ALPINEMACRO
A Unique Mind On The Markets

GEOPOLITICAL STRATEGY

June 5, 2024

A 2024 Elections Preview (Part II): Europe's Rightward Drift & The U.S.' Legal Rift?

- European Parliament (E.P.) elections will lead to right-wing gains.

- A right-leaning E.P. will favor national-security industries (industrials, aerospace & defense, semiconductors) and cheaper energy, while creating headwinds for renewable energy sectors.

- Uncertainty surrounds the impact of Trump's New York criminal conviction on his candidacy. Markets will not price in the elections until after July, and for now will ignore Trump's legal issues. However, rising political unrest in the U.S. could impact market volatility this year.
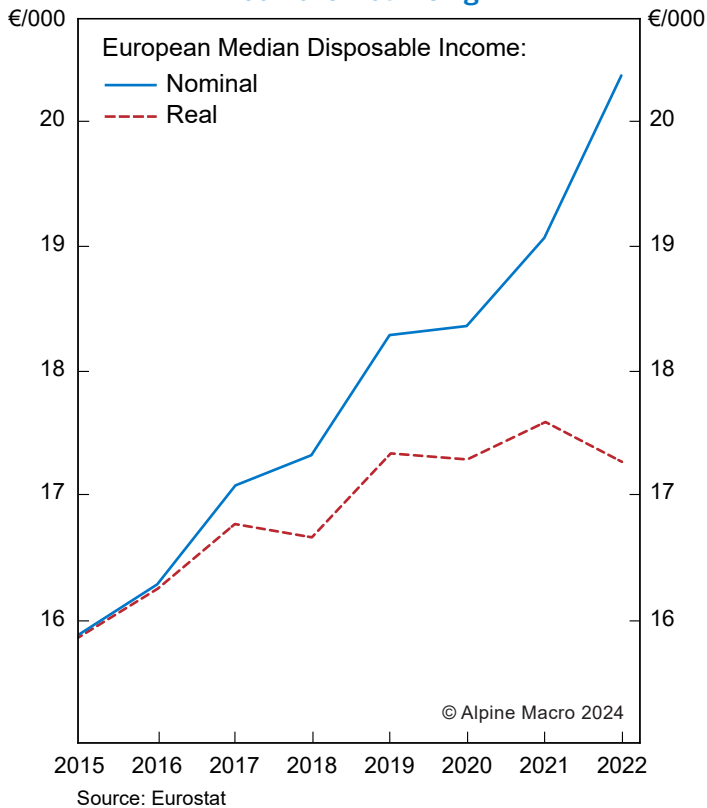
In this report, we continue our analysis of consequential upcoming 2024 elections, focusing on the June 6-9 European Parliament elections and providing a brief update on the U.S. elections considering former President Trump's recent felony convictions. A follow-up report (Part III) will focus on the upcoming U.K. general elections on July 4.

The European Parliament's Rightward Drift

Polling indicates that right-wing parties and coalitions will make significant gains in the June 6-9 European Parliament elections. These elections will determine which party grouping will dominate the legislature, drive European-level legislation, and select the next European Commission President and Commissioners.

