Big market swings after Trump's election

Nick Beams
10 November 2016

Global markets swung wildly yesterday as it became clear that Donald Trump was going to be the next US president. After the futures markets had shown the Dow Jones index could drop more than 500 points when trading opened yesterday, it finished up 257 points for the day, a rise of 1.4 percent.

The day’s trading in the US was preceded by sharp movements in American and global markets, pointing to the economic and financial instability that will accompany a Trump presidency, notwithstanding the initial market boost.

At the end of trading on Wall Street on Tuesday, election day, markets were up, continuing the rise that had begun, following a nine-day losing streak—the longest in 36 years—on the prospect of a Hillary Clinton victory.

But as the election count began and the prospect of Trump victory became more likely, markets in Asia plunged. The Japanese Nikkei index was down more than 5 percent for the day, Hong Kong fell more than 2 percent, and the Australian stock market dropped by nearly by 2 percent.

As more states went to Trump, the futures market for US stocks fell sharply. At one point, S&P futures were down by 5 percent, triggering electronic trading curbs.

However, during the count there was something of a reassessment. The conclusion was drawn, at least in the short term, that profit opportunities from Trump’s policies outweighed prospects of uncertainty.

Market fears were further eased by a late-night conciliatory victory speech by Trump, in which he praised Clinton for her service, after calling for her to be locked up during the course of the campaign.

Markets received a boost yesterday with remarks from President Barack Obama promising a smooth transition to a Trump administration “because we are now all rooting for his success in uniting and leading the country.”

Several aspects of his policies won immediate support. Trump has pledged to reduce the corporate tax rate to 15 percent, from 35 percent, and cut taxes on the wealthy. As the chief economist of one investment fund put it, Trump had made a good start because “we have never seen a tax cut we don’t appreciate.”

According to the Tax Policy Center, the top 1 percent of income earners would receive an average tax cut of more than $214,000 in 2017 and the top 0.1 percent, a reduction of more than $1 million each.

Trump is also committed to reducing regulations on businesses, another avenue for increased profitability. The turnaround in immediate business sentiment was exemplified by the financial trader Carl Icahn, one of Trump’s supporters, who is reported to have made $1 billion worth of trades to lessen his hedging positions, that is, to bet on a rise in the market.

The shift was reflected first in Europe where the pan-European Stoxx 600 index finished up 1.5 percent for the day, in contrast to the earlier steep decline in Asian markets.

By the time Wall Street opened yesterday, the initial plunge on share markets was over and indexes moved up, finishing the day close to their record highs. The biggest increases were recorded in healthcare and financial stocks.

The former were lifted by the removal of the prospect of a tighter regulation under a Clinton administration. Bank stocks received a boost from the prospect of higher interest rates and less financial regulation. The president-elect has denounced the quantitative easing policies of the US Federal Reserve and accused Fed chair Janet Yellen of keeping interest rates artificially low in order to aid the Obama-Clinton camp. He has touted a rise in infrastructure spending to boost the US economy.

The prospect of higher interest rates was also reflected in significant moves in bond markets. At one point, the yield on US 10-year Treasury bonds fell to 1.71 percent as investors sought a safe haven. But then money was moved out of government debt and into the share market, leading to a sell-off of bonds and a jump in the yield to more than 2 percent, the first time it has reached such a level since January. (Bond prices and yields have an inverse relationship to each other.)

The shift was ignited in part by the view that Trump's promises of tax cuts and increased infrastructure spending would lift inflation and thereby bring about a fall in bond prices and a rise in interest rates. The gamble on increased infrastructure spending was also reflected in the share market, where the engineering and construction company Caterpillar saw a 6 percent rise in its stocks.

However, the elevation of bond yields and the prospect of rising inflation and interest rates do not point to a return to financial stability. In fact, the opposite may be the case. Such is the extent of the bond market bubble—the product of years of quantitative easing and the cheap-money policies of the Fed—that it has been calculated that a 1 percentage point rise in interest rates could bring losses of around $3.36 trillion for traders, who have been buying on the expectation that prices will go even higher.

There are many other areas of economic uncertainty and potential turbulence resulting from policies announced by Trump during the campaign, including to rip up trade deals he considers to be unfavourable to the US. The Obama administration's Trans-Pacific Partnership (TPP) deal, awaiting ratification by Congress, appears to be dead in the water. Whether this extends to a renegotiation of the North American Free Trade Agreement (NAFTA) remains to be seen.

Trump has said he would impose penalties on US companies deemed to be shifting factory jobs offshore and also designate China a currency manipulator. He has threatened to use presidential authority to impose tariffs on Chinese goods, possibly as high as 45 percent.

In his victory speech, Trump adopted a more conciliatory tone, saying that while "we will always put America's interests first, we will deal fairly with everyone" and seek "common ground not hostility."

With world trade expected to rise by only 1.7 percent this year, Trump's "America first" agenda is certain to increase global economic tensions as other powers respond with retaliatory measures. Moreover, his claim that his agenda of economic nationalism can revive the US economy, when it is completely integrated into and dependent on the world economy, is a reactionary utopia, the content of which will be revealed rapidly as the Trump presidency unfolds.