

## Market reaction will depend on election outcome

With just under two months to go before the US Presidential Election (November 8th) more focus is starting to come on what a Clinton presidency and a Trump presidency could mean for the US economy and financial markets. Various opinion polls show Hillary Clinton in the lead by just 3-6 basis points, which represents a narrowing in her lead compared to a few weeks back.

However, markets have so far taken a fairly sanguine view of precedings, with no noticeable 'election uncertainty' impacting investor sentiment. This relative indifference regarding the outcome may start to disappear if polls continue to narrow and suggest the race will go down to the wire. In the lead up to polling day, more attention and analysis is also likely to come on the candidates respective economic policies and the potential impacts these could have on the US economy.

From a market viewpoint, a Clinton victory might not solicit any significant moves on financial markets. However, a Trump victory could provoke a much greater reaction on markets, given his 'anti-establishment' policies and the uncertainty his presidency could create.

Currency-wise, historically, the US dollar has tended to react more positively to a Democrat in the White House than a Republican. If Donald Trump was victorious, there would be increased uncertainty. The dollar often strengthens during bouts of uncertainty and risk aversion. However, given that this uncertainty would be US centric, the initial reaction could be a weakening of the dollar.

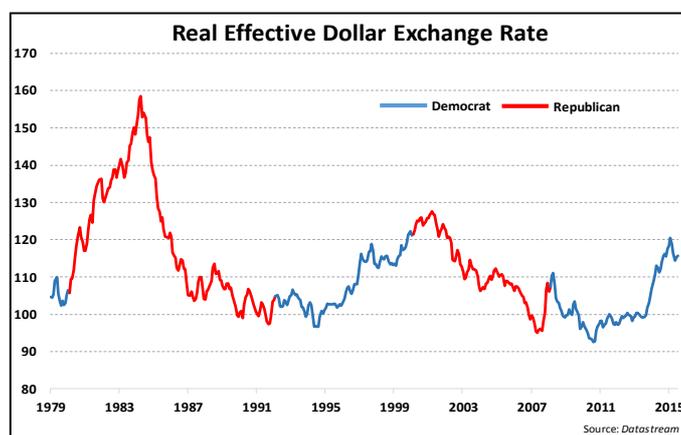
Although, Trump's policies of increased protectionism and an associated reduction in free trade, combined with a looser fiscal policy stance, could lead to higher inflation in the US.

This in turn could require tighter monetary policy which could result in a stronger dollar. Elsewhere, on the FX front, given the isolation bias of a Trump presidency, we are likely to see increased volatility and downward pressure on emerging market currencies in the context of the risk of an unwinding in globalisation and restrictions on free trade.

For bond markets, a Clinton win is unlikely to provoke any major moves. However, a Trump win could provide an immediate negative reaction. Given the uncertainty his victory could create, as well as expectations of increased expansionary fiscal policy and the upside risks to US inflation from this, we are likely to see an upward shift in the US yield curve. The curve is also likely to steepen given the heightened level of uncertainty that would prevail following a victory for the 'anti-establishment' candidate.

A Trump victory would probably provoke some degree of a sell-off on global equity markets. Equity investors tend not to like uncertainty and this, combined with a US Presidency that may be characterised by a protectionist stance on international trade, could weigh on investor sentiment. Emerging market equities could be especially vulnerable in this environment.

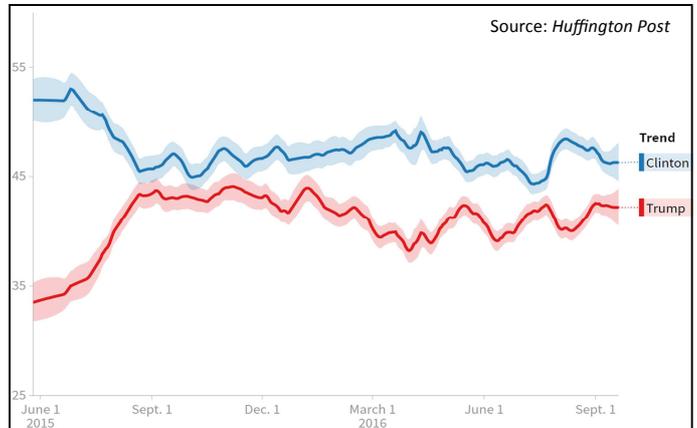
Overall, much like the election outcome, the impact on the US economy and market reaction to whoever becomes the 45th President is far from certain. However, a Clinton presidency probably involves far less uncertainty and therefore, the market focus in this scenario is likely to remain on the Fed. On the other hand, a Trump presidency throws up a whole raft of unknowns, meaning the market's focus may have to shift from the Fed to the White House.



## Two quite different policy platforms

In terms of the Democratic candidate, Hillary Clinton, her policies could at a broad level be described as ‘mainstream’, with a large degree of continuity with the current administration. One of her flagship policies is a \$275bn infrastructure plan to help deal with ageing roads, bridges etc. and provide a boost to economic growth. This would be funded by revenue generated through reforming the current business tax regime. In terms of income tax, proposals include tax cuts for the ‘middle class’ and increased taxes on high income households. Meanwhile, she is not currently advocating any changes to business/corporate tax rates but rather implementing “business tax reform”.

On the issue of trade, Mrs. Clinton has come out in opposition to the Trans-Pacific Partnership (a proposed trade agreement among twelve Pacific Rim countries, including Japan, known as TPP). However, in general she favours the US continuing to maintain a non-isolationist approach to international trade. On the sensitive topic of immigration, Hillary Clinton has portrayed herself as a strong supporter of immigrant rights, including a proposal to help create a pathway to citizenship for immigrants.



Meanwhile, Donald Trump’s policy proposals fall into the category of ‘anti-establishment’. In terms of infrastructure spending, Mr Trump has stated that he would at least double the \$275bn plan proposed by his rival Hillary Clinton. Meanwhile, in relation to taxes, a Trump presidency would favour tax cuts, both for households and businesses. Current proposals suggest he would cut the top rate of income tax to 33% (from 39.6%), as well as reduce the number of tax brackets from 7 to 3 (12%, 25% and 33%). He is also planning to cut the corporate tax rate from 35% to 15%.

Mr Trump’s ‘anti-establishment’ credentials are most evident in his policies on trade and immigration. Like Hillary Clinton, he opposes the TPP. However, here the similarities between the two candidates trade policies end. He has **very much an isolationist bias in relation to his trade proposals**, which involve more protectionism, including the introduction of tariffs to protect American businesses (current plan includes imposition of a 35% tariff on imports from Mexico and a 45% tariff on imports from China). He favours a renegotiation and/or potential withdrawal from existing trade agreements including NAFTA and the WTO. He is also proposing much stricter immigration controls.

The Washington based non-partisan Peterson Institute for International Economics has recently carried out an assessment of both candidates trade policies. **The research concluded that, if enacted, both candidates trade policies could be harmful to the US economy, albeit to varying degrees.** The report commented that the “proposed trade policies of both Hillary Clinton and Donald J. Trump” would “deeply harm the American economy”, with Mr Trump’s policies deemed to be potentially the most harmful.

**Of course an important point to bear in mind is the make up of Congress and the ability of either candidate to actually to implement their policies once in office.** The control of Congress is also up for grabs on November 8th. Republican’s currently control both the Senate and the House. However, the next President could face a split Congress which may limit their ability to implement their proposed policies. Indeed, given his difference of opinion on many policies with the Republican hierarchy, even a Republican controlled Congress might still entail some policy implementation issues for Donald Trump.

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