The E.P. has been dominated by a centrist coalition comprising of the center-right EPP, the center-left S&D, and the liberal Renew Europe, who have held the majority since 2019. However, voter discontent over inflation, rising prices and declining standards (**Chart 1**), the cost of energy, and immigration has fueled a rise in support for anti-establishment right-wing parties.
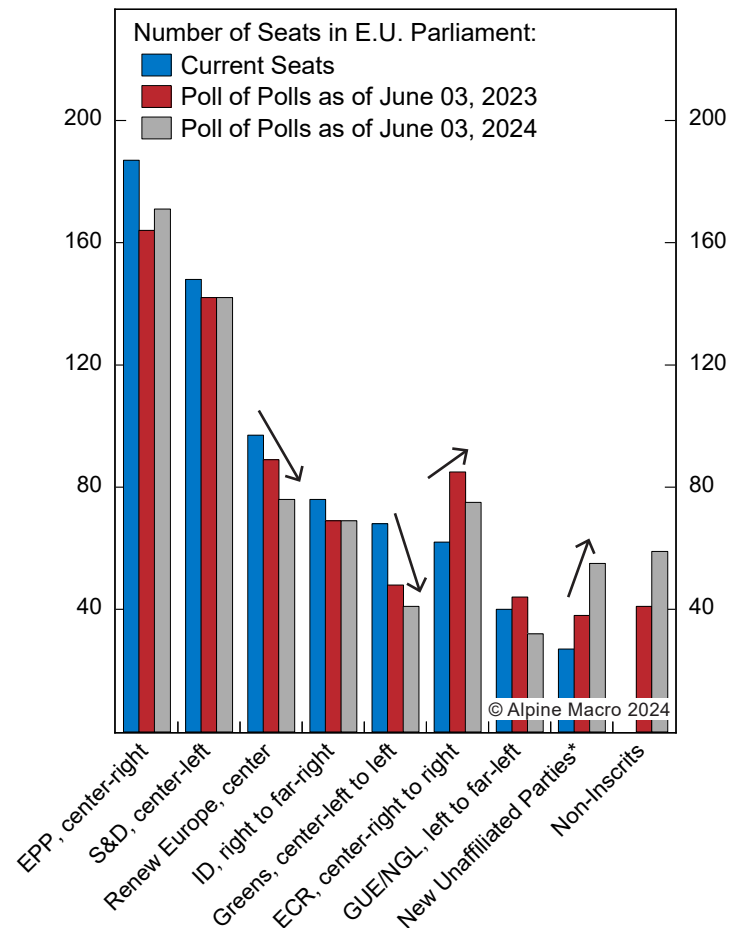
As a result, the right-wing European Conservatives and Reformists (ECR) and far-right Identity and Democracy (ID) political groupings are likely to increase their representation in the 720-member body, with substantial gains expected by parties such as France's National Rally and Italy's Brothers of Italy. Other unaffiliated right-wing parties, such as Germany's AfD, also seem poised to perform well. Renew Europe and the Green parties of the Greens/

€/000 — European Median Disposable Income:
— Nominal
-- Real

Source: Eurostat

© Alpine Macro 2024

Number of Seats in E.U. Parliament:
- Current Seats
- Poll of Polls as of June 03, 2023
- Poll of Polls as of June 03, 2024

Categories: EPP, center-right; S&D, center-left; Renew Europe, center; ID, right to far-right; Greens, center-left to left; ECR, center-right to right; GUE/NGL, left to far-left; New Unaffiliated Parties*; Non-Inscrits

© Alpine Macro 2024

*New unaffiliated parties are largely right-wing
Note: At least 361 seats needed to form a majority; source: Politico

European Free Alliance are expected to lose seats (**Chart 2**).

Which party groupings will form the new E.P. governing majority? One undoubted outcome is that the center-right EPP will remain the dominant party and the lynchpin of any governing coalition. Two possibilities:

1. The baseline is that the current centrist coalition will tenuously hold, as the EPP and the S&D have maintained relatively stable voter support. Even if the liberal Renew loses support, the three are still likely to secure a 361+ seat majority in the 720-member body (**Chart 3**).

2. The less likely outcome is a massive and unexpected rightward shift in voter preferences. This

entails the EPP forming a right-wing coalition with the ECR and some non-affiliated national parties. The ID will not be allowed to join such coalition but could provide ad hoc voting support. However, this outcome is now unlikely as the rise of right-wing parties in polls has recently stalled due to political fragmentation and some controversies.

