2024 US Election

High-Stake Agendas

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12 JULY 2024, CIO OFFICE & MACRO RESEARCH

FLASHNOTE

SUMMARY

- The 2024 US presidential election **is likely to be decided by narrow margins in a few battleground states, as the electorate has become deeply divided**. Polls indicate an expanding lead for Trump over Biden in what was expected to be a close race before the first presidential debate. Two historically unpopular candidates, Biden's age, and Trump's legal troubles add **an exceptional level of uncertainty**.
- **Our base case is a Trump win with a unified government conditional on Biden staying in the race,** with a divided government the next likely scenario. If Biden wins, a divided government would be the most likely outcome compared to a sweep. However, **we assign a significant probability to Biden dropping out of the race, in which case** most signs point to Vice President Kamala Harris becoming the Democratic nominee**. We stand ready to adjust our scenarios** depending on who the replacements are on the ticket. Our working assumption is that the policy agenda of a replacement nominee would look similar to Biden's.
- **We expect Trump's policies on taxes, trade, and immigration to be more inflationary** than those of a Democratic president. Macro uncertainty also rises under Trump, as the range of outcomes is wider.
- A second Trump administration would be much more protectionist and combative than a second Democrat administration, with trade tensions rising for both adversaries and allies. **Tariffs and restricted labor supply from reduced immigration would clearly boost inflation**. The scope of any potential tariffs under Trump is significantly wider than in his first term, but we would treat the proposal of a 10% universal tariff and a 60% tariff on Chinese imports as the upper bounds of any eventual outcome.
- The growth impact under Trump is mixed, as tariffs and immigration restrictions are likely to have a negative effect near term, but could be offset by tax cuts and deregulation. The growth impact would lean negative if there is a divided

government under Trump, as significant tax cuts would have to be ruled out and tariffs would likely weaken US and global growth.

- Under all scenarios, **we expect some or most of the 2017 Trump tax cuts to be extended once they expire at the end of 2025, raising the deficit relative to a full roll-off of the tax cuts**, which is the current law. There is a lack of political consensus on both sides to address fiscal (un)sustainability. A focus on industrial policy and deepening political polarization suggest meaningful debt reduction is unlikely any time soon.
- The fiscal deficit is likely to rise the most under a Republican sweep as Trump has proposed additional tax cuts that cannot be fully funded by revenue generated from tariffs. The deficit increase would likely be smallest under a Democratic sweep as the agenda focuses on raising taxes on high-income earners and corporates. A divided government is likely to produce a deficit somewhere in the middle with limited extension of the tax cuts and not much more.
- **We expect a hawkish tilt to monetary policy under Trump, and little change under Biden**. In the next two years, we expect 225bps of rate cuts, bringing the policy rate to 3% by the end of 2026. Under a Trump presidency, we would remove 75-100bps of rate cuts from the baseline, as the boost to inflation from tariffs and restricted immigration and the boost to growth from tax cuts and deregulation outweigh a negative growth shock from tariffs. Although the risk of an unorthodox candidate for a new Fed chair, who could be directly influenced by the president, arises under a Trump presidency, we see it as unlikely that the executive branch would de facto set monetary policy.
- The current macroeconomic backdrop differs significantly from the onset of the previous presidential races in 2016 and 2020 - a deteriorating fiscal trajectory and above-target inflation introduce new uncertainties.
- **Fixed income**: Whether we see new tariffs that push inflation higher after the election will help determine the trajectory of policy rates in the years ahead. In the case of a Republican sweep, the Fed could cut the fed fund rate only to 4% by end-2026 from 5.5% currently, which is largely in line with current market pricing. Nevertheless, we could see the 10-year US Treasury yield rise from 4.2% (on July 11) towards 4.9% by end-2025, as a number of factors (among them, a sustained increase in the US fiscal deficit) point to a structural rise in the 10-year term premium from its current low level of 0.13% (on June 30). In the case of Trump winning but Congress being divided, the impact of higher tariffs on economic growth would not be fully offset by more fiscal stimulus. In this situation, we could see a limited rise in the 10-year yield to around 4.6% by end-2025 in a context where the Fed still has room to cut the fed funds rate to 3.75%. The scenario of Democrats winning the election is the most favourable for US Treasuries in our view, as this would enable the Fed to cut rates to as low as 3% by end-2026 which is about 100 bps lower than recent market pricing. Under this scenario, we would foresee the 10-year US Treasury yield falling below 4%, likely settling at a level of around 3.7-3.8% by end-2026.
- **Equities**: While geopolitical newsflow can create short-term volatility in equity markets, longer-term performance will reflect the extent to which political decisions impact subsequent economic growth, interest rates and profit trends. We do not believe any of our election scenarios explicitly represent an outright

