August 21, 2020

Maybank

FX Insight

US Elections & Implications on AxJ FX

US Elections on 3rd Nov

Come 3rd Nov, Americans will decide on whether Trump has been the leader that they can count on to guide them out of the healthcare/economic crises or they would rather give that chance to a familiar alternative - Joe Biden. The US Senate elections and the House of Representative elections will also be closely watched.

Biden Win A Positive on AXJs vs. Trump Win

We put together 4 potential permutations of Trump/Biden Presidency vs. Republicans/Democrats Senate and share what these scenarios could mean for markets with a focus on Asian FX. A Biden win and a Democratic Congress (our scenario #4) could imply a (1) **softer USD broadly** (on expectations of large fiscal spending contributing to deterioration in deficits); (2) neutral to slight negative market sentiment (on tax increases but slightly mitigated by spending proposals) and (3) positive relief for AXJs including RMB (on expectations for less confrontational approach and more predictive behavior of Biden). Our current year-end forecasts for USDSGD, USDMYR, USDIDR at 1.35, 4.15, 14,200, respectively, inherently prices in a Biden win (scenarios #3 or #4).

To more clearly verify linkages between the US elections and regional currencies' performance, we conduct a quantitative analysis using polling stats, USD NEER and a house-constructed risk sentiment indicator. Our analysis shows that the widening of Biden's lead over Trump is indeed statistically significant in contributing to ASEAN and commodity currencies' recovery since March, although the explanatory power of this lead pales in comparison to broader risk-on/off shifts in markets (Covid & other factors).

Polls are currently biased for scenario #4 outcome. **We caution that political developments can be fluid. A potential narrowing of Biden lead over Trump in the lead up to polling day is not impossible and this could warrant caution as markets may be caught wrong footed.** Scenarios of #1 and #2 would be less positive for AXJs including RMB.

Analysts

Saktiandi Supaat
(65) 6320 1379
saktiandi@maybank.com.sg

Christopher Wong
(65) 6320 1347
wongkl@maybank.com.sg

Fiona Lim
(65) 6320 1374
fionalim@maybank.com.sg

Tan Yanxi
(65) 6320 1378
tanyx@maybank.com.sg

This document was first published in Maybank KE's ASEAN X Macro on 21 Aug 2020.

US Elections – Scenarios and AXJ FX Implications – Quick Summary

	Senate	
	Republicans Retain Control	Democrats Take Over
Trump Win	*Scenario #1 - Status Quo: Trump as President and GOP Republican as Senate* - *An underpriced scenario for now and one that is likely to see trade uncertainty pick up, alongside FX volatility. Trump's "very tough" stance on China could risk deteriorating US-China relations.* ↓ *RMB and AXJ FX including SGD and MYR* ↑ *USD and safe-haven proxy FX JPY*	*Scenario #2 - Trump Presidency but Democratic Congress* - *Legislative deadlock; could hamper on post-COVID recovery momentum in US. Trump likely to continue "very tough" stance on China.* ↓ *AXJs such as RMB, SGD and MYR. Weakness could be amplified if risk assets come under pressure especially if slower US recovery momentum drags on global momentum.*
Biden Win	*Scenario #3 - Biden Presidency while Congress Remains Status Quo* - *Split congress may imply curtailed stimulus spending but also difficulty in increasing taxes. On net this maybe neutral for market sentiments. Biden Presidency may imply more predictability and less confrontational approach to China.* ↑ *AXJ FX including RMB, SGD and MYR.*	*Scenario #4 - Democratic Clean Sweep with Biden as President and Democrats Control Congress* - *Consensus base case scenario. Fiscal expansion policy and tax hike proposal can be pushed through with ease. These policies are likely to be mixed for sentiments (or market neutral to slight negative) from a markets perspective.* ↓ *USD (due to fiscal expansion)* ↑ *AXJ FX, including RMB and those currencies that closely correlates with RMB, such as SGD, MYR.*

Note: Assuming that Democrats retain control of the House of Reps.

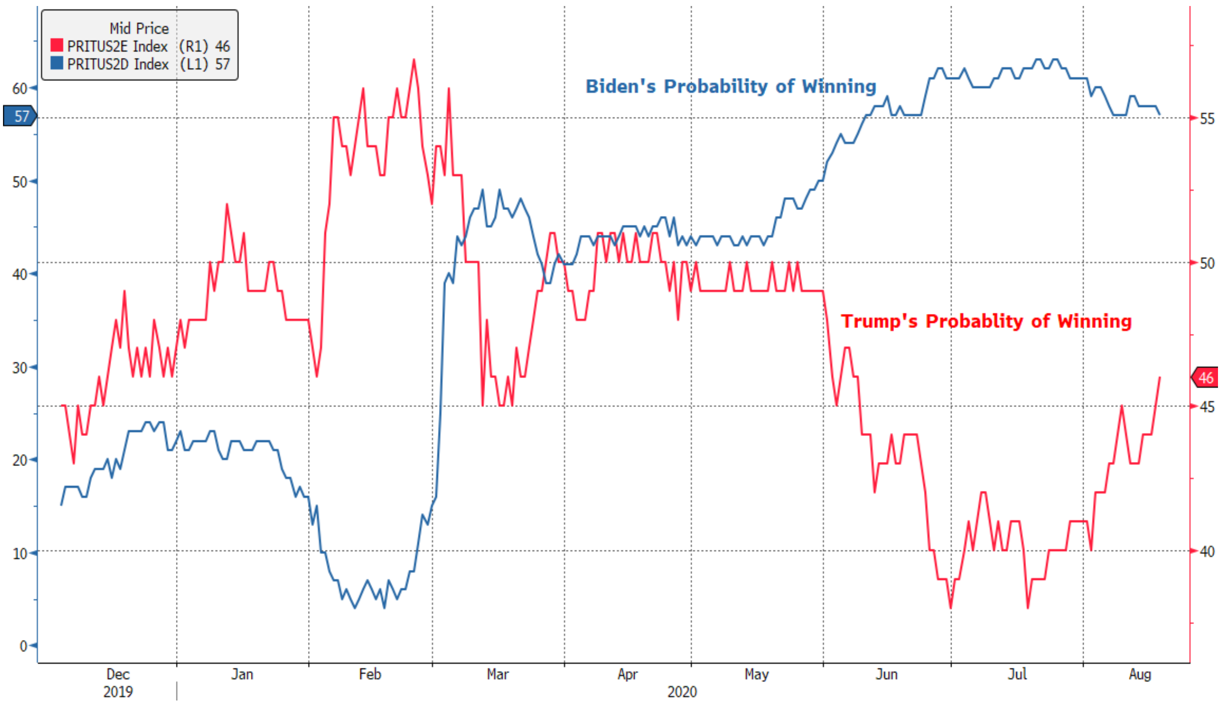
What is at Stake?

The US Elections will be held on 3 Nov and apart from the widely watched 59th US Presidential Election, there would be some focus on the 2020 US Senate elections (33 + 2 Seats contested) and the 2020 US House of Representative elections (all 435 seats contested).

59th Quadrennial Presidential Election - Incumbent Trump Vs. Joe Biden

President Donald J. Trump, along with Vice President Mike Pence would be vying for a second term and he would be up against Democratic Presidential candidate, Joe Biden whose running mate is Kamala Harris. According to PredictIt (as illustrated in the chart above) and punting data from the political market exchange, Biden is projected to have a greater probability of winning the Presidential Elections vs. Trump at this point, although the gap seems to be narrowing.

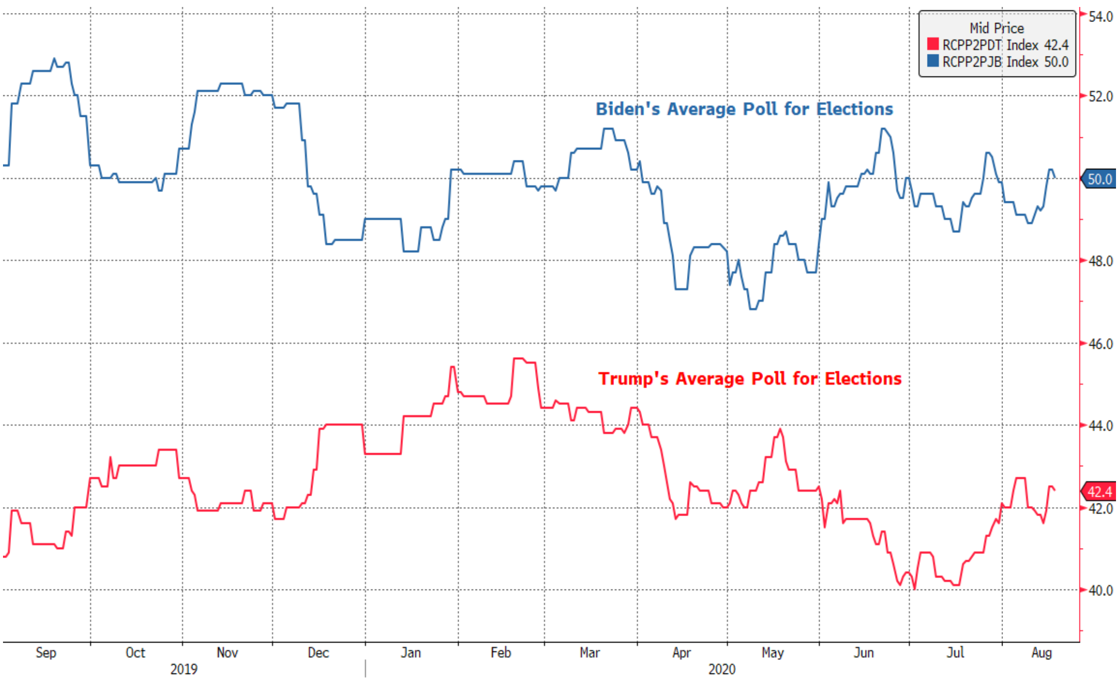
Figure 1: PredictIt Current Projection: Biden has a Higher Probability of Winning but Gap is Narrowing



Source: PredictIt, Bloomberg, Maybank FX Research & Strategy
Note: Data is as of 19 Aug 2020. For clarity, Blue is the party colour of the Democrats and Red, the Republicans'.

Based on Real Clear Politics which provides an average of polls that are available and updated daily, Biden retains a stable lead over Trump for the Elections, now at 50 vs. Trump's 42.4.