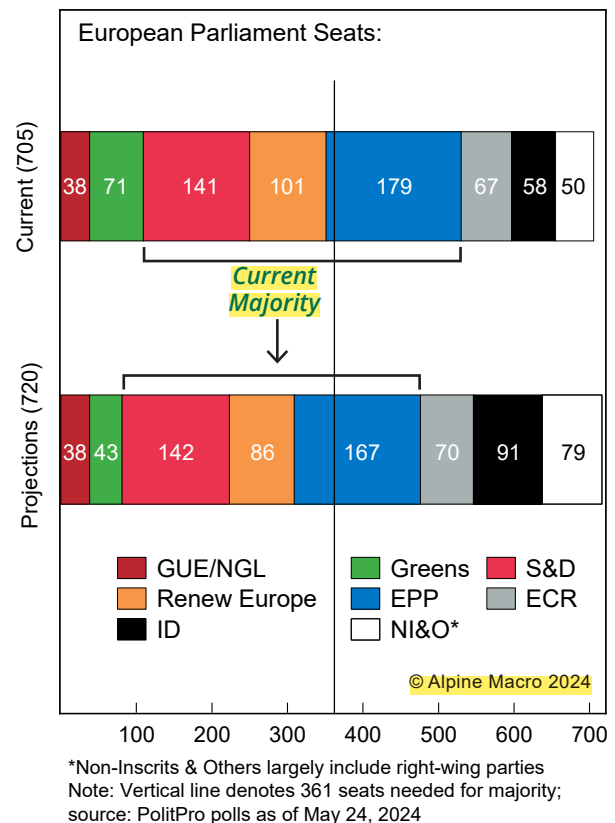Even in the baseline scenario, despite the seeming continuation of the status quo, the rightward

shift in the E.P. composition will grant significant influence to right-of-center parties. These parties are expected to gain at least 25% of parliamentary seats and possibly as much as a third, giving them considerable leverage and veto power. Consequently, the right-wing of the E.P. will exert policymaking influence and pressure the EPP to govern "from the right". The EPP may also choose at times to rely on right-wing votes to pass its preferred policies and possibly even to re-elect Ursula von der Leyen as the European Commission President.

After the elections, it will take most of the year to select the new E.U. governing structures. The 27 E.U. heads of state will have to select the President of the European Council and propose the new European Commission President. Ursula von der Leyen is likely to be proposed as the representative of the largest party (EPP) and has a solid chance of being re-elected. The policy agenda of the next European Commission, and the different commissioners, will be confirmed over the summer and fall.

Europe's Likely Policy Shifts

The rightward shift in the E.P. will have significant policy implications. In the baseline scenario, the current governing coalition stays in power, but a more right-wing E.P. has greater influence over policymaking. The unlikely scenario of a right-wing governing coalition would be more chaotic and un-predictable, but the policy shifts would be similar, though far more pronounced. In either case, green energy mandates and policies will be deemphasized, while the new E.P. and Commission will push for stronger defense and industrial policies, including

Chart 3 **A Similar Governing Coalition Is Likely In the Next E.P.**

European Parliament Seats:

Current (705): GUE/NGL 38 | Greens 71 | S&D 141 | Renew Europe 101 | EPP 179 | ECR 67 | ID 58 | NI&O* 50

Current Majority

Projections (720): GUE/NGL 38 | Greens 43 | S&D 142 | Renew Europe 86 | EPP 167 | ECR 70 | ID 91 | NI&O* 79

Legend:
- GUE/NGL (dark red)
- Greens (green)
- S&D (red/pink)
- Renew Europe (orange)
- EPP (blue)
- ECR (gray)
- ID (black)
- NI&O* (white)

© Alpine Macro 2024

100 200 300 400 500 600 700

*Non-Inscrits & Others largely include right-wing parties
Note: Vertical line denotes 361 seats needed for majority;
source: PolitPro polls as of May 24, 2024

tariffs and more protectionist measures. There will also be a push for more market-friendly policies within the E.U., possibly favoring some deregulation. Stronger anti-migration policies are likely.

Defense and Foreign Policies: A more right-wing E.P. will emphasize deeper defense integration. While an E.U. army remains unlikely, more common defense initiatives are expected. The biggest change could be higher defense spending by member states, which seems likely. Coordination with the U.S. will remain high, with stronger alignment on policies related to Russia and China and enhancing NATO capabilities. These trends will persist even if Trump is elected. Lastly, support for Ukraine will remain

strong − despite likely electoral gains by some pro-Russia right-wing parties.

