BNY

iFlow

MACRO MORNING BRIEFING

November 8, 2024

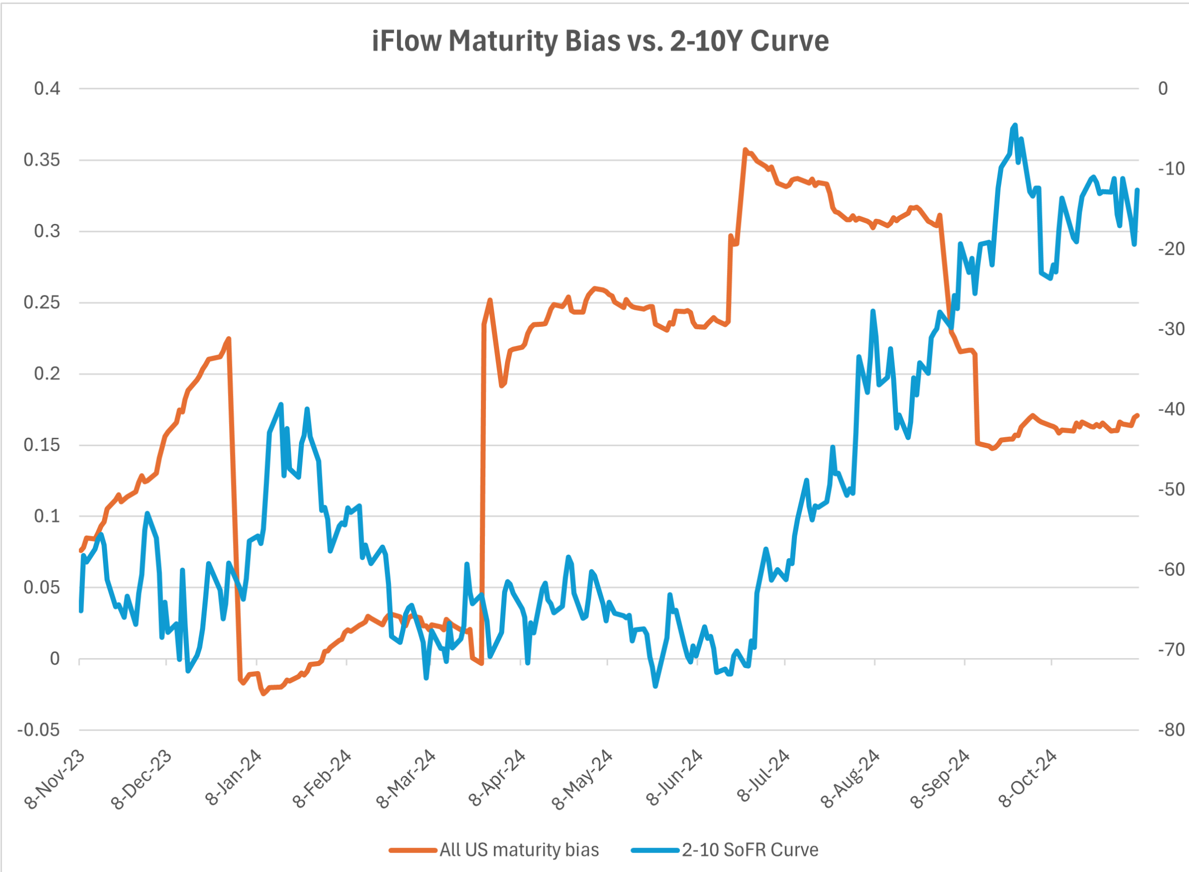
Trump Trades

- While most focus on the election revolves around the **three key trades for the Trump presidency (yield curve steepening, higher equities and a stronger USD)** the less discussed trades may have better outcomes – particularly M&A and defense.
- The **iFlow data show that the equity market was not prepared for a significant rally**. Most investors were set up for a more protracted election outcome with hopes for significant trading volatility. Instead, the speed of the certainty from the election outcome has led momentum factors – fear-of-missing-out trading dominated.
- The **setup for the US bond market is more problematic** as the US easing and the demand for duration that was notable from October 2023 to the summer stalled but did not reverse. The risk of a yield curve steepening was not the central expectation of client holdings given the dominance of Fed rate cuts as the key concern for 2024.
- **USD holdings are negative** and that reflects hedging of US assets for cross-border investors. As equities rally from cross-border buying, USD selling into Fed rate cuts continues. The setup for the election did see a slowing in this process with some currency-specific holdings.