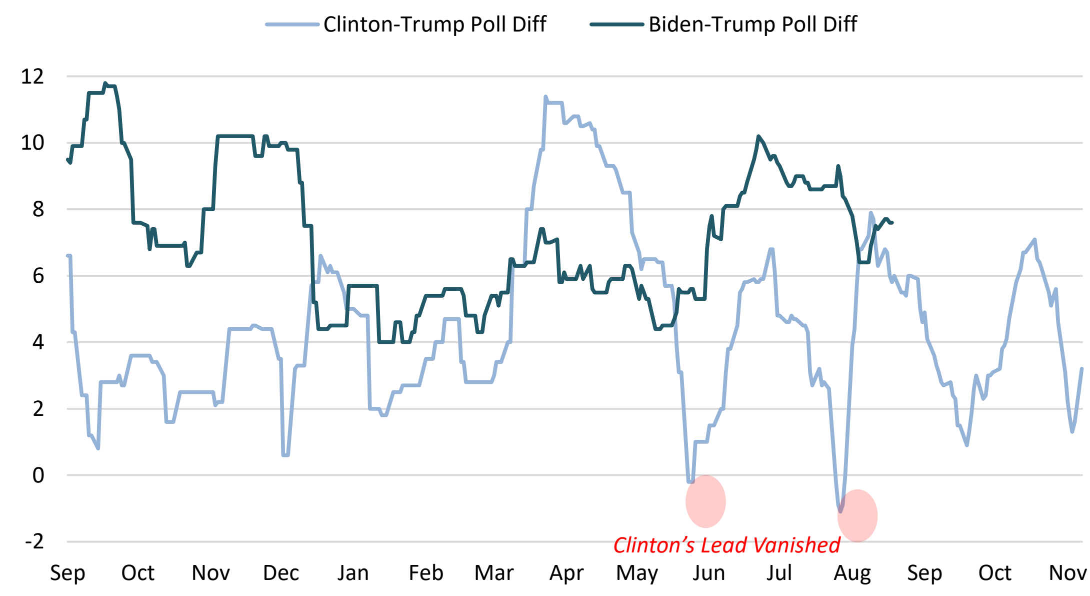
Figure 2: Real Clear Politics Show Stable Biden Lead



Source: Bloomberg, Maybank FX Research & Strategy

Back in 2016, Trump's victory was considered to be an upset as Clinton too maintained a lead over Trump for much of that year. However, the Biden's lead has averaged at 7.2 since the start of the year while the same measure for Hillary Clinton's lead at this point of the race averaged around 4.6. In addition, Clinton even lost her lead a couple of times in 2016 while Biden's lead has been rather steady so far.

Figure 3: Biden Maintains a Wider Lead over Trump vs. Clinton in 2016



Source: Bloomberg, Real Clear Politics, Maybank FX Research & Strategy

Note: The x-axis shows the dates for the Clinton-Trump pol difference in 2016. Period captured is 1 Jan 2016 to 7 Nov 2016. Period used for Biden-Trump Poll Difference is aligned correspondingly for comparison purpose - from 1 Jan 2019 to date (19 Aug 2019).

2020 US Senate Elections - Risks of Democrats Seizing Control

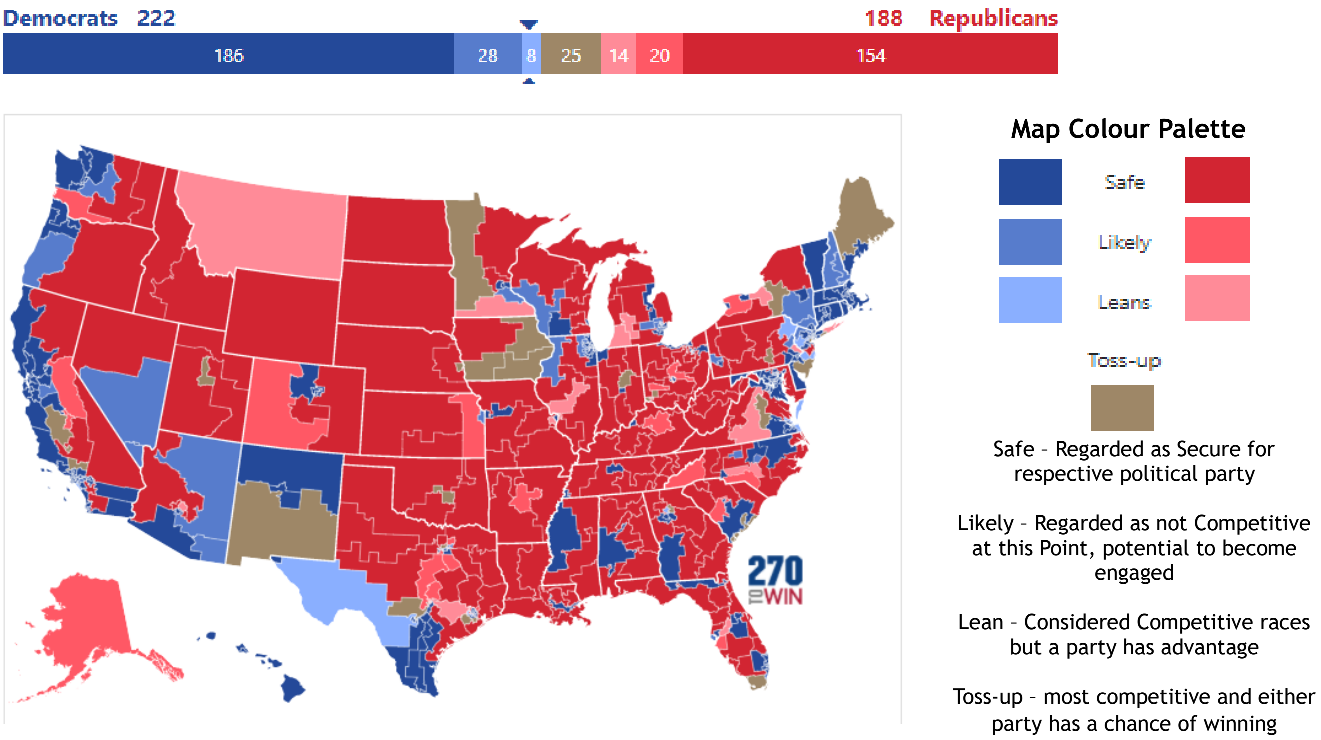
The US Senate is now controlled by the Republicans who hold 53 seats out of 100. 45 seats are now held by the Democrats along with 2 Independents who caucus with the Democrats. Assuming that Joe Biden wins and the Vice President (Kamala Harris) is a Democrat, the Democrats only need a net gain of 3 more seats to seize control of the senate. If Trump retains power, the Democrats would need 4 as the Vice President is a tie-breaker.

The US senate elections for this year comprise of the regular elections and 2 other special elections. For regular elections, 33 Seats would be contested for a 6y term (3 Jan 2021 – 3 Jan 2027). Two other special elections are held – one in Arizona due to the death of John McCain in 2018 and the other in Georgia because of the resignation of Johnny Isakson in 2019. As a result, taking into consideration the seats to be contested in the special elections, Republicans have to defend 23 seats this year. That is twice as many seats to defend vs. the Democrats' 12. We do see a real chance that the Senate could fall into the hands of the Blue.

2020 US House of Representatives Elections

The House of Representatives is now led by the Speaker of the House, Nancy Pelosi and controlled by the Democrats with 232 seats out of 435. Republicans have 198 seats. The Republicans need a net gain of 20 seats in order to seize control of the House and they have a lot more incumbents (27) that will not be seeking re-election vs. Democrats at only 9 (*Ballot Pedia*). The fewer number of open seats suggest that Democrats have a fair chance of retaining control of the House but the electoral climate could shift according to the Presidential race. Figure 4 below shows the current consensus forecast of seat leanings but note that the map tends to **exaggerate the advantage of the Republicans (Red) because areal units differ in size and significance.**

Figure 4: 2020 House Elections: Consensus Forecast



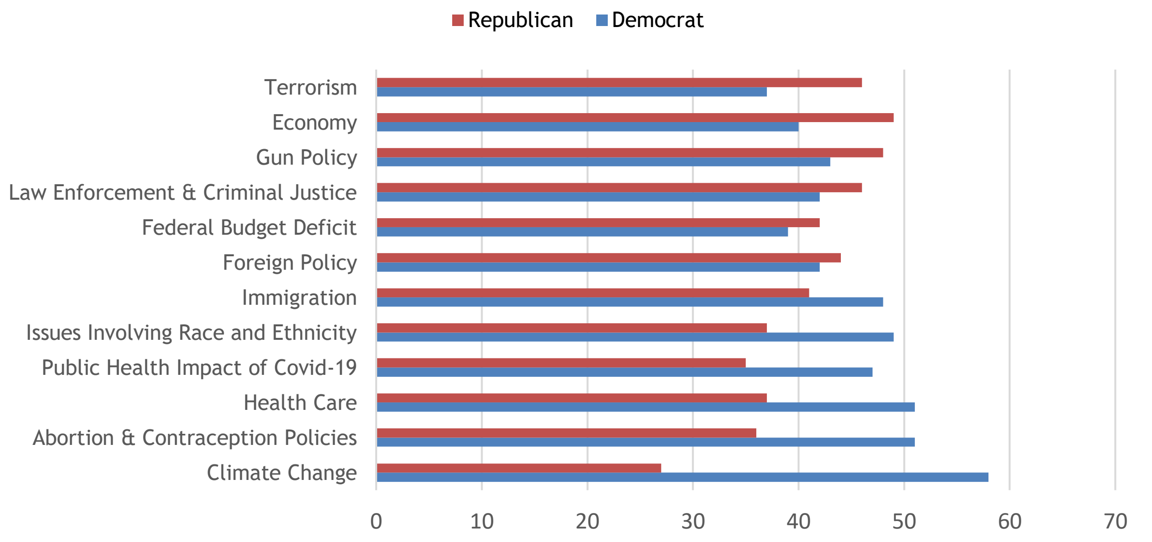
Source: 270 to Win (https://www.270towin.com/2020-house-election/consensus-2020-house-forecast)
Note: Updated 14 Aug 2020. Consensus is gathered from Sabato's Crystal Ball, The Cook Political Report, and Inside Elections. Also note that the map tends to exaggerate the advantage of the Republicans (red) because areal units differ in size and significance.

Taking into consideration the "open seats" in the House, the contested seats in the Senate as well as the current polls, there is a real possibility of Democrats achieving a **clean sweep** at the 2020 Elections – 1) seizing control of the senate, 2) retaining the House and 3) a Biden win.

Policy Leanings—Perceptions and Expectations

To better understand policy stances on both sides, we delve into how the average US voter may perceive the Republican/Democrat administration in their handling of key issues. Results from polls conducted by the PEW Research Centre are utilized.