Industrial and Trade Policies: A more right-wing E.P. will support re-industrialization plans, emphasizing high-tech fields like semiconductors and securing critical supply chains. However, the lack of funding for subsidies comparable to the U.S. and China and disagreements between member states will make E.U. industrial policies less effective. To compensate, the E.U. may lean more heavily on strategic trade protectionism. Thus, trade and investment restrictions will continue to mount, driven by greater geopolitical alignment with the U.S. on China and Russia. Chart 4 shows how E.U. vs. China policy interventions harmful to free trade and investment are increasing in a tit-for-tat fashion.

Competitiveness: A report by Mario Draghi, expected in June, could set the agenda for the next European Commission. It is expected to argue for pan-European consolidation in telecoms, energy, and defense, favoring large companies.

A push for a Capital Markets Union is likely to have consensus support in the E.P., though legislation will take time to craft. A banking union is also discussed, but creating a common deposit insurance scheme will be challenging.

Some deregulation is also possible, particularly on Artificial Intelligence (AI), as the E.U.'s stringent AI regulation is stifling the nascent industry. (We will discuss the global politics of AI and their market implications in an upcoming report).

Fiscal and Monetary Policies: The immediate fiscal impact of the elections will be minor, as the next E.U.

Chart 4　**E.U.27 - China Policy Interventions**

EU27 New Economic Interventions vs. China:

Liberalising — — — Harmful

China New Economic Interventions vs. EU27:

© Alpine Macro 2024
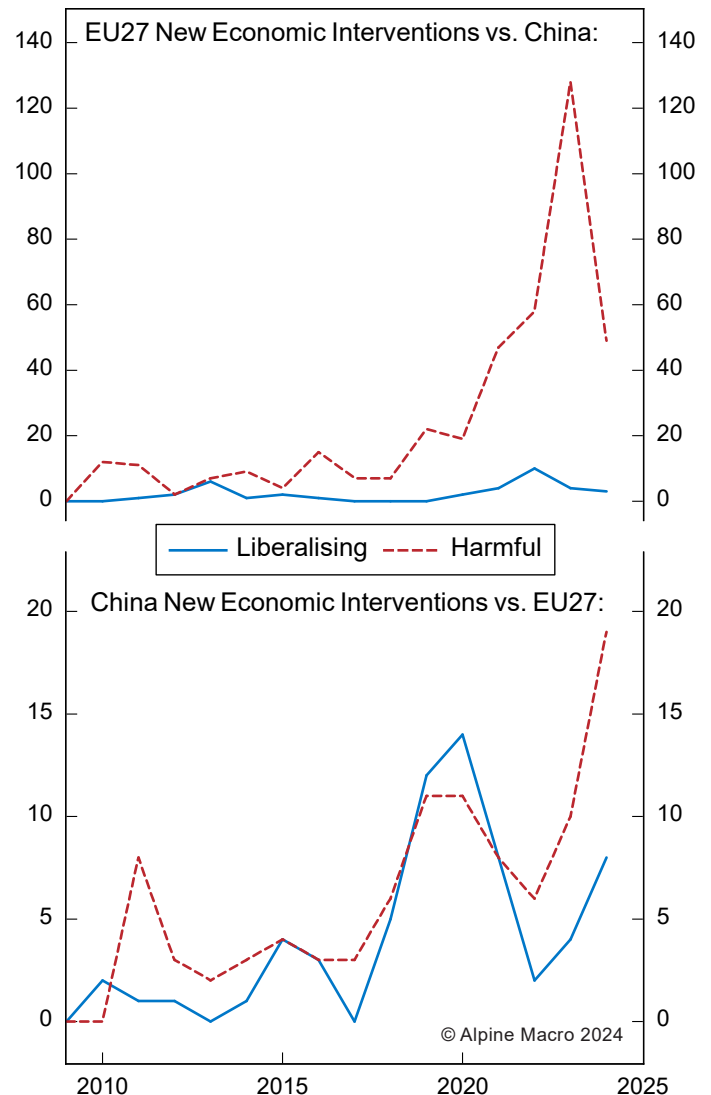
Note: Policy actions are based on implementation date, and are adjusted for reporting lags; source: Global Trade Alert

7-year budget is years away, though negotiations for the 2028-34 budget will be intense[1].

