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GEOPOLITICAL STRATEGY

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United States: Trump's Comeback — Brace For Headlines, Expect Policy Surprises

- The Trump administration's policies will likely be more moderate than his rhetoric suggests.
- This moderation applies to fiscal, tariff, and key foreign policy areas.
- A window of geopolitical risk exists between now and Trump's inauguration.

In This Report

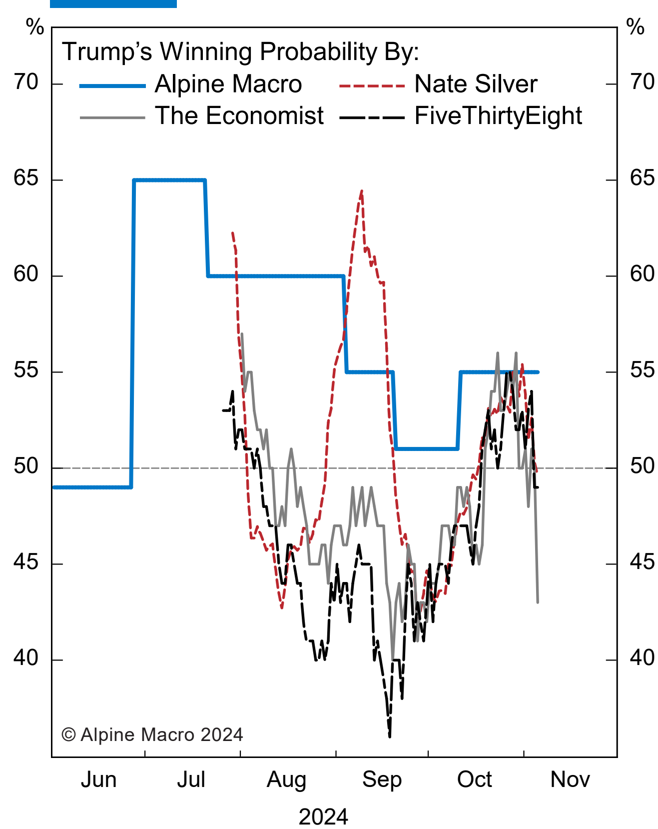
Donald Trump has won the Presidency, as we expected. A Republican sweep appears likely. Yet, control of Congress remains undecided at the time of writing: Republicans hold a Senate majority (at least 52 seats, with more likely as votes are finalized) and appear on course to win a majority in the House. Currently, Republicans have 212 seats in the House (218 needed for a majority), Democrats have 197, and ~26 seats are yet to be decided. Expectations center on a narrow Republican majority of around 222 seats[1].

Since Biden's meltdown in the June 27 debate, we viewed this as Trump's election to lose. When Harris emerged as the likely Democratic nominee (July 21), we argued she was similarly unviable[2]. This was based on our analysis of polling (which underestimated Republican strength) and structural factors. While our estimates moved over time, we consistently saw Trump as the likely winner (**Chart 1**).

1 Decision Desk HQ, 2024 General Election Results

2 Alpine Macro *Geopolitical Strategy* "United States: Harris Isn't Much More Viable Than Biden" (July 22, 2024).

Chart 1 Presidential Election Forecasts



Note: Series end before close of polls on Nov. 05

While going forward we will analyze Trump's agenda in greater detail as we gain clarity on his team, policy priorities, and the specific congressional makeup, in this report, we highlight a broad area where we differ from the analytic consensus in significant ways. Namely, we expect the Trump administration will govern more moderately than Trump's rhetoric suggests.

Domestic Moderation?

Listening to media and political analysts, one might think Trump is on the brink of becoming an authoritarian leader or is poised to crash the economy with massive tariffs, blow up the deficit, spike inflation, meddle with the Fed, provoke geopolitical crises, or abandon U.S. allies to the tender mercies of rival powers.

We don't buy most (or any) of these mainstream views.

