

# CIO Viewpoint

## Biden's US Ambitions Face Limits of a Split Congress

Investment Solutions

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On 7 November, news outlets declared Joe Biden and Kamala Harris winners of the US election with a 290 Electoral College majority, versus 214 for Donald Trump. Results, which may boost the Democrat win to 306 votes, are still pending for North Carolina and Georgia. President Trump has yet to concede, and continues to claim voter fraud and plan legal challenges without so far producing evidence of widespread irregularities.

When Mr Biden becomes the 46<sup>th</sup> US president on 20 January 2021, Congress is still likely to be divided between a Democrat-controlled House of Representatives and Republican-led Senate. The Senate's final majority depends on a run-off for the two seats in Georgia on 5 January 2021, the eve of the new Congress' first gathering.

The Congressional split complicates the task of building consensus over additional fiscal stimulus and increases the reliance on monetary policy for economic support. Republicans in the Senate are likely to oppose ambitious new spending and may show a sudden concern for the swelling US budget deficit.

Markets have therefore scaled back their expectations for the boost from an economic stimulus package. We believe that an eventual compromise may cut the Democrats' USD2 trillion proposal to between USD 500 billion and USD1 trillion.

### Relying on the Fed

Less fiscal stimulus means that monetary policy will have to be looser for longer, all else being equal, making the economic recovery more dependent on the Federal Reserve. A first rate hike may be delayed until 2024, and its large-scale asset purchases (LSAPs) continue.

During the campaign, Mr Biden pledged to raise corporate rates from 21% to 28%, still below the 35% rate in place through 2017. However, we do not believe that the new administration will be able to deliver a corporate tax increase while the economy is still running at around 80-90% of its pre-pandemic activity levels.

Mr Biden's presidential campaign promised more jobs, a higher minimum wage, to rebuild businesses, new spending on infrastructure projects and support for sustainable energy. Many of these initiatives would underpin corporate earnings, and largely offset any corporate tax hike designed to pay for cleaner energy.



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### Key takeaways

- Joe Biden wins US presidency and Congress looks likely to remain split
- The Biden administration will push for a stimulus package and increased clean energy spending
- The economic priority remains a full pandemic recovery; without ambitious stimulus, the economy will rely more on Fed policy
- We use some cash holdings to buy emerging debt as we expect the dollar to depreciate.

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

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The Biden administration's pledges offer a radically different ambition for the US globally. Given the geopolitical stakes, tensions with China will undoubtedly continue. Nevertheless, some thawing of trade tensions is likely, notably with the removal of some US import tariffs on Chinese goods. Mr Biden has also promised to return the US to the Paris Agreement on climate change on his first day in office.

### **Headwinds**

However, Mr Biden's priority will be to complete the recovery. He inherits a US economy forecast to contract by -3,5% for the full year 2020 compared with 2019, according to our estimates, and an unemployment rate of 7.9% in September, more than double its 2019 level.

The Biden administration will also be constrained by Mr Trump's appointments to the Supreme Court. Over the past four years, Mr Trump appointed three conservative justices to the nine-member body, who serve for life. The court is the highest judiciary body in the US, and has the final say on all federal and state matters that affect federal law. The Court is scheduled to begin examining President Barack Obama's Affordable Care Act this week in a challenge that seeks to overturn health insurance for an estimated 20 million Americans.

### **Positioning portfolios for the new administration**

In the absence of a strong economic boost from government stimulus, yields have dropped, reflecting the slower expected pace of growth. We have reduced our exposure to US high-yield credit as the risk of corporate defaults rises in line with expectations for lower fiscal support to businesses.

We maintain our current balanced risk stance in client portfolios. In the light of the US election, we are increasing our exposure to emerging-market debt in local currencies, based on the improving outlook for international trade as well as expectations for a weaker US dollar.

In equity markets, we expect growth and quality sectors, such as information technology, to remain supported. In the short run, stocks will continue to react to the politically complex legislative power balance, with slower US growth and a global outlook that remains clouded by the pandemic.

This said, we remain cautiously optimistic on the prospects for the US economy, since American household incomes continue to rise. Consumption will also be resilient thanks to the high savings rate of households. Finally, the recovery in house prices, although modest, will benefit the outlook for consumers.

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