Figure 5: % of Registered Voters Saying that Republican/Democrat Party Can Handle Key Issues Better



Source: PEW Research Centre
Note: Sample survey of registered voters conducted 23 Jul to 4 Aug.

The Democrats are clearly seen as being able to handle concerns over climate change (+31%-pt lead), abortion (+15%-pt), health care (+14%-pt), Covid-19 containment (+12%-pt) and racial discrimination issues (+12%-pt) better, whereas the Republicans are perceived to be more capable in handling of terrorism (+9%-pt), economy (+9%-pt), gun policy (+5%-pt) and law enforcement (+4%-pt).

Given the current state of affairs in the US, we think that voters could disproportionately be focused on (i) saving the economy and jobs, (ii) healthcare/Covid-19 handling, and (iii) racial tensions. Trump/Republicans would likely attempt to leverage on (i) in the lead-up to the elections, where they currently have a modest edge in perception, in the hopes that it can narrow the lead that Biden/Democrats are holding.

Interestingly, US voters are more or less neutral on the effectiveness of either administration on the key issues of budget deficit and foreign policy, which would arguably be of greater concern to international market watchers. On foreign policy, this could suggest that US voters largely feel that either administration would be inclined to view China as a long-term geopolitical rival and maintain inherently competitive stances on China-linked issues, despite potentially different approaches.

We summarize the key potential policy leanings of the two presidential candidates in a quick table.

Table 1: Policy Leanings of Trump vs. Biden in Key Issues

	Trump as President	Biden as President
US-China Issues	China-bashing may continue as Trump reverts to blaming China for the economic deterioration of America. **Conflicts on more fronts, with more sanctions**, but unlikely to use tariff policy as it has hurt domestic manufacturers, farmers.	China containment could resemble Obama's—pragmatic, rational. **Might strike a more outwardly reconciliatory tone with China in terms of international cooperation but maintain competitive stances in areas of tech, trade (via subsidies, tax incentives etc.)**. Likelihood of resorting to tariff policy is relatively low. Negative spillover impact on ASEAN from policy moves could be more modest. Biden has shown strategic yet ambiguous support for Taiwan in the past though, and may continue to render Taiwan subtle military assistance to prevent a forceful reunification.
Other Foreign Policy	Rely on phased bilateral deals, with frequent reviews and ad-hoc threats. Potential trade confrontation with EU. **Greater volatility in trade and investment relations.** Maintain status quo on Iran and climate change cooperation.	Likely to look for broad coalition of allies and increased reliance on, or cooperation with existing international institutions. **Hence more predictability in US foreign policy.** **Re-engagement in the TPP (now CPTPP) and T-TIP** could be positive for ASEAN members (Singapore, Malaysia, Vietnam) and EU, respectively. Re-enter nuclear deal with Iran. Resuscitate efforts on international climate change cooperation.
Fiscal/Tax	Near-term Covid Stimulus: **Likely more modest fiscal support, unemployment benefits**. Priority is to get workers back to jobs, hence proposal for liability protection for businesses (against lawsuits if customers contact Covid-19 on premises). Longer-term: Potential tax cuts supposedly skewed towards the "middle class". Boost domestic manufacturing, particularly in industries critical to national security (e.g., health supplies). Tax credits/tariffs to redirect jobs back from China. Focus on infrastructure spending.	Near-term Covid Stimulus: **Likely push for more aid to state and local govts, and higher jobless benefits**. Longer-term: Market-positives—Close to US$7trn more in spending over the next decade, including US$2trn in green investments and US$1.3trn in infra, US$750bn in healthcare. Market-negatives—Est. US$4trn increase in taxes on corporations, investments and wealthy Americans.
Healthcare/Covid-19 Handling	Status quo. Priority on re-opening of economy and schools, rather than on healthcare outcomes. Yet to propose alternative to Affordable Care Act after undermining it.	Ramp-up in testing, ensuring better coordination of medical supplies and healthcare aid. More cautious stance in normalizing activity. Bolster Affordable Care Act.

Source: Maybank FX Research & Strategy

Potential Scenarios and Implication on Markets

But to some extent, we think this is not just about a Biden or Trump win, but also, the **potential for Democrats to do a clean sweep**. There is a possibility that Democrats may take control of the Senate and from what we know, the Senate has certain powers. Together with the President from the same party, both the President and Senate can appoint the cabinet members as advisors to the President, as well as nominate and approve the Justices of the Supreme Court. According to what polls are saying for now, a number of seats are considered toss-ups including 6 GOP seats (Colorado, Georgia, Iowa, Maine, Montana and North Carolina). Democrats will need to gain 3 – 4 seats to take control (depending on whether Biden wins as the new Vice-President will be a tie-breaker).

We put together 4 scenarios in the matrix below, and share our views on how each scenario may pan out for markets, in particular on Asian FX. While there is focus on potential tax or regulatory changes from a Democratic sweep and whether Trump or Biden win is positive or negative for stock markets, our focus here is intended to put more emphasis on what the scenarios may mean for foreign trade policy, US-China relations and its potential implications on Asian FX. **Our scenarios assume Democrats will continue to retain control of the House of Representatives (HoRs).**

Table 2: Summary of Trump/Biden-Senate Scenarios Implication on FX (Expanded Version from Page 1)

	Senate	
	Republicans Retain Control	**Democrats Take Over**
Trump Win	**Scenario #1 - Status Quo of Trump retains Presidency and Republicans retain control of the Senate** For a start a continuation of current policy agenda of de-regulation, boosting manufacturing sector and potentially extension of tax cuts. May translate into a near term positive for market sentiment however lack of clarity on second term policy agenda raises doubts if positive market sentiment can be sustained Policy continuity of America First foreign policies. US-China tensions at risk of re-escalating, putting depreciation pressure on AXJs including RMB, SGD, MYR vs. USD and safe-haven FX JPY.	**Scenario #2 - Likely a case of legislative deadlock as HoRs and Senate are under Democrats while President is of different party - Republican** Policy compromises, pertaining to domestic issues (stimulus, tax cuts, etc.) will be challenging and less forthcoming. Could hamper post-Covid recovery momentum. Potentially weighing on risk assets. But on foreign trade issues, Trump is likely to continue with prior policies practices, re-negotiating trade deals on bi-lateral approach instead of multi-lateral and relying on the use of executive powers. US-China tensions could still be at risk of escalation. Depreciation pressure on AXJs such as RMB, SGD, MYR likely and could be amplified if risk assets come under pressure, especially if slow US recovery momentum drags on global momentum.
Biden Win	**Scenario #3 - Status Quo in Congress with a change of Presidency** Split congress may imply curtailed stimulus spending (risks of economic recovery momentum being derailed) and difficulty in increasing taxes (may be positive on risk sentiments). Biden's plans may have to be deferred till after mid-term elections in 2022 to carry them out (provided Democrats can take over the Senate). On net this may imply market neutral. Biden Presidency may imply less confrontational (but strategic) approach to China. From a market point of view, this could suggest marginal positivity on AXJ FX including RMB, SGD, MYR.	**Scenario #4 - Consensus Base Case (implied by polling results)** Allows for Biden to implement wide-ranging policies including Covid support measures, fiscal spending including the expansion of healthcare coverage (i.e. bolstering affordable Care Act) and pursuing tax increases with greater ease. These policies are likely to be mixed for sentiments (or market neutral to slight negative) from a markets perspective and possibly an overall negative for USD (due to fiscal expansion). Biden Administration is probably less likely to resort to trade tariffs threat as the only tool of choice and lower risks of new trade tariff implementation should serve as a positive relief to AXJ FX, including RMB and those currencies that closely correlate with RMB such as SGD, MYR.

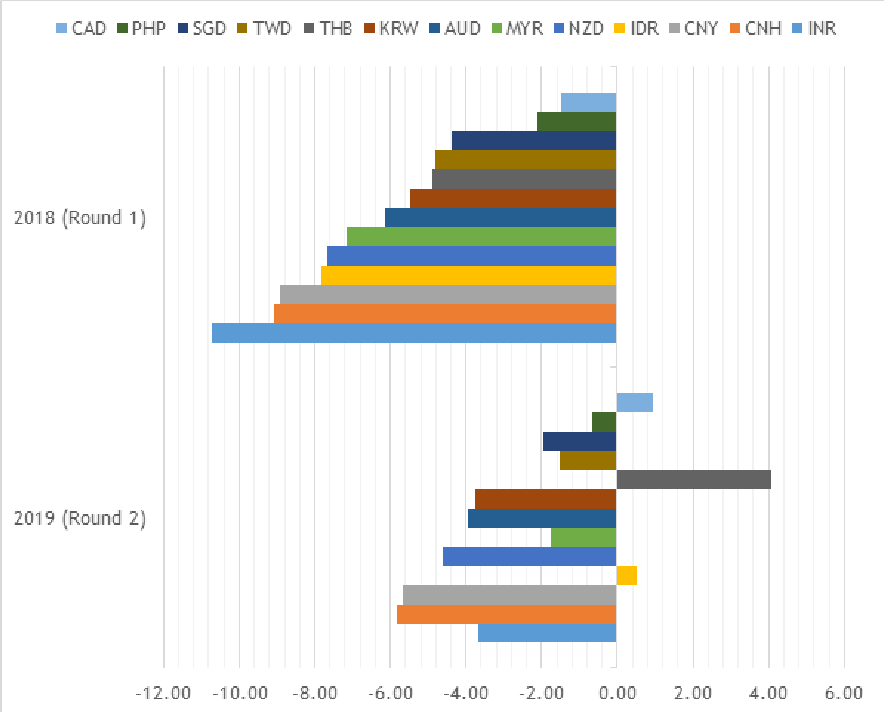
Source: Maybank FX Research & Strategy

In **scenario 1 - a status quo outcome - Trump is re-elected as President for a second term and GOP Republicans retain control of Senate**, we would expect policy continuity in terms of pushing for “America First” foreign policies, which is focused on American interests and national security. This will also pose as a big surprise to markets, given that polls are suggesting a scenario 4 – Biden win and Democratic sweep.

As a recap, the “America First” strategy started by withdrawing from Trans-Pacific Partnership (TPP) and making sure that any new trade deals are in the interests of American workers (in terms of bring back jobs, supporting US manufacturing sectors and increasing wages). Re-negotiation of NAFTA and repeated use of tariffs on imports from China, Europe were some examples over the past 4 years under Trump’s Presidency.

