



Global Macro Research

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#Emerging markets / #Geopolitics / #Growth

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What does Trump's win mean for emerging markets?

The return of Donald Trump to the White House opens the door to a wide range of shocks for emerging markets, both positive and negative.

Key Takeaways

- Trump and the Republican party have swept the US' political landscape, opening up a wide range of large policy changes that could shock the emerging market (EM) economic and geopolitical outlook.
- We do not know the exact policy mix that Trump will follow the second time round. But one common feature across plausible policy constellations is more inflationary pressure and a higher-than-otherwise federal funds rate, reducing the magnitude of EM central bank rate cuts.
- A 'market friendly' Trump presidency may be noisy, but ultimately would be good for many EMs: the Fed may cut by less, but a stronger global economy and 'risk on' market sentiment would mitigate the impact of USD pressure.
- By contrast, a far-reaching trade war would be much harder to navigate, creating a wide range of winners and losers across EMs. This is a particular risk for China, but could ultimately benefit countries that are able to capture the reshoring of manufacturing.
- A tougher US stance on migration and deportations would be felt most in Latin America, complicating the 2026 USMCA review. But, ultimately, the more the US decouples from China, the more it will need Mexico.
- A wider range of foreign policy aims and outcomes is also possible under a second Trump presidency. Resolutions to the Ukraine-Russia and Middle East conflicts remain unlikely in the near term, but a more isolationist and transactional approach could recast relations with both friends and foes.

Trump 2.0

Donald Trump has staged a remarkable political comeback to retake the US presidency, with the Republicans taking hold of both the House and Senate, giving them significant control of the US policy agenda.

Markets' initial reaction was to sell EM currencies, with the US dollar strengthening sharply. The bond market reaction was most evident through the bear steepening of the US treasury curve as longer-dated bond yields rose and a higher federal funds rate path was priced in, which put pressure on some EM rates.

In the days since, two-year US yields have risen slightly more than the 10-year as near-term price expectations have picked up. Meanwhile, FX moves have been mixed. Initial gains for the dollar were reversed within a day, but have since resumed to bring the DXY index 2% higher compared to 5 November, resuming some pressure on EM currencies.

The market reaction highlights the uncertainty around US policy for emerging markets, even if the initial consensus is broadly pricing higher US nominal growth and potentially less scope for the Federal Reserve to cut policy rates.

Significant 'known unknowns' around Trump's domestic and foreign policy agenda will take time to become clear. And even as the broad contours take shape, ongoing noise is likely to make judging the implications for emerging markets far from easy.

Given this uncertainty around Trump 2.0, we consider the impact on EMs through the lens of four broad channels: 1) how US monetary and fiscal policy will impact EMs; 2) shifts in global trade; 3) implications of Trump's immigration policy; and 4) how US foreign policy will impact global conflicts.

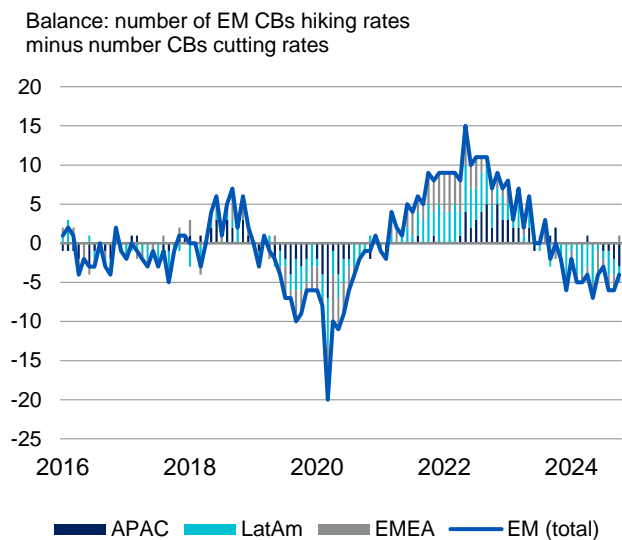


1. Trump's reflationary agenda may slow the pace of EM central bank rate cuts

Key parts of Trump's agenda – namely tax cuts, higher tariffs and reduced immigration – will be inflationary for the US, tempering the Federal Reserve's scope for rate cuts. Only a desire to drill for more oil will provide a partial relief.

