Swedbank

Macro Focus

US Election 2020: Bidenomics gives short run growth boost

- Joe Biden's economic plan is expected to lift GDP growth in the years to come
- ...but the plan also comes with some long run risks
- From a global and Swedish perspective, the Biden policy will be more predictable

In previous publications (here and here) we discuss the electoral system and briefly go through the possible market reactions. In this analysis we dig further into the economic consequences of the Biden plan.

First, we find that Bidenomics to some extent helps bringing the US economy back on a stronger footing. The increased spending on education, healthcare and housing etc. would especially benefit low- and middle-income earners. At the same time high-income earners and corporations would face higher taxes. But Biden will likely not succeed with all suggested reforms. Both the spending plan and the proposed tax revenues are expected to be much smaller than his proposal.

Second, Biden's reform will in the long run also make US growth more sustainable. The suggested green elements come at a time when the climate crisis is a high priority for many. In addition, it may contribute to more innovation and investments in R&D, which could increase productivity after a weak period following the Great Financial Crisis. But the Biden plan is not all roses and even without the proposed spending measures the federal debt held by the public will be record high (almost 200% of GDP in 2050).

From a global and Swedish standpoint, Bidenomics would likely put the economies in a better position. Geopolitical risks would decrease, international cooperation with US allies may rise and the risk for an escalated trade war would be lower with Biden in the Oval Office.

With less than one week left until election, Biden is still in the lead in the polls and is seen as the winner by betting markets. However, the lead has narrowed lately. In this analysis we continue to assume a Biden victory and a Democratic Congress.

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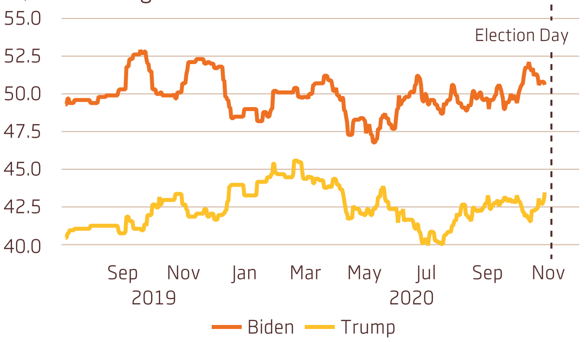
Presidential election, opinion polls

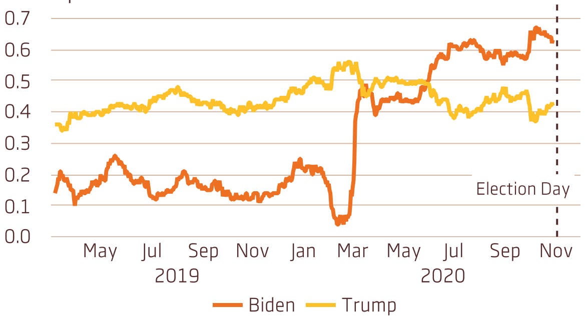
%, RCP Average



Sources: RealClearPolitics, Swedbank Research & Macrobond

Presidential election, prediction market

Cents per dollar



Note: Price per contract. Winning outcome receives $1.
Sources: PredictIt, Swedbank Research & Macrobond

Bidenomics puts the US economy on stronger footing in the short run

The success of Bidenomics will partly depend on the new Congress. A split Congress would limit what can be done, but also the size of the assumed Democratic majority would matter.

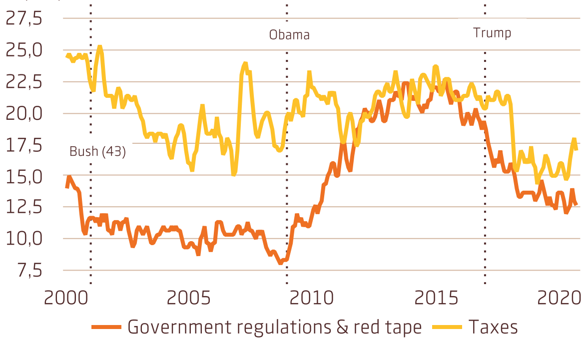
We expect that the Democratic Party gets a slim majority in the Senate and that **filibuster rules remain in place** meaning that a debate can end with the support of three-fifths of the senators (60 people). If so, tax and spending legislation would need bipartisan support or may be passed via reconciliation. Budget reconciliation is a work-around for filibuster but can't be used for everything. For example, it tends to limit the number of bills per year to three (one each on spending, taxes and debt limits), it doesn't allow for changes to social security – something Biden wants to do – and it usually requires that reforms are deficit neutral over a decade (The Economist, Oct. 3rd, 2020).

