

# US ELECTION FIXED INCOME IMPACT

## LIKELY POLITICAL MAKEUP OF WASHINGTON: ELECTION OUTCOME REMAINS TOO CLOSE TO CALL

President Elect: Joe Biden – Democrat

Senate: Republican Control – no change

House of Representatives: Democratic control – no change

Presidential outcome may be challenged in court – continuing to monitor

### KEY FEATURES:

- The failure of either party to get a clean sweep will hamper new policy initiatives
- If President Trump stays in power, basic policy agenda will remain as it has been
- Fiscal loosening will still be on the agenda but a large package is now unlikely and tax hikes are less likely
- A shift in trade talk with global partners – a less aggressive tone is likely with Biden
- Refocus on global partnership – no change under Trump

In the table below, summaries in **Green** highlight potential changes to policy/monetary stances and London & Capital’s Fixed Income allocation response, respectively.

	PRE-ELECTION	POST-ELECTION
<b>MONETARY POLICY</b>	<ul style="list-style-type: none"> <li>▪ Tilt to “lower for longer”</li> <li>▪ Zero rates</li> <li>▪ Quantitative Easing (QE) and wider liquidity support</li> </ul>	<p><b>No change in policy stance</b></p> <ul style="list-style-type: none"> <li>▪ The Federal Reserve (the Fed) will keep an eye on fiscal policy, but this will complement monetary policy not substitute it</li> </ul>
<b>FISCAL POLICY</b>	<ul style="list-style-type: none"> <li>▪ Second fiscal boost failed</li> </ul>	<p><b>Targeted fiscal package likely</b></p> <ul style="list-style-type: none"> <li>▪ Focus on supporting consumers and companies</li> <li>▪ Potential \$7tn public spending boost over 10 years. This requires tax hikes but may fail in the Senate</li> </ul>
<b>TREASURY MARKET</b>	<ul style="list-style-type: none"> <li>▪ The short-end of the yield curve is anchored by the Fed</li> <li>▪ Longer-end yields are expected to rise, reflecting fiscal boost and inflation expectations</li> </ul>	<ul style="list-style-type: none"> <li>▪ The short-end of the yield curve will still be anchored by the Fed</li> <li>▪ The longer-end yields will be under less pressure</li> <li>▪ Significant yield curve steepening may be delayed</li> </ul>

<b>CREDIT SPREADS</b>	<ul style="list-style-type: none"> <li>Continuing to narrow, reflecting improving credit dynamics, low Treasury volatility, QE and strong investor demand</li> </ul>	<p style="text-align: right;"><b>Basic fundamentals remain intact</b></p> <ul style="list-style-type: none"> <li>Supporting further gradual spread narrowing to pre-COVID-19 lockdown levels</li> </ul>
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**CREDIT SECTOR ALLOCATION**

<b>BANKS</b>	<ul style="list-style-type: none"> <li>Improving balance sheets</li> <li>Positive earnings trends</li> <li>Supportive Fed and regulations</li> <li>Source of strength</li> </ul>	<p style="text-align: right;"><b>Maintain allocation</b></p> <ul style="list-style-type: none"> <li>Yield curve steepening is good for banks</li> <li>We continue to watch for any regulatory changes that could impact earnings but will bolster the balance sheet</li> </ul>
<b>UTILITIES</b>	<ul style="list-style-type: none"> <li>Key stable economic sector</li> <li>Resilient balance sheets</li> <li>Regulated</li> <li>Non-cyclical</li> </ul>	<p style="text-align: right;"><b>Maintain allocation</b></p> <ul style="list-style-type: none"> <li>Key players in renewable energy</li> </ul>
<b>PHARMA/HEALTHCARE</b>	<ul style="list-style-type: none"> <li>Strong balance sheets and key economic sector</li> <li>Regulated</li> <li>Benefitting from COVID-19</li> <li>Demographics supportive</li> </ul>	<p style="text-align: right;"><b>Maintain allocation</b></p> <ul style="list-style-type: none"> <li>Vaccine rollout is a positive for earnings</li> <li>We continue to watch for regulatory oversight and change in pricing mechanism</li> </ul>
<b>TECH/TELECOM</b>	<ul style="list-style-type: none"> <li>Key economic sector</li> <li>Key beneficiary of new global work trends</li> <li>High operating cash flow sectors</li> <li>Barrier to entry</li> </ul>	<p style="text-align: right;"><b>Maintain allocation</b></p> <ul style="list-style-type: none"> <li>Tax burden rise is a potential threat but is unlikely to change credit dynamics</li> <li>Regulatory oversight to be monitored</li> </ul>
<b>CYCLICAL SECTORS – MAJOR GLOBAL CORPORATES</b>	<ul style="list-style-type: none"> <li>Key beneficiary of reflation trade</li> <li>Fiscal and monetary support</li> <li>Boosting cash flow</li> <li>Successful debt maturity profile lengthening</li> <li>Earnings improving</li> </ul>	<p style="text-align: right;"><b>Increase allocation</b></p> <ul style="list-style-type: none"> <li>Reflation trade may give a further boost</li> <li>Infrastructure boost is a positive</li> <li>Energy sector will watch for new energy initiatives</li> <li>More encouraging trade outlook</li> </ul>
<b>YIELD ENHANCING STRATEGIES</b>	<ul style="list-style-type: none"> <li>Zero/negative rates backdrop</li> <li>Diversified portfolio</li> <li>Focus on major banks, utilities, tech/telecom and pharma</li> <li>Focus on short-medium maturity bonds</li> <li>Maximising coupon flows</li> <li>Low credit risk</li> </ul>	<p style="text-align: right;"><b>Maintain allocation</b></p> <ul style="list-style-type: none"> <li>Many of the sectors will benefit from reflation trade</li> <li>Low rate risk profile</li> </ul>

INFLATION-HEDGING

- Major deflationary shock from a hit to potential economic growth rates
- Central Banks are willing to tolerate higher inflation
- Weak commodity prices keeping low inflation
- Wage pressures under control
- Inflation linked bonds provide negative yields and long duration
- Cyclical exposure good inflation hedge
- Banks a good play on inflation

Maintain cyclical and banking exposure to benefit from any uptick in inflation

EMERGING MARKET

- Selective exposure
- Focus on quasi-sovereign key sectors
- Benefit from low rates
- Benefit from weak USD

- Maintain allocation
- Looking for wider opportunities from less strident trade policy out of the US

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