Take fiscal policies for starters. There's concern that Trump will increase deficits. His administration likely aims to extend the 2017 Tax Cuts and Jobs Act (TCJA), and this will be a priority.

However, there are additional proposals being discussed to reduce the corporate tax to 15% for domestic manufacturers, offer small-business tax breaks, and cut specific taxes, like those on Social Security benefits and tips. There is also discussion of increased spending on childcare, healthcare, defense, and immigration enforcement.

To fund these, Trump has suggested a baseline 10% tariff, with higher rates (up to 60%) for countries like China, alongside budget cuts to departments like Education and efforts to reduce governmental waste and fraud. Clearly those numbers do not quite add up[3].

However, we think most of these proposals won't materialize, even with a Republican Congress. While tariffs will likely rise, the 10% baseline and 15% corporate tax cut are likely overstated and served as campaign bluster.

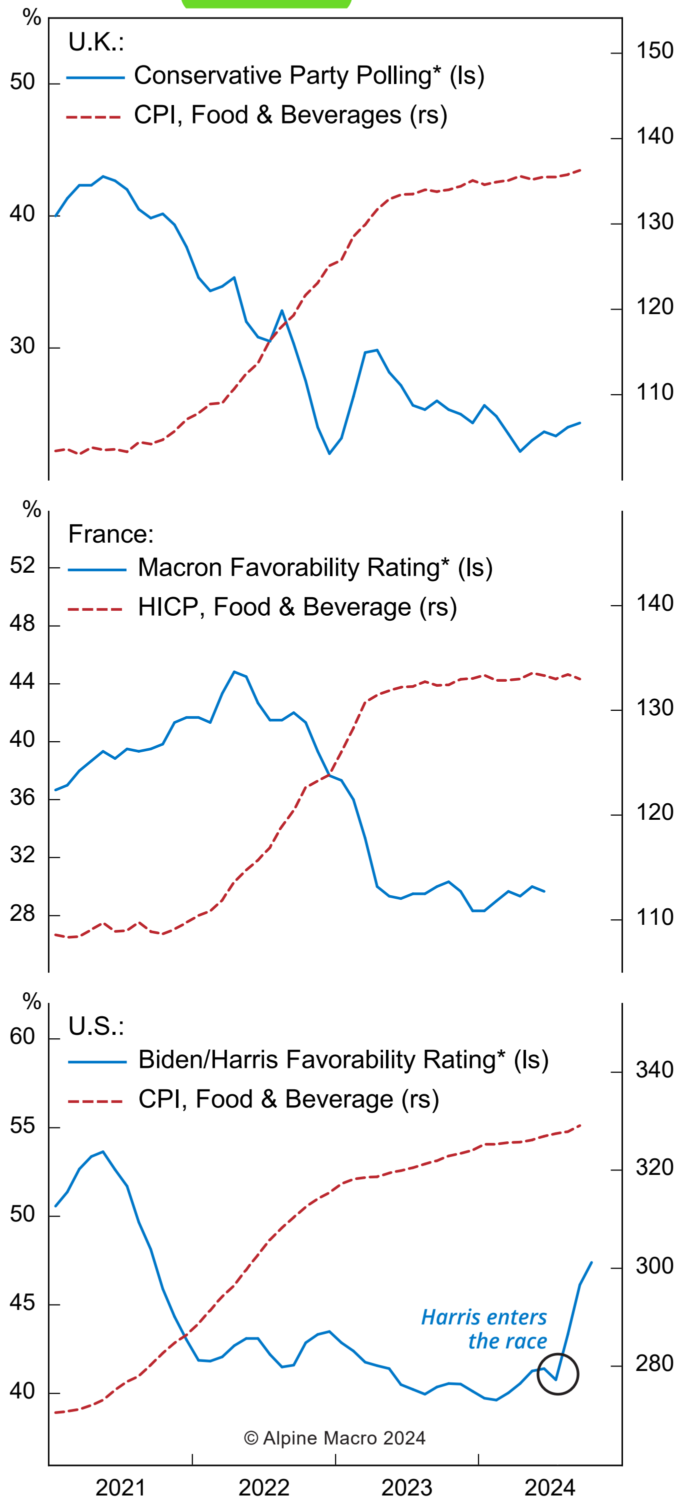
While the second Trump administration will aim to cut taxes, reduce regulations, and raise tariffs, it will be more fiscally cautious than feared. There are three reasons why:

- First, the Trump administration aims to maintain market and economic stability. For Trump, market performance has long been a measure of his own governing success, so he is unlikely to enact policies that would significantly disrupt markets and growth.
- Second, and most critically, the Trump team understands that governments overseeing inflation spikes court political defeat. **Chart 2** shows that rising food prices contributed to the political downfalls of incumbent administrations in the U.K., France, and the U.S.[4] Inflation spikes are political poison. Why would Trump care, given this is his last term in office? Because his administration faces the 2026 midterm elections. If Democrats were to win Congress in 2026, this would leave

3 Committee for a Responsible Federal Budget "The Fiscal Impact of the Harris and Trump Campaign Plans" (October 28, 2024).

4 Yes, the price of things like eggs was a main reason why Harris did not win the election, as a quasi-incumbent.

Chart 2 Incumbents Doomed By Higher Price Levels



*Shown as 3-month moving average

Trump as a lame-duck president in his final two years (2026-28), facing a hostile Congress, investigations, and potentially further impeachments.

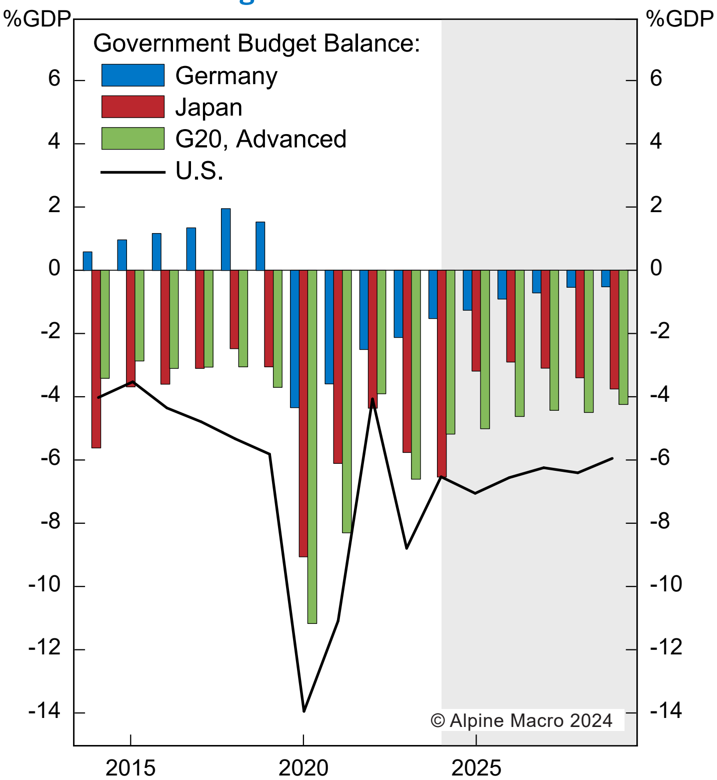
- Finally, Trump's economic team will likely be Wall Street-friendly and more economically orthodox than expected, with a Reagan-like, *laissez-faire* approach — except with an emphasis on higher tariffs and on U.S. reindustrialization, things for which there is a measure of bipartisan support.

Trump's economic advisors — both formal and informal — include figures like Scott Bessent, John Paulson, Howard Lutnick, Kevin Hassett, David Malpass, and Jay Clayton, and Stephen Moore. Former officials like Steven Mnuchin and Gary Cohn may also play some role. These advisors or similar, which are likely to dominate Trump's economic team, tend to be market-friendly.