Biden's proposed spending sums to approx. USD 7trn over ten years and will in part be financed by tax hikes of suggested USD 4trn. However, it's hard to see that he will succeed passing such a comprehensive agenda. More likely we'll see **spending and tax revenue corresponding to at most half the suggested sizes**. On top of this, the Congress is expected to pass **a new corona relief package** of USD 2-3trn after the election (likely in Q1 2021). Taken together it means that the US economy will face expansionary fiscal policy in 2021 and 2022.

In the short run Biden's stimulus may include cash for state and local governments, higher unemployment benefits, increased minimum wage and additional support for small companies (The Economist, Oct. 3rd, 2020). Next year may also see tax credits for various social aims such as caregiving. Those who primarily benefit from Bidenomics and its increased spending on education, healthcare and housing are low- and middle-income earners. We expect that further fiscal stimulus especially would support consumption by low-income households, as was the case during the spring when the corona stimulus started.

NFIB: Single most important problem

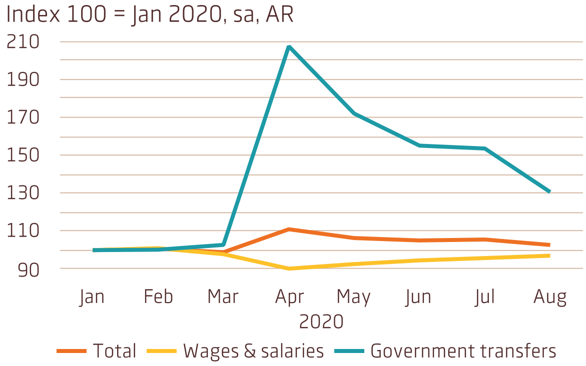
%, sa, 3m ma



Sources: Swedbank Research & Macrobond

Household income

Index 100 = Jan 2020, sa, AR



Sources: Swedbank Research & Macrobond

The wealthiest taxpayers would be hardest hit by Bidenomics and face higher taxes, as would corporates which could see a partial reversal of the 2017 Trump tax cuts. According to Penn Wharton Budget Model and University of Pennsylvania the impact of the suggested tax changes would, in 2021, be minor for 99% of the income earners and we think that the affected high-income earners likely would reduce savings rather than consumption.

Taken together we find that **Bidenomics will contribute to a somewhat faster US economic recovery.** However, policies and their economic effects may come with a delay and should not lift the economy until later in 2021 and onwards. Sectors that will contribute are consumption as well as public consumption and investments.

There are also long-run benefits with the Biden plan, but it is not all roses

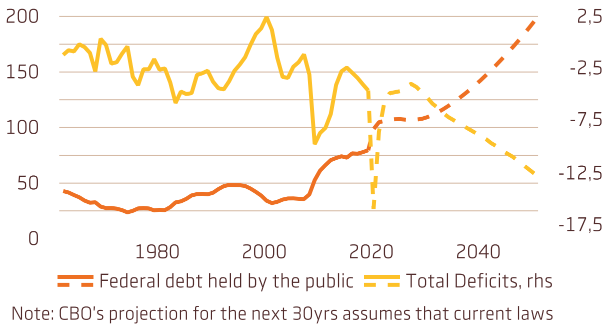
Long run growth under Bidenomics may also be higher. First, Biden may propose an immigration reform or via executive orders change Trump's immigration policies. There are beliefs that the visa rules for skilled people would be eased so the borders to skilled migrants would become more open. Together with a reform of the educational system, that e.g. makes public-university studies cheaper for low-income households, **the level of knowledge could rise**. The Biden policy would also invest in R&D on renewable-energy technologies and other areas like 5G, which **may spur innovation and contribute to higher productivity growth**. Biden's agenda to invest more in green infrastructure would, together with the above, both **boost USA's long run competitiveness and make growth more sustainable**.

Second, Biden's trade policy may contribute to higher global trade which can lift the overall demand, something that can benefit the US too. However, **Biden's trade policy is not all roses**. It includes some protectionism, though in a softer version, which could limit global competition. Global competition is a necessity for countries to specialize on goods and services where they have competitive advantages, it can help to drive down prices, it usually lifts living standards and it tends to provide employment.

The Biden plan includes other challenges as well. For example, there is a **risk that increased minimum wages and higher corporate taxes lowers incentives for companies to hire and invest**. There is also a risk that new regulation could hurt the business sector. Small businesses have over the years complained about government regulation and red tape, which under the Trump era has been a less severe problem.

