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A European view on the US elections

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There has never been such a wide gulf between Republicans and Democrats, and the looming presidential election is very likely to further accentuate the country's divisions. According to a survey conducted at the beginning of August by the Pew Research Center[1], more than eight out of ten voters today believe that it is "really important" to know who will win it, the highest figure for 20 years (in 2000, it was 50%). The fact that the main reason for supporting Joe Biden is opposition to Donald Trump also speaks volumes. This increased polarisation of the electorate, the rise of what political scientist Amy Chua calls "tribalism", threatens the very unity of the Nation.

Where is Donald Trump's United States in all this?

During his 2016 election campaign, Donald Trump promised to revitalise growth, assuring that GDP could rise by at least 3% a year... "and even much faster"! The superlatives used at the end of 2019 to describe the state of the economy were pretty emphatic: "tremendous", "booming", "terrific", "the greatest it's been in HISTORY". Solid growth, falling unemployment... was Donald Trump's economic record sheet before the Coronavirus crisis really exceptional? To what extent did his economic policy contribute to it?

2017-19: a slow return to full employment

Uninterrupted since the end of the Great Recession (2007-2009), growth continued over the first three years of Donald Trump's mandate, making it the longest post-war cycle. However, the unusual length of this expansion phase cannot mask its lack of strength: after having briefly exceeded 3% in 2018, thanks to massive tax cuts and, above all, higher public spending, growth returned to around 2% at the end of 2019, a level more in line with the economy's growth potential.

Far from the "3% or more" announced, this growth nevertheless enabled the labour market to continue its recovery. As a result, continuous job creation ended up reducing the unemployment rate to 3.5% in December 2019, a level last seen at the end of the 1960s. Better, this sustained pace of job creation encouraged the return to the labour market of a part of the population who had withdrawn from it, as evidenced by the increase in the participation rate of people aged 25-54, and, more generally, the decline

[1] Pew Research Center (2020), "Election 2020: Voters Are Highly Engaged, but Nearly Half Expect To Have Difficulties Voting", August 13.

in underemployment indicators. At the end of 2019, the "U6" rate, which gives the broadest measure, even fell below its pre-Great Recession levels, returning to those seen in the early 2000s.

This slow improvement on the labour market has led to a general upturn in wage increases. The highest have certainly increased more quickly than the average. But the situation has also clearly improved at the bottom of the income scale. In a stretched labour market, wage demands, notably brought by unions and workers in the fast food and mass-market retail sectors, have found fertile ground. In the absence of an increase in the federal minimum wage (to $7.25 per hour, this minimum has not been reviewed since 2009), around twenty states have introduced regular rises since 2017. By encouraging the return to employment of an increasingly large portion of the population and creating the conditions for a sustained acceleration in wages, the expansion of activity, which has continued for ten years, has helped to improve the situation of the least well-off: the poverty rate has continued its decline, reaching 10.5% in 2019, its lowest level since the early 2000s.

However, this general improvement in US household income should be put in perspective. First, it took thirteen years for the income (before taxes and transfers) of households at the bottom of the scale (the lowest-earning 20%) to return to their 2006 levels. Secondly, the labour market was far from as stretched as it seemed: the participation rate of men forming the core of the working population (those aged 25-54) was still struggling to rise at the beginning of 2020[2]. Finally, unlike the policies pursued by Barack Obama, Donald Trump's policies have contributed to increasing already glaring inequalities.

The "great" tax reform or the illusions of the supply economy

Donald Trump's economic policy was based on two pillars: a "great" tax reform – which was to boost business investment – and a trade war – supposed to bring back industrial jobs and rebalance the US trade deficit.

More surreptitiously, but with a certain efficiency, the Trump Administration also undertook, in the name of freedom, a quasi-systematic deregulation in the areas of energy and ecology, as well as in the social and financial arenas. As for the promise of a large infrastructure investment plan, which was placed prominently in his election programme, it was quickly forgotten.

The first pillar of Donald Trump's policy, the 2017 Tax Cuts and Jobs Act (TCJA) was implemented quickly: it took just fifty days, while in 1986, it

[2] The weak participation rate among men is explained at least in part by the mass disappearance of manufacturing jobs, mainly held by men, but also by the opioid crisis: one fifth of men aged 25-54 who remained outside the working population experienced difficulties walking or climbing stairs in the mid-2010s, and half took analgesics every day [Krueger, 2017].

took long months of negotiations for Ronald Reagan's Tax Reform Act (TRA) to see the light of day. The logic behind the reform sought by President Trump was also very different: in 1986, to reduce household taxation without excessively damaging the budget balance, tax loopholes on companies were removed. This time, the first step was to reduce corporate tax; the reduction in the household tax burden, generally temporary (most measures are due to expire in 2025), was largely minimal except for... the most wealthy. The top 20% in terms of income distribution thus benefited from two-thirds of the tax cuts. Tax cuts

> *This time, the first step was to reduce corporate tax; the reduction in the household tax burden, generally temporary (most measures must expire in 2025), was largely minimal except for... the most wealthy.*

amounted to more than $51,000 on average in 2018 for the 1% of households at the top of the scale... compared with an average reduction of approximately $40 for those whose income was less than $25,000 a year. Compared with their incomes, the gains were also significantly higher for the richest: those earning more than $500,000 a year saw their after-tax incomes increase from 3.5% to 4%, while those earning less than $20,000 saw theirs increase by...0.2%. Hopes that such a policy would significantly boost household demand were therefore in vain.

