Election 2024: Win, Lose or Draw in Investment Grade Credit

The incoming administration will have an impact on every industry within investment grade credit, and each will face its own challenges and opportunities.

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Investment grade credit spreads have tightened to levels last seen in the late 1990s following the 2024 presidential election on the heels of higher growth expectations, tax cuts, and deregulation. The tightening has been broad-based across industries and ratings, but has it been justified?

The current rally provides an opportunity for active managers to reduce exposure to names that may be adversely affected by potential policy changes under the new administration. The uncertainty in the timing and prioritization of any changes is key. For example, although deregulation may initially be positive for corporate credit, it could also increase risk over the long term.

Here, **we examine the impacts of potential policy changes across the industries within the investment grade credit market.**

Win

Energy

An easier regulatory environment could be offset by lower oil prices and higher debt issuance.

Life, Property & Casualty Insurers

Higher interest rates are expected to benefit net investment income, which should support reserve adequacy over time. Additionally, these higher rates are likely to support continued strength in annuity originations.

Airlines

The potential for lax regulation on mergers and acquisitions (M&A) could restart consolidation talks.

Rail Transportation

Freight recession could ease with more industrial onshoring, higher commodity exports and an overall pickup in economic activity. The sector would benefit from lower tax rates and less regulation.

Tobacco

The tobacco industry may find some relief due to lesser regulatory burdens, as the likelihood of a menthol ban would diminish. This could provide a more stable environment for tobacco companies to operate in, although long-term impacts are unclear.

Lose

Banking

While a Republican sweep could be bullish for U.S. bank stocks due to potential regulatory relief and tax cuts, there are concerns about lower capital requirements leading to aggressive growth strategies and the uncertain impact of tariffs. For non-U.S. banks, the impact is also expected to be net negative, particularly in Europe and regions with exposure to China and Latin America. Risks include protectionism, economic ties to China, and the influence of U.S. monetary policy on Europe. However, Europe may respond cohesively to perceived threats, potentially mitigating some negative impacts.

Retail

Retailers are expected to face mostly negative impacts due to potential tariffs that could pressure supply chains and increase costs. This, in turn, could squeeze profit margins. However, the possibility of lower taxes could benefit retailers focused on the domestic market, providing some offset to the challenges posed by tariffs.

Food, Beverage, & Consumer Products

We expect this sector to face mostly negative impacts. The risk of increased mergers and acquisitions looms large against a backdrop of growth, and there are real concerns about food ingredients and health regulations under a new administration. While lower taxes could offer some relief, alcohol brands may be exposed to tariffs, further complicating the landscape for consumer products.

Housing & Building Products

Higher interest rates and import tariffs on materials could make housing and remodeling less affordable. Downpayment assistance, funding for affordable housing construction, and rental control measures are unlikely under the next administration.

Draw

Technology, Media & Telecommunications

Outcomes for Big Tech will likely be uneven. Despite Trump's recent critical comments aimed at Google over search engine dominance, there's a low likelihood that these companies will be broken up. Trade restrictions on China could adversely affect net exporters in the sector. Tariffs on imported technology might increase consumer prices, but could encourage domestic production. There is a slight risk that the CHIPS Act could be repealed, which would particularly impact Intel.

The media sector might see an easier path for mergers and acquisitions, driven more by specific company fundamentals than by broad regulatory changes.

Within telecommunications, potential easing of environmental regulations could reduce costs related to infrastructure development. Changes at the Federal Communications Commission might lead to the repeal of net neutrality legislation, which would benefit internet service providers. Overall, lower corporate tax rates could boost free cash flow across these sectors. However, restrictions on immigration could pose challenges in recruiting top talent.

Health Care

The outlook is mixed for this sector. Within pharmaceuticals, there is potential for larger M&A; an RFK, Jr. appointment to a health care role would create uncertainty. An increase in uninsured patients would challenge hospitals. Within health care services, labs may see marginally lower volumes if uninsured lives increase. Medical devices could be negatively affected by tariffs. Within managed care, Medicare reimbursement has generally been more favorable under Republican administrations; however, total or partial repeal of Affordable Care Act subsidies would negatively impact Medicaid plans.

Utilities

Within renewable developers, elimination of Inflation Reduction Act (IRA) subsidies could result in less favorable economics for solar and wind generation. There should be little impact within the regulated and merchant subsectors.

Automobiles

Tariffs could increase input costs, posing a challenge for manufacturers with significant production in Mexico. Conversely, companies with a stronger domestic presence may benefit. The future of electric vehicle (EV) policy remains uncertain, but a reduction in regulatory burdens could be advantageous for domestic auto manufacturers.

Basic Materials

We expect tariffs to produce winners and losers here, plus increase rates and risk to infrastructure spending bills. Chemicals will most likely be negatively affected, while metals are more likely to get a boost. Paper and packaging are mixed: Stimulative U.S. consumer spending and less regulation on water could help packaging, while paper could be hurt by the impact of tariffs on global growth.

Aerospace & Defense

Aerospace could face challenges due to potential tariffs and protectionism, particularly regarding China, which might affect aircraft demand. However, increased orders for commercial planes from Boeing could help reduce the trade deficit. Defense spending is more influenced by Congress than the president, but low tax rates and potential increases in international demand could occur if U.S. allies are required to pay more for shared defense.

Manufacturing

On one hand, the push for onshoring could serve as a significant tailwind for certain companies, potentially boosting domestic production and reducing reliance on overseas manufacturing. However, changes to the IRA could present headwinds, particularly for firms heavily involved in mergers and acquisitions or those undergoing portfolio transformations. Additionally, tariffs and input costs remain a concern, especially for companies with a substantial portion of their production overseas.

A note about risk

The principal risks are generally those attributable to bond investing. Holdings are subject to market, issuer, credit, prepayment, extension and other risks, and their values may fluctuate. Market risk is the risk that securities may decline in value due to factors affecting the securities markets or particular industries. Issuer risk is the risk that the value of a security may decline for reasons specific to the issuer, such as changes in its financial condition.

IM4014968 • 222977 • 111524 • 2024-11-3872505

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