

CEE SPECIAL REPORT

US election: What would a Trump victory mean for CEE?

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Major Markets: Rainer Singer

26 September 2024

The outcome of the US presidential election

There are two issues we see having potentially the greatest impact on the markets globally: future US trade policy and the development of the country's public budget. For the CEE region, the declarations regarding aid to Ukraine and, more broadly speaking, matters of defense will be important developments as well.

Future US trade policy:

Donald Trump has repeatedly called for tariffs of 10% on all imports and 60% on imports from China. The highest proportion of EU exports to the US is accounted for by machinery and components of all kinds, closely followed by pharmaceutical products and vehicles. Conversely, with the exception of fossil fuels, pharmaceutical products, aircraft industry products and machinery also account for the highest share of US exports to the EU. As far as the CEE region is concerned, the share of its exports to the US is rather low.

Economic impact of global trade wars on CEE:

The German Economic Institute looked at the impact of tariffs on the world economy, including Germany. We use its estimates for Germany as a key input to estimate the impact on CEE. A -1.4% shock to the German economy would translate into lower GDP growth for CEE economies ranging from -1.0% to -0.2% in the first year after the shock (depending on the country).

The outcome of the US presidential election

Budget deficit in US:

It is likely that the tax cuts expiring at the end of 2025 will be at least partially extended and both candidates have additional costly proposals in their program. The steady rise in US debt over the coming years has hardly been an issue in the US election so far.

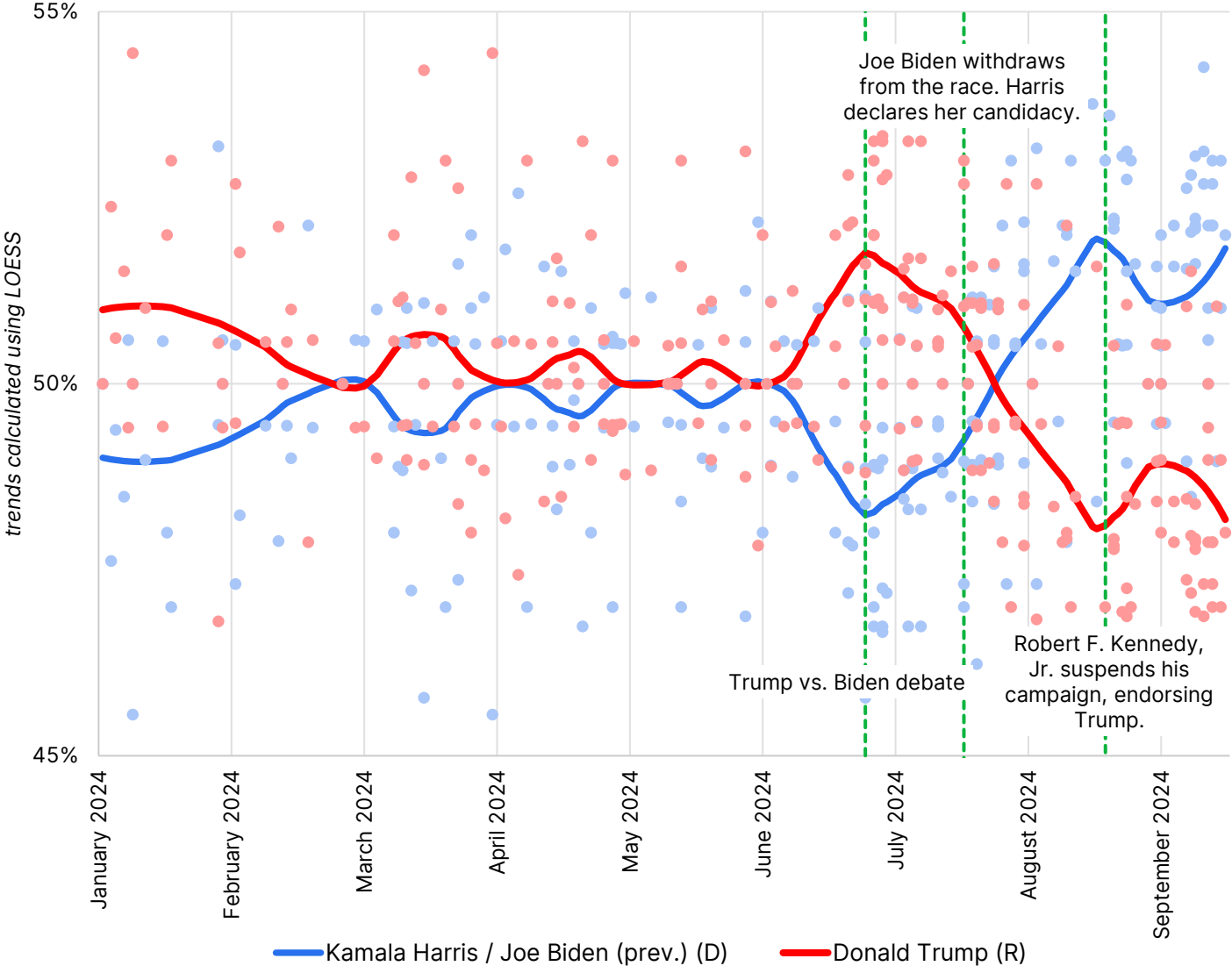
Electric vehicles and climate issues:

In the US, new electric car registrations totaled 1.4mn in 2023, increasing by more than 40% compared to 2022. EV industry officials say they would expect Trump to reduce the efforts to get more electric vehicles on the roads, and to repeal tax incentives. The 100% tariffs on Chinese electric vehicles are already in place. European manufacturers could benefit from rising export opportunities in the US in the face of higher tariffs with China.

Defense:

The biggest threat to NATO alliance would be that member countries that have not yet met NATO's target spending on defense would not enjoy the defense largess and security guarantee of the US. Support for Ukraine is a security issue for the region.

2024 presidential election polling data



Polling data has changed drastically

President Biden's removal from the Democratic ticket and Kamala Harris' takeover of the campaign has flipped polling data. Currently, she leads former President Donald Trump by around two percentage points nationally. However, for the final outcome, it is the voting results in the battleground states that will matter the most. With the race still within the margin of error in many of these states, it is very hard to predict who will get a majority in the Electoral College and become president.

US ELECTION: WHAT SHOULD CEE EXPECT

US trade policy and budget deficits to have biggest impact globally

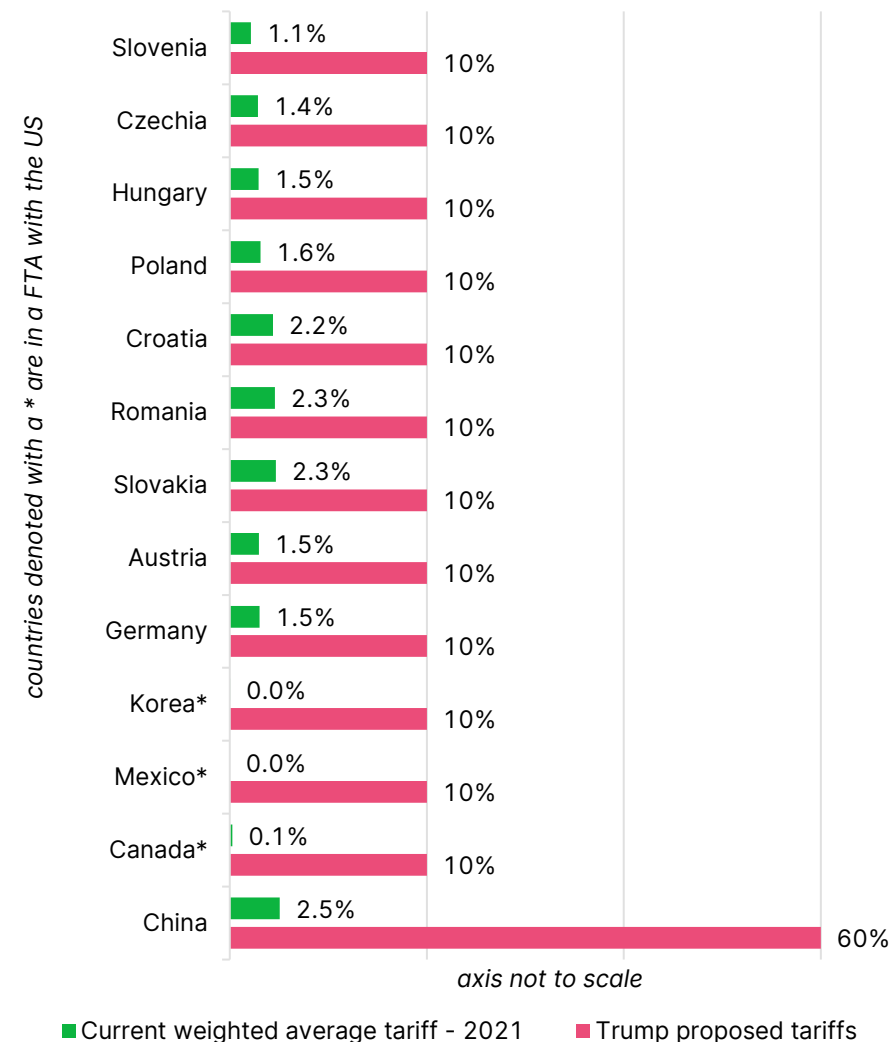


Trade conflicts are in the cards

Donald Trump has repeatedly called for tariffs of 10% on all imports and 60% on imports from China. Such a scenario would mean that world trade would come under enormous pressure. The comparatively more moderate measures taken by the Trump and Biden administrations have already led to a drop in the proportion of Chinese imports to the US. The main beneficiaries of higher US tariffs on Chinese products would be other countries outside the US (Southeast Asian countries, Taiwan or Mexico). By contrast, the EU would barely benefit from the higher US tariffs on Chinese goods, as the EU and China hardly compete with each other in the US market. In contrast to China, the EU roughly kept its share of US imports (under higher tariffs)

The US Constitution states that Congress, not the president, has the authority to impose general purpose tariffs. Thus, Congress must align with the president's policies to pursue such change. However, the president can raise tariffs on imports that pose a threat to national security. These tariffs can be implemented without the approval of Congress, after an investigation by the Department of Commerce.