The discussion around what trades work best with a Trump administration centers on the following three points: **1) Tax cuts = higher deficits.** Trump policy shifts from the current government will revolve around taxes – expected to be lower thereby increasing the government deficits and borrowing needs. **2) Tariffs = inflation**. Investors also fear the role of tariffs as they are expected to disrupt global trade and supply chains as they did in 2016-2020 with risk of inflation and less investment. **3) Deregulation = more lending**. The markets also see Trump pushing for less regulation by government – leading to easier lending as capital requirements drop, along with more pressure on the FOMC to ease.

Adding these points together and throwing in that some Trump advisors have pushed for issuing longer maturing debt, the first focus on a yield curve steepening trade dominates post-election trading. The setup for this risk was modest, but there was a notable pullback in positioning into the election – some of this reflects the US FOMC rate path rethinking more than speculation about the election outcome. There is a notable lag to the market and our maturity bias – which is breaking down given the election result.

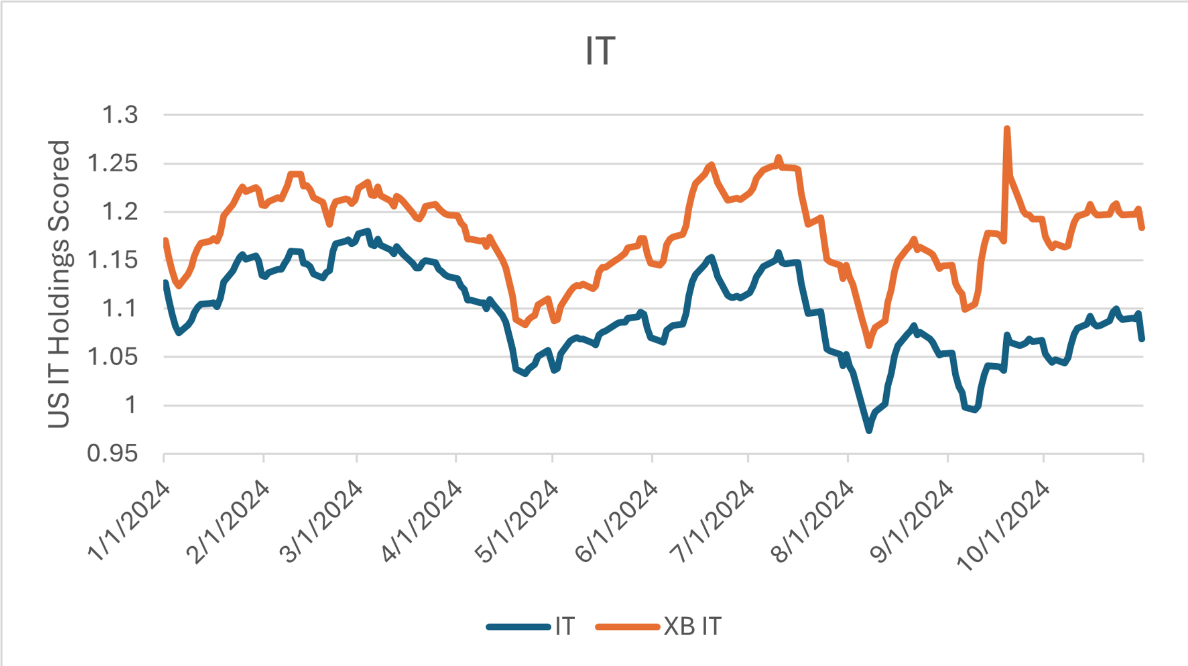
Exhibit #1: iFlow US Bond Maturity Bias Leads Curve



Source: iFlow, Bloomberg, BNY

The US equity market was the most consistent Trump trade post-election. The mixture of policies was supportive, but there are mixed signals in the policy – with two notable points: 1) Deregulation could promote DeFi, adding to pressure on smaller and medium-sized US banks. The link of crypto regulation relief has made BTC a barometer for this risk. This is at odds with the November 6 price action, where financials dominated gains. 2) The bias to boost made in US products via tariffs and to reindustrialize the nation will make the S&P 500 a more difficult benchmark given that the average of the index has 40% of its earnings abroad. The ability of the IT sector to remain the largest market cap is going to be assessed by markets.