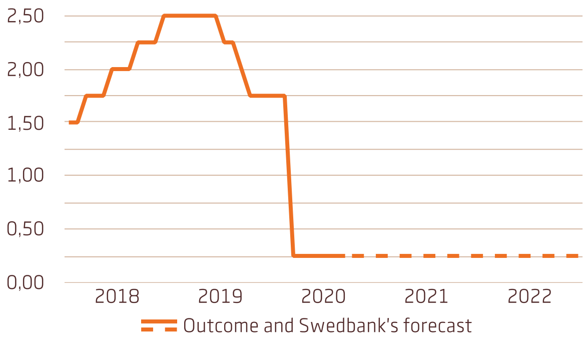
Furthermore, the Biden plan would likely deteriorate the **long run fiscal position** further (note that Trump's proposals would weigh on public finances too). Already under the current laws on government taxes and spending the Congressional Budget Office (CBO) projects a deficit that is large in historical standards. By 2050 the deficit is forecasted to be approx. 13% of GDP and the federal debt held by the public is projected at 195% of GDP. **An important mitigating factor is that current US interest rates are low**. But if there is a perception that increased debt would drive up inflation ahead, investors may require higher inflation compensation (i.e. bond yields). Thus, all else equal, prospects of higher inflation could make the US long run fiscal equation more troublesome. But Fed's new policy signals that interest rates will remain low for long even as inflation rises. Taken together, actual high inflation and continued low rates is one way to reduce the debt burden. Another channel would be through stronger US growth, which is something we expect to see over time.

CBO's projections of US public finances



Note: CBO's projection for the next 30yrs assumes that current laws governing taxes & spending generally did not change.
Sources: Swedbank Research & Macrobond

Fed funds (upper bound)



Sources: Swedbank Research & Macrobond

A pause from increased global tensions but soft protectionism to remain

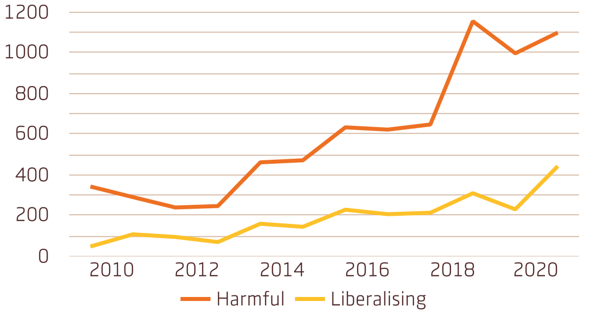
As the world's largest economy, US plays an important role on the global stage. **A Biden presidency is expected to result in changes to both global politics and the world economic development.** For example, he wants to renew commitments to the Iran nuclear deal (if Teheran is compliant with the deal) and re-join the Paris Climate Accord. This, among others, could help to win back trust of America's allies. Biden has the ambition to strengthen the coalition of democracies after a few years where the global economic policy uncertainty index has increased. From a global standpoint, **Biden's view that the US should work with some international organisations aids international cooperation and it may lower global tensions.**

However, geopolitical risks won't fully disappear. Biden's trade policy may be less aggressive and more predictable than Trump's, which should reduce the chance of an accidental military escalation in the South China Sea. His approach to China is also expected to be more polite. But that's basically how far he will go.

The relationship with China is expected to remain frosty and current tariffs will likely be kept. We expect that Biden will try to gather USA's allies to put in place a co-ordinated response to China. Some European countries have already tried to counterbalance Beijing – this is something the US, under Biden, may draw advantage from. Thus, it's possible that Biden will try to form a semi-formal anti-China alliance. While the Trump administration has focused much on Chinese trade, a Biden administration may emphasise human rights and possibly also intellectual property rights. In addition, Biden may stick to the embargo on Huawei and be cautious about high-tech trade with China. Nevertheless, **the psychological effect from a shift from hard to soft protectionism could be profound**.