'good' or 'bad' outcome for stocks as each contains a mix of positive and negative implications. For example, while we expect markets will react most positively to a Republican 'clean sweep' initially on hopes that further tax cuts and deregulation foster stronger profits, the prospect of higher tariffs means this is likely to come at the expense of stickier inflation, fewer rate cuts and higher yields. This trade-off suggests that a repeat of the low quality, pro-cyclical rotation we saw after Trump's 2016 victory is unlikely to be sustained. Nor would such an outcome be a major threat to US tech leadership. While we believe a Republican victory is likely to lead to a bigger 'knee-jerk' equity rally, this doesn't imply that a Democratic win would represent a negative for US stocks, especially if it comes with a divided congress which represents the current status quo. A Republican victory should favour US stocks over their global peers given the prospect of additional tariffs and a stronger USD. We see less US election risk for Japan than either Europe (more sensitive to trade restrictions) or EM (negatively exposed to stronger USD).

- **FX**: Under our base case of a Trump victory and a Republican House (a 'clean sweep'), the US dollar will likely strengthen significantly, mostly due to the imposition of wide-ranging tariffs (though the net effect of these will depend on any retaliatory measures adopted by the US's trading partners). In addition, protectionist measures will likely have an inflationary effect, which would lead, all else being equal, to higher policy rates and an upward shift in the yield curve. Even if price and rate shocks weigh on domestic demand in the short term, US growth is likely to continue to outperform that of its peers. Our belief that equity markets would continue to perform well under a Trump presidency is likely to bolster sentiment towards the USD. Finally, the prospect of sustained re-shoring, increased capital expenditure and a manufacturing revival provide fundamental support for the USD in the medium term. We expect the EUR/USD rate to be at 1.05 at end-2024 and at 1.02 at end-2025. In case of a divided government, the appreciation effect would be less pronounced given the constraints on policies dependent on legislative approval. In the case of a Biden victory, the USD would likely depreciate slightly as lower interest rate levels could bring valuation concerns back to the fore.
- In this note, we analyse the state of play in the presidential and congressional races, and the economic impact of different election scenarios. We then dive deeper into fiscal policy, trade policy, immigration policy, and monetary policy.

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THE PRESIDENTIAL RACE – EXCEPTIONAL UNCERTAINTY, WITH TRUMP LEADING IN POLLS

This election is likely to be decided by **narrow margins in a few battleground states**, as the electorate has become deeply divided. A presidential candidate has to receive a majority of electoral college votes (at least 270 out of 538), and the candidate who wins the majority of votes in a state typically receives all of that state's electoral votes (except in Maine and Nebraska, which split their electoral votes).

Before the first presidential debate in late June, we were already pointing to an exceptional level of uncertainty in this year's race due to two historically unpopular candidates**,** Biden's age, Trump's legal troubles, and a fast-changing economic outlook.

Post the debate, national polls (chart 1), swing state polls (chart 2), polling-based forecast models, and betting markets all indicate **an expanding lead** for Trump in what was expected to be a close race pre-debate. Trump's rise in the polls could potentially put more traditionally Democrat-leaning states in play for the general election.

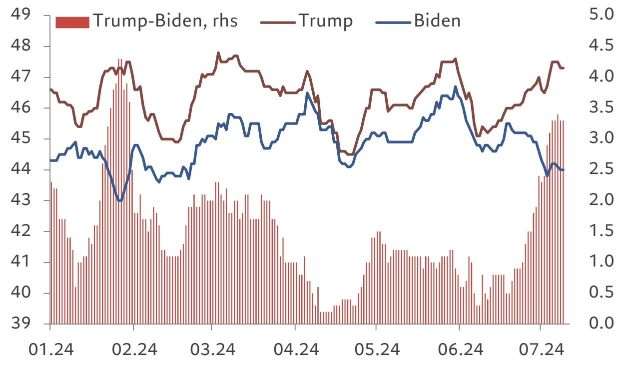
In this note, **we consider four different election scenarios under a Trump-Biden rematch**. At the time of writing, political pressures are building for President Biden to step down as the Democratic party nominee (not the presidency, which is a separate issue). W**e assign a significant probability to Biden dropping out of the race**. In that scenario, most signs point to Vice President Kamala Harris becoming the Democratic nominee. Several state governors could also be in the running (Gavin Newsom, Gretchen Whitmer, J.B. Pritzker, Josh Shapiro, etc.). Without much public comments on their respective policy platforms, our working assumption is that their policy agenda would look similar to Biden's. However, **We stand ready to adjust our scenarios** depending on who the potential replacements are on the ticket.