There is also preference for negotiating trade deals on bi-lateral approach (under Trump) as opposed to multi-lateral approach. Progress towards new trade deals with UK (post brexit with EU), phase-2 with Japan and possibly an extension of phase-1 trade deal with China could be on his second-term agenda. US-China relations will be of key focus, in relation to Asian FX. Under Trump, US-China relations have been strained on multiple fronts over trade, technology, national security issues, HK, South China Sea, accusations of Covid handling, etc. In particular US-China trade war when it first erupted in 2018 (we called it round 1) on tit-for-tat tariffs proved risk-off on sentiment and was negative on broad Asian-ex JPY (AXJ) currencies. CNH depreciated more than 10% at one point (vs. USD) between Apr and Nov 2018. We do note that the subsequent round of trade war in 2019 (we called it round 2) between May and Sep 2019 saw similar negative impact on AXJ FX but by a smaller magnitude.

Figure 6: AXJs Suffer on Tariff Trade War, Though Damage Was Lesser in 2019

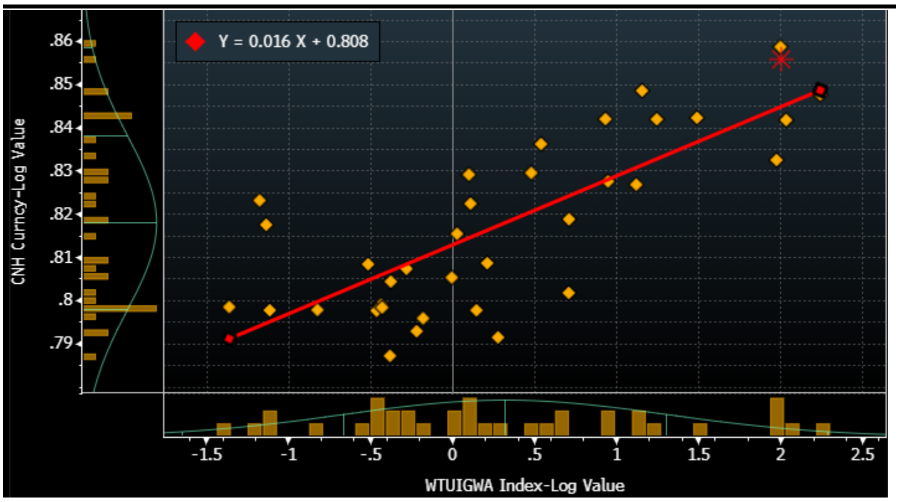


Source: Bloomberg, Maybank FX Research & Strategy

Note: Round 1 takes the currency performances between Apr-Nov 2018 (roughly the trough and peak of USDCNY). The start of the period also coincides with Trump’s first tariff threat on 3rd Apr 2018. Round 2 takes the currency performances between 4 May – 2 Sep 2019. The start of round 2 coincides with Trumps renewal of tariff threats.

In the current environment of Biden lead over Trump in polls and with world trade uncertainty index back to historical lows, we believe markets may not be fully pricing in the risks of trade policy uncertainty in our status quo scenario 1 (Trump re-elected and GOP republicans retains senate). And this implies that **AXJ FX could stand to succumb to depreciation pressure (vs. USD and safe haven proxy JPY)** if (i) Biden lead over Trump narrows in the lead up to election day; and/or (ii) election outcome surprise of scenario 1 catching markets off-guard (possibly resulting in deeper AXJ depreciation)

Figure 7: USDCNH Positively Correlates with World Trade Uncertainty



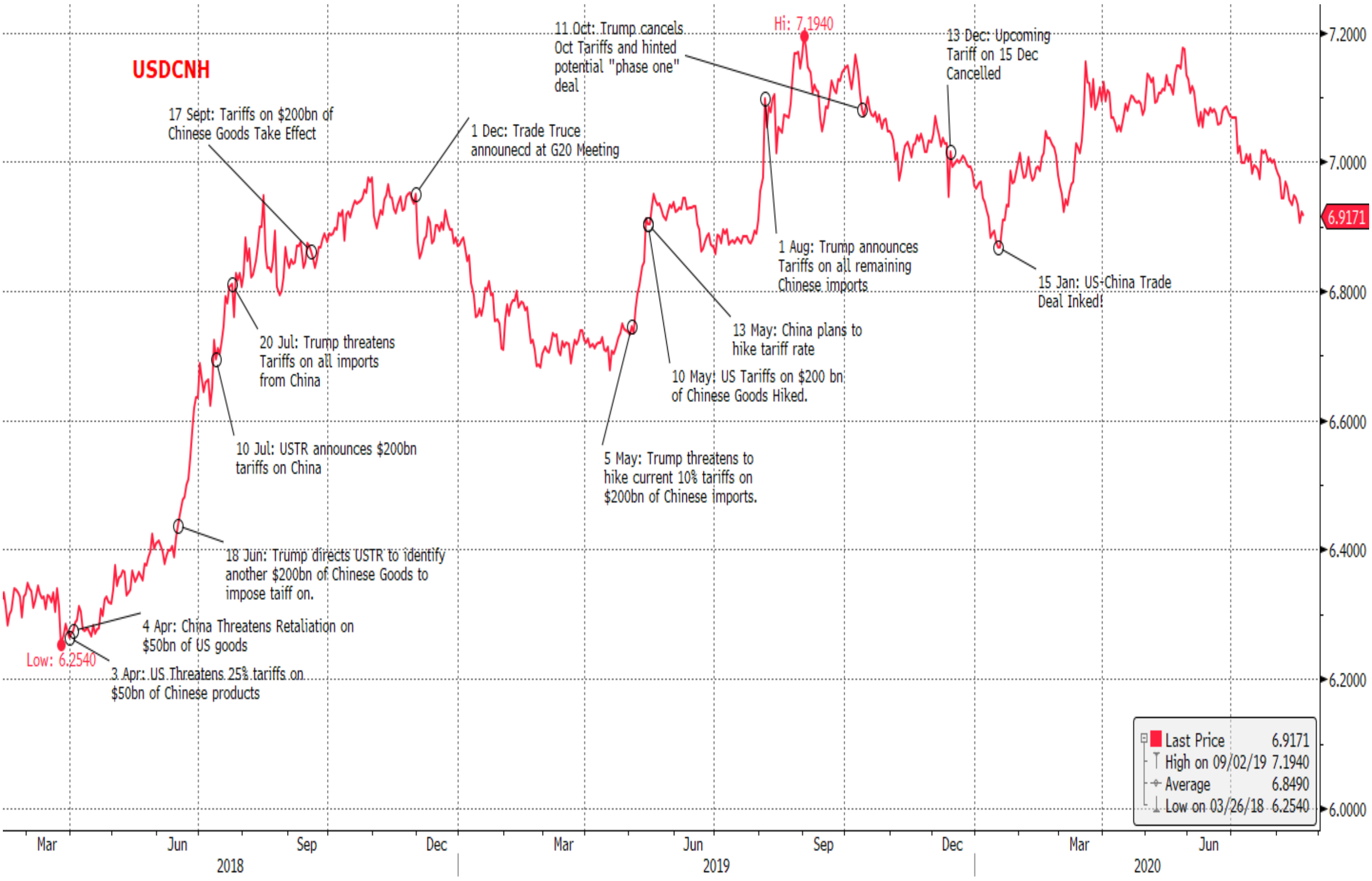
Source: Bloomberg, Maybank FX Research & Strategy
Note: OLS regression between USDCNH as Y-dependent variable and World Trade Uncertainty Index as X-independent variable, Quarterly log values over 2009 and 2020.

In terms of Trump's fiscal and tax policies, he has yet to share much on his second-term agenda. As of 6th Aug, Trump gave no clear replies when asked for the fourth time in six weeks what his second term agenda is. From what we understand from some media reports, TV interviews, payroll tax cuts and boosting domestic manufacturing are likely to be part of Trump's agenda. And that could at the margin, be positive for US markets. But we stress that the unexpected outcome of scenario 1 may have overriding negative implications for AXJ FX.

Scenario 2 of Democrats taking control of Senate and retaining the House but with a President of another party - Republican - is likely to be a legislative gridlock. No doubt Trump could still sign executive orders but political wrangling is likely to be a key feature and policy compromises between Trump Administration and Democratic Congress could be far and few in between given different policy bias between the parties. Recall how Democrats are proposing \$3tn - \$3.5tn fiscal stimulus this time round but Republicans were only after \$1tn stimulus and the impasse resulted in Trump signing 4 executive orders including expanded unemployment benefits (\$400 per week scaled down from \$600), temporary payroll tax deferral, provision of eviction protection and student relief. Slower and less economic support due to political wrangling could hamper post-Covid economic recovery momentum in US, pose spill-over risk to global growth. On net this could weigh on risk assets.

In terms of foreign and trade policies, it is likely Trump continues with prior policy practices, re-negotiating trade deals on bi-lateral approach instead of multi-lateral and relying on the use of signing executive orders, when needed. Most recently Trump signed executive orders ending HK's preferential trade status with US (14 Jul 2020), as well as signed executive orders on Bytedance divestment of TikTok and a similar order that bans transactions involving Wechat due to national security concerns (6 Aug). On China, he is likely to continue with prior practices. US-China tensions will continue to experience bouts of re-escalation due to threats ranging from trade, technology, sanctions and investment. On the latter, Trump Administration wants university endowments to divest from Chinese holdings as enhanced listing standards could lead to "wholesale de-listing of PRC firms from US exchanges by end-2021". Depreciation pressure on AXJs likely and could be amplified if risk assets come under pressure especially if slow US recovery momentum drags on global momentum.

Figure 8: CNH Weakens in Episodes of Tariff War



Source: Bloomberg, Maybank FX Research & Strategy

In **scenario 3 where Biden wins Presidency and Congress remains status quo - split (i.e. GOP Republicans retains Senate and Democrats retains HoRs),** we expect Biden Administration to attempt to push through with its Covid stimulus package and pursue his proposals to increase taxes and expand healthcare coverage. But a split congress could mean that Biden's plans may have to be deferred till mid-term elections after 2022. In the interim, he will have to work with a split congress to support his proposals but is likely to face challenges. A likely outcome would be curtailed near-term stimulus spending, difficulty pushing through tax hikes and reliance on executive orders to implement policies. Difficulty in pushing through tax increases may be positive on sentiments but curtailed stimulus spending may derail economic recovery momentum. On net, this may imply some degree of market neutral.