Tariffs: weighted average and planned

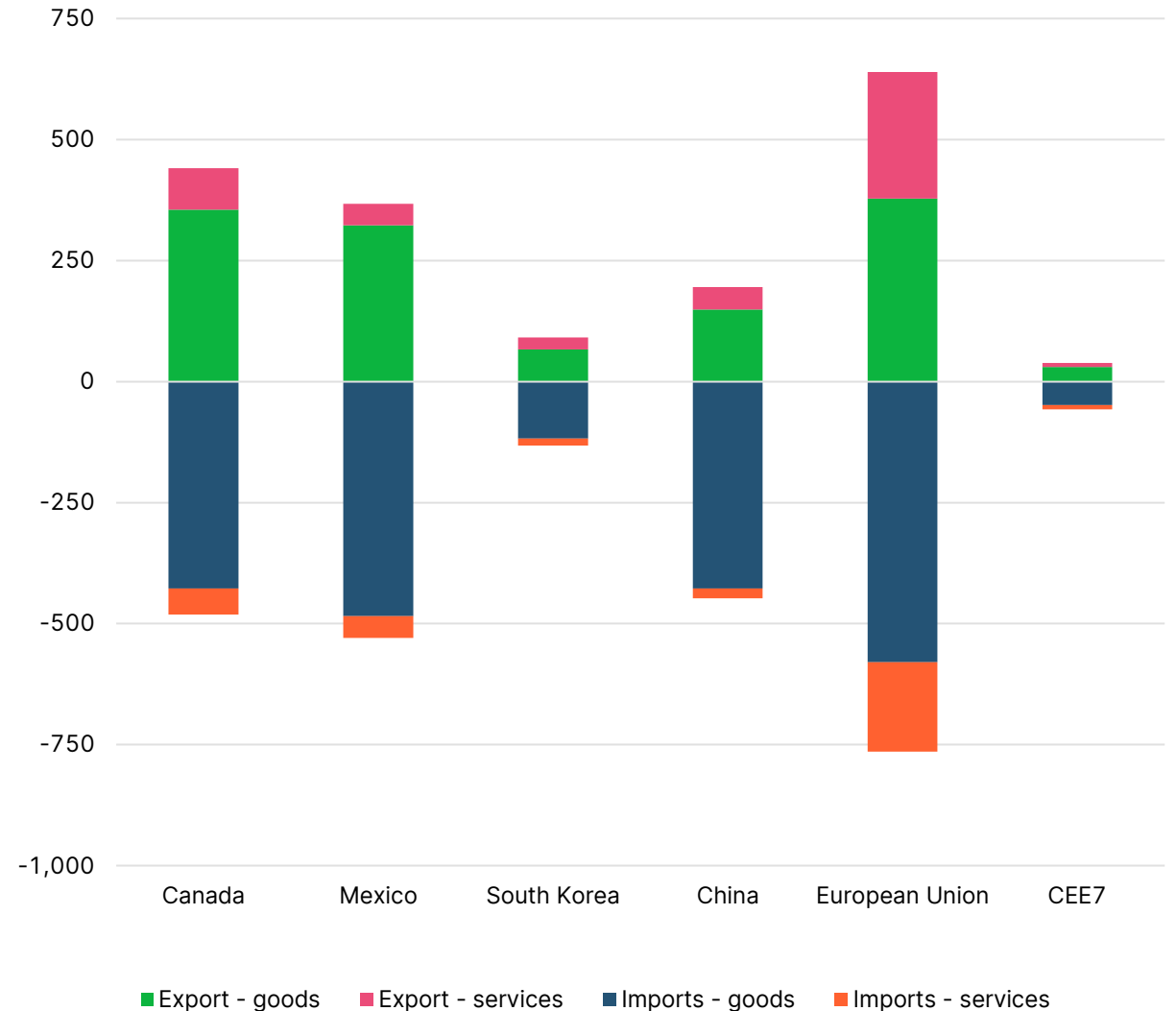


Trump's protectionism and deficits

Donald Trump's presidency (2017-2021) saw an increase in protectionist trade policy. Some trade deals were renegotiated, and new tariffs were introduced, especially on selected Chinese products, with the goal of strengthening and protecting US industry and reducing the US's trade deficit. However, the trade deficit as a percent of GDP increased during Trump's term in office.

As for the impact of increased tariffs on budget revenues: in 2023, customs made up roughly 2% of total tax revenue in comparison to 49% generated by Individual Income Tax and 10% by Corporation Income Tax. Increased customs following the 2024 elections would most likely fall short of covering suggested fiscal measures by either candidate.

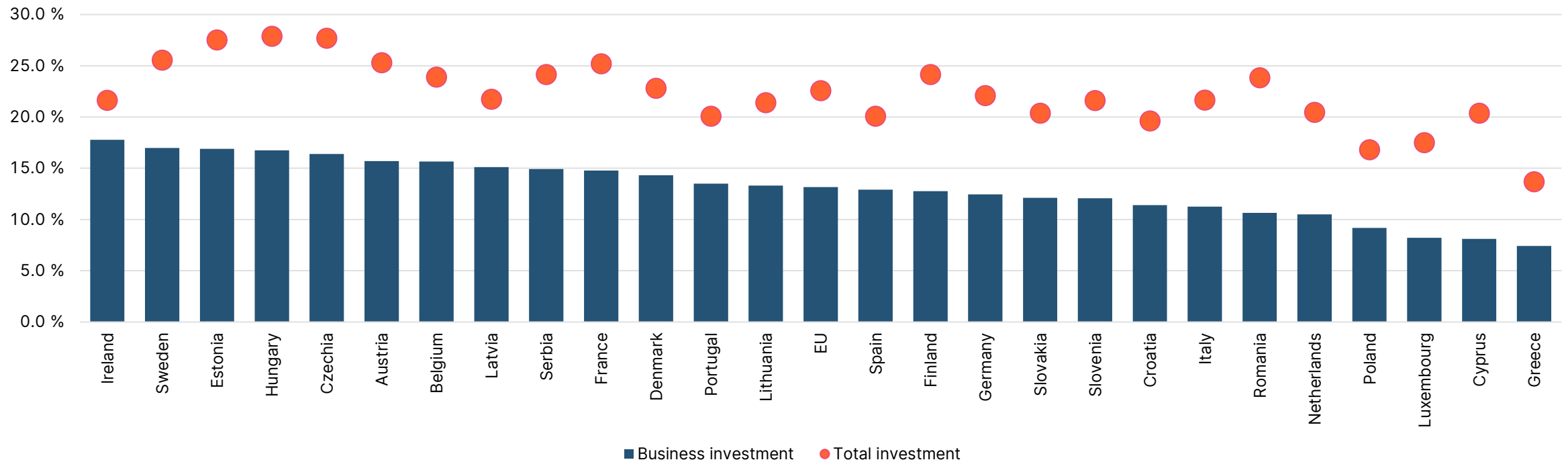
US trade balance with selected partners in 2023, USD billion



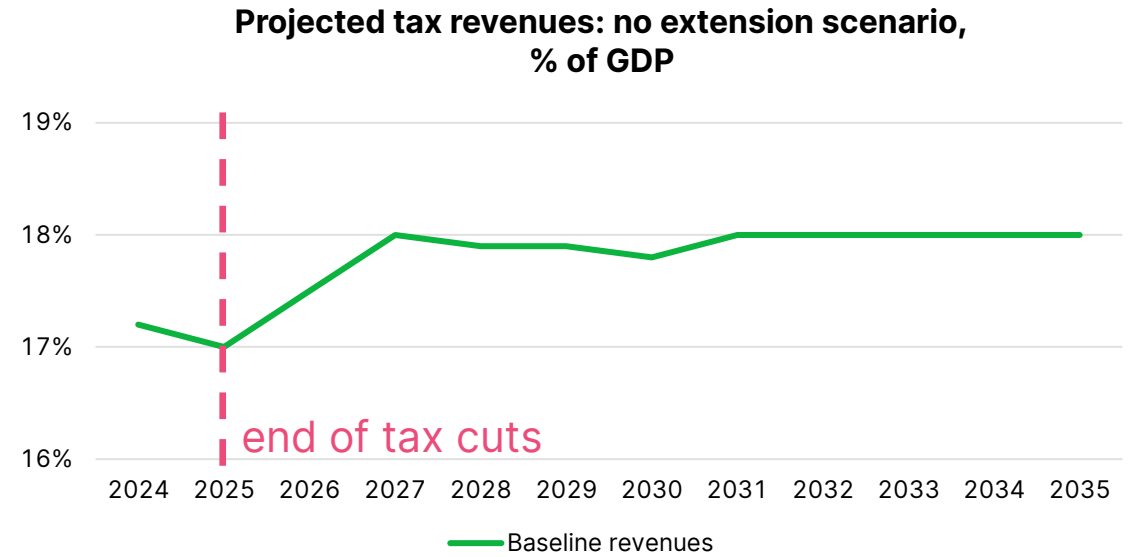
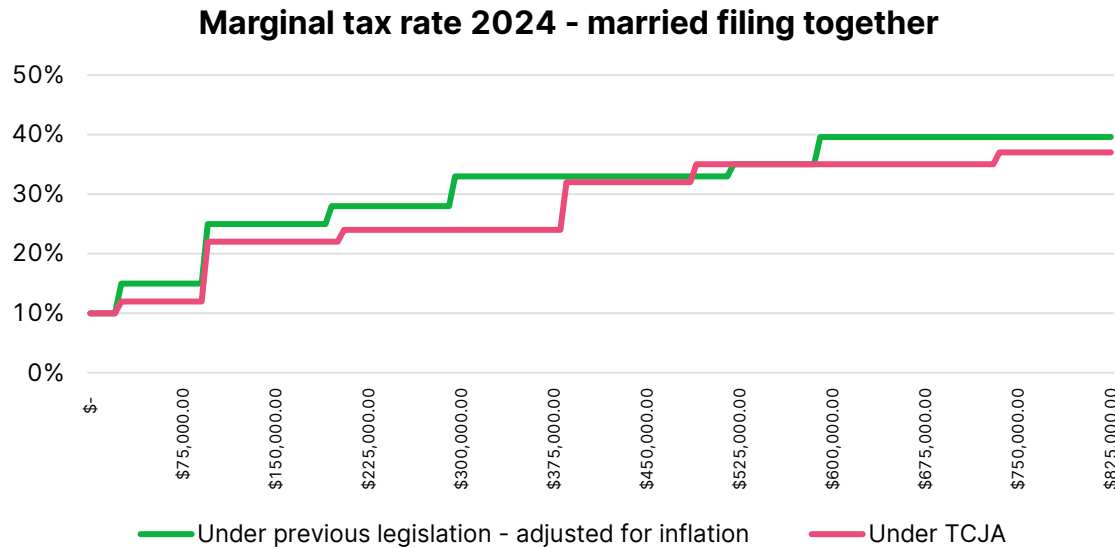
Trade conflicts would increase uncertainty

A renewed trade conflict would also lead to great uncertainty among companies, leading to delays in investments. Such a development would affect more sectors of the economy. For the Eurozone economy, this indirect impact would probably be stronger than through trade flows.

