

CIO Viewpoint

US election result in the balance

Investment Solutions

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The day following the US presidential [election](#), it is unclear who won at the time of writing. Counting continues and the US political system faces the most contentious short-term result of days, if not weeks of legal challenges to resolve who will sit in the White House for the four years starting 20 January 2021.

With a number of key state results undeclared, incumbent President Donald Trump claimed that the result was “a [fraud on the American public](#),” telling supporters that “we were getting ready to win this election, frankly we did win this election.” He promised to take the count to the Supreme Court, adding “we want all voting to stop.” Rival Democrat candidate Joe Biden’s team shot back that the call to “shut down the counting of duly cast ballots was outrageous, unprecedented and incorrect.”

In some ways, the first part of the US election process closed with the polls on 3 November. Now, a second legal stage is beginning, because the winner does not hinge on the number of votes cast, but the allocation of seats in the Electoral College.

Pre-election polling proved inaccurate, and an anticipated Democratic sweep of the presidency, House of Representatives and Senate has not materialised. At the time of publication, the White House result depends on counts from the last states to report, in particular, Wisconsin, Michigan and Pennsylvania. In the meantime, it looks likely that Congress will remain divided, complicating the next administration’s ability to pass legislation and deliver their campaign promises. In particular, that will make it tougher to pass a pandemic recovery package.

The Covid-19 pandemic has made voting by mail more important in this election. However, the volume of early votes, and the different ways in which they are counted from state to state, means that they may flip any result or estimated result, based only on in-person voting. For now, only one state, Arizona, has [changed hands](#) in favour of the Democrats, compared with the 2016 election.

In the months prior to the election, President Trump tried to cast doubt on the vote’s credibility. Mr Trump consistently suggested that the US voting system was subject to fraud and worked to discourage voting by mail as well as cut funds to the US postal service. On 27 October, Mr Trump [tweeted](#), “Big problems and discrepancies with Mail In Ballots all over the USA. Must have final total on November 3rd.” Twitter flagged the message as potentially misleading and added a link describing how “voting by mail is legal and safe, experts and data confirm.”



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Key takeaways

- The US election result remains in doubt and open to legal challenges
- A number of key states have not yet declared their vote counts
- US stability looks likely to be further tested in the days and weeks ahead
- Market volatility may be short-lived; we raise our cash holdings and sell some US high-yield exposure.

Important information: Please read the important information at the end of the document.

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Weeks, not days

The US election system is complex because each state has its own rules and deadlines for counting votes. In some states, postmarked ballots count if they arrive after the election date, although the deadlines are different in each case. This includes states such as Mississippi, Kentucky, North Dakota and West Virginia, all of which traditionally vote Republican. Others, including solid Democrat states such as Vermont and Oregon, refuse mailed ballots delivered after the election date. In at least 32 states, counting of mailed ballots started before the election. By last week, an estimated [101 million votes](#) had already been cast and at the time of writing, turnout was the highest in more than a century.

There are of course recent examples of presidential election counts taking time. In 2000, it took three weeks for Florida to determine that George W. Bush had beaten Al Gore. In 2004, a result was not formally decided until the day after the election. In 2020, Florida state law says that a voter who mails-in a rejected ballot, because it is missing a signature for example, must get a second chance to vote.

Deadlines

Despite Mr Trump's assertions that the vote should be complete within hours of ballots closing, under federal law, there is an 8 December, legal 'safe harbour' deadline for settling any controversies before certifying the counting process at the state level.

By 14 December, the Electoral College has to meet in state capitals to ratify each state's count. Under the US electoral system, voters cast a ballot for an 'elector' who represents a candidate's party. These 538 electors then vote for the president on behalf of their state's voters, with each state declaring all of its seats for the candidate with the highest number of votes – with the exceptions of Maine and Nebraska.

