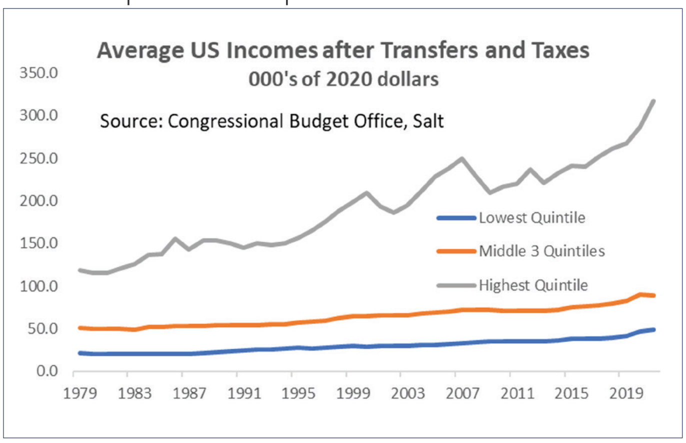
Trump 2.0:
Implications for our Structural Themes

As we expanded our product offering in 2021, there were several structural themes we identified that our new funds would have to navigate over the next 20-30 years. These included challenges to fiscal sustainability, likely higher inflation and neutral interest rates, likely lower growth, de-globalisation and rising Geo-political tensions, particularly between the United States and China. Donald Trump's return to the White House has significant implications for these themes.

It's the economy, stupid

In the lead up to the election and on election day itself, polls confirmed the economy was front of mind for many voters. A narrow interpretation of that concern suggested Advantage Harris: the economy has remained resilient through the tightening in monetary policy, inflation has moderated, and the unemployment rate has risen, though remains as historically low levels.

That interpretation missed the bigger point. The true meaning of "the economy" requires casting one's mind back to the reason Trump won in 2016. He won then in what was a bigger surprise than this latest victory because of a deep dissatisfaction from the bulk of Americans who feel that traditional politics have failed their needs, particularly in areas such as economic security (particularly jobs and incomes), immigration, and foreign policy. This is driven by the reality of only subdued growth in real after-tax incomes of low- and middle-income American's when compared with top income earners.



In 2016, many Americans saw Trump as a figure who was prepared to challenge the liberal orthodoxy they believed has failed to serve their interests. His supporters therefore like that he is willing to question the long-standing alliances, economic strategies, and positions on globalisation that, in 2024, more than half of voting American's believe have not benefited American workers. His stance on issues like deregulation and trade resonates with those who believe that mainstream policies have contributed to the decline of American industries and jobs.

Hold onto your hats

Trump was a political novice in 2016. He seemed frustrated by his inability, even as President of the United States, to do what he wanted. He will be more prepared this time. The document "Project 2025" is, according to some, a blueprint for the implementation of his strategy. Trump has so far distanced himself from the document prepared by the ultra-conservative Heritage Foundation.

This time he will be better organised and is moving quickly to appoint his Cabinet. He will be in a strong position to implement his agenda given the Republicans will likely hold all three branches of Government – the White House, the Senate (looking like a 6-seat majority) and the House (looking like a 9-seat majority) of Representatives, at least up until Senate mid-terms in 2026. Expect Trump to seize on this opportunity. He also faces likely less internal Republican party resistance than in his first term.

The agenda

The President-elect campaigned on several key policy pillars. These include:

