

Fixed Income Research & Macro Strategy (FIRMS) – 12th January 2021

Biden's trump cards and challenges

Barring another dramatic twist in an already torturous two months of political upheaval, Joe Biden will find a very full in-tray when he settles into the famed Oval Office in eight days time. The two most pressing issues which he will need to resolve are arguably the Covid-19 pandemic and the associated impact on already tepid US economic growth.

The overall picture is one of less confident US consumers faced with a decline in personal disposable income having cut their spending on goods and services (see Figure 1). Corporates confronted with declining demand have slowed their hiring and in December shed labour while domestic investment growth has slowed to a trickle.

Despite the Dollar's slide since May, the goods and services trade deficit hit an all-time high of \$68.1bn in November as a result of a collapse in US exports, a clear stain on President Trump's track record given his penchant for protectionist measures.

ISM manufacturing and non-manufacturing PMI data for December offer a glimmer of hope, with both having risen at their fastest rates since July. Nevertheless the rate of annualised, seasonally-adjusted quarter-on-quarter GDP growth in Q4 was likely significantly slower than the all-time high of 33.4% recorded in Q3 and potentially negligible, in our view.

This has not stopped US equity markets from rising to new-all time highs but these wealth gains have likely been very unevenly distributed.

Biden's administration will face many challenges but also has a reasonably strong political platform from which to launch and fine-tune its policies. The Democratic Party has a majority in both houses of Congress (albeit by the slimmest margins in the Senate) and the US economy should in theory benefit from the recently approved \$900bn stimulus package.

However, the near-term outlook for the US economy remains lacklustre in our view. The fiscal stimulus package is a fraction of the \$2.2trn (10.6% of GDP) CARES Act which came into effect in late-March and the US cannot escape weak global growth. Finally, tougher social distancing measures would likely weigh on US economic growth.

President Biden faced with pressing matters of Covid-19 pandemic and slowing US growth

Much has been written about the tragic events which unfolded in the Capitol last week and historians and political and constitutional experts will undoubtedly have much more to say in months and years ahead. The odds of Donald Trump's presidency ending in a bang rather than a whimper were always high and what Trump will do for the next four years remains a riddle wrapped in a mystery inside an enigma (to paraphrase Sir Winston Churchill). However, barring another dramatic twist in an already torturous two months of political upheaval, Joe Biden will officially be sworn in as the 46th President of the United States and move into the White House on 20th January (with President Trump having said he would not attend the swearing in ceremony).

Biden will find a very full in-tray when he settles into the famed Oval Office in eight days time. Unifying a bitterly torn country is a multi-year project and he could do worse than to look at the United Kingdom which remains deeply divided four and a half years after the British electorate voted to leave the European Union. Rebuilding relations with the United States' key trading partners, including Canada and Mexico, may take less time but is unlikely to happen overnight while moulding a new relationship with China will be fraught with challenges.

However, the two most pressing issues which Biden will need to resolve are arguably the Covid-19 pandemic and the associated impact on already tepid US economic growth. Trump's disjointed, back-of-the-envelope approach to dealing with the virus which has often sidelined medical experts has arguably contributed to 376,000 Covid-19 related deaths – a number which continues to rise by over 2,000 a day. Moreover, despite the US never going into lockdown at a national level the rate of growth in economic activity has slowed sharply in Q4, as seen in Figure 1.

The overall picture which emerges is one of less confident consumers faced with a decline in personal disposable income having cut their spending on goods and services. Corporates confronted with declining demand have slowed their hiring and in December shed labour (for the first time since April) while domestic investment growth (as proxied by new orders for non-defence capital goods excluding aircrafts) has slowed to a trickle. Manufacturing output, which accounts for about 11% of GDP, rose only 2% in September-November and was still down 3.7% yoy in November. Retail sales and industrial output figures for December are due out 15th January.