Our base case for the Fed's rate path is one more 25bps cut in December, followed by quarterly reductions of the same magnitude over 2025. But the risks are clearly weighted to a slower and more gradual cutting cycle. This could restrict EM central banks' ability to push ahead with their easing cycles, which only began conclusively across all regions in September (see Figure 1).

Figure 1: Trump's reflationary agenda for the US and uncertainty for EMs will restrict central bank cuts



Source: Haver, abrdrn, November 2024

More Fed-sensitive central banks, such as Mexico's and Indonesia's, will therefore limit their rate cuts over the short term to maintain favourable differentials against the US.

That said, there are important differences depending on which 'type' of Trump we get (see Figure 6).

A more market-friendly 'Trump delivers for markets' mix of policies could be less constraining for EM policymakers. US tax cuts and deregulations could provide an ongoing tailwind to corporate earnings and bolster global 'risk on' sentiment.

If the worst of Trump's proposed tariff increases are avoided, this may offer relief for currencies versus USD, while stronger US nominal growth would boost global trade.

However, with the Republicans taking both the Senate and the House, there is also the possibility of more sweeping changes across trade, immigration, fiscal and regulatory policy. This 'Trump unleashed' scenario could amplify the inflationary impulse as a larger fiscal deficit comes alongside weaker potential growth from the mass deportation of illegal migrants, a starker decoupling from

China and stronger attempts to 'onshore' manufacturing back to the US.

In such a scenario, high levels of trade uncertainty would likely push up on risk premia and hurdle rates, keeping EM market sentiment cautious and constraining firms' investment.

2. US-China decoupling will benefit some EMs

Trump has threatened a 60% tariff on all Chinese trade, alongside a universal 10% tariff on all other imports, partly as a means of financing his planned tax cuts.

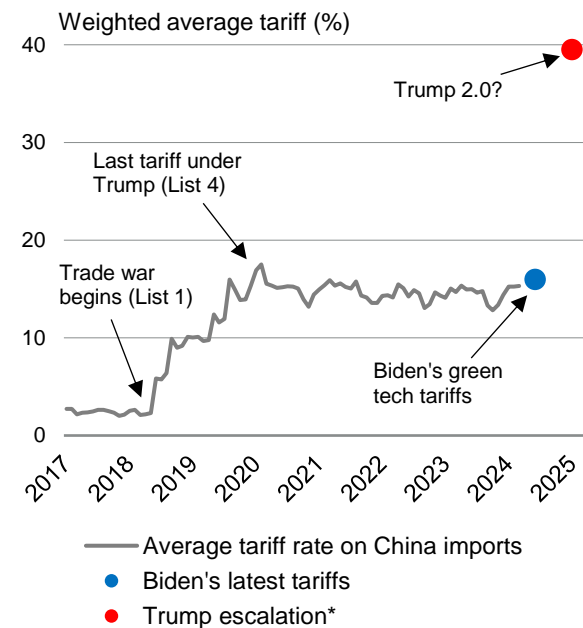
The first Trump term saw tariffs either being threatened or applied as a means of gaining concessions from trading partners. This time around, we think that a meaningful and lasting increase in US tariffs on China is likely, but that the threat of a universal baseline tariff is being used primarily as a negotiating mechanism.

The failure of the Phase One trade deal – which only saw Chinese purchases of US goods rise by \$20bn, rather than the \$200bn agreed – makes us think a deal this time around is less likely, albeit still possible.

Instead, higher tariffs on previously targeted goods appear motivated by a desire to reduce the bilateral deficit and reliance on Chinese-made products as part of a broader economic decoupling.

The economic shock on China – and indirectly on its EM trading partners – could be large. Even if tariffs are only increased on goods previously targeted, the average bilateral tariff rate could more than double (see Figure 2).