1. **Taxation:** Trump has indicated he would make his 2017 tax cuts, which are scheduled to expire next year, permanent. He has hinted at additional tax cuts for the middle-class but has not provided specific details. He intends to cut the corporate tax rate to 20% with 15% applying to domestic profits.
2. **Trade:** Trump has proposed a new "universal baseline tariff" of 10% on all imports to the United States. This would represent a significant increase from the current tariff levels on many products. Trump has specifically targeted China, indicating he would expand tariffs on Chinese goods to up to 60%. He argues that this would counteract what he sees as unfair trade practices, such as intellectual property theft, currency manipulation, and state subsidies for Chinese companies. He's also hinted at targeting other countries he believes engage in "unfair" trade practices, though specifics beyond China are less defined. Exactly how serious he is about the proposed tariff level remains to be seen.
3. **Immigration:** Trump's proposals focus on strict border control, reducing illegal immigration, and limiting certain types of legal immigration. He intends finishing his border wall, improving surveillance technology at the border and Trump has also suggested implementing large-scale deportations of undocumented immigrants.
4. **Deregulation:** Trump aims to reduce what he sees as bureaucratic overreach by cutting federal regulations, especially in areas impacting business and industry. He has promised to dismantle regulations he argues slow down economic growth and limit American energy production and manufacturing. He intends to scale back financial regulations, such as those on banks and investment firms, to encourage lending and investment.
5. **Climate change:** Trumps policy emphasises energy independence, deregulation, and a move away from climate-centric policies that he argues hinder economic growth. Unlike climate policies that prioritise emissions reductions, Trump's approach focuses on promoting fossil fuels, reducing government oversight, and fostering energy independence. He intends to keep the U.S. out of global climate commitments and instead focus on policies that prioritise American interests.

Implications

While Trump's 2024 policy proposals were undoubtedly designed to appeal to certain segments of the electorate, his unpredictable, transactional approach suggests that many of these ideas could remain unfulfilled. His propensity for abrupt pivots, reliance on populist support, and a history of incomplete policy follow-through (e.g. repeal of Obamacare) indicate that his ambitious agenda might not withstand the realities of governance, even with the tailwind of Republican majorities in both the House and Senate. So, while acknowledging the outcome may look very different from his current vision, this is how we see the current economic and market implications of his policy program.

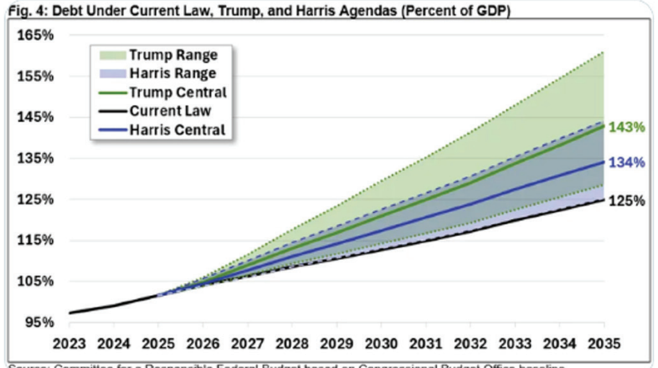
1. **US growth.** There are positives and negatives. Tax cuts and deregulation are positives for growth, tariffs are a negative. Tariffs, intended by Trump to protect domestic industries and promote re-shoring particularly of manufacturing industries always backfire by increasing consumer prices and limiting choices. They often provoke retaliatory measures, hurting exporters and straining international relations. Moreover, tariffs can stifle innovation and efficiency within protected industries, leading to long-term economic stagnation rather than fostering sustainable growth. A report* from the Peterson Institute for International Economics (PIIE) found that assuming the tariffs are fully implemented and passed on to US buyers, the combination of new Trump tariff proposals will generate consumer costs of at least 1.8% of GDP, not considering further damage from foreign retaliation and lost competitiveness. This calculation implies that the costs from Trump's proposed new tariffs will be nearly five times those caused by the Trump tariff shocks through late 2019, generating additional costs to consumers from this channel alone of about $500 billion per year. Tax cuts and deregulation will help the supply side of the US economy, assuming they lead to greater investment and productivity, however tariffs will be negative for competition and productivity. Immigration restrictions will also be bad for potential growth. Depending on the sequencing of his policy changes, there may be

some initial positives for US growth if deregulation and tax cuts come early, but tariffs are a medium to longer term negative.