The main component of the tax reform was, however, something else: the reduction in the corporate tax rate from 35% to 21% and an accelerated depreciation system were expected to stimulate business investment, increase productivity and enable the economy to sustainably return to growth of more than 3%. Again, reality diverged considerably from expectations. The pace of growth increased little, and its (very temporary) acceleration was largely due to the increase in public spending decided in early 2018 by Congress. The response of productive investment to these tax incentives was largely disappointing. While in 2018 the effective corporate tax rate was reduced by half (from 17.2% in 2017 to 8.8% in 2018) and companies repatriated nearly $800 billion in foreign income (more than in the five previous years), their investment barely increased. Employees also benefited little from the decline in the corporate tax rate. Admittedly, according to a survey, a small portion ($4.4 billion) of the tax cuts seem to have been paid to them in the form of bonuses in 2018. However, divided by the number of jobs, this represents less than $30 per worker… In the absence of investment in the real economy, companies have, as expected [Brender and Pisani, 2018], used most of the tax cuts and repatriated profits to buy back their shares (up to $800 billion in 2018 for S&P 500 companies versus $520 billion in 2017) or pay dividends. Finally, unlike what was promised, the reform has been far from self-financing: it hugely contributed to the increase in the public deficit between 2016 and 2019, from $585 billion… to nearly $1,000 billion.

A trade war neither “good” nor “easy to win”

Alongside tax reform, the re-industrialisation of the US was Donald Trump’s other major campaign promise.

To achieve this, the President announced that he would take the US out of the Trans-Pacific Partnership Agreement (TPP), would renegotiate NAFTA (North American Free Trade Agreement) and, if necessary, increase customs duties. Promises kept: the Trump Administration withdrew from the TPP, renegotiated with Mexico and Canada “the largest trade deal in history” – called the United States–Mexico-Canada Agreement (USMCA) – and started a tariff war, with China in particular.

However, the expected effects both in terms of rebalancing the trade balance and industrial job creation were rather far from those initially promised. Half a million jobs were admittedly created in the manufacturing sector, but the share of manufacturing employment in total non-farm employment, after rising slightly in 2018, fell again from spring 2019, falling to its lowest level (8.1%), the same as at the start of Donald Trump’s mandate. Above all, despite an expansionary fiscal policy, the trade war has significantly curtailed US investment and exports. The rise in uncertainty alone is thought to have shaved 0.8 of a percentage point of GDP off growth in the first half of 2019 [Caldera *et al.*, 2019[3]]. Of course, the trade war is not solely responsible for the slowdown in US activity: domestic problems in China and other emerging countries have also contributed. It will however leave deep scars. This war has highlighted a number of latent concerns in the US, particularly the fear of dependence on China in areas of strategic importance or related to national security. For this reason, it will have a lasting effect on international relations, and the truce concluded at the beginning of January 2020 will change nothing.

Climate scepticism driving deregulation

One final component of Donald Trump's economic policy has gone almost unnoticed: alongside the tax reform and the trade war, an executive order signed in the first week of his coming to power (no. 13771) required federal agencies to remove two regulatory measures for every new measure adopted ("One In, Two Out").

In four years, the "reduction in regulation" has been spectacular: cancellation of the obligation for oil and gas companies to report methane emissions; elimination of California's right to establish its own, more demanding, emissions standards for light vehicles; replacement of the Clean Power Plan implemented under Barack Obama, which set strict limits on carbon emissions from coal and gas power plants, with a new version that leaves it to individual states to set their own rules; repeal of a Executive Order that set a target for reducing federal government greenhouse gas emissions by 40% in ten years. In total, nearly

[3] Caldara D., Lacoviello M., Molligo P., Prestipino A. and Raffo A., 2019, "Does Trade Policy Uncertainty Affect Global Economic Activity?", *FEDS Notes.*

70 environmental protection rules have been removed and about 30 are in the process of being removed[4].

The environment was not the only sector affected by deregulation[5]. Having failed to successfully repeal Obamacare[6], which had reduced the number of people without health insurance from 46.5 million in 2010 to 26.7 million in 2016, the Trump Administration returned to an essential aspect of the reform – the compulsory nature of insurance – by cancelling the penalty to be paid for not having insurance. It also allowed states to ask beneficiaries to provide evidence that they are in employment – which is sometimes difficult even for those who are working[7]. Between 2016 and 2018, the number of people without health insurance increased by more than 1 million. The conditions for accessing food assistance (the Supplemental Nutrition Assistance Program) were also being toughened. Until now, in regions where unemployment was higher than the national average, states could decide to provide aid to unemployed people. The Administration wanted to take this freedom away from them. If this toughening of regulation had been applied in 2018, 3.7 million people would have lost access to the SNAP [Wheaton, 2019]. Under fire from critics, the Trump Administration decided in spring 2020 that it would wait for the end of the national emergency to tighten access rules.

> *Between 2016 and 2018, the number of people without health insurance increased by more than 1 million.*

[4] https://www.nytimes.com/interactive/2020/climate/trump-environment-rollbacks.html

[5] The telecommunications sector was also subject to deregulation. For example, the Federal Communications Commission (FCC) has reduced the Net neutrality rules adopted under the Obama administration – particularly those relating to high-speed confidentiality – and has removed newly granted broadband subsidies for the poorest under the federal Lifeline program. A recent exception to this deregulation of the sector is the executive order aimed at "limiting the legal protection of social media platforms if they do not comply with the principle of neutrality". The targets were Twitter and Facebook, which had described certain statements made by Donald Trump as "misleading or false".

[6] Despite a Congress controlled by Republicans, President Trump was unable to repeal Obamacare owing to divisions within the Grand Old Party.

[7] Some people may be forced to provide proof each month that they are in employment, and confirmation from their employer could sometimes be required.

Wasted ammunition

While US growth was steady over the first three years of Donald Trump's mandate, keeping unemployment figures down, the margins for economic policy were however significantly reduced in these years.

