



CIO Special

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Biden agenda stands at a crossroads

01 Introduction

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Key take aways

- Following his 2020 election victory, President Biden faces policy uncertainty after initially delivering COVID-19 rescue and infrastructure packages for the U.S. economy.
- Falling poll numbers and high inflation are proving to be a difficult combination for his administration to navigate with political in-fighting within the Democratic Party making any further progress difficult to achieve.
- History shows that midterm elections typically swing in favor of the opposition party, but America remains a deeply divided nation – potential surprises could occur.
- Market performance during times of a Democratic Executive and a Republican Congress has typically been positive. However, macro tail risks remain on the table.

01 Introduction

For many, November 3, 2020, and the weeks that followed will be seen as the one of the most pivotal moments in American political history. The Presidential election between Republican incumbent Donald Trump, whose anti-establishment rhetoric and combative style had repositioned the United States' place on the world stage since 2016, and Democratic former Vice President Joe Biden, campaigning to return stability to the American people, was as controversial as it was highly contested.

Biden's victory to become the 46th President of the United States was delivered with the highest number of votes ever received by a candidate in U.S. history, with his opponent President Donald Trump receiving the second highest. The impact of the COVID-19 pandemic, which was the central campaign issue of the election, saw many voters stay at home and cast their votes by mail. This saw early electoral college victories for Trump ebb away over the course of election night with the laborious process of collecting and counting these mail-in votes going on through the night. Once all votes had been counted, Joe Biden had won by just under 43,000 votes across three states – Arizona, Georgia, and Wisconsin.

Following Election Day, the events leading up to President Biden's inauguration were as controversial as they were unprecedented. False accusations of voter fraud as well as violent protests by Trump supporters in Washington D.C. are still being dealt with, but as the United States entered 2021, they did so with a new Democratic administration in the White House.

The composition of the United States Congress however remains finely balanced, within both the Senate and House of Representatives. As with so many presidencies, it is this dynamic that sets the tone for an administration's political agenda. After some early success, President Biden faces uncertainty on several fronts with both domestic (COVID-19, high inflation, political in-fighting) and foreign (Afghanistan, Russia-Ukraine conflict, U.S.-China relations) issues requiring attention in order to boost his lackluster poll numbers. Almost all these issues will require the President to deliver on his reputation as the experienced political deal-maker and reset the direction of travel



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before the next election battle arrives over the horizon, the November mid-terms.

Within this CIO Special we will look back at President Biden's first year in the White House and his administration's successes and disappointments, as well as looking ahead to what will be a defining period for his presidency. Biden's early ambitions to be the great reformer alongside previous presidents such as Franklin D. Roosevelt (FDR) or even arguably Richard Nixon, have been tempered by a combination of factors which we will discuss in detail. How President Biden navigates the remainder of 2022 will set the stage for the rest of his Presidency.

02 From early success to slowing momentum...

Entering the White House, Biden's immediate focus was to turn the tide on the COVID-19 pandemic which saw both rising cases and deaths still being recorded across the country. Within the first three months of his presidency, Biden had signed the America Rescue Plan; an economic stimulus package totaling USD1.9tn. Designed to provide economic relief to Americans during the pandemic, the main highlights of the package were the immediate payment of USD1,400 directly to individuals as well as an expansion of tax credits and unemployment benefits across the country. Further initiatives included increased funding for medical centers tackling COVID-19, schools, and small businesses.

Whilst the first major piece of legislation passed by the Biden administration undoubtedly assisted all Americans during a time of extreme hardship, the bill's focus was mainly towards lower-income families as part of the growing Progressive influence within the Democratic Party. The make-up of Democrats elected to the U.S. Congress following the 2020 election included a new number of progressive members who were vocal not only in their dissatisfaction with the previous Trump administration and its handling of the pandemic (Trump for example did not propose any federal mandates in 2020, instead placing responsibility in the hands of individual states) but also in their unified resolve that President Biden should push for a more progressive agenda in areas such as the minimum wage, increasing taxes on high-income earners and corporations as well as tackling climate change.

