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UOB Investment Insights

Quick Note

8 January 2021

What Should Investors Make of The US Elections' 'Blue Wave' Outcome?

- The Democrats now control 50 out of 100 seats in the US Senate, giving them a slim majority with incoming Vice President Kamala Harris. This also means the Democrats control the White House, the Senate and the House of Representatives, constituting a 'Blue Wave'.
- The slim Senate majority means this 'Blue Wave' may not be as market-negative as the media portrays it to be. Moderate policies will take centre stage; a larger fiscal stimulus bill will be on the way; while a tax hike is unlikely this year.
- Investors may want to consider being more selective in US equities and fixed income, while remaining positive on Asian equities.

Democrats take control of the Senate (barely)

- Following the US elections last November, the US state of Georgia proceeded to conduct runoff elections for both of its US Senate seats since no candidate won 50% of the votes.
- The latest results show that Raphael Warnock (Democrat) and Jon Ossoff (Democrat) have won both seats, giving the Democrats 50 seats total in the US Senate. Both candidates have won by a margin of more than 0.5% (Figure 1), hence there will not be a recount.
- Although the Republicans hold the remaining 50 seats, incoming Vice President Kamala Harris will cast the tiebreaker vote as the US vice president is also the president of the US Senate. This allows the Democrats to control both houses of Congress and the government, resulting in a 'Blue Wave'.

Figure 1: Results of the US Senate Elections for the State of Georgia

State	Candidate Name	Latest Results
Georgia	**Jon Ossoff (Democrat)**	**50.5%**
	David Perdue (Republican)	49.5%
Georgia (Special Election)	**Raphael Warnock (Democrat)**	**50.9%**
	Kelly Loeffler (Republican)	49.1%

Source: Bloomberg, as at 0642H Singapore time on 8 January 2021.

Setting the stage for US policies

- The slim 51-50 Senate majority for the Democrats places more influence on the moderate Democrats and is an important reason why investors need not be too bearish over this 'Blue Wave'. The thin majority means the Republicans need just one Democrat to switch votes to defeat a more extreme agenda, and therefore these moderate Democrats will likely be courted by both parties to make or break votes. Hence, future policies will need to avoid being either too liberal or too conservative to pass muster.
- The Democrats will likely push for a larger fiscal stimulus bill shortly after Biden takes office in two weeks' time, followed by an infrastructure bill possibly in H2 2021. This will be positive for risk assets like US equities, but longer-term US bond yields could rise due to the increased debt burden and a more optimistic growth outlook.
- With more fiscal stimulus driving economic recovery, the US Federal Reserve (Fed) can afford to soften their monetary stimulus measures this year, removing a tailwind for US bonds.
- Possible tax hikes are also on the Democrats' agenda and a cause of concern for investors. Biden will likely try to raise taxes on wealthy individuals[1] this year, but the uncertain economic recovery and the associated political risk for the 2022 midterm elections reduces the probability of a broad corporate tax hike this year.
- Policy-wise, both Democrats and Republicans continue to view China as a rising threat. Tighter regulation on the US Technology sector continues to receive bipartisan support. A significant expansion of Obamacare could prove challenging with the slim majority, which should leave the Healthcare sector relatively unscathed for the near-term.

Figure 2: Market reactions

Equity markets indifferent		
Equities: Global equities were initially cautious of the 'Blue Wave', but welcomed the possibility of a larger US stimulus package.	**Government Bonds:** US government bond yields, especially the 10-year yield, rose as markets braced for higher US debt after another round of fiscal stimulus.	**Currencies:** The US Dollar Index rose slightly, but the USD weakened against the EUR, JPY and CNY.

[1] **Individuals earning more than USD$400,000**

Figure 2: Market reactions (continued)

	Name	6 to 7 Jan 2021
US Equities	S&P 500 Index	+2.06%
	NASDAQ Composite Index	+1.94%
European Equities	STOXX Europe 600 Index	+1.88%
	FTSE 100 Index	+3.70%
Asian Equities	Nikkei 225 Index	+1.22%
	Shanghai Composite	+1.35%
	Straits Times Index	+1.65%
US Government Bonds	US Generic Govt 2 Year Yield	+1.58 bps
	US Generic Govt 5 Year Yield	+8.26 bps
	US Generic Govt 10 Year Yield	+12.46 bps
Currencies	US Dollar Index Spot	+0.44%
	USD-JPY Cross-Rate	+1.06%
	EUR-USD Cross-Rate	-0.21%
	USD-CNY Cross-Rate	+0.35%

Source: Bloomberg, as at 0900H Singapore time on 8 January 2021.

What should investors do?

- **Be selective in US investments.** A rise in long-term US bond yields will benefit some value sectors like **US Financials**, but will be a headwind for **longer-dated US Treasuries**. The **US Technology** sector will likely face tighter regulations, though this is not an immediate priority for the Biden administration. We will continue to monitor for possible developments on this front.

- **Remain positive on Asia.** Although the US is unlikely to change its stance on China, we continue to remain positive on the **China Megatrend** because of its potential domestic growth that will likely be driven by China's "dual-circulation" economic model. The Biden presidency will likely bring back Obama's tilt towards Asia; the US has to rebuild relationships within the region if they want to slow China's rise. Overall, this will be positive for **Asian equities**.

- **Ensure adequate diversification across assets classes and regions.** Although the risk of extreme policies being implemented has reduced significantly with the slim Senate majority, there could be some policy uncertainties ahead for the US. Therefore, review your portfolio periodically in accordance with your risk profile and consider a mix of fixed income and equities.

- Please speak to your UOB Advisor to determine the right solutions for you in light of these latest developments.

All data are sourced from Bloomberg unless otherwise stated.

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