They are also not fiscal doves. Most Trump economic advisors are at least somewhat concerned about the deficit. With a Republican-controlled Congress, Trump may pursue very material cuts or rollbacks to programs like the CHIPS Act or the Inflation Reduction Act through budget reconciliation, as well as reductions in some discretionary spending programs. That said, we do not think budget deficits will be less than 3% of GDP, and **Chart 3** shows the likely progression of U.S. budgetary deficits. Ultimately austerity is politically unpalatable, but a Trump administration with a Republican Congress may aim to keep the deficit closer to 3% of GDP, rather than the projected 6-7%.

A Republican sweep may offer the best chance for more significant spending cuts. While markets

Chart 3 U.S. Budget Deficits Likely To Stay High



Note: Shading denotes projections; source: IMF

often expect a split Congress to curb spending, that isn't necessarily the case. If Democrats were to win the House, the Trump administration would likely negotiate to extend the 2017 tax cuts, requiring compromises to also fund Democratic spending priorities. This fiscal "horse trading" could lead to increased, unpaid-for spending.

This dynamic has already been observed under Biden, where, despite a split Congress, fiscal deficits stayed high over the past two years.

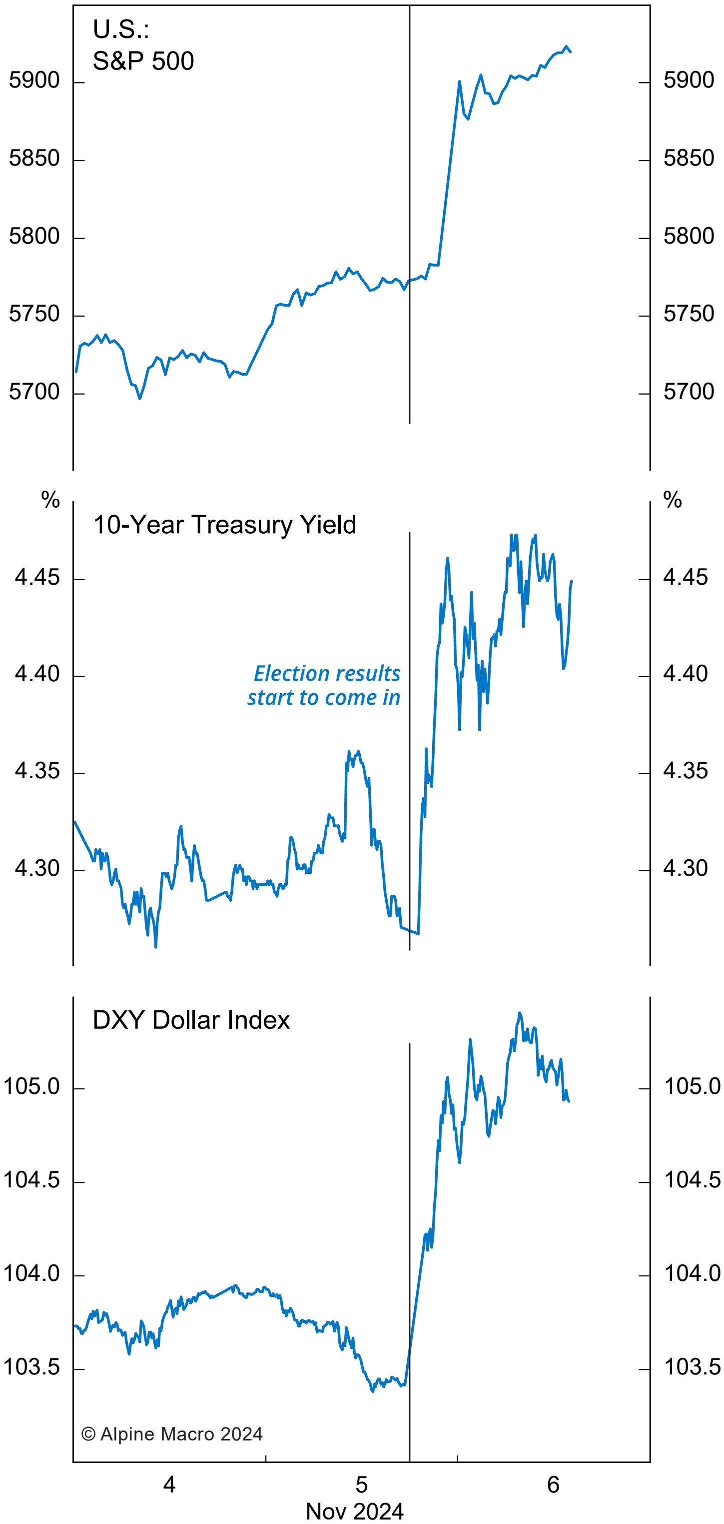
The same political considerations also apply to Trump's preference for higher tariffs. His administration is unlikely to impose tariffs that cause economic or political disruptions, and will likely favor imposing tariffs at lower levels than expected, and in a targeted way (e.g., the S. 301 tariffs that were aimed largely at intermediate goods). There will be a gradual, staggered approach to such measures. The idea of getting rid of income taxes and replacing them with tariff revenues is not likely to fly politically, and again is campaign-trail bombast.