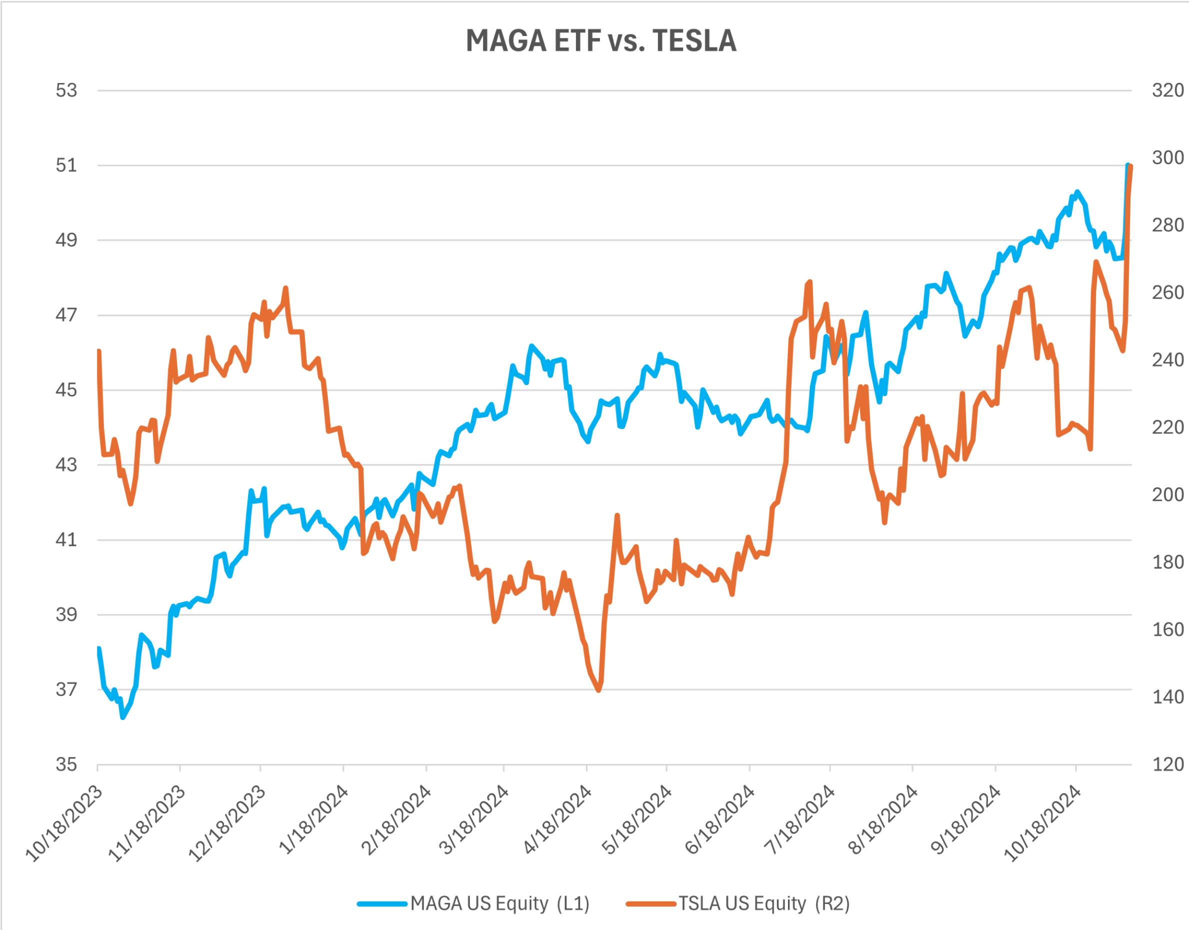
Exhibit #2: US IT Sector Holdings from iFlow



Source: iFlow BNY

The US information technology holdings from iFlow are interesting to consider. The cross-border holdings of the US IT sector are notably higher than the US domestic market. Further, IT has gained through the election for both domestic and cross-border, highlighting the dominance of the sector in market cap. The risk that hasn't been considered rests on how JD Vance views on breaking up monopolies in big tech balance out against others in the Trump administration. The risk of a breakup of the big tech names is not in the price. When we look at the volumes of the IT sector against just the Magnificent Seven, we can see that most of the IT sectors are the big tech names. One way to compare the dichotomies of the present equity trade is to compare the MAGA ETF to TESLA shares and to understand that there is a clash between stocks with a global focus vs. those with a domestic focus.