Following on from the initial success of delivering a wide-ranging COVID relief bill, Biden's administration turned its attention to finally delivering an infrastructure package long discussed by both Democrat and Republican leadership. The Bipartisan Infrastructure Fund (BIF) originally started life as a multi trillion-dollar package spread across transportation, energy renewal, education and housing as well as further strengthening workers' rights. Funding of this bill would come from several sources, including potentially reversing the Trump administration's 2017 tax cuts and increase corporation tax from 21% to 28%, which would still be below the pre-2017 tax rate of 35%, however.

Negotiations between Democrat and Republican members of Congress continued throughout much of the year whilst at the same time, an internal standoff developed over key elements of Biden's separate 'Build Back Better' bill (focusing more on

social issues and climate change) between moderate Democrats and the more progressive wing of the party. Tensions within the party have been ever present throughout Biden's presidency, and even as centrist Democrats agreed to support the separate legislation and finally deliver on a bipartisan USD1.2 trillion infrastructure package, mistrust has remained in the air.

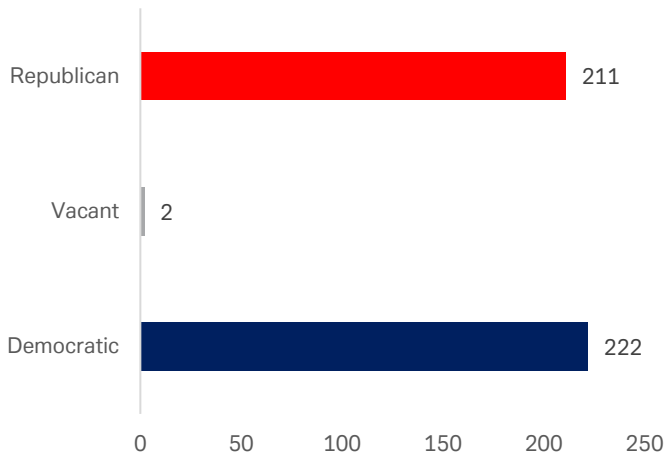
Elements of both the American Rescue Plan and Bipartisan Infrastructure Bill also highlight a new dynamic within the Democratic Party. Prominent progressive voices such as Senators Bernie Sanders and Elizabeth Warren, both of whom have had their own Presidential ambitions in the past, have now been joined by younger, motivated progressives within the party determined to have a greater say in deciding the political agenda. Sensitive to these concerns, Biden moved quickly at the start of his presidency by issuing more Executive Orders than any other president since FDR in the 1930s to appease these voices. Executive Orders ranged from re-joining the Paris Climate Accord and revoking construction permits for oil pipelines to declaring a federal mandate requiring face masks to be worn in government buildings and reversing immigration controls. More recently, President Biden has announced his nomination for Supreme Court Justice – Judge Ketanji Brown Jackson. If confirmed, Judge Jackson will be the first African American woman to be appointed to the highest court in the land. This choice comes at a particularly sensitive time for one of the landmark cases in American judicial history – *Roe v. Wade*. The decision by the Supreme Court in 1973 to constitutionally guarantee a woman's right to an abortion is now being challenged again in a pending case in Mississippi which could have widespread consequences across the country.

Such appeasement must be balanced with the concerns of more moderate members of the Democratic Party. Joe Manchin and Kyrsten Sinema, both Senators within the key swing states of West Virginia and Arizona, have been vocal critics in many of the negotiations throughout this year and have become symbolic of the congressional headache that Biden must address to achieve substantive progress in his presidency. This is all due to the composition of the U.S. Congress, which remains finely balanced. Following the 2020 election, the U.S. Senate consisted of 48 Democrats, alongside 2 Independent Senators on one side of the aisle with 50 Republican Senators residing on the opposite side. In the lower chamber, the House of Representatives, the numbers currently favor the Democrats by 10 but overall, the picture is clear to President Biden, every vote counts.

