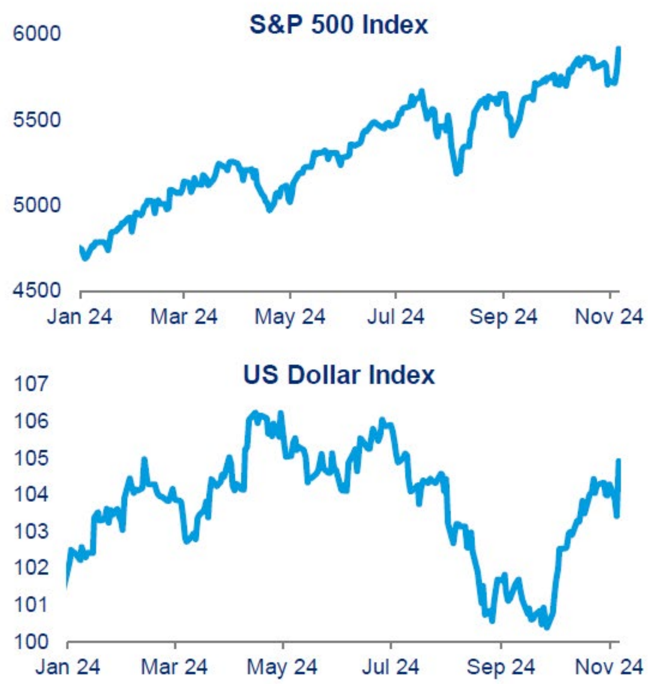
Newsletter on Market Implications of the U.S. Election

Former U.S. president, Donald Trump, has won the election on November 5th, 2024 and will begin with his second-term as the 47th president of the United States in January 2025. At the same time, the Republicans will regain the majority seats in the Senate and the House of Representatives. With control of both chambers of the Congress, the new administration is expected to encounter less resistance in vetting the policies pledged by Trump, e.g., trade tariffs, tax cuts, immigration restrictions, etc. The global markets have already reacted in anticipation of such potential changes to the U.S. policies. The U.S. equity markets rallied to record high while the U.S. bond markets sold off as the yields jumped. Also, the U.S. dollar strengthened against other major currencies. In light of the upcoming new regime in the U.S., the Retirement Scheme Team takes the liberty to provide an update from our investment managers on the views of potential implications to the global markets.

Financial Markets Movements



Source: Bloomberg. Data as November 6, 2024.

Global Equity Markets

U.S. Equities:

Trump is well-positioned to implement his policy agenda. He has pledged to cut taxes and de-regulation further while also raising tariffs and restricting immigration, the combination of which will be reflationary for the U.S. economy. The prospective of U.S. equities remains constructive on a 12-month view, underpinned by modest earnings growth, although if the yield curve continues to move higher, this will begin to impact valuations.

On the negative side, there are some risks to the U.S. company profitability from a Trump win since tariffs could pose a headwind for profit margins in some sectors, which rely on China-imported goods. Meanwhile, an expected clampdown on immigration could drive wage growth, particularly in consumer and construction sectors. Companies with pricing power should fare better in this environment. There is no doubt that the U.S. will be taken out of most global efforts to tackle climate change under Trump's administration. Business investments in the U.S. value chain around key climate technologies is likely to be set back.

On the positive side, for U.S. companies, Trump's proposed corporate tax cuts would clearly be a tailwind. Deregulation should be supportive for U.S. equities as well, particularly for larger banks and areas of technology such as artificial intelligence outside of the mega cap tech companies. Indeed, structural investment themes in some cases could thrive in a new Trump era where innovation is likely to be underpinned by looser regulation to maintain US technological leadership.

China Equities:
The Chinese government, along with the general population and investors, generally expected that Trump would be elected as the next President of the US. However, with the Republicans controlling the Senate and the House of Representatives, this has a far-reaching implication. This is likely to force the Chinese government to adopt more long-term and proactive measures to restore and maintain the growth of aggregate domestic demand, and possibly increase its support for real estate in order to cope with the substantial tariffs going forward and the longer-term negative impact of prolonged U.S. protectionism on Chinese exports.

Despite the challenges, China manufacturing/export industry has successfully climbed up the value chain and should show resiliency. While China lags in certain manufacturing fields such as high-end semiconductors and high-precision instruments, "Made in China" has continued to gain new market share due to its high product quality at reasonable, even low, product prices. While potential future tariffs of up to 60% may be destructive in the short-term, the impact is not one-sided as it is likely to hurt the U.S. economy as well. As a result, the long-term impact of tariff hikes may be overestimated and likely be manageable.