On monetary policymaking, the new E.P. majority will also have little impact. While some right-wing

---

1　More important will be the application of the more lenient fiscal rule which was already adopted this year (and parts of it are still being crafted), including the Excessive Debt Procedure, though that is not contingent on the E.P. elections.

parties would prefer to rein in the ECB's independence, they will lack the votes.

Climate Policies: Green energy mandates will get further delayed and watered down due to domestic political opposition. This is already happening, not only in the E.U., but also in the U.S.

The E.U. estimates that it needs to spend EUR 1.5tn annually on green energy and transport to reach net-zero emissions, and the money is simply not there. Net-zero carbon mandates are unpopular and also in conflict with other E.U. policy preferences, such as re-industrialization and the military build-up. Accordingly, the Greens are expected to be the biggest losers, with their E.P. seats possibly being cut by a third.

Market Implications

The immediate market reaction to the E.P. election will be subdued, even in the unexpected case of a right-wing "wave" election. Ultimately, the E.P. is one of three major E.U. institutions, along with the European Commission and the European Council, and any policy risks will likely be moderated. We do not expect the election to have any risk-on or risk-off effects on the Euro or on European government bonds. However, expected policy changes could have notable sectoral impacts.

Cheap energy is critical to European growth. As green energy mandates and policies will be delayed and watered down, European alternative energy assets will continue to underperform (Chart 5). The E.U. seeks to reindustrialize, and to build out its arms and tech industries, it will need cheaper

Chart 5 **European Renewable Energy Underperforms**

European Stock Performance:
— Renewable Energy*
---- STOXX 600 Oil & Gas
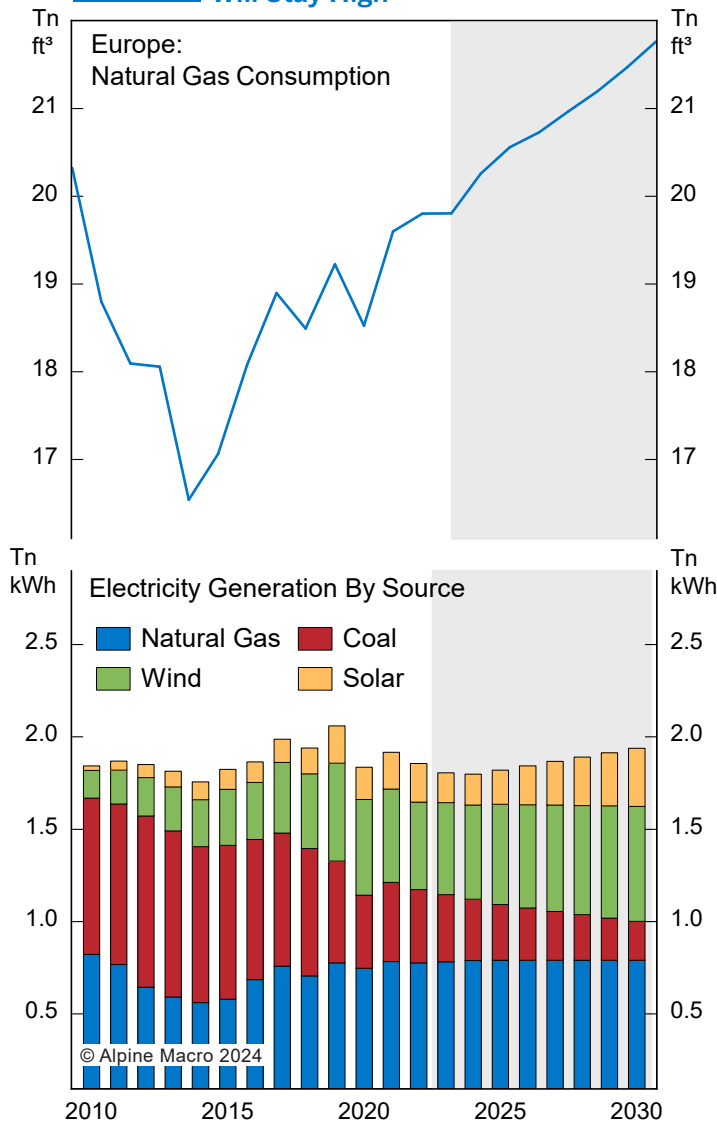— STOXX 600