Monetary policy in particular was forced to adjust to the climate of uncertainty created by the President: after raising rates until the end of 2018 to slow down an economy threatened by overheating owing to the tax reform, the Federal Reserve, in light of the uncertainty caused by the trade war, was forced to bring them down again to "insure" against an excessive slowdown in activity. The poisonous atmosphere created by the White House and the President's killer tweets against "J. Powell[8] and the Fed boneheads" did not make its task any easier. By gradually tightening monetary policy throughout 2019, the Federal Reserve was able to give the impression of giving in to political pressure. Nonetheless, it was right to be cautious, having learned from past experiences.

Ammunition was also wasted on the budget front. The 2017 tax reform and the spending increases decided in 2018 and 2019 significantly increased the federal government deficit: the Congressional Budget Office estimated that the TCJA alone would increase public debt by more than $2,000 billion by 2028 (assuming that household income tax cuts expire, as expected, in 2025). The US government thus faced the Coronavirus shock with a greater financial liability than it should have had.

[8] Jerome Powell has been the Chairman of the Federal Reserve since 2018.

The limits of favouring liberalism faced with Covid-19

While Donald Trump has long prevaricated on the attitude to be adopted to the Coranavirus pandemic, the Federal Reserve quickly understood that it had to act immediately.

As early as mid-March, it not only reduced its key rate to zero, but also launched a treasury securities purchase programme, initially set at $700 billion, then quickly raised to an "unlimited" amount. It also urgently opened several windows of intervention: every time a segment of the credit market looked like becoming clogged up, it sought to ease tensions by providing liquidity, even agreeing to relieve financial players from the risks they could no longer bear, acting as buyer of last resort. Some pointed to a hidden bank bailout. This analysis is incorrect: the origin of this crisis does not lie in the imprudence of the financial system, but in the real economy. If sectors representing two-fifths of an economy remain inactive for several weeks, or even several months, this can only result in an abrupt slowdown. Without support measures, many companies will be forced to close down, and the contraction in activity will accelerate, with the recession turning into a depression. In addition, the deterioration in the labour market will cause the most vulnerable to lose their health insurance.

Congress also understood the urgency of the situation: while Democrats and Republicans have been unable to reach agreement since the mid-terms, a bipartisan agreement was reached in record time, and a budget of more than $2,000 billion (then raised to $2,700 billion) was passed. This sum is impressive compared to that mobilised in Europe. But the social net is much less generous in the US, and requires the adoption of additional measures in response to depressive shocks[9]. As in most other developed countries, the US plan also aims to ensure companies continue to have access to credit. It also includes incentives to preserve employment or at least enable employees to continue to benefit from health insurance. Finally, this plan seeks to compensate households for the income they could lose. Each adult thus received $1,200 (plus $500 per child). Unemployment benefits became more generous: the law provided for 13 weeks of additional benefits and the extension of rights to workers who were formerly ineligible. Laid-off employees also received $600 per week in addition to the "normal" allowance (on average, $372 per week). If we add the compensation paid by the states, they received an average of $900 to $1,300 per week, more than the median weekly pay of full-time workers ($933 at end-2019).

[9] See Jérémie Cohen-Setton and Jean Pisani-Ferry (2020), "When More Delivers Less: Comparing the US and French COVID-19 Crisis Responses", https://www.piie.com/system/files/documents/pb20-9.pdf.

This aid is, however, temporary. Emergency unemployment benefits of $600 per week ended in July. Now, with the elections approaching, partisan divisions have re-emerged. Mid-September, no agreement had been reached in Congress on the extension of the exceptional boost of $600 per week[10] or on support to be given to states and local authorities whose budgets have been undermined

> *And while knowing who the next President will be is important, knowing if he will have a sufficient majority in Congress to implement his programme is equally crucial.*

by the crisis. While the four Executive Orders issued by Donald Trump should save time, they will not be enough to get the economy going again. Against this backdrop, the candidates' economic programmes are of greater importance than usual. And while knowing who the next President will be is important, knowing if he will have a sufficient majority in Congress to implement his programme is equally crucial.

[10] Donald Trump has just issued an executive order enabling $400 per week of additional unemployment benefits to be paid (versus $600 in the CARES Act): the federal government will pay $300, and the states that are able to the remaining $100. The federal share will come from the Department of Homeland Security's Disaster Relief Fund (DRF), which currently has $70 billion. These allowances will stop being paid when the DRF has only $25 billion or no later than 6 December 2020. The payment of an allowance of $300 would cost about $50 billion per month: the DRF's resources could therefore be exhausted by the end of August!

The economic issues in the election

As is often the case, the economy plays an important role in the campaign. Almost eight out of ten voters today say that economic issues will be essential in their choice (followed by the healthcare system, appointments to the Supreme Court, the Covid-19 epidemic; inequality and climate change are right at the back of the queue!). This proportion is, we should note, quite close to that observed in the previous elections, that of 2016 in particular. But it is less the state of the American economy that will be decisive in the outcome of the election[11] than the candidates' ability to carry a political project that responds in particular to an increasingly large proportion of the population's "fear of losing status". While they both aim to revitalise activity and increase the deficit – one by increasing spending, the other by reducing receipts – these programmes reflect the very different direction in which each candidate wishes to take the US over the next decade. Donald Trump presents himself as an alternative to the elites that are said to be increasingly remote from the people and unable to protect them against the forces of globalisation. Joe Biden wants to oppose his "laissez-faire" approach and combat the inequalities of all kinds created by capitalism that has been left too long to its own devices.

