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Reflections

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Better growth outlook with Biden, but election still uncertain

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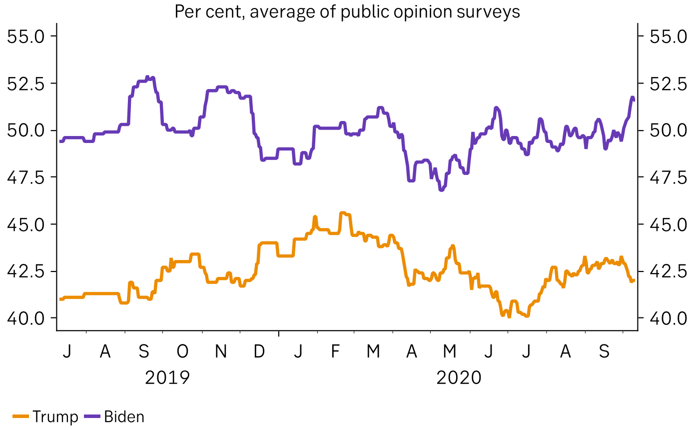
Improved prospects for Democratic candidate Joe Biden to win the presidency and majorities in both the House of Representatives and Senate are increasing the probability of expansionary fiscal policy in the United States after the November election. Assuming a continued loose monetary policy by the US Federal Reserve, this may boost economic growth substantially over the next few years. Yet the election outcome is still uncertain, both in terms of the winners and when the results will be declared final.

Biden is still ahead of Trump

The chaotic first election debate and President Donald Trump's coronavirus infection have strengthened Joe Biden's chances ahead of the US presidential election, in a situation where Trump remains behind in voter surveys. Deadlocked talks between Democrats and Republicans on a new federal stimulus package and signs that the recovery has lost momentum are meanwhile calling attention to the differences in the election platforms of the two main presidential candidates regarding fiscal policy.

Biden has widened his lead ahead of the presidential election

Per cent, average of public opinion surveys



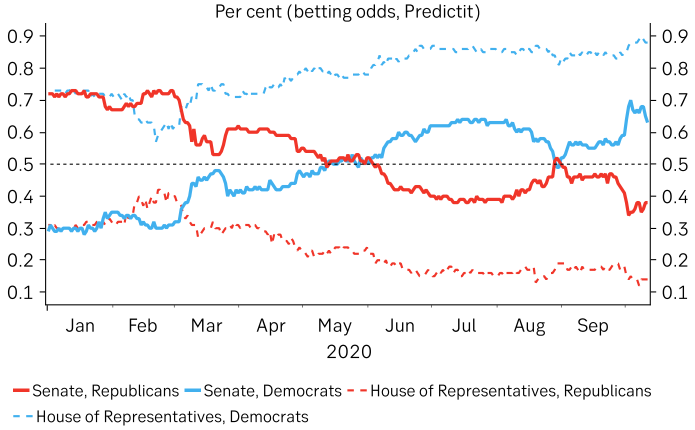
Source: RealClearPolitics (RCP), Macrobond, SEB

We still see Joe Biden as the most likely winner. Due to recent events – plus his continued stable lead in the opinion polls – we are raising the probability of a Biden victory from 60 to 70 per cent. If Biden captures the presidency, this also increases the likelihood that the Democrats will gain control of both the House and the Senate, thereby enabling him to enact at least his budget policies.

The September 29 election debate made few television viewers happy. Biden had the most to lose but came out no worse than Trump – rather the contrary. Because Trump then contracted COVID-19, along with a large number of his closest colleagues, the virus has again become the focus of attention. It is an issue on which the public has a low level of trust in the president.

Odds-makers signal Democratic victory in Congress

Per cent (betting odds, Predictit)



Source: PredictIt, Macrobond, SEB

Do we dare rely on opinion polls this time around?

If we believe most public opinion surveys, Biden may be cruising towards a landslide victory. Odds-makers also see a rising probability that Biden will help bring about Democratic majorities in both the House of Representatives and the Senate, thereby ensuring a greater chance of pushing through his policies. Biden continues to maintain a clear margin over Trump in national surveys and also leads the president in all but one of the 12 most important "swing states". But experience from 2016 calls for caution. Biden's margins in these key states are narrower than at a national level. Hillary Clinton enjoyed similar leads in a number of swing states which then unexpectedly – in some cases by tiny margins – shifted in favour of Trump. Yet a number of factors strengthen Biden's position compared to Clinton in 2016. Biden does not run as big a risk of losing votes to a third-party candidate, as Clinton did to Green Party candidate Jill Stein in states like Michigan, Wisconsin and Pennsylvania, which might have given

Clinton an Electoral College victory (but whether these voters were actually prepared to support Clinton instead of Stein is unclear). Opinion polling institutions should have learned something from their failure to identify many Trump voters in 2016. Unlike both Clinton and Trump, Biden has also avoided scandals so far.