Investment as share of GDP



US budget: no consolidation in sight



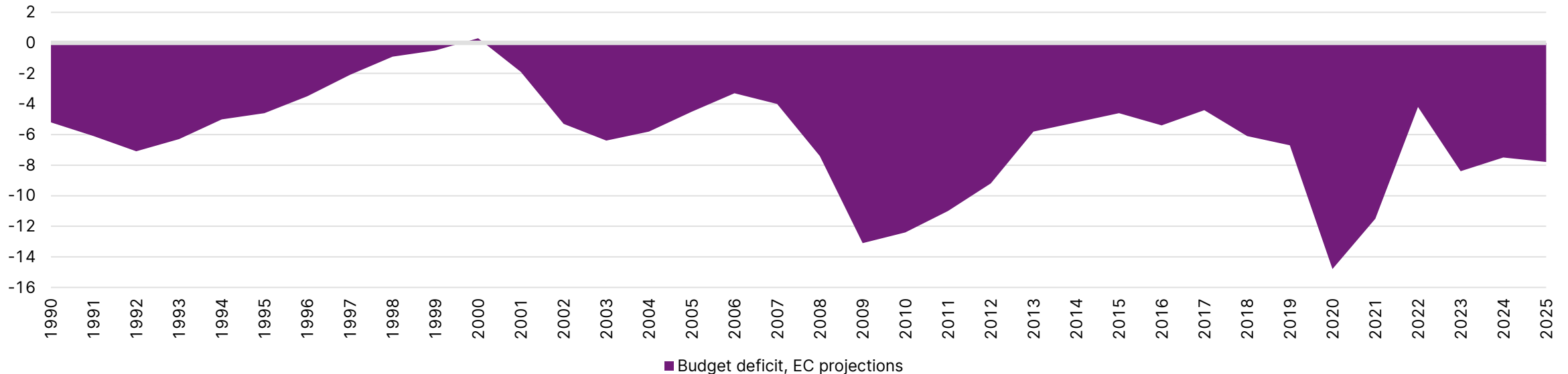
Many parts of the 2017 'Tax Cuts and Jobs Act' (TCJA), a key achievement of Trump's 2017-2021 presidency, are set to expire in 2025. The TCJA includes cuts in personal and corporate income tax and increases in deductibles. According to estimates from the Congressional Budget Office, the debt-to-GDP ratio would increase by 20 percentage points between 2025 and 2034 without an extension of the TCJA.

It is likely that the tax cuts expiring at the end of 2025 will be at least partially extended and the programs of both candidates have additional costly proposals with unclear financing. A sharper increase in deficits -- and subsequently, also of debt -- than the above forecast is therefore a realistic possibility.

US budget: Risks for US in medium and long term

For the markets, the steady rise in US debt over the coming years has hardly been an issue so far. It remains to be seen how long the debt can rise before the markets demand a higher premium. On the one hand, the US is in a unique position as a global hegemonic power, with the US dollar serving as the dominant reserve and trading currency. On the other hand, the US has become accustomed to the constant influx of foreign capital and has thus become dependent. Experience shows that foreign capital reacts more sensitively to rising risks than domestic capital, all the more so if competition among global reserve and trading currencies becomes tougher. There are therefore risks for the US in the medium and long term.

Budget deficit in the US, % of GDP



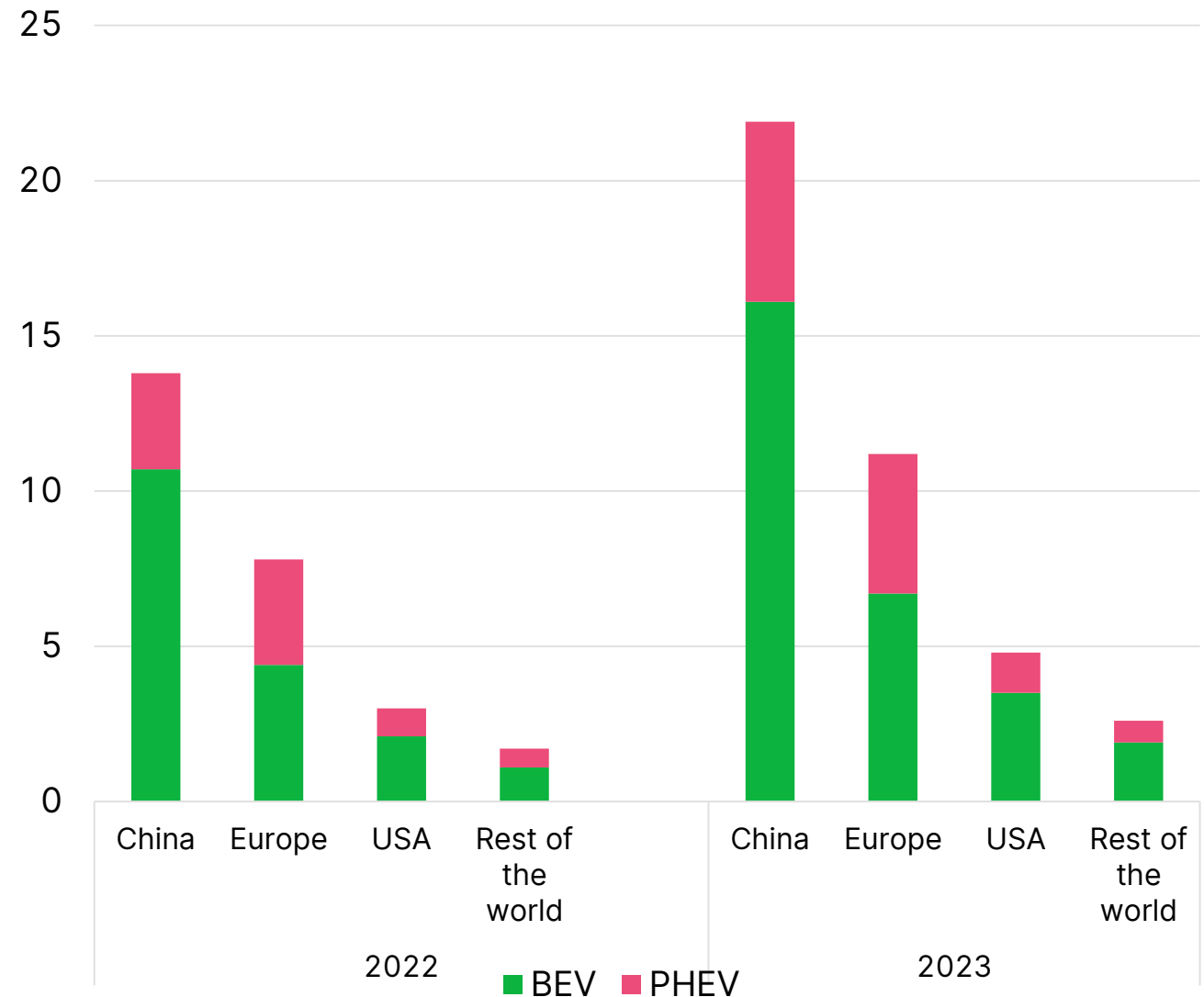
Electric vehicles seen as threat to auto industry by Trump

In the US, new electric car registrations totaled 1.4mn in 2023, increasing by more than 40% compared to 2022. EV industry officials say they would expect Trump to reduce efforts to get more electric vehicles on the roads and to repeal tax incentives for EVs.

Looking at the stock of electric cars, China leads, followed by Europe and the US in third place with almost 5mn electric cars in stock (battery electric cars and plug-in hybrid electric cars).

The US resistance toward electric vehicles would naturally hold-off the global demand, reducing Europe's and the region's export potential in that category.

Global stock of electric cars, million units

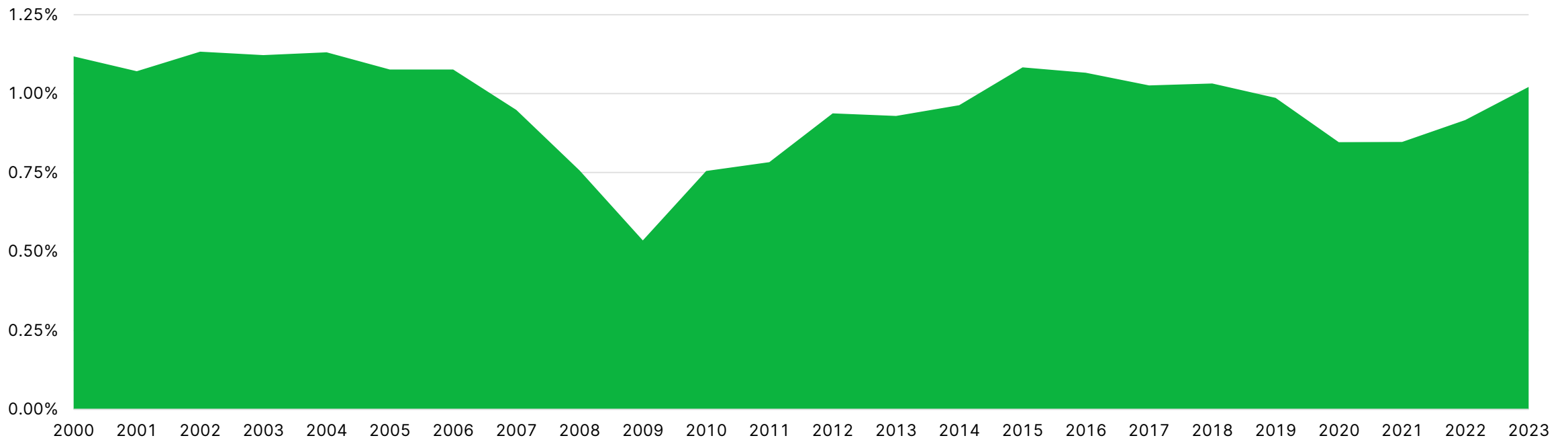


100% tariffs on Chinese electric vehicles already in place

In May 2024, Biden introduced new tariffs on China that range from 100% tariffs on electric vehicles to 50% on solar cells and 25% on aluminum and steel products and respirators and face masks. Other hikes will go into effect in 2025 and 2026.