Trade measures introduced at a global level

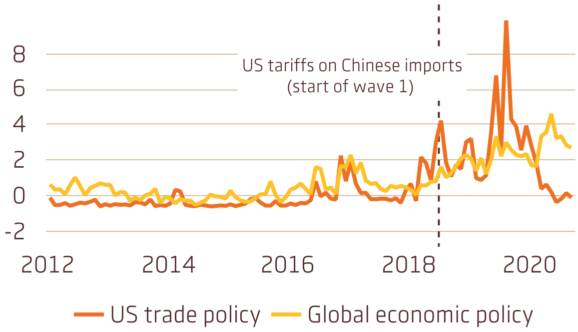
Number of interventions per year for service & goods trade



Note: Adjusted for reporting lag
Sources: Global Trade Alert, Swedbank Research & Macrobond

Policy uncertainty indices

Number of standard deviations



Sources: Swedbank Research & Macrobond

Finally, the Biden plan plays **an important role in the climate crisis battle**. The proposed spending on green infrastructure should speed up the green transformation and give renewed momentum in global climate efforts. Possibly Biden's policies could lead to a green technology race with China, which would support innovation and growth globally (read our analysis here). No matter what, it will be crucial to have China on board (either via cooperation, competition or both) when tackling the climate challenges.

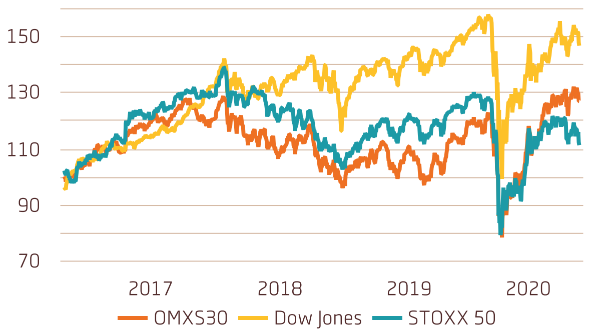
A Biden-victory preferable from a Swedish trade perspective

The short run effects from the US election on the Swedish economy is expected to be limited and mainly go through financial markets. The fiscal stimulus under Bidenomics is seen as inflationary and Swedish yields on bonds with long maturities, that usually move in tandem with global counterparts, could consequently increase somewhat. At the same time, some sectors on the Swedish stock market would, in due time, benefit from the Biden plan where e.g. the green infrastructure elements may boost "climate shares" and we may see further Swedish investments in renewables or climate related R&D.

Of course, the above mentioned assumes that the election result is uncontested and undisputed. If this doesn't hold, we could see turbulence on financial markets followed by risk off movements. Safe haven assets would initially benefit, and the krona would depreciate. Thus, **Swedish households may indirectly be affected by the US election** via their exposure on the stock market (either by private savings or pension funds). The business sector could face volatility on the FX market, but this risk could be hedged away.

Equity markets

Index 100 = Nov 2016, price return, close, USD



Sources: Swedbank Research & Macrobond

FX Spot Rates

SEK per USD

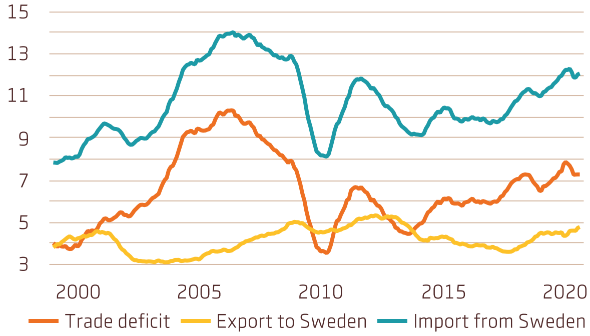
Sources: Swedbank Research & Macrobond

It is hard to imagine a scenario where the US election has major negative implications for the Swedish business sector if there is no escalation in protectionism. Sweden is a member of the EU and the economy is small and open. Sweden is an outspoken advocate of free trade and it is, together with Denmark, Germany, Finland, the Netherlands and the Czech Republic, described as a liberal EU country.

In 2019 the Swedish import and export values of goods were SEK 1.5trn, respectively (approx. USD 0.16trn). Trade in services was smaller, corresponding to nearly half the value of the goods trade (SEK 0.7trn for each category). Looking at countries of destination and consignment, the US (North- and Central America) was ranked high when looking at services trade. **Our calculations found that the US (North- and Central America) was Sweden's 3rd largest service export market and the 2nd largest service import market in 2019**, when looking at individual countries. **However, for goods trade the US was ranked 3rd on the goods export market but only the 12th largest goods import market in 2019.** Hence, the US seems to be of greater importance to services trade than goods trade.