2. **Immigration and the US labour market:** Immigration has been a significant benefit to the US economy over time, adding to potential growth and especially in times of labour shortages. Recent growth in labour supply explains how resiliency in the labour market has been able to endure while at the same time, wage growth has been moderating, albeit only gradually. Trump's agenda to significantly restrict immigration and potentially deport millions of workers, while no doubt be appealing to some voters, will have serious negative implication for the US labour market, wage growth and inflation.

3. **US fiscal (un)sustainability:** Any positive take on tax cuts ignores the longer-term issue of fiscal sustainability. Latest fiscal data for the September 2024 Fiscal Year showed a deficit of $1.8 trillion (-6.4% of GDP), the third highest on record after the Covid-fuelled deficits of 2020 and 2021. This result comes at a time when the economy is growing strongly, and the unemployment rate is still low. Looking ahead, the Congressional Budget Office expects deficits to continue to rise, hitting $2.8 trillion by 2034 and for debt to rise from its current level near 100% of GDP to 122% over the same period. But that's on a "no policy change" basis which assumes the 2017 tax cuts expire next year. The Committee for a Responsible Federal Budget estimates that a full implementation of President-elect Trump's fiscal agenda would see the debt to GDP ratio rise to 143% of GDP by fiscal 2035. Trump is proposing to appoint Elon Musk to a role charged with finding places to cut government spending. However, once you account for big-ticket areas that are unlikely or unable to be cut such as Medicare, Medicaid, Social Security, Defence and interest payments, there isn't much left to trim.

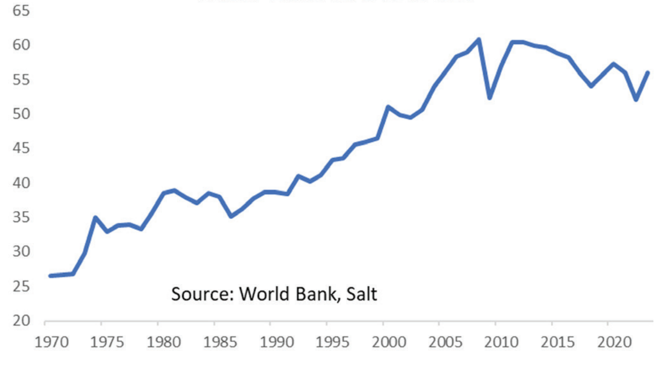
Fig. 4: Debt Under Current Law, Trump, and Harris Agendas (Percent of GDP)



Source: Committee for a Responsible Federal Budget based on Congressional Budget Office baseline.

4. **Globalisation and Geo-politics:** In recent years, global trade has held up better than we expected. Rather than going backwards, global trade as a percentage of global GDP has stabilised, however if Trump imposes his tariffs as proposed, a downward trajectory will undoubtedly emerge. This will be a negative for global growth and see the demise of globalisation as a significant contributor to the closing up of inequality between countries. As we highlighted in 2016, Trump's "Make America Great Again" leads us to a more fragmented and regionalised world economy. Trump has an unhealthy disregard for global institutions. Withdrawal from international climate agreements could affect global efforts to address climate change, with economic implications for industries related to renewable energy and carbon-intensive sectors. His policies would encourage economic nationalism and disrupt established political (NATO) and trade relationships. While this might strengthen some domestic industries, it risks inflating consumer prices and encouraging other nations to adopt similarly "tit-for-tat" protectionist policies. Ultimately, Trump's approach could reshape globalisation into a less interconnected, more competitive, and more unpredictable system where economic alliances are fluid and driven by national interests over collective global interests. A more isolated, fortress America approach will also require countries to take greater responsibility for their own security interests via higher Defence budgets, adding to existing fiscal pressures.

