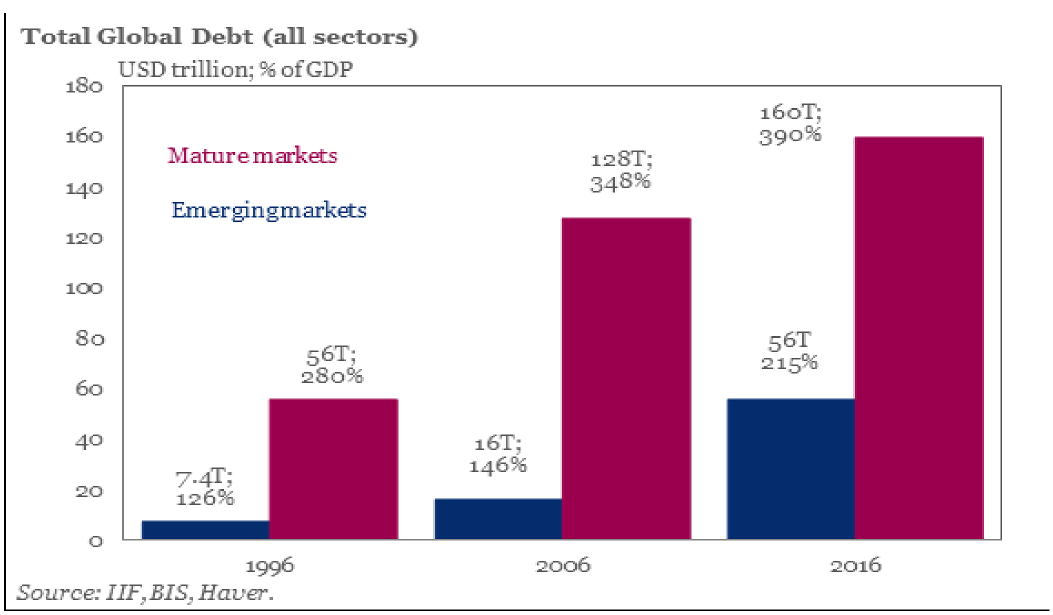
GETAnalysis.ca

The Economic Dangers Of Trump Hype

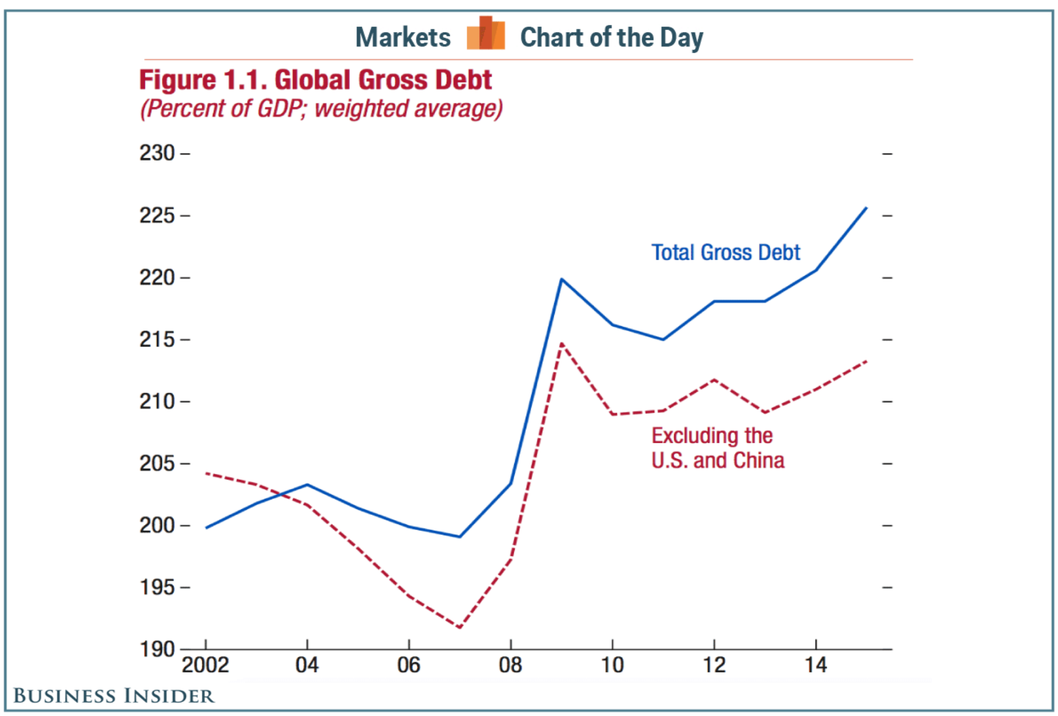
About 9 years ago, after the greatest financial-economic crisis of modern times in late 2008, the Federal Reserve (*the Fed*) led the major Central Banks of the World in an unprecedented rescue effort of the global financial system. They flooded the system with liquidity through extraordinary measures called 'Quantitative Easing' (*printing money and purchasing Bonds to flood the financial system with cash*), and by dropping interest rates to unprecedented historic low levels of near zero to negative rates. By taking these extraordinary steps, they, the Fed, and the other major Central Banks, collectively, saved the global financial system from total collapse, and thus the global economy from complete chaos. The price of this rescue effort? A sharp and significant rise in Global Debt.



