

Election Update: Prioritize Flexibility

When uncertainty is high, it's important for bond investors to prioritize flexibility. Making small decisions across multiple sectors while maintaining investment flexibility is preferable to one big macro view.

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Topic

Market Events

Key takeaways

- Elections matter for bond investors because the ruling party's economic philosophy directly affects growth, inflation, and monetary policy.
- Although the political landscape is in flux, the favorable economic backdrop in many major economies should help bond investors.
- The second half of 2024 could be volatile, however, and we believe careful security selection will be critical.

Elections matter for bond investors because the economic philosophy of a ruling party directly affects growth, inflation, and monetary policy. Over the past three weeks, the U.S. presidential campaign experienced an assassination attempt on one candidate and the sitting president dropped out of the race. Earlier in the month, the Labour Party won a landslide victory in the U.K. and a snap election in France left that country politically divided. In the U.S., the presidential election race is far from over, and it's too early to call. What is a bond investor to do?

Prioritize flexibility

During periods of heightened uncertainty, it's important for bond investors to prioritize flexibility. When the winds of change are blowing, implementing small decisions across multiple sectors and maintaining investment flexibility are preferable to one big macro view. This is a cornerstone of Allspring's investment process. Fortunately, in today's market, bonds are doing exactly what they're designed to do—namely, generating consistent, predictable cash flows. In markets like the U.S., those cash flow yields are well above medium-term inflation expectations. These positive real yields can help investors manage changing growth and inflation dynamics as political change unfolds.

Economic foundation

With the political landscape influx, the economic backdrop continues to demonstrate decelerating growth and modest disinflation in many major economies. In response, some central banks have started cutting rates, and the Federal Reserve (Fed) is biased toward following that path. This favorable macro backdrop should help bond investors—however, softer data is likely necessary to solidify the Fed's willingness to cut rates.

Waiting game

Investors hoping for political clarity are going to have to wait. The U.S. presidential election is still over three months away and far from over, and the impacts of other elections around the world are just starting to be felt.

For bond investors, the story of 2024 continues as all-in yields are high in both nominal and real terms, yet credit spreads remain tight. We've kept our duration exposure close to neutral relative to benchmarks in many of our strategies, while some accounts have started to position for steeper yield curves. We continue to favor higher-yielding strategies at the front end of yield curves. Corporate credit fundamentals remain intact, and the demand for incremental yields remains robust. However, cyclically tight credit spreads suggest a rotation from corporate credit to securitized products could be warranted. Perhaps of most importance, careful security selection is critical for navigating what's likely to be a volatile second half of 2024.

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