The near-term, post-election environment appears challenging for emerging markets, despite tailwinds related to China's stimulus and further Federal Reserve rate cuts. (UBS)

What does a decisive Republican victory mean for emerging markets?

07 November 2024, 5:55 pm CET, written by UBS Editorial Team US Editorial Team

The Republican Party achieved a historic victory in this week's US election, securing a strong mandate to effect change with significant influence across the executive, legislative, and judicial branches of government.

Donald Trump won on a platform advocating lower taxes, deregulation, strict immigration control, a focus on domestic interests over international affairs, and higher trade tariffs. There is considerable uncertainty regarding the sequence and extent of policy implementation. However, the strength of the mandate may narrow the gap between campaign proposals and actual policies.

Few emerging markets are expected to thrive amid increased uncertainty over global trade, US waning support for multilateral institutions, and a deepening fragmentation of the global economy. The cross-border movement of people, capital, goods, and services is likely to face increased friction; this will be coupled with higher US interest rate volatility, as markets digest Trump's fiscal proposals. Indeed, the near-term post-election environment appears challenging for emerging markets, despite tailwinds related to China's stimulus and further Federal Reserve rate cuts.

Equities

Even in this complex backdrop, we expect emerging market stocks to deliver mid- to high-single-digit returns driven by earnings growth. North Asian markets, particularly Taiwan, offer appealing upside potential from the artificial intelligence

wave. India, with its domestic focus and "geopolitical swing state" status, also presents attractive growth opportunities. We also favor South Africa, benefiting from domestic reform momentum and favorable valuations.

For China, Trump's victory clouds the near-term outlook. Nonetheless, recent domestic policy signals since late September indicate a strong commitment to stabilizing the economy, providing a cushion for market sentiment. We are monitoring the upcoming National People's Congress Standing Committee meeting, expected to unveil more detailed support addressing cyclical and structural challenges.

Higher tariffs could negatively impact companies with significant US revenue exposure. Mexico appears especially vulnerable, at least initially. We expect the bilateral relationship to eventually stabilize, as Mexico's role in North American manufacturing is crucial for competitiveness and for keeping US inflation low.

Bonds

Emerging market bond spreads over US Treasuries have been supported by resilient global growth. Emerging market sovereigns are also seeing moderate net positive ratings actions this year, concentrated in countries that have improved their fiscal trends. Sovereigns like Brazil, Costa Rica, Paraguay, Oman, Serbia, Qatar, and Turkey have been upgraded, helping the asset class remain resilient to recent US interest rate volatility.

Emerging market US dollar-denominated bonds—although largely rated as investment grade—offer interest rates of 6.5-7.0%, well above those of US high-yield bonds. We expect emerging market bond spreads to remain stable over the next six to 12 months, allowing investors to achieve high-single-digit returns. Emerging market bonds also provide broad diversification across countries, limiting exposure to those targeted by US tariff policy.

Currencies

Emerging market currencies may remain under pressure in the near term due to upward moves on US Treasury yields and uncertainties surrounding Trump's tariffs. However, it is unlikely that the US dollar's gains will be sustained. Unlike in 2016, the Fed is in a cutting cycle, the fiscal deficit is higher, and US dollar valuations are stretched. Thus, we maintain a view of medium-term dollar weakness, which should eventually support emerging market currencies.

The CNY and MXN are particularly exposed to US policy changes. We have raised our USDCNY forecasts for the next year to as much as 7.5 to reflect moderate depreciation. In the short term, the People's Bank of China (PBoC) is likely to contain currency spikes. However, in the medium term, the risk for the currency will likely be skewed toward depreciation.

In the short term, we believe that the MXN could depreciate to as much as 21 against the US dollar, given external trade and tariff uncertainty, and domestic reform noise. However, we expect the Mexican peso to eventually recover to around 19.5 by the end of 2025, as we believe the fundamentals of the bilateral relationship with the US will hold.

Main contributor – Alejo Czerwonko

Original report - **What does a decisive Republican victory mean for emerging markets?, 7 November 2024.**

The document and the information contained herein is intended for UBS internal use only and solely for the UBS employee to whom it was provided. It may in no circumstances be distributed outside of UBS. Information contained in this document has not been tailored to the specific needs, investment objectives, personal and financial circumstances of a client or any other recipient outside of UBS. This document shall not be construed to include any legal or tax advice, investment research, sales prospectus, an offer or a solicitation of an offer to enter in any investment activity. Neither UBS nor its directors, employees or agents accept any liability for any loss or damage arising out of the use of all or any part of this document. For further information, please contact the document owner.

Important information
As a firm providing wealth management services to clients, UBS Financial Services, Inc is registered with the U.S. Securities and Exchange Commission (SEC) as an investment adviser and a broker-dealer, offering both investment advisory and brokerage services. Advisory services and brokerage services are separate and distinct, differ in material ways and are governed by different laws and separate contracts. It is important that you carefully read the agreements and disclosures UBS provides to you about the products or services offered. For more information, please visit our website at www.ubs.com/workingwithus.
© UBS 2024. All rights reserved. UBS Financial Services Inc. is a subsidiary of UBS AG. Member FINRA/SIPC.
There are two sources of UBS research. Reports from the first source, UBS CIO Global Wealth Management, are designed for individual investors and are produced by UBS Global Wealth Management (which includes UBS Financial Services Inc. and UBS International Inc.). The second research source is UBS Group Research, whose primary business focus is institutional investors. The two sources operate independently and may therefore have different recommendations. The various research content provided does not take into account the unique investment objectives, financial situation or particular needs of any specific individual investor. If you have any questions, please consult your Financial Advisor. UBS Financial Services Inc. is a subsidiary of UBS AG and an affiliate of UBS International Inc.