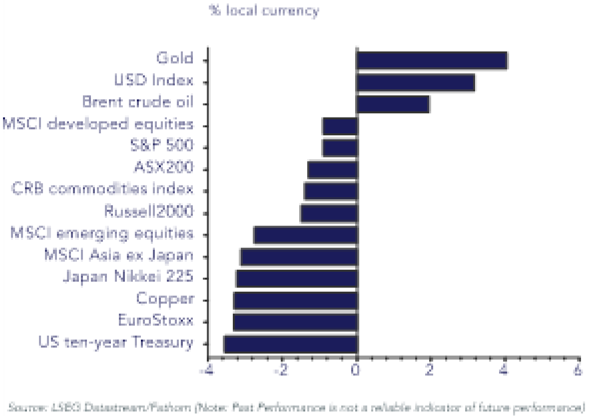
Markets in October

Bond yields rose dramatically on stronger-than-expected U.S. economic data. This also dialled back markets' view on both recession risk and rate cuts from the U.S. Federal Reserve (Fed). U.S. equities broke the winning streak and fell over the month for the first time since April, despite a decent, US3Q earnings season to date.

Chart 1: October Asset Class Performance



Bond yields moved higher globally despite the growing momentum of central bank cutting. The Australian 10-year government bond yield rose by 53 bps to 4.51%, while the US 10-year rose 50 bps to 4.28%.

Equities in most developed markets fell during October. The ASX 200 fell 1.3%, lagging peers again. The S&P500 was down 0.9%, while Europe fell 2.8%, and Japan rose 1.9% over the month. Weaker economic data in Europe weighed on equity returns there.

The MSCI World Developed Markets Index rose (+1.9%) in USD terms, underperforming relative to the Emerging Markets index, which rose by +7.1% in USD terms. Globally, the Communication Services (+1.4%), Financials (+0.6%), and Energy (+0.2%) sectors relatively outperformed in USD terms. The Materials (-5.8%), Health Care (-4.8%), and Consumer Staples (-4.6%) sectors relatively underperformed in October.

Eight of the ASX 200 sectors were in the red for the month. Utilities (-7.2%) was the worst performer, followed by consumer staples (-7.0%), materials (-5.2%) and energy (-5.0%). Offsetting this was the 3.3% rise in financials.

Chart 2: Selected Equity Markets YTD Relative Performance (0 = 1 Jan 2024)

Brent Oil rose by US$0.78 to US$72.55/bbl, whilst Iron Ore prices fell by US$8.00 to US$105.00/Mt. In precious metals, broad-based buying of gold combined with a lack of sellers, led to prices rising by US$147.85 over the month to US $2,777.80 per ounce.

Key Themes

US Economic Exceptionalism Continues

The first estimate of US third-quarter GDP growth came in at a healthy 2.8% quarter-on-quarter annualised, confirming that the economy continues to grow at an above-trend pace. Services activity reading remains strong, while the labour market data is volatile it remains in good shape.

Chart 3: Citi Economic Surprise

Outside of the U.S., concerns about the growth outlook are rising, most notably in Europe, where incoming data suggests a sharper slowdown in

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economic activity. While ECB president Lagarde reiterated that the region is not sliding into recession, there is a greater urgency for the ECB to accelerate upcoming interest rate cuts given how weak the data has been, especially out of economic powerhouse Germany.

Following the guidance provided in late September on stimulus measures, further announcements were made in October, focused on long-term structural repairs such as raising the debt ceiling to alleviate local governments' debt burden, expanding the property projects whitelist, and utilising special local government bonds to support housing de-stocking.

These announcements have fallen short of market expectations for a large fiscal stimulus injection. Although the latest economic data suggests a marginal improvement, upcoming data will be crucial in assessing if the economy has bottomed out. Regardless, the market is expecting more meaningful and larger stimulus from the Chinese government, and soon.

Australian Inflation is still too high

The third quarter consumer price index report was very close to expectations, and the annual rate of inflation dropped to 2.8% y/y. This put headline inflation back in the Reserve Bank of Australia (RBA) target band for the first time since 2021.

However, the distortions from government subsidies were very clear as the trimmed mean rate of inflation was 3.5% y/y. What is also clear from the data is that services inflation is rising again, rather than falling. With all the heavy lifting being done by the goods component of the CPI basket. For inflation to track back within the target band in a sustainable way services inflation needs to drop quickly, or goods inflation needs to go negative. Something that consumers would no doubt welcome.

Chart 4: Stubborn Australian Services Inflation

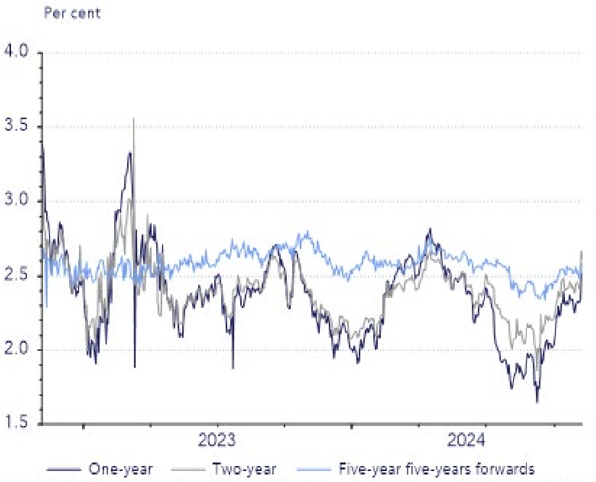
Source: LSEG Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

Overall, inflation is moving very much in line with RBA expectations. The RBA is going to need to see more meaningful progress on the trimmed mean measure in February's 4Q CPI print to move interest rates early next year.