Figure 1: US macro indicators point to sharp growth slowdown in Q4, December offers slim glimmer of hope

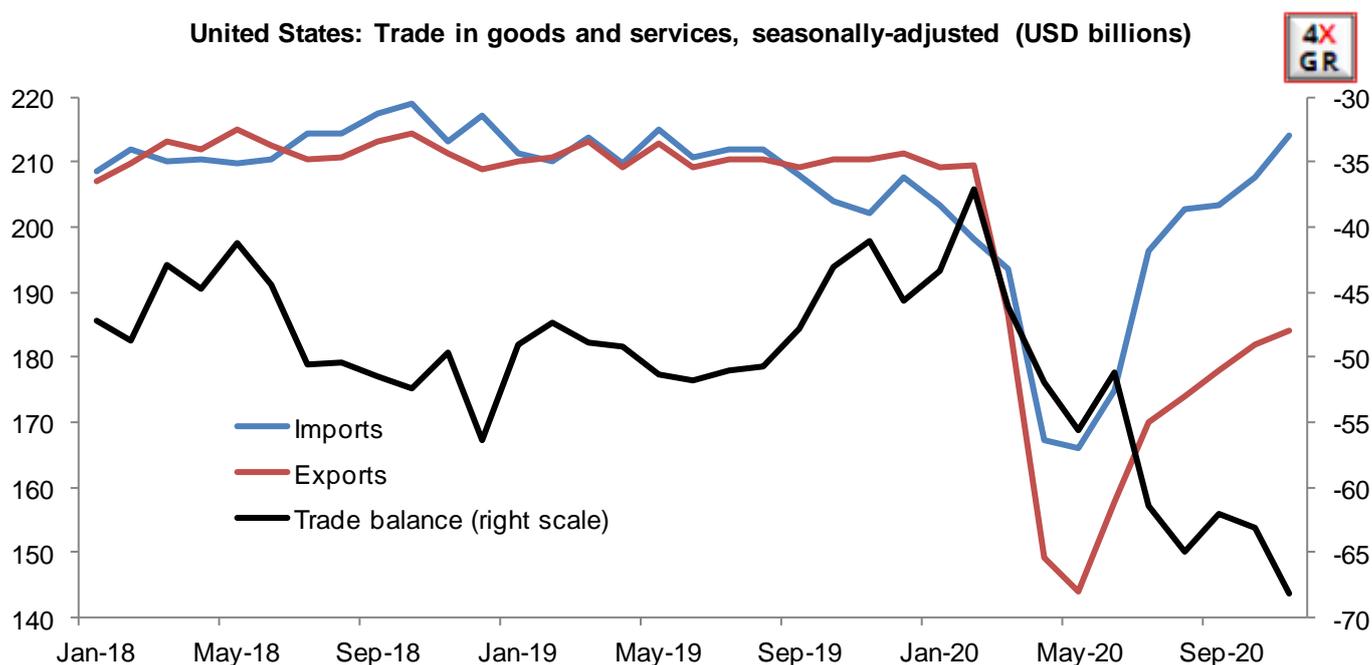
United States Macro Indicators 	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21
Core CPI-inflation, % year-on-year	2.1	1.4	1.2	1.2	1.6	1.7	1.7	1.6	1.7		
Core PCE-inflation, % year-on-year	1.7	0.9	1.0	1.1	1.3	1.4	1.5	1.4	1.4		
US Dollar Nominal Effective Exchange Rate, % change in monthly average **	5.0	2.7	-0.4	-2.5	-0.4	-1.1	-0.5	-0.1	-1.4	-1.7	-0.2
Personal Consumption Expenditure (PCE), constant prices, seasonally-adjusted, % month-on-month	-6.5	-12.3	8.5	5.9	1.2	0.9	1.1	0.3	-0.4		
Retail sales, constant prices, seasonally-adjusted, % month-on-month*	-8.0	-14.3	18.1	8.0	0.9	1.1	1.6	-0.1	-1.1		
Personal disposable income, constant prices, seasonally-adjusted, % month-on-month	-1.4	15.6	-4.8	-1.8	0.5	-3.3	0.6	-0.8	-1.3		
Non-Farm payrolls, seasonally-adjusted, change (thousands)	-1,373	-20,787	2,725	4,781	1,761	1,493	711	654	336	-140	
Conference Board consumer confidence index	118.8	85.7	85.9	98.3	91.7	86.3	101.3	101.4	92.9	88.6	
Manufacturing output, seasonally-adjusted, % month-on-month	-5.0	-15.8	3.8	7.7	4.2	1.5	0.1	1.1	0.8		
ISM manufacturing PMI, seasonally-adjusted, percentage point change	-1.0	-7.6	1.6	9.5	1.6	1.8	-0.6	3.9	-1.8	3.2	
ISM non-manufacturing PMI, seasonally-adjusted, percentage point change	-4.8	-10.7	3.6	11.7	1.0	-1.2	0.9	-1.2	-0.7	1.3	
Durable goods orders, seasonally-adjusted, % month-on-month	-16.7	-18.3	15.0	7.7	11.8	0.4	2.1	1.8	0.9		
New orders for non-defense capital goods excluding aircrafts, seasonally-adjusted, % month-on-month	-1.3	-6.6	1.5	4.3	2.6	2.4	1.9	1.6	0.4		
Goods & services trade balance, seasonally-adjusted, \$ bn	-46.1	-51.9	-55.6	-51.2	-61.4	-64.9	-62.1	-63.1	-68.1		
New privately-owned housing units started ("Housing Starts"), seasonally-adjusted, % month-on-month	-19.0	-26.4	11.1	21.9	17.5	-7.7	4.7	6.3	1.2		
S&P 500, % month-on-month **	-12.5	12.7	4.5	1.8	5.5	7.0	-3.9	-2.8	10.8	3.7	1.2