© Alpine Macro 2024
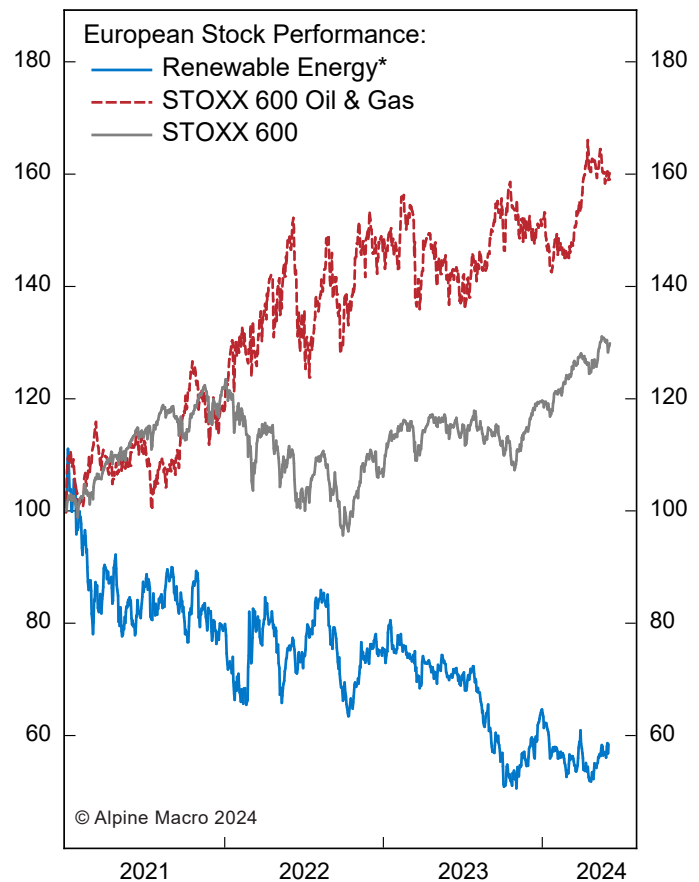
*Source: Bloomberg Finance L.P.
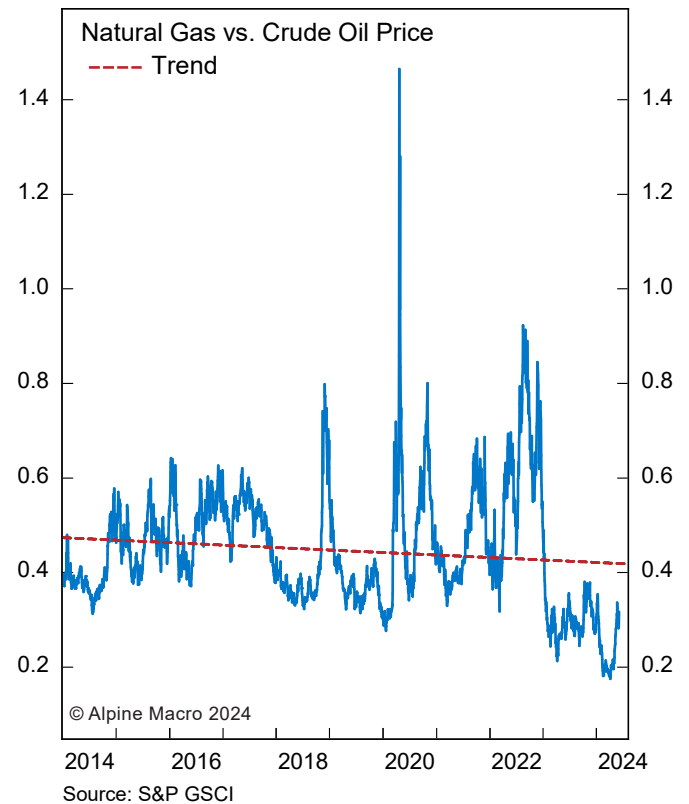Note: Series are rebased to Jan 2021=100

energy. An obvious candidate is natural gas, and demand for it will stay high (Chart 6). Natural gas is now also cheap relative to oil prices and has upside given likely greater demand in Europe and elsewhere (Chart 7).