Almost nine years later, the ensuing ‘recovery’, bought so expensively, is still not robust enough for the Central Banks to be able to withdraw their ongoing support, which they continue to provide through aggressive ‘Asset Purchase’ programs, and ultra-low to negative interest rates.

The Bank of Japan is the most aggressive Central Bank, with an ever increasing role in its financial markets to the point of becoming the financial market itself as it dominates asset buying function by crowding private players out. It’s increasingly dominant role is due to the unresponsiveness of the Japanese economy that has been in the doldrums for almost three decades, in spite of extreme stimulative efforts by successive Japanese Governments, and by the increasingly desperate Bank of Japan. The European Central Bank and China’s Central Bank are also providing close and aggressive support to their financial markets and their economies, in an effort to keep everything from sinking into negative territory. And the U.S. Federal Reserve is close behind, for though it keeps talking ‘normalization’ of interest rates and the unwinding of its bloated balance sheet, till now, except for token movements it has not been able to fully act on its intent.

As a result of the ongoing extraordinary and direct support of their asset markets, and their economies in general, the negative side of their actions, the extraordinary dependence of all systems, public and private sector, on the constant monetary support and ultra low to negative interest rates, and the unprecedented and rising levels of global debt that are required to keep it all going, pose an ever present danger to the ever shaky recovery, and the long term stability of the global economic order. Like some of the major financial and real estate markets, global debt is at an all time high, but no one wants to own that dubious milestone.



This unusual global banking and economic trajectory has been set since the near-collapse of the financial, economic systems at the end of 2008, to the present seemingly robust record setting asset price highs, with an ever present core-weakness that requires ongoing stimulus and endless support. The ‘Obama Rally’ (2009 – 2017) is still going under Trump, who consistently criticized it when campaigning, but now boasts about it.

The Economic Dangers Of Trump Hype

WRITTEN BY: ASHOK DHILLON

Trump came to power touting his ability to boost economic growth through a strange combination of 'Protectionism', the busting of 'International Trade Agreements', 'Deregulation', 'Tax Reform', a 'Trillion dollar Infrastructure Spend', and 'Repatriation of Offshore Jobs' and 'the over $2 Trillion of Capital sitting in Tax Havens' in the accounts of American companies. And just so nobody mistakes him to be a do-gooder, Trump has made sure that all regulations assuring the protection of the average consumer and the environment are also stripped away, so that his economic recovery can have the traditional telltale signs of old fashioned rape and pillage and none of the modern progressive ideas of win-win, but the good old win-lose. Towards those goals he has made tremendous progress, but unfortunately for him the losses are piling up on his side of the ledger, so far, and the wins have been very few.

The keen anticipation of his 'agenda' has of late helped inflate the asset markets beyond the Fed's stated goals of asset price inflation. But the record-setting performance of the financial markets do not necessarily reflect the dangers of perpetual monetary stimulus, ultra low interest rates, the Central Bank's asset purchases, or the reality of the underlying economic fundamentals. And therefore, they are a poor indicator of the current global economic health, which is touted as good but in reality is very fragile, as it is still entirely dependent on Central Bank's support, which dare not be withdrawn with any certainty, or in any specified time frame.

In any case, the logic and merits of Trump's so called economic agenda is questionable to begin with. In this day and age to assume that America can grow robustly, on its own, or by looking for one-sided wins only, is to be naive at best and ignorant at worst.

Protectionism doesn't grow economies, as has been proven time and again in history, and more recently with the liberalization of the 'Central Control & Command Economies' of Russia, China and India. As long as and to the degree these economies were shuttered, they were moribund and stagnant. When in the early nineties, the governments of these countries opened up their economies to the outside World, and to freer trade and foreign investment, their economies grew robustly, setting a pace of growth they hadn't experienced for decades. To the degree they have kept them open they continue to grow strongly, but to the degree they regressed, as with Putin's Russia, and the erratic go-no-go policies of India in the past two decades, their growth rates have reflected the interruption in trade and investment, through lower growth rates.