US goods trade with Sweden

USD bn, 12m rolling



Sources: Census Bureau, Swedbank Research & Macrobond

US trade with European Union

USD bn, sa

Sources: Census Bureau, Swedbank Research & Macrobond

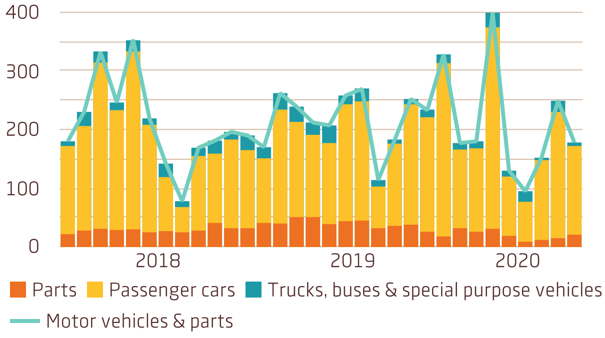
That said, additional harmful intervention would hurt Swedish economy in general and trade in particular. Biden will likely not reverse USA's new protectionism even though he has been a free trader in the past (The Economist, Oct. 3rd, 2020). **But Biden's trade policy would be more predictable and the relationship with allies like Europe would be less strained than in the past few years. From a Swedish perspective that is positive as threats of additional tariffs, e.g. on car imports, would disappear.**

But don't be too optimistic – new trade deals won't be prioritized even though Biden has supported the Trans-Pacific Partnership (TPP) and the revised trade deal between the US-Mexico-Canada (USMCA). Both of which were rejected by the vice-president candidate Kamala Harris (The Economist, Oct. 3rd, 2020). The trade negotiations with the EU (TTIP) have stalled since 2016 and no new rounds of talks are planned. Also, the Trade in Services Agreement (TiSA), between EU and 22 WTO members of which the US is one, is put on hold. **We don't expect Biden to resume trade talks with the EU**. Rather Biden's policy is laced with soft protectionism as he e.g. promises to bring supply chains back to the US, tighten rules on product labelling and use American steel for transport projects etc. (The Economist, Oct. 3rd, 2020).

If, on the other hand, Trump wins the election the negative long run implications could be larger. This is not our baseline but poses some risks to European and Swedish trade policies. **A Trump victory could imply additional harmful trade interventions.** During Trump's first four years he mainly focused on China, but in the next four year's **he may shift his focus to regions where the US trade deficit has increased e.g. the EU**. As late as in end-January 2020 Trump threatened to impose additional tariffs on car imports from EU. However, threats of new tariffs may be his strategy to bring trading partners to the table **so a trade deal with the EU, or at least resumed negotiations, can't be completely ruled out**. But one thing is certain – tariffs on EU car imports would hurt the EU and Swedish economies. The Swedish car industry would be hurt both directly and indirectly via lower European demand, which in turn affects Swedish subcontractors of parts and services to the car industry.

US motor vehicles import from Sweden

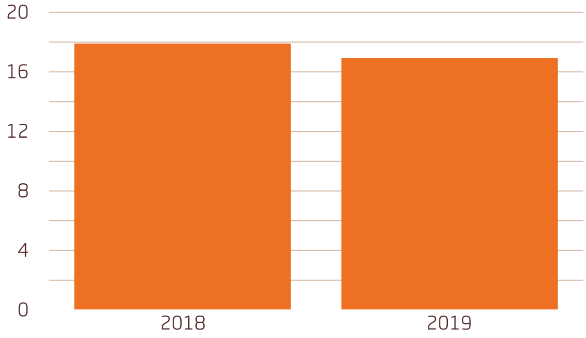
USD mn



Sources: Census Bureau, Swedbank Research & Macrobond

US passenger car imports from Sweden

Share of total goods import from Sweden



Sources: Census Bureau, Swedbank Research & Macrobond

A 2019 analysis by the National Board of Trade Sweden on UN data finds that **Swedish exports of motor vehicles and parts to the US would be 36% lower in five to ten years if additional tariffs of 25 percentage points were implemented**, on top of the already existing US import duties. When including the indirect effects, the Swedish total exports to the rest of the world be 0.1% lower and Swedish production of vehicles would be approx. 2% lower. (The Swedish exports of vehicles to the rest of the world would be 2.7% lower with additional tariffs). **The effects on Swedish GDP is estimated to be small**; a decline by 0.01% or by SEK 0.5bn. Note that the above findings only are based on a tariff change where all other parameters are held constant. Hence, **the figures are a "hint"** rather than the "actual truth".

Taken together, **a US policy that includes new harmful trade interventions, especially if they're directed towards Europe, would hurt Swedish businesses and could affect job opportunities. In addition, new tariffs could affect consumer prices and thereby also hurt consumers**.

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