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THE POTENTIAL IMPACT OF A TRUMP PRESIDENCY ON FINANCIAL MARKETS

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Although the US election race is not looking as uncomfortably tight as it was, it has been surprising that financial markets have not shown more nervousness about the possibility of Donald Trump becoming US president, a man who has been described as a ‘con man’ and a ‘duplicitous demagogue’. Brexit provided us with a reminder that in any two-horse race, each potential outcome should be taken seriously, so we must carefully consider the disquieting possibility of a Trump presidency.

How much damage could President Trump do?

Some of the apparent complacency in financial markets may come from a belief (or hope) that the powers of a US president are limited. While it is true that there are important constraints, the president does have more discretion than is comfortable in current circumstances. A key concern is, he can ‘un-sign’ the executive orders of previous presidents. Apparently Trump’s transition team are identifying orders issued by President Obama which could be rescinded – this does not mean that things can be reversed overnight, but these are genuine powers. For example, Trump could suspend the Syrian refugee program. More worryingly, he could ask the Commerce department to impose tariffs on Chinese goods (the World Trade Organisation would rule this illegal but Trump could ignore that and leave the WTO).

One of the biggest areas of concern is US interaction with the rest of the world. Particularly worrying are suggestions that the US may reduce its role in tackling global problems – and may not provide guaranteed support for NATO countries under attack, which would fundamentally change the balance of power in Europe. Equally concerning are his beliefs that free trade and immigration are bad for the economy.

Trump will need the support of federal employees to get things done, which could prove an obstacle, even after appointing loyalists to senior positions. This is why Trump is looking at weakening the high level of employment security currently enjoyed by government officials.

Trump has the potential to damage the economy simply by undermining confidence. He has commented “I am the king of debt...I would borrow, knowing that if the economy crashed, you could make a deal.” This statement shows Trump’s astounding naivety. The implication that the world’s safe haven asset, US treasuries, might be much riskier than perceived could represent a more fundamental shift than even the US housing debt crisis in 2008. His naivety with respect to NATO treaty obligations to treat an attack on one as an attack on all is equally alarming.

Best and worst case scenarios in a Trump presidency

The worst case Trump scenario is that he triggers a shift in risk perceptions which leads to sharp declines in both bond and share prices. At the other end of the spectrum, being unconstrained by prevailing dogma, a Trump best case scenario for the economy could result from significant fiscal stimulus in the form of badly needed infrastructure spending. Though this would present challenges for financial markets, a properly targeted range of measures could stimulate demand in a sustainable fashion.

Our base expectation is that a Trump victory would be destabilising for financial markets. We can hope that November will result in a new President Clinton; however, Trump has changed the political landscape and we also hope that policy makers will reflect on what has brought us to the current predicament. The rise of Trump and extremist political parties in Europe, plus the Brexit vote, are a wake-up call for the establishment. We can hope that these forces empower governments to act more boldly and take on more of the burden of stimulating the economy, rather than relying on the central banks.

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