Source: 4X Global Research, Conference Board, Federal Reserve, Institute of Supply Management, investing.com, US Bureau of Economic Analysis, US Bureau of Labour Statistics, US Census Bureau

Note: *US Dollar-value of retail sales deflated by headline PCE-inflation; ** Data till 11th January 2021

The goods and services trade deficit (seasonally-adjusted) hit an all-time high of \$68.1bn in November as a result of a collapse in US exports (see Figure 2). Notably the Dollar's slide since mid-May has done nothing to arrest the widening of the trade deficit, suggesting that the US is struggling to compete internationally despite its gain in currency competitiveness. This is a clear stain on President Trump's track record given his view that a weaker Dollar would help him deliver his electoral pledge to redress the trade imbalances between the United States and its main trading partners, including China.

Figure 2: US exports have collapsed despite weaker Dollar, driving trade deficit to record-high



Source: 4X Global Research, US Bureau of Economic Analysis

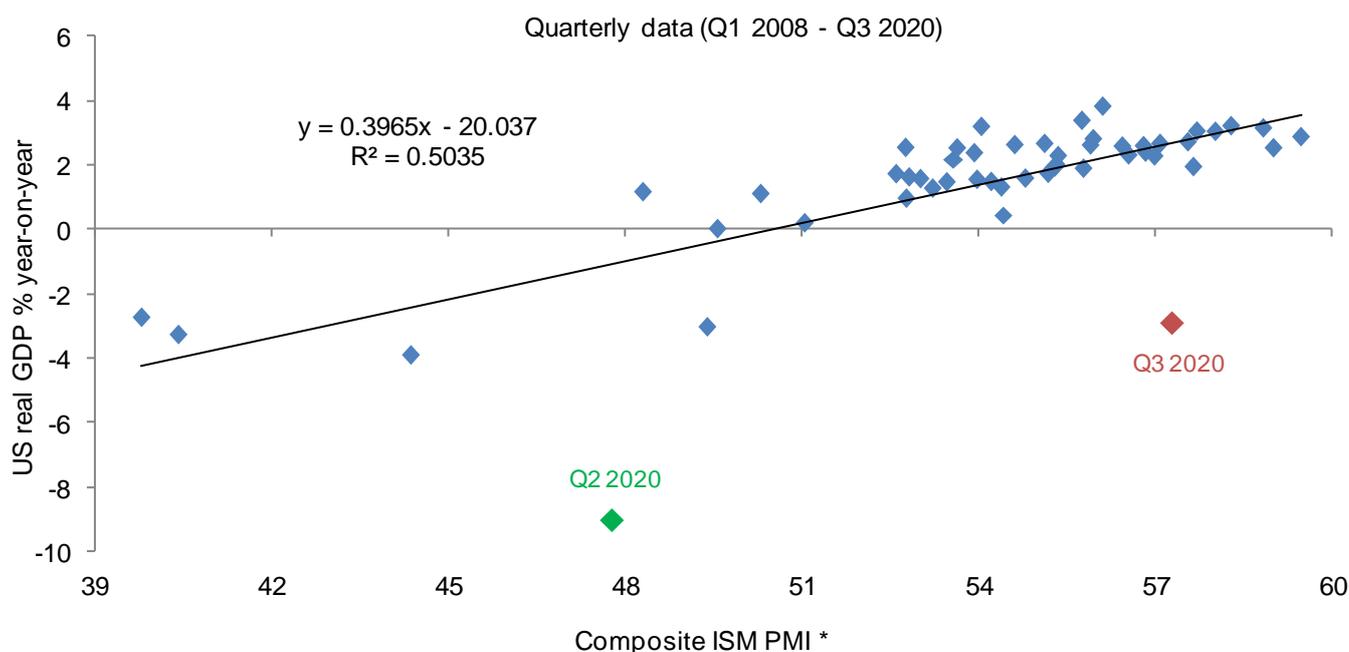
Institute of Supply Management (ISM) data for December offer a glimmer of hope, with both the manufacturing and non-manufacturing Purchasing Managers Indices (PMI) having risen at their fastest rates since July. These timely indicators suggest that economic activity in the manufacturing sector and the critical service sector picked up in December¹. Figure 3 points to a positive, historical correlation between our measure of the “composite” ISM PMI (an 86.5-13.5 weighted average of the non-manufacturing and manufacturing PMIs) and year-on-year GDP growth although Q2 and Q3 2020 are clear outliers (GDP growth was far weaker than implied by the composite PMI).

