Daiwa's View

Market anomalies related to US presidential elections

- After presidential elections, we tend to see a rise in stock prices and the USD/JPY rate, and a decline in the Dollar Index
- When former President Donald Trump won in 2016, we saw a rise in stock prices, the USD/JPY rate, and the Dollar Index
- If former President Donald Trump were to win this time, the reaction may be similar to that in 2016, but US economic trends should be monitored carefully

FICC Research Dept

Kengo Shiroyama
81-3-5555-8755
kengo.shiroyama@daiwa.co.jp

Kenta Tadaide
81-3-5555-8466
kenta.tadaide@daiwa.co.jp

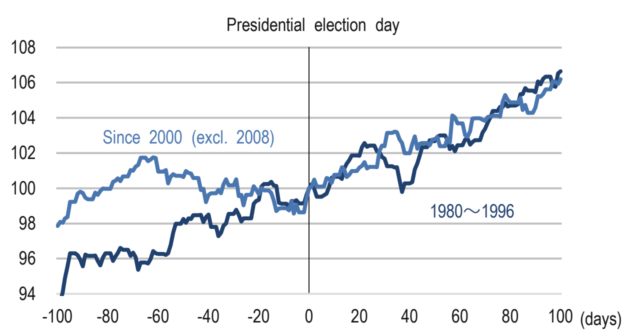
Daiwa Securities Co. Ltd

The US presidential election will be held on 5 November of this year. Being an event that could have a major impact on the financial market, it is attracting a lot of interest. In this report, we examine how the financial market has tended to react during presidential elections in the past, and look back on the election in 2016 when the winner was Donald Trump, who is a strong Republican candidate in the upcoming election.

After presidential elections, the financial market often appears to go into something like risk-on mode. The stock market in particular often sees a post-election rally, probably due to feelings of uncertainty about the future fading after the election (Chart 1). However, there are cases when stock prices fail to rise even after a presidential election during or around times of economic recession, as seen during the bursting of the IT bubble in 2000 and the Global Financial Crisis (GFC) in 2008. Chart 1, which shows data from 2000 onwards, excludes data in 2008 due to the extremely strong fluctuations in stock prices that occurred during the GFC. Provided we take special note of recessions, we can think of the time following presidential elections as being a time when stock prices rise.

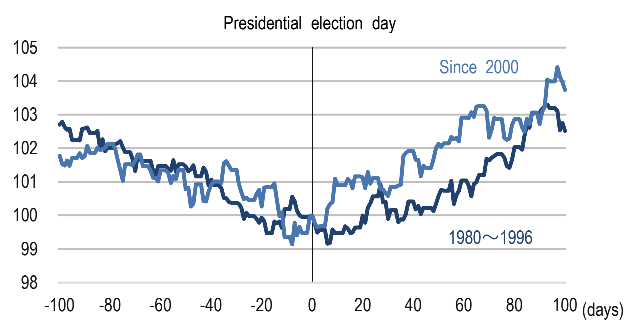
The USD/JPY rate also tends to rise after presidential elections (Chart 2). Here, too, the fading of sense of uncertainty about the future following the election also plays a part. That said, the movement of the USD/JPY rate is influenced by both Japanese and US factors, meaning that post-election dollar appreciation and yen depreciation do not necessarily have the same factors in common. In fact, in order to exclude the impact from the Japanese side, we confirm the movement of the Dollar Index. Until 2000, the dollar tended to strengthen after presidential elections. However, we have seen no clear trend since 2000 (Chart 3). In other words, factors behind the post-election rise in the USD/JPY rate sometimes include dollar appreciation and sometimes include yen depreciation.

Chart 1: Stock Prices Around US Presidential Elections (S&P500, average)



Source: Bloomberg; compiled by Daiwa.
Note: Average of index using data on presidential election day as 100.

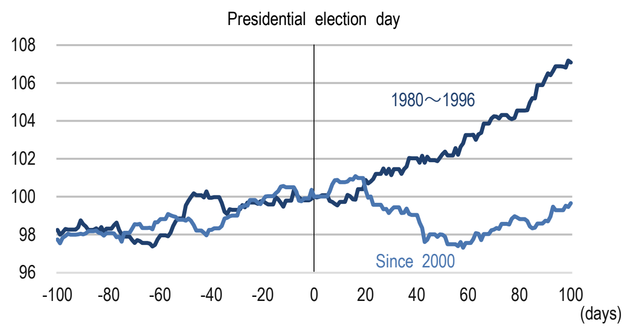
Chart 2: USD/JPY Rate Around US Presidential Elections (average)



Source: Bloomberg; compiled by Daiwa.
Note: Average of index using data on presidential election day as 100.

