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GLOBAL X ETFs INVESTMENT STRATEGY

Investment Strategy Insights

Election Implications in Focus: Catalysts, Clean Energy, and Infrastructure

The 2024 election cycle is in full swing, bringing new uncertainties to the markets but also potential opportunities. In this piece, the focus is given to the market's search for catalysts amid geopolitical volatility and what U.S., France, and UK election outcomes may mean for Infrastructure and Clean Energy investment themes.

Key Takeaways:

- Election and geopolitical risks may make it harder for markets to find new catalysts, especially if they contribute to reversing inflation's downward trend.
- U.S. Clean Energy themes likely face headwinds in a second Trump presidency, while Infrastructure Development and Defence Tech appear poised for continued growth.
- France and the UK elections show climate change and new construction are a priority.

Markets Seek Fresh Catalysts Amid U.S. Election Uncertainties

U.S. CPI numbers for June were lower-than-expected at 3.0% and 3.3% for the headline and core measures, respectively, but they are still running above the Federal Reserve's 2% target.¹ Core services inflation is now just below 3.0%, marked by an encouraging cooldown of domestic inflation with the shelter index declining slightly. As a result, markets participants are now pricing over two rate cuts this year compared to a maximum of two before the inflation release.

However, it is believed that that markets may be overreacting to the good inflation print and overlooking political and global trade tail risks that could materially derail inflation's march back to 2%. While the U.S. economy is slowing, unemployment rate remains low from historical standpoints and services and manufacturing activities remain in expansion territory according to the June PMIs.² The current economic stance does not warrant urgent nor aggressive rate cuts.

Should the Fed determine that economic conditions warrant a lower benchmark rate than the current 5.25–5.50%, the window to do so could close soon. One reason is that if Donald Trump wins the presidential election in November, his agenda of more protectionist policies and higher tariffs could reverse inflation's downward trend. That scenario would possibly add to the current supply chain disruptions that caused freight costs to almost quadruple since November 2023.

As it is, markets may be underestimating the risks of these higher freight costs caused by geopolitical tensions in and around the Suez Canal.³ High shipping costs translate into higher costs of production and eventually upward pressure on retail prices. The situation recalls the inflationary effects of pandemic-related supply chain issues. Based on the timing of those issues in 2022 and inflation's subsequent rise, inflation could reverse trend and tick higher by year-end.

In the near term, with a soft-landing scenario and easing cycle already factored in, markets are looking for new catalysts. However, catalysts could be difficult to find if inflation risks turn material and push out a Fed pivot to meaningfully lower rates. Also, markets could turn more volatile in the run up to the election, as its outcome could significantly alter fiscal policies and the broader economic outlook.



For the longer-term, if the Democrats prevail, the Clean Energy theme likely presents opportunities for investors. Democrats consistently advocate for robust federal support for clean energy, and the trend of substantial federal investments and incentives for clean energy infrastructure under the Biden administration would be expected to continue. The Inflation Reduction Act (IRA), which allocated \$369 billion towards clean energy initiatives, is one example.⁴ The IRA aims to lower greenhouse gas emissions, create millions of jobs, and foster a sustainable energy economy.

On the other hand, a Republican victory would likely result in increased investments in infrastructure to further promote reshoring and defence. Historically, Republican administrations favour higher defence spending, as evidenced by proposals like Senator Roger Wicker's plan to increase defence spending to 5% of GDP, which would add \$55 billion to the FY 2025 defence budget.⁵

Beyond election scenarios and across time frames, tech can continue to catalyse markets. Recent advancements, particularly in Artificial Intelligence (AI), signal that they have the potential to drive productivity gains and efficiency across various sectors. In June, technology trade show Computex 2024 event showcased numerous groundbreaking innovations, highlighted by AI integration in industries such as video games, healthcare, and robotics.

France and UK Elections Appear to Give Clean Energy and Infrastructure a Boost

Recent elections resulting in political shifts to the right could lead to more protectionism and heightened focus on Europe's technological and energy independence. Increased defence spending and tougher immigration policies are also likely outcomes.

That said, in France, the surprise win by the leftist Nouveau Front Populaire (NFP) in the parliamentary election may bring new infrastructure and climate-focused opportunities.⁶ The NFP supports a comprehensive approach to infrastructure development, a strong push for renewable energy, and a cautious but strategic use of nuclear power to meet climate goals. Key initiatives include modernising rail networks, expanding public transport, and significantly increasing investments in solar and wind energy capacities.

In the UK, Keir Starmer's Labour Party victory brings a seemingly stable political backdrop that markets may perceive as positive. The centre-left Labour government plans significant investments in clean energy through the establishment of Great British Energy, a new publicly owned company. Besides this, the Labour government has announced up to £500 million per year of public investments into low-carbon industries such as wind and solar energy, and carbon capture from 2026.⁷ Infrastructure reforms are also on the agenda, with plans to accelerate the construction of clean energy infrastructure and housing projects.

Footnotes

1. Bureau of Labor Statistics, June 2024 release. Consumer Price Index (CPI) News Release : U.S. Bureau of Labor Statistics (bls.gov)
2. S&P Global US Sector PMI (spglobal.com)
3. Bloomberg data as of 17 July 2024.
4. 8.18 InflationReductionAct_Factsheet_Final.pdf (energy.gov)
5. Powerful GOP senator eyes ships, jets, nukes in defense spending surge (defensenews.com)
6. France election 2024: What the manifestos say on energy and climate - Carbon Brief
7. Labour's Manifesto website accessed as of 23 July 2024. Make Britain a clean energy superpower



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