The economic impact of both pieces of legislation have been the clear successes for the Biden administration so far. However, the size of the packages could well be argued to have contributed to the higher inflation levels that the U.S. economy is currently dealing with as the demand side of the economy received a significant boost. Consumer prices have increased by 7.5% since the start of 2021 with the Biden administration's expectations that such a sharp rise would begin to subside looking more suspect with his recent poll numbers reflecting public scepticism. Combined with the ongoing issues of rising input costs and supply chain constraints, the prospect of a further USD1.75 trillion in government spending through the 'Build Back Better' social package has been derailed by the previously mentioned Manchin and Sinema, citing the growing risk of inflation and its effect on the U.S. economy.

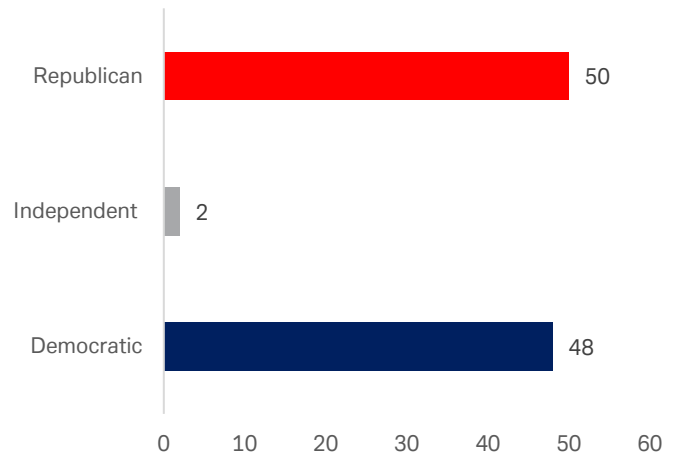


Chart 1: House of Rep. breakdown



Source: www.house.gov, Deutsche Bank AG. Data as of March 2022.

Chart 2: U.S. Senate breakdown



Source: www.senate.gov, Deutsche Bank AG. Data as of March 2022.

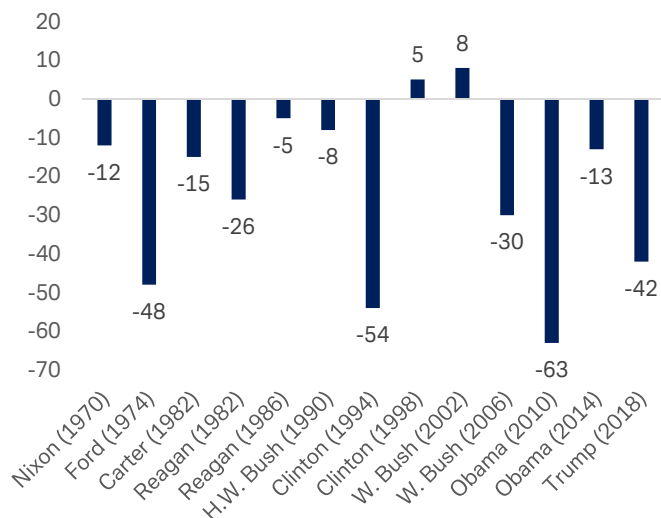
03 Midterm matters...

It was once said that “elections are not a beauty contest; it is all about tolerance” and on November 8, President Biden and the Democratic Party will discover how much tolerance the American people have for their abilities to guide the country through the next two years as the pandemic and economic pressures continue to cast a shadow over the country. Historically speaking, the midterms are a challenging time for every President, with a common belief that they are simply a ‘referendum on the executive’. Regardless of economic landscape or political temperature within the country, only twice has the President’s party gained seats in both the Senate and

the House: Franklin D. Roosevelt’s first midterm election and George W. Bush’s first midterm election – the latter of which being driven heavily by the events of September 11, 2001, and a more unified feeling across the country.

