

# Top Trumps?

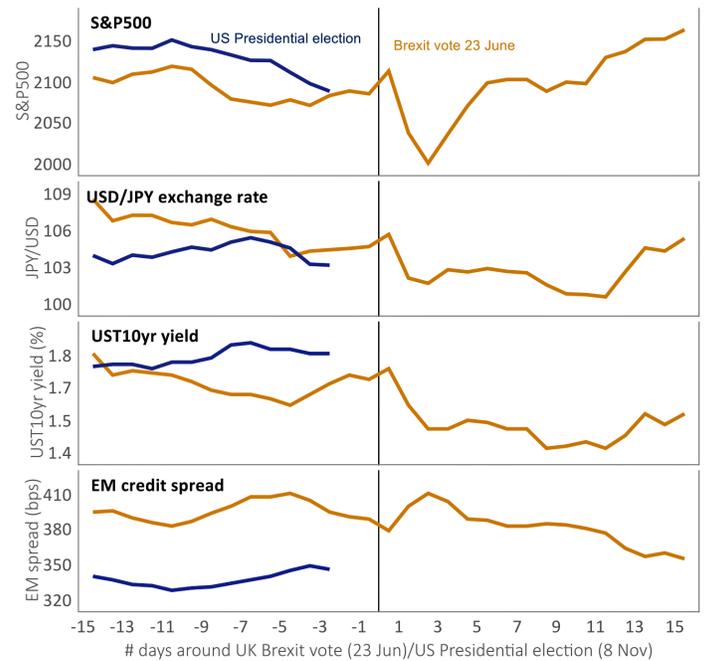
November 7, 2016

**There are a number of political outcomes in the US election, it isn't just about who is president. The balance in Congress is also important.**

A victory for Hillary Clinton in Tuesday's US presidential election will be greeted by the market with relief for 'more of the same' rather than the radical uncertainty of a Trump presidency. The outcome of the US Presidential election is of far greater global significance than the UK referendum on EU membership, but the Brexit vote nonetheless may prove instructive as to the short-term market reaction to a Trump victory. Irrespective of the vote on Tuesday and the market reaction on Wednesday and beyond, the fracturing of popular support for the economic and political status quo is raising the political and policy risks faced by investors.

In the chart on the right, the evolution of the S&P500 (top panel); Japanese yen (2nd panel); 10-year Treasury yield (3rd panel); and EM credit spreads (bottom panel) is shown for the fifteen days in the run-up to and after the UK Brexit vote (the gold lines) alongside the countdown to Tuesday's presidential election (the blue line). The short-term market reaction to the Brexit vote was a surprise - despite opinion polls suggesting a close outcome – and dismay with global stocks down 7% and a rally in 'safe haven' assets such as US Treasury bonds and the yen. But the sell-off in risk assets proved short-lived, especially for emerging markets, although the post-Brexit fall in 'core' government bond yields was only fully unwound last month.

**Exhibit 1**  
Countdown to US Presidential Election & the UK Brexit Referendum



Note: EM spread is the credit spread on the JP Morgan EMBI Global Diversified Index  
Source: Bloomberg; Macrobond; data at 4 November 2016

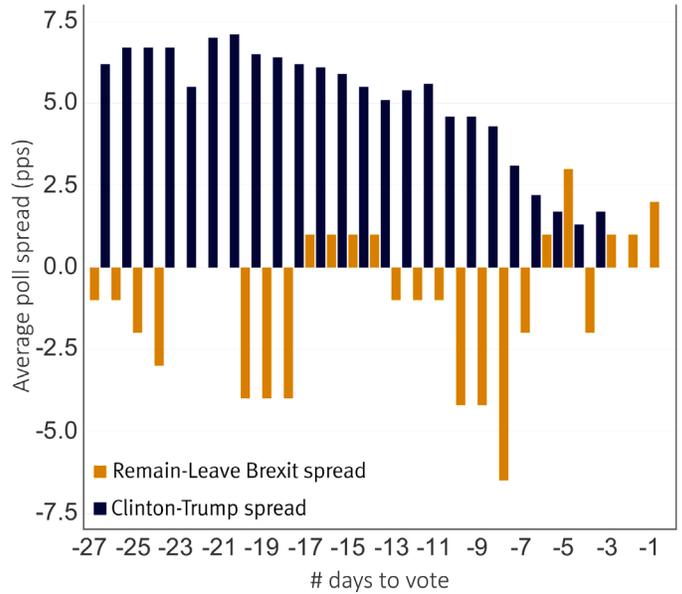
One of the many differences between the UK referendum and the US presidential election is that the former had an irreversible binary outcome (in or out of the EU) while the US President is constrained by Congress and their decisions are reversible. The Congressional elections will also be important in determining the market reaction to a Trump or Clinton victory in the presidential race. Financial markets would likely react negatively to a ‘clean sweep’ of Congress (Senate and House of Representatives) and the Presidency by either the Democrats or Republications. Inasmuch as a Republican Congress is likely to be viewed as less of a constraint on a radical and maverick Trump presidency, it is a more ‘risk-off’ as well as more likely scenario than a Democratic ‘clean sweep’.

As the blue bars in Fig. 2 on the right illustrate, the spread between the Clinton and Trump is now within the margin of error (as was the case in the run-up to the Brexit referendum). Whatever happens on Tuesday, Wednesday will be interesting.



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**Exhibit 2**  
 Average Poll Spread in the Run-up to Voting Day



Source: Bloomberg; data at 4 November 2016

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