

US Elections: Low measures on the Richter Scale – an initial reaction

Donald Trump's victory in the US presidential elections may appear seismic. But what of the aftershocks over the next few years?

Don't panic yet

The victory certainly comes as a surprise; particularly because of his vagueness on policy. However, there's no reason to panic just yet. Time will tell on what President Trump plans to do and what he achieves, although unintended consequences, as is often the case, may well be the biggest worries. Here are some of our initial thoughts.



Trade

One of the main aftershocks could well be trade. The US President does have a relatively large amount of discretion in trade. New agreements, such as the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP), are likely to be halted. However, these agreements were essentially political constructs that were primarily designed to benefit the US – and those nations which allied themselves to the US – at the expense of others. The TPP has already started to divide Asia into those who benefit most from it (e.g. Vietnam) and those who don't (e.g. China and Thailand). Trump is basically moving those battle lines but I don't see these fractures as being worse. In fact, a better outcome for China may even delay global and regional instability. Similarly, Trump will no doubt cut the TTIP.

A Trump trade war with China is likely to be no more damaging and arguably less damaging and less effective (but much clumsier, more visible and playing to the gallery) than the TPP would have been. Ultimately this may be a zero-sum game but a zero-sum game where China can't afford to lose without there being potentially serious consequences for the Chinese and global economy.

For this reason, Trump barging noisily through the front door (like a drunkard trying to sneak in stealthily after a late night on the tiles) may prove less of an immediate trigger to a Chinese depression than TPP more subtly attacking China via the backdoor, like a stealthy cat burglar. This makes the FOMC meeting next month even more crucial. Unless policy decisions then also result in a relatively stronger US Dollar, China would almost certainly need to take drastic remedial action because, unless the USD appreciates, RMB may still need to fall a further 20-25% to head off Chinese depression. Such a drastic devaluation makes global deflation almost inevitable.

As debt deflation is a pre-cursor to economic depression, it's a case of 'heads you lose, tails you get slaughtered'. Whilst the FOMC may have been planning to raise rates (even though they may have intended to counteract these with countervailing liquidity measures and asset purchases), any signs of market or economic data weakness may cause the FOMC to delay. Any sizeable delay will likely trigger RMB devaluation. This isn't a new danger but it is now in much sharper focus.

Trump has stated that he would renegotiate NAFTA and potentially withdraw the US from the agreement if consensus with other members could not be found. He would not need congressional approval to do this; although this is not saying he would. Trump will likely come under pressure to give details of his plans, particularly as the Peso drops significantly in value.

Tax

Trump has given some, though little, detail to date. His plans for individuals may send tremors, as they look like Speaker Paul Ryan's 33% tax cut, simplifying the filing process and restructuring the international tax code. Again, the specifics, and what it means for FATCA, are unclear. Trump's corporate tax plan is very much like that of the Congressional Republicans' 20% rate. Reform of both individual and corporate taxation is a priority of Congressional Republicans; however, even with control of the House, it will likely face several obstacles, especially without a supermajority.

Financial Regulation

Trump's victory may mean large parts of the post-GFC Dodd-Frank financial reform act being retracted. It could also mean the end of the Department of Labour's Fiduciary Rule, requiring higher standards of all financial professionals working in retirement planning. This will depend on who Trump brings in as advisors.

Infrastructure

In his campaign, Trump alluded to a US\$1 trillion spending package. Some of this may get past Congress, but it's unlikely the whole lot would. Just a few ripples here but the obvious opportunity may be in US Treasuries that appear to have (to misquote the previous Republican President) misoverreacted badly to the result

Obamacare

Not only has Trump spoken of repealing and repealing the Affordable Care Act (ACA) and replacing Obamacare (within 100 days) but it is also a priority of Republican Congress members in 2017. However, the details of how this will be done are, as yet, unknown. Healthcare could be volatile as a Trump administration may be perceived to be more amenable to Big Pharma but medical services providers could suffer in the ACA.

Overall

This is an unexpected result and the markets clearly didn't like the initial surprise. But no incoming President wants to be responsible for a stock or property market crash as he takes office. So, it's likely that Trump will announce some Wall Street-friendly advisors/nominees to appease the markets. A few small aftershocks possible.

Unintended consequences

Earlier this year Carmignac's Didier Saint-Georges spoke of investing in the volatile global economy as 'dancing on a volcano'.¹ We're now dancing on a volcano that's shaking from the aftershock of the 'Trumpquake'.

We could start to see stronger shakes. Any cancellation or delay of the TTIP could be the trigger for the really big one. As Europe is so fragile, it's unclear whether delaying the TTIP will prolong the agony or bring matters to a head. The biggest immediate risk of a Trump presidency may be that it sets off a populist reaction in Europe. The Italian referendum remains a potential flashpoint and consequently the single currency has now moved from 'under threat' to 'almost certainly terminal and probably within the next 12 months' (if the Euro were a hospital patient, its



Eyjafjallajökull eruption, Iceland. 2010

¹ <https://www.carmignac.co.uk/en/analysis/vigil-arms>

prognosis just became so dire that if it had taken out terminal illness insurance, it could probably submit a claim today). This is the most immediate major danger of today's result. The volcanic lava has been bubbling for some time but the pyroclastic flows are getting harder to dodge because of the sheer scale of issues also piling up in Europe and China.

There's been a lot of use of the 'R' word but I'm not worried about an America recession² – we're beyond that: I'm worried that a recession with this level of private debt will be a depression. I think the jury is out as to whether Trump will bring forward America's next great depression or not – I guess we'll never know the counterfactual but we were getting closer to being trapped between rocks and hard places anyway with nowhere to hide from the inevitable volcanic eruption, especially in China and in Europe whose depressions may well precede and be the catalysts for America's next Great Depression.

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² <http://time.com/money/4563085/donald-trump-global-recession-fears/>