The Democrat Programme: a "social democrat" programme

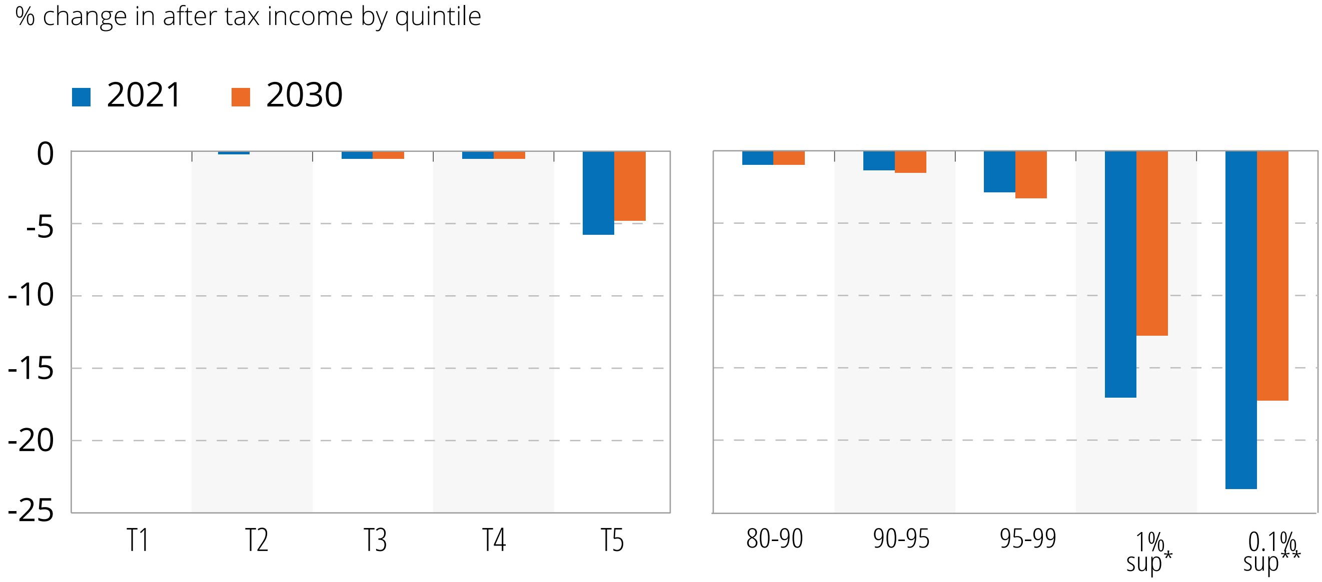
Joe Biden's programme is part of the social democrat tradition. It proposes to finance infrastructure, education and health expenditure through tax increases on household incomes[12] and corporate earnings, and to put in place a short-time work system inspired by the German model.

The increase in income tax on households largely relates to the 5% most affluent, and among them mainly the 1% at the top of the scale (Chart 1). At the same time, a gradual increase to $15 in the minimum hourly wage would boost the purchasing power of less well-paid workers.

[11] In 2016, Hillary Clinton lost against Donald Trump with a continually declining unemployment rate, which even fell below 5% at the end of Barack Obama's second term.

[12] In addition to increasing household income tax rates, the Democrat Programme sets out an increase in the tax rate on capital gains on the sale of securities for households earning more than $1 million.

Chart 1: Income taxes

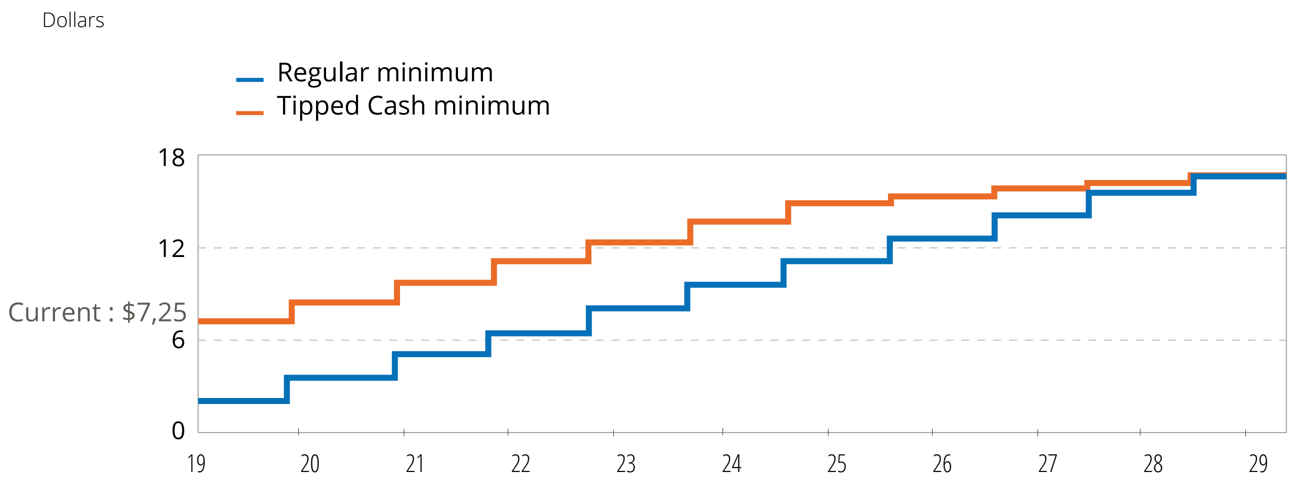


* Top 1%: income > $837,000
** Top 0.1% > $3.7mn

Source: CRFB

In the coming weeks, these proposals could be supplemented by that of Biden's running mate, Kamala Harris, who wants to restore the middle class's purchasing power (see Box 1).