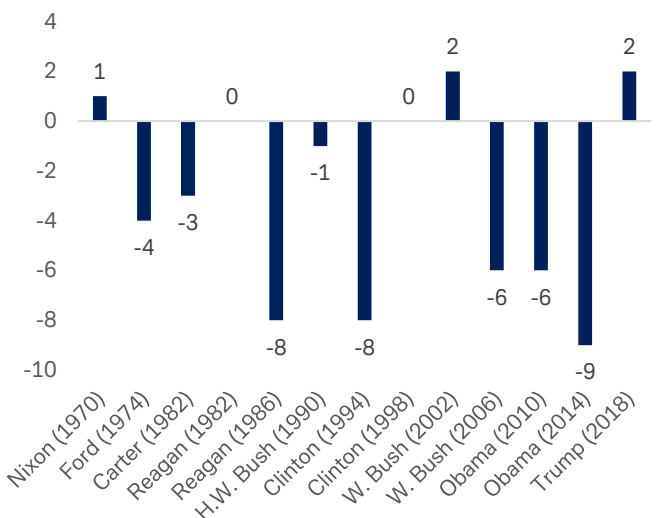
Such swings in both the House and Senate will clearly influence the Administration’s ability to deliver policy successes over the remainder of the President’s term. Such examples include President Obama’s infamous “shellacking” in 2010, where a record 69 seats were lost in total – essentially bringing his legislative agenda to a standstill against a newly crowned Republican House. Similar patterns had also occurred in 2018 for President Donald Trump, with the Democrats regaining control of the lower chamber.

Chart 3: Change in House seats by President's party



Source: FiveThirtyEight, Deutsche Bank AG. Data as of March 2022.

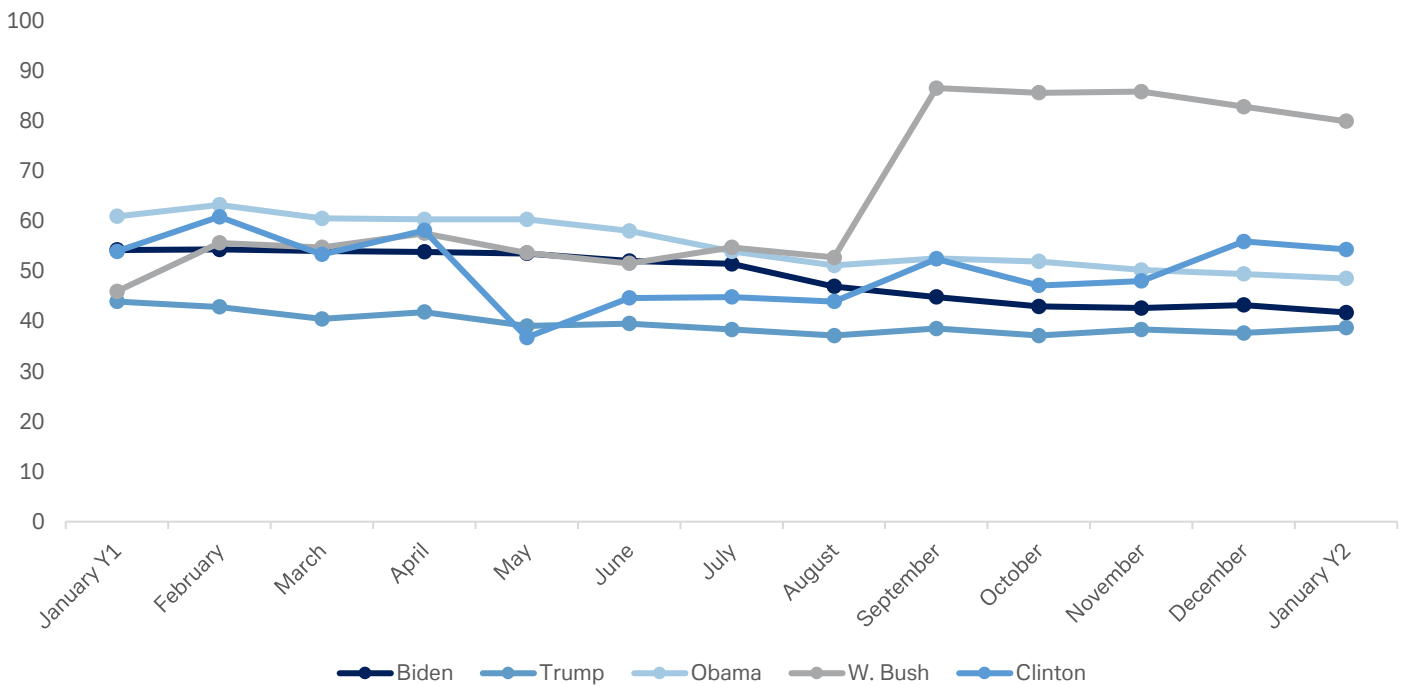
Charts 4: Change in Senate seats by President's party



Source: FiveThirtyEight, Deutsche Bank AG. Data as of March 2022.