Such development can be seen as an advantage for trade flows from Europe to the US. On more general note, European manufacturers could benefit from rising export opportunities in the US in the face of higher tariffs with China.

The US automotive trade deficit, % of GDP



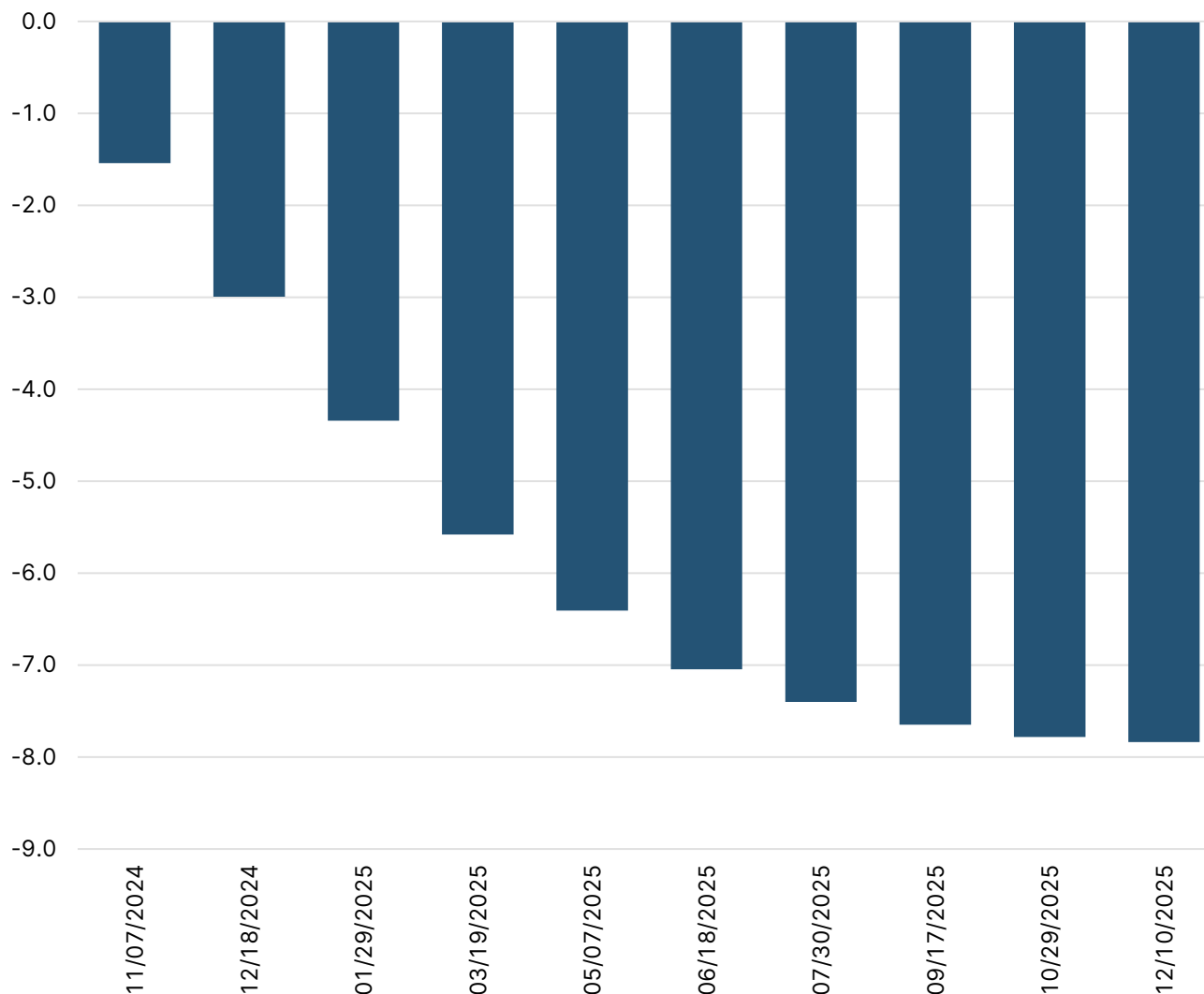
Would monetary policy in the US be affected?

In August 2024, Donald Trump said that presidents should be allowed to influence the Federal Reserve in setting interest rates. That would be a major policy shift that would threaten the Fed's historical independence from politics.

While such a scenario is highly unlikely, we would consider the possibility of higher interest rates in the US in case the FED would evaluate the impact of higher tariffs on inflation as lasting beyond the initial price increases. The FX market could react with dollar strengthening.

Higher interest rates on the major markets would potentially affect the FX and bond markets development in the region.

Implied number of hikes/cuts in the US based on Fed Funds Futures as of September 2024

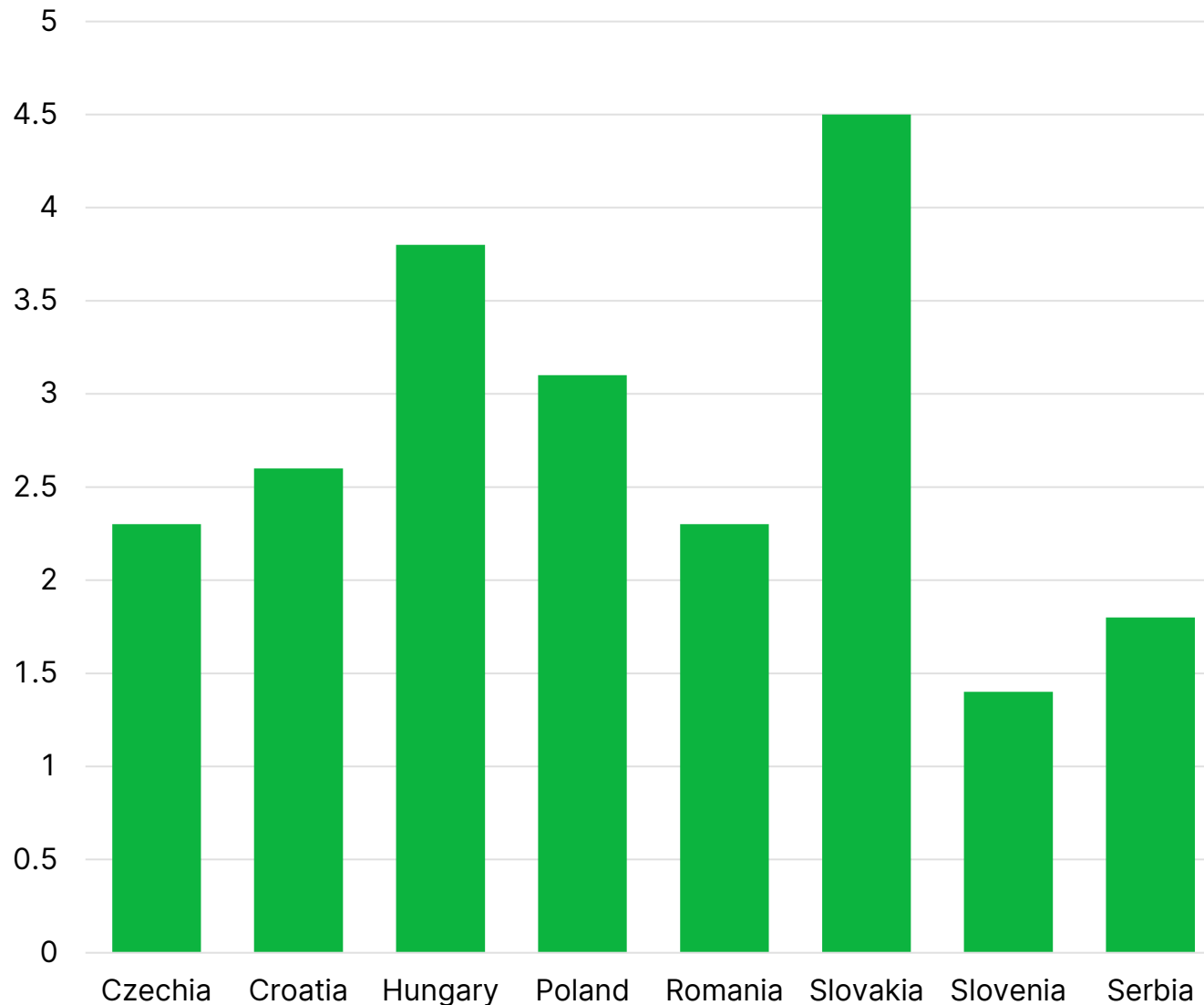


US ELECTION: WHAT SHOULD CEE EXPECT

Economic effects of trade wars on CEE



CEE exports to the US, percent of total



Slovakia and Hungary have highest export share to US

When looking at trade by CEE economies, the share that exports to the US hold is rather low. Slovakia and Hungary are the most exposed in these terms within the region, exporting to the US 4.5% and 3.8% of their total exports, respectively. That comes in contrast to exports to Germany that differs between 20% and 30% for most of the CEE counties

