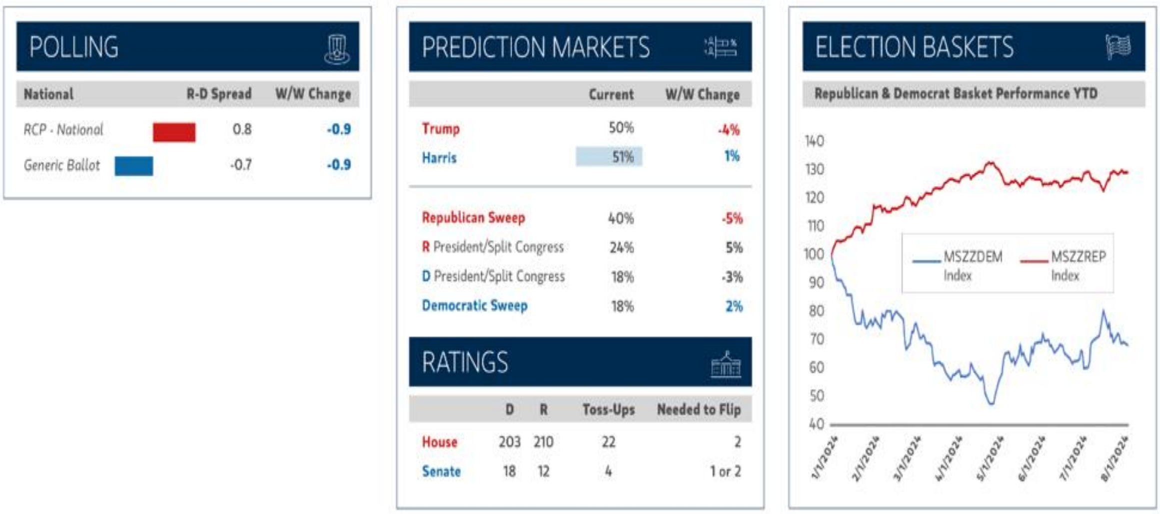
John F. Kennedy: “The margin is narrow, but the responsibility is clear. Elections can be as unpredictable as a coin toss, but they shape our future.”

US Presidential Election 2024 has been full of twists and turns. It started on June 27 with President Biden’s unexpected weak debate performance, which hurt him in the polls and brought a crescendo of calls from Democrats for a change at the top of the tickets. Then came the assassination attempt on former President Trump on July 13, where he was shot in the ear during a campaign rally. The fact that the previous assassination attempt dated back to 1981, when President Ronald Reagan was shot and survived the attack, just proved that the possibility of this incident happening in today’s time is unthinkable. Then came a nearly unprecedented event on July 21, where President Joe Biden eligible for another term, announced that he would not seek re-election. Before this, the last US president to make a similar decision was Lyndon B. Johnson in 1968, largely due to the ongoing Vietnam war and concerns about his health. Then Vice President Harris quickly declared her candidacy and eventually secured the Democratic presidential nomination on August 5. This historic moment made her the first Black women and first Asian American to lead a major party ticket in the US.

Following these events, the election outcome has largely reset to pre-debate readings and is now back to a coin toss probability. After surviving the assassination, Former President Trump’s win probability reached a high of nearly 75%, while the probability of a republican sweep touched a high of over 50%. In national polls, Harris is either slightly behind or ahead of Trump. Though fewer swing state polls are available, they similarly show Harris in a competitive position, with only a slight deficit in key swing states.

Chart 1 – Election Dashboard



Source: FiveThirtyEight, RealClearPolitics, Polymarket, PredictIt, Cook Political Report, Morgan Stanley Research.

Despite the change at the top of the Democratic ticket, there should not be significant changes on policy paths given that 1) VP Harris's policy positions are similar to President Biden's key issues of import to markets, and 2) the details of key legislative policies in a Democratic win scenario will likely be shaped by the party's elected officials overalls. As of the latest updates, Democratic nominee VP Harris' detailed agenda is not yet publicly released. However, we would expect VP Harris to roll forward many of the Biden administration's policies should she win the election. While Democratic win scenarios mostly represent policy continuity, Republican win scenarios yield greater potential change on policies such as Tariffs and immigration via executive action and, unlike in 2017, they may be sequenced to precede, rather than follow, fiscal expansion via tax policy.

Domestic Tax Policy

The Tax Cuts and Jobs Act (TCJA), implemented in 2018 by former President Trump, is set to expire at the end of 2025. In the event of a Harris win, we would expect a partial extension of the TCJA, even though as a presidential candidate, VP Harris supported a repeal of the legislation and higher corporate rate. TCJA's tax cuts for large corporations would most likely be repealed, while allowing tax cuts to expire only for the highest income 1 percent of households. Like President Biden, she has vowed to protect households making USD 400,000 or less from tax hike in 2025.

Sectors most negatively exposed to higher rate changes include domestic-focused and consumer-oriented businesses, such as retail, energy, transportation, regional financial services and health care services. Sectors negatively exposed to increased minimum taxes are primarily large multinationals, including pharma, tech, and industrials. The deficit impact would be minimal given a unified Democratic scenario, which Morgan Stanley projected a national deficit of USD 600 billion for the next 10 years.

In the event of a Trump win, it is likely that he would seek to extend and possibly expand the TCJA. US equity market would likely see gain given the stimulation of economic growth at the expense of worsening the national deficits. The outperformance and rotation into US small cap validate the market prediction when odds of a Trump win were at its peak. Sectors such as financials and telecommunication would perform well with deregulation. Higher deficits would result in higher long-term interest rate without considering other factors such as business cycle etc. As a result, the impact on Fixed Income is less clear.