On foreign policies, trade matters, Biden is likely to adopt a different approach from Trump (more strategic, less confrontational against China) and could look for broad coalition of allies and increased reliance on, or cooperation with existing international institutions. Multi-lateral approach will be preferred over bilateral when it comes to re-negotiating trade agreements. Biden penned an article on The Foreign Affairs (Mar/Apr 2020 issue) – on why America must lead again. He said that *"Trump has designated imports from the US' closest allies – from Canada to EU – as national security threats in order to impose damaging and reckless tariffs. By cutting us off from the economic clout of our partners, Trump has kneecapped our country's capacity to take on the real economic threat."* He went on to say that *"on its own, the US represents about 1 quarter of global GDP. When we join together with fellow democracies, our strength more than doubles. China cannot afford to ignore more than half the global economy. That gives us substantial leverage to shape the riles of the road on everything from environment to trade, technology and transparency, so they continue to reflect democratic interests and values".*

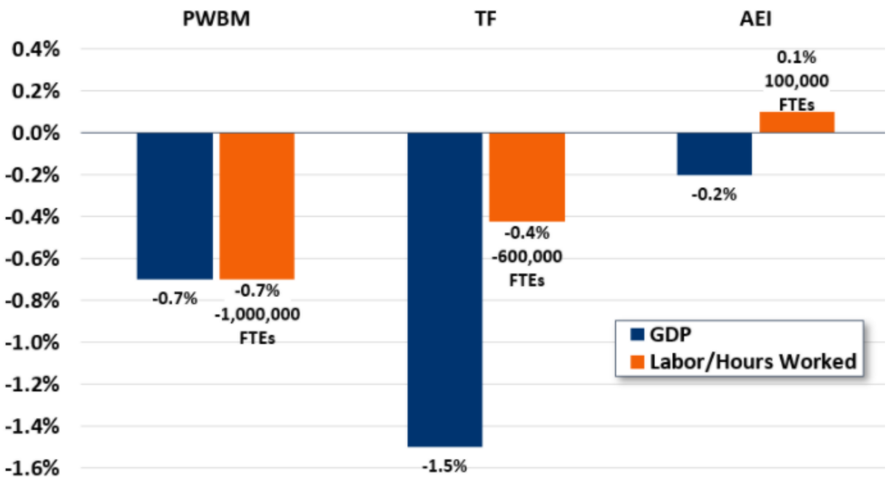
On net we should expect relative predictability in US foreign policy. On US-China relations, we expect a more conciliatory tone with China in terms of international cooperation. The use of tariff threat on China is also likely to be more restrained, relative to Trump's days. China containment could resemble former President Obama's pragmatic, rational approach. From a markets point of view, Biden could be perceived as a slight positive for AXJ FX and a net positive for allies' FX such as CAD and EUR (as some of the earlier tensions caused by Trump could be reversed).

Scenario 4 of Biden winning Presidency and the Democrats taking over Senate (i.e. a Democratic clean sweep assuming Democrats retains HoRs) is current expectations of consensus polling (as of 18 Aug). This scenario allows for Biden to implement wide-ranging policies including Covid response fiscal stimulus, expand healthcare coverage (i.e. bolstering affordable Care Act) and pursuing tax increases with greater ease. These policies are likely to be **mixed for sentiments (or market neutral to slight negative) from a markets perspective and possibly an overall negative for USD (due to fiscal expansion).**

On market-negatives, Biden has called for rolling back on the Tax Cuts and Jobs Act – raising marginal tax rate to 39.6% (from 37%) on the highest income earners (incomes exceeding $400,000) while those with household income exceeding $1mio could see long term capital gains tax rise to 39.6%, from 20%. According to Committee for a Responsible Federal Budget (based on analyses from Penn Wharton Budget Model, Tax Foundation, American Enterprise Institute), Biden's tax plan will raise revenue between $3.5tn and $3.67tn over 10 years if enacted in full starting 2021 (about 1.3% to 1.4% of GDP) but the new tax increases would be borne nearly in full by very high income households and would likely slow the pace of economic growth modestly as Biden's plan would reduce incentives to work, save and invest due to its increases in effective marginal tax rates. He also proposed increasing corporate tax rate to 28%, following Republican cuts in 2017 to 21% (from 35%).

However, there are also market-positives. Biden is proposing a $700bn domestic spending plan ("buy American") to revitalize American manufacturing and business. His infrastructure spending plan proposes a $400bn federal investment in "products and materials our country needs to modernize our infrastructure, to replenish stockpiles and to enhance national security" as well as another $300bn investment over 4 years for research and development. This aims to create 5mio jobs. So on net, we see tax hikes and spending hike proposals as market-neutral to negative for sentiment.

Figure 9: Estimates of Long Term Economic Effects of Biden Tax Plan (% Change from baseline)



Source: Penn Wharton Budget Model (PWBM), Tax Foundation (TF), American Enterprise Institute (AEI), Committee for a Responsible Federal Budget Calculations, Maybank FX Research & Strategy

On overall fiscal spending, **Biden wants the Federal government to spend close to $7tn more over the next decade** on issues pertaining to "buy American" plan ($700bn), housing ($640bn), healthcare ($750bn), higher education ($750bn), child and elder care ($775bn), infrastructure ($1.3tn) and climate change ($2tn). He intends to pay for this with about $4tn in tax increases on wealthy Americans, corporations and investments. According to the Treasury Department in the 10 months-to-date, budget deficit has risen to a record high of $2.81tn and is projected to hit $3.7tn for fiscal year 2020 (according to projection from Congressional Budget Office). This is much higher than the record deficit set in 2009 at $1.41tn. We have shown that **increase in fiscal deficit, alongside current account deficit - deterioration in twin deficits typically accelerates USD sell-off**.

On the topic of US-China relations, we expect a Biden Presidency to take on a different approach – less confrontational, more strategic - on China, as opposed to Trump. We also believe **Biden Administration is less likely to resort to trade tariffs threat as the only tool of choice and this (lower risk of new trade tariffs implementation) in itself should serve as a positive relief to AXJ FX, including RMB and those currencies that closely correlate with RMB.**

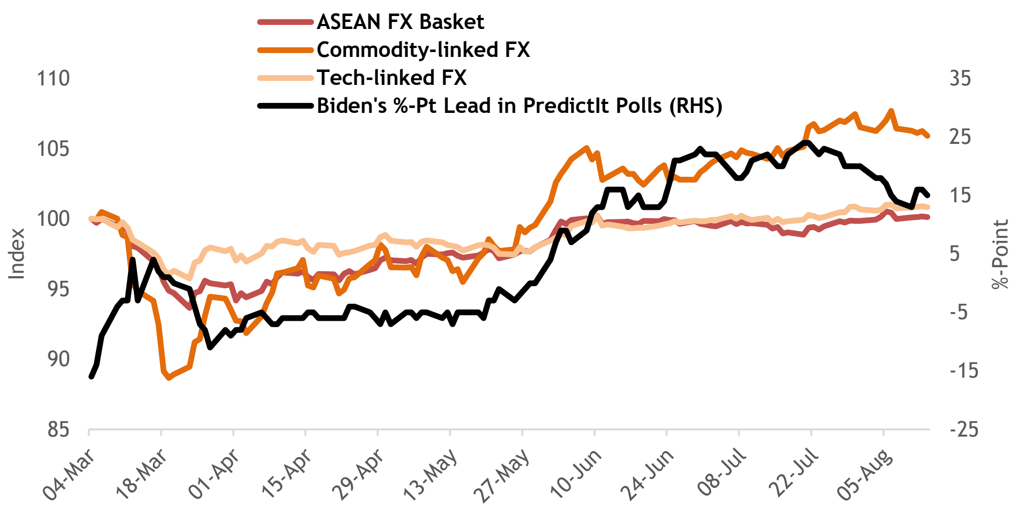
But that is not to say that US-China relationship will surely improve in a fundamental way with Biden as President. US will still seek to contain the rise of China, maintain its competitive stances on wide-ranging issues including technology, trade (via subsidies, tax incentives, etc.). In Biden article on why America must lead again, he said "*the US does need to get tough with China. If China has its way, it will keep robbing US and American companies of their technology and intellectual property… the most effective way to meet that challenge is to build a united front of US allies and partners to confront China's abusive behaviors and human rights violations, even as we seek to cooperate with Beijing on issues where our interests converge, such as climate change, nonproliferation and global health security*".

A Biden Lead—Modestly Positive for ASEAN FX?

The above scenarios set out our assessment of market biases under different US election outcomes, and **a key theme is that for Asia or ASEAN risk assets and currencies, a Biden presidency may be more beneficial for sentiments relative to a Trump presidency**. In this section, we attempt to evaluate this in a quantitative manner.

But looking at recent data, a confluence of Covid, macro and policy circumstances have led currencies (or most assets for that matter) to run in, more or less, a single direction since late March. Add to that the observation that Biden's lead in polls over Trump happen to be widening steadily over the same period, and it is hard to argue causality when the same set of broad market circumstances are driving shifts in FX trajectories.

Figure 10: Recoveries in Regional FX (vs. USD) Coincide with Period of Biden Gaining in Lead



Source: Bloomberg, Maybank FX Research & Strategy

Note: FX Baskets are indexed to 100 on 4 Mar. ASEAN FX basket refers to equal-weighted SGD, MYR, THB, IDR, PHP (vs. USD) series. Commodity-linked FX refers to AUD and NZD. Tech-linked FX refers to SGD, KRW, TWD.

Taking the above into consideration, we attempt to distill any real explanatory impact of Biden's increasing lead over Trump on FX moves via a two-step approach.

First, we create a proxy for broad market risk sentiments using *Principal Component Analysis* (PCA) across 27 data series, incorporating most equity and commodity price indices. Simply put, PCA is just a technique to extract/compress common information from multiple series into fewer new series. The first principal component, which contains around three-quarters of information embodied by moves in the 27 individual series, will be used as our "risk sentiment proxy", and is as shown in the chart below.

Figure 11: Risk Sentiment Proxy Series Captures Main Shifts in Market Mood

Source: Bloomberg, Maybank FX Research & Strategy

As expected, results show that risk sentiments have been on a broad recovery trajectory since late-March.

In step two, we regress returns in custom FX baskets vs. Biden's lead over Trump in polls, while controlling for (i) broad dollar strength (USD NEER) and (ii) cyclical market sentiments (our derived risk sentiment proxy series). T-statistics from the various regressions for both Biden's lead and our risk proxy series are shown in the table below.

The larger the t-statistic (in magnitude), the more likely the factor in question (Biden lead, broad market risk sentiments) is to be significant to moves in the particular FX proxy basket. E.g., a high t-stat (magnitude 8.5) for "broad market risk factors" in the regression for commodity-linked FX returns suggests that AUD and NZD tend to be the most sensitive to the recovery in market sentiments post-Mar (coming out of lockdowns, vaccine developments, policy aid etc.).