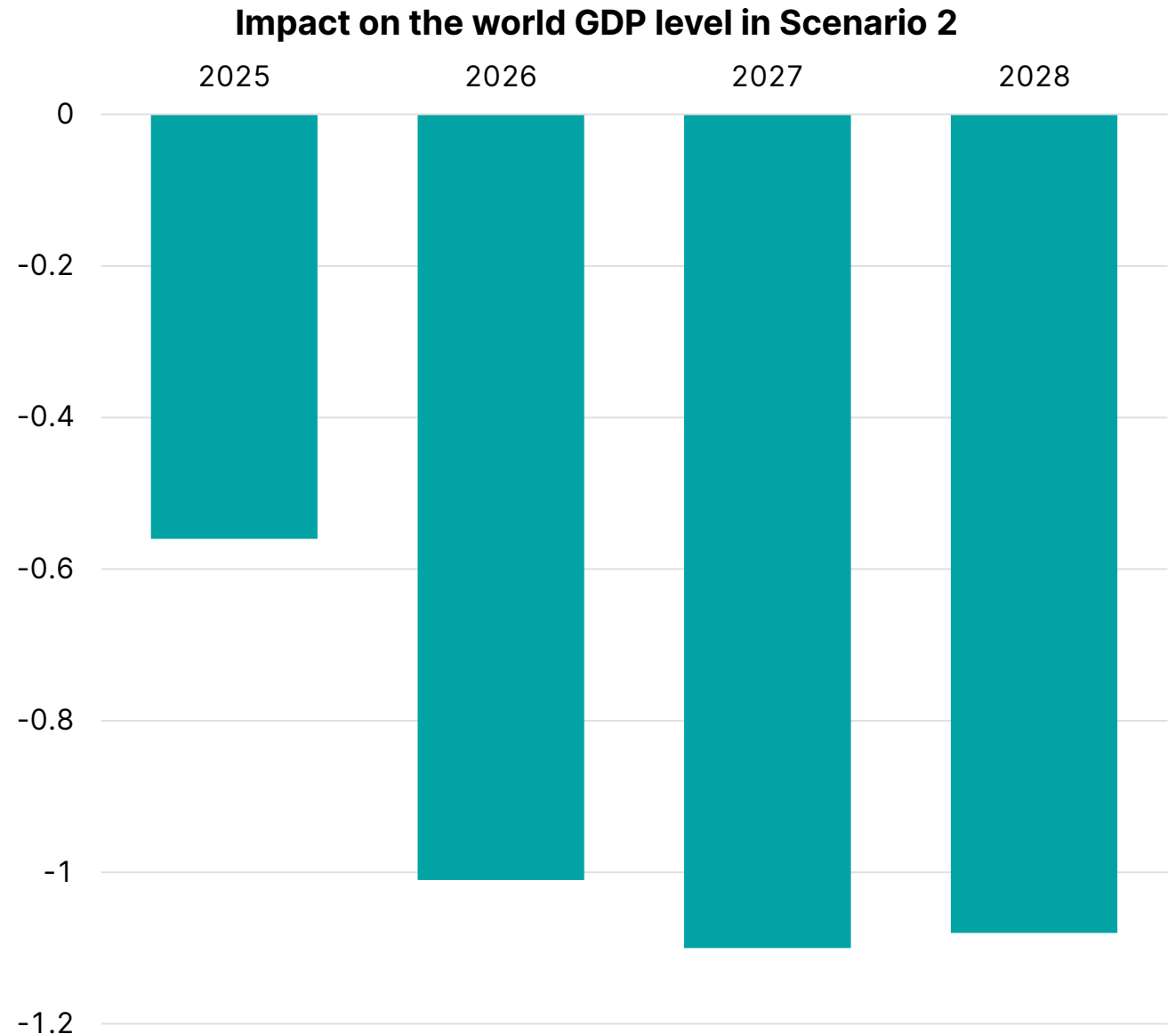
Regarding the products exported to the US, vehicles and automotive parts rank at the top for Slovakia and Hungary. In other countries, electrical machinery and equipment, boilers, machinery and mechanical appliances, as well as pharmaceutical products are among the most exported products.

World economy would be hit hard by trade wars

The German Economic Institute looked at the impact of tariffs on the world economy. Their Scenario 1 involves an increase of US tariffs to 10 percent on all US imports and to 60 percent on US imports from China in 2025. These threats have been publicly promoted by Trump and his former trade advisers.

In Scenario 2 (in reaction to Scenario 1), China would retaliate with a tariff increase of 40 percentage points on imports from the US.

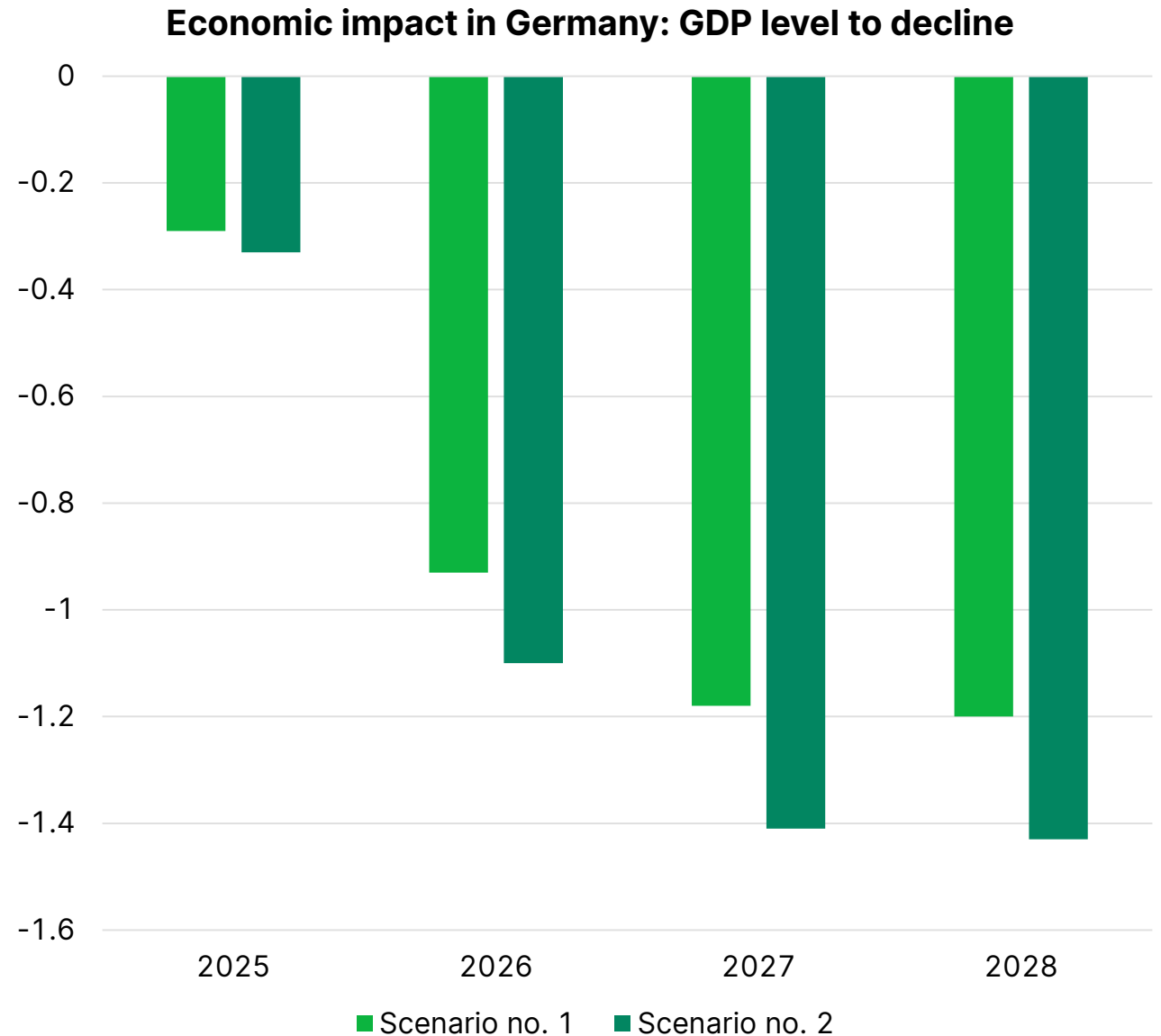
World GDP (in constant prices) would clearly suffer from the tariff shock. Compared to the baseline scenario, the world GDP level would be almost 0.6 percent lower in 2025, with the effect peaking at 1.1 percent in 2027.



Impact on Germany is what matters most for CEE

As far as Germany (CEE's main trading partner) is concerned, the effects become increasingly negative, as the exogenous trade shock takes time to materialize. In 2028, German GDP level would be about 1.2% lower in Scenario 1 and about 1.4% in Scenario 2.

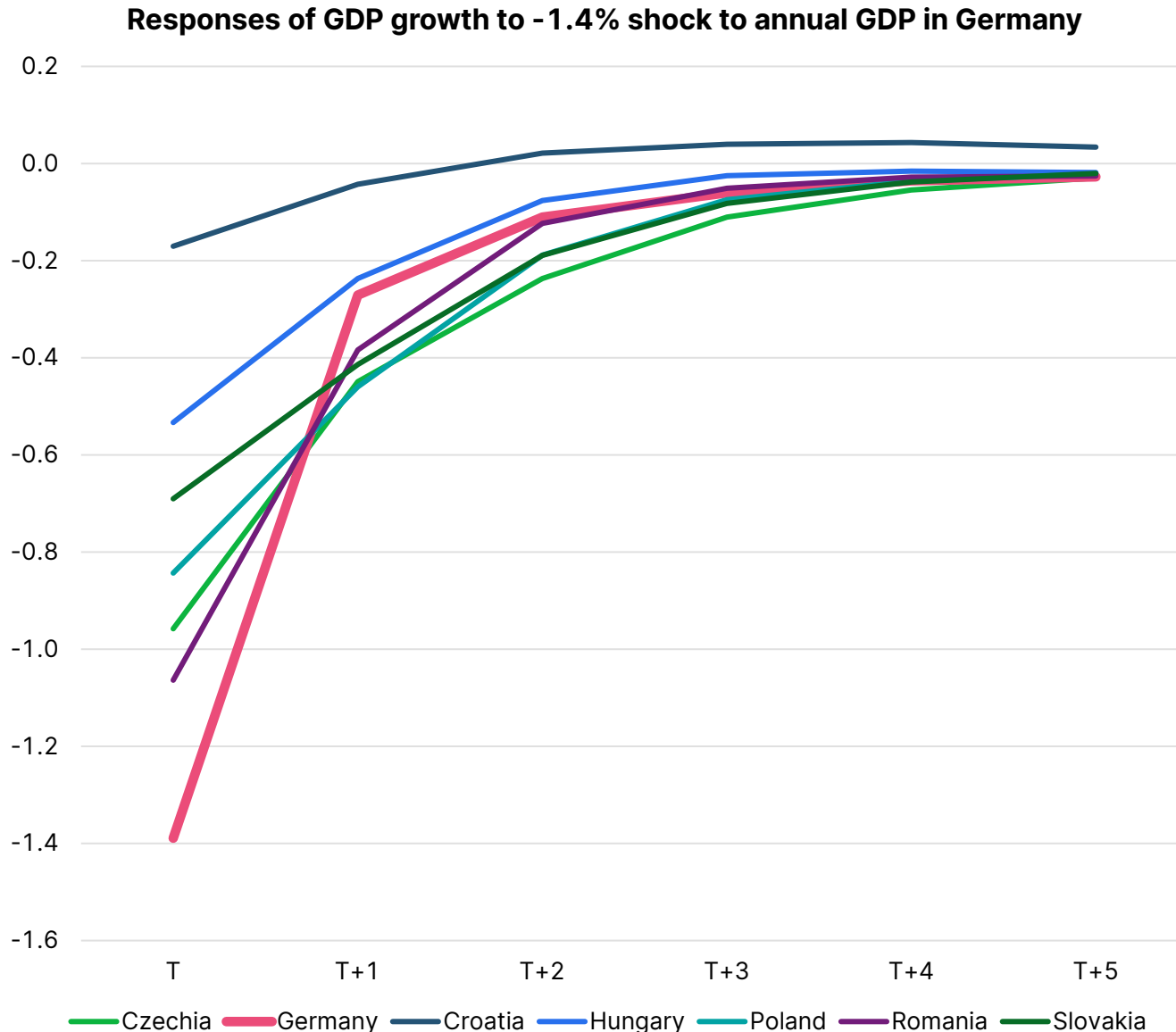
The German Economic Institute reports that the cumulated GDP losses (in constant prices) over the 4-year time horizon amount to approx. EUR 123bn in Scenario 1 and EUR 146bn in Scenario 2. The institute's model also shows that the EU would be hit harder than the US.