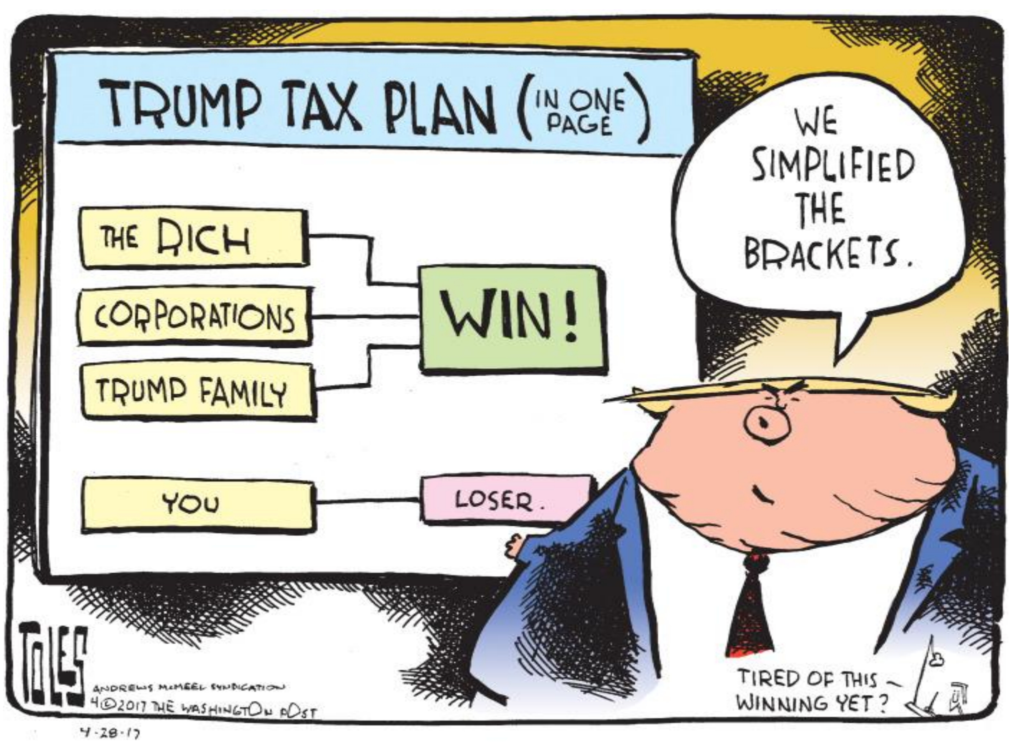
As Trump threatens NAFTA, the new TPP, and other International Trade Agreements to which the U.S. was party, the American economy will be affected negatively.

The growth rates of the past months are in general still reflective of the policies of the previous Administration, the Fed’s continued monetary and low interest rates support, and the ‘recovery’ of global economies from the years of stimulus, and not because of Trump’s past nine months of erratic policies which are to still take shape, and take root. If his protectionist tendencies were to be fully implemented, IF, the U.S. economy will reflect those policies negatively. The warnings of the U.S. Chambers of Commerce to Trump not to mess with NAFTA are a case in point.

The mass of deregulation that Trump has inked through his Executive Orders have had some beneficial effects, even if they have been primarily because of the positive feelings they have generated in the business community, rather than real effect in practice as they are too recent. But, overall America responds well to deregulation, in spite of the heightened risks, as do most economies. Overall the effect of the recent deregulation spree is too early to judge, and even though the environment and the consumers need greater protection from the inevitable abuses that are sure to follow, the economic sentiment is perhaps positively impacted by the idea of deregulation in the American business community.

The one Trillion dollar infrastructure rebuild plan is still an idea whose time, seemingly, hasn’t come, as it is not even being discussed currently.

Trump’s Tax Reform is another matter altogether. There are two great flaws in the current version of the ‘Tax Plan’. One is that this Tax Plan will overwhelmingly favor the minority rich rather than the majority working class, and therefore will have limited impact on growing the economy. Two, the Tax Plan is not revenue neutral, but purports to shave over $2 Trillion from the current Revenues, and, is going to depend on future economic growth to make up the deficit. That assumption of future growth paying for the significant shortfall in revenue is pure and simple, fool’s gold, and just asking for serious trouble down the road.