We think **third-party presidential candidates play the role of spoiler rather than viable options**. In the 1992 election, Independent Party candidate Ross Perot won 18.9% of the national popular vote, the largest in recent history, but he received zero electoral college vote and Clinton went on to win the election with only 43% of the popular vote. **Third-party candidates are drawing more from Biden than Trump in national polls, but support for third-party candidates and the undecided vote share tend to decline as the election approaches and voter impressions solidify**[1].

Polls also need to be interpreted with a grain of salt. For example, polls consistently underestimated Trump's support in the 2016 election. Trump supporters are likely less trusting of polls and the establishment, making them less likely to express their support for Trump when surveyed. On the other hand, polls suggesting a "red wave" in the 2022 mid-term elections turned out to be wrong.

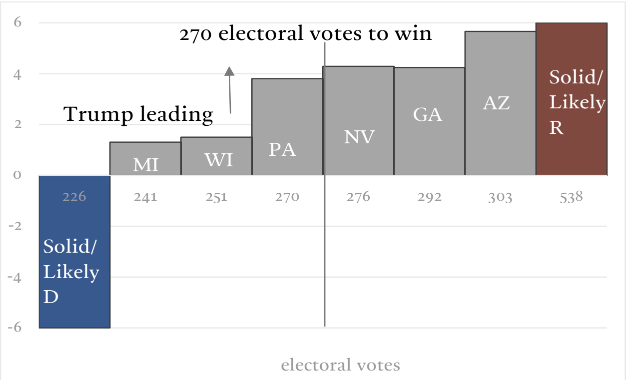
[1] In the event that no one gets 270 electoral votes (not impossible but highly un-likely), the newly elected U.S. House of Representatives would elect a president by allocating one vote to each of the 50 states. A simple majority, 26 state votes, would decide the presidency.

Chart 1: General election polling average, %



Source: Pictet Wealth Management, RCP, as of July 2024

Chart 2: Key swing state polls, 7d average, %



Source: Pictet Wealth Management, RCP, as of July 2024

CONGRESSIONAL RACES – CLOSE, WITH A REPUBLICAN ADVANTAGE IN THE SENATE

The make-up of Congress is crucial in determining what policy proposals can become legislation. Policies on taxes and spending need Congressional approval, while the Senate votes on nominations, like Federal Reserve Chair and Supreme Court justices. In past election cycles, single-party control has generally led to more meaningful fiscal policy changes, on average. However, even in a clean sweep scenario, we expect slim majorities in Congress, which could limit policy ambitions as compromises need to be made to moderate policymakers.

In our view, a unified government is more likely under a Republican victory, and a divided government with a Republican Senate is more likely under a Democrat Victory, especially in a close race. Regardless of the winning party, we current see about even odds of a unified vs. a divided government.

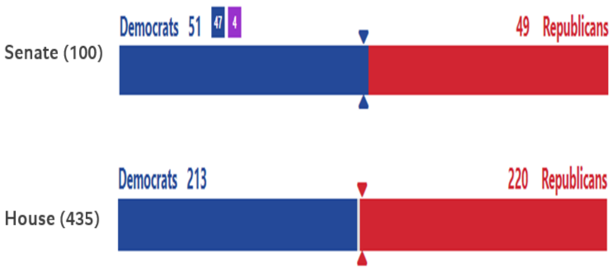
Republicans are favoured to take back the Senate, while Democrats have a slight advantage in the House of Representatives.

However, **we think the performance of presidential candidates is an important factor in the down-ballot Congressional races, especially in the House**. Every House seat is up for election in November, and split-ticket voting (voting for different parties for national and congressional elections) has become less common. **We expect the House to go in the direction of the party winning the presidency**. That said, the current margin is so thin that one cannot rule out a scenario in which the White House and House go in opposite directions, leading to a divided government.

