

# Heightened uncertainty following US elections

Atradius Economic Research – November 2016

## Summary

- While the policy agenda of a Trump presidency remains unclear, two of his pledges could have significant ramifications for global trade and GDP growth: protectionism and fiscal stimulus.
- The US economy could see a short-term boost to growth through the fiscal stimulus, but in the longer term would suffer from lower international trade.
- Pressure is already felt in EMEs due to capital outflows and tightening financing conditions. This is likely to continue as protectionist measures in the US could weigh on their medium term growth outlooks.

### Trump policies to have global effects

The election of Donald Trump as President of the United States has introduced a large source of uncertainty for the global outlook. Not only did his victory come as a surprise, but his policy platform is also largely unknown. With many grand, and often conflicting, promises made on the campaign trail, it is unclear how exactly US policy will look.

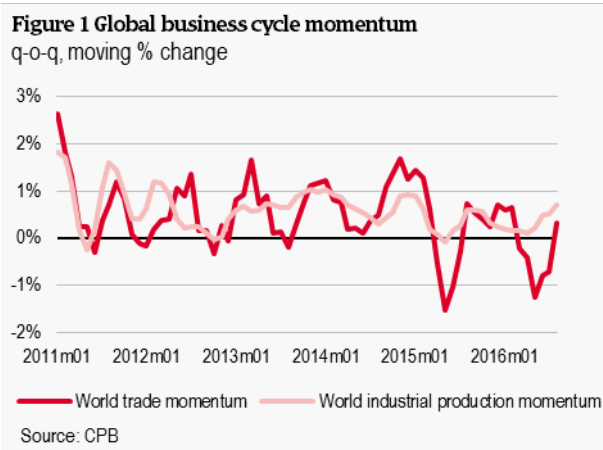
On the economic side, there are two major points that appear certain though on the Trump agenda that will have global implications: (1) protectionist trade policy and (2) expansionary fiscal policy. Even more importantly, these policies are politically feasible for the future president. Mr Trump will have more flexibility in negotiating trade policy but less reach in setting fiscal policy, needing to garner support from fiscal hawks in Congress.

### Another blow to the international trade outlook

Trump's election means further slowing of international trade growth. Negotiations to move forward with trade liberalisation measures – most notably TTIP between the

EU and US and TPP between the US and 11 other Pacific countries – are all but off the table now. There are also calls to go back on current trade arrangements – most notably NAFTA and relations with China. President-elect Trump for instance has taken consistent positions on renegotiating or withdrawing from NAFTA as well as introducing tariffs on Mexican and Chinese goods imports (up to 35% and 45% respectively). We do not expect these to be implemented to the full extent though, largely due to the disruption it would cause to global supply chain networks.

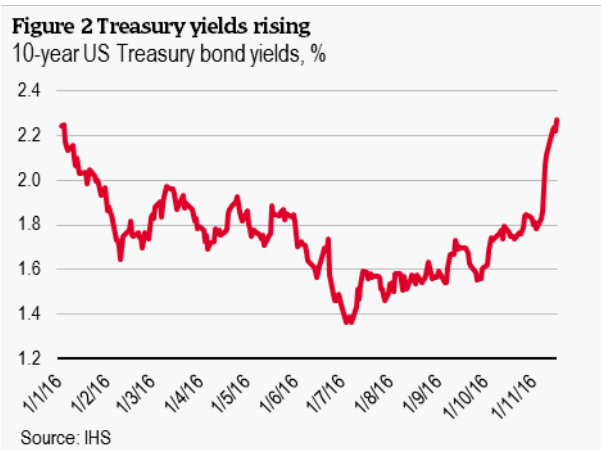
Underlying trade indicators show trade momentum improving in both advanced and emerging markets and export orders rising since May. This offers some confidence that trade growth could pick up in 2017, but we see the Trump presidency, alongside Brexit and trends in Europe, as an effective lid on growth, and potentially worse. The extent to which can be better predicted in coming months as his trade policy comes to light.



### High demand for a fiscal stimulus

Trump is consistently committed to increasing infrastructure investment and cutting taxes, totaling 3% of GDP in 2017 and 2018 (conservative estimate by ABN AMRO). While there will be some resistance from fiscal hawks in the Congress, large-scale spending on infrastructure is most likely due to strong bipartisan and popular support.

Fiscal stimulus in the current upswing of the US business cycle would boost economic growth and cause inflation to pick up more rapidly than previously expected. Higher inflation suggests the Federal Reserve will raise interest rates more quickly. Higher growth and inflation expectations have also put more upward pressure on the dollar, which affects the already weak exports. It is also driving up bond yields. As of 18 November, 10-year Treasury yields are 2.27%, 0.45 bps higher than the eve of the election.