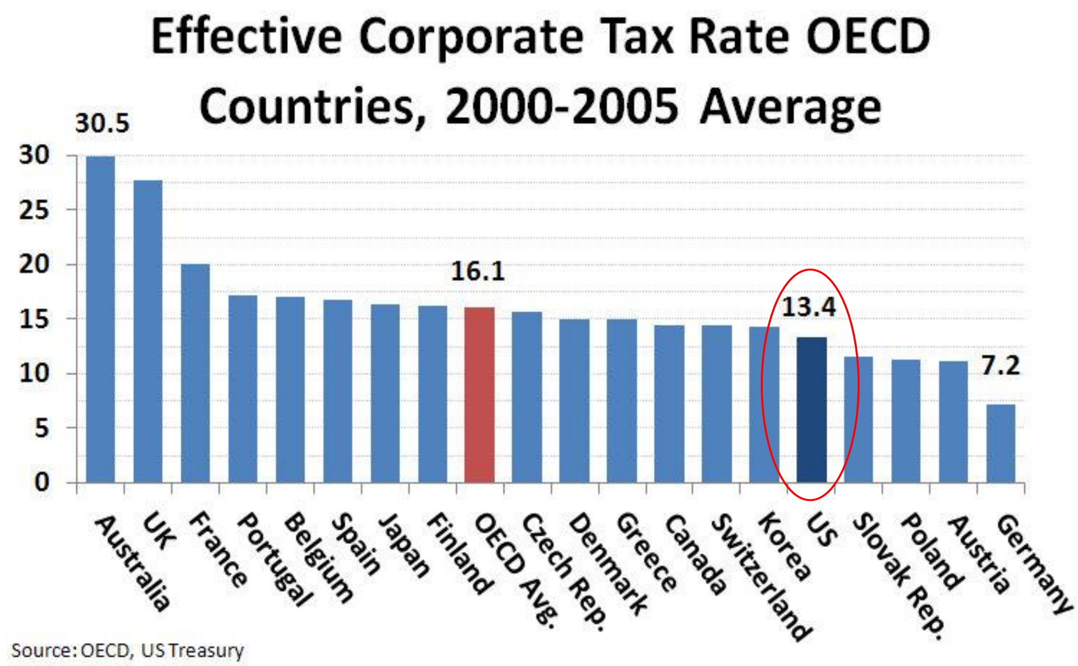
The Economic Dangers Of Trump Hype

WRITTEN BY: ASHOK DHILLON

Apart from the fact that the economic 'Recovery' is a bit long in the tooth and overdue for a contraction (*recession*), but even if the Fed and the Central Banks manage to stave off that natural cycle semi-permanently, any black swan event could send the entire structure off the rails, and the projected growth rates required to make up the shortfall, out-the-window. That would leave a huge gaping hole in revenues and put the entire economy at risk by sharply boosting deficits, and the cost of that debt. A sharp reversal in the American economy would then impact the other major economies, and that could spiral into another global recession.

Additionally, any major reversal in any of the other large economies, like China's, or a European economy for instance, could throw the American economy badly off. Either way, Trump Administration's Tax Plan is highly dangerous as it depends on future growth rates for its revenues, against which the odds are 'bigly' stacked.

The other problem with Trump's Tax Plan is that it rests on a lie that corporate America is not competitively positioned globally, corporate tax-wise. That simply isn't true. After all the deductions and the loopholes available to American businesses, the effective tax rate is substantially lower than the given statutory rate.



The Chart above is a bit outdated but proves the point.

Therefore the idea that somehow making the U.S. more tax competitive is going to bring jobs and Capital flooding back is naïve and misleading. Some jobs and capital might come back, but it won't be because of greater competitiveness of the tax rate. It will be for other more mundane business reasons, such as costs.

Where the U.S. and other developed countries are not competitive, is in hourly wages, when it comes to the average manufacturing and services jobs as the developing countries have unlimited supply of cheap human capital when it comes to unskilled or semi-skilled workers, and they always will.

And zero taxes in the offshore tax havens still beat the heck out of 15% -20% onshore tax rate, plus they give the Corporations a degree of privacy and unaccountability that is not available on the mainland. The $2 Trillion plus, sitting offshore, pays little to NO taxes, and is free to be deployed without the pesky scrutiny of the various authorities. Therefore it will probably stay offshore.

WRITTEN BY: ASHOK DHILLON

What might bring some jobs back to America is technology, like automation, the ease and prices of raw commodities, and proximity to the main markets for the manufactured products. So we doubt the Trump Tax-Plan will bring jobs or capital back, sound business reasons such as overall costs and proximity to prime markets might.

The stock markets that are flying high may be in for a shock if the Tax-Plan doesn't work, or before that, if it doesn't even achieve consensus within the fractured Republican Party, or break the united opposition of the Democratic Party to it, and therefore never really see the light of day.

If Trump's much anticipated economic stimulus policies don't work, but his destructive tendencies to break America's agreements, be they in Trade, or Defense, or in Climate Change, incur push-backs from its prime trading partners, its long-standing allies such as NATO, or the majority of the World as with the Climate Change Agreement known as the 'Paris Accord', then he will isolate America, and standing alone America cannot prosper no matter how strong it may seem to Trump and his fellow Nationalists. Plus Trump has taken on the international saber rattling role with relish, especially where North Korea, Iran, and to a lesser degree China are concerned. These hot spots could possibly explode into real conflicts under Trump's loud and constant prodding, and that would certainly change the fundamental economic equation, especially between China and the U.S., two of the World's largest economies. In our view, Trump's ability to carry out his agenda and stimulate the economy is limited, but his ability to damage and de-rail the economy is acute.