Figure 2: Higher tariffs will be hard for China to avoid



*Scenario assumes 60% tariffs applied to Lists 1-4

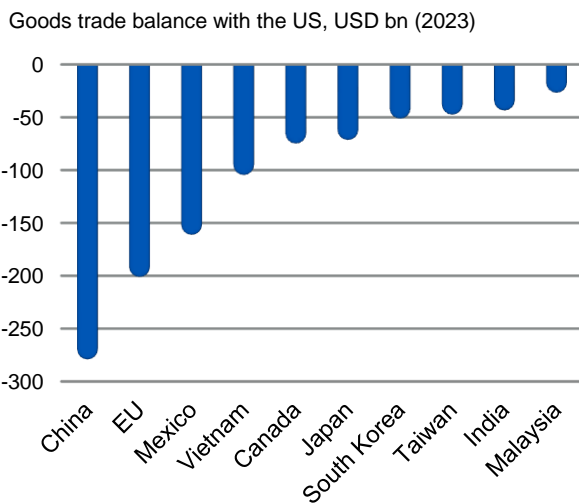
Source: US Census Bureau, USTR, WITS, Haver, abrdrn, November 2024



We expect that stimulus measures from Chinese policymakers will ramp up somewhat following Trump's election victory, helping to cushion the negative effects on China and spillovers for other EMs. Nonetheless, we recently downgraded our China 2025 and 2026 GDP growth forecasts by 0.2% in each year.

While we think a universal baseline tariff may be avoided, the likes of India and Brazil could be singled out for their high tariffs on US imports. Risks will also be high for EMs with large trade surpluses, especially those – such as Vietnam and Malaysia – which could be accused of re-exporting Chinese goods to circumvent tariffs (see Figure 3).

Figure 3: China not the only trade partner at risk



Source: Haver, abrdrn, November 2024

Many EMs could navigate a rise in tariffs – or the indirect effects from Chinese depreciation on their trade-weighted baskets – via FX devaluation. However, US accusations of 'currency manipulation', which could be met with additional tariffs or other trade actions, may limit the scope for manoeuvre. Indeed, there is a risk that Trump pushes for a weaker USD.

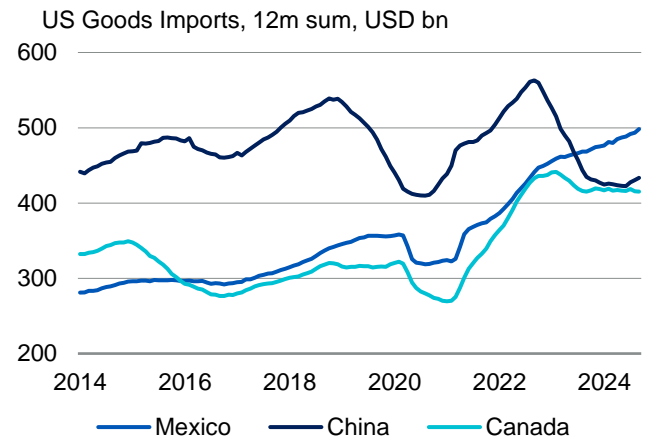
The re-routing of Chinese exports could ultimately prove disinflationary for other EMs as Chinese goods seek new markets. There is a risk that economies competing at similar levels to China's manufacturing value add – such as Thailand or the emerging Europe economies tied to German supply-chains – face prolonged pressure.

Bilateral trade agreements, like those with Japan and South Korea during Trump's first presidency, are at least still possible for other EMs, even if it is a long shot for China.

And many emerging markets are still likely to benefit from US-China tensions as a driver of reshoring. The US will need other countries more as its actions against China scale up.

Mexico stands out in this regard, having become the US' largest source of imports in 2023 (see Figure 4).

Figure 4: North American trade ties have deepened since the first trade war with China



Source: Haver, abrdrn, November 2024

Significantly, this implies that, while the Trump administration may threaten a *renegotiation* rather than a *review* of the United States-Mexico-Canada Agreement (USMCA), it is not clear that ripping it up – or changing it in a way that reverses the tailwinds to Mexican manufacturing – is plausible. Instead, such threats may be aimed at extracting other concessions, for example on migration and border security.

3. Poor, huddled masses? No, thanks

It is uncertain how much Trump will follow through with his proposals regarding immigration, owing to economic and logistical hurdles. That said, Trump's base will almost certainly expect action.

We think Trump will try to ramp-up deportations, even if this likely falls well short of threats to remove millions of people. He will also beef-up border security to stem the inflow of migrants. We expect H.R.2 (the 'Secure the Border Act') to be passed, which would crack down on use of illegal migrant workers, restrict the asylum process and allocate funding to extending the border wall with Mexico. In addition, legal migration may also be slowed.