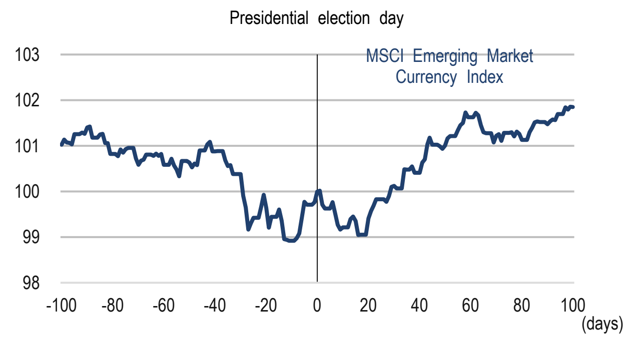
Up until 2000, the rise in the dollar after presidential elections may have been caused by people purchasing the dollar as feelings of uncertainty faded. However, we do not think that reduced uncertainty has necessarily led to purchases of the dollar since 2000. We can point out, for example, emerging-nation currencies as currencies that have become the target of buying instead of the dollar. Since 2000, the performance of the dollar and that of emerging-nation currencies have been inversely correlated. Emerging-nation currencies tend to be bought during risk-on mode in particularly. In fact, calculating the average since 2000, we see a tendency for emerging-nation currencies to rise after presidential elections (Chart 4). So, the fact that non-dollar currencies tend to be bought is likely why there is not a clear rise in the dollar following presidential elections.

Chart 3: Dollar Index Around US Presidential Elections (average)



Source: Bloomberg; compiled by Daiwa.
Note: Average of index using data on presidential election day as 100.

Chart 4: Emerging-nation Currencies Around US Presidential Elections (since 2000)

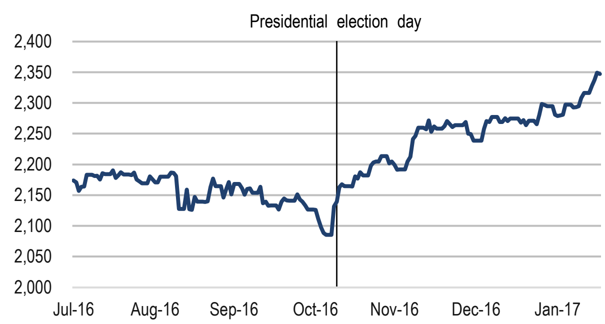


Source: Bloomberg; compiled by Daiwa.
Note: Average of index using data on presidential election day as 100.

As mentioned above, presidential elections can be said to often be followed by a rise in stock prices, a rise in the USD/JPY rate, and a slight decline in the Dollar Index. So, what will happen if Donald Trump, a strong Republican candidate for the 2024 presidential election, wins? When Trump won in 2016, the financial market responded with higher stock prices, a rise in the USD/JPY rate, and dollar appreciation (Charts 5-7). The reactions with stock prices and the USD/JPY rate were in line with anomalies, but the rise in the Dollar Index differed from the anomalies seen since 2000.

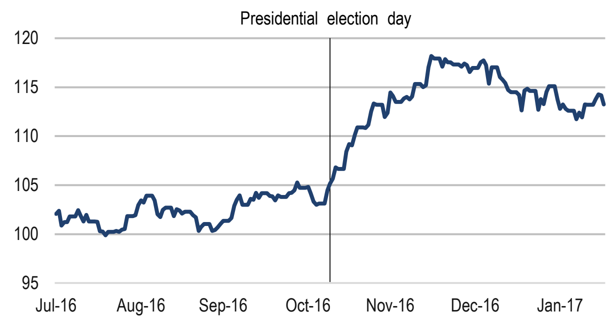
At the time, the reaction with stock prices was probably relatively strong because people had strong expectations that President Trump's policies would substantially boost the US economy. And, it is possible that the risk-on mode in the financial market had an influence that led to dollar appreciation, rather than depreciation. Furthermore, as the Fed was in a rate-hike cycle, it can be said that the dollar was easily supported from the perspective of interest rates, as well.

Chart 5: Stock Prices Around US Presidential Elections (S&P500)



Source: Bloomberg; compiled by Daiwa.

Chart 6: USD/JPY Rate Around US Presidential Elections

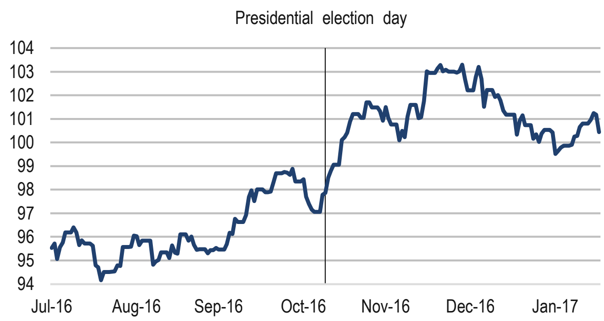


Source: Bloomberg; compiled by Daiwa.

If former President Trump were to win this year, the market would likely see higher stock prices and a rise in the USD/JPY rate based on these anomalies and the precedent in 2016, assuming the US economy does not fall into a recession. If former President Trump continues to advocate the policies he did during his term in office from 2017 to 2020, the Dollar Index is highly likely to rise due to similarities with 2016. Of course, how the financial market reacts following the presidential election will be affected profoundly by (1) how the financial market evaluates the policies of each candidate in the presidential election, which will gradually become clear from now on, and (2) how the Fed operates its monetary policy from now on. However, we can refer to past experience to some extent, provided the financial market is not in major turmoil.

