Impacts and implications of a Trump presidency

By Dr Adrian Saville

18 Nov 2016

Whether Hillary Clinton or Donald Trump emerged victorious in the US presidential election, the result was always going to be a second-best outcome for global economies and markets with both candidates being widely regarded as weak.

Given the skew in polling data towards a Clinton victory, the results of the 8 November presidential election came as significant surprise to many voters, with many political experts believing that the race was “Clinton’s to lose”.

123rf.com

On the morning of 9 November, as the prospect of a Trump victory emerged, markets panicked: Japan’s Nikkei 225 stock index slumped 5,4% and the US dollar moved sharply weaker. A little later the FTSE 100 dropped by 146,8 points – or just over 2% – at the opening, while the Dow Jones Industrial Average futures at one point slumped by more than 800 points or 4,2%. These market moves captured the immediate nervousness borne out of Trump’s divisive and erratic campaign. Where Clinton promised a continuation of the same, Trump’s electioneering consisted of sweeping statements, bold – often aggressive – proposals and very little in terms of practical, implementable policy.

From campaigner to statesman in a moment

Then came Trump’s victory speech where he appeared to have transformed from a demagogue to a statesman. As the president-elect spoke, a sense of calm returned to capital markets, with sentiment improving. Markets shifted from scathing to forgiving in the space of Trump’s 15-minute speech. After a campaign marked by threats to build physical and metaphorical walls and create a more isolated US, the conciliatory speech served to elevate Trump to a more presidential status.

It will, however, take time for the full impact of a Trump presidency to emerge. The immediate expectation is for capital markets to be faced with greater uncertainty. Nevertheless, the statesman that emerged on 9 November was constructive and in some regards, even impressive. Trump promised to “double our growth and have the strongest economy anywhere in the world”. Of course, the economic consequences of this election result will be far less dramatic than imagined and they will depend not only on the extent to which Trump tempers his stance and the policy decisions he takes, but also on the administration that he installs and the moderating effects of the institutions around him. It is worth bearing in mind that Trump’s presidency is attached to a Republican Congress with the GOP holding a clean sweep of the House of Representatives and the Senate.

Financial markets may also have started to digest a moderated outcome. By the end of 9 November, the DJIA had added 256 points to the previous day’s close, making for a gain of 1,4% and just 0,3% off its August record high and it went on to close at a record high on 10 November.

But where’s the beef?

A shift in domestic policy will probably favour looser monetary policy and bolder fiscal policy. This could provide a strong short-term stimulus to the US economy and may also have spill-over effects which bolster global demand. For South Africa, stronger world economic growth would boost commodity prices which would aid growth in our economy and strengthen the rand.

Early evidence of domestic policy direction could come in the form of the December Federal Reserve Bank (Fed) interest rate announcement. Trump favours lower interest rates which could be positive for the real economy in the near-term by sustaining consumer spending and boosting parts of industry. However, this would lead to higher consumer price inflation and compromised longer-term growth of the US economy.

Stimulus is also likely to come from fiscal policy in the form of government infrastructure spending. Sectors such as steel, engineering, building and construction are likely to be boosted, but a question mark hangs over the funding plans.

Trump has proposed tax cuts of $3trn over 10 years – equivalent to 1,6% of GDP – leaving the suggested higher spending unfunded. Not only does this point to a larger budget deficit, but it could bring into question the country’s sovereign credit rating. The proposals on the table would put US government debt on course to exceed 100% of GDP in just a few years, placing the US economy in a precarious fiscal position.

Trumpeting Mexican walls and protectionism against China

Trump’s protectionist rhetoric regarding relationships with Mexico and China could translate into friction with European countries, too. South Korea and Japan will also have to step up defence spending, which Trump has threatened to reallocate, which could place stresses on foreign relations among old allies.

There is also potential for a reduction in tensions between the US and Russia under a Trump presidency which could have some constructive geo-political outcomes, including a possible ending of the civil war in Syria. However, the obvious negative effects cannot be overlooked.

Uncertainty also surrounds existing trade agreements and it remains to be seen which direction Trump will take. Higher tariffs on international trade are a way the Trump government could afford some protection to the domestic economy, especially manufacturing. However, this could well be negative for global trade and world economic growth.

A move towards greater protectionism could also represent a specific risk for SA as a beneficiary of the African Growth and Opportunity Act (AGOA), which has seen US become of SA's most important trade partners, comprising $13bn (R176bn) last year alone. AGOA is believed to have created more than 50,000 SA jobs in the last 15 years in labour-intensive industries.

All of that said, in his victory speech Trump indicated that he would promote cooperation among nations, saying: "While we will always put America's interests first, we will deal fairly with everyone. All people and all other nations. We will seek common ground, not hostility; partnership, not conflict."

This last point is perhaps the most critical of all. Borders that have been relatively open to immigrants have been a key factor in promoting US economic growth in modern times. In 1970, the US population comprised 9,6m immigrants, or 4,7% of the population. Today, the immigrant population stands at about 45m people or 13,3%. Based on the experiences of other countries, putting up walls and ejecting migrants would have a net negative impact on capital flows, skills migration, demographic dividend and job creation – all of which are associated with slower economic growth and falling competitiveness.

Investing: never based on forecasts

In considering market reaction to the shock Trump election, it might be helpful to recall what happened in the aftermath of the UK's Brexit vote. After initially recoiling in horror, markets stabilised as the implications were digested. However, Trump has a mercurial nature, and even if a sense of calm returns – as it did after Brexit – there is a resident risk of Trump flare-outs creating greater political uncertainty.

Trump's policies are likely to be marginally negative for the US dollar. However, the near-term outlook for equities is good as fiscal and monetary policies promoted under Trump will help US consumer spending, infrastructural spending and corporate profitability. It is important not to lose sight of the fact that this could ultimately translate into higher productivity, improved competitiveness and faster economic growth, which could more than offset the concerns noted regarding unfunded fiscal spending.

This election result is a reminder that making investments should never be based on predictions, but rather that we should construct our investment portfolios to survive a world of uncertainty and, oftentimes, unknowability. The events since 8 November underscore the permanent importance of a sound investment philosophy and policy, along with the pivotal roles of process, discipline and perspective in investment decision making.

ABOUT THE AUTHOR

Dr Adrian Saville is Citadel's chief strategist.