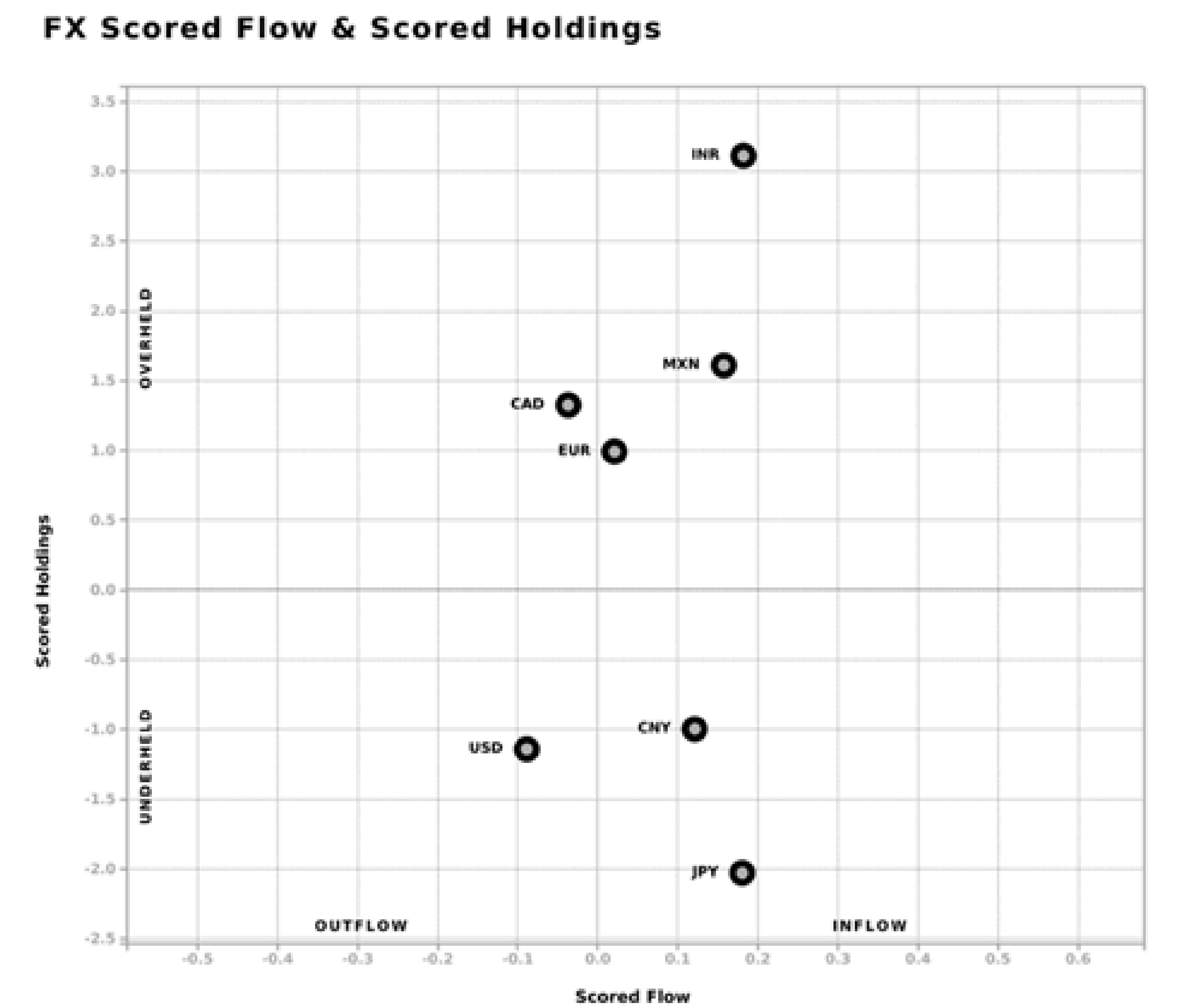
Exhibit #3: Trump Stocks?



