Insights, Tacit Thought | Weekly Investment Insights

A result rather than uncertainty

Published on: 8 November, 2024 | Author: Investment Team

The US elections were the last major election of 2024 and therefore we are now moving into a period of less political uncertainty and less political risk for investment markets to deal with.

The immediate market reaction was pretty much as expected: US$ up, US bond yields up, US equities up, Asian equities (China mainly) down. Interestingly, European equities have not risen in line with the US which further strengthens our view that selective exposure to equities globally is vital in the current economic cycle. Since the initial reaction, Asian equities have rebounded strongly, the US$ has fallen back, with the US equity market remaining higher. A knee jerk reaction was expected but the volatility will fade.

Overall, the next few years for the US can summarised as a pro-growth environment with concerns about US government debt levels leading to prospects of volatility. For the rest of the world however, we fear this higher economic growth outlook for the US will be at the expense of others. Other G7 economies, with high government debts and aging populations, are unlikely to increase GDP per capita in such an environment.

When investing, government bond yields matter more than most other factors as they provide the risk-free rate to which other returns are compared. This is why controlling inflation is at the core of most central bank economic models. For UK investors, a comparison between the UK risk free rate and the US risk free rate provides context which we must not forget or ignore. The 30-year US bond yields 4.6% today, down 0.2% over the year. The equivalent UK 30-year bond currently yields 5%, up 0.25% over the past year. We ask the question: is the UK yield higher because of its better growth prospects?

Ignoring the short-term noise, we look at the US election result through the lens of our six longer term investment themes which provide the guardrails for our positioning in strategies.

1. Low growth coupled with increased conflicts
2. Ongoing climate transition
3. Developed Asian Economies being ranked equally for capital allocation to their Western peers
4. Impact of Artificial Intelligence on societies and tax rates
5. A resurgence of currency trading blocks
6. High national debt levels leading to an erosion of fiat currencies as stores of value

Of the above, we do not currently see any material changes to our investment thesis: climate transition will be slowed, whilst others, such as the resurgence of currency trading blocks will be accelerated. Ultimately, we remain in a world where US growth outstrips other G7 countries and a pull away from globalisation at the margins.

US economic strength has been a theme in the global economy for the past decade, however the election of President Trump for a second term will, if anything, result in higher US economic growth in the short term but also higher price pressures. How these price pressures play out will depend on how supply chains alter. There is no economically right or wrong way to manage an economy other than to keep an eye on inflationary pressures, a phenomenon which the UK has had to contend with over the past few years.

The issue with government deficits and borrowing is important to monitor. However, the US is uniquely positioned due to the international dominance of its currency and its relatively low tax take which gives the federal government scope to underpin solvency should bond markets begin to request a higher risk premium of the US government. The initial reaction has been relatively muted but nevertheless needs to be monitored carefully over the coming months and years.

The US elections were the last major election of 2024 and therefore we are now moving into a period of less political uncertainty and therefore less political risk for investment markets to deal with.

The immediate market reaction was pretty much as expected: US$ up, US bond yields up, US equities up, Asian equities (China mainly) down. Interestingly European equities have not risen in line with the US which further strengthens our view that selective exposure to equities globally is vital in the current economic cycle. Since the initial reaction, Asian equities have rebounded strongly, the US$ has fallen back, with the US equity market remaining higher. A knee jerk reaction was expected but the volatility will fade.

Overall, the next few years for the US can summarised as a pro-growth environment with concerns about US government debt levels leading to prospects of volatility. For the rest of the world however, we fear this higher economic growth outlook for the US will be at the expense of others. Other G7 economies, with high government debts and aging populations, are unlikely to increase GDP per capita in such an environment.

When investing, government bond yields matter more than most other factors as they provide the risk-free rate to which other returns are compared. This is why controlling inflation is at the core of most central bank economic models. For UK investors, a comparison between the UK risk free rate and the US risk free rate provides context which we must not forget or ignore. The 30-year US bond yields is 4.6% today, down 0.2% over the year. The equivalent UK 30-year bond currently yields 5%, up 0.25% over the past year. We ask the question: is the UK yield higher because of its better growth prospects?

Ignoring the short-term noise, we look at the US election result through the lens of our six longer term investment themes which provide the guardrails for our positioning in strategies.

1. Low growth coupled with increased conflicts
2. Ongoing climate transition
3. Developed Asian Economies being ranked equally for capital allocation to their Western peers
4. Impact of Artificial Intelligence on societies and tax rates
5. A resurgence of currency trading blocks
6. High national debt levels leading to an erosion of fiat currencies as stores of value

Of the above, we do not currently see any material changes to our investment thesis, climate transition, will be slowed, whilst others, such as the resurgence of currency trading blocks will be accelerated. Ultimately, we remain in a world where US growth outstrips other G7 countries and a pull away from globalisation at the margins.

US economic strength has been a theme in the global economy for the past decade however the election of President Trump for a second term will, if anything, result in higher US economic growth in the short term but also higher price pressures. How these price pressures play out will depend on how supply chains alter. There is no economically right or wrong way to manage an economy other than to keep an eye on inflationary pressures, a phenomenon which the UK has had to contend with over the past few years.

The issue with government deficits and borrowing is important to monitor. However, the US is uniquely positioned due to the international dominance of its currency and its relatively low tax take which gives the federal government scope to underpin solvency should bond markets begin to request a higher risk premium of the US government. The initial reaction has been relatively muted but nevertheless needs to be monitored carefully over the coming months and years.

Important Information: Any views, insights, or commentary are for general information only, do not constitute personal investment advice or research, and are intended for UK residents. They may not be appropriate in all jurisdictions. While sourced from information we believe to be reliable, we make no guarantee as to accuracy or completeness. Past performance is not a guide to future results, and the value of investments can go down as well as up.

Regulatory Disclaimer: Tacit Investment Management is the trading name of TIML Limited (No. 9228395), part of Tacit Holdings Limited (No. 10611211). Both companies are incorporated in England and Wales, with the registered office at 14 Hanover Square, London W1S 1HN. TIML Limited is authorised and regulated by the Financial Conduct Authority (FCA ref. 670184) and approves and issues this communication under Section 21 of the Financial Services and Markets Act 2000. Please note, tax and estate planning services are not regulated by the FCA.