The candidate winning a majority of more than 270 electoral seats then wins the presidency. This is why it was possible for Mr Trump to win all 29 seats in Florida in 2016 with a majority of just 2.2% of that state's vote. Nationally, he won 304 electoral seats with 2.87 million fewer votes than rival Hilary Clinton. And this is also why Mr Bush's victory in the same state in 2000, by a margin of 537 votes, was enough to hand him Florida's seats and an electoral college majority, despite losing the popular vote by almost 544,000 nationwide.

In the normal course of events, Congress will then ratify the election of the next US president when it first meets on 6 January 2021, and the president elect will be sworn into office two weeks later.

Trump's legacy

In December 2017, Mr Trump signed into law broad changes to the US tax code, cutting the corporate tax rate from 35% to 21%, which supported equity markets by increasing company profits and encouraging a round of share buybacks. Whoever sits in the White House next year will have to halt the pandemic and then reboot an economy that will contract by an estimated -3.8% for the full year 2020, compared with 2019, according to the Organisation for Economic Cooperation and Development (OECD). With the arrival of the Covid-19 pandemic, the US unemployment rate spiked in April at 14.7%, seasonally adjusted. By September, the rate had fallen to 7.9%, more than double its 2019 level.

Whichever way the final count lands, in some areas, Mr Trump's influence will be felt for decades. The president has used his term to alter the balance of the Supreme Court by appointing three conservative justices to the nine-member body over his term. The court, whose justices serve for life, is the highest judiciary body in the US and has the final say on all federal and state matters that affect federal law. Its first test, with Trump's latest appointment, Justice Amy Coney Barrett, will relate to a challenge to the Affordable Care Act put in place by President Barack Obama's administration. The ruling could overturn health insurance for an estimated 20 million Americans. Even more immediately, and as Mr Trump signalled, the Court may be called to rule in any contested vote counts.

More lasting may be the changes that Mr Trump brought about to the US's international position. The Trump administration has weakened the US's multilateral position, picking a trade fight with China, pledging to reduce the US trade deficit by imposing tariffs on imports, criticised the World Trade Organisation and then crippled its ability to rule in [disputes](#). Under a Democrat administration, trade relations with China would thaw, removing the threat of an all-out trade war. However, some tensions with China would persist, given that at their heart the issue is geopolitical leadership and whether the US will continue as the main engine of global growth.

Furthermore, Mr Trump took the US out of the Paris Agreement on climate change that committed the US and the rest of the world to limiting global warming to less than 2 degrees centigrade. Those commitments expire today (4 November).

Finally, we cannot ignore the rising social tensions over race and inequalities that have been a feature of the Trump presidency. After four years of inflammatory language, the social infrastructure and democratic norms underlying the US have come under great pressure. In the days ahead, the country's political stability and systems will be tested further.

Portfolio positioning

Until a winner is confirmed, there will be some market volatility. The yield on the benchmark 10-year US Treasury bond recorded its biggest daily decline since April, trading as much as 14 basis points lower at 0.76% as markets reacted to the likelihood of a split Congress and less chance of a massive stimulus package. We expect yields to remain low as, for now, the Federal Reserve can be expected to maintain its accommodative stance pending a stronger economic recovery from the pandemic. The dollar initially appreciated against the euro, yen, Swiss franc and other currencies, as investors sought a safe haven from higher market volatility. If Mr Biden eventually wins the election, the dollar should then return to a slightly more negative path as the prospects for international relations, and trade, improve.

Our clients' portfolios are well positioned for this uncertainty with overweight positions in cash and underweight allocations to equities. For now, we are also overweight Chinese debt and keep our short positions on the dollar.

If, as seems likely, Congress can only agree to less generous fiscal support or it is delayed and slow to materialise, some heavily-indebted US companies may face a worsening environment for credit. We therefore increase our cash holdings by selling some high-yield exposure.

Until the legal situation is clearer, the market environment will favour defensive sectors such as consumer staples, communication services, as well as the IT sector, which has outperformed throughout the pandemic period. We expect volatility to remain short-lived and offer better entry points to reposition portfolios accordingly.

With our existing portfolio positions in the Japanese currency, gold and US Treasuries, we believe that our clients' portfolios are well balanced and positioned to withstand this period of instability.

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