Which is not to say that many in Trump's economic team do not support tariffs. Some, like former U.S. Trade Representative Robert Lighthizer, advocate significantly higher tariffs, as does former Trump advisor Peter Navarro. Yet they are unlikely to dominate economic policymaking, which will likely be overseen by the more market-friendly advisors – which will moderate Trump's own consistently pro-tariff stated preferences.

Consequently, we expect tariffs to be well below 10% across the board, though higher tariffs on China may be prioritized (though not at 60%). On tariffs targeting allies, we anticipate pragmatism will prevail, and that threats of tariffs in trade negotiations will be used as leverage to gain market access, or to get allies to follow U.S. economic policies on China.

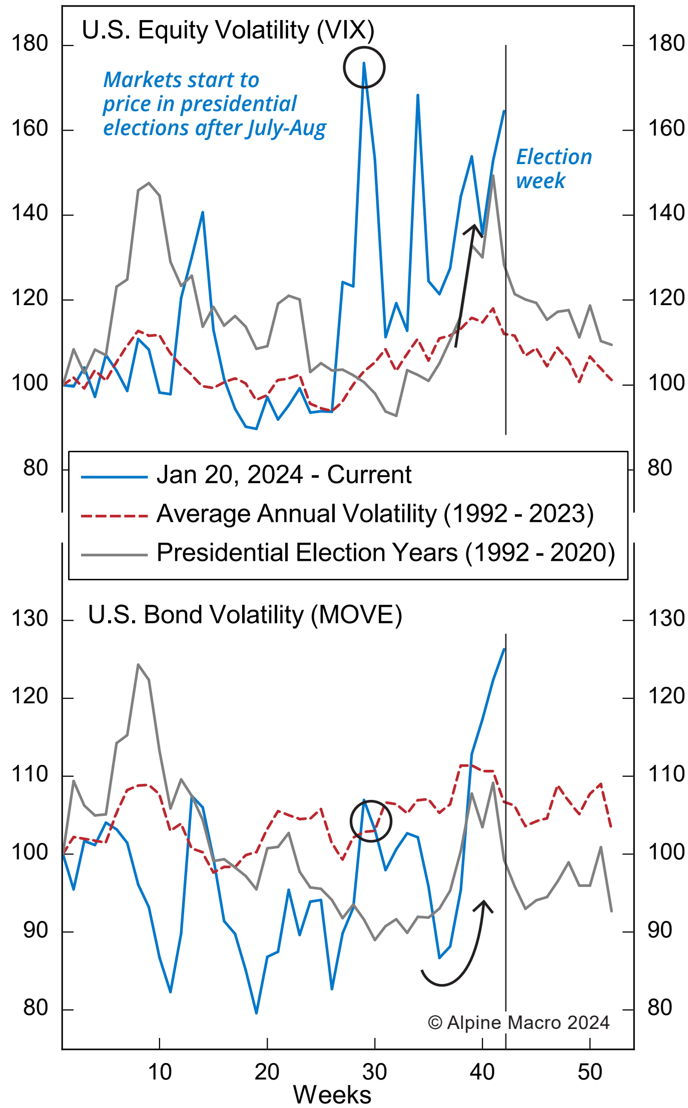
Lastly, Trump is unlikely to interfere with the Fed, or try to limit its independence. Trump will likely criticize Chair Powell, as he did during his first term, and may at times threaten to fire Powell or change the workings on the FOMC. However, these are likely to be just threats. The markets' negative reactions to any such possibility, as well as Congressional opposition (including from Republicans) will significantly constrain Trump from taking such actions. One thing to potentially watch for are legislative measures to increase congressional oversight of the Fed, such