Effects of shocked German GDP on CEE economies

- To quantify the relationships between CEE economies and Germany, we used a (Bayesian) Global Vector Autoregression Model (BGVAR), whose sole purpose is to model relations among complex entities.
- To estimate the impact on CEE, we apply the biggest magnitude of the decline in the German GDP level (namely, of about 1.4 percent relative to the baseline scenario) that the German Economic Institute sees occurring in the third and fourth year since the shock (ie, in 2027 and 2028).
- In order to simplify analysis, we consider the biggest impact on GDP level in Germany as happening immediately, in the first year. Under such assumption, lower GDP level by 1.4% would be consistent with GDP growth dynamics that is our direct input into the model.
- We understand that the -1.4% decline in Germany's GDP level in the third and the fourth year since the shock does not imply the same GDP growth dynamics in the respective years. Nevertheless, we decide to take such an approach and label it as "the worst-case scenario" or "the biggest impact scenario".
- Based on that assumption, GDP growth among the CEE economies would be lower by between 1.0% and 0.2% in the first year after the shock.

Effects of shocked German GDP on CEE economies



Romania and Czechia would be the most impacted countries, with GDP growth coming in around 1.0 percentage points lower in response to a -1.4% shock to GDP growth in Germany. The GDP response in Czechia is quite intuitive, given the country's ties to Germany through the manufacturing sector. Romania has the lowest share of gross value added in German exports and final demand. But because Romanian suppliers are smaller and prone to be less integrated in the value chains also due to geographical distance, they are also prone to being cut off first. Poland, Slovakia and Hungary would see GDP growth dropping between -0.8% and -0.5%. Croatia is the least exposed to German underperformance.

US ELECTION: WHAT SHOULD CEE EXPECT

Defense is one of the key issues for CEE that will be influenced greatly by the outcome of the US elections



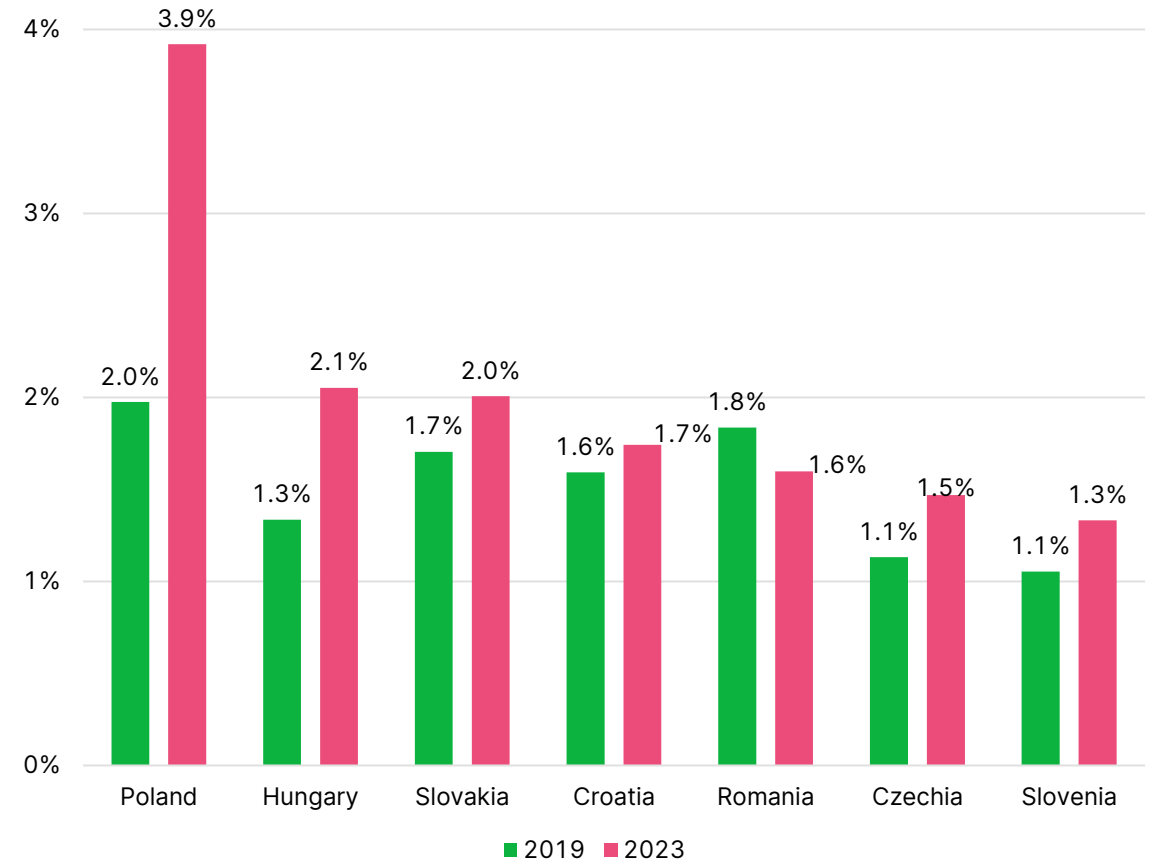
Sustaining the NATO alliance should be high priority for CEE

A second Trump administration would no doubt expect NATO's European members to increase their defense spending. The failure of many of these countries to reach the 2% of GDP target for defense spending was already Trump's main complaint during his presidency. The biggest threat to NATO under a second Trump administration would be that those member countries that have not yet met this target would no longer enjoy the defense largesse and security guarantee provided by the US.

Hungary, Poland and Slovakia met NATO's 2% defense spending goal in 2023. Czechia, Croatia, Romania, and Slovenia are below NATO's guideline, but defense expenditures have increased significantly when compared to a 2019 baseline.

Poland saw the largest increase in defense spending, with expenditure almost doubling over the past four years to 3,9% of GDP. The country plans to further increase its spending on defense to 4.7% of GDP in 2025.

Defense spending, % of GDP

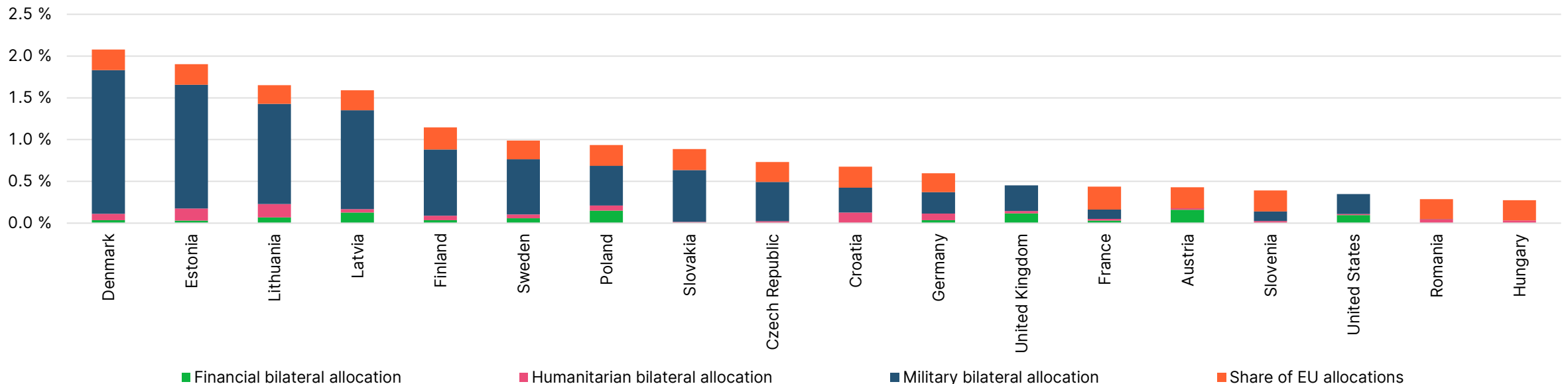


Support for Ukraine is a security issue for the region

Next to NATO alliance, support for Ukraine is also an important security issue for the region. Next to military assistance, EU provides financial and budgetary support as well as humanitarian and emergency assistance. In the region, Romania does not disclose military bilateral support to Ukraine, although it has been praised several times by president Zelenskiy and Romanian parliament approved the transfer of a Patriot system to Ukraine in September.

Trump wants to end the 'endless flow of American treasure' to Ukraine and for European nations to reimburse the US for weapons sent to Ukraine. While these comments were made in 2023, at a June 2024 rally, Trump maintained that sentiment, calling for an end of US aid to Ukraine.

