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Market View

Global markets had been set up for a decisive victory in the US election for Joe Biden and the Democrats, as it turned out it was closer than they thought. The Democrats appear to have won the Presidency but lost seats in Congress and may have also lost the Senate, which could prove to be, very significant. US markets generally lean towards the more pro-business Republicans but had persuaded themselves that a less aggressive President together with a promised stimulus package would outweigh higher taxes and greater regulation. What would be even better for the markets would be a less confrontational individual with a Senate controlled by the Republicans, thus restricting a Democratic President's room for manoeuvre. Who wins the Senate will depend upon a run-off in early January. In the meantime the second wave of the pandemic is accelerating, social lock-downs have been reintroduced across Europe, and now the remaining parts of the UK. So far markets have been more relaxed as these new restrictions are not as stringent as they were before. New infection numbers are, however, also growing in the US. Whoever finally wins the White House will not move in until January 20th, that may dictate how this second wave will be handled in the USA. When the final result (after the legal challenges) for both the Presidency and Senate is declared what will be the impact for investment markets?

US Presidential Election

Stimulus: The Chair of the Federal Reserve Bank has stated on many occasions that each new monetary stimulus package has a lesser impact on the US economy. QE works best in conjunction with increased capital spending by governments. Prior to the election Senate Democrats tried to implement a $2trillion plan but were rebuffed by Republicans that only wanted to spend around $1trillion. Clearly, any stimulus is better than nothing but it does need to be targeted. The Democrats are pushing for their version of a "Green New Deal", whether this happens or not depends on who controls the purse strings i.e. the Senate. If the Democrats do manage to win the Senate then US Treasuries should see yields rise and the cyclical businesses will find favour at the expense of technology. As we write the most probable outcome is for a Republican Senate and thus a smaller more focussed package.

Tax: A Democratic Presidency will look to raise taxes both on individuals and businesses. An increase without a counterbalancing stimulus package would economically not be well received by markets.

Regulation: Trump's Presidency was marked by the rolling back of regulations across many industries such as banking, energy and healthcare. Also, there was a refusal to restrict the activities of the big technology companies. A Democratic President may seek to reinstate these controls. Much will depend on his cabinet appointees and on the make-up of the two houses of Congress. The general trend though will be towards greater regulation.

China: Hopes that there will be a thaw in US/China relations may be dashed post the election. The Democrats have been just as critical of China. A Biden Presidency might, however, be more consistent and predictable?

Trade: Just as it is with China the US is in a trade dispute with the EU and again hopes of an early resolution are likely to be disappointed. The US may focus instead on ratifying the trans-Pacific trade agreement (now known as CPTPP) and reinvigorating NAFTA with Mexico and Canada. For the UK, Trump claimed to have offered the UK a free trade deal but no details were ever disclosed. The suspicion remains that this was all part of the UK/EU trade talks "poker game". The UK is, however, negotiating to join the CPTPP, thus, if the US also re-joins a UK/US trade deal would be made by default. A Biden victory, given the traditional Democrat pro-Irish bias might just give the UK a greater impetus to agree a deal with the EU sooner rather than later.

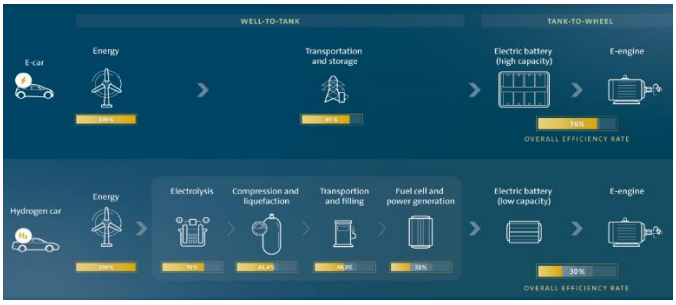
Overall, a Democratic President held in check by a Republican Senate, with a more constructive tone to international relations will for the markets be just fine.

Pandemic Second Wave

Boris Johnson has announced that the remaining parts of the UK that are not under restrictive social movements would now do so. This new national lockdown is not the same as the first economically damaging one. Clearly, the hospitality, travel and retail industries remain in a very precarious position, as we have said before, they will need the vaccines to arrive before they can truly recover. However, it would appear that most other industries should remain relatively unaffected by this latest move. This is a social

lockdown rather than a total one. It will have an economic impact but, hopefully, nowhere near as severe as the first one. Economists will also be very wary that economies bounced strongly once the restrictions were eased and won't want to be seen to be wrong again! For the markets, more lock downs mean more money printing and also increases the probability that true stimulus packages will arrive. Christmas for many in the impacted industries will be crucial, what happens at the beginning of December may well be the tipping point for many. We also need to watch for new infections in the USA, Thanksgiving is coming this month.

Electric Batteries v Hydrogen Fuel Cells



As governments globally introduce Green New Deal programmes, as part of currently modest fiscal stimulus programmes there is a battle between hydrogen fuel cells and batteries to replace petrol and diesel engines. Fuel cells have double the present range of batteries and can be quickly refuelled. Both will require massive infrastructure spending. Germany and China are already investing heavily and capital is flowing into new hydrogen production.

Hydrogen produced from renewable sources is a "hot" investment at present. But as the above chart shows it is not a simple process. The investment case relies on the attraction of a quick refill and longer range. If battery technology develops as anticipated and the recharging infrastructure grows as it should, then the case for hydrogen fuel cells will weaken.

UK/EU Trade deal timetable

16th November. EU leaders meet in Berlin. First opportunity for approval of any possible deal and the first "true" deadline.
23rd to 26th November. European Parliament meets. Needed to ratify any Trade agreement made by EU Leaders.
10th to 11th December EU Summit. Last scheduled event for an agreement to be signed.
31st December. End of Brexit Transition Period. If no agreement, UK defaults to World Trade Organisation terms of trade and tariffs.

We are approaching the end of the current timetable for the UK and the EU to agree a new free-trade deal. As we know, nothing in the EU happens until the very last possible minute and the probability is that both sides might "create" a crisis as they run the clock down. It is though possible that with all that is going on in the world at present a deal might be done by the middle of this month, but based on historic norms the probability is low. The markets are not expecting anything other than a "skinny" deal by the end of the year with the "fat" added on a piecemeal basis throughout 2021. Recent strength in the pound indicates that the markets remain relaxed, for now.

Markets

In the short term markets are unpredictable, but over the long term they follow a broad roadmap. There is a cycle, every 9 years or so, after annual average growth of around 5% to 7% above inflation, leads to a c33% pull-back in share prices. This disruption tends to coincide with US Presidential elections and takes around 12 to 18 months to work through prices before the uptrend restarts. Covid-19 lockdowns in March gave us a 34% pullback, and we have just had the election, so we have ticked three boxes for the roadmap. However, it has also only been eight months since the shock, so it is perhaps too early to expect to be out of woods just yet? In the very short term predictions remain difficult, as in the UK and Europe economic decisions remain in the hands of health professionals not Central Bankers or Chancellors. For the markets, the one good thing that will come from the election is that it is close to becoming history and thus can be removed from the market's pricing mechanism. It thus clears the air for the eventual start of the new cycle. When this happens will depend on the pandemic passing and/or the vaccine(s) arriving, we should shortly hear the results of the first clinical trials. The news flow on the pandemic and the election will remain intense throughout the month. We do need to remember that the Trump first term does not end until the 20th January.

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