Source Bloomberg, BNY

The USD role in markets will be an interesting and developing one should Trump's plans on taxes, regulation and tariffs play out. Looking at our iFlow holdings of FX against flows in the last quarter you can see investors have been wary of the USD, CNY and JPY against holding INR, MXN and EUR. The risk of a larger reversal in the USD does have a correlation to US bond and stock market performance.

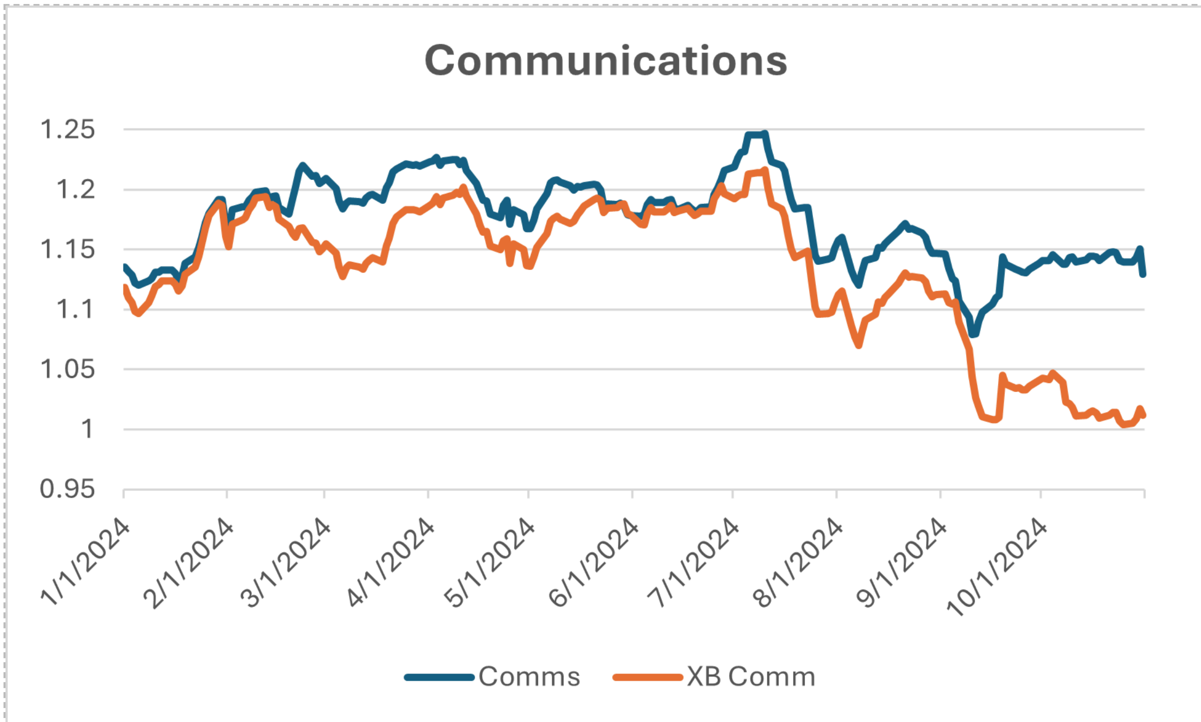
Exhibit #4: USD Underheld and Still Sold in the Last 3 Months



Source: iFlow, BNY

The role of mergers and acquisitions is an under-considered consequence of the current set of economic variables and new Trump policies. The M&A world has two kinds of mergers – horizontal ones where one company buys the other to eliminate competition and have greater pricing power, usually following the late-stage economy cycle – something that a soft-landing or bumpy-landing for the US economy would encourage. Regulation has a key role in preventing the monopoly push at the expense of the consumer, but deregulation from the new administration could be important – an example of this is the Discover and Capital One merger. The role of tariffs in the US supply chain is a risk to consider for the other kind of merger – verticals – where a company buys a key part of their supply chain to secure better cost controls and certainty. A world of rising trade tariffs would see a spike in US M&A for owning key suppliers for end products. The correlation of M&A to GDP now is lagged as you would expect, while the link to logistics has been recently significantly positive. The one US sector where cross-border holdings lag the whole in our iFlow may be instructive – communications have since the start of the US election season shifted notably.