If, and it remains a big if, this historical relationship re-established itself in Q4 2020 the average composite PMI of 56.9 suggests that year-on-year GDP growth may have been modestly positive in Q4 (about 2.5%

¹ The ISM non-manufacturing PMI includes the service sector (by far the largest component), retail and wholesale trade, utilities and agriculture, forestry, fishing, and hunting.

based on the regression in Figure 3). Nevertheless the rate of annualised, seasonally-adjusted quarter-on-quarter GDP growth in Q4 was likely significantly slower than the all-time high of 33.4% recorded in Q3 and potentially negligible, in our view.

Figure 3: Based on history composite PMI of 56.9 in Q4 points to modestly positive year-on-year GDP growth



Source: 4X Global Research, Institute of Supply Management., US Bureau of Economic Analysis

Note: * Our measure attributes 86.5% weight to non-manufacturing PMI (services, retail and wholesale trade, utilities and agriculture, forestry, fishing, and hunting) and 13.5% weight to manufacturing PMI. Mining and construction (which contribute to industrial output) are not covered by the US ISM PMIs.

This has not stopped US equity markets from rising to new-all time highs (see Figure 1). Cheap money and the lack of opportunities for households to spend and corporates to invest have arguably contributed to the metronomic rise in US equity indices. However, the gains which have accrued have most likely been unevenly spread across US society (a recent Federal Reserve study estimates that 10% of the wealthiest US households by net wealth owned about 87% of stocks held by US households at end-Q1 2020).

Biden's (modest) political and fiscal trump cards may not prove sufficient near-term

There is little doubt that Biden's administration will face many challenges but it also has a reasonably strong political platform from which to launch and fine-tune its policies.