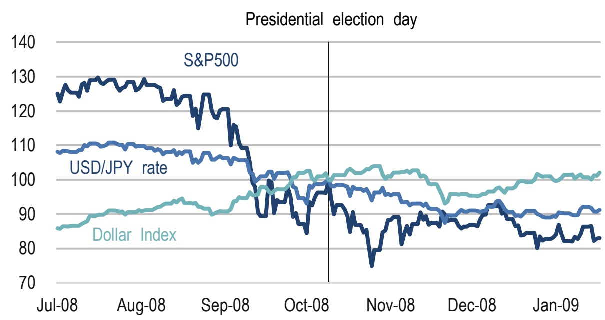
That said, if the US economy were to fall into a recession and that were to affect the financial market, we may see reactions that differ from past anomalies. For example, when the presidential election in 2008 was held immediately after the GFC, a downtrend in stock prices continued due to risk-off mode, which led to a decline in the USD/JPY rate and a slight rise in the Dollar Index. The upcoming presidential election will be held following monetary tightening by the Fed at an extraordinary pace. Therefore, if the US economy were to fall into a recession, we may see reactions that differ from anomalies seen in ordinary times. When forecasting the reactions we will see after the presidential election, we need to consider economic conditions and developments in the Fed's monetary policy, given past experience.

Chart 7: Dollar Index Around US Presidential Election in 2016



Source: Bloomberg; compiled by Daiwa.

Chart 8: Financial Market Around US Presidential Election in 2008



Source: Bloomberg; compiled by Daiwa.
Note: Index using data on presidential election day as 100.

IMPORTANT

Ratings
Issues are rated 1, 2, 3, 4, or 5 as follows:
1: Outperform TOPIX/benchmark index by more than 15% over the next 12 months.
2: Outperform TOPIX/benchmark index by 5-15% over the next 12 months.
3: Out/underperform TOPIX/benchmark index by less than 5% over the next 12 months.
4: Underperform TOPIX/benchmark index by 5-15% over the next 12 months.
5: Underperform TOPIX/benchmark index by more than 15% over the next 12 months.

Benchmark index: TOPIX for Japan, S&P 500 for US, STOXX Europe 600 for Europe, HSI for Hong Kong, STI for Singapore, KOSPI for Korea, TWII for Taiwan, and S&P/ASX 200 for Australia.

Target Prices
Daiwa Securities Co. Ltd. sets target prices based on its analysts' earnings estimates for subject companies. Risks to target prices include, but are not limited to, unexpected significant changes in subject companies' earnings trends and the macroeconomic environment.

Disclosures related to Daiwa Securities
Please refer to https://drp.daiwa.co.jp/rp-daiwa/direct/reportDisclaimer/e_disclaimer.pdf for information on conflicts of interest for Daiwa Securities, securities held by Daiwa Securities, companies for which Daiwa Securities or foreign affiliates of Daiwa Securities Group have acted as a lead underwriter, and other disclosures concerning individual companies. If you need more information on this matter, please contact the Research Production Department of Daiwa Securities.

Explanatory Document of Unregistered Credit Ratings
This report may use credit ratings assigned by rating agencies that are not registered with Japan's Financial Services Agency pursuant to Article 66, Paragraph 27 of the Financial Instruments and Exchange Act. Please review the relevant disclaimer regarding credit ratings issued by such agencies at: https://drp.daiwa.co.jp/rp-daiwa/direct/reportDisclaimer/credit_ratings.pdf. If you need more information on this matter, please contact the Research Production Department of Daiwa Securities.

Notification items pursuant to Article 37 of the Financial Instruments and Exchange Law
(This Notification is only applicable to where report is distributed by Daiwa Securities Co. Ltd.)
If you decide to enter into a business arrangement with our company based on the information described in this report, we ask you to pay close attention to the following items.

- In addition to the purchase price of a financial instrument, our company will collect a trading commission* for each transaction as agreed beforehand with you. Since commissions may be included in the purchase price or may not be charged for certain transactions, we recommend that you confirm the commission for each transaction. In some cases, our company also may charge a maximum of ¥2 million per year as a standing proxy fee for our deposit of your securities, if you are a non-resident.
- For derivative and margin transactions etc., our company may require collateral or margin requirements in accordance with an agreement made beforehand with you. Ordinarily in such cases, the amount of the transaction will be in excess of the required collateral or margin requirements**.
- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by our company.
- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.

* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.
** The ratio of margin requirements etc. to the amount of the transaction cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

When making an actual transaction, please be sure to carefully read the materials presented to you prior to the execution of agreement, and to take responsibility for your own decisions regarding the signing of the agreement with our company.

Corporate Name: Daiwa Securities Co. Ltd.
Registered: Financial Instruments Business Operator, Chief of Kanto Local Finance Bureau (Kin-sho) No.108
Memberships: Japan Securities Dealers Association, The Financial Futures Association of Japan, Japan Investment Advisers Association, Type II Financial Instruments Firms Association, Japan Security Token Offering Association