Meanwhile there are new sources of uncertainty. The high percentage of postal votes in this pandemic year – especially among Democrats (more than 50 per cent according to the latest surveys) – will mean that election results may both be delayed and questioned by both parties. Trump continues to argue that mail-in ballots are fraudulent. Democrats risk losing votes because mail-in ballots are more often ruled invalid (1 per cent in 2016) and will push for recounts if they suspect "unfair" vote counts and Republican attempts to prevent voting among important Democratic-leaning groups such as African-Americans. We thus still foresee a relatively low probability that the election will be decided on the evening of November 3. But if Biden's clear lead persists, the outcome may nevertheless be finalised within a week or two, thereby avoiding a lengthy period of uncertainty and escalating disputes.

Front-loaded fiscal stimulus under Biden

Because the probability of a decisive Biden victory has increased, investors need to take a closer look at the platforms of the two candidates. We actually know rather little about what Trump wants, since he is campaigning on his 2016 platform and has only published a brief description of his plans for his next four years in office. China, protectionism, trade and immigration appear likely to remain in focus. Plans for additional tax cuts are vague. Looking at Biden, a combination of large-scale green infrastructure spending, increased social spending and tax hikes on businesses and high income earners points to clearly expansionary, front-loaded fiscal stimulus. Democratic proposals for another COVID-19 relief package are also larger than those presented by the Republicans. The Democratic-controlled House of Representatives recently approved a new USD 2.2 trillion package (over 10 per cent of GDP), which died as predicted in the Republican-controlled Senate. The Republican counterproposal, which was rejected by the House, totalled USD 300 billion – down from USD 1 trillion during the summer. Overall, this indicates that economic growth forecasts for the next few years can be revised upward under a President Biden, especially if the Democrats control both houses of Congress. If Trump wins, he will probably be forced to negotiate with a Democratic-controlled House. The risk of policy deadlocks will then remain, for example given the differences in how the two parties view federal grants to state and local governments – an important issue for Democrats.

Green infrastructure plan more in tune with the times

An expansionary fiscal policy, including higher public investments, is more effective in a recession when the central bank cannot be expected to respond with key interest rate changes. This is the message that the International Monetary Fund (IMF) is now sending to advanced economies in particular. US Federal Reserve Chairman Jerome Powell has also clearly stated that fiscal and monetary policy makers should work together to support the recovery. We interpret this as a signal that the Fed is prepared to counter upward pressure on Treasury yields – due to more expansionary fiscal policies – by expanding its own bond purchases.

The recovery is slowing after initial strength

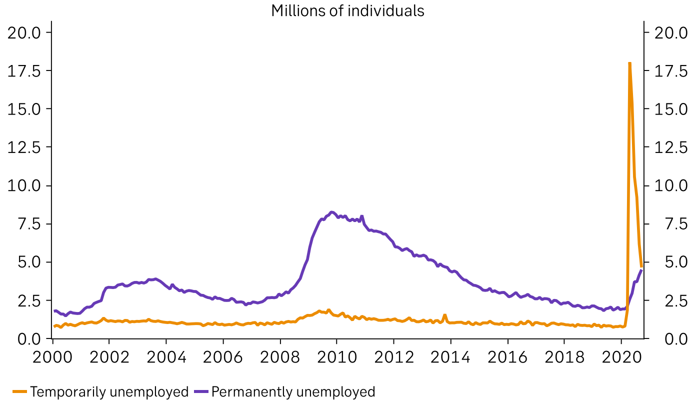
The need for more fiscal stimulus is underscored by signs that the US economic recovery is starting to lose momentum. The initial upturn when the economy reopened after last spring's COVID-19 lockdowns occurred faster than expected. Consensus forecasts now point to a GDP increase of more than 5 per cent (25 per cent annualised, according to American practice) during the third quarter of 2020. Even if there is zero growth during Q4, this would point to a GDP decline of only 4.5 per cent this year compared to 2019, instead of the 5.5 per cent decline we foresaw in our September forecast. The main underlying reason why GDP will not fall as much as previously thought is last spring's historically large federal subsidies to individual incomes, which enabled households to continue consuming even in a situation of steeply rising unemployment.

The plan was for last spring's temporary relief measures to be followed by a new stimulus package during the second half. The prospects of such a package now look poor, although President Trump has continued to send contradictory signals about the continuing negotiations. If stimulus measures are delayed, this will increase the risk of a decelerating recovery in a situation of persistently high unemployment (7.9 per cent in September).

The downturn in unemployment since last spring, when it peaked at nearly 15 per cent, has occurred more rapidly than expected. It has been driven by people who were temporarily prevented from working due to the pandemic and who have now returned to their jobs. But room for further reductions of this kind is probably approaching its limit, since some portions of the labour market – especially service sector jobs in tourism, entertainment and related fields – probably cannot bounce back until the coronavirus is under control. Meanwhile permanent job losses are starting to climb, probably reflecting shutdowns and bankruptcies in the hardest-hit sectors. Another factor is that companies are now beginning to adapt their business models to their new, less favourable outlook in the post-pandemic economy. The prospect of an expansionary Biden agenda after the election may help boost optimism even today, by lowering the risk of continued cutbacks. A Trump victory would increase uncertainty about federal policies going forward.

Temporary job losses are being replaced by permanent ones

Millions of individuals



Source: U.S. Bureau of Labor Statistics (BLS), Macrobond, SEB