Chart 2 - Tax Scenarios by Outcome

Outcome		Unified Democratic	Divided Government	Thin Republican Sweep	Republican Sweep - Larger Margin
Summary		Narrow extension of core business & individual provisions; revenue raisers to offset extensions	Narrow extension of core business & individual provisions	Narrower extension of most TCJA provisions	Closest to original TCJA extension
Plausible Key Policies	Child Tax Credit Enhancement	✓✓	✓	✓	✓
	Corporate Rate increase	✓✓	✓	✓	✓
	Extensions of Key Business Provisions	✓	✓✓	✓✓	✓✓✓
	Revenue Raisers	✓			
	Potential SALT Cap				✓
	Limited Extension of Individual Cuts		✓	✓	
Key Sector Impact		• Technology, Telecommunications, Health Care, Industrials most exposed to TCJA expiration • Telecommunications, Banks & Financial Services, Health Care Services, Consumer Services & Retail most exposed to higher corporate rate • Pharmaceuticals, Tech Hardware, Software & Consumer Brands most exposed to potential minimum taxes	• Telecommunications, Banks & Financial Services, Health Care Services, Consumer Services & Retail most exposed to higher corporate rate	• Telecommunications, Banks & Financial Services, Health Care Services, Consumer Services & Retail most exposed to higher corporate rate	• Telecommunications, Banks & Financial Services, Health Care Services, Consumer Services & Retail most exposed to higher corporate rate
Deficit Impact (10y)		$600 billion	$1.1 trillion	$1.1 trillion	$1.6 trillion

Source: Morgan Stanley Research

Immigration

In the event of a Trump win, he plans to carry out the largest domestic deportation operation in American history, targeting both unauthorized immigrants and those with final deportation orders. Immigration has significant implications for population growth, labour supply and GDP, as it can affect both aggregate supply and aggregate demand. Large negative net immigration typically leads to weaker consumption spending, a smaller labour force and may drive down investment spending. In truth, the upside surprise in US real GDP growth in 2023 was partly driven by the expansion of the labour supply, and a contributing factor could be a lagged disinflationary effect from immigration.

Chart 3 – Immigration Scenarios

2025 Immigration Scenarios					
Scenario	**Deportation**	**Normalized**	**Bipartisan Border Agreement (BBA)**	**Baseline**	**Rapid Immigration**
Population Growth	0.2%	0.6%	0.8%	0.9%	1.4%
Net Immigration (thous)	0	800	1400	2600	3300
Nonfarm Payrolls Breakeven	45k	87k	135k	210k	265k
Description	No net immigration. Population growth reflects native born only.	Pre-Covid immigration flows of 800k/year. Breakeven NFP is near pre-Covid rate of ~87k.	Bipartisan Border Agreement passed and enforced. Immigration flows slow from 3.3mil to 1.4mil. Breakeven estimated ~135k.	Halfway between current immigration flows and Bipartisan Border Agreement. Immigraton slows from 3.3mil to 2.6mil, in-line with CBO. Breakeven estimated 210k.	Current immigration flows of 3.3 million persist. Breakeven estimated to be similar to 2024 at 265k.
Policy	Trump wins the election and changes immigration policy mainly through executive action: stricter border policy enforced, as well as deporting some migrants who are already in the US and awaiting trials or working.	Trump wins election and changes immigration policy: Stricter border enforcement via leverage of executive authorities, excluding actions that courts have previously disallowed + some implementation of new authorities.	Trump or Biden wins election and change immigration policy: Limited executive authorities/implementation but Bipartisan Border Agreement curbs crossings	Trump or Biden wins election, but no policy change: No new policy change but flows moderate due to either perceived worse conditions for crossing/general deterrence (Trump) or natural moderation/mean reversion (Biden).	Trump or Biden wins election, but no policy change.

Source: Morgan Stanley Research

Tariffs and trade barriers

For the 2024 election, Trump has proposed a new 10% tariffs on virtually all goods imported into the US, and even imposing a 60% tariff on all goods imported from China. Back in 2018-19, the rise in US tariffs were associated with a decline in US growth expectations and a larger reduction in growth expectations outside the US. As a result, rising US tariffs raise the risk of a higher US Dollar by creating asymmetric downside risks to foreign growth. The impact on inflation is, however, less clear. On theory, tariff is inflationary, but the passthrough to inflation is less certain when slowdown in economic growth is included.

Clean energy and infrastructure

The outcome of 2024 election have significant implications on clean energy and climate. Trump proposed cutting or eliminating tax incentives for renewable energy projects and electric vehicles. In addition, he plans to promote fossil fuel production, and may roll back environmental regulations that limit emissions from power plants and other industrial sources. A Harris win would likely see the extension of Inflation Reduction Act (IRA), expanding tax credits and incentives for renewable energy projects and electric vehicles. As a result, a Harris win is likely to boost investments in clean energy sector, while a Trump win could favour traditional energy sectors like oil and gas.

It is important to consider US election risks while formulating your investment asset allocation and strategy, as it can create significant market volatility due to uncertainty about future policies. That being said, long term market trends are often driven by broader economic factors such as business cycle, instead of election outcomes. Staying focused on fundamentals and maintaining a diversified portfolio will help to mitigate election related risks.