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Literally or Seriously?

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In 1650, during the English Civil War, Oliver Cromwell wrote to the Scottish Kirk with the plea, “I beseech you in the bowels of Christ, consider that you may be mistaken.” The re-election of Donald Trump to the US Presidency is gravely consequential, but outside of the US Midwest, it has been greeted with a combination of fear, derision and astonishment.

Nonetheless, with a clean sweep of the Senate, House of Representatives and, effectively, the Supreme Court; Trump is unequivocally the person the US wants at its head. Is it time, therefore, to ask whether we ourselves are mistaken? Can Trump be a positive development for the world economy and by extension, in our area of concern, world markets. Is it possible that the new President could be a catalyst for major positive change. If so, how can we position for it?

There are four areas of policy that have serious implications for growth: tariffs, immigration, taxation and federal spending.

We spoke about tariffs in our last Thought so we won’t run through the details again. Nevertheless, it is notable and surprising that the proposed China Tariff has been moderated to 10% which is substantially less than the 60% initially mooted. That is good for Sino-US relations (and tech, since much of the tech hardware that runs our lives these days, is still made in China). But Trump announced a 25% tariff on Canada and Mexico to “fight illegal migration and drug trafficking.” The problem is that much of US manufacturing relies on base commodity inputs imported from Canada and much of US industry and farming relies of labour imported from Mexico. Prices of base commodities and labour will therefore rise.

The subject of migration/immigration has become deeply politicised but suffice to say that the US is at full employment and any reduction in labour supply will tend to raise wages. That is a good thing for affected labour segments, but it is merely inflationary for everybody else. Higher average real wages require a rise in productivity which requires investment.

In his first administration, Trump passed a $1 trillion tax cut to benefit corporations and shareholders that was reflected in an immediate increase in the Federal Debt. There is every indication that he intends to the same this time around. In principle a lower corporation tax rate should allow businesses to invest more and thus raise productivity. In practice, the tax cuts tend to be passed onto shareholders via dividends and share buybacks; net investment doesn’t increase much, if at all. Nonetheless, a Trump presidency is likely to offer a bonanza to owners of corporate wealth i.e. shareholders with obvious implications for investors.

Elon Musk, the storied technocrat and world’s richest man, has been appointed by Trump to head the DOGE – Department of Government Efficiency – with the aim of reducing federal spending by $2 trillion – circa 8% of US GDP. When Musk bought Twitter (now -X) in 2022, he immediately fired 80% of Twitter’s employees. The prognosis for federal employees under the new administration is not good. Equally, it implies a substantial fall in public investment, the more so since Trump is expected to pledge significant increases in “defense” spending crowding out other areas.

In a modern economy, a net fall in public spending can be expected to reduce productivity via impaired infrastructure and impaired human capital. But, more positively, a Trump presidency is likely to catalyse European spending (on defence) and has already sparked a fierce debate about the damaging “debt-brake” imposed on the German Federal budget process.

Much of Trump’s policy programme is likely to induce a rise in inflation forcing the US Federal Reserve to keep interest rates higher than they otherwise would, also raising the spectre of early interest rate increases. That would bring Trump and the Fed into conflict, a development markets would not welcome.

The word most associated with Trump is “unpredictable” and much of Trump’s policy programme is loaded with the risks of “unintended consequences”. There are some aspects of the programme that are good news for investors in US companies, principally the tax breaks, although the innate unpredictability of the administration can be expected to weigh on markets suggesting some caution is still warranted.

As you would expect, we expend a lot of energy in Tacit considering the implications of the policy pronouncements emerging from President-elect Trump and his associates. Our concern is to have a proportionate and realistic perspective on the possible implications for global trade and investments. We think it wise not to take the most extreme policy pronouncements literally, but to take Donald Trump very seriously, for he is nothing if not the consummate dealmaker. In a recent Financial Times interview with Christine Lagarde, head of the European Central Bank, she advocates meeting Trump on familiar ground by actively pursuing trade with the US in sectors such as energy and defence, and not to retreat behind the barricades of a trade war. For the moment, our expectation is that international pragmatism will bridge the gulf between extreme policy rhetoric and economic reality.