In the Senate, Republicans have an edge in the Democrat-controlled chamber. Only 34 of the 100 Senate seats will be up for election this year, with 23 of this year's contests for seats currently held by Democrats, compared with just 11 for Republicans. Senator Manchin's (D-WV) retirement in a heavily Republican state is likely to leave Democrats with 50 seats at most, which would make the vice president the tie-breaking vote. Democrats will have to defend two additional seats in states that Trump won by a wide margin in 2020 (Montana and Ohio). On the other hand, we wouldn't rule out a Democratic Senate especially if the Democrats win the White

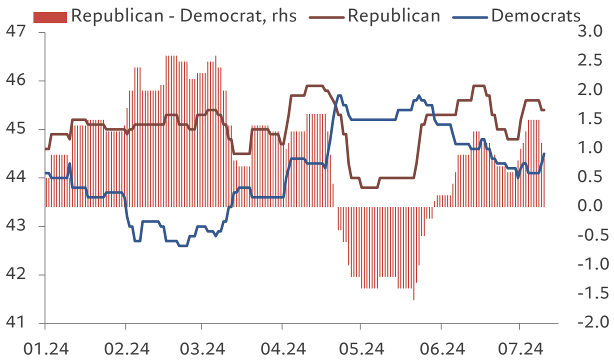
House. Democratic Senate candidates in Republican and swing states are still polling ahead in most of them, despite trailing in presidential polling.

Chart 3: Current composition of Congress



Source: Pictet Wealth Management, 270towin, as of July 2024. 4 independent Senators caucus with Democrats. There are two vacant seats in the House

Chart 4: Generic congressional ballot - do voters want Republicans or Democrats in Congress?



Source: Pictet Wealth Management, RCP, as of July 2024

ECONOMIC IMPACT OF DIFFERENT ELECTION SCENARIOS

This US election has the potential to significantly reshape the macro outlook, as the Republicans and the Democrats propose substantially different policy agendas.

In the table below, we summarize our expectations for inflation and growth under the four election scenario, **ranked in order of likelihood and conditional on Biden staying in the race**. We also present the impact of each scenario on the fiscal deficit relative to the current law of no tax cuts extension, and the policy rate relative to our baseline. Under trade tariffs, the arrows indicate our subjective probabilities of implementation.

We summarize our policy expectations, focusing on four key areas we identify as the most impactful for the outlook - **fiscal policy on taxes and spending, trade policy, immigration policy, and monetary policy implications**.

Chart 5: Potential economic impact under different election scenarios

More likely to less likely →

Potential impact on macro variables	Republican sweep	Republican w/ divided Congress	Democrat w/ divided Congress	Democratic sweep
Inflation	↑↑	↑↑	=	=
Growth*	=	↓	=	=
Fiscal deficit*	↑↑↑	↑↑	↑↑	↑
Trade tariffs (likelihood)	↑↑↑	↑↑↑	=	=
Policy rate (relative to our baseline)	↑	↑	=	=

*Growth impact relative to baseline of partial tax cuts extension
*Fiscal deficit impact relative to current law of no tax cuts extension (current law/CBO projections)
Source: Pictet Wealth Management, as of July 2024

The expiration of the 2017 Tax Cuts and Jobs Act (TCJA) on personal income at the end of 2025 will be the central focus for Congress next year. Policy proposals on the corporate tax rate, small business taxes, and the budget on social spending and clean energy differ significantly between the two parties. **Taxes and spending changes would require Congressional approval, through a budget process known as "reconciliation"**[2].

The president has significant power over trade, foreign, and immigration policy. Protectionist policies and stricter immigration policies will be pursued by both candidates, but they will be more disruptive under Trump and conflicts with the US' allies are more likely.

Importantly, **the current macroeconomic backdrop differs significantly** from the onset of the 2016 and 2020 presidential races. For one, **the fiscal trajectory has deteriorated sharply** after the 2017 Trump tax cuts, pandemic response, and Biden-era spending on infrastructure. Both the primary deficit and net interest payments are elevated and projected to rise to historic highs in coming years. For another, **inflation is above, not below target. Investors in the 2016 election focused primarily on fiscal benefits, but a deteriorating fiscal backdrop and above-target inflation introduce new uncertainties**.

[2] It allows the majority party to include instructions in the annual budget resolu-tion to pass legislation affecting taxes, spending, or the debt limit, which can then pass with only 51 votes in the Senate (i.e., it is protected against filibusters. This process can only be used once per budget cycle (normally once per year) for each subject, and typically results in no more than one reconciliation bill per year.