The Democratic Party has an 11 -seat majority in the 435-seat House of Representatives, albeit a narrower one following the 3rd November Congressional elections (the Democrats have 222 seats, the Republicans 211 while two seats remain vacant). Moreover the Democratic Party has regained control of the Senate, the upper house of Congress, albeit by the slenderest of margins. Following the 5th January run-off for the two seats in Georgia, both won by the Democratic candidates, both parties now have 50 seats each in the Senate with Vice-President Kamala Harris having the casting vote.

Aside from the political landscape, the US economy, households (and Biden's standing) should in theory benefit from a substantial fiscal injection as Congress approved on 21st December and President Trump signed into law on 27th December:

- A \$1.4trn spending bill to avoid a shutdown of government; and
- A stimulus package of nearly \$900bn (4.3% of GDP). The economic relief package, the second largest in American history, includes i) nearly \$300bn in small business relief, ii) a new round of direct payments of up to \$600 for US taxpayers and their dependent children², and iii) a \$300 per-week top-up in unemployment insurance until mid-March 2021, among dozens of other provisions. Some of these payments to US households have reportedly already started.

Moreover, the House of Representatives approved on 28th December 2020 the "[Caring for Americans with Supplemental Help Act of 2020](#)" (CASH Act of 2020) which increases the payment to eligible US tax payers from \$600 to \$2,000 and would reportedly require an extra \$385bn in funding. The Democrats' slender majority in the Senate could prove critical when the upper house reconvenes to vote on the bill (Senate would need to approve the CASH Act with a simple majority).

However, the near-term outlook for US economic growth remains lacklustre in our view.

For starters the recently passed second fiscal stimulus package is a fraction of the \$2.2trn (10.6% of GDP) Coronavirus Aid, Relief and Economic Security (CARES) Act which Trump signed into law on 27th March 2020. Moreover, while the US is a relatively closed developed economy (compared to its European peers for example), it cannot escape weak global growth. Finally, and perhaps most importantly, we think the risk is clearly tilted towards Biden introducing far tougher social distancing measures (than Trump did) in a bid to arrest the climb in the number of Covid-19 cases and deaths. If correct, the experience of Europe suggests that growth in US household consumption, corporate investment and ultimately headline GDP could face material headwinds.



² Single people earning up to \$75,000 and their dependent children (under the age of 17) will receive a cheque of \$600, while married couples earning up to \$150,000 will receive \$1,200. For single people, the payment will be reduced by \$5 for every \$100 of income earned above the \$75,000 threshold. Single people earning over \$87,000 or married couples earning more than \$174,000 will not receive any payments.

DISCLAIMER & DISCLOSURE STATEMENT

THIS MATERIAL IS: (I) FOR YOUR PRIVATE INFORMATION, AND WE ARE NOT SOLICITING ANY ACTION BASED UPON IT; (II) NOT TO BE CONSTRUED AS AN OFFER OR A SOLICITATION OF AN OFFER TO BUY OR SELL ANY SECURITY IN ANY JURISDICTION WHERE SUCH OFFER OR SOLICITATION WOULD BE ILLEGAL; AND (III) BASED UPON INFORMATION THAT WE CONSIDER RELIABLE.

4X GLOBAL RESEARCH DOES NOT WARRANT OR REPRESENT THAT THE PUBLICATION IS ACCURATE, COMPLETE, RELIABLE, FIT FOR ANY PARTICULAR PURPOSE OR MERCHANTABLE AND DOES NOT ACCEPT LIABILITY FOR ANY ACT (OR DECISION NOT TO ACT) RESULTING FROM THE USE OF THIS PUBLICATION AND RELATED DATA. TO THE MAXIMUM EXTENT PERMISSIBLE ALL WARRANTIES AND OTHER ASSURANCES BY 4X GLOBAL RESEARCH ARE HEREBY EXCLUDED AND 4X GLOBAL RESEARCH SHALL HAVE NO LIABILITY FOR THE USE, MISUSE, OR DISTRIBUTION OF THIS INFORMATION.