Outlook

US inflation expectations have been rising again and are likely to rise faster post the election result. While the US Fed has been cutting rates (including this morning) they are likely to now have to refocus their attention on the risk of inflation reigniting through next year.

Chart 5: US inflation swaps



Source: LSEG Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

As outlined earlier in this document, Trump has the power to impose new and higher tariffs on imports from China via executive orders. These tariffs are likely to raise the prices of imported goods, which in turn could drive up overall consumer prices.

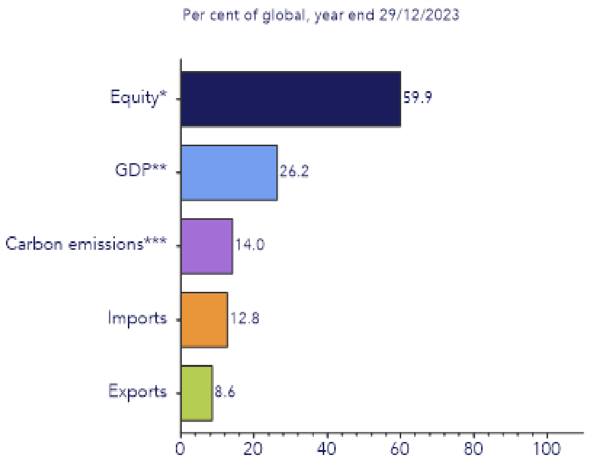
Additionally, Trump can unilaterally implement policies that immediately restrict immigration. By restricting the flow of immigrants, the labour market may experience shortages, leading to higher wages as businesses compete for a smaller pool of workers.

While he cannot directly dismiss the Fed Chair, he may nominate a more dovish successor after Jerome Powell's term ends in 2026. A more dovish Fed Chair might be inclined to keep interest rates lower for longer, which can stimulate economic activity but also risk higher inflation if the economy overheats.

Moreover, Trump's fiscal policies, including the extension of the expiring tax cuts, could lead to a higher budget deficit putting upward pressure on interest rates and inflation.

Does it matter for the rest of the world? Yes. As of the end of 2023, the US represented over 25% of global GDP. While the economy itself is surprisingly insular with just 12% of imports and 8% of exports the impact of tariff policy on global trade is likely to reduce global growth.

Chart 6: US world standing



Source: LSEG Datastream/Fathom (Note: Past Performance is not a reliable indicator of future performance)

On balance, US equities, which are the majority of global market cap, are likely to outperform their global peers given many stocks will remain insulated from the impact of tariffs, while a general policy of deregulation and the promise of corporate tax cuts are likely to be positive for US earnings.

How to Position

We remained underweight equities overall in the run-up to the election, as like many pundits we had expected a closer result with the potential for a drawn-out process. Regardless, our portfolios were well positioned with large exposure to a rising USD, unhedged exposure to Treasury yields which has been offset by a stronger USD, a position in US small caps and an overall bias to smaller and mid-cap equities.

Equities: Short-term boost or next leg higher?

Markets had been solid into the election but have rallied strongly afterwards, on a clear and decisive result. There is the potential for Trump to fail to get his tax cuts and other corporate-friendly policies through Congress, however, we see the potential for a rotation/catch-up from small-cap equities in the US.

US quarterly earnings season is almost done, with 82.7% of the S&P 500's market cap reporting at the time of writing. 3Q expectations are for revenues to grow 5.4% and EPS by 7.9%. Earnings are beating estimates by 6.4% in aggregate, with 66% of companies topping projections which is at the lower end of historical ranges. Critically for market sentiment though, 5 of the 6 largest Tech companies have reported earnings (NVDA reports later in November), beating EPS expectations by 10.4% in aggregate.

In Australia, major bank results suggest that conditions are deuterating and margins are under pressure. Trading at incredibly stretched valuations, we would expect a rotation out of banks that we saw in September to repeat soon.

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Cash Rates: RBA to cut later in 2025?

Market expectations have been pushed out again for rate cuts with inflation tracking in line with RBA expectations. February's Q4 CPI print will be crucial on whether they can move in March, with the strong risk that they don't. Deposit rates however are dropping mostly due to slower credit growth and a lack of deposit competition.

Corporate Bonds: Conditions remain supportive

Public market credit spreads continue to march inwards as strong capital flows hunting for yields support new issuance and hover up secondary market supply. With cash rates staying higher for longer, we still believe a 50/50 split between fixed and floating is advisable. Clients should add duration selectively when yields blow out as they have done recently.

Alternatives: Invaluable in times of stress

With the US election uncertainty out of the way, we would expect

Currencies: USD Strength Back with a Vengeance

Stronger US economic data and higher yields have pushed the USD higher. That run may continue as markets continue to factor in what a Trump Presidency will look like. Continued weakness in China should be putting further downward pressure on the AUD, but the RBA looking to remain on hold until 2025 while the Fed cuts the currency is being supported.

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