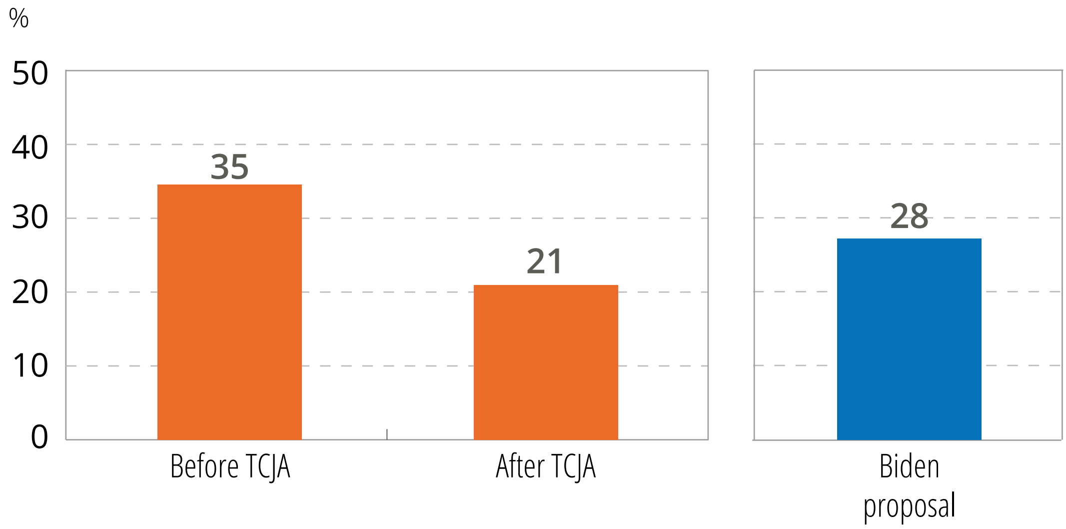
Chart 2: Minimum hourly wages



Source: Candriam

The Democrat candidate also proposes a significant increase in infrastructure spending ($2,000 billion over four years), incorporating in his programme some of the aspirations set out in Bernie Sanders' Green New Deal. During his mandate, he thus proposes to renovate millions of buildings and to achieve carbon neutrality in power generation by 2035, to invest $100 billion in the modernisation of schools and $50 billion in the repair of roads and bridges... The aim is to modernise the ageing infrastructure that has been cause for concern to the American Society of Civil Engineers for many years now. This spending would provide strong support to growth: the Congressional Budget Office, a non-partisan organisation, estimated in 2015 that, for every dollar spent on infrastructure, the economic benefit could be up to $2.20[13].

Chart 3: Federal corporate tax rate



Source: Candriam

Joe Biden also proposes to support the US manufacturing sector: the federal government would commit $400 billion to the purchase of products manufactured in the US, and would invest $300 billion in research and development for electric cars, artificial intelligence, etc. Of course, his "Buy American" is a response to Donald Trump's "America First".

It is difficult to assess the total amount of expenditure and receipts of the Democrat candidate's programme, because promises have multiplied in the run-up to the election. The CRFB estimates that, over ten years, healthcare reform would increase spending by $2,250 billion (net cost to the budget: $1,800 billion) and its education programme (including universal preschool of

[13] CBO (2015), "Estimated Impact of the American Recovery and Reinvestment Act on Employment and Economic Output in 2014"

children aged 3-4) would cost $850 billion. In addition to these expenses, $2,000 billion must be added for the infrastructure plan and $300 billion for the Innovate in America programme. In total, the candidate's programme would increase spending by approximately $5,000 billion; this would only partially be funded by an increase in receipts of $3,500 billion[14].

A Biden-Harris Administration would also likely move towards greater regulation of the technology sector. This could include a competition policy and the application of less favourable antitrust rules to the sector, as well as a stricter privacy and cyber security policy.

Box 1: *LIFT (Livable Incomes for Families Today) the Middle Class Act*

In 2018, Kamala Harris, then Senator of California, proposed to restore purchasing power to the middle class through a tax credit of up to $3,000 for single people to $6,000 for couples. The proposed mechanism is based on the *EITC* (Earned Income Tax Credit).

The *EITC** is a federal government tax credit granted to low-income households (26 states and the District of Columbia add their own tax credit to that of the federal government). The amount of the tax credit depends on the marital status, number of children and income of the beneficiary: from the first dollar of income, it increases to a certain threshold and then decreases to zero when the income exceeds a given amount. When the amount of the tax credit is greater than the tax due, the difference is paid to the household. In 2017, the average tax credit for a family with children was just over $3,000 (but it was less than $300 for a family without children). The mechanism is intended to encourage low-income employees to work as full-time as possible. In 2018, it prevented 5.6 million people from living off incomes below the poverty threshold. A family of two children with only one full-time worker paid the minimum wage ($12,500 per year approximately in 2016), will indeed be above this threshold, but only if it actually benefits from the *EITC*... and the *SNAP* food assistance programme!

By allowing households earning up to $100,000 to benefit from a tax credit (compared to $55,000 for the *EITC*), Kamala Harris's proposal aims to increase the purchasing power of the middle classes. Its implementation would also support the lowest incomes by plugging one of the gaps of the *EITC*: single people without children could receive a tax credit of up to $3,000, compared to a maximum of $529 in 2019 with the *EITC*.

* On this point, see "The earned income tax credit", Policy Basics, Center on Budget and Policy Priorities, December 2019.

[14] According to the CRFB, President Biden's tax plan would raise between $3.35 trillion and $3.67 billion over a decade. In Understanding Joe Biden's 2020 Tax Plan. http://www.crfb.org/papers/understanding-joe-bidens-2020-tax-plan.

Donald Trump's programme: following on from 2016...

Donald Trump's economic programme is more vague, but it takes up the same themes as in 2016: "Make America Great Again" has been turned into "Keep America Great". The measures mentioned above suggest that his economic policy will continue to be a mix of trade mercantilism, regulatory liberalism and tax cuts.

The President has thus promised to maintain the 2017 tax cuts and to turn the deferral of the payment of employee social security contributions between August and December 2020 (passed by executive order) into a cancellation. Donald Trump is also in favour of increasing infrastructure spending – a promise already made in his 2016 programme – but the majority of Republicans are opposed to it. Having failed to achieve this during his first term, partly as a result of the public health crisis, Donald Trump seems to have put to one side the idea of repealing Obama's health reform (Affordable Care Act).