Another beneficiary could be the utilities sector, long underperforming but which will increasingly be benefiting from subsidies and higher energy demand. Other sectors likely to gain from industrial policies include industrials and semiconductors. Though the latter two have outperformed and semiconductors

Chart 6 **European Natural Gas Consumption Will Stay High**

Europe: Natural Gas Consumption

Electricity Generation By Source
- Natural Gas
- Coal
- Wind
- Solar

© Alpine Macro 2024

Note: Shaded region denotes forecasts; source: EIA

Chart 7 **Natural Gas Is Still Cheap**

Natural Gas vs. Crude Oil Price
--- Trend

© Alpine Macro 2024

Source: S&P GSCI

The U.S. Elections: A Legal Shift?

Last week, Donald Trump was convicted of all 34 felony charges he faced in a New York state trial over hush money payments deemed campaign finance violations. The presumptive Republican nominee faces criminal sentencing on July 11, days before the Republican National Convention.

It is unclear how Trump will be sentenced. He may not face prison time, given his lack of prior criminal record. Trump will appeal the conviction, and the judge could allow him to remain free until his appeals are decided, extending beyond November.

Trump's conviction and potential prison time do not disqualify him from running for the presidency. Despite legal challenges (Trump faces three

are richly priced, they will continue to benefit from political tailwinds (Chart 8).

The European Aerospace & Defense sector has already outperformed, and assets are expensive (Chart 9). However, it benefits from the insatiable demand for ammunition and supplies in Ukraine, and if Europe moves to further increase defense spending, it will have room to run.

Chart 8   Industrial Policies Will Benefit Specific Sectors

Note: Series are rebased to Jan 2022=100; source: MSCI Mid & Large cap

Chart 9   Rearmament And Ukraine War Boost Aerospace & Defense

*Source: MSCI Mid & Large cap
Note: All series are rebased to Jan 2021=100; source: Bloomberg Finance L.P.
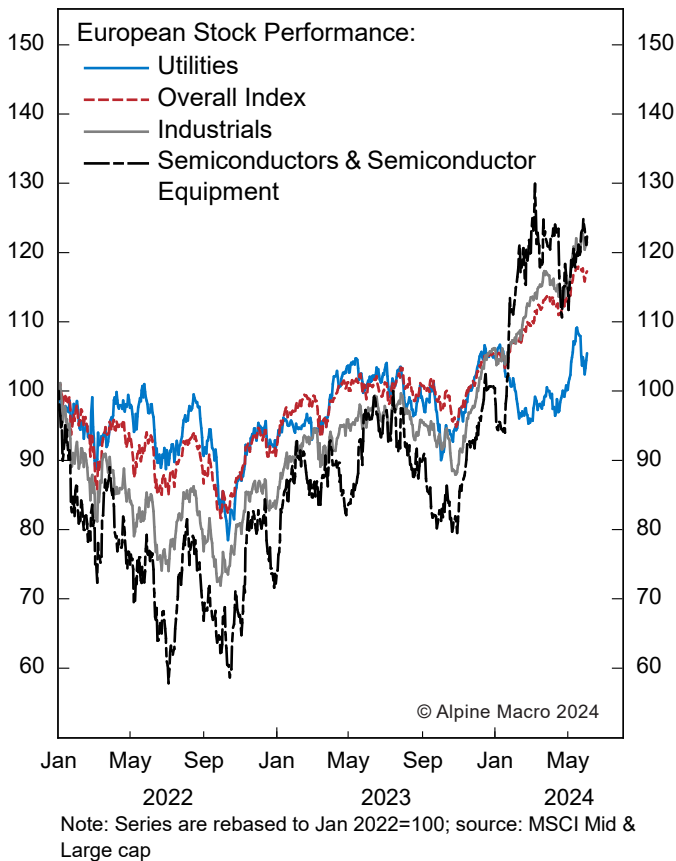
more trials, though these may be decided after November), Trump remains a viable candidate, with most of the Republican Party, including the Senate leadership, supporting him. Republicans argue that the New York trial is a politicized attempt to derail Trump's candidacy. There are recent examples of convicted politicians winning elections, such as Lula in Brazil in 2022.