Chart 4 Market's Immediate Reaction To Trump's Victory



Source: Bloomberg Finance L.P.

Chart 5 Volatility Should Come Down Post-Election



Note: Presidential election years are calculated from Jan 20 of the election year to Jan 20 of the next year, using the Jan 20 Presidential inauguration date as year-markers, with values rebased to 100 on Jan 20

as were proposed in the early 2010s — yet for now these are not on the legislative body's agenda.

This is not to say that Trump will abandon his campaign promises. He will not, but as during his first term he will tweak them to make them more palatable to consumers, voters and markets. A harder line on immigration enforcement and border is likely, which, depending on implementation details, could worry labor economists.

On the plus side, deregulation will be emphasized, as will be cost-cutting across the government (e.g., Elon Musk is likely to play some role in this sphere). The bottom line is that this will be a market-friendly administration, that has strong political incentives to soften some of its more radical policy proposals.

Markets responded as anticipated to Trump's victory: stocks and the USD rose, alongside the U.S. 10-year Treasury yield (**Chart 4**). U.S. equities are pricing in deregulation and lower corporate taxes, while bond markets, similar to 2016, reacted to concerns over potential higher fiscal spending.

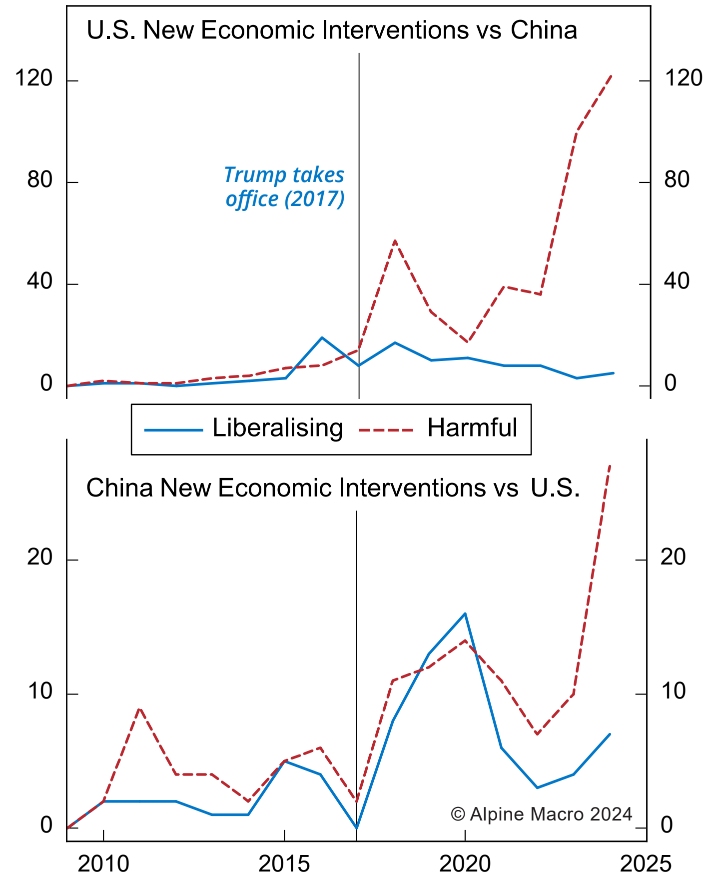
Typically, post-election market volatility subsides in both equities and bonds, with stocks and bonds settling in a new steady state but fear of fiscal deterioration is overdone (**Chart 5**).