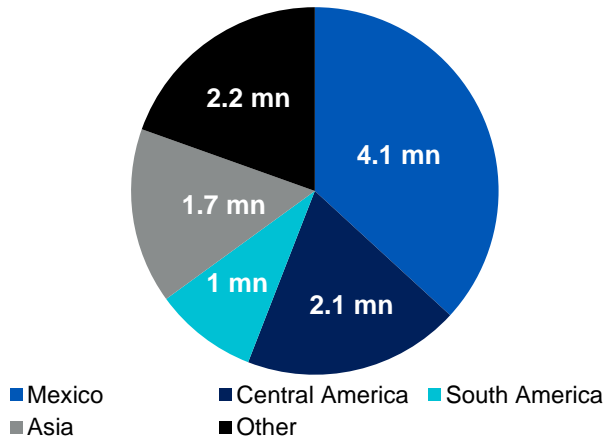
The cost of this policy will go beyond mass deportations and border security. The Pew Research Centre estimates that 75% of unauthorised migrants work. As such, deportations and restrictions will tighten the labour market in the US, particularly in cost-sensitive sectors such as construction.

All of this means that tensions with new Mexican President Claudia Sheinbaum are likely to rise, adding to a challenging policy backdrop in Mexico.

Relative to the size of their own populations and economies, Mexico and Colombia are most reliant on their migrant workers residing in the US (see Figure 5). Indeed, their 2023 remittance receipts totalled 3.7% and 2.8% of GDP respectively.



Figure 5: An estimated 11 million unauthorised migrants resided in the US in 2022



Source: Pew Research Centre estimates for population of unauthorised immigrants in the US, abrdrn, November 2024

For the wealthier LatAm economies, having to manage an increase in migrants and deportees from the US will add to social tensions, put more strain on public finances and add a disinflationary impulse from increased labour supply.

Authors

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4. US foreign policy will shape conflict risk

The US approach to geopolitics, particularly to conflicts (either live or potential) will be a major factor driving market perceptions of tail risk.

How the next president approaches conflicts in Ukraine and the Middle East will be crucial.

Trump has promised to end the Ukraine-Russia war as soon as he becomes president and has shown scepticism towards aid for Ukraine. A ceasefire would be positive for markets, but we think he is overestimating his ability to secure peace quickly (or indeed at all).

During his first term, Trump was a strong supporter of Israel, moving the US embassy to Jerusalem (where it has stayed) and took a hawkish approach to Iran. While relations between Trump and Israeli president Benjamin Netanyahu are not good, we would expect him to strongly back Israeli military operations and increase sanction threats on Iran.

The tensions in the Taiwan Strait and South China Sea are also highly contingent on the approach of the next US administration.

At his rallies Trump has sometimes aired a grievance about the cost of US support for Taiwan. And we see some risk that 'strategic ambiguity' is undermined. That said, US reliance on high-end semiconductors for its military suggests that the status quo will likely be maintained.