In all four scenarios, we expect some or most of the 2017 Trump tax cuts to be extended, raising the deficit relative to full roll-off of the tax cuts, which is the current law and the assumptions made under the current Congressional Budget Office (CBO) projections. This should start to raise the deficit beginning in 2026 as the tax cuts expire.

The fiscal deficit is likely to rise the most under a Republican sweep as Trump has proposed additional tax cuts, which won't be fully offset by the revenue generated by new trade tariffs. The deficit increase is likely the smallest under a Democratic sweep as Biden focuses on raising taxes for high-income earners and corporates. A divided government is likely to produce a deficit somewhere in the middle with limited extension of the Trump tax cuts and not much more. It is not our baseline but a divided government, either with a Republican or a Democratic president, faces the risk of the economy falling over a **fiscal cliff** by not extending the tax cuts, which would produce the most negative growth shock.

There is a lack of political consensus to address fiscal (un)sustainability. Neither candidate has put fiscal sustainability as a priority (or even a talking point) in their agenda. A focus on industrial policy and deepening political polarization suggest **meaningful debt reduction is unlikely any time soon**.

We expect Trump's policies on taxes, trade, and immigration to be more inflationary. A second Trump administration would be much more protectionist and combative than a second Biden administration, with trade tensions rising for both adversaries and allies. Tariffs and restricted labor supply from immigration would clearly boost inflation. The scope of any potential tariffs is significantly wider than those in his first term, but we would treat the 10% universal tariff and the 60% China tariff as the upper bounds of any eventual implementation.

The growth impact under Trump is mixed, as tariffs and immigration restrictions are likely negative near term, but **tax cuts and deregulation could offset** some impact. The growth impact would lean negative if there is a divided government under Trump, as significant tax cuts would have to be ruled out.

Macro uncertainty also rises under Trump, as the predictability is lower and the range of outcomes is wider compared to Biden.

We therefore expect a hawkish tilt to monetary policy under Trump, and little change to our interest rate baseline under Biden. In the next two years, we expect 225bps of rate cuts, bringing the policy rate to 3% by the end of 2026. Under a Trump win, we would remove 75-100bps of rate cuts from the base line, as the boost to inflation from tariffs and the boost to growth from tax cuts and deregulation outweigh the negative growth shock from tariffs.

Although the risk of an unorthodox candidate for a new Fed Chair, whose policy making could be directly influenced by the president, arises under a Trump presidency, we see it as unlikely that the executive branch would de facto set monetary policy.

SUMMARY OF POLICY EXPECTATIONS

Below we detail our policy expectations that underpin our macro outlook summarized above.

Republican sweep - Almost full extension of the 2017 Trump tax cuts, substantial tariffs (but less than what Trump has proposed) that would then fund small business tax cuts, corporate tax rate unchanged at 21% (but could be reduced to 15-20%), a small extension of the Child Tax Credit (CTC), curtailment of IRA subsidies, support for the oil and gas sector, deregulation, stricter immigration policy by ending asylum and reinstating the "Remain in Mexico" policy, less support for Ukraine and increasing pressure on NATO allies.

Republican president with a divided Congress - Narrower extension of the 2017 Trump tax cuts than under a Republican sweep, substantial tariffs (but less than what Trump has proposed), corporate tax rate unchanged at 21%, a larger extension of the Child Tax Credit (CTC) than under a Republican sweep, support for the energy sector, deregulation, stricter immigration policy by ending asylum and reinstating the "Remain in Mexico" policy, less support for Ukraine and increasing pressure on NATO allies.

Democratic president with a divided Congress - Narrower extension of the 2017 Trump tax cuts similar to the Republican divided scenario, limited tariffs and investment restrictions on strategically important products, corporate tax rate unchanged at 21%, a larger extension of the Child Tax Credit (CTC) than under a Republican sweep, support for alternative energy, slightly stricter immigration policy by closing asylum loopholes, and continued support for Ukraine.

Democratic sweep - Narrowest extension of the 2017 Trump tax cuts of all the scenarios, with tax increases on income over $400k, wealth tax and higher capital gains tax, limited tariffs and investment restrictions on strategically important products, corporate tax rate raised to 28% (but could be unchanged), the largest extension of the Child Tax Credit (CTC) with refundability, support for alternative energy, slightly stricter immigration policy by closing asylum loopholes, and continued support for Ukraine.