Exhibit #5: Biggest Holdings Difference Is in US communications Sector

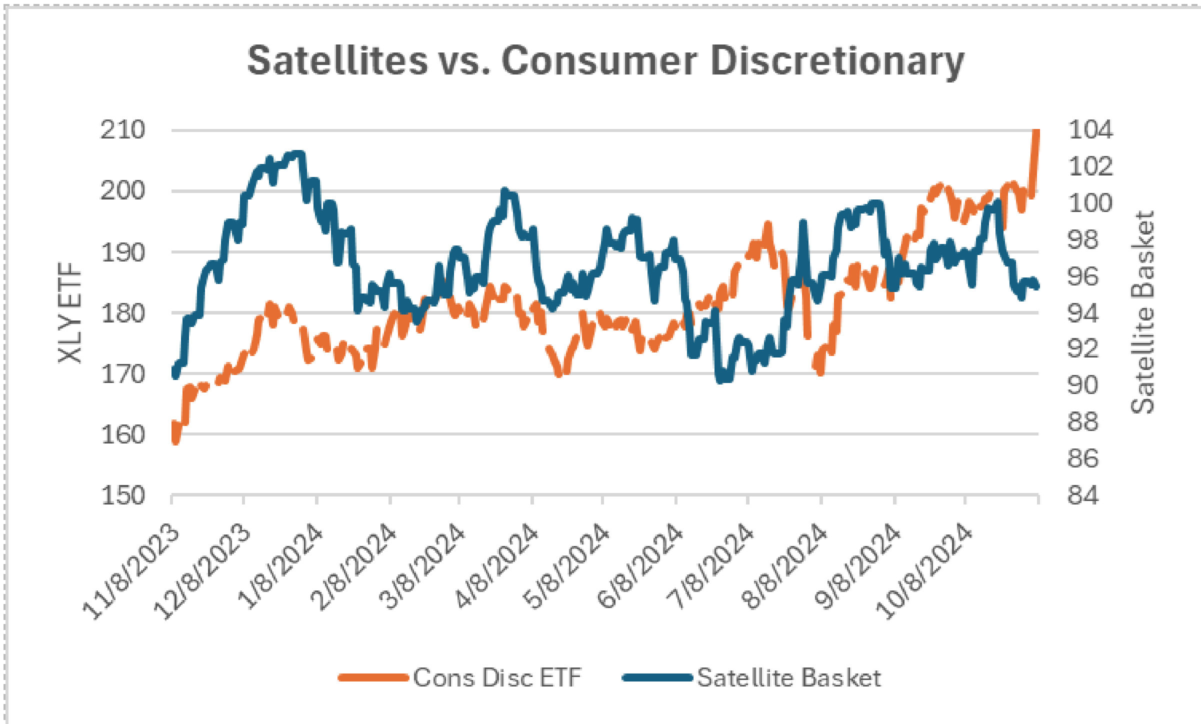


Source: iFlow, BNY

The least discussed risk revolves around foreign policy. Geopolitical risks are expected to be "on hold" as Trump reconsiders the US role in supporting Ukraine and negotiates with China on trade, Taiwan and North Korea. Support for Israel is also assumed to remain intact with less emphasis on quick diplomacy. The net result could be an escalation in how China and other nations see US isolationism and move to fill the void with defense spending. The focus here may not be in traditional places, as space looks to be the next zone for control. As the war in Ukraine has highlighted, the use of Starlink has been critical for both Ukraine and Russia. Satellite technology and control of low-earth orbit communications will be critical and this plays into the role of Elon Musk as a part of the Trump administration. Looking at the list of key satellites producers in the US and EU, which also happen to be key defense companies, against the global peace index is informative, but the higher frequency would be to compare this to consumer discretionary sector as that represents a peacetime activity. The split of the two highlight the dichotomy of risks into the way markets are pricing 2025.

Bottom Line: There are a considerable number of trades to investigate for markets into 2025. The first out of the post-election trades may not be the best ones. We covered how our iFlow data is counter to a few of these, highlighted a few other ideas and see one common ground – volatility – as most of the policies that drive one trade have another one limiting its success – as bond yields have a valuation effect on stocks and both matter to FX movements. Risks into Trump administration policy shifts are likely to remain unclear until well into January 2025, making the last two months of 2024 more prone to speculation and position shifts.

Exhibit #6: Satellites Basket vs. Consumer Discretionary



Source: iFlow, Bloomberg, BNY

Disclaimer & Disclosures

Please direct questions or comments to: iFlow@BNY.com

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