What will be the impact on the November election outlook? We do not know how a convicted candidate will be perceived by voters, a truly new situation. ==Democrats are banking that independent and moderate voters will turn against Trump now, favoring Biden.== It is possible, and some polls suggest

Trump could lose 5-10 points, though these are at least somewhat flawed. Conversely, ==voters could see Trump's convictions as a politicized sham and his support could increase, especially as Biden is quite unpopular himself.==

Polling over the next 1-2 months will be the telling factor. If Biden gains a lead, especially in swing states, the political effect of Trump's conviction will be clear. He trails Trump in all expected swing states: by more than 4 points in Arizona, Georgia, North Carolina, and Nevada, while he is within a margin of error of Trump in Michigan, Pennsylvania, and Wisconsin. In national polling, Trump is still marginally ahead.

For now, there are no serious market implications. Investors will wait to see how the presidential race develops. Key events will include the first Biden-Trump debate on June 27, the Republican National Convention (July 15-18), Trump selecting a running mate, and the Democratic nomination of Biden and Harris ahead of the August Democratic National Convention (due to a ballot registration deadline in Ohio).

As **Chart 10** shows, ==markets start to price in elections roughly after July==. Even with all the political polarization, we expect this to be the case this year.

A potential risk to markets is if massive election-related social instability leads to risk-off events. However, there is little historical evidence of that. For example, in 1968, the worst American electoral year in terms of social instability, markets were up. Could this year be different? Given the unprecedented political situation, with either losing party likely to question the election results, and fears from both sides of creeping authoritarianism, there is a qualitative argument that markets could sell off on political instability. A risk to monitor.

Dan Alamariu
Chief Geopolitical Strategist

Chart 10 **Markets Price-In Elections After July-August**
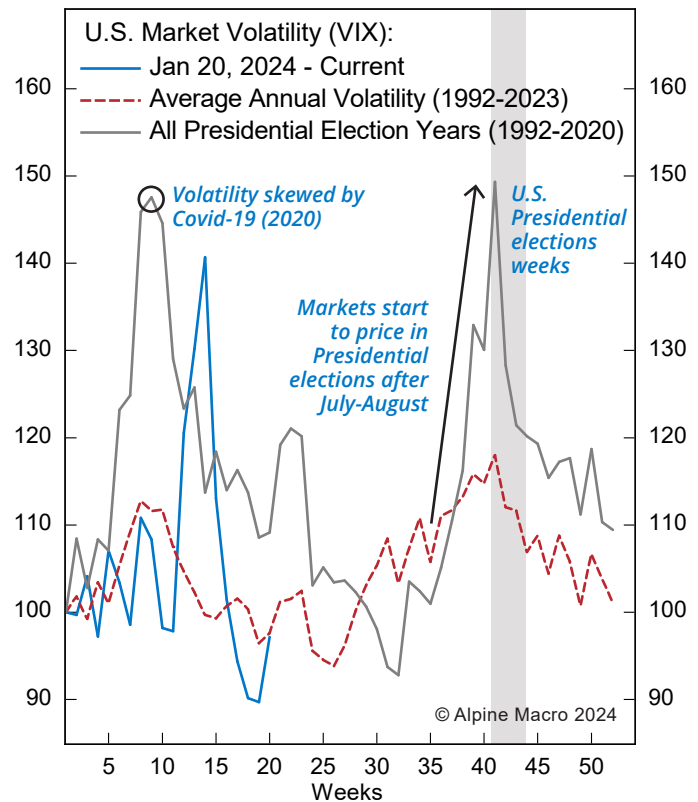
Note: Presidential election years are calculated from Jan 20 of the election year to Jan 20 of the next year, using Jan 20 Presidential inauguration date as year-markers, with values indexed to 100 on Jan 20

ALPINE MACRO
A Unique Mind On The Markets