In the sections below, we dive deeper into four main policy areas we deem essential for investors – fiscal policy, trade policy, immigration policy, and monetary policy.

FISCAL POLICY – ALL ROADS LEAD TO HIGHER DEFICITS

Neither candidate has outlined a strategy to guide the US toward sustainable debt levels, despite projections that budget deficits will continue to be substantial, and the debt-to-GDP ratio is set to surpass the post-WWII high of 106%. These challenges, including the projected insolvency of Social Security within ten years and interest payments now ranking as the third largest budget expense—above defense spending—will confront the next administration.

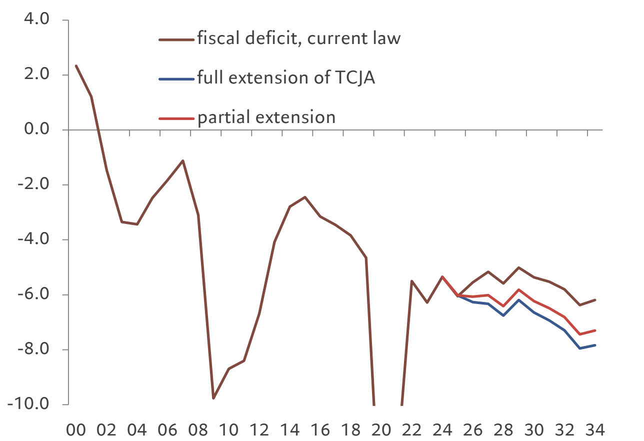
The most pressing issue in 2025 is the expiration of the 2017 Trump tax cuts on personal income. The risks to growth are asymmetric – extending the tax cuts would lead to a status quo for households, so it won't be a positive. However, not extending the tax cuts would lead to higher tax burdens, effectively lowering disposable income, creating a headwind for consumption growth. Under the CBO's projections, extending fully expiring income tax provisions could add $3.3 trillion to the primary deficits over the next decade, with net interest payment adding another $467 billion to those deficits. Extending the tax cuts only for those making under $400k per year, proposed by Biden, would still add a huge chunk to the deficits, as those higher-income households make up only roughly 2% of the households (chart 6 and 7).

However, we think these estimates are probably the upper limits for the increase in deficits, as even in a sweep scenario the margins in Congress are likely to be thin, limiting policy ambitions.

The proposed revenue offsets from either party would not be enough to fully reverse the rise in deficits. Trump has vowed to use revenues generated by tariffs to fund further tax cuts on top of the extension. Importantly, raising tariffs would likely reduce imports and erode the tax base, limiting the magnitude of any potential revenue raising.

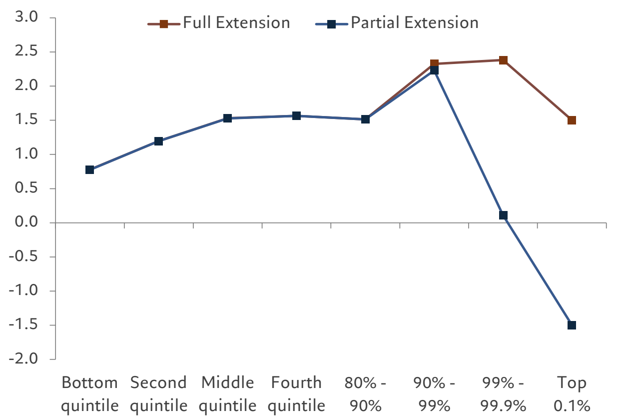
President Biden has proposed raising the corporate tax rate, capital gains tax, and to introduce a new wealth tax to offset the extension of the 2017 tax cuts. This would only be possible under a Democratic sweep scenario (the least likely in our view), and even then the math would not work. Democrats have proposed extra spending measures, including raising the child tax credit and making it fully refundable, increasing spending on affordable housing and green energy. These will offset any revenue raised from higher taxes.

Chart 6: Fiscal deficit under different scenarios for the 2017 Trump tax cuts



Source: Pictet Wealth Management, CBO, Yale Budget Lab, as of July 2024

Chart 7: Percent change in after-tax income by income group, 2026, relative to current law of no tax cuts extension



Source: Pictet Wealth Management, CBO, Yale Budget Lab, as of July 2024

TRADE POLICY – "NO TRADE IS FREE"

Although both candidates champion industrial policy, the two candidates differ significantly in their approach to tariffs. **A second Trump administration would be much more protectionist and combative than a second Biden administration, with trade tensions rising for both adversaries and allies**.

