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Economic Overview for Business Owners

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Globalisation Outplayed?

Taking Donald Trump's stated economic policy preferences at face value it appears as though his election as President of the USA holds significant implications for businesses and households around the globe.

The US has numerous checks and balances in its legislative system and ground-breaking changes to legislation typically take a long time to implement. Moreover, there may be division within the Republican Party on economic policy. That said, we should not ignore the fact that the Republicans gained a majority in both Chambers of Congress. That should make it easier to pass legislation.

Amongst his numerous proposals, those relating to US government finance and US trade policy stand out as potentially having the biggest impact, not only in the US, but also around the world.

Firstly, on US fiscal policy, Trump favours fiscal expansion primarily through tax cuts (including for businesses), which would leave the US with a larger budget deficit and a higher level of debt. In addition, increased spending on infrastructure seems likely, although expenditure elsewhere is likely to be cut. All else remaining equal, commodity prices and, hence, the currencies and purchasing power of commodity producers, including South Africa, should benefit from this.

However, the problem is that a larger US fiscal deficit, against the backdrop of an unemployment rate near historic lows and a decent recovery in credit extension in real terms, is likely to tilt the US Federal Reserve into a more hawkish stance. This could end in a more aggressive interest rate hiking cycle in the US than what has been expected , which could support the US$, while likely placing downward pressure on currencies and upward pressure on interest rates in emerging market (EM) countries, especially those running macroeconomic imbalances (including South Africa).

Admittedly, it is difficult to disentangle the nett effect of these opposing developments.

And, secondly, from a longer term, "structural" perspective, the new president's stance on trade is of key importance. In essence, it appears as though the era of globalisation, led by freer trade and less restrictive movement of people will lose considerable momentum. It may even reverse course.

One fears this could have far-reaching consequences. There are no specific action plans evident as yet. But one surmises the abandonment of the Trans-Pacific Partnership or TPP (a trade agreement between a number of countries from the Pacific Rim and the United States) seems like a possibility, while withdrawal from the proposed Trans-Atlantic Trade and Investment Partnership (TIPP) between the US and the European Union may also be considered. The North American Free Trade Agreement (NAFTA) between the USA, Canada and Mexico could also come under review from the new administration.

None of this precludes the US from signing bilateral trade deals. Also, the specific actions and details of possible changes to these trade agreements are not predictable. But as a general conclusion the nett result seems likely to be the curtailment or even withdrawal of US involvement in the drive for freer trade.

Such an outcome would not reflect a unique policy stance on behalf of the US. Indeed, global trade liberalisation has already lost considerable momentum in recent years, given the pressures created by job losses in specific countries and industries, and downward pressure on real wages. These

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unwanted economic outcomes are often viewed as a direct consequence of the removal of trade barriers.

At least part of the blame must be apportioned to the inadequate social safety nets and re-skilling programmes available to affected workers. But no matter what, anti-trade sentiment is rapidly gaining momentum. The likely impact of this anti-globalisation trend, also in the US, is somewhat clearer than for US fiscal expansion. Ultimately, to the extent one believes globalisation promotes competition, underpins productivity growth and constrains inflation, stalling (or even unwinding) free trade is likely to have the opposite effect across the world's economies. In the end, one eventually has a relatively worse trade-off between real GDP growth and inflation than would have been the case.

Finally, there is the question of the free movement of people, with a Trump administration likely to implement greater control over immigration. The consequence of this is long term in nature, as growth is a function of demographics and productivity growth. In time, it is likely that an anti-immigration stance would curtail US labour force growth and overall GDP growth, since it is not easy to maintain growth through constant productivity gains – especially if one of the building blocks of enhanced productivity, namely trade liberalisation, is curtailed!

Sadly, apart from a possible boost to commodity prices if US infrastructure spending is ramped up, again all else being equal, it is difficult to find any obvious good news in any of this for emerging market economies, including South Africa.

Written by Arthur Kamp, Investment Economist, Sanlam Investment Management