Following the announcements of policy easing by the Chinese government, investor sentiments shifted from being bearish to being bullish. Although the market will inevitably experience significant fluctuations in the future with the changes in U.S. policy, the investor mentality appears to have shifted from overly-pessimistic on China economy.

European Equities:
Tariffs are certainly the main risk, but it is still uncertain about the policies of Trump's administration on trade at this point especially on the extent of tariff war with Europe, which may impact pharmaceutical, automobile, and machinery companies. Having said that, this tariff may have various conditions and exemptions for strategically-important areas including defense, energy, and pharmaceutical companies.

Another factor impacting European equities might be China. China is the second largest trading partner of the European Union after the U.S. Europe's largest imports from China are telecommunications equipment, electrical machinery, etc., while its main exports are automobiles, medicines, etc. These are all key sectors. If these trades are negatively impacted, it will hurt the European economy. Having said that, China is likely to announce further fiscal stimulus, which may be positive for many European companies.

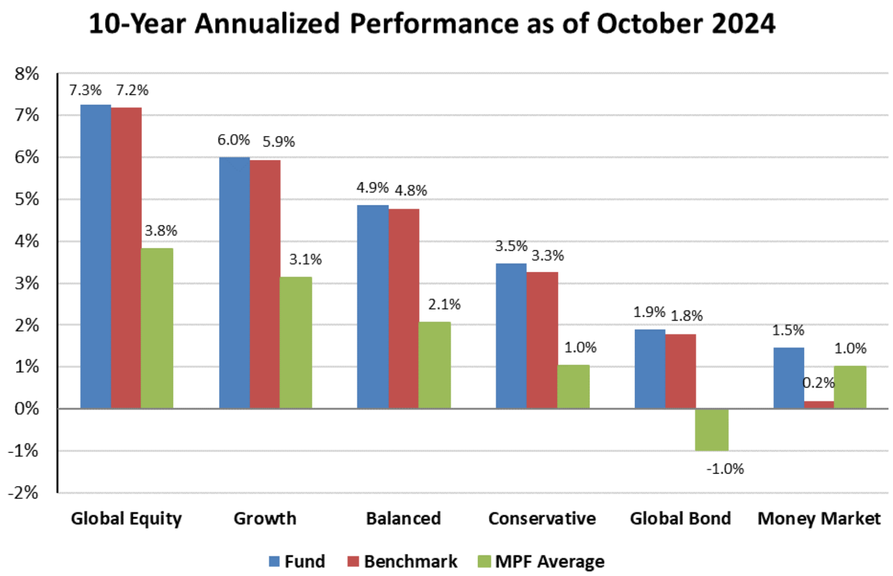
Global Bond Markets
Currently, the Republicans will sweep both the Senate and House of Representatives in addition to the presidency. The fixed income market, therefore, is expected to price in both the impact of greater fiscal easing and more aggressive trade policy. This couples with ongoing strength of the U.S. economy, which should lead to

higher yields, bond underperformance, and continued U.S. dollar strength in the short-term. Markets have already moved significantly in this direction since the election. That being said, the U.S. long-term imbalances, including fiscal issues, may ultimately weigh on the U.S. dollar in the long run.

Investment grade bonds and high yield bonds also reacted positively to the election outcome, as the markets moved to price in a more supportive backdrop (potentially lower corporate taxes and reduced regulation) for the corporate sector. Financials, energy, and defense sectors will be in a position to benefit from any regulatory relaxation.

Looking to international implications, European growth is fragile and corporate fundamentals have not remained as strong as the U.S., which leaves the European markets vulnerable. The struggling European auto sector is likely to continue to underperform with trade tensions being the primary concern whilst other cyclical sectors will also struggle. For Asia, weaker Asian currencies versus the U.S. dollar is expected. Meanwhile, Asian investment grade spreads should continue to be supported by relatively high total yields and strong technical factors.

Conclusion



Source: HAPFS Office, HKIFA

Although the global markets have shown a knee-jerk reaction to Trump's presidency, the new polices may take time to unfold and there could be uncertainties along the road. Also, more importantly, we would like to reiterate that members should focus on long-term rather than reacting to short-term news given that the retirement purpose of the Scheme, which has added value to members over the long run (see chart above). Members are advised to regularly review the retirement investment portfolio to ensure that it remains in line with the investment objectives and the risk tolerance level, taking into consideration of the investment time horizon before retirement.

Hospital Authority Provident Fund Scheme
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