Foreign Policy Realism

We expect significant headline risks and rhetoric from Trump that may offend or rattle global political actors, as during his first term. However, beneath the noise, a pragmatic, realist approach to national interests is likely. Except in the Middle East, the administration will aim to minimize conflicts, though often through strong rhetoric and saber-rattling (i.e., headline risks), which as during Trump's first term could be disconcerting to markets.

Trump is unlikely to abandon Ukraine. A recent Alpine report argued this[5], noting that U.S. national interest and domestic constraints favor continued

Chart 6 U.S.-China Policy Interventions



Note: Policy actions are based on the implementation date, and are adjusted for reporting lags; source: Global Trade Alert

support for Kyiv, something which Trump has also acknowledged. The U.S. and NATO will press for a truce next year, though negotiations may be challenging. Pressure will also increase on NATO and EU allies to boost their military spending. In short, Trump will not withdraw support from NATO or from Ukraine.

The administration's main strategic focus will be on managing the U.S. rivalry with China, which will be marked by continued tensions and by partial

5 Alpine Macro *Geopolitical Strategy* "The Russia-Ukraine War: Lurching Toward An Uneasy Truce?" (October 11, 2024).

economic decoupling. Chart 6 illustrates the intensifying trade and investment policy restrictions between the U.S. and China since Trump's first term — these will likely deepen. Yet Trump's approach could be transactional, and there is a chance he will pursue a Phase II economic deal with China, though the success of that is uncertain.

Overall, we think the approach of the Trump administration to China will be realist, looking to manage tensions with a focus on the U.S. national interest. Contrary to what many fear, we do not think that there will be a conflict over Taiwan, and Taiwan's status will remain as-is.

The Trump administration aims to reduce tensions in the Middle East and revive the Abraham Accords, its key achievement in the region. However, this approach will likely involve a more hawkish stance toward Iran, potentially increasing the risk of conflict in the short to medium term.

A Geopolitical Risk Window

Before Trump's inauguration on Jan. 20, 2025, an obviously Democratic lame-duck government under President Biden may invite strategic challenges from adversarial nations. The primary concern is potential escalation in the Middle East. Iran, fearing that Trump may give Israel more freedom to act, might declare itself a nuclear power before Trump's inauguration, risking a quick response from Israel or the U.S., or it may stir regional instability. That said, an opposite argument can be made, that Iran will try to tone down tensions, fearing an incoming Trump administration. Overall, we think the first scenario is more likely than the second, given Iran's domestic dynamics. Lmao what does that even mean?

Israel, aware of Trump's desire to end Middle Eastern hostilities, could also preemptively target Iran's nuclear or oil facilities before Jan. 20, especially given the Biden administration's lame-duck status and thus lack of influence. The recent dismissal of Israel's more moderate Defense Minister could increase the chances of decisive action against Iran, and thus the risk of major regional escalation.

Moderate?!! Hahahahahahaha

North Korea is another potential hotspot, and it could conduct a nuclear test to try to gain leverage with the incoming Trump administration, in hopes of future talks. This could raise considerable fears in South Korea, especially given North Korean troop support for Ukraine.

Additionally, concerns exist over a potential Russian offensive against Ukraine before Trump's inauguration, though adverse weather will likely hinder this, U.S.-China tensions appear less immediate.

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