Comments by Trump and his former trade advisor Robert Lighthizer, who wrote the book "*No Trade is Free*", serve as guidance for his likely trade policy. Trump's policy proposals include a universal 10% tariff on all imported goods, reciprocal tariffs on countries imposing tariffs on the US, 60% tariffs on Chinese imports, and ending China's permanent most-favored-nation status and return to the status quo of pre-WTO entry.

In our view, **Trump's words need to be taken seriously but not literally**. Trump would have the legal authority to impose many tariffs without congressional approval, and he could move to impose such tariffs very early on in his presidency.

However, **we would treat the 10% universal tariff and the 60% China tariffs as the upper bounds of any eventual outcome**, because 1) His authority to impose tariffs on countries the US has free trade agreements with (Canada, Mexico, and 18 other countries) alone, without Congress, is at least up for a legal challenge. This could complicate and delay their implementation. 2)Trump tends to open negotiations with significant threats. And 3) There will inevitably be dramatic negotiations as other countries are now likely more experienced to retaliate.

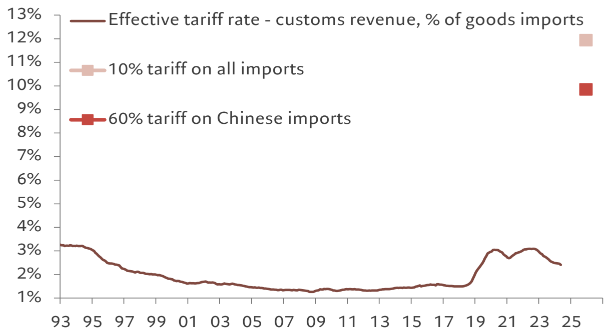
A Biden victory would largely maintain current trade policies with a focus on investment restriction and export controls rather than reducing trade deficits through higher tariffs. We expect tariff rates to remain stable for most imported goods, especially for US' allies. However, targeted tariffs on a select few industrial goods seem likely, similar to tariffs recently imposed on Chinese electric vehicles and solar cells. With no material change in direction (with the exception of more protectionism against China) we would not expect any significant economic impact.

Tariffs would clearly boost inflation, but likely weaken growth. The scope of the tariffs that Trump is proposing is significantly wider than the ones he introduced in 2019. Measured in the effective tariff rate (chart 8), customs revenue as a share of goods imports rose by around 2% during the Trump trade war. A 10% blanket tariff on all imports would raise the effective tariff rate by 10%, while a 60% tariff on Chinese imports would rase it by 8%.

The boost to prices could be considerable, but also highly uncertain as it depends on actual tariffs implemented, the ability of exporters to circumvent, the response of domestic producers, and any retaliation from trading partners. Overall, estimates point to as much as a 0.1% boost to core PCE inflation for every 1% increase in the tariff rate.

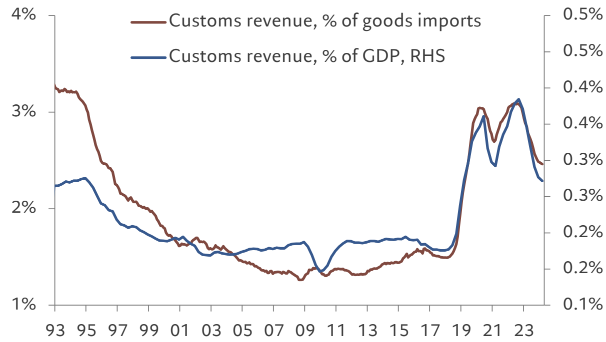
Tariffs would also be a drag on domestic and global growth. During the trade war unleased by Trump in 2019, the Federal Reserve had to implement insurance cuts as the trade conflict with China led to deteriorating business sentiment and a sharp tightening in financial conditions.

