

U.S. election: Trump win

Key views

Republican nominee Donald Trump's unexpected election win points to increased market and policy uncertainty ahead.

We expect an initial sell-off in risk assets and flight to perceived safe havens. We see emerging markets as particularly vulnerable due to their reliance on exports and investor sentiment.

We expect steeper yield curves and see health care stocks outperforming due to likely reduced regulation under Trump.

We see Republican presidential nominee Donald Trump's unexpected election victory bringing market and policy uncertainty in the short run. Trump's agenda lacks detail and departs from the Republican Party tradition on trade, security and entitlements. Tapping into a backlash against the Washington status quo, he has often appeared at war with his own party and has surrounded himself with less known advisors.

Trump has said he may withdraw from or renegotiate trade deals as well as label China a "currency manipulator." This raises the specter of retaliatory protectionist moves by other nations. Any such tensions, coupled with general uncertainty over the Trump administration's goals, would likely initially result in "risk-off" sentiment hitting stocks and corporate bonds – and a flight to perceived safety havens such as gold and the Japanese yen.

U.S. Treasuries may initially benefit, but long-term bonds could come under pressure if markets perceive Trump's policies to widen the budget deficit. Emerging market (EM) assets could sell off in the short run due to their reliance on trade and investor sentiment, with Mexico looking vulnerable because of its dependence on exports to the U.S. We see many EMs supported by improving economies, easing monetary policies and a global focus on fiscal spending, but Trump's victory poses a challenge.

We see any market turmoil potentially leading the Federal Reserve to hold off on a widely expected rate increase in December, but the path thereafter looks less clear. Trump's planned income tax cuts could initially boost consumer spending, but might soon lead to a deterioration in the U.S. budget and rising rates, in our view. Similarly, plans to deport undocumented immigrants could cause labor shortages and rising wages over time. This might lift inflation, leading to a faster pace of rate increases. Also, the Fed's board could change significantly over the next four years, given that Trump has criticized the current low-for-longer monetary stance.

A balancing factor is that Trump's ability to carry out his stated goals looks restricted. Even though Republicans now maintain control of both the Senate and the House of Representatives, Trump may have to compromise with the party leadership. We could see gridlock on the legislative agenda as a result. Corporate tax reform and increased spending on infrastructure appear to have limited bipartisan support, however, and could be a ripe area for negotiation. Any infrastructure spending would come with a lag but should boost growth more than usual amid rock-bottom rates, in our view.

Steeper yield curves could pressure "bond proxies" such as utility stocks, and we see cyclical and value stocks outperforming. Health care stocks may rebound from recent losses on perceptions that a Trump administration would exert less pressure to lower drug prices. Yet we see drug pricing under pressure amid media and political scrutiny. We also expect rising uncertainty over potential attempts to repeal or shake up the Affordable Care Act.

We could see relative outperformance by financial stocks in the medium term amid higher inflation and steeper yield curves. Republicans also have proposed paring back post-crisis Dodd-Frank regulations. Yet uncertainty surrounding potential changes may unsettle investors, and any Fed delay in raising rates is a near-term negative. We generally see U.S. regional banks as a bright spot. Proposals to reduce their regulatory burden could help them grow faster and return capital to shareholders.

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