

Insights, Tacit Thought | Weekly Investment Insights

Thinking about the Mid-terms

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"It's eight o'clock, good morning and here is the fake news!"

Now that's not something you'd expect to hear in any news broadcast. But with the results of the US midterm elections well documented, both sides unsurprisingly are claiming victory.

Here are the factual headlines. The Democrats have taken control of the House of Representatives. But the Republicans and President Trump secured their hold on the Senate, the upper house of Congress.

In reality it's a victory for the far-sightedness of the Founding Fathers who designed a written constitution steeped in the values of 18th century British Enlightenment.

They set out to create a written constitution that would prevent the concentration of power being held by one man or legislative body. They did it with an elaborate 'Separation of Powers' which divided the US government into three. The Executive (President), Legislature (Congress) and the Judiciary (Supreme Court). By deliberate design, they're all separate and independent of each other.

The mid-term elections are congressional. Congress itself is divided into two bodies: The House of Representatives and the Senate. Congressmen are subject to election every two years but Senators (the smaller of the two bodies) serve 6 year terms so that at any given election only a third of senatorial seats are up for grabs.

Until this week, and in breach of the spirit of the constitution, each branch of government was Republican including the Supreme Court following the controversial appointment of Donald Trump's candidate, Brett Kavanaugh.

The mid-terms have gone some way to redressing the balance. The fabled checks and balances of the constitution have been restored. The results mean there is an effective domestic opposition to the President.

But what does this mean for investors?

In the near-term we're looking at gridlock. No more tax cuts but also no cuts to Medicare or other social programs either. The Trump tax cut was ill timed from a cyclical perspective with the US economy already booming. But tax-cutting restraint will have positive implications for the long-term deficit and may reduce upward pressure on interest rates, bond yields and the US dollar.

The Democratic House will now have subpoena powers to investigate Trump's tax affairs, suspected Russian collusion as well as his business interests.

He will inevitably blame Democrats for any slowdown in the economy and this will shield the Federal Reserve from pressure to restrain monetary policy. Financial markets will be reassured by a depoliticised Federal Reserve.

What won't happen is any change in US foreign policy. The president always has a free hand unrestricted by other branches of government. Foreign policy could well take the place of his domestic agenda.

President Trump is due to meet Xi Jinping at the G20 summit in Buenos Aires on December 1st. Whatever the outcome of the talks we can surely expect a Trump tweet to declare "Best TRADE deal ever in HISTORY with CHINA."

Fake or fact it depends from which political perspective you view it from. Only the future will determine whether or not he's right or wrong.

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