Chart 5: Approval ratings during a President's first year in office



Source: FiveThirtyEight, Deutsche Bank AG. Data as of March 2022.

The results of the midterms typically occur as the President faces falling poll numbers in the build-up to the election. The difficult situation facing President Biden is that his poll numbers are amongst the weakest in modern times; only President Trump had a lower approval rating at this point of his Presidency.

Away from the legislative action undertaken by the Biden administration, firstly to take control of the pandemic and secondly to deliver an infrastructure package, there has been growing public frustration with the White House and the Democratic Party overall. The mishandled withdrawal of U.S. troops from Afghanistan in the summer of 2021, which subsequently led to the almost overnight recapture of Kabul by Taliban forces, placed the President under scrutiny for his handling of foreign affairs. Back in the United States, the Omicron variant emerged to become the dominant strain of COVID-19, with cases and deaths rising substantially. Such negative headlines have influenced poll numbers, reflecting an America where many have become impatient at the handling of the pandemic as well as being hit by rising prices.

Political infighting within the Democratic Party has meant that Biden's flagship social policy; Build Back Better, has slowed to a complete stop. The lack of unity within the party has given Biden's opponents ample firepower to present his presidency as one where little progress will ever be made. Regardless of the fact that almost all the Republican Party have refused to back any of the President's legislative agenda.

All these factors create a difficult landscape for Biden and the Democrats to navigate over the next 9 months. As things stand, the Republican Party needs to win an additional 5 seats in the

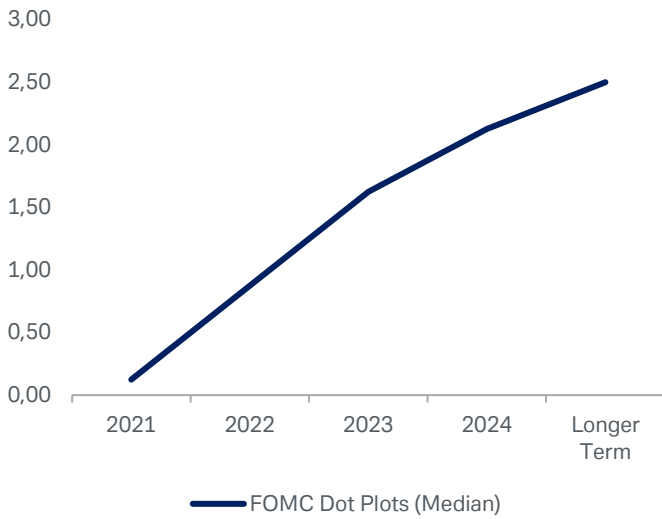
House whilst just 1 further Senate seat will be enough to secure a full majority in the U.S. Congress. This fine balance is further complicated by a record number of Democratic retirements (those not looking for re-election) amounting to 30 members of Congress – the highest since 1996.

As with many elections in modern times, there will be several key states to keep an eye on during the election. Ohio, North Carolina, Pennsylvania, and Georgia will remain vital for any victory in U.S. politics. In the U.S. Senate, there are 34 seats up for re-election; 20 Republican seats and 14 Democratic. Of these races the most competitive will be Nevada, Georgia, New Hampshire, and Arizona. All 5 will be the key races in which Senate Democrats must defend their seats. For the Republican Party, several long-serving Senators are retiring from public service in what will be closely fought states. Such retirees include Senators Richard Burr (North Carolina), Pat Toomey (Pennsylvania), Rob Portman (Ohio) and Roy Blunt (Missouri).

Using history as a guide, Republicans have a strong possibility of taking complete control of the U.S. Congress. Of course, it is important to state that the United States remains a deeply divided country; with record electoral turnouts becoming the norm as seen in the 2020 Presidential election and 2018 midterms, there could well be another tightly contested race. In the instance that history continues its trend and the party in power come out of the midterms weaker than when it entered, policy implications will be significant. Republican control will mean that any chance of progressive policy from the White House, in particular Build Back Better, will be dead in the water. Without any means to push through its original agenda, Congressional focus will move towards such issues as the debt ceiling and other fiscal debates.