Aid to Ukraine Jan 2022 – Jun 2024 (% of 2021 GDP)



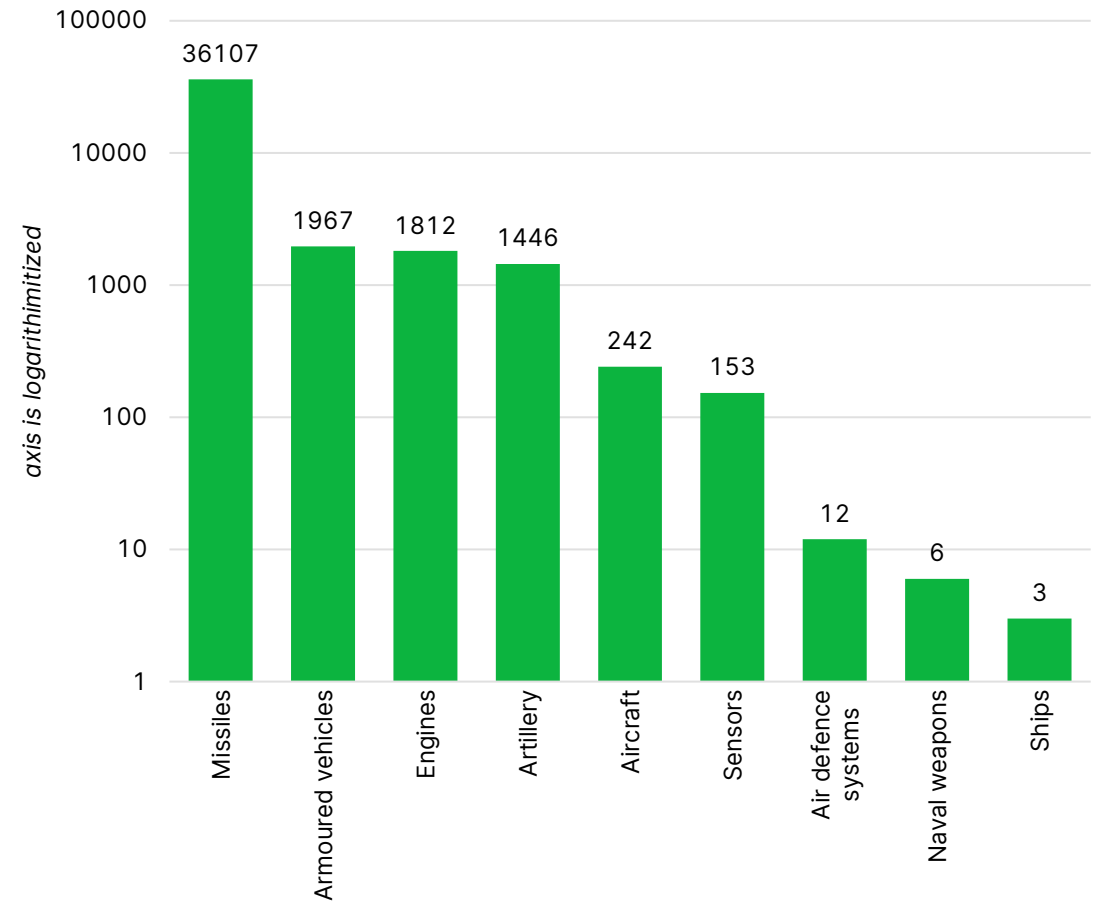
Poland is serious about defense and NATO cooperation

Poland has reacted to the full-scale Russian invasion of Ukraine like no other EU nation. Since the beginning of 2022, the country has ordered almost 1,400 tanks, 700+ rocket launchers, 600+ self-propelled howitzers, 2,100 infantry fighting vehicles, and more than 400 armoured vehicles. In addition to the F-35s already ordered before 2022, Poland ordered 48 light combat aircraft from South Korea, as well as placing orders for attack and transport helicopters.

The 'V Corps' of the US army was reestablished in 2020 to strengthen the US forces in Europe with headquarters established in Poland.

Poland also has established itself as the key logistics hub for weapon deliveries to Ukraine. The newly established NATO-Ukraine 'Joint Analysis, Training and Education Center' in Bydgoszcz creates a further NATO facility in Poland.

Polish armament (number of weapon ordered) in categories from 2022 to 2024



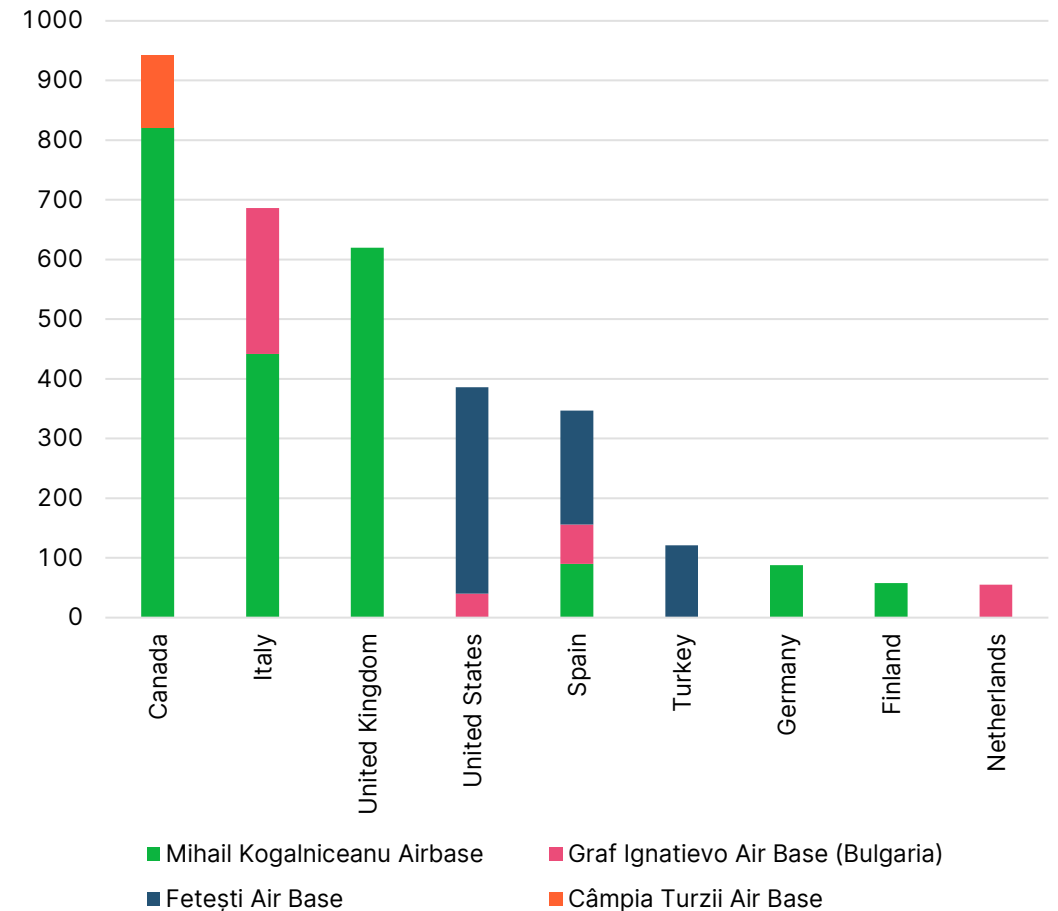
Romania's national security is heavily linked with NATO

The Mihail Kogalniceanu Airbase (MKAB) in the port city of Constanța has been serving as a US military installation since 1999. As part of Operation Atlantic Resolve, MKAB is the main base of a rotating brigade-sized (3-5,000 soldiers) US Army task force. Currently, MKAB is NATO's most eastern base in mainland Europe.

In addition, NATO's enhanced Air Policing in Romania was established in 2014 as a response to Russian aggression, with NATO aircraft deploying to MKAB alongside the Romanian air force.

Starting in 2024, the base is undergoing a EUR 2.5bn construction project with expansion work allowing for more than 10,000 NATO troops to be permanently stationed there alongside their families once finished.

Days deployed to NATO southern Air Policing since 2014



US ELECTION: WHAT SHOULD CEE EXPECT

Climate: US oil and gas production has reached all-time highs



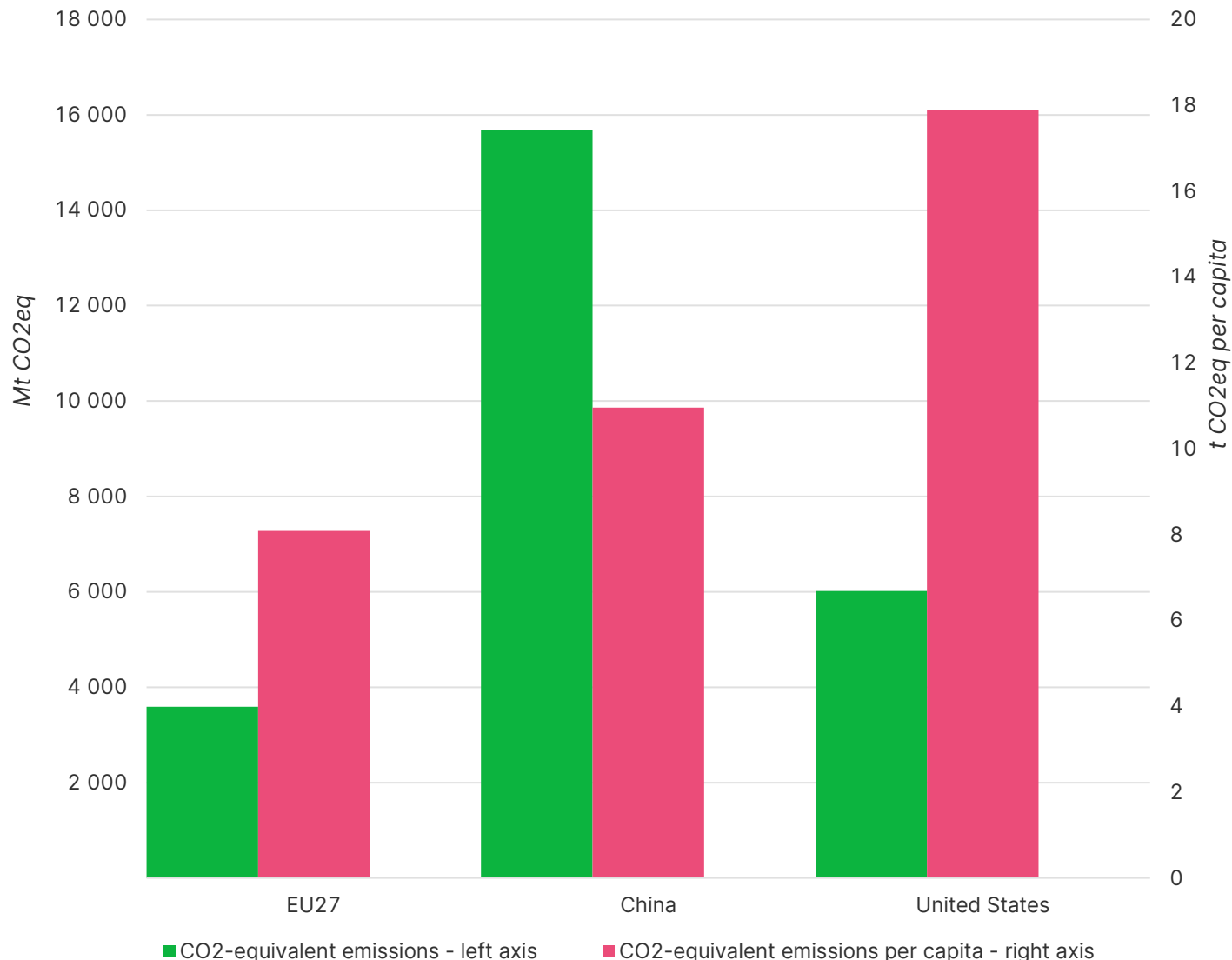
Donald Trump rejects climate science

The US accounts for around 13 percent of global climate pollution and is the world's top oil and gas producer.

