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The US election outcome will change the investment landscape

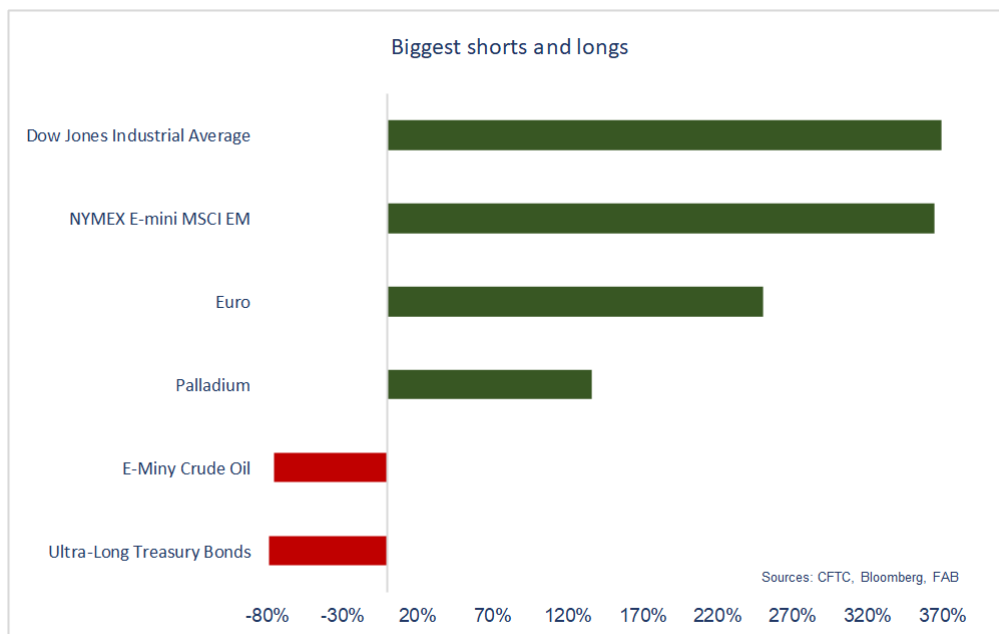
◆ Investors have built large speculative positions in industrial companies, emerging market stocks and the euro.

◆ Such large positions are likely to trigger some short-term movements as the election results start to come out.

◆ However, the long-term horizon will depend on the make-up of the US Congress and the White House.

◆ A Republican victory is seen as less bullish for emerging markets and better for the dollar against other currencies.

◆ The FAB AAC remains slightly underweight in equities, and overweight in IG bonds and gold



This is it. The US presidential election day happens today. However, in some ways, it is some 60% done. By the time polls officially opened, more than 99 million votes had been cast by mail or in early voting. Still, the opening of the normal booths also means that the other ballots start to be counted and the results made public, which offers investors a clearer picture of the political landscape in the world's largest economy.

With the latest polls showing a nearly tied race, it is hard to predict what the outcome will be. However, investors have been expressing their views in futures markets for weeks. A look at the positions in place as of last Thursday, the last available data, suggests that many investors had been betting on a Democratic sweep. There were large bullish positions in the Dow Jones Industrial Average, the Russell 2000 and the MSCI Emerging Markets index. The biggest shorts were crude oil and long-dated Treasuries.

Indeed, if the Democrats take the Senate and the White House, as polls suggested as recently as Saturday, they would probably move quickly to enact up to US\$3.6 trillion in fiscal stimulus. This could weaken the dollar. A weaker greenback helps emerging markets, as does the trade-friendly stance of Democrats. All these also benefit small-cap stocks and industrial companies.

Meanwhile, former Vice-President Joe Biden has suggested that he could lead something akin to a national lockdown if the Covid-19 case count is still high by the time he takes office. That would undermine oil demand, which would be in line with the short position in crude. The large amount of stimulus, along with the potential for economic contraction on the back of a potential closure also suggest more Treasury issuance, which would be bearish for these bonds. So much stimulus could also prompt future inflation, which would mean higher yields eventually too.

Speculative investors seemed positioned for a Democratic win ahead of the US election

Some of these positions could work in favour of investors independent of who wins, but some of them may have to be unwound if there is a surprise. This could generate some short-term volatility.

In that case, the assets which have the most stretched positions are the ones likely to move the most. Aside from the ones indicated above, investors also had large speculative positions in interest rate swaps and Libor, suggesting they expect the largest percentage moves to happen in the rates space.

One thing is for sure: today investors will start to know how to position for the future. In the next few days, however, they will just be adjusting their existing positions.

Investment Strategy Update

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