Chart 8: effective tariff rate



Source: Pictet Wealth Management, Census Bureau, US Treasury, as of July 2024

Chart 9: tariff revenue



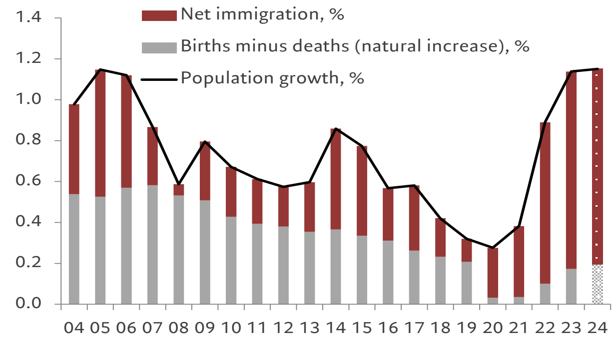
Source: Pictet Wealth Management, Census Bureau, US Treasury, BEA, as of July 2024

IMMIGRATION POLICY – TIGHTER CONTROLS

Immigration has become a pivotal issue in the election. **Both candidates have committed to tightening immigration controls, but a key difference is Trump's pledge to deport undocumented immigrants. This could trigger a meaningfully negative labor supply shock and increase wage pressures**. Net immigration is estimated at about 3 million in each of the past two years, significantly above the run rate under the first Trump administration (chart 10 and 11). The recent surge in immigration has driven faster population growth, adding to the labour supply, and helping to alleviate wage pressures. Net immigration could decline more rapidly than the CBO's projections under either president, but especially under a Trump presidency.

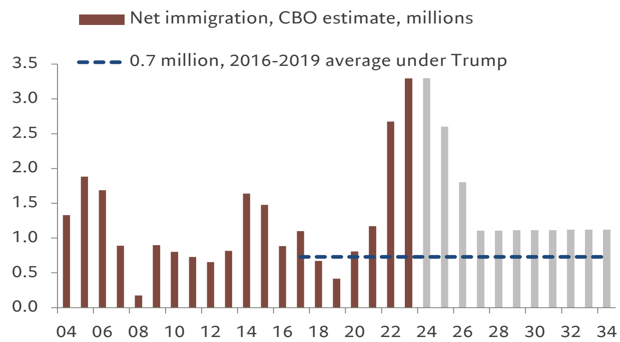
Trump has pledged to immediately launch "the largest deportation in American history". Trump's proposed measures include ending asylum and reinstating the "Remain in Mexico" policy from his first term. It is unclear how quickly any changes could be implemented, but this would eventually normalize border crossings following the recent post-pandemic surge. Under Biden, policies are also expected to become stricter, likely addressing loopholes in the current asylum process and continuing outreach to Latin American countries to control the flow of immigrants.

Chart 10: Population growth



Source: Pictet Wealth Management, CBO, as of July 2024

Chart 11: Net immigration with CBO estimates



Source: Pictet Wealth Management, CBO, as of July 2024

MONETARY POLICY – A HAWKISH TILT UNDER TRUMP

Monetary policy is not in the job description of the president. However, elections can impact monetary policy through the president's nomination of the Fed Chair and Board members. Former President Trump has said, if elected, he would not re-appoint Chair Powell when his term expires in 2026, and several names have emerged as potential candidates.

Can the president fire the Fed chair before his term ends? **Trump cannot fire Powell for policy differences alone**, only "for cause" which the courts have historically interpreted as requiring "inefficiency, neglect of duty, or malfeasance in office. Firing a Fed Chair would be unprecedented and likely end up in court. The same goes for demoting a chair and replacing him with a sitting governor.

The risk of an unorthodox candidate, whose policy making could be directly influenced by the president, arises under a Trump presidency. However, **we see it as unlikely that the executive branch would de facto set monetary policy,** for two reasons.

First, **the Senate has the final say in nominating the Chair**, and there is a common understanding among senators that Fed independence shall be preserved. In fact, in 2019 and 2020, a Republican Senate refused to advance the nomination of a few controversial candidates supported by Trump.

Second, Fed policy independence from political influence has been the bedrock of the global financial system. If the Fed was seen as simply taking marching orders from the White House, markets could react forcefully, leading to significant volatility which could in return cause the administration to back off.

Another risk arises from the president's comments. Trump regularly criticized Fed policy-making while he was in office. An NBER paper found that Trump's tweets had a negative impact on the expected policy rate, and led to an increase in stock prices and a decrease in long-term Treasury yields.

Although the executive branch doesn't make monetary policy, its decisions on spending, taxes, trade, and immigration have important macro impact.

We expect a hawkish tilt to monetary policy under Trump, and little change under Biden. In the next two years, we expect 225bps of rate cuts, bringing the policy rate to 3% by the end of 2026. Under a Trump presidency, we would remove 75-100bps of rate cuts from the baseline, as the boost to inflation from tariffs and the boost to growth from tax cuts and deregulation outweigh the negative growth shock from tariffs.

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