As a convinced climate-sceptic, Donald Trump will certainly continue his environmental policy. Finally, on the trade front, Trump is very likely to continue his "war" with China, of course, but also with Europe. The first objective of this war is to address the latent concerns of the electorate. It also responds to fears of increasing dependence on China in strategic or national security areas. On this front, it is not certain that the Democrats have a very different position, but a Democrat Administration would undoubtedly offer an opportunity to repair transatlantic relations by defusing trade tensions with Europe and encouraging the search for multilateral solutions. Its campaign team has already stressed that the Democrat candidate's approach complies with World Trade Organisation rules, although his Administration will seek to amend the agreement in place guaranteeing a mutual opening of public procurement markets.

Overall, Donald Trump's programme, liberal in terms of regulation and protectionist in trade matters, is the same as the one that secured his victory in 2016, when he played not only on the fear of losing status, but also on anger against globalisation, multiculturalism and immigration. However, with lower employment than in the depths of the recession in 2009, the public health crisis at the beginning of the year could only revive fears of losing status: the employment rate among men forming the core of the working population (those aged 25-54) in particular fell by more than ten points between February and April, and it was still seven points lower in July than at the beginning of the year.

A tighter race than it seems

Mid-September, Joe Biden was well ahead in the polls: 51% of voters say they are ready to vote for him, compared with 42% for Donald Trump. President Trump also seems to be losing ground in several of the key states that he won in 2016, such as Michigan.

To win the election, a candidate needs to obtain a majority in the electoral college[15], i.e. 270 votes out of 538. In most states, elections are already a done deal, such as in California, largely Democrat, or in Oklahoma, largely Republican. However, about 45% of the US population lives in states where the results are more uncertain, including just over 20% in swing states, which can change allegiance at the drop of a hat. Mid-September, Joe Biden seemed to have a comfortable majority with 268 votes in the electoral college versus 169 for Donald Trump[16], but we should remember that in 2016 these same polls put Hillary Clinton well ahead.

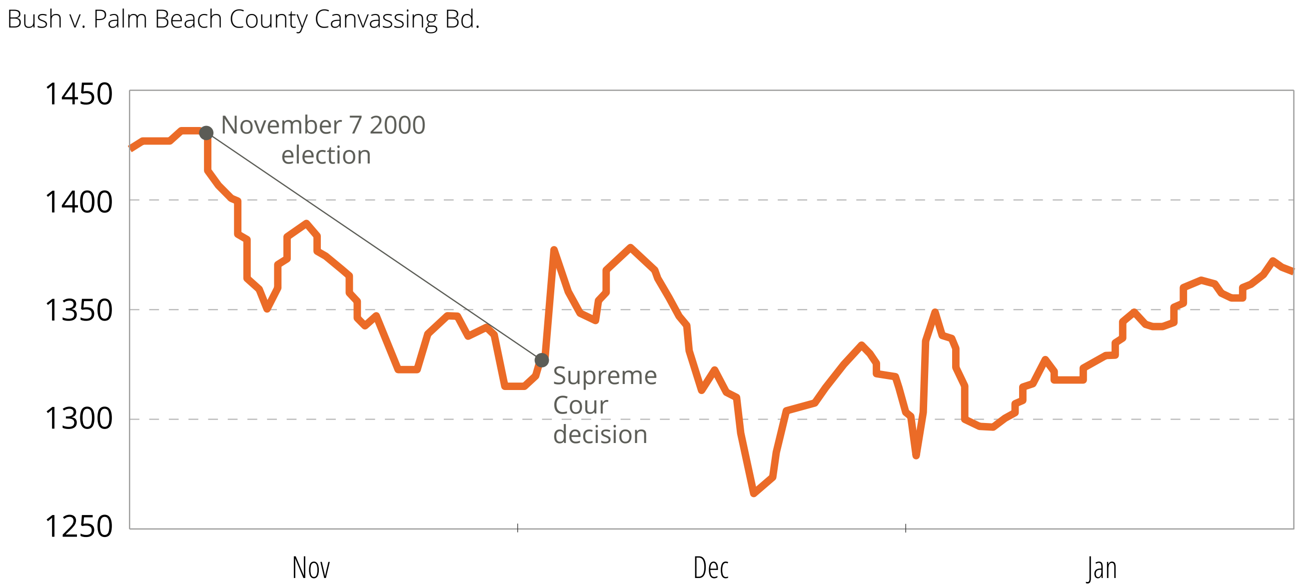
> *Despite the polls favourable to Joe Biden, the election is therefore far from a fait accompli.*

Despite the polls favourable to Joe Biden, the election is therefore far from a fait accompli. Donald Trump enjoys very strong support from his voters (two-thirds of his supporters say they support him "strongly", versus less than half of Biden's supporters). With more than 80 million followers on Twitter (compared to 6 million for his rival), the President also has a formidable communication tool in his arsenal, which he made considerable use of during the 2016 campaign

[15] The US presidential election is an indirect election; voters designate representatives who are then responsible for electing the President and Vice-President.
[16] On this point, see https://www.npr.org/2020/09/16/912004173/2020-electoral-map-ratings-landscape-tightens-some-but-biden-is-still-ahead.

("I have my own media. I don't have to go to the fake media"). The problem of mail-in voting – "the greatest fraud in history" according to Donald Trump! – could also play an important role in this election: at the beginning of August, half of voters – 60% among Democrats and 35% among Republicans – anticipated difficulties in voting in November [Pew Research, op. cit.], compared to only 15% in October 2018, just before the mid-term elections. Now, a sharp increase in mail-in voting could lead to a repetition of the November 2000 scenario, when we had to wait for weeks before knowing the result of the election: in the meantime, the stock exchange recorded significant falls (Chart 4).