Table 3: Higher Biden Win Chances Benefits ASEAN and Commodity FX Modestly

FX Proxy Baskets	T-stat - Biden's Lead in Polls	T-stat - Broad Market Risk Factors
ASEAN (SGD, MYR, IDR, THB, PHP)	**3.2**	**5.1**
Commodity (AUD, NZD)	**2.6**	**8.5**
TECH (SGD, KRW, TWD)	1.4	**6.3**
OIL (CAD, MYR)	-0.2	**6.9**
CNY	0.9	**3.6**
Haven (JPY, CHF)	-1.2	**-4.5**

Source: Bloomberg, PredictIt, Maybank FX Research & Strategy
Note: Sample is from Mar to mid-Aug. 5-day returns/changes used in regression. T-stats with magnitude >2 (bold) are considered relatively significant.

From the results, **the widening of Biden's lead over Trump appears to be modestly positive for ASEAN and commodity FX sentiments to some extent.** This could be due to expectations for more stable US policy stances on the international stage benefitting trade and investment dependent economies regionally. As mentioned earlier, if Biden is elected, we also note a higher likelihood of the US re-engaging in the Trans-Pacific Partnership (TPP; now Comprehensive and Progressive Agreement for Trans-Pacific Partnership, CPTPP), which could be positive for some ASEAN members (Singapore, Malaysia, Vietnam), as well as Australia and New Zealand. Coincidentally, Singapore, Malaysia and Vietnam also happen to be on the last version of the US "monitoring list" of trading partners whose "currency practices merit close attention" released in Jan 2020. Biden arguably has a much lower tendency to resort to criticism of, or take actions against, FX intervention by countries in the list vs. Trump.

We note that significance of a Biden win to oil-linked FX is less discernible. Biden's agenda does include stricter oil exploration permits, and new protections for the Arctic National Wildlife Refuge and other areas that Trump has sought to open up for O&G development, which could impact US O&G supplies in the longer run. But he has also resisted a push by his party's liberal wing to impose a nationwide ban on fracking. On net, with other more pressing drivers (OPEC+ decisions etc.) driving near-term oil price trajectory, the relevance of a Biden win to oil-linked FX could be more muted in the interim.

Interestingly, higher chance of a Biden win does not seem to be a significant driver for CNY moves in the last several months. This ties in somewhat with our earlier assessment that while Biden might strike an outwardly reconciliatory tone with China in terms of international cooperation, his policies are likely to maintain competitive stances (vs. China) in key areas of tech and trade, and US-China relations may not improve in a fundamental manner.

The natural caveat here is that across all FX baskets, any explanatory power the Biden lead might have for FX pales in comparison to broader risk-on/off shifts in markets (Covid & other factors) since March.

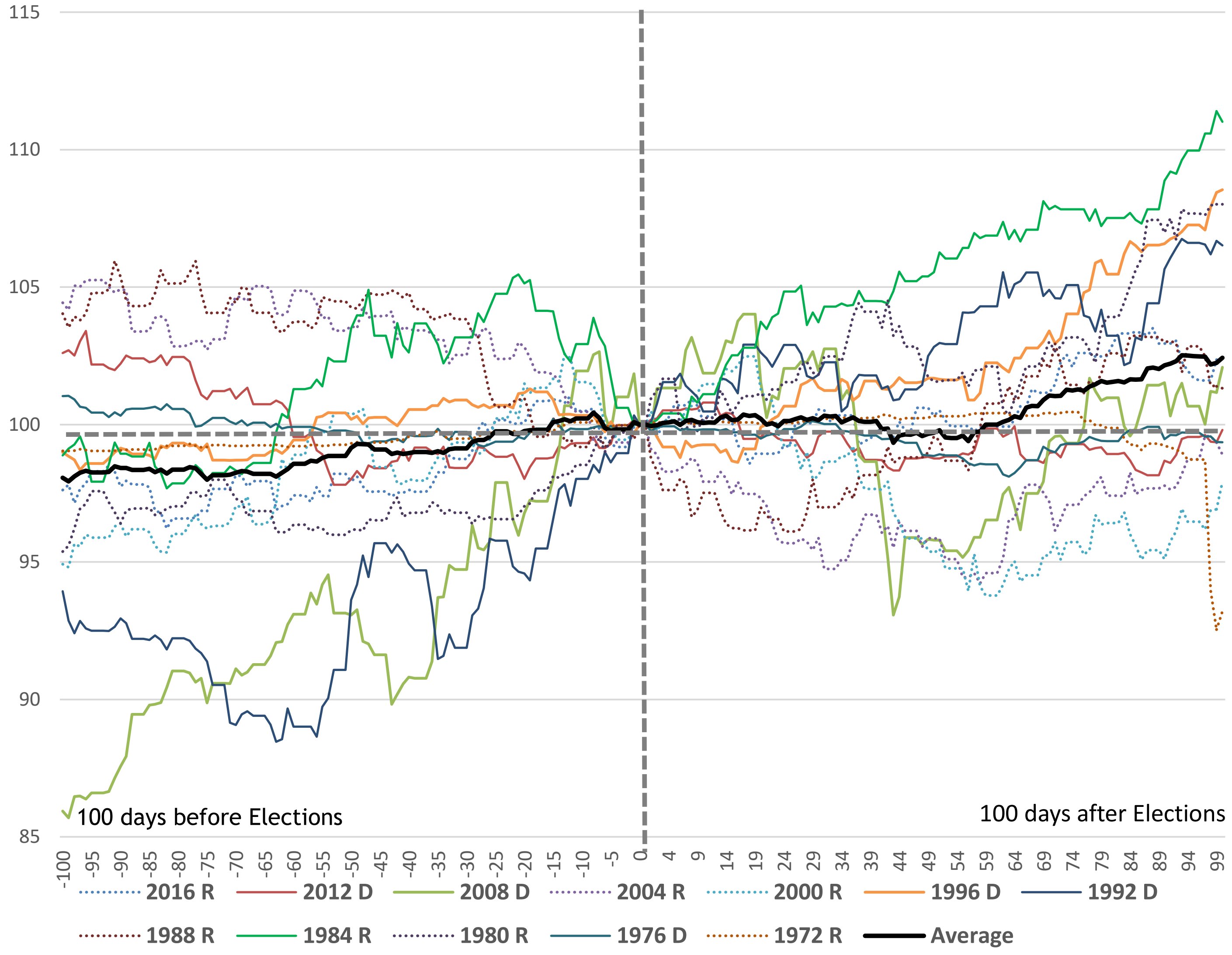
Looking Back at History: FX Behavior Around Election Periods

While the circumstances surrounding this election (pandemic, fragile macro outlook) are very different vs. past election episodes, and history may arguably not repeat itself this time, we should still not ignore any FX lessons which history has to teach us.

First, dollar behavior. We look at USD performance 100 days before and after elections as the US elections come into more focus within this period and markets are thus, more sensitive to the developments on that front.

For the past 50 years, the US election periods have been net positive for the USD. The DXY index appreciated an average of 2.4% in the 100 days after the elections, possibly buoyed by the promise of growth-positive policies that the newly elected or re-elected Presidents campaigned on and tend to implement first. Out of the past 12 elections, the greenback rose in 7 instances 100 days after the event and 8 instances 100 days before the event. Taking into account the full 200 days observed, the DXY index clocked an average of 4.36% gains during elections for the past 50 years.

Figure 12: DXY Typically Strengthens Into Election Period and Beyond

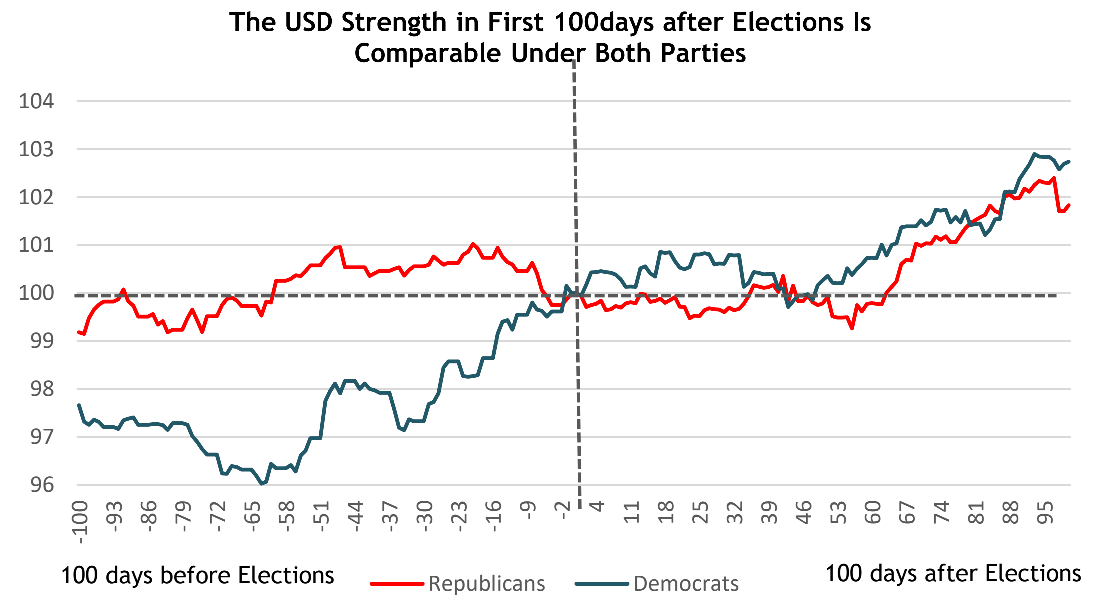


Source: Bloomberg, Maybank FX Research & Strategy

Note: The DXY index is taken to be 100 on the day of election.

The tendency for the USD to rise actually holds true regardless of the allegiance of the newly elected President. The strength of the DXY index in the early days of the Presidencies were comparable for both parties and we allude it to the executive orders/policies that Presidents tend to issue that could be growth-positive such as President Obama's (Democratic) healthcare bill for children and the American Recovery and Reinvestment Act. Within the first 100 days of Trump's term (Republican), he also introduced an outline of tax reform with the aim of delivering deep tax cuts. Note that both started their respective terms with full control of Congress.