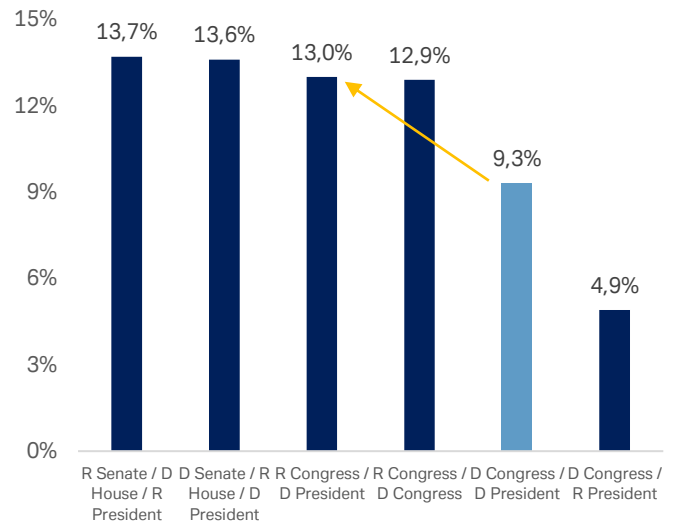
Chart 6: FOMC dot plots



Source: Bloomberg Finance L.P., Deutsche Bank AG. Data as of March 2022.

If the Democrats do hold onto their seats, then there would be a second chance to give Biden’s agenda a new lease of life. However, the realities of the balanced Congress as well as the continued friction within the Democratic Party means that any new version of Build Back Better would need to be watered down further to be successfully passed. For such a scenario to play out, two main issues must begin to resolve themselves and give Biden a stronger footing in the polls. Firstly, the current trend of falling Omicron cases (and deaths) must continue to the point where restrictions are significantly lifted, and a sense of normalcy can return to the American people after 2 years of COVID-19. Secondly, inflation must be reined in. Rising costs across the country cannot completely be put at the door of the White House and its economic team – many drivers are indeed due to global fallout from the pandemic, but questions around the continued use of Trump-era tariffs on Chinese products for example, have been raised. With the Fed funds rate expected to rise in March, the Biden administration will be hoping that Jerome Powell and the other members of the FOMC will act

Chart 7: Partisan Control, annual S&P 500 performance



Footnote: S&P 500 Annual Returns 1933-2020, excluding 2001-2002 due to Sen. Jeffords changing party mid-2001. Source: Strategas Securities LLC., Deutsche Bank AG. Data as of February 2022.

swiftly to tame the highest inflation figures in 40 years, ideally before the midterms arrive.

The market impact of the midterms has generally been positive, underpinning the inherent strength of the U.S. economy. Looking into the various scenarios however, whilst the upcoming elections could see pains for the Democrats, markets would appear to take the combination of a Republican legislature and Democratic executive in its stride – delivering an annualized return of 13%.

The market reaction to the midterms will also be influenced by events closer to the time. As we have witnessed recently with geopolitical situation between Ukraine and Russia, markets will take their cues from more than just a new look Congress. The unpredictability of macro events could mean that the focus of investors could well be drawn elsewhere besides Capitol Hill. But regardless of the market reaction, the political consequences for Biden after November could well decide how his presidency will be remembered.



Glossary

Congress is the bicameral federal legislature of the United States.

Democrats is short for the Democratic Party in the U.S., one of the two major parties.

The **Federal Reserve (Fed)** is the central bank of the United States. Its **Federal Open Market Committee (FOMC)** meets to determine interest rate policy.

The **House of Representatives** is one house in the bicameral U.S. Congress with some exclusive powers e.g. to initiate revenue bills.

Republicans is short for the Republican Party, one of the two major parties in the U.S.

The **Senate** is the smaller house in the bicameral U.S. Congress, with a more deliberative function.

USD is the currency code for the U.S. Dollar.



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