Trump 2.0: what impact for the markets?

Didier Bouvignies
General Partner, CIO

In contrast to the envisaged scenario, Donald Trump's victory in the race for the US presidential election seems clear. Given the gap between the two candidates, a recount will not be necessary, while a 'Republican sweep scenario' even seems to be taking shape. This 'Grand Slam', with the conquest of the White House and a majority in the Senate and the House of Representatives (to be confirmed), should give the 47th President of the United States a free hand for his second term.

Markets are neither political nor moral. As in real estate, where investments are based on rents received and borrowing rates, equity investors evaluate programmes on their influence on corporate earnings. This vision, which is generally short-term, also takes into account the level of interest rates with which they will have to discount them.

On the earnings front, with his pro-business agenda favouring growth and profits, Trump's election is viewed fairly favourably. The main measures include:

- Cutting corporate tax rate from 21% to 15%, with an estimated impact on earnings per share of between 3% and 4% by 2026[1].
- The renewal of tax cuts for households and businesses enacted in 2017 and due to expire, the cost of which is estimated at between $3.3 trillion and $4.6 trillion over 10 years[2].
- Cheaper energy, with the end of restrictions on oil and gas drilling.
- Deregulation of the banking sector.

These measures do, however, carry a significant risk of higher interest rates in the inflationary component with :

- The introduction of tariffs of 60% on Chinese imports and 10% on others.
- An immigration plan that aims to expel 3 million illegal immigrants, who have nonetheless made a major contribution to productivity and limited inflationary pressures under the Biden era.

But also in the real component, due to :

- A more moderate outlook for a cut in Fed intervention rates, due to an increase in the risks associated with the pace of growth and inflation potentially generated by the implementation of D. Trump's programme.
- A fiscal policy leading to a widening of the budget deficit, estimated at 7.5 trillion dollars by 2035, with a deficit of 6.4% of GDP[2]. Public debt, currently at 120%, could prove difficult to control, prompting investors to raise the terminal rate[3].
- Uncertainty about the future, with the risk of the Fed making a mistake in its monetary policy, which could also justify raising the neutral rate.

The impact of this election on the rest of the world is difficult to envisage, particularly for China and Europe. For European companies, the return of Donald Trump to the White House is synonymous with an unfavourable trade policy and considerable geopolitical uncertainties, with negative implications for the continent's growth. All the more so as Europe's share of US imports rose to 23%, while China's slowed to 17%[4]. In the case of China, the hope of a more precise, and even more massive, recovery plan will help to lend credibility to the initial initiatives.

However, the positive fallout from temporarily faster US growth and a stronger US dollar may mitigate this damage somewhat. Weaker growth in Europe could also tip the balance towards a slightly more flexible stance on the part of the European Central Bank.

Trump's approach to geopolitical issues (less support for Ukraine, pressure on Kiev to accept an armistice on favourable terms to Russia) remains a major issue. Their consequences are just as important for Europe as they are for China, in terms of gauging the determination of the United States to dissuade a potential attempt to take Taiwan by force. The markets will probably not have the will to anticipate the impact at this stage.

What are the consequences for the markets?

Unlike in 2016, the result of this election comes as no real surprise to the markets. Investors had been betting heavily on the Trump trade since the beginning of October, as evidenced by the rate hikes that were ignored by the equity markets, which continued to set successive record highs.

A number of sectors are likely to emerge as winners, led by Banks, Energy and Industrials, while the outlook for importing consumer spending stocks and renewables is gloomier.

The effects on technology are more uncertain. The fact that monopolies are no longer being called into question is proving rather favourable for the sector, but the appreciation of the dollar and Mr Trump's difficult relations with the leaders of the ‘Tech’ industry could have deleterious effects. The greenback should benefit from the rise in interest rates and the outlook for growth, while crypto-currencies should benefit from measures to promote the digital currency and from fears about runaway debt.

However, the history of the markets leads us to believe that these reactions should be tempered. Investors' expectations regarding political considerations have often been disappointed. Similarly, the markets have frequently preferred a divided Congress to a President with full powers. There are two main reasons for this analysis.

Trump 2.0 comes at a very different time in the economic cycle than when version 1.0 took office in 2016, with a growth rate of around 3%, a low household savings rate and twin deficits - fiscal at 6% and trade amounting to $1 trillion[5]. Launching a fiscal stimulus programme in these conditions, while the fight against inflation continues, could be tantamount to adding fuel to the fire.

In addition, the formidable economic success of the United States, which has no equal, is characterised by significant productivity gains thanks to flexibility, innovation and state support, generating returns on equity of over 15% for listed companies[1]. These results were made possible by access to abundant savings from surplus countries in the rest of the world (Asia, Germany, oil-producing countries) which, attracted by this success, financed the private equity investments at low interest rates through the “US America Fund“. For this dynamic to last, the cycle would have to continue - the last real recession dates back to 2008 - and creditors would have to agree to continue financing the deficits of a potentially more aggressive partner.

This election could also prove to be an opportunity for Europe. An electroshock to encourage the Union to reinvest its surplus savings, currently totalling 400 billion euros[5] , within its own area, given the need for defence and energy transition.

In conclusion, the US market is moving along a ridge where earnings growth can offset a very low risk premium with hopes of lower interest rates. Donald Trump's measures could disrupt this vision, and the interest rate market will dictate developments in the equity markets. However, if the recent slowdown in employment is confirmed, the rise in interest rates should be more contained and prove favourable for the equity markets.

Check this document on our website

(1) Source: Goldman Sachs, 2024.
(2) Source: Committee for Responsible Federal Budget, 2024.
(3) Source: Federal Reserve, 2024.
(4) Source: MUFG Bank Economic Research, 2024.
(5) Source: Bloomberg, November 2024.

About the Asset Management's division of Rothschild & Co

As the specialised asset management division of the Rothschild & Co group, we offer personalised asset management services to a broad client base of institutional investors, financial intermediaries and distributors.

Our development is focused on a range of open-ended funds, marketed under five strong brands: Conviction, Valor, Thematic, 4Change and OPAL, leveraging our long-term expertise in active management with conviction as well as in delegated management. Based in Paris and established in 9 European countries, we manage more than 34billion euros and employ nearly 170 people.

More information at: www.am.eu.rothschildandco.com

France

29, Avenue de Messine
75008 Paris
+33 1 40 74 40 74

Belgium – Netherlands – Luxembourg

Rue de la Régence 52
1000 Bruxelles
+32 2 627 77 30

Switzerland

Rothschild & Co Bank AG
Rue de la Corraterie 6
1204 Genève
+41 22 818 59 00

Italy

Passaggio Centrale 3
20 123 Milano
+39 02 7244 31

Germany - Austria

Börsenstraße 2 - 4
Frankfurt am Main 60313
+49 69 299 8840

Spain

Paseo de la Castellana 40 bis
28046 Madrid
+39 02 7244 31

Visit our internet site

Follow us on LinkedIn