Figure 13: USD Tends to Begin Most Presidencies on a Firm Foothold

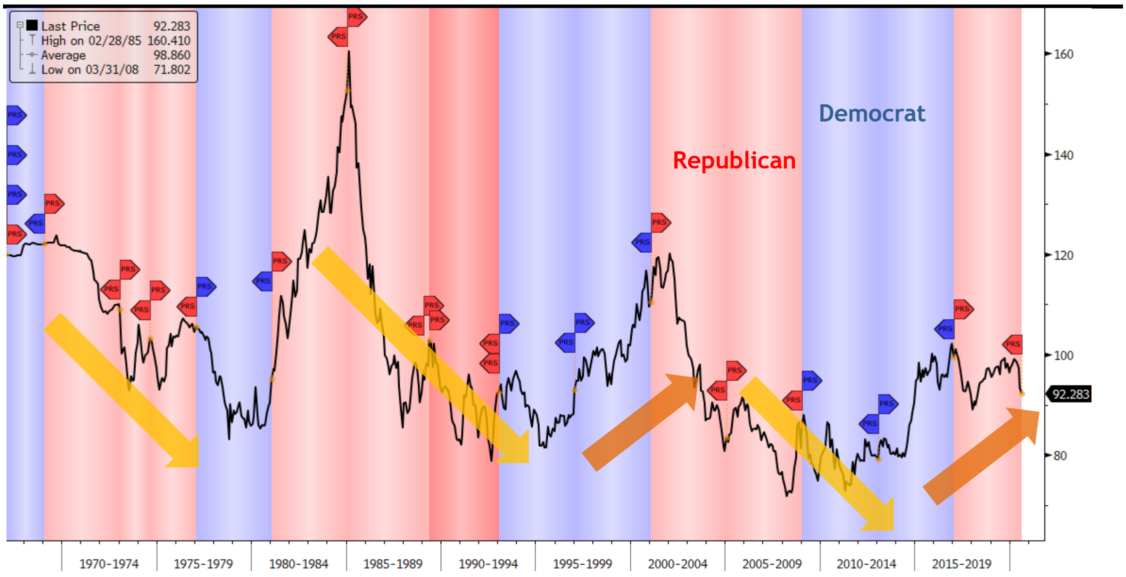


Source: Bloomberg, Maybank FX Research & Strategy

Note: The DXY index is taken to be 100 on the day of election.

For a longer-term view, Democrats and Republicans rule do not have a consistent effect on the USD. However, periods of Republican Presidencies (Red) tend to see larger declines in the USD while USD strength dominates those of the Democrats (Blue).

Figure 14: DXY Biases in Republican Vs. Democrat Presidencies

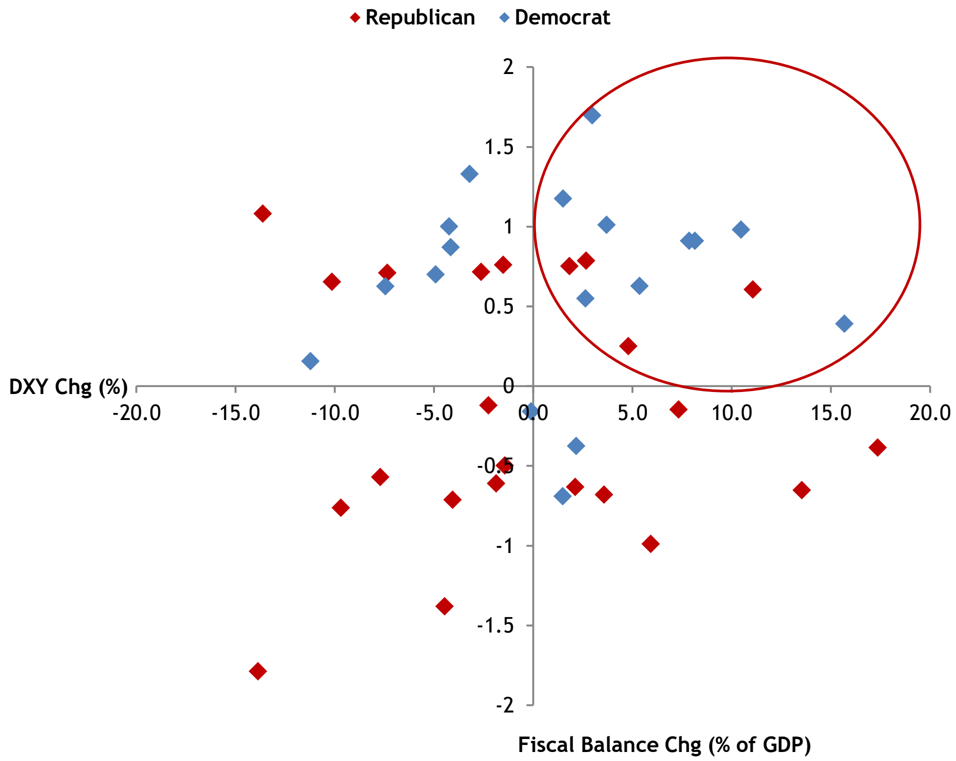


Source: Bloomberg, Maybank FX Research & Strategy

Stronger Fiscal Management Could See Stronger USD

We suspect that a key reason could be the fiscal management of each parties. The scatterplot below reiterates our assessment that while democrats have often been seen as fiscal negative as they promote policies that are interventionist, data shows that they have actually been better for fiscal balances (i.e., blue dots mostly above horizontal axis). On average, years under a Democrat President have seen a 0.44%-pt improvement in fiscal balance (over prior year) while years under a Republican President have seen a -0.42%-pt deterioration.

Figure 15: On Average, Democrat Presidents Are Associated With Better Fiscal Balance & USD Performance (Dots Show Average Annual Changes from 1972 to 2019)



Source: Bloomberg, Maybank FX Research & Strategy

Consistent with this sense of greater fiscal discipline, Democrats have on average been better for the dollar as well. Democrat years have seen the USD (proxied by the DXY index) strengthen by around 1.7% on average, while Republican years have seen a -1.1% decline. Table 4 includes more policy details of different Presidencies along with the respective USD behaviour.

Table 4: Expansionary/ Contractionary Fiscal Policies' Impact on USD

Fiscal Expansion	1986 - 1989	Reagan's tax reform saw budget deficit narrowing as his supply-side (Reaganomics) reform boosted tax revenues	Dollar ↓
	2001 - 2007	After the dot.com bubble, defence spending substantially increased following the 9/11 attack, while Bush's tax cut saw tax revenue decreasing, where budget deficit increased	
	2007 - 2009	Budget deficit increase was largely due to the great banking bail-out from the Financial Crisis	
Fiscal Contraction	1992 - 2001	Clinton's tax hike narrowed the budget deficit (even into surplus in 1998)	Dollar ↑
	2012 - 2016	American Taxpayer Relief act narrowed the fiscal deficit	

Source: Maybank FX Research & Strategy

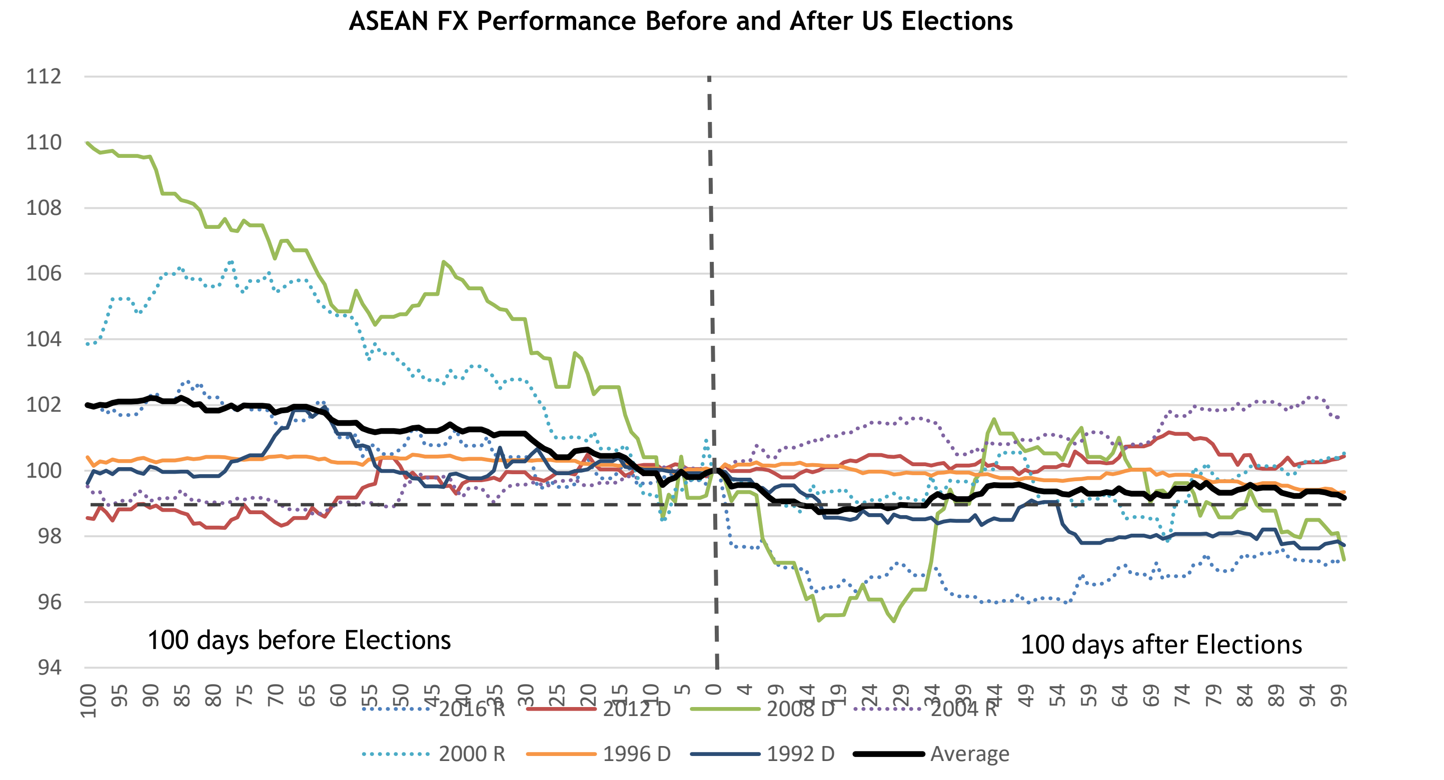
Impact of US Elections on ASEAN FX

When it comes to the impact of US elections on ASEAN FX, we also looked at the ASEAN FX performance (against the USD) in the 100 days before the elections and 100 days after. ASEAN currencies have a shorter history and thus, the complete ASEAN data set (consisting of SGD, THB, MYR, IDR and PHP) was only available from the election year of 1992.

