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How a Trump Presidency May Impact Australia

The recent US presidential election has given a clear mandate for Donald Trump to be the next President, and the Republican party have already gained enough seats for a majority in the Senate and the House of Representatives. The control of both chambers of the US Congress has improved the prospects that they can deliver their policy agenda, including tighter border security, tax and spending cuts, and deregulation. How might these policies affect Australian investors over the next 4 years?

In the immediate aftermath of the election outcome, markets reacted with higher Treasury bond yields as traders scaled back expectations for substantial Federal Reserve rate cuts over the coming year, equities continued their rise, and the US dollar strengthened. These moves were already evident in the lead up to the election in what was termed the “Trump Trade”, as markets started to price in the increasing probability of a Republican victory in the last weeks of the campaign.

In essence, bond yields moved higher as the prospect of lower taxes, spending cuts and tariffs on imports are all seen as inflationary, while equities moved higher as less regulation is seen as benefitting the stock market. However, these sudden moves should be seen in the light of comments from Jerome Powell, the Chair of the Federal Reserve, who said in a press conference following the Fed meeting the day after the election: “In the near term the election will have no effects on our policy decisions. We don’t guess, speculate and we don’t assume what future government policy choices will be”.

It is important to keep this in mind when considering what impact Trump’s policies may have on Australian investors. We note that politicians of all colors (including our own) make a lot of promises in an election campaign, but not all promises turn to reality.

Having said that, most Australian economists are forecasting that any increase in tariffs is likely to put pressure on Australia's economy through China, while tax cuts and reduced immigration will support larger US budget deficits that could stoke US inflation, which in turn may curb global economic growth.

Any trade war that is triggered by proposed tariff increases would push up the price of goods around the world. In particular, if imports from China were hit with a 60 per cent tariff and duties of 10 to 20 per cent on other countries this would put pressure on the Reserve Bank of Australia to deliver further interest rate rises.

US tariffs of 60 per cent on Chinese goods would slow the Chinese economy and reduce demand for Australian iron ore that is used to make steel to construct buildings, bridges and other infrastructure. In this case, the price of mining exports, particularly iron ore, would fall as the Chinese economy slows even further.

However, this is a worst case scenario and Trump's proposals may not come to pass. Even if such a high tariff was introduced, the RBA has said it was possible China could unleash further spending stimulus to offset any hit to growth, so the overall impact on Australia's exports from a trade war would be uncertain.

In terms of any direct affect that tariffs on Australian goods would have, the United States is only Australia's fifth-largest destination for goods exports and is just 4 per cent of total exports. Australia's major trading partners are China (37 per cent of total), Japan (15 per cent), and South Korea (7 per cent). Australia's biggest exports to the US last financial year were beef, gold and pharmaceutical products.

The Trump Presidency introduces other uncertainties for business, investors and governments, including on climate change policy and global trade. He has vowed to again withdraw the US from the United Nations Paris Agreement on climate change and back fossil fuels. If the Trump Administration does implement the tariffs, there is no doubt that will be disruptive to global trading patterns – and some of our commodities and manufactured goods and services may be impacted.

While the change of Administration in the US will bring some uncertainty to financial markets, it is important to realize that the economy is not the stock market – while some of the suggested policies will have economic consequences it is not clear how that translates into stock market performance. What we do know is that the stock market has been positive in every 4 year Presidential period – a reminder that the best course of action is always to stay discipled in a diversified portfolio that has been designed to meet your goals.

Dr Steve Garth
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