World Trade as a % of GDP

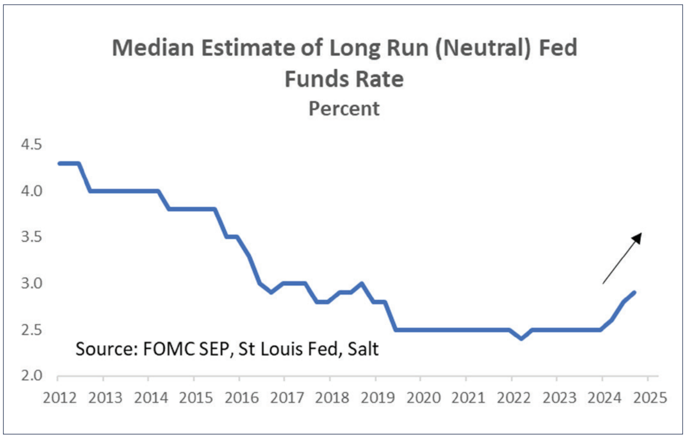


5. **US Inflation:** Trump's policy agenda is unambiguously inflationary. Higher tariffs would almost certainly be passed on in full to the end consumer – as a business, why wouldn't you when the higher costs are a result of government policy? Rebuilding supply chains will also inevitably lead to higher business costs and consumer prices. The labour market will be tighter and wage pressure higher as lower immigration bites, and fiscal policy will be easier, putting extra demand pressure on the economy.

6. **Neutral Interest rates and monetary policy:** Trump's victory plays into our expectation of higher neutral monetary policy rates in the period ahead. Deglobalisation, easier fiscal policy, higher public debt, rising geo-political tensions leading to greater global fragmentation all point to higher neutral rates, and therefore less scope for central banks to ease monetary

1. *Why Trump's Tariff Proposals Would Harm Working Americans, Kimberly A. Clausing and Mary E. Lovely, PIIE, May 2024

policy in the period ahead. An added concern for markets is Trump's threat to reduce the independence of the Federal Reserve.



7. **New Zealand:** As a small, open exporting country, our economic aspirations are best met in a rules-based trading environment. Looking ahead, the global environment seems likely to be less conducive to us meeting our goals. That is especially the case if tensions are ramped up between the US and China, as our security interests align with the west, while our trade aspirations align in the east. The influence of multi-lateral global agencies such as the World Trade Organisation and the International Monetary Fund seems likely to reduce, so we must forge our own path in either bilateral or regional alliances (CPTTP, RCEP). The recent trade agreement with the Gulf Co-operation Council (Saudi Arabia, United Arab Emirates, Qatar, Kuwait, Oman and Bahrain) is a welcome development. But these agreements are never easy. This one took 18 years, stalled for a long period of time over our decision to halt live sheep exports. It is likely we will have to take greater responsibility for our own security interest, putting further pressure on fiscal spending. With respect to interest rates, we have long argued that global, and therefore New Zealand, interest rates would be higher in the future. A second Trump term seems likely to double-down on that risk.

8. **Bond and Equity markets:** Higher inflation and higher US debt and bond issuance means higher bond yields globally. US 10-year Treasury yields have already reacted negatively to Trump's re-election, rising around 80bp from a pre-election low of 3.6% to 4.4% currently. The implication for equities is more ambiguous and will come down to exactly how much of his promises get kept (e.g. tariffs) and the sequencing of his other proposals including deregulation and tax cuts. The knee-jerk positive reaction to the election outcome appears to be assuming the growth enhancing policies come first, or that Trump won't enact the most growth-detracting elements of his agenda. And remember, higher bond yields over time will be a negative for equities. Finally, the prospect of lower growth and higher inflation ahead supports the case for an allocation to real assets (global listed property and infrastructure) in portfolios.

2028

In 2016, Trump clearly wasn't a Democrat, but neither was he really a Republican. He was probably best described as an independent who managed to secure the Republican nomination. In 2024, there appears less dissent within the Republican Party to his victory. Perhaps that's because his second term reflects an inability of the political elite/ liberal orthodoxy, either Democrat of Republican, to present a compelling alternative vision or believable plan for greater prosperity amongst low- and middle-income America. Fast-forward to 2028 and it's hard to see the Republicans selecting anybody other than another authoritarian, anti-China nationalist candidate for the Presidency. The bigger question is how the Democrats will respond.