Chart 4: The S&P 500 in November and December 2000



Sources: Refinitiv Datastream, Candriam

An even more chaotic sequence of events cannot be ruled out. In his day, Al Gore, after a few weeks, ended up conceding defeat. Some observers are concerned today that the 2020 election is more like that of... 1876, when Republican Rutherford Hayes took on Democrat Samuel Tilden. In three Southern states, then dominated by the Republicans, electoral commissions met and cited various dubious reasons to invalidate the results in several electoral districts. After a challenge by the Democrats, a commission was created in the House of Representatives. But it took long weeks of heated debate for a compromise – not a glorious one![17] – to be found: Rutherford Hayes was finally elected President on 4 March 1877 with 185 votes (compared to 184 for his opponent[18])... and barely 48% of the electoral body.

[17] The Democrats conceded the Presidency. In return, they obtained "the drawdown of federal troops in the Southern states, the end of Reconstruction – the reforms that followed the Civil War – and the consignment of Black citizens to a century of violent repression", in E. Lach (2020), "What happens if Donald Trump fights the election results", The New Yorker.
[18] See A. Coutant (2012), "Minority Presidents in the United States", *French Journal of Constitutional Law*, no. 90.

How to build a portfolio?

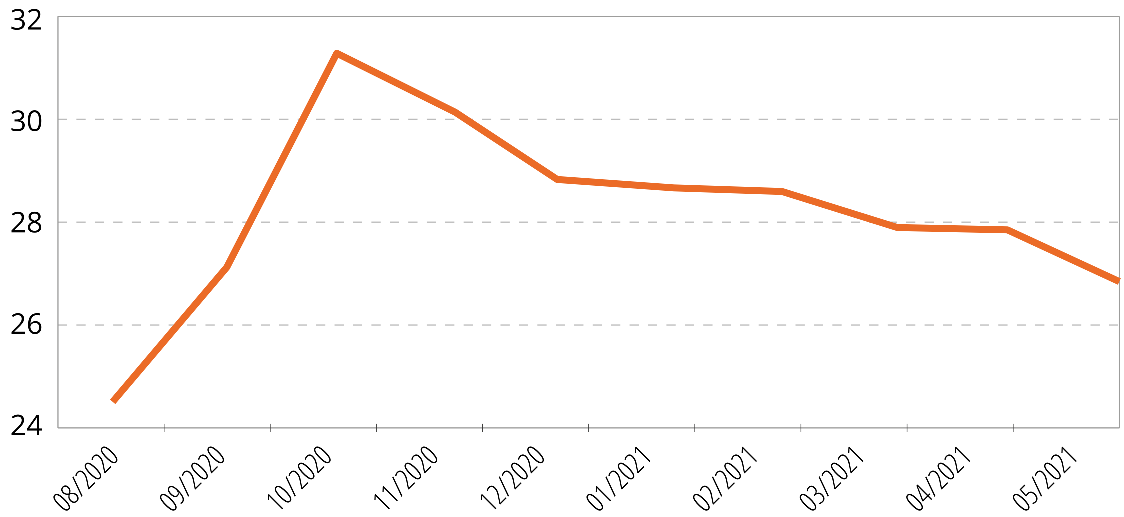
A high level of uncertainty that could continue

The US election is another source of uncertainty for the markets that will influence performance between now and the end of the year. Managing the public health crisis caused by Covid-19 remains the number one driver of the global economy and trends on the financial markets. Nevertheless, the US election remains the second most important factor, given the possible domestic and international implications, depending on the name of the President and the composition of Congress.

The extreme polarisation seen in this election makes market expectations particularly sensitive, especially against the backdrop of a health crisis. The first issue is the date on which we will know the name of the new US president. In the event of a close result between the two candidates, it will probably be disputed.

Markets are likely to respond to this uncertainty with an increase in volatility. This has already been partially factored in by investors until the election date at least, as shown by the trend of futures on the VIX (forward-looking volatility on the S&P 500 at different maturities).

Chart 5: Futures curve on expected volatility on the S&P 500 (VIX)



Source: Candriam

How should you protect yourself?

- We have chosen to maintain optional protections on US and European equities in order to reduce the impact on our performance of increased volatility over the coming weeks. For the time being, by incorporating these protections, we are therefore slightly underweight on equities.
- We have increased our exposure to gold, which provides effective protection in this environment.
- Risks on US assets are accumulating, and may weigh on their valuations ahead of the elections. The region is less of a safe haven than in past crises (political risk may weigh on the valuation of the US currency and US risky assets). We have therefore decided to underweight US equities and the US dollar. We have temporarily reduced our exposure to US technology stocks. Their strong performance and high relative valuation make them now more vulnerable to a correction. As we remain structurally positive on this theme, we would take the opportunity of a correction to reinforce our exposure to the technology sector.

Below we analyse the possible impact of the outcome of the presidential election on US assets and on financial markets more generally.

Which president? Which Congress? Unified or divided? The impact on the economy and markets is an equation with several unknowns

The next US president will potentially be disruptive! Joe Biden will be disruptive on domestic policy, which will not provide continuity with the current president, while Donald Trump will continue to be disruptive on the international stage. Regardless of the President-elect, we must also take into account the composition of Congress.

A unified Congress would make it possible to anticipate more clearly the policy that will be pursued by the new government

- Generally speaking, with a unified Congress, there will be less uncertainty about the policy that will be adopted. Investors will be able to position themselves more quickly in relation to the domestic and international consequences of the candidates' programmes.

- In an economic crisis, the government's response may be more definite and substantial, even if Republicans and Democrats do not provide the same type of support.