Donald Trump's presidency pushed back on climate change regulation, rolling back many environmental rules and withdrawing from the Paris Agreement in 2020.

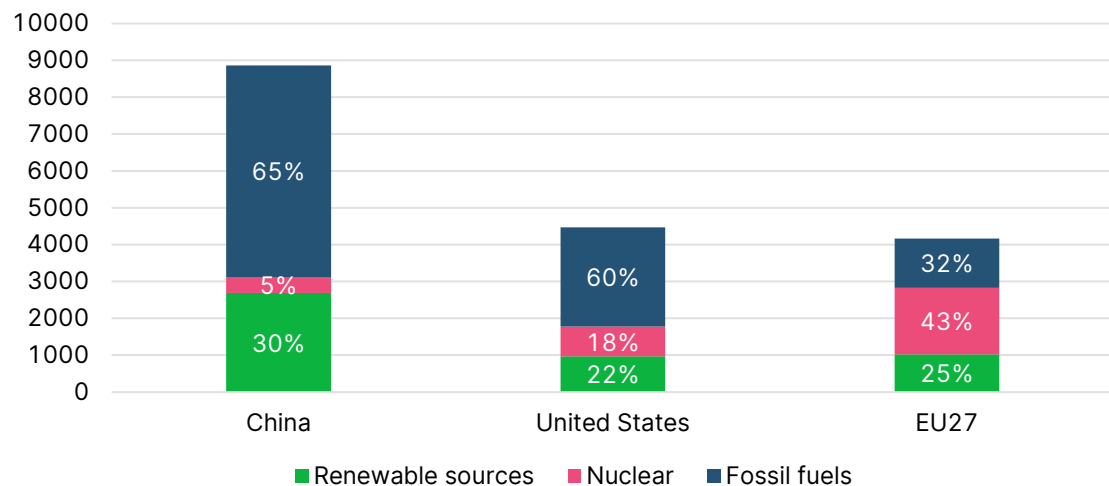
His stance on the climate has not changed. Trump has promised to once again exit the Paris climate agreement (which the Biden administration had rejoined), if not even the entire 1992 treaty known as the UN Framework Convention on Climate Change.

Greenhouse Gas Emission in 2022

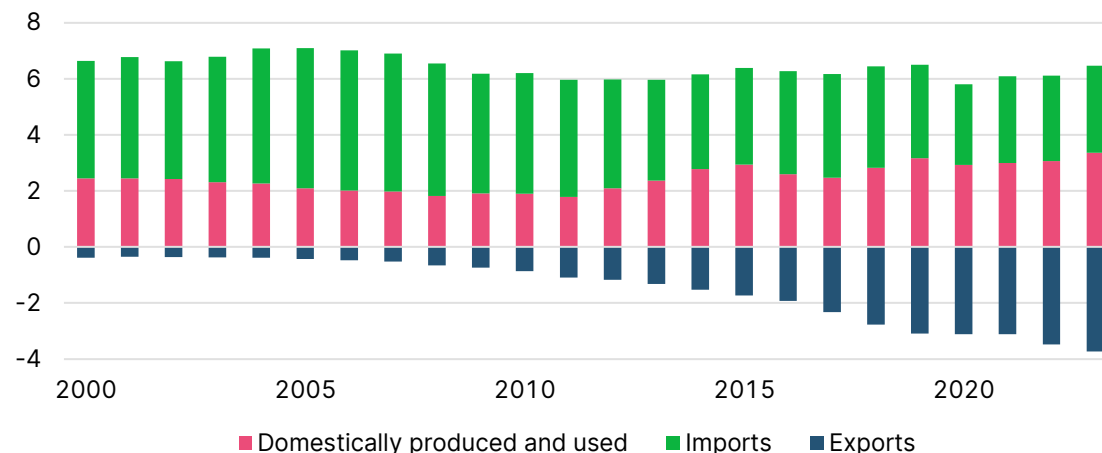


Drill, baby, drill!

Source of electricity generation in TWh - 2022



US crude oil and petroleum products production, imports and exports, billion barrels



Regaining 'energy independence' and cheap energy through fossil fuels are key in GOP energy policy.

During Donald Trump’s presidency, the share of imported crude and petroleum products of oil used in the US remained at about 46-47%. The share of exports of total domestic US production increased by 16 percentage points, however. Crude oil production averaged 12.9 million barrels per day in 2023 setting a global record under the Biden-Harris administration. The previous US and global record of 12.3mn was set in 2019, according to the agency US Energy Information Administration. In other words, the US produced the most crude oil in the past six years in a row.

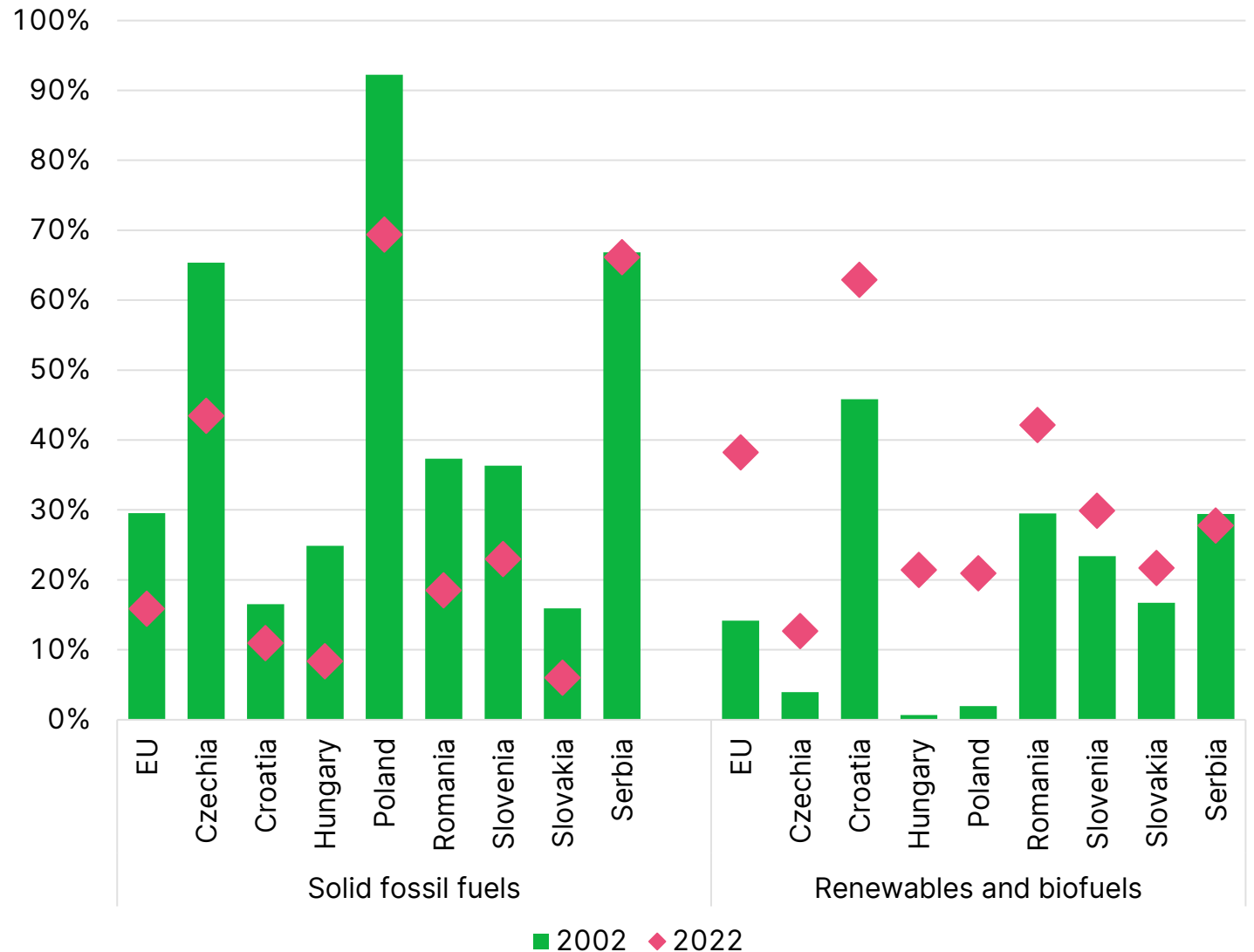
Donald Trump's stance on climate in contrast to EU green transition

The European Green Deal aims to make Europe climate neutral by 2050, boost the economy through green technology, create sustainable industry and transport, and cut pollution.

Decarbonizing the energy system is critical to reach the EU's climate objectives in 2030 and 2050.

European Green Deal might be subject to further negotiations, however.

Production of electricity and derived heat by type of fuel



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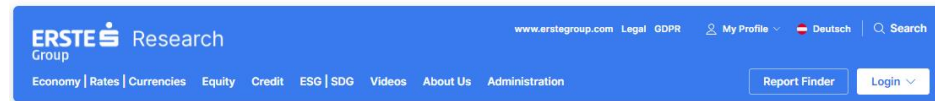


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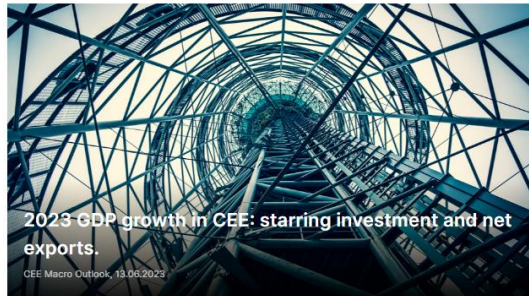


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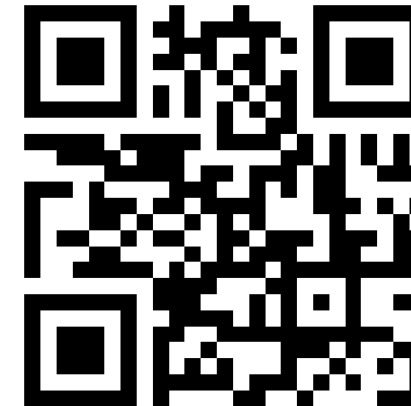
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