The analysis and information presented in this report (Report) by 4X Global Research Ltd (4X Global Research), an independent research company registered in the UK, is offered for subscriber interest only. The content is intended for investment professionals only, and is not to be viewed or used by individual investors in any regulatory jurisdiction. By accessing this Report you confirm that you meet these criteria.

This Report is not to be used or considered as a recommendation to buy, hold or sell any securities or other financial instruments and does not constitute an investment recommendation or investment advice. The information contained in this Report has been compiled by 4X Global Research from various public and industry sources that we believe to be reliable; no representation or warranty, expressed or implied is made by 4X Global Research, its affiliates or any other person as to the accuracy or completeness of the information. 4X Global Research is not responsible for any errors in or omissions to such information, or for any consequences that may result from the use of such information. Such information is provided with the expectation that it will be read as part of a wider investment analysis and this Report should not be relied upon on a stand-alone basis. Past performance should not be taken as an indication or guarantee of future performance; we make no representation or warranty regarding future performance. The opinions expressed in this Report reflect the judgment of 4X Global Research as of the date hereof and are subject to change without notice.

This Report is not, and should not be construed as, an offer or the solicitation of an offer to buy or sell any securities. The offer and sale of securities are regulated generally in various jurisdictions, particularly the manner in which securities may be offered and sold to residents of a particular country or jurisdiction. Securities referenced in this Report may not be eligible for sale in some jurisdictions. To the fullest extent provided by law, neither 4X Global Research nor any of its affiliates, nor any other person accepts any liability whatsoever for any direct or consequential loss, including without limitation, or lost profits arising from any use of this Report or the information contained herein.

No director, officer or employee of 4X Global Research is on the board of directors of any company referenced herein and no one at any such referenced company is on the board of directors of 4X Global Research. 4X Global Research does not invest in any securities although it is possible that one or more of 4X Global Research's directors, officers, employees or consultants may at times be invested in the securities referenced.

4X Global Research is not authorized or regulated in the United Kingdom by the Financial Conduct Authority (FCA) or by any other regulator in any jurisdiction for the provision of investment advice. Specific professional financial and investment advice should be sought from your stockbroker, bank manager, solicitor, accountant or other independent professional adviser authorized pursuant to the Financial Services and Markets Act 2000 if you are resident in the United Kingdom or, if not, another appropriately qualified independent financial adviser who specializes in advising on the acquisition of shares and other securities before any investment is undertaken.

This Report, including the text and graphics, is subject to copyright protection under English law and, through international treaties, other countries. No part of the contents or materials available in this Report may be reproduced, licensed, sold, hired, published, transmitted, modified, adapted, publicly displayed, broadcast or otherwise made available in any way without 4X Global Research's prior written permission. All rights reserved. This document is produced using open sources believed to be reliable. However, their accuracy and completeness cannot be guaranteed. The statements and opinions herein were formed after due and careful consideration for use as information for the purposes of investment. The opinions contained herein are subject to change without notice. The use of any information contained in this document shall be at the sole discretion and risk of the user. Investors should consider this report as only a single factor in making their investment decision and, as such, the report should not be viewed as identifying or suggesting all risks, direct or indirect, that may be associated with any investment decision.

No liability whatsoever is accepted for any loss arising whether directly or indirectly as a result of the recipient acting on such information or opinion or estimates. 4X Global Research employees may have or take positions in the markets and securities mentioned in this document. The stated price of any securities mentioned herein is not a representation that any transaction can be effected at this price. Investing in securities may entail certain risks. The securities referred to are not suitable for all investors and should not be relied upon in substitution for the exercise of independent judgment. This material is not directed at you if 4X Global Research is prohibited or restricted by any legislation or regulation in any jurisdiction from making it available to you. 4X Global Research and its analysts are remunerated for providing independent investment research to financial institutions, corporations, and governments.

DISCLOSURE: This Report is not to be copied, forwarded or otherwise disseminated to non-subscribers in electronic or physical form without prior consent.