- A more sustained growth trajectory could lead to a greater steepening of the yield curve. However, the rise in rates will remain limited, given the change in strategy that the Federal Reserve has just announced. Risky assets (equities and credit) should also react positively to the prospect of higher growth. The impact on the US currency is less clear, and will also depend on the growth trajectory of other major economies.

- A political and economic programme with a clearer direction… for better or worse. President Biden's agenda would be more favourable to a greener economy (a target of zero net emissions by 2050), but would also be more disruptive for domestic assets (impact of tax increases?). Donald Trump will surely continue to exacerbate domestic and international tensions, maintaining a higher level of political uncertainty.

Conversely, a divided Congress (a Democrat House of Representatives and a Republican Senate) could represent a risk to growth in the event that Joe Biden wins

In the absence of a majority in Congress, the President can only implement part of his programme. The potentially most negative scenario would be a Democrat victory for the presidency, having to deal with a divided Congress. In this case, Republicans could oppose part of the economic programme: higher spending financed by tax rises. If Donald Trump was re-elected, a divided Congress could nevertheless have a positive aspect, as this counterweight would be a moderating factor.

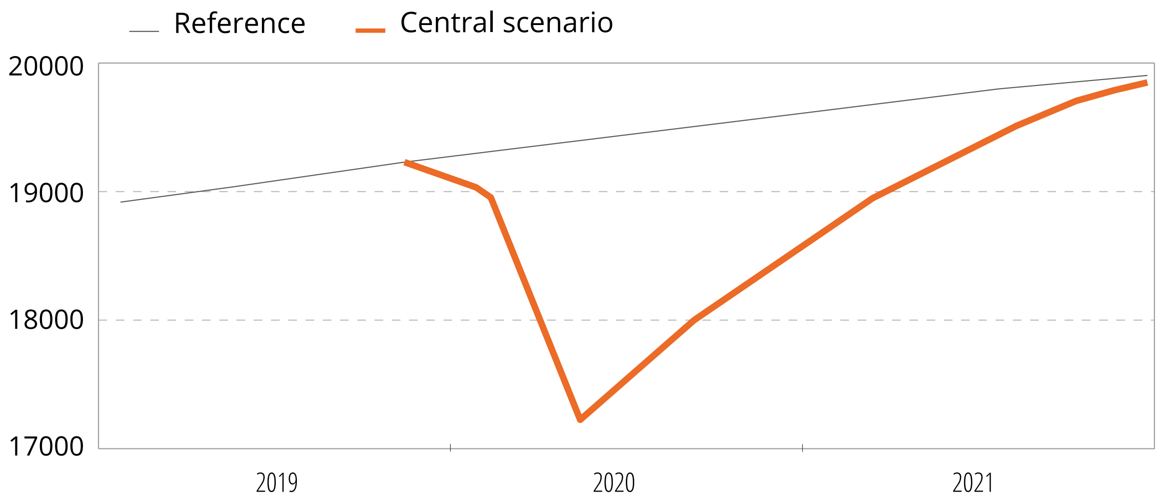
Our central economic scenario is compatible with a victory of one or the other of the candidates, which would not lead to excessive domestic or international disruption likely to destabilise the economic recovery under way.

Our central scenario – a gradual return of the economy to its reference trend – assumes moderate additional fiscal support at the end of the summer ($300 in additional weekly unemployment benefits until December 2020) and a marked reduction in social distancing at the end of 2021.

Chart 6: Central scenario

GDP level

Constant dollars



	GDP growth		Cumulated GDP loss* over 2020-21
	2020	2021	
Central scenario	-5.1	7.0	4.4

* Loss compared to the baseline

Impact on GDP level in 2020

% against the baseline

	March	April	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
Central scenario	-5	-14	-11	-9	-9	-8	-8	-7	-6	-5

Sources : Refinitiv Datastream, Candriam

What will be the impact of Republican and Democratic programmes on the various asset classes?

	Re-election of Donald Trump	Election of Joe Biden
Election programme	**His election programme is the same as in 2016.**	**His programme may produce significant reversals on the domestic market.**
	Domestic policy will be marked by a certain continuity, with the key points of tax cuts, continued deregulation and restrictions on immigration. His policies would avert regulatory risks for companies in the oil and health sectors.	Joe Biden's election will be more destabilising for the US domestic market than for the rest of the world. There will be considerable economic support, but it will be applied differently: tax rises, minimum wage increases, infrastructure investment plans, taking the climate and more sustainable development into account. The healthcare sector is also a major divergence point (anticipated extension of Obamacare), and the move towards deregulation is likely to stop.
	Foreign policy remains the main cause of uncertainty, as the President's behaviour proved to be unpredictable during his first term of office. As the only anchor, we still anticipate less multilateralism and a strong line with China.	On the other hand, US international relations will be able to regain a more traditional and less chaotic footing, with the return of multilateralism. In this scenario, the strategic, economic and trade dialogue with Europe would be re-established.
What impacts can we anticipate on the markets?	Foreign policy was destabilising for non-US assets during the President's first mandate. Risky assets in China, emerging countries and Europe could suffer as a result of US protectionist pressures, as has been the case over the past four years. Political risk will continue to be a key factor for the financial markets.	The sectoral impact on the US domestic market will probably be greater. It will be positive in the infrastructure and transport sectors, renewable energies and more generally on issues relating to sustainable development. Conversely, the impact will be more negative on healthcare and energy (oil and gas).
	On the US domestic market, the re-election of Donald Trump could favour a reduction in the risk premium on the energy and healthcare sectors.	Non-US assets could benefit from more constructive and less chaotic relations. Europe and emerging countries are unlikely to see their performance negatively impacted by unpredictable political risk.

Whatever the results, our allocation will remain flexible and opportunistic, and may benefit from corrective periods to increase our exposure to risky assets (equities and bonds) if our economic scenario remains valid.

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