Figure 6: US election scenarios and implications for emerging markets

Scenario	US policy overview	EM implications
<p>Trump 2.0</p> <p><i>Trump follows through with most of his tariff threats on China, but trade deals done elsewhere. US fiscal deficit widens on tax cuts and immigration slowed.</i></p>	<p>Tariff hikes focused on China. This results in an effective tariff rate of 35-40% on imports that comes into force around the middle of 2025. Isolated trade spats (including tariffs) with other countries over bilateral trade deficits and in some instances national security. USMCA renegotiated modestly, such that tariffs and non-tariff barriers are largely avoided.</p> <p>Fiscal deficit wider, resulting in higher US nominal growth (supporting global trade). An expansion of US oil drilling provides only a partial inflationary relief for energy importers. A roll-back of Biden's green initiatives tempers the green investment tailwind (Indonesia, Chile) H.R.2 passed, slowing migration and adding to inflationary pressures. Overall, Fed rate cuts are tempered.</p> <p>Ukraine pressured into negotiations, with eventual ceasefire, but the Middle East conflict persists. More military spending in Europe/Asia as the US pressures NATO allies to spend more and policymakers have less assurances of US support.</p>	<p>Trade uncertainty hits EMs, weighing on near-term investment and FDI, but there are some winners from nearshoring and friendshoring, which emerge over a longer time horizon.</p> <p>EM central banks cut policy rates more gradually, with some terminal rates shifting higher in US rate sensitive EMs. Instances of weak domestic economies and progress lowering inflation means some EM central banks can continue to cut. China steps up stimulus to offset much, but not all, of the trade shock, while few attempts are made to reorienting its economy towards consumption.</p> <p>Tensions in the Taiwan Strait steadily rise, albeit with the US de facto maintaining its 'strategic ambiguity' and 'One China' policies.</p>
<p>Trump delivers for markets</p> <p><i>Trump's agenda largely follows the pattern set in the first half of his first presidential term, with efforts focussed on deregulation and tax cuts.</i></p>	<p>Trade actions against China proceed, but average bilateral tariffs are increased (relatively) modestly, generating an effective tariff rate closer to 25%. Possibility of some easing of technology restrictions alongside Chinese purchase commitments as a Phase Two deal defuses some tension. Trump threatens tariffs on Mexico, but noise is short-lived and there is limited drama around the USMCA review, which leads to only minor changes to the agreement.</p> <p>Migration tightened via H.R.2 but only modest deportations limit the shock to US labour supply. Tax cuts, along with other business friendly fiscal measures and deregulation, are delivered, boosting global trade. Fed cuts gradually as the US economy remains resilient, helping risk assets.</p> <p>Ukraine pressured into negotiations and credible settlement agreed upon within 12 months. Ceasefire agreed within 12 months in the Middle East, easing regional tensions.</p>	<p>EMs benefit from a less disruptive trade policy and the 'transactional' nature of Trump, with trade deals secured where needed and the most extreme tariff threats not materialising.</p> <p>This allows EMs ex. China to continue to benefit from a gradual shift in global supply chains, via 'China + 1' strategies and friend/nearshoring, boosting FDI.</p> <p>Global growth benefits from stronger US growth and global risk appetite, which ease US dollar pressures and support EM assets. This allows the pan-EM central banks easing cycle to resume, taking some strain off fiscal deficits.</p> <p>Tensions over Taiwan are little changed; US re-affirms 'strategic ambiguity' and 'One China'.</p>
<p>Trump unleashed</p> <p><i>Trump takes advantage of a unified Republican Congress to enact his entire political platform – across trade, immigration, fiscal and regulatory policy.</i></p>	<p>Trump raises tariffs on all imports from China to 60% in early 2025 and Congress acts to more aggressively restrict the use of US technology by Chinese companies and reciprocal investment. Rules of origin are tightened significantly, making it hard to re-route China trade, while tensions between the two countries rise sharply.</p> <p>USMCA put under significant stress and put under annual review. 10% tariffs implemented across all imports and trade tensions with the EU and other major trading partners rise notably as US pushes for 'onshoring'.</p> <p>Full suite of migration policies attempted resulting in a labour supply shock in the US. Fiscal deficit widens significantly, resulting in higher nominal growth, but giving the Fed limited scope to cut.</p> <p>US military support for allies put in doubt, while allies are pressured to boost military spending. Funding for Ukraine cut abruptly, raising tensions between Europe and Russia. Middle East tensions are aggravated by sanctions on Iran and more explicit US military support for Israel.</p>	<p>EM growth suffers trade shock and EM assets suffer.</p> <p>External funding pressures rise, particularly for frontiers, while most EM central banks have less scope to cut and some are forced to hike. For some EMs, politicians use fiscal stimulus to support growth, worsening debt dynamics and market scrutiny.</p> <p>China stimulus is insufficient to offset the trade shock, and consensus expectations for Chinese growth are marked down to 2.5-3%. China's disinflationary impulse to EMs is larger.</p> <p>Migration shock hits LatAm via lower remittances and disinflationary effects of workers returning. Social tensions rise as government fiscal positions are put under strain.</p> <p>Taiwan tensions become 'front & centre' for markets. Conflict risk adds to regional risk premia and EMs embrace a faster shift towards a 'multi-polar' world.</p>

Source: abrdn, November 2024



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