The ASEAN FX index used in our charts henceforth is an equally weighted average of all ASEAN FX indices which were in turn indexed by taking their respective currency levels (vs. base USD) on election day as 100.

In the past 30 years, ASEAN FX broadly tends to weaken in the lead up to US Election day and are likely to remain on the backfoot after the event.

Figure 16: ASEAN FX Tends to Tread Water into US Elections



Source: Bloomberg, Maybank FX Research & Strategy

Note: R denotes a Republican President Win that year while D denotes a Democratic President Win.

A Successful Incumbent Usually Brings Policy Certainty, Anchors ASEAN FX

But delving into subsets of events, we found that ASEAN FX actually tends to see modest appreciation in the lead-up to election day when the current President successfully secures a second term. This happened in the years 1996, 2004 and 2012 as indicated in the left chart below.

Conversely, when the incumbent seeks to be re-elected and fails, ASEAN FX would weaken in the lead up to election day (1992) with the exception of the THB. ASEAN FX also behaved in a similar way when the incumbent did not fight for re-election in 2000, 2008, 2016 due to reasons such as the 2-term limit. **The weakness in ASEAN FX may be a reflection of US policy uncertainty as the world is faced with a new US President.**

Overall, a successful re-election by an incumbent President tends to bring more policy certainty including in foreign relations, and ASEAN FX were thus more stable compared to scenarios where the US elects a new President. In particular, risk-sensitive IDR seems to be more penalized vs. its peers for the 100 days in the lead up to Election day when the President is about to change.

Figure 17A: Currency Changes (vs. USD) 100 days *Before* US Elections

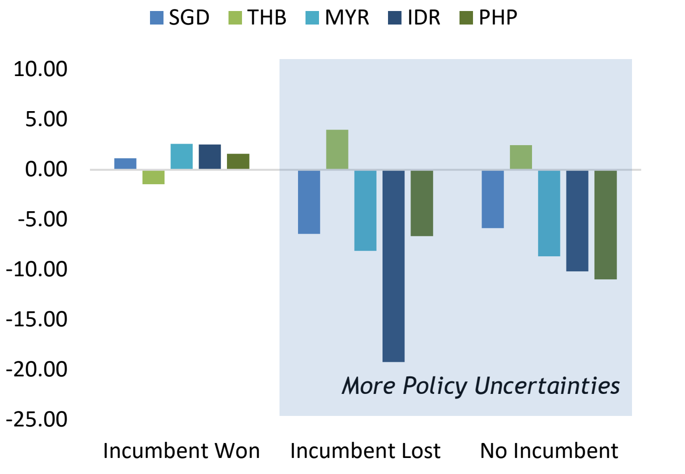
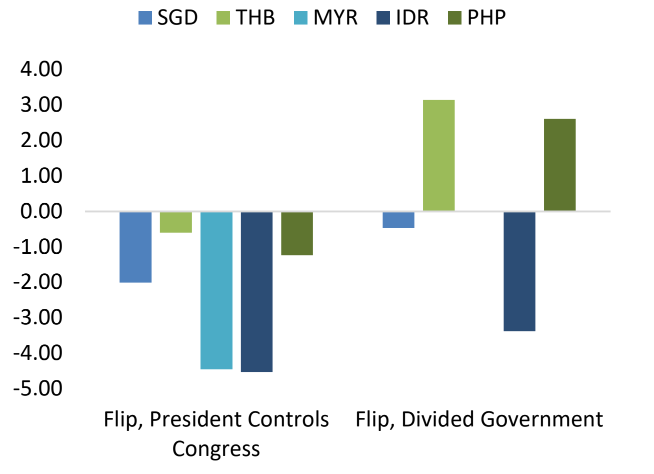


Figure 17B: Currency Changes (vs. USD) 100 days *After* US Elections



Source: Bloomberg, Maybank FX Research & Strategy

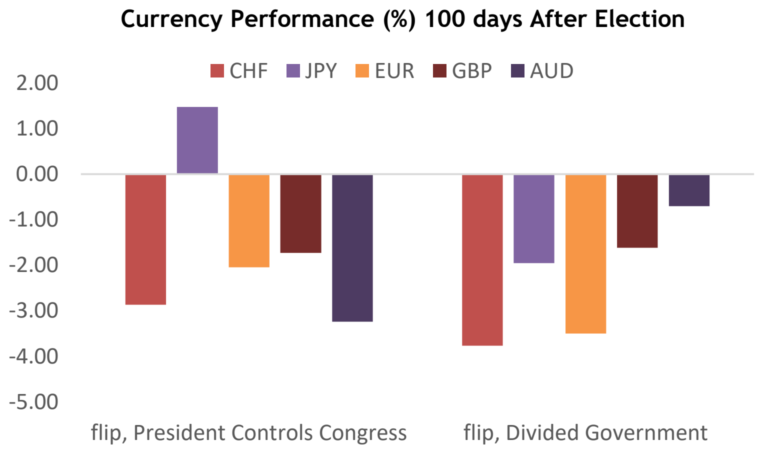
Note: "flip" describes the case where the new President is from a different party vs. the former President.

Based on the chart on the right, ASEAN currencies also behaved differently when the new President is able to gain control of the Congress vs. a new President who faces a divided government.

A New President with Control of Congress Could Weaken ASEAN FX More

We found that when the new President gains full control of Congress, ASEAN FX weakens across the board. This scenario happened in 1992, 2008 and 2016. This could be due to the potential for strong policy volatility, given that likelihood of passing new policy changes is higher. When the flip happens without a full control of both chambers of Congress, ASEAN currencies may see a more uneven performance. This happened in the year 2000. Due to the limited availability of data for this scenario, we also looked into some G7 currencies that have longer historical prices. Based on data that dates back to 1976, most G7 currencies (CHF, JPY, EUR, GBP, AUD) weaken in the flip scenario but **only JPY strengthened** when the new President controls both chambers of Congress (1976, 1992, 2008, 2016), which underscores the demand for safe haven in light of the potential for disruptive policy changes.

Figure 18: JPY Strengthens when A New President Has Full Control of Congress



Source: Bloomberg, Maybank FX Research & Strategy

Concluding Remarks…

Current FX markets (AXJs) movements are consistent with poll results of Biden leading over Trump and expectations for Democrats to take over Senate, alongside low trade uncertainty index readings—a scenario #4 outcome (current base case scenario). Such an outcome could imply a (1) softer USD broadly (on expectations of large fiscal spending contributing to deterioration in deficits); (2) market sentiment could be neutral to slight negative (on tax increases but modestly mitigated by spending proposals) and (3) positive relief for AXJs including RMB (on expectations for less confrontational approach by Biden).

On (3), to more clearly verify linkages between the US elections and regional currencies' performance, we conduct a quantitative analysis using polling stats, USD NEER and a house-constructed risk sentiment indicator. Our analysis shows that the widening of Biden's lead over Trump is indeed statistically significant in contributing to ASEAN and commodity currencies' recovery since March, although the explanatory power of this lead pales in comparison to broader risk-on/off shifts in markets (Covid & other factors). This gives us more confidence that markets could indeed be gradually pricing in higher expectations for more stable US policy stances on the international stage, lower chance for tariff threats, as well as a higher likelihood of the US re-engaging in the TPP (now CPTPP), on a Biden win. Going forward, barring any serious re-emergence of COVID-19 outbreaks globally or any unknown negative shocks, ASEAN and commodity-linked FX could continue to benefit from a Biden win (if it comes to pass), as these baskets are typical proxy plays for growth rebound, which a Biden presidency could help anchor. Our current year-end forecasts for USDSGD, USDMYR, USDIDR at 1.35, 4.15, 14,200, respectively, inherently prices in a Biden win (scenarios #3 or #4), i.e., assumes no derailment of cautious recovery sentiments.

We make two additional important caveats.

First, at this point, markets are probably not as positioned for a surprise scenario 1 (status quo with Trump win) – likely a negative for AXJs, including RMB (fears of re-escalation in US-China tensions, use of tariff threats, etc.). This warrants caution as political developments can be fluid and prediction markets can fail (as 2016 US Presidential Elections and EU Referendum had shown). The occurrence of scenario #1 could derail current appreciation momentum in AXJs. Among ASEAN FX, IDR could be particularly susceptible to sentiment shocks at this stage, given its increasing tight fiscal purse-strings, inability to taper domestic Covid-19 contagion, and mixed showing in external portfolio flows.

Second, we remain mindful of lessons from history, even as we understand that circumstances are largely different this time round. Looking at US elections over the past few decades, we note the dollar actually performed well pre- and post-elections (-/+100 days), whereas ASEAN currencies tend to be more cautious. In particular, higher chances of a change in the sitting president tends to be consistent with softer ASEAN FX (except THB) on net in the lead-up to the elections. If the president controls Congress post-elections, markets also tend to see episodes of weaker ASEAN FX performance as well. We think that such underperformance could be due to concerns over changes in US' foreign policy stance, or worries over sweeping policy changes. Bearing this in mind, market's familiarity with Biden in his former role as a former Vice President to Obama vs. Trump's belligerent approach on China and spending could render this situation unique. Our earlier assessment of a Biden win being positive for regional FX should remain intact on net and our forecast levels (in Table 5) assume that scenario #3 and #4 are largely priced.

Table 5: FX Forecasts

	End Q3-20	End Q4-20	End Q1-21	End Q2-21
USD/JPY	103.00	103.00	102.00	102.00
AUD/USD	0.7000	0.7200	0.7300	0.7400
NZD/USD	0.6500	0.6400	0.6600	0.6700
USD/SGD	1.3700	1.3500	1.3400	1.3300
USD/MYR	4.2300	4.1500	4.1300	4.1000
USD/IDR	14800	14200	13900	13700
USD/THB	31.50	31.20	30.80	30.60
USD/PHP	48.50	48.00	47.50	47.50
USD/CNY	7.05	7.00	6.95	6.90

Source: Maybank FX Research & Strategy

Note: These forecasts are meant to be indicative of FX trends and not meant to be point forecasts. Projections are as of 21 Aug 2020.

DISCLAIMER

Published by:

Maybank

Malayan Banking Berhad
(Incorporated in Malaysia)

Saktiandi Supaat	Christopher Wong	Fiona Lim	Yanxi Tan
Head, FX Research	Senior FX Strategist	Senior FX Strategist	FX Strategist
saktiandi@maybank.com.sg	wongkl@maybank.com.sg	Fionalim@maybank.com.sg	tanyx@maybank.com.sg
(+65) 63201379	(+65) 63201347	(+65) 63201374	(+65) 63201378