### Short-term boost for US, but medium-term uncertainty

The potential implications of the Trump presidency on the US are mixed. US GDP will likely be boosted in 2017 and 2018 by large fiscal stimulus. USD appreciation and potentially protectionist policies will increasingly weigh on exports though, putting downward pressure on medium-term growth. In addition, foreign demand for US exports will be depressed by more restrictive financing.

Fiscal stimulus would decrease unemployment through higher economic growth, which would further tighten labour market and increase wage growth. Restrictions on

both legal and illegal immigration though would decrease the labour supply which would also contribute to lower unemployment. Protectionist policies could also put further upward pressure on inflation as imports become more expensive. Higher wages and inflation may accelerate the rate hikes, thus triggering second round effects.

### Consequences for NAFTA countries could be very negative

Mexico is highly vulnerable to economic developments in the US with 81.2% of exports going to the US. Trump's indication of tariffs on Mexican imports especially targets the maquiladoras, the factories in Mexico dedicated to producing cheaper goods aimed at the US market. The peso has thus far acted as a shock absorber depreciating 15% so far in the aftermath of the election (23% YTD). Interest rates have been hiked to counter inflation stemming from peso depreciation and overall tighter financing conditions will weigh on the GDP growth outlook.

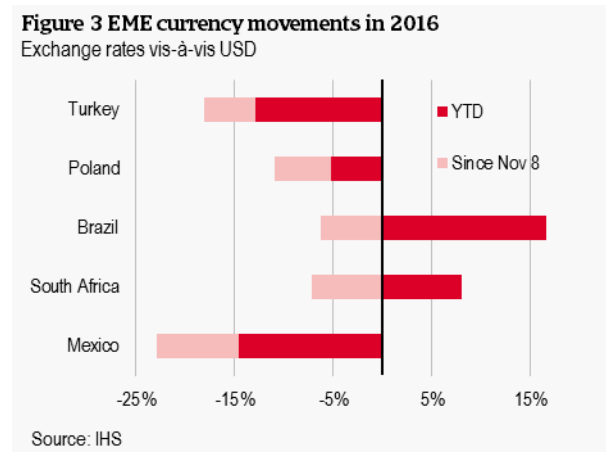
Canada also sends more than 75% of its exports to the US and a renegotiation of NAFTA puts this at risk. The country's oil sector could benefit though from projects like the Keystone XL pipeline, favoured by Trump, which would connect Alberta crude oil to refineries in the US.

### Most EMEs stand to lose, but potential opportunities for commodity exporters

At this point, the outlook for emerging markets is less nuanced than for the US – the impacts of Trump's likely policy stance are largely negative. The main channels through which Trump's presidency will harm EMEs is as described above: trade, finance and commodities.

Countries with close trade ties to the US will most likely see lower import demand in the US which will weigh on growth in their markets.

The countries most exposed to the Trump effect are those with the highest external vulnerabilities. An overview of selected EMEs' vulnerability is presented in the Table 1. Turkey, South Africa and Argentina are among the most vulnerable countries. This is due to their high external financing needs, dependency on volatile portfolio flows, low external and financial buffers and high external debt.



**Table 1 External vulnerabilities of EMEs**

Vulnerability	Country	Stock of inward portfolio investments (% reserves)	Gross external financing needs (% reserves)	Doubts about effectiveness of monetary policy
<b>High</b>	Turkey	138	166	Yes
	South Africa	366	99	Yes
	Argentina	147	151	Falling
<b>Moderate</b>	Indonesia	174	102	No
	Mexico	266	81	No
	Brazil	112	39	Falling
<b>Low</b>	Russia	42	15	Yes
	India	66	43	No
	Thailand	67	30	No

Sources: EIU, IMF, Atradius Economic Research

Higher yields on US treasuries and the stronger USD cause capital to move away from EMEs. As has been seen in many EMEs since the election, their currencies have depreciated relative to the USD (note the declines in Turkey, South Africa, Mexico exchange rates in Figure 3).

Currency depreciation increases financing risks for corporates and governments in EMEs with unhedged FX debt as its local value rises. Currency depreciation also puts upward pressure on inflation, driving EME central banks to tighten monetary conditions further. This will weigh negatively on their GDP growth outlooks.

Depending on which commodity a market depends on, it could have large impacts on EMEs. Trump-supported deregulation in the oil and gas sector, as well as the easing of environmental restrictions, could increase the supply of oil ensuring a slower price recovery. Oil exporters then would continue to face challenges in generating government and export revenues. Other commodity exporters may benefit since large-scale infrastructure projects in the US would increase demand, and thus raise prices, for some construction inputs like iron and cement.

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